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Highlights of this Issue

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These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-1, page 5.

Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for January 1986.

EMPLOYMENT TAX

Notice 86-1, page 33.

Minimum distributions required for the 1985 calendar year need not be made until December 31, 1986, from qualified plans and individual retirement accounts and annuities (IRAs) pursuant to sections 401(a)(9), 408(a)(6), and 408(b)(3) of the Code, as amended by section 521 of the Tax Reform Act of 1984. An IRA with a current favorable opinion letter need not be amended to provide the distribution rules in section 408(a)(6) and (b)(3), as amended, until further notice.

ADMINISTRATIVE

Rev. Proc. 86-1, page 6.

Rulings; determination letters; closing agreements. Revised procedures are provided for issuing rulings, determination letters, and information letters, and for entering into closing agreements on specific issues. Rev. Proc. 85-1 superseded.

Rev. Proc. 86-2, page 19.

Technical advice to District Directors and Chiefs, Appeal Offices. Revised procedures are provided for furnishing technical advice to District Directors and Chiefs, Appeals Offices. Taxpayers' rights when such advice has been requested, are also set forth. Rev. Proc. 85-2 superseded.

Rev. Proc. 86-3, page 26.

Areas in which advance rulings will not be issued. A revised list sets forth those areas of the Code under the jurisdiction of the Associate Chief Counsel (Technical) in which the Service will not issue advance rulings or determination letters. Rev. Procs. 85-22, 85-24, 85-27, 85-28, 85-34 and 85-59 superseded.

Announcement 86-1, page 35.

Regulations imposing reporting requirements on charitable organizations that dispose of certain donated property within two years after the date of the contribution of the property will be modified.

A list of Announcements of Actions on Decisions of the Tax Court published in the Bulletin from January through December 1985 on page 4.
Cumulative Listing of Organizations Challenging Revocation of Status begins on page 35.
Finding List of Revenue Rulings, Revenues Procedures, Treasury Decisions, etc. published in the Bulletin from July through December 1985 begins on page 37.
Finding List of Previously Published Rulings currently mentioned in the Bulletin from July through December 1985 on page 39.
Index of Items published in the Bulletin from July through December 1985 begins on page 40.
Announcement of Voluntary Suspensions and Disbarments begins on page 49.

Department of the Treasury
Internal Revenue Service

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Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the Internal Revenue Bulletin as the source would be appropriate.

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Cumulative List of Announcement Relating Decisions of the Tax Court Published in the Internal Revenue Bulletin from January 1, 1985 thru December 31, 1985

It is the policy of the Internal Revenue Service to announce in the Internal Revenue Bulletin at the earliest practicable date the determination of the Commissioner to acquiesce or not acquiesce in a decision of the Tax Court which disallows a deficiency in tax determined by the Commissioner to be due.

Notice that the Commissioner has acquiesced or nonacquiesced in a decision of the Tax Court relates only to the issue or issues decided adversely to the Government.

Actions of acquiescences in adverse decisions shall be relied on by Revenue officers and others concerned as conclusions of the service only to the application of the law to the facts in the particular case. Caution should be exercised in extending the application of the decision to a similar case unless the facts and circumstances are substantially the same, and consideration should be given to the effect of new legislation, regulations, and rulings as well as subsequent court decisions and actions thereon.

Acquiescence in a decision means acceptance by the Service of the conclusion reached, and does not necessarily mean acceptance approval of any or all of the reasons assigned by the court for its conclusions.

No announcements are made in the Bulletin with respect to memorandum opinions of the tax court.

The announcements published in the weekly Internal Revenue Bulletins are consolidated semiannually and annually. The semiannual consolidation appears in the first Bulletin for July and in the Cumulative Bulletin for the first half of the year and the annual consolidation appears in the first bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner ACQUIESCES in the following decisions:

Taxpayer	Docket No.	Report Volume	Report Page
Cologne Life Reinsurance Co.[1]	10337-81	80	859
Cooper, Robert E.[2]	3164–75 6401–75	67	870
Gershman Family Foundation, Harold & Julia[3]	16385-84	83	217
Sibla, Richard R.[4]	2864-76	68	422

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[1] Acquiescence relating to whether the taxpayer is entitled to take into account the reserves held and the premiums received under its risk premium reinsurance contracts in computing the deduction under section 809(d)(5) of the Code.

[2] Nonacquiescence published in 1978-1 C.B. 2, relating to whether payments made by petitioner for meal expenses in connection with his employment as a fireman are deductible under section 162(a) of the Code or excludable under section 119(b)(3), is withdrawn and acquiescence is substituted therefore.

[3] Acquiescence relating to whether the petitioner, a disqualified person with respect to the private foundation, committed an act of self-dealing proscribed by section 4941(d)(1)(A) of the Code when he transferred to the foundation a promissory note subject to two senior notes secured by an all-inclusive deed of trust.

[4] Nonacquiescence published in 1978-1 C.B. 3, relating to whether payments made by petitioner for meal expenses in connection with his employment as a fireman are deductible under section 162(a) of the Code or excludable under section 119(b)(3), is withdrawn and acquiescence is substituted therefore.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates determined under the alternate method as provided by section 1.1274-6T of the Temporary Income Tax Regulations are set forth for the month of January 1986. See Rev. Rul. 86-1, this page.

Section 483.—Interest on Certain Deferred Payments

Federal short-term, mid-term and long-term rates determined under the alternate method as provided by section 1.1274-6T of the Temporary Income Tax Regulations are set forth for the month of January 1986. See Rev. Rul. 86-1, this page.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 280G, 467, 468, 483, 7872.)

Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for January 1986.

Rev. Rul. 86-1

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of January 1986 are as follows:

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term				
AFR	8.32%	8.15%	8.07%	8.01%
110% AFR	9.17%	8.97%	8.87%	8.81%
120% AFR	10.02%	9.78%	9.66%	9.59%
Mid-Term				
AFR	9.44%	9.23%	9.13%	9.06%
110% AFR	10.41%	10.15%	10.02%	9.94%
120% AFR	11.39%	11.08%	10.93%	10.83%
Long-Term				
AFR	10.13%	9.89%	9.77%	9.69%
110% AFR	11.18%	10.88%	10.74%	10.64%
120% AFR	12.22%	11.87%	11.70%	11.59%

Section 7872.—Treatment of Loans with Below-Market Interest Rates

Federal short-term, mid-term and long-term rates determined under the alternate method as provided by section 1.1274-6T of the Temporary Income Tax Regulations are set forth for the month of January 1986. See Rev. Rul. 86-1, this page.

Part III. Administrative Procedural, and Miscellaneous

26 CFR 601.201. Rulings and determination letters.

Rev. Proc. 86-1

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SECTION 1. PURPOSE

The purpose of this revenue procedure is to update Rev. Proc. 85-1, 1985-1 C.B. 440 which provides procedures for issuing rulings, determination letters and information letters, and for entering into closing agreements on specific issues involving the interpretation or application of the federal tax laws. It also tells taxpayers and their representatives where to send requests for rulings, determination letters and information letters. It gives the steps to follow so that requests may be handled more efficiently. Changes to this revenue procedure will be incorporated annually in a new revenue procedure published as the first revenue procedure of the year.

SEC. 2. SCOPE

This revenue procedure applies only to ruling requests, information letters, and closing agreements under the jurisdiction of the Associate Chief Counsel (Technical), and to requests for determination letters under the jurisdiction of field offices that relate to Code sections under the jurisdiction of the Associate Chief Counsel (Technical). The Chief Counsel through the Associate Chief Counsel (Technical) provides basic principles and rules for the uniform interpretation and application of the federal tax laws under the jurisdiction of the Associate Chief Counsel (Technical). The procedures for obtaining rulings, etc., that apply specifically to federal firearms, alcohol and tobacco taxes under subtitle E of the Internal Revenue Code are under the jurisdiction of the Bureau of Alcohol, Tobacco and Firearms. The procedures for obtaining rulings, determination letters, etc., on employee plans and exempt organizations are under the jurisdiction of the Assistant Commissioner (Employee Plans and Exempt Organizations). See Rev. Proc. 83-36, 1983-1 C.B. 763. However, the jurisdiction of the Associate Chief Counsel (Technical) includes section 521 of the Code, on exemption of farmer's cooperatives from tax; section 526, on shipowners' protection and indemnity associations; section 527(a), (b), (c), (d), (e), and (g), on political organizations, and section 528, on certain homeowners' associations.

SEC. 3. CHANGES

.01 A table of contents has been added to the beginning of this revenue procedure to assist taxpayers and Service personnel.

.02 Section 5.01 has been amended to indicate the specific sections of this revenue procedure (Rev. Proc. 86-1) that are applicable to requests for accounting period changes.

.03 Section 9.02 has been amended to require a penalties of perjury statement with any change in a ruling request.

.04 Section 9.05 has been amended to require that telephone numbers also be a part of the factual information submitted with each request for a ruling or a determination letter. Also, the list of revenue procedures that provide specific guidelines for requesting rulings has been revised by updating the list.

.05 Section 16.01 has been amended, as previously announced in Rev. Proc. 85-50, 1985-40 I.R.B. 26, to allow personnel in the rulings divisions to discuss orally substantive tax issues with taxpayers or their representatives on a time-available basis.

SEC. 4. GENERAL PRACTICE AND DEFINITIONS

.01 The Service answers inquiries of individuals and organizations, when appropriate in the interest of sound tax administration, about their status for tax purposes and the tax effects of their acts or transactions. The National Office issues rulings in such matters.

.02 District Directors of Internal Revenue apply the statutes and tax treaties, regulations, revenue rulings, and other precedents published in the Internal Revenue Bulletin in determining tax liability, collecting taxes, and issuing information letters and determination letters in answer to taxpayers' inquiries or requests. For purposes of this revenue procedure, any reference to District Director or district office includes their respective offices or, when appropriate, the director of an Internal Revenue Service Center.

.03 The word "taxpayer" includes all persons subject to any provision of the Internal Revenue Code and, when appropriate, their representatives and issuers of section 103 obligations. Any reference to National Office means only the Office of the Associate Chief Counsel (Technical).

.04 A "ruling" is a written statement

issued to a taxpayer by the National Office that interprets and applies the tax laws to that taxpayer's specific set of facts. Rulings are issued only by the National Office, under the general supervision of the Associate Chief Counsel (Technical). Issuing rulings has been largely delegated to the Directors of the Corporation Tax Division and the Individual Tax Division.

.05 A "determination letter" is a written statement issued by a District Director in response to a written inquiry by a taxpayer that applies the principles and precedents previously announced by the National Office to a specific set of facts. A determination letter is issued only when a determination can be made on the basis of clearly established rules in the statute or regulations, or by a position in a ruling, opinion, or court decision published in the Internal Revenue Bulletin that specifically answers the question presented. A determination letter will not be issued if a determination cannot be made, for example, when the question presents a novel issue, or if the matter is excluded from the jurisdiction of a District Director under section 7 of this revenue procedure.

.06 An "information letter" is a statement issued either by the National Office or by a District Director that calls attention to a well-established interpretation or principle of tax law, without applying it to a specific set of facts. It may be issued if the request indicates that the taxpayer is seeking general information. If the request does not meet the requirements of section 9 of this revenue procedure, but the Service thinks that the general information may help the individual or organization, it may issue an information letter.

.07 A "revenue ruling" is an interpretation by the Service that has been published in the Internal Revenue Bulletin. It is the conclusion of the Service on how the law is applied to an entire set of facts. Revenue rulings are issued only by the National Office and are published for the information and guidance of taxpayers. Internal Revenue Service officials, and other interested parties.

.08 A "closing agreement" is an agreement between the Commissioner of Internal Revenue or the Commissioner's delegate and a taxpayer on a specific issue or issues or liability that is entered into under the authority in section 7121 of the Code. A closing agreement prepared in an office under the responsibility of the Associate Chief Counsel (Technical) is based on a ruling that has been signed by the Commissioner, or the Commissioner's delegate, that says that a closing agreement will be entered into on the basis of the holding of the ruling letter. Closing agreements are final, unless fraud, malfeasance, or misrepresentation of a material fact can be shown. Closing agreements may be entered into when it is advantageous to have the matter permanently and conclusively closed, or when a taxpayer can show good and sufficient reasons for an agreement and the government will sustain no disadvantage by its consummation. In appropriate cases, taxpayers may be asked to enter into a closing agreement as a condition to the issuing of a ruling. If, in a single case, closing agreements are requested for each of a number of taxpayers, such agreements are entered into only if the number of taxpayers is 25 or less. However, if the issue and holding are identical for all taxpayers and they number more than 25, a "mass closing agreement" will be entered into with the taxpayer who is authorized by the others to represent the entire group.

SEC. 5. RULINGS ISSUED BY THE NATIONAL OFFICE

01. *In income and gift tax matters,* the National Office issues rulings on prospective transactions and on completed transactions that occurred before the return is filed for the year in which such transactions are consummated. However, the National Office will issue rulings after the return is filed if a ruling was required by section 367 of the Code (as in effect prior to the amendment made by the Tax Reform Act of 1984) and the ruling request was filed on time under that section. Further, see Rev. Proc. 79-63, 1979-2 C.B. 578, which concerns applications for extensions of the time for making an election or application for relief under section 1.9100-1 of the regulations. If a request for an extension of time under section 1.9100-1 is submitted after the return is filed but before the return is examined, the procedures under Rev. Proc. 86-1 are applicable. If an examination of the return has begun, or is being considered by an Appeals Office, the procedures of Rev. Proc. 86-2, page 19, this Bulletin, are applicable. The National Office issues rulings on the exempt status of organizations under section 521. See Rev. Proc. 84-46, 1984-1 C.B. 541. Specific instructions and guidelines relating to corporate distributions and the determination of the earnings and profits of corporate taxpayers are contained in Rev. Proc. 75-17, 1975-1 C.B. 644. In such matters only the provisions of sections 9.10, 9.11, 9.14 and 11 of this revenue procedure (Rev. Proc. 86-1) are applicable. Specific instructions and guidelines relating to a change in method of accounting for federal income tax purposes are contained in Rev. Proc. 84-74, 1984-2 C.B. 736. In such matters only the provisions of sections 8.02, 9.02, 9.08, 9.10, 9.11, 9.15, 9.17, 9.18 and 9.21, 11, 15, 16 and 17 of this revenue procedure (Rev. Proc. 86-1) are applicable. In matters relating to accounting period changes only the provisions of sections 8.02, 9.02, 9.08, 9.10, 9.11, 9.15, 9.17, 9.18, and 9.21, 11, 15, 16, and 17 of this revenue procedure (Rev. Proc. 86-1) are applicable. The National Office ordinarily does not issue rulings if, at the time the ruling is requested, the identical issue is involved in the taxpayer's return for an earlier period, and (1) that issue is being examined by a District Director or is being considered by an Appeals Office, or (2) that issue has been examined by a District Director or considered by an Appeals Office and the statutory period of limitation on either assessment or for filing a claim for refund or credit of tax has not expired, or a closing agreement covering the issue or liability has not been entered into by a District Director or by an Appeals Office. If a return dealing with an issue for a particular year is filed while a request for ruling on that issue is pending, the National Office will issue the ruling unless it is notified by the taxpayer that an examination of that issue or the identical issue on an earlier year's return has been started by a District Director. See section 9.06. However, even if an examination has begun, the National Office ordinarily will issue the ruling if the District Director agrees, by memorandum, to permit the ruling to be issued. The National Office does not issue rulings on

the replacement of involuntarily converted property, whether or not replacement has been made, if the taxpayer has already filed a return for the tax year in which the property was converted. See section 7.06 of the District Director's authority to issue determination letters in this connection. In addition, the National Office does not issue rulings on the classification of an organization if a return has been filed for the organization for an earlier period.

.02 *In estate tax matters*, the National Office issues rulings with respect to transactions affecting the estate tax of a decedent before the estate tax return is filed. If the estate tax return is due to be filed before the ruling is issued, the taxpayer should secure an extension of time for filing the return for the maximum period of six months, and notify the National Office Branch considering the request for ruling that an extension has been secured. If the return is filed before the ruling is issued, the taxpayer must disclose on the return that a ruling has been requested, attach a copy of the pending ruling request to the return, and notify the National Office that the return has been filed. The National Office will make every effort to issue the ruling within three months of the day on which the return was filed. If the ruling cannot be issued within that three month period, the National Office will notify the District Director having jurisdiction of the return who may, by memorandum to the National Office, grant an additional period for the issuance of the ruling. The National Office will not rule on matters relating to the application of the estate tax to property or the estate of a living person.

1 *In matters involving additional tax under section 2032A(c)*, the National Office issues rulings on prospective transactions and on completed transactions that occurred before the return is filed for the year in which such transactions are consummated.

.03 *In generation-skipping transfer tax matters*, the National Office issues rulings on transactions that affect the generation-skipping transfer tax before the return is filed. Rulings are not issued until after the generation-skipping trust, or trust equivalent, has been established. Rulings are not issued on a generation-skipping transfer tax matter before the distribution or termination takes place. Notwithstanding the foregoing, the National Office will issue rulings regarding the application of the generation skipping transfer tax effective date rules (section 2006(c) of the Tax Reform Act of 1976, Pub. L. 94-455, 1976-3 C.B. (Vol. 1) 1, 365, as amended by section 702(n)(1) of the Revenue Act of 1978, Pub. L. 95-600 1978-3 C.B. (Vol. 1) 1, 169) to wills, trusts, and trust equivalents in existence on June 11, 1976.

.04 *In employment and excise tax matters*, the National Office issues rulings on prospective transactions and on completed transactions either before or after the return is filed for those transactions. In employment tax matters, generally the taxpayer is the employer. However, if the worker asks for the ruling, both the worker and the employer are considered to be the taxpayer and both are entitled to the ruling. The National Office usually will not issue rulings if, at the time the ruling is requested, the identical issue is involved in the taxpayer's return for an earlier period and (1) that issue is under examination by a District Director or under consideration by an Appeals Office, or (2) that issue has been examined by a District Director or considered by an Appeals Office and the statutory period of limitation on either assessment or for filing a claim for refund or credit of tax has not expired, or a closing agreement covering the issue or liability has not been entered into by a District Director or by an Appeals Office. However, if a District Director began an examination of the issue involved in the ruling request, the National Office usually will issue the ruling if the District Director agrees, by memorandum, to permit the ruling to be issued.

.05 *In administrative provisions matters*, the National Office issues rulings on issues arising under the Internal Revenue Code, and related statutes, and the regulations thereunder, that relate primarily to the time, place, manner, and procedures, for reporting and paying taxes; assessing and collecting taxes (including interest and penalties); abating, crediting, or refunding overassessments or overpayments of tax; and filing information returns. Rulings ordinarily are not issued, if, at the time the ruling is requested, the identical issue is involved in the taxpayer's return for an earlier period and (1) that issue is being considered by a District Director or an Appeals Office, or (2) that the issue has been examined by a District Director or considered by an Appeals Office and the statutory period of limitation on either assessment or for filing a claim for refund, or credit of tax has not expired, or a closing agreement covering the issue or liability has not been entered into by a District Director or Appeals Office. If a return involving an issue for a particular year is filed while a request for a ruling on that issue is pending, the National Office will issue the ruling unless an examination of that issue or an examination of the identical issue on an earlier year's return has been started by a District Director. But, even if consideration has begun, the National Office ordinarily will issue the ruling if the District Director agrees, by memorandum, to permit the ruling to be issued.

.06 The National Office does not issue rulings to business, trade, or industrial associations or to similar groups concerning the application of the tax laws to members of the group. It may, however, issue rulings to these groups or associations on their own tax status or liability if the request meets the requirements of this section.

.07 Pending the adoption of regulations (either temporary or final) that interpret the provisions of any act, the issuing of rulings will be considered under the following conditions.

1 If the ruling request presents an issue on which the answer seems clear by applying the statute to the facts, a ruling will be issued under the usual procedures.

2 If the ruling request presents an issue on which the answer seems reasonably certain but not entirely free from doubt, a ruling will be issued only if it is established that a business emergency requires a ruling or that unusual hardship will result from failure to obtain a ruling. If the taxpayer believes that a business emergency exists or that an unusual hardship will result from failure to obtain a ruling, the taxpayer should submit with the request a separate letter stating the facts necessary for the Service to reach a conclusion. In this connection, the Service will not consider a "business emergency" to result from circumstances under the taxpayer's control, such as scheduling within an inordinately short time the

closing date for a transaction or a meeting of the board of directors or the shareholders of a corporation. However, if the ruling request presents an issue that cannot be readily resolved before regulations are issued, a ruling will not be issued.

SEC. 6. DETERMINATIONS UNDER SECTION 999(d) OF THE CODE

Under Rev. Proc. 77-9, 1977-1 C.B. 542, the National Office issues determinations under section 999(d) of the Code that may deny certain benefits of the foreign tax credit, deferral of earnings of foreign subsidiaries and domestic international sales corporations (DISC) to a person, if that person, or a member of a controlled group (within the meaning of section 993(a)(3)) that includes that person, or a foreign corporation of which a member of the controlled group is a United States shareholder, agrees to participate in, or cooperate with, an international boycott.

SEC. 7. DETERMINATION LETTERS ISSUED BY DISTRICT DIRECTOR

.01 *In income and gift tax matters.* District Directors issue determination letters in response to taxpayers' written requests on completed transactions that affect returns over which they have examination jurisdiction. This applies only if the question presented is specifically answered by statute or regulation, or by the position stated in a ruling, opinion or court decision published in the Internal Revenue Bulletin. A determination letter usually is not issued for a question concerning a return to be filed by the taxpayer if the same question is involved in a return already filed. District Directors do not issue determination letters on the tax consequences of prospective or proposed transactions, except as provided in section 7.06.

.02 *In estate tax matters.* District Directors issue determination letters in response to written requests affecting the estate tax returns over which they have examination jurisdiction, but only if the question presented is specifically answered by statute or regulation, or by the position stated in a ruling, opinion, or court decision published in the Internal Revenue Bulletin. District Directors do not issue determination letters on matters concerning the application of the estate tax to property or the estate of a living person.

.03 *In generation-skipping transfer tax matters.* District Directors issue determination letters in response to written requests affecting the generation skipping transfer tax returns over which they have examination jurisdiction, but only if the questions presented are specifically answered by statute or regulation, or by a position stated in a ruling, opinion, or court decision published in the Internal Revenue Bulletin. District Directors do not issue determination letters or matters concerning the application of the generation-skipping transfer tax before the distribution or termination takes place.

.04 *In employment and excise tax matters.* District Directors issue determination letters on completed transactions in response to written requests from taxpayers over which they have examination jurisdiction, but only if the question presented is specifically answered by statute or regulation, or by the position stated in a ruling, opinion, or court decision published in the Internal Revenue Bulletin.

.05 Notwithstanding the provision of section 7.01, 7.02, 7.03 and 7.04, a District Director will not issue a determination letter in response to a request that presents a question specifically answered by statute or regulation, or by the position stated in rulings, etc., published in the Internal Revenue Bulletin, if (1) it appears that the taxpayer has directed a similar inquiry to the National Office, (2) the same issue involving the same taxpayer is pending in a case before an Appeals Office, (3) the determination letter is requested by an industry, trade association, or similar group, or (4) the request involves an industrywide problem. Under no circumstances will a District Director issue a determination letter unless it is clearly shown that the request concerns a return that has been filed or is required to be filed over which the District Director has or will have examination jurisdiction. Notwithstanding the provisions of section 7.04, a District Director will not issue a determination letter on an employment tax question if the specific question for the same taxpayer has been or is being considered by the Central Office of the Social Security Administration or the Railroad Retirement Board. Nor will District Directors issue determination letters for determination of a constructive sales price under section 4216(b) or 4218(e) of the Code. The National Office, however, will issue rulings in this area. See section 8.04.

.06 District Directors issue determination letters on the replacement of involuntarily converted property under section 1033 even though the replacement has not been made, if the taxpayer has filed an income tax return for the year in which the property was involuntarily converted.

.07 A request received by a District Director on a question concerning an income, estate, or gift tax return already filed will be, in general, considered in connection with the examination of the return. If a response is made to such a request before the return is examined, it will be considered a tentative finding in any later examination of that return.

SEC. 8. DISCRETIONARY AUTHORITY TO ISSUE RULINGS AND DETERMINATION LETTERS

.01 The Service ordinarily will not issue rulings or determination letters in certain areas because of the factual nature of the problem involved, or for other reasons. Rev. Proc. 86-3, page 26, this Bulletin, provides a list of these areas. This list is not all inclusive, since the Service may decline to issue a ruling or a determination letter on other grounds, whenever warranted by the facts or circumstances of a particular case. The National Office and District Directors may, when it is considered appropriate and in the best interest of the Service, issue information letters calling attention to well-established principles of tax law.

.02 A ruling or a determination letter is not issued on alternative plans of proposed transactions or on hypothetical situations.

.03 The National Office ordinarily will not issue rulings on only part of an integrated transaction.

.04 The National Office will issue rulings in all cases on the determination of a constructive sales price under section 4216(b) or 4218(c) and in all other cases on prospective or future transactions if the law or regulations requires a determination of the effect of a proposed transaction for tax purposes.

SEC. 9. INSTRUCTIONS TO TAXPAYER

.01 The taxpayer should submit a request for a ruling or a determination letter in duplicate if (1) more than one issue is presented in the request, or (2) a closing agreement is requested on the issue presented. It is not necessary to submit requests in duplicate under other circumstances except as set forth in section 9.09.

.02 A request for a ruling or determination letter and any factual information or change in the ruling request submitted at a later time must be accompanied by a declaration in the following form: "Under penalties of perjury, I declare that I have examined this request, including accompanying documents, and to the best of my knowledge and belief, the facts presented in support of the requested ruling or determination letter are true, correct, and complete." The declaration may not be made by the taxpayer's representative. It must be signed by the person or persons on whose behalf the request is made. The person who must sign for a corporate taxpayer must be an officer of the corporate taxpayer who has personal knowledge of the facts. The officer must be one whose duties are not limited to obtaining a ruling or determination letter from the Service. The person signing for a trust or partnership must be a trustee or partner who has personal knowledge of the facts.

.03 If more than one issue is presented in a request for a ruling, the Service generally will issue a single ruling letter. However, the taxpayer may request a separate ruling letter on any of the issues. Unless the Service determines that it is not feasible or not in the best interest of the Service to comply with such a request, it will issue separate ruling letters.

.04 When multiple issues are involved in a single factual situation and separate letters requesting rulings are submitted, a statement to this effect must be included in each ruling letter request. The Service in issuing each ruling will state that separate rulings have been issued or requests for rulings are pending.

.05 Each request for a ruling or a determination letter must contain a complete statement of all of the facts relating to the transaction. Such facts include: names, addresses, telephone numbers, and taxpayer identification numbers of all interested parties; the location of the District Office that has or will have examination jurisdiction over the return, not the Service Center where the return is filed; a full and precise statement of the business reasons for the transaction, and a carefully detailed description of the transaction. (The term "all interested parties" does not mean that a list is required of all shareholders of a widely-held corporation requesting a ruling relating to a reorganization, or a list of employees where a larger number may be involved.) If the request deals with only one step of a larger integrated transaction, the facts, circumstances, etc. relating to the entire transaction must be submitted. However, see section 8.03 of this revenue procedure (Rev. Proc. 86-1). In addition, true copies of all contracts, wills, deeds, agreements, instruments, and other documents in the transaction must be submitted with the request. Original documents, such as contracts, wills, etc., should not be submitted because they become part of the Service's file and will not be returned. All material facts in documents must be included in the taxpayer's letter requesting a ruling or in supplemental letters, and not merely incorporated by reference, and must be accompanied by an analysis of their bearing on the issue or issues, specifying the provisions that apply. If the request concerns a corporate distribution, reorganization, or similar transaction, the corporate balance sheet and profit and loss statement should be submitted. If the request relates to a prospective transaction, the most recent balance sheet and profit and loss statement should be submitted.

Material facts furnished to the Service by telephone or orally at a conference must be promptly confirmed by letter to the Service with a declaration in the form described in section 9.02. This confirmation must be furnished within 21 calendar days to be considered part of the request. An extension of the 21-day period will be granted only if justified in writing by the taxpayer and approved by the Chief or Assistant Chief of the branch to which the case is assigned. A request for extension should be submitted before the end of the 21-day period. If unusual circumstances close to the end of the 21-day period make a written request impractical, within the 21-day period the National Office should be told of the problem and that the written request for extension will be coming soon. Such a request must be sent promptly. The taxpayer or taxpayer's representative will be told promptly and later in writing of the approval or denial of the requested extension. There is no right of appeal to a denial of an extension request. Because the purpose of these procedures is to speed up the ruling process, the taxpayer is encouraged to submit the required relevant material promptly. Therefore, requests for extension should be justified by compelling facts and circumstances. If the Service is not made aware, as provided above, of problems in meeting the 21-day period, or if the request is not sent promptly after the National Office is notified of problems in meeting the 21-day period, the Service will process the case on the assumption that no further submission will be received.

Specific guidelines for requesting rulings under certain Code sections follow: Rev. Proc. 84-48, 1984-1 C.B. 547, as amplified by Rev. Proc. 84-49, 1984-1 C.B. 548, and Rev. Proc. 84-50, 1984-1 C.B. 550, (guidelines for submitting requests for rulings under sections 103 and 7478); Rev. Proc. 80-36, 1980-2 C.B. 769, as amended by Rev. Proc. 83-73, 1983-2 C.B. 593 (certification of manufacturers under section 44C); Rev. Proc. 68-11, 1968-1 C.B. 761 (guidelines for a ruling request under section 117); Rev. Proc. 81-62, 1981-2 C.B. 684 (guidelines concerning a request for a ruling under section 302 or 311); Rev. Proc. 81-68, 1981-2 C.B. 723 (guidelines concerning a request for a ruling under section 332, 334(b)(1) or 334(b)(2)); Rev. Proc. 81-52, 1981-2 C.B. 625 (guidelines concerning a request for a ruling under sections 331 and 337); Rev. Proc. 81-42, 1981-2 C.B. 611 (guidelines concerning a request for a ruling under section 302(b)(4)); Rev. Proc. 83-59, 1983-2 C.B. 575 (guidelines concerning a request for a ruling under section 351); Rev. Proc. 81-41, 1981-2 C.B. 605 (guidelines concerning a request for a ruling under section 355); Rev. Proc. 68-23, 1968-1 C.B. 821, as modified by Rev. Proc. 77-17, 1977-1 C.B. 577, and as amplified by Rev. Proc. 76-20, 1976-1 C.B. 560 and Rev. Proc. 80-14, 1980-1 C.B. 617, Rev. Proc. 69-19, 1969-2 C.B. 301, as amplified by Rev. Proc. 74-36, 1974-2 C.B. 491, Rev. Proc. 77-5, 1977-1 C.B. 536, Rev. Proc. 78-27, 1978-2 C.B. 526, and Rev. Proc. 78-28, 1978-2 C.B. 526 (guidelines concerning a request for a ruling under section 367). However, see section 7.367(b) of the Temporary Income Tax Regulations and section 1.367(a) of the Income Tax Regulations under the Tax Reform Act of 1976, which superseded the previously mentioned revenue procedures relating to section 367, to the extent of overlapping rules; Rev. Proc. 81-70, 1981-2 C.B. 729 (guidelines for estimating the basis of stock acquired in a section 368(a)(1)(B) reorganization); Rev. Proc. 81-60, 1981-2 C.B. 680 (guidelines concerning a request for a ruling under section 368(a)(1)(E)). See, however, Rev. Proc. 86-3, page 26, this Bulletin, which provides that a ruling whether a transaction constitutes a corporate recapitalization within the meaning of section 368(a)(1)(E) will not be issued except when the recapitalization is an integral part of a larger transaction and it is impossible to determine the tax consequences of the larger transaction without making a determination with regard to the recapitalization, Rev. Proc. 77-30, 1977-2 C.B. 539, as clarified by Rev. Proc. 78-18, 1978-2 C.B. 491 and Rev. Proc. 78-23, 1978-2 C.B. 503, and Rev. Proc. 77-37, 1977-2 C.B. 568, as amplified by Rev. Proc. 77-41, 1977-2 C.B. 574 and Rev. Proc. 83-81, 1983-2 C.B. 598 and Rev. Proc. 84-42, 1984-1 C.B. 521 (certain other guidelines concerning requests for rulings handled by the Reorganization Branch of the Corporation Tax Division); Rev. Proc. 71-19, 1971-1 C.B. 698 (guidelines concerning requests for rulings on unfunded deferred compensation); Rev. Proc. 83-25, 1983-1 C.B. 689 (guidelines for requesting changes in accounting period for Subchapter S corporations); Rev. Proc. 72-13, 1972-1 C.B. 735, Rev. Proc. 74-17, 1974-1 C.B. 438, and Rev. Proc. 75-16, 1975-1 C.B. 676 (guidelines on classification of limited partnerships); Rev. Proc. 82-58, 1982-2 C.B. 847 (guidelines on classification of organizations as liquidating trusts); Rev. Proc. 82-36, 1982-1 C.B. 490 (guidelines concerning requests for consent to elect not to defer gain or loss on deferred intercompany transactions); Rev. Proc. 79-63, 1979-2 C.B. 578 (factors considered and information needed for granting extensions under section 1.9100-1 of the Income Tax Regulations.

A ruling request that involves a question of whether a rate order, proposed or issued by a regulatory agency, will meet the normalization requirements of sections 46(f), 167(l), and 168(e)(3) of the Code, ordinarily will not be considered unless the taxpayer states in the request for ruling whether:

(1) the regulatory authority responsible for establishing or approving the taxpayer's rates has reviewed the request and believes that the request is adequate and complete, and

(2) the taxpayer will permit the regulatory authority to participate in any National Office conference concerning the request.

.06 The request must contain a statement of whether, to the best of the knowledge of the taxpayer and the taxpayer's representative(s), if any, the identical issue is in a return of the taxpayer within the meaning of section 267 of the Code, or a member of an affiliated group of which the taxpayer is also a member within the meaning of section 1504) and, if so, whether the issue (1) is being examined by a District Director, (2) has been examined and the statutory period of limitation on either assessment or for filing a claim for refund or credit of tax has not expired or a closing agreement covering the issue or liability has not been entered into by a District Director, (3) is being considered by and Appeals Office in connection with the taxpayer's return for an earlier period, or has been considered by an Appeals Office and the statutory period of limitation on either assessment or for filing a claim for refund or credit of tax has not expired or a closing agreement covering the issue or liability has not been entered into by an Appeals Office, or (4) is pending in litigation in a case involving the taxpayer or a related taxpayer. The request must also contain a statement whether, to the best of the knowledge of the taxpayer and the taxpayer's representative(s), the identical or similar issue has been (i) submitted to the Service, but withdrawn before a ruling was issued, or (ii) ruled on by the Service to the taxpayer or to the taxpayer's predecessor and, if so, when and with what results. If, after the request is filed but before a ruling is issued, the taxpayer knows that an examination of the issue by a District director has been started, the taxpayer must notify the National Office of such action. If a return is filed before a ruling is received from the National Office concerning the issue, a copy of the request must be attached to the return. This alerts the District Office and avoids premature District action on the issue.

.07 As an alternative procedure (known as the "two-part" ruling request procedure) for the issuance of rulings on prospective transactions, the taxpayer may submit a summary of the facts considered to be controlling the issue, in addition to the complete statement required for ruling requests by section 9.05. If the National Office agrees with the summary, the National Office will use it as the basis for the ruling. To use this procedure, the taxpayer should submit the following with the request for a ruling:

1 A complete statement of facts about the transaction, together with related documents, as required by section 9.05; and

2 A summary statement of the facts believed to be controlling in reaching the request conclusion. When the taxpayer's statement of controlling facts is accepted, the Service will base its ruling on these facts and only this statement will ordinarily be incorporated in the ruling letter. It is emphasized, however, that:

(a) The taxpayer may elect this procedure for a "two-part" ruling request. It is not to be considered a required substitute for the regular procedures provided by this revenue procedure;

(b) The taxpayer's rights and responsibilities are the same under the "two-part" ruling request procedure as those provided in this revenue procedure;

(c) The Service reserves the right to rule on the basis of a more complete statement of facts it considers controlling and to seek more information in developing facts and restating them; and

(d) The "two-part" ruling request procedure will not apply if it is inconsistent with other procedures, such as those dealing with request for permission to change accounting methods or periods; applications for recognition of exempt status under section 521 of the Code; or rulings or employment tax status.

.08 If the taxpayer advocates a particular conclusion, an explanation of the grounds for the assertion must be furnished, together with a statement of relevant authorities in support of the taxpayer's views. Even though the taxpayer is urging no particular tax treatment of a proposed or prospective transaction, the taxpayer's views on the tax results of the proposed action and a statement of relevant authorities to support those views must be furnished. In addition, the taxpayer is encouraged to inform the Service, and discuss the implications of any legislation, tax treaties, court decisions, regulations, revenue rulings or revenue procedures that the taxpayer determines to be contrary to the position advanced. If the taxpayer determines that there are no contrary authorities, a statement to this effect would be helpful in the ruling request. Identification and discussion of contrary, authorities will generally enable Service personnel to arrive more quickly at a full understanding of the issue and the relevant authorities. There is a further advantage to the taxpayer. When Service personnel receive the request, they will have before them the taxpayer's thinking on the effect and applicability of contrary authorities. Such information should, therefore, make research easier and lead to earlier action by the Service. Conversely, failure to disclose and distinguish significant contrary authorities may result in requests for additional memoranda that will delay action on the ruling request.

.09 To assist the Service in making the deletions required by section 6110(c) of the Code from the text of rulings and determination letters, to be made open to public inspection under section 6110(a), a deletions statement must accompany each request. The statement must either state that no information other than names, addresses, and identifying numbers need be deleted or, if more information is proposed to be deleted, the statement must indicate the deletions proposed by the person requesting the ruling or determination letter. If the latter alternative is chosen, the statement must be made in a separate document, and it must be accompanied by a copy of the request for a ruling or determination letter and supporting documents, on which must be shown by the use of brackets, the material that the person making the request believes should be deleted pursuant to section 6110(c). The statement of proposed deletions must indicate the statutory basis, under section 6110(c), for each proposed deletion. The statement of proposed deletions must not appear to be referred to anywhere in the request for a ruling or determination letter. If the person making the request decides to ask for additional deletions before the ruling or determination letter is issued, additional statements may be submitted. The procedures in this paragraph also apply to additional information that is submitted after the initial request.

.10 A request by or for a taxpayer must be signed by the taxpayer or the taxpayer's authorized representative. if the request is signed by a representative, or if the representative is to appear before the Service in connection with the request, the representative must be:

1 an attorney who is a member in good standing of the bar of the highest court of any state, possession, territory, commonwealth, or the District of Columbia, and who files with the Service a written declaration that he or she is currently qualified as an attorney and is authorized to represent the taxpayer.

2 a certified public accountant who is qualified to practice in any state, possession, territory, commonwealth, or the District of Columbia, and who files with the Service a written declaration that he or she is currently qualified as a certified public accountant and is authorized to represent the taxpayer; or

3 a person, other than an attorney or certified public accountant who is currently enrolled to practice before the Service, and who files with the Service a written declaration that he or she is currently enrolled (including in the declaration either the enrollment number or the expiration date of the enrollment card) and is authorized to represent the taxpayer. (See Treasury Department Circular No. 230 (31 CFR Part 10), 1985-51 I.R.B. 6, for the rules on who may practice before the Service.) These requirements do not apply to an individual representing his or her fulltime employer, or to a bona fide officer, administrator, administratrix, trustee, etc., representing a corporation, trust, estate, association, or organized group. An unenrolled preparer of a return (other than an attorney or certified public accountant referred to in (1) and (2) above) who is not a full-time employee or a bona fide officer, administrator, administratrix, trustee, etc., may not represent a taxpayer in connection with a ruling or a determination letter. Any authorized representative, whether or not enrolled to practice, must also comply with the conference and practice requirements of the Statement of Procedural Rules (26 CFR 601). Form 2848, Power of Attorney, and Form 2848-D, Authorization and Declaration, may be used with regard to rulings, closing agreements, and determination letters requested under this revenue procedure.

.11 If a taxpayer has more than one representative, it is sufficient to send a copy of the ruling to any one of them. Copies of a ruling will be sent to no more than two representatives, provided that they are located at different mailing addresses. If a taxpayer does not designate which representative is to receive a copy of the ruling, a copy of the ruling will be sent to the first representative named on the latest power of attorney. If the original of the ruling is to be sent to a representative, the power of attorney should contain a statement to that effect and designate the mailing address of the representative.

.12 A request for a ruling letter by the National Office should be sent to the Internal Revenue Service, Associate Chief Counsel (Technical), Attention CC:IND:S:3, Room 6545, 1111 Constitution Avenue, N.W., Washington, DC 20224. A request for a determination letter should be sent to the District Director of Internal Revenue whose office has or will have examination jurisdiction over the taxpayer's return.

.13 If a request for a ruling or determination letter does not comply with all the provisions of this revenue procedure, the request will be acknowledged, and the requirements that have not been met will be pointed out. If a request for a ruling lacks essential information, the taxpayer will be told that if the information is not received within 30 calendar days, the request will be closed. If the information is received after the request is closed, it will be reopened and treated as a new request as of the date the essential information is received. A request for a ruling letter sent to the District Director that does not comply with the provisions of this revenue procedure will be returned by the District Director for corrections before it is sent directly to the National Office.

14. A taxpayer who wants to have a conference on the issue or issues involved should indicate this in writing when, or soon after, filing the request.

.15 The Service processes requests for ruling and determination letters in regular order and as expeditiously as possible. Consideration of a request for processing ahead of its regular order, or by a specified time, delays the processing of other matters. Requests for processing ahead of the regular order must be made in writing, preferably in a separate letter sent with, or soon after, the request. If the request is not made in a separate letter, then the letter in which the request is made should say, at the top of the first page: "Expeditious Handling Is Requested. See page of this letter." The request should give a compelling need for such treatment. The Service cannot give assurance that any letter will be processed by the time requested. For example, the scheduling of a closing date for a transaction or a meeting of the board of directors or shareholders of a corporation, without regard for the time it may take to obtain a ruling or determination letter, will not be considered sufficient reason for handling a request ahead of its regular order. Nor will the possible effect of fluctuation in the market price of stocks on a transaction be considered sufficient reason for handling a request out of order. Requests by telegram will be treated in the same manner as requests by letter. Ruling and determination letters ordinarily are not issued by telegram. A request for expeditious handling will not cause the Communications and Records Group to route the case to the Ruling. Branch ahead of normal processing; and a request for expeditious handling will not be considered until the underlying ruling request has been found to satisfy the section 6110 requirements.

.16 The Director, Individual Tax Division, has primary responsibility for providing basic principles for uniform interpretation and application of the federal tax laws in those areas involving: income taxes of noncorporate taxpayers (including individuals, partnerships, estates, and trusts political organizations under section 527 (except subsection (f)); employment taxes and taxes on self-employment income; estate, gift, generation-skipping transfer, and certain excise taxes; and procedure and administration provisions of the Internal Revenue Code, except those that apply specifically to employee plans, exempt organizations, and actuarial determinations.

.17 The Director, Corporation Tax Division, has primary responsibility for providing basic principles of and rules for uniform interpretation and application of the federal tax laws in those areas involving: income taxes and earnings and profits of corporate taxpayers; changes in methods and periods of accounting, depreciation, depletion, valuation and other engineering issues; the taxable status of exchanges and distributions in connection with corporate organizations, reorganizations, and liquidations; and the exemption of farmers' cooperatives (under section 521), shipowners' protection and indemnity associations (under section 526), and certain homeowners associations (under section 528).

.18 A taxpayer may obtain information regarding the status of a request by calling the person whose name and telephone number is shown on the acknowledgement of receipt of the request.

.19 If, after receiving the notice under section 6110(f)(l) of the Code of intention to disclose the ruling or determination letter (including a copy of the version proposed to be open to public inspection and notation of third-party communications under section 6110(d)), the person requesting the ruling or determination letter wants to protest the disclosure of certain information in the ruling or determination letter, that person must within 20 calendar days send a written statement to the Internal Revenue Service office indicated on the notice of intention to disclose, identifying those deletions that the Service has not made and that the person requesting the ruling or determination letter believes should have been made. That person must also submit a copy of the version of the ruling or determination letter proposed to be open to public inspection on which the person indicates, by use of brackets, the deletions proposed by the taxpayer that have not been made by the Service. Generally, the Service will not consider the deletion under this subparagraph of any material that the taxpayer did not propose to be deleted before the ruling or determination letter was issued. Within 20 days after it receives the response to the notice under section 6110(f)(1), the Service will mail to that person its final administrative conclusion regarding the deletions to be made. The taxpayer does not have the right to a conference to resolve any disagreements concerning material to be deleted from the text of the ruling. However, these matters may be taken up at any conference that is otherwise scheduled regarding the request.

.20 After receiving the notice under section 6110(f)(1) of the Code of intention to disclose (but not later than 60 calendar days after the notice is mailed), the person requesting a ruling or determination letter may send a request for delay of public inspection under either section 6110(g)(3) or section 6110(g)(3) and (4). The request for delay must be sent to the Internal Revenue Service office indicated on the notice of intention to disclose. A request for delay must contain the date on which it is expected that the underlying transaction will be completed. The request for delay under section 6110(g)(4) must contain a statement from which the Commissioner may determine that there are good reasons for the delay.

.21 A taxpayer who receives a ruling or determination letter before filing a return about any transaction that has been consummated and that is relevant to the return being filed should attach a copy of the ruling or determination letter to the return when it is filed.

.22 Protests to adverse rulings under section 367 will be processed as follows:

Under Rev. Proc. 77-5, 1977-1 C.B. 536, a taxpayer may protest an adverse, or terms and conditions, ruling letter issued on or after January 31, 1977 under section 367(a)(1) of the Code. This protest procedure applies only to transactions consummated prior to 1985 or described in a request for ruling filed before March 1, 1984. Under Rev. Proc. 77-5 the protest may not be made later than the close of the 45th calendar day after the date of the ruling letter. A protest is considered made on the date of the postmark of a letter of protest sent to the Associate Chief Counsel (Technical), or the date that the letter is hand delivered to the Service. The letter must include: (1) a copy of the ruling letter; (2) the reasons for the protest including, if applicable, (a) the grounds for asserting that none of the principal purposes for the exchange is the avoidance of federal income tax, (b) the grounds for asserting that the terms and conditions in the ruling letter pursuant to which an exchange to which section 367 applies will be considered not to be in pursuance of tax avoidance are not reasonable, and (c) the arguments supporting a protest of the validity of a ruling position published by the Service, such as a position in the guidelines announced in Rev. Proc. 68-23, 1968-1 C.B. 821 (factual material not previously submitted and considered by the Service should not be included in the protest); (3) a statement of whether a conference is desired; and (4) names of persons (including authorized representatives) expected to attend the conference, if a conference is granted. The Associate Chief Counsel (Technical) will establish an ad hoc advisory board to consider each protest, whether or not a conference is requested. The taxpayer will be granted one conference upon request. Whether or not such a request is made, the board may ask for one or more conferences or for written submissions. The taxpayer will be notified of the time, date, and place of the conference, and of the names of the members of the board. The board will consider all materials submitted in writing by the taxpayer and oral arguments presented at the conference. The board will make its recommendation to the Associate Chief Counsel (Technical) who will make a decision in the matter. Any oral arguments made at a conference by the taxpayer, which have not previously been submitted to the Service in writing, may, if desired, be submitted to the Service in writing if postmarked no later than the end of the 7th calendar day after the day of the conference. The taxpayer will be informed of the decision of the Associate Chief Counsel (Technical) by certified or registered mail.

.23 For appeal procedures with regard to adverse determination letters under section 521 of the Code and revocation or modification of exemption rulings and determination letters under section 521, see Rev. Proc. 84-46, 1984-1 C.B. 541.

SEC. 10. HANDLING OF RULING REQUESTS

.01 Within 21 calendar days after a ruling request is received in the branch, Service personnel will contact the taxpayers to discuss informally the procedural and substantive issues in the ruling request.

.02 The following subject matters are included in the 21 calendar day procedure:

1 Individual Income Tax Branch

(a) Partnerships and trusts

(b) Real estate investment trusts

(c) Stock options

(d) Employment and self-employment taxes (except ruling requests from individuals for employment status submitted on Forms SS-8)

(e) Credit for employment of certain new employees

(f) Rental value of parsonages

2 All matters within the jurisdiction of the Corporation Tax Branch, except cases

(a) involving a request for change in accounting methods or periods, generally governed by Rev. Proc. 84-74, 1984-2 C.B. 736,

(b) relating to the last-in, first-out method of computing inventory,

(c) concerning insurance issues on contracts with reserves based on segregated asset accounts,

(d) concerning insurance issues requiring actuarial computations.

3 All matters within the jurisdiction of the Specialty Tax Branch.

4 All matters within the jurisdiction of the Engineering Branch (except cases involving a request for a change in accounting methods), and the Reorganization Branch.

.03 Procedures to be followed regarding ruling requests are:

1 Within 21 calendar days after a ruling request has been received in the branch having jurisdiction, a representative of the branch will contact the taxpayer to discuss the procedural issues in the ruling requests covered by this procedure. Considering the complexity of some cases or the number of issues involved, it may not be possible for the branch representative to discuss the substantive issues in the ruling request during this initial contact. However, when possible, as to each issue coming within the jurisdiction of the branch, the branch representative will tell the taxpayer:

(a) whether the branch representative will recommend the Service rule as the taxpayer requested, rule adversely on the matter, or not rule;

(b) whether the taxpayer should submit additional information or representations to enable the Service to rule on the matter; or

(c) whether because of the nature of the transaction, or the issue presented, a tentative conclusion on the issue cannot be reached.

2 When the rulings requested involve matters within the jurisdiction of more than one branch or more than one office in the same branch, a representative of the branch that received the original ruling request will tell the taxpayer within the initial 21 calendar day contact period: (1) that the rulings requested involving matters within the jurisdiction of another branch or another office in the same branch have been referred to the other branch or office for consideration; and (2) that a representative of the other branch or office will contact the taxpayer within 21 calendar days after receiving the referral to informally discuss the procedural and, to the extent possible, the substantive issues if covered by this procedure.

3 If something less than a fully favorable ruling is indicated, the branch representative will tell the taxpayer if minor modifications of the transaction or adherence to certain published positions will warrant the issuance of a favorable ruling. In addition, the branch representative may tell the taxpayer what representations must be furnished in a document to comply with the requirements of the Service. However, the branch representative will not suggest precise changes that would materially alter the form of the proposed transaction. If, at the conclusion of the discussion, the branch representative determines that a meeting in the National Office would better serve the purpose of developing or exchanging information, a meeting will be offered and an early meeting date arranged. This meeting will not be the taxpayer's conference of right, as described in this revenue procedure.

4 The Service will not be bound by the informal opinion expressed by the branch representative or any other authorized Service representative under this procedure, and such an opinion cannot be relied upon as a basis for granting retroactive relief under the provisions of section 7805(b) of the Code.

5 The ruling request will then be processed under present procedures.

SEC. 11. CONFERENCES IN THE NATIONAL OFFICE

.01 A taxpayer may request a conference only in connection with a ruling request. Normally, a conference is scheduled only when the National Office considers it to be helpful in deciding the case or when an adverse decision is indicated. If conferences are being arranged for more than one request for a ruling involving the same taxpayer, they will be scheduled so as to cause the least inconvenience to the taxpayer. If a conference has been requested, the taxpayer will be notified by telephone, if possible, of the time and place of the conference. The conference must be held within 21 calendar days after such contact has been made. Procedures for requesting an extension of the 21-day period and notifying the taxpayer or the taxpayer's representative of the Service's decision are the same as those stated in section 9.05.

.02 A taxpayer is entitled, as a matter of right, to only conference in the National Office unless one of the circumstances discussed in section 11.06 develops. This conference normally will be held at the branch level of the appropriate division in the office of the Associate Chief Counsel (Technical) and will be attended by a person who, at the time of the conference, has authority to sign the ruling letter for the branch chief in the case being discussed. When more than one branch has taken an adverse position of an issue within its jurisdiction presented in a ruling request, or when the position ultimately adopted by one branch will affect another branch's determination, a representative from each branch with the authority to sign for the branch chief will attend the conference. If more than one subject is to be discussed at the conference, the discussion will constitute a conference on each subject. In order to promote a free and open discussion of the issues, the conference usually will be held after the branch has had an opportunity to study the case. However, at the request of the taxpayer or representative, the conference of right may be held at an earlier stage in the consideration of the case than the Service ordinarily would designate. No taxpayer has a "right" to appeal the action of a branch to a division director or to any other official of the Service.

.03 In employment tax matters, only the party entitled to the ruling is entitled to a conference.

.04 Since conference procedures are informal, no tape, stenographic, or other verbatim recording of a conference will be made.

.05 The senior Service representative present at the conference insures that the taxpayer has full opportunity to present views on all of the issues that are in question. The Service representative explains the Service's tentative decision on the substantative issues and the reason for that decision. If the taxpayer advances prospective application under section 7805(b) of the Code, the Service, representative will discuss the tentative recommendation concerning the request for relief and the reason for the tentative recommendation. No commitment will be made as to the conclusion that the Service will finally adopt.

.06 An invitation to an additional conference will be extended if, after the conference of right, an adverse holding is proposed but on a new issue or on the same issue but on different grounds from those discussed at the first conference. There is no right to another conference when a proposed holding is reversed at a higher level with a result less favorable to the taxpayer if the ground or arguments on which the reversal is based were discussed at the conference of right. The provision of this revenue procedure limiting the number of conferences to which a taxpayer is entitled will not prevent a taxpayer from attending further conferences when, in the opinion of National Office personnel, such conferences are necessary. All additional conferences of the type discussed in this paragraph are held only at the invitation of the Service.

.07 It is the responsibility of the taxpayer to furnish in writing to the National Office any additional data, lines of reasoning, precedents, etc. that are proposed by the taxpayer and discussed at the conference but that were not previously or adequately presented in writing. The taxpayer must furnish the additional information within 21 calendar days. If the additional information is not received within that time, a ruling will be issued on the basis of the information on hand or, if appropriate, no ruling will be issued. Procedures for requesting an extension of the 21-day period and notifying the taxpayer or the taxpayer's representative of the Service's decision are the same as those stated in section 9.05.

SEC. 12. DISTRICT OFFICE REFERRAL OF MATTERS TO THE NATIONAL OFFICE

.01 Request for determination letters received by District Directors that, under the provisions of this revenue procedure, may not be acted upon by a District Office, will be forwarded to the National Office for reply. The District Office will let the taxpayer know that this action has been taken. District Directors will also refer to the National Office any request for a determination letter that in their judgment should have the attention of the National Office.

.02 If the request involves an issue on which the Service will not issue a ruling or determination letter, the request will not be forwarded tot the National Office. The District Office will let the taxpayer know that the Service will not issue a ruling or a determination letter on the issue. See section 8.01 of this revenue procedure.

SEC. 13. REFERRAL OF MATTERS TO DISTRICT OFFICES

Requests for rulings received by the National Office that, under section 5 of this revenue procedure, may not be acted upon by the National Office will be forwarded to the District Office that has examination jurisdiction over the taxpayer's return. The taxpayer will be notified of this action. If the request is on an issue or in an area of the type discussed in section 8.01 and it is decided not to issue a ruling or an information letter, the National Office will let the taxpayer know and the request will then be forwarded to the appropriate District Office for association with the related return.

SEC. 14. REVIEW OF DETERMINATION LETTERS

Determination letters issued under sections 7.01, 7.02, 7.03 and 7.04 are not reviewed by the National Office before they are issued. If a taxpayer believes that a determination letter of this type is in error the taxpayer may ask the District Director to reconsider the matter. The taxpayer may also ask the District Director to request technical advice from the National Office. In such an event the procedures in Rev. Proc. 86-2 must be followed.

SEC. 15. WITHDRAWAL OF REQUESTS

A request for a ruling or determination letter may be withdrawn at any time before the signing of the letter of reply. If a request for a ruling is withdrawn, the National Office may give its views on the subject matter of the request to the District Director whose office will have examination jurisdiction over the taxpayer's return for consideration in connection with any later examination of the taxpayer's return. Even though a request is withdrawn, all correspondence and exhibits will be kept by the Service and will not be returned to the taxpayer. In appropriate cases, the Service may publish its findings in a revenue ruling or revenue procedure.

SEC. 16. ORAL ADVICE TO TAXPAYERS

.01 The Service does not issue rulings or determination letters on oral requests. However, personnel in the rulings divisions ordinarily will discuss with taxpayers or their representatives inquiries regarding: substantive tax issues; whether the Service will rule on particular issues; and questions relating to procedural matters about submitting ruling requests (including the application of section 9, of this revenue procedure, to a particular case). Any discussion of substantive issues will be at the discretion of the Service on a time-available basis, and will not be binding on the Service.

.02 A taxpayer may seek oral technical assistance from a Taxpayer Service Representative in a District Office or Service Center when preparing a return or report, under other established procedures. Oral advice is advisory only and the Service is not bound to recognize it in the examination of the taxpayer's return.

SEC. 17. EFFECT OF RULINGS

.01 A taxpayer may not rely on a ruling issued to another taxpayer. A ruling, except to the extent incorporated in a closing agreement, may be revoked or modified at any time under appropriate circumstances. See section 4.08 for the effect of a closing agreement. If a ruling is revoked or modified, the revocation or modification applies to all years open under the statutes, unless the Commissioner or the Commissioner's delegate exercises the discretionary authority under section 7805(b) of the Code to limit the retroactive effect of the revocation or modification. The manner in which the authority generally is exercised is given later in this section. For information on rulings relating to the sale or lease of articles subject to the manufacturer's excise tax and the retailer's excise tax, see section 17.08.

.02 When determining a taxpayer's liability, the District Director must ascertain whether (1) any ruling previously issued to the taxpayer has been properly applied, (2) the representations upon which the ruling was based reflected an accurate statement of the material facts, and (3) the transaction actually was carried out substantially as proposed. If, in the course of determining the tax liability, the District director finds that a ruling should be modified or revoked, the findings and recommendations of the District Director will be forwarded to the National Office for consideration before further action. Such a referral to the National Office will be treated as a request for technical advice and the procedures of Rev. Proc. 86-2 will be followed. Otherwise the ruling is to be applied by the District Office in its determination of the taxpayer's liability.

.03 Appropriate coordination with the National Office will be undertaken if any field official having jurisdiction over a return or other matter proposes to reach a conclusion contrary to a ruling previously issued to the taxpayer.

.04 A ruling found to be in error or not in accord with the current views of the Service may be modified or revoked. Modification or revocation of a ruling may be made by (1) a notice to the taxpayer to whom the ruling was issued, (2) an enactment of legislation or ratification of a tax treaty, (3) a decision of the United States Supreme Court, (4) the issuing of temporary or final regulations, or (5) the issuing of a revenue ruling, a revenue procedure, or other statement published in the Internal Revenue Bulletin. Consistent with these provisions, if a ruling relates to a continuing action or a series of actions, the ruling will ordinarily be applied until any one of the actions described above has taken place, or until specifically withdrawn. Publication of a notice of proposed rulemaking will not affect the application of any ruling issued under the procedures stated in this revenue procedure.

.05 Except in rare or unusual circumstances, the revocation or modification of a ruling will not be applied retroactively to the taxpayer for whom the ruling was issued or to a taxpayer whose tax liability was directly involved in the ruling if (1) there has been no misstatement or omission of material facts, (2) the facts developed later are not materially different from the facts on which the ruling was based, (3) there has been no change in the applicable law, (4) the ruling was originally issued with respect to a prospective or proposed transaction, and (5) the taxpayer directly involved in the ruling acted in good faith in reliance upon the ruling and the retroactive revocation would be to the taxpayer's detriment. For example, the tax liability of each shareholder is directly involved in a ruling on the reorganization of a corporation. However, the tax liability of members of an industry is not directly involved in a ruling issued to one of the members, and the holding in a revocation or modification of a ruling to one member of an industry may be retroactively applied to other members of the industry. By the same reasoning, a tax practitioner may not obtain the nonretroactive application to one client of a modification or revocation of a ruling previously issued to another client. If a ruling is revoked by letter with retroactive effect, the letter will, except in fraud cases, state the grounds upon which the revocation is being made and the reasons why the revocation is being applied retroactively.

.06 A ruling issued on a particular transaction represents a holding of the Service on that transaction only. However, the application of that ruling to the transaction will not be affected by the later issuing of regulations (either temporary or final), if the conditions specified in section 17.05 are met. If the ruling is later found to be in error or no longer in accord with the position of the Service, it will not give the taxpayer protection for a like transaction in the same year or later year.

.07 However, if a ruling is issued covering a continuing action or a series of actions and it is determined that the ruling was in error, or no longer in accord with the position of the Service, the Associate Chief Counsel (Technical) ordinarily will limit the retroactivity of the revocation or modification to a date that is not earlier than that on which the ruling is modified or revoked. To illustrate, if a taxpayer receives a ruling that certain payments are excludable from gross income for federal income tax purposes and it is later determined that the ruling is in error or no longer in accord with the position of the Service, the Associate Chief Counsel (Technical) ordinarily will restrict the retroactive application of the revocation or modification of the ruling. If a taxpayer rendered service or provided a facility that is subject to the excise tax on services or facilities, and in reliance on a ruling issued to the same taxpayer did not pass the tax on to the user of the service of the facility, the Associate Chief Counsel (Technical) ordinarily will restrict the retroactive application of the revocation or modification of the ruling. If an employer incurred liability under the Federal Insurance Contributions Act, but in reliance on a ruling made to the same employer, neither collected the employee tax nor paid the employee and employer taxes under the Act, the Associate Chief Counsel (Technical) ordinarily will restrict the retroactive application of the revocation or modification of the ruling for both the employer tax and the employee tax. In the last situation, however, the restriction of retroactive application ordinarily will be conditioned on the furnishing by the employer of wage data, as may be required by section 31.6011(a)-1 of the Employment Tax Regulations.

.08 A ruling holding that the sale or lease of a particular article is subject to the manufacturer's excise tax or the retailer's excise tax may not retroactively revoke or modify an earlier ruling holding that the sale or lease of such an article was not taxable, if the taxpayer to whom the ruling was issued, in reliance upon the earlier ruling, parted with possession or ownership of the article without passing the tax on to the customer. Section 1108(b), Revenue Act of 1926.

.09 For rulings involving completed transactions, other than those described in sections 17.07 and 17.08, taxpayers will not be given the protection against retroactive revocation provided in section 17.05, since they will not have entered into the transactions in reliance on the ruling.

SEC. 18. EFFECT OF DETERMINATION LETTERS

A determination letter issued by a District Director has the same effect as a ruling issued to a taxpayer under section 17 of this revenue procedure. However, if the District Director is of the opinion that a conclusion contrary to that expressed in the determination letter is indicated, the matter need not be referred to the National Office. A District Director may not limit the modification or revocation of a determination letter but may refer the matter to the National Office for the possible exercise by the Commissioner of the Commissioner's delegate of the authority to limit the modification or revocation.

SEC. 19. EFFECT OF INFORMATION LETTERS

An information letter issued by the National Office or by a District Director is advisory only and the provisions of section 17 do not apply.

SEC. 20. PROCEDURE FOR REQUESTING APPLICATION OF SECTION 7805(b) IN THE CASE OF RULINGS AND DETERMINATION LETTERS

.01 Pursuant to section 7805(b) of the Code, it is within the discretion of the Commissioner or the Commissioner's delegate to prescribe the extent, if any, to which any ruling (including termination letters) will be applied without retroactive effect.

A taxpayer to whom a ruling or determination letter has been issued may request that the Associate Chief Counsel (Technical), the Commissioner's delegate, exercise the discretionary authority under section 7805(b) of the Code to limit the retroactive effect of any subsequent revocation or modification of the ruling or determination letter.

.02 In the case of a ruling, a request to limit the retroactive effect of the revocation or modification of a ruling must be in the form of, and meet the requirements for, a ruling request generally. These requirements are set forth in section 9 of this revenue procedure. Specifically, the request must state that it is being made pursuant to section 7805(b), contain a statement of the relief sought and an explanation of the reasons and arguments in support of the relief requested, and also be accompanied by any documents bearing on the request. The explanation in support of the application of section 7805(b) should include a discussion of the five items enumerated in section 17.05 of this revenue procedure as they relate to the taxpayer's particular situation.

A request for the application of section 7805(b) of the Code may take the form of a separate request for ruling when, for example, a revenue ruling has the effect of modifying or revoking a ruling previously issued to the taxpayer or when the Service notifies the taxpayer of a change in position that will have the effect of revoking or modifying such a ruling. However, when such notice is given by the District Director during the course of an examination of the taxpayer's return, or during consideration by the Chief, Appeals Office, a request to limit the retroactive effect of the modification or revocation of a ruling must be made in the form of a request for technical advice. See section 12.03 of Rev. Proc. 86-2. When germane to a pending ruling request, a request for the application of section 7805(b) may be made as part of the request, either initially or at any time before the ruling is issued. When a ruling that concerns a continuing transaction is modified or revoked by, for example, a subsequent revenue ruling, a request to limit the retroactive effect of the modification or revocation of the ruling must be made before the return is examined that contains the transaction that is the subject of the request for ruling.

.03 When a request for the application of section 7805(b) of the Code is made in a separate ruling request, the taxpayer has the right to a conference in the National Office in accordance with the provisions of section 11 of this revenue procedure. If the request is made initially as part of a pending ruling request or is made before the conference of right is held on the substantive issues, the section 7805(b) issue will be discussed at the taxpayer's one conference of right. (See section 11.05 of this revenue procedure). If the request for the application of section 7805(b) is made as part of a pending ruling request after a conference has been held on the substantive issue, and the Service determines that there is justification for having delayed the request, then the taxpayer will have the right to one conference of right concerning the application of section 7805(b) with the conference limited to discussion of this issue.

.04 In the case of a determination letter that the District Director proposes to modify or revoke, a request to limit the modification or revocation of the determination letter must be made by requesting the District Director who issued the determination letter to seek technical advice from the National Office, since a District Director has not been delegated authority under section 7805(b) of the Code to limit the modification or revocation of a determination letter. See section 12.03 of Rev. Proc. 85-2. The Taxpayer's request must state that it is being made pursuant to section 7805(b), contain a statement of the relief sought and an explanation of the reasons and arguments in support of the relief requested, and also be accompanied by any documents bearing on the request. The explanation in support of the application of section 7805(b) should include a discussion of the five items enumerated in section 17.05 of this revenue procedure as they relate to the taxpayer's particular situation.

.05 When technical advice is requested with respect to the application of section 7805(b) of the Code under the circumstances set forth in .04 above, the taxpayer has a right to a conference in the National Office to the same extent as does any taxpayer who is the subject of a technical advice request. See section 8 of Rev. Proc. 86-2.

SEC. 21. EFFECT OF OTHER DOCUMENTS

Rev. Proc. 85-1, as modified by Rev. Proc. 85-50 and as amplified by Rev. Proc. 85-57, is superseded.

26 CFR 601.105. Examination of returns and claims for refund, credit or abatement; determination of correct tax liability.

Rev. Proc. 86-2

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SECTION 1. PURPOSE

The purpose of this revenue procedure is to update Rev. Proc. 85-2, 1985-1 C.B. 452, which provides revised procedures for furnishing technical advice to District Directors and Chiefs, Appeals Offices, by the Associate Chief Counsel (Technical). It also tells taxpayers about their rights when a District Director or a Chief, Appeals office, requests such advice. Changes to this revenue procedure will be incorporated annually in a new revenue procedure published as the second revenue procedure of the year.

SEC. 2. SCOPE

.01 The Chief Counsel through the Associate Chief Counsel (Technical) provides principles and rules for uniformly interpreting and applying the federal tax laws under the jurisdiction of the Associate Chief Counsel (Technical). The procedures for obtaining technical advice specifically applicable to federal firearms, alcohol and tobacco taxes under subtitle E of the Internal Revenue Code are under the jurisdiction of the Bureau of Alcohol, Tobacco and Firearms. The procedures for obtaining technical advice specifically on employee plans and exempt organizations are under the jurisdiction of the Assistant Commissioner (Employee Plans and Exempt Organizations). See Rev. Proc. 80-26, 1980-1 C.B. 671. The procedures that apply to technical advice for employee plans and exempt organizations are followed in obtaining technical advice on exemption of farmers' cooperatives from tax under section 521 of the Code, even though the Associate Chief Counsel (Technical) has jurisdiction for issuing technical advice under this section. The Associate Chief Counsel (Technical) also has jurisdiction for issuing technical advice under section 526, on shipowners' protection and indemnity associations; section 527 (a), (b), (c), (d), (e), and (g), on political organizations; and section 528, on certain homeowners' associations, under this revenue procedure.

.02 In the Office of the Associate Chief Counsel (Technical), the authority to issue technical advice has been largely redelegated to the Branch Chiefs in the Individual Tax Division and the Corporation Tax Division.

SEC. 3. CHANGES

.01 A table of contents has been added to the beginning of this revenue procedure to assist taxpayers and Service personnel.

.02 Section 5.13 has been added to set forth the requirements for filing Form 2848 (Power of Attorney) with requests for technical advice.

SEC. 4. DEFINITIONS AND NATURE OF TECHNICAL ADVICE

.01 For purposes of this revenue procedure, the word "taxpayer" includes all persons subject to any provision of the Internal Revenue Code and, when appropriate, their representatives and issuers of section 103 obligations.

.02 Any reference to the National Office means only the Office of the Associate Chief Counsel (Technical).

.03 Any reference to District Director or District Office includes the office of the Director of the Foreign Operations District, where appropriate. Any reference to Chief, Appeals Office, includes Associate Chief, Appeals Office.

.04 "Technical advice" means advice or guidance furnished by the National Office upon requests of a District or an Appeals Office in response to any technical or procedural question that develops during any stage of any proceeding on the interpretation and proper application of tax law, tax treaties, regulations, revenue rulings, or other precedents published by the National Office to a specific set of facts. Such proceedings include (1) the examination of a taxpayer's return, (2) consideration of a taxpayer's claim for refund or credit, or (3) any other matter involving a specific taxpayer under the jurisdiction of the Chief, Examination Division, such as the consideration of a taxpayer's application to enter into an agreement about the useful life method, and rate of depreciation of business property provided by section 167(d) of the Code. These proceedings include an examination to determine whether obligations issued are described in section 103(a). They also include processing and considering nondocketed cases in an Appeals Office. Technical advice is furnished as a way of helping Service personnel close cases and establish and maintain consistent holdings throughout the Internal Revenue Service. A District Director or an Appeals Office may raise an issue in any tax period, even though technical advice may have been asked for and furnished for the same or a similar issue for another tax period. Technical advice does not include memoranda on matters of general technical application furnished to District or Appeals Offices when the issues are not raised in connection with a proceeding involving a specific taxpayer.

.05 If a District Director, Chief, Appeals Office, or a taxpayer requests technical advice on a determination letter under section 521 of the Code, the procedures under Rev. Proc. 80-26, 1980-1 C.B. 671, and Rev. Proc. 84-46, 1984-1 C.B. 541, as well as section 601.201(n) of the Statement of Procedural Rules must be followed.

.06 Only the National Office can revoke a ruling letter. Therefore, if a District Director or a Chief, Appeals Office, thinks that a ruling letter previously issued to a taxpayer should be modified or revoked, the procedures in section 5 of this revenue procedures must be followed.

.07 The provisions of this revenue procedure apply only to a case under the jurisdiction of a District director or Chief, Appeals Office. Technical advice may be requested on issues considered in a prior Appeals disposition, not based on mutual concessions for the same tax period of the same taxpayer, if the Appeals Office that had the case concurs in the request. A District Director may not request technical advice on an issue if an Appeals Office is currently considering an identical issue of the same taxpayer (or of a related taxpayer within the meaning of section 267 of the Code or a member of an affiliated group of which the taxpayer is also a member within the meaning of section 1504). A case remains under the jurisdiction of the District Director even though an Appeals Office has the identical issue under consideration in the case of another taxpayer (not related within the meaning of sections 267 and 1504, respectively) in an entirely different transaction. With respect to the same taxpayer or the same transaction, when the issue is under the jurisdiction of an Appeals Office, and the applicability of more than one kind of tax is dependent upon the resolution of that issue, a District Director may not request technical advice on the applicability of any of the taxes involved.

SEC. 5. REQUESTING TECHNICAL ADVICE

.01 The District of Appeals Office is responsible for determining whether to request technical advice on any issue being considered. Each request must be submitted through channels and signed by a person who is authorized to sign for the District Director or Chief, Appeals Office, and should include, in writing, the arguments submitted by the District or Appeals Office in support of its position on the issue or issues. All requests for technical advice from Appeals Offices should be submitted to Associate Chief Counsel (Technical) through the Director, Appeals Division, CC:AP:PT. However, while the case is under the jurisdiction of the District Director or the Chief, Appeals Office, a taxpayer may request that an issue be referred to the National Office for technical advice. All requests for technical advice should be made at the earliest possible stage of the proceedings. The grounds for a request are that a lack of uniformity exists on the disposition of the issue or that the issue is unusual or complex enough to warrant consideration by the National Office. Taxpayers may also request technical advice when seeking an extension of time fixed by regulations for making an election or application for relief pursuant to section 1.9100-1 of the Income Tax Regulations. See section 5.11 of this revenue procedure for additional information. Although taxpayers are encouraged to make written requests setting forth the facts, law, and argument on the issue, and reasons for requesting National Office technical advice, they may make the request orally. If, after considering the taxpayer's request, the examining officer or Appeals Officer thinks that the circumstances do not warrant referral of the case to the National Office, the examining officer or Appeals Officer will tell the taxpayer. (See section 6 for taxpayer's appeal rights when an examining officer or an Appeals Officer declines to request technical advice).

.02 When technical advice is going to be requested, whether or not on the request of the taxpayer, the taxpayer will be told about it and given a copy of the arguments submitted by the District Director or Chief, Appeals Office, in support of its position on the issue or issues, except as noted in section 5.10. If the examining officer or the Appeals Officer initiates the action, the Service will give the taxpayer a copy of the statement of the pertinent facts and the questions proposed for submission to the National Office. The request for technical advice should be worded to avoid possible misunderstanding in the National Office of the facts or the specific points at issue.

.03 If the Service initiates the request for technical advice, the taxpayer has 10 calendar days after receiving the statement of facts and specific questions to indicate in writing any disagreement about them. The taxpayer must justify in writing an extension of time beyond the 10 calendar days. The justification must be approved by the Chief, Examination Division, or the Chief, Appeals Office. Every effort should be made to reach agreement on the facts and the specific points at issue. If agreement cannot be reached, the taxpayer may send, within 10 calendar days after receipt of notice, a statement of the taxpayer's understanding of the new specific points at issue. This statement will be forward to the National Office with the request for technical advice. The taxpayer must justify in writing an extension of time beyond the 10 calendar days. The justification must be approved by the Chief, Examination Division, or the Chief, Appeals Office.

.04 If the taxpayer initiates the action to request technical advice and the taxpayer's statement of the facts and points at issue is not wholly acceptable to the District or Appeals Office, the Service will tell the taxpayer in writing what the areas of disagreement are. The taxpayer has 10 calendar days after receiving the written notice to reply to it. The taxpayer must justify in writing an extension of time beyond the 10 calendar days. The justification must be approved by the Chief, Examination Division or the Chief, Appeals Office. If agreement cannot be reached, both the statements of the taxpayer and the District or Appeals Office will be forwarded to the National Office with the request for technical advice.

.05 If it has not already been done, the taxpayer may submit a statement explaining the taxpayer's position on the issues and citing precedents that the taxpayer believes will bear on the case. This statement will be forwarded to the National Office with the request for technical advice. If the taxpayer's statement is received after the request for technical advice has been forwarded to the National Office, it will be forwarded there to be associated with the request for technical advice. The taxpayer is encouraged to comment on any legislation, tax treaties, regulations, revenue rulings, revenue procedures, or court decisions contrary to the taxpayer's position.

.06 At the time the taxpayer is told that the matter is being referred to the National Office, the taxpayer will also be told about the right to a conference in the National Office if an adverse decision is indicated and will be asked to say whether such a conference is desired.

.07 In connection with requests for technical advice, the taxpayer also has the same 10 days as in sections 5.03 and 5.04 to submit the statement described in section 5.09 of proposed deletions under section 6110(c) of the Code. If the taxpayer does not submit it, the District Director or the Chief, Appeals Office, will tell the taxpayer that such a statement is required. If the District Director or the Chief, Appeals Office, does not receive that statement within 10 days after such notification, the District Director or the Chief, Appeals Office, may decline to submit the request for technical advice. If the District Director or the Chief, Appeals Office, decides to request technical advice in a case in which the taxpayer has not submitted the statement of proposed deletions, the National Office will make those deletions that the Commissioner determines are required by section 6110(c).

.08 The requirements for submitting statements and other material for proposed deletions in technical advice memoranda before public inspection is allowed do not apply to requests for any documents to which section 6104 of the Code applies.

.09 To help the National Office make the deletions required by section 6110(c) of the Code in technical advice memoranda to be made open to public inspection under section 6110(a), a deletions statement must accompany requests. The statement must either state that no information other than names, addresses, and identifying numbers need be deleted, or if more information is proposed to be deleted, the statement must indicate the deletions proposed by the taxpayer. If the latter alternative is chosen, the statement must be made in a separate document, and it must be accompanied by a copy of all statements of facts and supporting documents that are submitted to the National Office under sections 5.03 and 5.04. The material that the taxpayer wants deleted must be shown in brackets. The statement of proposed deletions must show the statutory basis, under section 6110(c), for each proposed deletion. The statement of proposed deletions must not appear or be referred to anywhere in the request for technical advice. If the taxpayer decides to request additional deletions under section 6110(c) before the National Office replies to the request of technical advice, the taxpayer may submit additional statements. The procedures in this paragraph also apply to additional information submitted during consideration of the technical advice request.

.10 The provisions of this section (about referring issues upon the taxpayer's request, telling the taxpayer about the referral of issues, giving the taxpayer a copy of the arguments submitted by the District Director or Chief, Appeals Office, in support of its position on the issue or issues, submitting proposed deletions, and granting conferences in the National Office) do not apply to technical advice memoranda, described in section 6110(g)(5)(A) of the Code, on cases involving criminal or civil fraud investigations and jeopardy or termination assessments. However, in these cases the taxpayer may provide the statement of proposed deletions to the National Office after all proceedings in the investigations or assessments are complete but before the Commissioner mails the notice, under section 6110(f)(1), of intention to disclose the technical advice memorandum.

.11 See Rev. Proc. 79-63, 1979-2 C.B. 578, which concerns applications for extension of the time for making an election or application for relief pursuant to section 1.9100-1 of the Income Tax Regulations. If a taxpayer requests an extension of time under section 1.9100-1 during an examination or when being considered by an Appeals Office, the procedures of Rev. Proc. 86-2 are applicable, except for Sec. 6. The examination officer or Appeals Officer is not authorized to deny consideration of a request for technical advice that involves section 1.9100-1 relief. All such requests must be referred to the National Office. See section 4.03 of Rev. Proc. 79-63.

.12 Form 4463, Request for Technical Advice, should be used for transmitting requests for technical advice to the National Office.

.13 Any authorized representative, whether or not enrolled to practice, must comply with the conference and practice requirements of the Statement of Procedural Rules (26 CFR 601). Form 2848, Power of Attorney, and Form 2848-D, Authorization and Declaration, may be used with regard to requests for technical advice under this revenue procedure.

SEC. 6. APPEAL BY TAXPAYERS OF DISTRICT OR APPEALS OFFICE DETERMINATION NOT TO SEEK TECHNICAL ADVICE

.01 If the examining officer or Appeals Officer thinks that a taxpayer's request for referral of an issue to the National Office for technical advice does not warrant referral, the examining officer or Appeals Officer will tell the taxpayer.

.02 The taxpayer may appeal the decision of the examining officer or the Appeals Officer not to request technical advice by submitting to that official, within 10 calendar days after being told of the decision, a statement of the facts, law, and arguments on the issue, and the reasons why the taxpayer believes the matter should be referred to the National Office for technical advice. The taxpayer must justify in writing a request for an extension of time beyond the 10 calendar days. The justification must be approved by the Chief, Examination Division, or the Chief, Appeals Office.

.03 The examining officer or the Appeals Officer submits the taxpayer's statement through channels to the Chief, Examination Division, or the Chief, Appeals Office, along with the examining officer's or the Appeals Officer's statement of why the issue should not be referred to the National Office. The Chief determines, on the basis of the statement, whether technical advice will be requested. If the Chief determines that technical advice is not warranted and proposes to deny the request, the taxpayer is told in writing about the determination. In the letter to the taxpayer, the Chief states the reasons for the proposed denial (except in unusual situations when doing so would be prejudicial to the best interests of the Government). The taxpayer has 10 calendar days after receiving the letter to notify the Chief of agreement or disagreement with the proposed denial. The taxpayer may not appeal the decision of the Chief, Examination Division, or the Chief, Appeals Office, not to request technical advice from the National Office. However, if the taxpayer does not agree with the proposed denial, all data on the issue for which technical advice has been sought, including the taxpayer's written request and statements, will be submitted to the Assistant Commissioner (Examination) or the Director, Appeals Division, for review. If the Assistant Commissioner (Examination) or the Director, Appeals Division, thinks the circumstances warrant it, he or she may consult the Associate Chief Counsel (Technical) or his or her representatives. After this review, the District Office or the Appeals Office is notified whether the proposed denial is approved or disapproved.

.04 While the matter is being reviewed, the District Office or the Appeals Office suspends action on the issue (except when the delay would prejudice the Government's interest) until it is notified that the proposed denial is approved or disapproved. This notification is made within 30 calendar days after receipt of the data. The review is solely on the basis of the written record and no conference is held on the matter.

SEC. 7. WITHDRAWAL OF REQUESTS

.01 The District Director or Chief, Appeals Office, may withdraw a request for technical advice at any time before the responding transmittal memorandum is signed. The District Director or Chief, Appeals Office, must notify the taxpayer in writing of intent to withdraw the request for technical advice except (1) when the period of limitation on assessment is about to expire and the taxpayer has declined to sign a consent to extend the period, or (2) when such notification would be prejudicial to the best interests of the government. If the taxpayer does not agree that the request for technical advice should be withdrawn, the procedure in section 6 of this revenue procedure must be followed.

.02 When a request for technical advice is withdrawn, the National Office may send its views to the District Director or the Chief, Appeals Office, when acknowledging the withdrawal request. In an Appeals case, acknowledgment of the withdrawal request should be sent to the appropriate Appeals Office, through the Director, Appeals Division, CC:AP:PT. In appropriate cases, the subject matter may be published as a revenue ruling or as a revenue procedure.

SEC. 8. CONFERENCES IN THE NATIONAL OFFICE

.01 If after an analysis of the technical advice request it appears that advice adverse to the taxpayer will be given, and if a conference has been requested, the taxpayer will be told, by telephone if possible, the time and place of the conference. The conference must be held within 21 calendar days after such contact has been made. If conferences are being arranged for more than one request for technical advice for the same taxpayer, they will be scheduled to cause the least inconvenience to the taxpayer. An extension of the 21-day period will be granted only if the taxpayer justifies it in writing and the Chief or Assistant Chief of the technical branch to which the case is assigned approves it. Because the purpose of these procedures is to facilitate the technical advice process, requests for extensions should be justified by compelling facts and circumstances. The request for extension should be submitted before the end of the 21-day period. If unusual circumstances near the end of the 21-day period make a written request impractical, within the 21-day period the National Office should be told orally about the problem and of the forthcoming written request for extension. These requests must be promptly submitted. The taxpayer or taxpayer's representative will be told promptly and later in writing of the approval or denial of the requested extension. There is no right to appeal the denial of an extension request. If it is not advised of problems with meeting the 21-day period, or if the request is not sent promptly after the National Office is notified of problems with meeting the 21-day period, the Service will process the case on the basis of the existing record.

.02 A taxpayer is entitled by right to only one conference in the National Office unless one of the circumstances discussed in this section exists. This conference is normally held at the branch level in the appropriate division (Individual Tax Division or Corporation Tax Division) of the office of the Associate Chief Counsel (Technical). It is attended by a person who has authority to sign the transmittal memorandum discussed in section 9.07 on behalf of the Branch Chief. When more than one branch has taken an adverse position on an issue within its jurisdiction presented in a request for technical advice, or when the position ultimately adopted by one branch will affect another branch's determination, a representative from each branch with authority to sign for the Branch Chief will attend the conference. In appropriate cases, the examining officer or the Appeals Officer may also attend the conference to clarify the facts in the case. If more than one subject is discussed at the conference, the discussion constitutes a conference for each subject. To promote a free and open discussion of the issues, the conference usually is held after the branch has an opportunity to study the case. However, the taxpayer may request that the conference of right be held at a stage earlier in the consideration of the case than the Service would ordinarily designate. The taxpayer has no right to appeal the action of a branch to a Division Director or to any other official of the Service.

.03 Because conference procedures are informal, no tape, stenographic, or other verbatim recording of a conference is made.

.04 The senior Service representative at the conference ensures that the taxpayer has full opportunity to present views on all the issues in question. The Service representatives explain the Service's tentative decision on the substantive issues and the reasons for it. If prospective application under section 7805(b) of the Code is advanced by the taxpayer, the Service representative will discuss the tentative recommendation concerning the request for relief and the reason for the tentative recommendation. No commitment will be made as to the conclusion that the Service will finally adopt.

.05 An invitation to an individual conference is made if, after the conference of right, an adverse holding is proposed either (1) on a new issue or (2) on the same issue but on grounds different from those discussed at the first conference. When a proposed holding is reversed at a higher level with a result less favorable to the taxpayer, the taxpayer has no right to another conference if the grounds or arguments on which the reversal is based were discussed at the conference of right. The limitation on the number of conferences to which a taxpayer is entitled does not prevent inviting a taxpayer to attend further conferences when National Office personnel think they are necessary. These additional conferences are held only at the invitation of the National Office.

.06 The taxpayer is responsible for furnishing in writing to the National Office within 21 calendar days after the conference any additional data, line of reasoning, precedents, etc., that the taxpayer proposed and that were discussed at the conference but not previously or adequately presented in writing. An extension of the 21-day period may be granted only if the taxpayer justifies it in writing and the Chief or the Assistant Chief of the Technical branch to which the case is assigned approves it. Procedures for requesting an extension of the 21-day period and notifying the taxpayer or the taxpayer's representative of the Service's decision are the same as those in section 8.01. Any additional material should be submitted in duplicate to the National Office. If the additional information would have a significant impact on the facts in the request for technical advice, the National Office sends a copy to the District Director or the Chief, Appeals Office, for comment on the facts contained in the additional information submitted. The District Director or the Chief, Appeals Office, gives the matter prompt attention.

.07 A taxpayer must get information on the status of the request for technical advice by contacting the District or Appeals Office that requested the technical advice.

.08 A District Director or a Chief, Appeals Office, may get current information on the status of the request for technical advice by calling the person whose name and telephone number are shown on the acknowledgment of receipt of the request for technical advice.

SEC. 9. PREPARATION OF TECHNICAL ADVICE MEMORANDUM BY THE NATIONAL OFFICE

.01 As soon as the request for technical advice is assigned, the technical employee analyzes the file to see whether it meets all requirements of section 5. If it does not comply with the requirements of section 5.09 relating to the statement of proposed deletions, the National Office makes the deletions from the technical advice memorandum that the Commissioner determines are required by section 6110(c) of the Code.

.02 Usually, within 21 calendar days after the Branch Office receives the request for technical advice, a representative of the Branch telephones the District or Appeals Office to discuss the procedural and substantive issues in the request that come within the Branch's jurisdiction. The Branch representative informs the District or Appeals Office:

(a) that the case is being returned because substantial additional information is required to resolve an issue, because significant unresolved factual variances exist between the statements of facts submitted by the District or Appeals Office and the taxpayer, or because major procedural problems cannot be resolved by phone; or

(b) that the case is not being returned but more information is needed or minor procedural deficiencies exist; or

(c) what the Branch representative's tentative conclusion is and the estimated date that the technical advice memorandum will be mailed; or

(d) that a tentative conclusion has not been reached because of the complexity of the issue and the estimated date the tentative conclusion will be made.

.03 Within 21 calendar days after the Branch receives the additional information requested in section 9.02(b), the Branch representative telephones the District or Appeals Office to discuss the procedural and substantive issues in the request that come within the jurisdiction of the Branch. The representative indicates either (1) the tentative conclusion and the estimated date the technical advice memorandum will be mailed, or (2) the fact that a tentative conclusion has not been reached because of the complexity of the issue and the estimated date the tentative conclusion will be made.

.04 Because the Branch representative's tentative conclusion may change during the preparation and review of the technical advice memorandum, it is not, under any circumstances, considered final. The District or Appeals Office may not tell the taxpayer what the tentative conclusion is.

.05 When the technical advice request concerns matters within the jurisdiction of more than one Branch or more than one office in the same Branch, a representative of the Branch that received the original technical advice request informs the District or Appeals Office within the initial 21 calendar day period: (1) that the matters within the jurisdiction of another Branch or another office in the same Branch have been referred to the other Branch or office for consideration, and (2) that a representative of the other Branch or office will contact the District or Appeals Office about the referral of the technical advice request within 21 calendar days after receiving it in accordance with section 9.02.

.06 Generally, before replying to the request for technical advice, the National Office informs the taxpayer orally or in writing of the material likely to appear in the technical advice memorandum which the taxpayer proposed be deleted but which the Service determined should not be deleted. If so informed, the taxpayer may submit within 10 calendar days any further information, arguments, or other material that should be deleted. The Service attempts, if possible, to resolve all disagreements about proposed deletions before the National Office replies to the request for technical advice. However, the taxpayer does not have the right to a conference to resolve any disagreements about material to be deleted from the text of the technical advice memorandum. These matters, however, may be considered at any conference otherwise scheduled for the request.

.07 Replies to requests for technical advice are addressed to the District Director or the Chief, Appeals Office. When a request for technical advice is from Appeals, the response to the appropriate Appeals Office will be routed through the Director, Appeals Division, CC:AP:PT. The replies to technical advice requests are in two parts. Each part identifies the taxpayer by name, address, identification number, and year or years involved. The first part of the reply is a transmittal memorandum. In unusual cases it is a way of giving the District or Appeals Office administrative information or other information that under the nondisclosure statutes or for other reasons, may not be discussed with the taxpayer. The second part (the "technical advice memorandum") contains: (1) a statement of the issues; (2) a statement of the pertinent facts in the issues; (3) a statement of the pertinent law, tax treaties, regulations, revenue rulings and other precedents published in the Bulletin, and court decisions; (4) a discussion of the rationale developed by the National Office; and (5) the conclusions of the National Office. The conclusions give direct answers, whenever possible, to the specific questions of the District or Appeals Office. The discussion of the issues is in enough detail so the District or Appeals officials know the reasoning underlying the conclusion. Accompanying the technical advice memorandum is a notice, under section 6110(f)(1) of the Code, of intention to disclose a technical advice memorandum (including a copy of the version proposed to be open to public inspection and notations of third party communications under section 6110(d)). The District Director or the Chief, Appeals Office, forwards this notice to the taxpayer when the District Director or the Chief, Appeals Office gives a copy of the technical advice memorandum to the taxpayer according to section 9.08.

.08 The general practice of the Service is to give a copy of the technical advice memorandum to the taxpayer after it has been adopted by the District Director or the Chief Appeals Office. However, in the case of technical advice memoranda described in section 6110(g)(5)(A) of the Code, relating to cases involving criminal or civil fraud investigations and jeopardy or termination assessments, a copy of the technical advice memorandum is not given to the taxpayer until all proceedings in the investigations or assessments are completed.

.09 If after receiving the notice under section 6110(f)(1) of the Code of intention to disclose the technical advice memorandum the taxpayer wants to protest the disclosure of certain information in it, the taxpayer must submit a written statement within 20 calendar days identifying those deletions not made by the Service that the taxpayer believes should have been made. The taxpayer must also submit a copy of the version of the technical advice memorandum proposed to be open to public inspection with brackets around deletions that are proposed by the taxpayer but that have not been made by the National Office. Generally, the National Office does not consider the deletion of any material that the taxpayer has not proposed be deleted before the National Office reply is sent to the request for technical advice to the District Director or the Chief, Appeals Office. Within 20 days after it receives the taxpayer's response to the notice under section 6110(f)(1), the National Office must mail the taxpayer its final administrative conclusion about the deletions to be made.

SEC. 10. ACTION ON TECHNICAL ADVICE IN DISTRICT AND APPEALS OFFICES

.01 The District Director or the Chief, Appeals Office, processes the taxpayer's case on the basis of the conclusions in the technical advice memorandum unless (1) the District Director or the Chief, Appeals Office, thinks that the conclusions reached by the National Office in a technical advice memorandum should be reconsidered, or (2) the Chief, Appeals Office, in the case of technical advice unfavorable to the taxpayer, decides to settle the issue in the usual manner under existing authority.

.02 The District Director or the Chief, Appeals Office, gives the taxpayer (1) a copy of the technical advice memorandum described in section 9.07, and (2) the notice under section 6110(f)(1) of the Code of intention to disclose the technical advice memorandum (including a copy of the version proposed to be open to public inspection and notations of third party communications under section 6110(d)). This requirement does not apply to technical advice memoranda involving civil fraud or criminal investigations; jeopardy or termination assessments, as described in section 5.10; or documents to which section 6104 applies.

.03 In those cases in which the National Office tells the District Director or the Chief, Appeals Office, that a copy of the technical advice memorandum should not be given to the taxpayer, the District Director or the Chief, Appeals Office tells this to the taxpayer if the taxpayer requests a copy.

SEC. 11. EFFECT OF TECHNICAL ADVICE

.01 Except in rare or unusual circumstances, a holding in a technical advice memorandum that is favorable to the taxpayer is applied retroactively. Moreover, since technical advice, as described in section 4.04 of this revenue procedure, is issued only on closed transactions, a holding that is adverse to the taxpayer is also applied retroactively unless the Associate Chief Counsel (Technical) exercises the discretionary authority under section 7805(b) of the Code to limit the retroactive effect of the holding.

.02 A holding that modifies or revokes a holding in a prior technical advice memorandum is applied retroactively, with one exception. If the new holding is less favorable to the taxpayer than the earlier one, it generally is not applied to the period in which the taxpayer relied on the prior holding in situations involving continuing transactions.

.03 If a technical advice memorandum relates to a continuing action or a series of actions, it is ordinarily applied until specifically withdrawn or until the conclusion is modified or revoked by enactment of legislation, ratification of a tax treaty, or issuance of a United States Supreme Court decision, regulations (temporary or final), a revenue ruling, or other statement published in the Internal Revenue Bulletin. Publication of a notice of proposed rulemaking does not affect the application of a technical advice memorandum.

.04 Generally, a technical advice memorandum that revokes or modifies a letter ruling or another technical advice memorandum is not applied retroactively for either the taxpayer to whom or for whom the ruling or memorandum was originally issued or for a taxpayer whose tax liability was directly involved in such ruling or memorandum if: (1) there has been no misstatement or omission of material facts; (2) the facts later developed are not materially different from the facts on which the ruling or memorandum was based; (3) there has been no change in the applicable law; (4) the ruling was originally issued for a prospective or proposed transaction; and (5) the taxpayer directly involved in the ruling or memorandum acted in good faith in relying on the ruling or memorandum and the retroactive revocation would be to the taxpayer's detriment. The tax liabilities of members of an industry are not directly affected by a ruling or a memorandum issued to or for one of the members. The holding in a revocation or modification of a ruling or a memorandum to or for one member of an industry may be retroactively applied to other members of that industry. A tax practitioner may not obtain the nonretroactive application for one client. When a ruling to a taxpayer or a memorandum involving a taxpayer is revoked with retroactive effect, the notice to the taxpayer, except in fraud cases, sets forth the grounds on which the revocation is being made and the reasons why the revocation is being applied retroactively.

SEC. 12. PROCEDURES FOR REQUESTING APPLICATION OF SECTION 7805(b) IN THE CASE OF TECHNICAL ADVICE

.01 Pursuant to section 7805(b) of the Code, it is within the discretion of the Commissioner or the Commissioner's delegate to prescribe the extent, if any, to which any ruling (including technical advice) will be applied without retroactive effect.

A taxpayer to whom a technical advice memorandum has been addressed or with respect to whom a technical advice request is pending may request that the Associate Chief Counsel (Technical), the Commissioner's delegate, exercise the discretionary authority under section 7805(b) of the Code to limit the retroactive effect of any holding stated in the technical advice memorandum or to limit the retroactive effect of any subsequent modification or revocation of the technical advice memorandum.

.02 When a technical advice memorandum that concerns a continuing transaction is modified or revoked by, for example, a subsequent revenue ruling or final regulations, a request to limit the retroactive effect of the modification or revocation of the technical advice memorandum must be made in the form of a request for a ruling when the request is submitted before the return is examined that contains the transaction that is the subject of the request for ruling. See section 20.02 of Rev. Proc. 86-1, page 6, this Bulletin.

.03 When a taxpayer is informed of the modification or revocation of a technical advice memorandum, ruling letter, or determination letter during the course of an examination of the taxpayer's return by the District Director or during consideration by the Chief, Appeals Office, a request to limit the retroactive application of the modification or revocation of the technical advice memorandum, ruling letter, or determination letter must itself be made in the form of a request for technical advice. See section 5 of this revenue procedure. However, the taxpayer must also submit a statement, which will be forwarded to the National Office with the request for technical advice, that the request for technical advice is being made pursuant to section 7805(b) of the Code. This statement must also set for the relief sought and an explanation of the reasons and arguments in support of the relief requested, and it must be accompanied by any documents bearing on the request. The explanation in support of the application of section 7805(b) should include a discussion of the five items enumerated in section 11.04 of this revenue procedure as they relate to the taxpayer's particular situation.

.04 A request to limit the retroactive effect of a holding in a technical advice memorandum that does not modify or revoke a technical advice memorandum may be made as part of that technical advice request, either initially, or at any time before the technical advice memorandum is issued by the National Office. In such a case, the taxpayer must also submit a statement in support of the application of section 7805(b) of the Code, as described in .03 above.

.05 When a request for technical advice concerns only the application of section 7805(b) of the Code, the taxpayer has the right to a conference in the National Office in accordance with the provisions of section 8 of this revenue procedure. If the request for application of section 7805(b) is included in the request for technical advice on the substantive issues or is made before the conference of right on the substantive issues, the section 7805(b) issue will be discussed at the taxpayer's one conference of right. If the request for the application of section 7805(b) is made as part of a pending technical advice request after a conference has been held on the substantive issue, and the Service determines that there is justification for having delayed the request, then the taxpayer will have the right to one conference of right concerning the application of section 7805(b) with the conference limited to discussion of this issue.

SEC. 13 EFFECT ON OTHER DOCUMENTS

Rev. Proc. 85-2 is superseded.

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26 CFR 601.201: Rulings and determination letters.

Rev. Proc. 86-3

SECTION 1. PURPOSE AND NATURE OF CHANGES

.01 The purpose of this revenue procedure is to update Rev. Proc. 85-22, 1985-1 C.B. 550, as amplified and modified by subsequent revenue procedures, by providing a revised list of those areas of the Internal Revenue Code under the jurisdiction of the Associate Chief Counsel (Technical) in which the Internal Revenue Service will not issue advance rulings or determination letters.

.02 Changes

1 New section 3.0133 refers to section 871. See Rev. Proc. 85-59, 1985-50 I.R.B. 16.

2 New section 3.0134 refers to section 956. See Rev. Proc. 85-59, 1985-50 I.R.B. 16.

3 New section 4.014 refers to section 103. See Rev. Proc. 85-28, 1985-1 C.B. 581.

4 New section 5.13 refers to sections 331, 337, 453, and 1239. See Rev. Proc. 85-24, 1985-1 C.B. 558.

5 Old Sections 5.19 and 5.31 have been deleted. See Rev. Proc. 85-34, 1985-29 I.R.B. 13, and Rev. Proc. 85-27, 1985-1 C.B. 580.

SEC. 2. BACKGROUND AND SCOPE OF APPLICATION

.01 Background

Whenever appropriate in the interest of sound tax administration, it is the policy of the Service to answer inquiries of individuals and organizations regarding their status for tax purposes and the tax effects of their acts or transactions, prior to the filing of returns or reports that are required by the revenue laws.

There are, however, certain areas in which, because of the inherently factual nature of the problems involved, or for other reasons, the Service will not issue advance rulings or determination letters. These areas are set forth in three sections of this revenue procedure. Section 3 reflects those areas in which advance rulings and determinations will not be issued. Section 4 sets forth those areas in which they will not ordinarily be issued. "Not ordinarily" connotes that unique and compelling reasons must be demonstrated to justify a ruling or determination letter. Those sections reflect a number of specific questions and problems as well as general areas. Section 5 lists specific areas for which the Service is temporarily not issuing advance rulings and determinations because those matters are under extensive study.

With respect to the items listed, revenue rulings or revenue procedures may be published in the Internal Revenue Bulletin from time to time to provide general guidelines regarding the position of the Service.

Additions or deletions to this revenue procedure as well as restatement of items listed will be made by modification of this revenue procedure. Changes will be published as they occur throughout the year and will be incorporated annually in a new revenue procedure published as the third revenue procedure of the year. These lists should not be considered all inclusive. Decisions not to rule on individual cases, as contrasted with those that present significant pattern issues, are not reported in this revenue procedure and will not be added to subsequent revisions.

The authority and general procedures of the Technical Function of the National Office of the Internal Revenue Service or the Offices of the District Directors of the Internal Revenue with respect to the issuance of advance rulings and determination letters with respect to Code sections under the jurisdiction of the Associate Chief Counsel (Technical) are outlined in Rev. Proc. 86-1, page 6, this Bulletin.

.02 Scope of Application.

This revenue procedure is not to be considered as precluding the submission of requests for technical advice to the National Office from the Office of a District Director of the Internal Revenue or a Chief, Appeals Office.

SEC. 3. AREAS IN WHICH RULINGS OR DETERMINATION LETTERS WILL NOT BE ISSUED

.01 Specific questions and problems.

1 Section 79.—Group Term Life Insurance Purchased for Employees.—Whether a group insurance plan for 10 or more employees qualifies as group-term insurance if the amount of insurance is not computed under a formula that would meet the requirements of section 1.79-1(c)(2)(ii) if the group consisted of fewer than 10 employees.

2 Section 83.—Property Transferred in Connection with Performance of Services.—Whether a restriction constitutes a substantial risk of forfeiture if the employee is a controlling shareholder. Also, whether a transfer has occurred if the amount paid for a purported transfer of property involves a nonrecourse obligation.

3 Section 105(h).—Amount Paid to Highly Compensated Individuals under a Discriminatory Self-Insurance Medical Expense Reimbursement Plan.—Whether, following a determination that a self-insured medical expense reimbursement plan is discriminatory, that plan had previously made reasonable efforts to comply with tax discrimination rules.

4 Section 117.—Scholarships and Fellowship Grants.—Whether an employer-related scholarship or fellowship grant is excludable from the employee's gross income if there is no intermediary private foundation distributing the grants, as there was in Rev. Proc. 76-47, 1976-2 C.B. 670.

5 Section 119.—Meals or Lodging Furnished for the Convenience of the Employer.—Whether the value of meals or lodging is excludable from gross income by an employee who is a controlling shareholder of the employer.

6 Sections 121 and 1034.—One-Time Exclusion of Gain from Sale of Principal Residence by Individual Who Has Attained Age 55; Rollover of Gain on Sale of Principal Residence.—Whether property qualifies as the taxpayer's principal residence.

7 Section 162.—Trade or Business Expenses.—Whether compensation is reasonable in amount.

8 Section 163.—Interest.—The income tax consequences of transactions involving 'shared appreciation mortgage" (SAM) loans in which a taxpayer, borrowing money to purchase real property, pays a fixed rate of interest on the mortgage loan below the prevailing market rate and will also pay the lender a percentage of the appreciation in value of the real property upon termination of the mortgage. This applies to all SAM arrangements where the loan proceeds are used for commercial or business activities, or where used to finance a personal residence if the facts are not similar to those described in Rev. Rul. 83-51, 1983-1 C.B. 48. (Also sections 61, 451, 461, 856, 1001, and 7701).

9 Section 170.—Charitable, Etc., Contributions and Gifts.—Whether a charitable lead interest qualifies as a guaranteed annuity interest for purposes of section 170(f)(2)(B) of the Code if that interest may be prepaid before the expiration of the specified term of that interest or before the death of the life or lives used to measure the term of such interest.

10 Section 170.—Charitable, Etc., Contributions and Gifts.—Whether a taxpayer who advances funds to a charitable organization and receives therefor a promissory note may deduct as contributions, in one taxable year or in each of several years, amounts forgiven by the taxpayer in each of several years by endorsement on the note.

11 Section 213(a).—Medical, Dental, Etc., Expenses.—Whether a capital expenditure for an item that is ordinarily used for personal, living, or family purposes, such as a swimming pool, has as its primary purpose the medical care of the taxpayer or the taxpayer's spouse or dependent, or is related directly to such medical care.

12 Section 264(b).—Certain Amounts Paid in Connection with Insurance contracts.—Whether "substantially all" the premiums of a contract of insurance are paid within a period of 4 years from the date on which the contract is purchased. Also, whether an amount deposited is in payment of a "substantial number" of future premiums on such a contract.

13 Section 264(c)(1).—Certain Amounts Paid in Connection with Insurance Contracts.—Whether section 264(c)(1) of the Code applies.

14 Section 269.—Acquisitions Made to Evade or Avoid Income Tax.—Whether an acquisition is within the meaning of section 269 of the Code.

15 Section 274.—Disallowance of Certain Entertainment, Etc., Expenses.—Whether a taxpayer who is traveling away from home on business may, in lieu of substantiating the actual cost of meals, deduct a fixed per-day amount for meal expenses that differs from the amount prescribed in Rev. Proc. 83-71, 1983-2 C.B. 590, or any later revenue procedure that modifies Rev. Proc. 83-71.

16 Section 302.—Distributions in Redemption of Stock.—Whether section 302(b) of the Code applies when the consideration given in redemption by a corporation consists entirely or partly of its notes payable, and the shareholder's stock is held in escrow or as security for payment of the notes with the possibility that the stock may or will be returned to the shareholder in the future, upon the happening of specified defaults by the corporation.

17 Section 302.—Distributions in Redemption of Stock.—Whether section 302(b) of the Code applies when the consideration given in redemption by a corporation in exchange for a shareholder's stock consists entirely or

partly of the corporation's promise to pay an amount based on, or contingent on, future earnings of the corporation, when the promise to pay is contingent on working capital being maintained at a certain level, or any other similar contingency.

18 Section 302.—Distributions in Redemption of Stock.—Whether section 342(b) of the Code applies to a redemption of stock if after the redemption the distributing corporation uses property that is owned by the shareholder from whom the stock is redeemed and the payments by the corporation for the use of the property are dependent upon the corporation's future earnings or are subordinate to the claims of the corporation's general creditors. Payments for the use of property will not be considered to be dependent upon future earnings merely because they are based on a fixed percentage of receipts or sales.

19 Section 302.—Distributions in Redemption of Stock.—Whether the acquisition or disposition of stock described in section 302(c)(2)(B) of the Code has, or did not have, as one of its principal purposes the avoidance of federal income taxes within the meaning of that section, unless the facts and circumstances are materially identical to those set forth in Rev. Rul. 56-556, 1956-2 C.B. 177, Rev. Rul. 56-584, 1956-2 C.B. 179, Rev. Rul. 57-387, 1957-2 C.B. 225, Rev. Rul. 77-293, 1977-2 C.B. 91, Rev. Rul. 79-67, 1979-1 C.B. 128, or Rev. Rul. 85-19 1985-1 C.B. 94.

20 Section 302(b)(4) and (e) (pre-TEFRA sections 346(a)(2) and (b)).—Partial Liquidation.—The amount of working capital attributable to a business or portion of a business terminated that may be distributed in partial liquidation.

21 Sections 311 and 336.—Taxability of Corporation on Distribution; General Rule.—Upon distribution of property in kind by a corporation to its shareholders, in complete liquidation under section 331 of the Code (when under the facts a sale of the property by the corporation would not qualify under section 337) and section 346(a) (pre-TEFRA section 346(a)(1)), in partial liquidation under section 302(b)(4) and (e) (Pre-TEFRA sections 346(a)(2) an (b)) or in redemption of stock under section 302(a), followed by a sale of the property, whether the sale can be deemed to have been made by the corporation under the doctrine of *Commissioner v. Court Holding Company*, 324 U.S. 331 (1945), 1945 C.B. 58.

22 Section 312.—Effect on Earnings and Profits.—The determination of the amount of earnings and profits of a corporation.

23 Section 368(a)(1)(B).—Definitions Relating to Corporate Reorganizations.—The acceptability of an estimation procedure or the acceptability of a specific sampling procedure to determine the basis of stock acquired by an acquiring corporation in a reorganization described in section 368(a)(1)(B).

24 Section 368(a)(1)(E).—Definitions Relating to Corporate Reorganizations.—Whether a transaction constitutes a corporate recapitalization within the meaning of section 368(a)(1)(E) of the Code (or a transaction that also qualifies under section 1036) except when the recapitalization is an integral part of a larger transaction and it is impossible to determine the tax consequences of the larger transaction without making a determination with regard to the recapitalization.

25 Section 451.—General Rule for Taxable Year of Inclusion.—The tax consequences of a nonqualified unfunded deferred compensation arrangement with respect to a controlling shareholder employee eligible to participate in the arrangement.

26 Sections 451 and 457.—General Rule for Taxable Year of Inclusion; Deferred Compensation Plans with Respect to Service for State and Local Governments.—The tax consequences to unidentified independent contractors in nonqualified unfunded deferred compensation plans. This applies to plans established under section 451 of the Code by employers in the private sector and to eligible state plans under section 457. However, a ruling with respect to a specific independent contractor's participation in such a plan may be issued.

27 Section 453.—Revolving Credit Sales as Installment Sales.—Whether a proposed sampling procedure will be acceptable by the Service for the purpose of determining the portion of revolving credit balances to be treated as installment account balances. See Rev. Proc. 64-4, 1964-1 (Part 1) C.B. 644, and Rev. Proc. 65-5, 1965-1 C.B. 720.

28 Section 641.—Imposition of Tax.—Whether the period of administration or settlement of an estate is reasonable or unduly prolonged.

29 Section 642(c).—Deduction for Amounts Paid or Permanently Set Aside for a Chargeable Purpose.—Allowance of an unlimited deduction for amounts set aside by a trust or estate for charitable purposes when there is a possibility that the corpus of the trust or estate may be invaded.

30 Section 704(b)(2).—Partner's Distributive Share Determined.—Whether the allocation to a partner under the partnership agreement of income, gain, loss, deduction, or credit (or an item thereof) has substantial economic effect.

31 Section 704(e).—Family Partnerships.—Matters relating to the validity of a family partnership when capital is not a material income producing factor.

32 Section 856.—Definition of a Real Estate Investment Trust.—Whether a corporation whose stock is "paired" with or "stapled" to stock of another corporation will qualify as a real estate investment trust under section 856 of the Code if the activities of the corporations are integrated.

33 Section 871(g)(1)(B).—Original Issue Discount Obligations.—Whether a debt instrument having original issue discount within the meaning of section 1273 is not an original issue discount obligation within the meaning of section 871(g)(1)(B)(i) when the instrument is payable 183 days or less from the date of original issue (without regard to the period held by the taxpayer) and such debt instrument is issued by a domestic corporation and is purchased by its controlled foreign corporation.

34 Section 956(b)(1)(C).—United States Property Defined.—Whether an indebtedness is excludable from the definition of the term "obligation" under section 1.956-2(d)(2)(ii) of the regulations because the indebtedness is collected within one year from the time it is incurred or matures within one year from the time it is incurred but is not collected within such period solely by reason of the inability or unwillingness of the debtor to make payment within such period.

35 Section 1221.—Capital Asset Defined.—Whether specialty stock al-

located to an investment account by a registered specialist on a national securities exchange is a capital asset.

36 Section 1551.—Disallowance of Surtax Exemption and Accumulated Earnings Credit.—Whether a transfer is within section 1551 of the Code.

37 Section 2031.—Definition of Gross Estate.—Actuarial factors for valuing interests in the prospective gross estate of a living person.

38 Section 2055.—Transfers for Public, Charitable and Religious Uses.—Whether a charitable lead interest qualifies as a guaranteed annuity interest for purposes of section 2055(e)(2)(b) of the Code if that interest may be prepaid before the expiration of the specified term of that interest or before the death of the life or lives used to measure the term of such interest.

39 Section 2512.—Valuation of Gifts.—Actuarial factors for valuing prospective or hypothetical gifts of a donor.

40 Section 2522.—Charitable and Similar Gifts.—Whether a charitable lead interest qualifies as a guaranteed annuity interest for purposes of section 2522(c)(2)(B) of the Code if that interest may be prepaid before the expiration of the specified term of that interest or before the death of the life or lives used to measure the term of such interest.

41 Section 7701.—Definitions.—Whether a foreign arrangement that is a participant in a domestic arrangement classified as a partnership for U.S. tax purposes will itself be classified as a partnership.

42 Section 7701.—Definitions.—Whether a foreign limited liability company will be classified as a partnership if the taxpayer requests classification as a partnership and (1) the taxpayer is a corporation and less than 20 percent of the interests in the limited liability company are held by independent parties or (2) the taxpayer is not a corporation and independent parties hold only a nominal interest in the company.

43 Section 7701.—Definitions.—Whether an organization, formed in a state that has a statute corresponding to the Uniform Limited Partnership Act or the Revised Uniform Limited Partnership Act, lacks the corporate characteristic of continuity of life where, in the case of the removal of a general partner, the partnership agreement allows less than a majority in interest of limited partners to elect a new one to continue the partnership.

44 Section 7701.—Definitions.—Whether a limited partnership will be classified as a partnership if the partnership agreement does not provide that, notwithstanding anything to the contrary that may be expressed or implied in the agreement, the interests of all of the general partners, taken together, in each material item of partnership income, gain, loss, deduction, or credit is equal to at least one percent of each such item at all times during the existence of the partnership. In determining the general partners' interests in such items, limited partnership interests owned by the general partners shall not be taken into account.

45 Section 7701.—Definitions.—Whether a limited partnership will be classified as a partnership if the partnership agreement does not expressly provide that, upon the dissolution and termination of the partnership, the general partners will contribute to the partnership an amount equal to: (a) the deficit balances in their capital accounts; or (b) the excess of 1.01 percent of the total capital contributions of the limited partners over the capital previously contributed by the general partners; or (c) the lesser of (a) or (b).

.02 General Areas

1 The results of transactions that lack bona fide business purpose or have as their principal purpose the reduction of federal taxes.

2 A matter upon which a court decision adverse to the government has been handed down and the question of following the decision or litigating further has not yet been resolved.

3 A matter involving the prospective application of the estate tax to the property or the estate of a living person.

4 A matter involving alternate plans of proposed transactions or involving hypothetical situations.

5 A matter involving the federal tax consequences of any proposed federal, state, local or municipal legislation. The Service may provide general information in response to an inquiry.

6 Whether reasonable cause exists under Subtitle F (Procedure and Administration) of the Code.

7 Whether a proposed transaction would subject the taxpayer to a criminal penalty.

8 A request that does not comply with the provisions of Rev. Proc. 86-1.

9. Whether, under the common law rules applicable in determining the employer-employee relationship, a professional staffing corporation (loan-out corporation) or the subscriber is the employer of individuals if:

(a) the loan-out corporation hires employees of the subscriber and assigns the employees back to the subscriber or;

(b) the loan-out corporation assigns individuals to subscribers for more than a temporary period (1 year or longer).

SEC. 4. AREAS IN WHICH RULINGS OR DETERMINATION LETTERS WILL NOT ORDINARILY BE ISSUED

.01 Specific questions and problems.

1 Sections 38, 39, 46, and 48.—Investment Tax Credit.—Application of these sections where the formal ownership of property is in a party other than the taxpayer, except when title is held merely as security.

2 Section 61.—Gross Income Defined.—Determination as to who is the true owner of property in cases involving the sale of securities, or participation interests therein, where the purchaser has the contractual right to cause the security, or participation interest therein, to be purchased by either the seller or a third party.

3 Sections 61 and 163.—Gross Income Defined; Interest.—Determinations as to who is the true owner of property or the true borrower of money in cases in which the formal ownership of the property or liability for the indebtedness is in another party.

4 Section 103.—Interest on Certain Governmental Obligations.—Whether the interest on state and local governmental obligations will be excludable from gross income under section 103(a) of the Internal Revenue Code if the proceeds of issues of obligations (other than advance refunding issues) are placed in escrow or otherwise not expended for a governmental purpose for an extended period of time even though the proceeds are invested at a yield that will not exceed the yield on the governmental obligations prior to their expenditure.

5 Section 103.—Interest on Certain Governmental Obligations.—Whether municipal bonds will meet the "security interest test" under section 103(b)(2)(B)

of the Code and section 1.103-7(b)(4) of the regulations because an underlying arrangement is inferred, as illustrated in Rev. Rul. 80-251, 1980-2 C.B. 40, and Rev. Rul. 80-339, 1980-2 C.B. 42, when payments not pledged as security for the bonds are received in respect of the bond-financed property used in the trade or business of nonexempt persons in an amount equal to more than 25 percent of the principal or interest payments on the bonds.

6 Section 103.—Interest on Certain Governmental Obligations.—Whether an issue of industrial development bonds is exempt under section 103(b) of the Code when 10 percent or more of the proceeds of the issue (minus "neutral costs," as described in Rev. Rul. 80-171, 1980-2 C.B. 44) are used to finance a facility in what an owner (or a related person) or a lessee (or a related person), who was a user of the facility at any time before the bonds were issued, will be a user of the facility after the bonds are issued.

7 Section 103.—Interest on Certain Governmental Obligations.—Whether amounts received as proceeds from the sale of municipal bond financed property and pledged to the payment of debt service or pledged as collateral for the municipal bond issue are sinking fund proceeds within the meaning of section 1.103-13(g) of the Income Tax Regulations or replaced proceeds described in section 103(c)(2)(B) of the Internal Revenue Code.

8 Section 162.—Trade or Business Expenses.—Whether the requisite risk shifting and risk distribution necessary to constitute insurance are present for purposes of determining the deductibility under section 162 of amounts paid (premiums) by a taxpayer for insurance, unless the facts of the transaction are within the scope of Rev. Rul. 77-316, 1977-2 C.B. 53, or Rev. Rul. 78-338, 1978-2 C.B. 107.

9 Section 167.—Depreciation.

(a) Useful lives of assets.

(b) Depreciation rates.

(c) Salvage value of assets.

10 Sections 167 and 168.—Depreciation; Accelerated Cost Recovery System.—Application of these sections where the formal ownership of property is in a party other than the taxpayer, except when title is held merely as security.

11 Section 170(c).—Charitable, etc., Contributions and Gifts.—Whether a taxpayer who transfers property to a charitable organization and thereafter leases back all or a portion of the transferred property, may deduct the fair market value of the property transferred and leased back as a charitable contribution.

12 Section 302.—Distribution in Redemption of Stock.—The tax effect of the redemption of stock for notes, when the payments on the notes are to be made over a period in excess of 15 years from the date of issuance of such notes.

13 Section 302(b)(4) and (e)(pre-TEFRA section 346(a)(2)).—Partial Liquidation.—Whether a distribution will qualify as a distribution in partial liquidation under section 302(b)(4) and (e)(1)(A) (pre-TEFRA section 346(a)(2)) of the Code unless it results in a 20 percent or greater reduction in (1) gross revenue, (2) net fair market value of assets, and (3) employees.

14 Sections 302(b)(4) and (e) (Pre-TEFRA sections 346(a)(2) and (b)), 331, 332, 333 and section 346(a) (Pre-TEFRA section 346(a)(1)).—Effects on Recipients of Distributions in Corporate Liquidations.—The tax effect of the liquidation of a corporation preceded or followed by the reincorporation of all or a part of the business and assets when more than a nominal amount of the stock (that is, more than 20 percent in value) of both the liquidating corporation and the transferee corporation is owned by the same shareholders; or when a liquidation is followed by the sales of the corporate assets by the shareholders to another corporation in which such shareholders own more than a nominal amount of the stock (that is, more than 20 percent in value).

15 Section 306.—Disposition of Certain Stock.—Whether the distribution or disposition or redemption of "section 306 stock" in a closely held corporation is in pursuance of a plan having as one of its principal purposes the avoidance of federal income taxes within the meaning of section 306(b)(4) of the Code.

16 Sections 331 and 346(a).—Gain or Loss to Shareholders in Corporate Liquidations.—The tax effect of the liquidation of a corporation by a series of distributions, when the distributions in liquidation are to be made over a period in excess of 3 years from the adoption of the plan of liquidation.

17 Section 337.—Gain or Loss; Certain Liquidations.—The application of this section to a corporation upon the sale of property, in connection with its liquidation, to another corporation, when more than a nominal amount of the stock (that is, more than 20 percent in value) of both the selling corporation and the purchasing corporation is owned by the same persons.

18 Section 341.—Collapsible Corporations.—Whether a corporation will be considered to be a "collapsible corporation," that is, whether it was "formed or availed of" with the view of certain tax consequences. However, ruling requests will be considered on this matter when the enterprise (1) has been in existence for at least 20 years or has clearly demonstrated that it has realized two-thirds of the taxable income to be derived from the manufacturing, constructing, producing, or purchasing of property as stated in section 341(b)(1)(A) of the Code and as described in Rev. Rul. 72-48, 1972-1 C.B. 102, (2) has had an aggregate change in the shareholders' interests of not more than 10 percent during that period (except for transfers among family members, as defined in section 267(c)(4), or redemptions of stock to pay death taxes pursuant to section 303), and (3) has conducted substantially the same trade or business during that period. The period referred to in (2)and (3) above is the lesser of 20 years of corporate existence or the period in which the enterprise has realized two-thirds of the taxable income from activities specified in section 341(b)(1)(A).

19 Section 351.—Transfers to Controlled Corporation.—The tax effect of the transfer when part of the consideration received by the transferors consists of bonds, debentures, or any other evidence of indebtedness of the transferee and the term of the "indebtedness" is either less than 10 years or a determination as to whether the "indebtedness" is properly classified as debt or equity is required in order to establish that the requirements of section 351 are met.

20 Section 355.—Distribution of Stock and Securities of a Controlled Corporation.—Whether the active business requirement of section 355(b) of the Code is met when, within the 5-year period described in section

1355(b)(2)(B), a distributing corporation acquired control of a controlled corporation as a result of the distributing corporation transferring cash or other liquid or inactive assets to the controlled corporation in a transaction in which gain or loss was not recognized as a result of the transfer meeting the requirements of section 351(a) or 368(a)(1)(D).

21 Section 816.—Definition of Life Insurance Company.—Whether the requisite risk shifting and risk distribution necessary to constitute insurance are present for purposes of determining if a company is an "insurance company" under section 1.801-3(a) of the regulations, unless the facts of the transaction are within the scope of Rev. Rul. 77-316, 1977-2 C.B. 53, or Rev. Rul. 78-338, 1978-2 C.B. 107.

22 Section 864.—Definitions.—Whether a taxpayer is engaged in trade or business within the United States and whether income is effectively connected with the conduct of a trade or business within the United States.

23 Section 871.—Tax on Nonresident Alien Individuals.—The determination as to whether an alien individual is either a resident or nonresident of the United States will not be made with respect to situations in which the determination is dependent on factual representations that cannot be confirmed until the close of the alien individual's affected taxable year(s), that is, representations concerning an alien individual's projected stay and activities in the United States.

24 Sections 894.—Income Affected by Treaty.—Whether a taxpayer has a permanent establishment in the United States for the purpose of any United States Income Tax Treaty.

25 Section 897(e).—Coordination with Nonrecognition Provisions—Whether any nonrecognition provision shall apply for purposes of section 897, unless the transaction clearly falls within the provision of section 897(e)(1). See Rev. Rul. 84-160, 1984-2 C.B. 125.

26 Section 901.—Taxes of Foreign Countries and of Possessions of United States.—Whether a person claiming credit has established, based on all of the relevant facts and circumstances, the amount, if any, paid by the dual capacity taxpayer pursuant to the qualifying levy, that is not paid in exchange for a specific economic benefit. Section 1.901-2A(c)(2) of the regulations.

27 Section 992.—Requirements of a Domestic International Sales Corporation.—The tax effects of a Domestic International Sales Corporation's stock being held by individuals who are also shareholders in a related supplier corporation.

28 Section 7701.—Definitions.—Whether what is generally known as a foreign corporation will be classified as a partnership for U.S. tax purposes if the taxpayer requests classification as a partnership.

29 Section 7701.—Definitions.—Whether a foreign partnership will be classified as an association for U.S. tax purposes if the taxpayer requests classification as an association.

.02 General areas.

1 Any matter in which the determination requested is primarily one of fact, e.g., market value of property, or whether an interest in a corporation is to be treated as stock or indebtedness.

2 The tax effect of any transaction to be consummated at some indefinite future time.

3 Any matter dealing with the question of whether property is held primarily for sale to customers in the ordinary course of trade or business.

4 The tax effect of a transaction if any part of the transaction is involved in litigation among the parties affected by the transaction, except for transactions involving bankruptcy reorganizations.

SEC. 5. AREA UNDER EXTENSIVE STUDY IN WHICH RULINGS OR DETERMINATION LETTERS WILL NOT BE ISSUED UNTIL THE SERVICE RESOLVES THE ISSUE THROUGH PUBLICATION OF A REVENUE RULING, REVENUE PROCEDURE, REGULATIONS OR OTHERWISE

.01 Section 61.—Gross Income Defined.—Whether amounts voluntarily deferred by a taxpayer under a deferred compensation plan maintained by an organization described in section 501 of the Code are currently includible in the taxpayer's gross income.

.02 Sections 61 and 162.—Gross Income Defined; Trade or Business Expenses.—The tax consequences with respect to a salary reduction arrangement under which an employee receives and returns salary amounts to the employer. (Also sections 3121, 3306 and 3401).

.03 Section 79.—Group-Term Life Insurance Purchased for Employees.—Whether life insurance provided for employers under a "retired lives reserve" plan will be considered group-term insurance (also sections 61, 72, 83, 101, 162, 264, and 641).

.04 Section 101.—Certain Death Benefits.—Whether proceeds of "self-insured" life and survivor benefit plans established through a trust qualified under section 501(c)(9) of the Code are excludable from the beneficiary's gross income as amounts paid by reason of the death of the insured under section 101(a).

.05 Section 103.—Interest on Certain Governmental Obligations.—With respect to requests made pursuant to Rev. Proc. 79-12, 1979-1 C.B. 492, whether municipal bonds will meet the "trade or business test" and the "security interest test" under sections 103(b)(2)(A) and (B) of the Code and section 1.103-7(b)(5) of the regulations when the proceeds are used to finance facilities such as electric energy, gas or water facilities and, pursuant to a contract to take, or to take or pay for, a nonexempt person purchases 75 percent or more of the actual output of the facility but less than 25 percent of the subparagraph (5) output of the facility as defined in section 1.103-7(b)(5)(ii)(b) of the regulations.

.06 Section 103.—Interest on Certain Governmental Obligations.—With respect to requests made pursuant to Rev. Proc. 84-49, 1984-1 C.B. 548, whether bonds issued to provide owner-occupied mobile homes (not permanently fixed to real property) are exempt from federal income tax under section 103(a) of the Code.

.07 Section 162—Trade or Business Expenses.—Whether payments paid or accrued by a corporation to an exempt organization as described in section 501(c)(7), (c)(9), (c)(17) or (c)(20) of the Internal Revenue Code, are deductible under section 162.

.08 Sections 162 and 262.—Commuting Expenses.— Whether expenses are non-deductible commuting expenses.

.09 Section 168(f)(8).—Special Rule for Leases.—The tax consequences in certain areas specifically reserved in the

Temporary Income Tax Regulations under the Economic Recovery Act of 1981, relating to special rules for leases. The areas specifically reserved are: section 5c.168(f)(8)-8(b)(9) on retirements and casualties; section 5c.168(f)(8)-9 on the transfer of investment tax credit by section 168(f)(8) leases; section 5c.168(f)(8)-10 on leases between related parties; and section 5c.168(f)(8)-11 on consolidated returns.

.10 Section 216.—Deduction of Taxes, Interest, and Business Depreciation by Cooperative Housing Corporation Tenant-Stockholder.—If a cooperative housing corporation, as defined in section 216(b)(1) of the Code, transfers an interest in real property to a corporation (not a cooperative housing corporation), in exchange for stock or securities of the transferee corporation, which engages in commercial activity with respect to the real property interest transferred, whether (1) the income of the transferee corporation derived from the commercial activity, and (2) any cash and property attributable to the real property interest transferred that may be distributed by the transferee corporation to the cooperative housing corporation, will be considered as gross income of the cooperative housing corporation for the purpose of determining whether 80 percent or more of the gross income of the cooperative housing cooperation is derived from tenant-stockholders within the meaning of section 216(b)(1)(D).

.11 Section 302(b)(4) and (e) (also Pre-TEFRA section 346(a)(2) and (b)).—Partial Liquidation.—Whether the absence of an actual redemption of stock is a meaningless gesture within the meaning of Rev. Rul. 79-257, 1979-2 C.B. 136, as amplified by Rev. Rul. 81-3, 1981-1 C.B. 125, when:

(i) The corporation has outstanding more than one class of stock and there are priorities are dividend or liquidating distributions or any other differences in stock rights, or

(ii) Either under the terms of the stock or as established contractually, there are outstanding any rights affecting the corporation's stock, such as, but not limited to, warrants, options, convertible securities, shareholder agreements, or rights of first refusal.

.12 Section 306(b)(4).—Transactions Not in Avoidance.—Whether section 306(b)(4) of the Code applies to the distribution and disposition or redemption of "section 306 stock" that is subject to mandatory redemption.

.13 Sections 331, 337, 453, and 1239.—The Tax Effects of Installment Sales of Property Between Entities with Common Ownership.—The tax effects of a transaction in which there is a transfer of property by a corporation to a partnership or other noncorporate entity (or the transfer of stock to such entity followed by a liquidation of the corporation) when more than a nominal amount of the stock of such corporation and the capital or beneficial interests in the purchasing entity (that is, more than 20 percent in value) is owned by the same persons, and the consideration to be received by the selling corporation or the selling shareholders includes an installment obligation of the purchasing entity.

.14 Section 334(b)(2) (pre-TEFRA).—Liquidation of Subsidiary.—Whether an acquiring corporation may treat the life insurance reserves received in the liquidation as unsecured liabilities assumed.

.15 Section 336 (pre-TEFRA).—Distribution of Property in Liquidation.—Whether the liquidation of a life insurance subsidiary is a termination pursuant to section 815(d)(2) as in effect before the enactment of the Tax Reform Act of 1984.

.16 Section 338 (pre-TEFRA section 334(b)(2)).—Certain Stock Purchases Treated as Asset Acquisitions.—The Tax consequences, under subchapter L, from the stock purchase and the deemed purchase of the assets of a life insurance subsidiary.

.17 Section 351.—Transfer to Corporation Controlled by Transferor.—Whether section 351 applies to the transfer of widely held developed or undeveloped real property or interests therein; widely held oil and gas properties or interests therein; or any similarly held properties or interests to a corporation in exchange for shares of stock of such corporation when (i) the transfer is the result of solicitation by promoters, brokers, or investment houses, or (ii) the transferee corporation's stock is issued in a form designed to render it readily tradable.

.18 Section 351.—Transfer to Corporation Controlled by Transferor.—Whether section 351 of the Code applies to the transfer of an interest in real property by a cooperative housing corporation (as defined in section 216(b)(1)) to a corporation in exchange for stock or securities of the transferee corporation engages in commercial activity with respect to the real property interest transferred.

.19 Section 368.—Definitions Relating to Corporate Reorganizations.—Whether a transaction qualifies under either section 368(a)(1)(B) or section 351(a) of the Code by reason of Rev. Rul. 67-448, 1967-2 C.B. 144, when the same transaction is structured under sections 368(a)(1)(A) and 368(a)(2)(E) (as a reverse triangular merger) and fails to qualify for an advance ruling under those sections merely because (i) the "substantially all" requirement set forth in section 3.01 of Rev. Proc. 77-37, 1977-2 C.B. 568, is not met, or (ii) the "control" requirement of section 368(a)(2)(E)(ii) is not met where the step transaction doctrine may be applied to treat a prior redemption of stock as part of the plan of reorganization.

.20 Section 422A.—Incentive Stock Options.—Whether Holding (1) of Rev. Rul. 80-244, 1980-2 C.B. 234, relating to section 1036, applies to incentive stock options.

.21 Section 565.—Whether the consent dividend procedure under section 565 applies to corporations other than those corporations to which sections 535, 545, 556, 852, and 857 are applicable.

.22 Section 671.—Trust Income Deductions, and Credits Attributable to Grantor and Others as Substantial Owners.—Whether the grantor will be considered the owner of any portion of a trust when (1) the trust corpus consists or will consist substantially of insurance policies on the life of the grantor or the grantor's spouse, (2) the trustee or any other person has a power to apply the trust's income or corpus to the payment of premiums on policies of insurance on the life of the grantor or the grantor's spouse, (3) the trustee or any other person has a power to use the trust's assets to make loans to the grantor's estate or to purchase assets from the grantor's estate, and (4) there is a right or power in any person that would cause the grantor to be treated as the owner of all or a portion of the trust under sections 673 to 677.

.23 Section 704(e).—Family Partnerships.—Any matter relating to a family partnership in which, on formation of the partnership or other specified date, there is a special allocation of an item of income, gain, loss deduction or credit for the purpose of fixing or freezing the value of a partner's partnership interest.

.24 Section 721.—Nonrecognition of Gain or Loss on Contribution.—Whether section 721 applies to the contribution of widely held developed or undeveloped real property or interests therein; widely held oil and gas properties or interest therein; or any similarly held properties or interests to a partnership in exchange for an interest in the partnership when (i) the contribution is the result of solicitation by promoters, brokers, or investment houses, or (ii) - the interest in the transferee partnership is issued in a form designed to render it readily tradable.

.25 Section 801(b)—Life Insurance Company Taxable Income Defined.—Whether the liquidation of a life insurance subsidiary pursuant to either section 334(b)(2) (pre-TEFRA) or section 338 (added by TEFRA) is a termination under section 315(d)(2) causing a distribution from the subsidiary's policyholders surplus account.

.26 Section 805(a)(8)—Other Deductions.—Whether a portion of the purchase price of the stock of the life insurance subsidiary is properly allocable to insurance in force.

.27 Section 811 (b)(34)—Amortization of Premium and Accrual of Discount-Exception.— Whether the difference between the face value of bonds held by a life insurance subsidiary liquidating under section 334(b)(2) (pre-TEFRA) or section 338 (added by TEFRA) and the amount allocable to such bonds pursuant to the liquidation is market discount and need not be accrued.

.28 Section 815(d)(2), as in effect before the enactment of the Tax Reform Act of 1984—Termination as Life Insurance Company.—Whether the liquidation of a life insurance subsidiary pursuant to section 334(b)(2) (pre-TEFRA) or section 338 (added by TEFRA) is a termination requiring the application of section 801(c) or section 802(b)(3) as in effect before the enactment of the Tax Reform act of 1984.

.29 Section 816(b).—Life Insurance Reserves Defined.—Whether the life insurance reserves acquired in the liquidation of a life insurance subsidiary qualify as unsecured liabilities assumed by the acquiring corporation for purposes of section 334(b)(2) (pre-TEFRA) and section 338 (added by TEFRA).

.30 Section 818(b)—Treatment of Capital Gains and Losses, etc.—Whether the purchase of the stock of a life insurance subsidiary and its subsequent liquidation under section 334(b)(2) (Pre-TEFRA) or section 338 (added by TEFRA) is, in fact, a purchase of the subsidiary's insurance contracts.

.31 Section 1502.—Regulations.—Whether a parent cooperative housing corporation (as defined in section 216(b)(1)) will be permitted to file a consolidated income tax return with its transferee subsidiary if the transferee engages in commercial activity with respect to the real property interest transferred to it by the cooperative housing corporation.

.32 Section 2503.—Taxable Gifts.—Whether the transfer of property to a trust will be a gift of a present interest in property when (1) the trust corpus consists or will consist substantially of insurance policies on the life of the grantor or the grantor's spouse, (2) the trustee or any other person has a power to apply the trust's income or corpus to the payment of premiums on policies or insurance on the life of the grantor of the grantor's spouse, (3) the trustee or any other person has a power to use the trust's assets to make loans to the grantor's estate or to purchase assets from the grantor's estate, (4) the trust beneficiaries have the power to withdraw, on demand, any additional transfers made to the trust, and (5) there is a right or power in any person that would cause the grantor to be treated as the owner of all or a portion of the trust under sections 673 to 677.

.33 Section 2514.—Powers of Appointment.—If the beneficiaries of a trust permit a power of withdrawal to lapse, whether section 2514(e) of the Code will be applicable to each beneficiary in regard to the power when (1) the trust corpus consists or will consist substantially of insurance policies on the life of the grantor or the grantor's spouse, (2) the trustee or any other person has a power to apply the trust's income or corpus to the payment of premiums on policies of insurance on the life of the grantor or the grantor's spouse, (3) the trustee or any other person has a power to use the trust's assets to make loans to the grantor's estate or to purchase assets from the grantor's estate, (4) the trust beneficiaries have the power to withdraw, on demand, any additional transfers made to the trust, and (5) there is a right or power in any person that would cause the grantor to be treated as the owner of all or a portion of the trust under sections 673 to 677.

.34 Sections 3121, 3306, and 3401.—Employment Taxes.—Who is the employer of an "employee-owner" as defined as section 269A of the Code.

.35 Section 7701.—Definitions.—The classification of arrangements formed as trusts under local law, in which the trust borrows money to purchase equipment or property and leases it to third parties, and in which the grantor or grantors have a beneficial interest in the trust and the power to manage the activities of the trust.

.36 Section 7701.—Definitions.—The classification of limited liability companies for federal income tax purposes.

.37 Section 7701.—Definitions.—The classification of an arrangement as a fixed investment trust when the arrangement has multiple classes of equitable ownership.

SEC. 6. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Procs. 85-22, 85-24, 85-27, 85-28, 85-34, and 85-59 are superseded.

Required Distributions from IRAs and Qualified Plans under Sections 401(a)(9), 408(a)(6), and 408(b)(3) of the Internal Revenue Code and Amendments to IRAs as a result of Amendments by Section 521 of the Tax Reform Act of 1984 (Pub. L. 98-369)

Notice 86-1

This notice provides that minimum distributions required for the 1985 calendar year need not be made until December 31, 1986, from qualified plans and individual retirement accounts and annuities (IRAs) pursuant to sections 401(a)(9), 408(a)(6), and 408(b)(3) of the Internal Revenue Code, as amended by section 521 of the Tax Reform Act of 1984 (TRA of 1984). It also provides that an IRA with a current favorable opinion letter need not be amended to provide the distribution rules in section 408(a)(6) and (b)(3), as amended, until further notice.

Section 401(a)(9), as amended, requires qualified plans to make minimum distributions to certain participants and beneficiaries for the 1985 calendar year. Section 408(a)(6) and (b)(3), as amended, requires distributions from IRAs for the 1985 calendar year to be made, pursuant to regulations of the Secretary, under rules similar to those of section 401(a)(9) for qualified plans. Distributions not required to be made until April 1, 1986, shall be considered distributions for the 1985 calendar year. For qualified plans and IRAs (including IRAs from which distributions were required to commence prior to the 1985 calendar year), if minimum distributions required to be made to participants (or individuals) and beneficiaries for the 1985 calendar year are made on or before December 31, 1986, such distributions will be deemed for purposes of sections 401(a)(9), 408(a)(6), and 408(b)(3), as amended, to have been made within the time limits for making minimum distributions for the 1985 calendar year. Minimum distributions required for the 1986 calendar year must also be made on or before December 31, 1986 for those participants (or individuals) and beneficiaries for whom distributions are required for the 1985 calendar year (even if such 1985 calendar year distributions are made in the 1986 calendar year).

Further guidance will be provided in the future with respect to the minimum distribution requirements of sections 401(a)(9), 408(a)(6), and 408(b)(3).

An IRA with a current favorable opinion letter, i.e., issued on or before December 31, 1985, need not be amended to provide the distribution rules in section 408(a)(6) and (b)(3), as amended, until further notice. In addition, a sponsor of an IRA with a current favorable opinion letter should not submit a request for an opinion letter on amendments proposed to be made to comply with section 408(a)(6) and (b)(3), as amending IRAs with current favorable opinion letters, the Service will publish sample language for IRAs, including IRAs used for funding simplified employee pensions (SEPs), that, if adopted, will satisfy section 408(a)(6) and (b)(3). In the case of an existing IRA or a newly established IRA which is established by executing Form 5305 or Form 5305A, the current (Rev. 11-83) editions of those forms may be used until further notice. However, an IRA which does not have a current favorable opinion letter and which is not established by executing Form 5305 or Form 5305A must contain rules similar to the minimum distribution rules in section 401(a)(9), as amended, in order to comply with section 408(a)(6) and 408(b)(3), and thus be the subject of a favorable opinion letter.

The guidance in this Notice may be relied upon to comply with sections 401(a)(9), 408(a)(6) and 408(b)(3), as amended, with respect to distributions for the 1985 calendar year.

Part IV. Items of General Interest

Dispositions by Charitable Organizations of Certain Donated Property

Announcement 86-1

This announcement concerns modification of the rules under section 6050L of the Internal Revenue Code regarding information reporting by charitable organizations that dispose of certain donated property within 2 years after the date of the contribution of the property. This reporting requirement applies only where the donee charity signs an appraisal summary (Form 8283) with respect to the donated property. The donor is required to obtain the donee's signature on an appraisal summary for items whose value when aggregated with that of similar items of property contributed during the donor's taxable year exceeds $5,000. Taxpayers may rely on this announcement until final regulations are issued under section 6050L. The Service expects to issue final regulations in 1986 in which the modifications discussed in this announcement will be incorporated.

Background

On December 31, 1984, the Service published section 1.170A-13T and section 1.6050L-1T of the temporary regulations. Section 1.170A-13T(c) sets forth substantiation requirements that apply to donors for deductions claimed in excess of $5,000 for certain charitable contributions of property. Section 1.170A-13T(c)(1) provides that, for purposes of the donor's determination of whether the claimed value of property he contributed during his taxable year exceeds $5,000, the claimed value of all similar items of property donated to any charitable organization during that year are aggregated. In addition to other requirements, the regulations provide in section 1.170A-13T(c)(2)(i) that an appraisal summary (Form 8283) must be attached to the tax return of the donor on which a deduction for a contribution subject to the regulations is first claimed.

Section 1.6050L-1T(a) provides that, if the donee of any "charitable deduction property" sells, exchanges, or otherwise disposes of the property within 2 years after the date of the contribution of the property, the donee must make an information return on Form 8282. Charitable deduction property is defined in section 1.6050L-1T(d) as any property (other than money or publicly traded securities) contributed after December 31, 1984, with respect to which a donee signs an appraisal summary (as described in section 1.170A-13T(c)(4)).

Donee Reporting Exclusion

Under final regulations donee reporting will not be required with respect to an item of charitable deduction property disposed of by sale if the appraisal summary signed by the donee with respect to the item contains, at the time of the donee's signature, a statement signed by the donor that the appraised value of the item does not exceed $500. In the case of an appraisal summary that includes more than one item, the exclusion is available with respect to an item only if the item is clearly identified as having a value of $500 or less. However, for purposes of the donor's determination of whether the appraised value of the property exceeds $500, all shares of nonpublicly traded stock, or items that form a set (such as, for example, a collection of books written by the same author, components of a stereo system, or six place settings of a pattern of silverware), are considered one item. The requirement to obtain a statement from the donor on the appraisal summary is satisfied with respect to an appraisal summary submitted to the donee on or before January 31, 1986, if the donee obtains the required statement from the donor on or before March 31, 1986, on either an amended appraisal summary or an attachment for the original appraisal summary.

In addition, no reporting will be required with respect to an item consumed or distributed without consideration if the consumption or distribution is in furtherance of a purpose or function constituting a basis for the donee's exemption under section 501 of the Internal Revenue Code. For example, no reporting is required with respect to medical supplies consumed or distributed by a tax-exempt relief organization in aiding disaster victims.

Cumulative List of Announcements Relating to Section 7428(c) Validation of Certain Contributions Made During Pendency of Declaratory Judgment Proceedings from December 2, 1985 through December 31, 1985

The following is a cumulative listing of names of organizations that are presently challenging, under section 7428 of the Internal Revenue Code, the revocation of their status as organizations entitled to receive deductible contributions in declaratory judgment suits in the Tax Court, the United States District Court for the District of Columbia, or the United States Claims Court. The initial announcement listing the names of these organizations appeared as Announcement 85-169 in Internal Revenue Bulletin No. 1985-48, dated December 2, 1985. The purpose of this announcement is to inform potential donors to these organizations of the protection under 7428(c) for certain contributions made during the litigation period.

Protection under section 7428(c) of the Code begins on the date that the notice of revocation is published in the Internal Revenue Bulletin and ends on the date on which a court first determines that an organization is not described in section 170(c)(2), as more particularly set forth in section 7428(c)(1). In the case of individual contributors, the maximum amount of contributions protected during this period is limited to $1,000.00, with a husband and wife being treated as one contributor. This protection is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organizations that were the basis for the revocation. This protection also applies (but without limitation as to amount) to organizations described in section 170(c)(2) which are exempt from tax under section 501(a). If the organization ultimately prevails in its declaratory judgment suit, deductibility of contributions would be subject to the normal limitations set forth under section 170.

The names of organizations that have timely filed declatory judgment suits under section 7428 of the Code, challenging revocation of their status as eligible donees under section 170(c)(2) are listed below.

The Adam School, Inc.	New York, NY
Tony and Susan Alamo Foundation	Alma, AR
American Dental Association Disaster Victims Relief Emergency Loan Fund	Chicago, IL
Carolina Hospital and Health Services, Inc.	Charlotte, NC
Centre for International Understanding	St. Louis, MO
Church of Gospel Ministry, Inc.	Chula Visa, CA
Contemporary Mission, Inc.	Westport, CT
Deer Creek Educational Institute, Inc.	Arcola, MS
Far Eastern University	Newark, NJ
Charles A. Fields Medical Foundation	Madison, WI
First Church of God the Father of San Gabriel	Albuquerque, NM
Foundation for Restoration of the Physically Disfigured	W. Des Moines, IA
International Postgraduate Medical Foundation	Newport Beach, CA
The Kinnaird Foundation	Cincinnati, OH
Lula—Rich Educational Foundation	Clarksdale, MS
Marshall County Educational Foundation, Inc.	Holly Springs, MS
Maryland Right to Life, Inc.	Kensington, MD
Ministry of Bob Harrington, Inc.	New Orleans, LA
New Faith, Inc.	Bonita, CA
Newspaper Guild of New York, Times Unit Times College Scholarship Fund	New York, NY
Orange County Agricultural Society	Middletown, NY
Ours, Inc.	Atlanta, GA
Parents Aid Society	Hempstead, NY
Quitman County Educational Foundation	Marks, MS
Brian Rudd International, Inc.	Phoenix, AZ
Sunburst Communities, Inc.	Goleta, CA
The Way International	New Knoxville, OH
Untied Community Church	Berkley, MI
Universal Church of Jesus Christ, Inc.	Ohatchee, AL
Universal Life Church, Inc.	Modesto, CA
University of Kansas City	Kansas City, MO
Urban Local Development Corporation	Philadelphia, PA

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Key to Abbreviations

RR	Revenue Ruling
RP	Revenue Procedure
TD	Treasury Decision
CD	Court Decision
PL	Public Law
EO	Executive Order
DO	Delegation Order
TDO	Treasury Department Order
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  26 CFR Part 41 authority citation, revised; 41.4481-1, revised; 41.4481-1T, removed; 41.4481-1aT, redesignated as 41.4481-1T; 41.4481-2, 41.4482(b)-1, 41.4482(o)-1, 41.4483-2(f), 41.6001-1, amended; 41.4483-5, 41.4483-6 41.6001-2, added; 48.6427-1T, 48.6427-2T, removed & new 48.6427-2 through 48.6427-7, r[illegible]ed; 602, 101(c), amended; heavy vehicle use tax, credits and refunds on sale of diesel fuel (TD 8027) 26, *6*

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  26 CFR 48.4071-1(d), revised; treatment of sales of retreaded tires (TD 8057) 46, *33*
  26 CFR 51.4994-1, amended; 41.4995-2(b)(1), 51.4996-1(b)(2), revised; definitions of exempt oil for windfall profit tax purposes (TD 8035) 45, *9*
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  26 CFR 136.4064-1, 138.45222-1, removed; 48.4064-1, added; 48.44222(d)-1(d), revised; 602.101(c), 1.101605, 48.4217-2, 48.4221-1, 48.4221-5, 40.4221-6, 48.6416(b)-2(b), amended; gas guzzler tax (TD 8036) 34, *16*
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  26 CFR 1.44C-1 through 1.44C-3, redesignated as 1.23-1 through 1.23-3 & amended; 1.44C-4, redesignated as 1.23-4 & text added; 1.44C-5, 1.44C-6, redesignated as 1.23-5, 1/23-65 & amended; 1.1016-5(t), revised; residential energy credit (LR-73-80) 49, *13*
  26 CFR 1.46-1, 1.48-1, 1.191-1, 1.191-2, amended; 1.48-12, added; investment credit for certain rehabilitation expenditures (LR-238-81) 30, *34*
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  26 CFR 1.48-12T, 1.168(f)(8)-1T, 1.168(j)-1T, added; 602.101(c), amended; tax-exempt entity leasing (LR-31-85) 31, *29*

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  26 CFR 1.103-8, amended; industrial development bonds for residential rental property (LR-269-84) 50, *17*
  26 CFR 1.163-3T, amended; sanctions on issuers of registration-required obligations in bearer forms (LR-151-83 & LR-179-04) 40, *27*
  26 CFR 1.179-1 through 1.179-4, revised: 1.179-5, added; 1.263(a)-1, 1.263(a)-3, 1.1033(g)-1, amended; 1.1245-2(a)(3), revised; election to certain depreciable business assets expense (LR-233-81) 42, *16*
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  26 CFR 1.419A-2T, added; welfare benefit funds maintained pursuant to a collective bargaining agreement (EE-66-84) 33, *25*
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- 26 CFR 1.25-4T(e), (f), revised; mortgage credit certificates (TD 8048) *5*
- 26 CFR 1.46-4(d), 1.48-1, 1.48-2, amended; 1.48-11, added; investment credit for qualified rehabilitated buildings (TD 8031) 30, *5*
- 26 CFR 1.46-10, 1.46-11, added; 1.47-1, amended; computing investment credit for commuter highway vehicles (TD 8035) 33, *5*
- 26 CFR 1.48-12T, 1.168(f)(a)-1T, 1.163(j)-1T, added; 602.101(c), amended; tax-exempt entity leasing (TD 8033) 31, *6*
- 26 CFR 1.51-1, added; 1.381(c)(26)-1, amended; 5.51-1, 5h.4(e), removed; targeted jobs credit (TD 8062) 50, *4*
- 26 CFR 1.61-2T, 1.132-1T, 1.280F-1T, 1.280F-5T, 1.280F-6T, amended; 1.162-25T, revised; 1.274-5T, 1.274-6T, added; recordkeeping requirements with respect to listed property, taxation of fringe benefits, limitations on deductions for lessees of passenger automobiles (TD 8061) 46, 7
- 26 CFR 1.83-3, amended; property transferred in connection with the performance of services (TD 8042) 36, *4*
- 26 CFR 1.103A-2, added; 6a.103A-2, amended; information reporting for mortgage subsidy bonds (TD 8049) 41, *6*
- 26 CFR 1.117-3(b), 1.117-4(c)(1), amended; 1.117-5, added; federal grants and scholarships not includible in income (TD 8032) 32, *5*
- 26 CFR 1.163-5T, amended; sanctions on issuers of registration-required obligations in bearer form (TD 8046) 40, *9*
- 26 CFR 1.274-2, 1.274-5(c)(6)(iii), amended; 1.274-6, 1.274-8, revised; disallowance of deductions for expenditures incurred with respect to facilities, other than clubs, used in connection with entertainment (TD 8051) 42, *5*

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- 26 CFR 1.274-5T, 1.274-6T, 1.132-1T Q/A-4a, removed; substantiation of certain deductions and credits for business expenses, taxation of fringe benefits (TD 8060) 49, *5*
- 26 CFR 1.368-2, amended; statutory merger using voting stock of the corporation controlling the merged corporation (TD 8059) 49, *8*
- 26 CFR 1.401(a)-11T, amended; 1.402(f)-1T, added; 602.101(c), added; notice, election, and consent rules under the Retirement Equity Act of 1984 (TD 8037) 33, *8*
- 26 CFR 1.401(a)-11T, 1.401(a)-13T, 1.410(a)-5T, 1.410(a)-7T, 1.411(a)(11)-1T, added; 1.411(a)-7(d)(4)(iv)(B), 1.411(d)-3, amended; effective dates, transitional rules, restrictions on distributions, and other issues arising under the Retirement Equity Act of 1984 (TD 8038) 34, *5*
- 26 CFR 1.419A-2T, added; welfare benefit funds maintained pursuant to a collective bargaining agreement (TD 8034) 33, *12*
- 26 CFR 1.527-1, 1.527-2, amended; 1.527-8(d), revised; 1.527-9, added; 602.101(c), amended; designation of a principal campaign committee by a candidate for Congress (TD 8041) 36, 7
- 26 CFR 1.1092(b)-4T(f), revised; 1.6081-1T, added; mixed straddle account elections (TD 8058) 46, *30*
- 26 CFR 1.1275-3T, added; reporting requirements for original issue discount on publicly offered debt instruments (TD 8030) 29, *8*
- 26 CFR 1.6038-2, revised; 1.6038A-1, added; 601.101(c), amended; information returns required of certain foreign-owned corporations and required of U.S. persons with respect to certain foreign corporations (TD 8040) 35, 7
- 26 CFR 1.6045-2, added; 1.6042-3(a)(2), 1.6049-5(a)(5), amended, statements required with respect to certain substitute payments (TD 8029) 27, *10*

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Announcement of the Disbarment, Suspension and Consent Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries From Practice Before the Internal Revenue Service

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Allan T. Quello	Wayzata, MN	Attorney	October 12, 1985

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and address of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletins for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Arnold Asman	Great Neck, NY	Certified Public Accountant	Indefinite from October 12, 1985
Thomas P. Cornett	Toledo, OH	Enrolled Agent	Indefinite from December 1, 1985
Horace N. Tremelling	Spring Valley, CA	Enrolled Agent	Indefinite from October 17, 1985

Name	Address	Designation	Term of Suspension
Frank Riggsby, Jr.	Sierra Vista, AZ	Enrolled Agent	Indefinite from October 17, 1985
Edward L. Lambert	Rancho Mirage, CA	Certified Public Accountant	From November 6, 1985 Until January 8, 1990
Benjamin Ostfield	Minneapolis, MN	Attorney and Certified Public Accountant	Indefinite from November 20, 1985
Kenneth D. Short	Ellicott City, MD	Attorney	Indefinite from November 6, 1985

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-2, page 4.

Credit for producing oil from a nonconventional source. A taxpayer may receive the production credit on sales of gas during a calendar year in which the taxpayer also received the incentive price from other sales of gas from the same wells under section 107 of the Natural Gas Policy Act of 1978 (NGPA).

Rev. Rul. 86-3, page 4.

Business expenses; state legislator; legal expenses. A politician may not deduct legal fees under section 162(e)(2) of the Code paid to defend against criminal charges arising from participation in a political campaign in support of a candidate for political office.

Rev. Rul. 86-4, page 5.

Controlled corporations; stock distribution; device to distribute earnings and profits. The transfer of a small percentage of investment assets relative to the other assets transferred by a corporation to a controlled corporation prior to the distribution of the stock of the controlled corporation is a factor to be considered in determining whether the transaction is a device for the distribution of earnings and profits. Rev. Rul. 56-557 clarified.

ADMINISTRATIVE

Rev. Proc. 86-4 page 7.

Electronic filing pilot project. Specifications are set forth for qualified income tax return preparers to file 1985 individual income tax returns electronically.

Announcement 86-2, page 54.

New Form 8308, Report of a Sale or Exchange of Certain Partnership Interests, has been developed for partnerships to report a sale or exchange of all or a part of a partnership interest involving unrealized receivables or substantially appreciated inventory items.

Finding Lists begin on page 57.
Announcement of Suspensions on page 55.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 29.—Credit for Producing Fuel from a Nonconventional Source

Credit for producing oil from a nonconventional source. A taxpayer may receive the production credit on sales of gas during a calendar year in which the taxpayer also received the incentive price from other sales of gas from the same wells under section 107 of the Natural Gas Policy Act of 1978 (NGPA).

Rev. Rul. 86-2

ISSUE

Whether taxpayer is allowed the credit under section 29(a) of the Internal Revenue Code for producing fuel from a nonconventional source for sales of gas during part of a calendar year, notwithstanding that during the same calendar year other sales of gas from the same wells were made under the incentive pricing provisions of section 107 of the Natural Gas Policy Act of 1978 (NGPA).

FACTS

During the first part of the 1983 calendar year, the taxpayer sold gas produced from a tight formation at an incentive price under section 107(b) of the NGPA. But for section 107 of the NGPA, the gas in question would qualify under section 103 (ceiling price for new, onshore production wells) of the NGPA. For the remainder of the calendar year, the taxpayer sold the gas at a price not higher than the maximum lawful price under section 103 of the NGPA. All sales were made to an unrelated person within the meaning of section 29(d)(8) of the Code.

LAW AND ANALYSIS

Section 29(a) of the Internal Revenue Code (formerly section 44D, but renumbered by section 47(c)(1) of the Tax Reform Act of 1984, 1984-3 (Vol. 1) C.B. 1, 333) provides for a credit against income tax of an amount equal to $3 multiplied by the barrel of oil equivalent of qualified fuels which were sold by the taxpayer to an unrelated person during the taxable year, and the production of which is attributable to the taxpayer.

Section 29(e) of the Code provides that subsection (a) applies with respect to natural gas that is produced from a tight formation and that is sold during the taxable year only if that natural gas is sold at a lawful price which is determined without regard to the provisions of section 107 of the NGPA of 1978 and subtitle B of title I of the NGPA.

The provision now contained in section 29(e) was amended by section 611(a) of the Economic Recovery Tax Act of 1981 (ERTA) (1981-2 C.B. 256, 343). Before this amendment, that provision had required that if the taxpayer made an election under section 107(d) of the NGPA to receive the incentive price, the taxpayer could not receive the credit provided by section 29(a) of the Code. This was an irrevocable election that, according to the NGPA, had to be made either before the well was drilled or within 30 days after the passage of any Act providing a tax credit. Because Congress recognized that fluctuating market conditions might cause variation in whether the incentive price or the production credit was more advantageous, what is now section 29(e) was amended to allow the taxpayer to use either one, so long as both are not used for the same gas.

HOLDING

The taxpayer is allowed the production credit under section 29(a) of the Code for sales of gas during part of a calendar year, notwithstanding that during the same calendar year other sales of gas from the same wells were made under the incentive pricing provisions of section 107 of the NGPA.

Section 162.—Trade or Business Expenses

26 CFR 1.162-20: Expenditures attributable to lobbying, political campaigns, attempts to influence legislation, etc., and certain advertising.

Business expenses; state legislator; legal expenses. A politician may not deduct legal fees under section 162(e)(2) of the Code paid to defend against criminal charges arising from participation in a political campaign in support of a candidate for political office.

Rev. Rul. 86-3

ISSUE

If a politician makes expenditures for legal fees to defend against charges of buying votes in an election, are the expenditures deductible under section 162(a) of the Internal Revenue Code?

FACTS

A performed voluntary campaign work on behalf of a candidate in a party primary election for a county law enforcement office. *A* was indicted for buying votes during the course of this campaign work. *A* paid substantial legal fees in connection with the defense of the criminal charges. At the time the alleged illegal acts were committed, *A* was a state legislator and an independent businessman.

LAW AND ANALYSIS

Section 162(a) of the Code provides, in part, that there shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.

Section 162(e)(2)(A) of the Code provides, in effect, that no trade or business expense deduction shall be allowed for any amount paid or incurred for participation in, or intervention in, any political campaign on behalf of any candidate for public office.

Section 1.162-20(c)(1) of the Income Tax Regulations provides, in part, that expenditures for political campaign purposes (including the support of, or opposition to, any candidate for public office) are not deductible.

The deductibility of expenses for legal fees depends on the factual context in which the expenses originate. *See United States v. Gilmore*, 372 U.S. 39 (1963), 1963-1 C.B. 355. Thus, whether a taxpayer ultimately is convicted of a criminal offense does not determine deductibility under section 162(a) of costs for defense. A taxpayer may therefore deduct expenses that are incurred for legal fees in an unsuccessful defense against criminal charges if the charges grow out of activities in the taxpayer's trade or business and the expenses are otherwise deductible under section 162(a). *See*

Commissioner v. Tellier, 383 U.S. 687 (1966), 1966-1 C.B. 32.

For purposes of section 162 of the Code, the office of a state legislator is a "trade or business." Section 7701(a)(26) of the Code provides that the term "trade or business" includes the performance of the functions of a public office. *See* Rev. Rul. 84-110, 1984-2 C.B. 35. Therefore, legal expenses incurred "in carrying on" the trade or business of being a state legislator are deductible, unless they are made nondeductible by specific provisions of the Code or regulations.

In the present situation, the criminal charges in connection with which *A* incurred legal fees grew out of *A*'s participation in a political campaign in support of a candidate for public office. Expenditures for purposes of such political campaigns are not deductible under section 162(a) of the Code. *See* section 1.162-20(c)(1) of the regulations. The charges against *A* grew out of a factual context, a political campaign, in which *A*'s expenses are not deductible. *A*'s legal fees in contesting the charges, therefore, are, likewise, not deductible.

HOLDING

Under section 162(e)(2) of the Code, *A* may not deduct legal fees paid to defend against criminal charges arising from *A*'s participation in a political campaign in support of a candidate for public office.

Section 355.—Distribution of Stock and Securities of a Controlled Corporation

26 CFR 1.355-1: Distribution of stock and securities of a controlled corporation.

Controlled corporations; stock distribution; device to distribute earnings and profits. The transfer of a small percentage of investment assets relative to the other assets transferred by a corporation to a controlled corporation prior to the distribution of the stock of the controlled corporation is a factor to be considered in determining whether the transaction is a device for the distribution of earnings and profits. Rev. Rul. 56-557 clarified.

Rev. Rul. 86-4

ISSUE

Whether the transfer of a small percentage of investment assets relative to the other assets transferred by a corporation to a controlled corporation prior to the distribution of the stock of the controlled corporation may be considered evidence that the transaction is a device for the distribution of earnings and profits within the meaning of section 355(a)(1)(B) of the Internal Revenue Code.

FACTS

P corporation has been engaged in the active conduct of two businesses, business *Q* and business *R*, throughout the past 5 years. For bona fide business reasons, *P* is required to separate ownership of the two businesses. Accordingly, *P* proposes to transfer all the assets associated with business *R* and investment assets not related to business *R* to corporation *S*, a newly-formed corporation, in exchange for all the outstanding stock of *S* and the assumption by *S* of related liabilities. *P* will then distribute all the *S* stock to *P*'s shareholders, pro rata. The fair market value of the investment assets is 20*x* dollars, and the fair market value of all the assets associated with business *R* is in excess of 155*x* dollars.

LAW AND ANALYSIS

Section 368(a)(1)(D) of the Code provides that a reorganization includes a transfer by a corporation of all or part of its assets to another corporation if, immediately after the transfer, the transferring corporation, or one or more of its shareholders, or any combination thereof, is in control of the corporation to which the assets are transferred; but only if, in pursuance of the plan, stock of the corporation to which the assets are transferred is distributed in a transaction which qualifies under section 354, 355, or 356.

Section 355(a)(1) of the Code provides generally for the distribution, without recognition of gain or loss to the shareholders, of stock of a corporation controlled by the distributing corporation, provided certain requirements are met. Pursuant to section 355(a)(1)(B), the distribution will not qualify under section 355 if the transaction was used principally as a device for the distribution of the earnings and profits of the distributing corporation, or the controlled corporation, or both. Section 1.355-2(b)(3) of the Income Tax Regulations provides that in determining whether a transaction was used principally as a device for the distribution of earnings and profits, all the facts and circumstances of the transaction must be considered. Particular attention must be paid to the nature, kind, and amount of the assets of the distributing and controlled corporations.

Rev. Rul. 83-114, 1983-2 C.B. 66, holds that a contribution to capital followed by a pro rata distribution of a controlled corporation's stock, while not *per se* a transaction used principally as a device for the distribution of earnings and profits, may constitute evidence thereof. A determination as to whether the transaction is a device for distribution of earnings and profits requires an evaluation of all the facts and circumstances surrounding the transaction, including the business reasons for the contribution to capital and subsequent stock distribution. See also Rev. Rul. 78-383, 1978-2 C.B. 142.

On the other hand, in Rev. Rul. 56-557, 1956-2 C.B. 199, involving facts similar to those described above, it was held that, in connection with the transfer by the distributing corporation to the newly-formed controlled corporation of 155*x* dollars of assets relating to an active business, the transfer of 20*x* dollars of assets having no relation to the transferred business did not render the provisions of section 355 inapplicable. Neither the facts nor the discussion set forth in that ruling clearly indicate the reasons for the transfer of the investment assets. Rev. Rul. 56-557 might be read to indicate that a relatively small percentage of investment assets among the transferred assets is not relevant to the inquiry as to whether the transaction is a device for the distribution of earnings and profits under section 355(a)(1)(B) of the Code. Because the ruling is misleading, Rev. Rul. 56-557 needs clarification.

HOLDING

In the present situation, the transfer by *P* to *S* of investment assets not related to the transferred business is a factor to be considered in determining whether the transaction is a device for the distribution of earnings and profits regardless of the percentage of such assets relative to the total amount of assets transferred. The percentage of investment assets transferred relative to the other assets held by *P* and *S* will be taken into account, along with the other facts and circumstances surrounding the transaction, including the reasons for the asset transfers and stock distribution, in determining whether the transaction is a device for the distribution of earnings and profits, and, thus, fails to qualify under section 355 of the Code.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 56-557 is clarified.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.602: Tax forms and instructions.

Rev. Proc. 86-4

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I. ELECTRONIC RETURNS

1. Overview

This Revenue Procedure sets the specifications for the 1986 Individual Tax Return Electronic Filing Test of Tax Year 1985 returns. In this Test, qualified individual income tax return preparers will transmit tax return information to the Internal Revenue Service over communications lines and will retain related paper documents (taxpayer declarations, Forms W-2, etc.) for submission every two weeks. To participate in this Test, preparers must follow all requirements and specifications in this Revenue Procedure and must provide a signed statement to that effect (see attachment IV). Preparers will also have to successfully complete a test transmission by January 30, 1986. The data for the test transmission will be provided by the Service. In addition, preparers will be required to give each taxpayer for whom they file an electronic return a copy of a letter provided by the Internal Revenue Service (see attachment I). Approval to participate will be for 1986 only. Specifications and application procedures for 1987 will be issued in the fall of 1986.

The Service reserves the right to revoke the electronic filing privilege of any preparer/transmitter who varies from these requirements and specifications or does not consistently transmit error-free returns.

2. Composition of an Electronic Return

a. An electronic return consists of data transmitted to the Service electronically and data filed with the Service on paper documents. In total, an electronic return must contain the same information as a comparable return filed entirely on paper documents.

b. For the 1986 test, electronically transmitted data is limited to entries from the return, Forms, and schedules listed below. Forms W-2, W-2P and W-2G will have selected data transmitted electronically. The paper copies will be transmitted to the Service attached to the back of the Forms 8453. All other schedules and forms listed are to be filed with the Service only in electronic form.

Form 1040 U.S. Individual Income Tax Return
  Schedule A Itemized Deductions
  Schedule B Interest and Dividend Income
  Schedule E Supplemental Income Schedule (limited to three (3) rental properties)
  Schedule R Credit for the Elderly and Permanently and Totally Disabled
Schedule W Deduction for a Married Couple When both Work
Form W-2 Wage and Tax Statement
Form W-2P Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments, when there is tax withholding
Form W-2G Statement for Recipients of Certain Gambling Winnings
  Form 2106 Employee Business Expense
  Form 2441 Credit for Child and Dependent Care Expenses
  Form 4562 Depreciation and Amortization
  Form 8283 Non-Cash Contributions

(Note: Taxpayers who would normally file Form 1040A or Form 1040EZ are *not* excluded from the test. They will instead file these electronically in the format of a Form 1040. Participating preparers are not to charge an additional fee for using the long Form 1040 format for short form filers).

c. The non-electronic portion of the return consists of the following segments:

(1) Copy B of a Form W-2, W-2P, or W-2G which would be attached to the front of a return filed entirely on paper documents.

(2) A document containing a required signature, such as Form 2120 (Multiple Support), a physician's statement required in connection with an entry on Schedule R, a proof of blindness certification from a physician or registered optometrist, an Exemption for Non-Custodial Parent (Form 8332) and Form 8453 (Taxpayer Declaration). Form 8453 is required for all electronic returns. (See part IV of these instructions and attachment II, Form 8453).

(3) Any other documents which are (a) not required by the Service, (b) are not IRS forms or schedules, (c) are not covered in sub-paragraph (2) above, and (d) are voluntarily being included with the return by the taxpayer as supporting material.

d. The non-electronic material described in sub-paragraph 2.c above must be stapled together, with the Taxpayer Declaration (Form 8453) on top, followed by the material described in 2.c(1), the remaining material described in 2.c(2), then the material in 2.c(3).

3. Exclusions

The following types of returns are excluded from the 1986 test.

1. Those returns with tax owed, with remittance or with an even balance.

2. Decedent or power of attorney returns, including returns filed by surviving spouses.

3. Amended or corrected returns. (even if the return being amended was filed electronically). Only one electronic return should be filed for any taxpayer for the filing season.

4. Returns containing Forms or Schedules not listed above.

5. Returns for any tax period other than January 1, 1985 to December 31, 1985.

6. Returns not transmitted by a preparer approved by the Service for electronic filing.

7. Returns filed after April 15, 1986, even if the taxpayer has secured an extension.

8. Returns subject to community property rules, with filing status "married filing separately".

9. Returns with Casualty Loss Deduction.

10. Returns containing multiple Schedules E or more than three rental properties on a Schedule E.

11. Returns with dollars and cents entries (even dollars only accepted).

12. Returns claiming a Mortgage Interest Credit on line 45 of Form 1040.

13. Returns containing more than 20 pages on continuation statements.

14. Returns containing vehicle entries in Section C of Form 4562.

II. PREPARER ELIGIBILITY REQUIREMENTS

A participating preparer must meet the following qualifications:

1. prepared individual income tax returns for compensation in 1984 and 1985 in one of the test metropolitan areas,

2. used computers to prepare individual income tax returns for at least two years, either directly or through a service bureau,

3. has substantial communication experience under IBM 3780 RJE bisynchronous protocol at 4800 BAUD through a dial-up modem, or will be associated with another firm which has such experience,

4. will observe all requirements of this revenue procedure,

5. will provide an acceptable test transmission to the Service.

III. ADVERTISING STANDARDS

In addition to meeting normal Service advertising standards, as outlined in Rev. Proc. 81-38, Limited Practice Without Enrollment, Section 8, Solicitation and Advertising, preparers must not advertise electronic filing outside the three Test metropolitan areas. Advertising must not infer a special relationship with the Internal Revenue Service. Claims for faster refunds should be consistent with the language in official Service publications.

IV. TAXPAYER DECLARATIONS (FORM 8453)

1. Prior to submitting an electronic return, a preparer must obtain the taxpayer's signature on a declaration form (see attachment II). In addition, the preparer must obtain all other documents currently required to be filed with returns, as detailed in I.2.c above.

The declaration will serve the following purposes:

—authenticate the return.

—authorize the preparer to file the return on behalf of the taxpayer.

—provide a transmittal for the associated paper documents that will be stapled to the declaration.

—authorize the preparer to transmit via a third-party transmitter.

2. If the amounts on the declaration differ from corresponding amounts on the return, the preparer will be required to file a corrected declaration or file a corrected return. If a taxpayer declaration is found to be missing, the preparer must expeditiously provide a signed form; otherwise the return will be considered unsigned.

3. Preparers must use the official Form 8453 or a substitute form which duplicates the official form in format, language and content. Computer printed Forms 8453 are acceptable.

4. After the declaration has been preperly executed, including the taxpayer and preparer signatures, the preparer will transmit the electronic portion of the return to the Service in accordance with Service specifications (see Section VI for signature requirements). By transmitting the electronic portion of the return to the Service the preparer is stipulating that the declaration has been executed and that the official descriptions of each entry of the electronic return apply (i.e., retained copies do not contain any unauthorized caveats).

5. The preparer will assign a unique 14 digit Declaration Control Number (DCN) to each Form 8453. Its structure will be as follows:

Position	Comments
1-2	These two digits must be "00".
3-7	The Electronic Filer Identification (EFIN). This is a unique number assigned by the IRS to each participating preparer for each site where electronic returns are prepared. The first two digits will always be the District Office code.
8-13	A sequential number assigned to each return by the preparer.
14	This digit must be "6". (e.g. 00-12345-678910-6)

6. The DCN must be recorded in the upper right hand corner of the Form 8453 for each taxpayer. Hyphens must appear between the 2nd and 3rd, 7th and 8th and 13th and 14th digits.

V. FILING OF ELECTRONIC RETURNS AND DISTRIBUTION OF COPIES

1. The Service will advise electronic filers when they can begin to file electronic returns. This will be as early in the filing period as possible, but only after all the programs, equipment, and facilities related to electronic filing have been thoroughly tested. Until this notification has been issued, electronic returns will not be accepted by the Service.

2. Similarly, if the electronic filing system breaks down for a potentially lengthy period, the Service will advise preparers to discontinue electronic filing until they are notified by the Service that the problem has been resolved.

3. Because electronic filing is a new program and tax return processing is very complex, prudence dictates that the Service have contingency plans to cover the remote possibility that filers will be requested to provide to the Service paper copies of returns previously filed electronically. This would only be necessary if all of the back-up systems built into electronic filing by the Service become inoperable simultaneously.

4. To Be Filed With The Service.

a. Participating preparers must transmit to the Service all electronic data, all taxpayer declarations, and all other materials described in Section I.2.c above.

b. The preparer will maintain the documents referred to in Section I.2.c in DCN order and place them in the provided folders in groups of 100.

c. Beginning on January 31, 1986, and every two weeks thereafter through May 22, 1986, the preparer will send this material to the Cincinnati Service

Center, in accordance with shipping instructions described in paragraphs V.4.d-k below. No Form 8453 may be sent to the Service for any electronic return that has not been acknowledged as received by the Service. Each shipment should include forms for all electronic returns filed during that period which have been acknowledged by the Service.

d. A Form 1332, Block and Selection Record, (see attachment III) must be the first item inside each folder. The Service will provide these forms. Record the last DCN at the top of the form as illustrated in attachment III. If a return has been rejected or not acknowledged by the Service (see Section VIII) pull the applicable Forms 8453 from the folder and circle the last two digits of the sequential number for each such form not included in the folder. If rejected or unacknowledged returns are subsequently transmitted, the applicable Forms 8453 must be renumbered.

e. The paper documents in each folder must be maintained in ascending sequence following the Form 1332. The first DCN must be recorded on the tab of the folder.

f. Place folders in the IRS Standard Type 3 Cartons that have been provided to you, so that the identifying sequence number information appearing on the tab is visible from the open end of the container.

g. The sequence of folders in the carton is from right to left, beginning with the lowest number. The top of the returns must always be at the open end of the container. Number and ship boxes in strict DCN sequence.

h. Place the lids provided on the cartons and seal with gummed tape which is at least 2 inches wide.

i. Ship cartons to:

Internal Revenue Service
Cincinnati Service Center
200 W. 4th St.
Covington, KY 41011
Attn: Alan Law
Stop #21

j. The initial supply of shipping materials will be forwarded directly to your offices. If additional supplies are needed, contact the Management Support Branch of the Cincinnati Service Center at 606-292-5241.

k. Cartons should be shipped via a carrier that will ensure receipt at the service center within two days of shipment.

5. To Be Retained By The Preparer—The preparer must retain a copy of the material furnished to the taxpayer. The preparer copy of the electronic material (described in Paragraph I.2.b) may be retained on magnetic media. In addition, the preparer must retain the acknowledgement file received from the Service to facilitate taxpayer inquiries. The retention period for this material must be consistent with IRC 6107.

6. To Be Provided To The Taxpayer—The preparer must furnish the taxpayer with a printed copy of all material filed with the Service covered in Paragraphs I.2.b and I.2.c(2), and any material covered I.2.c(3) initiated by the preparer. In addition, the preparer should advise the taxpayer to retain copies of materials described in Paragraph I.2.c(1) and materials described in Paragraph I.2.c(3) which were not provided by the preparer. The copy of the electronic material described in Paragraph I.2.b can be contained on replicas of official forms or on forms designed by the preparer. If the latter, data entries must be referenced to the line numbers on official forms.

VI. ELECTRONIC FILER REQUIREMENTS AND RESPONSIBILITIES

1. The Service will accept electronic returns only from preparers who have been approved for electronic filing.

2. Electronic filers must not prepare or transmit returns for taxpayers (or their representatives) who do not personally appear before them (at least one taxpayer on a joint return) unless the taxpayers are residents of the metropolitan area during the filing season.

3. Normally the electronic filer must be identified on the electronic return as the paid preparer, and must also sign the Form 8453 as the preparer.

4. If an electronic filer accepts returns prepared by individuals or by other preparers solely for purposes of electronic input, this will be considered to come under the "mechanical assistance" exception described in Treasury Regulation 301.7701-15(d)(1), and hence the approved firm will not be considered to be a paid preparer for purposes of 301.7701. However, in these cases the following requirements must be met:

a. The electronic filer must sign the Form 8453 as the transmitter, and obtain the taxpayer's signature on the same form.

b. The return must meet all of the consistency tests required for any other electronic return. However, the minor correction provisions in VI.6 are not applicable. The taxpayer or the preparer must correct the source material prior to submission. If the electronic filer corrects any material, the electronic filer becomes the return preparer.

c. If the return was prepared by another paid preparer, that other firm must be identified in the appropriate field of the electronic return as the paid preparer, and a copy of the tax return signed and prepared by that other firm must be attached to the Form 8453. If the return was self-prepared by the taxpayer, a copy of the return, signed by the taxpayer, must be retained by the preparer and the paid preparer field on the electronic return must be left blank.

5. If electronic returns are transmitted to the Service via a communications company, and the communications company does not alter the return information, the Service will consider the actions of the approved preparer as a permissible disclosure under Treas. Reg. 301.7216-2h, and will consider the actions of the communications company as an "auxiliary service" under Treas. Reg. 301.7216-1(b)(2)(i)(B).

6. If an electronic return is corrected in a non-substantive way after the taxpayer's signature has been obtained on Form 8453, but before the transmission to the Service, it will not be necessary for the preparer to obtain the taxpayer's signature on a new Form 8453, provided the following conditions are met:

a. The corrections do not affect any of the amounts included on the Form 8453 signed by the taxpayer.

b. The non-substantive changes are limited to corrections of arithmetic errors, inconsistencies due to rounding, and corrections of spelling errors.

7. Once an electronic return is submitted, it cannot be recalled or intercepted in process. Hence, if either the preparer or the taxpayer wishes to change any entries, an amended return must be filed, in the form of a paper document.

8. The preparer must promptly satisfy Service requests to resolve prob-

lems relating to missing or inconsistent Forms 8453 and provide copies of such forms within 24 hours upon request by the Service.

9. If a preparer shows a consistent pattern of failing to correctly carry out all requirements of this Revenue Procedure, or consistently files returns not meeting Service specifications, the Service may take unilateral action to revoke the electronic filing privilege for the remainder of the year.

10. The preparer must provide access to all materials that the preparer is required to maintain for the purpose of ensuring compliance with the retention requirements of this Revenue Procedure.

VII. ELECTRONIC FILING COMMUNICATIONS REQUIREMENTS

1. These procedures will only apply to this limited test and may not be relevant when this project is expanded in subsequent years.

2. Returns can be transmitted by preparers or by communications firms acting for preparers. For purposes of this section both will be termed transmitters. The Internal Revenue Service will arrange a schedule of days and times when approved transmitters may transmit return data, in the format covered in this Revenue Procedure. Normally, all data communications will be over the Public Telephone Switching Network to the Cincinnati Service Center. However, if a firm prefers to provide a dedicated line for transmission of its data it should contact the Electronic Filing Office at (202) 566-7541. Telephone numbers, specific password conventions and a test transmission schedule will be developed between the IRS and transmitters at a later time.

3. All data communications over the Public Telephone Switching Network between transmitters and the Service will be accomplished using the following requirements:

a. 4800 BAUD line speed.

b. EBCDIC or ASCII character code.

c. IBM 3780 communications protocol.

d. Half-duplex, Synchronous Bell compatible dial-up MODEMs.

e. Line-level and system-level security (passwords).

4. Transmitters will be responsible for the security of all transmitted data. Transmittals will not be considered filed returns until they successfully pass through the IRS Electronic Filing Pre-Processor. The Service will acknowledge all recognizable returns to the sender via return transmission within 24 hours of receipt (see Section VIII for Acknowledgement File).

5. The receipt date of the electronic record will constitute the receipt date of the return if it is acknowledged by the Service.

VIII. ACKNOWLEDGEMENT OF ELECTRONICALLY FILED RETURNS

Each transmission of a file of electronic returns will normally be acknowledged to the transmitter within 24 hours of successful receipt. The transmitter should immediately match the acknowledgement file back to the original file transmitted. Any tax return transmitted which is not acknowledged will have been bypassed by the Service due to transmission or file format problems and must be resubmitted to be considered a filed return. Any return not acknowledged as received by the Service will be considered not filed.

Note: Any transmitter who receives acknowledgements for returns which were *not transmitted on the designated transmission* or who does not receive transmission of an Acknowledgment File within 48 hours must immediately contact the Cincinnati Service Center at 606-292-5241.

IX. OVERVIEW OF TRANSMISSION PROCEDURES

(See appendices A through C for all record formats.)

The following sequence of events will constitute a tax return data transmission session:

1. The Cincinnati Service Center will call the number of the transmitter's MODEM during the scheduled time and initiate the authentication procedure.

2. When the transmitter has been authenticated, a tax return data session will commence. During the session, two types of transmissions will occur. The transmitter will send return records and the Service will acknowledge the previous transmission.

3. Each transmitter sending session will consist of no more than 500 tax returns (approximately 30 minutes line time). If more returns are available for transmission, they must be sent in subsequent transmissions during the same scheduled time slot (on the same day). Broken transmissions must be re-initiated from the beginning; there is no checkpoint capability at the IRS site. The IRS Service Center will continue to poll the transmitter for returns after each session until an "End of Returns" record is sent by the transmitter.

4. After receiving the "End of Returns" record, the IRS Service Center will send to the transmitter an Acknowledgement File for each return file received in the prior day's transmission. The IRS center will break the connection after the last Acknowledgement File for the transmitter has been sent.

X. EVALAUTION REQUIREMENTS

To assist the Service in evaluation, participants will be required to compile narrative reactions of clients to electronic filing, and reactions of the preparer to electronic filing, including statistics on the number of taxpayers eligible for electronic filing and the number of electronic returns filed. This information will be sent to the Service in June 1986. The Service will provide forms for these purposes at a later date.

APPENDIX A

ELECTRONIC RETURN FILE SPECIFICATIONS

Summary

After the transmitter has been authenticated, the sequence of record transmissions is as follows:

1. TRANS record (this record identifies the transmitter).

2. Tax Return records (including all form, schedule, and statement records).

3. Summary record.

4. Recap record.

This sequence will be repeated for each 500 returns transmitted.

5. End of Returns record (follows the final Recap record for final filing session of the day).

After the End of Returns record, the acknowledgement transmission will commence. The sequence of acknowledgement records is as follows:

1. The original Trans record.

2. An Ack record for each recognizable return received.

3. The original Recap record plus counts for accepted and rejected returns.

I. GENERAL DESCRIPTION

a. The IBM byte count convention may be used as an option, but is not required. This option is for a four byte counter to precede each block and a four byte counter to precede each logical record.

b. The first record on a transmitted file (the TRANS record) contains information regarding the transmitter and file format. This record should be followed by the records comprising the tax returns being transmitted. The last record on a transmitted file (the RECAP record) will provide balancing counts of returns.

c. A tax return will consist of a variable number of fixed-field records. The size and format of the logical record for each page of each form, schedule etc., are specified herein. In addition, a variable field/record format option is acceptable. See details under Variable Length Option.

d. Maximum-sized physical record (i.e., block) is 4500 characters. Physical records may be of varying lengths but the logical records described herein may not be broken between physical records.

e. Each logical record should contain all data fields pertaining to one printed page of an official form, schedule or continuation statement. The logical record therefore contains either an entire form, schedule or statement, or a logical part (i.e., a page) of a form, schedule or statement. The complete tax return must consist of all logical records pertaining to it in the following sequence: ***Return, Schedules, Forms, Statements and Summary***. Schedules must be in alphabetical sequence and forms must be in numeric sequence. Forms W-2, W-2G, and W-2P records shall appear as the final forms in the Form Record sequence. Return, Schedule, Form, and Statement Records may contain additional sequential Page Records if they consist of more than one printed page. (Pages are only numbered within a form schedule or statement, not across the return.) All records must appear in the proper sequence with the proper control information, and the counts of the schedules and forms must balance to the Summary Record or the return will be rejected.

f. If there are no entries on the form, schedule, or statement, the form, schedule, or statement should not be generated. If there is no significant data for any page within a form or schedule a "skip" short record may be used (see format in SKIP PAGE record layout). Numeric fields may be filled with spaces to facilitate data compression when transmitted.

g. The first logical record for a tax return (i.e., the Return Record for page 1 of the tax form) will include the tax period and return type and a unique 16-digit field for user-assigned return transmission number which will include the preparer's identification and the date, time and sequence of the transmitted return. This 16 digit Return Sequence Number appears in the RETURN record and consists of the following fields:

(1) Electronic Filer Identification Number (EFIN) (5 characters)

(2) EFIN suffix for optional use by preparers (2 characters)

(3) Julian date of transmission (3 characters)

(4) Transmission sequence number for the given Julian date (2 characters)

(5) Sequential number assigned to the return (4 characters)

h. If the number of data items appearing on the same line exceeds the number that can be contained in the space provided on the printed form or schedule, the data must be provided on a separate continuation statement (STM) record. There is a maximum of 20 statement page records per return in total. If STM is used, no data should be entered in the base return. The first line entry for the continued item on the base form or schedule record itself shall read "STMbnn ("nn" being the applicable statement number). All of the applicable entries must then be on the statement record and cannot be split between the continued item record(s) and the statement. The first statement record will contain a literal description of the item continued (e.g., "Interest Income, Schedule B"). The second statement record for all continuations of tabular data should contain the column headings (e.g., "Name of Payer . . . Amount . . .") spaced with the headings as they would appear on the printed form they continue. Conform to the same column headings. The related dollar amount must be on the first line of entry. Each following statement record from "LN03" on will contain, left justified, the related data fields in the same format as they appear in the base layout. Statements can always be used at the option of the preparer, even if the open-ended item can be contained in the space provided on the printed form or schedule. See details under Statement Record Layout in VI, below.

i. All money fields are 12 characters, 11 numerics followed by the sign character. Money fields containing no significant data must be filled with spaces. The significant numeric characters should be right justified, and zero filled. Dollar signs, decimal points, or other non-numeric characters are not permitted. The right-most position of any negative money field must contain the negative sign; for positive fields this position is always blank. Money fields must be all whole dollars (no cents).

j A summary record will be the final record for each tax return. This record will contain preparer identification data and counts of the Schedules, Forms and Statements included in the return and indicators for paper documents retained by the preparer for subsequent transmission to the IRS.

k. Except where designated, do not enter blanks or spaces between data elements.

j. The file should be unlabeled (no standard header or trailer records).

l. Each file must contain only complete returns.

Following is the format of each record.

II. TRANS RECORD

The first record on each file is the TRANS record which will contain the following (for this purpose, Transmitter is the firm handling the data communication):

Field#	Identification	Length	Description
(1)	Record I.D.	5	Value "TRANS"
(2)	Transmitter Name	35	Alphanumeric
(3)	EIN of Transmitter	9	Numeric
(4)	Address	35	Alphanumeric
(5)	City, State, Zip Code	35	Alphanumeric
(6)	Area Code, Telephone Number	10	Numeric
(7)	Type Transmitter (Preparer's Agent or Preparer)	16	Alphanumeric
(8)	Reserved	6	Blank
(9)	Reserved	12	Blank
(10)	Transmission Date	6	MMDDYY
(11)	Electronic Transmitter Identification Number	7	Numeric
(12)	Julian Date of Transmission	3	Numeric
(13)	Transmission Sequence Number for Julian Date in (12)	2	Numeric
(14)	Reserved	1	
(15)	Record Type	1	F = fixed, V = variable length option

III. VARIABLE LENGTH OPTION

The variable format will be indicated by a "V" in the Record Type field of the initial Transmitter (TRANS) Record for a file. In this format the data field is preceded by the applicable field identification number shown in specific record layouts. The field identification number is enclosed with field delimiters ([ ]). These characters will also enclose the control information (i.e., Record I.D. field) which begins each return, schedule or form record. The beginning of record control information remains in the same fixed format shown; the individual data fields need only contain the significant data (i.e. no leading zeros or trailing spaces). The Summary and Statement records, which are not keyed to field numbers, must be full length expanded records but must still be enclosed in field delimiters.

Each variable record will end with a Record Terminus Character (#). *IMPORTANT*: THE FOLLOWING THREE CHARACTERS "[", "]", and "#" ARE RESERVED AS DELIMITERS AND MAY *NOT* APPEAR AS DATA CHARACTERS.

The basic record would follow this format.

[RECORD ID FIELD] [1st field number] DATA
[Next field number] DATA . . . #

] = ASCII 93
[= ASCII 91
# = ASCII 35

IV. TAX RETURN RECORD

The Page 01 record for each tax return starts with the following 12 fields. Each page of the return will have a new page record with the page Number incremented. These records will each begin with Fields 1–9 below.

Field#	Identification	Length	Description
(1)	Record ID	3	Value "RET"
(2)	Filler	1	Blank
(3)	Return Type	6	Alphanumeric; Valid Value "1040bb"
(4)	Filler	1	Blank
(5)	Page Number	4	Value "PG01", format PGnnb, "nn" will increment for each printed page
(6)	Filler	1	Blank
(7)	Tax Period	4	Value "8512", YYMM
(8)	Filler	1	Blank
(9)	Social Security Number	9	9 Numerics (≥ 001010000)
Begin data fields here for pages after Page 01			
(10)	Sequence Number	16	Return Transmission Sequence Number (see item g. under General Description)
(11)	Declaration Control Number	14	Assigned by preparer to taxpayer declaration and related paper documents
Begin data fields here for Page 01			
(12)	Data Fields	various	Page data fields

V. SCHEDULE RECORDS

The second record or series of records is the Schedule Record. Each page of a schedule will have a new Schedule Record with the Page Number incremented. This record should appear in alphabetic order by Schedule type.

Field	Identification	Length	Description
(1)	Record ID	3	Value "SCH"
(2)	FILLER	1	Blank
(3)	Schedule Type	2	Alphanumeric (left justified) Values "Ab", "Bb" etc.
(4)	FILLER	1	Blank
(5)	Page Number	4	Value "PGnn" nn = 01 to 99
(6)	FILLER	1	Blank
(7)	SSN	9	Primary SSN
(8)	Data fields	various	Page 1 data fields

VI. FORM RECORD

The third series of records after Returns and Schedules are the Form records. They should appear in numeric order by form number. Each page of a form will have a new Form Record with the Page Number incremented.

Field	Identification	Length	Description
(1)	Record ID	3	Value "FRM"
(2)	FILLER	1	Blank
(3)	Form Number	6	Alphanumeric (left justified)
(4)	FILLER	1	Blank
(5)	Page Number	4	"PGnn" nn = 01 to 99
(6)	FILLER	1	Blank
(7)	SSN	9	Primary SSN
(8)	Data fields	various	Page 1 data fields

VII. STATEMENT RECORD

The statement record is the fourth series of records after Returns, Schedules and Forms. Statement records are used to continue a field or related series of fields which *appear on the same print line.* Each statement is given a sequential number from 00 to 99 in the order of appearance on the tax return. The first data field of the line items) being continued will contain "STMbnn" with "nn" being the sequential statement number. Each statement will consist of a series of records with LINE NUMBERS of 01 up to 50 for each sequential PAGE NUMBER. There is a maximum of 20 statement pages per return. After the control information there will be 80 characters of data for each line. The first line record (LN01) for each page of a statement will contain only the title of the item(s) being continued. The second line of each page (LN02) will contain the column titles for tabular data. For continuous non-tabular data (e.g., Number of Dependent Children) this line will be blank. The tabular column titles will be spaced in the same format as would be printed on a blank continuation page with the asterisk as the leftmost character of each column title (these will serve as "tabs" for the receiving program to line up data in the proper column). Related contiguous fields which would have appeared as a single print line on the basic form or schedule shall also appear on the same Statement line record, left justified, beginning with the third line record ("LN03") on. The first data field for a table or a group of related line entries (e.g., Interest or Dividends on Schedule B) must contain the "STMbnn" for the entire table (i.e., parrt of the table cannot appear on the form and part in a statement). Only fields marked with an asterisk in the record layout may contain "STMbnn".

Field	Identification	Length	Description
(1)	Record ID	3	Value "STM"
(2)	FILLER	1	Blank
(3)	Statement Number	2	nn Value 00-99
(4)	FILLER	1	Blank
(5)	Page Number	4	Value "PGnn" nn = 01 to 99
(6)	FILLER	1	Blank
(7)	Line Number	4	LNnn, nn = 01-50
(8)	FILLER	1	Blank
(9)	SSN	9	primary SSN
(10)	Data Record	80	Statement Title if "LN01"; column Titles and tab settings or blank if "LN02"; otherwise left justified field(s) from record being continued

VIII. SKIP PAGE RECORD

This short record may replace any page record in a Schedule or form for which there is no significant data.

Field	Identification	Length	Description
(1)	Record ID	3	Value "SCH", "FRM"
(2)	FILLER	1	Blank
(3)	Type	2 or 6	Schedule Identification Form Number
(4)	FILLER	1	Blank
(5)	Page Number	4	Value "PGnn" nn = page number
(6)	Filler	1	Blank
(7)	SSN	9	Numeric
(8)	Skip Indicator	2	Value "**"

IX. SUMMARY RECORD

The final record for each tax return is the summary record. (A "1" in the paper document indicator field shows that the paper document specified is a part of the return, and has been attached to the Taxpayer Declaration Form 8453.) The format is as follows:

Field	Identification	Length	Description
(1)	Record ID	3	Value "SUM"
(2)	FILLER	1	blank
(3)	Taxpayer's SSN	9	Primary SSN
(4)	Name of Preparer	35	Alphanumeric
(5)	Preparer's SSN	9	Numeric
(6)	Preparer Self-Employment Indicator	1	Alphanumeric ("x" if self employed), otherwise blank
(7)	Preparer Firm EIN	9	Numeric
(8)	Preparer Firm Name	35	Alphanumeric
(9)	Firm's City	20	Alphanumeric
(10)	Firm's State	2	Alpha
(11)	Firm's Zip	9	Numeric
(12)	Number of Logical Records in Tax Return (including Summary)	4	Numeric
(13)	Number of Schedules	2	(00-99) (Occurrences of "SCH")
(14)	Number of Forms	2	(00-99) (Occurrences of "FRM")
(15)	Number of Statements	2	(00-99) (Occurrences of "STM")
(16)	Paper Document Indicator 1	1	"1"=Form W-2, else "0"
(17)	Paper Document Indicator 2	1	"1 = Multiple Support Agreement (Form 2120), else "0"
(18)	Paper Document Indicator 3	1	"1" = Exemption for Non-Custodial Parent (Form 8332), else "0"
(19)	Paper Document Indicator 4	1	"1" = Physician's Certification of Blindness, else "0"
(20)	Paper Document Indicator 5	1	"1" = Physician's Certification of Disability (signed paper Sch. R), else "0"
(21)	Paper Document Indicator 6	1	"1" = W2-P, else "0"
(22)	Paper Document Indicator 7	1	"1" = W2-G, else "0"
(23)	Paper Document Indicator 8	1	"1" = Other Document(s), else "0"

X. RECAP RECORD

The final record on each file is the RECAP record. This record will contain a count of all returns in the file by type, and by a grand total. The format is as follows:

Field	Identification	Length	Description
(1)	Record ID	5	Value "RECAP"
(2)	Reserved	6	Numeric
(3)	Reserved	6	Numeric
(4)	Reserved	6	Numeric
(5)	Reserved	6	Numeric
(6)	Total Return Count	6	Numeric
(7)	Total Logical Data Records (not including TRANS and RECAP)	6	Numeric
(8)	Reserved	12	Numeric
(9)	Reserved	6	Numeric
(10)	Count of Refund Returns	6	Numeric
(11)	Electronic Transmitter Identification Number	7	Numeric
(12)	Julian date of transmission	3	Numeric
(13)	Transmission sequence number for Julian date in (12)	2	Numeric
(14)	Transmitter User Area	50	Filler (alphanumeric)

XI. FORMAT OF END OF RETURNS RECORD

Field	Identification	Length	Description
(1)	Record ID	2	Value P
(2)	Filler	2	Spaces
(3)	Today's Date	8	MM/DD/YY
(4)	Filler	2	Spaces
(5)	Time	5	Military, hours and minutes HH:MM
(6)	Filler	2	Spaces
(7)	Message	18	Value "End of Returns For"
(8)	Filler	1	Space
(9)	Transmitter's ID	5	Transmitter ID Number
(10)	Filler	2	Spaces
(11)	Constant	5	Value "TRANS"
(12)	Filler	1	Space
(13)	Electronic Transmitter Identification Number	7	Numeric
(14)	Julian date of transmission	3	Numeric
(15)	Transmission sequence number for Julian date in (14)	2	Numeric
(16)	Filler	11	Spaces

XII. FORMAT OF THE ACKNOWLEDGMENT FILE

The acknowledgment will be a transmission of a file consisting of the TRANS record submitted by the transmitter, an acknowledgment ("ACK") record for each recognizable return transmitted and the original "RECAP" record information submitted, plus counts for accepted and rejected records. For each transmission file sent during a transmission session, a separate ACK file will be transmitted back to the sender.

Further, if an ACK record contains an "R" in the Acceptance Code field, the return has been rejected due to a fatal error involving the return format, internal consistency, or data errors in a key field, and must also be corrected and resubmitted to the IRS to be considered as a filed return.

Any tax return with an "A" in the Acceptance Code field has been accepted as a filed tax return and will be processed from that point in the same manner as a return originally submitted on a paper document. This does not imply that the return will pass all IRS service center validity checks or post to the IRS Master File without delays.

The acknowledgement file can be a separate transmission or can precede or follow a return file transmission.

The first record on the acknowledgement file will be the same TRANS record as the first record of the tax return file being acknowleged. (see TRANS Record format above). For each recognizable tax return in the transmission an ACK record will be generated.

XIII. ACKNOWLEDGEMENT RECAP RECORD

After the ACK records, the final record of the file will be the RECAP record which is the final record of the tax return file being acknowledged with the addition of counts for accepted and rejected returns. The format for the ACK record is as follows:

Field	Identification	Length	Description
(1)	Record ID	3	Value "ACK"
(2)	Return Type	6	Item 3, Return Record (see IV. Tax Return General Specifications)
(3)	Primary Social Security Number	9	Numeric
(4)	Electronic Filer Identification Number (EFIN).	5	Numeric
(5)	Preparer's use to further identify originating office.	2	Alphanumeric
(6)	Julian date of transmission from originating office.	3	Numeric
(7)	Transmission sequence number for date specified in (6)	2	Numeric
(8)	Sequential number assigned return for transmission sequence in (7)	4	Numeric
(9)	Expected Refund	10	Refund field from applicable return
(10)	Acceptance Code	1	Value "A" Accepted "R" = Rejected
(11)	Date Accepted	6	Date of Acceptance (MMDDYY)
(12)	Time Accepted	4	Time of Acceptance
(13)	Error Counters		
	(a) Internal Inconsistency	2	Numeric 00-99
	(b) Control Data Error	2	Numeric 00-99
	(c) Key Field Data Error	2	Numeric 00-99

Error Counter Explanation

(a) Internal Inconsistency—The return's total number of records, forms, schedules or statements does not balance to totals in Summary Record, or left bottom line entries for schedules and forms do not coincide with return carry forward entries.

(b) Control Data Error—Erroneous data or sequence error(s) found in analyzing the control information at the beginning of each logical record.

(c) Key Field Data Error—Nonnumeric data found in social security number(s) or money fields, or significant data present in prohibited fields.

XIV. FORMAT OF THE ACKNOWLEDGMENT FILE RECAP RECORD

Field	Identification	Length	Description
(1)	Record ID	5	VALUE "RECAP"
(2)	Reserved	6	NUMERIC
(3)	Reserved	6	NUMERIC
(4)	Reserved	6	NUMERIC
(5)	Reserved	6	NUMERIC
(6)	Total Return Count	6	NUMERIC
(7)	Total Return Records	6	NUMERIC
(8)	Reserved	12	NUMERIC
(9)	Reserved	6	NUMERIC
(10)	Count of Refund Returns	6	NUMERIC
(11)	Total Returns Accepted	6	NUMERIC
(12)	Total Returns Rejected	6	NUMERIC

Fields 1-10 are identifical to those in the RECAP record originally transmitted. Fields 11 and 12 are the total returns accepted and rejected (counts of "A" and "R" codes from ACK record field 10, Acceptance Code).

XV. DATA VALIDATION AND REJECTION CRITERIA

The following data controls must be adhered to or the return shall be rejected:

A. The data records must be in the following sequence; Return, Schedule, Form, Statement and Summary.

B. Page records must be consecutive and sequential.

C. Schedule records must be in ascending alpha sequence.

D. Form records must be in ascending numeric sequence.

E. The primary social security number must be numeric and be consistent throughout all data records for a tax return.

F. The tax period must be "8512".

G. The format and content of the record identification information which begins each type of record must be exactly as presented in the input specifications.

H. Statement records do *not* have to be consecutive or in sequence but each statement number reference occuring in a data field ("STMbNN") must have a corresponding statement record. A statement record may be referenced multiple times but must be referenced at least once. There may be no more than 20 statement page records with any return.

I. Only one Schedule E with no more than three rental properties may be included in an electronic tax return.

J. Married filing joint and married filing separate returns must contain both a primary and a secondary SSN or the literal "NRA" instead of the secondary SSN indicating a non-resident alien spouse with no income or SSN.

K. There *must be no* significant data present for the following fields from the Form 1040 record:

SEQ #	Title	Line #
440	Business Income	12
450	Capital Gain/Loss	13
470	Supplemental Gain	15
520	Farm Income	19
610	Moving Expense	24
940	Residential Energy Credit	43
990	Foreign Tax Credit	47
1010	General Business Credit	48
1020	Business and Other	49
1040	Self-Employment Tax	51
1050	Alternative Minimum Tax	52
1060	Recapture Investment Credit	53
1080	Social Security on Tips	54
1090	Tax on IRA	55
1190	Form 4868 Amount	60
1210	Credit for Special Fuels Tax	62
1230	Regulated Investment Co.	63

L. There may be no significant entry for the Casualty field (Seq 370) of the Schedule A record.

M. The following fields must be equal (comparison of bottom line of schedule or form with return carry-forward line):

LINE FROM 1040 RECORD

SEQ #	Title	Line #	Sch/Form	SEQ #	Title	Line #
*380	Interest (If > $400)	8	Sch. B	290	Taxable Interest	3
*390	Dividends (If > $400)	9a	Sch. B	580	Taxable Dividends	10
510	Rents	18	Sch. E	1150	Total Income or loss	26
			or Sch. E	2010	Total Sup. Income	36
620	Employee Business Expense	25	2106	110	Line 7 More Than Line 8	9
700	Married Couple Deduction	30	W	120	Deduction	8
780	Excess Itemized	34a	Sch. A	550	Excess Itemized	26
925	Credit for Child & Dependent	41	2441	120	Line 7 + Line 8	9
930	Credit For Elderly	42	Sch. R	250	Credit	21

* Do not perform check unless amount exceeded.

N. If EIC, SEQ 1180 Form 1040 contains significant data, one or more Form W-2 records must be present for the return.

O. The format of the TRANS and the RECAP records must correspond exactly to those shown herein. Program accumulators will be maintained which correspond to the counters shown in the RECAP record. If they disagree at the end of processing the entire transmission will be rejected.

P. Accumulators will be maintained when processing each set of records for a tax return which corresponds to the counters in the SUMMARY record. If they disagree, the return will be rejected.

Q. "Child Care", "Medical", "Casualty" and "Theft" may not be present in Miscellaneous Deducations (Seq 420, 440, 460, 480 of Schedule A.

XVI. SPECIAL INSTRUCTIONS FOR ENTERING TAXPAYER'S NAME AND ADDRESS

These instructions must be carefully

followed to avoid delaying returns for error conditions. They must be included in preparers' programs as consistency tests and in the data entry instructions.

1. *Name Line 1*

A. Only alphabetic characters, spaces and the special characters Less-Than (<), ampersand (&) and hyphen (-) may appear in Name Line 1.

B. Only one intervening space may separate any component of a name line. The special character Less-Than replaces an intervening space to identify the primary taxpayer's last name.

C. All apostrophes and any other punctuation characters except hyphen must be omitted from names and the alphabetic characters shifted to the left in their place (e.g., O'Shea = OSHEA).

D. Numeric Characters in name components must be replaced by alphabetic Roman Numerals (e.g., Charles 3rd = CHARLES III

E. Enter a Less-Than (<) before the last name of the primary taxpayer. Enter a Less-Than after the name only if a title suffix follows (e.g., "MD" or "III", etc.). Do not enter a space before or after any Less-Than; the Less-Than takes the place of a space.

F. Enter first name, space, middle name or initial, Less-Than, last name. (The last name(s) of the individuals must be completed within this name line field.) If there is a suffix, enter a Less-Than between the last name and the suffix. Joint returns *must* contain one ampersand (&) between taxpayers' first names. The taxpayer whose first name is associated with the Primary SSN used on the return must be entered first and the last name of that taxpayer must be identified by a preceding Less-Than. If spouses use different last names, the primary taxpayer's first and last name appear first, with the last name bracketed by less-Thans followed by an ampersand and the full name of the spouse.

Examples	*Enter As*
Henry A. (Carter)*	HENRY A<CARTER
John A. and Jane B. (Smith)	JOHN A & Jane B<SMITH
Carl A. (Jones) & Angie Myer	CARL A<JONES<& ANGIE MYER
J. B. (Smith) Jr. & Ann Trent	J B <SMITH<JR & ANN TRENT
Florence E. (Jones) M. D.	FLORENCE E<JONES<M D
Alfred (Newman) Minor	ALFRED<NEWMAN<MINOR
Frank N. (De Porta)	FRANK N<DE PORTA
Lillie B. (Owen-Smith)	LILLIE B<OWEN-SMITH
John M (Brown), M.D.	JOHN M<BROWN<MD
James R. (O'Donnell)	JAMES R<ODONNELL
John C. (Brown), III	JOHN C<BROWN<III
Timothy (Jackson), 2nd	TIMOTHY<JACKSON<II
James (Oliver-Keogh), 3rd	JAMES<OLIVER-KEOGH<III

*Parentheses illustrate last name of taxpayer with primary SSN.

2. *Instructions for Street Address and Name Line 2*

A. Only alphabetic and numeric characters, ampersand (&), hyphen (-), percent (%) and spaces appear in the Street Address and Name Line 2 field.

B. Name Line 2 will be used for street addresses that require two lines or "In Care Of" address. An "In Care of" address must be indicated by a percent character (%) followed by the name which is in care of delivery.

C. Enter the house number and street, route number, post office box, or box number.

D. Abbreviate words requiring standard abbreviations unless the word is a proper name.

Examples	*Enter As*
South Court Street	S COURT ST
Circle Drive	CIRCLE DR
Lane Building	LANE BLDG
Northeast Street	NORTHEAST ST
Third Street	THIRD ST
3 Ave.	3RD AVE

E. If two addresses are present, enter the address shown immediately above or before the city and state in the Street Address field. This remaining address should be entered in the Name Line 2 field.

Example 1:	Mr. John Jones 801 N. Erie Street P.O. Box 1502 Toledo, OH 43603	
Enter As:	JOHN<JONES	(First Name Line)
	801 N ERIE ST	(Second Name Line)
	PO BOX 1502	(Street Address)
Example 2:	Mr. John Jones P.O. Box 1502 801 N. Erie St., Toledo, OH 43603	
Enter As:	JOHN<JONES	(First Name Line)
	PO BOX 1502	(Second Name Line)
	801 N ERIE ST	(Street Address)

F. Enter college, building, post office branch as the address if no mailing address is given.

G. If "In Care Of" is the mailing address, use the symbol "%" followed by a space.

Example: Mr. John Jones
In Care of Alice B. Smith
801 Brown St.

Enter As: JOHN<JONES (Name Line 1)
%ALICE SMITH (Name Line 22)
801 Brown St. (Street Address)

H. Do not use "#" symbol, "No.", and "Number" as a prefix to a house, apt., route, or P.O. Box.

I. Always add st, nd, rd, th, to a numbered street or avenue. Examples: 1 = 1ST; 2 = 2ND; 3 = 3RD, etc.

J. Enter 1/2 as 1/2 (no spaces).

K. Plurals for street, road, avenue, apartment, etc., will be entered as STS, RDS, AVES, APTS, etc.

L. Omit the letters "APO" and "FPO" for address. ZIP Code MUST be transcribed as five digits.

M. Space for all hyphens and periods in the address line.

N. Always use the following street abbreviations:

WORD	*ABBR.*
and	&
Air Force Base	AFB
Apartment	APT
Avenue	AVE
Boulevard	BLVD
Building	BLDG
Care of, or In care of	%
Circle	CL
Court	CT
Drive	DR
East	E
General Delivery	GEN DEL
Highway	HWY
Lane	LN
North	N
Northeast, N.E.	NE
Northwest, N.W.	NW
One-Half	1/2 (all fractions, space before and after the number, i.e., 1012 1/2 ST)
Parkway	PKY
Place	PL
Post Office Box, P.O. Box	PO BOX
Route, Rte.	RT
Road	RD
R.D., Rural Delivery, PFD, R.F.D., R.R. or Rural Route	R D
South	S
Southeast, S.E.	SE
Southwest, S.W.	SW
Street	ST
Terrace	TER
West	W

3. *Instructions for City-State and Zip Code Fields*

A. The City-State field may contain only alphabetic or numeric characters, ampersand, percent, slash or spaces.

B. The City-State field consists of the city followed by a slash and the valid code abbreviation *with no intervening spaces* between the city and state (e.g., NEW YORK/NY).

C. The following standard abbreviations for STATE CODE and corresponding three high order zip code digits must always be used.

STATE	*Abbrev.*	*Zip Code*
Alabama	AL	350–369
Alaska	AK	995–999
Arizona	AZ	850–865

STATE	*Abbrev.*	*Zip Code*
Arkansas	AR	716–729 & 755
California	CA	900–966
Colorado	CO	800–816
Connecticut	CT	060–069
Delaware	DE	196–199
District of Columbia	DC	200–205
Florida	FL	320–340 & 392
Georgia	GA	300–319
Hawaii	HI	967–968
Idaho	ID	832–838
Illinois	IL	600–629
Indiana	IN	460–479
Iowa	IA	500–528
Kansas	KS	600–679
Kentucky	KY	400–427
Louisiana	LA	700–714
Maine	ME	039–049
Maryland	MD	206–219
Massachusetts	MA	010–027
Michigan	MI	480–499
Minnesota	MN	550–567
Mississippi	MS	386–397
Missouri	MO	630–658
Montana	MT	590–599
Nebraska	NE	680–693
Nevada	NV	890–898
New Hampshire	NH	030–038
New Jersey	NJ	070–089
New Mexico	NM	870–884
New York	NY	090–149
North Carolina	NC	270–289
North Dakota	ND	580–588
Ohio	OH	430–458
Oklahoma	OK	730–749
Oregon	OR	970–979
Pennsylvania	PA	150–196
Rhode Island	RI	028–029
South Carolina	SC	290–299
South Dakota	SD	570–577
Tennessee	TN	370–385
Texas	TX	750–799
Utah	UT	840–847
Vermont	VT	050–059
Virginia	VA	220–246
Washington	WA	980–994
West Virginia	WV	247–268
Wisconsin	WI	530–549
Wyoming	WY	820–831

4. ***Special Instructions for Determining the IRS Name Control Field***

A. The Name Control consists of the first four significant characters of the individual's last name whose social security number is the Primary SSN for the return being filed. Disregard blanks between letters in the last name. Omit punctuation marks, titles and suffixes.

B. Consider certain foreign suffixes as part of the last name (i.e., Armah-Bey, Paz-Ayala, Allar-Sid). Particular attention must be given to those names which incorporate a mother's maiden name as a suffix to the last name. This practice is common in names of Spanish extraction. Consider the mother's maiden name as part of the surname for Name Control purposes.

Examples *Individual Name*	*Name Control*
John Brown	BROW
John Lea-Smith	LEA-
John Di Angelo	DIAN
John O'Neil	ONEI
John En, Sr.	EN
Pedro Paz-Ayala	PAZ-
Abdullah Allar-Sid	ALLA
Joe McCarty	MCCA
Juan de la Rosa Y Obregon	DELA

Examples *Individual Name*	*Name Control*
Jose Alvarado Nogales	ALVA
Donald Vander Neut	VAND
Otto Von Wodtke	VONW
Mary Smith & John Jones	SMIT

APPENDIX B

I. *Return Specification and Record Layouts*

An asterisk (*) precedes any field which may contain a statement reference (STMbnn) indicating either the first entry of a line or table of related items to be continued on a statement record.

Form 1040 for Tax Year 1985

Record Length Page 1: 990 Characters

Record Length Page 2: 681 Characters

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
000	Record ID		60	Value "RETb1040bbbPG01b8512b999999999N(30) (N=sequence # & DCN, 9 = Primary SSN)
007	Divorce Indicator		3	"DIV" or blank
009	Divorced SSN		9	SSN of divorced spouse for ES credit allocation
010	Primary SSN		9	Numeric (Your social security number, line 1)
020	Primary Date of Death		6	NO ENTRY
030	Secondary SSN		9	Numeric (Spouse social security number, line 2 or literal "NRAbbbbbb" if spouse is non-resident alien with no SSN or income)
040	Secondary Date of Death		6	NO ENTRY
050	Name Control		4	First 4 significant characters of Taxpayer's last name, no embedded spaces; allowable characters are alpha, hyphen, or space (see special instructions)
060	Name line 1		35	Alpha, Taxpayer's name, allowable special characters are: spaces, less-than (<), hyphen (-), ampersand (&) (See special instructions)
070	Name line 2		35	Alpha, in care of addressee, or address continuation. Allowable special characters are spaces, ampersand, hyphen, percent (%), (See special instructions)
080	Street address		35	Alphanumeric. Allowable special characters are spaces, ampersand, hyphen, and percent.
090	City/State code		25	Alphanumeric. Allowable special characters are ampersand, hyphen, percent, slash (/), and spaces. (Format is city followed by a / and the valid two character state abbreviation. See special instructions).
095	Zip Code		5	Numeric
100	Occupation		15	Alphanumeric
105	Spouse Occupation		15	Alphanumeric
110	PECF 1 Yes		1	Value "X" or "b"
120	PECF 2 Yes		1	Value "X" or "b"
130	Filing Status	1-5	1	Value 1, 2, 3, 4, or 5 (Applicable block, line 1-5)
140	Spouse's Name	3	25	Alpha (must be present if status 3, otherwise blank)
150	Qualifying Name for H of Household	4	25	Alpha or blank
155	Year Spouse Died	5	2	Numeric
160	Exempt Self	6a	1	Value "X" (1st block on line 6a)

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
170	Exempt 65/1	6a	1	Value "X" or blank (2nd block on line 6a)
180	Exempt Blind 1	6a		Value "X" or blank (3rd block on line 6b)
190	Exempt Spouse	6b	1	Value "X" or blank (1st block on line 6a)
200	Exempt 65/2nd	6b	1	Value "X" or blank (2nd block on line 6b)
210	Exempt Blind/2nd	6b	1	Value "X" or blank (3rd block on line 6b)
220	Pers. Exemption	6b	1	Values 1, 2, 3, 4, 5, or 6
*230	Names of Children Who Live With You	6c	35	Alpha (Names of children from 6c, separated by a comma and a blank (e.g. XXXX,bYYYYY))
240	Number of children	6c	2	Value 00-99 (Number of entries from 6c)
241	Agreement box		1	"X" or blank
*243	Names of Children Not Living With You	6d	35	Alpha (Names of children from 6d, separated by a comma and blank (e.g., XXXX,bYYYY))
247	Number Children	6d	2	Value 00-99 Number of children from 6d
*250	Other Dep. Name 1	6e(1)	25	Alpha/blank
260	Other Relation. 1	6e(2)	11	Values: "CHILD", "GRANDCHILD", "PARENT", "GRANDPARENT", "BROTHER", "SISTER", "AUNT", "UNCLE", "NEPHEW", "NIECE" or blank
270	Number months 1	6e(3)	2	Range 00-12, Db, Bb or blank
280	$1040 or more 1	6e(4)	1	"Y", "N" or blank
290	Half Support 1	6e(5)	1	"Y", "N" or blank
300	Other Dep. Name 2	6e(1)	25	See 250
310	Other Relation. 2	6e(2)	11	See 260
320	Number months 2	6e(3)	2	See 270
330	$1040 or more 2	6e(4)	1	See 280
340	Half Support 2	6e(5)	1	See 290
350	Number others	6e(6)	2	Value Range 00-99
360	Total Exempts	6f	2	Value Range 00-99
370	Fringe benefit indicator	7	2	"FB" or blank
375	Wages	7	12	Numeric
380	Interest	8	12	Numeric
390	Dividends	9a	12	Numeric
400	Exclusion	9b	12	Numeric
410	Tax Dividends	9c	12	Numeric
420	State Refund	10	12	Numeric
430	Alimony	11	12	Numeric
440	Business Income	12	12	NO ENTRY
450	Cap. Gain/Loss	13	12	NO ENTRY
460	40% Cap. Gain	14	12	Numeric
470	Other Gain	15	12	NO ENTRY
480	Taxable Pension	16	12	Numeric
490	Other Pensions	17a	12	Numeric
500	Taxable Amount	17b	12	Numeric
510	Rents	18	12	Numeric
520	Farm income	19	12	NO ENTRY

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
540	Total Unemploy.	20a	12	Numeric
550	Taxable Unemploy.	20b	12	Numeric
551	Repayment		9	Value "REPAYMENT"
552	Repayment Amount		12	Numeric
553	Social Security Benefits	21a	12	Numeric
555	Tax exempt interest amount	21b	12	Numeric
557	Taxable Amount of Social Security Income	21b	12	Numeric
*560	Nature of other Income		20	Value: "NOL", "GAMBLING", "PRIZES/AWARDS", "FEES (JURY, ETC.)", "MEDICAL REIMBURSEMENT", "TAXABLE GRANT," "FORGIVEN DEBT", "IN LIEU OF DIVIDENDS", "OTHER", or blank
570	Source of Other Income		20	Alphanumeric
590	Total Other Income	22	12	Numeric
600	Total Income	23	12	Numeric
610	Moving Expense	24	12	NO ENTRY
620	Employee Business Expense	25	12	Numeric
630	IRA Deduction	26	12	Numeric
650	Defined Benefit		2	Value "DB"
660	Keogh Deduction	27	12	Numeric
680	Early Withdrawal Penalty	28	12	Numeric
690	Recipient Last Name		15	Alpha
693	Recip. Soc. Sec. #		9	Numeric
697	Alimony Paid	29	12	Numeric
700	Married Couple Deduction	30	12	Numeric
*720	Other Adjustments		13	Values are "REFORESTATION", "SUB-PAYbTRA" or blank
730	Other Adjustment Amounts		12	Numeric
740	Total Adjustments	31	12	Numeric
750	Adjusted Gross Income	32	12	Numeric
760	Record ID		30	Value "RETb1040bbbPG02b8512bnnnnnnnnn" (n = SSN)
770	AGI Repeated	33	12	Numeric
780	Excess Itemized	34a	12	Numeric
785	Dependent Indicator	34a	1	"X" or blank
790	Charitable (Cash) Contributions	34b	12	Numeric
793	Char Contributions (Non-Cash)	34c	12	Numeric
795	Char. Cont. (Total)	34d	12	Numeric
797	Line 34d divided by 2	34e	12	Numeric
800	Line 33 Less 34a or 34e	35	12	Numeric
810	Exemption Amount	36	12	Numeric
820	Taxable Income	37	12	Numeric
830	Tax Table Block	38	1	"X" or blank

Field No.	Identification	Form Ref.	Length	Field Description
840	Rate Schedule Block	38	1	"X" or blank
850	Schedule G Block	38	1	NO ENTRY
860	Tax	38	12	Numeric
870	Form 4970 Block	39	1	NO ENTRY
880	Form 4972 Block	39	1	NO ENTRY
890	Form 5544 Block	39	1	NO ENTRY
910	Additional Taxes	39	12	NO ENTRY
920	Total Taxes Before Credits	40	12	Numeric
925	Credit for Child & Dependent	41	12	Numeric
930	Credit for Elderly	42	12	Numeric
940	Residential Energy Credit	43	12	NO ENTRY
960	Polit. Contribs.	44	12	Numeric
970	Total Pers. Credits	45	12	Numeric
980	Tax Less Pers. Creds.	46	12	Numeric
990	Foreign Tax Credit	47	12	NO ENTRY
*1000	General Business Cred. Description		18	NO ENTRY
1003	Form 3800 Block		1	NO ENTRY
1005	Form 3468 Block		1	NO ENTRY
1007	Form 5884 Block		1	NO ENTRY
1009	Form 6874 Block		1	NO ENTRY
*1010	General Business Credit	48	12	NO ENTRY
1020	Business & Other	49	12	NO ENTRY
1030	Tax Less Business & Other Credits	50	12	Numeric
1040	Self Employment Tax	51	12	NO ENTRY
1050	Alternative Minimum Tax	52	12	NO ENTRY
1060	Recapture Investment Credit	53	12	NO ENTRY
1070	Railroad Retire. indicator		4	NO ENTRY
1080	Social Security on Tips	54	12	NO ENTRY
1090	Tax on IRA	55	12	NO ENTRY
1110	Other Tax Indicators		4	"AEIC" "EPPb" "S72P" or blank
1120	AEIC Amount		12	Numeric
1130	Total Tax	56	12	Numeric
1140	1099 Indicator		9	"FORMb1099" or blank
1150	1099 Amount		12	Numeric
1160	Withholding	57	12	Numeric
1170	ES Payments	58	12	Numeric
1180	EIC	59	12	Numeric
1185	Child's name		15	Alpha
1190	Form 4868 Amount	60	12	NO ENTRY
1200	Excess SS Tax	61	12	Numeric
1210	Credit for Special Fuels Tax	62	12	NO ENTRY
1220	Form 4469 Indic.		9	NO ENTRY

Field No.	Identification	Form Ref.	Length	Field Description
1225	4469 Amount		12	NO ENTRY
1230	Regulated Investment Co.	63	12	NO ENTRY
1240	Overpaid Windfall Indicator		28	NO ENTRY
1245	Overpaid Windfall Amount		12	NO ENTRY
1250	Total Payments	64	12	Numeric
1260	Overpaid	65	12	Numeric
1270	Refund	66	12	Numeric
1280	Applied to ES	67	12	Numeric
1290	Amount Owed	68	12	NO ENTRY
1300	Form 2210 Indic.		1	NO ENTRY
1310	ES Penalty Amount		12	NO ENTRY
1320	Remittance		12	NO ENTRY

II. *Tax Schedule Record Specifications*

A. *Schedule A*

Record Length 855 Characters

Field No.	Identification	Form Ref.	Length	Field Description
000	Record ID		21	Value "SCHbAbbPG01bnnnnnnnnn" (n = SSN)
005	Alternative Min. Tax Indicator		1	NO ENTRY
010	Medicine/Drugs	1	12	Numeric
020	Doctors, Etc.	2a	12	Numeric
030	Transportation	2b	12	Numeric
*040	Other Medical Type 1	2c	20	Alphanumeric
041	Other Medical Amount 1	2c	12	Numeric
042	Other Medical Type 2	2c	20	Alphanumeric
043	Other Medical Amount 2	2c	12	Numeric
050	Other Total	2c	12	Numeric
060	Total 1 thru 2c	3	12	Numeric
070	5% of AGI	4	12	Numeric
080	Total Medical	5	12	Numeric
090	State & Local	6	12	Numeric
100	Real Estate	7	12	Numeric
110	General Sales	8a	12	Numeric
120	Motor Vehicles	8b	12	Numeric
*130	Other Tax Type	9	20	Alphanumeric
140	Total Other Tax Amount	9	12	Numeric
150	Total Taxes	10	12	Numeric
160	Mortgage Interest to a Financial Institution	11a	12	Numeric
*170	Individual Mortgage Name	11b	20	Alphanumeric
180	Individual Mortgage Address	11b	35	Alphanumeric
190	Indiv. Mortgage Interest Amount	11b	12	Numeric

Field No.	Identification	Form Ref.	Length	Field Description
200	Credit Cards/Charges	12	12	Numeric
*210	Other Interest Type 1	13	20	Alphanumeric
220	Other Interest Amount 1	13	12	Numeric
230	Other Interest Type 2	13	20	Alphanumeric
240	Other Interest Amount 2	13	12	Numeric
250	Other Interest Type 3	13	20	Alphanumeric
260	Other Interest Amount 3	13	12	Numeric
270	Other Interest Type 4	13	20	Alphanumeric
280	Other Interest Amount 4	13	12	Numeric
285	Total Other Interest	13	12	Numeric
290	Total Interest	14	12	Numeric
300	Cash Contributions	15a	12	Numeric
*310	Cash Over $3000 Org 1	15b	20	Alphanumeric
320	Cash Over $3000 Amount 1	15b	12	Numeric
330	Cash Over $3000 Org 2	15b	20	Alphanumeric
340	Cash Over $3000 Amount 2	15b	12	Numeric
350	Total Cash Over $3000	15b	12	Numeric
360	Non-cash	16	12	Numeric
370	Carryover	17	12	Numeric
380	Total Contributions	18	12	Numeric
390	Casualty	19	12	NO ENTRY
400	Union Dues	20	12	Numeric
410	Return Preparation Fee	21	12	Numeric
*420	Other Misc 1	22	20	Alphanumeric
430	Other Misc Amt 1	22	12	Numeric
440	Other Misc 2	22	20	Alphanumeric
450	Other Misc Amt 2	22	12	Numeric
460	Other Misc 3	22	20	Alphanumeric
470	Other Misc Amt 3	22	12	Numeric
480	Other Misc 4	22	20	Alphanumeric
490	Other Misc Amt 4	22	12	Numeric
500	Total Other Misc	22	12	Numeric
510	Total Misc	23	12	Numeric
520	Total Deductions	24	12	Numeric
530	Zero Bracket Amt.	25	12	Numeric
540	Must Itemize Indicator		2	"TC" or blank
550	Excess Itemized	26	12	Numeric

B. *Schedule B*

Record Length 915 Characters

Field No.	Identification	Form Ref.	Length	Field Description
000	Record ID		21	Value "SCHbBbbPG01bnnnnnnnnn" (n = SSN)

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
*010	Seller Financed Mortgage Name	1	25	Alphanumeric
020	Seller Financed Mortgage Amt.	1	12	Numeric
*030	Interest Payer 1	2	20	Alphanumeric
040	Interest Amount 1	2	12	Numeric
050	Interest Payer 2	2	20	Alphanumeric
060	Interest Amount 2	2	12	Numeric
070	Interest Payer 3	2	20	Alphanumeric
080	Interest Amount 3	2	12	Numeric
090	Interest Payer 4	2	20	Alphanumeric
100	Interest Amount 4	2	12	Numeric
110	Interest Payer 5	2	20	Alphanumeric
120	Interest Amount 5	2	12	Numeric
130	Interest Payer 6	2	20	Alphanumeric
140	Interest Amount 6	2	12	Numeric
150	Interest Payer 7	2	20	Alphanumeric
155	Interest Amount 7	2	12	Numeric
160	Interest Payer 8	2	20	Alphanumeric
170	Interest Amount 8	2	12	Numeric
220	Interest Subtotal	2	12	Numeric
230	Nominee Literal	2	20	"NOMINEEbDISTRIBUTION" or blank
240	Nominee Amount	2	12	Numeric
250	Accrued Interest Literal	2	16	"ACCRUEDbINTEREST" or blank
260	Accrued Interest Amount	2	12	Numeric
270	Tax-Exempt Literal	2	19	"TAX-EXEMPTbINTEREST" or blank
280	Tax Exempt Amount	2	12	Numeric
285	OID Adjustment Literal	2	14	"OID ADJUSTMENT"
287	OID Amount	2	12	Numeric
290	Taxable Interest	3	12	Numeric
*300	Dividend Payer 1	4	20	Alphanumeric
310	Dividend Amount 1	4	12	Numeric
320	Dividend Payer 2	4	20	Alphanumeric
330	Dividend Amount 2	4	12	Numeric
340	Dividend Payer 3	4	20	Alphanumeric
350	Dividend Amount 3	4	12	Numeric
360	Dividend Payer 4	4	20	Alphanumeric
370	Dividend Amount 4	4	12	Numeric
380	Dividend Payer 5	4	20	Alphanumeric
390	Dividend Amount 5	4	12	Numeric
400	Dividend Payer 6	4	20	Alphanumeric
410	Dividend Amount 6	4	12	Numeric
420	Dividend Payer 7	4	20	Alphanumeric

Field No.	Identification	Form Ref.	Length	Field Description
430	Dividend Amount 7	4	12	Numeric
440	Dividend Payer 8	4	20	Alphanumeric
450	Dividend Amount 8	4	12	Numeric
460	Dividend Payer 9	4	20	Alphanumeric
470	Dividend Amount 9	4	12	Numeric
480	Dividend Payer 10	4	20	Alphanumeric
490	Dividend Amount 10	4	12	Numeric
500	Dividend Subtotal	4	12	Numeric
510	Nominee Literal	4	20	“NOMINEEbDISTRIBUTION” or blank
520	Nominee Amount	4	12	Numeric
530	Total Dividends	5	12	Numeric
540	Capital Gains	6	12	Numeric
550	Nontaxable Distribution	7	12	Numeric
560	Qualified Reinvestment	8	12	Numeric
570	Total Nontaxable Dividends	9	12	Numeric
580	Taxable Dividends	10	12	Numeric
590	Foreign Account Questions	11	2	“Xb” or “bX” (first X = YES, 2nd X = NO)
600	Foreign Country	11	20	Alphanumeric
610	Foreign Trust Question	12	2	“Xb” or “bX” (first X = YES, 2nd X = NO)

C. *Schedule E*

Record Length Page 1: 1,529 Characters
Record Length Page 2: 939 Characters

Field No.	Identification	Form Ref.	Length	Field Description
000	Record ID		21	“SCHbEbbPG01bnnnnnnnnn” (n=SSN)
010	Property Kind	A-1	20	Alphanumeric
020	Prop. Address	A-1	30	Alphanumeric
030	Personal Use—Yes	A-2	1	“X” or blank
035	Personal Use—No	A-2	1	“X” or blank
040	Property Kind	B-1	20	Alphanumeric
050	Prop. Address	B-1	30	Alphanumeric
060	Personal Use—Yes	B-2	1	“X” or blank
065	Personal Use—No	B-2	1	“X” or blank
070	Property Kind	C-1	20	Alphanumeric
080	Prop. Address	C-1	30	Alphanumeric
090	Personal Use—Yes	C-2	1	“X” or blank
095	Personal Use—No	C-2	1	“X” or blank
100	Rents Received A	A-3a	12	Numeric
110	Rents Received B	B-3a	12	Numeric
120	Rents Received C	C-3a	12	Numeric
130	Royalties Received A	A-3b	12	Numeric
140	Royalties Rec’d B	B-3b	12	Numeric
150	Royalties Rec’d C	C-3b	12	Numeric

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
160	Total Rent/Royalty	3	12	Numeric
170	Advertising A	A-4	12	Numeric
180	Advertising B	B-4	12	Numeric
190	Advertising C	C-4	12	Numeric
200	Auto-Travel A	A-5	12	Numeric
210	Auto-Travel B	B-5	12	Numeric
220	Auto-Travel C	C-5	12	Numeric
230	Cleaning-Maint. A	A-6	12	Numeric
240	Cleaning-Maint. B	B-6	12	Numeric
250	Cleaning-Maint. C	C-6	12	Numeric
260	Commissions A	A-7	12	Numeric
270	Commissions B	B-7	12	Numeric
280	Commissions C	C-7	12	Numeric
290	Insurance A	A-8	12	Numeric
300	Insurance B	B-8	12	Numeric
310	Insurance C	C-8	12	Numeric
320	Legal-Pro Fees A	A-9	12	Numeric
330	Legal-Pro Fees B	B-9	12	Numeric
340	Legal-Pro Fees C	C-9	12	Numeric
350	Mortgage Interest A	A-10	12	Numeric
360	Mortgage interest B	B-10	12	Numeric
370	Mortgage Interest C	C-10	12	Numeric
380	Total Mort. Interest	10	12	Numeric
390	Other Interest A	A-11	12	Numeric
400	Other Interest B	B-11	12	Numeric
410	Other Interest C	C-11	12	Numeric
420	Repairs A	A-12	12	Numeric
430	Repairs B	B-12	12	Numeric
440	Repairs C	C-12	12	Numeric
450	Supplies A	A-12	12	Numeric
460	Supplies B	B-12	12	Numeric
470	Supplies C	C-12	12	Numeric
480	Taxes A	A-13	12	Numeric
490	Taxes B	B-13	12	Numeric
500	Taxes C	C-13	12	Numeric
510	Utilities A	A-14	12	Numeric
520	Utilities B	B-14	12	Numeric
530	Utilities C	C-14	12	Numeric
540	Wages—Salaries A	A-16	12	Numeric
550	Wages—Salaries B	B-16	12	Numeric
560	Wages—Salaries C	C-16	12	Numeric
*570	Other—Description 1	A-17-1	20	Alphanumeric
580	Other Amount A	A-17-1	12	Numeric

Field No.	Identification	Form Ref.	Length	Field Description
590	Other Amount B	B-17-1	12	Numeric
600	Other Amount C	C-17-1	12	Numeric
610	Other—Description 2	A-17-2	20	Alphanumeric
620	Other Amount A	A-17-2	12	Numeric
630	Other Amount B	B-17-2	12	Numeric
640	Other Amount C	C-17-2	12	Numeric
650	Other—Description 3	A-17-3	20	Alphanumeric
660	Other Amount A	A-17-3	12	Numeric
670	Other Amount B	B-17-3	12	Numeric
680	Other Amount C	C-17-3	12	Numeric
690	Other—Description 4	A-17-4	20	Alphanumeric
700	Other Amount A	A-17-4	12	Numeric
710	Other Amount B	B-17-4	12	Numeric
720	Other Amount C	C-17-4	12	Numeric
730	Other—Description 5	A-17-5	20	Alphanumeric
740	Other Amount A	A-17-5	12	Numeric
750	Other Amount B	B-17-5	12	Numeric
760	Other Amount C	C-17-5	12	Numeric
770	Other—Description 6	A-17-6	20	Alphanumeric
780	Other Amount A	A-17-6	12	Numeric
790	Other Amount B	B-17-6	12	Numeric
800	Other Amount C	C-17-6	12	Numeric
810	Other—Description 7	A-17-7	20	Alphanumeric
820	Other Amount A	A-17-7	12	Numeric
830	Other Amount B	B-17-7	12	Numeric
840	Other Amount C	C-17-7	12	Numeric
850	Other—Description 8	A-17-8	20	Alphanumeric
860	Other Amount A	A-17-8	12	Numeric
870	Other Amount B	B-17-8	12	Numeric
880	Other Amount C	C-17-8	12	Numeric
890	Other—Description 9	A-17-9	20	Alphanumeric
900	Other Amount A	A-17-9	12	Numeric
910	Other Amount B	B-17-9	12	Numeric
920	Other Amount C	C-17-9	12	Numeric
930	Other—Description 10	A-17-10	20	Alphanumeric
940	Other Amount A	A-17-10	12	Numeric
950	Other Amount B	B-17-10	12	Numeric
960	Other Amount C	C-17-10	12	Numeric
970	Tot Expenses Less Deprec A	A-18	12	Numeric
980	Tot Expenses Less Deprec B	B-18	12	Numeric

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
990	Tot Expenses Less Deprec C	C-18	12	Numeric
1000	Tot Expenses Less Deprec	18	12	Numeric
1010	Deprec Expense A	A-19	12	Numeric
1020	Deprec Expense B	B-19	12	Numeric
1030	Deprec Expense C	C-19	12	Numeric
1040	Total Depreciation	19	12	Numeric
1050	Total Expenses A	A-20	12	Numeric
1060	Total Expenses B	B-20	12	Numeric
1070	Total Expenses C	C-20	12	Numeric
1080	Net Rental Income (Loss) A	A-21	12	Numeric
1090	Net Rental Income (Loss) B	B-21	12	Numeric
1100	Net Rental Income (Loss) C	C-21	12	Numeric
1110	Total Profits	22	12	Numeric
1120	Total Losses	23	12	Numeric
1130	Net Profit (Loss)	24	12	Numeric
1140	Net Farm Rental Profit-Loss	25	12	NO ENTRY
1150	Total Income or Loss	26	12	Numeric
1160	Record ID		21	“SCHbEbbPG02bnnnnnnnnn”
*1170	Partnership Name 1	P-A-1	20	Alphanumeric
1172	Appropriate Code	P-B-1	1	“P” or “S”
1174	Foreign Partner	P-C-1	1	“X” = Yes, “ ” = No
1176	Partnership EIN	P-D-1	9	Numeric
1180	Partner. Net Loss	P-E-1	12	Numeric
1190	Partner. Net Income	P-F-1	12	Numeric
1200	Partnership Name 2	P-A-2	20	Alphanumeric
1210	Appropriate Code	P-B-2	1	“P” or “S”
1220	Foreign Partner	P-C-2	1	“X” = Yes, “ ” = No
1230	Partnership EIN	P-D-2	9	Numeric
1240	Partner. Net Loss	P-E-2	12	Numeric
1250	Partner. Net Income	P-F-2	12	Numeric
1260	Partnership Name 3	P-A-3	20	Alphanumeric
1270	Appropriate Code	P-B-3	1	“P” or “S”
1280	Foreign Partner	P-C-3	1	“X” = Yes, “ ” = No
1290	Partnership EIN	P-D-3	9	Numeric
1300	Partner. Net Loss	P-E-3	12	Numeric
1310	Partner. Net Income	P-F-3	12	Numeric
1320	Partnership Name 4	P-A-4	20	Alphanumeric
1330	Appropriate Code	P-B-4	1	“P” or “S”
1340	Foreign Partner	P-C-4	1	“X” = Yes, “ ” = No
1350	Partnership EIN	P-D-4	9	Numeric
1360	Partner. Net Loss	P-E-4	12	Numeric
1370	Partner. Net Income	P-F-4	12	Numeric

Field No.	Identification	Form Ref.	Length	Field Description
1380	Partnership Name 5	P-A-5	20	Alphanumeric
1390	Appropriate Code	P-B-5	1	"P" or "S"
1400	Foreign Partner	P-C-5	1	"X" = Yes, " " = No
1410	Partnership EIN	P-D-5	9	Numeric
1420	Partner. Net Loss	P-E-5	12	Numeric
1430	Partner. Net Income	P-F-5	12	Numeric
1440	Partnership Name 6	P-A-5	20	Alphanumeric
1450	Appropriate Code	P-B-5	1	"P" or "S"
1460	Foreign Partner	P-C-5	1	"X" = Yes, " " = No
1470	Partnership EIN	P-D-5	9	Numeric
1480	Partner. Net Loss	P-E-5	12	Numeric
1490	Partner. Net Income	P-F-5	12	Numeric
1500	Partnership Name 7	P-A-5	20	Alphanumeric
1510	Appropriate Code	P-B-5	1	"P" or "S"
1520	Foreign Partner	P-C-5	1	"X" = Yes, " " = No
1530	Partnership EIN	P-D-5	9	Numeric
1540	Partner. Net Loss	P-E-5	12	Numeric
1550	Partner. Net Income	P-F-5	12	Numeric
1560	Partnership Name 8	P-A-5	20	Alphanumeric
1570	Appropriate Code	P-B-5	1	"P" or "S"
1580	Foreign Partner	P-C-5	1	"X" = Yes, " " = No
1590	Partnership EIN	P-D-5	9	Numeric
1600	Partner. Net Loss	P-E-5	12	Numeric
1610	Partner. Net Income	P-F-5	12	Numeric
1620	Partnership Name 9	P-A-5	20	Alphanumeric
1630	Appropriate Code	P-B-5	1	"P" or "S"
1640	Foreign Partner	P-C-5	1	"X" = Yes, " " = No
1650	Partnership EIN	P-D-5	9	Numeric
1660	Partner. Net Loss	P-E-5	12	Numeric
1670	Partner. Net Income	P-F-5	12	Numeric
1680	Partnership Name 10	P-A-5	20	Alphanumeric
1690	Appropriate Code	P-B-5	1	"P" or "S"
1700	Foreign Partner	P-C-5	1	"X" = Yes, " " = No
1710	Partnership EIN	P-D-5	9	Numeric
1720	Partner. Net Loss	P-E-5	12	Numeric
1730	Partner. Net Income	P-F-5	12	Numeric
1740	Total Partner Loss	27e	12	Numeric
1750	Tot Partner Income	27f	12	Numeric
1760	Net Income or Loss	28	12	Numeric
1770	Deduction 179 Prop	29	12	Numeric
1780	Total Partner Income (Loss)	30	12	Numeric
*1790	Estate Name 1	E-A-1	20	Alphanumeric
1800	Estate EIN	E-C-1	9	Numeric

Field No.	Identification	Form Ref.	Length	Field Description
1810	Estate Net Loss	E-D-1	12	Numeric
1820	Estate Net Income	E-E-1	12	Numeric
1830	Estate Name 2	E-A-2	20	Alphanumeric
1840	Estate EIN	E-C-2	9	Numeric
1850	Estate Net Loss	E-D-2	12	Numeric
1860	Estate Net Income	E-E-2	12	Numeric
1870	Estate Name 3	E-A-3	20	Alphanumeric
1880	Estate EIN	E-C-3	9	Numeric
1890	Estate Net Loss	E-D-3	12	Numeric
1900	Estate Net Income	E-E-3	12	Numeric
1910	Estate Name 4	E-A-3	20	Alphanumeric
1920	Estate EIN	E-C-3	9	Numeric
1930	Estate Net Loss	E-D-3	12	Numeric
1940	Estate Net Income	E-E-3	12	Numeric
1950	Total Estate Loss	31e	12	Numeric
1960	Tot Estate Income	31f	12	Numeric
1970	Total Estate Net Income (Loss)	32	12	Numeric
1980	Windfall Profit Credit Rec 1985	33	12	Numeric
1990	Windfall Profit Withheld in 1985	34	12	Numeric
2000	Total Windfall Profit Credit	35	12	Numeric
2010	Total Supplemental Income (Loss)	36	12	Numeric
2020	Farming/Fishing Share	37	12	Numeric

D. *Schedule R*

Record Length Page 1: 33 Characters
Record Length Page 2: 153 Characters

Field No.	Identification	Form Ref.	Length	Field Description
000	Record ID		21	Value "SCHƀRƀƀPG01ƀnnnnnnnnn" (n = SSN)
010	Over 65	1	1	"X" or Blank
020	Retire/Disabled	2	1	"X" or Blank
030	Both Over 65	3	1	"X" or Blank
040	Both Under 65, One Retired	4	1	"X" or Blank
050	Both Under 65, Both Retired	5	1	"X" or Blank
060	One Over 65, Other Retired	6	1	"X" or Blank
070	One Over 65, Other Not Retired	7	1	"X" or Blank
080	Over 65, Did Not Live With Spouse	8	1	"X" or Blank
090	Under 65, Did Not Live With Spouse	9	1	"X" or Blank
100	Prior Year Start Indicator	II2	1	"X" or Blank

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
110	At Least One Year	II2a	1	"X" or Blank
120	Permanent Disability	II2b	1	"X" or Blank
130	Record ID		21	Value "SCHbRbbPG02bnnnnnnnnn" (n = SSN)
140	Write Amount	10	12	Numeric
150	Taxable Disability	11	12	Numeric
160	Smaller Amount	12	12	Numeric
170	Pensions & Annuit.	13	12	Numeric
180	Amount 1040, Line 33	14	12	Numeric
190	Write 7500, 10000, or 5000	15	12	Numeric
200	Line 14–Line 15	16	12	Numeric
210	Line 16 Divided by 2	17	12	Numeric
220	Line 13 + Line 17	18	12	Numeric
230	Line 12–Line 18	19	12	Numeric
250	Credit	21	12	Numeric

E. *Schedule W*

Record length 165 Characters

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
000	Record ID		21	Value "SCHbWbbPG01bnnnnnnnnn" (n = SSN)
010	Wages	1(a)	12	Numeric
020	Spouses Wages	1(b)	12	Numeric
030	Self-employment	2(a)	12	Numeric
040	Spouses Self-employment	2(b)	12	Numeric
050	Earned Income	3(a)	12	Numeric
060	Spouses Earned Income	3(b)	12	Numeric
070	Adjustments	4(a)	12	Numeric
080	Spouses Adjustments	4(b)	12	Numeric
090	Qualified Income	5(a)	12	Numeric
100	Spouses Qualified Income	5(b)	12	Numeric
110	Smaller Income	6	12	Numeric
120	Deduction	8	12	Numeric

III. *Form Record Specifications*

A. *Form W-2*

Record Length 116 Characters

(This form does not contain all fields from the printed form but only the selected items shown.)

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
010	Record ID		25	Value "FRMbW-2bbbbPG01bnnnnnnnnn" (n = Primary SSN from Form 1040)
020	Employer Name	2	35	Alphanumeric
030	Employer Identification Number	3	9	Numeric
040	SSN	8	9	Numeric (W-2 Social Security Number)

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
050	Withholding	9	12	Numeric
060	Wages	10	12	Numeric
070	Social Security Tax	11	12	Numeric
080	Non-Standard Indicator		1	Value "Y" or "N" (Y = W-2 has been hand prepared or hand altered)
090	Fringe Benefit Indicator		1	"X" or blank

B. *Form W-2G*

Record Length 103 Characters

(This form does not contain all fields from the printed fonn but only the selected items shown.)

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
010	Record ID		25	Value "FRMbW-2GbbbPG01bnnnnnnnnn" (n = Primary SSN from Form 1040)
020	Payer Name		35	Alphanumeric
030	Payer Identific. Number		9	Numeric
040	Gross Winnings etc.	1	12	Numeric
050	Withholding	2	12	Numeric
060	SSN	9	9	Numeric (W-2G Social Sec. No.)
070	Non-Standard Indicator		1	Value "Y" or "N" (Y = W-2G was hand prepared or hand altered)

C. *Form W-2P*

Record Length 115 Characters

(This form does not contain all fields from the printed form but only the selected items shown.)

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
010	Record ID		25	Value "FRMbW-2PbbbPG01bnnnnnnnnn" (n = Primary SSN from Form 1040)
020	Payer Name	2	35	Alphanumeric
030	Payer Identific. Number	3	9	Numeric
040	SSN	8	9	Numeric (W-2P Social Sec. No.)
050	Annuity, Pension etc.	9	12	Numeric
060	Taxable Amount	10	12	Numeric
070	Withholding	11	12	Numeric
080	Non-Standard Indicator		1	Value "Y" or "N" (Y = W-2P was hand prepared or hand altered)

D. *Form 2106*

Record Length 699 Characters

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
000	Record ID		25	Value "FRMb2106bbbPG01bnnnnnnnnn" (n = Primary SSN from Form 1040)
005	Occupation		15	Alpha Numeric
010	Vehicle Expenses	1-1	12	Numeric

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
020	Fees, Tolls	1-2	12	Numeric
030	Transportation	1-3	12	Numeric
040	Travel Expenses	1-4	12	Numeric
050	RESERVED		12	NO ENTRY
060	RESERVED		12	NO ENTRY
070	Reimbursed	1-5	12	Numeric
080	Expenses	1-6	12	Numeric
090	Add Lines 1 thru 6	1-7	12	Numeric
100	Reimbursements	1-8	12	Numeric
110	7 More Than 8	1-9	12	Numeric
120	8 More Than 7	1-10	12	Numeric
130	Vehicle Date (1)	2-1	6	Numeric (MMDDYY)
140	Vehicle Date (2)	2-1	6	Numeric (MMDDYY)
150	Total Miles (1)	2-2	12	Numeric
160	Total Miles (2)	2-2	12	Numeric
170	Business Miles (1)	2-3	12	Numeric
180	Business Miles (2)	2-3	12	Numeric
190	Percent of Use (1)	2-4	2	Numeric
200	Percent of Use (2)	2-4	2	Numeric
210	Average Distance (1)	2-5	12	Numeric
220	Average Distance (2)	2-5	12	Numeric
230	Miles Commuting (1)	2-6	12	Numeric
240	Miles Commuting (2)	2-6	12	Numeric
250	Other Mileage (1)	2-7	12	Numeric
260	Other Mileage (2)	2-7	12	Numeric
270	Another Vehicle Yes	2-8	1	"X" or blank
275	Another Vehicle No	2-8	1	"X" or blank
280	Personal Use Yes	2-9	1	"X" or blank
283	Personal Use No	2-9	1	"X" or blank
285	Personal Use Not Applicable	2-9	1	"X" or blank
290	Evidence Yes	2-10	1	"X" or blank
295	Evidence No	2-10	1	"X" or blank
300	Written Yes	2-10	1	"X" or blank
305	Written No	2-10	1	"X" or blank
310	Smaller	2-11	12	Numeric
320	Line 11 from Line 3	2-12	12	Numeric
330	Line 11 × .205	2-13	12	Numeric
340	Line 12 × .11	2-14	12	Numeric
350	Line 13 + Line 14	2-15	12	Numeric
360	Gas, Oil (1)	2-16	12	Numeric
370	Gas, Oil (2)	2-16	12	Numeric
380	Rentals (1)	2-17	12	Numeric

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
390	Rentals (2)	2-17	12	Numeric
400	Value (1)	2-18	12	Numeric
410	Value (2)	2-18	12	Numeric
420	Add Lines 16-18 (1)	2-19	12	Numeric
430	Add Lines 16-18 (2)	2-19	12	Numeric
440	Line 19 × Line 4 Percent (1)	2-20	12	Numeric
450	Line 19 × Line 4 Percent (2)	2-20	12	Numeric
460	Depreciation (1)	2-21	12	Numeric
470	Depreciation (2)	2-21	12	Numeric
480	Line 20 + Line 21 (1)	2-22	12	Numeric
490	Line 20 + Line 21 (2)	2-22	12	Numeric
500	Vehicle 1 Basis	a	12	Numeric
510	Vehicle 1 Recovery	b	12	Numeric
520	Vehicle 1 Method	c	11	Alphanumeric
530	Vehicle 1 Depreciat.	d	12	Numeric
540	Vehicle 1 179	e	12	Numeric
550	Vehicle 1 Total	f	12	Numeric
560	Vehicle 2 Basis	a	12	Numeric
570	Vehicle 2 Recovery	b	12	Numeric
580	Vehicle 2 Method	c	11	Alphanumeric
590	Vehicle 2 Depreciat.	d	12	Numeric
600	Vehicle 2 179	e	12	Numeric
610	Vehicle 2 Total	f	12	Numeric

E. *Form 2441*

Record Length 138 Characters

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
000	Record ID	0	25	Value "FRMb244lbbbPG01bnnnnnnnnn"
010	Qualifying Person	1	2	Numeric
020	$50 or More Question	2a	2	Value "Xb", "bX" or "bb" (first x = YES, 2nd x = NO)
030	Wage Tax Return Question	2b	2	Value "b", "b" or "bb" (first x = YES, 2nd x = NO)
035	EIN	2c	9	Numeric
040	Expenses	3	12	Numeric
050	Earned Income	4a	12	Numeric
060	Spouses Income	4b	12	Numeric
070	Smaller Income	4c	12	Numeric
080	Smaller of Expense or Income	5	12	Numeric
090	Applicable Percentage	6	2	Numeric
100	Line 5 times Line 6	7	12	Numeric
110	Last Year Carryover	8	12	Numeric
120	Line 7 plus Line 8	9	12	Numeric

F. *Form 4562*

Record Length Page 1: 739 Characters
Record Length Page 2: 1,031 Characters

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
000	Record ID		25	"FRMb4562bbbPG01bnnnnnnnnn"
010	Activity		30	Alphanumeric
020	Class of Property 1	1a	20	Alphanumeric
030	Cost 1	1b	12	Numeric
040	Expense Deduction 1	1c	12	Numeric
050	Class of Property 2	1a	20	Alphanumeric
060	Cost 2	1b	12	Numeric
070	Expense Deduction 2	1c	12	Numeric
080	Listed Property	2	12	Numeric
090	Total Deduction	3	12	Numeric
*100	3-Year Cost	4Ac	12	Numeric
110	3-Year Recovery	4Ad	2	Numeric
120	3-Yr. Method Figuring	4Ae	5	Alphanumeric
130	3-Year Deduction	4Af	12	Numeric
*140	5-Year Cost	4Bc	12	Numeric
150	5-Year Recovery	4Bd	2	Numeric
160	5-Yr. Method Figuring	4Be	5	Alphanumeric
170	5-Year Deduction	4Bf	12	Numeric
*180	10-Year Cost	4Cc	12	Numeric
190	10-Year Recovery	4Cd	2	Numeric
200	10-Yr. Method Figuring	4Ce	5	Alphanumeric
210	10-Year Deduction	4Cf	12	Numeric
*220	15-Year Public Utility Cost	4Dc	12	Numeric
230	15-Year Public Util Recovery	4Dd	2	Numeric
240	15-Yr. Public Util Meth of Recovery	4De	5	Alphanumeric
250	15-Year Public Utility Deduction	4Df	12	Numeric
*260	Low Inc Date Serv 1	4Eb1	6	MMDDYY
270	Low Inc Cost	4Ec1	12	Numeric
280	Low Inc Recovery	4Ed1	2	Numeric
290	Low Inc Meth of Fig	4Ee1	5	Alphanumeric
300	Low Inc Deduction	4Ef1	12	Numeric
310	Low Inc Date Serv 2	4Eb2	6	MMDDYY
320	Low Inc Cost	4Ec2	12	Numeric
330	Low Inc Recovery	4Ed2	2	Numeric
340	Low Inc Meth of Fig	4Ee2	5	Alphanumeric
350	Low Inc Deduction	4Ef2	12	Numeric
*360	15-Year Real Date Serve	4Fb1	6	MMDDYY
370	15-Year Real Cost	4Fc1	12	Numeric
380	15-Year Real	4Fd1	2	Numeric

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
390	15-Year Real Meth	4Fe1	5	Alphanumeric
400	15-Year Real Deduct	4Ff1	12	Numeric
*410	18-Yr Real Date Serve	4Gb	6	MMDDYY
420	18-Yr Real Prop Cost	4Gc	12	Numeric
430	18-Yr Real Prop Recov	4Gd	2	Numeric
440	18-Yr Real prop Meth of Figure	4Ge	5	Alphanumeric
450	18Yr Real Prop Deduct	4Gf	12	Numeric
460	Listed Property	5	12	Numeric
470	ACRS Deduction	6	12	Numeric
480	Prop Subj to Sect 168	7	12	Numeric
490	Other Depreciation	8	12	Numeric
500	Total Depreciation	9	12	Numeric
*510	Descrip of Prop 1	II-A1	20	Alphanumeric
520	Date Acquired	II-B1	6	MMDDYY
530	Cost	II-C1	12	Numeric
540	Code Section	II-D1	5	Alphanumeric
550	Amortization Period or %	II-E1	2	Alphanumeric
560	Amortization	II-F1	12	Numeric
570	Descrip of Prop 2	II-A2	20	Alphanumeric
580	Date Acquired	II-B2	6	MMDDYY
590	Cost	II-C2	12	Numeric
600	Code Section	II-D2	5	Alphanumeric
610	Amortization Period or %	II-E2	2	Alphanumeric
620	Amortization	II-F2	12	Numeric
630	Descrip of Prop 3	II-A3	20	Alphanumeric
640	Date Acquired	II-B3	6	MMDDYY
650	Cost	II-C3	12	Numeric
660	Code Section	II-D3	5	Alphanumeric
670	Amortization Period or %	II-E3	2	Alphanumeric
680	Amortization	II-F3	12	Numeric
690	Descrip of Prop 4	II-A4	20	Alphanumeric
700	Date Acquired	II-B4	6	MMDDYY
710	Cost	II-C4	12	Numeric
720	Code Section	II-D4	5	Alphanumeric
730	Amortization Period or %	II-E4	2	Alphanumeric
740	Amortization	II-F4	12	Numeric
750	Total Amortization	II-TF	12	Numeric
760	Record ID		25	“FRMb4562bbbPG02bnnnnnnnnn”
*770	Description 1	III(i)(a)	13	Alphanumeric
780	Date Service	III(i)(b)	6	MMDDYY
790	Percent Use	III(i)(c)	2	Numeric
800	Cost or Basis	III(i)(d)	12	Numeric

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
810	Recovery Per.	III(i)(e)	10	Alphanumeric
820	Method Deprec.	III(i)(f)	5	Alphanumeric
830	Deduction	III(i)(g)	12	Numeric
840	179 Expense	III(i)(h)	12	Numeric
850	Description 2	III(ii)(a)	13	Alphanumeric
860	Date Service	III(ii)(b)	6	MMDDYY
870	Percent Use	III(ii)(c)	2	Numeric
880	Cost of Basis	III(ii)(d)	12	Numeric
890	Recovery Per.	III(ii)(e)	10	Alphanumeric
900	Method Deprec.	III(ii)(f)	5	Alphanumeric
910	Deduction	III(ii)(g)	12	Numeric
920	179 Expense	III(ii)(h)	12	Numeric
930	Description 3	III(iii)(a)	13	Alphanumeric
940	Date Service	III(iii)(b)	6	MMDDYY
950	Percent Use	III(iii)(c)	2	Numeric
960	Cost or Basis	III(iii)(d)	12	Numeric
970	Recovery Per.	III(iii)(e)	10	Alphanumeric
980	Method Deprec.	III(iii)(f)	5	Alphanumeric
990	Deduction	III(iii)(g)	12	Numeric
1000	179 Expense	III(iii)(h)	12	Numeric
1010	Description 4	III(iv)(a)	13	Alphanumeric
1020	Date Service	III(iv)(b)	6	MMDDYY
1030	Percent Use	III(iv)(c)	2	Numeric
1040	Cost or Basis	III(iv)(d)	12	Numeric
1050	Recovery Per.	III(iv)(e)	10	Alphanumeric
1060	Method Deprec.	III(iv)(f)	5	Alphanumeric
1070	Deduction	III(iv)(g)	12	Numeric
1080	179 Expense	III(iv)(h)	12	Numeric
1090	Description 5	III(v)(a)	13	Alphanumeric
1100	Date Service	III(v)(b)	6	MMDDYY
1110	Percent Use	III(v)(c)	2	Numeric
1120	Cost of Basis	III(v)(d)	12	Numeric
1130	Recovery Per.	III(v)(e)	10	Alphanumeric
1140	Method Deprec.	III(v)(f)	5	Alphanumeric
1150	Deduction	III(v)(g)	12	Numeric
1160	179 Expense	III(v)(h)	12	Numeric
1170	Description 6	III(vi)(a)	13	Alphanumeric
1180	Date Service	III(vi)(b)	6	MMDDYY
1190	Percent Use	III(vi)(c)	2	Numeric
1200	Cost or Basis	III(vi)(d)	12	Numeric
1210	Recovery Per.	III(vi)(e)	10	Alphanumeric
1220	Method Deprec.	III(vi)(f)	5	Alphanumeric
1230	Deduction	III(vi)(g)	12	Numeric

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
1240	179 Expense	III(vi)(h)	12	Numeric
1250	Description 7	III(vii)(a)	13	Alphanumeric
1260	Date Service	III(vii)(b)	6	MMDDYY
1270	Percent Use	III(vii)(c)	2	Numeric
1280	Cost of Basis	III(vii)(d)	12	Numeric
1290	Recovery Per.	III(vii)(e)	10	Alphanumeric
1300	Method Deprec.	III(vii)(f)	5	Alphanumeric
1310	Deduction	III(vii)(g)	12	Numeric
1320	179 Expense	III(vii)(h)	12	Numeric
1330	Description 8	III(viii)(a)	13	Alphanumeric
1340	Date Service	III(viii)(b)	6	MMDDYY
1350	Percent Use	III(viii)(c)	2	Numeric
1360	Cost of Basis	III(viii)(d)	12	Numeric
1370	Recovery Per.	III(viii)(e)	10	Alphanumeric
1380	Method Deprec.	III(viii)(f)	5	Alphanumeric
1390	Deduction	III(viii)(g)	12	Numeric
1400	179 Expense	III(viii)(h)	12	Numeric
1410	Description 9	III(ix)(a)	13	Alphanumeric
1420	Date Service	III(ix)(b)	6	MMDDYY
1430	Percent Use	III(ix)(c)	2	Numeric
1440	Cost or Basis	III(ix)(d)	12	Numeric
1450	Recovery Per.	III(ix)(e)	10	Alphanumeric
1460	Method Deprec.	III(ix)(f)	5	Alphanumeric
1470	Deduction	III(ix)(g)	12	Numeric
1480	179 Expense	III(ix)(h)	12	Numeric
1490	Total 179 Expense	III	12	Numeric
1500	Total Deduction	III	12	Numeric
1510	Evidence Yes	IIIB1	1	"X" or blank
1520	Evidence No	IIIB1	1	"X" or blank
1530	Evidence Written Yes	IIIB2	1	"X" or blank
1540	Evidence Written No	IIIB2	1	"X" or blank
1550	Maintain Statement Yes	IIIB3	1	NO ENTRY
1560	Maintain Statement No	IIIB3	1	NO ENTRY
1570	Maintain Statement Yes	IIIB4	1	NO ENTRY
1580	Maintain Statement No	IIIB4	1	NO ENTRY
1590	More Than 5 Yes	IIIb5	1	NO ENTRY
1600	More Than 5 No	IIIB5	1	NO ENTRY
1610	Total Miles 1	III6i	12	NO ENTRY
1620	Business Miles	III7i	12	NO ENTRY
1630	Commuting Miles	III8i	12	NO ENTRY
1640	Other Personal Mi.	III9i	12	NO ENTRY
1650	Total Miles 2	III6ii	12	NO ENTRY
1660	Business Miles	III7ii	12	NO ENTRY

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
1670	Commuting Miles	III8ii	12	NO ENTRY
1680	Other Personal Mi.	III9ii	12	NO ENTRY
1690	Total Miles 3	III6iii	12	NO ENTRY
1700	Business Miles	III7iii	12	NO ENTRY
1710	Commuting Miles	III8iii	12	NO ENTRY
1720	Other Personal Mi.	III9iii	12	NO ENTRY
1730	Total Miles 4	III6iv	12	NO ENTRY
1740	Business Miles	III7iv	12	NO ENTRY
1750	Commuting Miles	III8iv	12	NO ENTRY
1760	Other Personal Mi.	III9iv	12	NO ENTRY
1770	Total Miles 5	III6v	12	NO ENTRY
1780	Business Miles	III7v	12	NO ENTRY
1790	Commuting Miles	III8v	12	NO ENTRY
1800	Other Personal Mi.	III9v	12	NO ENTRY
1810	Total Miles 6	III6vi	12	NO ENTRY
1820	Business Miles	III7vi	12	NO ENTRY
1830	Commuting Miles	III8vi	12	NO ENTRY
1840	Other Personal Mi.	III9vi	12	NO ENTRY
1850	Vehicle Available Yes	III10i	1	NO ENTRY
1860	Vehicle Available No	III10i	1	NO ENTRY
1870	Another Vehicle Yes	III11i	1	NO ENTRY
1880	Another Vehicle No	III11i	1	NO ENTRY
1890	Disqual. Person Yes	III12i	1	NO ENTRY
1900	Disqual. Person No	III12i	1	NO ENTRY
1910	Vehicle Available Yes	III10ii	1	NO ENTRY
1920	Vehicle Available No	III10ii	1	NO ENTRY
1930	Another Vehicle Yes	III11ii	1	NO ENTRY
1940	Another Vehicle No	III11ii	1	NO ENTRY
1950	Disqual. Person Yes	IIi12ii	1	NO ENTRY
1960	Disqual. Person No	II12ii	1	NO ENTRY
1970	Vehicle Available Yes	III10iii	1	NO ENTRY
1980	Vehicle Available No	III10iii	1	NO ENTRY
1990	Another Vehicle Yes	III11iii	1	NO ENTRY
2000	Another Vehicle No	III11iii	1	NO ENTRY
2010	Disqual. Person Yes	III12iii	1	NO ENTRY
2020	Disqual. Person No	IIi12iii	1	NO ENTRY
2030	Vehicle Available Yes	III10iv	1	NO ENTRY
2040	Vehicle Available No	III10iv	1	NO ENTRY
2050	Another Vehicle Yes	III11iv	1	NO ENTRY
2060	Another Vehicle No	III11iv	1	NO ENTRY
2070	Disqual. Person Yes	III12iv	1	NO ENTRY
2080	Disqual. Person No	III12iv	1	NO ENTRY
2090	Vehicle Available Yes	III10v	1	NO ENTRY

Field No.	Identification	Form Ref.	Length	Field Description
2100	Vehicle Available No	III10v	1	NO ENTRY
2110	Another Vehicle Yes	III11v	1	NO ENTRY
2120	Another Vehicle No	III11v	1	NO ENTRY
2130	Disqual. Person Yes	III12v	1	NO ENTRY
2140	Disqual. Person No	III12v	1	NO ENTRY
2150	Vehicle Available Yes	III10vi	1	NO ENTRY
2160	Vehicle Available No	IIi10vi	1	NO ENTRY
2170	Another Vehicle Yes	III11vi	1	NO ENTRY
2180	Another Vehicle No	III11vi	1	NO ENTRY
2190	Disqual. Person Yes	III12vi	1	NO ENTRY
2200	Disqual. Person No	III12vi	1	NO ENTRY

G. *Form 8283*

Record Length Page 1: 885 Characters
Record Length Page 2: 487 Characters

Field No.	Identification	Form Ref.	Length	Field Description
000	Record ID		25	"FRMb8283bbbPg01bnnnnnnnnn" (n = Primary SSN From 1040)
*010	Donee Organization A	A1a	25	Alphanumeric
020	Donee Address A	A1a	25	Alphanumeric
030	Descrip. of Prop. A	A1b	25	Alphanumeric
050	Donee Organization B	B1a	25	Alphanumeric
060	Donee Address B	B1a	25	Alphanumeric
070	Descrip. of Prop. B	B1b	25	Alphanumeric
090	Donee Organization C	C1a	25	Alphanumeric
100	Donee Address C	C1a	25	Alphanumeric
110	Descrip. of Prop. C	C1b	25	Alphanumeric
130	Donee Organization D	D1a	25	Alphanumeric
140	Donee Address D	D1a	25	Alphanumeric
150	Descrip. of Prop. D	D1b	25	Alphanumeric
170	Donee Organization E	E1a	25	Alphanumeric
180	Donee Address E	E1a	25	Alphanumeric
190	Descrip. of Prop. E	E1b	25	Alphanumeric
*210	Contribution Date A	Ac	6	Numeric (MMDDYY)
220	Date Acquired A	Ad	4	Numeric (MMYY)
230	How Acquired A	Ae	10	Alphanumeric
240	Cost of Basis A	Af	12	Numeric
250	Fair Market Value A	Ag	12	Numeric
255	Method Used A	Ah	20	Alphanumeric
260	Contribution Date B	Bc	6	Numeric (MMDDYY)
270	Date Acquired B	Bd	4	Numeric (MMYY)
280	How Acquired B	Be	10	Alphanumeric
290	Cost of Basis B	Bf	12	Numeric

Field No.	*Identification*	*Form Ref.*	*Length*	*Field Description*
300	Fair Market Value B	Bg	12	Numeric
305	Method Used B	Bh	20	Alphanumeric
310	Contribution Date C	Cc	6	Numeric (MMDDYY)
320	Date Acquired C	Cd	4	Numeric (MMYY)
330	How Acquired C	Ce	10	Alphanumeric
340	Cost or Basis C	Cf	12	Numeric
350	Fair Market Value C	Cg	12	Numeric
355	Method Used C	Ch	20	Alphanumeric
360	Contribution Date D	Dc	6	Numeric (MMDDYY)
370	Date Acquired D	Dd	4	Numeric (MMYY)
380	How Acquired D	De	10	Alphanumeric
390	Cost or Basis D	Df	12	Numeric
400	Fair Market Value D	Dg	12	Numeric
405	Method Used D	Dh	20	Alphanumeric
410	Contribution Date E	Ec	6	Numeric (MMDDYY)
420	Date Acquired E	Ed	4	Numeric (MMYY)
430	How Acquired E	Ee	10	Alphanumeric
440	Cost or Basis E	Ef	12	Numeric
450	Fair Market Value E	Eg	12	Numeric
455	Method Used E	Eh	20	Alphanumeric
460	Amount This Year	2a	12	Numeric
470	Amount Prior Year	2a	12	Numeric
480	Name Donee	2b	35	Alphanumeric
490	Number & Street	2b	25	Alphanumeric
500	City, State, Zip	2b	25	Alphanumeric
510	Place Kept	2c	25	Alphanumeric
520	Name of Person	2d	25	Alphanumeric
530	Restriction YES	3a	1	"X" or Blank
540	Restriction NO	3a	1	"X" or Blank
550	Give Rights YES	3b	1	"X" or Blank
560	Give Rights NO	3b	1	"X" or Blank
570	Restriction on Use YES	3c	1	"X" or Blank
580	Restriction on Use NO	3c	1	"X" or Blank
590	Record ID		25	"FRMb8283bbbPG02bnnnnnnnnn"
600	Date Received	B1	6	Numeric (MMDDYY)
610	Donee Name	B1	35	Alphanumeric
620	Employer ID	B1	9	Numeric
630	Number & Street	B1	25	Alphanumeric
640	City, State, Zip	B1	25	Alphanumeric
*650	Descrip. of Prop. (1)	B2a	25	Alphanumeric
660	Date Acquired (1)	B2b	4	Numeric (MMYY)
670	How Acquired (1)	B2c	25	Alphanumeric
680	Cost or Basis (1)	B2d	12	Numeric

Field No.	Identification	Form Ref.	Length	Field Description
690	Fair Market Value (1)	B2e	12	Numeric
700	Descrip. of Prop. (2)	B2a	25	Alphanumeric
710	Date Acquired (2)	B2b	4	Numeric (MMYY)
720	How Acquired (2)	B2c	25	Alphanumeric
730	Cost or Basis (2)	B2d	12	Numeric
740	Fair Market Value (2)	B2e	12	Numeric
750	Descrip. of Prop. (3)	B2a	25	Alphanumeric
760	Date Acquired (3)	B2b	4	Numeric (MMYY)
770	How Acquired (3)	B2c	25	Alphanumeric
780	Cost or Basis (3)	B2d	12	Numeric
790	Fair Market Value (3)	B2e	12	Numeric
800	Descrip. of Prop. (4)	B2a	25	Alphanumeric
810	Date Acquired (4)	B2b	4	Numeric (MMYY)
820	How Acquired (4)	B2c	25	Alphanumeric
830	Cost or Basis (4)	B2d	12	Numeric
840	Fair Market Value (4)	B2e	12	Numeric
850	Condition Summary	B3	50	Alphanumeric

APPENDIX C

RETURN PREPARER PROGRAMMING CHECKS

All electronically filed returns must be logically consistent and mathematically perfect. The following data validation requirements must be incorporated into the programs used to prepare returns for electronic filing.

FORM 1040 GENERAL

All subtotal/total lines must equal the line entries leading to the subtotals/totals.

SOCIAL SECURITY NUMBER

The primary social security number must be entered in "Your Social Security Number" block. On a joint return, the secondary social security number must be entered in "Spouse's Social Security Number" block.

NAME (See Special Instructions for Name and Name Control)

ADDRESS

All addresses must include zip code and the standard state abbreviation (See Special Instructions).

FILING STATUS

Only one filing status can be used.

EXEMPTIONS

The number of exemptions in box 1 must equal the number of boxes checked on lines 6a and 6b. On a joint return, at least one box must be checked on line 6a and one box on line 6b.

The number of exemptions in box 2 must equal the number of names on line 6c.

The number of exemptions in box 3 must equal the number of names on line 6d. If names are present on line 6d, either the block for pre-1985 agreement must be checked, or Form 8332 must be present.

The number of exemptions in box 5 must equal the total number of exemptions in boxes 1 through 4.

FORM 1040, PAGE 1

LINE ENTRY SUPPORT

Interest Income—If the interest amount is over $400.00, a Schedule B must be present.

Dividends—If the dividend amount is over $400.00, a Schedule B must be present.

Taxable Dividends—The amount on this line must equal the result of dividends less dividend exclusion.

Business Income or Loss—NO ENTRY

Capital Gain or Loss—NO ENTRY

Supplemental Gains and Losses—NO ENTRY

Taxable Pensions and Annuities—If there is an amount on this line, there must be an entry for other pensions and annuities.

Rents, Royalties, Partnerships, Estates, Trusts, etc.—If there is an amount on this line, a Schedule E must be present.

Farm Income or Loss—NO ENTRY

Taxable Unemployment Compensation (insurance)—If there is an amount on this line, there must be an amount for total unemployment compensation received.

Taxable Social Security Benefits—If there is an amount on this line, there must be an amount for total social security benefits received.

Other Income—If there is an amount on this line, the nature and source of this income must be stated.

Total Income—The amount on this line must equal the sum of all income lines.

Moving Expense—NO ENTRY

Employee Business Expenses—If there is an amount on this line, a Form 2106 must be present

Alimony Paid—If an amount is present for alimony paid on line 29, the recipient's name and Social Security Number must be present.

Deduction for a Working Couple—If there is an amount on this line, a Schedule W must be present.

Total Adjustments—The amount on this line must equal the sum of all adjustment lines.

Adjusted Gross Income (page 1)—the amount on this line must equal the result of total income less total adjustments.

FORM 1040, PAGE 2

Adjusted Gross Income (page 2)—the amount on this line must equal the adjusted gross income on page 1.

Itemized Deduction Amount—If there is an amount on this line, a Schedule A must be present.

Charitable Contributions—If a Schedule A is present, there cannot be an entry on this line.

Adjusted Gross Income After Deduction—The amount on this line must equal the result of adjusted gross income less excess itemized deductions or charitable contributions. (There cannot be entries for both excess itemized deductions and charitable contributions.)

Exemption Amount—The amount on this line divided by $1040 must equal the number of exemptions in line 6e.

Taxable Income—The amount on this line must equal the result of adjusted gross income after deduction less exemption deduction.

Tax Method—There must be one entry. NO ENTRY for Schedule G.

Additional Taxes—NO ENTRY

Total Tax—The amount on this line must equal the sum of the amount on the tax method line and the amount of additional taxes.

Child Care Credit—If there is an amount on this line, a Form 2441 must be present.

Credit For The Elderly—If there is an amount on this line, a Schedule R must be present.

Foreign Tax Credit—NO ENTRY

General Business Credit—NO ENTRY

Total Credits—The amount on this line must equal the sum of all credit lines.

Tax After Credits—The amount on this line must equal the result of total tax less total credits.

Self-Employment Tax—NO ENTRY

Alternative Minimum Tax—NO ENTRY

Tax From Recapture of Investment Credit—NO ENTRY

SST on Tip Income Not Reported To Employer—NO ENTRY

Tax On An IRA—NO ENTRY

Total Additional Tax—NO ENTRY

Federal Income Tax Withheld—If there is an amount on this line, a W-2(s) must be present.

Credit For Federal Tax On Special Fuels—NO ENTRY

Regulated Investment Company Credit—NO ENTRY

Total Payments—The amount on this line must equal the sum of all payments.

Overpayment—If total payments is larger than total tax, there must be an amount on this line.

Refund—Enter refund amount if applicable.

Applied Estimated Tax—Enter estimated tax amount if applicable.

Amount Owed—NO ENTRY

SCHEDULE A

If there is an amount in itemized deductions, Form 1040, page 1, a Schedule A must be present.

Medical Deduction Before Limitation—This amount must equal the sum of all medical and dental expenses.

Five Percent AGI—This amount must equal 5 percent of the adjusted gross income, Form 1040, page 1.

Total Medical—This amount must equal the result of medical deduction less 5 percent AGI.

Other Taxes—If there is an amount on this line, list the type and amount of taxes paid.

Total Tax—This amount must equal the sum of all taxes paid.

Home Mortgage Interest Paid To Individuals—If there is an amount on this line, the name and address of the payee(s) must be listed.

Other Interest Paid—If there is an amount on this line, the payee(s) and amount(s) must be listed.

Total Interest—This amount must equal the sum of all interest paid.

Cash Contributions Totaling $3,000 Or More—If there is an amount on this line, list to whom and how much given.

Other Than Cash—If there is an amount on this line exceeding $500.00, a Form 8283 must be present.

Total Contributions—This amount must equal the sum of all contributions paid.

Total Casualty And Theft Loss(es)—NO ENTRY

Other Miscellaneous Deductions—This amount must qualify the sum of all miscellaneous deductions.

Total Itemized Deductions—The amount on this line must equal the sum of medical, taxes, interest, contributions, casualty or theft less, and miscellaneous deductions.

Standard Deduction Amount—There must be an amount on this line.

Excess Itemized Deductions—This amount must equal the result of total itemized deductions less standard deduction amount.

SCHEDULE B

If the interest income amount or the dividend amount is over $400.00, a Schedule B must be present.

Seller Financed Mortgage Name—If interest is from a seller financed mortgage, the name must be listed.

Interest Income—List the names of all payers and each individual interest amount received.

Taxable Interest—This amount must equal the sum of all interest received.

Dividend Income—List the names of all payers and each individual dividend amount received.

Dividend Subtotal—This amount must equal the sum of all dividends received.

Capital Gains Distribution—This amount must equal the amount of capital gains distributed on Schedule D.

Total Non-Taxable Dividends—This amount must equal the sum of capital gains distribution, non-taxable distribution, and qualified reinvestment.

Taxable Dividends—This amount must equal the result of dividend subtotal less total non-taxable dividends.

Foreign Account Question—This question must be answered.

Foreign Country—If the answer to the foreign account question is yes, the foreign country must be listed.

Foreign Trust Question—This question must be answered.

SCHEDULE W

If there is an amount on the deduction for a working couple line, a Schedule W must be present.

Wages, Salaries, Tips, Etc.—The sum of these two fields must equal the amount of wages, salaries, tips, etc. on Form 1040, page 1.

Net Profit Or Loss From Self-Employment—The sum of these two fields must equal the amount of net profit or loss from Schedule(s) C and F (Form 1040), Schedule K-1 (Form 1065), and any other taxable self-employment or earned income).

Total Earned Income—The sum of these two fields must equal the sum of wages, salaries, tips, etc. and net profit or loss from self-employment.

Adjustments From Form 1040—The sum of these two fields must equal the sum of employee business expense, IRA deduction, payments to a Keogh, and any repayment of sub-pay included in total adjustments, Form 1040, page 1.

Qualified Earned Income—The sum of these two fields must equal the result of adjustments from Form 1040 field, less total earned income field.

Smaller Qualified Earned Income—The smaller amount of qualified earned income must be entered here, but not more than $30,000.

Deduction—The amount of smaller qualified earned income multiplied by 10 percent. This amount must equal the amount of deduction for a married couple on Form 1040, page 1.

FORM 2441

Number of Qualifying Persons—There must be an entry on this line.

Payments To An Individual—If payments to an individual in a calendar year were $50.00 or more, the "were services performed in your home" question must be answered. If yes, the "have appropriate tax returns on wages for services in your home been filed" question must be answered. If yes, the employer identification number must be listed.

Qualified Expenses—Enter the amount of qualified expenses incurred and actually paid in this tax year, but not more than $2,400.00 ($4,800.00 if paid for the care of two or more qualifying persons).

Primary Taxpayer's Earned Income—Enter the amount of the primary taxpayer's earned income.

Spouse's Earned Income—Enter the amount of the spouse's earned income.

Earned Income—This amount must be the smaller of the primary taxpayer's earned income or the spouse's earned income.

Allowable Percentage—This percentage must be the amount from the table that applies to the adjusted gross income from Form 1040, page 1.

Credit For This Tax Year—This amount must equal the product of the smaller of qualified expenses or earned income multiplied by the allowable percentage.

Prior Year Tax Credit—This amount must equal the product of the prior year's qualified expenses paid in this year, multiplied by the allowable prior year percentage.

Allowable Credit—This amount

must equal the sum of credit for this tax year and prior year tax credit and must equal the amount of child care credit on Form 1040, page 2.

Attachment I

Internal Revenue Service

Assistant Commissioner
(Planning, Finance and
Research)

Department of the Treasury

Washington, DC 20224

January 1986

Participating Taxpayers
Electronic Filing Project

Dear Fellow Taxpayer:

Thank you for participating in our test project for electronic filing of individual tax returns with refunds. Electronic filing eliminates most of the manual processes required to handle paper returns. As a result, the Internal Revenue Service expects to reduce by two to three weeks the time required to issue refunds on electronically filed returns.

We cannot, however, guarantee a faster refund because, as with any return, errors made by you, your preparer or by us may delay your refund. Also, in the case of electronic filing, we cannot begin processing your refund until your preparer correctly transmits your return to us.

I want to stress that electronic filing will neither increase nor decrease the chances that we will audit your return. Receiving tax returns electronically allows us to accomplish quickly and economically the same processing that is performed on paper returns.

Your preparer will provide you with the required preparer-signed copy of your return and ask you to sign a declaration form which your preparer must file with us. This declaration form replaces the signature part of a paper return and also serves as your authorization to have your return electronically filed. Again, I want to thank you for participating in this test which offers benefits both to you and to the Internal Revenue Service.

Sincerely,

John L. Wedick, Jr.

Attachment II

Form **8453**

Department of the Treasury
Internal Revenue Service

U.S. Individual Income Tax Declaration for Electronic Filing

For the year January 1-December 31, 1985

OMB No. 1545-0936

1985

Your first name and initial (if joint return, also give spouse's name and initial)	Last name	Your social security number
		Spouse's social security number

Paperwork Reduction Act Notice.—We ask for this information to carry out the Internal Revenue laws of the United States. We need it to ensure that taxpayers are complying with these laws and to allow us to figure and collect the right amount of tax. You are required to give us this information.

Part I Tax Return Information

1	Total income (Form 1040, line 23; Form 1040A, line 10; Form 1040EZ, line 3)	1	
2	Adjustments to income (Form 1040, line 31; Form 1040A, line 13)	2	
3	Adjusted gross income (Form 1040, line 32; Form 1040A, line 14; Form 1040EZ, line 3)	3	
4	Taxable income (Form 1040, line 37; Form 1040A, line 19; Form 1040EZ, line 7)	4	
5	Total tax (Form 1040, line 56; Form 1040A, line 23; Form 1040EZ, line 9)	5	
6	Total payments (Form 1040, line 64; Form 1040A, line 25; Form 1040EZ, line 8)	6	
7	Refund (Form 1040, line 66; Form 1040A, line 26; Form 1040EZ, line 10)	7	

Part II Declaration of Taxpayer

Under penalties of perjury, I declare that the above described amounts agree with the amounts shown on the corresponding lines of my 1985 Federal income tax return shown or given to me by my tax return preparer/transmitter, and that I have also compared the information contained on my return with the information I provided to my preparer/transmitter. To the best of my knowledge and belief, my return is true, correct, and complete. I consent that my return, including this declaration and accompanying schedules and statements, be sent to the Internal Revenue Service by my tax return transmitter. I understand that portions of my return will be transmitted to the Internal Revenue Service electronically by a communications company.

Please Sign Here ▶

Your signature | Date ▶ Spouse's signature (if filing jointly, BOTH must sign)

Part III Declaration of Preparer/Transmitter (If the transmitter also prepared the tax return, check here ▶ ☐ .)

I declare that the above taxpayer's return is based on all information of which I have knowledge. A copy of all forms and information to be filed with the Internal Revenue Service has been or will be provided to the taxpayer.

Paid Preparer's/ Transmitter's Use Only	Your signature ▶	Date	Check if self-employed ☐	Your social security number
	Firm's name (or yours, if self-employed) and address ▶			E.I. No.
				ZIP code

Form **8453** (1985)

Attachment III

S.C. block control number	Document Locator Number	Year	Transaction code	MFT code
	Batch control number	Count Code	Date	
Surveyed by and date	Missing numbers at time of survey		*(If short block, show number of last return)*	

Record of Selected Returns

Returns marked "S" forwarded to Statistics	Date	All returns in block forwarded to Statistics	Date

00	25	50	75
01	26	51	76
02	27	52	77
03	28	53	78
04	29	54	79
05	30	55	80
06	31	56	81
07	32	57	82
08	33	58	83
09	34	59	84
10	35	60	85
11	36	61	86
12	37	62	87
13	38	63	88
14	39	64	89
15	40	65	90
16	41	66	91
17	42	67	92
18	43	68	93
19	44	69	94
20	45	70	95
21	46	71	96
22	47	72	97
23	48	73	98
24	49	74	99

Form **1332** (Rev. 8-81)
Use "Rev. 1-78" first

Block and Selection Record

☆U.S. GPO: 1985—529-878/30550

Department of the Treasury
Internal Revenue Service

Preparer/Transmitter Agreement for Electronic Filing

Name and Address of Preparer/Transmitter

____

Name and title of responsible company official

____

Address of location(s) where electronic returns are prepared (if more than one location, list all on back)

____

Address of location(s) where taxpayer declarations are stored while awaiting shipment to the Internal Revenue Service (if more than one location, list all on back)

____

Name and address of communications company, and name of responsible official of that company

____

____

I agree to the following conditions to file Individual Income Tax Returns electronically. I understand that my failure to meet any of the criteria will result in my not being certified to participate in the program.

1. I agree to submit a test transmission by January 30, 1986. I understand that until a successful test transmission has been acknowledged by the Service I am not certified to file.

2. Before transmitting an electronic return, I agree to secure a taxpayer declaration signed by each taxpayer for whom I file a return, and to store and submit the declarations in the manner and timeframes prescribed by the Service.

3. I agree to secure, store and submit Forms W-2 and all other forms, documents, etc., that are required for a complete return, and to do so in the manner and timeframes prescribed by the Service.

4. I agree that my return transmission will conform exactly to all prescribed specifications.

5. I understand that any return not acknowledged as received by the Service will be considered not filed.

6. I understand that inclusion in the Pilot does not guarantee permission to file electronically in future years.

7. I agree that all returns I file electronically will be original, current year, individual income tax, refund returns.

8. I agree that the advertising language I use will not infer any special relationship with the Internal Revenue Service, and that claims for faster refunds will not differ from language in Service publications.

9. I agree to not advertise outside the agreed upon metropolitan areas and I agree to not transmit returns for taxpayers who do not personally appear in my office (at least one taxpayer on a joint return) unless the taxpayers are residents of the metropolitan areas during the filing season.

10. I will keep copies of the returns at ________________________
(address)
in accordance with Service specifications.

11. I understand that if a taxpayer declaration is missing or in error, I will be responsible for supplying another together with accompanying paper documents. If a copy cannot be supplied, the return will be considered unsigned.

12. I agree to comply with all provisions of the Revenue Procedure for the Electronic Filing Test. In particular, I agree to give each taxpayer for whom I file an electronic return a copy of the letter provided by the Internal Revenue Service concerning electronic filing (Attachment I to the Revenue Procedure).

____

Signature of responsible company official

Part IV. Items of General Interest

New Form 8308, Report of a Sale or Exchange of Certain Partnership Interests

Announcement 86-2

New Form 8308, Report of a Sale or Exchange of Certain Partnership Interests, has been developed for partnerships to report a sale or exchange of all or a part of a partnership interest involving unrealized receivables or substantially appreciated inventory items under Internal Revenue Code Section 751(a). A separate Form 8308 must be filed for each Section 751(a) exchange. However, the form need not be filed until the partnership has received written notice of the exchange from the transferor, or until the partnership has knowledge that there has been a transfer of an interest, and at the time of the transfer, the partnership has Section 751(a) property. This new reporting is required by Internal Revenue Code 6050K and is effective for all Section 751(a) exchanges occurring after 1984.

A transferor in a Section 751(a) exchange must notify the partnership, in writing, within 30 days of the exchange. Note: The instructions to Form 8308 state that a transferor must notify the partnership within 14 days. However, recently issued regulations provide 30 days for the notification. The written notification must include:

(1) The names and addresses of both parties to the sale or exchange;

(2) The taxpayer identification number of the transferor and, if known, of the transferee, and

(3) The date of the exchange.

Partnerships must furnish a copy of Form 8308 to each transferor and transferee in a section 751(a) exchange by January 31 following the calendar year in which the exchange occurred (or, 30 days after the partnership has notice of the exchange, if this is later than the January 31 date). The copy of Form 8308 alerts transferors that they may be required to treat a portion of the gain realized from the sale or exchange as ordinary income.

Form 8308 must also be attached to the partnership Form 1065 for the taxable year in which the calendar year of the exchange ends. For example, if a section 751(a) exchange took place on February 1, 1985 and the partnership files its return on a fiscal year, Form 8308 must be attached to the Form 1065 for the partnership's fiscal year ending in 1986.

If a partnership is notified of a section 751(a) exchange after it has filed its Form 1065, the partnership must amend its return within 30 days after receiving the notification and attach a completed Form 8308 to the amended return.

Form 8308 may be ordered from the Forms Distribution Center whose addresses appear in the tax forms instruction booklets.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Edward L. Lambert	Rancho Mirage, CA	Certified Public Accountant	From November 6, 1985 Until January 8, 1990
Benjamin Ostfield	Minneapolis, MN	Attorney and Certified Public Accountant	Indefinite from November 20, 1985
Kenneth D. Short	Ellicott City, MD	Attorney	Indefinite from November 6, 1985

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

Finding List of Current Action on Previously Published Rulings[1]

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*Denotes entry since last publication

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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Nf- 1986-3

Internal Revenue bulletin

January 21, 1986
Bulletin No. 1986-3

Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

T.D. 8063, page 4.

LR-216-84, page 40.

LR-216-84, Withdrawal in Part, page 41.

Temporary and proposed regulations under sections 61 and 132 of the Code relate to the taxation of fringe benefits and exclusions from gross income for certain fringe benefits. Portions of certain other temporary and proposed regulations relating to fringe benefits are withdrawn.

Announcement 86-5, page 43.

Tables reflecting the increase in the recovery period to 19 years provide guidance to taxpayers depreciating real property placed in service after May 8, 1985.

ADMINISTRATIVE

Announcement 86-3, page 42.

Certain provisions of the temporary regulations under section 6050 of the Code relating to the reporting of mortgage interest will be modified.

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Announcement of Suspensions on page 46.

Department of the Treasury
Internal Revenue Service

T 22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 61.—Gross Income Defined

26 CFR 1.61-2T: Taxation of fringe benefits (Temporary).
(Also Section 132; 1.132-1T.)

T.D. 8063

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER A, PART 1—INCOME TAXES; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Temporary Regulations Relating to the Taxation of Fringe Benefits and Exclusions From Gross Income for Certain Fringe Benefits

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations concerning the taxation and valuation of fringe benefits and exclusions from gross income for certain fringe benefits. Changes to the applicable law were made by the Tax Reform Act of 1984 (98 Stat. 877). [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1]. The regulations affect any person providing or receiving fringe benefits. The regulations provide these persons with the guidance necessary to comply with the law.

DATES: Except to the extent otherwise provided, the regulations are effective as of January 1, 1985.

FOR FURTHER INFORMATION CONTACT: Annette J. Guarisco of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service, (202-566-3918, not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains temporary regulations relating to the taxation and valuation of fringe benefits and exclusions from gross income for certain fringe benefits. Section 61 of the Internal Revenue Code of 1954 (Code) was amended, and section 132 was added to the Code, by section 531 of the Tax Reform Act of 1984 (98 Stat. 877) [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 385]. Temporary and proposed regulations were published in the FEDERAL REGISTER for January 7, 1985 (50 FR 747, 836) [T.D. 8004, LR-216-84, 1985-1 C.B. 23, 655]. These regulations were later amended in part in the FEDERAL REGISTER for February 20, 1985 (50 FR 7038, 7073) [T.D. 8009, LR-216-84, 1985-1 C.B. 82, 657].

Subsequently, Public Law 99-44 (Repeal of Contemporaneous Recordkeeping Requirements) [1985-34 I.R.B. 22] affected the proposed and temporary regulations published in February. To implement the provisions of Public Law 99-44, the Service withdrew the affected proposed and temporary regulations published in February 1985 (50 FR 46,004, 46,086) [T.D. 8060, LR-145-84 and LR-216-84, 1985-49 I.R.B. 5, 20] and published new proposed and temporary regulations on November 6, 1985 (50 FR 46,006, 46,087) [T.D. 8061, LR-216-84, 1985-46 I.R.B. 7, 48].

Many comments were received from the public concerning the provisions in the proposed and temporary regulations previously published in 1985. In addition, on April 16, 17, and 18, 1985, the Internal Revenue Service (Service) held public hearings on the proposed regulations. In response to the comments and the statements made at the public hearings, the regulations have been amended. Due to the extent of the amendments, the Service is issuing the regulations in temporary rather than final form and is providing a cross-reference notice of proposed rulemaking (see * * * [page 40, this Bulletin]). This will provide the public with an opportunity to comment on the revised provisions of the regulations before they become final. The Service expects to hold public hearings on the regulations early next year.

The regulations contain general rules relating to valuation of fringe benefits and special rules that may be used to value certain fringe benefits, including the availability of employer-provided automobiles, the use of employer-provided vehicles for personal purposes or for commuting only, flights on employer-provided aircraft, and taxable flights on commercial airlines.

SUMMARY OF COMMENTS AND EXPLANATION OF PROVISIONS

In general

All of the regulations issued in January, February, and November of 1985 under sections 61 and 132 (the "proposed regulations") were removed and are replaced by these revised temporary regulations (the "new temporary regulations"). Many of the provisions contained in the proposed regulations were revised in response to comments received. The explanation of provisions describes the changes made to the proposed regulations and the reasons that certain comments are not reflected in the new temporary regulations. Many of the comments received are not included in this summary because they suggested changes that were contrary to the statutory amendments or the legislative intent evidenced in committee reports accompanying the legislation.

In addition to revised rules, the new temporary regulations contain rules relating to areas not addressed in the proposed regulations. For example, the regulations contain a special rule that may be used to value meals provided at an employer-operated eating facility for employees. This section contains an explanation of many of these new rules.

Valuation of employer-provided vehicles

Determination of fair market value

The proposed regulations provided that the Annual Lease Value is determined by reference to the fair market value of the employer-provided automobile made available to the employee. Many commentators suggested that the regulations provide additional guidance concerning determination of the fair market value of the automobile. In response, the new temporary regulations provide fair market value safe harbor rules. Many commentators requested that the proposed regulations allow the use of an automobile pricing guide to determine fair market value. Other commentators suggested that the cost of purchasing the automobile be treated as the fair market value of the automobile, either with or without an adjustment reflecting group or volume discount secured by the employer. In response, the new temporary regulations provide that for an automobile owned by an employer, the employer's cost of purchasing the automobile may be treated as the fair market value of the automobile, provided the purchase is made at arm's length. For an automobile that is leased or revalued by an employer, the retail value provided in any nationally recognized publication that regularly reports retail automobile values may be treated as the fair market value of the automobile, provided the value is reasonable with respect to the automobile.

Many commentators suggested that the regulations provide that the fair market value of an automobile be reduced by the value of special equipment contained in the automobile. In response, the new temporary regulations provide that the fair market value of an automobile does not include the fair market value of any specialized equipment that is added to or carried in the automobile if the presence of the equipment is necessitated by, and attributable solely to, the business needs of the employer. This rule does not apply to equipment susceptible to personal use.

Fleet-average valuation rule

The proposed regulations provided that the Annual Lease Value of each automobile must be determined based on its fair market value. Commentators suggested that this rule would be difficult to administer when an employer has a large fleet of automobiles. The new temporary regulations provided that employers may determine a fleet-average value of the automobiles in the fleet that may be used to determine an Annual Lease Value for all the automobiles in the fleet. This rule is available for an automobile the value of which does not exceed $16,500 and that is regularly used in the employer's business.

Provision of fuel in kind

The proposed regulations provided that the provision of fuel in kind may be valued at 5.5 cents-per-mile. Commentators indicated that employers with large fleets of automobiles need a special rule of value fuel where fuel is not provided from a company pump but the cost is reimbursed by or charged to the employer. In response to this comment, the new temporary regulations provide that an employer may value the provision of fuel for automobiles eligible for the fleet-average valuation rule by reference to average fuel costs and miles-per-gallon rates determined by sampling the greater of 10 percent of the automobiles in the fleet or 20 automobiles.

Redetermination of Annual Lease Value

The Annual Lease Values contained in the proposed regulations are based on a four-year, level-payment lease. Thus, the proposed regulations provided that the Annual Lease Value amount must generally be used for the period beginning on the day of the special rule is first used and ending on December 31 of the fourth full year following that date. A number of commentators stated that the Annual Lease Value amount should be redetermined more frequently than every four years. Because the Annual Lease Values are based on a four-year, level-payment lease, however, it would be inappropriate to redetermine the Annual Lease Value more frequently. An alternative would be to base the Annual Lease Values on a shorter lease period. This alternative would require an increase in the Annual Lease Values to reflect the shorter lease term.

Use of Daily Lease Value

The proposed regulations provided that a pro-rated Annual Lease Value may be used when the automobile is available to an employee for at least 30 days. If the automobile is available for less than 30 days, the availability of the automobile may be valued by applying the Daily Lease Value to the number of days the automobile is available to the employee. Alternatively, the availability may be valued by deeming the automobile available to the employee for at least 30 days. Some commentators suggested that the regulations provide that a pro-rated Annual Lease Value be used regardless of the number of days of availability. This suggestion was not adopted because the Daily Lease Value amount was based on an approximation of the lowest fair market rental values. The lessors' charge is higher for leases for shorter periods. The Service's market analysis indicated that a daily lease value is typically 700 percent of the daily pro-rated four-year lease rate in the proposed regulation. Consequently, the new temporary regulations retain the rules regarding Daily Lease Values.

Vehicle cents-per-mile special rule

The proposed regulations provided that the availability of an automobile cannot be determined by reference to a cents-per-mile rate multiplied by the number of miles driven. This rule was provided because automobiles are generally not leased on a cents-per-mile basis, but rather on the basis of the amount of time the automobile is available to the lessee.

Many commentators suggested that the regulations allow the use of a cents-per-mile rate, such as the standard mileage rate, to determine the value of the personal use of employer-provided automobiles. In response, the new temporary regulations provide that the standard mileage rate (21 cents-per-mile in 1985) may be used to determine the value of the personal use of an employer-provided vehicle (including an automobile) that is (1) reasonably expected to be regularly used in the employer's business or (2) actually driven (primarily by employees) at least 10,000 miles in a calendar year. This rule may be used for any vehicle the value of which in the calendar year in which it is first made available to an employee for personal use, or, if later, January 1, 1985, does not exceed the sum of the maximum recovery deductions allowable under section 280F(a)(2) for the first three taxable years in the recovery period for an automobile first placed in service during that calendar year. For 1985, that value is $12,800.

The reason for the regularly used in the employer's business requirement (and the alternative mileage rule) is that the vehicle cents-per-mile rule assumes that at least a fixed number of personal miles will be driven in a year (i.e., 15,000). Therefore, unlimited use of the special vehicle cents-per-mile rule would result in a significantly lower valuation for the use of an employer-provided vehicle in certain circumstances. For example, an employee who drives an employer-provided automobile valued at $12,000 for 5,000 miles (all personal) in a year, but who is not provided fuel by his employer, will include $775 in income. Under the Annual Lease Value table, which generally reflects the market value of the availability of an automobile for a year, the employee would include $3,600 in income. Because the valuation distortion is so great, use of the vehicle cents-per-mile rule is permitted only if the vehicle satisfies the regularly used in business requirement or the alternative mileage rule. The alternative mileage rule is intended to provide a mechanical alternative to the more general concept of "regularly used in business." The reason that the mileage must be primarily by employees, rather than, for example, by employees' families, is precisely because the mileage rule is intended as a mechanical alternative to the business use rule.

It should also be noted that in certain situations use of the cents-per-mile rule will result in a higher inclusion than will the automobile lease valuation rule.

Commuting special valuation rule

The proposed regulations provided that the value of the commuting use of an employer-provided vehicle may be valued at $3.00 per one-way or round-trip commute. The new temporary regulations clarify that the value of the commuting use is $1.50 per one-way commute. In the case where more than one employee commutes in an employer-provided vehicle, such as in the case of an employer-sponsored car pool, the value of the commuting use is $1.50 per one-way commute per employee.

The proposed regulations provided that the commuting special rule may not be used to value the commuting use of an employer-provided vehicle by an officer or a five-percent owner of the employer. Many commentators requested that the regulations define an officer, especially for government employees. The new temporary regulations provide that, for commuting that occurs after 1985, the special rule cannot be used to value the commuting use of an employer-provided vehicle by a "control employee". This term (which is defined differently for other purposes) includes certain officers, directors, and owners and is defined in the regulations for both government and non-government employers. The new temporary regulations provide that the officer component of the control employee definition may be applied to define an officer in 1985.

Valuation of flights on employer-provided aircraft

The proposed regulations provided a special rule that may be used to value certain flights on employer-provided airplanes. The value determined under the special rule depended on the purpose of the trip by the airplane and on whether the employee receiving the fringe benefit was a "key employee".

Many commentators stated that the values provided under the special rule were excessive and that the rule was complicated and too "fact-sensitive" to administer. In response to taxpayer and congressional concerns, the Treasury Department indicated in a letter to Senator Robert Dole (131 Cong. Rec. S6369 (daily ed. May 16, 1985)) that the regulations would be amended. The new temporary regulations adopt the provisions set out in that letter. Accordingly, under the new temporary regulations, the value of a flight under the special rule depends on the weight of the aircraft and whether the employee receiving the benefit is a control employee (defined separately for government and non-government employers).

Generally, the value of a flight determined under the new temporary regulations is lower than the value of a flight determined under the proposed regulations. Under certain circumstances, however, the value of a flight determined under the proposed regulations would be lower than the value of a flight determined under the new temporary regulations. Therefore, the new temporary regulations provide that the value of a flight taken in 1985 may be valued at the lower of the value determined under the proposed regulations.

The new temporary regulations retain the use of the Standard Industry Fare Level (SIFL) rates to determine the value of flights on employer-provided aircraft. The regulations provide the new SIFL rates that may be used to determine the value of flights taken during the last six months of 1985. As in the proposed regulations, the multiples used are intended to approximate coach and first-class fares on commercial airlines (e.g., 125 percent of the SIFL rates approximates coach fare and 200 percent of the SIFL rates approximates first-class fare).

The proposed regulations provided that the special valuation rule may only be used to value flights on employer-provided airplanes, rather than all aircraft (such as helicopters). The new temporary regulations provide that the special rule may be used to value flights on all employer-provided aircraft.

The proposed regulations also provided that the special valuation rule may not be used to value international flights. The new temporary regulations remove this restriction.

Many commentators noted that if an aircraft makes a certain flight for a business purpose, there is no additional cost incurred by the employer in allowing other persons to fly for personal purposes on such trip. They argued, therefore, that no income should be imputed to those persons who fly for personal purposes under such circumstances. Whether the employer incurs an additional cost, however, is not relevant to whether an employee receives a benefit. Certainly, those employees who are allowed to fly for personal purposes place some value on the flight provided.

It should be noted, however, that the proposed regulations provide that where at least 50 percent of the regular seating capacity of an aircraft is occupied by individuals whose flights are primarily for the employer's business (and whose flights are excludable as working condition fringes), the value of flights provided to employees (and certain others) will be considered to be zero. The inclusion of this special rule in the proposed regulations is intended to be a limited provision and is not to be interpreted as an exception to the general valuation principles which the Service will continue to apply outside the scope of this rule.

Valuation of taxable flights on commercial airlines

The proposed regulations provided a special valuation rule under which certain taxable flights on commercial airlines (i.e., stand-by or space-available flights) may be valued at 50 percent of the highest unrestricted coach fare of the flight taken. Many commentators protested that the 50 percent value was excessive in light of the restrictions imposed on the persons taking the flights, such as the lack of a guaranteed seat. The commentators submitted relevant data and suggested that 25 percent of the highest unrestricted coach fare is a more appropriate value of the benefit received. In response, the new temporary regulations provide that stand-by or space-available flights on commercial airlines may be valued at 25 percent of the highest unrestricted coach fare.

Valuation of meals provided at employer-operated eating facilities for employees

The new temporary regulations contain a special valuation rule that may be used to value meals provided at employer-operated eating facilities for employees. Pursuant to the special rule, the fair market value of all meals provided at the facility (the "total meal value") will be deemed to equal 150 percent of the facility's direct operating costs. This total meal value, less the actual gross receipts of the facility (the "total meal subsidy"), may then be allocated among employees in any manner reasonable under the circumstances. Alternatively, the employer may determine the fair market value of the taxable part of meals provided to a particular employee under a special "individual meal subsidy" rule.

Section 132 regulations

In general

The new temporary regulations provide rules relating to the exclusion from gross income for certain fringe benefits. Section 132 provides that certain fringe benefits, such as no-additional-cost services, qualified employee discounts, working condition fringes, and de minimis fringes may be excludable from the income of employees receiving the benefits. The regulations provide that, for purposes of the no-additional-cost service and qualified employee discount exclusions, the term "employee" means any individual who is currently employed by the employer, who was employed by the employer but separated from service by reason of retirement or disability, or who is a widow or widower of an employee. The regulations provide that a partner who performs services for a partnership is considered employed by the partnership.

The regulations provide that any individual listed above who could exclude from income no-additional-cost services or qualified employee discounts may exclude from income working condition fringes. In addition, solely for purposes of administrative convenience, the regulations provide that directors of the employer and independent contractors who perform services for the employer may generally exclude from income working condition fringes. This special rule is only available when, as set forth in Rev. Rul. 84-151, any amount included in income would also be deductible as an ordinary and necessary business expense. Therefore, this special rule does not apply, for example, to exclude from the income of an independent contractor or a director as a working condition fringe the value of the use of consumer goods under a product testing program. Directors and independent contractors are not treated as employees for any other purposes.

There is no limitation under section 132 as to who may exclude a de minimis fringe from income. Therefore, the regulations provide that any recipient may exclude a de minimis fringe from income.

Line of business limitation

No-additional-cost services and qualified employee discounts are available to employees of the line of business providing discounts or services. The regulations define a line of business based on the Enterprise Standard Industrial Classification Manual (ESIC Manual) prepared by the Statistical Policy Division of the U.S. Office of Management and Budget. An employer is generally considered to have more than one line of business if the employer offers for sale to customers property or services in more than one two-digit classification referred to in the ESIC Manual. [To be reprinted in 1986-4 I.R.B.] Examples of two-digit classifications are general retail merchandise stores; hotels and other lodging places; and auto repair, services, and garages.

The regulations also provide special rules under which an employer's separate lines of business will be aggregated. Under one rule, if it is uncommon in the employer's industry for any of the separate lines of business to be operated without the others, the separate lines of business are treated as one line of business. Under another rule, separate lines of business are aggregated if it is common for a substantial number of employees (other than those employees who work at the headquarters or main office of the employer) to perform substantial services for more than one line of business of the employer so that any determination of which employees perform substantial services for which lines of business would be difficult. Under another aggregation rule, separate retail lines of business located on the same premises are generally treated as the same line of business.

Working condition fringes

Employer-provided transportation for security reasons

The proposed regulations provide that the value of transportation provided by the employer for security reasons may be excludable as a working condition fringe to the extent a deduction under section 162 or 167 would be allowable to the employee had the employee paid for the transportation. Many commentators requested that the Service provide additional guidance concerning the appropriateness and amount of any working condition fringe exclusion for the value of security provided for bona fide business-oriented security reasons. In response, the new temporary regulations provide rules concerning the existence of bona fide business-oriented security reasons and the effect of an independent security study particular to the employer and its employees. The new temporary regulations also contain several examples of the application of the rules.

Product testing

The regulations provide that the value of the use of consumer goods may be exludable as a working condition fringe if certain conditions are met. This portion of the regulations is based on the legislative history of section 531 of the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 385]. The exclusion for product testing is limited so as to permit employers to have the benefit of product testing programs without allowing a major deviation from the general overall legislative intent of taxation of nonstatutory fringe benefits.

Qualified automobile demonstration use

The value of qualified automobile demonstration use is excludable from income as a working condition fringe. The regulations provide guidance concerning when the exclusion is available. In addition, the regulations provide a safe harbor rule that defines the sales area in which an automobile is located.

Parking

The value of parking may be excluded as a working condition fringe. The regulations provide rules relating to when the exclusion is available.

Employer-operated athletic facilities

Under a special rule, the value of the use of employer-operated athletic facilities may be excluded from income. The regulations provide rules concerning the definition of an employer-operated athletic facility and when the exclusion is available.

Nondiscrimination rules

No-additional-cost services, qualified employee discounts, and meals provided at employer-operated eating facilities for employees are only excludable from the income of an employee who is an officer, owner, or highly compensated employee (i.e., a member of the "prohibited group") if the benefits are offered on substantially the same terms to each member of a group of employees that is defined under a reasonable classification set up by the employer that does not discriminate in favor of the members of the prohibited group. Many commentators suggested that the definitions of owner and highly compensated employee contained in the proposed regulations were arbitrary and mechanical. The definitions were not amended in the new temporary regulations because, based on data submitted by commentators, the Service believes that the definitions comprise a reasonable and appropriate framework for identifying employees as members of the prohibited group. In addition, many commentators requested that the Service retain definitions that provide certainty.

The regulations provide that a classification is nondiscriminatory under section 132 if the classification would be nondiscriminatory under the rules provided in the qualified plan area (section 410(b)(1)(B) of the Code and the regulations thereunder).

Employer-operated eating facilities for employees

The value of meals provided at employer-operated eating facilities for employees are excludable from income as de minimis fringes if the revenues from the facility equal or exceed the direct operating costs of the facility and the nondiscrimination requirements of section 132 are satisfied. In response to comments, direct operating costs are narrowly defined as the cost of food and beverages and the cost of labor for personnel whose services relating to the facility are performed primarily on the premises of the eating facility. If meals provided at an eating facility are not excludable because, for example, the direct operating costs of the facility exceed revenues from the facility, the special meal valuation rule provided in the regulations under section 61 (described above) may be used to value the meals provided at the facility.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

No general notice of proposed rulemaking is required by 5 U.S.C. 553(b) for temporary regulations. Accordingly, the temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB. Control number [1545-0771].

DRAFTING INFORMATION

The principal author of these regulations is Annette J. Guarisco of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * *

Adoption of Amendment to the Regulations

Accordingly, 26 CFR Parts 1 and 602 are amended as follows:

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805 * * * 1.61-2T, 1.132-1T, 1.132-2T, 1.132-3T, 1.132-4T, 1.132-5T, 1.132-6T, 1.132-7T, and 1.132-8T also issued under 26 U.S.C. 132.

Par. 2. Section 1.61-2T is removed and a new §1.61-2T is added in its place, as follows:

§1.61-2T Taxation of fringe benefits (Temporary)

(a) *Fringe benefits*—(1) *In general.* Section 61(a)(1) provides that, except as otherwise provided in subtitle A, gross income includes compensation for services, including fees, commissions, fringe benefits, and similar items. Examples of fringe benefits include: an employer-provided automobile, a flight on an employer-provided aircraft, an employer-provided free or discounted commercial airline flight, an employer-provided vacation, an employer-provided discount on property or services, an employer-provided membership in a country club or other social club, and an employer-provided ticket to an entertainment or sporting event.

(2) *Fringe benefits excluded from income.* To the extent that a particular fringe benefit is specifically excluded from gross income pursuant to another section of subtitle A, that section shall govern the treatment of that fringe benefit. Thus, if the requirements of the governing section are satisfied, the fringe benefits may be excludable from gross income. Examples of excludable fringe benefits are qualified tuition reductions provided to an employee (section 117(d)); meals and lodging furnished to an employee for the convenience of the employer (section 119); and benefits provided under a dependent care assistance program (section 129). Similarly, the value of the use by an employee of an employer-provided vehicle or a flight provided to an employee on an employer-provided

aircraft may be excludable from income under section 105 (because, for example, the transportation is provided for medical reasons) if and to the extent that the requirements of that section are satisfied. Section 61 and the regulations thereunder shall apply, however, to the extent that they are not inconsistent with such other section. For example, many fringe benefits specifically addressed in other sections of subtitle A are excluded from gross income only to the extent that they do not exceed specific dollar or percentage limits, or only if certain other requirements are met. If the limits are exceeded or the requirements are not met, some or all of the fringe benefit may be includible in gross income. See paragraph (b)(3) of this section.

(3) *Compensation for services.* A fringe benefit provided in connection with the performance of services shall be considered to have been provided as compensation for services. Refraining from the performance of services (such as pursuant to a convenant not to compete) is deemed to be the performance of services for purposes of this section.

(4) *Recipient of a fringe benefit*—(i) *Definition.* A fringe benefit is included in the income of the "recipient" of the fringe benefit. The recipient of a fringe benefit is the person performing the services in connection with which the fringe benefit is provided. Thus, a person may be considered to be a recipient, even though that person did not actually receive the fringe benefit. For example, a fringe benefit provided to any person in connection with the performance of services by another person is considered to have been provided to the person who performs the services and not the person who receives the fringe benefit. In addition, if a fringe benefit is provided to a person, but taxable to a second person as the recipient, such benefit is referred to as provided to the second person and use by the first person is considered use by the second person. For example, provision of an automobile to an employee's spouse by the employer is taxable to the employee as the recipient. The automobile is referred to as available to the employee and use by the employee's spouse is considered use by the employee.

(ii) *Recipient may be other than an employee.* The recipient of a fringe benefit need not be an employee of the provider of the fringe benefit, but may be a partner, director, or an independent contractor. For convenience, the term "employee" includes a reference to any recipient of a fringe benefit, unless otherwise specifically provided in this section.

(5) *Provider of a fringe benefit.* The "provider" of a fringe benefit is that person for whom the services are performed, regardless of whether that person actually provides the fringe benefit to the recipient. The provider of a fringe benefit need not be the employer of the recipient of the fringe benefit, but may be, for example, a client or customer of an independent contractor. For convenience, the term "employer" includes a reference to any provider of a fringe benefit, unless otherwise specifically provided in this section.

(6) *Effective date.* This section is effective as of January 1, 1985. No inference may be drawn from the promulgation or terms of this section concerning the application of law in effect prior to January 1, 1985.

(b) *Valuation of fringe benefits*—(1) *In general.* An employee must include in gross income the amount by which the fair market value of the fringe benefit exceeds the sum of (i) the amount, if any, paid for the benefit, and (ii) the amount, if any, specifically excluded from gross income by some other section of subtitle A. Therefore, for example, if the employee pays fair market value for what is received, no amount is includible in the gross income of the employee.

(2) *Fair market value.* In general, fair market value is determined on the basis of all the facts and circumstances. Specifically, the fair market value of a fringe benefit is that amount a hypothetical person would have to pay a hypothetical third party to obtain (i.e., purchase or lease) the particular fringe benefit. Thus, for example, the effect of any special relationship that may exist between the employer and the employee must be disregarded. This also means that an employee's subjective perception of the value of a fringe benefit is not relevant to the determination of a fringe benefit's fair market value. In addition, the cost incurred by the employer is not determinative of the fair market value of the fringe benefit. For special rules relating to the valuation of certain fringe benefits, see paragraph (c) of this section.

(3) *Exclusion from income based on cost.* If a statutory exclusion phrased in terms of cost applies to the provision of a fringe benefit, section 61 does not require the inclusion in the recipient's gross income of the difference between the fair market value and the excludable cost of that fringe benefit. For example, section 129 provides an exclusion from an employee's gross income for amounts paid or incurred by an employer to provide dependent care assistance to employees. Even if the fair market value of the dependent care assistance exceeds the employer's cost, the excess is not subject to inclusion under section 61 and this section. If the statutory cost exclusion is a limited amount, however, then the fair market value of the fringe benefit attributable to any excess cost is subject to inclusion.

(4) *Fair market value of the availability of an employer-provided vehicle.* If the vehicle special valuation rules of paragraphs (d), (e), or (f) of this section are not used by a taxpayer entitled to use such rules, the value of the availability of an employer-provided vehicle is determined under the general valuation principles set forth in this section. In general, such valuation must be determined by reference to the cost to a hypothetical person of leasing from a hypothetical third party the same or comparable vehicle on the same or comparable terms in the geographic area in which the vehicle is available for use. Unless the employee can substantiate that the same or comparable vehicle could have been leased on a cents-per-mile basis, the value of the availability of the vehicle cannot be determined by reference to a cents-per-mile rate applied to the number of miles the vehicle is driven. An example of a comparable lease term is the amount of time that the vehicle is available to the employee for use, e.g., a one-year period.

(5) *Fair market value of a flight on an employer-provided aircraft.* If the non-commercial flight special valuation rule of paragraph (g) of this section is not used (or is not properly used) by a taxpayer entitled to use such rule, the value of a flight on an employer-provided aircraft is determined under the general valuation principles set

forth in this section. An example of how the general valuation principles would apply is that if an employee whose flight is primarily personal controls the use of an aircraft with respect to such flight, such flight is valued by reference to how much it would cost a hypothetical person to charter the same or comparable aircraft for the same or comparable flight. The cost to charter the aircraft must be allocated among all employees on board the aircraft based on all the facts and circumstances, including which employee or employees controlled the use of the aircraft. Notwithstanding the allocation required by the preceding sentence, no additional amount shall be included in the income of any employee whose flight is properly valued under the special valuation rule of paragraph (g) of this section.

(c) *Special valuation rules*—(1) *In general*. Paragraphs (d) through (j) of this section provide special valuation rules that may be used under certain circumstances for certain commonly provided fringe benefits. paragraph (d) provides a lease valuation rule relating to employer-provided automobiles. Paragraph (e) provides a cents-per-mile valuation rule relating to employer-provided vehicles. Paragraph (f) provides a commuting valuation rule relating to employer-provided vehicles. Paragraph (g) provides a flight valuation rule relating to flights on employer-provided aircraft. Paragraph (h) provides a flight valuation rule relating to flights on commercial airlines. Paragraph (i) is reserved. Paragraph (j) provides a meal valuation rule relating to employer-operated eating facilities for employees. For general rules relating to the valuation of fringe benefits not eligible for valuation under the special valuation rules, see paragraph (b) of this section.

(2) *Use of the special valuation rules*—(i) *In general*. The special valuation rules may be used for income, employment tax, and reporting purposes. Use of any of the special valuation rules is optional. An employer need not use the same vehicle special valuation rule for all vehicles provided to all employees. For example, an employer may use the automobile lease valuation rule for automobiles provided to some employees, and the commuting and vehicle cents-per-mile valuation rules for automobiles provided to other employees. Except as otherwise provided, however, if either the commercial flight valuation rule or the noncommercial flight valuation rule is used, such rule must be used by an employer to value all flights taken by employees in a calendar year. Effective January 1, 1986, if an employer uses one of the special rules to value the benefit provided to an employee, the employee may not use another special rule to value that benefit. The employee may, however, use general valuation rules based on facts and circumstances (see paragraph (b) of this section). Effective January 1, 1986, an employee may only use a special valuation rule if the employer uses the rule. If a special rule is used, it must be used for all purposes. If an employer properly uses a special rule and the employee uses the special rule, the employee must include in gross income the amount determined by the employer under the special rule less any amount reimbursed by the employee to the employer. The employer and the employee may use the special rules to determine the amount of the reimbursement due the employer by the employee. If an employer properly uses a special rule and properly determines the amount of an employee's working condition fringe under section 132 and §1.132-5T (under the general rule or under a special rule), and the employee uses the special valuation rule, the employee must include in gross income the amount determined by the employer less any amount reimbursed by the employee to the employer.

(ii) *Transitional rules*—(A) *Use of vehicle special valuation rules for 1985 and 1986*. For purposes of valuing the use or availability of a vehicle, the consistency rules provided in paragraphs (d)(6) and (e)(5) of this section (relating to the automobile lease valuation rule and the vehicle cents-per-mile valuation rule, respectively) apply for 1987 and thereafter. Therefore, for 1985 and 1986 an employer (and employee, subject to paragraph (c)(2)(i) of this section) may use any applicable special valuation rule (or no special valuation rule) to value the use or availability of a vehicle, subject to paragraph (c)(2)(ii)(B) of this section.

(B) *Consistency Rules for 1985 and 1986*. If an employer uses the automobile lease valuation rule of paragraph (d) of this section in 1985 or 1986 with respect to an automobile, such rule must be used for the entire calendar year with respect to the automobile except for any period during which the commuting valuation rule of paragraph (f) of this section is properly used. If an employer uses the vehicle cents-per-mile valuation rule of paragraph (e) of this section in 1985 or 1986 with respect to a vehicle, such rule must be used for the entire calendar year with respect to the vehicle except for any period during which the commuting valuation rule of paragraph (f) of this section is properly used. The rules of this paragraph (c)(2)(ii)(B) also apply to employees using the special valuation rules of paragraph (d) or (e) of this section.

(C) *Employee's use of special valuation rules for 1985*. An employee may use a special valuation rule (other than the rule in paragraph (e) of this section relating to the vehicle cents-per-mile valuation rule) during 1985 even if the employer does not use the same special valuation rule during 1985. An employee's use of a special valuation rule in 1986 and thereafter must be consistent with his employer's use of the rule as required under paragraph (c)(2)(i) of this section.

(D) *Examples*. The following examples illustrate the rules of paragraph (c)(2)(ii) of this section:

Example (1). Assume that an employer properly uses the automobile lease valuation rule in 1985. The employer may use the vehicle cents-per-mile valuation rule in 1986 if the requirements of the vehicle cents-per-mile valuation rule are satisfied.

Example (2). Assume that an employer does not use a special valuation rule to value the availability of an automobile in 1985. The employer may use any of the special valuation rules in 1986 if the requirements of the rule chosen are satisfied. The same applies for 1987.

Example (3). Assume that an employer properly uses the vehicle cents-per-mile valuation rule in 1985. The employer may continue to use the rule or use any of the other special valuation rules to value the benefit provided in 1986 if the requirements of the rule chosen are satisfied. Alternatively, the employer may use none of the special valuation rules in 1986 but use any of the rules in 1987 if the requirements of the rule chosen are satisfied.

Example (4). Assume that an employee properly uses the automobile lease valuation rule in 1985. In 1986 and thereafter the employee may use a special valuation rule only if the employee's employer uses the same special valuation rule. The employee may use general valuation principles to value the benefit provided in 1986 and thereafter.

(3) *Election to use the special valuation rules*—(i) *In general*. A particular special valuation rule is deemed to have been elected by the employer (and, if applicable, by the employee), if the employer (and, if applicable, the employee) determines the value of the fringe benefit provided by applying the special valuation rule and treats such value as the fair market value of the fringe benefit for income, employment tax, and reporting purposes. Neither the employer nor the employee is required to notify the Internal Revenue Service of the election.

(ii) *Notification to employee*. Effective January 1, 1987, an employer who elects to use a special valuation rule must notify the employee of the election by the later of January 31 of the calendar year for which the election is to apply or 30 days after the employer first provides the benefit to the employee. An employer who elects to use a special valuation rule with respect to 1986 must notify the employee of the election by the later of March 31, 1986, or 30 days after the employer first provides the benefit to the employee. An employer who elects to use a special valuation rule with respect to 1985 need not provide notification of this election to the employee.

(4) *Application of section 414 to employers*. For purposes of paragraphs (c) through (j) of this section, except as otherwise provided therein, the term "employer" includes all entities required to be treated as a single employer under section 414(b), (c), or (m).

(5) *Valuation formulas contained in the special valuation rules*. The valuation formulas contained in the special valuation rules are provided only for use in connection with such rules. Thus, when a special valuation rule is properly applied to a fringe benefit, the Commissioner will accept the value calculated pursuant to the rule as the fair market value of that fringe benefit. However, when a special valuation rule is not properly applied to a fringe benefit (see, for example, paragraph (g)(11) of this section), or when a special valuation rule is not used to value a fringe benefit by a taxpayer entitled to use the rule, the fair market value of that fringe benefit may not be determined by reference to any value calculated under any special valuation rule. Under the circumstances described in the preceding sentence, the fair market value of the fringe benefit must be determined pursuant to paragraph (b) of this section.

(6) *Modification of the special valuation rules*. The Commissioner may, if he deems it necessary, add, delete, or modify the special valuation rules, including the valuation formulas contained herein, on a prospective basis.

(7) *Special Accounting Period*. If the employer is using the special accounting rule provided in Announcement 85-113 (1985-13 I.R.B. 31, August 5, 1985) (relating to the reporting of and withholding on the value of noncash fringe benefits), benefits which are deemed provided in a subsequent calendar year pursuant to such rule are considered as provided in such subsequent calendar year for purposes of the special valuation rules. Thus, if a particular special valuation rule is in effect for a calendar year, it applies to benefits deemed provided during such calendar year under the special accounting rule.

(d) *Automobile lease valuation rule*—(1) *In general*—(i) *Annual Lease Value*. Under the special valuation rule of this paragraph (d), if an employer provides an employee with an automobile that is available to the employee for an entire calendar year, the value of the benefit provided is the Annual Lease Value (determined under paragraph (d)(2) of this section) of that automobile. Except as otherwise provided, for an automobile that is available to an employee for less than an entire calendar year, the value of the benefit provided is either a pro-rated Annual Lease Value or the Daily Lease Value (as defined in paragraph (d)(4) of this section), whichever is applicable. Absent any statutory exclusion relating to the employer-provided automobile (see, for example, section 132(a)(3) and §1.132-5T(b)), the amount of the Annual Lease Value (or a pro-rated Annual Lease Value or the Daily Lease Value, as applicable) is included in the gross income of the employee.

(ii) *Definition of automobile*. For purposes of this paragraph (d), the term "automobile" means any four-wheeled vehicle manufactured primarily for use on public streets, roads, and highways.

(2) *Calculation of Annual Lease Value*—(i) *In general*. The Annual Lease Value of a particular automobile is calculated as follows:

(A) Determine the fair market value of the automobile as of the first date on which the automobile is made available to any employee of the employer for personal use. For an automobile first made available to any employee for personal use prior to January 1, 1985, determine the fair market value as of January 1, 1985. For rules relating to determination of the fair market value of an automobile for purposes of this paragraph (d), see paragraph (d)(5) of this section.

(B) Select the dollar range in column 1 of the Annual Lease Value Table, set forth in paragraph (d)(2)(iii) of this section, corresponding to the fair market value of the automobile. Except as otherwise provided in paragraphs (d)(2)(iv) and (v) of this section, the Annual Lease Value for each year of availability of the automobile is the corresponding amount in column 2 of the Table.

(ii) *Use by employee only in 1985*. If the employee, but not the employer, is using the special rule of this paragraph (d), the employee may calculate the Annual Lease Value in the same manner as described in paragraph (d)(2)(i)(A) of this section, except that the fair market value of the automobile is determined as of the first date on which the automobile is made available to the employee for personal use or, for an automobile made available to the employee for personal use prior to January 1, 1985, by determining the fair market value as of January 1, 1985. If the employer is also using the special rule of this paragraph (d), however, then the employee to whom the automobile is made available must use the special rule if at all, by using the Annual Lease Value calculated by the employer. The rules of this paragraph (d)(2)(ii) apply only for 1985.

(iii) *Lease Value Table*.

Automobile fair market value (1)	*Annual Lease Value* (2)
$0 to 999	$600
1,000 to 1,999	850
2,000 to 2,999	1,100
3,000 to 3,999	1,350
4,000 to 4,999	1,600
5,000 to 5,999	1,850
6,000 to 6,999	2,100

Automobile fair market value (1)	*Annual Lease Value* (2)
7,000 to 7,999	2,350
8,000 to 8,999	2,600
9,000 to 9,999	2,850
10,000 to 10,999	3,100
11,000 to 11,999	3,350
12,000 to 12,999	3,600
13,000 to 13,999	3,850
14,000 to 14,999	4,100
15,000 to 15,999	4,350
16,000 to 16,999	4,600
17,000 to 17,999	4,850
18,000 to 18,999	5,100
19,000 to 19,999	5,359
20,000 to 20,999	5,600
21,000 to 21,999	5,850
22,000 to 22,999	6,100
23,000 to 23,999	6,350
24,000 to 24,999	6,600
25,000 to 25,999	6,850
26,000 to 27,999	7,250
28,000 to 29,999	7,750
30,000 to 31,999	8,250
32,000 to 33,999	8,750
34,000 to 35,999	9,250
36,000 to 37,999	9,750
38,000 to 39,999	10,250
40,000 to 41,999	10,750
42,000 to 43,999	11,250
44,000 to 45,999	11,750
46,000 to 47,999	12,250
48,000 to 49,999	12,750
50,000 to 51,999	13,250
52,000 to 53,999	13,750
54,000 to 55,999	14,250
56,000 to 57,999	14,750
58,000 to 59,999	15,250

For vehicles having a fair market value in excess of $59,999, the Annual Lease Value is equal to: (.25 × the fair market value of the automobile) + $500.

(iv) *Recalculation of Annual Lease Value*. The Annual Lease Values determined under the rules of this paragraph (d) are based on a four-year lease term. Therefore, except as otherwise provided in paragraph (d)(2)(v) of this section, the Annual Lease Value calculated by applying paragraph (d)(2)(i) or (ii) of this section shall remain in effect for the period that begins with the first date the special valuation rule of paragraph (d) of this section is applied by the employer to the automobile and ends on December 31 of the fourth full calendar year following that date. The Annual Lease Value for each subsequent four-year period is calculated by determining the fair market value of the automobile as of the January 1 following the period described in the previous sentence and selecting the amount in column 2 of the Annual Lease Value Table corresponding to the appropriate dollar range in column 1 of the Table. If, however, the employer is using the special accounting rule provided in Announcement 85-113 (1985-31 I.R.B. 31, August 5, 1985) (relating to the reporting of and withholding on the value of noncash fringe benefits), the employer may calculate the Annual Lease Value for each subsequent four-year period as of the beginning of the special accounting period that begins immediately prior to the January 1 described in the previous sentence. For example, assume that pursuant to Announcement 85-113, an employer uses the special accounting rule. Assume further that beginning on November 1, 1985, the special accounting period is November 1 to October 31 and that the employer elects to use the special valuation rule of this paragraph (d) as of January 1, 1985. The employer may recalculate the Annual Lease Value as of November 1, 1988, rather than as of January 1, 1989.

(v) *Transfer of the automobile to another employee*. Unless the primary purposes of the transfer is to reduce Federal taxes, if an employer transfers an automobile from one employee to another employee, the employer may recalculate the Annual Lease Value based on the fair market value of the automobile as of January 1 of the year of transfer. If, however, the employer is using the special accounting rule provided in Announcement 85-113 (1985-31 I.R.B. 31, August 5, 1985) (relating to the reporting of and withholding on the value of noncash fringe benefits), the employer may recalculate the Annual Lease Value based on the fair market value of the automobile as of the beginning of the special accounting period in which the transfer occurs. If the employer does not recalculate the Annual Lease Value, and the employee to whom the automobile is transferred uses the special valuation rule, the employee may not recalculate the Annual Lease Value.

(3) *Services included in, or excluded from, the Annual Lease Value Table*—(i) *Maintenance and insurance included*. The Annual Lease Values contained in the Annual Lease Value Table include the fair market value of maintenance of, and insurance for, the automobile. Neither an employer nor an employee may reduce the Annual Lease Value by the fair market value of any service included in the Annual Lease Value that is not provided by the employer, such as reducing the Annual Lease Value by the fair market value of a maintenance service contract or insurance. An employer or employee may take into account the services actually provided with respect to the automobile by valuing the availability of the automobile under the general valuation rules of paragraph (b) of this section.

(ii) *Fuel excluded*—(A) *In general*. The Annual Lease Values do not include the fair market value of fuel provided by the employer, regardless of whether fuel is provided in kind or its cost is reimbursed by or charged to the employer.

(B) *Valuation of fuel provided in kind*. The provision of fuel in kind may be valued at fair market value based on all the facts and circumstances or, in the alternative, it may be valued at 5.5 cents per mile for all miles driven by the employee. However, the provision of fuel in kind may not be valued at 5.5 cents per mile for miles driven outside the United States, Canada, and Mexico. For purposes of this section, the United States includes the United States and its territories.

(C) *Valuation of fuel where cost reimbursed by or charged to employer*. The fair market value of fuel, the cost of which is reimbursed by or charged to an employer, is generally the amount of the actual reimbursement or the amount charged, provided the purchase of the fuel is at arm's length. If an employer with a fleet of at least 20 automobiles that meet the requirements of paragraph (d)(5)(v)(C) of this section reimburses employees for the cost of fuel or allows employees to charge the employer for the cost of the fuel, however, the fair market value of fuel provided to those automobiles may be determined by reference to the employer's fleet-average cents-per-mile fuel cost. The fleet-average cents-per-mile fuel cost is equal to the fleet-average per-gallon fuel cost divided by the fleet-average miles-per-gallon rate. The averages described in the preceding sentence must be determined by averaging the per-gallon fuel costs and miles-per-gallon rates of a representative sample of the automobiles in the fleet equal to the greater of ten percent of the automobiles in the fleet or 20 automobiles for a representative period, such as a two month period.

(iii) *All other services excluded.* The fair market value of any service, not specifically identified in paragraph (d)(3)(i) of this section that is provided by the employer with respect to an automobile (such as the services of a chauffeur) must be added to the Annual Lease Value of the automobile in determining the fair market value of the benefit provided.

(4) *Availability of an automobile for less than an entire calendar year*—(i) *Pro-rated Annual Lease Value used for continuous availability of 30 or more days.* Except as otherwise provided in paragraph (d)(4)(iv) of this section, for periods of continuous availability of 30 or more days, but less than an entire calendar year, the value of the availability of the employer-provided automobile is the pro-rated Annual Lease Value. The pro-rated Annual Lease Value is calculated by multiplying the applicable Annual Lease Value by a fraction, the numerator of which is the number of days of availability and the denominator of which is 365.

(ii) *Daily Lease Value used for continuous availability of less than 30 days.* Except as otherwise provided in paragraph (d)(4)(iii) of this section, for periods of continuous availability of one or more but less than 30 days, the value of the availability of the employer-provided automobile is the Daily Lease Value. The Daily Lease Value is calculated by multiplying the applicable Annual Lease Value by a fraction, the numerator of which is four times the number of days of availability and the denominator of which is 365.

(iii) *Election to treat all periods as periods of at least 30 days.* A pro-rated Annual Lease Value may be applied with respect to a period of continuous availability of less than 30 days, by treating the automobile as if it had been available for 30 days, if to do so would result in a lower valuation than applying the Daily Lease Value to the shorter period of actual availability.

(iv) *Periods of unavailability*—(A) *General rule.* In general, a pro-rated Annual Lease Value (as provided in paragraph (d)(4)(i) of this section) is used to value the availability of an employer-provided automobile when the automobile is available to an employee for a period of continuous availability of at least 30 days but less than the entire calendar year. Neither an employer nor an employee may use a prorated Annual Lease Value when the reduction of Federal taxes is the primary reason the automobile is unavailable to an employee during the calendar year.

(B) *Unavailability for personal reasons of the employee.* If an automobile is unavailable to an employee because of personal reasons of the employee, such as while the employee is on vacation, a pro-rated Annual Lease Value may not be used. For example, assume an automobile is available to an employee during the first five months of the year and during the last five months of the year. Assume further that the period of unavailability occurs because the employee is on vacation. The Annual Lease Value, if it is applied, must be applied with respect to the entire 12 month period. The Annual Lease Value may not be pro-rated to take into account the two-month period of unavailability.

(5) *Fair market value*—(i) *In general.* For purposes of determining the Annual Lease Value of an automobile under the Annual Lease Value Table, the fair market value of an automobile is that amount a hypothetical person would have to pay a hypothetical third party to purchase the particular automobile provided. Thus, for example, any special relationship that may exist between the employee and the employer must be disregarded. Also, the employee's subjective perception of the value of the automobile is not relevant to the determination of the automobile's fair market value. In addition, except as provided in paragraph (d)(5)(ii) of this section, the cost incurred by the employer of either purchasing or leasing the automobile is not determinative of the fair market value of the automobile.

(ii) *Safe-harbor valuation rule.* For purposes of calculating the Annual Lease Value of an automobile under this paragraph (d), the safe-harbor value of the automobile may be used as the fair market value of the automobile. For an automobile owned by the employer, the safe-harbor value of the automobile is the employer's cost of purchasing the automobile, provided the purchase is made at arm's length. For an automobile leased by the employer, the safe-harbor value of the automobile is the value determined under paragraph (d)(5)(iii) of this section.

(iii) *Use of nationally recognized pricing guides.* The fair market value of an automobile that is (A) provided to an employee prior to January 1, 1985, (B) being revalued pursuant to paragraphs (d)(2)(iv) or (v) of this section, or (C) is a leased automobile being valued pursuant to paragraph (d)(5)(ii) of this section, may be determined by using the retail value of such automobile as reported in a nationally recognized publication that regularly reports new or used automobile retail values, whichever is applicable. The values contained in (and obtained from) the publication must be reasonable with respect to the automobile being valued.

(iv) *Fair market value of special equipment*—(A) *Certain equipment excluded.* The fair market value of an automobile does not include the fair market value of any telephone or any specialized equipment that is added to or carried in the automobile if the presence of such equipment is necessitated by, and attributable to, the business needs of the employer.

(B) *Use of specialized equipment outside of employer's business.* The value of specialized equipment must be included, however, if the employee to whom the automobile is available uses the specialized equipment in a trade or business of the employee other than the employee's trade or business of being an employee of the employer.

(C) *Equipment susceptible to personal use.* The exclusion rule provided in this paragraph (d)(5)(iv) does not apply to specialized equipment susceptible to personal use.

(v) *Fleet-average valuation rule*—(A) *In general.* An employer with a fleet of 20 or more automobiles may use a fleet-average value for purposes of calculating the Annual Lease Values of the automobiles in the fleet. The fleet-average value is the average of the fair market values of each automobile in the fleet. The fair market value of each automobile in the fleet shall be determined, pursuant to the rules of paragraphs (d)(5)(i) through (iv) of this section, as of the later of January 1, 1985, or the first date on which the automobile is made available to any employee of the employer for personal use.

(B) *Period for use of rule.* The fleet-average valuation rule of this paragraph (d)(5)(v) may be used by an employer as of January 1 of any calendar year following the calendar year in which the employer acquires a fleet of 20 or more automobiles. The Annual Lease Value calculated for the automobiles in the fleet, based on the fleet-average value, shall remain in effect for the period that begins with the first January 1 the fleet-average valuation rule of this paragraph (d)(5)(v) is applied by the employer to the automobiles in the fleet and ends on December 31 of the subsequent calendar year. The Annual Lease Value for each subsequent two year period is calculated by determining the fleet-average value of the automobiles in the fleet as of the first January 1 of such period. An employer may cease using the fleet-average valuation rule as of any January 1. The fleet-average valuation rule does not apply as of January 1 of the year in which the number of automobiles in the employer's fleet declines to fewer than 20. If, however, the employer is using the special accounting rule provided in Announcement 85-113 (1985-31 I.R.B. 31, August 5, 1985), the employer may apply the rules of this paragraph (d)(5)(v)(B) on the basis of the special accounting period rather than the calendar year. (This is accomplished by substituting (*1*) the beginning of the special accounting period that begins immediately prior to the January 1 described in this paragraph (d)(5)(v)(B) for January 1 wherever it appears in this paragraph (d)(5)(v)(B) and (*2*) the end of such accounting period for December 31.) The revaluation rules of paragraph (d)(2)(iv) and (v) of this section do not apply to automobiles valued under this paragraph (d)(5)(v).

(C) *Limitation on use of fleet-average rule.* The rule provided in this paragraph (d)(5)(v) may not be used for any automobile whose fair market value (determined pursuant to paragraphs (d)(5)(i) through (iv) of this section as of either the first date on which the automobile is made available to any employee of the employer for personal use or, if later, January 1, 1985) exceeds $16,500. In addition, the rule provided in this paragraph (d)(5)(v) may only be used for automobiles that the employer reasonably expected will regularly be used in the employer's trade or business. Infrequent use of the vehicle, such as for trips to the airport or between the employer's multiple business premises, does not constitute regular use of the vehicle in the employer's trade or business.

(D) *Additional automobiles added to the fleet.* If the rule provided in this paragraph (d)(5)(v) is used by an employer, it must be used for every automobile included in or added to the fleet that meets the requirements of paragraph (d)(5)(v)(C) of this section. The fleet-average value in effect at the time an automobile is added to the fleet is treated as the fair market value of the automobile for purposes of determining the Annual Lease Value of the automobile until the fleet-average value changes pursuant to paragraph (d)(5)(v)(B) of this section.

(E) *Use of the fleet-average rule by employees.* An employee can only use the fleet-average value if it is used by the employer. If an employer uses the fleet-average value, and the employee uses the special valuation rule of paragraph (d) of this section, the employee must use the fleet-average value.

(6) *Consistency rules*—(i) *Use of the automobile lease valuation rule by an employer.* Except as provided in paragraph (d)(5)(v)(B) of this section, an employer may adopt the automobile lease valuation rule of this paragraph (d) for an automobile only if the rule is adopted with respect to the later of the period that begins on January 1, 1987, or the first period in which the automobile is made available to an employee of the employer for personal use or, if the commuting valuation rule of paragraph (f) of this section is used when the automobile is first made available to an employee of the employer for personal use, the first period in which the commuting valuation rule is not used.

(ii) *An employer must use the automobile lease valuation rule for all subsequent periods.* Once the automobile lease valuation rule has been adopted for an automobile by an employer, the rule must be used by the employer for all subsequent periods in which the employer makes the automobile available to any employee, except that the employer may, for any period during which use of the automobile qualifies for the commuting valuation rule of paragraph (f) of this section, use the commuting valuation rule with respect to the automobile.

(iii) *Use of the automobile lease valuation rule by an employee.* Except as provided in paragraph (c)(2)(ii)(C) of this section, an employee may adopt the automobile lease valuation rule for an automobile only if the rule is adopted (A) by the employer and (B) with respect to the first period in which the automobile for which the employer (consistent with paragraph (d)(6)(i) of this section) adopted the rule is made available to that employee for personal use, or, if the commuting valuation rule of paragraph (f) of this section is used when the automobile is first made available to that employee for personal use, the first period in which the commuting valuation rule is not used.

(iv) *An employee must use the automobile lease valuation rule for all subsequent periods.* Once the automobile lease valuation rule has been adopted for an automobile by an employee, the rule must be used by the employee for all subseqquent periods in which the automobile for which the rule is used is available to the employee, except that the employee may, for any period during which use of the automobile qualifies for use of the commuting valuation rule of paragraph (f) of this section and for which the employer uses the rule, use the commuting valuation rule with respect to the automobile.

(v) *Replacement automobiles.* Notwithstanding anything in this paragraph (d)(6) to the contrary, if the automobile lease valuation rule is used by an employer, or by an employer and an employee, with respect to a particular automobile, and a replacement automobile is provided to the employee for the primary purpose of reducing Federal taxes, then the employer, or the employer and the employee, using the rule must continue to use the rule with respect to the replacement automobile.

(e) *Vehicle cents-per-mile valuation rule*—(1) *In general*—(i) *General rule.* Under the vehicle cents-per-mile valuation rule of this paragraph (e), if an employer provides an employee with the use of a vehicle that (A) the employer reasonably expects will be regularly used in the employer's trade or business throughouit the calendar year (or such shorter period as the vehicle may be owned or leased by the employer) or (B) satisfies the requirements of paragraph (e)(1)(ii) of this section, the value of the benefit provided in the calendar year is the standard mileage rate provided in the applicable Revenue Ruling or Revenue Procedure ("cents-per-mile rate") multiplied by the total number of miles the vehicle is driven by the employee for personal purposes. For 1985, the standard mileage rate is 21 cents per mile for the first 15,000 miles and 11 cents per mile for all miles over 15,000. See Rev. Proc. 85-49, 1985-40 I.R.B. 26. The standard mileage rate must be applied to personal miles independent of business miles. Thus, for example, if an employee drives 20,000 personal miles and 35,000 business miles in 1985, the value of the personal use of the vehicle is $3,700 (15,000 × $.21 + 5,000 × $.11). For purposes of this section, the use of a vehicle for personal purposes is any use of the vehicle other than use in the employee's trade or business of being an employee of the employer. Infrequent use of the vehicle, such as for trips to the airport or between the employer's multiple business premises, does not constitute regular use of the vehicle in the employer's trade or business.

(ii) *Mileage Rule.* A vehicle satisfies the requirements of this paragraph (e)(1)(ii) in a calendar year if (A) it is actually driven at least 10,000 miles in that year, and (B) use of the vehicle during the year is primarily by employees. For example, if a vehicle is used by only one employe during the year and that employee drives a vehicle at least 10,000 miles in a calendar year, such vehicle satisfies the requirements of this paragraph (e)(1)(ii) even if all miles driven by the employee are personal. The requirements of this paragraph (e)(1)(ii), however, will not be satisfied if during the year the vehicle is transferred among employees in such a way which enables an employee whose use was at a rate significantly less than 10,000 miles per year to meet the 10,000 mile threshold. Assume that an employee uses a vehicle for the first six months of the year and drives 2,000 miles, and that vehicle is then used by other employees who drive the vehicle 8,000 miles in the last six months of the year. Because the rate at which miles were driven in the first six months of the year would result in only 4,000 miles being driven in the year, and because the first employee did not use the vehicle during the last six months of the year, the requirements of this paragraph (e)(1)(ii) are not satisfied. The requirement of paragraph (e)(1)(ii)(B) of this section is deemed satisfied if employees use the vehicle on a consistent basis for commuting. If the employer does not own or lease the vehicle during a portion of the year, the 10,000 mile threshold is to be reduced proportionately to reflect the periods when the employer owned or leased the vehicle. For purposes of this paragraph (e)(1)(ii), use of the vehicle by an individual (other than the employee) whose use would be taxed to the employee is not considered use by the employee.

(iii) *Limitation on use of the vehicle cents-per-mile valuation rule.* The value of the use of an automobile (as defined in paragrapyh (d)(1)(ii) of this section) may not be determined under the vehicle cents-per-mile valuation rule of this paragraph (e) if the fair market value of the automobile (determined pursuant to paragraphs (d)(5)(i) through (iv) of this section as of the later of January 1, 1985, or the first date on which the automobile is made available to any employee of the employer for personal use) exceeds the sum of the maximum recovery deducations allowable under section 280F(a)(2) for the first three taxable years in the recorvery period for an automobile first placed in service during that calendar year. For 1985, that value is $12,800.

(2) *Definition of vehicle.* For purposes of this paragraph (e), the term "vehicle" means any motorized wheeled vehicle manufactured primarily for use on public streets, roads, and highways. The term "vehicle" includes an automobile as defined in paragraph (d)(1)(ii) of this section.

(3) *Services included in, or excluded from, the cents-per-mile rate*—(i) *Maintenance and insurance included.* The cents-per-mile rate includes the fair market value of maintenance of, and insurance for, the vehicle. An employer may not reduce the cents-per-mile rate by the fair market value of any service included in the cents-per-mile rate but not provided by the employer. An employer or employee may take into account the services provided with respect to the automobile by valuing the availability of the automobile under the general valution rules of paragraph (b) of this section.

(ii) *Fuel provided by the employer*—(A) *Miles driven in the United States, Canada, and Mexico.* With respect to miles driven in the United States, Canada, and Mexico, the cents-per-mile rate includes the fair market value of fuel provided by the employer. If fuel is not provided by the employer, the cents-per-mile rate may be reduced by no more than 5.5 cents or the amount specified in any applicable Revenue Ruling or Revenue Procedure. For purposes of this section, the United States includes the United States and its territories.

(B) *Miles driven outside the United States, Canada, and Mexico.* With respect to miles driven outside the United States, Canada, and Mexico, the fair market value of fuel provided by the employer is not reflected in the cents-per-mile rate. Accordingly, the cents-per-mile rate may be reduced but by no more than 5.5 cents or the amount specified in any applicable revenue ruling or revenue procedure. If the employer provides the fuel in kind, it must be valued based on all the facts and circumstances. If the employer reimburses the employee for the cost of fuel or allows the employee to charge the employer for the cost of fuel, the fair market value of the fuel is generally the amount of the actual reimbursement or the amount charged, provided the purchase of fuel is at arm's length.

(4) *Valuation of personal use only.* The vehicle cents-per-mile valuation rule of this paragraph (e) may only be used to value the miles driven for personal purposes. Thus, the employer must include an amount in an employee's income with respect to the use of a vehicle that is equal to the product of the number of personal miles driven by the employee and the appropriate cents-per-mile rate. The employer may not include in income a greater or lesser amount; for example, the employer may not include in income 100 percent (all business and personal miles) of the value of the use of the vehicle. The term "personal miles" means all miles driven by the employee except miles driven by the employee in the employee's trade or business of being an employee of the employer.

(5) *Consistency rules*—(i) *Use of the vehicle cents-per-mile valuation rule by an employer.* An employer must adopt the vehicle cents-per-mile valuation rule of this paragraph (e) for a vehicle

by the later of the period that begins on January 1, 1987, or the first period in which the vehicle is used by an employee of the employer for personal use or, if the commuting valuation rule of paragraph (f) of this section is used when the vehicle is first used by an employee of the employer for personal use, the first period in which the commuting valuation rule is not used.

(ii) *An employer must use the vehicle cents-per-mile valuation rule for all subsequent periods.* Once the vehicle cents-per-mile valuation rule has been adopted for a vehicle by an employer, the rule must be used by the employer for all subsequent periods in which the vehicle qualifies for use of the rule, except that (A) the employer may, for any period during which use of the vehicle qualifies for the commuting valuation rule of paragraph (f) of this section, use the commuting valuation rule with respect to the vehicle, and (B) if the employer elects to use the automobile lease valuation rule of paragraph (d) of this section for a period in which the vehicle does not qualify for use of the vehicle cents-per-mile valuation rule, then the employer must comply with the requirements of paragraph (d)(6) of this section. If the vehicle fails to qualify for use of the vehicle cents-per-mile valuation rule during a subsequent period, the employer may adopt for such subsequent period and thereafter any other special valuation rule for which the vehicle then qualifies. For purposes of paragraph (d)(6) of this section, the first day on which an automobile with respect to which the vehicle cents-per-mile rule had been used fails to qualify for use of the vehicle cents-per-mile valuation rule may be deemed to be the first day on which the automobile is available to an employee of the employer for personal use.

(iii) *Use of the vehicle cents-per-mile valuation rule by an employee.* An employee may adopt the vehicle cents-per-mile valuation rule for a vehicle only if the rule is adopted (A) by the employer and (B) with respect to the first period in which the vehicle for which the employer (consistent with paragraph (e)(5)(i) of this section) adopted the rule is available to that employee for personal use or, if the commuting valuation rule of paragraph (f) of this section is used by both the employer and the employee when the vehicle is first used by an employee for personal use, the first period in which the commuting valuation rule is not used.

(iv) *An employee must use the vehicle cents-per-mile valuation rule for all subsequent periods.* Once the vehicle cents-per-mile valuation rule has been adopted for a vehicle by an employee, the rule must be used by the employee for all subsequent periods of personal use of the vehicle by the employee for which the rule is used by the employer, except that the employee may, for any period during which use of the vehicle qualifies for use of the commuting valuation rule of paragraph (f) of this section and for which such rule is used by the employer, use the commuting valuation rule with respect to the vehicle.

(v) *Replacement vehicles.* Notwithstanding anything in this paragraph (e)(5) to the contrary, if the vehicle cents-per-mile valuation rule is used by an employer, or by an employer and an employee, with respect to a particular vehicle, and a replacement vehicle is provided to the employee for the primary purpose of reducing Federal taxes, then the employer, or the employer and the employee, using the rule must continue to use the rule with respect to the replacement vehicle if the replacement vehicle qualifies for use of the rule.

(f) *Commuting valuation rule*—(1) *In general.* Under the commuting valuation rule of this paragraph (f), the value of the commuting use of an employer-provided vehicle may be determined pursuant to paragraph (f)(3) of this section if the following criteria are met by the employer and employees with respect to the vehicle:

(i) The vehicle is owned or leased by the employer and is provided to one or more employees for use in connection with the employer's trade or business and is used in the employer's trade or business;

(ii) For bona fide noncompensatory business reasons, the employer requires the employee to commute to and/or from work in the vehicle;

(iii) The employer has established a written policy under which the employee may not use the vehicle for personal purposes, other than for commuting or de minimis personal use (such as a stop for a personal errand on the way between a business delivery and the employee's home);

(iv) Except for de minimis personal use, the employee does not use the vehicle for any personal purpose other than commuting; and

(v) The employee required to use the vehicle for commuting is not a control employee of the employer (as defined in paragraphs (f)(5) and (6) of this section).

If the vehicle is a chauffeur-driven vehicle, the commuting valuation rule of this paragraph (f) may not be used to value the commuting use of any passenger who commutes in the vehicle. The rule may be used, however, to value the commuting use of the chauffeur. Personal use of a vehicle is all use of the vehicle by the employee that is not use in the employee's trade or business of being an employee of the employer.

(2) *Special rules.* Notwithstanding anything in paragraph (f)(1) of this section to the contrary, the following special rules apply—

(i) *Written policy not required in 1985.* The policy described in paragraph (f)(1)(iii) of this section prohibiting personal use need not be written with respect to the commuting use which occurs prior to January 1, 1986;

(ii) *Commuting use during 1985.* For commuting use that occurs after December 31, 1984, but before January 1, 1986, the restrictions of paragraph (f)(1)(v) of this section shall be applied by substituting "an employee who is an officer or a five-percent owner of the employer" in lieu of "a control employee". For purposes of determining who is a five-percent owner, any individual who owns (or is considered as owning) five or more percent of the fair market value of an entity (the "owned entity") is considered a five-percent owner of all entities that would be aggregated with the owned entity under the rules of section 414(b), (c), or (m). An employee who is an officer of an employer shall be treated as an officer of all entities treated as a single employer pursuant to section 414(b), (c), or (m). The definitions provided in paragraphs (f)(5)(i) and (f)(6) of this section may be used to define an officer; and

(iii) *Control employee exception.* If the vehicle in which the employee is required to commute is not an automobile as defined in paragraph (d)(1)(ii) of this section, the restrictions of paragraph (f)(1)(v) of this section do not apply.

(3) *Commuting value*—(i) *$1.50 per one-way commute*. If the requirements of this paragraph (f)are satisfied, the value of the commuting use of an employer-provided vehicle is $1.50 per one-way commute (e.g., from home to work or from work to home).

(ii) *Value per employee*. If there is more than one employee who commutes in the vehicle, such as in the case of an employer-sponsored car pool, the amount includible in the income of each employee is $1.50 per one-way commute. Thus, the amount includible for each round-trip commute is $3.00 per employee.

(4) *Definition of vehicle*. For purposes of this paragraph (f), the term "vehicle" means any motorized wheeled vehicle manufactured primarily for use on public streets, roads, and highways. The term "vehicle" includes an automobile as defined in paragraph (d)(1)(ii) of this section.

(5) *Control employee defined—Non-government employer*. For purposes of this paragraph (f), a control employee of a non-government employer is any employee—

(i) Who is a Board- or shareholder-appointed, confirmed, or elected officer of the employer,

(ii) who is a director of the employer, or

(iii) Who owns a one-percent or greater equity, capital, or profits interest in the employer.

For purposes of determining who is a one-percent owner under paragraph (f)(5)(iii) of this section, any individual who owns (or is considered as owning under section 318(a) or principles similar to section 318(a) for entities other than corporations) one percent or more of the fair market value of an entity (the "owned entity") is considered a one-percent owner of all entities which would be aggregated with the owned entity under the rules of section 414(b), (c), or (m). An employee who is an officer of an employer shall be treated as an officer of all entities treated as a single employer pursuant to section 414(b), (c) or (m).

(6) *Control employee defined— Government employer*. For purposes of this paragraph (f), a control employee of a government employer is any—

(i) Elected official,

(ii) Federal employee who is appointed by the President and confirmed by the Senate. In the case of commissioned officers of the United States Armed Forces, an officer is any individual with the rank of brigadier general or above or the rank of rear admiral (lower half) or above; or

(iii) State or local executive officer comparable to the individuals described in paragraph (f)(6)(i) and (ii) of this section.

For purposes of this paragraph (f), the term "government" includes any Federal, state, or local governmental unit, and any agency or instrumentality thereof.

(g) *Non-commercial flight valuation rule*—(1) *In general*. Under the non-commercial flight valuation rule of this paragraph (g), if an employee is provided with a flight on an employer-provided aircraft, the value of the flight is calculated using the aircraft valuation formula provided in paragraph (g)(5) of this section. Except as otherwise provided, for purposes of this paragraph (g), a flight provided to a person whose flight would be taxable to an employee as the recipient is referred to as provided to the employee, and a flight taken by such person is considered a flight taken by the employee.

(2) *Eligible flights and eligible aircraft*. The valuation rule of this paragraph (g) may be used to value flights on all employer-provided aircraft, including helicopters. The valuation rule of this paragraph (g) may be used to value international as well as domestic flights. The valuation rule of this paragraph (g) may not be used to value a flight on any commercial aircraft on which air transportation is sold to the public on a per-seat basis. For a special valuation rule relating to certain flights on commercial aircraft, see paragraph (h) of this section.

(3) *Definition of a flight*—(i) *General rule*. Except as otherwise provided in paragraph (g)(3)(iii) of this section (relating to intermediate stops), for purposes of this paragraph (g), an individual's flight is the distance (in statute miles) between the place at which the individual boards the aircraft and the place at which the individual deplanes.

(ii) *Valuation of each flight*. Under the valuation rule of this paragraph (g), value is determined separately for each flight. Thus, a round-trip is comprised of at least two flights. For example, an employee who takes a personal trip on an employer-provided aircraft from New York, New York to Denver, Colorado, Denver to Los Angeles, California, and Los Angeles to New York has taken three flights and must apply the aircraft valuation formula separately to each flight. The value of a flight must be determined on a passenger-by-passenger basis. For example, if an individual accompanies an employee and the flight taken by the individual would be taxed to the employee, the employee would be taxed on the special rule value of the flight by the employee and by the individual.

(iii) *Intermediate stop*. If the primary purpose of a landing is necessitated by weather conditions, by an emergency, for purposes of refueling or obtaining other services relating to the aircraft, or for purposes of the employer's business unrelated to the employee whose flight is being valued ("an intermediate stop"), the distance between the place at which the trip originates and the place at which the intermediate stop occurs is not considered a flight. For example, assume that an employee's trip originates in St. Louis, Missouri, on route to Seattle, Washington, but, because of weather conditions, the aircraft lands in Denver, Colorado, and the employee stays in Denver overnight. Assume further that the next day the aircraft flies to Seattle where the employee deplanes. The employee's flight is the distance between the airport in St. Louis and the airport in Seattle. Assume that a trip originates in New York, New York, with five passengers and makes an intermediate stop in Chicago, Illinois, before going on to Los Angeles, California. If one of the five passengers deplanes in Chicago, the distance of that passenger's flight would be the distance between the airport in New York and the airport in Chicago. The intermediate stop is disregarded when measuring the flights taken by each of the other passengers. Their flights would be the distance between the airport in New York and the airport in Los Angeles.

(4) *Personal and non-personal flights*—(i) *In general*. The valuation rule of this paragraph (g) applies to personal flights on employer-provided aircraft. A personal flight is one the value

of which is not excludable under another section of subtitle A, such as under section 132(d) (relating to a working condition fringe). However, solely for purposes of paragraphs (g)(4)(ii) and (g)(4)(iii) of this section, references to personal flights do not include flights a portion of which would not be excludable by reason of section 274(c).

(ii) *Trip primarily for employer's business.* If an employee combines, in one trip, personal and business flights on an employer-provided aircraft and the employee's trip is primarily for the employer's business (see §1.162-2 (b)(2)), the employee must inlude in income the excess of the value of all the flights that comprise the trip over the value of the flights that would have been taken had there been no personal flights but only business flights. For example, assume that an employee flies on an employer-provided aircraft from Chicago, Illinois to Miami, Florida, for the employer's business and that from Miami the employee flies on the employer-provided aircraft to Orlando, Florida, for personal purposes and then flies back to Chicago. Assume further that the primary purpose of the trip is for the employer's business. The amount includible in income is the excess of the value of the three flights (Chicago to Miami, Miami to Orlando, and Orlando to Chicago), over the value of the flights that would have been taken had there been no personal flights but only business flights (Chicago to Miami and Miami to Chicago).

(iii) *Primarily personal trip.* If an employee combines, in one trip, personal and business flights on an employer-provided aircraft and the employee's trip is primarily personal (see §1.162-2(b)(2)), the amount includible in the employee's income is the value of the personal flights that would have been taken had there been no business flights but only personal flights. For example, assume that an employee flies on an employer-provided aircraft from San Francisco, California, to Los Angeles, California, for the employer's business and that from Los Angeles the employee flies on an employer-provided aircraft to Palm Springs, California, primarily for personal reasons and then flies back to San Francisco. Assume further that the primary purpose of the trip is personal. The amount includible in the employee's income is the value of personal flights that would have been taken had there been no business flights but only personal flights (San Francisco to Palm Springs and Palm Springs to San Francisco).

(iv) *Application of Section 274(c).* The value of employer-provided travel outside the United States away from home may not be excluded from the employee's gross income as a working condition fringe, by either the employer or the employee, to the extent not deductible by reason of section 274(c). The valuation rule of this paragraph (g) applies to that portion of the value of any flight not excludable by reason of section 274(c). Such value must be included in income in addition to the amounts determined under paragraphs (g)(4)(ii) and (g)(4)(iii) of this section.

(v) *Flight by individuals who are not personal guests.* If an individual who is not an employee of the employer providing the aircraft is on a flight, and the individual is not the personal guest of any employee, the flight by the individual is not taxable to any employee of the employer providing the aircraft. The rule in the preceding sentence applies where the individual is provided the flight by the employer for noncompensatory business reasons of the employer. For example, assume that G, an employee of company Y, accompanies A, an employee of company X, on company X's aircraft for the purpose of inspecting land under consideration for purchase by company X from company Y. The flight by G is not taxable to A.

(5) *Aircraft valuation formula.* Under the valuation rule of this paragraph (g), the value of a flight is determined by multiplying the base aircraft valuation formula for the period during which the flight was taken by the appropriate aircraft multiple (as provided in paragraph (g)(7) of this section) and then adding the applicable terminal charge. The base aircraft valuation formula (also known as the Standard Industry Fare Level formula or SIFL) in effect on June 30, 1985, is as follows: ($.1402 per mile for the first 500 miles, $.1069 per mile for miles between 501 and 1500, and $.1028 per mile for miles over 1500). The terminal charge in effect on June 30, 1985, is $25.62. The SIFL cents-per-mile rates in the formula and the terminal charge are calculated by the Department of Transportation and are revised semi-annually.

(6) *SIFL formula in effect for a particular flight.* For purposes of this paragraph (g), in determining the value of a particular flight during the first six months of a calendar year, the SIFL formula (and terminal charge) in effect on December 31 of the preceding year applies, and in determining the value of a particular flight during the last six months of a calendar year, the SIFL formula (and terminal charge) in effect on June 30 of that year applies. The following is the SIFL formula in effect on December 31, 1984: ($.1480 per mile for the first 500 miles, $.1128 per mile for miles between 501 and 1500, and $.1085 per mile for miles over 1500. The terminal charge in effect on December 31, 1984, is $27.05.

(7) *Aircraft multiples*—(i) *In general.* The aircraft multiples are based on the maximum certified takeoff weight of the aircraft. For purposes of applying the aircraft valuation formula described in paragraph (g)(5) of this section, the aircraft multiples are as follows:

6,000 lbs. or less	62.5 percent	15.6 percent
6,001—10,000-lbs.	125 percent	23.4 percent
10,001—25,000-lbs.	300 percent	31.3 percent
25,001 lbs. or more	400 percent	31.3 percent

(ii) *Flights treated as provided to a control employee.* Except as provided in paragraph (g)(10) of this section, any flight provided to an individual whose flight would be taxable to a control employee (as defined in paragraph (g)(8) and (9) of this section) as the recipient shall be valued as if such flight had been provided to that control employee. For example, assume that the chief executive officer of an employer, his spouse, and his two children fly on an employer-provided aircraft for personal purposes. Assume further that the maximum certified takeoff weight of the aircraft is 12,000 lbs. The amount includible in the employee's income is 4 × (300 percent × base aircraft valuation formula) plus the applicable terminal charge.

(8) *Control employee defined—Nongovernment employer.* For purposes of this paragraph (g), a control

employee of a non-government employer is any employee—

(i) Who is a Board- or shareholder-appointed, confirmed, or elected officer of the employer, limited to the lesser of (A) one-percent of all employees (increased to the next highest integer, if not an integer) or (B) ten employees;

(ii) Whose compensation equals or exceeds the compensation of the top one percent most highly-paid employees of the employer (increased to the next highest integer, if not an integer) limited to a maximum of 25 employees;

(iii) Who owns a ten-percent or greater equity, capital or profits interest in the employer; or

(iv) Who is a director of the employer.

For purposes of this paragraph (g), any employee who is a family member (within the meaning of section 267(c)(4)) of a control employee is also a control employee. Pursuant to this paragraph (g)(8), an employee may be a control employee under more than one of the requirements listed in paragraphs (g)(8)(i) through (iv) of this section. For example, an employee may be both an officer under paragraph (g)(8)(i) of this section and a highly-paid employee under paragraph (g)(8)(ii) of this section. In this case, for purposes of the officer limitation rule of paragraph (g)(8)(i) of this section and the highly-paid employee limitation rule of paragraph (g)(8)(ii) of this section, the employee would be counted as reducing both such limitation rules. In no event shall an employee whose compensation is less than $50,000 be a control employee under paragraph (g)(8)(ii) of this section. For purposes of determining who is a ten-percent owner under paragraph (g)(8)(iii) of this section, any individual who owns (or is considered as owning under section 318(a) or principles similar to section 318(a) for entities other than corporations) ten percent or more of the fair market value of an entity (the "owned entity") is considered a ten-percent owner of all entities which would be aggregated with the owned entity under the rules of section 414(b), (c), or (m). For purposes of determining who is an officer under paragraph (g)(8)(i) of this section, notwithstanding anything in this section to the contrary, if the employer would be aggregated with other employers under the rules of section 414(b), (c), or (m), the officer definition and the limitations are applied to each separate employer rather than to the aggregated employer. If applicable, the officer limitation rule of paragraph (g)(8)(i) of this section is applied to employees in descending order of their compensation. Thus, if an employer has 11 board-appointed officers, the employee with the least compensation of those officers would not be an officer under paragraph (g)(8)(i) of this section. For purposes of this paragraph (g), the term "compensation" means the amount reported on a Form W-2 as income for the prior calendar year. Compensation includes all amounts received from all entities treated as a single employer under section 414(b), (c), or (m).

(9) *Control employee defined— Government.* For purposes of this paragraph (g), a control employee of a government employer is any—

(i) Elected official;

(ii) Federal employee who is appointed by the President and confirmed by the Senate. In the case of commissioned officers of the United States Armed Forces, an officer is any individual with the rank of brigadier general or above or the the rank of rear admiral (lower half) or above; or

(iii) State or local executive officer comparable to the individuals in paragraph (g)(9)(i) and (ii) of this section.

For purposes of this paragraph (g), the term "government" includes any Federal, state, or local government unit, and any agency or instrumentality thereof.

(10) *Seating capacity rule*—(i) *In general.* Where 50 percent or more of the regular passenger seating capacity of an aircraft (as used by the employer) is occupied by individuals whose flights are primarily for the employer's business (and whose flights are excludable from income under section 132(d)), the value of a flight on that aircraft by any employee who is not flying primarily for the employer's business (or who is flying primarily for the employer's business but the value of whose flight is not excludable under section 132(d) by reason of section 274(c)) is deemed to be zero. See §1.132-5T which limits the exclusion under section 132(d) to situations where the employee receives the flight in connection with the performance of services for the employer providing the aircraft. For purposes of this paragraph (g)(10), the term "employee" includes only employees and partners of the employer providing the aircraft and does not include independent contractors and directors of the employer. For purposes of this paragraph (g)(10), the second sentence of paragraph (g)(1) of this section will not apply. Instead, a flight taken by an individual who is either treated as an employee pursuant to section 132(f)(1) or whose flight is treated as a flight taken by an employee pursuant to section 132(f)(2) is considered a flight taken by an employee. If (A) a flight is considered taken by an individual other than an employee (as defined in this paragraph (g)(10)), (B) the value of that individual's flight is not excludable under section 132(d), and (C) the seating capacity rule of this paragraph (g)(10) otherwise applies, then the value of the flight provided to such an individual is the value of a flight provided to a non-control employee (even if the individual who would be taxed on the value of such individual's flight is a control employee).

(ii) *Application of 50-percent test to multiple flights.* The seating capacity rule of this paragraph (g)(10) must be met both at the time the individual whose flight is being valued boards the aircraft and at the time the individual deplanes. For example, assume that employee A boards an employer-provided aircraft for personal purposes in New York, New York, and that at that time 80 percent of the regular passenger seating capacity of the aircraft is occupied by individuals whose flights are primarily for the employer's business (and whose flights are excludable from income under section 132(d)) ("the business passengers"). If the aircraft flies directly to Hartford, Connecticut where all of the passengers, including A, deplane, the requirements of the seating capacity role of this paragraph (g)(10) have been satisfied. If instead, some of the passengers, including A, remain on the aircraft in Hartford and th eaircraft continues on to Boston, Massachusetts, where they all deplane, the requirements of the seating capacity rule of this paragraph (g)(10) will not be satisfied unless at least 50 percent of the seats comprising the aircraft's regular passenger seating capacity were occupied by the business passnegers at the time A deplanes in Boston.

(iii) *Regular passenger seating capacity.* The regular passenger seating capacity of an aircraft is the maximum number of seats that have at any time been on the aircraft (while owned or leased by the employer). Except to the extent excluded pursuant to paragraph (g)(10)(v) of this section, regular seating capacity includes all seats which may be occupied by members of the flight crew. It is irrelevant that on a particular flight, less than the maximum number of seats are available for use, because, for example, some of the seats are removed. When determining the maximum number of seats, those seats that cannot at any time be legally used during takeoff and are not any time used during takeoff are not counted.

(iv) *Examples.* The rules of paragraph (g)(10)(iii) of this section are illustrated by the following examples:

Example (1). Employer A and employer B order the same aircraft, except that A orders it with 10 seats and B orders it with eight seats. A always uses its aircraft as a 10-seat aircraft; B always uses its aircraft as an eight-seat aircraft. The regular passenger seating capacity of A's aircraft is 10 and of B's aircraft is eight.

Example (2). Assume the same facts as in example (1), except that whenever A's chief excutive officer and spouse use the aircraft eight seats are removed. Even if substantially all of the use of the aircraft is by the chief executive officer and spouse the regular passenger seating capacity of the aircraft is 10.

Example (3). Assume the same facts as in example (1), except that whenever more than eight people want to fly in B's aircraft, two extra seats are added. Even if substantially all of the use of the aircraft occurs with eight seats, the regular passenger seating capacity of the aircraft is 10.

(v) *Seats occupied by flight crew.* When determining the regular passenger seating capacity of an aircraft, any seat occupied by a member of the flight crew (whether or not such individual is an employee of the employer providing the aircraft) shall not be counted, unless the purpose of the flight by such individual is not primarily to serve as a member of the flight crew. If the seat occupied by a member of the flight crew is not counted as a passenger seat pursuant to the previous sentence, such member of the flight crew is disregarded in applying the 50 percent test described in the first sentence of paragraph (g)(10)(i) of this section. For example, assume that, prior to application of this paragraph (g)(10)(v), the regular passenger seating capacity of an aircraft is two seats. Assume further that an employee pilots the aircraft and that the employee's flight is not primarily for the employer's business. If the employee's spouse occupies the other seat for personal purposes, the seating capacity rule is not met and the value of both flights must be included in the employee's income. If, however, the employee's flight were primarily for the employer's business (unrelated to serving as a member of the flight crew), then the seating capacity rule is met and the value of the flight for the employee's spouse is deemed to be zero. If the employee's flight were primarily to serve as a member of the flight crew, then the seating capacity rule is not met and the value of a flight by any passenger for primarily personal reasons is not deemed to be zero.

(11) *Erroneous use of the non-commercial flight valuation rule*—(i) *In general.* If the non-commercial flight valuation rule of this paragraph (g) is used by an employer or a control employee, as the case may be, on a return as originally filed, on the grounds that either the control employee is not in fact a control employee, or that the aircraft is within a specific weight classification, and either position is subsequently determined to be erroneous, the valuation rule of this paragraph (g) (including paragraph (g)(13) of this section) is not available to value the flight taken by that control employee by the person or persons taking the erroneous position. With respect to the weight classifications, the previous sentence does not apply if the position taken is that the weight of the aircraft is greater than it is subsequently determined to be. If, with respect to a flight by a control employee, the seating capacity rule of paragraph (g)(10) of this section is used by an employer or the control employee, as the case may be, on a return as originally filed, and it is subsequently determined that the requirements of paragraph (g)(10) of this section were not met, the valuation rule of this paragraph (g) (including paragraph (g)(13) of this section) is not available to value the flight taken by that control employee by the person or persons taking the erroneous position.

(ii) *Value of flight excluded as a working condition fringe.* If either an employer or an employee, on a return as originally filed, excludes from the employee's income or wages the value of a flight on the grounds that the flight was excludable as a working condition fringe under section 132, and that position is subsequently determined to be erroneous, the valuation rule of this paragraph (g) (including paragraph (g)(13) of this section) is not available to value the flight taken by that employee by the person or persons taking the erroneous position.

(12) *Consistency rules*—(i) *Use by the employer.* Except as otherwise provided in paragraphs (g)(11) and (g)(13)(iv) of this section, if the non-commercial flight valuation rule of this paragraph (g) is used by an employer to value flights provided in a calendar year, the rule must be used to value all flights provided in the calendar year.

(ii) *Use by the employee.* Except as otherwise provided in paragraphs (g)(11) and (g)(13)(iv) of this section, if the non-commercial flight valuation rule of this paragraph (g) is used by an employee to value a flight taken in a calendar year, the rule must be used to value all flights taken in the calendar year.

(13) *Transitional valuation rule*—(i) *In general.* If the value of a flight determined under this paragraph (g)(13) is lower than the value of the flight otherwise determined under paragraph (g) of this section, the value of the flight is the lower amount. The transitional valuation rule of this paragraph (g)(13) is available only for flights provided after December 31, 1984, and before January 1, 1986.

(ii) *Transitional valuation rule aircraft multiples.* The appropriate aircraft multiples under the transitional valuation rule are as follows:

(A) 125 percent of the base aircraft valuation formula, plus the applicable terminal charge, for any flight by any employee who is not a key employee (as defined in paragraph (g)(13)(iii) of this section.

(B) 125 percent of the base aircraft valuation formula, plus the applicable terminal charge, for a flight by a key employee if there is a primary business purpose for the trip by the aircraft. For purposes of this paragraph (g)(13)(ii)(B), entertaining an employee or other individual is not a business purpose.

(C) 600 percent of the base aircraft valuation formula, plus the applicable terminal charge, for a flight by a key employee if there is no primary business purpose for the trip by the aircraft. Where there is no business purpose for the trip by the aircraft, the alternative valuation rule may not be used to value a flight by a key employee. For purposes of this section, compensating an employee is not a business purpose.

(iii) *Key employee defined.* A "key employee" is any employee who is a five-percent owner or an officer of the employer, or who, with respect to a paticular trip by the aircraft, controls the use of the aircraft. For purposes of determining who is a five-percent owner, any individual who owns (or is considered as owning) five or more percent of the fair market value of an entity (the "owned entity") is considered a five-percent owner of all entities that would be aggregated with the owned entity under the rules of section 414(b), (c), or (m).

(iv) *Erroneous use of transitional valuation rule.* If the transitional valuation rule is used by an employer or a key employee, as the case may be, on a return as originally filed, on the grounds that—

(A) The key employee is not in fact a key employees.

(B) An aircraft trip had a primary business purpose, or

(C) An araft trip had some business purpose,

and such position is subsequently determined to be erroneous, neither the transitional valuation rule nor the noncommercial flight valuation rule of this paragraph (g) is available to value such flight taken by that key employee by the person or persons taking the erroneous position.

(h) *Commercial flight valuation rule*—(1) *In general.* Under the commercial flight valuation rule of this paragraph (h), the value of a space-available flight (as defined in paragraph (h)(2) of this section) on a commercial aircraft is 25 percent of the actual carrier's highest unrestricted coach fare in effect for the particular flight taken.

(2) *Space-available flight.* The commercial flight valuation rule of this paragraph (h) is available to value a space-available flight. The term "space-available flight" on a commercial aircraft (i) for which the airline (the actual carrier) incurs no substantial additional cost (including forgone revenue) determined without regard to any amount paid for the flight and (ii) which is subject to the same types of restrictions customarily associated with flying on an employee "standby" or "space-available" basis. A flight may be a space-available flight even if the airline that is the actual carrier is not the employer of the employee.

(3) *Commercial aircraft.* If the actual carrier does not offer, in the ordinary course of its business, air transportation to customers on a per-seat basis, the commercial flight valuation rule of this paragraph (h) is not available. Thus, if, in the ordinary course of its line of business, the employer only offers air transportation to customers on a charter basis, the commercial flight valuation rule of this paragraph (h) may not be used to value a space-available flight on the employer's aircraft. Similarly, if, in the ordinary course of its line of business, an employer only offers air transportation to customers for the transport of cargo, the commercial flight valuation rule of this paragraph (h) may not be used to value a space-available flight on the employer's aircraft.

(4) *Timing of inclusion.* The date that the flight is taken is the relevant date for purposes of applying section 61(a)(1) and this section to a space-available flight on a commercial aircraft. The date of purchase or issuance of a pass or ticket is not relevant. Thus, this section applies to a flight taken on or after January 1, 1985, regardless of the date on which the pass or ticket for the flight was purchased or issued.

(5) *Consistency rules*—(i) *Use by employer.* If the commercial flight valuation rule of this paragraph (h) is used by an employer to value flights provided in a calendar year, the rule must be used to value all flights provided in the calendar year.

(ii) *Use by employee.* If the commercial flight valuation rule of this paragraph (h) is used by an employee to value a flight taken in a calendar year, the rule must be used to value all flights taken by such employee in the calendar year.

(i) [Reserved]

(j) *Valuation of meals provided at an employer-operated eating facility for employees*—(1) *In general.* The valuation rule of this paragraph (j) may be used to value a meal provided at an employer-operated eating facility for employees (as defined in §1.132-7T). For rules relating to an exclusion for the value of meals provided at an employer-operated eating facility for employees, see §1.32-7T.

(2) *Valuation formula*—(i) *In general.* The value of all meals provided at an employer-operated eating facility for employees during a calendar year is 150 percent of the direct operating costs of the eating facility ("total meal value"). For purposes of this paragraph (j), the definition of direct operating costs provided in §1.32-7T applies. The taxable value of meals provided at an eating facility may be determined in two ways. The "individual meal subsidy" may be treated as the taxable value of a meal provided at the eating facility (see paragraph (j)(2)(ii) of this section). Alternatively, the employer may allocate the "total meal subsidy" among employees (see paragraph (j)(2)(iii) of this section).

(ii) *"Individual meal subsidy" defined.* The "individual meal subsidy" is determined by multiplying the price charged for a particular meal by a fraction, the numerator of which is the total meal value and the denominator of which is the gross receipts of the eating facility, and then subtracting the amount paid for the meal. The taxable value of meals provided to a particular employee during a calendar year, therefore, is the sum of the individual meal subsidies provided to the employee during the calendar year.

(iii) *Allocation of "total meal subsidy."* Instead of using the individual meal value method, the employer may allocate the "total meal subsidy" (total meal value less the gross receipts of the facility) among employees in any manner reasonable under the circumstances.

Par. 3. Section 1.132-1T is removed and a new §1.132-1T is added in its place, as follows:

§1.32-1T Exclusion from gross income of certain fringe benefits (Temporary).

(a) *In general.* Gross income does not include any fringe benefit which qualifies as a—

(1) no-ladditional-cost service,

(2) qualified employee discount,

(3) working condition fringe, or

(4) de minimis fringe.

Special rules apply with respect to certain on-premises gyms and other athletic facilities (§1.132-1T(e)), demonstration use of employer-provided automobiles by full-time automobile salesmen (§1.132-5T(n)), parking provided to an employee on or near the business premises of the employer (§1.132-5T(o)), and on-premises eating facilities (§1.322-7T).

(b) *Definition of employee*—(1) *No-additional-cost services and qualified employee discounts*. For purposes of section 132(a)(1) (relating to no-additional-cost services) and section 132(a)(2) (relating to qualified employee discounts), the term "employee" (with respect to a line of business of an employer) means—

(1) any individual who is currently employed by the employer in the line of business,

(ii) any individual who was formerly employed by the employer in the line of business and who separated from service with the employer in the line of business by reason of retirement or disability, and

(iii) any widow or widower of an individual who died while employed by the employer in the line of business or who separated from service with the employer in the line of business by reason of retirement or disability.

For purposes of this paragraph (b)(1), any partner who performs services for a partnership is considered employed by the partnership. In addition, any use by the spouse or dependent child (as defined in this paragraph (b)) of the employee will be treated as use by the employee.

(2) *Working condition fringes*. For purposes of section 132(a)(3) (relating to working condition fringes), the term "employee" means—

(i) any individual who is currently employed by the employer,

(ii) any partner who performs services for the partnership,

(iii) any director of the employer, and

(iv) any independent contractor who performs services for the employer.

Notwithstanding anything in this paragraph (b)(2) to the contrary, any independent contractor who performs services for the employer cannot exclude the value of parking or the use of consumer goods provided pursuant to a product testing program under §1.132-5T(n); in addition, any director of the employer cannot exclude the value of the use of consumer goods provided pursuant to a product testing program under §1.132-5T(n).

(3) *De minimis fringe*. For purposes of section 132(a)(4) (relating to de minimis fringes), the term "employee" means any recipient of a fringe benefit.

(4) *Dependent child*. For purposes of this paragraph (b), the term "dependent child" means any son, stepson, daughter, or stepdaughter of the employee who is a dependent of the employee, or both of whose parents are deceased. Any child to whom section 152(e) applies will be treated as the dependent of both parents.

(c) *Special rules for employers—Effect of section 414*. All employees treated as employed by a single employer under section 414(b), (c), or (m) will be treated as employed by a single employer for purposes of this section. Thus, employees of one corporation that is part of a controlled group of corporations may under certain circumstances be eligible to receive section 132 benefits from the other corporations that comprise the controlled group. However, the aggregation of employers described in this paragraph (c) does not change the other requirements for an exclusion, such as the line of business requirement. Thus, for example, if a controlled group of corporations consists of two corporations that operate in different lines of business, the corporations are not treated as operating in the same line of business even though the corporations are treated as one employer.

(d) *Customers not to include employees*. For purposes of section 132 and the regulations thereunder, the term "customer" means customers who are not employees. However, the preceding sentence does not apply to section 132(c)(2) (relating to the gross profit percentage for determining a qualified employee discount). Thus, an employer that provides employee discounts cannot exclude sales made to employees in determining the aggregate sales to customers.

(e) *Treatment of on-premises athletic facilities*— (1) *In general*. Gross income does not include the value of any on-premises athletic facility provided by the employer to its employees. For purposes of section 132 and this paragraph (e), the term "on-premises athletic facility" means any gym or other athletic facility such as a pool, tennis court, or golf course)—

(i) which is located on the premises of the employer,

(ii) which is operated by the employer, and

(iii) where substantially all of the use of which is, during the calendar year, by employees of the employer, their spouses, and their dependent children.

For purposes of this paragraph (e)(1)(iii), the term "dependent children" has the same meaning as the plural of the term "dependent child" in paragraph (b)(4) of this section. The exclusion of this paragraph (e) does not apply to any athletic facility if access to the facility is made available to the general public through the sale of memberships, the rental of the facility, etc.

(2) Premises of the employer. The athletic facility need not be located on the employer's business premises. However, the athletic facility must be located on premises of the employer. The exclusion provided in this paragraph (e) applies whether the premises are owned or leased by the employer; in addition, the exclusion is available even if the employer is not a named lessee on the lease so long as the employer pays reasonable rent. The exclusion provided in this paragraph (e) does not apply to any athletic facility that is a facility for residential use. Thus, for example, a resort with accompanying athletic facilities (such as tennis courts, pool, and gym) would not qualify for the exclusion provided in this paragraph (e).

(3) *Application of rules to membership in an athletic facility*. The exclusion provided in this paragraph (e) does not apply to any membership in an athletic facility (including health clubs or country clubs) unless the facility is owned (or leased) and operated by the employer and substantially all the use of the facility is by employees of the employer, their spouses, and their dependent children. Therefore, membership in a health club or country club not meeting the rules provided in this paragraph (e) would not qualify for the exclusion.

(4) *Operation by the employer*. An employer is considered to operate the athletic facility if the employer itself operates the facility through its own employees, or if the employer contracts out to another to operate the athletic fa-

cility. For example, if an employer hires an independent contractor to operate the athletic facility for the employer's employees, the facility is considered to be operated by the employer. In addition, if an athletic facility is operated by more than one employer, it is considered to be operated by each employer. For purposes of paragraph (e)(1)(iii) of this section, substantially all the use of a facility operated by more than one employer must be by employees of all of the employers, their spouses, and their dependent children. Where the facility is operated by more than one employer, an employer than either pays rent directly to the owner of the premises or pays rent to a named lessor of the premises is eligible for the exclusion.

(5) *Nonapplicability of nondiscrimination rules.* The nondiscrimination rules of section 132 and §1.132-8T do not apply to on-premises athletic facilities.

(f) *Nonapplicability of section 132.* If the tax treatment of a particular fringe benefit is expressly provided for in another section of Chapter 1, section 132 and the applicable regulations (except for section 132(e) and the regulations thereunder) do not apply to such fringe benefit. For example, since section 129 provides an exclusion from gross income for amounts paid or incurred by the employer for dependent care assistance for an employee, the exclusions under section 132 and this section do not apply to the provision by an employer to an employee of dependent care assistance.

Par. 4. The following new section is added at the appropriate place:

§1.132-2T No-additional-cost service (Temporary).

(a) *In general*—(1) *Definition.* Gross income does not include the value of a no-additional-cost service. The term "no-additional-cost service" means any service provided by an employer to an employee for the employee's personal use if—

(i) the service is offered for sale to customers in the ordinary course of the line of business of the employer in which the employee performs substantial services, and

(ii) the employer incurs no substantial additional cost in providing the service to the employee (including forgone revenue and excluding any amount paid by or on behalf of the employee for the service).

For rules relating to the line of business limitation, see §1.132-4T.

(2) *Examples.* Services that are eligible for treatment as no-additional-cost services are excess capacity services such as hotel accommodations; transportation by aircraft, train, bus, subway, or cruise line; and telephone services. Services that are not eligible for treatment as no-additional-cost services are non-excess capacity services such as the facilitation by a stock brokerage firm of the purchase of stock. Employees who receive non-excess capacity services may, however, be eligible for a qualified employee discount of up to 20 percent of the value of the service provided. See §1.132-3T.

(3) *Cash rebates.* The exclusion for a no-additional-cost service applies whether the service is provided at no charge or at a reduced price. The exclusion also applies if the benefit is provided through a partial or total cash rebate of an amount paid for the service.

(4) *Applicability of nondiscrimination rules.* The exclusion for a no-additional-cost service applies to officers, owners, and highly compensated employees only if the service is available on substantially the same terms to each member of a group of employees that is defined under a reasonable classification set up by the employer that does not discriminate in favor of officers, owners, or highly compensated employees. See §1.132-8T.

(5) *No substantial additional cost*—(i) *In general.* The exclsuion for a no-additional-cost service applies only if the employer does not incur substantial additional cost in providing the service to the employee. For purposes of the preceding sentence, the term "cost" includes revenue that is forgone because the service is provided to an employee rather than a nonemployee. (For purposes of determining whether any revenue is forgone, it is assumed that the employee would not have purchased the service unless it were available to the employee at the actual price charged to the employee.) Whether an employer incurs substantial additional cost must be determined without regard to any amount paid by the employee for the service. Thus, any reimbursement by the employee for the cost of providing the service does not affect the determination of whether the employer incurs substantial additional cost.

(ii) *Labor intensive services.* An employer must include the cost of labor incurred in providing services to employees when determining whether the employer has incurred substantial additional cost. An employer incurs substantial additional cost, whether or not non-labor costs are incurred, if a substantial amount of time is spent by the employer or its employees in providing the service to employees. This would be the result whether or not the time spent by the employer or its employees in providing the services would have been "idle", or if the services were provided outside normal business hours. An employer generally incurs no substantial additional cost, however, if the employee services provided are merely incidental to the primary service being provided by the employer. For example, the in-flight services of a flight attendant provided to airline employees traveling on a space-available basis are merely incidental to the primary service being provided (i.e., air transportation). In addition, the cost of in-flight meals provided to airline employees is not considered substantial in relation to the air transportation being provided.

(b) *Reciprocal agreements.* For purposes of the exclusion for a no-additional-cost service, any service provided by an employer to an employee of another employer shall be treated as provided by the employer of such employee if all of the following requirements are satisfied:

(1) The service is provided pursuant to a written reciprocal agreement between the employers under which a group of employees of each employer, all of whom perform substantial services in the same line of business, may receive no-additional-cost services from the other employer;

(2) The service provided pursuant to the agreement to the employees of both employers is the same type of service provided by the employers to customers both in the line of business in which the employees perform substantial services and the line of business in which the service is provided to customers; and

(3) Neither employer incurs substantial additional cost (including forgone

revenue) in providing the service to the employees of the other employer or pursuant to the agreement.

If one employer receives a substantial payment from the other employer with respect to the reciprocal agreement, the paying employer will be considered to have incurred a substantial additional cost pursuant to the agreement.

Par. 5. The following paragraph is added at the appropriate place:

§1.132-3T Qualified employee discount (Temporary).

(a) *In general*—(1) *Definition.* Gross income does not include the value of a qualified employee discount. The term "qualified employee discount" means any employee discount with respect to qualified property or services provided by an employer to an employee for the employee's personal use to the extent the discount does not exceed—

(i) the gross profit percentage of the price at which the property is offered to customers, for discounts on property, or

(ii) 20 percent of the price at which the services are offered to customers, for discounts on services.

(2) *Qualified property or services*—(i) *In general.* The term "qualified property or services" means any property or services that are offered for sale to customers in the ordinary course of the line of business of the employer in which the employee performs substantial services. For rules relating to the line of business limitation, see §1.132-4T.

(ii) *Exception for certain property.* The term "qualified property" does not include real property and it does not include personal property (whether tangible or intangible) of a kind commonly held for investment. Thus, an employee may not exclude from gross income the amount of an employee discount provided on the purchase of either residential or commercial real estate, securities, commodities, or currency, whether or not the particular purchase is made for investment purposes.

(iii) *Property and services not offered in ordinary coure of business.* The term "qualified property or services" does not include any property or services of a kind that is not offered for sale to customers in the ordinary course of the line of business of the employer. For example, employee discounts provided on property or services that are offered for sale only to employees and their families (such as merchandise sold at an employee store or through an employer-provided catalog service) may not be excluded from gross income.

(3) *No reciprocal agreement exception.* The exclusion for a qualified employee discount does not apply to property or services provided by another employer pursuant to a written reciprocal agreement that exists between employers to provide discounts on property and services to employees of the other employer.

(4) *Cash or third-party rebates*—(i) *Property or services provided without charge or at a reduced price.* The exclusion for a qualified employee discount applies whether the property or service is provided at no charge (in which case only part of the discount may be excludable as a qualified employee discount) or at a reduced price. The exclusion also applies if the benefit is provided through a partial or total cash rebate of an amount paid for the property or service.

(ii) *Property or services provided directly by the employer or indirectly through a third party.* For example, an employee of an appliance manufacturer may receive a qualified employee discount on the manufacturer's applicances purchased at a retail store that offers such appliances for sale to customers. The employee may exclude the amount of the qualified employee discount whether the employee is provided the appliance at no charge or purchases it at a reduced price, or whether the employee receives a partial or total cash rebate from either the employer-manufacturer or the retailer. If an employee receives additional rights associated with the property that are not provided by the employee's employer to customers in the ordinary course of the line of business in which the employee performs substantial services (such as the right to return or exchange the property or special warranty rights), the employee may only receive a qualified employee discount with respect to the property and not the additional rights. Receipt of such additional rights may occur, for example, when an employee of a manufacturer purchases property manufacturered by the employee's employer at a retail outlet.

(5) *Applicability of nondiscrimination rules.* The exclusion for a qualified employee discount applies to officers, owners, and highly compensated employees only if the discount is available on substantially the same terms to each member of a group of employees that is defined under a reasonable classification set up by the employer that does not discriminate in favor of officers, owners, or highly compensated employees. See §1.132-8T.

(b) *Employee discount*—(1) *Definition.* The term "employee discount" means the excess of—

(i) the price at which the property or service is being offered by the employer for sale to customers, over

(ii) the price at which the property or service is provided by the employer to an employee for use by the employee.

A transfer of property by an employee without consideration is considered use by the employee for purposes of this section. Thus, for example, if an employee receives a discount on property offered for sale by his employer to customers and the employee makes a gift of the property to his parent, the property will be considered to be provided for use by the employee, thus enabling the discount to be eligible for exclusion as a qualified employee discount.

(2) *Price to customers*—(i) *Determined at time of sale.* In determining the amount of an employee discount, the price at which the property or service is being offered to customers at the time of the employee's purchase is controlling. for example, assume that an employer offers a product to customers for $20 during the first six months of a calendar year, but at the time the employee purchases the product at a discount, the price at which the product is being offered to customers is $25. In this case, the price from which the employee discount is measured is $25.

(ii) *Quantity discount not reflected.* The price referred to in paragraph (b)(2)(i) of this section cannot reflect any quantity discount unless the employee actually purchases the requisite quantity of the property or service.

(iii) *Customers of employee's employer controls.* In determining the amount of an employee discount, the price at which the property or service is offered to customers of the employee's employer is controlling. Thus, the price at which property is sold to the wholesale customers of a manufacturer will generally be lower than the price at which the same property is sold to the customers of a retailer. However, see paragraph (a)(4)(ii) of this section regarding the effect of a wholesaler providing to its employees additional rights not provided to customers of the wholesaler in the ordinary course of its business.

(iv) *Discounts to discrete customer or consumer groups*. In determining the amount of an employee discount, if an employer offers for sale property or services at one or more discounted prices to discrete customer or consumer groups, and sales at all such discounted prices comprise at least 35 percent of the employer's gross sales for a representative period, then the price at which property or service is being offered to customers is a discounted price. The applicable discounted price is the current undiscounted price, reduced by the percentage discount at which the greatest percentage of the employer's gross sales are made for such representative period. If sales at different percentage discounts equal the same percentage of the employer's gross sales, the price at which the property or service is being provided to customers may be reduced by the average of the two group discounts. For purposes of this section, a representative period is the taxable year of the employer immediately preceding the taxable year in which the property or service is provided to the employee at a discount. If more than one employer would be aggregated under section 414(b), (c), or (m), and all of the employers do not have the same taxable year, the employers required to be aggregated must designate the 12-month period to be used in determining gross sales for a representative period.

(v) *Examples*. The rules provided in this paragraph (b)(2) are illustrated by the following examples:

Example (1). Assume that a wholesale employer offers property for sale to two discrete customer groups at differing prices. Assume further that during the prior taxable year of the employer, 70 percent of the employer's gross sales are made at a 15-percent discount and 30 percent at no discount. The current undiscounted price at which the property or service is being offered by the employer for sale to customers may be reduced by the 15-percent discount.

Example (2). Assume that a retail employer offers a 20 percent discount to members of the American Bar Association, a 15 percent discount to members of the American Medical Association, and a ten percent discount to employees of the Federal Government. Assume further that during the prior taxable year of the employer, sales to American Bar Association members equal 15 percent of the employer's gross sales, sales to American Medical Association members equal 20 percent of the employer's gross sales, and sales to Federal Government employees equal 25 percent of the employer's gross sales. The current undiscounted price at which the property or service is being offered by the employer for sale to customers may be reduced by the ten percent Federal Government discount.

(3) *Damaged, distressed, or returned goods*. If an employee pays at least fair market value for damaged, distressed, or returned property, such employee will not have income attributable to such purchase.

(c) *Gross profit percentage*—(1) *In general*—(i) *General rule*. An exclusion from gross income for an employee discount on qualified property is limited to the price at which the property is being offered to customers in the ordinary course of the employer's line of business, multiplied by the employer's gross profit percentage. The term "gross profit percentage" means the excess of the aggregate sales price of the property sold by the employer to customers (including employees) over the employer's aggregate cost of the property, then divided by the aggregate sales price.

(ii) *Calculation of gross profit percentage*. The gross profit percentage must be calculated separately for each line of business based on the aggregate sales price and aggregate cost of property in that line of business for a representative period. For purposes of this section, a representative period is the taxable year of the employer immediately preceding the taxable year in which the discount is available. For example, if the aggregate sales of property in an employer's line of business for the prior taxable year were $800,000, and the aggregate cost of the property for the year were $600,000, the gross profit percentage would be 25 percent ($800,000 minus $600,000, then divided by $800,000). If more than one employer would be aggregated under section 414(b), (c), or (m), and all of the employers do not have the same taxable year, the employers required to be aggregated must designate the 12-month period to be used in determining the gross profit percentage. If an employee performs substantial services in more than one line of business, the gross profit percentage of the line of business in which the property is sold determines the amount of the excludable employee discount.

(ii) *Special rule for employers in their first year of existence*. An employer in its first year of existence may estimate the gross profit percentage of a line of business based on its mark-up from cost. Alternatively, an employer in its first year of existence may determine the gross profit percentage by reference to an appropriate industry average.

(iv) *Redetermination of gross profit percentage*. If substantial changes in an employer's business indicate at any time that it is inappropriate for the prior years' gross profit percentage to be used for the current year, the employer must, within a reasonable period, redetermine the gross profit percentage for the remaining portion of the current year as if such portion of the year were the first year of the employer's existence.

(2) *Line of business*. In general, an employer must determine the gross profit percentage on the basis of all property offered to customers (including employees) in each separate line of business. An employer may instead select a classification of property that is narrower than the applicable line of business. However, such classification must be reasonable. For example, if an employer computes gross profit percentage according to the department in which products are sold, such classification is reasonable. Similarly, it is reasonable to compute gross profit percentage on the basis of the type of merchandise sold (such as high mark-up and low mark-up classifications). It is not reasonable, however, for an employer to classify certain low mark-up products preferred by certain employees (such as officers, owners, and highly compensated employees) with high mark-up products or to classify certain high mark-up products preferred by other employees with low mark-up products.

(3) *Generally accepted accounting principles*. In general, the aggregate sales price of property must be determined in accordance with generally accepted accounting principles. An employer must compute the aggregate cost of property in the same manner in

which it is computed for the employer's Federal income tax liability, pursuant to the inventory rules in section 471 and the regulations thereunder.

(d) *Treatment of leased sections of department stores*—(1) *In general*—(i) *General rule*. For purposes of determining whether employees of a leased section of a department store may receive qualified employee discounts at the department store and whether employees of the department store may receive qualified employee discounts at the leased section of the department store, the leased section is treated as part of the line of business of the person operating the department store, and employees of the lease section are treated as employees of the person operating the department store as well as employees of their employer. The term "leased section of a department store" means a section of a department store where substantially all of the gross receipts of the leased section are over-the-counter sales of property made under a lease, license, or similar arrangement where it appears to the general public that individuals making such sales are employed by the department store. An example of a leased section of a department store is a cosmetics firm that leases floor space from a department store.

(ii) *Calculation of gross profit percentage*. When calculating the gross profit percentage of property and services sold at the department store under paragraph (c) of this section, sales of property and services sold at the department store, as well as sales of property and services sold at the leased section, are considered. The rule provided in the preceding sentence does not apply, however, if it is reasonable to calculate the gross profit percentage for the department store and leased section separately, or if it would be inappropriate to combine them (such as where either the department store or the leased section, but not both, provides employee discounts).

(2) *Employees of the leased section*—(i) *Definition*. For purposes of this paragraph (d), "employees of the leased section" means all employees who perform substantial services at the leased section regardless of whether the employees engage in over-the-counter sales of property or services. The term "employee" has the same meaning as in section 132(f).

(ii) *Discounts offered to either department store employees or employees of the leased section*. If the requirements of this paragraph (d) are satisfied, employees of the leased section may receive qualified employee discounts at the department store regardless of whether employees of the department store are offered discounts at the leased section. Similarly, regardless of whether employees of the leased section are offered discounts at the department store, employees of the department store may receive qualified employee discounts at the leased section.

(e) *Excess discounts*. Unless excludable under a statutory provision other than section 132(a)(2), an employee discount provided on property is excludable to the extent of the gross profit percentage multiplied by the price at which the property is being offered for sale to customers. If an employee discount exceeds the gross profit percentage, the excess discount is includible in the employee's income. For example, if the discount on property is 30 percent and the employer's gross profit percentage for the period in the relevant line of business is 25 percent, then 5 percent of the price at which the property is being offered for sale to customers is includible in the employee's income. With respect to services, an employee discount of up to 20 percent may be excludable. If an employee discount exceeds 20 percent, the excess discount is includible in the employee's income.

Par. 6. The following section is added at the appropriate place:

§1.132-4T Line of business limitation (Temporary).

(a) *In general*—(1) *Applicability*—(i) *General rule*. A no-additional-cost service or qualified employee discount provided to an employee must be for property or services that are offered for sale to customers in the ordinary course of the same line of business in which the employee receiving the property or service performs substantial services. Thus, an employee who does not perform substantial services in a particular line of business of the employer may not exclude the value of services or employee discounts received on property or services in that line of business.

(ii) *Property and services sold to employees rather than customers*. Since the property or services must be offered for sale to customers in the ordinary course of the same line of business in which the employee performs substantial services, the line of business limitation is not satisfied if the employer's products or services are sold to employees of the employer, rather than to customers. Thus, for example, an employer in the banking line of business is not considered in the variety store line of business if the employer establishes an employee store that offers variety store items for sale to the employer's employees.

(iii) *Performance of substantial services in more than one line of business*. An employee who performs services in more than one of the employer's lines of business may only exclude no-additional-cost services and qualified employee discounts in the lines of business in which the employee performs substantial services.

(iv) *Performance of services that directly benefit more than one line of business*—(A) *In general*. An employee who performs substantial services that directly benefit more than one line of business of an employer is treated as performing substantial services in all such lines of business. For example, an employee who maintains accounting records for an employer's three lines of business may receive qualified employee discounts in all three lines of business.

(B) *Significantly interrelated minor line of business*. The employees of a minor line of business of an employer that is significantly interrelated with a major line of business of the employer who perform substantial services that directly benefit both the major and the minor lines of business are treated as employees of both the major and the minor lines of business. Employees of the minor line of business who do not perform substantial services which directly benefit the major line of business are not treated as employees of the major line of business. A minor line of business is significantly interrelated with a major line of business when, for example, the activity of the minor line of business is directly related to but is a minor part of the major line of business (such as laundry services provided at a hospital).

(C) *Examples*. The rules provided in

this paragraph are illustrated in the following examples:

Example (1). Assume that employees of units of an employer provide repair or financing services, or sell by catalog, with respect to retail merchandise sold by the employer. Such employees may be considered as employees of the retail merchandise line of business under this paragraph (a)(1)(iv).

Example (2). Assume that an employer operates a hospital and a laundry service. Assume further that some of the gross receipts of the laundry service line of business are from laundry services sold to customers other than the hospital employer. Only the employees of the laundry service who perform substantial services which directly benefit the hospital line of business (through the provision of laundry services to the hospital) will be treated as employees of the hospital line of business. Other employees of the laundry service line of business will not be treated as employees of the hospital line of business.

(*Example (3).* Assume the same facts as in example (2), except that the minor line of business also operates a chain of dry cleaning stores. Employees who perform substantial services which directly benefit the dry cleaning stores but who do not perform substantial services that directly benefit the hospital line of business will not be treated as employees of the hospital line of business.

(2) *Definition*—(i) *In general*. An employer's line of business is determined by reference to the Enterprise Standard Industrial Classification Manual (ESIC Manual) prepared by the Statistical Policy Division of the U.S. Office of Management and Budget. [To be reprinted in 1986-4 I.R.B.] An employer is considered to have more than one line of business if the employer offers for sale to customers property or services in more than one two-digit code classification referred to in the ESIC Manual.

(ii) *Examples*. Examples of two-digit classifications are general retail merchandise stores; hotels and other lodging places; auto repair, services, and garages; and food stores.

(3) *Aggregation of two-digit classifications*. If, pursuant to paragraph (a)(2) of this section, an employer has more than one line of business, such lines of business will be treated as a single line of business where and to the extent that one or more of the following aggregation rules apply:

(i) If it is uncommon in the industry of the employer for any of the separate lines of business of the employer to be operated without the others, the separate lines of business are treated as one line of business.

(ii) If it is common for a substantial number of employees (other than those employees who work at the headquarters or main office of the employer) to perform substantial services for more than one line of business of the employer, so that determination of which employees perform substantial services for which line of business would be difficult, then the separate lines of business of the employer in which such employees perform substantial services are treated as one line of business. For example, assume that an employer operates a delicatessen with an attached service counter at which food is sold for consumption on the premises. Assume further that most but not all employees work both at the delicatessen and at the service counter. The delicatessen and the service counter are treated as one line of business.

(iii) If the retail operations of an employer that are located on the same premises are in separate lines of business but would be considered to be within one line of business under paragraph (a)(2) of this section if the merchandise offered for sale in such lines of business were offered for sale at a department store, then the operations are treated as one line of business. For example, assume that on the same premises an employer sells both women's apparel and jewelry. Since, if sold together at a department store, the operations would be part of the same line of business, the operations are treated as one line of business.

(b) *Grandfather rule for certain retail stores*—(1) *In general*. The line of business limitation may be relaxed under a special grandfather rule. If—

(i) on October 5, 1983, 85 percent of the employees of one member of an affiliated group (as defined in section 1504 without regard to subsections (b)(2) and (b)(4) thereof) were entitled to employee discounts at retail department stores operated by another member of the affiliated group, and

(ii) More than 50 percent of the current year's sales of the affiliated group are attributable to the operation of retail department stores,

then for purposes of the exclusion from gross income of a qualified employee discount, the first member is treated as engaged in the same line of business as the second member (the operator of the retail department stores). Therefore, employees of the first member of the affiliated group may exclude qualified employee discounts received at the retail department stores operated by the second member. However, employees of the second member of the affiliated group may not exclude any discounts received on property or services offered for sale to customers by the first member of the affiliated group.

(2) *Taxable year of affiliated group*. If all of the members do not have the same taxable year, the affiliated group must designate the 12-month period to be used in determining the "current year's sales" (as referred to in this paragraph (b)). The 12-month period designated, however, must be used consistently.

(3) *Definition of "sales"*. For purposes of this paragraph (b), the term "sales" means the gross receipts of the affiliated group, based upon the accounting methods used by its members.

(4) *Retired and disabled employees*. For purposes of this paragraph (b), an employee includes any individual who was, or whose spouse was, formerly employed by the first member of the affiliated group and who separated from service with the member by reason of retirement or disability if the second member of the group provided employee discounts to such individuals on October 5, 1983.

(5) *Increase of employee discount*. If, after October 5, 1983, the employee discount described in this paragraph (b) is increased, the grandfather rule of this paragraph (b) does not apply to the amount of the increase. For example, if on January 1, 1985, the employee discount is increased from ten percent to 15 percent, the grandfather rule will not apply to the additional five percent discount.

(c) *Relaxation of line of business requirement*. The line of business requirement may be relaxed under an elective grandfather rule provided in section 4977. For rules relating to the section 4977 election, see §54.4977-1.

Par. 7. The following section is added at the appropriate place:

§1.132-5T Working condition fringe (Temporary).

(a) *In general*—(1) *Definition*. Gross income does not include the value of a working condition fringe. The term "working condition fringe" means any property or service provided to an employee of an employer to the extent that, if the employee paid for the property or service, the amount paid would be allowable as a deduction under section 162 or 167. If, under section 274 or any other section, certain substantiation requirements must be met in order for a deduction under section 162 or 167 to be allowable, those substantiation requirements apply to the determination of a working condition fringe. An amount that would be deductible by the employee under, for example, section 212 is not a working condition fringe.

(2) *Trade or business of the employee.* If the hypothetical payment for the property or service would be allowable as a deduction with respect to a trade or business of the employee other than the employee's trade or business of being an employee of the employer, it cannot be taken into account for purposes of determining the amount, if any, of the working condition fringe. For example, assume that, unrelated to company X's trade or business and unrelated to company X's employee's trade or business of being an employee of company X, the employee is a member of the board of directors of company Y. Assume further that company X provides the employee with air transportation to a company Y board of director's meeting. The employee may not exclude the value of the air transportation to the meeting as a working condition fringe. The employee may, however, deduct such amount under section 162 if the section 162 requirements are satisfied. The result would be the same whether the air transportation was provided in the form of a flight on a commercial airline or a seat on a company X airplane.

(b) *Vehicle allocation rules*—(1) *In general*—(i) *General rule.* In general, with respect to an employer-provided vehicle, the amount excludable as a working condition fringe is the amount that would be allowable as a deduction under section 162 or 167 if the employee paid for the availability of the vehicle. For example, assume that the value of the availability of an employer-provided vehicle for a full year is $2,000, without regard to any working condition fringe (i.e., assuming all personal use). Assume further that the employee drives the vehicle 6,000 miles for his employer's business and 2,000 miles for reasons other than the employer's business. In this situation, the value of the working condition fringe is $2,000 multiplied by a fraction, the numerator of which is the business-use mileage (6,000 miles) and the denominator of which is the total mileage (8,000 miles). Thus, the value of the working condition fringe is $1,500. The total amount includible in the employee's gross income on account of the availability of the vehicle is $500. For purposes of this section, the term "vehicle" has the same meaning given the term in §1.61-2T(e)(2). Generally, when determining the amount of an employee's working condition fringe, miles accumulated on the vehicle by all employees of the employer during the period in which the vehicle is available to the employee must be considered. For example, assume that an employee of the employer is provided the availability of an automobile for one year. Assume further that during the year, the automobile is regularly used in the employer's business by other employees. All miles accumulated on the automobile by all employees of the employer during the year must be considered. If, however, substantially all the use of the automobile by other employees in the employer's business is permitted during a certain period, such as the last three months of the year, the miles driven by the other employees during that period would not be considered when determining the employee's working condition fringe exclusion.

(ii) *Use by an individual other than the employee.* For purposes of this section, if the availability of a vehicle to an individual would be taxed to an employee, use of the vehicle by the individual is included in references to use by the employee.

(iii) *Provision of an expensive vehicle for personal use.* Assume an employer provides an employee with an expensive vehicle that an employee may use in part for personal purposes. Even though the decision to provide an expensive rather than an inexpensive vehicle is made by the employer for bona fide noncompensatory business reasons, there is no working condition fringe exclusion with respect to the personal miles driven by the employee. If the employee paid for the availability of the vehicle, he would not be entitled to deduct any part of the payment attributable to personal miles.

(2) *Use of different employer-provided automobiles.* The working condition fringe exclusion must be applied on an automobile by automobile basis. For example, assume that automobile Y is available to employee D for 3 days in January and for 5 days in March, and automobile Z is available to D for a week in July. Assume further that the Daily Lease Value, as defined in §1.61-2T, of each automobile is $50. For the eight days of availability of Y in January and March, D uses Y 90 percent for business (by mileage). During July, D uses Z 60 percent for business (by mileage). The value of the working condition fringe is determined separately for each automobile. Therefore, the working condition fringe for Y is $360 ($400 × .90) leaving an income inclusion of $40. The working condition fringe for Z is $210 ($350 × .60) leaving an income inclusion of $140. If the value of the availability of an automobile is determined under the Annual Lease Value rule for one period and Daily Lease Value rule for a second period (see §1.61-2T), the working condition fringe exclusion must be calculated separately for the two periods.

(c) *Applicability of section 162 and 274(d)*—(1) *In general.* The value of property or services provided to an employee may not be excluded from the employee's gross income as a working condition fringe, by either the employer or the employee, unless the applicable substantiation requirements of either section 274(d) or section 162 (whichever is applicable) and the regulations thereunder are satisfied. With respect to listed property, the substantiation requirements of section 274(d) and the regulations thereunder do not apply to the determination of an employee's working condition fringe exclusion prior to the date that those requirements apply to the first taxable year of the employer beginning after December 31, 1985. For example, if an employer's first taxable year beginning after December 31, 1985, begins on July 1, 1986, with respect to listed property, the substantiation requirements of section 274(d) apply as of that date. The substantiation requirements of section 274(d) apply to an employee even if the requirements of section 274 do not apply to the employee's employer for deduction purposes (such as when the employer is a tax-exempt organization or a governmental unit); in these cases, the requirements of section 274(d) apply to the employee as of January 1, 1986.

(2) *Section 274(d) requirements.* The substantiation requirements of section 274(d) are satisfied by "adequate records or sufficient evidence corroborating the [employee's] own statement". Therefore, such records or evidence provided by the employee, and relied upon by the employer to the extent permitted by the regulations promulgated under section 274(d), will be sufficient to substantiate a working condition fringe exclusion.

(d) *Safe harbor rules*—(1) *In general.* Section 1.274-6T provides that the substantiation requirements of section 274(d) and the regulations thereunder may be satisfied, in certain circumstances, by using one or more of the safe harbor rules prescribed in §1.274-6T. If the employer uses one of the safe harbor rules prescribed in §1.274-6T during a period with respect to a vehicle (as defined in §1.61-2T), that rule must be used by the employer to substantiate a working condition fringe exclusion with respect to that vehicle during the period. An employer that is exempt from Federal income tax may still use one of the safe harbor rules (if the requirements of that section are otherwise met during a period) to substantiate a working condition fringe exclusion with respect to a vehicle during the period. If the employer uses one of the methods prescribed in §1.274-6T during a period with respect to an employer-provided vehicle, that method may be used by an employee to substantiate a working condition fringe exclusion with respect to the same vehicle during the period, as long as the employee includes in gross income the amount allocated to the employee pursuant to §1.274-6T and this section. (See §1.61-2T(c)(2)(i) for other rules concerning when an employee must include in income the amount determined by the employer.) If, however, the employer uses the safe harbor rule prescribed in §1.274-6T(a)(2) or (3) and the employee without the employer's knowledge uses the vehicle for purposes other than de minimis personal use (in the case of the rule prescribed in §1.274-6T (a)(2)), or for purposes other than de minimis personal use and commuting (in the case of the rule prescribed in §1.274-6T(a)(3)), then the employee must include additional income for the unauthorized use of the vehicle.

(2) *Period for use of safe harbor rules.* The rules prescribed in this paragraph (d) assume that the safe harbor rules prescribed in §1.274-6T are used for a one-year period. Accordingly, references to the value of the availability of a vehicle, amounts excluded as a working condition fringe, etc., are based on a one-year period. If the safe harbor rules prescribed in §1.274-6T are used for a period of less than a year, the amounts referenced in the previous sentence must be adjusted accordingly. For purposes of this section, the term "personal use" has the same meaning as prescribed in §1.274-6T(e)(5).

(e) *Vehicles not available to employees for personal use.* For a vehicle described in §1.274-6T(a)(2) (relating to certain vehicles not used for personal purposes), the working condition fringe exclusion is equal to the value of the availability of the vehicle if the employer uses the method prescribed in §1.274-6T(a)(2).

(f) *Vehicles not available to employees for personal use other than commuting.* For a vehicle described in §1.274-6T(a)(3) (relating to certain vehicles not used for personal purposes other than commuting), the working condition fringe exclusion is equal to the value of the availability of the vehicle for purposes other than commuting if the employer uses the method prescribed in §1.274-6(T)(a)(3). This rule applies only if the special rule for valuing commuting use, as prescribed in §1.61-2T, is used and the amount determined under the special rule is either included in the employee's income or reimbursed by the employee.

(g) *Vehicles used in connection with the business of farming that are available to employees for personal use*—(1) *In general.* For a vehicle described in §1.274-6T(b) (relating to certain vehicles used in connection with the business of farming), the working condition fringe exclusion is calculated by multiplying the value of the availability of the vehicle by 75 percent.

(2) *Vehicles available to more than one individual.* If the vehicle is available to more than one individual, the employer must allocate the gross income attributable to the vehicle (25 percent of the value of the availability of the vehicle) among the employees (and other individuals whose use would not be attributed to an employee) to whom the vehicle was available. This allocation must be done in a reasonable manner to reflect the personal use of the vehicle by the individuals. An amount that would be allocated to a sole proprietor reduces the amounts that may be allocated to employees but are otherwise to be disregarded for purposes of this paragraph (g). For purposes of this paragraph (g), the value of the availability of a vehicle may be calculated as if the vehicle were available to only one employee continuously and without regard to any working condition fringe exclusion.

(3) *Examples.* The following examples illustrate a reasonable allocation of gross income with respect to an employer-provided vehicle between two employees:

Example (1). Assume that two farm employees share the use of a vehicle which for a calendar year is regularly used directly in connection with the business of farming and qualifies for use of the rule in §1.274-6T(b). Employee A uses the vehicle in the morning directly in connection with the business of farming and employee B uses the vehicle in the afternoon directly in connection with the business of farming. Assume further that employee B takes the vehicle home in the evenings and on weekends. The employer should allocate all the income attributable to the availability of the vehicle to employee B.

Example (2). Assume that for a calendar year, farm employees C and D share the use of a vehicle that is regularly used directly in connection with the business of farming and qualifies for use of the rule in §1.274-6T(b). Assume further that the employees alternate taking the vehicle home in the evening and alternate the availability of the vehicle for personal purposes on weekends. The employer should allocate the income attributable to the availability of the vehicle for personal use (25 percent of the value of the availability of the vehicle) equally between the two employees.

Example (3). Assume the same facts as in example (2) except that C is the sole proprietor of the farm. Based on these facts, C should allocate the same amount of income to D as was allocated to D in example (2). No other income attributable to the availability of the vehicle for personal use should be allocated.

(h) *Qualified non-personal use vehicles.* Effective January 1, 1985, 100 percent of the value of the use of qualified nonpersonal use vehicle (as described in §1.274-5T(k)) is excluded from gross income as a working condition fringe, provided that, in the case of a vehicle described in paragraph (k)(3) through (7) of that section, the use of the vehicles conforms to the requirements of that paragraph.

(i) [Reserved].

(j) *Application of section 280F*. In determining the amount, if any, of an employee's working condition fringe, section 280F and the regulations thereunder do not apply. For example, assume that an employee has available for a calendar year an employer-provided automobile with a fair market value of $28,000. Assume further that the special rule provided in §1.61-2T is used and that the Annual Lease Value, as defined in §1.61-2T, is $7,750, and that all of the employee's use of the automobile is in the employer's business. The employee would be entitled to exclude the entire Annual Lease Value as a working condition fringe, despite the fact that if the employee paid for the availability of the automobile, an income inclusion would be required under §1.280F-5T(d)(1). This paragraph (j) does not affect the applicability of section 280F to the employer with respect to such employer-provided automobile, nor does it affect the applicability of section 274. For rules concerning substantiation of an employee's working condition fringe, see paragraph (c) of this section.

(k) *Aircraft allocation rule*. In general, with respect to a flight on an employer-provided aircraft, the amount excludable as a working condition fringe is the amount that would be allowable as a deduction under section 162 or 167 if the employee paid for the flight on the aircraft. For example, if employee P flies on P's employer's airplane primarily for business reasons of P's employer, the value of P's flight is excludable as working condition fringe. However, if P's spouse and children accompany P on such airplane trip primarily for personal reasons, the value of the flights by P's spouse and children are includible in P's gross income. See §1.61-2T(g) for special rules for valuing personal flights.

(l) [Reserved].

(m) *Employer-provided transportation for security concerns*—(1) *In general*. The amount of a working condition fringe exclusion with respect to employer-provided transportation is the amount that would be allowable as a deduction under section 162 or 167 if the employee paid for the transportation. Generally, if an employee pays for transportation taken for primarily personal purposes, the employee may not deduct any part of the amount paid. Thus, the employee may not generally exclude the value of employer-provided transportation as a working condition fringe if such transportation is primarily personal. If, however, for bona fide business-oriented security concerns, the employee purchases transportation that provides him or her with additional security, the employee may generally deduct the excess of the amount paid for the transportation over the lesser amount the employee would have paid for the same mode of transportation absent the bona fide business-oriented security concerns. With respect to a vehicle, the phrase "the same mode of transportation" means use of the same vehicle without the additional security aspects, such as bulletproof glass. With respect to air transportation, the phrase "the same mode of transportation" means comparable air transportation. These same rules apply to the determination of an employee's working condition fringe exclusion. For example, if an employer provides an employee with an automobile for commuting and, for bona fide business-oriented security concerns, the automobile is specially designed for security, then the employee may exclude the value of the special security design as a working condition fringe if the employee's automobile would not have had such security design but for the bona fide business-oriented security concerns. The employee may not exclude the value of the commuting from income as a working condition fringe because commuting is a nondeductible personal expense. Similarly, if an employee travels on a personal trip in an employer-provided aircraft for bona fide business-oriented security concerns, the employee may exclude the excess, if any, of the value of the flight over the amount the employee would have paid for comparable air transportation, but for the bona fide business-oriented security concerns. Because personal travel is a nondeductible expense, the employee may not exclude the total value of the trip as a working condition fringe.

(2) *Demonstration of bona fide business-oriented security concerns*—(i) *In general*. For purposes of this paragraph (m), the existence of a bona fide business-oriented security concern for the furnishing of a specific form of transportation to an employee is determined on the basis of all the facts and circumstances within the following guidelines:

(A) *Services performed outside the United States*. With respect to an employee performing services for an employer in a geographic area other than the United States, a factor indicating a bona fide business-oriented security concern is a recent history of violent terrorist activity in such geographic area (such as bombings or abductions for ransom), unless such activity is focused on a group of individuals which does not include the employee or a similarly situated employee or on a section of the geographic area which does not include the employee.

(B) *Services performed in the United States*. With respect to an employee performing services for an employer in the United States, a factor indicating a bona fide business-oriented security concern is threats on the life of the employee or on the life of a similarly situated employee because of the employee's status as an employee of the employer.

(ii) *Establishment of overall security program*. Notwithstanding anything in paragraph (m)(2)(i) of this section to the contrary, *no* bona fide business-oriented security concern will be deemed to exist unless the employee's employer establishes an overall security program with respect to the employee involved.

(iii) *Overall security program*—(A) *Definition*. An overall security program is one in which security is provided to protect the employee on a 24-hour basis. The employee must be protected while at the employee's residence, while commuting to and from the employee's workplace, and while at the employee's workplace. In addition, the employee must be protected while traveling, whether for business or personal purposes. An overall security program would include the provision of a bodyguard/driver who is trained in evasive driving techniques; an automobile specially equipped for security; guards, metal detectors, alarms, or similar methods of controlling access to the employee's workplace and residence; and, in appropriate cases, flights on the employer's aircraft for business and personal reasons.

(B) *Application*. There is no overall

security program when, for example, security is provided at the employee's workplace but not at the employee's residence. In addition, the fact that an employer requires an employee to travel on the employer's aircraft, or in an employer provided vehicle that contains special security features, does not alone constitute an overall security program. The preceding sentence applies regardless of the existence of a corporate or other resolution requiring the employee to travel in the employer's airplane or vehicle for personal as well as business reasons. Similarly, the existence of an independent security study particular to the employer and its employees, or to the employee involved, does not alone constitute an overall security program.

(iv) *Effect of an independent security study*. An overall security program with respect to an employee is deemed to exist even through security is not provided to an employee on a 24-hour basis if the conditions of this paragraph (m)(2)(iv) are satisfied:

(A) A security study is performed with respect to the employer and the employee (or a similarly situated employee) by an independent security consultant;

(B) The security study is based on an objective assessment of all the facts and circumstances;

(C) The recommendation of the security study is that an overall security program (as defined in paragraph (m)(2)(iii) of this section) is not necessary and such recommendation is reasonable under the circumstances; and

(D) The employer applies the specific security recommendations contained in the security study to the employee on a consistent basis.

The value of the security provided pursuant to a security study that meets the requirements of this paragraph (m)(2)(iv) may be excluded from income, if the security study conclusions are reasonable and, but for the bona fide business-oriented security concerns, the employee would not have had such security. No exclusion from income applies to security provided by the employer that is not recommended in the security study. Security study conclusions may be reasonable even if, for example, it is recommended that security be limited to certain geographic areas, as in the case where air travel security is provided only in certain foreign countries.

(v) *Application of security rules to spouses and dependents*. The availability of a working condition fringe exclusion based on the existence of a bona fide business-oriented security concern with respect to the spouse and dependents of an employee is determined separately for such spouse and dependents under the rules established in this paragraph (m).

(vi) *Working condition safe harbor*. Under the special rule of this paragraph (m)(2)(vi), if, for a bona fide business-oriented security concern, the employer requires that the employee travel on an employer-provided aircraft for a personal trip, the employer and the employee may exclude, as a working condition fringe, the excess value of the trip over comparable first-class airfare without having to show that but for the bona fide business-oriented security concerns, the employee would have flown first-class on a commercial aircraft. If the special valuation rule provided in §1.61-2T is used, the excess over the amount determined by multiplying an aircraft multiple of 200-percent by the base aircraft valuation formula may be excluded as a working condition fringe.

(3) *Examples*. The provisions of this paragraph (m) may be illustrated by the following examples:

Example (1). Assume that in response to several death threats on the life of A, the president of a multinational company (company X), company X establishes an overall security program for A, including an alarm system at A's home and guards at A's workplace, the use of a vehicle that is specially equipped with alarms, bullet-proof glass, and armor plating and a bodyguard/driver who is trained in evasive driving techniques. Assume further that A is driven for both personal and business reasons in the vehicle. Also, assume that but for the bona fide business-oriented security concerns, no part of the overall security program would have been provided to A. With respect to the transportation provided for security reasons, A may exclude as a working condition fringe the value of the special security features of the vehicle and the value attributable to the bodyguard/driver. Thus, if the value of the specially equipped vehicle is $40,000, and the value of the vehicle without the security features is $25,000, A may determine A's income attributable to the vehicle as if the vehicle were worth $25,000. A must include in income the value of the availability of the vehicle for personal use.

Example (2). Assume that B is the chief executive officer of a multinational corporation (company Y). Assume further that there have been kidnapping attempts and other terrorist activities in the foreign countries in which B performs services and that at least some of such activities have been directed against B or similarly situated employees. In response to these activities, company Y provides B with an overall security program, including an alarm system at B's home and bodyguards at B's workplace, a bodyguard/driver who is trained in evasive driving techniques, and a vehicle specially designed for security during B's overseas travels. In addition, assume that company Y requires B to travel in company Y's airplane for business and personal trips taken to, from, and within these foreign countries. Also, assume that but for bona fide business-oriented security concerns, no part of the overall security program would have been provided to B. B may exclude as a working condition fringe the value of the special security features of the automobile and the value attributable to the bodyguards and the bodyguard/driver. B may also exclude as a working condition fringe the excess, if any, of the value of personal flights in the company Y airplane over first-class airfare (as determined under the special valuation rule provided in §1.61-2T if the safe harbor described in paragraph (m)(2)(vi) of this section is used). B must include in income the value of the availability of the vehicle for personal use and the lesser of the value of first-class airfare or the value of the flight determined under §1.61-2T for each personal flight taken by B in company Y's airplane.

Example (3). Assume the same facts as in example (2) except that company Y also requires B to travel in company Y's airplane within the United States, and provides B with a chauffeur-driven limousine for business and personal travel in the United States. Assume further that company Y also requires B's spouse and dependents to travel in company Y's airplane for personal flights in the United States. If no bona fide business-oriented security concern exists with respect to travel in the United States, B may not exclude any portion of the value of the availability of the driver or limousine for personal use in the United States. Thus, B must include in income the value of the availability of the vehicle and driver for personal use. In addition, B may not exclude any portion of the value attributable to personal flights by B or B's spouse and dependents on company Y's airplane. Thus, B must include in income the value attributable to the personal use of company Y's airplane. See §1.61-2T for rules relating to the valuation of personal flights on employer-provided airplanes.

Example (4). Assume that company Z retains an independent security consultant to perform a security study with respect to its chief executive officer. Assume further that, based on an objective assessment of the facts and circumstances, the security consultant reasonably recommends that the employee be provided security at his workplace and for ground transportation, but not for air transportation. if company Z follows the recommendations on a consistent basis, an overall security program will be deemed to exist with respect to the workplace and ground transportation security only.

Example (5). Assume the same facts as in example (4) except that company Z only provides the employee security while commuting to and from work, but not for any other ground transportation. Since the recommendations of the independent security study are not applied on a consistent basis, an overall security program will not be deemed to exist.

(n) *product testing*—(1) *In general.* The fair market value of the use of consumer goods, which are manufactured for sale to nonemployees, for product testing and evaluation by an employee outside the employer's workplace is excludable as a working condition fringe if—

(i) Consumer testing and evaluation of the product is an ordinary and necessary business expense of the employer,

(ii) Business reasons necessitate that the testing and evaluation of the product be performed off the employer's business premises by employees (i.e., the testing and evaluation cannot be carried out adequately in the employer's office or in laboratory testing facilities),

(iii) HE product is furnished to the employee for purposes of testing and evaluation,

(iv) The product is made available to the employee for no longer than necessary to test and evaluate its performance and must be returned to the employer at completion of the testing and evaluation period,

(v) The employer imposes limitations of the employee's use of the product which significantly reduce the value of any personal benefit to the employee, and

(vi) The employee must submit detailed reports to the employer on the testing and evaluation.

The length of the testing and evaluation period must be reasonable in relation to the product being tested.

(2) *Employer imposed limitations.* The requirement of paragraph (n)(1)(v) of this section is satisfied if—

(i) The employer places limitations on the employee's ability to select among different models or varieties of the consumer product that is furnished for testing and evaluation purposes,

(ii) The employer's policy provides for the employee, in appropriate cases, to purchase or lease at his or her own expense the same type of product as that being tested (so that personal use by the employee's family will be limited), and

(iii) The employer generally prohibits use of the product by members of the employee's family.

(3) *Discriminating classifications.* If an employer furnishes products under a testing and evaluation program only to officers, owners, or highly compensated employees, this fact may be considered in a determination of whether the products are furnished for testing and evaluation purposes or for compensation purposes, unless the employer can show a business reason for the classification of employees to whom the products are furnished (e.g., that automobiles are furnished for testing and evaluation by an automobile manufacturer to its design engineers and supervisory mechanics).

(4) *Factors that negate the existence of a product testing program.* If an employer fails to tabulate and examine the results of the detailed reports within a reasonable period of time after expiration of the testing period, the program will not be considered a product testing program. Existence of one or more of the following factors may also establish that the program is not a bona fide product testing program:

(i) The program is in essence a leasing program under which employees lease the consumer goods from the employer for a fee;

(ii) The nature of the product and other considerations are insufficient to justify the testing program; or

(iii) The expense of the program outweighs the benefits to be gained from testing and evaluation.

(5) *Failure to meet the requirements of this paragraph (n).* The fair market value of the use of property for product testing and evaluation by an employee outside the employee's workplace, under a product testing program that does not meet all of the requirements of this paragraph (n), is not excludable as a working condition fringe.

(6) *Example.* Assume that an employer that manufactures automobiles establishes a product testing program under which 50 of its 5,000 employees test and evaluate the automobiles for 30 days. Assume further that the 50 employees represent a fair cross section of all of the employees of the employer, such employees submit detailed reports to the employer on the testing and evaluation, the employer tabulates and examines the test results within a reasonable time, and the use of the automobiles is restricted to the employees. If the rules of paragraph (n)(2) of this section are also met, the employees may exclude the value of the use of the automobile during the testing and evaluation period.

(o) *Qualified automobile demonstration use*—(1) *In general.* The value of qualified automobile demonstration use is excludable from gross income as a working condition fringe. The term "qualified automobile demonstration use" means any use of a demonstration automobile by a full-time automobile salesman in the sales area in which the automobile dealer's sales office is located if—

(i) Such use is provided primarily to facilitate the salesman's performance of services for the employer, and

(ii) There are substantial restrictions on the personal use of the automobile by the salesman.

(2) *Full-time automobile salesman*—(i) *Definition.* The term "full-time automobile salesman" means any individual who—

(A) Is employed by an automobile dealer,

(B) Customarily spends substantially all of a normal business day on the sales floor selling automobiles to customers of the automobile dealership,

(C) Customarily works a number of hours considered full-time in the industry (but at a rate not less than 1,000 hours per year), and

(D) Derives at least 85 percent of his or her gross income from the automobile dealership directly as a result of such automobile sales activities.

An individual, such as the general manager of an automobile dealership, who receives a sales commission on the sale of an automobile is not a full-time automobile salesman unless the requirements of this paragraph (o)(2)(i) are met. The exclusion provided in this paragraph (o) is available to an individual who meets the definition of this paragraph (o)(2)(i) regardless of whether the individual performs services in addition to those described in this paragraph (o)(2)(i). For example, an individual who is an owner of the automobile dealership but who otherwise meets the requirements of this paragraph (o)(2)(i) may exclude from gross income the value of qualified automobile demonstration use.

(ii) *Use by an individual other than a full-time automobile salesman.* Personal use of a demonstration automobile by an individual other than a full-time automobile salesman is not treated as a working condition fringe. Therefore, any personal use, including commuting use, of a demonstration automobile by a part-time salesman, automobile mechanic, manager, or other individual is not "qualified automobile demonstration use" and thus not excludable from gross income.

(3) *Demonstration Automobile.* The exclusion provided in this paragraph (o) applies only to qualified use of a demonstration automobile. A demonstration automobile is an automobile that is—

(i) currently in the inventory of the automobile dealership, and

(ii) Available for test drives by customers during the normal business hours of the employee.

(4) *Substantial restrictions on personal use.* Substantial restrictions on the personal use of demonstration automobiles exist when all of the following conditions are satisfied:

(i) Use by individuals other than the full-time automobile salesmen (e.g., the salesman's family) is prohibited,

(ii) Use for personal vacation trips is prohibited,

(iii) The storage of personal possessions in the automobile is prohibited, and

(iv) The total use by mileage of the automobile by the salesman outside the salesman's normal working hours is limited.

(5) *Sales area*—(i) *In general.* Qualified automobile demonstration use must be use in the sales area in which the automobile dealer's sales office is located. The sales area is the geographic area surrounding the automobile dealer's sales office from which the office regularly derives customers.

(ii) *Sales area safe harbor.* With respect to a particular full-time salesman, the automobile dealer's sales area may be treated as the larger of the area within a 75 mile radius of the dealer's sales office, or the one-way commuting distance (in miles) of the particular salesman.

(p) *Parking*—(1) *In general.* The value of parking provided to an employee on or near the business premises of the employer is excludable from gross income as a working condition fringe. The working condition fringe exclusion applies whether the employer owns or rents the parking facility or parking space.

(2) *Reimbursement of parking expenses.* Any reimbursement to the employee of the ordinary and necessary expenses of renting a parking space on or near the business premises of the employer is excludable as a working condition fringe. The preceding sentence does not apply, however, to cash payments that are not actually used for renting a parking space. Thus, that part of a general transportation allowance that is not used for parking is not excludable as a working condition fringe under this paragraph (p).

(3) *parking on residential property.* With respect to an employee, this paragraph (p) does not apply to any parking facility or space located on property owned or leased for residential purposes by the employee.

(q) *Nonapplicability of nondiscrimination rules.* Except to the extent provided in paragraph (n)(3) of this section, the nondiscrimination rules of section 132 (h)(1) and §1.132-8T do not apply in determining the amount, if any, of a working condition fringe.

Par. 8. The following section is added at the appropriate place:

§1.132-6T De minimis fringe (Temporary).

(a) *In general.* Gross income does not include the value of a de minimis fringe provided to an employee. The term "de minimis fringe" means any property or service the value of which is (after taking into account the frequency with which similar fringes are provided by the employer to the employer's employees) so small as to make accounting for it unreasonable or administratively impracticable.

(b) *Frequency.* Generally, the frequency with which similar fringes are provided by the employer to the employer's employees is determined by reference to the frequency with which the employer provides the fringe to each individual employee. For example, if an employer provides a free meal to one employee on a daily basis, but not to any other employee, the value of the meals is not de minimis with respect to that one employee even though with respect to the employer's entire workforce the meals are provided "infrequently." However, where it would be administratively difficult to determine frequency with respect to individual employees, the frequency with which similar fringes are provided by the employer to the employer's employees is determined by reference to the frequency with which the employer provides the fringes to the employees and not the frequency with which individual employees receive them. In these cases, if an employer occasionally provides a fringe benefit of de minimis value to the employer's employees, the de minimis fringe exclusion may apply even through a particular employee receives the benefit frequently. For example, if an employer exercises sufficient control and imposes significant restrictions on the personal use of a company copying machine so that at least 85 percent of the use of the machine is for business purposes, any personal use of the copying machine by particular employees is considered to be a de minimis fringe.

(c) *Administrability.* Unless excluded by a statutory provision other than section 132(a)(4), the value of any fringe benefit that would not be unreasonable or administratively impracticable to account for must be included in the employee's gross income. Thus, except as otherwise provided in this section, the provision of any cash fringe benefit (or any fringe benefit provided to an employee through the use of a charge or credit card) is not excludable as a de minimis fringe. For example, the provision of cash to an employee for personal entertainment is not excludable as a de minimis fringe.

(d) *Special rules*—(1) *Transit passes.* A transit pass provided to an employee at a discount not exceeding $15 per month may be excluded as a de minimis fringe. The exclusion provided in this paragraph (d) also applies to the provision of $15 in tokens or fare cards that enable an individual to travel on the transit system. The exclusion provided in this paragraph (d) does not apply to any provision of cash or other benefit to defray transit expenses incurred for personal travel.

(2) *Occasional meal money or local transportation fare.* Occasional meal money or local transportation fare provided to an employee because overtime work necessitates an extension of the employee's normal workday is excluded as a de minimis fringe.

(3) *Use of special rules to establish a general rule.* The special rules provided in this paragraph (d) may not be used to establish any general rule. For example, the fact that $180 ($15 per month for 12 months) worth of transit passes can be excluded in a year does not mean that any fringe benefit with a value equal to or less than $180 may be excluded as a de minimis fringe.

(4) *Benefits exceeding value and frequency limitations.* If the benefit provided to an employee is not de minimis because either the value or frequency exceeds a limit provided in this paragraph (d), no amount of the benefit is considered to be de minimis. For example, if an employer provides a $20 monthly transit pass, the entire $20 must be included in income, not just the excess value over $15.

(e) *Nonapplicability of nondiscrimination rules.* Except to the extent provided in §1.132-7T, the nondiscrimination rules of section 132(h)(l) and §1.132-8T do not apply. Thus, for example, a fringe benefit may be a de minimis fringe even if the benefit is provided exclusively to officers of the employer.

(f) *Examples*—(l) *Benefits excludable from income.* Examples of de minimis fringe benefits are occasional typing of personal letters by a company secretary; occasional personal use of an employer's copying machine, provided that the employer exercises sufficient control and imposes significant restrictions on the personal use of the machine so that at least 85 percent of the use of the machine is for business purposes; occasional cocktail parties or picnics for employees and their guests; traditional holiday gifts of property (not cash) with a low fair market value; occasional theatre or sporting event tickets; and coffee and doughnuts.

(2) *Benefits not excludable as de minimis fringes.* Examples of fringe benefits that are not excludable from income as de minimis fringes are: season tickets to sporting or theatrical events; the commuting use of an employer-provided automobile or other vehicle more than once a month; membership in a private country club or athletic facility, regardless of the frequency with which the employee uses the facility; and use of employer-owned or leased facilities (such as an apartment, hunting lodge, boat, etc.) for a weekend. Some amount of the value of these fringe benefits may be excluded under other statutory provisions, such as the exclusion for working condition fringes. See §1.132-5T.

Par. 9. The following section is added at the appropriate place:

§1.132-7T Treatment of employer-operated eating facilities (Temporary).

(a) *In general*—(1) *General rule.* The value of meals provided to employees at an employer-operated eating facility for employees is excludable from gross income as a de minimis fringe only if—

(i) On an annual basis, the revenue from the facility equals or exceeds the direct operating costs of the facility, and

(ii) With respect to any officer, owner or highly compensated employee, access to the facility is available on substantially the same terms to each member of a group of employees that is defined under a reasonable classification set up by the employer that does not discriminate in favor of officers, owners, and highly compensated employees. See §1.132-8T.

(2) *Employer-operated eating facility for employees.* An employer-operated eating facility for employees is a facility that meets all of the following conditions—

(i) The facility is owned or leased by the employer,

(ii) The facility is operated by the employer,

(iii) The facility is located on or near the business premises of the employer,

(iv) Substantially all of the use of the facility is by employees of the employer operating the facility, and

(v) The meals furnished at the facility are provided during, or immediately before or after, the employee's workday.

For purposes of this section, the term "meals" means food, beverages, and related services provided at the facility. If an employer can determine the number of employees who receive meals that are excludable from income under section 119, the employer may, in determining whether the requirement of paragraph (a)(1)(i) of this section is satisfied, disregard all costs and revenues attributable to such meals provided to such employees. For purposes of this section, each dining room or cafeteria in which meals are served is treated as a separate eating facility, regardless of whether each such dining room or cafeteria has its own kitchen or other food-preparation area.

(3) *Operation by the employer.* If an employer contracts with another to operate an eating facility for its employees, the facility is considered to be operated by the employer for purposes of this section. If an eating facility is operated by more than one employer, it is considered to be operated by each employer.

(b) *Direct operating costs.* The direct operating costs test must be applied separately for each dining room or cafeteria. For purposes of this section, the direct operating costs of an eating facility are (1) the cost of food and beverages and (2) the cost of labor for personnel whose services relating to the facility are performed primarily on the premises of the eating facility. Direct operating costs do not include the cost of labor for personnel whose services relating to the facility are not performed primarily on the premises of the eating facility. Thus, for example, the labor cost for cooks, waiters, and waitresses is included in direct operating costs, but the labor cost for a manager of an eating facility whose services relating to the facility are not primarily performed on the premises of the eating facility is not included in direct operating costs. If an employee performs services both on and off the premises of the eating facility, only the applicable percentage of the total labor cost of the employee that bears the same proportion as time spent on the premises bears to total time is included in direct operating costs. For example, assume that 60 percent of the services of the cooks in the above example are not related to the eating facility. Only 40 percent of the total labor cost of the cooks is includible in direct operating costs. For purposes of this section, labor costs include all compensation required to be reported on a Form W-2 for income tax purposes and related employment taxes paid by the employer.

(c) *Valuation of non-excluded meals provided at an employer-operated eating facility for employees.* If the exclusion for meals provided at an employer-operated eating facility for employees is not available, the recipient of meals provided at such facility must include in income the amount by which the fair market value of the meals provided exceeds the sum of (1) the amount, if any, paid for the meals, and (2) the amount, if any, specifically excluded by another section of the Code. For special valuation rules relating to such meals see §1.61-2T(j).

Par. 10. The following section is added at the appropriate place:

§1.132-8T Nondiscrimination rules (Temporary).

(a) *Application of nondiscrimination rules*—(1) *General rule*. To qualify under section 132 for the exclusions for no-additional cost services, qualified employee discounts, or meals provided at employer-operated eating facilities for employees, the fringe benefit must be available on substantially the same terms to each member of a group of employees which is defined under a reasonable classification set up by the employer that does not discriminate in favor of officers, owners, or highly compensated employees (the "prohibited group employees").

(2) *Consequences of discrimination*. If the availability of or the provision of the fringe benefit does not satisfy the nondiscrimination rules provided in this section, the exclusion applies only to those employees (if any) who receive the benefit and who are not prohibited group employees. For example, if an employer offers a 20 percent discount (which otherwise satisfies the requirements for a qualified employee discount) to all nonprohibited group employees and a 35 percent discount to all prohibited group employees, the entire value of the 35 percent discount (not just the excess over 20 percent) is includible in the gross income and wages of the prohibited group employees who make purchases at a discount.

(3) *Scope of the nondiscrimination rules provided in this section*. The nondiscrimination rules provided in this section apply only to fringe benefits provided pursuant to section 132(a)(1), (a)(2), and (e)(2). These rules have no application to any other employee benefit that may be subject to nondiscrimination requirements under any other section of the Code.

(b) *Coverage requirement*—(1) *Section 132(a)(1) and(2)*. For purposes of the exclusions for no-additional-cost services and qualified employee discounts, the nondiscrimination rules of this section are applied by aggregating the employees of all related employers (as defined in §1.132-1T(c)), but without aggregating employees in different lines of business (as defined in §1.132-4T). Employees in different lines of business will be aggregated, however, if the line of business limitation has been relaxed pursuant to either section 1.132-4T(b) or (c). Except as provided in paragraph (e) of this section, the nondiscrimination rules of this section are generally applied separately to each fringe benefit program of an employer.

(2) *Section 132(e)(2)*. For purposes of the exclusion for meals provided at employer-operated eating facilities for employees, the nondiscrimination rules of this section are applied by aggregating the employees of all related employers, without regard to different lines of business, who regularly work at or near the premises on which the eating facility is located. The nondiscrimination rules of this section are applied separately to each eating facility. Each dining room or cafeteria in which meals are served is treated as a separate eating facility, regardless of whether each such dining room or cafeteria has its own kitchen or other food-preparation area.

(3) *Classes of employees who may be excluded*. Except as otherwise provided in this section, for purposes of applying the nondiscrimination rules of this section to a particular fringe benefit program, there may be excluded from consideration the following classes of employees provided that, with respect to each class (other than the class described in paragraph (b)(3)(iii) of this section), all employees in the class are excluded from participating in the particular fringe benefit program—

(i) all part-time or seasonal employees who are (or who are reasonably expected to be) credited with less than 1,000 hours (or such lesser number required for the program) of service during a calendar year;

(ii) all employees who are included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and one or more employers, if there is evidence that the particular fringe benefit program was the subject of good faith bargaining between such employee representatives and such employer or employers (and if, after march 31, 1984, the additional condition of section 7701(a)(46) is satisfied);

(iii) all employees who are nonresident aliens and who receive no earned income (within the meaning of section 911(d)(2)) from the employer which constitutes income from services within the United States (within the meaning of section 861(a)(3));

(iv) all employees who have not completed at least one year (or such lesser period required for the program) of service with the employer;

(v) all employees who have separated from the service of the employer in a year prior to the current year (regardless of the reason for the separation);

(vi) all employees who have separated from the service of the employer in a year prior to the current year except for retired and/or disabled employees (either with or without a time limit based on a set number of years since separation from the service of the employer); and

(vii) all employees of a leased section of a department store.

(c) *Classification requirement*—(1) *General rule*. The determination of whether a particular classification established by an employer discriminates in favor of the prohibited group will depend on the facts and circumstances involved, based on principles similar to those applied in the qualified plan area (see section 410(b)(1)(B) and the regulations thereunder). In general, except as otherwise provided in this section, a classification that would be determined to be nondiscriminatory pursuant to the application of the nondiscrimination standards that are applied in the qualified plan area shall be deemed to be nondiscriminatory for purposes of section 132.

(2) *Classifications that are per se discriminatory*. A classification that, on its face, makes fringe benefits available only to prohibited group employees is per se discriminatory, and no exclusion from gross income is available to any prohibited group employee under section 132. In addition, a classification that is based on either an amount or rate of compensation is per se discriminatory if it favors those with the higher amount or rate of compensation. On the other hand, a classification that is based on factors such as seniority, full-time vs. part-time employment, or job description is not per se discriminatory but may be discriminatory as applied to the workforce of a particular employer.

(3) *Former employees*. When determining whether a classification is discriminatory, former employees shall not be considered together with other

employees of the employer. Therefore, a classification is not discriminatory if the employer does not make the fringe benefits available to any former employee. Whether a classification of former employees discriminates in favor of prohibited group employees will depend on the facts and circumstances. The rules of this section shall apply separately to the former employee classification.

(4) *Employer-operated eating facilities for employees*—(i) *General rule*. If access to an employer-operated eating facility for employees is available to a classification of employees that discriminates in favor of highly compensated employees, the classification will not be treated as discriminating in favor of the prohibited group employees unless the facility is used, more than a de minimis amount, by any executive group employee.

(ii) *Executive group employees*. For purposes of this paragraph (c)(4), the term "executive group employees" has the same meaning as the term "prohibited group employees" (as defined in paragraph (g) of this section), except that for purposes of identifying highly compensated employees—

(A) The exception provided in paragraph (g)(1)(i)(A) of this section does not apply, and

(B) The phrase "highest-paid one percent of all employees of an employer" is substituted for the phrase "highest-paid ten percent of all employees of an employer" in paragraph (g)(1)(ii)(A) of this section.

(d) *Substantially-the-same-terms requirement*—(1) *General rule*. Fringe benefits available to a particular classification of employees must be available to each employee in the classification on substantially the same terms. The determination of whether this requirement is met shall depend on the facts and circumstances involved. For example, if a department store provides a 20 percent qualified employee discount to its employees on all merchandise, the substantially-the-same-terms requirement will be satisfied. Similarly, if the discount provided to all employees is 30 percent on certain merchandise (such as apparel), and 20 percent on all other merchandise, the substantially-the-same-terms requirement will be satisfied. However, if the discount provided is 20 percent on all merchandise for hourly employees and 30 percent on all merchandise for salaried employees, the substantially-the-same-terms requirement will not be satisfied. In addition, if the percentage discount varies depending on either an employee's amount or rate of compensation, or volume of purchases, the substantially-the-same-terms requirement will not be satisfied. In order to determine whether such a discount program satisfies the nondiscrimination requirements of section 132, each group of employees that does receive fringe benefits on substantially the same terms must be treated as a separate classification. However, subject to the rules of paragraph (e)(2) of this section, an employer may divide a fringe benefit program into two programs for purposes of aggregating groups of employees. See Example (1) of paragraph (d)(3) of this section.

(2) *Terms relating to priority*. Certain fringe benefits made available to employees are available only in limited quantities that may be insufficient to meet employee demand. This may occur either because of employer policy (such as where an employer determines that only a certain number of units of a specific product will be made available to employees each year) or because of the nature of the fringe benefit (such as where an employer provides a no-additional-cost transportation service that is limited to the number of seats available just before departure). Under these circumstances, an employer may find it necessary to establish some method of allocating the limited fringe benefits among the employees eligible to receive the fringe benefits. An allocation among employees on a "first-come, first-served" basis will not violate the substantially-the-same-terms requirement provided that such an allocation is not discriminatory in practice. In addition, an allocation among employees on a lottery basis will not violate the substantially-the-same-terms requirement provided that such an allocation is nondiscriminatory in practice. For example, assume that an employer has a limited number of a particular benefits to offer to its employees. Assume further that the employees interested in receiving the benefit submit their names to the employer who then selects a number of names, at random, equal to the number of fringe benefits available. This lottery system would not violate the substantially-the-same-terms requirement. An allocation among employees on other than a "first-come, first-served", lottery, or similar basis will violate the substantially-the-same-terms requirement. Therefore, an allocation based on seniority, full-time vs. part-time employment, or job description will violate the substantially-the-same-terms requirement. In order to determine whether such a fringe benefit program satisfies the nondiscrimination requirements of section 132, each group of employees that does receive fringe benefits on substantially the same terms must be treated as a separate classification. For purposes of this rule, the last two sentences of paragraph (d)(1) of this section apply.

(3) *Examples*. The following examples illustrate the provisions of this paragraph (d):

Example 1. Assume that with respect to a benefit available in limited quantities an employer provides priority to employees based on seniority. Assume further that all non-prohibited group employees have ten years of seniority and all prohibited group employees have nine years seniority. If each of these groups were tested separately, the benefits offered to prohibited group employees would be discriminatory under this section. In this case, the employer could divide the fringe benefit program provided to non-prohibited group employees into two parts: one relating to nine years of seniority and one relating to an additional year of seniority. As restructured in this manner, all employees receive the benefit relating to nine years seniority and only non-prohibited group employees receive the benefit relating to an additional year of seniority. Both groups (all employees and all non-prohibited group employees) are nondiscriminatory groups.

Example 2. Assume that prices charged to prohibited group employees at an employer-operated eating facility for employees are lower than prices charged to non-prohibited group employees. The substantially-the-same requirement is not satisfied.

(4) *Disproportionate use of eating facility*. If access to an employer-operated eating facility for employees is technically available on substantially-the-same-terms to (i) all employees who regularly work at or near the premises on which the eating facility is located (the employee group), or (ii) a nondiscriminatory classification of the employee group, but in practice a highly disproportionate number of the prohibited group employees in the employee group, compared to the non-prohibited group employees in the employee group, use the facility, the substantially-the-same-terms require-

ment will not be satisfied unless no member of the executive group eats there more than a de minimis amount.

(e) *Aggregation of separate fringe benefit programs*—(1) *General rule*. If an employer maintains more than one fringe benefit program, i.e., two or more classifications of employees providing either identical or different fringe benefits, the nondiscrimination requirements of section 132 will generally be applied separately to each such program. Thus, a determination that one fringe benefit program discriminates in favor of prohibited group employees generally will not cause other fringe benefit programs covering the same prohibited group employees to be treated as discriminatory.

(2) *Exception*—(i) *Related fringe benefit programs*. If one of a group of fringe benefit programs discriminates in favor of prohibited group employees, no related fringe benefit provided to such prohibited group employees under any other fringe benefit program may be excluded from the gross income of such prohibited group employees. For example, assume a department store provides a 20 percent merchandise discount to all employees under one fringe benefit program. Assume further that under a second fringe benefit program, the department store provides an additional 15 percent merchandise discount to a group of employees defined under a classification which discriminates in favor of the prohibited group. Because the second fringe benefit program is discriminatory, the 15 percent merchandise discount provided to the prohibited group employees is not a qualified employee discount. In addition, because the 20 percent merchandise discount provided under the first fringe benefit program is related to the fringe benefit provided under the second fringe benefit program, the 20 percent merchandise discount provided the prohibited group employees is not a qualified employee discount. Thus, the entire 35 percent merchandise discount provided to the prohibited group employees is includible in such employees' gross incomes.

(ii) *Employer-operated eating facilities for employees*. For purposes of paragraph (e)(2)(i) of this section, meals at different employer-operated eating facilities for employees are not related fringe benefits, so that a prohibited group employee may exclude the value of a meal at a nondiscriminatory facility even though any meals provided to him or her at the discriminatory facility cannot be excluded.

(f) *Cash bonuses or rebates*. A cash bonus or rebate provided to an employee by an employer that is determined pursuant to the value of employer-provided property or services purchased by the employee, is treated as an equivalent employee discount. For example, assume a department store provides a 20 percent merchandise discount to all employees under a fringe benefit program. In addition, assume that the department store provides cash bonuses to a group of employees defined under a classification which discriminates in favor of the prohibited group. Assume further that such cash bonuses equal 15 percent of the value of merchandise purchased by each employee. This arrangement is substantively identical to the example described in paragraph (e)(2) of this section. Thus, both the 20 percent merchandise discount and the 15 percent cash bonus provided to the prohibited group employees are includible in such employees' gross incomes.

(g) *Prohibited group employees*—(1) *Highly compensated*—(i) *General rule*. Except as otherwise provided in this paragraph (g)(1)(i), any employee of an employer who has (or is reasonably expected to have) compensation during a calendar year equal to or greater than the employer's base compensation amount is highly compensated. There are two exceptions to this rule:

(A) any employee who has (or is reasonably expected to have) compensation during a calendar year equal to or greater than $50,000 is highly compensated, regardless of whether such compensation is in excess of the base compensation amount, and

(B) any employee who is reasonably expected to have compensation during a calendar year equal to or less than $20,000 is not highly compensated, unless no employee of the employer is reasonably expected to have compensation equal to or greater than $35,000.

The determination of whether an employee is a highly compensated employee will be determined based on the entire employee workforce of all employers aggregated pursuant to the rules of section 414(b), (c), or (m) without regard to the regular workplace of the employees.

(ii) *Base compensation amount*—(A) *General rule*. The term "base compensation amount" is defined as that amount corresponding to the lowest annual compensation amount received by the highest-paid ten percent of all employees of an employer (the number of employees in the top ten percent will be increased to the next highest integer if necessary), determined on the basis of the preceding calendar year. For purposes of this paragraph (g)(1)(ii), the term "employer" includes all entities that would be aggregated pursuant to the rules of section 414(b), (c), or (m).

(B) *Employees that are excluded*. For purposes of determining the base compensation amount with respect to a fringe benefit program, employees described in paragraph (b)(3) of this section are excluded whether or not they are covered under the fringe benefit program, except that *(1)* employees described in paragraph (b)(3)(ii) of this section are taken into account with respect to the program even if they are excluded under paragraph (b)(3), and *(2)* employees described in paragraph (b)(3)(i) and (iv) of this section are taken into account with respect to the program unless they are excluded under paragraph (b)(3).

(C) *Exception to preceding calendar year rule*. In the case of an employer's first year of operation, or where employer's business has changed significantly from the prior calendar year (e.g., due to an acquisition or merger), the employer must make a good faith attempt to either determine or adjust the base compensation amount for the current year based on reasonable estimates of current year compensation.

(iii) *Compensation*. The term "compensation" is defined as the amount reportable on a Form W-2 as income. Amounts that would be excluded from income but for section 132(h)(1) are not included in compensation for purposes of this paragraph (g)(1). Compensation includes amounts received from all entities which would be treated as a single employer under section 414(b), (c), or (m) and is not restricted to amounts received with respect to any one line of business.

(iv) *Employee*. Generally, for purposes of determining whether an employee is highly compensated under this paragraph (g)(1), the term "employee" does not include any individual who does not perform services for the employer as an employee during the calendar year. For example, if an employer has active employees, retired or disabled employees, and widows or widowers who are "employees" under section 132(f)(1)(B), the general rule (described in paragraph (g)(1)(i) of this section) applies only to the active employees.

(2) *Owner*.—(i) *General rule*. For purposes of this section, the term "owner" means any employee who owns a one percent or greater interest in either the employer or in any entity that would be aggregated with the employer pursuant to the rules of section 414(b), (c), or (m). In addition, such an employee shall be treated as an owner of all entities that would be aggregated with the employer pursuant to the rules of section 414(b), (c), or (m).

(ii) *Determining ownership*. Ownership in a corporation shall be determined pursuant to the rules of section 318(a). For purposes of determining ownership in an entity other than a corporation, the rules of section 318(a) shall apply in a manner similar to the way in which they apply for purposes of determining ownership in a corporation. For non-corporate interests, capital or profits interest must be substituted for stock.

(3) *Officer*.—(i) *Non-government*. For purposes of this section, an officer of a non-government employer is any employee who is appointed, confirmed, or elected by the Board of shareholders of the employer. An employee who is an officer of an employer shall be treated as an officer of all entities treated as a single employer pursuant to section 414(b), (c), or (m). The number of officers is not to exceed one-percent of the total number of employees of all entities treated as a single employer pursuant to section 414(b), (c), or (m) (increased to the next highest integer, if necessary). If the number of officers exceeds one-percent of all employees, then the limitation is to be applied to employees in descending order of compensation (as defined in paragraph (g)(1)(iii) of this section). Thus, if an employer with 1,000 employees has 11 board-appointed officers, the employee with the least compensation of those officers would not be an officer under this paragraph (g)(3)(i). In determining the total number of employees with respect to a fringe benefit program, employees described in paragraph (b)(3) of this section are excluded whether or not they are covered under the fringe benefit program, except that (A) employees described in paragraph (b)(3)(ii) of this section are taken into account with respect to the program even if they are excluded under paragraph (b)(3), and (B) employees described in paragraph (b)(3)(i) and (iv) of this section are taken into account with respect to the program unless they are excluded under paragraph (b)(3).

(ii) *Government*. For purposes of this section, an officer of a government employer is any—

(A) Elected official,

(B) Federal employee appointed by the President and confirmed by the Senate. However, in the case of any commissioned officer of the United States Armed Forces, an officer is any employee with the rank of brigadier general or rear admiral (lower half) or above, and

(C) State or local executive officer comparable to individuals described in paragraphs (g)(3)(ii)(A) and (B) of this section.

For purposes of this paragraph (g)(3)(ii), the term "government" includes any Federal, state, or local governmental unit, and any agency or instrumentality thereof.

(4) *Former employees*. [Reserved]

Par. 11. Paragraph (b) of §1.162-25T is amended by removing the words "(as defined in §1.61-2T Q/A-20)" and adding in their place the words "(as defined in §1.61-2T(e)(2))".

Par. 12. Section 1.274-5T is amended as follows:

1. Paragraph (e)(1)(ii) is amended by removing the words "(as defined in §1.61-2T Q/A-20)" and adding in their place the words "(as defined in §1.61-2T(e)(2))".

2. The first sentence of paragraph (l) is revised to read as follows: "For purposes of section 274(d) and this section, the terms "automobile" and "vehicle" have the same meanings as prescribed in §1.61-2T(d)(1)(ii) and §1.61-2T(e)(2), respectively.".

3. The third sentence of paragraph (m) is amended by removing the words "except as provided in §1.132-1T Q/A-4b" and adding in their place the words "except as provided in §1.132-5T(h)".

Par. 13. Section 1.274-6T is amended as follows:

1. Paragraph (a)(3)(i)(E) is revised to read as follows: "The employee required to use the vehicle for commuting is not a control employee (as defined in §1.61-2T(f)(5) and (6)) required to use an automobile (as defined in §1.61-2T(d)(1)(ii)), and".

2. Paragraph (a)(3)(i)(F) is amended by removing the citation "§1.61-2T Q/A-21" and adding in its place the citation "§1.61-2T(f)(3)".

3. Paragraph (a)(3)(ii) is amended by removing from the introductory text the citation "§1.61-2T Q/A-21" and adding in its place the citation "§1.61-2T(f)(3)".

4. Paragraph (a)(3)(ii)(E) is revised to read as follows: "The employee required to use the vehicle for commuting is not a control employee (as defined in §1.61-2T(f)(5) and (6)) required to use an automobile (as defined in §1.61-2T(d)(10)(ii)), and".

5. Paragraph (a)(3)(ii)(F) is amended by removing the citation "§1.61-2T Q/A-21" and adding in its place the citation "§1.61-2T(f)(3)".

6. Paragraph (b)(1) is amended by removing from the last sentence the citation "§1.132-1T Q/A-4a(f)" and adding in its place the citation "§1.132-5T(g)".

7. Paragraph (b)(3) is amended by removing from the last sentence the citation "§1.132-1T Q/A-4a(f)" and adding in its place the citation "§1.132-5T(g)(3)".

8. Paragraph (e)(3) is amended by removing the citation "§1.61-2T Q/A-11" and adding in its place the citation "§1.61-2T(d)(1)(ii)".

9. Paragraph (e)(4) is amended by removing the citation "§1.61-2T Q/A-20" and adding in its place the citation "§1.61-2T (e)(2)".

Par. 14. The authority for Part 602 continues to read as follows:

26 U.S.C. 7805.

Par. 15. Section 602.101(cc) is amended by inserting in the appropriate place in the table "1.61-2T . . . 1545-0771; 1.132-2T . . . 1545-0771; and 1.132-5T . . . 1545-0771".

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved: December 11, 1985.

RONALD A. PEARLMAN,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on December 18, 1985, 11:08 a.m., and published in the issue of the Federal Register for December 23, 1985, 50 F.R. 52281).

Section 132.—Certain Fringe Benefits

26 CFR 1.132-1T: Exclusion from gross income of certain fringe benefits (Temporary).

Whether certain fringe benefits are included in gross income. See T.D. 8063, page 4.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Taxation of Fringe Benefits and Exclusions From Gross Income for Certain Fringe Benefits

LR-216-84

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary regulations relating to the taxation of fringe benefits. The text of those temporary regulations serves as the comment document for this proposed rulemaking.

DATES: Written comments and requests for a public hearing must be mailed or delivered by February 21, 1986. Except to the extent otherwise provided, the regulations are proposed to be effective as of January 1, 1985.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-216-84 and LR-37-85), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Annette J. Guarisco of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service, (202-566-3918, not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

The temporary regulations * * * [on page 4, this Bulletin] amend Parts 1 and 602 of Title 26 of the Code of Federal Regulations. The temporary regulations are designated by a "T" following their section citation. The final regulations, which this document proposes to base on those temporary regulations, would amend Parts 1 and 602 of Title 26 of the Code of Federal Regulations.

The regulations provide guidance on the tax treatment of taxable and nontaxable fringe benefits, including the valuation of taxable fringe benefits for purposes of income and employment tax reporting and withholding. The regulations provide special rules for valuing employer-provided automobiles, use of employer-provided aircraft, free or discounted flights on commercial airlines, and meals provided at employer-operated eating facilities. The regulations also provide rules relating to the exclusions from gross income for certain fringe benefits and applicable nondiscrimination rules.

Section 61 of the Internal Revenue Code of 154 (the Code) was amended, and section 132 was added to the Code, by section 531 of the Tax Reform Act of 1984 (98 Stat. 877) [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 385]. Temporary and proposed regulations were published in the FEDERAL REGISTER on January 7, 1985 (50 FR 747, 836) [T.D. 8004, LR-216-84, 1985-1 C.B. 23, 655]. These regulations were later amended in the FEDERAL REGISTER on February 20, 1985 (50 FR 7038, 7073) [T.D. 8009, LR-216-84, 1985-1 C.B. 82, 657].

Subsequently, Public Law 99-44 (Repeal of Contemporaneous Recordkeeping Requirements) [1985-34 I.R.B. 22] affected some of the proposed and temporary regulations published in February. To implement the provisions of Public Law 99-44, the Service withdrew the affected proposed and temporary regulations published in February (50 FR 46,004, 46,086) [T.D. 8060, LR-145-84 and LR-216-84, 1985-49 I.R.B. 5, 20] and published new proposed and temporary regulations on November 6, 1985 (50 FR 46,006, 46,087) [T.D. 8061, LR-216-84, 1985-46 I.R.B. 7, 48]. This document replaces portions of the previously issued proposed regulations.

Many comments were received from the public concerning the provisions in the proposed and temporary regulations published earlier this year. In addition, on April 16, 17, and 18, 1985, the Internal Revenue Service (Service) held public hearings concerning the temporary and proposed regulations. In response to the comments and the statements made at the public hearings, the regulations have been amended. Due to the extent of the amendments, the Service is issuing the regulations in temporary rather than final form. This document contains the cross-reference notice of proposed rulemaking to provide the public with an opportunity to comment on the revised provisions of the regulations before they become final. The Service expects to hold public hearings on the proposed regulations early next year.

For the text of the temporary regulations, see FR Doc. [T.D. 8063] published * * * [on page 4, this Bulletin]. The preamble to the temporary regulations contains a summary of the provisions of these regulations.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

Although this document is a notice of proposed rulemaking that solicits public comments, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, no Regulatory Flexibility Analysis is required by 5 U.S.C. chapter 6.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. When the public hearing is scheduled, notice of the time and place will be published in the FEDERAL REGISTER.

Comments are particularly invited concerning the administrability and appropriateness of the special rules contained in the temporary regulations relating to valuing the availability of employer-provided automobiles, the personal use of employer-provided vehicles for commuting, flights on employer-provided aircraft, free or discounted flights on commercial airlines, and meals provided at employer-operated eating facilities for employees.

With regard to the automobile special valuation rule, comments are requested concerning the use of a four-year, level-payment lease term as the basis of the Annual Lease Value Table.

(For a further discussion of this rule, see the preamble to the temporary regulations * * * [on page 4, this Bulletin].)

The proposed regulations provide guidance on valuing an automobile for purposes of determining the Annual Lease Value. In particular, the proposed regulations provide that for this purpose the value of an automobile does not include the value of specialized equipment which is not susceptible to personal use or of a telephone. An example of such equipment would be permanent shelving custom designed to hold special business tools. This provision does not mean that any property susceptible to personal use which is in an automobile must be valued as part of the automobile. The regulations are not intended to address the treatment of property which, although susceptible to personal use, is not commonly included in an automobile but when included in an automobile is commonly used for business while the automobile is being used for personal purposes. An example of such property is a car telephone, which may be used for business purposes while the car is being used for personal purposes (e.g., a business call while an employee is commuting to work). Comments are requested as to what other property falls into this category and as too the appropriate tax treatment for personal use of such property.

The vehicle cents-per-mile rule may be used to value the personal use of employer-provided vehicles regularly used in the employer's business if the value of the vehicle does not exceed $12,800 (for 1985). Comments are requested concerning (1) the need for further definition of the regularly used in business standard, (2) suggestions for such a definition, and (3) the appropriateness of and suggestions for refining the alternative mileage rule for use of the vehicle cents-per-mile rule.

Comments are requested concerning the definitions of Federal officers and executive officers at the state and local levels, for purposes of determining who is a control employee and thus ineligible to use the commuting special valuation rule.

Comments are also requested relating to the tax treatment of so-called "bonus" programs (such as "frequent flier" programs) under which a company provides benefits (such as free flights, automobile rentals, and hotel rooms) to their customers on the basis of the amount of business the customer does with the company. The issue of tax treatment arises when, for example, the business that gives rise to the benefits or bonuses is paid for by the customer's employer rather than the customer (i.e., business flights or hotel rooms are paid for by the employer and the company awards the bonus flight or hotel room to the employee). Comments are requested on the need for special rules relating to the valuation of the benefits, the administrability of either withholding on or reporting the value of such benefits, and the appropriate party to charge with the responsibility for reporting. Comments are specifically requested regarding whether the benefits should be regarded as "wages" subject to withholding.

In August 1985, the Service announced rules relating to reporting and withholding on the value of fringe benefits (Announcement 85-113, 1985-31 I.R.B. 31, August 5, 1985). Comments are requested relating to those withholding and reporting rules.

Collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. Comments on those requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on those requirements to OMB also send copies to the Service.

DRAFTING INFORMATION

The principal author of these regulations is Annette J. Guarisco of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * * *

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on December 18, 1985, 11:09 a.m., and published in the issue of the Federal Register for December 23, 1985, 50 F.R. 52333)

Withdrawal of Notice of Proposed Rulemaking

Taxation of Fringe Benefits

LR-216-84

SUMMARY: This document withdraws portions of the notice of proposed rulemaking by cross-reference to temporary regulations published in the FEDERAL REGISTER for January 7, 1985 (50 FR 836) [LR-216-84, 1985-1 C.B. 655], February 20, 1985 (50 FR 7073) [LR-216-84, 1985-1 C.B. 657], and November 6, 1985 (50 FR 46,006) [T.D. 8061, 1985-46 I.R.B. 7], relating to the taxation of fringe benefits. The text of the temporary regulations under sections 61 and 132 served as the comment document for the notice of proposed rulemaking. * * * [T]he Internal Revenue Service is removing portions of those temporary regulations. This document withdraws portions of the notice of proposed rulemaking that relate to the removed portions of the temporary regulations. Changes to the applicable tax law were made by section 531 of the Tax Reform Act of 1984 (98 Stat. 877) [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 385].

DATES: The withdrawal of portions of the notice of proposed rulemaking is effective as of January 1, 1985.

FOR FURTHER INFORMATION CONTACT: Annette J. Guarisco of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service, (202) 566-3918, not a toll-free call.

SUPPLEMENTARY INFORMATION

BACKGROUND

Section 61 was amended and section 132 was added to the Internal Revenue Code of 1954 (Code) by section 531 of the Tax Reform Act of 1984 (98 Stat. 877). Temporary regulations published in the FEDERAL REGISTER for January 7, 1985 (50 FR 747) [T.D. 8004, 1985-1 C.B. 23], amended the Income Tax Regulations (26 CFR Part 1) to reflect the changes in the law relating to the taxation of fringe benefits. These regulations were later amended in the FEDERAL REGISTER for February 20, 1985 (50 FR 7038) [T.D. 8009, 1985-1 C.B. 82], and November 6, 1985 (50 FR 46,006) [T.D. 8061, 1985-46 I.R.B. 7].

Many comments were received on the proposed and temporary regulations published during 1985. In addition, on April 16, 17, and 18, 1985, the Internal Revenue Service held public hearings concerning the provisions of the proposed regulations. In response to the comments and the statements made at the public hearings, the rules provided in the proposed and temporary regulations have been amended. Due to the extent of the amendments, the regulations have been issued in temporary rather than final form. In addition, the temporary regulations * * * [on page 4, this Bulletin] also serve as the comment document for a notice of proposed rulemaking * * * on page 40, this Bulletin]. Because the rules are being reissued as proposed and temporary regulations rather than final regulations, portions of the previously published notice of proposed rulemaking and temporary regulations must be withdrawn. The portion of the temporary and proposed regulations relating to the election to aggregate lines of business for purposes of certain fringe benefit exclusions under section 4977 of the Code is not withdrawn.

DRAFTING INFORMATION

The principal author of this document is Annette J. Guarisco of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing this document on matters of both substance and style.

The proposed amendments to 26 CFR Part 1 under § 1.61-2T and §1.132-1T published in the FEDERAL REGISTER for January 7, 1985, February 20, 1985, and November 6, 1985, are hereby withdrawn.

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on December 18, 1985, 11:10 a.m., and published in the issue of the Federal Register for December 23, 1985, 50 F.R. 52333).

Reporting of Mortgage Interest Payments

Announcement 86-3

This announcement concerns the reporting of mortgage interest payments under section 6050H of the Internal Revenue Code. Section 6050H provides that persons who are engaged in a trade or business and receive at least $600 of interest on a mortgage in a calendar year from an individual must report the amount of interest received to the Internal Revenue Service (Service) and to the person from whom the interest was received. The reporting requirement is effective for interest received after December 31, 1984.

On August 20, 1985, the Service published proposed and temporary regulations relating to mortgage interest reporting (50 FR 33551, 33529). A public hearing concerning these regulations is scheduled for January 7, 1986.

The Service has decided to modify certain provisions of the temporary regulations as they relate to the reporting of mortgage interest received in 1985. In addition, the Service intends to clarify the application of certain other provisions of the temporary regulations. These modifications and clarifications are discussed below. Taxpayers may rely on this announcement until publication of final regulations under section 6050H.

For purposes of this announcement, persons required to report under section 6050H are referred to as "interest recipients," and persons from whom interest is received are referred to as "borrowers."

(1) *Points*

The temporary regulations provide that points are not to be reported as interest received (§1.6050H-1T Q/A-17(c)).

For 1985, however, if an interest recipient cannot, from the records used to prepare its mortgage interest reports, exclude the portion of interest that represents points in order to report interest received in the year, the recipient may report the points as part of interest. An interest recipient who reports an amount as interest that may include points must provide the borrower with the notice described in section (4)(a), in the manner described in section 4(d), of this announcement.

(2) *Other prepaid interest*

The temporary regulations also provide that prepaid interest is not reportable as interest received (§1.6050H-1T Q/A-17(c)). Prepaid interest is interest that a borrower pays in a calendar year which has not properly accrued as of the end of the year. Prepaid interest is not deductible by the borrower in the year of prepayment (see section 461(g) of the Code).

For 1985, if an interest recipient cannot, from the records used to prepare its mortgage interest reports, exclude prepaid interest in order to report interest received in the year, the interest recipient may report prepaid interest as part of interest received. An interest recipient who reports prepaid interest as interest received must provide the borrower with the notice described in section (4)(b), in the manner required by section 4(d), of this announcement.

(3) *Rule of 78's method of accounting*

Interest recipients have asked whether the Rule of 78's method of accounting should be used to determine the amount of reportable interest received from the borrower if the interest recipient calculates interest earned on the mortgage under this method.

The Rule of 78's method is permitted to be used to determine interest earned or paid for federal income tax purposes only in the case of a self-amortizing consumer loan that requires level payments, at regular intervals (at least annually), over a period not in excess of five years (with no balloon payment at the end of the loan term), and only when the loan agreement provides for use of the Rule of 78's method to determine interest earned (see Rev. Proc. 83-40, 1983-1 C.B. 774, and Rev. Rul. 83-84, 1983-1 C.B. 97).

Interest recipients who are permitted by Rev. Proc. 83-40 to use the Rule of 78's method to calculate interest earned with respect to a transaction may report interest earned under the Rule of 78's method on that transaction as interest received from the borrower. The interest recipient must provide the borrower with the notice described in section (4)(c), in the manner reqquired by sectin (4)(d), of this announcement.

(4) *Notice to borrowers*

(a) *Points*

Interest recipients who for 1985 report an amount which may include points as interest received in 1985 must clearly notify the borrower (i) that the amount reported may include points; (ii) that points actually paid in respect of debt incurred in connection with the purchase or improvement of the borrower's principal residence that is secured by the residence are deductible in full in the year of payment only if—

(A) the payment of points is an established business practice in the area in which the debt is incurred, and

(B) the amount of the payment does not exceed the amount generally charged in the area; and

(iii) that, if the borrower deducted points in the year of payment, amortized points reported as received by the interest recipient in 1985 are not deductible by the borrower for 1985.

(b) *Prepaid interest*

Interest recipients who report interest prepaid in 1985 as interest received in 1985 must notify the borrower that prepaid interest is not deductible until the year in which it is properly accrued.

(c) *Rule of 78's method of accounting*

Interest recipients who properly report interest received under the Rule of 78's method must notify the borrower that the Rule of 78's method was used to calculate interest received and that the borrower may not deduct this amount unless the borrower is also properly using the Rule of 78's method to determine interest deductions. Interest recipients should notify borrowers that the Rule of 78's method may only be used in the circumstances described in section 3 above.

(d) *Manner of providing notice*

Notices given to borrowers under these guidelines must accompany the statement required to be furnished to the borrower under the regulations. The interest recipient may provide the notice on the front or reverse side of the statement or on a separate attachment. The notification should not be placed on the Form 1098, "Mortgage Interest Statement," that the interest recipient sends to the Service.

(5) *Interest received by cooperative housing corporations*

The regulations provide that cooperative housing corporations must report, as interest received in a trade or business, the amount of the tenant-stockholder's proportionate share of interest. This requirement will be suspended for calendar year 1985. Thus, cooperative housing corporations may, but are not required to, report under section 6050H with respect to such amounts for 1985.

(6) *Interest received from nonresident aliens*

the regulations do not provide an exception from the reporting requirement for interest received from nonresident alien individuals. This announcement clarifies that interest recipients who receive interest from nonresident alien individuals may, but are not required to, report under section 6050H with respect to such interest for 1985.

The evidence required to determine whether an individual is a nonresident alien depends on whether the interest is paid inside or outside the United States. The place of payment of interest is considered to be where the payor completes the acts necessary to effect payment. However, an amount paid by transfer to an account maintained by the interest recipient in the United States or by mail to a United States address is considered to be paid within the United States.

Interest recipients who receive interest that is paid outside the United States need not report if the documentary evidence standard provided in paragraph (iii) of §35a.9999-4T (Q/A-5) of the Temporary Employment Tax Regulations under the Interest and Dividend Tax Compliance Act of 1983 is satisfied.

Domestic or foreign interest recipients who receive interest that is paid inside the United States must secure a Form W-8 "Certificate of Foreign Status" from an individual in order to be excepted from reporting with respect to that individual.

The treatment of nonresident aliens for future years is still under consideration and comments are invited.

(7) *Interest received on behalf of another*

The regulations provide that interest received on behalf of another must be reported by the first person receiving the interest (§1.6050H-1T (Q/A-11)). Reporting is required regardless of whether the person for whom the interest is received would be required to report.

For calendar year 1985, any person receiving payments on behalf of another who does not know the portion of the payment that represents interest need not report. Thus, for example, a savings and loan institution receiving payments on behalf of a customer under an arrangement that requires the institution to deposit the payments directly into the customer's account need not report with respect to the amounts received in calendar year 1985 if the institution does not know the amount of the payments that represents interest.

19-year ACRS Tables to be Used With Form 4562, Depreciation and Amortization

Announcement 86-5

The attached cost recovery tables have been developed to provide guidance to taxpayers depreciating real property placed in service after May 8, 1985. Pub. L. 99-121, 1985-48 I.R.B. 11, increased the recovery period for real property placed in service after May 8, 1985 to 19 years. These tables and additional tables applicable to 19-year real property will be published in a future Revenue Procedure.

Table 1 provides the rates to be used generally with respect to real property (other than low-income housing) placed in service after May 8, 1985, and is based on the use of the mid-month convention and the 19-year 175-percent declining balance method, later switching to the straight line method to maximize the annual depreciation deduction.

Table 2 provides the rate to be used generally with respect to real property (other than low-income housing) placed in service after May 8, 1985, for which an optional 19-year straight line method is elected. It is also based on the use of the mid-month convention.

In general, in the case of any building placed in service before May 9, 1985, components of such buildings placed in service after May 8, 1985 shall be treated as 19-year real property.

Taxpayers with fiscal years beginning in 1984, who during that year placed in service 19-year real property (real property placed in service after May 8, 1985), should use the 1984 Form 4562 Depreciation and Amortization. They should enter the recovery deduction on Line 2(g) and enter "19 YRS" for the recovery period in Col-

umn D, unless an alternate period is elected.

Fiscal year taxpayers who have filed a 1984 tax return without taking into account the rates applicable to 19-year real property should file an amended return.

For tax years beginning in 1985, taxpayers should enter 19-year real property in the space provided below line 4g on the 1985 Form 4562. The 1985 instructions for Form 4562 should be used with these tables, noting that these tables apply generally to real property placed in service after May 8, 1985.

ACRS Cost Recovery Tables for 19-Year Real Property

1. *19-Year Property (19-Year 175% Declining Balance) (Assuming Mid-Month Convention)*

If the Recovery Year is:	*And the Month in the First Recovery Year the Property is Placed in Service is:*											
	1	*2*	*3*	*4*	*5*	*6*	*7*	*8*	*9*	*10*	*11*	*12*
	The applicable percentage is:											
1	8.8	8.1	7.3	6.5	5.8	5.0	4.2	3.5	2.7	1.9	1.1	.4
2	8.4	8.5	8.5	8.6	8.7	8.8	8.8	8.9	9.0	9.0	9.1	9.2
3	7.6	7.7	7.7	7.8	7.9	7.9	8.0	8.1	8.1	8.2	8.3	8.3
4	6.9	7.0	7.0	7.1	7.1	7.2	7.3	7.3	7.4	7.4	7.5	7.6
5	6.3	6.3	6.4	6.4	6.5	6.5	6.6	6.6	6.7	6.8	6.8	6.9
6	5.7	5.7	5.8	5.9	5.9	5.9	6.0	6.0	6.1	6.1	6.2	6.2
7	5.2	5.2	5.3	5.3	5.3	5.4	5.4	5.5	5.5	5.6	5.6	5.6
8	4.7	4.7	4.8	4.8	4.8	4.9	4.9	5.0	5.0	5.1	5.1	5.1
9	4.2	4.3	4.3	4.4	4.4	4.5	4.5	4.5	4.5	4.6	4.6	4.7
10	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
11	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
12	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
13	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
14	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
15	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
16	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
17	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
18	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
19	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
20	0.2	0.5	0.9	1.2	1.6	1.9	2.3	2.6	3.0	3.3	3.7	4.0

2. *19-Year Real Property For Which An Optional 19-Year Straight Line Method is Elected (Assuming Mid-Month Convention)*

If the Recovery Year is:	*And the Month in the First Recovery Year the Property is Placed in Service is:*											
	1	*2*	*3*	*4*	*5*	*6*	*7*	*8*	*9*	*10*	*11*	*12*
1	5.0	4.6	4.2	3.7	3.3	2.9	2.4	2.0	1.5	1.1	.7	.2
2	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
4	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
5	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
6	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
7	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
8	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
9	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
10	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
11	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
12	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
13	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.2	5.2	5.2	5.2
14	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
15	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
16	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
17	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
18	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
19	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
20	.2	.6	1.0	1.5	1.9	2.3	2.8	3.2	3.7	4.1	4.5	5.0

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Edward L. Lambert	Rancho Mirage, CA	Certified Public Accountant	From November 6, 1985 Until January 8, 1990
Benjamin Ostfield	Minneapolis, MN	Attorney and Certified Public Accountant	Indefinite from November 20, 1985
Kenneth D. Short	Ellicott City, MD	Attorney	Indefinite from November 6, 1985

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1939-1-1	9.50
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1939-2	10.00
1940-1	6.50
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1944-(*)	*9.00*
1945-(*)	10.00
1946-1	*3.00*
1946-2	6.00
1947-1	*2.00*
1947-2	3.75
1948-1	*3.50*
1948-2	8.50
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1949-2	*3.25*
1950-1	7.00
1950-2	*5.50*
1951-1	*13.00*
1951-2	*6.00*
1952-1	*3.00*
1952-2	8.00
1953-1	*4.75*
1953-2	13.00
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1954-2	13.00
1955-1	11.00
1955-2	14.00
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1986 - 4

Internal Revenue bulletin

January 27, 1986
Bulletin No. 1986-4

Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

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INCOME TAX

Rev. Rul. 86-5, page 4.

Residential energy credit. A window covering and its integral edge mounting system is insulation under section 23(c)(3); expenditures for the system and its installation qualify for the residential energy tax credit under section 23(a).

Rev. Rul. 86-6, page 4.

Tax on income of foreign corporations not connected with United States business. A domestic corporation that owns all of the stock of a Netherlands Antilles corporation may withdraw a portion of its paid in capital contribution such that the subsidiary's debt-to-equity ratio is increased from 3-to-1 to 5-to-1 without jeopardizing the subsidiary's separate corporate status.

Rev. Rul. 86-7, page 6.

Regulated futures contracts; qualified board or exchange. The Mercantile Division of the Montreal Exchange is a qualified board or exchange for purposes of section 1256 of the Code.

Rev. Rul. 86-8, page 6.

Regulated futures contracts; nonequity option. An option on the High Technology Index of the Pacific Stock Exchange is a nonequity option for purposes of section 1256 of the Code.

Rev. Rul. 86-9, page 6.

Obsolete rulings. Certain rulings involving section 1032(a) of the Code are declared obsolete with respect to options acquired or lapsing after July 18, 1984, the effective date of section 57(a) of the Tax Reform Act of 1984.

LR-92-73, page 42.

Proposed amendments to the regulations relate to the recapture of investment credit for mass assets.

Announcement 86-4, page 51.

Final regulations under section 170 of the Code relating to charitable contributions of certain securities valued over $5,000 will modify the definition of publicly traded securities in section 1.170A-13T(c)(7)(iv) of the temporary regulations.

Announcement 86-6, page 52.

Portions of the Enterprise Standard Industrial Classification Manual (ESIC Manual) are reprinted. The codes provided in the ESIC Manual are used to determine an employer's lines of business for purposes of the availability of exclusions from gross income for certain fringe benefits under section 132 of the Code.

EMPLOYMENT TAXES

Rev. Rul. 86-10, page 7.

Withholding; failure to withhold tax or file return. An employer that inadvertently fails to deduct and withhold income taxes may make an interest-free adjustment if the employer files timely supplemental returns reporting the underpayment and the employee files an income tax return and pays the tax due. Rev. Rul. 58-577 modified.

ADMINISTRATIVE

Rev. Proc. 86-5, page 9.

Substitute printed, computer-prepared and computer-generated tax forms and schedules. Requirements are set forth for privately designed and printed federal tax return forms and the conditions under which the Service will accept computer-prepared and computer-generated tax forms and schedules. Rev. Proc. 85-3 superseded.

Announcement 86-7, page 67.

Publication 1212, List of Original Issue Discount Instruments (Rev. Dec. 85), is supplemented to provide information to banks, brokers, and other middlemen regarding Treasury bills issued at a discount and maturing during January through June 1986. Section II of Publication 1212 is also supplemented to include maturity dates and amounts of original issue discount for use *solely* by brokers and other middlemen in preparing information returns for zero coupon instruments issued under the Treasury's STRIP program or backed by Treasury securities.

Finding Lists begin on page 71
Announcement of Notice of Proposed Rulemaking on page 69.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 23.—Residential Energy Tax Credit

26 CFR 1.44C-2: Definitions.

Residential energy credit. A window covering and its integral edge mounting system is insulation under section 23(c)(3); expenditures for the system and its installation qualify for the residential energy tax credit under section 23(a).

Rev. Rul. 86-5

ISSUE

Whether the window covering system described below is "insulation" within the meaning of section 23(c)(3) (formerly section 44C) of the Internal Revenue Code so that expenditures for the system and its installation qualify for the residential energy tax credit under section 23(a).

FACTS

Taxpayer purchased a moveable, textile-based window covering that was installed in the taxpayer's principal residence. The residence was constructed before April 20, 1977. The product is a four-ply quilted window covering consisting of a vapor barrier and a layer of polyester batting sandwiched between two layers of a polyester cotton blend fabric, one of which is white. Each layer of the product, except the face fabric, is designed to enhance its insulating properties. The vapor barrier reduces heat transfer by preventing the passage of water vapor, the batting reduces conductive heat transfer, and the white fabric reflects radiant energy. Included as an integral part of the product is a draft resistant mounting and edge sealing system that reduces air infiltration.

Tests performed on the window covering system by an independent laboratory, in accordance with a recognized industrial standard, determined that the system's R-value is five times that of an ordinary drape. The R-value is a measure of the thermal insulating value of an item. The higher the R-value the better the insulating effect.

The cost of the window covering system greatly exceeds the cost of a decorative fabric drapery of equal dimensions. Consequently, it is not sold primarily for its decorative aspects as it could not be competitive with decorative drapes on the basis of either cost or aesthetics. Unlike decorative drapes, the system is marketed primarily for its insulating properties. The system can reasonably be expected to remain in operation for at least 3 years.

LAW AND ANALYSIS

Section 23(a) of the Code provides a credit for qualified energy conservation expenditures.

Section 23(c)(1) of the Code defines "energy conservation expenditure" to include an expenditure for insulation or any other energy-conserving component (or for the original installation of the insulation or other component) installed in or on the taxpayer's principal residence, but only if the construction of the residence was substantially completed before April 20, 1977.

Section 1.44c-2(c) of the Income Tax Regulations provides that the term "insulation" means any item that satisfies all of the following conditions:

(1) The item is specifically and primarily designed to reduce the heat loss or gain of a delling in which it is installed. To qualify as insulation, the item must be installed between a conditioned area and a nonconditioned area. Thus, for example, awnings do not qualify as insulation. For purposes of this section, the term "conditioned area" means an area that has been heated or cooled by conventional or renewable energy source means. Insulation includes materials made of fiberglass, rock wool, cellulose, urea based foam, urethane, vermiculite, perlite, polystyrene, and extruded polystyrene foam.

(2) The original use of the item begins with the taxpayer.

(3) The item can reasonably be expected to remain in operation at least three years.

(4) The item meets the applicable performance and quality standards prescribed in section 1.44C-4 of the regulations (if any) that are in effect at the time the taxpayer acquires the item.

The section also provides that the term "insulation" does not include items whose primary purpose is not insulation (for instance, items whose primary function is structural, decorative, or safety related). For example, carpeting, drapes (including linings), shades, wood paneling, fireplace screens (including those made of glass), new or replacement walls (except for qualifying insulation therein) and exterior siding do not qualify although they may have been designed in part to have an insulating effect.

The provision in the regulations that denies the credit to drapes does not apply to the window covering system at issue here. The test results indicate that the manufacturer considered all aspects of heat transfer, including air infiltration, when it designed the product and its sealing system. This resulted in a multi-layered design in which each layer and the mounting method reduce heat flow through the system and provide protection from the outside environment. These features are inherent in the design of the system and distinguish it from an insulated drape. In addition, the system costs more than a drape, provides draft resistance, and has a significantly greater R-value than a drape.

HOLDING

The window covering and its integral edge mounting system installed by the taxpayer is insulation within the meaning of section 23(c)(3) of the Code. Expenditures for the system and its installation qualify for the residential energy tax credit under section 23(a).

Section 871.—Tax on Nonresident Alien Individuals

26 CFR 1.871-7: Taxation of nonresident alien individual not engaged in a U.S. business.

A domestic taxpayer that owns all of the stock of an Antilles corporation may withdraw a portion of its paid in capital contribution such that the Antilles corporation's debt-to-equity ratio is increased from 3-to-1 to 5-to-1 without jeopardizing the Antilles corporation's separate corporate existence. See Rev. Rul. 86-6, below.

Section 881.—Tax on Income of Foreign Corporations not connected with United States Business

(Also Section 871; 1.871-1)

Tax on income of foreign corporations not connected with United States

business. A domestic corporation that owns all of the stock of a Netherlands Antilles corporation may withdraw a portion of its paid in capital contribution such that the subsidiary's debt-to-equity ratio is increased from 3-to-1 to 5-to-1 without jeopardizing the subsidiary's separate corporation status.

Rev. Rul. 86-6

ISSUE:

If a domestic corporation owns 100 percent of the stock of a corporation organized under the laws of the Netherlands Antilles (Antilles) and if the domestic corporation withdraws a portion of its equity capital invested in that Antilles subsidiary and thus increases the subsidiary's debt-to-equity ratio from 3-to-1 to 5-to-1, does this course of action jeopardize the subsidiary's separate corporate status for purposes of section 127(g)(3) of the Tax Reform Act of 1984 (the Act), 1984-3 (Vol. 1) C.B. 1, 160, and the principles set forth in the rulings cited therein.

FACTS:

P is a domestic bank holding company. In 1980, *P* organized *S* in the Netherlands Antilles for the purpose of raising funds in the Eurodollar market for *P*. S is a controlled foreign corporation (CFC).

S sold 15 million dollars of notes (Euronotes), denominated in United States dollars, to foreign investors during 1981. These notes were unconditionally guaranteed by *P*, and all of the net proceeds from the sale of the Euronotes were loaned to *P* by *S* in exchange for notes from *P*. The notes from *P* had the same terms as, and a slightly higher interest rate than, the Euronotes issued by *S*.

Prior to the Euronote issue, *P* contributed equity in the form of 5 million dollars to *S* such that immediately following the Euronote issue the debt to equity ratio of *S* was no more than 3 to 1 (that is, the face amount of *S*'s outstanding Euronote obligations was no more than three times the equity of *S*). *S* then placed this equity contribution in short term bank deposits with *Y*, an unrelated domestic corporation. Neither *P* nor any of its affiliates have any loans outstanding with *Y*.

In November 1984, in order to meet further cash requirements, *P* withdrew 2 million dollars of its previously contributed equity from *S*. *S*'s remaining equity capital, measured by the amount of *P*'s capital contribution of United Stats dollars that was being held in short term bank deposits in the United States, was 3 million dollars, and at no time was this capital contribution less than one-fifth of the face amount of *S*'s outstanding Euronote obligations.

LAW AND ANALYSIS:

Sections 871(a)(1)(A) and 881(a)(1) of the Internal Revenue Code, except as provided in the portfolio interest exemption in sections 871(h) and 881(c), respectively (added to the Code by section 127 of the Act), generally impose a 30 percent tax on any interest received by non-United States persons from sources within the United States, to the extent such interest is not effectively connected with the conduct of a trade or business within the United States. Section 1441(a) and 1442(a) provide generally that such tax is to be deducted and withheld at the source of the income.

A special grandfather rule in section 127(g)(3)(A) of the Act provides that, for purposes of the Code, payments of interest on a United States affiliate obligation to an applicable CFC in existence on or before June 22, 1984, shall be treated as payments to a resident of the country in which the CFC is incorporated.

Sections 127(g)(3)(C)(i) and 121(b)(2)(D) of the Act provide that the term "applicable CFC" means any controlled foreign corporation (within the meaning of section 957) which was in existence on the date of interest payment and the principal purpose of which on such date consisted of the issuing of CFC obligations or the holding of short-term obligations and lending the proceeds of such obligations to affiliates.

Section 957 of the Code provides, in part, that the term "controlled foreign corporation" means any foreign corporation of which more than 50 percent of the total combined voting power of all classes of stock entitled to vote is owned by United States shareholders on any day during the taxable year of such foreign corporation.

Sections 127(g)(3)(C)(ii) and 121(b)(2)(F) of the Act provide that the term "United States affiliate obligation" mans any obligation of (and payable by) a United States affiliate which was issued before June 22, 1984.

Section 121(b)(2)(E) of the Act defines the term "United States affiliate" to mean any United States person that is an affiliate (that is, any person that is a related person within the meaning of section 482 of the Code) of the "applicable CFC.

Section 127(g)(3)(B) of the Act provides that section 127(g)(3)(A) shall not apply to any "applicable CFC which did not meet requirements which are based on the principles set forth in Rev. Rul. 69-377, 1969-2 C.B. 231; Rev. Rul. 69-501, 1969-2 C.B. 233; Rev. Rul. 70-645, 1970-2 C.B. 273; and Rev. Rul. 73-110, 1973-1 C.B. 454. The four rulings concerned the Interest Equalization Tax (IET) and were revoked by Rev. Rul. 74-464, 1974-2 C.B. 46, when the IET expired (June 30, 1974).

Rev. Ruls. 69-377, 69-501, and 70-645 all concerned whether debt obligations issued by domestic or foreign subsidiaries of domestic parent corporations were bona fide. Under the facts of each of these revenue rulings, the bona fide nature of the debt obligations was generally dependent on the subsidiary maintaining a debt-to-equity ratio of no more than 5-to-1.

Rev. Rul. 73-110 concerned a domestic parent corporation that purchased all of the capital stock of its foreign financing subsidiary for United States dollars in an amount equal to 20 percent of the principal amount of the total debt obligations to be issued by the subsidiary. The parent made additional contributions in dollars to the subsidiary's equity capital each time the latter incurred additional indebtedness so that the subsidiary's capital would remain at least 20 percent of the principal amount of its outstanding indebtedness.

The subsidiary received Swiss francs in return for its debt obligations. During a taxable year, the financing subsidiary reduced the amount of its principal indebtedness and the domestic parent withdrew part of its equity capital contribution to maintain a five to one debt-to-equity ratio. The reduction in equity capital was computed on the basis of the currency exchange rate in existence at the time the principal debt of the subsidiary was incurred. Fluctuations in the value of the United States dollar relative to the Swiss franc resulted in an increase in the value of the Swiss franc. Thus, when computed on the basis of the actual currency exchange rate prevailing at the time of the withdrawal, the debt-to-equity capital ratio was, after the withdrawal by the parent, greater than five-to-one.

Rev. Rul. 73-110 held that in determining whether the aggregate face amount of the subsidiary's outstanding indebtedness never exceeds five times the amount of its equity capital, the ratio must be periodically recomputed on the basis of the currency exchange rate in existence at the time of any of the following occurrences: (1) additional borrowings by the financing subsidiary and/or (2) withdrawals from the subsidiary's equity capital by its parent for any reason, such as a reduction in the subsidiary's indebtedness.

In order to meet its cash requirements and because of the passage of section 127(g)(3) of the Act, *P* decided to reduce its equity contribution to *S* by 2 million dollars. This reduction increased *S*'s debt-to-equity ratio from 3-to-1 to 5-to-1.

Rev. Rul. 73-110 contemplated that periodic adjustments may be made to a financing subsidiary's equity capital. Neither Rev. Rul. 73-110 nor the other revenue rulings cited above indicated that the debt of a financing subsidiary could be recharacterized as the debt of the parent merely on the grounds that the subsidiary's debt-to-equity ratio had increased from 3-to-1 to 5-to-1 and was maintained at a ratio of 5-to-1.

For the limited purpose of measuring *S*'s debt-to-equity ratio to determine if that ratio meets the requirements of section 127(g)(3) of the Act, the dollar-denominated Euronotes of *S* are taken into account at face value in accordance with Rev. Rul. 73-110. The equity capital of *S*, for this same limited purpose, is the amount of United States dollars contributed as equity to *S* to the extent that this dollar equity contribution has not subsequently been withdrawn from *S*.

In the present situation, *P* withdrew 2 million dollars of its original 5 million dollar capital contribution, leaving *S* with an equity capital amount of 3 million dollars. Because *S*'s liabilities are computed at face value, they remained at 15 million dollars. Thus, after the transaction, *S* had a debt-to-equity ratio that did not exceed 5-to-1.

HOLDING:

P may withdraw equity capital from *S* without jeopardizing *S*'s separate corporate status or the bona fide nature of *S*'s indebtedness under section 127(g)(3) of the Act and the principles set forth in the revenue rulings cited therein, provided that immediately following the withdrawal of a portion of *S*'s equity capital *S*'s indebtedness does not exceed five times the remaining equity capital.

Section 1032.—Exchange of Stock for Property

26 CFR 1.1032-1: Disposition by a corporation of its own capital stock.

Obsolete rulings Certain rulings involving section 1032(a) of the Code are declared obsolete with respect to options acquired or lapsing after July 18, 1984, the effective date of section 57(a) of the Tax Reform Act of 1984.

Rev. Rul. 86-9

Certain rulings involving section 1032(a) of the Internal Revenue Code are declared obsolete with respect to options acquired or lapsing after July 18, 1984, the effective date of section 57(a) of the Tax Reform Act of 1984, 1984-3 (Vol. 1) C.B. 1, 82, which amended section 1032(a).

Periodically, the Internal Revenue Service has declared obsolete rulings that are not considered determinative with respect to future transactions because the applicable statutory provisions have been changed or repealed.

In accordance with this policy, the Internal Revenue Service has reviewed revenue rulings published in the Internal Revenue Bulletin regarding section 1032(a) of the Code to determine whether they are applicable to transactions after July 18, 1984, and has determined that the following revenue rulings are obsolete and are not determinative with respect to stock warrants that were acquired, or that lapse, after July 18, 1984, in tax years ending after that date:

Rev. Rul. 72-198, 1972-1 C.B. 223
Rev. Rul. 77-40, 1977-1 C.B. 248
Rev. Rul. 78-73, 1978-1 C.B. 265
Rev. Rul. 80-134, 1980-1 C.B. 187.

Section 1256.—Section 1256 Contracts Marked To Market

Regulated futures contracts: qualified board or exchange. The Mercantile Division of the Montreal Exchange is a qualified board or exchange for purposes of section 1256 of the Code.

Rev. Rul. 86-7

ISSUE

Whether the Mercantile Division of the Montreal Exchange is a qualified board or exchange within the meaning of section 1256(g)(7)(C) of the Internal Revenue Code.

LAW

Section 1256(g)(7) of the Code provides that the term "qualified board or exchange" means—

(A) a national securities exchange which is registered with the Securities and Exchange Commission,

(B) a domestic board of trade designated as a contract market by the Commodity Futures Trading Commission, or

(C) any other exchange, board of trade, or other market which the Secretary determines has rules adequate to carry out the purposes of this section.

HOLDING

The Internal Revenue Service has determined that the Mercantile Division of the Montreal Exchange is a qualified board or exchange within the meaning of section 1256(g)(7)(C) of the Code.

Regulated futures contracts; nonequity option. An option on the High Technology Index of the Pacific Stock Exchange is a nonequity option for purposes of section 1256 of the Code.

Rev. Rul. 86-8

ISSUE

Whether an option on the High Technology Index of the Pacific Stock Exchange is a nonequity option within the meaning of section 1256(g)(3) of the Internal Revenue Code.

LAW

Section 1256 of the Code prescribes special rules for reporting gains and losses from "section 1256 contracts."

Section 1256(b) defines the term "section 1256 contract" as any regulated futures contract, any foreign currency contract, any nonequity option, and any dealer equity contract.

Section 1256(g)(3) of the Code provides that the term "nonequity option" means any listed option which is not an equity option.

Section 1256(g)(6)(B) of the Code provides that the term "equity option" does not include any option with respect to any group of stocks or stock index if—

(i) there is in effect a designation by the Commodities Futures Trading Commission of a contract market for a contract based on such group of stocks or index, or

(ii) the Secretary determines that such option meets the requirements of law for such a designation.

HOLDING

The Internal Revenue Service has determined that an option on the High Technology Index of the Pacific Stock Exchange is a nonequity option within the meaning of section 1256(g)(3) of the Code.

Section 3402.—Income Tax Collected At Source

26 CFR 31.3402(d)-1: Failure to withhold.

Whether an employer that inadvertantly fails to deduct and withhold income taxes may make an interest-free adjustment if the employer files timely supplemental returns reporting the underpayment and the employee files an income tax return and pays the tax due. See Rev. Rul. 86-10, this page.

Section 6011.—General Requirement of Return, Statement, or List

26 CFR 1.6011-1: General requirement of return, statement, or list.

Requirements for the reproduction and private design and printing of federal tax return forms and the conditions under which the Service will accept computer-prepared and computer-generated tax forms and substitutes. See Rev. Proc. 86-5, page 9.

Section 6205.—Special Rules Applicable to Certain Employment Taxes

26 CFR 31.6205-1: Adjustment of underpayments.
(Also Sections 3402, 6601; 31.3402(d)-1, 301.6601-1.)

Withholding; failure to withhold tax or file return. An employer that inadvertently fails to deduct and withhold income taxes may make an interest-free adjustment if the employer files timely supplemental returns reporting the underpayment and the employee files an income tax return and pays the tax due. Rev. Rul. 58-577 modified.

Rev. Rul. 86-10

ISSUE

Is interest due from an employer who failed to deduct and withhold income tax from the wages of an employee if the employee subsequently filed an income tax return and paid the tax due, and the employer filed timely supplemental returns reporting the underpayment?

FACTS

An employer inadvertently failed to deduct and withhold income tax from the wages of an employee in 1983, as required under section 3402 of the Internal Revenue Code, and did not report any amount as being withheld from the employee on its Form 941, Employer's Quarterly Federal Tax Return, for any quarter in that year. The employer ascertained the error within the meaning of section 31.6205-1(a)(4) of the Employment Tax Regulations in May 1984, and filed the necessary supplemental returns for all quarters in 1983 by July 31, 1984. The tax that should have been withheld, plus interest, was then assessed. Meanwhile, the employee had filed a timely income tax return for 1983 and paid the tax due. When the employer presented this information to the Internal Revenue Service, the tax assessed against the employer with respect to the supplemental returns was abated in accordance with section 3402(d).

LAW AND ANALYSIS

Section 6205(a) of the Code provides that if less than the correct amount of tax imposed by section 3402 is paid with respect to any payment of wages or compensation, proper adjustments of both the tax and the amount to be deducted must be made, without interest, in the manner prescribed by regulations.

Section 31.6205-1(c)(2)(i) of the regulations sets forth the conditions under which an interest-free adjustment is made if an employer filed a return and reported either no income tax or less than the correct amount of income tax required to be withheld by an employer from the wages of an employee. The employer must adjust the error by either (a) reporting the additional amount due on a return for any quarter in the calendar year in which the wages were paid or (b) reporting the additional amount on a supplemental return for the period in which the wages were paid. Such reporting constitutes an adjustment under section 6205(a) of the Code only if the return or supplemental return is filed on or before the due date for the return for the quarter in which the error is ascertained.

Under section 31.6205-1(a)(4) of the regulations, an error is ascertained, for purposes of section 31.6205-1(c)(2)(i), when the employer has sufficient knowledge of the error to be able to correct it. An employer has such sufficient knowledge if the employer disregards facts with the knowledge that there is a substantial possibility that further inquiry into such facts would result in the employer discovering the error.

Section 31.6205-1(c)(3)(ii) of the regulations provides that, except as provided in section 31.3402(d)-1, any amount reported as an adjustment under section 6205(a) of the Code must be paid, without interest, at the time fixed for reporting the adjustment.

Under section 31.3402(d)-1 of the regulations, if the employer fails to deduct and withhold the tax, but can show that the income tax has been paid against which the tax under section 3402 of the Code may be credited, the tax under section 3402 will not be collected from the employer.

In this case, the employer made a proper and timely adjustment under section 6205 of the Code and section 31.6205-1(c) of the regulations. The tax required to be withheld that was assessed against the employer was abated because the employee's tax liability had been satisfied.

HOLDING

The employer is not liable for interest because the requirements for an interest-free adjustment were met.

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 58-577, 1958-2 C.B. 744, holds, in part, that interest is due from an employer under similar facts. Rev. Rul. 58-577, as modified by Rev. Rul. 66-113, 1966-1 C.B. 244, is further modified.

Section 6601.—Interest on Underpayment, Nonpayment, or Extensions of Time for Payment, of Tax

26 CFR 301.6601: Interest on underpayments

Whether an employer that inadvertantly fails to deduct and withhold income taxes may make an interest-free adjustment if the employer files timely supplemental returns reporting the underpayment and the employee files an income tax return and pays the tax due. See Rev. Rul. 86-10, page 7.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.602: Tax forms and instructions.
(Also Part I, Section 6011; 1.6011-1.)

Rev. Proc. 86-5

SECTION 1. PURPOSE

This revenue procedure states the Internal Revenue Service (the Service) requirements relating to acceptable privately designed and printed or computer-prepared substitute federal tax return forms, (i.e., Forms 1040, 1040A, 1040EZ, 1120, 1120A, 940, 941, etc.) and computer-generated substitute schedules or forms to be attached thereto. It also authorizes the use of reproductions of official forms and gives direction for the proper completion of returns.

SEC. 2. SCOPE

This revenue procedure is the guide for preparing substitutes for most printed, computer-prepared and computer-generated tax forms. This procedure does not include guidance for Form 1040-ES, Form 1042S, Form 5498, Form 1098, the Form 1099 series, Form W-9 and the Form W-2 series. (See Sec. 18 to obtain guidance for the excluded forms.)

SEC. 3. DEFINITIONS

.01 *Substitute Form.* A tax form (or related schedule) that differs in any way from the official version and is intended to replace the entire form that is printed and distributed by the Service. This term also covers those approved substitute forms exhibited in this revenue procedure.

.02 *Printed Form.* A form produced using conventional printing processes. Also, a printed form which has been reproduced by photocopying or similar processes.

.03 *Preprinted Pin-Fed Form.* A printed form that has marginal perforations for use with automated and high-speed printing equipment.

.04 *Computer-Prepared Substitute Form.* A pre-printed form in which the taxpayer's tax entry information has been inserted by a computer, computer-printer or other computer-type equipment, such as word-processing equipment.

.05 *Computer-Generated Substitute Form.* A form that is entirely prepared by the use of a computer printer so that all the line numbers, line captions, and the tax amount data entries are in the same typeface. No graphics usually appear on the form. (Most tax returns requiring signature and establishing tax liability may not be computer generated. Among them are Forms 1040, 1040A, 1040EZ, and 1120.)

.06 *Manually Prepared Form.* A pre-printed reproduced form in which the taxpayer's tax entry information is entered by an individual using a pen, pencil, typewriter, or other non-automated equipment.

.07 *Graphics.* Those parts of a printed tax form that are not tax amount entries or called-for information. Generally, these are line numbers, captions, shadings, instructions, special indicators, borders, rules, and strokes created by typesetting, photo-graphics, photo-composition, etc.

.08 *Acceptable Reproduced Form.* A photocopy of an original form or of an unchanged reproduction proof supplied by the Service. (A reproduction is not a substitute form.)

.09 *Supporting Statement (Supplemental Schedule).* A document providing detailed information to support an entry for a line(s) on an official or approved substitute form and filed with (attached to) a tax return. (A supporting statement is not a tax form and does not take the place of an official form, unless specifically permitted elsewhere in this procedure).

.10 *Specific Form Terms.* The following terms are used throughout this revenue procedure in reference to all substitute forms.

1 *Format.* The overall physical arrangement and general layout of a substitute form, as represented by the official form version.

2 *Sequence.* The same numeric and logical placement order of data, as reflected on the official form version. Sequence is an integral part of the total format requirement.

3 *Line Reference (Code).* The line numbers, letters or alpha-numerics used to identify each captioned line on the official forms; and printed to the immediate left of each caption or data entry field.

4 *Item Caption.* The textual portion of each line on the form, identifying the specific data elements required.

5 *Data Entry Field.* All areas designated on a form for the insertion of data, such as dollar amounts, quantities, responses, check-boxes, etc.

SEC. 4. MESSAGE TO TAX RETURN PREPARERS

.01 If you plan to change or modify *any* tax forms, you must follow these procedures, and, in many cases, you must get official approval before using substitute forms. The Service is continuing a program to identify and contact tax return preparers using unapproved forms which do not conform to this revenue procedure and impede processing of the return.

SEC. 5. HIGHLIGHTS OF PERMITTED CHANGES AND REQUIREMENTS

.01 THINGS YOU *CAN DO* TO INTERNAL REVENUE SERVICE PRINTED TAX FORMS TO MAKE THEM SUITABLE FOR USE AS SUBSTITUTE TAX FORMS WITHOUT PRIOR APPROVAL.

1 You can photocopy any tax form and use it instead of the official one.

2 You can reproduce any current tax form as cut sheets, snap-sets, and marginally-punched, pin-fed forms, so long as you use an official Service version as the master copy. Official versions are supplied by the Service, such as those in the taxpayer's tax package, those in Package X, those printed in revenue procedures, and reproduction proofs sold by the Service.

3 You can adjust the graphics on specified areas of printed forms 1040 and 1040A (and other forms) to allow for computer-printed or word processor fill-in. Only the areas listed in this revenue procedure may be adjusted without specific prior approval.

4 You can print and duplicate the substitute "worksheet-type" versions of Schedules A and B of Form 1040 (see exhibits). The Service will accept these substitute schedules instead of the official versions. These Schedules serve different purposes. One allows the form to contain state tax information which is blocked out before filing with the Service. The other allows the form to be used singly or as part of a snap-set.

.02 THINGS YOU *CANNOT DO* TO INTERNAL REVENUE SERVICE PRINTED TAX FORMS TO MAKE

THEM SUITABLE FOR USE AS SUBSTITUTE TAX FORMS.

1 You cannot, without prior Service approval, change any Internal Revenue Service tax forms or use your own (non-approved) version, unless specifically permitted by this revenue procedure. Only minor changes are permitted to an official tax form, as OPM approval was based on the specific format and content of each form submitted by the Service.

2 You cannot adjust any of the graphics on Forms 1040, 1040A and 1040EZ (except in those areas specified in revenue procedures) without prior approval from the Service.

3 You cannot use your own version of Schedule A (Form 1040) unless you first get it approved. The Service wants only one Schedule A—either yours or the Service's; yours needs prior approval from the Service.

4 With some exceptions, you cannot omit filling out pertinent referenced (numbered or lettered) lines of the official Schedule A (and other tax forms) when attaching a supporting statement. Exceptions to line completion requirements are listed in this revenue procedure.

5 You cannot use your own preprinted label on tax returns filed with the Service. The ONLY label permitted is the one provided the taxpayers in their tax packages. Otherwise, the taxpayer's name, address, and other identifying information must be entered on the return in the spaces provided.

6 You cannot computer-generate the TAX RETURNS THEMSELVES (i.e. forms requiring signature and that establish tax liability; for example, Forms 1040, 1040A, 1040EZ, 1120, 940 and 941). These forms must be preprinted using conventional printing processes, photocopying or similar reproduction processes. The forms may be filled in by a computer, by a word processor, or the like, but the forms themselves must be printed like the Service versions are. First-time users of forms designed using computer graphics must receive prior written approval. (See Exception in Sec. 22).

(a) Schedules are considered to be an integral part of the tax return itself and, therefore, cannot be computer-generated when they have been assigned consecutive page numbers and printed contiguous with page one of the return. Form 706, United States Estate Tax Return is an example of this situation, where Schedules A through P are on pages numbered as part of the basic return and cannot be separately computer-generated.

(b) However, Schedule 1 of Form 1040A is an example of when a schedule can be acceptably computer-generated. Although printed as a continuation of Form 1040A, the two pages of Schedule 1 do not have consecutive page numbers, and may, therefore, be separated from Form 1040A and submitted as a computer-generated substitute schedule.

(c) A "tax return" must remain complete, with its signature covering the entire return including all its assigned or associated (numbered) pages.

7 A few selected Service forms can never be reproduced as substitute forms, because only the official versions are acceptable for filing, due to their use in critical Service programs. These forms specify in their instructions that a substitute cannot be accepted or used in lieu of the prescribed, official form.

(a) Forms 8109 and 8264 are the major forms that currently fall in this excluded category.

.03 THINGS YOU CAN DO TO FILE COMPUTER-PREPARED/ GENERATED FORMS. PRIOR APPROVAL IS NOT REQUIRED.

1 You can duplicate the approved, computer-generated formats of Schedules 1, A, B, C, D, E, F, G, R, SE, and W (of this revenue procedure), and use them without prior approval.

2 You can fill in official Service supplied forms using computer or word-processing equipment. Most official Service forms are designed for a vertical spacing of six lines to the inch, with money amount columns wide enough to allow for the computer printing of ten characters.

3 You can change certain specified areas on the Forms 1040 and 1040A (spelled out in the revenue procedures) to assist computer-printing requirements and to allow for a little more room on certain lines.

4 If you meet the requirements, standards, and qualifications of this revenue procedure, *you can*, without prior approval, computer-generate your own substitutes of the tax forms (except for actual tax returns) not exhibited here. (See Agreement in Sec 21).

SEC. 6. APPROVAL

.01 *Basic Requirements*. Preparers who desire to file substitute privately designed and printed tax forms and/or computer-generated and computer-prepared tax forms must develop such substitutes using these guidelines. These substitutes, unless excepted by revenue procedure, must be approved by the Service before being filed.

.02 *Requests for Approval.*

1 The Service cannot approve your substitute form until the official form has been published. Please propose your substitute after you have examined the official form.

2 You should know the Service revenue procedure relating to the official form before you attempt to alter the form to meet your needs. Any alteration of forms must be within the limits acceptable to the Service. It is possible that, from one filing period to another, a change in law or a change in internal need (processing, audit, compliance, etc.) may change the allowable limits for the alteration of the official form.

3 When specific approval of any substitute form is desired, a sample of the proposed substitute should be forwarded for consideration by letter to the Internal Revenue Service, Attention: Substitute Forms Program Coordinator, D:R:R:I, 1111 Constitution Avenue, N.W., Washington, DC 20224. To expedite multiple forms approval, we prefer that your proposed forms be submitted in separate sets by return. For example, Forms 1040 and their normally related schedules or attachments should be separated from Forms 1120, etc., if at all possible. Schedules and forms (i.e., Forms 3468, 4136, etc.) that can be used with more than one type of return (1040, 1041, 1120, etc.) should be submitted only once for approval, regardless of the number of different tax returns they may ultimately be associated with.

4 As no Service office outside Washington, D.C. is authorized to approve substitute forms, unnecessary delay may result if forms are sent elsewhere for approval. All such forms must be forwarded to the above address for formal control, review, and official approval.

.03 *When to Send Proposed Substitutes*. Proposed substitutes should be sent to the address listed in .02 above, as much in advance of the filing period for the form as possible. This is to allow adequate time for analysis and response and to permit notice to our field offices that your substitute is acceptable. Quarterly filed forms, such as the Form 941, must be submitted by the first day of the last month of the quarter.

.04 *Accompanying Statement.* When the sample substitute is submitted, there should be an accompanying statement that lists the form number of each substitute requested and details those items that deviate from the official form in position, arrangement, appearance, line numbers, additions, deletions, etc. Included with each of the items should be a detailed reason or justification for the change and an approximation of the number of forms expected to be filed.

.05 *Approval/Non-Approval Letter.* The Service sends a formal letter of approval/non-approval. Approval letters may contain qualifications for use of the substitutes. Non-approval letters may specify the changes required for approval, but also may require resubmission for approval. Telephone contact is used when warranted.

.06 *Duration of Approval.*

1 Approvals are good for only one calendar year (January through December) or, in the case of corporation tax forms (with the exception noted below), for the remainder of the quarters of the calendar year.

2 Please Note: In most cases each new filing season requires a new approval, even if the official form does not change. But see the exceptions in 3 and 4 below.

3 Exception: Quarterly tax forms in the 94X series (941, 942, etc.) are approved only for one quarter. Each new quarter requires a new approval.

4 Exception: Limited continued use of a change approved for one tax year may be allowed for the same form in the following tax year. See 07. below for the limitations and for other requirements. Examples of such changes are the use of abbreviated words, revised form spacing, compressed text lines, shortened captions, etc., which do not change the consistency of lines or text on the official forms.

.07 *Limited Continued Use of an Approved Change.*

1 If you received written approval of a previous tax year substitute form governed by this revenue procedure and wish to continue to use the approved change in your current tax year substitute form, you may revise your form to include this change and, without additional written approval, use it as a current tax year substitute form, provided you comply with the requirements in this revenue procedure. See exception in 2 below.

2 This means that if you received written approval for a specific change on a specific form last year, you may again make the same change on the same form this year, if the item changed is present on this year's official form. Thus, the change allowed in last year's approved substitute Schedule A, for example, can be continued in your new substitute for this year. The new substitute does not have to be sent to the Service, and written approval is not required. However, the new substitute must conform to the official current year form in other respects: date, Office of Management and Budget (OMB) approval number, sequence number, Paperwork Reduction Act Notice Statement, arrangement, item caption, line number, line reference, data sequence, etc. It must also comply with this revenue procedure—which may have eliminated, added to, or otherwise changed the guideline which affected the change approved last year. Additionally, you will be bound by the "Agreement" in Section 21. Exception: Those written approvals which stated that the approved change or form would not be allowed in any other tax year.

3 This authorization for continued use of an approved change is limited to the continuation of design logic from an immediately prior tax year substitute form to a current tax year substitute form.

.08 *Requested Copies.* In our letter of approval, *you may* be requested to send to the Service eleven (11) copies of each approved form. When received, the copies will be used to notify Internal Revenue Service Centers that your proposed substitute forms are approved. The requested forms should be assembled in sets. A set constitutes a return with the related schedules and forms in the same order as they will be filed, i.e., Form 1040, Schedules A, B, C, etc., and associated Forms 2119, 2441, etc.

.09 *Responsibility.* Following the receipt of initial approval for a substitute forms package, or of a software output program to print substitute forms, it is the responsibility of the originator (designer or distributor) to provide each subsequent client firm or individual with the pertinent Service forms requirements which must be met for continuing acceptability. Examples of this responsibility include the use of prescribed print paper, font size, legibility, state tax data deletion, the legal requirement of the Paperwork Reduction Act Notice for informing all users of substitute forms of the official use and collection requirements stated in the instructions for the official Service forms, completion of documents, etc.

SEC. 7. OFFICE OF MANAGEMENT AND BUDGET (OMB) REQUIREMENTS FOR ALL SUBSTITUTE FORMS

.01 *Legal Requirements of the Paperwork Reduction Act of 1980.* Public Law 96-511 requires that: (1) OMB approve all Service tax forms, (2) each Service form contains (in the upper right corner) the OMB approval number and any expiration date, and (3) each Service form (or instructions) state why the Service is collecting the information, how it will be used, and whether or not the information is required to be furnished. This information *must* be provided to every user of any official or substitute tax forms.

.02 *Application to Substitute Forms.*

1 *Approval Number and Date Is Required.* All substitute forms must contain in the upper right corner (see Marginal Printing, Sec. 11.02.1(c)) the OMB number and any expiration date that is on the official form.

2 Format Required (3 Options).

(a) OMB No. XXXX-XXXX (preferred) or OMB # XXXX-XXXX

(b) OMB No. XXXX-XXXX (preferred) Expires XXXXXX (mmddyy) or OMB # XXXX-XXXX Expires XXXXXX (mmddyy)

(c) OMB No. XXXX-XXXX Expires XXXXXX (mmddyy) (preferred) or OMB # XXXX-XXXX Expires XXXXXX (mmddyy)

3 *Required Explanation to Users of Substitute Forms.* You must also inform the users of your substitute forms of the Service use and collection requirements stated in the instructions for

the official Service form. If you provide your users or customers with official Service instructions, page 1 of each form must retain the Paperwork Reduction Act Notice Statement as on the official forms (usually in the lower left corner of the forms). Otherwise, you must duplicate the material in the statement and add the phrase, "For Paperwork Reduction Act Notice, See Separate Instructions."

(a) If the Service instructions are not provided to users of your forms, the exact text of the Paperwork Reduction Act Notice must be furnished separately. This notice reads, "We ask for this information to carry out the Internal Revenue laws of the United States. We need it to ensure that taxpayers are complying with these laws and to allow us to figure and collect the right amount of tax. You are required to give us this information."

.03 *Obtaining OMB Number, Date, and Statement*. The OMB approval number, expiration date, and use and collection requirements may be obtained from the official printed form (or its instructions), the reproduction proof (or instructions), or from the Service.

SEC. 8 GENERAL GUIDELINES

.01 *Official Form is the Standard*. Because a substitute form is a variation from the official form, you should know the requirements of the official form for the year of use before you modify it to meet your needs. For the most frequently used tax forms, the quickest way to obtain an official form is to request reproduction proofs of these forms. (See Sec. 20.)

.02 *Design*. Each form must follow the design of the official form as to format, arrangement, item caption, line numbers, line references, and sequence.

.03. *State Tax Information Prohibited*. State tax information must not appear (be visible) on the federal tax return which is filed with the Internal Revenue Service Center, except where amounts are claimed on or required by the federal return, e.g., line 6, Schedule A (Form 1040). (See Sec. 12.05 Block Out Methods.)

.04 *Federal and State Columns*. When a form is designed with both federal and state columns, the federal column must be to the left of the state column and adjacent to the line caption.

.05 *Vertical Alignment of Amount Fields*. 1 When a form is to be computer-prepared, you may remove the vertical line in the amount field that separates dollars from cents. When a form is to be computer-generated, vertically align the amount entry fields where possible. You must also use one of the ten-character amount formats shown in Sec. 23.04. Amount fields may be "rounded off" to dollars only, where form instructions specifically permit such entries.

2 When a form is to be manually prepared, the federal column must have a vertical line or some type of indicator in the amount field to separate dollars from cents if the official form has a vertical line. The cents colums must be at least ⅛-inch wide.

.06 *Sequence Number*. Please note that most forms have a "sequence number" located just below the year designation in the upper right corner of the form. The Service uses this number to indicate the order in which forms are processed when filed with a return. On computer-prepared forms it must be printed no less than 12-point, bold-face type and centered below the form's year designation. On computer-generated forms, place this sequence number following the year designation for the tax form and separate with an asterisk. (See Forms Exhibits at end of this Revenue Procedure).

.07 *Sequence Numbers Required*. The sequence number is required on most Service forms. Please note that some of the numbers necessarily change each year. The specific sequence numbers used on official Service forms must be duplicated on the representative substitute form. If a sequence number is not provided on the official form, it is not required on a substitute of that form either.

.08 *Paid Preparer's Information and Signature Area*.

1 On Forms 1040A, 1040, and 1120, etc., the "Paid Preparer's Use Only" area may not be rearranged or relocated. You may, however, add three extra lines to the paid preparer's address area without prior approval. This applies to other tax forms as well.

2 On Form 1040EZ this information must be provided at the bottom of the form below the taxpayer's signature area. As an alternative, the printed Paid Preparer's Information and Signature Area from either a Form 1040 or 1040A may be attached to the bottom of Form 1040EZ.

.09 *Assemblage of Forms*. When filing a return (i.e., Form 1040), the return must be arranged in this order: (1) the tax return, (2) Form 1040 schedules and forms in sequence number order, (3) all others (Form 1120, 1120S, 1065, 1041, etc.), lettered schedules (Schedule D, etc.) in alphabetical order and numbered forms in numerical order (Forms 2220, 4626, etc.) (4) supporting statements in the same sequence as the forms they support, and (5) additional information required or voluntarily submitted. In this way, they are received in the order in which they must be processed. If you do not send them to us in this order, the Service has to disassemble them and place them in this order before processing is continued.

SEC. 9. PHYSICAL ASPECTS AND REQUIREMENTS: PAPER

.01 *Paper Content*. The paper must be:

1 Chemical wood writing paper that is equal to or better than the quality used for the official form;

2 at least 18 pound (17″ × 22″, 500 sheets) or

3 at least 45 pound (25″ × 38″, 500 sheets).

.02 *Paper Prohibited*. Carbon-bonded paper is prohibited from use for all substitute forms filed with the Service.

.03 *Paper with Chemical Transfer Properties—Limited Use*. Chemical transfer paper for all substitute forms may be used only when the following specifications are met.

1 Each ply within the chemical transfer set of forms must be labeled.

2 Only the top ply (ply one and white in color), the one which contains chemical on the back only (coated back), may be filed with the Service. For example, a set containing three plies would be constructed as follows: ply one (coated back), "Federal Return, File with IRS"; ply two (coated front and back), "Taxpayer's copy"; and ply three (coated front), "Preparer's copy."

3 The file designation, "Federal Return, File with IRS," for ply one must be printed in the bottom right margin (just below the last line of the form) in 12-point, bold-face type. It is not man-

datory, but recommended, that the file designation, "Federal Return, File with IRS," be printed in a contrasting ink for visual emphasis.

4 Carbon Paper. We prefer that you do not attach any carbon paper to any return you file with the Service.

.04 *Paper and Ink Color.* We prefer that the color of paper substantially duplicate that of the original form. You may use white paper. This means that your substitute must be printed in black ink and may be on white or on the color paper the Service form is printed on. An exception to this rule is that Forms 1040A, 1040EZ, and 1040 substitute reproductions may be in black ink without the colored screening. Any additional exception to this rule requires written approval from the Service.

.05 *Page Size.* Substitute or reproduced forms and computer-prepared/generated substitutes may be the same size as the official form (8" × 11", in most cases) or they may be the standard commercial size (8½ × 11") exclusive of pin-feed holes. The thickness of the stock cannot be less than .003 inch.

.06 *Lined Paper.* Computer-generated substitute forms must be submitted on quality lined, machine paper. Lined, color-barred paper is also acceptable. Lined paper assists Service employees during processing of the returns by allowing speedy and accurate location of tax entries corresponding to line captions. The lines provide the basic means for eye-travel from one side of the form to the other, and significantly reduces processing errors. Only original forms should be filed with IRS, as copies frequently do not meet legibility requirements, especially copies of forms originally printed on color-barred paper stock.

.07 *Exception to Lined Paper Requirement.* If your printer has underlining capability, you do not have to use lined or color-barred paper so long as you underline every other text line on the form. The underlining must be a continuous line and extend from the left text margin to the right text margin and be the same length for all lines on the page.

SEC. 10. PHYSICAL ASPECTS AND REQUIREMENTS: PRINTING

.01 *Printing Medium.* The private printing of all substitute tax forms must be by conventional printing processes, photocopying, computer-graphics, or similar reproduction processes.

.02 *Legibility.* All forms must have a high standard of legibility, both as to printing and reproduction and as to fill-in matter. The Service reserves the right to reject those with poor legibility. The ink and printing method used must ensure that no part of a form (including text, graphics, data entries, etc.) developes "smears" or similar quality deterioration, including any subsequent copies or reproductions made from an approved master substitute form; either during preparation or during Service processing.

.03 *Type Font.* Almost all federal tax forms are printed using "News Gothic" as the basic type font. We request that you use this type font when composing any substitute forms.

.04 *Image Size.* The image size of printed substitute forms should be as close as possible to that of the official form. You may omit any text on both computer-prepared and computer-generated forms that is solely instructional.

.05 *Title Area Changes.* To allow a larger top margin for marginal printing and more lines per page (see Sec. 11 below), the title line(s) for all substitute forms (not including the form's year designation and sequence code, when present), may be photographically reduced by 40 percent or reset as one line of type. When reset as one line, the type size may be no smaller than 14-point. You may omit "Department of the Treasury, Internal Revenue Service" and all reference to instructions in the form's title area.

.06 *Remove Government Printing Office Symbol.* When privately printing substitute tax forms, the Government Printing Office symbol and/or jacket number must be removed. In the same place, using the same type size, print the Employer Identifying Number (EIN) or the Social Security Number (SSN) of the printer or designer.

.07 *Printing On One Side of Paper.* While it is preferred that both sides of the paper be used for substitute and reproduced forms, resulting in the same page arrangement as that of the official form or schedule, the Service will not object if only one side of the paper is used.

.08 *Photocopy Equipment.* The Service does not undertake to approve or disapprove the specific equipment or process used in reproducing official forms, but requires only that the reproduced forms satisfy the conditions stated in the revenue procedures.

.09 *Reproductions.* Reproductions of official forms and substitute forms which do not meet the requirements of this revenue procedure may not be filed instead of the official forms.

.10 *Removal of Instructions.* You may remove all references to instructions. No prior approval is needed. One exception is that the statement "For Paperwork Reduction Act Notice, See Instructions", must be retained or a similar statement provided on each form.

SEC. 11. PHYSICAL ASPECTS AND REQUIREMENTS: MARGINS

.01 *Margin Size.*

1 The format of a reproduced tax return when printed on the page must have margins on all sides at least as large as the margins on the official form. This allows room for Service employees to make the necessary entries on the form during processing.

2 A one-half to one quarter inch margin must be maintained across the top, bottom, and both sides (exclusive of any pin-feed holes) of all computer-generated substitutes. The margin area is also used by Service employees to make necessary entries on the form during processing.

3 The marginal, perforated strips containing the pin-feed holes must be removed prior to filing the form with the Service.

.02 *Marginal Printing.*

1 Non-Tax Material Allowed in Limited Areas.

(a) On any 8- or 8½-inch-wide Service or substitute form, you may print your logo, company or firm name, identifying and collation symbols, etc., in the *left half of the top margin.*

(b) With the exception of the actual tax return forms (i.e., Forms 1040, 1040A, 1040EZ, 1120, 940, 941, etc.), you may also print in the *left vertical margin* and in the *left half of the bottom margin.*

(c) Printing is never allowed in the *right half of the top margin* of the tax return form (i.e. Forms 1040, 1040A, 1040EZ, 1120, 940, 941, etc). The Service uses this area to imprint a File

Location Number for each return.

2 *Prior Approval Not Required.* Prior approval is not required for the marginal printing allowed in 1 above when used with the unchanged exhibits in this revenue procedure or when printed on an official form, on a photocopy of an official form or on an (unchanged) Service reproduction proof.

3 *Prior Approval Required.* The marginal printing allowance in 1 above is also the guide for the preparation of acceptable substitute forms. There is no exception to the requirement that no printing is allowed in the *right half of the top margin* of the tax return form.

SEC. 12. APPROVED SUBSTITUTE FORMATS FOR FORM 1040 SCHEDULES

.01 *Exhibits of Approved Formats.* Two sets of exhibits (Exhibits A-1, B-1, A-2 and B-2) are at the end of this revenue procedure. They are acceptable substitutes for the official forms. They are intended to be used in place of the official forms and may be used without prior approval. Both sets are usable for manual entry or computer preparation. Vertical spacing is six (6) lines to the inch. You may also refer to them as examples of how the guidelines in this revenue procedure may be used in some specific cases. Please note that the Service does not supply reproduction proofs for these exhibits.

.02 *Printing or Duplication of Exhibits A-1 and A-2 and B-1 and B-2.* You may (1) print these exhibits or (2) duplicate them photographically or by using photo-reproduction techniques, providing your printed or reproduced images are exactly like the ones in the exhibits. With the exception noted below, nothing can be changed.

.03 *EXCEPTION.* In Exhibit A-1 and A-2 you may change the areas containing "other" items (lines 2c, 9, 11b, 13, 15b, and 22) as follows: (1) the areas inside the perimeter of the boxes containing the dash-leaders (- - -) may be used to print any particular deduction item associated with the corresponding deduction category, and (2) the dash-leaders may be removed (but you may not change the amount column box size or position).

.04 *Exhibits A-1 and A-2.*

1 *Exhibit A-1.* This substitute Schedule A format may be used as a single sheet or as one of the copies of a snapset. It is designed to be used in place of the official Schedule A (Form 1040).

2 *Exhibit A-2.* This substitute Schedule A format may be used as a single sheet when both federal and state tax information is placed on the same form.

3 *No State Tax Information.* No state tax information can appear on these forms when filed with the Form 1040. The state column may be present but the *state tax information must not be visible* when filed with the Service. We prefer that the entire state column be *completely blocked out.*

.05 *BLOCK OUT METHODS.* A suggested method to block out the state tax information is: (1) place the substitute form in a clear plastic folder, (2) on the folder, place a strip of opaque material the exact width and length of the column you wish to block out, then (3) photocopy the substitute form while still in the folder. The result will be a form with only the federal tax information visible. Another method is to take a black marking pen and, using either vertical or horizontal strokes, cross out the state figures. Carbon-interleaved sets may be used where the amounts entered in the state column are filled in with black carbon overprint. This copy may be filed with the return.

.06 *Exhibits B-1 and B-2.* These exhibits correspond to Exhibits A-1 and A-2, and the provisions in .04.1 and 2 above apply. Both of these exhibits are acceptable for use in place of the official Schedule B (Form 1040).

.07 *Exhibits A-1 and B-1 or A-2 and B-2.* These exhibits may be used as sets when the return calls for both Schedule A and B.

1 Acceptable computer-generated formats for the schedules usually attached to the Form 1040 are shown in the Exhibits section of this revenue procedure. The exhibits are for Schedules A, B, C, D, E, F, G, R, SE and W. Schedule 1 (Form 1040A) is also included. All are acceptable substitutes for the official forms. They are intended to be used (without change) in place of the official forms and may be used without prior approval. All lines (including those not used for tax information) must be printed. (Any change to text or format of an exhibit requires prior written approval.) Vertical spacing is six (6) lines to the inch. You may also refer to them as examples of how the guidelines in this revenue procedure may be applied to the production of any substitute form.

2 A combination of upper and lower case print fonts is acceptable in producing the computer-generated exhibits included in this procedure.

SEC. 13. SPECIFICATIONS FOR FILING SUBSTITUTE SCHEDULES K-1

Prior approval is NOT required for a substitute Schedule K-1 that accompanies Form 1065 (for partnership), a Form 1120-S (for small business corporation), or a Form 1041 (for fiduciary) when the substitute Schedule K-1 meets all of the following requirements.

.01 The Schedule K-1 must contain the payer and recipient's name, address and SSN/EIN.

.02 The Schedule K-1 must contain all line items required for use by the taxpayer.

.03 The line items must be in the same order and arrangement as those on the official form.

.04 The line items must be numbered, titled, and/or captioned exactly as shown on the official form.

.05 Each taxpayer's information must be on a separate sheet of paper. Therefore, all continously printed substitutes must be separated, by taxpayer, before filing with the service.

.06 Schedules K-1 for recipients must have instructions for required line items attached.

.07 You may be subject to penalties if you file Schedules K-1 with the Service and furnish Schedules K-1 to partners, shareholders, or beneficiaries that do not conform to the specifications of this revenue procedure.

.08 The amount of each partner's, shareholder's, or beneficiary's share of each line item must be shown. The furnishing of a total amount for each line item and a percentage (or decimal equivalent) to be applied to such total amount by the partner, shareholder, or beneficiary does not satisfy the law and the specifications of this revenue procedure.

.09 If you file Schedules K-1 not conforming to the above specifications, the Service may consider these as not processable and return them to you to be filed correctly. You may also be subjected to the penalty as mentioned in .07 above.

SEC. 14. REQUIRED PREPARATION OF FORMS

.01 *Completely Fill In Lines.* You must completely fill in all the applicable numbered or reference lines on computer-prepared or generated forms (not just the totals) but all the items that make up the totals as well, before attaching any supporting statement (see Sec. 15 below for exceptions).

.02 *Service Processing of Forms.* The Service processes the return based on information entered on the official forms or approved substitutes. References are made to attachments only as required by law and as processing requirements direct. When you fail to complete all the pertinent lines on the official forms, Service Tax Examiners have to locate the information on your attachment and write it on the proper line of the official form. This time consuming process causes delays in processing the return and increases the potential for errors both in transcription and in interpretation.

.03 *Notification of Preparers.* The Service is continuing a program to notify preparers who fail to meet the requirement to completely fill in lines.

SEC. 15. EXCEPTIONS TO LINE COMPLETION REQUIREMENTS

.01 *Zero Entries.* Detailed information for any deduction or income category may be omitted from the printout if the category total to be reported is zero. However, the substitute form must show the total (zero when applicable) for each category. This means when no tax information is applicable, leave the line blank.

.02 *Lines Captioned "Other" (All Forms).* It is not necessary to fill in every numbered or referenced line of tax forms when the line caption calls for "Other," i.e., "Other (itemize)," "Other (specify)," "Other (attach schedule)," etc. Examples of this exception are lines 2c, 9, 11b, 13, 15b, 16 and 22 for Schedule A, Form 1040. When this occurs, you may use a supporting statement and enter only the total amount of these "Other" items on the line of the official form. However, we prefer that you use the space on the official form when it is adequate.

.03 *Schedule A (Form 1040).* All numbered and lettered lines must be filled in, if applicable. Supporting statements may be used to give the details of the totals entered on such lines but may not be used as a substitute for a collection of lines. For example, the detailed information for "Taxes" may not be shown on a supporting statement (supplemental schedule) and only line 10 filled in. Lines 6 through 9 must also be completed. Also, for example the details of "State and local income taxes" may be shown on a supporting statement and the total of such taxes entered on line 6. Also, the total of itemized deductions must be entered on line 24.

.04 *Schedule B (form 1040).* Lines 2 and 4 need not be filled in on the form. A supporting statement may be used for the details of interest and dividend income and the appropriate totals of such income entered on lines 3 and 5, unless nominee distribution or accrued interest criteria apply. (See the tax package instructions concerning interest and dividends).

.05 *Schedule C (Form 1040).* All lines must be filled in when applicable, except the line where "Other expenses-specify" is listed. (See instruction in .02 above).

.06 *Schedule E (Form 1040).*

1 When there are entries on page 1 for any of Part I, the following requirements must be met: (1) In Part I, lines 1 and 2, the questions must be answered and tax information must be entered on the lines provided for each property.

2 Supporting statements may be used for the details of rental and royalty income and expenses. The appropriate totals must be carried over and entered in the total column for lines 3, 10, 18, 19 and 22 through 26.

3 Part II (page 2)—The income and loss from various partnerships, estates or trusts, and small business corporations also may be detailed on a supporting statement, but the appropriate total income and total loss must be entered on lines 27 through 37.

4 As applicable, either page 1 or page 2 may be filed separately and independently of each other, as a valid Schedule E. Both pages are not required, unless the entered tax data applies to all parts of the form.

.07 *Schedule F (Form 1040).* If the cash method is used, only page one is needed. Otherwise both pages one and two must be entirely printed. Page two cannot be filed separately.

SEC. 16. SUPPORTING STATEMENTS

.01 *Use of Supporting Statements.* Supporting statements are to be used to explain an individual line entry on an official or substitute form. Unless specifically authorized by this revenue procedure (see Sec. 15), they must not be used to avoid completing required lines on the official form, or in lieu of a prescribed official schedule or form. Supporting statements are never to be used until the required official return or form they support are first totally filled in (completed). it is not acceptable to submit a blank or incomplete official form that refers to a supporting statement, and then to submit the form data entries solely on the statement, in lieu of completing a tax return or form.

.02 *Supporting Statements.* Supporting statements must: (1) provide details and explain entries made on the official form, (2) furnish all required information in the same sequence as called for on the official form, (3) furnish any additional information in the order of appearance on the form to which it refers, and (4) show taxpayer's name and social security number (SSN) or employer identification number (EIN), as applicable, and (5) clearly identify which official form it supports.

.03 *Cross-Reference.* Each supporting statement must be referenced to the form it supports, and the entry on the form must be cross-referenced to the supporting statement. For example, put "Statement X" on the top of the supporting statement that contains the identified line number and the supporting information, and put "See Statement X" on the line of the form that references the statement.

.04 *Extent of Use.* You may attach supporting statements to explain or support any line item on an official or approved substitute form.

.05 *Assemblage.* For filing purposes, supporting statements are not attached directly to their related forms. Rather, all supporting statements are assembled in the same sequence as the forms they support; they are then placed at the back of the form package, after the lettered and numbered forms (See Sec. 8.09).

.06 *Multiple Supporting Statements.* Supporting statements for each numbered or lettered tax form may be on one page or may be on multiple pages. But each numbered or lettered form must have a separate page for its supporting statement(s). Each page should be the size of the form it supports, or it may be 8" × 11" or 8½" × 11".

.07 *Not Reviewed for Approval.* The Service does not give its approval for specific supporting statements. The taxpayer or the tax practitioner for the taxpayer must meet the needs as they arise, using the guidelines in this revenue procedure.

SEC. 17. SPECIFICATIONS FOR FILING SUBSTITUTE FORMS

.01 *Filing Substitute Forms.* Follow the same instructions as for filing official forms. These instructions are in the taxpayer's tax package.

.02 *Computer-Prepared Tax Forms.* For filing purposes, the Service will accept computer-prepared tax returns (i.e., Forms 1040, 1040A, 1040EZ, 1120, 940, 941, etc.) filled in by a computer or by word-processing equipment or similar manual equipment, but these forms must be pre-printed.

.03 *Computer-Generated Forms.* For filing purposes, the Service will accept computer-generated versions of forms that are attached to individual and business income tax returns, provided the substitutes and their manner of completion meet the guidelines prescribed herein.

.04 *Combination of Manually Prepared and Computer-Prepared/Generated Forms.* For filing purposes, the Service will accept substitute tax forms that contain a combination of computer-prepared/generated and manually filled in information.

.05 *Taxpayer and Preparer Signatures.* All taxpayer signatures on forms to be filed with the Service must be original signatures, affixed subsequent to the reproduction process. However, the income tax preparer can satisfy the manual signature requirement by signing a completed income tax return form, making a photocopy of the return form, and having the taxpayer sign and file the photocopy. (See Rev. Rul. 78-370, 1978-2 C.B. 336.)

.06 *Use Preaddressed Label.* When filing substitute or reproduced forms, use the preaddressed label included in the tax package the Service sent to the taxpayer. Use of the label avoids larger processing costs because it reduces the potential for error—the kind of error which can delay the receipt of refund and information needed by the taxpayer, as well as significantly reducing the processing time for each return. No other label may be used. If taxpayer address is incorrect, line out old address and insert new address on the preaddressed label provided.

.07 *Use Internal Revenue Service Envelope.* When filing substitute or reproduced forms, use the envelope enclosed with the taxpayer's tax package. This envelope is coded for sorting into several categories. Use of the coded envelope can help speed up the processing and reduce processing costs. Do not use the Service-provided, tax-package envelope for other correspondence with the Service, as its misuse can delay the correspondence.

.08 *Voluntarily Submitted Information.* Additional information required or voluntarily submitted should be on the same size paper as the official form and attached to the return following the supporting statement. (See Sec. 8.09.)

SEC. 18. GUIDANCE FROM OTHER REVENUE PROCEDURES

.01 Guidance for the substitute tax forms not covered in this revenue procedure and the revenue procedures which govern their use, are as follows:

Form 1040-ES Revenue Procedure—82-7, 1982-1 C.B. 410, not reprinted for distribution

Form 1042S Revenue Procedure —81-28, 1981-2 C.B. 549; order as IRS Publication 1161.

Form W-2 series Revenue Procedure—84-44, 1984-1 C.B. 523, order as IRS Publication 1141.

Form 1099 series and Form 5498 Revenue Procedure—85-25, 1985-1 C.B. 558; order as IRS Publication 1179.

SEC. 19. ORDERING REVENUE PROCEDURES

.01 If you receive Package X, Informational Copies of Federal Tax Forms, you may use the Form 2333P, order Blank for Revenue Procedures, contained therein to order the following revenue procedures:

Pub. 1220, the revenue procedure on magnetic tape reporting for information returns (Forms 1099 series, 1098, 5498, 1096 and W-2G).

Pub. 1141, the revenue procedure on specifications for private printing of Forms W-2, W-2P, and W-3.

Pub. 1253, the revenue procedure on magnetic cassette/mini-disk reporting for information returns (Forms 1099, series, 1098, 5498, 1096 and W-2G).

Pub. 1255, the revenue procedure on magnetic diskette reporting for information returns (Forms 1099 series, 1098, 5498, 1096 and W-2G).

Pub. 1149, the revenue procedure on magnetic tape reporting for Windfall Profit Tax (Form 6248).

Pub. 1161, the revenue procedure on reprinted paper substitutes for Form 1042S.

Pub. 1162, the revenue procedure on group exemption procedures.

Pub. 1167, the revenue procedure on general substitute form requirements. (The controlling general procedure.)

Pub. 1179, the revenue procedure on paper substitute information returns (Forms 1099 series, 1098, 5498, 1096, W-2G and W-3G).

Pub. 1187 (and Pub. 1187 Supplement), the revenue procedures on magnetic tape reporting for Form 1042S.

.02 The above listed revenue procedures may be obtained also by writing to: Internal Revenue Service Publications, P.O. Box 25866, Richmond, VA 23260. Be sure to order using IRS Publication number.

SEC. 20. ORDERING REPRODUCTION PROOFS

.01 The Service provides for the public camera-ready, reproduction proofs of many of its printed tax forms. These reproduction proofs can only be ordered by using Form 6747, Order for Reproduction Proofs. Form 6747 can be obtained by written request to Internal Revenue Service, PM:S:FM:P, Attention: Reproduction Proof Coordinator, Room 1528, 1111 Constitution Ave., N.W., Washington, DC 20224.

1 Recorded forms distribution information is continuously available, and may be accessed by dialing 202-566-2473 or 2474 (not toll-free numbers). This recording provides for the receipt of form requests and inquiries at the end of the taped message.

.02 Basic specifications, such as margin, pagination, etc., will be printed in the margins of the reproduction proofs and must be removed before printing. The official reproduction proof margins across the top, bottom, and sides must be maintained on all reproductions and substitute forms.

.03 A charge of $1.00 per page will be made for each reproduction proof regardless of page size. After an order has been filled, invoices will be mailed to the requestor.

SEC. 21. AGREEMENT

Any person or company who uses substitute forms and makes all or part of the changes specified in this revenue procedure agrees to the following stipulation: The Service presumes the changes are made in accordance with these procedures and, as such, will be noninterruptive to the processing of the tax return. Should any of the changes prove to be not exactly as described, and as a result become disruptive to the Service during processing of the tax return, the person or company agrees to accept the determination of the Service whether or not the form may continue to be used during the filing season and also agrees to work with the Service in correcting noted deficiencies. Notification of deficiencies may be made by letter, phone call, or both.

SEC. 22 CONDITIONS—TAX FORMS (1040A, 1040EZ, 1040, 1120, 940, 941, Etc.)

.01 PROHIBITED FORMS.

1 COMPUTER-GENERATED VERSIONS.

Computer-generated versions of a tax return form (e.g. Form 1040, 1040EZ, 1040A, 1120, 940, 941, etc.) which requires a signature are not permitted. Only preprinted substitutes of these forms are allowed. Approval is extended to consider certain types of computer-generated graphic formats as acceptable "preprinted" substitutes. All such forms must have formal approval prior to their use.

2 COMPUTER-GENERATED GRAPHICS—First Time users

First-time users who design substitute forms using computer-graphics (e.g. laser printing, dot matrix addressable printing, etc.) must receive prior approval before using them. Exception: Experienced users who have previously received written approval from the Service for tax forms do not need written approval before using their forms. This assumes that all new requirements for the tax year have been fully complied with, based on actual comparison with final versions of the official Service tax forms. However, users are bound by the agreement in Sec. 21.

.02 FILL-IN INFORMATION.

The tax return form itself (i.e., 1040, 1040A, 1040EZ, 1120, 940, 941, etc) may be filled in by a computer printer or other similar automated equipment, but the form itself must be created beforehand (i.e., preprinted) using conventional printing methods, photocopying, computer-graphics (laser printing) or other similar reproduction processes.

.03 CHANGES PERMITTED TO THE FORMS 1040, 1040A & 1040EZ.

1 Certain changes (listed below) are permitted to the graphics of the form without prior approval, but these changes apply only to preprinted forms as described in .02 above.

2 Changes not requiring prior approval are good only for the annual filing period, January through December.

3 Other Changes Not Listed. All changes not listed here require prior approval from the Service BEFORE the form may be filed with the Service.

SEC. 23. CHANGES PERMITTED TO GRAPHICS (FORMS 1040A, 1040 AND 1040EZ).

Changes Permitted to the Graphics on Forms 1040, 1040A and 1040EZ and, Where Applicable, on Other Forms as Well for Use With Computer-Prepared (i.e. printed forms *Only*).

.01 *Adjustments.*

You may make minor vertical and horizontal spacing adjustments to allow for computer or word-processing printing. This includes widening the amount columns or tax entry areas so long as the adjustments do not exceed other provisions stated in revenue procedures. No prior approval is needed for these changes. However, the user of forms with such changes are bound by the "Agreement" in Section 21.

.02 *Name and Address Area.*

1 The horizontal rules and instructions within the name and address area may be removed and the entire area left blank; no line or instruction can remain in the area. However, the statement regarding use of the Service mail label should be retained.

2 The heavy ruled border (when present) that outlines the name and address area must not be removed, relocated, expanded or contracted.

3 Required Format

(a) When the name and address area is left blank, as provided in 1 above, the following format must be used when printing the taxpayer's name and address. Otherwise, unless the taxpayer's preprinted label is affixed over the information entered in this area, the lines must be filled-in as shown.

1st name line (35 characters maximum)

In-care-of name line (35 characters maximum)

Street address (35 characters maximum)

City, State (24 char. max.), one blank char., & zip (five char.)

(b) When there is no in-care-of name line, the name and address will consist of only three lines. Examples of the formats follow:

Example of name and address with no in-care-of name line:

JOHN AND MARY JONES
1234 ANYWHERE ST. APT 111
ANYTOWN, DC 12345

Example of name and address with in-care-of name line:

JOHN AND MARY JONES
C/O THOMAS A. JONES
4311 SOMEWHERE AVE.
SAMETOWN, DC 54321

(c) YOU MAY NOT USE YOUR OWN PREADDRESSED LABEL ON ANY INTERNAL REVENUE SERVICE FORM.

(d) The ONLY label that may be used is the OFFICIAL INTERNAL REVENUE SERVICE LABEL SUPPLIED to the taxpayer in his/her tax package. Please use the official Internal Revenue Service supplied label to help reduce errors, and to expedite Service input and processing of returns received.

(e) For identification purposes, you may computer print the taxpayer's name and address on the form and afterward affix the OFFICIAL INTERNAL REVENUE SERVICE SUPPLIED LABEL over the computer printed address. This applies whether or not the horizontal rules and the instructions have been removed from the address area.

.03 *Social Security Number (SSN) AND Employer Identification Number (EIN) Area.*

1 The vertical lines separating the format arrangement of the SSN/EIN may be removed.

2 When the vertical lines are removed, the SSN and EIN formats must be 000-00-0000 or 00-0000000, respectively.

.04 *Cents Columns.*

1 You may remove the vertical rule that separates dollars from the cents.

2 All entries in the amount column should have a decimal point following the whole dollar amounts whether or not the vertical line that separates the dollars from the cents is present.

3 You may omit printing the cents, but all amounts entered on the form must follow a consistent format. You are strongly urged to round off the figures to whole dollar amounts, following the official return instructions.

4 When printing money amounts, you must use one of the following ten-character formats: (a) 0,000,000. (b) 000,000.00

5 When there is no entry for a line, leave the line blank.

.05 *"Paid Preparer's Use Only" Area.*

1 On all forms, where present, the paid preparer's information area may not be rearranged or relocated.

2 You may add three lines and remove the horizontal rules in the preparer's address area.

3 Form 1040EZ preparers must sign the return and provide all other required information. This information should be provided at the bottom of the form below the taxpayer's signature area. (See Section 8.)

SEC. 24. CHANGES PERMITTED TO FORM 1040A GRAPHICS

No prior approval is needed for the following changes (for use with computer-prepared forms only):

.01 *Line 4.*

The line caption may be compressed vertically to one line (to allow for same line entry for the name of the qualifying unmarried child) by using the following caption:

"Head of household; unmarried child's name. . . ." name field

.02 *Line 5c.*

To allow for a two-line field for printing dependent children's names, you may shorten the caption to:

"Dep. children" (names field)
(names field)

.03 *Line 5e.*

1 The number of lines for listing "other dependents" may be expanded to a maximum of 5.

2 Column captions may be shortened to one line descriptions.

.04 *Other Lines.*

Any line whose caption takes up two or more vertical lines may be compressed to one line by using contractions, etc., and by removing instructional references.

.05 *Page 2 (Form 1040A)*

All lines must be present and numbered in the order shown on the official form.

SEC. 25. OTHER CHANGES PROHIBITED

No other changes to the Form 1040A graphics are allowed without prior approval.

SEC. 26. CHANGES PERMITTED TO THE FORM 1040 GRAPHICS

No prior approval is needed for the following changes (for use with computer-prepared forms only):

.01 *Line 4.* This line may be compressed horizontally (to allow for a larger entry area for the name of the qualifying unmarried child) by using the following caption:

"Head of Household; unmarried child's name" (name field)

.02 *Line 6e.*

1 The vertical lines separating columns (1) through (5) may be removed. The captions may be shortened to allow a one-line caption for each column.

2 The number of lines for listing "other dependents" may be expanded to a maximum of 5 by compressing other noted areas and lines.

.03 *Other Lines.*

Any other line whose caption takes up two or more vertical lines may be compressed to one line by using contractions, etc., and by removing instructional references.

.04 *Line 22*

1 This line may be expanded vertically to a maximum of 3 lines.

2 The amount entry box must remain a single entry and the cross hatched shading must extend down the numbered line box to the same number of lines you add.

.05 *Line 38*. You may change the line caption to read "Tax" and computer-print either the words "FROM TAX TABLES:" OR "FROM SCHEDULE/*FORM*" and computer-print the appropriate text.

.06 *LINE 39*. You may change the caption to read: "Additional taxes from Form" and computer-print only the form(s) that apply.

SEC. 27. OTHER CHANGES PROHIBITED

No other changes to the Form 1040 graphics are permitted without prior approval.

SEC. 28. ACCEPTABLE FORMATS OF COMPUTER-GENERATED FORMS AND SCHEDULES

1 Exhibits of acceptable computer-generated formats for the schedules usually attached to the Form 1040 are shown in the Exhibits section of this revenue procedure.

2 Use of Acceptable Formats. If your computer-generated forms appear exactly like the exhibits, no prior authorization is needed.

3 Changes to exhibits are not permitted without prior approval. Any change to the text or format of any of the exhibits requires prior written approval.

SEC. 29. COMPUTER-GENERATED FORMS NOT SHOWN AS EXHIBITS IN THIS REVENUE PROCEDURE

.01 Those desiring to computer-generate forms not shown here may do so, but they must design such forms themselves by following the manner and style of those in the Exhibits section of this publication, and by taking care to observe other requirements and conditions stated here.

.02 Computer-generated forms so designed do not require prior approval from the Service. However, the user of such forms is bound by the "Agreement" in Sec. 21 above.

.03 If you wish, you may submit any substitute form to the Service for approval consideration, or you may submit only a representative sample of your forms.

SEC. 30. INSTRUCTIONS FOR PREPARING COMPUTER-GENERATED SUBSTITUTES

.01 *Format Arrangement.*

The format of each substitute schedule or form must follow the format of the official schedule or form as to item captions, line references, line numbers, sequence, form arrangement and format, etc. Basically try to make the form look like the official one, with readability and consistency being primary factors. Use periods and/or other special characters to separate the various parts and sections of the form. With the exceptions in .02 below, all line numbers and items must be printed even though an amount is not entered on the line.

.02 *Line Numbers.*

1 When a line on an official form is designated by a number or a letter, that designation (reference code) must be used on a substitute form.

2 The reference code must be printed to the left of the corresponding captioned line and also immediately preceding the data entry field even if there is no reference code immediately preceding the data entry field on the official form.

3 In addition, the reference code that is immediately before the data field must either be followed by a period or enclosed in parentheses. There also must be at least two blank spaces between the period or the right parentheses and the first digit of the data field. (See example below.)

4 A decimal point (i.e., a period) should be used for each money amount regardless of whether the amount is reported in dollars and cents or in whole dollars, or whether or not the vertical line that separates the dollars from the cents is present. The decimal points must be vertically alligned when possible.

Example:

7	REAL ESTATE ...	7.	495.00
8A	GENERAL SALES	8A.	
8B	GEN SALES MOTOR VEH ..	8B.	198.00

or

7	REAL ESTATE ..	(7)	495.00
8A	GENERAL SALES	(8A)	
8B	GEN SALES MOTOR VEH ..	(8B)	198.00

.03 *Multiple Page Forms.* With the exceptions noted below, when printing multiple page forms the entire form with all its parts and pages must be printed. When printed on continuous forms, they must be burst and pin-feed holes removed before filing with the return.

.04 *Exception to Forms that must be entirely printed in whole or in part.*

1 On Schedule F, depending on which accounting method is used (cash or accrual), the following will apply. If the cash accounting method is used, only page one of Schedule F needs to be printed. Otherwise, both page one and two must be entirely printed. Page two cannot be filed separately.

2 On Schedule E, it is not necessary to print both pages if data does not apply. Either page one or page two can be printed and filed separately.

SEC. 31. ADDITIONAL INSTRUCTIONS FOR ALL FORMS

.01 Internal control numbers and identifying symbols of the computer preparer may be shown on the substitute, if the use of such numbers or symbols is acceptable to the taxpayer and the taxpayer's representative. If shown, such information must not be printed in the top one-half inch clear area, from the center to the right edge, of any form or schedule requiring a signature. With the exception of the actual tax return form (i.e. Forms 1040, 1120, 940, 941, etc.), you may also print in the left vertical and bottom left margins. The bottom left margin you may use extends 3 1/2 inches from the left edge of the form. (See Sec. 11 for more information on this subject.)

.02 Descriptions for captions, lines, etc., appearing on the substitute forms may be limited to one print line by using abbreviations and contractions and by omitting articles, prepositions, etc. However, sufficient key words must be retained to permit ready identification of the caption, line or item.

1 Explanatory detail and/or intermediate calculations for derivation of fine line totals, may be included on the substitute. We prefer that such calculations be submitted in the form of a supporting statement. If intermediate calculations are included on the substitute, the line on which they appear may not be numbered or lettered. Intermediate calculations may not be printed in the right column. This column is reserved for official numbered and lettered lines that correspond to the ones on the official form. If a supporting statement is submitted, intermediate calculations or subtotals may be formatted at the preparer's option.

2 Text prescribed for the official form, which is solely instructional in nature, e.g., "Attach this schedule to Form 1040," "See instructions," etc., may be omitted from the substitute form.

3 Information for more than one schedule or form may not be shown on the same printout page. Except for high volume computer-generated Schedules A and B (Form 1040), almost any form may be continued on two or more pages if necessary. When a form is continued on two or more pages, clearly identify at the bottom of each page, including page 1, that is continued, e.g., "Page 1, Schedule C Continued." It is strongly recommended that a substitute form not exceed the same number of pages used for the official form.

(a) Both sides of the paper may be printed for multiple page official forms; but it is unacceptable to intermix single page schedules or forms, except for Schedules A and B which are printed back to back by the Service. For example Schedule E can be printed on both sides of the paper, because the official form is multiple page, with page two continued on the back. However, for example do not print Schedule G on the front page and Schedule SE on the back, or Schedule A on the front and Form 3903 on the back, etc.). Both pages of a substitute form must match the official form version it represents

4 Identify all computer-prepared substitutes clearly; print the form designation one-half inch from the top margin and one and one-half inches from the left margin; print the title centered on the first line of print; and print the taxable year and, where applicable, the sequence number on the same line one-half to one inch from right margin. Include the taxpayer's name and SSN on all forms and attachments. Also print the OMB number and (when applicable) the form's expiration date, as reflected on the official form.

5 The state tax column may be present, but the state tax information must NOT be visible on the copy filed with the Service. When a form is designed with both federal and state columns, the federal column must be to the left

of the state column and adjacent to the line caption.

6 Attach all payments (check or money order, no cash) to the front of the tax return.

7 Negative (or loss) monetary amount entries should be enclosed in brackets, or signed minus, to assist in the accurate computation and input of form data. On many official forms the Service pre-prints brackets in selected negative data fields, and those designations should be retained or inserted on affected substitute forms.

SEC. 32. FILING SUBSTITUTE FORMS WITH THE SERVICE

Follow the same instructions as for filing official forms. These instructions are in the taxpayer's tax package.

SEC. 33. SPECIAL FORM 1040EZ OPTICAL CHARACTER RECOGNITION (OCR) REQUIREMENTS

.01 The Form 1040EZ is designed in OCR format. The Service has the capability to machine read this form by optical character recognition (OCR) equipment (Scan-Optics-System 540).

.02 It is optional to produce the 1040EZ substitute as a normal (black and white) reproduction, or as an actual OCR version. The following criteria apply if the form is to be OCR scannable. Otherwise, you may print this form under the previous general guidelines of this Revenue procedure.

.03 An acceptable substitute OCR Form 1040EZ must generally be an exact replica of the official OCR reproduction proof with respect to layout, content, and required OCR characteristics.

.04 The specific paper requirements which must be met for the development of substitute (privately printed) forms include the following:

1 Color and quality of paper—Paper must be white, OCR grade bond, with no flourescent additives or water marks, and with zero rag content.

2 Reflectivity of paper—Must be 80% or greater.

3 Opacity—The paper opacity ratio must be 80% or more.

4 Paper Weight—Specified paper weight is 20 lb. OCR bond (.0035″).

5 Dirt—Must not exceed 10 parts per million.

6 Finish (smoothness)—Must be between 90 and 160 units (Sheffield).

7 Porosity—Paper should have a Gurley reading between 15 and 95.

8 Gloss—Paper with shiny or lustrous appearance (glossy) should be avoided.

9 Size—Form trim size must be 8″ × 11″.

.05 The specific ink requirements which must be met for this form include the following:

1 Print Color—The face of the form prints in black and green, the back prints in black only.

2 Ink—Green ink used must be highly reflective OCR type, such as Sinclair and Valentine J-27975, or an exact match. Black ink used must be non-reflective.

3 Face Registration—Black to green must be .02″ (plus or minus) both horizontally and vertically.

4 Face Screen—Forms contain a green screened background equal to a 15% tone of a 110-line screen. Follow registration marks on repro-proof for screen positioning. Handprint boxes are included on Page 1 of the reproduction proof and should be printed as a 50% value of the recommended OCR green ink. Inks used for handprint boxes must reflect at least 90% of the background on which it is printed as measured in the visible range.

5 Face Margins—Approximately 2/6″ head from top trimmed edge to screen (½″ to black image). ⅙″ outside from trimmed edges to screen. Exact margins are provided with reproduction proofs.

6 Back Margins—½″ head, 5/16″ foot, and 5/16″ sides.

.06 *Typography*—Type must be substantially identical in both size and shape with corresponding type on the official form reproduction proof.

.07 To assure proper alignment and position of hand-printed characters representing return lines 1 through 11 tax data, they must be hand printed (entered) into the pre-printed amount field boxes on the form. A #2 lead wooden pencil is recommended as the writing tool which will consistently provide the required stroke width and print contrast on entered characters.

.08 Reading of handprinted characters requires adherance to the following techniques.

1 Enter numeric amount digits carefully and clearly. Fill at least ⅔ of the individual character box height, keeping the character within the box with no overlapping or touching characters. Specific required digit constraints are shown below.

2 When entering "fours", keep the top open.

3 When entering "one", do not use serifs.

4 When entering "twos", do not add extra loops.

5 All character lines must be connected, with no gaps.

.09 *Use Taxpayer's Preaddressed Label.* Reproduced OCR Forms 1040EZ must have ONLY the taxpayer's preaddressed label affixed to be processable as an OCR document. Substitute labels and handwritten name/address information is not acceptable.

.10 All the general and detailed provisions of this Revenue Procedure apply (in addition to this specific OCR Section) for the development of substitute OCR Forms 1040EZ.

SEC. 34. SPECIAL FORM 1120A OPTICAL CHARACTER RECOGNITION (OCR) REQUIREMENTS

.01 Form 1102A has been developed and designed in OCR format. This return will be read by Optical Character Recognition (OCR) equipment (Recognition Equipment Inc.—Input 80 Model B Scanner), if submitted in acceptable OCR format.

.02 It is optional to produce the 1120A substitute as a normal (black and white) reproduction, or as an OCR scannable version. The following specific criteria apply if the substitute form is to be produced for OCR processing. Otherwise, you may print this form under the general guidelines of this Revenue Procedure.

.03 An acceptable substitute OCR Form 1120A must be an exact replica of the official reproduction proof with respect to layout, content, and required OCR characteristics.

.04 The specific paper requirements for this form generally duplicate those specified in Section 33, with the following exception:

1. Size—Form 1120A trim size must be 8½″ × 11″.

.05 The specific ink requirements which must be met for this form include the following.

1 Print Color—Black and maroon.

2 Ink—Maroon ink must be highly reflective OCR type, such as Sinclair and Valentine J-31859, or an exact match. Black ink must be non-reflective.

3 Face Registration—Black to maroon must be 0.015 (1/64)″ (plus or minus) both horizontally and vertically.

4 Handprint Boxes—These handprint boxes (for IRS entries and use only) are included on Page 2 of the reproduction proof, and should be printed as a 50% screen value of the recommended OCR maroon ink. Inks used for handprint boxes must measure .19 PCS or less when tested using MacBeth PCM-II tester 'C' scale.

5 Face margins—Minimum margins require 11 2/6″ head, ½″ left and right, and 5/16″ foot.

6 Back margins—11 2/6″ head, ½″ left and right, and 5/16″ foot. Exact margins are provided with reproduction proofs.

.06 *Typography*—Type must be substantially identical in both size and shape with corresponding type on the official form reproduction proof.

.07 All entries on an OCR Form 1120A must be either typed or machine printed, to permit OCR scanning. Otherwise the return will be manually processed.

.08 *Use Taxpayer's Preaddressed Label.* Reproduced OCR Forms 1120A must have the taxpayer's preaddressed label affixed or must be typed or machine printed to be processable as an OCR document. Substitute labels and handwritten name/address information is not acceptable.

.09 All general and detailed provisions of this revenue Procedure apply (in addition to this specific OCR Section) for the development of substitute OCR Forms 1120A.

SEC. 35. SPECIAL FORM 941 AND 942 OPTICAL CHARACTER RECOGNITION (OCR) REQUIREMENTS

.01 Forms 941 and 942 are designed in OCR format. The Service has the capability to machine read these forms by Optical Character Recognition (OCR) equipment (Recognition Equipment Inc—Input 80 Model B Scanner), if submitted in acceptable OCR format.

.02 It is optional to produce the Forms 941 and 942 (all four quarters of 1986) as a black and white reproduction, or as an OCR scannable version. However, effective with the 1987 tax returns, it is requested that you produce the returns in only scannable format. The following specific criteria applies if the substitute form is to be produced for OCR processing. Otherwise, you may print these forms under the general guidelines of this Revenue Procedure.

.03 An acceptable substitute OCR Form 941 or 942 must be an exact replica of the official reproduction proof with respect to layout, content, and required OCR characteristics.

.04 The specific paper requirements which must be met for the development of substitute (privately printed) forms generally duplicate those specified in section 33, with the following exception:

1 Size—Forms 941 and 942 trim size must be 8½″ × 11″.

.05 The specific ink requirements which must be met for these forms include the following:

1 Print Color—Black and Maroon.

2 Ink—Maroon ink must be a highly reflective (not less than 85%) OCR type ink, such as Sinclair/Valentine J31859, or an exact match. Black ink reflectance must not be greater than 15%.

3 Handprint Boxes—These handprint boxes (for IRS entries and use only) are included on the reproduction proof, and should be printed as a 50% screen value of the recommended OCR maroon ink. Inks used for handprint boxes must measure 15% or less when tested using the MacBeth or Kidder testers (see #5 below).

4 Face Margins—Minimum margins require ½″ head; center sides'; and, 5/16″ foot.

5 Testers—The following two print testers may be used for Forms 941 and 942. Any other type tester must first be approved by the IRS.

(a) MacBeth PCM-II

Use 'C' scale. Range must be between .13 minimum to .19 maximum.

(b) Kidder 082 A

Use infrared scale. PSC values must fall in the range of .32 minimum to .38 maximum. White calibration disk must be set at 100%. Sensitivity must be set at "1".

SEC. 36 EFFECT ON OTHER DOCUMENTS

This revenue procedure supersedes Revenue Procedure 85-3, 1985—1 C.B. 459.

Exhibit A-1 (Preferred Format)

SCHEDULE A
(Form 1040)
Department of the Treasury
Internal Revenue Service

Substitute Schedule A
Itemized Deductions

OMB No. 1545-0074
1985
07

Name(s) as shown on Form 1040

Your social security number

Medical and Dental Expenses	1	Prescription medicines and drugs; and insulin	1	
	2 a	Doctors, dentists, nurses, hospitals, insurance premiums you paid for medical and dental care, etc.	2a	
	b	Transportation and lodging	2b	
	c	Other (list—include hearing aids, dentures, eyeglasses, etc.) ▶	2c	
	3	Add lines 1 through 2c, and write the total here	3	
	4	Multiply the amount on Form 1040, line 33, by 5% (.05)	4	
	5	Subtract line 4 from line 3. If zero or less, write -0-. **Total medical and dental** . ▶		5
Taxes You Paid	6	State and local income taxes	6	
	7	Real estate taxes	7	
	8 a	General sales tax (see sales tax tables in instruction booklet)	8a	
	b	General sales tax on motor vehicles	8b	
	9	Other taxes (list—include personal property taxes) ▶	9	
	10	Add the amounts on lines 6 through 9. Write the total here. **Total taxes** . ▶		10
Interest You Paid	11 a	Home mortgage interest you paid to financial institutions	11a	
	b	Home mortgage interest you paid to individuals (show that person's name and address) ▶	11b	
	12	Total credit card and charge account interest you paid	12	
	13	Other interest you paid (list) ▶	13	
	14	Add the amounts on lines 11a through 13. Write the total here. **Total interest** . ▶		14
Contributions You Made	15 a	Cash contributions. (If you gave $3,000 or more to any one organization, report those contributions on line 15b.)	15a	
	b	Cash contributions totaling $3,000 or more to any one organization. (Show to whom you gave and how much you gave.) ▶	15b	
	16	Other than cash (You must attach Form 8283 if over $500.)	16	
	17	Carryover from prior year	17	
	18	Add the amounts on lines 15a through 17. Write the total here. **Total contributions** . ▶		18
Casualty and Theft Losses	19	Total casualty or theft loss(es). (You must attach Form 4684 or similar statement.) (see page 21 of Instructions) ▶		19
Miscellaneous Deductions	20	Union and professional dues	20	
	21	Tax return preparation fee	21	
	22	Other (list type and amount) ▶	22	
	23	Add the amounts on lines 20 through 22. Write the total here. **Total miscellaneous** . ▶		23
Summary of Itemized Deductions	24	Add the amounts on lines 5, 10, 14, 18, 19, and 23. Write your answer here.		24
	25	If you checked Form 1040 { Filing Status box 2 or 5, write $3,540 Filing Status box 1 or 4, write $2,390 Filing Status box 3, write $1,770 }		25
	26	Subtract line 25 from line 24. Write your answer here and on Form 1040, line 34a. (If line 25 is more than line 24, see the Instructions for line 26 on page 22.) . . . ▶		26

For Paperwork Reduction Act Notice, see Form 1040 Instructions.

Schedule A (Form 1040) 1985

Exhibit A-2 (Acceptable Format)

(Form 1040)
Department of the Treasury
Internal Revenue Service

Substitute Schedule A Itemized Deductions

OMB No. 1545-0074
1985
07

Name(s) as shown on Form 1040	Your social security number

Medical and Dental Expenses	1	Prescription medicines and drugs; and insulin	1		
	2 a	Doctors, dentists, nurses, hospitals, insurance premiums you paid for medical and dental care, etc.	2a		
	b	Transportation and lodging	2b		
	c	Other (list—include hearing aids, dentures, eyeglasses, etc.) ▶	2c		
	3	Add lines 1 through 2c, and write the total here	3		
	4	Multiply the amount on Form 1040, line 33, by 5% (.05)	4		
	5	Subtract line 4 from line 3. If zero or less, write -0-	5		
Taxes You Paid	6	State and local income taxes	6		
	7	Real estate taxes	7		
	8 a	General sales tax (see sales tax tables in instruction booklet)	8a		
	b	General sales tax on motor vehicles	8b		
	9	Other taxes (list—include personal property taxes) ▶	9		
	10	Add the amounts on lines 6 through 9. Write the total here	10		
Interest You Paid	11 a	Home mortgage interest you paid to financial institutions	11a		
	b	Home mortgage interest you paid to individuals (show that person's name and address) ▶	11b		
	12	Total credit card and charge account interest you paid	12		
	13	Other interest you paid (list) ▶	13		
	14	Add the amounts on lines 11a through 13. Write the total here	14		
Contributions You Made	15 a	Cash contributions. (If you gave $3,000 or more to any one organization, report those contributions on line 15b.)	15a		
	b	Cash contributions totaling $3,000 or more to any one organization. (Show to whom you gave and how much you gave.) ▶	15b		
	16	Other than cash. (You must attach Form 8283 if over $500.)	16		
	17	Carryover from prior year	17		
	18	Add the amounts on lines 15a through 17. Write the total here	18		
Casualty and Theft Losses	19	Total casualty or theft loss(es). (You must attach Form 4684 or similar statement.) (see page 21 of Instructions)	19		
Miscellaneous Deductions	20	Union and professional dues	20		
	21	Tax return preparation fee	21		
	22	Other (list type and amount) ▶	22		
	23	Add the amounts on lines 20 through 22. Write the total here	23		
Summary of Itemized Deductions	24	Add the amounts on lines 5, 10, 14, 18, 19, and 23	24		
	25	If you checked Form 1040 { Filing Status box 2 or 5, write $3,540 Filing Status box 1 or 4, write $2,390 Filing Status box 3, write $1,770 }	25		
	26	Subtract line 25 from line 24. Write your answer here and on Form 1040, line 34a.	26		

For Paperwork Reduction Act Notice, see Form 1040 Instructions.

Schedule A (Form 1040) 1985

Exhibit B-1 (Preferred Format)

Schedules A&B (Form 1040) 1985

Substitute Schedule B
Interest and Dividend Income

08 OMB No. 1545-0074 Page 2

Name(s) as shown on Form 1040

Your social security number

Part I Interest Income

If you received more than $400 in interest income, you must complete Part I and list ALL interest received. If you received interest as a nominee for another, or you received or paid accrued interest on securities transferred between interest payment dates, see page 22.

Interest income		Amount	
1 Interest income from seller-financed mortgages. (See Instructions and show name of payer.) ▶	1		
2 Other interest income (list name of payer) ▶	2		
3 Add the amounts on lines 1 and 2. Write the total here and on Form 1040, line 8 ▶	3		

Part II Dividend Income

If you received more than $400 in gross dividends and other distributions on stock, or you are electing to exclude qualified reinvested dividends from a public utility, complete Part II. If you received dividends as a nominee for another, see page 22.

Dividend income			Amount	
4 Dividend income (list name of payer—include on line 4 capital gain distributions, nontaxable distributions, etc.) ▶		4		
5 Add the amounts on line 4. Write the total here		5		
6 Capital gain distributions. Enter here and on line 15, Schedule D.*	6		▨	▨
7 Nontaxable distributions. (See Schedule D Instructions for adjustment to basis.)	7		▨	▨
8 Exclusion of qualified reinvested dividends from a public utility. (See page 23 of Instructions.)	8		▨	▨
9 Add the amounts on lines 6, 7, and 8. Write the total here		9		
10 Subtract line 9 from line 5. Write the result here and on Form 1040, line 9a ▶		10		

**If you received capital gain distributions for the year and you do not need Schedule D to report any other gains or losses, do not file that schedule. Instead, enter 40% of your capital gain distributions on Form 1040, line 14.*

Part III Foreign Accounts and Foreign Trusts

If you received more than $400 of interest or dividends, OR if you had a foreign account or were a grantor of, or a transferor to, a foreign trust, you must answer both questions in Part III.	**Yes**	**No**
11 At any time during the tax year, did you have an interest in or a signature or other authority over a financial account in a foreign country (such as a bank account, securities account, or other financial account)? (See page 23 of the Instructions for exceptions and filing requirements for Form TD F 90-22.1.)		
If "Yes," write the name of the foreign country ▶	▨	▨
12 Were you the grantor of, or transferor to, a foreign trust which existed during the current tax year, whether or not you have any beneficial interest in it? If "Yes," you may have to file Forms 3520, 3520-A, or 926.		

For Paperwork Reduction Act Notice, see Form 1040 Instructions.

Schedule B (Form 1040) 1985

Exhibit B-2 (Acceptable Format)

(Form 1040)
Department of the Treasury
Internal Revenue Service

Substitute Schedule B
Interest and Dividend Income

OMB No. 1545-0074
1985
08

Name(s) as shown on Form 1040

Your social security number

Part I.—Interest Income

Interest income		Federal
1 Interest income from seller-financed mortgages. (See Instructions and show name of payer.) ▶	1	
2 Other interest income (list name of payer) ▶	2	
....		
....		
....		
....		
....		
....		
....		
....		
....		
....		
....		
....		
....		
....		
3 Add the amounts on lines 1 and 2. Write the total here and on Form 1040, line 8 ▶	3	

Part II.—Dividend Income

Dividend income		Amount
4 Dividend income (list name of payer) ▶	4	
....		
....		
....		
....		
....		
....		
....		
....		
....		
....		
....		
....		
....		
5 Add the amounts on line 4. Write the total here	5	
6 Capital gain distributions. Enter here and on line 15, Schedule D.*	6	
7 Nontaxable distributions. (See Schedule D Instructions for adjustment to basis.)	7	
8 Exclusion of qualified reinvested dividends from a public utility. (See page 23 of Instructions.)	8	
9 Add the amounts on lines 6, 7, and 8. Write the total here .	9	
10 Subtract line 9 from line 5. Write the result here and on Form 1040, line 9a . . ▶	10	

Part III.—Foreign Accounts and Foreign Trusts

	Yes	No
11 At any time during the tax year, did you have an interest in or a signature or other authority over a financial account in a foreign country (such as a bank account, securities account, or other financial account)? (See page 23 of the Instructions for exceptions and filing requirements for Form TD F 90-22.1.) . . . . If "Yes," write the name of the foreign country ▶		
12 Were you the grantor of, or transferor to, a foreign trust which existed during the current tax year, whether or not you have any beneficial interest in it? If "Yes," you may have to file Forms 3520, 3520-A, or 926		

For Paperwork Reduction Act Notice, see Form 1040 Instructions.

Schedule B (Form 1040) 1985

EXHIBIT CG - 1 (SCHEDULE 1 - PAGE 1)

SCHEDULE 1 INCOME AND DEDUCTIONS 1985
(FORM 1040A) OMB NO. 1545-0085
JOHN Q. AND MARY J. TAXPAYER SSN 000-00-0000

****

PART I DEDUCTION FOR MARRIED WORKING COUPLE

		(A) SELF		(B) SPOUSE
1.	WAGES, SALARIES, TIPS, ETC.	1. 000,000.00		000,000.00
2.	IRA DEDUCTION	2.		
3.	LN 1 MINUS LN 2	3. 000,000.00		
4.	SMALLER OF LN 3(A) OR 3(B)	XXXXXXXXXX	4.	000,000.00
5.	MULTIPLY LN 4 BY 10%	XXXXXXXXXX	5.	X.10
6.	DEDUCTION (TO FM 1040A, LN 12)	XXXXXXXXXX	6.	000,000.00

****

PART II CHILD AND DEPENDENT CARE CREDIT

1.	NO. OF QUALIFYING PERSONS CARED FOR IN 1985		1.	XXX
2.	1985 EXPENSES INCURRED (MAX $2,400/$4,800)		2.	0,000.00
3.	EARNED INCOME IF UNMARRIED, OR			
	A. EARNED INCOME	3A 000,000.00		
	B. SPOUSE EARNED INCOME	3B 000,000.00		
	C. SMALLER OF LN 3A or 3B		3C.	000,000.00
4.	SMALLER OF LN 2 or 3C		4.	
5.	TABLE PERCENTAGE APPLIED TO LN 15		5.	X.XX
6.	MULTIPLY LN 4 BY LN 5 (TO FM 1040A, LN 21A)		6.	000,000.00

```
EXHIBIT CG-1 (SCHEDULE 1 - PAGE 2)
                                                              1985
SCHEDULE 1 (CON'T)PAGE 2                          OMB NO. 1545-0085
(FORM 1040A)
                                                    SSN  000-00-0000
JOHN Q. AND MARY J. TAXPAYER
**********************************************************************
PART III INTEREST INCOME                         AMOUNT
1.  PAYERS (LIST)                              00,000.00
(1ST PAYER) (2ND PAYER) (3RD PAYER)                         2.  000,000.00
2.  TOTAL OF LINE 1 (TO FM 1040A, LN 7)
**********************************************************************
PART IV DIVIDEND INCOME                          AMOUNT
1.  PAYERS (LIST)                              00,000.00
(1ST PAYER) (2ND PAYER)(3RD PAYER)                          2.  000,000.00
2.  TOTAL OF LINE 1 (TO FM 1040A, LN 8A)
```

EXHIBIT CG - A (SCHEDULE A)

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SCHEDULE A (FORM 1040)            ITEMIZED DEDUCTIONS                 1985 * 07
                                                          OMB NO. 1545-0074
JOHN Q. & MARY J. TAXPAYER                                            SSN 000-00-0000
**MEDICAL AND DENTAL EXPENSES*************************************************
  1  MEDICINE AND DRUGS.........................................1.      00,000.00
  2  A DOCTORS, DENTISTS, NURSES, HOSPITALS, ETC..................2A.
     B TRANSPORTATION...........................................2B.
     C OTHER (LIST)
       1st
       2nd - OR SEE STATEMENT XX................................2C.
  3  ADD LINES 1 THRU 2C........................................3.
  4  5% OF LINE 33, FORM 1040...................................4.
  5  SUBTRACT LN. 4 FROM LN. 3 (OR ZERO)........................5.
**TAXES***********************************************************************
  6  STATE AND LOCAL INCOME..................................... 6.
  7  REAL ESTATE................................................ 7.
 8A  GENERAL SALES..............................................8A.
  B  GENERAL SALES ON MOTOR VEHICLES............................8B.
  9  OTHER (LIST) - 1ST
     2ND - OR SEE STATEMENT XX..................................9.
 10  ADD LINES 6 THRU 9.........................................10.
**INTEREST EXPENSE************************************************************
11A  HOME MORTGAGE INTEREST TO FINANCIAL INSTITUTIONS..........11A.
  B  HOME MORTGAGE INTEREST TO INDIVIDUALS (LIST)- 1st
     2nd OR SEE STATEMENT XX...................................11B.
 12  CREDIT CARDS AND CHARGE ACCOUNT INT........................12.
 13  OTHER (LIST) - 1st
     2nd
     3rd - OR SEE STATEMENT XX..................................13.
 14  ADD LINES 11A THRU 13......................................14.
**CONTRIBUTIONS***************************************************************
15A  CASH CONTRIBUTIONS UNDER $3,000...........................15A.
  B  CASH CONTRIBUTIONS OF $3,000 AND OVER (LIST)
     1st
     2nd OR SEE STATEMENT XX...................................15B.
 16  OTHER THAN CASH............................................16.
 17  CARRYOVER FROM PRIOR YEARS.................................17.
 18  ADD LINES 15A THRU 17......................................18.
**CASUALTY AND THEFT LOSSES***************************************************
 19  TOTAL CASUALTY/THEFT LOSSES FROM FORM 4684.................19.
**MISCELLANEOUS DEDUCTIONS****************************************************
 20  UNION AND PROFESSIONAL DUES................................20.
 21  TAX RETURN PREPARATION FEE.................................21.
 22  OTHER (LIST) 1st
     2nd
     3rd - OR SEE STATEMENT XX..................................22.
 23  ADD LINES 20 THRU 22.......................................23.
**SUMMARY OF ITEMIZED DEDUCTIONS**********************************************
 24  ADD LINES 5, 10, 14, 18, 19 AND 23.........................24.
 25  FILING STATUS ZERO BRACKET AMOUNT..........................25.
 26  SUBTRACT LINE 25 FROM LINE 24..............................26.      00,000.00
     FOR PAPERWORK REDUCTION ACT NOTICE, SEE SEPARATE INSTRUCTIONS
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EXHIBIT CG - B (SCHEDULE B)

```
                                                              1985  *08
SCHEDULE B (FORM 1040) INTEREST AND DIVIDEND INCOME    OMB NO. 1545-0074
                                                         SSN 000-00-0000
JOHN Q. & MARY J. TAXPAYER
*************************************************************************
PART I  INTEREST INCOME                                         AMOUNT
 1.  INTEREST INCOME FROM SELLER FINANCED MORTGAGE        1.  00,000.00
     NAME OF PAYER                                        2.  00,000.00
 2.  OTHER INTEREST INCOME (LIST)
     (1st PAYER) (2nd PAYER) (3rd PAYER) (4th PAYER)
 3.  ADD LINES 1 AND 2.....................................3.  00,000.00
*************************************************************************
PART II DIVIDEND INCOME                                         AMOUNT
 4.  NAME OF PAYER
     (1st PAYER) (2nd PAYER) (3rd PAYER) (4th PAYER)      4.
 5.  TOTAL OF LINE 4...................................... 5.  00,000.00
 6.  CAPITAL GAIN DISTRIBUTIONS........................... 6.
 7.  NON TAXABLE DISTRIBUTIONS............................ 7.
 8.  EXCLUSION DIVIDEND FROM PUB. UTILITY................. 8.
 9.  ADD LINES 6, 7, and 8 ............................... 9.
10.  LINE 5 MINUS LINE 9 .................................10.  00,000.00
*************************************************************************
PART III - FOREIGN ACCOUNTS AND FOREIGN TRUSTS
11.  DID YOU HAVE AN INTEREST IN OR A SIGNATURE OR OTHER AUTHORITY
     OVER A BANK ACCOUNT, SECURITIES ACCOUNT, OR OTHER FINANCIAL   (ANS)
     ACCOUNT IN A FOREIGN COUNTRY?          COUNTRY NAME
12.  WERE YOU THE GRANTOR OF OR TRANSFEROR TO A FOREIGN TRUST
     WHICH EXISTED DURING THE CURRENT TAX YEAR WHETHER OR NOT
     YOU HAVE ANY BENEFICIAL INTEREST IN IT?                       (ANS)
*************************************************************************


          FOR PAPERWORK REDUCTION ACT NOTICE, SEE SEPARATE INSTRUCTIONS
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EXHIBIT CG - C  (SCHEDULE C)

SCHEDULE C      PROFIT (OR LOSS) FROM BUSINESS OR PROFESSION          1985 * 09
(FORM 1040)           (SOLE PROPRIETORSHIP)          OMB NO.  1545-0074
JOHN Q. AND MARY J. TAXPAYER                                 SSN 000-00-0000
*********************************************************************
A.   MAIN BUSINESS ACTIVITY:                          B.  BUSINESS CODE:
C.   NAME AND ADDRESS:                                D.  EMPLOYER ID NO.:  00-0000000

E.   METHOD(S) USED TO VALUE CLOSING INVENTORY:  (1)X COST
F.   ACCOUNTING METH.:  (1)   XX CASH
G.   WAS THERE ANY MAJOR CHANGE IN THE METHOD OF VALUATION?          (ANS)
H.   DID YOU DEDUCT EXPENSES FOR OFFICE IN HOME?                      (ANS)
*********************************************************************
PART I - INCOME:
1A.  GROSS RECEIPTS OR SALES ..................................1A.    0,000.00.
 B.  RETURNS AND ALLOWANCES...................................1B.
 C.  BALANCE (LINE 1A LESS LINE 1B)...........................1C.    0,000.00
2.   COST OF GOODS SOLD AND/OR OPERATIONS ....................2.
3.   GROSS PROFIT (LINE 1C LESS LINE 2).......................3.     0,000.00
4A   WINDFALL PROFIT TAX CREDIT/REFUND FOR 85.................4A.
4B   OTHER INCOME - SEE STATEMENT XX..........................4B.
5    INCOME (ADD LINES 3, 4A & 4B)............................5.     0,000.00
*********************************************************************
PART II-DEDUCTIONS:
 6.    ADVERTISING...........0,000,000.   22  PENSION/PROFIT SHARE....0,000.00
 7.    BAD DEBTS........                  23  RENT ON BUSINESS PROP...
       FM SALES OR SERVICES               24  REPAIRS.................
 8.    BANK CHARGES..........             25  SUPPLIES (NOT PT III)...
 9.    CAR/TRUCK EXPENSES....             26  TAXES (NOT WINDFALL)...
10.    COMMISSIONS...........             27  TRAVEL & ENTERTAINMENT..
11.    DEPLETION............              28  UTILITIES & PHONE.......
12.    DEPRECIATION AND 179               29A WAGES...................
        DED FM 4562.........                B JOBS CREDIT.............
       (NOT PT III).........                C 29A LESS 29B............
13.   DUES AND PUBLICAIONS                30  WINDFALL PROF. TAX......
14.   EMPLOYEE BNFT PROGRAMS              31  OTHER EXPENSES (LIST)...
15.   FREIGHT (NOT PT III)                 A
16.   INSURANCE............                B
17.   LAUNDRY AND CLEANING                 C
18.   LEGAL/PROF'L SERVICES                D
19.   MORTGAGE INT. PAID TO                E
      FINANCIAL INST                       F
20.   OFFICE EXP...........                G
21.   OTHER INTEREST                         OR SEE STATEMENT XX
*********************************************************************
32   TOTAL DEDUCTIONS (ADD COLS. 6 THROUGH 31G)...............32.   0,000.00
33   NET PROFIT (OR LOSS) (LINE 5 LESS LINE 32)...............33.   0,000.00
33   IF LOSS, DO YOU HAVE AMTS IN THIS BUSINESS NOT AT RISK?     (ANS)
*********************************************************************
PART III - COST OF GOODS SOLD AND/OR OPERATIONS
1.  INVENTORY AT BEGINNING OF YEAR (EXPLAIN IF DIFFERENT)..........1. 0,000,000.
2.  PURCHASES (LESS COST OF PERSONAL ITEMS)........................2.
3.  COST OF LABOR (DO NOT INCLUDE OWN SALARY)......................3.
4.  MATERIALS AND SUPPLIES.........................................4.
5.  OTHER COSTS....................................................5.
6.  ADD LINES 1 THROUGH 5..........................................6.
7.  INVENTORY AT END OF YEAR.......................................7.
8.  COST OF GOODS AND/OR OPERATIONS (LN 6 MINUS LN 7)..............8. 0,000,000.
*********************************************************************
    FOR PAPERWORK REDUCTION ACT NOTICE, SEE SEPARATE INSTRUCTIONS
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EXHIBIT CG - D (SCHEDULE D - PAGE 1)
                                                                   1985*12
                              CAPTIAL GAINS AND LOSSES
SCHEDULE D                                                     OMB NO. 1545-0074
(FORM 1040)                                                    SSN  000-00-0000
JOHN Q. AND MARY J. TAXPAYER
*********************************************************************************
*****************PART I - SUMMARY OF FORMS 1099 - B*******************************
1A  ENTER HERE & IN PT VII, PG 2, TOTAL SALES OF STOCKS, BONDS, ETC., REPORTED FOR
    1985 BY YOUR BROKER ON FM 1099-B OR EQUIVALENT STATEMENT.           1A 0,000,000.
*********************************************************************************
*****************PART II - SHORT-TERM CAPITAL GAINS AND LOSSES*********************
                                                   (E)       (F)          (G)
      (A)            (B)      (C)      (D)          COST OR   LOSS:  (E)  GAIN:  (D)
1B  KIND OF          DATE     DATE     GROSS        BASIS     LESS   (D)  LESS   (E)
    PROPERTY         ACQ.     SOLD     SALE PRICE
(1ST)                M/D/Y    M/D/Y    0,000,000.   0,000,000. 0,000,000.   0,000,000.
(2ND)
(3RD)                  OR SEE STATEMENT XX
---------------------------------------------------------------------------------
2   GAIN FROM SALE/EXC RES. (FM 2119)            2.XXXXXXXXXXXXXXXXXX      0,000,000.
3   SHORT-TERM CAP GAIN (FROM FM 6252)           3.XXXXXXXXXXXXXXXXXX
4   NET S-TERM GAIN PARTN/SCORP/FIDUC............4.          0,000,000.    0,000,000.
5   ADD LN 1B-4, COLS F & G......................5.
6   COMBINE LN 5, COLS F & G.................................6.
7   SHORT TERM LOSS CARRYOVER (AFTER 1969)...................7.
8   NET ST GAIN OR LOSS ADD LNS 6 & 7........................8.         0,000,000.
***************** PART III - LONG-TERM CAPITAL GAINS AND LOSSES********************
9   (1st)           M/D/Y   M/D/Y   0,000,000.   0,000,000. 0,000,000.   0,000,000.
    (2nd)
    (3rd)
                     OR SEE STATEMENT XX
10  GAIN FROM SALE/EXC RES.  (FM 2119)           10.XXXXXXXXXXXXXXXXXXXX     0,000,000.
11  LONG-TERM GAIN - INSTALL. SALES (F6252)      11.XXXXXXXXXXXXXXXXXXXX
12  NET L-TERM GAIN/LOSS PARTN/SCORP/FIDUC       12.0,000,000                0,000,000.
13  ADD LNS 9 THRU 12, COLS  F & G..............13.
14  ADD LN 13 COL F & G, ENTER GAIN OR LOSS..................14.
15  CAPITAL GAIN DISTRIBUTIONS...............................15.
16  GAIN FROM FORM 4797......................................16.
17  ADD LNS 14 THRU 16.......................................17.
18  L-TERM CAPITAL LOSS CARRYOVER AFTER 1969.................18.
19  NET L-TERM GAIN OR (LOSS), ADD LNS 17 AND 18.............19.          0,000,000.

                      SCHEDULE D CONTINUED ON PAGE 2

             FOR PAPERWORK REDUCTION ACT NOTICE, SEE SEPARATE INSTRUCTIONS
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EXHIBIT CG - D (SCHEDULE D - PAGE 2)

```
SCHEDULE D (CON'T)  PG 2                                                1985 * 12
(FORM 1040)
JOHN Q. & MARY J. TAXPAYER                                          SSN 000-00-0000
******************  PART IV    SUMMARY OF PARTS II & III   *****************************
20  ADD LINES 8 & 19.......................................................20.
21  IF LINE 20 IS GAIN ENTER SMALLER OF LINE 19 OR 20......................21.
22  ENTER 60% of LINE 21...................................................22.
23  SUBTRACT LINE 22 FROM LINE 20..........................................23.
24  IF LN 20 LOSS, ENTER ONE OF THE FOLLOWING AMOUNTS:.....................24.
    (A)  IF LINE 8 IS ZERO OR A NET GAIN, ENTER 50% OF LINE 20,
    (B)  IF LINE 19 IS ZERO OR A NET GAIN, ENTER LINE 20; OR
    (C)  IF LN 8 & 19 ARE LOSS, ENTER LN 8 AMT + 50% LN 19
25  ENTER SMALLEST OF LINE 24, $3,000 OR ADJ TAXABLE INCOME.................25.
*****************************************************************************************
PART V    COMPUTATION OF POST-1969 CAPITAL LOSS CARRYOVERS (85 to 86)
26  ENTER LOSS SHOWN ON LINE 8; IF NONE, ENTER ZERO.........................26.
27  ENTER GAIN SHOWN ON LINE 19.............................................27.
28  SUBTRACT LINE 27 FROM LINE 26...........................................28
29  ENTER SMALLER OF LINE 25 OR 28..........................................29.
30  SUBTRACT LINE 29 FROM LINE 28...........................................30
31  SUBTRACT LINE 29 FROM LINE 25...........................................31.
32  ENTER LOSS FROM LINE 19;................................................32.
33  ENTER GAIN SHOWN ON LINE 8:.............................................33.
34  SUBTRACT LINE 33 FROM LINE 32...........................................34
35  MULTIPLY AMOUNT ON LINE 31 BY 2.........................................35.
36  SUBTRACT LINE 35 FROM LINE 34...........................................36.
*****************************************************************************************
PART VI COMPLETE IF YOU ELECT OUT OF THE INSTALLMENT METHOD AND ARE REPORTING A NOTE,
  ETC., AT LESS THAN FACE VALUE

(ANS)     CHECK IF ELECTED
    ENTER FACE AMOUNT OF NOTE.................................0,000,000.
    ENTER THE PERCENTAGE OF VALUATION OF NOTE...........................XX%.
*****************************************************************************************
PART VII RECONCILIATION OF FORMS 1099-B
          SECTION A-RECONCILIATION OF STOCK SALES
37  TOTAL STOCK SALES FROM 1099-B...........................................37.
38  PROCEEDS FROM CAPITAL ASSET SALES.......................................38.
39  ADD LINES 37 AND 38.....................................................39.
40  LINE 37 NOT ON SCHEDULE D...............................................40.
41  SUBTRACT LINE 40 FROM LINE 39...........................................41.
        SECTION B - RECONCILIATION OF BARTER INCOME
42  FORM 1040, LINE 22......................................................42.
43  SCHEDULE C..............................................................43.
44  SCHEDULE D..............................................................44.
45  SCHEDULE E..............................................................45.
46  SCHEDULE F..............................................................46.
47  OTHER (LIST)............................................................47.
48  TOTAL OF LINES 42 THRU 47...............................................48.
```

EXHIBIT CG - E (SCHEDULE E - PAGE 1)

```
                                                              1985 * 13
SCHEDULE E        SUPPLEMENTAL INCOME SCHEDULE       OMB NO.  1545 - 0074
(FORM 1040)                                            SSN  000-00-0000
JOHN Q. AND MARY J. TAXPAYER              ************************
****************** PART I - RENT & ROYALTY INCOME/LOSS
1   KIND & LOCATION OF EACH RENTAL PROPERTY
2   WAS PROPERTY USED BY YOU OR FAMILY MORE THAN 14 DAYS OR 10% OF DAYS RENTED?
    PROPERTY A                                                   (ANS)
    PROPERTY B                                                   (ANS)
    PROPERTY C                                                   (ANS)
***************************************************************************
RENTAL AND ROYALTY INCOME          : PROPERTIES                   TOTALS
                           A           B           C

3   A RENTS RECEIVED     :00,000.  :00,000.   : 00,000. :3.  00,000,000.
    B ROYALTIES RECEIVED :         :          :
***************************************************************************
                                                        :XXXXXXXXXXXXXXXXXX
RENTAL AND ROYALTY EXPEN.  :         :          :         :
4   ADVERTISING          4.:         :          :         :
5   AUTO AND TRAVEL      5.:         :          :         :
6   CLEANING AND MAINTENANCE 6.:     :          :         :
7   COMMISSIONS          7.:         :          :         :
8   INSURANCE            8.:         :          :         :
9   LEGAL PROF FEES      9.:         :          :         :
10  MORTAGAGE INTEREST PAID 10.:     :          :         :
11  OTHER INTEREST PAID 11.:         :          :         :
12  REPAIRS             12.:         :          :         :
13  SUPPLIES            13.:         :          :         :
14  TAXES NOT WINDFALL  14.:         :          :         :
15  UTILITIES           15.:         :          :         :
16  WAGES AND SALARIES  16.:         :          :         :
17. OTHER (LIST)        17.:         :          :         :
    (1ST)                  :         :          :         :
    (2ND)                  :         :          :         :
    (3RD)                  :         :          :         :
    (4TH) OR SEE STATEMENT :         :          :         :
***************************************************************************
18  TOTAL EXPENSES                                    18.
19  DEPRECIATION EXPENSE                              19.
20  TOTAL (ADD LINES 18 & 19)                         20.  XXXXXXXXXXXXXXXXXX
21  INCOME OR (LOSS)                                  21.  XXXXXXXXXXXXXXXXXX
22  ADD PROFIT PROPERTIES                             22.
23  ADD LOSS PROPERTIES                               23.
24  COMBINE LNS 22/23                                 24.
25  NET FARM PROFIT/LOSS                              25.
26  TOTAL RENT/ROYALTY INC.                           26.

    SCHEDULE E CONTINUED ON PAGE 2

          FOR PAPERWORK REDUCTION ACT NOTICE, SEE SEPARATE INSTRUCTIONS
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EXHIBIT CG - E (SCHEDULE E - PAGE 2)

SCHEDULE E (CONT'D) PAGE 2 1985*13
(FORM 1040) SSN 000-00-0000
JOHN Q. & MARY J. TAXPAYER

****

PART II INCOME OR LOSS FROM PARTNERSHIPS, S. CORP., ESTATES, OR TRUSTS

(A) NAME	(B) CODE	(C)FOREIGN (X)	(D)EIN	(E) NET LOSS	(F) NET INCOME
				00,000,000.	00,000,000.

(INSERT INFO HERE & BETWEEN LINES 30 & 31, AS NEEDED OR SEE STATEMENT X)

27	ADD AMOUNTS IN COLUMNS (E) AND (F)	27.
28	COMBINE AMOUNTS IN (E) AND (F) ENTER NET INCOME	28.
29	SEC. 179 DEDUCTION	29.
30	TOTAL PARTNERSHIP & S CORP. INCOME LINES 28 and 29	30.
31	ADD AMOUNTS IN COLUMNS (E) AND (F)	31.
32	TOTAL ESTATE AND TRUST INCOME	32.

****************** PART III WINDFALL PROFIT TAX SUMMARY ******************

33	WINDFALL PROFIT TAX CREDIT OR REFUND IN 1985	33.
34	WINDFALL PROFIT TAX WITHELD IN 1985	34.
35	COMBINE AMOUNTS ON LINES 33 AND 34	35.

**************************** PART IV SUMMARY ****************************

36	TOTAL INCOME OR (LOSS)	36.
37	FARMERS AND FISHERMEN	37.

*************** PART V - DEPRECIATION CLAIMED IN PART I ******************

(A) PROP DESCRIPTION	(B) DATE ACQUIRED	(C) COST/ BASIS	(D) PRIOR YR DEPR	(E) DEPR METHOD	(F) L/R	(G) CURR YR DEPR
PROPERTY A........						
1ST	2/80	0,000,000.	0,000,000.	SL	L	0,000,000.
(ADD LINES AS NEEDED)						
TOTAL PROP A		OR SEE STATEMENT XX				

****

PROPERTY B						
1ST						
(ADD LINES AS NEEDED)		OR SEE STATEMENT XX				
TOTAL PROP B						

****

(C PROPERTY-ADD AS NEEDED)

OR SEE STATEMENT XX

```
EXHIBIT CG - F (SCHEDULE F - PAGE 1)
                                                                  1985 * 14
   SCHEDULE F                   FARM INCOME AND EXPENSES  OMB NO.  1545-0074
(FORM 1040)                                                    SSN  000-00-0000
JOHN Q. & MARY J. TAXPAYER
A AGRICULTURAL ACTIVITY CODE:  0000         B PRINCIPAL PRODUCT:
COMM DISPOSAL (PIK)   FEED (X)   SALES (X)                     EIN  00-0000000
**********PART I - FARM INCOME - CASH METHOD**************************************
 1  SALES OF LIVESTOCK AND ITEMS FOR RESALE                1. 0,000,000.
 2  COST OR BASIS OF LIVESTOCK FOR RESALE                  2.
 3  SUBTRACT LN 2 FM LN 1                                  3.
 4  SALES OF LIVESTOCK & PRODUCTS RAISED                   4.
 5A TOTAL DISTRIBUTIONS FM COOPERATIVES (FM 1099-PATR)     5A.
 5B LESS: NONINCOME ITEMS                                  5B.
 6  NET DISTRIBUTIONS (LN 5A MINUS LN 5B)                  6.
 7A AGRICULTURAL PROG PAYMENTS - CASH                      7A.
 7B AGRICULTURAL PROG PAYMENTS - MATERIAL & SVCS           7B.
 8  COMMODITY CREDIT LOANS                                 8.
 9  CROP INSURANCE PROCEEDS                                9.
10  MACHINE WORK                                           10.
11  OTHER INCOME                                           11.
12  GROSS INCOME (LN 3,4,6,& 7A thru 11, or PART III, LN 52)   12. 0,000,000.
**********PART II - FARM DEDUCTIONS - CASH & ACCRUAL METHOD***********************
13   BREEDING FEES              0,000,000.  26  MORTGAGE INT PAID
14   CHEMICALS                                  TO FINANCIAL INST. 0,000,000.
15   CONSERVATION EXPENSE                   27  OTHER INTEREST
16   DEPRECIATION & SECT. 179               28  PENSION/PROF SHARE
     EXPENSE DEDUCTION                      29  RENT OF FARM/PASTURE
17   EMPLOYEE BENEFIT PROG                  30  REPAIR,MAINT
     NOT ON LN 28                           31  SEEDS,PLANTS PURCH
18   FEED PURCHASED                         32  STORAGE,WAREHOUSING
19   FERTILIZER & LIME                      33  SUPPLIES PURCHASED
20   FREIGHT, TRUCKING                      34  TAXES             ,
21   GASOLINE, FUEL, OIL                    35  UTILITIES
22   INSURANCE                              36  VET FEES, MEDICINE
23A  LABOR HIRED                            37  OTHER
  B  JOBS CREDIT                                A
  C  BALANCE (SUBTRACT                          B
     LN 23B FM LN 23A)                          C
24   LAND CLEARING                              D                  0,000,000.
25   MACHINE HIRE               0,000,000.      E
**********************************************************************************
38 TOTAL DEDUCTIONS FM PT II (ADD LN 13 THRU 37)       38
39 NET FARM PROFIT/LOSS LN 12 LESS LN 38               39
40 IF LOSS , DO YOU HAVE AMTS FOR FARM THAT ARE NOT "AT RISK"       (ANS)



                     SCHEDULE F CONTINUED ON PAGE 2



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EXHIBIT CG - F (SCHEDULE F - PAGE 2)

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SCHEDULE F (CON'T)              PAGE 2                               1985 *14
JOHN Q. & MARY J. TAXPAYER                                 SSN  000-00-0000
********************** PART III - FARM INCOME - ACCURAL METHOD ****************
41   SALES OF LIVESTOCK & PRODUCTS DURING YEAR                41.  0,000,000.
42A  AGRICULTUAL PROG PAYMENTS - CASH                         42A.
42B  AGRICULTUAL PROG PAYMENTS - MATERIAL & SVCS              42B.
43   COMMODITY CREDIT LOANS                                   43.
44   MACHINE WORK                                             44.
45   OTHER INCOME                                             45.
46   TOTAL (ADD LN 41 THRU 45)                                46.
47   INVENTORY OF LIVESTOCK & PROD BEGIN OF YEAR              47.
48   COST OF LIVESTOCK & PROD PURCHASE DURING YEAR            48.
49   ADD LN 47 & 48                                           49.
50   INVENTORY OF LIVESTOCK & PROD END OF YEAR                50.
51   COST OF LIVESTOCK & PROD SOLD (LN 49 MINUS LN 50)        51.
52   GROSS INCOME (LN 46 MINUS LN 51)                         52.
     ENTER ALSO ON PART I, LN 12
*******************************************************************************
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EXHIBIT CG - G  (SCHEDULE G)

                                                                  1985 * 16
                                  INCOME AVERAGING
SCHEDULE G                                                  OMB NO.  1545-0074
(FORM 1040)                                                 SSN  000-00-0000
JOHN Q AND MARY J TAXPAYER
*******************************************************************************
STEP 1   ADD YOUR INCOME FROM 1982-1984                                    1.
 1982    1  AMOUNT FROM 1982 FORM 1040, LINE 37..........................2.
 1983    2  AMOUNT FROM 1983 FORM 1040, LINE 37..........................3.
 1984    3  AMOUNT FROM 1984 FORM 1040, LINE 37
 TOTAL   4  ALL INCOME EARNED FROM OUTSIDE THE U.S. OR WITHIN
            U.S. POSSESIONS, EXCLUDED FOR 1982 THRU 1984..................4.
                                                                           5.
         5  ADD LINES 1 THRU 4..............................................
*******************************************************************************
STEP 2   FIGURE YOUR AVERAGEABLE INCOME                                    6.
         6  DIVIDE LINE 5 BY THREE (3)....................................7.
         7  LINE 6 TIMES 140% (1.4).......................................8.
         8  TAXABLE INCOME FOR 1985 FROM FORM 1040, LN. 37................9.
         9  PREMATURE EXCESS DISTRIBUTION.................................10.
        10  SUBTRACT LINE 9 FROM LINE 8...................................11.
        11  EXCESS COMMUNITY PROP INCOME..................................12.
        12  SUBTRACT LINE 11 FROM LINE 10.................................13.
        13  AMOUNT FROM LINE 7 ABOVE......................................14.
        14  SUBTRACT LINE 13 FROM 12-AVERAGEABLE INCOME.
*******************************************************************************
STEP 3   FIGURE YOUR TAX                                                   15.
        15  LINE 14 TIMES 25% (.25).......................................16.
        16  AMOUNT FROM LINE 7 ABOVE......................................17.
        17  ADD LINES 15 AND 16...........................................18.
        18  AMOUNT FROM LINE 11 ABOVE.....................................19.
        19  ADD LINES 17 AND 18...........................................20.
        20  TAX ON AMOUNT ON LINE 19......................................21.
        21  TAX ON AMOUNT ON LINE 17......................................22.
        22  TAX ON AMOUNT ON LINE 16......................................23
        23  SUBTRACT LINE 22 FROM LINE 21.................................24.
        24  LINE 23 TIMES 3...............................................25.
        25  TAX ON AMOUNT ON LINE 8.......................................26.
        26  TAX ON AMOUNT ON LINE 10......................................27.
        27  SUBTRACT LINE 26 FROM LINE 25.................................28.
        28  ADD LINES 20, 24, & 27..........................................



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EXHIBIT CG-R (SCHEDULE R-PAGE 1)

SCHEDULE R CREDIT FOR THE ELDERLY AND DISABLED 1985#17
(FORM 1040) OMB NO. 1545-0074
JOHN Q. AND MARY J. TAXPAYER SSN 000-00-0000

****

PART I - FILING STATUS AND AGE

STATUS (END OF 1985)		CHECK ONLY ONE ANSWER:	
SINGLE	65 OR OVER	1.	(X)
	UNDER 65, RETIRED ON DISABILITY	2.	( )
MARRIED FILING JOINTLY	BOTH 65 OR OVER	3.	( )
	BOTH UNDER 65, ONE DISABILITY RET	4.	( )
	BOTH UNDER 65, BOTH DISABILITY RET	5.	( )
	ONE 65, ONE UNDER 65 ON DIS RET	6.	( )
	ONE 65, ONE UNDER 65 NOT DIS RET	7.	( )
MARRIED FILING SEP	65 AND DID NOT LIVE W/SPOUSE IN 1985	8.	( )
	UNDER 65, DIS RET & NOT LIVE W/SPOUSE	9.	( )

************************PART II - STATEMENT OF PERMANENT AND TOTAL DISABILITY********

CHECK IF STATEMENT FILED IN 1983 OR EARLIER, OR IN 1984 WITH BOX B CHECKED BY PHYSICIAN, AND YOU WERE UNABLE TO WORK IN 1985. ( )

PHYSICIAN'S STATEMENT

I CERTIFY THAT ____________________
NAME OF DISABLED PERSON

WAS PERMANENTLY AND TOTALLY DISABLED ON JANUARY 1, 1976, OR JANUARY 1, 1977, OR WAS PERMANENTLY AND TOTALLY DISABLED ON THE DATE HE OR SHE RETIRED. DATE RETIRED IF RETIRED AFTER DECEMBER 31, 1976: ____________,

PHYSICIAN: CHECK EITHER BOX A OR B BELOW AND SIGN. (CHECK ONLY ONE BOX)

A. ( ) DISABILITY HAS LASTED, OR CAN BE EXPECTED TO LAST CONTINUOUSLY FOR AT LEAST A YEAR. ______ PHYSICIANS SIGNATURE DATE

B. ( ) THERE IS NO REASONABLE PROBABILITY THAT THE DISABLED CONDITION WILL EVER IMPROVE. ______ PHYSICIANS SIGNATURE DATE

PHYSICIAN'S NAME: PHYSICIAN's ADDRESS:

****

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EXHIBIT CG-R (SCHEDULE R - PAGE 2)

1985

SCHEDULE R (CON'T) PAGE 2
(FORM 1040)
JOHN Q. & MARY J. TAXPAYER SSN 000-00-0000

****

PART III - FIGURE CREDIT

10	ENTER $5,000, $7,500 OR $3,750	10.	00,000.00
11	TAXABLE DISABILITY INCOME	11.	
12	ENTER SMALLER AMOUNT FROM LINE 10 OR LINE 11	12.	
13	NON-TAXABLE PENSION, ANNUITY & DISABILITY AMOUNTS	13.	
14	ENTER AMOUNT FROM FORM 1040, LN 33	14.	
15	ENTER $7,500, $10,000 OR $5,000	15.	
16	SUBTRACT LINE 15 FROM LINE 14, OR ZERO	16.	
17	DIVIDE LINE 16 BY 2	17.	
18	ENTER TOTAL OF LINE 13 AND LINE 17	18.	
19	SUBTRACT LINE 18 FROM LINE 12	19.	
20	PERCNTAGE USED TO FIGURE CREDIT	20.	X.15
21	MULTIPLY LINE 19 BY 15% (.15) (ENTER THIS AMOUNT ON FORM 1040, LINE 42)	21.	

EXHIBIT CG - SE (SCHEDULE SE)

SCHEDULE SE 1985 * 18

COMPUTATION OF SOCIAL SECURITY SELF-EMPLOYMENT TAX

(FORM 1040) OMB NO. 1545-0074

JOHN Q AND MARY J. TAXPAYER SSN 000-00-0000

* * *

PART I - REGULAR COMPUTATION OF NET EARNINGS FROM SELF EMPLOYMENT

1 NET PROFIT OR (LOSS) FROM SCHEDULE F, LN. 39, AND FARM PARTNERSHIPS, SCHEDULE K-1 (1065), LN.13A ....1.

2 NET PROFIT OR (LOSS) FROM SCHEDULE C, LN. 33, AND SCHEDULE K-1(FORM 1065), LN. 13A AND W-2 CHURCH WAGES.......2.
FORM 4361 FILED (ANS)

* * *

PART II - OPTIONAL COMPUTATION OF NET EARNINGS FROM SELF EMPLOYMENT

3 MAXIMUM INCOME FOR OPTIONAL METHOD..3. 1,600.00

4 FARM OPTIONAL METHOD -2/3 RDS OF GROSS INCOME FROM SCH. F, LN. 12 AND FARM PARTNERSHIPS, SCH. K-1, (1065), LN. 13B, OR $1,600, WHICHEVER IS SMALLER...4.

5 SUBTRACT LINE 4 FROM LINE 3................................ 5.

6 NONFARM OPTIONAL METHOD - SMALLER, 2/3 RDS GROSS INCOME FROM SCH. C, LN. 5, AND SCH. K-1, (1065) LINE 13C (OTHER THAN FARMING), $1,600, OR, IF YOU ELECTED FARM OPTIONAL METHOD, AMOUNT ON LINE 5... 6.

* * *

PART III - COMPUTATION OF SOCIAL SECURITY SELF EMPLOYMENT TAX

7 AMOUNT FROM PART I, LINE 1, OR, PART II, LINE 4............7.

8 AMOUNT FROM PART I, LINE 2, OR, PART II, LINE 6............8.

9 ADD LINES 7 AND 8...9.

10 LARGEST AMOUNT SUBJECT TO SOCIAL SECURITY OR RRTA TAX......10. 39,600.00

11A TOTAL SOC. SEC. WAGES FROM W-2 AND RRTA COMPENSATION.......11A.

11B UNREPORTED TIPS SUBJECT TO SS (FORM 4137) OR RRTA..........11B.

11C ADD LINES 11A AND 11B.................................... 11C.

12A SUBTRACT LINE 11C FROM LINE 10.............................12A

12B QUALIFIED U.S. GOVT WAGES..................................12B.

12C FORM W-2 ELECTING CHURCH & ORG WAGES.......................12C.

13 SMALLER OF LINE 9 OR 12A...................................13.

14 SELF EMPLOYMENT TAX - ENTER ON FORM 1040, LINE 51........14.

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EXHIBIT CG-W  (SCHEDULE W)

SCHEDULE W            DEDUCTION FOR MARRIED WORKING COUPLE          1985*20
                                                              OMB No. 1545-0074
(FORM 1040)                                                   SSN  000-00-0000
JOHN Q AND MARY J TAXPAYER
**********************************************************************************
                                                   (A) SELF         (B) SPOUSE
STEP 1 FIGURE YOUR EARNED INCOME
1  WAGES, SALARIES, TIPS, ETC. FM 1040 (LN 7)   1.   000,000    1.   000,000.
2  NET PROFIT/LOSS FM SELF-EMP.                 2.              2.
3  TOTAL EARNED INCOME (LN 1 PLUS LN 2)         3.              3.
**********************************************************************************
STEP 2 FIGURE YOUR QUALIFIED EARNED INCOME
4  ADJUSTMENTS FM 1040 (LN 25, 26, 27 & 31)     4.              4.
5  QUAL. EARNED INCOME (LN 3 MINUS LN 4)        5.   000,000    5.   000,000.
**********************************************************************************
STEP 3 FIGURE YOUR DEDUCTION
6  ENTER SMALLER OF LN 5A OR 5B                      XXXXXX     6.   000,000.
7  PERCENT USED                                      XXXXXX     7.   X.10
8  MULTIPLY LN 6 BY 10% -                            XXXXXX     8.   000,000.
   DEDUCTION (ENTER ON FORM 1040 LN 30)
**********************************************************************************

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Part IV. Items of General Interest

Notice of Proposed Rulemaking

Recapture of Investment Credit for Mass Assets

LR-92-73

SUMMARY: This document contains proposed regulations relating to recapture of investment credit for mass assets. The amendment will allow provision of new standard mortality dispersion tables and new rules for applying them so as to correct certain situations that resulted in inaccurate computations and to incorporate the rules under the Accelerated Cost Recovery System (ACRS). The regulations would provide specific rules for the treatment of mass assets which are recovery property governed by ACRS. In addition, the regulations would provide new rules for assigning individual lives to mass assets and assets similar in kind.

DATES: Written comments and requests for a public hearing must be delivered or mailed by February 18, 1986. The amendments would apply to assets placed in service in taxable years beginning [30 days after date of publication of the Treasury Decision in the Federal Register] and are proposed to be effective on the same date, except as otherwise provided for property depreciated under the ACRS methods.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-92-73) Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Sandra E. Wallach of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T (202-566-3458, not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 46 and 47 of the Internal Revenue Code of 1954.

The investment tax credit is allowed for certain depreciable property used in a trade or business. The amount of credit available is determined by reference to the depreciable life of the property. Recapture of a certain amount of the credit is required when the property is disposed of or ceases to be eligible for the credit with respect to the taxpayer before the end of its depreciable life (recapture period, in the case of recovery property). For most assets, it is easy to determine when the asset is retired or ceases to be eligible for the credit. The investment tax credit is available for certain other assets, however, which are fungible assets too numerous to be accounted for on an asset-by-asset basis. These assets are known as "mass assets." Special rules are required for recapture in the case of these mass assets. This project amends regulations setting out the rules for recapture for mass assets and updates the rules to include ACRS.

Under the existing regulations, taxpayers are allowed to determine statistically when mass assets are retired for recapture of investment credit. The determinations are based on mortality dispersion tables. The taxpayer may use its own mortality dispersion table or a standard mortality dispersion table prescribed by the Commissioner.

The proposed regulations contain two new standard mortality dispersion tables. One applies to non-recovery property (in general, property to which the ACRS depreciation methods do not apply) and the other to recovery property within the meaning of section 168. The proposed regulations also change the rules for applying mortality dispersion tables, for assigning individual useful lives to mass assets and assets similar in kind, and provide rules specifically applicable to recovery property.

RECAPTURE DETERMINATIONS

The existing standard mortality dispersion table is designed for recapture in the year assets are placed in service, based on expected retirements (front-end recapture). The new tables are designed for recapture in each year assets are expected to be retired (rear-end recapture). The proposed regulations do not require taxpayers to account for actual retirements, other than abnormal or extraordinary retirements.

The existing regulations made no provision for application of a standard mortality dispersion table to recovery property. The proposed regulations would provide a standard mortality dispersion table specifically applicable to recovery property. In addition, the regulations would provide that an asset's present class life is to be used in determining retirements on the standard mortality dispersion table even though the recovery period (as defined in section 168(c)) is determinative of the investment credit.

GROUPING OF MASS ASSETS

The existing regulations allow taxpayers to place assets with different lives in the same mass assets account. Recapture determinations under a mortality dispersion table are based on the average life of the account. Thus, taxpayers may shield assets with shorter lives from recapture because the assets with longer lives increase the average life of the account. In order to remove this potential for abuse, the proposed regulations require that all mass assets in an account have the same useful life, or the same present class life and recovery period in the case of recovery property.

The existing regulations require taxpayers to maintain sufficient records on which to substantiate the accuracy of the retirement statistics used in establishing their own mortality dispersion tables. The proposed regulations continue to require these records and, in addition, state that, if a taxpayer fails to maintain adequate records, the Service will determine recapture based on the standard mortality dispersion table.

The proposed regulations require that a mass asset account contain only assets placed in service in the same taxable year (closed-end or vintage accounts). In the case of property that is subject to an election under section 167(m) or that is recovery property, this rule conforms these regulations to the regulations under sections 167(m) and 168. In the case of property that is not ADR or recovery property this rule imposes a new requirement. Due to the change to rear-end recapture, the use of the open-end accounts distorts the retirement figures determined under a mortality dispersion table because, for example, some assets in the account may be in the first year since they were placed in service while others are in the second or third year. In the interest of accurate administration of the mortality dispersion tables, the proposed regulations require the use of closed-end accounts for all mass assets.

ASSETS SIMILAR IN KIND

The existing regulations allow taxpayers to assign separate lives to certain assets placed in multiple asset accounts. In determining investment credit for assets similar in kind, the taxpayer may assign each asset the average useful life used in computing the allowance for depreciation. Alternatively, the taxpayer may assign the assets different lives based on the range of estimated lives used in determining the average life. This allows taxpayers to receive investment credit for some assets in an account based on a useful life greater than the average life of those assets. This rule is inconsistent with section 46(c) which requires that taxpayers use the period used for depreciation in determining investment credit. In computing the allowance for depreciation, assets placed in a multiple asset account must, in general, be assigned the average life of the account. See example 2 of paragraph (b) of §1.167(b)-1. Therefore, in order that the investment credit be determined based on the same life used for depreciation, under the proposed regulations, taxpayers must assign to each asset in the account the average life of the assets.

EFFECTIVE DATES

The amendments to the existing regulations relating to assignment of individual lives and recapture of credit taken for non-recovery property (in general, property to which the ACRS depreciation methods do not apply) are applicable prospectively only.

The new rules added for recovery property apply to all property depreciated under the ACRS methods (*i.e.*, recovery property placed in service on or after January 1, 1981).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER. The collection of information requirements contained herein have been submitted for OMB review under the Paperwork Reduction Act, and comments on them should be sent to the Office of Information and Regulatory Affairs of OMB, Attn: Desk Officer for Internal Revenue Service, New Executive Office Bldg, Washington, D.C. 20503. The Internal Revenue Service requests persons submitting comments to OMB to also send copies of the comments to the Service.

EXECUTIVE ORDER 12291 AND REGULATORY FLEXIBILITY ACT

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. Although this document is a notice of proposed rulemaking which solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not consititute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

DRAFTING INFORMATION

The principal author of these proposed regulations is Sandra E. Wallach of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Proposed amendments to the regulations

The proposed amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * * Section 1.48-1 is also issued under 26 U.S.C. 38(b) (as in effect before the amendments made by Subtitle F of the Tax Reform Act of 1984) and 26 U.S.C. 47.

Par. 2. In §1.46-3, paragraph (e) is revised to read as set forth below.

§1.46-3 Qualified investment.

* * * * *

(e) *Useful life/recovery period*—(1) *In general*. For purposes of computing qualified investment in property that is not recovery property (within the meaning of section 168) the useful life of such property to be used in determining the applicable percentage to be applied to its basis or cost is the life used or to be used by the taxpayer in computing the allowance for depreciation with respect to such property for the taxable year in which the property is placed in service. Thus, if property is placed in service by a taxpayer in a taxable year but the period for depreciation with respect to such property does not begin until a succeeding taxable year (see paragraph (d)(1) of this section), the useful life for purposes of computing qualified investment must be the useful life that the taxpayer uses in computing the allowance for depreciation. See paragraph (e)(6) of this section for rules for determining the useful life of property with respect to which the allowance for depreciation is computed under the unit of production method, the income forecast method, or any other method which does not measure the useful life of the property in terms of years. For purposes of computing qualified investment in recovery property (within the meaning of section 168) the class of recovery property which applies to such property (as determined under section 168(c)) is determinative of the applicable percentage to be applied to its basis or cost.

(2) *Individual life*. (i) In order to determine qualified investment for multiple asset accounts (or single asset accounts for which an average life rate is used) it is necessary to determine the average life of the account. In order to determine average life, each asset which is section 38 property must be assigned an individual life. The rules for assigning individual lives to section 38 property are set forth below.

(ii) The individual life of any section

38 property to which an election under section 167(m) applies is the present class life selected for such property under §1.167(a)-11(b)(4), whether or not such property constitutes mass assets (as defined in §1.47-1(g)(2)).

(iii) The individual life of section 38 property described in this paragraph (e)(2)(iii) is determined for each asset on the best estimate obtainable on the basis of all the facts and circumstances. The individual life for each asset placed in a multiple asset account (including a mass asset account) must be the same as the useful life of such asset used in determining the group, classified, or composite life for the account for purposes of computing depreciation. Property is described in this paragraph (e)(2)(iii) if:

(A) it is not recovery property within the meaning of section 168;

(B) no election under section 167(m) is applicable to the property; and

(C) it is placed in a multiple asset account for which a group, classified, or composite rate is used in computing depreciation (or in single asset accounts for which an average life rate is used).

(iv) The individual life for recovery property within the meaning of section 168 is the recovery period which applies to such property as determined under section 168(c).

(3) *Assets similar in kind.* (i) For assets similar in kind contained in a multiple asset account (or in a single asset account for which an average life rate is used) and placed in service in taxable years beginning on or after [30 DAYS AFTER PUBLICATION OF THIS TREASURY DECISION IN THE FEDERAL REGISTER], the taxpayer must assign to each of those assets the average life of those assets used in computing the allowance for depreciation. Thus no assets may receive investment credit for a life longer than the average life of the assets in the account. For example, assume the taxpayer places 10 similar trucks in a multiple asset account for which a group rate is used in computing the allowance for depreciation. The trucks have an average useful life of 6 years, based on an estimated range of 5 to 7 years. The taxpayer must assign each asset a useful life of 6 years, even though some assets in the account are expected to remain in service for more than 6 years. For assets similar in kind that are placed in service in taxable years beginning before [30 DAYS AFTER PUBLICATION OF THIS TREASURY DECISION IN THE FEDERAL REGISTER], the rules contained in paragraph (e)(3)(ii) and (iv) of 26 CFR 1.46-3 (revised as of April 1, 1983) apply.

(ii) For purposes of paragraph (e)(3)(i) of this section, assets shall not be considered as "similar in kind" in respect of other assets unless all such assets are substantially of the same value, nor shall used section 38 property be considered as "similar in kind" to new section 38 property.

(4) *Mass assets.* For "mass assets" (as defined in paragraph (g)(2) of §1.47-1) placed in service in taxable years beginning on or after [30 DAYS AFTER PUBLICATION OF THIS TREASURY DECISION IN THE FEDERAL REGISTER], each asset must be assigned the life of the account, even if a mortality dispersion table indicates that some assets are expected to remain in service longer than the life of the account. See paragraphs (g)(3) and (n)(2) or §1.47-1 regarding the grouping of mass assets. For mass assets placed in service in taxable years beginning before [30 DAYS AFTER PUBLICATION OF THIS TREASURY DECISION IN THE FEDERAL REGISTER], the rules contained in paragraph (j)(3)(iii) of this section apply.

(5) *Useful life of property subject to amortization.* In the case of property with respect to which amortization in lieu of depreciation is allowable, the term over which amortization deductions are taken shall be considered as the useful life of such property.

(6) *Useful life of property subject to certain methods of depreciation.* If a taxpayer is using a method of depreciation, such as the unit of production or retirement method, which does not measure the useful life of the property in terms of years, he must estimate such useful life in years in order to compute his qualified investment.

(7) *Record requirements.* The taxpayer shall maintain sufficient records to determine whether section 47 (relating to certain dispositions, etc., of section 38 property) applies with respect to any asset.

(8) *Effective dates.* The provisions in paragraphs (e)(1) through (7) of this section apply only to property—

(i) the construction, reconstruction, or erection of which—

(a) is completed by the taxpayer after August 15, 1971, or

(b) is begun by the taxpayer after March 31, 1971, or

(ii) which is acquired by the taxpayer—

(a) after August 15, 1971, or

(b) after March 31, 1971, and before August 16, 1971, pursuant to an order which the taxpayer establishes was placed after March 31, 1971.

For property not described in this paragraph (e)(8), the rules in paragraphs (j)(1) through (6) of this section apply.

* * * * *

Par. 3. Section 1.47-1 is amended as follows:

1. The heading of paragraph (a)(1) is revised to read as follows: "*Property which is not recovery property within the meaning of section 168.*"

2. The first sentence of paragraph (a)(1)(i) is amended by adding the language "which is not recovery property within the meaning of section 168 (see paragraph (a)(3) of this section for special rules for recovery property within the meaning of section 168)" after the phrase "section 38 property" and before the phrase "the basis (or cost)".

3. The last sentence of paragraph (a)(1)(i) is amended by removing the language "paragraph (h)" and adding in its place the language "paragraph (l)".

4. Paragraph (a) is amended by adding a new paragraph (a)(3) to read "(3) *Special rules for recovery property within the meaning of section 168.* [Reserved]."

5. Paragraphs (f), (g), and (h) are redesignated (j), (k), and (l), respectively.

6. Paragraph (e) is amended by—

a. Redesignating paragraphs (e)(2) through (e)(5) as paragraphs (f)(1) through (f)(4);

b. Removing the heading for paragraph (e)(1), and redesignating paragraphs (e)(1)(i), (ii), and (iii) as paragraphs (e)(1), (2), and (3), respectively;

c. Revising redesignated paragraphs (e)(1) and (e)(2), and the introductory text of redesignated paragraph (e)(3), to read as follows:

§1.47-1 Recomputation of credit allowed by section 38.

* * * * *

(e) *Identification of property*—(1) *Record requirements.* In general, the taxpayer must maintain records from which he can establish, with respect to each item of section 38 property, the following facts:

(i) The date the property is disposed of or otherwise ceases to be section 38 property,

(ii) The estimated useful life or recovery period in the case of recovery property (within the meaning of section 168) which was assigned to the property under paragraph (e) of §1.46-3,

(iii) The month and the taxable year in which the property was placed in service and,

(iv) The basis (or cost), actually or reasonably determined, of the property.

(2) *Recapture determination.* For purposes of determining whether section 38 property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, before the close of its estimated useful life or recovery period in the case of recovery property (within the meaning of section 168), and for purposes of determining recomputed qualified investment, the taxpayer must establish from his records the facts required by paragraph (e)(1) of this section.

(3) *Examples.* If the taxpayer fails to maintain records from which he can establish the facts required by paragraph (e)(1) of this section, then this section shall be applied to the taxpayer in the manner indicated in the following examples:

* * * * *

7. Paragraph (i) is added and reserved.

8. A new heading is added to redesignated paragraph (f), and the heading for redesignated paragraph (f)(1) is revised, to read as follows: "(f) *Treatment of mass assets placed in service in taxable years beginning before [30 DAYS AFTER PUBLICATION OF THIS TREASURY DECISION IN THE FEDERAL REGISTER]*—(1) *In general.* (i)".

9. Paragraph (f)(1)(i), as redesignated, is amended by removing the language "in the case of mass assets (as defined in subparagraph (4) of this paragraph)" from the first sentence and adding in its place the language "for mass assets (as defined in paragraph (f)(3) of this section) placed in service in taxable years beginning before [30 DAYS AFTER PUBLICATION OF THIS TREASURY DECISION IN THE FEDERAL REGISTER]" and by removing the language "facts required by subparagraph (1) of this paragraph," from the first sentence and adding in its place the language "facts required by paragraph (e) of this section,".

10. Paragraph (f)(1)(ii)*(a)*, as redesignated, is amended by removing the language "(e)(3)(ii)*(b)*" and adding in its place the language "(j)(3)(ii)*(b)*".

11. Paragraph (f)(1)(iii), as redesignated, is amended by removing the language "§1.46-3(e)(3)(iii)" and adding in its place the language "§1.46-3(j)(3)(iii)".

12. Paragraph (f)(1)(v) in example *(c)*, as redesignated, is amended by removing the language "3(iv)" from the last sentence and adding in its place the language "(2)(iv)".

13. Paragraph (f)(2)(i), as redesignated, is amended by removing, in the first sentence, the language "§1.46-3(e)(3)(ii)*(b)* or (iii)" and adding in its place the language "§1.46-3(j)(3)(ii)*(b)* or (iii)".

14. Paragraph (f)(2)(ii), as redesignated, is amended by removing, in the first sentence, the language "§1.46-3 (e)(3)(iii)" and adding in its place the language "1.46-3(j)(3)(iii)".

15. Paragraph (f)(2)(iii), as redesignated, is amended by removing from the first sentence in the introductory text and from paragraph (f)(2)(iii)*(a)* the language "(e)(3)(ii)*(b)*" and adding in its place the language "(j)(3)(ii)*(b)*", and by removing from the second sentence of the introductory text the language "subparagraph (1)(i) of this paragraph" and adding in its place the language "paragraph (e)(1) of this section".

16. Paragraph (f)(2)(iv) is amended by removing the language "§1.46-3(e)(3)(ii)*(b)* or (iii)" and adding in its place the language "§1.46-3(j)(3)(ii)*(b)* or (iii)".

17. Paragraph (f)(3), as redesignated, is amended by removing in the first sentence the language "(e)(3)(iii)" and adding in its place the language "(j)(3)(iii)".

18. Paragraphs (f)(4)(ii), (iii), and (iv), as redesignated, are amended by removing the language "3(i)" and adding in its place the language "2(i)".

19. New paragraphs (g) and (h) are added to read as follows:

§1.47-1 Recomputation of credit allowed by section 38.

* * * * *

(g) *Treatment of mass assets which are not recovery property for taxable years beginning on or after [30 DAYS AFTER PUBLICATION OF THIS TREASURY DECISION IN THE FEDERAL REGISTER]*—(1) *In general.* (i) For mass assets which are not recovery property within the meaning of section 168 and are placed in service in taxable years beginning on or after [30 DAYS AFTER PUBLICATION OF THIS TREASURY DECISION IN THE FEDERAL REGISTER] the taxpayer may use its own mortality dispersion table or a standard mortality dispersion table prescribed by the Commissioner to recompute qualified investment for mass assets (as defined in paragraph (g)(2) of this section). The taxpayer must then use whichever table was chosen to determine the number of assets expected to be retired each year after the assets are placed in service. Recapture determinations must be made at the end of each taxable year in which assets are expected to be retired before the end of the useful life used to determine qualified investment. Taxpayers may rely on the table and, in general, do not need to account for actual retirements.

(ii) If the taxpayer uses its own mortality dispersion table, the table must be based on an acceptable survey of the taxpayer's actual experience and on appropriate statistical methods. The survey of the taxpayer's actual experience must be based on a sample of not less than 250 items. The taxpayer must maintain records showing the historical data used to develop the table. If the taxpayer does not maintain adequate records, the standard mortality dispersion table will be used to recompute qualified investment. The taxpayer may not use its own table for assets placed in service in a taxable year, unless the table was prepared before the beginning of that year. For example, assume a calendar year taxpayer completes preparation of its own table on July 1, 1979. It may use the table for assets placed in service in 1980, but not for assets placed in service in 1979.

(iii) A taxpayer may use the standard mortality dispersion table for one mass asset account and its own table for a different mass asset account. However, if the taxpayer applies a table to a mass asset account in any taxable year, the taxpayer must treat a subsequent change to another table for that account as a change of accounting methods under section 446(e) and obtain consent of the Commissioner.

(2) *Definition of mass assets*. The term "mass assets" means a mass or group of individual items of section 38 property (i) not necessarily homogeneous, (ii) each of which is minor in value relative to the total value of such mass or group, (iii) numerous in quantity, (iv) usually accounted for only on a total dollar or quantity basis, (v) with respect to which separate identification is impracticable, (vi) with the same useful life (in the case of recovery property, with the same present class life and recovery period) and (vii) placed in service in the same taxable year.

(3) *Grouping of mass assets*. In general, items in a mass asset account need not be of a similar type although they must have the same useful life. See paragraph (e) of §1.465-3 for rules for assigning useful lives to mass assets. For example, hammers and saws with useful lives of 4 years may be put in the same account. Hammers with useful lives of 5 years, however, may not be put in an account with hammers with useful lives of 4 years. However,if a taxpayer uses its own mortality dispersion table, all assets in an account must have approximately the same basis or cost. All mass assets in an account must be treated as placed in service (within the meaning of §1.46-3(d)) on the same date. Taxpayers must use appropriate averaging conventions to determine the date mass assets are placed in service. See paragraph (c)(2) of this section, paragraph (b) of §1.167(a)-10 for property not subject to an election under section 167(m), and paragraph (c)(2) of §1.167(a)-11 for property subject to an election under section 167(m).

(4) *Useful life*. The useful life of mass assets used in computing the allowance for depreciation must be used in applying the taxpayer's mortality dispersion table or the standard mortality dispersion table. See paragraph (e) of §1.46-3 for rules for assigning useful lives to mass assets. For example, if the taxpayer computes the depreciable life of mass assets under section 167(m), it must use the same depreciable life in applying the standard mortality dispersion table.

(5) *Standard mortality dispersion table*. The standard mortality dispersion table prescribed by the Commissioner and set forth below is based on whole and half-year average useful life categories. Each category contains 30 columns. Each column shows the percentage of basis or cost in a mass asset account expected to be retired in each of the first 30 years after the property is placed in service. The table is set forth below:

STANDARD MORTALITY DISPERSION TABLE
PERCENTAGE OF BASIS OR COST OF MASS ASSET ACCOUNT CONSIDERED DISPOSED OF EACH 12-MONTH PERIOD AFTER THE ACCOUNT IS PLACED IN SERVICE

Average Useful Life (Years)	1st (1)	2nd (2)	3rd (3)	4th (4)	5th (5)	6th (6)	7th (7)	8th (8)	9th (9)	10th (10)
3	2.28	13.59	34.13	34.13	13.59	2.28	—	—	—	—
3.5	1.62	8.23	23.51	33.28	23.51	8.23	1.62	—	—	—
4	1.22	5.46	15.98	27.34	27.34	15.98	5.46	1.22	—	—
4.5	.99	3.76	11.12	21.20	25.86	21.20	11.12	3.76	.99	—
5	.82	2.77	7.92	15.91	22.58	22.58	15.91	7.92	2.77	.82
5.5	.71	2.10	5.88	11.92	18.75	21.28	18.75	11.92	5.88	2.10
6	.62	1.66	4.40	9.19	14.98	19.15	19.15	14.98	9.19	4.40
6.5	.55	1.33	3.38	7.25	12.00	16.39	18.20	16.39	12.00	7.25
7	.51	1.11	2.74	5.49	9.64	13.87	16.64	16.64	13.87	9.64
7.5	.47	.92	2.20	4.49	7.79	11.55	14.65	15.86	14.65	11.55
8	.44	.78	1.85	3.61	6.46	9.52	12.91	14.43	14.43	12.91
8.5	.40	.70	1.52	2.97	5.16	8.19	10.87	13.05	14.28	13.05
9	.38	.61	1.29	2.47	4.43	6.69	9.27	11.93	12.93	12.93
9.5	.37	.52	1.13	2.07	3.69	5.57	8.13	10.44	11.72	12.72
10	.35	.47	.97	1.80	3.09	4.83	6.90	9.01	10.79	11.79
11	.32	.39	.75	1.35	2.24	3.64	5.10	6.82	8.51	10.24
12	.30	.32	.60	1.06	1.73	2.67	3.88	5.31	6.79	8.19
13	.28	.27	.49	.84	1.34	2.04	3.12	4.13	5.37	6.63
14	.27	.24	.40	.71	1.06	1.68	2.32	3.17	4.38	5.26
15	.26	.21	.35	.57	.89	1.31	1.89	2.60	3.43	4.36
16	.25	.18	.29	.49	.75	1.10	1.48	2.13	2.83	3.38
17	.24	.16	.28	.42	.60	.92	1.30	1.67	2.34	2.82
18	.23	.15	.24	.37	.51	.78	1.08	1.39	1.93	2.50
19	.23	.14	.20	.32	.47	.66	.92	1.15	1.61	2.08
20	.22	.13	.19	.28	.40	.57	.77	1.03	1.36	1.73
25	.20	.09	.12	.18	.23	.31	.41	.53	.67	.85
30	.19	.07	.09	.12	.15	.20	.25	.32	.40	.49

Average Useful Life (Years)	11th (11)	12th (12)	13th (13)	14th (14)	15th (15)	16th (16)	17th (17)	18th (18)	19th (19)	20th (20)
	—	—	—	—	—	—	—	—	—	—
.5	—	—	—	—	—	—	—	—	—	—
	—	—	—	—	—	—	—	—	—	—
.5	—	—	—	—	—	—	—	—	—	—
	—	—	—	—	—	—	—	—	—	—
.5	.71	—	—	—	—	—	—	—	—	—
	1.66	.62	—	—	—	—	—	—	—	—
.5	3.38	1.33	.55	—	—	—	—	—	—	—
7	5.49	2.74	1.11	.51	—	—	—	—	—	—
7.5	7.70	4.49	2.20	.92	.47	—	—	—	—	—
8	9.52	6.46	3.61	1.85	.78	.44	—	—	—	—
8.5	10.87	8.19	5.16	2.97	1.52	70	.40	—	—	—
9	11.93	9.27	6.69	4.43	2.47	1.29	.61	.38	—	—
9.5	11.72	10.44	8.13	5.57	3.69	2.07	1.13	.52	.37	—
10	11.79	10.79	9.01	6.90	4.83	3.09	1.08	.97	.47	.35
11	10.64	10.64	10.24	8.51	6.82	5.10	3.64	2.24	1.35	.75
12	9.28	9.87	9.87	9.28	8.19	6.79	5.31	3.88	2.67	1.73
13	7.77	8.62	9.10	9.10	8.62	7.77	6.63	5.37	4.13	3.12
14	6.62	7.25	8.32	8.32	8.32	8.32	7.25	6.62	5.26	4.38
15	5.32	6.23	7.04	7.61	7.93	7.93	7.61	7.04	6.23	5.32
16	4.22	5.30	6.11	6.80	6.89	7.54	7.54	6.89	6.80	6.11
17	3.71	4.48	4.94	5.93	6.51	6.54	7.14	7.14	6.54	6.51
18	3.12	3.57	4.46	4.81	5.71	6.19	6.21	6.75	6.75	6.21
19	2.60	2.97	3.76	4.37	4.96	5.48	5.53	6.19	6.36	6.36
20	2.17	2.66	3.18	3.72	4.25	4.76	5.22	5.57	5.83	5.96
25	1.06	1.29	1.55	1.85	2.18	2.50	2.84	3.19	3.54	3.84
30	.59	.72	.87	1.02	1.20	1.40	1.60	1.83	2.06	2.30

Average Useful Life (Years)	21st (21)	22nd (22)	23rd (23)	24th (24)	25th (25)	26th (26)	27th (27)	28th (28)	29th (29)	30th (30)
3	—	—	—	—	—	—	—	—	—	—
3.5	—	—	—	—	—	—	—	—	—	—
4	—	—	—	—	—	—	—	—	—	—
4.5	—	—	—	—	—	—	—	—	—	—
5	—	—	—	—	—	—	—	—	—	—
5.5	—	—	—	—	—	—	—	—	—	—
6	—	—	—	—	—	—	—	—	—	—
6.5	—	—	—	—	—	—	—	—	—	—
7	—	—	—	—	—	—	—	—	—	—
7.5	—	—	—	—	—	—	—	—	—	—
8	—	—	—	—	—	—	—	—	—	—
8.5	—	—	—	—	—	—	—	—	—	—
9	—	—	—	—	—	—	—	—	—	—
9.5	—	—	—	—	—	—	—	—	—	—
10	—	—	—	—	—	—	—	—	—	—
11	.39	.32	—	—	—	—	—	—	—	—
12	1.06	.60	.32	.30	—	—	—	—	—	—
13	2.04	1.34	.84	.49	.27	.28	—	—	—	—
14	3.17	2.32	1.68	1.06	.71	.40	.24	.27	—	—
15	4.36	3.43	2.60	1.89	1.31	.89	.57	.35	.21	.26
16	5.30	4.22	3.63	2.83	2.13	1.48	1.10	.75	.49	.29
17	5.93	4.94	4.48	3.71	2.82	2.34	1.67	1.30	.92	.60
18	6.19	5.71	4.81	4.46	3.57	3.12	2.50	1.93	1.39	1.08
19	6.19	5.53	5.48	4.96	4.37	3.76	2.97	2.60	2.08	1.61
20	5.96	5.83	5.57	5.22	4.76	4.25	3.72	3.18	2.66	2.17
25	4.13	4.38	4.58	4.70	4.78	4.78	4.70	4.58	4.38	4.13
30	2.54	2.78	3.01	3.23	3.42	3.61	3.75	3.86	3.95	3.98

The following notes explain the derivation of the table:

(i) The table is based on normal probability distribution. A normal distribution is characterized by a symmetrical dispersion of assets around the average. The equation of the normal probability distribution is

$$\left(Y = \frac{N}{\sigma \sqrt{2\pi}}\right) x \left(e^{z}\right)$$

The symbols in the equation are as follows:

N = the number of mass assets in the group

σ = the standard deviation of the normal distribution

π = the constant 3.14159

$z = \frac{-\frac{1}{2}(X - \bar{X})^2}{2}$

e = the constant 2.71828

x = an independent variable

$\bar{X}$ = mean or average of the mass assets in the group (average useful life)

$(x - \bar{X})$ = the deviation of x from the mean or average of the mass assets in the group

$\sigma 2$ = the variance of x

(ii) The range of expected useful lives is assumed to extend from the time of acquisition (− 3 Standard Deviations) to double the average useful life (+ 3 Standard Deviations). Practically all cases (99.73 percent) fall within the 3 Standard Deviation range under the assumption of a normal probability distribution. The first year mortality figures shown in the table for assets with a long average useful life are greater than those shown for one or more of the succeeding years. In addition, the last year mortality figures shown in the table for assets with a long average useful life are greater than those shown for one or more of the preceeding years. The reason is that the tails (beginning and ending years) of the distribution have been adjusted so that 100 percent of the assets (and not 99.73 percent) are included within the range of useful lives.

(6) *Recapture determinations*. A recapture determination must be made at the end of each taxable year in which assets are expected to be retired before the end of the useful life used to determine qualified investment. The percentage of basis or cost in a mass asset account expected to be retired under the taxpayer's mortality dispersion table or under a standard mortality dispersion table will be considered disposed of ratably over the year. The taxpayer is not required to account for actual retirements other than abnormal or extraordinary retirements. See paragraph (b) of §1.167(a)-8 for definitions of abnormal retirements of non-recovery property that is not subject to an election under section 167(m). See paragraph (d)(3)(ii) of §1.167(a)-11 for definitions of extraordinary retirements of non-recovery property subject to an election under section 167(m).

(7) *Example*. Paragraph (g)(6) of this section may be illustrated by the following example.

Example. (i) A calendar year taxpayer placed 1000 assets which are not recovery property in service in 1984. Taxpayer established a single mass asset account for these assets. Under the taxpayer's averaging convention the taxpayer uses July 1 as the assumed date of all additions to mass asset accounts. The assets have estimated useful lives of 3 years. The unadjusted basis in the account is $10,000.

(ii) The standard mortality dispersion table indicates that 2.28% of basis will be considered retired in the first year, 13.59% more will be considered retired in the second year, and 34.13% will be considered retired in the third year. The remaining 50% of basis will be in service for 3 years or more.

(iii) For 1984, no credit is allowed for 1.14% of the basis in the account, because 1984 is the taxable year the assets were placed in service. The standard mortality dispersion table indicates that 2.28% of basis is expected to be retired in the first year after the assets were placed in service. Since the assets were not considered placed in service until July 1, only 50 percent, or a 6-month ratable portion, of the 2.28% of basis is considered disposed of in 1984. The remaining 1.14% will be considered disposed of over the first half of 1985. Qualified investment for the remaining 98.86% is $3,295., which is 33⅓ percent of the basis attributable to that portion of the account.

(iv) For 1985, credit for 7.94% of the basis placed in service has to be recaptured. Of the 2.28% indicated by the standard mortality dispersion table to be disposed of in the first year, 1.14%, or a 6-month ratable portion, will be considered disposed of in the first half of 1985. of 13.59% indicated by the table to be disposed of in the second year, 6.8%, or a 6-month ratable portion, will be considered disposed of in the second half of 1985. Removing the qualified investment with respect to 7.94% of the account from the $9886. for which the credit was allowed in year 1 results in a qualified investment of $3030.36 (33⅓% of $9092). Thus, the credit allowed is $303.04, as compared to a $329.50 credit "allowable" for the full basis placed in the account. The decrease in allowable credit and, therefore, the amount recaptured is $26.46.

(v) For 1986, credit for 23.87% of the basis placed in service has to be recaptured. Of the 13.59% indicated by the standard mortality dispersion table to be disposed of in the second year, 6.8%, or a 6-month ratable portion, will be considered disposed of in the first half of 1986. Of the 34.13% indicated by the table to be disposed of in the third year, 17.07%, or a 6-month ratable portion, will be considered disposed of in the second half of 1986. Removing the qualified investment with respect to 23.87% of the account from the $9886. for which the credit was allowed in year 1 results in a qualified investment of $2499.42 (33⅓% of $7499.). Thus, the credit allowed is $249.94, as compared to a $329.50 credit "allowable" for the full basis placed in the account. The decrease in allowable credit and, therefore, the amount recaptured is $79.56.

(vi) For 1987, credit for 17.07% of the basis placed in service has to be recaptured. Of the 34.13% indicated by the standard mortality dispersion table to be disposed of the third year, 17.07%, or a 6-month ratable portion, will be considered disposed of in the first half of 1987. Removing the qualified investment with respect to 17.07% of the account from the $9886. for which the credit was allowed in year 1 results in a qualified investment of $2726.06 (33⅓% of $8179.). Thus, the credit allowed is $272.61, as compared to a $329.50 credit "allowable" for the full basis placed in the account. The decrease in allowable credit and, therefore, the amount recaptured is $56.89.

(vii) None of the credit is recaptured for the percent of basis disposed of after June 30, 1987.

(h) *Treatment of mass assets which*

are recovery property within the meaning of section 168—(1) *In general.* (i) For mass assets (as defined in paragraph (g)(2) of this section) which are recovery property within the meaning of section 168, the taxpayer must determine dispositions of assets from a mass asset account by the use of an appropriate mortality dispersion table. Such table must be used to determine the number of assets expected to be retired each year after the assets are placed in service. Recapture determinations must be made at the end of each taxable year in which assets are expected to be retired before the end of the recapture period (as defined in subsection (a)(5)(E)(ii) of section 47).

(ii) The taxpayer may use its own mortality dispersion table or a standard mortality dispersion table prescribed by the Commissioner. The taxpayer's own mortality dispersion table must be based on an acceptable survey of the taxpayer's actual experience and on appropriate statistical methods. The survey of the taxpayer's actual experience must be based on a sample of not less than 250 items. The taxpayer must maintain records showing the historical data used to develop the table. If the taxpayer does not maintain adequate records, the standard mortality dispersion table will be used to determine dispositions of assets from a mass account. The taxpayer may not use its own table for assets placed in service in a taxable year unless the table was prepared before the beginning of that year. For example, assume a calendar year taxpayer completes preparation of its own table on July 1, 1981. It may use the table for assets placed in service in 1982, but not for assets placed in service in 1981.

(iii) A taxpayer may use the standard mortality dispersion table for one mass asset account and its own table for a different mass asset account. However, if the taxpayer applies a table to a mass asset account in any taxable year, the taxpayer must treat a subsequent change to another table for that account as a change of accounting methods under section 446(e) and obtain consent of the Commissioner.

(2) *Grouping of mass assets.* In general, all items in a mass asset account must have the same present class life (as defined in §1.167(a)-11(b)(4)) and the same recovery period but need not be of a similar type. However, if a taxpayer uses its own mortality dispersion table, all assets in an account must have approximately the same cost. For purposes of applying a mortality dispersion table, all assets placed in service during a taxable year will be considered to be placed in service on the first day of the second half of the taxable year.

(3) *Present class life.* The present class life of the assets placed in a mass asset account must be used in applying either the taxpayer's mortality dispersion table or the standard mortality dispersion table, notwithstanding the fact that the appropriate recovery period is used in computing the tax credit.

(4) *Standard mortality dispersion table.* The standard mortality dispersion table prescribed by the Commissioner for purposes of this paragraph is set forth below.

STANDARD MORTALITY DISPERSION TABLE

PERCENTAGE OF BASIS OR COST OF MASS ASSET ACCOUNT CONSIDERED DISPOSED OF EACH 12-MONTH PERIOD AFTER THE ACCOUNT IS PLACED IN SERVICE

Present Class Life	1st (1)	2nd (2)	3rd (3)	4th (4)	5th (5)	6th (6)	7th (7)	8th (8)	9th (9)	10th (10)
2.5	3.59	23.84	45.14	23.84	3.59	—	—	—	—	—
3	2.28	13.59	34.13	34.13	13.59	2.28	—	—	—	—
3.5	1.62	8.23	23.51	33.38	23.51	8.23	1.62	—	—	—
4	1.22	5.46	15 98	27.34	27.34	15.98	5.46	1.22	—	—
5	.82	2.77	7.92	15.91	22.58	22.58	15.91	7.92	2.77	.82
6	.62	1.66	4.40	9.19	14.98	19.15	19.15	14.98	9.19	4.40
6.5	.55	1.33	3.38	7.25	12.00	16.39	18.20	16.39	12.00	7.25
7	.51	1.11	2.74	5.49	9.64	13.87	16.64	16.64	13.87	9.64
7.5	.47	.92	2.20	4.49	7.79	11.55	14.65	15.86	14.65	11.55
8	.44	.78	1.85	3.61	6.46	9.52	12.91	14.43	14.43	12.91
8.5	.40	.70	1.52	2.97	5.16	8.19	10.87	13.05	14.28	13.05
9	.38	.61	1.29	2.47	4.43	6.69	9.27	11.93	12.93	12.93
9.5	.37	.52	1.13	2.07	3.69	5.57	8.13	10.44	11.72	12.72
10 and 10.5	.35	.47	.97	1.80	3.09	4.83	6.90	9.01	10.79	11.79
11 and 11.5	.32	.39	.75	1.35	2.24	3.64	5.10	6.82	8.51	10.24
12 and 12.5	.30	.32	.60	1.06	1.73	2.67	3.88	5.31	6.79	8.19
13 and 13.5	.28	.27	.49	.84	1.34	2.04	3.12	4.13	5.37	6.63
14	.27	.24	.40	.71	1.06	1.68	2.32	3.17	4.38	5.26
15	.26	.21	.35	.57	.89	1.31	1.89	2.60	3.43	4.36
16 and 16.5	.25	.18	.29	.49	.75	1.10	1.48	2.13	2.83	3.38
17	.24	.16	.28	.42	.60	.92	1.30	1.67	2.34	2.82
18	.23	.15	.24	.37	.51	.78	1.08	1.39	1.93	2.50
19	.23	.14	.20	.32	.47	.66	.92	1.15	1.61	2.08
20-24	.22	.13	.19	.28	.40	.57	.77	1.03	1.36	1.73
25-29	.20	.09	.12	.18	.23	.31	.41	.53	.67	.85
30-50	.19	.07	.09	.12	.15	.20	.25	.32	.40	.49

Present Class Life	11th (11)	12th (12)	13th (13)	14th (14)	15th (15)	16th (16)	17th (17)	18th (18)	19th (19)	20th (20)
2.5	—	—	—	—	—	—	—	—	—	—
3	—	—	—	—	—	—	—	—	—	—
3.5	—	—	—	—	—	—	—	—	—	—
4	—	—	—	—	—	—	—	—	—	—
5	—	—	—	—	—	—	—	—	—	—
6	1.66	.62	—	—	—	—	—	—	—	—
6.5	3.38	1.33	.55	—	—	—	—	—	—	—
7	5.49	2.74	1.11	.51	—	—	—	—	—	—
7.5	7.70	4.49	2.20	.92	.47	—	—	—	—	—
8	9.52	6.46	3.61	1.85	.78	.44	—	—	—	—
8.5	10.87	8.19	5.16	2.97	1.52	70	.40	—	—	—
9	11.93	9.27	6.69	4.43	2.47	1.29	.61	.38	—	—
9.5	11.72	10.44	8.13	5.57	3.69	2.07	1.13	.52	.37	—
10 and 10.5	11.79	10.79	9.01	6.90	4.83	3.09	1.80	.97	.47	.35
11 and 11.5	10.64	10.64	10.24	8.51	6.82	5.10	3.64	2.24	1.35	.75
12 and 12.5	9.28	9.87	9.87	9.28	8.19	6.79	5.31	3.88	2.67	1.73
13 and 13.5	7.77	8.62	9.10	9.10	8.62	7.77	6.63	5.37	4.13	3.12
14	6.62	7.25	8.32	8.32	8.32	8.32	7.25	6.62	5.26	4.38
15	5.32	6.23	7.04	7.61	7.93	7.93	7.61	7.04	6.23	5.37
16 and 16.5	4.22	5.30	6.11	6.80	6.89	7.54	7.54	6.89	6.80	6.11
17	3.71	4.48	4.94	5.93	6.51	6.54	7.14	7.14	6.54	6.51
18	3.12	3.57	4.46	4.81	5.71	6.19	6.21	6.75	6.75	6.21
19	2.60	2.97	3.76	4.37	4.96	5.48	5.53	6.19	6.36	6.36
20-24	2.17	2.66	3.18	3.72	4.25	4.76	5.22	5.57	5.83	5.96
25-29	1.06	1.29	1.55	1.85	2.18	2.50	2.84	3.19	3.54	3.84
30-50	.59	.72	.87	1.02	1.20	1.40	1.60	1.83	2.06	2.30

Present Class Life	21st (21)	22nd (22)	23rd (23)	24th (24)	25th (25)	26th (26)	27th (27)	28th (28)	29th (29)	30th (30)
2.5	—	—	—	—	—	—	—	—	—	—
3	—	—	—	—	—	—	—	—	—	—
3.5	—	—	—	—	—	—	—	—	—	—
4	—	—	—	—	—	—	—	—	—	—
5	—	—	—	—	—	—	—	—	—	—
6	—	—	—	—	—	—	—	—	—	—
6.5	—	—	—	—	—	—	—	—	—	—
7	—	—	—	—	—	—	—	—	—	—
7.5	—	—	—	—	—	—	—	—	—	—
8	—	—	—	—	—	—	—	—	—	—
8.5	—	—	—	—	—	—	—	—	—	—
9	—	—	—	—	—	—	—	—	—	—
9.5	—	—	—	—	—	—	—	—	—	—
10 and 10.5	—	—	—	—	—	—	—	—	—	—
11 and 11.5	.39	.32	—	—	—	—	—	—	—	—
12 and 12.5	1.06	.60	.32	.30	—	—	—	—	—	—
13 and 13.5	2.04	1.34	.84	.49	.27	.28	—	—	—	—
14	3.17	2.32	1.68	1.06	.71	.40	.24	.27	—	—
15	4.36	3.43	2.60	1.89	1.31	.89	.57	.35	.21	.26
16 and 16.5	5.30	4.22	3.63	2.83	2.13	1.48	1.10	.75	.49	.29
17	5.93	4.94	4.48	3.71	2.82	2.34	1.67	1.30	.92	.60
18	6.19	5.71	4.81	4.46	3.57	3.12	2.50	1.93	1.39	1.08
19	6.19	5.53	5.48	4.96	4.37	3.76	2.97	2.60	2.08	1.61
20-24	5.96	5.83	5.57	5.22	4.76	4.25	3.72	3.18	2.66	2.17
25-29	4.13	4.38	4.58	4.70	4.78	4.78	4.70	4.58	4.38	4.13
30-50	2.54	2.78	3.01	3.23	3.42	3.61	3.75	3.86	3.95	3.98

(5) *Recapture determinations*. A recapture determination must be made at the end of each taxable year in which assets are expected to be retired before the end of the recapture period. The percentage of basis or cost in a mass asset account expected to be retired under the taxpayer's mortality dispersion table or under a standard mortality dis-

persion table will be considered disposed of ratably over the taxable year. The taxpayer is not required to account for actual retirements. The concept of abnormal or extraordinary retirements does not apply to recovery property. See paragraph (l)(1) of §1.168-2.

(6) *Example*. Paragraph (h)(5) of this section may be illustrated by the following example.

Example. (i) A calendar year taxpayer placed 1000 assets which are recovery property in service in 1981. Taxpayer established a single mass asset account for these assets. July 1 is the assumed date of all additions to mass asset accounts. Each asset is 3 year recovery property and has a present class life of 4 years. The unadjusted basis in the account is $10,000.

(ii) by applying the 4 year present class life, the standard mortality dispersion table indicates that 1.22% of basis would be considered retired in the first year, 5.46% more would be considered retired in the second year, and 15.98% more would be considered retired in the third year. The remaining 77.3% of basis will be in service longer than the 3 year recapture period.

(iii) For 1981, no credit was allowed for .61% of the basis in the account, because 1981 was the taxable year the assets were placed in service. The standard mortality dispersion table indicates that 1.22% of basis was expected to be retired in the first year after the assets were placed in service. Since the assets were not considered placed in service until July 1, only 50 percent, or a 6-month ratable portion of the 1.22% of basis was considered disposed of in 1981. The remaining .61% was considered disposed of over the first half of 1982. Qualified investment for the remaining 99.3% is $5963.40, which is 60 percent of the basis attributable to that portion of the account.

(iv) For 1982, credit for 3.34% of the basis placed in service was recaptured. Of the 1.22% indicated by the standard mortality dispersion table to be disposed of in the first year, .61%, or a 6-month ratable portion, was considered disposed of in the first half of 1982. Of the 5.46% indicated by the table to be disposed of in the second year, 2.73%, or a 6-month ratable portion, was considered disposed of in the second half of 1982. Removing the qualified investment with respect to 3.34% of the account from the $9939. for which the credit was allowed in year 1 results in a qualified investment of $5763. (60% of $9605.). Thus, the credit allowed was $576.30 as compared to a $596.34. credit "allowable" for the full basis placed in the account. The decrease in allowable credit was therefore $20.04, $3.66 of which is recaptured at 100% and $16.38 of which is recaptured at 66% (see paragraph (h)(6)(viii) of this section). The amount recaptured was therefore $14.47.

(v) For 1983, credit for 10.72% of the basis placed in service must be recaptured. Of the 5.46% indicated by the standard mortality dispersion table to be disposed of in the second year, 2.73%, or a 6-month ratable portion, will be considered disposed of in the first half of 1983. Of the 15.98% indicated by the table to be disposed of in the third year, 7.99%, or a 6-month ratable portion, will be considered disposed of in the second half of 1983. Removing the qualified investment with respect to 10.72% of the account from the $9939. for which the credit was allowed in year 1 results in a qualified investment of $5320.20 (60% of $8867.). Thus, the credit allowable is $532.02, as compared to a $596.34 credit "allowable" for the full basis placed in the account. The decrease in allowable credit is therefore 64.32, $16.38 of which is recaptured at 66% and $47.94 of which is recaptured at 33%. The amount recaptured is therefore $26.63.

(vi) For 1984 credit for 7.99% of the basis placed in service must be recaptured. Of the 15.98% indicated by the standard mortality dispersion table to be disposed of in the third year, 7.99%, or a 6-month ratable portion, will be considered disposed of in the first half of 1984. Removing the qualified investment with respect to 7.99% of the account from the $9939. for which the credit was allowed in year 1 results in a qualified investment of $5484. (60% of $9140.). Thus, the credit allowable is $548.40, as compared to a $596.34 credit "allowable" for the full basis placed in the account. The decrease in allowable credit is therefore $47.94, 33% of which is recaptured ($15.82).

(vii) None of the credit is recaptured for the percent of basis disposed of after June 30, 1984.

(viii) The amount of the decrease in allowable credit attributable to the first half of a taxable year is determined by multiplying the decrease in allowable credit for the entire taxable year by a fraction, the numerator of which is the percent of basis disposed of in the first half of the taxable year and the denominator of which is the entire percent of basis disposed of in the taxable year. The amount of the decrease in allowable credit attributable to the second half of a taxable year is determined by applying the formula above, except the numerator of the fraction will be the percent of basis disposed of in the second half of the taxable year.

(7) *Effective date*. The rules in this paragraph (h) apply to all recovery property placed in service on or after January 1, 1981.

* * * * *

20. paragraph (l)(4), as redesignated, is amended by removing "paragraph (e)(1) of this section" from the first sentence and inserting in its place "paragraph (e) of this section".

21. paragraph (l)(5), as redesignated, is amended by removing "(h)" from the first sentence and inserting in its place "(l)".

Par. 4. Section 1.48-9 is amended as follows:

1. Paragraph (a)(4)(ii) is amended by removing "§1.46-3(e)(7)" and inserting in its place "§1.46-3(e)".

2. Paragraph (b)(1)(i) is amended by removing "§1.47-1(h)" from the last sentence and inserting in its place "§1.47-1(l)".

3. Paragraph (l)(2) is amended by removing "§1.47-1(h)(5)" from the last sentence and inserting in its place "§1.47-1(l)(5)".

4. Paragraph (q)(1) is amended by removing "(h)(3)(ii)" from the last sentence and inserting in its place "(l)(3)(ii)".

5. Paragraph (q)(7)(iv) is amended by removing "(h)(3)(ii)" from the last sentence and inserting in its place "(l)(3)(ii)".

Par. 5. Paragraph (d)(3)(v)(*d*)(*2*) of §1.167(a)-11 is amended by removing "paragraph (e)(4)" and inserting in its place "paragraph (g)(2)."

ROSCOE L. EGGER, JR.,
Commission of
Internal Revenue.

(Filed by the Office of the Federal Register on December 19, 1985, 8:45 a.m., and published in the issue of the Federal Register for December 20, 1985, 50 F.R. 51874)

Charitable Contributions of Certain Securities

Announcement 86-4

This announcement concerns the definition of publicly traded securities in connection with the rules under section 170 of the Internal Revenue Code that exempt charitable contributions of such securities from certain substantiation requirements. The Internal Revenue Service has decided to modify the definition of publicly traded securities in §1.170A-13T(c)(7)(iv) of the temporary regulations as discussed below. The Service expects to issue final regulations in 1986 in which the modifications discussed in this announcement will be incorporated. Taxpayers may rely on this announcement until such final regulations are issued under section 170.

BACKGROUND

On December 31, 1984, the Service published section 1.170A-13T of the temporary regulations. Section 1.170A-13T(c)(1) provides that no deduction shall be allowed for charitable contributions, by individuals and certain entities, of property (other than money and publicly traded securities) the claimed value of which exceeds $5,000 unless certain substantiation requirements are met. In summary, the temporary regulations require a donor to obtain a qualified appraisal of the property and to attach an appraisal summary to the tax return on which the deduction for the contribution of the property is claimed.

Section 1.170A-13T(c)(7)(iv) defines "publicly traded securities" as securities for which market quotations are readily available on an established securities market. Market quotations are considered to be readily available on an established securities market if a security is (i) listed on a stock exchange in which quotations are published on a daily basis or (ii) regularly traded in a national or regional over-the-counter market for which published quotations are available. This announcement relates only to securities that do not satisfy either (i) or (ii) and, accordingly, are not "publicly traded securities" under existing regulations.

DEFINITION OF PUBLICLY TRADED SECURITIES

Under final regulations, market quotations for an issue of a security (as defined in section 165(g)(2)) will be considered to be readily available on an established securities market for purposes of the appraisal requirement for a computational period (as defined below), if the following five requirements are met:

(1) The issue is regularly traded during the computational period in a market that is reflected by the existence of an interdealer quotation system for the issue,

(2) the issuer or agent of the issuer computes the "average trading price" (as defined below) for the issue for the computational period,

(3) the average trading price and total volume of the issue during the computational period are published in a newspaper of general circulation throughout the United States (such as the Wall Street Journal or Barron's) not later than the last day of the month following the end of the calendar quarter in which the computational period ends,

(4) the issuer or its agent keeps books and records that list for each transaction during the computational period involving each issue covered by this procedure the date of the settlement of the transaction, the name and address of the broker or dealer making the market in which the transaction occurred, and the trading price and volume, and

(5) the issuer or agent permits the Internal Revenue Service to review the books and records described in paragraph (4) with respect to transactions during the computational period upon giving reasonable notice to the issuer or agent.

For purposes of this procedure, an issue of a security is a class of debt securities with the same obligor and identical terms except as to their relative denominations (amounts) or a class of stock having identical rights. An interdealer quotation system is any system of general circulation to brokers and dealers that regularly disseminates quotations of obligations by two or more identified brokers or dealers who are not related to either the issuer of the security or to the issuer's agent who computes the average trading price of the security. A quotation sheet prepared and distributed by a broker or dealer in the regular course of his business and containing only quotations of such broker or dealer is not an interdealer quotation system. See section 15A.453-1(e)(4) and section 1.897-1(m)(3).

The average trading price is the mean price of all transactions (weighted by volume), other than original issue or redemption transactions, conducted through a United States office of a broker or dealer who maintains a market in the issue of the security during the computational period. Bid and asked quotations are not taken into account. The computational period is weekly during October through December and monthly during January through September.

The procedure described in this announcement relates only to whether or not a qualified appraisal of donated securities is required. The fair market value of a security is the value of the security determined under section 1.170A-1(c)(2) and, therefore, is generally not the face value of the security. Accordingly, the final regulations will provide clearly that the average trading price is not binding as to valuation of the issue. Moreover, no inference should be made regarding whether or not the procedure is appropriate for purposes other than the qualified appraisal requirement (such as for purposes of section 170(e)(5)).

Taxpayers who are not required to obtain a qualified appraisal of donated securities because the securities meet the five requirements described above must attach a partially completed appraisal summary (section B of Form 8283 (Rev. Oct. 1985)) to the appropriate returns (see section 1.170A-13T(c)(2)(i)(B)). The summary must contain the information required by Parts I and II of the Form including the pertinent average trading price published for the securities. Part III of the Form regarding the certification by an appraiser is not required to be completed.

Enterprise Standard Industrial Classification Manual

Announcement 86-6

The relevant portions of the Enterprise Standard Industrial Classification Manual (ESIC Manual) are reprinted below.

The codes provided in the ESIC Manual are used to determine an employer's lines of business for purposes of the availability of exclusions from gross income for certain fringe benefits under section 132 of the Internal Revenue Code. The regulations requiring use of the ESIC Manual to define an employer's lines of business were set forth in §1.132-4T(a)(2)(i) printed in 1986-3 I.R.B., dated January 21, 1986.

INTRODUCTION

PURPOSE OF THE CLASSIFICATION

This Classification was developed to provide a standard for use with statistics about enterprises (i.e., companies, rather than their individual establishments) by kind of economic activity. Its use will facilitate the collection, tabulation, presentation, and analysis of data relating to enterprises; and will promote uniformity and comparability in the statistical data of federal government agencies. The classification of enterprises, rather than that of their constituent establishments, is used for compiling and analyzing financial and related statistics (such as income, expenses, and profits from the income statement; debt, liquidity, and other balance sheet items; and other data that may be available only on an enterprise basis).

DEFINITION OF THE ENTERPRISE

The enterprise unit consists of all establishments under common direct or indirect ownership. It is defined to include all entities, including subsidiaries, where there is more than 50 percent ownership. It may vary in composition ranging from a single legal entity (e.g. corporation, partnership, individual proprietorship) to a complex family of legal entities under common ownership. All subsidiaries of a subsidiary which are more than 50 percent owned would also be included. The 50 percent rule is applied to each level of subsidiaries. Even though a company may be able effectively to control another company with 50 percent or less ownership, the controlled company is not to be considered part of the enterprise. In some cases, it may not be feasible or possible to follow this definition. For this reason a detailed written description of the enterprise should be included in publications presenting enterprise industry statistics, especially if it differs from this definition.

SCOPE OF THE CLASSIFICATION

The Classification covers the entire field of economic activities: agriculture, forestry, and fishing; mining; construction; manufacturing; transportation and public utilities; wholesale trade, retail trade; finance, insurance, and real estate; services; and public administration.

The structure follows closely that of the Standard Industrial Classification (SIC)* used for the classification of establishments, thus providing a means for linking establishment statistics and enterprise statistics.

* Standard Industrial Classifiction Manual 1972, Office of Management and Budget, Stock number 4101-0066, available at the Government Printing Office.

The four-digit SIC structure is not practical for enterprise statistics since many enterprises encompass establishments in several industries. For instance, the Motor Vehicles and Equipment industry is made up of the establishment industries for Motor Vehicles, Motor Vehicle Parts, Truck and Bus Bodies, and Truck Trailers, since they are frequently owned by the same company.

The classification covers all enterprises, regardless of ownership. Where a classification by ownership or legal form of organization is needed, the clasification appearing in the Introduction of the SIC Manual should be used.

PRINCIPLES OF THE CLASSIFICATION

The following criteria were used as guidelines in evaluating the changes to the enterprise industries:

(1) The industry classification for enterprises should be essentially compatible with that for establishments. However, the industrial activity patterns of enterprise organizations may in some instances result in enterprise industries crossing major groups or divisions.

(2) The group of enterprises comprising an industry should be economically significant; that is, have 50,000 or more employees, or annual business receipts of $2 billion or more.

(3) The group of enterprises comprising an industry should be engaged to a high degree in the activity defining the industry, preferably 70 percent or more for nonmanufacturing and 60 percent or more for manufacturing.

This Classification is a revision of the 1968 Enterprise Standard Industrial Classification (ESIC). The revisions were evaluated on the basis of enterprise data from the 1967 Economic Censuses and from other sources, by applying the criteria described above. Most of the changes were made so that the ESIC would conform with the latest revision of the Standard Industrial Classification (1972). Some additional industries were created, and in a few cases small industries were combined. A table showing the changes is shown in the Appendix.

BASIS FOR ASSIGNING INDUSTRY CLASSIFICATION TO ENTERPRISES

An enterprise should be assigned to the industrial classification which includes the plurality contribution of its establishments. Ideally, the value added by the establishments to the goods and services should be the measure for determining the classification. In practice, value added data are not always available; in these cases it is necessary to use whatever available measure of activity could most closely approximate the same results.

STRUCTURE OF THE CLASSIFICATION

The structure of the Enterprise Classification makes it possible to tabulate, analyze, and publish enterprise data on a division, two-digit, three-digit, or four-digit basis. If possible, enterprises should be classified at the four-digit level even though the detail is not used in analysis or publication. This permits an agency to select the level of detail considered most appropriate for presentation of its data and to use additional subdivisions in adapting this Clasification for its own use, while still retaining basic comparability with the classifications used by other agencies. Any regroupings or industry subdivisions should be clearly labeled.

INDUSTRY CODE NUMBERING SYSTEM OF THE CLASSIFICATION

The detailed enterprise industry code of the Classification is a four-digit number with a decimal point between the second and third digits to distinguish visually the Enterprise from the Establishment SIC numbering system. The first two digits of the code represent the Major Group, similar to that for the establishment SIC. The third and fourth digits represent the enterprise subdivision.

The codes for enterprise industries were selected to provide codes as close in content to the establishment SIC as possible, but they do not necessarily have the same definition as the establishment industry. Where the content of the classes was identical in the two systems, the SIC code was used. Where the content was different, another code was used if possible. Miscellaneous and "not elsewhere classified" industries were coded with a "9" even though the industry was not identical in content to the SIC.

DEFINITION OF ENTERPRISE CLASSES

The enterprise industries are defined by one or more SIC industries as shown in the right hand column and are not defined specifically in this manual. The content of each enterprise industry is fully defined only by the reference to the corresponding industries in the 1972 SIC Manual. The titles in this manual were shortened so they could be used in publication tables (4-digit titles have been limited to 36 characters and the rest to 38 characters).

ENTERPRISE STANDARD INDUSTRIAL CLASSIFICATION (1974)

ESIC code	Title	SIC code
A	AGRICULTURE, FORESTRY, AND FISHING	
01.	Agricultural Production—Corps	01
01.2	Field crops	011,3,9
01.20	Field crops	0111-39, 91
01.5	Fruits, vegetables, & nursery stock	016-8
01.50	Fruits, vegetables, & nursery stock	0161-89
02.	Agricultural Production—Livestock	01
02.2	Livestock	021-5,9
02.20	Livestock	0211-59,91
02.7	Animal specialities	027
02.70	Animal specialities	0271-9
07.	Agricultural Services	07
07.4	Veterinary services	074
07.40	Veterinary services	0741,2
07.9	Agricultural services, nec	071,2,5-8
07.90	Agricultural services, nec	0711-29,51-83
08.	Forestry	08
08.0	Forestry	081-5
08.00	Forestry	0811-51
09.	Fishing, Hunting, and Trapping	09
09.0	Fishing, hunting, and trapping	091-7
09.00	Fishing, hunting, and trapping	0912-71
B	MINING	
10.	Metal Mining	10
10.0	Metal mining	101-9
10.00	Metal mining	1011-99
11.	Coal Mining	11,2
11.0	Coal mining	111,21
11.00	Coal mining	1111-1213
13.	Oil and Gas Extraction	13pt
13.3	Crude petroleum (no refining)	131pt., 2
13.30	Crude petroleum (no refining)	1311pt., 21
13.8	Oil and gas field services	138
13.80	Oil and gas field services	1381-9
14.	Nonmetallic Minerals, except Fuels	14
14.0	Nonmetallic minerals, except fuels	141-9
14.00	Nonmetallic minerals, except fuels	1411-99
C	CONSTRUCTION	
15.	General Building Contractors	15
15.2	Residential building construction	152
15.20	Residential building construction	1521,2
15.3	Operative builders	153
15.31	Operative builders	1531
15.4	Nonresidential building construction	154
15.40	Nonresidential building construction	1541,2
16.	Heavy Construction Contractors	16
16.1	Highway and street construction	161
16.11	Highway and street construction	1611
16.2	Heavy construction, except highway	162
16.20	Heavy construction, except highway	1622-9
17.	Special Trade Contractors	17
17.1	Plumbing, heating, air conditioning	171
17.11	Plumbing, heating, air conditioning	1711
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89.31	Accounting, auditing & bookkeeping	8931
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89.90	Services, nec	8411,21,811,922,99
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90.0	Public administration	911-72
90.00	Public administration	9111-721
K	NONCLASSIFIABLE ENTERPRISES	
99.	Nonclassificable Enterprises	99
99.9	Nonclassifiable enterprises	999
99.99	Nonclassifiable enterprises	9999

Appendix—Relation of 1974 to 1968 ESIC—changes only

1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
1974	1968 ESIC code
01.20	01.10,01.90pt.
01.50	01.20,01.90pt.
02.20	01.30,01.90pt.,07.90pt.
02.70	01.90pt.,07.90pt., 09.00pt.
07.40	07.22pt.
07.90	07.90pt.,07.22pt., 89.90pt.
09.00	09.00pt.,07.90pt
11.00*	12.00
13.30	13.10pt.
13.80	13.81,13.89
15.20	15.00pt.
15.31	65.50pt.
15.40	15.00pt.
16.11	16.00pt.
16.20	16.00pt.,15.00pt.
17.11*	17.10
17.21	17.90pt.
17.31*	17.30
17.40	17.90pt.
17.50	17.90pt.
17.61	17.90pt.
17.71	17.90pt.
17.90	17.90pt.,16.00pt.
20.11	20.11pt.
20.12	20.15pt.
20.39	20.39pt.,20.11pt., 20.15pt
20.40	20.42,20.49,20.11pt.
20.60	20.60,20.70
20.70*	20.91
20.81	20.81,20.84
20.88*	20.87
20.90	20.99,30.39pt.
21.00	21.10,21.90
22.10	22.10,22.30,22.60
22.56	22.50pt.
22.59	22.50pt.
23.11*	23.10
23.32	23.30pt
23.37	23.30pt.
23.39	23.30pt.
24.11*	24.10
24.20	24.20pt.
24.30	24.30pt.
24.50	37.90pt.,24.30pt.
25.11	25.11pt.,24.30pt
25.12	25.12,24.20pt.
25.19	25.19,25.11pt.
27.11*	27.10
27.21*	27.20
27.50	27.50pt.
27.80	27.80,27.50pt.
28.10	28.10pt.,13.10pt., 28.90pt
28.40	28.40pt.,28.10pt.
28.51	28.50pt.
28.70	28.90pt.,28.10pt., 28.40pt.
28.90	28.90pt.,28.10pt., 28.50pt.,29.90pt., 30.10pt.
29.10	29.11pt.,29.15
29.90	29.90pt.,29.11pt.

30.50	30.10pt.,30.70pt.
30.79	30.70pt.,28.10pt.
31.90	31.90pt.
32.90	32.40,32.90,30.10pt., 31.90pt.,35.90pt.
33.12*	33.10
33.23*	33.24
33.29	33.29pt.
33.50	33.50pt.
34.10	34.10,34.90pt.
34.30	34.30pt.
34.61	33.29pt.,33.50pt.
34.64*	34.60
34.80	39.80pt.
34.91*	34.80
34.99	34.90pt.
35.20	35.20,37.90pt.
35.31	35.31,35.35pt.
35.38	35.35pt.
35.43	35.41,35.49pt.
35.49	35.49pt.
35.80	35.80pt., 34.30pt.
35.90	35.90pt.
36.30	36.30,35.80pt.
36.60	36.60,39.80pt.
36.90	36.90pt.
37.71*	37.21
37.79*	37.29
37.90	37.90pt.,39.80pt.
38.10	38.10,36.90pt.
38.30	38.30, 39.80pt.
38.61*	38.60
38.73*	38.70
39.90	39.90 +
40.00	40.00pt.
41.90	41.90pt.
42.40*	42.10
43.11	none
46.10*	46.00
47.00	47.00,40.00pt.
48.11*	48.10
48.21*	48.20
48.99*	48.90
49.11*	49.10
50.30	50.98,50.91pt.,52.10pt.
50.50	50.91pt.
50.60	60.60,52.10pt.
50.70	50.70,52.10pt.
50.82	50.80pt.
50.83	50.80pt.,52.52
50.89	50.80pt.
50.90	50.99pt.,50.80pt.
51.10*	50.96
51.22	50.20pt.
51.30*	50.30
51.40*	50.40
51.50	50.50,07.90pt.
51.70*	50.92
51.80*	50.95
51.90	50.99pt.,50.20pt., 52.10pt.,59.60pt.
52.20	52.10pt.
52.61	59.60pt.
52.71	55.90pt.
53.11*	53.10
53.31*	53.30
53.99	53.90pt.
54.11*	54.10
55.31*	55.30
55.41*	55.40
55.90	55.90pt.
56.11	56.10pt.
56.21	56.20pt.
56.51*	56.50
56.61*	56.00
56.90	56.90,56.10pt.,56.20pt., 59.90pt.
57.40*	57.10
57.90	57.90,53.90pt.
59.12*	59.10
59.21*	59.20
59.60*	53.60
59.90	59.90pt.,53.90pt.
60.11	60.90pt.
60.20	60.90pt.
60.90	60.90pt.
61.60	61.60,61.50pt.
61.70	61.40,61.50pt.,73.20pt., 73.99pt.,75.90pt.
62.40*	62.10
62.81*	62.80
63.11	63.10pt.
63.20	63.10pt.
63.31	63.30pt.,63.90pt.
63.90	63.90pt.,63.30pt.
64.11*	64.00
65.12	65.11pt.
65.16	65.11pt.
65.19	65.16,65.17,65.19,70.30pt.
65.31*	65.30
65.41*	65.40
65.50	65.50pt.
66.11*	66.00
67.20	67.00pt.
67.92	67.00pt.
67.98	67.00pt.
67.99	67.00pt.,79.90Opt.
70.11	70.10,70.30pt.
70.21	70.90pt.
70.30	70.30pt.
70.41	70.90pt.
72.11	72.11pt.
72.16	72.15,72.90pt.
72.19	72.19,72.11pt.,72.90pt.
72.31*	72.30
72.41*	72.40
72.61*	72.60
72.90	72.90pt., 89.30pt.
73.21	73.20pt.
73.30	73.30,72.90pt.,73.99pt., 78.10pt.,89.90Opt.
73.70	73.92pt.,73.99pt.,76.00pt., 89.30pt.
73.91	73.91,89.90pt.
73.92	73.92pt.
73.93	73.93,73.99pt.
73.99	73.99pt.,73.92pt., 79.90Opt.
75.90	75.90pt.
76.00	76.00pt.
78.40	78.10pt.
79.90	79.90pt.,41.90pt.,70.30pt., 89.90pt.
80.10	80.10,80.90pt.
80.21*	80.20
80.40	80.90pt.
80.50	80.90pt.
80.60	80.90pt.
80.70	80.90pt.
80.90	80.90pt.
81.11*	81.00
82.00	82.00pt.,75.90pt.
83.00	89.90pt.,70.90pt.,80.90pt., 82.00pt.
86.71	89.90pt.
86.73	89.90pt.
86.76	89.90pt.
86.79	89.90pt.
89.11*	89.10
89.31	89.30pt.
89.90	89.90pt.
90.00	none
99.99	none

Appendix—Relation of 1968 to 1974 ESIC—changes only

1968	1974 ESIC code
01.10	01.20pt
01.20	01.50pt.
01.30	02.20pt.
01.90	01.20pt.,01.50pt.,02.20pt., 02.70pt.
07.22	07.40,07.90pt.
07.90	02.20pt.,02.70pt.,07.90pt., 09.00pt.,51.50pt.
09.00	02.70pt.,09.00pt.
12.00	11.00*
13.10	13.30,28.10pt.
13.81	13.80
13.89	
15.00	15.20,15.40,16.20pt.

16.00	16.11,16.20pt.,17.90pt.
17.10	17.11*
17.30	17.31*
17.90	17.21,17.40,17.50,17.61, 17.71,17,90pt.
20.11	20.11,20.39pt.,20.40pt.
20.15	20.12,20.39pt.
20.39	20.39pt.,20.90pt.
20.42	20.40pt.
20.49	20.40pt.
20.60 20.70	20.60
20.81	20.81
20.84	
20.87	20.88*
20.91	20.70*
20.99	20.90pt.
21.10 21.90	21.00
22.10 22.30 22.60	22.10
22.50	22.56,22.59
23.10	23.11*
23.30	23.22,23.37,23.39
24.10	?4.11*
24.20	24.20,25.12pt
24.30	24.30,24.50pt.,25.11pt.
25.11	25.11pt.,25.19pt.
25.12	25.12pt.
25.19	25.19pt.
27.10	27.11*
27.20	27.21*
27.50	27.50,27.80pt.
27.80	27.80pt.
28.10	28.10pt.,28.4pt., 28.70pt.,28.90pt.,30.79pt.
28.40	28.40pt.,28.70pt.
28.50	28.51,28.90pt.
28.90	28.90pt.,28.10pt.,28.70pt.
29.11	29.10pt.,29.90pt.
29.15	29.10pt.
29.90	29.90pt.,28.90pt.
30.10	30.50pt.,28.90pt32.90pt.
30.70	30.79pt.,30.50pt.
31.90	31.90,32.90pt.
31.90	31.90,32.90pt.
31.90	31.90,32.90pt.
32.40	32.90pt.
32.90	32.90pt.
33.10	33.12*
33.24	33.23*
33.29	33.29,34.61pt.
33.50	33.50,34.61pt.
34.10	34.10pt.
34.30	34.30,35.80pt.
34.60	34.64*
34.80	34.91*
34.90	34.99,34.10pt.
35.20	35.20pt.
35.31	35.31pt.
35.35	35.38.31pt.
35.41	35.43pt.
35.49	35.49,35.43pt.
35.80	35.80pt.,36.30pt.
35.90	35.90,32.90pt.
36.30	36.30pt.
36.60	36.60pt.
36.90	36.90,38.10pt.
37.21	37.71*
37.29	37.79*
37.90	37.90pt.,24.50pt.,35.20pt.
38.10	38.10pt.
38.30	38.30pt.
38.60	38.61*
38.70	38.73*
39.80	34.80,36.60pt.,37.90pt., 38.30opt.
39.00 +	39.90
40.00	40.00,47.00pt.
41.90	41.90,79.90pt.
42.10	42.40*
46.00	46.10*
47.00	47.00pt.
48.10	48.11*
48.20	48.21
48.90	48.99*
49.10	49.11*
50.20	51.22,51.90pt
50.30	51.30*
50.40	51.40*
50.50	51.50pt.
50.60	50.60pt.
50.70	50.70pt.
50.80	50.82,50.83pt.,50.89, 50.89,50.90pt.
50.91	50.50,50.30pt
50.92	51.70*
50.95	51.80*
50.96	51.10*
50.98	50.30pt.
50.99	50.90pt.,51.90pt.
52.10	52.20,50./30pt.,50.60pt., 50.70pt.,51.90pt.
52.52	50.83pt.
53.10	53.11*
53.30	53.31*
53.60	59.60*
53.90	53.99,57.90pt.,59.90pt.
54.10	54.11*
55.30	55.31*
55.40	55.41*
55.90	55.90,52.71
56.10	56.11,56.90pt.
56.20	56.21,56.90pt.
56.50	56.51*
56.60	56.61*
56.90	56.90pt.
57.10	57.40*
57.90	57.90pt.
59.10	59.12*
59.20	59.21*
59.60	52.61,51.90pt.
59.90	59.90pt.,56.90pt.
60.90	60.11,60.20,60.90
61.40	61.70pt.
61.50	61.70pt.,61.60pt.
61.60	61.60pt.
62.10	62.40*
62.80	62.81*
63.10	63.11,63.20
63.30	63.31pt.,63.90pt.
63.90	63.90pt.,63.3pt.
64.00	64.11*
65.11	65.12,65.16
65.16	65.19pt
65.17	65.19pt.
65.19	65.19pt.
65.30	65.31*
65.40	65.41*
65.50	65.50,15.31
66.00	66.11*
67.00	67.20,67.92,67.98,67.99pt.
70.10	70.11pt
70.30	70.30,65.19pt.,70.11pt., 79.90pt.
70.90	70.21,70.41,83.00pt.
72.11	72.11,72.19pt.
72.15	72.16pt.
72.19	72.19pt.
72.30	72.31*
72.40	72.41*
72.60	72.61*
72.90	72.90pt.,72.16pt., 72.19pt.,73.30pt.
73.20	73.21,61.70pt.
73.30	73.30pt.
73.91	73.91pt.
73.92	73..92,73.70pt.,73.99pt.
73.93	73.93pt.
73.99	73.99pt.,61.70pt.,73.30pt., 73.70pt.,73.93pt.
75.90	75.90,61.70pt.82.00pt.
76.00	76.00,73.70pt.
78.10	78.40,73.30pt.
79.90	79.90pt.,67.99pt.,73.99pt.
80.10	80.10pt.
80.20	80.21*

80.90	80.90,80.10pt.,80.40,80.50,80.60,80.70,83.00pt.
81.00	81.11*
82.00	82.00pt.,83.00pt.
89.10	89.11*
89.30	89.31,72.90pt.,73.70pt.
89.90	89.90,07.90pt.,73.30pt.73.91pt.,79.90pt.,83.00pt.,86.71,86.73,86,76,86.79
none	43.11
none	90.00
none	99.99

*Codes changed, but content of industry unchanged

+Mortician's goods distributed to several industries

PART V

Modifications to the Enterprise Standard Industrial Classification Manual 1974

The following changes should be made in the Enterprise Standard Industrial Classification Manual 1974.

The SIC code for ESIC Industry 67.98 should be changed to 6798.

The SIC codes for ESIC Industry 67.99 should include all of 6799.

The SIC codes for ESIC Industry 37.10 should include 3716.

Supplemental Information for Publication 1212

Announcement 86-7

The purpose of this announcement is to provide information to banks, brokers, and other middlemen regarding Treasury bills issued at a discount and maturing January through June 1986. This information will assist middlemen in reporting the discount, on Forms 1099-INT, for Treasury bill redemptions in cases where the owner's purchase price *cannot* be determined by owner or middleman records (see discussion below). It will also enable the middlemen to determine amounts subject to backup withholding where required. This information supplements cumulatively the listing of Treasury bills appearing in Publication 1212, *List of Original Issue Discount Instruments* (rev. Dec. 1985).

If the price which the owner paid for the Treasury bill is obtained from the owner's copy of the purchase confirmation receipt or similar record, or is reflected in the transaction records of the middleman, such price shall be used to determine the amount of discount to be reported on Form 1099-INT. If the owner's purchase price cannot be so determined, then the broker or other middleman shall report the discount as if the holder had purchased the Treasury bill at its original issue price. Under these circumstances a special rule is provided for determining the original issue price for Treasury bills issued at a discount. The special rule is that the middleman will prepare the Form 1099-INT by using the noncompetitive issue price for the longest-maturity Treasury bill maturing on that date. This price is reflected in the listing below for Treasury bills maturing January through June 1986.

Short Term United States Treasury Bills
Issued At A Discount And Maturing January—June 1986

CUSIP Number	Maturity Date	Issue Date	Noncompetitive Issue price (% of Principal Amount)	Dollar Amount of Discount to be Reported as Interest for 1986 (Per $1,000 of Maturity Value)
912794JL	01/02/86	07/05/85	96.440	35.60
JM	01/09/86	07/11/85	96.461	35.39
JN	01/16/86	07/18/85	96.360	36.40
JP	01/23/86	01/24/85	91.517	84.83
JQ	01/30/86	08/01/85	96.259	37.41
JR	02/06/86	08/08/85	96.198	38.02
JS	02/13/86	08/15/85	96.279	37.21
JT	02/20/86	02/21/85	91.446	85.54
JU	02/27/86	08/29/85	96.355	36.45
JV	03/06/86	09/05/85	96.309	36.91
JW	03/13/86	09/12/85	96.264	37.36
JX	03/20/86	03/21/85	90.657	93.43
JY	03/27/86	09/26/85	96.436	35.64
JZ	04/03/86	10/03/85	96.340	36.60
KA	04/10/86	10/10/85	96.299	37.01
KB	04/17/86	04/18/85	91.466	85.34
KC	04/24/86	10/24/85	96.299	37.01
KD	05/01/86	10/31/85	96.274	37.26
KE	05/08/86	11/07/85	96.309	36.91
KF	05/15/86	05/16/85	91.972	80.28
KG	05/22/86	11/21/85	96.330	36.70
KH	05/29/86	11/29/85	96.350	36.50
KJ	06/05/86	12/05/85	96.330	36.70
KK	06/12/86	06/13/85	92.740	72.60
KL	06/19/86	12/19/85	96.456	35.44
KM	06/26/86	12/26/85	96.436	35.64

IRS has also been advised of certain information to be added to Section II of Publication 1212 (Rev. Dec. 1985). Section II reflects a listing of amounts of original issue discount (OID) for use *solely* by brokers and other middlemen in preparing information returns for zero coupon instruments issued either under the Department of the Treasury's STRIPS program or as instruments backed by U.S. Treasury securities that represent ownership interests in those securities. The listing of such OID amounts is arranged according to the maturity date of the respective stripped interest and principal components. The additional stripped component maturity dates and amounts of OID to be reported per $1,000 of maturity value are provided in the following list:

STRIPPED COMPONENT MATURITY	OID PER $1000
1/15/1985	3.17
1/31/1985	6.47
2/28/1985	12.73
3/31/1985	19.35
4/15/1985	22.78
4/30/1985	26.20
5/31/1985	33.43
6/30/1985	40.67
7/15/1985	44.64
7/31/1985	48.47
8/31/1985	56.23
9/30/1985	63.78
10/15/1985	67.60
10/31/1985	71.86
11/30/1985	78.95
12/31/1985	86.18
1/15/1986	86.51
1/31/1986	86.34
2/28/1986	86.44
3/31/1986	86.35
4/15/1986	86.37
4/30/1986	86.30
5/31/1986	86.29
6/30/1986	86.06
7/15/1986	86.26
7/31/1986	86.14
8/31/1986	85.99
9/30/1986	85.75
10/15/1986	85.56
10/31/1986	85.53
11/30/1986	85.30
12/31/1986	84.86
1/15/1987	84.77
1/31/1987	75.83
2/28/1987	73.81
3/31/1987	83.96
4/15/1987	83.76
4/30/1987	55.81
5/31/1987	42.65
6/30/1987	82.68
7/15/1987	82.42
7/31/1987	31.63
8/31/1987	23.39
9/30/1987	81.34
10/15/1987	81.11
10/31/1987	11.80
11/30/1987	5.74
12/31/1987	79.92
1/15/1988	79.72
3/31/1988	78.46
4/15/1988	78.24
6/30/1988	76.90
7/15/1988	76.58
9/30/1988	75.21
10/15/1988	74.93
12/31/1988	73.60
1/15/1989	73.29
3/31/1989	52.43
4/15/1989	71.65
6/30/1989	32.67
7/15/1989	69.95
9/30/1989	10.76
10/15/1989	68.34
1/15/1990	66.64
4/15/1990	65.03
7/15/1990	63.45
10/15/1990	61.87
1/15/1991	60.35
4/15/1991	58.80
7/15/1991	57.31
10/15/1991	55.76
1/15/1992	52.74
4/15/1992	39.45
7/15/1992	25.23
10/15/1992	8.73

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.61-2T, removed; new 1.61-2T, added; 1.132-1T, removed; new 1.1.32-1T, added; 1.132-2T through 1.132-8T, added; 1.162-25T 1.274-5T, 1.274-6T, amended.	Taxation of fringe benefits and exclusions from gross income of certain fringe benefits	1986-3 I.R.B. 40	Feb. 21, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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*Denotes entry since last publication

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

SPECIAL ANNOUNCEMENTS

Announcement 86-15, page 48.

A public hearing will be held on February 10, 1986, on proposed regulations relating to residential rental property.

Announcement 86-16, page 48.

A public hearing will be held on February 14, 1986, on proposed regulations relating to the residential energy credit.

INCOME TAX

Rev. Rul. 86-11, page 4.

Investment credit; section 38 property; used elevators. Used elevators, although purchased after June 30, 1963, cannot be used section 38 property. Rather, the extent of costs incurred for reconstruction completed after June 30, 1963, the elevators qualify as new section 38 property.

Rev. Rul. 86-12, page 32.

Involuntary conversion; insurance proceeds; use and occupancy insurance contract. The Service will look to the underwriting and actuarial criteria and any other information used in writing the insurance to determine if the insurance is designed to reimburse for a loss of profits and fixed charges. Rev. Rul. 73-477 amplified.

Rev. Rul. 86-13, page 33.

Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for February 1986.

Rev. Rul. 86-14, page 33.

Payment of employee FICA tax by employer without deduction from wages. Payments by an employer of employee FICA tax without deduction from employee's wages under an agreement between them are additional wages for FICA purposes, the amount of wages to be determined by a formula. The additional FICA wages so determined are includible in the employee's gross income and are wages for purposes of income tax withholding. If otherwise appropriate, the employer may deduct the payments as ordinary and necessary business expenses under section 162 of the Code. Rev. Rul. 74-75 modified.

Rev. Proc. 86-6, page 36.

Depreciation; recovery period. Tables reflect the increase in the recovery period from 18 years to 19 years for real property placed in service after May 8, 1985.

T.D. 8065, page 4.

Amendments to the regulations under section 704(b) of the Code relate to the determination of a partner's distributive share of partnership income, gain, loss, deduction, or credit (or item thereof).

Announcement 86-8 page 45.

The date by which partnerships must furnish statements on Form 8308 for calendar year 1985 in order to avoid penalties under section 6678(a) of the Code is extended to March 14, 1986.

EXEMPT ORGANIZATIONS

Announcement 86-10, page 45.

A list is given of organizations now classified as private foundations and organizations that are not private operating foundations.

ADMINISTRATIVE

Announcement 86-9, page 45.

Certain errors in Publication 225, Farmer's Tax Guide, are corrected.

Announcement 86-11, page 47.

Errors in Publication 505, Tax Withholding and Estimated Tax, are corrected.

Announcement 86-12, page 47.

Schedule T (Form 5300), Supplemental Application for Approval of Employee Benefit Plans Under TEFRA, TRA 84, and REA, has been updated.

Announcement 86-13, page 47.

Form 5498, Individual Retirement Arrangement Information, has been revised for 1986 and is now available.

Finding Lists begin on page 52.
Announcement of Suspensions on page 49.
Announcement of Notice of Proposed Rulemaking on page 50.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 48.—Definitions; Special Rules

26 CFR 1.48-1: Definition of section 38 property.

Investment credit; section 38 property; used elevators. Used elevators, although purchased after June 30, 1963, cannot be used section 38 property. Rather, to the extent of costs incurred for reconstruction completed after June 30, 1963, the elevators qualify as new section 38 property.

Rev. Rul. 86-11

ISSUE

Are used elevators, purchased after June 30, 1963, used section 38 property?

FACTS

In 1985, a taxpayer purchased two commercial buildings, each containing an elevator within the meaning of section 1.48-1(m)(2) of the Income Tax Regulations. Both elevators had been previously used. The taxpayer kept one of the elevators in service. The other elevator was taken out of service for reconstruction including the replacement of the motor, cables, controller, and cage.

LAW AND ANALYSIS

Section 38 of the Internal Revenue Code allows a credit against income tax for investment in certain depreciable property. Under section 48(a)(1)(C), the term "section 38 property" includes elevators, but only if the construction, reconstruction, or erection of the elevator is completed by the taxpayer after June 30, 1963, or the elevator is acquired after June 30, 1963, and the original use of the elevator commences with the taxpayer and commences after that date.

Section 48(b)(1) of the Code provides that the term "new section 38 property" means section 38 property the original use of which commences with the taxpayer. Section 48(c)(1) provides, in general, that the term "used section 38 property" means section 38 property acquired by purchase after December 31, 1961, that is not new section 38 property.

Section 1.48-1(m)(1) of the regulations provides, in part, that if an elevator or escalator is reconstructed by the taxpayer after June 30, 1963, the basis attributable to the reconstruction may be taken into account in determining qualified investment under section 46(c). Section 1.48-2(b)(7) of the regulations provides that the term "original use" means the first use to which the property is put, whether or not that use corresponds to the use of the property by the taxpayer.

When section 48 was added to the Code by the Revenue Act of 1962, section 2(b), 1962-3 C.B. 111, 117, the definition of section 38 property did not include elevators. The Revenue Act of 1964, section 203(c), 1964-1 (Part 2) C.B. 6, 18, added elevators to the definition of section 38 property. Congress believed that new elevator and escalator equipment represents an important aspect of modernization of plant and facilities; thus, new elevators and escalators installed after June 30, 1963, and modernization of existing elevators after that date should be eligible for the investment credit. *See* H.R. Rep. No. 749, 88th Cong., 1st Sess. 35-36 (1963), 1964-1 (Part 2) C.B. 125, 159-160. The definitions of new and used section 38 property were unaffected.

Because section 48(a) of the Code, regarding the definition of section 38 property, includes only elevators constructed, reconstructed, or erected by the taxpayer and elevators the original use of which commences with the taxpayer, any elevator that meets the requirements of section 48(a) will also satisfy the requirements of section 48(b), regarding new section 38 property. Thus, a qualifying elevator can be only new section 38 property. In the present case, the elevator that the taxpayer purchased and reconstructed in 1985 is section 38 property to the extent of costs incurred for the reconstruction. Since the reconstruction was completed after June 30, 1963, the elevator satisfies the definition of new section 38 property to the extent of those costs.

However, the other elevator does not qualify as section 38 property; therefore, it can be neither used for new section 38 property. Although the elevator was acquired after June 30, 1963, the original use of the elevator did not commence with the taxpayer after that date.

HOLDING

Used elevators, although purchased after June 30, 1963, cannot be used section 38 property. Rather, to the extent of costs incurred for reconstruction completed after June 30, 1963, the elevators qualify as new section 38 property.

Section 61.—Gross Income Defined

26 CFR 1.61-2: Compensation for services, including fees, commissions, and similar items.

Whether payments by an employer of the employee FICA tax without deduction from the employee's wages under an agreement between the two are includible in gross income. See Rev. Rul. 86-14, page 33).

Section 162.—Trade or Business Expenses

26 CFR 1.162-7: Compensation for personal services.

Whether payments by an employer of the employee FICA tax without deduction from the employee's wages under an agreement between them are deductible. See Rev. Rul. 86-14, page 33.

Section 168.—Accelerated Cost Recovery System

Tables set forth the cost recovery rates for real property placed in service after May 8, 1985. See Rev. Proc. 86-6, page 36).

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of February 1986. See Rev. Rul. 86-13, page 33).

Section 483.—Interest on Certain Deferred Payments

Federal short-term, mid-term and long-term rates are set forth for the month of February 1986. See Rev. Rul. 86-13, page 33).

Section 704.—Partner's Distributive Share

26 CFR 1.704-1: Partner's distributive share.

T.D. 8065

TITLE 26—INTERNAL REVENUE. —CHAPTER I, SUBCHAPTER A, PART 1—INCOME TAX, TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Partner's Distributive Share

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final Income Tax Regulations under section 704(b) of the Internal Revenue Code of 1954, relating to the determination of a partner's distributive share of partnership income, gain, loss, deduction, or credit (or item thereof). It reflects certain changes made to the law by the Tax Reform Act of 1976 [Pub. L. 94-455, 1976-3 C.B. (Vol. 1) 1]. These final regulations provide taxpayers with the guidance needed to comply with the law.

DATE: The amendments generally are effective for partnership taxable years beginning after December 31, 1975.

FOR FURTHER INFORMATION: Contact John G. Schmalz of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. ATTN: CC:LR:T Phone 202-566-3297

SUPPLEMENTARY INFORMATION:

BACKGROUND

On March 9, 1983, the FEDERAL REGISTER published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 704(b) of the Internal Revenue Code of 1954 [LR-262-76, 1983-1 C.B. 930]. The amendments were proposed to conform the regulations to section 213(d) of the Tax Reform Act of 1976 (95 Stat. 1548). Numerous written comments were submitted during the comment period, and a public hearing was held on May 4, 1983. After consideration of all comments regarding the proposed regulations, these regulations are adopted as revised by this Treasury decision. This Treasury decision reserves §1.704-1(b)(4)(iv), relating to allocations attributable to nonrecourse debt, with respect to which the March 9, 1983, notice of proposed rulemaking remains outstanding.

EXPLANATION OF THE PROVISIONS

Section 704(b), as amended by the Tax Reform Act of 1976, provides that a partner's distributive share of income, gain, loss, deduction, or credit (or item thereof) is determined in accordance with such partner's interest in the partnership (determined by taking into account all facts and circumstances) if either the partnership agreement does not provide for the distributive share, or the allocation to the partner under the partnership agreement does not have substantial economic effect.

The final regulations provide rules and examples relating to the substantial economic effect test and to the determination of a partner's interest in the partnership. An allocation that does not meet the substantial economic effect test will not be disturbed if it is consistent with the partners' interests in the partnership. Special rules provide that certain allocations will be deemed to be in accordance with the partners' interests in the partnership.

SUBSTANTIAL ECONOMIC EFFECT

The final regulations provide that the determination of whether an allocation has substantial economic effect involves a two-part test. Under the first part of the test, the allocation must have economic effect. This means that in the event there is an economic benefit or burden that corresponds to an allocation, the partner receiving such allocation will receive such benefit or bear such burden. Generally, an allocation will not have economic effect unless the partners' capital accounts are maintained properly, liquidation proceeds are required to be distributed in accordance with the partners' capital account balances, and, following the distribution of such proceeds, partners are required to restore any deficits in their capital accounts to the partnership.

The final regulations provide rules concerning the sufficiency of a partner's obligation to restore the deficit balance in his capital account to the partnership. With respect to this deficit makeup requirement, the regulations make clear that the obligation to restore need not be unlimited. If certain other requirements are satisfied, an allocation of loss or deduction to a partner that creates or increases a deficit balance in such partner's capital account will be respected so long as such deficit balance does not exceed the dollar amount that such partner is obligated to restore.

The final regulations also provide for an economic effect equivalence test under which allocations have economic effect even though capital accounts are not maintained in accordance with the regulations so long as the same results as would be obtained under a capital account analysis are produced in all possible cases.

Under the second part of the two-part test, the economic effect of the allocation must be substantial. The general rules under this second test require that the allocation have a reasonable possibility of affecting the dollar amounts to be received by the partners, independent of tax consequences. Furthermore, these general rules provide that an allocation is insubstantial if, as a result of the allocation, the after-tax economic consequences of at least one partner may, in present value terms, be enhanced, and there is a strong likelihood that the after-tax economic consequences of no partner will, in present value terms, be diminished. The final regulations provide specifically that allocations are insubstantial if they merely shift tax consequences within a partnership taxable year or are likely to be offset by other allocations in subsequent taxable years.

CAPITAL ACCOUNTS

The final regulations provide rules concerning the proper determination and maintenance of the partners' capital accounts. Under these rules a partner's capital account must be increased by the amount of money contributed by such partner to the partnership and allocations to such partner of income (including tax-exempt income) and gain, and must be decreased by the amount of money distributed to such partner by the partnership and allocations to such partner of loss, deduction, and section 705(a)(2)(B) expenditures. In the case of contributed property and property distributed in kind, the regulations adopt a fair market value approach. Thus, a partner's capital account must be increased by the fair market value of the property he contributes to the partnership (rather than its adjusted tax basis) and must be decreased by the fair market value of property distributed to him by the partnership. Consistent with these rules, the final regulations require a preliquidation adjustment to be made to capital accounts to reflect unrealized appreciation or depreciation in the value of distributed property.

The final regulations are permit adjustments to the partners' capital accounts to reflect unrealized appreciation or depreciation in partnership property in connection with the acquisition of an interest from the partnership and the disposition of an interest to the partnership, and in certain other specified circumstances. Additional rules provide for adjustments to the partners' capital accounts to reflect basis adjustments under section 48(q), syndication expenses under section 709, disallowed losses under sections 267(b) and 707(b), transfers of partnership interests, section 754 elections, and depletion, gain, and loss in respect of partnership oil and gas properties.

The final regulations provide examples relating to the substantial economic effect test. To the extent an allocation fails the substantial economic effect test and is inconsistent with the partners' interests in the partnership, it will be reallocated in accordance with the partners' interests in the partnership.

PARTNER'S INTEREST IN THE PARTNERSHIP

Section 704(b) provides that a partner's interest in the partnership shall be determined by taking into account all the facts and circumstances. The final regulations provide rules and examples for determining a partner's interest in the partnership. Under the final regulations a partner's interest in the partnership is to be determined with reference to the underlying economic arrangement of the partners relating to the particular allocation under consideration. If the economic arrangement cannot be determined, each partner's interest in the partnership is presumed to be equal. The examples contained in the final regulations specify, in certain situations, the partners' interests in the partnership.

SPECIAL RULES

The final regulations contain special rules concerning allocations of tax credits, allocations of excess percentage depletion, and allocations of tax items where there has been a revaluation of partnership property. Allocations made in accordance with these special rules are deemed to be in accordance with the partners' interests in the partnership. Finally, the regulations contain rules for determining, in certain instances, the partners' allocable shares of adjusted basis and amount realized under section 613A(c)(7)(D).

PUBLIC COMMENTS AND CHANGES IN RESPONSE TO PUBLIC COMMENTS EFFECTIVE DATE

Several public comments questioned the statement in the proposed regulations that the fundamental principles of the rules contained therein relating to substantial economic effect would be applicable to taxable years beginning after December 31, 1975. The effective date rules have been clarified in the final regulations to make clear that the detailed requirements contained in the regulations concerning the maintenance of capital accounts are not mandated for taxable years beginning before May 1, 1986. The final regulations provide that, for taxable years beginning after December 31, 1975, but before May 1, 1986, an allocation that does not have substantial economic effect under the final regulations nevertheless may have substantial economic effect under section 704(b), as interpreted by case law prior regulations, and the legislative history of the Tax Reform Act of 1976. In addition, in order to permit existing partnerships to begin complying with the capital accounting rules contained in the final regulations for future taxable years, the final regulations allow existing partnerships to restate their capital accounts, as of the beginning of their first taxable year for which the final regulations are effective, to reflect the manner in which partnership property would be distributed if the partnership were liquidated at that time.

ALLOCATIONS ATTRIBUTABLE TO NONRECOURSE DEBT

Several comments suggested that the so-called minimum gain rule contained in the proposed regulations was too restrictive. These comments contended that allocations attributable to nonrecourse debt should be permitted (without reference to minimum gain) to the extent the value of the property securing such debt exceeds the balance of the debt. Other comments urged that the nonrecourse rule was too lenient, and that, under the statute, deductions attributable to nonrecourse debt must follow the partners' interests in the partnership. These comments asserted that the minimum gain rule was inconsistent with such interests and proposed alternative measurements which the commentators felt would be more indicative of the partners' interests in the partnership. In addition, some comments pointed out certain technical deficiencies in the proposed regulations. The Treasury Department and the Internal Revenue Service are still considering the issues raised by these comments and, accordingly, have decided to defer any action on the portion of the proposed regulations concerning allocations attributable to nonrecourse debt.

APPLICATION OF PROFIT MOTIVE TEST AT THE PARTNER LEVEL

Several comments criticized the inference in the proposed regulations that the profit motive test of section 183 would be applied at the partner level for purposes of determining the deductibility of a partner's share of partnership losses or expenses. Since the Treasury Department and the Internal Revenue Service agree that it is inappropriate to decide in these regulations whether section 183 applies at the partner level, the reference to section 183 is deleted and replaced with the case law requirement that the partner receiving an allocation have a bona-fide motive for economic gain, independent of tax consequences.

INTERACTION BETWEEN SECTION 704(b) AND SECTION 704(c)

Several comments concerned the relationship between the proposed rules relating to allocations under section 704(b) and the rules under section 704(c) relating to the determination of the partners' distributive shares of certain tax items with respect to contributed property. Specifically, some comments criticized the general rule in the proposed regulations that contributed property be reflected in capital accounts at its adjusted tax basis, even though an optional rule permitted the property to be reflected in capital accounts at fair market value if certain conditions were satisfied.

The final regulations clarify the relationship between section 704(c) and section 704(b) allocations. In view of the comments received and recent amendments to section 704(c), the suggestion that contributed property be required to be reflected in the contributing partner's capital account at fair market value (rather than adjusted tax basis) has been adopted in the final regulations.

The final regulations make clear that, if section 704(c) determines the partners' distributive shares of depreciation, depletion, and gain or loss with respect to the contributed property, such determination is not subject to the substantial economic effect test of section 704(b). However, the final regulations also make clear that in these cases the partners' distributive shares of the corresponding book items are determined under section 704(b) and the final regulations, and that it is with reference to that determination that section 704(c) determines the partners' distributive shares of the tax items.

Some comments questioned the reference to section 704(c) principles for purposes of determining the partners' shares of depreciation, depletion, and gain or loss, as computed for tax purposes, when capital accounts are adjusted to reflect unrealized appreciation or depreciation in partnership property. The final regulations clarify this reference and provide additional rules for certain cases not expressly addressed under the existing section 704(c) regulations. It is expected that similar rules will be included when new regulations under section 704(c) are proposed and that additional guidance will be contained in those regulations.

TWO-PART SUBSTANTIAL ECONOMIC EFFECT TEST

Several comments challenged the elevation of "substantiality" to a separate test within the substantial economic effect determination. Some comments asserted that absolute economic effect was not necessary to meet the statutory test. These comments were given careful consideration. Nevertheless, the Treasury Department and the Internal Revenue Service maintain that an allocation must have economic effect and that such economic effect must be substantial.

Several comments asserted that the substantiality test was vague and subjective, resulting in undue uncertainty. Although the concept of substantiality by its nature is not easily susceptible to mechanical tests, the final regulations provide clarification and additional guidance on theissue of substantiality. In particular, the final regulations make clear that the timing of the economic consequences that correspond to an allocation are taken into account in determining whether the economic effect of such allocation is substantial. The Treasury Department and the Internal Revenue Service are considering whether further guidance is warranted concerning the relationship of the substantial economic effect test to time value of money principles. *See* H.R. Rep. No. 99-426, 99th Cong., 1st Sess. 259 (1985). To assist in this consideration, comments from interested parties are invited.

DEFICIT MAKE-UP REQUIREMENT

Several comments questioned the necessity for the deficit make-up requirement in the economic effect test. Many of these comments concerned the applicability of this requirement to limited partners. The Treasury Department and the Internal Revenue Service gave careful consideration to these comments, but by the economic effect test. However, the rule has been clarified in certain respects. For instance, the final regulations clarify under what circumstances an allocation to a partner who is not obligated to restore the deficit balance in his capital account (or who is obligated to restore only a limited dollar amount of such deficit) will have economic effect. In general, an allocation will have economic effect in such circumstances, provided the allocation does not cause the recipient partner's capital account (as determined taking into account certain adjustments) to become less than zero (or to become negative by more than the amount of his limited deficit make-up obligation), and provided certain other requirements are satisfied.

CAPITAL ACCOUNT MAINTENANCE RULES

Several comments questioned the use of tax accounting principles for maintaining capital accounts. Generally, the final regulations adopt the rule contained in the proposed regulations that requires the partners' capital accounts to reflect tax accounting principles. Nevertheless, the final regulations deviate from this general requirement in two principal respects. First, as described above, the final regulations adopt the suggestion of several commentators that all contributions and distributions of property be reflected in capital accounts at their fair market value when contributed or distributed (rather than at their adjusted tax basis), and that subsequent capital account adjustments in respect of such property reflect this fair market value.

Second, comments suggested that partnerships should have an unlimited right to adjust capital accounts to reflect unrealized appreciation and depreciation in the value of partnership assets. These comments suggested that the rule in the proposed regulations that permits such adjustments to capital accounts only upon the occurrence of certain specified events is too narrow. On the other hand, several members of the accounting profession expressed concern about the reference in the proposed regulations to sound financial accounting principles, since they believe such principles would rarely, if ever, allow capital accounts to be booked to fair market value. Accordingly, the final regulations eliminate this reference and modify the class of cases in which capital accounts may be adjusted to reflect the fair market value of partnership property and still comply with the capital account maintenance rules.

In addition, a number of technical suggestions and modifications relating to the maintenance of capital accounts have been adopted in the final regulations, including provisions to take into account the effect of liabilities and the provisions of sections 48(q), 267, 707(b), 709, and 754.

SIMULATED DEPLETION ALLOWANCE

A number of comments suggested that the rule requiring adjustments to capital account balances to reflect a simulated partnership depletion allowance be changed to allow partnerships to choose to adjust capital accounts by the actual depletion deductions taken by the partners. This suggestion has been adopted. A modified form of simulated depletion is retained as an option for those partnerships that elect it.

ECONOMIC EFFECT EQUIVALENCE

Several comments questioned the strictness of the capital account equivalence test. Some comments asked for a more liberal test, whereas others suggested certain technical and clarifying changes. Given that the taxpayer has the benefit of certain special rules deeming certain allocations to be consistent with the partners' interests in the partnership and the opportunity to demonstrate by the facts and circumstances that an allocation is in accordance with a partner's interest in the partnership, the test in the proposed regulations (which, for the sake of precision, has been relabeled the economic effect equivalence test) has not been liberalized, but its application has been clarified.

PARTNERS' INTERESTS IN THE PARTNERSHIP

A number of comments asked for more guidance concerning how to determine a partner's interest in the partnership in various factual settings. Specific comments questioned the effect that a reallocation of an item would have on prior or subsequent allocations. The final regulations provide additional guidance in certain cases.

EXAMPLE (19)(iii)

In the proposed regulations, public comment was specifically requested on how to apply the partners' interests in the partnership test to the facts in example (19)(iii) of the proposed regulations. After studying the public comments, the Treasury Department and the Internal Revenue Service have determined that under the standard in §1.704-1(b)(3) both partners in example (19)(iii) of the proposed regulations are equal partners. The final regulations have incorporated this additional guidance into example (19)(iii).

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. The Internal Revenue Service has concluded that the final regulations contained herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is John G. Schmalz of the legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and the Treasury Department participated in developing these regulations both on matters of substance and style.

* * * *

Adoption of amendments to the regulations

Accordingly, effective for partnership taxable years beginning after April 30, 1986, 26 CFR Part 1 is amended to read as follows:

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805.* * *

Par. 2. Section 1.704-1 is amended by revising paragraph § 1.704-1(b) is revised to read as follows:

§1.704-1 Partner's distributive share.

* * * * *

(b) *Determination of partner's distributive share*—(0) *Cross-references.*

Heading	*Section*
Cross-references	1.704-1(b)(0)
In general	1.704-1(b)(1)
Basic principles	1.704-1(b)(1)(i)
Effective dates	1.704-1(b)(1)(ii)
Effect of other sections	1.704-1(b)(1)(iii)
Other possible tax consequences	1.704-1(b)(1)(iv)
Purported allocations	1.704-1(b)(1)(v)
Section 704(c) determinations	1.704-1(b)(1)(vi)
Bottom line allocations	1.704-1(b)(1)(vii)
Substantial economic effect	1.704-1(b)(2)
Two-part analysis	1.704-1(b)(2)(i)
Economic effect	1.704-1(b)(2)(ii)
Fundamental principles	1.704-1(b)(2)(ii)*(a)*
Three requirements	1.704-1(b)(2)(ii)*(b)*
Obligation to restore deficit	1.704-1(b)(2)(ii)*(c)*
Alternate test for economic effect	1.704-1(b)(2)(ii)*(d)*
Partial economic effect	1.704-1(b)(2)(ii)*(e)*
Reduction of obligation to restore	1.704-1(b)(2)(ii)*(f)*
Liquidation defined	1.704-1(b)(2)(ii)*(g)*
Partnership agreement defined	1.704-1(b)(2)(ii)*(h)*
Economic effect equivalence	1.704-1(b)(2)(ii)*(i)*
Substantiality	1.704-1(b)(2)(iii)
General rules	1.704-1(b)(2)(iii)*(a)*
Shifting tax consequences	1.704-1(b)(2)(iii)*(b)*
Transitory allocations	1.704-1(b)(2)(iii)*(c)*
Allocations with economic deferral	1.704-1(b)(2)(iii)*(d)*
Maintenance of capital accounts	1.704-1(b)(2)(iv)
In general	1.704-1(b)(2)(iv)*(a)*
Basic rules	1.704-1(b)(2)(iv)*(b)*
Treatment of liabilities	1.704-1(b)(2)(iv)*(c)*
Contributed property	1.704-1(b)(2)(iv)*(d)*
In general	1.704-1(b)(2)(iv)*(d)(1)*
Contribution of promissory notes	1.704-1(b)(2)(iv)*(d)(2)*
Section 704(c) considerations	1.704-1(b)(2)(iv)(d)*(3)*

Heading	*Section*
Distributed property	1.704-1(b)(2)(iv)*(e)*
In general	1.704-1(b)(2)(iv)*(e)(1)*
Distribution of promisory notes	1.704-1(b)(2)(iv)*(e)(2)*
Revaluations of property	1.704-1(b)(2)(iv)*(f)*
Adjustments to reflect book value	1.704-1(b)(2)(iv)*(g)*
In general	1.704-1(b)(2)(iv)*(g)(1)*
Payables and receivables	1.704-1(b)(2)(iv)*(g)(2)*
Determining amount of book items	1.704-1(b)(2)(iv)*(g)(3)*
Determinations of fair market value	1.704-1(b)(2)(iv)*(h)*
Section 705(a)(2)(B) expenditures	1.704-1(b)(2)(iv)*(i)*
In general	1.704-1(b)(2)(iv)*(i)(1)*
Expenses described in section 709	1.704-1(b)(2)(iv)*(i)(2)*
Disallowed losses	1.704-1(b)(2)(iv)*(i)(3)*
Basis adjustments to section 38 property	1.704-1(b)(2)(iv)*(j)*
Depletion of oil and gas properties	1.704-1(b)(2)(iv)*(k)*
In general	1.704-1(b)(2)(iv)*(k)(1)*
Simulated depletion	1.704-1(b)(2)(iv)*(k)(2)*
Actual depletion	1.704-1(b)(2)(iv)*(k)(3)*
Effect of book values	1.704-1(b)(2)(iv)*(k)(4)*
Transfers of partnership interests	1.704-1(b)(2)(iv)*(l)*
Section 754 elections	1.704-1(b)(2)(iv)*(m)*
In general	1.704-1(b)(2)(iv)*(m)(1)*
Section 743 adjustments	1.704-1(b)(2)(iv)*(m)(2)*
Section 732 adjustments	1.704-1(b)(2)(iv)*(m)(3)*
Section 734 adjustments	1.704-1(b)(2)(iv)*(m)(4)*
Limitations on adjustments	1.704-1(b)(2)(iv)*(m)(5)*
Partnership level characterization	1.704-1(b)(2)(iv)*(n)*
Guaranteed payments	1.704-1(b)(2)(iv)*(o)*
Minor discrepancies	1.704-1(b)(2)(iv)*(p)*
Adjustments where guidance is lacking	1.704-1(b)(2)(iv)*(q)*
Restatement of capital accounts	1.704-1(b)(2)(iv)*(r)*
Partner's interest in the partnership	1.704-1(b)(3)
In general	1.704-1(b)(3)(i)
Factors considered	1.704-1(b)(3)(ii)
Certain determinations	1.704-1(b)(3)(iii)
Special rules	1.704-1(b)(4)
Allocations to reflect revaluations	1.704-1(b)(4)(i)
Credits	1.704-1(b)(4)(ii)
Excess percentage depletion	1.704-1(b)(4)(iii)
Nonrecourse debt	1.704-1(b)(4)(iv)
Allocations under section 613A(c)(7)(D)	1.704-1(b)(4)(v)
Amendments to partnership agreement	1.704-1(b)(4)(vi)
Recapture	1.704-1(b)(4)(vii)
Examples	1.704-1(b)(5)

(1) *In general*—(i) *Basic principles*. Under section 704(b) if a partnership agreement does not provide for the allocation of income, gain, loss, deduction, or credit (or item thereof) to a partner, or if the partnership agreement provides for the allocation of income, gain, loss, deduction, or credit (or item thereof) to a partner but such allocation does not have substantial economic effect, then the partner's distributive share of such income, gain, loss, deduction, or credit (or item thereof) shall be determined in accordance with such partner's interest in the partnership (taking into account all facts and circumstances). If the partnership agreement provides for the allocation of income, gain, loss, deduction, or credit (or item thereof) to a partner, there are three ways in which such allocation will be respected under section 704(b) and this paragraph. First, the allocation can have substantial economic effect in accordance with paragraph (b)(2) of this section. Second, taking into account all facts and circumstances, the allocation can be in accordance with the partner's interest in the partnership. See paragraph (b)(3) of this section. Third, the allocation can be deemed to be in accordance with the partner's interest in the partnership pursuant to one of the special rules contained in paragraph (b)(4) of this section. To the extent an allocation under the partnership agreement of income, gain, loss, deduction, or credit (or item thereof) to a partner does not have substantial economic effect, is not in accordance with the partner's interest in the partnership, and is not deemed to be in accordance with the partner's interest in the partnership, such income, gain, loss, deduction, or credit (or item thereof) will be reallocated in accordance with the partner's interest in partnership (determined under paragraph (b)(3) of this section).

(ii) *Effective dates*. The provisions of this paragraph are effective for partnership taxable years beginning after December 31, 1975. However, for partnership taxable years beginning after December 31, 1975, but before May 1, 1986, an allocation of income, gain, loss, deduction, or credit (or item thereof) to a partner that is not respected under this paragraph nevertheless will be respected under section 704(b) if such allocation has substantial economic effect as that term has been interpreted under the relevant case law, the legislative history of section 210(d) of the Tax Reform Act of 1976, and the provisions of this paragraph in effect for partnership taxable years beginning before May 1, 1986.

(iii) *Effect of other sections*. The determination of a partner's distributive share of income, gain, loss, deduction, or credit (or item thereof) under section 704(b) and this paragraph is not conclusive as to the tax treatment of a partner with respect to such distributive share. For example, an allocation of loss or deduction to a partner that is respected under section 704(b) and this paragraph may not be deductible by such partner if the partner lacks the requisite motive for economic gain (see, *e.g.*, *Goldstein v. Commissioner*, 364 F.2d 734 (2d Cir. 1966)), or may be disallowed for that taxable year (and held in suspense) if the limitations of section 465 or section 704(d) are applicable. Similarly, an allocation that is respected under section 704(b) and this paragraph nevertheless may be reallocated under other provisions, such as section 482, section 704(e)(2), section 706(d) (and related assignment of income principles), and paragraph (b)(2)(ii) of §1.751-1. If a partnership has a section 754 election in effect, a partner's distributive share of partnership income, gain, loss, or deduction may be affected as provided in §1.743-1 (see paragraph (b)(2)(iv)*(m)(2)* of this section). The examples in paragraph (b)(5) of this section concern the validity of allocations under section 704(b) and this paragraph and, except as noted, do not address other tax consequences that may result from such allocations.

(v) *Purported allocations.* Section 704(b) and this paragraph do not apply to a purported allocation if it is made to a person who is not a partner of the partnership (see section 7701(a)(2) and paragraph (d) of §301.7701-3) or to a person who is not receiving the purported allocation in his capacity as a partner (see section 707(a) and paragraph (a) of §1.707-1).

(vi) *Section 704(c) determinations.* Under section 704(c) if property is contributed by a partner to a partnership, the partners' distributive shares of income, gain, loss, and deduction, as computed for tax purposes, with respect to such property are determined so as to take account of the variation between the adjusted tax basis and fair market value of such property. Although section 704(b) does not directly determine the partners' distributive shares of tax items governed by section 704(c), the partners' distributive shares of tax items are determined under section 704(c) with reference to the partners' distributive shares of the corresponding book items, as determined under section 704(b) and this paragraph. (See paragraphs (b)(2)(iv)*(d)* and (b)(4)(i) of this section.) Section 704(c), as cited in this paragraph, refers to such section as in effect for property contributed to a partnership after March 31, 1984. See example (13)(i) of paragraph (b)(5) of this section.

(vii) *Bottom line allocations.* Section 704(b) and this paragraph are applicable to allocations of income, gain, loss, deduction, and credit, allocations of specific items of income, gain, loss, deduction, and credit, and allocations of partnership net or "bottom line" taxable income and loss. An allocation to a partner of a share of partnership net or "bottom line" taxable income or loss shall be treated as an allocation to such partner of the same share of each item of income, gain, loss, and deduction that is taken into account in computing such net or "bottom line" taxable income or loss. See example (15)(i) of paragraph (b)(5) of this section.

(2) *Substantial economic effect*—(i) *Two-part analysis.* The determination of whether an allocation of income, gain, loss, or deduction (or item thereof) to a partner has substantial economic effect involves a two-part analysis that is made as of the end of the partnership taxable year to which the allocation relates. First, the allocation must have economic effect (within the meaning of paragraph (b)(2)(ii) of this section). Second, the economic effect of the allocation must be substantial (within the meaning of paragraph (b)(2)(iii) of this section).

(ii) *Economic effect—(a) Fundamental principles.* In order for an allocation to have economic effect, it must be consistent with the underlying economic arrangement of the partners. This means that in the event there is an economic benefit or economic burden that corresponds to an allocation, the partner to whom the allocation is made must receive such economic benefit or bear such economic burden.

(b) Three requirements. Based on the principles contained in paragraph (b)(2)(ii)*(a)* of this section, and except as otherwise provided in this paragraph, an allocation of income, gain, loss, or deduction (or item thereof) to a partner will have economic effect if, and only if, throughout the full term of the partnership, the partnership agreement provides—

(1) For the determination and maintenance of the partners' capital accounts in accordance with the rules of paragraph (b)(2)(iv) of this section,

(2) Upon liquidation of the partnership (or any partner's interest in the partnership), liquidating distributions are required in all cases to be made in accordance with the positive capital account balances of the partners, as determined after taking into account all capital account adjustments for the partnership taxable year during which such liquidation occurs (other than those made pursuant to this requirement *(2)* and requirement *(3)* of this paragraph (b)(2)(ii)*(b)*), by the end of such taxable year (or, if later, within 90 days after the date of such liquidation), and

(3) If such partner has a deficit balance in his capital account following the liquidation of his interest in the partnership, as determined after taking into account all capital account adjustments for the partnership taxable year during which such liquidation occurs (other than those made pursuant to this requirement *(3)*), he is unconditionally obligated to restore the amount of such deficit balance to the partnership by the end of such taxable year (or, if later, within 90 days after the date of such liquidation), which amount shall, upon liquidation of the partnership, be paid to creditors of the partnership or distributed to other partners in accordance with their positive capital account balances (in accordance with requirement *(2)* of this paragraph (b)(2)*(ii)*(*b*)).

For purposes of the preceding sentence, a partnership taxable year shall be determined without regard to section 706(c)(2)(A). See examples (1)(i) and (ii), (4)(i), (8)(i), and (16)(i) of paragraph (b)(5) of this section.

(c) Obligation to restore deficit. If a partner is not expressly obligated to restore the deficit balance in his capital account, such partner nevertheless will be treated as obligated to restore the deficit balance in his capital account (in accordance with requirement *(3)* of paragraph (b)(2)(ii)((*b*) of this section) to the extent of—

(1) The outstanding principal balance of any promissory note (of which such partner is the marker) contributed to the partnership by such partner (other than a promissory note that is readily tradable on an established securities market), and

(2) The amount of any unconditional obligation of such partner (whether imposed by the partnership agreement or by State or local law) to make subsequent contributions to the partnership (other than pursuant to a promissory note of which such partner is the marker),

provided that such note or obligation is required to be satisfied at a time no later than the end of the partnership taxable year in which such partner's interest is liquidated (or, if later, within 90 days after the date of such liquidation). If a promissory note referred to in the previous sentence is negotiable, a partner will be considered required to satisfy such note within the time period specified in such sentence if the partnership agreement provides that, in lieu of actual satisfaction, the partnership will retain such note and such partner will contribute to the partnership the excess, if any, of the outstanding principal balance of such note over its fair market value at the time of liquidation. See paragraph (b)(2)(iv)*(d)(2)* of this section. See examples (1)(ix) and (x) of paragraph (b)(5) of this section. A partner in no event will be considered obligated to restore the deficit balance in his capital account to the partnership (in accordance with requirement *(3)* of paragraph (b)(2)(ii)*(b)* of this section) to the extent such partner's obligation is not legally enforceable, or the facts and circumstances otherwise indicate a plan to avoid or circumvent such obligation. See paragraphs (b)(2)(ii)*(f)*, (b)(2)(ii)*(h)*, and (b)(4)(vi) of this section for other rules regarding such obligation.

(d) Alternate test for economic effect. If—

(1) Requirements *(1)* and *(2)* of paragraph (b)(2)(ii)*(b)* of this section are satisfied, and

(2) The partner to whom an allocation is made is not obligated to restore the deficit balance in his capital account to the partnership (in accordance with requirement *(3)* of paragraph (b)(2)(ii)*(b)* of this section), or is obligated to restore only a limited dollar amount of such deficit balance, and

(3) The partnership agreement contains a "qualified income offset,"

such allocation will be considered to have economic effect under this paragraph (b)(2)(ii)*(d)* to the extent such allocation does not cause or increase a deficit balance in such partner's capital account (in excess of any limited dollar amount of such deficit balance that such partner is obligated to restore) as of the end of the partnership taxable year to which such allocation relates. In determining the extent to which the previous sentence is satisfied, such partner's capital account also shall be reduced for—

(4) Adjustments that, as of the end of such year, reasonably are expected to be made to such partner's capital account under paragraph (b)(2)(iv)*(k)* of this section for depletion allowances with respect to oil and gas properties of the partnership, and

(5) Allocations of loss and deduction that, as of the end of such year, reasonably are expected to be made to such partner pursuant to section 704(e)(2), section 706(d), and paragraph (b)(2)(ii) of §1.751-1, and

(6) Distributions that, as of the end of such year, reasonably are expected to be made to such partner to the extent they exceed offsetting increases to such partner's capital account that reasonably are expected to occur during (or prior to) the partnership taxable years in which such distributions reasonably are expected to be made.

For purposes of determining the amount of expected distributions and expected capital account increases described in *(6)* above, the rule set out in paragraph (b)(2)(iii)*(c)* of this section concerning the presumed value of partnership property shall apply. The partnership agreement contains a "qualified income offset" if, and only if, it provides that a partner who unexpectedly receives an adjustment, allocation, or distribution described in *(4)*, *(5)*, or *(6)* above, will be allocated items of income and gain in an amount and manner sufficient to eliminate such deficit balance as quickly as possible. See examples (1)(iii), (iv), (v), (vi), (viii), (ix), and (x), (15), and (16)(ii) of paragraph (b)(5) of this section.

(e) Partial economic effect. If only a portion of an allocation made to a partner with respect to a partnership taxable year has economic effect, both the portion that has economic effect and the portion that is reallocated shall consist of a proportionate share of all items that made up the allocation to such partner for such year. See examples (15)(ii) and (iii) of paragraph (b)(5) of this section.

(f) Reduction of obligation to restore. If requirements *(1)* and *(2)* of paragraph (b)(2)(ii)*(b)* of this section are satisfied, a partner's obligation to restore the deficit balance in his capital account (or any limited dollar amount thereof) to the partnership may be eliminated or reduced as of the end of a partnership taxable year without affecting the validity of prior allocations (see paragraph (b)(4)(vi) of this section) to the extent the deficit balance (if any) in such partner's capital account, after reduction for the items described in *(4)*, *(5)*, and *(6)* of paragraph (b)(2)(iv)*(d)* of this section, will not exceed the partner's remaining obligation (if any) to restore the deficit balance in his capital account. See example (1)(viii) of paragraph (b)(5) of this section.

(g) Liquidation defined. For purposes of this paragraph, a liquidation of a partner's interest in the partnership occurs upon the earlier of *(1)* the date upon which there is a liquidation of the partnership, or *(2)* the date upon which there is a liquidation of the partner's interest in the partnership under paragraph (d) of §1.761-1. For purposes of this paragraph, the liquidation of a partnership occurs upon the earlier of *(3)* the date upon which the partnership is terminated under section 708(b)(1), or *(4)* the date upon which the partnership ceases to be a going concern even though it may continue in existence for the purpose of winding up its affairs, paying its debts, and distributing any remaining balance to its partners). Requirements *(2)* and *(3)* of paragraph (b)(2)(ii)*(b)* of this section will be considered unsatisfied if the liquidation of a partner's interest in the partnership is delayed after its primary business activities have been terminated (for example, by continuing to engage in a relatively minor amount of business activity, if such actions themselves do not cause the partnership to terminate pursuant to section 708(b)(1)) for a principal purpose of deferring any distribution pursuant to requirement *(2)* of paragraph (b)(2)(ii)*(b)* of this section or deferring any partner's obligation under requirement *(3)* of paragraph (b)(2)(ii)*(b)* of this section.

(h) Partnership agreement defined. For purposes of this paragraph, the partnership agreement includes all agreements among the partners, or between one or more partners and the partnership, concerning affairs of the partnership and responsibilities of partners, whether oral or written, and whether or not embodied in a document referred to by the partners as the partnership agreement. Thus, in determining whether distributions are required in all cases to be made in accordance with the partners' positive capital account balances (requirement *(2)* of paragraph (b)(2)(ii)*(b)* of this section), and in determining the extent to which a partner is obligated to restore a deficit balance in his capital account (requirement *(3)* of paragraph (b)(2)(ii)*(b)* of

this section), all arrangements among partners, or between one or more partners and the partnership relating to the partnership, direct and indirect, including puts, options, and other buy-sell agreements, and any other "stop-loss" arrangement, are considered to be part of the partnership agreement. In addition, the partnership agreement includes provisions of Federal, State, or local law that govern the affairs of the partnership or are considered under such law to be a part of the partnership agreement (see the last sentence of paragraph (c) of §1.761-1). For purposes of this paragraph (b)(2)(ii)*(h)*, an agreement with a partner of a partnership shall include an agreement with a person related, within the meaning of section 267(b) (without modification by section 267(e)(1)) of section 707(b)(1), to such partner.

(i) Economic effect equivalence. Allocations made to a partner that do not otherwise have economic effect under this paragraph (b)(2)(ii) shall nevertheless have economic effect, provided that the partnership agreement ensures that a liquidation of the partnership as of the end of each partnership taxable year will produce the same economic results to the partners as would occur if requirements *(1)*, *(2)*, and *(3)* of paragraph (b)(2)(ii)*(b)* of this section had been satisfied. See examples (4)(ii) and (iii) of paragraph (b)(5) of this section.

(iii) *Substantiality—(a) General rules.* Except as otherwise provided in this paragraph (b)(2)(iii), the economic effect of an allocation (or allocations) is substantial if there is a reasonable possibility that the allocation (or allocations) will affect substantially the dollar amounts to be received by the partners from the partnership, independent of tax consequences. Notwithstanding the preceding sentence, the economic effect of an allocation (or allocations) is not substantial if, at the time the allocation becomes part of the partnership agreement, *(1)* the after-tax economic consequences of at least one partner may, in present value terms, be enhanced compared to such consequences if the allocation (or allocations were not contained in the partnership agreement, and *(2)* there is a strong likelihood that the after-tax economic consequences of no partner will, in present value terms, be substantially diminished compared to such consequences if the allocation (or allocations) were not contained in the partnership agreement. In determining the after-tax economic benefit or detriment to a partner, tax consequences that result from the interaction of the allocation with such partner's tax attributes that are unrelated to the partnership will be taken into account. See examples (5) and (9) of paragraph (b)(5) of this section. The economic effect of an allocation is not substantial in the two situations described in paragraphs (b)(2)(iii)*(b)* and *(c)* of this section. However, even if an allocation is not described therein, its economic effect may be insubstantial under the general rules stated in this paragraph (b)(2)(iii)*(a)*. References in this paragraph (b)(2)(iii) to allocations includes capital account adjustments made pursuant to paragraph (b)(2)(iv)*(k)* of this section.

(b) Shifting tax consequences. The economic effect of an allocation (or allocations) in a partnership taxable year is not substantial if, at the time the allocation (or allocations) becomes part of the partnership agreement, there is a strong likelihood that—

(1) The net increases and decreases that will be recorded in the partners' respective capital accounts for such taxable year will not differ substantially from the net increases and decreases that would be recorded in such partners' respective capital accounts for such year if the allocations were not contained in the partnership agreement, and

(2) The total tax liability of the partners (for their respective taxable years in which the allocations will be taken into account) will be less than if the allocations were not contained in the partnership agreement (talking into account tax consequences that result from the interaction of the allocation (or allocations) with partner tax attributes that are unrelated to the partnership).

If, at the end of a partnership taxable year to which an allocation (or allocations) relates, the net increases and decreases that are recorded in the partners' respective capital accounts do not differ substantially from the net increases and decreases that would have been recorded in such partners' respective capital accounts had the allocation (or allocations) not been contained in the partnership agreement, and the total tax liability of the partners is (as described in *(2)* above) less than it would have been had the allocation (or allocations) not been contained in the partnership agreement, it will be presumed that, at the time the allocation (or allocations) became part of such partnership agreement, there was a strong likelihood that these results would occur. This presumption may be overcome by a showing of facts and circumstances that prove otherwise. See examples (6), (7)(ii) and (iii), and (10)(ii) of paragraph (b)(5) of this section.

(c) Transitory allocations. If a partnership agreement provides for the possibility that one or more allocations (the "original allocation(s)") will be largely offset by one or more other allocations (the "offsetting allocations(s)"), and, at the time the allocations become part of the partnership agreement, there is a strong likelihood that—

(1) The net increases and decreases that will be recorded in the partners' respective capital accounts for the taxable years to which the allocations relate will not differ substantially from the net increases and decreases that would be recorded in such partners' respective capital accounts for such years if the original allocation(s) and offsetting allocation(s) were not contained in the partnership agreement, and

(2) The total tax liability of the partners (for their respective taxable years in which the allocations will be taken into account) will be less than if the allocations were not contained in the partnership agreement (taking into account tax consequences that result from the interaction of the allocation (or allocations) with partner tax attributes that are unrelated to the partnership)

the economic effect of the original allocation(s) and offsetting allocation(s) will not be substantial. If, at the end of a partnership taxable year to which an offsetting allocation(s) relates, the net increases and decreases recorded in the partners' respective capital accounts do not differ substantially from the net increases and decreases that would have been recorded in such partners' respective capital accounts had the original allocation(s) and the offsetting allocation(s) not been contained in the partnership agreement, and the total tax liability of the partners is (as described in *(2)* above) less than it would have been had such allocations not been contained in the partnership agreement, it will be presumed that, at the time the allocations became part of the partnership agreement, there was a strong likelihood that these results would occur. This presumption may be overcome by a showing of facts and circumstances that prove otherwise. See examples (1)(xi), (2), (3), (7)(i) and (iv), (8)(ii), and (17) of paragraph (b)(5) of this section. Notwithstanding the foregoing, the original allocation(s) and the offsetting allocation(s) will not be insubstantial (under this paragraph (b)(2)(iii)(*c*)) if, at the time the allocations become part of the partnership agreement, there is a strong likelihood that the offsetting allocation(s) will not, in large part, be made within five years after the original allocation(s) is made (determined on a first-in, first-out basis). See example (2) of paragraph (b)(5) of this section. For purposes of applying the provisions of this paragraph (b)(2)(iii) (and paragraphs (b)(2)(ii)(*d*)(*6*) and (b)(3)(iii) of this section), the adjusted tax basis of partnership property (or, if partnership property is properly reflected on the books of the partnership at a book value that differs from its adjusted tax basis, the book value of such property) will be presumed to be the fair market value of such property, and adjustments to the adjusted tax basis (or book value) of such property will be presumed to be matched by corresponding changes in such property's fair market value. Thus, there cannot be a strong likelihood that the economic effect of an allocation (or allocations) will be largely offset by an allocation (or allocations) of gain or loss from the disposition of partnership property. See examples (1)(vi) and (xi) of paragraph (b)(5) of this section.

(iv) *Maintenance of capital accounts—(a) In general.* The economic effect test described in paragraph (b)(2)(ii) of this section requires an examination of the capital accounts of the partners of a partnership, as maintained under the partnership agreement. Except as otherwise provided in paragraph (b)(2)(ii)(*i*) of this section, an allocation of income, gain, loss, or deduction will not have economic effect under paragraph (b)(2)(ii) of this section, and will not be deemed to be in accordance with a partner's interest in the partnership under paragraph (b)(4) of this section, unless the capital accounts of the partners are determined and maintained throughout the full term of the partnership in accordance with the capital accounting rules of this paragraph (b)(2)(iv).

(b) Basic rules. Except as otherwise provided in this paragraph (b)(2)(iv), the partners' capital accounts will be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) if, and only if, each partner's capital account is increased by *(1)* the amount of money contributed by him to the partnership, *(2)* the fair market value of property contributed by him to the partnership (net of liabilities securing such contributed property that the partnership is considered to assume or take subject to under section 752), and *(3)* allocations to him of partnership income and gain (or items thereof), including income and gain exempt from tax and income and gain described in paragraph (b)(2)(iv)(*g*) of this section, but excluding income and gain described in paragraph (b)(4)(i) of this section; and is decreased by *(4)* the amount of money distributed to him by the partnership, *(5)* the fair market value of property distributed to him by the partnership (net of liabilities securing such distributed property that such partner is considered to assume or take subject to under section 752), *(6)* allocations to him of expenditures of the partnership described in section 705(a)(2)(B), and *(7)* allocations of partnership loss and deduction (or item thereof), including loss and deduction described in paragraph (b)(2)(iv)(*g*) of this section, but excluding items described in *(6)* above and loss or deduction described in paragraphs (b)(4)(i) or (b)(4)(iii) of this section; and is otherwise adjusted in accordance with the additional rules set forth in this paragraph (b)(2)(iv). For purposes of this paragraph, a partner who has more than one interest in a partnership shall have a single capital account that reflects all such interests, regardless of the class of interests owned by such partner (*e.g.*, general or limited) and regardless of the time or manner in which such interests were acquired.

(c) Treatment of liabilities. For purposes of this paragraph (b)(2)(iv), *(1)* money contributed by a partner to a partnership includes the amount of any partnership liabilities that are assumed by such partner (other than liabilities described in paragraph (b)(2)(iv)(*b*)(*5*) of this section that are assumed by a distributee partner) but does not include increases in such partner's share of partnership liabilities (see section 752(a)), and *(2)* money distributed to a partner by a partnership includes the amount of such partner's individual liabilities that are assumed by the partnership (other than liabilities described in paragraph (b)(2)(iv)(*b*)(*2*) of this section that are assumed by the partnership) but does not include decreases in such partner's share of partnership liabilities (see section 752(b)). For purposes of this paragraph (b)(2)(iv)(*c*), liabilities may be considered to be assumed only to the extent the assuming party is thereby subjected to primary and personal liability with respect to such obligation, and the obligee is aware of the assumption and can directly enforce the assuming party's obligation.

(d) Contributed property—(1) In general. The basic capital accounting rules contained in paragraph (b)(2)(iv)(*b*) of this section require that a partner's capital account be increased by the fair market value of property contributed to the partnership by such partner on the date of contribution. See examples (13)(i) and (v) of paragraph (b)(5) of this section. Consistent with section 752(c), section 7701(g) does not apply in determining such fair market value.

(2) Contribution of promissory notes. Notwithstanding the general rule of paragraph (b)(2)(iv)(*b*)(*2*) of this section, except as provided in this paragraph (b)(2)(iv)(*d*)(*2*), if a promissory note is contributed to a partnership by a partner who is the maker of such note, such partner's capital account will be increased with respect to such note only when there is a taxable disposition of such note by the partnership or when the partner makes principal payments on such note. See example (1)(ix) of paragraph (b)(5) of this section. The first sentence of this paragraph (b)(2)(iv)(*d*)(*2*) shall not apply if the note referred to therein is readily tradable on an established securities market. See also paragraph (b)(2)(ii)(*c*) of this section. Furthermore, a partner whose interest is liquidated will be considered as satisfying his obligation to restore the deficit balance in his capital

account to the extent of *(i)* the fair market value, at the time of contribution, of any negotiable promissory note (of which such partner is the maker) that such partner contributes to the partnership on or after the date his interest is liquidated and within the time specified in paragraph (b)(2)(ii)*(b)(3)* of this section, and *(ii)* the fair market value, at the time of liquidation, of the unsatisfied portion of any negotiable promissory note (of which such partner is the maker) that such partner previously contributed to the partnership. For purposes of the preceding sentence, the fair market value of a note will be no less than the outstanding principal balance of such note, provided that such note bears interest at a rate no less than the applicable federal rate at the time of valuation.

(3) Section 704(c) considerations. Section 704(c) governs the determination of the partners' distributive shares of income, gain, loss, and deduction, as computed for tax purposes, with respect to property contributed to a partnership (see paragraph (b)(1)(iv) of this section). In cases where section 704(c) applies to partnership property, the capital accounts of the partners will not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) unless the partnership agreement requires that the partners' capital accounts be adjusted in accordance with paragraph (b)(2)(iv)*(g)* of this section for allocations to them of depreciation, depletion, amortization, and gain and loss, as computed for book purposes, with respect to such property. See example (13)(i) of paragraph (b)(5) of this section.

(e) Distributed property—(1) In general. The basic capital accounting rules contained in paragraph (b)(2)(iv)*(b)* of this section require that a partner's capital account be decreased by the fair market value of property distributed by the partnership (without regard to section 7701(g)) to such partner (whether in connection with a liquidation or otherwise). To satisfy this requirement, the capital accounts of the partners first must be adjusted to reflect the manner in which the unrealized income, gain, loss, and deduction inherent in such property (that has not been reflected in the capital accounts previously) would be allocated among the partners if there were a taxable disposition of such property for the fair market value of such property (taking section 7701(g) into account) on the date of distribution. See example (14)(v) of paragraph (b)(5) of this section.

(2) Distribution of promissory notes. Notwithstanding the general rule of paragraph (b)(2)(iv)*(b)*(5), except as provided in this paragraph (b)(2)(iv)*(e)(2)*, if a promissory note is distributed to a partner by a partnership that is the maker of such note, such partner's capital account will be decreased with respect to such note only when there is a taxable disposition of such note by the partner or when the partnership makes principal payments on the note. The previous sentence shall not apply if a note distributed to a partner by a partnership who is the maker of such note is readily tradable on an established securities market. Furthermore, the capital account of a partner whose interest in a partnership is liquidated will be reduced to the extent of *(i)* the fair market value, at the time of distribution, of any negotiable promissory note (of which such partnership is the maker) that such partnership distributes to the partner on or after the date such partner's interest is liquidated and within the time specified in paragraph (b)(2)(ii)*(b)(2)* of this section, and *(ii)* the fair market value, at the time of liquidation, of the unsatisfied portion of any negotiable promissory note (of which such partnership is the maker) that such partnership previously distributed to the partner. For purposes of the preceding sentence, the fair market value of a note will be no less than the outstanding principal balance of such note, provided that such note bears interest at a rate no less than the applicable federal rate at the time of valuation.

(f) Revaluations of property. A partnership agreement may, upon the occurrence of certain events, increase or decrease the capital accounts of the partners to reflect a revaluation of partnership property on the partnership's books. Capital accounts so adjusted will not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) unless—

(1) The adjustments are based on the fair market value of partnership property (taking section 7701(g) into account) on the date of adjustment, and

(2) The adjustments reflect the manner in which the unrealized income, gain, loss, or deduction inherent in such property (that has not been reflected in the capital accounts previously) would be allocated among the partners if there were a taxable disposition of such property for such fair market value on that date, and

(3) The partnership agreement requires that the partners' capital accounts be adjusted in accordance with paragraph (b)(2)(iv)*(g)* of this section for allocations to them of depreciation, depletion, amortization, and gain or loss, as computed for book purposes, with respect to such property, and

(4) The partnership agreement requires that the partners' distributive shares of depreciation, depletion, amortization, and gain or loss, as computed for tax purposes, with respect to such property be determined so as to take account of the variation between the adjusted tax basis and book value of such property in the same manner as under section 704(c) (see paragraph (b)(4)(i) of this section), and

(5) The adjustments are made principally for a substantial non-tax business purpose—

(i) In connection with a contribution of money or other property (other than a *de minimis* amount) to the partnership by a new or existing partner as consideration for an interest in the partnership, or

(ii) In connection with a distribution of money or other property (other than a *de minimis* amount) by the partnership to a retiring or continuing partner as consideration for an interest in the partnership, or

(iii) Under generally accepted industry accounting practices, provided substantially all of the partnership's property (excluding money) consists of stock, securities, commodities, options, warrants, futures, or similar instruments that are readily tradable on an established securities market.

See examples (14) and (18) of paragraph (b)(5) of this section. If the capital accounts of the partners are not adjusted to reflect the fair market value of partnership property when an interest in the partnership is acquired from or relinquished to the partnership, paragraphs (b)(1)(iii) and (b)(1)(iv) of this section should be consulted regarding the potential tax consequences that may arise if the principles of section 704(c) are not applied to determine the partners' distributive shares of depreciation, depletion, amortization, and gain or loss, as computed for tax purposes, with respect to such property.

(g) Adjustments to reflect book value—(1) In general. Under paragraphs (b)(2)(iv)*(d)* and (b)(2)(iv)*(f)* of this section, property may be properly reflected on the books of the partnership at a book value that differs from the adjusted tax basis of such property. In these circumstances, paragraphs (b)(2)(iv)*(d)(3)* and (b)(2)(iv)*(f)(3)* of this section provide that the capital accounts of the partners will not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) unless the partnership agreement requires the partners' capital accounts to be adjusted in accordance with this paragraph (b)(2)(iv)*(g)* for allocations to them of depreciation, depletion, amortization, and gain or loss, as computed for book purposes, with respect to such property. In determining whether the economic effect of an allocation of book items is substantial, consideration will be given to the effect of such allocation on the determination of the partners' distributive shares of corresponding tax items under section 704(c) and paragraph (b)(4)(i) of this section. See example (17) of paragraph (b)(5) of this section. If an allocation of book items under the partnership agreement does not have substantial economic effect (as determined under paragraphs (b)(2)(ii) and (b)(2)(iii) of this section), or is not otherwise respected under this paragraph, such items will be reallocated in accordance with the partners' interests in the partnership, and such reallocation will be the basis upon which the partners' distributive shares of the corresponding tax items are determined under section 704(c) and paragraph (b)(4)(i) of this section. See examples (13), (14), and (18) of paragraph (b)(5) of this section.

(2) Payables and receivables. References in this paragraph (b)(2)(iv) and paragraph (b)(4)(i) of this section to book and tax depreciation, depletion, amortization, and gain or loss with respect to property that has an adjusted tax basis that differs from book value include, under analogous rules and principles, the unrealized income or deduction with respect to accounts receivable, accounts payable, and other accrued but unpaid items.

(3) Determining amount of book items. The partners' capital accounts will not be considered adjusted in accordance with this paragraph (b)(2)(iv)*(g)* unless book depreciation, depletion, and amortization with respect to partnership property are computed in accordance with a reasonable method selected by the partnership, and under such method *(i)* if the book value of partnership property exceeds the adjusted tax basis thereof, the depreciation, depletion, or amortization, as computed for book purposes, will be no less than the depreciation, depletion, or amortization, as computed for tax purposes, and *(ii)* if the adjusted tax basis of partnership property exceeds the book value thereof, the depreciation, depletion, or amortization, as computed for book purposes, will be no greater than the depreciation, depletion, or amortization, as computed for tax purposes, and (iii) if the book value of partnership property equals the adjusted tax basis thereof, the depreciation, depletion, or amortization, as computed for book purposes, will equal the depreciation, depletion, or amortization, as computed for tax purposes.

(h) Determinations of fair market value. For purposes of this paragraph (b)(2)(iv), the fair market value assigned to property contributed to a partnership, property distributed by a partnership, or property otherwise revalued by a partnership, will be regarded as correct, provided that *(1)* such value is reasonably agreed to among the partners in arm's-length negotiations, and *(2)* the partners have sufficiently adverse interests. If, however, these conditions are not satisfied and the value assigned to such property is overstated or understated (by more than an insignificant amount), the capital accounts of the partners will not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv). Valuation of property contributed to the partnership, distributed by the partnership, or otherwise revalued by the partnership shall be on a property-by-property basis, except to the extent the regulations under section 704(c) permit otherwise.

(i) Section 705(a)(2)(B) expenditures—(1) In general. The basic capital accounting rules contained in paragraph (b)(2)(iv)*(b)* of this section require that a partner's capital account be decreased by allocations made to such partner of expenditures described in section 705(a)(2)(B). See example (11) of paragraph (b)(5) of this section. If an allocation of these expenditures under the partnership agreement does not have substantial economic effect (as determined under paragraphs (b)(2)(ii) and (b)(2)(iii) of this section), or is not otherwise respected under this paragraph, such expenditures will be reallocated in accordance with the partners' interest in the partnership.

(2) Expenses described in section 709. Except for amounts with respect to which an election is properly made under section 709(b), amounts paid or incurred to organize a partnership or to promote the sale of (or to sell) an interest in such a partnership shall, solely for purposes of this paragraph, be treated as section 705(a)(2)(B) expenditures, and upon liquidation of the partnership no further capital account adjustments will be made in respect thereof.

(3) Disallowed losses. If a deduction for a loss incurred in connection with the sale or exchange of partnership property is disallowed to the partnership under section 267(a)(1) or section 707(b), that deduction shall, solely for purposes of this paragraph, be treated as a section 705(a)(2)(B) expenditure.

(j) Basis adjustments to section 38 property. The capital accounts of the partners will not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) unless such capital accounts are adjusted by the partners' shares of any upward or downward basis adjustments allocated to them under this paragraph (b)(2)(iv)*(j)*. When there is a reduction in the adjusted tax basis of partnership section 38 property under section 48(q)(1) or section 48(q)(3), section 48(q)(6) provides for an equivalent downward adjustment to the aggregate basis of partnership interests (and no additional adjustment is made under section 705(a)(2)(B). These downward basis adjustments shall be shared among the partners in the same proportion as the adjusted tax basis or cost of (or the qualified investment in) such section 38 property is allocated among the partners under paragraph (f) of

§1.46-3 (or paragraph (a)(4)(iv) of §1.48-8). See example (2)(iii) of paragraph (b)(5) of this section. Conversely, when there is an increase in the adjusted tax basis of partnership section 38 property under section 48(q)(2), section 48(q)(6) provides for an equivalent upward adjustment to the aggregate basis of partnership interests. These upward adjustments shall be allocated among the partners in the same proportion as the investment tax credit from such property is recaptured by the partners under §1.47-6.

(k) Depletion of oil and gas properties—(1) In general. The capital accounts of the partners will not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) unless such capital accounts are adjusted for depletion and gain or loss with respect to the oil or gas properties of the partnership in accordance with this paragraph (b)(2)(iv)*(k)*.

(2) Simulated depletion. Except as provided in paragraph (b)(2)(iv)*(k)(3)* of this section, a partnership shall, solely for purposes of maintaining capital accounts under this paragraph, compute simulated depletion allowances with respect to its oil and gas properties at the partnership level. These allowances shall be computed on each depletable oil or gas property of the partnership by using either the cost depletion method or the percentage depletion method (computed in accordance with section 613 at the rates specified in section 613A(c)(5) without regard to the limitations of section 613A, which theoretically could apply to any partner) for each partnership taxable year that the property is owned by the partnership and subject to depletion. The choice between the simulated cost depletion method and the simulated percentage depletion method shall be made on a property-by-property basis in the first partnership taxable year beginning after April 30, 1986 for which it is relevant for the property, and shall be binding for all partnership taxable years during which the oil or gas property is held by the partnership. The partnership shall make downward adjustments to the capital accounts of the partners for the simulated depletion allowance with respect to each oil or gas property of the partnership, in the same proportion as such partners (or their predecessors in interest) were properly allocated the adjusted tax basis of each such property. The aggregate capital account adjustments for simulated percentage depletion allowances with respect to an oil or gas property of the partnership shall not exceed the aggregate adjusted tax basis allocated to the partners with respect to such property. Upon the taxable disposition of an oil or gas property by a partnership, such partnership's simulated gain or loss shall be determined by subtracting its simulated adjusted basis in such property from the amount realized upon such disposition. (The partnership's simulated adjusted basis in an oil or gas property is determined in the same manner as adjusted tax basis except that simulated depletion allowances are taken into account instead of actual depletion allowances.) The capital accounts of the partners shall be adjusted upward by the amount of any simulated gain in proportion to such partners' allocable shares of the portion of the total amount realized from the disposition of such property that exceeds the partnership's simulated adjusted basis in such property. The capital accounts of such partners shall be adjusted downward by the amount of any simulated loss in proportion to such partners' allocable shares of the total amount realized from the disposition of such property that represents recovery of the partnership's simulated adjusted basis in such property. See section 613A(c)(7)(D) and the regulations thereunder and paragraph (b)(4)(v) of this section. See example (19)(iv) of paragraph (b)(5) of this section.

(3) Actual depletion. Pursuant to section 613A(c)(7)(D) and the regulations thereunder, the depletion allowance under section 611 with respect to the oil and gas properties of a partnership is computed separately by the partners. Accordingly, in lieu of adjusting the partners' capital accounts as provided in paragraph (b)(2)(iv)*(k)(2)* of this section, the partnership may make downward adjustments to the capital account of each partner equal to such partner's depletion allowance with respect to each oil or gas property of the partnership (for the partner's taxable year that ends with or within the partnership's taxable year). The aggregate adjustments to the capital account of a partner for depletion allowances with respect to an oil or gas property of the partnership shall not exceed the adjusted tax basis allocated to such partner with respect to such property. Upon the taxable disposition of an oil or gas property by a partnership, the capital account of each partner shall be adjusted upward by the amount of any excess of such partner's allocable share of the total amount realized from the disposition of such property over such partner's remaining adjusted tax basis in such property. If there is no such excess, the capital account of such partner shall be adjusted downward by the amount of any excess of such partner's remaining adjusted tax basis in such property over such partner's allocable share of the total amount realized from the disposition thereof. See section 613A(c)(7)(D) and the regulations thereunder and paragraph (b)(4)(v) of this section.

(4) Effect of book values. If an oil or gas property of the partnership is, under paragraphs (b)(2)(iv)*(d)* or (b)(2)(iv)*(f)* of this section, properly reflected on the books of the partnership at a book value that differs from the adjusted tax basis of such property, the rules contained in this paragraph (b)(2)(iv)*(k)* and paragraph (b)(4)(v) of this section shall be applied with reference to such book value. A revaluation of a partnership oil or gas property under paragraph (b)(2)(iv)*(f)* of this section may give rise to a reallocation of the adjusted tax basis of such property, or a change in the partners' relative shares of simulated depletion from such property, only to the extent permitted by section 613A(c)(7)(D) and the regulations thereunder.

(l) Transfers of partnership interests. The capital accounts of the partners will not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) unless, upon the transfer of all or a part of an interest in the partnership, the capital account of the transferor that is attributable to the transferred interest carries over to the transferee partner. (See paragraph (b)(2)(iv)*(m)* of this section for rules concerning the effect of a section 754 election on the capital accounts of the partners.) However, if the transfer of an interest in a partnership causes a termination of the partnership under section 708(b)(1)(B), the capital account

that carries over to the transferee partner will be adjusted in accordance with paragraph (b)(2)(iv)(*e*) of this section in connection with the constructive liquidation of the partnership under paragraph (b)(1)(iv) of §1.708-1. Moreover, the constructive reformation of such partnership will, for purposes of this paragraph, be treated as the formation of a new partnership, and the capital accounts of the partners of such new partnership will be determined and maintained accordingly. See example (13) of paragraph (b)(5) of this section.

(m) Section 754 elections—(1) In general. The capital accounts of the partners will not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) unless, upon adjustment to the adjusted tax basis of partnership property under sections 732, 734, or 743, the capital accounts of the partners are adjusted as provided in this paragraph (b)(2)(iv)(*m*).

(2) Section 743 adjustments. In the case of a transfer of all or a part of an interest in a partnership that has a section 754 election in effect for the partnership taxable year in which such transfer occurs, adjustments to the adjusted tax basis of partnership property under section 743 shall not be reflected in the capital account of the transferee partner or on the books of the partnership, and subsequent capital account adjustments for distributions (see paragraph (b)(2)(iv)(*e*)(1) of this section) and for depreciation, depletion, amortization, and gain or loss with respect to such property will disregard the effect of such basis adjustment. The preceding sentence shall not apply to the extent such basis adjustment is allocated to the common basis of partnership property under paragraph (b)(1) of §1.734-2; in these cases, such basis adjustment shall, except as provided in paragraph (b)(2)(iv)(*m*)(*5*) of this section, give rise to adjustments to the capital accounts of the partners in accordance with their interests in the partnership under paragraph (b)(3) of this section. See examples (13)(iii) and (iv) of paragraph (b)(5) of this section.

(3) Section 732 adjustments. In the case of a transfer of all or a part of an interest in a partnership that does not have a section 754 election in effect for the partnership taxable year in which such transfer occurs, adjustments to the adjusted tax basis of partnership property under section 732(d) will be treated in the capital accounts of the partners in the same manner as section 743 basis adjustments are treated under paragraph (b)(2)(iv)(*m*)(*2*) of this section.

(4) Section 734 adjustments. Except as provided in paragraph (b)(2)(iv)(*m*)(*5*) of this section, in the case of a distribution of property by a partnership that has a section 754 election in effect for the partnership taxable year in which the distribution occurs, the partner who receives a distribution that gives rise to the adjustment to the adjusted tax basis of partnership property under section 734 shall have a corresponding adjustment made to his capital account.

(5) Limitations on adjustments. Adjustments may be made to the capital account of a partner (or his successor in interest) in respect of basis adjustments to partnership property under sections 732, 734, and 743 only to the extent that such basis adjustments (i) are permitted to be made to one or more items of partnership property under section 755, and (ii) result in an increase or a decrease in the amount at which such property is carried on the partnership's balance sheet, as computed for book purposes. For example, if the book value of partnership property exceeds the adjusted tax basis of such property, a basis adjustment to such property may be reflected in a partner's capital account only to the extent such adjustment exceeds the difference between the book value of such property and the adjusted tax basis of such property prior to such adjustment.

(n) Partnership level characterization. Except as otherwise provided in paragraph (b)(2)(iv)(*k*) of this section, the capital accounts of the partners will not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) unless adjustments to such capital accounts in respect of partnership income, gain, loss, deduction, and section 705(a)(2)(B) expenditures (or item thereof) are made with reference to the Federal tax treatment of such items (and in the case of book items, with reference to the Federal tax treatment of the corresponding tax items) at the partnership level, without regard to any requisite or elective tax treatment of such items at the partner level (for example, under section 58(i)). However, a partnership that incurs mining exploration expenditures will determine the Federal tax treatment of income, gain, loss, and deduction with respect to the property to which such expenditures relate at the partnership level only after first taking into account the elections made by its partners under section 617 and section 703(b)(4).

(o) Guaranteed payments. Guaranteed payments to a partner under section 707(c) cause the capital account of the recipient partner to be adjusted only to the extent of such partner's distributive share of any partnership deduction, loss, or other downward capital account adjustment resulting from such payment.

(p) Minor discrepancies. Discrepancies between the balances in the respective capital accounts of the partners and the balances that would be in such respective capital accounts if they had been determined and maintained in accordance with this paragraph (b)(2)(iv) will not adversely affect the validity of an allocation, provided that such discrepancies are minor and are attributable to good faith error by the partnership.

(q) Adjustments where guidance is lacking. If the rules of this paragraph (b)(2)(iv) fail to provide guidance on how adjustments to the capital accounts of the partners should be made to reflect particular adjustments to partnership capital on the books of the partnership, such capital accounts will not be considered to be determined and maintained in accordance with those rules unless such capital account adjustments are made in a manner that *(1)* maintains equality between the aggregate governing capital accounts of the partners and the amount of partnership capital reflected on the partnership's balance sheet, as computed for book purposes, *(2)* is consistent with the underlying economic arrangement of the partners, and *(3)* is based, wherever practicable, on Federal tax accounting principles.

(r) Restatement of Capital Accounts. With respect to partnerships that began operating in a taxable year beginning before May 1, 1986, the capital accounts of the partners of which have not been determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) since inception, such

capital accounts shall not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) for taxable years beginning after April 30, 1986 unless *(1)* such capital accounts are adjusted, effective for the first partnership taxable year beginning after April 30, 1966, to reflect the fair market value of partnership property as of the first day of such taxable year, and *(2)* in connection with such adjustment, the rules contained in paragraph (b)(2)(iv)*(f)(2), (3),* and *(4)* of this section are satisfied. However, compliance with the previous sentence will have no bearing on the validity of allocations that relate to partnership taxable years beginning before May 1, 1986.

(3) *Partner's interest in the partnership*—(i) *In general.* References in section 704(b) and this paragraph to a partner's interest in the partnership, or to the partners' interests in the partnership, signify the manner in which the partners have agreed to share the economic benefit or burden with respect to the income, gain, loss, deduction, or credit (or item thereof) that is allocated. This sharing arrangement may or may not correspond to the overall economic arrangement of the partners. Thus, a partner who has a 50 percent overall interest in the partnership may have a 90 percent interest in a particular item of income or deduction. The determination of a partner's interest in a partnership shall be made by taking into account all facts and circumstances relating to the economic arrangement of the partners. All partners' interests in the partnership are presumed to be equal (determined on a per capita basis). However, this presumption may be rebutted by the taxpayer or the Internal Revenue Service by establishing facts and circumstances that show that the partners' interests in the partnership are otherwise.

(ii) *Factors considered.* In determining a partner's interest in the partnership, the following factors are among those that will be considered:

(a) The partners' relative contributions to the partnership,

(b) The interests of the partners in economic profits and losses (if different than that in taxable income or loss),

(c) The interests of the partners in cash flow and other non-liquidating distributions, and

(d) The rights of the partners to distributions of capital upon liquidation.

The provisions of this subparagraph (b)(3) are illustrated by examples (1)(i) and (ii), (4)(i), (5)(i) and (ii), (6), (7)(i), (ii), and (iv), (8), (10)(ii), (16)(i), and (19)(iii) of paragraph (b)(5) of this section. See paragraph (b)(4)(i) of this section concerning rules for determining the partners' interests in the partnership with respect to certain tax items.

(iii) *Certain determinations.* If—

(a) Requirements *(1)* and *(2)* of paragraph (b)(2)(ii)*(b)* of this section are satisfied, and

(b) All or a portion of an allocation of income, gain, loss, or deduction made to a partner for a partnership taxable year does not have economic effect under paragraph (b)(2)(ii) of this section,

the partners' interests in the partnership with respect to the portion of the allocation that lacks economic effect will be determined by comparing the manner in which distributions (and contributions) would be made if all partnership property were sold at book value and the partnership were liquidated immediately following the end of the taxable year to which the allocation relates with the manner in which distributions (and contributions) would be made if all partnership property were sold at book value and the partnership were liquidated immediately following the end of the prior taxable year, and adjusting the result for the items described in *(4), (5),* and *(6)* of paragraph (b)(2)(ii)*(d)* of this section. A determination made under this paragraph (b)(3)(iii) will have no force if the economic effect of valid allocations made in the same manner is insubstantial under paragraph (b)(2)(iii) of this section. See examples (1)(iv), (v), and (vi), and (15)(ii) and (iii) of paragraph (b)(5) of this section.

(4) *Special rules*—(i) *Allocations to reflect revaluations.* If partnership property is, under paragraphs (b)(2)(iv)*(d)* or (b)(2)(iv)*(f)* of this section, properly reflected in the capital accounts of the partners and on the books of the partnership at a book value that differs from the adjusted tax basis of such property, then depreciation, depletion, amortization, and gain or loss, as computed for book purposes, with respect to such property will be greater or less than the depreciation, depletion, amortization, and gain or loss, as computed for tax purposes, with respect to such property. In these cases the capital accounts of the partners are required to be adjusted solely for allocations of the book items to such partners (see paragraph (b)(2)(iv)*(g)* of this section), and the partners' shares of the corresponding tax items are not independently reflected by further adjustments to the partners' capital accounts. Thus, separate allocations of these tax items cannot have economic effect under paragraph (b)(2)(ii)*(b)(1)* of this section, and the partner's distribution share of such tax items must (unless governed by section 704(c)) be made in accordance with the partners' interests in the partnership. These tax items must be shared among the partners in a manner that takes account of the variation between the adjusted tax basis of such property and its book value in the same manner as variations between the adjusted tax basis and fair market value of property contributed to the partnership are taken into account in determining the partners' shares of tax items under section 704(c). See examples (14) and (18) of paragraph (b)(5) of this section.

(ii) *Credits.* Allocations of tax credits and tax credit recapture are not reflected by adjustments to the partners' capital accounts (except to the extent that adjustments to the adjusted tax basis of partnership section 38 property in respect of tax credits and tax credit recapture give rise to capital account adjustments under paragraph (b)(2)(iv)*(j)* of this section). Thus, such allocations cannot have economic effect under paragraph (b)(2)(ii)*(b)(1)* of this section, and the tax credits and tax credit recapture must be allocated in accordance with the partners' interests in the partnership as of the time the tax credit or credit recapture arises. With respect to the investment tax credit provided by section 38, allocations of cost or qualified investment made in accordance with paragraph (f) of §1.46-3 and paragraph (a)(4)(iv) of §1.48-8 shall be deemed to be made in accordance with the partners' interests in the partnership. With respect to other tax credits, if a partnership expenditure (whether or not deductible) that gives rise to a tax credit in a partnership taxable year also gives rise to valid allocations of partnership loss or deduction (or other downward capital account adjustments) for such year, then the partners' interests in the partnership with respect to such credit (or the cost giving rise thereto) shall be in the same proportion as such partners' respective distributive shares of such loss or deduction (and adjustments). See example (11) of paragraph (b)(5) of this section. Identical principles shall apply in determining the partners' interests in the partnership with respect to tax credits that arise from receipts of the partnership (whether or not taxable).

(iii) *Excess percentage depletion.* To the extent the percentage depletion in respect of an item of depletable property of the partnership exceeds the adjusted tax basis of such property, allocations of such excess percentage depletion are not reflected by adjustments to the partners' capital accounts. Thus, such allocations cannot have economic effect under paragraph (b)(2)(ii)(*b*)(*1*) of this section, and such excess percentage depletion must be allocated in accordance with the partners' interests in the partnership. The partners' interests in the partnership for a partnership taxable year with respect to such excess percentage depletion shall be in the same proportion as such partners' respective distributive shares of gross income from the depletable property (as determined under section 613(c)) for such year. See example (12) of paragraph (b)(5) of this section. See paragraphs (b)(2)(iv)(*k*) and (b)(4)(v) of this section for special rules concerning oil and gas properties of the partnership.

(iv) *Nonrecourse debt.* [Reserved.]

(v) *Allocations under section 613A(c)(7)(D).* Allocations of the adjusted tax basis of a partnership oil or gas property are controlled by section 613A(c)(7)(D) and the regulations thereunder. However, if the partnership agreement provdies for an allocation of the adjusted tax basis of an oil or gas property among the partners, and such allocation is not otherwise governed under section 704(c) (or related principles under paragraph (b)(4)(i) of this section), that allocation will be recognized as being in accordance with the partners' interests in partnership capital under section 613A(c)(7)(D), provided (*a*) such allocation does not give rise to capital account adjustments under paragraph (b)(2)(iv)(*k*) of this section the economic effect of which are insubstantial (as determined under paragraph (b)(2)(iii) of this section), and (*b*) all other allocations and capital account adjustments under the partnership agreement are recognized under this paragraph. Otherwise, such adjusted tax basis must be allocated among the partners pursuant to section 613A(c)(7)(D) in accordance with the partners' actual interests in partnership capital or income. For purposes of section 613A(c)(7)(D) the partners' allocable shares of the amount realized upon the partnership's taxable disposition of an oil or gas property will, except to the extent governed by section 704(c) (or related principles under paragraph (b)(4)(i) of this section), be determined under this paragraph (b)(4)(v). If, pursuant to paragraph (b)(2)(iv)(*k*)(*2*) of this section, the partners' capital accounts are adjusted to reflect the simulated depletion of an oil or gas property of the partnership, the portion of the total amount realized by the partnership upon the taxable disposition of such property that represents recovery of its simulated adjusted tax basis therein will be allocated to the partners in the same proportion as the aggregate adjusted tax basis of such property was allocated to such partners (or their predecessors in interest). If, pursuant to paragraph (b)(2)(iv)(*k*)(*3*) of this section, the partners' capital accounts are adjusted to reflect the actual depletion of an oil or gas property of the partnership, the portion of the total amount realized by the partnership upon the taxable disposition of such property that equals the partners' aggregate remaining adjusted basis therein will be allocated to the partners in proportion to their respective remaining adjusted tax bases in such property. An allocation provided by the partnership agreement of the portion of the total amount realized by the partnership on its taxable disposition of an oil or gas property that exceeds the portion of the total amount realized allocated under either of the previous two sentences (whichever is applicable) shall be deemed to be made in accordance with the partners' allocable shares of such amount realized, provided (*c*) such allocation does not give rise to capital account adjustments under paragraph (b)(2)(iv)(*k*) of this section the economic effect of which is insubstantial (as determined under paragraph (b)(2)(ii) of this section), and (*d*) all other allocations and capital account adjustments under the partnership agreement are recognized under this paragraph. Otherwise, the partners' allocable shares of the total amount realized by the partnership on its taxable disposition of an oil or gas property shall be determined in accordance with the partners' interests in the partnership under paragraph (b)(3) of this section. See example (19) of paragraph (b)(5) of this section. (See paragraph (b)(2)(iv)(*k*) of this section for the determination of appropriate adjustments to the partners' capital accounts relating to section 613A(c)(7)(D).)

(vi) *Amendments to partnership agreement.* If an allocation has substantial economic effect under paragraph (b)(2) of this section or is deemed to be made in accordance with the partners' interests in the partnership under paragraph (b)(4) of this section under the partnership agreement that is effective for the taxable year to which such allocation relates, and such partnership agreement thereafter is modified, both the tax consequences of the modification and the facts and circumstances surrounding the modification will be closely scrutinized to determine whether the purported modification was part of the original agreement. If it is determined that the purported modification was part of the original agreement, prior allocations may be reallocated in a manner consistent with the modified terms of the agreement, and subsequent allocations may be reallocated to take account of such modified terms. For example, if a partner is obligated by the partnership agreement to restore the deficit balance in his capital account (or any limited dollar amount thereof) in accordance with requirement *(3)* of paragraph (b)(2)(ii)(*b*) of this section and, thereafter, such obligation is eliminated or reduced (other than as provided in paragraph (b)(2)(ii)(*f*) of this section), or is not complied with in a timely manner, such elimination, reduction, or noncompliance may be treated as if it always were part of the partnership agreement for purposes of making any reallocations and determining the appropriate limitations period.

(vii) *Recapture.* For special rules applicable to the allocation of recapture income or credit, see paragraph (e) of §1.1245-1, paragraph (f) of §1.1250-1, paragraph (c) of §1.1254-1, and paragraph (a) of §1.47-6.

(5) *Examples*. The operation of the rules in this paragraph is illustrated by the following examples:

Example (1). (i) A and B form a general partnership with cash contributions of $40,000 each, which cash is used to purchase depreciable personal property at a cost of $80,000. The partnership elects under section 48(q)(4) to reduce the amount of investment tax credit in lieu of adjusting the tax basis of such property. The partnership agreement provides that A and B will have equal shares of taxable income and loss (computed without regard to cost recovery deductions) and cash flow and that all cost recovery deductions on the property will be allocated to A. The agreement further provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, but that upon liquidation of the partnership, distributions will be made equally between the partners (regardless of capital account balances) and no partner will be required to restore the deficit balance in this capital account for distribution to partners with positive capital accounts balances. In the partnership's first taxable year, it recognizes operating income equal to its operating expenses and has an additional $20,000 cost recovery deduction, which is allocated entirely to A. That A and B will be entitled to equal distributions on liquidation, even though A is allocated the entire $20,000 cost recovery deduction, indicates A will not bear the full risk of the economic loss corresponding to such deduction if such loss occurs. Under paragraph (b)(2)(ii) of this section, the allocation lacks economic effect and will be disregarded. The partners made equal contributions to the partnership, share equally in other taxable income and loss and in cash flow, and will share equally in liquidation proceeds, indicating that their actual economic arrangement is to bear the risk imposed by the potential decrease in the value of the property equally. Thus, under paragraph (b)(3) of this section the partners' interests in the partnership are equal, and the cost recovery deduction will be reallocated equally between A and B.

(ii) Assume the same facts as in (i) except that the partnership agreement provides that liquidation proceeds will be distributed in accordance with capital account balances if the partnership is liquidated during the first five years of its existence but that liquidation proceeds will be distributed equally if the partnership is liquidated thereafter. Since the partnership agreement does not provide for the requirement contained in paragraph (b)(2)(ii)*(b)(2)* of this section to be satisfied throughout the term of the partnership, the partnership allocations do not have economic effect. Even if the partnership agreement provided for the requirement contained in paragraph (b)(2)(ii)*(b)(2)* to be satisfied throughout the term of the partnership, such allocations would not have economic effect unless the requirement contained in paragraph (b)(2)(ii)*(b)(3)* of this section or the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* of this section were satisfied.

(iii) Assume the same facts as in (i) except that distributions in liquidation of the partnership (or any partner's interest) are to be made in accordance with the partners' positive capital account balances throughout the term of the partnership (as set fourth in paragraph (b)(2)(ii)*(b)(2)* of this section). Assume further that the partnership agreement contains a qualified income offset (as defined in paragraph (b)(2)(ii)*(d)* of this section) and that, as of the end of each partnership taxable year, the items described in paragraphs (b)(2)(ii)*(d)(4)*, *(5)*, and *(6)* of this section are not reasonably expected to cause or increase a deficit balance in A's capital account.

	A	*B*
Capital account upon formation	$40,000	$40,000
Less: year 1 cost recovery deduction	(20,000)	-0-
Capital account at end of year 1	$20,000	$40,000

Under the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* of this section, the allocation of the $20,000 cost recovery deduction to A has economic effect.

(iv) Assume the same facts as in (iii) and that in the partnership's second taxable year it recognizes operating income equal to its operating expenses and has a $25,000 cost recovery deduction which, under the partnership agreement, is allocated entirely to A.

	A	*B*
Capital account at beginning of year 2	$20,000	$40,000
Less: year 2 cost recovery deduction	(25,000)	-0-
Capital account at end of year 2	($5,000)	$40,000

The allocation of the $25,000 cost recovery deduction to A satisfies the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* of this section only to the extent of $20,000. Therefore only $20,000 of such allocation has economic effect, and the remaining $5,000 must be reallocated in accordance with the partners' interests in the partnership. Under the partnership agreement, if the property were sold immediately following the end of the partnership's second taxable year for $35,000 (its adjusted tax basis), the $35,000 would be distributed to B. Thus, B, and not A, bears the economic burden corresponding to $5,000 of the $25,000 cost recovery deduction allocated to A. Under paragraph (b)(3)(iii) of this section, $5,000 of such cost recovery deduction will be reallocated to B.

(v) Assume the same facts as in (iv) except that the cost recovery deduction for the partnership's second taxable year is $20,000 instead of $25,000. The allocation of such cost recovery deduction to A has economic effect under the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* of this section. Assume further that the property is sold for $35,000 immediately following the end of the partnership's second taxable year, resulting in a $5,000 taxable loss ($40,000 adjusted tax basis less $35,000 sales price), and the partnership is liquidated.

	A	*B*
Capital account at beginning of year 2	$20,000	$40,000
Less: year 2 cost recovery deduction	(20,000)	-0-
Capital account at end of year 2	-0-	$40,000
Less: loss on sale	(2,500)	(2,500)
Capital account before liquidation	($2,500)	$37,500

Under the partnership agreement the $35,000 sales proceeds are distributed to B. Since B bears the entire economic burden corresponding to the $5,000 taxable loss from the sale of the property, the allocation of $2,500 of such loss to A does not have economic effect and must be reallocated in accordance the partners' interests in the partnership. Under paragraph (b)(3)(iii) of this section, such $2,500 loss will be reallocated to B.

(vi) Assume the same facts as in (iv) except that the cost recovery deduction for the partnership's second taxable year is $20,000 instead of $25,000, and that as of the end of the partnership's second taxable year it is reasonably expected that during its third taxable year the partnership will (1) have operating income equal to its operating expenses (but will have no cost recovery deductions), (2) borrow $10,000 (recourse) and distribute such amount $5,000 to A and $5,000 to B, and (3) thereafter sell the partnership property, repay the $10,000 liability, and liquidate. In determining the extent to which the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* of this section is satisfied as of the end of the partnership's second taxable year, the fair market value of partnership property is presumed to be equal to its adjusted tax basis (in accordance with paragraph (b)(2)(iii)*(c)* of this section). Thus, it is presumed that the selling price of such property during the partnership's third taxable year will be its $40,000 adjusted tax basis. Accordingly, there can be no reasonable expectation that there will be increases to A's capital account in the partnership's third taxable year that will offset the expected $5,000 distribution to A. Therefore, the distribution of the loan proceeds must be taken into account in determining to what extent the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* is satisfied.

	A	*B*
Capital account at beginning of year 2	$20,000	$40,000
Less: expected future distribution	(5,000)	(5,000)
Less: year 2 cost recovery deduction	(20,000)	(-0-)
Hypothetical capital account at end of year 2	($5,000)	$35,000

Upon sale of the partnership property, the $40,000 presumed sales proceeds would be used to repay the $10,000 liability, and the remaining $30,000 would be distributed to B. Under these circumstances the allocation of the $20,000 cost recovery deduction to A in the partnership's second taxable year satisfies the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* of this section only to the extent of $15,000. Under paragraph (b)(3)(iii) of this section, the remaining $5,000 of such deduction will be reallocated to B. The results in this example would be the same even if the partnership agreement also provided that any gain (whether ordinary income or capital gain) upon the sale of the property would be allocated to A to the extent of the prior allocations of cost recovery deductions to him, and, at end of the partnership's second taxable year, the partners were confident that the gain on the sale of the property in the partnership's third taxable year would be sufficient to offset the expected $5,000 distribution to A.

(vii) Assume the same facts as in (iv) except that the partnership agreement also provides that any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraph (b)(2)(ii)*(b)(3)* of this section). Thus, if the property were sold for $35,000 immediately after the end of the partnership's second taxable year, the $35,000 would be distributed to B, A would contribute $5,000 (the deficit balance in his capital account) to the partnership, and that $5,000 would be distributed to B. The allocation of the entire $25,000 cost recovery deduction to A in the partnership's second taxable year has economic effect.

(viii) Assume the same facts as in (vii) except that A's obligation to restore the deficit balance in his capital account is limited to a maximum of $5,000. The allocation of the $25,000 cost recovery deduction to A in the partnership's second taxable year has economic effect under the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* of this section. At the end of such year, A makes an additional $5,000 contribution to the partnership (thereby eliminating the $5,000 deficit balance in his capital account). Under paragraph (b)(2)(ii)*(f)* of this section, A's obligation to restore up to $5,000 of the deficit balance in his capital account may be eliminated after he contributes the additional $5,000 without affecting the validity of prior allocations.

(ix) Assume the same facts as in (iv) except that upon formation of the partnership A also contributes to the partnership his promissory note with a $5,000 principal balance. The note unconditionally obligates A to pay an additional $5,000 to the partnership at the earlier of (a) the beginning of the partnership's fourth taxable year, or (b) the end of the partnership taxable year in which A's interest is liquidated. Under paragraph (b)(2)(ii)*(c)* of this section, A is considered obligated to restore up to $5,000 of the deficit balance in his capital account to the partnership. Accordingly, under the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* of this section, the allocation of the $25,000 cost recovery deduction to A in the partnership's second taxable year has economic effect. The results in this example would be the same if (1) the note A contributed to the partnership were payable only at the end of the partnership's fourth taxable year (so that A would not be required to satisfy the note upon liquidation of his interest in the partnership), and (2) the partnership agreement provided that upon liquidation of A's interest, the partnership would retain A's note, and A would contribute to the partnership the excess of the outstanding principal balance of the note over its then fair market value.

(x) Assume the same facts as in (ix) except that A's obligation to contribute an additional $5,000 to the partnership is not evidenced by a promissory note. Instead, the partnership agreement imposes upon A the obligation to make an additional $5,000 contribution to the partnership at the earlier of (a) the beginning of the partnership's fourth taxable year, or (b) the end of the partnership taxable year in which A's interest is liquidated. Under paragraph (b)(2)(ii)*(c)* of this section, as a result of A's deferred contribution requirement, A is considered obligated to restore up to $5,000 of the deficit balance in this capital account to the partnership. Accordingly, under the alternate economic effect test contained in paragraph (b)(2)(*ii*)(*d*) of this section, the allocation of the $25,000 cost recovery deduction to A in the partnership's second taxable year has economic effect.

(xi) Assume the same facts as in (vii) except that the partnership agreement also provides that any gain (whether ordinary income or capital gain) upon the sale of the property will be allocated to A to the extent of the prior allocations to A of cost recovery deductions from such property, and additional gain will be allocated equally between A and B. At the time the allocations of cost recovery deductions were made to A, the partners believed there would be gain on the sale of the property in an amount sufficient to offset the allocations of cost recovery deductions to A. Nevertheless, the existence of the gain chargeback provision will not cause the economic effect of the allocations to be insubstantial under paragraph (b)(2)(iii)*(c)* of this section, since in testing whether the economic effect of such allocations is substantial, the recovery property is presumed to decrease in value by the amount of such deductions.

Example (2). C and D form a general partnership solely to acquire and lease machinery that is 5-year recovery property under section 168. Each contributes $100,000, and the partnership obtains an $800,000 recourse loan to purchase the machinery. The partnership elects under section 48(q)(4) to reduce the amount of investment tax credit in lieu of adjusting the tax basis of such machinery. The partnership, C, and D have calendar taxable years. The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). The partnership agreement further provides that (a) partnership net taxable loss will be allocated 90 percent to C and 10 percent to D until such time as there is partnership net taxable income, and thereafter C will be allocated 90 percent of such taxable income until he has been allocated partnership net taxable income equal to the partnership net taxable loss previously allocated to him, (b) all further partnership net taxable income or loss will be allocated equally between C and D, and (c) distributions of operating cash flow will be made equally between C and D. The partnership enters into a 12-year lease with a financially secure corporation under which the partnership expects to have a net taxable loss in each of its first 5 partnership taxable years due to cost recovery deductions with respect to the machinery and net taxable income in each of its following 7 partnership taxable years, in part due to the absence of such cost recovery deductions. There is a strong likelihood that the partnership's net taxable loss in partnership taxable years 1 through 5 will be $100,000, $90,000, $80,000, $70,000, and $60,000, respectively, and the partnership's net taxable income in partnership taxable years 6 through 12 will be $40,000, $50,000, $60,000, $70,000, $80,000, $90,000, and $100,000, respectively. Even though there is a strong likelihood that the allocations of net taxable loss in years 1 through 5 will be largely offset by other allocations in partnership taxable years 6 through 12, and even if it is assumed that the total tax liability of the partners in years 1 through 12 will be less than if the allocations had not been provided in the partnership agreement, the economic effect of the allocations will not be insubstantial under paragraph (b)(2)(iii)*(c)* of this section. This is because at the time such allocations became part of the partnership agreement, there was a strong likelihood that the allocations of net taxable loss in years 1 through 5 would not be largely offset by allocations of income within 5 years (determined on a first-in, first-out basis). The year 1 allocation will not be offset until years 6, 7, and 8, the year 2 allocation will not be offset until years 8 and 9, the year 3 allocation will not be offset until years 9 and 10, the year 4 allocation will not be offset until years 10 and 11, and the year 5 allocation will not be offset until years 11 and 12.

Example (3). E and F enter into a partnership agreement to develop and market experimental electronic devices. E contributes $2,500 cash and agrees to devote his full-time services to the partnership. F contributes $100,000 cash and agrees to obtain a loan for the partnership for any additional capital needs. The partnership agreement provides that all deductions for research and experimental expenditures and interest on partnership loans are to be allocated to F. In addition, F will be allocated 90 percent, and E 10 percent, of partnership taxable income or loss, computed net of the deductions for such research and experimental expenditures and interest, until F has received allocations of such taxable income equal to the sum of such research and experimental expenditures, such interest expense, and his share of such taxable loss. Thereafter, E and F will share all taxable income and loss equally. Operating cash flow will be distributed equally between E and F. The partnership agreement also provides that E's and F's capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in this capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). These allocations have economic effect. In addition, in view of the nature of the partnership's activities, there is not a strong likelihood at the time the allocations become part of the partnership agreement that the economic effect of the allocations to F of deductions for research and experimental expenditures and interest on partnership loans will be largely offset by allocations to F of partnership net taxable income. The economic effect of the allocations is substantial.

Example (4). (i) G and H contribute $75,000 and $25,000, respectively, in forming a general partnership. The partnership agreement provides that all income, gain, loss, and deduction will be allocated equally between the partners, that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, but that all partnership distributions will, regardless of capital account balances, be made 75 percent to G and 25 percent to H. Following the liquidation of the partnership, neither partner is required to restore the deficit balance in his capital account to the partnership for distribution to partners with positive capital account balances. The allocations in the partnership agreement do not have economic effect. Since contributions were made in a 75/25 ratio and the partnership agreement indicates that all economic profits and losses of the partnership are to be shared in a 75/25 ratio, under paragraph (b)(3) of this section, partnership income, gain, loss, and deduction will be reallocated 75 percent to G and 25 percent to H.

(ii) Assume the same facts as in (i) except that the partnership maintains no capital accounts and the partnership agreement provides that all income, gain, loss, deduction, and credit will be allocated 75 percent to G and 25 percent to H. G and H are ultimately liable (under a State law right of contribution) for 75 percent and 25 percent, respectively, of any debts of the partnership. Although the allocations do not satisfy the requirements of paragraph (b)(2)(ii)*(b)* of this section, the allocations have economic effect under the economic effect equivalence test of paragraph (b)(2)(ii)*(i)* of this section.

(iii) Assume the same facts as in (i) except that the partnership agreement provides that any partner with a deficit balance in his capital account must restore that deficit to the partnership (as set forth in paragraph (b)(2)(ii)*(b)(2)* of this section). Although the allocations do not satisfy the requirements of paragraph (b)(2)(ii)*(b)* of this section, the allocations have economic effect under the economic effect equivalence test of paragraph (b)(2)(ii)*(i)* of this section.

Example (5). (i) Individuals I and J are the only partners of an investment partnership. The partnership owns corporate stocks, corporate debt instruments, and tax-exempt debt instruments. Over the next several years, I expects to be in the 50 percent marginal tax bracket, and J expects to be in the 15 percent marginal tax bracket. There is a strong likelihood that in each of the next several years the partnership will realize between $450 and $550 of tax-exempt interest and between $450 and $550 of a combination of taxable interest and dividends from its investments. I and J made equal capital contributions to the partnership, and they have agreed to share equally in gains and losses from the sale of the partnership's investment securities. I and J agree, however, that rather than share interest and dividends of the partnership equally, they will allocate the partnership's tax-exempt interest 80 percent to I and 20 percent to J and will distribute cash derived from interest received on the tax-exempt bonds in the same percentages. In addition, they agree to allocate 100 percent of the partnership's taxable interest and dividends to J and to distribute cash derived from interest and dividends received on the corporate stocks and debt instruments 100 percent to J. The partnership agreement further provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partner's positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). The allocation of taxable interest and dividends and tax-exempt interest has economic effect, but that economic effect is not substantial under the general rules set forth in paragraph (b)(2)(iii) of this section. Without the allocation I would be allocated between $225 and $375 of tax-exempt interest and between $225 and $275 of a combination of taxable interest and dividends, which (net of Federal income taxes he would owe on such income) would give I between $337.50 and $412.50 after tax. With the allocation, however, I will be allocated between $360 and $440 of tax-exempt interest and no taxable interest and dividends, which (net of Federal income taxes) will give I between $360 and $440 after tax. Thus, at the time the allocations became part of the partnership agreement, I is expected to enhance his after-tax economic consequences as a result of the allocations. On the other hand, there is a strong likelihood that neither I nor J will substantially diminish his after-tax economic consequences as a result of the allocations. Under the combination of likely investment outcomes least favorable for J, the partnership would realized $550 of tax-exempt interest and $450 of taxable interest and dividends, giving J $492.50 after tax (which is more than the $466.25 after tax J would have received if each of such amounts had been allocated equally between the partners). Under the combination of likely investment outcomes least favorable for I, the partnership would realize $450 of tax-exempt interest and $550 of taxable interest and dividends, giving I $360 after tax (which is not substantially less than the $362.50 he would have received if each of such amounts had been allocated equally between the partners). Accordingly, the allocations in the partnership agreement must be reallocated in accordance with the partners' interests in the partnership under paragraph (b)(3) of this section.

(ii) Assume the same facts as in (i). In addition, assume that in the first partnership taxable year in which the allocation arrangement described in (i) applies, the partnership realizes $450 of tax-exempt interest and $550 of taxable interest and dividends, so that, pursuant to the partnership agreement, I's capital account is credited with $360 (80 percent of the tax-exempt interest), and J's capital account is credited with $640 (20 percent of the tax-exempt interest and 100 percent of the taxable interest and dividends). The allocations of tax-exempt interest and taxable interest and dividends (which do not have substantial economic effect for the reasons stated in (i)) will be disregarded and will be reallocated. Since under the partnership agreement I will receive 36 percent (360/1,000) and J will receive 64 percent (640/1,000) of the partnership's total investment income in such year, under paragraph(b)(3) of this section the partnership's tax-exempt interest and taxable interest and dividends each will be reallocated 36 percent to I and 64 percent to J.

Example (6). K and L are equal partners in a general partnership formed to acquire and operate property described in section 1231(b). The partnership, K, and L have calendar taxable years. The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, that distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and that any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraphs (6)(2)(ii)*(b)(2)* and *(3)* of this section). For a taxable year in which the partnership expects to incur a loss on the sale of a portion of such property, the partnership agreement is amended (at the beginning of the taxable year) to allocate such loss to K, who expects to have no gains from the sale of depreciable property described in section 1231(b) in that taxable year, and to allocate an equivalent amount of partnership loss and deduction for that year of a different character to L, who expects to have such gains. Any partnership loss and deduction in excess of these allocations will be allocated equally between K and L. The amendment is effective only for that taxable year. At the time the partnership agreement is amended, there is a strong likelihood that the partnership will incur deduction or loss in the taxable year other than loss from the sale of property described in section 1231(b) in an amount that will substantially equal or exceed the expected amount of the section 1231(b) loss. The allocations in such taxable year have economic effect. However, the economic effect of the allocations is insubstantial under the test described in paragraph (b)(2)(iii)*(b)* of this section because there is a strong likelihood, at the time the allocations become part of the partnership agreement, that the net increases and decreases to K's and L's capital accounts will be the same at the end of the taxable year to which they apply with such allocations in effect as they would have been in the absence of such allocations, and that the total taxes of K and L for such year will be reduced as a result of such allocations. If in fact the partnership incurs deduction or loss, other than loss from the sale of property described in section 1231(b), in an amount at least equal to the section 1231(b) loss, the loss and deduction in such taxable year will be reallocated equally between K and L under paragraph (b)(3) of this section. If not, the loss from the sale of property described in section 1231(b) and the items of deduction and other loss realized in such year will be reallocated between K and L in proportion to the net decreases in their capital accounts due to the allocation of such items under the partnership agreement.

Example (7). (i) M and N are partners in the MN general partnership, which is engaged in an active business. Income, gain, loss, and deduction from MN's business is allocated equally between M and N. The partnership, M, and N have calendar taxable years. Under the partnership agreement the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in this capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraph (b)(2)(ii)*(b)(2)* and *(3)* of this section). In order to enhance the credit standing of the partnership, the partners contribute surplus funds to the partnership, which the partners agree to invest in equal dollar amounts of tax-exempt bonds and corporate stock for the partnership's first 3 taxable years. M is expected to be in a higher marginal tax bracket than N during those 3 years. At the time the decision to make these investments is made, it is agreed that, during the 3-year period of the investment, M will be allocated 90 percent and N 10 percent of the interest income from the tax-exempt bonds as well as any gain or loss from the sale thereof, and that M will be allocated 10 percent and N 90 percent of the dividend income from the corporate stock as well as any gain or loss from the sale thereof. At the time the allocations concerning the investments become part of the partnership agreement, there is not a strong likelihood that the gain or loss from the sale of the stock will be substantially equal to the gain or loss from the sale of the tax-exempt bonds, but there is a strong likelihood that the tax-exempt interest and the taxable dividends realized from these investments during the 3-year period will not differ substantially. These allocations have economic effect, and the economic effect of the allocations of the gain or loss on the sale of the tax-exempt bonds and corporate stock is substantial. The economic effect of the allocations of the tax-exempt interest and the taxable dividends, however, is not substantial under the test described in paragraph (b)(2)(iii)*(c)* of this section because there is a strong likelihood, at the time the allocations become part of the partnership agreement, that at the end of the 3-year period to which such allocations relate, the net increases and decreases to M's and N's capital accounts will be the same with such allocations as they would have been in the absence of such allocations, and that the total taxes of M and N for the taxable years to which such allocations relate will be reduced as a result of such allocations. If in fact the amounts of the tax-exempt interest and taxable dividends earned by the partnership during the 3-year period are equal, the tax-exempt interest and taxable dividends will be reallocated to the partners in equal shares under paragraph (b)(3) of this section. If not, the tax-exempt interest and taxable dividends will be reallocated between M and N in proportion to the net increases in their capital accounts during such 3-year period due to the allocation of such items under the partnership agreement.

(ii) Assume the same facts as in (i) except that gain or loss from the sale of the tax-exempt bonds and corporate stock will be allocated equally between M and N and the partnership agreement provides that the 90/10 allocation arrangement with respect to the investment income applies only to the first $10,000 of interest income from the tax-exempt bonds and the first $10,000 of dividend income from the corporate stock, and only to the first taxable year of the partnership. There is a strong likelihood at the time the 90/10 allocation of the investment income became part of the partnership agreement that in the first taxable year of the partnership, the partnership will earn more than $10,000 of tax-exempt interest and more than $10,000 of taxable dividends. The allocations of tax-exempt interest and taxable dividends provided in the partnership agreement have economic effect, but under the test contained in paragraph (b)(2)(iii)*(b)* of this section, such economic effect is not substantial for the same reasons stated in (i) (but applied to the 1 taxable year, rather than to a 3-year period). If in fact the partnership realizes at least $10,000 of tax-exempt interest and at least $10,000 of taxable dividends in such year, the allocations of such interest income and dividend income will be reallocated equally between M and N under paragraph (b)(3) of this section. If no, the tax-exempt interest and taxable dividends will be reallocated between M and N in proportion to the net increases in their capital accounts due to the allocations of such items under the partnership agreement.

(iii) Assume the same facts as in (ii) except that at the time the 90/10 allocation of investment income becomes part of the partnership agreement, there is not a strong likelihood that (1) the partnership will earn $10,000 or more of tax-exempt interest and $10,000 or more of taxable dividends in the partnership's first taxable year, and (2) the amount of tax-exempt interest and taxable dividends earned during such year will be substantially the same. Under these facts the economnic effect of the allocations generally will be substantial. (Additional facts may exist in certain cases, however, so that the allocation is insubstantial under the general rules of paragraph (b)(2)(iii). See example (5) above.)

Example (8). (i) O and P are equal partners in the OP general partnership. The partnership, O, and P have calendar taxable years. Partner O has a net operating loss carryover from another venture that is due to expire at the end of the partnership's second taxable year. Otherwise, both partners expect to be in the 50 percent marginal tax bracket in the next several taxable years. The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). The partnership agreement is amended (at the beginning of the partnership's second taxable year) to allocate all the partnership net taxable income for that year to O. Future partnership net taxable loss is to be allocated to O, and future partnership net taxable income to P, until the allocation of income to O in the partnership's second taxable year is offset. It is further agreed orally that in the event the partnership is liquidated prior to completion of such offset, O's capital account will be adjusted downward to the extent of one-half of the allocations of income to O in the partnership's second taxable year that have not been offset by other allocations, P's capital account will be adjusted upward by a like amount, and liquidation proceeds will be distributed in accordance with the partners' adjusted capital account balances. As a result of this oral amendment, all allocations of partnership net taxable income and net taxable loss made pursuant to the amendment executed at the beginning of the partnership's second taxable year lack economic effect and will be disregarded. Under the partnership agreement other allocations are made equally to O and P, and O and P will share equally in liquidation proceeds, indicating that the partners' interests in the partnership are equal. Thus, the disregarded allocations will be reallocated equally between the partners under paragraph (b)(3) of this section.

(ii) Assume the same facts as in (i) except that there is no agreement that O's and P's capital accounts will be adjusted downward and upward, respectively, to the extent of one-half of the partnership net taxable income allocated to O in the partnership's second taxable year that is not offset subsequently by other allocations. The income of the partnership is generated primarily by fixed interest payments received with respect to highly rated corporate bonds, which are expected to produce sufficient net taxable income prior to the end of the partnership's seventh taxable year to offset in large part the net taxable income to be allocated to O in the partnership's second taxable year. Thus, at the time the allocations are made part of the partnership agreement, there is a strong likelihood that the allocation of net taxable income to be made to O in the second taxable year will be offset in large part within 5 taxable years thereafter. These allocations have economic effect. However, the economic effect of the allocation of partnership net taxable income to O in the partnership's second taxable year, as well as the offsetting allocations to P, is not substantial under the test contained in paragraph (b)(2)(iii)*(c)* of this section because there is a strong likelihood that the net increases or decreases in O's and P's capital accounts will be the same at the end of the partnership's seventh taxable year with such allocations as they would have been in the absence of such allocations, and the total taxes of O and P for the taxable years to which such allocations relate will be reduced as a result of such allocations. If in fact the partnership, in its taxable years 3 through 7, realizes sufficient net taxable income to offset the amount allocated to O in the second taxable year, the allocations provided in the partnership agreement will be reallocated equally between the partners under paragraph (b)(3) of this section.

Example (9). Q and R form a limited partnership with contributions of $20,000 and $180,000, respectively. Q, the limited partner, is a corporation that has $2,000,000 of net operating loss carryforwards that will not expire for 8 years. Q does not expect to have sufficient income (apart from the income of the partnership) to absorb any of such net operating loss carryforwards. R, the general partner, is a corporation that expects to be in the 46 percent marginal tax bracket for several years. The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). The partnership's cash, together with the proceeds of an $800,000 loan, are invested in assets that are expected to produce taxable income and cash flow (before debt service) of approximately $150,000 a year for the first 8 years of the partnership's operations. In addition, it is expected that the partnership's total taxable income in its first 8 taxable years will not exceed $2,000,000. The partnership's $150,000 of cash flow in each of its first 8 years will be used to retire the $800,000 loan. The partnership agreement provides that partnership net taxable income will be allocated 90 percent to Q and 10 percent to R in the first through eighth partnership taxable years, and 90 percent to R and 10 percent to Q in all subsequent partnership taxable years. Net taxable loss will be allocated 90 percent to R and 10 percent to Q in all partnership taxable years. All distributions of cash from the partnership to partners (other than the priority distributions to Q described below) will be made 90 percent to R and 10 percent to Q. At the end of the partnership's eighth taxable year, the amount of Q's capital account in excess of one-ninth of R's capital account on such date will be designated as Q's "excess capital account." Beginning in the ninth taxable year of the partnership, the undistributed portion of Q's excess capital account will begin to bear interest (which will be paid and deducted under section 707(c)) at a rate of interest below the rate that the partnership can borrow from commercial lenders, and over the next several years (following the eighth year) the partnership will make priority cash distributions to Q in prearranged percentages of Q's excess capital account designed to amortize Q's excess capital account and the interest thereon over a prearranged period. In addition, the partnership's agreement prevents Q from causing his interest in the partnership from being liquidated (and thereby receiving the balance in this capital account) without R's consent until Q's excess capital account has been eliminated. The below-market rate of interest and the period over which the amortization will take place are prescribed such that, as of the end of the partnership's eighth taxable year, the present value of Q's right to receive such priority distributions is approximately 46 percent of the amount of Q's excess capital account as of such date. However, because the partnership's income for its first 8 taxable years will be realized approximately ratably over that period, the present value of Q's right to receive the priority distributions with respect to its excess capital account is, as of the date the partnership agreement is entered into, less than the present value of the additional Federal income taxes for which R would be liable if, during the partnership's first 8 taxable years, all partnership income were to be allocated 90 percent to R and 10 to Q. The allocations of partnership taxable income to Q and R in the first through eighth partnership taxable years have economic effect. However, such economic effect is not substantial under the general rules set forth in paragraph (b)(2)(iii) of this section. This is true because R may enhance his after-tax economic consequences, on a present value basis, as a result of the allocations to Q of 90 percent of partnership's income during taxable year 1 through 8, and there is a strong likelihood that neither R nor Q will substantially diminish its after-tax economic consequences, on a present value basis, as a result of such allocation. Accordingly, partnership taxable income for partnership taxable years 1 through 8 will be reallocated in accordance with the partners' interests in the partnership under paragraph (b)(3) of this section.

Example (10). (i) S and T form a general partnership to operate a travel agency. The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). The partnership agreement provides that T, a resident of a foreign country, will be allocated 90 percent, and S 10 percent, of the income, gain, loss, and deduction derived from operations conducted by T within his country, and all remaining income, gain, loss, and deduction will be allocated equally. The amount of such income, gain, loss, or deduction cannot be predicted with any reasonable certainty. The allocations provided by the partnership agreement have substantial economic effect.

(ii) Assume the same facts as in (i) except that the partnership agreement provides that all income, gain, loss, and deduction of the partnership will be shared equally, but that T will be allocated all income, gain, loss, and deduction derived from operations conducted by him within his country as a part of his equal share of partnership income, gain, loss, and deduction, up to the amount of such share. Assume the total tax liability of S and T for each year to which these allocations relate will be reduced as a result of such allocation. These allocations have economic effect. However, such economic effect is not substantial under the test stated in paragraph (b)(2)(iii)*(b)* of this section because, at the time the allocations became part of the partnership agreement, there is a strong likelihood that the net increases and decreases to S's and T's capital accounts will be the same at the end of each partnership taxable year with such allocations as they would have been in the absence of such allocations, and that the total tax liability of S and T for each year to which such allocations relate will be reduced as a result of such allocations. Thus, all items of partnership income, gain, loss, and income, gain, loss, and deduction will be reallocated equally between S and T under paragraph (b)(3) of this section.

Example (11). (i) U and V share equally all income, gain, loss, and deduction of the UV general partnership, as well as all non-liquidating distributions made by the partnership. The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore such deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). The agreement further provides that the partners will be allocated equal shares of any section 705(a)(2)(B) expenditures of the partnership. In the partnership's first taxable year, it pays qualified first-year wages of $6,000 and is entitled to a $3,000 targeted jobs tax credit under sections 44B and 51 of the Code. Under section 280C the partnership must reduce its deduction for wages paid by the $3,000 credit claimed (which amount constitutes a section 705(a)(2)(B) expenditure). The partnership agreement allocates the credit to U. Although the allocations of wage deductions and section 705(a)(2)(B) expenditures have substantial economic effect, the allocation of tax credit cannot have economic effect since it cannot properly be reflected in the partners' capital accounts. Furthermore, the allocation is not in accordance with the special partners' interests in the partnership rule contained in paragraph (b)(4)(ii) of this section. Under that rule, since the expenses that gave rise to the credit are shared equally by the partners, the credit will be shared equally between U and V.

(ii) Assume the same facts as in (i) and that at the beginning of the partnership's second taxable year, the partnership agreement is amended to allocate to U all wage expenses incurred in that year (including wage expenses that constitute section 705(a)(2)(B) expenditures) whether or not such wages qualify for the credit. The partnership agreement contains no offsetting allocations. That taxable year the partnership pays $8,000 in total wages to its employees. Assume that the partnership has operating income equal to its operating expenses (exclusive of expenses for wages). Assume further that $6,000 of the $8,000 wage expense constitutes qualified first-year wages. U is allocated the $3,000 deduction and the $3,000 section 705(a)(2)(B) expenditure attributable to the $6,000 of qualified first-year wages, as well as the deduction for the other $2,000 in wage expenses. The allocations of wage deductions and section 705(a)(2)(B) expenditures have substantial economic effect. Furthermore, since the wage credit is allocated in the same proportion as the expenses that gave rise to the credit, and the allocation of those expenses has substantial economic effect, the allocation of such credit to U is in accordance with the special partners' interests in the partnership rule contained in paragraph (b)(4)(ii) of this section and is recognized thereunder.

Example (12). (i) W and X form a general partnership for the purpose of mining iron ore. W makes an initial contribution of $75,000, and X makes an initial contribution of $25,000. The partnership agreement provides that non-liquidating distributions will be made 75 percent to W and 25 percent to X, and that all items of income, gain, loss, and deduction will be allocated 75 percent to W and 25 percent to X, except that all percentage depletion deductions will be allocated to W. The agreement further provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore such deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). Assume that the adjusted tax basis of the partnership's only depletable iron ore property is $1,000 and that the percentage depletion deduction for the taxable year with respect to such property is $1,500. The allocation of partnership income, gain, loss, and deduction (excluding the percentage depletion deduction) as well as the allocation of $1,000 of the percentage depletion deduction have substantial economic effect. The allocation to W of the remaining $500 of the percentage depletion deduction, representing the excess of percentage depletion over adjusted tax basis of the iron ore property, cannot have economic effect since such amount cannot properly be reflected in the partners' capital accounts. Furthermore, the allocation to W of that $500 excess percentage depletion deduction is not in accordance with the special partners' interests in the partnership rule contained in paragraph (b)(4) (iii) of this section, under which such $500 excess depletion deduction (and all further percentage depletion deductions from the mine) will be reallocated 75 percent to W and 25 percent to X.

(ii) Assume the same facts as in (i) except that the partnership agreement provides that all percentage depletion deductions of the partnership will be allocated 75 percent to W and 25 percent to X. Once again, the allocation of partnership income, gain, loss, and deduction (excluding the percentage depletion deduction) as well as the allocation of $1,000 of the percentage depletion deduction have substantial economic effect. Furthermore, since the $500 portion of the percentage depletion deduction that exceeds the adjusted basis of such iron ore property is allocated in the same manner as valid allocations of the gross income from such property during the taxable year (*i.e.*, 75 percent to W and 25 percent to X), the allocation of the $500 excess percentage depletion contained in the partnership agreement is in accordance with the special partners' interests in the partnership rule contained in paragraph (b)(4)(iii) of this section.

Example (13). (i) Y and Z form a brokerage general partnership for the purpose of investing and trading in marketable securities. Y contributes cash of $10,000, and Z contributes securities of P corporation, which have an adjusted basis of $3,000 and a fair market value of $10,000. The partnership would not be an investment company under section 351(e) if it were incorporated. The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). The initial capital accounts of Y and Z are fixed at $10,000 each. The agreement further provides that all partnership distributions, income, gain, loss, deduction, and credit will be shared equally between Y and Z, except that the taxable gain attributable to the precontribution appreciation in the value of the securities of P corporation will be allocated to Z in accordance with section 704(c). During the partnership's first taxable year, it sells the securities of P corporation for $12,000, resulting in a $2,000 book gain ($12,000 less $10,000 book value) and a $9,000 taxable gain ($12,000 less $3,000 adjusted tax basis). The partnership has no other income, gain, loss, or deductions for the taxable year.

The gain from the sale of the securities is allocated as follows:

	Y		*Z*	
	Tax	*Book*	*Tax*	*Book*
Capital account upon formation	$10,000	$10,000	$3,000	$10,000
Plus: gain	1,000	1,000	8,000	1,000
Capital account at end of year	$11,000	$11,000	$11,000	$11,000

The allocation of the $2,000 book gain, $1,000 each to Y and Z, has substantial economic effect. Furthermore, under section 704(c) the partners' distributive shares of the $9,000 taxable gain are $1,000 to Y and $8,000 to Z.

(ii) Assume the same facts as in (i) and that at the beginning of the partnership's second taxable year, it invests its $22,000 of cash in securities of G Corp. The G Corp. securities increase in value to $40,000, at which time Y sells 50 percent of his partnership interest (*i.e.*, a 25 percent interest in the partnership) to LK for $10,000. The partnership does not have a section 754 election in effect for the partnership taxable year during which such sale occurs. In accordance with paragraph (b)(2)(iv)*(l)* of this section, the partnership agreement provides that LK inherits 50 percent of Y's $11,000 capital account balance. Thus, following the sale, LK and Y each have a capital account of $5,500, and Z's capital account remains at $11,000. Prior to the end of the partnership's second taxable year, the securities are sold for their $40,000 fair market value, resulting in an $18,000 taxable gain ($40,000 less $22,000 adjusted tax basis). The partnership has no other income, gain, loss, or deduction in such taxable year. Under the partnership agreement the $18,000 taxable gain is allocated as follows:

	Y	*Z*	*LK*
Capital account before sale of securities	$5,500	$11,000	$5,500
Plus: gain	4,500	9,000	4,500
Capital account at end of year 2	$10,000	$20,000	$10,000

The allocation of the $18,000 taxable gain has substantial economic effect.

(iii) Assume the same facts as in (ii) except that the partnership has a section 754 election in effect for the partnership taxable year during which Y sells 50 percent of his interest to LK. According, under §1.743-1 there is a $4,500 basis increase to the G Corp. securities with respect to LK. Notwithstanding this basis adjustment, as a result of the sale of the G Corp. securities, LK's capital account is, as in (ii), increased by $4,500. The fact that LK recognizes no taxable gain from such sale (due to his $4,500 section 743 basis adjustment) is irrelevant for capital accounting purposes since, in accordance with paragraph (b)(2)(iv)*(m)(2)* of this section, that basis adjustment is disregarded in the maintenance and computation of the partners' capital accounts.

(iv) Assume the same facts as in (iii) except that immediately following Y's sale of 50 percent of his interest to LK, the G Corp. securities decrease in value to $32,000 and are sold. The $10,000 taxable gain ($32,000 less $22,000 adjusted tax basis) is allocated as follows:

	Y	*Z*	*LK*
Capital account before sale of securities	$5,500	$11,000	$5,500
Plus: gain	2,500	5,000	2,500
Capital account at end of the year 2	$8,000	$16,000	$8,000

The fact that LK recognizes a $2,000 taxable loss from the sale of the G Corp. securities (due to his $4,500 section 743 basis adjustment) is irrelevant for capital accounting purposes since, in accordance with paragraph (b)(2)(iv)*(m)(2)* of this section, that basis adjustment is disregarded in the maintenance and computation of the partners' capital accounts.

(v) Assume the same facts as in (ii) except that Y sells 100 percent of his partnership interest (*i.e.*, a 50 percent interest in the partnership) to LK for $20,000. Under section 708(b)(1)(B) the partnership terminates. Under paragraph (b)(1)(iv) of §1.708–1, there is a constructive liquidation of the partnership. Immediately preceding the constructive liquidation, the capital accounts of Z and LK equal $11,000 each (LK having inherited Y's $11,000 capital account). In accordance with paragraph (b)(2)(iv)*(e)* of this section, the partnership agreement provides that the partners' capital accounts are adjusted to reflect how unrealized taxable gain would have been allocated if the securities had been sold for their $40,000 fair market value. Accordingly, the $18,000 of unrealized gain ($40,000 less $22,000 adjusted tax basis) is credited to the partners' capital accounts as follows:

	Z	*LK*
Capital account following sale	$11,000	$11,000
Deemed sale adjustment	9,000	9,000
Capital account before constructive liquidation	$20,000	$20,000

Constructive liquidating distributions of the securities are made with reference to their $40,000 fair market value. Under section 732(b) the adjusted tax basis of the G Corp. securities constructively distributed to Z is equal to the $11,000 adjusted tax basis of Z's partnership interest before the constructive liquidation, and the adjusted tax basis of the G Corp. securities constructively distributed to Z is equal to the $20,000 adjusted tax basis of LK's partnership interest partnership before the constructive liquidation. Under paragraph (b)(1)(iv) of §1.708-1, the partners then are treated as contributing to a new partnership the property constructively distributed to them in connection the partnership's termination. In accordance with paragraph (b)(2)(iv)*(d)* of this section, the capital accounts of Z and LK in the reconstituted partnership are stated at $20,000 each (*i.e.*, the fair market value of the property constructively contributed to the new partnership by each of the partners).

Example (14). (i) MC and RW form a general partnership to which each contributes $10,000. The $20,000 is invested in securities of Ventureco (which are not readily tradable on an established securities market). In each of the partnership's taxable years, it recognizes operating income equal to its operating deductions (excluding gain or loss from the sale of securities). The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interst) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). Assume that the Ventureco securities subsequently appreciate in value to $50,000. At that time SK makes a $25,000 cash contribution to the partnership (thereby acquiring a one-third interest in the partnership), and the $25,000 is placed in a bank account. Upon SK's admission to the partnership, the capital accounts of MC and RW (which were $10,000 each prior to SK's admission) are, in accordance with paragraph (b)(2)(iv)*(f)* of this section, adjusted upward (to $25,000 each) to reflect their shares of the unrealized appreciation in the Ventureco securities that occurred before SK was admitted to the partnership. Immediately after SK's admission to the partnership, the securities are sold for their $50,000 fair market value, resulting in taxable gain of $30,000 ($50,000 less $20,000 adjusted tax basis) and no book gain or loss. An allocation of the $30,000 taxable gain cannot have economic effect since it cannot properly be reflected in the partners' book capital accounts. Under paragraph (b)(2)(iv)*(f)* of this section and the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, unless the partnership agreement provides that the $30,000 taxable gain will, in accordance with section 704(c) principles, be shared $15,000 to MC and $15,000 to RW, the partners' capital accounts will not be considered maintained in accordance with paragraph (b)(2)(iv) of this section.

	MC		*RW*		*SK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account following SK's admission	$10,000	$25,000	$10,000	$25,000	$25,000	$25,000
Plus: gain	15,000	-0-	15,000	-0-	-0-	-0-
Capital account following sale	$25,000	$25,000	$25,000	$25,000	$25,000	$25,000

(ii) Assume the same facts as (i), except that after SK's admission to the partnership, the Ventureco securities appreciate in value to $74,000 and are sold, resulting in taxable gain of $54,000 ($74,000 less $20,000 adjusted tax basis) and book gain of $24,000 ($74,000 less $50,000 book value). Under the partnership agreement the $24,000 book gain (the appreciation in value occurring after SK became a partner) is allocated equally among MC, RW, and SK, and such allocations have substantial economic effect. An allocation of the $54,000 taxable gain cannot have economic effect since it cannot properly be reflected in the partners' book capital accounts. Under paragraph (b)(2)(iv)*(f)* of this section and the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, unless the partnership agreement provides that the taxable gain will, in accordance with section 704(c) principles, be shared $23,000 to MC, $23,000 to RW, and $8,000 to SK, the partners' capital accounts will not be considered maintained in accordance with paragraph (b)(2)(iv) of this section.

	MC		*RW*		*SK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account following SK's admission	$10,000	$25,000	$10,000	$25,000	$25,000	$25,000
Plus: gain	23,000	8,000	23,000	8,000	8,000	8,000
Capital account following sale	$33,000	$33,000	$33,000	$33,000	$33,000	$33,000

(iii) Assume the same facts as (i) except that after SK's admission to the partnership, the Ventureco securities depreciate in value to $44,000 and are sold, resulting in taxable gain of $24,000 ($44,000 less $20,000 adjusted tax basis) and a book loss of $6,000 ($50,000 book value less $44,000). Under the partnership agreement the $6,000 book loss is allocated equally among MC, RW, and SK, and such allocations have substantial economic effect. An allocation of the $24,000 taxable gain cannot have economic effect since it cannot properly be reflected in the partners' book capital accounts. Under paragraph (b)(2)(iv)*(f)* of this section and the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, unless the partnership agreement provides that the $24,000 taxable gain will, in accordance with section 704(c) principles, be shared equally between MC and RW, the partners' capital accounts will not be considered maintained in accordance with paragraph (b)(2)(iv) of this section.

	MC		*RW*		*SK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account following SK's admission	$10,000	$25,000	$10,000	$25,00 0	$25,000	$25,000
Plus: gain	12,000	-0-	12,000	-0-	-0-	-0-
Less: loss	-0-	(2,000)	-0-	(2,000)	-0-	(2,000)
Capital account following sale	$22,000	$23,000	$22,000	$23,000	$25,000	$23,000

That SK bears an economic loss of $2,000 without a corresponding taxable loss is attributable entirely to the "ceiling rule." See paragraph (c)(2) of §1.704-1.

(iv) Assume the same facts as in (ii) except that upon the admission of SK the capital accounts of MC and RW are not each adjusted upward from $10,000 to $25,000 to reflect the appreciation in the partnership's securities that occurred before SK was admitted to the partnership. Rather, upon SK's admission to the partnership, the partnership agreement is amended to provide that the first $30,000 of taxable gain upon the sale of such securities will be allocated equally between MC and RW, and that all other income, gain, loss, and deduction will be allocated equally between MC, RW, and SK. When the securities are sold for $74,000, the $54,000 of taxable gain is so allocated. These allocations of taxable gain have substantial economic effect. (If the agreement instead provides for all taxable gain (including the $30,000 taxable gain attributable to the appreciation in the securities prior to SK's admission to the partnership) to be allocated equally between MC, RW, and SK, the partners should consider whether, and to what extent, the provisions of paragraphs (b)(1)(iii) and (iv) of this section are applicable.)

(v) Assume the same facts as in (iv) except that instead of selling the securities, the partnership makes a distribution of the securities (which have a fair market value of $74,000). Assume the distribution does not give rise to a transaction described in section 707(a)(2)(B). In accordance with paragraph (b)(2)(iv)(*e*) of this section, the partners' capital accounts are adjusted immediately prior to the distribution to reflect how taxable gain ($54,000) would have been allocated had the securities been sold for their $74,000 fair market value, and capital account adjustments in respect of the distribution of the securities are made with reference to the $74,000 "booked-up" fair market value.

	MC	*RW*	*SK*
Capital account before adjustment	$10,000	$10,000	$25,000
Deemed sale adjustment	23,000	23,000	8,000
Less: distribution	(24,667)	(24,667)	(24,667)
Capital account after distribution	$8,333	$8,333	$8,333

(vi) Assume the same facts as in (i) except that the partnership does not sell the Ventureco securities. During the next 3 years the fair market value of the Ventureco securities remains at $50,000, and the partnership engages in no other investment activities. Thus, at the end of that period the balance sheet of the partnership and the partners' capital accounts are the same as they were at the beginning of such period. At the end of the 3 years, MC's interest in the partnership is liquidated for the $25,000 cash held by the partnership. Assume the distribution does not give rise to a transaction described in section 707(a)(2)(B). Assume further that the partnership has a section 754 election in effect for the taxable year during which such liquidation occurs. Under sections 734(b) and 755 the partnership increases the basis of the Ventureco securities by the $15,000 basis adjustment (the excess of $25,000 over the $10,000 adjusted tax basis of MC's partnership interest).

	MC		*RW*		*SK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account before distribution	$10,000	$25,000	$10,000	$25,000	$25,000	$25,000
Plus: basis adjustment	15,000	-0-	-0-	-0-	-0-	-0-
Less: distribution	(25,000)	(25,000)	-0-	-0-	-0-	-0-
Capital account account after liquidation	-0-	-0-	$10,000	$25,000	$25,000	$25,000

(vii) Assume the same facts as in (vi) except that the partnership has no section 754 election in effect for the taxable year during which such liquidation occurs.

	MC		*RW*		*SK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account before distribution	$10,000	$25,000	$10,000	$25,000	$25,000	$25,000
Less: distribution	(25,000)	(25,000)	-0-	-0-	-0-	-0-
Capital account after liquidation	($15,000)	-0-	$10,000	$25,000	$25,000	$25,000

Following the liquidation of MC's interest in the partnership, the Ventureco securities are sold for their $50,000 fair market value, resulting in no book gain or loss but a $30,000 taxable gain. An allocation of this $30,000 taxable gain cannot have economic effect since it cannot properly be reflected in the partners' book capital accounts. Under paragraph (b)(2)(iv)(*f*) of this section and the special partners' interests in the partnership rule contained in section paragraph (b)(4)(i) of this section, unless the partnership agreement provides that $15,000 of such taxable gain will, in accordance with section 704(c) principles, be included in RW's distributive share, the partners' capital accounts will not be considered maintained in accordance with paragraph (b)(2)(iv) of this section. The remaining $15,000 of such gain will, under paragraph (b)(3) of this section, be shared equally between RW and SK.

Example (15). (i) JB and DK form a limited partnership for the purpose of purchasing residential real estate to lease. JB, the limited partner, contributes $13,500, and DK, the general partner, contributes $1,500. The partnership, which uses the cash receipts and disbursements method of accounting, purchases a building for $100,000 (on leased land), incurring a recourse mortgage of $85,000 that requires the payment of interest only for a period of 3 years. The partnership agreement provides that partnership net taxable income and loss will be allocated 90 percent to JB and 10 percent to DK, the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances (as set forth in paragraph (b)(2)(ii)(*b*)(*2*) of this section), and JB is not required to restore any deficit balance in his capital account, but DK is so required. The partnership agreement contains a qualified income offset (as defined in paragraph (b)(2)(ii)(*d*) of this section). As of the end of each of the partnership's first 3 taxable years, the items described in paragraphs (b)(2)(ii)(*d*)(*4*), (*5*), and (*6*) of this section are not reasonably expected to cause or increase a deficit balance in JB's capital account. In the partnership's first taxable year, it has rental income of $10,000, operating expenses of $2,000, interest expense of $8,000, and cost recovery deductions of $12,000. Under the partnership agreement JB and DK are allocated $10,800 and $1,200, respectively, of the $12,000 net taxable loss incurred in the partnership's first taxable year.

	JB	*DK*
Capital account upon formation	$13,500	$1,500
Less: Year 1 net loss	(10,800)	(1,200)
Capital account at end of year 1	$2,700	$300

The alternate economic effect test contained in paragraph (b)(2)(ii)(*d*) of this section is satisfied as of the end of the partnership's first taxable year. Thus, the allocation made in the partnership's first taxable year has economic effect.

(ii) Assume the same facts as in (ii) and that in the partnership's second taxable year it again has rental income of $10,000, operating expenses of $2,000, interest expense of $8,000, and cost recovery deductions of $12,000. Under the partnership agreement JB and DK are allocated $10,800 and $1,200, respectively, of the $12,000 net taxable loss incurred in the partnership's second taxable year.

	JB	*DK*
Capital account at beginning of year 1	$2,700	$300
Less: year 2 net loss	(10,800)	(1,200)
Capital account at end of year 2	($8,100)	($900)

Only $2,700 of the $10,800 net taxable loss allocated to JB satisfies the alternate economic effect test contained in paragraph (b)(2)(ii)*(d)* of this section as of the end of the partnership's second taxable year. The allocation of such $2,700 net taxable loss to JB (consisting of $2,250 of rental income, $450 of operating expenses, $1,800 of interest expense, and $2,700 of cost recovery deductions) has economic effect. The remaining $8,100 of net taxable loss allocated by the partnership agreement to JB must be reallocated in accordance with the partners' interests in the partnership. Under paragraph (b)(3)(iii) of this section, the determination of the partners' interests in the remaining $8,100 net taxable loss is made by comparing how distributions (and contributions) would be made if the partnership sold its property at its adjusted tax basis and liquidated immediately following the end of the partnership's first taxable year with the results of such a sale and liquidation immediately following the end of the partnership's second taxable year. If the partnership's real property were sold for its $88,000 adjusted tax basis and the partnership were liquidated immediately following the end of the partnership's first taxable year, the $88,000 sales proceeds would be used to repay the $85,000 note, and there would be $3,000 remaining in the partnership, which would be used to make liquidating distributions to DK and JB of $300 and $2,700, respectively. If such property were sold for its $76,000 adjusted tax basis and the partnership were liquidated immediately following the end of the partnership's second taxable year, DK would be required to contribute $9,000 to the partnership in order for the partnership to repay the $85,000 note, and there would be no assets remaining in the partnership to distribute. A comparison of these outcomes indicates that JB bore $2,700 and DK $9,300 of the economic burden that corresponds to the $12,000 net taxable loss. Thus, in addition to the $1,200 net taxable loss allocated to DK under the partnership agreement, $8,100 of net taxable loss will be reallocated to DK under paragraph (b)(3)(iii) of this section. Similarly, for subsequent taxable years, absent an increase in JB's capital account, all net taxable loss allocated to JB under the partnership agreement will be reallocated to DK.

(iii) Assume the same facts as in (ii) and that in the partnership's third taxable year there is rental income of $35,000, operating expenses of $2,000, interest expense of $8,000, and cost recovery deductions of $10,000. The capital accounts of the partners maintained on the books of the partnership do not take into account the reallocation to DK of the $8,100 net taxable loss in the partnership's second taxable year. Thus, an allocation of the $15,000 net taxable income $13,500 to JB and $1,500 to DK (as dictated by the partnership agreement and as reflected in the capital accounts of the partners) does not have economic effect. The partners' interests in the partnership with respect to such $15,000 taxable gain again is made in the manner described in paragraph (b)(3)(iii) of this section. If the partnership's real property were sold for its $76,000 adjusted tax basis and the partnership were liquidated immediately following the end of the partnership's second taxable year, DK would be required to contribute $9,000 to the partnership in order for the partnership to repay the $85,000 note, and there would be no assets remaining to distribute. If such property were sold for its $66,000 adjusted tax basis and the partnership were liquidated immediately following the end of the partnership's third taxable year, the $91,000 ($66,000 sales proceeds plus $25,000 cash on hand) would be used to repay the $85,000 note and there would be $6,000 remaining in the partnership, which would be used to make liquidating distributions to DK and JB of $600 and $5,400, respectively. Accordingly, under paragraph (b)(3)(iii) of this section the $15,000 net taxable income in the partnership's third taxable year will be reallocated $9,600 to DK (minus $9,000 at end of the second taxable year to positive $600 at end of the third taxable year) and $5,400 to JB (zero at end of the second taxable year to positive $5,400 at end of the third taxable year).

Example (16). (i) KG and WN form a limited partnership for the purpose of investing in improved real estate. KG, the general partner, contributes $10,000 to the partnership, and WN, the limited partner, contributes $990,000 to the partnership. The $1,000,000 is used to purchase an apartment building on leased land. The partnership agreement provides that (1) the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section; (2) cash will be distributed first to WN until such time as he has received the amount of his original capital contribution ($990,000), next to KG until such time as he has received the amount of his original capital contribution ($10,000), and thereafter equally between WN and KG; (3) partnership net taxable income will be allocated 99 percent to WN and 1 percent to KG until the cumulative net taxable income allocated for all taxable years is equal to the cumulative net taxable loss previously allocated to the partners, and thereafter equally between WN and KG; (4) partnership net taxable loss will be allocated 99 percent to WN and 1 percent to KG, unless net taxable income has previously been allocated equally between WN and KG, in which case such net taxable loss first will be allocated equally until the cumulative net taxable loss allocated for all taxable years is equal to the cumulative net taxable income previously allocated to the partners; and (5) upon liquidation, WN is not required to restore any deficit balance in his capital account, but KG is so required. Since distributions in liquidation are not required to be made in accordance with the partners' positive capital account balances, and since WN is not required, upon the liquidation of his interest, to restore the deficit balance in his capital account to the partnership, the allocations provided by the partnership agreement do not have economic effect and will be reallocated in accordance with the partners' interests in the partnership under paragraph (b)(3) of this section.

(ii) Assume the same facts as in (i) except that the partnership agreement further provides that distributions in liquidation of the partnership (or any partner's interest) are to be made in accordance with the partners' positive capital account balances (as set forth in paragraph (b)(2)(ii)*(b)(2)* of this section). Assume further that the partnership agreement contains a qualified income offset (as defined in paragraph (b)(2)(ii)*(d)* of this section) and that, as of the end of each partnership taxable year, the items described in paragraphs (b)(2)(iii)*(d)(4)*, *(5)*, and *(6)* of this section are not reasonably expected to cause or increase a deficit balance in WN's capital account. The allocations provided by the partnership agreement have economic effect.

Example (17). FG and RP form a partnership with FG contributing cash of $100 and RP contributing property, with 2 years of cost recovery deductions remaining, that has an adjusted tax basis of $80 and a fair market value of $100. The partnership, FG, and RP have calendar taxable years. The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, liquidation proceeds will be made in accordance with capital account balances, and each partner is liable to restore the deficit balance in his capital account to the partnership upon liquidation of his interest (as set forth in paragraphs (b)(2)(ii)*(b)(2)* and *(3)* of this section). FG expects to be in a substantially higher tax bracket than RP in the partnership's first taxable year. In the partnership's second taxable year, and in subsequent taxable years, it is expected that both will be in approximately equivalent tax brackets. The partnership agreement allocates all items equally except that all $50 of book depreciation is allocated to FG in the partnership's first taxable year and all $50 of book depreciation is allocated to RP in the partnership's second taxable year. If the allocation to FG of all book depreciation in the partnership's first taxable year is respected, FG would be entitled under section 704(c) to the entire cost recovery deduction ($40) for such year. Likewise, if the allocation to RP of all the book depreciation in the partnership's second taxable year is respected, RP would be entitled under section 704(c) to the entire cost recovery deduction ($40) for such year. The allocation of book depreciation to FG and RP in the partnership's first 2 taxable years has economic effect within the meaning of paragraph (b)(2)(ii) of this section. However, the economic effect of these allocations is not substantial under the test described in paragraph (b)(2)(iii)*(c)* of this section since there is a strong likelihood at the time such allocations became part of the partnership agreement that at the end of the 2-year period to which such allocations relate, the net increases and decreases to FG's and RP's capital accounts will be the same with such allocations as they would have been in the absence of such allocation, and the total tax liability of FG and RP for the taxable years to which the section 704(c) determinations relate would be reduced as a result of the allocations of book depreciation. As a result the allocations of book depreciation in the partnership agreement will be disregarded. FG and RP will be allocated such book depreciation in accordance with the partners' interests in the partnership under paragraph (b)(3) of this section. Under these facts the book depreciation deductions will be reallocated equally between the partners, and section 704(c) will be applied with reference to such reallocation of book depreciation.

Example (18). (i) WM and JL form a general partnership by each contributing $300,000 thereto. The partnership uses the $600,000 to purchase an item of tangible personal property, which it leases out. The partnership elects under section 48(q)(4) to reduce the amount of investment tax credit in lieu of adjusting the tax basis of such property. The partnership agreement provides that (1) the partners' capital account will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, (2) distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the parents' positive capital account balances (as set forth in paragraph (b)(2)(ii)(*b*)(*2*) of this section), (3) any partner with a deficit balance in his capital account following the liquidation of his interest must restore that deficit to the partnership (as set forth in paragraph (b)(2)(ii)(*b*)(*3*) of this section), (4) all income, gain, loss, and deduction of the partnership will be allocated equally between the partners, and (5) all non-liquidating distributions of the partnership will be made equally between the partners. Assume that in each of the partnership's taxable years, it recognizes operating income equal to its operating deductions (excluding cost recovery and depreciation deductions and gain or loss on the sale of its property). During its first 2 taxable years, the partnership has an additional $200,000 cost recovery deduction in each year. Pursuant to the partnership agreement these items are allocated equally between WM and JL.

	WM	*Jul*
Capital account upon formation	$300,000	$300,000
Less: net loss for years 1 and 2	(200,000)	(200,000)
Capital account at end of year 2	$100,000	$100,000

The allocations made in the partnership's first 2 taxable years have substantial economic effect.

(ii) Assume the same facts as in (i) and that MK is admitted to the partnership at the beginning of the partnership's third taxable year. At the time of his admission, the fair market value of the partnership property is $600,000. MK contributes $300,000 to the partnership in exchange for an equal one-third interest in the partnership, and, as permitted under paragraph (b)(2)(iv)(*g*), the capital accounts of WM and JL are adjusted upward to $300,000 each to reflect the fair market value of partnership property. In addition, the partnership agreement is modified to provide that depreciation and gain or loss, as computed for tax purposes, with respect to the partnership property that appreciated prior to MK's admission will be shared among the partners in a manner that takes account of the variation between such property's $200,000 adjusted tax basis and its property's $200,000 adjusted tax basis and its $600,000 book value in accordance with paragraph (b)(2)(iv)(*f*) and the special rule contained in paragraph (b)(4)(i) of this section. Depreciation and gain or loss, as computed for book purposes, with respect to such property will be allocated equally among the partners and, in accordance with paragraph (b)(2)(iv)(*g*) of this section, will be reflected in the partners' capital accounts, as will all other partnership income, gain, loss, and deduction. Since the requirements of (b)(2)(iv)(*g*) of this section are satisfied, the capital accounts of the partners (as adjusted) continue to be maintained in accordance with paragraph (b)(2)(iv) of this section.

(iii) Assume the same facts as in (ii) and that immediately after MK's admission to the partnership, the partnership property is sold for $600,000, resulting in a taxable gain of $400,000 ($600,000 less $200,000 adjusted tax basis) and no book gain or loss, and the partnership is liquidated. An allocation of the $400,000 taxable gain cannot have economic effect because such gain cannot properly be reflected in the partners' book capital accounts. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the $400,000 taxable gain will, in accordance with section 704(c) principles, be shared equally between WN and JL.

	WM		*JL*		*MK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account at beginning of year 3	$100,000	$300,000	$100,000	$300,000	$300,000	$300,000
Plus: gain	200,000	-0-	200,000	-0-	-0-	-0-
Capital account before liquidation	$300,000	$300,000	$300,000	$300,000	$300,000	$300,000

The $900,000 of partnership cash ($600,000 sales proceeds plus $300,000 contributed by MK) is distributed equally among WM, JL, and MK in accordance with their adjusted positive capital account balances, each of which is $300,000.

(iv) Assume the same facts as in (iii) except that prior to liquidation the property appreciates and is sold for $900,000, resulting in a taxable gain of $700,000 ($900,000 less $200,000 adjusted tax basis) and a book gain of $300,000 ($900,000 less $600,000 book value). Under the partnership agreement the $300,000 of book gain is allocated equally among the partners, and such allocation has substantial economic effect.

	WM		*JL*		*MK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account at beginning of year 3	$100,000	$300,000	$100,000	$300,000	$300,000	$300,000
Plus: gain	300,000	100,000	300,000	100,000	100,000	100,000
Capital account before liquidation	$400,000	$400,000	$400,000	$400,000	$400,000	$400,000

Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the $700,000 taxable gain is, in accordance with section 704(c) principles, shared $300,000 to JL, $300,000 to WM, and $100,000 to MK. This ensures that (1) WM and JL share equally the $400,000 taxable gain that is attributable to appreciation in the property that occurred prior to MK's admission to the partnership in the same manner as it was reflected ir their capital accounts upon MK's admission, anc (2) WM, JL, and MK share equally the additiona $300,000 taxable gain in the same manner as they shared the $300,000 book gain.

(v) Assume the same facts as in (ii) except that shortly after MK's admission the property depreciates and is sold for $450,000, resulting in a taxable gain of $250,000 ($450,000 less $200,000 adjusted tax basis) and a book loss of $150,000 $450,000 less $600,000 book value). Under the partnership agreement these items are allocated as follow:

	WM		*JL*		*MK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account at beginning of year 3	$100,000	$300,000	$100,000	$300,000	$300,000	$300,000
Plus: gain	125,000	-0-	125,000	-0-	-0-	-0-
Less: loss	-0-	(50,000)	-0-	(50,000)	-0-	(50,000)
Capital account before liquidation	$225,000	$250,000	$225,000	$250,000	$300,000	$250,000

The $150,000 book loss is allocated equally among the partners, and such allocation has substantial economic effect. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the $250,000 taxable gain is, in accordance with section 704(c) principles, shared equally between WM and JL. The fact that MK bears an economic loss of $50,000 without a corresponding taxable loss is attributable entirely to the "ceiling rule." See paragraph (c)(2) of §1.704-1.

(vi) Assume the same facts as in (ii) except that the property depreciates and is sold for $170,000, resulting in a $30,000 taxable loss ($200,000 adjusted tax basis less $170,000) and a book loss of $430,000 ($600,000 book value less $170,000). The book loss of $430,000 is allocated equally among the partners ($143,333 each) and has substantial economic effect. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the entire $30,000 taxable loss is, in accordance with section 704(c) principles, included in MK's distributive share.

	WM		*JL*		*MK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account at beginning of year 3	$100,000	$300,000	$100,000	$300,000	$300,000	$300,000
Less: loss	-0-	(143,333)	-0-	(143,333)	(30,000)	(143,333)
Capital account before liquidation	$100,000	$156,667	$100,000	$156,667	$270,000	$156,667

(vii) Assume the same facts as in (ii) and that during the partnership's third taxable year, the partnership has an additional $100,000 cost recovery deduction and $300,000 book depreciation deduction attributable to the property purchased by the partnership in its first taxable year. The $300,000 book depreciation deduction is allocated equally among the partners, and that allocation has substantial economic effect. Consistent with the special partners' interests in the partnership rule contained in paragraph(b)(4)(i) of this section, the partnership agreement provides that the $100,000 cost recovery deduction for the partnership's third taxable year is, in accordance with section 704(c) principles, included in MK's distributive share. This is because under those principles MK must include the cost recovery deduction for such property in his distributive share up to the amount of the book depreciation deduction for such property properly allocated to him.

	WM		*JL*		*MK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account at beginning of year 3	$100,000	$300,000	$100,000	$300,000	$300,000	$300,000
Less: recovery/depreciation deduction for year 3	-0-	(100,000)	-0-	(100,000)	(100,000)	(100,000)
Capital account at end of year 3	$100,000	$200,000	$100,000	$200,000	$2 00,000	$200,000

(viii) Assume the same facts as in (vii) except that upon MK's admission the partnership property has an adjusted tax basis of $220,000 (instead of $200,000), and thus the cost recovery deduction for the partnership's third taxable year is $110,000. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the excess $10,000 cost recovery deduction ($110,000 less $100,000 included in MK's distributive share) is, in accordance with section 704(c) principles, shared by WM and JL in proportion to their shares of book depreciation. Since their shares of book depreciation were equal, they each must include $5,000 of the cost recovery deduction in their distributive shares for the partnership's third taxable year.

(ix) Assume the same facts as in (vii) except that upon MK's admission the partnership agreement is amended to allocate the first $400,000 of book depreciation and loss on partnership property equally between WM and JL and the last $200,000 of such book depreciation and loss to MK. Assume such allocations have substantial economic effect. Pursuant to this amendment the $300,000 book depreciation deduction in the partnership's third taxable year is allocated equally between WM and JL. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the $100,000 cost recovery deduction is, in accordance with section 704(c) principles, shared equally between WM and JL. In the partnership's fourth taxable year, it has a $60,000 cost recovery deduction and a $180,000 book depreciation deduction. Under the amendment described above, the $180,000 book depreciation deduction is allocated $50,000 to WM, $50,000 to JL, and $80,000 to MK. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the $60,000 cost recovery deduction is, in accordance with section 704(c) principles, included entirely in MK's distributive share.

	WM		*JL*		*MK*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account at beginning of year 3	$100,000	$300,000	$100,000	$300,000	$300,000	$300,000
Less: (a) recovery/depreciation deduction for year 3	(50,000)	(150,000)	(50,000)	(150,000)	-0-	-0-
(b) recovery/depreciation deduction for year 4	-0-	(50,000)	-0-	(50,000)	(60,000)	(80,000)
Capital account at end of year 4	$50,000	$100,000	$50,000	$100,000	$240,000	$220,000

(x) Assume the same facts as in (vii) and that at the beginning of the partnership's third taxable year, the partnership purchases a second item of tangible personal property for $300,000 and elects under section 48(q)(4) to reduce the amount of investment tax credit in lieu of adjusting the tax basis of such property. The partnership agreement is amended to allocate the first $150,000 of cost recovery deductions and loss from such property to WM and the next $150,000 of cost recovery deductions and loss from such property equally between JL and MK. Thus, in the partnership's third taxable year it has, in addition to the items specified in (vii), a cost recovery and book depreciation deduction of $100,000 attributable to the newly acquired property, which is allocated entirely to WM. As in (vii), the allocation of the $300,000 book depreciation attributable to the property purchased in the partnership's first taxable year equally among the partners has substantial economic effect, and consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement properly provides for the entire $100,000 cost recovery deduction attributable to such property to be included in MK's distributive share. Furthermore, the allocation to WM of the $100,000 cost recovery deduction attributable to the property purchased in the partnership's third taxable year has substantial economic effect.

	WM		JL		MK	
	Tax	Book	Tax	Book	Tax	Book
Capital account at beginning of year 3	$100,000	$300,000	$100,000	$300,000	$300,000	$300,000
Less: (a) recovery/depreciation deduction for property bought in year 1	-0-	(100,000)	-0-	(100,000)	(100,000)	(100,000)
(b) recovery/depreciation deduction for property bought in year 3	(100,000)	(100,000)	-0-	-0-	-0-	-0-
Capital account at end of year 3	-0-	$100,000	$100,000	$200,000	$200,000	$200,000

(xii) Assume the same facts as in (x) and that in the partnership's fourth taxable year it has a cost recovery deduction of $60,000 and book depreciation deduction of $180,000 attributable to the property purchased in the partnership's first taxable year, and a cost recovery and book depreciation deduction of $100,000 attributable to the property purchased in the partnership's third taxable year. The $180,000 book depreciation deduction attributable to the property purchased in the partnership's first taxable year is allocated equally among the partners, and such allocation has substantial economic effect. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the $60,000 cost recovery deduction attributable to the property purchased in the first taxable year is, in accordance with section 704(c) principles, included entirely in MK's distributive share. Furthermore, the $100,000 cost recovery deduction attributable to the property purchased in the third taxable year is allocated $50,000 to WM, $25,000 to JL, and $25,000 to MK, and such allocation has substantial economic effect.

	WM		JL		MK	
	Tax	Book	Tax	Book	Tax	Book
Capital account at beginning of year 4	-0-	$100,000	$100,000	$200,000	$200,000	$200,000
Less: (a) recovery/depreciation deduction for property bought in year 1	-0-	(60,000)	-0-	(60,000)	(60,000)	(60,000)
(b) recovery/depreciation deduction for property bought in year 3	(50,000)	(50,000)	(25,000)	(25,000)	(25,000)	(25,000)
Capital account at end of year 4	($50,000)	($10,000)	$75,000	$115,000	$115,000	$115,000

At the end of the partnership's fourth taxable year the adjusted tax bases of the partnership properties acquired in its first and third taxable years are $40,000 and $100,000, respectively. If the properties are disposed of at the beginning of the partnership's fifth taxable year for their adjusted tax bases, there would be no taxable gain or loss, a book loss of $80,000 on the property purchased in the partnership's first taxable year ($120,000 book value less $40,000), and cash available for distribution of $140,000.

	WM		JL		MK	
	Tax	Book	Tax	Book	Tax	Book
Capital account at beginning of year 5	($50,000)	($10,000)	$75,000	$115,000	$115,000	$115,000
Less: loss	-0-	(26,667)	-0-	(26,667)	-0-	(26,667)
Capital account before liquidation	($50,000)	($36,667)	$75,000	$88,333	$115,000	$88,333

If the partnership is then liquidated, the $140,000 of cash on hand plus the $36,667 balance that WM would be required to contribute to the partnership (the deficit balance in his book capital account) would be distributed equally between JL and MK in accordance with their adjusted positive book capital account balances.

(xiii) Assume the same facts as in (i). Any tax preferences under section 57(a)(12) attributable to the partnership's cost recovery deductions in the first 2 taxable years will be taken into account equally by WM and JL. If the partnership agreement instead provides that the partnership's cost recovery deductions in its first 2 taxable years are allocated 25 percent to WM and 75 percent to JL (and such allocations have substantial economic effect), the tax preferences attributable to such cost recovery deductions would be taken into account 25 percent by WM and 75 percent by JL. The conclusion in the previous sentence is unchanged even if the partnership's operating expenses (exclusive of cost recovery and depreciation deductions) exceed its operating income in each of the partnership's first 2 taxable years, the resulting net loss is allocated entirely to WM, and the cost recovery deductions are allocated 25 percent to WM and 75 percent to JL (provided such allocations have substantial economic effect). If the partnership agreement instead provides that all income, gain, loss, and deduction (including cost recovery and depreciation deductions) are allocated equally between JL and WM, the tax preferences attributable to the cost recovery deductions would be taken into account equally by JL and WM. In this case, if the partnership has a $100,000 cost recovery deduction in its first taxable year and an additional net loss of $100,000 in its first taxable year (*i.e.*, its operating expenses exceed its operating income by $100,000) and purports to categorize JL's $100,000 distributive share of partnership loss as being attributable to the cost recovery deduction and WM's $100,000 distributive share of partnership loss as being attributable to the net loss, the economic effect of such allocations is not substantial, and each partner will be allocated one-half of all partnership income, gain, loss, and deduction and will take into account one-half of the tax preferences attributable to the cost recovery deductions.

Example (19). (i) DG and JC form a general partnership for the purpose of drilling oil wells.

DG contributes an oil lease, which has a fair market value and adjusted tax basis of $100,000. JC contributes $100,000 in cash, which is used to finance the drilling operations. The partnership agreement provides that DG is credited with a capital account of $100,000, and JC is credited with a capital account of $100,000. The agreement further provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances, and any partner with a deficit balance in his capital account following the liquidation of his interest must restore such deficit to the partnership (as set forth in paragraphs (b)(2)(ii)(b)*(2)* and *(3)* of this section). The partnership chooses to adjust capital accounts on a simulated cost depletion basis and elects under section 48(q)(4) to reduce the amount of investment tax credit in lieu of adjusting the basis of its section 38 property. The agreement further provides that (1) all additional cash requirements of the partnership will be borne equally by DG and JC, (2) the deductions attributable to the property (including money) contributed by each partner will be allocated to such partner, (3) all other income, gain, loss, and deduction (and item thereof) will be allocated equally between DG and JC, and (4) all cash from operations will be distributed equally between DG and JC. In the partnership's first taxable year $80,000 of partnership intangible drilling cost deductions and $20,000 of cost recovery deductions on partnership equipment are allocated to JC, and the $100,000 basis of the lease is, for purposes of the depletion allowance under sections 611 and 613A(c)(7)(D), allocated to DG. The allocations of income, gain, loss, and deduction provided in the partnership agreement have substantial economic effect. Furthermore, since the allocation of the entire basis of the lease to DG will not result in capital account adjustments (under paragraph (b)(2)*(iv)(k)* of this section) the economic effect of which is insubstantial, and since all other partnership allocations are recognized under this paragraph,the allocation of the $100,000 adjusted basis of the lease to DG is, under paragraph (b)(4)(v) of this section, recognized as being in accordance with the partners' interests in partnership capital for purposes of section 613A(c)(7)(D).

(ii) Assume the same facts as in (i) except that the partnership agreement provides that (1) all additional cash requirements of the partnership for additional expenses will be funded by additional contributions from JC, (2) all cash from operations will first be distributed to JC until the excess of such cash distributions over the amount of such additional expenses equals his initial $100,000 contribution, (3) all deductions attributable to such additional operating expenses will be allocated to JC, and (4) all income will be allocated to JC until the aggregate amount of income allocated to him equals the amount of partnership operating expenses funded by his initial $100,000 contribution plus the amount of additional operating expenses paid from contributions made solely by him. The allocations of income, gain, loss, and deduction provided in the partnership agreement have economic effect. In addition, the economic effect of the allocations provided in the agreement is substantial. Because the partnership's drilling activities are sufficiently speculative, there is not a strong likelihood at the time the disproportionate allocations of loss and deduction to JC are provided for by the partnership agreement that the economic effect of such allocations will be largely offset by allocations of income. In addition, since the allocation of the entire basis of the lease to DG will not result in capital account adjustments (under paragraph (b)(2)*(iv)(k)* of this section) the economic effect of which is insubstantial, and since all other partnership allocations are recognized under this paragraph, the allocation of the adjusted basis of the lease to DG is, under paragraph (b)(4)(v) of this section, recognized as being in accordance with the partners' interests in partnership capital under section 613A(c)(7)(D).

(iii) Assume the same facts as in (i) except that all distributions, including those made upon liquidation of the partnership, will be made equally between DG and JC, and no partner is obligated to restore the deficit balance in his capital account to the partnership following the liquidation of his interest for distribution to partners with positive capital account balances. Since liquidation proceeds will be distributed equally between DG and JC irrespective of their capital account balances, and since no partner is required to restore the deficit balance in his capital account to the partnership upon liquidation (in accordance with paragraph (b)(2)(ii)*(b)(3)* of this section), the allocations of income, gain, loss, and deduction provided in the partnership agreement do not have economic effect and must be reallocated in accordance with the partners' interests in the partnership under paragraph (b)(3) of this section. Under these facts all partnership income, gain, loss, and deduction (and item thereof) will be reallocated equally between JC and DG. Furthermore, the allocation of the $100,000 adjusted tax basis of the lease to DG is not, under paragraph (b)(4)(v) of this section, deemed to be in accordance with the partners' interests in partnership capital under section 613A(c)(7)(D), and such basis must be reallocated in accordance with the partners' interests in partnership capital or income as determined under section 613A(c)(7)(D). The results in this example would be the same if JC's initial cash contribution were $1,000,000 (instead of $100,000), but in such case the partners should consider whether, and to what extent, the provisions of paragraph (b)(1) of §1.721-1, and principles related thereto, may be applicable.

(iv) Assume the same facts as in (i) and that for the partnership's first taxable year the simulated depletion deduction with respect to the lease is $10,000. Since DG properly was allocated the entire depletable basis of the lease (such allocation having been recognized as being in accordance with DG's interest in partnership capital with respect to such lease), under paragraph (b)(2)(iv)*(k)(1)* of this section the partnership's $10,000 simulated depletion deduction is allocated to DG and will reduce his capital account accordingly. If (prior to any additional simulated depletion deductions) the lease is sold for $100,000, paragraph (b)(4)(v) of this section requires that the first $90,000 (*i.e.*, the partnership's simulated adjusted basis in the lease) out of the $100,000 amount realized on such sale be allocated to DG (but does not directly affect his capital account). The partnership agreement allocates the remaining $10,000 amount realized equally between JC and DG (but such allocation does not directly affect their capital accounts). This allocation of the $10,000 portion of amount realized that exceeds the partnership's simulated adjusted basis in the lease will be treated as being in accordance with the partners' allocable shares of such amount realized under section 613A(c)(7)(D) because such allocation will not result in capital account adjustments (under paragraph (b)(2)(iv)*(k)* of this section) the economic effect of which is insubstantial, and all other partnership allocations are recognized under this paragraph. Under paragraph (b)(2)(iv)*(k)* of this section, the partners' capital accounts are adjusted upward by the partnership's simulated gain of $10,000 ($100,000 sales price less $90,000 simulated adjusted basis) in proportion to such partners' allocable shares of the $10,000 portion of the total amount realized that exceeds the partnership's $90,000 simulated adjusted basis ($5,000 to JC and $5,000 to DG). If the lease is sold for $50,000, under paragraph (b)(4)(v) of this section the entire $50,000 amount realized on the sale of the lease will be allocated to DG (but will not directly affect this capital account). Under paragraph (b)(2)(iv)*(k)* of this section the partners' capital accounts will be adjusted downward by the partnership's $40,000 simulated loss ($50,000 sales price less $90,000 simulated adjusted basis) in proportion to the partners' allocable shares of the total amount realized from the property that represents recovery of the partnership's simulated adjusted basis therein. Accordingly, DG's capital account will be reduced by such $40,000.

* * * * *

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved, December 19, 1985

RONALD A. PEARLMAN,
Assistant Secretary
of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on December 24, 1985, 11:58 a.m., and published in the issue of the Federal Register for December 31, 1985, 50 F.R. 53420)

Section 1033.—Involuntary Conversions

26 CFR 1.1033(a)-2: Involuntary conversion into similar property, into money or into dissimilar property.

Involuntary conversion; insurance proceeds; use and occupancy insurance contract. The Service will look to the underwriting and actuarial criteria and any other information used in writing the insurance to determine if the insurance is designed to reimburse for a loss of profits and fixed charges. Rev. Rul. 73-477 amplified.

Rev. Rul. 86-12

ISSUE

Are the written terms of a contract,

described as a "use and occupancy insurance contract", the sole basis to determine whether insurance proceeds from the contract are proceeds from insurance against lost profits within the meaning of section 1.1033(a)-2(c)(8) of the Income Tax Regulations?

FACTS

The taxpayer, a domestic corporation, purchased a business interruption insurance policy. The written terms of the contract provide for protection and reimbursement for loss of the use and occupancy of the taxpayer's building and machinery resulting from fire or other casualty. The contract provides for a fixed payment of 200x dollars per day. The written contract does not specify how the amount of this coverage or the premium for the policy was computed. However, the premium and coverage were arrived at by application of underwriting and actuarial criteria and were based exclusively on the profits and fixed charges experience of the taxpayer.

In 1981 the building and machinery were destroyed by fire and the taxpayer was reimbursed under its policy. The taxpayer invested all of the proceeds, received from the insurance company for its loss, in the rebuilding of the building and in repurchasing machinery.

LAW AND ANALYSIS

Section 1033 of the Internal Revenue Code provides, in general, for the nonrecognition of gain to the extent that the proceeds of an involuntary conversion of property are used to purchase qualified replacement property.

Section 1.1033(a)-2(c)(8) of the regulations provides that the proceeds of a use and occupancy insurance contract, which by its terms insured against actual loss sustained of net profits in the business, are not proceeds of an involuntary conversion but are income in the same manner that the profits for which they are substituted would have been.

In Rev. Rul. 73-477, 1973-2 C.B. 302, the Internal Revenue Service was asked to consider whether the proceeds from an insurance contract that provided for per diem payments of 35*x* dollars, whenever specified causes suspended business operations, were subject to the nonrecognition treatment under section 1033 of the Code. Rev. Rul. 73-477 holds that because the insurance contract permits reduction of coverage based on profits and fixed charges experience, the insurance is designed to reimburse the taxpayer for a loss of net profits and fixed charges. Thus, the insurance proceeds were treated as ordinary income and nonrecognition treatment under section 1033 was not available.

The facts in the instant situation are similar to those in Rev. Rul. 73-477, except that it is necessary to go beyond the terms on the face of the use and occupancy contract to determine the precise nature of the contract. See, *Helvering v. Le Gierse*, 312 U.S. 531 (1941), 1941-1 C.B. 430.

Section 1.1033(a)-2(c)(8) of the regulations is not intended to limit determinations of the type of insurance provided by a use and occupancy insurance contract to an examination of only the terms on the face of the contract. Thus, the insurance contract in this situation is determined to include underwriting and acturial criteria based on the profits and fixed charges experience of the taxpayer.

HOLDING

Written terms of a contract, described as a use and occupancy insurance contract, are not the sole basis to determine whether insurance proceeds from the contract qualify as proceeds of an involuntary conversion under section 1033 of the Code. The Service will look to the underwriting and actuarial criteria and any other information used in writing the insurance to determine if the insurance is designed to reimburse for a loss of profits and fixed charges. Accordingly, under the policy described above, insurance proceeds will be ordinary income and nonrecognition treatment under section 1033 will not be available.

EFFECT ON OTHER DOCUMENT

Rev. Rul. 73-477 is amplified.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 467, 483.)

Rev. Rul. 86-13

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of February 1986 are as follows:

	Period for Compounding			
	Annual	Semiannual	Quarterly	Monthly
Short-Term				
AFR	8.06%	7.90%	7.82%	7.77%
110% AFR	8.88%	8.69%	8.60%	8.54%
120% AFR	9.70%	9.48%	9.37%	9.30%
Mid-Term				
AFR	8.96%	8.77%	8.68%	8.61%
110% AFR	9.88%	9.65%	9.54%	9.46%
120% AFR	10.80%	10.52%	10.39%	10.30%
Long-Term				
AFR	9.63%	9.41%	9.30%	9.23%
110% AFR	10.62%	10.35%	10.22%	10.13%
120% AFR	11.61%	11.29%	11.14%	11.03%

Section 3101.—Rate of Tax

26 CFR 31.3101-1: Measure of employee tax.

Whether payments by an employer of the employee FICA tax without deduction from the employee's wages under an agreement between them are subject to employee FICA tax. See Rev. Rul. 86-14, this page.

Section 3121.—Definitions

26 CFR 31.3121(a)(6)-1 Payment by an employer of employee tax under section 3101 or employee contributions under a State law.

(Also Sections 61, 162, 3101, 3306, 3401, 6051, 6413; 1.61-2, 1.162-7, 31.3101-1, 31.3306(b)(6)-1, 31.3401(a)-1, 31.6051-1, 31.6413(c)-1.)

Payment of employee FICA tax by employer without deduction from wages. Payments by an employer of employee FICA tax without deduction from employee's wages under an agreement between them are additional wages for FICA purposes, the amount of wages to be determined by a formula. The additional FICA wages so determined are includible in the employee's gross income and are wages for purposes of income tax withholding. If otherwise appropriate, the employer may deduct the payments as ordinary and necessary business expenses under section 162 of the Code. Rev. Rul. 74-75 modified.

Rev. Rul. 86-14

ISSUE

What are the federal income and employment tax consequences when an employer agrees with an employee to pay the employee Federal Insurance Contributions Act (FICA) tax imposed by section 3101 of the Internal Revenue Code without deducting the amount of the taxes from the employee's pay?

FACTS

Situation 1. During 1985, an employer agreed to pay an employee $200 weekly. The payments are "wages" for "employment" under section 3121(a) of the Code (relating to the FICA), section 3306(b) (relating to the Federal Unemployment Tax Act (FUTA)), and section 3401(a) (relating to income tax withholding). The payments are not for domestic service in the employer's private home or for agricultural labor. The employer further agreed to pay the employee FICA taxes imposed by section 3101 without deducting them from the $200 paid to the employee.

Situation 2. The facts are the same as in *Situation 1*, except that the pay was either for domestic service in the employer's private home or for agricultural labor.

LAW AND ANALYSIS

Section 61(a) of the Code defines gross income as all income from whatever source derived, including compensation for services.

Taxes assessed against an employee and paid by an employer in partial consideration for service are includible in the employee's gross income. *Old Colony Trust Co. v. Commissioner*, 279 U.S. 716 (1929), VIII-2 C.B. 222 (1929).

Sections 3121(a)(6)(A) and 3306(b)(6)(A) of the Code except from "wages," for FICA and FUTA purposes, respectively, an employer's payment (without deduction from the employee's pay) of the employee FICA taxes imposed by section 3101, in the case of pay for domestic service in the employer's private home or for agricultural labor. Those sections previously excepted from wages all payments of employee FICA taxes by an employer without deduction from the employee's pay, but the exception was limited to domestic service in the employer's home and agricultural labor by section 1141 of the Omnibus Reconciliation Act of 1980, 1980-2 C.B. 509, 530, effective for remuneration paid after December 31, 1980. (December 31, 1983, in the case of certain state and local government employees who are covered for social security purposes under an agreement under section 218 of the Social Security Act, 42 U.S.C. section 418 (1982).)

Section 31.3401(a)-1(b)(6) of the Employment Tax Regulations states that "wages," for income tax withholding purposes, includes amounts paid by an employer on behalf of an employee without deduction from the employee's pay) of the employee FICA taxes imposed by section 3101 of the Code.

Section 3401(a)(2) of the Code excepts from wages for income tax withholding purposes payments for agricultural labor, and section 3401(a)(3) excepts payments for domestic service in a private home.

Rev. Proc. 81-48, 1981-2 C.B. 623, provides a formula for determining the amount of wages under sections 3121(a), 3306(b), and 3401(a) of the Code if an employer, under an arrangement with an employee, pays the employee FICA taxes imposed by section 3101 after December 31, 1980, without deducting them from the employee's pay. However, the revenue procedure and the formula do not apply if the pay is for domestic service in the employer's private home or for agricultural labor.

The effect of section 1141 of the 1980 Act is that if an employer pays the employee FICA taxes imposed by section 3101 of the Code without deducting them from the employee's pay, the amount of the employee's wages under section 3121(a) is increased by the amount of the taxes. This increase in the wage payment is also subject to the employee FICA taxes, which has the effect of again increasing the employee's wages under section 3121(a) by the amount of the additional taxes paid by the employer. This continuing series of additional wages and additional taxes on such wages is known as "pyramiding." See Rev. Proc. 81-48.

The formula for determining an employee's FICA wages set forth in Rev. Proc. 81-48 is:

$$W = \frac{S}{1-R}$$

W = The employee's total FICA wages after the increase reflecting the pyramiding effect,

S = State pay (the pay before taking into account the pyramiding effect), and

R = Rate of employee FICA taxes.

During 1985, the employee FICA taxes imposed by section 3101 of the Code are 7.05 percent (.0705) of the wages received by the employee during the year.

In addition, in order to determine the increased wages under section 3306(b) of the Code (FUTA) and section 3401(a) (income tax withholding), it is first necessary to compute the employee FICA tax under section 3101. See section 3306(b)(6)(A) of the Code (as amended by the 1980 Act) and section 31.3401(a)-1(b)(6) of the regulations, above.

HOLDINGS

Situation 1 Using the formula set forth above, weekly FICA wages are $215.17 ($200/.9295). The weekly employee FICA taxes are 7.05 percent of those wages or $15.17.

For income tax purposes, the entire $215.17 ($200 + $15.17) is includible in the employee's gross income as compensation under section 61(a)(1) of the Code.

For FUTA and income tax withholding purposes, the employee's weekly wages are $215.17.

On the Form W-2, Wage and Tax Statement, for 1985, the employer should report the weekly $215.17 as "wages" paid subject to both income tax withholding and the FICA taxes in the boxes entitled "Wages, tips, other compensation" and "social security wages." The employer should report the weekly $15.17 in the box entitled "Social security tax withheld," even though the tax was not actually withheld.

Assuming that it is otherwise appropriate, the employer may deduct the $215.17 as an ordinary and necessary business expense under section 162 of the Code.

Situation 2 Because in this situation FICA and FUTA wages do not include the employee FICA taxes paid by the employer, FICA and FUTA wages are equal to the $200 stated pay. The employee FICA taxes are $14.10 (7.05 percent of FICA wages).

For income tax purposes, $214.10 ($200 + $14.10) is includible in the employee's gross income as compensation under section 61(a)(1) of the Code.

Pursuant to section 3401(a)(2) or (3) of the Code, none of the $214.10 is wages for purposes of income tax withholding.

On the Form W-2 for 1985, the employer should report the weekly $214.10 as "other compensation" in the box entitled "Wages, tips, other compensation"; the weekly $200 in the box entitled "Social security wages"; and the weekly $14.10 in the box entitled "Social security tax withheld," even though the tax was not actually withhheld.

Assuming that it is otherwise appropriate, the employer may deduct the $214.10 attributable to agricultural labor as an ordinary and necessary business expense under section 162 of the Code. Ordinarily, wages paid for domestic services in one's home are not deductible under section 162.

Both Situations If the employee received wages subject to FICA taxes from two or more employers during the year, and as a result the wages exceeded the annual limitation on wages subject to FICA taxes under section 3121(a)(1) of the Code ($39,600 in 1985), the employee is entitled, under section 6413(c)(1), to a special refund of the excess FICA taxes paid. That section indicates that the refund is conditioned on the taxes being deducted from the employee's wages. Because the tax liability incurred on behalf of the employee in either situation is included in the employee's gross income, it was, in effect, deducted from the employee's pay.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 74-75, 1974-1 C.B. 19, is modified.

Section 3306.—Definition

26 CFR 31.3306(b)(6)-1: Payment by an employer of employee tax under section 3101 or employee contributions under a State law.

Whether payments by an employer of the employee FICA tax without deduction from the employee's wages under an agreement between them are wages. See Rev. Rul. 86-14, page 33).

Section 3401.—Definitions

26 CFR 31.3401(a)-1: Wages.

Whether payments by an employer of the employee FICA tax without deduction from the employee's wages under an agreement between them are wages. See Rev. Rul. 86-14, page 33).

Section 6051.—Receipts for Employees

26 CFR 31.6051-1: Statements for employees.

Whether payments by an employer of the employee FICA tax without deduction from the employee's wages under an agreement between them are to be reported as wages on Form W-2. See Rev. Rul. 86-14, page 33).

Section 6413.—Special Rules Applicable to Certain Employment Taxes

26 CFR 31.6413(c)-1: Special refunds.

Whether payments by an employer of the employee FICA tax without deduction from the employee's wages under an agreement between them are considered to be deducted from the employee's pay. See Rev. Rul. 86-14, page 33).

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.105: Examination of returns and claims for refund, credit, or abatement; determination of correct tax liability.
(Also Part I, Section 168.)

Rev. Proc. 86-6

SECTION 1. PURPOSE

The purpose of this revenue procedure is to provide the revised cost recovery rates for real property under section 168 of the Internal Revenue Code.

SEC. 2. BACKGROUND

Section 168 of the Code was adopted as part of the Economic Recovery Tax Act of 1981, section 201, 1981-2 C.B. 256, 275. The Tax Reform Act of 1984, section 111, 1984-3 (Vol. 1) C.B. 1, 139, amended section 168 by changing 15-year real property to 18-year real property. Title I of the Act of October 11, 1985 (relating to Amendments to the Imputed Interest Rules), Pub. L. No. 99-121, section 103, 1985-48 I.R.B. 11, 12, changed 18-year real property to 19-year real property and extended the recovery period for real property from 18 years to 19 years.

SEC. 3. AUTHORITY

The revisions enacted as part of Title I of the Act of October 11, 1985, require the Secretary of the Trasury to prescribe tables setting forth revised rates for real property.

SEC. 4. RULES OF APPLICATION

.01 In general, these revised cost recovery rates apply to real property placed in service after May 8, 1985. However, these revised cost recovery rates do not apply to property placed in service before January 1, 1987, if before May 9, 1985, the taxpayer or a qualified person entered into a binding contract to purchase or construct such property or if before May 9, 1985, construction of such property was commenced by the taxpayer or a qualified person. For purposes of the preceding sentence, the term "qualified person" means any person whose rights in such a contract or such property are transferred to the taxpayer, but only if such property is not placed in service before such rights are transferred to the taxpayer.

.02 The revised recovery rates for 19-year real property are presented by the tables in section 5. Except with respect to low-income housing, these tables adopt the mid-month convention, which is required by section 168(b)(2)(A) of the Code. Under the mid-month convention, real property placed in service by the taxpayer at any time during a particular month is treated as placed in service in the middle of that month. Thus, only one-half month's cost recovery is permitted for the month the property is placed in service. A similar convention is to be applied with respect to dispositions prior to the end of the recovery period. Thus, one-half month's cost recovery is also permitted for the month of disposition. For low-income housing, a full-month convention is used. *See* section 168(b)(4)(A). Under the full-month convention, real property placed in service by the taxpayer at any time during a particular month is treated as placed in service on the first day of that month. Thus, a full month's cost recovery is permitted for the month the property is placed in service. A similar convention is to be applied with respect to dispositions prior to the end of the recovery period. Thus, under the full-month convention, a full-month's cost recovery is also permitted for the month of disposition.

.03 Table 1 provides the rates to be used under section 168(b)(2) of the Code for 19-year real property (other than low-income housing). This table is based on the use of the 175 percent declining balance method followed by a switch to use of the straight line method at a time to maximize the amounts deductible.

.04 Table 2 provides the rates to be used under section 168(f)(2)(B) of the Code for 19-year real property (other than low-income housing) which during the taxable year is used predominantly outside the United States. This table is based on a 35-year recovery period and the use of the 150 percent declining balance method followed by a switch to use of the straight line method at a time to maximize the amounts deductible

.05 Tables 3, 4, and 5 provide the rates to be used under section 168(b)(3) of the Code for 19-year real property (other than low-income housing) for which the optional straight line method is elected. Tables 4 and 5 also provide the rates to be used for 19-year real property which during the taxable year is used predominantly outside the U.S. for which an election under section 168(f)(2)(C) of the Code is made.

.06 Table 3 provides the rates to be used under section 168(b)(3) of the Code for 19-year real property when a 19-year recovery period is elected.

.07 Table 4 provides the rates to be used under section 168(b)(3) of the Code or section 168(f)(2)(C) of the Code for 19-year real property when a 35-year recovery period is elected.

.08 Table 5 provides the rates to be used under section 168(b)(3) of the Code or section 168(f)(2)(C) of the Code for 19-year real property when a 45-year recovery period is elected.

.09 Tables 6 through 10 provide the rates to be used for low-income housing. Table 6 provides the rates to be used under section 168(b)(4) of the Code for low-incoming housing. This table is based on the use of the 200 percent declining balance method followed by a switch to use of the straight line method at a time to maximize the amounts deductible. This table is also based on the full-month convention and a 15-year recovery period.

.10 Table 7 provides the rates to be used under section 168(f)(2)(B) of the Code for low-income housing which during the taxable year is used predominantly outside the United States. This table is based on the use of the 150 percent declining balance method followed by a switch to use of the straight line method at a time to maximize the amounts deductible. This table is also based on the full-month convention and a 35-year recovery period.

.11 Tables 8, 9, and 10 provide rates to be used under section 168(b)(3) of the Code for low-income housing for which the optional straight line method is elected. Tables 9 and 10 also provide the rates to be used for low-income housing which during the taxable year is used predominantly outside the United States for which an election under section 168(f)(2)(C) is made. Tables 8, 9, and 10 are based on the full-month convention.

.12 Table 8 provides the rates to be used under section 168(b)(3) of the Code for low-income housing for which an optional 19-year recovery period is elected.

.13 Table 9 provides the rates to be used under section 168(b)(3) of the Code for low-income housing for which an optional 35-year recovery period is elected.

.14 Table 10 provides the rates to be used under section 168(b)(3) of the Code for low-income housing for which an optional 45-year recovery period is elected.

SEC. 5. COST RECOVERY TABLES FOR 19-YEAR REAL PROPERTY:

ACRS Cost Recovery Tables for 19-Year Real Property

1. *19-Year Real Property (19-Year 175% Declining Balance)*

(Assuming Mid-Month Convention)

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	8.8	8.1	7.3	6.5	5.8	5.0	4.2	3.5	2.7	1.9	1.1	0.4
2	8.4	8.5	8.5	8.6	8.7	8.8	8.8	8.9	9.0	9.0	9.1	9.2
3	7.6	7.7	7.7	7.8	7.9	7.9	8.0	8.1	8.1	8.2	8.3	8.3
4	6.9	7.0	7.0	7.1	7.1	7.2	7.3	7.3	7.4	7.4	7.5	7.6
5	6.3	6.3	6.4	6.4	6.5	6.5	6.6	6.6	6.7	6.8	6.8	6.9
6	5.7	5.7	5.8	5.9	5.9	5.9	6.0	6.0	6.1	6.1	6.2	6.2
7	5.2	5.2	5.3	5.3	5.3	5.4	5.4	5.5	5.5	5.6	5.6	5.6
8	4.7	4.7	4.8	4.8	4.8	4.9	4.9	5.0	5.0	5.1	5.1	5.1
9	4.2	4.3	4.3	4.4	4.4	4.5	4.5	4.5	4.5	4.6	4.6	4.7
10	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
11	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
12	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
13	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
14	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
15	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
16	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
17	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
18	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
19	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
20	0.2	0.5	0.9	1.2	1.6	1.9	2.3	2.6	3.0	3.3	3.7	4.0

2. *19-Year Real Property Used Predominantly Outside the U.S. (35-Year 150% Declining Balance)*

(Assuming Mid-Month Convention)

If the Recovery Year is	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	4.1	3.7	3.4	3.0	2.7	2.3	2.0	1.6	1.3	0.9	0.5	0.2
2	4.1	4.1	4.1	4.2	4.2	4.2	4.2	4.2	4.2	4.3	4.3	4.3
3	3.9	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.1	4.1	4.1	4.1
4	3.8	3.8	3.8	3.8	3.8	3.8	3.9	3.9	3.9	3.9	3.9	3.9
5	3.6	3.6	3.6	3.6	3.7	3.7	3.7	3.7	3.7	3.8	3.7	3.7
6	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.6	3.6	3.6
7	3.3	3.3	3.3	3.3	3.3	3.4	3.4	3.4	3.4	3.4	3.4	3.4
8	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.3	3.3	3.3	3.3
9	3.0	3.0	3.0	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1
10	2.9	2.9	2.9	2.9	2.9	2.9	3.0	3.0	3.0	3.0	3.0	3.0
11	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.9	2.9	2.9	2.9
12	2.6	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.8	2.8
13	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
14	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6

2. *19-Year Real Property Used Predominantly Outside the U.S. (35-Year 150% Declining Balance) (Assuming Mid-Month Convention)*

If the Recovery Year is	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
15	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
16	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
17	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
18	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
19	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
20	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
21	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
22	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
23	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
24	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
25	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
26	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
27	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
28	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
29	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
30	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
31	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
32	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
33	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
34	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
35	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
36	0.0	0.2	0.5	0.7	0.9	1.2	1.3	1.7	1.7	1.8	2.2	2.5

3. *19-Year Real Property For Which An Optional 19-Year Straight Line Method is Elected (Assuming Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	5.0	4.6	4.2	3.7	3.3	2.9	2.4	2.0	1.5	1.1	0.7	0.2
2	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
4	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
5	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
6	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
7	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
8	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
9	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
10	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
11	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
12	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
13	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
14	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
15	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
16	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
17	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
18	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
19	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
20	0.2	0.6	1.0	1.5	1.9	2.3	2.8	3.2	3.7	4.1	4.5	5.0

4. *19-Year Real Property For Which an Optional 35-Year Straight Line Method is Elected (Assuming Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	2.7	2.5	2.3	2.0	1.8	1.5	1.3	1.1	0.8	0.6	0.4	0.1
2	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
3	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
4	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
5	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
6	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
7	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
8	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
10	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
11	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
12	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
13	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
14	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
15	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
16	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
17	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
18	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
19	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
20	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
21	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
22	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
23	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
24	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
25	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
26	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
27	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
28	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
29	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
30	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
31	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
32	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
33	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
34	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
35	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
36	0.2	0.4	0.6	0.9	1.1	1.4	1.6	1.8	2.1	2.3	2.5	2.8

5. *19-Year Real Property For Which an Optional 45-Year Straight Line Method is Elected (Assuming Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	2.1	1.9	1.8	1.6	1.4	1.2	1.0	0.8	0.6	0.5	0.3	0.1
2	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
4	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
5	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
6	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3

5. *19-Year Real Property For Which an Optional 45-Year Straight Line Method is Elected (Assuming Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
7	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
8	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
9	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
10	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
11	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
12	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
13	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
14	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
15	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
16	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
17	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
18	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
19	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
20	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
21	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
22	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
23	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
24	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
25	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
26	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
27	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
28	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
29	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
30	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
31	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
32	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
33	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
34	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
35	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
36	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
37	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
38	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
39	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
40	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
41	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
42	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
43	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
44	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
45	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
46	0.1	0.3	0.4	0.6	0.8	1.0	1.2	1.4	1.6	1.7	1.9	2.1

6. *Low-income Housing (15-Year 200% Declining Balance) (Assuming No Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	13.3	12.2	11.1	10.9	8.9	7.8	6.6	5.6	4.4	3.3	2.2	1.1
2	11.6	11.7	11.9	12.0	12.1	12.3	12.5	12.6	12.7	12.9	11.0	13.2
3	10.0	10.1	10.2	10.4	10.5	10.7	10.8	10.9	11.1	11.2	11.3	11.4
4	8.7	8.8	8.9	9.0	9.1	9.2	9.3	9.5	9.6	9.7	9.8	9.9

6. *Low-income Housing (15-Year 200% Declining Balance) (Assuming No Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
5	7.5	7.6	7.7	7.8	7.9	8.0	8.1	8.2	8.3	8.4	8.5	8.6
6	6.5	6.6	6.7	6.8	6.9	6.9	7.0	7.1	7.2	7.3	7.4	7.4
7	5.7	5.7	5.8	5.9	5.9	6.0	6.1	6.1	6.2	6.3	6.4	6.5
8	4.9	5.0	5.0	5.1	5.2	5.2	5.3	5.3	5.4	5.5	5.5	5.6
9	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.7	4.8	4.8
10	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
11	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
12	4.5	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
13	4.5	4.5	4.6	4.5	4.6	4.6	4.6	4.6	4.6	4.5	4.6	4.6
14	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.6	4.6	4.5	4.5	4.5
15	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5
16	0.0	0.4	0.7	1.1	1.5	1.9	2.3	2.6	3.0	3.4	3.7	4.1

7. *Low-income Housing Used Predominantly Outside the U.S. (35-year 150% Declining Balance) (Assuming No Mid-Month Convention)*

If the Recovery year is:	And the Month in the First Recovery Year the Property is placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	4.2	3.9	3.6	3.2	2.8	2.5	2.1	1.8	1.4	1.1	0.7	0.4
2	4.1	4.1	4.1	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.3	4.3
3	3.9	3.9	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.1	4.1	4.1
4	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.9	3.9	3.9	3.9
5	3.6	3.6	3.6	3.6	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7
6	3.4	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.6	3.6	3.6
7	3.3	3.3	3.3	3.3	3.3	3.4	3.4	3.4	3.4	3.4	3.4	3.4
8	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.3	3.3	3.3	3.3
9	3.0	3.0	3.0	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1
10	2.9	2.9	2.9	2.9	2.9	2.9	3.0	3.0	3.0	3.0	3.0	3.0
11	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.9	2.9
12	2.6	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.8
13	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
14	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
15	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
16	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
17	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
18	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
19	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
20	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
21	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
22	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
23	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
24	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
25	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
26	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
27	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
28	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
29	2.6	2.5	2.5	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
30	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
31	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2. 5	2.5	2.5	2.5

7. *Low-income Housing Used Predominantly Outside the U.S. (35-year 150% Declining Balance) (Assuming No Mid-Month Convention)*

If the Recovery year is:	And the Month in the First Recovery Year the Property is placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
32	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
33	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
34	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
35	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
36	0.0	0.2	0.4	0.6	0.8	1.0	1.3	1.6	1.8	1.9	2.1	2.3

8. *Low-income Housing For Which An Optional 19-Year Straight Line Method is Elected (Assuming No Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	5.3	4.8	4.4	3.9	3.5	3.1	2.6	2.2	1.8	1.3	0.9	0.4
2	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
4	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
5	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
6	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
7	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
8	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
9	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
10	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
11	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
12	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
13	5.2	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
14	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
15	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
16	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
17	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
18	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
19	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
20	0.0	0.4	0.8	1.3	1.7	2.1	2.6	3.0	3.4	3.9	4.3	4.8

9. *Low-income Housing For Which an Optional 35-Year Straight Line Method is Elected (Assuming No Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	2.9	2.6	2.4	2.1	1.9	1.7	1.4	1.2	1.0	0.7	0.5	0.2
2	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
3	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
4	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
5	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
6	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
7	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9

9. *Low-income Housing For Which an Optional 35-Year Straight Line Method is Elected (Assuming No Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is: 1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
8	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
10	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
11	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
12	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
13	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
14	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
15	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
16	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
17	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
18	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
19	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
20	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
21	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
22	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
23	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
24	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
25	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
26	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
27	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
28	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
29	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
30	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
31	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
32	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
33	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
34	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
35	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
36	0.0	0.3	0.5	0.8	1.0	1.2	1.5	1.7	1.9	2.2	2.4	2.7

10. *Low-income Housing For Which an Optional 45-Year Straight Line Method is Elected (Assuming No Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is: 1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	2.3	2.0	1.9	1.7	1.5	1.3	1.2	0.9	0.7	0.6	0.4	0.2
2	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
4	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
5	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
6	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
7	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
8	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
9	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
10	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
11	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
12	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
13	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2

10. *Low-income Housing For Which an Optional 45-Year Straight Line Method is Elected (Assuming No Mid-Month Convention)*

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
14	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
15	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
16	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
17	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
18	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
19	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
20	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
21	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
22	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
23	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
24	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
25	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
26	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
27	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
28	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
29	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
30	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
31	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
32	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
33	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
34	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
35	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
36	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
37	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
38	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
39	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
40	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
41	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
42	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
43	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
43	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
44	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
45	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
46	0.0	0.3	0.4	0.6	0.8	1.0	1.1	1.4	1.6	1.7	1.9	2.1

Part IV. Items of General Interest

Time for Furnishing Statements on Form 8308

Announcement 86-8

This announcement concerns the date by which partnerships must furnish statements on Form 8308 for calendar year 1985 in order to avoid penalties under section 6678(a) of the Internal Revenue Code. The Internal Revenue Service will not impose penalties under that section on partnerships that mail Form 8308 for calendar year 1985 to new and former partners on or before March 14, 1986. Form 8308 is to be used as the statement requiqred under section 6050K(b) of the Code to be furnished to transferor and transferee partners in a sale or exchange of an interest in a partnership that has unrealized receivables or substantially appreciated inventory items. Section 6050K(b) provides that the statements must be furnished on or before January 31 following the calendar year in which the sale or exchange occurred. The penalty for failure to timely furnish Form 8308 is $50 for each form, with a maximum penalty for each partnership of $50,000 for any year.

Temporary regulations under section 6050K were published in the Federal Register on December 23, 1985 (50 Fed. Reg. 52,313). Copies of Form 8308 may be obtained by calling the telephone number listed in the local telephone directory for "Federal Tax Information and Forms" under the heading for the Internal Revenue Service.

Errors in Publication 225

Announcement 86-9

Publication 225, *Farmer's Tax Guide*, contains an error in the Timber discussion on page 39, Chapter 10, third column, last paragraph, and in the related example in the first column, second paragraph, of page 40. The paragraph on page 39 discusses the election to treat the cutting of timber as a sale or exchange in the year the timber is cut. The discussion omits the requirements of section 631(a) that the timber be owned or a contract to cut be held on the first day of the tax year. In addition, the last sentence in the paragraph should end after the words, ". . . the timber is cut . . . ," to avoid implying that an additional holding period is required after the timber is cut.

The example on page 40 describes a taxpayer as having owned standing timber on January 3, 1985. The fair market value of the timber is $40 per MBF (or $4,000) on July 5, 1985. Under section 631(a), the taxpayer is required to have held the timber on the first day of the tax year and for more than 6 months before the timber is cut. The fair market value is determined on the first day of the tax year. The example is corrected by changing both the January 3 and July 5 dates to January 1 and by adding the fact that the standing timber was held for more than 6 months before it was cut.

Publication 225 also contains an error in the basis reduction example in Chapter 11, page 41, first column, fourth paragraph. The example states that the property is sold in 1985 for $10,000. The example should have also stated that the property was held for 8 months. Further, to figure gain on the sale, the basis of the property, as required by section 48(q)(2), must be increased by 50% of the investment credit being recaptured, which is $185. Therefore, when sold, the adjusted basis is $3,173 ($2,988 plus $185). The gain is corrected to $6,827 ($10,000 less $3,173). Of this amount, $5,527 is ordinary income, and $1,300 is section 1231 gain.

Foundations Status of Certain Organizations

Announcement 86-10

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does not indicate that the organiations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundation:

Access To Life, Inc., Boston, MA
African-American Cultural Assn of Sharon, Sharon, MA
Alcove, Auburne, ME
American Friends of Yeshivat Orot Hagalil, Inc., Brooklyn, NY
Ann Tubbs Housing For The Handicapped, Inc., Medina, OH
Artists Orphanage Inc., Allston, MA
Associates For The Performing Arts, Inc., Stamford, CT
Atoms Track Club, Brooklyn, NY
Banish All Tolls—Charitable Fund, Guilford, CT
Bay Shore Irish American Choral Society, The, Bay Shore, NY
Beefalo Research & Development Foundation, Inc., Mineola, NY
Boonslick, Senior Center Site Advisory Board, Boonville, MO
Buffalo Area Engineering Awareness For Minorities, Inc., Amherst, NY
Buffalo Marathon Association, Ltd., Synder, NY
Built on Faith Housing Corporation, Bridgeport, CT
Burlington Area Community Gardens, Inc., Burlington, VT
Burnt Seina, Inc., New York, NY
Catholic Charismamtic Conferences of New England, Inc., Providence, RI
Center For French Colonial Studies, Prairie Du Rocher, IL
Center For Humanistic Change of New Hampshire, Inc., Keene, NH
Center For Integral Medicine, Inc., Brookline, MA
Chelsea Local Development Corp., The, New York, NY
Chesed Yeshva Inc., Brooklyn, NY
Childrens Holistic Institute For Life Development, New York, NY
Childrens Atelier, Inc., New York, NY
Chinese American Cultural Relations Foundation, Kansas City, MO
Christian Life Ministries, Inc., Centerville, MA
Citizens Economic Research Foundation, Boston, MA
Citizens For Responsible Area Growth, Norwich, VT
Co Vis, Incorporated, New York, NY

Coalition of Block Associations and Organizations For The Betterment of East Flatbush North, Inc., Brooklyn, NY
Committee For The Advancement of Puerto Rican Culture, Bronx, NY
Committee to Free New York, Inc., New York, NY
Community Alternatives 2 Inc., Albany, NY
Community Focus on Developmental Disabilities Inc., Joplin, MO
Concept Universal Choreo-Theatre Ensemble, Inc., New York, NY
Concilio De Madres Hispanas De Worcester, Inc., Worcester, MA
Connecticut Cleft Lip and Palate Parents Group Inc., Cromwell, CT
Connecticut Jazz Dance Company, Inc., Torrington, CT
Connecticut Wildlife Federation Endowment, Inc., Middletown, CT
David Howard Foundation, The, New York, NY
Durruti Institute Inc., Northampton, MA
East Hampton Flotilla 18-2 Inc., East Hampton, NY
Education and Science Society, Inc., New York, NY
Fab Foundation Inc., The, Jefferson City, MO
Fall River Committee to Employ The Handicapped Inc., The, Fall River, MA
Family Mediation Service, Inc., Greenwich, CT
Family Practice Associates of Monona, Monona, IA
Fordham Club of Central New York, The, Syracuse, NY
Frank Lyons Community Association, Inc., Bronx, NY
Free Zone Production Company, Inc., Chilmark, MA
Friends of Senior Citizens of Westport Mass, Inc., Westport, MA
Friends of The Baldwin Outdoor Educational Center, Guilford, CT
Friends of The Noank-Mystic Community Band, Noank, CT
Genesee Region Family Counseling Service, Batavia, NY
Gospel Jamboree Family International, Inc., East Weymouth, MA
Greater Bourne Development Corp., Buzzards Bay, MA
Greek American Center Research Studies Inc., Long Island City, NY
Harlem Council For The Church and Community Change, Inc., New York, NY
Harlem S. Ark of Freedom, Inc., New York, NY
Hartfield Emergency Medical Technicians Association, Hatfield, MA
Health Care Research Foundation, Inc., Albany, NY
Hellgate Management Corp., New York, NY
Help Inc., Brooklyn, NY
Help Me A Respite House For The Physically Handicapped, Spring Valley, NY
Help The Zoo of Watertown New York, Inc., Watertown, NY
Heritage Institute of Ellis Island, Inc., New York, NY
Himalayan Institute of Buffalo, Inc., Buffalo, NY
Hispanic Association of Health Services Executives, Inc., New York, NY
Hope House, Inc., Bangor, ME
Institute For Humanistic Studies, Edwardsville, IL
Institute For The Development of Youth Programs, Inc., New York, NY
Interactive Education Foundation, Inc., Stony Brook, NY
International Center For Integral Education, Inc., Cambridge, MA
International Oil Working Group, Inc., New York, NY
Issues Management Association, Inc., Stamford, CT
Justice Project Inc., The, Springfield, MA
Kingdoms Kitchen, Inc., The, Malden, MA
Liberty Media Services Corp., New York, NY
Little Community Theatre, Inc., The, New York, NY
Long Island Institute of Natural History, Inc., Central Islip, NY
Long Island Tomahawks, Inc., Queens Village, NY
Madison Foundation, Inc., Madison, CT
Mainstream Ministries, Inc., Vernon, CT
Manhattan East Development Corporation, New York, NY
Mass Bay Road Club, Inc., Plymouth, MA
Masstars Team Fund, Inc., Waltham, MA
Medical Network For Lebanon Relief, Inc., Cambridge, MA
Metro Dance Theatre, Waterloo, IA
Michigan Sesquicentennial Foundation, Lansing, MI
Mithstry Dance Ensemble Foundation, Pittsfield, MA
Modern Jewish Studies, Inc., Hanover, NH
Myriad Association Inc., Brooklyn, NY
Nassau-Suffolk Association of Black Social Workers Karen T. Lacy Memorial Scholarship Fund, Inc., Hempstead, NY
National Minority Education Foundation Inc., Albany NY
New Alternatives For Children, Inc., New York, NY
New Bedford Olympic Hopefuls, Inc., New Bedford, MA
New England Appropriate Technologies, Inc., Bolton, MA
New England Jazz Society, The, Ridgefield, CT
North Country Arts Center Inc., Glen Falls, NY
North Country Development Corporation Harvard, MA
North Shore Preservation Society, New York, NY
North Utica Senior Citizens Recreation Center, Inc., Utica, NY
Odaat, Inc., West Haven, CT
Opera Camerata, Inc., New York, NY
Pandora Educational Film Center, Inc., New York, NY
Paras Jewish Organization, Ltd., Rego Park, NY
Paws In Manhattan, Inc., New York, NY
Penobscot Bay Medical Associates, Rockland, ME
Philip Caggiano Enterprises Limited, New York, NY
Pickering Volunteer Fire Dept, Pickering, MO
Planned Pethood, Inc., Toledo, OH
Portsmouth Aquatic Club, Portsmouth, NH
Portsmouth Automobile Dealers Association Combined Charities Trust, Portsmouth, NH
Private Theatre Corp., The, New York, NY
Provincetown Theater Company, Inc., Provincetown, MA
Public Association of Library Supporters, Inc., Durham CT
Ra Yash-Shiya Inc., Boston, MA

Randy Sheridan Ministries Inc., Neosho, MO
Rhode Island Jazz Society, Providence, RI
Rhode Island Radio Information Service, Cranston, RI
Rochester Genesee Valley Club of the National Association of Negro Business and Professional, Rochester, NY
Rochester Magnet Schools Foundation, Inc., Rochester, NY
Rodney C. Norris Memorial Scholarship Fund, Mattapoisett, MA
Rotary East Foundation Inc., St. Joseph, MO
Run-Aways of Putnam, Inc., Carmel, NY
St. Jerome Hospital Foundation Inc., Batavia, NY
St. Mary of the Plains Hospital Foundation, Lubbock, TX
Smugglers Notch Foundation For Computer Use, Inc., Smugglers Notch, VT
Somali Refugee Relief Fund, Inc., Boston, MA
Special Housing and Development Fund Company, Inc., New York, NY
Springfield Tennis Club, Inc., Springfield, MA
Staten Island Pipers, Inc., Staten Island, NY
Surry Historical Society, Surry, ME
Tabitha, Inc., Rochester, NY
Tamchin D. Oraiso Inc., Supporters of Torah, Brooklyn, NY
Teatro Guatro, Inc., New York, NY
Tofr Foundation, Inc., Garden City, NY
Transamerican Medical and Educational Foundation, Inc., New York, NY
Unity Through Creativity Production Co., Inc., Boston, MA
University of New Haven Pilots Association Inc., West Haven, CT
Urbis Community Development Corp., New York, NY
Vale Chamber Orchestra, Inc., Weston, MA
Van Courtlandt Village Civilian Patrol, Inc., Bronx, NY
Vanguard, Inc., Waterbury, VT
Vermont Reperatory Theatre Co., The, Peacham, VT
Vietnam Veterans Leadership Program of The Niagre Frontier, Inc., Buffalo, NY
Viking Ship Society Ltd., Boston, MA
Waterbury Crime Stoppers, Inc., Waterbury, CT
Watertown Lyric Theater Productions, Inc., Watertown, NY
Westchester Youth Jazz Ensemble, Katonak, NY
Windsor Arts Council, Inc., Windsor, CT
Woburn High School Academic Awards Association, Inc., Woburn, MA
Yeshivat Avi-Haezri, Inc., Brooklyn, NY

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

The following organizations, which have been treated as private operating foundations described in section 4942 (j)(3) of the Code, are now been classified as organizations that are not private operating foundations. Grantors and contributors may no longer rely upon rulings or determinations that these organizations are private operating foundations. The organizations are:

Foundation For Advanced Medical Display Technology, Torrance, CA
Grocery Basket, Inc., Kahului, HI
Institute for Christian Values, Inc., El Segundo, CA
Maui Missionary Ministries, Kahului, HI
Monavista, Inc., Los Angeles, CA

Correction to Publication 505

Announcement 86-11

Publication 505, *Tax Withholding and Estimated Tax* (Revised November 1985), contains incorrect dollar amounts on the filled-in Form 2210, *Underpayment of Estimated Tax by Individuals*, illustrated on page 20. The incorrect amounts are in columns (c) and (d) of lines 17, 18, 20b, 20c, and 21. The correct amounts are as follows:

	Column	
	(c)	(d)
Line 17	705	597
Line 18	324	432
Line 20b	10.45	
Line 20c	1.33	10.65
Line 21		29

Revision of Schedule T (Form 5300), Supplemental Application for Approval of Employee Benefit Plans Under TEFRA, TRA84, and REA

Announcement 86-12

Schedule T (Form 5300), Supplemental Application for Approval of Employee Benefit Plans Under TEFRA, TRA 84, and REA, has been updated. The Schedule T, which is used by most applicants who file determination requests on Forms 5300, 5301, 5303, 5307, and 6406, was revised to comply with the requirements of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), the Tax Reform Act of 1984 (TRA 84), and the Retirement Equity Act of 1984 (REA).

Revision of Form 5498, Individual Retirement Arrangement Information

Announcement 86-13

Form 5498, Individual Retirement Arrangement Information, has been revised for 1986 and are now available at Internal Revenue Service offices.

On the revised form, contributions to a simplified employee pension (SEP) made in 1986 and through April 15, 1987, must be reported separately in Box 1, which has been retitled "Regular SEP contributions made in 1986 and 1987 for 1986." Contributions to an individual retirement arrangement (IRA) and to an employer plan that accepts deductible voluntary employee contributions (DECs) are reportable in Box 2, which has been retitled "Regular IRA or DEC contributions made in 1986 and 1987 for 1986."

Residential Rental Property—Public Hearing

Announcement 86-15[1]

SUMMARY: This document provides a notice of public hearing on proposed regulations relating to tax exempt status of industrial development bonds.

DATES: The public hearing will be held on Monday February 10, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Monday, January 27, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, ATTN: CC:LR:T (LR-269-84), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: B. Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935 (not a toll free call).

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under section 103(b) of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Thursday, November 7, 1985 (50 FR 46303) [LR-269-84, 1985-50 I.R.B. 17].

The rules of § 601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations, should submit, not later than Monday, January 27, 1986, an outline of the oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions, attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

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[1] Filed by the Office of the Federal Register on January 10, 1986, 8:45 a.m. and published in the issue of the Federal Register for January 13, 1986, 51 F.R. 1392.

Residential Energy Credit—Public Hearing

Announcement 86-16[1]

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to the residential energy credit.

DATES: The public hearing will be held on February 14, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by January 31, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W. Washington, D.C. The request to speak and outlines or oral comments should be submitted to the Commissioner of Internal Revenue, Attn: CC:LR:: (LR-73-80), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: B. Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, 202-566-3935, not a toll-free call.

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations which amend the Income Tax Regulations under section 23 of the Internal Revenue Code of 1954. The proposed regulations appeared in the Federal Register for Thursday, October 31, 1985 (50 FR 45423).

The rules of § 601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations, should submit, not later than Friday, January 31, 1986, an outline of the oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions, attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

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[1] Filed by the Office of the Federal Register on January 15, 1986, 2:47 p.m., and published in the issue of the Federal Register for January 17, 1986, 51 F.R. 2524.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Philip G. Arneson	Sparta, WI	Attorney	Indefinite from December 15, 1985
Joseph P. Day	Woburn, MA	Attorney	Indefinite from December 24, 1985
Kenneth H. Dillard	Nashville, TN	Certified Public Accountant	Indefinite from December 31, 1985
LeRoy Hodge	Hamilton, NY	Attorney	Indefinite from December 10, 1985
Frank S. Lukuch	Barberton, OH	Certified Public Accountant	Indefinite from December 4, 1985
W. Stephen McConnell	Tampa, FL	Certified Public Accountant	Indefinite from December 26, 1985
Nathan Rich	Wilmington, DE	Certified Public Accountant	Indefinite from December 1, 1985
Walter E. Shettlemore	Long Beach, MS	Certified Public Accountant	Indefinite from December 20, 1985

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.61-2T, removed; new 1.61-2T, added; 1.132-1T, removed; new 1.1.32-1T, added; 1.132-2T through 1.132-8T, added; 1.162-25T, 1.274-5T, 1.274-6T, amended.	Taxation of fringe benefits and exclusions from gross income of certain fringe benefits	1986-3 I.R.B. 40	Feb. 21, 1986
26 CFR 1.43-3(e), revised 1.47-1, 1.48-9, 1.167(a)-11, amended	Recapture of investment credit for mass assets	1986-4 I.R.B. 42	Feb. 18, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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Key to Abbreviations

RR	Revenue Ruling
RP	Revenue Procedure
TD	Treasury Decision
CD	Court Decision
PL	Public Law
EO	Executive Order
DO	Delegation Order
TDO	Treasury Department Order
TC	Tax Convention
SPR	State of Procedural Rules
PTE	Prohibited Transaction Exemption

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1986-6

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

SPECIAL ANNOUNCEMENT

Announcement 86-18, page 56.

A public hearing will be held on March 4, 1986, on proposed regulations relating to the substantiation requirements with respect to listed property and the limitations on the investment credit and deductions applicable to lessees of passenger automobiles.

INCOME TAX

Rev. Rul. 86-15, page 4.

Investment credit; definition of building and structural components. Certain natural gas pipeline compressor station structures are not section 38 property for purposes of the investment tax credit. Rev. Rul. 66-215 distinguished.

Rev. Rul. 86-17, page 26.

Forgone interest determination. For purposes of section 7872(e)(2) of the Code, the applicable rate for purposes of determining "foregone interest" on certain below-market loans outstanding from January 1, 1985 to December 31, 1985 is 9.24 percent.

T.D. 8067, page 5.

LR-121-85, page 55.

Amendments to the regulations under section 451 of the Code relate to accounting for long-term contracts. Proposed amendments clarify how certain rules apply in the case of certain corporations that file consolidated returns with a contractor.

LR-214-82, page 46.

Proposed amendments to the regulations under sections 3508, 3509, and 6041A of the Code relate to the treatment of qualified real estate agents and direct sellers as nonemployees, the determination of employer liability for certain employment taxes, and information reporting of direct sales and payments of remuneration for services.

Announcement 86-14, page 56.

This Bulletin contains a list of organizations that no longer quality as organizations contributions to which are deductible under section 170(c)(2) of the Code.

EMPLOYMENT TAX

LR-214-82, page 46.

Proposed amendments to the regulations under sections 3508, 3509, and 6041A of the Code relate to the treatment of qualified real estate agents and direct sellers as nonemployees, the determination of employer liability for certain employment taxes, and information reporting of direct sales and payments of remuneration for services.

EXCISE TAXES

Rev. Rul. 86-16, page 24.

Coal; sale price determination; freeze conditioning additive. In computing the taxable sale price of coal for purposes of the tax imposed by section 4121 of the Code, a charge for the application of a freeze conditioning additive to the coal is includible.

Rev. Rul. 86-18, page 25.

Liability of unregistered manufacturer; sale for further manufacture. When a manufacturer that has not registered pursuant to section 4222(a) of the Code makes a sale for further manufacture pursuant to the tax-free sale provisions under section 4221(a)(1), the manufacturer remains liable for the manufacturers excise tax. The manufacturer's vendee does not become the statutory manufacturer of the article under section 4223(a) and may file for a refund or claim a credit for any tax paid on its resale of the article.

ADMINISTRATIVE

Rev. Proc. 86-7, page 28.

Magnetic tape filing; information returns; windfall profit tax. Requirements and conditions are updated for the filing of annual information returns for windfall profit tax on magnetic tape. Rev. Proc. 84-81 superseded.

Finding Lists begin on page 61.
Announcement of Suspensions on page 58.
Announcement of Notice of Proposed Rulemaking on page 59.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 48.—Definitions; Special Rules

26 CFR 1.48-1: Definition of section 38 property.

Investment credit; definition of building and structural components. Certain natural gas pipeline compressor station structures are not section 38 property for purposes of the investment tax credit. Rev. Rul. 66-215 distinguished.

Rev. Rul. 86-15

ISSUE

Whether natural gas pipeline compressor station structures described below are section 38 property for investment tax credit purposes.

FACTS

The taxpayer, a natural gas pipeline transmission company, constructed compressor station structures that house compressor station machinery, equipment and fixtures for natural gas pipelines. The structures house compressors and engines; auxiliary service machinery; natural gas metering and pressure regulating equipment; telemetering, communication, and calorimetric devices; and other laboratory equipment. Following industry practice, each structure encloses multiple compressor/engine units and can be extended to accommodate additional units. Each structure consists of removable side panels mounted on a steel framework supporting a single roof. Removal of the side panels near a compressor/engine unit permits removal of the unit without affecting the remainder of the structure. The steel framework also supports a craneway for use in moving equipment and in maintenance. No partitions or other separations are placed between the compressor/engine units. In addition to enclosing the compressor/engine units, instrumentation, controls, piping, and other required equipment, the structure provides working space to permit repositioning of the equipment, if necessary, and a 24-hour schedule of operation, maintenance, overhaul and repair.

LAW AND ANALYSIS

Section 38 of the Internal Revenue Code allows a credit against federal income tax for qualified investment in section 38 property. Section 38 property, as defined in section 48(a)(1), includes (A) tangible personal property, and (B) other tangible property (not including buildings and their structural components) only if used as an integral part of certain activities. Section 38 property must be recovery property or depreciable property having a useful life of 3 years or more. Section 1.48-1(c) of the Income Tax Regulations provides that the term "tangible personal property" means any tangible property except land and improvements thereto, such as buildings or other inherently permanent structures (including items which are structural components of such buildings or structures).

Section 1.48-1(e)(1) of the regulations provides that the term "building" generally means any structure or edifice enclosing a space within its walls, and usually covered by a roof, the purpose of which is, for example, to provide shelter, working, office, parking, display or sales space. It does not include (i) a structure that is essentially an item of machinery or equipment, or (ii) a structure that houses property used as an integral part of any of the activities specified in section 48(a)(1)(B)(i) of the Code (which include furnishing gas) if the use of the structure is so closely related to the use of such property that the structure clearly can be expected to be replaced when the property it initially houses is replaced. Factors which indicate that a structure is closely related to the use of the property it houses include the fact that the structure is specifically designed to provide for the stress and other demands of such property and the fact that the structure could not be economically used for other purposes.

The structures described above enclose a space within their walls and are covered by a roof. They provide shelter and sufficient working space to permit repositioning of the equipment, if necessary, and a 24-hour schedule of operation, maintenance, overhaul, and repair. The structures are erected separately from the engines and are independent to a degree that permits the removal and relocation of a compressor/engine unit or units without damage to the structures. The structures are not essentially items of machinery or equipment. Even though they house machinery and equipment used as an integral part of the furnishing of gas, these structures are not so closely related to this machinery and equipment that they meet the definition of section 1.48-1(e)(1)(ii) as an exception to the term "building". In this regard, the Fourth Circuit, in *Monk & Co., Inc. v. United States*, 686 F.2d 1058 (4th Cir. 1982), stated the following:

> . . . a structure housing machinery, in order not to be considered part of a building, must be "*so closely* related to the use (of the machinery) that the structure *clearly* can be expected to be replaced when (the machinery) is replaced." (Emphasis added.) The import is that the taxpayer has the distinct burden of showing the structure has no feasible alternate use than housing the specific machinery it currently houses.

The structures in the present case resemble standard buildings used by other industries to house equipment. They can be expanded as necessary to house additional units and units can be removed without affecting the structure. These structures can be used for other purposes and they will not clearly be replaced with the compressor/engine units. Therefore, the structures do not fit the exception contained in section 1.48-1(e)(1)(ii) of the regulations, and they are buildings within the meaning of that section.

In Rev. Rul. 66-215, 1966-2 C.B. 11, an enclosing structure was built around each compressor/engine unit after the unit was placed on a specially designed, reinforced concrete pad. Removal of the compressor/engine unit would require contemporaneous removal of the compressor station structures. The ruling concludes that the described compressor station structures are section 38 property.

Under the facts in Rev. Rul. 66-215, the entire structure houses a single unit and would be replaced contemporaneously with the compressor unit; but here the structure houses the multiple compressor facility and the structure would not be so replaced with replacement of a compressor unit. A single compressor unit could be replaced with a minimum of inconvenience with the building continuing to serve its ongoing functions.

HOLDING

The natural gas pipeline compressor station structures described above are not section 38 property.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 66-215 is distinguished.

Section 446.—General Rule for Methods of Accounting

26 CFR 1.446-1: General rule for methods of accounting.

Accounting for long-term contracts. See T.D. 8067, below.

Section 451.—General Rule for Taxable Year of Inclusion

26 CFR 1.451-3: Long-term contracts.
(Also Sections 446, 471; 1.446-1, 1.471-11.)

T.D. 8067

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART I—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Accounting for Long-term Contracts

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to accounting for long-term contracts. The regulations affect taxpayers who have long-term contracts whether or not they use a long-term contract method of accounting for such contracts. Modifications to the regulations were required to be made by the Tax Equity and Fiscal Responsibility Act of 1982 (Pub. L. 97-248) [1982-2 C.B. 462].

DATES: In general, the regulations relating to the allocation of indirect costs to extended period long-term contracts and the rules relating to the use of inventory methods with a long-term contract method are effective for taxable years beginning after December 31, 1982. The regulations relating to the time at which a contract is to be considered completed and to aggregating and severing agreements are effective for taxable years ending after December 31, 1982.

FOR FURTHER INFORMATION CONTACT: Paulette Chernyshev of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T (202-566-3288, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

On March 14, 1983, proposed amendments to the Income Tax Regulations (26 CFR Part 1) under sections 446, 451 and 471 of the Internal Revenue Code were published in the FEDERAL REGISTER (48 FR 10702) [LR-274-81, 1983-1 C.B. 1021]. The amendments were proposed to conform the regulations to the requirements of section 229 of the Tax Equity and Fiscal Responsibility Act of 1982 (Pub. L. 97-248; 96 Stat. 324, 493) [1982-2 C.B. 462, 506] as amended by section 712(m) of the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 463].

Many written comments were received. A public hearing was held on June 29, 1983. After consideration of all comments and testimony received on the proposed amendments, the amendments, with revisions, are adopted by this Treasury decision. The revisions and public comments are discussed below.

DISCUSSION

CLEAR REFLECTION OF INCOME

Comments received expressed the concern that the introductory language of section 1.451-3(a) changed the standard for the application of the clear reflection of income concept. No change in the standard was contemplated. The Treasury decision retains the reference to clear reflection of income consistent with the provisions of section 1.446-1(a)(2) and (c), which permit various methods of accounting, subject to the requirement that any method, including the long-term contract method, must clearly reflect income in its application.

CLASSIFICATION OF CONTRACTS

Contracts that the taxpayer estimates will be completed within 2 years of the contract commencement date (3 years in the case of a construction contract) are not subject to the extended period costing rules. The proposed regulations provided that contracts that are not completed within that time period will not be reclassified if the taxpayer could reasonably have expected the contract to be completed within the time period. The proposed regulations further provided that the taxpayer's estimated time of completion for classifying and accounting for a long-term contract will not be considered unreasonable if the contract is not completed within the expected time solely because of unforeseeable factors not within the control of the taxpayer. Comments considered this exception too limited, as the exception is only available if the delay in completion was due solely to unforseeable factors. Therefore, the Treasury decision modifies the exception to apply to delays occurring primarily because of unforeseeable factors.

SHIPBUILDING CONTRACTS

Comments submitted by members of the shipbuilding industry expressed concern as to the definition of "construction contracts" in paragraph (b)(3)(ii) of section 1.451-3. Such definition was intended only for purposes of that paragraph (i.e., for determining the applicability of the 3-year exception to the extended period costing rules). Shipbuilding contracts are not "construction contracts" for this purpose, because ships do not constitute real property. Any implication that shipbuilding does not constitute construction for purposes of the general definition of a long-term contract (contained in paragraph (b)(1) of section 1.451-3) has been removed; that issue is beyond the scope of these regulations.

$25 MILLION GROSS RECEIPTS TEST

In determining a taxpayer's gross receipts for purposes of the $25 million test, the proposed regulations required, for persons not under common control with the taxpayer, attribution of gross receipts to the contractor from persons owning an interest in the contractor, and from persons in which the contractor owns an interest, in proportion to the amount owned. If the amount of ownership varies during the year, the proposed regulations required attribution in proportion to the largest amount of this interest owned during such year. Additionally, the proposed regulations required proportionate attribution of gross receipts realized from the conduct of any trade or business. In response to comments, the attribution rules of paragraph (b)(3)(iii)(C) of section 1.451-3 (attribution from persons not under common control with the taxpayer) have been revised in two respects. Interests owned in or by a contractor that vary during the year are to be measured using a weighted average, based on the number of days each interest is owned during such calendar year. In addition, gross receipts attributed to a contractor under this rule are to be limited to gross receipts from the trade or business of construction.

RESEARCH AND EXPERIMENTAL EXPENSES

Several comments objected to the inclusion of research and experimental expenses in the list of indirect costs required to be allocated to non-extended period long-term contracts in the proposed regulations. The comments interpret legislative history to preclude changes in period costs under existing regulations with respect to non-extended period contracts. In response to these comments, research and experimental expenses have been deleted from the list of indirect costs required to be allocated to non-extended period long-term contracts.

BIDDING EXPENSES

The proposed regulations required a "defer-and-deduct" treatment for bidding expenses for unawarded contracts. Comments favored a "deduct-and-recapture" approach. That approach would treat bidding expenses relating to contracts not awarded as of the end of a taxable year as period costs. Bidding expenses for contracts ultimately awarded to the taxpayer would be recaptured in the year in which the contract is awarded. After consideration, this alternative was rejected as inconsistent with the purpose of the new extended period costing rules. The defer-and-deduct rule is retained in the Treasury decision, with additional guidance as to how bidding expenses for unawarded contracts are to be accounted for by the taxpayer.

INVENTORY METHODS

The proposed regulations provided that the taxpayer may not use LIFO or the lower of cost or market method to determine costs attributable to long-term contracts. The primary motivation in taking this position was to prohibit the accounting practice of delaying the determination of the cost of raw materials and components incorporated into the subject matter of the contract until the year of completion, and then using LIFO to determine such costs. It is the firmly-held view of the Internal Revenue Service that costs attributable to a long-term contract should be determined costs is deferred until the year of completion of the contract. To the extent that the holding of *Peninsula Steel Products Co. v. Commissioner*, 78 T.C. 1029 (1982), is inconsistent with this principle, the Service will not follow that case.

Many commentators state that the position of the proposed regulations regarding LIFO is overboard in precluding the use of LIFO in making the required determination of the costs of materials and components at the time of dedication. Because using LIFO to determine costs at dedication is not inconsistent with the primary position that costing must occur in the year of dedication, the Treasury decision provides that the costs of raw materials or components allocable to a long-term contract shall be determined, in the year of dedication, using the taxpayer's method of accounting for each material (*e.g.*,—specific identification, FIFO, LIFO). Guidance is provided as to when raw materials and components are dedicate to a particular long-term contract.

SERVICE COSTS

The proposed regulations provide an insignificant deviation rule for methods used by taxpayers in allocating service costs. Comments suggested that the intent of the rule would be better served if applied to the taxpayer's contracts on an overall basis, rather than contract-by-contract. The Treasury decision reflects this suggestion in providing that the taxpayer's method of allocation will be tested on the basis of the taxpayer's extended period long-term contracts taken as a whole.

Many commentators considered it unreasonable to require a taxpayer to attach a statement to its tax return describing the allocation of service costs and general administrative costs. As a result, paragraph (d)(9)(v) of section 1.451-3 has been revised to require only that such records describing the taxpayer's cost allocations be maintained and made available for examination and verification by the district director.

Among the illustrations of allocation methods, the proposed regulations provided rules for allocating the cost of a department providing engineering and design services "unless the engineering and design services provided to a long-term contract are properly accounted for as a separate contract". Many of the commentators requested clarification concerning the circumstances under which it is appropriate to account for such services as a separate contract. The only purpose of paragraph (d)(9)(x) of section 1.451-3 is to describe how engineering and design department costs not properly accounted for separately may be allocated.

SEVERING AND AGGREGATING

The proposed regulations provided that, in addition to the instances provided in paragraph (e)(1) of this section, there may be other instances in which it may be necessary for the Commissioner to sever or aggregate agreements in order to clearly reflect income. Several commentators objected to this provision on the grounds that it creates uncertainty as to the application of the severing and aggregating rules. This additional reference has been omitted from the Treasury decision.

The Treasury decision provides clarification that, in general, only the Commissioner (and not the taxpayer) may sever or aggregate agreements.

For purposes of severing and aggregating (as well as for all other purposes), fact situations to which this Treasury decision does not apply because of the effective date of this Treasury decision will be tested underTreas. Reg. §1.451-3 as it existed before the promulgation of this Treasury decision. Pursuant to section 229 of TEFRA, this Treasury decision constitutes a clarification of the prior regulations. No inference should be drawn that a fact situation clearly subject to severing or aggregating under this Treasury decision is not subject to severing or aggregating under the prior regulations.

COST ALLOCATION RULES FOR TAXPAYERS USING INVENTORY METHODS

The proposed regulations required an inventory method taxpayer to apply the new cost allocation rules to its extended period long-term contracts. In the preamble, the Commissioner specifically invited comments on whether this requirement should be modified in the case of taxpayers using an inventory method of accounting for extended period long-term contracts under which some threshold amount of the income from such contracts is recognized in taxable years before the taxable year such contracts would be considered completed under the completed contract method. This was in response to footnote 1 in S. Rep. No. 97-494, 97th Cong., 2d Sess. 201 (1982), which provided that "in order to prevent avoidance of the new cost allocation rules, it is anticipated that Treasury may be required to amend both the regulations relating to the completed contract method and the regulations relating to the full absorption inventory costing method." A number of comments were received in this regard. In response to these comments, yet in order to prevent avoidance of the new cost allocation rules, the Treasury decision requires taxpayers who use a method of accounting that uses inventories (other than a long-term contract method) to apply the new cost allocation rules in accounting for all extended period long-term contracts except those as to which the taxpayer reasonably expects to recognize a threshold percentage of gross income in each of the three years following the year in which the contract is entered into.

CONSOLIDATED GROUPS

Amendments to this Treasury decision are proposed to be made in paragraphs 1.451-3(b)(3)(v) and 1.451-3(d)(6)(iv), relating to rules for taxpayers who file as members of consolidated groups. The new rules are proposed elsewhere in this *** [Bulletin].

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required. Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

PAPER REDUCTION ACT OF 1980

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB.

DRAFTING INFORMATION

The principal author of these regulations in the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service, is Paulette Chernyshev. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations, both on matters of substance and style.

* * * * *

Amendments to the regulations

The following amendments to 26 CFR Part 1 are adopted:

Income Tax Regulations
(26 CFR Part 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805 * * * Section 471 also issued under 26 U.S.C. 471. Sections 1.451-3 and 1.451-5 amended under the authority in 96 Stat. 324, 493.

Par. 2. Section 1.446-1(c)(1)(ii) is amended by revising the last sentence and by adding a new sentence at the end to read as follows:

§1.446-1 General rule for methods of accounting.

* * * * *

(c) *Permissible method*—(1) *In general.* * * *

(ii) *Accrual method.* * * * For example, under an accrual method, a taxpayer engaged in manufacturing may account for the sale of an item when the item is shipped, when the item is delivered, when the item is accepted, or when title to the item passes to the purchaser, whether or not billed, depending upon the method regularly employed in keeping the taxpayer's books; however, see §1.451-5 relating to advance payments. The determination of when an item is shipped, delivered or accepted, or when title passes, does not depend upon when any other item in the contract is shipped, delivered or accepted, or when title passes.

* * * * *

Par. 3 Section 1.451-3 is amended as follows:

1. Paragraph (a) is revised;
2. Paragraph (b) is revised
3. Paragraph (d) is amended by revising paragraphs (d)(1) and (5), redesignating paragraph (d)(5)(iv) as paragraph (d)(7), revising and redesignating paragraph (d)(6) as paragraph (d)(8), and by adding new paragraphs (d)(6) and (9);
4. Paragraph (e) is amended by revising paragraph (e)(1), revising examples (1) and (2) of paragraph (e)(2), revising and redesignating example (3) of paragraph (e)(2) as example (4), adding new examples (3), (5), (6) and (7) of paragraph (e)(2), and adding new paragraph (e)(3); and
5. A new paragraph (g) is added.

The revised and added provisions read as follows:

§1.451-3 Long-term contracts.

(a) *Introduction and Effective date*—(1) *In general.*

Income from a long-term contract (as defined in paragraph (b)(1) of this section) may be included in gross income in accordance with one of the two long-term contract methods, namely, the percentage of completion method (as described in paragraph (c) of this section) or the completed contract method (as described in paragraph (d) of this section), or any other method. Whichever method is chosen must, in the opinion of the commissioner, clearly reflect income. See §1.446-1(a)(2) and (c). In addition, it must be applied consistently to all long-term contracts within the same trade or business except that a taxpayer who has long-term contracts of substantial duration and long-term contracts of less than substantial duration in the same trade or business may report the income from all the contracts of substantial duration on the same long-term contract method and report the income from the contracts of less than substantial duration pursuant to another proper method of accounting. For example, if a manufacturer of heavy machinery has special-order contracts of a type that generally take 15 months to complete and also has contracts of a type that generally take 3 months to complete, the manufacturer may use a long-term contract method for the 15-month contracts and a proper inventory method pursuant to section 471 and the regulations thereunder for the 3-month contracts. Similarly, if a construction contractor has construction contracts of a type that generally take 15 calendar months to complete and other construction contracts that take only 5 months to complete but that are long-term contracts because they are not completed in the taxable years in which they are entered into (pursuant to paragraph (b)(1)(i) of this section), such contractor may either use a long-term contract method for all the contracts of both types or use a long-term contract method for the 15-month contracts and another proper method of accounting for the 5-month contracts. If a taxpayer distinguishes between contracts of substantial duration and other long-term contracts of less than substantial duration, he must adhere to a consistently applied standard for determining substantial duration.

(2) *Reporting requirement.* When a taxpayer reports income under the percentage of completion method or the completed contract method, a statement to that effect shall be attached to his income tax return.

(3) *Allocation among activities required.* The percentage of completion method and the completed contract method apply only to the accounting for income and expenses attributable to long-term contracts. The term "expenses attributable to long term contracts" means all direct labor costs and direct material costs (within the meaning of paragraph (d)(5)(i) or (6)(i) of this section), and all direct costs except those described in paragraph (d)(5)(iii) or, in the case of extended period long-term contracts, paragraph (d)(6)(iii). Other income and expense items, such as investment income, expenses not attributable to such contracts, and costs incurred with respect to any guarantee, warranty, maintenance, or other service agreement relating to the subject matter of such contracts, shall be accounted for under a proper method of accounting. See section 446(c) and § 1.446-1(c).

(4) *Severing and aggregating contracts.* In the case of income attributable to a long-term contract, whether or not a long-term contract method is used, for the purpose of clearly reflecting income, it may be necessary in some instances for the Commissioner either to treat one agreement as several contracts or to treat several agreements as one contract. The rules of paragraph (e)(1) of this section shall apply to determine whether an agreement should be so severed or several agreements so aggregated.

(5) *Certain taxpayers not using a long-term contract method.* In the case of a taxpayer using a method of accounting that uses inventories (other than a long-term contract method) for any extended period long-term contract entered into after December 31, 1982, see paragraphs (d)(6)(v) and (g) of this section.

(6) *Use of inventory methods in connection with the long-term contract method.* Effective for taxable years beginning after December 31, 1982, the taxpayer may use an inventory method to determine the costs attributable to a long-term contract accounted for under a long term contract method only in accordance with paragraph (d)(8) of this section.

(7) *Effective date.* Except as otherwise provided, this section is effective for taxable years ending after December 31, 1982. For taxable years ending before January 1, 1983, see CFR §1.451-3, revised as of 4/1/85.

(b) *Definitions, and special rules relating to certain contracts*—(1) *Long-term contract*—(i) *In general.* Except as provided in paragraph (b)(1)(ii) of this section, the term "long-term contract" means a building, installation, construction or manufacturing contract which is not completed within the taxable year in which it is entered into.

(ii) *Manufacturing contracts.* Notwithstanding paragraph (b)(1)(i) of this section, a manufacturing contract is a "long-term contract" only if such contract involves the manufacture of (A) unique items of a type which is not normally carried in the finished goods inventory of the taxpayer, or (B) items which normally require more than 12 calendar months to complete (regardless of the duration of the actual contract). Thus, for example, a contract to manufacture a unit of industrial machinery specifically designed for the needs of a customer and not normally carried in the taxpayer's inventory or a contract to manufacture machinery which will require more than 12 calendar months to complete are long-term contracts[.] However, a contract to manufacture 15,000 folding chairs which take 3 days each to manufacture is not a long-term contract even though it takes more than 12 calendar months to manufacture all 15,000 chairs and the contract is not completed within the taxable year it is entered into.

(2) *Completion*—(i) *Final completion and acceptance*—(A) *General rule.* Except as otherwise provided in this paragraph (b)(2), and in paragraph (d)(2), (3), and (4) of this section (relating to disputes), a long-term contract shall not be considered "completed" until final completion and acceptance have occurred. Nevertheless, a taxpayer may not delay the completion of a contract for the principal purpose of deferring Federal income tax.

(B) *Completion determined on basis of all facts and circumstances.* Final completion and acceptance of a contract for Federal income tax purposes is determined from an analysis of all the relevant facts and circumstances, including the manner in which the parties to the contract deal with each other and with the subject matter of the contract, the physical condition and state of readiness of the subject matter of the contract, and the nature of any work or costs remaining to be performed or incurred on the contract. In considering the manner in which the parties deal with the subject matter of the contract, any use of the primary subject matter of the contract by the purchaser (except for testing purposes that produce no gross revenue, cost savings, or other substantial benefits for the purchaser) will be considered.

(C) *Examples.* The principles of paragraph (b)(2)(i) of this section are illustrated by the following examples:

Example (1). In 1982, A, a calendar year contractor, contracts with B to construct a building. The initial completion date specified in the contract is October 1984. In November 1984, the building is completed in every respect necessary for the use for which the building is intended. Later in November 1984, B occupies the building and notifies A that certain minor deficiencies should be corrected. A agrees to correct the deficiencies. Under these circumstances, the contract is considered completed for Federal income tax purposes in A's taxable year ending December 31, 1984, without regard to when A corrects the deficiencies. The contract is considered completed because the parties have dealt with each other and with the subject matter of the contract in a manner that indicates that final completion and acceptance have occurred.

Example (2). Assume the same facts as in example 1, except that there are no deficiencies in the building that require correction or repair. In addition, assume that the contract between A and B provides that none of the retainage under the contract may be released to A until A obtains an architect's certificate that the building has been completed according to the specifications of the contract. A obtains this certificate in February, 1985. Under these circumstances, the contract is considered completed for Federal income tax purposes in A's taxable year ending December 31, 1984, with regard to when A obtains the required architect's certificate, and without regard to when the retainage is released to A, because the parties have dealt with each other and with the subject matter of the contract in a manner that indicates that final completion and acceptance have occurred.

Example (3) In 1982, X, a calendar year taxpayer who manufactures industrial machinery, contracts with F to build and install one large item of industrial machinery to be delivered in August 1983 and to be installed and tested by X in F's factory. The contract provides that the machinery will be accepted by F when the tests performed by X demonstrate that the machinery will perform within certain environmental standards required by a government agency, regardless of whether an operating permit has been obtained. Because of technical problems the machinery is not ready for delivery until December 1983. F accepts delivery of the machinery in December 1983 subject to installation and testing to determine if the assembled machinery meets the environmental standards. The machinery is installed and tested during December 1983 through February 1984, and F accepts the machinery in February 1984. An operating permit required to operate the machinery under the environmental standards is issued by the governmental agency in February, 1985. Under these circumstances final completion and acceptance of the machinery for Federal income tax purposes occurs in February, 1984.

Example (4). In 1983, D, a calendar year taxpayer, contracts with E to construct a shopping center and related parking areas. The shopping center is completed in October 1985. In December 1985, the shopping center and three-fourths of the parking area are opened to the general public. At that time, the entire parking area of the shopping center has been graded and three-fourths has been paved, but the final asphalt coating has not been laid due to general weather conditions. Under these circumstances, the contract to construct the shopping center and parking area is considered completed for Federal income tax purposes in December 1985, because the shopping center and a major portion of the parking area were ready to be used and were used at that time.

(ii) *Contracts with more than one subject matter*—(A) *General rule.* In the case of a long-term contract (which, after the application of the rules provided in paragraph (e) of this section, is treated as a single long-term contract for Federal income tax purposes) for one or more units (such as an aircraft or an item of industrial machinery) that represent the primary subject matter of the contract, and for other items (such as training manuals, or spare or replacement parts or components) that do not represent the primary subject matter of the contract, "final completion and acceptance" shall be determined without regard to the contractor's obligation to supply the other items that do not represent the primary subject matter of the contract. If at the end of the taxable year in which the long-term contract is completed there remain any other items that do not represent the primary subject matter of the contract and that have not been finally completed and accepted then the costs that have been incurred prior to the end of such year and that are properly allocable to such other items (determined pursuant to paragraph (d)(5) or (6) (as the case may be) of this section), and a portion of the gross contract price (if any) reasonably allocable to such other items shall be separated from the long-term contract, and such costs and such portion of the gross contract price shall be accounted for under a proper method of accounting. Such proper method of accounting includes a long-term contract method only if a separate contract for such other items would be a long-term contract (as defined in paragraph (b)(1) of this section).

(B) *Example.* The principles of paragraph (b)(2)(ii)(A) of this section may be illustrated by the following example:

Example. In 1982, X contracts with the Y Government to manufacture five aircraft and to manufacture 12 spare and replacements parts for the five aircraft and for certain other aircraft supplied to Y under prior contracts. Assume that under all the facts and circumstances it is determined that the portion of the contract relating to the 12 spare and replacement parts does not have to be severed from the portion of the contract relating to the five aircraft. Assume also that under all the facts and circumstances it is determined that the five aircraft represent the primary subject matter of the contract, and that the spare and replacement parts do not represent the primary subject matter of the contract. In 1984, X tenders the five aircraft and seven of the spare and replacement parts to Y. Y accepts the aircraft and the parts subject to X's delivery of the balance of the spare and replacement parts. For Federal income tax purposes the contract is deemed to have been completed in 1984. Accordingly, X must include in gross income in 1984 the entire contract price, less the portion of the gross contract price reasonably allocable (if any) to the parts not delivered in 1984. X must deduct from gross income in 1984 the entire costs properly allocable to the contract, less the entire costs incurred that are properly allocable to the parts not delivered in 1984. X will account for the income and costs allocable to the parts not delivered in 1984 under a proper method of accounting.

(iii) *Contingent compensation.* In the case of a long-term contract, "final completion and acceptance" shall be determined without regard to any term of the contract providing for additional compensation contingent upon the continued successful performance of the subject matter of the contract after the subject matter of the contract has been accepted by the purchaser (such as an incentive fee payable if a satellite remains in operation after it is placed on orbit). Such contingent compensation shall be included in gross income in the appropriate taxable year determined under the taxpayer's method of accounting other than a long-term contract method.

(iv) *Certain supervision of installation.* In the case of a long-term contract, "final completion and acceptance" shall be determined without regard to any obligation on the part of the contractor to assist or to supervise installation or assembly of the subject matter of the contract where such installation or assembly is to be performed by the purchaser and, under applicable contract law, the subject matter of the contract may be accepted by the purchaser prior to such installation or assembly. If the preceding sentence applies to a contract, "final completion and acceptance" shall be determined without regard to such obligation [.] In addition, the entire gross contract price less the portion of the gross contract price (if any) reasonably allocable to such obligation, shall be included in gross income in the taxable year in which the contract is completed [.] Further, all costs properly allocable to the contract and which have been incurred prior to the end of the taxable year in which such contract is completed shall be deducted in such year [.] Finally, all other costs properly allocable to such contract and the portion of the gross contract price reasonably allocable to the obligation to assist or to supervise installation shall be accounted for under a proper method of accounting other than a long-term contract method.

(v) *Subcontractors*. In the case of a subcontractor who completes work on a long-term contract prior to the completion of the entire contract, "final completion and acceptance" of the contract with respect to such subcontractor shall be deemed to have occurred when the subcontractor's work has been completed and has been accepted by the party with whom the subcontractor has contracted.

(vi) *Disputes*. Completion of a long-term contract is determined without regard to whether a dispute exists at the time the taxpayer tenders the subject matter of the contract to the party with whom the taxpayer has contracted. See paragraph (d)(2), (3) and (4) of this section.

(3) *Extended period long-term contract*—(i) *General Rule*. This paragraph (b)(3) does not apply to contracts accounted for under the percentage of completion method. Except as provided in paragraph (b)(3)(ii) of this section, the term "extended period long-term contract" means any long-term contract that the taxpayer estimates (at the time such contract is entered into) will not be completed (as defined in paragraph (b)(2) of this section) within the 2-year period beginning on the first date (hereinafter, "the contract commencement date") that the taxpayer incurs any costs (other than costs such as bidding expenses, or expenses incurred in connection with negotiating the contract) allocable to such contract (under the cost allocation rules of paragraph (d)(6) of this section). The preceding sentence shall be applied without regard to when costs allocable to a contract are recorded under the cost accounting procedures used by the taxpayer. In general, the contract commencement date will be the first date that any of the following activities occur; the taxpayer incurs design or engineering costs allocable to the contract other than design or engineering costs incurred solely for purposes of bidding for the contract; materials or equipment are shipped to the jobsite; or workers whose labor cost is treated as direct labor are sent to the jobsite. If the first date when any costs allocable to a contract are incurred is not determinable, the contract commencement date of a contract shall be the date such contract is entered into, unless the taxpayer establishes to the satisfaction of the district director that another date is a more appropriate contract commencement date. The contract commencement date shall not be earlier than the date the contract is entered into, unless the taxpayer delayed entering into the contract for a principal purpose of ávoiding the rules of this section.

(ii) *Certain construction contracts*. The term "extended period long-term contract" does not include any construction contract entered into by a taxpayer—

(A) Who estimates (at the time such contract is entered into) that such contract will be completed within the 3-year period beginning on the contract commencement date of such contract, or

(B) Whose average annual gross receipts (determined under paragraph (b)(3)(iii) of this section) over the 3 taxable years preceding the taxable year the contract is entered into (or, if less, the number of preceding taxable years the taxpayer has been in existence) do not exceed $25 million.

For purposes of this paragraph (b)(3)(ii), the term "construction contract" means any contract for the building, construction, or erection of, or the installation of any integral component to, improvements to real property. For purposes of the preceding sentence, construction includes reconstruction and rehabilitation. An improvement to real property includes buildings or other structures intended to be permanently affixed to real property, roadways, dams, or bridges, but does not include such items as vessels or offshore drilling platforms. An integral component to an improvement to real property includes property not produced at the site of the real property but intended to be permanently affixed to an improvement to real property, for example, elevators and central heating and cooling systems. In the case of a contract that provides for the manufacture and the installation of an integral component to an improvement to real property (such as the pollution control equipment for a power plant), only the part of the overall gross contract price and the costs properly allocable to the work of installing the finished component is a construction contract. For example, in the case of a contract both to manufacture and to install an elevator in an office building, only the portion of the gross contract price and only the costs properly allocable to installing the elevator is a construction contract. However, in determining whether the installation portion of a contract is expected to be completed within three years, the time expected to complete both the manufacture and the installation of the contract subject matter must be taken into account. Similarly, in determining whether the manufacturing portion of a contract is expected to be completed within two years, the time expected to complete both the manufacture and the installation of the contract subject matter must be taken into account. Alternatively, the taxpayer may consistently account for the manufacturing portion and the installation portion of all such agreements as separate contracts if there is an appropriate allocation of the gross contract price between the manufacturing portion and the installation portion of the agreement.

The preceding sentence applies without regard to paragraph (e)(1) of this section.

(iii) *Determination of gross receipts*—(A) *Aggregation and attribution of gross receipts*. The following rules shall apply in determining the gross receipts of the taxpayer for purposes of paragraph (b)(3)(ii)(B) of this section, that is, for determining if the average annual gross receipts of the taxpayer over the 3 taxable years preceding the taxable year in which a construction contract is entered into (or, if less, the number of preceding taxable years the taxpayer been in existence) exceed $25 million. Under paragraph (b)(3)(iii)(B) of this section, the average annual gross receipts of all trades or businesses (regardless of the nature of such trades or businesses) under common control with the taxpayer who enters into the construction contract are combined. Under paragraph (b)(3)(iii)(C), a portion of the average annual gross receipts from building, installation or construction contracts (hereinafter "construction gross receipts") of trades or businesses not under common control with the taxpayer who enters into the contract, but which are related to the taxpayer through a chain of attribution (using indirect and constructive ownership), are attributed to the taxpayer who enters into the contract. Except as provided in paragraph (b)(3)(iii)(C)*(4)(i)*, the rules of paragraph (b)(3)(iii)(B) and (C) are both applied. For purposes of paragraph (b)(3) of this section, "gross receipts" include the gross receipts realized from the active conduct of any trade or business, (*e.g.*, —sales revenue), and shall be the gross receipts of the taxable year in which such receipts are recognized properly under the tax accounting method of the taxpayer. For this purpose "gross receipts" shall not include amounts that, under Federal income tax law, are interest, dividends, rents, royalties, annuities or the amount realized from the sale or exchange of property used in the trade or business or held for the production of income. Gross receipts of a contract includes the gross contract price (whether the contract is a general contract or a subcontract, and whether or not the contract is a long-term contract). If the taxpayer enters into a contract which provides that any direct materials (as described in paragraph (d)(5)(i) of this section) will be supplied by the party for whom the contract is being performed (and thus the cost of which is not represented in the gross contract price), gross receipts do not include the cost of such direct materials unless the contractual arrangement was entered into for a principal purpose of reducing the contractor's gross receipts.

(B) *Aggregation of all gross receipts of trades or businesses under common control*. If, at any time during the calendar year in which the taxpayer enters into a construction contract, such taxpayer and any other trades or businesses (whether or not incorporated) are under common control, then the average annual gross receipts of each such trade or business (for the 3 taxable years of such trade or business preceding the taxable year of such trade or business in which the construction contract is entered into or, if less, the number of preceding taxable years such trade or business has been in existence) shall be combined with the average annual gross receipts of the taxpayer for taxpayer's 3 taxable years preceding the taxable year of the taxpayer in which the construction contract is entered into (or, if less, the number of preceding taxable years the taxpayer has been in existence). Gross receipts attributable to transactions between trades or businesses under common control shall be eliminated. For purposes of paragraph (b)(3) of this section, the term "trades or businesses under common control" means any group of trades or businesses that is either—

(1) A "parent-subsidiary group under common control" as defined in § 1.52-1(c).

(2) A "brother-sister group under common control" as defined in § 1.52-1(d), or

(3) A "combined group under common control" as defined in § 1.52-1(e).

(C) *Attribution of construction gross receipts to or from individuals, proprietorships, corporations, partnerships, trusts and estates not under common control—(1) Attribution of construction gross receipts to the contractor from persons owning an interest in the contractor*. For purposes of paragraph (b)(3) of this section, if a 5 percent or greater interest in the person who enters into a construction contract (hereinafter, "the contractor") is owned (at any time during the calendar year in which the construction contract is entered into), directly, or indirectly through the application of this paragraph (b)(3)(iii)(C), by or for any person, the average annual gross receipts of the contractor for the contractor's 3 taxable years preceding the taxable year of the contractor in which the contract was entered into (or, if less, the number of preceding taxable years the contractor has been in existence) shall include the average annual construction gross receipts of such person (for the 3 taxable years of such person preceding the taxable year of such person in which the contract was entered into or, if less, the number of preceding taxable years in which such person has been in existence) in proportion to the interest of such person in the contractor. If an interest is not owned for the entire calendar year, or if an interest varies during the calendar year, the amount of such interest for such year shall be the weighted average based on the number of days each interest is owned during such calendar year.

(2) *Attribution of construction gross receipts to the contractor from persons in which the contractor owns an interest*. For purposes of paragraph (b)(3) of this section, if (at any time during the calendar year in which the contractor enters into a construction contract) a 5 percent or greater interest in any person is owned, directly, or indirectly through the application of this paragraph (b)(3)(iii)(C), by or for the contractor, the average annual gross receipts of the contractor for the contractor's 3 taxable years preceding the taxable year of the contractor in which the contract was entered into (or, if less, the number of preceding taxable years the taxpayer has been in existence) shall include the average annual construction gross receipts of such person (for the 3 taxable years of such person preceding the taxable year of such person in which the contract was entered into or, if less, the number of preceding taxable years such person has been in existence) in proportion to the interest of the contractor in such person. If an interest is not owned for the entire calendar year, or if an interest varies during the calendar year, the amount of such interest for such year shall be the weighted average based on the number of days each interest is owned during such calendar year.

(3) Rules for determining ownership—(i) *In general*. in determining the ownership of an interest in any person for purposes of paragraph (b)(3)(iii)(C) of this section, the indirect and constructive ownership rules of this paragraph (b)(3)(iii)(C)*(3)* shall apply, subject to the operating rules contained in paragraph (b)(3)(iii)(C)*(4)*. For purposes of paragraph (b)(3)(iii)(C), an "interest" means: in the case of a corporation, stock; in the case of a trust or estate, an actuarial in-

terest; in the case of a partnership, an interest in capital or profits; and in the case of a sole proprietorship, the proprietorship.

(ii) Members of a family. An individual shall be considered as owning any interest in any person owned, directly or indirectly, by or for—

(A) Such individual's spouse (other than a spouse who is legally separated from the individual under a decree of divorce or separate maintenance, whether final or interlocutory), and

(B) such individual's children, grandchildren, parents and grandparents. A legally adopted child of an individual shall be treated as the child of such individual.

(iii) Attribution from partnerships, estates, trusts and corporations (A) From Partnerships. An interest in any person owned, directly or indirectly, by or for a partnership shall be considered as owned by any partner having a 5 percent or greater interest in either the profits or capital of the partnership, in proportion to such partner's interest in profits or capital, whichever is greater.

(B) From estate and trusts. An interest in any person (hereinafter an "organization interest") owned, directly or indirectly, by or for an estate or trust shall be considered as owned by any beneficiary of such estate or trust who has an actuarial interest of 5 percent or greater in such organization interest, to the extent of such actuarial interest, as determined under § 11.414(c)-4(b)(3).

An interest in any person owned, directly or indirectly, by or for any portion of a trust of which a person is considered the owner under subpart E of part I of subchapter J (relating to grantors and others treated as substantial owners) shall be considered as owned by such person.

(C) From corporations. An interest in any person owned, directly or indirectly, by or for a corporation shall be considered as owned by any shareholder who owns (directly, and indirectly through the application of paragraph (b)(3)(iii)(C) of this section) 5 percent or more in value of such corporation's stock, in proportion to the value of the stock owned by such shareholder to the total value of all the outstanding stock in such corporation.

(iv) Attribution to partnerships, estates, trusts and corporations—(A) To partnerships. An interest in any person owned, directly or indirectly, by or for a partner having a 5 percent or greater interest partnership profits or capital shall be considered as owned by the partnership in proportion to partner's interest in profits or capital, whichever is greater.

(B) To estates and trusts. An interest in any person owned, directly or indirectly, by or for a beneficiary having an actuarial interest of 5 percent or greater in the value of property of an estate or trust shall be considered as owned by such estate or trust in proportion to the beneficiary's actuarial interest in the assets of the estate or trust. For purposes of this paragraph (b)(3)(iii)(C)*(3)(iv)(B)* the actuarial interest of a beneficiary shall be determined under the maximum exercise of discretion by the executor or trustee in favor of such beneficiary. An interest in any person owned, directly or indirectly, by or for a person who is considered the owner of any portion of a trust under subpart E of part I of subchapter J (relating to grantors and others treated as substantial owners) shall be considered as owned by such trust.

(C) To corporations. An interest in any person owned, directly or indirectly, by or for a shareholder who owns (directly, and indirectly through the application of paragraph (b)(3)(iii)(C) of this section) 5 percent or more in value of the stock in a corporation shall be considered as owned by such corporation, in proportion to the value of the stock owned by such shareholder to the total value of all the outstanding stock in such corporation.

(v) Options. If a person has an option to acquire any outstanding interest in any organization, such interest shall be considered as owned by such person. An option to acquire an option, and each one of a series of such options, shall be considered as an option to acquire such an interest.

(4) Operating rules—(i) Common control. Paragraph (b)(3)(iii)(C) of this section shall not apply between two persons both of whom, under paragraph (b)(3)(iii)(B), are members of the group of trades or businesses under common control that includes the contractor. However, in applying paragraph (b)(3)(iii)(C) between two persons where one or both of such persons are not members of the group of trades or businesses under common control that includes the contractor, paragraph (b)(3)(iii)(C) shall be applied without regard to paragraph (b)(3)(iii)(B).

(ii) Reattribution. Except as provided in paragraph (b)(3)(iii)(C)*(4)(iii)* (relating to no double family attribution) or (iv) (relating to no reattribution to certain co-owners), in applying paragraph (b)(3)(iii)(C)*(3)(ii), (iii), (iv),* or *(v)*, an interest constructively owned by a person shall, in applying paragraph (b)(3)(iii)(C)*(3)(ii), (iii), (iv)* or *(v)*, be considered as actually owned by such person, and such interest may be reattributed to another person.

(iii) No double family attribution. An interest constructively owned by an individual by reason of paragraph (b)(3)(iii)(C)*(3)(ii)* shall not be considered as owned by such individual for purposes of again applying such paragraph to make another the constructive owner of such interest.

(iv) No reattribution to certain co-owners. An interest constructively owned by a person by reason of paragraph (b)(3)(iii)(C)*(3)(iv)* shall not be considered as owned by such person for purposes of applying paragraph (b)(3)(iii)(C)*(3)(iii)* in order to make another person the constructive owner of such interest.

(v) Option rule in lieu of family rule. If an interest may be considered as owned by an individual under paragraph (b)(3)(iii)(C)*(3)(ii)* or *(v)*, it shall be considered as owned by such individual under paragraph (b)(3)(iii)(C)*(3)(v)*.

(vi) Limitation. In applying paragraph (b)(3)(iii)(C)*(3)* to determine the ownership of an interest by any person for any one purpose—

(A) A corporation shall not be considered to own its own stock by reason of paragraph (b)(3)(iii)(C)*(3)(iv)(C)*, and

(B) If an interest owned by any person may be included in the computation more than one time, such interest shall be included only once, in the manner that will impute to the person concerned the largest total interest.

(C) *Short taxable years.* For any taxpayer required to determine its average annual gross receipts over the three taxable year period of such person preceding the taxable year in which a construction contract is entered into, if such period includes a taxable year of less than 12 full months, the taxpayer shall place the gross receipts of such taxable year on an annual basis by dividing the gross receipts of such taxable year by the number of full calendar months in such taxable year and multiplying the result by 12.

(iv) *Classification of contracts*—(A) *Initial classification by taxpayer*. The taxpayer shall determine whether a contract is an extended period long-term contract at the time such contract is entered into. In estimating the time required to perform any contract, the taxpayer shall anticipate and provide a reasonable allowance for delay, rework, change orders, technology or design problems, and other problems. If the taxpayer determines that a contract is an extended period long-term contract, the cost allocation rules of paragraph (d)(6) of this section shall apply, and such contract shall be treated as an extended period long-term contract even if such contract is actually completed within the 2-year period (3 years in the case of certain construction contracts) beginning on the contract commencement date of such contract. Except as provided in paragraph (b)(3)(iv)(B) of this section, a long-term contract that is not completed within the 2-year period (3 years in the case of certain construction contracts) beginning on the actual contract commencement date of such contract and which the taxpayer did not classify and account for as an extended period long-term contract will not be required to be reclassified (for any taxable year) and accounted for as an extended period long-term contract if, at the time the contract was entered into, the taxpayer reasonably could have expected the contract to be completed within that time. The taxpayer shall maintain contemporaneous written records setting forth the basis for classifying each contract, and such records shall be in sufficient detail to enable the district director readily to determine whether the taxpayer's estimate of the time required to complete a contract was made on a reasonable basis. A contract term specifying an expected completion or delivery date may be considered evidence that the parties expected completion or delivery to occur on or about the date specified, especially if there are actual bona fide penalties for not meeting the specified date. The taxpayer's estimate will not be considered unreasonable if a contract was not completed within the expected time primarily because of unforeseeable factors not within the control of the taxpayer. For purposes of the preceding sentence, "unforeseeable factors" are abnormal factors, such as prolonged third-party litigation, abnormal weather (considering the season and the jobsite), prolonged strikes, and prolonged delays in securing required permits or licenses, that could not reasonably be anticipated considering the nature of the contract and prior experience.

(B) *Exception for unreasonable classification; amended returns*. If under all the facts and circumstances it is determined that a contract which the taxpayer did not classify and account for as an extended period long-term contract reasonably should have been so classified and accounted for, the taxpayer shall reclassify and account for such contract as an extended period long-term contract for the current taxable year and all subsequent taxable years. In addition, the taxpayer should file an amended return for each prior taxable year (assuming that the period for assessment has not run for such year) in which costs were incurred with respect to such contract, and such amended returns should reflect an allocation to the contract of costs incurred in such prior years using the cost allocation rules provided in paragraph (d)(6) of this section. If a contract is not an extended period long-term contract by reason of the $25 million gross receipts test of paragraph (b)(3)(ii)(B) of this section, such contract shall not be reclassified regardless of the taxpayer's gross receipts for any subsequent year and regardless of the time required to complete such contract.

(v) *Special rule for contract commencement date in case of components or subassemblies produced by the taxpayer*. (If the cost of components or subassemblies produced by the taxpayer represents a significant amount of the total costs allocable to a contract, the contract commencement date of such contract shall be the first date the taxpayer incurs any costs allocable either to (1) such type or category of components or subassemblies, or (2) any other subject matter of the contract. The contract commencement date shall not be earlier than the date the contract is entered into, unless the taxpayer delayed entering into the contract for a principal purpose of avoiding the rules for this section. For example, assume an airplane manufacturer who also manufactures a type of engine that represents a significant amount of the total costs of the airplanes produced enters into one or more contracts to manufacture airplanes containing such type of engine. For purposes of determining the contract commencement date with respect to each contract, the first date the manufacturer incurs any cost allocable to any of the engines is the first date that the taxpayer incurs any cost allocable to such type of engine, even if the manufacturer has not yet produced enough engines to satisfy all contracts.

See §1.451-3(d)(6)(iv) for the cost allocation rules required in the case of certain components or subassemblies.

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(d) *Completed contract method*—(1) *In general*. Except as otherwise pro vided in paragraphs (d)(2), (3) or (4) (relating to disputes) of this section, under the completed contract method, gross income derived from long-term contracts must be reported by including the gross contract price of each contract in gross income for the taxable year in which such contract is completed (as defined in paragraph (b)(2) of this section). All costs properly allocable to a long-term contract (determined pursuant to paragraph (d)(5) or (6) of this section) must be deducted from gross income for the taxable year in which the contract is completed. In addition, account must be taken of any material and supplies charged to the contract but remaining on hand at the time of completion.

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(5) *General rule for allocation of costs to long-term contracts*. The following rules shall apply in determining what costs are properly allocable to a long-term contract, (other than an extended period long-term contract to which the rules of paragraph (d)(6) of this section apply) in the case of a taxpayer using the completed contract method of accounting for tax purposes:

(i) *Direct costs*. Direct material costs and direct labor costs must be treated as costs properly allocable to a long-term contract. "Direct material costs" include the costs of those materials which become an integral part of the subject matter of the long-term contract and those materials which are consumed in the ordinary course of building, constructing, installing, or manufacturing the subject matter of a long-term contract. See §1.471-3(b) for the elements of direct material costs. "Direct labor costs" include the cost of labor which can be identified or associated with a particular long-term contract. The elements of direct labor costs include such items as basic compensation, overtime pay, vacation and holiday pay, sick leave pay (other than payments pursuant to a wage continuation plan under section 105(d) as it existed prior to its repeal in 1983), shift differential, payroll taxes and payments to a supplemental unemployment benefit plan paid or incurred on behalf of employees engaged in direct labor.

(ii) *Indirect costs allocated to long-term contracts.* The term "indirect costs" includes all costs (other than direct material costs and direct labor costs) which are incident to and necessary for the performance of particular long-term contracts. Indirect costs which must be allocated to long-term contracts include:

(A) Repair expenses of equipment or facilities used in the performance of particular long-term contracts,

(B) Maintenance of equipment or facilities used in the performance of particular long-term contracts,

(C) Utilities, such as heat, light, and power, relating to equipment or facilities used in the performance of particular long-term contracts,

(D) Rent of equipment or facilities used in the performance of particular long-term contracts,

(E) Indirect labor and contract supervisory wages, including basic compensation, overtime pay, vacation and holiday pay, sick leave pay, (other than payments pursuant to a wage continuation plan under section 105(d) as it existed prior to its repeal in 1983), shift differential, payroll taxes and contributions to a supplemental unemployment benefit plan incurred in the performance of particular long-term contracts.

(F) Indirect materials and supplies used in the performance of particular long-term contracts.

(G) Tools and equipment not capitalized used in the performance of particular long-term contracts,

(H) Costs of quality control and inspection incurred in the performance of particular long-term contracts,

(I) Taxes otherwise allowable as a deduction under section 164 (other than State and local, and foreign income taxes) to the extent such taxes are attributable to labor, materials, supplies, equipment or facilities used in the performance of particular long-term contracts,

(J) Depreciation, amortization and cost recovery allowances reported for the taxable year for financial purposes on equipment and facilities used in the performance of particular long-term contracts (but not in excess of the depreciation, amortization or cost recovery allowance allowable for the taxable year under Chapter I of the Code with respect to any item of equipment or facility),

(K) Cost depletion incurred in the performance of particular long-term contracts,

(L) Administrative costs incurred in the performance of particular long-term contracts (but not including any cost of selling or any return on capital),

(M) Compensation paid to officers attributable to services performed on particular long-term contracts (other than incidental or occasional services), and

(N) Costs of insurance incurred in the performance of particular long-term contracts, such as insurance on machinery and equipment used in the construction of the subject matter of a long-term contract.

(iii) *Costs not allocated to long-term contracts.* Costs which are not required to be included in costs attributable to a long-term contract include:

(A) Marketing and selling expenses, including bidding expenses,

(B) Advertising expenses,

(C) Other distribution expenses,

(D) Interest,

(E) General and administrative expenses attributable to the performance of service which benefit the long-term contractor's activities as a whole (such as payroll expenses, legal and accounting expenses, etc.),

(F) Research and experimental expenses (described in section 174 and the regulations thereunder),

(G) Losses under section 165 and the regulations thereunder,

(H) Percentage of depletion in excess of cost depletion,

(I) Depreciation, amortization and cost recovery allowances on equipment and facilities that have been placed in service but are temporarily idle (for this purpose, an asset is not considered to be temporarily idle on non-working days, and an asset used in construction is considered to be idle when it is not enroute to or not located at a job-site), and depreciation, amortization and cost recovery allowances under Chapter I of the Code in excess of depreciation, amortization and cost recovery allowances reported by the taxpayer in the taxpayer's financial reports,

(J) Income taxes attributable to income received from long-term contracts,

(K) Contributions paid to or under a stock bonus, pension, profit-sharing or annuity plan or other plan deferring the receipt of compensation whether or not the plan qualifies under section 401(a), and other employee benefit expenses paid or accrued on behalf of labor, to the extent such contributions or expenses are otherwise allowable as deductions under chapter 1 of the Code. "Other employee benefit expenses" include (but are not limited to): worker's compensation; amounts deductible or for whose payment reduction in earnings and profits is allowed under section 404A and the regulations thereunder; payments pursuant to a wage continuation plan under section 105(d) as it existed prior to its repeal in 1983; amounts includible in the gross income of employees under a method or arrangement of employer contributions or compensation which has the effect of a stock bonus, pension, profit-sharing, or annuity plan, or other plan deferring the receipt of compensation or providing deferred benefits; premiums on life and health insurance; and miscellaneous benefits provided for employees such as safety, medical treatment, recreational and eating facilities, membership dues, etc.

(L) Cost attributable to strikes, rework labor, scrap and spoilage, and

(M) Compensation paid to officers attributable to the performance of services which benefit the long-term contractor's activities as a whole.

(6) *Allocation of costs to extended period long-term contracts.* Except as

provided in paragraph (g) of this section, this paragraph (d)(6) applies to taxable years beginning after December 31, 1982. The following rules shall apply in determining what costs are properly allocable to an extended period long-term contract (as defined in paragraph (b)(3) of this section) in the case of a taxpayer using the completed contract method of accounting for long-term contracts for tax purposes. These rules may also apply to certain extended period long-term contracts accounted for under a method of accounting that uses inventories (other than a long-term contract method). See paragraph (d)(6)(v) of this section.

(i) *Direct costs.* Direct material costs and direct labor costs must be treated as costs properly allocable to an extended period long-term contract. "Direct material costs" include the costs of those materials which become an integral part of the subject matter of the extended period long-term contract and those materials which are consumed in the ordinary course of building, constructing, installing or manufacturing the subject matter of an extended period long-term contract. See §1.471-3(b) for the elements of direct material costs. "Direct labor costs" include the cost of labor which can be identified or associated with a particular extended period long-term contract. The elements of direct labor costs include such items as basic compensation, overtime pay, vacation and holiday pay, sick leave pay (other than payments pursuant to a wage continuation plan under section 105(d) as it existed prior to its repeal in 1983), shift differential, payroll taxes and payments to a supplemental unemployment benefit plan paid or incurred on behalf of employees engaged in direct labor.

(ii) *Indirect costs allocated to extended period long-term contracts.* The term "indirect costs" include all costs other than direct material costs and direct labor costs. In determining what indirect costs are properly allocable to an extended period long-term contract, all such costs that directly benefit the performance of extended period long-term contracts, or are incurred by reason of the performance of extended period long-term contracts must be allocated to extended period long-term contracts unless otherwise provided in paragraph (d)(6)(iii) of this section. Certain types of costs may directly benefit, or be incurred by reason of the performance of extended period long-term contracts of the taxpayer even though the same type of costs also benefits other activities of the taxpayer. Accordingly, such costs require a reasonable allocation between the portion of such costs that are attributable to extended period long-term contracts and the portion attributable to the other activities of the taxpayer. Indirect costs that must be allocated to extended period long-term contracts include:

(A) Repair expenses of equipment or facilities used in the performance of particular extended period long-term contracts,

(B) Maintenance of equipment or facilities used in the performance of particular extended period long-term contracts,

(C) Utilities, such as heat, light, and power, relating to equipment or facilities used in the performance of particular extended period long-term contracts,

(D) Rent of equipment or facilities used in the performance of particular extended period long-term contracts,

(E) Indirect labor and contract supervisory wages, including basic compensation, overtime pay, vacation and holiday pay, sick leave pay (other than payments pursuant to a wage continuation plan under section 105(d) as it existed prior to its repeal in 1983), shift differential, payroll taxes and contributions to a supplemental unemployment benefit plan incurred in the performance of particular extended period long-term contracts,

(F) Indirect materials and supplies used in the performance of particular extended period long-term contracts,

(G) Tools and equipment not capitalized used in the performance of particular extended period long-term contracts,

(H) Costs of quality control and inspection incurred in the performance of particular extended period long-term contracts,

(I) Taxes otherwise allowable as a deduction under section 164 (other than State and local [,] and foreign income taxes) to the extent such taxes are attributable to labor, materials, supplies, equipment or facilities used in the performance of particular extended period long-term contracts,

(J) Depreciation, amortization and cost recovery allowances on equipment and facilities (to the extent allowable as deductions under Chapter 1 of the Code) used in the performance of particular extended period long-term contracts,

(K) Depletion (whether or not in excess of cost) incurred in the performance of particular extended period long-term contracts,

(L) Administrative costs (whether or not performed on a job-site) directly attributable to the performance of particular extended period long-term contracts (but not including any cost of selling, or any return on capital),

(M) Direct and indirect costs incurred by any administrative, service, or support function or department to the extent such costs are allocable to particular extended period long-term contracts pursuant to paragraph (d)(9) of this section,

(N) Compensation paid to officer attributable to services performed on particular extended period long-term contracts (but not including any cost of selling),

(O) Costs of insurance incurred in the performance of particular extended period long-term contracts, such as insurance on machinery and equipment used in the construction of the subject matter of an extended period long-term contract,

(P) Contributions paid to or under a stock bonus, pension, profit-sharing or annuity plan or other plan deferring the receipt of compensation whether or not the plan qualifies under section 401(a) (except for amounts described in paragraph (d)(6)(iii)(I) of this section), and other employees benefit expenses paid or accrued on behalf of labor, to the extent such contributions or expenses are otherwise allowable as deductions under chapter 1 of the Code. "Other employee benefit expenses" include (but are not limited to): worker's compensation; amounts deductible or for whose payment reduction in earnings of profits is allowed under section 404A and the regulations thereunder; payments pursuant to a wage continuation plan under section 105(d) as it existed prior to its repeal in 1983; amounts includible in the gross income of employees under a method or arrangement of employer contributions or compensation which has the effect of a stock bonus, pension, profit-sharing, or annuity plan, or other plan deferring the receipt of compensation or providing deferred benefits; premiums on life and health insurance; and miscellaneous benefits provided for employees such as safety, medical treatment, recreational and eating facilities, membership dues, etc.

(Q) Research and experimental expenses (described in section 174 and the regulations thereunder) directly attributable to particular extended period long-term contracts in existence at the time such expenses are incurred, or incurred under an agreement to perform research or experimentation

(R) Rework labor, scrap and spoilage to the extent incurred in the performance of particular extended period long-term contracts, and

(S) Bidding expenses incurred in the solicitation of particular extended period long-term contracts ultimately awarded to the taxpayer. For purposes of this section, the term "bidding expenses" does not include any research and experimental expenses described in section 174 and the regulations thereunder. The taxpayer shall defer all bidding expenses paid or incurred in the solicitation of a particular extended period long-term contract until the contract is awarded. If the contract is awarded to the taxpayer, the bidding costs become part of the indirect costs assigned to the contract. If the contract is not awarded to the taxpayer, bidding costs become deductible in the taxable year the contract is awarded, or the taxable year the taxpayer is notified in writing that no contract will be awarded and that the contract (or similar or related contract) will not be re-bid, or in the taxable year that the taxpayer abandons its bid or proposal, whichever occurs first. Abandoning a bid does not include modifying, supplementing, or changing the original bid or proposal. If the taxpayer is awarded only part of the bid (for example, the taxpayer submitted one bid to build each of two different types of bridges and the taxpayer was awarded a contract to build only one of the two bridges), the taxpayer shall deduct the portion of the bidding expenses related to the portion of the bid not awarded to the taxpayer; in the case of a bid or proposal for a multi-unit contract, however, all the bidding expenses shall be allocated to a contract awarded to the taxpayer to produce any or such units (for example, where the taxpayer submitted one bid to produce three similar turbines and the taxpayer was awarded a contract to produce only two of the three turbines).

(iii) *Costs not allocated to extended period long-term contracts.* Costs which are not required to be included in costs attributable to an extended period long-term contract include:

(A) Marketing, selling and advertising expenses;

(B) Bidding expenses incurred in the solicitation of contracts not awarded to the taxpayer (see paragraph (d)(6)(ii)(S) of this section),

(C) Interest,

(D) General and administrative expenses (but not including any cost described in paragraph (d)(6)(ii)(L) or (M) of this section) and compensation paid to officers attributable to the performance of services that do not directly benefit or are not incurred by reason of any extended period long-term contracts,

(E) Research and experimental expenses (described in section 174 and the regulations thereunder) neither directly attributable to particular extended period long-term contracts in existence at the time such expenses are incurred nor incurred under any agreement to perform research or experimentation,

(F) losses under section 165 and the regulations thereunder,

(G) Depreciation, amortization and cost recovery allowances on equipment and facilities that have been placed in service but are temporarily idle (for this purpose, an asset is not considered to be temporarily idle on non-working days, and an asset used in construction is considered to be idle when it is not enroute to or not located at a job-site),

(H) Income taxes attributable to income received from extended period long-term contracts,

(I) Contributions paid to or under a pension or annuity plan allowable as a deduction under section 404 (and section 404A if applicable) to the extent such contributions represent past service costs, and

(J) Costs attributable to strikes.

(iv) *Special rule for component parts or subassemblies produced by the taxpayer.* In the case of any type of component or subassembly produced by the taxpayer, the taxpayer shall use the cost allocation rules prescribed in paragraph (d)(6) and (8) of this section to determine the unit cost of the components or subassemblies that reasonably can be expected to be incorporated into the subject matter of extended period long-term contracts of the taxpayer. The taxpayer may use other proper cost allocation rules (see §1.471-11) to determine the unit cost of the components or subassemblies other than those described in the preceding sentence. For each taxable year, the taxpayer's estimate of the number of components or subassemblies that can be expected to be incorporated into the subject matter of extended period long-term contracts shall be considered reasonable if the estimate is based upon facts known at the beginning of the taxable year.

(v) *Taxpayers not using a long-term contract method.* Taxpayers who use a method of accounting that uses inventories (other than a long-term contract method) must use the cost allocation rules provided in paragraph (d)(6) of this section (rather than the cost allocation rules provided in §1.471-11) for any extended period long-term contract unless the taxpayer reasonably expects that

(A) 40% of the gross income from such contract will be recognized no later than the taxable year after the taxable year in which the contract is entered into;

(B) 70% of the gross income from such contract will be recognized no later than the second taxable year after the taxable year in which the contract is entered into; and

(C) 100% of the gross income from such contract will be recognized no later than the third taxable year after the taxable year in which the contract is entered into.

In determining whether the taxpayer meets the "reasonably expected" test of this paragraph (d)(6)(v), rules consistent with the rules of paragraph (b)(3)(iv) of this section will apply.

(7) *Guarantees, warranties, maintenance costs, etc.* "Costs which are properly allocable to a long-term contract" do not include costs incurred with respect to any guarantee, warranty, maintenance, or other service agreement relating to the subject matter of the long-term contract. See paragraph (a)(3) of this section.

(8) *Separate accounts; annual cost allocation; use of inventory methods in*

connection with the completed contract method—(i) *General rule*. This paragraph (d)(8) is effective for taxable years beginning after December 31, 1982. For taxable years beginning before January 1, 1983, see 26 CFR 1.451-3(d)(6) (revised as of April 1, 1985). The taxpayer shall maintain separate accounts for each long-term contract, and both the direct costs (as described in paragraph (d)(5)(i) or (d)(6)(i) of this section) and the indirect costs (as described in paragraph (d)(5)(ii) or (d)(6)(ii) of this section) incurred during the taxable year attributable to long-term contracts shall be allocated to particular long-term contracts for the taxable year such costs are incurred. Any change in the taxpayer's method of accounting for costs attributable to long-term contracts required by this paragraph (d)(8) is a change in method of accounting to which section 446(e) and the regulations and procedures thereunder apply.

(ii) *Direct labor*. Direct labor costs incurred during the taxable year shall be allocated to particular long-term contracts using a specific identification (or "tracing") method. However, if direct labor costs attributable to more than one long-term contract are intermingled so that it is impractical to specifically identify (or "trace") such costs to a particular long-term contract, such costs shall be allocated to particular long-term contracts using any reasonable method, provided that the method employed reasonably allocates direct labor costs among long-term contracts completed during the taxable year and long-term contracts that have not been completed as of the end of the taxable year.

For the purpose of allocating elements of direct labor cost other than basic compensation to particular long-term contracts, all such cost elements may be grouped together and then allocated to particular long-term contracts in proportion to the charge for basic compensation.

(iii) *Direct materials*. (A) *General rule*. The cost of direct materials that are dedicated to a long-term contract in a taxable year shall be allocated to that long-term contract for that year. The cost that is allocated to the particular contract for the year of dedication shall be determined using the taxpayer's method of accounting for inventories (e.g., specific identification, FIFO, LIFO, etc.) of the material whose cost is being allocated. The costing rule in the preceding sentence applies both when materials are purchased specifically for a contract and when materials previously held by the taxpayer are dedicated to the contract. Examples of dedication of materials to a long-term contract include the following: *(1)* delivery of materials to a job site (if only one contract is being performed at that site); *(2)* association of materials with a specific contract (for example, by purchase order, entry on books and records, shipping instructions, etc.); and, if not previously assigned, the physical incorporation of the material into the subject matter of the contract or the consumption of the material in the production of the subject matter of the contract.

(B) *Alternative rule for taxable years beginning after December 31, 1982 and before January 1, 1986*. For taxable years beginning after December 31, 1982, and before January 1, 1986, taxpayers may, in lieu of applying the general rule of paragraph (d)(8)(iii)(A) of this section, allocate direct costs incurred during the taxable year to particular long-term contracts using the specific identification (or "tracing") method, and if direct costs attributable to more than one long-term contract are intermingled so that such costs cannot be identified (or "traced") specifically to a particular long-term contract, such costs shall be allocated to particular long-term contracts using any reasonable method, provided that the method employed reasonably allocates direct costs among long-term contracts completed during the taxable year and long-term contracts that have not been completed as of the end of the taxable year. However, taxpayers utilizing the rule of this paragraph (d)(8)(iii)(B) may not use any LIFO or lower of cost or market method of identifying or allocating direct costs to any long-term contract.

(iv) *Indirect costs*. The indirect costs required to be allocated to a long-term contract under paragraph (d)(5)(ii) or (d)(6)(ii) of this section shall be allocated to particular contracts for the year such costs are incurred using either—

(A) A specific identification (or "tracing") method, or

(B) A method using burden rates, such as ratios based on direct costs, hours, or other items, or similar formulas, so long as the method employed for such allocation reasonably allocates indirect costs among long-term contracts completed during the taxable year and long-term contracts that have not been completed as of the end of the taxable year. Indirect costs may ordinarily be allocated to long-term contracts on the basis of direct labor and material costs, direct labor hours, or any other basis which results in a reasonable allocation of such indirect costs.

(9) *Allocation of administrative, service, or support costs to extended period long-term contracts*—(i) *Introduction*. (A) If a function or department of the taxpayer incurs costs that directly benefit or are incurred by reason of the extended period long-term contract activities of the taxpayer, the costs of such function or department are allocable to such extended period long-term contracts. See paragraph (d)(6)(ii)(M) of this section. However, if a function or department incurs costs that do not directly benefit and are not incurred by reason of the taxpayer's extended period long-term contracts, but rather, for example, benefit only the overall management or policy guidance functions of the taxpayer, the costs incurred by such function or department are not allocable to any extended period long-term contract. In some cases, the costs incurred by a function or department may directly benefit or be incurred by reason of the taxpayer's extended period long-term contract activities as well as the taxpayer's overall management or policy guidance function. In such cases, the taxpayer shall reasonably allocate the costs of such function or department between the taxpayer's extended period long-term contract activities and the taxpayer's overall management or policy guidance functions. Paragraph (d)(9) of this section provides guidance in making these allocations.

(B) If the methods of allocation used by the taxpayer, or the taxpayer's selection of specific types of costs to be allocated differs from the allocation methods or the specific types of costs to be allocated described in this paragraph (d)(9), the taxpayer's allocation methods and selection of specific types of costs to be allocated shall generally not be changed if with respect to the taxpayer's extended period long-term contracts taken as a whole—

(1) The total amount of costs incurred during the taxable year of a type described in this paragraph (d)(9) that the taxpayer allocated to such contracts does not differ significantly from the total amount of costs that would be allocated to such contracts under this paragraph (d)(9); and

(2) the taxpayer's selection of cost allocation methods and specific types of costs to be allocated are applied consistently and do not result in any disproportionate allocation of costs to contracts expected to be completed in the near future.

(ii) *General rule.* The total amount of administrative, service, or support costs that directly benefit or are incurred by reason of only a particular extended period long-term contract shall be directly assigned to such contract. The direct and indirect costs (hereinafter "service costs") of administrative, service or support functions or departments (hereinafter "service departments") that directly benefit or are incurred by reason of more than one activity shall be allocated to particular extended period long-term contracts on the basis of a factor or relationship that reasonably relates the incurring of the service cost to the benefits received by the extended period long-term contract. In general, the direct costs of a service department include costs that an be identified specifically with the services provided by the department, and the indirect costs of a service department include costs not identified specifically with the services provided by the function or department, but incurred by reason of the direct costs of the function or department. Such direct and indirect costs include, but are not limited to, compensation (including compensation described in paragraph (d)(6)(ii)(E) and (P) of this section) of employees directly engaged in performing the services provided by the department, travel, materials and supplies consumed by the department, supervisory and clerical compensation, occupancy costs (rents or an allocable share of depreciation and property taxes), depreciation or rent of office machines, utilities, telephone, and other department overhead. The types of activities that are administrative, service or support functions or departments are not predetermined, but depend upon the facts and circumstances of each contractor's activities and business organization. In a decentralized business organization, all costs incurred at higher levels, for example, at a parent corporation or organization, or at the headquarters of a subsidiary corporation or division, are not necessarily general and administrative expenses (as described in paragraph (d)(6)(iii)(D) of this section) with respect to an extended period long-term contract.

(iii) *Rules for allocation of service costs.* The taxpayer shall allocate the total direct and indirect costs of a service department to extended period long-term contracts by applying consistently any reasonable method of cost allocation authorized by cost accounting principles. Reasonable methods include:

(A) The direct reallocation method whereby the total costs (direct and indirect) of all service departments are allocated only to production departments, and then from the production departments to particular extended period long-term contracts and to other production activities that are not extended period long-term contracts. The service costs allocable to such other production activities shall be accounted for under a proper method of accounting. This direct reallocation method ignores benefits provided by one service department for other service departments, and also excludes such other service departments from the base used to make the allocation;

(B) The step-allocation method, whereby a sequence of allocations is made beginning with the allocation to other service departments and to production departments of the total costs (direct and indirect) of the service department that provides benefits to the greatest number of other service departments, and ending with the allocation of the total costs (including the costs allocated to it from the other service departments) of the service department that provides benefits to the least number of other service departments. Under this allocation method, the costs of service departments allocated properly to functions or departments that are not service departments or production departments (for example, payroll costs allocated to a financial planning function or department) are not reallocated to any other service department or production department. The taxpayer shall then allocate the costs of the production departments (including the reallocated service department costs) to extended period long-term contracts and to other production activities that are not extended period long-term contracts. The service costs allocable to such other production activities shall be accounted for under a proper method of accounting; or

(C) Other methods of cost allocation authorized by cost accounting principles. However, a reasonable method does not include allocating service department costs to other service departments without taking such allocation into account in allocating the costs of such other service departments.

(iv) *Relationship of service costs to benefits received.* Factors or relationships that relate the incurring of service costs to the benefits received by an extended period long-term contract include measures based upon the total output of the service department (for example, the approximate number of service hours or the approximate number or the dollar volume of transactions provided to an extended period long-term contract as a fraction of the total number of service hours or the total number or the total dollar volume of transactions provided by the department), or measures based upon the relative size of the extended period long-term contract to the size of the taxpayer's other production activities (for example, the number of direct labor employees or direct labor hours or direct labor costs (as described in paragraph (d)(6)(i) of this section) incurred on an extended period long-term contract as a fraction of the total number of direct labor employees, direct labor hours, or direct labor costs incurred by the taxpayer in all production activities). In general, allocation methods prescribed in regulations of the Cost Accounting Standards Board, 4 CFR Chapter III, Subchapter G, as well as other allocation methods consistent with the principles of paragraph (d)(g) of this section are acceptable allocation methods, provided that the taxpayer applies such methods consistently.

(v) *Additional requirements.* (A) If, pursuant to section 482 and the regulations thereunder, the district director makes an allocation of income or deductions between members of a group of controlled entities to reflect the performance of services or the provision of equipment or facilities at other than an arm's length charge, any taxpayer that has extended period long-term contracts and is affected by such allocation is required to take such allocation into account in making the taxpayer's allocation to extended period long-term contracts of the cost of administrative, service or support functions or departments, (B) If the taxpayer establishes to the satisfaction of the district director that all of a particular type of administrative, service or support function is performed only at the jobsite (that is, at the offices of a production plant or at a construction site), then all the direct and indirect costs of such function incurred at the jobsite shall be directly allocated to each particular extended period long-term contract and any other activities performed at that jobsite, and no further allocation of that type of cost shall be required. (C) For each taxable year that the taxpayer allocates service costs to an extended period long-term contract, the taxpayer shall maintain the records used to make such allocation so that the allocations may be readily examined and verified by the district director. The taxpayer shall also maintain records describing the types of costs that the taxpayer has deducted currently under paragraph (d)(6)(iii)(D) (general and administrative expenses), so that the amount, nature and allocation of such costs may be verified readily by the district director. A change in the method or base used in allocating such service costs (such as changing from an allocation base using direct labor cost to a base using direct labor hours), or a change in the taxpayer's determination of what functions or departments of the taxpayer are required or not required to be allocated to extended period long-term contracts is a change in method of accounting to which section 446(e) and the regulations and procedures thereunder apply. See §1.446-1(e).

(vi) *Illustration of types of activities with respect to which costs ordinarily are required to be allocated.* Costs incurred by the following types of functions or departments ordinarily are required to be allocated to extended period long-term contracts:

(A) The administration and coordination of manufacturing or construction projects (wherever performed in the business organization of the taxpayer);

(B) Personnel operations, including the cost of recruiting, hiring, relocating, assigning, and maintaining personnel records of employees whose labor cost is allocable to extended period long-term contracts;

(C) Purchasing operations, including purchasing materials and equipment, scheduling and coordinating delivery and return of materials and equipment to or from factories or jobsites, and expediting and follow-up;

(D) Materials handling and warehousing operations;

(E) Accounting and data services operations related to contract activities, including cost accounting, accounts payable, disbursements, billing, accounts receivable and payroll;

(F) Data processing;

(G) Security services; and

(H) Legal departments that provide legal services to contracts.

(vii) *Illustration of types of activities with respect to which costs ordinarily are not required to be allocated.* Costs incurred by the following types of functions or departments ordinarily are not required to be allocated to extended period long-term contracts:

(A) Functions or departments responsible for overall management of the taxpayer, or for setting overall policy for all of the taxpayer's activities or trades or businesses (such as, the board of directors including their immediate staff), and the chief executive, financial, accounting and legal officers (including their immediate staffs) of the taxpayer, provided that no substantial part of the costs of such departments or functions directly benefit extended long-term contracts);

(B) General business planning;

(C) Financial accounting (including the accounting services required to prepare consolidated reports, but not including any accounting for particular contracts);

(D) General financial planning (including general budgeting) and financial management (including bank relations and cash management);

(E) General economic analysis and forecasting;

(F) Internal audit;

(G) Shareholder, public and industrial relations;

(H) Tax department; and

(I) Other departments or functions that are not responsible for day-to-day operations but are instead responsible for setting policy and establishing procedures to be used by all of the taxpayer's activities or trades or businesses.

(viii) *Policy and overall management services.* Examples of such functions or departments that are responsible for setting policy and establishing procedures applicable to all of the taxpayer's activities or trades or businesses (see paragraph (d)(9)(vii)(I) of this section) are:

(A) Purchasing policy (such as maintaining lists of approved suppliers, developing purchasing manuals and policy directives of general application, developing general quality standards for purchased materials and components, general auditing and review of purchasing activities to assure compliance with the taxpayer's purchasing policy and compliance with government purchasing requirements, and management of small business participation),

(B) Personnel policy (such as establishing and managing personnel policy in general, developing general wage, salary and benefit policies, developing employee training programs unrelated to particular contracts, negotiations with labor unions and relations with retired workers),

(C) Quality control policy,

(D) Safety engineering policy,

(E) Insurance or risk management policy (but not including bid or performance bonds or insurance related to particular contracts), and

(F) Environmental management policy. However, the cost of establishing any system or procedure that will only benefit a particular extended period long-term contract shall be directly allocated to such contract.

(ix) *Costs not described.* The costs of any administrative, service or support function or department of the taxpayer not described in paragraph (d)(9)(iv) or (vii) of this section are required to be allocated to extended period long-term contracts to the extent that the nature of the benefits provided by such function or department is more like the type of benefits described in paragraph (d)(9)(vi) than the type of benefits described in paragraph (d)(9)(vii).

(x) *Illustrations of the allocations required by this paragraph (d)(9).* The following illustrate the types of considerations that are to be taken into account in making the allocations required by paragraph (d)(9) of this section. The taxpayer need not use the same method to allocate a particular type of administrative, service or support cost as the method described in these illustrations provided that the method used by the taxpayer is reasonable. See paragraph (d)(9)(iii) of this section. The allocation methods illustrated may be used to allocate other types of service costs not illustrated [.]

(A) *Security services.* The cost of security or protection services benefits all areas covered by the service and should be allocated to each physical area that receives the service in proportion either to the size of the physical area, number of employees in the areas, or in proportion to the relative fair market value of assets located in the area, or in any other reasonable basis applied consistently. That part of the total cost allocable to a factory or jobsite where the only work being performed is an extended period long-term contract shall be directly allocated to that contract. The treatment of the cost of security services allocable to other service departments depends upon the method of allocation adopted by the taxpayer under paragraph (d)(9)(iii) of this section.

(B) *Legal services.* The cost of a legal department includes rent (or an allocation of building depreciation and occupancy costs), travel, office machines, supplies, telephone, library, and other overhead, and the compensation of the attorneys and other employees assigned to the department. For this purpose compensation includes compensation described in paragraph (d)(6)(ii)(E) and (P) of this section. These costs only benefit activities of the taxpayer requiring legal services. These costs are generally allocable directly to an extended period long-term contract on the basis of the approximate number of hours of legal services (including research) performed in connection with the contract, including bidding, negotiating, drafting, or reviewing the contract (including subcontracts and supply contracts), obtaining necessary licenses and permits, and in resolving contract disputes, termination claims or disputes arising from the performance of the contract. Different hourly rates may be appropriate for different services. In determining the number of hours allocable to any contract, approximations are appropriate, detailed time records need not be kept, and insubstantial amounts of services provided to a contract by senior legal staff as administrators or as reviewers may be ignored. The taxpayer shall also allocate directly to a contract the cost of any outside legal services provided to the contract. Instead of an allocation based upon total hours of legal services provided to an activity, the taxpayer may choose to allocate the costs of a legal department to an extended period long-term contract and to other production activities on the basis of total direct costs (as described in paragraph (d)(6)(i) of this section) incurred on an extended period long-term contract as a fraction of the total direct costs incurred on all production activities. Legal costs may also be allocable to long-term contracts of the taxpayer that are not extended period long-term contracts under paragraph (d)(5)(ii) of this section. Legal activities relating to general corporate functions, financing, securities law compliance, antitrust law compliance, tax compliance, industrial relations, compliance with laws and regulations not related to particular contracts, after the fact review of contracts to insure compliance with company policies, patents and licensing unrelated to particular contracts, and similar general legal functions are not required to be allocated to long-term contracts.

(C) *Centralized payroll department.* The cost of a payroll department includes rent (or an allocation of building depreciation and occupancy costs), office machines, supplies, telephones and other overhead and compensation of employees assigned to the department. The department cost may also include the cost of data processing and file maintenance, or these costs may be incurred by a separate data processing or records department and allocated to the payroll department. Payroll service costs benefit any production department or other service department incurring labor costs. The cost of a payroll department is generally allocated on the basis of the gross amount of payroll processed.

(D) *Centralized data processing.* The cost of a data processing department includes rent or depreciation of data processing machines, supplies, rent (or an allocation of building depreciation and occupancy costs), power, telephone and other overhead, and the compensation of employees assigned to the department. These costs benefit all production departments and all other service departments that require data processing services. Data processing costs are generally allocated based upon the number of data processing hours supplied. Other reasonable bases, such as an allocation based upon total direct costs, may also be used. The costs of data processing systems developed for a particular long-term contract shall be directly allocated to such contract.

(E) *engineering and design services.* The cost of an engineering or design department includes rent (or an allocation of building depreciation and occupancy costs), travel, office machines, supplies, telephones, library, and other overhead, and compensation of employees assigned to the department. Unless the engineering and design services are properly accounted for separately, the cost of engineering or design service departments generally is directly allocable to a long-term contract (whether or not the contract is an extended period long-term contract) on the basis of the approximate number of hours of work performed on the contract as a fraction of the total hours of engineering or design work performed for all activities. Different services may be allocated at different hourly rates. Engineering and design services may also be treated as direct costs of the contract, provided that the taxpayer also treats all engineering and design overhead as a direct or indirect cost of the contract.

(F) *Safety and engineering.* The cost of a safety engineering department includes the compensation paid to employees assigned to the department, rent (or an allocation of building depreciation and occupancy costs), travel, office, machines, supplies, telephones, library, and other overhead. These costs benefit all the production activities of the taxpayer and should be allocated to an extended period long-term contract on the basis of the approximate number of safety inspections made on the contract as a fraction of total inspections, or on the basis of the number of employees assigned to the contract as a fraction of total production employees or on the basis of total labor hours worked on the contract as a fraction of total production hours, whichever is most reasonable. The cost of a safety engineering department responsible only for setting safety policy and establishing safety procedures to be used in all of the taxpayer's production activities or trades or businesses is not required to be allocated to extended period long-term contracts and other production activities. However, in determining the total costs of a safety engineering department to be allocated, costs attributable to providing a safety program only for a particular long-term contract shall be directly assigned to the contract.

(e) *Severing and aggregating contracts*—(1) *In general.* (i)(A) For the purpose of clearly reflecting income (*e.g.*, to prevent the unreasonable deferral of recognition of income or the premature recognition of loss), it may be necessary in some instances for the Commissioner either to treat one agreement as several contracts or to treat several agreements as one contract.

(B) However, in the case of long-term contracts since the factors described in this paragraph are different from the factors for determining whether certain elements of an agreement are eligible for long-term contract treatment, the factors described in this paragraph do not apply in determining which elements of an agreement that are ineligible for long-term contract treatment must be separated from those elements that are eligible for long-term contract treatment.

(C) In general only the Commissioner (and not the taxpayer) may take action under this paragraph. Thus, for example, if the taxpayer enters into one agreement, the taxpayer may not treat that agreement as several contracts for purposes of this section unless and until that agreement is changed into several agreements. See examples 3 and 5 for instances when one agreement is changed into several agreements.

(ii) Whether an agreement should be so severed or several agreements so aggregated will depend on all the facts and circumstances. Such facts and circumstances may include whether there is separate delivery or separate acceptance of units representing a portion of the subject matter of the contract, whether such units are independently priced, whether there is no business purpose for one agreement rather than several agreements or several agreements rather than one agreement, and such other factors as customary commercial practice, the dealings between parties to the contract, the nature of the subject matter of the contract, the total number of units to be constructed, manufactured, or installed under the contract, and the contemplated time between the completion of each unit.

(iii) Generally, one agreement will not be treated as several contracts unless such agreement contemplates separate delivery or separate acceptance of portions of the subject matter of the contract. However, separate delivery or separate acceptance of portions of the subject matter of a contract does not necessarily require severing of an agreement (see example (4) of paragraph (e)(2) of this section).

(iv) One agreement may be severed, or several agreements may be aggregated, based upon the pricing formula of such agreements. For example, in the case of a multi-unit agreement for several similar items, if the price to be paid for similar units is determined under different terms or formulas (for example, if some units are priced under a cost-plus incentive fee arrangement, and later units are to be priced under a fixed-price arrangement), then the difference in the pricing terms or formulas may indicate that the agreement should be treated as several contracts.

(v) An agreement generally will be treated as several contracts where there is no business purpose for entering into one agreement rather than several agreements. A factor which may evidence that no such business purpose exists is that the agreement covers two or more subject matters, none of which readily can be determined to be the primary subject matter of the contract (within the meaning of paragraph (b)(2)(ii) of this section); such factor must be considered along with other factors indicating the presence or absence of business purpose.

(vi) Several agreements generally will not be aggregated unless there is no business purpose for entering into several agreements rather than one agreement.

(vii) An example of a factor which is evidence that two agreements entered into between the same parties should be aggregated is that (without regard to the order in which the agreements were entered into or performed, and without regard to whether one of the agreements could actually be performed without the prior or contemporaneous performance of the other agreement) a reasonable business-person would not have entered into one of the agreement for the terms agreed upon but for entering into the other agreement in such other agreement for the terms agreed upon (or for more favorable terms). See example (2) of paragraph (e)(2) of this section. An example of a factor which is not evidence that two agreements entered into between the same parties should be aggregated is that one of the agreements would not have been entered into containing the terms agreed upon but for the expectation that the parties would enter into the other agreement.

(viii) If the number of items to be supplied is increased (as by the exercise of an option or the issuance of a "change order"), the supplying of such additional items generally results in the agreement being changed into several agreements. See paragraph §1.451-3(e)(1)(i).

(ix) See paragraph (b)(2)(ii) of this section for special rules relating to the time for completion of certain contracts having more than one subject matter.

(2) *Examples.* The application of paragraph (e) of this section may be illustrated by the following examples.

Example (1). X, a calendar year taxpayer engaged in the construction business and using a long-term contract method, enters into one agreement in 1972 with A, a real estate developer, to build three houses of different designs in three different suburbs of a large city. The houses are to be completed, accepted, and put into service in 1973, 1974, and 1975, respectively. The portion of the total contract price attributable to each house can reasonably be determined. In these circumstances it may be necessary for the Commissioner to sever and threat the agreement as separate contracts to build each house for purposes of applying X's long-term contract method.

Example (2). Y, a calendar year shipbuilder using a long-term contract method, enters into two agreements at about the same time during 1982 with M. These agreements are the product of a single negotiation. Under each agreement the taxpayer is to construct for M a submarine of the same class. Although the specifications for each submarine are similar, it is anticipated that, since the taxpayer has never constructed this class of submarine before, the costs incurred in constructing the first submarine (to be delivered in

1983) will be substantially greater than the costs incurred in constructing the second submarine (to be delivered in 1984.) If the agreements are treated as separate contracts, it is estimated that the first contract could result in little or no gain, while the second contract would result in substantial profits. A reasonable business person would not have entered into the agreement to construct the first submarine for the price specified without entering into the agreement to construct the second submarine. In these circumstances, it may be necessary for the Commissioner to aggregate the two agreements for purposes of applying Y's long-term contract method.

Example (3). Assume the same facts as in example (2) with the addition of the following facts: IN 1983, M issues a "change order" providing for a third submarine of the same class to be constructed by Y and delivered to M in 1985. The portion of the total contract price attributable to the "change order" providing for the third submarine can reasonably be determined. A reasonable business person would have entered into the agreements to construct the first two submarines for the price specified without regard to whether M would issue the "change order" for the third submarine. In these circumstances the "change order" providing for the third submarine must be treated as a separate contract for purposes of applying Y's long-term contract method.

Example (4). Z, a calendar year taxpayer engaged in the construction business and using a long-term contract method, enters into an agreement in 1983 to build a ten story office building for the Y Bank. In 1984, the structure is completed and the first three floors of the building are completed and accepted, and Y occupies these floors and uses them for the conduct of its banking business. Construction, however, continues on the remaining seven floors, which are completed and accepted in 1985. In these circumstances, it is clear that even though separate acceptance of portions of the subject matter of the agreement has occurred, the subject matter of the agreement was essentially a single unit, namely a building, and that there was a business purpose for entering into one contract rather than several contracts. Consequently, the agreement ordinarily will not be severed into separate contracts for purposes of applying Z's long-term contract method.

Example (5). The facts are the same as in example (4), except that due to a change in business conditions, Y will not require (either for its own use or for rental) the remaining seven floors for at least two years and, pursuant to a separate agreement entered into in 1984 between the parties, substantially all work on completing the remaining seven floors is stopped. In these circumstances, due to the change in business conditions and the actions of the parties, the original agreement (as modified by the second agreement) is changed into two agreements, each of which is treated as a separate contract for purposes of this section, one contract (entered into in 1983) for the construction of a ten story building with the first three floors completed for occupancy, and a separate contract (or contracts) to finish work on the remaining seven floors on an "as requested" basis.

Example (6). T, a calendar year taxpayer engaged in the business of manufacturing aircraft and related equipment, enters into an agreement in 1982 with the B government to manufacture 10 military aircraft for delivery in 1984. It is anticipated at the time the agreement entered into that B may enter into an agreement with T for the production and sale of as many as 300 of these aircraft over the next 20 years. In negotiating the price for the agreement B and T take into account the expected total cost of manufacturing the 10 aircraft, the risks and the opportunities associated with the agreement, and all other factors that the parties consider relevant, in such a manner that T would have entered into the agreement with the terms agreed upon whether or not T would actually enter into one or more additional production agreements. However, it is unlikely that T would have entered into the agreements but for the expectation that T and B would enter into additional production. In 1984, the 10 aircraft are completed by T and accepted by B. In 1984, T also enters into agreements with B to manufacture 20 aircraft of the same type for delivery in 1986. In negotiating the price for these 20 aircraft, B and T take into account the fact that the expected unit costs for this production of 20 will be different than the unit costs of the 10 aircraft completed in 1984, but also that the expected unit costs of this production of 20 will be substantially higher than the costs of future production. Because the price awarded for each of the two agreements takes into account the expected total costs and the risks expected for each agreement standing alone, the terms agreed upon for any one of of the agreements are independent of the terms agreed upon for the other agreements. Under the facts of this example, the two may not be aggregated, into one contract for purposes of applying T's long-term contract method.

Example (7). R, a calendar year taxpayer engaged in the manufacture of industrial machinery, enters into one agreement in 1982 with Z to manufacture five specialized machines and to manufacture spare and replacement parts for the machines. The machines are to be delivered in 1982 and 1983, and the spare and replacement parts are to be delivered in 1983 through 1985. The portion of the total contract price attributable to the five machines and to the spare and replacement parts reasonably can be determined. The portion of the total contract price reasonably attributable to the spare and replacement parts is more than an insignificant amount of the total contract price. Assume that, under all the facts and circumstances, it is determined that the portion of the agreement attributable to the five machines need not be severed as between the machines. In these circumstances, because the agreement contemplates separate delivery of the machines and the parts, because more than an insignificant amount of the total contract price is allocable to the spare and replacement parts, and because spare or replacement parts are items different than entire machine, it may be necessary for the Commissioner to sever the agreement, treating the agreement to manufacture the five machines as a separate contract and the agreement to manufacture the spare and replacement parts as another separate contract (or as several separate contracts depending on the facts and circumstances) for purposes of applying R's long-term contract method.

(3) *Cross reference.* See §1.6001-1(a) regarding the duty of taxpayers to keep such records as are sufficient to establish the amount of gross income, deductions, etc.

* * * * *

(g) *Effective date and transition to 1983 cost allocation rules; special rules*—(1) *In general.* In the case of a taxpayer using the completed contract method or a method of accounting that uses inventories (other than a long-term contract method), the cost allocation rules prescribed in paragraph (d)(6) of this section (hereinafter "the 1983 cost allocation method") shall apply (with the phase-in described in paragraph (g)(2) of this section) to costs incurred by the taxpayer in taxable years beginning after December 31, 1982, but only with respect to extended period long-term contracts (as defined in paragraph (b)(3) of this section) entered into after December 31, 1982. No costs incurred with respect to any contract entered into before January 1, 1983 are required to be accounted for under the 1983 cost allocation method. Such costs shall be accounted for under the cost allocation method prescribed in paragraph (d)(5) of this section. Because the transition to the 1983 cost allocation method is to be applied on a "cut-off" basis, sections 446(e) and 481 do not apply to the transition to the 1983 cost allocation method.

(2) *Phase-in.* For costs required to be allocated to an extended period long-term contract under the 1983 cost allocation method that are not required to be allocated to the contract under the cost allocation method prescribed in paragraph (d)(5) of this section (or in paragraph (c) of §1.471-11 in the case of a taxpayer accounting for extended period long-term contracts under a method of accounting that uses inventories (other than a long-term contract method)), in lieu of allocating the full amount of such costs to the extended period long-term contract, the taxpayer shall allocate to the contract only the applicable percentage of such costs incurred in taxable years beginning after December 31, 1982 and before January 1, 1986, with respect to extended period long-term contracts entered into after December 31, 1982. The applicable percentage shall be determined as follows:

For taxable years beginning in calendar year	The applicable percentage Is
1983	33 1/2%
1984	66 2/3%
1985 or thereafter	100%

In the case of a taxpayer whose taxable year does not begin on January 1, costs incurred with respect to extended period long-term contracts entered into after December 31, 1982, shall be accounted for under the cost allocation method prescribed in paragraph (d)(5) of this section or paragraph (c) of §1.471-11 in the case of a taxpayer using an inventory method) in the case of costs incurred in taxable years beginning before January 1, 1983, and under the 1983 cost allocation method (with the application of paragraph (g) of this section) in the case of taxable years beginning after December 31, 1982.

(3) *Special rule for completion of certain contracts in taxable years ending before January 1, 1983.* Any contract that would (but for this paragraph (g)(3)) be considered to be completed in a taxable year ending before January 1, 1983, solely by reason of the application of paragraph (b)(2)(i)(B), (ii), (iii) or (iv) of this section, shall be considered to be completed on the first day of the taxpayer's first taxable year ending after December 31, 1982. The application of this paragraph (g)(3) shall not be considered to be a change in method of accounting to which section 481 applies.

(4) *Special rule for severing and aggregating certain contracts in taxable years ending before January 1, 1983.* Any contract of a taxpayer that would (but for this paragraph (g)(4)) be considered completed in a taxable year ending before January 1, 1983—

(i) Solely by reason of the application of those provisions of paragraph (e)(1) of this section expressly made applicable to taxable years ending after December 31, 1982 (hereinafter, the "severing/aggregating modifications") or,

(ii) Solely by reason of the application of both the severing/aggregating modifications and the application of paragraph (b)(2)(i)(B), (ii), (iii) or (iv) of this section (hereinafter, the "completion modifications"), shall be treated as having been completed on the first day after December 31, 1982, on which any contract that was severed from such contract (by reason of the severing/aggregating modifications) is completed (determined with application of the completion modifications). The application of this paragraph (g)(4) shall not be considered to be a change in method of accounting to which section 481 applies.

(5) *Special rule for estimated tax payments.* For purposes of the addition to the tax for underpayment of estimated tax under section 6654 (relating to individuals) and section 6655 (relating to corporations), the gross income realized in the taxpayer's first taxable year ending after December 31, 1982, attributable to long-term contracts deemed to be completed in such taxable year solely by the application of paragraphs(b)(2)(i)(B), (ii), (iii) or (Iv), (g)(3) or (g)(4) of this section, or those portions of paragraph (e)(1) of this section made applicable to taxable years ending after December 31, 1982, shall be considered to be taxable income for such taxable year, but only with respect to installments of estimated tax required to be paid on or after April 13, 1983.

(6) *Taxpayer changing from a method more inclusive of indirect costs.* Except as provided in paragraph (g)(1) and (2) of this section, if a taxpayer wishes to change to a method of accounting for indirect costs prescribed under this section (or under §1.471-11(c) in the case of a taxpayer using an inventory method of accounting for long-term contracts) from a method of accounting for indirect costs that is more inclusive of indirect costs, the taxpayer must secure the consent of the Commissioner prior to making the change in accordance with the regulations and procedures established under section 446(e).

Par. 4. Paragraph (b) of §1.451-5 is revised to read as follows:

§1.451-5 Advance payments for goods and long-term contracts.

* * * * *

(b) *Taxable year of inclusion*—(1) *In general.* Advance payments must be included in income either—

(i) In the taxable year of receipt; or

(ii) Except as provided in paragraph (c) of this section,

(a) In the taxable year in which properly accruable under the taxpayer's method of accounting for tax purposes if such method results in including advance payments in gross receipts no later than the time such advance payments are included in gross receipts for purposes of all of his reports (including consolidated financial statements) to shareholders, partners, beneficiaries, other proprietors, and for credit purposes, or

(b) If the taxpayer's method of accounting for purposes of such reports results in advance payments (or any portion of such payments) being included in gross receipts earlier than for tax purposes, in the taxable year in which includible in gross receipts pursuant to his method of accounting for purposes of such reports.

(2) *Examples.* This paragraph may be illustrated by the following examples:

Example(1). S, a retailer who uses for tax purposes and for purposes of the reports referred to in subparagraph (1)(ii)(a) of this paragraph, an accrual method of accounting under which it accounts for its sales of goods when the goods are shipped, receives advance payments for such goods. Such advance payments must be included in gross receipts for tax purposes either in the taxable year the payments are received or in the taxable year such goods are shipped (except as provided in paragraph (c) of this section).

Example (2). T, a manufacturer of household furniture, is a calendar year taxpayer who uses an accrual method of accounting pursuant to which income is accrued when furniture is shipped for purposes of its financial reports (referred to in subparagraph (1)(ii)*(a)* of this paragraph) and an accrual method of accounting pursuant to which the income is accrued when furniture is delivered and accepted for tax purposes. See §1.446-1(c)(1)(ii). In 1974, T receives an advance payment of $8,000 from X with respect to an order of furniture to be manufactured for X for a total price of $20,000. The furniture is shipped to X in December 1974, but it is not delivered to and accepted by X until January 1975. As a result of this contract, T must include the entire advance payment in its gross income for tax purposes in 1974 pursuant to subparagraph (1)(ii)*(b)* of this paragraph. T must include the remaining $12,000 of the gross contract price in its gross income in 1975 for tax purposes.

(3) *Long-term contracts.* In the case of a taxpayer accounting for advance payments for tax purposes pursuant to a long-term contract method of accounting under §1.451-3, or of a taxpayer accounting for advance payments with respect to a long-term contract pursuant to an accrual method of accounting referred to in the succeeding sentence, advance payments shall be included in income in the taxable year in which properly included in gross receipts pursuant to such method of accounting (without regard to the financial reporting requirement contained in subparagraph (1)(ii)*(a)* or *(b)* of this paragraph). An accrual method of accounting to which the preceding sen-

tence applies shall consist of any method of accounting under which the income is accrued when, and costs are accumulated until, the subject matter of the contract (or, if the subject matter of the contract consists of more than one item, an item) is shipped, delivered, or accepted.

(4) *Installment method.* The financial reporting requirement of subparagraph (1)(ii)*(a)* or *(b)* of this paragraph shall not be construed to prevent the use of the installment method under section 453. See §1.446-1(c)(1)(ii).

* * * * *

Par. 5. Section 1.471-10 is revised to read as follows:

§1.471-10. Applicability of long-term contract methods.

See §1.451-3 for rules providing for the application of the long-term contract methods to certain manufacturing contracts.

Par. 6. Paragraph (c) of §1.471-11 is amended by revising paragraph (c)(1) and (3) to read as follows:

§1.471-11 Inventories of Manufacturers.

* * * * *

(c) *Certain indirect and production costs*—(1) *General rule.* Except as provided in paragraph (c)(3) of this section and in paragraph (d)(6)(v) of §1.451-3, in order to determine whether indirect production costs referred to in paragraph (b) of this section must be included in a taxpayer's computation of the amount of inventoriable costs, three categories of costs have been provided in subparagraph (2) of this paragraph. Costs described in subparagraph (2)(i) of this paragraph must be included in the taxpayer's computation of the amount of inventoriable costs, regardless of their treatment by the taxpayer in his financial reports. Costs described in subparagraph (2)(ii) of this paragraph need not enter into the taxpayer's computation of the amount of inventoriable costs, regardless of their treatment by the taxpayer in his financial reports. Costs described in subparagraph (2)(iii) of this paragraph must be included in or excluded from the taxpayer's computation of the amount of inventoriable costs in accordance with the treatment of such costs by the taxpayer in his financial reports and generally accepted accounting principles. For the treatment of indirect production costs described in subparagraph (2) of this paragraph in the case of a taxpayer who is not using comparable methods of accounting for such costs for tax and financial reporting see paragraph (c)(3) of this section. For contracts entered into after December 31, 1982, notwithstanding this section, taxpayers who use an inventory method of accounting for extended period long-term contracts (as defined in paragraph (b)(3) of §1.451-3) for tax purposes may be required to use the cost allocation rules provided in paragraph (d)(6) of §1.451-3 rather than the cost allocation rules provided in this section. See paragraph (d)(6)(v) of §1.451-3. After a taxpayer has determined which costs must be treated as indirect production costs includible in the computation of the amount of inventoriable costs, such costs must be allocated to a taxpayer's ending inventory in a manner prescribed by paragraph (d) of this section.

* * * * *

(3) *Exception.* Except as provided in paragraph (d)(6) of §1.451-3, in the case of a taxpayer whose method of accounting for production costs in his financial reports is not comparable to his method of accounting for such costs for tax purposes (such as a taxpayer using the prime cost method for purposes of financial reports), the following rules apply:

* * * * *

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved December 20, 1985.

Ronald A. Pearlman,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on December 30, 1985, 3:12 p.m., and published in the issue of the Federal Register for January 6, 1986, 541 F.R. 376).

Section 471.—General Rule for Inventories

26 CFR 1.471-11: Inventories of manufacturers.

Accounting for long-term contracts. See T.D. 8067, page 5.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property.

For below-market demand loans of a fixed principal amount that remains outstanding for the entire calendar year, foregone interest for purposes of section 7872 of the Code is equal to the excess of 9.24 percent of the outstanding principal over any interest payable on the loan properly allocable to 1985. See Rev. Rul. 86-17, page 26.

Section 4121.—Imposition of Tax

26 CFR 48.4121-1: Imposition and rate of tax on coal.
(Also Section 4216; 48.4216(a)-2.)

Coal; sale price determination; freeze conditioning additive. In computing the taxable sale price of coal for purposes of the tax imposed by section 4121 of the Code, a charge for the application of a freeze conditioning additive to the coal is includible.

Rev. Rul. 86-16

ISSUE

In the situation described below, if a coal producer charges a coal purchaser for the application of a freeze conditioning additive to the coal before delivery, is the charge includible in the taxable sale price for purposes of the tax imposed by section 4121 of the Internal Revenue Code?

FACTS

X, a producer of coal, agrees to sell cleaned coal to *Y* f.o.b. *X*'s cleaning plant. Under the terms of the contract, *Y* may request that *X*, for an additional charge per ton, apply to the coal a freeze conditioning additive. Under the agreement, the failure of *X* to add the additive does not cause the coal to become rejectable by *Y*.

Application of the freeze conditioning additive is helpful to *Y* during sustained periods of low temperatures. Since the additive is glycol based, its application to the coal modifies the formation of ice crystals, and thus prevents the coal from sticking together. If the additive were not applied during cold weather, the coal would not unload easily from the bottom of the railroad cars at *Y*'s unloading facility, and more expensive methods would have to be used by *Y* to remove the coal. The additive is applied by *X* as the cleaned coal goes into silos for loading into railroad carts at *X*'s cleaning plant.

LAW AND ANALYSIS

Section 4121(a) of the Code imposes a tax on the producer's sale of coal at the rate of 50 cents per ton for coal from underground mines and 25 cents per ton for coal from surface mines, but in each case section 4121(b) limits the tax to 2 percent of the sale price per ton. Section 4121(e) provides for a temporary increase of the rates for coal sold after December 31, 1981, to one dollar for coal from underground mines and 50 cents for coal from surface mines, with a limit of 4 percent of the sale price per ton.

Section 48.4121-1(d)(4) of the Manufacturers and Retailers Excise Tax Regulations provides that, for purposes of determining both the amount of coal sold by a producer and the sales price of the coal, the point of sale is f.o.b. mine, or f.o.b. cleaning point if the producer cleans the coal before selling it.

Section 4216(a) of the Code provides that in determining, for purposes of section 4121, the price for which an article is sold, there shall be included any charge for coverings and containers of whatever nature, and any charge incident to placing the article in condition packed ready for shipment, but there shall be excluded the amount of tax imposed by section 4121, whether or not stated as a separate charge. A transportation, delivery, insurance, installation, or other charge (not required by the foregoing sentence to be included) shall be excluded from the price only if the amount is established to the satisfaction of the Secretary in accordance with the regulations.

X cleans the coal before delivery. Thus, under section 48.4121-1(d)(4) of the regulations, the tax base for the coal sold is f.o.b. *X*'s cleaning plant. The tax is computed under section 4121(a) of the Code at 50 cents or one dollar per ton (according to whether the coal is from a surface mine or an underground mine), but the tax is limited to no more than four percent of the per ton price charged by *X*.

In this case, *X* sells coal to *Y* at one of two prices: a regular price per ton of coal, and a higher price that includes the per ton charge for the additive when *Y* elects to have *X* apply the freeze conditioning additive. The question is whether, for the purpose of the limitation under section 4121(b), the per ton price includes the charge for the additive. The answer to this question is determined by whether, pursuant to section 4216(a), the charge is excludible as a delivery charge and, if not, whether it is includible as a charge incident to placing the coal in condition ready for shipment.

The freeze conditioning additive is applied before the coal is loaded into railroad cars for transportation to *Y*'s facility. Section 4216(a) of the Code excludes charges for the actual transportation of a completed product to the customer's premises. Section 48.4216(a)-2(b)(1) of the regulations provides that the charges excluded by section 4216(a) "include all items of transportation, delivery, insurance, installation, and similar expense incurred *after shipment to a customer begins*, in response to the customer's order pursuant to a bona fide sale." (Emphasis added.) On the other hand, section 48.4216(a)-2(b)(3) of the regulations provides: "All expenses incurred in placing an article packed, ready for shipment on the loading dock at the manufacturer's factory are not excludible transportation or delivery expenses." The closest analogy to this in the coal industry is the placing of the coal in silos ready for loading onto railroad cars. Thus, a charge for treating coal prior to the loading of the coal onto railroad cars for transportation to the customer's premises is not a transportation or delivery charge, even though the treatment is intended to facilitate the delivery of the coal.

Furthermore, section 4216(a) of the Code expressly includes in the taxable price any charge incident to placing an article in condition packed ready for shipment. Under section 48.4216(a)-(1)(d) of the regulations, this includes charges for any special parking services, such as for extra protection of the article. Accordingly, a charge for a treatment of the coal which is done before the coal is loaded onto the cars and which is part of the preparation of the coal for shipment is includible as a packing charge under section 4216(a).

HOLDING

In computing its taxable sale price for purposes of the tax imposed by section 4121 of the Code, *X* must include the charge for the application of the freeze conditioning additive to the coal.

Section 4216.—Definition of Price

26 CFR 48.4216(a)-2: Exclusions from sale price.

Whether a charge for the application of a freeze conditioning additive to coal before delivery is includible in the taxable sale price for purposes of the tax imposed on the sale of coal by section 4121 of the Code. See Rev. Rul. 86-16, page 24.

Section 4221.—Certain Tax-Free Sales

26 CFR 48.4221-1: Tax-free sales; general rule.

Whether an unregistered manufacturer may make a tax-free sale of an article for further manufacture. See Rev. Rul. 86-18, below.

Section 4222.—Registration

26 CFR 48.4222(a)-1: Registration.
(Also Sections 4221, 4223; 48.4221-1, 48.4223-1.)

Liability of unregistered manufacturer; sale for further manufacture. When a manufacturer that has not registered pursuant to section 4222(a) of the Code makes a sale for further manufacture pursuant to the tax-free sale provisions under section 4221(a)(1), the manufacturer remains liable for the manufacturers excise tax. The manufacturer's vendee does not become the statutory manufacturer of the article under section 4223(a) and may file for a refund or claim a credit for any tax paid on its resale of the article.

Rev. Rul. 86-18

ISSUE

Is a manufacturer of an article subject to manufacturers excise tax under chapter 32 of the Internal Revenue Code liable for tax in the situation described below?

FACTS

X, a manufacturer of an article subject to manufacturers excise tax under chapter 32 of the Code, sold the article for further manufacture without paying the tax thereon. *X* intended the sale to be tax-free pursuant to section 4221(a)(1) of the Code. All the requirements for a tax-free sale were met except that *X* was not registered with the Internal Revenue Service District Director as required by section 4222 and section 48.4222(a)-1 of the Manufacturers and Retailers Excise Tax Regulations. Although at the time of purchase *Y*, the purchaser, intended to use the article in further manufacture, *Y* instead resold the article and paid manufacturers excise tax on its sale pursuant to the provisions of section 4223.

LAW AND ANALYSIS

Section 4221(a)(1) of the Code provides that, under regulations prescribed by the Secretary or his delegate, no tax shall be imposed under Chapter 32 (other than the section 4121 tax on coal) on the sale by the manufacturer of an article for use by the purchaser for further manufacture, or for resale by the purchaser to a second purchaser for use by such second purchaser in further manufacture.

Section 4222(a) of the Code provides, with the exception of the transactions set forth in section 4222(b), which are not here pertinent, that section 4221 shall not apply with respect to the sale of any article unless the manufacturer, the first purchaser, and the second purchaser (if any) are all registered under this section. Registration must be made at such time, in such manner and form, and subject to such terms and conditions, as is prescribed by regulations.

Section 48.4222(a)-1(b) of the regulations provides that any person who is eligible to sell or purchase articles free of a tax imposed by chapter 342 and who has not registered in accordance with the provisions of the regulations shall, prior to making a tax-free sale or purchase, file Form 637, Certificate of Registry, in duplicate, executed in accordance with the instructions contained on the reverse of Form 637. This form shall be filed with the District Director of Internal Revenue for the district in which the principal place of business of the applicant is located (or if the applicant has no principal place of business in the United States, with the Internal Revenue Service Center, Philadelphia, Pennsylvania). The person who receives a validated Form 637 shall be considered to be registered for purposes of selling or purchasing articles tax free.

Section 48.4222(a)-1(d) of the regulations provides that if either the seller or purchaser is not registered as required by section 48.4222(a)-1, tax-free sales may not be made unless the sale is within one of the section 4222(b) exceptions.

Section 4223(a) of the Code provides that for purposes of chapter 32, a manufacturer or producer to whom an article is sold or resold free of tax under section 4221(a)(1) for use in further manufacture shall be treated as the manufacturer or producer of such article.

Under the facts described above, since *X*, the manufacturer, did not comply with the registration requirements prior to the sale of the article to *Y* for further manufacture, *X* is liable for tax on the sale of the article. Since registration must occur prior to sale of an article, registration after the sale will not relieve the manufacturer of liability for the tax. *Y* is not treated as the manufacturer or producer of the article under section 4223(a) of the Code and, therefore, is not liable for tax on its sale because the sale from the manufacturer to the vendee was not a tax-free sale. *Y*, having mistakenly paid tax under section 4223 on its sale of the article, may file for a refund or claim a credit pursuant to the provisions of sections 6401(c) and 6402(a) for the tax *Y* paid on the sale, provided the conditions to allowance set forth in section 6416(a) are met.

HOLDING

If a manufacturer who has not registered pursuant to section 4222(a) of the Code, makes a sale for further manufacture under section 4221(a)(1), the manufacturer remains liable for the manufacturers excise tax. The person to whom the article was sold for further manufacture does not become the statutory manufacturer or producer of the article under section 4223(a) because the unregistered manufacturer's sale to the person was not tax-free.

Section 4223.—Special Rules Relating to Further Manufacture

26 CFR 48.4223-1: Special rules relating to further manufacture.

Whether an unregistered manufacturer may make a tax-free sale of an article for further manufacture. See Rev. Rul. 86-18, page 25.

Section 7872.—Treatment of Loans with Below-Market Interest Rates

(Also Section 1274.)

Forgone interest determination. For purposes of section 7872(e)(2) of the Code, the applicable rate for purposes of determining "foregone interest" on certain below-market loans outstanding from January 1, 1985 to December 31, 1985 is 9.24 percent.

Rev. Rul. 86-17

Section 7872(a)(1) of the Internal Revenue Code provides that in the case of certain below-market loans, an amount known as the foregone interest shall be treated as transferred from the lender to the borrower, and retransferred by the borrower to the lender as interest.

In the case of a demand loan, section 7872(e)(1)(A) of the Code defines the term "below-market loan" to mean any demand loan in which interest is payable on the loan at a rate less than the applicable federal rate.

Section 7872(e)(2) of the Code defines the term "foregone interest" to mean, with respect to any period during a calendar year in which the loan is outstanding, the excess of (A) the amount of interest which would have been payable on the loan for the period if interest accrued on the loan at the applicable federal rate and was payable annually on the last day of such calendar year, over (B) any interest payable on the loan properly allocable to this period. For purposes of this revenue ruling the amount described in section 7872(e)(2)(A) is called the "section 7872(e)(2)(A) amount."

Section 1274(d) of the Code, as amended by section 101(b)(1) of the 1985 imputed interest simplification act (the Act), Pub. L. No. 99-121, 1985-48 I.R.B. 11, provides that the applicable federal short-term, mid-term, and long-term rates shall be determined each month. The applicable federal rates are relevant under several Code provisions, including sections 1274 and 483. These sections relate to certain transactions in which a debt instrument is issued in exchange for property and, when applicable, they generally provide the minimum interest rate that must be stated in the debt instrument in order to avoid having interest imputed for federal income tax purposes at a higher rate than the stated rate.

Prior to the amendment of section 1274(d) by section 101(b)(1) of the Act, the applicable federal rates were determined semiannually, and monthly determinations were computed under the alternate method provided by section 1.1274-6T of the Temporary Income Tax Regulations. The method prescribed by section 1274(d) as amended reflects this prior alternate method. Each month the Internal Revenue Service publishes a revenue ruling containing the applicable federal rates, including a short-term applicable rate based on semiannual compounding.

In the case of a below-market demand loan of a fixed principal amount that remains outstanding for the entire calendar year, the section 7872(e)(2)(A) amount equals the sum of: (1) The product of one-half of the January short-term rate based on semiannual compounding times the principal amount of the loan; and (2) the product of one-half of the July short-term rate based on semiannual compounding times the sum of the principal amount of the loan and the amount described in (1) above.

To allow easier computation of the section 7872(e)(2)(A) amount for loans described in the preceding paragraph, the Internal Revenue Service is publishing in this revenue ruling a "blended annual rate." For these loans, the section 7872(e)(20(A) amount can be computed by multiplying the blended annual rate by the fixed principal amount that remained outstanding for the entire calendar year.

To determine foregone interest on these loans from January 1 through December 31, 1985, the blended annual rate is 9.24 percent. This rate is derived from: (1) The January 1985 short-term rate based on semiannual compounding (9.56 percent), as set forth in Rev. Rul. 85-21, 1985-1 C.B. 286; and (2) the July 1985 short-term rate based on semiannual compounding (8.51 percent), as set forth in Rev. Rul. 85-91, 1985-26 I.R.B. 4.

Therefore, for the period January 1, 1985, through December 31, 1985, in the case of a below-market demand loan of a fixed principal amount that remains outstanding for the entire calendar year, foregone interest for purposes of section 7872 of the Code is equal to the excess of 9.24 percent of the outstanding principal over any interest payable on the loan properly allocable to 1985.

In the future the blended annual rate will be published annually with the applicable federal short-term, mid-term and long-term rates for the month of July.

26 CFR 601.602: Forms and instructions.
(Also Part I, Section 4997; 51.4997-2.)

Rev. Proc. 86-7

PART A—GENERAL

SECTION 1. PURPOSE AND NATURE OF CHANGES

The purpose of this revenue procedure is to update Rev. Proc. 84-81, 1984-2 C.B. 759, concerning the requirements and conditions for filing annual information returns for windfall profit tax on magnetic tape instead of on paper returns. Specifications for filing Form 6248, Annual Information Return of Windfall Profit Tax, are contained in this procedure. For tax year 1985 the following changes have been included in this revenue procedure:

.01 In Part A, Sec. 2, a paragraph has been added to request inclusion of your assigned transmitter control code on any correspondence to the magnetic media coordinator.

.02 Part A, Sec. 10 has been revised to show transfer of magnetic media processing from all service centers to the Internal Revenue Service National Computer Center in Martinsburg, WV, effective JANUARY 1, 1986. References to service center filing and magnetic media coordinators at the service centers have been corrected throughout.

.03 In Part B, Sec. 5, a new paragraph, .03, has been added as follows: "A separate 'G' Record is required for each type of return, e.g., original, corrected, etc."

.04 Part B, Sec. 6, paragraph .01 has been revised to clarify how fields in the Producer/Recipient "H" Record are to be filled.

.05 All requests for ZIP Code information now call for nine digits. Affected records, from Part B, are the Filer/Transmitter "G" Record, positions 118-126 and 284-292; and the Producer/Recipient "H" Record, positions 340-348. If you do not have the nine digit ZIP Code, LEFT JUSTIFY the five digit ZIP Code and fill the remaining four positions with ZEROS. Part B, Sec. 4 has been amended to show that the table provides state abbreviations and ZIP Code ranges.

.06 In Part B, Sec. 6, for the description of Producer ZIP Code in positions 340-348 of the Producer/Recipient "H" Record, a sentence has been added to emphasize the importance of entering the Producer's ZIP Code in this field.

.07 In Part B, Sec. 6, for the description of Number of Barrels of Sadlerochit Oil Removed 70% Rate in positions 725-736 of the Producer/Recipient "H" Record, a final sentence has been added as follows: "Enter in whole barrels, right justified and zero filled."

.08 In Part B, Sec. 7, for the description of Number of 6248s for this Filer in positions 2-7 of the End of Filer "I" Record, a sentence has been added as follows: "This field must be numerically unsigned."

.09 In Part B, Secs. 8 and 9, paragraphs .05 have been added to indicate that all fields in the End of Reel "J" Record, and End of Transmission "K" Record must be numerically unsigned.

.10 There are various editorial changes.

SEC. 2. APPLICATION FOR MAGNETIC MEDIA REPORTING

.01 For the purpose of this revenue procedure only, the first purchasers, filers, and payers are equivalent to each other, and are considered to be the person making the payments. The producer, recipient, or payee is the receiver of the payments. The transmitter is the organization preparing the tape file. Payers or transmitters who decide to file information returns on magnetic tape must complete Form 4419, Application for Magnetic Media Reporting of Information Returns. Instructions for completing the application appear on the reverse side of the form.

.02 The Internal Revenue Service will act on an application and notify the applicant of authorization to file within 30 days of receipt of the application. No magnetic tape returns may be filed with the Service until authorization to file is received.

.03 The Service will assist new filers with their initial magnetic tape submission by reviewing test tapes in advance of the filing season. Approved payers or transmitters who wish to submit test tapes should contact the magnetic media coordinator at the National Computer Center. See Part A, Sec. 10, for the correct address.

.04 Once authorization to file on magnetic tape has been granted to a payer or transmitter, it will remain in effect in succeeding years, provided that all the requirements of this revenue procedure are met and there are no equipment changes by the filer. If a filer discontinues filing on magnetic tape, a new application must be filed before this method of filing may be resumed.

.05 Upon receiving approval to file on magnetic tape, each transmitter will be assigned a unique five character Transmitter Control Code (TCC). This code should be included on any correspondence to the magnetic media coordinator.

SEC. 3. FILING OF TAPE REPORT

.01 A magnetic tape reporting package, which includes all the necessary transmittals, labels, and instructions, will be mailed to all approved filers between October and December of each year.

.02 Payers may submit a portion of their information returns on magnetic tape and the remainder on paper forms provided there is no duplicate filing. A Form 6248-T, Summary and Transmittal of Windfall Profit Tax, must accompany paper submissions and Form 4804, Transmittal of Information Returns Reported on Magnetic Media, must accompany magnetic tape submissions. See Part A, Sec. 10, for information on where to file.

.03 The affidavit which appears on Form 6248-T and Form 4804 must be signed by the payer. However, one of the following, the transmitter, service bureau, or disbursing agent may sign the affidavit on behalf of the payer if three conditions are met. The conditions are that the agent must:

1. have the authority to sign the affidavit under an agency agreement (either oral, written, or implied) that is valid under state law;
2. have the responsibility (either oral, written or implied) conferred on it by the payer to request the taxpayer identification numbers of payees reported on magnetic tape or paper returns; and
3. sign the affidavit and add the cap-

tion "For: (name of payer)".

.04 Although a duly authorized agent signs the affidavit, the payer is held responsible for the accuracy of the Form 4804 and will be liable for penalties for failure to comply with filing requirements.

.05 The preceding requirements also apply to paper filers submitting Form 6248-T. The failure of duly authorized agents of paper filers to comply with filing requirements for Form 6248-T and attachments does not relieve the payers of any penalties that may arise as a result of such failure to comply.

.06 If a portion of the returns is submitted on paper documents, include a statement on the Form 6248-T that the remaining returns are being filed on magnetic tapes. Please note that Form 6248-T instructions normally apply to filing of information returns on paper; however, filers of magnetic tape must review the Form 6248-T instructions and file Form 6248-T if appropriate.

SEC. 4. FILING DATES

.01 Magnetic tape reporting to IRS for Forms 6248 is on a calendar year basis.

.02 The dates prescribed for filing paper returns with the Service will also apply to magnetic tape filing. Tapes must be submitted to the Internal Revenue Service National Computer Center in Martinsburg, WV, by April 30. Copies required to be furnished to the producer or other recipients must be furnished by March 31.

SEC. 5. EXTENSIONS OF TIME TO FILE

.01 If a payer or transmitter is unable to submit the tape file by the April 30 due date, a letter requesting an extension must be filed before April 30. The letter should be sent to the attention of the magnetic media coordinator at the Internal Revenue Service National Computer Center in Martinsburg, WV. The request should include the estimated number of returns which will be filed late, the reason for the delay, and the date by which the returns will be filed.

.02 If an extension is granted by the Service, a copy of the letter granting the extension must be attached to the transmittal Form 4804 when the file is submitted.

SEC. 6. PROCESSING OF TAPE RETURNS

.01 The Service will process tax information from the tapes. Tapes which are timely received by the Service will be returned to the filer within six months of receipt.

.02 All tapes submitted must conform totally to this revenue procedure. If tapes are unprocessable, they will be returned to the filer for correction. Unprocessable tapes must be corrected and returned to the National Computer Center within 45 days of receipt by the filer. Corrected files will be returned by the Service within six months of receipt.

SEC. 7. CORRECTED RETURNS, SUBSTITUTE FORMS AND COMPUTER-GENERATED FORMS

.01 If returns must be corrected or amended, approved magnetic media filers should make every attempt to provide such corrections on tape. The filer must contact the magnetic media coordinator for format and shipping instructions. A corrected Form 4804 must accompany the shipment and be marked "Magnetic Media Correction" on the top margin of the form. Corrected or amended Form 6248 data must be filed in accordance with Rev. Proc. 83-86, 1983-2 C.B. 604.

.02 If corrections are not submitted on tape, payers must submit them on official Forms 6248 (Copy A). Substitute forms that have been previously approved by the Service, or computer-generated forms that are exact facsimilies of the official form (except for minor page size or print style deviations), may be submitted without reobtaining IRS approval before using the form. In all other cases, Service approval must be obtained before a substitute or computer-generated form can be used. Publication 1167, containing specifications for paper returns, is available from most Service offices.

.03 Requests for approval of computer-generated or substitute forms should be sent to the following address with a copy of the proposed form:

Internal Revenue Service
Attn: Substitute Forms Program
Room 7033 D:R:R:I
1111 Constitution Avenue N.W.
Washington, D.C. 20224

.04 Form 6248 instructions are to be followed when paper returns are filed to correct returns submitted on magnetic media. The caption "Magnetic Media Correction" must appear on the top right corner of the form. PAPER CORRECTIONS WILL BE SENT TO THE APPROPRIATE SERVICE CENTER, as prescribed in the instructions for Form 6248-T.

SEC. 8. TAXPAYER IDENTIFICATION NUMBERS

.01 Under Section 6109 of the Internal Revenue Code, recipients of income are required to furnish taxpayer identification numbers (TINs) to the payer whether or not the payee is required to file a tax return.

.02 Payers are expected to keep to a minimum those statements submitted without TINs. It is particularly important that correct social security and employer identification numbers for payees be provided on magnetic media or paper forms submitted to the Service.

.03 For each omission of a required TIN, Section 6676 of the Internal Revenue Code imposes a $50 penalty, unless the payer or payee responsible for furnishing the number establishes reasonable cause for not having done so.

.04 The TIN to be furnished depends primarily upon the manner in which the account is maintained or set up on the record of the payer. The number to be provided must be that of the owner of record. If the account is recorded in more than one name, furnish the TIN and name of one of the holders of record. For those engaged in a trade or business (including employee trusts, retirement systems, etc.) the TIN is the employer identification number (EIN), without hyphens. For individuals, it is a social security number (SSN), without hyphens.

.05 Sole proprietors who are payers should show their employer identification number and/or their social security number in the Filer/Transmitter "G" Record. The tables provided in Part A, Sec. 8.06 will help to determine the number to be furnished to the Service.

.06 Any person required to file an information return that is based, in whole or in part, upon information received from another person MUST include the taxpayer identification number of that person on the return. The tables provided in Part A, Sec. 8.06, will determine the number to be furnished to the Service.

Table 1. Guidelines for Social Security Numbers

If the producer/ recipient is:	In tape positions 2-10 of the Producer/ Recipient "H" Record, enter the SSN of:	In tape positions 20-339 of the Producer/ Recipient "H" Record, enter the name of:
1. An individual	The individual	The individual
2. A joint account of two or more individuals, a husband and wife or adult and minor	The actual or principal owner of the account	The individual whose SSN is entered
3. An account in the name of the guardian or committee for a designated ward, minor, or incompetent person	The ward, minor, or incompetent person	The individual whose SSN is entered
4. A custodian of a minor (Uniform Gifts to Minors Act)	The minor	The minor
5. a. The usual revocable savings trust account (grantor is also trustee)	The grantor-trustee	The grantor-trustee
b. So-called trust account that is not a legal or valid trust under State Law	The actual owner	The actual owner
6. A sole proprietor	The owner	The owner
7. A grantor trust described in section 1.671-4(b) of the Income Tax Regulations	The grantor	The grantor

Table 2. Guidelines for Employer Identification Numbers

If the producer/ recipient is:	In tape positions 11-19 of the Producer/ Recipient "H" Record, enter the EIN of:	In tape positions 20-339 of the Producer/ Recipient "H" Record, enter the name of:
1. A valid trust, estate or pension trust	Legal entity (Do not furnish the identification number of the personal representative or trustee unless the legal entity itself is designated in the account title)	The legal trust, estate or pension trust
2. A corporation	The corporation	The corporation
3. A religious, charitable or educational organization	The organization	The organization
4. A partnership held in the name of the business	The partnership	The partnership
5. An association, club, or other tax-exempt organization	The organization	The organization
6. A broker or registered nominee	The broker or nominee	The broker or nominee
7. An account with the Department of Agriculture in the name of a public entity (such as a state or local government, school district or prison that receives agriculture program payments)	The public entity	The public entity

SEC. 9. EFFECT ON PAPER RETURNS

.01 Magnetic tape reporting of the information return listed in Part A, Sec. 1 applies only to the original (Copy A).

.02 Payers are permitted considerable flexibility in designing the copy of the information return to be furnished to the payee. The payer may combine the information return data with other reports or financial or commercial notices, or expand them to include other information. This is permissible so long as all required information present on the official form is included and that payees' copies are conducive to proper reporting of income on tax returns.

Payers must include the message "This information is being furnished on Form 6248 to the Internal Revenue Service" on the recipients' copies.

.03 If a portion of the returns is reported on magnetic tape and the remainder is reported on paper forms, those returns not submitted on magnetic tape must be filed on official Forms 6248.

SEC. 10. ADDITIONAL INFORMATION

.01 Beginning January 1, 1986, magnetic media processing for all service centers will be centralized at the Internal Revenue Service National Computer Center in Martinsburg, WV. Functions previously performed by the magnetic media coordinators at the service centers will be performed at the National Computer Center.

.02 All magnetic media files forwarded on or after January 1, 1986, (including current reporting, corrected records and test tapes) are to be submitted to the National Computer Center at the address shown below. In addition, all correspondence or contacts regarding magnetic media related forms, publications, information, applications for reporting on magnetic media, and requests for extensions of time to file will be directed to:

Magnetic Media Reporting
Internal Revenue Service
National Computer Center
P.O. Box 1359
Martinsburg, WV 25401-1359

.03 Only MAGNETIC MEDIA reporting is to be submitted to the National Computer Center. ALL PAPER FORMS WILL CONTINUE TO BE SENT TO THE APPROPRIATE INTERNAL REVENUE SERVICE CENTER, AS PRESCRIBED IN THE INSTRUCTIONS FOR FORM 6248-T.

PART B.—MAGNETIC TAPE SPECIFICATIONS

SECTION 1. GENERAL

.01 The magnetic tape specifications contained in this part prescribe the required format and contents of the records to be included in the file. THESE SPECIFICATIONS MUST BE ADHERED TO UNLESS DEVIATIONS HAVE BEEN SPECIFICALLY GRANTED BY THE SERVICE IN WRITING.

.02 In most instances, the Service will be able to process tape files that meet any one set of the following specifications:

(a) 9 track EBCDIC (Extended Binary Coded Decimal Interchange Code) with

(1) Odd Parity and

(2) A density of 800, 1600, or 6250 BPI

(b) 9 track ASCII (American Standard Coded Information Interchange) with

(1) Odd Parity and

(2) A density of 800, 1600, or 6250 BPI

(c) 7 track BCD (Binary Coded Decimal) with

(1) Either Even or Odd Parity and

(2) A density of 556 or 800 BPI

.03 All tape files must have the following characteristics:

(a) Type of tape—1/2 inch Mylar base, oxide coated; and

(b) Interrecord Gap

(1) .75 inch for 556 or 800 BPI density 7 track

(2) .6 inch for 800 or 1600 BPI density 9 track

(3) .3 inch for 6250 BPI density 9 track

.04 Service programs are capable of accommodating some minor deviations. Filers who can substantially conform to these specifications, but do require some minor deviations, must contact the magnetic media coordinator at the INTERNAL REVENUE SERVICE National Computer Center in Martinsburg, WV. UNDER NO CIRCUMSTANCES MAY TAPES DEVIATING FROM THE SPECIFICATIONS IN THIS REVENUE PROCEDURE BE SUBMITTED WITHOUT PRIOR WRITTEN APPROVAL FROM THE SERVICE.

SEC. 2. RECORD LENGTH

.01 The tape records prescribed in these specifications may be blocked or unblocked, subject to the following:

(a) A block must not exceed 14,500 tape positions.

(b) If the use of blocked records would result in a short block, all remaining positions of the block must be filled with 9s. Do not pad a block with blanks.

(c) All records except the Header and Trailer Labels, may be blocked.

.02 All records, other than Header and Trailer records, must be 1450 characters long.

SEC. 3. OPTIONS FOR FILING

.01 For filing convenience, this procedure contains two options for using Header Labels and Filer/Transmitter "G" Records. For purposes of this procedure the following conventions must be used:

Header Label:

1. Payers may use standard headers; however, they must begin with 1HDR, HDR1, HDR2, VOL1 or VOL2.

2. Consist of either 80 or 120 positions each.

Trailer Label:

1. Standard trailer labels may be used; however, they must begin with 1EOR, 1EOF, EOR1, or EOF1.

2. Consist of either 80 or 120 positions each.

Record Mark:

1. Special character used to separate blocked records on tape.

2. Can be written only at the end of a record or block.

3. For odd parity tapes, use BCD bit configuration 011010 ("A82").

Tape Mark:

1. Used to signify the physical end of the recording on tape.

2. Must be even parity, BCD configuration 001111 ("8421").

3. May follow the header label(s) and precede and/or follow the trailer label(s).

Option 1: When using this option, a correct Filer/Transmitter "G" Record, described in Part B, Sec. 5 is to be the first record on each reel. Filers using this option may have Header Labels preceding the "G" Record; however, headers are not required. The reel sequence number must appear in positions 3-5 of each "G" Record and must be incremented by 1 on each tape reel of the file after the first reel.

Option 2: Requires a Header Label as the first record on each reel. The Header Label must contain the reel sequence number and it must be incremented by 1 on each reel. The "G" Record will contain the location of the reel sequence number in the Header Label. If your system generates a four digit reel sequence number, ignore the first digit when determining the location of the reel sequence in the "G"

Record.

Example 1: If your Header Label reel sequence is four digits (e.g., 0001) and is in positions 28-31, enter 29 as the location in positions 3 and 4 of the "G" Record and also enter an "X" in position 5 of the "G" Record.

Example 2: If your Header Label reel sequence number is 3 digits (e.g., 001) and is in positions 10-12, enter 10 as the location in positions 3 and 4 of the "G" Record. This option requires a Trailer Label at the end of each reel. Also, ignore the "J" Record instructions in this part if you use option 2.

SEC. 4. STANDARD STATE ABBREVIATIONS AND ZIP CODE RANGES

The following table gives the list of valid state abbreviations and ZIP Code ranges to be used in the "G" and (in the case of ZIP Codes) "H" records. Although the ZIP Code ranges are provided in the five digit format, the actual ZIP Codes should be in the nine digit format. The valid abbreviations for the U.S. territories American Samoa, Guam, Puerto Rico and the Virgin Islands are also included. If the producer lives in a foreign country, then a period followed by a blank (".ƀ") should be entered in the two position state field and blanks should be entered for ZIP Code. The table lists the only valid data entries for state information.

Table 3. STATE ABBREVIATIONS and ZIP CODE RANGES

Alabama	AL	350nn-369nn	Montana	MT	590nn-599nn
Alaska	AK	995nn-999nn	Nebraska	NE	680nn-693nn
American Samoa	AS	(Blank)	Nevada	NV	890nn-898nn
Arizona	AZ	850nn-865nn	New Hampshire	NH	030nn-038nn, 04037
Arkansas	AR	716nn-729nn, 75501	New Jersey	NJ	070nn-089nn
California	CA	900nn-966nn	New Mexico	NM	870nn-884nn
Colorado	CO	800nn-816nn	New York	NY	090nn-098nn, 100nn-149nn
Connecticut	CT	060nn-069nn, 02891, 10573	North Carolina	NC	270nn-289nn
Delaware	DE	197nn-199nn	North Dakota	ND	580nn-588nn
Dist. of Columbia	DC	200nn-205nn	Ohio	OH	430nn-458nn
Florida	FL	320nn-340nn	Oklahoma	OK	730nn-749nn
Georgia	GA	300nn-319nn, 37347	Oregon	OR	970nn-979nn
Guam	GU	969nn	Pennsylvania	PA	150nn-196nn
Hawaii	HI	967nn-968nn	Puerto Rico	PR	006nn-009nn
Idaho	ID	832nn-838nn	Rhode Island	RI	028nn-029nn, 02701
Illinois	IL	600nn-606nn, 609nn-629nn	South Carolina	SC	290nn-299nn
Indiana	IN	460nn-479nn	South Dakota	SD	570nn-577nn
Iowa	IA	500nn-528nn	Tennessee	TN	370nn-385nn, 35740, 42041
Kansas	KS	660nn-679nn	Texas	TX	750nn-799nn, 73949, 88021
Kentucky	KY	400nn-427nn, 45275	Utah	UT	840nn-847nn
Louisiana	LA	700nn-714nn, 71749	Vermont	VT	050nn-059nn
Maine	ME	039nn-049nn, 03801	Virginia	VA	220nn-246nn, 203nn
Maryland	MD	206nn-219nn, 203nn	Virgin Islands	VI	008nn
Massachusetts	MA	010nn-027nn	Washington	WA	980nn-994nn
Michigan	MI	480nn-499nn, 55617	West Virginia	WV	247nn-268nn
Minnesota	MN	550nn-567nn	Wisconsin	WI	530nn-549nn, 49936
Mississippi	MS	386nn-397nn	Wyoming	WY	820nn-831nn
Missouri	MO	630nn-658nn	Foreign City	.ƀ	Blank

FOOTNOTES: "n" denotes any numeric digit; "ƀ" denotes a blank

SEC. 5. FILER/TRANSMITTER "G" RECORD

.01 This record identifies the filer and the transmitter of the tape file and provides parameters for the processing of the succeeding records. Internal Revenue Service computer programs rely on the parameters supplied in this record in the processing of the tape file.

.02 The number of "G" Records appearing on a tape reel will depend on the number of filers for whom data is present. A transmitter may include Producer/Recipient "H" Records for more than one filer on a tape reel, however, each series of separate Producer/Recipient "H" Record(s) must be preceded by a "G" Record. All "G" Records must be 1,450 characters in length.

.03 A separate "G" Record is required for each type of return, e.g., original, corrected, etc.

RECORD NAME: FILER/TRANSMITTER "G" RECORD

Tape Position	Field Title	Length	Description and Remarks
1	Record Type	1	Enter "G".
2	Filing Year	1	Must be the rightmost digit of the year for which WPT data is being reported (e.g., if data is for 1985 enter a 5). This number must be incremented each year.
3-5	Reel Sequence Number	3	Sequential number of the reel within the tape file upon which this record appears (see explanation of Option 1 and Option 2 filing). Position 5 must contain an X if you are using option 2.
6-9	"G" Record Length	4	Enter 1450.
10-13	"H" Record Length	4	Enter 1450.
14-17	"I" Record Length	4	Enter 1450
18	Type of Account Filer's TIN	1	This field is used to identify the data in tape positions 19-27 as either an EIN (employer identification number) or an SSN (social security number). Use one of the following codes as appropriate. 0 Use the digit 0 if the number provided is an SSN. 1 Use the digit 1 if the number provided is an EIN. 2 Use the digit 2 if it is not known if the number provided is an SSN or EIN. 3 Use the digit 3 if no number is provided (positions 19-27 should be blank filled in this case).
19-27	Filer's Taxpayer Identification Number	9	Enter the taxpayer identification number of the filer (SSN or EIN as appropriate). If no TIN is provided leave blank.
28-67	Filer's Name	40	Enter the name of the filer as used in normal business. Abbreviate any extraneous data other than the name as necessary. Left justify and blank fill.
68-102	Filer's Street Address	35	Enter the street address of the filer. Left justify and blank fill.
103-115	Filer's City	13	Enter the city of the filer. Left justify and blank fill.
116-117	Filer's State	2	Enter the two digit abbreviation of the filer's state. (See Table of Valid State Abbreviations in Part B, Sec. 4.)
118-126	Filer's ZIP	9	Enter the nine digit ZIP Code of the filer. If ZIP Code of the filer is not known this field must be blank. If you do not have the nine digit ZIP Code, LEFT JUSTIFY the five digit ZIP Code and fill the remaining four positions with ZEROS. (See also the ZIP Code ranges by State in the Table in Part B, Sec. 4.)
127	Type of Filing Indicator	1	Enter a zero ("0") if the documents being filed are original returns. Enter "1" if the documents are corrected returns (adjustments to previously supplied returns). Enter "2" if the documents are "Corrected Suspense Accounts" (proceeds are released from suspense). Enter "3" if the documents are "Suspense Accounts" (proceeds being held in suspense).

RECORD NAME: FILER/TRANSMITTER "G" RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
128-178	Reserved	51	Reserved for Service use. Enter blanks.
179-183	Transmitter Control Code	5	Enter the 5 digit transmitter control code assigned by the Service.
184	Transmitter Code	1	If the filer of these Forms 6248 and the transmitter are the same, enter the digit "0" in this location and blank fill the rest of the record.. If they are not the same, enter the digit "1" and supply the information indicated for the remainder of the record.
185-193	Reserved	9	Reserved for Service use. Blank fill.
194-233	Transmitter's Name[1]	40	Enter the name of the transmitter. Left justify and blank fill.
234-268	Transmitter's Street Address[1]	35	Enter the street address of the transmitter. Left justify and blank fill.
269-281	Transmitter's City[1]	13	Enter city of transmitter. Left justify and blank fill.
282-283	Transmitter's State[1]	2	Enter abbreviation of state of transmitter.
284-292	Transmitter's ZIP Code[1]	9	Enter the nine digit ZIP Code of transmitter. If you do not have the nine digit ZIP Code, LEFT JUSTIFY the five digit ZIP Code and fill the remaining four positions with ZEROS.
293-1450	Reserved	1158	Reserved for Service use. Blank fill.

[1] If file is being transmitted by filer, then the Transmitter Name, Street Address, City, State and Zip Code can be blank filled.

SEC. 6. PRODUCER/RECIPIENT "H" RECORD

.01 This record is used to provide the information contained in Parts I, II, III, IV, and V of Form 6248. All "H" Records must be of the same fixed length. Records may be blocked or unblocked. A block may not exceed 14,500 positions. Do not pad unused blocks with blank records, fill with 9s. Zero fill any barrel or liability field for which data is not present. Right justify and zero fill any barrel or liability field for which data is present. Blank fill any other field for which data is not present.

.02 Each field must contain data (dollars, barrels, etc.) covering only the interest of the producer/recipient for whom the Form 6248 is prepared.

.03 All amount fields in this section should be expressed in whole dollars without decimals. All quantities of oil should be expressed in whole barrels without decimals or fractions.

.04 Amount fields and barrel fields may be signed or unsigned. Unsigned fields will always be considered positive. If signed decimal data is used, the rightmost (units) position of the field must be used to carry the sign of the field (negative or positive) as an overpunch character. This is the *only* format permissible for the entry of signed decimal data. If your computer system cannot conform to this standard, or if you have any questions about entering data in this format, please contact the magnetic media coordinator at the National Computer Center.

.05 All "H" Records must be 1450 characters long.

RECORD NAME: PRODUCER/RECIPIENT "H" RECORD

Tape Position	Field Title	Length	Description and Remarks
1	Record Type	1	Enter "H".
2-10	Producer's SSN	9	Enter social security number of Producer, without hyphens, if available. Otherwise, blank fill.

RECORD NAME: PRODUCER/RECIPIENT "H" RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
11-19	Producer's EIN	9	Enter employer identification number of Producer, without hyphens, if available. Otherwise, blank fill.
NOTE:	The following 8 fields are for the Producer Name/Address information. If your name/address fields contain less than 40 characters, do not pack information from more than one of your name/address fields into any one of the following name/address fields. If your name/address fields are longer than 40 characters each, contact the magnetic media coordinator at the National Computer Center for instructions on entering the data. You are encouraged to use the 2 character state abbreviations. Valid characters for these name lines are: Alphabetic, Numeric, Blanks, "&", "-", "/", "%", commas, and periods.		
20-59	Producer's 1st Name/Address Line	40	Enter data from your first Name/Address field for this Producer.
60-99	Producer's 2nd Name/Address Line	40	Enter data from your second Name/Address field for this Producer.
100-139	Producer's 3rd Name/Address Line	40	Enter data from your third Name/Address field for this Producer. If no data is present, enter blanks.
140-179	Producer's 4th Name/Address Line	40	Enter data from your fourth Name/Address field for this producer. If no data is present, enter blanks.
180-219	Producer's 5th Name/Address Line	40	Enter data from your fifth Name/Address field for this Producer. If no data is present, enter blanks.
220-259	Producer's 6th Name/Address Line	40	Enter data from your sixth Name/Address field for this Producer. If no data is present, enter blanks.
260-299	Producer's 7th Name/Address Line	40	Enter data from your seventh Name/Address field for this Producer. If no data is present, enter blanks.
300-339	Producer's 8th Name/Address Line	40	Enter data from your eighth Name/Address field for this Producer. If no data is present, enter blanks.
340-348	Producer ZIP Code	9	Enter the nine digit ZIP Code of the Producer. If you do not have the nine digit ZIP Code LEFT JUSTIFY the five digit ZIP Code and fill the remaining four positions with ZEROS. (See Part B, Sec. 4). THE PRODUCER/RECIPIENT ZIP CODE MUST BE ENTERED HERE EVEN IF YOU PROVIDED IT IN ONE OF THE ABOVE NAME/ADDRESS LINES.
349-351	Type of Producer	3	Use up to 3 of the codes below to indicate the Type of Producer. YOU MUST USE AT LEAST ONE OF THE CODES. LEFT JUSTIFY AND BLANK FILL. *Type of Producer* — *Code* (Unable to determine) — 0 Individual — 1 Partnership — 2 Corporation — 3 Estate — 4 Trust — 5 US Citizen or Entity, or Resident Alien — 6 Resident of US Possession — 7 Foreign Citizen or Non-Resident Alien — 8
352-354	Producer Status	3	Use up to 3 of the following codes to indicate the status of the producer. YOU MUST USE AT LEAST ONE CODE. LEFT JUSTIFY AND BLANK FILL.

RECORD NAME: PRODUCER/RECIPIENT "H" RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
			Producer Status *Code* (Unable to determine) 0 Independent Producer 1 Member of "related group" 2 Producer with no withholding 3 Royalty Owner 4 Integrated Oil Company 5 Operator 6 Working Interest 7 Trust Beneficiary 8
355-364	Exempt Tier One	10	Enter the number of barrels of Exempt Tier One Oil. Enter in whole barrels, right justified and zero filled.
365-374	Exempt Tier Two	10	Enter the number of barrels of Exempt Tier Two Oil (*not* to include Exempt Stripper Well Oil). Enter in whole barrels, right justified and zero filled.
375-384	Exempt Newly Discovered	10	Enter the number of barrels of Exempt Newly Discovered Oil. Enter in whole barrels, right justified and zero filled.
385-394	Exempt Incremental Tertiary	10	Enter the number of barrels of Exempt Incremental Tertiary Oil. Enter in whole barrels, right justified and zero filled.
395-404	Exempt Heavy	10	Enter the number of barrels of Exempt Heavy Oil. Enter in whole barrels, right justified and zero filled.
405-414	Total Exempt Barrels	10	Enter the total number of barrels of exempt oil. Enter in whole barrels, right justified and zero filled.
415-419	Type of Exempt Oil	5	Use up to 4 of the following codes to indicate the type of exempt oil. Left justify and blank fill. *Type of Exempt Oil* *Code* Qualified Governmental Interests 1 Qualified Charitable Interests 2 Exempt Indian Oil 3 Exempt Alaskan Oil 4
420-429	Qualified Royalty 1st Quarter	10	Enter the number of certified barrels of Qualified Royalty Owner Oil removed in the first calendar quarter. Enter in whole barrels, right justified and zero filled.
430-439	Qualified Royalty 2nd Quarter	10	Enter the number of certified barrels of Qualified Royalty Owner Oil removed in the second calendar quarter. Enter in whole barrels, right justified and zero filled.
440-449	Qualified Royalty 3rd Quarter	10	Enter the number of certified barrels of Qualified Royalty Owner Oil removed in the third calendar quarter. Enter in whole barrels, right justified and zero filled.
450-459	Qualified Royalty 4th Quarter	10	Enter the number of certified barrels of Qualified Royalty Owner Oil removed in the fourth calendar quarter. Enter in whole barrels, right justified and zero filled.
460-469	Total Qualified Royalty	10	Enter the total number of certified barrels of Qualified Royalty Owner Oil. Enter in whole barrels, right justified and zero filled.

RECORD NAME: PRODUCER/RECIPIENT "H" RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
470-604	Reserved	135	Reserved for Service use. Blank fill.
605-616	Number of Barrels Other Oil Removed 70% Rate	12	Enter the number of taxable barrels of Tier One Oil other than Sadlerochit Oil, subject to the 70% tax rate, removed during the tax year. Enter in whole barrels, right justified and zero filled.
617-628	Exempt Stripper Well Oil	12	Enter the total number of barrels of Exempt Stripper Well Oil. Enter in whole barrels, right justified and zero filled.
629-652	Reserved	24	Reserved for Service use. Blank fill.
653-664	Tax Liability Other Oil Removed 70% Rate	12	Enter the tax liability for Tier One Oil other than Sadlerochit Oil, subject to the 70% tax rate, removed during the tax year. Enter in dollars only, right justified and zero filled.
665-676	Number of Barrels Other Oil Removed 50% Rate	12	Enter the number of taxable barrels of Tier One Oil other than Sadlerochit Oil, subject to the 50% tax rate, removed during the tax year. Enter in whole barrels, right justified and zero filled.
677-712	Reserved	36	Reserved for Service use. Blank fill.
713-724	Tax Liability Other Oil Removed 50% Rate	12	Enter the tax liability for Tier One Oil other than Sadlerochit Oil, subject to the 50% tax rate, removed during the tax year. Enter in dollars only, right justified and zero filled.
725-736	Number of Barrels Sadlerochit Oil Removed 70% Rate	12	Enter the number of taxable barrels of Tier One Sadlerochit Oil, subject to the 70% tax rate, removed during the tax year. Enter in whole barrels, right justified and zero filled.
737-772	Reserved	36	Reserved for Service use. Blank fill.
773-784	Tax Liability Sadlerochit Oil Removed 70% Rate	12	Enter the tax liability for Tier One Sadlerochit Oil, subject to the 70% tax rate, removed during the tax year. Enter in dollars only, right justified and zero filled.
785-796	Number of Barrels Sadlerochit Oil Removed 50% Rate	12	Enter the number of taxable barrels of Tier One Sadlerochit Oil, subject to the 50% tax rate, removed during the tax year. Enter in whole barrels, right justified and zero filled.
797-832	Reserved	36	Reserved for Service use. Blank fill.
833-844	Tax Liability Sadlerochit Oil Removed 50% Rate	12	Enter the tax liability for Tier One Sadlerochit Oil, subject to the 50% tax rate, removed during the tax year. Enter in dollars only, right justified and zero filled.
845-856	Number of Barrels Tier Two Oil 60% Rate	12	Enter the number of taxable barrels of Tier Two Oil subject to a 60% tax rate, removed this tax year. Enter in whole barrels, right justified and zero filled.
857-892	Reserved	36	Reserved for Service use. Blank fill.
893-904	Tax Liability Tier Two Oil 60% Rate	12	Enter the tax liability for the Tier Two Oil, subject to a 60% tax rate, removed this tax year. Enter in dollars only, right justified and zero filled.

RECORD NAME: PRODUCER/RECIPIENT "H" RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
905-916	Number of Barrels Tier Two Oil 30% Rate	12	Enter the number of taxable barrels of Tier Two Oil, subject to a 30% tax rate, removed this tax year. Enter in whole barrels, right justified and zero filled.
917-952	Reserved	36	Reserved for Service use. Blank fill.
953-964	Tax Liability Tier Two Oil 30% Rate	12	Enter the tax liability for the Tier Two Oil, subject to a 30% tax rate, removed this tax year. Enter in dollars only, right justified and zero filled.
965-976	Number of Barrels Newly Discovered Oil 22 1/2% Rate	12	Enter the number of taxable barrels of Newly Discovered Oil, taxed at the 22 1/2% rate, removed this tax year. Enter in whole barrels, right justified and zero filled.
977-1012	Reserved	36	Reserved for Service use. Blank fill.
1013-1024	Tax Liability Newly Discovered Oil 22 1/2% Rate	12	Enter the tax liability for the Newly Discovered Oil, taxed at the 22 1/2% rate, removed this tax year. Enter in dollars only, right justified and zero filled.
1025-1036	Number of Barrels Incremental Oil 30% Rate	12	Enter the number of taxable barrels of Incremental Tertiary Oil, taxed at the 30% rate, removed this tax year. Enter in whole barrels, right justified and zero filled.
1037-1072	Reserved	36	Reserved for Service use. Blank fill.
1073-1084	Tax Liability Incremental Oil 30% Rate	12	Enter the tax liability for the Incremental Tertiary Oil, taxed at the 30% rate, removed this tax year. Enter in dollars only, right justified and zero filled.
1085-1096	Number of Barrels Heavy Oil 30% Rate	12	Enter the number of taxable barrels of Heavy Oil, taxed at the 30% rate, removed this tax year. Enter in whole barrels, right justified and zero filled.
1097-1132	Reserved	36	Reserved for Service use. Blank fill.
1133-1144	Tax Liability Heavy Oil 30% Rate	12	Enter the tax liability for the Heavy Oil, taxed at the 30% rate, removed this tax year. Enter in dollars only, right justified and zero filled.
1145-1156	Total Taxable Barrels	12	Enter the total number of taxable barrels of oil removed this tax year for all classes of taxable crude oil. Enter in whole barrels, right justified and zero filled.
1157-1168	Total Tax Liability	12	Enter the total tax liability for all oil, removed this tax year. Enter in dollars only, right justified and zero filled.
1169-1180	Tax Withheld Oil Removed This Tax Year	12	Enter the amount of windfall profit tax withheld with respect to oil removed during the tax year. Enter in dollars only, right justified and zero filled.
1181-1192	Underwithheld Tax	12	Enter the amount of windfall profit tax underwithheld, if any. Enter in dollars only, right justified and zero filled. If no underwithholding, zero fill this field.
1193-1204	Overwithheld Tax	12	Enter the amount of windfall profit tax overwithheld, if any. Enter in dollars only, right justified and zero filled. If no overwithholding, zero fill this field.

RECORD NAME: PRODUCER/RECIPIENT "H" RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
1205-1216	WPT Withheld From Payments	12	Enter the amount of windfall profit tax withheld from payments made during this tax year, regardless of when the liability for the tax arose. Enter in dollars only, right justified and zero filled.
1217-1219	Originator(s) of 1st Form 6248 Indicator	3	Enter the total number of originators for this form. Right justify and zero fill. If none, zero fill.
1220-1259	Originator's Name (Person furnishing Form 6248 information to payer/filer/first purchaser)	40	If the information on this Form 6248 is based on information from another Form 6248, enter the name of the person who furnished you with Form 6248. Left justify and blank fill. If not present, blank fill.
1260-1268	Originator's TIN	9	If available, enter the TIN of the originator. If no data is available, blank fill.
1269-1308	Second Originator's Name	40	If the information on this Form 6248 is based on information compiled from two or more Forms 6248, enter the name of the second person who furnished you with a Form 6248. If not present, blank fill.
1309-1317	Second Originator's TIN	9	If available, enter the TIN of the second originator. If no data is available, blank fill.
1318-1357	Third Originator's Name	40	If the information on this form is based on information compiled from three or more Forms 6248, enter the name of the third person who furnished you with a form 6248. If not relevant, blank fill.
1358-1366	Third Originator's TIN	9	If available, enter the TIN of the third originator. If no data is available, blank fill.
1367-1372	Preparation Date	6	Enter the date of preparation of this form. If unknown, blank fill.
1373-1382	Owners I.D.	10	Enter up to 10 characters of your account number for the owner/producer. If no data, blank fill.
1383-1450	Reserved	68	Reserved for Service use. Blank fill.

SEC. 7. END OF FILER "I" RECORD

.01 The End of Filer "I" Record is a summary record for a given filer. This record must be 1450 characters long.

.02 The "I" Record will contain the number of documents transmitted for each individual filer. The "I" Record must be written after the last Producer "H" Record for each filer. For each "G" Record on the file there must be a corresponding "I" Record.

.03 The "I" Record cannot be followed by a Tape Mark.

RECORD NAME: END OF FILER "I" RECORD

Tape Position	Field Title	Length	Description and Remarks
1	Record Type	1	Enter "I".
2-7	Number of 6248s for This Filer	6	Enter the number of "H" Records for this filer. This number should also be shown on Form 4804, Box 13. Right justify, zero fill. This field must be unsigned.

RECORD NAME: END OF FILER "I" RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
8-47	Filer's Name	40	Enter the name of the filer. Use the same name as shown on the Filer/Transmitter "G" Record. Left justify, blank fill.
48	Type of Account Filer's TIN	1	This position is used to identify the data in tape positions 49 thru 57 as either an EIN or SSN. Use one of the following codes as appropriate. 0 use the digit "0" if the number provided is an SSN. 1 use the digit "1" if the number provided is an EIN. 2 use the digit "2" if it is not known whether the number provided is an SSN or EIN. 3 use the digit "3" if no number is provided (positions 49-57 should be blank filled in this case).
49-57	Filer's Account Number	9	Enter the taxpayer identification number of the filer (SSN or EIN as appropriate). If no TIN is provided, leave blank.
58-69	Filer's Total Tax Liability	12	Enter the sum of the filer's total tax liability. This amount should be shown on Form 4804, Box 16, Total Payment Amount for each filer. This field may be signed or unsigned decimal data, in dollars only.
70-1450	Reserved	1381	Reserved for Service use. Blank fill to end of record.

SEC. 8. END OF REEL "J" RECORD

.01 The End of Reel "J" Record will be present for option 1 only. It must be 1450 characters long.

.02 Write this record when the end of the normal writing area of the reel has been reached, but all the records of the file have not been written. This record indicates that there are additional reels in the file.

.03 Each "J" Record must contain a count of Forms 6248 reported on all "H" Records not summarized in the preceding "I" Record on the Reel.

.04 If you do not wish to use a "J" Record, or your system is unable to generate it, you may delete it; however, the last "H" Record on the tape 'MUST' be followed by a Tape Mark.

.05 All fields in this record must be unsigned.

RECORD NAME: END OF REEL "J" RECORD

Tape Position	Field Title	Length	Description and Remarks
1	Record Type	1	Enter "J".
2-7	Number of 6248s	6	Enter the number of "H" Records not summarized in a previous "I" Record. Right justify, zero fill.
8-30	Reserved	23	Zero fill.
31-1450	Reserved	1420	Reserved for Service use. Blank fill.

SEC. 9. END OF TRANSMISSION "K" RECORD

.01 The End of Transmission "K" Record is a summary of the number of filers and the number of tapes in the entire file.

.02 This record should be written after the last "I" Record in the file.

.03 Only a Tape Mark or a Tape Mark and Trailer Labels may follow the "K" Record.

.04 The "K" Record must be 1450 characters long.

.05 All fields in this record must be unsigned.

RECORD NAME: END OF TRANSMISSION "K" RECORD

Tape Position	Field Title	Length	Description and Remarks
1	Record Type	1	Enter "K".
2-5	Number of Filers	4	Enter the number of filers in the transmission. Right justify and zero fill.
6-8	Number of Tapes	3	Enter the total number of tapes in the transmission. Right justify and zero fill.
9-30	Reserved	22	Enter zeros.
31-1450	Reserved	1420	Enter blanks.

SEC. 10. TAPE LAYOUTS—OPTION 1

(Reel Sequence Number is in the "G" Record)

The following chart shows, by type of file, the record types to be used in the first two and the last three records to be written on a tape.

Type of File	First record type	Second record type	Second from last record type	Next to last record type	Last record type
Single Filer, single reels	G	H	H	I	K
Single Filer, multiple reels:					
Reel 1	G	H	H	H	J(TM)[1]
Last Reel	G	H	H	I[2]	K
Multiple Filers, single reel:					
First Filer	G	H	H	H	I
Subsequent Filers	G	H	H	H	I
Final Filer	G	H	H	I	K
Multiple Filers, Multiple Reels: First filer's records split between reel 1 and reel 2; second filer's records split between reel 2 and reel 3:					
Reel 1:					
Filer 1	G	H	H	H	J(TM)[1]
Reel 2:					
Filer 1	G	H	H	H	I[2]
Filer 2	G	H	H	H	J(TM)[1]
Reel 3:					
Filer 2	G	H	H	H	I[2]
Filer 3	G	H	H	H	I
Reel 4: Last Filer	G	H	H	I	K
Multiple Filers, single transmitter, separate files for each filer:					
File 1: Filer 1: Last reel	G	H	H	I	K
File 2: Filer 2:					
Reel 1	G	H	H	H	J(TM)[1]
Last Reel	G	H	H	I[2]	K
File 3: Filer 3: Last reel	G	H	H	I	K

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[1] If your system cannot produce the End of Reel "J" Record, the final "H" Record on an intermediate reel can be followed by a Tape Mark.

[2] Must contain the "Number of 6248s" summarizing all "H" Records on this and previous reels for this filer, not summarized on a previous "I" record.

SEC. 11. TAPE LAYOUTS— OPTION 2

(Reel Sequence Number is in the Header Label)

Where the Header Label is the first record, the following chart shows, by type of file, the record types to be used in the 2nd and 3rd records, where the header label is the first record, and the last three records written on a tape reel prior to the Trailer label.

Type of File	Second record type	Third record type	Second from last record type	Next to last record type	Last record type
Single Filer, single reel	G	H	H	I	K
Single Filer, multiple reels:					
First Reel	G	H	H	H	H
Last Reel	H	H	H	I[1]	K
Multiple Filers, single reel:					
First Filer	G	H	H	H	I
Subsequent Filers	G	H	H	H	I
Final Filer	G	H	H	I	K
Multiple Filers, Multiple Reels: first filer's records split between reel 1 and reel 2; second filer's records split between reel 2 and reel 3:					
Reel 1:					
Filer 1	G	H	H	H	H
Reel 2:					
Filer 1	H	H	H	H	I[1]
Filer 2	G	H	H	H	H
Reel 3					
Filer 2	H	H	H	H	I[1]
Filer 3	G	H	H	H	I
Reel 4:					
Filer 4	G	H	H	I	K
Multiple filers, single transmitter, separate files for each filer:					
File 1: Filer 1: Last reel (could be multiple reel)	H	H	H	I[1]	K
File 2: Filer 2:					
Reel 1	G	H	H	H	H
Last Reel	H	H	H	I[1]	K

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[1] Must contain the "Number of 6248's" summarizing all "H" Records on this and previous reels for this filer not summarized in a previous "I" record.

SEC. 12. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 84-81 is superseded.

Form **6248**
Department of the Treasury
Internal Revenue Service

Annual Information Return of Windfall Profit Tax—1985

OMB No. 1545-0224
Copy A—File with the IRS

Producer or Other Recipient
Name, address, and ZIP code

Filer
Name, address, and ZIP code

Employer identification no. (EIN)	**Social security no., if no EIN**	**Employer identification no. (EIN)**	**Social security no., if no EIN**

If you have received a Form 6248 from another person concerning oil reported on this Form 6248, enter the name and employer identification number of that person below.

Name

Employer identification number

Type of return (Check only one box): Original ☐ Corrected 2 ☐ Suspense 3 ☐ Corrected suspense 4 ☐

For IRS use ☐ ☐

Part I Producer or Other Recipient

1 Type of Producer (check all applicable boxes):
Individual 1 ☐ Partnership 2 ☐ Trust 3 ☐ Estate 4 ☐ Corporation 5 ☐ Resident of U.S. Possessions 6 ☐ U.S. citizen or entity, or resident alien 7 ☐ Foreign citizen or entity, or non-resident alien 8 ☐

2 Producer Status (check all applicable boxes):
Independent producer 1 ☐ Integrated oil company 2 ☐ Member of "related group" 3 ☐ Producer–no withholding 4 ☐ Royalty owner 5 ☐ Working interest 6 ☐ Trust beneficary 7 ☐ Operator 8 ☐

Part II Exempt Oil

		a. Tier one	b. Tier two	c. Tier three (1) Newly discovered	c. Tier three (2) Incremental tertiary	c. Tier three (3) Heavy
1 Number of barrels of exempt oil (do not include exempt stripper well oil or exempt royalty owner oil)	1					
2 Total (add amounts on line 1, columns a through c(3))					2	

3 Type of exempt oil (check applicable boxes): Governmental interests 1 ☐ Exempt Indian oil 2 ☐ Charitable interests 3 ☐ Exempt Alaskan oil 4 ☐

4 Total barrels of exempt stripper well oil (see instructions)	4	

Part III Exempt Royalty Owner Oil

Total number of certified barrels		a. 1st quarter	b. 2nd quarter	c. 3rd quarter	d. 4th quarter
1 Barrels removed in calendar quarter	1				
2 Total (add amounts on line 1, columns a through d)				2	

Part IV Taxable Crude Oil Removed During 1985

		a. Number of barrels	b. Tax liability
1 Tier one, other than Sadlerochit oil, taxed at 70%	1		
2 Tier one, other than Sadlerochit oil, taxed at 50%	2		
3 Tier one Sadlerochit oil taxed at 70%	3		
4 Tier one Sadlerochit oil taxed at 50%	4		
5 Tier two oil taxed at 60%	5		
6 Tier two oil taxed at 30%	6		
7 Newly discovered oil	7		
8 Incremental tertiary oil	8		
9 Heavy oil	9		
10 Total barrels of oil (add amounts in column a)	10		▨

11 Amount of windfall profit tax liability for oil removed during 1985 (add amounts in column b)	11	
12 Amount of windfall profit tax withheld with respect to oil removed during 1985	12	
13 If line 11 is greater than line 12, subtract line 12 from line 11. This is underwithheld windfall profit tax	13	
14 If line 12 is greater than line 11, subtract line 11 from line 12. This is overwithheld windfall profit tax	14	

Part V Amount of Windfall Profit Tax Withheld from Payments Made in 1985

1 Windfall profit tax withheld from payments made in 1985 (regardless of when windfall profit tax liability arose)	1	

For Paperwork Reduction Act Notice, see the instructions on back of Copy A.

Form **6248** (1985)

Form **4419**
(Rev. July 1985)

Department of the Treasury — Internal Revenue Service

Application for Magnetic Media Reporting of Information Returns

IRS Use Only

OMB No. 1545-0387
Expires 7-31-88

1. Please fill in this form and send to

Internal Revenue Service Center

2. Name and address of organization *(street, city, State and ZIP code)*

3. Payment year for which you plan to begin reporting on magnetic media

4. Employer identification number

5. Kind of magnetic media you plan to submit *(check one)*

☐ Tape ☐ Cassette/Mini-Disk

☐ Disk ☐ Diskette

6. Person to contact about this request

Name:

Title:

Telephone number: *(include area code)*

7. **Documents To Be Reported**

Form	Estimated Volume		Form	Estimated Volume	
	Magnetic Media	Paper		Magnetic Media	Paper
☐ 1099-DIV			☐ 6248		
☐ 1099-INT			☐ W-4		
☐ 1099-MISC			☐ W-2G		
☐ 1099-OID			☐		
☐ 1099-R			☐		
☐ 1099-G			☐		
☐ 1099-PATR			☐		
☐ 1099-B			☐		
☐ 5498			☐		
☐ 8027			☐		
☐ 1042S			☐		

8. **Kind of equipment on which media will be prepared**

Main Frame *(all media types)*			Drive Unit *(all media)*	
Manufacturer	Model		Manufacturer	Model
Tape Only			**All Media Types**	
Width	Tracks ☐ 7 ☐ 9	Density	Recording code *(e.g., EBCDIC, BCD, or ASCII)*	

9. If your firm is acting as agent, please list the name and employer identification number of each payer on a separate sheet and attach it to this application.

10. **Person responsible for preparation of tax reports**	Name *(type or print)*	Title
	Signature	Date

See back of this form for Paperwork Reduction Act Notice.

Form **4419** (Rev. 7-85)

Instructions for Form 4419

Payers or agents who decide to file information returns on magnetic media must complete Form 4419 to receive authorization for filing. Please be sure to complete all appropriate blocks as explained in the following instructions:

Block 2

Enter the name and complete address of the person or organization that will prepare and submit the magnetic media.

Block 3

Show the tax *(payment)* year for which you intend to begin filing information returns on magnetic media.

Block 5

Check the kind of magnetic media you plan to submit. If you plan to submit more than one kind of magnetic media, you should complete a separate application for each kind.

Block 7

Check the boxes next to all of the information returns you file with the Internal Revenue Service.

a. **Magnetic media column**: Enter the total number of individual information returns to be reported on magnetic media *(an estimate is acceptable)*.

b. **Paper column**: Enter the total number of individual information returns to be reported on paper if not all returns will be filed in magnetic media form *(an estimate is acceptable)*.

Block 9

If your firm is preparing information returns on magnetic media for payers other than itself, attach to your application a list of the names and employer identification numbers of the payers. If you add or delete any payers from your file, you *must* submit an updated list of payers.

Block 10

The form must be signed and dated by an official of the company or organization requesting authorization to report on magnetic media.

Filing your application

1. Mail the completed application and any attached lists to the Internal Revenue Service Center at the address shown in BLOCK 1.

2. When we receive your application, we will review it. If it is acceptable, we will send you an authorization letter within 30 days. Do not submit magnetic media until you receive an authorization letter.

3. We encourage new filers to submit test data on magnetic media for review before the filing season. If you want to submit test data, contact the magnetic media coordinator where you file your application.

4. Your authorization will be valid as long as the magnetic media submitted conforms to the specifications of the applicable revenue procedures. However, a new application is required if:

a. filing is discontinued and then resumed, or

b. there is any change in the equipment listed on the application.

Paperwork Reduction Act Notice

We ask for this information to carry out the Internal Revenue laws of the United States. We need it to ensure that the magnetic media you are using will be compatible with our processing equipment. The information is also used to more efficiently schedule and manage its processing in the service centers. You are required to give us this information if you want to file your returns on magnetic media.

Notice of Proposed Rulemaking

Treatment of Qualified Real Estate Agents and Direct Sellers as Nonemployees; Determination of Employer Liability for Certain Employment Taxes; Information Reporting of Direct Sales and Payments of Remuneration for Services

LR-214-82

SUMMARY: This document contains proposed amendments to the Employment Tax Regulations under section 3508, relating to the treatment of qualified real estate agents and direct sellers as nonemployees for Federal income and employment tax purposes, and under section 3509, relating to the determination of employer liability for income tax withholding and employee social security taxes where the employer treated an employee as a nonemployee for purposes of such taxes. It also contains proposed amendments to the Income Tax Regulations under section 6041A, relating to information reporting of direct sales and payments of remuneration for services. Sections 3508, 3509, and 6041A were added to the tax law by sections 269, 270, and 312, respectively, of the Tax Equity and Fiscal Responsibility Act of 1982 (96 Stat. 551, 553, 601) [Pub. L. 97-248, 1982-2 C.B. 462, 535, 536, 561]. The regulations would provide the public with the guidance needed to comply with the applicable tax law.

DATES: Written comments and requests for a public hearing must be delivered or mailed by March 10, 1986. The regulations under section 3508 are proposed to be effective for services performed after December 31, 1982, and the regulations under section 6041A are proposed to be effective for payments and sales made after December 31, 1982. The regulations under section 3509 are proposed to be effective for any income and employee social security taxes required to be deducted and withheld, except with respect to assessments made before January 1, 1983.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-214-82), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Robert E. Shaw of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3297, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

The determination of whether an individual is an employee or independent contractor for Federal tax purposes is important for several reasons. Wages paid to employees generally are subject to social security taxes imposed on the employer and the employee under the Federal Insurance Contributions Act (FICA) and to unemployment taxes imposed on the employer under the Federal Unemployment Tax Act (FUTA). Compensation paid to independent contractors is subject to the tax on self-employment income (SECA), but not to FICA or FUTA taxes. The SECA is generally paid only by self-employed individuals. In addition, Federal income tax must generally be withheld from compensation paid to employees but not from compensation paid to independent contractors.

Except for sections 3121(d)(3) and 3306(i), which establish categories of statutory employees for social security and Federal unemployment tax purposes, prior to the enactment of the Tax Equity and Fiscal Responsibility Act of 1982, the determination of an individual's status as an employee or independent contractor generally was made under common-law (*i.e.*, nonstatutory) rules. Under the common-law test, an individual generally is an employee if the person for whom the individual performs services has the right to control and direct that individual, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. Thus, the most important factor under the common law is the degree of control, or right of control, which the employer has over the manner in which the work is to be performed.

The Service applies various factors that have evolved from the common law to determine whether the requisite control exists. Because of the difficulty that often arises in applying these factors, several bills introduced in both the House and the Senate during 1982 set forth statutory "safe-harbor" tests which, if satisfied with respect to an individual, would result in that individual being classified as an independent contractor. The proposed safe-harbor requirements, generally applicable to post-1982 services, related to (1) control of hours worked, (2) place of business, (3) investment or income fluctuation, (4) written contract and notice of tax responsibilities, and (5) the filing of required returns. S. Rep. No. 97-494, 97 Cong., 2d Sess. 364 (1982). Workers who did not meet the safe-harbor tests still would have had their employment tax status determined under the common-law rules.

In enacting the Tax Equity and Fiscal Responsibility Act of 1982 (P.L. 97-248) [1982-2 C.B. 462], Congress rejected the broader safe-harbor tests proposed by these bills and instead partially resolved the employee-independent contractor controversy by creating two categories of statutory nonemployees—qualified real estate agents and direct sellers. Thus, notwithstanding the common-law rules, an individual is an independent contractor for services that satisfy the statutory requirements of section 3508. Other employment situations generally must continue to be evaluated under common-law principles.

In response to the serious tax deficiencies that may arise when a worker erroneously treated as an independent contractor is reclassified as an employee, Congress enacted section 3509, which fixes an employer's liability for income tax withholding and employee social security taxes generally at a fraction of the amount of taxes which should have been deducted and withheld. Section 3509 provides relief to employers who would otherwise be liable for the full amount of such taxes which should have been deducted and withheld and provides a sanction for an employer's erroneous treatment of a worker in situations in which the employer would otherwise be able to escape liability for such taxes under the statutory offset provisions of sections 3402(d) and 6521.

To assure increased compliance by direct sellers with the income tax law, Congress added section 6041A (section 312 of the Tax Equity and Fiscal Responsibility Act of 1982) which, in addition to other requirements, imposes an obligation on direct sellers of consumer products to report gross sales totalling $5,000 or more in a calendar year to any buyer for resale in the home or some place other than a permanent retail establishment. Congress also provided a penalty for failure to file this return (section 6652) and a penalty for failure to furnish certain statements (section 6678).

EXPLANATION OF PROVISIONS

In general

The proposed regulations provide that an individual performing services as a qualified real estate agent or a direct seller will not be treated as an employee and the service-recipient will not be treated as an employer for Federal income and employment tax purposes. In order to qualify for such treatment substantially all the remuneration paid by a service-recipient to an individual for services as a real estate agent or direct seller must be directly related to sales or other output and such services must be performed pursuant to a written contract providing that such individual will not be treated as an employee for Federal tax purposes.

The proposed regulations make clear that a statutory employee (that is, an individual treated as an employee under section 3121(d)(3) of the Code) who also qualifies as a nonemployee under section 3508 will be treated as a nonemployee for FICA, FUTA, and Federal income tax withholding purposes with respect to services described in section 3508. For example, an agent-driver (statutory employee) who qualifies as a direct seller (statutory nonemployee) will be treated as a nonemployee for FICA, FUTA, and income tax withholding purposes with respect to services performed as a direct seller. The regulations also make clear that the written contract requirement is not met unless the contract specifically states that the individual will not be treated as an employee for Federal tax purposes. For this purpose, it is not sufficient that the contract merely states that the individual will not be treated as an employee.

"Substantially all" remuneration requirement

Section 3508 requires that in order for an individual to be treated as a qualified real estate agent or a direct seller substantially all of the remuneration received for services as a real estate agent or direct seller must be directly related to sales or other output. The proposed regulations provide that the "substantially all remuneration" test is satisfied with respect to services performed as a real estate agent or direct seller if at least 90 percent of the total remuneration received during the calendar year by the individual for services performed as a real estate agent or direct seller is directly related to sales or other output rather than to the number of hours worked. The proposed regulations also provide rules for applying the "directly related to sales or other output" requirement to pooled remuneration arrangements, remuneration received in advance of sales or performance, and remuneration dependent on the productivity of others.

Direct sellers

A direct seller is any salesperson who, in addition to meeting the "substantially all" remuneration and written contract requirements, sells consumer products, either directly or through a middleperson (*i.e.*, a buyer) for ultimate resale, in the home or in a place other than in a permanent retail establishment. The proposed regulations define "consumer product" as any tangible personal property which is distributed in commerce and which is normally used for personal, family, or household purposes (including any such property intended to be attached to or installed in any real property without regard to whether it is so attached or installed). This definition corresponds to the definition provided in 15 U.S.C. §2301, and the limitation to tangible property is consistent with other definitions of consumer products found in the United States Code (15 U.S.C. §2052; 18 U.S.C. §1365; 42 U.S.C. §6291). The proposed regulations define "permanent retail establishment" as any business operating in or from a structure or facility which remains stationary for a substantial period of time to which consumers go to purchase consumer goods. The proposed regulations also clarify that vendors operating within, or on the grounds of, a permanent structure or facility such as a sports arena or amusement park are considered to operate in a permanent retail establishment for purposes of section 3508. Thus, the term "direct seller" may include door-to-door salespersons of not only products traditionally thought of as consumer products (*e.g.*, personal toiletry items, vacuum cleaners, kitchen products) but also products which require installation or construction on the consumer's property (*e.g.*, residential swimming pools, aluminum siding, kitchen cabinets, storm windows, insulation, carpeting) and products not used in or around the home. The term also includes salespersons who sell consumer goods directly to consumers through an exchange medium other than a permanent retail establishment (*e.g.*, mobile meal wagons or street vendors). The term does not include door-to-door salespersons of intangible products (*e.g.*, insurance, cable television subscription).

Persons who provide services generally are not direct sellers. For example, persons who provide services that do not involve the use of a product (*e.g.*, polltakers) or services that involve parts or materials which are incidental to providing services (*e.g.*, painting, carpet cleaning, septic tank cleaning, lawn care, pest control services, or appliance repair) are considered service providers rather than direct sellers.

Services of real estate agent and direct seller

The proposed regulations provide that the services performed as a direct seller are activities generally associated with the sale of consumer products in the home or otherwise than in a permanent retail establishment. These services include activities that are necessary to increase the sales efforts of other individuals, such as providing motivation, encouragement, training, recruitment, or counseling. Installation services performed by a direct seller in connection with the sale of a consumer product generally are not services performed by a direct seller. However, the proposed regulations provide that installation services rendered by a seller in conjunction with the sale of a consumer product will be services performed as a direct seller if the value of the installation services is 10 percent or less of the purchase price of the product (including installation).

The services performed as a real estate agent are those activities generally associated with the sale of real property. Such services include appraising property, advertising and showing property, closing sales, acquiring a lease to the property, and recruiting, training and supervising other salespersons. The services performed as a real estate agent do not include the management of property.

Retirement plans for self-employed individuals

The proposed regulations make clear that the fact that an individual is treated as a nonemployee under section 3508 for employment tax purposes will not prevent the individual from being covered under a qualified retirement plan for self-employed individuals.

Employer liability under section 3509

An employer's liability for failure to deduct and withhold income tax or employee social security taxes by reason of treating an employee as a nonemployee for purposes of such taxes is generally determined under section 3509. The employer's liability for income tax withholding is determined as if the amount required to be deducted and withheld was equal to 1.5 percent (3 percent where the employer disregards certain reporting requirements) of the wages paid to the individual erroneously treated as a nonemployee. The employer's liability for employee social security taxes is determined as if such taxes imposed were 20 percent (40 percent where the employer disregards certain reporting requirements) of the amount imposed without regard to section 3509. The increased percentages are applicable where an employer fails to timely file any return or statement under sections 6041(a), 6041A, or 6051 that would be required consistent with the employer's treatment of the worker as a nonemployee.

The proposed regulations clarify that, for purposes of section 3509, an employer fails to withhold taxes when the employer fails to pay over the full amount of tax required to be deducted and withheld during a calendar year on or before the due date for the return relating to such taxes for the final quarter fo such calendar year. Thus, section 3509 is generally applied with respect to each calendar year as a unit.

Under section 3509 and the proposed regulations, if an employer's liability for any tax is determined under section 3509 the employer (i) may not collect from the employee any amount of tax so determined, and (ii) is not entitled to any offset of liability under section 3402(d) or 6521. An employee's liability for taxes is not affected by application of section 3509 to the employer and the offset provisions of section 6521 may, where applicable, apply with respect to the employee's liability for employee social security taxes. An employer's liability for employer social security taxes is not affected by section 3509.

Section 3509 does not apply where an employer deducts income tax but not employee social security taxes or where the employer intentionally disregards the requirements to withhold and deduct Federal income tax or employee social security taxes. Section 3509 does not apply to employee social security taxes with respect to statutory employees described in section 3121(d)(3). The proposed regulations clarify that if an employer's liability for any tax is determined under section 3509 the employer may still be liable for penalties with respect to his or her failure to deduct and withhold such tax. The amount of such penalties, however, is based on the amount of the employer's liability for such tax under section 3509.

The proposed regulations also clarify that the amount of an employer's liability for tax determined under section 3509 will be considered satisfied to the extent of the amount of such tax which was actually withheld and deducted from the employee and paid. If the amount withheld, deducted, and paid exceeds the employer's liability as computed under section 3509, however, the employer may not claim a refund or credit of such excess amount.

New reporting requirements

Section 6041A added two reporting requirements relating to payments as remuneration for services and gross sales of consumer products to a buyer for resale in the home or otherwise than in a permanent retail establishment. Section 6041A(a) requires that a service-recipient engaged in a trade or business, who, in the course of that trade or business, makes payments to a person as remuneration for services, report such payments if the total remuneration paid to that person by the service-recipient during the calendar year is $600 or more. The proposed regulations provide that such remuneration does not include any amounts which the service-recipient knows are excludable from the gross income of the person performing services (*e.g.*, qualified foster care payments under section 131). Section 6041A(b) requires a direct seller to report gross sales of consumer products totaling $5,000 or more in a calendar year to any buyer who resells the product in the home or any place other than a permanent retail establishment. All sales of consumer products to a buyer for resale to another person are taken into account in determining the aggregate amount of sales to that buyer during the calendar year, even if the buyer resells some of the products in a permanent retail establishment.

The proposed regulations clarify that the aggregate amount of sales of consumer products to a buyer during a calendar year includes the sale of products used by the buyer for the buyer's personal use or consumption (including products disposed of in a manner other than resale such as gifts to friends or relatives). However, the aggregate amount of sales does not include the sale of goods that cannot be resold, such as catalogs and samples.

The proposed regulations make clear that an information return is required with respect to any person who sells consumer products in the home or otherwise than in a permanent retail establishment regardless of whether that person purchases the product from the company and resells it to the consumer or is a company salesperson (other than an employee) who does not acquire title to a product before selling it.

The proposed regulations provide that the regulatory exceptions to the reporting requirement under section 6041, as set forth in §1.6041-3, are applicable to the reporting requirement under section 6041A(a).

COMMENTS AND PUBLIC HEARING

Before adoption of these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the Federal Register.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20530. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies of those comments to the Service.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required.

Although this document is a notice of proposed rulemaking which solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public comment requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal authors of these proposed regulations are Robert E. Shaw of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service, and Donald W. Stevenson, formerly of that Division. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

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Proposed amendments to the regulations

The proposed amendments to 26 CFR Parts 1 and 31 are as follows:

EMPLOYMENT TAX REGULATIONS
(26 CFR Part 31)

Paragraph 1. The authority for Part 31 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 2. There are inserted immediately after §31.3507-2 the following two new sections.

§31.3508-1 Treatment of qualified real estate agents and direct sellers as nonemployees.

(a) *In general.* For Federal income and employment tax purposes,

(1) An individual who performs services after December 31, 1982, as a qualified real estate agent or as a direct seller shall not be treated as an employee with respect to such services, and

(2) The service-recipient shall not be treated as an employer with respect to such services.

(b) *Qualified real estate agent defined*—(1) *In general.* For purposes of section 3508 and this section, the term "qualified real estate agent" means any individual who is a sales person (including an individual who does not personally make sales but who recruits, trains, or supervises other individuals who make sales) if—

(i) Such individual is a licensed real estate agent,

(ii) Substantially all of the remuneration (whether or not paid in cash) for the service performed by such individual as a real estate agent is directly related to sales or other output (including the performance of services) rather than to the number of hours worked, and

(iii) The services performed by such individual as a real estate agent are performed pursuant to a written contract between such individual and the service-recipient and the contract provides that such individual will not be treated as an employee with respect to such services for Federal tax purposes.

(2) *services performed as a real estate agent.* For purposes of this section, the services performed by an individual as a real estate agent include any activities that customarily are performed in connection with the sale of an interest in real property. Such services include the advertising or showing of real property, the acquisition of a lease to real property, and the recruitment, training, or supervision of other real estate sales persons. Such services also include the appraisal activities of a licensed real estate agent in connection with the sale of real property. Services performed as a real estate agent do not include the management of property.

(c) *Direct seller defined*—(1) *In general.* For purposes of section 3508 and this section, the term "direct seller" means any person if—

(i) Such person—

(A) Is engaged in the trade or business of selling (or soliciting the sale of) consumer products to any buyer on a buy-sell or deposit-commission basis for resale by the buyer or any other person in the home or in some other place that does not constitute a permanent retail establishment, or

(B) Is engaged in the trade or business of selling (or soliciting the sale of) consumer products in the home or in some other place that does not constitute a permanent retail establishment,

(ii) Substantially all the remuneration (whether or not paid in cash) for the performance of the services described in paragraph (c)(2) of this section is directly related to sales or other output (including the performance of services) rather than to the number of hours worked, and

(iii) Such person performs the services described in paragraph (c)(2) of this section pursuant to a written contract between such person and the service-recipient, and the contract provides that such person will not be treated as an employee with respect to such services for Federal tax purposes.

(2) *Services performed as a direct seller*—(i) *In general.* The services described in this paragraph (c)(2) are any services that customarily are directly related to the trade or business of selling (or soliciting the sale of) consumer products in the home or in any other location that does not constitute a permanent retail establishment. Such services include any activity to increase the productivity of other individuals engaged

in such sales, such as recruiting, training, motivating, and counseling such individuals. Except as provided in paragraph (c)(2)(ii) of this section, such services do not include the installation or construction on the customer's property of a consumer product. See paragraphs (f) and (g)(3) of this section for the inapplicability of section 3508 where the sale or use of consumer products is only incidental to the rendering of services.

(ii) *Installation of consumer product in conjunction with the sale of such product.* If an individual engaged in the trade or business of selling consumer products performs installation services in conjunction with the sale of a consumer product such services shall be included as services performed as a direct seller only if the value of such installation services is 10 percent or less of the purchase price of such consumer product (including installation). If the value of such installation services exceeds 10 percent of the purchase price of the consumer product (including installation) the installation services shall not be included as services performed as a direct seller. See paragraph (j) of this section for treatment of dual services under section 3508.

(d) *Substantially all remuneration directly related to sales or other output*—(1) *Substantially all remuneration*—(i) *In general.* The requirement of paragraph (b)(1)(ii) or (c)(1)(ii) of this section is satisfied for any calendar year with respect to the services described in such paragraph if at least 90 percent of the total remuneration, including advances and draws (except as provided in paragraph (d)(1)(ii) of this section), received by the individual from the service-recipient for performing such services during that calendar year is directly related to sales or other output rather than to the number of hours worked.

(ii) *Repayment of advances or draws.* For purposes of paragraph (d)(1)(i) of this section, total reumuneration received by an individual does not include any portion of an advance or draw that is repaid directly or indirectly (including repayment by a debit against the individual's account with the service-recipient) pursuant to a binding written agreement which on the date the advance or draw is received requires repayment of the amount by which such advance or draw exceeds the amount which is directly related to sales or other output (as defined in paragraph (d)(2) of this section). The determination of whether any amounts not excluded under this paragraph (d)(1)(ii) from the total remuneration received by an individual is directly related to sales or other output for purposes of paragraph (d)(1)(i) of this section is made on the basis of all the facts and circumstances (see paragraph (d)(2)(i) of this section).

(2) *Directly relating to sales or other output*—(i) *In general.* An item of remuneration is directly related to sales or other output if that item is paid, awarded, or credited to the individual on the basis of the individual's services with respect to one or more specific sales transactions or the accomplishment of one or more specific tasks rather than on the basis of the number of hours worked. Whether an item of remuneration is directly related to sales or other output shall be determined on the basis of all the facts and circumstances. For purposes of this section an item of remuneration that is in the nature of salary, that is, a fixed periodical compensation paid for services rendered without regard to the amount of services rendered, shall be treated as an item of remuneration that is paid, awarded, or credited on the basis of the number of hours worked.

(ii) *Directly related to sales or output of some other person.* for purposes of this section, remuneration received by an individual based on the sale or productivity of some other individual shall be treated as directly related to sales or other output if it was paid, awarded, or credited on the basis of such other individual's services with respect to one or more particular sales transactions or the accomplishment of one or more specific tasks.

(iii) *Remuneration received from a pool.* Remuneration received by an individual under an arrangement whereby a service-recipient pools the remuneration of several individuals and a portion of the aggregate pooled remuneration is periodically distributed to each pool participant shall be treated as directly related to sales or other output only to the extent that the amount of remuneration received by that individual from the pool does not exceed the amount of remuneration that, in the absence of the pool arrangement, such individual would have received on the basis of the individual's services with respect to one or more specific sale transactions or the accomplishment of one or more specific tasks. Amounts received from the pool in excess of the amount that person would have ordinarily received for performing services in connection with such specific sales transactions or specific tasks are not directly related to sales or other output.

(e) *Written contract requirement*—(1) *In general.* Except as otherwise provided in paragraph (e)(2) of this section, a written contract that states that the individual will not be treated as an employee without specifically stating "for Federal tax purposes" does not meet the written contract requirements set forth in paragraph (b)(1)(iii) and (c)(1)(iii).

(2) *Existing contracts*—(i) *In general.* A contract which—

(A) Is in effect on or before February 28, 1983, and

(B) States that the individual performing the services will not be treated as an employee but does not specifically include the phrase "for Federal tax purposes,"

will be deemed to satisfy the written contract requirement if the service-recipient furnishes to the individual performing the services a written notice that specifically states that the individual will not be treated as an employee "for Federal tax purposes."

(ii) *Date contract requirement deemed satisfied.* If the notice described in paragraph (e)(2)(i) of this section is mailed or otherwise furnished on or before February 28, 1983, the written contract requirement shall be deemed satisfied as of the date of the original contract. If the notice is furnished after that date, the written contract requirement is deemed satisfied as of the date the notice is furnished.

(f) *Trade or business of selling consumer products.* For purposes of section 3508 and this section, a person is not engaged in the trade or business or selling (or soliciting the sale of) consumer products if the sale or use of such products is in an incidental part of a trade or business in which such person primarily renders services to clients. Whether the sale or use of a product is an incidental part of a trade or business that primarily consists of rendering services shall be determined on the basis of all the facts and circumstances, taking into account such factors as the cost of the product in relation to the cost of the service. Generally, the sale or use of a product is an incidental part of a trade or business that primarily consists of rendering services if the use of the product is necessary to the performance of the particular service (*e.g.*, insecticide in a pest control business). See paragraph (c)(2) of this section for the applicability of this section to individuals who install consumer products in conjunction with the sale of such products.

(g) *Definitions*—(1) *Buy-sell basis.* A transaction is on a buy-sell basis if the buyer performing the services is entitled to retain part or all of the difference between the price at which the buyer purchases the product and the price at which the buyer sells the product as part or all of the buyer's remuneration for the services.

(2) *Deposit-commission basis.* A transaction is on a deposit-commission basis if the buyer performing the service is entitled to retain part or all of a purchase deposit paid by the consumer in connection with the transaction as part or all of the buyer's remuneration for the services.

(3) *Consumer product.* The term "consumer product" means any tangible personal property which is distributed in commerce and which is normally used for personal, family, or household purposes (including any such property intended to be attached to or installed in any real property without regard to whether it is so attached or installed). The term "consumer product" does not include any product used in the manufacture of another product to be distributed in commerce or any product used only incidentally in providing a service (*e.g.*, insecticide used in a pest control service, materials used in an appliance repair business).

(4) *Permanent retail establishment.* A permanent retail establishment is any retail business operating in a structure or facility that remains stationary for a substantial period of time to which consumers go to purchase consumer goods. Examples of these establishments are: grocery stores, hardware stores, clothing stores, hotels, restaurants, drug stores, and newsstands. In addition, amusement areas, such as amusement parks and sports arenas, at which consumer products are sold are permanent retail establishments. Portable or mobile structures, facilities, or equipment, such as street vendor stands and mobile carts or vehicles, generally do not constitute permanent retail establishments. However, sales of consumer products may occur in a permanent retail establishment for purposes of this section even though portable or mobile structures, facilities, or equipment is used. For example, a vendor who sells consumer products, such as souvenirs or food, in the stands of a sports arena or on the grounds of an amusement park sells consumer products in a permanent retail establishment. Also, a vendor who sells consumer products in a parking lot or other property which is near to and serving a sports arena or other amusement area pursuant to an agreement which grants to the vendor or to the service-recipient the right to sell consumer products on such property sells consumer products in a permanent retail establishment, regardless of whether the sale is made within a permanent structure.

(5) *Service-recipient.* The term "service-recipient" means the person (other than a client or customer) for whom the services as a qualified real estate agent or direct seller are performed (*e.g.*, a real estate firm or a company whose consumer products are sold door-to-door).

(h) *No inference.* The fact that an individual does not qualify under section 3508 and this section as a qualified real estate agent or as a direct seller with respect to any services does not create an inference that such individual is an employee or the service-recipient is an employer with respect to such services.

(i) *Application to statutory employees.* A statutory employee (that is, an individual in one of the categories of workers defined in section 3121(d)(3) or 3306(i) to be employees) who meets the requirements of paragraph (b) or (c) of this section for classification as a qualified real estate agent or as a direct seller shall be treated as a nonemployee for Federal income tax, Federal Insurance Contribution Act (FICA), and Federal Unemployment Tax Act (FUTA) purposes with respect to services performed as a qualified real estate agent or as a direct seller (as described in paragraphs (b)(2) and (c)(2) of this section, respectively).

(j) *Dual services*—(1) *In general.* Section 3508 shall apply only with respect to services performed as a qualified real estate agent or a direct seller. Whether an individual is treated as an employee or as a self-employed individual with respect to services other than those performed as a qualified real estate agent or a direct seller shall be determined under common-law principles.

(2) *Examples.* The Following examples illustrate the principles set forth in this paragraph (j).

Example (1). A is a licensed real estate agent who performs services as a real estate agent pursuant to a written contract described in paragraph (b)(1)(iii) of this section. In addition to performing services as a real estate agent A performs general bookkeeping duties for the same service-recipient. All of the remuneration for the services performed as a real estate agent is directly related to sales. A will be treated as a nonemployee under section 3508 only with respect to A's services as a real estate agent. Whether A is treated as an employee or as a self-employed individual with respect to the bookkeeping duties will be determined under common-law principles.

Example (2). B is engaged in the trade or business of selling aluminum siding. B performs services as a direct seller pursuant to a written contract described in paragraph (c)(1)(iii) of this section. All sales are made in the customer's home and the purchase price includes installation. B installs all aluminum siding which he sells and receives a commission based upon the purchase price as compensation for his services with respect to both the sale and the installation. The value of such installation services exceeds 10 percent of the purchase price of the siding. B will be treated as a nonemployee under section 3508 only with respect to his services as a direct seller. Whether B is treated as an employee or as a self-employed individual with respect to services performed in installing the siding will be determined under common-law principles.

Example (3). The facts are the same as in example (2) except that B sells and installs personal computers and that the value of the installation services performed by B is less than 10 percent of the purchase price of the computers including installation. B is treated as a nonemployee under section 3508 with respect to both his services in selling the computers and in installing them. See paragraph (c)(2)(ii) of this section.

Example (4). Assume all the requirements of section 3508(b)(1) and paragraph (b) of this section are satisfied with respect to A, a real estate agent, except that A did not obtain a real estate license until March 29. The license was valid for the remainder of the year. A is treated as self-employed under section 3508 for that portion of the year beginning on March 29. Whether for Federal tax purposes A is to be treated as self-employed for the other portion of the year shall be determined under common law.

(k) *Coordination with retirement plans for self-employed.* this section shall not prevent an individual who is treated as self-employed under section 3508 from being covered under a qualified retirement plan for self-employed individuals pursuant to section 401(c)(1) of the Code.

§31.3509-1 Determination of employer's liability for certain employment taxes.

(a) *In general.* Except as otherwise provided in this section, if during any calendar year any employer fails to deduct and withhold any tax under chapter 24 (relating to withholding of income tax) or subchapter A of chapter 21 (relating to the social security tax on employees) of the Internal Revenue Code of 1954 with respect to any employee by reason of treating such employee as not being an employee for purposes of such chapter or subchapter, the amount of the employer's liability for such tax with respect to such year shall be determined under this paragraph (a).

(1) *Income tax withholding.* The employer's liability for tax under chapter 24 for such year with respect to such employee shall be determined as if the amount required to be deducted and withheld were equal to 1.5 percent of the wages (defined in section 3401(a)) paid to such employee for such year.

(2) *Employee social security taxes.* The employer's liability for employee social security taxes under subchapter A of chapter 21 for such year with respect to such employee shall be determined as if the taxes imposed under such subchapter were 20 percent of the amount imposed under such subchapter for such year without regard to this paragraph (a)(2).

Section 3509 and this section do not affect an employer's liability for taxes under subchapter B of chapter 21 (relating to employer social security taxes) of the Internal Revenue Code of 1954. See paragraph (c) of this section for increased employer liability where an employer fails to meet certain reporting requirements.

(b) *Definitions*—(1) *Fails to deduct and withhold any tax*—(i) *In general.* For purposes of section 3509 and this section, an employer fails to deduct and withhold any tax under chapter 24 or under subchapter A of chapter 21 with respect to an employee for a calendar year if such employer fails to pay over the full amount of such tax required to be deducted and withheld during such calendar year (determined without regard to section 3509 and this section) on or before the due date for the return relating to such tax for the final quarter of such calendar year.

(ii) *Example.* The provisions of this paragraph (b)(1) may be illustrated by the following example:

Example. M, an employer, does not deduct and withhold income and social security taxes with respect to A, an employee, for the first quarter of 1985 because of M's erroneous belief that A is not an employee. On April 1, 1985, M ascertains the error and begins to withhold and deduct the full amount of income and social security taxes with respect to A for the remaining three quarters of 1985. M also makes timely adjustments under section 6205 with respect to the first quarter's taxes not deducted and withheld, and pays over the full amount of income and social security taxes which were required to be deducted and withheld during 1985 on or before the due date for the return for the fourth quarter of 1985. M has not failed to deduct and withhold income and social security taxes with respect to A during 1985 for purposes of section 3509 and this section.

(2) *Treatment of employee as not being an employee.* For purposes of section 3509 and this section, an employer has treated an employee as not being an employee for purposes of the withholding requirements of chapter 24 or subchapter A of chapter 21 if, because of his belief that the employee was not an employee, the employer (i) has failed to deduct and withhold such tax as defined in paragraph (b)(1) of this section for the calendar year and (ii) has also failed to file one or more employment tax returns (including, where applicable, Forms 940 (Employer's Annual Federal Unemployment (FUTA) Tax Return), 941 (Employer's Quarterly Federal Tax Return), 942 (Employer's Quarterly Tax Return for Household Employees), 943 (Employer's Annual Tax Return for Agricultural Employees), and W-2 (Wage and Tax Statement)) for any period during the calendar year with respect to such employee. For purposes of this paragraph (b)(2) an employer who has filed a delinquent or amended employment tax return as a result of Internal Revenue Service compliance procedures (*i.e.*, examination or collection activities) has failed to file an employment tax return.

(c) *Employer's liability increased where employer fails to meet reporting requirements*—(1) *In general.* In the case of an employer who fails to meet the applicable requirements of section 6041(a), 6041A, or 6051 with respect to any employee, unless such failure is due to reasonable cause, paragraph (a) of this section shall be applied with respect to such employee:

(i) By substituting "3 percent" for "1.5 percent" in paragraph (a)(1) of this section; and

(ii) By substituting "40 percent" for "20 percent" in paragraph (a)(2) of this section.

(2) *Applicable requirements.* For purposes of paragraph (c)(1) of this section, an employer has failed to meet the applicable requirements of section 6041(a), 6041A, or 6051 with respect to an employee if—

(i) The employer has treated such employee as not being an employee for purposes of the withholding requirements of chapter 24 or subchapter A of chapter 21, and

(ii) The employer has failed to satisfy any of the requirements described in sections 6041(a), 6041A, and 6051 and the regulations thereunder (relating to information returns and statements) which would be applicable consistent with the treatment described in paragraph (c)(2)(i) of this section.

An employer who has failed to timely file any return or statement required under section 6041(a), 6041A, or 6051 has failed to meet the applicable requirements of that section.

(d) *Special rules.* For purposes of section 3509 and this section:

(1) *Determination of liability.* If the amount of any employer's liability for tax with respect to an employee is determined under section 3509 and this section:

(i) Such employee's liability for income tax or employee social security taxes shall not be affected by the assessment or collection of any tax so determined and any amount assessed or collected as a result of the application of this section shall not be credited against the employee's tax liability;

(ii) Such employer shall not be entitled to recover from such employee any tax determined under this section;

(iii) Sections 3402(d) and 6521 shall not apply with respect to such employer's liability determined under this section, although section 6521 may apply with respect to an employee's liability regardless of whether the employer's liability is determined under section

3509; and

(iv) Tax imposed by section 3101 or 3402 (including amounts determined under section 3509) for any calendar year that the employer has reported and paid over with respect to such employee shall be allowed as a credit against tax determined under section 3509 with respect to such employee for such calendar year. If the amount of such reported and paid over tax exceeds the employer's liability for tax as determined under section 3509, however, such excess does not constitute an overpayment of tax and does not entitle the employer to a refund or credit for the amount of such excess.

(2) *Section not to apply where employer deducts and withholds income tax but not social security taxes.* Section 3509 and this section shall not apply to any employer with respect to any wages if:

(i) The employer deducted and withheld any amount of the tax imposed by chapter 24 with respect to such wages, but

(ii) Failed to deduct and withhold the amount of the taxes imposed by subchapter A of chapter 21 with respect to such wages.

(3) *Section not to apply to social security tax with respect to certain statutory employees.* Section 3509 and this section shall not apply to any tax under subchapter A of chapter 21 with respect to an individual described in section 3121(d)(3). For purposes of the preceding sentence, if an individual would be an employee under section 34121(d)(3) but for the fact that such individual is an employee under section 3121(d)(1) or (2), such individual shall be treated as an individual described in section 3121(d)(3).

(4) *Section not to apply in cases of intentional disregard.* Section 3509 and this section shall not apply to the determination of any employer's liability for tax under chapter 24 or subchapter A of chapter 21 for any calendar year if any part of such liability is due to the employer's intentional disregard of the requirement to deduct and withhold such tax. For purposes of the preceding sentence, an employer has intentionally disregarded the requirement to deduct and withhold a tax if the employer intentionally failed to deduct and withhold the full amount of such tax with respect to any wages paid on or after the date on which the employer ascertained the employee status of a worker.

(5) *Section not to apply to assessments made before January 1, 1983.* Section 3509 and this section shall not apply to any tax assessed before January 1, 1983.

(6) *Penalties.* Section 3509 and this section do not relieve an employer from liability for any penalties, additions to tax, or additional amounts otherwise applicable with respect to a failure to deduct and withhold any taxes. However, for purposes of applying any penalty, addition to tax, or additional amount with respect to any tax for which an employer's liability is determined under section 3509, the employer's tax liability as determined under that section shall be treated as the tax the employer should have withheld, deducted, and paid over.

INCOME TAX REGULATIONS
(26 CFR Part 1)

Par. 3. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.6041A-1 also issued under 26 U.S.C. 6041A.

Par. 4. A new §1.6041A-1 is added immediately after §1.6041-7 to read as set forth below:

§1.6041A-1 Returns regarding payments of remuneration for services and certain direct sales.

(a) *Returns regarding remuneration for services*—(1) *In general.* If—

(i) Any service-recipient engaged in a trade or business pays in the course of that trade or business during any calendar year after 1982 remuneration to any person for services performed by that person, and

(ii) The aggregate amount of remuneration paid to such person during such calendar year is $600 or more.

then the service-recipient shall make a return in accordance with paragraph (e) of this section. For purposes of the preceding sentence, the term "service-recipient" means the person for whom the service is performed (*e.g.*, in the case of a real estate agent, the real estate firm for which such agent performs services). For purposes of this paragraph (a)(1) only, the term remuneration does not include amounts paid to any person for service performed by such person if the service-recipient knows that such amounts are excludable from the gross income of the person performing such services. For example, a return is not required with respect to amounts paid to a foster parent which are known by the service-recipient to constitute foster care payments that are excludable from gross income under section 131. For purposes of this paragraph (a)(1), a service-recipient shall be considered to know facts set forth in a written statement provided to the service-recipient, made under the penalties of perjury and signed by the person performing such services, in the absence of knowledge by the service-recipient that such statement is untrue. See section 6041A(d) for rules relating to the application of section 6041A and this section to governmental units (and agencies or instrumentalities thereof).

(2) *Payment attributable to parts and materials.* For purposes of section 6041A and this section, the aggregate amount of remuneration paid to any person for services rendered includes any payments for parts or materials used by such person in rendering the services unless the trade or business of such person is primarily that of selling parts or materials. Whether a person is engaged primarily in the trade or business of selling parts and materials rather than of providing services shall be determined on the basis of all the facts and circumstances, taking into account such factors as whether such person holds himself or herself out as a dealer in parts and whether, with respect to the type of service rendered, a service-recipient ordinarily would specify the type or brand of parts or materials to be used.

Example. X company makes a payment to an unincorporated repair shop for repairs to one of the company's automobiles. The automobile sustained body damage in an accident. The repair contract requires payment of $300 for labor and $400 for new parts that were installed. The repair shop does not hold itself out as a dealer in parts. Generally, customers of the repair shop do not specify the type or brand of replacement parts to be installed. Therefore, the aggregate amount of remuneration that is required to be reported pursuant to section 6041A(a) includes the payment for parts.

(b) *Returns regarding direct sales of $5,000 or more.* (1) *In general.* If—

(i) any person engaged in a trade or business in the course of such trade or business during any calendar year sells consumer products to any buyer on a buy-sell, deposit-commission, or other commission basis for resale (by the buyer or any other person) in the home or otherwise than in a permanent retail establishment, and

(ii) The aggregate amount of such sales made by such person to such buyer during such calendar year is $5,000 or more,

then such person shall make a return with respect to such buyer in accordance with paragraph (e) of this section. This requirement shall apply to sales made in any calendar year after 1982.

(2) *Sale defined.* For purposes of this paragraph (b), a person will be considered to sell a product to a buyer for resale even though such buyer does not acquire title to the product prior to selling it to the consumer. For example, a company sales person, paid on a commission basis, who does not acquire title to a product before selling it to the consumer is considered to have bought the product for resale for purposes of section 6041A(b) and this paragraph.

(3) *Acquisition for resale in a permanent retail establishment.* Section 6041A(b) and this paragraph do not apply to sales of a product to a buyer who resells the product only in a permanent retail establishment, as defined in §31.3508-1(g)(4) of this chapter (Employment Tax Regulations). If a buyer acquires consumer products from a person for resale both in the home (or otherwise than in a permanent retail establishment) as well as in a permanent retail establishment, then such person shall, for purposes of determining the aggregate amount of sales made to such buyer under paragraph (b)(1)(i) of this section, take into account all sales of such products made to such buyer during the calendar year.

(4) *Products purchased for personal use or consumption.* All sales to a buyer of consumer products on a buy-sell, deposit-commission, or other commission basis that are suitable for resale to another person shall be taken into account in determining the aggregate amount of sales made to such buyer under paragraph (b)(1)(i) of this section even if such buyer purchases some of the products for the buyer's personal use or consumption or disposes of some of the products other than by resale (for example, gifts to relatives). Sales of products that cannot be resold, such as samples and catalogues, are not taken into account in determining the aggregate amount of sales to a buyer during the calendar year.

(5) *Consumer product defined.* For purposes of section 6041A(b) and this paragraph, the term "consumer product" means any tangible personal property which is distributed in commerce and which is normally sued for personal, family, or household purposes (including any such property intended to be attached to or installed in any real property without regard to whether it is so attached or installed). The term "consumer product" does not include any product used to manufacture another product to be distributed in commerce or any product used only incidentally in providing a service (*e.g.*, insecticide used in a pest control service, materials used in an appliance repair business).

(c) *Engaged in trade or business.* For purposes of section 6041A(a)(1) or (b)(1) and this section, whether a service-recipient or other person is engaged in a trade or business shall be determined under the rules set forth in §1.6041-1(b).

(d) *Exceptions to return requirement*—(1) *Return required under another section.* No return shall be required under paragraph (a) of this section if a statement with respect to the services is required to be furnished under section 6051, 6052, or 6053.

(2) *Transactions exempt from reporting under section 6041.* No return shall be required under paragraph (a) of this section with respect to a payment which is exempted under §1.6041-3 from the reporting requirement of section 6041, and no return shall be required under paragraph (b) of this section with respect to sales made to a corporation.

(e) *time and manner of filing*—(1) *Form.* The return required to be filed under section 6041A(a) or (b) and paragraph (a) or (b) of this section shall be filed on Forms 1096 and 1099 in accordance with the instructions accompanying those forms.

(2) *Time for filing.* The return shall be filed on or before February 28 of the year following the calendar year for which the return is filed.

(3) *Place of filing.* The return shall be filed with the appropriate Internal Revenue Service Center, at the address listed in the instructions for Forms 1096 and 1099.

(4) *Contents*—(i) *In general.* Unless otherwise provided in the instructions to Form 1099, the return required under section 6041A(a) or (b) and paragraph (a) or (b) of this section shall set forth the information contained in paragraph (e)(4)(ii) or (iii) of this section.

(ii) *Return required under section 6041A(a).* The return required to be filed under section 6041A(a) and paragraph (a)(1) of this section shall set forth the aggregate amount of remuneration paid to the person with respect to whom the return is made during the calendar year for services rendered, the name, address, and taxpayer identification number of the person making the payment, and the name, address, and taxpayer identification number of the recipient of the remuneration.

(iii) *Return required under section 6041A(b).* A return required to be filed under section 6041A(b) and paragraph (b)(1) of this section shall set forth the name, address, and taxpayer identification number of the person making the sales, and the name, address, and taxpayer identification number of the buyer.

(f) *Statements to be furnished to persons with respect to whom information is required to be furnished*—(1) *In general.* Every person required to file a return pursuant to section 6041A(a) or (b) and paragraph (a) or (b) of this section shall furnish a written statement to each person whose name is required to be set forth in that return.

(2) *Time for furnishing statement.* The written statement required under paragraph (f)(1) of this section shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under section 6041A(a) or (b) was made.

(3) *Contents of statement.* The statement shall contain—

(i) The name, address, and taxpayer identification number of the person required to make the return, and

(ii) In the case of a return required to be filed under section 6041A(a) and paragraph (a)(1) of this section, the aggregate amount of payments to the person required to be shown on the return.

(g) *Recipient to furnish name, address, and identification number.* Any person with respect to whom a return or statement is required to be made pursuant to section 6041A and this section by another person shall furnish to that other person his name, address, and identification number upon demand by the person required to make the return.

(h) *Penalties*. For provisions relating to the penalties for failure to file a return or to furnish a statement under section 6041A and this section, see sections 6652 and 6678 of the Code. For provisions relating to the penalty for failure to supply identification numbers under this section, see section 6676.

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

(Filed by the of the Federal Register on January 6, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 7, 1986, 51 F.R. 619)

Notice of Proposed Rulemaking

Accounting for Long-term Contracts; Corporations Filing Consolidated Returns With a Contractor

LR-121-85

SUMMARY: * * * [T]he Internal Revenue Service is issuing a Treasury decision, adopting final regulations relating to accounting for long-term contracts. This document contains a notice of proposed rulemaking to amend the regulations adopted by that Treasury decision. The amendments clarify how certain rules of the Treasury decision apply in the case of certain corporations which produce components or subassemblies and with which the contractor joins in filing a consolidated return.

DATES: Written comments and requests for a public hearing must be delivered or mailed by March 7, 1986. The proposed regulations are proposed to be effective on January 6, 1986 and would apply to taxable years ending after such date.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T, (LR-121-85) Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Paulette Chernyshev of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T (202-566-3288, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 451 of the Internal Revenue Code of 1954 which have been adopted by Treasury decision and published * * * [on page 5, this Bulletin]. The Treasury decision provides that the beginning of manufacture by the taxpayer of components and subassemblies related to a contract can constitute the contract commencement date, and that the taxpayer must use the extended period costing rules for components and subassemblies produced by the taxpayer which reasonably can be expected to be incorporated into the subject matter of extended period long-term contracts. These amendments are proposed to extend the rules set forth in the preceding sentence to certain corporations with which the taxpayer joins in filing a consolidated return.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required. Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the notice and public procedure requirements of 5 U.S.C. 553 do not apply because the rules proposed are interpretative. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these proposed regulations is Paulette Chernyshev of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and the Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Proposed amendments to regulations

The proposed amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805 * * *

Section 1.451-3 amended under the authority in 96 Stat. 324, 493.

Par. 2. Section 1.451-3 is amended as follows:

1. Paragraph (b) is amended by adding a sentence to the end of paragraph (b)(3)(v) as set forth below:

2. Paragraph (d) is amended by adding a sentence to the end of paragraph (d)(6)(iv) as set forth below.

The added language reads as follows:

§1.451-3 Long-term contracts.

(b) *Definitions, and special rules relating to certain contracts.* * * *

(3) *Extended period long-term contract.* * * *

(v) *Special rule for contract commencement date in case of components or subassemblies produced by the taxpayer.* * * * For taxable years ending after the date the Treasury decision based on these proposed amendments is published in the Federal Register, the term "taxpayer" as used in this paragraph (b)(3)(v) includes members of a group with which the taxpayer joins in the filing of a consolidated return if such group does not elect not to defer gains and losses on intercompany transactions (See §1.1502-13(c)(3)).

§1.451-3 Long-term Contracts

(d) *Completed contract method.* * * *

(6) *Allocation of costs to extended*

period long-term contracts. * * *

(iv) *Special rule for component parts or subassemblies produced by the taxpayer.* * * *

For taxable years ending after the date the Treasury decision based on these proposed amendments is published in the Federal Register, the term "taxpayer" as used in this paragraph (d)(6)(iv) includes members of a group with which the taxpayer joins in the filing of a consolidated return if such group does not elect not to defer gains and losses on intercompany transactions (See §1.1502-13(c)(3)).

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on December 30, 1985, 3:12 p.m., and published in the issue of the Federal Register for January 6, 1986, 51 F.R. 401)

Deletions from Cumulative List of Organizations Contributions to Which Are Deductible Under Section 170 of the Code

Announcement 86-14

The names of organizations that no longer qualify as organizations described in section 170(c)(2) of the Internal Revenue Code of 1954 are listed below.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgment has been timely field, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deducible. Protection under section 7428(c) would begin on February 10, 1966, (the date of publication of this announcement) and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is $1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

DKT International Fund, Ltd.,
New York, NY

Medical Future Foundation, Inc.,
Palm Beach, FL

Substantiation Requirements With Respect to Listed Property; Limitations Applicable to Lessees of Passenger Automobiles—Public Hearing

Announcement 86-18 [1]

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to the requirements to substantiate certain deductions and credits claimed with respect to "listed property," and the limitations on the investment credit and deductions for lease payments that apply to certain lessees of passenger automobiles.

DATES: The public hearing will be held on Monday, March 3, 1986, beginning at 10:00 a.m. If necessary to accommodate all speakers, the public hearing will be reconvened on Tuesday, March 4, 1986, at 10:00 a.m. Outlines of oral comments must be delivered or mailed by February 17, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, Attn: CC:LR:T (LR-145-85), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: B. Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, 202-566-3935, not a toll-free call.

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed and temporary regulations under sections 61, 132, 162, 274, and 280F of the Internal Revenue Code of 1954. These regulations first appeared in the Federal Register for Wednesday, November 6, 1985 (50 FR 46088 [LR-145-84, 1985-46 I.R.B. 47] and 50 FR 46006 [T.D. 8061, 1985-46 I.R.B. 7]). Portions of the regulations then appeared in revised format in the Federal Register for Monday, December 23, 1985 (50 FR 52281) [T.D. 8063, 1986-3 I.R.B. 4]. These regulations relate to the requirement to substantiate certain business expenses with adequate records or sufficient corroborative evidence, the limitations on the investment credit and deductions for lease payments that apply to certain lessees of passenger automobiles, and certain substantiation rules related to the taxation of fringe benefits.

The following specific topics are covered in the regulations published on November 6, 1986, and will be the subject of the public hearing:

Substantiation requirements (§§1.274-5T and 1.274-6T),

Limitations applicable to lessees of passenger automobiles (§§1.280F-1T and 1.280F-5T),

Deductions with resect to noncash fringe benefits (§1.162-25T),

Special rule for valuing commuting use of employer-provided vehicles (§1.61-2T Q/A-20 through Q/A-21, now §1.61-2T(f), as revised by T.D. 8063, published in the Federal Register for December 23, 1985 (50 FR 52281)), and

Substantiation requirements applicable to a working condition fringe (§ 1.132-1T Q/A-4a and Q/A-4b, now §1.132-5T(c) through (h), as revised by T.D. 8063, published in the Federal Register for December 23, 1985 (50 FR 52281)).

No other provisions of the proposed

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[1] Filed by the Office of the Federal Register on January 21, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 22, 1986, 51 F.R. 2898.

and temporary regulations on the taxation of fringe benefits contained in T.D. 8063, published in the Federal Register for December 23, 1985 (50 FR 52333 and [LR-216-84, 1985-3 I.R.B. 40] 50 FR 52281 [T.D. 8063, 1986-3 I.R.B. 4]), are to be addressed at the hearing. These provisions will be the subject of a separate public hearing to be scheduled in the near future.

Comments on §1.274-5T at the hearing on March 3, are to be limited to the portions of that section that are new. Existing §1.274-5 of the Income Tax Regulations, which was first adopted by Treasury decision in 1962, reflects the addition to the Code of the substantiation requirements of section 274(d). That section of the regulations served as the basis for new temporary regulation §1.274-5T, which reflects the application of section 274(d) to listed property. As published in the Federal Register for November 6, 1985, the portions of §1.274-5T that differ from existing §1.274-5 are underlined. Testimony on the provisions of §1.274-5T should be limited to the underlined portions of that section.

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations, should submit, not later than Monday, February 17, 1986, an outline of the oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions, attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Philip G. Arneson	Sparta, WI	Attorney	Indefinite from December 15, 1985
Joseph P. Day	Woburn, MA	Attorney	Indefinite from December 24, 1985
Kenneth H. Dillard	Nashville, TN	Certified Public Accountant	Indefinite from December 31, 1985
LeRoy Hodge	Hamilton, NY	Attorney	Indefinite from December 10, 1985
Frank S. Lukuch	Barberton, OH	Certified Public Accountant	Indefinite from December 4, 1985
W. Stephen McConnell	Tampa, FL	Certified Public Accountant	Indefinite from December 26, 1985
Nathan Rich	Wilmington, DE	Certified Public Accountant	Indefinite from December 1, 1985
Walter E. Shettlemore	Long Beach, MS	Certified Public Accountant	Indefinite from December 20, 1985

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.61-2T, removed; new 1.61-2T, added; 1.132-1T, removed; new 1.1.32-1T, added; 1.132-2T through 1.132-8T, added; 1.162-25T, 1.274-5T, 1.274-6T, amended.	Taxation of fringe benefits and exclusions from gross income of certain fringe benefits	1986-3 I.R.B. 40	Feb. 21, 1986
26 CFR 1.43-3(e), revised 1.47-1, 1.48-9, 1.167(a)-11, amended	Recapture of investment credit for mass assets	1986-4 I.R.B. 42	Feb. 18, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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*Denotes entry since last publication

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-19, page 4.

Credit for producing fuel from a nonconventional source. After December 31, 1984, gas produced from a tight formation that also falls under any of the categories of gas specified in 18 CFR 272.103(a) under the Natural Gas Policy Act of 1978 (NGPA) will no longer be eligible for the credit allowed by section 29 (formerly section 44D) of the Internal Revenue Code.

Rev. Rul. 86-21, page 17.

Corporations; odd-lot purchases of own stock; broker reporting requirements. A corporation that purchases odd-lot shares from its stockholders on an irregular basis is not a broker for purposes of the reporting requirements of section 6045(a) of the Code.

Rev. Rul. 86-22, page 4.

LIFO; price indexes; department stores. The October 1985 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, October 31, 1985.

T.D. 8064, page 18.

LR-236-84, page 26.

Temporary and proposed regulations under section 6050K of the Code relate to information returns, statements, and notifications required when there is a sale or exchange of certain partnership interests.

EXEMPT ORGANIZATIONS

Announcement 86-19, page 31.

A list is given of organizations now classified as private foundations.

Finding Lists begin on page 37.
Announcement of Suspensions on page 35.
Announcement of Notice of Proposed Rulemaking on page 36.

Department of the Treasury
Internal Revenue Service

EMPLOYMENT TAXES

Rev. Proc. 86-8, page 22.

Form 940; credit reductions; computation. The credit against employment tax for amounts paid into the unemployment funds maintained by various states, Puerto Rico, and the Virgin Islands, is reduced for wages paid by employers during 1985 for services performed in those jurisdictions.

EXCISE TAXES

Rev. Rul. 86-20, page 16.

Gas guzzler tax liability. The gas guzzler tax imposed by section 4064 of the Code applies to automobiles imported without a prototype-based fuel economy rating assigned by the Environmental Protection Agency.

Rev. Proc. 86-9, page 22.

Gas guzzler tax; computation of liability. Guidelines are set forth for importers of automobiles to compute gas guzzler tax liability under section 4064 of the Code for automobiles that are imported without a fuel economy rating assigned by the Environmental Protection Agency.

T.D. 8066, page 4.

Amendments to the regulations under section 4041 of the Code relate to the retail excise tax on special fuels.

EMPLOYEE PLANS

Announcement 86-20, page 34.

Group legal services plans, cafeteria plans, and educational assistance plans are required to file an annual return for years beginning after December 31, 1984. The return should be filed on either Form 5500, Form 5500-C, or Form 5500-R. These forms have been revised and are now available.

ADMINISTRATIVE

LR-59-85, page 26.

Proposed amendments to the regulations relate to information reporting of allowances, or reimbursements, or charges for travel and other expenses of public employees and certain other persons.

Announcement 86-17, page 27.

Publication 1212, List of Original Issue Discount Instruments (Revised December 1985), contains incorrect information in Section I-B. The corrected information is provided in this Announcement and will also be available from IRS Distribution Centers together with Publication 1212.

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 29—Credit for Producing Fuel from a Nonconventional Source

Credit for producing fuel from a nonconventional source. After December 31, 1984, gas produced from a tight formation that also falls under any of the categories of gas specified in 18 CFR 272.103(a) under the Natural Gas Policy Act of 1978 (NGPA) will no longer be eligible for the credit allowed by section 29 (formerly section 44D) of the Internal Revenue Code.

Rev. Rul. 86-19

Section 29(a) of the Code (formerly Section 44D(a)) provides a credit against income tax of $3 per barrel-of-oil equivalent of qualified fuels sold by the taxpayer during the taxable year, subject to stated conditions. Section 29(c)(1)(B) provides that the term "qualified fuels" includes "gas produced from . . . a tight formation." However, section 29(c)(2)(B)(i) provides that the term "gas produced from a tight formation" shall only include gas the price of which is regulated by the United States.

Section 121 of the Natural Gas Policy Act of 1978, Pub. L. No. 95-621, 15 U.S.C. section 3331 (1982) (NGPA) eliminated price controls as of January 1, 1985, on certain categories of natural gas classified under section 102(c) and section 103(c) of the NGPA. The Federal Energy Regulatory Commission (FERC) has issued regulations concerning the types of gas that were deregulated by section 121. *See* 49 Fed. Reg. 46,874 (Nov. 29, 1984). These regulations include amendments to 18 C.F.R. section 272.103(a), which defines "deregulated natural gas." *See* 49 Fed. Reg. 46,884. The FERC also decided that gas is deregulated if it falls into two or more categories any one of which is a deregulated category. *See* 49 Fed. Reg. 46,877-79.

Thus, gas produced and sold after December 31, 1984, that falls under any of the categories listed in 18 C.F.R. section 272.103(a) (as amended) is gas the price of which is not regulated by the United States. Gas produced from a tight formation is generally classified as section 107(c)(5) gas under the NGPA. However, a considerable amount of section 107(c)(5) gas also is classified as section 102 or 103 gas. Thus, if gas from a tight formation also qualifies under section 102 of 103, it is deregulated for purposes of the NGPA. In accordance with section 29(c)(2)(B)(i) of the Code, even if such gas would otherwise qualify as gas produced from a tight formation, it is not a qualified fuel under section 29(c), and producers of the gas are not eligible for the credit allowed by section 29(a).

Section 472.—Last-in, First-out Inventories

26 CFR 1.472-1: Last-in, first-out inventories.

LIFO; price indexes; department stores. The October 1985 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, October 31, 1985.,

Rev. Rul. 86-22

The price indexes (appearing at the top of page 5) for October 1985 were issued by the Bureau of Labor Statistics on November 26, 1985, for use by department stores, and are accepted by the Internal Revenue Service, under section 1.472-1(k) of the Income Tax Regulations and Rev. Proc. 72-21, 1972-1 C.B. 745, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, October 31, 1985.

Indexes are prepared on a national basis for the store total, for 20 major groups of departments, and for two special combinations—soft and durable goods. The store total index covers all departments, including some not listed separately, with the following exceptions: candy, foods, liquor, tobacco, paints, and wallpaper, as well as contract departments.

Section 3302.—Credits Against Tax

26 CFR 31.3302(c)-1: Limit on total credits.

Reductions (for 1985) in credit applicable to employers for whom services are performed in various "states." See Rev. Proc. 86-8, page 22.

Section 4041.—Imposition of Tax [Special Fuels]

26 CFR 48.4041-1: Taxes on diesel fuel, special motor fuel, and fuel used in noncommercial aviation.

T.D. 8066

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER D, SUBCHAPTER H, PART 48—MANUFACTURERS AND RETAILERS EXCISE TAXES; PART 154—TEMPORARY REGULATIONS IN CONNECTION WITH THE AIRPORT AND AIRWAY REVENUE ACT OF 1970; PART 602—REPORTING AND RECORDKEEPING REQUIREMENTS

Retail Excise Tax on Special Fuels

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document provides final regulations which revise and update the regulations relating to excise taxes on special fuels. Changes to the applicable law were made by the Excise Tax Reduction Act of 1965 [Pub. L. 98-44, 1965-2 C.B. 568], the Airport and Airway Revenue Act of 1970 [Pub. L. 91-258, 1970-1 C.B. 361], the Energy Tax Act of 1978, [Pub. L. 95-618, 1978-3 C.B. (Vol. 2) 1], the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462], the Surface Transportation Assistance Act of 1982 [Pub. L. 97-424, 1983-1 C.B. 405], and the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1]. These regulations provide necessary guidance to the public for compliance with the law and affect sales or uses of diesel fuel, special motor fuels and fuels for use in noncommercial aviation.

DATES: Except as otherwise provided in this document, the regulations are effective for sales or uses of diesel fuel, special motor fuels and fuels for use in an aircraft after December 31, 1954.

FOR FURTHER INFORMATION CONTACT: William A. Jackson of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224,

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS

(January 1941 = 100)

		October 1984	October 1985	Percentage Change from: October 1984 to October 1985[1]
I.	Piece Goods	393.6	396.2	0.7
II.	Domestics and Draperies	559.8	549.7	−1.8
III.	Women's and Children's Shoes	559.4	549.3	−1.8
IV.	Men's Shoes	709.2	717.8	1.2
V.	Infants' Wear	480.9	496.9	3.3
VI.	Women's Underwear	424.9	442.4	4.1
VII.	Women's and Girls' Hosiery	233.4	233.9	0.2
VIII.	Women's and Girls' Accessories	446.4	453.5	1.6
IX.	Women's Outerwear and Girls' Wear	356.3	367.6	3.2
X.	Men's Clothing	474.6	481.5	1.5
XI.	Men's Furnishings	474.2	490.6	3.5
XII.	Boys' Clothing and Furnishings	443.8	458.3	3.3
XIII.	Jewelry	693.7	671.6	−3.2
XIV.	Notions	479.3	491.1	2.5
XV.	Toilet Articles and Drugs	623.3	648.0	4.0
XVI.	Furniture and Bedding	536.1	540.5	0.8
XVII.	Floor Coverings	454.1	452.1	−0.4
XVIII.	Housewares	706.9	706.6	0.0
XIX.	Major Appliances	242.3	247.3	2.1
XX.	Radio and Television	108.9	101.8	−6.5
	Groups I–XV: Soft Goods	480.0	488.2	1.7
	Groups XVI–XX: Durable Goods	444.2	443.2	−0.2
	Store Total	469.7	475.7	1.3

[1] Absence of a minus sign before percentage change in this column signifies price increase.

Attention: CC:LR:T (202-566-4336, not a toll-free call.)

SUPPLEMENTARY INFORMATION:

BACKGROUND

On October 22, 1980, the FEDERAL REGISTER published proposed amendments to the Manufacturers and Retailers Excise Tax Regulations (26 CFR Part 48) under section 4041 of the Internal Revenue Code of 1954 (Code) (45 FR 69933). The amendments were proposed to conform the regulations to statutory changes made to section 4041 of the Code since 1964. These statutory changes were made by the Excise Tax Reduction Act of 1965 (P.L. 89-44, 79 Stat. 136) [1965-2 C.B. 568], which repealed all retailers excise taxes on articles other than special fuels, and the Airport and Airway Revenue Act of 1970 (P.L. 91-258, 84 Stat. (Part 1) 237) [1970-1 C.B. 361], which imposed a tax under section 4041 of the Code on the use of fuels in noncommercial aviation. A public hearing on the proposed regulations was held on April 8, 1981. After consideration of all comments received concerning the proposed amendments, those amendments are adopted as revised by this Treasury decision. In addition, this Treasury decision revises the proposed regulations by incorporating the statutory changes made to section 4041 by the Energy Tax Act of 1978 (P.L. 95-618, 92 Stat. 3174) [1978-3 C.B. (Vol. 2) 1], which repealed the excise tax reduction for special motor fuels used in a motor vehicle for non-business, off-highway purposes; the Tax Equity and Fiscal Responsibility Act of 1982 (P.L. 97-248, 92 Stat. 324) [1982-2 C.B. 462], which reimposed the tax and increased the rate of tax on fuel used in noncommercial aviation; the Surface Transportation Assistance Act of 1982 (P.L. 97-424, 96 Stat. 2168) [1983-1 C.B. 405], which increased the rate of tax on diesel and special motor fuels and which repealed the excise tax reduction for diesel fuel used in a diesel-powered highway vehicle for non-business, off-highway purposes; and the Tax Reform Act of 1984 (P.L. 98-369, 98 Stat. 1005) [1984-3 C.B. (Vol. 1) 1], which increased the tax on diesel fuel.

PUBLIC COMMENTS

Several public comments were received regarding the proposed regulations. The more significant comments are discussed below.

In response to a comment suggesting the deletion of the temporary regulations under §154.1-1 to confirm that these regulations supersede that section, §154.1-1 has been removed.

Taxable Sales

Sections 48.4041-2(a), 48.4041-2(b), 48.4041-3(a), 48.4041-3(b), 48.4041-4(a), and 48.4041-4(b) all deal with the sales of special fuels. Two commentators requested that the term "sale" as used in these sections be changed to "taxable sale". The commentators were concerned that, absent this change, some sales, not taxable in fact, might be presumed to be taxable. In response to the comments, the suggested changes were made.

Bulk Sales

Sections 48.4041-5 and 48.4041-6 established general rules on fuels sold or used, including rules on bulk sales. Commentators suggested amending §48.4041-5(a)(2)(ii) and §48.4041-6(b) to make it clear that a taxable bulk sale has not occurred unless the seller acknowledges in writing the receipt of the purchaser's statement that the bulk sale was taxable. This would protect a seller from the later claim of a purchaser that such a statement was delivered when this was not the case. The final regulations do not adopt this request because the seller's liability for the tax would then depend upon the seller's acknowledgement and this would defeat the purpose of the regulation.

Section 48.4041-5(a)(2) also establishes requirements for purchasers who make bulk purchases from a single seller for both taxable and nontaxable purposes. These sales may be treated as only partially taxable if proper records are kept and certain other requirements are satisfied. Two commentators requested adding language to §48.4041-5(a)(2) stating that the recordkeeping burden is on the purchaser, not the seller, because the information for such records is within the control of the purchaser, not the seller. The final regulations adopt this suggestion.

Consignments

Section 48.4041-5(b)(2) concerns consignments which are generally not taxable. Tax is due on the later sale of the fuel by the consignee on behalf of the consignor where the fuel is sold for taxable use. Consistent with the suggestions of the comments, §48.4041-5(b)(2) was changed to make it clear that the owner of the fuel at the time of the taxable sale is the person liable for the tax.

Registered Highway Vehicles

Two commentators requested that the definition of "registered highway vehicle" in §48.4041-8(i)(2) be changed to exclude vehicles operated pursuant to special permits "for operation at particular times and under specified conditions." These vehicles were considered registered highway vehicles under the proposed regulations. Under the final regulations, a vehicle will not be considered registered solely by reason of the fact that a special permit has been issued.

Noncommercial Aviation

Another commentator requested that §48.4041-8(j) be rewritten to define noncommercial aviation so as to exclude from the tax imposed by section 4041 special fuel used in "carriage for hire" which is only an "incidental" use as opposed to a major enterprise for profit. The final regulations do not adopt this position because it is not authorized under section 4041(c).

The commentators suggested that a "good faith", rather than "reasonable diligence", test should be imposed on sellers under §48.4041-11(d)(5), relating to tax-free sales of fuel for use in noncommercial aviation. It was determined, however, that sellers should exercise reasonable diligence in ascertaining that the liquid fuel is not being used in noncommercial aviation.

PAPERWORK REDUCTION ACT

The collection of information requirements contained in these final regulations have been submitted to the Office of Management and Budget (OMB) for review under the Paperwork Reduction Act. These regulations have been approved by OMB (control number 1545-0023).

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. Although a notice of proposed rulemaking which solicited public comments was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirement of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. 6).

DRAFTING INFORMATION

The principal author of this regulation is William A. Jackson of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulation, both on matters of substance and style.

* * * * *

Adoption of Amendments to the regulations

Accordingly, 26 CFR Parts 48, 154 and, 602 are amended as follows:

Paragraph 1. The authority citation for Part 48 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 2. Sections 48.4041, 48.4041-1, and 48.4041-2 are removed and new §§48.4041-1 and 48.4041-2 are added immediately after §48.0-5 and the heading for subpart B-E. The new sections read as follows:

Subpart F—Special Fuels

§48.4041-1 Taxes on diesel fuel, special motor fuel, and fuel used in noncommercial aviation.

(a) *In general*. Section 4041 imposes an excise tax at the retail level on the sale of diesel fuel for use as a fuel in a diesel-powered highway vehicle, special motor fuel for use as a fuel in a motor vehicle or motorboat, and fuel for use in an aircraft in noncommercial aviation. A tax is also imposed when these liquid fuels are purchased tax-free and subsequently used for one of the above-mentioned purposes, or when these liquid fuels are purchased at one rate of tax and a higher rate of tax applies as a result of the use made of the liquid fuels.

(b) *Rates of tax*. Following are the rates of tax per gallon applicable to liquid fuels taxable under section 4041.

(1) *Diesel fuels.* (i) Before April 1, 1983, diesel fuel sold for use or used as a fuel in a diesel-powered highway vehicle that at the time of the sale or use is—

(A) Registered or required to be registered for highway use—4 cents

(B) Owned by the United States and used on the highway—4 cents

(C) Not registered and not required to be registered for highway use—2 cents

(D) Owned by the United States and not used on the highway—2 cents

(E) A vehicle described in paragraphs (b)(1)(i)(A) or (B) of this section in which the fuel that is used before April 1, 1983, was purchased at the rate of 2 cents a gallon for use in a vehicle described in paragraphs (b)(1)(i)(C) or (D) of this section, an additional—2 cents.

(F) A vehicle described in paragraphs (b)(1)(i)(A) or (B) of this section in which the fuel that is used on or after April 1, 1983, and before August 1, 1984, was purchased before April 1, 1983, at a rate of 2 cents a gallon for use in a vehicle described in paragraphs (b)(1)(i)(C) or (D) of this section, an additional—7 cents

(G) A vehicle described in paragraphs (b)(1)(i)(A) or (B) of this section in which the fuel that is used on or after August 1, 1984, and before October 1, 1988, was purchased before April 1, 1983, at a rate of 2 cents a gallon for use in a vehicle described in paragraphs (b)(1)(i)(C) or (D) of this section, an additional—13 cents.

(ii) On or after April 1, 1983, and before August 1, 1984, diesel fuel—

(A) Sold by any person to an owner, lessee, or other operator of a diesel-powered highway vehicle for use as a fuel in such a vehicle—9 cents

(B) Used by any person as a fuel in a diesel-powered highway vehicle, unless there was a tax imposed by reason of paragraphs (b)(1)(i) or (ii)(A) of this section—9 cents

(C) Sold for use or used in an off-highway business—no tax

(D) On which no tax was imposed by reason of paragraph (b)(1)(ii)(C) of this section, relating to an off-highway business use, and is used before August 1, 1984, in other than an off-highway business use—9 cents

(E) Sold before August 1, 1984, and on which no tax was imposed by reason of paragraph (b)(1)(ii)(C) of this section, relating to off-highway business use, and is used on or after August 1, 1984, in other than an off-highway business use—15 cents. For purposes of paragraphs (b)(1)(iii)(C), (D), and (E) of this section, the term "off-highway business use" has the same meaning given to such term by section 6421(d)(2).

(iii) On or after August 1, 1984, and before October 1, 1988, diesel fuel—

(A) Sold by any person to an owner, lessee, or other operator of a diesel-powered highway vehicle for use as a fuel in such a vehicle—15 cents

(B) Used by any person as a fuel in a diesel-powered highway vehicle, unless there was a tax imposed by reason of paragraphs (b)(1)(i), (ii), or (iii)(A) of this section—15 cents

(C) Sold for use in an off-highway business use—no tax

(D) On which no tax was imposed by reason of paragraph (b)(1)(iii)(C) of this section, relating to an off-highway business use, and which is used in other than an off-highway business use—15 cents. For purposes of paragraphs (b)(1)(iii)(C) and (D) of this section, the term "off-highway business use" has the same meaning given to such term by section 6421(d)(2).

(2) *Special motor fuels.* (i) On or after January 1, 1979, and before April 1, 1983, special motor fuel—

(A) Sold by any person to an owner, lessee or other operator of a motor vehicle or motorboat for use as fuel in such motor vehicle or motorboat—4 cents

(B) Used by any person as a fuel in a motor vehicle or motorboat, unless there was a taxable sale of such liquid under paragraph (b)(2)(i) of this section—4 cents

(C) Sold for use or used in a qualified business use, the tax imposed under paragraph (b)(2)(i)(A) and (B) of this section is—2 cents

(D) On which tax was imposed at a rate of 2 cents a gallon by reason of paragraph (b)(2)(i)(C) of this section, relating to a qualified business use, is used in other than a qualified business use, an additional—2 cents

(E) Sold before April 1, 1983, and on which tax was imposed at a rate of 2 cents a gallon by reason of paragraph (b)(2)(i)(C) of this section, relating to qualified business use, and which is used on or after April 1, 1983, and before October 1, 1988, in other than an off-highway business use, an additional—7 cents. For purposes of paragraphs (b)(2)(i)(C) and (D) of this section, the term "qualified business use" has the same meaning as that given to the term "off-highway business use" by section 6421(d)(2).

(ii) On or after April 1, 1983, and before October 1, 1988, special motor fuel—

(A) Sold by any person to an owner, lessee or other operator of a motor vehicle or motorboat for use as a fuel in such motor vehicle or motorboat—9 cents

(B) Used by any person as a fuel in a motor vehicle or motorboat, unless there was a tax imposed by reason of paragraph (b)(2)(i) or (ii)(A) of this section—9 cents

(C) Sold for use or used in an off-highway business use—no tax

(D) On which no tax was imposed by reason of paragraph (b)(2)(ii)(C) of this section relating to an off-highway business use, which and is used in other than an off-highway business use—9 cents. For purposes of paragraphs (b)(2)(ii)(C) and (D) of this section, the term "off-highway business use" has the same meaning given to such term by section 6241(d)(2).

(3) *Noncommercial aviation.* (i) On or after July 1, 1970, and before October 1, 1980, any liquid—

(A) Other than any product taxable under section 4081, that is—

(*1*) Sold by any person to an owner, lessee or other operator of an aircraft, for use as a fuel in such aircraft in noncommercial aviation—7 cents

(*2*) Used by any person as a fuel in an aircraft in noncommercial aviation, unless there was a taxable sale of such liquid under paragraph (b)(3)(i)(A)(*1*) of this section—7 cents

(B) That is taxable under section 4081 and that is—

(*1*) Sold by any person to an owner, lessee or other operator of an aircraft for use as a fuel in such aircraft in noncommercial aviation—3 cents

(*2*) Used by any person as a fuel in an aircraft in noncommercial aviation, unless there was a taxable sale of such liquid under paragraph (b)(3)(i)(B)(*1*)—3 cents.

(ii) On or after October 1, 1980, and

before September 1, 1982, any liquid sold for use or used as a fuel in an aircraft in noncommercial aviation—no tax.

(iii) On or after September 1, 1982, and before January 1, 1988, any liquid—

(A) Other than any product taxable under section 4081, that is—

(1) Sold by any person to an owner, lessee or other operator of an aircraft for use as a fuel in such aircraft in noncommercial aviation—14 cents

(2) Used by any person as a fuel in an aircraft in noncommercial aviation, unless there was a tax imposed by reason of paragraph (b)(3)(i)(A)*(1)* or (iii)(A)*(1)* of this section, or unless no tax was imposed by reason of paragraph (b)(3)(ii) of this section—14 cents

(3) Used by any person as a fuel in an aircraft in noncommercial aviation where tax was imposed on the sale of such liquid—the excess of the rate set forth in paragraph (b)(3)(iii)(A)(2) of this section over the tax imposed on the sale

(B) That is taxable under section 4081 and that is—

(1) Sold by any person to an owner, lessee or other operator of an aircraft for use as a fuel in such aircraft—the excess of 12 cents a gallon over the rate at which the tax was imposed under section 4081

(2) Used by any person as a fuel in an aircraft in noncommercial aviation, unless there was a tax imposed by reason of paragraph (b)(3)(i)(B)(*1*) or (iii)(B)(*1*) of this section, or unless no tax was imposed by reason of paragraph (b)(3)(ii) of this section—the excess of 12 cents a gallon over the rate of which tax was imposed under section 4081.

(iv) On or after January 1, 1988, any liquid sold for use or used as a fuel in an aircraft in noncommercial aviation—no tax.

(c) *Credit for tax paid.* For a credit or refund for tax paid on diesel fuel, special motor fuel, or fuel used in noncommercial aviation that is resold, or used otherwise than for the purpose for which purchased, see section 6427(a).

§48.4041-2 Application of tax on sales of diesel fuel use in diesel-powered highway vehicles.

(a) *In general*—(1) *Sales of diesel fuel before April 1, 1983.* The tax imposed by paragraph (1) of section 4041(a) applies to the taxable sale of diesel fuel before April 1, 1983, by any person to an owner, lessee, or other operator of a diesel-powered highway vehicle for use as a fuel in the diesel-powered vehicle. The tax applies to diesel fuel sold for use in a diesel-powered highway vehicle, whether the vehicle actually is employed in highway or off-highway use.

(2) *Sales of diesel fuel on or after April 1, 1983, and before October 1, 1988.* The tax imposed by paragraph (1)(A) of section 4041(a) applies to the taxable sale of diesel fuel on or after April 1, 1983, and before October 1, 1988, by any person to an owner, lessee, or other operator of a diesel-powered highway vehicle for use as a fuel in such a vehicle. The tax does not apply to diesel fuel sold for use in an off-highway business use.

(b) *Liability for tax.* The tax on the taxable sale of diesel fuel is payable by the person who sells the diesel fuel to the owner, lessee, or other operator of a diesel-powered highway vehicle.

(c) *Rate of tax*—(1) *In general.* Tax is imposed on the sale of diesel fuel at the rate applicable on the date on which the diesel fuel is sold. See §48.4041-1(b)(1) for rates.

(2) *Diesel fuel sold before April 1, 1983.* For diesel fuel sold before April 1, 1983, for use in a diesel-powered highway vehicle, the test of taxability at the rate specified in §48.4041-1(b)(1)(i)(A) is whether the vehicle in which the fuel is to be used is registered, or required to be registered, for highway use under the laws of any State or foreign country at the time of sale. Tax at a rate specified in that section applies to all fuel sold for use in a diesel-powered highway vehicle which is registered, or required to be registered, for highway use under the laws of any State or foreign country, even though the vehicle is seldom or never used on the highway and regardless of the proportion of the fuel used off the highway as compared to total fuel consumption.

(3) *Diesel fuel sold on or after April 1, 1983, and before October 1, 1988.* For diesel fuel sold for use in a diesel-powered highway vehicle on or after April 1, 1983, and before October 1, 1988, the test of taxability at the rate specified in paragraph (b)(1)(ii)(A) or (iii)(A) of §48.4041-1 is whether the vehicle in which the fuel is to be used is a diesel-powered highway vehicle. The tax applies to all fuel sold for use in a diesel-powered highway vehicles unless the diesel fuel is sold for use or used in an "off-highway business use" as defined in section 6421(d)(2).

(d) *Example.* Application of the tax to the sale of diesel fuel may be illustrated by the following example:

Example. The M Corporation is engaged in the construction of a power dam at a site removed from all public highways. Part of its construction equipment consists of diesel-powered shovels; bulldozers, and highway-type dump trucks. Some of the trucks are registered for highway use and are used both on and off the public roads. Others are not registered and under the applicable State law are not required to be registered for highway use because they are used entirely on the construction site. Before April 1, 1983, the diesel fuel sold for use in the registered dump trucks is all subject to tax at the rate specified in §48.4041-1(b)(1)(i)(A), even though a portion of it is used off the public highway. Before April 1, 1983, the fuel sold for use in the nonregistered trucks, that are operated entirely off the highway, is taxable at the rate specified in paragraph (b)(1)(i)(C) of §48.4041-1. On and after April 1, 1983, and before August 1, 1984, fuel sold for use in the registered trucks is taxable at the rate specified in §48.4041-1(b)(1)(ii)(A), and the fuel sold for use in the nonregistered trucks that are operated entirely off the highway is exempt from tax as specified in §48.4041-1(b)(1)(ii)(C), assuming the trucks are used in off-highway business uses. On and after August 1, 1984, and before October 1, 1988, fuel sold for use in the registered trucks is taxable at the rate specified in §48.4041-1(b)(1)(iii)(A), and fuel sold for use in the nonregistered trucks is exempt from tax as specified in §48.4041-1(b)(1)(iii)(C), assuming the trucks are used in off-highway business uses. No tax is payable with respect to the diesel fuel sold for use in the power shovels and bulldozers, since they are not "highway vehicles" as defined in §48.4041-8(b).

(e) *Cross references.* (1) For the tax applicable in certain cases based on the use of diesel fuel as a fuel in a diesel-powered highway vehicle, see §48.4041-6.

(2) For the definition of the terms "highway", "highway vehicle", "diesel-powered highway vehicle", "diesel fuel", and "registered", see paragraphs (a), (b)(1), (b)(4), (e), and (i) of §48.4041-8, respectively. For the definition of the term "off-highway business use", see section 6421(d)(2).

(3) For the exemption from tax with respect to diesel fuel sold for use on a farm for farming purposes, or as sup-

plies for vessels, see §§48.4041-9 and 48.4041-10, respectively.

(4) For the credit or refund of tax paid on diesel fuel resold or used for a purpose other than the purpose for which purchased, see section 6427(a).

Par. 3. Sections 48.4041-3, 48.4041-4, 48.4041-5, 48.4041-6, 48.4041-7, 48.4041-8, 48.4041-9, and 48.4041-10 are removed, and §§48.4041-11, 48.4041-12, 48.4041-13, and 48.4041-14 are redesignated as §§48.4041-15, 48.4041-16, 48-4041-17, and 48.4041-18, respectively.

Par. 4. The following new sections are added immediately after §48.4041-2T. The new sections read as follows:

§48.4041-3 Application of tax on sales of special motor fuel for use in motor vehicles and motorboats.

(a) *In general.* The tax imposed by paragraph (2)(A) of section 4041(a), (or before April 1, 1983, paragraph (1) of section 4041(b)), applies to the taxable sale of special motor fuel by any person to an owner, lessee, or other operator of a motor vehicle or motorboat, for use as a fuel in the motor vehicle or motorboat. The tax does not apply to special motor fuel sold for use on or after April 1, 1983, and before October 1, 1988, in an off-highway business use.

(b) *Liability for tax.* The tax on the taxable sale of special motor fuel is payable by the person who sells the special motor fuel to the owner, lessee, or other operator of a motor vehicle or motorboat.

(c) *Rate of tax*—(1) *In general.* Tax is imposed on the sale of special motor fuel at the rate applicable on the date on which the special motor fuel is sold. See §48.4041-1(b)(2) for rates. The test of taxability at the rates specified in §48.4041-1(b)(2)(i)(A) and (ii)(A) is whether the fuel is to be used in a motor vehicle or motorboat. For purposes of paragraphs (c)(2) and (3) of this section, the term "qualified business use" has the same meaning as that given to the term "off-highway business use" by section 6421(d)(2).

(2) *Special motor fuel sold for use as a fuel in a motor vehicle.* Tax at the rates specified in paragraphs (b)(2)(i)(A) and (ii)(A) of §48.4041-1 applies in the case of the sale of special motor fuel for use as a fuel in a motor vehicle. Tax at the rates specified in that section applies regardless of whether the motor vehicle is a highway vehicle. However, a reduced rate of tax from that imposed by paragraph (b)(2)(i)(A) of §48.4041-1 is allowed by paragraph (b)(2)(i)(C) of §48.4041-1 if special motor fuel is sold for use in a qualified business use. An exemption from the tax imposed by paragraph (b)(2)(ii)(A) of §48.4041-1 is allowed by paragraph (b)(2)(ii)(C) of §48.4041-1 if the special motor fuel is sold for use in an off-highway business use.

(3) *Special motor fuel sold for use as fuel in a motorboat.* Tax at the rates specified in paragraphs (b)(2)(i)(A) and (ii)(A) of §48.4041-1 applies in the case of the sale of special motor fuel for use as fuel in a motorboat. The qualified business use reduced rate of tax set forth in paragraph (b)(2)(i)(C) of §48.4041-1 and the off-highway business use exemption set forth in paragraph (b)(2)(ii)(C) of §48.4041-1 are not applicable to motorboats unless the motorboat is a vessel employed in the fisheries or whaling business. See section 6421(d)(2)(B).

(d) *Example.* Application of the tax to the sale of special motor fuels may be illustrated by the following example.

Example. The N Company is engaged in the manufacture of ceramic products. It has a vehicle which is used to haul clay from a clay pit to its factory. This vehicle has not been registered for highway use and under the applicable State law is not required to be registered for highway use since none of the hauling of clay is done on public highways. The N Company also uses a ditch digging machine in the vicinity of the clay pit for the construction of drains. A fork lift truck is used to move cartons of merchandise from place to place inside the company's warehouse and to assist in the loading of merchandise onto the company's highway trucks for delivery to purchasers. The highway trucks are registered by the State for use on highways. Special motor fuel is used for the operation of all of these items of equipment. Before April 1, 1983, the special motor fuel sold for use as a fuel in the registered highway trucks is subject to tax at the rate specified in §48.4041-1(b)(2)(i)(A). On or after January 1, 1979, and before April 1, 1983, the special motor fuel sold for use as a fuel in the unregistered truck used to haul clay from the pit to the factory and in the fork lift truck, assuming both of these are used in qualified business uses, is subject to tax at the rate specified in §48.4041-1(b)(2)(i)(C). If the unregistered truck and forklift are not used in qualified business uses, then the special motor fuel sold for use in these vehicles is taxable at the rate specified in §48.4041-1(b)(2)(i)(A) since both are motor vehicles. No tax is payable with respect to the special motor fuel sold for use in the ditch digging machine since that machine is not a motor vehicle. On and after April 1, 1983, and before October 1, 1988, special motor fuel sold for use in the registered trucks is taxable at the rate specified in §48.4041-1(b)(2)(ii)(A) because the trucks are motor vehicles. On and after April 1, 1983, and before October 1, 1988, special motor fuel sold for use in the unregistered truck and the fork lift, assuming that both vehicles are used in off-highway business uses, is exempt from tax as specified in §48.401-1(b)(2)(ii)(C). If the unregistered truck and fork lift are not used in off-highway business uses, then the special motor fuel sold for use in these vehicles is taxable at the rate specified in §48.4041-1(b)(2)(ii)(A) since both are motor vehicles. No tax is payable with respect to the special motor fuel sold for use in the ditch digging machine since that machine is not a motor vehicle.

(e) *Cross reference.* (1) For the tax applicable in certain cases based on the use of special motor fuel as a fuel in a motor vehicle or motorboat, see §48.4041-6.

(2) For the definition of the terms "highway", "motor vehicle", "special motor fuel", and "registered", see paragraphs (a), (c), (f), and (i) of §48.4041-8. For the definition of the term "Off-highway business use", see section 6421(d)(2).

(3) For the exemption from tax with respect to special motor fuel sold for use on a farm for farming purposes or as supplies for vessels, see §§48.4041-9 and 48.4041-10, respectively.

(4) For credit or refund of tax paid on special motor fuel resold or used otherwise than for the purpose for which purchased, see section 6427(a).

§48.4041-4 Application of tax on sales of liquid for use as fuel in aircraft in noncommercial aviation.

(a) *In general.* The taxes imposed by subparagraphs (1)(A) and (2)(A) of section 4041(c) apply to the taxable sale of any liquid by any person to an owner, lessee, or other operator of an aircraft, for use as a fuel in the aircraft in noncommercial aviation.

(b) *Liability of tax.* The tax on the taxable sale of any liquid used as fuel in aircraft in noncommercial aviation is payable by the person who sells the liquid to the owner, lessee, or operator of an aircraft in noncommercial aviation.

(c) *Rate of tax.* Tax is imposed on the sale of liquids used as fuel in aircraft in noncommercial aviation at the rate applicable on the date on which the liquid is sold. See §48.4041-1(b)(3) for rates.

(d) *Cross references.* (1) For the tax applicable on the basis of the use of fuel in an aircraft in noncommercial aviation, see §48.4041-6.

(2) For the definition of the term "noncommercial aviation", see paragraph (j) of §48.4041-8.

(3) For the exemption of tax with respect to liquids used as fuel in aircraft in noncommercial aviation sold for use on a farm for farming purposes or as supplies for vessels or aircraft, see §§48.4041-9 and 48.4041-10, respectively. For tax-free sales if sellers and purchasers are registered, see §48.4041-11.

(4) For credit or refund of tax paid on fuel used in noncommercial aviation that is resold or used otherwise than for the purpose for which purchased, see section 6427(a).

(e) *Effective date.* The provision of this section shall apply to sales or uses occurring before October 1, 1980, and to sales or uses occurring on or after September 1, 1982, and ending before January 1, 1988.

§48.4041-5 Sales of diesel and special motor fuels and fuel for use in aircraft; rules of general application.

(a) *Taxability of liquid fuel delivered into purchaser's tanks—(1) Fuel supply tanks.* The sale of diesel fuel to an owner, lessee, or other operator of a diesel-powered highway vehicle, or of special motor fuel to an owner, lessee, or other operator of a motor vehicle or motorboat, or of fuel to an owner, lessee, or other operator of an aircraft used in noncommercial aviation is considered a taxable sale of the liquid fuel if the liquid fuel is delivered by the seller into the fuel supply tank of the vehicle, motorboat, or aircraft. For purposes of this paragraph (a), liquid fuel sold at a location unattended by the seller (such as under a meter system) is considered to be delivered into the fuel supply tank by the seller. In this regard, see section 6427(a) for credit or refund of tax if liquid fuel acquired in a transaction subject to tax is used in a nontaxable use.

(2) *Bulk tanks.* The sale of diesel fuel to an owner, lessee, or other operator of a diesel-powered highway vehicle, or of special motor fuel to an owner, lessee, or other operator of a motor vehicle or motorboat, or of fuel to an owner, lessee, or other operator of an aircraft used in noncommercial aviation is considered a taxable sale of the liquid fuel of—

(i) The liquid fuel is delivered by the seller into a bulk supply tank (or other container) that is not the fuel supply tank of a vehicle, motorboat, or aircraft; and

(ii) The purchaser furnishes a written statement to the seller before or at the time of the sale stating that the entire quantity of the liquid fuel covered by the sale is for use by it for a taxable purpose as a fuel in such a vehicle, motorboat, or aircraft.

If the purchaser fails to provide the written statement required by paragraph (a)(2)(ii) of this section, the purchaser is liable for the tax on the later taxable sale or use. If a purchaser acquires both fuel that is to be used for taxable purposes and fuel that is to be used for nontaxable purposes, and the fuel that is to be used for taxable purposes is stored in a different storage tank (or container) from the tank used to store the fuel to be used for nontaxable purposes, the written statement described in paragraph (a)(2)(ii) of this section will relate to the fuel to be used for taxable purposes if proper records are kept by the purchaser that sufficiently identify the tanks (or containers) into which tax-paid fuel is delivered and the quantities of fuel delivered into those tanks (or containers). If only occasional sales for delivery into a bulk storage tank (or other container) are made to a purchaser, a separate statement must be furnished for each order. However, if sales are regularly or frequently made to a purchaser, a written statement covering all orders for a specified period not to exceed 12 calendar quarters is acceptable.

(b) *Sales for resale and to consignees.* (1) A sale to a dealer for resale is not subject to tax even if it is known at the time of the sale that the liquid fuel will be resold by the dealer for use as a fuel in a diesel-powered highway vehicle, motor vehicle, motorboat, or aircraft.

(2) The tax is payable by the person who makes the taxable sale. If a taxable liquid fuel is consigned to a person for sale and the consignor retains ownership in the liquid fuel until it is disposed of by the consignee, the consignor is the person liable for the tax when a taxable sale of the liquid fuel is made by the consignee. If the consignor transfers ownership in the taxable liquid fuel to the consignee before sale of the liquid fuel by the consignee, the consignee is the person liable for the tax upon a subsequent taxable sale of the liquid. However, if ownership of the liquid fuel is transferred back to the consignor or to another person before a taxable sale is made, as described in paragraph (a) of this section, and thereafter a taxable sale of the liquid fuel is made by such person or by another person acting as the person's agent, such person is liable for the tax. See paragraph (d) of §48.4041-8 for definition of the term "taxable liquid fuel."

§48.4041-6 Application of tax on use of taxable liquid fuel.

(a) *In general—*(1) *Diesel fuel.* (i) If, before April 1, 1983, a person acquires any diesel fuel by any means other than through a transaction subject to tax under section 4041(a)(1) and uses it as a fuel in a diesel powered highway vehicle, the person is liable for a tax under section 4041(a)(2) on the quantity of diesel fuel so used at the appropriate rate set forth in §48.4041-1(b)(1)(i). If a person acquired any diesel fuel through a transaction which is subject to tax at the rate set forth in paragraph (b)(1)(i)(C) or (D) of §48.4041-1 and uses it for a use described in paragraph (b)(1)(i)(A) or (B) of §48.4041-1, the person is liable for an additional tax under section 4041(a)(2) on the quantity of diesel fuel so used. See §48.4041-1(b)(1)(i)(E), (F), or (G) for the applicable rate of tax. See section 6427(a) for credit or refund of tax where diesel fuel acquired in a transaction subject to tax at the rate set forth in paragraph (b)(1)(i)(A) or (B) of §48.4041-1 is used as described in paragraph (b)(1)(i)(C) or (D) of §48.4041-1 or in a nontaxable use.

(ii) On or after April 1, 1983, and before August 1, 1984, if a person acquires any diesel fuel by any means other than through a transaction subject to tax under section 4041(a)(1)(A) and uses it as a fuel in a diesel-powered highway vehicle, the person is liable for a tax under section 4041(a)(1)(B) on the quantity of diesel fuel so used at the appropriate rate set forth in paragraph (b)(1)(ii) of §48.4041-1. If a person acquired any diesel fuel through a transaction for which no tax is imposed by reason of paragraph (b)(1)(ii)(C) of §48.4041-1 and uses it in other than a nontaxable use, the person is liable for a tax under section 4041(a)(1)(B) on the quantity of fuel so used. See paragraph (b)(1)(ii)(D) or (E) of §48.4041-1 for the applicable rate of tax. See section 6427(a) for credit or refund of tax where diesel fuel acquired in a transaction subject to tax at the rate set forth in paragraph (b)(1)(ii)(A) of §48.4041-1 is used as described in paragraph (b)(1)(ii)(C) of §48.4041-1 or in another nontaxable use

(iii) On or after August 1, 1984, and before October 1, 1988, if a person acquires any diesel fuel by any means other than through a transaction subject to tax under section 4041(a)(1)(A) and uses it as a fuel in a diesel-powered highway vehicle, the person is liable for a tax under section 4041(a)(1)(B) on the quantity of diesel fuel so used at the appropriate rate set forth in paragraph (b)(1)(iii) of §48.4041-1. If a person acquired any diesel fuel through a transaction for which no tax is imposed by reason of paragraph (b)(1)(iii)(C) of §48.4041-1 and uses it in other than a nontaxable use, the person is liable for a tax under section 4041(a)(1)(B) on the quantity of fuel so used. See paragraph (b)(1)(iii)(D) of §48.4041-1 for the applicable rate of tax. See section 6427(a) for credit or refund of tax where diesel fuel acquired in a transaction subject to tax at the rate set forth in paragraph (b)(1)(iii)(A) of §48.4041-1 is used as described in paragraph (b)(1)(iii)(C) of §48.4041-1 or in another nontaxable use.

(2) *Special motor fuel.* (i) On or after January 1, 1979, and before April 1, 1983, if a person acquired any special motor fuel by any means other than through a transaction subject to tax under section 4041(b)(1) and uses it as a fuel in a motor vehicle or motorboat; the person is liable for a tax under section 4041(b)(2) on the quantity of special motor fuel so used at the appropriate rate set forth in §48.4041-1(b)(2)(i). If a person acquired any special motor fuel through a transaction which is subject to a tax at the rate set forth in paragraph (b)(2)(i)(C) of §48.4041-1 and uses it in a use other than one for which the reduced rate applies, the person is liable for an additional tax under section 4041(b)(2) on the quantity of special motor fuel so used. See §48.4041-1(b)(2)(i)(D) or (E) for the applicable rate of tax. See section 6427(a) for credit or refund of tax where special motor fuel acquired in a transaction subject to tax at the rate set forth in paragraph (b)(2)(i)(A) of §48.4041-1 is used for a purpose described in paragraph (b)(2)(i)(C) of §48.4041-1 or in a nontaxable use.

(ii) On or after April 1, 1983, and before October 1, 1988, if a person acquired any special motor fuel by any means other than through a transaction subject to tax under section 4041(a)(2)(A) and uses it as a fuel in a motor vehicle or motorboat, the person is liable for a tax under section 4041(a)(2)(B) on the quantity of special motor fuel so used at the appropriate rate set forth in paragraph (b)(2)(ii) of §48.4041-1. If a person acquired any special motor fuel through a transaction for which no tax is imposed by reason of paragraph (b)(2)(ii)(C) of §48.4041-1 and uses it in other than a nontaxable use, the person is liable for a tax under section 4041(a)(2)(B) on the quantity of fuel so used. See paragraph (b)(2)(ii)(D) of §48.4041-1 for the applicable rate of tax. See section 6427(a) for credit or refund of tax where special motor fuel acquired in a transaction subject to tax at the rate set forth in paragraph (b)(2)(ii)(A) of §48.4041-1 is used for a purpose described in paragraph (b)(2)(ii)(C) of §48.4041-1 or in another nontaxable use.

(3) *Noncommercial aviation.* If a person acquires any liquid fuel by any means other than through a transaction subject to tax under section 4041(c)(1)(A) or section 4041(c)(2)(A) and uses it as fuel in an aircraft in noncommercial aviation, the person liable for a tax under section 4041(c)(1)(B) or section 4041(c)(2)(B) on the quantity of the liquid fuel so used at the appropriate rate set forth in §48.4041-1(b)(3).

(b) ***Bulk purchases by users.*** Taxpayers who purchase taxable liquid fuel in bulk delivered into storage tanks or other containers and use it for taxable or nontaxable purposes or in registered and nonregistered vehicles must maintain adequate records of all fuel used for each purpose to permit verification of the tax paid and of any credits, refunds, or exemptions claimed.

§48.4041-7 Dual use of taxable liquid fuel.

Tax applies to all taxable liquid fuel sold for use or used as a fuel in the motor which is used to propel a diesel-powered highway vehicle or in the motor used to propel a motor vehicle, motorboat, or aircraft, even though the motor is also used for a purpose other than the propulsion of the vehicle, motorboat, or aircraft. Thus, if the motor of a diesel-powered highway vehicle or a motorboat operates special equipment by means of a power take-off or power transfer, tax applies to all taxable liquid fuel sold for this use or so used, whether or not the special equipment is mounted on the vehicle or boat. For example, tax applies to diesel fuel sold to operate the mixing unit on a concrete mixer truck if the mixing unit is operated by means of a power take-off from the motor of the vehicle. Similarly, tax applies to all taxable liquid fuel sold for use or used in a motor propelling a fuel oil truck even though the same motor is used to operate the pump (whether or not mounted on the truck) for discharging the fuel into customers' storage tanks. However, tax does not apply to liquid fuel sold for use or used in a separate motor to operate special equipment (whether or not the equipment is mounted on the vehicle). If the taxable liquid fuel used in a separate motor is drawn from the same tank as the one which supplies fuel for the propulsion of the vehicle, a reasonable determination of the quantity of taxable liquid fuel used in such separate motor or during such period is acceptable for purposes of application of the tax. This determination must be based, however, on the operating experience of the person using the taxable liquid fuel, and the taxpayer must maintain records which support the allocation used. Devices to measure the number of miles the vehicle has traveled, such as hubometers, may be used in making a preliminary determination of the number of gallons of fuel used to propel the vehicle. In order to make a final determination of the number of gallons of fuel used to propel the vehicle, there must be added to this preliminary determination the amount of fuel consumed while idling or warming up the motor preparatory to propelling the vehicle.

§48.4041-8 Definitions.

For purposes of the regulations in this subpart, unless otherwise expressly indicated:

(a) *Highway*. The term "highway" includes any road (whether a Federal highway, State highway, city street, rural road, or otherwise) in the United States which is not a private roadway.

(b) *Highway vehicle*—(1) *In general*. The term "highway vehicle" means any self-propelled vehicle, or any trailer or semi-trailer, designed to perform a function of transporting a load over highways, whether or not also designed to perform other functions, but does not include a vehicle described in paragraph (b)(2) of this section. For purposes of this definition, a vehicle consists of a chassis, or a chassis and a body if the vehicle has a body, but does not include the vehicle's load. Therefore, in determining whether a vehicle is a "highway vehicle", it is immaterial that the vehicle is designed to perform a highway transportation function for only a particular kind of load, such as passengers, furnishings and personal effects (as in a house, office, or utility trailer), a special type of cargo, goods, supplies, or materials, or, except to the extent otherwise provided in paragraph (b)(2)(i) of this section, machinery or equipment specially designed to perform some off-highway task unrelated to highway transportation. In the case of specially designed machinery or equipment, it is also immaterial, except as provided in paragraph (b)(2)(i) of this section, that such machinery or equipment is permanently mounted on the vehicle. For purposes of paragraph (b) of this section, the term "transport" includes the term "tow". A vehicle which is not a highway vehicle within the meaning of this paragraph shall be treated as a nonhighway vehicle for purposes of section 4041. Examples of vehicles that are designed to perform a function of transporting a load over the public highways are passenger automobiles, motorcycles, buses, and highway-type trucks, truck tractors, trailers, and semi-trailers.

(2) *Exceptions*—(i) *Certain specially designed mobile machinery for nontransportation functions*. A self-propelled vehicle, or trailer or semi-trailer, is not a highway vehicle if it (A) consists of a chassis to which there has been permanently mounted (by welding, bolting, riveting, or other means) machinery or equipment to perform a construction, manufacturing, processing, farming, mining, drilling, timbering, or other operation similar to any one of the forgoing enumerated operations if the operation of the machinery or equipment is unrelated to transportation on or off the public highways, (B) the chassis has been specially designed to serve only as a mobile carriage and mount (and a power source, where applicable) for the particular machinery or equipment involved, whether or not such machinery or equipment is in operation, and (C) by reason of such special design, such chassis could not, without substantial structural modification, be used as a component of a vehicle designed to perform a function of transporting any load other than that particular machinery or equipment or similar machinery or equipment requiring such a specially designed chassis.

(ii) *Certain vehicles specially designed for off-highway transportation*. A self-propelled vehicle, or a trailer or semi-trailer, is not a highway vehicle if it is (A) specially designed for the primary function of transporting a particular type of load other than over the public highway in connection with a construction, manufacturing, processing, farming, mining, drilling, timbering, or other operation similar to any one of the forgoing enumerated operations, and (B) if by reason of such special design, the use of such vehicle to transport such load over the public highways is substantially limited or substantially impaired. For purposes of applying the rule of clause (b) of this paragraph (b)(2)(ii), account may be taken of whether the vehicle may travel at regular highway speeds, requires a special permit for highway use, is overweight, overheight or overwidth for regular use, and any other relevant considerations. Solely for purposes of determinations under this paragraph (b)(2)(ii), where there is affixed to the vehicle equipment used for loading, unloading, storing, vending, handling, processing, preserving, or otherwise caring for a load transported by the vehicle over the public highways, the functions are related to the transportation of a load over the public highways even though the functions may be performed off the public highways.

(iii) *Certain trailers and semi-trailers specially designed to perform nontransportation functions off the public highways*. A trailer or semi-trailer is not a highway vehicle if it is specially designed to serve no purpose other than providing an enclosed stationary shelter for the carrying on of a function which is directly connected with and necessary to, and at the off-highway site of, a construction, manufacturing, processing, mining, drilling, farming, timbering, or other operation similar to any one of the forgoing enumerated operations, such as a trailer specially designed to serve as an office for such an operation.

(3) *Optional application*. For purposes of section 4041, if any rules existing immediately prior to January 13, 1977, would, if applicable, unequivocally resolve an issue involving the definition of a highway vehicle with respect to a period prior to such date, at the option of the taxpayer, such rules existing prior to such date shall be applied to resolve the issue for all periods prior to such date, and the rules of paragraph (b)(1) and (2) of this section, which define the term "highway vehicle", shall not apply with respect to such issue for all periods prior to such date.

(4) *Diesel-powered highway vehicle*. The term 'diesel-powered highway vehicle" means any highway vehicle (within the meaning of paragraph (b)(1) of this section) which is also a motor vehicle (as defined in paragraph (c) of this section) and which uses diesel fuel (as defined in paragraph (e) of this section) for propulsion purposes.

(c) *Motor vehicles*. The term "motor vehicle" includes all types of vehicles propelled by motor that are designed for carrying or towing loads from one place to another, regardless of the type of load or material carried or towed and whether or not the vehicle is registered or required to be registered for highway use. Included are fork lift trucks used to carry loads at railroad stations, industrial plants, warehouses, etc. The term does not include farm tractors, trench diggers, power shovels, bulldozers, road graders or rollers, and similar equipment which does not carry or tow a load; nor does it include any vehicle which moves exclusively on rails. For periods prior to January 6, 1977, a vehicle which is designed for towing, but not carrying, loads shall not be considered to be a motor vehicle.

(d) *Taxable liquid fuel.* The term "taxable liquid fuel" (or "taxable liquid") means any liquid which is either—

(1) Diesel fuel as defined in paragraph (e) of this section,

(2) Special motor fuel as defined in paragraph (f) of this section, or

(3) Any liquid fuel used in an aircraft in "noncommercial aviation", as defined in paragraph (h) of this section.

(e) *Diesel fuel.* The term "diesel fuel" means any liquid (other than a product taxable as gasoline under the provisions of section 4081) which is sold for use or used as a fuel in a diesel-powered highway vehicle.

(f) *Special motor fuel.* (1) The term "special motor fuel" includes any of the following sold for use or used as a fuel for the propulsion of a motor vehicle or motorboat:

(i) Liquefied petroleum gases (such as propane, butane, pentane, or methane, or mixtures of the same), or

(ii) Benzol, benzene, naptha, or any other liquid, whether a refined, partly refined, or unrefined product, 10 percent of which has been recovered when the thermometer reads 347° F. (175° C.) or 95 percent of which has been recovered when the thermometer reads 464° F. (240° C.) when subjected to distillation in accordance with the "Standard Method of Test for Distillation of Gasoline, Naptha, Kerosene, and Similar Petroleum Products" (A.S.T.M. designation: D86) of the American Society for Testing Materials, regardless of the trade name under which sold.

(2) The term "special motor fuel" does not include diesel fuel or any product taxable under the provisions of section 4081, nor does it include "kerosene, gas oil, or fuel oil", as defined in paragraph (g) of this section.

(g) *Kerosene, gas oil, or fuel oil.* (1) The term "kerosene, gas, oil or fuel oil" means any product (i) 10 percent of which has not been recovered when the thermometer reads 347° F. (175° C.), and (ii) 95 percent of which has not been recovered when the thermometer reads 464° F. (240° C.), when subjected to distillation in accordance with the "Standard Method of Test for Distillation of Gasoline, Naptha, Kerosene, and Similar Petroleum Products" (A.S.T.M. designation: D86) of the American Society for Testing Materials.

(2) Products designated as kerosene, gas, oil, or fuel oil which do not fall within the specifications of both paragraphs (g)(1)(i) and (ii) of this section are taxable as special motor fuel if sold or used as a fuel in a motor vehicle or motorboat.

(h) *Fuel used in the aircraft in noncommercial aviation.* The term "fuel used in an aircraft in noncommercial aviation" means any liquid (including any product taxable under section 4081) that is sold for use or used as a fuel in an aircraft in noncommercial aviation (as defined in paragraph (j) of this section).

(i) *Registered.* The term "registered", when used with reference to a highway vehicle, means—

(1) Registered for highway use under the laws of any State, District of Columbia, or foreign country, or

(2) Required to be registered for highway use under the law of the State, District of Columbia, or foreign country in which it is operated or situated. Any highway vehicle which is operated under a dealer's tag, license, or permit is considered to be registered. A highway vehicle is not considered to be "registered" solely because there has been issued a special permit for operation of the vehicle at particular times and under specified conditions. However, a highway vehicle which is required to be registered and which also has been issued a special permit for operation of the vehicle under specified conditions, such as carrying an oversized load, is still considered to be "registered".

(j) *Noncommercial aviation.* The term "noncommercial aviation." means any use of an aircraft, other than in a business of transporting persons or property for compensation or hire by air. The term also includes any use of an aircraft, in a business described in the preceding sentence, which is properly allocable to any transportation exempt from taxes imposed by sections 4261 (transportation of persons) and 4271 (transportation of property) by reason of section 4281 (use of small aircraft on nonestablished lines) or 4282 (transportation of members of affiliated group.)

§48.4041-9 Exemption for farm use.

(a) *In general.* The tax imposed by section 4041 does not apply to diesel fuel or special motor fuel, or fuel used in noncommercial aviation, sold for use or used on a farm in the United States for farming purposes. The tax applies in the case of diesel fuel delivered into the fuel supply tank of a highway vehicle, or special motor fuel delivered into the fuel supply tank of a motor vehicle or motorboat, even if it is known that the liquid fuel is to be used on a farm for farming purposes. Credit or refund of the tax paid in such case may be claimed as provided by section 6427(c) upon proof that the taxable liquid was used on a farm for farming purposes. A tax-free sale of fuel delivered into the fuel supply tank of an aircraft in noncommercial aviation where such fuel is to be used on the farm for farming purposes may be made only if the requirements of §48.4041-11 are met. The terms "used on a farm for farming purposes", and related terms, have the same meaning for purposes of the exemption in section 4041(f) and the regulations in this section as these terms are defined in paragraphs (1), (2), and (3) of section 6420(c) and the regulations contained in §48.6420-4.

(b) *Application of exemption.* The exemption referred to in paragraph (a) of this section does not apply with respect to diesel fuel or special motor fuel or fuel used in noncommercial aviation sold for use or used for nonfarming purposes, or diesel fuel or special motor fuel or fuel used in noncommercial aviation sold for use or used off a farm, regardless of the nature of the use. Thus, if a vehicle, motorboat, or aircraft is used both on a farm and off the farm, or if it is used on a farm both for farming and nonfarming purposes, the exemption applies only with respect to that portion of the diesel fuel or special motor fuel or fuel used in noncommercial aviation which is sold for use or used "on a farm for farming purposes". For purposes of this exemption, it is immaterial whether or not a vehicle is registered for highway use. However, the actual use of the vehicle and the place where it is used are material. For example if a truck used on a farm for farming purposes is also used on the highways (even though in connection with operating the farm), tax applies to that diesel fuel or special motor fuel which is sold for use or used in operating the truck on the highways, since the fuel was used off the farm.

(c) *Termination of exemption.* The exemption referred to in paragraph (a) of this section shall not apply on and after October 1, 1988.

§48.4041-10 Exemption for use as supplies for vessels or aircraft.

(a) *Application of exemption.* The tax imposed by section 4041 does not apply to any fuels which are sold for use or used as supplies for vessels or aircraft within the meaning of section 4221(a)(3) and (d)(3), and §48.4221-4. In the case of a liquid sold for use as fuel in an aircraft, a tax-free sale may be made only if the requirements of §48.4041-11 are met. For credit or refund of tax paid on fuels which have been sold or used as supplies for vessels or aircraft, see section 6416(b)(2)(B), section 6427, and paragraph (f) of this section.

(b) *Evidence required to establish exemption.* (1) In order to establish exemption from tax in the case of a sale of fuels for use as supplies for vessels or aircraft, it is necessary that the seller obtain from the owner, charterer, or authorized agent of the vessel or aircraft and retain in its possession a properly executed exemption certificate in the form prescribed by paragraph (c) of this section. If fuel is sold tax free for use as supplies for civil aircraft employed in foreign trade or in trade between the United States and any of its possessions, the exemption certificate must show the name of the country in which the aircraft is registered.

(2) If only occasional sales of fuels are made to a purchaser for use which is exempt from tax as provided in this section, a separate exemption certificate must be furnished for each order. However, if sales are regularly or frequently made to a purchaser for such exempt use, a certificate covering all orders for a specified period not to exceed 12 calendar quarters is acceptable. Such certificates and proper records of invoices, orders, etc., relative to tax-free sales must be kept for inspection by the district director as provided in section 6001. If a seller's records with respect to any sale claimed to be tax free do not include a proper certificate, with supporting invoices and such other evidence as may be necessary to establish the exempt character of the sale, tax is payable by the seller on the sale.

(c) *Acceptable form of exemption certificate.* The following form of exemption certificate, which must be adhered to in substance, is acceptable for the purpose of this section.

Exemption Certificate

(For use by purchasers of fuels for use as supplies for certain vessels or aircraft (section 4041(g) of the Internal Revenue Code of 1954).)

(Date), 19____ ____________________

The undersigned purchaser hereby certifies that he/she is the

____

(owner, character, or authorized agent of owner or charter)

of

____

(Name of company and vessel)

and that the fuel specified in the accompanying order, or a specified below or on the reverse side hereof, will be used only as fuel supplies for a vessel belonging to one of the following classes of vessels (including aircraft) to which section 4041(g) of the Internal Revenue Code applies: (Check class to which vessel belongs):

(1) Vessels (including aircraft) engaged in foreign trade.

(2) Vessels engaged in trade between the Atlantic and Pacific ports of the United States.

(3) Vessels (including aircraft) engaged in trade between the United Sates and any of its possessions.

(v) Vessels employed in the fisheries or whaling business.

(5) Vessels (including aircraft) of war of the United States or a foreign nation.

The undersigned understands that if the fuels are sold or used otherwise than as stated above and for a taxable purpose specified in section 4041 of the Internal Revenue Code, the undersigned will be liable for the tax upon such sale or use. It is also understood that this certificate may not be used in purchasing fuels, if such fuels are for use as fuel in pleasure vessels, or of any type of aircraft except (1) civil aircraft employed in foreign trade or trade between the United States and any of its possessions, and otherwise entitled to exemption, and (2) aircraft owned by the United States or any foreign country and constituting a part of the armed forces thereof.

The undersigned understands that the fraudulent use of this certificate to secure exemption will subject the undersigned and all others making fraudulent use to a penalty equivalent to the amount of tax due on the sale of the fuel and, upon conviction, to a fine of not more than $10,000, or to imprisonment for not more than 5 years, or both, together with the costs of prosecution. The purchaser also understands that it must be prepared to establish by satisfactory evidence the purpose for which the fuel purchased under this certificate was used.

(Signature) ____________________

(Address) ____________________

____

Registration Number if Fuel Used as supplies for civil aircraft engaged in foreign trade or in trade between the United States and any of its possessions.

(d) *Exemption certificate not obtained prior to filing of seller's excise tax return.* If the exemption certificate is not obtained prior to the time the seller files a return covering taxes due for the period during which the sale was made, the seller must include the tax on the sale in its return for that period. However, if the certificate is later obtained, a claim for refund of the tax paid on the sale may be filed on From 843, or a credit for the tax paid may be taken upon a subsequent return as provided by section 6416(b)(2)(B) and §48.6416(b)-2(c).

(e) *Liability of purchaser.* The person who purchases fuels tax free as provided in this section is liable for the tax imposed by section 4041 if the person sells or uses such fuel in a sale or use that is not exempt under any provision of law applicable to the taxes imposed by section 4041.

(f) *Credit or refunds.* (1) If diesel fuel or special motor fuel upon which the tax imposed by section 4041(a)(1) or (2) has been paid, is sold or used as supplies for vessels, a credit or refund of the tax is available under section 6416(b)(2)(B) to the retail dealer who paid the tax. As an alternative, a credit or refund of tax is available under section 6427 to the operator of the vessel who used the fuel. Where the retail dealer claims refund of the tax, the dealer, in accordance with section 6416(a), must reimburse the operator of the vessel for the amount of tax or obtain the written consent of the operator to the filing of such claim.

(2) If aviation fuel upon which the tax imposed by section 4041(c) has been paid is sold or used as supplies for aircraft, credit or refund of the tax is available only as a payment under section 6427 to the operator of the aircraft who uses the fuel or to the person who resells the fuel for such use.

§48.4041-11 Tax free sales of fuel for use in noncommercial aviation only if sellers and certain purchasers are registered.

(a) *In general.* Any sale of liquid fuel for delivery into a fuel supply tank of an aircraft is presumed to be subject to tax under section 4041(c), unless both the seller and purchaser of the liquid fuel are registered as provided in paragraph (b) of this section or are within one of the exceptions provided in paragraph (c) of this section.

(b) *Form of registration.* Except as provided in paragraph (c) of this section (relating to exceptions for State and local governments, for fuel purchased from customs bonded warehouses or continuous customs custody, and for fuel purchased for use in certain aircraft of the United States or of any foreign nation), tax-free sales under section 4041(c) may be made only if both the seller and the purchaser have registered as required by section 4041(i) and this paragraph (b). If fuel is purchased tax paid for use in noncommercial aviation but is used for a nontaxable purpose, see section 6427(a) for provisions relating to refunds or credits of tax for tax-paid fuels not used for the purpose for which sold. Any person desiring to be registered in order to sell or purchase fuel free of the tax imposed by section 4041(c) must, before making any tax-free sale or purchase, file Form 637A, in duplicate. Form 637A must be filed with the District Director of Internal Revenue for the district in which the principal place of business of the applicant is located (or if the applicant has no principal place of business in the United States, with the Director of International Operations, Internal Revenue Service, Washington, DC 20224). The person who receives a validated Certificate of Registry (Validated Form 637A) is considered to be registered for purposes of selling or purchasing fuel tax free as provided in this section.

(c) *Transactions excepted from registrations.* (1) A State or local government purchasing fuel delivered into a fuel supply tank of an aircraft it operates for its exclusive use may, but is not required to, register as provided in this section.

(2) Any purchaser of aircraft fuel who purchases fuel from any customs bonded warehouse or from continuous customs custody elsewhere than in a bonded warehouse is not required to register to purchase aircraft fuel from these sources tax free.

(3) Any purchaser of fuel for use in an aircraft which is owned by the United States or any foreign country and constitutes a part of the armed forces thereof is not required to register to purchase aircraft fuel tax free.

(4) The exceptions from registration in paragraphs (c)(1), (2), and (3) of this section do not relieve purchasers from the requirement of furnishing an exemption certificate as required by paragraph (d) of this section.

(d) *Evidence of tax-free sale.* (1) To establish the right of a purchaser to purchase fuel delivered into the fuel supply tank of an aircraft tax free, the seller must obtain from the purchaser and retain on its possession a certificate, properly executed and signed by or on behalf of the purchaser, containing the following information:

(i) Date of purchase,

(ii) The purchaser's registration number (or the exception from registration which is relied upon), and

(iii) A brief statement of the intended tax-free use of the fuel (for example, by an airline in the business of transporting persons or property for hire).

(2) The following form of certificate, which must be adhered to in substance, is acceptable for the purposes of this paragraph.

(Date) ______________________, 19 ____

The undersigned signifies that he/she, or the

____

(Name of purchaser if other than undersigned)

of which the undersigned is

____

(Title)

holds Certificate of Registry No. ____________

or has not registered because

____

(Brief statement of exception from registration relied upon)

delivered into a supply tank of the subject aircraft may be purchased free of tax because the fuel will be used

____

(Brief statement of tax free use)

The undersigned understands that if the fuel is used otherwise than as stated above and for a purpose taxable under section 4041 of the Internal Revenue Code, the undersigned will be liable for the tax upon such use, and that the undersigned must be prepared to establish by satisfactory evidence the purpose for which the fuel purchase under this certificate was used.

The undersigned also understands that the fraudulent use of this certificate to secure exemption will subject the undersigned and all others making fraudulent use to a penalty equivalent to the amount of tax due on the sale of the fuel and, upon conviction, to a fine of not more than $10,000, or to imprisonment for not more than 5 years, or both, together with the costs of prosecution.

____

(Signature)

____

(Address)

(3) Except as provided in paragraph (d)(4) of this section, a separate exemption certificate must be furnished for each sale of fuel delivered into a fuel supply tank of an an aircraft. If a portion of the fuel is intended to be used for a nontaxable purpose, the entire amount of the fuel may be sold tax free. Exemption certificates and proper supporting records such as invoices, orders, etc., relative to tax-free sales must be readily accessible for inspection by internal revenue officers and retained as provided in section 6001 of the Code and the regulations thereunder.

(4) If the purchaser of fuel to be used in an aircraft has reasonable grounds to believe that 90 percent or more of the total of the fuel to be purchased by it during a specified period not to exceed 12 calendar quarters will be used in a tax-free use, it may furnish each of its suppliers an exemption certificate covering all purchases for the specified period. The certificate shall be substantially in the same form as the certificate in paragraph (d)(2) of this section, except that in place of the date the purchaser shall specify the period covered by the certificate, and the purchaser shall give a brief explanation of its grounds for belief that 90 percent or more of its total fuel will be used in a tax-free use.

(5) The presumption under section 4041(i) that any liquid delivered into a fuel supply tank of an aircraft is taxable places the duty on the seller of the liquid fuel to use reasonable diligence to satisfy itself that a tax-free sale of fuel to the purchaser is allowed by law. In the absence of circumstances surrounding a sale that would raise a question as to whether tax-free sale is allowable, the requirement of reasonable diligence is satisfied if the seller receives and retains the required certificate evidencing the right of the purchaser to buy the fuel tax free. However, if the circumstances are such as to indicate the seller has failed to use reasonable diligence, it is not relieved of liability for the tax imposed by section 4041(c). In addition, if the seller fails to obtain and retain the evidence of taxfree sales as required by this paragraph (d), it is not relieved of liability for the tax imposed by section 4041(c).

§48.4041-12 Sales by United States, etc.

The taxes imposed by section 4041 apply to the sale at retail of taxable liquid fuels by the United States or by any agency or instrumentality of the Untied States, unless by statute specifically exempted from these taxes. However, the exemptions from these taxes provided by section 4041(f), (g), and (h) and the regulations thereunder contained in this subpart F are available to the extent therein provided.

§48.4041-13 Other credits or refunds.

(a) *In general*. For provisions relating to credit or refund of tax paid on taxable liquid fuel resold by the purchaser, or used otherwise than for the purpose for which purchased, see section 6427 and the regulations thereunder contained in Subpart O of this part.

(b) *Taxpaid liquid fuel used by local transit systems*. For provisions relating to credit or refund in the case of taxable liquid fuel used in vehicles while engaged in furnishing scheduled common carrier public passenger land transportation service along regular routes, see section 6427(b) and the regulations thereunder contained in Subpart O of this part.

(c) *Credit or refund of diesel fuel differential amount*. For provisions relating to an income tax credit or refund of the increased diesel fuel tax for original purchasers of diesel-powered automobiles and light trucks, see section 6427(g) and the regulations thereunder contained in Subpart O of this part.

§48.4041-14 Exemption for sale to or use by certain aircraft museums.

(a) *In general*. (1) The tax imposed by section 4041 does not apply to liquids which are sold for use or used by an aircraft museum in an aircraft or vehicle owned by such museum and used exclusively for the procurement, care, and exhibition of aircraft of the type used for combat or transport in World War II.

(2) In the case of liquid sold for use in an aircraft owned by an aircraft museum and to be used for the purposes described in paragraph (a)(1) of this section, a tax-free sale may be made only if the requirements of §48.4041-11 are met.

(b) *Cross reference*. For the definition of aircraft museum, see section 4041(h)(2).

PART 154—TEMPORARY REGULATIONS IN CONNECTION WITH THE AIRPORT AND AIRWAY REVENUE ACT OF 1970

Par. 5. The authority citation for Part 154 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 6. Section 154.1-1 is hereby removed.

Par. 7. The authority citation for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 8. Section 602.101(c) is amended by inserting in the appropriate places in the table:

"§48.4041-5(a)(2)	1545-0023"
"§48.4041-6(b)	1545-0023"
"§48.4041-7	1545-0023"
"48.4041-10	1545-0023"
"§48.4041-11	1545-0023"

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved September 17, 1985.

Ronald A. Pearlman,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on December 31, 1985, 8:45 a.m., and published in the issue of the Federal Register for January 2, 1986, 51 F.R. 11)

Section 4064.—Gas Guzzlers Tax

26 CFR 48.4064-1: Gas guzzler tax.

Gas guzzler tax liability. The gas guzzler tax imposed by section 4064 of the Code applies to automobiles imported without a prototype-based fuel economy rating assigned by the Environmental Protection Agency.

Rev. Rul. 86-20

ISSUE

If an automobile is imported without a prototype-based fuel economy rating assigned by the Environmental Protection Agency (EPA), is that automobile subject to the requirements of the tax imposed by section 4064(a) of the Internal Revenue Code (the "gas guzzler tax")?

FACTS

EPA issues certificates of conformity to domestic manufacturers and large importers of automobiles for those classes of automobiles complying with federal emission standards. This certificate is based on tests of a prototype vehicle and is the manufacturer's or importer's license to build or import automobiles as described in the manufacturer's or importer's application to EPA for certification. The EPA also conducts fuel economy testing in conjunction with the emission testing conducted on these vehicles. An urban fuel economy test and highway fuel economy test are conducted utilizing different driving schedules and different test procedures, and urban and highway fuel economy values are then determined. The combined fuel economy (also referred to as model type fuel economy), upon which the gas guzzler tax is based, is a weighted average of the urban and highway fuel economy values (with urban weighted 55 and highway weighted 45).

When an automobile is imported without a "certificate of conformity," a bond equal to the value of the vehicle, plus duty, is posted with the U.S. Customs Service. Most such "nonconforming vehicles" are imported by individuals or small volume importers. EPA requires any nonconforming vehicle to be either (1) converted, by installation of emission controls, to conform, in all material respects, to a vehicle that is already certified for sale in the United States, or (2) modified by the installation of emission control components and then individually tested to demonstrate emission compliance in accord with the Federal Test Procedure outlined in 40 C.F.R. Part 86 (1984). After the conversion or modification is completed and emission compliance has been demonstrated to EPA, a bond release letter is issued by EPA to the Customs Service. Inasmuch as a highway economy test is not required by EPA under either of these two procedures, no fuel economy ratings are derived from establishing the emission compliance of the individual automobiles.

There are also certain EPA enforcement and regulatory exemptions to the emissions compliance requirements for imported automobiles. Fuel economy ratings are not required by EPA for these automobiles.

LAW AND ANALYSIS

Section 4064(a) of the Code imposes

on the sale by the manufacturer of each automobile a tax determined on the basis of fuel economy ratings for vehicle model years beginning with 1980.

Section 48.4064-1(a)(3) of the Manufacturers and Retailers Excise Tax Regulations provides that the tax imposed by section 4064 of the Code is payable by the manufacturer making the sale. An automobile sold before the time a determination of fuel economy is made for the model type (as defined in section 48.4064-1(b)(6)) is subject to tax if it is subsequently determined that the fuel economy level of that model type is within the taxable range.

Section 48.4064-1(b)(1) of the regulations provides that a "sale" includes the use (within the meaning of section 4218) or the first lease (within the meaning of section 4217(e)) of an automobile by the manufacturer.

Section 4064(b)(1)(A) of the Code defines the term "automobile" as meaning any 4-wheeled vehicles propelled by fuel which is manufactured primarily for use on public streets, roads, and highways (except any vehicle operated exclusively on a rail or rails) and which is rated at 6,000 pounds gross vehicle weight or less.

Section 4064(b)(5) of the Code provides that the term "manufacturer" includes a producer or importer. Under section 48.4064-1(b)(2) of the regulations, an importer is a person who imports an automobile whether or not in connection with a trade or business.

Section 4064(c)(1) of the Code provides that fuel economy for any model type shall be measured in accordance with testing and calculation procedures established by the EPA Administrator by regulation. Procedures so established shall be the procedures utilized by the EPA Administrator for model year 1975 (weighted 55 percent urban cycle, and 45 percent highway cycle), or procedures which yield comparable results. Procedures under this subsection, to the extent practicable, shall require the fuel economy tests be conducted in conjunction with emissions tests conducted under section 206 of the Clean Air Act, (42 U.S.C. section 7521 (1982). The EPA Administrator shall report any measurements of fuel economy to the Secretary.

Section 48.4064-1(c) of the regulations provides that, for purposes of the gas guzzler tax, the fuel economy for any model type is determined (or redetermined) in accordance with the testing and calculation procedures utilized by the Environmental Protection Agent Administrator for model year 1975 (weighted 55 percent urban cycle and 45 percent highway cycle) or any other procedures (yielding comparable results) established by the Administrator. The Environmental Protection Agency's determination (or redetermination) of a model type's fuel economy is made at the time the general label fuel economy value is calculated (or recalculated). This determination (or redetermination) is conclusive for purposes of the gas guzzler tax.

Thus, the sale, use, or first lease by an importer of a new or used automobile (as defined in section 4064(b)(1) of the Code) that has not previously been subject to the tax imposed by section 4064(a) is subject to tax if the fuel economy rating of the model type in which the automobile falls is within one of the taxable categories in the tables in section 4064(a).

In those situations where an automobile is imported without a "certificate of conformity" and an accompanying EPA assigned fuel economy rating, the fact that EPA has not required a highway fuel economy test for purposes of emission compliance and bond release does not exempt the importer from liability for the gas guzzler tax. It would be impractical, however, for EPA to ascribe a fuel economy rating to all imported nonconforming automobiles of a particular model, based on EPA's testing of one such nonconforming vehicle.

The method of determining the amount of tax depends on the manner in which the vehicle establishes emissions compliance. If the automobile is modified to conform to a vehicle already certified for sale in the U.S., tax liability is based on the fuel economy rating of the certified vehicle it has been made to conform with. Alternatively, if the vehicle is brought into conformity with emission standards through modification and testing, tax liability is based on a presumption of low fuel economy. *See* Rev. Proc. 86-9, page 22, this bulletin, for procedures on the computation of liability. In either instance, the importer may elect to have the vehicle tested for the purposes of generating a fuel economy rating. The procedures to calculate fuel economy are set forth in 40 C.F.R. Part 86 (1984) and are available for use in situations where a fuel economy rating for a certified vehicle is not available for reference.

An automobile that is imported into the United States in a noncomforming mode and that is exempted from conformance to federal emissions standards is not exempted from the gas guzzler tax unless specifically exempted under the gas guzzler tax provisions. Inasmuch as an automobile without emission system modification cannot be compared, for fuel economy purposes, to a certified automobile that is in compliance with federal emission standards, the fuel economy rating of such an automobile has to be independently determined. *See* Rev. Proc. 86-9, page 22, this Bulletin.

HOLDING

An automobile imported without a fuel economy rating assigned by EPA is subject to the requirements of section 4064 of the Code and is subject to the gas guzzler tax if its fuel economy rating falls within one of the taxable categories under section 4064(a).

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26 CFR 48.4064-1: Gas guzzler tax.

Guidelines for importers of automobiles to compute gas guzzler tax liability for automobiles imported without a fuel economy rating assigned by the Environmental Protection Agency (EPA). See Rev. Proc. 86-9, page 22.

Section 6045.—Returns of Brokers

26 CFR 1.6045-1: Returns of information of brokers and barter exchanges.

Corporations; odd-lot purchases of own stock; broker reporting requirements. A corporation that purchases odd-lot shares from its stockholders on an irregular basis is not a broker for purposes of the reporting requirements of section 6045(a) of the Code.

Rev. Rul. 86-21

ISSUE

Is a corporation's one time purchase of its own stock on an "odd-lot" basis (fewer than 100 shares) subject to the broker reporting requirements of section 6045(a) of the Internal Revenue Code?

FACTS

X corporation made a one time offer to purchase the entire "odd-lot" stock holdings of its stockholders, that is, holdings of less than 100 shares of *X*'s common stock and holdings of 50 shares or less of its preferred stock. *X*'s offer applied to shares tendered during a two month period. The purpose was to reduce the number of stockholder accounts it had to maintain and, thereby, reduce *X*'s stockholder servicing expenses.

The tendered shares were purchased by *X* for a price equal to the mean average market price on the day *X* received the customer's acceptance of *X*'s offer, plus a bonus of less than one dollar per share. Stockholders who tendered their odd-lot shares were required to sell all of their shares including shares held of record and shares held in a broker's or nominee's name. The stockholders were not required to pay brokerage commissions, transfer taxes, or any other fees. All of the purchased shares were retained by *X* as treasury shares which *X*, at the time of the purchase, had no intention to reissue.

LAW AND ANALYSIS

Section 6045(a) of the Code provides that every person doing business as a broker shall, when required by the Secretary, make a return, in accordance with such regulations as the Secretary may prescribe, showing the name and address of each customer, with such details regarding gross proceeds and such other information as the Secretary may by forms or regulations require with respect to such business.

Section 6045(c)(1) of the Code defines the term "broker" to include a dealer, a barter exchange, and any other person who (for a consideration) regularly acts as a middleman with respect to property or services.

The term "broker" is further defined by section 1.6045-1(a)(1) of the Income Tax Regulations to mean a person that, in the ordinary course of a trade or business during the calendar year, stands ready to "effect" sales to be made by others. Section 1.6045-1(a)(10) provides that the term "effect" includes acting as a principal in a sale.

Section 1.6045-1(b), Example (2)(vi), of the Income Tax Regulations provides that a corporation that issues and retires long-term debt on an irregular basis is not a broker within the meaning of section 1.6045-1(a)(1) in the absence of additional facts that indicate the corporation is a broker.

The one time offer by *X* to purchase the odd-lot shares of stock was intended to reduce *X*'s stockholder servicing costs. Such a purchase was not in the corporation's ordinary course of business nor was it a transaction that occurs on a regular basis. A corporation that retires its long term debt on an irregular basis is not a broker. Similarly, a corporation purchasing odd-lot shares from its stockholders on an irregular basis is not a broker for purposes of section 6045(a) of the Code, where, as here, there are no additional facts that indicate otherwise. On the other hand, a corporation is a broker for purposes of section 6045(a) if it regularly stands ready to redeem its stock or to retire its debt.

HOLDING

X's one time odd-lot purchases of its own stock are not subject to the broker reporting requirements of section 6045(a) of the Code.

Section 6050K.—Returns Relating to Exchanges of Certain Partnership Interests

26 CFR 1.6050K-1T: Returns relating to exchanges of certain partnership interest. (Temporary)

T.D. 8064

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER A, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; SUBCHAPTER H, PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Information Returns Relating to Sales or Exchanges of Certain Partnership Interests

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document provides temporary regulations relating to information returns, statements, and notifications required where there is a sale or exchange of certain partnership interest. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations cross-referenced * * * [on page 26, this Bulletin]. The temporary regulations reflect changes to the applicable tax law made by section 149 of the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 197] and provide guidance on the manner of filing and contents of required information returns, statements, and notifications under section 6050K of the Internal Revenue Code of 1954.

DATES: The regulations contained in this document are effective with respect to sales or exchanges of partnership interests made after December 31, 1984.

FOR FURTHER INFORMATION CONTACT: Robert E. Shaw of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, (Attention: CC:LR:T LR-129-85). Telephone 202-566-3297 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

EXPLANATION OF PROVISIONS

Under section 6050K(a) and §1.6050K-1T a partnership must file a return on Form 8308 when there is a sale or exchange described in section 751(a) (a "section 751(a) exchange") of any interest in that partnership during any calendar year after 1984. A section 751(a) exchange occurs when any portion of any money or other property received by a transferor partner in exchange for all or a part of his or her interest in the partnership is attributable to section 751 property (unrealized receivables and substantially appreciated inventory items as defined in section 751(c) and (d)). Generally, a sale or exchange of an interest in a partnership (or a portion thereof) at a time when the partnership has any section 751 property will constitute a section 751(a) exchange.

A return on Form 8308 must be filed with respect to each sale or exchange. Section 1.6050K-1T(a)(2), however, provides that the Commissioner may, at a future date, authorize the use of a single document which includes all of the partnership's returns for a calendar year, or of a composite document, by partnerships that are required to file 25 or more separate returns in any calendar year. The information to be supplied on Form 8308 includes the names, addresses, and taxpayer identification numbers of the transferee and transferor in the exchange and of the partnership, the date of the exchange, and such other information as may be required by Form 8308 or its instructions. Form 8308 shall contain a printed notice that the information on the Form has been supplied to the Internal Revenue Service, that the transferor is required to treat a portion of the gain realized from the section 751(a) exchange as ordinary income, and that the transferor in a section 751(a) exchange is required under §1.751-1(a)(3) to attach a statement relating to the exchange to his or her income tax return for the taxable year in which the exchange occurred. The partnership return on Form 8308 is to be filed as an attachment to the partnership's Form 1065 for its taxable year in which the calendar year in which the section 751(a) exchange occurred ends.

Under section 6050K(b) and the temporary regulations all partnerships that are required to file returns under section 6050K(a) must furnish a statement to each person whose name appears on the partnership's Form 8308 showing the name and address of the partnership in addition to the information shown on the Form 8308 with respect to that person. A copy of Form 8308 is to be used as the statement. The statement must be furnished on or before January 31 following the calendar year in which the section 751(a) exchange occurred (or, if later, 30 days after the partnership has notice of the exchange). Thus, under the statute the partnership must generally prepare Form 8308 prior to the time it must be filed so as to allow the timely furnishing of statements to the transferor and transferee.

Section 6050K(c)(1) and the temporary regulations require the transferor of a partnership interest in a section 751(a) exchange to notify the partnership of the exchange, in writing, on or before the thirtieth day after the date of the exchange (or, if earlier, January 15 of the calendar year following the calendar year in which the exchange occurred). The written notification from the transferor must include the names and addresses of the transferor and transferee, the date of the exchange, and the taxpayer identification number of the transferor and, if known, of the transferee.

Under section 6050K(c)(2) and the temporary regulations the partnership is not required to file a return or furnish statements under section 6050K until the partnership has notice of the section 751(a) exchange. Section 1.6050K-1T(e) clarifies that a partnership has notice of a section 751(a) exchange when either (1) the partnership receives the written notification from the transferor required under section 6050K(c)(1), or (2) the partnership has knowledge that there has been a transfer of a partnership interest at a time when the partnership had any section 751 property. However, no return or statements are required under section 6050K if the transfer was not a section 751(a) exchange (*e.g.*, a transfer which in its entirety constitutes a gift for federal income tax purposes). A partnership may rely on a written statement from the transferor that the transfer was not a section 751(a) exchange in the absence of knowledge to the contrary. Under the temporary regulations the partnership is generally not required to value property. However, in certain circumstances a partnership may not be able to determine whether it had any section 751 property on the date of a transfer of a partnership interest without determining the value of such property. In such cases, partnerships that do not wish to make such a valuation may file Form 8308 in order to avoid the risk of incurring a penalty under section 6652(a).

REGULATORY FLEXIBILITY ACT; EXECUTIVE ORDER 12291; PAPERWORK REDUCTION ACT OF 1980

No general notice of proposed rulemaking is required by 5 U.S.C. 553(b) for temporary regulations. Accordingly, the Regulatory Flexibility Act does not apply and no Regulatory Flexibility Analysis is required for this rule. The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. The reporting requirements added by this document have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. The reporting requirements have been approved by OMB.

DRAFTING INFORMATION

The principal author of these temporary regulations is Robert E. Shaw of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 1 and Part 602 are amended as follows:

INCOME TAX REGULATIONS
(26 CFR Part 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.6050K-1T also issued under 26 U.S.C. 6050K.

Par. 2. A new §1.6050K-1T is added immediately after §1.6050J-1T to read as follows:

§1.6050K-1T Returns relating to sales or exchanges of certain partnership interests. (Temporary)

(a) *Partnership return required.* (1) Except as provided in paragraph (a)(2) of this section, a partnership shall make a separate return on Form 8308 with respect to each section 751(a) exchange of an interest in such partnership which occurs after December 31, 1984. The term "section 751(a) exchange" means any sale or exchange of a partnership interest (or portion thereof) in which any portion of any money or other property received by a transferor partner in exchange for all or a part of his or her interest in the partnership is attributable to section 751 property. The term does not include a distribution which is treated as a sale or exchange between the distributee and the partnership under section 751(b). For purposes of this section, the term "section 751 property" means unrealized receivables, as defined in section

751(c), and inventory items which have appreciated substantially in value ("substantially appreciated inventory items"), as defined in section 751(d). A partnership that is in doubt as to whether partnership property constitutes section 751 property to any extent or as to whether a transfer of a partnership interest constitutes a section 751(a) exchange may file Form 8308 in order to avoid the risk of incurring a penalty under section 6652(a). The penalty under section 6652(a) will generally apply, however, to partnerships that do not file Form 8308 where in fact a section 751(a) exchange occurred, except as provided in paragraph (e) of this section.

(2) The Commissioner may authorize the use, at the option of the partnership, of a single document which includes all of the partnership's returns for a calendar year in the case of partnerships required under paragraph (a)(1) of this section to make 25 or more returns on Form 8308 for any calendar year. In addition, the Commissioner may authorize the use for this purpose, also at the option of such a partnership, of a composite document. These authorizations shall be subject to such conditions, limitations, and special rules governing the preparation, execution, filing, and correction thereof as the Commissioner may deem appropriate. Such composite document shall consist of a form prescribed by the Commissioner and an attachment or attachments of magnetic tape or other approved media. To the extent that the use of a single or composite document has been authorized by the Commissioner, references in this section to Form 8308 shall be deemed to refer also to returns included in a single or composite document under this paragraph (a)(2). Any single or composite document so authorized shall include the information required to be provided on Form 8308 under paragraph (b) of this section with respect to each section 751(a) exchange.

(b) *Contents of return.* The return on Form 8308 shall include the following information:

(1) The names, addresses, and taxpayer identification numbers of the transferee and transferor in the exchange and of the partnership filing the return;

(2) The date of the exchange; and

(3) Such other information as may be required by Form 8308 or its instructions.

(c) *Statement to be furnished to transferor and transferee.* Every partnership making a return under paragraph (a) of this section must furnish to each person whose name is set forth in such return a written statement on or before January 31 of the calendar year following the calendar year in which the section 751(a) exchange occurred to which the return under paragraph (a) relates (or, if later, 30 days after the partnership is notified of the exchange as defined in paragraph (e) of this section). The partnership shall use a copy of the completed Form 8308 as a statement unless the Form 8308 contains information with respect to more than one section 751(a) exchange (see paragraph (a)(2) of this section). If the partnership does not use a copy of Form 8308 as a statement, the statement shall include the information required to be shown on Form 8308 with respect to the section 751(a) exchange to which the person to whom the statement is furnished is a party, as well as the printed notice on Form 8308 with respect to the facts that the information shown on the statement has been supplied to the Internal Revenue Service, that a transferor of a partnership interest in a sale or exchange described in section 751(a) of the Internal Revenue Code is required to treat a portion of any gain or loss resulting from the sale or exchange as ordinary income or loss, and that the transferor in a section 751(a) sale or exchange is required under paragraph (a)(3) of §1.751-1 to attach a statement relating to the sale or exchange to his or her income tax return for the taxable year in which the sale or exchange occurred.

(d) *Requirement that transferor notify partnership.* The transferor of any partnership interest in a section 751(a) exchange shall notify the partnership of such exchange in writing within 30 days of the exchange, (or, if earlier, January 15 of the calendar year following the calendar year in which the exchange occurred). The written notification from the transferor shall include the following information:

(1) The names and addresses of the transferor and transferee in the section 751(a) exchange;

(2) The taxpayer identification number of the transferor and, if known, of the transferee; and

(3) The date of the exchange.

Any transferor who notified a partnership under section 6050K(c)(1) prior to January 22, 1986 by a notification that does not meet the requirements of this paragraph (d) shall furnish such partnership with the written notification described in this paragraph (d) on or before February 21, 1986.

(e) *Partnership not required to make a return or furnish statements under this section until it has notice of the exchange.* A partnership shall not be required to make a return or furnish statements under this section with respect to any section 751(a) exchange until it has been notified of the exchange. For purposes of section 6050K(c)(2) and this section a partnership is notified of a section 751(a) exchange when either:

(1) The partnership receives the written notification from the transferor required by paragraph (d) of this section; or

(2) The partnership has knowledge that there has been a transfer of a partnership interest or any portion thereof, and, at the time of the transfer, the partnership had any section 751 property. However, no return or statements are required under section 6050K if the transfer was not a section 751(a) exchange (*e.g.*, a transfer which in its entirety constitutes a gift for federal income tax purposes). For purposes of this paragraph (e)(2), the partnership may rely on a written statement from the transferor that the transfer was not a section 751(a) exchange in the absence of knowledge to the contrary. For rules applicable where the partnership is in doubt as to whether partnership property constitutes section 751 property to any extent or as to whether a transfer of a partnership interest constitutes a section 751(a) exchange, see paragraph (a)(1) of this section.

(f) *Partnership return is to be attached to Form 1065.* Any partnership return on Form 8308 required under this section shall be filed as an attachment to the partnership's From 1065 for its taxable year in which the calendar year in which the section 751(a) exchange occurred ends and shall be filed at the time (determined with regard to any extension of time for filing) and place prescribed for filing of the partnership's Form 1065 for that taxable year (see paragraph (e) of §1.6031-1 for the time and place for filing Form 1065). However, if a partnership is notified of an exchange (as defined in paragraph (e) of this section) after the partnership has filed Form 1065 for the taxable year for which the exchange should have been reported, Form 8308 shall be filed by amending the partnership's Form 1065 for that taxable year and filing the amended Form 1065 with the Form 8308 attached on or before the thirtieth day after the partnership is notified of the exchange.

(g) *Penalties*. For penalties for failure of:

(1) Transferors to furnish the notification required by paragraph (d) of this section see section 6678(c);

(2) Partnerships to furnish any statement required under paragraph (c) of this section see section 6678(a); and

(3) Partnerships to file the return on Form 8308 as required by paragraph (a) of this section see section 6652(a)(1) and (3).

OMB CONTROL NUMBERS UNDER THE PAPER REDUCTION ACT

(26 CFR Part 602)

Par. 3. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. Section 602.101(c) is amended by inserting in the appropriate places in the table "1.6050K-1T . . . 1545-0941."

* * * * *

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue it with notice and public procedure under subsection (b) of section 553 of title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

Approved December 12, 1985.

Ronald A. Pearlman,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on December 20, 1985, 8:45 a.m., and published in the issue of the Federal Register for December 23, 1985, 50 F.R. 52313)

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.602: Forms and instructions.
(Also Part I, Section 3302; 31.3302(c)-1.)

Rev. Proc. 86-8

SECTION 1. PURPOSE

The purpose of this revenue procedure is to bring up to date the procedure to be followed in computing reductions in the credit against the tax reportable on Form 940, Employer's Annual Federal Unemployment Tax Return, for 1985.

SEC. 2. BACKGROUND

.01 Section 3301 of the Internal Revenue Code imposes an excise tax on employers based on wages paid with respect to employment. Section 3306(a) defines the term "employer," and section 3306(b) defines the term "wages," for purposes of the tax imposed by section 3301.

.02 Section 3302 of the Code provides for credits against the tax imposed by section 3301. Reductions in the amount of credit otherwise allowable are provided for in section 3302(c). If a state has not restored amounts that were advanced under Title XII of the Social Security Act, 42 U.S.C. sections 1321-1324 (1982), then section 3302(c)(2) provides that reductions in the credit otherwise available shall occur in the case of a taxpayer that is subject to the unemployment compensation law of that state and that pays wages attributable to that state.

.03 Section 3302(c)(2)(A) of the Code, in conjunction with section 3302(d), provides with respect to 1985 that, for each taxable year beginning with the second consecutive calendar year in which the advances have not been repaid, the reduction is equal to 0.3 percent of the wages paid.

.04 Section 3302(c)(2)(B) of the Code provides for an additional reduction for a taxable year beginning with the third or fourth consecutive year in which the advances have not been repaid, and section 3302(c)(2)(C) provides for an additional reduction for a taxable year beginning with the fifth or any succeeding consecutive year. Section 3302(d)(7) provides that the percentage of any additional reduction is determined by the Secretary of Labor.

.05 Section 3302(f) of the Code provides a cap on the credit reduction in the case of any state that meets certain solvency requirements, as determined by the Secretary of Labor on or before November 10. The credit reduction applicable to employers subject to the unemployment compensation law of such a state is limited to either 0.6 percent of wages paid or the percentage credit reduction that was in effect in the case of the state for the preceding taxable year, if greater than 0.6 percent. A state that partially meets the solvency requirements may partially limit the credit reduction. A state must apply to the Secretary of Labor in order for a cap to be put into effect.

.06 Section 3302(d)(3) of the Code provides that credit reductions for any year may be forestalled if a state restores to the United States Treasury, before November 10 of that year, the full amount of the advances.

.07 For purposes of the tax imposed by section 3301 of the Code, section 3306(j)(1) provides that the term "state" includes the District of Columbia, the Commonwealth of Puerto Rico, and the Virgin Islands.

SEC. 3. CREDIT REDUCTIONS FOR 1985

In a letter of November 12, 1985, 50 Fed. Reg. 49142 (1985), the Department of Labor advised the Secretary of the Treasury that none of the following states had repaid the advances before November 10, 1985. In addition, the Department of Labor has set forth the appropriate credit reduction for employers subject to the unemployment compensation law of each state, with respect to employment attributable to that state. As a result, credit reductions will take effect in the amount of the following percentages of the wages (as defined in section 3306(b) of the Code) paid by such an employer that are attributable to the following states:

(a) 0.6 percent—Louisiana, Puerto Rico, and Vermont;

(b) 0.7 percent—Connecticut;

(c) 0.8 percent—Ohio and West Virginia;

(d) 0.9 percent—Illinois and Pennsylvania;

(e) 1.1 percent—Minnesota;

(f) 1.2 percent—the Virgin Islands.

SEC. 4. PROCEDURE

If a credit reduction applies, it is computed on Part I, lines 6 and 7 of the Form 940 for 1985, and carried to line 2, Part II or line 4, Part III.

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26 CFR 601.402: Sales taxes collected by return.
(Also Section 4064; 48.4064-1.)

Rev. Proc. 86-9

SECTION 1. PURPOSE

The purpose of this revenue procedure is to set forth guidelines for importers of automobiles to compute gas guzzler tax liability under section 4064 of the Internal Revenue Code for automobiles that are imported without a fuel economy rating assigned by the Environmental Protection Agency (EPA).

SEC. 2. BACKGROUND

.01 Section 4064 of the Code imposes on the sale by the manufacturer (the definition of which includes an importer) of each automobile a tax in accordance with the tables set forth in section 4064(a). The liability for tax is based on the model year of the automobile and the fuel economy rating of the model type into which the automobile falls.

.02 Rev. Rul. 86-20, page 16, this Bulletin, concerns automobiles that are imported without a prototype-based fuel economy rating assigned by the EPA. The ruling holds that the sale, use, or first lease of such an automobile is subject to the gas guzzler tax imposed by section 4064(a) of the Code.

.03 Unless specifically excepted, automobiles imported into the United States must conform to federal emission standards. The large importers usually apply for a "certificate of conformity" to those emission standards by having prototype models tested for compliance. The certificate then becomes the importer's license to import vehicles into the United States. EPA also normally assigns fuel economy ratings to those prototype automobiles. The fuel economy rating is a combination of the urban economy rating, which is based on the emission test results, and the highway economy rating.

.04 Automobiles that are imported without a "certificate of conformity" must either be (1) converted, by installation of emission controls, to conform in all material respects to an automobile that is already certified for sale in the United States or (2) modified by installation of emission control components and individually tested to demonstrate emission compliance. *See* EPA regulations, Importation of Motor Vehicles and Motor Vehicle Engines, 40 C.F.R. section 85.1504 (1984). A fuel economy rating is not generally available for these vehicles because EPA does not require a highway fuel economy test on them and thus a separate highway fuel economy test would be required in order to devise a fuel economy rating.

SEC. 3. SCOPE AND OBJECTIVE

.01 Section 4064(c)(1) of the Code provides that, for purposes of the gas guzzler tax, fuel economy for any model type shall be measured in accordance with testing and calculation procedures established by the EPA Administrator by regulation. Procedures so established shall be the procedures utilized by the EPA Administrator for model year 1975 (weighted 55 percent urban cycle, and 45 percent highway cycle), or procedures which yield comparable results. Such procedures, to the extent practicable, shall require that fuel economy tests be conducted in conjunction with emissions tests conducted under section 206 of the Clear Air Act, 42 U.S.C. section 7521 (1982). The EPA Administrator shall report any measurements of fuel economy to the Secretary.

.02 Although those automobiles that are imported into the United States and are modified under the two methods described in section 2.04 are not assigned fuel economy ratings at the time of emission testing or modification, these vehicles are subject to the gas guzzler tax under Rev. Rul. 86-20, and liability is computed as follows:

SEC. 4. PROCEDURE

.01 Except as provided in section 4.04, in those instances where the importer modifies, or causes to be modified, an imported automobile under the first method set forth in section 2.04, the fuel economy rating for such automobile shall be equal to the EPA-prescribed rating for the original manufacturer's certified prototype to which such automobile has been modified to conform for emission purposes. The EPA-prescribed fuel economy ratings for model years, 1980 through 1986 are listed below.

MFR	*CARLINE*	*CID/CYL*	*FUEL SYSTEM*	*TRANS*	*FUEL ECONOMY RATING*
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	A3	12.1
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	M5	11.7
FERRARI	308	179/8	FI	M5	13.2
MASERATI	QUATTROPORTE	301/8	8	A3	8.8
MASERATI	MERAK	181/6	6	M5	12.1
ROLLS-ROYCE MOTORS	ROLLS-ROYCE/BENTLEY	412/8	2	A3	11.6
ROLLS-ROYCE MOTORS	ROLLS-ROYCE/BENTLEY	412/8	FI	A3	10.4
ROLLS-ROYCE MOTORS	CAMARGUE	412/8	2	A3	11.6
ROLLS-ROYCE MOTORS	CAMARGUE	412/8	FI	A3	10.9
1981					
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	A3	12.1
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	M5	11.7
CHECKER	MARATHON/TAXICAB	267/8	2	A3	16.5
CHECKER	MARATHON/TAXICAB-E	267/8	2	A3	16.5
FERRARI	308	179/8	FI	M5	13.1
FERRARI	MONDIAL	179/8	FI	M5	13.1
MASERATI	QUATTROPORTE	301/8	8	A3	10.0
ROLLS-ROYCE MOTORS	CAMARGUE	412/8	FI	A3	10.1
ROLLS-ROYCE MOTORS	CORNICHE	412/8	FI	A3	10.1
ROLLS-ROYCE MOTORS	SILVER SPIRIT/ SPUR/MULSANNE	412/8	FI	A3	11.0
EXALIBER AUTOS	PHAETON	305/8	4	A3	16.2
1982					
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	A3	12.1
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	M5	11.7
BITTER GMBH & CO. KG	SC	181/6	FI	A3	16.7
BITTER GMBH & CO. KG	SC	181/6	FI	M5	17.8
CHECKER	MARATHON/TAXICAB	267/8	2	A3	16.5
CHECKER	MARATHON/TAXICAB-E	267/8	2	A3	16.5
FERRARI	308	179/8	FI	M5	13.0

MFR	CARLINE	CID/CYL	FUEL SYSTEM	TRANS	FUEL ECONOMY RATING
FERRARI	MONDIAL	179/8	FI	M5	13.0
JAGUAR	XJ-S	326/12	FI	A3	16.8
MASERATI	QUATTROPORTE	301/8	8	A3	10.0
ROLLS-ROYCE MOTORS	CAMARGUE	412/8	FI	A3	10.1
ROLLS-ROYCE MOTORS	CORNICHE	412/8	FI	A3	10.1
ROLLS-ROYCE MOTORS	SILVER SPIRIT/SPUR/MULSANNE	412/8	FI	A3	11.0
EXCALIBUR AUTOS	PHAETON	305/8	4	A3	16.2
1983					
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	A3	11.8
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	M5	10.3
ASTON MARTIN	LAGONDA	326/8	8	A3	11.3
BITTER GMBH & CO. KG	SC	181/6	FI	M5	17.8
BITTER GMBH & CO. KG	SC	181/6	FI	A3	16.7
FERRARI	308	179/8	FI	M5	13.1
FERRARI	MONDIAL	179/8	FI	M5	13.1
JAGUAR	XJS	326/12	FI	A3	16.9
LOTUS	ESPRIT	132/4	4	M5	17.7
MASERATI	QUATTROPORTE	301/8	8	A3	10.0
ROLLS-ROYCE-MOTORS	CAMARGUE	412/8	FI	A3	11.0
ROLLS-ROYCE-MOTORS	CORNICHE	412/8	FI	A3	11.0
ROLLS-ROYCE-MOTORS	SILVER SPIRIT/SPUR/MULSANNE	412/8	FI	A3	11.0
ZIMMER MOTOR CARS CO.	GOLDEN SPIRIT	302/8	4	A3	14.8
LAMBORGHINI	COUNTACH LP500S	290/12	FI	M5	13.7
1984					
ASTON MARTIN LOGONDA	SALOON VANTAGE VOLANTE	326/8	8	A3	11.8
ASTON MARTIN LAGONDA	SALOON VANTAGE VOLANTE	326/8	8	M5	10.3
ASTON MARTIN LAGONDA	LAGONDA	326/8	8	A3	11.3
AURORA CARS LTD	AURORA MK II	302/8	4	M5	19.3
BITTER GMBL & CO. KG	SC	181/6	FI	M5	17.8
BITTER GMBL & CO. KG	SC	181/6	FI	A3	16.7
MERCEDES BENZ	500SEL	303/8	FI	A4	17.0
MERCEDES BENZ	500SEC	303/8	FI	A4	17.0
FERRARI	3O8	179/8	FI	M5	14.1
FERRARI	MONDIAL	179/8	FI	M5	14.1
JAGUAR	XJS	326/12	FI	A3	16.9
LOTUS	ESPRIT	132/4	4	M5	17.7
MASERATI	BITURBO	153/6	2	M5	18.7
MASERATI	QUATTROPORTE	301/8	8	A3	10.0
ROLLS-ROYCE MOTORS	CAMARGUE	412/8	FI	A3	11.0
ROLLS-ROYCE MOTORS	CORNICHE	412/8	FI	A3	11.0
ROLLS-ROYCE MOTORS	SILVER SPIRIT/SPUR MULSANNE	412/8	FI	A3	11.0
ROLLS-ROYCE MOTORS	SILVER SPUR LIMOUSINE	412/8	FI	A3	10.1
EXCALIBUR MOTORS	PHAETON	305/8	4	A4	17.9
LAMBORGHINI OF NORTH AMERICA	COUNTACH LP500S	290/12	FI	M5	13.7
1985					
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	L3	10.3
ASTON MARTIN	SALOON/VANTAGE/VOLANTE	326/8	8	M5	10.7
ASTON MARTIN	LAGONDA	326/8	8	L3	10.3
BMW	7-SERIES	209/6	FI	M5	20.3
MERCEDES-BENZ	380SE	234/8	FI	A4	20.0
MERCEDES-BENZ	380SL	234/8	FI	A4	20.0
MERCEDES-BENZ	500SEL	303/8	FI	A4	17.1
MERCEDES-BENZ	500SEC	303/8	FI	A4	17.1

MFR	*CARLINE*	*CID/CYL*	*FUEL SYSTEM*	*TRANS*	*FUEL ECONOMY RATING*
FERRARI	308	179/8	FI	M5	14.0
FERRARI	MODIAL	179/8	FI	M5	14.0
FERRARI	TESTAROSSA	302/12	FI	M5	13.4
JAGUAR CARS INC.	XJ	258/6	FI	A3	20.0
JAGUAR CARS INC.	JAGUAR XJ-S	326/12	FI	A3	16.9
LOTUS	ESPRIT TURBO	133/4	4	M5	17.7
MASERATI	QUATTROPORTE	301/8	8	L3	10.0
MASERATI	BITURBO (SUBCOMPAT)	152/6	2	M5	18.7
MASERATI	BITURBO (MINICOMPACT)	152/6	2	M5	18.4
MASERATI	BITURBO	152/6	2	A3	15.7
NISSAN MOTOR CO., LT	300ZX	181/6	FI	A4	20.2
1986					
BMW	5-SERIES	209/6	FI	L4	21.2
BMW	5-SERIES	209/6	FI	M5	21.2
BMW	6-SERIES	209/6	FI	L4	21.2
BMW	6-SERIES	209/6	FI	M5	21.2
BMW	7-SERIES	209/6	FI	L4	19.7
BMW	7-SERIES	209/6	FI	M5	20.0
MERCEDES BENZ	420SEL	256/8	FI	A4	19.1
MERCEDES BENZ	560SEL	338/8	FI	A4	17.3
MERCEDES BENZ	560SEC	338/8	FI	A4	17.3
MERCEDES BENZ	560SL	338/8	FI	A4	17.7
FERRARI	TESTAROSSA	302/12	FI	M5	13.5
FERRARI	328 GTS/GTB	194/8	FI	M5	17.2
FERRARI	3.2 MONDIAL/CABRIOLET	194/8	FI	M5	17.2
JAGUAR CARS INC.	JAGUAR XJ6	258/6	FI	A3	19.7
JAGUAR CARS INC.	JAGUAR XJ-S	326/12	FI	A3	16.7
MASERATI	BITURBO SPYDER	152/6	2	A3	16.8
MASERATI	BITURBO	152/6	2	A3	16.8
MASERATI	BITURBO 425	152/6	2	A3	16.8
PORSCHE	911	201/6	FI	M4	21.7
ROLLS-ROYCE	CAMARGUE	412/8	FI	A3	11.0
ROLLS-ROYCE	CORNICHE II/CONTINENTAL	412/8	FI	A3	11.0
ROLLS-ROYCE	SILVER SPIRIT/SPUR/MULSANNE	412/8	FI	A3	11.1
ROLLS-ROYCE	SILVER SPUR LIMOUSINE	412/8	FI	A3	10.2
LAMBORGHINI EA	COUNTACH	315/12	FI	M5	8.8

.02 If, as in the second method set forth in section 2.04, an automobile has been modified and individually tested for emission compliance, no certified automobile is available for comparison. Except as provided in section 4.04, the imported automobile is presumed to fall within the lowest fuel economy rating prescribed for the particular model year of the automobile in the tax rate tables contained in section 4064(a) of the Code. For purposes of complying with section 4.01 and this section 4.02, the importer shall retain documentation of modification and/or testing for a period of three years from the date the tax becomes due or the date the tax is paid, whichever is later.

.03 Certain imported automobiles are exempted from compliance with the federal emission standards by virtue of EPA enforcement and regulatory exemptions. Those vehicles may be driven in the United States without modification or testing. For purposes of the gas guzzler tax, such a vehicle is ascribed the lowest fuel economy rating in the tables in section 4064(a) of the Code for the particular model year of the automobile. An automobile that is imported under an EPA exemption and is later modified to conform to federal emission standards is ascribed a fuel economy rating gas if it had been imported and modified according to one of the methods described in section 2.04.

.04 In any instance where an importer believes that an ascribed fuel economy rating is inappropriate for a particular vehicle, the importer may, at the importer's own expense, have the vehicle individually tested. The testing must be in accordance with EPA procedures for a fuel economy rating and must be carried out at one of the EPA (Office of Air, Noise and Radiation) recognized laboratories that are capable of conducting motor vehicle emission tests. State emission checks or tests performed at service stations or repair shops are not acceptable. The taxpayer shall retain the fuel economy test documentation for a period of three years from the date the tax becomes due or the date the tax is paid, whichever is later.

SEC. 5. EFFECTIVE DATE

This revenue procedure is effective with respect to 1980 and later model year automobiles.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Information Returns Relating to Sales or Exchanges of Certain Partnership Interests

LR-236-84

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary income tax regulations relating to information returns, statements, and notifications required where there is a sale or exchange of certain partnership interests. The text of the temporary regulations serves as the comment document for this notice of proposed rulemaking.

DATES: Written comments and requests for a public hearing must be delivered or mailed by February 21, 1986. The regulations are proposed to be effective with respect to sales or exchanges of partnership interests made after December 31, 1984.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, 1111 Constitution Avenue, N.W., Attention: CC:LR:T (LR-236-84), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Robert E. Shaw of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, (Attention: CC:LR:T LR-236-84). Telephone 202-566-3297 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

The temporary regulations in the Rules and Regulations portion of this issue of the FEDERAL REGISTER amend the Income Tax Regulations (26 CFR Part 1) under section 6050K of the Internal Revenue Code of 1954.

For the text of the temporary regulations see T.D. 8064 published * * * [on page 18, this Bulletin]. The preamble to the temporary regulations explains the addition to the regulations.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that the proposed rule is not subject to review under Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required. Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request of any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer of Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies of those comments to the Service.

DRAFTING INFORMATION

The principal author of these proposed regulations is Robert E. Shaw of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations both on matters of substance and style.

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on December 20, 1985, 9:22 a.m., and published in the issue of the Federal Register for December 23, 1985 50 F.R. 52332)

Notice of Proposed Rulemaking

Information Reporting of Allowances, or Reimbursements, or Charges for Travel and Other Expenses of Public Employees and Certain Other Persons

LR-59-85

SUMMARY: This document contains proposed regulations governing information returns required to be filed by public sector employers and by payors with respect to persons in the service of an international organization regarding allowances or reimbursements provided for traveling or other bona fide ordinary and necessary expenses, including an allowance for meals and lodging or a per diem allowance in lieu of subsistence. This action is necessary to clarify existing regulations with respect to information reporting. These regulations affect employers, employees, certain third-party paying agents, and payors with respect to persons in the service of an international organization.

DATES: The regulations are proposed to be effective January 1, 1986, and would apply to information returns required to be filed for calendar years after 1986. Written comments must be delivered or mailed by March 10, 1986.

ADDRESS: Send comments to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-59-85), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Renay France of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) Telephone 202-566-3829 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 6041(a) of the Internal Revenue Code of 1954. The amendments would clarify the Internal Revenue Service's position with respect to amounts provided to employees and certain other persons as allowances or reimbursements for traveling or certain other business expenses. This clarification is necessary because some employers and payors appear to be either unaware of, or failing to comply with, the Service's position.

EXPLANATION OF PROVISIONS

The proposed amendments would delete present §1.6041-3(j) to make clear that all employers, including the United States, a State, Territory or a political subdivision thereof, and the District of Columbia, are required to report amounts provided to persons in the military or civil service as allowances, reimbursements, or charges for traveling and other business expenses, including an allowance for meals and lodging or a per diem allowance in lieu of subsistence, except to the extent that such persons are required to and do account to the employer for such expenses within the meaning of §1.162-17(b)(4).

Similarly, the amendments would delete §1.6041-3(n) to make clear that allowances, reimbursements, or charges for traveling and other business expenses, including an allowance for meals and lodging or a per diem allowance in lieu of subsistence, provided to persons in the service of an international organization, as defined in section 7701(a)(18), are subject to reporting except to the extent that such persons are required to and do account to the international organization for such expenses within the meaning of §1.162-17(b)(4).

These proposed amendments would make clear that payments of this character are subject to §1.6041-3(i), which provides that no information return is required with respect to advances, reimbursements, or charges for traveling and other business expenses of an employee to the extent that the employee is required to account (within the meaning of the term "account" as set forth in §1.162-17(b)(4)) and does so account to the employer for such expenses.

NON-APPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis, therefore, is not required.

REGULATORY FLEXIBILITY ANALYSIS

It is hereby certified that this rule will not have a significant impact on a substantial number of small entities because the number of significantly affected small entities is insubstantial.

COMMENTS AND REGULATIONS FOR A PUBLIC HEARING

Before adopting these proposed regulations consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

DRAFTING INFORMATION

The principal author of these proposed regulations is Renay France of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Proposed amendments to the regulations

The proposed amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.6041-3 also issued under 26 U.S.C. 6041(a).

Par. 2. Section 1.6041-3 is amended as follows:

1. Paragraph (j) is removed.

2. Paragraph (k) is redesignated as paragraph (j).

3. Paragraph (l) is redesignated as paragraph (k).

4. Paragraph (m) is redesignated as paragraph (l).

5. Paragraph (n) is removed.

6. Paragraph (o) is redesignated as paragraph (m).

7. Paragraph (p) is redesignated as paragraph (n)

8. Paragraph (q) is redesignated as paragraph (o).

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on January 8, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 9, 1986, 51 F.R. 985).

Corrections to Publication 1212

Announcement 86-17

Publication 1212, *List of Original Issue Discount Instruments* (Revised December 1985), contains incorrect information in Section I-B about the publicly traded long-term corporate debt instruments originally issued at a discount after December 31, 1984. The Internal Revenue Service was advised that, for those instruments listed in Section I-B, an inaccurate procedure had been utilized in calculating both the "daily portion" of original issue discount (OID) for the "accrual periods" covering calendar years 1985 and 1986, and the dollar amount of OID to be reported by brokers and middlemen on information returns for those calendar years. Copies of the revised Section I-B will be made available with Publication 1212 through Internal Revenue Service distribution centers. The corrected information is also provided in the list that follows:

Publication 1212
Section I—B
(Revised January 1986)

This section reflects publicly traded corporate debt instruments--mostly long-term--which were originally issued at a discount after December 31, 1984.

Name of Issuer	CUSIP No.	Issue Date	Maturity Date	Issue Price (Percent of Principal Amount)	Annual Stated Interest Rate	Daily Portion of OID (Dollar Amount per $1,000 of Maturity Value in each Accrual Period)					OID to be Reported per 1,000 of Maturity value For Calendar Year	
						1985 1st Period	1985 2nd Period	1985 3rd& 1986 1st	1986 2nd Period	1986 3rd Period	1985	1986
AMR Corporation	001765AA4	06/12/85	04/01/06	86.0625	10.2500		0.004383	0.004648	0.004929	0.005227	0.91	1.80
Amalgamated Sugar Company	022771AE9	05/30/85	09/15/90	96.7500	13.1250		0.010457	0.011187	0.011968	0.012803	2.33	4.40
American Capital Corporation	024898AB4	06/26/85	06/15/93	71.0000	8.4000		0.055549	0.059630	0.064011	0.068714	10.51	22.71
American Fructose Corporation	026296AA1	06/17/85	06/15/00	75.0000	9.4000		0.015430	0.016455	0.017548	0.018714	3.06	6.25
American Quasar Petroleum Co.	029145AE9	07/24/85	05/15/95	53.8400	4.5000		0.067402	0.071763	0.076406	0.081350	10.98	27.49
	029145AG4	07/24/85	08/15/90	89.6260	0.0000		0.048470	0.048950	0.049434	0.049924	7.83	18.09
	029145AH2	07/24/85	08/15/90	89.6260	4.5000		0.042826	0.044276	0.045775	0.047324	7.06	16.85
	029145AJ8	07/24/85	05/15/95	53.8429	4.5000		0.067401	0.071761	0.076404	0.081347	10.98	27.49
Ampal-American Israel Corp.	032015BF5	01/23/85	12/01/94**	97.0000	13.5000	0.004093	0.004380	0.004688	0.005019	0.005371	1.48**	1.80
	032015BG3	01/23/85	01/23/95	29.4000	0.0000		0.096436	0.102225	0.108361	0.114865	33.91	40.46
	032015BH1	01/23/85	12/01/99	90.0000	12.0000	0.006143	0.006560	0.007005	0.007481	0.007989	2.21	2.68
Atlas Van Lines, Inc.	049457AB0	07/08/85	01/01/94	81.7360	11.1250		0.031059	0.033389	0.035894	0.038586	5.91	13.59
	049457AC8	07/08/85	01/01/95	41.4830	6.0000		0.062773	0.069051	0.075957	0.083553	12.22	29.11
Centrust Savings Bank	156401AB3	05/16/85	05/15/95	83.5000	13.5000		0.018663	0.020248	0.021967	0.023833	4.35	7.88
Cogenic Energy Systems, Inc.	192391AB6	03/21/85	02/29/00	73.7500	10.2500		0.014494	0.015554	0.016690	0.017910	4.26	6.18
Colonial Savings & Loan Assn.	196028AD6	09/01/85	06/01/10	90.5625	11.1250		0.001729	0.001835	0.001948	0.002069	0.22	0.70
Conair Corp.	205889AA6	06/20/85	06/15/90	53.3650	0.0000		0.189544	0.201864	0.214984	0.228958	36.97	76.52
	205889AB4	06/20/85	06/15/91	46.3940	0.0000		0.167951	0.179077	0.190941	0.203590	32.76	67.93
	205889AC2	06/20/85	06/15/92	39.8180	0.0000		0.148226	0.158324	0.169110	0.180631	28.92	60.12
	205889AD0	06/20/85	06/15/93	34.2550	0.0000		0.129857	0.138866	0.148499	0.158802	25.34	52.77
	205889AE8	06/20/85	06/15/94	29.6420	0.0000		0.113381	0.121318	0.129810	0.138897	22.12	46.12
	205889AF5	06/20/85	06/15/95	25.8900	0.0000		0.099032	0.105964	0.113381	0.121318	19.32	40.28
Cronus Industries, Inc.	227174AA7	02/04/85	02/01/95	87.7780	12.3750		0.015659	0.016814	0.018055	0.019386	5.35	6.76
Electro Audio Dynamics, Inc.	285055AF6	02/01/85	02/01/91	80.0500	15.0000		0.043400	0.047897	0.052860	0.058337	15.14	19.97

** OID applies to purchases of $100,000 or more.

						Daily Portion of OID (Dollar Amount per $1,000 of Maturity Value in each Accrual Period)					OID to be Reported per 1,000 of Maturity value For Calendar Year	
Name of Issuer	CUSIP No.	Issue Date	Maturity Date	Issue Price (Percent of Principal Amount)	Annual Stated Interest Rate	1985 1st Period	1985 2nd Period	1985 3rd& 1986 1st	1986 2nd Period	1986 3rd Period	1985	1986
Facet Enterprises, Inc.	303032AB2	02/20/85	02/15/00	88.0440	12.7500		0.006478	0.006955	0.007468	0.008019	2.10	2.78
Federal Farm Credit Banks	313311NY4	02/15/85	02/15/95	79.2926	7.8750		0.029457	0.031120	0.032877	0.034733	9.63	12.18
Federal Home Loan Mortgage Corp.	313400KN2	04/03/85	04/03/95	75.7290	7.9500		0.032989	0.034984	0.037099	0.039342	9.15	13.54
Ford Motor Credit Co.	345397DA8	08/13/85	08/15/90	63.5236	1.0000		0.156151	0.164405	0.173094	0.182243	23.00	64.04
General Defense Corporation	369491AB1	04/15/85	04/15/95	89.8500	13.0000		0.011701	0.012575	0.013515	0.014526	3.11	4.92
Georgia-Pacific Corp.	373298AN8	06/20/85	06/15/86	92.0760	0.0000						0.00	79.24
	373298AP3	06/20/85	06/15/87	83.4820	0.0000		0.212097	0.221959	0.232278	0.243078	41.30	83.24
	373298AQ1	06/20/85	06/15/88	75.2560	0.0000		0.200462	0.210235	0.220484	0.231231	39.05	78.95
	373298AR9	06/20/85	06/15/89	67.3910	0.0000		0.186879	0.196363	0.206328	0.216798	36.41	73.82
	373298AS7	06/20/85	06/15/90	60.6060	0.0000		0.170548	0.179330	0.188565	0.198276	33.23	67.45
Greater Southwestern Funding Corp.	392360AB9	04/15/85	12/01/99	11.6350	0.0000	0.048509	0.052210	0.056194	0.060481	0.065096	13.52	21.56
	392360AC7	04/15/85	06/01/00	10.8020	0.0000	0.045052	0.048491	0.052191	0.056175	0.060462	12.56	20.03
	392360AD5	04/15/85	12/01/00	10.0320	0.0000	0.041848	0.045043	0.048481	0.052182	0.056166	11.66	18.60
	392360AE3	04/15/85	06/01/01	9.3250	0.0000	0.038891	0.041859	0.045054	0.048492	0.052193	10.84	17.29
	392360AF0	04/15/85	12/01/01	8.6650	0.0000	0.036136	0.038894	0.041862	0.045056	0.048495	10.07	16.06
	392360AG8	04/15/85	06/01/02	7.7370	0.0000	0.032794	0.035338	0.038079	0.041032	0.044215	9.15	14.62
	392360AH6	04/15/85	12/01/02	7.1800	0.0000	0.030433	0.032794	0.035337	0.038078	0.041032	8.50	13.57
	392360AJ2	04/15/85	06/01/03	6.6640	0.0000	0.028245	0.030436	0.032796	0.035340	0.038081	7.89	12.59
	392360AK9	04/15/85	12/01/03	6.1840	0.0000	0.026211	0.028244	0.030435	0.032795	0.035339	7.32	11.69
	392360AL7	04/15/85	06/01/04	5.7400	0.0000	0.024327	0.026214	0.028247	0.030438	0.032798	6.79	10.85
	392360AM5	04/15/85	12/01/04	5.0900	0.0000	0.021920	0.023647	0.025511	0.027521	0.029690	6.13	9.81
	392360AN3	04/15/85	06/01/05	4.7180	0.0000	0.020318	0.021919	0.023647	0.025510	0.027521	5.68	9.09
	392360AP8	04/15/85	12/01/05	4.3740	0.0000	0.018836	0.020320	0.021921	0.023649	0.025513	5.27	8.43
	392360AQ6	04/15/85	06/01/06	4.0540	0.0000	0.017458	0.018834	0.020319	0.021920	0.023647	4.88	7.81
	392360AR4	04/15/85	12/01/06	3.7580	0.0000	0.016184	0.017459	0.018835	0.020319	0.021920	4.53	7.24
	392360AS2	04/15/85	06/01/07	3.3100	0.0000	0.014479	0.015638	0.016890	0.018242	0.019703	4.05	6.50
	392360AT0	04/15/85	12/01/07	3.0650	0.0000	0.013407	0.014480	0.015640	0.016891	0.018244	3.75	6.02
	392360AU7	04/15/85	06/01/08	2.8380	0.0000	0.012414	0.013408	0.014481	0.015641	0.016893	3.48	5.58
	392360AV5	04/15/85	12/01/08	2.6770	0.0000	0.011647	0.012575	0.013576	0.014657	0.015824	3.26	5.22
	392360AW3	04/15/85	06/01/09	2.4330	0.0000	0.010642	0.011494	0.012414	0.013408	0.014481	2.98	4.78

Name of Issuer	CUSIP No.	Issue Date	Maturity Date	Issue Price (Percent of Principal Amount)	Annual Stated Interest Rate	Daily Portion of OID (Dollar Amount per $1,000 of Maturity Value in each Accrual Period) 1985 1st Period	1985 2nd Period	1985 3rd& 1986 1st	1986 2nd Period	1986 3rd Period	OID to be Reported per 1,000 of Maturity value For Calendar Year 1985	1986
Green Tree Acceptance, Inc.	393505AE2	06/10/85	05/15/95	72.8500	8.2500		0.038188	0.040717	0.043413	0.046288	7.91	15.61
Heileman (G.) Brewing Co.	422884AB2	08/01/85	04/03/03	25.0000	0.0000		0.054648	0.056834	0.059107	0.061471	8.51	21.57
Intel Overseas Corporation	458141AA6	05/20/85	05/15/95	32.0000	0.0000		0.108233	0.114932	0.122046	0.129600	24.66	43.93
Intermark, Inc.	458776AG6	04/01/85	10/01/98	89.0000	13.2000		0.007375	0.007933	0.008533	0.009179	2.08	3.12
LTV Corp.	502210AS6	09/23/85	04/01/98	59.5000	7.8750		0.031963	0.034392	0.037006	0.039818	3.39	13.53
	502210'T4	09/23/85	06/01/98	86.9000	8.7500		0.013953	0.014697	0.015479	0.016305	1.41	5.56
M.D.C. Corporation	552676AE	04/10/85	04/15/95	78.7000	10.5000	0.027382	0.029383	0.031530	0.033834	0.036306	7.95	12.30
MAI Holdings, Inc.	552915AA8	01/29/85	11/15/97	71.7500	varies						76.14	18.76
Merrill Lynch & Co. LYONS	590188AV0	08/15/85	02/21/06	20.0000	0.0000		0.044832	0.046672	0.048586	0.050579	6.49	17.90
Minstar, Inc.	604442AF0	10/15/85	10/15/95	75.5000	10.0000		0.031321	0.033632	0.036115	0.038781	2.63	13.13
Nu-Med, Inc.	670903AC7	03/14/85	03/15/05	90.2650	13.5000	0.002325	0.002500	0.002687	0.002890	0.003107	0.75	1.07
Oak Industries, Inc.	671400AF6	03/29/85	05/15/90	87.9943	13.5000	0.042499	0.046135	0.050081	0.054366	0.059017	12.79	19.48
Petro-Lewis Corp.	716451AR0	05/30/85	04/01/93	65.0000	13.7500		0.047124	0.052733	0.059010	0.066034	10.64	21.61
Plitt Theatres, Inc.	729173AA2	07/01/85	08/15/00	78.2330	11.0000		0.010833	0.011621	0.012468	0.013376	2.10	4.64
Polycast Technology Corp.	731691AB7	08/07/85	08/01/95	75.0000	9.8750		0.035047	0.037655	0.040455	0.043464	5.54	15.13
Price Communications Corp.	741437AA5	02/15/85	02/15/95	84.5500	11.7500		0.018089	0.019416	0.020841	0.022371	5.96	7.76
Staley Continental, Inc.	852567AC0	05/15/85	02/14/01	25.0000	0.0000		0.061459	0.064224	0.067113	0.070133	14.52	24.79
Sunshine Mining Company	867833AE5	04/18/85	04/15/04	90.0000	9.7500		0.004799	0.005063	0.005342	0.005637	1.26	1.95
Texas International Co.	882534AK6	09/13/85	11/01/91	92.8870	12.8750		0.018357	0.019695	0.021131	0.022673	2.09	7.64
	882534AL4	08/28/85	12/15/91	79.0424	14.1250		0.043339	0.047646	0.052381	0.057587	5.49	18.42
	882534AM2	09/06/85	02/01/93	92.3510	12.0000		0.018710	0.019995	0.021367	0.022835	2.34	7.98
	882534AN0	09/06/85	02/01/93	85.9060	12.0000		0.032546	0.035045	0.037735	0.040633	4.11	14.13
Tipperary Corp.	888002AC6	05/06/85	06/15/90	85.0000	0.0000	0.074463	0.075657	0.076870	0.078102	0.079354	18.05	28.32
	888002AD4	05/06/85	09/15/95	85.0000	12.0000		0.016314	0.017523	0.018822	0.020216	4.03	6.93
Town & Country Jewelry Mfg. Corporation	892054AB3	06/21/85	07/01/95	80.0000	10.2500		0.024344	0.026039	0.027852	0.029792	5.01	10.52
Transworld Corporation	894076306	01/18/85	06/01/07	85.5000	11.2500	0.003137	0.003346	0.003568	0.003806	0.004058	1.14	1.36
U.S. Home Corporation	912061AH1	04/15/85	04/15/00	87.5000	varies						12.89	20.37
Waste Management, Inc.	941063AA7	04/12/85	01/21/01	25.0000	0.0000		0.061360	0.064116	0.066996	0.070005	16.59	24.88
Wickes Companies, Inc.	967442AA2	01/26/85	01/31/87	97.0600	12.0000	0.035975	0.038443	0.041080	0.043899	0.046910	13.42	16.40
Willcox & Gibbs, Inc.	969207AB5	04/16/85	04/15/97	88.7500	13.0000		0.010722	0.011531	0.012401	0.013337	2.84	4.51

Foundations Status of Certain Organizations

Announcement 86-19

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. the following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

A Traveling Jewish Theatre, Los Angeles, CA
Abounding Grace Ministries, Inc., Staten Island, NY
Achievements Systems, Inc., Beaumont, TX
Agape Crisis Pregnancy Center, Fergus Falls, MN
Aging Services, Inc., Denver, CO
Al-Anon Alateen Information Service, Chicago, IL
Alcoholic Services of Texoma, Inc., Sherman, TX
Alliance for The Mentally Ill of Michigan, Birmingham, MI
Alpha Industries, Inc., Jamestown, ND
American Back Society, Oakland, CA
American Basketball Classic, Inc., Pasadena, CA
American Disability Evaluation Research Institute (ADERI), Ann Arbor, MI
American Eagles Gymnastics Booster Club, OH
American Institute of Childbirth Educators, Northridge, CA
Antelope Valley Discovery House Inc., Lancaster, CA
Arbuckle Childrens Village Inc., Ardmore, OK
Arizona Classic Guitar Society, Inc., Tempe, AZ
Artists Theatre Group Inc., Balboa Island, CA
Artreach Touring Theatre, Cincinnati, OH
Asian-American Services and Cultural Association, Columbus, OH
Associates In Juvenile Justice, Tucson, AZ
Association for Politics and The Life Services, DeKalb, IL
Association of the Philippine Practicing Physicians in America, Pico Rivera, CA
Asylum Hill Organizing Project Inc., Hartford, CT
BCACS Foundation, Inc., Battle Creek, MI
Barstow College Foundation, Barstow, CA
Batavia Village Resident Council, Batavia, OH
Batiquitos Lagoon Foundation, Carlsbad, CA
Bay Cities Center for Human Development, Los Angeles, CA
Bay Clinic Inc., The, Hilo, HI
Before and Tafter School, Orange, CA
Berrien-Cass-Van Buren Private Industry Council, St. Joseph, MI
Betty Smith Memorial Fund, Gladewater, TX
Big Brothers, Big Sisters of Marion County, Salem, IL
Blue Ridge Scholarship Fund Inc., Pinetop, AZ
Boating Ministries of America, Spring Valley, CA
Briandale Therapeutic Riding Center, Norco, CA
Bridge Foundation, The, Westerville, OH
Broadcast Designer's Assoc. Foundation, Hollywood, CA
Camelot Therapeutic Horsemanship Inc., Scottsdale, AZ
Cameron County Private Industry Council, Brownsville, TX
Casa La Merced, Los Angeles, CA
Catholic Collegiate Association, Youngstown, OH
Cedarburg/Grafton Rotary Fdn., Cedarburg, WI
Central Overland Commercial Development Corp., Overland, MO
Central Pomona Housing Corporation, Claremont, CA
Champions Kids Camp, Inc., Tulsa, OK
Chicago Area Friends of Interlocken, Chicago, IL
Christian Intergalactic Alliance, Federal Way, WA
Church Resource Ministries, Fullerton, CA
Circle Seven Training Council, Inc., Greenwood, IN
Citizens For The Developmentally Disabled, Conroe, TX
Clarion Singers Inc., The, San Diego, CA
Cleveland Police Patrolmen's Authority, Inc., Cleveland, OH
Coalition of Handicapped Citizens of Kentucky, Inc., Louisville, KY
Committee to Preserve Allegan Forest and Game Area, Allegan, MI
Community Action Human Resources Agency, Coolidge, AZ
Community Options, Inc., Westerville, OH
Community Programs Research Institute, Reseda, CA
Co-Pas Inc., Tucson, AZ
Cordova Senior High School Music Boosters Association, Inc., Rancho Cordova, CA
Covington Community Resources Corporation, Covington, KY
Cross Cultural Dance Resources Inc., Flagstaff, AZ
Dance And Company, Inc., Chicago, IL
Darlington Youth Sports Association, Inc., Darlington, WI
Denver Area Center For Employment Training Corporation, Denver, CO
Desert Coves Art Foundation, Palm Desert, CA
Designs For Success Inc., San Diego, CA
Drake Scholarship Fund, Drake, ND
Duncan Citizens Crime Commission Inc., Duncan, OK
Dystonia Foundation, San Bernardino, CA
E.F.F.O.R.T. Espanol Francais Fund Organization for Research and Travel, Cincinnati, OH
Eastmoor High School Athletic Boosters Association, Columbus, OH
Ecodemocracy Foundation, Inc., The, Putnam Valley, NY
Educatec-Multi Educational Services, Inc., Fort Wayne, IN
Educational Center for The Deaf, Inc., Los Angeles, CA
Elder-Tot Centers International Inc., Newport Beach, CA
Englewood Economic Development Corp., Chicago, IL
Ephpheta Counseling, Hypnosis & Alcohol Center of San Gabriel/Pomona Valleys, San Dimas, CA
Episcopal Chorale Society, The, Los Angeles, CA

Episcopal Trinity Housing Development Corp., Chicago, IL
Evergreen Gate Parents Association, San Jose, CA
Experimental Film Coalition, Evanston, IL
Fairbanks Youth Hockey Association, Inc., Fairbanks, AK
Fairview Park Jaycee Foundation, Fairview Park, OH
Faith Alive Ministries, Inc., Cherry Valley, MA
Faith Christian Camp, Inc., Cayuta, NY
Faith With Action Corp., Harrisonville, MO
Festival of Faith, Inc., Lexington, KY
Flip Flop School of Gymnastics, Inc., The, Austintown, OH
Flora Rogge Memorial Scholarship Committee, Inc., Brooklyn Center, MN
Foundation For Acupuncture Research, San Diego, CA
Frameries Fest, Willmar, MN
Fraser Youth Soccer Club, Fraser, MI
Friends of Imogen Cunningham, Inc., Berkeley, CA
Friends of The Santa Monica Playhouse, Santa Monica, CA
Fulton County Community Residential Project, Inc., Johnstown, NY
Glendale College Foundation Inc., Glendale, CA
Glendora Educational Foundation, Pasadena, CA
Golden Flower Foundation, Beverly Hills, CA
Goshen Elementary School Parent-Teacher Organization, Inc., Goshen, KY
Grayson County Crime Stoppers, Inc., Sherman, TX
Greater Mankato Wellness Committee, Mankato, MN
Greater Organization For Less Fortunate, Chicago, IL
Guild of Quilter of Contra Costa County, Pleasant Hill, CA
Halstead Community Preventive Medical Clinic, Loma Linda, CA
Harbor Dental Health Foundation, Long Beach, CA
Harbor Math/Science Magnet Community Support Group, San Pedro, CA
Hawaii Imin Centennial Corp., Honolulu, HI
Helping Other People Eat, Redlands, CA
Hispanic-American Science and Technology Association, Hacienda Heights, CA
Hispanic Financial Institute Inc., Montebello, CA
Hope Clinic, Duvall, WA
Hopkins County Council on Alcoholism, Sulphur Springs, TX
House of Bread, Dayton, OH
Housing And Rehabilitation, Inc., La Salle, CO
Indian Wells Charities, Farm Desert, CA
Inland Empire Mental Health Group, Redlands, CA
Inland Opera Company, Redlands, CA
Institute For Equine Research, Inc., San Luis Obispo, CA
Institute for Old Testament Related Studies, Shafter, CA
Institute For Primary Care Education and Research, San Diego, CA
Inter Share Time Ministries, Orange, CA
International Medical Exchange, The, Los Angeles, CA
Irving H E L P, Inc., Irving, TX
Isojiro Oka Parent Teachers Organization, Huntington Beach, CA
Jackson Civic Theater of Jackson Community Center, Jackson, MI
Joseph Principle Inc., Beaumont, CA
Judith Kirby Memorial Children's Foundation, Tucson, AZ
Jungle Exotics Study Program, San Bernardino, CA
Kansas Food Bank Warehouse, Inc., Wichita, KS
Kaw Valley Soccer Association, Lawrence, KS
Kenosha Christmas Charities, Inc., Kenosha, WI
Kentucky Association for Development Education, Lexington, KY
Kidney Foundation of Thief River Falls, Thief River Falls, MN
La Mesa Nutrition Board, La Mesa, CA
La Plaza Little League, Las Vegas, NM
L.A. Stage Co., The, Los Angeles, CA
Lafayette Jaycee Charitable Fund, Lafayette, IN
Leadership Skills Institute, Inc., New York, NY
L'Espirit Chamber Orchestra of Southern California Inc., Los Angeles, CA
Littig Housing Community Center, Inc., Port Washington, NY
Little River Soccer Club, Alexandria, VA
Living Epistle Outreach Ministry, The, Los Angeles, CA
Logan County Community Concert Association, Bellefontaine, OH
Long Beach Junior Chamber of Commerce Charitable Foundation, Long Beach, CA
Maine Arson Information Award Program, Inc., Westbrook, ME
Margaret Glazier Charitable Trust, Pheonix, AZ
Marquette Rotary Fund, The, Marquette, MI
Maryvale II, Inc., St. Mary-Of-The-Woods, MI
McDonald Youth Study Council, Beverly Hills, CA
Medina County Citizens' Council on Alcoholism, The, Medina, OH
Mental Health Association-West Inc., Upland, CA
Military Heritage Command, Inc., Denver, CO
Millwood School District Enrichment Foundation, Oklahoma City, OK
Missouri Valley Excellence Inc., Overland Park, KS
Monmouth-By-The-Atlantic, Red Bank, NJ
Monteverdi Chamber Orchestra Inc., San Diego, CA
Mother Theresa Hospice, Inc., Crown Point, MI
Multiple Ministries, Inc., Edmond, OK
National Emphysema Foundation, Norwalk, CT
National Hydrocephalus Association, Chester, NH
Montana Disabled Outdoor Group, Missoula, MT
National Donation Services, Glendale, CA
New Front Programming Services, Inc., Minneapolis, MN
New Mexico Special Olympics, Inc., Albuquerque, NM
New Richmond Boosters, Inc., New Richmond, OH
New Ulm Area Dinners For Shut-Ins Inc., New Ulm, MN
New World Chamber Orchestra, Inc., Carmel, IN
Newport Harbor Actors Theatre, Costa Mesa, CA
Nez Perce Tribal Foundation, Lapwai, ID
Nicaraguan Relief Society, San Gabriel, CA
Northeast Community Free Clinic, Los Angeles, CA

Northeastern Private Industry Council Inc., Oconto, WI
Ohio Black Women's Leadership Caucus, Akron, OH
Ohio Valley Regional Media Arts Coalition, Athens, OH
Oklahoma Heart Center, Inc., Oklahoma City, OK
Oklahoma Marriage Encounter/The Weekend Family, Bixby, OK
Oklahoma's Abducted Children, Inc., Oklahoma City, OK
Omega Outreach Ministries, San Gabriel, CA
Open Door Arts, Inc., The, Tulsa, OK
Orange County Masonic Memorial Foundation, Fullerton, CA
Overload, Jackson, MI
Palm Springs Newsletter, Palm Springs, CA
Paraiso de Los Ninos, Monterey Park, CA
Parents Association for Catholic Education, Bay City, MI
People Against Child Exploitation, Inc., Lexington, KY
Pima County Academic Decathlon Association, Tucson, AZ
Pleasant Valley Senior Center, Inc., Plain City, OH
Power Shop, Inc., Duncan, OK
Presbyterian College & Theological Seminary of the USA Synod, Los Angeles, CA
Problem Center of Long Beach, Long Beach, CA
Project Just Business Charitable Trust, Los Angeles, CA
Queen of the America's Guild Inc., Addison, IL
Raza Administrators & Counselors in Higher Education, Long Beach, CA
Reach Foundation Inc., Long Beach, CA
Redondo Beach Seahawk Booster Club—c/o Redondo Union High School, Redondo Beach, CA
Regional Research Institute of Southern California Inc., Los Angeles, CA
Riverfront Task Force, Great Falls, MT
Rockford Rehabilitation Network, Inc., Rockford, IL
Safe Birthing Information Network Inc., San Diego, CA
Saint Saviour Helping Hands, Cincinnati, OH
San Diegans Against Sudden Infant Death Syndrome, San Diego, CA
San Diego Figure Skating Club, San Diego, CA
San Francisco Regional Chapter The Society of Air Safety Investigators, Berkeley, CA
San Gabriel Valley Civic Light Opera Assoc., San Gabriel, CA
Sandusky County Council on Alcoholism, Fremont, OH
Santa Fe De Bogota Foundation, Inc., New Haven, CT
Santa Monica Amateur Boxing Club, Santa Monica, CA
Seascape Senior Housing, Oakland, CA
Self-Reliance Inc., Sunnyvale, CA
Senior Adults of Cedar Hill Texas, Cedar Hill, TX
Senior Center, Inc., Florissant, MO
Senior Citizens Enterprise, Inc., Louisville, KY
Senior Citizens United Organization, Inc., Gary, IN
Service and Assistance for Victims of Spouse Abuse, Waverly, OH
Share Experience, The, Chula Vista, CA
Sharing A Volunteer Tutoring Program, Inc., La Mesa, CA
Sheperd Communications, Inc., San Bernardino, CA
Sickle Cell Anemia Education & Information Center, National City, CA
Sidney Kays School of Theatre, Swarthmore, PA
Snelling-Hamline Community Council, St. Paul, MN
Socio Tec, Inc., Chicago, IL
South Dakota Association of Student Financial Aid Administrators, Yankton, S.D.
South East Productions Inc., San Diego, CA
Southside Operation Snowball, Chicago, IL
Spokane Bar Association for Legal Education, Spokane, WA
Spokane Womens Self-Help Center, The, Spokane, WA
Spring Valley Bible College & Seminary, Spring Valley, CA
Springfield Township Amateur Athletic Association, Inc., Lakemore, OH
Stanton Neighborhood Program, Stanton, CA
State Society of Mayflower Descendents in Hawaii, Honolulu, HI
Stebbins Housing Corporation, San Francisco, CA
Stop and Start Multi-Service Community Center, Inc., Cleveland, OH
Street People Foundation for Displaced Persons, Inc., Tulsa, OK
Sun Prairie Repertory Dance Company Inc., Sun Prairie, WI
Sunrise Environmental Corporation, Altedena, CA
Surgical Infection Society, Cincinnati, OH
Sweet Swingers Golf Club of Houston, Houston, TX
Symphony of The Verdugos, Glendale, CA
Target Spokane, Spokane, WA
Telecommunications and Telephone Association, Inc., Arlington, VA
Telesis II of California, San Diego, CA
Tell City Band Boosters, Inc., Tell City, IN
Themis Foundation, Inc., Norman, OK
Tiburon Peninsula Soccer League, Inc., Tiburon, CA
Ticker Taker, Inc., The, Denver, CO
Twelve Oaks Rehabilitation Services, Inc., Denton, TX
Twin City Youth Alliance, Inc., Minneapolis, MN
Two Dance and Design Company, Inc., Los Angeles, CA
United Care Center, St. Paul, MN
United States-China Medical Research Expedition, Princeton, NJ
United States Lighthouse Society, San Francisco, CA
United Way of Imperial County, El Centro, CA
University of Kentucky Mining Engineering Foundation, Inc., Lexington, KY
Utility Consumers Action Network Inc., San Diego, CA
Valley Tumor & Blood Institute, Inc., Bakersfield, CA
Villa Agave Corporation, Phoenix, AZ
Walnut Street Community Center Associates, Berkeley, CA
Washington Scoliosis Organization, Seattle, WA
West Maui Youth Center, Lahaina, HI
Western Institute for Health Studies Inc., Northridge, CA
White Heron Chorale Inc., Appleton, WI
Wilderness Communion, Altadena, CA
Will County Local Development Company, Joliet, IL
Wings of Grace Inc., Duncanville, TX
Winn Blake and Associates, Hollywood, CA
Women's Alcoholic Halfway House, Inc., Evansville, IN
Women's Center of Central Kentucky, Inc., Lexington, KY
Woodruff Manor, Long Beach, CA

World Equipoise Inc., San Diego, CA
Wranglers Soccer Club, Plano, TX
Youth's Hope, Northridge, CA

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Annual Return Required for Fringe Benefit Plans

Announcement 86-20

Section 6039D of the Internal Revenue Code, which was added by Public Law 98-611 and Public Law 98-612, requires group legal services plans described in section 120, cafeteria plans described in section 125, and educational assistance programs described in section 127 to file an annual return with the Internal Revenue Service for years beginning after December 31, 1984. The Service will issue regulations soon stating that these plans should file the required return on either Form 5500, Annual Return/Report of Employee Benefit Plan; Form 5500-C, Return/Report of Employee Benefit Plan; or Form 5500-R, Registration Statement of Employee Benefit Plan.

The forms and their related instructions have been revised so that fringe benefit plans required to file need only complete specified items.

For more information, see Forms 5500, 5500-C, and 5500-R and instructions, which are now available.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Philip G. Arneson	Sparta, WI	Attorney	Indefinite from December 15, 1985
Joseph P. Day	Woburn, MA	Attorney	Indefinite from December 24, 1985
Kenneth H. Dillard	Nashville, TN	Certified Public Accountant	Indefinite from December 31, 1985
LeRoy Hodge	Hamilton, NY	Attorney	Indefinite from December 10, 1985
Frank S. Lukuch	Barberton, OH	Certified Public Accountant	Indefinite from December 4, 1985
W. Stephen McConnell	Tampa, FL	Certified Public Accountant	Indefinite from December 26, 1985
Nathan Rich	Wilmington, DE	Certified Public Accountant	Indefinite from December 1, 1985
Walter E. Shettlemore	Long Beach, MS	Certified Public Accountant	Indefinite from December 20, 1985

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.61-2T, removed; new 1.61-2T, added; 1.132-1T, removed; new 1.1.32-1T, added; 1.132-2T through 1.132-8T, added; 1.162-25T, 1.274-5T, 1.274-6T, amended.	Taxation of fringe benefits and exclusions from gross income of certain fringe benefits	1986-3 I.R.B. 40	Feb. 21, 1986
26 CFR 1.451-3, amended.	Accounting for long-term contracts	1986-6 I.R.B. 55	Mar. 7, 1986
26 CFR 31.3508-1, 31.3509-1, 1.6041A-1, added.	Treatment of real estate agents and direct sellers; determination of employer liability for certain employment taxes	1986-6 I.R.B. 46	Mar. 10, 1986

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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1927-1	$8.00
1927-2	*18.00*
1928-1	8.00
1928-2	10.00
1929-1	13.00
1929-2	*3.50*
1930-1	8.50
1930-2	10.00
1931-1	*4.00*
1931-2	14.00
1932-1	*3.25*
1932-2	10.00
1933-1	*3.75*
1933-2	*4.00*
1934-1	(**)
1934-2	15.00
1935-1	8.00
1935-2	*15.00*
1936-1	*4.00*
1936-2	*15.00*
1937-1	*14.00*
1937-2	8.50
1938-1	*17.00*
1938-2	*14.00*
1939-1-1	9.50
1939-1-2	12.00
1939-2	10.00
1940-1	6.50
1940-2	15.00
1941-1	8.00
1941-2	*4.00*
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1946-2	6.00
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1947-2	3.75
1948-1	*3.50*
1948-2	8.50
1949-1	*8.00*
1949-2	*3.25*
1950-1	7.00
1950-2	*5.50*
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1951-2	*6.00*
1952-1	*3.00*
1952-2	8.00
1953-1	*4.75*
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1955-1	11.00
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1966-2	15.00
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1968-2	13.00
1969-1	15.00
1969-2	7.50
1969-3	14.00
1970-1	12.00
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1971-1	12.00
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1974-3 Supp.	11.00
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1976-2	11.00
1976-3-1	10.00
1976-3-2	18.00
1976-3-3	11.00
1977-1	12.00
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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-23, page 6.

Investment credit; recapture; distribution to parent corporation; subsequent transfer to partnership. Recapture of investment credit under section 47 of the Code does not occur where a wholly owned subsidiary corporation distributes section 38 property to its parent corporation in complete liquidation and the parent subsequently contributes the property to a partnership in which the parent holds a 75 percent interest.

Rev. Rul. 86-24, page 7.

Expenses of farmers; amounts paid for cows and embryo transplants. A purchaser of cows that are pregnant with transplanted embryos, who subsequently sells the cows and the calves separately, must allocate the original purchase price between the cows and the calves. The portion of the original purchase price that equals the fair market value of the cows is allocated to the cows; the remaining amount is allocated to the calves. Neither the costs attributable to the cows, nor the costs attributable to the embryos, are deductible currently as expenses. Gain or loss from the sale of the cows or calves is ordinary income or ordinary loss.

Rev. Rul. 86-25, page 18.

Recapitalization; exchange or old stock for three new classes. In a corporation's plan of recapitalization, the exchange by one group of shareholders of voting common stock for newly issued class A voting common stock and nonvoting preferred stock and, by another group of shareholders, the exchange of voting common stock for newly issued class A voting common stock and nonvoting class B common stock is a reorganization within the meaning of section 368(a)(1)(E) of the Code provided the transaction has a bona fide business purpose, is an isolated transaction, and is not part of a plan to increase periodically the proportionate interest of any shareholder in the assets or earnings and profits of the corporation.

Finding Lists begin on page 39.
Announcement Relating to Decisions of the Tax Court on page 5.
Announcement of Suspensions on page 37.
Announcement of Notice of Proposed Rulemaking on page 38.

Department of the Treasury
Internal Revenue Service

T 22.23:

Rev. Rul. 86-26, page 19.

LIFO; price indexes; department stores. The November 1985 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, November 30, 1985.

Rev. Rul. 86-27, page 20.

Dividends paid deduction; personal holding company income. A personal holding company subsidiary liquidated into its parent corporation may claim a deduction for dividends paid under section 561 of the Code to the extent of the amount distributed to the parent that represents the subsidiary's undistributed personal holding company income.

Rev. Rul. 86-30, page 24.

Limited partnerships. The states of Alabama, Minnesota, Nebraska, Oklahoma, West Virginia, and Wisconsin are added to the list of the states that have enacted legislation that corresponds to the Uniform Limited Partnership Act for purposes of section 301.7701-2 of the regulations. Rev. Rul. 84-80 amplified.

T.D. 8068, page 9.
LR-218-83, page 35.

Temporary and proposed amendments to the regulations relate to elections under section 338(h)(10) of the Code and to the extension of time for making certain other elections under section 338.

LR-106-77, page 33.

Proposed amendments to the regulations under section 936 of the Code relate to qualified possession source investment income for purposes of the Puerto Rico and possession tax credit.

EXCISE TAXES

Rev. Rul. 86-28, page 22.

Sale price of truck; tire exclusion; use of predetermined price. A vehicle retailer that does not have an established retail price of tires may use the tire manufacturer's predetermined price established by the manufacturer under Federal Trade Commission (FTC) regulations in determining the retail fair market value of the tire pursuant to section 4052(b)(1)(B)(iii) of the Code.

(Continued on page 4)

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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ADMINISTRATIVE

Rev. Rul. 86-29, page 23.

Returns; information failure to file; Form 1041, Schedule K-1. Schedule K-1 is considered an information return that is required to be timely filed with Form 1041, U.S. Fiduciary Income Tax Return. Trusts that fail to file Schedule K-1, file K-1s that omit material information, or file substitute K-1s not in an approved format, are subject to the penalty under section 6652(a)(1)(A) of the Code.

Rev. Proc. 86-10, page 25.

Assessments; penalties; appeal procedures. Procedures for appeal of assessments of certain additions to tax, additional amounts, and penalties are now found in section 601.106 of the Statement of Procedural Rules. Rev. Proc. 78-1 is obsolete.

Rev. Proc. 86-11, page 25.

Information retrieval and videotex; user charges and guidelines. User charges and guidelines are set forth for information retrieval and videotex tax library material produced by the Service.

Notice 86-2, page 25.

Regulations relating to the enrollment of individuals to practice before the Service have been amended.

Announcement 86-21, page 36.

Publication 583, Information for Business Taxpayers (Revised November 1985), contains an incorrect dollar amount and an incorrect line reference.

Announcement Relating to Decisions of the Tax Court

It is the policy of the Internal Revenue Service to announce in the Internal Revenue Bulletin at the earliest practicable date the determination of the Commissioner to acquiesce or not acquiesce in a decision of the Tax Court which disallows a deficiency in tax determined by the Commissioner to be due.

Notice that the Commissioner has acquiesced or nonacquiesced in a decision of the Tax Court relates only to the issue or issues decided adversely to the Government.

Actions of acquiescences in adverse decisions shall be relied on by Revenue officers and others concerned as conclusions of the Service only to the application of the law to the facts in the particular case. Caution should be exercised in extending the application of the decision to a similar case unless the facts and circumstances are substantially the same, and consideration should be given to the effect of new legislation, regulations, and rulings as well as subsequent court decisions and actions thereon.

Acquiescence in a decision means acceptance by the Service of the conclusion reached, and does not necessarily mean acceptance and approval of any or all of the reasons assigned by the Court for its conclusions.

No announcements are made in the Bulletin, with respect to memorandum opinions of the Tax Court.

The announcements published in the weekly Internal Revenue Bulletins are consolidated semiannually and annually. The semiannual consolidation appears in the first bulletin for July and in the Cumulative Bulletin for the first half of the year and the annual consolidation appears in the first Bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner ACQUIESCES in the following decision:

Taxpayer	Docket No.	*Report* Volume	Page
Gamble, Launce E. & Joan L.[1]	1617-76	68	972

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[1] Acquiescence in the issues relating to (1) whether petitioners must report as ordinary trade or business income, the gain on the sale of a thoroughbred colt which was 16½ months old, and (2) what portion, if any, of the purchase price of a mare in foal must be allocated to the foal. See Rev. Rul. 86-24, page 7, this Bulletin.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 38.—General Business Credit

26 CFR 1.38-1: Investment in certain depreciable property.

Whether recapture of investment credit under section 47 of the Code occurs where a wholly owned subsidiary corporation distributes section 38 property to its parent corporation in complete liquidation and the parent subsequently contributes the property to a partnership in which the parent holds a 75 percent interest. See Rev. Rul. 86-23, below.

Section 47.—Certain Dispositions, Etc., of Section 38 Property

26 CFR 1.47-3: Exceptions to the application of section 1.47-1.
(Also Sections 38, 332, 381, 721, 723; 1.38-1, 1.332-1, 1.381-1, 1.721-1, 1.723-1.)

Investment credit; recapture; distribution to parent corporation; subsequent transfer to partnership. Recapture of investment credit under section 47 of the Code does not occur where a wholly owned subsidiary corporation distributes section 38 property to its parent corporation in complete liquidation and the parent subsequently contributes the property to a partnership in which the parent holds a 75 percent interest.

Rev. Rul. 86-23

ISSUE

If a wholly owned subsidiary corporation had claimed investment tax credit with respect to certain property and if the property is later distributed to the parent corporation in a complete liquidation of the subsidiary and is then contributed by the parent to a partnership in which the parent corporation holds a 75 percent interest, does section 47(a) of the Internal Revenue Code require any recapture of the investment tax credit?

FACTS

X and its three subsidiaries were corporations engaged in active businesses. *X* determined that it would be advantageous to operate the businesses in partnership form in conjunction with corporation *Y* and *Z*. Accordingly, *X* liquidated the three subsidiaries in transactions that qualified under section 332(a) of the Code. Subsequently, in a transaction that qualified under section 721(a), *X* contributed all of the property it had received in the liquidations to a new partnership it had formed with *Y* and *Z*. In return for the contribution of property, *X* received a 75 percent interest in the partnership. In return for their cash contributions to the partnership, *Y* and *Z* received 15 percent and 10 percent partnership interests, respectively.

The property received by *X* in the liquidation of its subsidiaries and subsequently transferred to the partnership included section 38 property that had been previously placed in service by the subsidiaries. The liquidations and subsequent transfer occurred before the close of the useful life that was taken into account in computing the investment tax credit under section 38 of the Code.

The partnership continued to operate the businesses previously operated by *X*'s three subsidiaries. The section 38 property transferred to the partnership was retained as section 38 property in the same businesses.

LAW AND ANALYSIS

Section 38 of the Code provides for a general business credit that includes for a taxable year the investment tax credit determined under section 46(a). Sections 46(a) and (c) provide that the amount of the investment tax credit for any taxable year is equal to the sum of certain specified percentages of the qualified investment in section 38 property.

Section 47(a)(1) of the Code provides that if, during any taxable year, any property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, before the close of the useful life that was taken into account in computing the credit under section 38, then the tax under chapter 1 for the taxable year shall be increased by an amount equal to the aggregate decrease in the credits allowed under section 38 for all prior taxable years that would have resulted solely from substituting, in determining qualified investment, for the useful life the period beginning with the time the property was placed in service by the taxpayer and ending with the time the property ceased to be section 38 property.

Section 47(b) of the Code provides that property shall not be treated as ceasing to be section 38 property with respect to the taxpayer by reason of a mere change in the form of conducting the trade or business as section 38 property and the taxpayer retains a substantial interest in the trade or business.

Section 1.47-1(a) of the Income Tax Regulations reiterates the substance of section 47(a)(1) of the Code.

Section 1.47-3(e)(1) of the regulations provides that section 1.47-1(a) shall not apply to a disposition of section 38 property in a transaction to which section 381(a) of the Code (relating to carryovers in certain corporate acquisitions) applies. If the section 38 property described in the preceding sentence is disposed of, or otherwise ceases to be section 38 property with respect to the acquiring corporation, before the close of the estimated useful life that was taken into account in computing the transferor corporation's qualified investment, then section 1.47-1(a) shall apply to the acquiring corporation with respect to the section 38 property.

Sections 1.47-3(f)(1)(i) and (ii) of the regulations provide that provisions concerning investment tax credit recapture do not apply to section 38 property where the relevant disposition or cessation is by reason of a mere change in the form of conducting the trade or business in which section 38 property is used, provided that the following four conditions are satisfied:

(a) the section 38 property is retained as section 38 property in the same trade or business;

(b) the transferor of the section 38 property retains a substantial interest in the trade or business;

(c) substantially all of the assets (whether or not section 38 property) necessary to operate the trade or business are transferred to the transferee to whom the section 38 property is transferred; and

(d) the basis of the section 38 property in the hands of the transferee is determined in who or in part by reference to the basis of the section 38 property in the hands of the transferor.

Section 1.47-3(f)(2) of the regulations states that a substantial interest is retained in a trade or business only if, after the change in form, the retained interest in the trade or business is substantial in relation to the total interest of all persons or is equal to or greater than the transferor's interest prior to the change in form.

Section 332(a) of the Code provides that no gain or loss shall be recognized on the receipt by a corporation of property distributed in complete liquidation (as determined under section 332(b)) of another corporation.

Sections 381(a)(1) and 381(c)(26) of the Code provide that, in the case of the acquisition of assets of a corporation by another corporation in a distribution to such other corporation to which section 332 (relating to liquidations of subsidiaries) applies, the acquiring corporation shall take into account the items required to be taken into account for purposes of section 38 in respect of the transferor corporation.

Section 721(a) of the Code provides that no gain or loss shall be recognized to a partnership or to any of its partners in the case of a contribution of property to the partnership in exchange for an interest in the partnership.

Section 723 of the Code provides that the basis of property contributed to a partnership by a partner shall be the adjusted basis of such property to the contributing partner at the time of the contribution increased by the amount (if any) of gain recognized to the contributing partner at such time.

In the present situation, because the liquidation of *X*'s subsidiaries are complete liquidations that qualify for nonrecognition treatment under section 332(a) of the Code, section 381(a) is applicable to the liquidation transactions. Section 1.47-3(e)(1) of the regulations provides that the recapture provisions do not apply to a transaction to which section 381(a) is applicable. Therefore, the liquidation of *X*'s subsidiaries into *X* does not result in investment tax credit recapture.

The recapture issue, however, is presented a second time by *X*'s contribution of the businesses to the partnership. Section 1.47-3(e)(1) of the regulations provides that if section 38 property that was subject to a section 381(a) transaction is later disposed of, or otherwise ceases to be section 38 property with respect to the acquiring corporation, before the close of the estimated useful life which was taken into account in computing the transferor corporation's qualified investment, then the recapture provisions of section 1.47-1(a) apply to the acquiring corporation with respect to the section 38 property.

X is an acquiring corporation for purposes of section 1.47-3(e)(1) of the regulations, and *X* disposed of the section 38 property received from the liquidation transactions when it contributed the property to the partnership. The contributions, however, are not treated as dispositions for investment tax credit recapture purposes if the four conditions set forth in section 1.47-3(f)(1)(ii) are satisfied.

The first condition of section 1.47-3(f)(1)(ii) of the regulations is satisfied because, following the transfer by *X* of the subsidiaries' property to the partnership, the same businesses previously operated by the subsidiaries continued to be operated by the partnership. The third condition is satisfied because all of the assets necessary to operate those businesses were transferred to the partnership. The fourth condition is satisfied because of the application of sections 721(a) and 723 of the Code,; which provide that the basis of the section 38 property in the hands of the partnership is determined by reference to *X*'s basis in the property.

With respect to the second condition of section 1.47-3(f)(1)(ii) of the regulations, a transfer may result in a decrease in the transferor's interest without triggering disposition treatment provided that a substantial interest in relation to the total interest of all persons is retained by the transferor. *See* Rev. Rul. 77-361, 1977-2 C.B. 6, 7. In *Example (5)* of section 1.47-3(f)(6) a corporation transferred all of the assets it used to its manufacturing business to a partnership in exchange for a 50 percent interest in the partnership. The *example* concludes that the corporation retained a substantial interest in the business. In the present situation, because *X* has a 75 percent general partnership interest in the partnership following the contribution of property to the partnership, *X* has retained a substantial interest in the business for purposes of section 1.47-3(f)(1)(ii).

Accordingly, the transfer of the property by *X* to the partnership meets the four conditions of section 1.47-3(f)(1) of the regulations for treatment under section 47(b) of the Code as a mere change in the form of doing business. The transfer, therefore, does not result in investment credit recapture.

HOLDING

Under the circumstances described above, the complete liquidation by a parent corporation of its subsidiaries followed by the transfer of the subsidiaries' property to a partnership does not result in investment tax credit recapture under section 47(a) of the Code.

Section 61.—Gross Income Defined

26 CFR 1.61-4: Gross income of farmers.

What is the proper amount to include in income from the sale of breeding cows and calves. See Rev. Rul. 86-24, below.

Section 162.—Trade or Business Expenses

26 CFR 1.162-12: Expenses of farmers.
(Also Sections 61, 263, 1012, 1231; 1.61-4, 1.263(a)-1, 1.1012-1, 1.1231-2.)

Expenses of farmers; amounts paid for cows and embryo transplants. A purchaser of cows that are pregnant with transplanted embryos, who subsequently sells the cows and the calves separately, must allocate the original purchase price between the cows and the calves. The portion of the original purchase price that equals the fair market value of the cows is allocated to the cows; the remaining amount is allocated to the calves. Neither the costs attributable to the cows, nor the costs attributable to the embryos, are deductible currently as expenses. Gain or loss from the sale of the cows or calves is ordinary income or ordinary loss.

Rev. Rul. 86-24

ISSUE

What is the proper federal income tax treatment of the cost of (1) nonpurebred cows carrying embryos transplanted from purebred cows and of (2) purebred calves under the circumstances described below?

FACTS

After hormone treatments, purebred cows owned by *X* corporation are artificially inseminated with semen from a purebred bull. The embryos are surgically removed and implanted in the non-purebred cows. Following a positive pregnancy test, *X* offers the implanted cows for sale to the public. The cows are usually resold after giving birth to purebred calves. The purchase price of each cow pregnant with an embryo transplant is 25*x* dollars, which is equal to its fair market value. The fair market value of a cow similar to the implanted cow which was not pregnant is 8*x* dollars. The sales price of an implanted cow after it has given birth to a purebred calf is 8*x* dollars.

A, an individual that uses the cash receipts and disbursements method of accounting and files income tax returns on a calendar year basis, purchased from *X* 10 cows pregnant with transplanted purebred embryos for 250*x* dollars in July 1984. *A* allocated the entire purchase price to the cows and none of the purchase price to the purebred embryos.

In 1984, 10 purebred calves were born to the implanted cows and *A* then sold the cows for 80*x* dollars. Since *A* had allocated the entire purchase price to the cows, *A* intends to claim an ordinary loss of 170*x* dollars with respect to the sale of the cows on the 1984 federal income tax return. *A* intends to hold the purebred calves for sale.

LAW AND ANALYSIS

Section 162 of the Internal Revenue Code provides that there shall be allowed as a deduction all ordinary and necessary expenses paid or incurred during the tax year in carrying on any trade or business.

Section 1.162-12(a) of the Income Tax Regulations provides that the purchase of feed and other costs connected with raising livestock may be treated as expense deductions but that amounts expended in purchasing work, breeding, dairy, or sporting animals are regarded as investments of capital and shall be depreciated unless the animals are included in an inventory in accordance with section 1.61-4.

Section 263(a) of the Code provides generally that no deduction shall be allowed for capital expenditures.

In *Gamble v. Commissioner*, 68 T.C. 800 (1977), acq., page 5 this Bulletin, a taxpayer purchased for $60,000 a pregnant broodmare for use in the taxpayer's business of racing thoroughbred horses. When the taxpayer purchased the pregnant broodmare, the taxpayer received a broodmare and also an unborn foal. The court concluded that the portion of the $60,000 purchase price that was properly allocable to the unborn foal became the taxpayer's cost basis in the foal under section 1012 of the Code.

Section 1.61-4(a) of the regulation provides that, for farmers using the cash receipts and disbursements method of accounting, the profit from the sale of livestock or other items which were purchased is generally ascertained by deducting the cost from the sales price in the year in which the sale occurs. However, in the case of the sale of purchased animals held for draft, breeding or dairy purposes, the profits shall be the amount of any excess of the sales price over the amount representing the difference between the cost and the depreciation allowed or allowable.

Section 1221 of the Code defines the term "capital asset" as property held by the taxpayer (whether or not connected with the taxpayer's trade or business) but does not include, among other things, property used in a trade or business that is subject to an allowance for depreciation and property held by the taxpayer of a kind which would properly be included in the inventory of a taxpayer or property held by the taxpayer primarily for sale to customers in the ordinary course of the taxpayer's trade or business.

Section 1222(3) of the Code provides that the term "long-term capital gain" means gain from the sale or exchange of a capital asset held for more than 6 months if and to the extent such gain is taken into account in computing gross income.

Section 1231(a) of the Code provides that if, during the tax year, the recognized gains on sales or exchanges of property used in the trade or business, plus the recognized gains from the compulsory or involuntary conversion of property used in the trade or business and capital assets held for more than 6 months into other property or money, exceed the recognized losses from such sales, exchanges, and conversions, such gains and losses shall be considered as gains and losses from sales or exchanges of capital assets held for more than 6 months. If such gains do not exceed such losses, such gains and losses shall not be considered as gains and losses from sales or exchanges of capital assets.

Section 1231(b)(3)(A) of the Code provides that the term "property used in the trade or business" includes cattle, regardless of age, held by the taxpayer for draft, breeding, dairy, or sporting purposes , and held by the taxpayer for 24 months or more from the date of acquisition.

In the present situation, *A* purchased cows carrying transplanted purebred embryos. The 25*x* dollar purchase price must be allocated to the cow and the embryo on the basis of the fair market value of each. The fair market value of the cow is 8*x* dollars and the fair market value of the cow plus embryo is 25*x* dollars. Accordingly, the portion of each 25*x* purchase price that is equal to the fair market value of the cows, 8*x* dollars, is properly treated as the purchase price of the cow. *A*'s income from the sale of the cows will be determined in accordance with section 1.61-4(a) of the regulations. In this case, because the cows were used in a trade or business and were subject to depreciation, they are not capital assets under section 1221. Since the cows were purchased by *A* for breeding purposes and sold within 24 months, the cows do not qualify as property used in the taxpayer's trade or business within the meaning of section 1231(b)(3)(A) of the Code. Thus, any gain or loss on the sale of the cows will be ordinary income or ordinary loss. Since only 80*x* dollars of the purchase price is properly allocable to the cows and *A* sold the cows for 80*x* dollars, *A* has no gain or loss on the sale of the cows.

A also purchased purebred embryos that will become purebred calves. The balance of the 25*x* dollars that is not allocable to the cost of the cow is properly allocable to the cost of the embryo. The amount allocable to the embryo is an amount expended in purchasing livestock and must be capitalized under section 1.162-12(a) of the regulations. In this case, the calves were primarily held for sale to customers in the ordinary course of business. Thus, the calves are not capital assets under section 1221 of the Code. Thus, any gain or loss on the sale of the calves will be ordinary income or ordinary loss.

HOLDING

The portion of the 250*x* dollars paid

to *X* for the pregnant non-purebred cows, the fair market value of the cows of 80*x* dollars, is treated as the purchase price of the cows. *A* will not recognize any gain or loss on the sale of cows because *A*'s 80*x* dollar basis in the cows equal the 80*x* dollars received on the sale.

The balance of the 250*x* dollar purchase price, 170*x* dollars, is attributable to the cost of purchasing the purebred calves. Since the calves are not capital assets under section 1221 of the Code and are not property used in the taxpayer's trade or business within the meaning of section 1231(b), any gain or loss on the sale of the calves will be ordinary income or ordinary loss.

Section 263.—Capital Expenditures

26 CFR 1.263(a)-1: Capital expenditures.

Whether the cost of a cow and an embryo transplant may be deducted as an expense. See Rev. Rul. 86-24, page 7.

Section 305.—Distributions of Stock and Stock Rights

26 CFR 1.305-4: Distributions of common and preferred stock.

Whether a certain transaction is a distribution of property to which section 301 of the Code applies by reason of the application of section 305(b)(3). See Rev. Rul. 86-25, page 18.

Section 332.—Complete Liquidation of Subsidiaries

26 CFR 1.332-1: Corporate liquidations.

Whether recapture of investment credit under section 47 of the Code occurs where a wholly owned subsidiary corporation distributes section 38 property to its parent corporation in complete liquidation and the parent subsequently contributes the property to a partnership in which the parent holds a 75 percent interest. See Rev. Rul. 86-23, page 6.

Section 338.—Certain Stock Purchases Treated as Asset Acquisitions

26 CFR 1.338(h)(10)-1T: Elective recognition by selling consolidated group of deemed sale gain or loss on target's assets (temporary).
(Also Section 1502; 1.1502-75T.)

T.D. 8068

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, SUBCHAPTER H, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Temporary Regulations Under Section 338(h)(10) of the Internal Revenue Code of 1954 and Extension of Time to Make Certain Elections

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to section 338(h)(10) of the Internal Revenue Code of 1954 ("Code") as added by the Technical Corrections Act of 1982 ("TCA") [Pub. L. 97-498, 1983-1 C.B. 451, 470]. This document also contains amendments to temporary regulations so as to extend the time for making certain elections under section 338 to March 15, 1986. The temporary regulations provide guidance to taxpayers concerning the application of section 338. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations cross-referenced * * * [on page 35, this Bulletin].

DATES: These regulations are effective upon publication in the FEDERAL REGISTER. These temporary regulations under section 338(h)(10) generally apply to stock acquisitions made after January 12, 1983. The temporary regulations being amended generally apply to stock acquisitions made after August 31, 1982.

FOR FURTHER INFORMATION CONTACT: Patricia Wendlandt or Bennett C. Steinhauer of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T (202-566-3458, not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document adds new temporary regulations §1.338(h)(10)-1T to Part 1 of Title 26 of the Code of Federal Regulations. The temporary regulations implement section 338(h)(10) of the Code by adding new §§1.338(h)(10)-1T and 1.1502-75T and by amending §1.338-1T(e). Section 338(h)(10) was originally added as section 338(h)(9) by section 306(a)(8)(B)(i) of TCA (Pub. L. No. 97-448; 96 Stat. 2402) [1983-1 C.B. 451, 470] and was redesignated as section 338(h)(10) by section 712(k)(6) of the Tax Reform Act of 1984 (Pub. L. 98-369; 98 Stat. 951) [1984-3 C.B. (Vol. 1) 1, 458].

This document also amends §§1.338-1T and 1.338-4T to extend from August 23, 1985, to March 15, 1986, the date for electing section 338, for making certain other elections under section 338, and for certain other purposes. Finally, this document amends the table of OMB control numbers in Part 602 of Title 26 of the CFR to reflect the OMB control number assigned to §1.338(h)(10)-1T. The temporary regulations added and amended by this document will remain in effect until superseded by later temporary or final regulations relating to these matters.

EXPLANATION OF PROVISIONS

INTRODUCTION

Section 338, generally, provides that, if the stock of a corporation ("target") is acquired by another corporation ("purchasing corporation") in a qualified stock purchase, the purchase corporation may elect (or may be deemed to elect under certain consistency rules) to have the target treated as if it had sold all of its assets (as "old target") and then purchased those assets (as "new target"). The deemed sale of assets by old target generally is governed by the nonrecognition rule of section 337. Section 338(h)(9) now provides that old target is not treated as a member of an affiliated group with respect to the deemed sale of its assets, except as otherwise provided in section 338(h)(10). Thus, even if consolidated returns are filed by the selling group and by the purchasing group, the general rule is that any gain that target must recognize notwithstanding section 337 is reported by target on its final return which is a separate return referred to as a "deemed sale return." See §1.338-1T(f)(3)(i). Section 338(h)(10) provides that, under regulations, if the target is a member of a selling consolidated group ("selling group") and section 338(h)(10) is elected, old target is treated as having sold all of its assets to new target in a single transaction. Gain or loss is recognized by old target on the deemed sale of its assets but, except as provided by regulations, no gain or loss is recognized upon the sale or exchange of old target stock to the purchasing corporation. Old target, then, is treated as having sold all of its assets in a single taxable transaction while a member of the selling consolidated group. For an exception, see the discussion of tandem transactions below. Thus, if section 338(h)(10) is elected, the selling consolidated group directly bears any income tax on the deemed sale of target's assets instead of target initially bearing that tax on a separate return.

CHARACTERIZATION OF TRANSACTION

Under the document, the section 338(h)(10) transaction is characterized as if old target sells all of its assets at the close of the acquisition date and then immediately liquidates under section 332. Thus, this document rejects the alternative of treating old target in the transaction as simply terminating.

ELIGIBILITY FOR ELECTION

Under §1.338(h)(10)-1T, section 338(h)(10) may be elected for any target that is a member of a selling group whose acquisition date occurs after January 12, 1983, the date section 338(h)(10) was enacted.

The selling group is an affiliated group that filed or is required to file a consolidated return for the taxable period that includes the acquisition date, provided that the group's common parent is not a target. Notwithstanding §1.1502-75(a)(1) and (c), §1.1502-75T (as added by this document) provides that the selling group may not withdraw its consolidated return or elect to discontinue filing consolidated returns on or after the day that a section 338(h)(10) election is made for a former member of the group.

TIME AND MANNER OF ELECTION

The procedural rules for making a section 338(h)(10) election and related reporting requirements are designed to ensure that the purchasing corporation (through the target) receives the intended results of a section 338 election while any income tax arising on target's deemed sale of its assets is shifted to the selling consolidated group. Thus, the section 338(h)(10) election is an irrevocable election made jointly by the selling group and the purchaser on Form 8023 (the statement of section 338 election). A copy of this form must be filed with the return of the selling group for the taxable period that includes the acquisition date. The schedule listing each corporation subject to the section 338 election required by §1.338-1T(e)(1) shall indicate which of the listed corporations is subject to the section 338(h)(10) election under the stock consistency rules explained below in this document. As part of the election procedure, the selling group must indicate the date and Service Center where the group filed its consolidated return for the taxable period that includes the acquisition date or for the last taxable period for which one was filed.

Interim election procedures provide the method of making an election until Form 8023 is modified to include a section 338(h)(10) election.

A section 338(h)(10) election may be made on or before the later of March 15, 1986, or the 15th day of the 9th month beginning after the month in which the acquisition date occurs. This last day is the same date as the last day for making a section 338 election since both elections must be made simultaneously. Exceptions to the simultaneous election requirement are provided for transitional section 338(h)(10) elections and pre-section 338(h)(10) target elections. In the case of a pre-section 338(h)(10) target election, all parties shall treat the transaction as if the election is not made until a delayed section 338(h)(10) statement of election is filed.

CONSEQUENCES OF ELECTION

The following consequences obtain when an election is made for a section 338(h)(10) target:

1. Old target recognizes gain or loss as if, while a member of the selling group, it sold in a single taxable transaction all of its assets at the close of the acquisition date. For an exception, see the discussion of tandem transactions below.

2. Gain or loss from the sale or deemed sale of the stock of a section 338(h)(10) target or target affiliate to the purchaser by the selling group is ignored for all purposes of chapter 1 of the Code.

3. Old target is deemed to have liquidated under section 332 at the close of the acquisition date but after the deemed asset sale. Thus, attributes listed in section 381, such as net operating loss carryovers, carry over from target to the transferee in the deemed liquidation.

4. No gain or loss is recognized by the selling group or by shareholders other than the purchasing corporation with respect to target stock that is not acquired by the purchasing corporation in the transaction. The basis of such stock in the hands of minority shareholders (other than the selling group) remains unchanged. The basis of such stock retained by the selling group is adjusted to reflect its proportionate share of the net fair market value of new target's assets and no gain or loss is recognized as a result of this basis adjustment.

5. If the purchasing corporation owns shares of nonrecently purchased stock, it is deemed to have made a gain recognition election with respect to such shares.

6. The adjusted grossed-up basis (the "AGUB") of the target stock is the same as if only an express election were made except that it does not include income tax liabilities resulting from the deemed sale. The AGUB is allocated to assets in accordance with section 338(b)(5).

7. The foregoing deemed sale and liquidation rule applies for purposes of the consolidated returns regulations.

DEEMED SALE PRICE

The price at which the assets of each old target is deemed to be sold is their fair market value. An elective formula (the "MADSP") for deemed sale price is provided that takes into account liabilities and other relevant items.

STOCK CONSISTENCY REQUIREMENTS

The temporary regulations require that, if a section 338(h)(10) election is made for one target, it is deemed to be made for all target affiliates that are members of the same selling group and whose stock is purchased by members of the same purchasing group.

TANDEM TRANSACTIONS

The temporary regulations provide rules coordinating section 338(h)(10) with sections 337 and 338(h)(12). These rules may apply when the sale of old target stock is part of the liquidation of the entire selling consolidated group.

MISCELLANEOUS MATTERS

The information return and recordkeeping requirements of section 6043 and §1.332-6 are inapplicable to the constructive section 332 liquidation of target.

Further, a deemed sale return for target that is subsequently mooted by a section 338(h)(10) election is considered to be a return so that interest will be paid on the overpayment of tax.

AMENDMENTS TO §§1.338-1T and 1.338-4T

Section 1.338-1T(e) is amended to integrate the requirements for making a section 338(h)(10) election with requirements for a section 338 election. Sections 1.338-1T and 1.338-4T are amended to extend certain due dates from August 23, 1985, to March 15, 1986.

COMMENTS REQUESTED

Comments are requested on the rules for determining the deemed sale price under §1.338(h)(10)-1T(f). Consideration is being given to determining such amount under a mandatory formula (the "mandatory MADSP formula") and eliminating the option to determine the deemed sale price by reference to the fair market value of each asset of old T. Such comments should address, among other things, the concern that the mandatory formula not impose any undue administrative burdens on taxpayers.

REGULATORY FLEXIBILITY ACT; EXECUTIVE ORDER 12291; AND PAPERWORK REDUCTION ACT OF 1980

A general notice of proposed rulemaking is not required by 5 U.S.C. 553 for temporary regulations. Accordingly, these temporary regulations do not constitute regulations subject to the Regulatory Flexibility act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required. The collection of information contained in these regulations has been submitted to the Office of Management and Budget in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB (control No. 1545-0702).

DRAFTING INSTRUCTION

The principal author of these temporary regulations is Bennett C. Steinhauer of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Parts 1 and 602 are amended as follows:

PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Paragraph 1. The authority citation for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805; * * * §§1.338(h)(10)-1T, 1.338-1T, and 1.338-4T also issued under 26 U.S.C. 338; * * * §1.1502-75T also issued under 26 U.S.C. 1502.

Par. 2. There is inserted in the appropriate place a new §1.338(h)(10)-1T. The new section reads as follows:

§1.338(h)(10)-1T Election recognition by selling consolidated group of deemed sale gain or loss on target's assets (temporary).

(a) *Scope*. This section sets forth the requirements, conditions, and consequences of a section 338(h)(10) election if a target corporation is acquired in a qualified stock purchase from a selling consolidated group. Subject to the detailed rules in paragraphs (c) and (j) of this section, the primary effects of a section 338(h)(10) election are a deemed taxable sale by target of all its assets followed by a deemed complete liquidation to which section 332 applies. In addition, gain or loss on the actual sale of target stock by a member of the selling group to a member of the purchasing group included in the qualified stock purchase is ignored.

(b) *Definitions and nomenclature*. For purposes of this section (and except as otherwise provided in this section)—

(1) *In general*. The definitions set forth in §§1.338-1T(b) and 1.338-4T(b)(2) also apply to this section. The nomenclature in §1.338-4T(b)(1) does not apply to this section.

(2) *Section 338(h)(10) target*. A corporation is a 'section 338(h)(10) target" if it is an original target that is included in the selling group's consolidated return for the taxable period that includes the acquisition date.

(3) *Selling consolidated group*. The "selling consolidated group" is the affiliated group (as defined in section 1504) which for the taxable period that includes the acquisition date—

(i) Includes the section 338(h)(10) target,

(ii) Filed a consolidated return or is required to file a consolidated return, and

(iii) Has as its common parent a corporation for which a section 338 election by the purchasing corporation does not apply.

(4) *Section 338(h)(10) target affiliate*. A "section 338(h)(10) target affiliate" is any member of the selling consolidated group that is an affected target.

(5) *Nomenclature*. (i) The S group is a selling consolidated group.

(ii) T is a section 338(h)(10) target.

(iii) T1, T2, etc. are section 338(h)(10) target affiliates.

(iv) S1, S2, etc. are members of the S group other than T, T1, T2, etc.

(v) P, P1, P2, etc. are members of the purchasing group. When the context requires, a reference to P refers to the purchasing corporation or corporations. See section 338(h)(8).

(vi) K is a shareholder of T other than a member of the S group of a member of the purchasing group.

(6) *Examples*. The provisions of this paragraph (b) may be illustrated by the following examples.:

Example (1). T is a wholly-owned subsidiary of S2. T1 is a wholly-owned subsidiary of S2. T2 is a wholly-owned subsidiary of T1. S1, S2, T, T1, and T2 are all members of an affiliated group that files a consolidated return for calendar year 1986 with S1 as its common parent. On June 1, 1986, P1 purchases all of the outstanding stock of T and an express election and a section 338(h)(10) election are made for T. On July 1, 1986, P2 purchases all the outstanding stock of T1. Both T1 and T2 are section 338(h)(10) target affiliates.

Example (2). Assume the same facts as in *Example (1).* Assume further that P1 purchases all of the stock of S1 on July 10, 1986. Since the express election for T causes a deemed election for S1 (an affected target), a section 338(h)(10) election may not be made for S1, T, T1, or T2 because there is no selling consolidated group.

(c) *Eligibility for section 338(h)(10) election.* A section 338(h)(10) election may be made for T if—

(1) P makes a qualified stock purchase of T stock,

(2) The acquisition date with respect to the stock of T or of any section 338(h)(10) target affiliate is after January 12, 1983, and

(3) An express election is made for T.

(d) *Time and manner of making section 338(h)(10) election*—(1) *Simultaneous joint election requirement.* Except as provided for a delayed election in paragraph (d)(7) of this section, the section 338(h)(10) election is made jointly by P and the S group on Form 8023 in accordance with the instructions to the Form.

(2) *Election irrevocable.* Once made, a section 338(h)(10) election is irrevocable.

(3) *Annotation on required schedule.* Section 1.338-1T(e)(1)(i)(D) requires that the schedule required by §1.338-1T(e)(1) must indicate which of the listed corporations is subject to a section 338(h)(10) election, including corporations subject to deemed section 338(h)(10) elections under paragraph (h) of this section. This indication is made by clearly identifying such corporations, such as by a footnote system.

(4) *Attachments to target returns and additional filings.* Under §1.338-1T(e)(2)(i), a copy of the statement of section 338 election that is filed with the return of the S group for the taxable period which includes the acquisition date is considered filed with the last return of old target.

(5) *Consequence of failure to comply with requirements of §1.338-1T(e)(1) and (2).* For consequences of failure to comply with the requirements of §1.338-1T(e)(1) and (2), see §1.338-1T(e)(3). Thus, an election and failure to comply with these requirements will not invalidate a section 338(h)(10) election and will have no effect on the applicability of paragraph (h) of this section.

(6) *Interim procedures*—(i) *In general.* If Form 8023 and accompanying instructions do not prescribe making the statement of section 338(h)(10) election on the face of Form 8023, then a separate statement of section 338(h)(10) election must be attached to the Form 8023 filed for T. For purposes of §1.338-1T(e) and paragraph (d)(4) of this section (relating to attachments to target returns and additional filings), this attached statement of section 338(h)(10) election is treated is an integral part of the Form 8023.

(ii) *Contents of separate section 338(h)(10) election statement.* The separate statement of section 338(h)(10) election must—

(A) Contain the name, address, and employer identification number of each of P, T, and the common parent of the S group,

(B) Identify the election as an election under section 338(h)(10) of the Code,

(C) Indicate the date and Service Center where the S group filed its consolidated return for the taxable period that includes the acquisition date or for the last taxable period for which one was filed, and

(D) Be signed by both a person for P and a person for the common parent of the S group each of whom states under penalties of perjury that he or she is authorized to make the section 338(h)(10) election on behalf of P or the S group (as the case may be).

(7) *Delayed elections*—(i) *In general.* In lieu of the simultaneous election requirement of paragraph (d)(1) of this section, a delayed section 338(h)(10) statement of election ("delayed election") may be filed with the Internal Revenue Service Centers with which P and the S group file their respective annual income tax returns in the following two situations:

(A) An express election was made before March 15, 1986 ("transitional election").

(B) An express election was made before the date the target became a section 338(h)(10) target, *i.e.*, before the date that the affiliated group of which the target was a member filed or was required to file a consolidated return ("pre-section 338(h)(10) target election").

(ii) *Time for filing*—(A) *Transitional election.* A transitional section 338(h)(10) election must be filed on or before March 15, 1986.

(B) *Pre-section 338(h)(10) target election.* A pre-section 338(h)(10) target election must be filed on or before the date that is the earlier of *(1)* the 30th day after the day the affiliated group of which the target is a member files a consolidated return for the period that includes the target's acquisition date or *(2)* the 15th day of the 4th month following the close of the S group's taxable year in which the acquisition date occurs.

(iii) *Contents of delayed statement.* The delayed section 338(h)(10) statement of election must contain the same information as required for a separate statement of section 338(h)(10) election by paragraph (d)(6)(ii) of this section except that the election must be prominently identified as a "DELAYED SECTION 338(h)(10) STATEMENT OF ELECTION ON ACCOUNT OF A TRANSITIONAL ELECTION" or "DELAYED SECTION 338(h)(10) STATEMENT OF ELECTION ON ACCOUNT OF A PRE-SECTION 338(h)(10) TARGET ELECTION" (as the case may be).

(iv) *Attachments to delayed statement.* There must be attached to the delayed statement of election copies of both the Form 8023 filed for T and the schedule required under §1.338-1T(e)(1) properly annotated in accordance with paragraph (d)(3) of this section.

(v) *Application of certain provisions.* The delayed section 338(h)(10) statement of election is treated as an integral part of Form 8023 for purposes of §1.338-1T(e) and paragraph (d)(4) of this section as of the day such delayed statement of election is filed.

(vi) *Operating rule.* Beginning with the date an express election is made and until a delayed section 338(h)(10) statement of election is filed for T, all parties shall treat the transaction as if a section 338(h)(10) election is not made. Thus, for example, until the delayed election is made, any recapture gain (as defined in §1.338-4T(h)(2) (iv)) recognized by old T is reported, pursuant to

§1.338-1T(f)(3), by old T in its last return.

(8) *Coordination with consolidated returns regulations.* On or after the day that a section 338(h)(10) election is made for a former member of the S group, the group may not withdraw its consolidated return for the taxable period that includes the acquisition date or for certain periods elect to discontinue filing consolidated returns. See §1.1502-75T.

(e) *Detailed consequences of section 338(h)(10) election.* If a section 338(h)(10) election is made, the following consequences apply:

(1) *Taxable sale of all target assets.* Old T recognizes gain or loss as if, while a member of the S group, it sold all of its assets in a single transaction as of the close of the acquisition date. For determination of deemed selling price, see paragraph (f) of this section. For coordination with sections 337 and 338(h)(12), see paragraph (j) of this section.

(2) *Nonrecognition treatment for target stock*—(i) *General rule.* For purposes of chapter 1 of the Code, gain or loss on the actual sale or exchange by the S group to P of stock of T or of a section 338(h)(10) target affiliate included in a qualified stock purchase is ignored. Likewise, gain or loss on the deemed sale of the stock of a section 338(h)(10) target affiliate that is a subsidiary of T is ignored.

(ii) *Example. The provisions of this subparagraph (2) may be illustrated by the following example:*

Example. S1 owns all of the outstanding stock of T and T1. T1 owns all of the outstanding stock of T2. On March 1, 1986, P purchases all of the outstanding stock of each of T and T1. An express election and a section 338(h)(10) election are made for T. Thus, a deemed election and a deemed section 338(h)(10) election, under paragraph (h) of this section, are caused for T1 and T2. Gain or loss realized by S1 on the actual sale of the T and T1 stock is ignored as is the gain or loss on the deemed sale of T2 stock by old T1. Thus, for example, gain or loss realized on the sale of the T and T1 stock is not taken into account in S1's earnings and profits.

(3) *Deemed section 332 liquidation for target*—(i) *In general.* Except as otherwise provided in this section, the target corporation is treated as if (at the close of the acquisition date but after the deemed sale of its assets) it distributed all its assets in a complete liquidation to which section 332 applies.

(ii) *Cross-references.* (A) For treatment of T stock retained by K and the S group, see paragraph (e)(4) of this section.

(B) For deemed gain recognition election with respect to nonrecently purchased T stock held by P, see paragraph (e)(5) of this section.

(C) For carryovers of old T's tax attributes (*e.g.*, earnings and profits and net operating loss carryovers) to certain members of the S group that owned T stock, see section 381.

(4) *Treatment of unacquired target stock*—(i) *Nonrecognition treatment.* No gain or loss shall be recognized by K or the members of the S group with respect to their shares of T stock that are not acquired by P as part of the qualified stock purchase ("unacquired stock").

(ii) *Basis to K.* K's basis for its new T stock is the same as K's basis for its unacquired old T Stock.

(iii) *Basis to S group.* The basis of the unacquired T stock held by members of the S group shall be equal to the net fair market value of the portion of the new T assets that such members would receive were new T to complete liquidate at the beginning of the day after the acquisition date.

(iv) *Net fair market value.* For purposes of this subparagraph (4), the net fair market value of new T's assets is the excess of their fair market value over new T's liabilities as of the beginning of the day after the acquisition date.

(v) *Fair market value.* For purposes of paragraph (e)(4)(iv) of this section, the fair market value of new T assets is determined in the same manner as is the deemed sale price of old T assets under paragraph (f) of this section except that, if the S group elects the MADSP formula to determine the deemed selling price of old T assets, then the fair market value of new T assets is the MADSP amount determined under paragraph (f)(2)(i) of this section for old T assets.

(vi) *Example.* For an example illustrating S11's basis in unacquired T shares if the MADSP formula is not used, see *Example (4)* in paragraph (g) of this section.

(5) *Deemed gain recognition election.* If P owns shares of nonrecently purchased T stock (as defined in section 338(b)(6)(B)) on the acquisition date, then P shall be deemed to have made a gain recognition election with respect to these shares and to have sold those shares under §1.338-4T(j)(2) *Answer 2* (i).

(6) *Adjusted grossed-up basis*—(i) *In general.* P's adjusted grossed-up basis of T is the sum of—

(A) P's grossed-up basis in recently purchased T stock,

(B) The basis amount (as set forth in section 338(b)(3)(B)) of P's nonrecently purchased T stock,

(C) The liabilities of new T as of the beginning of the day after the acquisition date (other than liabilities that were not liabilities of old T), and

(D) Other relevant items.

(ii) *Allocation.* P's adjusted grossed-up basis for the T stock shall be allocated as basis among the T assets in accordance with section 338(b)(5).

(7) *Effect on consolidated returns*—(i) *General rule.* The deemed sale and liquidation rules of paragraph (e)(1) and (3) of this section apply for purposes of the consolidated return regulations. Illustrations of the preceding sentence are set forth in the remainder of this subparagraph (7).

(ii) *Investment credit recapture.* Any section 38 property deemed sold by T on the close of the acquisition date may be subject to section 47(a) (relating to dispositions of section 38 property). An increase in tax is added to the tax liability of the S group under §1.1502-2 for the taxable period that includes the acquisition date. See §1.1502-3(f)(1).

(iii) *Deferred intercompany transactions*—(A) *Target as selling member.* In general, in the case of an acquisition to which section 381(a) applies, under §1.1502-13(c)(6), the transferee inherits the entire remaining balance of the deferred gain or loss of the transferor. Thus, the member or members of the S group that would be subject to §1.1502-13(d), (e), and (f) (relating to restoration of deferred gain or loss) with respect to T's entire remaining balance of deferred gain or loss as of the close of the acquisition date had T actually liquidated under section 332 are thereafter subject to such provisions as a result of the deemed liquidation under section 332.

(B) *Target as owning member.* Deferred gain or loss is taken into account under §1.1502-13(f)(1) as of the close of the acquisition date by selling members of the S group with respect to any items which T (as the owning member) is deemed to have sold.

(iv) *Cross-references.* See §1.1502-75T(a) for prohibition on selling consolidated group withdrawing a consolidated return on or after the day that a section 338(h)(10) election is made for a former member of the group. See §1.1502-75T(b) for prohibition on selling consolidated group electing to discontinue filing consolidated returns on or after the day that a section 338(h)(10) election is made for a former member of the group.

(8) *Coordination with §§1.338-1T and 1.338-4T*—(i) *References to §1.338-1T.* The following table sets forth the subunits of §1.338-1T and indicates whether each is applicable or irrelevant to this section and section 338(h)(10).

Subunit of §1.338-1T	*Applicable to this section*	*Irrelevant to this section*
(a)		X
(b)(1)-(7)	X	
(b)(8)		X
(c)	X	
(d)	X	
(e)	X	
(f)(1)-(3), (6), and (8)		X
(f)(4), (5), and (7)	X	
(g)		
(h)	X	
(j)	X	
(k)		X
(l)		X

(ii) *References to §1.338-4T.* The following table sets forth the subunits of §1.338-4T and whether each is applicable or irrelevant to this section and section 338(h)(10).

Subunit of §1.338-4T	*Applicable to this section*	*irrelevant to this section*
(a)		X
(b)(1)		X
(b)(2)-(10)	X	
(c)	X	
(d)	X	
(e)	X	
(f)		X
(g)	X	
(h)	X*	
(j)	X**	
(k)(1) Q.1-3	X***	
(k)(1) Q.4-5		X
(k)(2)	X	
(k)(3)	X	
(k)(4)-(6)		X
(l)	X	

***Paragraph (h) of §1.338-4T is modified by paragraph (f) of this section.**

****Paragraph (j) of §1.338-4T is modified by paragraph (e)(5) of this section.**

*****§1.338-4T(k)(1) *Answers 1-3* are applicable as modified by paragraph (j) of this section.**

(f) *Deemed sale price*—(1) *General rule.* The price at which each asset of old T is deemed to have been sold is its fair market value as of the close of the acquisition date.

(2) *Elective MADSP formula.* Under the authority of section 338(h)(11), in lieu of the general rule, the S group may elect to determine the price at which each asset of old T is deemed sold by—

(i) Determining modified ADSP ("MADSP") and

(ii) Then determining the deemed selling price by allocating MADSP to each asset in proportion to its relative fair market value.

(3) *Formula.* The elective formula is:

$$MADSP = G + L + X$$

For purposes of this formula:

(i) "G" is the grossed-up basis of P's recently purchased T stock as set forth in §12.338-4T(h)(3). *Answer 2* (ii).

(ii) "L" is the sum of new T's liabilities as of the beginning of the day after the acquisition date (other than liabilities that were not liabilities of old T).

(iii) "X" is other relevant items.

(4) *Procedure for electing MADSP formula and revoking that election.* The election to apply the MADSP formula is made by attaching to the consolidated Federal income tax return of the S group (including an amended return) for the taxable period in which the acquisition date falls (the "taxable period return") a statement containing the following, or substantially similar, declaration: "THIS RETURN REFLECTS A MADSP FORMULA ELECTION FOR T UNDER SECTION 338(h)(10) AND §1.338(h)(10)-1T(f)". The MADSP election is revoked by attaching to an amended consolidated Federal income tax return of the S group for that taxable period the following, or substantially similar, declaration: "THIS RETURN DOES NOT REFLECT A MADSP FORMULA ELECTION FOR T UNDER SECTION 338(h)(10) AND §1.338(h)(10)-1T(f)". In addition, a MADSP election may be made or revoked in connection with the examination of the taxable period return. A MADSP election made for T also applies to all section 338(h)(10) target affiliates as does the revocation for T. A MADSP election may not be made or revoked if the period within which to make an assessment of tax has expired for any return that would be affected by the election or revocation. For this purpose, a return would be affected by the election (or revocation) if the election (or revocation) would have the effect, directly or indirectly, of increasing the tax liability reported in that return. If a MADSP election is made or revoked, members of the S group shall make proper adjustment to the basis of their unacquired T stock referred to in paragraph (e)(4)(iii) of this section.

(g) *Examples.* The provisions of paragraphs (e) and (f) of this section may be illustrated by the following examples:

Example (1). (i) T is a member of the S group which uses the calendar year. T uses the accrual method of accounting. T has only one class of stock, all of which is owned by S1. On March 1, 1986, S1 sells all of its T stock to P for $80,000 and both an express election and a section 338(h)(10) election are made for T. The S group does not elect the MADSP formula. On that date, assume the following facts:

	Basis	*Fair market value*	*Liability*
Assets:			
Land	$50,000	$75,000	
Equipment (recomputed basis $70,000)	30,000	60,000	
Liability:			
Note payable			$40,000

(ii) The deemed selling price of each old T asset, as determined under the general rule of paragraph (f)(1) of this section, is as follows:

	Fair market value
Land	$75,000
Equipment	60,000

(iii) Under paragraph (e)(1) of this section, old T recognizes $25,000 gain on the deemed sale of the land, *i.e.*, $75,000–$50,000, and ordinary income under section 1245 of $30,000 on the deemed sale of the equipment, *i.e.*, (the lower of fair market value, $60,000, or recomputed basis, $70,000) less adjusted basis, $30,000.

Example (2). (i) Assume the same facts as in *Example (1)*, except that the S group elects the MADSP formula.

(ii) Under paragraph (f)(3) of this section, the MADSP is as follows:

	*Basis**
Land	$50,000
Equipment	30,000
Total	80,000

*Basis shown for reference.

Gain on the deemed sale of the land is $16,667, *i.e.*, $66,667–$50,000. Ordinary income under section 1245 on the deemed sale of the equipment is $23,333, *i.e.*, (the lower of the amount deemed realized, $53,333, or the recomputed basis, $70,000) minus adjusted basis, $30,000.

Example (3). (i) The facts are the same as in *Example (1)*. In addition, assume the following:

(A) As of the close of the acquisition date, old T's current earnings and profits, other than those generated from the deemed sale of its assets, are $21,950. As of the close of 1985, old T had neither accumulated earnings and profits nor a deficit.

(B) Other than earnings and profits, old T has no items described in section 381(c).

(ii) The consequences that obtain to P, T, and S1 include the following:

(A) As determined in *Example (1)*, old T recognizes $25,000 of gain on the deemed sale of the land and $30,000 of ordinary income under section 1245 on the deemed sale of the equipment. Thus, earnings and profits attributable to the deemed sale of all of old T's assets are $55,000.

(B) P's basis in new T stock is P's cost for the stock, $80,000.

(C) The adjusted grossed-up basis of new T is $120,000, *i.e.*, P's cost for the old T stock ($80,000) plus T's liability (note payable, $40,000). (Assume there are no other relevant items.) This adjusted grossed-up basis is allocated as basis among the new T assets under section 338(b)(5).

MADSP = G + L + X
MADSP = $80,000 + $40,000 + 0
MADSP = $120,000

(iii) The portion of MADSP allocated to each asset is determined under paragraph (f)(2)(ii) of this section as follows:

Fair market value	*Fraction*	*Allocable MADSP portion*
$ 75,000	5/9	$ 66,667
60,000	4/9	53,333
$135,000	1	$120,000

(D) Assume that, under §1.1502-33(d), old T's allocable share of the S group's consolidated tax liability for 1986 (all of which is attributable to the deemed sale of T's assets) is $11,950.

(E) As of the close of the acquisition date but after the deemed sale of its assets, old T's earnings and profits are $65,000, *i.e.*, $21,950 + $55,000 − $11,950.

(F) S1 succeeds to and takes into account old T's earning and profits of $65,000, determined as of the close of the acquisition date but after the deemed sale.

(G) S1 does not recognize gain or loss upon its sale of the old T stock to P.

Example (4). (i) Assume the same facts as in *Example (3)* except that S1 sells 80 percent of the old T stock to P for $64,000.

(ii) The consequences that obtain to P, T, and S1 include the following:

(A) P's basis for the new T stock is P's cost for the stock, $64,000.

(B) The adjusted grossed-up basis of new T is $120,000 as in *Example (3)*. The calculation (which is different) is not shown.

(C) S1 does not recognize gain or loss with respect to the retained stock in T.

(D) Under paragraph (e)(4)(iii) of this section, the basis of the T stock retained by S1 is $19,000, calculated as follows:

Net fair market value of T assets as of the beginning of the day after the acquisition date ($75,000 + $60,000 − $40,000)	$95,000
Multiplied by the proportion of T stock retained by S1	.20
Basis of S1's retained 20 percent of T stock	19,000

(E) S1 succeeds to and takes into account old T's earnings and profits of $65,000 as in *Example (3)*.

(F) The other consequences are the same as in *Example (3)*, except to the extent inconsistent with this subdivision (ii).

Example (5). (i) Assume the same facts as in *Example (4)* except that K owns 20 percent of the outstanding T stock and these shares are not purchased by P. K's basis in its T shares is $5,000.

(ii) The consequences that obtain to P, T, and S1 include the following:

(A) Section 1.381(c)(2)-1(c)(2) requires that T's earnings and profits be computed by taking into account the amount of its earnings and profits properly applicable to distributions to minority shareholders. Hence, S1 succeeds to and takes into account 80 percent of T's earnings and profits of $65,000, or $52,000, as a result of the deemed distribution of 80 percent of old T's assets to S1 in the deemed liquidations to which section 332 applies.

(B) K recognizes no gain or loss.

(C) K's basis in its T stock remains at $5,000.

(D) The other consequences are the same as in *Example (4)*, except to the extent inconsistent with this subdivision (ii). The consequences in *Example (4)* with respect to stock retained by S1 are inapplicable.

Example (6). (i) Assume that S1 sells all of its T stock to P and that all of the other facts are the same as in *Example (3)* except that the equipment is held by T1, a wholly-owned subsidiary of T.

(ii) In addition, assume the following:

(A) T1 has no liabilities other than its share of the S group's consolidated tax liability generated by the deemed sale of the equipment, its sole asset.

(B) As of the close of the acquisition date, but before the deemed sale of the equipment, T1 has none of the attributes listed in section 381(c).

(iii) The consequences that obtain to T1 include the following:

(A) The deemed selling price of the equipment, under the general rule of paragraph (f)(1) of this section, is $60,000.

(B) Under paragraph (e)(1) of this section, T1 recognizes ordinary income under section 1245 of $30,000 on the deemed sale of the equipment as determined in *Example (1)*.

(C) Assume that, under §1.1502-33(d), T1's allocable share of the S group's consolidated tax liability for 1986 is $4,950.

(D) As of the close of the acquisition date, but after the deemed sale of the equipment, T1's earnings and profits are $25,050, *i.e.*, $0 + $30,000 − $4,950.

(iv) The consequences that obtain to T include the following:

(A) Old T does not recognize gain or loss upon its deemed sale of the T1 stock.

(B) The deemed selling price of the land, under the general rule of paragraph (f)(1) of this section, is $75,000.

(C) Gain on the deemed sale of the land is $25,000, the same amount as T recognizes in *Example (1)*.

(D) Assume that, under §1.1502-33(d), old T's allocable share of the S group's consolidated tax liability for 1986 is $7,000.

(E) Old T succeeds to and takes into account old T1's earnings and profits of $25,050, determined as of the close of the acquisition date but after the deemed sale by T1 of its asset.

(F) As of the close of the acquisition date, but after the deemed sale of its assets, old T's earnings and profits are $65,000, *i.e.*, $21,950 + $25,050 + ($25,000 − $7,000). (Note that T's current earnings and profits, other than those generated by the deemed sale of its assets, are $21,950, as set forth in subdivision (i)(A) of *Example (3)*.)

(v) The consequences that obtain to S1 include the following:

(A) S1 does not recognize gain or loss upon its sale of the old T stock to P.

(B) S1 succeeds to and takes into account old T's earnings and profits of $65,000, determined as of the close of the acquisition date but after the deemed sale of old T's assets.

(vi) P's basis in the new T stock is P's cost for the old T stock, $80,000.

Example (7). (i) The facts are the same as in Example (6) except that S1 elects to use the MADSP formula and P already owns 20 percent of the T stock which constitutes nonrecently purchased stock. Assume further that P's basis in these shares of nonrecently purchased T stock is $6,000, that P paid $64,000 for the 80 percent of old T stock purchased from S1, and that the fair market value of the T1 stock is $60,000.

(ii) The gain recognized by old T on the deemed sale of its assets is calculated as follows:

(A) Under paragraph (f)(3) of this section, the MADSP for the T assets is as follows:

MADSP = G + L + X
MADSP = $64,000/.8 + $40,000 + 0
MADSP = $80,000 + $40,000 + 0
MADSP = $120,000

(B) The portion of MADSP allocated to each T asset is determined under paragraph (f)(2)(ii) of this section as follows:

	Basis*	Fair market value	Fraction	Allocable MADSP portion
Land	$50,000	$ 75,000	5/9	$ 66,667
T1 stock	**	60,000	4/9	53,333
Total	**	$135,000	1	$120,000

*Amount not stated.

(C) Old T recognizes gain of $16,667 on the deemed sale of the land, *i.e.*, the same amount as T recognizes in *Example (2).*

(D) Old T does not recognize gain or loss upon its deemed sale of the old T1 stock.

(iii) The gain recognized by T1 on the deemed sale of its asset (equipment) is calculated as follows:

(A) Under paragraph (f)(2) of this section, the MADSP for the T1 asset (equipment) is as follows:

(B) MADSP = G + L + X
MADSP = $53,333 + 0 + 0
MADSP = $53,333

(C) Under paragraph (e)(1) of this section, T1 recognizes ordinary income under section 1245 of $23,333 on the deemed sale of the equipment, *i.e.*, (the lower of the amount deemed realized, $53,333, or the recomputed basis, $70,000) minus adjusted basis, $30,000.

(iv) The additional consequences to T1 include the following:

(A) Assume that, under §1.1502-33(d), old T1's share of the S group's consolidated tax liability (all of which is attributable to the deemed sale of old T1's equipment) for 1986 is $3,733.

(B) As of the close of the acquisition date, but after the deemed sale of its asset, T1's earnings and profits are $19,600, *i.e.*, $23,333 − $3,733.

(v) The additional consequences that obtain to T include the following:

(A) Assume that, under §1.1502-33(d), old T's allocable share of the S group's consolidated tax liability for 1986 (all of which is attributable to the deemed sale of old T's land) is $4,667.

(B) Old T succeeds to and takes into account old T1's earnings and profits of $19,600, determined as of the close of the acquisition date but after the deemed sale by T1 of its asset.

(C) As of the close of the acquisition date, but after the deemed sale of its assets, old T's earnings and profits are $53,550, *i.e.*, $21,950 + $19,600 + ($16,667 − $4,667).

(vi) The additional consequences that obtain to S1 include the following:

(A) S1 does not recognize gain or loss upon its sale to P of old T stock (that is recently purchased stock).

(B) S1 succeeds to and takes into account 80 percent of old T's earnings and profits of $53,550, or $42,840, determined as of the close of the acquisition date but after the deemed sale of the T and T1 assets. See §1.381(c)(2)-1(c)(2).

(vii) P is deemed to have made a gain recognition election for its nonrecently purchased T stock. As a result, it recognizes gain of $10,000, calculated under paragraph (e)(5) of this section as follows:

(A) P's grossed-up basis for its recently purchased T stock is $64,000, *i.e.*, the basis of the recently purchased T stock, $64,000, multiplied by the fraction in section 338(b)(4), (1 − .2)/(.8).

(B) P's basis amount for its nonrecently purchased T stock is $16,000, *i.e.*, the grossed-up basis in the recently purchased T stock, $64,000, multiplied by the fraction in section 338(b)(3)(B), (.2/(1.0 − .2).

(C) The recognized gain is $10,000, *i.e.*, the basis amount, $16,000, minus P's basis, $6,000.

(viii) As a result of the deemed gain recognition election, P's basis in the nonrecently purchased T stock is increased from $6,000 to $16,000. P's basis in all the T stock is $80,000, *i.e.*, 64,000 plus $16,000.

(h) *Deemed section 338(h)(10) election*—(1) *In general.* P and S shall be treated as having made a section 338(h)(10) election for any section 338(h)(10) target affiliate if—

(i) P makes an express election for T and

(ii) P and S make a section 338(h)(10) election for T.

(2) *Example.* The provisions of this paragraph (h) may be illustrated by the following examples:

Example (1), On January 1, 1986, and February 1, 1986, P purchases directly from S1 the stock of T and T1, respectively. An express election and a section 338(h)(10) election are made for T. P and S are treated as having made a section 338(h)(10) election for T1.

Example (2). T1 is a wholly-owned subsidiary of T. On March 1, 1987, P purchases all the T stock from S1. An express election and a section 338(h)(10) election are made for T. P and S are treated as having made a section 338(h)(10) election for T1.

(i) [Reserved]

(j) *Coordination with section 337 and section 338(h)(12)*—(1) *General rule.* If all the conditions set forth in paragraph (j)(2) of this section are met, then—

(i) Old T is treated as having distributed all of its assets as of the close of the acquisition date for purposes of section 337 and provisions that relate to section 337 and

(ii) Any items reportable for old T for its last taxable period are included in the S group's consolidated return for the taxable period that includes the acquisition date.

(2) *Conditions.* The conditions referred to in paragraph (j)(1) of this section are as follows:

(i) A section 338(h)(10) election is made for T.

(ii) The provisions of section 338(h)(12) (relating to transaction 337-338 transactions) are satisfied.

(iii) The provisions of section 337(c)(3) (relating to section 337 chain liquidations) are met.

(3) *Exception for section 338(c)(1) percentage.* If the general rule of this paragraph (j) applies, then, under §1.338-4T(k)(1) *Answer 3* (ii), T nevertheless recognizes gain or loss on both actual and deemed sales (that would otherwise by subject to the nonrecognition rule of section 337) to the extent of the section 338(c)(1) percentage.

(4) *Deemed gain recognition election.* The provisions of paragraph (e)(5) of this section (relating to deemed gain recognition election) apply to transactions described in this paragraph (j).

(5) *Examples.* The provisions of this paragraph (j) may be illustrated by the following examples:

Example (1). (i) Individual A owns all of the stock of S1, S1 owns all of the stock of S2, and S2 owns all of the stock of T. These corporations constitute an affiliated group. T has two assets. Asset No. 1, a capital asset, has a basis of $200 and fair market value of $300. Asset No. 2, which is section 1245 property, has a basis of $50 and a fair market value of $75. Its recomputed basis is $60. On January 1, 1986, plans of complete liquidation are adopted for all members of the group, including T. On June 1, 1986, members of the group sell property including all of the T stock, to P. At no time is the plan for T's liquidation rescinded before June 1, 1986 (the acquisition date). An express election and a section 338(h)(10) election are made for T. On October 1, 1986, all of the members of the S group, other than T, distribute their respective assets in complete liquidation.

(ii) The following consequences obtain to the members of the S group, T, and A:

(A) Under section 337(a), no gain or loss is recognized to the members of the S group (including T) upon the actual sale of property (as defined in section 337(b)) including the sale of T stock by S2.

(B) T realizes gain of $125, *i.e.*, ($300 − $200) + ($75 − $50), on the deemed sale of its assets. Since section 337(a) applies, T recognizes only $10 of this gain which is ordinary income under section 1245, *i.e.*, (the lower of the fair market value, $75, or recomputed basis, $60) minus adjusted basis, $50. This ordinary income under section 1245 is reported on the consolidated return of the S group for the taxable period that includes the acquisition date. The remaining realized gain of $115 (*i.e.*, $125–$10) is not recognized under section 337.

(C) Pursuant to section 332, no gain or loss is recognized to S1 upon the complete liquidation of S2.

(D) Pursuant to section 331, gain or loss is recognized to A upon the complete liquidation of S1.

Example (2). Assume the same facts as in *Example (1)*, except that K owns 20 percent of the outstanding T stock and such shares are not disposed of in the transaction. Thus, this section

338(c)(1) percentage (within the meaning of §1.338-4T(h)(2)(v)) is 20 percent. The consequences are the same as in *Example (1)*, except that T recognizes capital gain of $20 on the deemed sale of Asset No. 1, i.e. 20 percent of $100, and section 1231 gain of $3 on the deemed sale of Asset No. 2, *i.e.*, 20 percent of $15.

Example (3). Assume the same facts as in *Example (2)*, except that T makes an actual sale of Asset No. 2 on May 15, 1986, to individual C for $75. The consequences are the same as in *Example (2)*.

(k) *Miscellaneous procedural matters*—(1) *Inapplicability of provisions*. The provisions of section 6043 and §1.332-6 (relating to information returns and recordkeeping requirements for corporate liquidations) shall no apply to the constructive section 332 liquidation of T as provided by paragraph (e)(3) of this section. However, these provisions apply to transactions to which paragraph (j) of this section applies.

(2) *Mooted section 338(h)(9) return*—(i) *Transitional rule*. A deemed sale return for T (as defined in § §1.338-1T(f)(3)(i)) that is subsequently mooted by a section 338(h)(10) election shall be considered a return within the meaning of section 6011 for purposes of section 6513 (relating to time return deemed filed and tax considered paid) and section 6611 (relating to interest on overpayment of tax).

(ii) *Example*. The provisions of this subparagraph (2) may be illustrated by the following example:

Example. On January 1, 1984, P purchases all of the outstanding T stock from S1 and makes an express election for T. Old T's final tax return is filed on April 15, 1984 and the tax due of $10,000 is paid at that time. Subsequently, a delayed statement of a section 338(h)(10) election is filed for T pursuant to the provisions of paragraph (d)(7) of this section. As a result, section 338(h)(10) is elected for T. T is entitled to a refund of $10,000 plus interest thereon from April 15, 1984.

Par. 3. Section 1.338-1T is amended as follows:

1. Paragraph (c) is amended by removing from the first sentence the words "August 23, 1985" and by adding in their place the words "March 15, 1986".

2. Paragraph (e)(1)(i) is amended by—

a. Removing the word "and" from the end of paragraph (e)(1)(i)(B),

b. Removing the period from the end of paragraph (e)(1)(i)(C), and by adding in its place ", and ", and

c. Adding, immediately following paragraph (e)(1)(i)(C), a new paragraph (e)(1)(i)(D) to read as set forth below.

3. Paragraph (e)(1)(ii) is amended by removing, from each place they appear, the words "August 23, 1985" and by adding in their place the words "March 15, 1986".

4. Paragraph (e)(2)(i) is revised to read as set forth below.

5. Paragraph (e)(2)(ii) is amended by removing, from each place they appear, the words "August 23, 1985" and by adding in their place the words "March 15, 1986".

6. Paragraph (e)(3) is amended by inserting in the last sentence after "§1.338-4T(j)(2)" the words "or a section 338(h)(10) election under §1.338(h)(10)-1T(d)".

7. Paragraph (f)(7)(ii) is amended by removing the words "August 23, 1985" and adding in their place the words "March 15, 1986".

8. Paragraph (h) is amended by removing, from each place they appear, the words "August 23, 1985" and by adding in their place the words "March 15, 1986".

9. Paragraph (j)(2) is amended by removing from the third sentence the words "August 23, 1985" and by adding in their place the words "March 15, 1986".

§1.338-1T Elections under section 338(g) of the Internal Revenue Code of 1954 (temporary).

* * * * *

(e) *Schedule; attachments to target returns*—(1) *Schedule of information relating to corporations subject to election*—(i) *Required data*. * * *

(D) If an election under section 338(h)(10) is made, clearly identify (such as by a footnote system) each corporation listed on the schedule which is subject to that election, including corporations subject to deemed section 338(h)(10) elections under §1.338(h)(10)-1T(h).

* * * * *

(2) *Attachments to target returns; additional filings with certain Service Centers*—(i) *Attachments*. Required items must be attached to old target's final return and to the first return of new target. If target is a foreign corporation not subject to United States tax (as defined in paragraph (k)(3)(iii) of this section), the first return of new target is considered to be the return specified in paragraph (k)(6) of this section. If the target is subject to section 338(h)(10) election, the final return of old target is considered to be the return of the selling consolidated group for the taxable period which includes the acquisition date. The required items are (A) a copy of the statement of election, (B) the schedule described in paragraph (e)(1) of this section ("schedule"), and (C) if a gain recognition election under section 338(b)(3) is made in the statement of election, a copy of the gain recognition statement ("GRS"). See §1.338-4T(j)(2) for guidance on the GRS and §1.338(h)(10)-1T(d) for guidance for a section 338(h)(10) election. The requirement of this subdivision (i) applies both to the corporation for which the statement of election is expressly made and to a corporation subject to such a statement by reason of section 338(f)(1).

* * * * *

Par. 4. Section 1.338-4T is amended as follows:

1. Paragraph (f)(5) Answer (vii)(A) is amended by removing the words "[120th day after date of publication of these regulations in the Federal Register]" and by adding in their place the words "March 15, 1986".

2. Paragraph (f)(6)(iv) Answer 1(i)(C)(*1*) is amended by removing the words "August 23, 1985" and by adding in their place the words "March 15, 1986".

3. Paragraph (j)(2) Answer 5(i) is amended by removing from the third sentence the words "August 23, 1985" and by adding in their place the words "March 15, 1986".

Par. 5. Immediately after §1.1502-75 there is added a new §1.1502-75T. The new section reads as follows:

§1.1502-75T Temporary regulations for filing of consolidated returns; coordination with section 338(h)(10).

(a) *Withdrawal of consolidated return barred*. Notwithstanding the last sentence of §1.1502-75(a)(1), a consolidated return for the taxable period that includes the acquisition date (as defined in section 338(h)(2)) may not be withdrawn on or after the day that a section 338(h)(10) election is made for a former member of a selling consolidated group (as defined in §1.338(h)(10)-1T(b)(3)).

(b) *Election to discontinue barred*. Notwithstanding §1.1502-75(c), if a section 338(h)(10) election is made for a former member of a selling consolidated group that has not filed a consolidated return for the taxable period that includes the acquisition date but filed a consolidated return for a preceding taxable period, the selling consolidated group must file a consolidated return for the taxable period that includes the acquisition date and permission to discontinue filing consolidated returns cannot be granted for, and shall not apply to, that period or a preceding period.

* * * * *

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 6. The authority citation for 26 CFR Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 7. Section 602.101(c) is amended by inserting in the appropriate place in the table "§1.338(h)(10)-1T(d), (f)(2), and (f)(4) . . . 1545-0702".

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

Approved December 10, 1985.

Ronald A. Pearlman,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on January 3, 1986, 12:46 p.m., and published in the issue of the Federal Register for January 8, 1986, 51 F.R. 741)

Section 368.—Definitions Relating to Corporate Reorganizations

26 CFR 1.368-2: Definition of terms.
(Also Section 305; 1.305-4.)

Recapitalization; exchange of old stock for three new classes. In a corporation's plan of recapitalization, the exchange by one group of shareholders of voting common stock for newly issued class A voting common stock and nonvoting preferred stock and, by another group of shareholders, the exchange of voting common stock for newly issued class A voting common stock and nonvoting class B common stock is a reorganization within the meaning of section 368(a)(1)(E) of the Code provided the transaction has a bona fide business purpose, is an isolated transaction, and is not part of a plan to increase periodically the proportionate interest of any shareholder in the assets or earnings and profits of the corporation.

Rev. Rul. 86-25

Is the transaction described below a reorganization as defined in section 368(a)(1)(E) of the Internal Revenue Code or is it a distribution of property to which section 301 applies by reason of the application of section 305(b)(3)?

FACTS

X, a closely held domestic corporation, had 3,000 shares of $100 par value voting common stock ("old common") outstanding. For valid business reasons, a plan of reorganization was adopted pursuant to which *X* authorized the issuance of a new class A no par value voting common stock, a new class B no par value nonvoting common stock, and a new class C $100 par value nonvoting, nonparticipating, nonconvertible preferred stock. The only difference between the class A and class B common stock was the voting rights of the class A stock, and the only difference between the class A common stock and the old common stock was the par values. No terms of the old common stock, such as dividend or liquidation rights, are tied to the par value.

The plan of reorganization provided that each outstanding share of old common stock could be exchanged either for one share of class A common stock plus 99 shares of class B common stock, or for one share of class A common stock plus six shares of class C preferred stock. Pursuant to the plan of reorganization, one group of *X* shareholders surrendered 2,500 shares of *X* old common stock in exchange for 2,500 shares of class A common stock and 15,000 shares of class C preferred stock. A second group of shareholders surrendered 500 shares of old common stock in exchange for 500 shares of class A common stock and 49,500 shares of class B common stock. The value of the stock received by each shareholder of *X* was equal to the value of the stock surrendered by such shareholder in the exchange. The exchange of stock was an isolated transaction and not part of a plan to increase periodically the proportionate interest of any shareholder in the assets or earnings and profits of *X*.

LAW AND ANALYSIS

Section 368(a)(1)(E) of the Code provides that the term "reorganization" includes a recapitalization. In *Helvering v. Southwest Consolidated Corp.*, 315 U.S. 194, 202 (1942), 1942-1 C.B. 218, the Supreme Court of the United States defined a recapitalization under a predecessor of section 368(a)(1)(E) as a "reshuffling of a capital structure within the framework of an existing corporation."

Section 354(a) of the Code states that no gain or loss will be recognized if stock in a corporation that is a party to a reorganization is exchanged solely for stock in such corporation.

Section 305(a) of the Code contains the general rule that gross income does not include the amount of any distribution of the stock of a corporation made by such corporation to its shareholders with respect to its stock.

Section 305(b)(3) of the Code provides that section 305(a) shall not apply to a distribution by a corporation of its stock, and the distribution shall be treated as a distribution of property to which section 301 applies if the distribution (or a series of distributions of which such distribution is one) has the result of the receipt of preferred stock by some common shareholders and the receipt of common stock by other common shareholders.

Section 305(c) of the Code provides that a change in redemption price, a difference between redemption price and issue price, a redemption which is treated as a distribution to which section 301 applies, or any transaction (including a recapitalization) having a similar effect on the interest of any shareholder may be treated as a distribution with respect to any shareholder whose proportionate interest in the earnings and profits or assets of the corporation is increased by such change, difference, redemption, or similar transaction.

Section 1.305-7(c)(1) of the Income Tax Regulations provides that a recapitalization (whether or not an isolated transaction) will be deemed to result in a distribution to which section 305(c) of the Code applies if it is pursuant to a plan to periodically increase a shareholder's proportionate interest in the assets or earnings and profits of the corporation.

Section 1.305-7(c)(4) of the regulations provides that an example of the application of section 1.305-7(c) is example (12) of section 1.305-3(e).

In Example (12) contained in section 1.305-3(e) of the regulations, five shareholders owned 300 shares each and five shareholders owned 100 shares each of Corporation *R*'s 2,000 shares of class A stock outstanding. In preparation for the retirement of the five major shareholders, *R*, in a single and isolated transaction, had a recapitalization in which each share of class A stock was exchanged either for five shares of new class B nonconvertible preferred stock plus 0.4 share of new class C common stock, or for two shares of new class C common stock. As a result of the exchanges, each of the five major shareholders received 1,500 shares of class B nonconvertible preferred stock and 120 shares of class C common stock, and the remaining shareholders each received 200 shares of class C common stock. The example concludes that none of the exchanges are within the purview of section 305 of the Code.

In the instant case, had *X* made an outright distribution of the new preferred stock and new class B common stock on the old common stock, the distribution would have been taxable as a distribution of property under section 301 of the Code by reason of the application of section 305(b)(3).

Nevertheless, a transaction that effects a reshuffling of a corporation's capital structure will be respected as a recapitalization exchange to which section 305(b)(3) of the Code does not apply so long as it has a bona fide business purpose and is an isolated transaction and not part of a plan to increase periodically the proportionate interest of any shareholder in the assets or earnings and profits of a corporation. *See* Example (12) in section 1.305-3(e) of the regulations, discussed above. *Compare Bazley v. Commissioner*, 331 U.S. 737 (1947), 1947-2 C.B. 79, (the exchange lacked a bona fide business purpose and was therefore not a reorganization) and section 1.301-1(l) of the regulations (a distribution occurring at the same time as a recapitalization is taxable as a dividend if, in substance, it is not part of the recapitalization).

HOLDING

Under the circumstances set forth above, the exchange of old voting common stock for either class A voting common stock plus class C nonvoting preferred stock or class A voting common stock plus class B nonvoting common stock, will qualify as a tax-free recapitalization under section 368(a)(1)(E) and 354(a) of the Code, and will not be treated as distributions of property to which section 301 applies by reason of the application of section 305(b)(3).

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 54-192, 1954-1 C.B. 99, and Rev. Rul. 54-482, 1954-2 C.B. 148, are amplified.

Section 381.—Carryovers in Certain Corporate Acquisitions

26 CFR 1.381-1: General rule relating to carryovers in certain corporate acquisitions.

Whether recapture of investment credit under section 47 of the Code occurs where a wholly owned subsidiary corporation distributes section 38 property to its parent corporation in complete liquidation and the parent subsequently contributes the property to a partnership in which the parent holds a 75 percent interest. See Rev. Rul. 86-23, page 6.

Section 472.—Last-in, First-out Inventories

26 CFR 1.472-1: Last-in, first-out inventories

LIFO; price indexes; department stores. The November 1985 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, November 30, 1985.

Rev. Rul. 86-26

The following price indexes for November 1985 were issued by the Bureau of Labor Statistics on December 23, 1985, for use by department stores, and are accepted by the Internal Revenue Service, under section 1.472-1(i) of the Income Tax Regulations and Rev. Proc. 72-21, 1972-1 C.B. 745, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, November 30, 1985.

Indexes are prepared on a national basis for the store total, for 20 major groups of departments, and for two special combinations—soft and durable goods. The store total index covers all departments, including some not listed separately, with the following exceptions: candy, foods, liquor, tobacco, paints, and wallpaper, as well as contract departments.

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS

(January 1941 = 100)

		November 1984	November 1985	Percentage Change from Novembe4 1984 to November 1985[1]
I.	Piece Goods	394.9	400.0	1.3
II.	Domestics and Draperies	554.7	554.6	0.0
III.	Women's and Children's Shoes	557.0	558.2	0.2
IV.	Men's Shoes	710.6	728.7	2.5
V.	Infants' Wear	481.4	505.2	4.9
VI.	Women's Underwear	425.4	441.0	3.7
VII.	Women's and Girls' Hosiery	232.4	235.7	1.2
VIII.	Women's and Girls' Accessories	445.9	455.0	2.0
IX.	Women's Outerwear and Girls' Wear	350.4	362.2	3.4
X.	Men's Clothing	475.4	482.4	1.5
XI.	Men's Furnishings	475.5	492.2	3.5
XII.	Boys' Clothing and Furnishings	444.5	457.3	2.9
XIII.	Jewelry	689.4	670.7	−2.7
XIV.	Notions	479.0	487.3	1.7
XV.	Toilet Articles and Drugs	625.0	647.6	3.6
XVI.	Furniture and Bedding	534.8	543.7	1.7
XVII.	Floor Coverings	455.5	458.3	0.6
XVIII.	Housewares	717.0	712.5	−0.6
XIX.	Major Appliances	241.2	245.3	1.7
XX.	Radio and Television	107.7	101.0	−6.2
	Groups I–XV: Soft Goods	477.8	488.1	2.2
	Groups XVI–XX: Durable Goods	445.8	445.6	0.0
	Store Total	468.5	476.2	1.6

[1] Absence of a minus sign before percentage change in this column signifies price increase.

Section 541.—Imposition of Personal Holding Company Tax

26 CFR 1.541-1: Imposition of tax.

Whether a personal holding company subsidiary liquidated into its parent corporation may claim a deduction for dividends paid under section 561 of the Code to the extent of the amount distributed to the parent that represents the subsidiary's undistributed personal holding company income. See Rev. Rul. 86-27, this page.

Section 545.—Undistributed Personal Holding Company Income

26 CFR 1.545-1: Definition.

Whether a personal holding company subsidiary liquidated into its parent corporation may claim a deduction for dividends paid under section 561 of the Code to the extent of the amount distributed to the parent that represents the subsidiary's undistributed personal holding company income. See Rev. Rul. 86-27, this page.

Section 561.—Definition of Deduction for Dividends Paid

26 CFR 1.561-1: Deduction for dividends paid. (Also Sections 541, 545, 562; 1.541-1, 1.545-1, 1.562-1.)

Dividends paid deduction; personal holding company income. A personal holding company subsidiary liquidated into its parent corporation may claim a deduction for dividends paid under section 561 of the Code to the extent of the amount distributed to the parent that represents the subsidiary's undistributed personal holding company income.

Rev. Rul. 86-27

ISSUE

May a personal holding company subsidiary that is liquidated into its parent corporation claim a deduction for dividends paid under section 561 of the Internal Revenue Code to the extent of the amount distributed to the parent that represents the subsidiary's undistributed personal holding company income under the circumstances described below?

FACTS

P and *S* are corporations. *S* was a wholly owned subsidiary of *P*. *P* is, and *S* was, engaged in the business of investing and reinvesting in stocks and securities and collecting, investing, and distributing the income therefrom. *P* is, and *S* was, a personal holding company within the meaning of section 542 of the Code.

In February 1984 the management of each corporation determined that it would be administratively convenient to liquidate *S* and place all of its assets in *P*. Accordingly, the Board of Directors of *S* adopted a resolution containing a plan of complete liquidation under which *S* was to be merged into *P* pursuant to state law. *P* approved and adopted *S*'s plan of liquidation. Pursuant to the plan, the liquidation and merger occurred in November 1985. Neither *P* nor *S* transferred any of *S*'s assets to another corporation before or after *S*'s liquidation except to unrelated third parties in the ordinary course of their businesses of investing and reinvesting in stocks and other securities. *S* sought to take its liquidation distribution into account when computing its undistributed personal holding company income under section 545(a) for the taxable year of the distribution.

LAW AND ANALYSIS

Section 541 of the Code provides for the imposition of a personal holding company tax for each tax year on the undistributed personal holding company income of personal holding companies equal to 50 percent of the undistributed personal holding company income.

Section 545(a) of the Code provides that the term "undistributed personal holding company income" means taxable income of a personal holding company adjusted in the manner provided in subsections (b), (c), and (d), minus the dividends paid deduction.

Section 561(a) of the Code provides that the deduction for dividends paid shall be the sum of (1) the dividends paid during the taxable year, (2) the consent dividends for the taxable year (determined under section 565), and (3) in the case of a personal holding company, the dividend carryover described in section 564.

Section 562(a) of the Code provides that the term "dividend" shall, except as otherwise provided in this section, include only dividends described in section 316 (relating to definition of dividends for purposes of corporate distributions).

Section 562(b)(2) provides that in the case of a complete liquidation of a personal holding company occurring within 24 months after the adoption of a plan of liquidation, the amount of any distribution within that period pursuant to the plan shall be treated as a dividend for purposes of computing the dividends paid deduction, to the extent the amount is distributed to corporate distributees and represents the distributees' allocable share of the undistributed personal holding company income for the taxable year of the distribution computed without regard to this paragraph and section 316(b)(2)(B).

Section 1.562-1(b)(2)(i) of the Income Tax Regulations notes that section 562(b)(2) of the Code makes an exception to the general rule that a deduction for dividends paid is permitted only with respect to dividends described in section 316. This regulation also provides that amounts distributed in liquidation in a transaction which is preceded or followed by a transfer to another corporation of all or part of the assets of the liquidating corporation may not be eligible for the dividends paid deduction. This language indicates that a dividends paid deduction in the context of a complete liquidation will be closely scrutinized to assure that the benefit of the deduction is only obtained if there is in fact a complete liquidation. Thus, the dividends paid deduction will not be available where the distributed assets are reincorporated by the distributee.

Section 1.562-1(b)(2)(ii) of the regulations provides that the corporate distributees' allocable share of undistributed personal holding company income for the taxable year of the distribution (computed without regard to sections 316(b)(2)(B) and 562(b)(2) of the Code) shall be determined by multiplying the undistributed personal holding company income by the ratio which the aggregate value of the stock held by all corporate shareholders immediately before the record date of the last liquidating distribution in the year bears to the total value of all stock outstanding on that date.

In the present situation *S* was a personal holding company and *P* was a corporate distributee. *S*'s complete liquidation occurred within 24 months of adoption of the plan of liquidation. Because *S* was a wholly owned subsidiary of *P*, the amount distributed to *P*, to the extent it represents *S*'s undistributed personal holding company income, represented *P*'s allocable share of that income within the meaning of section 562(b)(2) of the Code. In addition, none of *S*'s assets was transferred to another corporation before or after *S*'s liquidation except to unrelated third parties in the ordinary course of *P*'s or *S*'s business of investing and reinvesting in stocks and securities. Any such transfer did not affect the complete nature of *S*'s liquidation and, therefore, the abuse that section 1.562-1(b)(2)(i) of the regulations was intended to prevent is absent. Under these circumstances *S*'s liquidation falls within the scope of section 562(b)(2) and the regulations thereunder.

HOLDING

A personal holding company subsidiary that is liquidated into its parent corporation may claim a deduction for dividends paid under section 561 of the Code to the extent of the amount distributed to the parent that represents the subsidiary's undistributed personal holding company income under the circumstances described above.

Section 562.—Rules Applicable in Determining Dividends Eligible for Dividends Paid Deduction

26 CFR 1.562-1: Dividends for which the dividends paid deduction is allowable.

Whether a personal holding company subsidiary liquidated into its parent corporation may claim a deduction for dividends paid under section 561 of the Code to the extent of the amount distributed to the parent that represents the subsidiary's undistributed personal holding company income. See Rev. Rul. 86-27, page 20.

Section 721.—Nonrecognition of Gain or Loss on Contribution

26 CFR 1.721-1: Nonrecognition of gain or loss on contribution.

Whether recapture of investment credit under section 47 of the Code occurs where a wholly owned subsidiary corporation distributes section 38 property to its parent corporation in complete liquidation and the parent subsequently contributes the property to a partnership in which the parent holds a 75 percent interest. See Rev. Rul. 86-23, page 6.

Section 723.—Basis of Property Contributed to Partnership

26 CFR 1.723-1: Basis of property contributed to partnership.

Whether recapture of investment credit under section 47 of the Code occurs where a wholly owned subsidiary corporation distributes section 38 property to its parent corporation in complete liquidation and the parent subsequently contributes the property to a partnership in which the parent holds a 75 percent interest. See Rev. Rul. 86-23, page 6.

Section 1012.—Basis of Property—Cost

26 CFR 1.1012-1: Basis of property.

What portion of the purchase price of a cow impregnated with an embryo must be allocated between the cow and the calf subsequently born. See Rev. Rul. 86-24, page 7.

Section 1231.—Property used in the Trade or Business and Involuntary Conversions

26 CFR 1.1231-2: Livestock held for draft, breeding, dairy or sporting purposes.

Whether cows purchased for breeding purposes qualify as property used in the taxpayer's trade or business. See Rev. Rul. 86-24, page 7.

Section 1502.—Regulations [Consolidated Returns]

26 CFR 1.1502-75T: Temporary regulations for filing of consolidated returns; coordination with section 338(h)(10).

Election under section 338(h)(10) of the Code for a former member of a consolidated group. See T.D. 8068, page 9.

Section 4051.—Imposition of Tax on Heavy Trucks and Trailers Sold at Retail

Whether, for purposes of determining the taxable sale price of a highway vehicle under section 4052(b) of the Code, a dealer may exclude as the fair market value at retail of the tires, a predetermined price established by the tire manufacturer under Federal Trade Commission regulations for warranty adjustment purposes. See Rev. Rul. 86-28, below.

Section 4052.—Definitions and Special Rules

26 CFR 145.4052-1: Special rules and definitions.
(Also Section 4051.)

Sale price of truck; tire exclusion; use of predetermined price. A vehicle retailer that does not have an established retail price of tires may use the tire manufacturer's predetermined price established by the manufacturer under Federal Trade Commission (FTC) regulations in determining the retail fair market value of the tire pursuant to section 4052(b)(1)(B)(iii) of the Code.

Rev. Rul. 86-28

ISSUE

For purposes of determining the taxable sale price of a highway vehicle under section 4052(b) of the Internal Revenue Code, if a vehicle dealer does not have an established lowest retail price of tires, may the dealer exclude, as the fair market value at retail of the tires, a predetermined price established by the tire manufacturer under Federal Trade Commission (FTC) regulations for warranty adjustment purposes?

FACTS

X, a vehicle dealer, sells at retail trucks and trailers that are subject to the tax imposed by section 4051(a)(1) of the Code. Some of the vehicles sold by *X* are equipped with tires manufactured by *Y*. *X* does not make separate sales of *Y*'s tires at retail, and *Y* does not provide *X* with manufacturer's suggested retail prices for any of its tires. Title 16 C.F.R. section 228.16 (1985) contains the FTC rules concerning the advertising of tire warranties. Section 228.16(b) provides that to avoid deception of purchasers as to the value of guarantees, adjustments should be made on the basis of a price which realistically reflects the actual selling price of the tire. Under section 228.16(b)(3), a predetermined price which fairly represents the actual selling price of the tire is considered to be an appropriate price base for making such guarantee adjustments.

In accordance with this FTC regulation, *Y* has published a predetermined price list which consists of the average selling prices for which its retail dealers sell their tires. It is based on an annual survey that *Y* performs in its markets in the United States.

LAW AND ANALYSIS

Section 4051(a)(1) of the Code imposes on the first retail sale of certain truck and trailer chassis and bodies (including in each case parts or accessories sold on or in connection therewith or with the sale thereof) a tax of 12 percent of the amount for which the article is so sold.

Section 145.4052-1(d)(2)(iii) of the Code provides that in determining the price for which an article is sold, there shall be excluded the fair market value (including any tax imposed by section 4071) at retail of any tires (not including any metal rim or rim base).

Section 145.4052-1(d)(2)(iii) of the Temporary Excise Tax Regulations, as amended by T.D. 8050, 50 Fed. Reg. 37350, 37351 (1985), 1985-42 I.R.B. 12, provides that the fair market value at retail of tires shall be determined by the lowest established price for which the vehicle retailer would sell such tires at retail in the ordinary course of trade. The lowest established price is the lowest price for which the vehicle retailer sells, or offers to sell, a single tire to an independent purchaser who would not ordinarily be expected to buy more than one. If the vehicle retailer has no lowest established price, the Commissioner will accept any price, provided that, under the facts and circumstances, such price is not unreasonable. (For vehicles sold on or after April 1, 1983, and before October 13, 1985, a price will not be considered unreasonable if it is no more than an amount equal to 50 percent of the manufacturer's suggested retail price.)

As *X* does not make separate sales of *Y*'s tires at retail, it does not have a lowest established price for which it sells, or offers to sell, such tires to independent purchasers within the terms of section 145.4052-1(d)(2)(iii) of the temporary regulations. In the absence of a lowest established price for *Y*'s tires, the Commissioner will accept from *X*, as the fair market value at retail of the tires, any price that is not unreasonable. The use of *Y*'s predetermined price (which was developed for purposes of 16 C.F.R. section 228.16 and which is computed annually on the average actual sale price of *Y*'s tires by its dealers) is not unreasonable.

In lieu of using the tire manufacturer's predetermined price, however, a vehicle retailer can continue to use any price not unreasonable under the facts and circumstances test, as set forth in section 145.4052-1(d)(2)(iii) of the Temporary Excise Tax Regulations.

HOLDING

A vehicle retailer that does not have an established lowest retail price of tires because such retailer does not make separate sales of tires at retail may use, but is not required to use, the tire manufacturer's predetermined price as defined in 16 C.F.R. section 228.16(b)(3) in determining the retail fair market value of a tire pursuant to section 4052(b)(1)(B)(iii) of the Code.

Section 6041.—Information at Source

26 CFR 1.6041-1: Return of information as to payments of $600 or more.

Whether Schedule K-1 of Form 1041 is an information return for purposes of sections 6041(a) and 6652(a)(1)(A) of the Code. See Rev. Rul. 86-29, below.

Section 6652.—Failure to File Certain Information Returns, Registration Statements, Etc.

26 CFR 301.6652-1: Failure to file certain information returns.
(Also Section 6041; 1.6041-1.)

Returns; information; failure to file; Form 1041, Schedule K-1. Schedule K-1 is considered an information return that is required to be timely filed with Form 1041, U.S. Fiduciary Income Tax Return. Trusts that fail to file Schedule K-1, file K-1s that omit material information, or file substitute K-1s not in an approved format, are subject to the penalty under section 6652(a)(1)(A) of the Code.

Rev. Rul. 86-29

ISSUE

For purposes of the penalty imposed by section 6652(a)(1)(A) of the Internal Revenue Code, does the term "statement of the amount of payments to another person required by . . . section 6041(a)" of the Code include Schedule K-1 to Form 1041 (U.S. Fiduciary Income Tax Return)?

FACTS

Situation 1 Trust *TrA* filed Form 1041, U.S. Fiduciary Income Tax Return, and made payments to each beneficiary of $600 or more in a taxable year, but failed to file any of five required Schedules K-1 with the Form 1041.

Situation 2: Trust *TrB* filed Form 1041 and filed Schedules K-1, and made payments to each beneficiary of $600 or more in a taxable year, but omitted certain material information from three of the five schedules.

Situation 3: Trust *TrC* filed Form 1041 and made payments to each beneficiary of $600 or more in a taxable year, but filed five "substitute" Schedules K-1 (summaries). Contrary to the requirements in Rev. Proc. 83-9, 1983-1 C.B. 639 and in the instructions to Schedule K-1 (Form 1041) the substitutes were not in an approved format and were unprocessible.

LAW AND ANALYSIS

Section 6041(a) of the Code provides, with certain exceptions not here relevant, that all persons engaged in a trade or business and making payment in the course of such trade or business to another person of rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable gains, profits, and income of $600 or more in any taxable year shall render a true and accurate return to the Secretary, under such regulations and in such form and manner and to such extent as may be prescribed by the Secretary, setting forth the amounts of such gains, profits, and income, and the name and address of the recipient of such payment.

Section 6652(a)(1)(A) of the Code provides that in the case of each failure to file a statement of the amount of payments to another person required by section 6041(a) or (b) (relating to certain information at source) on the date prescribed therefore (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid (upon notice and demand by the Secretary and in the same manner as tax) by the person failing to file the statement, $50 for each such failure, but the total amount imposed on the delinquent person for all such failures during any calendar year shall not exceed $50,000.

Section 1.6041-1(a)(2) of the Income Tax Regulations provides that information returns are required to be made on Forms 1096 and 1099 except that the return with respect to distributions to beneficiaries of a trust or of an estate shall be made on Form 1041. Instructions for Form 1041 and Schedules A, B, D, J and K-1, state that a Schedule K-1 must be filed with Form 1041 to report a beneficiary's income from the estate or trust. The instructions also describe acceptable substitute Schedules K-1. Form 1096, instruction paragraph K, "Other Information Returns," lists the Schedule K-1 for Form 1041 and states that income information reported on the K-1s must not be reported on any of the other Forms covered in the instructions to Form 1096.

In *Commissioner v. Lane-Wells Co.*, 321 U.S. 219, 223 (1944), 1944 C.B. 540, the Supreme Court noted that the Congress gave discretion to the Commissioner to prescribe by regulation forms of returns. The discretion was granted so that the Commissioner would not only obtain necessary tax information but obtain that information with such "uniformity, completeness, and arrangement that the physical task of handling and verifying returns may be readily accomplished."

The Schedules K-1 are required to be filed with Form 1041 and serve the function of reporting the income of a beneficiary of an estate or trust. Thus, the schedules are among the information returns required by section 1.6041-1(a)(2) of the regulations.

In *Situation 1*, *TrA* filed Form 1041 but failed to file five Schedules K-1. In *Situation 2*, *TrB* omitted material information on three of five Schedules K-1. In *Situation 3*, *TrC* filed five substitute Schedules K-1 that were not in an approved format.

Thus, in the three situations the Schedules K-1 either were not furnished to the Service or were not in acceptable format. The Service, therefore, was hindered in carrying out its responsibility of performing the information collection duties placed upon it by Congress.

HOLDINGS

For purposes of the penalty imposed by Section 6652(a)(1)(A) of the Code, the term "statement of the amount of payments to another person required by . . . Section 6041(a)" of the Code includes Schedule K-1 to Form 1041. Therefore, the consequence of the three fact situations would be as follows:

Situation 12. *TrA*'s failure to file five Schedules K-1 resulted in five failures to file an information return for the purpose of imposing the penalty provided by section 6652(a)(1)(A) of the Code.

Situation 2. *TrB*'s failure to provide the missing information for three of five Schedules K-1 resulted in three failures to file an information return for the purpose of imposing the penalty provided by section 6652(a)(1)(A) of the Code.

Situation 3. *TrC*'s failure to file five substitute Schedules K-1 in an approved and processible format resulted in five failures to file an information return for the purpose of imposing the penalty provided by section 6652(a)(1)(A) of the Code.

Section 7701.—Definitions

26 CFR 301.7701-2: Associations.

Limited partnerships. The states of

Alabama, Minnesota, Nebraska, Oklahoma, West Virginia, and Wisconsin are added to the list of states that have enacted legislation that corresponds to the Uniform Limited Partnership Act for purposes of section 301.7701-2 of the regulations. Rev. Rul. 84-80 amplified.

Rev. Rul. 86-30

In Rev. Rul. 84-80, 1984-1 C.B. 275, Rev. Rul. 84-180, 1984-2 C.B. 314, and Rev. Rul. 85-178, 1985-43 I.R.B. 16, the Internal Revenue Service listed several states that revised their limited partnership statutes following the promulgation of the Revised Uniform Limited Partnership Act. The Service determined that the legislation enacted by those states corresponds to the Uniform Limited Partnership Act ("ULPA") for purposes of section 301.7701-2 of the Procedure and Administration Regulations.

The Service has determined that the following additional states have enacted legislation that, as of the effective date, corresponds to ULPA for purposes of section 301.7701-2 of the regulations:

ALABAMA: Ala. Code sections 10-9A-1 through 10-9A-203 (Supp. 1984) effective January 1, 1984.

MINNESOTA: Minn. Stat. Ann. sections 322A.01 through 322A.87 (West 1982) effective January 1, 1981.

NEBRASKA: Neb. Rev. Stat. Sections 67-237 through 67-297 (R.S. Supp., 1982) effective January 1, 1982.

OKLAHOMA: Okla. Stat. Ann. tit. 54, sections 301 through 364 (West Supp. 1984) effective November 1, 1984.

WEST VIRGINIA: W. Va. Code sections 47-9-1 through 47-9-63 (Michie Supp. 1984) effective January 1, 1982.

WISCONSIN: Wis. Stat. Ann. sections 179.01 through 179.94 (West Supp. 1984) effective September 1, 1984.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 84-80 is amplified.

Section 7805.—Rules and Regulations

26 CFR 301.7805-1: Rules and regulations

Administrative procedure for appeal of certain assessed penalties described in Rev. Proc. 78-1 is obsolete. See Rev. Proc. 86-10, page 25.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.104: Collection functions.
(Also Part I, Section 7805; 301.7805-1.)

Rev. Proc. 86-10

Rev. Proc. 78-1, 1978-1 C.B. 550, implemented on a trial basis procedures for appeal of assessments of certain additions to tax, additional amounts, and penalties. That revenue procedure is obsolete. Procedures for appeal of such assessment are now found in sections 601.106(a)(1)(ii)(c) and 601.106-(a)(1)(iii) of the Statement of Procedural Rules.

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26 CFR 601.602: Tax forms and instructions.

Rev. Proc. 86-11

SECTION 1. PURPOSE

The purpose of this Revenue Procedure is to notify the public that the Internal Revenue Service has revised its policies set forth in Revenue Procedure 85-14, 1985-1 C.B. 515, regarding the user charge and user guidelines for the Internal Revenue Service Videotex Tax Library.

SEC. 2. BACKGROUND

.01 The Internal Revenue Service produces an annual library of tax information that is formatted for electronic publishing (information retrieval and videotex) applications. This library (database) consists of selected Taxpayer Information Publications (TIPS) as well as tax information briefs and other items.

.02 The public also has the option of obtaining magnetic tapes of the Taxpayer Information Publications and other items in unformatted masterfile form. These masterfiles have their elements identified by Standard Generalized Markup Language (SGML) concepts.

SEC. 3. PROCEDURE

.01 A user charge of $0.11 per thousand characters will be charged for magnetic tapes of the library.

.02 Information on the configuration and acquisition of the magnetic tapes containing the library and masterfile tapes can be obtained from the address referenced in Section 5.

SEC. 4. LIMITATIONS

.01 All material contained on the tapes may be used freely. A citation to the publication number and title would be appropriate.

.02 As an alternative method of ordering forms and publications, the Internal Revenue Service has instituted the Order Entry Program. Order Entry allows subscribers to commercial videotex services to order forms and publications through their service's network. These orders are filled by the Internal Revenue Service. Any vendor or service desiring to participate in the Order Entry Program must conform with the procedures and specifications prescribed by the Service.

SEC. 5. INQUIRIES

Any inquiries in regards to this Revenue Procedure should be made to Internal Revenue Service, 1111 Constitution Avenue, N.W., Room 1231, Washington, D.C. 20224, Attention: PM:S:FM:P.

SEC. 6. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 85-14, 1985-1 C.B. 515, is superseded.

Regulations Governing the Practice of Attorneys, Certified Public Accountants, Enrolled Agents, and Enrolled Actuaries Before the Internal Revenue Service

Notice 86-2

AGENCY: Department of the Treasury.

ACTION: Final rule.

SUMMARY: This document contains final regulations governing practice before the Internal Revenue Service (31 CFR Part 10) by requiring that those who are enrolled to practice before the Internal Revenue Service renew their enrollment on a periodic basis. A condition of eligibility for renewal of enrollment will be the satisfaction of continuing professional education requirements. The rule also establishes a fee for the renewal of enrollment. The fee will be for the purpose of defraying the costs of administering the program. In addition, this notice contains modifications of the regulations reflecting the transfer to the Office of Director of Practice certain functions formerly performed by the Commissioner of Internal Revenue relative to the enrollment of individuals who wish to practice before the Internal Revenue Service.

DATE: These final regulations are effective January 22, 1986.

FOR FURTHER INFORMATION CONTACT: Mr. Leslie S. Shapiro, Director of Practice, Internal Revenue Service, Washington, DC 20224 (202) 535-6787.

SUPPLEMENTARY INFORMATION:

BACKGROUND AND COMMENTS

The administration of the program relating to the enrollment of those who wish to practice before the Internal Revenue Service was transferred to the Office of Director of Practice in 1982. At that time a complete study was made of the enrollment process and the applicable regulations. Those regulations accord individuals permanent enrollment with no need to renew that status. There are over 33,000 enrolled individuals on the enrollment roster. However, there is no means for determining the accuracy of that roster. For example, persons on the roster may have passed away, have become certified public accountants or attorneys, no longer have a need to retain their enrollment status, etc. Consequently, as a sheer "housekeeping" measure, renewal of enrollment was deemed necessary. At the same time, consideration was given the desirability of continuing professional education for the enrollee community. In this regard, the public relies on tax practitioners to be competent and skillful in representing taxpayers' interests before the Internal Revenue Service. The Internal Revenue Service also relies on the competence and skill of tax practitioners. Continuing professional education was found to be the most widely accepted means of retaining the knowledge of a professional and of keeping abreast of changes in the subject matter, methodology and state of the art applicable to a particular profession. It also was determined that most professions, both learned and trade, have mandated continuing professional education as a requirement for continued licensure. For example, 46 states require continuing professional education as a condition for certified public accountants to retain their active licenses to practice. For those who are enrolled to practice before the Internal Revenue Service, the need for continuing professional education is manifest. Our Federal tax laws and procedures are volatile and dynamic. In 1984 alone, massive changes were made in the Internal Revenue Code by the Tax Reform Act of 1984 (Pub. L. 98-369); the Retirement Equity Act of 1984 (Pub. L. 98-397); the Child Support Enforcement Amendments of 1984 (Pub. L. 98-378); Pub. L. 98-573; Pub. L. 98-611; and Pub. L. 98-612. The benefits of continuing one's education in the tax area and related subjects are abundant; the detriments appear to be non-existent. Accordingly, it was concluded that formalization of a continuing professional education program for individuals enrolled to practice before the Internal Revenue Service would be in the best interest of the public and would be consistent with what has been found necessary and desirable for the other professions in our country. The requirements and methodologies of the continuing education programs of other professions, particularly those relating to certified public accountants, also were studied. Our proposals were based on those studies and on recommendations made to us by representatives of the enrolled practitioner community.

On July 3, 1984, the Treasury Department published in the Federal Register (49 FR 27326) an advance notice of proposed rulemaking that would amend the regulations governing practice before the Internal Revenue Service contained in 31 CFR Part 10 (Treasury Department Circular No. 230). The notice addressed the Treasury Department's intent to require those enrolled to practice before the Internal Revenue Service (enrolled agents) to renew their enrollment status on a periodic basis. A condition for renewal would be the satisfaction of continuing education requirements described in the notice. Comments on the advance notice were invited.

On April 23, 1985, the Treasury Department published in the Federal Register (50 FR 15937) a proposed rule to amend the regulations governing practice before the Internal Revenue Service. The notice of proposed rulemaking addressed the comments on the advance notice, and a number of modifications were made.

Approximately thirty-five written comments on the proposed rule were received. After consideration of all comments regarding the proposed rule, it is hereby adopted with modifications as explained below.

COMMENTS

1. A number of comments support the proposal in its entirety. Other comments supporting the concept of continuing professional education have raised concerns the same as those raised in response to the advance notice of proposed rulemaking. (a) One such concern is that the scope of the proposal should be extended to include attorneys and certified public accountants as well as enrolled agents. The concern was addressed in detail in the notice of proposed rulemaking. We continue to endorse the concept that all who practice before the Internal Revenue Service should further their knowledge of Federal tax laws and procedures. However, as discussed in the notice of proposed rulemaking, the Agency Practice Act, 5 U.S.C. 500, prohibits the Treasury Department from placing any limitation or qualification on the recognition of an attorney or certified public accountant who has met the conditions of the statute. Accordingly, to require continuing education of attorneys and certified public accountants would not be a condition for renewal of enrollment since they are not enrolled to practice before the Internal Revenue Service by the Treasury Department; to require it as a condition of eligibility to practice before the Internal Revenue Service would be a limitation not permitted by law. (b) A similar concern is that licensed public accountants in some jurisdictions must meet state licensing authorities' continuing education requirements in order to maintain their good standing. As a result, they should not be subject to the continuing education requirements of the proposal. We continue to believe the requirements of the regulations should be applied evenly to all enrolled agents, regardless of licensed public accountant status. An undue hardship is not anticipated for those individuals to meet the continuing education requirements for renewal of enrollment. We expect that satisfaction of recognized continuing education programs in the field of taxation which meet state requirements also will meet the Treasury Department requirements. Consequently, it is more likely than not that a licensed public accountant will satisfy, through one continuing education program, both his or her state's continuing education requirements and those of the Treasury Department. (c) Another comment supporting continuing professional education expresses concern that regulations relating to those who prepare Federal tax returns are nonexistent even though such individuals may be in the most need of continuing professional education. This is an area not under the jurisdiction of regulations in 31 CFR Part 10, since preparers of tax returns are not required to be attorneys, certified public accountants, or enrolled agents. We therefore cannot act on this comment.

2. Comments were received regarding the number of continuing professional education hours required for renewal of enrollment. Concern has been expressed that the number of hours required in the proposal is insufficient. Other commenters believe that the proposed required hours are too rigorous. Further comments reflect concern that the unavailability of sufficient courses in certain geographic areas and the registration costs for some courses may make it inconvenient or difficult to meet the continuing education requirements of the proposal. The same comments in response to the advance notice were considered, together with a further analysis of the various state requirements regarding certified public accountants. As a result, the notice of proposed rulemaking reduced the number of hours from 30 hours per year (90 hours over a three year period) to 24 hours per year (72 hours over a three year period). In addition, the proposal contemplates that qualifying correspondence and home study courses may be utilized to satisfy the requirements of the regulations. The number of hours in the proposal is what is believed necessary to sustain continuing professional education and is in fact less than that required of professionals by most licensing agencies. A sound program cannot be effected if the number of hours is reduced. In addition, we con-

tinue to believe that correspondence and/or home study courses will be appropriate for those who find the availability of other courses inconvenient because of geographic location or cost. Correspondence and home study courses are those programs not qualifying as formal group sessions under the regulations and which: (1) Are offered by qualified sponsors; (2) provide a means for measuring completion of the course by the attendees, e.g. written test; (3) have certificates of completion issued by the sponsor specifying subject matter and recommended continuing education credit hours; and (4) require that the sponsor maintain written records relating to each student and of the program outline for a period of three years immediately following completion of the program by each student.

3. Concern has been expressed regarding the amount of the renewal fee, hoping it will not be a revenue raising measure. We are obliged to follow the guidelines on user charges issued by the Office of Management and Budget. Under those guidelines, a reasonable charge is made to each identifiable recipient from a measurable unit or amount of government service from which he or she derives a special benefit. In this connection, the government agency is responsible for establishing the charges based on a determination of estimated costs for carrying out the activity. Those costs include such things as salaries, management, research and enforcement. The maximum charge or fee is governed by the total cost of the program. The costs and charges must be reviewed periodically. The renewal fee, which will be consistent with such guidelines, is not expected to be prohibitive. It clearly will not be a revenue raising measure in the sense the comments indicate.

4. Some comments address the renewal period. The notice of proposed rulemaking establishes the renewal period to be three years. The comments suggest the renewal period be changed from three years to either two years or four years. The reason for the suggestion appears to be that two years would be consistent with most state continuing professional education programs for certified public accountants. An analysis of the continuing education requirements of State Boards of Accountancy has disclosed that approximately fifty per cent of the states requiring continuing education have a biennial reporting period and approximately fifty per cent have triennial reporting period. We believe that to achieve operating efficiency and in the interest of the planning of individuals enrolled to practice before the Internal Revenue Service, a three year enrollment period is the most beneficial. Consequently, the renewal cycle will remain the same as in the proposal.

5. Concern has been expressed regarding the time period during which individuals enrolled to practice before the Internal Revenue Service must apply for renewal of enrollment. The proposal contemplates applications for renewal to be made between October 1 and December 31. The commenters suggest the filing of renewal applications should be extended from December 31 to January 31 to allow individuals who participate in year-end tax updates to file a renewal application timely. We concur in this suggestion. Thus, all individuals enrolled to practice before the Internal Revenue Service will be required to apply for renewal during the period November 1, 1986 to January 31, 1987. The first effective date of renewal will be April 1, 1987. Thereafter, applications for renewal will be required during the period between November 1, 1989 and January 31, 1990 and between November 1 and January 31 every third year subsequent thereto.

6. Consistent with the above modifications, a change also is required relating to the time period in which to satisfy the continuing professional education requirements. In this regard, the notice of proposed rulemaking requires that a minimum of 24 hours of continuing education credit be completed between January 1, 1986 and December 31, 1986. A minimum of 72 hours of continuing education credit is required to be completed between January 1, 1987 and December 31, 1989, and during each three year period subsequent thereto. The final rule has been changed to provide that a minimum of 24 hours of continuing education credit must be completed between January 1, 1986 and January 31, 1987, and a minimum of 72 hours of continuing education credit must be completed between February 1, 1987 and January 31, 1990, and during each three year period subsequent thereto.

7. Comments were received regarding the additional hours of continuing professional education an individual who fails to meet the continuing education requirement would be required to attain. The proposal requires four additional hours for each month an individual's enrollment is inactive, not to exceed 36 hours, if there has been a failure to satisfy the continuing education requirement of the regulations. The comments suggest this may be an onerous burden. An individual is precluded from practice before the Internal Revenue Service for failure to comply with the requirement. The additional hours requirement would only exacerbate the problem of those who have not complied with the continuing education requirement and are ineligible for renewal of enrollment to practice before the Internal Revenue Service. We concur in this suggestion. Thus, an individual who fails to comply with the continuing education requirement and is determined ineligible to practice before the Internal Revenue Service by reason thereof may be reinstated upon completing the continuing education requirement of the renewal period immediately preceding the reapplication period and filing the renewal application with the Director of Practice. The individual would be required to comply with the continuing education requirement of the enrollment cycle in which he or she is reinstated. The "make-up" hours cannot be used for this purpose.

8. There has been an expression of concern that those ineligible to practice before the Internal Revenue Service should not indicate in any manner that they are eligible to practice before the Internal Revenue Service. While such prohibition was implicit in the proposed rule, the final rule makes it explicit. Any individual ineligible to practice before the Internal Revenue Service for failure to renew enrollment is prohibited, in any manner, from directly or indirectly indicating he or she is enrolled to practice before the Internal Revenue Service and from using the term "enrolled agent," the designation "E.A." or other form of reference to eligibility to practice before the Internal Revenue Service.

9. Concern has been expressed that consideration should be given to indi-

viduals who voluntarily request being placed in an inactive status, thereby permitting such individuals to retire from enrollment with dignity. We believe this suggestion to be sound, and have provided in the final rule that an individual may request that his/her enrollment be placed in an an inactive status on the basis of retirement from practice before the Internal Revenue Service or for other reasons the Director of Practice will consider on an individual basis. An individual in an inactive retirement status may not practice before the Internal Revenue Service and may only hold his/her former enrollment status if such status is classified as inactive. Reinstatement to active enrollment may only be effected by satisfying the continuing education requirements of the enrollment cycle immediately preceding the application for renewal of enrollment.

10. Some comments have suggested that the regulations identify qualifying sponsors as including the programs of the American Bar Association, American Institute of Certified Public Accountants, National Society of Public Accountants, National Association of Enrolled Agents and their respective affiliated state organizations. Considerable attention has been given this recommendation. We believe the recognition of courses offered or approved by bona fide professional organizations having viable continuing education programs in the areas contemplated by the regulations is a desirable goal. In order to achieve this goal, the final rule provides for the recognition of such courses as being acceptable. In order to be so recognized, it will be necessary for a professional organization each enrollment cycle to seek approval by the Director of Practice for this purpose. A list of approved professional organizations will be published in order that the enrolled agent community is made aware of the organizations having programs available to them. In this manner, not only is there the availability of the four organizations and their state affiliates referred to above to be recognized, but there will be flexibility for recognizing other organizations having viable programs. For example, the International Foundation of Employee Benefits has advised us of its educational programs. It should be considered for inclusion with those organizations having courses acceptable for meeting the requirements of the regulations.

11. Concern has been expressed that the proposed renewal of enrollment requirement is inconsistent with enrollment previously granted, enrollment which was considered permanent. The commenters believe that the requirement for continuing professional education should not apply to those individuals currently enrolled to practice before the Internal Revenue Service; rather, it should be prospective in nature. The proposed rule does not change the permanent nature of enrollment. Active enrollment to practice before the Internal Revenue Service will continue to remain permanent so long as renewal of enrollment is effected. As noted previously, continuing professional education must be applicable to all who are enrolled to practice before the Internal Revenue Service. An exception for those who are already enrolled would be at variance with the purposes of the proposal.

12. Comments received have questioned the relevance of allowing courses in business computer science and financial management. We believe the business community has acknowledged that we are now engaged in an information management society. The growth in the use of computers to process information has been immense in recent years. There has been a rapid rise in the use of computers by all facets of business for the recording and reporting of financial information. This includes tax records and the preparation of tax returns. The Internal Revenue Service is now embarking on a test project involving the electronic filing of tax returns. Consequently, we believe the allowance of continuing education credit for courses in business computer science and financial management to be appropriate and necessary in today's environment.

13. Comments received concern the number of hours of credit allowed for serving as an instructor, discussion leader or speaker. It is felt that the 25% maximum credit contemplated in the proposal is arbitrary and unnecessarily low. Based on our consideration of the comments and further evaluation of the subject, we have determined that expanding the maximum credit for instruction and preparation of 50% of the continuing education requirement for an enrollment cycle to be appropriate.

14. The final rule also makes some changes not addressed in the comments. They include the following. (a) The final rule clarifies the fact that failure to renew enrollment or a request to be placed in an inactive retirement status is not available to an individual who is the subject of a discipline matter. (b) The final rule eliminates the requirement for documentation of continuing professional education at the time an application for renewal of enrollment is made. Instead, the necessary records must be retained and furnished the Director of Practice upon request consistent with the verification program provided for in the final rule. (c) A number of changes of a stylistic or clarifying nature have been made.

SPECIAL ANALYSIS

This rule relates solely to professional services in connection with Internal Revenue Service and Treasury Department proceedings and is not expected to have any significant economic consequences. Therefore, it has been determined that this rule is not a major rule as defined in Executive Order 12291 and a regulatory impact analysis is not required. It is hereby certified that this rule is not expected to have a significant economic impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not required.

PAPERWORK REDUCTION ACT

The collection of information requirements contained in this proposed rule have been approved by the Office of Management and Budget pursuant to the Paperwork Reduction Act of 1980 (44 U.S.C. 3504(h)) under Control No. 1545-0946.

DRAFTING INFORMATION

The author of these regulations is Mr. Leslie S. Shapiro, Director of Practice, Department of the Treasury. Other personnel in the Treasury Department participated in the development of the regulations, both as to substance and style.

LIST OF SUBJECTS IN 31 CFR PART 10

Administrative rules and procedures, Lawyers, Accountants, Enrolled

Agents, Enrolled Actuaries, Appraisers.

Authority: These rules are issued under authority of Sec. 3, 23 Stat. 258, secs. 2.12, 60 Stat. 237 et seq.; 5 U.S.C. 301; 31 U.S.C. 330; 31 U.S.C. 321.

AMENDMENTS TO REGULATIONS

PART 10—[AMENDED]

Accordingly, 31 CFR Part 10 is amended as follows:

1. The authority for Part 10 continues to read as follows:

Authority: Sec. 3, 23 Stat. 258, secs. 2-12, 60 Stat. 237 et seq.; 5 U.S.C. 301; 31 U.S.C. 330; 31 U.S.C. 321.

§10.1 [Amended]

2. In section 10.1, paragraph (b) is revised to read as follows:

* * * * *

(b) *Duties*. The Director of Practice shall act upon applications for enrollment to practice before the Internal Revenue Service; institute and provide for the conduct of disciplinary proceedings relating to attorneys, certified public accountants, enrolled agents, enrolled actuaries and appraisers; make inquiries with respect to matters under his jurisdiction; and perform such other duties as are necessary or appropriate to carry out his functions under this part or as are prescribed by the Secretary of the Treasury.

* * * * *

§§10.4, 10.5, and 10.7 [Amended]

3. In section 10.4; sections 10.5(a), (b), and (c); and §10.7; in each place where it appears, the word "Commissioner" is removed and the words "Director of Practice" inserted.

4. In §10.5 paragraph (d) is revised to read as follows:

§10.5 Application for enrollment.

* * * * *

(d) *Appeal from denial of application*. The Director of Practice, in denying an application for enrollment, shall inform the applicant as to the reason(s) therefor. The applicant may, within 30 days after receipt of the notice of denial, file a written appeal therefrom, together with his/her reasons in support thereof, to the Secretary of the Treasury. A decision on the appeal will be rendered by the Secretary of the Treasury as soon as practicable.

5. Section 10.6 is revised to read as follows:

§10.6 Enrollment.

(a) *Roster*. The Director of Practice shall maintain rosters of all individuals:

(1) Who have been granted active enrollment to practice before the Internal Revenue Service;

(2) Whose enrollment has been placed in an inactive status for failure to meet the requirements for renewal of enrollment;

(3) Whose enrollment has been placed in an inactive retirement status;

(4) Who have been disbarred or suspended from practice before the Internal Revenue Service;

(5) Whose offer of consent to resignation from enrollment to practice before the Internal Revenue Service has been accepted by the Director of Practice under section 10.55 of this part; and

(6) Whose application for enrollment has been denied.

(b) *Enrollment card*. The Director of Practice will issue an enrollment card to each individual whose application for enrollment to practice before the Internal Revenue Service is approved after the effective date of this regulation. Each such enrollment card will be valid for the period stated thereon. Enrollment cards issued individuals before February 1, 1987 shall become invalid after March 31, 1987. An individual having an invalid enrollment card is not eligible to practice before the Internal Revenue Service.

(c) *Term of enrollment*. Active enrollment to practice before the Internal Revenue Service is accorded each individual enrolled, so long as renewal of enrollment is effected as provided in this part.

(d) *Renewal of enrollment*. To maintain active enrollment to practice before the Internal Revenue Service, each individual enrolled is required to have his/her enrollment renewed as set forth herein. Failure by an individual to receive notification from the Director of Practice of the renewal requirement will not be justification for circumvention of such requirement.

(1) All individuals enrolled to practice before the Internal Revenue Service before November 1, 1986 shall apply for renewal of enrollment during the period between November 1, 1986 and January 31, 1987. Those who receive initial enrollment between November 1, 1986 and January 31, 1987 shall apply for renewal of enrollment by March 1, 1987. The first effective date of renewal will be April 1, 1987.

(2) Thereafter, applications for renewal will be required between November 1, 1989 and January 31, 1990, and between November 1 and January 31 of every third year subsequent thereto. Those who receive initial enrollment during the renewal application period shall apply for renewal of enrollment by March 1 of the renewal year. The effective date of renewed enrollment will be April 1, 1990, and April 1 of every third year subsequent thereto.

(3) The Director of Practice will notify the individual of renewal of enrollment and will issue a card evidencing such renewal.

(4) A reasonable nonrefundable fee may be charged for each application for renewal of enrollment filed with the Director of Practice.

(5) Forms required for renewal may be obtained from the Director of Practice, Internal Revenue Service, Washington, DC 20224.

(e) *Condition for renewal: Continuing Professional Education*. In order to qualify for renewal of enrollment, an individual enrolled to practice before the Internal Revenue Service must certify, on the application for renewal form prescribed by the Director of Practice, that he/she has satisfied the following continuing professional education requirements.

(1) *For renewed enrollment effective April 1, 1987.*

(i) A minimum of 24 hours of continuing education credit must be completed between January 1, 1986 and January 31, 1987.

(ii) An individual who receives initial enrollment between January 1, 1986 and January 31, 1987 is exempt from the continuing education requirement for the renewal of enrollment effective April 1, 1987, but is required to file a timely application for renewal of enrollment.

(2) *For renewed enrollment effective April 1, 1990 and every third year thereafter.*

(i) A minimum of 72 hours of continuing education credit must be completed between February 1, 1987 and January 31, 1990, and during each three year period subsequent thereto. Each such three year period is known as an enrollment cycle.

(ii) A minimum of 16 hours of continuing education credit must be completed in each year of an enrollment cycle.

(iii) An individual who receives initial enrollment during an enrollment cycle must complete two (2) hours of qualifying continuing education credit for each month enrolled during such enrollment cycle. Enrollment for any part of a month is considered enrollment for the entire month.

(f) *Qualifying continuing education.*

(1) *In General.* To qualify for continuing education credit, a course of learning must:

(i) Be a qualifying program designed to enhance the professional knowledge of an individual in Federal taxation or Federal tax related matters, i.e. programs comprised of current subject matter in Federal taxation or Federal tax related matters to include accounting, financial management, business computer science and taxation; and

(ii) Be conducted by a qualifying sponsor.

(2) *Qualifying Programs.*

(i) *Formal programs.* Formal programs qualify as continuing education programs if they:

(A) Require attendance;

(B) Require that the program be conducted by a qualified instructor, discussion leader or speaker, i.e. a person whose background, training, education and/or experience is appropriate for instructing or leading a discussion on the subject matter of the particular program; and

(C) Require a written outline and/or textbook and certificate of attendance provided by the sponsor, all of which must be retained by the attendee for a three year period following renewal of enrollment.

(ii) *Correspondence or individual study programs (including taped programs).* Qualifying continuing education programs include correspondence or individual study programs completed on an individual basis by the enrolled individual and conducted by qualifying sponsors. The allowable credit hours for such programs will be measured on a basis comparable to the measurement of a seminar or course for credit in an accredited educational institution. Such programs qualify as continuing education programs if they:

(A) Require registration of the participants by the sponsor;

(B) Provide a means for measuring completion by the participants (e.g., written examination); and

(C) Require a written outline and/or textbook and certificate of completion provided by the sponsor which must be retained by the participant for a three year period following renewal of enrollment.

(iii) *Serving as an instructor, discussion leader or speaker.*

(A) One hour of continuing education credit will be awarded for each contact hour completed as an instructor, discussion leader or speaker at an educational program which meets the continuing education requirements of this part.

(B) Two hours of continuing education credit will be awarded for actual subject preparation time for each contact hour completed as an instructor, discussion leader or speaker at such programs. It will be the responsibility of the individual claiming such credit to maintain records to verify preparation time.

(C) The maximum credit for instruction and preparation may not exceed 50% of the continuing education requirement for an enrollment cycle.

(D) Presentation of the same subject matter in an instructor, discussion leader or speaker capacity more than one time during an enrollment cycle will not qualify for continuing education credit.

(iv) *Credit for published articles, books, etc.*

(A) Continuing education credit will be awarded for publications on Federal taxation or Federal tax related matters to include accounting, financial management, business computer science, and taxation, provided the content of such publications is current and designed for the enhancement of the professional knowledge of an individual enrolled to practice before the Internal Revenue Service.

(B) The credit allowed will be on the basis of one hour credit for each hour of preparation time for the material. It will be the responsibility of the person claiming the credit to maintain records to verify preparation time.

(C) The maximum credit for publications may not exceed 25% of the continuing education requirement of any enrollment cycle.

(3) *Periodic examination.* Individuals may establish eligibility for renewal of enrollment for any enrollment cycle by:

(i) Achieving a passing score on each part of the Special Enrollment Examination administered under this part during the three year period prior to renewal; and

(ii) Completing a minimum of 16 hours of qualifying continuing education during the last year of an enrollment cycle.

(g) *Sponsors.* (1) Sponsors are those responsible for presenting programs.

(2) To qualify as a sponsor, a program presenter must:

(i) Be an accredited educational institution;

(ii) Be recognized for continuing education purposes by the licensing body of any State, possession, territory, Commonwealth, or the District of Columbia responsible for the issuance of a license in the field of accounting or law;

(iii) Be recognized by the Director of Practice as a professional organization or society whose programs include offering continuing professional education opportunities in subject matter within the scope of this part; or

(iv) File a sponsor agreement with the Director of Practice to obtain approval of the program as a qualified continuing education program.

(3) A qualifying sponsor must ensure the program complies with the following requirements:

(i) Programs must be developed by individual(s) qualified in the subject matter;

(ii) Program subject matter must be current;

(iii) Instructors, discussion leaders, and speakers must be qualified with respect to program content;

(iv) Programs must include some means for evaluation of technical content and presentations;

(v) Certificates of completion must be provided those who have successfully completed the program; and

(vi) Records must be maintained by the sponsor to verify completion of the program and attendance by each participant. Such records must be retained for a period of three years following completion of the program. In the case of continuous conferences, conventions, and the like, records must be maintained to verify completion of the program and attendance by each participant at each segment of the program.

(4) Professional organizations or societies wishing to be considered as qualified sponsors shall request such status of the Director of Practice and furnish information in support of the request together with any further information deemed necessary by the Director of Practice.

(5) Sponsor agreements and qualified professional organization or society sponsors approved by the Director of Practice shall remain in effect for one enrollment cycle. The names of such sponsors will be published on a periodic basis.

(h) *Measurement of continuing education coursework.*

(1) All continuing education programs will be measured in terms of contact hours. The shortest recognized program will be one contact hour.

(2) A contact hour is 50 minutes of continuous participation in a program. Credit is granted only for a full contact hour, i.e. 50 minutes or multiples thereof. For example, a program lasting more than 50 minutes but less than 100 minutes will count as one contact hour.

(3) Individual segments at continuous conferences, conventions and the like will be considered one total program. For example, two 90-minute segments (180 minutes) at a continuous conference will count as three contact hours.

(4) For university or college courses, each semester hour credit will equal 15 contact hours and a quarter hour credit will equal 10 contact hours.

(i) *Recordkeeping requirements.*

(1) Each individual applying for renewal shall retain for a period of three years following the date of renewal of enrollment the information required with regard to qualifying continuing professional education credit hours. Such information shall include:

(i) The name of the sponsoring organization;

(ii) The location of the program;

(iii) The title of the program and description of its content e.g., course syllibi and/or textbook;

(iv) The dates attended;

(v) The credit hours claimed;

(vi) The name(s) of the instructor(s), discussion leader(s), or speaker(s), if appropriate; and

(vii) The certificate of completion and/or signed statement of the hours of attendance obtained from the sponsor.

(2) To receive continuing education credit for service completed as an instructor, discussion leader, or speaker, the following information must be maintained for a period of three years following the date of renewal of enrollment:

(i) The name of the sponsoring organization;

(ii) The location of the program;

(iii) The title of the program and description of its content;

(iv) The dates of the program; and

(v) The credit hours claimed.

(3) To receive continuing education credit for publications, the following information must be maintained for a period of three years following the date of renewal of enrollment:

(i) The publisher;

(ii) The title of the publication;

(iii) A copy of the publication; and

(iv) The date of publication.

(j) *Waivers.* (1) Waiver from the continuing education requirements for a given period may be granted by the Director of Practice for the following reasons:

(i) Health, which prevented compliance with the continuing education requirements;

(ii) Extended active military duty;

(iii) Absence from the United States for an extended period of time due to employment or other reasons, provided the individual does not practice before the Internal Revenue Service during such absence; and

(iv) Other compelling reasons which will be considered on a case-by-case basis.

(2) A request for waiver must be accompanied by appropriate documentation. The individual will be required to furnish any additional documentation or explanation deemed necessary by the Director of Practice. Examples of appropriate documentation could be a medical certificate, military orders, etc.

(3) A request for waiver must be filed no later than the last day of the renewal application period.

(4) If a request for waiver is not approved, the individual will be so notified by the Director of Practice and placed on a roster of inactive enrolled individuals.

(5) If a request for waiver is approved, the individual will be so notified and issued a card evidencing such renewal.

(6) Those who are granted waivers are required to file timely applications for renewal of enrollment.

(k) *Failure to comply.* (1) Compliance by an individual with the requirements of this part shall be determined by the Director of Practice. An individual who fails to meet the requirements of eligibility for renewal of enrollment will be notified by the Director of Practice at his/her last known address by first class mail. The notice will state the basis for the noncompliance and will provide the individual an opportunity to furnish in writing information relating to the matter within 60 days of the date of the notice. Such information will be considered by the Director of Practice in making a final determination as to eligibility for renewal of enrollment.

(2) The Director of Practice may require any individual, by first class mail to his/her last known mailing address, to provide copies of any records required to be maintained under this part. The Director of Practice may disallow any continuing professional education hours claimed if the individual concerned fails to comply with such requirement.

(3) An individual who has not filed a timely application for renewal of enrollment, who has not made a timely response to the notice of noncompliance with the renewal requirements, or who has not satisfied the requirements of eligibility for renewal will be placed on a roster of inactive enrolled individuals for a period of three years. During this time, the individual will be ineligible to practice before the Internal Revenue Service.

(4) During inactive enrollment status or at any other time an individual is ineligible to practice before the Internal Revenue Service, such individual shall not in any manner, directly or indirectly, indicate he or she is enrolled to practice before the Internal Revenue Service, or use the term "enrolled agent," the designation "E.A.," or other form of reference to eligibility to

practice before the Internal Revenue Service.

(5) An individual placed in an inactive status may satisfy the requirements for renewal of enrollment during his/her period of inactive enrollment. If such satisfaction includes completing the continuing education requirement, a minimum of 16 hours of qualifying continuing education hours must be completed in the 12 month period preceding the date on which the renewal application is filed. Continuing education credit under this subsection may not be used to satisfy the requirements of the enrollment cycle in which the individual has been placed back on the active roster.

(6) An individual placed in an inactive status must file an application for renewal of enrollment and satisfy the requirements for renewal as set forth in this section within three years of being placed in an inactive status. The name of such individual otherwise will be removed from the inactive enrollment roster and his/her enrollment will terminate. Eligibility for enrollment must then be reestablished by the individual as provided in this part.

(7) Inactive enrollment status is not available to an individual who is the subject of a discipline matter in the Office of Director of Practice.

(l) *Inactive retirement status.* An individual who no longer practices before the Internal Revenue Service may request being placed in an inactive status at any time and such individual will be placed in an inactive retirement status. The individual will be ineligible to practice before the Internal Revenue Service. Such individual must file a timely application for renewal of enrollment at each applicable renewal or enrollment as provided in this part. An individual who is placed in an inactive retirement status may be reinstated to an active enrollment status upon filing an application for renewal of enrollment and providing evidence of the completion of the required continuing professional education hours for the enrollment cycle. Inactive retirement status is not available to an individual who is the subject to a discipline matter in the Office of Director of Practice.

(m) *Renewal while under suspension or disbarment.* An individual who is ineligible to practice before the Internal Revenue Service by virtue of disciplinary action is required to meet the requirements for renewal of enrollment during the period of ineligibility.

(n) *Verification.* The Director of Practice may review the continuing education records of an enrolled individual and/or qualified sponsor in a manner deemed appropriate to determine compliance with the requirements and standards for renewal of enrollment as provided in this part. (Approved by the Office of Management and Budget under Control No. 1545-0946).

6. Section 10.99 is revised to read as follows:

§10.99 Effective date of regulations.

The regulations of this part shall become effective on January 22, 1986 and shall supersede all prior regulations related to this part.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Qualified Possession Source Investment Income

LR-106-77

SUMMARY: This document contains proposed regulations defining the term "qualified possession source investment income" for purposes of the Puerto Rico and possession tax credit enacted by the Tax Reform Act of 1976 [Pub. L. 94-455, 1976-3 C.B. (Vol. 1) 1].

DATES: Written comments and requests for a public hearing must be delivered or mailed by March 24, 1986. The regulations are proposed to apply generally to taxable years beginning after December 31, 1975.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-106-77), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Jacob Feldman of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T, 202-566-3289, not a toll-free call.

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 936 of the Internal Revenue Code of 1954, and deletes Temporary Regulations (26 CFR Part 7) under section 936. Section 936 was added to the Code by section 1051(b) of the Tax Reform Act of 1976 [Pub. L. 94-455, 1976-3 C.B. (Vol. 1) 1, 119] and was amended by section 701(u)(11) of the Revenue Act of 1978 [Pub. L. 95-600, 1978-3 C.B. (Vol. 1) 1, 151].

EXPLANATION OF PROVISIONS

A domestic corporation that elects the application of section 936 may qualify for the Puerto Rico and possession tax credit. This credit is equal to the Federal income tax attributable to *inter alia* the corporation's qualified possession source investment income. Section 936(d)(2) defines qualified possession source investment income as gross income (less the properly apportioned or allocated deductions) that is—

(1) From sources within a possession of the United States in which a trade or business is actively conducted;

(2) Attributable to investment in that possession (for use therein); and

(3) Attributable to the investment of funds initially derived from the active conduct of a trade or business in that possession or from such investment.

Source of Income

Proposed §1.936-2(a) provides that generally the source of income for purposes of section 936 is to be determined in accordance with §1.863-6. Special rules are provided for determining the source of certain interest and dividends (proposed §1.936-2(b)).

Investment in a Possession (for use therein)

Proposed §1.936-3 takes the position that interest and certain dividends derived by a U.S. corporation which conducts an active trade or business in Puerto Rico will be treated as attributable to investment in Puerto Rico (for use therein) as required under section 936(d)(2) if the interest or certain dividends qualify for exemption from Puerto Rican income tax. To qualify for exemption from Puerto Rican income tax, a taxpayer must satisfy criteria in the Puerto Rican income tax statute and regulations thereunder that the funds invested are in fact used in Puerto Rico. This is the position taken in temporary regulation §7.936-1. The present proposed regulations, however, reflect the updating of the Puerto Rican regulations on April 17, 1984. In addition, for investments made by the U.S. corporation more than 30 days after publication of the regulation by Treasury decision, the U.S. corporation must obtain at the time it makes the investment the written agreement of the institution receiving the funds that the investment of the funds by the institution will qualify for the exemption under Puerto Rican regulations.

Reliance on the Puerto Rico regulatory system for satisfaction of this requirement is based on the rules in existence as a result of the April 17, 1984, amendments. Changes in those rules, or in the method of operation of the Puerto Rico government's regulatory or investment authority, may require the development and application of a separate set of rules for determining when investment income is attributable to investment in Puerto Rico (for use therein).

Proposed §1.936-3 deals only with the application of section 936(d)(2) to investment in Puerto Rico. The credit provided by section 936 is also available with respect to certain investment income derived from other possessions of the United States (not including the Virgin Islands), if such income is attributable to investment of funds in the possession "for use therein" and if the other requirements of section 936(d)(2) are met.

Initially Derived from a Possession

Proposed §1.936-3A takes the position that funds are treated as initially derived from a possession if such funds represent an investment of taxable income from sources without the United States derived from the active conduct of a trade or business in a possession or a reinvestment of qualified possession source investment income. Such funds are treated as qualified funds and the amount which may be invested is determined on an annual basis. Losses as well as distributions with respect to these funds will reduce the amount of qualified funds. Therefore, an investment which is treated as made from qualified funds in one year might no longer qualify if a loss or a distribution of income reduces the amount of qualified funds. The proposed regulation also takes the position that an investment of funds derived from a capital contribution does not qualify.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

Although this document is a notice of proposed rulemaking which solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this proposed rule is not subject to Executive Order 12291, and, accordingly, a regulatory impact analysis is not required.

DRAFTING INFORMATION

The principal author of these proposed regulations is Jacob Feldman of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulation, both on matters of substance and style.

* * * * *

Proposed Amendments to the Regulations

The proposed amendments to 26 CFR Parts 1 and 7 are as follows:

INCOME TAX REGULATIONS

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * * Section 1.936-2, 1.936-3, and 1.936-3A also issued under 26 U.S.C. 936(d)(2). * * *

Par. 2. New §1.936-2, 1.936-3 and 1.936-3A are added after §1.936-1 to read as follows:

§1.936-2 Source of income.

(a) *In general.* Except as provided in §1.936-2(b) (relating to certain interest), for purposes of section 936(d)(2), the determination as to whether gross income is from sources within a particular possession shall be made in accordance with §1.863-6.

(b) *Certain interest.* (1) Interest paid by a possessions corporation that meets the condition of section 936(a)(2)(A) with respect to a particular possession is from sources within that possession.

(2) Interest paid or credit on deposit accounts with a possession branch of a corporation or partnership is from sources within the possession if, at the time of payment or crediting, the branch is engaged within the possession in the commercial banking business or the business of a savings and loan or similar association.

§1.936-3 Investment in a possession (for use therein).

For purposes of section 936(d)(2), interest and certain dividends derived after April 17, 1984 (less deductions allocable and apportionable thereto) by a domestic corporation engaged in the active conduct of a trade or business in Puerto Rico shall be treated as attributable to investment in Puerto Rico (for use therein) if the interest or certain dividends qualify for exemption from Puerto Rican Income Tax under regulations issued by the Secretary of the Treasury of Puerto Rico, as in effect on April 17, 1984 under the authority of the Acts No. 6 of December 15, 1953, 57 of June 13, 1963, and 25 of June 2, 1978, as amended, to determine the institutions which are eligible to receive funds from exempted businesses under those Acts. In the case of any investment of funds made by the possessions corporation after [Date that is 30 days after the date of publication in the Federal Register of this regulation as a Treasury decision], the preceding sentence shall not apply unless the possessions corporation receives, at the time the funds are delivered for investment, the written agreement of the institution receiving the funds that the funds will be invested by the institution so as to qualify for exemption under the foregoing regulations of Puerto Rico. Interest derived after September 30, 1976 and before April 18, 1984 shall be treated as attributable to investment in Puerto Rico (for use therein) if the interest qualifies for exemption from Puerto Rican Income Tax under regulations issued by the Secretary of the Treasury of Puerto Rico as in effect on September 28, 1976 under the authority of section 2(j) of the Puerto Rico Industrial Incentive Act of 1963, as amended.

§1.936-3A Funds derived from a possession.

(a) *In general.* Funds treated as derived from the active conduct of a trade or business in a possession or from investment of such funds in a possession ("qualified funds") include—

(1) Taxable income from sources without the United States derived from the active conduct of a trade or business in the possession, and

(2) Qualified possession source investment income,

reduced by any distributions paid with respect to such income and by any losses (not otherwise taken into account under subparagraph (1) or (2)) from such activity or investment. The amount of any capital contributions to a possessions corporation is not treated as qualified funds.

(b) *Limitation on investment.* Notwithstanding paragraph (a), the amount of qualified funds which may be invested in a possession and give rise to income which is treated as qualified possession source investment income is limited to the total qualified funds for the taxable year and for all prior taxable years which are not already invested in a possession. For this purpose, qualified possession source investment income is not included in total qualified funds for the current taxable year, but is included with respect to prior taxable years.

(c) *Illustration:* The principles of paragraphs (a) and (b) of this section are illustrated by the following example:

Example: X has operated in Puerto Rico as a section 936 corporation since January 1, 1980. In 1980 X earned $30,000 from the active conduct of a business in Puerto Rico and paid a dividend of $20,000. On January 1, 1981 X invested $20,000 in a Puerto Rican financial institution. For the year 1981 X had a loss of $10,000 from the conduct of its business and received $1500 in interest. For the years 1982 and 1983 X earned $40,000 and $60,000 respectively from its business and $2,000 each year from its investments which qualify under §1.936-3 and paid dividends of $20,000 and $30,000 respectively. On January 1, 1984 X deposited $80,000 in the same Puerto Rican financial institution for a total deposit of $100,000. For 1984 X had a $5,000 loss from its business, but received $15,000 of interest form its investments.

For 1981, the interest received from the investment in the Puerto Rican financial institution was not qualified possession source investment income since there were no qualified funds for 1981. The $30,000 of income received by X from the active conduct of its business in 1980 was reduced to zero by a $20,000 dividend in 1980 and a $10,000 loss in 1981.

For 1982 and 1983 the $20,000 originally deposited in 1981 and not withdrawn are treated as qualified funds and all of the income derived therefrom as qualified possession source investment income assuming the requirements of §§1.936-2 and 1.936-3 are met. The zero qualified funds at the end of 1981 were increased to $20,000 in 1982, representing $40,000 of active business income less $20,000 of dividends; in 1983, the qualified funds available for investment were further increased to $52,000, representing $60,000 of active business income in 1983 less dividend payment of $30,000 (or $30,000) plus $2,000 of qualified possession source investment income accrued in 1982). The $1500 of interest earned in 1981 was not derived from qualified funds and, therefore, was not qualified possession source investment income. In addition, this amount and any amount of interest derived therefrom can never be qualified funds since the $1500 was neither derived initially from the active conduct of a trade or business in Puerto Rico nor was it qualified possession source investment income.

For 1984, $7350 of the $15,000 of interest received on the $100,000 investment constitutes qualified possession source investment income since only $49,000 of the $100,000 deposited was from qualified funds ($52,000 of qualified funds at the end of 1983 reduced by the $5000 of loss incurred in 1984 and increased by the $2,000 of qualified possession source investment income accrued in 1983).

TEMPORARY INCOME TAX REGULATIONS UNDER THE TAX REFORM ACT OF 1976

Par. 3 The authority for Part 7 continues to read as follows:

Authority: 26 U.S.C. 7805

Par. 4. Section 7.936-1 is removed.

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on January 17, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 21, 1986, 51 F.R. 2726)

Notice of Proposed Rulemaking

Section 338(h)(10) Election and Extension of Time to Make Certain Elections

LR-218-83

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary regulations that add new §§1.338(h)(10)-1T and 1.1502-75T, relating to elections under section 338(h)(10), and that amend existing temporary regulations §§1.338-1T and 1.338-4T, relating generally to procedural and miscellaneous matters under section 338. The text of the new and revised sections also serves as the comment document for this notice of proposed rulemaking.

DATES:

PROPOSED EFFECTIVE DATE

The regulations under section 338(h)(10) are proposed to generally apply to stock acquisitions made after January 12, 1983. The temporary regulations being amended generally apply to stock acquisitions made after August 31, 1982.

DATE FOR COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Written comments and requests for a public hearing must be delivered or mailed by March 10, 1986.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T [LR-218-83], Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Patricia Wendlandt or Bennett C. Steinhauer of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3458, not a toll-free call).

SUPPLEMENTARY INFORMATION

BACKGROUND

Temporary regulations published in the Rules and Regulations portion of this issue of the FEDERAL REGISTER add new temporary regulations §§1.338(h)(10)-1T and 1.1502-75T to Part 1 of Title 26 of the Code of Federal Regulations ("CFR") and amend temporary regulations §§1.338-1T and 1.338-4T. Section 1.338-1T was published as T.D. 7942 in the FEDERAL REGISTER on February 8, 1984 (49 FR 4722) [1984-1 C.B. 93], was amended and redesignated (as §1.338-1T) by temporary regulations published as T.D. 7975 in the FEDERAL REGISTER on September 6, 1984 (49 FR 35086) [1984-2 C.B. 81], and was further amended by T.D. 8021 in the FEDERAL REGISTER on April 25, 1985 (50 FR 16428) [1985-1 C.B. 96]. Section 1.338-4T was also published in T.D. 8021. The final regulations that are proposed to be based on the new and amended temporary regulations would be added to Part 1 of Title 265 of the CFR. Those final regulations would provide guidance on elections under section 338(h)(10) of the Code as well as on the date for electing section 338, for making certain other elections under section 338, and for certain other purposes. Section 338 of the Code was added by section 224 of TEFRA (Pub. L. No. 97-248; 96 Stat. 485) [1982-2 C.B. 462, 501] and was amended by section 306(a)(8) of the Technical Corrections Act (Pub. L. No. 97-448; 96 Stat. 2402) [1983-1 C.B. 451, 470] and section 712(k) of the Tax Reform Act of 1984 (Pub. L. No. 98-369; 98 Stat. 946) [1984-3 C.B. (Vol. 1) 1, 456]. For the text of the new and amended temporary regulations, see T.D. 8068, published * * * [on page 9, this Bulletin]. The preamble to the temporary regulations explains the additions to the regulations.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required.

COMMENTS AND REQUEST FOR A PUBLIC HEARING

Before these proposed regulations are adopted, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER. The collection of information requirements contained herein have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on the requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service. New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests persons submitting comments to OMB to also send copies of the comments to the Service.

DRAFTING INFORMATION

The principal author of these proposed regulations is Bennett C. Steinhauer of the Legislation and Regulations Division off the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on January 3, 1986, 12:46 p.m., and published in the issue of the Federal Register for January 8, 1986, 51 F.R. 763)

Correction to Publication 583

Announcement 86-21

Publication 583, *Information for Business Taxpayers* (Revised November 1985), contains an incorrect dollar amount and an incorrect line reference in the last paragraph of the first column of page 6. The corrections are as follows:

line 7 should be Line 9
$7,368 should be $7.433

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Philip G. Arneson	Sparta, WI	Attorney	Indefinite from December 15, 1985
Joseph P. Day	Woburn, MA	Attorney	Indefinite from December 24, 1985
Kenneth H. Dillard	Nashville, TN	Certified Public Accountant	Indefinite from December 31, 1985
LeRoy Hodge	Hamilton, NY	Attorney	Indefinite from December 10, 1985
Frank S. Lukuch	Barberton, OH	Certified Public Accountant	Indefinite from December 4, 1985
W. Stephen McConnell	Tampa, FL	Certified Public Accountant	Indefinite from December 26, 1985
Nathan Rich	Wilmington, DE	Certified Public Accountant	Indefinite from December 1, 1985
Walter E. Shettlemore	Long Beach, MS	Certified Public Accountant	Indefinite from December 20, 1985

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.451-3, amended.	Accounting for long-term contracts	1986-6 I.R.B. 55	Mar. 7, 1986
26 CFR 31.3508-1, 31.3509-1, 1.6041A-1, added.	Treatment of real estate agents and direct sellers; determination of employer liability for certain employment taxes	1986-6 I.R.B. 46	Mar. 10, 1986
26 CFR 1.6041-3, amended.	Information reporting of allowances or reimbursements for travel expenses of public employees	1986-7 I.R.B. 26	Mar. 10, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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The contents of the weekly Bulletin are consolidated semiannually into a permanent, indexed, Cumulative Bulletin. These are sold on a single copy basis and *are not* included as part of the subscription to the Internal Revenue Bulletin. Subscribers to the weekly Bulletin are notified when copies of the Cumulative Bulletin are available. Certain issues of Cumulative Bulletins are out of print and are not available. Persons desiring available Cumulative Bulletins, which are listed on the reverse, may purchase them from the Superintendent of Documents.

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These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-31, page 4.

Prizes and awards; NASA awards. The Service will not follow the decision in *Jones v. Commissioner*, 743 F.2d 1429 (9th Cir. 1984) relating to the taxability of NASA awards, but will continue to follow the decision in *Rogallo v. United States*, 475 F.2d (4th Cir. 1973) and Rev. Rul. 69-129, 1969-1 C.B. 35.

Rev. Rul. 86-32, page 16.

Trusts; reversionary interest; determination of life expectancy. Actuarial tables are adopted for determining life expectancy for purposes of section 673 of the Code for transfers to a trust occurring after November 30, 1983.

Rev. Rul. 86-33, page 17.

Controlled foreign corporations; Subpart F income; dividend distribution within same chain of foreign corporations. For purposes of calculating the limitation on subpart F income under section 952(c) of the Code, a controlled foreign corporation (CFC) that receives a dividend distribution from another CFC within the same chain of ownership is required to increase its earnings and profits for the tax year by the amount of the distribution.

Rev. Rul. 86-34, page 20.

Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for March 1986.

T.D. 8069, page 4.

Amendments to the regulations under sections 167, 170, 2055, and 2522 of the Code relate to contributions not in trust of partial interests in property for conservation purposes.

LR-198-82, page 30.

Proposed amendments to the regulations under section 6031 of the Code relate to partnership returns.

EMPLOYEE PLANS

Notice 86-3, page 21.

The Service has established guidelines for granting partial relief from the sanctions for failure to satisfy the requirements of section 401(a) of the Code in the case of certain employee plans that were not timely amended to comply with the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), the Tax Reform Act of 1984 (TRA), or the Retirement Equity Act of 1984 (REA).

EE-95-84, page 25.

Proposed amendments to the regulations under sections 401 and 411 of the Code relate to certain restrictions on an employee's right to receive alternative forms of benefit under qualified plans.

ESTATE & GIFT TAXES

T.D. 8069, page 4.

Amendments to the regulations under sections 167, 170, 2055, 2522 of the Code relate to contributions not in trust of partial interests in property for conservation purposes.

ADMINISTRATIVE

Rev. Proc. 86-12, page 21.

Rulings; partnership issues. Guidance is provided for taxpayers requesting rulings concerning certain partnership issues on which the Service has previously declined to rule. Rev. Proc. 86-1 modified.

Announcement 86-22, page 34.

Guidance is provided concerning information reporting rules under sections 1275 and 6049 of the Code for issuers of publicity offered original issue discount (OID) debt instruments and for brokers and other middlemen who hold interest in those debt instruments as nominees.

Announcement 86-24, page 35.

Instructions for 1985 Form 2106, Employee Business Expenses, are incomplete for taxpayers who choose an alternative ACRS method for vehicles.

Announcement 86-25, page 35.

The 1985 Form 5695, Residential Energy Credit, contains an incorrect line reference.

Announcement 86-26, page 35.

The 1985 Schedule D (Form 1040) instructions under the heading "Investment Interest Deduction Adjustment" are incorrect.

Finding Lists begin on page 40.
Announcement of Suspensions begin on page 36.
Announcement of Notice of Proposed Rulemaking on page 38.
Index for January and February begins on page 42.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 74.—Prizes and Awards

26 CFR 1.74-1: Prizes and awards.

Prizes and awards; NASA awards. The Service will not follow the decision in *Jones v. Commissioner*, 743 F.2d 1429 (9th Cir. 1984) relating to the taxability of NASA awards, but will continue to follow the decision in *Rogallo v. United States*, 475 F.2d (4th Cir. 1973) and Rev. Rul. 69-129, 1969-1 C.B. 35.

Rev. Rul. 86-31

The Internal Revenue Service will not follow the decision in *Jones v. Commissioner*, 743 F.2d 1429 (9th Cir. 1984). That case concerned an award made to the taxpayer by the National Aeronautics and Space Act of 1958, 42 U.S.C. section 2458 (1982). The opinion held that the award was a prize or award excludable from gross income under section 74(b) of the Internal Revenue Code. Rather, the Service will continue to follow the analysis of the law published in Rev. Rul. 69-129, 1969-1 C.B. 35. Rev. Rul. 69-129 holds that awards made under 42 U.S.C. section 2458 are not made primarily in recognition of achievement within the meaning of section 74(b) of the Code, but are made to reward contributions to NASA by employees and others that advance the goals and interests of NASA. As such, these awards are includible in the gross incomes of the recipients. Rev. Rul. 69-129 was upheld in *Rogallo v. United States*, 475 F.2d 1 (4th Cir. 1973), and remains the position of the Service.

In addition, the Service will continue to follow section 1.74-1(b) of the Income Tax Regulations. That provision states that section 74(b) of the Code does not exclude from gross income prizes or awards from an employer to an employee in recognition of some achievement in connection with the employee's employment.

Section 170.—Charitable, Etc., Contributions and Gifts

26 CFR 1.170A-14: Qualified conservation contributions.
(Also Sections 2055, 2522; 20.2055-2, 25.2522(c)-3.)

T.D. 8069

TITLE 26—INTERNAL REVENUE.—CHAPTER 1 SUBCHAPTER A, SUBCHAPTER B, SUBCHAPTER H, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 20—ESTATE TAX; ESTATES OF DECEDENTS DYING AFTER AUGUST 16, 1954; PART 25—GIFT TAX; GIFTS MADE AFTER DECEMBER 31, 1954; PART 602—REPORTING AND RECORDKEEPING REQUIREMENTS

Qualified Conservation Contributions

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final Regulations.

SUMMARY: This document contains final regulations relating to contributions not in trust of partial interests in property for conservation purposes. Changes to the applicable law made by the Temporary Tax Provisions, Extension [Pub. L. 96-541, 1980-2 C.B. 596] and the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1] are reflected in this document. These regulations provide necessary guidance to the public for compliance with the law and affect donors and donees of qualified conservation contributions.

DATES: Except as otherwise provided in §1.170A-14(g)(4)(ii), the regulations are effective for contributions made on or after December 18, 1980.

FOR FURTHER INFORMATION CONTACT: Ada S. Rousso of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR.T), Telephone 202-566-3287 (not a toll free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

On May 23, 1983, the FEDERAL REGISTER (48 FR 22940) [LR-200-76, 1983-1 C.B. 910] published proposed amendments to the Income Tax Regulations (26 CFR Part 1) and Estate and Gift Tax Regulations (26 CFR Parts 20 and 25) under section 170(h), 2055 and 2522 of the Internal Revenue Code of 1954 (Code). The amendments were proposed to conform the regulations to section 6 of the Temporary Tax Provisions, Extension (P.L. 96-541, 96 Stat. 3206). [1980-2 C.B. 596, 598]. A public hearing was held on September 15, 1983. Subsequent to the hearing, section 170(h)(5) of the Code was amended by section 1035(a) of the Tax Reform Act of 1984 (P.L. 98-369, 98 Stat. 1042) [1984-3. C.B. (Vol. 1) 1, 550]. On December 10, 1984, the Service issued a news release (IR-84-125) reminding taxpayers claiming deductions for donations of conservation easements that such deductions are limited to the fair market value of the easement at the time of the contribution. The news release further indicated that if the donation of the easement does not decrease the value of the property on which the easement is granted, the fair market value of the easement, and thus, the deduction, is zero.

After consideration of all comments regarding the proposed amendments and of the revision made by the Tax Reform Act of 1984, those amendments are adopted as revised by this Treasury decision.

SUMMARY OF COMMENTS

Qualified Contribution of Entire Interest of Donor Other Than Qualified Mineral Interest

In response to many comments regarding the donation of an entire interest of the donor other than a qualified mineral interest, proposed §1.170A-14(b) has been revised to provide that section 170(h) will not disallow a deduction for a conservation contribution where the donor has previously transferred a portion of the entire interest unless the donor has purposefully reduced his interest before the contribution is made, for example, by transferring a portion to a related person in order to retain control of more than a qualified mineral interest.

Access

The final regulations have been revised to clarify the extent of public access required for each type of qualified conservation contribution under section 170(h). Thus, in order to qualify for a deduction under section 170(h), donations of property to preserve land areas for outdoor recreation by or for the education of the general public, for the preservation of a view, for the preservation of land pursuant to a governmental conservation policy, or for the preservation of historic structures or land areas must provide for either physical or visual access. Examples have been included to clarify the public access requirement in specific circumstances.

Inconsistent Use

Section 1.170A-14(e)(2) provides that a deduction will not be allowed if a contribution would accomplish one of the enumerated conservation purposes but would permit impairment of other enumerated conservation interests. However, inconsistent use of the property is permitted if that use is necessary for the protection of the conservation interests that are the subject of the contribution. Commenters felt that the proposed regulations were not specific enough regarding permitted inconsistent uses. Therefore, the final regulations have been revised to include examples of certain uses that are not prohibited if, under the circumstances, they do not impair significant conservation interests. See §1.170A-14(e)(2).

Third Party Mineral Rights

The proposed regulations provided that the interest in property that is retained by the donor (and the donor's successor in interest) must be subject to legally enforceable restrictions that will prevent uses of the retained interest inconsistent with the conservation purposes of the donation. In addition, there was a prohibition against any method of mining on property that is the subject of a gift that would be inconsistent with the conservation purposes of the donation. Furthermore, a contribution was disallowed if at any time there may be surface mining on the property.

Many comments were received requesting relief from this rule because in many areas of the country, the mineral rights are not and may never have been owned by the donor; thus the donor can not ensure that a third party owner of the mineral rights will not engage in surface mining on the property that is the subject of the gift.

Subsequent to publication of the proposed regulations, section 1035(a) of the Tax Reform Act of 1984 amended section 170(h)(5)(B) (relating to surface mining) to provide an exception to the general rule precluding a deduction for a conservation contribution if there is any likelihood of surface mining occurring at any time on the property to which the contribution relates. For conservation contributions made after July 18, 1984, the general rule with respect to surface mining will not apply to preclude a deduction if the surface estate and mineral interests were separated before June 13, 1976, remain so separated up to and including the time of the gift, and the probability of surface mining occurring on the property is so remote as to be negligible. Factors that may be considered in determining if the probability of surface mining is so remote as to be neglible are provided in the final regulations. In addition, the regulations provide that no deduction for a conservation contribution of the surface estate is permitted under this exception if the present owner is related to the owner of the surface estate at the time of the gift. Finally, these regulations clarify that any person may retain the mineral interest so long as the donor can guarantee observance of the restrictions to protect the conservation interests. See §1.170A-14(g)(4) and the example thereunder.

Preservation of Open Space

In general, the staute provides that a donation of real property to preserve open space for conservation purposes (including farmland and forestland) will qualify as a deductible contribution if either of two tests are met: (1) The preservation must be pursuant to a clearly delineated governmental policy and must yield a significant public benefit, or (2) the preservation must be for the scenic enjoyment of the general public and must yield a significant public benefit. In connection with the first test, the final regulations retain the "sliding scale" approach adopted in the proposed regulations which is used to establish a relationship between the two requirements. Thus, although the requirements of governmental policy and public benefit must be met independently, the more specific the governmental policy with respect to a particular site to be protected, the more likely the governmental decision, by itself, will tend to establish the significant public benefit associated with the donation.

Commenters felt the regulations did not sufficiently clarify the standards under which deductions are allowed for the preservation of open space. Many of the comments received suggested revisions in the final regulations to provide donors with procedural "safe harbors" to avoid uncertainty regarding the deductibility of their donations. Commentators believed that without safe harbors, donors either will have to bear the expense of seeking advance rulings, or will risk additional tax liability if their deductions are later disallowed. Generally, the commenters suggested the following:

(1) A declaration by a unit of government identifying a particular property as worthy of protection should meet the clearly delineated governmental policy test and thus be sufficient to eliminate the need to meet the significant public benefit test.

(2) Acceptance of a donation by a unit of government (federal, state or local) or a duly constituted commission of such unit of government, should establish both a clearly delineated governmental policy and significant public benefit.

(3) A sliding scale approach should be extended to the relationship between scenic enjoyment of the general public and significant public benefit. Thus, the more scenic the view and the more people who see it, the more it tends to confer a significant public benefit.

(4) The regulations should encourage donations of farmland for agricultural uses by expanding references to the preservation of farmland to uses other than just the preservation of farmland pursuant to a state program for flood prevention and control. See §1.170A-14(d)(4)(iv)(B). Commenters believed the reference was misleading because it implied that such is the only use for which there can be a deductible donation of farmland.

(5) Acceptance of a donation by a qualified conservation organization should be conclusive evidence of deductibility. Because the Internal Revenue Service lacks the expertise to make the subjective determinations of "significant public benefit" and "scenic enjoyment", that responsibility should be delegated to either a private organization or to another governmental agency with acknowledged expertise in

this area.

In general, the rules in the proposed regulations relating to open space easements have been retained in the final regulations. However, in response to the comments, some clarifications have been made regarding such easements. First, the fact that a unit of government has identified a particular property as worthy of protection does not by itself show the existence of a clearly delineated governmental policy, and thus, the significant public benefit associated with the donation must be independently demonstrated. Second, when there is a rigorous review of a donation by a unit of government or a duly constituted commission of a unit of government, the acceptance of a donation by such unit or commission of government tends to establish the clearly delineated governmental policy. An example of a rigorous review process has been included in the final regulations. The more specific the governmental policy with respect to a particular site to be protected, the more likely it is that the governmental decision to accept the donation will tend, by itself, to establish the significant public benefit associated with the donation. A degree of certainty is available to donors in jurisdictions that have clearly articulated preservation policies, but as with any subjective test, there must ultimately be some exercise of judgment and responsibility by both donors and donees. Third, the terms "significant public benefit" and "scenic enjoyment" necessarily require a case-by-case factual determination and hence cannot be defined precisely. The list of factors included at §1.170A-14(d)(4)(iv) with respect to "significant public benefit" and §1.170A-14(d)(4)(ii) with respect to "scenic enjoyment" are intended to be illustrative, rather than all-inclusive. In a particular case, other facts and circumstances may be relevant. Fourth, the regulations clarify that farmland, as recognized by the statute, is merely a category of open space that must meet either of the two prescribed tests in order to be a deductible contribution. Finally, acceptance of a donation by a qualified organization is not conclusive evidence of the deductibility of a donation. The Internal Revenue Service has the responsibility for making final determinations as to the deductibility of donations. That responsibility cannot be delegated to a private organization or to another governmental agency, although the Service accords substantial weight to the determinations of qualified organizations and governmental agencies in its decision-making process.

Donations of Mortgaged Property

Section 170(h)(5) provides that the conservation purposes of the donation must be protected in perpetuity. The proposed regulations did not specifically address how this requirement applies to mortgaged property.

In response to comments received, the final regulations clarify that when a contribution of mortgaged property is made to a qualified organization, the mortgagee must subordinate its rights under the mortgage to the right of the qualified organization to enforce the conservation purposes of the gift in perpetuity. However, since certain donees, unaware of this clarification, accepted (or will have accepted) contributions of mortgaged property prior to February 12, 1986, without requiring subordination of the mortgagee's rights in the property, a donor will be allowed a deduction for such a contribution provided that the donor can demonstrate that the conservation purposes of the gift are protected in perpetuity absent subordination.

Valuation

Section 1.170A-14(h)(3)(i) of the final regulations has been revised to indicate that increases in the value of any property owned by the donor or a related person—not just contiguous property—resulting from the granting of a perpetual conservation restriction must be taken into account in determining the amount of the deduction.

PAPERWORK REDUCTION ACT

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. Although a notice of proposed rulemaking which solicited public comments was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is Ada S. Rousso of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Parts 1, 20, 25, and 602 are amended as follows:

Paragraph 1. The authority for Part 1 continues to read in part: 26 U.S.C. 7805. * * *

§1.167(a)-5 [Amended]

Par. 2. Section 1.167(a)-5 is amended by adding at the end thereof the following new sentence: "For the adjustment to the basis of a structure in the case of a donation of a qualified conservation contribution under section 170(h), see §1.170A-14(h)(3)(iii)."

Par. 3. Section 1.170A-7 is amended as follows:

a. The first sentence of paragraph (b)(1)(ii) is revised to begin with the phrase "With respect to contributions made on or before December 17, 1980,".

b. Paragraph (b)(1)(ii) is revised by adding at the end the following new sentence: "For the deductibility of a qualified conservation contribution, see §1.170A.-14".

c. A new paragraph (b)(5) is added immediately after paragraph (b)(4), as set forth below.

d. The first sentence of paragraph (c) is revised to begin with the phrase "Except as provided in §1.170A-14."

e. Paragraph (e) is revised as set forth below.

§1.170A-7 Contributions not in trust of partial interests in property.

* * * * *

(b) *Contributions of certain partial interests in property for which a deduction is allowed.** * *

(5) *Qualified conservation contribution.* A deduction is allowed under section 170 for the value of a qualified conservation contribution. For the definition of a qualified conservation contribution. See §1.170A-14

* * * * *

(e) *Effective date.* This section applies only to contributions made after July 31, 1969. The deduction allowable under §1.170A-7(b)(1)(ii) shall be available only for contributions made on or before December 17, 1980. Except as otherwise provided in §1.170A-14(g)(4)(ii) the deduction allowable under §1.170A-7(b)(5) shall be available for contributions made on or after December 18, 1980.

Par. 4. A new §1.170A-14 is added after §1.170A-13T to read as set forth below.

§1.170A-14 Qualified conservation contributions.

(a) *Qualified conservation contributions.* A deduction under section 170 is generally not allowed for a charitable contribution of any interest in property that consists of less than the donor's entire interest in the property other than certain transfers in trust (see §1.170A-6 relating to charitable contributions in trust and §1.170A-7 relating to contributions not in trust of partial interests in property). However, a deduction may be allowed under section 170(f)(3)(B)(iii) for the value of a qualified conservation contribution if the requirements of this section are met. A qualified conservation contribution is the contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes. To be eligible for a deduction under this section, the conservation purpose must be protected in perpetuity.

(b) *Qualified real property interest*—(1) *Entire interest of donor other than qualified mineral interest.* (i) The entire interest of the donor other than a qualified mineral interest is a qualified real property interest. A qualified mineral interest is the donor's interest in subsurface oil, gas, or other minerals and the right of access to such minerals.

(ii) A real property interest shall not be treated as an entire interest other than a qualified mineral interest by reason of section 170(h)(2)(A) and this paragraph (b)(1) if the property in which the donor's interest exists was divided prior to the contribution in order to enable the donor to retain control of more than a qualified mineral interest or to reduce the real property interest donated. See Treasury regulations §1.170A-7(a)(2)(i). An entire interest in real property may consist of an undivided interest in the property. But see section 170(h)(5)(A) and the regulations thereunder (relating to the requirement that the conservation purpose which is the subject of the donation must be protected in perpetuity). Minor interests, such as rights-of-way, that will not interfere with the conservation purposes of the donation, may be transferred prior to the conservation contribution without affecting the treatment of a property interest as a qualified real property interest under this paragraph (b)(1).

(2) *Perpetual conservation restriction.* A perpetual conservation restriction is a qualified real property interest. A "perpetual conservation restriction" is a restriction granted in perpetuity on the use which may be made of real property—including, an easement or other interest in real property that under state law has attributes similar to an easement (e.g., a restrictive covenant or equitable servitude). For purposes of this section, the terms "easement", "conservation restriction", and "perpetual conservation restriction" have the same meaning. The definition of "perpetual conservation restriction" under this paragraph (b)(2) is not intended to preclude the deductibility of a donation of affirmative rights to use a land or water area under §1.170A-13(d)(2). Any rights reserved by the donor in the donation of a perpetual conservation restriction must conform to the requirements of this section. See *e.g.*, paragraph (d)(4)(ii), (d)(5)(i), (e)(3), and (g)(4) of this section.

(c) *Qualified organization*—(1) *Eligible donee.* To be considered an eligible donee under this section, an organization must be a qualified organization, have a commitment to protect the conservation purposes of the donation, and have the resources to enforce the restrictions. A conservation group organized or operated primarily or substantially for one of the conservation purposes specified in section 170(h)(4)(A) will be considered to have the commitment required by the preceding sentence. A qualified organization need not set aside funds, to enforce the restrictions that are the subject of the contribution. For purposes of this section, the term "qualified organization" means:

(i) A governmental unit described in section 170(b)(1)(A)(v);

(ii) An organization described in section 170(b)(1)(A)(vi);

(iii) A charitable organization described in section 501(c)(3) that meets the public support test of 509(a)(2);

(iv) A charitable organization described in section 501(c)(3) that meets the requirements of section 509(a)(3) and is controlled by an organization described in paragraphs (c)(1)(i), (ii), or (iii) of this section.

(2) *Transfers by donee.* A deduction shall be allowed for a contribution under this section only if in the instrument of conveyance the donor prohibits the donee from subsequently transferring the easement (or, in the case of a remainder interest or the reservation of a qualified mineral interest, the property), whether or not for consideration, unless the donee organization, as a condition of the subsequent transfer, requires that the conservation purposes which the contribution was originally intended to advance continue to be carried out. Moreover, subsequent transfers must be restricted to organizations qualifying, at the time of the subsequent transfer, as an eligible donee under paragraph (c)(1) of this section. When a later unexpected change in the conditions surrounding the property that is the subject of a donation under paragraph (b)(1), (2), or (3) of this section makes impossible or impractical the continued use of the property for conservation purposes, the requirement of this paragraph will be met if the property is sold or exchanged and any proceeds are used by the donee organization in a manner consistent with the conservation purposes of the original contribution. In the case of a donation under paragraph (b)(3) of this section to which the preceding sentence

applies, see also paragraph (g)(5)(ii) of this section.

(d) *Conservation purposes*—(1) *In general.* For purposes of section 170(h) and this section, the term "conservation purposes" means—

(i) The preservation of land areas for outdoor recreation by, or the education of, the general public, within the meaning of paragraph (d)(2) of this section.

(ii) The protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem, within the meaning of paragraph (d)(3) of this section.

(iii) The preservation of certain open space (including farmland and forest land) within the meaning of paragraph (d)(4) of this section, or

(iv) The preservation of a historically important land area or a certified historic structure, within the meaning of paragraph (d)(5) of this section.

(2) *Recreation or education*—(i) *In general.* The donation of a qualified real property interest to preserve land areas for the outdoor recreation of the general public or for the education of the general public will meet the conservation purposes test of this section. Thus, conservation purposes would include, for example, the preservation of a water area for the use of the public for boating or fishing, or a nature or hiking trail for the use of the public.

(ii) *Access.* The preservation of land areas for recreation or education will not meet the test of this section unless the recreation or education is for the substantial and regular use of the general public.

(3) *Protection of environmental system*—(i) *In general.* The donation of a qualified real property interest to protect a significant relatively natural habitat in which a fish, wildlife, or plant community, or similar ecosystem normally lives will meet the conservation purposes test of this section. The fact that the habitat or environment has been altered to some extent by human actrivity will not result in a deduction being denied under this section if the fish, wildlife, or plants continue to exist there in a relatively natural state. For example, the preservation of a lake formed by a man made dam or a salt pond formed by a man-made dike would meet the conservation purposes test if the lake or pond were a nature feeding area for a wildlife community that included rare, endangered, or threatened native species.

(ii) *Significant habitat or ecosystem.* Significant habitats and ecosystems include, but are not limited to, habitats for rare, endangered, or threatened species of animal, fish, or plants; natural areas that represent high quality examples of a terrestrial community or aquatic community, such as islands that are undeveloped or not intensely developed where the coastal ecosystem is relatively intact; and natural areas which are included in or which contribute to, the ecological viability of a local, state, or national park, nature preserve, wildlife refuge, wilderness area, or other similar conservation area.

(iii) *Access.* Limitations on public access to property that is the subject of a donation under this paragraph (d)(3) shall not render the donation nondeductible. For example, a restriction on all public access to the habitat of a threatened native animal species protected by a donation under this paragraph (d)(3) would not cause the donation to be nondeductible.

(4) *Preservation of open space*—(i) *In general.* The donation of a qualified real property interest to preserve open space (including farmland and forest land) will meet the conservation purposes test of this section if such preservation is—

(A) Pursuant to a clearly delineated Federal, state, or local governmental conservation and will yield a significant public benefit, or

(B) For the scenic enjoyment of the general public and will yield a significant public benefit.

An open space easement donated on or after December 18, 1980, must meet the requirements of 170(h) in order to be deductible.

(ii) *Scenic enjoyment*—(A) *Factors.* A contribution made for the preservation of open space may be for the scenic enjoyment of the general public. Preservation of land may be for the scenic enjoyment of the general public if development of the property would impair the scenic character of the local rural or urban landscape or would interfere with a scenic panorama that can be enjoyed from a park, nature preserve, road, waterbody, trail, or historic structure or land area, and such area or transportation way is open to, or utilized by, the public. "Scenic enoyment" will be evaluated by considering all pertinent facts and circumstances germane to the contribution. Regional variations in topography, geology, biology, and cultural and economic conditions require flexibility in the application of this test, but do not lessen the burden on the taxpayer to demonstrate the scenic characteristics of a donation under this paragraph. The application of a particular objective factor to help define a view as "scenic" in one setting may in fact be entirely inappropriate in another setting. Among the factors to be considered are:

(1) The compatibility of the land use with other land in the vicinity;

(2) The degree of contrast and variety provided by the visual scene;

(3) The openness of the land (which would be a more significant factor in an urban or densely populated setting or in a heavily wooded area);

(4) Relief from urban closeness;

(5) The harmonious variety of shapes and textures;

(6) The degree to which the land use maintains the scale and character of the urban landscape to preserve open space, visual enjoyment, and sunlight for the surrounding area:

(7) The consistency of the proposed scenic view with a methodical state scenic identification program, such as a state landscape inventory; and

(8) The consistency of the proposed scenic view with a regional or local landscape inventory made pursuant to a sufficiently rigorous review process, especially if the donation is endorsed by an appropriate state or local governmental agency.

(B) *Access.* To satisfy the requirement of scenic enjoyment by the general public, visual (rather than physical) access to or across the property by the general public sufficient. Under the terms of an open space easement on scenic property, the entire property need not be visible to the public for a donation to qualify under this section, although the public benefit from the donation may be insufficient to quality for a deduction if only a small portion of the property is visible to the public.

(iii) *Governmental conservation policy*—(A) *In general.* The requirement that the preservation of open space be pursuant to a clearly delineated Federal, state, or local governmental policy is intended to protect the types of property identified by representatives of the general public as worthy of preservation or conservation. A general declaration of conservation goals by a single official or legislative body is not sufficient. However, a governmental conservation policy need not be a certification program that identifies particular lots or small parcels of individually owned property. This requirement will be met by donations that further a specific, identified conservation project, such as the preservation of land within a state or local landmark district that is locally recognized as being significant to that district; the preservation of a wild or scenic river, the preservation of farmland pursuant to a state program for flood prevention and control; or the protection of the scenic, ecological, or historic character of land that is contiguous to, or an integral part of, the surroundings of existing recreation or conservation sites. For example, the donation of a perpetual conservation restriction to a qualified organization pursuant to a formal resolution or certification by a local governmental agency established under state law specifically identifying the subject property as worthy of protection for conservation purposes will meet the requirement of this paragraph. A program need not be funded to satisfy this requirement, but the program must involve a significant commitment by the government with respect to the conservation project. For example, a governmental program according preferential tax assessment or preferential zoning for certain property deemed worthy of protection for conservation purposes would constitute a significant commitment by the government.

(B) *Effect of acceptance by governmental agency.* Acceptance of an easement by an agency of the Federal Government or by an agency of a state or local government (or by a commission, authority, or similar body duly constituted by the state or local government and acting on behalf of the state or local government) tends to establish the requisite clearly delineated governmental policy, although such acceptance, without more, is not sufficient. The more rigorous the review process by the governmental agency, the more the acceptance of the easement tends to establish the requisite clearly delineated governmental policy. For example, in a state where the legislature has established an Environmental Trust to accept gifts to the state which meet certain conservation purposes and to submit the gifts to a review that requires the approval of the state's highest officials, acceptance of a gift by the Trust tends to establish the requisite clearly delineated governmental policy. However, if the Trust merely accepts such gifts without a review process, the requisite clearly delineated governmental policy is not established.

(C) *Access.* A limitation on public access to property subject to a donation under this paragraph (d)(4)(iii) shall not render the deduction nondeductible unless the conservation purpose of the donation would be undermined or frustrated without public access. For example, a donation pursuant to a governmental policy to protect the scenic character of land near a river requires visual access to the same extent as would a donation under paragraph (d)(4)(ii) of this section.

(iv) *Significant public benefit*—(A) *Factors.* all contributions made for the preservation of open space must yield a significant public benefit. Public benefit will be evaluated by considering all pertinent facts and circumstances germane to the contribution. Factors germane to the evaluation of public benefit from one contribution may be irrelevant in determining public benefit from another contribution. No single factor will necessarily be determinative. Among the factors to be considered are:

(1) The uniqueness of the property to the area;

(2) The intensity of land development in the vicinity of the property (both existing development and foreseeable trends of development);

(3) The consistency of the proposed open space use with public programs (whether Federal, state or local) for conservation in the region, including programs for outdoor recreation, irrigation or water supply protection, water quality maintenance or enhancement, flood prevention and control, erosion control, shoreline protection, and protection of land areas included in, or related to, a government approved master plan or land management area;

(4) The consistency of the proposed open space use with existing private conservation programs in the area, as evidenced by other land, protected by easement or fee ownership by organizations referred to in §1.170A-14(c)(1), in close proximity to the property;

(5) The likelihood that development of the property would lead to or contribute to degradation of the scenic, natural, or historic character of the area:

(6) The opportunity for the general public to use the property or to appreciate its scenic values;

(7) The importance of the property in preserving a local or regional landscape or resource that attracts tourism or commerce to the area;

(8) The likelihood that the donee will acquire equally desirable and valuable substitute property or property rights;

(9) The cost to the donee of enforcing the terms of the conservation restriction;

(10) The population density in the area of the property; and

(11) The consistency of the proposed open space use with a legislatively mandated program identifying particular parcels of land for future protection.

(B) *Illustrations.* The preservation of an ordinary tract of land would not in and of itself yield a significant public benefit, but the preservation of ordinary land areas in conjunction with other factors that demonstrate significant public benefit or the preservation of a unique land area for public enjoyment would yield a significant public benefit. For example, the preservation of a vacant downtown lot would not by itself yield a significant public benefit, but the preservation of the downtown lot as a public garden would, absent countervailing factors, yield a significant public benefit. The following are other examples of contributions which would, absent countervailing factors, yield a significant public benefit: the preservation of farmland pursuant to a state program for flood prevention and control; the preservation of a unique natural land formation for the enjoyment of the general public; the preservation of woodland along a public highway pursuant to a government program to preserve the appearance of the area so as to maintain the scenic view from the highway; and the preservation of a stretch of undeveloped property located between a public highway and the ocean in order to maintain the scenic ocean view from the highway.

(v) *Limitation.* A deduction will not

be allowed for the preservation of open space under section 170(h)(4)(A)(iii), if the terms of the easement permit a degree of intrusion or future development that would interfere with the essential scenic quality of the land or with the governmental conservation policy that is being furthered by the donation. See §1.170A-14(e)(2) for rules relating to inconsistent use.

(vi) *Relationship of requirements*—(A) *Clearly delineated governmental policy and significant public benefit.* Although the requirements of "clearly delineated governmental policy" and "significant public benefit" must be met independently, for purposes of this section the two requirements may also be related. The more specific the governmental policy with respect to the particular site to be protected, the more likely the governmental decision, by itself, will tend to establish the significant public benefit associated with the donation. For example, while a statute in State X permitting preferential assessment for farmland is, by definition, governmental policy, it is distinguishable from a state statute, accompanied by appropriations, naming the X River as a valuable resource and articulating the legislative policy that the X River and the relatively natural quality of its surrounding be protected. On these facts, an open space easement on farmland in State X would have to demonstrate additional factors to establish "significant public benefit." The specificity of the legislative mandate to protect the X River, however, would by itself tend to establish the significant public benefit associated with an open space easement on land fronting the X River.

(B) *Scienic enjoyment and significant public benefit.* With respect to the relationship between the requirements of "scenic enjoyment" and "significant public benefit," since the degrees of scenic enjoyment offered by a variety of open space easements are subjective and not as easily delineated as are increasingly specific levels of governmental policy, the significant public benefit of preserving a scenic view must be independently established in all cases.

(C) *Donations may satisfy more than one test.* In some cases, open space easements may be both for scenic enjoyment and pursuant to a clearly delineated governmental policy. For example, the preservation of a particular scenic view identified as part of a scenic landscape inventory by a rigorous governmental review process will meet the tests of both paragraphs (d)(4)(i)(A) and (d)(4)(i)(B) of this section.

(5) *Historic preservation*—(i) *In general.* The donation of a qualified real property interest to preserve an historically important land area or a certified historic structure will meet the conservation purposes test of this section. When restrictions to preserve a building or land area within a registered historic district permit future development on the site, a deduction will be allowed under this section only if the terms of the restrictions require that such development conform with appropriate local, state, or Federal standards for construction or rehabilitation within the district. See also §1.170A-14(h)(3)(ii).

(ii) *Historically important land area.* The term "historically important land area" includes:

(A) An independently significant land area including any related historic resources (for example, an archaeological site or a Civil War battlefield with related monuments, bridges, cannons, or houses) that meets the National Register Criteria for Evaluation in 36 CFR 60.4 (Pub. L. 89-665, 80 Stat. 915);

(B) Any land area within a registered historic district including any buildings on the land area that can reasonably be considered as contributing to the significance of the district; and

(C) Any land area (including related historic resources) adjacent to a property listed individually in the National Register of Historic Places (but not within a registered historic district) in a case where the physical or environmental features of the land area contribute to the historic or cultural integrity of the property.

(iii) *Certified historic structure—Definition.* The term "certified historic structure," for purposes of this section, means any building, structure or land area which is—

(A) listed in the National Register, or

(B) located in a registered historic district (as defined in section 48(g)(3)(B)) and is certified by the Secretary of the Interior (pursuant to 36 CFR 67.4) to the Secretary of the Treasury as being of historic significance to the district.

A "structure" for purposes of this section means any structure, whether or not it is depreciable. Accordingly easements on private residences may qualify under this section. In addition, a structure would be considered to be a certified historic structure if it were certified either at the time the transfer was made or at the due date (including extensions) for filing the donor's return for the taxable year in which the contribution was made.

(iv) *Access.* (A) In order for a conservation contribution described in section 170(h)(4)(A)(iv) and this paragraph (d)(5) to be deductible, some visual public access to the donated property is required. In the case of an historically important land area, the entire property need not be visible to the public for a donation to qualify under this section. However, the public benefit from the donation may be insufficient to qualify for a deduction if only a small portion of the property is so visible. Where the historic land area or certified historic structure which is the subject of the donation is not visible from a public way (*e.g.*, the structure is hidden from view by a wall or shrubbery, the structure is too far from the public way, or interior characteristics and features of the structure are the subject of the easement), the terms of the easement must be such that the general public is given the opportunity on a regular basis to view the characteristics and features of the property which are preserved by the easement to the extent consistent with the nature and condition of the property.

(B) Factors to be considered in determining the type and amount of public access required under paragraph (d)(5)(iv)(A) of this section include the historical significance of the donated property, the nature of the features that are the subject of the easement, the remoteness or accessibility of the site of the donated property, the possibility of physical hazards to the public visiting the property (for example, an unoccupied structure in a dilapidated condition), the extent to which public access would be an unreasonable intrusion on any privacy interests of individuals living on the property, the degree to which public access would impair the preservation interests which are the subject of the donation, and the availability of opportunities for the public to view the property by means other than visits to the site.

(C) The amount of access afforded the public by the donation of an easement shall be determined with reference to the amount of access permitted by the terms of the easement which are established by the donor, rather than the amount of access actually provided by the donee organization. However, if the donor is aware of any facts indicating that the amount of access that the donee organization will provide is significantly less than the amount of access permitted under the terms of the easement, then the amount of access afforded the public shall be determined with reference to this lesser amount.

(v) *Examples*. The provisions of paragraph (d)(5)(iv) of this section may be illustrated by the following examples:

Example (1). A and his family live in a house in a certified historic district in the State of X. The entire house, including its interior, has architectural features representing classic Victorian period architecture. A donates an exterior and interior easement on the property to a qualified organization but continues to live in the house with his family. A's house is surrounded by a high stone wall which obscures the public's view of it from the street. Pursuant to the terms of the easement, the house may be opened to the public from 10:00 a.m. to 4:00 p.m. on one Sunday in May and one Sunday in November each year for house and garden tours. These tours are to be under the supervision of the donee and open to members of the general public upon payment of a small fee. In addition, under the terms of the easement, the donee organization is given the right to photograph the interior and exterior of the house and distribute such photographs to magazines, newsletters, or other publicly available publications. The terms of the easement also permit persons affiliated with educational organizations, professional architectural associations, and historical societies to make an appointment through the donee organization to study the property. The donor is not aware of any facts indicating that the public access to be provided by the donee organization will be significantly less than that permitted by the terms of the easement. The 2 opportunities for public visits per year, when combined with the ability of the general public to view the architectural characteristics and features that are the subject of the easement through photographs, the opportunity for scholarly study of the property, and the fact that the house is used as an occupied residence, will enable the donation to satisfy the requirement of public access.

Example (2). B owns an unoccupied farmhouse built in the 1840's and located on a property that is adjacent to a Civil War battlefield. During the Civil War the farmhouse was used as quarters for Union troops. The battlefield is visited year round by the general public. The condition of the farmhouse is such that the safety of visitors will not be jeopardized and opening it to the public will not result in significant deterioration. The farmhouse is not visible from the battlefield or any public way. It is accessible only by way of a private road owned by B. B donates a conservation easement on the farmhouse to a qualified organization. The terms of the easement provide that the donee organization may open the property (via B's road) to the general public on four weekends each year from 8:30 a.m. to 4:00 p.m. The donation does not meet the public access requirement because the farmhouse is safe, unoccupied, and easily accessible to the general public who have come to the site to visit Civil War historic land areas (and related resources), but will only be open to the public on four weekends each year. However, the donation would meet the public access requirement if the terms of the easement permitted the donee organization to open the property to the public every other weekend during the year and the donor is not aware of any facts indicating that the donee organization will provide significantly less access than that permitted.

(e) *Exclusively for conservation purposes*. (i) *In general*. To meet the requirements of this section, a donation must be exclusively for conservation purposes. See paragraphs (c)(1) and (g)(1) through (g)(6)(ii) of this section. A deduction will not be denied under this section when incidental benefit inures to the donor merely as a result of conservation restrictions limiting the uses to which the donor's property may be put.

(2) *Inconsistent use*. Except as provided in paragraph (e)(4) of this section, a deduction will not be allowed if the contribution would accomplish one of the enumerated conservation purposes but would permit destruction of other significant conservation interests. For example, the preservation of farmland pursuant to a State program for flood prevention and control would not qualify under paragraph (d)(4) of this section if under the terms of the contribution a significant naturally occurring ecosystem could be injured or destroyed by the use of pesticides in the operation of the farm. However, this requirement is not intended to prohibit uses of the property, such as selective timber harvesting or selective farming if, under the circumstances, those uses do not impair significant conservation interests.

(3) *Inconsistent use permitted*. A use that is destructive of conservation interests will be permitted only if such use is necessary for the protection of the conservation interests that are the subject of the contribution. For example, a deduction for the donation of an easement to preserve an archaeological site that is listed on the National Register of Historic Places will not be disallowed if site excavation consistent with sound archaeological practices may impair a scenic view of which the land is a part. A donor may continue a pre-existing use of the property that does not conflict with the conservation purposes of the gift.

(f) *Examples*. The provisions of this section relating to conservation purposes may be illustrated by the following examples.

Example (1). State S contains many large tract forests that are desirable recreation and scenic areas for the general public. The forests' scenic values attract millions of people to the State. However, due to the increasing intensity of land development in State S, the continued existence of forestland parcels greater than 45 acres is threatened. J grants a perpetual easement on a 100-acre parcel of forestland that is part of one of the State's scenic areas to a qualifying organization. The easement imposes restrictions on the use of the parcel for the purpose of maintaining its scenic values. The restrictions include a requirement that the parcel be maintained forever as open space devoted exclusively to conservation purposes and wildlife protection, and that there be no commercial, industrial, residential, or other development use of such parcel. The law of State S recognizes a limited public right to enter private land, particularly for recreational pursuits, unless such land is posted or the landowner objects. The easement specifically restricts the landowner from posting the parcel, or from objecting thereby maintaining public access to the parcel according to the custom of the State. J's parcel provides the opportunity for the public to enjoy the use of the property and appreciate its scenic values. Accordingly, J's donation qualifies for a deduction under this section.

Example (2). A qualified conservation organization owns Greenacre in fee as a nature preserve. Greenacre contains a high quality example of a tall grass prairie ecoystem. Farmacre, an operating farm, adjoins Greenacre and is a compatible buffer to the nature preserve. Conversion of Farmacre to a more intense use, such as a housing development, would adversely affect the continued use of Greenacre as a nature preserve because of human traffic generated by the development. The owner of Farmacre donates an easement preventing any future development on Farmacre to the qualified conservation organization for conservation purposes. Normal agricultural uses will be allowed on Farmacre. Accordingly, the donation qualifies for a deduction under this section.

Example (3). H owns Greenacre, a 900-acre parcel of woodland, rolling pasture, and orchards on the crest of a mountain. All of Greenacre is clearly visible from a nearby national park. Because of the strict enforcement of an applicable zoning plan, the highest and best use of Greenacre is as a subdivision of 40-acre tracts. H wishes to donate a scenic easement on Greenacre to a qualifying conservation organization, but H would like to reserve the right to subdivide Greenacre into 90-acre parcels with no more than one single-family home allowable on each parcel. Random building on the property, even as little as one home for each 90 acres, would destroy the scenic character of the view. Accordingly, no deducation would be allowable under this section.

Example (4). Assume the same facts as in *example (3)*, except that not all of Greenacre is visible from the park and the deed of easement allows for limited cluster development of no more than five nine-acre clusters (with four houses on each cluster) located in areas generally not visible from the national park and subject to site and building plan approval by the donee organization in order to preserve the scenic view from the park. The donor and the donee have already identified sites where limited cluster development would not be visible from the park or would not impair the view. Owners of homes in the clusters will not have any rights which respect to the surrounding Greenacre property that are not also available to the general public. Accordingly, the donation qualifies for a deduction under this section.

Example (5). In order to protect State S's declining open space that is suited for agricultural use from increasing development pressure that has led to a marked decline in such open space, the Legislature of State S passed a statute authorizing the purchase of "agricultural land development rights" on open acreage. Agricultural land development rights allow the State to place agricultural preservation restrictions on land designated as worthy of protection in order to preserve open space and farm resources. Agricultural preservation restrictions prohibit or limit construction or placement of buildings except those used for agricultural purposes or dwellings used for family living by the farmer and his family and employees; removal of mineral substances in any manner that adversely affects the land's agricultural potential; or other uses determinental to retention of the land for agricultural use. Money has been appropriated for this program and some landowners have in fact sold their "agricultural land development rights" to State S. K owns and operates a small" dairy farm in State S located in an area designated by the Legislature as worthy of protection. K desires to preserve his farm for agricultural purposes in perpetuity. Rather than selling the development rights to State S. K grants to a qualified organization an agricultural preservation restriction on his property in the form of a conservation easement. K reserves to himself, his heirs and assigns the right to manage the farm consistent with sound agricultural and management practices. The preservation of K's land is pursuant to a clearly delineated governmental policy of preserving open space available for agricultural use, and will yield a significant public benefit by preserving open space against increasing development pressures. Accordingly, a deduction is allowed under this section.

(g) *Enforceable in perpetuity*—(1) *In general.* In the case of any donation under this section, any interest in the property retained by the donor (and the donor's successors in interest) must be subject to legally enforceable restrictions (for example, by recordation in the land records of the jurisdiction in which the property is located) that will prevent uses of the retained interest inconsistent with the conservation purposes of the donation. In the case of a contribution of a remainder interest, the contributrion will not qualify if the tenants, whether they are tenants for life or a term of years, can use the property in a manner that diminishes the conservation values which are intended to be protected by the contribution.

(2) Protection of a conservation purpose in case of donation of property subject to a mortgage. In the case of conservation contributions made after February 13, 1986, no deduction will be permitted under this section for an interest in property which is subject to a mortgage unless the mortgagee subordinates its rights in the property to the right of the qualified organization to enforce the conservation purposes of the gift in perpetuity. For conservation contributions made prior to February 14, 1986, the requirement of section 170(h)(5)(A) is satisfied in the case of mortgaged property (with respect to which the mortgagee has not subordinated its rights) only if the donor can demonstrate that the conservation purpose is protected in perpetuity without subordination of the mortgagee's right.

(3) *Remote future event.* A deduction shall not be disallowed under section 170(f)(3)(B)(iii) and this section merely because the interest which passes to, or is vested in, the donee organization may be defeated by the performance of some act or the happening of some event, if on the date of the gift it appears that the possibility that such act or event will occur is so remote as to be negligible. See paragraph (e) of §1.170A-1. For example, a state's statutory requirement that use restrictions must be rerecorded every 30 years to remain enforceable shall not, by itself, render an easement nonperpetual.

(4) *Retention of qualified mineral interest*—(i) *In general.* Except as otherwise provided in paragraph (g)(4)(ii) of this section, the requirements of this section are not met and no deduction shall be allowed in the case of a contribution of any interest when there is a retention by any person of qualified mineral interest (as defined in paragraph (b)(1)(i) of this section) if at any time there may be extractions or removal of minerals by any surface mining method. Moreover, in the case of a qualified mineral interest gift, the requirement that the conservation purposes be protected in perpetuity is not satisfied if any method of mining that is inconsistent with the particular conservation purposes of a contribution is permitted at any time. See also §1.170A-14(e)(2). However, a deduction under this section will not be denied in the case of certain methods of mining that may have limited, localized impact on the real property but that are not irremediably destructive of significant conservation interests. For example, a deduction will not be denied in a case where production facilities are concealed or compatible with existing topography and landscape and when surface alteration is to be restored to its orginal state.

(ii) *Exception for qualified conservation contributions after July 1984.* (A) A contribution made after July 18, 1984, of a qualified real property interest described in section 170(h)(2)(A) shall not be disqualified under the first sentence of paragraph (g)(4)(i) of this section if the following requirements are satisfied.

(1) The ownership of the surface estate and mineral interest were separated before June 13, 1976, and remain so separated up to and including the time of the contribution.

(2) The present owner of the mineral interest is not a person whose relationship to the owner of the surface estate is described at the time of the contribution in section 267(b) or section 707(b), and

(3) The probability of extraction or removal of minerals by any surface mining method is so remote as to be negligible.

Whether the probability of extraction or removal of minerals by surface mining is so remote as to be negligible is a question of fact and is to be made on a case by case basis. Relevant factors to be considered in determining if the probability of extraction or removal of minerals by surface mining is so remote as to be negligible include: geological, geophysical or economic data showing the absence of mineral reserves on the property, or the lack of commercial feasibility at the time of the contribution of surface mining the mineral interest.

(B) If the ownership of the surface estate and mineral interest first became separated after June 12, 1976, no deduction is permitted for a contribution under this section unless surface mining on the property is completely prohibited.

(iii) Examples. The provisions of paragraph (g)(4)(i)and (ii) of this section may be illustrated by the following examples:

Example (1). K owns 5,000 acre of bottomland hardwood property along a major watershed system in the southern part of the United States. Agencies within the Department of the Interior have determined that southern bottomland hardwoods are a rapidly diminishing resource and a critical ecosystem in the south because of the intense pressure to cut the trees and convert the land to agricultural use. These agencies have further determined (and have indicated in correspondence with K) that bottomland hardwoods provide a superb habitat for numerous species and play an important role in controlling floods and in purifying rivers. K donates to a qualified organization his entire interest in this property other than his interest in the gas and oil deposits that have been identified under K's property. K covenants and can ensure that, although drilling for gas and oil on the property may have some temporary localized impact on the real property, the drilling will not interfere with the overall conservation purpose of the gift, which is to protect the unique bottomland hardwood ecosystem. Accordingly, the donation qualifies for a deduction under this section.

Example (2). Assume the same facts as in example (1), except that in 1979, K sells the mineral interest to A, an unrelated person, in an arm's-length transaction, subject to a recorded prohibition on the removal of any minerals by any surface mining method and a recorded prohibition against any mining technique that will harm the bottomland hardwood ecosystem. After the sale to A, K donates a qualified real property interest to a qualified organization to protect the bottomland hardwood ecosystem. Since at the time of the transfer, surface mining and any mining technique that will harm the bottomland hardwood ecosystem are completely prohibited, the donation qualifies for a deduction under this section.

(5) *Protection of conservation purpose where taxpayer reserves certain rights,* (i) *Documentation.* In the case of a donation made after February 13, 1986, of any qualified real property interest when the donor reserves rights the exercise of which may impair the conservation interests associated with the property, for a deduction to be allowable under this section the donor must make available to the donee, prior to the time the donation is made, documentation sufficient to establish the condition of the property at the time of the gift. Such documentation is designed to protect the conservation interests associated with the property, which although protected in perpetuity by the easement, could be adversely affected by the exercise of the reserved rights. Such documentation may include:

(A) The appropriate survey maps from the United States Geological Survey, showing the property line and other contiguous or nearby protected areas;

(B) A map of the area drawn to scale showing all existing man-made improvements or incursions (such as roads, buildings, fences, or gravel pits), vegetation and identification of flora and fauna (including, for example, rare species locations, animal breeding and roosting areas, and migration routes), land use history (including present uses and recent past disturbances), and distinct natural features (such) as large trees and aquatic areas);

(C) An aerial photograph of the property at an appropriate scale taken as close as possible to the date the donation is made; and

(D) On-site photographs taken at appropriate locations on the property. If the terms of the donation contain restrictions with regard to a particular natural resource to be protected, such as water quality or air quality, the condition of the resource at or near the time of the gift must be established. The documentation, including the maps and photographs, must be accompanied by a statement signed by the donor and a representative of the donee clearly referencing the documentation and in substance saying "The natural resources inventory is an accurate representation of (the protected property) at the time of the transfer".

(ii) *Donee's right to inspection and legal remedies.* In the case of any donation referred to in paragraph (g)(5)(i) of this section, the donor must agree to notify the donee, in writing, before exercising any reserved right, *e.g.*, the right to extract certain minerals which may have an adverse impact on the conservation interests associated with the qualified real property interest. The terms of the donation must provide a right of the donee to enter the property at reasonable times for the purpose of inspecting the property to determine if there is compliance with the terms of the donation. Additionally, the terms of the donation must provide a right of the donee to enforce the conservation restrictions by appropriate legal proceedings, including but not limited to, the right to require the restoration of the property to its condition at the time of the donation.

(6) *Extinguishment. (i) In general.* If a subsequent unexpected change in the conditions surrounding the property that is the subject of a donation under this paragraph can make impossible or impractical the continued use of the property for conservation purposes, the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding and all of the donee's proceeds (determined under paragraph (g)(6)(ii) of this section) from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution.

(ii) *Proceeds.* In case of donation made after February 13, 1986, for a deduction to be allowed under this section, at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a property right, immediately vested in the donee organization, with a fair market value that is at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift, bears to the value of the property as a whole at that time. See §1.170A-14(h)(3)(iii) relating to the allocation of basis. For purposes of this paragraph (g)(6)(ii), that proportionate value of the donee's property rights shall remain constant. Accordingly, when a change in conditions give rise to the extinguishment of a perpetual conservation restriction under paragraph (g)(6)(i) of this section, the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to that proportionate value of the perpetual conservation restriction, unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction.

(h) *Valuation*—(1) *Entire interest of donor other than qualified mineral interest.* The value of the contribution under section 170 in the case of a contribution of a taxpayer's entire interest in property other than a qualified mineral interest is the fair market value of the surface rights in the property contributed. The value of the contribution shall be computed without regard to the mineral rights. See paragraph (h)(4), *example (1)*, of this section.

(2) *Remainder interest in real property.* In the case of a contribution of any remainder interest in real property, section 170(f)(4) provides that in determining the value of such interest for purposes of section 170, depreciation and depletion of such property shall be taken into account. See §1.170A-12. In the case of the contribution of a remainder interest for conservation purposes, the current fair market value of the property (against which the limitations of §1.170A-12 are applied) must take into account any pre-existing or contemporaneously recorded rights limiting, for conservation purposes, the use to which the subject property may be put.

(3) *Perpetual conservation restriction*—(1) *In general.* The value of the contribution under section 170 in the case of a charitable contribution of a perpetual conservation restriction is the fair market value of the perpetual conservation restriction at the time of the contribution. See §1.170A-7(c). If there is a substantial record of sale of easements comparable to the donated easement (such as purchases pursuant to a governmental program), the fair market value of the donated easement is based on the sales prices of such comparable easements. If no substantial record of market-place sales is available to use as a meaningful or valid comparison, as a general rule (but not necessarily in all cases) the fair market value of a perpetual conservation restriction is equal to the difference between the fair market value of the property it encumbers before the granting of the restriction and the fair market value of the encumbered property after the granting of the restriction. The amount of the deduction in the case of a charitable contribution of a perpetual conservation restriction covering a portion of the contiguous property owned by a donor and the donor's family (as defined in section 267 (c)(4)) is the difference between the fair market value of the entire contiguous parcel of property before and after the granting of the restriction. If the granting of a perpetual conservation restriction after January 14, 1986, has the effect of increasing the value of any other property owned by the donor or a related person, the amount of the deduction for the conservation contribution shall be reduced by the amount of the increase in the value of the other property, whether or not such property is contiguous. If, as a result of the donation of a perpetual conservation restriction, the donor or a related person receives, or can reasonably expect to receive, financial or economic benefits that are greater than those that will inure to the general public from the transfer, no deduction is allowable under this section. However, if the donor or a related person receives, or can reasonably expect to receive, a financial or economic benefit that is substantial, but it is clearly shown that the benefit is less than the amount of the transfer, then a deduction under this section is allowable for the excess of the amount transferred over the amount of the financial or economic benefit received or reasonably expected to be received by the donor or the related person. For purposes of this paragraph (h)(3)(i), related person shall have the same meaning as in either section 267(b) or section 707(b). (See *example (10)* of paragraph (h)(4) of this section.)

(ii) Fair market value of property before and after restriction. If before and after valuation is used, the fair market value of the property before contribution of the conservation restriction must take into account not only the current use of the property but also an objective assessment of how immediate or remote the likelihood is that the property, absent the restriction, would in fact be developed, as well as any effect from zoning, conservation, or historic preservation laws that already restrict the property's potential highest and best use. Further, there may be instances where the grant of a conservation restriction may have no material effect on the value of the property or may in fact serve to enhance, rather than reduce, the value of property. In such instances no deduction would be allowable. In the case of a conservation restriction that allows for any development, however limited, on the property to be protected, the fair market value of the property after contribution of the restriction must take into account the effect of the development. In the case of a conservation easement such as an easement on a certified historic structure, the fair market value of the property after contribution of the restriction must take into account the amount of access permitted by the terms of the easement. Additionally, if before and after valuation is used, an appraisal of the property after contribution of the restriction must take into account the effect of restrictions that will result in a reduction of the potential fair market value represented by highest and best use but will, nevertheless, permit uses of the property that will increase its fair market value above that represented by the property's current use. The value of a perpetual conservation restriction shall not be reduced by reason of the existence of restrictions on transfer designed solely to ensure that the conservation restriction will be dedicated to conservation purposes. See §1.170A-14(c)(3).

(iii) *Allocation of basis.* In the case of the donation of a qualified real property interest for conservation purposes, the basis of the property retained by the donor must be adjusted by the elimination of that part of the total basis of the property that is properly allocable to the qualified real property interest granted. The amount of the basis that is allocable to the qualified real property interest shall bear the same ratio to the total basis of the property as the fair market value of the qualified real property interest bears to the fair market value of the property before the granting of the qualified real property interest. When a taxpayer donates to a qualifying conservation organization an easement on a structure with respect to which deductions are taken for depreciation, the reduction required by this paragraph (h)(3)(ii) in the basis of the property retained by the taxpayer must be allocated between the structure and the underlying land.

(4) *Examples.* The provisions of this section may be illustrated by the following examples. In examples illustrating the value or deductibility of donations, the applicable restrictions and limitations of §1.170A-4, with respect to reduction in amount of charitable contributions of certain appreciated property, and §1.170A-8, with respect to limitations on charitable deductions by individuals, must also be taken into account.

Example (1). A owns Goldacre, a property adjacent to a state park. A wants to donate Goldacre to the state to be used as part of the park, but A wants to reserve a qualified mineral interest in the property, to exploit currently and to devise at death. The fair market value of the surface rights in Goldacre is $200,000 and the fair market value of the mineral rights is $100,000. In order to ensure that the quality of the park will not be degraded, restrictions must be imposed on the right to extract the minerals that reduce the fair market value of the mineral rights to $80,000. Under this section, the value of the contribution is $200,000 (the value of the surface rights).

Example (2). In 1984, B, who is 62, donates a remainder interest in Greenacre to a qualifying organization for conservation purposes. Greenacre is a tract of 200 acres of undeveloped woodland that is valued at $200,000 at its highest and best use. Under §1.170A-12(b), the value of a remainder interest in real property following one life is determined under §25.2512-5 of the Gift Tax Regulations. (See §25.2512-9 with respect to the valuation of annuities life estates, terms for years, remainders, and reversions transferred after December 31, 1970 and before December 1, 1983. With respect to the valuation of annuities, life estates, terms for years, remainders, and reversions transferred before January 1, 1971, see T.D. 6334, 23 FR 8904, November 15, 1958 [1958-2 C.B. 627], as amended by T.D. 7077, 35 FR 18464, December 4, 1970). [1970-2 C.B. 183] Accordingly, the value of the remainder interest, and thus the amount eligible for an income tax deduction under section 170(f), is $55,996 ($200,000 × .27998).

Example (3). Assume the same facts as in example (2), except that Greenacre is B's 200-acre estate with a home built during the colonial period. Some of the acreage around the home is cleared; the balance of Greenacre, except for access roads, is wooded and undeveloped. See section 170(f)(3)(B)(i). However, B would like Greenacre to be maintained in its current state after his death, so he donates a remainder interest in Greenacre to a qualifying organization for conservation purposes pursuant to section 170(f)(3)(B)(iii) and (h)(2)(B). At the time of the gift the land has a value of $200,000 and the house has a value of $100,000. The value of the remainder interest, and thus the amount eligible for an income tax deduction under section 170(f), is computed pursuant to §1.170A-12. See §1.170A-12(b)(3).

Example (4). Assume the same facts as in example (2), except that at age 62 instead of donating a remainder interest B donates an easement in Greenacre to a qualifying organization for conservation purposes. The fair market value of Greenacre after the donation is reduced to $110,000. Accordingly, the value of the easement, and thus the amount eligible for a deduction under section 170(f), is $90,000 ($200,000 less $110,000).

Example (5). Assume the same facts as in example (4), and assume that three years later, at age 65, B decides to donate a remainder interest in Greenacre to a qualifying organization for conservation purposes. Increasing real estate values in the area have raised the fair market value of Greenacre (subject to the easement) to $130,000. Accordingly, the value of the remainder interest, and thus the amount eligible for a deduction under section 170(f), is $41,639 ($130,000 ×.32030).

Example (6). Assume the same facts as in example (2), except that at the time of the donation of a remainder interest in Greenacre, B also donates an easement to a different qualifying organization for conservation purposes. Based on all the facts and circumstances, the value of the easement is determined to be $100,000. Therefore, the value of the property after the easement is $100,000 and the value of the remainder interest and thus the amount eligible for deduction under section 170(f), is $27,998 ($100,000 ×.27998).

Example (7). C owns Greenacre, a 200-acre estate containing a house built during the colonial period. At its highest and best use, for home development, the fair market value of Greenacre is $300,000. C donates an easement (to maintain the house and Greenacre in their current state) to a qualifying organization for conservation purposes. The fair market value of Greenacre after the donation is reduced to $125,000. Accordingly, the value of the easement and the amount eligible for a deduction under section 170(f) is $175,000 ($300,000 less $125,000).

Example (8) Assume the same facts as in example (7) and assume that three years later, C decides to donate a remainder interest in Greenacre to a qualifying organization for conservation purposes. Increasing real estate values in the area have raised the fair market value of Greenacre to $180,000. Assume that because of the perpetual easement prohibiting any development of the land, the value of the house is $120,000 and the value of the land is $60,000. The value of the remainder interest, and thus the amount eligible for an income tax deduction under section 170(f), is computed pursuant to §1.170A-12. See §1.170A-12(b)(3).

Example (9) D owns a property with a basis of $20,000 and a fair market value of $80,000. D donates to a qualifying organization an easement for conservation purposes that is determined under this section to have a fair market value of $60,000. The amount of basis allocable to the easement is $15,000 ($60,000/$80,000 = $15,000/$20,000). Accordingly, the basis of the property is reduced to $5,000 ($20,000 minus $15,000).

Example (10). E owns 10 one-acre lots that are currently woods and parkland. The fair market value of each of E's lots is $15,000 and the basis of each lot is $3,000. E grants to the county a perpetual easement for conservation purposes to use and maintain eight of the acres as a public park and to restrict any future development on those eight acres. As a result of the restrictions, the value of the eight acres is reduced to $1,000 an acre. However, by perpetually restricting development on this portion of the land, E has ensured that the two remaining acres will always be bordered by parkland, thus increasing their fair market value to $22,500 each. If the eight acres represented all of E's land, the fair market value of the easement would be $112,000, an amount equal to the fair market value of the land before the granting of the easement (8 × $15,000 = $120,000) minus the fair market value of the encumbered land after the granting of the easement (8 × $1,000 = $8,000). However, because the easement only covered a portion of the taxpayer's contiguous land, the amount of the deduction under section 170 is reduced to $97,000 ($150,000 – $53,000), that is, the difference between the fair market value of the entire tract of land before ($150,000) and after (8 × $1,000) + (2 × $22,500)) the granting of the easement.

Example (11). Assume the same facts as in *example (10)*. Since the easement covers a portion of E's land, only the basis of that portion is adjusted. Therefore, the amount of basis allocable to the easement is $22,400 ((8 × $3,000) × ($112,000 $120,000)). Accordingly, the basis of the eight acres encumbered by the easement is reduced to $1,600 ($24,000 – $22,400), or $200 for each acre. The basis of the two remaining acres is not affected by the donation.

Example (12). F owns and uses as professional offices a two-story building that lies within a registered historic district. F's building is an outstanding example of period architecture with a fair market value of $125,000. Restricted to its current use, which is the highest and best use of the property without making changes to the facade, the building and lot would have a fair market value of $100,000, of which $80,000 would be allocable to the building and $20,000 would be allocable to the lot. F's basis in the property is $50,000, of which $40,000 is allocable to the building and $10,000 is allocable to the lot. F's neighborhood is a mix of residential and commercial uses, and it is possible that F (or another owner) could enlarge the building for more extensive commercial use, which is its highest and bes use. However, this would require changes to the facade. F would like to donate to a qualifying preservation organization an easement restricting any changes to the facade and promising to maintain the facade in perpetuity. The donation would qualify for a deduction under this section. The fair market value of the easement is $25,000 (the fair market value of the property before the easement, $125,000, minus the fair market value of the property after the easement, $100,000). Pursuant to §1.170A-14 (h)(3)(iii), the basis allocable to the easement is $10,000 and the basis of the underlying property (building and lot) is reduced to $40,000.

(i) *Substantiation requirement.* If a taxpayer makes a qualified conservation contribution and claims a deduction, the taxpayer must maintain written records of the fair market value of the underlying property before and after the donation and the conservation purpose furthered by the donation and such information shall be stated in the taxpayer's income tax return if required by the return or its instructions. See also §1.170A-13T(c) (relating to substantiation requirements for deductions in excess of $5,000 for charitable contributions made after 1984), and section 6659 (relating to additions to tax in the case of valuation overstatements).

(j) *Effective date*. Except as otherwise provided in §1.170A-14(g)(4)(ii), this section applies only to contributions made on or after December 18, 1980.

PART 20—[AMENDED]

Par. 5. The authority for Part 20 continues to read in part:

26 U.S.C. 7805. * * *

Par. 6. Paragraph (e)(2) of §20.2055-2 is amended as follows:

a. The sixth sentence of paragraph (e)(2)(i) is revised to read: "However, except as provided in paragraphs (e)(2)(ii), (iii), and (iv) of this section, for purposes of this subdivision a charitable contribution of an interest in property not in trust where the decedent transfers some specific rights to one party and transfers other substantial rights to another party will not be considered a contribution of an undivided portion of the decedent's entire interest in property".

b. The seventh sentence of paragraph (e)(2)(i) is revised to read: "A bequest to charity made on or before December 17, 1960, of an open space easement in gross in perpetuity shall be considered the transfer to charity of an undivided portion of the decedent's entire interest in the property".

c. Paragraphs (e)(2)(iv), (e)(2)(v), a (e)(2)(vi) are redesignated (e)(2)(v), (e)(2)(vi), and (e)(2)(vii), respectively.

d. A new paragraph (e)(2)(iv) is inserted after paragraph (e)(2)(iii) to read as set forth below.

§20.2055-2 Transfers not exclusively for charitable purposes.

* * * * *

(e) *Limitations applicable to decedents dying after December 31, 1969.* * **

(2) *Deductible interests.* * **

(iv) *Qualified conservation contribution.* The charitable interest is a qualified conservation contribution. For the definition of a qualified conservation contribution, see §1.170A-14.

Part 25—[AMENDED]

Par. 7. The authority for Part 25 continues to read in part:

26 U.S.C. 7805. * * *

Par. 8. Paragraph (c)(2) of §25.2522(c)-3 is amended as follows:

a. The sixth sentence of paragraph (c)(2)(i) is revised to read: "However, except as provided in paragraphs (e)(2)(ii), (iii), and (iv) of this section, for purposes of this subdivision a charitable contribution of an interest in property not in trust where the decedent transfers some specific rights to one party and transfers other substantial rights to another party will not be considered a contribution of an undivided portion of the decent's entire interest in property".

b. The eighth sentence of paragraph (c)(2)(i) is revised to read: "A gift to charity made on or before December 17, 1980, of an open space easement in gross in perpetuity shall be considered the transfer to charity of an undivided portion of the donor's entire interest in property.".

c. Paragraphs (c)(2)(iv), (c)(2)(v), and (c)(2)(vi) are redesignated (c)(2)(v), (c)(2)(vi), and (c)(2)(vii), respectively.

d. A new paragraph (c)(2)(iv) is inserted after paragraph (c)(2)(iii), to read as set forth below.

§25.2522(c)-3 Transfers not exclusively for charitable, etc., purposes in the case of gifts made after July 31, 1969.

* * * * *

(c) *Transfers of partial interest in property.* * **

(2) *Deductible interest.* * **

(iv) *Qualified conservation contribution.* The charitable interest is a qualified conservation contribution. For the definition of a qualified conservation contribution, see §1.170A-14.

* * * * *

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 9. The authority for Part 602 continues to read in part:

26 U.S.C. 7805. * * *

Par. 10. Section 602.101(c) is amended by inserting in the appropriate place in the table "§1.170A-14 . . . 1545–0763."

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved December 20, 1985
RONALD A. PEARLMAN,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on January 13, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 14, 1986, 51 F.R. 1496, and corrected in the issue of the Federal Register for February 13, 1986, 51 F.R. 5322)

Section 312.—Effect on Earnings and Profits

26 CFR 1.312-8: Effect on earnings and profits of receipt of tax-free distributions requiring adjustment of basis of stock.

For purposes of calculating the limitation on Subpart F income under section 952(c) of the Code, a CFC that receives a dividend distribution from another CFC within the same chain of ownership is required to increase its earnings and profits. See Rev. Rul. 86-33, page 17.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of March 1986. See Rev. Rul. 86-34, page 20.

Section 483.—Interest on Certain Deferred Payments

Federal short-term, mid-term and long-term rates are set forth for the month of March 1986. See Rev. Rul. 86-34, page 20.

Section 673. Reversionary Interests

26 CFR 1.673(a)-1: Reversionary interests; income payable to beneficiaries other than certain charitable organizations; general rule.

Trusts; reversionery interests; determination of life expectancy. Actuarial tables are adopted for determining life expectancy for purposes of section 673 of the Code for transfers to a trust occuring after November 30, 1983.

Rev. Rul. 86-32

ISSUE

For transfers occurring after November 30, 1983, to a trust that reverts to the grantor upon a person's death, what are the appropriate actuarial tables to determine whether a portion of the trust will revert within ten years for purposes of section 673(a) of the Internal Revenue Code?

FACTS

On December 1,1984, the date of *A*'s 73rd birthday, *A* transferred certain property to an irrevocable trust. The trust instrument directs the trustee to pay the income of the trust to other persons during the life of *A* and, on the death of *A*, to distribute the corpus of the trust to *A*'s estate.

LAW AND ANALYSIS

Section 673(a) of the Code provides that the grantor shall be treated as the owner of any portion of a trust in which the grantor has a reversionary interest in either the corpus or the income therefrom if, as of the inception of that portion of the trust, the interest will or may reasonably be expected to take effect in possession or enjoyment within

10 years commencing with the date of the transfer of that portion of the trust.

Section 1.673(a)-1(c) of the Income Tax Regulations provides that if the reversionary interest in any portion of a trust is to take effect on or after the death of the grantor (or any person other than the person to whom the income is payable), the trantor is treated under section 673(a) of the Code as the owner of that portion if the life expectancy of the grantor (or the person other than the person to whom the income is payable) is less than 10 years on the date of transfer of the portion. The grantor is not treated as the owner if the life expectancy of the measuring life is 10 years or longer.

For transfers occurring after November 30, 1983, the appropriate actuarial table is determining life expectancy is Table 1 of United States Life Tables: 1969-1971, published by the Department of Health, Education, and Welfare, Public Health Service. *See*, T.D. 7955, 1984-1 C.B. 40, which revises actuarial tables used for valuation purposes in various regulations. Table 1 of United States Life Tables was used to derive the actuarial tables in T.D. 7955. Table 1 eliminates the distinction between male and female mortality and is, thus, gender neutral.

Column (7) of Table 1 states the life expectancy of persons of given ages. At age 73, a person has a life expectancy of 10.34 years. At the age of 74, life expectancy is 9.82 years. To apply the table, the age of the measuring life should be taken at the person's age at the birthday nearest to the date of the transfer. For example, a grantor 73 years and six months old or more on the date of a transfer to a trust has a life expectancy of no more than 9.82 years as of the date of transfer.

On December 1, 1984, the date of the transfer of property to the trust, *A* has a life expectancy of 10 years or more (10.34 years). Accordingly, *A* is not treated, under section 673(a) of the Code, as the owner of the corpus of the trust that will revert to *A*'s estate upon *A*'s death.

HOLDING

For transfers occurring after November 30, 1983, Table 1 of United States Life Tables: 1969-1971 is the appropriate actuarial table to determine whether a portion of a trust that reverts to the grantor upon a person's death will revert within ten years for purposes of section 673(a) of the Code.

EFFECTIVE DATE

The revenue ruling is effective for transfers occurring after November 30, 1983, which is the general effective date of T.D. 7955.

For transfers occurring after December 31, 1970, and on or before November 30, 1983, see Rev. Rul. 73-251, 1973-1 C.B. 324. For transfers occurring on or before December 31, 1970, see Rev. Rul. 58-567, 1958-2 C.B. 365.

Section 701.—Partners, Not Partnership, Subject To Tax

26 CFR 1.701-1: Partners, not partnerships, subject to tax.

The Service will now entertain ruling requests concerning certain partnership issues in areas in which the Service has heretofore declined to rule. See Rev. Proc. 86-12, page 21.

Section 951.—Amounts Included in Gross Income of United States Shareholders

26 CFR 1.951-1: Amounts included in gross income of United States shareholders.

For purposes of calculating the limitation on Subpart F income under section 952(c) of the Code, a CFC that receives a dividend distribution from another CFC within the same chain of ownership is required to increase its earnings and profits. See Rev. Rul. 86-33, below.

Section 952.—Subpart F Income Defined

26 CFR 1.952-1: Subpart F income defined. (Also Sections 312, 951, 954, 958, 964; 1.312-1, 1.951-1, 1.954-1, 1.958-1, 1.964-1.)

Controlled foreign corporations; Subpart F income; dividend distribution within same chain of foreign corporations. For purposes of calculating the limitation on subpart F income under section 952(c) of the Code, a controlled foreign corporation (CFC) that receives a dividend distribution from another CFC within the same chain of ownership is required to increase its earnings and profits for the tax year by the amount of the distribution.

Rev. Rul. 86-33

ISSUE

If a controlled foreign corporation (CFC) receives a dividend distribution from another CFC within the same chain of foreign corporations, is the recipient CFC required to increase its earnings and profits for the tax year by the amount of the distribution for purposes of calculating the limitation on subpart F income under section 952(c) of the Internal Revenue Code?

FACTS

Z, a domestic corporation, wholly owns *P*, a foreign corporation. *P* is principally a holding company and wholly owns two foreign corporations, *S-1* and *S-2*. *S-1* and *S-2* are engaged in foreign commerce through shipping operations. *P*, *S-1*, and *S-2* are CFCs within the meaning of section 957(a) of the Code for the entire 1984 calendar year. For purposes of section 952(d), *P*, *S-1*, and *S-2* form a "chain of foreign corporations," as described in section 1.952-1(d)(2)(ii) of the Income Tax Regulations, because *P* is owned directly by *Z* and *S-1* and *S-2* are considered as being owned by *Z* under section 958(a). Such a chain is also called a "chain of ownership."

For the year 1984, *P* has foreign personnel holding company income (FPHCI), as defined in section 954(c) of the Code, consisting of interest and dividends of 5*x* dollars and has foreign base company shipping income (FBCSI), as defined in section 945(f), of 2*x* dollars. During 1985 *S-1* has FBCSI of 8*x* dollars, and *S-2* has an operating loss of 40*x* dollars. *S-1*'s pre-1984 accumulated earnings and profits (all of which are attributable to FBCSI) are 100*x* dollars, and, because of the application of section 954(b)(2), this amount has not been previously taxed. Similarly, by application of section 954(b)(2), *S-1*'s FBCSI of 8*x* dollars and *P*'s FBCSI of 2*x* dollars will be excluded from FBCSI.

Prior to the end of 1984, *S-1* distributed all of its current and accumulated earnings and profits (108*x* dollars) to *P*. For 1984, *Z* elected to include *P* and *S-1* in a "related group" pursuant to section 955(b)(2) of the Code and section 1.955A-3 of the regulations. Pursuant to section 1.955A-3(c)(1), because the dividend that *P* received from *S-1* is attributable entirely to FBCSI, *P* excluded that dividend from *P*'s gross income for purposes of determining *P*'s foreign base company income within the meaning of section 954.

LAW AND ANALYSIS

Section 951(a)(1)(A)(i) of the Code provides that if a foreign corporation is a CFC for an uninterrupted period of 30 days or more during any tax year of the corporation, a United States shareholder that owns stock in the corporation on the last day which is in the year and on which the corporation is a CFC shall include in gross income, for the United States shareholder's tax year in which or with which the tax year of the corporation ends, the shareholder's pro rata share of the corporation's subpart F income. The types of income that comprise subpart F income are described in sections 952 through 954. Subpart F income includes foreign base company income, which in turn includes FPHCI and FBCSI.

Section 952(c) of the Code provides generally that the subpart F income of any CFC for any tax year shall not exceed the earnings and profits of such corporation for such year reduced by an amount that reflects the deficits in earnings and profits for prior years.

With respect to section 952(c) of the Code, section 1.952-1(c) of the regulations provides as follows:

> (1) *In general.* A United States shareholder's pro rata share of a controlled foreign corporation's subpart F income for any tax year shall not exceed such shareholder's pro rata share of the earnings and profits (as defined in section 964(a) and §1.964-1) of such corporation for such tax year, computed as of the close of such tax year without diminution by reason of any distributions made during such tax year, minus the sum of—
>
> (i) The amount, if any, by which such shareholder's pro rata share of—
>
> (a) The sum of such corporation's deficits in earnings and profits for prior tax years beginning after December 31, 1962, plus
>
> (b) The sum of such corporation's deficits in earnings and profits for tax years beginning after December 31, 1959, and before January 1, 1963 (reduced by the sum of the earnings and profits (as so defined) of such corporation for any of such tax years) exceeds
>
> (c) The sum of such corporation's earnings and profits for prior tax years beginning after December 31, 1962, which, with respect to such shareholder, are allocated to other earnings and profits under section 959(c)(3) and §1.959-3; and
>
> (ii) Such shareholder's pro rata share of any deficits in earnings and profits of other foreign corporations for a tax year beginning after December 31, 1962, which are attributable to stock of such other foreign corporations owned by such shareholder within the meaning of section 958(a) and which, in accordance with section 952(d) of [§1.952-1(d)], are taken into account as a reduction in the controlled foreign corporation's earnings and profits for such tax year.
>
> For purposes of applying [§1.952-1(c)(1)], the reduction (if any) provided by [§1.952-1(c)(1)(i)] in a United States shareholder's pro rata share of the earnings and profits of a controlled foreign corporation shall be taken into account before the reduction provided by [§1.952-1(c)(1)(ii)]. See section 952(c).

Section 952(d) of the Code provides a special rule for the reduction of earnings and profits in the case of indirect ownership.

With respect to section 952(d) of the Code, section 1.952-1(d) of the regulations provides as follows:

> (1) *In general.* For purposes of [§1.952-1(c)(1)(ii)], if—
>
> (i) A United States shareholder owns (within the meaning of section 958(a)) stock in two or more foreign corporations in a chain of foreign corporations (as defined in [§1.952-1(d)(2)(ii)]), and
>
> (ii) Any of the corporations in such chain has a deficit in earnings and profits for a tax year beginning after December 31, 1962,
>
> then, with respect to such shareholder and only for purposes of determining the limitation on subpart F income under [§1.952-1(c)], the earnings and profits for the tax year of each such foreign corporation which is a controlled foreign corporation shall, in accordance with the rules of [§1.952-1(d)(2)], be reduced to take into account any deficit in earnings and profits referred to in [§1.952-1(d)(2)(ii)]. See section 952(d).
>
> (2) *Special rules.* For purposes of this paragraph—
>
> . . .
>
> (ii) "Chain" defined. A chain of foreign corporations shall, with respect to the United States shareholder, include—
>
> (a) Any foreign corporation in which such shareholder owns (within the meaning of section 958(a)(1)(A)) stock, but only to the extent of the stock so owned, and
>
> (b) All foreign corporations in which such shareholder owns (within the meaning of section 958(a)(2)) stock, but only to the extent of the stock so owned by reason of such shareholder's ownership of the stock referred to in [§1.952-1(d)(2)(ii)(a)].
>
> (iii) Allocation of deficit. If one or more foreign corporations (whether or not a controlled foreign corporation) includible in a chain of foreign corporations has a deficit in earnings and profits (determined under section 964(a) and §1.964-1) for the tax year, the amount of deficit taken into account under section 952(d) with respect to a United States shareholder in such chain as a reduction in earnings and profits for the tax year of a controlled foreign corporation includible in such chain shall be an amount which bears the same ratio to such shareholder's pro rata share of the total deficit in earnings and profits for the tax year of all includible foreign corporations as such shareholder's pro rata share of the earnings and profits (determined under [§1.952-1(c)] but without regard to the provisions of §[1.952-1(c)(1)(ii)]) for the tax year of such includible controlled foreign corporation bears to such shareholder's pro rata share of the total earnings and profits (as so determined under [§1.952-1(c)]) for the tax year of all includible controlled foreign corporations. The amount of deficit taken into account under [§1.952-1(d)(2)(iii)] with respect to any controlled foreign corporation includible in a chain of foreign corporations shall not exceed the United States shareholder's pro rata share of the controlled foreign corporation's earnings and profits for the tax year.

The rule in the paragraph quoted immediately above is sometimes called the "chain deficit rule."

Section 958(a)(1) of the Code provides that, as a general rule, "stock owned" means stock owned directly and stock owned by applying section 958(a)(2). Section 958(a)(2) provides that stock owned, directly or indirectly, by or for a foreign corporation is considered as being owned proportionately by its shareholders. Stock considered to be owned by a person by reason of the application of section 958(a)(2) is, for purposes of applying that section, treated as actually owned by such person.

Section 964(a) of the Code provides that, except as provided in section 312(k)(4), for purposes of subpart F the earnings and profits of any foreign corporation, and the deficit in earnings and profits of any foreign corporation, for any taxable year, shall be determined according to rules substantially similar to those applicable to domestic corporations, under regulations prescribed by the Secretary.

Section 1.964-1(a) of the regulations provides that for purposes of section 951 through 964, the earnings and profits (or deficit in earnings and profits) of a foreign corporation for its tax year shall be computed substantially as if such corporation were a domestic corporation.

Section 312(f)(2) of the Code provides that where a corporation receives a distribution from a second corporation which (under the law applicable to the year in which the distribution was made) was not a taxable dividend to the shareholders of the second corporation, the amount of such distribution shall not increase the earnings and profits of the first corporation in the following two circumstances. First, there is no increase in respect of the part of such distribution which (under the law) is directly applied in reduction of the basis of the stock in respect of which the distribution was made. Second, there is no increase if (under such law) the distribution causes the basis of the stock in respect of which the distribution was made to be allocated between such stock and the property received.

As noted above, section 1.952-1(c)(1) of the regulations provides that a United States shareholder's pro rata share of a CFC's subpart F income for any tax year shall not exceed the shareholder's pro rata share of the earnings and profits, as defined in section 964(a) of the Code and section 1.964-1, of such corporation for such tax year, computed as of the close of such tax year without diminution by reason of any distributions made during such tax year. Section 964(a) and section 1.964-1(a) provide the general rule that the earnings and profits of a foreign corporation shall be computed substantially as if such corporation were a domestic corporation. A domestic corporation's earnings and profits for any tax year include the amount of any distributions received from its subsidiaries. The fact that the dividend distribution is not taxed to the recipient corporation does not preclude the distribution from increasing the recipient's earnings and profits except in situations that are described in section 312(f)(2) and that require an adjustment or allocation of basis. There is no indication in the instant case that the distribution from *S-1* to *P* will be directly applied to reduce *P*'s basis in the *S-1* stock, and thus section 312(f)(2) is not applicable.

Examples 2 and 3 under section 1.952-1(d)(3) of the regulations illustrate how the earnings and profits of a CFC for the tax year are computed under the chain deficit rule. These examples state that the earnings and profits are determined "without regard to distributions" for the tax year.

In these examples, the phrase "without regard to distributions" refers to distributions of a dividend in the tax year by the CFC whose earnings and profits are at issue and not to distributions received by that CFC. The phrase "without regard to distributions" in these examples simply reflects the fact that dividend distributions made by a CFC for the tax year do not affect the CFC's earnings and profits for that tax year for purposes of the limitation in section 952(c) on subpart F income. Section 1.952-1(c)(1) of the regulations. Also, section 316(a)(2) of the Code provides that a dividend is any distribution of property made by a corporation to its shareholders out of its earnings and profits for the tax year (computed as of the close of the tax year without diminution by reason of any distributions made during the tax year), without regard to the amount of the earnings and profits at the time the distribution was made. See also section 1.952-1(c)(3), example (1)(d), which illustrates that in determining the subpart F income limitation under section 952(c), the earnings and profits of a CFC for the tax year include dividend distributions received by the CFC during the tax year from another CFC within the same chain of ownership. Example 1(d) indicates that although the earnings and profits of a CFC for the tax year are determined "without diminution for any distributions made during such year," the earnings and profits of the CFC, nevertheless, are increased by dividends received from another CFC within the same chain of ownership during the year.

Accordingly, the dividend distribution received by *P* from *S-1* in 1984 increases *P*'s earnings and profits for 1984 by the amount of the dividend (108*x* dollars), and the chain deficit rule of section 952(d) of the Code applies only after *P*'s earnings and profits for 1984 are increased to reflect the dividend *P* received from *S-1* in that year. Pursuant to the chain deficit rule, *P*'s earnings and profits are reduced by the amount of *S-2*'s deficit in earnings and profits for the year (40*x* dollars). After the reduction, *P* has sufficient earnings and profits so that the 5*x* dollars of FPHCI are subpart F income includible in the 1984 gross income of Z.

HOLDING

For purposes of calculating the limitation on subpart F income under section 952(c) of the Code, a CFC that receives a dividend distribution from another CFC within the same chain of ownership is required to increase its earnings and profits. The earnings and profits are to be increased for the tax year in which the dividend is received and are to be increased by the amount of the dividend distribution.

Section 954.—Foreign Base Company Income

26 CFR 1.954-1: Foreign base company income; taxable years beginning after December 31, 1975.

For purposes of calculating the limitation on Subpart F income under section 952(c) of the Code, a CFC that receives a dividend distribution from another CFC within the same chain of ownership is required to increase its earnings and profits. See Rev. Rul. 86-33, page 17.

Section 958.—Rules for Determining Stock Ownership

26 CFR 1.958-1: Direct and indirect ownership of stock.

For purposes of calculating the limitation on Subpart F income under section 952(c) of the Code, a CFC that receives a dividend distribution from another CFC within the same chain of ownership is required to increase its earnings and profits. See Rev. Rul. 86-33, page 17.

Section 964.—Miscellaneous Provisions

26 CFR 1.964-1: Determination of the earnings and profits of a foreign corporation.

For purposes of calculating the limitation on Subpart F income under section 952(c) of the Code, a CFC that receives a dividend distribution from aonther CFC within the same chain of ownership is required to increase its earnings and profits. See Rev. Rul. 86-33, page 17.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 467, 483.)

Rev. Rul. 86-34

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of March 1986 are as follows:

	Period for Compounding			
	Annual	Semiannual	Quarterly	Monthly
Short-Term				
AFR	8.06%	7.90%	7.82%	7.77%
110% AFR	8.88%	8.69%	8.60%	8.54%
120% AFR	9.70%	9.48%	9.37%	9.30%
Mid-Term				
AFR	8.92%	8.73%	8.64%	8.58%
110% AFR	9.83%	9.60%	9.49%	9.41%
120% AFR	10.75%	10.48%	10.35%	10.26%
Long-Term				
AFR	9.55%	9.33%	9.22%	9.15%
110% AFR	10.52%	10.26%	10.13%	10.05%
120% AFR	11.51%	11.20%	11.05%	10.95%

Section 2055.—Transfer for Public, Charitable, and Religious Uses

26 CFR 20.2055-2: Transfers not exclusively for charitable purposes.

Deduction for qualified conservation contributions. See T.D. 8069, page 4.

Section 2522.—Charitable and Similar Gifts

26 CFR 25.2522(c)-3: Transfers not exclusively for charitable, etc., purposes in the case of gifts made after July 31, 1969.

Deduction for qualified conservation contributions. See T.D. 8069, page 4.

Section 7701.—Definitions

26 CFR 301.7701-3: Partnerships.

The Service will now entertain ruling requests concerning certain partnership issues in areas in which the Service has heretofore declined to rule. See Rev. Proc. 86-12, page 21.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.201: Rulings and determination letters.
(Also Part I, Sections 701, 7701; 1.701-1, 301.7701-3.)

Rev. Proc. 86-12

SECTION 1. PURPOSE

The purpose of this revenue procedure is to provide guidance to taxpayers concerning the preparation of ruling requests involving certain partnership issues.

SEC. 2. BACKGROUND

Subchapter K of the Internal Revenue Code, sections 701 through 761, sets forth the rules concerning the federal income tax treatment of partners and partnerships. Section 7701(a)(2) of the Code defines the term "partnership," and section 301.7701-2 and 301.7701-3 of the Procedure and Administration Regulations set forth the standards that must be satisfied for an organization to be classified as a partnership.

The Internal Revenue Service recently has reviewed its practice concerning the issuance of letter rulings on partnership issues arising under subchapter K of the Code and partnership classification issues arising under sections 301.7701-2 and 301.7701-3 of the regulations. As a result of this review, the Service has determined that it will expand the scope of its rulings program with regard to these issues.

SEC. 3. SCOPE AND OBJECTIVE

.01 The Service presently considers ruling requests submitted by a newly formed organization concerning the classification of the organization as a partnership for federal income tax purposes and, if the organization is so classified, the Service also presently considers any partnership issues arising under subchapter K. If, however, the newly formed organization does not request a partnership classification ruling, but requests rulings only on partnership issues arising under subchapter K, the general practice of the Service has been not to rule in such circumstances.

The Service will now consider a ruling request concerning issues arising under subchapter K provided the newly formed organization declares in its ruling request that it is properly classified as a partnership for federal income tax purposes and that it will file federal income tax returns in a manner consistent with that declaration. When the Service issues a ruling concerning issues arising under subchapter K but does not issue a partnership classification ruling, the ruling will contain a proviso that no opinion is expressed concerning the organization's classification for federal income tax purposes.

.02 The Service presently considers ruling requests submitted by an existing organization (an organization that was formed in, and has filed a tax return for, a taxable year before the taxable year in which the ruling request is filed) concerning partnership issues arising under subchapter K, provided that the organization declares in its ruling request (1) that it is properly classified as a partnership for federal income tax purposes, (2) that it has, for prior taxable years, filed federal income tax returns in a manner consistent with that declaration, and (3) that it will continue so to file its federal income tax returns. When the Service issues a ruling to an existing organization concerning issues arising under subchapter K but has not previously issued a partnership classification ruling to the organization, the ruling contains a proviso that no opinion is expressed concerning the organization's classification for federal income tax purposes. The general practice of the Service has been not to issue partnership classification rulings to existing organizations. *See* Rev. Proc. 86-1, section 5.01, 1986-1 I.R.B. 6, 8-9.

The Service will now consider ruling requests concerning the classification of an existing organization as a partnership. A ruling issued in response to such a request will be effective prospectively.

SEC. 4. AREAS NOT COVERED BY THIS REVENUE PROCEDURE

This revenue procedure is not intended to modify Rev. Proc. 86-3, 1986-1 I.R.B. 26, which sets forth a list of matters upon which the Service generally will decline to rule. Furthermore, this revenue procedure is not intended to modify any part of Rev. Proc. 86-1, other than the next to the last sentence of section 5.01.

SEC. 5. INQUIRIES

Inquiries concerning this revenue procedure should be addressed to the Internal Revenue Service, Associate Chief Council (Technical), Attention CC:IND:I, Room 5016, 1111 Constitution Avenue, N.W., Washington, D.C. 20224.

SEC. 6. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 86-1 is modified.

SEC. 7. EFFECTIVE DATE

This revenue procedure applies to requests for rulings filed in the National Office after March 3, 1986.

Employee Plans Not Timely Amended—7805(b) Relief

Notice 86-3

The Internal Revenue Service has established procedures for granting partial relief from the sanctions for failure to satisfy the requirements of section 401(a) of the Internal Revenue Code in the case of certain employee plans that were not timely amended to comply with the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), Pub. L. 97-248, including the requirements listed in Notice 85-14, 1985-33 I.R.B. 16; the Tax Reform Act of 1984 (TRA), Pub. L. 98-369; or the Retirement Equity Act of 1984 (REA), Pub. L. 98-397.

ELIGIBILITY

These procedures will apply only to a plan for which the employer (1) was entitled, until the applicable compliance date by which the plan had to be amended to comply with TEFRA, TRA or REA, to rely for plan qualification purposes on a favorble determination letter; (2) had, on or before March 19, 1984, adopted a master or prototype plan for which a favorable post-ERISA opinion letter had been issued (that is, an opinion letter issued after the Employee Retirement Income Security Act of 1974 (ERISA) became effective with respect to the plan); and (3) had adopted, after March 19, 1984, a master or prototype plan for which a favorable post-ERISA opinion letter had been issued, provided that such master or prototype plan does not replace another plan or, if it does replace another plan, the plan replaced is one to which this notice applies. The procedures will apply where such plans were not amended to comply with TEFRA, TRA or REA (and for which determination letters, as necessary for reliance, were not requested) by the applicable compliance date.

Failure to comply with TEFRA, TRA or REA by the applicable compliance date results in a plan not being a qualified plan under section 401(a) of the Code for the plan year during which any such qualification requirement became effective for that plan. The compliance date for an individually designed plan (or a master or prototype plan first adopted by an employer after March 19, 1984, for which a determination letter was required for reliance but was not issued) is the last day of the plan year in which the qualification requirement becomes effective for that plan, except that, in the case of a "disqualifying provision" as defined in section 1.401(b)-1(b) of the Income Tax Regulations, the compliance date is the last day of the remedial amendment period as defined in section 1.401(b)-1(c). See Notice 85-5, 1985-1 C.B. 427; Notice 85-14, 1985-33 I.R.B. 16, and Announcement 85-128, 1985-35 I.R.B. 44. News Release IR-85-89, dated August 30, 1985, extended until November 1, 1985, the time for complying with the requirements of TEFRA, TRA and REA applicable to pension, profit-sharing, stock bonus, and annuity plans. This extension of time applied to all such plans whose compliance date was before November 1, 1985. The compliance date for a master or prototype plan adopted by an employer on or before March 19, 1984, to which the relief described in these procedures applies, is determined in accordance with section 12 of Rev. Proc. 84-23, 1984-1 C.B. 457.

CONDITIONS FOR GRANTING RELIEF

An employer who has a plan to which these procedures are applicable may obtain relief by executing the necessary plan amendments to comply retroactively with TEFRA, TRA and REA as of their respective effective dates and by taking appropriate action to adjust employees' rights and/or benefits so that such rights and/or benefits correspond to what they would have been had the plan or plans been amended timely. To take advantage of this procedure, the plan administrator must make the necessary amendments and request a determination letter with respect thereto no later than the last day of the eleventh month beginning after the applicable compliance date, if such date fell in November or December 1985; the last day of the tenth month beginning after the applicable compliance date, if such date fell in January or February 1986; or the last day of the ninth month beginning after the applicable compliance date, if such date fell in March 1986 or a later month.

If the plan administrator takes these actions, relief generally will be granted to the extent described below.

SCOPE OF RELIEF

The relief provided for in these procedures will have the following effects: (1) plan participants other than key employees, as defined below, will be treated in all respects, including the tax treatment of distributions and employee contributions, as though they were participants in a qualified plan during the entire noncompliance period as defined below; (2) the plan's assets and the income earned by such assets, including any amounts allocable to key employees that are not actually distributed to them but made available to them and otherwise taxable under section 72 of the Code pursuant to section 402(b), will continue to be treated as assets of a qualified plan during the noncompliance period; (3) if employer contributions are made in a taxable year which ends within or with a taxable year of the plan's trust for which the trust is not exempt under section 501(a) because of a failure to comply with TEFRA, TRA or REA, the allowable deduction for such contributions may be greater than the amount otherwise allowable under section 404(a)(5) for contributions made to a nonqualified plan; and (4) the amounts attributable to contributions in (3) above that are includible in the key employees' gross incomes may be less than the amounts otherwise includible.

The term "key employee" for purposes of these procedures has the same meaning as in section 416(i)(1) of the Code, but with the words "or any of the 4 preceding years" omitted and with "plan year" replaced by "noncompliance period." The term "noncompliance period" in this context means the period of plan years for which the plan failed to meet any of the qualification requirements of TEFRA, TRA or REA.

If relief is granted under these procedures, the allowable deduction under section 404(a) of the Code for employer contributions will be equal to the following amount, if greater than the amount otherwise allowable as a deduction under section 404(a)(5): the product of the "number-of-months factor" (defined below) multiplied by the lesser of (a) the amount contributed by the employer, or (b) the limitation under section 404(a)(1), (2), (3) or (9) that would apply if the plan were qualified.

The "number-of-months factor" is a percentage that is based on the number of months that have ended after the applicable compliance date and before the date a determination letter is requested for the required retroactive amendments, and is determined by reference to the following table:

NUMBER-OF-MONTHS FACTOR (%)

Month in which compliance date falls	Number of months that have ended after the compliance date and before the date of submission 1	2	3	4	5	6	7	8	9	10	11
Nov. 1985	95	90	85	80	70	60	50	40	30	20	10
Dec. 1985	95	90	85	75	65	55	45	35	25	15	5
Jan. 1986	95	90	80	70	60	50	40	30	20	10	
Feb. 1986	95	85	75	65	55	45	35	25	15	5	
Mar. 1986 or later	90	80	70	60	50	40	30	20	10		

In applying the number-of-months factor, the deductible amount is determined separately with respect to each taxable year of the employer affected

by the failure to timely amend the plan. Thus, the case of plans not timely amended to comply with TEFRA, TRA or REA, a separate product must be determined for each taxable year of the employer for which the plan is not qualified.

The following examples illustrate how the allowable deduction would be determined:

Example (1)

An employer whose taxable year is the calendar year contributed $120,000 in 1984 and $110,000 in 1985 to its employees' defined benefit plan for the plan and trust years 1984 and 1985, which are calendar years. The plan was not amended by the applicable compliance date, which was Nov. 1, 1985, to meet the qualification requirements under TEFRA that applied to it. The deductibility limitation under section 404(a)(1) of the Code that would have applied if the plan had not become disqualified is $100,000 for 1984 and $115,000 for 1985.

On Jan. 15, 1986, the employer requested a determination letter with respect to a proposed amendment.

Since two months have ended after the Nov. 1, 1985 compliance date and before the date of submission of the determination letter request, the number-of-months factor, from the above table, is 90 percent.

The amount deductible by the employer for 1984, if relief is granted, is $90,000, determined as follows:

(1) Limitation for 1984 under section 404(a)(1) of the Code if plan were qualified	$100,000
(2) Employer's contribution for 1984	$120,000
(3) Lesser of (1) or (2)	$100,000
(4) Number-of-months factor	90%
(5) (4) × (3)	$90,000
(6) Amount includible in participating employees' gross income under section 402(b) for 1984 and deductible by employer under section 404(a)(5), if relief is not granted	$0
(7) Amount deductible if relief is granted: greater of (5) or (6)	$90,000

The amount deductible for 1985 is $99,000, determined as follows:

(1) Limitation for 1985 under section 404(a)(1) if plan were qualified	$115,000
(2) Employer's contribution for 1985	$110,000
(3) Lesser of (1) or (2)	$110,000
(4) Number-of-months factor	90%
(5) (4) × (3)	$99,000
(6) Amount includible in participating employees' gross income under section 402(b) for 1985 and deductible by employer under section 404(a)(5), if relief is not granted	$0
(7) Amount deductible if relief is granted: greater of (5) or (6)	$99,000

The $30,000 for 1984 and $11,000 for 1985 are not deductible under section 404(a) of the Code for 1984 or 1985 and are treated as contributions to a nonqualified plan.

The results would be the same if the employer had executed the plan amendment just prior to submission to the Service of a determination letter request.

Example (2)

In 1985 an employer whose taxable year is a calendar year contributed $120,000 to its employees' profit-sharing plan for the plan and trust year ending Jan. 31, 1986. The plan had been timely amended to comply with TEFRA but was not amended by the applicable compliance date, which was Jan. 31, 1986, to meet the qualification requirements that applied to it under TRA and REA. The deductibility limitation under section 404(a)(3) of the Code that would have applied for 1985 if the plan had not become disqualified is $150,000. The amount that would be allowable as a deduction under section 404(a)(5) for 1985 as a contribution to a nonqualified plan is $120,000. Of the $120,000 amount, $100,000 is attributable to key employees and would, absent relief, be includible in the income of such employees.

The employer subsequently amends the plan to meet all of the applicable qualification requirements under TRA and REA, and also appropriately adjusts employees' and beneficiaries' rights and benefits. On Nov. 9, 1986, the employer requests a determination letter with respect to the amendment.

Since nine months have ended after the Jan. 31, 1986 compliance date and before the date of submission of the determination letter request, the number-of-months factor, from the above table, is 20 percent.

The amount deductible by the employer for 1985, if relief is granted, is $120,000, determined as follows:

(1) Limitation under section 404(a)(3) if plan were qualified	$150,000
(2) Employer's contribution	$120,000
(3) Lesser of (1) or (2)	$120,000
(4) Number-of-months factor	20%
(5) (4) × (3)	$24,000
(6) Amount includible in participating employees' gross income under section 402(b) and deductible by employer under section 404(a)(5), if relief is not granted	$120,000
(7) Amount deductible if relief is granted: greater of (5) or (6)	$120,000

If relief is granted under these procedures, the amounts that would otherwise be included in the gross incomes of key employees in accordance with section 83 of the Code pursuant to section 402(b) (amounts otherwise includible) may be reduced. In the case of employees of employers other than governmental entities or tax-exempt organizations, the total of the increases in amounts otherwise includible in the key employees' respective gross incomes resulting from the plan's disqualification will be limited to the excess, if any, of the amount deductible by the employer under section 404(a)(5), if relief is not granted, over the product of the number-of-months factor multiplied by the lesser of (a) the amount contributed by the employer, or (b) the limitation under section 404(a)(1), (2), (3) or (9) that would apply if the plan were qualified.

If the employer is a tax-exempt organization, the total of the increases in the amounts otherwise includible in the key employees' respective gross incomes resulting from the plan's disqualification will be limited to the product obtained by multiplying the excess of 100 percent over the number-of-months factor by the lesser of the amount contributed by the employer or the limitation under section 404(a) of the Code that would apply if the employer were a taxable entity and the plan were qualified. If the total of the additional amounts otherwise includible is less because relief is granted, such total will be allocated to the key employees in the same manner as illustrated below for other employers.

The following example, continuing Example (2) above, illustrates how the amount includible in the key employees' gross income would be determined under these procedures:

Example (2) (continued)

(5) (4) × (3)	$24,000
(6) Amount includible in participating employees' gross income under section 402(b) and deductible by employer under section 404(a)(5), if relief is not granted	$120,000
(6a) Portion of (6) attributable to key employees	$100,000
(7) Amount deductible by employer if relief is granted	$120,000
(8) Limit on total of amounts otherwise includible in key employees' gross income as result of plan's disqualification if relief is granted: excess of (7) over (5)	$96,000
(9) Amount includible in key employees' gross income: lesser of (6a) or (8)	$96,000

The total of the additional amounts otherwise includible if relief is granted ($96,000 in Example 2) will be allocated first to 5-percent owners within the meaning of section 416(i)(1)(B)(i) of the Code, in order of descending ownership interest. In the case of 5-percent owners with equal ownership interests, the aggregate amount allocable to such employees will be allocated to them in proportion to the respective increases in their otherwise includible

income if relief were not granted. Any remainder not allocated to 5-percent owners will be allocated to the other key employees in proportion to the respective increases in their amounts otherwise includible if relief were not granted.

The following examples illustrate how the additional amounts includible in the gross incomes of key employees would be allocated under these procedures where the total of the additional amounts is less than the total of the amounts otherwise includible because of this relief.

Example (3)

Assume there are 9 key employees having the ownership interests shown:

Key Employee	Ownership Interest	Addidtional Amounts Includible If Relief Not Granted	Additional Amounts Includible If Relief Granted
A	30%	$ 20,000	$20,000
B	18%	—	—
C	15%	18,000	18,000
D	10%	40,000	38,667(a)
E	10%	20,000	19,333(b)
F	8%	—	—
G	5%	500	—
Subtotals for 5-percent Owners		$ 98,500	$96,000
H	—	1,000	—
I	—	500	—
Totals		$100,000	$96,000

Allocation of additional amounts between 5-percent owners with identical ownership interests:

(a) $\frac{\$40,000}{60,000} \times \$58,000 = \$38,667$

(b) $\frac{\$20,000}{\$60,000} \times \$58,000 = \$19,333$

Example (4)

Assume there are 5 key employees having the ownership interests shown:

Key Employee	Ownership Interest	Additional Amounts Includible If Relief Not Granted	Additional Amounts Includible If Relief Granted
A	40%	$ 30,000	$30,000
B	40%	25,000	25,000
C	20%	20,000	20,000
Subtotals for 5-percent Owners		$ 75,000	$75,000
D	—	15,000	12,600(c)
E	—	10,000	8,400(d)
Totals		$100,000	$96,000

Allocation of additional amounts between key employees with less than a 5-percent ownership interest:

(c) $\frac{\$15,000}{\$25,000} \times \$21,000 = \$12,600$

(d) $\frac{\$10,000}{\$25,000} \times \$21,000 = \$8,400$

INSTRUCTIONS TO TAXPAYERS

Eligible employers who wish to obtain relief under this procedure must satisfy the "section 7805(b) request requirement" and the "determination letter follow-up requirement."

A plan will satisfy the section 7805(b) request requirement if, prior to the issuance of the determination letter, a letter is sent to the appropriate key district that (1) requests section 7805(b) treatment, (2) indicates the effective date and compliance date of TEFRA, TRA and REA with respect to the plan, and (3) states (a) the employer's taxable years in which deductions were claimed to which an adjustment to the deductible limit is made under the notice, (b) the due date of the return for each such year, (c) whether the return for such year was filed, and (d) the number-of-months factor from the table in this notice. Furthermore, the employer must agree to satisfy the "amended return requirement." An employer will satisfy the amended return requirement if the employer agrees to file with the Service (1) the employer's amended corporate, partnership or individual income tax return, as appropriate, to reflect any decrease in employer deductions under section 404 of the Internal Revenue Code resulting from the recomputation of allowable deductions under these procedures for all taxable years falling within the noncompliance period, and (2) information returns with respect to key employees who have includible income in any taxable year as a result of the plan's nonqualified status during the noncompliance period. Such returns will, of course, reflect the application of the section 7805(b) relief provided under these procedures. The amended return requirement applies only to the taxable year or years impacted by these procedures for which the applicable returns were actually filed or required to be filed prior to the issuance of the determination letter. Lastly, the employer must agree to reflect the changes required under the procedure for returns impacted thereby which were returns neither filed nor required to be filed by the date of issuance of the determination letter.

An employer will satisfy the determination letter follow-up requirement only if by the last day of the second month following issuance of the determination letter the employer files the amended returns necessary to satisfy the amended return requirement and send copies of such returns to the key district director. Failure of the employer to satisfy the section 7805(b) request requirement or the determination letter follow-up requirement will preclude the employer from obtaining 7805(b) treatment under these procedures.

If a request for section 7805(b) treatment is made, the key district will consider such section 7805(b) treatment concurrently but separately. If there are taxable years for which a return was due, the Service will not issue a section 7805(b) letter until the follow-up requirement has been satisfied. After the follow-up requirement has been satisfied, the Service will issue a letter granting section 7805(b) relief with respect to defects resulting from the plan's failure to amend to comply with TEFRA, TRA and REA, whichever is applicable.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Limitations on Alternative Benefits

EE-95-84

SUMMARY: This document contains proposed regulations relating to certain restrictions on an employee's right to receive alternative forms of benefit under qualified plans. They reflect changes made by the Retirement Equity Act of 1984 (REA) [Pub. L. 98-397; 1984-2 C.B. 433]. The regulations will generally affect sponsors of, and participants in, pension, profit-sharing and stock bonus plans, and they provide plan sponsors with guidance necessary to comply with the law.

DATES: Written comments and requests for a public hearing must be delivered or mailed by March 31, 1986. These regulations are proposed to be effective January 30, 1986, except as otherwise specified in these regulations.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (EE-95-84) Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Nancy J. Marks of the Employee Plans and Exempt Organizations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T). Telephone 202-566-3903 (not a toll-free number).

SUPPLEMENTARY INFORMATION:
BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under sections 401 and 411 of the Internal Revenue Code of 1954 (Code). Generally, the proposed regulations under section 401(a)(4) clarify existing law. The proposed regulations under sections 401 and 411 conform the regulations to section 301 of the Retirement Equity Act of 1984 (REA) [Pub. 98-397, 1984-2 C.B. 433, 445]. The regulations are proposed to be issued under the authority of Code sections 411(d)(6) and 7805 (98 Stat. 1450, 68A Stat. 917; 26 U.S.C. 411(D)(6), 7805).

NONDISCRIMINATION REQUIREMENTS

SECTION 401(a)(4) of the Code provides that a qualified plan must provide either contributions or benefits that do not discriminate in favor of employees who are officers, shareholders or highly compensated (the prohibited group).

Rev. Rul. 85-59, 1985-1 C.B. 135, considered whether plans providing actuarilly equivalent forms of benefit that are subject to certain conditions (including a requirement that the trustee approve a participant's request to receive a single sum distribution) would satisfy section 401(a)(4). Rev. Rul. 85-59 held that these restrictions on a plan participant's ability to receive a single sum distribution may be discriminatory under section 401(a)(4).

The proposed regulations generally restate the position taken in Rev. Rul. 85-59. However, they provide that this position will be applied only prospectively with respect to existing conditional alternative forms of benefit. Thus, with respect to such benefits, Rev. Rul. 85-59 will not be applied until these regulations are effective.

REA REQUIREMENTS

Rev. Rul. 79-90, 1979-1 C.B. 155, held that a defined benefit pension plan violates the definitely determinable benefits requirement of section 401 and Treas. Reg. §1.401-1(b)(1)(i) unless, whenever the amount of any optional or early retirement benefit is to be determined on the basis of actuarial assumptions, such assumptions are specified in the plan in a manner that precludes employer discretion. For this purpose employer discretion includes discretion of the employer, plan administrator, fiduciary, actuary or other person.

Rev. Rul. 81-12, 1981-1 C.B. 228, considered whether plan amendments that changed actuarial factors directly or indirectly affected the computation of a participant's accrued benefit in a manner that violated section 411(d)(6) of the Code. Rev. Rul. 81-12 held that a change in actuarial factors that affects the calculation of a participant's optional or early retirement benefit is subject to the protective language of section 411(d)(6). Thus, a change in actuarial factors that could result in the decrease of a participant's accrued benefit, including an optional or early retirement benefit, would result in plan disqualification.

Section 401(a)(25) of the Code, added by section 301 of REA, affirms the Service's application (in Rev. Ruls. 79-90 and 81-12) of the section 401(a) definitely determinable benefit requirement. Section 401(a)(25) provides that a defined benefit plan shall not be treated as providing definitely determinable benefits unless any actuarial assumptions used to determine the amount of any benefit are specified in the plan in a way that precludes employer discretion.

Section 411(d)(6) of the Code, as amended by section 301 of REA, provides that, in general, a plan will not satisfy the requirements of this section if the accrued benefit of a participant is decreased by an amendment of the plan, other than an amendment described in section 412(c)(8), or section 4281 of the Employee Retirement Income Security Act of 1974 (ERISA) [Pub. L. 93-406, 1974-3 C.B. 1]. Section 411(d)(6) also provides that a plan amendment that has the effect of eliminating or reducing an early retirement benefit or, under certain conditions, a retirement-type subsidy or an optional form of benefit, with respect to benefits attributable to service before the amendment, shall be treated as impermissibly reducing accrued benefits. An exception is provided to the extent that such amendments are permitted under regulations promulgated by the Secretary under the grant of regulatory authority contained in section 411(d)(6).

The proposed regulations provide that the definitely determinable benefit requirement precludes a pension plan provision that allows employer consent or discretion with respect to the availability or payment of any alternative forms of benefit. The proposed regulations further provide that any qualified plan, including any profit-sharing or stock bonus plan that is not subject to the definitely determinable benefit requirement, may not contain these types of employer consent or discretion provisions. These provisions would effectively enable an employer to eliminate or reduce the availability of alternative forms of benefit without regard to the protection given to plan participants under section 411(d)(6) that such accrued benefits not be eliminated or reduced. However, the proposed regulations clarify that a qualified plan may condition the availability of an alternative form of benefit on satisfaction of objective and clearly ascertainable criteria specifically set forth in the plan, including, for example, the insurability of the employee or the existence of extreme financial need. The prohibition on employer consent or discretion is not violated where the employer reasonably and consistently applies such objective and clearly ascertainable criteria.

TITLE I OF ERISA

The proposed regulations under section 411 are also applicable to identical provisions of Title I. Thus, these requirements also apply to employee plans subject to Title I of ERISA. Under section 101 of Reorganization Plan No. 4 of 1978 [43 FR 47713], the Secretary of the Treasury has jurisdiction over the subject matter addressed in these regulations. Therefore, under section 104 of the Reorganization Plan, these regulations apply when the Secretary of Labor exercises authority under Title I of ERISA.

PLAN AMENDMENTS

Existing plans that contain alternative forms of benefit that are subject to consent or discretion provisions, or other conditions that discriminate, must be amended by the first day of the first plan year for which these regulations are effective, such amendments to be effective as of that day. These amendments must eliminate (a) employer discretion or consent provisions applicable to the availability of alternative forms of benefit, and (b) other conditions with respect to such alternative forms of benefit that discriminate. Alternatively, the plan must be amended to eliminate the alternative forms of benefit that are subject to such discretion or consent provisions or other conditions that discriminate. In addition, existing plans that contain conditions applicable to alternative forms of benefit that may reasonably be expected to discriminate may be amended either to eliminate such conditions or to eliminate the alternative forms of benefit subject to such conditions. Furthermore, plans may not be amended to add employer discretion or consent provision or other conditions that discriminate with respect to an alternative form of benefit.

EFFECTIVE DATES OF THIS REGULATION

Section 1.401(a)-4 of these regulations is generally proposed to be effective January 30, 1986, in the case of plans either adopted or made effective on or after that date. With respect to plans in existence (adopted and in effect) prior to January 30, 1986, the following effective dates are applicable. In the case of existing plans that are amended to add discriminatory provisions or conditions relating to the availability of an alternative from of benefit, of the type described herein, the regulation is proposed to be effective January 30, 1986, with respect to such alternative form of benefit. In the case of existing non-collectively bargained plans, the regulation is proposed to be effective for the second plan year commencing on or after January 30, 1986. For existing collectively bargained plans, the regulation is proposed to be effective for the earlier of (a) the third plan year commencing on or after January 30, 1986, or (b) the second plan year beginning after the expiration of the last of the collective bargaining agreements, in effect on January 30, 1986, pursuant to which the plan is maintained.

Section 1.411(d)-4 is proposed, except in the case of adoptions of certain master or prototype plans, to be effective August 1, 1986, in the case of plans either adopted or effective on or after that date. Employers who adopt a master or prototype plan for which a sponsor applied to the Service for an opinion letter on or before December 31, 1984, and for which a favorable opinion letter was received after that date are deemed to have existing plans for purposes of this regulation. However, such adopting employers who cease to be covered under such a master or prototype plan prior to the proposed applicable effective date for their plan will be treated as through they had a new plan as of the date they cease to be so covered.

With respect to existing plans, other than master or prototype plans that are deemed to be existing plans, the following effective dates are applicable. In the case of existing plans that are amended to add provisions or conditions relating to the availability of an alternative form of benefit, of the type described herein, the regulation is proposed to be effective the first day of the first month commencing on or after six months after January 30, 1986, with respect to such alternative form of benefit. In the case of existing non-collectively bargained plans, the regulations are proposed to be effective for the second plan year commencing on or after January 30, 1986. For existing collectively bargained plans, these regulations are proposed to be effective for the earlier of (a) the third plan year commencing on or after January 30, 1986, the second plan year beginning after the expiration of the last of the collective bargaining agreements, in effect on January 30, 1986, pursuant to which the plan is maintained. However, in the case of employers who adopt master or prototype plans that are deemed to be existing plans, the effective date will be the earlier of the second plan year commencing on or after January 30, 1986, or the first plan year commencing on or after January 30, 1987.

Taxpayers may rely on these proposed regulations for guidance pending the issuance of final regulations. The transitional rule provisions of these regulations, allowing plan amendments described above, are immediately effective. Thus, existing plans may make the plan amendments described above, thereby eliminating certain benefit alternatives, prior to the general effective date of these new rules.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291. Therefore, a Regulatory Impact Analysis is not required. Although this document is a notice of proposed rulemaking which solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

COMMENTS AND REQUESTS FOR PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

DRAFTING INFORMATION

The principal author of these proposed regulations is Nancy J. Marks of the Employee Plans and Exempt Organizations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * *

Proposed Amendments to the Regulations

The proposed amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority citation for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.411(d)-4 also issued under 26 U.S.C. 411(d)(6).

Par. 2. A new section 1.401(a)-4 is added immediately after §1.401(a)-3 to read as follows:

§1.401(a)-4 Limitations on availability of alternative forms of benefit.

Q-1: Does a pension, profit-sharing or stock bonus plan satisfy section 401(a)(4) if, in form or operation, the availability of an alternative form of benefit favors the prohibited group?

A-1: No. Section 401(a)(4) provides that a qualified plan must provide either contributions or benefits that do not discriminate in favor of employees who are officers, shareholders, or highly compensated (the prohibited group). When a plan provides for alternative forms of benefit, i.e., different forms of distribution commencing at the same time or the same form of distribution commencing at different times (see definition in §1.411(d)-4, Q&A-1), the availability of each of these alternative forms of benefit is subject to this nondiscrimination requirement. Thus, the availability of such alternative forms of benefit may not favor the prohibited group. For example, a plan may not condition the availability of a single sum optional benefit in a manner that favors the prohibited group. This is true whether or not the particular benefit option is the actuarial equivalent of any other form of benefit under the plan.

Q-2: How is it determined whether or not a plan conditions the availability of alternative forms of benefit in a manner that violates, or may reasonably be expected to violate, the nondiscrimination requirements of section 401(a)(4)?

A-2: This determination must be based on all the surrounding facts and circumstances of the employer maintaining the plan. However, a condition is discriminatory if the group of employees to whom the benefit is available does not satisfy either the seventy percent test of section 410(b)(1)(A) or the nondiscriminatory classification test of section 410(b)(1)(B). Thus, the availability of a particular alternative form of benefit will not be considered discriminatory if the benefit is available to seventy percent or more of all employees. If the seventy percent test is not satisfied, the condition limiting availability will be discriminatory if it results in more than a reasonable difference between (a) the ratio of prohibited group employees to whom a particular alternative form of benefit is available to all prohibited group employees and (b) the ratio of employees (other than prohibited group employees) to whom the same alternative form of benefit is available to all employees (other than prohibited group employees). A condition with respect to the availability of a particular alternative form of benefit may reasonably be expected to violate the nondiscrimination requirements of section 401(a)(4) if, under the applicable facts and circumstances, there is a reasonable expectation that the condition will result in the benefit not being available to a group of employees that meets the requirements of section 410(b)(1)(A) or (B) set forth above. The following examples are illustrative:

Example (1). A plan conditions the availability of a single sum benefit alternative by limiting it either to (a) employees earning $50,000 or more in the final year of employment, (b) employees who furnish evidence that they have a net worth above a certain specified amount, or (c) employees who present a letter from an accountant or attorney declaring that it is in the employee's best interest to receive a single sum distribution. Whether such conditions are permissible depends on all the facts and circumstances of the employer maintaining the plan. However, all three of these conditions may reasonably be expected to discriminate in favor of the prohibited group in operation because of the probability of a significant positive correlation between the ability to meet these requirements and membership in the prohibited group.

Example (2). A plan limits the availability of a single sum optional benefit to employees employed in one particular division of the employer's company. All the employees of the company are participants in the plan. The division currently employs individuals who represent a nondiscriminatory classification of that company's employees and is unlikely to cease employing such a nondiscriminatory classification in the future. This condition with respect to availability does not result in discrimination nor may it reasonably be expected to do so.

Q-3: May a pension, profit-sharing or stock bonus plan provide that the employer or some other person, other than the participant (and, where relevant, other than the participant's spouse), through withholding consent or otherwise exercising discretion, may deny a participant an alternative form of benefit for which the participant is otherwise eligible?

A-3: No. Even though in certain circumstances this type of provision may satisfy the nondiscrimination requirements of section 401(a)(4), the provision results in the failure of the plan to satisfy section 401(a), including the requirements set forth in sections 401(a)(25) and 411(d)(6). *See* §1.411(d)-4 Q&As 2-5. This result is true whether the consent or discretion in question is vested in the employer or in some other person. *See* §1.411(d)-4 Q&A-4. The applicable effective dates with respect to such rules relating to consent or discretion are set forth in §1.411(d)-4 Q&A-8.

Q-4: Will a plan provision violate section 401(a)(4) merely because it mandates a single sum distribution in the event that the present value of a participant's nonforfeitable accrued benefit is not more than $3,500?

A-4: No. A provision that mandates a single sum distribution if the present value of a participant's nonforfeitable accrued benefit is not more than $3,500 will be deemed not to be discriminatory under section 401(a)(4). This is an exception to the general principles of this section based on sections 411(a)(11) and 417(e).

Q-5: If a plan contains a provision with respect to the availability of alternative forms of benefit that discriminates or may reasonably be expected to discriminate, what acceptable alternatives exist for amending the plan without violating section 411(d)(6)?

A-5: (a) The following transitional rules apply for purposes of making necessary amendments to existing plans, as defined in Q&A-6 of this section, that contain conditions governing the availability of one or more alternative forms of benefit that violate the nondiscrimination requirements of section 401(a)(4) or may reasonably be expected to violate such requirements. These transitional rules are provided under the authority of section 411(d)(6), which allows the elimination of optional forms of benefits if permitted by regulations, and section 7805(b).

(b) If an existing plan conditions the availability of an alternative form of benefit in a manner that discriminates, the plan must be amended to eliminate such condition. Alternatively, the plan must be amended to eliminate the alternative form of benefit subject to such condition, including any early or late retirement benefit which is so conditioned. If an existing plan conditions the availability of an alternative form of benefit in a manner that may reasonably be expected to discriminate, the plan may be amended to either eliminate such condition or eliminate the alternative form of benefit subject to such condition.

(c) Any amendment permitted under paragraph (b) of this Q&A-5 to eliminate an alternative form of benefit must be made on or before the applicable effective date for the plan as determined under Q&A-6 of this section. Thus, after the applicable effective date, any amendment that eliminates an alternative form of benefit, whether or not such form of benefit is subject to conditions that discriminate or may reasonably be expected to discriminate, will violate the requirements of section 411(d)(6) to the extent that such alternative form of benefit is protected by section 411(d)(6).

Q-6: What are the effective dates for the rules in this section?

A-6: (a) *New plans*. This section is effective January 30, 1986, in the case of plans which are either adopted or made effective on or after such date. This effective date is applicable to such plans whether or not they are collectively bargained.

(b) *Existing plans*. Existing plans, for purposes of this section, are plans which are both adopted and in effect prior to January 30, 1986. Subject to the limitations in paragraph (c) of this Q&A-6, the following effective dates apply to existing plans for purposes of this section.

(1) *Non-collectively bargained plans*. In the case of existing non-collectively bargained plans, the regulation is effective for the first day of the second plan year commencing on or after January 30, 1986.

(2) *Collectively bargained plans*. In the case of existing collectively bargained plans, the regulation is effective for the first day of the earlier of (i) the third plan year commencing on or after January 30, 1986, or (ii) the second plan year beginning after the expiration of the last of the collective bargaining agreements, in effect on January 30, 1986, pursuant to which the plan is maintained. Extensions of a collective bargaining agreement, if ratified on or after January 30, 1986, are disregarded.

(c) The delayed effective dates in paragraph (b)(1) and (2) of this Q&A-6 for existing plans are only applicable with respect to an alternative form of benefit if (1) both the alternative form of benefit and the condition to which it is subject were adopted and in effect prior to January 30, 1986, and (2) the condition to which it is subject is either discriminatory or may reasonably be expected to discriminate. If the conditions in the preceding sentence are not satisfied with respect to a particular alternative form of benefit, then this section is effective with respect to such alternative form of benefit as if the plan were a new plan.

(d) The transitional rule provided in Q&A-5 of this section is effective January 30, 1986.

Par. 3. A new §1.411(d)-4 is added immediately after 1.411(d)-3T to read as follows:

§1.411(d)-4 Alternative forms of benefit.

Q-1: What is meant by "alternative forms of benefit" for purposes of this section?

A-1: This term encompasses the different forms of benefit payment available under a plan which provides that (a) a participant's benefits under the plan may be paid in more than one form (for example, life annuities, installment payments and single sum distributions), or (b) payment of a particular form of benefit may commence at some time earlier or later than the normal date for the commencement of such benefit. For example, a life annuity beginning at early retirement age and a life annuity beginning at normal retirement age are alternative forms of benefit for purposes of this section.

Q-2: May a pension, profit-sharing or stock bonus plan provide that the employer may, through withholding consent or otherwise exercising discretion, deny a participant an alternative form of benefit for which the participant is otherwise eligible?

A-2: No. Such a provision will violate the requirement of section 411(d)(6), which applies to accrued benefits of pension, profit-sharing and stock bonus plans, to the extent that the consent or discretion may be exercised with respect to an alternative form of benefit protected by section 411(d)(6). In addition, in the case of a pension plan, such a provision violates the "definitely determinable" requirement of section 401(a), which applies to any alternative form of benefit available to participants under the plan, not merely to accrued benefits under section 411(d)(6). *See* §1.401-1(b)(1)(i). However, see Q&A-5 of this section regarding the application of objective and clearly ascertainable conditions on the availability of an alternative form of benefit.

Q-3: Is the result in Q&A-2 of this section any different if the plan specifically limits the employer's exercise of discretion to choosing among alternative forms of benefit that can be demonstrated to be actuarially equivalent based on reasonable actuarial assumptions set forth in the plan?

A-3: No.

Q-4: Is the answer in Q&A-2 of this section any different if a plan permits the exercise of discretion by, or requires consent from, some person or persons other than the employer and the participant (and, where relevant, other than the participant's spouse)?

A-4: No. The term "employer" includes plan administrator, fiduciary, trustee, actuary and other persons for purposes of applying the rules of this section and §1.401(a)-4. Thus, provisions permitting any person, other than the participant (and, where relevant, other than the participant's spouse), to deny the participant an alternative form of benefit otherwise available to the participant under the plan, violate the requirements of sections 401(a), including sections 401(a)(25) and 411(d)(6).

Q-5: May a pension, profit-sharing or stock bonus plan condition the availability of an alternative form of benefit on objective criteria that are specifically set forth in the plan?

A-5: Yes. Such provisions do not violate the requirements of section 411(d)(6) provided the criteria are objective, ascertainable, clearly set forth in the plan and not subject to the employer's discretion. For example, a plan may deny a single sum optional benefit to participants for whom life insurance is not available at standard rates provided this provision is specifically set forth in the plan. As another example, a plan may provide that an otherwise permissible single sum distribution alternative, based on separation from service, may be available only in the event of extreme financial need, after taking into account the employee's other assets available to meet those needs, determined under standards specifically set forth in the plan. On the other hand, a plan may not condition the availability of alternative forms of benefit permitted under the plan on factors that are within the employer's discretion. For example, the availability of alternative forms of benefit in a defined benefit plan may not be conditioned on a determination with respect to the level of the plan's funded status because the amount of plan funding is within the employer's discretion.

Q-6: May a plan be amended to add a consent or discretion provision or other condition to an alternative form of benefit?

A-6: No. Adding a consent or discretion provision or other conditions with respect to the availability of an employee's accrued benefit in an alternative form of benefit that is within section 411(d)(6) effectively enables an employer to eliminate or reduce an employee's accrued benefit within the meaning of such section. However, an amendment of the type described in Q&A-5 of this section that adds one or more objective and clearly ascertainable conditions on the availability of an employee's accrued benefit in an alternative form of benefit may be made with respect to benefits accrued after the later of the effective date of the amendment or the date such amendments is adopted. Also, after the effective date of this section, with respect to a pension plan, consent or discretion provisions may not be added with respect to any alternative form of benefit.

Q-7: If a plan contains discretion or consent provisions which violate the requirements of section 401(a), including sections 401(a)(25) and 411(d)(6), and this section, what acceptable alternatives exist for amending the plan without violating the requirements of section 411(d)(6)?

A-7: (a) The following transitional rules apply for purposes of making necessary amendments to existing plans, as defined under the effective date provisions in Q&A-8 of this section, that contain discretion or consent provision with respect to the availability of alternative forms of benefit that violate the requirements of section 401(a), including sections 401(a)(25) and 411(d)(6), and this section. These transitional rules are provided under the authority of section 411(d)(6), which allows the elimination of optional forms of benefits if permitted by regulations, and section 7805(b).

(b) If an existing plan provides for employer consent or discretion with respect to the availability of an alternative form of benefit, the plan must be amended to eliminate such consent or discretion provision. Alternatively, the plan must be amended to discretion provision, including any early or late retirement benefit that is so conditioned.

(c) Any amendment permitted under paragraph (b) of this Q&A-7 to eliminate an alternative form of benefit must be made on or before the applicable effective date for the plan as determined under Q&A-8 of this section. Thus, after the applicable effective date, any amendment that eliminates an alternative form of accrued benefit, whether or not such form of benefit is subject to employer consent or discretion, will be a violation of section 411(d)(6).

Q-8: What are the effective dates for the rules in this section?

A-8: (a) *New plans*. This section is effective August 1, 1986, in the case of plans that are either adopted or made effective on or after such date. This effective date is applicable to such plans whether or not they are collectively bargained.

(b) *Existing plans*. Existing plans, for purposes of this section, are those plans, with the exception of certain plans which are adoptions of master or prototype plans, which are both adopted and in effect prior to August 1, 1986. Employers who adopt a master or prototype plan for which a sponsor applied to the Service for an opinion letter on or before December 31, 1984, and for which a favorable opinion letter was received after that date, will be deemed to have existing plans for purposes of this section. *See* sections 4.01 and 4.02 of Rev. Proc. 84-23, 1984-1 C.B. 457, 459, for the definitions of master and prototype plans. However, if such adopting employers cease to be covered under a plan which is an adoption of a master or prototype plan of the type described above, as a result of amendment of the plan or adoption of a new plan, prior to the effective date of this section with respect to their plan, then the effective date of such employers will be determined as though the plan were a new plan as of the date of such amendment or adoption of a new plan. Subject to the limitations in paragraph (c) of this Q&A-8, the following effective dates apply to existing plans for purposes of this section:

(1) *Non-collectively bargained plans*. In the case of existing plans other than collectively bargained plans this section is effective for the first day of the second plan year commencing on or after January 30, 1986.

(2) *Collectively bargained plans*. In the case of existing collectively bargained plans this section is effective for the first day of the earlier of (i) the

third plan year commencing on or after January 30, 1986, or (ii) the second plan year beginning after the expiration of the last of the collective bargaining agreements, in effect January 30, 1986, pursuant to which the plan is maintained. Extensions of a collective bargaining agreement, if ratified on or after August 1, 1986, are disregarded.

(3) *Master and prototype plans.* In the case of plans which are adoptions of master or prototype plans that are deemed to be existing plans under the provisions of this paragraph (b), the effective date will be the earlier of the second plan year commencing on or after January 30, 1986, or the first plan year commencing on or after January 30, 1987.

(c) The delayed effective dates in paragraph (b)(1) and (2) of this Q&A-8 for existing plans are only applicable with respect to an alternative form of benefit if both the alternative form of benefit and the consent of discretion provision or other condition to which it is subject are adopted and in effect prior to August 1, 1986. If the conditions set forth in this paragraph are not satisfied with respect to a particular alternative form of benefit, then this section is effective with respect to such alternative form of benefit as if the plan were a new plan.

(d) The transitional rule provided in Q&A-7 of this section is effective January 30, 1986.

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on January 29, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 30, 1986, 51 F.R. 3798)

Notice of Proposed Rulemaking
Return of Partnership Income
LR-198-82

SUMMARY: This document contains proposed amendments to the income tax regulations relating to partnership returns. The proposed regulations require partnerships to furnish certain return information to their partners and revise the exceptions to the partnership filing requirement. Changes to the applicable tax law were made by the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462]. The regulations would provide guidance for determining what information a partnership must furnish to its partners and when certain partnerships must file partnership returns.

DATES: Written comments and requests for a public hearing must be delivered or mailed by March 24, 1986. The regulations are proposed to be effective for partnership taxable years beginning after September 3, 1982. For exceptions to this effective date, see the text of the regulations.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (L-198-82), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Beverly A. Baughman of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3297).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 6031 of the Internal Revenue Code of 1954. These amendments are proposed to conform the regulations to sections 403 and 404 of the Tax Equity and Fiscal Responsibility Act of 1982 (96 Stat. 669) [Pub. L. 97-248, 1982-2 C.B. 462, 596].

INFORMATION TO BE FURNISHED TO PARTNERS

Before the enactment of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), a partnership required under section 6031 to file a partnership return was not required by statute to furnish information to its partners. TEFRA amended section 6031 to require the partnership to furnish to every person who was a partner in the partnership at any time during the taxable year a copy of the information on the partnership return to the extent required by regulations.

The proposed regulations require the partnership to give each partner a statement showing that partner's distributive share of partnership income, gain, loss, deduction or credit and, to the extent required under the instructions for the partnership return, any additional information from the partnership that is necessary to enable the partner to determine the correct income tax treatment of an item related to the partnership. For example, the partnership may be required to furnish the information on partnership liabilities necessary for purposes of determining the application of section 465 (relating to limitation of deductions to amount at risk) to partners with respect to partnership activities.

EXCEPTION TO FILING REQUIREMENT

Existing §1.6031-1 provides exceptions from the requirements that a partnership return be filed for two classes of partnerships: partnerships electing exclusion from the partnership provisions of the Code under section 761(a) and partnerships that neither carry on any business in the United States nor derive any income from sources within the United States. Section 404 of TEFRA in effect nullified these exceptions in any case in which the tax liability of any United States person is affected by items flowing from a partnership. That section, however, authorizes new regulations to provide exceptions from the filing requirement.

The proposed regulations would provide exceptions for partnerships making the election under section 761(a) and for certain foreign partnerships with no United States business or income. Every domestic partnership (except a partnership making the election under section 761(a) or an inactive one that in a given taxable year conducts no business and has no income or deductions from any sources whatsoever) would be required to file a return even if it has no United States business and no United States income.

The proposed regulations provide an exception from the filing requirement for a foreign partnership carrying on no business in the United States and deriving no income from sources within the United States unless United States persons hold a specified interest in the partnership. The proposed regulations require that a foreign partnership file a return for a taxable year if at any time during that taxable year an aggregate of 25 percent or more of any item of income, gain, loss, deduction or credit of the partnership for the taxable year is allocable to a United States person or persons. For purposes of these rules, interests held by a pass-thru partner (such as another partnership or trust) that is not a United States person are also treated as held by each indirect partner to the extent that the indirect partner holds an interest in the foreign partnership through that pass-thru partner.

The percentage interest of an indirect partner in a foreign partnership is determined by multiplying the percentage interest of the pass-thru partner in any item of income, gain, loss, deduction, or credit of the foreign partnership by (1) the percentage interest of the indirect partner in that item of income, gain, loss, deduction, or credit of the pass-thru partner, when the pass-thru partner is a partnership, and (2) the percentage of the indirect partner's actuarial interest in the trust or estate when the pass-thru partner is a trust or estate.

The Internal Revenue Service recognizes that the rule requiring that interests held by indirect partners be taken into account may cause concern among certain taxpayers because a foreign partnership may not know whether it has indirect partners, and it may be very difficult for that partnership to obtain such information. Additionally, the consequences of failing to meet the filing requirement can be harsh. Therefore, the Service would appreciate comments on this rule.

If a foreign partnership would not be required to file a partnership return but for the 25 percent rule discussed above, the draft regulations provide that the reporting requirements of paragraphs (a)(2) and (b) of proposed §1.6031-1, which relate to a specific partner or partners, apply only with respect to partners who are United States persons or pass-thru partners through which United States persons hold interests in the foreign partnership as indirect partners. Thus, although the foreign partnership must report, for example, all items of gross income and all allowable deductions, it need not report the distributive shares of its partners other than for its partners who are United States persons or pass-thru partners through which United States person are indirect partners.

The draft regulations exclude from the definition of United States person, with respect to any partnership, any individual who is a bona fide resident of Puerto Rico (which is treated as a possession for certain tax purposes), the Virgin Islands, Guam or any other United States possession if no item of the partnership is taken into account in determining the United States income tax obligation of the individual that is required to be paid to the United States Treasury.

IMPORTANCE OF FILING REQUIREMENT

If a partnership that is not a small partnership under section 6231(a)(1)(B) is required to file a return under section 6031 but fails to do so, the period of limitations on assessment of tax attributable to items of that partnership remains open indefinitely under section 6229(a).

EFFECTIVE DATES

These regulations are proposed to be effective with respect to partnership taxable years beginning after September 3, 1982. A partnership that would be exempt from the filing requirement under the existing regulations, however, will not be required to file a partnership return for any partnership taxable year ending on or before the 90th day after the date on which a Treasury decision on this subject appears in the FEDERAL REGISTER.

SPECIAL ANALYSIS

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required.

Pursuant to 5 U.S.C. 605(b), the Secretary of the Treasury has certified that the requirements of the Regulatory Flexibility Act do not apply to this notice of proposed rulemaking because the proposed regulations will not have a significant economic impact on a substantial number of small entities. The only partnerships that the proposed regulations would for the first time require to file partnership returns are foreign partnerships in which United States persons hold a substantial interest; few small entities hold interests in foreign partnerships. The information that the proposed regulations require a partnership to furnish to its partners is limited to the information that the partners need to determine their own tax liability.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be made available for public inspection and copying. A public hearing will be held upon written request of any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the Federal Register. The collection of information requirements contained herein have been submitted for OMB review under the Paperwork Reduction Act, and comments on them should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments to OMB also send copies of the comments to the Service.

DRAFTING INFORMATION

The principal author of these proposed regulations is Beverely A. Baughman of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations both on matters of substance and style.

* * * * *

Proposed amendments to the regulations

The proposed amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority citation for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.6031-1 also issued under 26 U.S.C. 6031 and section 404 of the Tax Equity and Fiscal Responsibility Act of 1982 (96 Stat. 669) [Pub. L. 97-248, 1982-2 C.B. 462].

Par. 2. Section 1.6031-1 is revised to read as follows:

§1.6031-1. Return of partnership income.

(a) *In general*—(1) *Return required.* Except as otherwise provided in this section, every unincorporated organization, whether domestic or foreign, defined as a partnership in section 761(a), through or by means of which any business, financial operation, or venture is carried on, shall make a return for each taxable year on the form prescribed for the partnership return. For purposes of this section, an unincorporated organization will not be considered, within the meaning of section 761(a), to carry on a business, financial operation, or venture as a partnership in any taxable year in which the organization neither receives income nor incurs any expenditures treated as deductions or credits for federal income tax purposes. The return shall be made for the taxable year of the partnership, irrespective of the taxable years of the partners. For taxable years of a partnership and of a partner, see section 706 and §1.706-1. For signing of a partnership return, see §1.6063-1.

(2) *Content of return.* The return shall state specifically the items of partnership gross income and the deductions allowable by subtitle A of the Code and shall include the names and addresses of all the partners (as defined in section 7701(a)(2)) and the amount of the distributive shares of income, gain, loss, deduction, or credit allocated to each partner. Notwithstanding any exemption otherwise available under §401.6109-1(g), the return shall also include the identifying numbers of all the partners; provided, however, that any foreign partnership that would be exempted from the requirement to file a return under paragraph (d)(1) of this section but for the provisions of paragraph (d)(2)(i) of this section shall include in its return the identifying numbers of only those partners who are described in paragraph (d)(2)(iv). To the extent required by the form prescribed for the partnership return or by the instructions accompanying that form, the return shall also provide any additional information that may be necessary to determine the application to the partnership or the partners of particular provisions of subtitle A of the Code with respect to items related to the partnership. For example, the form may require information with respect to partnership liabilities for purposes of determining the application of section 465 (relating to limitation of deductions to amount at risk) to the partners with respect to partnership activities.

(3) *Special rule.* Except in the case of an unincorporated organization deemed to be excluded from the application of subchapter K in the manner described in §1.761-2(b)(2)(ii) for the first year of its existence, an unincorporated organization described in §1.761-2(a) shall file a partnership return for the first taxable year in which the participants by a formal agreement undertake to engage in joint operations or, in the absence of a formal agreement, for the first taxable year in which the participants with respect to the joint use of property jointly have income, or make or incur any expenditures treated as deductions or credits for Federal income tax purposes. Additionally, if an organization described in §1.761-2(a) (other than an unincorporated organization deemed to be excluded from the application of subchapter K in the manner described in §1.761-2(b)(2)(ii) for the first taxable year of its existence) does not elect under section 761 and the regulations thereunder to be excluded from the application of all the provisions of subchapter K of chapter 1 of the Code, it is required to file a return for each taxable year subsequent to its first taxable year in accordance with the requirements of this section until an election is made in accordance with §1.761-2(b)(2)(i). Where no annual accounting period has been adopted by an organization described in §1.761-2(a), its taxable year shall be the calendar year in accordance with section 441(g). For special rules in the case of an organization making the election for exclusion under section 761, see §1.761-2(b)(2)(i) and (c) and paragraph (c) of this section.

(b) *Information required to be provided to partners*—(1) *In general.* Any partnership required under paragraph (a)(1) of this section to file a partnership return for a taxable year shall furnish, on or before the day on which that return is filed, to every person who was a partner (as defined in section 7701(a)(2)) at any time during that taxable year a statement showing that person's distributive share of partnership income, gain, loss, deduction or credit. To the extent required by the form or the accompanying instructions, that statement shall also provide any additional information that may be necessary to determine the application to the partner of particular provisions of subtitle A of the Code with respect to items related to the partnership.

(2) *Information may be provided to agent.* If a partner has designated another person, such as an attorney or an investment advisor, as the partner's agent in dealing with the partnership, the partnership may provide the information referred to in paragraph (b)(1) of this section to that other person instead of the partner.

(3) *Penalties.* For penalties for failure to comply with the requirements of section 6031(b) and this paragraph (b), see section 6678(a)(3)(F).

(c) *Unincorporated organizations excluded from the application of subchapter K*—(1) *Wholly excluded*—(i) *Filing for the first year with respect to an election.* Any unincorporated organization with respect to which under section 761(a) an election to be excluded from all the provisions of subchapter K of chapter 1 of the Code has been made in the manner described in §1.761-2(b)(2)(i) shall file the form prescribed for the partnership return for the first year with respect to which such an election has been made. That return shall, in lieu of the information otherwise required, contain or be accompanied by the information required by §1.761-2(b)(2)(i).

(ii) *No requirement to file.* Except as otherwise provided in paragraph (c)(1)(i) of this section, an unincorporated organization which is wholly excluded from the application of subchapter K need not file a partnership return.

(1) *Partially excluded.* Any unincorporated organization excluded from the application of part of subchapter K of chapter 1 of the Code shall file a return on the form prescribed for the partnership return containing such information as the Commissioner may require. See section 761 and §1.761-2(c).

(d) *Foreign partnerships having no United States business*—(1) *General rule.* Except as otherwise provided in paragraph (d)(2), a foreign partnership that engages in no trade or business in the United States and derives no income from sources within the United States is not required to file a partnership return.

(2) *Special rule for certain foreign partnerships*—(1) *In general.* Notwithstanding paragraph (d)(1) of this section, a foreign partnership shall file a partnership return for a partnership taxable year if at any time during that year an aggregate of 25 percent or more of any item of income, gain, loss, deduction, or credit of the partnership is allocable to a United States person or persons.

(ii) *Interests held indirectly through pass-thru partners that are not United States persons.* If an interest in any item of income, gain, loss, deduction, or credit of a foreign partnership is held by a pass-thru partner that is not a United States person, then for purposes of this paragraph (d)(2) that interest shall be treated as held by each indirect partner to the extent that the indirect partner holds an interest in the foreign partnership through that pass-through partner. No person shall be treated as holding an interest in a foreign partnership by virtue of holding an interest in a pass-thru partner which is a United States person; the interest held by any such pass-thru partner shall be treated as an interest held by a United States person for purposes of this paragraph (d)(2).

(iii) *Determination of interest held by an indirect partner in a foreign partnership.* For purposes of paragraph (d)(2)(ii) of this section, the percentage interest of an indirect partner in a foreign partnership shall be determined by multiplying the percentage interest of the pass-thru partner in any item of income, gain, loss, deduction, or credit of the foreign partnership by—

(A) In the case of a pass-thru partner that is a partnership, the percentage interest of the indirect partner in that item of income, gain, loss, deduction, or credit of the pass-thru partner, or

(B) In the case of a pass-thru partner that is a trust or estate, the percentage of the indirect partner's actuarial interest in the trust or estate.

(iv) *Certain foreign partnerships.* In the case of a foreign partnership that would not be requred to file a partnership return but for the provisions of paragraph (d)(2)(i) of this section, those requirements of paragraphs (a)(2) and (b) of this section which relate to a specific partner or partners apply only with respect to partners who are United States persons or pass-thru partners through which United States persons held interests in the partnership as indirect partners. Thus, although the foreign partnership must report all items of gross income and all allowable deductions, it need not, for example, report the distributive share of its partners other than for its partners who are United States persons or pass-thru partners through which United States persons are indirect partners.

(v) *Examples.* The provisions of this paragraph (d)(2) may be illustrated by the following examples:

Example (1). L, a foreign partnership, engages in no trade or business in the United States and derives no income from sources within the United States. For taxable year 1985 all of L's income comes from investment activity and a retail business. Fifteen United States persons are partners in L. For 1985 each of these partners is allocated 2 percent of L's income from investment activities. Because United States persons are allocated 30 percent (15 × 2) of an item of L's income for taxable year 1985, L must file a partnership return for that year under section 6031 pursuant to paragraph (d)(2)(i) of this section. On that return L must include the information required with respect to partners under paragraph (a)(2) of this section only with respect to the fifteen partners who are United States persons. Similarly, L must furnish the statement required under paragraph (b)(1) of this section only to those fifteen partners.

Example (2). M, a foreign partnership, engages in no trade or business in the United States and derives no income from sources within the United States. All of M's income comes from investment activity. For M's taxable year 1985, 26 percent of M's income is allocable to N, a domestic partnership with three equal partners, one of whom is not a United States person. Because all of this 26 percent share is allocable to N as a pass-thru partner which is a United States person for purposes of applying paragraph (d)(2)(i) of this section, M is required to file a partnership return under section 6031 for its taxable year 1985.

Example (3). O, a foreign partnership, engages in no trade or business in the United States and derives no income from sources within the United States. All of O's income is from a retail business. For O's taxable year 1985, 20 percent of O's income is allocable to P, a partnership that is not a United States person. All of P's income is also from a retail business. A, a United States person, is a partner in P and 50 percent of P's income for 1985 is allocable to A. A's interest in O as an indirect partner through P is 10 percent (20% × 50%). A also holds a separate interest in O as a direct partner and 15 percent of O's income is allocable to A because of the separate interest. Because A in the aggregate is allocated 25 percent (10% + 15%) of O's income for purposes of applying paragraph (d)(2)(i) of this section, O is required to file a partnership return under section 6031 for its taxable year 1985.

(3) *Returns of information with respect to partnership required of partners who are United States persons.* If a United States person is a partner in a partnership described in paragraph (d)(1) of this section which is not required to file a partnership return, the district director or director of the service center may require that person to render such statements or provide such information as is necessary to show whether or not that person is liable for tax on income derived from that partnership. In addition, if an election in accordance with the provisions of section 703 (relating to elections affecting the computation of taxable income derived from a partnership) or section 761 (relating to the election to be excluded from the application of all or part of subchapter K, chapter 1 of the Code) is to be made by or for the partnership, a return on the form prescribed for the partnership return shall be filed for the partnership. See section 6063 and §1.6063-1, relating to the authority of a partner to sign a partnership return. The filing of one such return for a taxable year of the partnership by a partner who is a United States person shall constitute a filing for the partnership of a partnership return.

(4) *Exclusion for satellite organizations.* The return requirement of section 6031 and this section shall not apply to the International Telecommunications Satellite Organization, the International Maritime Satellite Organization, or any organization which is a successor of either of these organizations.

(5) *Meaning of terms*—(i) *pass-thru partner.* For the meaning of the term "pass-thru partner," see section 6231(a)(9).

(ii) *Indirect partner.* For the meaning of the term "indirect partner," see section 6231(a)(10).

(iii) *United States person*—(A) *In general.* For purposes of this section the term "United States person" has the meaning assigned to it by section 7701(a)(30) of the Code, except that with respect to any taxable year of a partnership the term does not include any individual who is a bona fide resident of the Commonwealth of Puerto Rico, the Virgin Islands, Guam or any other possession of the United States, if no item of income, gain, loss, deduction or credit of the partnership for the taxable year is taken into account in determining an income tax obligation of the individual under subtitle A of the Code that is required to be paid to the Treasury of the United States.

(B) *Example*. The provisions of this paragraph (d)(4)(iii) may be illustrated by the following example:

Example. S is a partnership organized in Denmark. C, an individual who is a citizen of the United States, is a bona fide resident of Guam and a partner in S. S and C use the calendar year as their taxable year. For 1985, C files his tax return with Guam pursuant to section 935. For purposes of applying this section to S for 1985, C is not considered to be a United States person.

(e) *Place and time for filing returns*—(1) *Place for filing*—(i) *Partnership with United States business or United States income*. The returns of partnerships engaged in trade or business, or having income from sources, within the United States shall be filed—

(A) With the service center for the internal revenue district in which the partnership has its principal office or principal place of business in the United States, or

(B) With the Philadelphia Service Center, Philadelphia, Pennsylvania 19255 if the partnership has no office or place of businesss in the United States.

(ii) *Partnership with no United States business and no United States income*. If a partnership engages in no trade or business in the United States and has no income from sources within the United States, but is required to file a return under paragraph (d)(2) of this section, it shall file its partnership return with the Philadelphia Service Center, Philadelphia, Pennsylvania 19255.

(iii) *Return filed under paragraph (d)(3)*. A partnership return filed under the authority of paragraph (d)(3) of this section shall be filed with the internal revenue officer with whom the partner who is a United States person files his separate income tax return.

(2) *Time for filing*. The return of a partnership shall be filed on or before the fifteenth day of the fourth month following the close of the taxable year of the partnership, except that the return of a partnership consisting entirely of nonresident aliens shall be filed on or before the fifteenth day of the sixth month following the close of the taxable year of the partnership.

(f) *Effective date*—(1) *In general*. This section applies with respect to partnership taxable years beginning after September 3, 1982. For partnership taxable years beginning before September 4, 1982, see 26 CFR 1.6031-1 (Rev. as of April 1, 1984).

(2) *Special rules*. If—

(i) The taxable year of a partnership ends on or before the 90th day after a Treasury decision on this subject appears in the Federal Register, and

(ii) The partnership would not be required to file a partnership return for that year if §1.6031-1 (Rev. as of April 1, 1984) were applied to the partnership for that year in place of paragraphs (a) through (e) of this section.

The partnership shall not be required to file a partnership return for that taxable year.

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on January 22, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 23, 1986, 51 F.R. 3075)

Original Issue Discount Reporting Requirements

Announcement 86-22

This announcement concerns information reporting rules under sections 1275 and 6049 of the Internal Revenue Code for issuers of publicly offered original issue discount (OID) debt instruments and for brokers and other middlemen who hold interests in those debt instruments as nominees. The Internal Revenue Service expects to issue amendments to the Temporary Income Tax Regulations under section 1275(c)(2), published in the Federal Register on June 18, 1985. In addition, the Service expects to issue regulations under section 6049 of the Code. Taxpayers may rely on this announcement until such regulations are issued.

BACKGROUND

As added by section 41 of the Tax Reform Act of 1984 ("the 1984 Act"), 1984-3 (Vol. 1) C.B. 221, section 1275(c)(2) of the Code requires issuers of publicly offered debt instruments having OID to furnish the Secretary with certain information with respect to those debt instruments. This requirement also applies to persons who make a public offering of stripped bonds or coupons as if those persons were issuers of publicly offered debt instruments having OID.

On June 18, 1985, the Service issued section 1.1275-3T of the temporary regulations, which is applicable to debt instruments issued with OID after August 16, 1984. Section 1.1275-3T requires issuers of publicly offered debt instruments having OID to file with the Service the following information: 1) the name, address, and taxpayer identification number of the issuer; 2) the issue date, maturity date, and CUSIP number of the issue; 3) the amount of OID for the entire issue; 4) the issue price expressed as a percentage of the principal amount; 5) the stated redemption price at maturity of the entire issue, or of each debt instrument within the issue if in denominations of other than $1,000; 6) the stated interest rate and interest payment dates; 7) a description of the debt instrument or, in place of such description, a copy of the offering circular or prospectus; and 8) the method used in determining the amount of OID allocable to a short accrual period. The information is to be filed on new Form 8281, Information Return for Publicly Offered Original Issue Discount Instruments.

For debt instruments issued after May 31, 1985, Form 8281 is required to be filed on or before the thirtieth day after issuance of the debt instruments. Failure to file Form 8281 in a timely manner will result in a penalty, pursuant to section 6706(b) of the Code, equal to the lesser of $50,000 or 1% of the aggregate issue price of the issue.

Section 1.6049-5(c) of the Income Tax Regulations provides that in determining whether a debt instrument has OID and, if so, in determining the amount of OID includible in the income of the holder, a payor (other than the issuer of the debt instrument) may rely on the Service's publication of publicly traded OID debt instruments. That reliance is for purposes of complying with the reporting requirements under section 6049 of the Code.

SCOPE

This announcement applies to issuers of publicly offered debt instruments issued with OID after August 16, 1984, with respect to the filing of Form 8281 pursuant to section 1275(c)(2) of the Code. This announcement also applies to brokers and other middlemen who hold as nominees: (1) on or after June 1, 1986, certificates of deposit (CDs) which were sold by the broker or middleman (whether for the broker's account or as an agent for the issuer) to the owner, (2) on or after January 1, 1987, any certificates of deposit, (3) U.S. Treasury STRIPS, and (4) debt instruments that are backed by U.S. Treasury securities and that represent ownership interests in those securities for purposes of information reporting under section 6049 of the Code.

PROCEDURES

The following interim procedures shall apply until further guidance is issued:

1) Form 8281 is not required to be filed with respect to certificates of deposit (CDs) issued by banks or other financial institutions. However, financial institutions that issue CDs must file information returns and statements with respect to OID and interest on such CDs as prescribed by section 6049 and the regulations thereunder.

2) Form 8281 is not required to be filed with respect to CDs containing OID that are sold by brokers or other middlemen. Brokers and other middlemen who hold interests in these instruments as nominees must file information returns and statements with respect to OID and interest on such CDs as prescribed by section 6049 and the regulations thereunder.

3a) Form 8281 is not required to be filed by a person who makes a public offering of instruments that constitute stripped bonds or stripped coupons. These instruments include instruments issued under the Department of the Treasury's STRIPS program, and instruments that constitute ownership interests in U.S. Treasury securities.

b) Brokers and other middlemen who hold as nominees interests in instruments issued under the Treasury's STRIPS program or instruments that constitute ownership interests in stripped U.S. Treasury securities must file information returns and statements with respect to OID on such instruments as prescribed by section 6049 and the regulations thereunder. Publication 1212, List of Original Issue Discount Instruments, provides information with respect to such instruments. Brokers and other middlemen who hold such instruments as nominees may rely on this information for purposes of filing the information returns and statements required by section 6049.

REPORTING REQUIREMENTS

The following reporting requirements will be effective for calendar years beginning in 1986:

The regulations under section 6049 will be amended to provide that all brokers or middlemen holding a CD as a nominee on or after June 1, 1986, who sold such CD (whether for the broker's or middleman's account or as an agent of the issuer) to the owner (regardless of when sold), will be required to report OID with respect to such CDs.

The following reporting requirements will be effective for calendar years beginning in 1987:

The regulations under section 6049 will be amended to provide that all brokers and other middlemen who hold interests in CDs as nominees will be required to report OID with respect to such CDs.

Clarification of Instructions for the 1985 Form 2106

Announcement 86-24

The instructions for Form 2106, Employee Business Expenses, are incomplete for taxpayers who choose an alternative ACRS method for vehicles. The instructions for method 2, column (c) of Section (D) call for the entry of "SL" and the choice of 3, 5, or 12 years. The instructions for column (d) ask the taxpayer to divide column (b) by column (c) if Method 2 is used.

However, if Method 2 is used, only one-half of the depreciation otherwise allowable can be claimed in the first and last year a vehicle is used for business purposes. Therefore, the following should be added at the end of the second sentence in the column (d) instructions: "and if this is the first or last year a vehicle was used for business, divide the result by 2."

Incorrect Line Reference—1985 Form 5695

Announcement 86-25

Line 24 of the 1985 Form 5695, Residential Energy Credit, contains an incorrect reference to line 49 of the 1984 Form 1040. The reference should be to line 50 of the 1984 Form 1040 as follows: "Caution—Do not make an entry on this line if your 1984 Form 1040, line 50, showed an amount of more than zero."

Correction of 1985 Schedule D (Form 1040) Instructions

Announcement 86-26

The 1985 Schedule D (Form 1040) instructions under the heading "Investment Interest Deduction Adjustment" are incorrect.

The instructions for Step 1 should read "reduce line 20 of Form 4952 to" instead of "reduce line 20 of Form 4952 by".

The correction affects only those taxpayers who have an entry on line 20 of Form 4952 (Investment Interest Expense Deduction) and also an entry on line 21 of Schedule D (Form 1040) (or line 8 of Form 4798).

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Philip G. Arneson	Sparta, WI	Attorney	Indefinite from December 15, 1985
Joseph P. Day	Woburn, MA	Attorney	Indefinite from December 24, 1985
Kenneth H. Dillard	Nashville, TN	Certified Public Accountant	Indefinite from December 31, 1985
LeRoy Hodge	Hamilton, NY	Attorney	Indefinite from December 10, 1985
Frank S. Lukuch	Barberton, OH	Certified Public Accountant	Indefinite from December 4, 1985
W. Stephen McConnell	Tampa, FL	Certified Public Accountant	Indefinite from December 26, 1985
Nathan Rich	Wilmington, DE	Certified Public Accountant	Indefinite from December 1, 1985
Walter E. Shettlemore	Long Beach, MS	Certified Public Accountant	Indefinite from December 20, 1985
Dal H. Felkel	Kingstree, SC	Certified Public Accountant	Indefinite from January 31, 1986

Name	Address	Designation	Term of Suspension
John J. Matonis	Walnut, CA	Attorney	Indefinite from January 24, 1986
Joel A. Shor	Baltimore, MD	Certified Public Accountant	Five Months from December 15, 1985

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.451-3, amended.	Accounting for long-term contracts	1986-6 I.R.B. 55	Mar. 7, 1986
26 CFR 31.3508-1, 31.3509-1, 1.6041A-1, added.	Treatment of real estate agents and direct sellers; determination of employer liability for certain employment taxes	1986-6 I.R.B. 46	Mar. 10, 1986
26 CFR 1.6041-3, amended.	Information reporting of allowances or reimbursements for travel expenses of public employees	1986-7 I.R.B. 26	Mar. 10, 1986
26 CFR 1.228(h)(10)-1T, 1.1502-75T, added; 1.338-1T, 1.338-4T, amended.	Elections under section 338(h)(10)	1986-8 I.R.B. 35	Mar. 10, 1986
26 CFR 1.936-2, 1.936-3, 1.936-3A, added; 7.936-1, removed.	Qualified possession source investment income	1986-8 I.R.B. 33	Mar. 24, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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Key to Abbreviations

RR	Revenue Ruling
RP	Revenue Procedure
TD	Treasury Decision
CD	Court Decision
PL	Public Law
EO	Executive Order
DO	Delegation Order
TDO	Treasury Department Order
TC	Tax Convention
SPR	State of Procedural Rules
PTE	Prohibited Transaction Exemption

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-35, page 4.
Accounting methods; hybrid method. A financial institution using the accrual method of accounting for all items of income and expense, except for interest income for commercial loans and mortgage loans, is not using a permissible method of accounting.

LR-3-77, page 14.
Proposed amendments to the regulations under sections 904 and 1502 of the Code relate to the recapture of foreign losses.

EXCISE TAXES

Rev. Rul. 86-36, page 4.
Communications; lease of teletypewriter terminal. Amounts paid by a lessee for the lease of a teletypewriter terminal are not subject to the communications tax imposed by section 4251 of the Code. Rev. Rul. 73-401 modified.

Rev. Rul. 86-37, page 5.
Obsolete rulings. Additional obsolete revenue procedures and revenue rulings are listed.

ADMINISTRATIVE

Rev. Proc. 86-13, page 7.
Forms; magnetic tape; Form W-4; reporting requirements. Requirements and conditions are set forth for submitting certain Forms W-4, Employee's Withholding Allowance Certificates, on magnetic tape instead of filing paper returns. Rev. Proc. 84-41 superseded.

Announcement 86-27, page 30.
Certain errors in Publication 510, Excise Taxes for 1986 (Revised October 1985) are corrected.

Announcement 86-28, page 30.
Publication 526, Rental Property, and Publication 17, Your Federal Income Tax, contain errors in examples relating to the reporting of rental income and expenses.

Announcement 86-33, page 30.
Rev. Rul. 86-33 is corrected.

Finding Lists begin on page 33.
Announcement of Suspensions on page 31.
Announcement of the Notice of Proposed Rulemaking on page 32.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 446.—General Rule for Methods of Accounting

26 CFR 1.446-1: General rule for methods of accounting.

Accounting methods; hybrid method. A financial institution using the accrual method of accounting for all items of income and expense, except for interest income from commercial loans and mortgage loans, is not using a permissible method of accounting.

Rev. Rul. 86-35

ISSUE

Is the taxpayer's method of accounting, which is a combination of the accrual and cash receipts and disbursements methods, a permissible method of accounting under section 446(c) of the Internal Revenue Code, under the circumstances described below?

FACTS

The taxpayer, a financial institution, has for several years consistently reported all items of income and expense on the accrual method of accounting except for interest income from commercial loans and mortgage loans, which is reported on the cash receipts and disbursements method.

LAW AND ANALYSIS

Section 446(b) of the Code provides that if no method of accounting has been regularly used by a taxpayer, or the method used does not clearly reflect income, the computation of taxable income shall be made under such method as, in the opinion of the Secretary, does clearly reflect income.

Section 446(c) of the Code enumerates methods of accounting taxpayers may use to compute taxable income. The use of these permissible methods is subject to the provisions of 446(b). That is, the accounting method used by a taxpayer must clearly reflect income. Such permissible methods are the cash receipts and disbursements method, the accrual method, any other method permitted under chapter 1 of the Code, and combinations of these methods permitted under the regulations.

Section 1.446-1(c)(1)(iv)(a) of the Income Tax Regulations provides that any combination of methods of accounting will be permitted if it clearly reflects income and is consistently used. A taxpayer using the accrual method of accounting with respect to purchases and sales may use the cash receipts and disbursements method in computing all other items of income and expense. However, a taxpayer who uses the cash receipts and disbursements method of accounting in computing gross income from a trade or business must use the cash receipts and disbursements method in computing expenses of such trade or business. Similarly, a taxpayer who uses the accrual method of accounting in computing business expenses must use the accrual method in computing items affecting gross income in such trade or business.

Rev. Rul. 75-171, 1975-1 C.B. 140, concerns a real estate developer who uses the accrual method of accounting for all items of income and expense except for lot sale contracts, which are reported on the installment method. The revenue ruling addresses the proper method of reporting the interest income attributable to the lot sale contracts. Rev. Rul. 75-171 concludes that the interest income must be reported on the accrual method because, under section 1.446-1(c)(1)(iv)(a) of the regulations, if the accrual method is used for deducting business expenses, then, in order to clearly reflect income, the accrual method must also be used for computing items affecting gross income.

The fact that the taxpayer consistently reported its income using the method described above does not mean that the method clearly reflects income. A failure to clearly reflect income over many years cannot be justified on grounds of tenure. *Coors v. Commissioner*, 60 T.C. 368, 395 (1973), *aff'd*, 519 F.2d 1280 (10th Cir. 1975), *cert. denied*, 423 U.S. 1087 (1976); *Madison Gas and Electric Company v. Commissioner*, 72 T.C. 521, 554 (1979), *aff'd on another issue*, 633 F.2d 512 (7th Cir. 1980).

In the present situation, the taxpayer uses the accrual method of accounting in computing business expenses for all its operations, including expenses relating to the mortgage and commercial loan operations. In order to clearly reflect its income, the taxpayer must report interest income from commercial loans and mortgage loans on the accrual method.

HOLDING

The taxpayer's method of accounting, which is a combination of the accrual and cash receipts and disbursements methods, is not a permissible method of accounting under section 446(c) of the Code.

Any change by the taxpayer from its present method of reporting interest income is a change in method of accounting subject to the provisions of sections 446 and 481 of the Code and the regulations thereunder.

This ruling is identified as a designated ruling pursuant to section 5.12(2) of Rev. Proc. 84-74, 1984-2 C.B. 736.

Section 3402.—Income Tax Collected at Source

26 CFR 31.3402(b)-1: Percentage method of withholding.

Requirements and conditions for submitting Forms W-4 on magnetic tape. See Rev. Proc. 86-13, page 7.

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26 CFR 31.3402(f)(5)-1: Form and contents of withholding exemption certificates.

Requirements and conditions for submitting Forms W-4 on magnetic tape. See Rev. Proc. 86-13, page 7.

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26 CFR 31.3402(h)(4)-1: Other methods.

Requirements and conditions for submitting Forms W-4 on magnetic tape. See Rev. Proc. 86-13, page 7.

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26 CFR 31.3402(p)-1: Voluntary withholding agreements.

Requirements and conditions for submitting Forms W-4 on magnetic tape. See Rev. Proc. 86-13, page 7.

Section 4251.—Imposition of Tax

26 CFR 49.4251-1: Imposition of tax.
(Also Section 4252.)

Communications; lease of teletypewriter terminal. Amounts paid by a lessee for the lease of a teletypewriter terminal are not subject to the communications tax imposed by section 4251 of the Code. Rev. Rul. 73-401 modified.

Rev. Rul. 86-36

ISSUE

If amounts are paid for the leasing of a teletypewriter terminal, are those amounts subject to the communications excise tax imposed by section 4251 of the Internal Revenue Code?

LAW AND ANALYSIS

Section 4251 of the Code imposes a tax on amounts paid for communications services, including teletypewriter exchange service.

Section 4252(c) of the Code defines "teletypewriter exchange service" as access from a teletypewriter or other data station to the teletypewriter exchange system of which such station is a part, and the privilege of intercommunication by such station with substantially all persons having teletypewriter or other data stations constituting a part of the same teletypewriter exchange system, to which the subscriber is entitled upon payment of a charge or charges.

Rev. Rul. 73-401, 1973-2 C.B. 363, describes certain companies which sell and lease communications equipment, such as telephones, switchboards, teletypewriter machines, and related equipment, but which are not otherwise engaged in providing communications services. The equipment is sold or leased to customers who use the equipment in connection with telephone service or teletypewriter exchange service provided by communications companies unrelated to the companies selling or leasing the equipment. The revenue ruling holds, in part, that amounts paid to lease teletypewriter equipment for use in connection with a taxable communications service are taxable under section 4251 of the Code.

In *Trans-Lux Corporation v. United States*, 696 F.2d 963 (Fed. Cir. 1982), the court held that payments for the lease of a teletypewriter terminal are not subject to the federal communications tax of teletypewriter exchange service imposed by section 4251 of the Code. The payments are not subject to the tax because the lease of the terminal does not provide access to a teletypewriter exchange system on the privilege of intercommunication with all persons constituting a part of the same teletypewriter exchange system.

The Internal Revenue Service will follow the decision in *Trans-Lux Corporation* with regard to the taxation of amounts paid to lease teletypewriter terminals, whether such terminals are provided by a company that also provides a teletypewriter exchange service or by a company that does not provide such a service.

HOLDING

Amounts paid by a lessee for the lease of a teletypewriter terminal are not subject to the communications excise tax imposed by section 4251 of the Code.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 73-401 is modified.

Section 4252.—Definitions

Whether amounts paid for the leasing of the teletypewriter terminal are subject to the communications tax imposed by section 4251 of the Code. See Rev. Rul. 86-36, above.

Section 6001.—Notice or Regulations Requiring Records, Statements, and Special Returns

26 CFR 31.6001-5: Additional records in connection with collection of income tax at source of wages.

Requirements and conditions for submitting Forms W-4 on magnetic tape. See Rev. Proc. 86-13, page 7.

Section 6361.—General Rules [Collection of State Individual Income Taxes]

Requirements and conditions for submitting Forms W-4 on magnetic tape. See. Rev. Proc. 86-13. page 7.

Section 7805.—Rules and Regulations

26 CFR 301.7805-1: Rules and regulations.

Obsolete rulings. Additional obsoleted revenue procedures and revenue rulings are listed.

Rev. Rul. 86-37

The Internal Revenue Service periodically reviews rulings that were published in the Internal Revenue Bulletin. Although focused on rulings published after 1952, this review is consistent with the objectives of the program (announced by Rev. Proc. 67-6, 1967-1 C.B. 576) for the review of rulings published in the Internal Revenue Bulletin before 1953. That program sought to identify, and to include in published lists, those rulings which, although not specifically revoked or superseded, are not considered determinative with respect to future transactions. As a result of this review of post-1952 rulings, the Service published Rev. Rul. 69-227, 1969-1 C.B. 315, Rev. Rul. 72-622, 1972-2 C.B. 652, Rev. Rul. 74-624, 1974-2 C.B. 406, Rev. Rul. 76-315, 1976-2 C.B. 449, and Rev. Rul. 78-231, 1978-1 C.B. 450, which declared obsolete numerous rulings having primary application in the excise tax area.

Upon further review of rulings in the excise tax area, the additional rulings and procedures listed below, although not specifically revoked or superseded, have been found to be not determinative with respect to future transactions because the applicable statutory provisions have been changed. Accordingly, the rulings listed below are hereby declared to be obsolete.

Rev. Proc. No.	**C.B. Citation**
67-39	1967-2 C.B. 673
74-48	1974-2 C.B. 504
74-49	1974-2 C.B. 505

Rev. Rul. No.	**C.B. Citation**
99	1953-1 C.B. 461
54-319	1954-2 C.B. 398
54-415	1954-2 C.B. 428
55-650	1955-2 C.B. 497
55-651	1955-2 C.B. 497
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73-291	1973-2 C.B. 368
74-124	1974-1 C.B. 320
75-219	1975-1 C.B. 358
77-178	1977-1 C.B. 43

The purpose of obsoleting the rulings listed above is to make clear that the rulings are not determinative with respect to future transactions. It is not the purpose of this revenue ruling to determine their applicability to past transactions.

Other rulings published after 1952 relating to excise tax matters will continue to be reviewed to ascertain those that are inapplicable to future transactions.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.602: Tax forms and instructions. (Also Part I, Sections 3402, 6001, 6361; 31.3402(b)-1, 31.3402(f)(5)-1, 31.3402(h)(4)-1, 31.3402(p)-1, 31.6001-5.)

Rev. Proc. 86-13

PART A—GENERAL

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to update Rev. Proc. 84-41, 1984-1 C.B. 515, concerning the requirements and conditions for submitting certain Forms W-4, Employee's Withholding Allowance Certificates, on magnetic tape instead of filing paper returns. All employers are required to send to the Internal Revenue Service copies of all Forms W-4 submitted by their employees who claim the following:

(a) 15 or more withholding allowances, or

(b) exempt status and usually earn more than $200 a week at the time the Form W-4 was filed.

Form W-4 information may be filed on magnetic tape and sent monthly to IRS.

SEC. 2. NATURE OF CHANGES

The following changes have been included in this revenue procedure:

.01 Part A, Sec. 8 has been revised to show transfer of magnetic media processing from all service centers to the Internal Revenue Service National Computer Center in Martinsburg, WV, effective JANUARY 1, 1986. References to service center filing and magnetic media coordinators at the service centers have been corrected throughout.

.02 Part B, Sec. 1 has been revised to identify which types of tape files are compatible with current processing equipment.

.03 In Part B, Sec. 1.03 a requirement has been added that recording code information is to be shown on the external tape label.

.04 In Part B, the following fields have been deleted from the W-4 Magnetic Tape Record: Number of W-4's Submitted, previously in positions 159-163; Employer Name Line 3, previously in positions 249-283; Employer Name Line 4, previously in positions 284-318; and the field for "IRS USE," previously in positions 396-400. The record length has been shortened to a total of 320 positions, and the remaining fields have been renumbered accordingly. Maximum block size is now 3,200 characters.

.05 In Part B, under Description and Remarks for the Student Status Field in position 149 of the W-4 Magnetic Tape Record, the remarks have been revised to indicate that if student status is not claimed, or if there is no entry, a blank will be entered.

.06 In Part B, under Description and Remarks for the Allowances field in positions 150 and 151 of the W-4 Magnetic Tape Record, the remarks have been revised to indicate that if there is no entry, or if the employee claimed exempt status, blanks will be entered.

PLEASE ENSURE THAT YOUR PROGRAM IS UPDATED TO INCORPORATE THE ABOVE CHANGES.

SEC. 3. APPLICATION FOR MAGNETIC MEDIA REPORTING

.01 Tape reporting is not restricted to employers with the ability to submit all their information on magnetic tape; a combination of tape records and paper documents is acceptable as long as there is no duplication or omission of documents.

.02 Employers or transmitters who desire to file statements in the form of magnetic tape must file a letter of application on Form 4419, Application for Magnetic Media Reporting of Information Returns. See Part A, Sec. 8 for information on where to file.

The letter of request must contain the following:

(a) Name, address, and employer identification number of the person, organization, or entity making the request.

(b) Name, title, and telephone number of the person to contact regarding the request.

(c) Estimate of the number of Forms W-4 to be reported in tape format, and the number, if any, expected to be reported on copies of paper Forms W-4.

(d) Type and nature of equipment to be used to prepare the tape such as manufacturer and model of the mainframe and tape drives, tape width (½", ¾", etc.), density (characters per inch), recording code (BCD, Excess 3, Octal, etc.).

(e) Signature of the official responsible for the preparation and submission of Forms W-4 to the Service.

.03 The Service will act on applications and notify applicants of authorization to file or of disapproval within 30 days of receipt of an application. No magnetic tape returns may be filed with the Service until authorization to file is received.

.04 Only employers or transmitters using equipment which can produce tape files meeting the specifications in Part B, Sec. 1, will have their applications approved.

.05 In general, once authorization to file on magnetic tape has been granted, such approval will continue in effect in succeeding years, providing that the requirements of this revenue procedure are met and there are no equipment changes by the employer or transmitter. However, new applications are required whenever any of the following situations arise:

(a) If the users change from equipment producing compatible tapes.

(b) If the users submit tapes that are not listed as compatible.

(c) If the users discontinue tape reporting for one or more quarters then decide to resume this method of reporting.

SEC. 4. FILING DATES

.01 Magnetic tape reporting of Forms W-4 to the Service must be at least quarterly (monthly reporting is encouraged) following the quarter ending due dates below:

Period Covered	Due Date
Jan. 1 thru March 31	April 30
Apr. 1 thru June 30	July 31
July 1 thru Sept. 30	October 31
Oct. 1 thru Dec. 31	January 31

SEC. 5. FILING OF MAGNETIC MEDIA REPORTS

.01 Packaging, shipping, and mailing instructions will be provided by the Service to all approved filers within 45 days of the granting of approval. A magnetic tape reporting package, which includes all necessary transmittals and labels, will be mailed to all approved filers.

.02 Employers or transmitters may submit a portion of their Forms W-4 information on magnetic tape and the remainder on paper forms, provided there is NO DUPLICATE FILING. A cover letter that includes the employer's name, address, employer identification number, and number of Forms W-4 being submitted must accompany all paper Forms W-4 sent to the Service. Form 6466, Transmittal of Magnetic Tape of Form W-4, Employee's Withholding Allowance Certificate, must be used to transmit magnetic tape shipments.

.03 The affidavit that appears on Form 6466 for tape submission must be signed by the employer, the transmitter, service bureau, or disbursing agent who must:

(a) have the authority to sign the affidavit under an agency agreement (either oral, written, or implied) that is valid under State law; and

(b) have the responsibility (either oral, written, or implied) conferred on it by the employer to request taxpayer identification numbers of employees reported on magnetic tape or paper returns; and

(c) sign the affidavit and add the caption "For: (name of employer)."

.04 Although a duly authorized agent signs the affidavit, the employer is held responsible for the accuracy of Forms W-4 contained on magnetic tape.

.05 EMPLOYERS MUST SEND PAPER FORMS W-4 WITH THE REQUIRED COVER LETTER TO THE INTERNAL REVENUE SERVICE CENTER TO WHICH THEY FILE FORMS 941. Magnetic Media files must be submitted to the Internal Revenue Service National Computer Center in Martinsburg, WV, as prescribed in Part A, Sec. 8.

SEC. 6. PROCESSING OF MAGNETIC MEDIA STATEMENTS

.01 THE MAGNETIC TAPE SPECIFICATIONS CONTAINED IN PART B OF THE REVENUE PROCEDURE MUST BE STRICTLY ADHERED TO. If files are unprocessable, they will be returned to the filer for correction and resubmission of tapes or for submission of copies of paper Forms W-4. Corrected files must be submitted to the Service as soon as possible. If the delay will be more than two weeks, contact the magnetic media coordinator for instructions.

.02 The Service will process the information from the original tapes and will return the original tapes to the employer. Normally tapes will be returned either within three months after the quarterly due date for submission to the Service or within three months after actual receipt of acceptable tapes, whichever is later.

SEC. 7. EFFECT ON PAPER DOCUMENTS

.01 Magnetic tape reporting to the Service eliminates the need to submit copies of paper Forms W-4. However, employers must maintain the original Forms W-4 for their records.

.02 If part of the Forms W-4 are reported on magnetic tape and the remainder are reported on paper forms, those paper statements must be filed on the prescribed forms.

SEC. 8. ADDITIONAL INFORMATION

.01 Beginning JANUARY 1, 1986, magnetic media processing for all service centers will be centralized at the Internal Revenue Service National Computer Center in Martinsburg, WV. Functions previously performed by the magnetic media coordinators at the service centers will be performed at the National Computer Center.

.02 All magnetic media files forwarded on or after JANUARY 1, 1986, must be submitted to the Internal Revenue Service National Computer Center at the address shown below. In addition, all correspondence or contacts regarding magnetic media related forms, publications, information and applications for reporting on magnetic media must be directed to:

Magnetic Media Reporting
P.O. Box 1359
Internal Revenue Service
National Computer Center
Martinsburg, WV 25401-1359

.03 Only MAGNETIC MEDIA reporting is to be submitted to the National Computer Center. ALL PAPER FORMS W-4 WILL CONTINUE TO BE SENT TO THE APPROPRIATE SERVICE CENTER.

PART B—MAGNETIC TAPE SPECIFICATIONS

SECTION 1. GENERAL

.01 These specifications prescribe the required format and content of the records to be included in the file but not the methods or equipment to be used in their preparation. Usually, the Service will be able to process, without translation, any compatible tape file. To be compatible, a tape file must meet all of the following specifications:

(a) Type of tape—½ inch Mylar base, oxide coated

(b) Interrecord Gap—¾ inch

(c) Recording Code—9 track ASCII (American Standard Coded Information Interchange) with:

(1) Odd parity, and

(2) A density of 800, 1600, or 6250 BPI (bits per inch).

.02 Conversion facilities are currently available for the following tapes:

(a) Recording Code—9 track EBCDIC (Extended Binary Coded Decimal Interchange Code) with:

(1) Odd parity, and

(2) A density of 800, 1600, or 6250 BPI.

(b) Recording Code—7 track BCD (Binary Coded Decimal) with:

(1) Even or odd parity, and

(2) A density of 556 or 800 BPI.

.03 The employer or the transmitter must affix an external label to each tape with the following information:

(a) Name of transmitter

(b) Number of data records on that reel

(c) Recording Code (ASCII, EBCDIC or BCD)

(d) Density (556, 800, 1600, or 6250 BPI)

(e) Track (7 or 9)

(f) Parity (odd or even)

(g) Manufacturer and model of main frame and tape drives

(h) Sequence number of reel and total number of reels in the file (for example, 1 of 3, 2 of 4)

.04 All records, including Header and Trailer Labels (if used), must be transmitted at the same density.

.05 Do not submit an employee W-4 record without the required employer identification information. Every record must contain both employee and employer data.

SEC. 2. LABEL CONVENTIONS

.01 Header Labels, Trailer Labels,

Record Marks, and Tape Marks are all optional. They may be used as required by the transmitter's equipment or programming. If used they must conform to the following standards:

(a) Header Labels

(1) Transmitters may use standard headers, provided they begin with 1HDR, HDR1, VOL1 or VOL2.

(2) Header labels may not exceed 80 characters in length.

(b) Trailer Labels

(1) Standard trailer labels may be used provided that they begin with 1EOR, 1EOF, EOR1, or EOF1.

(2) Trailer labels may not exceed 80 characters in length.

(c) Record Marks

(1) Special character used to separate blocked records on tape.

(2) Can be written only at the end of a record or block.

(3) All records are of uniform length; therefore, record marks are not necessary on this file. However, if you choose to use record marks, for odd parity tapes, use BCD bit configuration of 011010—for even parity, use 111010.

(d) Tape Marks

(1) Used to signify the physical end of the recording on tape.

(2) Tape marks, if used, must be BCD configuration 001111 in even parity.

(3) May follow the header label and precede and/or follow the trailer label.

SEC. 3. RECORD LENGTH AND BLOCKING

.01 Tape records prescribed in the specifications may be blocked or unblocked, subject to the following:

(a) All data records are of a fixed length of 320 positions.

(b) All records may be blocked, except header and trailer labels.

(c) If blocking is used (more than one record per block), the desired blocking factor is ten records per block. At no time may a block contain more than 3,200 characters, but a smaller block size may be used if necessary. If sufficient records are not available for a full block, the remainder should be "padded" with 9s to fill all unused positions. Do not pad the block with blanks or create blank records.

RECORD NAME: W-4 MAGNETIC TAPE RECORD

Tape Position	Field Title	Length	Description and Remarks
1-9	Employee Social Security Number (SSN)	9	Required. Must be the valid 9-digit number assigned to the employee. DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s or ALL ZEROES.
10-44	Employee Name Line 1	35	Required. Enter the name of the employee whose SSN appears in tape positions 1-9. Enter the complete name in the following order: first name, middle name (if present), and surname. (Use initials for the first and middle names where necessary to insure that the entire employee surname fits in tape positions 10-44.) If fewer than 35 characters are required, left justify and fill unused positions with blanks. ALLOWABLE CHARACTERS ARE ALPHAS, HYPHENS, BLANKS, A MINIMUM OF ONE AND A MAXIMUM OF TWO CARETS (<). (1) A blank must be surrounded by alphas or continued to the end of the field (for example, ab̸ . . . b̸, ab̸a). (2) Hyphens must be surrounded by alphas and must never occur in the first position of a name unless immediately followed by a caret. A hyphen in the first position is to identify an employee with surname only. (3) A caret is used to define an internal name control. It must immediately precede the employee surname in place of the blank. A second caret is used to separate a suffix from the surname (for example, JOHN J.<BLACK; BILL<OAK<JR; AMY FERN<BROWN<DECD).
45-79	Employee Name Line 2	35	Optional. This line is designated for an "in care of" (℅) situation. Left justify and fill with blanks. ALLOWABLE CHARACTERS ARE ALPHAS, BLANKS, NUMERICS, AMPERSANDS, HYPHENS, AND SLASHES. Note: Same exceptions as mentioned in employee name line 1. A percent sign (%) is not valid—use ℅ if necessary.

RECORD NAME: W-4 MAGNETIC TAPE RECORD—(Continued)

Tape Position	Field Title	Length	Description and Remarks
80-114	Employee Street Address	35	Required. Enter street address of employee. Left justify and fill unused positions with blanks. ALLOWABLE CHARACTERS ARE ALPHAS, BLANKS, NUMERICS, AMPERSANDS, HYPHENS AND SLASHES. Position one is an alpha or numeric; hyphens and slashes are surrounded by alphas; ampersands are surrounded by blanks.
115-139	Employee City	25	Required. Enter city of employee. Left justify and fill unused positions with blanks. If foreign address, enter city and country. ALLOWABLE CHARACTERS ARE ALPHAS, BLANKS, NUMERICS, AND HYPHENS. Position one is an alpha or numeric; hyphens are surrounded by alphas or numerics.
140-141	Employee State	2	Required. Enter the two character state code of employee—must be one of the following:

State	Code
Alabama	AL
Alaska	AK
Arizona	AZ
Arkansas	AR
California	CA
Colorado	CO
Connecticut	CT
Delaware	DE
District of Columbia	DC
Florida	FL
Georgia	GA
Guam	GU
Hawaii	HI
Idaho	ID
Illinois	IL
Indiana	IN
Iowa	IA
Kansas	KS
Kentucky	KY
Louisiana	LA
Maine	ME
Maryland	MD
Massachusetts	MA
Michigan	MI
Minnesota	MN
Mississippi	MS
Missouri	MO
Montana	MT
Nebraska	NE
Nevada	NV
New Hampshire	NH
New Jersey	NJ
New Mexico	NM
New York	NY
North Carolina	NC
North Dakota	ND
Ohio	OH
Oklahoma	OK

RECORD NAME: W-4 MAGNETIC TAPE RECORD—(Continued)

Tape Position	Field Title	Length	Description and Remarks	
			Oregon	OR
			Pennsylvania	PA
			Puerto Rico	PR
			Rhode Island	RI
			South Carolina	SC
			South Dakota	SD
			Tennessee	TN
			Texas	TX
			Utah	UT
			Vermont	VT
			Virgin Islands	VI
			Virginia	VA
			Washington	WA
			West Virginia	WV
			Wisconsin	WI
			Wyoming	WY
			Foreign Address	XX
142-146	Employee ZIP Code	5	Required. Enter ZIP Code of employee. Fill with blanks if unavailable. ALLOWABLE CHARACTERS ARE FIVE (5) NUMERICS OR FIVE (5) BLANKS. Enter first five (5) digits if more than five digits are present. Blank fill *only* if you are unable to ascertain the ZIP Code.	
147	Marital Status	1	Required. Enter appropriate code from the table below:	
			Marital Status Designated	Code
			Single	S
			Married	M
			Married, withhold at single rate	W
			No marital status designated	A
148	Exempt Status	1	Required. Enter "E" if employee claims exempt status; otherwise, blank.	
149	Student Status	1	Required. If full-time student status is claimed, enter the alpha "Y"; if not, or no entry, enter blank.	
150-151	Allowances	2	Required. Must be a two (2) digit numeric field corresponding to the number of allowances claimed by employee. (It is not necessary to file this W-4 with the Service if the number of allowances is less than fifteen (15) and exempt status is not claimed.) If no entry, or employee claimed exempt status, enter blanks. If entry is greater than 99, enter 99.	
152-158	Additional Amount of Withholding	7	Required. Enter numerics only. Enter the additional amount of withholding each pay period. Field is dollars and cents. Right justify and zero fill. Do not enter dollar signs, commas, decimal points, or negative numbers. If no entry, zero-fill.	
159-164	W-4 Date	6	Required. Enter date located on signature line of W-4. If no date entered, generate current system date. Format as MMDDYY where MM = 01-12, DD = 01-31, and YY = 82, 83, etc. Exempt Status W-4 (1983 and subsequent)—Compare "year effective date" on Line 6B to signature date. If year entered on Line 6B is later than signature date, use W-4 date as a 01/01 receipt for	

RECORD NAME: W-4 MAGNETIC TAPE RECORD—(Continued)

Tape Position	Field Title	Length	Description and Remarks
			subsequent calendar year (e.g., Line 6B of Form W-4 shows an exempt status date of 1984 but signature date is 10/30/83, use 01/01/84 as Form W-4 date.)
165-173	Employer Identification Number	9	Required. The 9 digit number assigned to the employer by IRS. DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s or ALL ZEROES.
174-208	Employer Name Line 1	35	Required. Enter the name of the employer as it appears on your employment tax forms (e.g., Form 941). Any extraneous information must be deleted from this name line. Left justify and fill with blanks. ALLOWABLE CHARACTERS ARE ALPHAS, BLANKS, NUMERICS, AMPERSANDS, HYPHENS AND SLASHES. Position one is an alpha or numeric; hyphens and slashes are surrounded by alphas—ampersands are surrounded by blanks.
209-243	Employer Name Line 2	35	Optional. If the employer name requires more space than is available in Employer Name Line 1, enter the remaining portion of the name in this field. Left justify and fill with blanks. ALLOWABLE CHARACTERS ARE ALPHAS, BLANKS, NUMERICS, AMPERSANDS, HYPHENS, AND SLASHES. Position one is an alpha or numeric; hyphens and slashes are surrounded by alphas—ampersands are surrounded by blanks.
244-278	Employer Street Address	35	Required. Enter street address of employer. Left justify and fill unused positions with blanks. ALLOWABLE CHARACTERS ARE ALPHAS, BLANKS, NUMERICS, AMPERSANDS, HYPHENS, AND SLASHES. Position one is an alpha or numeric; hyphens and slashes are surrounded by alphas—ampersands are surrounded by blanks.
279-303	Employer City	25	Required. Enter city of employer. Left justify and fill unused positions with blanks. If foreign address, enter city and country. ALLOWABLE CHARACTERS ARE ALPHAS, BLANKS, NUMERICS, AND HYPHENS. Position one is an alpha or numeric, hyphens are surrounded by alphas; blanks are surrounded by alphas or numerics or continued to the end of the field.
304-305	Employer State	2	Required. Enter State Code of Employer. Must be one of the state abbreviations shown above in the state abbreviation table for Employee State (Tape Positions 140-141).
306-310	Employer ZIP Code	5	Required. Enter ZIP Code of Employer. ALLOWABLE CHARACTERS ARE FIVE (5) NUMERICS OR FIVE (5) BLANKS. Enter first five (5) digits if more than five digits are present. Blank fill *only* if you are unable to ascertain Employer's ZIP Code.
311-315	Transmitter Control Code	5	Required. Enter 5-digit Transmitter Control Code (TCC) assigned by the Service.
316	"BLANK" Representation	1	Required. Enter character used to represent a blank.

RECORD NAME: W-4 MAGNETIC TAPE RECORD—(Continued)

Tape Position	Field Title	Length	Description and Remarks
317	"HYPHEN" Representation	1	Required. Enter character used to represent a hyphen.
318	"SLASH" Representation	1	Required. Enter character used to represent a slash.
319	"AMPERSAND" Representation	1	Required. Enter character used to represent an ampersand.
320	"CARET" Representation	1	Required. Enter character used to represent a caret.

SEC. 4. EFFECT OF OTHER DOCUMENTS

Rev. Proc. 84-41 is superseded.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Recapture of Overall Foreign Losses

LR-3-77

SUMMARY: This document contains proposed regulations relating to the recapture of overall foreign losses. Changes to the applicable tax law were made by the Tax Reform Act of 1976 [Pub. L. 94-455, 1976-3 C.B. (Vol. 1) 1]. These regulations provide the public with the guidance needed to comply with that Act and would affect all taxpayers receiving income from sources without the United States.

DATES: Written comments and requests for a public hearing must be delivered or mailed by March 25, 1986. The amendments are proposed to be effective in general for taxable years ending after December 31, 1975, except for the amendments under paragraph 2, which are proposed to be effective for taxable years for which the due date (without extensions) for filing returns is after [DATE THAT IS 30 DAYS AFTER THE DATE THESE REGULATIONS ARE PUBLISHED IN THE FEDERAL REGISTER AS FINAL REGULATIONS].

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-3-77), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Nerman D. Hubbard of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T (LR-3-77), (202) 566-3289, not a toll-free call.

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 904 (f) of the Internal Revenue Code of 1954. These amendments are proposed to conform the regulations to section 1032 of the Tax Reform Act of 1976 (90 Stat. 1624) [Pub.L. 94-455, 1976-3 C.B. (Vol. 1) 1, 100] and are to be issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917, 26 U.S.C. §7805). The amendments under paragraph 2 are also to be issued under the authority contained in section 1502 of the Internal Revenue Code (68A Stat. 637, 26 U.S.C. §1502).

STATUTORY PROVISIONS

In 1975, Congress enacted section 907 containing a separate overall foreign tax credit limitation for foreign oil related income. This new separate limitation (section 907(b)) required that foreign oil related income and expenses and deductions related thereto be kept separate from other types of foreign source taxable income and that the provisions of section 904 be applied separately to foreign oil related income. It thus prevented the averaging of taxes on foreign oil related income with taxes on other types of foreign source income and required foreign oil related losses to offset U.S. source income instead of other foreign source income. At the same time, Congress was also concerned about the potential double benefit of having foreign oil related losses offset U.S. source income in one year (as a result of the new limitation) and having the foreign tax credit reduce U.S. tax on foreign oil related income in a subsequent tax year. As a consequence, Congress provided for the recapture of foreign oil related losses under section 907(f).

Recognizing that the same double benefit could occur when non-oil related foreign source losses offset U.S. source income, Congress broadened its original recapture rule to cover other foreign source losses by enacting section 904(f) in the Tax Reform Act of 1976. It also consolidated all of the overall foreign loss recapture rules into section 904(f) by repealing section 907(f) and providing a separate definition of foreign oil related losses in section 904(f)(4).

Section 904(f) provides that a taxpayer that sustains an overall foreign loss in any taxable year beginning after December 31, 1975, or a foreign oil related loss in any taxable year ending after December 31, 1975 (and beginning before January 1, 1983), is required to recapture such loss in a succeeding taxable year in which it seeks the benefits of the foreign tax credit under section 901 or the Puerto Rico and possession tax credit under section 936. Recapture is accomplished by recharacterizing a portion of the taxpayer's foreign source taxable income as U.S. source income for purposes of the foreign tax credit limitation under section 904 and the allowable possession tax credit under section 936(a)(1). The effect of such recharacterization is a reduction in the taxpayer's foreign tax credit limitation or possession credit. Such reduction occurs annually until such time as the entire overall foreign loss has been recaptured.

EFFECT OF SEPARATE LIMITATIONS ON SECTION 904(f)

When Congress repealed section 907(f) and added the separate definition of a foreign oil related loss to section 904(f), it evidenced its intent that foreign oil related losses were to be determined separately without regard to other types of foreign source taxable income. It did not, however, enact a separate recapture provision for foreign oil related losses. This was unnecessary because the separate limitation for foreign oil related income under section 907(b) required the separate application of all the provisions of section 904, including 904(f), to foreign oil related income. Thus, a foreign oil related loss, as defined in section 904(f)(4) (prior to September 3, 1982), is to be recaptured by applying the recapture rules of section 904(f) separately to foreign oil related income.

Even if Congress had not included a separate definition of a foreign oil related loss in section 904(f)(4), the separate determination of foreign oil related losses and the recapture of such losses only out of foreign oil related income is consistent with the operative effect of the separate limitation for foreign oil related income. Such limitation required that foreign oil related income and expenses and deductions properly allocated and apportioned thereto be placed in a separate basket. The fact that the netting of foreign oil related income and expenses in the basket results in a loss does not change the fact that the foreign oil related basket must be kept separate from other baskets. Accordingly, foreign oil related losses are determined without regard to foreign source income or losses subject to another separate limitation. (The separate limitation for foreign oil related income was repealed in 1982; transitional rules are discussed below.)

Similarly, the separate limitations for certain interest income (section 904(d)(1)(A)), DISC dividend income (section 904(d)(1)(B)), foreign trade income (section 904(d)(1)(C)), distributions from a FSC (section 904(d)(1)(D)), and other foreign source income (section 904(d)(1)(E)), require a determination of taxable income (or loss) under each separate limitation without taking into consideration foreign source income and deductions subject to another separate limitation. In addition, section 936 requires a qualifying corporation to make separate determinations of its foreign taxable income from sources within a possession (income eligible for the section 936 credit) and other foreign source taxable income (income eligible for the section 901 credit). It thus creates another separate limitation.

As a consequence, for purposes of section 904(f), there are seven types of overall foreign losses, one under each of the above mentioned separate limitations. For instance, there can be an overall foreign "interest income" loss, an overall foreign "DISC dividend" loss, an overall "foreign trade income" loss, and overall "FSC distributions" loss, an overall "other" foreign loss, an overall foreign oil related loss, and an overall foreign "section 936" loss. For purposes of recapture it is necessary and consistent with the concept of the separate limitations that any overall foreign loss under a separate limitation be recaptured only out of foreign source taxable income subject to such separate limitation.

DETERMINATION OF OVERALL FOREIGN LOSSES

Section 1.904(f)-1(c) of the proposed regulations sets forth rules for determining a taxpayer's overall foreign losses in any taxable year. Generally, a taxpayer sustains an overall foreign loss in any taxable year in which its gross income from sources without the United States is exceeded by the sum of the deductions properly allocated or apportioned to such income. However, this is determined separately with respect to each of the seven separate limitations discussed above. For example, a taxpayer sustains an overall "other" foreign loss under the section 904(d)(1)(E) separate limitation in any taxable year in which its gross income subject to such separate limitation is exceeded by the sum of the deductions properly allocated and apportioned thereto. Thus, a taxpayer may have an overall foreign loss under its section 904(d)(1)(E) limitation in the same taxable year in which it has foreign DISC dividend income subject to the section 904(d)(1)(B) limitation which exceeds the sum of the deductions properly allocated or apportioned thereto.

THE OVERALL FOREIGN LOSS ACCOUNTS

A taxpayer sustaining any type of overall foreign loss is required under §1.904(f)-1(b) to establish an overall foreign loss account. A taxpayer is required to make additions and reductions to the account as specified in §1.904(f)-1(d) and (e). Generally, the amount of overall foreign loss sustained in the taxable year is added to the overall foreign loss account. In subsequent taxable years in which the loss is recaptured, the amount recaptured is subtracted from such account. Thus, the balance in an overall foreign loss account represents the amount of an overall foreign loss which is subject to recapture. Separate overall foreign loss accounts must be established for losses under each separate limitation.

"BENEFIT" RULE

Although a literal reading of the statute would require recapture of any overall foreign loss, these regulations adopt a tax benefit rule that limits recapture to those overall foreign losses which offset U.S. source income. Thus, in a taxable year in which the taxpayer has no U.S. source income, the exact amount of an overall foreign loss that will be subject to recapture can only be determined after application of the net operating loss deduction rules. To the extent that such foreign source net operating loss offsets foreign source taxable income in the year to which it is carried, there will be no recapture. The "benefit" concept is accomplished under §1.904(f)-1(d)(1) by providing that overall foreign losses are added to the overall foreign loss account only to the extent that they reduce U.S. source income. A similar "benefit" rule is provided for an overall foreign loss that is part of a net capital loss. As a result, an overall foreign capital loss is only recapturable to the extent it offsets U.S. source capital gain net income.

Paragraphs (d)(2) and (3) provide for further adjustments to the amount of overall foreign loss to be added to the applicable account if such amount includes net capital losses. A corporate taxpayer's foreign source net capital loss is reduced by the rate differential between the highest U.S. tax rate on ordinary income under section 11 and the U.S. tax on net capital gain under section 1201(a) before being added to the overall foreign loss account. A noncorporate taxpayer's foreign source net capital loss is reduced by the amount deducted from gross income under section 1202. These reductions are made in order to reflect the lower U.S. tax rate with respect to net capital gains, and thereby to take into account the actual benefit received by the taxpayer from foreign source capital losses that are subject to recapture.

EFFECT OF SECTION 904(b) ADJUSTMENTS ON TREATMENT OF FOREIGN CAPITAL LOSSES AS OVERALL FOREIGN LOSS

When a taxpayer's capital gain net income is reduced by foreign net capital losses, section 904(b) requires the numerator of the taxpayer's foreign tax credit limitation fraction to be reduced by the amount of the reduction in capital gain net income. To the extent that the reduction of capital gain net income is a reduction of U.S. source net capital gain, a further adjustment is made to the numerator of the foreign tax credit limitation fraction to reflect the tax rate differential between ordinary income and net capital gain. If these reductions of the numerator result in a reduction of foreign source taxable income (but not below zero), then, to that extent, the foreign capital loss is already being recaptured for purposes of the foreign tax credit, because the foreign tax credit limitation is already being reduced. Therefore, the amount of the foreign capital losses will not be treated as a recapturable overall foreign loss to the extent of the reduction of foreign source taxable income in the numerator of the foreign tax credit limitation fraction.

RECAPTURE OF OVERALL FOREIGN LOSSES

Section 1.904(f)-2 provides rules for determining the amount of an overall foreign loss subject to recapture in a given year, and for calculating the recapture. In general, the taxpayer is required to recapture a portion of any overall foreign loss equal to the lesser of the balance in the applicable overall foreign loss account or 50 percent of its foreign source taxable income subject to the separate limitation under which the loss arose. Recapture is accomplished by recharacterizing such foreign source taxable income as U.S. source income for purposes of the foreign tax credit limitation fraction. Section 1.904(f)-2(b) provides an ordering rule for determining the amount of a taxpayer's foreign source taxable income for purposes of recapture. Only the amount of foreign source income in the numerator of the foreign tax credit limitation fraction after making the adjustments required under section 904(a) and section 904(b) is subject to recapture. If this ordering rule were not applied, the overall foreign loss account would be reduced by recapturing amounts that were, in effect, already recaptured under other provisions, and thus should not be subject to recapture. Section 1.904 (f)-2(c)(2) provides that a taxpayer may elect to recapture a greater portion of any overall foreign loss than is required by statute. If the taxpayer has foreign source taxable income subject to a separate limitation other than the limitation under which the loss arose, such income is not taken into account in determining the amount of overall foreign loss to be recaptured in such year, nor is such other income subject to recharacterization. Therefore, a taxpayer's DISC dividend income subject to the section 904(d)(1)(B) limitation is not taken into account in determining how much of an overall foreign loss under the section 904(d)(1)(E) limitation is subject to recapture, nor is such income recharacterized for purposes ,of recapturing the section 904(d)(1)(E) overall foreign loss.

RELATIONSHIP OF RECAPTURE TO FOREIGN SOURCE CAPITAL GAIN

Foreign source capital gain net income is included in the foreign tax credit limitation fraction, and is therefore included in foreign source taxable income for purposes of recapture. The ordering rule for determining the amount of foreign source taxable income subject to recapture incorporates the section 904(b) adjustments for the tax rate differential between ordinary income and net capital gain. These adjustments have also been made in determining the amount of overall foreign loss that has been added to the applicable account. Thus, when recapture is applied to foreign source taxable income in the numerator of the limitation fraction, it applies to ordinary income and capital gain simultaneously.

DISPOSITION RULE

Section 1.904(f)-2(d) sets forth rules for recapturing an overall foreign loss in a taxable year in which a taxpayer disposes of property used predominantly outside of the United States in a trade or business. Under section 904(f)(3), a taxpayer making such a disposition is required to recapture an amount of any overall foreign loss equal to the lesser of the taxpayer's remaining overall foreign loss or 100 percent of the foreign source taxable income realized on such disposition.

The rules contained in §1.904(f)-2(d) apply regardless of whether or not the taxpayer actually recognized gain on such disposition. In the case of a disposition of property in which gain is recognized irrespective of §1.904(f)-2(d), paragraph (d)(3) provides that the general recapture rule of §1.904(f)-2(c) is applied prior to applying the special recapture rule for dispositions. If the taxpayer makes a disposition of property from which gain would otherwise not be recognized in that taxable year, §1.904(f)2(d)(4) provides that the taxpayer will be deemed to have recognized gain to the extent of the lesser of: (1) the balance in its overall foreign loss account (plus any overall foreign loss that is part of a net operating loss carryover from a prior year, or that would otherwise be part of a net operating loss for the year of the disposition), or (2) the excess of the fair market value of the property over its adjusted basis. The accelerated recapture rules of §1.904(f)–2(d) are applied first to dispositions in which gain is recognized irrespective of such section, and then to dispositions in which gain is deemed recognized by application of section 904(f)(3) and §1.904(f)-2(d)(4). The ordering rule of §1.904(f)-2(b) applies to determine the amount of gain which is deemed to be recognized, and which therefore will be recaptured. Since this ordering rule is applied before recapture, in some circumstances the application of section 904(b)(3) will recharacterize foreign source gain as U.S. source gain after it has been deemed to be recognized under section 904(f)(3) and §1.904(f)-2(d)(4), but before such gain can be recaptured under §1.904(f)-2(a). If this occurs in a case where the gain would not be recognized but for the application of section 904(f)(3), the overall foreign loss account will, nevertheless, be reduced by the amount of the gain deemed recognized even though the gain was not recharacterized by section 904(f).

Section 1.904(f)-2(d)(5) provides definitions of relevant terms.

SPECIAL RULES FOR NET OPERATING LOSS AND CAPITAL LOSS CARRYBACKS AND CARRYOVERS

Section 904(f)(2) defines an overall foreign loss as the amount by which the gross income for the taxable year from sources without the United States is exceeded by the deductions properly apportioned or allocated thereto. This definition includes not only amounts that reduce income from sources within the United States in the taxable year of the loss, but also amounts that, in carryback and carryover years, reduce income from sources both within and without the United States. Thus, under the statute, all such amounts are overall foreign losses in the loss year and are subject to recapture. In view of this, a foreign source loss that is part of a net operating loss deduction in a taxable year to which carried back or over should not be included in the determination of overall foreign loss for such year because it was included in the overall foreign loss for the year in which it arose. To prevent double counting of such a foreign source loss, section 904(f)(2)(A) specifically excludes net operating loss deductions from the determination of overall foreign losses in carryback or carryover years.

However, these proposed regulations take the position that a foreign source loss cannot be considered an overall foreign loss that is subject to recapture (and, therefore, included in the overall foreign loss account) unless it has reduced income from sources within the United States either in the loss year or in a carryback or carryover year. This position is more liberal than the rule under section 904(f)(2)(A), which would also reduce the foreign tax credit "benefit" in situations in which there has been no counter-vailing benefit to the taxpayer, i.e., the loss did not reduce its U.S. source income. To implement Congress' intent to prevent a double benefit in such a way as to avoid creating a detriment, these proposed regulations consider a foreign source loss to be an overall foreign loss (and thus added to the overall foreign loss account in the loss year) only to the extent that it has reduced U.S. source income in the loss year or in carryback years. Since the losses which are carried forward cannot be determined to have reduced U.S. source income until income in those years has been determined, the net operating loss rules must be applied. If the foreign source loss reduces U.S. source income in those carryforward years, it is added to the overall foreign loss account to that extent in those years. Section 1.904(f)-3 provides that net operating loss and net capital loss carrybacks and carryforwards from foreign source losses are first allocated to foreign source income, which does not give rise to overall foreign losses subject to recapture. This allocation is consistent with the rules applied in *Motors Insurance Corp. v. United States*, 530 F.2d 864 (Ct. Cl. 1976). To the extent that these losses exceed foreign source income in the year to which carried, they are allocated to U.S. source income in that year and are subject to recapture to the same extent as if they had reduced U.S. source income in the year in which they arose.

RECAPTURE OUT OF ACCUMULATION DISTRIBUTIONS OF A FOREIGN TRUST

Section 1.904(f)-4 provides rules for recapture of overall foreign losses out of accumulation distributions of a foreign trust. A taxpayer receiving accumulation distributions that are deemed distributed in preceding years under section 666 first applies the general recapture rules of §1.904(f)-2 to its other foreign source income, after which the amounts of foreign source taxable income deemed distributed in prior years are subject to recapture to the extent of 100 percent of such income or the remaining balance in the overall foreign loss account, if less. An exception from recapture is provided for income deemed distributed in a year for which the taxpayer elects under section 667(d)(1)(B) to deduct, rather than credit, foreign taxes deemed distributed with respect to accumulation distribution.

RECAPTURE OF FOREIGN LOSSES OF DOMESTIC TRUSTS

Section 1.904(f)-5 provides special rules for recapturing overall foreign losses of a domestic trust. In general, the rules of §§1.904(f)-1 through 1.904(f)-4 apply to domestic trusts, except that if foreign source taxable income subject to the separate limitation under which the trust's overall foreign loss arose is distributed to beneficiaries, a portion of the amount of the trust's loss to be recaptured in such year will be allocated to the beneficiaries receiving such income. The overall foreign loss of a trust so allocated to a beneficiary is recaptured by the beneficiary in the same year, in accordance with the rules of §1.904(f)-1 through §1.904(f)-4. If such trust distributes its income in whole or in part, paragraph (c) provides rules for apportioning the amount of the overall foreign loss subject to recapture in that taxable year between the trust and the beneficiaries.

REPEAL OF SEPARATE LIMITATION FOR FOREIGN OIL RELATED INCOME

Section 211 of the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462, 484] repealed the separate limitation for foreign oil related income contained in section 907(b). As a consequence, for taxable years beginning after December 31, 1982 there will no longer be a separate basket of foreign oil related income and no separately determined foreign oil related loss. Instead, foreign oil related income and deductions properly allocated and apportioned thereto are to be netted with other foreign source income subject to the section 904(d)(1)(E) limitation for purposes of determining the amount of foreign source taxable income or overall foreign loss under this limitation.

Section 211 of TEFRA also provided a transitional rule for recapture of pre-1983 foreign oil related and non-oil related losses out of post-1982 section 904(d)(1)(E) foreign source taxable income (which includes foreign oil related income). The transitional rule provides that a pre-1983 foreign source non-oil related loss may not be recaptured out of post-1982 foreign oil related income more rapidly than ratably over an 8-year period (or such shorter period as the taxpayer may select). Likewise, a pre-1983 foreign oil related loss may not be recaptured out of post-1982 non-oil related income more rapidly than ratably over an 8-year (or shorter) period. Section 1.904(f)-6 provides transitional rules for recapturing pre-1983 section 904(d)(1)(E) overall foreign losses and section 907(b) overall foreign losses (foreign oil related losses) out of taxable income subject to the section 904(d)(1)(E) limitation in taxable years beginning after December 31, 1982.

CONSOLIDATED OVERALL FOREIGN LOSSES

Section 1.1502-9(a) requires affiliated corporations filing consolidated returns to calculate their overall foreign losses on a consolidated basis and requires the establishment of consolidated overall foreign loss accounts. It also provides rules for allocating an overall foreign loss sustained by a member of the group in a separate return year or a separate return limitation year to a consolidated overall foreign loss account when such corporation joins in filing a consolidated return. Once the consolidated overall foreign losses have been determined, the rules contained in §1.904(f)-1 through 1.904(f)-6 are applied to recapture such losses. Section 1.1502-9(c) requires that individual members of an affiliated group keep separate notional loss accounts reflecting their portion of any consolidated overall foreign losses. Such notional accounts are reduced, when the consolidated overall foreign losses are recaptured, by the pro rata share (of the total amount recaptured) of each member that contributed to the consolidated overall foreign loss. Further, §1.1502-9 provides rules for allocating a portion of the balance in any consolidated overall foreign loss account to a member that leaves the group before such balance has been fully recaptured. This section also provides rules for recapturing an overall foreign loss that was incurred in a member's separate return limitation year. Such a loss is only recaptured to the extent of the foreign source taxable income of the member that incurred the loss. Finally, this section provides rules for recapturing a consolidated overall foreign loss in taxable years in which the excess loss account of a member is triggered.

Section 1.1502-9 of these proposed regulations provides for recapture of an overall foreign loss which arose in a separate return limitation year only from the separate foreign taxable income of the member of the consolidated group which incurred such overall foreign loss. The appropriateness of this position and whether there should be a recapture of such losses from the consolidated foreign taxable income, rather than solely from the separate foreign taxable income of the member of the consolidated group which sustained the loss will be considered in the final regulations. Taxpayers are invited to comment as to whether the rule in the proposed regulations is the correct one, or whether the alternative, which would recapture an overall foreign loss from a separate return limitation year from consolidated foreign taxable income, is the more appropriate rule.

DRAFTING INFORMATION

The principal author of these proposed regulations is David J. Dean formerly of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies of those comments to the Service.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

Although this document is a notice of proposed rulemaking which solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public comment procedural requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6). The Commissioner of Internal Revenue has determined that this proposed rule is not a major regulation as defined in Executive order 12291 and therefore a regulatory impact analysis is not required.

* * * *

Proposed amendments to the regulations.

Accordingly, the proposed amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority of Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * * Sections 1.904 (f)-2 and 1.1502-9 are also issued under 26 U.S.C. 904(f)(3)(B) are 26 U.S.C. 1502. * * *

Par. 2. The following new sections are added immediately following §1.904(b)-4 to read as set forth below:

§1.904(f)-1 Overall foreign loss and the overall foreign loss account.

(a) *Overview of regulations.* In general, section 904(f) and these regulations apply to any taxpayer that sustains an overall foreign loss (as defined in paragraph (c)(1) of this section) in a taxable year beginning after December 31, 1975. There can be seven types of overall foreign losses: an overall foreign loss under each of the five separate limitations contained in section 904(d)(1), a foreign oil related loss under the section 907(b) limitation (for taxable years ending after December 31, 1975 and beginning before January 1, 1983), and an overall foreign loss with respect to income subject to section 936. Section 1.904(f)-1 provides rules for determining a taxpayer's overall foreign losses, for establishing overall foreign loss accounts, and for making additions to and reductions of such accounts for purposes of section 904(f). Section 1.904(f)-2 provides rules for recapturing the balance in any overall foreign loss account under the general recapture rule of section 904(f)(1) and under the special recapture rule of section 904(f)(3) when the taxpayer disposes of property used predominantly outside the United States in a trade or business. Section 1.904(f)-3 provides rules for allocating overall foreign losses that are part of net operating losses or net capital losses to foreign source income in years to which such losses are carried. Section 1.904(f)-4 provides rules for recapture out of an accumulation distribution of a foreign trust. Section 1.904(f)-5 provides rules for recapture of overall foreign losses of domestic trusts. Section 1,904(f)-6 provides a transitional rule for recapturing a taxpayer's pre-1983 overall foreign losses under the section 904(d)(1)(C) and section 907(b) limitations, prior to their amendment by TEFRA, out of taxable income subject to the section 904(d)(1)(E) limitation (and its predecessor) in taxable years beginning after December 31, 1982. See §1.1502-9 for rules concerning the application of these regulations to corporations filing consolidated returns.

(b) *Overall foreign loss accounts.* Any taxpayer that sustains an overall foreign loss must establish an account for such loss. Separate types of overall foreign losses must be kept in separate accounts. The balance in any overall foreign loss account represents the amount of such overall foreign loss subject to recapture by the taxpayer in a given year. From year to year, amounts may be added to or subtracted from the balance in such account as provided in paragraphs (d) and (e) of this section. The taxpayer must report the balance in its overall foreign loss accounts annually on a Form 1116 or 1118 which is filed after these regulations are published as final regulations. The balance in each account does not have to be attributed to the year or years in which the loss was incurred.

(c) *Determination of a taxpayer's overall foreign loss*—(1) *Overall foreign loss defined.* A taxpayer sustains an overall foreign loss in any taxable year in which its gross income from sources without the United States subject to a separate limitation (as defined in paragraph (c)(2) of this section) is exceeded by the sum of the deductions properly allocated and apportioned thereto. Such losses are to be determined separately in accordance with the principles of the separate limitations. Accordingly, income and deductions subject to a separate limitation are not to be netted with income and deductions subject to another separate limitation for purposes of determining the amount of an overall foreign loss. A taxpayer may, for example, have an overall foreign loss under the section 904(d)(1)(E) limitation in the same taxable year in which it has taxable income under the section 904(d)(1)(B) limitation.

(2) *Separate limitation defined.* For purposes of paragraph (c)(1) of this section and these regulations, the term separate limitation means any of the separate limitations under section 904(d)(1)(A), (B), (C), (D), and (E); the separate limitation for foreign oil related income under section 907(b) (for taxable years ending after December 31, 1975 and beginning before January 1, 1983); or the separate limitation for the Puerto Rico and possession tax credit under section 936.

(3) *Method of allocation and apportionment of deductions.* In determining its overall foreign loss the taxpayer shall allocate and apportion expenses, losses, and other deductions to the appropriate category of gross income in accordance with section 862(b) and §1.861-8 of the regulations. However, the following deductions shall not be taken into account:

(i) The amount of any net operating loss deduction for such year under section 172(a); and

(ii) The amount of any—

(A) Expropriation losses for such year (as defined in section 172(h), or

(B) Loss for such year which arises from fire, storm, shipwreck, or other casualty, or from theft,

to the extent such loss is not compensated for by insurance or otherwise.

(d) *Additions to the overall foreign loss account*—(1) *General rule.* A taxpayer's overall foreign loss as determined under paragraph (c) of this section shall be added to the applicable overall foreign loss account at the end of its taxable year to the extent that the overall foreign loss has reduced U.S. source income during the taxable year or during a year to which the loss has been carried back. For rules with respect to carryovers see paragraph (d)(4) of this section and §1.904(f)-3.

(2) *Overall foreign net capital loss.* An overall foreign net capital loss shall be added to the overall foreign loss account at the end of the taxable year to the extent that the foreign source capital loss has reduced U.S. source capital gain net income during the current taxable year and during the years to which the loss has been carried back, subject to the adjustments in paragraph (d)(3) of this section. For rules with respect to carryovers, see paragraph (d)(5) of this section and §1.904(f)-3.

(3) *Adjustments.* The amount of overall foreign loss determined in paragraph (d)(1) of this section and the amount of overall foreign net capital loss determined in paragraph (d)(2) of this section shall be subject to the following adjustments:

(i) *Adjustment due to reduction in foreign source income under section 904(b).* A taxpayer's overall foreign loss account shall not include any net capital loss from sources without the United States to the extent that the application of section 904(b) would result in a reduction of foreign source taxable income (but not below zero) for purposes of the numerator of the foreign tax credit limitation fraction.

(ii) *Adjustment to account for rate differential between ordinary income rate and capital gain rate.* Subject to the provisions of paragraph (d)(3)(i) of this section, if an overall foreign loss for a taxable year includes an overall foreign net capital loss, such amount shall be reduced as follows, in accordance with the provisions of section 904(b), before being added to the overall foreign loss account:

(A) In the case of a corporate taxpayer, to the extent that the U.S. source capital gain net income reduced by the foreign source net capital loss consists of U.S. source net capital gain, by an amount equal to the rate differential portion (as defined in section 904(b)(3)(F) of the Code and the regulations thereunder) of the U.S. source net capital gain; or

(B) In the case of a taxpayer other than a corporate taxpayer, by 50 percent (for taxable years beginning prior to January 1, 1979) or 60 percent (for taxable years beginning after December 31, 1978) of the taxpayer's U.S. source net capital gain that is offset by such foreign source net capital loss.

(iii) *Illustrations.* The provisions of this paragraph (d)(3) may be illustrated by the following examples, which assume that all foreign source income and losses are under the section 904(d)(1)(E) separate limitation.

Example (1). V corporation has $1000 of foreign source taxable income and $500 of foreign source net capital loss which has reduced $500 of U.S. source capital gain net income (none of which is net capital gain). Under section 904(b), the numerator of V Corporation's foreign tax credit limitation fraction is reduced by $500 (see §1.904(b)-1(a)(3)). Under paragraph (d)(3)(i) of this section, none of that $500 goes into its overall foreign loss account.

Example (2). W Corporation has $1000 of foreign source taxable income and $2000 of foreign source net capital loss, which has reduced $2000 of U.S. source capital gain net income (all of which is U.S. source net capital gain). Under section 904(b), $1000 of W Corporation's foreign source net capital loss has reduced foreign source income in the numerator of the foreign tax credit limitation fraction (reducing the numerator to zero). As in example (1), that $1000 will not be included in W Corporation's overall foreign loss account. The additional amount of foreign source net capital loss which reduced U.S. source capital gain net income must be added to the overall foreign loss account. Since the U.S. source capital gain net income which was reduced by the foreign source net capital loss was net capital gain, a rate differential adjustment must be made under paragraph (d)(3)(ii) of this section before adding the overall foreign net capital loss to the account. The overall foreign loss is, therefore, $217.40 determined as follows. Under section 1.904(b)-1(a)(3) the $2000 foreign source net capital loss which has reduced $2000 of U.S. source net capital gain has resulted in a reduction in the numerator of the foreign tax credit limitation fraction of $1217.40

$$\frac{46.28}{(\$2000 - 46 \ (\$2000))}$$

$1000 of the $1217.40 will result in a reduction of foreign source taxable income (but not below zero) for purposes of the numerator of the foreign tax credit limitation fraction and is not included in the overall foreign loss account. Therefore $217.40 is included in the overall foreign loss account.

(4) *Overall foreign losses of another taxpayer.* If any portion of any overall foreign loss of another taxpayer is allocated to the taxpayer in accordance with §1.904(f)-5 (relating to overall foreign losses of domestic trusts) or §1.1502-9 (relating to consolidated overall foreign losses), the taxpayer shall add such amount to its applicable overall foreign loss account.

(5) *Loss carryovers.* Subject to the adjustments under paragraph (d)(3) of this section, the taxpayer shall add to the overall foreign loss account—

(i) All net operating loss carryovers to the current taxable year to the extent that overall foreign losses included in the net operating loss carryovers have reduced U.S. source income for the taxable year, and

(ii) All capital loss carryovers to the current taxable year to the extent that foreign source capital loss carryovers have reduced U.S. source capital gain net income for the taxable year.

(e) *Reductions of the overall foreign loss accounts.* The taxpayer shall subtract the following amounts from its overall foreign loss accounts at the end of its taxable year in the following order, if applicable:

(1) *Pre-recapture reduction for amounts allocated to other taxpayers.* The amount of any type of overall foreign loss which is allocated to another taxpayer in accordance with §1.904(f)-5 (relating to overall foreign losses of domestic trusts) or §1.1502-9 (relating to consolidated overall foreign losses).

(2) *Reduction for amounts recaptured.* The amount of any type of overall foreign loss which is recaptured in such year in accordance with §§1.904(f)-2(c) (relating to recapture under section 904(f)(1)), 1.904(f)-2(d) (relating to recapture when the taxpayer disposes of certain properties under section 904(f)(3)), and 1.904(f)-4 (relating to recapture when the taxpayer receives an accumulation distribution from a foreign trust under section 904(f)(4)).

(f) *Illustrations.* The rules of this section may be illustrated by the following examples.

Example (1). X Corporation is a domestic corporation with foreign branch operations in country C. X Corporation's taxable income and (losses) for its taxable year 1979 are as follows:

U.S. source taxable income	$1,000
Foreign source taxable income (loss) subject to section 904(d)(1)(E)	($500)
Foreign oil related income (loss) subject to section 907(b)	$200

X Corporation has a section 904(d)(1)(E) overall foreign loss of $500 for 1979 in accordance with paragraph *(c)*(1) of this section. Since the section 904(d)(1)(E) overall foreign loss is not considered to offset income under any other separate limitation described in paragraph (c)(1) of this section, it therefore offsets $500 of U.S. source taxable income. This amount is added to X Corporation's section 904(d) (1)(E) overall foreign loss account at the end of 1979 in accordance with paragraph (d)(1) of this section.

Example (2). X Corporation is a domestic corporation with foreign branch operations in country C. For its taxable year 1980, X Corporation has a net operating loss of $1250, determined as follows:

U.S. source tax income (loss)	($250)
Foreign source taxable income (loss) subject to section 904(d)(1)(E)	($1000)

The only prior year to which the net operating loss can be carried under section 172 is 1977. For its taxable year 1977, X Corporation had the following taxable income:

U.S. source taxable income	$1,900
Foreign source taxable income subject to section 904(d)(1)(E)	$400

X Corporation has a section 904(d)(1)(E) overall foreign loss for 1980 of $1,000. X Corporation's overall foreign loss is part of a net operating loss of $1,250 for 1980. Since, in accordance with §1.904(f)-3(a), the foreign loss carried back to 1977 is first allocated to X Corporation's foreign source taxable income subject to the limitation under which the loss arose, the amount of overall foreign loss to be added to X Corporation's overall foreign loss account in 1980 is $600 under paragraph (d)(1) of this section after the foreign loss carryback is first applied to foreign source income of $400 (which does not result in an overall foreign loss that is subject to recapture).

Example (3). The facts are the same as in example (2), except that in 1977 X Corporation's U.S. source taxable income was zero. Nothing is added to X Corporation's overall foreign loss account at the end of 1980. X Corporation's income and deductions for 1981 are as follows:

U.S. source taxable income	$1,250
Foreign source taxable income subject to section 904(d)(1)(E)	$300

X Corporation has a net operating loss carryover of $850 ($1250-$400) to 1981. The $600 of foreign losses that are part of this net operating loss ($1000 of 1980 loss, minus $400 offset by foreign source income in the carryback year) are allocated to X Corporation's foreign source taxable income subject to the section 904(d)(1)(E) limitation in such year, in accordance with §1.904(f)-3, prior to reducing U.S. source income. Thus, $300 of the remaining $600 of foreign source net operating loss carryover is first applied to foreign source income in the carryover year, leaving $300 which offsets U.S. source income in the carryover year. Therefore, $300 is added to X Corporation's section 904(d)(1)(E) overall foreign loss account in 1981 in accordance with paragraph (d)(5)(i) of this section. Since the entire net operating loss carryforward was absorbed in 1981, there are no further additions to X Corporation's overall foreign loss account under paragraph (d) as a result of this loss.

Example (4). Z Corporation is a domestic corporation with foreign branch operations. For the taxable year 1981, Z Coporation's taxable income and (losses) are as follows:

U.S. source taxable ordinary income	$1000
U.S. source net capital gain	$460
Foreign source taxable ordinary income subject to section 904 (d)(1)(E)	$200
Foreign source net capital loss subject to section 904(d)(1)(E)	($800)

Z Corporation had no capital gain net income in any prior taxable year. Under paragraph (d)(2) and (3) of this section, the amount to be added to Z Corporation's section 904(d)(1)(E) overall foreign loss account is the excess of the amount which has reduced U.S. source capital gain net income for the taxable year ($460), adjusted for the rate differential because it has reduced U.S. source net capital gain ($460 × 28/46 = $280), over the amount which has reduced the numerator of Z Corporation's foreign tax credit limitation fraction under section 904(b)(2), which is $200. (The $200 amount is foreign source net capital loss that has reduced U.S. source net capital gain in the donominator of the fraction, but not exceeding the amount of foreign source income in the numerator before the section 904(b)(2) adjustment.) Thus, Z Corporation must add $80 (the excess of the $280 over $200) to its section 904(d)(1)(E) overall foreign loss account in 1981. It should be noted that an overall foreign loss can occur in the absence of foreign branch operations.

§1.904(f)-2 Recapture of overall foreign losses.

(a) *In general.* A taxpayer electing the benefits of sections 901 or 936 with respect to foreign source taxable income subject to a separate limitation under which the taxpayer has sustained an overall foreign loss shall be required to recapture such loss as provided in this section. Recapture is accomplished by treating as U.S. source income a portion of the taxpayer's foreign source taxable income subject to the limitation under which the loss arose. As a result, the taxpayer's foreign tax credit limitation (or section 936 credit) with respect to such income is decreased. Recapture continues until such time as the amount of foreign source taxable income recharacterized as U.S. source income equals the U.S. source income which was previously offset by the overall foreign loss. As provided in §1.904(f)-1(e)(2), the balance in a taxpayer's overall foreign loss account is reduced by the amount of loss recaptured. Recapture is only applied to the extent that it will produce a reduction in the foreign tax credit limitation or the section 936 credit. This is accomplished by applying recapture to foreign source taxable income in the numerator of the foreign tax credit limitation fraction only after applying the section 904(a) limitation and section 904(b) adjustments, as provided in paragraph (b) of this section.

(b) *Determination of taxable income from sources without the United States for purposes of recapture.* For purposes of determining the amount of an overall foreign loss subject to recapture, the taxpayer's taxable income from sources without the United States, as determined in the numerator of the foreign tax credit limitation fraction, shall be computed with respect to each of the separate limitations described in §1.904(f)-1(c)(2) in accordance with §1.904(f)-1(c)(1) and (3). This computation is made without taking into account foreign source taxable income (and deductions properly allocated and apportioned thereto) subject to another separate limitation. Before applying the recapture rules to such foreign source taxable income, the following provisions shall be applied to such income in the following order:

(1) Section 904(b)(3)(C) and the regulations thereunder shall be applied to treat certain foreign source gain as U.S. source gain;

(2) Section 904(b)(2) and the regulations thereunder shall be applied to make adjustments in the foreign tax credit limitation fraction for certain capital gains and losses; and

(3) Section 904(a) shall be applied to determine foreign source taxable income in the numerator of the foreign tax credit limitation fraction.

An overall foreign loss under a separate limitation shall only be recaptured by recharacterizing foreign source taxable income subject to the same separate limitation as U.S. source income, except as provided in §1.904(f)-6. However, for purposes of recapturing an overall foreign loss incurred before a corporation elected to use section 936, the possession source income of a section 936 corporation shall be used to recapture the previously incurred overall foreign loss.

(c) *Section 904(f)(1) recapture*—(1) *In general.* The amount of any overall foreign loss subject to recapture in a taxable year in which paragraph (a) of this section is applicable is the lesser of the balance in the applicable overall foreign loss account (after reduction of such account in accordance with §1.904 (f)-1(e)(1); or fifty percent of the taxpayer's foreign source taxable income subject to the limitation under which the loss arose, as determined under paragraph (b) of this section.

(2) *Election to recapture more of the overall foreign loss than is required under paragraph (c)(1).* A taxpayer may make a revocable election to recapture a greater portion of the balance in an overall foreign loss account than is required to be recaptured under paragraph (c)(1) of this section. A taxpayer may make such an election or amend an election by attaching a statement to its Form 1116 or 1118 for the taxable year for which the election is made. This statement must indicate the percentage of the taxpayer's foreign source taxable income that is being recharacterized as U.S. source income and the percentage of the balance in the overall foreign loss account that is being recaptured. The taxpayer may not elect to recapture an amount in excess of the taxpayer's foreign source taxable income subject to the same separate limitation as the loss after applying paragraph (b) of this section to such income.

(3) *Illustrations.* The rules of this paragraph (c) may be illustrated by the following examples, all of which assume a U.S. corporate tax rate of 50 percent unless otherwise stated.

Example (1) X Corporation is a domestic corporation which does business in the United States and abroad. On December 31, 1980, the balance in X Corporation's section 904(d)(1)(E) overall foreign loss account is $600. For 1981, X Corporation has U.S. source taxable income of $500 and foreign source taxable income subject to section 904(d)(1)(E) of $500. For 1981, X Corporation pays $200 in foreign taxes and elects section 901. Under paragraph (c)(1) of this section, X Corporation is required to recapture $250 (the lesser of $600 or 50 percent of $500) of its overall foreign loss. As a consequence, X Corporation's foreign tax credit limitation under section 904(d) (1)(E) is $250/$1000 × $500, or $125, instead of $500/$1000 × $500, or $250. The balance in X Corporation's section 904(d)(1)(E) overall foreign loss account is reduced by $250 in accordance with §1.904(f)-1(e)(2).

Example (2). The facts are the same as in example (1) except that X Corporation makes an election to recapture its overall foreign loss to the extent of 80 percent of its foreign source taxable income subject to the section 904(d)(1)(E) limitation (or $400) in accordance with paragraph (c)(2) of this section. As a result of recapture, X Corporation's foreign tax credit limitation under section 904(d)(1)(E) for 1981 is $100/$1000 × $500, or $50, instead of $500/$1000 × $500, or $250. X Corporation's overall foreign loss account is reduced by $400 in accordance with §1.904(f)-1(e)(2).

Example (3). The facts are the same as in example (1) except that X Corporation does not elect the benefits of section 901 or 936 in 1981 and deducts its foreign taxes paid in 1981. The balance in X Corporation's section 904(d)(1)(E) overall foreign loss account on December 31, 1981 is $600. There is no recapture of the overall foreign loss since X Corporation did not elect the foreign tax credit.

Example (4). The facts are the same as in example (1) except that in 1981, X Corporation also has $1,000 of foreign source DISC dividend income subject to section 904(d)(1)(B) which carries a foreign tax of $50. Under paragraph (c)(1) of this section the amount of X Corporation's section 904(d)(1)(E) overall foreign loss subject to recapture is $250 (the lesser of the balance in the overall foreign loss account or 50 percent of the foreign source taxable income subject to the section 904(d)(1)(E) limitation (which excludes taxable income subject to the separate limitation of section 904(d)(1)(B))). X Corporation's separate limitation under section 904(d)(1)(B) for DISC dividend income is $1000/$2000 × $1000, or $500. Its limitation under section 904(d)(1)(E) for other foreign source taxable income is $250/$2000 × $1000, or $125, instead of $500/$2000 × $1000, or $250. The balance in X Corporation's section 904(d)(1)(E) overall foreign loss account is reduced by $250 in accordance with §1.904(f)-1(e)(2).

Example (5). The facts are the same as in example (1) except that on December 31, 1980 X Corporation also has a balance in its section 907 (b) overall foreign loss account of $900. For 1981, X Corporation also has foreign source taxable income subject to the section 907(b) limitation of $800. As in example (1), X Corporation is required to recapture $250 of its section 904(d)(1)(E) overall foreign loss, and its section 904(d)(1)(E) foreign tax credit limitation is $250/$1800 × $900, or $125, instead of

$500/$1800 × $900, or $250. X Corporation is also required to recapture $400 of its section 907(b) overall foreign loss (the lesser of $900 or 50 percent of $800). X Corporation's foreign tax credit limitation under section 907(b) is $400/$1800 × $900, or $200, instead of $800/$1800 × $900, or $400. The balance in X Corporation's section 907(b) overall foreign loss account is reduced to $500 in accordance with §1.904(f)-1(e)(2).

Example (6). This example assumes a U.S. corporate tax rate of 46% (under section 11(b)) and an alternative rate of tax under section 1201(a) of 28%. W is a U.S. corporation that does business in the United States and abroad. On December 31, 1980, W has $350 in its section 904(d)(1)(E) overall foreign loss account. For 1981, W has $500 of U.S. source taxable income, and has foreign source income subject to section 904(d)(1)(E) as follows:

Foreign source taxable income other than net capital gain	$720
Foreign source net capital gain	$460

Under paragraph (b)(2) of this section, foreign source taxable income for purposes of recapture includes foreign source capital gain net income, reduced, under section 904(b)(2), byu the rate differential portion of foreign source net capital gain, which adjusts for the reduced tax rate for net capital gain under section 1201(a):

Foreign source capital gain net income	$460
Rate differential portion of foreign source net capital gain (18/46 of $460)	-180
Foreign source capital gain included in foreign source taxable income	$280

The total foreign source taxable income of W for purposes of recaputre in 1981 is $1000 ($720 + $280). Under paragraph (c)91) of this section, W is required to recapture $350 (the lesser of $250 or 50 percent of $1000), and W's section 904(d)(1)(E) overall foreign loss account is reduced to zero W's section 904(d)(1)(E) foreign tax credit limitation is $650/$1500 × $690, or $299, instead of $1000/$1500 × $690, or $460.

(d) *Recapture of overall foreign losses from dispositions under section 904(f)(3)*—(9) *In general.* If the taxpayer disposes of property used or held for use predominantly without the United States in a trade or business during a taxable year in which paragraph (a) of this section is applicable, its overall foreign loss shall be recaptured as provided in paragraphs (d)(2), (d)(3), and (d)(4) of this section. See paragraph (d)(5) of this section for definitions. For the purposes of this paragraph (d), gain recognized on the disposition of property that was used or held for use to generate foreign source taxable income subject to a separate limitation will be treated as foreign source gain subject to the same separate limitation.

(2) *Treatment of net capital gain.* If the gain from a disposition of property to which this paragraph (d) applies is treated as net capital gain, all references to such gain in paragraphs (d)(3) and (d)(4) of this section shall mean such gain as adjusted under paragraph (b) of this section. The amount by which the overall foreign loss account shall be reduced shall be determined from such adjusted gain.

(3) *Dispositions where gain is recognized irrespective of section 904(f)(3).* If the taxpayer recognized foreign source gain subject to a separate limitation on the disposition of property described in paragraph (d)(1) of this section, and there is a balance in the taxpayer's overall foreign loss account under such separate limitation after applying paragraph (c) of this section, an additional portion of such balance shall be recaptured in accordance with paragraphs (a) and (b) of this section. The amount recaptured shall be the lesser of such balance or 100 percent of the foreign source gain recognized on the disposition that was not previously recharacterized under this section. The amount of gain not previously recharacterized shall be determined by subtracting 50 percent (or the percentage recaptured under paragraph (c)(2) of this section) of the gain recognized on such disposition from the entire amount of such gain.

(4) *Dispositions in which gain is not otherwise recognized*—(i) *Recognition of gain to the extent of overall foreign loss.* If the taxpayer makes a disposition of property described in paragraph (d)(1) of this section in which any amount of gain otherwise would not be recognized in the year of the disposition, and such property was used or held for use to generate foreign source taxable income subject to a separate limitation under which the taxpayer had an overall foreign loss (including an overall foreign loss incurred in the year of the disposition), the taxpayer shall recognize foreign source taxable income in an amount equal to the lesser of:

(A) The sum of the balance in the applicable overall foreign loss account (but only after such balance has been increased by amounts added to the account for the year of the disposition or has been reduced by amounts recaptured for the year of the disposition under paragraph (c) and paragraph (d)(3) of this section) plus the amount of any overall foreign loss that would be part of a net operating loss for the year of the disposition if gain from the disposition were not recognized under section 904(f)(3), plus the amount of any overall foreign loss that would be part of a net operating loss for the year of the disposition if gain from the disposition were not recognized under section 904(f)(3), plus the amount of any overall foreign loss that is part of a net operating loss carryover from a prior year, or

(B) The excess of the fair market value of such property over the taxpayer's adjusted basis in such property.

The excess of the fair market value of such property over its adjusted basis shall be determined on an asset by asset basis. Losses from the disposition of an asset shall not be recognized. Any foreign source taxable income deemed received and recognized under this paragraph (d)(4)(i) will have the same character as if the property had been sold or exchanged in a taxable transaction.

(ii) *Basis adjustment.* The basis of the property received in an exchange to which this paragraph (d)(4) applies shall be increased by the amount of gain deemed recognized, in accordance with applicable sections of subchapters C (relating to corporate distributions and adjustments), K (relating to partners and partnerships), O (relating to gain or loss on disposition of property), and P (relating to capital gains and losses). If the property to which this paragraph (d)(4) applies was transferred by gift, the basis of such property in the hand of the donor immediately preceding such gift shall be increased by the amount of the gain deemed recognized.

(iii) *Recapture of overall foreign loss to the extent of amount deemed recognized.* The provisions of paragraphs (a) and (b) of this section shall be applied to the extent of 100% of the foreign source taxable income which is recognized under paragraph (d)(4)(i) of this section. However, amounts of foreign source gain that would not be recognized except by application of section 904(f)(3) and paragraph (d)(4)(i) of this section, and which are treated as U.S. source gain by application of section 904(b)(3)(C) and paragraph (b)(1) of this section, shall reduce the overall foreign loss account, subject to the adjustments described in paragraph (b)(2) of this section if such gain is net capital gain, notwithstanding the fact that such amounts were precluded from recapture by paragraph (a) of this section due to the ordering rules in paragraph (b) of this section.

(iv) *Priorities among dispositions in which gain is deemed to be recognized.* If the taxpayer makes more than one disposition to which this paragraph (d)(4) is applicable, the rules of this paragraph (d)(4) shall be applied to each disposition in succession starting with the disposition which occurred earliest, until the balance in the applicable overall foreign loss account is reduced to zero.

(5) *Definitions*—(i) *Disposition.* A disposition to which this paragraph (d) applies includes a sale (including a sale in a lease back transaction); exchange; distribution; gift; transfer upon the foreclosure of a security interest (but not a mere transfer of title to a creditor upon the creation of a security interest or to a debtor upon termination of a security interest); involuntary conversion; contribution to a partnership, trust, or corporation; transfer at death; or any other transfer of property whether or not gain or loss is recognized. However, a disposition to which this paragraph (d) applies does not include:

(A) A distribution or transfer of property to a domestic corporation described in section 381 (a) (provided that paragraph (d)(6) of this section applies), or

(B) A disposition of property which is not a material factor in the realization of income by the taxpayer (as defined in paragraph (d)(5)(iv) of this section).

(ii) *Property used in a trade or business.* Property is used in a trade or business if it is held for the principal purpose of promoting the present or future conduct of the trade or business. This generally includes property acquired and held in ordinary course of a trade or business or otherwise held in a direct relationship to a trade or business. In determining whether an asset is held in a direct relationship to a trade or business, principal consideration shall be given to whether the asset is used in the trade or business. Property will be treated as held in a direct relationship to a trade or business if the property was acquired with funds generated by that trade or business or if income generated from the asset is retained or reinvested in that trade or business. Property used in a trade or business may be tangible or intangible, real or personal property. It includes property, such as equipment, which is subject to an allowance for depreciation under section 167 or cost recovery under section 168. Property may be considered used in a trade or business even if it is a capital asset in the hands of the taxpayer. Stock of another corporation held only for investment purposes shall not be considered property used in a trade or business. However, stock acquired or held to assure a source of supply for the trade or business shall be considered property used in a trade or business. Stock in trade is generally not considered property used in a trade or business. However, when disposed of in a manner not in the ordinary course of a trade or business, stock in trade will be considered as property used in the trade or business.

(iii) *Property used predominantly outside the United States.* Property will be considered used predominantly outside the United States if for a 3-year period ending on the date of the disposition (or, if shorter, the period during which the property has been used in the trade or business) such property was located outside the United States more than 50 percent of the time. An aircraft, railroad rolling stock, vessel, motor vehicle, container, or other property used for transportation purposes is deemed to be used predominantly outside the United States if, during the 3-year (or shorter) period, either such property is located outside the United States more than 50 percent of the time or more than 50 percent of the miles traversed in the use of such property are traversed outside the United States.

(iv) *Property which is a material factor in the realization of income.* For the purposes of this section, property used in a trade or business will be considered a material factor in the realization of income unless the taxpayer establishes that it is not (or, if the taxpayer did not realize income from the trade or business in the taxable year, would not be expected to be) necessary to the realization of income by the taxpayer.

(6) *Carryover of overall foreign loss account in a corporate acquisition to which section 381(a) applies.* In the case of a distribution or transfer described in section 381(a), an overall foreign loss of the distributing or transferor corporation shall be treated as the overall foreign loss of the acquiring or transferee corporation as of the close of the date of the distribution or transfer. If the transferee corporation has an overall foreign loss account under the same separate limitation prior to the distribution or transfer, the balance in the transferor's account may be added to the transferee's account. If not, the transferee must establish a new overall foreign loss account. An overall foreign loss of the transferor will be treated as incurred by the transferee in a year prior to the year of the transfer.

(7) *Illustrations.* The rules of this paragraph (d) may be illustrated by the following examples which assume that the U.S. corporate tax rate is 50 percent (unless otherwise stated). For purposes of these examples, none of the foreign source gains are treated as net capital gains (unless so stated).

Example (1). X Corporation has a balance in its section 904(d)(1)(E) overall foreign loss account of $600 at the close of its taxable year ending December 31, 1980. In 1981, X Corporation sells assets used predominantly outside the United States in a trade or business and recognizes $1,000 of gain on the sale under section 1001. This gain is subject to the section 904(d)(1)(E) limitation. This sale is a disposition within the meaning of paragraph (d)(4)(i) of this section, and to which this paragraph (d) applies. X Corporation has no other foreign source taxable income in 1981 and has $1,000 of U.S. source taxable income. X Corporation is required to recapture $500 (the lesser of the balance in X's section 904(d)(1)(E) overall foreign loss account ($600) or 50 percent of $1000) of its overall foreign loss under paragraph (c) of this section. The balance of X Corporation's section 904(d)(1)(E) overall foreign loss account is reduced to $100 in accordance with §1.904(f)-1(e)(2). In addition, under paragraph (d)(3) of this section, X Corporation is required to recapture $100 (the lesser of the remaining balance in its section 904(d)(1)(E) overall foreign loss account ($100) or 100 percent of its foreign source taxable income recognized on such disposition that has not been previously recharacterized ($500)). The total amount recaptured is $600. X Corporation's section 904(d)(1)(E) foreign tax credit limitation for 1981 is $200 ($400/$2,000 × $1,000) instead of $500 ($1,000/$2,000 × $1,000). The balance of X Corporation's section 904(d)(1)(E) overall foreign loss account is reduced to zero in accordance with §1.904(f)-1(e)(2).

Example (2). On December 31, 1980, Y Corporation has a balance in its section 904(d)(1)(E) overall foreign loss account of $1,500. In 1981, Y corporation has $500 of U.S. source taxable income and $200 of foreign source taxable income subject to the section 904(d)(1)(E) limitation. Y Corporation's foreign source taxable income is from the sale of property used predominantly outside of the United States in a trade or business. This sale is a disposition to which this paragraph (d) is applicable. In 1981, Y Corporation also transferred property used predominantly outside of the United States in a trade or business to another corporation. Under section 351, no gain was recognized on this transfer. Such property had been used to generate foreign source taxable income subject to the section 904(d)(1)(E) limitation. The excess of the fair market value of the property transferred over the corporation's adjusted basis in such property was $2,000. In accordance with paragraph (c) of this section, Y Corporation is required to recapture $100 (the lesser of $1500, the amount in Y Corporation's overall foreign loss account, or 50 percent of $200, the amount of foreign source taxable income for the current year) of its section 904(d)(1)(E) overall foreign loss. Y Corporation is then required to recapture an additional $100 of its overall foreign loss under paragraph (d)(3) of this section out of gain recognized on the sale of assets which has not been previously recharacterized, since 100 percent of such gain is subject to recapture. The balance in Y Corporation's section 904(d)(1)(E) overall foreign loss account is reduced to $1,300 in accordance with §1.904(f)-1(e)(2). Y Corporation is then required to recognize $1,300 of foreign source taxable income on its section 351 transfer under paragraph (d)(4) of this section. Under paragraph (d)(4), 100 percent of the amount so recognized is treated as U.S. source taxable income, and Y Corporation's section 904(d)(1)(E) overall foreign loss account is reduced to zero. X Corporation's entire taxable income for 1981 is:

U.S. source taxable income	$ 500
Foreign source taxable income subject to section 904(d)(1)(E) that is recharacterized as U.S. source income by paragraphs (c) and (d)(e) of this section	$ 200
Gain recognized under section 904(f)(3) and paragraph (d)(4) of this section, and recharacterized as U.S. source income	$1,300
Total	$2,000

Y Corporation's section 904(d)(1)(E) foreign tax credit limitation for 1981 is O ($0/$2,000 × $1,000) instead of $100 ($200/$700 × $350).

Example (3). Z Corporation has a balance in its section 907(d) overall foreign loss (foreign oil related loss) account of $1,500 at the end of its taxable year 1980. In 1981, Z Corporation has $1,600 of foreign oil related income subject to the section 907(b) limitation and no U.S. source income. In addition, in 1981, Z Corporation makes two dispositions of property used predominantly outside the United States in a trade or business on which no gain was recognized. Such property generated foreign oil related income. The excess of the fair market value of the property transferred in the first disposition over the taxpayer's adjusted basis in such property is $575. The excess of the fair market value of the property transferred in the second disposition over the taxpayer's adjusted basis in such property is $1,000. Under paragraph (c) of this section, Z Corporation is required to recapture $800 (the lesser of 50 percent of its foreign oil related income of $1600 or the balance ($1500) in its section 907(b) overall foreign loss account) of its foreign oil related loss. In accordance with paragraph (d)(4)(i) and (iv) of this section, Z Corporation is required to recognize foreign oil related income in the amount of $575 on the first disposition and, since the foreign oil related loss account is now reduced by $1375 ($800 and $575 amounts previously recaptured), Z Corporation is required to recognize foreign oil related income in the amount of $125 on the second disposition. In accordance with paragraph (d)(4)(iii) of this section, the entire amount recognized is treated as U.S. source income. The balance in its section 907(b) overall foreign loss account is reduced to zero under §1.904(f)-1(e)(2). Z Corporation's foreign tax credit limitation under section 907(b) is $400 ($800/$2,300 × $1,150) instead of $800 ($1,600/$1,600 × $800). Z Corporation has $700 of U.S. source taxable income with respect to which no foreign tax credit is allowed.

Example (4). The facts are the same as in example (3), except that the gain from the two dispositions of property is treated as net capital gain and the U.S. corporation tax rate is assumed to be 46 percent. As in example (3), Z Corporation is required to recapture $800 of its foreign oil related loss from its ordinary foreign oil related income. In accordance with paragraph (d)(4)(i) and (iv) of this section, Z Corportion is first required to recognize foreign oil related income (which is net capital gain) on the first disposition in the amount of $575. Under paragraphs (b) and (d)(2) of this section, this net capital gain is adjusted by subtracting the rate differential portion of such gain from the total amount of such gain to determine the amount by which the foreign oil related loss account is reduced, which is $350 ($575 − ($575 × 18/46)). The balance remaining in Z Corporation's foreign oil related loss account after this step is $350. Therefore, this process will be repeated, in accordance with paragraph (d)(4)(iv) of this section, to recapture that remaining balance out of gain deemed recognized on the second disposition, resulting in reduction of the foreign oil related loss account to zero and net capital gain required to be recognized from the second disposition in the amount of $575, which must also be adjusted by subtracting the rate differential portion to determine the amount by which the foreign oil related loss account is reduced (which is $350). The $575 of net capital gain is also recharacterized as U.S. source net capital gain. Z Corporation's section 907(b) foreign tax credit limitation is the same as in example (3), and Z Corporation has an additional $1,150 ($575 + $575) of U.S. source net capital gain for which no credit is available.

§1.904(f)-3 Allocation of net operating losses and net capital losses.

(a) *Allocation of net operating loss carrybacks and carryovers attributable to overall foreign losses.* If the taxpayer sustains an overall foreign loss that is part of a net operating loss for the year, then, in carrying such net operating loss back or over in accordance with section 172, (or §§1.1502-21(b) and 1.1502-79(a)), the portion of the net operating loss attributable to an overall foreign loss shall be allocated to foreign source taxable income subject to the same separate limitation the carryback or carryover year. To the extent that such overall foreign loss exceeds foreign source taxable income subject to the same separate limitation in the year to which it is carried, it shall be allocated to the taxpayer's U.S. source income for such year and not to foreign source taxable income subject to another separate limitation. See §1.904(f)-1(d) for additions to the applicable overall foreign loss account to the extent that U.S. source taxable income is reduced in the taxable year to which the loss is carried.

(b) *Allocation of net capital loss carrybacks and carryovers attributable to overall foreign losses.* If the taxpayer sustains an overall foreign loss that is part of a net capital loss for the year, then in carrying the net capital loss back or over in accordance with section 1212 (or §1.1502-22 and 1.1502-79(b)), the portion of the net capital loss that is attributable to a foreign source capital loss shall be allocated to foreign source capital gain net income subject to the same separate limitation in the carryback or carryover year. To the extent that such foreign source capital loss exceeds foreign source capital gain net income subject to the same separate limitation in the year to which carried, it shall be allocated to U.S. source capital gain net income in such year and not to foreign source capital gain net income subject to another separate limitation. An overall foreign source net capital loss carried over to a later year in accordance with this paragraph (b) shall be taken into consideration in determining the taxpayer's overall foreign loss in the year to which carried and shall be added to the applicable loss account for such year in accordance with §1.904(f)-1(d).

§1.904(f)-4 Recapture of foreign losses out of accumulation distributions from a foreign trust.

(a) ***In general.*** If the taxpayer receives a distribution of foreign source taxable income that is treated under section 666 as having been distributed by a foreign trust in a preceding taxable year, a portion of the balance in the taxpayer's overall foreign loss account shall be subject to recapture under this section. The amount subject to recapture shall be an amount equal to the lesser of the balance in the taxpayer's overall foreign loss account (after applying §§1.904(f)-1, -2, -3, and -6 to the taxpayer's other income or loss in the current taxable year) or the entire amount of foreign source taxable income deemed distributed in a preceding year or years under section 666.

(b) *Effect of recapture on foreign tax credit limitation under section 667(d).* If paragraph (a) of this section is applicable, then in applying the separate limitation (in accordance with section 667(d)(1)(A) and (C)) to determine the amount of foreign taxes deemed distributed under section 666(b) and (c) that can be credited against the increase in tax in a computation year, a portion of the foreign source taxable income deemed distributed in such computation year shall be treated as U.S. source income. Such portion shall be determined by multiplying the amount of foreign source taxable income deemed distributed in the computation year by the fraction. The numerator of this fraction is the balance in the taxpayer's overall foreign loss account (after application of §§1.904(f)-1, -2, -3, and -6), and the denominator of the fraction is the entire amount of foreign source taxable income deemed distributed under section 666. However, the numerator of this fraction shall not exceed the denominator of the fraction.

(c) *No recapture if taxpayer chooses to deduct foreign taxes deemed distributed.* The provisions of this section shall not apply to the income deemed distributed in any computation year of a taxpayer making an election under section 667(d)(1)(B) to deduct foreign taxes deemed distributed under section 666(b) or (c) for such computation year.

(d) *Illustration.* The provisions of this section may be illustrated by the following example:

Example. X Corporation is a domestic corporation that has a balance of $10,000 in its overall foreign loss account on December 31, 1980. For its taxable year beginning January 1, 1981, X Corporation's only income is an accumulation distribution from a foreign trust of $20,000 of foreign source taxable income. Under section 666, the amount distributed and the foreign taxes paid on such amount ($4,000) are deemed distributed in 2 prior taxable years. In determining the partial tax on such distribution under section 667(b), the amount added to each computation year is $12,000 (the sum of the actual distribution plus the taxes deemed distributed ($24,000) divided by the number of accumulation years (2)). Of that amount, $5,000 ($10,000/$24,000 × $12,000) is treated as U.S. source taxable income in accordance with paragraph (b) of this section. X Corportion's separate foreign tax credit limitation against the increase in tax in each computation year is $7,000/$12,000 × $6,000 instead of $12,000/$12,000 × $6,000. X Corporation's overall foreign loss account is reduced to zero in accordance with paragraph (a) of this section.

§1.904(f)-5 Special rules for recapture of overall foreign losses of a domestic trust.

(a) *In general.* Except as provided in this section, the rules contained in §§1.904(f)-1, -2, -3, -4, and -6 apply to domestic trusts.

(b) *Recapture of trust's overall foreign loss.* In taxable years in which a trust has foreign source taxable income subject to a separate limitation under which the trust has an overall foreign loss, the balance in the trust's overall foreign loss account shall be recaptured as follows:

(1) *Trust accumulates income.* If the trust accumulates all of its foreign source taxable income subject to the limitation under which the loss arose, its overall foreign loss shall be recaptured out of such income in accordance with §§1.904(f)-1 -2, -3, -4, and -6.

(2) *Trust distributes income.* If the trust distributes all of its foreign source taxable income subject to the limitation under which the loss arose, the amount of the overall foreign loss that would be subject to recapture by the trust under paragraph (b)(1) of this section shall be allocated to the beneficiaries in proportion to the amount of such income which is distributed to each beneficiary over the total amount of such income.

(3) *Trust accumulates and distributes income.* If the trust accumulates part of its foreign source taxable income subject to the limitation under which the loss arose and distributes part of such income, the portion of the overall foreign loss that would be subject to recapture by the trust under paragraph (b)(1) of this section if the distributed income were accumulated shall be allocated to the beneficiaries receiving income distributions. The amount of overall foreign loss to be allocated to such beneficiaries shall be the same portion of the total amount of such overall foreign loss that would be subject to recapture as the amount of such income which is distributed to each beneficiary bears to the total amount of such income of the trust for such year. That portion of the overall foreign loss subject to recapture in such year that is not allocated to the beneficiaries in accordance with this paragraph (b)(3) shall be recaptured by the trust in accordance with §§1.904(f)-1, -2, -3, -4, and -6.

(c) *Amounts allocated to beneficiaries.* Amounts of a trust's overall foreign loss allocated to any beneficiary in accordance with paragraph (b)(2) or (3) of this section shall be added to the beneficiary's applicable overall foreign loss account and treated as an overall foreign loss of the beneficiary incurred in the taxable year preceding the year of such allocation. Such amounts shall be subject to recapture in accordance with §§1.904(f)-1, -2, -3, -4, and -6 out of foreign source taxable income subject to the same separate limitation which is distributed to the beneficiaries.

(d) *Section 904(f)(3) dispositions to which §1.904(f)-2(d)(4)(i) is applicable.* Foreign source taxable income recognized by a trust under §1.904(f)-2(d)(4) on a disposition of property used in a trade or business outside the United States shall be deemed to be accumulated by the trust. One hundred percent of such income shall be used to recapture the trust's overall foreign loss in accordance with §1.904(f)-2(d)(4).

(e) *Illustrations.* The provisions of this section are illustrated by the following examples:

Example (1). T, a domestic trust, has a balance of $2000 in its overall foreign loss account on December 31, 1979. For its taxable year ending on December 31, 1980, T has foreign source taxable income (subject to the same separate limitation as that under which the overall foreign loss was incurred) of $1600, all of which it accumulates. Under paragraph (b)(1) of this section, T is required to recapture $800 in 1980 (the lesser of the overall foreign loss or 50 percent of the foreign source taxable income). At the end of its 1980 taxable year, T has a balance of $1200 in its overall foreign loss account.

Example (2). The facts are the same as in example (1). In 1981, T has foreign source taxable income (subject to the same separate limitation) of $1000, which it distributes to its beneficiaries as follows: $500 to A, $250 to B, and $250 to C. Under paragraph (b)(1) of this section, T would have been required to recapture $500 of its overall foreign loss if it had accumulated all of such income. Therefore, under paragraph (b)(2) of this section, T must allocate $500 of its overall foreign loss to A, B, and C as follows: $250 to A ($500 × $500/$1000), $125 to B ($500 × $250/$1000), and $125 to C ($500 × $250/$1000). Under paragraph (c) of this section and §1.904(f)-1(d)(4), A, B, and C must add the amounts of overall foreign loss allocated to them from T to their overall foreign loss accounts and treat such amounts as overall foreign loss incurred in 1980. A, B, and C must then apply the rules of §1.904(f)-1, -2, -3, -4, and -6 to recapture their overall foreign losses. T's overall foreign loss account is reduced, in accordance with §1.904(f)-1(e)(1), by the $500 that is allocated to A, B, and C. At the end of 1981, T's overall foreign loss account has a balance of $700.

Example (3). the facts are the same as in example (2), except that in 1981 T's foreign source taxable income under the applicable separate limitation is $1500 instead of $1000, and T accumulates the additional $500. Under paragraph (b)(1) of this section, T would be required to recapture $750 of its overall foreign loss if it accumulated all of the $1500. Under paragraph (b)(3) of this section, T must allocate $500 of its overall foreign loss to A, B, and C as follows: $250 to A ($750 × $500/$1500) and $125 each to B and C ($750 × $250/$1500). T must also recapture $250 of its overall foreign loss, which is the portion of the amount subject to recapture in 1981 that is not allocated to the beneficiaries ($750 – $500 = $250). Under §1.904(f)-1(e)(1), T subtracts $500 from its overall foreign loss account, and under §1.904(f)-1(e)(2), T subtracts $250 from its overall foreign loss account, leaving a balance at the end of 1981 of $450.

§1.904(f)-6 Transitional rule for recapture of old section 907(b) and section 904(d)(1)(E) overall foreign losses incurred in taxable years beginning before January 1, 1983 from foreign source taxable income subject to the section 904(d)(1)(E) limitaiton in taxable years beginning after December 31, 1982.

(a) *General rule*. For taxable years beginning after December 31, 1982, foreign source taxable income subject to the section 904(d)(1)(E) limitation includes foreign oil related income (as defined in section 907(c)(2) prior to its amendment by section 211 of the Tax Equity and Fiscal Responsibility Act of 1982) [Pub. L. 97-248, 1982-2 C.B. 462, 484]. However, for purposes of recapturing section 904(d)(1)(E) overall foreign losses incurred in taxable years beginning before January 1, 1983 (pre-1983) out of foreign source taxable income subject to the section 904(d)(1)(E) limitation in taxable years beginning after December 31, 1982 (post-1982), the taxpayer shall make separate determinations of foreign oil related income and other section 904(d)(1)(E) income (as if the "old section 907(d)" separate limitation, under section 907(b) prior to its amendment by section 211 of the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462, 484], were still in effect), and shall apply the rules set forth in this section. The taxpayer shall maintain separate accounts for its pre-1983 old section 907(b), pre-1983 section 904(d)(1)(E), and post-1982 section 904(d)(1)(E) overall foreign losses. The taxpayer shall continue to maintain such separate accounts, make such separate determinations, and apply the rules of this section until the earlier of—

(1) Such time as the taxpayer's entire pre-1983 old section 907(b) and pre-1983 section 904(d)(1)(E) overall foreign losses have been recaptured, or

(2) The end of the taxpayer's eighth post-1982 taxable year, at which time the taxpayer shall add any remaining balance in its pre-1983 old section 907(b) and pre-1983 section 904(d)(1)(E) overall foreign loss accounts to its post-1982 section 904(d)(1)(E) overall foreign loss account,

after which time the taxpayer shall recapture all overall foreign losses as provided in §§1.904(f)-1 through -5.

(b) *Recapture of pre-1983 old section 907(b) and section 904(d)(1)(E) overall foreign losses from post-1982 income*. A taxpayer having a balance in a pre-1983 old section 907(b) or section 904(d)(1)(E) overall foreign loss account in a post-1982 taxable year shall recapture a portion of such overall foreign loss as follows:

(1) *Recapture from income subject to the same limitation*. The taxpayer shall first apply the rules of §§1.904(f)-1 through -5 to the taxpayer's separately determined foreign oil related income to recapture pre-1983 old section 907(b) overall foreign losses, and shall apply such rules to the taxpayer's separately determined section 904(d)(1)(E) income (exclusive of foreign oil related income) to recapture pre-1983 section 904(d)(1)(E) overall foreign losses.

(2) *Recapture from income subject to the other limitation*. The taxpayer shall next apply the rules of §§1.904(f)-1 through -5 to the taxpayer's separately determined foreign oil related income to recapture pre-1983 section 904(d)(1)(E) overall foreign losses, and shall apply such rules to the taxpayer's separately determined section 904 (d)(1)(E) income to recapture pre-1983 old section 907(b) overall foreign losses, but only to the extent that—

(i) The amount recaptured from such separately determined income under paragraph (b)(1) of this section is less than 50 percent (or such larger percentage as the taxpayer elects) of such separately determined income, and

(ii) The amount recaptured from such separately determined income under this paragraph (b)(2) does not exceed an amount equal to 12½ percent of the balance in the taxpayer's pre-1983 old section 907(b) or section 904(d)(1)(E) (as applicable) overall foreign loss account at the beginning of the taxpayer's first post-1982 taxable year, multiplied by the number of post-1982 taxable years (including the year to which this rule is being applied) which have elapsed, less the amount (if any) recaptured in prior post-1982 taxable years under this paragraph (b)(2) from such separately determined income.

The taxpayer may elect to recapture a pre-1983 overall foreign loss from post-1982 income subject to the section 904(d)(1)(E) limitation at a faster rate than is required by this paragraph (b)(2). This election shall be made in the same manner as an election to recapture more than 50 percent of income subject to recapture under section 904(f)(1), as provided in §1.904(f)-2(c)(2).

(c) *Coordination of recapture of pre-1983 and post-1982 overall foreign losses*. A taxpayer incurring a section 904(d)(1)(E) overall foreign loss in any post-1982 taxable year in which the taxpayer has a balance in a pre-1983 old section 907(b) or section 904(d)(1)(E) overall foreign loss account shall establish a separate overall foreign loss account for such loss. The taxpayer shall recapture its overall foreign losses in succeeding taxable years by first applying the rules of this section to recapture its pre-1983 overall foreign losses, and then applying the rules of §§1.904(f)-1 through -5 to recapture its post-1982 section 904(d)(1)(E) overall foreign loss. A post-1982 section 904(d)(1)(E) overall foreign loss may only be recaptured to the extent that the amount of foreign source taxable income recharacterized under paragraph (b) of this section is less than 50 percent (or such greater percentage as the taxpayer elects) of the taxpayer's total section 904(d)(1)(E) foreign source taxable income (including foreign oil related income) for such taxable year (except as required by section 904(f)(3)).

(d) *Illustrations*. The provisions of this section may be illustrated by the following examples:

Example (1). X Corporation is a U.S. corporation which has the calendar year as its taxable year. On December 31, 1982, X Corporation has a balance of $1,000 in its section 904(d)(1)(E) overall foreign loss account and does not have a balance in an old section 907(b) overall foreign loss account. For 1983, X Corporation has section 904(d)(1)(E) income of $1,200, which includes foreign oil related income of $1,000 and other section 904(d)(1)(E) income of $200. In 1983 X Corporation is required to recapture $225 of its pre-1983 section 904(d)(1)(E) overall foreign loss, computed as follows:

Amount recaptured under paragraph(b)(1) of this section $100

The amount recaptured from section 904(d)(1)(E) income exclusive of foreign oil related income is the lesser of $1,000 (the pre-1983 section 904(d)(1)(E) overall foreign loss) or 50 percent of $200 (the separately determined section 904(d)(1)(E) income exclusive of foreign oil related income).

Amount recaptured under paragraph (b)(2) of this section $125

The amount recaptured from foreign oil related income is the lesser of $900 (The remaining pre-1983 section 904(d)(1)(E) overall foreign loss after recapture under paragraph (b)(1) of this section) or 50 percent of $1,000 (the separately determined foreign oil related income), but is limited by paragraph (b)(2)(ii) of this section (12½ percent of $1,000 × 1) − $0, which is $125.

Total amount recaptured in 1983 ...... $225

Example (2). The facts are the same as in example (1), except that X Corporation has section 904(d)(1)(E) income of $50 for 1984 and $600 for 1985, all of which is foreign oil related income. X Corporation is required to recapture $25 in 1984 and $225 in 1985 of its pre-1983 section 904(d)(1)(E) overall foreign loss, computed as follows:

Amount recaptured under paragraph (b)(2) of this section in 1984 .... $ 25

The amount recaptured from foreign oil related income is the lesser of $775 (the remaining pre-1983 section 904(d)(1)(E) overall foreign loss) or 50 percent of $50 (the separately determined foreign oil related income). This amount is within the limitation of paragraph (b)(2)(ii) of this section, (12½ percent of $1,000 × 2) − $125, which is $125.

Amount recaptured under paragraph (b)(2) of this section in 1985 .... $225

The amount recaptured from foreign oil related income is the lesser of $750 (the remaining pre-1983 section 904(d)(1)(E) overall foreign loss) or 50 percent of $600 (the separately determined foreign oil related income), but is limited by paragraph (b)(2)(ii) of this section to (12½ percent of $1,000 × 3) − ($125 + $25), which is $225. ($125 is the amount recaptured in 1983 under paragraph (b)(2) of this section, and $25 is the amount recaptured in 1984 under paragraph (b)(2) of this section.)

Example (3). Y Corporation is a U.S. corporation which has the calendar year as its taxable year. On December 31, 1982, Y Corporation has a balance of $400 in its section 904(d)(1)(E) overall foreign loss account and does not have a balance in a section 907(b) overall foreign loss account. For 1983, Y Corporation has a section 904(d)(1)(E) overall foreign loss of $200. For 1984, Y Corporation has section 904(d)(1)(E) income of $1,200, all of which is foreign oil related income. In 1984 Y Corporation is required to recapture a total of $300 computed as follows:

Amount of pre-1983 overall foreign loss recaptured under paragraph (b)(2) of this section $100

The amount of pre-1983 section 904(d)(1)(E) overall foreign loss recaptured from foreign oil related income is the lesser of $400 (the loss) or 50 percent of $1,200 (the separately determined foreign oil related income), but is limited by paragraph (b)(2)(ii) of this section to (12½ percent of $400 × 2) − $0, which is $100.

Amount of post-1982 overall foreign loss recaptured under paragraph (c) of this section .... $ 200

The amount of post-1982 section 904(d)(1)(E) overall foreign loss recaptured is the amount computed under §1.904(f)-2(c)(1), which is the lesser of $200 (the post-1982 loss) or 50 percent of $1,200 (the income), but only to the extent that the amount of pre-1983 loss recaptured under paragraph (b) of this section is less than 50 percent of such income ((50 percent of $1,200) − $100 recaptured under paragraph (b) = $500).

Total amount recaptured in 1984 ...... $ 300

At the end of 1984, Y Corporation has a balance in its pre-1983 section 904(d)(1)(E) overall foreign loss account of $300, and has reduced its post-1982 section 904(d)(1)(E) overall foreign loss account to zero.

Example (4). Z Corporation is a U.S. corporation which has the calendar year as its taxable year. On December 31, 1982, Z Corporation has a balance of $400 in its section 904(d)(1)(E) overall foreign loss account and a balance of $1,000 in its old section 907(b) overall foreign loss account. For 1983, Z Corporation has section 904(d)(1)(E) income of $2,000, which includes foreign oil related income of $1,000 and other section 904(d)(1)(E) income of $1,000. Keeping these amounts separate for purposes of this section, Z Corporation is required to recapture a total of $1,000 in 1983, computed as follows:

Amount recaptured under paragraph (b)(1) of this section .... $ 900

The amount of pre-1983 old section 907(b) overall foreign loss recaptured from foreign oil related income, in accordance with §1.904(f)-2(c)(1), is the lesser of $1,000 (the old section 907(b) overall foreign loss) or 50 percent of $1,000 (the foreign oil related income), which is $500.

The amount of pre-1983 section 904(d)(1)(E) overall foreign loss recaptured from section 904(d)(1)(E) income exclusive of foreign oil related income, in accordance with §1.904(f)-2(c)(1), is the lesser of $400 (the section 904(d)(1)(E) overall foreign loss) or 50 percent of $1,000 (the section 904(d)(1)(E) income exclusive of foreign oil related income), which is $400.

Amount recaptured under paragraph (b)(2) of this section .... $ 100

The amount of pre-1983 old section 907(b) overall foreign loss recaptured from section 904(d)(1)(E) income exclusive of foreign oil related income is the lesser of $500 (the remaining balance in that loss account) or 50 percent of $1,000 (the section 904(d)(1)(E) income exclusive of foreign oil related income), but only to the extent that the amount recaptured from such income under paragraph (b)(1) of this section is less than 50 percent of such income, or $100 (50 percent of $1,000) − $400 recaptured due to section 904(d)(1)(E) overall foreign loss), and only up to the amount permitted by paragraph (b)(2)(ii) of this section, which is (12½ percent of $1,000 × 1) − $0 − $0, or $125.

Total amount recaptured in 1983 $1000

At the end of 1983, Z Corporation has reduced its pre-1983 section 904(d)(1)(E) overall foreign loss account to zero, and has a balance in its pre-1983 old section 907(b) overall foreign loss account of $400.

Par. 3. A new §1.1502-9 is added in the appropriate place to read as set forth below:

§1.1502-9 Application of overall foreign loss recapture rules to corporations filing consolidated returns.

(a) *In general*. An affiliated group of corporations filing a consolidated return sustains an overall foreign loss (a consolidated overall foreign loss) in any taxable year in which its gross income from sources without the United States subject to a separate limitation (as defined in §1.904(f)-1(c)(2)) is exceeded by the sum of the deductions properly allocated and apportioned thereto. The rules contained in §§1.904(f)-1 through 1.904(f)-6 are applicable to affiliated groups filing consolidated returns. This section provides special rules for applying those sections to such groups. Paragraph (b) provides rules for additions and subtractions of overall foreign losses to and from consolidated overall foreign loss accounts. Paragraph (c) requires that separate notional overall foreign loss accounts be kept for each member of the group that contributes to a consolidated overall foreign loss account and provides for allocation of overall foreign losses when a member leaves the group prior to recapture of the entire amount of such losses. Paragraph (d) provides rules for recapture of amounts in consolidated overall foreign loss accounts. Paragraph (e) provides special rules pertaining to section 904(f)(3) dispositions between members of a group. Paragraphs (b), (c), and (e) also contain special rules applying to overall foreign losses arising in separate return limitation years; the principles therein shall also apply to overall foreign losses where there has been a consolidated return change of ownership (as defined in §1.1502-1(g)).

(b) *Consolidated overall foreign loss accounts.* Any group sustaining an overall foreign loss (or acquiring a member having an overall foreign loss) must establish a consolidated overall foreign loss account for such loss, and amounts shall be added to and subtracted from such account as provided in §§1.904(f)-1 through 1.904(f)-6 and this section.

(1) *Additions to the consolidated overall foreign loss accounts*—(i) *Consolidated overall foreign losses.* Any consolidated overall foreign loss shall be added to the applicable consolidated overall foreign loss account for such separate limitation, to the extent that the overall foreign loss has reduced U.S. source income, in accordance with the rules of §§1.904(f)-1 and 1.904(f)-3.

(ii) *Overall foreign losses from separate return years.* If a corporation joins in the filing of a consolidated return in a taxable year in which such corporation has a balance in an overall foreign loss account from a prior separate return year that is not a separate return limitation year, such balance shall be added to the applicable consolidated overall foreign loss account in such year and treated as a consolidated overall foreign loss incurred in the previous year (and shall therefore be subject to recapture, in accordance with paragraph (d) of this section, beginning in the same year in which it is added to the consolidated overall foreign loss account).

(iii) *Overall foreign losses from separate return limitation years.* If a corporation joins in the filing of a consolidated return in a taxable year in which such corporation has a balance in an overall foreign loss account from a prior separate return limitation year, such balance shall be added to the applicable consolidated overall foreign loss account in such consolidated return year to the extent of consolidated foreign source taxable income subject to the same separate limitation (computed in accordance with §§1.904(f)-2(b) and 1.1502-4(d)(1)) minus such consolidated foreign source taxable income recomputed by excluding the items of income and deduction of such corporation (but not less than zero). The amount added to a consolidated overall foreign loss account in any taxable year under this paragraph (b)(1)(iii) shall be treated as a consolidated overall foreign loss in the previous year (and shall therefore be subject to recapture, in accordance with paragraph (d) of this section, beginning in the same year in which it is added to the consolidated overall foreign loss account).

(iv) *Overall foreign losses that are part of net operating losses or net capital losses carried over from a separate return limitation year.* Overall foreign losses that are part of a net operating loss or net capital loss carryover from a separate return limitation year of a member that is absorbed in a consolidated return year are treated as though they were added to an overall foreign loss account in a separate return limitation year of such member. See paragraph (c)(2) of this section for rules regarding the addition of such losses to the applicable overall foreign loss account of such member.

(2) *Reductions of the consolidated overall foreign loss accounts*—(i) *Amounts allocated to members leaving the group.* When a member leaves the group, each applicable consolidated overall foreign loss account shall be reduced by the amount allocated from such account to such member in accordance with paragraph (c)(3)(i) of this section.

(ii) *Amounts recaptured.* Each applicable consolidated overall foreign loss account shall be reduced by the amount of the overall foreign loss under the same separate limitation that is recaptured from consolidated income in accordance with §1.904(f)-2.

(c) *Allocation of overall foreign losses among members of an affiliated group*—(1) *Notional overall foreign loss accounts.* Separate notional overall foreign loss accounts shall be established for each member of a group that contributes to a consolidated overall foreign loss account. Additions to and reductions of such notional accounts shall be made when additions or reductions are made to consolidated overall foreign loss accounts in accordance with paragraph (b) of this section and §1.904(f)-1.

(i) *Additions to notional accounts*—(A) *Consolidated overall foreign losses.* When a consolidated overall foreign loss is added to a consolidated overall foreign loss account, each member shall add its pro rata share of the amount of such loss added to a consolidated overall foreign loss account to such member's notional overall foreign loss account. A member's pro rata share of the amount of such loss added to a consolidated overall foreign loss account for any taxable year is determined by multiplying such amount by a fraction. The numerator of this fraction is the amount by which the member's separate gross income for the taxable year from sources without the United States is exceeded by the sum of the deductions properly allocated and apportioned thereto (including such member's share of any consolidated net operating loss deduction and consolidated net capital loss carryovers and carrybacks to the taxable year), for each member with such deductions in excess of such income. The denominator of this fraction is the sum of the numerators of this fraction for all such members of the group.

(B) *Overall foreign losses from separate return years and separate return limitation years.* When an amount from a member's overall foreign loss account from a separate return year or separate return limitation year is added to a consolidated overall foreign loss account in accordance with paragraph (b)(1)(ii) or (iii) of this section,

such amount shall also be added to that member's notional overall foreign loss account for such separate limitation.

(ii) *Reductions of notional accounts.* When a consolidated overall foreign loss account is reduced by recapture, in accordance with paragraph (b)(2)(ii) of this section, each member of the group shall reduce its notional overall foreign loss account for such separate limitation by its pro rata share of the amount by which the consolidated overall foreign loss account is reduced. A member's pro rata share of the amount by which a consolidated overall foreign loss account is reduced is determined by multiplying such amount by a fraction, the numerator of which is the amount in such member's notional account under such separate limitation, and the denominator of which is the amount in the consolidated overall foreign loss account under such separate limitation before reduction for the amount recaptured for that taxable year.

(2) *Overall foreign losses that are part of net operating losses or net capital losses from separate return limitation years.* An overall foreign loss that is part of a net operating loss or net capital loss carryover from a separate return limitation year of a member that is absorbed in a consolidated return year shall be treated as an overall foreign loss of such member (rather than the group) and shall be added to such member's separate overall foreign loss account (for losses added to the member's overall foreign loss account under such separate limitation in prior separate return limitation years), to the extent it reduces U.S. source income, in accordance with §1.904(f)-1(d)(5). Such overall foreign losses shall be added to the appropriate consolidated overall foreign loss account in later years in accordance with paragraph (b)(1)(iii) of this section.

(3) *Allocation of overall foreign losses to a member leaving the group*—(i) *Consolidated overall foreign losses.* When a corporation ceases to be a member of an affiliated group filing consolidated returns, a portion of the balance in each applicable consolidated overall foreign loss account shall be allocated to such corporation. The amount allocated to such corporation shall be equal to the amount in such member's notional overall foreign loss account under the same separate limitation.

(ii) *Overall foreign losses from separate return limitation years.* When a corporation ceases to be a member of an affiliated group filing consolidated returns, it shall take with it the remaining portion of its separate overall foreign loss account for its overall foreign losses from separate return limitation years (including amounts added to such account under paragraph (c)(2) of this section) that has not been added to a consolidated overall foreign loss account under paragraph (b)(1)(iii) of this section.

(d) *Recapture of consolidated overall foreign losses.* The amount in any consolidated overall foreign loss account shall be recaptured under §§1.904(f)-1 through 1.904(f)-6 by recharacterizing consolidated foreign source taxable income subject to the limitation under which the loss arose as U.S. source taxable income. For purposes of recapture, consolidated foreign source taxable income subject to the limitation under which the loss arose shall be determined in accordance with §§1.904(f)-2 and 1.1502-4. Amounts in a member's excess loss account that are included in income under §1.1502-19 shall be subject to recapture to the extent that they are included in consolidated foreign source taxable income subject to the limitation under which the loss arose.

(e) *Dispositions of property between members of the same affiliated group during a consolidated return year*—(1) *Recapture of overall foreign loss from a separate return limitation year.* To the extent of any balance in a separate account for overall foreign losses from a separate return limitation year of a member (a "selling member") making a disposition of property to which section 904(f)(3)(A) applies to another member of the same affiliated group, no gain from such disposition shall be deferred under the rules of §1.1502-13(c).

(2) *Recapture of consolidated overall foreign loss not from a separate return limitation year.* Except as provided in paragraph (e)(1) of this section, the rules of §1.1502-13 with respect to deferral of gain shall apply to dispositions of property to which section 904(f)(3)(A) applies.

(f) *Illustrations.* The provisions of this section are illustrated by the following examples. All foreign source income or loss in these examples is subject to the section 904(d)(10(E) limitation.

Example (1). A, B, and C are the members of an affiliated group of corporations (as defined in section 1504), and all use the calendar year as their taxable year. For 1983, A, B, and C file a consolidated return. ABC has U.S. source income of $1000 and foreign source losses (overall foreign loss) of $400. In accordance with paragraph (b)(1)(i) of this section, ABC adds $400 to its consolidated overall foreign loss account at the end of 1983. For 1983, the separate foreign source taxable income (or loss) of A is $400, of B is ($200), and of C is ($600). Under paragraph (c)(1) of this section, B and C must establish separate notional overall foreign loss accounts. Under paragraph (c)(1)(i)(A) of this section, the amount added to each notional account is the pro rata share of the consolidated overall foreign loss of each member contributing to such loss. The pro rata share is determined by multiplying the consolidated loss by the member's proportionate share of the total foreign source losses of all members having such losses. B's foreign source loss is $200 and C's foreign source loss is $600, totalling $800. B must add $400 × 200/800, or $100, to its notional overall foreign loss account. C must add $400 × 600/800, or $300, to its notional overall foreign loss account.

Example (2). The facts are the same as in example (1). In 1984, ABC has consolidated foreign source taxable income of $200. Under paragraph (d) of this section and §1.904(f)-2, ABC is required to recapture $100 of the amount in its consolidated overall foreign loss account, which reduces that account by $100 under paragraph (b)(2)(ii) of this section. In accordance with paragraph (c)(1)(ii) of this section, B reduces its notional account by $100 × 100/400, or $25, and C reduces its notional account by $100 × 300/400, or $75. At the end of 1984 ABC has $300 in its consolidated overall foreign loss account, B has $75 in its notional account, and C has $225 in its notional account.

Example (3). D and E are members of an affiliated group and file separate returns using the calendar year as their taxable year for 1980. In 1980, D has an overall foreign loss of $200, which it adds to its overall foreign loss account, and E has no overall foreign losses. For 1981, D and E file a consolidated return, and DE must establish a consolidated overall foreign loss account, to which D's overall foreign loss from 1980 is added under paragraph (b)(1)(ii) of this section. D also adds the same amount to its notional account under paragraph (c)(1)(i) (B) of this section. In 1981, DE has consolidated foreign source taxable income of $300. Since the amount added to the consolidated overall foreign loss account in 1981 is treated as a consolidated overall foreign loss from 1980, DE must recapture $150 in 1981 under paragraph (d) of this section and §1.904(f)-2. DE's consolidated overall foreign loss account is reduced by $150 under paragraph (b)(2)(ii) of this section, and D's notional account is reduced by $150 under paragraph (c)(1)(ii) of this section, leaving balances of $50 in each of those accounts at the end of 1981.

Example (4). F and G are not members of an affiliated group in 1980, and G has an overall foreign loss of $200, which it adds to its overall foreign loss account. F has no overall foreign loss. On January 1, 1981, F acquires G, and FG files a consolidated return for the calendar year 1981. In 1981, F has no foreign source taxable income or loss, and G has $100 of foreign source taxable income. FG's consolidated foreign source taxable income, $100, minus such income without G's items of income and deduction, $0, is $100. Therefore $100 of G's overall foreign loss from its 1980 separate return limitation year is added to FG's consolidated overall foreign loss account under paragraph (b)(1)(iii) of this section, and the same amount is added to G's notional account under paragraph (c)(1)(i)(B) of this section. In accordance with paragraph (d) of this section and §1.904(f)-2, FG must recapture $50 of the balance in its consolidated overall foreign loss account in 1981 because the amount added from G's separate return limitation year is treated as a 1980 consolidated overall foreign loss. At the end of 1981, FG has a balance of $50 in its consolidated overall foreign loss account, G has $50 in its notional account, and G also has $100 remaining from its 1980 overall foreign loss that has not yet been added to the consolidated overall foreign loss account. On January 1, 1982, F sells G and G leaves the affiliated group. Under paragraph (c)(3)(i) of this section, $50 of the consolidated overall foreign loss account is allocated to G (an amount equal to the amount in G's notional account), and G also takes with it the balance in its overall foreign loss account from 1980 (its prior separate return limitation year) that has not been added to the consolidated account. The FG consolidated overall foreign loss account is reduced by $50 (to zero) and G has $150 of overall foreign loss in its overall foreign loss account.

Example (5). (i) In 1982 corporation H has U.S. source income of $300 and foreign source losses of $500, resulting in a net operating loss of $200 and a balance in H's overall foreign loss account at the end of 1982 of $300.

(ii) On January 1, 1983, H is acquired by J, and for the calendar year 1983 JH files a consolidated return. JH has consolidated taxable income of $700 in 1983, including a consolidated net operating loss deduction of $100. This net operating loss deduction is $100 of H's $200 net operating loss from 1982 (a separate return limitation year), which is limited by §1.1502-21(c). For 1983, H has separate taxable income of $100, comprised of $100 of U.S. source taxable income and zero foreign source taxable income, and J has separate taxable income of $700, comprised of $700 of U.S. source taxable income and zero foreign source taxable income. Under paragraph (c)(2) of this section, H adds $100 to its separate overall foreign loss account, since that amount of its net operating loss has reduced U.S. source income. H has $400 in its separate overall foreign loss account at the end of 1983, none of which has been added to a consolidated overall foreign loss account.

Example (5). (i) In 1982 corporation H has U.S. source income of $300 and foreign source losses of $500, resulting in a net operating loss of $200 and a balance in H's overall foreign loss account at the end of 1982 of $300.

(ii) On January 1, 1983, H is acquired by J, and for the calendar year 1983 JH files a consolidated return. JH has consolidated taxable income of $700 in 1983, including a consolidated net operating loss deduction of $100. This net operating loss deduction is $100 of H's $200 net operating loss from 1982 (a separate return limitation year), which is limited by §1.1502-21(c). For 1983, H has separate taxable income of $100, comprised of $100 of U.S. source taxable income and zero foreign source taxable income, and J has separate taxable income of $700, comprised of $700 of U.S. source taxable income and zero foreign source taxable income. Under paragraph (c)(2) of this section, H adds $100 to its separate overall foreign loss account, since that amount of its net operating loss has reduced U.S. source income. H has $400 in its separate overall foreign loss account at the end of 1983, none of which overall foreign loss account at the end of 1983, none of which has been added to a consolidated overall foreign loss account.

(iii) In 1984, H has separate taxable income of $400, comprised of $100 of U.S. source taxable income and $300 of foreign source taxable income. J has separate taxable income of $900, comprised of $700 of U.S. source taxable income and $200 of the foreign source taxable income. JH has consolidated taxable income of $1200, which includes $100 of consolidated net operating loss deduction from H's 1982 net operating loss. Since this net operating loss deduction is allocated to foreign source income, it does not reduce U.S. source income and will not be added to an overall foreign loss account. Under paragraph (b)(1)(iii) of this section, $200 from H's overall foreign loss is added to the consolidated overall foreign loss account computed as follows:

Consolidated foreign source taxable income	$ 400
Consolidated foreign source taxable income recomputed by excluding H's foreign source income and deductions	−200
Amount from H's separate return limitation year overall foreign loss account added to the consolidated overall foreign loss accodnt	$ 200

This amount is subject to recapture beginning in the same taxable year, as it is treated as a consolidated overall foreign loss incurred in a previous year. Therefore, under paragraph (d) of this section and §1.904(f)-2, JH also recaptures this $200, reducing the consolidated overall foreign loss account to zero. H has $200 remaining in its separate overall foreign loss account at the end of 1984.

(iv) In 1985, H has separate taxable income of $400, comprised of $100 of U.S. source taxable income and $300 of foreign source taxable income J has separate taxable income of $300 comprised of $600 of U.S. source taxable income and $300 of foreign source losses. JH has consolidated taxable income of $700, all of which is U.S. source. Under paragraph (b)(1)(iii) of this section, the remaining $200 from H's separate overall foreign loss is added to the consolidated overall foreign loss account, computed as follows:

Consolidated foreign source taxable income	$ 0
Consolidated foreign source taxable income recomputed by excluding H's foreign source income and deductions	(− 300)
Amount from H's separate return limitation year overall foreign loss account that may be added to the consolidated overall foreign loss account	$ 300

Thus, the entire $200 balance of H's separate overall foreign loss is added to the consolidated overall foreign loss account, and, under paragraph (c)(1)(i)(B) of this section, the same amount is added to H's notional account. While this amount is subject to recapture beginning in the same taxable year, JH has no consolidated foreign source taxable income in 1985, so no overall foreign loss is recaptured.

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on January 23, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 24, 1986, 51 F.R. 3193)

Correction to Publication 510

Announcement 86-27

Publication 510, *Excise Taxes for 1986* (Revised October 1985), contains several errors. On page 7, under the heading "Articles not subject to tax," the phrase "unless there has been a bead-to-bead recapping or retreading," should be deleted from the paragraph beginning "Recapped or retreaded tires." On page 7, in the paragraph under "Fuel Economy," the name of Form 6197 should be "Gas Guzzler Tax." In the second full paragraph on page 8, the tax rate should be *4½* cents per gallon.

Correction to Publications 527 and 17

Announcement 86-28

Publication 527, Rental Property (Rev. Nov. 85), contains an error in Example 1 on page 7. The townhouse in the example should be depreciated over an 18-year recovery period, not the 15-year recovery period shown. Correct depreciation on the townhouse is $5,850 ($65,000 × 9%). Therefore, total depreciation on the rental property is $5,914, and the net rental loss for the townhouse is $4,411.

This error also appears on page 55 of Publication 17, Your Federal Income Tax (Rev. Nov. 85).

Correction to Rev. Rul. 86-33

Announcement 86-33

Rev. Rul. 86-33, 1986-9 I.R.B. 17, contains an error in the last line of the second paragraph under FACTS. The acronym "FBCSI" should be replaced by "foreign base company income."

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Dal H. Felkel	Kingstree, SC	Certified Public Accountant	Indefinite from January 31, 1986
John J. Matonis	Walnut, CA	Attorney	Indefinite from January 24, 1986
Joel A. Shor	Baltimore, MD	Certified Public Accountant	Five Months from December 15, 1985
Patrick H. Diamond	New York, NY	Attorney & Certified Public Accountant	Indefinite from February 10, 1986
Folger P. Gifford	Cold Spring Harbor, NY	Certified Public Accountant	Indefinite from February 11, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.936-2, 1.936-3, 1.936-3A, added; 7.936-1, removed.	Qualified possession source investment income	1986-8 I.R.B. 33	Mar. 24, 1986
26 CFR 1.6031-1, revised.	Partnership returns	1986-9 I.R.B. 31	Mar. 24, 1986
26 CFR 1.401(a)-4, 1.411(d)-4, added.	Limitations on alternative benefits under qualified plans	1986-9 I.R.B. 26	Mar. 31, 1986

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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INTERNAL REVENUE BULLETIN

The Introduction on page 3 describes the purpose and content of this publication. The weekly Internal Revenue Bulletin is sold on a yearly subscription basis by the Superintendent of Documents. Current subscribers are notified by the Superintendent of Documents when their subscriptions must be renewed.

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1986-11

March 17, 1986
Bulletin No. 1986–11

Internal Revenue bulletin

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

T.D. 8071, page 4.

Amendments to the regulations under section 166 of the Code relate to the treatment of reserves for certain guaranteed debt obligations.

T.D. 8072, page 7.

LR-191-82, page 28.

Temporary and proposed regulations under section 338 of the Code relate to the determination of the basis of assets of a target corporation. In addition, existing temporary regulations relating to miscellaneous matters under section 338 are amended.

EXEMPT ORGANIZATIONS

Announcement 86-29, page 28.

A list is given of organizations now classified as private foundations.

ESTATE TAX

Rev. Rul. 86-38, page 22.

State death tax paid in installments. When an estate elects to pay the federal estate tax in installments and also elects to pay state death taxes in annual installments over a period longer than four years from the date of the filing of the federal estate tax return, the exception described in section 2011(c)(2) of the Code is applicable. State death taxes paid by the estate more than four years after the filing of the federal estate tax return are not eligible for the credit described in section 2011 when none of the exceptions described in sections 2011(c)(1) through (3) are applicable.

ESTATE AND GIFT TAXES

Rev. Rul. 86-39, page 23.

Recapitalization; shift in value of trust assets; release of general power of appointment. Acquiescence in a recapitalization of closely held stock in a trust is a transfer by the trust beneficiary subject to the gift tax, where the recapitalization results in a shift in the beneficiary's interest by decreasing the value of the remainder interest over which the beneficiary has a general power of appointment.

EXCISE TAXES

Notice 86-4, page 26.

Windfall profit tax; inflation adjustment factor. For purposes of computing the windfall profit tax, the inflation adjustment for the quarter ending June 30, 1986, is 0.4524 for tier 1 or tier 2 oil and 0.6535 for tier 3 oil.

ADMINISTRATIVE

Rev. Proc. 86-15, page 26.

Publication standards; revenue rulings and revenue procedures. The objectives of, and standards for, publication of revenue rulings and revenue procedures in the Internal Revenue Bulletin are revised to reflect the reorganization of the Internal Revenue Service in accordance with Treasury Department Order No. 150-95, effective March 21, 1982, under Delegation Order No. 190, the establishment of the office of the Associate Chief Counsel (International), and the responsibility of the Assistant Commissioner (Support and Services) for publishing the Internal Revenue Bulletin. Rev. Proc. 78-24 superseded.

Announcement 86-30, page 29.

The instructions to Form 8308 are clarified.

Finding Lists begin on page 33.
Announcement of Suspensions on page 31.
Announcement of Notice of Proposed Rulemaking on page 32.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 166.—Bad Debts

26 CFR 1.166-1: Bad debts.
(Also Section 381: 1.381(c)(4)-1.)

T.D. 8071

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, SUBCHAPTER H, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Reserve for Certain Guaranteed Debt Obligations

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the treatment of reserves for certain guaranteed debt obligations. Changes in the applicable tax law were made by the Act of November 2, 1966 [Pub. L. 89-722, 1966-2 C.B. 645]. The regulations provide the public with the guidance needed to comply with that Act and affect taxpayers who have a reserve for guaranteed debt obligations or intend to set up such a reserve.

DATES: The amendments are generally effective for taxable years ending after October 21, 1965.

FOR FURTHER INFORMATION CONTACT: Bruce H. Jurist of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T (202-566-3238, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

On July 11, 1980, proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 166(f) of the Internal Revenue Code of 1954 were published in the FEDERAL REGISTER (45 FR 46815). The amendments were proposed to conform the regulations to changes made by the Act of November 2, 1966 (Pub. L. 89-722, 80 Stat. 1151) (the Act) [1966-2 C.B. 645], which added section 166(g) to the Internal Revenue Code of 1954. Section 166(g) was redesignated as section 166(f) by section 605 of the Tax Reform Act of 1976 (90 Stat. 1575) [Pub. L. 94-455, 1976-3 C.B. (Vol. 1), 51]. No public hearing was requested and accordingly none was held. After consideration of all comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

DISCUSSION

Section 166(f)(1) provides that a taxpayer who is a dealer in property may take an income tax deduction for reasonable additions to a reserve for bad debts which may arise from the dealer's contingent liability as a guarantor, endorser, or indemnitor of debt obligations arising out of the sale by the dealer of real property or tangible personal property (including related services) in the ordinary course of the dealer's trade or business.

Section 166(f)(2) makes section 166(f)(1) the exclusive section under which a deduction is allowable for an addition to a reserve for guaranteed debt obligations.

Section 166(f)(3) provides that a taxpayer shall establish an opening balance for a reserve for section 166(f)(1)(A) guaranteed obligations as if the taxpayer had maintained the reserve in prior years.

To prevent a doubling up of deductions in the period of transition from the specific charge-off method of treating these obligations to the new method, sections 81 and 166(f)(1)(B) mandate an addition to or a deduction from income based upon a required annual adjustment to the suspense account.

In addition, section 1(c) of the Act allows taxpayers a grace period in which to adopt such a reserve method without obtaining the permission of the Service. This Treasury decision extends that grace period until April 17, 1986.

Nothing in the new law or these regulations would affect the longstanding principle that additions to a reserve for bad debts previously deducted in computing taxable income must be included in taxable income when and to the extent that the reserve is longer necessary.

PUBLIC COMMENTS

The sole comment received requested that §1.166-10(d) be made prospective and apply only to returns filed after July 10, 1980, because a literal reading of §1.166-10(d) as set forth in the notice of proposed rulemaking seemed to require the filing of amended returns for any open year in which the taxpayer claimed deductions for additions to reserves for guaranteed debt obligations. Therefore, the Treasury decision makes it clear that the filing requirement set forth in §1.166-10(d) applies only to returns filed after April 17, 1986.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required. Although a notice of proposed rulemaking soliciting public comments was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these regulations are not subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB.

DRAFTING INFORMATION

The principal author of these proposed regulations is Bruce H. Jurist of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * * *

Proposed amendments to the regulations.

Accordingly 26 CFR Part 1 and Part 602 are amended as follows:

INCOME TAX REGULATIONS
(26 CFR Part 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.166-10 also issued under 26 U.S.C. 166(f).

Par. 2. Section 1.166-1 is amended by adding a new paragraph (b)(4) to read as follows:

§1.166-1 Bad debts.

* * * * *

(b) *Manner of selection method.* * * *

(4) Notwithstanding paragraph (b)(1), (2), and (3) of this section, a dealer in property currently employing the accrual method of accounting and currently maintaining a reserve for bad debts under section 166(c) (which may have included guaranteed debt obligations described in section 166(f)(1)(A)) may establish a reserve for section 166(f)(1)(A) guaranteed debt obligations for a taxable year ending after October 21, 1965 under section 166(f) and §1.166-10 by filing on or before April 17, 1986, an amended return indicating that such a reserve has been established. The establishment of such a reserve will not be considered a change in method of accounting for purposes of section 446(e). However, an election by a taxpayer to establish a reserve for bad debts under section 166(c) shall be treated as a change in method of accounting. See also §1.166-4, relating to reserve for bad debts, and §1.166-10, relating to reserve for guaranteed debt obligations.

* * * * *

Par. 3. Paragraph (a) of §1.166-4 is amended by adding at the end thereof the following:

§1.166-4 Reserve for bad debts.

(a) *Allowance of deduction.* * * *

This paragraph applies both to bad debts owed to the taxpayer and to bad debts arising out of section 166(f)(1)(A) guarantees debt obligations. If a reserve is maintained for bad debts arising out of section 166(f)(1)(A) guaranteed debt obligations, then a separate reserve must also be maintained for all other debt obligations of the taxpayer in the same trade or business, if any. A taxpayer may not maintain a reserve for bad debts arising out of section 166(f)(1)(A) guaranteed debt obligations if with respect to direct debt obligations in the same trade or business the taxpayer takes deductions when the debts become worthless in whole or in part rather than maintaining a reserve for such obligations. See §1.166-10 for rules concerning section 166(f)(1)(A) guaranteed debt obligations.

* * * * *

Par. 4. The following new section is inserted immediately after §1.166-9:

§1.166-10 Reserve for guaranteed debt obligations.

(a) *Definitions.* The following provisions apply for purposes of this section and section 166(f);

(1) *Dealer in property.* A dealer in property is a person who regularly sells property in the ordinary course of the person's trade or business.

(2) *Guaranteed debt obligation.* A guaranteed debt obligation is a legal duty of one person as a guarantor, endorser or indemnitor of a second person to pay a third person. It does not include duties based solely on moral or good public relations considerations that are not legally binding. A guaranteed debt obligation typically arises where a seller receives in payment for property or services the debt obligation of a purchaser and sells that obligation to a third party with recourse. However, a guaranteed debt obligation also may arise out of a sale in respect of which there is no direct debtor-creditor relationship between the debtor purchaser and the seller. For example, it arises where a purchaser borrows money from a third party to make payment to the seller and the seller guarantees the payment of the purchaser's debt. Generally, debt obligations which are sold without recourse do not result in any obligation of the seller as a guarantor, endorser, or indemnitor. However, there are certain without-recourse transactions which may give rise to a seller's liability as a guarantor or indemnitor. For example, such a liability may arise where a holder of a debt obligation holds money or other property of a seller which the holder may apply, without seeking permission of the seller, against any uncollectible debt obligations transferred to the holder by the seller without recourse, or where the seller is under a legal obligation to require the real or tangible personal property from the holder of the debt obligation who repossessed property in satisfaction of the debt obligations.

(3) *Real or tangible personal property.* Real or tangible personal property generally does not include other forms of property, such as securities. However, if the sale of other property is related to the sale of actual real or tangible personal property, the other property will be considered to be real or tangible personal property. In order for the sale of other property to be related, it must be—

(i) Incidental to the sale of the actual real or tangible personal property; and

(ii) Made under an agreement, entered into at the same time as the sale of actual real or tangible personal property, between the dealer in that property and the customer with respect to that property.

The other property may be charged for as a part of, or in addition to, the sales price of the actual real or tangible personal property. If the value of the other property is not greater than 20 percent of the total sales price, including the value of all related services other than financing services, the sale of the other property is related to the sale of actual real or tangible personal property.

(4) *Related services.* In the case of a sale of both property and services a determination must be made as to whether the services are related to the property. Related services include only those services which are—

(i) Incidental to the sale of the real or tangible personal property; and

(ii) To be performed under an agreement, entered into at the same time as the sale of the property, between the dealer in property and the customer with respect to the property.

Delivery, financing, installation, maintenance, repair, or instructional services, generally qualify as related services. The services may be charged for as a part of, or in addition to, the sales price of the property. Where the value of all services other than financing services is not greater than 20 percent of the total of the sales price of the property, including the value of all the services other than financing services, all of the services are considered to be incidental to the sale of the property. Where the value of the services is greater than 20 percent, the determination as to whether a service is a related service in a particular case is to be made on the basis of all relevant facts and circumstances.

(5) *Examples*. The following examples apply to paragraph (a)(4) of this section:

Example (1). A, a dealer in television sets, sells a television set to B, his customer. If at the time of the sale A, for a separate charge which is added to the sales price of the set and which is not greater than 20 percent of the total sales price, provides a 3-year service contract on only that television set, the service contract is a related service agreement. However, if A does not sell the service contract to B contemporaneously with the sale of the television set, as would be the case if the service agreement were entered into after the sale of the set were completed, or if the service contract includes services for a television set in addition to the one then sold by A to B, the service contract is not an agreement for a related service.

Example (2). C, an automobile dealer, at the time of the sale by C of an automobile to D, agrees to make available to D driving instructions furnished by the M driving school, the cost of which is included in the sale price of the automobile and is not greater than 20 percent of the total sales price. C also agrees to pay M for the driving instructions furnished to D. Since C's agreement with D to make available driving instructions is incidental to the sale of the automobile, is made contemporaneously with the sale, and is charged for as part of the sales price of the automobile, it is an agreement for a related service. In contrast, however, because M's agreement with C is not an agreement between the dealer in property and the customer, M's agreement with C to provide driving instructions to C's customers is not an agreement for a related service.

(b) ***Incorporation by reference of section 166(c) rules***. A reserve for section 166(f)(1)(A) guaranteed debt obligations must be established and maintained under the rules applicable to the reserve for bad debts under section 166(c) (with the exception of the statement requirement under §1.166-4(c)). For example, the rules in §1.166-4(b), relating to what constitutes a reasonable addition to a reserve for bad debts and to correction of errors in prior estimates, apply to a reserve for section 166(f)(1)(A) guaranteed debt obligations as well.

(c) *Special requirements*. Any reserve for section 166(f)(1)(A) guaranteed debt obligations must be established and maintained separately from any reserve for other debt obligations. In addition, a taxpayer who charges off direct debts when they become worthless in whole or in part rather than maintaining a reserve for such obligations may not maintain a reserve for section 166(f)(1)(A) guaranteed debt obligations in the same trade or business.

(d) *Requirement of statement*. A taxpayer who uses the reserve method of treating section 166(f)(1)(A) guaranteed debt obligations must attach to his return for each taxable year, returns for which are filed after April 17, 1986, and for each trade or business for which the reserve is maintained a statement showing—

(1) The total amount of these obligations at the beginning of the taxable year;

(2) The total amount of these obligations incurred during the taxable year;

(3) The amount of the initial balance of the suspense account, if any, established with respect to these obligations;

(4) The balance of the suspense account, if any, at the beginning of the taxable year;

(5) The adjustment, if any, to that account;

(6) The adjusted balance, if any, at the close of the taxable year;

(7) The reconciliation of the beginning and closing balances of the reserve for these obligations and the computation of the addition to the reserve; and

(8) The taxable year for which the reserve for these obligations was established.

(e) *Computation of opening balance*—(1) *In general*. The opening balance of a reserve for section 166(f)(1)(A) guaranteed debt obligations established for the first taxable year for which a taxpayer maintains such a reserve shall be determined as if the taxpayer had maintained such a reserve for the taxable years preceding that taxable year. The amount of the opening balance may be determined under the following formula:

$$OB = CG \times \frac{SNL}{SG}$$

where—

OB = the opening balance at the beginning of the first taxable year

CG = the amount of these obligations at the close of the last preceding taxable year

SG = the sum of the amounts of these obligations at the close of the five preceding taxable years

SNL = the sum of the amounts of net losses arising from these obligations for the five preceding taxable years

(2) ***Example***. The following example applies to paragraph (e)(1) of this section.

Example. For 1977, A, a dealer in automobiles who uses the calendar year as the taxable year, adopts in accordance with this section the reserve method of treating section 166(f)(1)(A) guaranteed debt obligations. A's first year in business as an automobile dealer is 1973. For 1972, 1973, and 1974, 1975, and 1976, A's records disclose the following information with respect to these obligations:

Year	Obligations outstanding at close of year	Gross losses from these obligations	Recoveries from these obligations	Net losses from these obligations
1972	$0	$0	$0	$0
1973	780,000	9,700	1,000	8,700
1974	795,000	8,900	1,050	7,850
1975	850,000	8,850	850	8,000
1976	820,000	9,300	1,400	7,900
Total	3,245,000	36,750	4,300	32,450

The opening balance for 1977 of A's reserve for these obligations is $8,200, determined as follows:

$$\$8,200 = \$820,000 \times \frac{\$32,450}{\$3,245,000}$$

(3) ***More appropriate balance***. A taxpayer may select a balance other than the one produced under paragraph (e)(1) of this section if it is more appropriate, based upon the taxpayer's actual experience, and in the event the taxpayer's return is examined, if the balance is approved by the district director.

(4) ***No losses in the five preceding taxable years***. If a taxpayer is in the

taxpayer's first taxable year of a particular trade or business, or if the taxpayer has no losses arising from section 166(f)(1)(A) guaranteed debt obligations in a particular trade or business for any other reason in the five preceding taxable years, then the taxpayer's opening balance is zero for that particular trade or business.

(5) *Where reserve method was used before October 22, 1965.* If for a taxable year ending before October 22, 1965, the taxpayer maintained a reserve for bad debts under section 166(c) which included guaranteed debt obligations described in section 166(f)(1)(A), and if the taxpyaer is allowed a deduction referred to in paragraph (g)(2) of this section on account of those obligations, the amount of the opening balance of the reserve for section 166(f)(1)(A) guaranteed debt obligations for the taxpayer's first taxable year ending after October 21, 1965, shall be an amount equal to that portion of the section 166(c) reserve at the close of the last taxable year which is attributable to those debt obligations. The amount of the balance of the section 166(c) reserve for the taxable year shall be reduced by the amount of the opening balance of the reserve for those guaranteed debt obligations.

(f) *Suspense account*—(1) *Zero opening balance cases.* No suspense account shall be maintained if the opening balance of the reserve for section 166(f)(1)(A) guaranteed debt obligations under section 166(f)(3) is zero.

(2) *Example.* The following example applies to section 166(f)(4)(B), relating to adjustments to the suspense account:

Example. In 1977, A, an individual who operates an appliance store and uses the calendar year as the taxable year, adopts the reserve method of treating section 166(f)(1)(A) guaranteed debt obligations. The initial balance of A's suspense account is $8,200. At the close of 1977, 1978, 1979, and 1980, the balance of A's reserve for these obligations is $8,400, $8,250, $8,150, and $8,175, respectively, after making the addition to the reserve for each year. The adjustments under section 166(f)(4)(B) to the suspense account at the close of each of the years involved are as follows:

(1) Taxable year	1977	1978	1979	1980
(2) Closing reserve account balance	$8,400	$8,250	$8,150	$8,175
(3) Opening suspense account balance	8,200	8.200	8,200	8,150
(4) Line (2) less line (3)	200	50	(50)	25
(5) Adjustment to suspense account balance	0	0	(50)	25
(6) Closing suspense account balance (line 3 plus line 5)	8,200	8,200	8,150	8,175

(g) *Effective date*—(1) *In general.* this section is generally effective for taxable years ending after October 21, 1965.

(2) *Transitional rule.* Section 2(b) of the Act of November 2, 1966 (Pub. L. 89-722, 80 Stat. 1151) allows additions to section 166(c) bad debt reserves in earlier taxable years on account of section 166(f)(1)(A) guaranteed debt obligations to be deducted for those earlier taxable years. Paragraphs (c), (d), (e), and (f) of this section do not apply in determining whether a deduction is allowed under section 2(b) of the Act. See Rev. Rul. 68-313 (1968-1 C.B. 75) for rules relating to that deduction.

Par. 5. Paragraph (a)(1)(ii) of §1.381(c)(4)-1 is amended by inserting a new sentence between the second and third sentences. The new sentence reads as follows:

§1.381(c)(4)-1 Method of accounting.

(a) *Carryover requirement*—(1) *General rule.* * * *

(ii) * * * The acquiring corporation shall also take into its accounts the dollar balance of that account of the distributor or transferor corporation which represents a suspense account established by the distributor or transferor corporation under section 166(f)(4) in taxable years ending on or before the date of distribution or transfer.* * *

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

(26 CFR Part 602)

Par. 6. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 7. Section 602.101(c) is amended by inserting in the appropriate places in the table "§1.661-1(b)(4) . . 1545-0123" and "§1.166-10 . . 1545-0123."

This Treasury decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved October 16, 1985.

RONALD A. PEARLMAN,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on January 16, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 17, 1986, F.R. 2478)

Section 338.—Certain Stock Purchases Treated as Asset Acquisitions

26 CFR 1.338-4T: Questions and answers relating to miscellaneous issues under section 338 (temporary).

TD. 8072

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Temporary Regulations Under Section 338(b) of the Internal Revenue Code of 1954

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to section 338(b) of the Internal Revenue Code of 1954 ("Code") as added by the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") [Pub. L. 97-248, 1982-2 C.B. 462]. This document also contains amendments to other temporary regulations under section 338. The temporary regulations provide guidance to taxpayers concerning the application of section 338. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations cross-referenced * * *[on page 28, this Bulletin].

DATES: These regulations are effective January 29, 1986. These temporary regulations under section 338(b) and the amendments to the temporary regulations generally apply to stock acquisitions made after August 31, 1982.

FOR FURTHER INFORMATION CONTACT: Patricia Wendlandt or

Bennett C. Steinhauer of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T (202-566-3458, not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document adds new temporary regulations §§1.338(b)-1T through 1.338(b)-3T to Part 1 of Title 26 of the Code of Federal Regulations to implement section 338(b) of the Code. Section 338(b) was originally added by section 224 of TEFRA (Pub. L. No. 97-248; 96 Stat. 485) [1982-2 C.B. 462, 501] and was amended by section 712(k) of the Tax Reform Act of 1984 (TRA) (Pub. L. 98-369; 98 Stat. 948) [1984-3 C.B. (Vol. 1), 1 456].

EXPLANATION OF PROVISIONS

INTRODUCTION

Section 338, generally, provides that, if the stock of a corporation ("target") is acquired by another corporation ("purchasing corporation") in a qualified stock purchase, the purchasing corporation may elect (or may be deemed to elect under certain consistency rules) to have the target treated as if it had sold in a single transaction all of its assets (as "old target") and then purchased those assets (as "new target"). The deemed sale of assets by old target takes place at the close of the day on which the purchase occurred ("acquisition date") and generally is governed by the nonrecognition provisions of section 337. New target is deemed to purchase those assets ("acquisition date assets") at the beginning of the day after the acquisition date. Section 338(b) sets forth the framework for determining the aggregate amount of new target's deemed purchase price of old target's assets ("adjusted grossed-up basis") and allocating this amount among new target's acquisition date assets.

The temporary regulations implement section 338(b) in three sections. The first, §1.338(b)-1T, provides rules to determine adjusted grossed-up basis generally as of the beginning of the day after the acquisition date. Section 1.338(b)-2T provides rules for allocating adjusted grossed-up basis, as determined under §1.338(b)-1T, among the acquisition date assets of new target. Sections 1.338(b)-1T and 1.338 (b)-2T also apply to certain increases (or decreases) in adjusted grossed-up basis that are attributable to increases (or decreases) in amounts paid for old target's stock, to reductions in old target's liabilities that were into account in determining adjusted grossed-up basis, or to liabilities of old target that become fixed and determinable if such events (collectively referred to as "adjustment events") occur during new target's first taxable year. The third, §1.338(b)-3T, provides rules for determining and allocating adjusted grossed-up basis attributable to adjustment events occurring after new target's first taxable year.

ADJUSTED GROSSED-UP BASIS

Adjusted grossed-up basis is the sum of (1) the basis of target's recently purchased stock (grossed-up to account for minority interests by multiplying the basis by the fraction set forth in section 338(b)(4)), (2) the basis of target's nonrecently purchased stock, (3) the liabilities of new target as of the beginning of the day after the acquisition date (other than liabilities that were not liabilities of old target), and (4) other relevant items. As previously stated, adjusted grossed-up basis is ordinarily determined at the beginning of the day after the acquisition date. However, adjustment events occurring by the close of new target's first taxable year are taken into account in determining adjusted grossed-up basis as if they had occurred at the beginning of the day after the acquisition date.

The liabilities of target accounted for in adjusted grossed-up basis include the liabilities to which its assets are subject. Except in the case of a qualified stock purchase for which an election is made under section 338(h)(10), liabilities also include income tax liabilities of old target resulting from the deemed sale of its assets. For a liability to be included in adjusted grossed-up basis, it must be a bona fide liability of target at the beginning of the day after the acquisition date that is properly includible in basis under principles of tax law that would apply if target had acquired its assets as of the beginning of the day after the acquisition date from an unrelated party and, as part of the transaction, had assumed or taken property subject to the liability. Liabilities excluded under that rule, however, are taken into account under principles of tax law that would apply if target had acquired its assets from an unrelated person and, as part of the transaction, had assumed or taken property subject to those liabilities. See §1.338(b)-3T for application of these principles of tax law to certain contingent liabilities that are initially excluded from adjusted grossed-up basis.

Grossed-up basis is also adjusted for "other relevant items." For this purpose, "other relevant items" include adjustment events occuring after new target's first taxable year. The rules governing the timing and allocation of these adjustments are in §1.338(b)-3T. If the amount of adjusted grossed-up basis of a target allocated to the stock of its subsidiary that is also a target is subsequently increased (or decreased) by reason of an other relevant item, the grossed-up basis of the subsidiary's stock (and adjusted grossed-up basis) is also increased (or decreased) as if the increase (or decrease) in basis of the subsidiary's stock was an adjustment to the purchase price deemed paid by the target parent.

Upon the examination of a return the Internal Revenue Service also may increase (or decrease) adjusted grossed-up basis under the authority of section 338(b)(2) for other items and allocate such amounts to target assets under the authority of section 338(b)(5) so that adjusted grossed-up basis and the basis of target assets properly reflect the purchasing corporation's cost of those assets. Such items may include distributions from target to the purchasing corporation, capital contributions from the purchasing corporation to target during the 12-month acquisition period, or acquisitions of target stock by the purchasing corporation after the acquisition date from minority shareholders at an average price which is lower than the average cost of recently purchased stock. In determining whether an adjustment is appropriate when stock is purchased after the acquisition date from minority shareholders at an average price which is lower than the average cost of recently purchased stock, the Internal Revenue Service will take into account all the facts and circumstances, which may include the account of the price differential and the reason therefor, the number of shares purchased after the acquisition date, the timing of the purchase, and the source of the additional shares.

ALLOCATION OF ADJUSTED GROSSED-UP BASIS

Adjusted grossed-up basis is generally allocated among the target assets as of the beginning of the day after the acquisition date. Prior to any allocation, adjusted grossed-up basis is reduced by the amount of cash, deposits in banks and similar depository institutions, and any other similar cash items designed by the Internal Revenue Service ("Class I assets"). The balance is generally alocated among the remaining assets of target in proportion to their fair market values as of the beginning of the day after the acquisition date in the following order:

1. Certificates of deposit, U.S. government securities, certain readily marketable stocks and securities, foreign currency, and any other similar items designated by the Internal Revenue Service ("Class II assets");
2. All other assets of target except assets in the nature of goodwill and going concern value ("Class III assets"); and
3. Intangible assets in the nature of goodwill and going concern value ("Class IV assets").

Because of the difficulty in valuing goodwill and going concern value, it was decided to value and assign basis to other assets first, with the residual excess (*i.e.*, the amount of adjusted grossed-up basis over the amount allocated to those other assets), if any, being assigned to goodwill and going concern value.

Section 1.338(b)-2T(c)(3) prescribes a special rule (the pro rata rule) for allocation of adjusted grossed-up basis when the purchasing corporation holds nonrecently purchased stock with an average basis lower than the average basis of its recently purchased stock. This special rule is provided in order to prevent an insufficient allocation of basis to assets in the nature of goodwill or going concern value. Solely for the purpose of allocating adjusted grossed-up basis, the fair market value of goodwill or going concern value is deemed to be the excess, if any, of the hypothetical purchase price (determined in accordance with §1.338(b)-2T(c)(3)(ii)) over the sum of the amount of Class I assets and the fair market values of Class II and III assets. The hypothetical purchase price is the basis of recently purchased stock (grossed-up to account for minority interests and nonrecently purchased stock), plus target's liabilities and other relevant items that are taken into account in determining adjusted grossed-up basis. Finally, adjusted grossed-up basis is allocated (after reduction by the amount of Class I assets of target) among the Class II, III, and IV assets in proportion to their fair market values as of the beginning of the day after the acquisition date. Changes in the price paid for recently or nonrecently purchased stock after the close of new target's first taxable year are not taken into account in determining whether this special basis allocation rule applies.

The amount of adjusted grossed-up basis allocated to an asset, other than those in the future of goodwill and going concern value, cannot exceed its fair market value. The "fair market value" of an asset is its fair market value determined without regard to mortgages, liens, pledges, or other liabilities.

Under the foregoing allocation rules (and unlike the rules under pre-TEFRA section 334(b)(2)), liabilities to which an asset is subject are no longer to be specifically allocated to the asset. The so-called specific lien rule has not been followed for purposes of allocating basis because in certain circumstances the rule could inappropriately shift the allocation of basis from some assets to others.

In general, §1.1001-2(a)(3) provides that the discharge of a liability incurred by reason of the acquisition of property is not included in the amount realized from the sale or other disposition of the property to the extent the liability was not taken into account in determining the transferor's basis of such property. For purposes of applying §1.1001-2(a) in determining the amount realized on a sale or other disposition of property deemed purchased by new target, the amount of any liability included in adjusted grossed-up basis is considered to be an amount taken into account in determining new target's basis in the property which is secured by such liability. Thus, if a liability is included in adjusted grossed-up basis, §1.1001-2(a)(3) shall not prevent the amount of such liability from being treated as discharged within the meaning of §1.1001-2(a)(4).

If the amount of basis of an asset acquired in a sale or exchange is limited under a provision of the Internal Revenue Code or principles of tax law, then the amount of adjusted grossed-up basis allocated to the asset is so limited. Thus, for example, the amount of the adjusted grossed-up basis allocated a player contract described in section 1056 cannot exceed the limitation imposed by that section.

Amendments are made to §1.338-4T to require, in cases in which section 338(h)(10) is not elected, that the fair market value of an asset (other than goodwill or going concern value) used to determine the amount of any gain (or loss) recognized under section 338(a)(1) or (c)(1) to be the same as the fair market value used to allocate basis under these temporary regulations. Similarly, the allocation fraction described in §1.338-4T(h)(3) *Answer 2* (vi)(E) (relating to allocation of aggregate deemed sale price under the elective formula under section 338(h)(11)) must assign the same fair market value to a given asset that is assigned to such asset for purposes of the basis allocation rules. The amounts assigned as fair market values are subject to section 7701(h) (relating to fair market value in the case of nonrecourse indebtedness).

Section 1.338-4T is also amended to prescribe that aggregate deemed sale price calculated under the elective formula must be allocated in a manner consistent with the allocation of adjusted grossed-up basis. Thus, aggregate deemed sale price, after reduction for Class I assets, generally is allocated among Class II assets, then among Class III assets, with the residual excess, if any, allocated to Class IV assets.

SUBSEQUENT ADJUSTMENTS TO ADJUSTED GROSSED-UP BASIS

Section 1.338(b)-3T provides rules for adjustments to adjusted grossed-up basis for adjustment events occurring after the close of new target's first taxable year. It also provides rules for the allocation of those adjustments among target's acquisition date assets. These rules provide for the incorporation of general principles of tax law which are applicable to the determination of the basis of assets acquired in actual asset purchases. See the discussion in the following section for the application of similar principles with respect to adjustments of the aggregate deemed sale price of old target's assets.

Contingent amounts paid by the purchasing corporation for target stock held on the acquisition date and liabilities of old target that become fixed and determinable after the close of new target's first taxable year (basis increase amounts) are taken into account in adjusted grossed-up basis when the amount becomes fixed and determinable. Basis increase amounts are allocated among target's acquisition date assets in accordance with the general allocation rules set forth in §1.338(b)-2T, subject to the limitation rules contained in that section. Thus, in general, the aggregate amount of adjusted grossed-up basis allocated to an acquisition date asset may not exceed the asset's fair market value at the beginning of the day after the acquisition date, except for assets in the nature of goodwill or going concern value.

If an acquisition date asset has been disposed of (or depreciated, amortized, or depleted) before a basis increase amount is included in adjusted grossed-up basis, the amount of adjusted grossed-up basis that would otherwise be allocated to the asset under §1.338(b)-2T is treated under principles of tax law applicable when part of the cost of an asset is paid after the asset has been disposed of (or depreciated, etc.). Thus, for example, an amount of adjusted grossed-up basis otherwise allocable to a disposed of capital asset may be deducted by new target as a capital loss. See *Arrowsmith v. Commissioner*, 344 U.S. 6 (1952).

The rule for reductions (or rebates) in the amount paid for target stock held on the acquisition date and reductions in old target's liabilities that were taken into account in determining adjusted grossed-up basis (basis decrease amounts) is similar to the one for basis increase amounts, except that basis decrease amounts are allocated to target's acquisition date assets in the reverse of the order in which adjusted grossed-up basis is allocated under §1.338(b)-2T. Thus, as general rule, basis decrease amounts are allocated first among the acquisition date assets in the nature of goodwill and going concern value of the extent of their bases, and then as a reduction in the basis of target's other acquisition date assets.

The basis decrease amount is taken into account for purposes of calculating adjusted grossed-up basis and basis of target's assets when the reduction occurs. Similar principles of tax law apply to amounts that are allocable to acquisition date assets that have been disposed of (or depreciated, etc.) as those that apply to basis increase amounts.

If the pro rata rule was used to allocate basis, special rules apply to account for basis increase amounts (or basis decrease amounts).

The temporary regulations provide a special rule for allocating a basis increase amount (or basis decrease amount) resulting from adjustment events that directly relate to the income produced by a particular intangible asset, such as a patent, copyright, or secret process ("contingent income assets"), as long as the basis increase amount (or basis decrease amount) does not relate to other target assets. Subject to the limitations in §1.338(b)-2T(c)(1) and (2), the basis increase amount (or basis decrease amount) is first allocated to the contingent income asset and then to other target assets. Solely for purposes of applying the various limitation rules to a contingent income asset, its fair market value may be redetermined as of the time when the basis increase amount (or basis decrease amount) is taken into account. In appropriate cases, the Internal Revenue Service may apply the principles of this provision to reallocate a basis increase amount (or basis decrease amount) among some of target's assets to the extent such allocation is necessary to reflect properly the consideration that relates to each of those assets.

OLD TARGET'S DEEMED SALE

Section 1.338(b)-3T(h) provides that the price at which old target is deemed to have sold its assets must be adjusted to take into account events occurring after the acquisition date as required under general principles of tax law. In making this determination, the recognition of income, loss, or other amount shall not be precluded because old target is treated as a new corporation after the acquisition date. For example, if an elective formula under section 338(h)(11) is used to determine the aggregate deemed sale price, that price generally must be increased by the amount of any additional payments made to the seller for recently purchased stock. Accordingly, to the extent general tax law principles would require seller to account for adjustment events, target (or a member of the selling consolidated group in the event of an election under section 338(h)(10)) must make such an accounting, which may result in reporting income, loss, or other amount.

If no election is made under section 338(h)(10), any income, loss, or other amount resulting from such change is included in new target's income tax return for the taxable year in which the adjustment event occurs. Although included in new target's return, such income, loss, or other amount is separately accounted for as an item of income, loss, or other amount of old target. Therefore, such income, loss, or other amount may not be offset by income, loss, etc. of new target. Any increase (or decrease) in new target's income tax liability by reason of this rule is allocated among new target's acquisition date assets. Also, if no election is made under section 338(h)(10), net operating losses and net capital losses of old target may be carried forward to offset income items described above. Similarly, any ordinary or capital loss of old target accounted for as a separate item after the acquisition date may be carried back to taxable years of old target. For these purposes, new target's taxable years shall not be taken into account in applying the taxable-year limitation (generally 15 years for ordinary losses and 5 years for capital losses) or loss carryovers or the taxable-year limitation (generally 3 years) or loss carrybacks. Thus, if old target has an unexpired net operating loss at the close of its taxable year in which the deemed asset sale occurred which could have been carried forward to a subsequent taxable year, such loss may be carried forward until it is absorbed by old target's income. A similar rule allows tax credit carryovers of old target to offset any tax on the income items of old target described above.

If an election is made under section

338(h)(10), any income, loss, or other amount resulting from such change is accounted for and reported by the appropriate member of the selling consolidated group for the taxable year in which the adjustment event occurs. In applying carryover and carryback limitations in such cases, the special rules relating to the application of the taxable-year limitation for losses provided in the preceding paragraph are inapplicable.

AMENDMENTS TO §1.338(h)(10)-1T

Section 1.338(h)(10)-T is amended to provide rules for the adjustment of the selling consolidated group's basis in unacquired target stock when the MADSP formula election is made or revoked after disposition of the unacquired stock. The amendment provides that if such unacquired target stock has been disposed of before the adjustment to the basis of such stock is made, the adjustment shall be treated under principles of tax law applicable when part of the cost of an asset is paid after the asset has been disposed of.

COMMENTS REQUESTED

Comments are requested on the contingent payment, etc. rules of §1.338(b)-3T with a view toward simplifying the method of taking such payments, etc. into account and allocating them to target's assets. Such comments should address the concern that any simplified method should not distort the character of the gain (or loss) recognized by a taxpayer. For example, if the general rules of §1.338(b)-3T would treat a basis increase amount as a capital loss with respect to an acquisition date asset that had been disposed of, the simplified method should not transmute that capital loss into a reduction of ordinary income as might occur if the basis increase amount were merely allocated to other depreciable assets held by target when the adjustment event occurs.

Comments are also requested on the need for an adjustment to adjusted grossed-up basis when stock is purchased from minority shareholders after the acquisition date at an average price greater than the purchaser's average per share basis in recently purchased stock. If such adjustment is considered appropriate, commentators should recommend the appropriate mechanism for implementing such adjustment. In this regard, commentators should address the manner in which all other relevant adjustment (*e.g.*, depreciation) should be made.

The temporary regulations reject the specific lien rule by providing that liabilities to which an asset is subject are not specifically allocated to the asset. Comments are requested on under what circumstances, if any, it may be appropriate to follow the specific lien rule for purposes of allocating adjusted grossed-up basis.

REGULATORY FLEXIBILITY ACT; EXECUTIVE ORDER 12291

A general notice of proposed rulemaking is not required by 5 U.S.C. 553 for temporary regulations. Accordingly, these temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

DRAFTING INFORMATION

The principal authors of these temporary regulations are Bennett C. Steinhauer and Patricia Wendlandt of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly 26 CFR Part 1 is amended as follows:

PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Paragraph 1. The authority citation for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805; * * * §§1.338(b)-1T through 1.338(b)-3T, 1.338-1T, 1.338-4T, and 1.338(h)(10)-1T are also issued under 26 U.S.C. 338.

Par. 2. Section 1.338-1T is amended as follows:

1. The first sentence of paragraph (b)(8) is amended by inserting "for the taxable year ending at the close of the acquisition date" after "income tax return of old target."

2. Paragraph (f)(3)(i) is amended by inserting a new sentence at the end thereof, to read as set forth below.

3. Paragraph (f) is amended by adding a new subparagraph (9) at the end thereof, to read as set forth below.

§1.338-1T Elections under section 338(g) of the Internal Revenue Code of 1954 (temporary).

* * * * *

(f) *Certain consequences of section 338 election.* * * *

(3) *Old target's final taxable year otherwise included in consolitated return of selling group*—(i) *General rule.* * * * A "deemed sale return" includes a "combined return" as defined in §1.338-4T(k)(6).

* * * * *

(9) *Cross reference.* See §1.338(b)-3T(h) for certain rules relating to any change in the aggregate deemed sale price of old target's assets.

* * * * *

Par. 3. Paragraph (h) of §1.338-4T is amended as follows:

1. A new sentence is added at the end of paragraph (h)(1) to read as set forth below.

2. A new sentence is added at the end of paragraph (h)(2)(i) to read as set forth below.

3. The last two sentences of paragraph (h)(2)(iii) are revised to read as set forth below.

4. New subdivision (vi) is added at the end of paragraph (h)(2) to read as set forth below.

5. The last sentence of paragraph (h)(3) *Answer 1* (i) is removed and in its place two new sentences are added to read as set froth below.

6. The first two sentences of paragraph (h)(3) *Answer 2* (vi) are removed and in their place three new sentences are added to read as set forth below.

7. *Example (1)* (ii) in paragraph (h)(3) *Answer 2* (vi) is amended by removing the second sentence and by adding two new sentences at the end to read as set forth below.

8. In *Example (2)* in paragraph (h)(3) *Answer 2* (vi)—

a. The first word of the footnote is

removed and there is added in its place the words "For an item of section 1245 property, section".

b. Two new sentences are added at the end thereof to read as set forth below.

9. In *Example (3)* in paragraph (h)(3) *Answer 2* (vi)—

a. The first table is amended by removing the word "Goodwill" and adding in its place the word "Land".

b. Two new sentences are added immediately before the words "The following table breaks the ADSP of \$190,173 down". The new sentences read as set forth below.

10. New *Examples* (4) through (9) are added at the end of paragraph (h)(3) *Answer 2* (vi) to read as set forth below.

11. Paragraph (j)(1) is amended by adding after the second sentence a new sentence to read as set forth below.

12. A new sentence is added at the end of paragraph (j)(2) *Answer 6* to read as set forth below.

§1.338-4T Questions and answers relating to miscellaneous issues under 338 (temporary).

* * * * *

(h) *Determination of section 338(a)(1) deemed sale price*—(1) *Introduction.* * * * See §1.338(b)-3T(h) and (j) for certain rules and examples relating to any change in the aggregate deemed sale price of old target's assets.

(2) *Definitions*—(i) *ADSP.* * * * In the absence of a subscript, "ADSP" refers to ADSP for Class III assets only. See §1.338(b)-2T(b).

* * * * *

(iii) *Allocable ADSP amount.* * * * Except as provided in section 7701(g) (relating to fair market value in the case of nonrecourse indebtedness), the ADSP is allocated among T assets for this purpose in accordance with the rules of §1.338(b)-2T (without regard to §1.338(b)-2T(c)(2)). Recapture gain on a T asset under the elective ADSP formula is computed by reference to the allocable ADSP amount for that asset.

* * * * *

(vi) *Classes of assets.* The four classes of assets are defined in §1.338(b)-2T(b). Examples of each class are: Class I, cash; Class II, marketable securities; Class III, assets other than Classes I, II, and IV; and Class IV, goodwill and going concern value.

(3) *Determination of ADSP.*

Question 1: * * *

Answer 1: (i) *General rule.* * * * Except as provided in section 7701(g) (relating to fair market value in the case of nonrecourse indebtedness), for assets other than Class IV assets (*i.e.*, goodwill and going concern value), the same fair market values shall be used for purposes of this paragraph (h) (old T's aggregate deemed sale price) and for purposes of §1.338(b)-2T(b) and (c)(1) or (c)(3) (allocating new T's adjusted grossed-up basis to its assets). If the elective ADSP formula is not used, a proper appraisal of Class IV assets will be considered evidence of their fair market value.

* * * * *

Question 2: * * *

Answer 2: * * *

(vi) *Sample elective ADSP formula.* the sample ADSP formula shown below takes into account the existence of recapture gain arising under sections 1245 and 338(c)(1). For illustrative purposes, *Examples (1)* through *(3)* of this subdivision (vi) assume that the target has only Class III assets (*e.g.*, property other than certain cash items, certain securities, and goodwill, etc.). for examples illustrating the effect on the elective ADSP formula of Class I, II, or IV assets, see *Examples (4)* through *(9)* of this subdivision (vi). * * *

Example (1). * * *

(ii) * * * Since the ADSP for T (\$88,616) does not exceed the fair market value of T's one asset (\$100,000), a Class III asset, its entire ADSP is allocated to that asset. See §1.338(b;-2T(c)(1) (relating to fair market value limitation).

Example (2). * * * Since the ADSP for T (\$89,127.12) does not exceed the fair market value of T's one asset (\$100,000), a Class III asset, its entire ADSP is allocated to that asset. See §1.338(b)-2T(c)(1) (relating to fair market value limitation).

Example (3). * * * Since the ADSP for T (\$190,172.76) does not exceed the sum of the fair market values of all of T's assets (\$215,000), and those assets are all Class III assets, its entire ADSP is allocated to those assets. See §1.338(b)-2T(c)(1) (relating to fair market value limitation). * * *

Example (4). Assume the same facts as in *Example (1)*, except that P purchases all of the stock of T for \$85,000 and that T has \$10,000 of cash, a Class I asset. The sample elective ADSP formula as applied to these facts is modified by referring to the amount of the Class I assets as "I". This modified formula is as follows:

ADSP = G − I + L + t_R × [(Lesser of R or ADSP) − B]

ADSP = (\$85,000/1) − \$10,000 + \$0 + .46 × [(Lesser of \$80,000 or ADSP) − \$50,400]

ADSP = \$75,000 + 0 + .46 × [(Lesser of \$80,000 or ADSP) − \$50,400]

The remainder of the calculation and result are the same as in *Example (1)*.

Example (5). Assume the same facts as in *Example (2)*, except that P purchases the 80 shares for \$68,000 and that T has \$10,000 of cash, a Class I asset. the elective ADSP formula used in *Example (4)* as applied to these facts is as follows:

ADSP = G − I + L + t_R × [(Lesser of R or ADSP) − B] + C × t_R × (ADSP − Cb)

ADSP = (\$68,000/.8) − \$10,000 + 0 + .46 × [(Lesser of \$80,000 or ADSP) − \$50,400] + .20 × .28 × [ADSP − (Lesser of \$80,000 or ADSP)]

ADSP = \$85,000 − \$10,000 + .46 × [(Lesser of \$80,000 or ADSP) − \$50,400] + .20 × .28 × [ADSP − (Lesser of \$80,000 or ADSP)]

ADSP = \$75,000 + .46 [(Lesser of \$80,000 or ADSP) − \$50,400] + .20 × .28 × [ADSP − (Leser of \$80,000 or ADSP)]

The remainder of the calculation and result are the same as in *Example (2)*.

Example (6). Assume the same facts as in *Example (5)*, except that T does not hold any cash. Assume further that T holds marketable securities, a Class II asset, it acquired 10 years ago having a fair market value of \$10,000 and a basis of \$4,000. The sample elective ADSP formula as applied to these facts is modified by referring to the fair market value of the Class II asset as "II" and the basis of that asset as "B_{II}." This modified formula for calculating the ADSP of the section 1245 property is as follows:

ADSP = G − II + L + t_R × [(Lesser of R or ADSP) − B] + C × t_R × [(ADSP − Cb) + (II − B_{II})]

ADSP = (\$68,000/.8 − \$10,000 + 0 + .46 × [(Lesser of \$80,000 or ADSP) − \$50,400] + .20 × .28 × [(ADSP − (Lesser of \$80,000 or ADSP)) + (\$10,000 − \$4,000)]

In this case, assume that for the item of section 1245 property, the recomputed basis is less than the allocable ADSP amount for that item. The elective ADSP formula computation, as applied to this assumption, is as follows:

ADSP = \$85,000 − \$10,000 + .46 × (\$80,000 − \$50,400) + .056 × [(ADSP − \$80,000) + (\$6,000)]

ADSP = \$75,000 + (.46 × 29,600) + .056ADSP − \$4,480 + \$336

ADSP = \$75,000 + \$13,616 + .056ADSP − \$4,480 + \$336

ADSP − .056ADSP = \$84,472

.0944ADSP/.944 = \$84,472/.944

ADSP = \$89,483.05

Since the ADSP for T's Class III asset (\$89,483.05) does not exceed its fair market value, its entire ADSP for its Class III assets is allocated to its one asset in the class. See §1.338(b)-2T(b) and (c)(1). The deemed selling price for the marketable securities (Class II assets) is their fair market value ($10,000).

Summary of calculation

1. Grossed-up basis of P's recently purchased T stock	$85,000.00
2. Less: Deemed selling price of Class II assets	10,000.00
3. Subtotal	75,000.00
4. Tax on section 1245 depreciation recapture gain	13,616.00
5. Tax on section 338(c)(1) gain on all property (531.05* + $336)	867.05
6. ADSP for Class III property (Sum of lines 3 + 4 + 5)	89,483.05

* .056 × ($89,483.05 − $80,000)

Example (7). Assume the same facts as in *Example (1)*, except that T has goodwill with an appraised value of $10,000. The result is the same as in *Example (1)* when the elective ADSP formula is used because the appraised value of goodwill is not taken into account under the formula, and, so long as the ADSP for T's Class III asset does not exceed its fair market value, goodwill does not arise under the formula.

Example (8). Assume the same facts as in *Example (7)*, except that P purchases all of the stock of T for $100,000 and the recomputed basis of the section 1245 property is $210,000. The elective ADSP formula as applied to these facts is as follows:

$$\text{ADSP} = G + L + t_R \times [(\text{Lesser of } R \text{ or ADSP}) - B]$$

$$\text{ADSP} = (\$100{,}000/1) + \$0 + .46 \times [(\text{Lesser of } \$210{,}000 \text{ or ADSP}) - \$50{,}400]$$

ADSP—Recomputed basis measurement:

$$\text{ADSP} = \$100{,}000 + .46 \times (\$210{,}000 - \$50{,}400)$$

$$\text{ADSP} = \$173{,}416$$

ADSP—ADSP measurement:

$$\text{ADSP} = \$100{,}000 + .46 \times (\text{ADSP} - \$50{,}400)$$

$$\text{ADSP} = \$100{,}000 + (.46 \times \text{ADSP}) - \$23{,}184$$

$$\text{ADSP} = \$76{,}816 + .46\ \text{ADSP}$$

$$\text{ADSP} - .46\ \text{ADSP} = \$76{,}816$$

$$.54\text{ADSP}/.54 = \$76{,}816/.54$$

$$\text{ADSP} = \$142{,}251.85$$

Accordingly, under the elective ADSP formula, as initially applied, the ADSP of T would be $142,251.85, *i.e.*, the ADSP measurement ($142,251.85) which is less than the recomputed basis measurement ($173,416). Since this ADSP for T ($142,251.85) exceeds the fair market value of T's Class III asset ($100,000), ADSP allocated to that asset is limited to the asset's fair market value under §1.338(b)-2T(c)(1). Thus, the elective ADSP formula must be applied to compute the ADSP for T's Class IV property (*e.g.*, goodwill). The sample ADSP formula is applied to this computation is modified by using III to refer to the fair market value of the Class III asset (*i.e.*, the section 1245 property) and ADSP$_{IV}$ to refer to the ADSP for the Class IV property. This modified formula is as follows:

$$\text{ADSP}_{IV} = G - III + L + t_R \times [(\text{Lesser of } R \text{ or } III) - B]$$

$$\text{ADSP}_{IV} = \$100{,}000 - \$100{,}000 + 0 + .46 \times (\text{Lesser of } \$210{,}000 \text{ or } \$100{,}000) - \$50{,}400]$$

$$\text{ADSP}_{IV} = .46 \times (\$100{,}000 - \$50{,}400)$$

$$\text{ADSP}_{IV} = \$22{,}816$$

Thus, the ADSP for the Class IV property is $22,816. Note that the appraised value of the goodwill is irrelevant.

Summary of calculation:

1. Grossed-up basis of P's recently purchased stock	$100,000
2. Less: Deemed selling price of Class III property	100,000
3. Subtotal	0
4. Tax on section 1245 recapture gain	22,816
5. ADSP for Class IV property	22,816

Example (9). Assume the same facts as in *Example (8)*, except that P purchases only 80 of the 100 outstanding shares of T's only class of stock for $96,000. Assume further that T's assets, all of which have been held for more than one year, are as follows:

Class		*Basis*	*Fair market value*
I	1. Cash	—	$10,000 *
II	2. Marketable security	$ 4,000	10,000
III	3. Section 1245 property (recomputed basis $210,000)	50,400	100,000
IV	4. Goodwill	3,000	15,000 **

*Amount

**Appraised value

The elective ADSP formula as applied to these facts is modified by referring to items for a class of property by using Roman subscripts. (Since there is only one asset in each class, subscripts as used in *Example (3)* are not necessary.) The modified formula is as follows:

$$\text{ADSP} = G - I - II + L + t_R \times [(\text{Lesser } R \text{ or ADSP}) - B_{III}] + C\ t_R \times [(\text{ADSP} - {}^{Cb}III) + (II - B_{II})]$$

$$\text{ADSP} = (\$96{,}000/.8) - \$10{,}000 - \$10{,}000 + 0 + .46 \times [(\text{Lesser } \$210{,}000 \text{ or ADSP}) - \$50{,}400] + .20 \times .28 \times [(\text{ADSP} - (\text{Lesser of } \$210{,}000 \text{ or ADSP})) + (\$10{,}000 - \$4{,}000)]$$

In this case, the allocable ADSP amount for the one Class III asset is less than its recomputed basis. The modified elective ADSP formula, based on these assumptions, is applied as follows:

$$\text{ADSP} = \$120{,}000 - \$20{,}000 + .46 \times (\text{ADSP} - \$50{,}400) + .20 \times .28 \times (\$10{,}000 - \$4{,}000)^{***}$$

*** Section 338(c)(1) gain does not exist in this case since the measure of section 1245 depreciation recapture is the ADSP measure. See the footnote in *Example (2)*.

$$\text{ADSP} = \$100{,}000 + .46\text{ADSP} - \$23{,}184 + .056 \times (\$6{,}000)$$

$$\text{ADSP} = \$100{,}000 + .46\text{ADSP} - \$23{,}184 + \$336$$

$$\text{ADSP} - .46\text{ADSP} = \$77{,}152$$

$$.54\text{ADSP}/.54 = \$77{,}152/.54$$

$$\text{ADSP} = \$142{,}874.07$$

Accordingly, under the modified elective ADSP formula, as initially applied, the ADSP of T would be $142,874.07, an amount that exceeds the fair market value of T's one Class III asset ($100,000). Thus, ADSP allocated to that asset cannot exceed $100,000 under §1.338(b)-2T (c)(1). It follows that the elective ADSP formula must be applied to compute the ADSP for T's Class IV property (*e.g.*, goodwill). The modified ADSP formula, as used initially in this example, is further modified in the manner shown in *Example (8)*. In this example, the application of this further modified formula assumes that the measure of section 1245 depreciation recapture is fair market value so that section 338(c)(1) gain cannot exist. (See the preceding footnote.) This further modified formula is as follows:

$$\text{ADSP}_{IV} = G - I - II - III + L + t_R \times (III - B_{III}) + C \times t_R \times [(II - B_{II}) + (\text{ADSP}_{IV} - B_{IV})]$$

$$\text{ADSP}_{IV} = \$120{,}000 - \$10{,}000 - \$10{,}000 - \$100{,}000 + 0 + .46 \times (\$100{,}000 - \$50{,}400) + .20 \times .28 \times [(\$10{,}000 - \$4{,}000) + (\text{ADSP}_{IV} - \$3{,}000)]$$

$$\text{ADSP}_{IV} = .46 \times \$49{,}600 + .056 \times (\$6{,}000 + \text{ADSP}_{IV} - \$3{,}000)$$

$$\text{ADSP}_{IV} = \$22{,}816 + \$336 + .056\text{ADSP}_{IV} - \$168$$

$$\text{ADSP}_{IV} - .056\text{ADSP}_{IV} = \$22{,}984$$

$$.944\text{ADSP}_{IV}/.944 = \$22{,}984/.944$$

$$\text{ADSP}_{IV} = \$24{,}347.46$$

Thus, the ADSP for the Class IV property is $24.357.46. Note that the appraised value for the goodwill is irrelevant.

Summary of calculation:

1. Grossed-up basis of P's recently purchased stock		$120,000.00
2. Less: deemed selling price of—		
a. Class I property	$10,000.00	
b. Class II property	10,000.00	
c. Class III property	100,000.00	
d. Total	120,000.00	
3. Subtotal		0
4. Tax and section 1245 recapture gain		22,816.00
5. Tax on section 338(c)(1) gain on—		
a. Class II property	336.00	
b. Class IV property	1,195.46*	
c. Total		1,531.46
6. ADSP for Class IV property (Sum of lines 3 + 4 + 5)		24,347.46

* .056 × ($24,347.46 − $3,000)

(j) ***Determination of basis of target assets after section 338 election***—(1) *Introduction.* * * * Rules relating to allocation of adjusted grossed-up basis among T's assets are provided in §§1.338(b)-2T and 1.338(b)-3T. * * *

(2) *Determination of adjusted grossed-up basis.*

* * * * *

Question 6.: * * *

Answer 6: * * * See also §1.338(b)-1T(d)(2).

Par. 4. §1.338(h)(10)-1T is amended by adding a new sentence at the end of paragraph (f)(4) and by adding a new paragraph (f)(5). The added provisions read as follows:

§1.338(h)(10)-1T Elective recognition by selling consolidated group of deemed sale gain or loss on target's assets (temporary).

* * * * *

(f) *Deemed sale price.* * * *

(4) *Procedure for electing MADSP formula and revoking that election.* * * * If such unacquired T stock has been disposed of before the adjustment to its basis is made, the members of the S group shall treat the adjustment under principles of tax law that apply when the purchase price of an asset is changed after the asset has been disposed of.

(5) *Cross-reference.* See §1.338 (b)-3T(h) for adjustments to the aggregate deemed sale price of old target's assets because of events occuring after the acquisition date.

* * * * *

Par. 5. There are added in the appropriate place the following new sections to read as follows:

§1.338(b)-1T Adjusted grossed-up basis (temporary).

(a) *Scope.* This section provides rules under section 338(b) to determine the adjusted grossed-up basis of a target for which a section 338 election is made. Adjusted grossed-up basis is allocated among the assets of target in accordance with §1.338(b)-2T to determine the price at which the assets of the target are deemed to have been purchased. Subsequent adjustments to grossed-up basis and the allocation of such adjustments to target's assets may be made under §1.338(b)-3T. This section does not apply to transactions to which section 224(d)(5) of the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462] (as added by section 306(a)(8)(B)(i) of the Technical Corrections Act of 1982) [Pub. L. 97-448, 1983-1 C.B. 451, 470] applies. For rules relating to such transactions, see §1.338-2T.

(b) *Nomenclature and definitions*—(1) *Nomenclature.* The nomenclature set out in §1.338-4T(b)(1) also applies to this section.

(2) *Definitions*—(i) *In general.* The definitions in section 338 and §§1.338-1T and 1.338-4T also apply to this section.

(ii) *Adjustment events.* "Adjustment events" are increases (or decreases) in the consideration paid for recently or nonrecently purchased stock, reductions in target's liabilities included in adjusted grossed-up basis as of the beginning of the day after the acquisition date, and old target liabilities that become fixed and determinable.

(c) *General rule*—(1) *Adjusted grossed-up basis.* "Adjusted grossed-up basis" is the sum of (i) the grossed-up basis of recently purchased stock (as defined in paragraph (d) of this section), (ii) the basis of nonrecently purchased stock (as defined in paragraph (e) of this section, (iii) the disabilities of target (as defined in paragraph (f) of this section, and (iv) other relevant items (as defined in paragraph (g) of this section).

(2) *time when adjusted grossed-up basis determined.* Adjusted grossed-up basis is initially determined at the beginning of the day after the acquisition date of target. However, adjustment events that occur during new target's first taxable year are taken into account for purposes of determining adjusted grossed-up basis and basis of target's assets as if they had occurred at the beginning of the day after the acquisition date.

(d) *Grossed-up basis of recently purchased stock*—(1) *In general.* The term "grossed-up basis of recently purchased stock" means the product of (i) the basis of the recently purchased stock at the beginning of the day after the acquisition date, multiplied by (ii) the fraction set forth in section 338(b)(4). For further detail, see §1.338-4T(j)(2) *Answer* 1 (ii).

(2) *Target subsidiary.* If a target (T) owns stock in an affected target (T1), the grossed-up basis of the recently purchased T1 stock is the product of—

(i) the basis of the T1 stock in the hands of T as of the beginning of the day after T's acquisition date, multiplied by

(ii) the fraction set forth in section 338(b)(4).

Thus, for example, if T is deemed to purchase 80 percent (by value) of T1's stock by reason of section 338(h)(3)(B), the grossed-up basis of recently purchased T1 stock is determined by multiplying 100/80 times the amount of adjusted grossed-up basis of T's stock allocated to T1's stock under §1.338(b)-2T. See also §1.338-4T(j)(2) *Answer* 6.

(e) *Basis of nonrecently purchased stock.* In the absence of an election under section 338(b)(3) ("gain recognition election"), the basis of nonrecently purchased stock is the historic basis in that stock. See §1.338-4T(j)(2) for rules relating to the gain recognition election.

(f) *Liabilities of target*—(1) *In general.* The liabilities of target include its liabilities (and the liabilities to which the target's assets are subject) as of the beginning of the day after the acquisition date (other than liabilities that were neither liabilities of old target nor liabilities to which old target's assets were subject). Unless an election is made under section 338(h)(10), liabilities of target also include income tax liabilities resulting from the deemed sale of its assets under section 338(a)(1).

(2) *Excluded obligations*—(i) *In general.* In order to be included in adjusted grossed-up basis at the beginning of the day after the acquisition date, an obligation must be a bona fide liability of target as of that date which is properly includible in basis under principles of tax law that would apply if new target had acquired old target's assets from an unrelated person and, as part of the transaction, had assumed or taken property subject to the obligation. Thus, for example, if, as of the beginning of the day after the acquisition date, the amount of the contingent or speculative obligation of target is not properly includible in basis under the preceding sentence, the obligation is not initially included in adjusted grossed-up basis.

(ii) *Time when excluded obligations taken into account.* Obligations that, under this subparagraph (2), are initially excluded from adjusted grossed-up basis, shall be taken into account in redetermining adjusted grossed-up basis and the basis of target's assets under principles of tax law that would apply if new target had acquired old target's assets directly from an unrelated person and, as part of the transaction, had assumed or taken property subject to those obligations. For the application of these principles of tax law to certain contingent liabilities that are initially excluded from adjusted grossed-up basis under this subparagraph (2), see §1.338(b)-3T.

(3) *Liabilities taken into account in determining amount realized on subsequent disposition.* In determining the amount realized on a subsequent sale or other disposition of property deemed purchased by new target, the entire amount of any liability included in adjusted grossed-up basis is considered to be an amount taken into account in determining new target's basis in property which secures such liability for purposes of applying §1.1001-2(a). Thus, if a liability is included in adjusted grossed-up basis, §1.1001-2(a)(3) shall not prevent the amount of such liability from being treated as discharged within the meaning of §1.1001-2(a)(4) as a result of new target's sale or disposition of the property which secures such liability.

(g) *Other relevant items*—(1) *In general.* Adjusted grossed-up basis may be increased (or decreased) for "other relevant items." For this purpose, other relevant items may only arise from adjustment events that occur after the close of new target's first taxable year and adjustments under paragraph (g)(3) of this section. See §1.338(b)-3T (relating to the treatment of certain subsequent adjustments to adjusted grossed-up basis).

(2) *Flow-through of relevant item adjustment to target subsidiary.* If the amount of adjusted grossed-up basis of a target (T) allocated to the stock of an affected target (T1) is subsequently increased (or decreased) by reason of an other relevant item under this paragraph (g), the grossed-up basis of the T1 stock (and T1's adjusted grossed-up basis) is then also increased (or decreased) as if the increase (or decrease) in the basis of the stock was an adjustment to the purchase price deemed paid by T for such stock. The resulting increase (or decrease) in adjusted grossed-up basis of T1 is then allocated among T1's assets in accordance with §§1.338(b)-2T and 1.338(b)-3T.

(3) *Adjustments by the Internal Revenue Service*—(i) *In general.* In connection with the examination of a return, the District Director may increase (or decrease) adjusted grossed-up basis for items other than those described in paragraph (g)(1) and (2) of this section under the authority of section 338(b)(2) and allocate such amounts to target's assets under the authority of section 338(b)(5) so that adjusted grossed-up basis and the basis of target's assets properly reflect the cost of the purchasing corporation of its interest in target's assets. Such items may include distributions from target to the purchasing corporation, capital contributions from the purchasing corporation to target during the 12-month acquisition period, or acquisitions of target stock by purchasing corporation after the acquisition date from minority shareholders at an average price lower than the average cost of recently purchased stock. In determining whether an adjustment is appropriate when stock is purchased after the acquisition date from minority shareholders at a price lower than the cost of recently purchased stock, the District Director will take into account all the facts and circumstances of the particular case. Relevant facts and circumstances may include the amount of the price differential and the reason therefor, the number of shares purchased after the acquisition date, the timing of the purchase, and the source of the additional shares.

(ii) *Examples.* The principles of this subparagraph (3) may be illustrated by the following examples:

Example (1). (i) On January 1, 1988, P purchases one-third of the sole class of outstanding stock of T for $300,000. T has no liabilities. On March 1, 1988, T distributes a dividend to all its shareholders consisting of property with a fair market value of $210,000 of which P receives $70,000. On April 15, 1988, P purchases the remaining T stock for $480,000 and makes an express election for T.

(ii) In appropriate circumstances, the District Director may decrease the adjusted grossed-up basis ("AGUB") of T by $59,500 (the nontaxed portion of the dividend, as defined in section 1059 (b)) in order to properly reflect the cost of P of its interest in T's assets which P is deemed to have purchased.

Example (2). (i) T's sole asset is a building worth $100,000. It has no liabilities. T has 100 shares of a single class of stock outstanding. On August 1, 1988, P purchases 10 shares of T stock for $8,000. On June 1, 1989, P purchases 50 shares of T stock for $50,000. On June 14, 1989, P contributes a tract of land to the capital of T and receives 10 additional shares of T stock as a result of the contribution. Both the basis and fair market value of the land at that time are $10,800. On June 30, 1989, P purchases the remaining 40 shares of T stock for $40,000 and makes an express election for T.

(ii) In order to prevent the shifting of basis from the contributed property to other assets of T, the District Director may specifically allocate part of T's AGUB to the contributed property as shown in subdivisions (iii) and (iv) of this example.

(iii) The AGUB of T is $108,800.

(iv) $10,800 of the AGUB is allocated to the land, leaving $98,000 to be allocated among T's other assets, here, only the building.

§1.338(b)-2T Allocation of adjusted grossed-up basis among target assets (temporary).

(a) *Introduction*—(1) *In general.* This section prescribes rules under section 338(b)(5) for allocating adjusted grossed-up basis among the assets of a target for which a section 338 election is made.

(2) *Nomenclature and definitions*—(i) *In general.* The nomenclature set out in §1.338-4T(b)(1) also applies to this section. The definitions in section 338 and §§1.338-1T, 1.338-4T, and 1.338(b)-1T also apply to this section.

(ii) *Fair market value.* The "fair market value" of an asset is the gross fair market value of that asset (*i.e.*, fair market value determined without regard to mortgages, liens, pledges, or other liabilities).

(b) *General rule for allocating adjusted grossed-up basis*—(1) *Cash and other items designated by the Internal Revenue Service.* Adjusted grossed-up basis is first reduced by the amount of Class I assets. Class I assets are cash, demand deposits and similar accounts in banks, savings and loan associations (and other similar depository institutions), and other items designated in the Internal Revenue Bulletin by the Internal Revenue Service

(2) *Other assets*—(i) *In general.* Subject to the limitations and other special rules of paragraph (c) of this section, adjusted grossed-up basis (as reduced by Class I assets) is allocated among Class II assets of target held at the beginning of the day after the acquisition date in proportion to their fair market values at such time, then among Class III assets so held in such proportion, and finally to Class IV assets so held in such proportion.

(ii) *Class II assets.* Class II assets are certificates of deposit, U.S. Government securities, readily marketable stock or securities (within the meaning of §1.351-1(c)(3)), foreign currency, and other items designated in the Internal Revenue Bulletin by the Internal Revenue Service.

(iii) *Class III assets.* Class III assets are all assets of target (other than Class I, II, and IV assets), both tangible and intangible (whether or not depreciable, depletable, or amortizable).

(iv) *Class IV assets.* Class IV assets are intangible assets in the nature of goodwill and going concern value.

(c) *Certain limitations and special rules for basis allocable to an asset*—(1) *Basis not to exceed fair market value.* The amount of adjusted grossed-up basis allocated to an asset (other than Class IV assets) shall not exceed the fair market value of that asset at the beginning of the day after the acquisition date. In assigning fair market values to Class II or III assets for purposes of this paragraph (c), the fact that the target has assets in the nature of goodwill or going concern value (Class IV assets) must be taken into account. For modification of this fair market value limitation with respect to certain contingent income assets, see §1.338(b)-3T(g).

(2) *Assets subject to other limitations.* The amount of adjusted grossed-up basis allocated to an asset shall be subject to the limitations under the provisions of the Internal Revenue Code or principles of tax law in the same manner as if such asset were acquired from an unrelated person in a sale or exchange. For example, if the deemed sale (and purchase) of assets is a transaction described in section 1056 (a) (relating to basis limitation for player contracts transferred in connection with the sale of a franchise), the amount of adjusted grossed-up basis allocated to a contract for the services of an athlete shall not exceed the limitation imposed by that section. For another example, see §1.338(b)-1T(f)(2), relating to excluded obigations.

(3) *Special rule for allocating adjusted grossed-up basis when purchasing corporation has nonrecently purchased stock*—(i) *Scope.* This paragraph (c)(3) applies if at the beginning of the day after the acquisition date (A) the purchasing corporation holds nonrecently purchased stock for which a gain recognition election under section 338(b)(3) and §1.338-4T(j)(2) is not made and (B) the hypothetical purchase price determined under paragraph (c)(3)(ii) of this section excceeds the adjusted grossed-up basis determined under §1.338(b)-1T(c)(1). The determinations required under the preceding sentence shall be made without regard to adjustment events occurring after the close of new target's first taxable year.

(ii) *Determination of hypothetical purchase price.* Hypothetical purchase price is the sum of the grossed-up basis of recently purchased stock as determined under §1.338-4T(h)(3) *Answer* 2 (ii) and liabilities of target.

(iii) *Allocation of adjusted grossed-up basis.* Subject to the limitations in paragraph (c)(1) and (2) of this section, adjusted grossed-up basis (after reduction by the amount of Class I assets) is allocated among Class II, III, and IV assets of target held at the beginning of the day after the acquisition date in proportion to their fair market values at such time. For this purpose, the fair market value of Class IV assets is deemed to be the excess, if any, of the hypothetical purchase price over the sum of (A) the amount of the Class I assets and (B) the fair market values of Class II and III assets.

(d) *Examples.* The provisions of this section and §1.338(b)-1T may be illustrated by the following examples:

Example (1). (i) T owns 90% of the only class of outstanding stock of T1. P purchases 100% of the only class of outstanding stock of T for $2,000 and makes an express election for T. The express election for T causes a deemed election for T1 under section 338(f)(1). The grossed-up basis of the T stock is $2,000 *i.e.*, $2,000 × 1/1.

(ii) Assume that the liabilities of T as of the beginning of the day after the acquisition date (including income tax liabilities arising on the deemed sale of its assets) are as follows:

Liabilities (nonrecourse mortgage plus unsecured liabilities)	$ 700
Taxes payable	300
Total	1,000

(iii) The adjusted grossed-up basis ("AGUB") of T is determined as follows:

Grossed-up basis	$2,000
Total liabilities	1,000
AGUB	3,000

(iv) Assume that, at the beginning of the day after the acquisition date, T's cash and the fair market values of T's Class II and III assets are as follows:

Asset Class	*Asset*	*Fair market value*
I	Cash	$ 200*
II	Portfolio of marketable securities	300
III	Inventory	300
III	Accounts receivable	600
III	Building	800
III	Land	200
III	Investment in T1	450
	Total	2,850

*Amount

(v) Under paragraph (b)(2) of this section the amount of AGUB allocable to T's Class II and III assets is reduced by the amount of cash to $2,800, *i.e.*, $3,000-$200. $300 of AGUB is then allocated to marketable securities. Since the remaining amount of AGUB is $2,500 (*i.e.*, $3,000-($200 + $300)), an amount which exceeds the sum of the fair market values of T's Class III assets, the amount allocated to each Class III asset is its fair market value:

Inventory	$ 300
Accounts receivable	600
Building	800
Land	200
Investment in T1	450
Total	2,350

(vi) The amount allocated to T's Class IV assets (assets in the nature of goodwill and going concern value) is $150, *i.e.*, $2,500-$2,350.

(vii) The grossed-up basis of the T1 stock is $500, *i.e.*, $450 × 1/.9.

(viii) Assume that the liabilities of T1 as of the beginning of the day after the acquisition date (including income tax liabilities arising on the deemed sale of its assets) are as follows:

General liabilities	$100
Taxes payable	20
Total	120

(ix) The AGUB of T1 is determined as follows:

Grossed-up basis of T1 stock	$500
Liabilities	120
AGUB	620

(x) Assume that at the beginning of the day after the acquisition date, T1's cash and the fair market values of its Class III assets are as follows:

Asset class	*Asset*	*Fair market value*
I	Cash	$ 50*
III	Patent	350
III	Equipment	200

*Amount

(xi) The amount of AGUB allocable to T1's Class III assets is first reduced by the $50 of cash.

(xii) Since the remaining amount of AGUB ($570) is an amount which exceeds the sum of the fair market values of T1's Class III assets, the amount allocated to each Class III asset is its fair market value:

Patent	$350
Equipment	200
Total	500

(xiii) The amount allocated to T1's Class IV assets (assets in the nature of goodwill and going concern value) is $20, *i.e.*, $570-$550.

Example (2). (i) Assume that the facts are the same as in *Example (1)* except that P has, for five years, owned 20% of T's stock, which has a basis in P's hands at the beginning of the day after the acquisition date of $100, and P purchases the remaining 80% of T's stock for $1,600. P does not make a gain recognition election under section 338(b)(3).

(ii) Under paragraph (d) of §1.338(b)-1T, the grossed-up basis of recently purchased T stock is $1,600, *i.e.*, $1,600 × (1 − .2)/.8.

(iii) The AGUB of T is determined as follows:

Grossed-up basis of recently purchased stock	$1,600

Basic of nonrecently purchased stock	100
Liabilities	1,000
AGUB	2,700

(iv) Since P holds nonrecently purchased stock, the hypothetical purchase price of the T stock must be computed and is determined as follows:

Gross-up basis of recently purchased stock as determined under §1.338-4T(h) ($1,600/.8)	$2,000
Liabilities	1,000
Total	3,000

(v) Since the hypothetical purchase price ($3,000) exceeds the AGUB (and no gain recognition election is made under section 338(b)(3)), AGUB is allocated under paragraph (c)(3) of this section.

(vi) The amount of AGUB ($2,700) available to allocate to T's assets is reduced by the amount of cash to $2,500, *i.e.*, $2,700-$200. This $2,500 balance is then allocated among the Class II, III, and IV assets in proportion to, and not in excess of, their fair market values.

(vii) Under paragraph (c)(3) of this section, the fair market value of Class IV assets is deemed to be $150, *i.e.*, the $3,000 hypothetical purchase price minus $2,850 (the sum of T's cash, $200, and the fair market values of its Class II and III assets, $2,650). The allocation is as follows:

Portfolio of marketable securities	$ 268*
Inventory	268
Accounts receivable	536
Building	714
Land	178
Investment in T1	402
Goodwill (and going concern value)	134
Total	2,500

*All numbers rounded for convenience.

(viii) If the AGUB of T is increased (or decreased) as a result of a subsequent adjustment, the hypothetical purchase price and the deemed fair market value of the Class IV assets shall be redetermined and the increase (or decrease) in AGUB shall be allocated among T's acquisition date assets pursuant to §1.338(b)-3T(f). The increase (or decrease) in AGUB is allocated pursuant to §1.338(b)-3T(f) even if the hypothetical purchase price, as redetermined, no longer exceeds AGUB, as redetermined.

§1.338(b)-3T Subsequent adjustments to adjusted grossed-up basis (temporary).

(a) *Scope*—(1) *In general.* This section provides rules for redetermining adjusted grossed-up basis to account for adjustment events that occur after the close of new target's first taxable year. These adjustments must be made upon the payment of contingent amounts for recently or nonrecently purchased stock, the change in a contingent liability of old target to one which is fixed and determinable, reductions in the amounts paid for recently or nonrecently purchased stock, and reductions in liabilities of target (and the liabilities to which its assets are subject) that were taken into account in determining adjusted grossed-up basis. Adjusted grossed-up basis is redetermined under this section only if such an adjustment would be required, under general principles of tax law, in connection with an actual asset purchase by new target from an unrelated person. This section also provides rules for the allocation of such adjustments subsequent to the close of new target's first taxable year. For the treatment of adjustments prior to the close of new target's first taxable year, see §§1.338(b)-1T and 1.338(b)-2T.

(2) *Exceptions to applicability of section.* This section does not apply to a reduction in indebtedness that is (1) includible in gross income as discharge of indebtedness income (or would be includible but for section 108(a)), (2) due to a contribution to capital, (3) payment of a liability, or (4) the discharge of a liability within the meaning of §1.1001-2.

(3) *Adjustment of aggregate deemed sale price.* See paragraph (h) of this section for certain rules relating to a change in the aggregate deemed sale price of target's assets.

(b) *Nomenclature and definitions*—(1) *Nomenclature.* The nomenclature set out in §1.338-4T(b)(1) also applies to this section.

(2) *Definitions*—(i) *In general.* The defintions in section 338 and §§1.338-1T, 1.338-4T, 1.338(b)-1T, and 1.338(b)-2T also apply to this section.

(ii) *Contingent liability.* A contingent liability is a liability of target at the beginning of the day after the acquisition date that is not fixed and determinable by the close of new target's first taxable year.

(iii) *Contingent amount.* The term "contingent amount" means the amount of the consideration to be paid for recently or nonrecently purchased stock that is not fixed and determinable by the close of new target's first taxable year, plus contingent liabilities of target.

(iv) *Reduction amount.* The term "reduction amount" means a reduction after the close of new target's first taxable year in either (A) the consideration paid for recently or nonrecently purchased stock, or (B) a liability of target (or a liability to which one or more of its assets are subject) that has been taken into account in determining adjusted grossed-up basis.

(v) *Acquisition date asset.* The term "acquisition date asset" means any asset held by new target at the beginning of the day after the acquisition date (other than Class I assets).

(c) *General rule*—(1) *Time when increases in adjusted grossed-up basis taken into account.* A contingent amount that is taken into account for purposes of calculating adjusted grossed-up basis and the bases of assets of target is taken into account at the time at which such amount becomes fixed and determinable.

(2) *Time when decreases in adjusted grossed-up basis taken into account.* A reduction amount is taken into account for purposes of calculating adjusted grossed-up basis and the bases of assets of target when the reduction in the consideration paid or the reduction of the liability occurs.

(3) *Amount of increases and decreases in adjusted grossed-up basis.* The amount of an increase (or decrease) in adjusted grossed-up basis described in paragraph (c)(1) or (2) of this section is the difference between (i) adjusted grossed-up basis immediately before the increase (or decrease) and (ii) adjusted grossed-up basis recomputed by taking into account the increase (or decrease). For example, if an additional amount is paid for recently purchased stock of target, grossed-up basis of recently purchased stock and adjusted grossed-up basis are recomputed by applying the fraction in section 338(b)(4) to the basis of the recently purchased stock at the beginning of the day after the acquisition date, adjusted for additional amounts paid. Any other adjustments required by a change in grossed-up basis would also be taken into account in making the recomputation, such as a change in the basis of nonrecently purchased stock under section 338(b)(3) and, if there has not been a section 338(h)(10) election, any additional income tax liabilities of target resulting from the additional payment.

(d) *Allocation of increases in adjusted grossed-up basis*—(1) *In general.* An increase in adjusted grossed-up basis (as determined under paragraph (c)(3) of this section) is allocating among target's acquisition date assets under §1.338(b)-2T.

Amounts allocable to an acquisition date asset (or with respect to a disposed-of acquisition date asset) are subject to the fair market value limitation and other limitations in §1.338(b)-2T(c)(1) and (2). Except as provided in paragraph (g) of this section, for the purpose of applying §1.338(b)-2T(c)(1) and (2), the fair market value is determined at the beginning of the day after the acquisition date. If adjusted grossed-up basis was allocated among target's assets pursuant to §1.338(b)-2T(c)(3), an increase in adjusted grossed-up basis (as determined under paragraph (c)(3) of this section) is accounted for in accordance with the rules of paragraph (f) of this section.

(2) *Effect of disposition or depreciation of acquisition date assets.* If an acquisition date asset has been disposed of, depreciated, amortized or depleted by new target before a contingent amount is taken into account in redetermining adjusted grossed-up basis, the contingent amount otherwise allocable to such asset is treated under principles of tax law applicable when part of the cost of an asset (not previously reflected in its basis) is paid after the asset has been disposed of, depreciated, amortized or depleted.

(e) *Allocation of decreases in adjusted grossed-up basis*—(1) *In general.* If adjusted grossed-up basis was allocated in accordance with the rules of §1.338(b)-2T(b)(2), a decrease in adjusted grossed-up basis (as determined under paragraph (c)(3) of this section) is allocated in the following order: (i) first as a reduction in the bases of target's Class IV acquisition date assets, (ii) second, as a reduction of the bases of target's Class III acquisition date assets in proportion to their fair market values at the beginning of the day after the acquisition date, and (iii) finally, as a reduction of the bases of target's acquisition date assets that are Class II assets in proportion to their fair market values at the beginning of the day after the acquisition date. The decrease in adjusted grossed-up basis allocated to an asset shall not exceed the adjusted grossed-up basis of target previously allocated to that asset. If adjusted grossed-up basis was allocated among target's assets pursuant to §1.338(b)-2T(c)(3), a decrease in adjusted grossed-up basis (as determined under paragraph (c)(3) of this section) is accounted for in accordance with the rules of paragraph (f) of this section.

(2) *Effect of disposition of assets or reduction of basis below zero.* If an acquisition date asset has been disposed of, depreciated, amortized, or depleted by new target before a reduction amount is taken into account in adjusted grossed-up basis, the decrease in adjusted grossed-up basis attributable to such reduction amount otherwise allocable to such asset is treated under principles of tax law applicable when the cost of an asset (previously reflected in its basis) is reduced after the asset has been disposed of or depreciated, amortized, or depleted. For purposes of this subparagraph (2), an asset is considered to have been disposed of to the extent that its allocable portion of the decrease in adjusted grossed-up basis would reduce its basis below zero.

(3) *Section 38 property.* Section 1.47-2(c) applies to a reduction in basis of section 38 property under this section.

(f) *Special rule for allocation of increases (or decreases) in adjusted grossed-up basis when hypothetical purchase price was used in allocating adjusted grossed-up basis.* (1) *Scope.* This paragraph (f) applies if (i) adjusted grossed-up basis was allocated among new target's Class II, III, and IV assets in accordance with §1.338(b)-2T(c)(3) and (ii) an adjustment event occurs after the close of new target's first taxable year.

(2) *Allocation of increases (decreases) in adjusted grossed-up basis.* If an adjustment event after the close of new target's first taxable year increases (or decreases) adjusted grossed-up basis, the following items shall be redetermined, taking into account such adjustment event: (i) the hypothetical purchase price, (ii) the deemed fair market value of Class IV assets, and (iii) the adjusted grossed-up basis allocable to each acquisition date asset under §1.338(b)-2T(c)(3) (the redetermined (c)(3) amount). (The redetermination of the deemed fair market value of Class IV assets under this subparagraph (2) is made by taking into account the target's Class I assets and the fair market values of its Class II and III assets at the beginning of the day after the acquisition date.) If the redetermined (c)(3) amount for an acquisition date asset exceeds the amount of adjusted grossed-up basis previously allocated to such asset (taking into account prior adjustments under this paragraph (f)), an amount of adjusted grossed-up basis equal to such excess shall be allocated to such asset. If the amount of adjusted grossed-up basis previously allocated to an acquisition date asset (taking into account prior adjustments under this paragraph (f)) exceeds the redetermined (c)(3) amount for that asset, an amount equal to such excess shall be allocated as a reduction in the basis of such asset. The rules of paragraph (d)(2) (or (e)(2)) apply for the treatment of amounts allocable under this paragraph (f) to an acquisition date asset that has been disposed of, depreciated, amortized, or depleted.

(3) *Allocation to contingent income assets.* For modification of this rule with respect to certain assets, see paragraph (g) of this section.

(g) *Special rule for allocation of increases (or decreases) in adjusted gross-up basis to specific assets*—(1) *Patents and similar property*—(i) *Scope.* The rules of this paragraph (g)(1) apply for purposes of allocating an increase (or decrease) in adjusted grossed-up basis to the extent (A) the contingency that results in the increase (or decrease) directly relates to income produced by a particular intangible asset ("contingent income asset"), such as a patent, a secret process, or a copyright, and (B) the increase (or decrease) is related to such contingent income asset and not to other target assets. Adjusted grossed-up basis, as determined under §1.338(b)-1T at the beginning of the day after the acquisition date, and any increase (or decrease) to adjusted grossed-up basis to which this paragraph (g) does not apply, are allocated among target's acquisition date assets (including contingent income assets) in accordance with the provisions of §1.338(b)-2T and paragraph (d), (e), or (f) of this section.

(ii) *Specific allocation.* Subject to the fair market value limitation and other limitations in §1.338(b)-2T(c)(1) and (2), any increase (or decrease) to adjusted grossed-up basis to which this paragraph (f) applies is allocated (A) first, specifically to the contingent income asset to which the increase (or decrease) relates and, then, (B) in accordance with the provisions of paragraph (d), (e), or (f) of this section. Solely for purposes of applying the fair market value limitation and other limitations of §1.338(b)-2T(c)(1) and (2) to a contingent income asset, the fair market value of such asset may be redetermined as of the time when the contingent amount (or reduction amount) is taken into account under paragraph (c) of this section. However, the fair market value limitation and other limitations of §1.338(b)-2T(c)(1) and (2) as they apply to target's other acquisition date assets are not affected by such adjustments.

(2) *Internal Revenue Service authority.* In connection with the examination of a return, the District Director, in appropriate cases, may apply the principles of paragraph (g)(1) of this section to allocate an increase (or decrease) in adjusted grossed-up basis among particular of target's acquisition date assets to the extent such allocation is necessary to reflect properly the consideration that relates to each of those assets.

(h) *Changes in old target's aggregate deemed sale price of assets*—(1) *General rule*—(i) *In general.* Pursuant to general principles of tax law, the price at which old target is deemed to have sold its assets shall be adjusted to take into account adjustment events occurring after the acquisition date. In making such an adjustment, recognition of income (or loss) under this paragraph (h) with respect to the deemed sale of assets is not precluded because the target is treated as a new corporation after the acquisition date. To the extent general tax law principles require seller to account for adjustment events, target (or a member of the selling consolidated group in the event of an election under section 338(h)(10)) shall make such an accounting, which may result in reporting income, loss, or other amount.

(ii) *Redetermination of aggregate deemed sale price if the elective formula under section 338(h)(11) is used.* If the elective formula under section 338(h)(11) is used to determine the aggregate deemed sale price, that price generally shall be redetermined under §1.338-4T(h) (or §1.338(h) (10)-1T(f)(2) if an election under section 338(h)(10) is in effect) to take into account, to the extent required by general principles of tax law, adjustment events occurring after the acquisition date. For example, the aggregate deemed sale price generally shall be redetermined to take into account any additional payments made to the seller for recently purchased stock. If an increase (or decrease) in adjusted grossed-up basis is specifically allocated to a contingent income asset (or other asset) under paragraph (g) of this section, then any redetermination of the fair market value of the asset under that paragraph (g) is taken into account in making adjustments to the aggregate deemed sale price allocable to such asset.

(iii) *Redetermination of aggregate deemed sale price if the elective formula under section 338(h)(11) is not used.* If the elective formula under section 338(h)(11) is not used to determine the aggregate deemed sale price, an adjustment to aggregate deemed sale price may be required under this paragraph (h) only with respect to assets described in paragraph (g)(1)(i) and (2) of this section. In such a case, the adjustment to the portion of the aggregate deemed sale price allocable to such asset shall be the amount of the increase (or decrease) in adjusted grossed-up basis specifically allocated to the asset. However, the amount of the increase (or decrease) allocated to such asset shall not increase (or decrease) the portion of the aggregate deemed sale price allocable to the asset (taking into account all previous adjustments under this paragraph (h)) above or below the fair market value of such asset as of the date an adjustment under this paragraph (h) is required.

(2) *Procedure for transactions in which section 338(h)(10) is not elected*—(i) *Income or loss included in new target's return.* If an election under section 338(h)(10) is not made, any income loss, or other amount of old target resulting from a change in the aggregate deemed sale price of old target's assets pursuant to paragraph (h)(1) of this section shall be included in new target's income tax return for new target's taxable year in which such change occurs. The amount of such income, loss, or other amount is determined with reference to old target's deemed sale of assets on the acquisition date. Thus, for example, if after the acquisition date there is an increase in the allocable aggregate deemed sale price of section 1245 property for which the recomputed basis (but not the adjusted basis) exceeded the portion of the aggregate deemed sale price allocable to that particular asset on the acquisition date, the additional gain shall be treated as ordinary income to the extent it does not exceed such excess amount. See paragraph (h)(2)(ii) for the special treatment of old target's carryovers and carrybacks. Although included in new target's income tax return, such income, loss, or other amount is separately accounted for as an item of old target and may not be offset by income, loss, credit, or other amount of new target. The amount of tax on income of old target recognized pursuant to this paragraph (h) is determined as if such income had been recognized in old target's taxable year ending at the close of the acquisition date. Any increase (or decrease) in new target's income tax liability by reason of this paragraph (h)(2)(i) shall be allocated among new target's acquisition date assets in accordance with paragraph (d), (e), (f), or (g) of this section when such liability becomes fixed and determinable.

(ii) *Carryovers and carrybacks*—(A) *Loss carryovers to new target taxable years.* A net operating loss or net capital loss of old target may be carried forward to a taxable year of new target, under the principles of section 172 or 1212, as the case may be, but is allowed as a deduction only to the extent of any recognized income of old target for such taxable year, as described in paragraph (h)(2)(i) of this section. For this purpose, however, taxable years of new target shall not be taken into account in applying the 15-taxable-year limitation (or other similar limitation) in section 172(b)(1) or the 5-taxable-year limitation (or other similar limitation) in section 1212(a)(1)(B). In applying section 172(b) and 1212(a)(1), only income, deductions, and other amounts of old target shall be taken into account. Thus, if old target has an unexpired net operating loss at the close of its taxable year in which the deemed asset sale occurred that could be carried forward to a subsequent taxable year, such loss may be carried forward until it is absorbed by old target's income.

(B) *Loss carrybacks to taxable years of old target.* An ordinary loss or capital loss accounted for as a separate item of old target under paragraph (h)(2)(i) of this section may be carried back to a taxable year of old target under the principles of section 172 or 1212, as the case may be. For this purpose, taxable years of new target shall not be taken into account in applying the 3-taxable-year limitation (or other similar limitation) in section 172(b) or 1212(a).

(C) *Credit carryovers and carrybacks*. The principles described in paragraph (h)(2)(ii)(A) and (B) of this section apply to carryovers and carrybacks of amounts for purposes of determining the amount of a credit allowable under part IV, subchapter A, chapter 1 of the Code. Thus, for example, credit carryovers of old target may only offset income tax attributable to items described in paragraph (h)(2)(i) of this section.

(3) *Procedure for transactions in which section 338(h)(10) is elected*—If an election under section 338(h)(10) is made, any income, loss, or other amount resulting from a change in the aggregate deemed sale price of old target's assets pursuant to paragraph (h)(1) of this section shall be accounted for in determining the taxable income (or other amount) of the member of the selling consolidated group (or other person) to which such income, loss, or other amount is attributable for the taxable year in which such change occurs. The amount of such income, loss, or other amount is determined with reference to old target's deemed sale of assets on the acquisition date.

(i) [Reserved.]

(j) *Examples*. This section is illustrated by the following examples. Any contingent amount or reduction amount described in the following examples is exclusive of interest. For rules characterizing deferred contingent payments as principal or interest, see regulations under section 1274 and 1275(d) or 483.

Example (1). (i) T's assets and their fair market values at the beginning of the day after the acquisition date are as follows:

Asset Class	*Assets*	*Fair market value*
III	Building	$100
III	Stock of X (not a target)	200
IV	Goodwill (and going concern value)	35
	Total	335

T has no liabilities other than a contingent obligation and T does not use the elective formula under section 338(h)(11).

(ii) On January 1, 1989, P purchases all of the outstanding stock of T for $270 and makes an express election for T. The grossed-up basis of the T stock and T's adjusted grossed-up basis ("AGUB") are both $270. The AGUB is ratably allocated among T's Class III assets in proportion to their fair market values as follows:

Asset	*Basis*
Building ($270 × 100/300)	$ 90
Stock ($270 × 200/300)	180
Total	270

No amount is allocated to the Class IV assets. New T is a calendar year taxpayer. Assume that the X stock is a capital asset in the hands of new T.

(iii) On January 1, 1990, new T sells the X stock and uses the proceeds of the sale to purchase inventory.

(iv) On June 30, 1991, the contingent liability of old T becomes fixed and determinable. The amount of the liability is $60.

(v) T's AGUB increases by $60 from $270 to $330. This $60 increase in AGUB is first allocated among T's acquisition date assets in accordance with the provisions of §1.338(b)-2T. Since the redetermined AGUB for T ($330) exceeds the sum of the fair market values at the beginning of the day after the acquisition date of the Class III acquisition date assets ($300), AGUB allocated to those assets is limited to those fair market values under §1.338(b)-2T(c)(1). The remaining AGUB of $30 is allocated to goodwill and going concern value (Class IV assets). The amount of increase in AGUB allocated to each acquisition date asset is determined as follows:

Asset	*Original AGUB*	*Redetermined AGUB*	*Increase in AGUB*
Building	$ 90	$100	$10
X stock	180	200	20
Goodwill and going concern value	0	30	30
Total	270	330	60

(vi) Since the X stock was disposed of before the contingent liability became fixed and determinable, no amount of the increase in AGUB attributable to such stock may be allocated to any T asset. Rather, such amount, $20, is allowed as a capital loss to T for the taxable year 1991 under the principles of *Arrowsmith v. Commissioner*, 344 U.S. 6 (1952). In addition, the $10 increase in AGUB allocated to the building is treated as a basis redetermination in 1991. See paragraph (d)(2) of this section.

Example (2). (i) On January 1, 1988, P purchases all of the outstanding stock of T and makes an express election for T. T does not use the elective formula under section 338(h)(11). Assume that the AGUB of T is $500 and is allocated among T's acquisition date assets as follows:

Asset Class	*Asset*	*Basis*
III	Machinery	$150
III	Land	250
IV	Goodwill and going concern value	100
	Total	$500

(ii) On June 1, 1994, P filed a claim against the selling shareholders of T in a court of appropriate jurisdiction alleging fraud in the sale of the T stock.

(iii) On January 1, 1995, the former shareholders refund part of the purchase price to P in a settlement of the 1994 lawsuit. This refund results in a decrease of T's AGUB of $140.

(iv) Under paragraph (e)(1) of this section, the decrease in AGUB is allocated among T's acquisition data assets. First, assuming the basis of the goodwill and going concern value on January 1, 1995, is still $100, then $100 of the decrease in AGUB is allocated to that asset. The remaining decrease in AGUB ($40) is allocated to the Class III assets in proportion to their fair market values at the beginning of the day after the acquisition date. Thus, $15 is allocated to the machinery ($40 × $150/$400) and $25 to the land ($40 × $250/$400).

(v) Assume that, as a result of deductions under section 168, the adjusted basis of the machinery immediately before the decrease in AGUB is zero. The machinery, therefore, is treated as if it were disposed of before the decrease is taken into account. T recognizes ordinary income of $15 for the taxable year 1995 under the principles of *Arrowsmith v. Commissioner*, 344 U.S. 6 (1952), and the tax benefit rule. No adjustment to the basis of T's assets is made for any tax paid on this amount.

(vi) In summary, the basis of T's acquisition date assets, as of January 1, 1995, is as follows:

Asset	*Basis*
Machinery	$ 0
Land	225
Goodwill and going concern value	0

Example (3). (i) Assume that the facts are the same as in *Example* (2) of §1.338(b)-2T(d) except that the recently purchased stock is acquired for $1,600 plus certain additional payments which are contingent upon T's future earnings. Thus, T's AGUB, determined as of the beginning of the day after the acquisition date (after reduction by T's cash of $200), is $2,500 and is allocated among T's Class II, III, and IV acquisition date assets pursuant to §1.338(b)-2T(c)(3)(iii) as follows:

Portfolio of marketable securities	$ 268*
Inventory	268
Accounts receivable	536
Building	714
Land	178
Investment in T1	402
Goodwill (and going concern value)	134
Total	2,500

*All numbers rounded for convenience.

(ii) Subsequent to the close of new target's first taxable year, P pays an additional $200 for its recently purchased T stock.

(iii) T's AGUB increases by $200, from $2,700 to $2,900. This $200 increase in AGUB is accounted for in accordance with the provisions of §1.338(b)-2T(c)(3)(iii) and paragraph (f) of this section.

(iv) The hypothetical purchase price of the T stock is redetermined as follows:

Grossed-up basis of recently purchased stock as determined under §1.338-4T(h) ($1,800/.8)	$2,250
Liabilities	1,000
Total	3,250

(v) Under §1.338(b)-2T(c)(3) the redetermined fair market value of Class IV assets is deemed to be $400, *i.e.*, the hypothetical purchase price, as redetermined, of $3,250 minus $2,850 (the sum of T's cash, $200, and the fair market values of its Class II and III assets, $2,650).

(vi) The amount of AGUB available to allocate to T's Class II, III, and IV acquisition date assets is $2,700 (*i.e.* redetermined AGUB reduced by cash). AGUB allocable to each of T's acquisition date assets (*i.e.*, the redetermined (c)(3) amount) is redetermined using the deemed fair market value of the Class IV asset from subdivision (v) as follows:

Portfolio of marketable securities	$ 266*
Inventory	266
Accounts receivable	531
Building	708
Land	177
Investment in T1	398
Goodwill (and going concern value)	354
Total	2,700

*All numbers rounded for convenience.

(vii) As illustrated by this example, the application of paragraph (f) of this section results in a basis increase for some assets and a basis decrease for other assets. The amount of increase (or decrease) in AGUB allocated to each acquisition date asset is determined as follows:

Asset	*Original AGUB*	*Redetermined (c)(3) amount*	*Increase (or Decrease in AGUB*
Portfolio of marketable securities	$268	$266	$(2)
Inventory	268	266	(2)
Accounts receivable	536	531	(5)
Building	714	708	(6)
Land	178	177	(1)
Investment T1	402	398	(4)
Goodwill (and going concern value)	134	354	220
Total	2,500	2,700	220

(viii) If P made a gain recognition election under section 338(b)(3) with respect to its nonrecently purchased stock, paragraph (f) of this section would be inapplicable.

Example (4). (i) On January 1, 1987, P purchases all of the outstanding T stock and makes an express election for T. The fair market value of T's assets (other than goodwill and going concern value) as of the beginning of the following day is as follows:

Asset class	*Assets*	*Fair market value*
III	Equipment	$200
III	Accounts receivable	100
III	Building	500
	Total	800

(ii) T has elected the elective ADSP formula, in accordance with §1.338-4T(h)(3) *Answer 2* (ii)(B), to determine the aggregate deemed sale price of old T's assets. Assume that the ADSP as so determined is $700. Assume also that the AGUB is equal to $700. T has no liabilities.

(iii) The AGUB of $700 is ratably allocated among T's Class III acquisition date assets in proportion to their fair market values as follows:

Asset	*Basis*
Equipment ($700 × 200/800)	$175.00
Accounts receivable ($700 × 100/800)	87.50
Building ($700 × 500/800)	437.50
Total	700.00

No amount is allocated to goodwill (or going concern value).

(iv) P and T file a consolidated return for 1987 and each following year with P as the common parent of the affiliated group.

(v) In 1990, a contingent amount of $117 is paid by P for the stock of old T. As a result, additional income is recognized under section 1245 by old T for 1990 on the deemed sale of old T's assets. This income must be reported on the consolidated return of new T for 1990, but it is separately accounted for and may not be absorbed by losses or deductions of P or of new T. Assume that the tax on this income is $3.

(vi) In 1990, there is an increase in T's AGUB of $120, *i.e.*, $117 + $3. The amount of this increase allocated to each acquisition date asset is determined as follows:

Assets	*Original AGUB*	*Redetermined AGUB*	*Increase*
Equipment	$175.00	$200.00	$25.00
Accounts receivable	87.50	100.00	12.50
Building	437.50	500.00	62.50
Goodwill (and going concern value)	0.00	20.00	20.00
Total	700.00	820.00	120.00

Example (5). (i) On June 1, 1990, P purchases all of the stock of T and makes an express election for T. T has one item of section 38 property whose basis on June 2, 1990 is $100,000. An investment credit of $8,000 is allowed to new T for the equipment because of an election under section 48(q)(4).

(ii) In 1992, part of the purchase price of the T stock is refunded to P. Assume that the amount of the resulting decrease in AGUB allocated to the machinery is $7,000. Pursuant to §1.47-2(c), the machinery ceases to be section 38 property to the extent of $7,000 of its original basis.

(iii) The additional tax of $560 (8% × $7,000) resulting from the machine ceasing to be section 38 property is reported on T's return for 1992. Such amount is not an adjustment to AGUB.

Example (6). (i) T has three assets (other than goodwill and going concern value) whose fair market values as of the beginning of the day after the acquisition date are as follows:

Asset Class	*Assets*	*Fair market value*
III	Building	$100
III	Equipment	50
III	Secret process	50
	Total	200

T has no liabilities. Assume that no election under section 338(h)(10) or (h)(11) is in effect.

(ii) On January 1, 1989, P purchases all of the outstanding T stock for $225 plus 50 percent of the net profits generated by the secret process for each of the next three years, determinable and payable on January 1 of each following year.

(iii) As of the beginning of January 2, 1989, T's AGUB is $225, allocated as follows:

Asset Class	*Assets*	*Basis*
III	Building	$100
III	Equipment	50
III	Secret Process	50
IV	Goodwill and going concern value	25
	Total	225

(iv) On January 1, 1990, $5 is paid by P for the T stock by reason of the net profits from the secret process. The payments are not attributable in any respect to any of T's other acquisition date assets. As a result, T's AGUB on January 1, 1990, is increased by $5.

(v) Assume that as of January 1, 1990, the fair market value of the secret process is determined to be $52.

(vi) On January 1, 1990, only $2 of the $5 increase in AGUB is allocated to the secret process because the increase in AGUB so allocated cannot increase the basis of the secret process above its redetermined fair market value ($52). The balance of the increase is allocated to goodwill and going concern value because the fair market value limitation of §1.338(b)-2T(c)(1) precludes allocating additional AGUB to the Class III assets.

(vii) The price for which old target is deemed to have sold the secret process is increased to reflect the $2 allocated to its basis to new carget. See §1.338-4T(h)(3) and paragraph (h)(1) of this section.

(viii) If the fair market value of the secret process as of January 1, 1990, is unchanged from its fair market value as of the beginning of the day after the acquisition date, then the $5 increase in AGUB is allocated to T's goodwill and going concern value.

Example (7). (i) The facts are the same as in *Example (6)* except that—

(A) The secret process is valued at $75 as of the beginning of the day after the acquisition date, and,

(B) P pays $250 for the T stock and the former T shareholders agree to refund a portion of the purchase price to P for each of the three years that the net income from the secret process is less than $15 per year, determinable and payable on January 1 of the next year.

(ii) Assume the net income from the process is less than $15 for 1989, and on January 1, 1990, P receives a refund that reduces the stock purchase price by $3.

(iii) Assume that as of January 1, 1990, the fair market value of the secret process is redetermined to be $65.

(iv) As of January 1, 1990, the AGUB of T is decreased by $3. This decrease is allocated to the secret process, whose basis becomes $72, (*i.e.*, $75-$3, assuming no adjustments thereto other than the decrease in AGUB).

(v) The price for which old target is deemed to have sold the secret process is decreased to reflect the $3 decrease allocated to its basis to new target. See §1.338-4T(h)(3) and paragraph (h) of this section.

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved January 18, 1986.

J. ROGER MENTZ,
Acting Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on January 23, 1986, 4:49 p.m., and published in the issue of the Federal Register for January 29, 1986, 51 F.R. 3583)

Section 381.—Carryovers in Certain Corporate Acquisitions

26 CFR 1.381(c)(4)-1: Method of accounting.

Treatment of reserves for certain guaranteed debt obligations. See T.D. 8071, page 4.

Section 2011.—Credit for State Death Taxes

26 CFR 20.2011-1: Credit for state death taxes.

State death tax paid in installments. When an estate elects to pay the federal estate tax in installments and also elects to pay state death taxes in annual installments over a period longer than four years from the date of the filing of the federal estate tax return, the exception described in section 2011(c)(2) of the Code is applicable. State death taxes paid by the estate more than four years after the filing of the federal estate tax return are not eligible for the credit described in section 2011 when none of the exceptions described in sections 2011(c)(1) through (3) are applicable.

Rev. Rul. 86-38

ISSUE

To what extent is a credit for state death tax allowable under section 2011 of the Internal Revenue Code if the state death tax is paid in installments over a period of more than four years where (1) the estate elects to pay the federal tax liability in ten annual installments, or (2) the estate does not elect to pay the federal estate tax liability in installments?

FACTS

A, a resident of State *S*, died in 1984 leaving a gross estate composed of stock of *X* Corporation and miscellaneous personal property. The value of *A*'s interest in *X* Corporation exceeded 35 percent of *A*'s adjusted gross estate. *A*'s interest in *X* qualified as an interest in a closely held business as defined in section 6166(b)(1) of the Code. The estate could, therefore, elect to pay in ten annual installments that portion of the federal estate tax attributable to the interest in a closely held business.

A similar provision under the law of *S* permited *A*'s estate to elect to pay in ten annual installments that portion of the state death tax attributable to an interest in a closely held business. Deferred payments and installment payments plus interest are required to be made under state law in the manner provided in section 6166 of the Code as in effect on *A*'s deate of death.

Situation 1.

In Situation 1, the representative of *A*'s estate made a timely election under section 6166 of the Code to pay part of the federal estate tax in ten equal annual installments and made a similar election under state law to pay part of the state death tax in ten annual installments. The representative of the estate timely paid in a single day the nondeferred portion of the federal estate tax, the first installment of the deferred estate tax, the nondeferred portion of the state death tax, and the first installment of the deferred state death tax. When the federal estate tax return was filed, the estate claimed as a credit under section 2011 of the Code the total amount of the state death tax liability, including the state death tax paid and the state death tax the estate expected to pay in installments over the next nine years.

Situation 2.

In Situation 2, the representative of the estate made a timely election under state law to pay part of the state death tax in ten annual installments. A similar election with respect to the federal estate tax was not made by the estate because the federal estate tax liability was substantially lower than the state death tax. Thus, the estate paid the federal estate tax in full.

When it filed the federal estate tax return, however, the estate claimed as a credit under section 2011 of the Code the total amount of the state death tax liability that the estate expected to pay.

LAW AND ANALYSIS

Section 6166(a)(1) of the Code provides that if the value of an interest in a closely held business that is included in determining the decedent's gross estate exceeds 35 percent of the adjusted gross estate, as defined in section 6166(b)(6), the executor may elect to pay part or all of the tax imposed by section 2001 in two or more (but not exceeding 10) equal installments.

Section 2011 of the Code provides that, within the limitations of section 2011(b), the tax imposed by section 2001 shall be credited with the amount of any estate, inheritance, legacy or succession taxes actually paid to any state.

Section 2011(c) generally provides that the credit allowed for state taxes described above shall include "only such taxes as were *actually* paid *and* credit therefor claimed within 4 years" after the filing of the estate tax return. (Emphasis added.)

Sections 2011(c)(1) through (3) contain exceptions to the four-year limitation on the period within which an estate may claim a credit for state taxes actually paid: (1) if a petition for redetermination of a deficiency has been filed with the Tax Court, before the expiration of 60 days after the decision of the Tax Court becomes final; (2) before the date of the expiration of the period of an extension granted under section 6161 or 6166 for payment of the tax shown on the return, or of a deficiency; or (3) if a claim for credit or refund of an overpayment of federal estate taxes has been filed within the time prescribed in section 6511 of the code, before the expiration of 60 days from the date of mailing by certified mail or registered mail by the Secretary to the taxpayer of a notice of the disallowance of any part of such claim, or before the expiration of 60 days after a decision by any court of competent jurisdiction becomes final with respect to a timely suit instituted upon such claim, whichever is later. According to section 2011(c), a refund based on the state death tax credit may (despite the provisions of sections 6511 and 6512) be made if the claim for the credit is filed within the prescribed period.

Section 6511(a) of the Code provides that a claim for credit or refund of an overpayment of any tax for which the taxpayer is required to file a return must be filed by the taxpayer within 3 years from the time the return was filed or 2 years from the time the tax was paid, whichever period expires later. The provisions of section 2011(c) provide a special 4-year period, or other extended period, as an alternative to the 2-year and 3-year periods described in section 6511(a) for credits and refunds.

In Rev. Proc. 81-27, 1981-2 C.B. 548, the Service set forth the procedure to be followed by an estate when installment payments due under section 6166 of the Code are recomputed because of a reduction in the estate tax liability caused by the deduction of interest paid on the estate tax due.

In Situation 1, the estate elected to pay the federal estate tax in ten annual installments. Accordingly, the exception described in section 2011(c)(2) is applicable, and the estate may qualify for the section 2011 credit for state death taxes paid for the period ending before the date of the expiration of the 10-year period elected for paying the federal estate tax. However, when the estate tax return is filed, only the state death taxes actually paid qualify for the section 2011 credit on the estate tax return. A recomputation procedure like the one described in Rev. Proc. 81-27 may be used to recompute the total remaining estate tax liability whenever the estate submits certification of payment of additional state death tax. The recomputation would take into account the section 2011 credit that may be allowed for any state death tax installment paid by the estate. After all state death taxes have been paid, a claim for refund may be made, if necessary, for an overpayment of tax but only after the federal estate tax liability has been paid in full.

In Situation 2, because the estate did not elect to extend the time to pay the federal estate tax, the extension of time within which to claim a refund based on the credit for state death taxes actually paid, described in section 2011(c)(2), is not applicable. Because none of the other extensions described in section 2011(c) apply, only installments *paid* to the state for death taxes within four years of the filing of the estate tax return can qualify for the credit described in section 2011 of the Code. Accordingly, when the estate files the estate tax return, only the state death taxes paid as of that time may be taken into account for a credit under section 2011. Certification of additional payments or installments made relating to the state death taxes during the four year period may be submitted for recomputation of the federal estate tax liability. A subsequent claim for a refund upon payment of each state installment may be made within the four-year period.

Any death tax installments paid to State *S* in Situation 2 after expiration of the four-year period described in section 2011(c) of the Code cannot be allowed as a credit against the federal estate tax liability of the estate. Because the tax was paid when the federal estate tax return was filed and none of the exceptions described in section 2011(c) are applicable, only state death taxes paid within four years of the filing of the federal estate tax return can qualify for the credit described in section 2011.

HOLDINGS

Situation 1.

When the estate elects the application of section 6166 of the Code to pay the federal estate tax, and also elects under state law to pay state death taxes in annual installments over a period longer than four years from the date of the filing of the federal estate tax return, the exception described in section 2011(c)(2) is applicable.

Situation 2.

State death taxes paid by the estate within four years of the filing of the federal estate tax return and the payment of the federal tax are eligible for the credit described in section 2011 of the Code. State death taxes paid by the estate more than four years after the filing of the federal estate tax return are not eligible for the credit described in section 2011 when none of the exceptions described in section 2011(c)(1) through (3) are applicable.

Section 2036.—Transfers with Retained Life Estate

26 CFR 20.2036-1(a): In general.

Whether property is includible in the decedent's gross estate under section 2041 of the Code where the decedent releases a general testamentary power of appointment over the property while retaining an income interest for life. See Rev. Rul. 86-39, below.

Section 2041.—Powers of Appointment

26 CFR 20.2041-3: Powers of appointment created after October 21, 1942.

Whether acquiescence in a recapitalization of closely held stock in a trust by the trust beneficiary, resulting in a shift in the beneficiary's interest by decreasing the value of the remainder interest over which the beneficiary has a general power of appointment, is a release of the power under section 2041 of the Code. See Rev. Rul. 86-39, below.

Section 2511.—Transfers in General

26 CFR 25.2511-1: Transfers in general. (Also Section 2036, 2041, 2514; 20.2036-1, 20.2041-3, 25.2514-1.)

Recapitalization; shift in value of trust assets; release of general power of appointment. Acquiescence in a recapitalization of closely held stock in a trust is a transfer by the trust beneficiary subject to the gift tax, where the recapitalization results in a shift in the beneficiary's interest by decreasing the value of the remainder interest over which the beneficiary has a general power of appointment.

Rev. Rul. 86-39

ISSUE

If the beneficiary of a trust possesses a general testamentary power of appointment over the trust corpus, if the trust holds stock of a closely held corporation, and if a recapitalization results in a shift in value from that trust to a second trust over which that beneficiary has no power of appointment, then for purposes of estate and gift taxation, is acquiescence in the recapitalization a release of the power of appointment?

FACTS

D owned 100 percent of the voting shares of *X* corporation. *D* died in 1980 and *D*'s will provided for the creation of two testamentary trusts. Trust *A* provided *D*'s spouse, *S*, with a lifetime income interest and a general testamentary power of appointment over the corpus. Trust *A* was funded with shares of *X* corporation common stock worth 120x dollars. Trust *B* provided *S* with a life income interest and *C*, *D*'s child, with the remainder interest. Trust *B* was funded with shares of *X* corporation common stock worth 80x dollars. The trustees of Trust *A* and Trust *B* were unrelated to the decedent or the trust beneficiaries.

In 1982, the stock of *X* corporation was recapitalized, resulting in two new classes of stock, voting common and nonvoting preferred. Preferred stock worth 50x dollars was allocated to Trust *A* and common stock worth 150x dollars was allocated to Trust *B*. The trustees of Trust *A* acquiesced in the recapitalization, and *S* executed a release, valid under local law, in which *S* agreed not to challenge the trustee's action with respect to the recapitalization. *S* died in 1985, when the fair market value of the preferred stock held by Trust *A* was 55x dollars and the fair market value of the common stock held by Trust *B* was 225x dollars.

LAW AND ANALYSIS

Section 2501 of the Internal Revenue Code imposes a tax on the transfer of property by gift.

Section 2511 of the Code applies the gift tax to transfers in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 2512(b) of the Code provides that where property is transferred for less than adequate and full consideration, the amount by which the value of the property transferred exceeds the value of the consideration received in a gift.

Section 2514(b) of the Code treats an exercise or release of a general power of appointment created after October 21, 1942, as a transfer of property by the individual possessing such power.

Section 25.2511-1 of the Gift Tax Regulations provides that all transactions whereby property or property rights or interests are gratuitously passed to, or conferred upon, another regardless of the means or device employed, constitute gifts subject to gift tax. However, the gift tax is not applicable to transfers for full and adequate consideration in money or money's worth, or to transactions at arm's length in the ordinary course of business.

Section 25.2511-2(b) of the regulations provides that a gift is complete if the donor parts with dominion and control so as to retain no power to change the disposition of property or any interest therein, whether for the donor's benefit or for the benefit of another.

Under section 2036(a) of the Code, for purposes of the estate tax, the value of the gross estate includes the value of any interest in property transferred, by trust or otherwise, by a decedent if the decedent had retained for life either the possession or enjoyment of, or the right to income from, the property, or the right to designate the persons who shall possess or enjoy the property or the income therefrom.

Section 2041(a)(2) of the Code provides, in part, that the gross estate shall include the value of property to the extent that the decedent had exercised or released a general power of appointment by a disposition which if it were a transfer of property owned by the decedent, would have been includible in the decedent's gross estate under section 2036 of the Code.

Section 20.2041–3 (d)(1) of the Estate Tax Regulations provides that a release of a power of appointment need not be formal or express in character. See section 25.2514-3(c)(4) for an identical rule under the Gift Tax Regulations.

Rev. Rul. 83-120, 1983-2 C.B. 170, sets forth factors to be considered in valuing the stock of a closely held corporation for gift tax purposes where a recapitalization of the corporation results in a stockholder receiving preferred and common stock in exchange for that individual's former common stock interest.

Rev. Rul. 84-105, 1984-2 C.B. 197, holds that if a surviving spouse acquiesces in an underfunding of a testamentary trust established for the spouse's benefit (by not appealing a local probate court's order), the acquiescence is treated as a gift by the spouse to the person or persons who receive the property that would otherwise have comprised the trust.

The recapitalization of the stock in *X* corporation resulted in a shift in the value of the interests between Trust *A* and Trust *B*.

Prior to the recapitalization, *S*, as beneficiary of Trust *A*, had an income interest in, and a general testamentary power of appointment over, the stock of *X* corporation worth 120x dollars and an income interest, as beneficiary of Trust *B*, in the remaining stock worth 80x dollars. As a result of the recapitalization, *S*, as beneficiary of Trust *A*, received an income interest in, and a general testamentary power of appointment over, a different class of stock worth 50x dollars and, as beneficiary of Trust *B*, received an income interest for life in stock worth 150x dollars. Although the total value of *S*'s income interest in the two trusts was unchanged as a result of the recapitalization, the value of the corpus of Trust *A* over which *S* retained a general testamentary power of appointment decreased by 70x dollars, the excess of 120x dollars over 50x dollars.

By consenting to the reallocation of stock, the trustee of Trust *A*, accepted stock with a lesser value than the value held prior to the recapitalization. *S*, as the beneficiary of Trust *A*, could have asserted the right of a trust beneficiary under local law to prevent the trustee from permitting a loss in value of the trust assets. The execution of the release in which *S* agreed not to raise an objection to the trustee's conduct with respect to the recapitalization constitutes a release of a general testamentary power of appointment by *S* over stock worth 70x dollars.

For purposes of the gift tax, the release by *S* is treated as a transfer of property to *C*, the owner of the remainder interest in Trust *B*, for which *S* did not receive adequate and full consideration. *See* Rev. Rul. 84-105. The value of the gift from *S* to *C* as as result of the recapitalization of *X* corporation is equal to the present value of the remainder interest in 70x dollars worth of stock that was shifted from Trust *A* to Trust *B*.

For purposes of the estate tax, the release of the general testamentary power of appointment over the remainder interest in the 70x dollars worth of stock is treated as a transfer under which *S*, as the income beneficiary of Trust *B*, retained an income interest for life in the transferred stock. An actual transfer of such an interest would have resulted, upon *S*'s death in 1985, in the portion of the Trust *B* corpus attributable to the value of the interest so transferred being includible in *S*'s gross estate under section 2036. Thus, in this case, *S*'s release of the power results in the inclusion of a portion of the corpus of Trust *B* in the gross estate under section 2041 of the Code to the same extent that the property would have been includible under section 2036 if there had been an actual transfer.

HOLDING

In the circumstances described above, if a recapitalization of a closely held corporation causes a shift in the value of the interests of the beneficiaries of trusts that own stock in the corporation, the shift is treated as a transfer for estate and gift tax purposes.

When the holder of a general testamentary power of appointment releases the power over property while retaining an income interest for life in that same property, the property is includible in the transferor's gross estate under section 2041 of the Code.

Section 2514.—Powers of Appointment

26 CFR 25.2514-1: Transfers under power of appointment.

Whether there is a transfer under a power of appointment for gift tax purposes where a recapitalization of a closely held corporation causes a shift in the value of the interest of a beneficiary of a trust that has a general power of appointment over the closely held stock. See Rev. Rul. 86-39, page 23.

Part III. Administrative, Procedural, and Miscellaneous

Inflation Adjustment for Computation of Windfall Profit Tax

Notice 86-4

Section 4989(b) of the Internal Revenue Code requires the determination of an inflation adjustment factor for use in computing the windfall profit tax.

The Service has determined that, for oil removed during the April-June quarter of 1986, the inflation adjustments are as follows:

Tier 1 or Tier 2 oil	0.4524
Tier 3 oil	0.6535

Worksheets for computation of the windfall profit tax are included in the Instructions for Form 6047, Windfall Profit Tax, and an explanation of the inflation adjustment may be found in the Specific Instructions for Line 4 of the worksheets.

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26 CFR 601.601: Rules and regulations.

Rev. Proc. 86-15

SECTION 1. PURPOSE

The purpose of this revenue procedure is to supersede Rev. Proc. 78-24, 1978-2 C.B. 503, and to restate the objectives of, and set forth the standards for, the publication of revenue rulings and revenue procedures in the Internal Revenue Bulletin.

SEC. 2. CHANGES

Sections 7 and 8 of Rev. proc. 78-24 have been revised to reflect the reorganization of the Internal Revenue Service in accordance with Treasury Department Order No. 150-95, 1982-1 C.B. 510, effective March 21, 1982, under Delegation Order No. 190, 1982-1 C.B. 350, the establishment of the office of the Associate Chief Counsel (International), and the responsibility of the Assistant Commissioner (Support and Services) for publishing the Internal Revenue Bulletin.

SEC. 3. DEFINITIONS

.01 A "revenue ruling" is an official interpretation of the internal revenue laws, related statutes, tax treaties and regulations, by the Service that has been published in the Bulletin. Revenue rulings are issued only by the National Office and are published for the information and guidance of taxpayers, Service officials, and others concerned.

.02 A "revenue procedure" is an official statement of a procedure published in the Bulletin that either affects the rights or duties of taxpayers or other members of the public under the Internal Revenue Code and related statutes and regulations, or, although not necessarily affecting the rights and duties of the public, should be a matter of public knowledge.

SEC. 4. BACKGROUND

.01 The Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for the publication of official rulings and procedures of the Service, including all rulings and statements of procedure that supersede, revoke, modify, amend, or affect any previously published ruling or procedure. The Service also announces in the Bulletin the Commissioner's acquiescence or nonacquiescence in decisions of the United States Tax Court (other than decisions in memorandum opinions), and publishes Treasury Decisions, Executive Orders, tax conventions, legislation, court decisions, and other items considered to be of general interest.

.02 The Bulletin is published weekly. In order to provide a permanent reference source, the contents of the bulletin are consolidated semiannually into an indexed Cumulative Bulletin. These materials are sold by the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402.

SEC. 5. OBJECTIVES

The purpose of publication of revenue rulings and revenue procedures in the Bulletin is to promote uniform application of the tax laws by Service employees and to assist taxpayers in attaining maximum voluntary compliance by informing Service personnel and the public of National Office interpretations of the internal revenue laws, related statutes, tax treaties, and regulations, and statements of Service procedures affecting the rights and duties of taxpayers.

SEC. 6. PUBLICATION STANDARDS

.01 It is the policy of the Service to publish in the Bulletin issues and answers involving substantive tax laws under the jurisdiction of the Service, except those involving—

(1) Issues answered by statute, tax treaties, or regulations;

(2) Issues answered by rulings, opinions, or court decisions previously published in the Bulletin;

(3) Issues that are of insufficient importance or interest to warrant publication;

(4) Determinations of fact rather than interpretations of law,

(5) Informers and informers' rewards; and

(6) Disclosure of secret formulas, processes, business practices, and similar information.

.02 It is the policy of the Service to publish in the bulletin procedures affecting taxpayers' rights or duties that relate to matters under the jurisdiction of the Service.

SEC. 7. FORM AND EFFECT OF PUBLICATION

.01 Revenue rulings.—(1) Rulings and other communications involving substantive tax law published in the Bulletin are published in the form of revenue rulings. The conclusions expressed in revenue rulings will be directly responsive to, and limited in scope by, the pivotal facts stated in the revenue ruling. Revenue rulings arise from various sources, including rulings to taxpayers, technical advice to district offices, court decisions, suggestions from tax practitioner groups, publications, etc.

(2) The Service publishes as much of the ruling or communication as is necessary for an understanding of the position stated. However, identifying details, including the names and addresses of persons involved, and information of a confidential nature are not included, to prevent unwarranted invasions of personal privacy and to comply with statutory provisions, such as 18 U.S.C. 1905 and 26 U.S.C. 6103 and 7213, dealing with disclosure of information obtained from members of the public.

(3) A revenue ruling, other than one relating to the qualification of pension, annuity, profit-sharing, stock bonus, and bond purchase plans, applies retroactively, unless it includes a specific statement indicating, under the authority of section 7805(b) of the Code, the extent to which it is to be applied without retroactive effect. When revenue rulings revoke or modify rulings previously published in the Bulletin, the authority of section 7805(b) ordinarily is invoked to provide that the new rulings will not be applied retroactively to the extent that the new rulings have adverse tax consequences to taxpayers. Section 7805(b) provides that the Secretary of the Treasury, or the Secretary's delegate, may prescribe the extent to which any ruling is to be applied without retroactive effect. That authority has been delegated to the Commissioner and has been redelegated to the Associate Chief Counsel (Technical), Associate Chief Counsel (International) and the Assistant Commissioner (Employee Plans and Exempt Organizations) and to each of their deputies. The exercise of this authority requires an affirmative action. For the effect of revenue rulings on determination letters and opinion letters issued with respect to the qualification of pension, annuity, profit-sharing, stock bonus, and bond purchase plans, see section 13 of Rev. Proc. 80-30, 1980-1 C.B. 685.

(4) Revenue rulings published in the Bulletin do not have the force and effect of Treasury Department Regulations (including Treasury Decisions), but are published to provide precedents to be used in the disposition of other cases, and may be cited and relied upon for that purpose. No unpublished ruling or decision will be relied on, used, or cited, by any officer or employee of the Service as a precedent in the disposition of other cases.

(5) Taxpayers generally may rely upon revenue rulings published in the Bulletin in determining the tax treatment of their own transactions and need not request specific rulings applying the principles of a published revenue ruling to the facts of their particular cases. However, since each revenue ruling represents the conclusion of the Service as to the application of the law to the entire statement of facts involved, the taxpayers, Service personnel, and others concerned are cautioned against reaching the same conclusion in other cases unless the facts and circumstances are substantially the same. They should consider the effect of subsequent legislation, regulations, court decisions, and revenue rulings.

(6) Comments and suggestions from taxpayers, taxpayer groups, or other interested parties, on revenue rulings being prepared for publication in the Bulletin may be solicited if justified by special circumstances. Conferences on revenue rulings being prepared for publication will not be granted except when the Service determines that such action is justified by special circumstances.

.02 Revenue procedures.—When revenue procedures reflect the contents of internal management documents, it is Service practice to publish as much of the internal management document as is necessary for an understanding of the procedure. When publication of the substance of a revenue procedure in the Federal Register is required pursuant to 5 U.S.C. 552, it will usually be accomplished by an amendment of the Statement of Procedural Rules (26 CFR Part 601).

SEC. 8. RESPONSIBILITIES

.01 The Chief Counsel is responsible for administering the Service's revenue ruling and revenue procedure publication program including the standards for style and format of revenue rulings and revenue procedures. The Assistant Commissioner (Support and Services) is responsible for publishing the Internal Revenue Bulletin weekly and for consolidating the contents of the Bulletin semiannually into an indexed Cumulative Bulletin.

.02 In accordance with the standards set forth in section 6 of this revenue procedure the Associate Chief Counsel (Technical), the Associate Chief Counsel (International) and the Assistant Commissioner (Employee Plans and Exempt Organizations) are responsible for the preparation and appropriate referral for publication of revenue rulings reflecting interpretations of substantive tax law made by their respective offices and communicated in writing to taxpayers or field offices.

.03 In accordance with the standards set forth in section 6 of this revenue procedure, all Assistant Commissioners and the Chief Counsel are responsible for determining whether procedures established by any office under their jurisdiction should be published as revenue procedures and for the initiation, content, and appropriate referral for publication of such revenue procedures.

SEC. 9. EFFECTS ON OTHER DOCUMENTS

Rev. Proc. 78-24 is superseded.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Section 338(b)—Basis of Target Corporation Assets

LR-191-82

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary regulations that add new §§1.338(b)-1T through 1.338(b)-3T, relating to the determination of the basis of assets of a target corporation, and that amend existing temporary regulations §1.338-4T, relating to miscellaneous matters under section 338. The text of the new and revised sections also serves as the comment document for this notice of proposed rulemaking.

DATES:

PROPOSED EFFECTIVE DATE

The final regulations under section 338(b) are proposed to be effective [upon publication in the FEDERAL REGISTER] and to apply generally to stock acquisitions made after August 31, 1982.

DATES FOR COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Written comments and requests for a public hearing must be delivered or mailed by March 31, 1986.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T [LR-191-82], Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Bennett C. Steinhauer or Patricia Wendlandt of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) or telephone 202-566-3458 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

Temporary regulations published * * *[on page 7, this Bulletin] add new temporary regulations §§1.338(b)-1T through 1.338(b)-3T to Part 1 of title 26 of the Code of the Federal Regulations ("CFR") and amend temporary regulations §§1.338-1T and 1.338-4T. The final regulations that are proposed to be based on the new and amended temporary regulations would be added to Part 1 of Title 26 of the CFR. Those final regulations would provide guidance on the determination of the basis of the assets of a target corporation for which an election is made under section 338 of the Internal Revenue Code. Section 338(b) was added by section 224 of the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") (Pub. L. No. 97-248; 96 Stat. 485) [1982-2 C.B. 462, 501] and was amended by section 712(k) of the Tax Reform Act of 1984 (Pub. L. No. 98-369; 98 Stat. 948) [1984-3 C.B. (Vol. 1), 1, 456]. For the text of the new and amended temporary regulations, see T.D. 8072, published * * * [on page 7, this Bulletin]. The preamble to the temporary regulations explains the additions to the regulations.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required.

COMMENTS AND REQUEST FOR A PUBLIC HEARING

Before these proposed regulations are adopted, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

DRAFTING INFORMATION

The principal authors of these proposed regulations are Bennett C Steinhauer and Patricia Wendlandt of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both of matters on substance and style.

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on January 23, 1986, 4:49 p.m., and published in the issue of the Federal Register for January 29, 1986, 51 F.R. 3634)

Foundations Status of Certain Organizations

Announcement 86-29

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings as designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

A.T.C. Research Foundation, San Diego, CA
American Multi-Cultural Women's & Children's Health & Community Ctr. Inc., Compton, CA
Assistance For Children Under Crisis, Inc., San Diego, CA

Assistance In Health Care, Inc., Zion, IL
Bonita Services, Inc., Berkeley, CA
Bonner General Hospital Foundation, Sandpoint, ID
Cedarburg Athletic Booster Club, Inc., Cedarburg, WI
Cherie and Eli Kaplan Foundation, The, Far Rockaway, NY
Company Theater, The, Minneapolis, MN
Council on Public Policy Education, Dayton, OH
Crowleys Booster Club, Oakdale, MN
Duluth Cathedral High School Teachers Scholarship Fund, Duluth, MN
Economic Growth Opportunity Ltd., Oakland, CA
Evangelisma International, Inc., Wilmington, DE
Festival of Light and Song, Inc., Cambridge, MA
Firefighters Annual Charitable Ski Race Corp., Staten Island, NY
Friends For Life, Inc., Chicago, IL
George P. Lockhart Foundation, Inc., Swansea, MA
Gyrphon Theatricals, Inc., New York, NY
Herr Foundation, Inc., Flushing, NY
Human Service Providers, Inc., Mansfield, PA
Idyllwild International Jazz Institute, Idyllwild, CA
Illinois Chamber Symphony, St. Charles, IL
Inglewood Philharmonic Association, Los Angeles, CA
Institute for Policy Development, Seattle, WA
Institute for Vico Studies, Inc., New York, NY
International Human Powered Vehicle Assoc., Claremont, CA
Iowa Mennonite Crowded Closet, Iowa City, IA
Iowa Neighborhood Improvement Corporation Inc., Des Moines, IA
Johnson County Humane Society, Inc., Iowa City, IA
Kahala Parent Teacher Organization, Honolulu, HI
Kettle Moraine Hospice Services, Inc., West Bend, WI
Korean Youth Center, Inc., Los Angeles, CA
Lincoln Neighborhoods, Inc., Lincoln, NE
Madrigal Singers of St. Louis, Inc., The, St. Louis, MO
Markham Community Christian Youth Center, Markham, IL
Math Unlimited Minnesota, St. Paul, MN
Meadows Amateur Ski Racing Association, Oregon City, OR
Nc Hi FPA Boosters, Milton-Freewater, OR
New Ulm Eagles Boosters Club, Inc., New Ulm, MN
Parents With Hearts of Northern Illinois, Rockford, IL
Performing Arts Collaborative Inc., The, Melville, NY
Rogers Park Cultural and Performing Arts Centre, Chicago, IL
Society To Save The Stage, San Gabriel, CA
Soda Pop Athletic Association, Portsmouth, NH
South Lincoln Terminal Care Support Group, Newport, OR
Swim San Diego, La Jolla, CA
Technology Awareness Center, Irvine, CA
Theatrical Resource Coalition, Tacoma, WA
United Indian Development Assoc., Los Angeles, CA
Venice of America Museum Foundation, Los Angeles, CA
Wisconsin Tavern League Foundation, Inc., Madison, WI
Women Lawyers Scholarship Fund, St. Louis, MO

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Clarification of Instructions to Form 8308

Announcement 86-30

This announcement concerns the information required to be provided on Form 8308 in certain situations which are not specifically addressed in the instructions accompanying that form. Form 8308 is to be used by partnerships as the return filed with the Internal Revenue Service and as the statement furnished to transferor and transferee partners in certain sales or exchanges of partnership interests under section 6050K of the Internal Revenue Code. Under section 6050K, partnerships generally must file returns and furnish statements with respect to each sale or exchange of a partnership interest where any portion of any money or property received in exchange for the partnership interest is attributable to unrealized receivables or substantially appreciated inventory items (hereinafter referred to as a "section 751(a) exchange"). Temporary regulations under section 6050K were published in the Federal Register on December 23, 1985 (50 Fed. Reg. 52,313). Announcement 86-8, 1986-5 I.R.B. 45, extended the due date for furnishing statements on Form 8308 for 1985 from January 31, 1986, to March 14, 1986.

A separate Form 8308 is required to be completed for each section 751(a) exchange. The form must contain the names, addresses, and taxpayer identification numbers of the transferor and transferee partners in the exchange and of the partnership filing the return, as well as the date of the exchange. Although this information is generally available to the partnership, in certain situations the partnership may not be able to include all of the information on Form 8308 with respect to a particular section 751(a) exchange. This announcement describes some of these situations and provides guidance to partnerships for completing Form 8308 for calendar year 1985 in order to avoid penalties under sections 6652(a) and 6678(a) of the Code. Generally, the penalty for failure to file a return or statement under section 6050K is $50 for each return or statement, with a maximum penalty for each partnership of $50,000 for all returns and $50,000 for all statements for any year. The penalty is not imposed if it is shown that the failure is due to reasonable cause.

Matching transferors and transferees. In certain situations partnerships may not be able to match the transferor and transferee partners in a particular section 751(a) exchange and are thus unable to complete all entries on Form 8308. For example, if a publicly traded limited partnership has notice that on July 1, 1985, partners A, B, and C sold their interests and partners D, E, and F purchased partnership interests in a section 751(a) exchange, the partnership may be unable to determine which interest was sold to whom (that is, whether A's interest was sold to D, E, or F, etc.).

Where a partnership is not able to match transferor and transferee partners in a particular section 751(a) exchange, the Service will not impose penalties under sections 6652(a) and 6678(a) for calendar year 1985 with respect to that exchange if the partnership: (1) Timely files a return on Form 8308 with respect to the exchange containing all information required to be provided except information relating to the transferee partner (Part II of Form 8308); and (2) timely furnishes a copy of that Form 8308 to the transferor partner. Similarly, no penalty will be imposed on transferor partners under section 6678(c) for calendar year 1985, with respect to a section 751(a) exchange, where the transferor partner does not know the identity of the transferee partner and timely notifies the partnership, in writing, of the section 751(a) exchange, if the written notification includes the name, address, and taxpayer identification number of the transferor partner and the date of the exchange.

Record interest holders. In certain situations partnerships may have notice that a section 751(a) exchange has occurred, but the identity of the transferor or transferee (the beneficial owner of the interest before or after the transfer) is unknown because the transferor or transferee may be a person other than the record holder of the partnership interest. This situation may arise, for example, where partnership interests are held in street name, or by a nominee, and the partnership is not notified of the sale or exchange directly by the transferor.

Where a partnership has notice that a section 751(a) exchange has occurred, the partnership may treat the record holder of the interest as the transferor or transferee for the purpose of completing Form 8308 for calendar year 1985, in the absence of knowledge of the identity of the beneficial holder of the partnership interest (even though the partnership has knowledge that the beneficial holder is not the record holder of the partnership interest). However, this rule does not relieve the transferor of his duty under section 6050K(c)(1) to notify the partnership of the section 751(a) exchange.

Multiple transfers between the same parties. Generally, a separate Form 8308 is required to be completed for each section 751(a) exchange occurring during 1985. However, for calendar year 1985 only, partnerships may use a single Form 8308 to report two or more section 751(a) exchanges *by a single transferor* if all exchanges reported on that form either: (1) Were with the same transferee; or (2) were exchanges in which the transferor and transferee cannot be matched (and therefore the transferee information is not required to be provided on the form).

The dates of all exchanges reported on the single Form 8308 must be included in the appropriate place on the form. The single Form 8308 may be used as the return required under section 6050K(a) for all exchanges included therein and a copy of the single Form 8308 may be used as the statement required to be furnished to the transferor and the transferee partners under section 6050K(b). If the single Form 8308 does not contain information with respect to the transferee partner, a copy must only be furnished to the transferor partner.

This announcement only applicable to calendar year 1985. The provisions of this announcement only apply with respect to returns and statements on Form 8308 for calendar year 1985.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Dal H. Felkel	Kingstree, SC	Certified Public Accountant	Indefinite from January 31, 1986
John J. Matonis	Walnut, CA	Attorney	Indefinite from January 24, 1986
Joel A. Shor	Baltimore, MD	Certified Public Accountant	Five Months from December 15, 1985
Patrick H. Diamond	New York, NY	Attorney & Certified Public Accountant	Indefinite from February 10, 1986
Folger P. Gifford	Cold Spring Harbor, NY	Certified Public Accountant	Indefinite from February 11, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.936-2, 1.936-3, 1.936-3A, added; 7.936-1, removed.	Qualified possession source investment income	1986-8 I.R.B. 33	Mar. 24, 1986
26 CFR 1.6031-1, revised.	Partnership returns	1986-9 I.R.B. 31	Mar. 24, 1986
26 CFR 1.401(a)-4, 1.411(d)-4, added.	Limitations on alternative benefits under qualified plans	1986-9 I.R.B. 26	Mar. 31, 1986
26 CFR 1.904(f)-1 through 1.904(f)-6, 1.1502-9, added.	Recapture of foreign losses	1986-10 I.R.B. 14	Mar. 25, 1986

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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______	*1927-2*	*18.00*
______	1928-1	8.00
______	1928-2	10.00
______	1929-1	13.00
______	*1929-2*	*3.50*
______	1930-1	8.50
______	1930-2	10.00
______	*1931-1*	*4.00*
______	1931-2	14.00
______	*1932-1*	*3.25*
______	1932-2	10.00
______	*1933-1*	*3.75*
______	*1933-2*	*4.00*
______	*1934-1*	(**)
______	1934-2	15.00
______	1935-1	8.00
______	*1935-2*	*15.00*
______	*1936-1*	*4.00*
______	*1936-2*	*15.00*
______	*1937-1*	*14.00*
______	1937-2	8.50
______	*1938-1*	*17.00*
______	*1938-2*	*14.00*
______	1939-1-1	9.50
______	1939-1-2	12.00
______	1939-2	10.00
______	1940-1	6.50
______	1940-2	15.00
______	1941-1	8.00
______	*1941-2*	*4.00*
______	1942-1	8.00
______	*1942-2*	*6.50*
______	*1943-(*)*	*11.00*
______	*1944-(*)*	*9.00*
______	1945-(*)	10.00
______	*1946-1*	*3.00*
______	1946-2	6.00
______	*1947-1*	*2.00*
______	1947-2	3.75
______	*1948-1*	*3.50*
______	1948-2	8.50
______	*1949-1*	*8.00*
______	*1949-2*	*3.25*
______	1950-1	7.00
______	*1950-2*	*5.50*
______	*1951-1*	*13.00*
______	*1951-2*	*6.00*
______	*1952-1*	*3.00*
______	1952-2	8.00
______	*1953-1*	*4.75*
______	1953-2	13.00
______	1954-1	13.00
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______	1958-2	(**)
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______	1962-2	14.00
______	1962-3	22.00
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______	1964-1-1	11.00
______	1964-1-2	12.00
______	1964-2	28.00
______	1965-1	19.00
______	1965-2	13.00
______	1966-1	15.00
______	1966-2	15.00
______	1967-1	11.00
______	1967-2	17.00
______	1968-1	15.00
______	1968-2	13.00
______	1969-1	15.00
______	1969-2	7.50
______	1969-3	14.00
______	1970-1	12.00
______	1970-2	(**)
______	1971-1	12.00
______	1971-2	17.00
______	1972-1	15.00
______	1972-2	15.00
______	1973-1	18.00
______	1973-2	15.00
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______	1974-2	11.00
______	*1974-3*	*9.50*
______	1974-3 Supp.	11.00
______	1975-1	15.00
______	1975-2	14.00
______	1976-1	12.00
______	1976-2	11.00
______	1976-3-1	10.00
______	1976-3-2	18.00
______	1976-3-3	11.00
______	1977-1	12.00
______	1977-2	13.00
______	1978-1	13.00
______	1978-2	14.00
______	1978-3-1	13.00
______	1978-3-2	9.50
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______	1979-2	17.00
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Internal Revenue
# bulletin

March 24, 1986
Bulletin No. 1986-12

Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

SPECIAL ANNOUNCEMENT

Announcement 86–34, page 26.

A public hearing will be held on June 4, 1986, on the $40 million limitation upon beneficiaries of certain tax-exempt bond issues and on the definition of the term "principal user" for purposes of section 103(b)(6) and (15) of the Code.

INCOME TAX

Rev. Rul. 86-40, page 5.

LIFO; price indexes; department stores. The December 1985 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, December 31, 1985.

Rev. Proc. 86-14, page 11.

Depreciation; recovery period. Section 4.02 of Rev. Proc. 86-6, relating to the increase in the recovery period from 18 to 19 years, is modified and certain numbers in tables are corrected. Rev. Proc. 86-6 modified and superseded.

T.D. 8070, page 6.

Temporary regulations relating to the loss deferral, wash sale, and holding period rules for straddles are amended.

LR-157-84, page 22.

LR-59-74, page 19.

Amendments to the regulations under section 103(b) of the Code relate to the $40 million limitation on beneficiaries of certain tax-exempt bond issues and to the definition of the term "principal user."

Finding Lists begin on page 33.
Announcement of Suspensions on page 30.
Announcement of Notice of Proposed Rulemaking on page 31.

Announcement 86-31, page 25.

The time for making certain elections and for taking certain other actions under section 338 of the Code has been extended.

Announcement 86-32, page 26.

The Service is not appealing the decision of the Tax Court in *Woods Investment Co. v. Commissioner.* Although the Service disagrees with the result in that case, it will no longer advance the position that it advanced in that case, pending a change in the regulations.

Announcement 86-35, page 27.

Taxpayers will be allowed to aggregate certain partnership and S corporation activities for purposes of the at-risk rules under section 465 of the Code.

Announcement 86-36, page 27.

The "differential earnings rate" under section 809 of the Code is tentatively determined for taxable year 1985 together with the "recomputed differential earnings rate" for 1984.

GIFT TAX

Rev. Rul. 86-41, page 9.

Transfers; real property; adjustment to portion transferred based on Service's valuation. The value of a gift will be determined without regard to an adjustment clause that provides for the recharacterization of the transaction depending on the Service's valuation of the property.

ADMINISTRATIVE

Rev. Proc. 86-16, page 13.

Liquidation of corporation; revised checklist for ruling request. A revised checklist sets forth the information and representations to be included in a request for a ruling under sections 331 and 337 of the Code with respect to a liquidation of a corporation. Rev. Proc. 81-52 superseded.

Announcement 86-23, page 25.

Certain depreciation tables for 19-year real property placed in service after May 8, 1986, should be used instead of the tables in Publication 534, Depreciation.

(Continued on page 4)

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

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HIGHLIGHTS OF THIS ISSUE—Continued

ADMINISTRATIVE—Continued

Announcement 86-37, page 26.

Several 1985 tax forms were printed before enactment of legislation extending the recovery period for 18-year real property to 19 years. Taxpayers should include amounts attributable to 19-year real property wherever "15 or 18-year" appear on these forms.

Announcement 86-38, page 27.

Publication 519, U.S. Tax Guide for Aliens, contains errors in three examples.

Announcement 86-40, page 29.

Form 8264, Application for Registration of a Tax Shelter, and instructions, have been revised. The form and instructions should be available by the end of March 1986.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 168.—Accelerated Cost Recovery System

The cost recovery rates for real property set forth in Rev. Proc. 86-6, are hereby corrected. See Rev. Proc. 86-14, page 11.

Section 331.—Gain or Loss to Shareholders in Corporate Liquidations

26 CFR 1.331-1: Corporate liquidations.

Checklist concerning information to be included in a request for a ruling with regard to corporate liquidations under sections 331 and 337 of the Code. See Rev. Proc. 86-16, page 13.

Section 337.—Gain or Loss on Sales or Exchanges in Connection With Certain Liquidations

26 CFR 1.337-1: General.

Checklist concerning information to be included in a request for a ruling with regard to corporate liquidations under sections 331 and 337 of the Code. See Rev. Proc. 86-16, page 13.

Section 472.—Last-in, First-out Inventories

26 CFR 1.472-1: Last-in, first-out inventories.

LIFO; price indexes; department stores. The December 1985 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, December 31, 1985.

Rev. Rul. 86-40

The following price indexes for December 1985 were issued by the Bureau of Labor Statistics on January 24, 1986, for use by department stores, and are accepted by the Internal Revenue Service, under section 1.472-1(k) of the Income Tax Regulations and Rev. Proc. 72-21, 1972-1 C.B. 745, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, December 31, 1985.

Indexes are prepared on a national basis for the store total, for 20 major groups of departments, and for two special combinations—soft and durable goods. The store total index covers all departments, including some not listed separately, with the following exceptions: candy, foods, liquor, tobacco, paints, and wallpaper, as well as contract departments.

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS
(January 1941 = 100)

		December 1984	December 1985	Percentage Change from December 1984 to December 1985[1]
I.	Piece Goods	399.1	404.4	1.3
II.	Domestics and Draperies	546.0	541.5	−0.8
III.	Women's and Children's Shoes	553.5	549.4	−0.8
IV.	Men's Shoes	704.8	727.0	3.1
V.	Infants' Wear	483.8	500.4	3.4
VI.	Women's Underwear	425.3	441.7	3.9
VII.	Women's and Girls' Hosiery	235.1	238.6	1.5
VIII.	Women's and Girls' Accessories	450.0	452.6	0.6
IX.	Women's Outerwear and Girls' Wear	343.0	351.8	2.6
X.	Men's Clothing	467.6	477.6	2.1
XI.	Men's Furnishings	472.1	488.5	3.5
XII.	Boys' Clothing and Furnishings	443.6	451.2	1.7
XIII.	Jewelry	677.9	665.2	−1.9
XIV.	Notions	485.7	488.5	0.6
XV.	Toilet Articles and Drugs	625.9	647.8	3.5
XVI.	Furniture and Bedding	530.2	540.7	2.0
XVII.	Floor Coverings	459.6	456.7	−0.6
XVIII.	Housewares	707.4	717.3	1.4
XIX.	Major Appliances	240.6	243.5	1.2
XX.	Radio and Television	107.2	100.5	−6.3
	Groups I–XV: Soft Goods	473.8	482.1	1.8
	Groups XVI–XX: Durable Goods	442.2	445.4	0.7
	Store Total	464.7	471.8	1.5

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[1] Absence of a minus sign before percentage change in this column signifies price increase.

Section 1092.—Straddles

26 CFR 1.1092(b)-1T: Coordination of loss deferral rules and wash sale rules (temporary).

T.D. 8070

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER A, PART 1—INCOME TAX: TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Coordination of Loss Deferral and Wash sale Rules and Treatment of Holding Periods and Losses Under Section 1092

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document amends temporary regulations relating to the loss deferral, wash sale, and holding period rules for straddles. Changes in the applicable tax law were made by the Economic Recovery Tax Act of 1981 [Pub. L. 97-34, 1981-2 C.B. 256], the Technical Corrections Act of 1982 [Pub. L. 97-448, 1983-1 C.B. 451], and the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1]. These regulations affect taxpayers holding straddles and provide Internal Revenue Service personnel who administer the Internal Revenue Code and members of the public with the guidance necessary to comply with the law.

DATES: The regulations under §1.1092(b)-1T, relating to the coordination of the loss deferral rules and wash sale rules, apply to dispositions of loss positions on or after January 24, 1985, and are effective on or after January 24, 1985. The regulations under §1.1092(b)-2T(d), relating to the treatment of holding periods and losses with respect to straddle positions, apply to positions established after June 23, 1981, and are effective after June 23, 1981.

FOR FURTHER INFORMATION CONTACT: Timothy J. McKenna of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T). Telephone 202-566-3287 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains amendments to the Temporary Income Tax Regulations (26 CFR Part 1) under section 1092(b) of the Internal Revenue Code of 1954 which were published in the FEDERAL REGISTER on January 24, 1985 (50 FR 3317 [T.D. 8007, 1985-1 C.B. 269]. A notice of proposed rulemaking cross-referencing these temporary regulations was published in the same issue of the FEDERAL REGISTER (50 FR 3352) [LR-297-84, 1985-1 C.B. 662]. These amendments conform the regulations to section 501 of the Economic Recovery Tax Act of 1981 (Pub. L. 97-34, 95 Stat. 323) [1981-2 C.B. 256, 335], section 105 of the Technical Corrections Act of 1982 (Pub. L. 97-448, 96 Stat. 2384) [1983-1 C.B. 451, 460], and section 103 of the Tax Reform Act of 1984 (Pub. L. 98-369, 98 Stat. 627) [1984-3 C.B. (Vol. 1) 1, 135]. The temporary regulations provided by this document will remain in effect until superseded by final regulations on this subject.

SUMMARY OF CHANGES IN TEMPORARY REGULATION

This document amends §1.1092(b)-1T by adding rules relating to the coordination of the loss deferral rules under section 1092 and the wash sale rules under section 1091, and by revising and adding certain examples in §1.1092(b)-1T. This document also amends §1.1092(b)-2T(d), relating to the treatment of holding periods and losses with respect to straddle positions held by regulated investment companies, and §1.1092(b)-5T, relating to definitions for §§1.1092(b)-1T through 1.1092(b)-4T.

Under §1.1092(b)-1T(a) of the prior temporary regulations, a taxpayer disposing of a loss position of a straddle generally had to defer the loss to the extent of unrecognized gain in successor positions, offsetting positions to the loss position, or offsetting positions to the successor positions. The revised temporary regulations provide rules under paragraph (a)(1) of §1.1092(b)-1T that are to be applied (with respect to dispositions of loss positions on or after January 24, 1985) prior to the application of the rules provided under §1.1092(b)-1T(a) of the prior temporary regulations. The rules of §1.1092(b)-1T(a) of the prior temporary regulations are now contained in paragraph (a)(2) of §1.1092(b)-1T. Paragraph (a)(1) of revised regulation §1.1092(b)-1T generally provides for the deferral of any loss sustained by a taxpayer from the disposition of stock or securities that constitute positions in a straddle when the taxpayer acquires substantially identical stock or securities within 30 days of the disposition. Under the revised regulations, if the loss is not deferred under §1.1092(b)-1T(a)(1), then the rules under §1.1092(b)-1T(a)(2) apply.

Paragraph (n) of temporary regulation §1.1092(b)-5T has been revised, and new paragraphs (p) and (q) have been added. Paragraph (n) contains the definition of a "successor position". The revised temporary regulations narrow the definition of a successor position for purposes of applying the loss deferral rules under section 1092(a). Under the revised regulations, a position entered into after all positions of a straddle are disposed of will not be considered a successor position. Paragraphs (p) and (q) of revised temporary regulations §1.1092(b)-5T contain the definitions of "substantially identical" and "securities", respectively. "Substantially identical" is defined with reference to section 1091(a). "Securities" is defined with reference to section 1236(c).

The examples in temporary regulation §1.1092(b)-1T(g) (paragraph (f) of the prior temporary regulations) have been revised. Examples (4), (8), (9), and (16) of the prior temporary regulations are revised; examples (13), (14), and (15) are deleted; several examples are renumbered; and new examples (8), (14), and (17) through (27) are added to reflect the changes to the temporary regulations.

Revised §1.1092(b)-2T(d) provides that the rules of §1.1092(b)-4T(c), relating to the daily marking-to-market of positions in a mixed straddle account, will not apply for purposes of section 851(b)(3) (relating to the definition of a regulated investment company).

REGULATORY FLEXIBILITY ACT

A general notice of proposed rulemaking is not required by 5 U.S.C. 553 for temporary regulations. Accordingly, the temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive order 12291 and that a regulatory impact analysis therefore is not required.

DRAFTING INFORMATION

The principal author of these temporary regulations is Timothy J. McKenna of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 1 is amended as follows:

Paragraph 1. The authority for Part 1 continues to read in part:

Authority 26 U.S.C. 7805. * * * Sections 1.1092(b)-1T and 1.1092(b)-2T also issued under 26 U.S.C. 1092(b)(1). * * *

Par. 2. Section 1.1092(b)-1T is amended as follows:

(a) Paragraphs (a) through (d) are revised to read as set forth below.

(b) Paragraphs (e) and (f) are redesignated as paragraphs (f) and (g), respectively, and a new paragraph (e) is added to read as set forth below.

(c) The examples in paragraph (g) are revised as follows:

(1) *Example* (4) is amended by adding at the end of the third sentence the words "but is not substantially identical to the long position disposed of on November 10, 1985."

(2) *Examples* (13), (14), and (15) are deleted.

(3) *Examples* (10), (11), and (12) are renumbered "*Example* (11).", "*Example* (12).", and "*Example* (13).", respectively.

(4) *Example* (9) is renumbered "*Example* (10)." and is amended by adding at the end of the fourth sentence the words "but is not substantially identical to the short position disposed of on November 10, 1985."

(5) *Example* (8) is renumbered "*Example* (9)." and is amended by adding after the first sentence the sentence "neither the long nor the short position is stock or securities."

(6) *Example* (16) is renumbered "*Example* (15).", and is amended by adding at the end of the third sentence the words "that is offsetting to the long position, but is not substantially identical to the short position disposed of on December 4, 1985" and by adding at the end of the fifth sentence the words "that is offsetting to the new short position, but is not substantially identical to the long position disposed of on December 6, 1985."

(7) *Example* (17) is renumbered "*Example* (16).".

(8) New examples (8), (14), and (17) through (27) are added to read as set forth below.

(9) In the first sentence in redesignated *Examples (11), (12)* and *(13)*, the language "example (9)" is removed and the language "*example (10)*" is added in its place.

§1.1092(b)-1T Coordination of loss deferral rules and wash sale rules (temporary).

(a) *In general.* Except as otherwise provided, in the case of the disposition of a position or positions of a straddle, the rules of paragraph (a)(1) of this section apply before the application of the rules of paragraph (a)(2) of this section.

(1) Any loss sustained from the disposition of shares of stock or securities that constitute positions of a straddle shall not be taken into account for purposes of this subtitle if, within a period beginning 30 days before the date of such disposition and ending 30 days after such date, the taxpayer has acquired (by purchase or by an exchange on which the entire amount of gain or loss was recognized by law), or has entered into a contract or option so to acquire, substantially identical stock or securities.

(2) Except as otherwise provided, if a taxpayer disposes of less than all of the positions of a straddle, any loss sustained with respect to the disposition of that position or positions ((hereinafter referred to as "loss position") shall not be taken into account for purposes of this subtitle to the extent that the amount of unrecognized gain as of the close of the taxable year in one or more of the following positions—

(i) Successor positions,

(ii) Offsetting positions to the loss position, or

(iii) Offsetting positions to any successor position,

exceeds the amount of loss disallowed under paragraph (a)(1) of this section. See §1.1092(b)-5T relating to definitions.

(b) *Carryover of disallowed loss.* Any loss that is disallowed under paragraph (a) of this section shall, subject to any further application of paragraph (a)(1) of this section and the limitations under paragraph (a)(2) of this section, be treated as sustained in the succeeding taxable year. However, a loss disallowed in Year 1, for example, under paragraph (a)(1) of this section will not be allowed in Year 2 unless the substantially identical stock or securities, the acquisition of which caused the loss to be disallowed in Year 1, are disposed of during Year 2 and paragraphs (a)(1) and (a)(2) of this section do not apply in Year 2 to disallow the loss.

(c) *Treatment of disallowed loss*—(1) *Character.* If the disposition of a loss position would (but for the application of this section) result in a capital loss, the loss allowed under paragraph (b) of this section with respect to the disposition of the loss position shall be treated as a capital loss. In any other case, a loss allowed under paragraph (b) of this section shall be treated as an ordinary loss. For example, if the disposition of a loss position would, but for the application of paragraph (a) of this section, give rise to a capital loss, that loss when allowed pursuant to paragraph (b) of this section will be treated as a capital loss on the date the loss is allowed regardless of whether any gain or loss with respect to one or more successor positions would be treated as ordinary income or loss.

(2) *Section 1256 contracts.* If the disposition of a loss position would (but for the application of this section) result in 60 percent long-term capital loss and 40 percent short-term capital loss, the loss allowed under paragraph (b) of this section with respect to the

disposition of the loss position shall be treated as 60 percent long-term capital loss and 40 percent short-term capital loss regardless of whether any gain or loss with respect to one or more successor positions would be treated as 100 percent long-term or short-term capital gain or loss.

(d) *Exceptions.*—(1) This section shall not apply to losses sustained—

(i) With respect to the disposition of one or more positions that constitute part of a hedging transaction;

(ii) With respect to the disposition of a loss position included in a mixed straddle account (as defined in paragraph (b) of §1.1092(b)-4T); and

(iii) With respect to the disposition of a position that is part of a straddle consisting only of section 1256 contracts.

(2) Paragraph (a)(1) of this section shall not apply to losses sustained by a dealer in stock or securities if such losses are sustained in a transaction made in the ordinary course of such business.

(e) *Coordination with section 1091*. Section 1092(b) applies in lieu of section 1091 to losses sustained from the disposition of positions in a straddle. See example (18) of paragraph (g) of this section.

* * * * *

(g) *Examples*. * * *

Example (8). Assume the facts are the same as in example (4), except at year-end there is $8 of unrecognized gain in the successor long position and $8 of unrecognized loss in the offsetting short position. Under these circumstances, $8 of the total $10 realized loss will be disallowed because there is $8 of unrecognized gain in the successor long position.

* * * * *

Example (14). On January 2, 1986, A enters into offsetting long and short positions. Neither the long nor the short position is stock or securities. On March 3, 1986, A disposes of the long position at a $10 gain. On March 10, 1986 A disposes of the short position at a $10 loss. On March 14, 1986, A enters into a new short position. On April 10, 1986, A enters into a new short position. On April 10, 1986, A enters into an offsetting long position. A holds both positions to year-end, at which time there is $10 of unrecognized gain in the offsetting long position and no unrecognized gain or loss in the short position. Under these circumstances, the $10 loss will be allowed because (1) the rules of paragraph (a)(1) of this section are not applicable; and (2) the rules of paragraph (a)(2) of this section do not apply, since all positions of the straddle that contained the loss position were disposed of.

* * * * *

Example (17). On January 2, 1986, A, not a dealer in stock or securities, acquires stock in X Corporation (X stock) and an offsetting put option. On March 3, 1986, A disposes of the X stock at a $10 loss. On March 10, 1986, A disposes of the put option at a $10 gain. On March 14, 1986, A acquires new X stock that is substantially identical to the X stock disposed of on March 3, 1986. A holds the X stock to year-end. Under these circumstances, the $10 loss will be disallowed for 1986 under paragraph (a)(1) of this section because A, within a period beginning 30 days before March 3, 1986 and ending 30 days after such date, acquired stock substantially identical to the X stock disposed of.

Example (18). On June 2, 1986, A, not a dealer in stock or securities, acquires stock in X Corporation (X stock). On September 2, 1986, A disposes of the X stock at a $100 loss. On September 15, 1986, A acquires new X stock that is substantially identical to the X stock disposed of on September 2, 1986, and an offsetting put option. A holds these straddle positions to year-end. Under these circumstances, section 1091, rather than section 1092(b), will apply to disallow the $100 loss for 1986 because the loss was not sustained from the disposition of a position that was part of a straddle. See paragraph (e) of this section.

Example (19). On November 1, 1985, A, not a dealer in stock or securities, acquires stock in Y Corporation (Y stock) and an offsetting put option. On November 12, 1985, there is $20 of unrealized gain in the put option and A disposes of the Y stock at a $20 loss. By November 15, 1985, the value of the put option has declined eliminating all unrealized gain in the position. On November 15, 1985, A acquires a second Y stock position that is substantially identical to the Y stock disposed of on November 12, 1985. At year-end there is no unrecognized gain in the put option or in the Y stock. Under these circumstances, the $20 loss will be disallowed for 1985 under paragraph (a)(1) of this section because A, within a period beginning 30 days before November 12, 1985 and ending 30 days after such date, acquired stock substantially identical to the Y stock disposed of.

Example (20). Assume the facts are the same as in example (19), and that on December 31, 1986, A disposes of the put option at a $40 gain and there is $20 of unrecognized loss in the Y stock. Under these circumstances, the $20 loss which was disallowed in 1985 also will be disallowed for 1986 under the rules of paragraph (a)(1) of this section because A has not disposed of the stock substantially identical to the Y stock disposed of on November 12, 1985.

Example (21). Assume the facts are the same as in example (19), except that on December 31, 1986, A disposes of the Y stock at a $20 loss and there is $40 of unrecognized gain in the put option. Under these circumstances, A will not recognize in 1986 either the $20 loss disallowed in 1985 or the $20 loss sustained with respect to the December 31, 1986 disposition of Y stock. Paragraph (a)(1) of this section does not apply to disallow the losses in 1986 since the substantially identical Y stock was disposed of during the year (and no substantially identical stock or securities was acquired by A within the 61 day period). However, paragraph (a)(2) of this section applies to disallow for 1986 the $40 of losses sustained with respect to the dispositions of positions in the straddle because there is $40 of unrecognized gain in the put option, an offsetting position to the loss positions.

Example (22). On January 2, 1986, A, not a dealer in stock or securities, acquires stock in X Corporation (X stock) and an offsetting put option. On March 3, 1986, A disposes of the X stock at a $10 loss. On March 17, 1986, A acquires new X stock that is substantially identical to the X stock disposed of on March 3, 1986. On December 31, 1986, A disposes of the X stock at a $5 gain, at which time there is $5 of unrecognized gain in the put option. Under these circumstances, the $10 loss sustained with respect to the March 3, 1986, disposition of X stock will be allowed under paragraph (a)(1) of this section since the substantially identical X stock acquired on March 17, 1986, was disposed of by year-end (and no substantially identical stock or securities were acquired by A within the 61 day period). However, $5 of the $10 loss will be disallowed under paragraph (a)(2) of this section because there is $5 of unrecognized gain in the put option, an offsetting position to the loss position.

Example (23). Assume the facts are the same as in example (22), except that on December 31, 1986, A disposes of the offsetting put option at a $5 loss and there is $5 of unrecognized gain in the X stock acquired on March 17, 1986. Under these circumstances, the $10 loss sustained with respect to the X stock disposed of on March 3, 1986, will be disallowed for 1986 under paragraph (a)(1) of this section. The $5 loss sustained upon the disposition of the put option will be allowed because (1) the rules of paragraph (a)(1) of this section are not applicable; and (2) the rules of paragraph (a)(2) of this section allow the loss, since the unrecognized gain in the X stock ($5) is not in excess of the loss ($10) disallowed under paragraph (a)(1) of this section.

Example (24). On January 2, 1986, A, not a dealer in stock or securities, acquires 200 shares of Z Corporation stock (Z stock) and 2 put options on Z stock (giving A the right to sell 200 shares of Z stock). On September 2, 1986, there is $200 of unrealized gain in the put option positions and A disposes of the 200 shares of Z stock at a $200 loss. On September 10, 1986, A acquires 100 shares of Z stock (substantially identical to the Z stock disposed of on September 2, 1986), and a call option that is offsetting to the put options on Z stock and that is not an option to acquire property substantially identical to the Z stock disposed of on September 2, 1986. At year-end, there is $80 of unrecognized gain in the Z stock position, $80 of unrecognized gain in the call option position, and no unrecognized gain or loss in the offsetting put option positions. Under these circumstances, $40 of the $200 loss sustained with respect to the September 2, 1986 disposition of Z stock will be recognized by A in 1986 under paragraph (a) of this section, as set forth below. Paragraph (a)(1) of this section applies first to disallow $100 of the loss (1/2 of the loss), since 100 shares of substantially identical Z stock (1/2 of the stock) were acquired within the 61 day period. Paragraph (a)(2) of this section then applies to disallow that portion of the loss allowed under paragraph (a)(1) of this section ($200 – $100 = $100) equal to the excess of the total unrecognized gain in the Z stock and call option positions (successor positions to the loss position) ($80 + $80 = $160) over the $100 loss disallowed under paragraph (a)(1) of this section ($160 − $100 = $60; $100 − $60 = $40).

Example (25). Assume the facts are the same as in example (24), except that at year-end there is $110 of unrecognized gain in the Z stock position, $78 of unrecognized gain in the call option position, and $10 of unrecognized gain in the offsetting put option positions. Under these circumstances, $2 of the $200 loss sustained with respect to the September 2, 1986 disposition of Z stock will be allowed in 1986 under paragraph (a) of this section, as set forth below. Paragraph (a)(1) of this section, as set forth below. Paragraph (a)(1) of this section applies first to disallow $100 of the loss (1/2 of the loss) since 100 shares of substantially identical Z stock (1/2 of the stock) were acquired within the 61 day period. Paragraph (a)(2) of this section then applies to disallow that portion of the loss allowed under paragraph (a)(1) of this section ($200 − $100 = $100) equal to the excess of the total unrecognized gain in the Z stock and call option positions (successor positions to the loss position) and the put option positions (offsetting positions to the loss position) ($110 + $78 + $10 = $198) over the $100 loss disallowed under paragraph (a)(1) of this section ($198 − $100 = $98; $100 − $98 = $2).

Example (26). Assume the facts are the same as in example (24), except that at year-end there is $120 of unrecognized gain in the Z stock position, $88 of unrecognized gain in the call option position, and $10 of unrecognized loss in one of the offsetting put option positions. At year-end A disposes of the other put option position at a $10 loss. Under these circumstances, $2 of the $210 loss sustained with respect to the September 2, 1986 disposition of Z stock ($200) and the year-end disposition of a put option ($10) will be allowed in 1986 under paragraph (a) of this section, as set forth below. Paragraph (a)(1) of this section applies first to disallow $100 of the loss from the disposition of Z stock (1/2 of the loss), since 100 shares of substantially identical Z stock (1/2 of the stock) were acquired within the 61 day period. Paragraph (a)(2) of this section then applies to disallow that portion of the loss allowed under paragraph (a)(1) of this section ($210 − $100 = $110) equal to the excess of the total unrecognized gain in the Z stock and call option positions (successor positions to the Z stock loss position, and offsetting positions to the put option loss position) ($120 + $88 = $208) over the $100 loss disallowed under paragraph (a)(1) of this section ($208 − $100 = $108; $110 − $108 = $2).

Example (27). On January 27, 1986, A enters into offsetting long (L1) and short (S1) positions. Neither L1 nor S1 nor any other positions entered into by A in 1986 are stock or securities. On February 3, 1986, A disposes of L1 at a $10 loss. On February 5, 1986, A enters into a new long position (L2) that is offsetting to S1. On October 15, 1986, A disposes of S1 at an $11 loss. On October 17, 1986, A enters into a new short position (S2) that is offsetting to L2. On December 30, 1986, A disposes of L2 at a $12 loss. On December 31, 1986, A enters into a new long position (L3) that is offsetting to S2. At year-end, S2 has an unrecognized gain of $33. Paragraph (a)(1) of this section does not apply since none of the positions were shares of stock or securities. However, all $33 ($10 + $11 + $12) of the losses sustained with respect to L1, S1 and L2 will be disallowed under paragraph (a)(2) because there is $33 of unrecognized gain in S2 at year-end. The $10 loss from the disposition of L1 is disallowed because S2 is or was an offsetting position to a successor long position (L2 or L3). The $11 loss from the disposition of S1 is disallowed because S2 is a successor position to S1. The $12 loss from the disposition of L2 is disallowed because S2 was an offsetting position to L2.

Par. 3. Paragraph (d) of §1.1092(b)-2T is amended by adding after the last sentence the words "Similarly, the effect of daily marking-to-market provided under §1.1092(b)-4T(c) will be disregarded for purposes of section 851(b)(3)."

Par. 4. Paragraph (n) of §1.1092(b)-5T is revised, and new paragraphs (p) and (q) are added to read as set forth below:

§1.1092(b)-5T Definitions (temporary).

* * * * *

(n) *Successor position.* The term "successor position" means a position ("P") that is or was at any time offsetting to a second position if—

(1) The second position was offsetting to any loss position disposed of; and

(2) P is entered into during a period commencing 30 days prior to, and ending 30 days after, the disposition of the loss position referred to in paragraph (n)(1) of this section.

* * * * *

(p) *Substantially identical*. The term "substantially identical" has the same meaning as substantially identical in section 1091(a).

(q) *Securities*. The term "security" means a security as defined in section 1236(c).

There is need for immediate guidance with respect to the provisions contained in this Treasury decision. For this season, it is found impracticable to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved December 20, 1985.

RONALD A. PEARLMAN,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on January 13, 1986, 8:45 a.m., and published in the issue of the Federal Register for January 15, 1986, 51 F.R. 1785)

Section 2501.—Imposition of Tax [Gift]

26 CFR 25.2501-1: Imposition of tax.

Tax consequences of a transfer of real property and a subsequent adjustment based on the Service's valuation of the property. See Rev. Rul. 86-41, below.

Section 2503.—Taxable Gifts

26 CFR 25.2503-3: Future interest in property. (Also Sections 2501, 2511; 25.2501-1, 25.2511-2.)

Transfers; real property; adjustment to portion transferred based on Service's valuation. The value of a gift will be determined without regard to an adjustment clause that provides for the recharacterization of the transaction depending on the Service's valuation of the property.

Rev. Rul. 86-41

ISSUE

What are the federal gift tax consequences in the two situations described below where a donor transfers a specified portion of real property under terms that provide for an adjustment to the portion transferred depending on the determination by the Internal Revenue Service of the value of the property for federal gift tax purposes?

FACTS

Situation 1.

In 1982, *A* transferred an interest in a tract of income producing real property to *B*. Under the deed of transfer, *B* received a one-half undivided interest in the tract. However, the deed further provided that if the one-half interest received by *B* were ever determined by the Internal Revenue Service to have a value for federal gift tax purposes in excess of $10,000, then *B*'s fractional interest would be reduced so that its value equaled $10,000. Under local law the adjustment clause operated as a condition subsequent. Thus, if the Service determined that a gift was made in excess of $10,000, the adjustment clause would effectively reconvey to *A* a fractional share of the tract of real property sufficient to reduce the value of *B*'s interest to $10,000 as of the date of the gift.

On *A*'s federal gift tax return, *A* reported that the fair market value of the one-half interest transferred by gift to *B* was $10,000 (one-half the value of the entire tract), and applied the annual exclusion against the gift. On examination of *A*'s 1982 federal gift tax return, it was determined that the fair market value of a one-half interest in the tract subject to the transfer to *B* was $15,000 rather than $10,000.

Situation 2.

The facts are the same as in *Situation 1*, except that *B* was not required to reconvey any property to *A*. Rather, the transfer contained the condition that if the Internal Revenue Service determined that *B* received a gift in excess of $10,000, *B* would transfer to *A* consideration equal to the amount of the excess.

LAW AND ANALYSIS

Section 2501 of the Internal Revenue Code imposes a tax on the transfer of property by gift. Section 2511(a) provides that the gift tax applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible, or intangible. Section 25.2511-2(a) of the Gift Tax Regulations states that the gift tax is not imposed upon the receipt of the property by the donee but rather is an excise upon the donor's act of transfer.

Section 2503(b) of the Code provides that a donor may exclude from his or her taxable gifts the first $10,000 of gifts of present interest in property made to each donee during the calendar year. Under section 25.2503 of the regulations, a "present interest" in property is defined as an unrestricted right to the immediate use, possession, or enjoyment of property or the income from property.

Rev. Rul. 65-144, 1965-1 C.B. 442, holds that if the terms of a trust provide that the trust terms will be substantially modified to the extent necessary to qualify the transfer in trust for the gift tax charitable deduction under section 2522 of the Code, those terms providing for modification are considered ineffective for federal gift tax purposes. Gifts subject to conditions subsequent of the kind considered in Rev. Rul. 65-144 tend to discourage the enforcement of federal gift tax provisions, because operation of the provisions would either defeat the gift or otherwise render examination of the return ineffective. See also *Commissioner v. Procter*, 142 F.2d 824 (4th Cir. 1944), *cert. denied*, 323 U.S. 756 (1944). The Service, accordingly, will not give effect to such clauses and will consider the terms of the gift as unmodified for federal tax purposes.

In *Situations 1* and *2*, the facts demonstrate that *A* intended to make a gift to *B* of a present one-half interest in the property. In both cases, the purpose of the adjustment clause was not to preserve or implement the original, bona fide intent of the parties, as in the case of a clause requiring a purchase price adjustment based on an appraisal by an independent third party retained for that purpose. Rather, the purpose of the clause was to recharacterize the nature of the transaction in the event of a future adjustment to *A*'s gift tax return by the Service. As in Rev. Rul. 65-144, the terms of the deed of transfer to *B* providing for the reduction of the portion transferred would tend to discourage the examination of returns and the collections of tax and therefore are ineffective for federal gift tax purposes. Because the reduction provision is ineffective for federal gift tax purposes, *A* has made a gift of a present one-half interest in the property, the first $10,000 of which qualifies for the annual exclusion under section 2503 of the Code. The value of the gift is $15,000, the fair market value of a one-half interest in the tract as determined on examination. The fact that, in *Situation 2*, the adjustment of the gift was to be made by recharacterizing the transfer as a part-gift/part-sale is irrelevant.

HOLDING

In both *Situations 1* and *2*, if the donor transfers a specified portion of real property under terms that provide for a recharacterization of the transaction depending on the Service's valuation of the property for federal gift tax purposes, the adjustment clause will be disregarded for federal tax purposes. Consequently, in both cases the value of the gift will be determined without regard to the adjustment clause and the first $10,000 in the value of the gift, as so determined, will qualify for the annual exclusion from gift tax.

Section 2511.—Transfers in General

26 CFR 25.2511-2: Cessation of donor's dominion and control.

Tax consequences on a transfer of real property and a subsequent adjustment based on the Service's valuation of the property. See Rev. Rul. 86-41, page 9.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.105 Examination of returns and claims fo refund, credit, or abatement; determination of correct tax liability.
(Also Part I, Section 168.)

Rev. Proc. 86-14

This revenue procedure corrects Rev. Proc. 86-6, 1986-5 I.R.B. 36. Rev. Proc. 86-6 is modified and superseded. These corrections to Rev. Proc. 86-6 are effective as if they had originally appeared in Rev. Proc. 86-6. Rev. Proc. 86-6 should have read as follows:

[Sections 1 through 4.01 are unchanged.]

.02 The revised recovery rates for 19-year real property are presented by the tables in section 5. Except with respect to low-income housing, these tables adopt the mid-month convention, which is required by section 168(b)(2)(A) of the Code. Under the mid-month convention, real property placed in service by the taxpayer at any time during a particular month is treated as placed in service in the middle of that month. Thus, only one-half month's cost recovery is permitted for the month the property is placed in service. A similar convention is to be applied with respect to dispositions prior to the end of the recovery period. Thus, one-half month's cost recovery is also permitted for the month of disposition. For low-income housing, a full-month convention is used. *See* section 168(b)(4)(A). Under the full-month convention, real property placed in service by the taxpayer at any time during a particular month is treated as placed in service on the first day of that month. Thus, a full month's cost recovery is permitted for the month the property is placed in service. In the case of a disposition at any time during a particular month prior to the end of the recovery period, no cost recovery is permitted for the month of disposition.

[Sections 4.03 through 4.14 are unchanged. Section 5 is unchanged except for the italicized numbers in tables 6 and 7 as follows:]

5. 19-Year Real Property For Which an Optional 45-Year Straight Line Method is Elected (Assuming Mid-Month Convention)

If the Recovery Year is:	And the Month in the First Recovery Year the Property is Placed in Service is:											
	1	2	3	4	5	6	7	8	9	10	11	12
	The applicable recovery percentage is:											
7	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
8	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
9	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
10	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
11	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
12	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
13	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
14	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
15	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
16	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
17	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
18	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
19	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
20	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
21	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
22	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
23	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
24	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
25	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
26	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
27	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
28	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
29	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
30	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
31	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
32	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
33	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
34	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
35	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
36	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
37	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2

5. 19-Year Real Property For Which an Optional 45-Year Straight Line Method is Elected (Assuming Mid-Month Convention)

If the recovery year is:	And the Month in the First Recovery Year the Property is Placed in Service is: 1	2	3	4	5	6	7	8	9	10	11	12
	The applicable recovery percentage is:											
38	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
39	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
40	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
41	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
42	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
43	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
44	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
45	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
46	0.1	0.3	0.4	0.6	0.8	1.0	1.2	1.4	1.6	1.7	1.9	2.1

6. Low-income Housing (15-Year 200% Declining Balance) (Assuming No Mid-Month Convention)

If the Recovery Year is:	And the Month in the First Recovery Year the property is Placed in Service is: 1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	13.3	12.1	11.1	*10.0*	8.9	7.8	6.6	5.6	4.4	3.3	2.2	1.1
2	11.6	11.7	11.9	12.0	12.1	12.3	12.5	12.6	12.7	12.9	*13.0*	13.2
3	10.0	10.1	10.2	10.4	10.5	10.7	10.8	10.9	11.1	11.2	11.3	11.4
4	8.7	8.8	8.9	9.0	9.1	9.2	9.3	9.5	9.6	9.7	9.8	9.9
5	7.5	7.6	7.7	7.8	7.9	8.0	8.1	8.2	8.3	8.4	8.5	8.6
6	6.5	6.6	6.7	6.8	6.9	6.9	7.0	7.1	7.2	7.3	7.4	7.4
7	5.7	5.7	5.8	5.9	5.9	6.0	6.1	6.1	6.2	6.3	6.4	6.5
8	4.9	5.0	5.0	5.1	5.2	5.2	5.3	5.3	5.4	5.5	5.5	5.6
9	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.7	4.8	4.8
10	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
11	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
12	4.5	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
13	4.5	4.5	4.6	4.5	4.6	4.6	4.6	4.6	4.6	4.5	4.6	4.6
14	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.6	4.6	4.5	4.5	4.5
15	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5
16	0.0	0.4	0.7	1.1	1.5	1.9	2.3	2.6	3.0	3.4	3.7	4.1

7. Low-income Housing Used Predominantly Outside the U.S. (35-year 150% Declining Balance) (Assuming No Mid-Month Convention)

If the Recovery Year is:	And the Month in the First Recovery Year the Property is placed in Service is: 1	2	3	4	5	6	7	8	9	10	11	12
	The applicable percentage is:											
1	4.2	3.9	3.6	3.2	2.8	2.5	2.1	1.8	1.4	1.1	0.7	0.4
2	4.1	4.1	4.1	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.3	4.3
3	3.9	3.9	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.1	4.1	4.1
4	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.9	3.9	3.9	3.9
5	3.6	3.6	3.6	3.6	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7
6	3.4	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.6	3.6	3.6
7	3.3	3.3	3.3	3.3	3.3	3.4	3.4	3.4	3.4	3.4	3.4	3.4

7. Low-income Housing Used Predominantly Outside the U.S. (35-year 150% Declining Balannce) (Assuming No Mid-Month Convention)

And the Month in the First Recovery Year the Property is placed in Service is:

The applicable percentage is:

If the Recovery year is:	1	2	3	4	5	6	7	8	9	10	11	12
8	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.3	3.3	3.3	3.3
9	3.0	3.0	3.0	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.1
10	2.9	2.9	2.9	2.9	2.9	2.9	3.0	3.0	3.0	3.0	3.0	3.0
11	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.9	2.9
12	2.6	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.8
13	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
14	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
15	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
16	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
17	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
18	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
19	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
20	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
21	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
22	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
23	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
24	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
25	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
26	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
27	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
28	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
29	2.6	2.5	2.5	2.5	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
30	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
31	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5

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26 CFR 601.201: Rulings and determination letters.
(Also Part I, Sections 331, 337; 1.331-1, 1.337-1.)

Rev. Proc. 86-16

SECTIONS 331 AND 337 CHECKLIST QUESTIONNAIRE

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SECTION 1. PURPOSE

The purpose of this revenue procedure is to update Rev. Proc. 81-52, 1981-2 C.B. 625, which sets forth in a checklist questionnaire the information that must be included in a request for a ruling under section 337 of the Internal Revenue Code (and its related provision, section 331 of the Code) relating to the nonrecognition of gain or loss on sales or exchanges in connection with a complete liquidation of a corporation (Distributor). This checklist questionnaire does not deal with the special rules of section 337(e), relating to involuntary conversions, or of section 337(g), relating to cases under title 11 of the United States Code, or a receivership, foreclosure, or similar proceeding in a federal or state court.

SEC. 2. BACKGROUND

The Internal Revenue Service receives many requests for rulings in which the information relating to the proposed transaction is not sufficient to permit a determination to be made. In those cases, it is necessary to obtain additional facts from the taxpayer before the request for a letter ruling can be considered. Obtaining these additional facts is time consuming for both Service personnel and taxpayers and delays issuance of the ruling letter.

This checklist will facilitate the filing and processing of requests for rulings under sections 331 and 337 of the Code by showing specific information and representations to be included so that the requests will be as complete as possible when initially filed. Because the information and representations necessary to rule on a particular transaction depend upon all the facts and circumstances, information or representations in addition to those set forth in this revenue procedure may be required.

The authority and general procedures of the National Office of the Internal Revenue Service and of the Office of the District Directors of Internal Revenue with respect to the issuance of letter rulings and determination letters are outlined in Rev. Proc. 86-1, 1986-1 I.R.B. 6. See also, Rev. Proc. 86-3, 1986-1 I.R.B. 26, relating to areas in which advance rulings generally will not be issued. These revenue procedures, along with the present checklist revenue procedure, are subject to periodic updating by the Service. Therefore, careful attention should be given to ensure usage of the most current revenue procedures.

Careful attention to all requirements of these revenue procedures will aid in the timely processing of letter ruling requests.

SEC. 3. CHANGES

.01 Section 1 is modified to indicate that the purpose of the revenue procedure is to update Rev. Proc. 81-52.

.02 Section 2 is modified to state that representations are now required, and to update references to revenue procedures cited.

.03 Section 4 is substantially altered, with numerous sections being renumbered and relocated in the interest of simplification. The taxpayer must now submit standard representations using the precise language specified herein, or submit an explanation why the representations cannot be made in the requested form. Sections 4.021, 4.023, 4.025, 4.026, 4.027, 4.031, 4.032, 4.041 and 4.045 are modified accordingly. To properly reflect applicable changes, some citations to Code sections and to revenue rulings and procedures have been added or deleted. Changes include:

1 Section 4.012 now requires taxpayers to submit information concerning any prior ruling requests submitted by the taxpayer (or predecessor) that were withdrawn in which the identical or similar issue was present.

2 Section 4.022 is added to request information concerning the liquidation of a subsidiary formerly requested in section 4.037(a). Reference to Rev. Rul. 69-172, 1969-1 C.B. 99, is deleted.

3 Section 4.023(a)(1)(B) is added to request information concerning convenants not to compete.

4 Section 4.033 has been modified to show changes in the recapture provisions.

5 Section 4.035 has been added to request information regarding advance payments received by Distributor.

6 Section 4.046 requires taxpayers to state whether the liquidation of Distributor will be carried out by the use of a statutory merger.

7 Section 4.05 requires taxpayers to list the specific rulings being requested and the authorities supporting the rulings.

.04 Section 5 is modified to substitute Associate Chief Counsel (Technical) for Assistant Commissioner (Technical), and CC:C:R for T:C:R.

.05 Section 6 is modified to state that Rev. Proc. 81-52 is superseded.

SEC. 4. INFORMATION TO BE INCLUDED IN REQUESTS FOR RULINGS UNDER SECTIONS 331 AND 337 OF THE CODE

Each of the items in this section should be specifically dealt with in the letter ruling request. If an item is not applicable, so state and briefly explain why. Standard representations are set forth throughout this section and are highlighted by the word "representation" in boldface type. These representations are of equal importance with the other factual information requested herein. The representations function to ensure that specific statutory and judicial requirements and administrative ruling guidelines are satisfied. Each representation set forth in this section should be submitted precisely in the language requested. If a representation cannot be submitted as requested, an explanation must be given. Variations of the language of the representations may delay processing the ruling request and will not be accepted unless reasons satisfactory to the Service are submitted. Submission of the information and representations should follow the format of this revenue procedure as closely as possible, with appropriate descriptive headings. Care must be taken to ensure that all the facts relating to the transaction are submitted.

.01 *Information regarding the liquidating corporation (Distributor).*

1 Identification.—Name, taxpayer identification number, and place and date of incorporation of Distributor.

2 Jurisdiction.—Identify the District Office that will have audit jurisdiction over the return of Distributor (referred to below as "taxpayer"). State whether, to the best knowledge of the taxpayer and the taxpayer's representatives, if any, the identical issue is in a return of the taxpayer (or of a related taxpayer within the meaning of section 267 of the Code, or a member of an affiliated group of which the taxpayer is also a member within the meaning of section 1504) and, if so, whether the issue (1) is being examined by a District Director, (2) has been examined by a District Director and (a) the statutory period of limitation either on assessment or for filing a claim for refund or credit of tax has not expired and (b) a closing agreement covering the issue or liability has not been entered into by a District Director, (3) is being considered by an Appeals Office in connection with the taxpayer's return for an earlier period, (4) has been considered by an Appeals Office and (a) the statutory period of limitation either on assessment or for filing a claim for refund or credit of tax has not expired and (b) a closing agreement covering the issue or liability has not been entered into by an Appeals Office, or (5) is pending in litigation in a case involving the taxpayer or a related taxpayer. The request must contain a statement whether, to the best knowledge of the taxpayer and the taxpayer's representatives, the identical or a similar issue has been (i) submitted to the Service, but withdrawn before a ruling was issued, or (ii) ruled on by the Service to the taxpayer or the taxpayer's predecessor and, if so, when and with what result. If, after the request is filed but before a ruling is issued, the taxpayer knows that an examination of the issue by a District Director has been started, the taxpayer must notify the National Office of this action. If a return is filed before a ruling is received from the National Office concerning the issue that is the subject of the request for ruling, a copy of the request must be attached to the return. This alerts the District Office and avoids premature District action on the issue.

3 Business.—Provide the following information about the Distributor: (i) a brief description of its businesses, (ii) its overall method of accounting, and (iii) its tax year.

4 Description of Distributor's capital structure and ownership of Distributor's stock.

(a) Description of capital structure.—Furnish a complete description of each class of Distributor's outstanding stock (or other evidence of equity ownership) setting forth the rights and privileges of each class, including voting or nonvoting rights, dividend and liquidation preferences or limitations, and whether classified as common or preferred stock. Also describe all other outstanding interests (bonds, debentures, notes, warrants, options, etc.), and briefly explain why each of these items should or should not be considered a stock interest.

(b) Ownership of stock.—State the total number of shares outstanding for each class of stock (or other equity) in Distributor, and the number of shares and percentage of each class of stock (or other equity) owned by each shareholder. However, if there are more than 25 shareholders, the statement in the preceding sentence may be limited by listing only those shareholders owning, directly or indirectly (within the meaning of section 318 of the Code), 5 percent or more of any class of stock and then stating the total number of remaining shareholders together with the total number of shares and percentages which these remaining shareholders own of each class of stock. State whether 80 percent or more of the voting power and stock in Distributor (within the meaning of section 332(b)(1)) is held by a corporate shareholder (see section 337(c) of the Code and section 1.1502-34 of the Income Tax Regulations).

5 Filing status.—State whether Distributor is a member of an affiliated group of corporations making a consolidated return and, if so, identify the common parent of the group.

.02 *Information regarding plan of liquidation.*

1 The plan of liquidation.

(a) Formal plan.—State whether the plan has been, or will be, adopted by Distributor's directors and shareholders and give the date, or expected date, of approval or adoption. See Rev. Rul. 57-140, 1957-1 C.B. 118.

(b) Prior informal plan.—Furnish any information which indicates that a plan of liquidation may have been informally adopted prior to the date set forth in 4.021(a) above. The information is not restricted to, but might include, facts indicating an informal agreement to liquidate by a significant number of shareholders, or the sale or distribution of a substantial portion of Distributor's assets prior to the formal date of adoption of the plan. See section 1.337-2(b) of the regulations and Rev. Rul. 65-235, 1965-2 C.B. 88. Describe any distributions to Distributor's shareholders during the 2-year period prior to the adoption of the plan of liquidation. State whether Distributor sold or otherwise disposed of any assets at a loss for federal income tax purposes, other than in the ordinary course of business, within the 2-year period preceding the date of adoption of the plan of liquidation. If so, furnish details, including the cost basis of each item and the amount for which each item was sold. If no sale or distribution of Distributor's assets has occurred, submit the following REPRESENTATION: *During the 2-year period prior to the adoption of the plan of liquidation, Distributor will not have sold any of its property of the type defined in section 337(b) of the Code, except in the ordinary course of business.*

(c) Rescission of a prior plan.—State whether Distributor has ever adopted a plan of liquidation, and, if so, provide full particulars regarding the abandonment or rescission of the plan. In this regard, indicate when Form 966, *Corporate Dissolution or Liquidation,* was filed in connection with the adoption of the plan, and provide pertinent dates and reasons for abandoning or rescinding the prior plan. If no prior plans were adopted submit the following REPRESENTATION: *No formal or informal plan of liquidation has ever been adopted by Distributor, except for the present plan which was [or will be] adopted on [date].*

2 Liquidation of Distributor's subsidiary.—State whether any subsidiary of Distributor was, or will be, liquidated in connection with the liquidation of Distributor. If so, submit details. If a ruling is requested that such liquidation will qualify under section 332 of the Code, see Rev. Proc. 81-68, 1981-2 C.B. 723.

3 Sales or other dispositions of assets pursuant to the plan.

(a) Sales pursuant to the plan.

(1) General description.—Describe the assets to be sold pursuant to the plan of liquidation and the consideration to be received for the assets. If a sales agreement has not yet been entered into, approximate the assets to be sold and the consideration to be received (if reasonably possible to do so). For sales pursuant to the plan, submit copies of sales contracts (or agreements in principal regarding these sales). State whether sales contracts are executory, contingent, or consummated.

(A) Stock in trade.—Briefly describe the stock in trade or inventory (as defined in section 1.337-3(a) of the regulations) of Distributor, and state whether it will be sold. If substantially all the stock in trade or inventory of Distributor will be sold to one person in one transaction, furnish details concerning this sale. See section 337(b) of the Code and section 1.337-3 of the regulations.

(B) Covenants not to compete.—If consideration is being received by Distributor or its shareholders for an agreement not to compete, provide full details concerning the agreement and the reporting of proceeds.

(2) Method of payment.—State the expected method of payment for the assets being sold. Summarize all pertinent portions of existing sales contracts (or agreements in principal regarding sales) relating to the method of payment.

(3) Information regarding each purchaser of Distributor's assets (Purchaser).—Identify each Purchaser, if known, and indicate whether Purchaser is an individual, partnership, corporation, or other entity. State whether there was, or will be, any transfer or sale of Distributor's assets to an entity that is wholly or partly owned by Distributor or Distributor's shareholders. If so, furnish full details concerning the transaction, including the type and percentage of the ownership interests involved. In this regard, note that section 4.0117 of Rev. Proc. 86-3 indicates the Service will not ordinarily issue rulings on the application of section 337 of the Code to a corporation upon the sale of property (in connection with its liquidation) to another corporation, where more than a nominal amount of the stock (that is, more than 20 percent in value) of both the selling corporation and the purchasing corporation are owned by the same shareholders. Submit the following REPRESENTATION: *The liquidation of Distributor will not be preceded or followed by the reincorporation in, or transfer or sale to, a recipient corporation (Recipient) of any of the business or assets of Distributor, if persons holding more than 20 percent in value of the stock in Distributor also hold more than 20 percent in value of the stock in Recipient. For purposes of this representation, ownership has been determined by application of the constructive ownership rules of section 318, as modified by section 304(c)(3).* Compare Rev. Ruls. 84-2, 1984-1 C.B. 92, and 61-156, 1961-2 C.B. 62.

(b) Other dispositions of assets pursuant to the plan.—Describe any other disposition of assets (for example, involuntary conversions), which will occur during the prescribed liquidation period, which the Distributor intends to treat as sales or exchanges pursuant to section 337 of the Code. Furnish complete details concerning these items.

4 Distribution of assets.

(a) Assets distributed directly to shareholders.

(1) Description of assets.—Describe the assets to be distributed directly to Distributor's shareholders.

(2) Dates.—Indicate when this distribution will be made.

(b) Assets distributed to an escrow or partnership on the liquidation of Distributor.

(1) Description of assets.—Describe the assets to be distributed to the escrow or partnership.

(2) Description of escrow or partnership.—Fully describe any escrow or partnership, including its partners and operation, receiving assets on Distributor's liquidation.

(3) Dates.—Indicate when this distribution will be made.

(c) Assets distributed to a liquidating trust.—State whether the plan of liquidation requires the use of a liquidating trust, or if the use of a liquidating trust is otherwise contemplated. See Rev. Ruls. 80-150, 1980-1 C.B. 316, and 72-137, 1972-1 C.B. 101.

(1) Description of assets.—Describe the assets to be distributed to the liquidating trust.

(2) The trust.—Describe whether the use of the trust is permitted under applicable law, the powers and identity of the trustee, and the time period during which the trust will remain in existence.

(3) Dates.—Indicate when this distribution will be made.

(4) Reasons.—Give the reasons for using a liquidating trust.

(5) Classification of the trust.—In issuing a ruling under sections 331 and 337 of the Code in a situation where a liquidating trust is used, it is the practice of the Service to state in the ruling letter that the ruling is valid only if the trust is not an association taxable as a corporation under section 301.7701 of the Procedure and Administration Regulations. However, if Distributor desires a ruling concerning the classification of the trust under section 301.7701, the ruling request should so indicate and it should include an additional copy of the entire ruling request. See Rev. Proc. 82-58, 1982-2 C.B. 847.

5 Assets retained.

(a) Description of assets.—Fully describe any assets to be retained by Distributor subsequent to the 12-month period beginning on the date of adoption of the plan of liquidation. See section 1.337-2(b) of the regulations. If no assets will be retained, submit the following REPRESENTATION: *All assets of Distributor will be distributed in complete liquidation of Distributor within the 12-month period beginning on the date of adoption of the plan of liquidation.*

(b) Reason for retention.—If assets will be retained beyond the 12-month period, set forth the reasons for their retention. Specifically, state whether any assets will be retained to satisfy claims of any shareholders with respect to their stock.

(c) Description of claims.—Describe the claims to be satisfied with the retained assets.

(d) Period of retention.—State whether the balance of the assets retained will be distributed as soon as all claims are satisfied.

6 Redemption and cancellation of Distributor's stock.

(a) Redemption of all stock.—State whether all the outstanding stock of Distributor will be redeemed and cancelled.

(b) Non pro rata redemption.—If the property to be used in redemption of Distributor's stock will not be distributed in exact proportion with the percentage of shares owned by each shareholder, submit reasons and details. See Rev. Rul. 79-10, 1979-1 C.B. 140.

(c) Shareholder and Distributor in dual capacity.—Submit the following REPRESENTATION: *No part of the consideration to be received by any shareholder of Distributor will be received by the shareholder as a creditor, employee, or in some capacity other than that of a shareholder of Distributor.*

7 Status of liquidation.

(a) Status.—Submit the following REPRESENTATION: *Pursuant to the plan of complete liquidation, Distributor will cease to be a going concern and its activities will be limited to the winding up of its affairs, paying its debts, and distributing any balance of its assets to its shareholders.* (See Rev. Rul. 60-50, 1960-1 C.B. 150.) If there is more than one liquidating distribution, furnish the following REPRESENTATION: *The status of liquidation will exist at the time of the first liquidating distribution and will continue until the final liquidating distribution is made.*

(b) Fair market value of assets.—Submit the following REPRESENTATION: *The fair market value of Distributor's assets will exceed its liabilities both on the date of adoption of the plan of liquidation and at the time the first liquidating distribution is made.*

(c) Corporate charter.—State whether Distributor intends to abandon its corporate charter. See Rev. Ruls. 60-50, 1960-1 C.B. 150, and 54-518, 1954-2 C.B. 142.

.03 *Recognition of gain or income to Distributor.*

In order to determine whether gain or income will be recognized to Distributor upon the distribution of property, submit statements or representations with respect to the following:

1 Unreported or anticipatory assignment of income.—State whether Distributor has any assets which represent earned but unreported income to Distributor, such as receivables being reported on a cash basis, unfinished construction contracts, commissions due, or other similar assets. If Distributor has any assets representing earned but unreported income, state whether Distributor will distribute these assets to its shareholders or dispose of them in some other manner. If none of these assets are being distributed, submit the following REPRESENTATION: *No distribution of assets representing earned but unreported income will be made by Distributor to its shareholders in the liquidation.*

2 Reserve for bad debts.—Submit the following REPRESENTATION: *Distributor does [or does not] maintain a reserve for bad debts.* See Rev. Rul. 78-279, 1978-2 C.B. 135.

3 Installment obligations and recapture provisions.—State whether Distributor is selling, distributing to its shareholders, or otherwise disposing of (i) any installment obligations (section 453B of the Code), (ii) any property described in the recapture provisions of the Code including, but not limited to, sections 47, 291(a), 337(f), 341(f), 617(d), 897(d), 904(f), 1245(a), 1248(f), 1250(c), 1252(a), 1254, or 1255, (iii) any property for which the taxpayer obtained a deduction (See *Hillsboro National Bank v. Commissioner*, 460 U.S. 370 (1983); Rev. Rul. 74-396, 1974-2 C.B. 106; Rev. Rul. 61-214, 1961-2 C.B. 60), or (iv) any property described in sections 1256 or 1276.

If installment obligations will be distributed, describe the nature and terms of the obligations. State how the shareholders intend to treat payments received on the installment obligations. State the effect of sections 453(h) and 453B(d)(2) of the Code on Distributor's distribution.

4 Partnership interests.—State whether Distributor will distribute to the shareholders any partnership interests representing property specified in sections 4.031, 4.032, or 4.033, above. See section 386 of the Code.

5 Advance payments.—State whether Distributor has any items constituting prepaid subscription income, prepaid dues income, advance payments for goods, or payments received for services to be performed in the future. See sections 455 and 456 of the Code, section 1.451-5 of the regulations, and Rev. Proc. 71-21, 1971-2 C.B. 549.

.04 *General*

1 Other transactions.—Submit the following REPRESENTATION: *The liquidating distribution(s) described in this ruling request is an isolated transaction and is not related to any other past or future transaction.* Alternatively, state whether there have been, or will be, any related transactions, and, if so, briefly describe these other transactions and fully explain their relationship to, and impact on, the present transaction. See section 9.06 of Rev. Proc. 86-1.

2 Financial statements.—Submit a copy of the most recent balance sheet of Distributor.

3 Copy of plan.—Submit a copy of the plan of liquidation adopted, or to be adopted.

4 Collapsible corporation.—In issuing a ruling under sections 331 and 337 of the Code, it is the practice of the Service to state in the ruling letter that the ruling under section 331 is valid only if section 341(a) is not applicable and that the ruling under section 337 is valid only if Distributor is not a collapsible corporation as defined in section 341(b) (or is not considered a collapsible corporation pursuant to section 341(e)(4)). See Rev. Proc. 86-3, 1986-1 I.R.B. 26, section 4.0117.

5 Section 333 of the Code.—Submit the following REPRESENTATION: *The shareholders of Distributor will not elect to have section 333 of the Code apply to this liquidation.* See section 337(c)(1)(B).

6 Applicability of merger statutes.—State whether the liquidation of Distributor will be carried out by the use of a statutory merger.

7 Additional statements.—See Rev. Proc. 86-1 for additional information

and statements that must be submitted with all ruling requests, including statements required under sections 9.02 and 9.09 (relating to instructions to taxpayers).

8 Requested Rulings.—List the rulings being requested in the exact wording desired, and provide statutory, regulatory, or other authority for their issuance.

9 Taxpayer's memorandum.—Submit the information required by section 9.08 of Rev. Proc. 86-1 (relating to relevant authorities regarding the tax results of the transaction).

SEC. 5. INQUIRIES

Inquiries in regard to this revenue procedure should refer to its number and should be addressed to the Associate Chief Counsel (Technical), Attention: CC:C:R, Internal Revenue Service, Washington, D.C. 20224.

SEC. 6. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 81-52 is superseded.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Definition of the Term "Principal User"

LR-59-74

SUMMARY: This document contains proposed regulations which would define the term "principal user" for purposes of paragraphs (6) and (15) of section 103(b) of the Internal Revenue Code of 1954. The regulations would affect issuers, holders, and recipients of the proceeds of industrial development bonds issued under section 103(b)(6) of the Code.

DATES: Written comments must be delivered or mailed by April 22, 1986. The amendments are proposed to be effective after August 20, 1986 in determining the tax-exempt status of obligations issued after August 20, 1986.

ADDRESS: Send comments to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-59-74), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: John A. Tolleris of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (Telephone: 202-566-3590, not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed clarifying amendments to the Income Tax Regulations (26 CFR Part 1) under section 103(b)(6) of the Internal Revenue Code of 1954.

EXPLANATION OF PROVISIONS

The amendments clarify the term "principal user" for purposes of applying the provisions of Code section 103(b)(6) and (15) and the regulations thereunder with respect to small issues of industrial development bonds. Section 103(b)(6) provides, among other things, that an issue of $1 million or less of industrial development bonds financing the acquisition, construction, reconstruction, or improvement of land or property of a character subject to the depreciation allowance (or an issue to redeem such a prior issue) is not exempt from Federal taxation when the issue in question combined with the outstanding face amount of prior issues financing certain similar facilities exceeds $1 million; the facilities which are taken into account for this purpose are those the "principal user" of which is or will be the same or two or more related persons, and which are located within the same county or incorporated municipality.

Section 103(b)(6) also provides that, if an issuer makes the necessary election, the limit for an exempt small issue of industrial development bonds is increased from $1 million to $10 million. In such case, however, certain other amounts must also be aggregated with the issue of obligations in question for purposes of determining whether the $10 million limitation has been exceeded and whether the interest upon the issue of obligations in question is thus subject to Federal income taxation. The additional amounts to be taken into account are certain capital expenditures, made within a 6-year period beginning 3 years before the date of issue of the obligations in question and ending 3 years after the date of issue, with respect not only to the facility financed by the issue in question, but also with respect to other facilities within the same county or incorporated municipality of which the "principal user" is or will be the same person or a person related to the "principal user" of the facility financed with the issue of obligations in question.

The proposed regulations provide, in general, that the principal users are persons who for tax purposes currently hold more than a 10-percent ownership interest in a facility. In addition, lessees or subleasees who use a sufficiently valuable portion of the facility pursuant to a sufficiently long-term lease are also principal users. Persons with interests comparable to that of an owner or lessee who is a principal user and some purchasers of the output of certain facilities are also treated as principal users.

The proposed regulations provide that, when a facility has more than one principal user, certain issues of obligations with respect to all principal users must be aggregated with the issue of obligations in question for purposes of determining whether the $1 million or $10 million limitation has been exceeded. Similarly, if the $10 million limitation has been elected by the issuer, certain capital expenditures with respect to all principal users must also be aggregated to determine whether the $10 million limitation has been exceeded.

For purposes of aggregating issues of obligations or capital expenditures of persons who are principal users, only issues and capital expenditures with respect to persons who are principal users of the facility before the expiration of the test period described in section 103(b)(15)(D) are aggregated. Accordingly, if a person who is a principal user of a facility financed by an exempt small issue becomes the principal user of another facility financed by a second exempt small issue more than 3 years after the later of the date of the second issue or the date the facility financed by the second issue was placed in service, the two issues are not aggregated. Similarly, capital expenditures during the 6-year period described in section 103(b)(6)(D)(ii) with respect to a principal user are not taken into account if that person does not become a principal user of the facility until more than 3 years after the later of the date of the issue or the date the facility financed by the issue is first placed in service.

The test-period concept was adopted for purposes of section 103(b)(6) for reasons of administrative convenience. The statutory reference to a person who "is or will be" a principal user could be construed as referring to a person who at any time is a principal user; as referring only to a person who is or is about to be a principal user on the date of issuance; or as referring to a person who becomes a principal user within some intermediate time period. In adopting the test-period concept, the Service attempted to reach a result which gives effect to the statutory language while also being administrable. Adoption of the test period described in section 103(b)(15)(D) serves the additional function of limiting the period for determination of the principal user status to a single period for purposes of both paragraphs (6) and (15) of section 103(b).

The proposed regulations provide special rules of for exempt persons, *i.e.*, State and local governments and organizations that are tax-exempt under section 501(c)(3), that are principal users of facilities financed with exempt small issues of industrial development bonds. For purposes of determining whether the small-issue limitation has been exceeded with respect to any facility of which an exempt person is a principal user, certain industrial development bonds issued with respect to the exempt person and, for purposes of the $10 million limitation, certain capital expenditures must be aggregated with the issue in question. This does not include capital expenditures with respect to other facilities used by the exempt person in an activity other than an unrelated trade or business (as defined by section 513).

REGULATORY FLEXIBILITY ACT

The Secretary of the Treasury has certified that this proposed rule will not have a significant impact on a substantial number of small entities because the economic and any other secondary or incidental impact flows directly from the underlying statute. A regulatory flexibility analysis, therefore, is not required under the Regulatory Flexibility Act (5 U.S.C. chapter 6).

NON-APPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

COMMENTS—PUBLIC HEARING

Before adoption of these proposed regulations, consideration will be given to any written comments that are submitted (preferably seven copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held * * * [on Wednesday, June 4, 1986].

DRAFTING INFORMATION

The principal author of these proposed regulations is John A. Tolleris of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Proposed amendments to the regulations

The proposed amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 2. Section 1.103-10 is amended by adding a new sentence after the second sentence of paragraph (b)(2)(i); by deleting "*(e)*" and adding "*(f)*" in lieu thereof in the first sentence of paragraph (b)(2)(iv) and by adding a new subdivision *(f)* at the end of subdivision (iv) thereof; by adding two new sentences after the first sentence of paragraph (d)(1); by revising paragraph (d)(2)(ii); by adding two new sentences at the end of paragraph (d)(2); by revising the first sentence of paragraph (g); and by adding a new paragraph (h). The revised and added provisions read as follows:

§1.103-10 Exemption for certain small issues of industrial development bonds.

* * * * *

(b) *Small issue exemption.* * * *

(2) *$10 million or less.* (i) * * * All capital expenditures described in paragraph (b)(2)(ii) with respect to each principal user and each related person must be aggregated with the issue of obligations in question for purposes of determining whether the $10 million limitation of section 103(b)(6)(D) is exceeded. * * *

(iv) * * *

(f) A capital expenditure with respect to a facility other than the bond-financed facility ("other facility") is an excluded expenditure of the principal user of the other facility does not become a principal user of the facility financed by the proceeds of the issue in question ("bond-financed facility") until after the last day of the test period described in paragraph (i)(3)(ii) of this section. In addition, a capital expenditure with respect to an "other facility" becomes an excluded expenditure on and after the date the principal user of the other facility ceases to use the bond-financed facility; if, however, the issue financing the bond-financed facility lost its tax-exempt status on or before that date, this sentence will not apply to restore its tax-exempt status. * * *

* * * * *

(d) *Certain prior issues taken into account*—(1) *In general.* * * * Thus, the outstanding face amount of all prior issues specified in paragraph (d)(2) with respect to each principal user and each related person and taken into account under this paragraph (d)(1) must be aggregated with the issue of obligations in question for purposes of determining whether the $1 million limitation of section 103(b)(6)(A) or the $10 million limitation of section 103(b)(6)(D) has been exceeded with respect to the issue in question. The outstanding face amount of the prior exempt small issue is the principal amount outstanding at the time of issuance of the subsequent exempt small issue. * * *

(2) *Prior issues specified.* * * *

(ii) The principal user of the facilities described in paragraph (d)(2)(i) of this section is the same person or two or more related persons (as defined in section 103(b)(6)(C) and in paragraph (e) of this section) at any time on or after the date of issue of the subsequent but before the expiration of the test period described in paragraph (i)(3)(ii) of this section with respect to the subsequent issue.

The loss of tax exemption with respect to the interest of the subsequent issue shall be effective on the date of issue of the subsequent issue. For purposes of this paragraph (d), when a person ceases to use a facility financed by either the prior issue or the subsequent issue, the prior issue will no longer be taken into account under paragraph (d)(1) with respect to the subsequent issue; if, however, the subsequent issue loses its tax-exempt status on or before the date the person ceases to use either of the facilities described in this subparagraph, this paragraph will not apply to restore the tax-exempt status of the subsequent issue. * * *

* * * *

(g) *Examples*. The application of the rules contained in section 103(b)(6) and in paragraphs (a) through (f) of this section are illustrated by the following examples: * * *

* * * * *

(h) *Rules relating to principal users*—(1) *Definition of principal user*. For purposes of section 103(b)(6) and §1.103-10, the term "principal user" means a person who is a principal owner, a principal lessee, a principal output purchaser, or an "other" principal user. The term "principal user" also includes a person who is related to another person who is a principal user under section 103(b)(6)(C) and paragraph (e) of this section, unless the other person ceased to use the facility before the two persons became related. For purposes of this paragraph (h)—

(i) *Principal owner*. A principal owner is a person who at any time holds more than a 10-percent ownership interest (by value) in the facility or, if no person holds more than a 10-percent ownership interest, then the person (or persons in the case of multiple equal owners) who holds the largest ownership interest in the facility. A person is treated as holding an ownership interest if such person is an owner for Federal income tax purposes generally. Thus, for example, where a facility constructed on land subject to a ground lease has an economic useful life less than the noncancellable portion of the term of the ground lease, the ground lessor shall not, merely by reason of that reversionary interest, be treated as the principal user of the facility before the ground lease expires.

(ii) *Principal lessee*. A principal lessee is a person who at any time leases more than 10 percent of the facility (disregarding portions used by the lessee under a short-term lease). The portion of a facility leased to a lessee is generally determined by reference to its fair rental value. A short-term lease is one which has a term of one year or less, taking into account all options to renew and reasonably anticipated renewals.

(iii) *Principal output purchaser*. A principal output purchaser is any person who purchases output of an electric or thermal energy, gas, water, or other similar facility, unless the total output purchased by such person during each one-year period beginning with the date the facility is placed in service is 10 percent or less of the facility's output during each such period.

(iv) *Other principal user*. An "other" principal user is a person who enjoys a use of the facility (other than a short-term use) in a degree comparable to the enjoyment of a principal owner or a principal lessee, taking into account all the relevant facts and circumstances, such as the person's participation in control over use of the facility or its remote or proximate geographic location. For example, a party to a contract who would be treated as a lessee using more than 10 percent of a facility on a long-term basis but for the special rules of section 7701(e)(3) and (5) (relating to service contracts for certain energy and water facilities and low-income housing) is an "other" principal user. A short-term use means use that is comparable to use under a short-term lease.

(2) *Operating rules*. (i) In determining whether a person is a principal user of a facility, it is irrelevant where in a chain of use such person's use occurs. For example, where a sublessee subleases more than 10 percent of a facility from a lessee, both the lessee and the sublessee are principal lessees.

(ii) In determining whether a person owns or uses more than 10 percent of a facility or whether he uses it for more than one year, the person is treated as owning or using the facility to the extent that any person related to such person under section 103(b)(6)(C) and paragraph (e) of this section owns or uses the facility. For purposes of the preceding sentence, the term "use" includes use pursuant to an output purchase arrangement.

(iii) Co-owners or co-lessees who are collectively treated as a partnership subject to subchapter K under section 761(a) are not treated as principal users merely by reason of their ownership of partnership interests; such ownership is, however, taken into account in determining whether persons are related under section 103(b)(6)(C) and paragraph (e) of this section.

(iv) For purposes of this section, a principal user of a facility is treated as ceasing to use the facility when he ceases to own, lease, purchase the output of, or otherwise use the facility, as the case may be. A person who is a principal user of a facility because he is related to another person who is a principal user is treated as ceasing to use the facility when the other person ceases to use the facility or when the two persons cease to be related. A principal user who ceases to use a facility continues to be a principal user. See, however, paragraph (b)(2)(iv)(*f*) of this section (relating to excluded expenditures), paragraph (d)(2) (relating to excluded expenditures), paragraph (d)(2) (relating to prior issues), and paragraph (h)(1) (defining principal user), which may apply when a principal user ceases to use a facility.

(3) *Special rule for exempt persons*. If an exempt person, as defined in section 103(b)(3) and §1.103-7(b)(2), is a principal user of a facility financed with an issue of obligations described in section 103(b)(6), the following amounts must be aggregated with the issue in determining whether the $1 million limit of section 103(b)(6)(A) or the $10 million limit of section 103(b)(6)(D) has been exceeded:

(i) The outstanding face amount of any prior exempt small issue of industrial development bonds described in paragraph (d) of this section that financed a facility of which the exempt person is a principal user,

(ii) For purposes of the $10 million limitation, capital expenditures described in paragraph (b)(2)(ii) of this section paid or incurred with respect to other facilities used by the exempt person in an unrelated trade or business (within the meaning of section 513 and §1.513-1) and of which the exempt person is a principal user, and

(iii) Any section 103(b)(6)(D) capital expenditures paid or incurred with respect to the facility financed by the issue in question.

(4) *Examples*. The application of the rules of section 103(b)(6) and this paragraph (h) is illustrated by the following examples:

Example (1). On September 1, 1986, City L, after making the section 103(b)(6)(D) election, issues $8 million of obligations to finance the costs of acquiring a newly constructed warehouse within City L, owned by Corporation Z, a non-exempt person, which thus is a principal user of the warehouse. Beginning on September 1, 1986, the entire warehouse is leased to Corporation Y, an unrelated non-exempt person, for a 2-year term; thus, Y is also a principal user of the warehouse. On June 30, 1988, Y ceases to lease the warehouse. On October 1, 1988, Y incurs $20 million of capital expenditures in connection with its purchase of an office building in City L. Although Y continues to be a principal user of the warehouse under paragraph (h)(2)(iv) of this section, Y's capital expenditures after the date it ceases to use the warehouse are excluded expenditures under paragraph (b)(2)(iv)(*f*) of this section. Accordingly, the $20 million Y incurred with respect to the office building is not taken into account for purposes of determining whether the $10 million limitation of section 103(b)(6)(D) has been exceeded.

Example (2). The facts are the same as in Example (1), except that on October 12, 1985, City L issued an exempt small issue to finance acquisition of a newly constructed office building in the amount of $5 million, of which $4 million is outstanding on September 1, 1986. On December 1, 1988, Corporation Z leases 15 percent (by fair rental value) of the office building financed by the 1985 issue for a 2-year term. Thus, beginning on December 1, 1988, Z is a principal user of the office building. On December 1, 1988, Z still owns the warehouse financed by the 1986 issue. Because Z became a principal user of the office building before the end of the 3-year test period described in paragraph (i)(3)(ii) of this section with respect to the 1986 issue, the $4 million outstanding amount of the 1985 issue must be aggregated with the $8 million 1986 issue for purposes of determining whether the 1986 issue has exceeded the $10 million limitation of section 103(b)(6)(D). Because the sum of the two issues ($4 million of the prior 1985 issue outstanding on September 1, 1986, and the $8 million subsequent issue issued on September 1, 1986) exceeds $10 million, the interest on the 1986 issue ceases to be tax-exempt on September 1, 1986. Had Z's lease begun after September 1, 1989, the two issues would not have to be aggregated.

Example (3). On June 1, 1985, City O issues $15 million of its obligations to finance an expansion of a hospital owned by H, an organization described in section 501(c)(3) exempt from taxation under section 501(a). None of the proceeds of the issue will be used by H in an unrelated trade or business or in the trade or business of non-exempt persons. On November 1, 1986, City O, after making the section 103(b)(6)(D) election, issues $5 million of its obligations to construct a medical office building which will be owned by H for Federal income tax purposes and which will be entirely leased (for terms in excess of one year) to physicians, none of whom will lease over 10 percent of the building by value. On July 1, 1987, H incurs a $500,000 capital expenditure for permanent improvements to the medical office building. In addition, on August 1, 1987, W, a non-exempt person related to H, incurs a $1 million capital expenditure with respect to a facility that W owns within City O and uses in its trade or business. For purposes of determining whether the $10 million limitation of section 103(b)(6)(D) has been exceeded with respect to the November 1, 1986, issue for the medical office building, H must take into account the $5 million issue, the $500,000 of capital expenditures made with respect to the medical office building, and W's $1 million capital expenditure. Because the sum of these amounts is less than $10 million, interest on the issue does not cease to be tax-exempt. H is not required to take into account the June 1, 1985, issue financing the hospital expansion because that issue is not an exempt small issue as defined in section 103(b)(6) (see paragraph (h)(3)(i) of this section) and because the cost of the facility financed by the June 1, 1985, issue is neither a section 103(b)(6)(D) capital expenditure with respect to the medical office building owned by H (see paragraph (h)(3)(iii) of this section) nor a section 103(b)(6)(D) capital expenditure for a separate facility used by H in an unrelated trade or business (see paragraph (h)(3)(ii) of this section).

* * * * *

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on February 20, 1986, 8:45 a.m., and published in the issue of the Federal Register for February 21, 1986, 51 F.R. 6274)

Notice of Proposed Rulemaking

$40 Million Limitation Upon Beneficiaries of Certain Tax-Exempt Bond Issues

LR-157-84

SUMMARY: This document contains proposed regulations that relate to certain industrial development tax-exempt bonds and to certain beneficiaries of such bond issues. Changes to the applicable tax law were made by the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1] that generally deny Federal income tax exemption for a small issue of industrial development bonds if any of its test-period beneficiaries is allocated more than $40 million of outstanding industrial development bonds, including its allocated portion of the small issue in question. This provision restricts the amount of small issues of industrial development bonds that may be issued for a beneficiary when that person already benefits from a significant amount of tax-exempt industrial development bonds.

DATES: Written comments must be delivered or mailed by April 22, 1986. These regulations are proposed to be effective after August 20, 1986 in determining the tax-exempt status of obligations issued after August 20, 1986. However, these regulations would not apply to certain obligations described in section 631(f) of the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 445] and to certain obligations with respect to facilities described in section 631(c)(3) of the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 444]. The provisions of §1.103-10(i)(4)(vi) are generally proposed to be effective after December 31, 1983, in determining the tax-exempt status of obligations issued after December 31, 1983.

ADDRESS: Please mail or deliver comments to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-157-84), 1111 Constitution Avenue, N.W., Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: John A. Tolleris of the Legislation and Regulations Division, Office of Chief Counsel, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (Telephone: 202-566-3590, not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 103(b)(15) of the Internal Revenue Code of 1954. These proposed amendments provide needed guidance regarding the provisions of section 103(b)(15) concerning the $40 million limitation which were enacted by section 623 of the Tax Reform Act of 1984 (Pub. L. 98-369; 98 Stat. 921) [1984-3 C.B. (Vol. 1) 1, 429].

EXPLANATION OF PROVISIONS

The $40 million limitation applicable to small issues of tax-exempt industrial development bonds was enacted in the Tax Reform Act of 1984. This limitation generally denies Federal income tax exemption for a small issue of industrial development bonds if any test-period beneficiary is allocated more than $40 million of outstanding industrial development bonds, including its allocated portion of the issue in question. A person is a "test-period beneficiary" of the bond-financed facility, if he is an owner or a principal user of a facility financed by the issue at any time during the 3-year period after the issue is issued, or after the facility is placed in service, whichever occurs later. A person who is related to a principal user at any time during the test period is also a test-period beneficiary, unless the principal user ceased using the facility before the two persons became related.

These proposed regulations provide guidance on the allocation of the proceeds of an issue of industrial development bonds among test-period beneficiaries. In determining whether the $40 million limitation has been exceeded with respect to a test-period beneficiary, the portions of the outstanding amounts of all industrial development bonds (not just small issues) allocable to the beneficiary are aggregated.

NONAPPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

REGULATORY FLEXIBILITY ACT

The Secretary of the Treasury has certified that this proposed rule will not have a significant impact on a substantial number of small entities because the economic and any other secondary or incidental impact flows directly from the underlying statute. A regulatory flexibility analysis, therefore, is not required under the Regulatory Flexibility Act (5 U.S.C. chapter 6).

DRAFTING INFORMATION

The principal author of these proposed regulations is John A. Tolleris of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and the Treasury Department participated in developing the regulations, on matters of both substance and style.

COMMENTS—PUBLIC HEARING

Before adoption of these proposed regulations, consideration will be given to any written comments that are submitted (preferably seven copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held * * * [on Wednesday, June 3, 1986.]

* * * * *

Proposed amendments to the regulations

The proposed amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.103-10(i) also issued under 26 U.S.C. 103(b)(15).

Par. 2. Section 1.103-10 is revised by adding a new paragraph (i) immediately following paragraph (h) therein. The new paragraph reads as follows:

§1.103-10 Exemption for certain small issues of industrial development bonds.

* * * * *

(i) *$40 million limitation for beneficiaries of small issues of industrial development bonds*—(1) *General rule.* Section 103(b)(6) and §1.103-10(a) do not apply to an issue of obligations ("issue in question") if—

(i) The portion of the aggregate authorized face amount of the issue in question allocated to any test-period beneficiary, as defined in paragraph (i)(3) of this section, of the issue, plus

(ii) The portion of the outstanding principal amount of prior bonds, as defined in paragraph (i)(2) of this section, allocated—

(a) To the test-period beneficiary described in paragraph (i)(1)(i) of this section, or

(b) To a person who at any time during the test period of the issue in question is related to such beneficiary,

exceeds $40 million. If interest on the issue in question would, but for this paragraph and section 103(b)(15), be exempt from Federal income taxation solely because of section 103(b)(6), the issue is treated as an issue of obligations not described in section 103(a) on and after the date of issuance. For purposes of this paragraph (i), the aggregate authorized face amount of the issue in question and the outstanding principal amount of a prior bond shall be determined without regard to section 103(b)(6)(B) or (D) (requiring certain amounts of prior issues or capital expenditures to be taken into account in determining the aggregate face amount of the issue in question or of the prior bond).

(2) *Prior bonds.* For purposes of this paragraph (i), "prior bonds" means prior or simultaneous issues of industrial development bonds described in paragraph (4), (5), or (6) of section 103(b) the interest on which is exempt from tax pursuant to section 103(a), including such bonds issued before January 1, 1984. For purposes of paragraph (i)(1)(ii) of this section, "outstanding principal amount of prior bonds" means the principal amount that is outstanding at the time of issuance of the issue in question, not including the amount to be redeemed from the proceeds of the issue in question. Thus, the outstanding principal amount of prior bonds does not include the portion of the original face amount that has been discharged, nor does it include any amount to be issued in the future.

(3) *Test-period beneficiary*—(i) *In general.* For purposes of this paragraph (i), a "test-period beneficiary" of the issue in question or of an issue of prior bonds means any person who at any time during the test period for the issue is a principal user, as defined in paragraph (h)(1) of this section, of a facility financed by the proceeds of the issue, including a person who is related to a principal user. For purposes of the preceding sentence, a person shall be treated as related to a principal user only if that person is related to such user within the meaning of section 103(b)(6)(C) and paragraph (e) of this section at any time during the test period, and such user has not ceased to use the facility before the persons became related. See paragraph (h)(2)(iv) of this section for circumstances in which a person will be treated as ceasing to use a facility. A test-period beneficiary does not cease to be a test-period beneficiary if he ceases to use the facility; the portion of the issue allocated to the test-period beneficiary continues to be so allocated until the issue is no longer outstanding.

(ii) *Test period.* The "test period" for an issue means the 3-year period beginning on the later of the date the facility financed by the proceeds of the issue is placed in service or the date of issue of such issue. A facility shall be considered as being placed in service at the time the facility is placed in a condition or state of readiness and availability for a specifically assigned function. If separate facilities are financed by an issue and the facilities are placed in service at different times, there shall be separate test periods for the portions of the issue financing each separate facility. If a single facility (consisting of separately depreciable items of property) is placed in service in stages, then the entire facility will be deemed placed in service when its last portion is placed in service.

(4) *Allocation of issue*—(i) *In general.* The portion of the amount of an issue allocated to a test-period beneficiary is the highest percent of the facility financed by proceeds of the issue that the beneficiary owned or used on a regular basis during the test period. For example, a person that owns the entire facility shall be allocated 100 percent of the issue; a person that leases 90 percent of a facility for two years of the test period and leases 35 percent for the third year shall be allocated 90 percent of the issue.

(ii) *Portion allocable to lessee and output purchaser.* The portion of a facility used by a lessee is generally determined by reference to its fair rental value. The portion of a facility used by a principal output purchaser, as defined in paragraph (h)(1)(iii) of this section, is the highest portion of the facility's total output purchased by such purchaser during any of the three years of the test period.

(iii) *Portion allocable to related person.* The portion of an issue allocable to a person who is a test period beneficiary because he is related to a principal user is the same portion allocated to such principal user.

(iv) *Double allocation.* The total amount of an issue allocated to test-period beneficiaries may exceed 100 percent of its outstanding face amount, such as when one test-period beneficiary is an owner and another person leases the facility for over a year. However, if a beneficiary is the owner of all or a portion of a facility that is leased to or otherwise used by such beneficiary or by a related person, then the portion of the issue the proceeds of which were used to finance the facility is allocated only once to the beneficiary. For example, if Corporation X owns an undivided 50 percent of a facility while related Corporation Y is the lessee of 60 percent of the facility, the portion of the issue financing the facility allocable to X is 80 percent (50 percent plus 30 percent), because one-half of the 60-percent portion used by Y (30 percent) is considered attributable to the portion owned by X.

(v) *Allocation of remainder of issue to owners.* If the portion of an issue allocated to all test-period beneficiaries of the bond-financed facility (other than related persons) is less than 100 percent, the remainder shall be allocated to test-period beneficiaries who are owners of the facility in proportion to the amount of the issue otherwise allocable to such persons by reason of their ownership interests during the test period.

(vi) *Bond redeemed before person becomes principal user.* If all or some of the outstanding principal amount of the issue in question or of prior bonds is redeemed other than from the proceeds of a refunding issue described in section 103(a) either before or as soon as reasonably practicable after a person becomes a test-period beneficiary with respect to the issue in question, but in no event later than 180 days after the date such person becomes a test-period beneficiary, then the amount of the issue so redeemed will not be allocated to such person (or to a related person) in determining whether the issue in question exceeds the $40 million limitation. With respect to obligations that are issued after August 20, 1986, paragraph (i)(4)(vi) shall not apply if the terms of the issue provide for a delay in redemption a principal purpose of which is to benefit from the 180-day period referred to therein. In the case of a person who becomes a test-period beneficiary before February 21, 1986, bonds redeemed before August 20, 1986 shall be considered redeemed as soon as reasonably practicable for purposes of the first sentence of this paragraph (i)(4)(vi) and the 180-day limitation referred to therein shall not apply.

(5) *Treatment of certain successors as test-period beneficiaries.* If a corporation, partnership, or other entity which is a test-period beneficiary with respect to one or more issues transfers substantially all of its properties to another person (or to two or more related persons within the meaning of section 103(b)(6)(C)), or if a corporation acquires the assets of a test-period beneficiary in a transaction described in section 381(a), the transferee shall be treated as a test-period beneficiary with respect to such issues and shall be allocated the portion of such issues that were allocated to the transferor prior to the transfer. The preceding sentence shall not apply to the extent that it would result in double allocation of an issue, such as in the case of a transfer to a related person. This paragraph (i)(5) shall apply regardless of whether gain is required to be recognized by the transferor for Federal income tax purposes and regardless of whether the transferor remains in existence after the transfer. If the transferor remains in existence after the transfer, this paragraph (i)(5) shall not relieve the transferor of its allocation of any issue. This paragraph (i)(5) shall apply only for purposes of determining the tax exemption of issues of which the transferee becomes the test-period beneficiary after the transfer described herein.

(6) *Examples.* The application of section 103(b)(15) and this paragraph (i) may be illustrated by the following examples:

Example (1). On September 1, 1986, City M issues a $9 million obligation to finance acquisition of a newly constructed shopping center that is placed in service on September 1, 1986, and is owned and managed by Corporation X. Half of the shopping center (determined by fair rental value) is leased for a term exceeding 1 year to Corporation Y. X owns 60 percent of the shares of Y. The other half of the shopping center (also determined by fair rental value) is leased in equal shares for a term exceeding 1 year to A and B, two unrelated corporations. As of September 1, 1986, $30 million of prior issues of obligations are outstanding and are allocable to X as a test-period beneficiary under the rules of §1.103-10(i)(4). As of that date there is no prior issue of obligations outstanding and allocable to Y, A, or B as test-period beneficiaries. Because X owns 100 percent of the shopping center, 100 percent of the 1986 issue ($9 million) is allocated to X. Therefore, for purposes of determining whether the 1986 issue exceeds the $40 million limitation of section 103(b)(15), the $30 million of outstanding prior issues must be added to the $9 million 1986 issue. Because Y leases 50 percent of the shopping center, 50 percent of the 1986 issue ($4.5 million) is allocated to Y. Although Y is related to X under section 103(b)(15)(E), the $4.5 million of the 1986 issue that is allocated to Y is not added to the $39 million allocated to X under paragraph (i)(4)(iv) of this section since such amount has already been allocated to X as owner of the shopping center. Because A and B each leases 25 percent of the shopping center, each is allocated 25 percent ($2.25 million) of the 1986 issue.

Example (2). The facts are the same as in *Example (1)* except that A owns a 60-percent interest in an airport hotel described in §1.103-8(e)(2)(ii)*(d)* and, because of such ownership interest, is allocated $15 million of prior outstanding obligations described in section 103(b)(4)(D). In addition, County N issues $25 million of obligations described in section 103(b)(4)(E) on October 1, 1986, to finance construction of a solid-waste disposal facility that will be owned by C, A's wholly-owned subsidiary corporation. In this case, with respect to the September 1, 1986, issue, A is allocated the $15 million prior issue that is outstanding with respect to A's share of the airport hotel bond and the $2.25 million that is A's allocable share of the September 1, 1986, issue for a total of $17.25 million. Because the solid-waste disposal facility bonds had not yet been issued when the September 1, 1986, obligation was issued, no portion of the $25 million of obligations to finance C's solid-waste disposal facility will be treated as part of A's allocable obligations with respect to the September 1, 1986, issue even though A and C are related persons. In addition, even though A and C are related persons and even though on the date of issue of the solid-waste disposal bonds C will be allocated more than $40 million of outstanding obligations for purposes of section 103(b)(15) (including A's $17.25 million of outstanding prior obligations), the $40 million limitation of section 103(b)(15) does not render the interest on the October 1, 1986, bonds taxable since the October 1, 1986, issue qualifies for tax exemption under section 103(b)(4), and the $40 million limitation of section 103(b)(15) does not apply to render taxable bonds issued under section 103(b)(4).

Example (3). On October 1, 1986, City K issues an $8 million issue of obligations exempt under section 103(b)(6) to finance acquisition of a newly-constructed manufacturing plant owned by Corporation L. On October 1, 1986, Corporation M has $35 million of prior outstanding obligations allocable to it under section 103(b)(15). On October 1, 1986, L has no prior outstanding obligations allocable to itself. On April 1, 1988, M acquires 100 percent of the stock of L, which still owns the plant financed by the 1986 issue. Since M and L became related to each other during the 3-year test period of the 1986 issue and L had not ceased to use the facility, the $8 million issue is allocated to M under section 103(b)(15). This allocation causes the 1986 issue to exceed the $40 million limitation of section 103(b)(15) and the interest upon the issue to become taxable on and after October 1, 1986. However, if at least $3 million of the 1986 issue or of other issues allocated to M are redeemed as soon as reasonably practicable, and no later than 180 days after M's acquisition of L's stock, then the 1986 issue would not exceed the $40 million limitation.

Example (4). The facts are the same as in *Example (3)*, except the October 1, 1986, bonds were issued on January 1, 1985, the plant acquired with the proceeds of the issue was placed in service on January 1, 1985, and M had $39 million of prior outstanding obligations allocable to it on January 1, 1985. Because M and L became related to each other after the test period for the January 1, 1985, issue ended, M is not a test-period beneficiary, and the January 1, 1985, issue does not exceed the $40 million limitation of section 103(b)(15). However, if either M or L subsequently becomes a test-period beneficiary of an issue of obligations, then the outstanding principal amount of the January 1, 1985, issue and of the other issues allocable to M would be taken into account in applying the $40 million limitation to that issue.

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on February 20, 1986, 8:45 a.m., and published in the issue of the Federal Register for February 21, 1986, 51 F.R. 6270)

Tables for Publications 534 and 1985 Instructions for Form 4562

Announcement 86-23

Recently issued Revenue Procedure 86-6, 1986-5 I.R.B. 36, as modified and superseded by Rev. Proc. 86-14, page 11, this Bulletin, contains depreciation tables that apply to certain real property placed in service after May 8, 1985.

Three of the tables in Revenue Procedure 86-6, as modified and superseded by Rev. Proc. 86-14, should be used for property placed in service after May 8, 1985, instead of the tables published in Publication 534, *Depreciation*, (Rev. Dec. 85). Tables 6 and 9 of the revenue procedure must be used for this property instead of Publication 534 tables II (page 28) and X (page 30), which apply to low-income housing and to low-income housing for which the alternate ACRS method over a 35-year period is elected. Table 4 of the revenue procedure must be used for property placed in service after May 8, 1985, instead of table IX (page 30 of the publication), which applies to 19-year real property for which the alternate ACRS method over a 35-year period is elected.

A "Note" on page 13 of Publication 534 refers to a table dealing with low-income housing placed in service after May 8, 1985, for which a 19-year recovery period under the alternate ACRS method is elected. This is table 8 of the revenue procedure.

The revenue procedure includes tables for certain property used predominantly outside the U.S. which have not been published previously. These are tables 2 and 7 of the revenue procedure.

For purposes of line 4e of Form 4562, *Depreciation and Amortization*, use table 6 of the revenue procedure for property placed in service after May 8, 1986, instead of the table provided in the instructions to Form 4562.

A reprint of Revenue Procedure 86-6 as, modified and superseded by Rev. Proc. 86-14, will be distributed with copies of Publication 534.

Extension of Time for Making Elections Under Section 338

Announcement 86-31

The Temporary Income Tax Regulations will soon be amended to provide that no elections under section 338 of the Internal Revenue Code are required to be filed before July 15, 1986, if the acquisition date of the target for which the election would apply occurs after August 31, 1982. In accordance with Announcement 85-178, dated December 6, 1985, the temporary regulations now provide that no section 338 elections are required before March 15, 1986. The period for making an election under section 338 for an acquisition occurring before September 1982 is not extended. The extension applies to all other elections under section 338 of the Internal Revenue Code and the regulations thereunder.

This extension of time does not alter the fact that any election under section 338, once filed, is irrevocable.

The temporary regulations will also extend the time for taking certain other actions under section 338. Thus, in temporary regulations section 1.338-1T (as amended by T.D. 8068), section 1.338-4T (as amended by T.D. 8068), section 1.338-5T (as added by T.D. 8074), and section 1.338(h)(10)-1T (as added by T.D. 8068), all references to "March 15, 1986" with respect to the time for making elections or taking certain other actions under section 338 will be changed to "July 15, 1986." However, references to "March 15, 1986" will not be amended insofar as the applicability of certain rules depends on whether the acquisition occurs after March 15, 1986.

Amendments to the temporary regulations will be published soon to provide guidance relating to elections made in circumstances when the statute of limitations has expired or is about to expire for the target's taxable year that includes the acquisition date. The amendments to the temporary regulations will provide that any statement of election under section 338 filed on or after December 9, 1985, and on or before July 15, 1986, will be ineffective unless the target agrees to take certain steps relating to the statute of limitations on assessment regarding target's taxable year that includes the acquisition date. Specifically, when the statement of election is filed, target must either execute a consent to extend the statute of limitations until May 15, 1987 (Form 872) or a closing agreement waiving the expiration of the statute of limitations and agreeing to extend the period of assessment to June 15, 1988. The amendments will also provide rules for perfecting statements of election which are filed within the relevant time period but do not comply with the provisions of the amendments to the temporary regulations.

The requirement of a Form 872 or closing agreement will also apply to certain subsequent taxable years of target and to certain corporate transferees of target. The amendments will also give the District Director discretion to waive the Form 872 and closing agreement requirements.

Consolidated Return Investment Adjustments—Decision Not to Appeal *Woods Investment Co. v. Commissioner*

Announcement 86-32

The Internal Revenue Service is not appealing the decision of the Tax Court in *Woods Investment Co. v. Commissioner*, 85 T.C. No. 14 (August 15, 1985). Although the Service disagrees with the result in that a case, it will no longer advance the position that it advanced in that case, pending a change in the regulations.

The issue in *Woods* was the determination of the amount of gain on the sale of a subsidiary's stock by a group filing consolidated returns where the subsidiary computes its earnings and profits under section 312(k) of the Internal Revenue Code. Section 312(k) requires that straight-line depreciation be used in computing earnings and profits, even if a subsidiary uses accelerated depreciation in computing taxable income. Because consolidated return basis adjustments are measured by earnings and profits, if a subsidiary uses accelerated depreciation, the basis of the stock of the subsidiary is in most cases higher under these adjustments, if they are applied mechanically, than it would have been if section 312(k) had not been enacted.

In *Woods*, the Service reduced the basis of the stock of subsidiaries the group had sold. The grounds for the Service's action was that the reduction was necessary to achieve the purposes of the consolidated return basis adjustment system, and to prevent a double deduction. The Tax Court rejected this adjustment, holding in effect that the adjustments provided under consolidated return regulations preempt the area, and they have not been amended to take section 312(k) into account.

Although the Service will not appeal the *Woods* case, it remains convinced that the effect of section 312(k) on the basis adjustment system is to understate the gain on the sale of the stock of a subsidiary in this and similar cases, creating the effect of a double deduction.

The Service is considering revisions to the investment adjustment provisions of the consolidated return regulations that would provide for investment adjustments that do not result in this understatement of gain. The revisions will also address other issues that have arisen under the current investment adjustment regulations.

$40 Million Limitation Upon Beneficiaries of Certain Tax-Exempt Bond Issues and Definition of the Term "Principal User"—Public Hearing

Announcement 86-34[1]

SUMMARY: This document provides notice of a public hearing on two proposed regulations. One of the two proposed regulations (LR-157-84) relates to certain industrial development tax-exempt bonds and to certain beneficiaries of such bond issues. The other proposed regulations (LR-59-74) define the term "principal user" for purposes of paragraphs (6) and (15) of section 103(b) of the Internal Revenue Code of 1954.

DATES: The public hearing will be held on Wednesday, June 4, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Wednesday, May 21, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, ATTN: CC:LR:T (LR-157-84 and LR-59-74), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Fay Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935 (not a toll-free call).

SUPPLEMENTARY INFORMATION: One of the two subjects of the public hearing is proposed regulations under section 103(b)(15) of the Internal Revenue Code of 1954. The proposed regulations appear * * * [on page 22, this Bulletin].

The second subject of the public hearing is proposed regulations under section 103(b)(6) of the Internal Revenue Code of 1954. The proposed regulations * * * [appear on page 19, this Bulletin].

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who submit written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Wednesday, May 21, 1986, an outline of the oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions, attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

Revisions to Various 1985 Forms Due to a Change in the Recovery Period of Real Property

Announcement 86-37

Public Law 99-121, 1985-48 I.R.B. 11, extended the recovery period for 18-year real property to 19 years. This new provision applies, in general, to real property placed in service after May 8, 1985.

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[1] Filed by the Office of the Federal Register on February 20, 1986, 8:45 a.m., and published in the issue of the Federal Register for February 21, 1986, 51 F.R. 6273.

Several 1985 tax forms were printed before the enactment of this legislation and therefore do not reflect the 19-year period. Consequently taxpayers should include amounts attributable to 19-year real property wherever "15 or 18-year property" appears on the following forms and in the related instructions for 1985:

Form 3468, Computation of Investment Credit

Form 4626, Computation of Minimum Tax-Corporations

Form 4797, Gains and Losses From Sales or Exchanges of Assets Used in a Trade or Business and Involuntary Conversions

Form 6251, Alternative Minimum Tax Computation

Schedule(s) K and K-1 (Form 1065), Partners' Shares of Income, Credits, Deductions, etc.

Schedule(s) K and K-1 (Form 1120S), Shareholders' Share of Income, Credits, Deductions, etc.

On Form 8038, Information Return for Private Activity Bond Issues, taxpayers should include 19-year real property on line 22g and attach a statement describing the property.

The 19-year ACRS tables were published in Rev. Rul. 86-6, 1986-5 I.R.B. 36.

Errors in Publication 519

Announcement 86-38

Publication 519, *U.S. Tax Guide for Aliens*, contains errors in three examples. Under the stated facts of each example, the taxpayers involved would be correctly classified as *resident* aliens (for pertinent parts of the year) rather than *nonresident* aliens as now incorrectly assumed. These examples are:

a) The comprehensive illustration of a dual-status tax year return beginning on page 7 and continuing with the filled-in forms on pages 9-12.

b) The example showing the treatment of salary payments received in a year in which the taxpayer is not engaged in a U.S. trade or a business, on page 13 of the publication.

c) The comprehensive example of how to fill in Form 1040NR, beginning on page 19 and including the filled in forms on pages 21 and 22.

The three examples can be corrected by making the changes set forth below in the facts of each one. If these revisions are made, no substantial changes to the entries in the filled-in forms will be necessary. The taxpayer in each case would be properly classified as a nonresident alien.

a) In the example of a dual-status return that begins on page 7, Hans Braun's date of initial arrival in the United States should be changed from January 15 to March 18 (or later). With this change, Braun's total presence in the United States would be less than 183 days during 1985 and he would not satisfy the substantial presence test for the year. His residency starting date under the green card test would be September 10 and the rest of the example would be correct.

b) Likewise, the example on page 13 related to the treatment of salary payments received in a tax year in which a nonresident alien is not engaged in a U.S. trade or business should be changed so that the taxpayer's date of arrival in the United States is July 3rd (or later). His stay in the United States would then be less than 183 days and he would not be treated as a resident alien under the substantial presence test.

c) The example beginning on page 19, illustrating the proper completion of Form 1040NR by a nonresident alien, should be changed so that the taxpayer, John Latter, is present in the United States for 9 1/2 months as an *exempt individual* for purposes of the substantial presence test. This would be the case if he were admitted to the United States under a "J" visa as a professor of engineering, rather than as a participating engineer as is now shown. Additionally, Latter's country of origin should be changed to Australia, rather than the United Kingdom, because the U.S.-U.K. income tax treaty exempts the salaries of teachers and professors from U.S. taxation for up to 2 years. The treaty with Australia does not contain such an exemption.

In the example, the taxpayer's bond interest income from Boston Transit Co. bonds is exempt from U.S. tax under the treaty with the United Kingdom. Under the treaty with Australia, this bond interest would be subject to a maximum U.S. tax of 10%. However, if the facts are clarified so that the bonds were issued after July 18, 1984, the interest could be portfolio interest that is exempt from tax under U.S. law when paid to a nonresident alien.

With these changes, the example is correct and no substantial changes are needed to the entries on the filled-in forms.

At Risk Rules—Aggregation of Partnership and S Corporation Activities

Announcement 86-35

Temporary regulations will be issued extending the aggregation rule contained in section 1.465-1T of the Income Tax Regulations to taxable years beginning during 1985. Thus, taxpayers will be allowed to aggregate certain partnership and S corporation activities for purposes of the at-risk rules under section 465 of the Internal Revenue Code for taxable years beginning during 1985 in the same manner as for taxable years beginning during 1984.

Under the temporary regulations, aggregation of partnership or S corporation activities will be allowed within each of four categories for taxable years beginning during 1985. Those categories are films and video tapes, farms, oil and gas properties, and geothermal properties. Thus, in applying the at-risk rules for 1985, partners and S corporation shareholders will be permitted to treat all of the partnership's or S corporation's films and video tapes as a single activity, and to treat all farms, all oil and gas properties, or all geothermal properties of the partnership or S corporation similarly.

Proposed regulations also will be issued concerning the aggregation of activities within the categories mentioned above for taxable years beginning after December 31, 1985. The proposed regulations will contain rules that would allow taxpayers to aggregate activities within those categories for purposes of applying the at-risk rules in taxable years beginning after December 31, 1985, only if certain conditions are satisfied.

Differential Earnings Rates for Mutual Life Insurance Companies

Announcement 86-36

This announcement concerns the determination under section 809 of the Internal Revenue Code of the "differential earnings rate" for taxable year 1985 and the rate that will be used to calculate the "recomputed differential earnings amount" for taxable year 1984. (The latter rate is referred to herein as the "recomputed differential earnings rate" for 1984.) These rates will be used by mutual life insurance companies to calculate their federal income tax liability for taxable year 1985.

BACKGROUND

Section 809(a) of the Code provides that, in the case of any mutual life insurance company, the amount of the deduction allowable under section 808 for policyholder dividends shall be reduced (but not below zero) by the "differential earnings amount." Any excess of the differential earnings amount over the amount of the deduction allowable under section 808 shall be taken into account as a reduction in the closing balance of reserves under subsections (a) and (b) of section 807. The "differential earnings amount" for any taxable year is an amount equal to the product of (a) the life insurance company's average equity base for the taxable year and (b) the "differential earnings rate" for such taxable year. The "differential earnings rate" for a taxable year is the excess of (a) the "imputed earnings rate" for the taxable year over (b) the "average mutual earnings rate" for the second calendar year preceding the calendar year in which the taxable year begins. The "imputed earnings rate" for any taxable year is an amount which bears the same ratio to 16.5 percent as the "current stock earnings rate" for the taxable years bears to the "base period stock earnings rate."

Section 809(f) of the Code provides that, in the case of any mutual life insurance company, if the "recomputed differential earnings amount" for any taxable year exceeds the differential earnings amount for such taxable year, such excess shall be included in life insurance gross income for the succeeding taxable year. If the differential earnings amount for nay taxable year exceeds the recomputed differential earnings amount for such taxable year, such excess shall be allowed as a life insurance deduction for the succeeding taxable year. The "recomputed differential earnings amount" for any taxable year is an amount calculated in the same manner as the differential earnings amount for such taxable year, but substituting the average mutual earnings rate for the calendar year in which the taxable year begins for the average mutual earnings rate for the second calendar year preceding the calendar year in which the taxable years begins. For example, while the differential earnings rate for 1985 is based on the average mutual earnings rate for 1983, the recomputed differential earnings rate for 1985 will be based on the average mutual earnings rate for 1985.

As described above, the differential earnings rate for 1985 and the recomputed differential earnings rate for 1984 will affect the income and deductions reported by mutual life insurance companies on their federal income tax returns for the 1985 taxable year. In addition, pending technical corrections legislation would permit mutual life insurance companies to use the most recently published differential earnings rate for purposes of calculating any additions to tax under section 6655 for underpayments of estimated tax.

Data necessary to determine the differential earnings rate for 1985 and the recomputed differential earnings rate for 1984 have been compiled from returns filed by mutual life insurance companies and certain stock life insurance companies. The Internal Revenue Service is currently examining these returns to verify the accuracy of the data reported on these returns. This examination will not be completed before the March 15, 1986 due date for filing 1985 calendar year returns. Moreover, there will not be an opportunity before March 15, 1986 to obtain public comment on forthcoming regulations that will address issues affecting the determination of the differential earnings rate for 1985 and the recomputed differential earnings rate for 1984.

ANNOUNCEMENT OF TENTATIVE RATES

This announcement publishes a tentative determination of the differential earnings rate for 1985 and recomputed differential earnings rate for 1984. This announcement also publishes a tentative determination of several rates on which the calculation of the differential earnings rate for 1985 and the recomputed differential earnings rate for 1984 are based. The final determination of these rates is expected to be published before September 1, 1986.

The tentative determination of the differential earnings rate for 1985 and recomputed differential earnings rate for 1984 that is published in this announcement should be used by mutual life insurance companies to calculate the amount of tax liability (in the case of companies that file returns before an announcement of the final determination of these rates) or to calculate the amount of properly estimated unpaid tax liability (in the case of companies that are allowed an extension of time to file returns) for taxable year 1985. Companies that file returns before an announcement of the final determination of these rates should file amended returns after the final determination of these rates is announced. Any failure to pay tax for the 1985 taxable year before September 15, 1986 that is attributable to a difference between the tentative determination of the differential earnings rate for 1985 and recomputed differential earnings rate for 1984 and the final determination of these rates will be treated as due to reasonable cause and will not give rise to any addition to tax under section 6651 of the Code.

The tentative determination of the differential earnings rate for 1985, recomputed differential earnings rate for 1984, and other relevant rates is as follows:

Differential earnings rate for 1985	6.754 percent
Recomputed differential earnings rate for 1984	12.302 percent
Imputed earnings rate for 1985	16.391 percent
Base period stock earnings rate	17.715 percent
Current stock earnings rate for 1985	17.598 percent
Stock earnings rate for 1981	17.112 percent
Stock earnings rate for 1982	17.411 percent
Stock earnings rate for 1983	18.622 percent
Stock earnings rate for 1984	16.760 percent
Average mutual earnings rate for 1983	9.637 percent
Average mutual earnings rate for 1984	4.198 percent

Revision of Form 8264 and Instructions

Announcement 86-40

Form 8264, Application for Registration of a Tax Shelter, and instructions, have been revised. Major changes include the following:

- The addition of the Tax Shelter Ratio Worksheet on page 2 of the form.
- The addition of space on page 2 for explanations of items from page 1 of the form.
- A change in the information requested by item 3b. Item 3b now asks whether the acquisition of the tax shelter's principal asset was from a related party. The previous version of the form asked whether the acquisition was from an unrelated party.

Amended Forms 8264 may now be filed if there is a material change in facts occurring after the initial registration.

The form and instructions (both carrying an August 1985 revision date) should be available in most Internal Revenue Service offices by the end of March. Previous versions of the form and instructions will be obsolete when the new form and instructions become available.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Dal H. Felkel	Kingstree, SC	Certified Public Accountant	Indefinite from January 31, 1986
John J. Matonis	Walnut, CA	Attorney	Indefinite from January 24, 1986
Joel A. Shor	Baltimore, MD	Certified Public Accountant	Five Months from December 15, 1985
Patrick H. Diamond	New York, NY	Attorney & Certified Public Accountant	Indefinite from February 10, 1986
Folger P. Gifford	Cold Spring Harbor, NY	Certified Public Accountant	Indefinite from February 11, 1986
Robert Allen Beamer	Wauwatosa, WI	Attorney	Indefinite from February 19, 1986
Robert L. Cummings	Springfield, MO	Certified Public Accountant	Indefinite from February 27, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.401(a)-4, 1.411(d)-4, added.	Limitations on alternative benefits under qualified plans	1986-9 I.R.B. 26	Mar. 31, 1986
26 CFR 1.904(f)-1 through 1.904(f)-6, 1.1502-9, added.	Recapture of foreign losses	1986-10 I.R.B. 14	Mar. 25, 1986
26 CFR 1.338-1T, 1.338-4T, 1.338(h)(10)-1T, amended; 1.338(b)-1T, 1.338(b)-2T, 1.338(b)-3T, added.	Basis of assets of a target corporation	1986-11 I.R.B. 28	Mar. 31, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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______	1931-2	14.00
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______	1932-2	10.00
______	*1933-1*	*3.75*
______	*1933-2*	*4.00*
______	*1934-1*	(**)
______	1934-2	15.00
______	1935-1	8.00
______	*1935-2*	*15.00*
______	*1936-1*	*4.00*
______	*1936-2*	*15.00*
______	*1937-1*	*14.00*
______	1937-2	8.50
______	*1938-1*	*17.00*
______	*1938-2*	*14.00*
______	1939-1-1	9.50
______	1939-1-2	12.00
______	1939-2	10.00
______	1940-1	6.50
______	1940-2	15.00
______	1941-1	8.00
______	*1941-2*	*4.00*
______	1942-1	8.00
______	*1942-2*	*6.50*
______	*1943-(*)*	*11.00*
______	*1944-(*)*	*9.00*
______	1945-(*)	10.00
______	*1946-1*	*3.00*
______	1946-2	6.00
______	*1947-1*	*2.00*
______	1947-2	3.75
______	*1948-1*	*3.50*
______	1948-2	8.50
______	*1949-1*	*8.00*
______	*1949-2*	*3.25*
______	1950-1	7.00
______	*1950-2*	*5.50*
______	*1951-1*	*13.00*
______	*1951-2*	*6.00*
______	*1952-1*	*3.00*
______	1952-2	8.00
______	*1953-1*	*4.75*
______	1953-2	13.00
______	1954-1	13.00
______	1954-2	13.00
______	1955-1	11.00
______	1955-2	14.00
______	1956-1	17.00
______	1956-2	20.00
______	1957-1	18.00
______	1957-2	(**)
______	1958-1	11.00
______	1958-2	(**)
______	1958-3	17.00
______	1959-1	19.00
______	1959-2	11.00
______	1960-1	21.00
______	1960-2	13.00
______	1961-1	15.00
______	1961-2	11.00
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______	1962-3	22.00
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______	1963-2	12.00
______	1964-1-1	11.00
______	1964-1-2	12.00
______	1964-2	28.00
______	1965-1	19.00
______	1965-2	13.00
______	1966-1	15.00
______	1966-2	15.00
______	1967-1	11.00
______	1967-2	17.00
______	1968-1	15.00
______	1968-2	13.00
______	1969-1	15.00
______	1969-2	7.50
______	1969-3	14.00
______	1970-1	12.00
______	1970-2	(**)
______	1971-1	12.00
______	1971-2	17.00
______	1972-1	15.00
______	1972-2	15.00
______	1973-1	18.00
______	1973-2	15.00
______	1974-1	12.00
______	1974-2	11.00
______	*1974-3*	*9.50*
______	1974-3 Supp.	11.00
______	1975-1	15.00
______	1975-2	14.00
______	1976-1	12.00
______	1976-2	11.00
______	1976-3-1	10.00
______	1976-3-2	18.00
______	1976-3-3	11.00
______	1977-1	12.00
______	1977-2	13.00
______	1978-1	13.00
______	1978-2	14.00
______	1978-3-1	13.00
______	1978-3-2	9.50
______	1979-1	15.00
______	1979-2	17.00
______	1980-1	17.00
______	1980-2	19.00
______	1980-3	11.00
______	1981-1	19.00
______	1981-2	18.00
______	1982-1	17.00
______	1982-2	12.00
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______	1984-1	17.00
______	1984-2	30.00
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______	1985-1	28.00

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(*) Printed in one volume. (**) Out of print.

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretation.

INCOME TAX

Rev. Rul. 86-42, page 33.
Interest; prepayment of Rule of 78's loan. An individual borrower who prepays a loan subject to the Rule of 78's, and who has been using the economic accrual method to account for interest expense, may deduct as interest the difference between the final payment based upon application of the Rule of 78's and the final payment based upon the economic accrual of interest. An individual borrower who uses the Rule of 78's to account for interest expense, in circumstances where it is still permitted, may deduct as interest the amount allocated to interest using the Rule of 78's when the loan is prepaid. The same rules apply to lenders.

Rev. Rul. 86-44, page 39.
Indian tribal governments; treatment as states or political subdivisions. Rev. Ruls. 58-610, 68-231 and 74-179 are declared obsolete.

EMPLOYEE PLANS

T.D. 8073, page 4.
EE-96-85, page 48.
Temporary and proposed amendments to the regulations relate to effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984.

EXEMPT ORGANIZATIONS

Announcement 86-39, page 49.
A list is given of organizaitons now classified as private foundations.

EXCISE TAXES

Rev. Rul. 86-43, page 36.
Determination of gross vehicle weight; postponement of effective date of Rev. Rul. 85-196. Rev. Rul. 85-196 is modified to provide that its conclusion will not be applied to sales prior to October 1, 1986.

Rev. Rul. 86-45, page 36.
Windfall profit tax; severance tax adjustment; Wyoming. The taxes imposed under Wyo. Stat. sections 39-6-302(g) and (h) are severance taxes within the meaning of section 4996(c) of the Code. Rev. Rul. 82-87 amplified.

Rev. Rul. 86-46, page 37.
Windfall profit tax; severance tax adjustment; New Mexico. The taxes imposed under N.M. Stat. Ann. sections 7-29-4, 7-30-4, and 7-31-4 are severance taxes within the meaning of section 4996(c) of the Code. The state portion of the tax imposed under N.M. Stat. Ann. 7-32-4 is also a severance tax within the meaning of section 4996(c). The portion of the tax imposed for purposes of other governmental units is not a severance tax.

ADMINISTRATIVE

Rev. Proc. 86-17, page 40.
Indian tribal governments; treatment as states or political subdivisions. The two-year limit referred to in Rev. Procs. 83-87, 84-36 and 84-37 is no longer applicable. Rev. Procs. 83-87, 84-36 and 84-37 modified.

Rev. Proc. 86-18, page 40.
Redemptions of stock; revised checklist for ruling request. A revised checklist sets forth the information and representations to be included in a request for a ruling under sections 302 and 311 of the Code with respect to redemptions of stock. Rev. Proc. 81-62 superseded.

Announcement 86-41, page 50.
Publication 572, Investment Credit, contains an error in one of the examples.

Finding Lists begin on page 53.
Announcement of Suspensions on page 51.
Announcement of Notice of Proposed Rulemaking on page 52.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part 1. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 61.—Gross Income Defined

26 CFR 1.61-7: Interest.

What is the proper amount to include in income when a loan subject to the Rule of 78's is prepaid? See Rev. Rul. 86-42, page 33.

Section 72.—Annuities; Certain Proceeds of Endowment and Life Insurance Contracts

26 CFR 1.72(e)-1T: Treatment of distributions where substantially all contributions are employee contributions. (Temporary)
(Also Sections 79, 125, 133, 162, 402, 404, 419, 461, 463, 505, 512, 1024, 2039, 4976, 4978, 7701; 1.79-4T, 1.125-2T, 1.133-1T, 1.162-10, 1.402(a)(5)-1T, 1.404(a)-1T, 1.419-1T, 1.461(h)-4T, 1.463-1T, 1.505(c)-1T, 1.512(a)-5T, 1.1042-1T, 20.2039-1T, 54.4976-1T, 54.4978-1T, 301.7701-17T.)

T.D. 8073

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, SUBCHAPTER B, SUBCHAPTER C, PART 1—TEMPORARY INCOME TAX REGULATIONS UNDER THE TAX REFORM ACT OF 1984; PART 20—TEMPORARY ESTATE TAX REGULATIONS UNDER THE TAX REFORM ACT OF 1984; PART 54—TEMPORARY PENSION EXCISE TAX REGULATIONS UNDER THE TAX REFORM ACT OF 1984; PART 301—TEMPORARY PROCEDURE AND ADMINISTRATION REGULATIONS UNDER THE TAX REFORM ACT OF 1984; PART 602—REPORTING AND RECORDKEEPING REQUIREMENTS

Effective Dates And Other Issues Arising Under The Employee Benefit Provisions of The Tax Reform Act of 1984

AGENCY: Internal Revenue Service, Treasury

ACTION: Temporary regulations

SUMMARY: This document provides temporary regulations relating to effective dates and certain other issues arising under sections 91, 223, and 511-561 of the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 106, 283, 362-409]. This action is necessary because of changes to the applicable tax law made by the Tax Reform Act of 1984. The temporary regulations will affect qualified employee benefit plans, welfare benefit funds and employees receiving benefits through such plans.

DATES: As follows, the temporary regulations are to be effective on varying dates dependent upon the effective dates of the underlying provisions of the Internal Revenue Code of 1954. In general, the effective dates are as follows:

Regulations §	*Subject*	*Effective Date*
§1.72(e)-1T	Treatment of distributions	Amounts received or loans made after October 16, 1984.
§1.79-4T	Group-term life insurance	Generally, taxable years beginning after December 31, 1983.
§1.125-2T	Cafeteria plans	Cafeteria plan years beginning on or after January 1, 1985.
§1.133-1T	ESOP loan interest exclusion	Loans extended to an ESOP or sponsoring employer after July 18, 1984.
§1.402(a)(5)-1T	Rollover of partial distributions	Distributions made after July 18, 1984.
§1.404(a)-1T	Deduction of deferred compensation and benefits.	Generally, amounts paid or incurred after July 18, 1984.
§1.404(a)(8)-1T	Deductions for plan contributions	Taxable years beginning after December 31, 1983.
§1.404(b)-1T	Deduction of deferred compensation and benefits	Generally, amounts paid or incurred after July 18, 1984
§1.404(d)-1T	Deduction of deferred benefits to nonemployees	Generally, amounts paid or incurred after July 18, 1984.
§1.404(k)-1T	Deduction for dividends on stock held by ESOP	Dividends paid in employer taxable years beginning after July 18, 1984.
§1.419-1T	Funded welfare benefits plans	Generally, contributions paid or accrued after December 31, 1985.
§1.419A-1T	Qualified asset account, etc.	Generally, contributions paid or accrued after December 31, 1985.
§1.461(h)-3T	Economic performance requirement for certain employee benefits	Generally, contributions incurred in taxable years ending after July 18, 1984.
§1.463-1T	Transitional rule for vested accrued vacation benefits	First taxable year ended on or before July 18, 1984.
§1.505(c)-1T	Requirements for exemption	Taxable years beginning after July 18, 1984.

Regulations §	*Subject*	*Effective Date*
§1.512(a)-5T	Unrelated business income of exempt organizations	Generally, income earned after December 31, 1985.
§1.1042-1T	Sale of stock to ESOP	Taxable years beginning after July 18, 1984.
§20.2039-1T	Repeal of estate tax exclusion for qualified plans	Generally, estates of decendents dying after December 31, 1984.
§54.4976-1T	Taxes with respect to welfare benefit plans.	Generally, disqualified benefits provided after December 31, 1985.
§54.4978-1T	Tax on certain dispositions by the ESOP	Taxable years beginning after July 18, 1984.
§301.7701-17T	Collective bargaining plans and agreements	Generally, after March 31, 1984.

FOR FURTHER INFORMATION CONTACT: The attorneys indicated in the table below at the Employee Plans and Exempt Organizations Division or the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington, D.C. 20224 (Attention: CC:LR:T).

Regulation §	*Subject*	*Attorney/Telephone (not toll-free calls)*
§1.72(e)-1T	Treatment of distributions	Philip R. Bosco (202)566-3430
§1.79-4T	Group-term life insurance	Nancy J. Marks (202)566-3430
§1.125-2T	Cafeteria plans	Harry Beker (202)566-6212
§1.133-1T	ESOP loan interest exclusion	John T. Ricotta (202)566-3544
§1.402(a)(5)-1T	Rollover of partial distributions	Richard J. Wickersham (202)566-3430
§1.404(a)-1T	Deduction of deferred compensation and benefits	John T. Ricotta (202)566-3544
§1.404(a)(8)-1T	Deductions for plan contributions	Richard J. Wickersham (202)566-3430
§1.404(b)-1T	Deduction of deferred compensation and benefits	John T. Ricotta (202)566-3544
§1.404(d)-1T	Deduction of deferred benefits to nonemployees	John T. Ricotta (202)566-3544
§1.404(k)-1T	Deduction for dividends on stock held by ESOP	Calder L. Robertson (202)566-3544
§1.419-1T	Funded welfare benefits plans	John T. Ricotta (202)566-3544
§1.419A-1T	Qualified asset account, etc.	John T. Ricotta (202)566-3544
§1.461(h)-3T	Economic performance requirement for certain employee benefits	John T. Ricotta (202)566-3544
§1.463-1T	Transitional rule for vested accrued vacation pay	Annette Guarisco (202)566-3238
§1.505(c)-1T	Requirements for exemption	Sylvia F. Hunt (202)566-6212
§1.512(a)-5T	Unrelated business income of exempt organizations	John T. Ricotta (202)566-3544
§1.1042-1T	Sale of stock to ESOP	Sylvia F. Hunt (202)566-6212
§20.2039-1T	Repeal of estate tax exclusion for qualified plans	Richard J. Wickersham (202)566-3430

Regulation §	*Subject*	*Attorney/Telephone (not toll-free calls)*
§54.4976-1T	Taxes with respect to welfare benefit plans	John T. Ricotta (202)566-3544
§54.4978-1T	Tax on certain dispositions by an ESOP	John T. Ricotta (202)566-3544
§301.7701-17T	Collective bargaining plans and agreements	Philip R. Bosco (202)566-3430

SUPPLEMENTARY INFORMATION: BACKGROUND

This document contains temporary regulations relating to the economic performance requirement for certain employee benefits under section 461(h) of the Internal Revenue Code of 1954 (Code), as added by section 91 of the Tax Reform Act of 1984 (Act) (P.L. 98-369, 98 Stat. 598); the transitional rule for vested accrued vacation pay under section 463 of the Code, as amended by section 91(i) of the Act (P.L. 98-369, 98 Stat. 609); the treatment of the group-term life insurance purchased for employees under section 79 of the Code, as amended by section 223 of the Act (P.L. 98-369, 98 Stat. 775); the treatment of funded welfare benefit plans under sections 419 and 419A of the Code, as added by section 511 of the Act (P.L. 98-369, 98 Stat. 854); the treatment of unfunded deferred benefits under sections 404(b) and 162 of the Code, as amended by section 512 of the Act (P.L. 98-369, 98 Stat. 862); additional requirements for tax-exempt status of certain organizations under section 505 of the Code, as amended by section 513 of the Act (P.L. 98-369, 98 Stat. 863); rollovers of partial distributions under sections 402 and 403, as amended by section 522 of the Act (P.L. 98-369, 98 Stat. 868); distributions where substantially all contributions are employee contributions under section 72, as amended by section 523 of the Act (P.L. 98-369, 98 Stat. 871); repeal of the estate tax exclusion for qualified plan benefits under section 2039, as amended by section 525 of the Act (P.L. 98-369, 98 Stat. 873); determination of whether there is a collective bargaining agreement under section 7701(a)(46), as added by section 526(c) of the Act (P.L. 98-369, 98 Stat. 874); statutory nontaxable benefits under section 125, as amended by section 531(b) of the Act (P.L. 98-369, 98 Stat. 881); nonrecognition of gain on stock sold to an employee stock ownership plan (ESOP) under section 1042, as added by section 541 of the Act (P.L. 98-369, 98 Stat. 887); deductibility of dividends relating to ESOPs under sections 404 and 3405, as amended by section 542 of the Act (P.L. 98-369, 98 Stat. 890); exclusion of interest on ESOP loans under section 133, as added by section 543 of the Act (P.L. 98-369, 98 Stat. 891); excise tax on certain dispositions by ESOPs under section 4978, as added by section 545 of the Act (P.L. 98-369, 98 Stat. 894); treatment of an employer and an employee benefit association as related under section 1239, as amended by section 557 of the Act (P.L. 98-369, 98 Stat. 898); and technical corrections to the pension provisions of the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462] under sections 713 and 715 of the Act (P.L. 98-369, 98 Stat. 955, 966).

FORMAT

These temporary regulations are generally presented in the form of questions and answers. Taxpayers may rely on them for guidance pending the issuance of final regulations. The questions and answers are not, however, intended to address comprehensively the issues raised by sections 91, 223 and 511-561 of the Act and no inference should be drawn regarding questions not expressly raised and answered.

For purposes of developing a notice of proposed rule-making to provide comprehensive guidance under section 404(b) as amended by the Tax Reform Act of 1984, written comments are requested regarding whether, in place of the presumption established under Q&A-2 of §1.404(b)-1T, compensation or benefits should be considered unconditionally provided under a plan, or method or arrangement, deferring the receipt of compensation or providing for deferred benefits for purposes of section 404(a) and (d) and section 404(b) if paid beyond a 2½ month period following the close of the taxable year. In conjunction with the presumption and safe harbor rules of Q&A-2 of §1.404(b)-1T, consideration was given to providing additionally for a fixed period beyond the close of the taxable year (e.g., 8½ months) beyond which a payment would unconditionally be treated as deferred compensation or benefits for purposes of section 404. However, that approach was dismissed because of a concern that such a fixed period would inappropriately be regarded and utilized as an extended safe harbor within which a payment would be treated as not constituting deferred compensation or benefits for purposes of section 404.

Further, written comments are requested with respect to the treatment of an account as a "fund" for purposes of section 419(e)(3)(C). In particular, comments are requested regarding the application of Q&A-3 of §1.419-1T to experience-rated insurance arrangements between employers and insurance companies to provide welfare benefits to employees, and the application of §54.4976-1T to dividends and refunds under such arrangements. In addition, comments are requested regarding the inclusion of additional experience-rated arrangements in the definition of "welfare benefit fund" under section 419(e)(3)(C), particularly where there is a pooling or spreading of experience among different employers.

SPECIAL ANALYSES

No general notice of proposed rulemaking is required by 5 U.S.C. 553(b) for temporary regulations. Accordingly, the Regulatory Flexibility Act does not apply and a Regulatory Impact Analysis is not required for this rule. The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required.

PAPERWORK REDUCTION ACT

The collection of information requirements contained in this temporary regulation have been submitted to the Office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act of 1980. These requirements have been approved by OMB under control number 1545-0916.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Parts 1, 20, 54, 301, and 602 are amended as follows:

Par. 1. These amendments and additions to parts 1, 20, 54, and 301 are issued under the authority contained in 26 U.S.C. §7805. The authority citations for Parts 1, 20, 54 and 301 are unchanged.

INCOME TAX REGULATIONS
(26 CFR Part 1)

Par. 2. The following new sections are added after §1.72-18 to read as follows:

§1.72(e)-1T Treatment of distributions where substantially all contributions are employee contributions. (Temporary)

Q-1: How did the Tax Reform Act (TRA) of 1984 change the law with regard to the treatment of non-annuity distributions (i.e., amounts distributed prior to the annuity starting date and not received as annuities) from a qualified plan that is treated as a single contract under section 72 and under which substantially all of the contributions are employee contributions?

A-1: (a) Prior to the amendment to section 72(e) by the TRA of 1984, nonannuity distributions from such a qualified plan generally were allocable, first, to nondeductible employee contributions and thus were not includible in gross income. After distributions qualified the balance of nondeductible employee contributions, further nonannuity distributions generally were includible in gross income.

(b) Pursuant to section 72(e)(7), as added by the TRA of 1984, nonannuity distributions from such a qualified plan that are allocable to investment in the plan after August 13, 1982 (as determined in accordance with section 72(e)(5)(B)), generally will be treated, first, as allocable to income and, second, as allocable to nondeductible employee contributions. Distributions allocable to income are includible in gross income. Distributions allocable to nondeductible employee contributions are not includible in gross income.

Q-2: To which qualified plans and contracts does section 72(e)(7) apply?

A-2: Section 72(e)(7) applies to any plan or contract under which substantially all of the contributions are employee contributions if—

(a) Such plan is described in section 401(a) and the related trust or trusts are exempt from tax under section 501(a); or

(b) Such contract is—

(1) Purchased by a trust described in (a) above,

(2) Purchased as part of a plan described in section 403(a), or

(3) Described in section 403(b).

Q-3: What is the definition of a qualified plan or contract under which substantially all of the contributions are employee contributions?

A-3: (a) A qualified plan or contract under which substantially all of the contributions are employee contributions is a plan or contract with respect to which 85 percent or more of the total contributions during the "representative period" are employee contributions. The "representative period" means the five-plan-year period proceeding the plan year during which a distribution occurs. However, if less than 85 percent of the total contributions for all plan years during which the plan or contract is in existence prior to the plan year of distribution are employee contributions, then the plan or contract is not one with respect to which substantially all of the contributions are employee contributions.

(b) For purposes of the 85 percent test, contributions made to a predecessor plan or contract are aggregated with contributions made to the plan or contract to which the 85 percent test is being applied (the successor plan or contract). For purposes of the preceding sentence, a predecessor plan or contract is a plan or contract the terms of which are substantially the same as the successor plan or contract.

Q-4: What is the definition of employee contributions for purposes of section 72(e)(7)?

A-4: For purposes of section 72(e)(7), employee contributions are those amounts contributed by the employee and those amounts considered contributed by the employee under section 72(f). For example, amounts contributed to a section 401(k) qualified cash or deferred arrangements, pursuant to an employee's election to defer such amounts, are employer contributions to the extent that such amounts are not currently includible in gross income. In addition, deductible employee contributions under section 72(o) are disregarded in their entirety (i.e., treated as neither employee contributions nor employer contributions) in determining whether substantially all the contributions are employee contributions.

Q-5: How is the 85 percent test of section 72(e)(7) applied to a qualified plan or contract?

A-5: (a) Except as provided in paragraphs (b), (c), and (d), the 85 percent test is applied separately with respect to each contract under section 72.

(b) If a single qualified plan described in section 401(a) and section 403(a) comprises more than one contract under section 72, regardless of whether such plan includes multiple trusts or combinations of profit-sharing and pension features, these contracts are aggregated for purposes of applying the 85 percent test. Thus, if substantially all of the contributions under a qualified plan comprising two contracts under section 72 are employee contributions, section 72(e)(5)(D) shall not apply to non-annuity distributions under either of the contracts.

(c) With respect to the plans maintained by the Federal Government or by instrumentalities of the Federal Government, the 85 percent test shall be applied by aggregating all such plans. This aggregation rule applies only to those plans that are actively administered by the Federal Government or an instrumentality thereof. Thus, if a plan of the Federal government is administered by a commercial financial institution, it would not be aggregated with other plans of the Federal government and its instrumentalities for purposes of applying the 85 percent test.

(d) In the case of a contract described in section 403(b), the 85 percent test is applied separately to each such contract.

Q-6: Is a loan from a qualified plan or contract described in section 72(e)(7) treated as a distribution under section 72(e)(4)(A)?

A-6: Yes. Pursuant to section 72(e)(4)(A), if an employee receives, either directly or indirectly, any amount as a loan from a qualified plan or contract described in section 72(e)(7), such amount shall be treated as a distribution from the plan or contract of an amount not received as an annuity. Similarly, if an employee assigns or pledges, or agrees to assign or pledge, any portion of the value of any qualified plan or contract, such portion shall be treated as a distribution from the plan or contract of an amount not received as an annuity.

Q-7: Does the five percent penalty for premature distributions from annuity contracts, as described in section 72(q), apply to distributions from a qualified plan or contract described in section 72(e)(7)?

A-7: No.

Q-8: When is section 72(e)(7) effective?

A-8: Section 72(e)(7) is effective for amounts received or loans made on or after October 17, 1984. For purposes of this effective date provision, loan amounts outstanding on October 16, 1984, which are renegotiated, extended, renewed, or revised after that date generally are treated as loans made on a date of the renegotiation, etc.

Par. 3. There is added the following new section after §1.79-3:

§1.79-4T Questions and answers relating to the nondiscrimination requirements for group-term life insurance. (Temporary)

Q-1: When does section 79, as amended by the Tax Reform Act of 1984, become effective?

A-1: (a) Generally, section 79, as amended, applies to taxable years (of the employee receiving insurance coverage) beginning after December 31, 1983. There are, however, several exceptions to this effective date where there is coverage under a group-term life insurance plan of the employer that was in existence on January 1, 1984, or a comparable successor to such a plan maintained by the employer or a successor employer.

(b) First, the new rules of section 79(b) and (e), that require the inclusion in income of a retired employee of amounts attributable to the cost of group-term life insurnace in excess of $50,000 and that include former employees within the definition of the term "employee" will not apply to any employee who retired from employment on or before January 1, 1984.

(c) Second, in the case of an individual who retires after January 1, 1984, and before January 1, 1987, the new rules of section 79(b) and (e) do not apply if (1) and individual attained age 55 on or before January 1, 1984, and (2) the plan was maintained by the same employer who employed the individual during 1983, or by a successor employer.

(d) Third, in the case of an individual who retires after December 31, 1986, the new rules of section 79(b) and (e) do not apply if (1) the individual attained age 55 on or before January 1, 1984, (2) the plan was maintained by the same employer who employed the individual during 1983, or by a successor employer, and (3) the plan is not, after December 31, 1986, a discriminatory group-term life insurance plan (not taking into account any group-term life insurance coverage provided to employees who retired before January 1, 1987).

(e) For purposes of determining whether a plan is, after December 31, 1986, a discriminatory group-term life insurance plan, there shall be ignored any insurance coverage provided pursuant to a state law requirement that an insurer continue to provide insurance coverage for a period of time not in excess of two months following the termination of a policy.

Q-2: What is meant by a "group-term life insurance plan of the employer that was in existence on January 1, 1984"?

A-2: A group-term life insurance plan of the employer was in existence on January 1, 1984, only if the group policy or policies providing group-term life insurance benefits under the plan were executed on or before January 1, 1984, and were not terminated prior to such date. The applicability of section 79, as amended, to an employee will not be affected by the transfer of the employee between employers treated as a single employer under section 79(d)(7) if the employee continues, after the transfer, to be provided with group-term life insurance benefits under a plan that is comparable (determined under the principles set forth in Q&A 3) to the plan provided by the former employer.

Q-3: When is a plan of group-term life insurance a "comparable successor" to another such plan?

A-3: A plan of group-term life insurance will be a comparable successor to another plan of group-term life insurance (the first plan) only if the plan does not differ from the first plan in any significant aspect with respect to individuals who are potentially eligible for benefits provided under the grandfather provisions in Q&A 1. These individuals consist of those persons who are covered under a plan of group-term life insurance of the employer that was in existence on January 1, 1984, or a comprable successor to such a plan maintained by the employer or a successor employer, and who either retired on or before January 1, 1984, or who both attained age 55 on or before January 1, 1984, and were employed by the employer maintaining the plan (or a predecessor of that employer) during the year 1983. Accordingly, if significant additional or reduced benefits are provided only to individuals who are not described in the preceding sentence, the plan will be considered a comparable successor plan. A plan will not fail to be a comparable succesor plan merely because the employer purchases a policy or policies identical to the employer's first plan from a different insurance company. If the new plan provides significant additional or reduced benefits (either as to the type or amount available) to employees, or provides benefits to a category of employees that was formerly excluded from participating in the plan, the plan is generally not a comparable successor to the first plan. However, a plan will not be considered as providing significant additional or reduced benefits merely because a participant's coverage is based on a percentage of compensation and the participant's compensation for the taxable year has been increased or decreased. Furthermore, a plan will not be considered a non-comparable successor plan merely because it is amended, either to decrease benefits provided to key employees or to increase benefits provided to non-key employees, solely in order to comply with the nondiscrimination requirements of section 79(d). Finally, a plan will not be considered a noncomparable successor plan merely because a policy that is part of a discriminatory plan is terminated in order to end discriminatory coverage.

Q-4: For purposes of determining the effective date of section 79, as amended by the Tax Reform Act of 1984, what is a "successor employer"?

A-4: A successor employer is an employer who employs a group of individuals formerly employed by another employer as a result of a business merger, acquisition or division.

Q-5: Under what circumstances will separate policies of group-term life insurance of an employer be considered to be a single plan in determining whether the employer's plan of group-term life insurance is discriminatory?

A-5: All policies providing group-term life insurance to a common key employee or key employees (as defined in this Q&A) carried directly or indirectly by an employer (or by a group of employers described in section 79(d)(7)) will be considered as a single plan for purposes of determining whether an employer's group-term life insurance plan is discriminatory. For example, if a key employee receives $50,000 of group-term life insurance coverage under one policy and the same key employee receives an additional $250,000 of coverage under a separate group-term life insurance policy, the two policies will be treated as a single plan in determining whether the group-term life insurance provided by the employer is discriminatory. If it is discriminatory, the key employees covered by either policy will not receive the benefit of section 79(a)(1) or section 79(c) for either policy. The result is the same even if each policy, considered alone, would be nondiscriminatory. A policy that provides group-term life insurance to a key employee and a policy under which the same key employee is eligible to receive group-term life insurance upon separation from service will be considered to provide group-term life insurance to a common key employee. In addition, an employer may treat two or more policies that do not provide group-term life insurance to a common key employee as constituting a single plan for purposes of satisfying the nondiscrimination provisions of section 79(d). For example, if the employer provides group-term life insurance coverage for non-key employees under one policy and provides group-term life insurance coverge for key employees under a second policy, the two policies may be considered together in determining whether the requirements of section 79(d) are satisfied with regard to the second policy. For purposes of this section, the term "key employee" has the meaning given to such term by paragraph (1) of section 416(i), except that subparagraph (A)(iv) of such paragraph shall be applied by not taking into account employees described in section 79(d)(3)(B) who are not participants in the plan. For purposes of this section, all references to "plan year" or "plan years" in section 416(g)(4)(C) and seciton 416(i) shall be deleted and replaced with "taxable year of the employer" or "taxable years of the employer," respectively.

Q-6: In the case of a discriminatory group-term life insurance plan, what amounts should be included in the gross income of a key employee?

A-6: (a) In the case of a discriminatory group-term life insurance plan, each key employee must include in gross income for the taxable year the cost of his or her insurance benefit for that year provided by the employer under the plan.

(b) The cost of group-term life insurance coverage provided by an employer for a key employee during the employee's taxable year is determined by apportioning the net premium (group premium less policy dividends, premium refunds or experience rating credits) allocable to the group-term life insurance coverge during the key employee's taxable year, less the actual cost allocated to other key employees pursuant to the method described in the subparagraph (d) of this answer, if applicable, among the covered employees. In the event that the employer has other forms and types of coverage with the same insurer, the employer must make a reasonable allocation of the total premiums paid to the insurer. For example, where an employer has both health insurance coverage and a plan of group-term life insurance with the same insurer, and there is no volume discount, the net premium for the plan of group-term life insurance must include the excess, if any, of the payments the employer makes for the health insurance coverage over the payments the employer would make for such coverage if the plan of group-term life insurance for which this calculation is being made did not exist.

(c) In general, the portion of the net premium for group-term life insurance that should be apportioned to a key employee, other than a key employee to whom the method in subparagraph (d) of this answer is applicable, is determined by (1) calculating a "tabular" premium for the entire group (with the exception of all key employees to whom the method in subparagraph (d) of this answer is applicable), in the manner described below, (2) determining the ratio of the total actual net premium (less the actual cost allocated to key employees pursuant to the method of subparagraph (d) of this answer) to the total tabular premium and (3) multiplying the tabular premium for the key employee at his or her attained age by such ratio. Thus, if the total actual net premium is 125 percent of the total tabular premium for all covered employees and the tabular premium at the key employee's attained age is $2.00 per thousand per month, the cost of such employee would be $2.50 per thousand per month ($2.00 times 125 percent). For these purposes the table used to calculate tabular premiums will be determined as follows:

(i) If the group policy contains a reasonable table (based on recognized mortality assumptions) of premium rates on an attained age basis (which table may use age brackets not exceeding five years) with reference to which the group premium is determined, such table will be used;

(ii) If such table is not available, the 1960 Basic Group Table published by the Society of Actuaries will be used.

(d) In cases where the mortality charge for group-term life insurance coverage provided to a key employee is calculated separately by the insurer (for example, where the charge for the coverage provided to a key employee is based on a medical examination) and the amount of such mortality charge plus a proportionate share of the loading charge for the coverage provided to the group is higher than the amount that would be allocable to such employee under the allocation method in subparagraph (c) the cost of group-term life insurance coverage for the employee shall be that higher amount.

Q-7: Must all active and former employees be considered in applying the coverage tests in section 79(d)(3) to determine whether or not a plan of group-term life insurance is discriminatory with respect to coverage?

A-7: No. Generally, a plan of group-term life insurance which covers both active and former employees will not satisfy the nondiscrimination requirements of section 79(d) unless the coverage tests in section 79(d)(3) are satisfied with respect to both the active and the former employees of the employer, except to the extent they are excluded from tests for discrimination by application of the grandfather provisions set forth in Q&A 1. However, for purposes of determining whether a plan is discriminatory with respect to coverage, the coverage tests must be applied separately to active and former employees. In addition, if the plan limits participation by former employees to employees who retired from employment with the employer, then only retired employees must be considered in applying the coverage tests to former employees. Also, in applying the coverage tests in section 79(d)(3), the employer may make reasonable mortality assumptions regarding former employees who are not covered under the plan but must be considered in applying the coverage tests. Furthermore, only those former employees who terminated employment on or after the earliest date of termination from employment for any former employee covered by the plan must be considered. Finally, for purposes of determining whether a plan of group-term life insurance of the employer (or a successor employer) that was in existence on January 1, 1984 (or a comparable successor of such a plan) is discriminatory, after December 31, 1986, with respect to group-term life insurance coverage for former employees, coverge provided to employees who retired on or before December 31, 1986, shall not be taken into account.

Q-8: Will a group-term life insurance plan be considered discriminatory if active employees receive greater benefits as a percentage of compensation than former employees, or vice versa?

A-8: No. For purposes of determining whether a plan is discriminatory with respect to the type and amount of benefits available, insurance coverage for former employees must be tested separately from insurance coverage for active employees. For example, a group-term life insurance plan that provides group-term life insurance benefits equal to 200 percent of compensation for all active employees and 100 percent of final compensation (based on the average annual compensation for the final five years) for all former employees would satisfy the nondiscrimination requirements of section 79(d). However, a group-term life insurance plan that provides group-term life insurance benefits equal to 200 percent of compensation for all active employees and 100 percent of final compensation (based on the average annual compensation for the final five years) only for key employees who are no longer employed by the employer (or a successor employer) would not satisfy the nondiscrimnation requirement of section 79(d)(2)(A).

Q-9: Under what circumstances will the amount of benefits available under a plan of group-term life insurance be considered not to discriminate in favor of participants who are key employees?

A-9: A plan of group-term life insurance will be considered not to discriminate in favor of participants who are key employees, as to the amount of benefits available, if the plan provides a fixed amount of insurance which is the same for all covered employees. In other circumstances, the determination of whether a plan is nondiscriminatory will be based on all of the facts and circumstances. Such plans will be considered not to discriminate in favor of participants who are key employees, as to the amount of benefits available, if the plan contains no group of employees described in the following sentence that, if tested separately, would fail to satisfy the requirements of section 79(d)(2)(A). The group subject to separate testing under the preceding sentence consists of a key employee and all other participants (including other key employees) who receive, under the plan, an amount of insurance (as a multiple of compensation (either total compensation or the basic or regular rate of compensation)) that is equal to or greater than the amount of insurance received by such key employee. As described in Q&As 7&8, active and former employees are tested separately under section 79(d)(2)(A).

Example: Assume that a plan of group-term life insurance has 500 participants, 10 of whom are key employees. Under the plan, 400 of the non-key employees receive an amount of insurance equal to 100 percent of compensation, while all of the key employees and 90 of the non-key employees receive an amount of insurance equal to 200 percent of compensation. The plan will be considered not to discriminate in favor of the participants who are key employees because, tested separately, the group of participants receiving an amount of insurance equal to or greater than 200 percent of compensation would satisfy the requirements of section 79(d)(2)(A) (by reason of section 79(d)(3)(A)(ii)). If one of the key employees received an amount of insurance equal to 300 percent of compensation, the plan would be considered to discriminate in favor of participants who are key employees, because, tested separately, the group consisting of the single key employee receiving an amount of insurance equal to or greater than 300 percent of compensation would fail to satisfy the requirements of section 79(d)(2)(A).

In determining the groups of employees that are tested separately for this purpose, allowance shall be made for reasonable differences in amount of insurance (as a multiple of compensation) due to rounding, the use of compensation brackets or other similar factors. Thus, if a plan bases group-term life insurance coverage on "compensation brackets," it is not intended that any participants will be treated as receiving an amount of insurance (as a multiple of compensation) that is greater (or less) than that of any other participant merely because the first participant's compensation is at the lower (or higher) end of a compensation bracket while the second participant's compensation is at the higher (or lower) end of a compensation bracket. However, any compensation brackets utilized by a plan will be examined to determine if the brackets, or compensation groupings, result in discrimination in favor of key employees. In addition, a plan does not meet the requirements for nondiscrimination as to the type and amount of benefits available under the plan unless all types of benefits (including permanent benefits) and all terms and conditions with respect to such benefits which are available to any participant who is a key employee are also available on a nondiscriminatory basis to non-key employee participants.

Q-10: How is additional coverage

purchased by employees under a plan of group-term life insurance treated for purposes of determining whether a plan of group-term life insurance is discriminatory?

A-10: (a) The extent to which employees purchase additional coverage under a plan of group-term life insurance is not taken into account for purposes of determining whether a plan of group-term life insurance is discriminatory. For example, a plan providing insurance to all employees of 1 times annual compensation, which gives all employees the option to purchase additional insurance of 1 times annual compensation at their own expense, would not be considered discriminatory as to the type and amount of benefits available, even if the group (or groups) of participants who purchase additional insurance, if tested separately, would not satisfy the requirements of section 79(d)(2)(A). Solely for this purpose, the choice of an amount of group-term life insurance as a benefit under a cafeteria plan will be treated as the purchase of group-term life insurance by an employee. If additional insurance coverage is available to any key employee that is not available, on a nondiscriminatory basis, to non-key employees, the plan will be considered discriminatory, even if the full cost of such additional insurance coverage is paid by the employee(s) electing such benefits.

(b) If the employer bears a part of the expense of any additional coverage that is purchased by an employee under a plan of group-term life insurance, the additional insurance shall be treated, in part, as an amount of insurance provided by the employer under the plan and, in part, as an amount of insurance purchased by the employee. Except to the extent provided in subparagraph (a) above, the portion of insurance treated as an amount of insurance purchased by the employee is not taken into account for purposes of determining whether the plan is discriminatory. Whether such insurance (together with any other insurance provided by the employer under the plan) will cause the plan to be considered to discriminate in favor of participants who are key employees is determined under the rules of Q&A 9.

Q-11: What effect do the provisions of section 79(d)(1) have if a plan of group-term life insurance is discriminatory for only part of a year?

A-11: If a plan of group-term life insurance is discriminatory at any time during the key employee's taxable year, then it is a discriminatory group-term life insurance plan for that taxable year and the provisions of section 79(d)(1) will be applicable with respect to all group-term life insurance costs allocable to that employee for that year.

Q-12: Are the section 79(d) provisions independent from the requirements contained in Treas. Reg. §1.79-1?

A-12: Yes. Treas. Reg. §1.79-1(c)(1) provides that life insurance provided to a group of employees cannot qualify as group-term life insurance if it is provided to less than ten full-time employees unless certain requirements are satisfied. The satisfaction of these requirements does not guarantee that the plan will be nondiscriminatory, and vice versa. Treas. Reg. §1.79-1(a)(4) provides that life insurance is not group-term life insurance unless the amount of insurance provided to each employee is computed under a formula that precludes individual selection. The mere fact that a life insurance policy is nondiscriminatory is not determinative as to whether the policy precludes individual selection, and vice versa.

Par. 4. The following section is added immediately after §1.125-1:

§1.125-2T Question and answer relating to the benefits that may be offered under a cafeteria plan. (Temporary)

Q-1: What benefits may be offered to participants under a cafeteria plan?

A-1: (a) Generally, for cafeteria plan years beginning on or after January 1, 1985, a cafeteria plan is a written plan under which participants may choose among two or more benefits consisting of cash and certain other permissible benefits. In general, benefits that are excludable from the gross income of an employee under a specific section of the Internal Revenue Code may be offered under a cafeteria plan. However, scholarships and fellowships under section 117, vanpooling under section 124, educational assistance under section 127 and certain fringe benefits under section 132 may not be offered under a cafeteria plan. In addition, meals and lodging under section 119, because they are furnished for the convenience of the employer and thus are not elective in lieu of other benefits or compensation provided by the employer, may not be offered under a cafeteria plan. Thus, a cafeteria plan may offer coverage under a group-term life insurance plan of up to $50,000 (section 79), coverage under an accident or health plan (sections 105 and 106), coverage under a qualified group legal services plan (section 120), coverage under a dependent care assistance program (section 129), and participation is a qualified cash or deferred arrangement that is part of a profit-sharing or stock bonus plan (section 401(k)). In addition, a cafeteria plan may offer group-term life insurance coverage which is includible in gross income only because it is in excess of $50,000 or is on the lives of the participant's spouse and/or children. In addition, a cafeteria plan may offer participants the opportunity to purchase, with after-tax employee contributions, coverage under a group-term life insurance plan (section 79), coverage under an accident or health plan (section 105(e)), coverage under a qualified group legal services plan (section 120), or coverage under a dependent care assistance program (section 129). Finally, a cafeteria plan may offer paid vacation days if the plan precludes any participant from using, or receiving cash for, in a subsequent plan year, any of such paid vacation days remaining unused as of the end of the plan year. For purposes of the preceding sentence, elective vacation days provided under a cafeteria plan are not considered to be used until all nonelective paid vacation days have been used.

(b) Note that benefits that may be offered under a cafeteria plan may or may not be taxable depending upon whether such benefits qualify for an exclusion from gross income. However, a cafeteria plan may not offer a benefit that is taxable because such benefit fails to satisfy any applicable eligibility, coverage, or nondiscrimination requirement. Similiarly, a plan may not offer a benefit for purchase with after-tax employee contributions if such benefit would fail to satisfy any eligibility, coverage, or nondiscrimination requirement that would apply if such benefit were designed to be provided on a nontaxable basis with employer contributions. Also, note that section 125(d)(2) provides that a cafeteria plan may not offer a benefit that defers the receipt of compensation (other than the opportunity to make elective contributions under a qualified cash or deferred arrangement) and may not operate in a manner that enables participants to defer the receipt of compensation.

Par. 5. The following new section is added immediately after §1.132-1T:

§1.133-1T. Questions and answers relating to interest on certain loans used to acquire employer securities. (Temporary)

Q-1: What does section 133 provide?

A-1: In general, section 133 provides that certain commercial lenders may exclude from gross income fifty percent of the interest received with respect to securities acquisition loans. A securities acquisition loan is any loan to an employee stock ownership plan (ESOP) (as defined in section 4975(e)(7)) that qualifies as an exempt loan underr §54.4975-7 and 11 to the extent that the proceeds are used to acquire employer securities (within the meaning of section 409(l)) for the ESOP. A loan made to a corporation sponsoring an ESOP (or to a person related to such corporation under section 133(b)(2)) may also qualify as a securities acquisition loan to the extent and for the period that the proceeds are (a) loaned to the corporation's ESOP under a loan that qualifies as an exempt loan under §54.4975-7 and -11 and that has substantially similar terms as the loan from the commercial lender to the sponsoring corporation, and (b) used to acquire employer securities for the ESOP. The terms of the loan between the commercial lender and the sponsoring corporation (or a related corporation) and the loan between such corporation and the ESOP shall be treated as substantially similar only if the timing and rate at which employer securities would be released from encumbrance if the loan from the commercial lender were the exempt loan under the applicable rule of §54.4975-7(b)(8) are substantially similar to the timing and rate at which employer securities will actually be released from encumbrance in accordance with such rule. For this purpose, if the loan from the commercial lender to the sponsoring corporation states a variable rate of interest and the loan between the corporation and the ESOP states a fixed rate of interest, whether the terms of the loans are substantially similar shall be determined at the time the obligations are initially issued by taking into account the adjustment interval on the variable rate loan and the maturity of the fixed rate loan. For example, if the rate on the loan from the commercial lender to the sponsoring corporation adjusts each six months and the loan from the corporation to the ESOP has a ten year term, the initial interest rate on the variable rate loan could be compared to the rate on the fixed rate loan by comparing the yields on 6 month and ten year Treasury obligations. Similarly, if the rates on the two loans are based on different compounding assumptions, whether the terms of the loans are substantially similar shall be determined by taking into account the different compounding assumptions. A securities acquisition loan may be evidenced by any note, bond, debenture, or certificate. Also, section 133(b)(2) provides that certain loans between related persons are not securities acquisition loans. In addition, a loan from a commercial lender to an ESOP or sponsoring corporation to purchase employer securities will not be treated as a securities acquisition loan to the extent that such loan is used, either directly or indirectly, to purchase employer securities from any other qualified plan, including any other ESOP, maintained by the employer or any other corporation which is a member of the same controlled group (as defined in section 409(l)(4)).

Q-2: What lenders are eligible to receive the fifty percent interest exclusion?

A-2: Under section 133(a), a bank (within the meaning of section 581), an insurance company to which subchapter L applies, or a corporation (other than a subchapter S corporation) actively engaged in the business of lending money may exclude from gross income fifty percent of the interest received with respect to a securities acquisition loan (as defined in Q&A-1 of §1.133-1T). For purposes of section 133(a)(3), a corporation is actively engaged in the business of lending money if it lends money to the public on a regular and continuing basis (other than in connection with the purchase by the public of goods and services from the lender or a related party). A corporation is not actively engaged in the business of lending money if a predominant share of the original value of the loans it makes to unrelated parties (other than in connection with the purchase by the public of goods and services from the lender or a related party) are securities acquisition loans.

Q-3: May loans which qualify for the fifty percent interest exclusion under section 133 be syndicated to other lending institutions?

A-3: Securities acquisition loans under section 133 may be syndicated to other lending institutions provided that such lending institutions are described in section 133(a)(1), (2) or (3) and the loan was originated by a qualified holder. Subsequent holders of the debt instrument may qualify for the partial interest exclusion of section 133 if such holders satisfy the requirements of section 133 and such loan does not fail to be a securities acquisition loan under section 133(b)(2).

Q-4: When is section 133 effective?

A-4: Section 133 applies to securities acquisition loans made after July 18, 1984, and used to acquire employer securities after July 18, 1984. The provision does not apply to loans made after July 18, 1984, to the extent that such loans are renegotiations, directly or indirectly, of loans outstanding on such date. A loan extended to an ESOP or sponsoring corporation after July 18, 1984, will be treated as a renegotiation of an outstanding loan if the loan proceeds are used to refinance acquisitions of employer securities made prior to July 19, 1984. For example, if an ESOP borrowed money prior to July 19, 1984, to purchase employer securities and after July 18, 1984, borrows other funds from the same or a different commercial lender to repay the first loan, the second loan will be treated as a renegotiation of an outstanding loan to the extent of the repaid amount. Similarly, if, after July 18, 1984, an ESOP sells employer securities, uses the proceeds to retire a pre-July 19, 1984, loan and obtains a second loan to acquire replacement employer securities, the second loan will be treated as a renegotiation of an outstanding loan.

Par. 6. The following new section is added immediately after §1.162-10:

§1.162-10T Questions aand answers relating to the deduction of employee benefits under the Tax Reform Act of 1984; certain limits on amounts deductible. (Temporary)

Q-1: How does the amendment of section 404(b) by the Tax Reform Act of 1984 affect the deduction of employee benefits under section 162 of the Internal Revenue Code?

A-1: As amended by the Tax Reform Act of 1984, section 404(b) clarifies that section 404(a) and (d) (in the case of employees and nonemployees, respectively) shall govern the deduction of contributions paid or compensation paid or incurred under a plan, or method or arrangement, deferring the receipt of compensation or providing for deferred benefits. Section 404(a) and (d) requires that such a contribution or compensation be paid or incurred for purposes of section 162 or 212 and satisfy the requirements for deductibility under either of these sections. However, notwithstanding the above, section 404 does not apply to contributions paid or accrued with respect to a "welfare benefit fund" (as defined in section 419(e)) after July 18, 1984, in taxable years of employers (and payors) ending after that date. Also, section 463 shall govern the deduction of vacation pay by a taxpayer that has elected the application of such section. Section 404(b), as amended, generally applies to contributions paid and compensation paid or incurred after July 18, 1984, in taxable years of employers (and payors) ending after that date. See Q&A-3 of §1.404(b)-1T. For rules relating to the deduction of contributions attributable to the provision of deferred benefits, see section 404(a), (b) and (d) and §1.404(a)-1T, §1.404(b)-1T and §1.404(d)-1T. For rules relating to the deduction of contributions paid or accrued with respect to a welfare benefit fund, see section 419, §1.419-1T and §1.419A-2T. For rules relating to the deduction of vacation pay for which an election is made under section 463, see §10.2 of this chapter and §1.463-1T.

Q-2: How does the enactment of section 419 by the Tax Reform Act of 1984 affect the deduction of employee benefits under section 162?

A-2: As enacted by the Tax Reform Act of 1984, section 419 shall govern the deduction of contributions paid or accrued by an employer (or a person receiving services under section 419(g)) with respect to a "welfare benefit fund" (within the meaning of section 419(e)) after December 31, 1985, in taxable years of the employer (or person receiving the services) ending after that date. Section 419)(a) requires that such a contribution be paid or accrued for purposes of section 162 or 212 and satisfy the requirements for deductibility under either of those sections. Generally, subject to a binding contract exception (as described in section 511(e)(5) of the Tax Reform Act of 1984), section 419 shall also govern the deduction of the contribution of a facility (or other contribution used to acquire or improve a facility) to a welfare benefit fund after June 22, 1984. See Q&A-11 of §1.419-1T. In the case of a welfare benefit fund maintained pursuant to a collective bargaining agreement, section 419 applies to the extent provided under the special effective date rule described in Q&A-2 of §1.419-1T and the special rules of §1.419-2T. For rules relating to the deduction of contributions paid or accrued with respect to a welfare benefit fund, see section 419 and §1.419-1T.

Par. 7. The following new section is added after §1.402(a)-1 to read as follows:

§1.402(a)(5)-1T Rollovers of partial distributions from qualified trusts and annuities. (Temporary)

Q-1: Can an employee or the surviving spouse of a deceased employee roll over to an individual retirement account or annuity, described in section 408(a) or (b), the taxable portion of a partial distribution from a qualified trust described in section 401(a), a qualified plan described in section 403(a), or a tax-sheltered annuity contract under section 403(b)?

A-1: Yes. For distributions made after July 18, 1984, the taxable portion of a partial distribution may be rolled over within 60 days of the distribution to an individual retirement account or annuity.

Q-2: Are there special requirements applicable to roll-overs of partial distributions?

A-2: Yes. Section 402(a)(5)(D)(i) specifies that no part of a partial distribution may be rolled over unless the distribution is equal to at least 50 percent of the balance to the credit of the employee in the contract or plan immediately before the distribution, and the distribution is not one of a series of periodic payments. For purposes of this section, the balance to the credit of an employee does not include any accumulated deductible employee contributions (within the meaning of section 72(o)). In addition, in calculating the balance to the credit for purposes of the 50 percent test, qualified plans are not to be aggregated with other qualified plans and tax-sheltered annuity contracts are not to be aggregated with other tax-sheltered annuity contracts. Also, in applying the 50 percent test to a surviving spouse, the balance to the credit is the maximum amount the spouse is entitled to receive under the plan or contract, rather than the total balance to the credit of the employee. The rollover of a partial distribution may result in adverse tax consequences; see section 402(a)(5)(D)(iii) and (iv).

Q-3: Are there any other requirements applicable to rollovers of partial distribution?

A-3: Yes. Section 402(a)(5)(i)(III) requires the employee to elect, in conformance with Treasury regulations, to treat a contribution of a partial distribution to an IRA as a rollover contribution. An election is made by designating, in writing, to the trustee or issuer of the IRA at the time of the contribution that the contribution is to be treated as a rollover contribution. This requirement of a written designation to the trustee or issuer of the IRA is effective for contributions paid to the trustee or issuer of the IRA after March 20, 1986. For contributions paid to the trustee or issuer before March 21, 1986, an election is made by computing the individual's income tax liability on the income tax return for the taxable year in which the distribution occurs in a manner consistent with not including the distribution (or portion thereof) in gross income. Both such elections are irrevocable, except that an election made on an income tax return filed before March 21, 1986 is revocable.

Q-4: Does the election requirement apply to rollovers of qualified total distributions or rollover contributions described in section 402(a)(5) or (7), 403(a)(4), 403(b)(8), 405(d)(3), or 408(d)(3) to individual retirement accounts and annuities (IRAs)?

A-4: Yes. No amounts may be treated as a rollover contribution to an

IRA under section 402(a)(5), 402(a)(7), 403(a)(4), 403(b)(8), 405(d)(3) (as amended by section 491(c) of the TRA of 1984), or 408(d)(3) unless the requirements described in Q & A-3 of this section are satisfied. Thus, once any portion of a total distribution is irrevocably designated as a rollover contribution, such distribution is not taxable under section 402 or 403 and, therefore, is not eligible for the special capital gains and separate tax treatment under section 402(a) and (e). Election requirements for rollover contributions to IRAs described in this Q&A-4 are subject to the same effective date rules set forth in Q&A-3.

Par. 8. The following new section is added immediately after §1.404(a)-1:

§1.404(a)-1(T) Questions and answers relating to deductibility of deferred compensation and deferred benefits for employees. (Temporary)

Q-1: How does the amendment of section 404(b) by the Tax Reform Act of 1984 affect the deduction of contributions or compensation under section 404(a)?

A-1: As amended by the Tax Reform Act of 1984, section 404(b) clarifies that section 404(a) shall govern the deduction of contributions paid and compensation paid or incurred by the employer under a plan, or method or arrangement, deferring the receipt of compensation or providing for deferred benefits to employees, their spouses, or their dependents. See section 404(b) and §1.404(b)-1T. Section 404(a) and (d) requires that such a contribution or compensation be paid or incurred for purposes of section 162 or 212 and satisfy the requirements for deductibility under either of those sections. However, notwithstanding the above, section 404 does not apply to contributions paid or accrued with respect to a "welfare benefit fund" (as defined in section 419(e)) after July 18, 1984, in taxable years of employers (and payors) ending after that date. Also, section 463 shall govern the deduction of vacation pay by a taxpayer that has elected the application of such section. For rules relating to the deduction of contributions paid or accrued with respect to a welfare benefit fund, see section 419, §1.419-1T and §1.419A-2T. For rules relating to the deduction of vacation pay for which an election is made under section 463, see §10.2 of this chapter and §1.463-1T.

Par. 9. The following new section is added after §1.404(a)-8 to read as follows:

§1.404(a)(8)-1T Deductions for plan contributions on behalf of self-employed individuals. (Temporary)

Q: How does the amendment to section 404(a)(8)(D), made by section 713(d)(6) of the Tax Reform Act of 1984 (TRA of 1984), affect section 404(a)(8)(C)?

A: In applying the rules of section 404(a)(8)(C), the Service will treat the amendment to section 404(a)(8)(D) as also having been made to section 404(a)(8)(C), pending enactment of technical corrections to TRA of 1984. The effect of treating the amendments as having also been made to section 404(a)(8)(C) is to increase the amount of contributions on behalf of a self-employed individual that will be treated as satisfying section 162 or 212. Generally, therefore, a contribution on behalf of a self-employed individual is treated as satisfying section 162 or 212 if it is not in excess of the individual's earned income for the year, determined without regard to the deduction allowed by section 404 for the self-employed individual's contribution.

Par. 10. The following new section is added immediately after §1.404(b)-1:

§1.404(b)-1T Method or arrangement of contributions, etc., deferring the receipt of compensation or providing for deferred benefits. (Temporary)

Q-1: As amended by the Tax Reform Act of 1984, what does section 404(b) of the Internal Revenue Code provide?

A-1: As amended, section 404(b) clarifies that any plan, or method of arrangement, deferring the receipt of compensation or providing for deferred benefits (other than compensation) is to be treated as a plan deferring the receipt of compensation for purposes of section 404(a) and (d). Accordingly, section 404(a) and (d) (in the case of employees and nonemployees, respectively) shall govern the deduction of contributions paid or compensation paid or incurred with respect to such a plan, or method or arrangement. Section 404(a) and (d) requires that such a contribution or compensation be paid or incurred for purposes of section 162 or 212 and satisfy the requirements for deductibility under either of those sections. Thus, for example, under section 404(a)(5) and (b), if otherwise deductible under section 162 or 212, a contribution paid or incurred with respect to a nonqualified plan, or method or arrangement, providing for deferred benefits is deductible in the taxable year of the employer in which or with which ends the taxable year of the employee in which the amount attrributable to the contribution is includible in the gross income of the employee (without regard to any applicable exclusion under Chapter 1, Subtitle A, of the Internal Revenue Code). Section 404(a) and (d) applies to all compensation and benefit plans, or methods or arrangements, however denominated, which defer the receipt of any amount of compensation or benefit, including fees or other payments. Thus, a limited partnership (using the accrual method of accounting) may not accrue deductions for a fee owed to an unrelated person (using the cash method of accounting) who performs services for the partnership until the partnership taxable year in which or within which ends the taxable year of the service provider in which the fee is included in income. However, notwithstanding the above, section 404 does not apply to contributions paid or accrued with respect to a "welfare benefit fund" (as defined in section 419(e)) after July 18, 1984, in taxable years of employers (and payors) ending after that date. Also, section 463 shall govern the deduction of vacation pay by a taxpayer that has elected the application of such section. For rules relating to the deduction of contributions paid or accrued with respect to a welfare benefit fund, see section 419, §1.419-T and §1.419A-2T. For rules relating to the deduction of vacation pay for which an election is made under section 463, see §10.2 of this chapter and §1.463-1T.

Q-2: When does a plan, or method or arrangement, defer the receipt of compensation or benefits for purposes of section 404(a), (b), and (d)?

A-2: (a) For purposes of section 404(a), (b), and (d), a plan, or method or arrangement, defers the receipt of compensation or benefits to the extent it is one under which an employee receives compensation or benefits more than a brief period of time after the end of the employer's taxable year in which the services creating the right to such compensation or benefits are performed. The determination of whether a plan, or method or arrangement, defers the receipts of compensation or benefits is made separately with respect to each employee and each amount of compensation or benefit. Compensation or benefits received by an employee's spouse or dependent or any other person, but taxable to the employee, are treated as received by the employee for purposes of section 404. An employee is determined to receive compensation or benefits within or beyond a brief period of time after the end of the employer's taxable year under the rules provided in this Q&A. For the treatment of expenses with respect to transactions between related taxpayers, see section 267.

(b)(1) A plan, or method or arrangement, shall be presumed to be one deferring the receipt of compensation for more than a brief period of time after the end of an employer's taxable year to the extent that compensation is received after the 15th day of the 3rd calendar month after the end of the employer's taxable year in which the related services are rendered ("the 2½ month period"). Thus, for example, salary under an employment contract or a bonus under a year-end bonus declaration is presumed to be paid under a plan, or method or arrangement, deferring the receipt of compensation, to the extent that the salary or bonus is received beyond the applicable 2½ month period. Further, salary or a year-end bonus received beyond the applicable 2½ month period by one employee shall be presumed to constitute payment under a plan, or method or arrangement, deferring the receipt of compensation for such employee even though salary or bonus payments to all other employees are not similarly treated because they are received within the 2½ month period. Benefits are "deferred benefits" if, assuming the benefits were cash compensation, such benefits would be considered deferred compensation. Thus, a plan, or method or arrangement, shall be presumed to be one providing for deferred benefits to the extent benefits for services are received by an employee after the 2½ month period following the end of the employer's taxable year in which the related services are rendered.

(2) The taxpayer may rebut the presumption established under the previous subparagraph with respect to an amount of compensation or benefits only by setting forth facts and circumstances the preponderance of which demonstrates that it was impracticable, either administratively or economically, to avoid the deferral of the receipt by an employee of the amount of compensation or benefits beyond the applicable 2½ month period and that, as of the end of the employer's taxable year such impracticability was unforeseeable. For example, the presumption may be rebutted with respect to an amount of compensation to the extent that receipt of such amount is deferred beyond the applicable 2½ month period (i) either because the funds of the employer were not sufficient to make the payment within the 2½ month period without jeopardizing the solvency of the employer or because it was not reasonably possible to determine within the 2½ month period whether payment of such amount was to be made, and (ii) the circumstance causing the deferral described in (i) was unforeseeable as of the close of the employer's taxable year. Thus, the presumption with respect to the receipt of an amount of compensation or benefit is not rebutted to the extent it was foreseeable, as of the end of the employer's taxable year, that the amount would be received after the applicable 2½ month period. For example, if, as of the end of the employer's taxable year, it is foreseeable that calculation of a year-end bonus to be paid to an employee under a given formula will not be completed and thus the bonus will not be received (and is in fact not received) by the end of the applicable 2½ month period, the presumption that the bonus is deferred compensation is not rebutted.

(c) A plan, or method or arrangement, shall not be considered as deferring the receipt of compensation or benefits for more than a brief period of time after the end of the employer's taxable year to the extent that compensation or benefits are received by the employee on or before the end of the applicable 2½ month period. Thus, for example, salary under an employment contract or a bonus under a year-end bonus declaration is not considered paid under a plan, or method or arrangement, deferring the receipt of compensation to the extent that such salary or bonus is received by the employee on or before the end of the applicable 2½ month period.

(d) Solely for purposes of applying the rules of paragraphs (b) and (c) of this Q&A, in the case of an employer's taxable year ending on or after July 18, 1984, and on or before March 21, 1986, compensation or benefits that relate to services rendered in such taxable year shall be deemed to have been received within the applicable 2½ month period if such receipt actually occurs after such 2½ month period but on or before March 21, 1986.

Q-3: When does section 404(b), as amended by the Tax Reform Act of 1984, become effective?

A-3: With the exceptions discussed below, section 404(b), as amended, and the rules under Q&A-2 are effective with respect to amounts paid or incurred after July 18, 1984, in taxable years of employers (and payors) ending after that date. In the case of an extended vacation pay plan maintained pursuant to a collective bargaining agreement (i) between employee representatives and one or more employers, and (ii) in effect on June 22, 1984, section 404(b) is not effective before the date on which such collective bargaining agreement terminates (determined without regard to any extension thereof agreed to after June 22, 1984). For purposes of the preceding sentence, any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added under section 512 of the Tax Reform Act of 1984 shall not be treated as a termination of such collective bargaining agreement. For purposes of this section, an "extended vacation pay plan" is one under which covered employees gradually over a specified period of years earn the right to additional vacation benefits, no part of which, under the terms of the plan, can be taken until the end of the specified period.

Par. 11. Section 1.404(d)-1 is removed and the following new section is added in its place.

§1.404(d)-1T Questions and answers relating to deductibility of deferred compensation and deferred benefits for independent contractors. (Temporary)

Q-1: How does the amendment of section 404(b) by the Tax Reform Act of 1984 affect the deduction of contributions or compensation under section 404(d)?

A-1: As amended by the Tax Reform Act of 1984, section 404(b) clarifies that section 404(d) shall govern the deduction of contributions paid and compensation paid or incurred by a payor under a plan, or method or arrangement, deferring benefits for service providers with respect to which there is no employer-employee relationship. In such a case, section 404(a) and (b) and the regulations thereunder apply as if the person providing the services were the employee and the person to whom the services are provided were the employer. Section 404(a) requires that such a contribution or compensation be paid or incurred for purposes of section 162 or 212 and satisfy the requirements for deductibility under either of those sections. However, notwithstanding the above, section 404 does not apply to contributions paid or accrued with respect to a "welfare benefit fund" (as defined in section 419(e)) after June 18, 1984, in taxable years of employers (and payors) ending after the date. Also, section 463 shall govern the deduction of vacation pay by a taxpayer that has elected under such section. For rules relating to the deduction of contributions paid or accrued with respect to a welfare benefit fund, see section 419, §1.419-1T and §1.419A-2T. For rules relating to the deduction of vacation pay for which an election is made under section 463, see §10.2 of this chapter and §1.463-1T.

Par. 12. The following new section is added immediately after §1.404(e)-1A:

§1.404(k)-1T Questions and answers relating to the deductibility of certain dividend distributions. (Temporary)

Q-1: What does section 404(k) provide?

A-1: Section 404(k) allows a corporation a deduction for dividends actually paid in accordance with section 404(k)(2) with respect to stock of such corporation held by an employee stock ownership plan (as defined in section 4975(e)(7)) maintained by the corporation (or by any other corporation that is a member of a "controlled group of corporations" within the meaning of section 409(l)(4) that includes the corporation), but only if such dividends may be immediately distributed under the terms of the plan and all of the applicable qualification and distribution rules. The deduction is allowed under section 404(k) for the taxable year of the corporation during which the dividends are received by the participants.

Q-2: Is the deductibility of dividends paid to plan participants under section 404(k) affected by a plan provision which permits participants to elect to receive or not receive payment of dividends?

A-2: No. Dividends actually paid in cash to plan participants in accordance with section 404(k) are deductible under section 404(k) despite such an election provision.

Q-3: Are dividends paid in cash directly to plan participants by the corporation and dividends paid to the plan and then distributed in cash to plan participants under section 404(k) treated as distributions under the plan holding stock to which the dividends relate for purposes of sections 72, 401 and 402?

A-3 Generally, yes. However, a deductible dividend under section 404(k) is treated for purposes of section 72 as paid under a contract separate from any other contract that is part of the plan. Thus, a deductible dividend is treated as a plan distribution and as paid under a separate contract providing only for payment of deductible dividends. Therefore, a deductible dividend under section 404(k) is a taxable plan distribution even though an employee has unrecovered employee contributions or basis in the plan.

Par. 13. A new §1.419-1T is added immediately following §1.417(e)-1T to read as follows:

§1.419-1T Treatment of welfare benefit funds. (Temporary)

Q-1: What does section 419 of the Internal Revenue Code provide?

A-1: Section 419 prescribes limitations upon deductions for contributions paid or accrued with respect to a welfare benefit fund. Under section 419(a) and (b), an employer's contributions to a welfare benefit fund are not deductible under section 162 (relating to trade or business expenses) or section 212 (relating to expenses for production of income) but, if the requirements of section 162 or 212 are otherwise met, are deductible under section 419 for the taxable year of the employer in which paid to the extent of the welfare benefit fund's qualified cost (within the meaning of section 419(c)(1)) for the taxable year of the fund that relates to such taxable year of the employer. Under section 419(g), section 419 and this section shall also apply to the deduction by a taxpayer of contributions with respect to a fund that would be a welfare benefit fund but for the fact that there is no employer-employee relationship between the person providing the services and the person for whom the services are provided. Contributions paid to a welfare benefit fund after section 419 becomes effective with respect to such contributions are deemed to relate, first, to amounts accrued and deducted (but not paid) by the employer with respect to such fund before section 419 becomes effective with respect to such contributions and thus shall not be treated as satisfying the payment requirement of section 419. See paragraph (b) of Q&A-5 for special deduction limits applicable to employer contributions to welfare benefit funds with excess reserves.

Q-2: When do the deducton rules of section 419, as enacted by the Tax Reform Act of 1984, become effective?

A-2: (a) Section 419 generally applies to contributions paid or accrued with respect to a welfare benefit fund after December 31, 1985, in taxable years of employers ending after that date. See Q&A-9 of this regulation for special rules relating to the deduction limit for the first taxable year of a fiscal year employer ending after December 31, 1985.

(b) In the case of a welfare benefit fund which is part of a plan maintained pursuant to one or more collective bargaining agreements (a) between employee representatives and one or more employers, and (b) that are in effect on July 1, 1985 (or ratified on or before such date), section 419 shall not apply to contributions paid or accrued in taxable years beginning before the termination of the last of the collective bargaining agreements pursuant to which the plan is maintained (determined without regard to any extension thereof agreed to after July 1, 1985). For purposes of the preceding sentence, any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added under section 511 of the Tax Reform Act of 1984 (i.e., requirements under section 419, 419A, 512(a)(3)(E), and 4976) shall not be treated as a termination of such collective bargaining agreement. See §1.419A-2T for special rules relating to the application of section 419 to collectively bargained welfare benefit funds.

(c) Notwithstanding paragraphs (a) and (b), section 419 applies to any contribution of a facility to a welfare benefit fund (or other contribution, such as cash, which is used to acquire, construct, or improve such a facility) after June 22, 1984, unless such facility is placed in service by the fund before January 1, 1987, and either (a) is acquired or improved by the fund (or contributed to the fund) pursuant to a binding contract in effect on June 22, 1984, and at all times thereafter, or (b) the construction of which was begun by or for the welfare benefit fund before June 22, 1984. See Q&A-11 of this regulation for special rules relating to the application of section 419 to the contribution of a facility to a welfare benefit fund (and to the contribution of other amounts, such as cash, used to acquire, construct, or improve such a facility) before section 419 generally becomes effective with respect to contributions to the fund.

Q-3. What is a "welfare benefit fund" under section 419?

A-3. (a) A "welfare benefit fund" is any fund which is part of a plan, or method or arrangement, of an employer and through which the employer provides welfare benefits to employees or their beneficiaries. For purposes of this section, the term "welfare benefit" includes any benefit other than a benefit with respect to which the employer's deduction is governed by section 83(h), section 404 (determined without regard to section 404(b)(2)), section 404A, or secition 463.

(b) Under section 419(e)(3)(A) and (B), the term "fund" includes any organization described in section 501(c)(7), (9), (17) or (20), and any trust, corporation, or other organization not exempt from tax imposed by chapter 1, subtitle A, of the Internal Revenue Code. Thus, a taxable trust or taxable corporation that is maintained for the purpose of providing welfare benefits to an employer's employees is a "welfare benefit fund."

(c) Section 419 (e)(3)(C) also provides that the term "fund" includes, to the extent provided in regulations, any account held for an employer by any person. Pending the issuance of further guidance, only the following accounts, and arrangements that effectively constitute accounts, as described below, are "funds" within section 419(e)(3)(C). A retired lives reserve or a premium stabilization reserve maintained by an insurance company is a "fund," or part of a "fund," if it is maintained for a particular employer and the employer has the right to have any amount in the reserve applied against its future years' benefit costs or insurance premiums. Also, if an employer makes a payment to an insurance company under an "administrative services only" arrangement with respect to which the life insurance company maintains a separate account to provide benefits, then the arrangement would be considered to be a "fund." Finally, an insurance or premium arrangement between an employer and an insurance company is a "fund" if, under the arrangement, the employer has a right to a refund, credit, or additional benefits (including upon termination of the arrangement) based on the benefit or claims experience, administrative cost experience, or investment experience attributable to such employer for such year or years. However, an arrangement with an insurance company is not a "fund" under the previous sentence merely because the employer's premium for a renewal year reflects the employer's own experience for an earlier year if the arrangement is both cancellable by the insurance company and cancellable by the employer as of the end of any policy year and, upon cancellation by either of the parties, neither of the parties can receive a refund or additional amounts or benefits and neither of the parties can incur a residual liability beyond the end of the policy year (other than, in the case of the insurer, to provide benefits with respect to claims incurred before cancellation). The determination whether either of the parties can receive a refund or additional amounts or benefits or can incur a residual liability upon cancellation of an arrangement will be made by examining both the contractual rights and obligations of the parties under the arrangement and the actual practice of the insurance company (and other insurance companies) with respect to other employers upon cancellation of similar arrangements. Similarly, a disability income policy does not constitute a "fund" under the preceding provisions merely because, under the policy, an employer pays an annual premium so that employees who became disabled in such year may receive benefit payments for the duration of the disability.

Q-4: For purposes of determining the section 419 limit on the employer's deduction for contributions to the fund for a taxable year of the employer, which taxable year of the welfare benefit fund is related to the taxable year of the employer?

A-4: The amount of an employer's deduction for contributions to a welfare benefit fund for a taxable year of the employer is limited to the "qualified cost" of the welfare benefit fund for the taxable year of the fund that is related to such taxable year of the employer. The taxable year of the welfare benefit fund that ends with or within the taxable year of the employer is the taxable year of the fund that is related to the taxable year of the employer. Thus, for example, if an employer has a calendar taxable year and it makes contributions to a fund having a taxable year ending June 30, the "qualified cost" of the fund for the taxable year of the fund ending on June 30, 1986, applies to limit the employer's deduction for contributions to the fund in the employer's 1986 taxable year. In the case of employer contributions paid directly to an account or arrangement with an insurance company that is treated as a welfare benefit fund for the purposes of section 419, the policy year will be treated as the taxable year of the fund. See Q&A-7 of this regulation for special section 419 rules relating to the coordination of taxable years for the taxable year of the employer in which a welfare benefit fund is established and for the next following taxable year of the employer.

Q-5: What is the "qualified cost" of a welfare benefit fund for a taxable year under section 419?

A-5: (a) Under section 419(c), the

"qualified cost" of a welfare benefit fund for a taxable year of the fund is the sum of (1) the "qualified direct cost" of such fund for such taxable year of the fund, and (2) the amount that may be added to the qualified asset account for such taxable year of the fund to the extent that such addition does not result in a total amount in such account as of the end of such taxable year of the fund that exceeds the applicable account limit under section 419A(c). However, in calculating the qualified cost of a welfare benefit fund for a taxable year of the fund, this sum is reduced by the fund's "after-tax income" (as defined in section 419(c)(4)) for such taxable year of the fund. Also, the qualified cost of a welfare benefit fund is reduced further under the provisions of paragraph (b) of this Q&A.

(b)(1) Pursuant to section 419A(i), notwithstanding section 419 and §1.419-1T, contributions to a welfare benefit fund during any taxable year of the employer beginning after December 31, 1985, shall not be deductible for such taxable year to the extent that such contributions result in the total amount in the fund as of the end of the last taxable year of the fund ending with or within such taxable year of the employer exceeding the account limit applicable to such taxable year of the fund (as adjusted under section 419A(f)(7)). Solely for purposes of this subparagraph, (i) contributions paid to a welfare benefit fund during the taxable year of the employer but after the end of the last taxable year of the fund that relates to such taxable year of the employer, and (ii) contributions accrued with respect to a welfare benefit fund during the taxable year of the employer or during any prior taxable year of the employer (but not actually paid to such fund on or before the end of a taxable year of the employer) and deducted by the employer for such or any prior taxable year of the employer, shall be treated as an amount in the fund as of the end of the last taxable year of the fund that relates to the taxable year of the employer. Contributions that are not deductible under this subparagraph are in excess of the qualified cost of the welfare benefit fund for the taxable year of the fund that relates to the taxable year of the employer and thus are treated as contributed to the fund on the first day of the employer's next taxable year.

(2) Subparagraph (1) shall not apply to contributions with respect to a collectively bargained welfare benefit fund within the meaning of §1.419A-2T. In addition, subparagraph (1) shall not apply to any taxable year of an employer beginning after the end of the earlier of the following taxable years: (i) the first taxable year of the employer beginning after December 31, 1985, for which the employer's deduction limit under section 419 (after the application of subparagraph (1)) is at least equal to the qualified direct cost of the fund for the taxable year (or years) of the fund that relates to such first taxable year of the employer, or (ii) the first taxable year of the employer beginning after December 31, 1985, with or within which ends the first taxable year of the fund with respect to which the total amount in the fund as of the end of such taxable year of the fund does not exceed the account limit for such taxable year of the fund (as adjusted under section 419A(f)(7)).

(3) For example, assume an employer with a taxable year ending June 30 and a welfare benefit fund with a taxable year ending January 31. During its taxable year ending June 30, 1987, and on or before January 31, 1987, the employer contributes $250,000 to the fund, and during the remaining portion of its taxable year ending June 30, 1987, the employer contributes $200,000. The qualified direct cost of the fund for its taxable year ending January 31, 1987, is $500,000, the account limit applicable to such taxable year (after the adjustment under section 419A(f)(7)) is $750,000, and the total amount in the fund as of January 31, 1987, is $800,000. Before the application of this paragraph, the employer may deduct the entire $450,000 contribution for its taxable year ending June 30, 1987. However, under this paragraph, the excess of (i) the sum of the total amount in the fund as of January 31, 1987 ($800,000), and employer contributions to the fund after January 31, 1987, and on or before June 30, 1987 ($200,000), over (ii) the account limit applicable to the fund for its taxable year ending January 31, 1987 ($750,000), $250,000. Thus, under this paragraph, only $200,000 of the $450,000 contribution the employer made during its taxable year ending June 30, 1987, is deductible for such taxable year. If the excess were $450,000 or greater, no portion of the $450,000 contribution would be deductible by the employer for its taxable year ending June 30, 1987. Such nondeductible contributions are in excess of the fund's qualified cost for the taxable year related to the employer's taxable year and thus are deemed to be contributed on the first day of the employer's next taxable year.

(c) See Q&A-7 of this regulation for special rules relating to the calculation of the qualified cost of a welfare benefit fund for an Initial Fund Year and an Overlap Fund Year (as defined in Q&A-7). See Q&A-11 of this regulation for special rules relating to the application of section 419 to the contribution to a welfare benefit fund of a facility (and to the contribution of other amounts, such as cash, used to acquire, construct, or improve a facility) before section 419 generally becomes effective with respect to contributions to the fund. See §1.419A-2T for special rules relating to certain collectively bargained welfare benefit funds.

Q-6: What is the "qualified direct cost" of a welfare benefit fund under section 419(c)(3)?

A-6: (a) Under section 419(c)(3), the "qualified direct cost" of a welfare benefit fund for any taxable year of the fund is the aggregate amount which would have been allowable as a deduction to the employer for benefits provided by such fund during such year (including insurance coverage for such year) if (1) such benefits were provided directly by the employer and (2) the employer used the cash receipts and disbursements method of accounting and had the same taxable year as the fund. In this regard, a benefit is treated as provided when such benefit would be includible in the gross income of the employee if provided directly by the employer (or would be so includible but for a provision of chapter 1, subtitle A, of the Internal Revenue Code excluding it from gross income). Thus, for example, if a calendar year welfare benefit fund pays an insurance company in July 1986 the full premium for coverage of its current employees under a term health insurance policy for the twelve month period ending June 30, 1987, the insurance coverage will be treated as provided by the fund over such twelve month period. Accordingly, only the portion of the premium for coverage during 1986 will be treated as a "qualified direct cost" of the fund for 1986; the remaining portion of the premium will be treated as a "qualified direct cost" of the fund for 1987. The "qualified direct cost" for a taxable year of the fund includes the administrative expenses incurred by the welfare benefit fund in delivering the benefits for such year.

(b) If, in a taxable year of a welfare benefit fund, the fund holds an asset with useful life extending substantially beyond the end of the taxable year (e.g., buildings, vehicles, tangible assets, and licenses) and, for such taxable year of the fund, the asset is used in the provision of welfare benefits to employees, the "qualified direct cost" of the fund for such taxable year of the fund includes the amount that would have been allowable to the employer as a deduction under the applicable Code provisions (e.g., sections 168 and 179) with respect to the portion of the asset used in the provision of welfare benefits for such year if the employer had acquired and placed in service the asset at the same time the fund received and placed in service the asset, and the employer had the same taxable year as the fund. This rule applies regardless of whether the fund received the asset through a contribution of the asset by the employer or through an acquisition or the construction by the fund of the asset. For example, assume that in 1986 a calendar year employer contributes recovery property under section 168(c) to a welfare benefit fund with a calendar taxable year to be used in the provision of welfare benefits. The employer will be treated as having sold the property in such year and thus will recognize gain to the extent that the fair market value of the property exceeds the employer's adjusted basis in the property. In this regard, see section 1239(d). Also, the employer will be treated as having made a contribution to the fund in such year equal to the fair market value of the property. Finally, the qualified direct cost of the welfare benefit fund for 1986 will include the amount that the employer could have deducted in 1986 with respect to the portion of the property used in the provision of welfare benefits if the employer had acquired the property in 1986 and had placed the property in service when the fund actually placed the property in service. Similarly, for example, assume that in 1986 a welfare benefit fund purchases and places in service a facility to be used in the provision of welfare benefits. The qualified direct cost of the fund for 1986 will include the amount that the employer could have deducted with respect to such facility if the employer had purchased and placed in service the facility at the same time that the fund purchased and placed in service the facility.

(c) The qualified direct cost of a welfare benefit fund does not include expenditures by the fund that would not have been deductible if they had been made directly by the employer. For example, a fund's purchase of land in a year for an employee recreational facility will not be treated as a qualified direct cost because, if made directly by the employer, the purchase would not have been deductible under section 263. See also sections 264 and 274.

(d) Notwithstanding the preceding paragraphs, the qualified direct cost of a welfare benefit fund with respect to that portion of a child care facility used in the provision of welfare benefits for a year will include the amount that would have been allowable to the employer as a deduction for the year under a straight-line depreciation schedule for a period of 60 months beginning with the month in which the facility is placed in service under rules similar to those provided for section 188 property under §1.188-1(a). For purposes of this section, a "child care facility" is tangible property of a character subject to depreciation that is located in the United States and specifically used as an integral part of a "qualified child care center facility" within the meaning of §1.188-1(d)(4).

(e) See Q&A-7 of this regulation for special section 419 rules relating to the calculation of the qualified direct cost of a welfare benefit fund for an Initial Fund Year and an Overlap Fund Year (as defined in Q&A-7). See Q&A-11 of this regulation for special rules relating to the contribution to a welfare benefit fund of a facility (and to the contribution of other amounts, such as cash, used to acquire, construct, or improve a facility) before section 419 generally becomes effective with respect to contributions to the fund.

Q-7: What special rules apply for purposes of determining the section 419 limit on the employer's deduction for contributions to a welfare benefit fund for the taxable year of the employer in which the fund is established and for the next following taxable year of the employer?

A-7: (a) If the taxable year of a welfare benefit fund is the same as the taxable year of the employer, there are no special rules that apply for purposes of determining the section 419 limit on an employer's deduction for contributions to the fund for either the taxable year of the employer in which the fund is established or the next following taxable year of the employer. However, if the taxable year of a welfare benefit fund is different from the taxable year of the employer, the general section 419 rules are modified by the special rules set forth below for purposes of determining the section 419 deduction limit for the taxable year of the employer in which a fund is established and for the next following taxable year of the employer.

(b) If a welfare benefit fund is established after December 31, 1985, during a taxable year of an employer and either (i) the first taxable year of the fund ends after the close of such taxable year of the employer, or (ii) the first taxable year of the fund is six months or less and ends before the close of such taxable year of the employer and the second taxable year of the fund begins before and ends after the close of such taxable year of the employer, the taxable year of the fund that contains the closing day of such taxable year of the employer will be treated as an "Overlap Fund Year." For purposes of determining the limit on the employer's deduction for contributions to a welfare benefit fund for the taxable year of the employer in which the fund was established, the period between the beginning of the fund's Overlap Fund Year and the end of the employer's taxable year in which the Overlap Fund Year began will be treated as a taxable year of the fund ("Initial Fund Year").

(c) The qualified cost of a welfare benefit fund for its Initial Fund Year will be equal to the qualified direct cost of the fund for such Initial Fund Year. The qualified cost of a fund for its Overlap Fund Year will be determined under the general rules of Q&A-5 of this regulation and section 419(c), with the exception that such qualified cost will be reduced by the employer contributions made during the Initial Fund Year and deductible by the employer for the taxable year of the employer in which the Overlap Fund Year of the fund begins.

(d) Assume that an employer with a calendar taxable year establishes on July 1, 1986, a welfare benefit fund with a taxable year ending on June 30. The fund's first taxable year from July 1, 1986, to June 30, 1987, is an Overlap Fund Year. The employer contributes $1,000 to the fund during its taxable year ending December 31, 1986 (i.e., during the period between July 1, 1986, and December 31, 1986, which is also the Initial Fund Year) and another $1500 to the fund during its taxable year ending December 31, 1987. Assume further that the qualified direct cost of the fund for the Initial Fund Year is $900 and that the qualified cost for the Overlap Fund year is $2500 (prior to the reduction required by paragraph (c) of this Q&A). Under the special rules of paragraphs (b) and (c), the employer may deduct $900 for its taxable year ending on December 31, 1986, and $1600 for its taxable year ending on December 31, 1987. If the qualified direct cost of the fund for the Initial Fund year had been $1050 and the qualified cost for the Overlap Fund year had been $2500 (prior to the reduction required by paragraph (c) of this Q&A), the employer's deduction for its taxable year ending December 31, 1986, would have been $1000 and its deduction for its taxable year ending December 31, 1987, would have been $1500.

(e) Assume that an employer with a calendar taxable year establishes on March 1, 1986, a welfare benefit fund with a taxable year ending June 30. Thus, the fund has a short first taxable year ending June 3, 1986, an Overlap Fund Year from July 1, 1986, until June 30, 1987, and an ongoing June 30 taxable year. The employer contributes $1750 to the fund during the employer's taxable year ending December 31, 1986—$750 during the short first taxable year of the fund and $1000 during the Initial Fund Year (i.e., the period between July 1, 1986, and December 31, 1986)—and $1500 to the fund during its taxable year ending December 31, 1987. Assume that the qualified cost of the fund for the short first taxable year of the fund is $800, the qualified direct cost for the Initial Fund Year is $900, and the qualified cost for the Overlap Fund Year is $2500 (prior to the reduction required by paragraph (c) of this Q&A). Under the special rules of paragraphs (b) and (c), the employer may deduct $1700 for its taxable year ending December 31, 1986, and $1550 for its taxable year ending December 31, 1987.

Q-8: How does section 419 treat an employer's contribution with respect to a welfare benefit fund in excess of the applicable deduction limit for a taxable year of the employer?

A-8: (a) If an employer makes contributions to a welfare benefit fund in a taxable year of the employer and such contributions (when combined with prior contributions that are deemed under the rule of this Q&A and section 419(d) to have been made in such taxable year) exceed the section 419 deduction limit for such taxable year of the employer, the excess amounts are deemed to be contributed to the fund on the first day of the next taxable year of the employer. Such deemed contributions are combined with amounts actually contributed by the employer to the fund during the next taxable year and may be deductible for such year, subject to the otherwise applicable section 419 deduction limit for such year.

(b) Contributions to a welfare benefit fund on or before December 31, 1985, that were not deductible by the employer for any taxable year of the employer ending on or before December 31, 1985, or for the first taxable year of the employer ending after December 31, 1985, as pre-1986 contributions (see Q&A-9 of this regulation) are deemed to be contributed to the fund on January 1, 1986. However, see Q&A-11 of this regulation for special rules relating to the contribution to a welfare benefit fund of amounts (such as cash) used to acquire, construct, or improve a facility before section 419 generally becomes effective with respect to contributions to the fund. Generally, such contributions (to the extent that they were made after June 22, 1984 and on or before December 31, 1985) are treated as nondeductible pre-1986 contributions and are deemed to be contributed in the form of a facility at the same time as when the facility is placed in service by the fund.

Q-9: How does an employer with a fiscal taxable year calculate its deduction limit for contributions with respect to a welfare benefit fund for the first taxable year of the employer ending after December 31, 1985?

A-9: (a) If the first taxable year of an employer ending after December 31, 1985 (or, if applicable under paragraph (b) of Q&A-2 of this section, the first taxable year of an employer beginning after termination of the last of the collective bargaining agreements pursuant to which the fund is maintained) is a fiscal year, the employer's deduction for such taxable year for contributions to a welfare benefit fund that is not a collectively bargained welfare benefit fund under §1.419A-2T is limited to the greater of the following two amounts: (i) the contributions paid to the fund during such first taxable year up to the qualified cost of the welfare benefit fund for the taxable year of the fund that relates to such taxable year of the employer, and (ii) the contributions paid to the fund during the 1985 portion of such first taxable year of the employer ("the pre-1986 contributions") to the extent that such pre-1986 contributions are deductible under the rules governing the deduction of such contributions before section 419 generally becomes effective (including the rules set forth in Q&A-10 of this regulation, modifed for purposes of this Q&A-9 by substituting "December 31, 1986" for "December 31, 1985" in paragraph (c)). See Q&A-11 of this regulation for special rules relating to the contribution to a welfare benefit fund of a facility (and to the contribution of other amounts, such as cash, used to acquire, construct, or improve such a facility) before section 419 generally becomes effective with respect to contributions to such fund.

(b) For example, assume that an employer with a taxable year ending June 30, contributes to a welfare benefit fund with a taxable year ending January 31. This employer contributes $1000 to the fund between July 1, 1985, and December 31, 1985, and an additional $500 to the fund between January 1, 1986, and June 30, 1986. Assume further that the qualified direct cost of the fund for the taxable year of the fund ending January 31, 1986, is $500 and that the qualified cost for such taxable year is $800. Under the deduction rule set forth above, the employer's deduction for its taxable year ending June 30, 1986, is the greater of two amounts: (i) the contributions made during such full taxable year ($1500) up to the qualified cost of the fund with respect to such taxable year ($800), and (ii) the pre-1986 contributions ($1000) to the extent that such pre-1986 contributions are deductible under the pre-section 419 rules. In determining the extent to which the pre-1986 contributions are deductible under the pre-section 419 rules, the rules contained in Q&A-10 apply as though December 31, 1985, in paragraph (c) were December 31, 1986. Assuming that only $875 is deductible under the pre-section 419 rules, because $875 is greater than $800, this employer may deduct $875 for its first taxable year ending after December 31, 1985. This full $875 deduction for 1985 is deemed to consist entirely of pre-1986 contributions.

Q-10: How do the rules of sections 263, 446(b), 461(a), and 461(h) apply in determining whether contributions with respect to a welfare benefit fund are deductible for a taxable year?

A-10: (a) Both before and after the effective date of section 419 (see Q&A-2 of this regulation), an employer is allowed a deduction for a taxable year for contributions paid or accrued with respect to a "welfare benefit fund" (as defined in Q&A-3 of this regulation and section 419(e)) only to the extent that such contributions satisfy the requirements of section 162 or 212. These requirements must be satisfied after the effective date of section 419 because section 419 requires that (among other requirements) contributions to a welfare benefit fund satisfy the requirements of section 162 or 212.

(b) Except as provided in paragraphs (c) and (d), in determining the extent to which contributions paid or accrued with respect to a welfare benefit fund satisfy the requirements of section 162 or 212 for a taxable year (both before and after section 419 generally becomes effective with respect to such contributions), the rules of sections 263, 446(b), 461(a) (including the rules that relate to the creation of an asset with a useful life extending substantially beyond the close of the taxable year), and 461(h) (to the extent that such section is effective with respect to such contributions) are generally applicable.

(c) Notwithstanding paragraph (b), under the authority of section 7805(b), the rules of sections 263, 446(b), and 461(a) shall not be applied in determining the extent to which an employer's contribution with respect to a welfare benefit fund is deductible under section 162 or 212 with respect to any taxable year of the employer ending on or before December 31, 1985, to the extent that, for such taxable year, (1) the contribution was made pursuant to a bona fide collective bargaining agreement requiring fixed and determinable contributions to a collectively bargained welfare benefit fund (as defined in §1.419A-2T), or (2) the contribution was not in excess of the amount deductible under the principles of Revenue Rulings 69-382, 1969-2 C.B. 28; 69-478, 1969-2 C.B. 29; and 73-599, 1973-2 C.B. 40, modified as appropriate for benefits for active employees.

(d) Nowithstanding paragraph (b), in determining the extent to which contributions paid or accrued with respect to a welfare benefit fund are deductible under section 419, the rules of sections 263, 446(b), and 461(a) will be treated as having been satisfied to the extent that such contributions satisfy the otherwise applicable rules of section 419. Thus, for example, contributions to a welfare benefit fund will not fail to be deductible under section 419 merely because they create an asset with a useful life extending substantially beyond the close of the taxable year if such contributions satisfy the otherwise applicable requirements of section 419.

(e) In determining the extent to which contributions with respect to a welfare benefit fund satisfy the requirements of section 461(h) for any taxable year for which section 461(h) is effective, pursuant to the authority under section 461(h)(2), economic performance occurs as contributions to the welfare benefit fund are made. Solely for purposes of section 461(h), in the case of an employer's taxable year ending on or after July 18, 1984, and on or before March 21, 1986, contributions made to the welfare benefit fund after the end of such taxable year and on or before March 21, 1986 shall be deemed to have been made on the last day of such taxable year.

Q-11: What special section 419 rules apply to the payment or accrual with respect to a welfare benefit fund of a facility (and the payment or accrual of other amounts, such as cash, used to acquire, construct, or improve such a facility)?

A-11: (a)(1) In the case of an employer's payment or accrual with respect to a welfare benefit fund after June 22, 1984, and on or before December 31, 1985, (or, if applicable under paragraph (b) of Q&A-2 of this regulation, before section 419 generally becomes effective with respect to contributions to such fund) of a facility, the rules of section 419, §1.419-1T, and §1.419A-2T generally apply to determine the extent to which such contribution is deductible by the employer for its taxable year of contribution. For this purpose, however, the facility is to be treated as the only contribution made to the fund and the qualified cost of the fund for the taxable year of the fund in which the facility was contributed is to be equal to the qualified direct cost directly attributable to the facility (as determined under Q&A-6 of this regulation). Also, for this purpose, the welfare benefit fund to which the facility was contributed may not be aggregated with any other fund. For purposes of this Q&A, "facility" means any tangible asset with a useful life extending substantially beyond the end of the taxable year (e.g., vehicles, buildings) and any intangible asset (e.g., licenses) related to a tangible asset, whether or not such asset is used in the provision of welfare benefits. See, however, paragraph (c) of Q&A-2 of this regulation for a binding contract exception.

(2) For example, assume that an employer and a welfare benefit fund each has a calendar taxable year and that, during 1985, the employer contributes to the fund $200,000 in cash and a facility with a fair market value of $100,000. Such facility is used in the provision of welfare benefits under the fund. The employer is treated as having sold the facility in such year and thus will recognize gain to the extent that the fair market value of the facility exceeds the employer's adjusted basis in the facility. In this regard, see section 1239(d). The extent to which the facility contribution is deductible by the employer for its 1985 taxable year is

determined as though it were the only contribution made by the employer to the fund during such year and the qualified cost of the fund for the taxable year of the fund in which the contribution was made (i.e., the 1985 taxable year) were equal to the amount that would have been allowable to the employer as a deduction for such year under the applicable Code provisions with respect to the portion of the facility used in the provision of welfare benefits for such year if the employer had placed in service the facility at the time the fund placed in service the facility and if the employer had the same taxable year as the fund. If, under these assumptions, the employer would have been allowed a $10,000 deduction with respect to the facility for the 1985 taxable year, the fund's qualified cost for its 1985 taxable year would be only $10,000. Thus, only $10,000 of the $100,000 facility contribution would be deductible by the employer for its 1985 taxable year (i.e., the taxable year of the employer with or within which the applicable taxable year of the fund ends). However, in determining the extent to which the $200,000 in cash is deductible by the employer for its 1985 taxable year, the $100,000 facility is not to be disregarded. Thus, if under the applicable pre-section 419 rules the employer is allowed for 1985 a total deduction of only $175,000, the employer would be permitted a deduction for 1985 of $175,000 ($10,000 with respect to the facility and $165,000 of the cash contribution). The nondeductible portion of the cash contribution is to be treated as contributed to the fund on the first day of the next taxable year of the employer. If under the applicable pre-section 419 rules the employer were allowed a total deduction of $300,000 for 1985, the employer would be permitted a deduction for 1985 of only $210,000 ($10,000 with respect to the facility and the full $200,000 cash contribution).

(3) For example, assume that an employer has a June 30 taxable year and maintains a welfare benefit fund with a taxable year ending January 31. During the 1985 portion of its taxable year ending June 30, 1986, the employer contributes $50,000 in cash and a facility with a fair market value of $100,000; and during the 1986 portion of such taxable year, the employer contributes another $75,000 in cash to the fund. The facility is used in the provision of welfare benefits under the fund. Under the rules of Q&A-9 of this regulation, the employer's deduction for its June 30, 1986, taxable year is limited to the greater of the following two amounts: (i) the contributions paid to the fund during such taxable year ($225,000) up to the qualified cost of the fund for the taxable year of the fund ending January 31, 1986, and (ii) the contributions paid to the fund during the 1985 portion of the employer's taxable year ending June 30, 1986 ("the pre-1986 contributions") ($150,000) to the extent that such pre-1986 contributions are deductible under the rules governing the deduction of such contributions before section 419 is generally effective with respect to the fund. For purposes of this rule, the contribution of the facility on or before December 31, 1985, is to be treated as a pre-1986 contribution and the rules of section 419 and this Q&A are to be treated as rules governing the deduction of such contribution before section 419 generally becomes effective with respect to the fund. Thus, in determining the extent to which the facility is deductible as a pre-1986 contribution under the rules before section 419 generally becomes effective, the facility is treated as the only contribution to the welfare benefit fund and the qualified cost of such fund for the taxable year of the fund in which the facility was contributed is the amount that would have been allowable to the employer as a deduction with respect to the portion of the facility used in the provision of welfare benefits if the employer had placed in service the facility at the same time that the fund placed in service the facility and the employer's taxable year ended on January 31, 1986.

(b)(1) The preceding rules shall also apply for purposes of determining when and the extent to which an employer may deduct contributions or other items and amounts after June 22, 1984 and on or before December 31, 1985 (or, if applicable under paragraph (b) of Q&A-2 of this regulation, before section 419 generally becomes effective with respect to contributions to the fund) that are not facilities (e.g., cash contributions) to a welfare benefit fund that are used by the fund to acquire, construct, or improve a facility. The most recent non-facility contributions made to a welfare benefit fund before the facility in question is placed in service by the fund (up to the fair market value of the facility at such time) are to be treated as used by the fund for the acquisition, construction, or improvement (as the case may be) of such facility. To the extent that contributions before such a facility is placed in service are not at least equal to the value of the facility at such time, contributions after such date (up to the value of the facility at the time it is placed in service) are treated as used for acquisition, construction, or improvement of the facility. Such non-facility contributions, to the extent that they were made after June 22, 1984, and on or before December 31, 1985 (or, if applicable under paragraph (b) of Q&A-2 of this regulation, before section 419 generally becomes effective with respect to contributions to the fund), are not deductible by the employer as non-facility contributions for any year. Instead, the employer is permitted a deduction with respect to such contributions only under the rules of this Q&A as though the employer had contributed a facility to the fund at the same time that the fund placed in service the facility in question and, at such time, the facility had a fair market value equal to the total of such non-facility contributions.

(2) For example, assume that an employer and a welfare benefit fund each has a calendar taxable year and during 1985 the fund acquired and placed in service a facility with a fair market value of $100,000 to be used in the provision of welfare benefits. Further, during July 1984 the employer contributed $150,000 in cash to the fund and, during the portion of 1985, before the facility was placed in service by the fund, the employer contributed another $75,000 in cash to the fund; during the remaining portion of 1985, the employer contributed $125,000 in cash. The facility is used in the provision of welfare benefits under the fund. Because $25,000 of the employer's 1984 contribution is treated under this rule as used for the acquisition of a facility, such $25,000 is not deductible by the employer for 1984. For purposes of determining the employer's deduction for 1985, the employer will be treated as having contributed $125,000 in cash and a facility with a fair market value

of $100,000. The employer's deduction for its 1985 taxable year will be determined under the rules relating to the contribution of a facility after June 22, 1984, and on or before December 31, 1985.

(3) For example, assume that an employer and a welfare benefit fund each has a calendar taxable year and during 1986 the fund placed in service a facility with a fair market value of $100,000 to be used in the provision of welfare benefits. During 1985, the employer contributed $125,000 in cash to the fund. During the portion of 1986 before the facility was placed in service, the employer contributed $60,000 in cash, and during the remaining portion of 1986, the employer contributed another $75,000 in cash. The facility is used in the provision of welfare benefits under the fund. Because $40,000 of its 1986 cash contribution is treated under this rule as used for the acquisition of the facility, such $40,000 is not deductible by the employer for 1985. For purposes of determining the employer's deduction for 1986, the employer will be treated as though it had contributed a $40,000 facility to the fund at the time the fund placed the facility in service.

(c) For purposes of calculating the "existing excess reserve amount" under Q&A-1 of §1.419A-1T and the "existing reserves for post-retirement medical or life insurance benefits" under A&A-4 of §1.512(a)-5T (but not the exempt function income under Q&A-3 of §1.512(a)-5T), the amount set aside as of any applicable date is to be reduced to the extent that contributions originally included in such amount are subsequently treated under this Q&A as used for the acquisition, construction, or improvement of an asset excluded from the calculation of the total amount set aside under paragraph (b) of §1.512(a)-5(T) (or would be so treated under this Q&A if it applied to such asset). The reduction required under this paragraph applies for purposes of calculating the "existing excess reserve amount" and the "existing reserves for post-retirement medical or life insurance benefits" for all taxable years of the welfare benefit fund.

Par. 14 A new §1.419A-1T is added immediately following §1.419-1T to read as follows:

§1.419A-1T Qualified asset account limitation of additions to account. (Temporary)

Q-1: What does the transition rule under section 419A(f)(7) provide?

A-1: Section 419A(f)(7) provides that, in the case of a welfare benefit fund that was in existence on July 18, 1984, the account limit (as determined under section 419A(c)) for each of the first four taxable years of the fund that relate to taxable years of the employer ending after December 31, 1985 (or, if applicable under paragraph (b) of Q&A-2 of this regulation, taxable years of the employer beginning after the termination of the last of the collective bargaining agreements pursuant to which the plan is maintained) shall be increased by the following percentages of the "existing excess reserve amount":

First taxable year	80 percent
Second taxable year	60 percent
Third taxable year	40 percent
Fourth taxable year	20 percent

For purposes of this section, the "existing excess reserve amount" for any taxable year of a fund is the excess of (1) the assets actually set aside for purposes described in section 419A(a) at the close of the first taxable year of the fund ending after July 18, 1984 (calculated in the manner set forth in Q&A-3 of §1.512(a)-3T, and adjusted under paragraph (c) of Q&A-11 of §1.419-1T), reduced by employer contributions to the fund before the close of such first taxable year to the extent that such contributions are not deductible for the taxable year of the employer with or within which such taxable year of the fund ends and for any prior taxable year of the employer, over (2) the account limit which would have applied to the taxable year of the fund for which the excess is being computed (without regard to this transition rule). A welfare benefit fund is treated as in existence on July 18, 1984, for purposes of this transition rule only if amounts were actually set aside in such fund on such date to provide welfare benefits enumerated under section 419A.

Par. 15. The following new section is added immediately after §1.461-3T to read as follows:

§1.461(h)-4T Questions and answers relating to the economic performance requirement for certain employee benefits. (Temporary)

Q-1: What is the relationship between the economic performance requirement of section 461(h) and sections 404 and 419?

A-1: Section 404 provides that contributions paid and compensation paid or incurred with respect to a plan, or method or arrangement, deferring the receipt of compensation or providing for deferred benefits will be deductible only to the extent that they satisfy the requirements of seciton 162 or 212 Section 419 provides that contributions paid or accrued with respect to a "welfare benefit fund" (as defined in section 419(e) and Q&A-3 of §1.419-1T) will be deductible only to the extent that they satisfy the requirements of section 162 and 212. In the case of the accrual method taxpayer, a contribution or compensation satisfies the requirements of section 162 or 212 only to the extent that the all events test (as defined in section 416(b)(4)) and the economic performance requirement of section 461(h)(1) are satisfied. In the case of a contribution or compensation subject to section 404 or 419, pursuant to the authority under section 461(h)(2), economic performance occurs (i) in the case of a plan subject to section 404, either as the contribution is made under the plan or, if section 404(a)(5) is applicable, as an amount attributable to such contribution is includible in the gross income of an employee (or, if section 404(d) applies, a nonemployee); or (ii) in the case of a welfare benefit fund, as a contribution is made to the welfare benefit fund. Solely for purposes of section 461(h), in the case of an employer's taxable year ending on or after July 18, 1984, and on or before March 21, 1986 contributions made to a welfare benefit fund after the end of such taxable year and on or before March 21, 1986 shall be deemed to have been made on the last day of such taxable year.

Par. 16. The following new section is added immediately after §1.461(h)-4T:

§1.463-1T Transitional rule for vested accrued vacation pay. (Temporary)

(a) *Introduction*. Section 91(i) of the Tax Reform Act of 1984 provides a transitional rule for the election under section 463, relating to accrual of vacation pay. Section 91(i) applies only in the case of taxpayers with respect to which a deduction was allowable (other than under section 463) for vested accrued vacation pay for the last taxable year ending on or before July 18, 1984.

(b) *Election under transitional rule.* A taxpayer described in paragraph (a) of this section that makes an election under section 463 for the first taxable year ending after July 18, 1984, shall compute the opening balance of the account described in section 463(a)(1) ("accrual account") with respect to such vacation pay under the rules provided in paragraph (e)(3) of this section.

(c) *Multiple vacation pay accounts within a single trade or business.* (1) An election under section 463 must be made with respect to all vacation pay accounts maintained by the taxpayer within a single trade or business whether the liability is for vested accrued vacation pay or for vacation pay that is contingent.

(2) If a taxpayer has elected, in a taxable year ending on or before July 18, 1984, to treat contingent vacation pay with respect to a single trade or business under section 463, the taxpayer may elect, under the provisions of section 91(i) of the Tax Reform Act of 1984, to treat vested accrued vacation pay with respect to the same trade or business under section 463. However, no election may be made with respect to vacation pay for which a prior section 463 election was made and that is accounted for under section 463.

(d) *Time for making election.* A taxpayer described in paragraph (a) of this section that makes an election under section 463 for the first taxable year ending after July 18, 1984, must make the election on or before the due date (determined with regard to extensions) for filing the taxpayer's income tax return for such taxable year. However, if the taxpayer's income tax return was filed for the first taxable year ending after July 18, 1984, prior to March 6, 1986, the taxpayer must make the election by the later of the due date (determined with regard to extensions) for filing the taxpayer's income tax return, or May 5, 1986. In this case, the election must be made by filing an amended return (showing adjustments, if any) for such year and attaching the statement required by paragraph (e) of this section on or before the later of the due date (determined with regard to extensions) for filing the taxpayer's income tax return, or May 5, 1986.

(e) *Manner of making election.* A taxpayer must make the election described in paragraph (b) of this section by attaching a statement to the taxpayer's income tax return for the first taxable year ending after July 18, 1984. the statement must indicate that the taxpayer is elected to apply the provisions of section 463 with respect to vested accrued vacation pay for the taxpayer's first taxable year ending after July 18, 1984. The statement must contain the following information:

(1) The taxpayer's name and a description of the vacation pay plans to which the election applies.

(2) If a taxpayer has more than one trade or business and is not making the election with respect to all trades or businesses, a description of the trades or businesses to which the election applies.

(3) The opening balance in the taxpayer's accrual account. This balance equals the amount determined as if the taxpayer had maintained an account for the last taxable year ending on or before July 18, 1984, representing the taxpayer's liability for vested accrued vacation pay earned by employees before the close of the last taxable year ending on or before July 18, 1984, and payable during that taxable year or within 12 months following the close of that taxable year. If the taxpayer's liability for vacation pay includes both vested accrued vacation pay and vacation pay the liability for which is contingent, the amount in the opening balance of the accrual account that represents the taxpayer's liability for contingent vacation pay is to be determined under the rules provided in section 10.2(c)(ii)(B) of this chapter.

(4) The opening balance in the taxpayer's suspense account. This balance equals the amount determined under paragraph (e)(3) of this section less the portion allowed as deductions under section 162 for prior taxable years for vacation pay earned but not paid at the close of the last taxable year ending on or before July 18, 1984.

(f) *Vested accrued vacation pay.* For purposes of paragraphs (a) through (e) of this section, "vested accrued vacation pay" means any amount allowable as deductions under section 162(a) for a taxable year with respect to vacation pay of employees of the taxpayer (determined without regard to section 463). For purposes of this section, vacation pay will be considered vested accrued vacation pay even though there is a limit or ceiling on the amount of vacation pay an employee is entitled to as of the close of any plan year. For example, if under a vacation pay plan an employee may accumulate no more than 40 days of vacation leave by the end of any plan year and any unused days in excess of 40 days are forfeited, the taxpayer is considered to have vested accrued vacation pay (even though the plan is not fully vested) and may make an election under the transitional rule.

Par. 17. A new §1.505(c)-1T is added immediately after §1.503(f)-1 to read as set forth below.

§1.505(c)-1T. Questions and Answers Relating to the Notification Requirement for Recognition of Exemption Under Paragraphs (9), (17) and (20) of Section 501(c). (Temporary)

Q-1: What does section 505(c) of the Internal Revenue Code provide?

A-1: Section 505(c) provides that an organization will not be recognized as exempt under section 501(c)(9) as a voluntary employees' beneficiary association, under section 501(c)(17) as a trust forming part of a plan providing for the payment of supplemental unemployment compensation benefits, or under section 501(c)(20) as a trust forming part of a qualified group legal services plan unless notification is given to the Internal Revenue Service. The notification required of a trust created pursuant to section 501(c)(20) and forming part of a qualified group legal services plan is set forth in Q&A-2. The notification required of an organization organized after July 18, 1984, and applying for exempt status as an organization described in section 501(c)(9) or (17) is set forth in Q&A-3 through Q&A-8. The notification required of an organization organized on or before July 18, 1984, and claiming exemption as an organization described in section 501(c)(9) or (17) is set forth in Q&A-9 through Q&A-11. However, an organization that has previously notified the Internal Revenue Service of its claim of exemption under section 501(c)(9), (17) or (20) or its claim to exemption under those sections pursuant to another provision of the Code, is not required, under section 505(c), to submit a renotification (See Q&A-2 and Q&A-12).

SECTION 501(c)(20) TRUSTS

Q-2: What is the notice required of a trust created pursuant to section 501(c)(20) and forming part of a qualified group legal services plan under section 120?

A-2: (a) A trust claiming exemption as an organization described in section 501(c)(20) will be recognized as exempt if the exclusive function of the trust is to form part of a qualified group legal services plan or plans. Exemption of the trust under section 501(c)(20) will generally be dependent upon and coextensive with recognition of the plan as a qualified group legal services plan. Therefore, a trust organized pursuant to seciton 501(c)(20) after July 18, 1984, need not file a separate notice with the Internal Revenue Service of its claim to exemption because the notice required by section 120(c)(4) will suffice for purposes of section 505(c), provided a copy of the trust instrument is filed with the Form 1024 submitted by the group legal services plan. If the trust instrument has not been filed with the Form 1024 submitted by the group legal services plan, the trust must comply with (and exemption will be dependent upon) the filing applicable to a trust organized on or before July 18, 1984. For the notice required and effective dates of exemption of a qualified group legal services plan under section 120, see §1.120-3.

(b) A trust organized on or before July 18, 1984, that claims exempt status as a trust described in section 501(c)(20) and that forms part of a qualified group legal services plan which has been recognized as exempt under section 120, must file a copy of its trust instrument with the Internal Revenue Service before February 4, 1987. If a copy of the trust instrument is filed within the time provided, the trust's exemption will be recognized retroactively to the date the qualified group legal services plan was recognized as exempt under section 120. However, if a copy of the trust instrument is filed after the time provided, exemption will be recognized only for the period after the copy of the trust instrument is filed with the Internal Revenue Service. See Q&A 7 for a further discussion of "date of filing." A trust that has previously filed a copy of its trust instrument with the Service need not refile that document.

SECTION 501(c)(9) and (17) ORGANIZATIONS ORGANIZED AFTER JULY 18, 1984

Q-3: What is the notice required of an organization or trust, organized after July 18, 1984, that is applying for recognition of tax exempt status under section 501(c)(9) or (17)?

A-3: An organization or trust that is organized after July 18, 1984, will not be treated as described in paragraphs (9) or (17) of section 501(c), unless the organization notifies the Internal Revenue Service that it is applying for recognition of exemption. In addition, unless the required notice is given in the manner and within the time prescribed by these regulations, an organization will not be treated as exempt for any period before the giving of the required notice. The notice is filed by submitting a properly completed and executed Form 1024, "Application for Recognition of Exemption Under Section 501(a) or for Determination Under Section 120" together with the additional information required under Q&A-4 and Q&A-5. The notice is filed with the district director for the key district in which the organization's principal place of business or principal office is located. The notice may be filed by either the plan administrator (as defined in section 414(g)) or the trustee. The Internal Revenue Service will not accept a Form 1024 for any organization or trust before such entity has been organized.

Q-4: What information, in addition to the information required by Form 1024, must be submitted by an organization or trust seeking recognition of exemption under section 501(c)(9) or (17)?

A-4: A notice will not be considered complete unless, in addition to a properly completed and executed Form 1024, the organization or trust submits a full description of the benefits available to participants under section 501(c)(9) or (17). Moreover, both the terms and conditions of eligibility for membership and the terms and conditions of eligibility for benefits must be set forth. This information may be contained in a separate document, such as a "plan document," or it may be contained in the creating document of the entity (e.g., the articles of incorporation or association, or a trust indenture). For benefits provided through a policy or policies of insurance, all such policies must be included with the notice. Where individual policies of insurance are provided to the participants, single exemplar copies, typical of policies generally issued to participants, are acceptable, provided they adequately describe all forms of insurance available to participants. In providing a full description of the benefits available, the benefits provided must be sufficiently described so that each benefit is definitely determinable. A benefit is definitely determinable if the amount of the benefit, its duration, and the persons eligible to receive it are ascertainable from the plan document or other instrument. Thus, a benefit is not definitely determinable if the rules governing either its amount, its duration, or its recipients are not ascertainable from the plan document or other instrument but are instead subject to the discretion of a person or committee. Likewise, a benefit is not definitely determinable if the amount for any individual is based upon a percentage share of any item that is within the discretion of the employer. However, a disability benefit will not fail to be considered definitely determinable merely because the determination of whether an individual is disabled is made under established guidelines by an authorized person or committee.

Q-5: What is the notice required of collectively bargained plans?

A-5: If an organization or trust claiming exemption under section 501(c)(9) or (17) is organized and maintained pursuant to a collective bargaining agreement between employee representatives and one or more employer, only one Form 1024 is required to be filed for the organization or trust, regardless of the number of employers originally participating in the agreement. Moreover, once a Form 1024 is filed pursuant to a collective bargaining agreement, an additional Form 1024 is not required to be filed by an employer who thereafter participates in that agreement. When benefits are provided pursuant to a collective bargaining agreement, the notice will not be considered complete unless, in addition to a properly completed and executed Form 1024, a copy of the collective bargaining agreement is also submitted together with the additional information delineated in Q&A-4.

Q-6: When must the required notice be filed by an organization or trust, organized after July 18, 1984, that seeks recognition of exemption under section 501(c)(9) or (17)?

A-6: An organization or trust applying for exemption must file the required notice by the later of February 4, 1987 or 15 months from the end of the month in which the organization or trust was organized. An extension of time for filing the required notice may be granted by the district director if the request is submitted before the end of the applicable period and it is demonstrated that additional time is needed.

Q-7: What is the effective date of exemption for a new organization or trust, organized after July 18, 1984, that has submitted the required notice?

A-7: If the required notice is filed within the time provided by these regulations, the organization's exemption will be recognized retroactively to the date the organization was organized, provided its purpose, organization and operation (including compliance with the applicable nondiscrimination requirements) during the period prior to the date of the determination letter are in accordance with the applicable law. However, if the required notice is filed after the time provided by these regulations, exemption will be recognized only for the period after the application is filed with the Internal Revenue Service. The date of filing is the date of the United States postmark on the cover in which an exemption application is mailed or, if no postmark appears on the cover, the date the application is stamped as received by the Service. If an extension for filing the required notice has been granted to the organization, a notice filed on or before the last day specified in the extension will be considered timely and not the otherwise applicable date under Q&A-6.

Q-8: What is the effect on exemption of the filing of an incomplete notice?

A-8: Although a properly completed and executed Form 1024 together with the required additional information (See Q&A-4 and Q&A-5) must be submitted to satisfy the notice required by section 505(c), the failure to file, within the time specified, all of the information necessary to complete such notice will not alone be sufficient to deny recognition of exemption from the date of organization to the date the completed information is submitted to the Service. If the notice which is filed with the Service within the required time is substantially complete, and the organization supplies the necessary additional information requested by the Service within the additional time allowed, the original notice will be considered timely. However, if the notice is not substantially complete or the additional information is not provided within the additional time allowed, exemption will be recognized only from the date of filing of the additional information.

SECTION 501(c)(9) and (17) ORGANIZATIONS ORGANIZED ON OR BEFORE JULY 18, 1984

Q-9: What is the notice required of an organization or trust organized on or before July 18, 1984, that claims exempt status as an organization described in section 501(c)(9) or (17)?

A-9: Section 505(c) provides a special rule for existing organizations and trusts organized on or before July 18, 1984. Such an organization or trust will not be treated as described in paragraphs (9) or (17) of section 501(c) unless the organization or trust notifies the Internal Revenue Service in the manner and within the time prescribed in these regulations that it is claiming exemption under the particular section. The type of notice, the manner for filing that notice, and the additional information required is the same as that set forth in Q&A-3 through Q&A-5 for new organizations.

Q-10: When must the required notice be filed by an organization or trust organized on or before July 18, 1984?

A-10: An organization or trust organized on or before July 18, 1984, that claims exempt status as an organization described in section 501(c)(9) or (17), must file the required notice before February 4, 1987. An extension of time for filing the required notice may be granted by the district director if the request is submitted before the due date of the notice and it is demonstrated that additional time is needed.

Q-11: What is the effective date of exemption for an organization or trust organized on or before July 18, 1984, that has submitted the required notice?

A-11: If the required notice is filed within the time provided by these regulations, the organization's exemption will be recognized retroactively to the date the organization was organized, provided its purpose, organization and operation (including compliance with the applicable nondiscrimination requirements) during the period prior to the date of the determination letter are in accordance with the applicable law. If, on the other hand, the required notice is filed after the time provided by these regulations, exemption will be recognized only for the period after the notice is received by the Internal Revenue Service. See Q&A-7 for a further discussion of "date of filing." See also Q&A-8 for the effect on exemption of a notice that has been timely filed but is incomplete.

EXCEPTIONS TO NOTICE REQUIREMENT

Q-12: Are any organizations or trusts claiming recognition of exemption as an organization described in section 501(c)(9) or (17) excepted from the notice requirement of section 505(c)?

A-12: An organization or trust that has previously notified the Internal Revenue Service of its claim to exemption by filing Form 1024 is not required, under section 505(c), to renotify the Service. Thus, an organization that has filed a Form 1024 that is pending with the Service need not refile that form. Also, an organization that has received a ruling or determination letter from the Service recognizing its exemption from taxation need not submit the notification required by section 505(c).

Par. 18. There is added the following new section after §1.512(a)-4 to read as follows:

§1.512(a)-5T Questions and answers relating to the unrelated business taxable income of organizations described in paragraphs (9), (17) or (20) of section 501(c). (Temporary)

Q-1: What does section 512(a)(3), as amended by the Tax Reform Act of 1984 (Act), provide with respect to organizations described in paragraphs (9), (17) or (20) of section 501(c)?

A-1: In general, section 512(a)(3), as amended by section 511 of the Act, extends the rules for determining the unrelated business income tax of voluntary employees' beneficiary associations (VEBAs) to supplemental unemployment compensation benefit trusts (SUBs) and group legal service organizations (GLSOs). The section also restricts the amount of income that may be set aside by such organizations for exempt purposes.

Q-2: What is the effective date of the amendments to section 512(a)(3)?

A-2: The amendments to section 512(a)(3) will apply to income earned by VEBAs, SUBs or GLSOs after December 31, 1985, in the taxable years of such organizations ending after such date. For purposes of applying section 512(a)(3) to the first taxable year of such an organization ending after December 31, 1985, the income of the VEBA, SUB or GLSO earned after December 31, 1985, will be determined by allocating the total income earned for such taxable year on the basis of the calendar year 1985 and 1986 months in such taxable year. However, if a VEBA, SUB or GLSO is part of a plan that is maintained pursuant to one or more collective bargaining agreements (i) between employee representatives and one or more employers, and (ii) which are in effect on July 1, 1985 (or ratified on or before that date), the amendments do not apply to income earned in a taxable year of a VEBA, SUB or GLSO beginning before the termination of the last of the collective bargaining agreements pursuant to which the plan is maintained (determined without regard to any extension of the contract agreed to after July 1, 1985). For purposes of the preceding sentence, any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added under section 511 of the Tax Reform Act 1984 (i.e., requirements under sections 419, 419A, 512(a)(3)(E), and 4976) shall not be treated as a termination of such collective bargaining agreement.

Q-3: What amount of income may be VEBA, SUB or GLSO set aside for exempt purposes?

A-3: (a) Pursuant to section 512(a)(3)(E)(i), the amounts set aside in a VEBA, SUB, or GLSO (including a VEBA, SUB, or GLSO that is part of a 10 or more employer plan, as defined in section 419A(f)(6)(B)) as of the close of a taxable year of such VEBA, SUB, or GLSO to provide for the payment of life, sick, accident, or other benefits may not be taken into account for purposes of determining "exemption function income" to the extent that such amounts exceed the qualified asset account limit, determined under sections 419A(c) and 419A(f)(7), for such taxable year of the VEBA, SUB, or GLSO. In calculating the qualified asset account limit for this purpose, a reserve for post-retirement medical benefits under section 419A(c)(2)(A) is not to be taken into account.

(b) The exempt functions income of a VEBA, SUB, or GLSO for a taxable year of such an organization, under section 512(a)(3)(B), includes: (1) certain amounts paid by members of the VEBA, SUB, or GLSO within the meaning of the first sentence of section 512(a)(3)(B) ("member contributions"); and (2) other income of the VEBA, SUB, or GLSO (including earnings on member contributions) that is set aside for the payment of life, sick, accident, or other benefits to the extent that the total amount set aside in the VEBA, SUB or GLSO as of the close of the taxable year for any purpose (including member contributions and other income set aside in the VEBA, SUB, or GLSO as of the close of the year) does not exceed the qualified asset account limit for such taxable year of the organization. For purposes of section 512(c)(3)(B), member contributions include both employee contributions and employer contributions to the VEBA, SUB, or GLSO. In calculating the total amount set aside in a VEBA, SUB, or GLSO as of the close of a taxable year, certain assets with useful lives extending substantially beyond the end of the taxable year (e.g., buildings, and licenses) are not to be taken into account to the extent they are used in the provision of life, sick, accident, or other benefits. For example, cash and securities (and similar investments) held by a VEBA, SUB or GLSO are not disregarded in calculating the total amount set aside for this purpose because they are used to pay welfare benefits, rather than merely used in the provision of such benefits. Accordingly, the unrelated business taxable income of a VEBA, SUB, or GLSO for a taxable year of such an organization generally will equal the lesser of two amounts: (1) the income of the VEBA, SUB, or GLSO for the taxable year (excluding member contributions), or (2) the excess of the total amount set aside as of the close of the taxable year (including member contributions, and excluding certain assets with a useful life extending substantially beyond the end of the taxable year to the extent they are used in the provision of welfare benefits) over the qualified asset account limit (calculated without regard to the otherwise permitted reserve for post-retirement medical benefits) for the taxable year. See §1.419A-2T for special rules relating to collectively bargained welfare benefit funds.

(c) The income of a VEBA, SUB, or GLSO for any taxable year includes gain realized by the organization on the sale or disposition of any assset during such year. The gain realized by a VEBA, SUB, or GLSO on the sale or disposition of an asset is equal to the amount realized by the organization over the basis of such asset (in the hands of the organization), reduced by any qualified direct costs attributable to such asset (under paragraphs (b), (c) and (d) of Q&A-6 of §1.419-1T).

Q-4: What transition rules apply to "existing reserves for post-retirement medical or life insurance benefits"?

A-4: (a) Section 512(a)(3)(E)(iii)(I) provides that income that is either directly or indirectly attributable to "existing reserves for post-retirement medical or life insurance benefits" will not be treated as unrelated business taxable income. An "existing reserve for post-retirement medical or life insurance benefits" (as defined in section 512(a)(3)(E)(iii)(II)) is the total amount of assets actually set aside in a VEBA, SUB, or GLSO on July 18, 1984 (calculated in the manner set forth in Q&A-3 of this regulation, and adjusted under paragraph (c) of Q&A-11 of §1.419-1T), reduced by employer contributions to the fund on or before such date to the extent such contributions are not deductible for the taxable year of the employer containing July 18, 1984, and for any prior taxable year of the employer, for purposes of providing such post-retirement benefits. For purposes of the preceding sentence only, an amount that was not actually set aside on July 18, 1984, will be treated as having been actually set aside on such date if (1) such amount was incurred by the employer (without regard to section 461(h)) as of the close of the last taxable year of the VEBA, SUB, or GLSO ending before July 18, 1984, and (2) such amount was actually contributed to the VEBA, SUB, or GLSO within 8½ months following the close of such taxable year.

(b) In addition, section 512(a)(3)(E)(iii)(I) applies to existing reserves for such post-retirement benefits only to the extent that such "existing reserves" do not exceed the amount that could be accumulated under the principles set forth in Revenue Rulings 69-382, 1969-2 C.B. 28; 69-478, 1969-2 C.B. 29; and 73-599, 1973-2 C.B. 40. Thus, amounts attributable to such excess "existing reserves" are not within this transition rule even though they were actually set aside on July 18, 1984.

(c) All post-retirement medical or life insurance benefits (or other benefits to the extent paid with amounts set aside to provide post-retirement medical or life insurance benefits) provided after July 18, 1984 (whether or not the employer has maintained a reserve or fund for such benefits) are to be charged, first, against the "existing reserves" within this transition rule (including amounts attributable to "existing reserves" within this transition rule) for post-retirement medical benefits or for post-retirement life insurance benefits (as the case may be) and, second, against all other amounts. For this purpose, the qualified direct cost of an asset with a useful life extending substantially beyond the end of the taxable year (as determined under Q&A-6 of §1.419-1T) will be treated as a benefit provided and thus charged against the "existing reserve" based on the extent to which such asset is used in the provision of post-retirement medical benefits or post-retirement life insurance benefits (as the case may be). All plans of an employer providing post-retirement medical benefits are to be treated as one plan for purposes of section 512(a)(3)(E)(iii)(III), and all plans of an employer providing post-retirement life insurance benefits are to be treated as one plan for purposes of section 512(a)(3)(E)(iii)(III).

(d) In calculating the unrelated business taxable income of a VEBA, SUB, or GLSO for a taxable year of such organization, the total income of the VEBA, SUB, or GLSO for the taxable year is reduced by the income attributable to "existing reserves" within the transition rule before such income is compared to the excess of the total amount set aside as of the close of the taxable year over the qualified asset account limit for the taxable year. Thus, for example, assume that the total income of a VEBA for a taxable year is $1,000, and that the excess of the total amount of the VEBA set aside as of the close of the taxable year over the applicable qualified asset account limit is $600. Assume also that of the $1,000 of total income, $500 is attributable to "existing reserves" within the transition rule of section 512(a)(3)(E)(iii)(I). The unrelated business income of this VEBA for the taxable year is equal to the lesser of the following two amounts: (1) the total income of the VEBA for the taxable year ($1,000), reduced to the extent that such income is attributable to "existing reserves" within the transition rule ($500); or (2) the excess of the total amount set aside as of the close of the taxable year over the applicable qualified asset account limit ($600). Thus, the unrelated business income of this VEBA for the taxable year is $500.

Par. 19. The following new section is added immediately after §1.1041-1T:

§1.1042-1T Questions and answers relating to the sales of stock to employee stock ownership plans or certain cooperatives. (Temporary)

Q-1: What does section 1042 provide?

A-1: (a) Section 1042 provides rules under which a taxpayer may elect not to recognize gain in certain cases where "qualified securities" are sold to a qualifying employee stock ownership plan or worker-owned cooperative in taxable years of the seller beginning after July 18, 1984, and "qualified replacement property" is purchased by the taxpayer within the "replacement period." If the requirements of Q&A-2 of this section are met, and if the taxpayer makes an election under section 1042(a) in accordance with Q&A-3 of this section, the gain realized by the taxpayer on the sale of the qualified securities is recognized only to the extent that the amount realized on such sale exceeds the cost to the taxpayer of the qualified replacement property.

(b) Under section 1042, the term "qualified securities" means employer securities (as defined in section 409(l)) with respect to which each of the following requirements is satisfied: (1) the employer securities were issued by a domestic corporation; (2) for at least one year before and immediately after the sale, the domestic corporation that issued the employer securities (and each corporation that is a member of a "controlled group of corporations" with such corporation for purposes of section 409(l)) has no stock outstanding that is readily tradable on an established market; (3) as of the time of the sale, the employer securities have been held by the taxpayer for more than 1 year; and (4) the employer securities were not received by the taxpayer in a distribution from a plan described in section 401(a) or in a transfer pursuant to an option or other right to acquire stock to which section 83, 422, 422A, 423, or 424 applies.

(c) The term "replacement period" means the period which begins 3 months before the date on which the sale of qualified securities occurs and which ends 12 months after the date of such sale. A replacement period may include any period which occurs prior to July 19, 1984.

(d) The term "qualified replacement property" means any securities (as defined in section 165(g)(2)) issued by a domestic corporation which does not, for the taxable year of such corporation in which the securities are purchased by the taxpayer, have passive investment income (as defined in section 1362(d)(3)(D)) that exceeds 25 percent of the gross receipts of such corporation for the taxable year preceding the taxable year of purchase. In addition, securities of the domestic corporation that issued the employer securities qualifying under section 1042 (and of any corporation that is a member of a "controlled group of corporations" with such corporation for purposes of section 409(l)) will not qualify as "qualified replacement property."

(e) For purposes of section 1042(a), there is a "purchase" of qualified replacement property only if the basis of such property is determined by reference to its cost to the taxpayer. If the basis of the qualified replacement property is determined by reference to its basis in the hands of the transferor thereof or another person, or by reference to the basis of property (other than cash or its equivalent) exchanged for such property, then the basis of such property is not determined solely by reference to its cost to the taxpayer.

Q-2: What is a sale of qualified securities for purposes of section 1042(b)?

A-2: (a) Under section 1042(b), a sale of qualified securities is one under which all of the following requirements are met:

(1) The qualified securities are sold to an employee stock ownership plan (as defined in section 4975(e)(7)) maintained by the corporation that issued the qualified securities (or by a member of the "controlled group of corporations" with such corporation for purposes of section 409(l)) or to an eligible worker-owned cooperative (as defined in section 1042(c)(2));

(2) The employee stock ownership plan or eligible worker-owned cooperative owns, immediately after the sale, 30 percent or more of the total value of the employer securities (within the meaning of section 409(l)) outstanding as of such time;

(3) No portion of the assets of the employee stock ownership plan or eligible worker-owned cooperative attributable to qualified securities that are sold to the plan or cooperative by the taxpayer or by any other person in a sale with respect to which an election under section 1042(a) is made accrue under the plan or are allocated by the cooperative, either directly or indirectly and either concurrently with or at any time thereafter, for the benefit of (i) the taxpayer; (ii) any person who is a member of the family of the taxpayer (within the meaning of section 267(c)(4)); or (iii) any person who owns (after the application of section 318(a)), at any time after July 18, 1984, and until immediately after the sale, more than 25 percent of in value of the outstanding portion of any class of stock of the corporation that issued the qualified securities (or of any member of the "controlled group of corporations" with such corporation for purposes of section 409(l)). For purposes of this calculation, stock that is owned, directly or indirectly, by or for a qualified plan shall not be treated as outstanding.

(4) The taxpayer files with the Secretary (as part of the required election described in Q&A-3 of this section) a verified written statement of the domestic corporation (or corporations) whose employees are covered by the plan acquiring the qualified securities or of any authorized officer of the eligible worker-owned cooperative, consenting to the application of section 4978(a) with respect to such corporation or cooperative.

(b) For purposes of determining whether paragraph (a)(2) above is satisfied, sales of qualified securities by two or more taxpayers may be treated as a single sale if such sales are made as part of a single, integrated transaction under a prearranged agreement between the taxpayers.

(c) For purposes of determining whether paragraph (a)(3) above is satisfied with respect to the prohibition against an accrual or allocation of qualified securities, the accrual or allocation of any benefits or contributions or other assets that are not attributable to qualified securities sold to the employee stock ownership plan or eligible worker-cooperative in a sale with respect to which an election under section 1042(a) is made (including any accrual or allocation under any other plan or arrangement maintained by the corporation or any member of the "the controlled group of corporations" with such corporation for purposes of section 409(l)) must be made without regard to the allocation of such qualified securities. Paragraph (a)(3) above may be illustrated in part by the following example: Individuals A, B, and C own 50, 25, and 25, respectively, of the 100 outstanding shares of common stock of Corporation X. Such shares constitute qualified securities as defined in Q&A-1 of this section. A and B, but not C, are employees of Corporation X. For the benefit of all its employees, Corporation X establishes an employee stock ownership plan that obtains a loan meeting the exemption requirements of section 4975(d)(3). The loan proceeds are used by the plan to purchase the 100 shares of qualified securities from A, B, and C, all of whom elect nonrecognition treatment under section 1042(a) with respect to the gain realized on their sale of such securities. Under the requirements of paragraph (a)(3) above, no part of the assets of the plan attributable to the 100 shares of qualified securities may accrue under the plan (or under any other plan or arrangement maintained by Corporation X) for the benefit of A or B or any person who is a member of the family of A or B (as determined under section 267(c)(4)). Furthermore, no other assets of the plan or assets of the employer may accrue for the benefit of such individuals in lieu of the receipt of assets attributable to such qualified securities.

(d) A sale under section 1042(a) shall not include any sale of securities by a dealer or underwriter in the ordinary course of its trade or business as a dealer or underwriter, whether or not guaranteed.

Q-3: What is the time and manner for making the election under section 1042(a)?

A-3: (a) The election not to recognize the gain realized upon the sale of qualified securities to the extent provided under section 1042(a) shall be made in a "statement of election" attached to the taxpayer's income tax return filed on or before the due date (including extensions of time) for the taxable year in which the sale occurs. If a taxpayer does not make a timely election under this section to obtain section 1042(a) nonrecognition treatment with respect to the sale of qualified securities, it may not subsequently make an election on an amended return or otherwise. Also, an election once made is irrevocable.

(b) The statement of election shall provide that the taxpayer elects to treat the sale of securities as a sale of qualified securities under section 1042(a), and shall contain the following information:

(1) A description of the qualified securities sold, including the type and number of shares;

(2) The date of the sale of the qualified securities;

(3) The adjusted basis of the qualified securities;

(4) The amount realized upon the sale of the qualified securities;

(5) The identity of the employee stock ownership plan or eligible worker-owned cooperative to which the qualified securities were sold; and

(6) If the sale was part of a single, interrelated transaction under a prearranged agreement between taxpayers involving other sales of qualified securities, the names and taxpayer

identification numbers of the other taxpayers under the agreement and the number of shares sold by the other taxpayers. See Q&A-2 of this section.

If the taxpayer has purchased qualified replacement property at the time of the election, the taxpayer must attach as part of the statement of election a "statement of purchase" describing the qualified replacement property, the date of the purchase, and the cost of the property, and declaring such property to be the qualified replacement property with respect to the sale of qualified securities. Such statement of purchase must be notarized by the later of thirty days after the purchase or March 6, 1986. In addition, the statement of election must be accompanied by the verified written statement of consent required under Q&A-2 of this section with respect to the qualified securities sold.

(c) If the taxpayer has not purchased qualified replacement property at the time of the filing of the statement of election, a timely election under this Q&A shall not be considered to have been made unless the taxpayer attaches the notarized statement of purchase described above to the taxpayer's income tax return filed for the taxable year following the year for which the election under section 1042(a) was made. Such notarized statement of purchase shall be filed with the district director or the director of the regional service center with whom such election was originally filed, if the return is not filed with such director.

Q-4: What is the basis of qualified replacement property?

A-4: If a taxpayer makes an election under section 1042(a), the basis of the qualified replacement property purchased by the taxpayer during the replacement period shall be reduced by an amount equal to the amount of gain which was not recognized. If more than one item of qualified replacement property is purchased, the basis of each of such items shall be reduced by an amount determined by multiplying the total gain not recognized by reason of the application of section 1042(a) by a fraction, the numerator of which is the cost of such item of property and the denominator of which is the total cost of all such items of property. For the rule regarding the holding period of qualified replacement property, see section 1223(13).

Q-5: What is the statute of limitations for the assessment of a deficiency relating to the gain on the sale of qualified securities?

A-5: (a) If any gain is realized by the taxpayer on the sale of any qualified securities and such gain has not been recognized under section 1042(a) in accordance with the requirements of this section, the statutory period provided in section 6501(a) for the assessment of any deficiency with respect to such gain shall not expire prior to the expiration of 3 years from the date of receipt, by the district director or director of regional service center with whom the statement of election under 1042(a) was originally filed, of:

(1) a notarized statement of purchase as described in Q&A-3;

(2) a written statement of the taxpayer's intention not to purchase qualified replacement property within the replacement period; or

(3) a written statement of the taxpayer's failure to purchase qualified replacement property within the replacement period.

In those situations when a taxpayer is providing a written statement of an intention not to purchase or of a failure to purchase qualified replacement property, the statement shall be accompanied, where appropriate, by an amended return for the taxable year in which the gain from the sale of the qualified securities was realized, in order to reflect the inclusion in gross income from that year of gain required to be recognized in connection with such sale.

(b) Any gain from the sale of qualified securities which is required to be recognized in connection with such sale.

(b) Any gain from the sale of the qualified securities was realized, in order to reflect the inclusion in gross income for that year of gain required to be recognized in connection with such sale.

(b) Any gain from the sale of qualified securities which is required to be recognized due to a failure to meet the requirements under section 1042 shall be included in the gross income for the taxable year in which the gain was realized. If any gain from the sale of qualified securities is not recognized under section 1042(a) in accordance with the requirements of this section, any deficiency attributable to any portion of such gain may be assessed at any time before the expiration of the 3-year period described in this Q&A, notwithstanding the provision of any law or rule of law which would otherwise prevent such assessment.

Q-6: When does section 1042 become effective?

A-6: Section 1042 applies to sales of qualified securities in taxable years of sellers beginning after July 18, 1984.

ESTATE TAX REGULATIONS
(26 CFR Part 20)

Par. 20. The following new section is added after §20.2039-5 to read as follows:

§20.2039-1T Limitations and repeal of estate tax exclusion for qualified plans and individual retirement plans (IRAs). (Temporary)

Q-1: Are there any exceptions to the general effective dates of the $100,000 limitation and the repeal of the estate tax exclusion for the value of interests under qualified plans and IRAs described in section 2039(c) and (e)?

A-1: (a) Yes. Section 245 of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) [Pub. L. 97-248, 1982-2 C.B. 462, 522] limited the estate tax exclusion to $100,000 for estates of decedents dying after December 31, 1982. Section 525 of the Tax Reform Act of 1984 (TRA of 1984) repealed the exclusion for estates of decedents dying after December 31, 1984.

(b) Section 525(b)(3) of the TRA of 1984 amended section 245 of TEFRA to provide that the $100,000 limitation on the exclusion for the value of a decedent's interest in a plan or IRA will not apply to the estate of any decedent dying after December 31, 1982, to the extent that the decedent-participant was in pay status on December 31, 1982, with respect to such interest and irrevocably elected the form of benefit payable under the plan or IRA (including the form of any survivor benefits) with respect to such interest before January 1, 1983.

(c) Similarly, the TRA of 1984 provides that the repeal of the estate tax exclusion for the value of a decedent's interest in a plan or IRA will not apply to the estate of a decedent dying after December 31, 1984, to the extent that the decedent-participant was in pay status on December 31, 1984, with respect to such interest and irrevocably elected the form of benefit payable under the plan or IRA (including the form of any survivor benefits) with respect to such interest before July 18, 1984.

Q-2: What is the meaning of "in pay status" on the applicable date?

A-2: A participant was in pay status on the applicable date with respect to a portion of his or her interest in a plan or IRA if such portion is to be paid in a benefit form that has been elected on or before such date and the participant has received, on or before such date, at least one payment under such benefit form.

Q-3: What is required for an election of the form of benefit payable under the plan to have been irrevocable as of any applicable date?

A-3: As of any applicable date, an election of the form of benefit payable under a plan is irrevocable if, as of such date, it was a written irrevocable election that, with respect to all payments to be received after such date, specified the form of distribution (e.g., lump sum, level dollar annuity, formula annuity) and the period over which the distribution would be made (e.g., single life, joint and survivor, term certain). An election is not irrevocable as of any applicable date if, on or after such date, the form or period of the distribution could be determined or altered by any person or persons. an election does not fail to be irrevocable as of an applicable date merely because the beneficiaries were not designated as of such date or could be changed after such date. If any interest in any IRA may not, by law or contract, be subject to an irrevocable election described in this section, any election of the form of benefit payable under the IRA does not satisfy the requirement that an irrevocable election have been made.

PENSION EXCISE TAX REGULATIONS

(26 CFR Part 54)

Par. 21. There is added the following new section after §54.4975-15 to read as follows:

§54.4976-1T Questions and answers relating to taxes with respect to welfare benefit funds. (Temporary)

Q-1: What does section 4976 provide?

A-1: Section 4976 imposes a tax on employers who provide disqualified benefits through a welfare benefit fund. The tax imposed is equal to 100 percent of the disqualified benefit.

Q-2: What constitutes a disqualified benefit?

A-2: A disqualified benefit is (a) any post-retirement medical or life insurance benefit provided with respect to a key employee (as defined in section 419A(d)(3)) through a welfare benefit fund if a separate account is required to be established for such employee under section 419A(d) and the cost for such coverage is not charged against or paid from such separate account; (b) any post-retirement medical or life insurance benefit provided through a welfare benefit fund with respect to an individual in whose favor discrimination is prohibited unless the plan of which the fund is a part meets the requirements of section 505(b) with respect to that benefit; and (c) any portion of the fund which reverts to the benefit of the employer. A post-retirement medical or life insurance benefit provided with respect to a key employee will not constitute a disqualified benefit even though such benefit is not provided through a separate account if the cost of such benefit is paid by the employer in the taxable year in which the benefit is provided and there is not (and there is not required to be) a separate account with an outstanding credit balance maintained for the key employee.

Q-3: What is the effective date of section 4976?

A-3: (a) Generally, section 4976 applies to disqualified benefits provided by a welfare benefit fund after December 31, 1985. However, a disqualified benefit, as defined in section 4976(b)(1) or (2), is not subject to section 4976(a) if it is provided from "existing reserves for post-retirement medical or life insurance benefits" that are within the transition rule set forth in section 512(a)(3)(E)(iii) and Q&A-4 of §1.512(a)-5T (or would be if such transition rule applied to such welfare benefit fund). For example, if a welfare benefit fund in existence on July 18, 1984, provides an individual in whose favor discrimination is prohibited with a post-retirement life insurance benefit after December 31, 1985, that does not meet the requirements of section 505(b) and if the welfare benefit fund received no contributions after July 18, 1984, then the disqualified benefit provided by the fund is not subject to section 4976(a).

(b) A welfare benefit fund will be able to avoid the application of section 4976(b)(1) and (2) if the employer withdraws from such fund, before April 7, 1986, any amounts that are not attributable to "existing reserves for post-retirement medical or life insurance benefits" because they were neither actually set aside nor treated as actually set aside under Q&A-4 of §1.512(a)-5T, on July 18, 1984. The employer making such a withdrawal must include the amount in income for the first taxable year ending after July 18, 1984, or, to the extent that the withdrawn amount is attributable to the following taxable year, for such following taxable year. Such a withdrawal will not be treated as an impermissible distribution or reversion under section 501(c)(9), and will not be treated as a disqualified benefit under section 4976(b)(3). Of course, to the extent that the welfare benefit fund contains amounts that are attributable to "existing reserves" but are not within the transition rule set forth in Q&A-4 of §1.512(a)-5T (as applied to welfare benefit funds), for example, because such amounts exceed the amounts that could have been accumulated under the principles set forth in Revenue Rulings 69-382, 1969-2 C.B. 28; 69-478, 1969-2 C.B. 29; and 73-599, 1973-2 C.B. 40, the fund will not be able to avoid the application of section 4976(b)(1) and (2) under this paragraph.

(c) In the case of a plan which is maintained pursuant to one or more collective bargaining agreements (1) between employee representatives and one or more employers and (2) which are in effect on July 1, 1985 (or ratified on or before that date), the provision does not apply to disqualified benefits provided in years beginning before the termination of the last of the collective bargaining agreements pursuant to which the plan is maintained (determined without regard to any extension of the contract agreed to after July 1, 1985). For purposes of the preceding sentence, any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added under section 511 of the Tax Reform Act 1984 (i.e., requirements under sections 419, 419A, 512(a)(3)(E), and 4976) shall not be treated as a termination of such collective bargaining agreement.

Par. 22. The following new section is added immediately after §54.4976-1T:

§54.4978-1T Questions and answers relating to the tax on certain dispositions by employee stock ownership plans and certain cooperatives. (Temporary)

Q-1: What does section 4978 provide?

A-1: Section 4978 imposes a tax (as determined under section 4978(b) and Q&A-2 of this section) on the amount realized on the disposition of any qualified securities, if:

(a) An employee stock ownership plan or eligible worker-owned cooperative acquires any qualified securities in a sale to which section 1042 applies;

(b) Such plan or cooperative disposes of any qualified securities during the 3-year period after the date on which any qualified securities were acquired in the sale to which section 1042 applies; and

(c) Either (1) the percentage of the total outstanding shares of the class of employer securities of which the disposed qualified securities are a part held by such plan or cooperative after such disposition is less than the percentage of the total outstanding shares of such class of employer securities held immediately after the sale to which section 1042 applies, or (2) the value of the employer securities held by such plan or cooperative immediately after such disposition is less than 30 percent of the total value of all employer securities outstanding at that time. For purposes of this section, the following terms have the same meanings given to such terms by the identified provisions: "employee stock ownership plan" (section 4975(e)(7)); "qualified securities" (section 1042(b)(1)); "eligible worker-owned cooperative" (section 1042(b)(2)); "employer securities" (section 409(l)). For purposes of determining what constitutes a disposition to which section 4978 applies, see Q&A-3 of this section.

Q-2: What is the amount of tax imposed under section 4978?

A-2: Section 4978 imposes a tax of 10 percent of the amount realized on the disposition of qualified securities. The amount realized that is subject to tax under section 4978 shall not exceed that portion of the amount realized that is allocable to qualified securities acquired within the 3-year period prior to the date of disposition and to which section 1042 applied ("restricted qualified securities"). In determining the amount realized (except as otherwise provided in Q&A-3 of this section), any disposition of employer securities with respect to which the condition contained in provision (c) of Q&A-1 is met shall be treated, first, as a disposition of restricted qualified securities (on a first in, first out basis) and, thereafter, as a disposition of any other employer securities. Thus, for example, if a plan disposes of more employer securities than the number of restricted qualified securities held by the plan at that time and immediately after such disposition the value of the employer securities held by the plan is less than 30 percent of the total value of all outstanding employer securities, the portion of the total amount realized that is allocable to restricted qualified securities subject to tax under section 4978 is determined by multiplying the total amount realized on the disposition by a fraction, the numerator of which is the total value of restricted qualified securities included in the disposition and the denominator of which is the total value of employer securities in the disposition.

Q-3: What constitutes a "disposition" under section 4978?

A-3: (a) Under section 4978, the term "disposition" includes any sale, exchange, or distribution. However, in the case of any exchange of qualified securities for stock of another corporation in any reorganization described in section 368(a)(1), such exchange shall not be treated as a disposition for purposes of section 4978.

(b) Section 4978 shall not apply to any disposition of qualified securities which is made by reason of:

(1) The death of the employee;

(2) The retirement of the employee after the employee has attained 59½ years of age;

(3) The disability of the employee (within the meaning of section 72(m)(5)); or

(4) The separation of the employee from service for any period which results in a 1-year break in service (within the meaning of section 411(a)(6)(A)).

Any disposition of employer securities within this paragraph and any disposition of employer securities with respect to which the condition contained in provision (c) of Q&A-1 of this section is not met shall be treated, first, as a disposition of securities that are not restricted qualified securities and, thereafter, as a disposition of restricted qualified securities (on a first-in, first-out basis).

(c) If restricted qualified securities held by an employee stock ownership plan or eligible worker-owned cooperative no longer meet the definition of qualified securities ("old restricted qualified securities") as a result of a transaction changing (1) the status of a corporation as an employer, or as a member of a controlled group of corporations including the employer, or (2) the existence of employer securities of the type described in section 409(l)(1), the disposition of such securities shall not be treated as a disposition of restricted qualified securities to which the tax under section 4978 is imposed if, within 90 days after such disposition, securities meeting the requirements of section 409(l) ("new restricted qualified securities") that are of equal value to the old restricted qualified securities (that are of equal value to the old restricted qualified securities (at the time of the disposition of the old restricted qualified securities) are substituted for such old restricted qualified securities. However, for purposes of determining the tax imposed under section 4978, old restricted qualified securities shall not be treated as if they retained their status as restricted qualified securities and now restricted qualified securities derived from the disposition of old restricted qualified securities pursuant to the preceding sentence shall be treated as restricted qualified securities for the remaining portion of the period during which the disposition of the old restricted qualified securities would have been subject to tax under section 4978.

Q-4: To whom does the tax under section 4978 apply?

A-4: The tax under section 4978 is imposed on the domestic corporation (or corporations) or the eligible worker-owned cooperative that made the written statement of consent as described in section 1042(a)(2)(B) and Q&A-2 of §1.1042-1T with respect to the disposition of the restricted qualified securities.

Q-5: When does section 4978, as enacted by the Tax Reform Act of 1984, become effective?

A-5: Section 4978 applies to the disposition of qualified securities acquired in a sale to which section 1042 applies. See Q&A-6 of §1.1042-1T for the effective date of section 1042.

PROCEDURE AND ADMINISTRATION REGULATIONS

(26 CFR Part 301)

Par. 23. The following new section is added after §301.7701-16 to read as follows:

§301.7701-17T Collective-bargaining plans and agreements. (Temporary)

Q-1: How did the Tax Reform Act of 1984 (TRA of 1984) change the laws with respect to plans that are maintained pursuant to collective bargaining agreements?

A-1: (a) Many of the requirements and rules applicable to deferred compensation and welfare benefit plans are different for plans maintained pursuant to a collective bargaining agreement. Prior to the TRA of 1984, the Internal Revenue Code provided no clear definition of an employee representative or whether there is a collective bargaining agreement between such employee representative and one or more employers.

(b) Section 526(c) of the TRA of 1984 added a new condition under a new section 7701(a)(46) that must be satisfied in order for a plan to be considered to be a plan maintained pursuant to a collective bargaining agreement between employee representatives and one or more employers for purposes of the Code after March 31, 1984. If more than one-half of the membership of an organization is comprised of owners, officers, and executives of employers covered by the plan, then such organization is not an employee representative for purposes of determining whether a plan is to be treated as maintained pursuant to a collective bargaining agreement between employee representatives and one or more employers. Whether an individual is an owner, officer or executive is to be determined separately with respect to each employer. Additionally, section 7701(a)(46) provides that the Internal Revenue Service shall make the determination for purposes of the Code as to whether there is a collective bargaining agreement between employee representatives and one or more employers.

Q-2: If an organization does not fail to be an employee representative under the 50 percent or less test of section 7701(a)(46), is a plan maintained pursuant to an agreement between such organization and one or more employers necessarily treated, under the Code, as a plan maintained pursuant to a collective bargaining agreement between an employee representative and one or more employers?

A-2: (a) No.

(b) Specific Code provisions generally require other conditions than that in section 7701(a)(46) to be satisfied in order for a plan to be considered to be collectively-bargained. For example, in order for a plan to be described in section 413(a), the Secretary of Labor must find that the plan is maintained pursuant to a collective bargaining agreement between employee representatives and one or more employers.

(c) Even if (1) the finding in the example in the preceding paragraph (b) is made by the Secretary of Labor, (2) the union has been recognized as exempt under section 501(c)(5), and (3) the percentage condition in section 7701(a)(46) is satisfied, the Internal Revenue Service has the authority, pursuant to section 7701(a)(46), to determine whether there is a collective bargaining agreement under the Code.

Par. 24. The authority citation for part 602 reads as follows:

Authority: 26 U.S.C. 7805

Par. 25. Section 602.101(c) is amended by inserting the following items in the appropriate places in the table:

§1.463-1T	1545-0916
§1.505(c)-1T	1545-0916
§1.1042-1T	1545-0916

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

Approved December 20, 1985.

RONALD A. PEARLMAN,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on January 29, 1986, 4:04 p.m., and published in the issue of the Federal Register for February 4, 1986, 51 F.R. 4312)

Section 79.—Group-Term Life Insurance Purchased for Employees

26 CFR 1.79-4T: Questions and answers relating to the nondiscrimination requirements for group-term life insurance. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 125.—Cafeteria Plans

26 CFR 1.125-2T: Question and answer relating to the benefits that may be offered under a cafeteria plan. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 133.—Interest on Certain Loans to Acquire Employer Securities

26 CFR 1.133-1T: Questions and answers relating to interest on certain loans used to acquire employer securities. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 162.—Trade or Business Expenses

26 CFR 1.162-10T: Questions and answers relating to the deduction of employee benefits under the Tax Reform Act of 1984; certain limits on amounts deductible. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 163.—Interest

26 CFR 1.163-1: Interest deduction in general. (Also Sections 61, 451, 461; 1.61-7, 1.451-1, 1.461-1.)

Interest; prepayment of Rule of 78's loan. An individual borrower who prepays a loan subject to the Rule of 78's, and who has been using the economic accrual method to account for interest expense, may deduct as interest the difference between the final payment based upon application of the Rule of 78's and the final payment based upon the economic accrual of interest. An individual borrower who uses the Rule of 78's to account for interest expense, in circumstances where it is still permitted, may deduct as interest the amount allocated to interest using the Rule of 78's when the loan is prepaid. The same rules apply to lenders.

Rev. Rul. 86-42

ISSUE

If a loan agreement provides that interest is earned in accordance with the Rule of 78's method, what portion of the last payment may be deducted as interest if the loan is prepaid?

FACTS

Situation 1

On November 26, 1981, an individual, *A*, borrowed $10,000 from a bank to use for home improvements. The terms of the financing agreement provided for a self-amortizing loan with level monthly payments of $222.44 for five years. The amortization schedule implies an effective rate of interest of 12 percent. The agreement further stated that interest was to be earned and principal to be amortized in accordance with the Rule of 78's method.

On May 26, 1984, *A* prepaid the loan in full. In accordance with the loan agreement, the last payment totaled $6,045.53. This amount included the monthly payment of $222.44 and the loan balance of $5,823.09, which was determined by the application of the Rule of 78's.

If the loan had been amortized using the effective interest rate of 12 percent instead of the Rule of 78's, the last payment would have totaled $5,963.38. This amount includes the monthly payment of $222.44 and the loan balance of $5,740.94, determined using an amortization schedule based upon the effective interest rate for the loan. Using the Rule of 78's, *A*'s total payment to the lender is $82.15 greater ($6,045.53 − $5,963.38). See Table 1 for an annual summary of the loan.

Loan Amount : $10,000
Term : 5 years
Effective Interest Rate : 12 percent
Monthly Payment : $222.44

	Annual Amortization Using Economic Accrual of Interest			*Annual Amortization Using Rule of 78's*		
	Interest	Principal	Balance	Interest	Principal	Balance
Dec. 31, 1981	$ 100.00	122.44	9,877.56	109.73	112.71	9,887.29
Dec. 31, 1982	1,100.92	1,568.36	8,309.20	1,174.07	1,495.21	8,392.08
Dec. 31, 1983	901.99	1,767.29	6,541.91	912.44	1,756.84	6,635.24
May 26, 1984	311.23	800.97	5,740.94	300.05	812.15	5,823.09

Note: The final payment is determined by adding the monthly payment ($222.44) to the loan balance on May 26, 1984, based upon the application of the Rule of 78's.

During the time the loan was outstanding, *A* used the effective interest rate for the loan as the basis for determining interest expense for federal tax purposes.

Situation 2

The facts are the same as in *Situation 1* except that *B* was the borrower and, during the time the loan was outstanding, *B* used the Rule of 78's as the basis for determining interest expense for federal tax purposes.

LAW AND ANALYSIS

Section 163(a) of the Code provides that all interest paid or accrued within the taxable year on indebtedness shall be allowed as a deduction in computing taxable income. Interest has been defined as compensation for the use or forbearance of money. *Deputy v. duPont*, 308 U.S. 488, 498 (1940), 1940-1 C.B. 118, 122; *Old Colony Railroad v. Commissioner*, 284 U.S. 552, XI-1 C.B. 274 (1932).

In *General American Life Insurance Co. v. Commissioner*, 25 T.C. 1265 (1956), *acq*., 1956-2 C.B. 5, the Tax Court held that prepayment charges for a loan are an additional fee for the use of money. Similar conclusions are reached in Rev. Rul. 57-198, 1957-1 C.B. 94, which considers a mortgage prepayment penalty, and Rev. Rul. 73-137, 1973-1 C.B. 68, which considers a prepayment charge under a retail installment contract.

Rev. Rul. 83-84, 1983-1 C.B. 97, considers the use of the Rule of 78's as a method to allocate interest to periods during the term of a loan. The ruling concludes that the borrowers with loans subject to the Rule of 78's may not deduct interest that exceeds the amount economically accrued using the effective rate of interest for their loans.

Rev. Proc. 83-40, 1983-1 C.B. 774, provides an exception to Rev. Rul. 83-84. It states that the Internal Revenue Service will accept the Rule of 78's method for computing a borrower's interest deductions for certain consumer loans as a matter of administrative convenience. The exception applies only when (1) there is a self-amortizing loan that requires level payments, at regular intervals at least annually, over a period not in excess of five years (with no balloon payment at the end of the loan term), and (2) the loan agreement expressly provides that interest is earned, or upon prepayment interest is treated as earned, in accordance with the Rule of 78's method.

In *Situation 1*, when *A* prepaid the loan on May 26, 1984, the final payment ($6,045.53) included the regular monthly payment ($222.44) and the balance due ($5,740.94) based upon amortizing the loan at its effective interest rate. The final payment also included an "additional" amount ($82.15), which was the difference between the balance due based upon the Rule of 78's and the balance due based upon the economic accrual of interest ($5,823.09 − $5,740.94). This "additional" amount is similar to the prepayment charges for the loans in Rev. Rul. 57-198 and Rev. Rul. 73-137, because it is a fee for the use of money that became payable in the year of prepayment. Accordingly, *A* may deduct this sum ($82.15) as interest in 1984, as well as the amount of the regular monthly payment allocated to interest using the effective interest rate.

In *Situation 2*, Rev. Proc. 83-40 permits *B* to use the Rule of 78's. Thus, *B*'s interest deduction equals the amount of the regular monthly payment allocated to interest under the Rule of 78's. Using this allocation method, the final payment ($6,045.53) includes the regular monthly payment ($222.44) and the balance due ($5,823.09) based upon the application of the Rule of 78's. The "additional" amount described in *Situation 1* does not exist in *Situation 2*. In *Situation 2*, because *B* used the Rule of 78's method to allocate payments between principal and interest, the difference between the balance due based on the Rule of 78's and the balance due based on the economic accrual of interest had already been allocated to interest over the term of the loan prior to prepayment.

It should be noted that if a lender is using the economic accrual method to account for interest income for a loan subject to the Rule of 78's, the additional amount received upon prepayment, in excess of the loan balance computer using the economic accrual method, is interest income in the year of payment.

HOLDING

In *Situation 1*, *A* may deduct as interest for 1984 the difference between the final payment based upon application of the Rule of 78's and the final payment based upon the economic accrual of interest, in additional to the amount of each regular monthly payment allocated to interest using the economic accrual method (including the last such payment).

In *Situation 2*, *B* may deduct as interest for 1984 the sum of the amount of each monthly payment allocated to interest based upon the Rule of 78's.

Section 302.—Distributions in Redemption of Stock

26 CFR 1.302-1: General

Checklist of information to be included in requests for rulings under sections 302 and 311 with respect to redemptions of stock. See Rev. Proc. 86-18, page 40.

Section 311.—Taxability of Corporation on Distribution

26 CFR 1.311-1: General.

Checklist of information to be included in requests for rulings under sections 302 and 311 with respect to redemptions of stock. See Rev. Proc. 86-18, page 40.

Section 402.—Taxability of Beneficiary of Employees' Trust

26 CFR 1.402(a)(5)-1T: Rollovers of partial distributions from qualified trusts and annuities. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 404.—Deduction for Contributions of an Employer to an Employees' Trust or Annuity Plan and Compensation Under a Deferred-Payment Plan

26 CFR 1.404(a)-1T: Questions and answers relating to deductibility of deferred compensation and deferred benefits for employees. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 419.—Treatment of Funded Welfare Benefit Plans

26 CFR 1.419-1T: Treatment of welfare benefit funds. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4

Section 419A.—Qualified Asset Account; Limitation on Additions to Account

26 CFR 1.419A-1T: Qualified asset account limitation of additions to account. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 451.—General Rule For Taxable Year of Inclusion

26 CFR 1.451-1: General rule for taxable year of inclusion.

What is the proper amount to include in income when a loan subject to the Rule of 78's is prepaid? See Rev. Rul. 86-42, page 33.

Section 461.—General Rule for Taxable Year of Deduction

26 CFR 1.461-1: General rule for taxable year of deduction.

What is the proper amount to include in income when a loan subject to the Rule of 78's is prepaid? See Rev. Rul. 86-42, page 33.

26 CFR 1.461(h)-4T: Questions and answers relating to the economic performance requirement for certain employee benefits. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 463.—Accrual of Vacation Pay

26 CFR 1.463-1T: Transitional rule for vested accrued vacation pay. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 505.—Additional Requirements for Organizations Described in Paragraph (9), (17), or (20) of Section 501(c)

26 CFR 1.505(c)-1T: Questions and answers relating to the notification requirement for recognition of exemption under paragraphs (9), (17) and (20) of section 501(c). (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 512.—Unrelated Business Taxable Income

26 CFR 1.512(a)-5T: Questions and answers relating to the unrelated business taxable income of organizations described in paragraphs (9), (17) or (20) of section 501(c). (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 1042.—Sales of Stock to Stock Ownership Plans or Certain Cooperatives

26 CFR 1.1042-1T: Questions and answers relating to the sales of stock to employee stock ownership plans or certain cooperatives. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 2039.—Annuities

26 CFR 20.2039-1T: Limitations and repeal of estate tax exclusion for qualified plans and individual retirement plans (IRAs). (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 4051.—Imposition of Tax on Heavy Trucks and Trailers Sold at Retail

26 CFR 145.4051-1: Imposition of tax on heavy trucks and trailers sold at retail.
(Also Section 7805; 301.7805.1.)

Determination of gross vehicle weight; postponement of effective date of Rev. Rul. 85-196. Rev. Rul. 85-196 is modified to provide that its conclusion will not be applied to sales prior to October 1, 1986.

Rev. Rul. 86-43

Rev. Rul. 85-196, 1985-51 I.R.B. 5, holds that for purposes of computing the gross vehicle weight of a vehicle pursuant to section 145.4051-1(e)(3) of the Temporary Excise Tax Regulations, the seller may not take into account any readily attachable components of the vehicle and that gross vehicle weight must be determined solely on the basis of the strength of the chassis frame and the axle capacity and placement.

Rev. Rul. 85-196 is modified to provide that its conclusion will not be applied to sales prior to October 1, 1986.

Further, during the period April 1, 1986, through September 30, 1986, the seller at retail of a heavy truck or trailer may not, by replacing a readily attachable component of the vehicle, lower the gross vehicle weight rating assigned to the vehicle by its manufacturer.

Section 4976.—Taxes With Respect to Funded Welfare Benefit Plans

26 CFR 54.4976-1T: Questions and answers relating to taxes with respect to welfare benefit funds. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 4978.—Tax on Certain Dispositions by Employee Stock Ownership Plans and Certain Cooperatives

26 CFR 54.4978-1T: Questions and answers relating to the tax on certain dispositions by employee stock ownership plans and certain cooperatives. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 4986.—Imposition of Tax

26 CFR 51.4986-1: Imposition of tax.

Whether the windfall profit tax severance tax adjustment applies to certain taxes imposed by the state of Wyoming. See Rev. Rul. 86-45, this page.

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26 CFR 51.4986-1: Imposition of tax.

Whether the windfall profit tax severance tax adjustment applies to certain taxes imposed by the State of New Mexico. See Rev. Rul. 86-46, page 37.

Section 4988.—Windfall Profit; Removal Price

26 CFR 51.4988-1: Windfall profit; removal price.

Whether the windfall profit tax severance tax adjustment applies to certain taxes imposed by the State of Wyoming. See Rev. Rul. 86-45, this page.

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26 CFR 51.4988-1: Windfall profit; removal price.

Whether the windfall profit tax severance adjustment applies to certain taxes imposed by the State of New Mexico. See Rev. Rul. 86-46, page 37.

Section 4996.—Other Definitions and Special Rules

26 CFR 51.4996-2: Severance tax adjustment.
(Also Sections 4986, 4988; 51.4986-1, 51.4988-1.)

Windfall profit tax; severance tax adjustment; Wyoming. The taxes imposed under Wyo. Stat. sections 39-6-302(g) and (h) are severance taxes within the meaning of section 4996(c) of the Code. The state portion of the tax imposed under Wyo. Stat. section 39-2-402 is also a severance tax within the meaning of section 4996(c). Rev. Rul. 82-87 amplified.

Rev. Rul. 86-45

ISSUE

Do the crude oil production taxes imposed by Wyoming Statutes sections 39-6-302(g) and (h) and 39-2-402 qualify as severance taxes for purposes of the crude oil windfall profit tax severance tax adjustment allowed by section 4988(a) of the Internal Revenue Code?

FACTS

Rev. Rul. 82-87, 1982-1 C.B. 189, holds, in part, that the tax imposed by Wyo. Stat. section 30-5-116 and two taxes imposed by Wyo. Stat. sections 39-6-302(a) and (b) (as in effect for removal years after 1980) on the production of crude oil are severance taxes for purposes of the crude oil windfall profit tax severance tax adjustment.

Wyo. Stat. section 39-6-302(g) (1985), added by 1981 Wyoming Session Laws Chapter 49, section 1, and amended by 1985 Wyoming Session Laws Chapter 182, section 1, imposes, except as otherwise provided in Wyo. Stat. section 39-6-302(h), an additional tax of 2 percent of the value of the gross product on the privilege of severing or extracting oil and gas.

Wyo. Stat. section 39-6-302(h), added by 1985 Wyoming Session Laws Chapter 182, Section 1, levies an excise tax of 1 1/2 percent of the value of the gross product on the privilege of severing or extracting oil and gas from collection wells prior to January 1, 1990. That section further provides that the taxes imposed by Wyo. Stat. sections 39-6-302(a), (b), and (g) do not apply to oil and gas subject to the tax imposed by section 39-6-302(h) but do apply to oil and gas extracted from collection wells on and after January 1, 1990. Wyo. Stat. section 39-6-301(a)(v) defines "collection wells" as meaning reservoir access holes drilled from underground shafts or tunnels from which oil or gas is produced.

Under Wyo. Stat. sections 39-6-301(a)(iv) and 39-6-304, the taxes imposed by section 39-6-302 for removal years after 1980 are computed based on actual production during each calendar quarter.

Wyo. Stat. section 39-2-402(a) authorizes the levy of property taxes for state purposes. Wyo. Stat. sections 39-2-402(b) through (f) authorize the levy of property taxes by counties, incorporated cities and towns, and other special districts. Under Wyo. Stat. sections 39-2-201 and 202, the State Board of Equalization is to value mines and mining claims for taxation based on the gross product for the preceding calendar year and certify the valuation to the county accessor.

Under Wyo. Stat. section 39-1-304(a), the State Board of Equalization is to annually certify the amount of the tax levy for state purposes to each County Board of Commissioners, and, under Wyo. Stat. section 39-2-403, the county board is to enter the requisite levy of record on or before the first Monday in August.

LAW AND ANALYSIS

Section 4986 of the Code imposes a tax on the windfall profit from taxable crude oil. It is to be paid by the producer of the crude oil.

Section 4988 of the Code allows a severance tax adjustment to be taken into account in determining the amount of the windfall profit.

Section 4996(c) of the Code provides that the severance tax adjustment on any barrel of crude oil is the amount by which (A) any severance tax imposed on the barrel exceeds (B) the severance tax that would have been imposed if the barrel had been valued at its adjusted base price. The term "severance tax" is defined as a tax (A) imposed by a state on the extraction of oil and (B) determined on the basis of the gross value of the extracted oil. Under section 4996(c)(3), a severance tax is not taken into account to the extent that its rate exceeds 15 percent.

Under section 51.4996-2(b) of the Excise Tax Regulations under the Crude Oil Windfall Profit Tax Act of 1980, the term "severance tax" does not include a tax levied on the value of reserves in the ground or a tax levied on the basis of net proceeds from production. Furthermore, a tax on the removal of crude oil from the ground levied as a fixed fee per barrel is not a severance tax within the meaning of section 4996(c) of the Code because the amount of that tax is not determined by reference to the gross value of the extracted oil.

The taxes imposed by Wyo. Stat. sections 39-6-302(g) and (h) are imposed by the state on the basis of the gross value of the extracted oil. Furthermore, when these taxes are added to the Wyoming severance taxes discussed in Rev. Rul. 82-87, the aggregate rate of tax does not exceed 15 percent.

The tax imposed under Wyo. Stat. section 39-2-402 is based on the gross value of the production of the calendar year preceding the year in which the tax is imposed. For example, the tax imposed in 1985 is based on 1984 production. For purposes of the windfall profit tax, therefore, producers may not deduct against 1985 production the section 39-2-402 tax that is imposed in 1985. The deduction is not allowed because there is no correspondence between the two amounts. Under section 4996(c) of the Code, the adjustment is the difference between the severance tax imposed and the severance tax that would have been imposed if the barrel had been valued at its adjusted base price. The difference between the tax actually imposed in any year by Wyo. Stat. section 39-2-402 and the tax that would have been imposed if the oil sold in that year and been valued at its adjusted base price will always be zero. The severance tax imposed in 1985 is based on the value of production in 1984 and will be the same regardless of the price of the oil or the number of barrels sold in 1985.

The severance tax offset is lost if it is not associated with the production of a particular period. In this case, if the severance tax is not associated with the production of the year preceding the imposition of the tax, a producer would be perpetually denied the effects of the severance tax adjustment with respect to Wyo. Stat. section 39-2-402, even though the rise in the price of oil due to decontrol raises the producer's severance tax liability. Further, a producer knows at the end of a calendar year the amount of production and the rate at which the tax will be assessed under Wyo. Stat. section 39-2-402. Therefore, to avoid the loss of the adjustment, the producer may take the severance tax adjustment in the current year in anticipation of the tax that will be assessed in the following year and that otherwise qualifies under section 4996(c) of the Code. This advance adjustment based on the following year's severance tax applies only for purposes of the windfall profit tax. For income tax purposes, a deduction for the severance tax may be taken only when the tax has been paid or accrued.

The tax imposed under Wyo. Stat. section 39-2-402 is not entirely a tax imposed by the state. Rather, it is a combination of taxes, some of which are imposed by the state and some of which are imposed by the counties (or other local governments). Although the tax is mandated by state statute and the rates for the state portion are set statewide, there is no requirement that any county have a tax for county purposes. Therefore, since section 4996(c) of the Code requires that a qualifying severance tax be a state tax, the adjustment must be limited to that portion of the tax imposed by the state, currently 4.3 percent. When this tax is added to the taxes discussed in Rev. Rul. 82-87 and the taxes imposed by Wyo. Stat. sections 39-6-302(g) and (h), the aggregate rate of tax does not exceed 15 percent. Therefore the state tax portion of the tax imposed by Wyo. Stat. section 39-2-402 may be taken into account for purposes of determining the severance tax adjustment.

HOLDING

The taxes imposed under Wyo. Stat. sections 39-6-302(g) and (h) are severance taxes within the meaning of section 4996(c) of the Code and may be taken into account in determining the severance tax adjustment.

The state portion of the tax imposed under Wyo. Stat. section 39-2-402 is a severance tax within the meaning of section 4996(c) of the Code and may be taken into account in determining the severance tax adjustment in the production year to which the tax relates.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 82-87 is amplified.

26 CFR 51.4996-2: Severance tax adjustment. (Also Sections 4986, 4988; 51.4986-1, 51.4988-1.)

Windfall profit tax; severance tax adjustment; New Mexico. The taxes imposed under N.M. Stat. Ann. sections 7-29-4, 7-30-4, and 7-31-4 are severance taxes within the meaning of section 4996(c) of the Code. The state portion of the tax imposed under N.M. Stat. Ann. 7-32-4 is also a severance tax within the meaning of section 4996(c). The portion of the tax imposed for purposes of other governmental units is not a severance tax.

Rev. Rul. 86-46

ISSUE

Are the taxes described below, imposed by the State of New Mexico on the production of oil, severance taxes for purposes of the crude oil windfall profit tax severance tax adjustment allowed by section 4988(a) of the Internal Revenue Code?

FACTS

New Mexico Statutes Annoted section 7-29-4 imposes, effective March 1, 1980, a tax of 3.75 percent of the taxable value of oil and of liquid hydrocarbons that are removed from natural gas at or near the wellhead and are severed and sold. Prior to March 1, 1980, the tax imposed by section 7-29-4 was a fixed fee per barrel.

N.M. Stat. Ann. section 7-30-4 imposes an Oil and Gas Conservation Tax of 0.19 percent of the taxable value of products sold.

N.M. Stat. Ann. section 7-31-4 imposes an Oil and Gas Emergency School Tax on the privilege of severing products in New Mexico. The tax is 3.15 percent of the taxable value of such products.

For purposes of these taxes (N.M. Stat. Ann. Sections 7-29-4, 7-30-4, and 7-31-4), taxable value generally is the value of the oil removed less royalties paid or due to exempt entities and the reasonable expense of trucking the oil from the property to the first place of market.

N.M. Stat. Ann. section 7-32-4 levies an Oil and Gas Ad Valorem Production Tax on the assessed value of products which are severed and sold from each production unit at the rate certified to the oil and gas accounting division of the taxation and revenue department by the department of finance and administration under N.M. Stat. Ann. section 7-37-7. The assessed value of products is determined under N.M. Stat. Ann. section 7-32-5 by applying the uniform assessment ratio (33 1/3 percent) to the taxable value of products (150 percent of the value of products less certain deductions).

Under N.M. Stat. Ann. sections 7-37-7 and 7-38-33 the secretary of finance and administration sets forth the tax rates for each of the governmental units that share in the tax levied under section 7-32-4 on a property. These rates are based on the budgets of each unit, legislative enactment of rates for state purposes, special levies, amounts needed to satisfy judgements, and debt service on general obligation bonds. The county treasurer prepares tax bills showing, among other things, the taxable value of the property, the allocation of net taxable value to the governmental units, the rate and amount of tax for each tax imposed for the governmental units sharing in the tax on the property under section 7-32-4. Any tax from a property is divided among those governmental units that have jurisdiction over the area in which the property is located. The governmental units that share in the tax include the state, counties, municipalities, and school districts.

LAW AND ANALYSIS

Section 4986 of the Code imposes a tax on the windfall profit from taxable crude oil. It is to be paid by the producer of the crude oil.

Section 4988 of the Code allows a severance tax adjustment to be taken into account in determining the amount of the windfall profit.

Section 4996(c) of the Code provides that the severance tax adjustment on any barrel of crude oil will be the amount by which (A) any severance tax imposed on the barrel exceeds (B) the severance tax that would have been imposed if the barrel had been valued at its adjusted base price. The term 'severance tax" is defined as a tax (A) imposed by a state on the extraction of oil and (B) determined on the basis of the gross value of the extracted oil. Under section 4996(c)(3), a severance tax is not taken into account to the extent that its rate exceeds 15 percent.

Under section 51.4996-2(b) of the Excise Tax Regulations under the Crude Oil Windfall Profit Tax Act of 1980, the term 'severance tax" does not include a tax levied on the value of reserves in the ground or a tax levied on the basis of net proceeds from production. Furthermore, a tax on the removal of crude oil from the ground levied as a fixed fee per barrel is not a severance tax within the meaning of section 4996(c) of the Code because the amount of that tax is not determined by reference to the gross value of the extracted oil.

Under section 51.4996-2(c)(2) of the regulations, the amount of a state's severance tax taken into account under section 51.4996-2(a) shall not exceed the amount which would have been imposed under that state's severance tax as in effect on March 31, 1979, unless that excess is attributable to an increase in the rate of the severance tax (or to the imposition of a severance tax) which applies equally to all portions of the gross value of each barrel of oil subject to that tax. For purposes of this subparagraph, the conversion of a tax levied at a fixed fee per barrel into a tax based on the gross value of oil removed constitutes an initial imposition of a severance tax.

The taxes imposed under N.M. Stat. Ann. sections 7-29-4, 7-30-4, and 7-31-4 are all imposed by the State on the basis of the gross value of each barrel of crude oil subject to the taxes. In addition, the tax imposed by section 7-29-4, which was converted from a fixed fee to a percentage of gross value after March 31, 1979, applies equally to all portions of the gross value of each barrel of oil subject to the tax.

The tax imposed under N.M. Stat. Ann. section 7-32-4 differs from the other taxes imposed by the State of New Mexico described above in several respects. Even though collected as a single tax it is made up of several taxes levied by the State for state purposes and levied on behalf of various local jurisdictions for local purposes. The rates of tax imposed for state purposes are uniform state wide and are set by the State. The rates of tax imposed for local purposes are based on various factors, such as budgets, special levies, and bond issues, which vary from one governmental unit to another. Under the statutory provisions for setting the rate of the Ad Valorem Production Tax, a change in the budget of a political subdivision of the State, or the approval of a special levy or general obligation bond issue by a political subdivision, will have the effect of changing the tax rate to be applied to oil produced from a property located within the jurisdiction of the political subdivision. Thus, even though the secretary of finance and administration formally sets the rates of tax for political subdivisions, those rates are indirectly, but significantly, determined by the political subdivisions of the State, and not by the State alone. This is not in substance a tax imposed by a state within the meaning of section 4996(c) of the Code.

HOLDINGS

The taxes imposed by N.M. Stat. Ann. sections 7-29-4, 7-30-4, and 7-31-4 are severance taxes within the meaning of section 4996(c) of the Code and may be taken into account in determining the severance tax adjustment to the extent that the aggregate amount of all severance taxes imposed by the

State of New Mexico does not exceed 15 percent.

The portion of the tax imposed under N.M. Stat. Ann. section 7-32-4 for state purposes is a severance tax for purposes of the windfall profit tax severance tax adjustment. The portion of the tax imposed for the purposes of other governmental units is not a severance tax for purpose of the windfall profit tax severance tax adjustment.

Section 7701.—Definitions

26 CFR 301.7701-17T: Collective-bargaining plans and agreements. (Temporary)

Effective dates and other issues arising under the employee benefit provisions of the Tax Reform Act of 1984. See T.D. 8073, page 4.

Section 7805.—Rules and Regulations

26 CFR 301.7805-1: Rules and regulations.

The effective date of Rev. Rul. 85-196, 1985-51 I.R.B. 5, is postponed until October 1, 1986. See Rev. Rul. 86-43, page 36.

Section 7871.—Indian Tribal Governments Treated As States for Certain Purposes

Indian tribal governments; treatment as states or political subdivisions. Rev. Ruls. 58-610, 68-231 and 74-179 are declared obsolete.

Rev. Rul. 86-44

The Indian Tribal Governmental Tax Status Act of 1982, 1983-1 C.B. 510, 511, added certain provisions to the Internal Revenue Code that pertained to the status of Indian tribal governments. For two years beginning in 1983, Indian tribal governments (or subdivisions thereof) are to be treated as states (or political subdivisions thereof) for specified federal tax purposes.

Before 1982, the Service had published several revenue rulings which either held or were based upon the assumption that an Indian tribe is neither a state nor a political subdivision. Rev. Rul. 58-610, 1958-2 C.B. 815, Rev. Rul. 68-231, 1968-1 C.B. 48, and Rev. Rul. 74-179, 1974-1 C.B. 279, applied variously to estate and gift taxes, charitable deductions, tax-exempt municipal bonds, and excise taxes and found Indian tribes to be communities rather than states or political subdivisions. As a result of the 1982 enactment, Rev. Rul. 84-93, 1984-1 C.B. 279, suspended Rev. Rul. 58-610, Rev. Rul. 68-231 and Rev. Rul. 74-179.

Section 7871 of the Code, added by the Indian Tribal Government Tax Status Act of 1982, describes the circumstances under which an Indian tribal government shall be treated as a state or a political subdivision. The term "Indian tribal government" is defined under section 7701(a)(40) to mean the governing body of any tribe, band, community, village, or group of Indians, or (if applicable) Alaska Natives, that is determined by the Secretary of the Treasury, after consultation with the Secretary of the Interior, to exercise governmental functions. Section 7871(d) provides that for purposes of section 7871, a subdivision of an Indian tribal government shall be treated as a political subdivision of a state if (and only if) the Secretary of the Treasury determines (after consultation with the Secretary of the Interior) that such subdivision has been delegated the right to exercise one or more of the substantial governmental functions of the Indian tribal government.

Rev. Proc. 83-87, 1983-2 C.B. 606, provides a list of Indian tribal governments that were to be treated as states for the two-year period. Rev. Proc. 84-36, 1984-1 C.B. 510, sets forth a list of subdivisions of Indian tribal governments that are to be treated as political subdivisions of states for the two-year period, and Rev. Proc. 84-37, 1984-1 C.B. 513, provides procedures under which a governmental unit of an Indian tribe or subdivision thereof may request a determination qualifying it for treatment as a state or political subdivision of a state for purposes of section 7871 of the Code.

Section 1065 of the Tax Reform Act of 1984, 1984-3 (Vol. 1) C.B. 556, made permanent the rules treating Indian tribal governments (or subdivisions thereof) as states (or political subdivisions thereof).

Rev. Proc. 86-17, page 40, this Bulletin, modifies Rev. Proc. 83-87, Rev. Proc. 84-36 and Rev. Proc. 84-37 to eliminate the two-year limitation period.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 58-610, Rev. Rul. 68-231, Rev. Rul. 74-179 and Rev. Rul. 84-93 are declared obsolete.

Certain revenue procedures suspended as to their respective applications to Indian tribes, or subdivisions thereof. See Rev. Proc. 86-17, page 40.

26 CFR 601.201: Rulings and determination letters.
(Also Section 7871.)

Rev. Proc. 86-17

SECTION 1. BACKGROUND

The Indian Tribal Governmental Tax Status Act of 1982, 1983-1 C.B. 510, 511, added certain provisions to the Internal Revenue Code that pertained to the status of Indian tribal governments. Forr two years beginning in 1983, Indian tribal governments (or subdivisions thereof) are to be treated as states (or political subdivisions thereof) for specified federal tax purposes.

Rev. Proc. 83-87, 1983-2 C.B. 606, provides a list of Indian tribal governments that were to be treated as states for the two-year period. Rev. Proc. 84-36, 1984-1 C.B. 510, sets forth a list of subdivisions of Indian tribal governments that are to be treated as political subdivisions of states for the two-year period, and Rev. Proc. 84-37, 1984-1 C.B. 513, provides procedures under which a governmental unit of an Indian tribe or subdivision thereof may request a determination qualifying it for treatment as a state or political subdivision of a state for purposes of section 7871 of the Code.

Section 1065 of the Tax Reform Act of 1984, 1984-3 (Vol. 1) C.B. 556, made permanent the rules treating Indian tribal governments (or subdivisions thereof) as states (or political subdivisions thereof).

SEC. 2. PROCEDURE

Rev. Proc. 83-87, Rev. Proc. 84-36 and Rev. Proc. 84-37 are modified by deleting the two-year limitation referred to therein.

SEC. 3. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 83-87, Rev. Proc. 84-36 and Rev. Proc. 84-37 are modified.

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26 CFR 601.201: Rulings and determination letters.
(Also Part I, Sections 302, 311; 1.302-1, 1.311-1.)

Rev. Proc. 86-18

SECTIONS 302 and 311
CHECKLIST QUESTIONNAIRE

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SECTION 1. PURPOSE

The purpose of this revenue procedure is to update Rev. Proc. 81-62, 1981-2 C.B. 684, which sets forth in a checklist questionnaire the information that must be included in a request for a ruling under sections 302 and 311 of the Internal Revenue Code, relating to distributions in redemption of stock.

SEC. 2. BACKGROUND

The Internal Revenue Service receives many requests for rulings in which the information relating to the proposed transaction is not sufficient to permit a determination to be made. In these cases, it is necessary to obtain additional facts from the taxpayer before the request for a letter ruling can be considered. Obtaining these additional facts is time consuming for both Service personnel and taxpayers and delays issuance of the ruling letter.

This checklist will facilitate the filing and processing of requests for rulings under sections 302 and 311 of the Code by showing specific information and representations to be included so that the requests will be as complete as possible when initially filed. Because the information and representations necessary to rule on a particular transaction depend upon all the facts and circumstances, information or representations in addition to those set forth in this revenue procedure may be required.

The authority and general procedures of the National Office of the Internal Revenue Service and of the office of the District Directors of Internal Revenue with respect to the issuance of letter rulings and determination letters are outlined in Rev. Proc. 86-1, 1986-1 I.R.B. 6. See also Rev. Proc. 86-3, 1986-1 I.R.B. 26, relating to areas in which advance rulings generally will not be issued. These revenue procedures, along with the present checklist revenue procedure, are subject to periodic updating by the Service. Therefore, careful attention should be given to ensure usage of the most current revenue procedures.

Careful attention to all requirements of these revenue procedures will aid in the timely processing of letter ruling requests.

SEC. 3. CHANGES

.01 Section 1 is modified to indicate that the purpose of the revenue procedure is to update Rev. Proc. 81-62.

.02 Section 2 is modified to state that representations are now required, and to update references to revenue procedures cited.

.03 Section 4 is modified to update references to Code sections.

.04 Section 5 is substantially altered. The taxpayer must now submit standard representations using the precise language specified herein, or submit an explanation why the representations cannot be made in the requested form. Sections 5.021, 5.032, 5.033, 5.041, 5.044, 5.051, and 5.052 are modified accordingly. To properly reflect applicable changes, some citations to Code sections and to revenue rulings and procedures have been added or deleted. Changes include:

1 Section 5.012 now requires taxpayers to submit information concerning any prior ruling requests submitted by the taxpayer (or predecessor) that were withdrawn in which the identical or similar issue was present.

2 Section 5.014 has been deleted.

3 Section 5.02 is modified to update references to revenue procedures cited.

4 Section 5.022(b) is modified to reflect the addition of section 318(a)(5)(E) to the Code.

5 Section 5.023 is amplified to request information concerning the acquisition by the Redeemed Shareholder of the redeemed stock.

6 Section 5.033(a) is modified to request information concerning changes in Corporation's outstanding equity in the past 5 years.

7 Section 5.033(b) is modified to request details of transactions involving any related corporation.

8 Section 5.033(c) is modified to include indirect sales or acquisitions of Corporation's stock by the Redeemed Shareholder.

9 Section 5.041(b)(2)(C) is modified to request supporting relevant authority for taxpayer's contention.

10 Section 5.041(c) is added and requests information and a representation if the Redeemed Shareholder is an entity.

11 Section 5.043 is modified to update reference to the partial liquidation section and to request supporting authority for taxpayer's contention.

12 Section 5.044(a)) is modified to request information if common stock is to be redeemed.

13 Section 5.062(b)(5) is modified to show changes in the recapture provisions.

14 Section 5.07 is modified to request general information, and requires taxpayers to list the specific rulings being requested and the authorities supporting the rulings.

.05 Section 6 is modified to substitute Associate Chief Counsel (Technical) for Assistant Commissioner (Technical), and CC:C:R for T:C:R.

.06 Section 7 is modified to state that Rev. Proc. 81-62 is superseded.

SEC. 4. TRANSACTIONS TO WHICH SECTION 303 OR 302(b)(4) OF THE CODE APPLIES

.01 *Section 303. Distribution in redemption to pay death taxes.*—To the extent the distribution is within the terms of section 303 of the Code, section 302(b)(1), (2) or (3) does not apply to the distribution. If the stock redeemed was included in a decedent's gross estate, see section 303 which treats these redemptions under certain circumstances as in full payment in exchange for the stock so redeemed.

.02 *Section 302(b)(4). Distribution in partial liquidation.*—If any part of the distribution will qualify as a partial liquidation under section 302(b)(4) of the Code, state the amount and the reason reasons why it qualifies under section 302(b)(4). See Rev. Proc. 81-42, 1981-2 C.B. 611.

SEC. 5. INFORMATION TO BE INCLUDED IN REQUESTS FOR RULINGS UNDER SECTIONS 302 AND 311 OF THE CODE

Each of the items in this section should be specifically dealt with in the letter ruling request. If an item is not applicable, so state, and breifly explain why. Standard representations are set forth throughout this section and are highlighted by the word "representation" in boldface type. These representations are of equal importance with the other factual information requested herein. The representations function to ensure that specific statutory and judicial requirements and administrative ruling guidelines are satisfied. Each representation set forth in this section should be submitted precisely in the languge requested. If a representation cannot be submitted as requested, an explanation must be given. Variations of the language of the representations may delay processing the ruling request and will not be accepted unless reasons satisfactory to the Service are submitted. Submission of the information and representations should follow the format of this revenue procedure as closely as possible, with appropriate descriptive headings. Care must be taken to ensure that all the facts relating to the transaction are submitted.

.01 *Information regarding the corporation that is redeeming its stock (Corporation).*

1 Identification.—Name, taxpayer identification number, and place and date of incorporation of Corporation.

2 Jurisdiction.—Identify the District Office that will have audit jurisdiction over the return of Corporation (referred to below as "taxpayer"). State whether, to the best knowledge of the taxpayer and the taxpayer's representatives, if any, the identical issue is in a return of the taxpayer (or of a related taxpayer within the meaning of section 267 of the Code, or a member of an affiliated group of which the taxpayer is also a member within the meaning of section 1504) and, if so, whether the issue (1) is being examined by a District Director, (2) has been examined by a District Director and (a) the statutory period of limitation either on assessment or for filing a claim for refund or credit of tax has not expired and (b) a closing agreement covering the issue or liability has not been entered into by a District Dirctor, (3) is being considered by an Appeals Office in connection with the taxpayer's return for an earlier period, (4) has been considered by an Appeals Office and (a) the statutory period of limitation either on assessment or for filing a claim for refund or credit of tax has not expired and (b) a closing agreement covering the issue or liability has not been entered into by an Appeals Office, or (5) is pending in litigation in a case involving the taxpayer or a related taxpayer. The request must contain a statement whether, to the best knowledge of the taxpayer and the taxpayer's representatives, the identical or a similar issue has been (i) submitted to the Service, but withdrawn before a ruling was issued, or (ii) ruled on by the Service to the taxpayer or the taxpayer's predecessor and, if so, when and with what result. If, after the request is filed but before a ruling is issued, the taxpayer knows that an examination of the issue by a District Director has been started, the taxpayer must notify the National Office of this action. If a return is filed before a ruling is received from the National Office concerning the issue that is the subject of the request for ruling, a copy of the request must be attached to the return. This alerts the District Office and avoids premature District action on the issue.

3. Business.—Provide the following information about Corporation: (i) a brief description of its businesses, (ii) its method of acounting, and (iii) its tax year.

.02 *Description of Corporation's capital structure and ownership of Corporation's stock.*

1 Description of capital structure.

(a) In general.—Furnish a complete description of each class of Corporation's outstanding stock (throughout this document the word "stock" includes all forms of equity ownership), setting forth the rights and privileges of each class, including voting or nonvoting rights, dividend and liquidation preferences or limitations, and whether classified as common or preferred stock. Also describe all other outstanding interests (bonds, debentures, notes, warrants, options, etc.), and briefly explain why each of these items should or should not be considered a stock interest. If Corporation has no outstanding interests convertible into stock, submit the following **REPRESENTATION:** *There are no outstanding options or warrants to purchase Corporation stock, nor are there any outstanding debentures or other obligations that are convertible into Corporation stock or would be considered Corporation stock.* Applying the constructive ownership rules of section 318(a) of the Code, state the relationship between the shareholders and the creditors of Corporation. In addition, describe any new debt or equity that Corporation anticipates issuing.

(b) Distribution of obligations of Corporation.—If applicable, submit the following **REPRESENTATION:** *No notes or other obligations of Corporation will be distributed to a redeemed shareholder.* Alternatively, if notes or other obligations of Corporation will be distributed to a shareholder whose stock is being redeemed (a Redeemed Shareholder), furnish the following:

(1) Copy.—Provide a copy or prototype of the instrument that sets forth its terms and limitations.

(2) Period of payments.—Give the beginning and ending payment dates. Submit the following **REPRESENTATION:** *In no event will the last payment on any note or other obligation be made more than 15 years after the date of issuance of the note or other obligation.* See section 4.0112 of Rev. Proc. 86-3.

(3) Payment of fixed amount.—State whether the amount to be paid, including interest, is a fixed amount payable at a fixed time, and whether the amount or the time of payment is subject to any change or adjustment. Submit the following **REPRESENTATION:** *None of the consideration from Corporation, including interest, consists entirely or partly of corporation's promise to pay an amount that is based on, or contingent on, future earnings of Corporation, an amount that is contingent on working capital being maintained at a certain level, or any other similar contingency.* See section 3.0117 of Rev. Proc. 86-3. Alternatively, furnish any

payments' terms and reasons why the right to the payments should not be considered an equity interest in Corporation.

(4) Financial statements.—Submit profit and loss statements and balance sheets for the latest 3 years.

(5) Subordination.—Submit the following REPRESENTATION: *Any note or other obligation to be issued to a redeemed shareholder will not be subordinated to the claims of general creditors of Corporation.*

(6) Default.—Submit the following REPRESENTATION: *In the event of default on any note or other obligation, no shares of stock will revert to or be received by a redeemed shareholder nor will any redeemed shareholder be permitted to purchase the stock at public or private sale.* See Section 3.0116 of Rev. Proc. 86-3.

2 Ownership of stock before the redemption.

(a) Shares owned directly.—State the total number of shares outstanding for each class of stock in Corporation immediately before the redemption. Also state the number of shares and percentage of each class of stock owned directly by each shareholder immediately before the redemption. However, if there are more than 25 shareholders, the statement in the preceding sentence may be limited to Redeemed Shareholders and those shareholders whose stock is attributed to them under section 318(a) of the Code.

(b) Shares constructively owned.—State the number of shares and percentage of each class of stock constructively owned by each Redeemed Shareholder, and the relationship under section 318(a) of the Code of any person or entity whose stock is attributed to a Redeemed Shareholder. In determining stock constructively owned by each Redeemed Shareholder under section 318(a), ownership may be attributed any number of times from one individual or entity to another, as provided in section 318(a)(5)(A). However, observe the exception in section 318(a)(5)(B) with respect to double attribution among members of the family (under section 318(a)(1)) and the exception in section 318(a)(5)(C) with respect to "sidewise" attribution to (under section 318(a)(3)) and from (under section 318(a)(2)) a partnership, estate, trust, or corporation.

Also, observe the following exceptions to constructive ownership: (i) to (under section 318(a)(3) of the Code) and from (under section 318(a)(2)) an employees' trust described in section 401(a) that is exempt from tax under section 501(a); and (ii) to a trust (under section 318(a)(3)) if the beneficiary's interest is a remote contingent interest. If it is contended that a trust is an employees' trust or that a beneficiary's interest is a remote contingent interest, submit information to support the contention.

In addition, observe that pursuant to section 318(a)(5)(E) of the Code, an S corporation is treated as a partnership and each of its shareholders as partners of the partnership for purposes of section 318(a). But note the limitation for purposes of constructive ownership provided by section 318(a)(5)(E).

(1) Section 318(a)(1) of the Code: family attribution.—If the Redeemed Shareholder is an individual, indicate the number of shares and percentage of each class of stock of Corporation owned actually and constructively under section 318(a) by members of the Redeemed Shareholder's family described in section 318(a)(1).

(2) Section 318(a)(2) of the Code: attribution from a partnership, estate trust, or corporation.—Indicate the number of shares and percentage of each class of stock of Corporation owned actually and constructively under section 318(a) by any partnership, estate, trust, or corporation in which the Redeemed Shareholder has an interest and the interest of the Redeemed Shareholder in each of these entitles.

(3) Section 318(a)(3) of the Code: attribution to a partnership, estate, trust, or corporation.—Indicate the number of shares and percentage of each class of stock of Corporation owned actually and constructively under section 318(a) as follows: (i) by any of the partners if the Redeemed Shareholder is a partnership; or (ii) by any of the beneficiaries if the Redeemed Shareholder is a trust or estate; or (iii) by any of the shareholders owning actually or constructively, under section 318(a), 50 percent or more in value of the stock of the Redeemed Shareholder, if the Redeemed Shareholder is a corporation.

(4) Section 318(a)(4) of the Code: options to acquire stock of Corporation.—Identify all holders of any rights or options (including those in the form of convertible debentures and stock rights or warrants) to acquire stock of Corporation and the relationship, direct or indirect under section 318(a), of the option holders to each of the Redeemed Shareholders.

(c) Percent of stock owned.—Indicate the total percentage of each class of stock of Corporation owned actually and constructively, as determined in section 5.022(a) and (b) above, by each shareholder of Corporation immediately before the redemption.

3 Stock to be redeemed.—State the number of shares of each class of stock to be redeemed from each shareholder of Corporation listed in section 5.022(a) above. Unless the stock is traded on an established securities market, also state when, from whom, and for what consideration each Redeemed Shareholder received the equity interest being redeemed.

4 Ownership of stock after the redemption.—Indicate the number of shares of each class of stock of Corporation owned actually and constructively by each shareholder, the total outstanding, and the percentage of each class of stock owned actually and constructively by each Redeemed Shareholder immediately after the redemption, determined in the same manner and including the same information as required in section 5.022 above.

.03 *Other relationships or transactions.*—Information showing the complete factual background relating to the redemption of each Redeemed Shareholder.

1 Other relationships between Corporation and any Redeemed Shareholder.—With regard to each Redeemed Shareholder, state whether the shareholder was, or will be, an employee of, an officer of, or in any way related to, Corporation. Describe fully all business and debtor-creditor relationships between each Redeemed Shareholder and Corporation. Describe all direct and indirect payments by Corporation to, or for the benefit of, each Redeemed Shareholder. (See e.g., Rev. Rul. 77-467, 1977-2 C.B. 92 and section 3.0118 of Rev. Proc. 86-3.) Give details of any agreements between a Redeemed Shareholder and Corporation, such as an employment contract, covenant not to compete, insurance,

pensions, deferred compensation, or other benefits, and state whether the agreements, payments, or benefits had an affect upon the amount of property to be distributed in the redemption. Describe any property a Redeemed Shareholder will transfer or surrender in the transaction other than stock of Corporation, and the consideration to be received in exchange therefor. State whether any part of the consideration from Corporation will be received by a Redeemed Shareholder, directly or indirectly, as a creditor, employee, or in some capacity other than as a Redeemed Shareholder. Describe whether the Redeemed Shareholder conducts or will conduct any business with, or leases or will lease any property to, Corporation.

2 Agreements between shareholders.—Submit the following REPRESENTATION: *No shareholder of Corporation has been or will be obligated to purchase any of the stock to be redeemed.* Alternatively, if there are, or within the 3-year period prior to the transaction have been, any agreements between a Redeemed Shareholder and other shareholders as to the acquisition or disposition of any equity interest, such as buy-sell agreements or options, describe the agreements or options in full. Submit copies of all pertinent agreements. See Rev. Rul. 69-608, 1969-2 C.B. 43.

3 Other transactions.—Submit the following REPRESENTATION: *The redemption described in this ruling request is an isolated transaction and is not related to any other past or future transaction.* Alternatively, state whether there have been, or will be, any related transactions, and, if so, briefly describe these other transactions and fully explain their relationship to, and impact on, the present transaction. See section 9.06 of Rev. Proc. 86-1.

(a) Transactions involving Corporation.—If there have been no changes in Corporation's outstanding equity in the past 5 years, submit the following REPRESENTATION: *There have been no redemptions, issuances, or exchanges by Corporation of its stock in the past 5 years.* Alternatively, describe all changes in Corporation's outstanding equity during this period, including every redemption, issuance, or exchange of stock by Corporation. State whether any of the shareholders involved in any of these prior transactions are Redeemed Shareholders, or related within the meaning of section 318 of the Code to a Redeemed Shareholder, in the present transaction.

If no future transactions are planned or intended, submit the following REPRESENTATION: *Corporation has no plan or intention to issue, redeem, or exchange additional shares of its stock.* Alternatively, if any issuances, redemptions, or exchanges are planned, describe the transaction, the number and type of shares, and the consideration to be paid or received in exchange for the stock, and state whether any of the shareholders involved in any future transaction are Redeemed Shareholders, or related within the meaning of section 318 of the Code to a Redeemed Shareholder, in the present transaction.

(b) Transactions involving any related corporation.—State whether there were, or will be, any distributions, redemptions, or issuances of stock of any related corporation, and if so, briefly describe the transactions and fully explain their relationship to the present transaction.

(c) Transactions involving any Redeemed Shareholder.—State whether any Redeemed Shareholder or a related party has sold or acquired, or intends to sell or acquire, any stock in Corporation or any related corporation either directly or constructively within five years of the redemption. If so, state the number of shares of each class, identify the parties to the transaction, the relationship of the parties and their relationship to any Redeemed Shareholder within the meaning of section 318(a) of the Code, and the consideration to be received in exchange therefor. State whether the sale or disposition of the stock has been considered consummated in computing the ownership of stock before and after the redemption in section 5.022 and 4 above. State whether Corporation will be liable, directly or indirectly, for any part of the buyer's obligation in the purchase of stock. See Rev. Rul. 69-608, *supra.*

4 In general.—Describe any relationship or transaction between Corporation and any Redeemed Shareholder, and describe any transaction by either Corporation or any Redeemed Shareholder, if the relationship or transaction affects the Redeemed Shareholder's percentage ownership of any class of Corporation's stock, regardless of whether the transaction or relationship is past, contemplated, or not considered related to the redemption.

.04 *Information to determine whether the redemption is an exchange or dividend.*

1 Termination of shareholder's interest.

(a) Complete termination of shareholder's stock interest.—

Submit the following REPRESENTATION: *None of the redeemed shareholders are related, within the meaning of section 318 of the Code, to any remaining shareholders of Corporation.*

(b) Termination of shareholder's interest except for constructive ownership under section 318(a)(1) of the Code.—If it is contended there has been a complete termination of a Redeemed Shareholder's interest except for constructive ownership from a family member under section 318(a)(1) so that section 302(b)(3) should apply pursuant to the application of section 302(c)(2), furnish the following with respect to the Redeemed Shareholders:

(1) Identity of the Redeemed Shareholders.

(2) Acquisitions or dispositions of stock of Corporation within the last 10 years by the Redeemed Shareholders. Do not include a change in interest resulting from partition of community property. See Rev. Rul. 82-129, 1982-2 C.B. 76.

(A) Acquisitions by Redeemed Shareholder within the last 10 years.—Submit the following REPRESENTATION: *None of the stock to be redeemed was acquired by the redeemed shareholder within the 10-year period preceding the redemption from a person whose stock would be attributed under section 318(a) of the Code to the redeemed shareholder at the time of redemption.* (Alternatively, see (C) below.)

(B) Dispositions by Redeemed Shareholder within the last 10 years.—Submit the following REPRESENTATION: *No person whose stock would be attributed to the redeemed shareholder under section 318(a) of the Code will own stock of Corporation after the redemption if the stock was acquired by that person from the redeemed shareholder within 10 years preceding the redemption.*

(Alternatively, see (C) below.)

(C) Avoidance of federal income tax.—If the representation in either (A) or (B) immediately above cannot be furnished because of an acquisition or disposition described therein, but it is contended that the acquisition or disposition did not have as one of its principal purposes the avoidance of federal income tax, give a full description of the acquisition or disposition and furnish an analysis of both the facts and supporting relevant authority for the contention. See section 3.0119 of Rev. Proc. 86-3.

(3) Interest in Corporation after the redemption.

(A) No interests other than creditor and constructive owner under section 318(a)(1) of the Code.—Describe whether Corporation will provide any compensation or economic benefit to any Redeemed Shareholder (regardless of whether the compensation or benefit is related to prior services) including termination bonuses, payments under covenants not to compete, free insurance, and future employment of any type whether directly as an officer or employee or indirectly as an independent contractor or consultant. Submit the following REPRESENTATION: *After the redemption, no redeemed shareholder will have any interest in Corporation, including an interest as officer, director, or employee (other than an interest as a creditor as described in section 1.302-4(d) of the Income Tax Regulations, and constructive ownership under section 318(a)(1) of the Code).* See Rev. Ruls. 84-135, 1984-2 C.B. 80, 81-233, 1981-2 C.B. 83, and 71-426, 1971-2 C.B. 173.

(B) Agreement as to future interests.—When attribution under section 318(a)(1) of the Code is to be waived pursuant to section 302(c)(2)(A), submit the following REPRESENTATION: *Each redeemed shareholder will execute and file the agreement required by section 302(c)(2)(A)(iii) of the Code with respect to the acquisition of any interest in Corporation within 10 years from the date of the redemption.*

(C) Termination of entity-shareholder's interest except for constructive ownership under section 318(a)(1) of the Code.—If a partnership, estate, trust, or corporation is a Redeemed Shareholder and stock is attributed to it under section 318(a)(3) of the Code from a "related person" (defined in section 302(c)(2)(C)(ii)), submit: (i) the name and relationship to the entity of each related person; (ii) the representations in section 5.041(b)(2)(A) for each Redeemed Shareholder and in section 5.041(b)(2)(B) for each Redeemed Shareholder and each related person (or the information in section 5.041(b)(2)(C)); (iii) the information and representations required by section 5.041(b)(3)(A) and (B) for each Redeemed Shareholder and each related person; and (iv) the following REPRESENTATION: *The Redeemed Shareholder and each related person will agree to be jointly and severally liable for any deficiency (including interest and additional tax) resulting from an acquisition of an interest in Corporation within 10 years from the date of the redemption.*

2 Substantially disproportionate redemption.—If it is contended the redemption is substantially disproportionate to one or more of the Redeemed Shareholders, furnish the information required in section 302(b)(2) of the Code with respect to each of those shareholders.

(a) Fifty-percent rule.—State the percent of the total combined voting power of all classes of stock entitled to vote owned actually and constructively by each Redeemed Shareholder (as determined in section 5.024 above) immediately after the redemption.

(b) Eighty-percent rule.—Submit computations to show that each Redeemed Shareholder owns actually and constructively immediately after the redemption (as determined under section 5.024 above) less than 80 percent of the percentage of the outstanding common stock (voting and nonvoting) owned immediately before the redemption, in accordance with the requirements in section 302(b)(2)(C) of the Code. If a Redeemed Shareholder holds no common stock, either directly or constructively, no computation for common stock is required (see Rev. Rul. 81-41, 1981-1 C.B. 121).

3 Redemption not essentially equivalent to a dividend.—If the redemption does not qualify as a partial liquidation under section 302(b)(4) of the Code, as an exchange under section 303, or under section 302(b)(2) or (3), and it is contended "the redemption is not essentially equivalent to a dividend" within the meaning of section 302(b)(1), submit whatever facts and analysis of supporting authority are relevant with respect to each Redeemed Shareholder (which have not been furnished above) to support this contention. Supply information to show that each Redeemed Shareholder will have a meaningful reduction in proportionate interest in vote, dividend rights, and right to receive assets on liquidation with regard to Corporation. See *United States v. Davis*, 397 U.S. 301 (1969), Ct. D. 1937, 1970-1 C.B. 62, section 1.302-2 of the regulations, and Rev. Rul. 81-289, 1981-2 C.B. 82.

4 Other information to determine whether the redemption is an exchange, a dividend, or other ordinary income transaction to the Redeemed Shareholder or any other person.

(a) "Section 306 stock".—If it is contended that none of the stock to be redeemed is "section 306 stock" within the meaning of section 306(c) of the Code, submit the following REPRESENTATION: *None of the stock to be redeemed is "section 306 stock" within the meaning of section 306(c) of the Code.* If the stock to be redeemed is common stock, state whether it was received in exchange for preferred stock. If the stock to be redeemed is preferred stock, furnish the following information:

(1) Issued for cash.—If issued for cash, furnish a statement to that effect and state whether the stock was paid for in full.

(2) Issued upon incorporation.—If the stock was issued upon incorporation in exchange for property, furnish a statement to that effect. (See section 306(c)(3) and (4) of the Code.)

(3) Issued under other circumstances.

(A) When issued.—Give the date or dates on which the stock was issued.

(B) Transaction.—Describe the transaction in which the stock was issued (whether a stock dividend, a reorganization, or other transaction).

(c) Consideration to Corporation.—Describe the kind of property, if any, Corporation received in exchange for the stock.

(b) Declared but unpaid dividends.—Submit the following REPRESENTATION: *There are no de-*

clared but unpaid dividends, or funds set apart for dividends, on any of the stock to be redeemed. (See Rev. Rul. 75-320, 1975-2 C.B. 105, and Rev. Rul. 69-130, 1969-1 C.B. 93.)

(c) Financing of redemption.—State the source of the cash or other property to be distributed in the redemption. If cash has been or will be borrowed for the redemption, give full particulars as to the parties to, and terms of, the loan agreement.

(d) Stock not to be cancelled, retired, or held as treasury stock.—If a party other than Corporation will hold the stock to be redeemed, give all facts concerning the arrangement and the conditions, if any, under which the stock may be returned to the Redeemed Shareholder or any person other than Corporation, and the relationship under section 318(a) of the Code of that person to the Redeemed Shareholder.

(e) Debt owed by Redeemed Shareholder to Corporation.—If a Redeemed Shareholder owes any amount to Corporation, state the circumstances under which the debt arose, the terms of the debt, and when and how it will be discharged.

(f) Redemption price and fair market value of the stock.—Submit the following REPRESENTATION:*At the time of the exchange, the fair market value of the consideration to be received by the redeemed shareholder will be approximately equal to the fair market value of Corporation's stock to be exchanged therefor.* Alternatively, if it will not be approximately equal, give a complete explanation, including the fair market value of both the stock redeemed and the assets distributed.

05 *Effect on Redeemed Shareholder when redemption is treated as an exchange.*

1 Loss to Redeemed Shareholder.—Submit the following REPRESENTATION: *The price to be paid for Corporation's stock to be redeemed will not result in a loss with respect to those shares of stock.* Alternatively, if any Redeemed Shareholder will realize a loss on the redemption, state reasons to establish why section 267 of the Code will not apply.

2 Installment method.—If a Redeemed Shareholder requests a ruling that the installment method under section 453 of the Code will apply to the redemption, furnish information to support the contention that the requirements in section 453(b) will be met with respect to the Redeemed Shareholder. Further, submit the following REPRESENTATION: *The redemption of Corporation stock (i) is not a disposition of personal property on the installment plan by a person who regularly sells or otherwise disposes of personal property on the installment plan and (ii) is not a disposition of personal property of a kind required to be included in the inventory of any redeemed shareholder at the close of the taxable year. Any note or other obligation to be issued to a redeemed shareholder will not be issued in any form designed to render it readily tradable on an established securities market.* See section 453(b), (f)(2), and (f)(5) of the Code.

06 *Property distributed in redemption of the stock.*—Describe in detail the property to be received by each Redeemed Shareholder.

1 United States cash.—Indicate the amount of United States cash (including cash equivalents within the meaning of Rev. Rul. 66-290, 1966-2 C.B. 112) to be distributed to each Redeemed Shareholder.

2 Property other than United States cash.

(a) Description.—Describe fully all types and categories of property, tangible and intangible, other than United States cash (including cash equivalents within the meaning of Rev. Rul. 66-290), to be distributed by Corporation to each Redeemed Shareholder.

(b) Recognition of gain or income to Corporation.—In order to determine whether gain or income will be recognized to Corporation upon the distribution of property, provide the following:

(1) Inventory (section 311(b)).—A statement whether any inventory will be distributed and, if distributed, whether Corporation is on the LIFO method of inventory.

(2) Liability in excess of basis (section 311(c)).—A statement as to the amount of any liabilities to be assumed by a Redeemed Shareholder, the amount of any liability to which the property distributed is subject, and the adjusted basis in the hands of Corporation of all property distributed.

(3) Appreciated property (section 311(d)).—A statement whether any appreciated property will be distributed by Corporation to a Redeemed Shareholder as part of the redemption. If so, state any exceptions or limitations which may be applicable to prevent recognition of gain to Corporation and give reasons for their applicability.

(4) Unreported and anticipatory assignment of income.—State whether Corporation will distribute to a Redeemed Shareholder any assets which represent earned but unreported income such as receivables being reported on a cash basis, unfinished construction contracts, commissions due, or other assets resulting in an anticipatory assignment of income.

(5) Installment obligations and recapture provisions.—State whether Corporation will distribute to a Redeemed Shareholder in the redemption (i) any installment obligations (section 453B of the Code), (ii) any property described in the recapture provisions of the Code including, but not limited to, sections 47, 291(a), 341(f), 617(d), 897(d), 904(f), 1245(a), 1248(f), 1250(c), 1252(a), 1254, or 1255, (iii) - any property for which the taxpayer obtained a deduction (See *Hillsboro National Bank v. Commissioner*, 460 U.S. 370 (1983); Rev. Rul. 74-396, 1974-2 C.B. 106; Rev. Rul. 61-214, 1961-2 C.B. 60), or (iv) any property described in sections 1256 or 1276.

(6) Reserve for bad debts.—A statement whether Corporation will distribute to a Redeemed Shareholder any receivables. If so, state the amount of any reserve for bad debts related to the receivables.

(7) Sale, lease, or other disposition of property.—State whether the Redeemed Shareholder will sell, lease, or otherwise dispose of any property received in the redemption, and give full particulars as to the circumstances and agreement with respect to the sale, lease, or other disposition. If property will be leased back to Corporation, submit a copy of the lease, and state whether: (i) the terms of the lease are the result of arm's-length negotiation; (ii) the payments to be made thereunder will be in an amount equal to the fair rental value of the property; (iii) the payments will be dependent on the future earnings of Corporation; and (iv) - the payments will be subordinated to the claims of general creditors. See Rev. Rul. 77-467, 1977-2 C.B. 92.

(8) Cross-redemption.—If the Redeemed Shareholder is a corporation and the property to be distributed by the Corporation is stock of the Redeemed Shareholder, submit a statement concerning treatment of the cross-redemption by each of the corporations, together with a statement of relevant authorities to support the treatment.

.07 *General*

1 Additional statements.—See Rev. Proc. 86-1 for additional information and statements that must be submitted with all ruling requests, including statements required under sections 9.02 and 9.09 (relating to instructions to taxpayers).

2 Requested rulings.—List the rulings being requested in the exact wording desired, and provide statutory, regulatory, or other authority for their issuance.

3 Taxpayer's memorandum.—Submit the information required by section 9.08 of Rev. Proc. 86-1 (relating to relevant authorities regarding the tax results of the transaction).

SEC. 6. INQUIRIES

Inquiries in regard to this revenue procedure should refer to its number and should be addressed to the Associate Chief Counsel (Technical), Attention: CC:C:R, Internal Revenue Service, Washington, D.C. 20224.

SEC. 7. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 81-62 is superseded.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Effective Dates and Other Issues Arising Under the Employee Benefit Provisions of The Tax Reform Act of 1984

EE-96-85

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary regulations relating to effective dates and certain other issues arising under the employee benefit provisions of the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1]. The text of those temporary regulations also serves as the comment document for this notice of proposed rulemaking.

DATES: Written comments and requests for a public hearing must be delivered or mailed by April 7, 1986. The regulations are proposed to be effective on varying dates provided in the temporary regulations.

ADDRESS: Send comments and request for a public hearing to Commissioner of Internal Revenue, Attn: CC:LR:T (EE-96-85), 1111 Constitution Avenue N.W., Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: John T. Ricotta of the Employee Plans and Exempt Organizations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington, D.C. 20224, Attention: CC:LR:T (EE-96-85), telephone: 202-566-3544 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

The temporary regulations provide guidance concerning the economic performance requirement for certain employee benefits under section 461(h) of the Internal Revenue Code of 1954 (Code), as added by section 91 of the Tax Reform Act of 1984 (Act) (P.L. 98-369, 98 Stat. 598); the transitional rule for vested accrued vacation pay under section 463 of the Code, as amended by section 91(i) of the Act (P.L. 98-369, 98 Stat. 609); the treatment of group-term life insurance purchased for employees under section 79 of the Code, as amended by section 223 of the Act (P.L. 98-369, 98 Stat. 775); the treatment of funded welfare benefit plans under sections 419 and 419A of the Code, as added by section 511 of the Act (P.L. 98-369, 98 Stat. 854); the treatment of unfunded deferred benefits under sections 404(b) and 162 of the Code, as amended by section 512 of the Act (P.L. 98-369, 98b Stat. 862); additional requirements for tax-exempt status of certain organizations under section 505 of the Code, as added by section 513 of the Act (P.L. 98-369, 98 Stat. 863); rollovers of partial distributions under sections 402 and 403 of the Code, as amended by section 522 of the Act (P.L. 98-369, 98 Stat. 868); distributions where substantially all contributions are employee contributions under section 72 of the Code, as amended by section 523 of the Act (P.L. 98-369, 98 Stat. 871); repeal of the estate tax exclusion for qualified plan benefits under section 2039 of the Code, as amended by section 525 of the Act (P.L. 98-369, 98 Stat. 873); determination of whether there is a collective bargaining agreement under section 7701(a)(46) of the Code, as added by section 526(c) of the Act (P.L. 98-369, 98 Stat. 881); nonrecognition of gain on stock sold to an employee stock ownership plan (ESOP) under section 1042 of the Code, as added by section 541 of the Act (P.L. 98-369, 98 Stat. 887); deductibility of dividends relating to ESOPs under sections 404 and 3405 of the Code, as amended by section 542 of the Act (P.L. 98-369, 98 Stat. 890); exclusion of interest on ESOP loans under section 133 of the Code, as added by section 543 of the Act (P.L. 98-369, 98 Stat. 894); treatment of an employer and an employee benefit association as related under section 1239 of the Code, as amended by section 557 of the Act (P.L. 98-369, 98 Stat. 898); and technical corrections to the pension provisions of the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462] under sections 713 and 715 of the Act (P.L. 98-369, 98 Stat. 955, 966). The proposed regulations are issued under the authority contained in section 7805 of the Code (26 U.S.C. §7805). For the text of the temporary regulations, see * * * [T.D. 8073, page 4, this Bulletin].

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. Although this document is a notice of proposed rulemaking which solicits public comment. the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before the adoption of these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the Federal Register. The collection of information requirements contained herein have been submitted to the Office of Management and Budget (OMB) for review under section 4504(h) of the Paperwork Reduction Act. Comments on the requirements should be sent to the Office of Information and Regulatory Affairs, of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests persons submitting comments to OMB also to send copies of the comments to the Service.

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on January 29, 1986, 4:06 p.m., and published in the issue of the Federal Register for February 4, 1986, 51 F.R. 4391)

Foundations Status of Certain Organizations

Announcement 86-39

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

Ann Mary Kelly Foundation for the Performing Arts, Sepulveda, CA
Bergen Passaic Chapter Howard University Alumni Association (New Jersey), Englewood, NJ
Bernard S. Jefferson Scholarship Fund, Long Beach, CA
Beverly Hills National Little League, Beverly Hills, CA
Biblical Research Center of Hawaii, The, Honolulu, HI
Bulldog Booster Inc., Burbank, CA
Calvary Community Consultants, Norwalk, CA
Charter Oak Gymnastics Booster Club, Covina, CA
Citizens Against Child Abuse, Portland, OR
Conservation and Renewable Energy, Inc., Anchorage, AK
Creative Kids Inc., San Diego, CA
Creative Youth Symphony, Portland, OR
Critical Mass Productions, Portland, OR
Data-Tech Institute, Nutley, NJ
Dystonia Foundation, San Bernardino, CA
East King Options, Bellevue, WA
Eastern Cumberland ALS c/o Hamden Ambulance Assn., Mechanicsburg, PA
Family Law Project, The, Los Angeles, CA
1st Cavalry Co. 1 Inc., Riverside, CA
Gospel Broadcasting Recording Service, Inc., Shelburne, VT
Health Services Foundation, Camden, NJ
Health Technologies Foundation, Camden, NJ
Institute of Dramatic Arts for Children, Altadena, CA
International Cross Cultural Alcohol Project, Nemana, AK
Kahala School Parent-Teacher Org., Honolulu, HI
Kotzebue Womens Crisis Project, Kotzebue, AK
L.A. Committee for the Georgetown University Spinal Cord Institute, Los Angeles, CA
MLR Productions, Inc., North Reading, MA
Mimesis Institute, Philadelphia, PA
Monmouth County Private Industry Council, Tinton, Falls, NJ
National Life Council, Inc., Wilmington, DE
National Right to Vote Committee, Media, PA
Newhall Education Foundation, Newhall, CA
Northeast Philadelphia String Band, Inc., Philadelphia, PA
Northwest Youth in Action Ministries, Inc., Philadelphia, PA
Old Landmark Day Care Center, Irvington, NJ
On The Outreach With Our God, Philadelphia, PA
1696 Thomas Massey House, Broomall, PA
Outreach Mission, Inc., Philadelphia, PA
P Tack, Ardmore, PA
Painters Local 1269 Apprentice Fund, Whitehall, PA
Partnership in Mission, Philadelphia, PA
Paulsboro Community Ambulance Association, Paulsboro, NJ
Performing Arts Network of New Jersey, The, Red Bank, NJ
Police Alcohol Recovery Team—P.A.R.T., Portland, OR
Pomona Neighborhood Center Inc., Pomona, CA
Portland Community Housing Resource Board, Portland, OR
Praise Repertory Co., Irvine, CA
Presbyterians for Lesbian/Gay Concerns, San Francisco, San Francisco, CA
Rancho Bernardo Pony Baseball Inc., San Diego, CA
Rancho Temecula Community Park Assoc., Temecula, CA
Reaching Out, Inc., Bristol, PA
Renaissance Inc. at Stonehedge, Tamaqua, PA
Roosevelt Senior Citizens Housing Corp., Roosevelt, NJ
San Diego County LaCrosse Organization, Escondido, CA
San Gabriel Valley Area Health Education Center, San Gabriel, CA
Sanctuary Community Center, Philadelphia, PA
Sand Point Broadcasting, Inc., Sandpoint, AK
Sarcoidosis Family Aid and Research Foundation, The, East Orange, NJ
Self-Help Groups for Anorexia & Bulimia, Pasadena, CA
Shippensburg Area Pool Association Inc., Shippensburg, PA
Sickle Cell Anemia Trust Fund, The, Philadelphia, PA
Sittos Foundation, Riverside, CA
Sivas Corporation, Philadelphia, PA
South Central Endowment Foundation, Inc., Bloomington, IN
South Eastern Pennsylvania Health Planning Organization, Philadelphia, PA
Starting Point, The, Trenton, NJ
Stuart L. Isler Foundation for Preventive Dentistry, Denville, NJ
Substance Abuse Rehabilitation Foundation, Klamath Falls, OR
Sullivan Scholarship Fund Trust, Wyoming, MI
Support Center—A Non-Profit Organization, Omak, WA
Sweetwater Rescue Association, Inc., Hammonton, NJ
Thats Fine Corporation, Inc., New Brunswick, NJ
Theatre for Youth and Community Awareness, Fort Lee, NJ
Theatre of Reviviscence, Inc., The, East Orange, NJ
Thomas E. Harrington Middle School Parent-Teacher Organization, Inc., Mount Laurel, NJ
3C's Association, Inc., Santa Fe Springs, CA
Thousand Oaks Professional Theatre and Conservatory, Thousand Oaks, CA
Tiger Historical Center, Inc., Ione, WA
Tim Sherman Ministries, Saugus, CA
Tri Community Maternity Center, Philadelphia, PA
Triad Ministries, Harrisburg, PA
Tri-County Big Brothers/Big Sisters,

Inc., Harrisburg, PA
Trinity Healthcare Services, Los Angeles, CA
Trojen Soccer Booster Club Inc., Irvine, CA
Understanding Incorporated, Palm Springs, CA
Unicorne Research Foundation, South Pasadena, CA
United Neighborhoods Security Assn., Los Angeles, CA
Valley Memorial Hospital Foundation, Sunnyside, WA
Van Nuys Civic Orchestra Assn., Van Nuys, CA
Victims For Victims, Los Angeles, CA
Victory Ministries, Wallingford, PA
Vietnam Memorial Foundation Inc., Philadelphia, PA
Vietnamese Service Center, Westminister, CA
Washington Square Fund, New York, NY
Watchung Hills Scholarship and Fellowship Association, Warren, NJ
Westmoor Gardens, Inc., Englewood, NJ
Westwood Literary Foundation, Los Angeles, CA
Whittington-Finch Housing Corp., Philadelphia, PA
Willamette World Affairs Council, Eugene, OR
Wilson Park Council for Youth and Community Development, The, Philadelphia, PA
Wings of Eagles Ministries, Pitman, NJ
Women for International Aid, Bogota, NJ
Zeta Nu Lambda Scholarship and Education Fund, Inc., Plainfield, NJ

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Correction of Error in Publication 572 Announcement 86-41

Publication 572, *Investment Credit*, (Rev. Nov. 85) contains an error in Example 4 in the third column on page 14. The years 1981, 1982 and 1983 in the second paragraph of that example should be 1980, 1981, and 1982, respectively.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Dal H. Felkel	Kingstree, SC	Certified Public Accountant	Indefinite from January 31, 1986
John J. Matonis	Walnut, CA	Attorney	Indefinite from January 24, 1986
Joel A. Shor	Baltimore, MD	Certified Public Accountant	Five Months from December 15, 1985
Patrick H. Diamond	New York, NY	Attorney & Certified Public Accountant	Indefinite from February 10, 1986
Folger P. Gifford	Cold Spring Harbor, NY	Certified Public Accountant	Indefinite from February 11, 1986
Robert Allen Beamer	Wauwatosa, WI	Attorney	Indefinite from February 19, 1986
Robert L. Cummings	Springfield, MO	Certified Public Accountant	Indefinite from February 27, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.103-10, amended.	Definition of "principal user"	1986-12 I.R.B. 19	Apr. 22, 1986
26 CFR 1.103-10, revised.	$40 million limitation on beneficiaries of certain tax-exempt bonds	1986-12 I.R.B. 22	Apr. 22, 1986

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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Highlights of this Issue

SPECIAL ANNOUNCEMENT

Announcement 86-42, page 13.
A public hearing will be held on April 29, 1986, on proposed regulations relating to the taxation of fringe benefits.

INCOME TAX

Rev. Rul. 86-50, page 9.
Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for April 1986.

Announcement 86-47, page 44.
The Service is considering whether the rules of subchapter L of the Code (and, in the case of life insurance companies, section 1.817-4(d) of the regulations) and/or the "tax benefit" rule require the taxation of income from the release of certain reserves when an election is made under section 338 of the Code to treat the purchase of stock of an insurance company as an asset acquisition.

EMPLOYEE PLANS

Rev. Rul. 86-47, page 4.
Funding; adjustments to funding standard account for spinoff of a plan. Guidance is provided for adjustments to the minimum funding requirements when a single plan, having assets greater in value than the present value of plan benefits on a termination basis, spins off assets and liabilities, and when one of the resultant spunoff plans has an unfunded accrued liability and the other does not. Rev. Rul. 81-212 amplified.

Rev. Rul. 86-48, page 6.
Spinoff; transfer; benefits on a termination basis. A defined benefit plan may fail to satisfy the spinoff requirements under section 414(l) of the Code if plan benefits included under section 411(d)(6)(B) or required under section 417(c) are not included in the determination of "benefits on a termination basis" within the meaning of section 1.414(l)-1(b)(5) and (n)(1) of the regulations.

Rev. Rul. 86-51, page 4.
Integrated pension plan; joint employers; compensation. An integrated pension plan will not automatically fail to qualify under section 401(a) of the Code because all compensation received by each employee from the employers who jointly maintain the plan is considered as total compensation for the purposes of determining excess contributions and plan benefits. Rev. Rul. 55-276 superseded.

Announcement 86-43, page 13.
In accordance with Section 12 of Rev. Proc. 84-23, set forth is a list of master and prototype plans closed or disposed of by the National Office of the Internal Revenue Service between October 1, 1985, and December 31, 1985, and a list of plans erroneously omitted from Announcement 85-99.

EXEMPT ORGANIZATIONS

Rev. Rul. 86-49, page 7.
Qualification; organization for historic preservation. An organization formed for the purpose of preserving the historic or architectural character of a community through the acquisition and occasional restoration of historically or architecturally significant properties, subject to restrictive covenants and subsequent disposition of these properties qualifies for exemption under section 501(c)(3) of the Code.

ADMINISTRATIVE

Rev. Proc. 86-19, page 10.
Automatic data processing systems; guidelines. The basic requirements that the Service considers to be essential in cases where a taxpayer's records are maintained within an Automatic Data Processing System are specified. References to the Automatic Data Processing System include all accounting and/or financial systems that process all or part of a taxpayer's transactions, records, or data by other than manual records. Rev. Procs. 64-12 and 80-42 superseded.

Announcement 86-44, page 41.
New Form 8404, Computation of Interest Charge on DISC-Related Deferred Tax Liability, is now available at most Service offices.

Finding Lists begin on page 48.
Announcement of Suspensions on page 45.
Announcement of Notice of Proposed Rulemaking on page 46.
Quarterly Index for January, February, and March begins on page 50.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 401.—Qualified Pension, Profit-Sharing, and Stock Bonus Plans

26 CFR 1.401-1: Qualified pension, profit-sharing, and stock bonus plans.
(Also Section 414; 11.414(c)-1.)

Integrated pension plan; joint employers; compensation. An integrated pension plan will not automatically fail to qualify under section 401(a) of the Code because all compensation received by each employee from the employers who jointly maintain the plan is considered as total compensation for the purposes of determining excess contributions and plan benefits. Rev. Rul. 55-276 superseded.

Rev. Rul. 86-51

PURPOSE

The purpose of this revenue ruling is to restate the position in Rev. Rul. 55-276, 1955-1 C.B. 401, under current law.

ISSUE

The issue in Rev. Rul. 55-276 is whether an integrated retirement plan maintained jointly by more than one employer will fail to qualify under section 401(a) of the Internal Revenue Code if all compensation received by each employee from one or more of the participating employers is considered as the total compensation for the purpose of determining excess compensation and the benefits under the plan.

FACTS

The *X*, *Y*, and *Z* corporations jointly maintain a single retirement plan that is not a collectively bargained plan. The plan provides for an annual retirement benefit of 30 percent of annual compensation in excess of $7,200. Annual compensation includes compensation paid from *X*, *Y*, and *Z* corporations. Thus, for example, employee *A*, who is employed by all three corporations, receiving an annual salary of $6,000 from *X* corporation, $4,000 from *Y* corporation, and $2,000 from *Z* corporation is entitled to a benefit based on $4,800 of excess compensation ($12,000 minus $7,200). The *X*, *Y*, and *Z* corporations are not affiliated and are not considered as a single employer under section 414(b), (c), or (m) of the Code.

LAW AND ANALYSIS

Section 401(a)(4) of the Code provides that a plan will not qualify unless the contributions or the benefits provided under the plan do not discriminate in favor of employees who are officers, shareholders, or highly compensated.

Section 1.401-1(d) of the Income Tax Regulations provides that a plan maintained by several employers will qualify if all the qualification requirements are otherwise satisfied.

In this case, benefits are provided to the employees whose total compensation exceeds the applicable integration level of $7,200. The amount of compensation received by *A* from a single employer is less than the plan's applicable integration level. Therefore, such employee would accrue no benefit if the plan were maintained by any single employer. Because the plan's provisions take compensation received from all jointly participating employers into consideration as the employee's total compensation, such employee is eligible for benefits.

Similarly, an employee whose compensation from each employer exceeds $7,200 receives a greater benefit from each employer under the jointly maintained plan since the total compensation is reduced only once by the $7,200 integration level and not once by each employer.

Basing integrated plan benefits on amounts in addition to compensation received from an individual employer does not necessarily cause discrimination in favor of officers, shareholders, or highly compensated employees. However, in testing whether a multiple employer plan, such as the plan maintained by *X*, *Y*, and *Z*, satisfies section 401(a)(4), the contributions or benefits provided by each employer are examined separately. In undertaking this examination with respect to an employer, only the compensation from that employer will be taken into account. Thus, for example, if only a few of a particular employer's rank-and-file employees are employed by more than one of the participating employers, the use of total compensation paid by all participating employers to employees who are officers, shareholders, or highly compensated may, in operation, result in discrimination prohibited under section 401(a)(4) of the Code.

HOLDING

In the case, the plan will not fail to qualify under section 401(a) of the Code merely because all compensation received by each employee from the unaffiliated employers that jointly maintain the plan is considered as the total compensation for the purpose of determining excess compensation and the benefits under the plan. However, the basis under which plan benefits are provided may in operation result in failure to satisfy section 401(a)(4).

The principles described above also apply for purposes of testing discrimination under section 410(b) of the Code.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 55-276 is superseded.

Section 411.—Minimum Vesting Standards

26 CFR 1.411(d)-3: Other special rules.

Whether plan benefits that are (a) included in participants' acrued benefits under section 411(d)(6)(B) of the Code or (b) required under sections 401(a)(11)(A)(ii) and 417(c) must be included in the determination of "benefits on a termination basis" within the meaning of section 1.414(1)-1(b)(5) and (n)(1) of the regulations. See Rev. Rul. 86-48, page 6.

Section 412.—Minimum Funding Standards

(Also Section 414; 26 CFR 1.414(1)-1.)

Funding; adjustments to funding standard account for spinoff of a plan. Guidance is provided for adjustments to the minimum funding requirements when a single plan, having assets greater in value than the present value of plan benefits on a termination basis, spins off assets and liabilities, and when one of the resultant spunoff plans has an unfunded accrued liability and the other does not. Rev. Rul. 81-212 amplified.

Rev. Rul. 86-47

ISSUES

In the case of a spinoff of a defined benefit plan having plan assets with a fair market value in excess of the present value of all plan benefits on a termination basis (within the meaning of section 1.414(l)-1 of the Income Tax Regulations) into two separate defined benefit plans:

(1) How is the credit balance in the funding standard account (FSA) of the plan prior to the spinoff allocated to the resultant spunoff plans?

(2) How are the amortization bases of the FSA of the plan prior to the spinoff allocated to the resultant spunoff plans?

FACTS

Prior to January 1, 1983, W was a defined benefit pension plan for which costs were computed using the entry age normal funding method. As of January 1, 1983, the beginning of the calendar plan year, W was spun-off into two defined benefit plans, X and Y. The assets of W were allocated between X and Y by a method not inconsistent with section 1.414(l)-1 of the regulations. The spinoff did not satisfy the de minimis rule in section 1.414(l)-1(n)(2). The allocations were made as described below:

	Plan W	Plan X	Plan Y
FSA credit balance	$ 20,000		
Market value of assets	400,000	$ 80,000	$320,000
Actuarial value of assets	375,000		
Present value of plan benefits on a termination basis for Code section 414(l)	180,000	58,000	122,000
Entry age normal accrued liability	425,000	200,000	225,000
Outstanding balance and remaining period of amortization bases			
Base A (28 payments remaining)	100,000		
Base B (14 payments remaining)	(30,000)		

LAW, ANALYSIS AND HOLDINGS

Issue 1:

When a defined benefit plan subject to the minimum funding standards undergoes a spinoff, each of the resulting plans must begin maintaining a separate FSA. The credit of debit balance of the single plan prior to the spinoff must be allocated to the FSAs of the spunoff plans on a reasonable basis, taking into account the assets and liabilities allocated between the plans in accordance with section 1.414(l)-1 of the regulations. Thus, the sum of the credit balances of each of the spunoff plans must equal the credit balance of the plan immediately prior to the spinoff.

Rev. Rul. 81-212, 1981-2 C.B. 99, provides a satisfactory method of allocating the credit balance between two plans that resulted from the spinoff of a single plan. However, that revenue ruling considers only the situation where the fair market value of plan assets is not greater than the present value of plan benefits on a termination basis. In such case, the allocation of any credit balance between the two plans is uniquely determined in that there can be but one possible result. As specified in Rev. Rul. 81-212, the credit balance of the single plan before the spinoff should be allocated between the spunoff plans under the asset allocation rules of section 1.414(l)-1(n) of the regulations with the credit balance considered to be the last portion of the assets allocated. This revenue ruling, following the principles of Rev. Rul. 81-212, provides in the case of a spinoff of an overfunded plan, a uniquely determined allocation of acredit balance with respect to any given spinoff.

In the case where, immediately prior to the spinoff, the fair market value of plan assets is greater than the present value of plan benefits on a termination basis, the credit balance of the single defined benefit plan (W) immediately before the spinoff should be allocated between the two plans (X and Y) resulting from the spinoff in the following manner:

(a) Allocate an amount equal to the lesser of (i) the excess of the fair market value of W's assets over W's FSA credit balance, or (ii) the present value of W's plan benefits on a termination basis, between X and Y in accordance with the asset allocation rules in section 1.414(l)-1(n) of the regulations.

(b) Allocate the credit balance of W between X and Y in proportion to the excess, for each plan, of the fair market value of assets actually allocated to each spunoff plan over the amount determined for each plan in step (a).

In the situation presented in this revenue ruling, the fair market value of W's assets minus W's FSA credit balance is greater than the present value of W's plan benefits on a termination basis. Therefore, the amount to be allocated in step (a) between X and Y is equal to the present value of W's plan benefits on a termination basis (i.e., $180,000). The required allocation in step (a) of such $180,000 using the rules of section 1.414(l)-1(n) of the regulations is $58,000 to X and $122,000 to Y. The excess of the fair market value of W's assets over the present value of W's plan benefits on a termination basis is $220,000. The excess of the fair market value of assets actually allocated to X ($80,000) over the amount allocated to X under step (a) ($58,000) is $22,000. The corresponding excess for Y is $198,000 (i.e., $320,000 minus $122,000). Under step (b), W's credit balance ($20,000) is allocated between X and Y in proportion to such excess amounts. Thus, a credit balance of $2,000 ($20,000 times the ratio of $22,000 to $220,000) is allocated to X. The credit balance allocated to Y is $18,000 ($20,000 times the ratio of $198,000 to $220,000).

Issue 2:

The allocation of W's amortization bases between X and Y must reasonably reflect the assets and liabilities of the two plans. Thus, the sum of the outstanding balances of W's amortization bases with a particular amortization period must equal the sum of the outstanding balances of the amortization bases with the same amortization period allocated to X and Y.

Rev. Rul. 81-212 provides a satisfactory method of allocating the amortization bases of a single defined benefit plan between two plans that result from a spinoff. However, that revenue ruling considers only the situation where each spunoff plan has an unfunded accrued liability, i.e., where, for each spunoff plan, the accrued liability is greater than the actuarial value of assets. In such case, the outstanding portion of each amortization base of the single plan before the spinoff is allocated between the plans resulting from the spinoff in proportion to the excess, for each spunoff plan, of (i) the accrued liability of the spunoff plan over (ii) the actuarial value of assets of the spunoff plan decreased by the credit balance or increased by the funding definciency of such plan. Rev. Rul. 81-212 does not address the situation where one or both of the two spunoff plans do not have an unfunded accrued liability.

As stated in Rev. Rul. 81-212, the actuarial value of assets of W ($375,000) should be allocated between X and Y in proportion to the fair market value of assets allocated to the two plans. Therefore, the actuarial value of assets of X is $75,000 ($375,000 times the ratio of $80,000 to $400,000), and X's unfunded accrued liability is $125,000 ($200,000 minus $75,000). The actuarial value of assets of Y is $300,000 ($375,000 times the ratio of $320,000 to $400,000), and Y has no unfunded accrued liability ($300,000 is greater than Y's accrued liability of $225,000).

Because X has an unfunded accrued liability and Y has no unfunded accrued liability, all of W's amortization bases should be allocated to X, retaining the remaining amortization period of each base. In addition, a new amortization base must be established for X. The outstanding balance of the new base is (1) the unfunded accrued liability of X ($125,000), minus (2) the sum of the outstanding balances of all amortization bases (treating the outstanding balances of credit bases under section 412(b)(3)(B) of the Internal Revenue Code as negative numbers) allocated to X, plus (3) the $2,000 credit balance of X previously computed under Issue 1. The amortization period of the new base will be the greater of (a) the amortization period of the base that would result if all amortization bases in the FSA of X prior to the establishment of the new base were combined and offset in accordance with section 412(b)(4) of the Code, and (b) 15 years. (It is not necessary to combine and offset the bases of X. It is only necessary to determine the amortization period that would result from combining and offsetting the bases.)

The net sum of the outstanding balances of the bases in W's FSA allocated to X is $70,000 ($100,000 minus $30,000). Therefore, the outstanding balance of the new base established as a result of the spinoff is $57,000 ($125,000 − $70,000 + $2,000). If the two amortization bases of X prior to the establishment of the new base were offset, the resulting base would have an amortization period of 28 years. Thus, the amortization period of the new base is 28 years (i.e., the greater of 28 and 15 years).

For Y, the actuarial value of assets is greater than the accrued liability. No amortization bases of W are allocated to Y and none should be established as a result of the spinoff. Also, no amortization bases should be established in Y in subsequent years until the accrued liability of Y is greater than the actuarial value of assets.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 81-212 is amplified.

Section 414.—Definitions and Special Rules

26 CFR 11.414(c)-1: Commonly controlled trades or businesses.

Whether an integrated pension plan jointly maintained by employers who are not considered as a single employer under section 414(b), (c), or (m) of the Code will automatically fail to qualify under section 401(a) because all compensation received by each employee from the employers is considered as total compensation for the purpose of determining excess contributions and plan benefits. See Rev. Rul. 86-51, page 4.

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26 CFR 1.414(l)-1: Mergers and consolidations of plans or transfers of plan assets.
(Also Section 411; 1.411(d)-3.)

Spinoff; transfers; benefits on a termination basis. A defined benefit plan may fail to satisfy the spinoff requirements under section 414(1) of the Code if plan benefits included under section 411(d)(6)(B) or required under section 417(c) are not included in the determination of "benefits on a termination basis" within the meaning of section 1.414(1)-1(b)(5) and (n)(1) of the regulations.

Rev. Rul. 86-48

ISSUE

Must plan benefits that are (a) included in participants' accrued benefits under section 411(d)(6)(B) of the Internal Revenue Code or (b) required under sections 401(a)(11)(A)(ii) and 417(c) be included in the determination of "benefits on a termination basis" within the meaning of section 1.414(1)-1(b)(5) and (n)(1) of the Income Tax Regulations?

FACTS

An employer mantained a nonmultiemployer defined benefit plan qualified under section 401(a) of the Code which was spunoff into two defined benefit plans as described in section 1.414(1)-1(b)(4) of the regulations. However, the benefits on a termination basis in the plan immediately prior to the spinoff was determined without regard to the benefits of participants that are (a) early retirement benefits, retirement-type subsidies and optional forms of benefits included in participants' accrued benefits under section 411(d)(6)(B) or (b) qualified preretirement survivor annuities required under sections 401(a)(11)(A)(ii) and 417(c).

LAW AND ANALYSIS

Section 414(1) of the Code provides that a plan will not qualify under section 401, in the case of any transfer of assets or liabilities of such plan to any other plan, unless each participant in the plan would (if the plan then terminated) receive a benefit immediately after the transfer that is equal to or greater than the benefit the participant would have been entitled to receive immediately before the transfer (if the plan had then terminated).

Section 1.414(1)-1(n)(1) of the regulations provides that the spinoff of a defined benefit plan will satisfy the requirements of section 414(1) of the Code if all the accrued benefits of each participant are allocated to only one of the spunoff plans and the value of the assets allocated to each spunoff plan is not less than the present value of the "benefits on a termination basis" in the plan prior to the spinoff for all participants in that spunoff plan.

Section 1.414(l)-1(b)(5) of the regulations defines the term "benefits on a termination basis" as the benefits that would be provided exclusively by the plan assets pursuant to section 4044 of the Employee Retirement Income Security Act of 1974 (ERISA), Pub. L. 93-406, 1974-3 C.B. 1, and the regulations thereunder if the plan had terminated.

Sections 403(d), 4021, and 4044(a) of ERISA provide that in the case of the termination of a nonmultiemployer defined benefit plan, the assets of the plan must be allocated to participants and beneficiaries of the plan in a specified order of six different categories of benefits. The six categories of benefits include all of the participants' benefits under the plan, whether forfeitable or nonforfeitable.

Section 401(a)(2) of the Code and section 1.401-2 of the regulations provide that, upon termination of a defined benefit plan, both the fixed and contingent liabilities of the plan to employees and beneficiaries (i.e., the vested and nonvested benefits of participants and beneficiaries) must be satisfied before the employer may recover any assets of the plan. Rev. Rul. 85-6, 1985-1 C.B. 133, provides guidance on the determination of the liabilities that must be satisfied upon plan termination prior to such a reversion.

Section 411(d)(6)(A) of the Code provides that a plan qualified under section 401 may not be amended (other than exceptions not relevant here) to reduce the accrued benefit of any participant. Section 411(d)(6)(B)(i) provides that a plan amendment that has the effect of eliminating or reducing an early retirement benefit, retirement-type subsidy or optional form of benefit (including any qualified joint and survivor annuity benefit required under sections 401(a)(11)(A)(i) and 417(b)) with respect to benefits attributable to service before the amendment will be treated as reducing accrued benefits. Rev. Rul. 85-6 provides that a defined benefit plan will fail to satisfy the requirements under section 411(d)(6) upon plan termination unless an early retirement subsidy that was provided prior to plan termination is provided for participants who satisfy the pretermination subsidy requirements after the termination of the plan.

Sections 401(a)(11)(A)(ii) and 417(c) of the Code provide that a qualified preretirement survivor annuity must be provided to the surviving spouse of a vested participant who dies before the annuity starting date.

To satisfy the requirements of section 1.414(l)-1(a)(1) of the regulations where a nonmultiemployer defined benefit plan is spunoff, each participant's total benefits that continue after the spinoff must be allocated to one of the spunoff plans and the value of the assets allocated to each of the spunoff plans must not be less than the value of such total benefits under each plan that would be provided by plan assets in accordance with section 4044 of ERISA. A participant's total benefits in the categories under section 4044 include (a) early retirement benefits, retirement-type subsidies and optional forms of benefits, described under section 411(d)(6)(B) of the Code that are part of the accrued benefit under section 411(d)(6) and (b) qualified preretirement survivor annuity benefits required under section 401(a)(11)(A)(ii), in each case, without regard to whether the participant has satisfied all of the conditions for such benefit as of the spinoff. These same benefits also must be taken into account under section 401(a)(2) and section 1.401-2 in determining the liabilities that must be satisfied upon plan termiantion before the employer may recover any plan assets.

In this case, the total benefits of participants were not taken into account to determine "benefits on a termination basis" with respect to the spinoff. Thus, the spinoff may fail to satisfy the requirements of section 1.414(l)-1(n)(1) of the regulations and section 414(l) of the Code.

HOLDING

The plan benefits that are (a) included in participants' accrued benefits under section 411(d)(6)(B) of the Code or (b) required under section 401(a)(11)(A)(ii) and 417(c) must be included in the determination of "benefits on a termination basis" within the meaning of section 1.414(l)-1(b)(5) and (n)(1) of the regulations.

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26 CFR 1.414(l)-1: Mergers and consolidations of plans or transfers of plan assets.

Whether the minimum funding requirements of section 412 are affected by a spinoff of assets and liabilities pursuant to section 414(l). See Rev. Rul. 86-47, page 4.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates determined for purposes of section 1274(d) of the Code are set forth for the month of April 1986. See Rev. Rul. 86-50, page 9.

Section 483.—Interest on Certain Deferred Payments

Federal short-term, mid-term and long-term rates determined for purposes of section 1274(d) of the Code are set forth for the month of April 1986. See Rev. Rul. 86-50, page 9.

Section 501.—Exemption From Tax on Corporations, Certain Trusts, Etc.

26 CFR 1.501(c)(3)-1: Organizations organized and operated for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals.

Qualification; organization for historic preservation. An organization formed for the purpose of preserving the historic or architectural character of a community through the acquisition and occasional restoration of historically or architecturally significant properties, and subsequent disposition of these properties subject to restrictive covenants qualifies for exemption under section 501(c)(3) of the Code.

Rev. Rul. 86-49

ISSUE

Does an organization that is formed for the purpose of preserving the historic or architectural character of a community through the acquisition, occasional restoration of historically or architecturally significant properties, and subsequent disposition of those properties under the circumstances described below, qualify as an organization organized and operated exclusively for charitable or educational purposes under section 501(c)(3) of the Internal Revenue Code?

FACTS

The organization was formed exclusively for the purposes of preserving the historic and architectural character of its community through the acquisition, occasional restoration of historically or architecturally significant properties, and subsequent disposition of those properties subject to restrictive covenants. These covenants are designed exclusively to preserve the historical character or architectural significance of the properties and, through such activities, of educating the public on the importance of historic preservation. The organization is composed of interested members of the public and is governed by a representative group that includes community and preservation leaders, and prominent architects and historians.

The organization has set up a "revolving fund" to acquire and resell historically or architecturally significant properties. The fund may also be used to restore the historically or architecturally significant properties in some cases. The acquisitions and sales are made at fair market value on arm's length terms and any profits from sales are used to purchase other historically or architecturally significant properties or for other activities in keeping with the organization's tax exempt purposes. The organization sells the properties subject to restrictive covenants designed exclusively to preserve the historical character or architectural significance of the properties. These covenants generally restrict the use and enjoyment of the property by controlling its physical and/or visual aspects. The covenants are granted in perpetuity, bar any interior or exterior alterations without the consent of the organization, give the organization the right of first refusal in the event a purchaser should later desire to sell, and, in some cases, require restoration of the structure to its original appearance. Unlike covenants imposed by local associations of homeowners, these covenants preserve the designated properties in their historical state or character for the benefit of the public, rather than merely ensuring their conformity to locally imposed standards. since such covenants may decrease the value of the property, the organization may lose some money in its resale operations. Such losses, if any, would be considered by it as a cost of its program.

The buyers include private individuals. However, the organization will not resell property to the person who initially sold or contributed the property to the organization or any related person.

The acquired structures are generally visible from the public right of way. Where they are not so visible, the organization provides in the restrictive covenants that visual access to the property will be made available to the public on a regular basis and the terms of the restrictive covenants contain prescribed conditions for such access, under the requirements set forth in section 1.170A-14(d)(5)(iv) of the Income Tax Regulations.

In order to ensure that only historically or architecturally significant structures are acquired, the organization confines its acquisitions to structures that possess integrity of location, design, setting, materials, and workmanship and:

(1) are closely associated with significant events or developments in Amnerican history; or

(2) are closely associated with the lives of significant American historical figures; or,

(3) embody distinctive characteristics of a type, period, or method of construction, or that represent the works of a master, or that possess high artistic value; and are either:

(a) listed in the National Register of Historic Places; or,

(b) located in a registered historic district and are certified by the Secretary of the Interior as being of historic significance to the district.

A registered historic district is either any district listed in the National Register of Historic Places or any district that is designated under a statute of an appropirate State or local government that is certified by the Secretary of the Interior as containing criteria which will substantially achieve the purpose of preserving and rehabilitating buildings of historic significance to the district and that is certified by the Secretary of the Interior as meeting substantially all of the requirements for the listing of districts in the National Register.

LAW

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable or educational purposes.

Section 1.501(c)(3)-(d)(2) of the regulations states that the term "charitable" is used in its generally accepted legal sense, and includes the advancement of education, the erection or maintenance of public buildings, monuments, or works, and the promotion of social welfare by organizations designed to combat community deterioration.

Section 1.501(c)(3)-1(d)(3) of the regulations provides that the term "educational" includes the instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for charitable or educational purposes unless it serves a public rather than a private interest.

The Historic Preservation Act of 1966 (16 U.S.C. §§461, 470) provides that it is a national policy to preserve for public use historic sites, buildings, and objects of national significance for the inspiration and benefit of the people of the United States. The Act further states that the historical and cultural foundations of the nation should be preserved as a living part of our community life and development to give a sense of orientation to the American people.

Rev. Rul. 67-391, 1967-2 C.B. 190, holds that a nonprofit organization formed to develop and disseminate an urban land-use plan that is designed to improve the area, eliminate existing blight, and guard against future deterioration qualifies for exemption under section 501(c)(3) of the Code as being operated exclusively for educational and charitable purposes. The organization does not ordinarily engage in real estate transactions but does purchase and sell property of strategic value that is in danger of being exploited in a manner that might endanger the plan.

Rev. Rul. 75-470, 1975-2 C.B. 207, holds that a nonprofit organization formed to promote an appreciation of history through the acquisition, restoration, and preservation of homes, churches, and public buildings having special historical or architectural significance and to open the buildings for viewing by the general public qualifies for exemption under section 501(c)(3) of the Code as being organized and operated exclusively for educational and charitable purposes.

ANALYSIS

The purpose of the organization in this case is to educate and otherwise benefit the public by restoring and preserving historically or architecturally significant properties through the acquisition, occasional restoration, and disposition of such properties at fair market value on arm's length terms. The continued preservation of such properties after their sale by the organization is guaranteed by means of restrictive convenants that are reasonably suited to preserving the historic or architectural character of the structures and community involved.

The identification, restoration, and preservation of historically or architecturally significant properties serves to educate the public and operates to prevent community deterioration within the meaning of section 1.501(c)(3)-1(d)(2) of the regulations. Under such circumstances, historic and architectural preservation is a charitable purpose and activity within the meaning of section 501(c)(3) of the Code.

The organization's utilization of a revolving fund to facilitate the purchase and sale of properties is reasonably calculated to accomplish its charitable purposes. This method of historic and architectural preservation does not serve private interests within the meaning of section 1.501(c)(3)-1(d)(1)(ii) of the regulations because any private purchaser pays not less than fair market value for the property purchased, and purchases subject to appropriate restrictive covenants.

HOLDING

An organization that is formed for the purpose of preserving the historic or architectural character of a community through the acquisition and occasional restoration of historically or architecturally significant properties and subsequent disposition of those properties under the circumstances described above, qualifies as an organization organized and operated exclusively for charitable or educational purposes under section 501(c)(3) of the Code. Such an organization must also meet the other requirements of section 501(c)(3) in order to be exempt from federal income tax.

APPLICATION INSTRUCTIONS

Even though an organization considers itself within the scope of this revenue ruling, it must file an application on Form 1023. Application for Recognition of Exemption, in order to be recognized by the Service as exempt under section 501(c)(3) of the Code. See sections 1.501(a)-1 and 1.508-1(a) of the regulations. In accordance with the instructions to Form 1023, the application should be filed with the District Director of Internal Revenue for the key district indicated therein.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 468, 483, 7872.)

Rev. Rul. 86-50

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of April 1986 are as follows:

	Period of Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term				
AFR	7.60%	7.46%	7.39%	7.35%
110% AFR	8.38%	8.21%	8.13%	8.07%
120% AFR	9.15%	8.95%	8.85%	8.79%
Mid-Term				
AFR	8.08%	7.92%	7.84%	7.79%
110% AFR	8.90%	8.71%	8.62%	8.56%
120% AFR	9.73%	9.50%	9.39%	9.32%
Long-Term				
AFR	8.52%	8.35%	8.26%	8.21%
110% AFR	9.40%	9.19%	9.09%	9.02%
120% AFR	10.27%	10.02%	9.90%	9.82%

Section 6001.—Notice or Regulations Requiring Records, Statements, and Special Returns

26 CFR 1.6001-1: Records.

Guidance is provided concerning the basic requirements that the Service considers essential in cases where all or part of a taxpayer's books and records are maintained within an automatic data processing system. See Rev. Proc. 86-19, page 10.

Section 7872.—Treatment of Loans with Below-Market Interest Rates

Federal short-term, mid-term and long-term rates determined for purposes of section 1274(d) of the Code are set forth for the month of April 1986. See Rev. Rul. 86-50, above.

26 CFR 601.105: Examination of returns and claims for refund, credit or abatement; determination of correct tax liability.
(Also Part I, Section 6001.)

Rev. Proc. 86-19

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to update Rev. Proc. 64-12, 1964-1 (Part 1) C.B. 672, and Rev. Proc. 80-42, 1980-2 C.B. 776, and to specify the basic requirements that the Internal Revenue Service considers to be essential in cases where a taxpayer's records are maintained within an Automatic Data Processing (ADP) system. Rev. Proc. 64-12 provides guidelines for record requirements to be followed in cases where part or all of the accounting records are maintained within an ADP system, and Rev. Proc. 80-42 extended the ADP requirements to the windfall profit tax under section 4997 of the Internal Revenue Code. References here to ADP systems include all accounting and/or financial systems that process all or part of a taxpayer's transactions, records, or data by other than manual methods.

.02 The technology of automatic data processing has evolved rapidly, and new methods and techniques are constantly being devised and adopted. The requirements set forth in Section 5 of this revenue procedure are intended to ensure that all machine-sensible records generated by a taxpayer's automatic data processing system are retained so long as they may become material in the administration of any internal revenue law. These requirements will be modified and amended as the need indicates to keep pace with developments in automatic data processing systems.

.03 This revenue procedure pertains to taxpayers with assets of $10 million or more. For the purpose of this revenue procedure, a controlled group of corporations will be considered to be one corporation and the assets of all members of the group will be aggregated.

.04 The District director has the authority to enter into an agreement with the taxpayer to modify or waive any or all of the specific requirements of this revenue procedure. The taxpayer remains subject to all requirements of this procedure that are not specifically modified or waived by the agreement.

SEC. 2. BACKGROUND

.01 Section 6001 of the Code provides that every person liable for any tax imposed by the Code, or for the collection thereof, shall keep such records as the Secretary may from time to time prescribe.

.02 Rev. Rul. 71-20, 1971-1 C.B. 392, establishes that all machine-sensible data media used for recording, consolidating, and summarizing accounting transactions and records within a taxpayer's automatic data processing system are records within the meaning of section 6001 of the Code and section 1.6001-1 of the Income Tax Regulations and are required to be retained so long as the contents may be material in the administration of any internal revenue law. Accordingly, a taxpayer is required to retain all machine-sensible files generated by its automatic data processing system unless a retention agreement is reached with the District Director to limit the retention to certain specified records.

SEC. 3. SCOPE AND OBJECTIVE

.01 Modern data processing accounting systems are capable of recording business transactions much more rapidly and accurately than manual systems, and they are capable of retaining and producing vast amounts of data. The ability to produce in legible form data necessary to determine at a later date whether or not the correct tax liability has been reported must be carefully considered in designing and programming an ADP system. This factor may add to the complexity of the system and require additional cost, but this cost may be negligible in comparison to the expense that may be incurred at a later date if the system cannot practically and readily provide the information needed to support and substantiate the accuracy of the previously reported tax liability. This revenue procedure encompasses all types of data processing systems, including those using a Data Base Management System.

.02 The requirements of this revenue procedure pertain to income, windfall profit, excise, employment, and estate and gift taxes.

.03 The requirements of this revenue procedure are applicable to the machine-sensible records generated by a Controlled Foreign Corporation (CFC), since the definition of "records" in section 964(c) and 982(d) of the Code and the regulations thereunder has the same meaning as "records" as used in section 6001 and section 1.6001-1(a) of the regulations.

.04 Machine-sensible records used by an insurance company to determine its loss deduction under section 832(b)(5) of the Code must be retained in accordance with the requirements of this revenue procedure and Rev. Proc. 75-56, 1975-2 C.B. 596. The machine-sensible file(s) for a particular taxable year include(s) that year and the seven preceding years, all of which must be retained so long as they are material to the examination of the return. Normally that materiality continues until the expiration of the statute of limitations (including extensions) for the tax year under examination.

SEC. 4. MACHINE-SENSIBLE RECORDS EVALUATION

.01 A record evaluation may be conducted by the District Director to determine if a taxpayer may limit its retention of machine-sensible records. This evaluation of the data processing and accounting systems may be initiated by the District Director or requested by the taxpayer and is not an "examination," "investigation," or "inspection" within the meaning of section 7605(b) of the Code, since such an evaluation is not directly related to the determination of tax liability for a particular taxable period.

.02 The District Director may periodically initiate tests to establish the readability and completeness of the machine-sensible records retained under a retention agreement. Such test are not an examination of the books and records within the meaning of section 7605(b) of the Code, since they are not directly related to the determination of tax liability for a particular taxable period.

SEC. 5. REQUIREMENTS

.01 All machine-sensible records must be retained by the taxpayer. The retained records must be in a retrievable format that provides the information necessary to determine the correct tax liability. The utilization of a service bureau or time-sharing service does not relieve the taxpayer of its responsibilities as described in this revenue procedure.

.02 Documentation that provides a complete description of the ADP portion of the accounting system and those files that feed into the accounting system must be retained. The statements and illustrations as to the scope of operations should be sufficiently detailed to indicate: (a) the application being performed, (b) the procedures employed in each application, and (c) the controls used to insure accurate and reliable processing. The following specific documentation for all files must also be retained:

(1) record formats (including the meaning of all "codes" used to represent information);

(2) flowcharts (system and program);

(3) label descriptions;

(4) source program listings of programs that created the files retained; and

(5) detailed charts of accounts (for specific periods).

Major changes to the ADP system, together with their effective dates, should be noted in order to preserve an accurate chronological record. This record should include any changes to software or systems and any changes to the formats of files. Audit trails should be designed to insure that details underlying the summary accounting data, such as invoices and vouchers, may be easily identified and made available to the Service upon request.

.03 The records are required to be retained so long as their contents may become material in the administration of any internal revenue law. At a minimum, this materiality is possible until the expiration of the statute of limitations (including extensions) for each tax year. In certain situations, files should be retained for a longer period (for example, fixed assets and insurance loss reserve).

.04 The provisions of this revenue procedure do not relieve taxpayers of their responsibility for retaining hardcopy records. The hardcopy records may be retained in microfiche or microfilm format in accordance with the requirements outlined in Rev. Proc. 81-46, 1981-2 C.B. 621. These records are *not* a substitute for the machine-sensible records required to be retained as described in section 5.01 above.

.05 All retained records must be clearly labeled and stored in a secure environment. For example, supplemental labels with the statement, "Retain for IRS until ________" or "Retain for IRS, Consult Tax Manager Before Releasing" should be used and affixed to each tape reel, disk pack, or diskette being retained, with a retention date on the internal label. Back up machine-sensible files being retained for the Service should be stored at an off-site location.

.06 The taxpayer must have the capability to access the retained records at the time of a Service examination. When the data processing system that created the records is being replaced by a system in which the records would not be compatible, the taxpayer must convert them to a compatible system. Any changes in the accessibility of the retained records must be reported to the Service. The District Director has the authority to enter into an agreement with the taxpayer to modify or waive any or all of the requirements for conversion or to approve substitute procedures. The taxpayer remains subject to all requirements that the agreement does not specifically modify, waive, or replace.

.07 The limitation pursuant to a retention agreement on machine-sensible records to be retained does not apply to subsidiary companies acquired, or accounting and tax systems added, subsequent to the completion of the record evaluation or re-evaluation. All machine-sensible records produced by these companies or systems must be retained until such time as a reevaluation is conducted by the District Director. On disposition of a subsidiary the files being retained for the Service by, or for, the disposed subsidiary should be retained until a new evaluation can be made by the District Director. A reevaluation can be requested by the taxpayer.

.08 The taxpayer should make periodic checks on all files being retained for use by the Service. If any machine-sensible records required to be retained are subsequently lost, destroyed, damaged, or found to be incomplete or materially inaccurate, the taxpayer must report this to the District Director and re-create the files within a reasonable period of time.

.09 The use of Data Base Management Systems (DBMS) necessitates the implementation by the taxpayer of appropriate procedures to ensure that required records and other needed documentation are retained to comply with this revenue procedure. A taxpayer is in compliance if it creates, for Service use, a sequential file(s) that contains all detail transactions necessary to create an audit trail to trace back to the underlying source documents. All necessary fields must be identified and the file documentation must follow the rules in section 5.02 above. This process should be reviewed by the Service prior to creation. These sequential files must be processible by conventional means. As a minimum, the following documentation must be made available:

(1) Data Base Description (DBD);

(2) Record layout of each segment with respect to the fields in the segments;

(3) Systems Control Language;

(4) Program Specification Block (PSB);

(5) Program Communication Block (PCB).

Any taxpayer that has questions or is uncertain as to its responsibilities with respect to the retention of data when utilizing a DBMS should contact the District Director.

SEC. 6. PENALTIES

Failure to comply with the provisions of this revenue procedure may result in the assertion of the addition to tax under section 6653(a) of the Code, a civil penalty. The criminal penalty under section 7203 may also be applicable. *See* Rev. Rul. 81-205, 1981-2 C.B. 225. In addition, the District Director may issue a Notice of Inadequate Records if machine-sensible records were not properly retained as required by this revenue procedure.

SEC. 7. COMMENTS OR INQUIRIES

Comments or inquiries to this revenue procedure should be addressed to the Assistant Commissioner (Examination), Attention: OP:EX, Internal Revenue Service, 1111 Constitution Ave. N.W., Washington, D.C. 20224.

SEC. 8. EFFECTIVE DATE

This revenue procedure is effective April 7, 1986, the date of publication.

SEC. 9. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 64-12 and Rev. Proc. 80-42 are superseded.

Part IV. Items of General Interest

Taxation of Fringe Benefits and Exclusions from Gross Income for Certain Fringe Benefits—Public Hearing

Announcement 86-42[1]

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to the taxation of fringe benefits.

DATES: The public hearing will be held on Tuesday, April 29, 1986, beginning at 10:00 a.m. If necessary to accommodate all speakers, the public hearing will be reconvened on Wednesday, April 30, 1986, at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Friday, April 11, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, ATT: CC:LR:T (LR-216-84), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935 (not a toll-free call).

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under sections 61 and 132 of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Monday, December 23, 1985 (50 FR 52333) [LR-216-84, 1986-3 I.R.B. 40].

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Friday, April 11, 1986, an outline of the oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions, attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

Lists of Master and Prototype Plans Closed or Otherwise Disposed of by December 31, 1985, and Plans Erroneously Omitted from Announcement 85-99

Announcement 86-43

This Announcement contains two lists of master or prototype (M&P) pension, annuity or profit sharing plans submitted to the National Office of the Internal Revenue Service by sponsoring organizations and mass submitters.

The first list (List A) includes those M&P plans that were timely submitted under Revenue Procedure 84-23, 1984-1 C.B. 457, by December 31, 1984, and were closed or otherwise disposed of by the Service between October 1, 1985, and December 31, 1985.

List A contains the names and addresses of the plans' sponsoring organization or mass submitter, symbols indicating the type of plan, and file folder number. It also shows the date of disposition of the plan and the type of disposition as follows: (1) favorable opinion letter (F), (2) unfavorable/nonopinion letter (U), (3) withdrawal letter (W), or (4) other (O).

Employers that adopted an approved M&P plan and, if appropriate, requested a determination letter on or before March 19, 1984, and received a favorable determination letter, retained reliance on their favorable letter under the provisions of Section 12 of Rev. Proc. 84-23. However, if the approved plan is included in List A, the employer must take further action in order to have continued reliance.

If List A shows that the plan adopted by the employer received a favorable opinion letter, the employer must, within 12 months after the sponsor received the favorable letter, either (1) amend its existing plan by adopting the sponsor's M&P plan is approved by the Service, or (2) adopt an M&P plan of another sponsor on List A or a subsequent quarterly list, that has received a favorable letter (See Announcement 85-130, 1985-36 I.R.B. 58).

If List A shows that the plan was closed other than by issuance of a favorable opinion letter, such employer must either (1) make all amendments required by Section 5 of Rev. Proc. 84-23, including amendments to conform with the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) Pub. L. 97-248, 1982-2 C.B. 462, the Tax Reform Act of 1984 (TRA) Pub L. 98-369, 1984-3 (Vol. 1) C.B. 1, and the Retirement Equity Act of 1984 (REA) Pub. L. 98-397, 1984-2 C.B. 433, and submit a request for a determination letter to the appropriate key district office, or (2) adopt an M&P plan of a sponsor listed in Announcement 85-99, 1985-28 I.R.B. 4, or List B of Announcement 85-165, 1985-47 I.R.B. 4, or this Announcement, that has received a favorable opinion letter. In either case, in order to be afforded continued reliance, the employer must adopt the amended plan by October 31, 1986.

After amending its existing plan or adopting another M&P plan, an employer must request a determination letter from the appropriate key district office in order to rely on the plan's qualification unless the employer adopts a standardized plan or paired plans within the meaning of Section 6.01 of Rev. Proc. 84-23.

The second list in this Announcement (List B) includes those M&P plans that were inadvertently omitted from the list published in Announcement 85-99. See Announcement 85-99 regarding when these plans must be amended.

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[1] Filed by the Office of the Federal Register on March 11, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 12, 1986, 51 F.R. 8517.

If there are any questions regarding the publication of this list, please call (202) 566-6783 (not a toll free number). Written inquiries should be addressed to Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. Attention: OP:E:EP:RQ:1.

LISTING OF MASTER OR PROTOTYPE PLANS

Abbreviations:

Type of Closing
F = Favorable
U = Unfavorable/nonopinion
W = Withdrawal
O = Other

Type of Plan
P = Paired
S = Standardized (not paired)
NS = Nonstandardized
PS = Profit Sharing
M = Money Purchase
T Target Benefit

Acadiana Bank; Eunice, LA; 50301630001-001; NS; PS; F; 12/19/85.
Acadiana Bank; Eunice, LA; 50301630001-002; NS; M; F; 12/28/85.
ADV Fund Inc; New York, NY; 50201700001-001; S; M; F; 12/02/85.
American Bank & Trust Co; Marion, IN; 50202471801-001; S; M; F; 10/03/85.
American Bar Retirement Association; Chicago, IL; 50202580001-001; P; PS; F; 12/24/85.
American Bar Retirement Association; Chicago, IL; 50202580001-002; P; M; F; 12/24/85.
American Bar Retirement Association; Chicago, IL; 50302580002-001; NS; PS; F; 12/24/85.
American Bar Retirement Association; Chicago, IL; 50302580002-002; NS; M; F; 12/24/85.
American Capital Marketing Inc; Houston, TX; 50202820002-001; S; PS; U; 11/07/85.
American Capital Marketing Inc; Houston, TX; 50202820004-001; S; PS; U; 11/07/85.
American Capital Marketing Inc; Houston, TX; 50202820004-002; S; M; U; 11/07/85.
American Consulting Engineers Council; Washington, DC; 50202660001-001; S; PS; F; 12/24/85.
American Defender Life Insurance Co; Raleigh, NC; 50302670001-001; NS; PS; F; 10/23/85.
American Defender Life Insurance Co; Raleigh, NC; 50302670001-002; NS; M; F; 12/02/85.
American Exchange Bank; Madison, WI; 50202710002-001; S; PS; F; 12/05/85.
American Exchange Bank; Madison, WI; 50202710002-002; S; M; F; 12/05/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963402-001; NS; PS; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963402-002; NS; PS; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963402-003; NS; PS; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963402-004; NS; PS; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963402-005; P; PS; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963402-006; NS; M; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963402-007; NS; M; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963402-008; NS; M; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963402-009; NS; M; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963402-010; P; M; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963402-011; P; PS; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963402-012; P; M; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963402-013; S; M; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963402-014; S; PS; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963402-015; S; PS; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963402-016; S; M; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963403-001; NS; D; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50360963403-002; NS; D; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963403-003; S; D; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963403-004; S; D; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963403-005; S; D; F; 10/07/85.
American First Title & Trust Co; Oklahoma City, OK; 50260963403-006; S; D; F; 10/07/85.
American Fund Advisors Inc; New York, NY; 50270410001-001; P; PS; F; 12/24/85.
American Fund Advisors Inc; New York, NY; 50270410001-002; P; M; F; 12/24/85.
American Fund Advisors Inc; New York, NY; 50370410001-003; NS; PS; F; 12/24/85.
American Fund Advisors Inc; New York, NY; 50370410001-004; NS; M; F; 12/24/85.
American Investors Fund Inc; Greenwich, CT; 50303035101-001; NS; M; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50203035101-002; P; M; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50203035101-003; P; M; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50303035101-004; NS; PS; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50203035101-005; P; PS; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50203035101-006; P; PS; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50303035102-001; NS; D; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50303035102-002; NS; D; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50203035102-003; P; D; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50203035102-004; P; D; F; 10/09/85.
American Investors Fund Inc; Greenwich, CT; 50203035102-005; P; D; F; 10/09/85.
American National Bank; Noblesville, IN; 50203171801-001; P; M; F; 10/03/85.
American National Bank; Noblesville, IN; 50303171801-002; NS; M; F; 10/03/85.
American National Bank; Noblesville, IN; 50203171801-003; P; PS; F; 10/03/85.
American National Bank; Noblesville, IN; 50303171801-004; NS; PS; F; 10/03/85.
American National Bank & Trust Co; Muncie, IN; 50203311801-001; P; M; F; 10/03/85.
American National Bank & Trust Co; Muncie, IN; 50303311801-002; NS; M; F; 10/03/85.
American National Bank & Trust Co; Muncie, IN; 50203311801-003; P; PS; F; 10/03/85.
American National Bank & Trust Co; Muncie, IN; 50303311801-004; NS; PS; F; 10/03/85.
American National Bank & Trust Co of Chicago; Chicago, IL; 50303290002-001; NS; PS; F; 12/19/85.
American National Bank & Trust Co of Chicago; Chicago, IL; 50203290002-002; S; PS; F; 12/19/85.
American National Bank & Trust Co of Chicago; Chicago, IL; 50303290002-003; NS; M; F; 12/19/85.
American National Bank & Trust Co of Chicago; Chicago, IL; 50203290002-004; S; M; F; 12/19/85.
American Security Bank NA; Washington, DC; 50203660001-001; P; M; F; 10/23/85.
American Security Bank NA; Washington, DC; 50303660001-002; NS; M; F; 10/23/85.
American Security Bank NA; Washington, DC; 50203660001-003; P; PS; F; 10/23/85.
American Security Bank NA; Washington, DC; 50303660001-004; NS; PS; F; 10/23/85.
American State Bank; Yankton, SD; 50303860001-001; NS; PS; F; 12/19/85.
American State Bank; Yankton, SD; 50303860001-002; NS; M; F; 12/19/85.
American United Life Insurance Co; Indianapolis, IN; 50303930001-001; NS; PS; F; 12/23/85.
American United Life Insurance Co; Indianapolis, IN; 50303930002-001; NS; M; F; 12/23/85.
American United Life Insurance Co; Indianapolis, IN; 50303930003-001; NS; D; F; 12/23/85.
American United Life Insurance Co; Indianapolis, IN; 50303930003-002; NS; D; F; 12/24/85.
American United Life Insurance Co; Indianapolis, IN; 50303930004-001; NS; PS; F; 12/23/85.
American United Life Insurance Co; Indianapolis, IN; 50203930004-002; S; PS; F; 12/23/85.
American United Life Insurance Co; Indianapolis, IN; 50303930005-001; NS; M; F; 12/23/85.
American United Life Insurance Co; Indianapolis, IN; 50203930005-002; S; M; F; 12/23/85.
AMOCO Life Insurance Co; Omaha, NE; 50204070001-001; P; PS; F; 12/02/85.
AMOCO Life Insurance Co; Omaha, NE; 50204070001-002; P; M; F; 12/02/85.
AMOCO Life Insurance Co; Omaha, NE; 50304070001-003; NS; PS; F; 12/02/85.
AMOCO Life Insurance Co; Omaha, NE; 50304070001-004; NS; M; F; 12/02/85.
AMOCO Life Insurance Co; Omaha, NE; 50204070002-001; P; D; F; 12/02/85.
AMOCO Life Insurance Co; Omaha, NE; 50204070002-002; P; D; F; 12/02/85.
AMOCO Life Insurance Co; Omaha, NE; 50304070002-003; NS; D; F; 12/02/85.
AMOCO Life Insurance Co; Omaha, NE; 50304070002-004; NS; D; F; 12/02/85.
Amoskeag National Bank & Trust Co; Manchester, NH; 50304080001-001; NS; M; F; 10/23/85.
Amoskeag National Bank & Trust Co; Manchester, NH; 50304080002-001; NS; PS; F; 10/23/85.
AmSouth Bank NA; Birmingham, AL; 50261413501-007; P; PS; U; 10/30/85.
AmSouth Bank NA; Birmingham, AL; 50261413501-009; P; M; U; 10/30/85.
Amway Mutual Fund Inc; Ada, MI; 50270420001-001; S; PS; F; 12/20/85.
Atlantic Permanent Federal Savings & Loan Association; Norfolk, VA; 50204680001-001; P; PS; F; 12/27/85.
Atlantic Permanent Federal Savings & Loan Association; Norfolk, VA; 50204680001-002; P; M; F; 12/20/85.
Atlantic Permanent Federal Savings & Loan Association; Norfolk, VA; 50304680001-003; NS; PS; F; 12/20/85.
Atlantic Permanent Federal Savings & Loan Association; Norfolk, VA; 50304680001-004; NS; M; F; 12/20/85.
Attleborough Savings Bank; Harrison, NY; 50204718601-001; S; M; F; 10/09/85.
Attleborough Savings Bank; Harrison, NY; 50204718601-002; S; M; F; 10/09/85.
Attleborough Savings Bank; Harrison, NY; 50304718601-003; NS; M; F; 10/09/85.
Attleborough Savings Bank; Harrison, NY; 50304718601-004; NS; M; F; 10/09/85.
Attleborough Savings Bank; Harrison, NY; 50204718601-005; S; PS; F; 10/09/85.
Attleborough Savings Bank; Harrison, NY; 50204718601-006; S; PS; F; 10/09/85.
Attleborough Savings Bank; Harrison, NY; 50304718601-007; NS; PS; F; 10/09/85.
Attleborough Savings Bank; Harrison, NY; 50304718601-008; NS; PS; F; 10/09/85.
Atwater State Bank; Atwater, MN; 50204727001-001; S; PS; F; 10/11/85.
Atwater State Bank; Atwater, MN; 50204727001-002; S; PS; F; 10/11/85.
Atwater State Bank; Atwater, MN; 50204727001-003; S; M; F; 10/11/85.
Atwater State Bank; Atwater, MN; 50204727001-004; S; M; F; 10/11/85.
Atwater State Bank; Atwater, MN; 50304727001-005; NS; PS; F; 10/11/85.
Atwater State Bank; Atwater, MN; 50304727001-006; NS; PS; F; 10/11/85.
Atwater State Bank; Atwater, MN; 50304727001-007; NS; M; F; 10/11/85.
Atwater State Bank; Atwater, MN; 50304727001-008; NS; M; F; 10/11/85.
Bank of Ashland; Ashland, KY; 50305070001-001; NS; PS; F; 11/15/85.
Bank of Ashland; Ashland, KY; 50305070001-002; NS; PS; F; 11/15/85.
Bank of Ashland; Ashland, KY; 50305070002-001; NS; M; F; 11/15/85.
Bank of Ashland; Ashland, KY; 50305070002-002; NS; M; F; 11/15/85.
Bank of Lansing; Lansing, MI; 50306020001-001; NS; PS; F; 10/30/85.
Bank of Lansing; Lansing, MI; 50206020001-002; S; PS; F; 10/30/85.
Bank of Lansing; Lansing, MI; 50306020001-003; NS; M; F; 10/30/85.
Bank of Lansing; Lansing, MI; 50206020001-004; S; M; F; 10/30/85.
Bank of Lansing; Lansing, MI; 50306020002-001; NS; D; F; 10/30/85.
Bank of Lansing; Lansing, MI; 50206020002-002; S; D; F; 10/30/85.
Bank of Lansing; Lansing, MI; 50306020002-003; NS; D; F; 10/30/85.
Bank of Lansing; Lansing, MI; 50206020002-004; S; D; F; 10/30/85.
Bank of Middleton; Middleton, WI; 50206210001-001; S; PS; F; 12/05/85.
Bank of Middleton; Middleton, WI; 50206210001-002; S; M; F; 12/05/85.
Bank of Mount Carmel; Mount Carmel, IL; 50206271802-001; P; M; F; 10/03/85.
Bank of Mount Carmel; Mount Carmel, IL; 50206271802-002; P; PS; F; 10/03/85.
Bank of New England NA; Boston, MA; 50206321401-001; P; M; F; 11/22/85.
Bank of New England NA; Boston, MA; 50206321401-002; P; PS; F; 11/22/85.
Bank of New England NA; Boston, MA; 50206321401-003; P; M; F; 11/22/85.

Bank of New England NA; Boston, MA; 50206321401-004; P; PS; F; 11/22/85.
Bank of New England NA; Boston, MA; 50206321401-005; P; M; F; 11/22/85.
Bank of New England NA; Boston, MA; 50206321401-006; P; PS; F; 11/22/85.
Bank of New England NA; Boston, MA; 50206321401-007; P; M; F; 11/22/85.
Bank of New England NA; Boston, MA; 50206321401-008; P; PS; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321402-001; NS; M; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321402-002; NS; PS; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321402-003; NS; M; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321402-004; NS; PS; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321402-005; NS; M; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321402-006; NS; PS; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321402-007; NS; M; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321402-008; NS; PS; F; [illegible]/22/85.
Bank of New England NA; Boston, MA; 50206321403-001; S; M; F; 11/22/85.
Bank of New England NA; Boston, MA; 50206321403-002; S; PS; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321403-003; NS; M; F; 11/22/85.
Bank of New England NA; Boston, MA; 50306321403-004; NS; PS; F; 11/22/85.
Bank of Pennsylvania; Reading, PA; 50206620001-001; S; PS; F; 10/23/85.
Bank of Pennsylvania; Reading, PA; 50206620001-002; S; PS; F; 10/23/85.
Bank of Pennsylvania; Reading, PA; 50206620002-001; S; M; F; 10/23/85.
Bank of Pennsylvania; Reading, PA; 50206620002-002; S; M; F; 10/23/85.
Bank of Shorewood Hills; Madison, WI; 50206670001-001; S; PS; F; 12/05/85.
Bank of Shorewood Hills; Madison, WI; 50206670001-002; S; M; F; 12/05/85.
Bank of Virginia; Richmond, VA; 50306961801-001; NS; M; F; 10/03/85.
Bank of Virginia; Richmond, VA; 50306961801-002; NS; PS; F; 10/03/85.
Bank One Alliance NA; Alliance, OH; 50226901901-001; P; PS; F; 12/06/85.
Bank One Alliance NA; Alliance, OH; 50226901901-002; P; M; F; 12/06/85.
Bank One Alliance NA; Alliance, OH; 50326901901-003; NS; PS; F; 12/06/85.
Bank One Alliance NA; Alliance, OH; 50326901901-004; NS; M; F; 12/06/85.
Bank One Alliance NA; Alliance, OH; 50326901901-005; NS; PS; F; 12/06/85.
Bank One Alliance NA; Alliance, OH; 50326901901-006; NS; M; F; 12/06/85.
Bankers Systems Financial Services Inc; St Cloud, MN; 50270380003-001; S; PS; F; 12/19/85.
Bankers Trust Co; New York, NY; 50233110001-001; P; PS; F; 12/26/85.
Bankers Trust Co; New York, NY; 50333110001-003; NS; PS; F; 12/26/85.
Bankers Trust Co; New York, NY; 50333110001-004; NS; M; F; 12/26/85.
Banking Spectrum Inc; New York, NY; 50299757501-001; P; PS; F; 10/31/85.
Banking Spectrum Inc; New York, NY; 50299757501-002; P; M; F; 10/31/85.
Banking Spectrum Inc; New York, NY; 50299757501-003; P; PS; F; 10/31/85.
Banking Spectrum Inc; New York, NY; 50299757501-004; P; M; F; 10/31/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50308244401-001; NS; D; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50308244401-002; NS; D; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244401-003; P; D; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244401-004; P; D; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244401-005; P; D; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244401-006; P; D; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50308244402-001; NS; PS; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50308244402-002; NS; M; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50308244402-003; NS; T; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50308244402-004; NS; PS; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244402-005; P; PS; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244402-006; P; M; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244402-007; P; T; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244402-008; P; PS; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244402-009; P; M; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244402-010; P; T; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244402-011; P; PS; F; 12/10/85.
Berkshire Bank & Trust Co; Pittsfield, MA; 50208244402-012; P; M; F; 12/10/85.
Beverly Bank; Chicago, IL; 50208300001-001; S; PS; F; 10/23/85.
Beverly Bank; Chicago, IL; 50208300001-002; S; M; F; 10/23/85.
Beverly Bank; Chicago, IL; 50208300001-003; S; PS; F; 10/23/85.
Beverly Bank; Chicago, IL; 50208300001-004; S; M; F; 10/23/85.
Beverly Bank; Chicago, IL; 50308300001-005; NS; PS; F; 10/23/85.
Beverly Bank; Chicago, IL; 50308300001-006; NS; M; F; 10/23/85.
Beverly Bank; Chicago, IL; 50308300001-007; NS; PS; F; 10/23/85.
Beverly Bank; Chicago, IL; 50208300001-008; S; M; F; 10/23/85.
Blue Ridge Bank & Trust Co; Kansas City, MO; 50373462201-001; NS; PS; F; 12/04/85.
Blue Ridge Bank & Trust Co; Kansas City, MO; 50373462201-002; NS; M; F; 12/04/85.
Boatmens Union National Bank of Springfield; Springfield, MO; 50308560001-001; NS; M; F; 12/26/85.
Boatmens Union National Bank of Springfield; Springfield, MO; 50308560001-002; NS; M; F; 12/26/85.
Boatmens Union National Bank of Springfield; Springfield, MO; 50308560001-003; NS; PS; F; 12/26/85.
Boatmens Union National Bank of Springfield; Springfield, MO; 50308560001-004; NS; PS; F; 12/26/85.
Boatmens Union National Bank of Springfield; Springfield, MO; 50308560001-005; NS; M; F; 12/26/85.
Boatmens Union National Bank of Springfield; Springfield, MO; 50308560001-006; NS; M; F; 12/26/85.
Boatmens Union National Bank of Springfield; Springfield, MO; 50308560001-007; NS; PS; F; 12/26/85
Boatmens Union National Bank of Springfield; Springfield, MO; 50308560001-008; NS; PS; F; 12/26/85.
Branch Banking & Trust Co; Wilson, NC; 50308790001-001; NS; PS; F; 12/19/85.
Branch Banking & Trust Co; Wilson, NC; 50308790001-002; NS; M; F; 12/19/85.
Bucks County Bank & Trust Co; Perkasie, PA; 50308990001-001; NS; M; F; 12/05/85.
Bucks County Bank & Trust Co; Perkasie, PA; 50308990002-001; NS; PS; F; 12/05/85.
Bucks County Bank & Trust Co; Perkasie, PA; 50208990003-001; S; M; F; 12/05/85.
Bucks County Bank & Trust Co; Perkasie, PA; 50208990004-001; S; PS; F; 12/05/85.
California Federal Savings & Loan Association; Los Angeles, CA; 50209320001-001; S; PS; U; 11/15/85.
California Federal Savings & Loan Association; Los Angeles, CA; 50209320001-002; S; M; U; 11/15/85.
California Federal Savings & Loan Association; Los Angeles, CA; 50309320001-003; NS; PS; U; 11/15/85.
California Federal Savings & Loan Association; Los Angeles, CA; 50309320001-004; NS; M; U; 11/15/85.
California League of Savings Institutions; Los Angeles, CA; 50209400001-001; P; PS; F; 11/15/85.
California League of Savings Institutions; Los Angeles, CA; 50209400001-002; P; M; F; 11/15/85.
California League of Savings Institutions; Los Angeles, CA; 50309400003-001; NS; PS; F; 11/15/85.
California League of Savings Institutions; Los Angeles, CA; 50309400003-002; NS; M; F; 11/15/85.
Calumet National Bank; Hammond, IN; 50262201801-001; P; M; F; 10/03/85.
Calumet National Bank; Hammond, IN; 50362201801-002; NS; M; F; 10/03/85.
Calumet National Bank; Hammond, IN; 50262201801-003; P; PS; F; 10/03/85.
Calumet National Bank; Hammond, IN; 50362201801-004; NS; PS; F; 10/03/85.
Calvin Bullock Ltd; New York, NY; 50209485001-003; P; PS; F; 12/04/85.
Calvin Bullock Ltd; New York, NY; 50209485001-004; P; M; F; 12/04/85.
Capital Holding Corp; Louisville, KY; 50370296401-001; NS; M; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50270296401-002; S; M; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50370296401-003; NS; PS; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50270296401-004; S; PS; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50370296401-005; NS; PS; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50370296402-001; NS; D; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50270296402-002; S; D; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50370296402-003; NS; D; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50270296402-004; S; D; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50370296402-005; NS; D; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50270296402-006; S; D; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50370296402-007; NS; D; F; 10/03/85.
Capital Holding Corp; Louisville, KY; 50270296402-008; S; D; F; 10/03/85.
Capitol Federal Savings & Loan Association; Lansing, MI; 50309840001-001; NS; PS; F; 10/23/85.
Capitol Federal Savings & Loan Association; Lansing, MI; 50309840001-002; NS; PS; F; 10/23/85.
Capitol Federal Savings & Loan Association; Lansing, MI; 50309840002-001; NS; M; F; 10/23/85.
Capitol Federal Savings & Loan Association; Lansing, MI; 50309840002-002; NS; M; F; 10/23/85.
Capitol Federal Savings & Loan Association; Lansing, MI; 50309840003-001; NS; D; F; 10/23/85.
Capitol Federal Savings & Loan Association; Lansing, MI; 50309840003-002; NS; D; F; 10/23/85.
Capitol Federal Savings & Loan Association; Lansing, MI; 50309840003-003; NS; D; F; 10/23/85.
Capitol Federal Savings & Loan Association; Lansing, MI; 50309840003-004; NS; D; F; 10/23/85.
Capitol Federal Savings & Loan Association; Lansing, MI; 50309840003-005; NS; D; F; 10/23/85.
Cash Equivalent Fund Inc; Chicago, IL; 50273308201-001; P; PS; F; 11/14/85.
Cash Equivalent Fund Inc; Chicago, IL; 50273308201-002; P; M; F; 11/14/85.
Cash Equivalent Fund Inc; Chicago, IL; 50373308201-003; NS; PS; F; 11/14/85.
Cash Equivalent Fund Inc; Chicago, IL; 50373308201-004; NS; M; F; 11/14/85.
Centerre Bank of Columbia; Columbia, MO; 50310300001-001; NS; PS; F; 12/28/85.
Centerre Bank of Columbia; Columbia, MO; 50310300001-002; NS; M; F; 12/28/85.
Central Bank; Walnut Creek, CA; 50210590002-001; S; M; F; 12/20/85.
Central Bank; Walnut Creek, CA; 50210590002-002; S; PS; F; 12/20/85.
Central Bank of the South; Birmingham, AL; 50310620001-001; NS; M; F; 12/23/85.
Central Bank of the South; Birmingham, AL; 50310620001-002; NS; M; F; 12/23/85.

Central Bank of the South; Birmingham, AL; 50310620002-001; NS; PS; F; 12/08/85.

Central Bank of the South; Birmingham, AL; 50310620002-002; NS; PS; F; 12/08/85.

Central National Bank of Greencastle; Greencastle, IN; 50210871801-001; S; PS; F; 10/03/85.

Central National Bank of Greencastle; Greencastle, IN; 50310871801-002; NS; PS; F; 10/03/85.

Central State Bank; Connersville, IN; 50210981801-001; P; M; F; 10/03/85.

Central State Bank; Connersville, IN; 50310981801-002; NS; M; F; 10/03/85.

Central State Bank; Connersville, IN; 50210981801-003; P; PS; F; 10/03/85.

Central State Bank; Connersville, IN; 50310981801-004; NS; PS; F; 10/03/85.

Central Trust Co NA; Cincinnati, OH; 50211060001-001; P; PS; F; 12/26/85.

Central Trust Co NA; Cincinnati, OH; 50211060001-002; P; M; F; 12/26/85.

Central Trust Co NA; Cincinnati, OH; 50311060001-003; NS; PS; F; 12/26/85.

Central Trust Co NA; Cincinnati, OH; 50311060001-004; NS; M; F; 12/26/85.

Central Trust Co NA; Cincinnati, OH; 50311060001-005; NS; PS; F; 12/26/85.

Central Trust Co NA; Cincinnati, OH; 50311060001-006; NS; M; F; 12/26/85.

Charleston National Bank; Charleston, WV; 50311370001-001; NS; PS; F; 12/02/85.

Charleston National Bank; Charleston, WV; 50311370001-002; NS; M; F; 12/02/85.

Charleston National Bank; Charleston, WV; 50211370002-001; P; PS; F; 12/02/85.

Charleston National Bank; Charleston, WV; 50211370002-002; P; M; F; 12/08/85.

Chase Manhattan Bank NA; New York, NY; 50211440001-001; P; PS; F; 12/19/85.

Chase Manhattan Bank NA; New York, NY; 50211440001-002; P; M; F; 12/19/85.

Chase Manhattan Bank NA; New York, NY; 50211440001-003; P; PS; F; 12/19/85.

Chase Manhattan Bank NA; New York, NY; 50211440001-004; P; M; F; 12/19/85.

Chase Manhattan Bank NA; New York, NY; 50311440001-005; NS; PS; F; 12/19/85.

Chase Manhattan Bank NA; New York, NY; 50311440001-006; NS; M; F; 12/19/85.

Chase Manhattan Bank NA; New York, NY; 50311440001-007; NS; PS; F; 12/19/85.

Chase Manhattan Bank NA; New York, NY; 50311440001-008; NS; M; F; 12/19/85.

Chatham Trust Co; Chatham, NJ; 50211460001-001; P; PS; F; 12/26/85.

Chatham Trust Co; Chatham, NJ; 50211460001-002; P; M; F; 12/26/85.

Chittenden Trust Co; Burlington, VT; 50311720001-001; NS; D; U; 11/01/85.

Chittenden Trust Co; Burlington, VT; 50311720002-001; NS; PS; U; 11/01/85.

Chittenden Trust Co; Burlington, VT; 50311720003-001; NS; M; U; 11/01/85.

Chittenden Trust Co; Burlington, VT; 50311720004-001; NS; T; U; 11/01/85.

Citizens Banking Co; Anderson, IN; 50212491801-001; P; M; F; 10/03/85.

Citizens Banking Co; Anderson, IN; 50312491801-002; NS; M; F; 10/03/85.

Citizens Banking Co; Anderson, IN; 50212491801-003; P; PS; F; 10/03/85.

Citizens Banking Co; Anderson, IN; 50312491801-004; NS; PS; F; 10/03/85.

Citizens Banking Co; Lynn, IN; 50212501801-001; S; M; F; 10/03/85.

Citizens Banking Co; Lynn, IN; 50312501801-002; NS; M; F; 10/03/85.

Citizens Fidelity Bank & Trust Co; Louisville, KY; 50262633501-007; P; PS; U; 10/30/85.

Citizens Fidelity Bank & Trust Co; Louisville, KY; 50262633501-009; P; M; U; 10/30/85.

Citizens National Bank; Tell City, IN; 50212654501-001; P; PS; F; 10/07/85.

Citizens National Bank; Tell City, IN; 50212654501-002; P; M; F; 10/07/85.

Citizens National Bank; Tipton, IN; 50212661801-001; S; M; F; 10/03/85.

Citizens National Bank; Tipton, IN; 50312661801-002; NS; M; F; 10/03/85.

Citizens State Bank in Owensboro; Owensboro, KY; 50213253501-007; P; PS; U; 10/30/85.

Citizens State Bank in Owensboro; Owensboro, KY; 50213253501-009; P; M; U; 10/30/85.

Citizens State Bank of Elizabethtown; Elizabethtown, KY; 50273133501-007; P; PS; U; 10/30/85.

Citizens State Bank of Elizabethtown; Elizabethtown, KY; 50273133501-009; P; M; U; 10/30/85.

Citizens State Bank of Hayfield; Hayfield, MN; 50213347001-001; S; PS; F; 10/11/85.

Citizens State Bank of Hayfield; Hayfield, MN; 50213347001-002; S; PS; F; 10/11/85.

Citizens State Bank of Hayfield; Hayfield, MN; 50213347001-003; S; M; F; 10/11/85.

Citizens State Bank of Hayfield; Hayfield, MN; 50213347001-004; S; M; F; 10/11/85.

Citizens State Bank of Hayfield; Hayfield, MN; 50313347001-005; NS; PS; F; 10/11/85.

Citizens State Bank of Hayfield; Hayfield, MN; 50313347001-006; NS; PS; F; 10/11/85.

Citizens State Bank of Hayfield; Hayfield, MN; 50313347001-007; NS; M; F; 10/11/85.

Citizens State Bank of Hayfield; Hayfield, MN; 50313347001-008; NS; M; F; 10/11/85.

Citizens State Bank of New Castle; New Castle, IN; 50313411801-001; NS; M; F; 10/03/85.

Citizens State Bank of New Castle; New Castle, IN; 50313411801-002; NS; PS; F; 10/03/85.

Citizens State Bank of New Castle; New Castle, IN; 50213411801-003; S; M; F; 10/03/85.

City National Bank & Trust Co of Rockford; Rockford, IL; 50313640001-001; NS; PS; U; 10/22/85.

City National Bank & Trust Co of Rockford; Rockford, IL; 50313640001-002; NS; PS; U; 10/22/85.

Clayton-Brown; Chicago, IL; 50371070001-001; P; PS; F; 12/19/85.

Clayton-Brown; Chicago, IL; 50271070001-002; P; M; F; 12/19/85.

Clinton County Bank & Trust; Frankfort, IN; 50213991801-001; P; M; F; 10/03/85.

Clinton County Bank & Trust; Frankfort, IN; 50213991801-002; P; PS; F; 10/03/85.

Colonial Bank; Waterbury, CT; 50314190001-001; NS; M; F; 12/16/85.

Colonial Bank; Waterbury, CT; 50314190002-001; NS; PS; F; 12/16/85.

Colorado National Bank Boulevard; Denver, CO; 50208680001-001; S; PS; F; 12/26/85.

Colorado National Bank Exchange; Colorado Springs, CO; 50218120001-001; P; PS; F; 12/26/85.

Colorado National Bank Exchange; Colorado Springs, CO; 50218120001-002; P; M; F; 12/26/85.

Colorado National Bank Exchange; Colorado Springs, CO; 50318120001-003; NS; PS; F; 12/26/85.

Colorado National Bank Exchange; Colorado Springs, CO; 50318120001-004; NS; M; F; 12/26/85.

Colorado National Bank Exchange; Colorado Springs, CO; 50218120001-005; S; PS; F; 12/26/85.

Colorado National Bank of Denver; Denver, CO; 50214360001-001; P; PS; F; 12/26/85.

Colorado National Bank of Denver; Denver, CO; 50214360001-002; P; M; F; 12/26/85.

Colorado National Bank of Denver; Denver, CO; 50314360001-003; NS; PS; F; 12/26/85.

Colorado National Bank of Denver; Denver, CO; 50314360001-004; NS; M; F; 12/26/85.

Colorado National Bank of Denver; Denver, CO; 50214360001-005; S; PS; F; 12/26/85.

Colorado National Bank Pueblo; Pueblo, CO; 50226150001-001; P; PS; F; 12/26/85.

Colorado National Bank Pueblo; Pueblo, CO; 50226150001-002; P; M; F; 12/26/85.

Colorado National Bank Pueblo; Pueblo, CO; 50326150001-003; NS; PS; F; 12/26/85.

Colorado National Bank Pueblo; Pueblo, CO; 50326150001-004; NS; M; F; 12/26/85.

Colorado National Bank Pueblo; Pueblo, CO; 50226150001-005; S; PS; F; 12/26/85.

Commerce Bank & Trust; Topeka, KS; 50314633401-001; NS; PS; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50314633401-002; NS; PS; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50314633401-003; NS; PS; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50314633401-004; NS; PS; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633401-005; P; PS; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50314633401-006; NS; M; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50314633401-007; NS; M; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50314633401-008; NS; M; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50314633401-009; NS; M; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633401-010; P; M; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633401-011; P; PS; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633401-012; P; M; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633401-013; S; M; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633401-014; S; PS; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633401-015; S; PS; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633401-016; S; M; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50314633402-001; NS; D; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50314633402-002; NS; D; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633402-003; S; D; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633402-004; S; D; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633402-005; S; D; F; 10/07/85.

Commerce Bank & Trust; Topeka, KS; 50214633402-006; S; D; F; 10/07/85.

Commerce Bank of Springfield; Springfield, MO; 50370650001-001; NS; M; F; 12/28/85.

Commerce Bank of Springfield; Springfield, MO; 50370650001-002; NS; M; F; 12/28/85.

Commerce Bank of Springfield; Springfield, MO; 50370650001-003; NS; PS; F; 12/28/85.

Commerce Bank of Springfield; Springfield, MO; 50370650001-004; NS; PS; F; 12/28/85.

Commerce Bank of Springfield; Springfield, MO; 50370650001-005; NS; PS; F; 12/28/85.

Commerce Bank of Springfield; Springfield, MO; 50370650001-006; NS; PS; F; 12/28/85.

Commerce Bank of Springfield; Springfield, MO; 50370650001-007; NS; M; F; 12/28/85.

Commerce Bank of Springfield; Springfield, MO; 50370650001-008; NS; M; F; 12/28/85.

Commercial Bank of Middlesboro; Middlesboro, KY; 50214833501-007; P; PS; U; 10/30/85.

Commercial Bank of Middlesboro; Middlesboro, KY; 50214833501-009; P; M; U; 10/30/85.

Commercial National Bank; Kansas City, KS; 50314983401-001; NS; PS; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50314983401-002; NS; PS; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50314983401-003; NS; PS; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50314983401-004; NS; PS; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983401-005; P; PS; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50314983401-006; NS; M; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50314983401-007; NS; M; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50314983401-008; NS; M; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50314983401-009; NS; M; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983401-010; P; M; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983401-011; P; PS; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983401-012; P; M; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983401-013; S; M; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983401-014; S; PS; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983401-015; S; PS; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983401-016; S; M; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50314983402-001; NS; D; F; 10/07/35.

Commercial National Bank; Kansas City, KS; 50314983402-002; NS; D; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983402-003; S; D; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983402-004; S; D; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983402-005; S; D; F; 10/07/85.

Commercial National Bank; Kansas City, KS; 50214983402-006; S; D; F; 10/07/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50315194401-001; NS; D; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50315194401-002; NS; D; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194401-003; P; D; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194401-004; P; D; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194401-005; P; D; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194401-006; P; D; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50315194402-001; NS; PS; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50315194402-002; NS; M; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50315194402-003; NS; T; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50315194402-004; NS; PS; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194402-005; P; PS; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194402-006; P; M; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194402-007; P; T; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194402-008; P; PS; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194402-009; P; M; F; 12/10/85.

Commercial Union Life Insurance Co of America; Boston, MA; 50215194402-010; P; T; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50378924401-001; NS; D; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50378924401-002; NS; D; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924401-003; P; D; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924401-004; P; D; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924401-005; P; D; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924401-006; P; D; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50378924402-001; NS; PS; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50378924402-002; NS; M; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50378924402-003; NS; T; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50378924402-004; NS; PS; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924402-005; P; PS; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924402-006; P; M; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924402-007; P; T; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924402-008; P; PS; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924402-009; P; M; F; 12/10/85.

Commercial Union Life Insurance Co of New York; Boston, MA; 50278924402-010; P; T; F; 12/10/85.

Commonwealth Life Insurance Co; Louisville, KY; 50315276401-001; NS; M; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50215276401-002; S; M; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50315276401-003; NS; PS; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50215276401-004; S; PS; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50315276401-005; NS; PS; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50315276402-001; NS; D; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50215276402-002; S; D; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50315276402-003; NS; D; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50215276402-004; S; D; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50315276402-005; NS; D; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY, 50215276402-006; S; D; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50315276402-007; NS; D; F; 10/03/85.

Commonwealth Life Insurance Co; Louisville, KY; 50215276402-008; S; D; F; 10/03/85.

Community State Bank in Huntington; Huntington, IN; 50215431801-001; P; M; F; 10/03/85.

Community State Bank in Huntington; Huntington, IN; 50315431801-002; NS; M; F; 10/03/85.

Community State Bank in Huntington; Huntington, IN; 50215431801-003; P; PS; F; 10/03/85.

Community State Bank in Huntington; Huntington, IN; 50315431801-004; NS; PS; F; 10/03/85.

Compensation Programs Inc; Overland Park, KS; 50399343401-001; NS; PS; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50399343401-002; NS; PS; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50399343401-003; NS; PS; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50399343401-004; NS; PS; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343401-005; P; PS; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50399343401-006; NS; M; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50399343401-007; NS; M; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50399343401-008; NS; M; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50399343401-009; NS; M; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343401-010; P; M; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343401-011; P; PS; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343401-012; P; M; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50399343402-001; NS; D; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50399343402-002; NS; D; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343402-003; S; D; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343402-004; S; D; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343403-001; S; M; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343403-002; S; PS; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343403-003; S; PS; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343403-004; S; M; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343404-001; S; D; F; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343404-002; S; D; F; 10/07/85.

Connecticut National Bank; Hartford, CT; 50252000001-001; S; M; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50252000001-002; S; PS; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50352000001-003; NS; M; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50352000001-004; NS; PS; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50252000002-001; S; M; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50252000002-002; S; PS; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50352000002-003; NS; M; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50352000002-004; NS; PS; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50252000005-001; S; M; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50252000005-002; S; PS; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50352000005-003; NS; M; F; 12/13/85.

Connecticut National Bank; Hartford, CT; 50352000005-004; NS; PS; F; 12/13/85.

Crete State Bank; Crete, NE; 50272190001-001; S; M; F; 12/20/85.

Crossland Savings FSB; Brooklyn, NY; 50259560002-001; P; D; F; 12/23/85.

Crossland Savings FSB; Brooklyn, NY; 50259560002-002; P; D; F; 12/23/85.

Crossland Savings FSB; Brooklyn, NY; 50359560002-003; NS; D; F; 12/23/85.

Crossland Savings FSB; Brooklyn, NY; 50359560002-004; NS; D; F; 12/23/85.

CUNA Mutual Insurance Society; Madison, WI; 50316380001-001; NS; D; F; 10/23/85.

CUNA Mutual Insurance Society; Madison, WI; 50316380001-002; NS; D; F; 10/23/85.

CUNA Mutual Insurance Society; Madison, WI; 50216380001-003; P; D; F; 10/23/85.

CUNA Mutual Insurance Society; Madison, WI; 50216380001-004; P; D; F; 10/23/85.

CUNA Mutual Insurance Society; Madison, WI; 50316380002-001; NS; M; F; 10/23/85.

CUNA Mutual Insurance Society; Madison, WI; 50216380002-002; P; M; F; 10/23/85.

CUNA Mutual Insurance Society; Madison, WI; 50316380002-003; NS; PS; F; 10/23/85.

CUNA Mutual Insurance Society; Madison, WI; 50316380002-004, NS; [illegible]; F; 10/23/85.

Cynthiana State Bank; Cynthiana, IN; 50270450001-001; S; PS; F; 12/03/85.

Dain Bosworth Inc; Minneapolis, MN; 50216410001-001; P; PS; F; 11/15/85.

Dain Bosworth Inc; Minneapolis, MN; 50216410001-002; P; PS; F; 11/15/85.

Dain Bosworth Inc; Minneapolis, MN; 50216410001-003; P; M; F; 11/15/85.

Dain Bosworth Inc; Minneapolis, MN; 50216410001-004; P; M; F; 11/15/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50279596201-001; P; D; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50379596201-002; NS; D; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50279596201-003; P; D; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50379596201-004; NS; D; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50279596202-001; P; PS; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50379596202-002; NS; PS; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50279596202-003; P; M; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50379596202-004; NS; M; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50279596202-005; P; PS; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50279596202-006; P; M; F; 10/31/85.

Dairyland County Mutual Insurance Co of Texas; Stevens Point, WI; 50379596202-007; NS; T; F; 10/31/85.

Dakota Bank & Trust Co; Faro, ND; 50216430001-001; P; PS; F; 12/26/85.

Dakota Bank & Trust Co; Faro, ND; 50216430001-002; P; M; F; 12/26/85.

Dakota Bank & Trust Co; Faro, ND; 50316430001-003; NS; PS; F; 12/26/85.

Dakota Bank & Trust Co; Faro, ND; 50316430001-004; NS; M; F; 12/26/85.

Dakota Bank & Trust Co; Faro, ND; 50316430001-005; NS; PS; F; 12/26/85.

Dakota Bank & Trust Co; Faro, ND; 50316430001-006; NS; M; F; 12/26/85.

Dauphin Deposit Bank & Trust Co; Harrisburg, PA; 50216520001-001; S; PS; F; 10/23/85.

Dauphin Deposit Bank & Trust Co; Harrisburg, PA; 50216520001-002; S; PS; F; 10/23/85.

Dauphin Deposit Bank & Trust Co; Harrisburg, PA; 50216520002-001; S; M; F; 10/23/85.
Dauphin Deposit Bank & Trust Co; Harrisburg, PA; 50216520002-002; S; M; F; 10/23/85.
Deposit Guaranty National Bank; Jackson, MS; 50316820001-001; NS; PS; F; 12/05/85.
Deposit Guaranty National Bank; Jackson, MS; 50216820001-002; S; PS; F; 12/05/85.
Deposit Guaranty National Bank; Jackson, MS; 50316820001-003; NS; M; F; 12/05/85.
Deposit Guaranty National Bank; Jackson, MS; 50216820001-004; S; M; F; 12/05/85.
Dollar Dry Dock Savings Bank; New York, NY; 50216970001-001; P; D; F; 12/24/85.
Dollar Dry Dock Savings Bank; New York, NY; 50216970001-002; P; D; F; 12/24/85.
Dollar Dry Dock Savings Bank; New York, NY; 50316970001-003; NS; D; F; 12/24/85.
Dollar Dry Dock Savings Bank; New York, NY; 50316970001-004; NS; D; F; 12/24/85.
Donaldson Lufkin & Jenrette Securities Corp; New York, NY; 50308710001-001; NS; M; F; 10/30/85.
Donaldson Lufkin & Jenrette Securities Corp; New York, NY; 50308710001-002; NS; PS; F; 10/30/85.
Drexel Burnham Fund; New York, NY; 50263435001-001; P; PS; F; 12/04/85.
Drexel Burnham Fund; New York, NY; 50263435001-002; P; M; F; 12/04/85.
Dubois County Bank; Jasper, IN; 50278084501-001; P; PS; F; 10/07/85.
Dubois County Bank; Jasper, IN; 50378084501-002; NS; PS; F; 10/07/85.
Dubois County Bank; Jasper, IN; 50278084501-003; P; M; F; 10/07/85.
Dubois County Bank; Jasper, IN; 50378084501-004; NS; M; F; 10/07/85.
Dubuque Bank & Trust Co; Dubuque, IA; 50317190001-001; NS; PS; F; 12/16/85.
Dubuque Bank & Trust Co; Dubuque, IA; 50317190001-002; NS; PS; F; 12/16/85.
Dubuque Bank & Trust Co; Dubuque, IA; 50317190001-003; NS; PS; F; 12/16/85.
Dubuque Bank & Trust Co; Dubuque, IA; 50317190001-004; NS; PS; F; 12/16/85.
Dubuque Bank & Trust Co; Dubuque, IA; 50317190002-001; NS; M; F; 12/16/85.
Dubuque Bank & Trust Co; Dubuque, IA; 50317190002-002; NS; M; F; 12/16/85.
Dubuque Bank & Trust Co; Dubuque, IA; 50317190002-003; NS; M; F; 12/16/85.
Dubuque Bank & Trust Co; Dubuque, IA; 50317190002-004; NS; M; F; 12/16/85.
E F Hutton & Co Inc; New York, NY; 50317260001-001; NS; M; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50317260001-002; NS; M; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260001-003; S; M; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260001-004; S; M; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50317260001-005; NS; PS; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50317260001-006; NS; PS; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260001-007; S; PS; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260001-008; S; PS; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50317260001-009; NS; T; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50317260001-010; NS; T; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260001-011; S; T; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260001-012; S; T; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260002-001; P; D; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260002-002; P; D; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50317260002-003; NS; D; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50317260002-004; NS; D; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260002-005; P; D; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50317260002-006; NS; D; U; 11/12/85.
E F Hutton & Co Inc; New York, NY; 50217260003-001; P; PS; F; 10/30/85.
E F Hutton & Co Inc; New York, NY; 50217260003-002; P; M; F; 10/30/85.
E F Hutton Trust Co; Wilmington, DE; 50380880001-001; NS; M; F; 10/30/85.
E F Hutton Trust Co; Wilmington, DE; 50280880001-002; P; M; F; 10/30/85.
E F Hutton Trust Co; Wilmington, DE; 50380880001-003; NS; PS; F; 10/23/85.
E F Hutton Trust Co; Wilmington, DE; 50280880001-004; P; PS; F; 10/30/85.
E F Hutton Trust Co; Wilmington, DE; 50380880001-005; NS; T; F; 10/30/85.
E F Hutton Trust Co; Wilmington, DE; 50280880001-006; P; T; F; 10/30/85.
E F Hutton Trust Co; Wilmington, DE; 50380880002-001; NS; D; F; 10/30/85.
E F Hutton Trust Co; Wilmington, DE; 50280880002-002; P; D; F; 10/30/85.
E F Hutton Trust Co; Wilmington, DE; 50280880002-003; P; D; F; 10/30/85.
E F Hutton Trust Co; Wilmington, DE; 50380880002-004; NS; D; F; 10/30/85.
Early American Life Insurance Co; St Paul, MN; 50217300001-001; P; PS; F; 11/15/85.
Early American Life Insurance Co; St Paul, MN; 50217300001-002; P; PS; F; 11/15/85.
Early American Life Insurance Co; St Paul, MN; 50217300001-003; P; M; F; 11/15/85.
Early American Life Insurance Co; St Paul, MN; 50217300001-004; P; M; F; 11/15/85.
Eastern Building Material Dealers Association; Media, PA; 50340460001-001; NS; PS; F; 11/26/85.
Eastern Building Material Dealers Association; Media, PA; 50340460001-002; NS; M; F; 11/26/85.
Eastern Building Material Dealers Association; Media, PA; 50340460002-001; NS; D; F; 12/05/85.
Eastern Building Material Dealers Association; Media, PA; 50340460002-002; NS; D; F; 12/05/85.
Eastern Building Material Dealers Association; Media, PA; 50340460002-003; NS; D; F; 12/05/85.
Eastern Building Material Dealers Association; Media, PA; 50340460002-004; NS; D; F; 12/05/85.
Eastern Building Material Dealers Association; Media, PA; 50340460002-005; NS; D; F; 12/05/85.
Eaton Vance Distributors Inc; Boston, MA; 50376774401-001; NS; D; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50376774401-002; NS; D; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774401-003; P; D; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774401-004; P; D; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774401-005; P; D; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774401-006; P; D; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50376774402-001; NS; PS; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50376774402-002; NS; M; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50376774402-003; NS; T; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50376774402-004; NS; PS; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774402-005; P; PS; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774402-006; P; M; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774402-007; P; T; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774402-008; P; PS; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774402-009; P; M; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774402-010; P; T; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774402-011; P; PS; F; 12/10/85.
Eaton Vance Distributors Inc; Boston, MA; 50276774402-012; P; M; F; 12/10/85.
Elston Bank & Trust Co; Crawfordsville, IN; 50217641801-001; P; M; F; 10/03/85.
Elston Bank & Trust Co; Crawfordsville, IN; 50317641801-002; NS; M; F; 10/03/85.
Elston Bank & Trust Co; Crawfordsville, IN; 50217641801-003; P; PS; F; 10/03/85.
Elston Bank & Trust Co; Crawfordsville, IN; 50317641801-004; NS; PS; F; 10/03/85.
Employers Life Insurance Co of Wausau; Wausau, WI; 50217750001-001; S; PS; U; 11/26/85.
Employers Life Insurance Co of Wausau; Wausau, WI; 50317750001-002; NS; PS; F; 12/05/85.
Employers Life Insurance Co of Wausau; Wausau, WI; 50217750001-003; S; M; U; 11/26/85.
Employers Life Insurance Co of Wausau; Wausau, WI; 50317750001-004; NS; M; F; 12/05/85.
Equitable Bank NA; Baltimore, MD; 50317850001-001; NS; PS; F; 12/26/85.
Equitable Bank NA; Baltimore, MD; 50317850001-002; NS; M; F; 12/26/85.
Equitable Bank NA; Baltimore, MD; 50217850001-003; P; PS; F; 12/26/85.
Equitable Bank NA; Baltimore, MD; 50217850001-004; P; M; F; 12/26/85.
Equitable Securities Corp; Nashville, TN; 50217893501-007; P; PS; U; 10/30/85.
Equitable Securities Corp; Nashville, TN; 50217893501-009; P; M; U; 10/30/85.
Equitec Securities Co; Oakland, CA; 50232700001-001; P; M; F; 10/30/85.
Equitec Securities Co; Oakland, CA; 50232700001-002; P; PS; F; 10/30/85.
Erie Family Life Insurance Co; Erie, PA; 50215660001-001; P; M; F; 10/30/85.
Essexbank of Peabody; Peabody, MA; 50317924401-001; NS; D; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50317924401-002; NS; D; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924401-003; P; D; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924401-004; P; D; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924401-005; P; D; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924401-006; P; D; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50317924402-001; NS; PS; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50317924402-002; NS; M; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50317924402-003; NS; T; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50317924402-004; NS; PS; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924402-005; P; PS; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924402-006; P; M; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924402-007; P; T; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924402-008; P; PS; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924402-009; P; M; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924402-010; P; T; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924402-011; P; PS; F; 12/10/85.
Essexbank of Peabody; Peabody, MA; 50217924402-012; P; M; F; 12/10/85.
Explorer Fund Inc; Valley Forge, PA; 50380265101-001; NS; M; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50280265101-002; P; M; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50280265101-003; P; M; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50380265101-004; NS; PS; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50280265101-005; P; PS; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50280265101-006; P; PS; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50380265102-001; NS; D; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50380265102-002; NS; D; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50280265102-003; P; D; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50280265102-004; P; D; F; 10/09/85.
Explorer Fund Inc; Valley Forge, PA; 50280265102-005; P; D; F; 10/09/85.

Farmers & Merchants Bank; Fort Branch, IN; 50218441801-001; S; M; F; 10/03/85.
Farmers & Merchants Bank; Fort Branch, IN; 50318441801-002; NS; PS; F; 10/03/85.
Farmers & Merchants Bank & Trust Co of Watertown; Watertown, SD; 50218570001-001; S; PS; F; 12/28/85.
Farmers & Merchants Bank & Trust Co of Watertown; Watertown, SD; 50218570001-002; S; PS; F; 12/28/85.
Farmers & Merchants Bank & Trust Co of Watertown; Watertown, SD; 50318570001-003; NS; PS; F; 12/28/85.
Farmers & Merchants Bank & Trust Co of Watertown; Watertown, SD; 50318570001-004; NS; PS; F; 12/28/85.
Farmers & Merchants Bank & Trust Co of Watertown; Watertown, SD; 50218570002-001; S; M; F; 12/28/85.
Farmers & Merchants Bank & Trust Co of Watertown; Watertown, SD; 50218570002-002; S; M; F; 12/28/85.
Farmers & Merchants Bank & Trust Co of Watertown; Watertown, SD; 50318570002-003; NS; M; F; 12/28/85.
Farmers & Merchants Bank & Trust Co of Watertown; Watertown, SD; 50318570002-004; NS; M; F; 12/28/85.
Farmers & Merchants Bank of Preston; Preston, MN; 50218697001-001; S; PS; F; 10/11/85.
Farmers & Merchants Bank of Preston; Preston, MN; 50218697001-002; S; PS; F; 10/11/85.
Farmers & Merchants Bank of Preston; Preston, MN; 50218697001-003; S; M; F; 10/11/85.
Farmers & Merchants Bank of Preston; Preston, MN; 50218697001-004; S; M; F; 10/11/85.
Farmers & Merchants Bank of Preston; Preston, MN; 50318697001-005; NS; PS; F; 10/11/85.
Farmers & Merchants Bank of Preston; Preston, MN; 50318697001-006; NS; PS; F; 10/11/85.
Farmers & Merchants Bank of Preston; Preston, MN; 50318697001-007; NS; M; F; 10/11/85.
Farmers & Merchants Bank of Preston; Preston, MN; 50318697001-008; NS; M; F; 10/11/85.
Farmers Bank; Frankfort, IN; 50218831801-001; S; PS; F; 10/03/85.
Farmers Bank & Trust Co; Wadesville, IN; 50263834501-001; P; PS; F; 10/07/85.
Farmers Bank & Trust Co; Wadesville, IN; 50363834501-002; NS; PS; F; 10/07/85.
Farmers Bank & Trust Co; Wadesville, IN; 50263834501-003; P; M; F; 10/07/85.
Farmers Bank & Trust Co; Wadesville, IN; 50363834501-004; NS; M; F; 10/07/85.
Farmers Loan & Trust Co; Tipton, IN; 50218971801-001; P; M; F; 10/03/85.
Farmers Loan & Trust Co; Tipton, IN; 50218971801-002; P; PS; F; 10/03/85.
Farmers National Bank; Shelbyville, IN; 50219001801-001; S; PS; F; 10/03/85.
Farmers National Bank; Shelbyville, IN; 50319001801-002; NS; PS; F; 10/03/85.
Farmers National Bank; Shelbyville, IN; 50219001801-003; S; M; F; 10/03/85.
Farmers National Bank of Remington; Remington, IN; 50218994501-001; P; PS; F; 10/07/85.
Farmers National Bank of Remington; Remington, IN; 50318994501-002; NS; PS; F; 10/07/85.
Farmers National Bank of Remington; Remington, IN; 50218994501-003; P; M; F; 10/07/85.
Farmers National Bank of Remington; Remington, IN; 50318994501-004; NS; M; F; 10/07/85.
Farmers State Bank; Mentone, IN; 50219151801-001; P; M; F; 10/03/85.
Farmers State Bank; Mentone, IN; 50319151801-002; NS; M; F; 10/03/85.
Farmers State Bank; Mentone, IN; 50219151801-003; P; PS; F; 10/03/85.
Farmers State Bank; Mentone, IN; 50319151801-004; NS; PS; F; 10/03/85.
Farmers State Bank; New London, MN; 50219477002-001; S; PS; F; 10/11/85.
Farmers State Bank; New London, MN; 50219477002-002; S; PS; F; 10/11/85.
Farmers State Bank; New London, MN; 50219477002-003; S; M; F; 10/11/85.
Farmers State Bank; New London, MN; 50219477002-004; S; M; F; 10/11/85.
Farmers State Bank; New London, MN; 50319477002-005; NS; PS; F; 10/11/85.
Farmers State Bank; New London, MN; 50319477002-006; NS; PS; F; 10/11/85.
Farmers State Bank; New London, MN; 50319477002-007; NS; M; F; 10/11/85.
Farmers State Bank; New London, MN; 50319477002-008; NS; M; F; 10/11/85.
Farmers State Bank of Lyle; Lyle, MN; 50219457001-001; S; PS; F; 10/11/85.
Farmers State Bank of Lyle; Lyle, MN; 50219457001-002; S; PS; F; 10/11/85.
Farmers State Bank of Lyle; Lyle, MN; 50219457001-003; S; M; F; 10/11/85.
Farmers State Bank of Lyle; Lyle, MN; 50219457001-004; S; M; F; 10/11/85.
Farmers State Bank of Lyle; Lyle, MN; 50319457001-005; NS; PS; F; 10/11/85.
Farmers State Bank of Lyle; Lyle, MN; 50319457001-006; NS; PS; F; 10/11/85.
Farmers State Bank of Lyle; Lyle, MN; 50319457001-007; NS; M; F; 10/11/85.
Farmers State Bank of Lyle; Lyle, MN; 50319457001-008; NS; M; F; 10/11/85.
Farmers State Bank of Rothsay; Rothsay, MN; 50219267001-001; S; PS; F; 10/11/85.
Farmers State Bank of Rothsay; Rothsay, MN; 50219267001-002; S; PS; F; 10/11/85.
Farmers State Bank of Rothsay; Rothsay, MN; 50219267001-003; S; M; F; 10/11/85.
Farmers State Bank of Rothsay; Rothsay, MN; 50219267001-004; S; M; F; 10/11/85.
Farmers State Bank of Rothsay; Rothsay, MN; 50319267001-005; NS; PS; F; 10/11/85.
Farmers State Bank of Rothsay; Rothsay, MN; 50319267001-006; NS; PS; F; 10/11/85.
Farmers State Bank of Rothsay; Rothsay, MN; 50319267001-007; NS; M; F; 10/11/85.
Farmers State Bank of Rothsay; Rothsay, MN; 50319267001-008; NS; M; F; 10/11/85.
Farmers State Bank of Sullivan; Sullivan, IN; 50219491801-001; P; M; F; 10/03/85.
Farmers State Bank of Sullivan; Sullivan, IN; 50319491801-002; NS; M; F; 10/03/85.
Farmers State Bank of Sullivan; Sullivan, IN; 50219491801-003; P; PS; F; 10/03/85.
Farmers State Bank of Sullivan; Sullivan, IN; 50319491801-004; NS; PS; F; 10/03/85.
Federated Guaranty Life Insurance Co; Montgomery, AL; 50219670001-001; S; M; F; 10/30/85.
Fifth Third Bank; Cincinnati, OH; 50320070001-001; NS; PS; F; 10/23/85.
Fifth Third Bank; Cincinnati, OH; 50320070001-002; NS; M; F; 10/23/85.
Fifth Third Bank; Cincinnati, OH; 50220070001-003; P; PS; F; 10/23/85.
Fifth Third Bank; Cincinnati, OH; 50220070001-004; P; M; F; 10/23/85.
Fifth Third Bank; Cincinnati, OH; 50220070001-005; P; PS; F; 10/23/85.
Fifth Third Bank; Cincinnati, OH; 50220070001-006; P; M; F; 10/23/85.
First & Farmers Bank of Somerset; Somerset, KY; 50273143501-007; P; PS; U; 10/30/85.
First & Farmers Bank of Somerset; Somerset, KY; 50273143501-009; P; M; U; 10/30/85.
First Agricultural Bank of Berkshire County; Pittsfield, MA; 50320210001-001; NS; PS; F; 12/26/85.
First Agricultural Bank of Berkshire County; Pittsfield, MA; 50320210001-002; NS; PS; F; 12/26/85.
First Agricultural Bank of Berkshire County; Pittsfield, MA; 50320210002-001; NS; M; F; 12/26/85.
First Agricultural Bank of Berkshire County; Pittsfield, MA; 50320210002-002; NS; M; F; 12/26/85.
First American Bank NA; Washington, DC; 50320340001-001; NS; PS; F; 12/02/85.
First American Bank NA; Washington, DC; 50320340001-002; NS; M; F; 12/02/85.
First American Bank NA; Washington, DC; 50220340002-001; P; PS; F; 12/02/85.
First American Bank NA; Washington, DC; 50220340002-002; P; M; F; 12/02/85.
First American Bank of Rugby; Rugby, ND; 50213227001-001; S; PS; F; 10/11/85.
First American Bank of Rugby; Rugby, ND; 50213227001-002; S; PS; F; 10/11/85.
First American Bank of Rugby; Rugby, ND; 50213227001-003; S; M; F; 10/11/85.
First American Bank of Rugby; Rugby, ND; 50213227001-004; S; M; F; 10/11/85.
First American Bank of Rugby; Rugby, ND; 50313227001-005; NS; PS; F; 10/11/85.
First American Bank of Rugby; Rugby, ND; 50313227001-006; NS; PS; F; 10/11/85.
First American Bank of Rugby; Rugby, ND; 50313227001-007; NS; M; F; 10/11/85.
First American Bank of Rugby; Rugby, ND; 50313227001-008; NS; M; F; 10/11/85.
First American National Bank; Nashville, TN; 50220433501-007; P; PS; U; 10/30/85.
First American National Bank; Nashville, TN; 50220433501-009; P; M; U; 10/30/85.
First Bank East; St Paul, MN; 50228817001-001; S; PS; F; 10/11/85.
First Bank East; St Paul, MN; 50228817001-002; S; PS; F; 10/11/85.
First Bank East; St Paul, MN; 50228817001-003; S; M; F; 10/11/85.
First Bank East; St Paul, MN; 50228817001-004; S; M; F; 10/11/85.
First Bank East; St Paul, MN; 50328817001-005; NS; PS; F; 10/11/85.
First Bank East; St Paul, MN; 50328817001-006; NS; PS; F; 10/11/85.
First Bank East; St Paul, MN; 50328817001-007; NS; M; F; 10/11/85.
First Bank East; St Paul, MN; 50328817001-008; NS; M; F; 10/11/85.
First Bank Minnesota NA; Virginia, MN; 50226647001-001; S; PS; F; 10/11/85.
First Bank Minnesota NA; Virginia, MN; 50226647001-002; S; PS; F; 10/11/85.
First Bank Minnesota NA; Virginia, MN; 50226647001-003; S; M; F; 10/11/85.
First Bank Minnesota NA; Virginia, MN; 50226647001-004; S; M; F; 10/11/85.
First Bank Minnesota NA; Virginia, MN; 50326647001-005; NS; PS; F; 10/11/85.
First Bank Minnesota NA; Virginia, MN; 50326647001-006; NS; PS; F; 10/11/85.
First Bank Minnesota NA; Virginia, MN; 50326647001-007; NS; M; F; 10/11/85.
First Bank Minnesota NA; Virginia, MN; 50326647001-008; NS; M; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50220727001-001; P; PS; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50220727001-002; P; PS; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50220727001-003; P; M; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50220727001-004; P; M; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50320727001-005; NS; PS; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50320727001-006; NS; PS; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50320727001-007; NS; M; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50320727001-008; NS; M; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50220727002-001; S; D; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50320727002-002; NS; D; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50220727003-001; S; PS; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50220727003-002; S; PS; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50220727003-003; S; M; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50220727003-004; S; M; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50320727003-005; NS; PS; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50320727003-006; NS; PS; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50320727003-007; NS; M; F; 10/11/85.
First Bank NA; Milwaukee, WI; 50320727003-008; NS; M; F; 10/11/85.
First Bank NA-Albert Lea; Albert Lea, MN; 50220797001-001; S; PS; F; 10/11/85.
First Bank NA-Albert Lea; Albert Lea, MN; 50220797001-002; S; PS; F; 10/11/85.
First Bank NA-Albert Lea; Albert Lea, MN; 50220797001-003; S; M; F; 10/11/85.

First Bank NA-Albert Lea; Albert Lea, MN; 50220797001-004; S; M; F; 10/11/85.

First Bank NA-Albert Lea; Albert Lea, MN; 50320797001-005; NS; PS; F; 10/11/85.

First Bank NA-Albert Lea; Albert Lea, MN; 50320797001-006; NS; PS; F; 10/11/85.

First Bank NA-Albert Lea; Albert Lea, MN; 50320797001-007; NS; M; F; 10/11/85.

First Bank NA-Albert Lea; Albert Lea, MN; 50320797001-008; NS; M; F; 10/11/85.

First Bank NA-Billings; Billings, MT; 50220737001-001; S; PS; F; 10/11/85.

First Bank NA-Billings; Billings, MT; 50220737001-002; S; PS; F; 10/11/85.

First Bank NA-Billings; Billings, MT; 50220737001-003; S; M; F; 10/11/85.

First Bank NA-Billings; Billings, MT; 50220737001-004; S; M; F; 10/11/85.

First Bank NA-Billings; Billings, MT; 50320737001-005; NS; PS; F; 10/11/85.

First Bank NA-Billings; Billings, MT; 50320737001-006; NS; PS; F; 10/11/85.

First Bank NA-Billings; Billings, MT; 50320737001-007; NS; M; F; 10/11/85.

First Bank NA-Billings; Billings, MT; 50320737001-008; NS; M; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50220807001-001, P; PS; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50220807001-002; P; PS; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50220807001-003; P; M; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50220807001-004; P; M; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50320807001-005; NS; PS; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50320807001-006; NS; PS; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50320807001-007; NS; M; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50320807001-008; NS; M; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50220807002-001; S; D; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50320807002-002; NS; D; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50220807003-001; S; PS; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50220807003-002; S; PS; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50220807003-003; S; M; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50220807003-004; S; M; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50320807003-005; NS; PS; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50320807003-006; NS; PS; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50320807003-007; NS; M; F; 10/11/85.

First Bank NA-Duluth; Duluth, MN; 50320807003-008; NS; M; F; 10/11/85.

First Bank NA-Lake; Minneapolis, MN; 50222177001-001; S; PS; F; 10/11/85.

First Bank NA-Lake; Minneapolis, MN; 50222177001-002; S; PS; F; 10/11/85.

First Bank NA-Lake; Minneapolis, MN; 50222177001-003; S; M; F; 10/11/85.

First Bank NA-Lake; Minneapolis, MN; 50222177001-004; S; M; F; 10/11/85.

First Bank NA-Lake; Minneapolis, MN; 50322177001-005; NS; PS; F; 10/11/85.

First Bank NA-Lake; Minneapolis, MN; 50322177001-006; NS; PS; F; 10/11/85.

First Bank NA-Lake; Minneapolis, MN; 50322177001-007; NS; M; F; 10/11/85.

First Bank NA-Lake; Minneapolis, MN; 50322177001-008; NS; M; F; 10/11/85.

First Bank NA-Little Falls; Little Falls, MN; 50220817001-001; S; PS; F; 10/11/85.

First Bank NA-Little Falls; Little Falls, MN; 50220817001-002; S; PS; F; 10/11/85.

First Bank NA-Little Falls; Little Falls, MN; 50220817001-003; S; M; F; 10/11/85.

First Bank NA-Little Falls; Little Falls, MN; 50220817001-004; S; M; F; 10/11/85.

First Bank NA-Little Falls; Little Falls, MN; 50320817001-005; NS; PS; F; 10/11/85.

First Bank NA-Little Falls; Little Falls, MN; 50320817001-006; NS; PS; F; 10/11/85.

First Bank NA-Little Falls; Little Falls, MN; 50320817001-007; NS; M; F; 10/11/85.

First Bank NA-Little Falls; Little Falls, MN; 50320817001-008; NS; M; F; 10/11/85.

First Bank NA-Northfield; Northfield, MN; 50220757001-001; S; PS; F; 10/11/85.

First Bank NA-Northfield; Northfield, MN; 50220757001-002; S; PS; F; 10/11/85.

First Bank NA-Northfield; Northfield, MN; 50220757001-003; S; M; F; 10/11/85.

First Bank NA-Northfield; Northfield, MN; 50220757001-004; S; M; F; 10/11/85.

First Bank NA-Northfield; Northfield, MN; 50320757001-005; NS; PS; F; 10/11/85.

First Bank NA-Northfield; Northfield, MN; 50320757001-006; NS; PS; F; 10/11/85.

First Bank NA-Northfield; Northfield, MN; 50320757001-007; NS; M; F; 10/11/85.

First Bank NA-Northfield; Northfield, MN; 50320757001-008; NS; M; F; 10/11/85.

First Bank NA-Southside Missoula; Missoula, MT; 50220827001-001; S; PS; F; 10/11/85.

First Bank NA-Southside Missoula; Missoula, MT; 50220827001-002; S; PS; F; 10/11/85.

First Bank NA-Southside Missoula; Missoula, MT; 50220827001-003; S; M; F; 10/11/85.

First Bank NA-Southside Missoula; Missoula, MT; 50220827001-004; S; M; F; 10/11/85.

First Bank NA-Southside Missoula; Missoula, MT; 50320827001-005; NS; PS; F; 10/11/85.

First Bank NA-Southside Missoula; Missoula, MT; 50320827001-006; NS; PS; F; 10/11/85.

First Bank NA-Southside Missoula; Missoula, MT; 50320827001-007; NS; M; F; 10/11/85.

First Bank NA-Southside Missoula; Missoula, MT; 50320827001-008; NS; M; F; 10/11/85.

First Bank NA-St Cloud; St Cloud, MN; 50220777001-001; S; PS; F; 10/11/85.

First Bank NA-St Cloud; St Cloud, MN; 50220777001-002; S; PS; F; 10/11/85.

First Bank NA-St Cloud; St Cloud, MN; 50220777001-003; S; M; F; 10/11/85.

First Bank NA-St Cloud; St Cloud, MN; 50220777001-004; S; M; F; 10/11/85.

First Bank NA-St Cloud; St Cloud, MN; 50320777001-005; NS; PS; F; 10/11/85.

First Bank NA-St Cloud; St Cloud, MN; 50320777001-006; NS; PS; F; 10/11/85.

First Bank NA-St Cloud; St Cloud, MN; 50320777001-007; NS; M; F; 10/11/85.

First Bank NA-St Cloud; St Cloud, MN; 50320777001-008; NS; M; F; 10/11/85.

First Bank NA-Western Montana Missoula; Missoula, MT; 50236077001-001; S; PS; F; 10/11/85.

First Bank NA-Western Montana Missoula; Missoula, MT; 50236077001-002; S; PS; F; 10/11/85.

First Bank NA-Western Montana Missoula; Missoula, MT; 50236077001-003; S; M; F; 10/11/85.

First Bank NA-Western Montana Missoula; Missoula, MT; 50236077001-004; S; M; F; 10/11/85.

First Bank NA-Western Montana Missoula; Missoula, MT; 50336077001-005; NS; PS; F; 10/11/85.

First Bank NA-Western Montana Missoula; Missoula, MT; 50336077001-006; NS; PS; F; 10/11/85.

First Bank NA-Western Montana Missoula; Missoula, MT; 50336077001-007; NS; M; F; 10/11/85.

First Bank NA-Western Montana Missoula; Missoula, MT; 50336077001-008; NS; M; F; 10/11/85.

First Bank of Langdon; Langdon, ND; 50221017001-001; S; PS; F; 10/11/85.

First Bank of Langdon; Langdon, ND; 50221017001-002; S; PS; F; 10/11/85.

First Bank of Langdon; Langdon, ND; 50221017001-003; S; M; F; 10/11/85.

First Bank of Langdon; Langdon, ND; 50221017001-004; S; M; F; 10/11/85.

First Bank of Langdon; Langdon, ND; 50321017001-005; NS; PS; F; 10/11/85.

First Bank of Langdon; Langdon, ND; 50321017001-006; NS; PS; F; 10/11/85.

First Bank of Langdon; Langdon, ND; 50321017001-007; NS; M; F; 10/11/85.

First Bank of Langdon; Langdon, ND; 50321017001-008; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Fargo; Fargo, ND; 50221077001-001; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Fargo; Fargo, ND; 50221077001-002; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Fargo; Fargo, ND; 50221077001-003; S; M; F; 10/11/85.

First Bank of North Dakota NA-Fargo; Fargo, ND; 50221077001-004; S; M; F; 10/11/85.

First Bank of North Dakota NA-Fargo; Fargo, ND; 50321077001-005; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Fargo; Fargo, ND; 50321077001-006; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Fargo; Fargo, ND; 50321077001-007; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Fargo; Fargo, ND; 50321077001-008; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Grand Forks; Grand Forks, ND; 50221097001-001; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Grand Forks; Grand Forks, ND; 50221097001-002; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Grand Forks; Grand Forks, ND; 50221097001-003; S; M; F; 10/11/85.

First Bank of North Dakota NA-Grand Forks; Grand Forks, ND; 50221097001-004; S; M; F; 10/11/85.

First Bank of North Dakota NA-Grand Forks; Grand Forks, ND; 50321097001-005; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Grand Forks; Grand Forks, ND; 50321097001-006; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Grand Forks; Grand Forks, ND; 50321097001-007; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Grand Forks; Grand Forks, ND; 50321097001-008; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Jamestown; Jamestown, ND; 50221067001-001; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Jamestown; Jamestown, ND; 50221067001-002; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Jamestown; Jamestown, ND; 50221067001-003; S; M; F; 10/11/85.

First Bank of North Dakota NA-Jamestown; Jamestown, ND; 50221067001-004; S; M; F; 10/11/85.

First Bank of North Dakota NA-Jamestown; Jamestown, ND; 50321067001-005; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Jamestown; Jamestown, ND; 50321067001-006; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Jamestown; Jamestown, ND; 50321067001-007; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Jamestown; Jamestown, ND; 50321067001-008; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Minot; Minot, ND; 50221087001-001; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Minot; Minot, ND; 50221087001-002; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Minot; Minot, ND; 50221087001-003; S; M; F; 10/11/85.

First Bank of North Dakota NA-Minot; Minot, ND; 50221087001-004; S; M; F; 10/11/85.

First Bank of North Dakota NA-Minot; Minot, ND; 50321087001-005; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Minot; Minot, ND; 50321087001-006; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Minot; Minot, ND; 50321087001-007; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Minot; Minot, ND; 50321087001-008; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Wahpeton; Wahpeton, ND; 50221057001-001; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Wahpeton; Wahpeton, ND; 50221057001-002; S; PS; F; 10/11/85.

First Bank of North Dakota NA-Wahpeton; Wahpeton, ND; 50221057001-003; S; M; F; 10/11/85.

First Bank of North Dakota NA-Wahpeton; Wahpeton, ND; 50221057001-004; S; M; F; 10/11/85.

First Bank of North Dakota NA-Wahpeton; Wahpeton, ND; 50321057001-005; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Wahpeton; Wahpeton, ND; 50321057001-006; NS; PS; F; 10/11/85.

First Bank of North Dakota NA-Wahpeton; Wahpeton, ND; 50321057001-007; NS; M; F; 10/11/85.

First Bank of North Dakota NA-Wahpeton; Wahpeton, ND; 50321057001-008; NS; M; F; 10/11/85.

First Bank of Rolla; Rolla, ND; 50220487001-001; S; PS; F; 10/11/85.

First Bank of Rolla; Rolla, ND; 50220487001-002; S; PS; F; 10/11/85.

First Bank of Rolla; Rolla, ND; 50220487001-003; S; M; F; 10/11/85.

First Bank of Rolla; Rolla, ND; 50220487001-004; S; M; F; 10/11/85.

First Bank of Rolla; Rolla, ND; 50320487001-005; NS; PS; F; 10/11/85.
First Bank of Rolla; Rolla, ND; 50320487001-006; NS; PS; F; 10/11/85.
First Bank of Rolla; Rolla, ND; 50320487001-007; NS; M; F; 10/11/85.
First Bank of Rolla; Rolla, ND; 50320487001-008; NS; M; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50221997001-001; P; PS; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50221997001-002; P; PS; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50221997001-003; P; M; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50221997001-004; P; M; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50321997001-005; NS; PS; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50321997001-006; NS; PS; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50321997001-007; NS; M; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50321997001-008; NS; M; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50221997002-001; S; D; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50321997002-002; NS; D; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50221997003-001; S; PS; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50221997003-002; S; PS; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50221997003-003; S; M; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50221997003-004; S; M; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50321997003-005; NS; PS; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50321997003-006; NS; PS; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50321997003-007; NS; M; F; 10/11/85.
First Bank of South Dakota NA; Sioux Falls, SD; 50321997003-008; NS; M; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50270447001-001; P; PS; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50270447001-002; P; PS; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50270447001-003; P; M; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50270447001-004; P; M; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50370447001-005; NS; PS; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50370447001-006; NS; PS; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50370447001-007; NS; M; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50370447001-008; NS; M; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50270447002-001; S; D; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50370447002-002; NS; D; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50270447003-001; S; PS; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50270447003-002; S; PS; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50270447003-003; S; M; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50270447003-004; S; M; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50370447003-005; NS; PS; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50370447003-006; NS; PS; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50370447003-007; NS; M; F; 10/11/85.
First Bank System Inc; Minneapolis, MN; 50370447003-008; NS; M; F; 10/11/85.
First Bank West-Billings; Billings, MT; 50236187001-001; S; PS; F; 10/11/85.
First Bank West-Billings; Billings, MT; 50236187001-002; S; PS; F; 10/11/85.
First Bank West-Billings; Billings, MT; 50236187001-003; S; M; F; 10/11/85.
First Bank West-Billings; Billings, MT; 50236187001-004; S; M; F; 10/11/85.
First Bank West-Billings; Billings, MT; 50336187001-005; NS; PS; F; 10/11/85.
First Bank West-Billings; Billings, MT; 50336187001-006; NS; PS; F; 10/11/85.
First Bank West-Billings; Billings, MT; 50336187001-007; NS; M; F; 10/11/85.
First Bank West-Billings; Billings, MT; 50336187001-008; NS; M; F; 10/11/85.
First Citizens Bank & Trust Co; Raleigh, NC; 50346680001-001; NS; PS; F; 12/28/85.
First Citizens Bank & Trust Co; Raleigh, NC; 50346680001-002; NS; M; F; 12/19/85.
First City Bank & Trust Co; Hopkinsville, KY; 50273183501-007; P; PS; U; 10/30/85.
First City Bank & Trust Co; Hopkinsville, KY; 50273183501-009; P; M; U; 10/30/85.
First Columbus National Bank; Columbus, MS; 50221473501-007; P; PS; U; 10/30/85.
First Columbus National Bank; Columbus, MS; 50221473501-009; P; M; U; 10/30/85.
First Continental Bank & Trust; Overland Park, KS; 50321523401-001; NS; PS; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50321523401-002; NS; PS; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50321523401-003; NS; PS; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50321523401-004; NS; PS; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523401-005; P; PS; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50321523401-006; NS; M; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50321523401-007; NS; M; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50321523401-008; NS; M; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50321523401-009; NS; M; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523401-010; P; M; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523401-011; P; PS; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523401-012; P; M; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523401-013; S; M; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523401-014; S; PS; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523401-015; S; PS; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523401-016; S; M; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50321523402-001; NS; D; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50321523402-002; NS; D; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523402-003; S; D; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523402-004; S; D; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523402-005; S; D; F; 10/07/85.
First Continental Bank & Trust; Overland Park, KS; 50221523402-006; S; D; F; 10/07/85.
First Edina National Bank; Edina, MN; 50221567001-001; S; PS; F; 10/11/85.
First Edina National Bank; Edina, MN; 50221567001-002; S; PS; F; 10/11/85.
First Edina National Bank; Edina, MN; 50221567001-003; S; M; F; 10/11/85.
First Edina National Bank; Edina, MN; 50221567001-004; S; M; F; 10/11/85.
First Edina National Bank; Edina, MN; 50321567001-005; NS; PS; F; 10/11/85.
First Edina National Bank; Edina, MN; 50321567001-006; NS; PS; F; 10/11/85.
First Edina National Bank; Edina, MN; 50321567001-007; NS; M; F; 10/11/85.
First Edina National Bank; Edina, MN; 50321567001-008; NS; M; F; 10/11/85.
First Fidelity Bank NA New Jersey; Newark, NJ; 50226960002-001; S; PS; F; 11/26/85.
First Fidelity Bank NA New Jersey; Newark, NJ; 50226960002-002; S; M; F; 11/26/85.
First Grand Avenue State Bank of St Paul; St Paul, MN; 50221837001-001; S; PS; F; 10/11/85.
First Grand Avenue State Bank of St Paul; St Paul, MN; 50221837001-002; S; PS; F; 10/11/85.
First Grand Avenue State Bank of St Paul; St Paul, MN; 50221837001-003; S; M; F; 10/11/85.
First Grand Avenue State Bank of St Paul; St Paul, MN; 50221837001-004; S; M; F; 10/11/85.
First Grand Avenue State Bank of St Paul; St Paul, MN; 50321837001-005; NS; PS; F; 10/11/85.
First Grand Avenue State Bank of St Paul; St Paul, MN; 50321837001-006; NS; PS; F; 10/11/85.
First Grand Avenue State Bank of St Paul; St Paul, MN; 50321837001-007; NS; M; F; 10/11/85.
First Grand Avenue State Bank of St Paul; St Paul, MN; 50321837001-008; NS; M; F; 10/11/85.
First Hardin National Bank & Trust; Elizabethtown, KY; 50221871801-001; P; M; F; 10/03/85.
First Hardin National Bank & Trust; Elizabethtown, KY; 50321871801-002; NS; M; F; 10/03/85.
First Hardin National Bank & Trust; Elizabethtown, KY; 50221871801-003; P; PS; F; 10/03/85.
First Hardin National Bank & Trust; Elizabethtown, KY; 50321871801-004; NS; PS; F; 10/03/85.
First Interstate Bank of Arizona NA; Phoenix, AZ; 50327260001-003; NS; PS; U; 11/14/85.
First Interstate Bank of Arizona NA; Phoenix, AZ; 50327260001-004; NS; M; U; 11/14/85.
First Interstate Bank of Billings NA; Billings, MT; 50375852201-001; NS; PS; F; 12/04/85.
First Interstate Bank of Billings NA; Billings, MT; 50375852201-002; NS; M; F; 12/04/85.
First Interstate Bank of Billings NA; Billings, MT; 50375852201-003; NS; PS; F; 12/04/85.
First Interstate Bank of Nevada NA; Reno, NV; 50225790001-001; S; PS; F; 11/26/85.
First Knox National Bank; Mount Vernon, OH; 50271970001-001; P; PS; F; 12/16/85.
First Knox National Bank; Mount Vernon, OH; 50371970001-002; NS; PS; F; 12/16/85.
First Knox National Bank; Mount Vernon, OH; 50271970001-003; P; M; F; 12/16/85.
First Knox National Bank; Mount Vernon, OH; 50371970001-004; NS; M; F; 12/16/85.
First Midwest Bank Danville; Danville, IL; 50250611801-001; P; M; F; 10/03/85.
First Midwest Bank Danville; Danville, IL; 50350611801-002; NS; M; F; 10/03/85.
First Midwest Bank Danville; Danville, IL; 50250611801-003; P; PS; F; 10/03/85.
First Midwest Bank Danville; Danville, IL; 50350611801-004; NS; PS; F; 10/03/85.
First Midwest Bank Moline; Moline, IL; 50240961801-001; P; M; F; 10/03/85.
First Midwest Bank Moline; Moline, IL; 50340961801-002; NS; M; F; 10/03/85.
First Midwest Bank Moline; Moline, IL; 50240961801-003; P; PS; F; 10/03/85.
First Midwest Bank Moline; Moline, IL; 50340961801-004; NS; PS; F; 10/03/85.
First Mississippi National Bank; Hattiesburg, MS; 50222190001-001; P; PS; F; 10/30/85.
First Mississippi National Bank; Hattiesburg, MS; 50322190001-002; NS; PS; F; 10/30/85.
First Mississippi National Bank; Hattiesburg, MS; 50222190001-003; P; M; F; 10/30/85.
First Mississippi National Bank; Hattiesburg, MS; 50322190001-004; NS; M; F; 10/30/85.
First National Bank; Bozeman, MT; 50224317001-001; S; PS; F; 10/11/85.
First National Bank; Bozeman, MT; 50224317001-002; S; PS; F; 10/11/85.
First National Bank; Bozeman, MT; 50224317001-003; S; M; F; 10/11/85.
First National Bank; Bozeman, MT; 50224317001-004; S; M; F; 10/11/85.
First National Bank; Bozeman, MT; 50324317001-005; NS; PS; F; 10/11/85.
First National Bank; Bozeman, MT; 50324317001-006; NS; PS; F; 10/11/85.
First National Bank; Bozeman, MT; 50324317001-007; NS; M; F; 10/11/85.
First National Bank; Bozeman, MT; 50324317001-008; NS; M; F; 10/11/85.
First National Bank; Plainview, MN; 50226097001-001; S; PS; U; 10/31/85.
First National Bank; Plainview, MN; 50226097001-002; S; PS; U; 10/31/85.
First National Bank; Plainview, MN; 50226097001-003; S; M; U; 10/31/85.

First National Bank; Plainview, MN; 50226097001-004; S; M; U; 10/31/85.

First National Bank; Plainview, MN; 50326097001-005; NS; PS; U; 10/31/85.

First National Bank; Plainview, MN; 50326097001-006; NS; PS; U; 10/31/85.

First National Bank; Plainview, MN; 50326097001-007; NS; M; U; 10/31/85.

First National Bank; Plainview, MN; 50326097001-008; NS; M; U; 10/31/85.

First National Bank; Spring Valley, MN; 50222537001-001; S; PS; F; 10/11/85.

First National Bank; Spring Valley, MN; 50222537001-002; S; PS; F; 10/11/85.

First National Bank; Spring Valley, MN; 50222537001-003; S; M; F; 10/11/85.

First National Bank; Spring Valley, MN; 50222537001-004; S; M; F; 10/11/85.

First National Bank; Spring Valley, MN; 50322537001-005; NS; PS; F; 10/11/85.

First National Bank; Spring Valley, MN; 50322537001-006; NS; PS; F; 10/11/85.

First National Bank; Spring Valley, MN; 50322537001-007; NS; M; F; 10/11/85.

First National Bank; Spring Valley, MN; 50322537001-008; NS; M; F; 10/11/85.

First National Bank & Trust Co; Crawfordsville, IN; 50223331801-001; P; M; F; 10/03/85.

First National Bank & Trust Co; Crawfordsville, IN; 50223331801-002; P; PS; F; 10/03/85.

First National Bank & Trust Co; Escanaba, MI; 50223071801-001; P; M; F; 10/03/85.

First National Bank & Trust Co; Escanaba, MI; 50323071801-002; NS; M; F; 10/03/85.

First National Bank & Trust Co; Escanaba, MI; 50223071801-003; P; PS; F; 10/03/85.

First National Bank & Trust Co; Escanaba, MI; 50323071801-004; NS; PS; F; 10/03/85.

First National Bank & Trust Co; Marquette, MI; 50223081801-001; P; M; F; 10/03/85.

First National Bank & Trust Co; Marquette, MI; 50323081801-002; NS; M; F; 10/03/85.

First National Bank & Trust Co; Marquette, MI; 50223081801-003; P; PS; F; 10/03/85.

First National Bank & Trust Co; Marquette, MI; 50323081801-004; NS; PS; F; 10/03/85.

First National Bank & Trust Co; Menominee, MI; 50227401801-001; P; M; F; 10/03/85.

First National Bank & Trust Co; Menominee, MI; 50327401801-002; NS; M; F; 10/03/85.

First National Bank & Trust Co; Menominee, MI; 50227401801-003; P; PS; F; 10/03/85.

First National Bank & Trust Co; Menominee, MI; 50327401801-004; NS; PS; F; 10/03/85.

First National Bank & Trust Co of Bismarck; Bismarck, ND; 50227117001-001; S; PS; F; 10/11/85.

First National Bank & Trust Co of Bismarck; Bismarck, ND; 50227117001-002; S; PS; F; 10/11/85.

First National Bank & Trust Co of Bismarck; Bismarck, ND; 50227117001-003; S; M; F; 10/11/85.

First National Bank & Trust Co of Bismarck; Bismarck, ND; 50227117001-004; S; M; F; 10/11/85.

First National Bank & Trust Co of Bismarck; Bismarck, ND; 50327117001-005; NS; PS; F; 10/11/85.

First National Bank & Trust Co of Bismarck; Bismarck, ND; 50327117001-006; NS; PS; F; 10/11/85.

First National Bank & Trust Co of Bismarck; Bismarck, ND; 50327117001-007; NS; M; F; 10/11/85.

First National Bank & Trust Co of Bismarck; Bismarck, ND; 50327117001-008; NS; M; F; 10/11/85.

First National Bank & Trust Co of Helena; Helena, MT; 50223287001-001; S; PS; F; 10/11/85.

First National Bank & Trust Co of Helena; Helena, MT; 50223287001-002; S; PS; F; 10/11/85.

First National Bank & Trust Co of Helena; Helena, MT; 50223287001-003; S; M; F; 10/11/85.

First National Bank & Trust Co of Helena; Helena, MT; 50223287001-004; S; M; F; 10/11/85.

First National Bank & Trust Co of Helena; Helena, MT; 50323287001-005; NS; PS; F; 10/11/85.

First National Bank & Trust Co of Helena; Helena, MT; 50323287001-006; NS; PS; F; 10/11/85.

First National Bank & Trust Co of Helena; Helena, MT; 50323287001-007; NS; M; F; 10/11/85.

First National Bank & Trust Co of Helena; Helena, MT; 50323287001-008; NS; M; F; 10/11/85.

First National Bank & Trust Co of Lincoln; Lincoln, NE; 50323210001-001; NS; PS; F; 10/23/85.

First National Bank & Trust Co of Lincoln; Lincoln, NE; 50323210001-002; NS; PS; F; 10/23/85.

First National Bank & Trust Co of Lincoln; Lincoln, NE; 50323210001-003; NS; M; F; 10/23/85.

First National Bank & Trust Co of Lincoln; Lincoln, NE; 50323210001-004; NS; M; F; 10/23/85.

First National Bank & Trust Co of Lincoln; Lincoln, NE; 50223210001-005; S; PS; F; 10/23/85.

First National Bank & Trust Co of Lincoln; Lincoln, NE; 50223210001-006; S; M; F; 10/23/85.

First National Bank & Trust Co of Lincoln; Lincoln, NE; 50223210001-007; S; PS; F; 10/23/85.

First National Bank & Trust Co of Lincoln; Lincoln, NE; 50223210001-008; S; M; F; 10/23/85.

First National Bank & Trust Co of Newtown; Newtown, PA; 50323050001-001; NS; M; F; 12/05/85.

First National Bank & Trust Co of Newtown; Newtown, PA; 50223050001-002; S; M; F; 12/05/85.

First National Bank & Trust Co of Newtown; Newtown, PA; 50323050002-001; NS; PS; F; 12/05/85.

First National Bank & Trust Co of Newtown; Newtown, PA; 50223050002-002; S; PS; F; 12/05/85.

First National Bank in Alexandria; Alexandria, MN; 50224047001-001; S; PS; F; 10/11/85.

First National Bank in Alexandria; Alexandria, MN; 50224047001-002; S; PS; F; 10/11/85.

First National Bank in Alexandria; Alexandria, MN; 50224047001-003; S; M; F; 10/11/85.

First National Bank in Alexandria; Alexandria, MN; 50224047001-004; S; M; F; 10/11/85.

First National Bank in Alexandria; Alexandria, MN; 50324047001-005; NS; PS; F; 10/11/85.

First National Bank in Alexandria; Alexandria, MN; 50324047001-006; NS; PS; F; 10/11/85.

First National Bank in Alexandria; Alexandria, MN; 50324047001-007; NS; M; F; 10/11/85.

First National Bank in Alexandria; Alexandria, MN; 50324047001-008; NS; M; F; 10/11/85.

First National Bank in Havre; Havre, MT; 50223657001-001; S; PS; F; 10/11/85.

First National Bank in Havre; Havre, MT; 50223657001-002; S; PS; F; 10/11/85.

First National Bank in Havre; Havre, MT; 50223657001-003; S; M; F; 10/11/85.

First National Bank in Havre; Havre, MT; 50223657001-004; S; M; F; 10/11/85.

First National Bank in Havre; Havre, MT; 50323657001-005; NS; PS; F; 10/11/85.

First National Bank in Havre; Havre, MT; 50323657001-006; NS; PS; F; 10/11/85.

First National Bank in Havre; Havre, MT; 50323657001-007; NS; M; F; 10/11/85.

First National Bank in Havre; Havre, MT; 50323657001-008; NS; M; F; 10/11/85.

First National Bank in Lidgerwood; Lidgerwood, ND; 50223667001-001; S; PS; F; 10/11/85.

First National Bank in Lidgerwood; Lidgerwood, ND; 50223667001-002; S; PS; F; 10/11/85.

First National Bank in Lidgerwood; Lidgerwood, ND; 50223667001-003; S; M; F; 10/11/85.

First National Bank in Lidgerwood; Lidgerwood, ND; 50223667001-004; S; M; F; 10/11/85.

First National Bank in Lidgerwood; Lidgerwood, ND; 50323667001-005; NS; PS; F; 10/11/85.

First National Bank in Lidgerwood; Lidgerwood, ND; 50323667001-006; NS; PS; F; 10/11/85.

First National Bank in Lidgerwood; Lidgerwood, ND; 50323667001-007; NS; M; F; 10/11/85.

First National Bank in Lidgerwood; Lidgerwood, ND; 50323667001-008; NS; M; F; 10/11/85.

First National Bank in Marion; Marion, IN; 50223701801-001; P; M; F; 10/03/85.

First National Bank in Marion; Marion, IN; 50323701801-002; NS; M; F; 10/03/85.

First National Bank in Marion; Marion, IN; 50223701801-003; P; PS; F; 10/03/85.

First National Bank in Marion; Marion, IN; 50323701801-004; NS; PS; F; 10/03/85.

First National Bank in Miles City; Miles City, MT; 50228157001-001; S; PS; F; 10/11/85.

First National Bank in Miles City; Miles City, MT; 50228157001-002; S; PS; F; 10/11/85.

First National Bank in Miles City; Miles City, MT; 50228157001-003; S; M; F; 10/11/85.

First National Bank in Miles City; Miles City, MT; 50228157001-004; S; M; F; 10/11/85.

First National Bank in Miles City; Miles City, MT; 50328157001-005; NS; PS; F; 10/11/85.

First National Bank in Miles City; Miles City, MT; 50328157001-006; NS; PS; F; 10/11/85.

First National Bank in Miles City; Miles City, MT; 50328157001-007; NS; M; F; 10/11/85.

First National Bank in Miles City; Miles City, MT; 50328157001-008; NS; M; F; 10/11/85.

First National Bank in Sioux Falls; Sioux Falls, SD; 50323790001-001; NS; PS; F; 10/30/85.

First National Bank in Sioux Falls; Sioux Falls, SD; 50323790001-002; NS; M; F; 10/30/85.

First National Bank in Sioux Falls; Sioux Falls, SD; 50223790001-003; P; PS; F; 10/30/85.

First National Bank in Sioux Falls; Sioux Falls, SD; 50223790001-004; P; M; F; 10/30/85.

First National Bank in Wabash; Wabash, IN; 50223831801-001; P; M; F; 10/03/85.

First National Bank in Wabash; Wabash, IN; 50323831801-002; NS; M; F; 10/03/85.

First National Bank in Wabash; Wabash, IN; 50223831801-003; P; PS; F; 10/03/85.

First National Bank in Wabash; Wabash, IN; 50323831801-004; NS; PS; F; 10/03/85.

First National Bank in Worthington; Worthington, MN; 50223387001-001; S; PS; F; 10/11/85.

First National Bank in Worthington; Worthington, MN; 50223387001-002; S; PS; F; 10/11/85.

First National Bank in Worthington; Worthington, MN; 50223387001-003; S; M; F; 10/11/85.

First National Bank in Worthington; Worthington, MN; 50223387001-004; S; M; F; 10/11/85.

First National Bank in Worthington; Worthington, MN; 50323387001-005; NS; PS; F; 10/11/85.

First National Bank in Worthington; Worthington, MN; 50323387001-006; NS; PS; F; 10/11/85.

First National Bank in Worthington; Worthington, MN; 50323387001-007; NS; M; F; 10/11/85.

First National Bank in Worthington; Worthington, MN; 50323387001-008; NS; M; F; 10/11/85

First National Bank of Atlanta; Atlanta, GA; 50324170001-001; NS; PS; F; 10/22/85.

First National Bank of Atlanta; Atlanta, GA; 50324170001-002; NS; PS; F; 10/22/85.

First National Bank of Atlanta; Atlanta, GA; 50224170001-003; S; PS; F; 10/22/85.

First National Bank of Atlanta; Atlanta, GA; 50324170001-004; NS; M; F; 10/22/85.

First National Bank of Atlanta; Atlanta, GA; 50324170001-005; NS; M; F; 10/22/85.

First National Bank of Austin; Austin, MN; 50256007001-001; S; PS; F; 10/11/85.

First National Bank of Austin; Austin, MN; 50256007001-002; S; PS; F; 10/11/85.

First National Bank of Austin; Austin, MN; 50256007001-003; S; M; F; 10/11/85.

First National Bank of Austin; Austin, MN; 50256007001-004; S; M; F; 10/11/85.

First National Bank of Austin; Austin, MN; 50356007001-005; NS; PS; F; 10/11/85.

First National Bank of Austin; Austin, MN; 50356007001-006; NS; PS; F; 10/11/85.

First National Bank of Austin; Austin, MN; 50356007001-007; NS; M; F; 10/11/85.

First National Bank of Austin; Austin, MN; 50356007001-008; NS; M; F; 10/11/85.

First National Bank of Baudette; Baudette, MN; 50224217001-001; S; PS; F; 10/11/85.

First National Bank of Baudette; Baudette, MN; 50224217001-002; S; PS; F; 10/11/85.

First National Bank of Baudette; Baudette, MN; 50224217001-003; S; M; F; 10/11/85.

First National Bank of Baudette; Baudette, MN; 50224217001-004; S; M; F; 10/11/85.

First National Bank of Baudette; Baudette, MN; 50324217001-005; NS; PS; F; 10/11/85.

First National Bank of Baudette; Baudette, MN; 50324217001-006; NS; PS; F; 10/11/85.

First National Bank of Baudette; Baudette, MN; 50324217001-007; NS; M; F; 10/11/85.

First National Bank of Baudette; Baudette, MN; 50324217001-008; NS; M; F; 10/11/85.

First National Bank of Bloomington; Bloomington, IN; 50224281801-001; P; M; F; 10/03/85.

First National Bank of Bloomington; Bloomington, IN; 50224281801-002; P; PS; F; 10/03/85.

First National Bank of Bloomington; Bloomington, IN; 50224281801-003; P; T; F; 10/03/85.

First National Bank of Blue Earth; Blue Earth, MN; 50206227001-001; S; PS; F; 10/11/85.

First National Bank of Blue Earth; Blue Earth, MN; 50206227001-002; S; PS; F; 10/11/85.

First National Bank of Blue Earth; Blue Earth, MN; 50206227001-003; S; M; F; 10/11/85.

First National Bank of Blue Earth; Blue Earth, MN; 50206227001-004; S; M; F; 10/11/85.

First National Bank of Blue Earth; Blue Earth, MN; 50306227001-005; NS; PS; F; 10/11/85.

First National Bank of Blue Earth; Blue Earth, MN; 50306227001-006; NS; PS; F; 10/11/85.

First National Bank of Blue Earth; Blue Earth, MN; 50306227001-007; NS; M; F; 10/11/85.

First National Bank of Blue Earth; Blue Earth, MN; 50306227001-008; NS; M; F; 10/11/85.

First National Bank of Bluefield; Bluefield, WV; 50227614501-001; P; PS; F; 10/07/85.

First National Bank of Bluefield; Bluefield, WV; 50327614501-002; NS; PS; F; 10/07/85.

First National Bank of Bluefield; Bluefield, WV; 50227614501-003; P; M; F; 10/07/85.

First National Bank of Bluefield; Bluefield, WV; 50327614501-004; NS; M; F; 10/07/85.

First National Bank of Brainerd; Brainerd, MN; 50224327002-001; S; PS; F; 10/11/85.

First National Bank of Brainerd; Brainerd, MN; 50224327002-002; S; PS; F; 10/11/85.

First National Bank of Brainerd; Brainerd, MN; 50224327002-003; S; M; F; 10/11/85.

First National Bank of Brainerd; Brainerd, MN; 50224327002-004; S; M; F; 10/11/85.

First National Bank of Brainerd; Brainerd, MN; 50324327002-005; NS; PS; F; 10/11/85.

First National Bank of Brainerd; Brainerd, MN; 50324327002-006; NS; PS; F; 10/11/85.

First National Bank of Brainerd; Brainerd, MN; 50324327002-007; NS; M; F; 10/11/85.

First National Bank of Brainerd; Brainerd, MN; 50324327002-008; NS; M; F; 10/11/85.

First National Bank of Burnsville; Burnsville, MN; 50222617001-001; S; PS; F; 10/11/85.

First National Bank of Burnsville; Burnsville, MN; 50222617001-002; S; PS; F; 10/11/85.

First National Bank of Burnsville; Burnsville, MN; 50222617001-003; S; M; F; 10/11/85.

First National Bank of Burnsville; Burnsville, MN; 50222617001-004; S; M; F; 10/11/85.

First National Bank of Burnsville; Burnsville, MN; 50322617001-005; NS; PS; F; 10/11/85.

First National Bank of Burnsville; Burnsville, MN; 50322617001-006; NS; PS; F; 10/11/85.

First National Bank of Burnsville; Burnsville, MN; 50322617001-007; NS; M; F; 10/11/85.

First National Bank of Burnsville; Burnsville, MN; 50322617001-008; NS; M; F; 10/11/85.

First National Bank of Cloquet; Cloquet, MN; 50224517001-001; S; PS; F; 10/11/85.

First National Bank of Cloquet; Cloquet, MN; 50224517001-002; S; PS; F; 10/11/85.

First National Bank of Cloquet; Cloquet, MN; 50224517001-003; S; M; F; 10/11/85.

First National Bank of Cloquet; Cloquet, MN; 50224517001-004; S; M; F; 10/11/85.

First National Bank of Cloquet; Cloquet, MN; 50324517001-005; NS; PS; F; 10/11/85.

First National Bank of Cloquet; Cloquet, MN; 50324517001-006; NS; PS; F; 10/11/85.

First National Bank of Cloquet; Cloquet, MN; 50324517001-007; NS; M; F; 10/11/85.

First National Bank of Cloquet; Cloquet, MN; 50324517001-008; NS; M; F; 10/11/85.

First National Bank of Cloverdale; Cloverdale, IN; 50223961801-001; S; M; F; 10/03/85.

First National Bank of Cloverdale; Cloverdale, IN; 50323961801-002; NS; M; F; 10/03/85.

First National Bank of Columbus; Columbus, IN; 50226541801-001; P; M; F; 10/03/85.

First National Bank of Columbus; Columbus, IN; 50226541801-002; P; PS; F; 10/03/85.

First National Bank of Dubuque; Dubuque, IA; 50324730001-001; NS; PS; F; 12/13/85.

First National Bank of Dubuque; Dubuque, IA; 50324730001-002; NS; PS; F; 12/13/85.

First National Bank of Dubuque; Dubuque, IA; 50324730001-003; NS; PS; F; 12/13/85.

First National Bank of Dubuque; Dubuque, IA; 50324730001-004; NS; PS; F; 12/13/85.

First National Bank of Dubuque; Dubuque, IA; 50324730002-001; NS; M; F; 12/13/85.

First National Bank of Dubuque; Dubuque, IA; 50324730002-002; NS; M; F; 12/13/85.

First National Bank of Dubuque; Dubuque, IA; 50324730002-003; NS; M; F; 12/13/85.

First National Bank of Dubuque; Dubuque, IA; 50324730002-004; NS; M; F; 12/16/85.

First National Bank of East Grand Forks; East Grand Forks, MN; 50224757001-001; S; PS; F; 10/11/85.

First National Bank of East Grand Forks; East Grand Forks, MN; 50224757001-002; S; PS; F; 10/11/85.

First National Bank of East Grand Forks; East Grand Forks, MN; 50224757001-003; S; M; F; 10/11/85.

First National Bank of East Grand Forks; East Grand Forks, MN; 50224757001-004; S; M; F; 10/11/85.

First National Bank of East Grand Forks; East Grand Forks, MN; 50324757001-005; NS; PS; F; 10/11/85.

First National Bank of East Grand Forks; East Grand Forks, MN; 50324757001-006; NS; PS; F; 10/11/85.

First National Bank of East Grand Forks; East Grand Forks, MN; 50324757001-007; NS; M; F; 10/11/85.

First National Bank of East Grand Forks; East Grand Forks, MN; 50324757001-008; NS; M; F; 10/11/85.

First National Bank of Fairmont; Fairmont, MN; 50224867001-001; S; PS; F; 10/11/85.

First National Bank of Fairmont; Fairmont, MN; 50224867001-002; S; PS; F; 10/11/85.

First National Bank of Fairmont; Fairmont, MN; 50224867001-003; S; M; F; 10/11/85.

First National Bank of Fairmont; Fairmont, MN; 50224867001-004; S; M; F; 10/11/85.

First National Bank of Fairmont; Fairmont, MN; 50324867001-005; NS; PS; F; 10/11/85.

First National Bank of Fairmont; Fairmont, MN; 50324867001-006; NS; PS; F; 10/11/85.

First National Bank of Fairmont; Fairmont, MN; 50324867001-007; NS; M; F; 10/11/85.

First National Bank of Fairmont; Fairmont, MN; 50324867001-008; NS; M; F; 10/11/85.

First National Bank of Fort Smith; Fort Smith, AR; 50280592801-001; P; M; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50280592801-002; P; M; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50280592801-003; P; PS; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50280592801-004; P; PS; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50280592801-005; S; M; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50380592801-006; NS; M; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50380592801-007; NS; M; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50380592801-008; NS; PS; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50380592801-009; NS; PS; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50380592801-010; NS; T; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50380592801-011; NS; T; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50280592801-012; S; PS; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50280592802-001; P; D; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50280592802-002; P; D; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50380592802-003; NS; D; F; 11/14/85.

First National Bank of Fort Smith; Fort Smith, AR; 50380592802-004; NS; D; F; 11/14/85.

First National Bank of Great Falls; Great Falls, MT; 50225047001-001; S; PS; F; 10/11/85.

First National Bank of Great Falls; Great Falls, MT; 50225047001-002; S; PS; F; 10/11/85.

First National Bank of Great Falls; Great Falls, MT; 50225047001-003; S; M; F; 10/11/85.

First National Bank of Great Falls; Great Falls, MT; 50225047001-004; S; M; F; 10/11/85.

First National Bank of Great Falls; Great Falls, MT; 50325047001-005; NS; PS; F; 10/11/85.

First National Bank of Great Falls; Great Falls, MT; 50325047001-006; NS; PS; F; 10/11/85.

First National Bank of Great Falls; Great Falls, MT; 50325047001-007; NS; M; F; 10/11/85.

First National Bank of Great Falls; Great Falls, MT; 50325047001-008; NS; M; F; 10/11/85.

First National Bank of Henderson; Henderson, KY; 50273121801-001; P; M; F; 10/03/85.

First National Bank of Henderson; Henderson, KY; 50373121801-002; NS; M; F; 10/03/85.

First National Bank of Henderson; Henderson, KY; 50273121801-003; P; PS; F; 10/03/85.

First National Bank of Henderson; Henderson, KY; 50373121801-004; NS; PS; F; 10/03/85.

First National Bank of Hopkins; Hopkins, MN; 50225147001-001; S; PS; F; 10/11/85.

First National Bank of Hopkins; Hopkins, MN; 50225147001-002; S; PS; F; 10/11/85.

First National Bank of Hopkins; Hopkins, MN; 50225147001-003; S; M; F; 10/11/85.

First National Bank of Hopkins; Hopkins, MN; 50225147001-004; S; M; F; 10/11/85.

First National Bank of Hopkins; Hopkins, MN; 50325147001-005; NS; PS; F; 10/11/85.

First National Bank of Hopkins; Hopkins, MN; 50325147001-006; NS; PS; F; 10/11/85.

First National Bank of Hopkins; Hopkins, MN; 50325147001-007; NS; M; F; 10/11/85.

First National Bank of Hopkins; Hopkins, MN; 50325147001-008; NS; M; F; 10/11/85.

First National Bank of Hutchinson; Hutchinson, KS; 50332520001-001; NS; PS; F; 10/23/85.

First National Bank of Kokomo; Kokomo, IN; 50222361801-001; P; M; F; 10/03/85.

First National Bank of Kokomo; Kokomo, IN; 50322361801-002; NS; M; F; 10/03/85.

First National Bank of Kokomo; Kokomo, IN; 50222361801-003; P; PS; F; 10/03/85.

First National Bank of Kokomo; Kokomo, IN; 50322361801-004; NS; PS; F; 10/03/85.

First National Bank of Lewistown; Lewistown, MT; 50223907001-001; S; PS; F; 10/11/85.

First National Bank of Lewistown; Lewistown, MT; 50223907001-002; S; PS; F; 10/11/85.

First National Bank of Lewistown; Lewistown, MT; 50223907001-003; S; M; F; 10/11/85.

First National Bank of Lewistown; Lewistown, MT; 50223907001-004; S; M; F; 10/11/85.

First National Bank of Lewistown; Lewistown, MT; 50323907001-005; NS; PS; F; 10/11/85.

First National Bank of Lewistown; Lewistown, MT; 50323907001-006; NS; PS; F; 10/11/85.

First National Bank of Lewistown; Lewistown, MT; 50323907001-007; NS; M; F; 10/11/85.

First National Bank of Lewistown; Lewistown, MT; 50323907001-008; NS; M; F; 10/11/85.

First National Bank of Logansport; Logansport, IN; 50278094501-001; P; PS; F; 10/07/85.

First National Bank of Logansport; Logansport, IN; 50378094501-002; NS; PS; F; 10/07/85.

First National Bank of Logansport; Logansport, IN; 50278094501-003; P; M; F; 10/07/85.

First National Bank of Logansport; Logansport, IN; 50378094501-004; NS; M; F; 10/07/85.

First National Bank of Luverne; Luverne, MN; 50225527001-001; S; PS; F; 10/11/85.

First National Bank of Luverne; Luverne, MN; 50225527001-002; S; PS; F; 10/11/85.

First National Bank of Luverne; Luverne, MN; 50225527001-003; S; M; F; 10/11/85.

First National Bank of Luverne; Luverne, MN; 50225527001-004; S; M; F; 10/11/85.

First National Bank of Luverne; Luverne, MN; 50325527001-005; NS; PS; F; 10/11/85.

First National Bank of Luverne; Luverne, MN; 50325527001-006; NS; PS; F; 10/11/85.

First National Bank of Luverne; Luverne, MN; 50325527001-007; NS; M; F; 10/11/85.

First National Bank of Luverne; Luverne, MN; 50325527001-008; NS; M; F; 10/11/85.

First National Bank of Madison County; Anderson, IN; 50325531801-001; NS; M; F; 10/03/85.

First National Bank of Madison County; Anderson, IN; 50325531801-002; NS; PS; F; 10/03/85.

First National Bank of Mankato; Mankato, MN; 50222547001-001; S; PS; F; 10/11/85.

First National Bank of Mankato; Mankato, MN; 50222547001-002; S; PS; F; 10/11/85.

First National Bank of Mankato; Mankato, MN; 50222547001-003; S; M; F; 10/11/85.

First National Bank of Mankato; Mankato, MN; 50222547001-004; S; M; F; 10/11/85.

First National Bank of Mankato; Mankato, MN; 50322547001-005; NS; PS; F; 10/11/85.
First National Bank of Mankato; Mankato, MN; 50322547001-006; NS; PS; F; 10/11/85.
First National Bank of Mankato; Mankato, MN; 50322547001-007; NS; M; F; 10/11/85.
First National Bank of Mankato; Mankato, MN; 50322547001-008; NS; M; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50225647001-001; P; PS; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50225647001-002; P; PS; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50225647001-003; P; M; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50225647001-004; P; M; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50325647001-005; NS; PS; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50325647001-006; NS; PS; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50325647001-007; NS; M; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50325647001-008; NS; M; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50225647002-001; S; D; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50325647002-002; NS; D; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50225647003-001; S; PS; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50225647003-002; S; PS; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50225647003-003; S; M; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50225647003-004; S; M; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50325647003-005; NS; PS; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50325647003-006; NS; PS; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50325647003-007; NS; M; F; 10/11/85.
First National Bank of Minneapolis; Minneapolis, MN; 50325647003-008; NS; M; F; 10/11/85.
First National Bank of Oak Brook; Oak Brook, IL; 50270660001-001; S; PS; F; 10/23/85.
First National Bank of Oak Brook; Oak Brook, IL; 50270660001-002; S; M; F; 10/23/85.
First National Bank of Oak Brook; Oak Brook, IL; 50270660001-003; S; PS; F; 10/23/85.
First National Bank of Oak Brook; Oak Brook, IL; 50270660001-004; S; M; F; 10/23/85.
First National Bank of Oakes; Oakes, ND; 50225877001-001; S; PS; F; 10/11/85.
First National Bank of Oakes; Oakes, ND; 50225877001-002; S; PS; F; 10/11/85.
First National Bank of Oakes; Oakes, ND; 50225877001-003; S; M; F; 10/11/85.
First National Bank of Oakes; Oakes, ND; 50225877001-004; S; M; F; 10/11/85.
First National Bank of Oakes; Oakes, ND; 50325877001-005; NS; PS; F; 10/11/85.
First National Bank of Oakes; Oakes, ND; 50325877001-006; NS; PS; F; 10/11/85.
First National Bank of Oakes; Oakes, ND; 50325877001-007; NS; M; F; 10/11/85.
First National Bank of Oakes; Oakes, ND; 50325877001-008; NS; M; F; 10/11/85.
First National Bank of Owatonna; Owatonna, MN; 50225967001-001; S; PS; F; 10/11/85.
First National Bank of Owatonna; Owatonna, MN; 50225967001-002; S; PS; F; 10/11/85.
First National Bank of Owatonna; Owatonna, MN; 50225967001-003; S; M; F; 10/11/85.
First National Bank of Owatonna; Owatonna, MN; 50225967001-004; S; M; F; 10/11/85.
First National Bank of Owatonna; Owatonna, MN; 50325967001-005; NS; PS; F; 10/11/85.
First National Bank of Owatonna; Owatonna, MN; 50325967001-006; NS; PS; F; 10/11/85.
First National Bank of Owatonna; Owatonna, MN; 50325967001-007; NS; M; F; 10/11/85.
First National Bank of Owatonna; Owatonna, MN; 50325967001-008; NS; M; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50226247001-001; P; PS; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50226247001-002; P; PS; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50226247001-003; P; M; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50226247001-004; P; M; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50326247001-005; NS; PS; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50326247001-006; NS; PS; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50326247001-007; NS; M; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50326247001-008; NS; M; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50226247002-001; S; D; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50326247002-002; NS; D; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50226247003-001; S; PS; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50226247003-002; S; PS; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50226247003-003; S; M; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50226247003-004; S; M; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50326247003-005; NS; PS; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50326247003-006; NS; PS; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50326247003-007; NS; M; F; 10/11/85.
First National Bank of Rochester; Rochester, MN; 50326247003-008; NS; M; F; 10/11/85.
First National Bank of Sauk Centre; Sauk Centre, MN; 50226307001-001; S; PS; F; 10/11/85.
First National Bank of Sauk Centre; Sauk Centre, MN; 50226307001-002; S; PS; F; 10/11/85.
First National Bank of Sauk Centre; Sauk Centre, MN; 50226307001-003; S; M; F; 10/11/85.
First National Bank of Sauk Centre; Sauk Centre, MN; 50226307001-004; S; M; F; 10/11/85.
First National Bank of Sauk Centre; Sauk Centre, MN; 50326307001-005; NS; PS; F; 10/11/85.
First National Bank of Sauk Centre; Sauk Centre, MN; 50326307001-006; NS; PS; F; 10/11/85.
First National Bank of Sauk Centre; Sauk Centre, MN; 50326307001-007; NS; M; F; 10/11/85.
First National Bank of Sauk Centre; Sauk Centre, MN; 50326307001-008; NS; M; F; 10/11/85.
First National Bank of Shelby; Shelby, NC; 50322810001-001; NS; PS; F; 12/19/85.
First National Bank of Shelby; Shelby, NC; 50322810001-002; NS; PS; F; 12/19/85.
First National Bank of Shelby; Shelby, NC; 50322810002-001; NS; M; F; 12/19/85.
First National Bank of Shelby; Shelby, NC; 50322810002-002; NS; M; F; 12/19/85.
First National Bank of St Paul; St Paul, MN; 50226277001-001; S; PS; F; 10/11/85.
First National Bank of St Paul; St Paul, MN; 50226277001-002; S; PS; F; 10/11/85.
First National Bank of St Paul; St Paul, MN; 50226277001-003; S; M; F; 10/11/85.
First National Bank of St Paul; St Paul, MN; 50226277001-004; S; M; F; 10/11/85.
First National Bank of St Paul; St Paul, MN; 50326277001-005; NS; PS; F; 10/11/85.
First National Bank of St Paul; St Paul, MN; 50326277001-006; NS; PS; F; 10/11/85.
First National Bank of St Paul; St Paul, MN; 50326277001-007; NS; M; F; 10/11/85.
First National Bank of St Paul; St Paul, MN; 50326277001-008; NS; M; F; 10/11/85.
First National Bank of Stillwater; Stillwater, MN; 50226497001-001; S; PS; F; 10/11/85.
First National Bank of Stillwater; Stillwater, MN; 50226497001-002; S; PS; F; 10/11/85.
First National Bank of Stillwater; Stillwater, MN; 50226497001-003; S; M; F; 10/11/85.
First National Bank of Stillwater; Stillwater, MN; 50226497001-004; S; M; F; 10/11/85.
First National Bank of Stillwater; Stillwater, MN; 50326497001-005; NS; PS; F; 10/11/85.
First National Bank of Stillwater; Stillwater, MN; 50326497001-006; NS; PS; F; 10/11/85.
First National Bank of Stillwater; Stillwater, MN; 50326497001-007; NS; M; F; 10/11/85.
First National Bank of Stillwater; Stillwater, MN; 50326497001-008; NS; M; F; 10/11/85.
First National Bank of Valley City; Valley City, ND; 50226637001-001; S; PS; F; 10/11/85.
First National Bank of Valley City; Valley City, ND; 50226637001-002; S; PS; F; 10/11/85.
First National Bank of Valley City; Valley City, ND; 50226637001-003; S; M; F; 10/11/85.
First National Bank of Valley City; Valley City, ND; 50226637001-004; S; M; F; 10/11/85.
First National Bank of Valley City; Valley City, ND; 50326637001-005; NS; PS; F; 10/11/85.
First National Bank of Valley City; Valley City, ND; 50326637001-006; NS; PS; F; 10/11/85.
First National Bank of Valley City; Valley City, ND; 50326637001-007; NS; M; F; 10/11/85.
First National Bank of Valley City; Valley City, ND; 50326637001-008; NS; M; F; 10/11/85.
First National Bank of Vicksburg; Vicksburg, MS; 50273153501-007; P; PS; U; 10/30/85.
First National Bank of Vicksburg; Vicksburg, MS; 50273153501-009; P; M; U; 10/30/85.
First National Bank of Warsaw; Warsaw, IN; 50326671801-001; NS; M; F; 10/03/85.
First National Bank of Warsaw; Warsaw, IN; 50326671801-002; NS; PS; F; 10/03/85.
First National Bank of Willmar; Willmar, MN; 50214967001-001; S; PS; F; 10/11/85.
First National Bank of Willmar; Willmar, MN; 50214967001-002; S; PS; F; 10/11/85.
First National Bank of Willmar; Willmar, MN; 50214967001-003; S; M; F; 10/11/85.
First National Bank of Willmar; Willmar, MN; 50214967001-004; S; M; F; 10/11/85.
First National Bank of Willmar; Willmar, MN; 50314967001-005; NS; PS; F; 10/11/85.
First National Bank of Willmar; Willmar, MN; 50314967001-006; NS; PS; F; 10/11/85.
First National Bank of Willmar; Willmar, MN; 50314967001-007; NS; M; F; 10/11/85.
First National Bank of Willmar; Willmar, MN; 50314967001-008; NS; M; F; 10/11/85.
First National Bank of Windom; Windom, MN; 50222557001-001; S; PS; F; 10/11/85.
First National Bank of Windom; Windom, MN; 50222557001-002; S; PS; F; 10/11/85.
First National Bank of Windom; Windom, MN; 50222557001-003; S; M; F; 10/11/85.
First National Bank of Windom; Windom, MN; 50222557001-004; S; M; F; 10/11/85.
First National Bank of Windom; Windom, MN; 50322557001-005; NS; PS; F; 10/11/85.
First National Bank of Windom; Windom, MN; 50322557001-006; NS; PS; F; 10/11/85.
First National Bank of Windom; Windom, MN; 50322557001-007; NS; M; F; 10/11/85.
First National Bank of Windom; Windom, MN; 50322557001-008; NS; M; F; 10/11/85.
First National Park Bank of Livingston; Livingston, MT; 50230547001-001; S; PS; F; 10/11/85.
First National Park Bank of Livingston; Livingston, MT; 50230547001-002; S; PS; F; 10/11/85.
First National Park Bank of Livingston; Livingston, MT; 50230547001-003; S; M; F; 10/11/85.
First National Park Bank of Livingston; Livingston, MT; 50230547001-004; S; M; F; 10/11/85.
First National Park Bank of Livingston; Livingston, MT; 50330547001-005; NS; PS; F; 10/11/85.
First National Park Bank of Livingston; Livingston, MT; 50330547001-006; NS; PS; F; 10/11/85.
First National Park Bank of Livingston; Livingston, MT; 50330547001-007; NS; M; F; 10/11/85.
First National Park Bank of Livingston; Livingston, MT; 50330547001-008; NS; M; F; 10/11/85.
First Northtown National Bank; Blaine, MN; 50208937001-001; S; PS; F; 10/11/85.
First Northtown National Bank; Blaine, MN; 50208937001-002; S; PS; F; 10/11/85.
First Northtown National Bank; Blaine, MN; 50208937001-003; S; M; F; 10/11/85.
First Northtown National Bank; Blaine, MN; 50208937001-004; S; M; F; 10/11/85.
First Northtown National Bank; Blaine, MN; 50308937001-005; NS; PS; F; 10/11/85.
First Northtown National Bank; Blaine, MN; 50308937001-006; NS; PS; F; 10/11/85.
First Northtown National Bank; Blaine, MN; 50308937001-007; NS; M; F; 10/11/85.

First Northtown National Bank; Blaine, MN; 50308937001-008; NS; M; F; 10/11/85.

First Oak Brook Bank Addison; Addison, IL; 50270670001-001; S; PS; F; 10/23/85.

First Oak Brook Bank Addison; Addison, IL; 50270670001-002; S; M; F; 10/23/85.

First Oak Brook Bank Addison; Addison, IL; 50270670001-003; S; PS; F; 10/23/85.

First Oak Brook Bank Addison; Addison, IL; 50270670001-004; S; M; F; 10/23/85.

First Oak Brook Bank DuPage; Warrenville, IL; 50269460001-001; S; PS; F; 10/23/85.

First Oak Brook Bank DuPage; Warrenville, IL; 50269460001-002; S; M; F; 10/30/85.

First Oak Brook Bank DuPage; Warrenville, IL; 50269460001-003; S; PS; F; 10/23/85.

First Oak Brook Bank DuPage; Warrenville, IL; 50269460001-004; S; M; F; 10/23/35.

First of America Bank Ann Arbor; Ann Arbor, MI; 50204200001-001; P; M; F; 12/13/85.

First of America Bank Ann Arbor; Ann Arbor, MI; 50204200001-002; P; M; F; 12/13/85.

First of America Bank Ann Arbor; Ann Arbor, MI; 50204200001-003; P; PS; F; 12/13/85.

First of America Bank Ann Arbor; Ann Arbor, MI; 50204200001-004; P; PS; F; 12/13/85.

First of America Bank Ann Arbor; Ann Arbor, MI; 50304200001-005; NS; M; F; 12/13/85.

First of America Bank Ann Arbor; Ann Arbor, MI; 50304200001-006; NS; M; F; 12/13/85.

First of America Bank Ann Arbor; Ann Arbor, MI; 50304200001-007; NS; PS; F; 12/13/85.

First of America Bank Ann Arbor; Ann Arbor, MI; 50304200001-008; NS; PS; F; 12/13/85.

First of America Bank Central; Lansing, MI; 50202350001-001; P; M; F; 12/13/85.

First of America Bank Central; Lansing, MI; 50202350001-002; P; M; F; 12/13/85.

First of America Bank Central; Lansing, MI; 50202350001-003; P; PS; F; 12/13/85.

First of America Bank Central; Lansing, MI; 50202350001-004; P; PS; F; 12/13/85.

First of America Bank Central; Lansing, MI; 50302350001-005; NS; M; F; 12/13/85.

First of America Bank Central; Lansing, MI; 50302350001-006; NS; M; F; 12/13/85.

First of America Bank Central; Lansing, MI; 50302350001-007; NS; PS; F; 12/13/85.

First of America Bank Central; Lansing, MI; 50302350001-008; NS; PS; F; 12/13/85.

First of America Bank Detroit NA; Detroit, MI; 50213720001-001; P; M; F; 12/12/85.

First of America Bank Detroit NA; Detroit, MI; 50213720001-002; P; M; F; 12/12/85.

First of America Bank Detroit NA; Detroit, MI; 50213720001-003; P; PS; F; 12/12/85.

First of America Bank Detroit NA; Detroit, MI; 50213720001-004; P; PS; F; 12/12/85.

First of America Bank Detroit NA; Detroit, MI; 50313720001-005; NS; M; F; 12/12/85.

First of America Bank Detroit NA; Detroit, MI; 50313720001-006; NS; M; F; 12/12/85.

First of America Bank Detroit NA; Detroit, MI; 50313720001-007; NS; PS; F; 12/12/85.

First of America Bank Detroit NA; Detroit, MI; 50313720001-008; NS; PS; F; 12/12/85.

First of America Bank Marquette NA; Marquette, MI; 50270470001-001; P; M; F; 12/12/85.

First of America Bank Marquette NA; Marquette, MI; 50270470001-002; P; M; F; 12/12/85.

First of America Bank Marquette NA; Marquette, MI; 50270470001-003; P; PS; F; 12/12/85.

First of America Bank Marquette NA; Marquette, MI; 50270470001-004; P; PS; F; 12/13/85.

First of America Bank Marquette NA; Marquette, MI; 50370470001-005; NS; M; F; 12/13/85.

First of America Bank Marquette NA; Marquette, MI; 50370470001-006; NS; M; F; 12/13/85.

First of America Bank Marquette NA; Marquette, MI; 50370470001-007; NS; PS; F; 12/13/85.

First of America Bank Marquette NA; Marquette, MI; 50370470001-008; NS; PS; F; 12/13/85.

First of America Bank Michigan NA; Kalamazoo, MI; 50223170001-001; P; M; F; 12/10/85.

First of America Bank Michigan NA; Kalamazoo, MI; 50223170001-002; P; M; F; 12/10/85.

First of America Bank Michigan NA; Kalamazoo, MI; 50223170001-003; P; PS; F; 12/13/85.

First of America Bank Michigan NA; Kalamazoo, MI; 50223170001-004; P; PS; F; 12/10/85.

First of America Bank Michigan NA; Kalamazoo, MI; 50323170001-005; NS; M; F; 12/10/85.

First of America Bank Michigan NA; Kalamazoo, MI; 50323170001-006; NS; M; F; 12/10/86.

First of America Bank Michigan NA; Kalamazoo, MI; 50323170001-007; NS; PS; F; 12/10/85.

First of America Bank Michigan NA; Kalamazoo, MI; 50323170001-008; NS; PS; F; 12/10/85.

First of America Bank Muskegon; Muskegon, MI; 50241380001-001; P; M; F; 12/10/85.

First of America Bank Muskegon; Muskegon, MI; 50241380001-002; P; M; F; 12/10/85.

First of America Bank Muskegon; Muskegon, MI; 50241380001-003; P; PS; F; 12/10/85.

First of America Bank Muskegon; Muskegon, MI; 50241380001-004; P; PS; F; 12/10/85.

First of America Bank Muskegon; Muskegon, MI; 503[illegible]0001-005; NS; M; F; 12/12/85.

First of America Bank Muskegon; Muskegon, MI; 50341380001-006; NS; M; F; 12/10/85.

First of America Bank Muskegon; Muskegon, MI; 50341380001-007; NS; PS; F; 12/10/85.

First of America Bank Muskegon; Muskegon, MI; 50341380001-008; NS; PS; F; 12/10/85.

First of America Bank Wayne Oakland; Royal Oak, MI; 50259020001-001; P; M; F; 12/10/85.

First of America Bank Wayne Oakland; Royal Oak, MI; 50259020001-002; P; M; F; 12/10/85.

First of America Bank Wayne Oakland; Royal Oak, MI; 50259020001-003; P; PS; F; 12/12/85.

First of America Bank Wayne Oakland; Royal Oak, MI; 50259020001-004; P; PS; F; 12/12/85.

First of America Bank Wayne Oakland; Royal Oak, MI; 50359020001-005; NS; M; F; 12/12/85.

First of America Bank Wayne Oakland; Royal Oak, MI; 50359020001-006; NS; M; F; 12/12/85.

First of America Bank Wayne Oakland; Royal Oak, MI; 50359020001-007; NS; PS; F; 12/12/85.

First of America Bank Wayne Oakland; Royal Oak, MI; 50359020001-008; NS; PS; F; 12/12/85.

First Plymouth National Bank; Plymouth, MN; 50217397001-001; S; PS; F; 10/11/85.

First Plymouth National Bank; Plymouth, MN; 50217397001-002; S; PS; F; 10/11/85.

First Plymouth National Bank; Plymouth, MN; 50217397001-003; S; M; F; 10/11/85.

First Plymouth National Bank; Plymouth, MN; 50217397001-004; S; M; F; 10/11/85.

First Plymouth National Bank; Plymouth, MN; 50317397001-005; NS; PS; F; 10/11/85.

First Plymouth National Bank; Plymouth, MN; 50317397001-006; NS; PS; F; 10/11/85.

First Plymouth National Bank; Plymouth, MN; 50317397001-007; NS; M; F; 10/11/85.

First Plymouth National Bank; Plymouth, MN; 50317397001-008; NS; M; F; 10/11/85.

First Robbinsdale State Bank; Robbinsdale, MN; 50227877001-001; S; PS; F; 10/11/85.

First Robbinsdale State Bank; Robbinsdale, MN; 50227877001-002; S; PS; F; 10/11/85.

First Robbinsdale State Bank; Robbinsdale, MN; 50227877001-003; S; M; F; 10/11/85.

First Robbinsdale State Bank; Robbinsdale, MN; 50227877001-004; S; M; F; 10/11/85.

First Robbinsdale State Bank; Robbinsdale, MN; 50327877001-005; NS; PS; F; 10/11/85.

First Robbinsdale State Bank; Robbinsdale, MN; 50327877001-006; NS; PS; F; 10/11/85.

First Robbinsdale State Bank; Robbinsdale, MN; 50327877001-007; NS; M; F; 10/11/85.

First Robbinsdale State Bank; Robbinsdale, MN; 50327877001-008; NS; M; F; 10/11/85.

First Security State Bank of St Paul; St Paul, MN; 50228117001-001; S; PS; F; 10/11/85.

First Security State Bank of St Paul; St Paul, MN; 50228117001-002; S; PS; F; 10/11/85.

First Security State Bank of St Paul; St Paul, MN; 50228117001-003; S; M; F; 10/11/85.

First Security State Bank of St Paul; St Paul, MN; 50228117001-004; S; M; F; 10/11/85.

First Security State Bank of St Paul; St Paul, MN; 50328117001-005; NS; PS; F; 10/11/85.

First Security State Bank of St Paul; St Paul, MN; 50328117001-006; NS; PS; F; 10/11/85.

First Security State Bank of St Paul; St Paul, MN; 50328117001-007; NS; M; F; 10/11/85.

First Security State Bank of St Paul; St Paul, MN; 50328117001-008; NS; M; F; 10/11/85.

First Source Bank; South Bend, IN; 50370350001-001; NS; M; F; 12/02/85.

First Source Bank; South Bend, IN; 50370350001-002; NS; M; F; 12/02/85.

First Source Bank; South Bend, IN; 50370350001-003; NS; M; F; 12/02/85.

First Source Bank; South Bend, IN; 50370350001-004; NS; M; F; 12/02/85.

First Source Bank; South Bend, IN; 50370350002-001; NS; PS; F; 12/02/85.

First Source Bank; South Bend, IN; 50370350002-002; NS; PS; F; 12/02/85.

First Source Bank; South Bend, IN; 50370350002-003; NS; PS; F; 12/02/85.

First Source Bank; South Bend, IN; 50370350002-004; NS; PS; F; 12/02/85.

First Southdale National Bank; Edina, MN; 50216957001-001; S; PS; F; 10/11/85.

First Southdale National Bank; Edina, MN; 50216957001-002; S; PS; F; 10/11/85.

First Southdale National Bank; Edina, MN; 50216957001-003; S; M; F; 10/11/85.

First Southdale National Bank; Edina, MN; 50216957001-004; S; M; F; 10/11[illegible]

First Southdale National Bank; Edina, [illegible] 50316957001-005; NS; PS; F; 10/11/[illegible]

First Southdale National Bank; Edina, M[illegible] 50316957001-006; NS; PS; F; 10/11/85

First Southdale National Bank; Edina, MN; 50316957001-007; NS; M; F; 10/11/85.

First Southdale National Bank; Edina, MN; 50316957001-008; NS; M; F; 10/11/85.

First State Bank in Paynesville; Paynesville, MN; 50228517001-001; S; PS; F; 10/11/85.

First State Bank in Paynesville; Paynesville, MN; 50228517001-002; S; PS; F; 10/11/85.

First State Bank in Paynesville; Paynesville, MN; 50228517001-003; S; M; F; 10/11/85.

First State Bank in Paynesville; Paynesville, MN; 50228517001-004; S; M; F; 10/11/85.

First State Bank in Paynesville; Paynesville, MN; 50328517001-005; NS; PS; F; 10/11/85.

First State Bank in Paynesville; Paynesville, MN; 50328517001-006; NS; PS; F; 10/11/85.

First State Bank in Paynesville; Paynesville, MN; 50328517001-007; NS; M; F; 10/11/85.

First State Bank in Paynesville; Paynesville, MN; 50328517001-008; NS; M; F; 10/11/85.

First State Bank of Benson; Benson, MN; 50207877001-001; S; PS; F; 10/11/85.

First State Bank of Benson; Benson, MN; 50207677001-002; S; PS; F; 10/11/85.

First State Bank of Benson; Benson, MN; 50207877001-003; S; M; F; 10/11/85.

First State Bank of Benson; Benson, MN; 50207877001-004; S; M; F; 10/11/85.

First State Bank of Benson; Benson, MN; 50307877001-005; NS; PS; F; 10/11/85.

First State Bank of Benson; Benson, MN; 50307877001-006; NS; PS; F; 10/11/85.

First State Bank of Benson; Benson, MN; 50307877001-007; NS; M; F; 10/11/85.

First State Bank of Benson; Benson, MN; 50307877001-008; NS; M; F; 10/11/85.

First State Bank of Cando; Cando, ND; 50228587001-001; S; PS; F; 10/11/85.

First State Bank of Cando; Cando, ND; 50228587001-002; S; PS; F; 10/11/85.

First State Bank of Cando; Cando, ND; 50228587001-003; S; M; F; 10/11/85.

First State Bank of Cando; Cando, ND; 50228587001-004; S; M; F; 10/11/85.

First State Bank of Cando; Cando, ND; 50328587001-005; NS; PS; F; 10/11/85.

First State Bank of Cando; Cando, ND; 50328587001-006; NS; PS; F; 10/11/85.

First State Bank of Cando; Cando, ND; 50328587001-007; NS; M; F; 10/11/85.

First State Bank of Cando; Cando, ND; 50328587001-008; NS; M; F; 10/11/85.

First State Bank of Cooperstown; Cooperstown, ND; 50280527001-001; S; PS; F; 10/11/85.

First State Bank of Cooperstown; Cooperstown, ND; 50280527001-002; S; PS; F; 10/11/85.

First State Bank of Cooperstown; Cooperstown, ND; 50280527001-003; S; M; F; 10/11/85.
First State Bank of Cooperstown; Cooperstown, ND; 50280527001-004; S; M; F; 10/11/85.
First State Bank of Cooperstown; Cooperstown, ND; 50380527001-005; NS; PS; F; 10/11/85.
First State Bank of Cooperstown; Cooperstown, ND; 50380527001-006; NS; PS; F; 10/11/85.
First State Bank of Cooperstown; Cooperstown, ND; 50380527001-007; NS; M; F; 10/11/85.
First State Bank of Cooperstown; Cooperstown, ND; 50380527001-008; NS; M; F; 10/11/85.
First State Bank of Forsyth; Forsyth, MT; 50220957001-001; S; PS; F; 10/11/85.
First State Bank of Forsyth; Forsyth, MT; 50220957001-002; S; PS; F; 10/11/85.
First State Bank of Forsyth; Forsyth, MT; 50220957001-003; S; M; F; 10/11/85.
First State Bank of Forsyth; Forsyth, MT; 50220957001-004; S; M; F; 10/11/85.
First State Bank of Forsyth; Forsyth, MT; 50320957001-005; NS; PS; F; 10/11/85.
First State Bank of Forsyth; Forsyth, MT; 50320957001-006; NS; PS; F; 10/11/85.
First State Bank of Forsyth; Forsyth, MT; 50320957001-007; NS; M; F; 10/11/85.
First State Bank of Forsyth; Forsyth, MT; 50320957001-008; NS; M; F; 10/11/85.
First State Bank of Fort Benton; Fort Benton, MT; 50228407001-001; S; PS; F; 10/11/85.
First State Bank of Fort Benton; Fort Benton, MT; 50228407001-002; S; PS; F; 10/11/85.
First State Bank of Fort Benton; Fort Benton, MT; 50228407001-003; S; M; F; 10/11/85.
First State Bank of Fort Benton; Fort Benton, MT; 50228407001-004; S; M; F; 10/11/85.
First State Bank of Fort Benton; Fort Benton, MT; 50328407001-005; NS; PS; F; 10/11/85.
First State Bank of Fort Benton; Fort Benton, MT; 50328407001-006; NS; PS; F; 10/11/85.
First State Bank of Fort Benton; Fort Benton, MT; 50328407001-007; NS; M; F; 10/11/85.
First State Bank of Fort Benton; Fort Benton, MT; 50328407001-008; NS; M; F; 10/11/85.
First State Bank of Froid Montana; Froid, MT; 50228657001-001; S; PS; F; 10/11/85.
First State Bank of Froid Montana; Froid, MT; 50228657001-002; S; PS; F; 10/11/85.
First State Bank of Froid Montana; Froid, MT; 50228657001-003; S; M; F; 10/11/85.
First State Bank of Froid Montana; Froid, MT; 50228657001-004; S; M; F; 10/11/85.
First State Bank of Froid Montana; Froid, MT; 50328657001-005; NS; PS; F; 10/11/85.
First State Bank of Froid Montana; Froid, MT; 50328657001-006; NS; PS; F; 10/11/85.
First State Bank of Froid Montana; Froid, MT; 50328657001-007; NS; M; F; 10/11/85.
First State Bank of Froid Montana; Froid, MT; 50328657001-008; NS; M; F; 10/11/85.
First State Bank of Highmore; Highmore, SD; 50228287001-001; S; PS; F; 10/11/85.
First State Bank of Highmore; Highmore, SD; 50228287001-002; S; PS; F; 10/11/85.
First State Bank of Highmore; Highmore, SD; 50228287001-003; S; M; F; 10/11/85.
First State Bank of Highmore; Highmore, SD; 50228287001-004; S; M; F; 10/11/85.
First State Bank of Highmore; Highmore, SD; 50328287001-005; NS; PS; F; 10/11/85.
First State Bank of Highmore; Highmore, SD; 50328287001-006; NS; PS; F; 10/11/85.
First State Bank of Highmore; Highmore, SD; 50328287001-007; NS; M; F; 10/11/85.
First State Bank of Highmore; Highmore, SD; 50328287001-008; NS; M; F; 10/11/85.
First State Bank of Litchfield; Litchfield, MN; 50228717001-001; S; PS; F; 10/11/85.
First State Bank of Litchfield; Litchfield, MN; 50228717001-002; S; PS; F; 10/11/85.
First State Bank of Litchfield; Litchfield, MN; 50228717001-003; S; M; F; 10/11/85.
First State Bank of Litchfield; Litchfield, MN; 50228717001-004; S; M; F; 10/11/85.
First State Bank of Litchfield; Litchfield, MN; 50328717001-005; NS; PS; F; 10/11/85.
First State Bank of Litchfield; Litchfield, MN; 50328717001-006; NS; PS; F; 10/11/85.
First State Bank of Litchfield; Litchfield, MN; 50328717001-007; NS; M; F; 10/11/85.
First State Bank of Litchfield; Litchfield, MN; 50328717001-008; NS; M; F; 10/11/85.
First State Bank of McLaughlin; Mclaughlin, SD; 50228297001-001; S; PS; F; 10/11/85.
First State Bank of McLaughlin; Mclaughlin, SD; 50228297001-002; S; PS; F; 10/11/85.
First State Bank of McLaughlin; Mclaughlin, SD; 50228297001-003; S; M; F; 10/11/85.
First State Bank of McLaughlin; Mclaughlin, SD; 50228297001-004; S; M; F; 10/11/85.
First State Bank of McLaughlin; Mclaughlin, SD; 50328297001-005; NS; PS; F; 10/11/85.
First State Bank of McLaughlin; Mclaughlin, SD; 50328297001-006; NS; PS; F; 10/11/85.
First State Bank of McLaughlin; Mclaughlin, SD; 50328297001-007; NS; M; F; 10/11/85.
First State Bank of McLaughlin; Mclaughlin, SD; 50328297001-008; NS; M; F; 10/11/85.
First State Bank of Minneota; Minneota, MN; 50228737001-001; S; PS; F; 10/11/85.
First State Bank of Minneota; Minneota, MN; 50228737001-002; S; PS; F; 10/11/85.
First State Bank of Minneota; Minneota, MN; 50228737001-003; S; M; F; 10/11/85.
First State Bank of Minneota; Minneota, MN; 50228737001-004; S; M; F; 10/11/85.
First State Bank of Minneota; Minneota, MN; 50328737001-005; NS; PS; F; 10/11/85.
First State Bank of Minneota; Minneota, MN; 50328737001-006; NS; PS; F; 10/11/85.
First State Bank of Minneota; Minneota, MN; 50328737001-007; NS; M; F; 10/11/85.
First State Bank of Minneota; Minneota, MN; 50328737001-008; NS; M; F; 10/11/85.
First State Bank of Park River; Park River, ND; 50228787001-001; S; PS; F; 10/11/85.
First State Bank of Park River; Park River, ND; 50228787001-002; S; PS; F; 10/11/85.
First State Bank of Park River; Park River, ND; 50228787001-003; S; M; F; 10/11/85.
First State Bank of Park River; Park River, ND; 50228767001-004; S; M; F; 10/11/85.
First State Bank of Park River; Park River, ND; 50328787001-005; NS; PS; F; 10/11/85.
First State Bank of Park River; Park River, ND; 50328787001-006; NS; PS; F; 10/11/85.
First State Bank of Park River; Park River, ND; 50328787001-007; NS; M; F; 10/11/85.
First State Bank of Park River; Park River, ND; 50328787001-008; NS; M; F; 10/11/85.
First State Bank of Waseca; Waseca, MN; 50228867001-001; S; PS; F; 10/11/85.
First State Bank of Waseca; Waseca, MN; 50228867001-002; S; PS; F; 10/11/85.
First State Bank of Waseca; Waseca, MN; 50228867001-003; S; M; F; 10/11/85.
First State Bank of Waseca; Waseca, MN; 50228867001-004; S; M; F; 10/11/85.
First State Bank of Waseca; Waseca, MN; 50328867001-005; NS; PS; F; 10/11/85.
First State Bank of Waseca; Waseca, MN; 50328867001-006; NS; PS; F; 10/11/85.
First State Bank of Waseca; Waseca, MN; 50328867001-007; NS; M; F; 10/11/85.
First State Bank of Waseca; Waseca, MN; 50328867001-008; NS; M; F; 10/11/85.
First State Bank of Wheaton; Wheaton, MN; 50227027001-001; S; PS; F; 10/11/85.
First State Bank of Wheaton; Wheaton, MN; 50227027001-002; S; PS; F; 10/11/85.
First State Bank of Wheaton; Wheaton, MN; 50227027001-003; S; M; F; 10/11/85.
First State Bank of Wheaton; Wheaton, MN; 50227027001-004; S; M; F; 10/11/85.
First State Bank of Wheaton; Wheaton, MN; 50327027001-005; NS; PS; F; 10/11/85.
First State Bank of Wheaton; Wheaton, MN; 50327027001-006; NS; PS; F; 10/11/85.
First State Bank of Wheaton; Wheaton, MN; 50327027001-007; NS; M; F; 10/11/85.
First State Bank of Wheaton; Wheaton, MN; 50327027001-008; NS; M; F; 10/11/85.
First State Bank of White Bear Lake; White Bear Lake, MN; 502288[illegible]7001-001; S; PS; F; 10/11/85.
First State Bank of White Bear Lake; White Bear Lake, MN; 50228877001-002; S; PS; F; 10/11/85.
First State Bank of White Bear Lake; White Bear Lake, MN; 50228877001-003; S; M; F; 10/11/85.
First State Bank of White Bear Lake; White Bear Lake, MN; 50228877001-004; S; M; F; 10/11/85.
First State Bank of White Bear Lake; White Bear Lake, MN; 50328877001-005; NS; PS; F; 10/11/85.
First State Bank of White Bear Lake; White Bear Lake, MN; 50328877001-006; NS; PS; F; 10/11/85.
First State Bank of White Bear Lake; White Bear Lake, MN; 50328877001-007; NS; M; F; 10/11/85.
First State Bank of White Bear Lake; White Bear Lake, MN; 50328877001-008; NS; M; F; 10/11/85.
First Tennessee Bank; Memphis, TN; 50328952201-001; NS; PS; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50328952201-002; NS; M; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50328952201-003; NS; PS; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50328952201-004; NS; T; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50228952202-001; P; PS; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50228952202-002; P; M; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50328952203-001; NS; D; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50328952203-002; NS; D; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50328952203-003; NS; D; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50328952203-004; NS; D; F; 12/05/85.
First Tennessee Bank; Memphis, TN; 50328952203-005; NS; D; F; 12/05/85.
First Trust Co of Arizona; Phoenix, AZ; 50229117001-001; P; PS; F; 10/11/85.
First Trust Co of Arizona; Phoenix, AZ; 50229117001-002; P; PS; F; 10/11/85.
First Trust Co of Arizona; Phoenix, AZ; 50229117001-003; P; M; F; 10/11/85.
First Trust Co of Arizona; Phoenix, AZ; 50229117001-004; P; M; F; 10/11/85.
First Trust Co of Arizona; Phoenix, AZ; 50329117001-005; NS; PS; F; 10/11/85.
First Trust Co of Arizona; Phoenix, AZ; 50329117001-006; NS; PS; F; 10/11/85.
First Trust Co of Arizona; Phoenix, AZ; 50329117001-007; NS; M; F; 10/11/85.
First Trust Co of Arizona; Phoenix, AZ; 50329117001-008; NS; M; F; 10/11/85.
First Trust Co of Arizona; Phoenix, AZ; 50229117002-001; S; D; F; 10/11/85.
First Trust Co of Arizona; Phoenix, AZ; 50329117002-002; NS; D; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50229127001-001; P; PS; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50229127001-002; P; PS; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50229127001-003; P; M; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50229127001-004; P; M; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50329127001-005; NS; PS; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50329127001-006; NS; PS; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50329127001-007; NS; M; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50329127001-008; NS; M; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50229127002-001; S; D; F; 10/11/85.
First Trust Co of Florida NA; Sarasota, FL; 50329127002-002; NS; D; F; 10/11/85.
First Trust Co of Montana; Billings, MT; 50229057001-001; P; PS; F; 10/11/95.
First Trust Co of Montana; Billings, MT; 50229057001-002; P; PS; F; 10/11/85.
First Trust Co of Montana; Billings, MT; 50229057001-003; P; M; F; 10/11/85.
First Trust Co of Montana; Billings, MT; 50229057001-004; P; M; F; 10/11/85.
First Trust Co of Montana; Billings, MT; 50329057001-005; NS; PS; F; 10/11/85.
First Trust Co of Montana; Billings, MT; 50329057001-006; NS; PS; F; 10/11/85.

First Trust Co of Montana; Billings, MT; 50329057001-007; NS; M; F; 10/11/85.

First Trust Co of Montana; Billings, MT; 50329057001-008; NS; M; F; 10/11/85.

First Trust Co of Montana; Billings, MT; 50229057002-001; S; D; F; 10/11/85.

First Trust Co of Montana; Billings, MT; 50329057002-002; NS; D; F; 10/11/85.

First Trust Co of North Dakota; Fargo, ND; 50229067003-001; S; PS; F; 11/04/85.

First Trust Co of North Dakota; Fargo, ND; 50229067003-002 S; PS; F; 11/04/85.

First Trust Co of North Dakota; Fargo, ND; 50229067003-003; S; M; F; 11/04/85.

First Trust Co of North Dakota; Fargo, ND; 50229067003-004; S; M; F; 11/04/85.

First Trust Co of North Dakota; Fargo, ND; 50329067003-005; NS; PS; F; 10/11/85.

First Trust Co of North Dakota; Fargo, ND; 50329067003-006; NS; PS; F; 10/11/85.

First Trust Co of North Dakota; Fargo, ND; 50329067003-007; NS; M; F; 10/11/85.

First Trust Co of North Dakota; Fargo, ND; 50329067003-008; NS; M; F; 10/11/85.

First Trust Co of North Dakota; Fargo, ND; 50229067004-001; S; D; F; 10/11/85.

First Trust Co of North Dakota; Fargo, ND; 50329067004-002; NS; D; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50229087001-001; P; PS; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50229087001-002; P; PS; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50229087001-003; P; M; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50229087001-004; P; M; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50329087001-005; NS; PS; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50329087001-006; NS; PS; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50329087001-007; NS; M; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50329087001-008; NS; M; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50229087002-001; S; D; F; 10/11/85.

First Trust Co of St Paul; St Paul, MN; 50329087002-002; NS; D; F; 10/11/85.

First Virginia Bank; Falls Church, VA; 50229270001-001; P; M; F; 10/23/85.

First Virginia Bank; Falls Church, VA; 50229270001-003; P; PS; F; 10/23/85.

First Virginia Bank; Falls Church, VA; 50329270001-004; NS; PS; F; 10/23/85.

First Westside National Bank of Great Falls; Great Falls, MT; 50229307001-001; S; PS; F; 10/11/85.

First Westside National Bank of Great Falls; Great Falls, MT; 50229307001-002; S; PS; F; 10/11/85.

First Westside National Bank of Great Falls; Great Falls, MT; 50229307001-003; S; M; F; 10/11/85.

First Westside National Bank of Great Falls; Great Falls, MT; 50229307001-004; S; M; F; 10/11/85.

First Westside National Bank of Great Falls; Great Falls, MT; 50329307001-005; NS; PS; F; 10/11/85.

First Westside National Bank of Great Falls; Great Falls, MT; 50329307001-006; NS; PS; F; 10/11/85.

First Westside National Bank of Great Falls; Great Falls, MT; 50329307001-007; NS; M; F; 10/11/85.

First Westside National Bank of Great Falls; Great Falls, MT; 50329307001-008; NS; M; F; 10/11/85.

Florida League of Financial Institutions; Orlando, FL; 50229920001-001; P; PS; F; 12/08/85.

Florida League of Financial Institutions; Orlando, FL; 50229920001-002; P; PS; F; 12/08/85.

Florida League of Financial Institutions; Orlando, FL; 50229920001-003; P; M; F; 12/08/85.

Florida League of Financial Institutions; Orlando, FL; 50229920001-004; P; M; F; 12/08/85.

Franklin Bank & Trust Co; Franklin, IN; 50230291801-001; S; M; F; 10/03/85.

Franklin Bank & Trust Co; Franklin, IN; 50330291801-002; NS; M; F; 10/03/85.

Franklin State Bank; Somerset, NJ; 50230340001-001; P; PS; F; 12/26/85.

Franklin State Bank; Somerset, NJ; 50230340001-002; P; M; F; 12/26/85.

Frost National Bank; San Antonio, TX; 50230521901-001; P; PS; F; 12/06/85.

Frost National Bank; San Antonio, TX; 50230521901-002; P; M; F; 12/06/85.

Frost National Bank; San Antonio, TX; 50330521901-003; NS; PS; F; 12/06/85.

Frost National Bank; San Antonio, TX; 50330521901-004; NS; M; F; 12/06/85.

Frost National Bank; San Antonio, TX; 50330521901-005; NS; PS; F; 12/06/85.

Frost National Bank; San Antonio, TX; 50330521901-006; NS; M; F; 12/06/85.

Fulton Federal Savings & Loan Association; Atlanta, GA; 50230560001-001; S; PS; F; 10/23/85.

Fulton Federal Savings & Loan Association; Atlanta, GA; 50230560001-002; S; M; F; 10/23/85.

Gateway Option Income Fund Inc; Cincinnati, OH; 50230780001-001; P; PS; F; 10/30/85.

Gateway Option Income Fund Inc; Cincinnati, OH; 50230780001-002; P; M; F; 10/30/85.

Georgia International Life Insurance Co; Atlanta, GA; 50331026401-001; NS; M; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50231026401-002; S; M; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50331026401-003; NS; PS; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50231026401-004; S; PS; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50331026401-005; NS; PS; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50331026402-001; NS; D; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50231026402-002; S; D; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50331026402-003; NS; D; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50231026402-004; S; D; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50331026402-005; NS; D; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50231026402-006; S; D; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50331026402-007; NS; D; F; 10/03/85.

Georgia International Life Insurance Co; Atlanta, GA; 50231026402-008; S; D; F; 10/03/85.

Glens Falls National Bank & Trust Co; Glens Falls, NY; 50331190001-001; NS; PS; F; 10/30/85.

Glens Falls National Bank & Trust Co; Glens Falls, NY; 50331190001-002; NS; M; F; 10/30/85.

Glens Falls National Bank & Trust Co; Glens Falls, NY; 50331190001-003; NS; T; F; 10/28/85.

Glens Falls National Bank & Trust Co; Glens Falls, NY; 50331190002-001; NS; D; F; 10/30/85.

Glens Falls National Bank & Trust Co; Glens Falls, NY; 50331190002-002; NS; D; F; 10/30/85.

Goodland State Bank; Goodland, IN; 50231311801-001; P; M; F; 10/03/85.

Goodland State Bank; Goodland, IN; 50231311801-002; P; PS; F; 10/03/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50279606201-001; P; D; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50379606201-002; NS; D; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50279606201-003; P; D; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50379606201-004; NS; D; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50279606202-001; P; PS; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50379606202-002; NS; PS; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50279606202-003; P; M; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50379606202-004; NS; M; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50279606202-005; P; PS; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50279606202-006; P; M; F; 10/31/85.

Great Southwest Surplus Lines Insurance Co; Stevens Point, WI; 50379606202-007; NS; T; F; 10/31/85.

Great Western Savings & Loan; Northridge, CA; 50265310001-001; P; PS; F; 11/15/85.

Great Western Savings & Loan; Northridge, CA; 50265310001-002; P; M; F; 11/15/85.

Greater Providence Deposit Corp; Proidence, RI; 50231670001-001; S; PS; F; 10/30/85.

Greater Providence Deposit Corp; Proidence, RI; 50231670001-002; S; M; F; 10/30/85.

Grenada Bank; Grenada, MS; 50331790001-001; NS; PS; F; 12/28/85.

Grenada Bank; Grenada, MS; 50231790001-002; S; PS; F; 12/28/85.

Grenada Bank; Grenada, MS; 50331790001-003; NS; M; F; 12/28/85.

Grenada Bank; Grenada, MS; 50231790001-004; S; M; F; 12/28/85.

Grenada Bank; Grenada, MS; 50331790001-005; NS; T; F; 12/28/85.

Grenada Bank; Grenada, MS; 50231790001-006; S; T; F; 12/28/85.

Guaranty Bank & Trust Co; Worcester, MA; 50332094402-001; NS; D; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50332094402-002; NS; D; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094402-003; P; D; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094402-004; P; D; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094402-005; P; D; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094402-006; P; D; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50332094403-001; NS; PS; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50332094403-002; NS; M; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50332094403-003; NS; T; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50332094403-004; NS; PS; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094403-005; P; PS; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094403-006; P; M; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094403-007; P; T; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094403-008; P; PS; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094403-009; P; M; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094403-010; P; T; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094403-011; P; PS; F; 12/10/85.

Guaranty Bank & Trust Co; Worcester, MA; 50232094403-012; P; M; F; 12/10/85.

Hawkeye-Capital Bank & Trust; Des Moines, IA; 50232882201-001; P; PS; F; 12/04/85.

Hawkeye-Capital Bank & Trust; Des Moines, IA; 50232882201-002; P; M; F; 12/04/85.

Hawkeye-Capital Bank & Trust; Des Moines, IA; 50332882202-001; NS; PS; F; 12/04/85.

Hawkeye-Capital Bank & Trust; Des Moines, IA; 50332882202-002; NS; M; F; 12/04/85.

Heart Federal Savings & Loan; Auburn, CA; 50365520001-001; NS; M; F; 12/24/85.

Heart Federal Savings & Loan; Auburn, CA; 50365520001-002; NS; PS; F; 12/24/85.

Hertiage Bank NA; Cherry Hill, NJ; 50233100001-001; P; PS; F; 12/20/85.

Hertiage Bank NA; Cherry Hill, NJ; 50233100001-002; P; M; F; 12/20/85.

Hertiage Bank NA; Cherry Hill, NJ; 50333100001-003; NS; PS; F; 12/20/85.

Hertiage Bank NA; Cherry Hill, NJ; 50333100001-004; NS; M; F; 12/20/85.

Hertiage Bank NA; Cherry Hill, NJ; 50333100001-005; NS; PS; F; 12/20/85.

Hertiage Bank NA; Cherry Hill, NJ; 50333100001-006; NS; M; F; 12/20/85.

Hibernia Bank; San Francisco, CA; 50272440001-001; S; PS; F; 12/20/85.

Hibernia Bank; San Francisco, CA; 50272440001-002; S; M; F; 12/20/85.

Hillsborough National Bank; Belle Mead, NJ; 50272750001-001; P; PS; F; 12/26/85.

Hillsborough National Bank; Belle Mead, NJ; 50272750001-002; P; M; F; 12/26/85.

Home Investors Fund Inc; Valley Forge, PA; 50380275101-001; NS; M; F; 10/09/85.

Home Investors Fund Inc; Valley Forge, PA; 50280275101-002; P; M; F; 10/09/85.

Home Investors Fund Inc; Valley Forge, PA; 50280275101-003; P; M; F; 10/09/85.

Home Investors Fund Inc; Valley Forge, PA; 50380275101-004; NS; PS; F; 10/09/85.
Home Investors Fund Inc; Valley Forge, PA; 50280275101-005; P; PS; F; 10/09/85.
Home Investors Fund Inc; Valley Forge, PA; 50280275101-006; P; PS; F; 10/09/85.
Home Investors Fund Inc; Valley Forge, PA; 50380275102-001; NS; D; F; 10/09/85.
Home Investors Fund Inc; Valley Forge, PA; 50380275102-002; NS; D; F; 10/09/85.
Home Investors Fund Inc; Valley Forge, PA, 50280275102-003; P; D; F; 10/09/85.
Home Investors Fund Inc; Valley Forge, PA; 50280275102-004; P; D; F; 10/09/85.
Home Investors Fund Inc; Valley Forge, PA; 50280275102-005; P; D; F; 10/09/85.
Home Savings of America Savings of America; Los Angeles, CA; 50233700001-001; P; PS; F; 12/24/85.
Home Savings of America Savings of America; Los Angeles, CA; 50233700001-002; P; M; F; 12/24/85.
Home Security Life Insurance Co; Durham, NC; 50332196401-001; NS; M; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50232196401-002; S; M; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50332196401-003; NS; PS; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50232196401-004; S; PS; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50332196401-005; NS; PS; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50332196402-001; NS; D; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50232196402-002; S; D; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50332196402-003; NS; D; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50232196402-004; S; D; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50332196402-005; NS; D; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50232196402-006; S; D; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50332196402-007; NS; D; F; 10/03/85.
Home Security Life Insurance Co; Durham, NC; 50232196402-008; S; D; F; 10/03/85.
Howard Bank; Burlington, VT; 50233930001-001; P; M; U; 11/21/85.
Howard Bank; Burlington, VT; 50233930001-002; P; PS; U; 11/21/85.
Huntington National Bank; Cincinnati, OH; 50234021902-001; S; D; F; 12/06/85.
Huntington National Bank; Cincinnati, OH; 50234021902-002; S; D; F; 12/06/85.
Huntington National Bank; Cincinnati, OH; 50234021902-003; S; D; F; 12/06/85.
Huntington National Bank; Cincinnati, OH; 50234021902-004; S; D; F; 12/06/85.
Huntington National Bank; Columbus, OH; 50334020001-001; NS; PS; F; 12/03/85.
Huntington National Bank; Columbus, OH; 50334020001-002; NS; PS; F; 12/03/85.
Huntington National Bank; Columbus, OH; 50234020001-003; S; PS; F; 12/03/85.
Huntington National Bank; Columbus, OH; 50334020001-004; NS; M; F; 12/03/85.
Huntington National Bank; Columbus, OH; 50334020001-005; NS; M; F; 12/03/85.
Huntington National Bank; Columbus, OH; 50234020001-006; S; PS; F; 12/05/85.
Huntington National Bank; Columbus, OH; 50234020001-007; S; M; F; 12/05/85.
Huntington National Bank; Columbus, OH; 50234020001-008; S; M; F; 12/05/85.
Hutton Investment Series; New York, NY; 50217270001-001; P; PS; F; 10/23/85.
Hutton Investment Series; New York, NY; 50217270001-002; P; M; F; 10/23/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50272686501-001; P; PS; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50272686501-002; P; M; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50272686501-003; P; T; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50272686501-004; P; PS; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50272686501-005; P; M; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50272686501-006; P; T; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50372686501-007; NS; PS; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50372686501-008; NS; M; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50272686502-001; P; D; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50272686502-002; P; D; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50372686502-003; NS; D; F; 12/30/85.
IDS Cash Management Fund Inc; Minneapolis, MN; 50372686502-004; NS; D; F; 12/30/85.
IDS Certificate Co; Minneapolis, MN; 50270490001-001; P; PS; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50270490001-002; M; T; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50270490001-003; P; T; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50270490001-004; P; PS; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50270490001-005; P; M; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50270490001-006; P; T; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50370490001-007; NS; PS; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50370490001-008; NS; M; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50270490002-001; P; D; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50270490002-002; P; D; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50370490002-003; NS; D; U; 10/29/85.
IDS Certificate Co; Minneapolis, MN; 50370490002-004; NS; D; U; 10/29/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50272696501-001; P; PS; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50272696501-002; P; M; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50272696501-003; P; T; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50272696501-004; P; PS; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50272696501-005; P; M; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50272696501-006; P; T; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50372696501-007; NS; PS; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50372696501-008; NS; M; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50272696502-001; P; D; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50272696502-002; P; D; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50372696502-003; NS; D; F; 12/30/85.
IDS Discovery Fund Inc; Minneapolis, MN; 50372696502-004; NS; D; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50235096501-001; P; PS; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50235096501-002; P; M; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50235096501-003; P; T; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50235096501-004; P; PS; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50235096501-005; P; M; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50235096501-006; P; T; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50335096501-007; NS; PS; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50335096501-008; NS; M; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50235096502-001; P; D; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50235096502-002; P; D; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50335096502-003; NS; D; F; 12/30/85.
IDS Financial Services Inc; Minneapolis, MN; 50335096502-004; NS; D; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50234096501-001; P; PS; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50234096501-002; P; M; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50234096501-003; P; T; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50234096501-004; P; PS; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50234096501-005; P; M; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50234096501-006; P; T; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50334096501-007; NS; PS; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50334096501-008; NS; M; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50234096502-001; P; D; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50234096502-002; P; D; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50334096502-003; NS; D; F; 12/30/85.
IDS Life Insurance Co; Minneapolis, MN; 50334096502-004; NS; D; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50232436501-001; P; PS; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50232436501-002; P; M; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50232436501-003; P; T; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50232436501-004; P; PS; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50232436501-005; P; M; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50232436501-006; P; T; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50332436501-007; NS; PS; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50332436501-008; NS; M; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50232436502-001; P; D; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50232436502-002; P; D; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50332436502-003; NS; D; F; 12/30/85.
IDS Life Insurance Co of New York; Albany, NY; 50332436502-004; NS; D; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50272706501-001; P; PS; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50272706501-002; P; M; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50272706501-003; P; T; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50272706501-004; P; PS; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50272706501-005; P; M; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50272706501-006; P; T; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50372706501-007; NS; PS; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50372706501-008; NS; M; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50272706502-001; P; D; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50272706502-002; P; D; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50372706502-003; NS; D; F; 12/30/85.
IDS Mutual Inc; Minneapolis, MN; 50372706502-004; NS; D; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50272716501-001; P; PS; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50272716501-002; P; M; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50272716501-003; P; T; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50272716501-004; P; PS; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50272716501-005; P; M; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50272716501-006; P; T; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50372716501-007; NS; PS; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50372716501-008; NS; M; F; 12/30/85.

IDS Selective Fund Inc; Minneapolis, MN; 50272716502-001; P; D; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50272716502-002; P; D; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50372716502-003; NS; D; F; 12/30/85.
IDS Selective Fund Inc; Minneapolis, MN; 50372716502-004; NS; D; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50272726501-001; P; PS; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50272726501-002; P; M; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50272726501-003; P; T; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50272726501-004; P; PS; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50272726501-005; P; M; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50272726501-006; P; T; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50372726501-007; NS; PS; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50372726501-008; NS; M; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50272726502-001; P; D; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50272726502-002; P; D; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50372726502-003; NS; D; F; 12/30/85.
IDS Stock Fund Inc; Minneapolis, MN; 50372726502-004; NS; D; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50272736501-001; P; PS; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50272736501-002; P; M; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50272736501-003; P; T; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50272736501-004; P; PS; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50272736501-005; P; M; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50272736501-006; P; T; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50372736501-007; NS; PS; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50372736501-008; NS; M; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50272736502-001; P; D; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50272736502-002; P; D; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50372736502-003; NS; D; F; 12/30/85.
IDS Trust Co; Minneapolis, MN; 50372736502-004; NS; D; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50272746501-001; P; PS; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50272746501-002; P; M; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50272746501-003; P; T; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50272746501-004; P; PS; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50272746501-005; P; M; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50272746501-006; P; T; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50372746501-007; NS; PS; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50372746501-008; NS; M; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50272746502-001; P; D; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50272746502-002; P; D; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50372746502-003; NS; D; F; 12/30/85.
IDS Variable Payment Fund Inc; Minneapolis, MN; 50372746502-004; NS; D; F; 12/30/85.
Industrial Trust & Savings Bank; Muncie, IN; 50234621801-001; P; M; F; 10/03/85.
Industrial Trust & Savings Bank; Muncie, IN; 50334621801-002; NS; M; F; 10/03/85.
Industrial Trust & Savings Bank; Muncie, IN; 50234621801-003; P; PS; F; 10/03/85.
Industrial Trust & Savings Bank; Muncie, IN; 50334621801-004; NS; PS; F; 10/03/85.
IntraWest Bank of Grand Junction; Grand Junction, CO; 50357562201-001; NS; PS; F; 12/06/85.
IntraWest Bank of Grand Junction; Grand Junction, CO; 50357562201-002; NS; M; F; 12/06/85.
Investment Portfolios Inc; Chicago, IL; 50273288201-001; P; PS; F; 11/14/85.
Investment Portfolios Inc; Chicago, IL; 50273288201-002; P; M; F; 11/14/85.
Investment Portfolios Inc; Chicago, IL; 50373288201-003; NS; PS; F; 11/14/85.
Investment Portfolios Inc; Chicago, IL; 50373288201-004; NS; M; F; 11/14/85.
Iowa Bankers Association; Des Moines, IA; 50235222201-001; P; PS; F; 12/09/85.
Iowa Bankers Association; Des Moines, IA; 50235222201-002; P; M; F; 12/09/85.
Iowa Bankers Association; Des Moines, IA; 50235222201-003; P; PS; F; 12/09/85.
Iowa Bankers Association; Des Moines, IA; 50235222201-004; P; M; F; 12/09/85.
Ivest Fund Inc; Valley Forge, PA; 50380285101-001; NS; M; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50280285101-002; P; M; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50280285101-003; P; M; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50380285101-004; NS; PS; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50280285101-005; P; PS; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50280285101-006; P; PS; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50380285102-001; NS; D; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50380285102-002; NS; D; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50280285102-003; P; D; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50280285102-004; P; D; F; 10/09/85.
Ivest Fund Inc; Valley Forge, PA; 50280285102-005; P; D; F; 10/09/85.
J C Bradford & Co; Nashville, TN; 50208723501-007; P; PS; U; 10/30/85.
J C Bradford & Co; Nashville, TN; 50208723501-009; P; M; U; 10/30/85.
Jackson County Bank; Seymour, IN; 50235414501-001; P; PS; F; 10/07/85.
Jackson County Bank; Seymour, IN; 50335414501-002; NS; PS; F; 10/07/85.
Jackson County Bank; Seymour, IN; 50235414501-003; P; M; F; 10/07/85.
Jackson County Bank; Seymour, IN; 50335414501-004; NS; M; F; 10/07/85.
Jasper State Bank; Jasper, IN; 50370484501-001; NS; PS; F; 10/07/85.
Jefferson Guaranty Bank; Metairie, LA; 50235551904-001; S; D; F; 12/06/85.
Jefferson Guaranty Bank; Metairie, LA; 50235551904-002; S; D; F; 12/06/85.
Jefferson Guaranty Bank; Metairie, LA; 50235551904-003; S; D; F; 12/06/85.
Jefferson Guaranty Bank; Metairie, LA; 50235551904-004; S; D; F; 12/06/85.
Jefferson Guaranty Bank; Metairie, LA; 50335551904-005; NS; D; F; 12/06/85.
Jefferson Guaranty Bank; Metairie, LA; 50335551904-006; NS; D; F; 12/06/85.
Jefferson Guaranty Bank; Metairie, LA; 50335551904-007; NS; D; F; 12/06/85.
Jefferson Guaranty Bank; Metairie, LA; 50335551904-008; NS; D; F; 12/06/85.
Kanaly Trust Co; Houston, TX; 50335780001-001; NS; M; F; 12/19/85.
Kanaly Trust Co; Houston, TX; 50335780001-002; NS; M; F; 12/19/85.
Kanaly Trust Co; Houston, TX; 50335780001-003; NS; PS; F; 12/19/85.
Kanaly Trust Co; Houston, TX; 50335780001-004; NS; PS; F; 12/19/85.
Kansas American Bank; Overland Park, KS; 50273373401-001; P; M; F; 10/07/85.
Kansas American Bank; Overland Park, KS; 50273373401-002; P; PS; F; 10/07/85.
Kansas American Bank; Overland Park, KS; 50273373401-003; P; PS; F; 10/07/85.
Kansas American Bank; Overland Park, KS; 50273373401-004; P; M; F; 10/07/85.
Kansas American Bank; Overland Park, KS; 50273373402-001; S; D; F; 10/07/85.
Kansas American Bank; Overland Park, KS; 50273373402-002; S; D; F; 10/07/85.
Kemper Financial Services Inc; Chicago, IL; 50235998202-001; P; PS; F; 11/14/85.
Kemper Financial Services Inc; Chicago, IL; 50235998202-002; P; M; F; 11/14/85.
Kemper Financial Services Inc; Chicago, IL; 50335998202-003; NS; PS; F; 11/14/85.
Kemper Financial Services Inc; Chicago, IL; 50335998202-004; NS; M; F; 11/14/85.
Kemper Government Money Market Fund Inc; Chicago, IL; 50273168201-001; P; PS; F; 11/14/85.
Kemper Government Money Market Fund Inc; Chicago, IL; 50273168201-002; P; M; F; 11/14/85.
Kemper Government Money Market Fund Inc; Chicago, IL; 50373168201-003; NS; PS; F; 11/14/85.
Kemper Government Money Market Fund Inc; Chicago, IL; 50373168201-004; NS; M; F; 11/14/85.
Kemper Growth Fund Inc; Chicago, IL; 50264378201-001; P; PS; F; 11/14/85.
Kemper Growth Fund Inc; Chicago, IL; 50264378201-002; P; M; F; 11/14/85.
Kemper Growth Fund Inc; Chicago, IL; 50364378201-003; NS; PS; F; 11/14/85.
Kemper Growth Fund Inc; Chicago, IL; 50364378201-004; NS; M; F; 11/14/85.
Kemper High Yield Fund Inc; Chicago, IL; 50273228201-001; P; PS; F; 11/14/85.
Kemper High Yield Fund Inc; Chicago, IL; 50273228201-002; P; M; F; 11/14/85.
Kemper High Yield Fund Inc; Chicago, IL; 50373228201-003; NS; PS; F; 11/14/85.
Kemper High Yield Fund Inc; Chicago, IL; 50373228201-004; NS; M; F; 11/14/85.
Kemper Income & Capital Preservation Fund Inc; Chicago, IL; 50273218201-001; P; PS; F; 11/14/85.
Kemper Income & Capital Preservation Fund Inc; Chicago, IL; 50273218201-002; P; M; F; 11/14/85.
Kemper Income & Capital Preservation Fund Inc; Chicago, IL; 50373218201-003; NS; PS; F; 11/14/85.
Kemper Income & Capital Preservation Fund Inc; Chicago, IL; 50373218201-004; NS; M; F; 11/14/85.
Kemper International Fund Inc; Chicago, IL; 50273258201-001; P; PS; F; 11/14/85.
Kemper International Fund Inc; Chicago, IL; 50273258201-002; P; M; F; 11/14/85.
Kemper International Fund Inc; Chicago, IL; 50373258201-003; NS; PS; F; 11/14/85.
Kemper International Fund Inc; Chicago, IL; 50373258201-004; NS; M; F; 11/14/85.
Kemper Money Market Fund Inc; Chicago, IL; 50273248201-001; P; PS; F; 11/14/85.
Kemper Money Market Fund Inc; Chicago, IL; 50273248201-002; P; M; F; 11/14/85.
Kemper Money Market Fund Inc; Chicago, IL; 50373248201-003; NS; PS; F; 11/14/85.
Kemper Money Market Fund Inc; Chicago, IL; 50373248201-004; NS; M; F; 11/14/85.
Kemper Option Income Fund Inc; Chicago, IL; 50273238201-001; P; PS; F; 11/14/85.
Kemper Option Income Fund Inc; Chicago, IL; 50273238201-002; P; M; F; 11/14/85.
Kemper Option Income Fund Inc; Chicago, IL; 50373238201-003; NS; PS; F; 11/14/85.
Kemper Option Income Fund Inc; Chicago, IL; 50373238201-004; NS; M; F; 11/14/85.
Kemper Summit Fund Inc; Chicago, IL; 50273208201-001; P; PS; F; 11/14/85.
Kemper Summit Fund Inc; Chicago, IL; 50273208201-002; P; M; F; 11/14/85.
Kemper Summit Fund Inc; Chicago, IL; 50373208201-003; NS; PS; F; 11/14/85.
Kemper Summit Fund Inc; Chicago, IL; 50373208201-004; NS; M; F; 11/14/85.
Kemper Total Return Fund Inc; Chicago, IL; 50273278201-001; P; PS; F; 11/14/85.
Kemper Total Return Fund Inc; Chicago, IL; 50273278201-002; P; M; F; 11/14/85.
Kemper Total Return Fund Inc; Chicago, IL; 50373278201-003; NS; PS; F; 11/14/85.
Kemper Total Return Fund Inc; Chicago, IL; 50373278201-004; NS; M; F; 11/14/85.
Kemper United States Government Securities Fund Inc; Chicago, IL; 50273268201-001; P; PS; F; 11/14/85.

Kemper United States Government Securities Fund Inc; Chicago, IL; 50273268201-002; P; M; F; 11/14/85.

Kemper United States Government Securities Fund Inc; Chicago, IL; 50373268201-003; NS; PS; F; 11/14/85.

Kemper United States Government Securities Fund Inc; Chicago, IL; 50373268201-004; NS; M; F; 11/14/85.

Kentland Bank; Kentland, IN; 50236084501-001; P; PS; F; 10/07/85.

Kentland Bank; Kentland, IN; 50336084501-002; NS; PS; F; 10/07/85.

Kentland Bank; Kentland, IN; 50236084501-003; P; M; F; 10/07/85.

Kentland Bank; Kentland, IN; 50336084501-004; NS; M; F; 10/07/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50373006401-001; NS; M; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50273006401-002; S; M; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50373006401-003; NS; PS; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50273006401-004; S; PS; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50373006401-005; NS; PS; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50373006402-001; NS; D; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50273006402-002; S; D; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50373006402-003; NS; D; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50273006402-004; S; D; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50373006402-005; NS; D; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50273006402-006; S; D; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50373006402-007; NS; D; F; 10/03/85.

Kentucky Bonded Funeral Insurance Co; Louisville, KY; 50273006402-008; S; D; F; 10/03/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50378904401-001; NS; D; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50378904401-002; NS; D; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904401-003; P; D; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904401-004; P; D; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904401-005; P; D; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904401-006; P; D; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50378904402-001; NS; PS; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50378904402-002; NS; M; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50378904402-003; NS; T; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50378904402-004; NS; PS; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904402-005; P; PS; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904402-006; P; M; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904402-007; P; T; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904402-008; P; PS; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904402-009; P; M; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904402-010; P; T; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904402-011; P; PS; F; 12/10/85.

Keystone Massachusetts Distributors Inc; Boston, MA; 50278904402-012; P; M; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50336194401-001; NS; D; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50336194401-002; NS; D; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194401-003; P; D; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194401-004; P; D; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194401-005; P; D; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194401-006; P; D; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194401-007; P; D; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194401-008; P; D; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50336194402-001; NS; PS; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50336194402-002; NS; M; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50336194402-003; NS; T; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50336194402-004; NS; PS; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-005; P; PS; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-006; P; M; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-007; P; T; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-008; P; PS; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-009; P; M; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-010; P; T; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-011; P; PS; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-012; P; M; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-013; P; T; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-014; P; PS; F; 12/10/85.

Keystone Provident Life Insurance Co; Boston, MA; 50236194402-015; P; M; F; 12/10/85.

Lafayette Bank & Trust Co; Lafayette, IN; 50236441801-001; P; M; F; 10/03/85.

Lafayette Bank & Trust Co; Lafayette, IN; 50336441801-002; NS; M; F; 10/03/85.

Lafayette Bank & Trust Co; Lafayette, IN; 50236441801-003; P; PS; F; 10/03/85.

Lafayette Bank & Trust Co; Lafayette, IN; 50336441801-004; NS; PS; F; 10/03/85.

Lake City Bank; Warsaw, IN; 50236481801-001; P; M; F; 10/03/85.

Lake City Bank; Warsaw, IN; 50236481801-002; P; PS; F; 10/03/85.

Lake Shore National Bank; Chicago, IL; 50236510001-001; S; M; F; 12/19/85.

Lake Shore National Bank; Chicago, IL; 50236510001-002; S; PS; F; 12/19/85.

Lake Shore National Bank; Chicago, IL; 50236510002-001; S; PS; F; 12/19/85.

Lake Shore National Bank; Chicago, IL; 50236510002-002; S; M; F; 12/19/85.

Lake Shore National Bank; Chicago, IL; 50336510002-003; NS; M; F; 12/19/85.

Lake Shore National Bank; Chicago, IL; 50336510002-004; NS; PS; F; 12/19/85.

Liberty Norstar Bank NA; Buffalo, NY; 50337190001-001; NS; PS; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50237190001-002; S; PS; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50337190001-003; NS; PS; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50237190001-004; S; PS; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50337190001-005; NS; M; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50237190001-006; S; M; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50337190001-007; NS; M; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50237190001-008; S; M; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50337190001-009; NS; T; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50237190001-010; S; T; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50337190001-011; NS; T; F; 11/18/85.

Liberty Norstar Bank NA; Buffalo, NY; 50237190001-012; S; T; F; 11/18/85.

Life Insurance Co of North America; Philadelphia, PA; 50337340001-001; NS; PS; F; 12/03/85.

Life Insurance Co of North America; Philadelphia, PA; 50337340001-002; NS; PS; F; 12/03/85.

Life Insurance Co of North America; Philadelphia, PA; 50237340001-003; S; PS; F; 12/05/85.

Life Insurance Co of North America; Philadelphia, PA; 50337340001-004; NS; M; F; 12/05/85.

Life Insurance Co of North America; Philadelphia, PA; 50237340001-005; S; M; F; 12/03/85.

Lincoln National Bank & Trust Co; Fort Wayne, IN; 50237581801-001; P; M; F; 10/03/85.

Lincoln National Bank & Trust Co; Fort Wayne, IN; 50337581801-002; NS; M; F; 10/03/85.

Lincoln National Bank & Trust Co; Fort Wayne, IN; 50237581801-003; P; PS; F; 10/03/85.

Lincoln National Bank & Trust Co; Fort Wayne, IN; 50337581801-004; NS; PS; F; 10/03/85.

Lincoln National Bank & Trust Co; Fort Wayne, IN; 50237581801-005; P; T; F; 10/03/85.

Lincoln National Bank & Trust Co; Fort Wayne, IN; 50337581801-006; NS; T; F; 10/03/85.

Lincoln Trust Co; Denver, CO; 50337642201-001; NS; PS; F; 12/05/85.

Lincoln Trust Co; Denver, CO; 50337642201-002; NS; M; F; 12/05/85.

Lincoln Trust Co; Denver, CO; 50237642202-001; P; PS; F; 12/05/85.

Lincoln Trust Co; Denver, CO; 50237642202-002; P; M; F; 12/05/85.

Lincoln Trust Co; Denver, CO; 50237642202-003; P; PS; F; 12/05/85.

Lincoln Trust Co; Denver, CO; 50237642202-004; P; M; F; 12/05/85.

Livestock Marketing Association; Kansas City, MO; 50373343401-001; NS; PS; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50373343401-002; NS; PS; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50373343401-003; NS; PS; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50373343401-004; NS; PS; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50273343401-005; P; PS; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50373343401-006; NS; M; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50373343401-007; NS; M; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50373343401-008; NS; M; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50373343401-009; NS; M; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50273343401-010; P; M; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50273343401-011; P; PS; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50273343401-012; P; M; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50373343402-001; NS; D; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50373343402-002; NS; D; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50273343402-003; S; D; F; 10/07/85.

Livestock Marketing Association; Kansas City, MO; 50273343402-004; S; D; F; 10/07/85.

Louisiana Bank & Trust Co; Shreveport, LA; 50237852201-001; P; PS; F; 12/04/85.

Louisiana Bank & Trust Co; Shreveport, LA; 50237852201-002; P; M; F; 12/04/85.

Louisiana Bank & Trust Co; Shreveport, LA; 50337852202-001; NS; PS; F; 12/04/85.

Louisiana Bank & Trust Co; Shreveport, LA; 50337852202-002; NS; M; F; 12/04/85.

Louisiana Bank & Trust Co; Shreveport, LA; 50337852203-001; NS; D; F; 12/04/85.

Louisiana Bank & Trust Co; Shreveport, LA; 50337852203-002; NS; D; F; 12/04/85.

Louisiana Bank & Trust Co; Shreveport, LA; 50337852203-003; NS; D; F; 12/04/85.

Louisiana Bank & Trust Co; Shreveport, LA; 50337852203-004; NS; D; F; 12/04/85.

Louisiana Bank & Trust Co; Shreveport, LA; 50337852203-005; NS; D; F; 12/04/85.

Lyndonville Savings Bank & Trust Co; Lyndonville, VT; 50248070001-001; S; PS; F; 11/26/85.

Lyndonville Savings Bank & Trust Co; Lyndonville, VT; 50248070001-002; S; M; F; 11/26/85.

Madison Bank & Trust Co; Madison, IN; 50238084501-001; P; PS; F; 10/07/85.

Madison Bank & Trust Co; Madison, IN; 50338084501-002; NS; PS; F; 10/07/85.

Madison Bank & Trust Co; Madison, IN; 50238084501-003; P; M; F; 10/07/85.

Madison Bank & Trust Co; Madison, IN; 50338084501-004; NS; M; F; 10/07/85.

Maine National Bank; Portland, ME; 50238240001-001; S; M; F; 10/23/85.

Maine National Bank; Portland, ME; 50338240001-002; NS; M; F; 10/30/85.

Maine National Bank; Portland, ME; 50238240001-003; S; PS; F; 10/23/85.

Maine National Bank; Portland, ME; 50338240001-004; NS; PS; F; 10/23/85.

Maine National Bank; Portland, ME; 50238240001-005; S; T; F; 10/23/85.

Maine National Bank; Portland, ME; 50338240001-006; NS; T; F; 10/23/85.

Manufacturers Hanover Trust Co; New York, NY; 50238410001-001; P; M; F; 12/19/85.

Manufacturers Hanover Trust Co; New York, NY; 50238410001-002; P; M; F; 12/19/85.

Manufacturers Hanover Trust Co; New York, NY; 50238410001-003; P; PS; F; 12/19/85.

Manufacturers Hanover Trust Co; New York, NY; 50238410001-004; P; PS; F; 12/19/85.

Manufacturers National Bank of Detroit; Detroit, MI; 50338430001-001; NS; PS; F; 10/23/85.

Manufacturers National Bank of Detroit; Detroit, MI; 50238430001-002; S; PS; F; 10/23/85.

Manufacturers National Bank of Detroit; Detroit, MI; 50338430001-003; NS; M; F; 10/23/85.

Manufacturers National Bank of Detroit; Detroit, MI; 50238430001-004; S; M; F; 10/23/85.

Manufacturers National Bank of Detroit; Detroit, MI; 50338430002-001; NS; D; F; 10/23/85.

Manufacturers National Bank of Detroit; Detroit, MI; 50238430002-002; S; D; F; 10/23/85.

Manufacturers National Bank of Detroit; Detroit, MI; 50338430002-003; NS; D; F; 10/23/85.

Manufacturers National Bank of Detroit; Detroit, MI; 50238430002-004; S; D; F; 10/23/85.

Maplewood Bank & Trust Co; Maplewood, NJ; 50238460001-001; P; PS; F; 12/26/85.

Maplewood Bank & Trust Co; Maplewood, NJ; 50238460001-002; P; M; F; 12/26/85.

Marine Midland Bank NA; Buffalo, NY; 50238560001-001; P; PS; F; 12/19/85.

Marine Midland Bank NA; Buffalo, NY; 50238560001-002; P; M; F; 12/19/85.

Marine Midland Bank NA; Buffalo, NY; 50338560001-003; NS; PS; F; 12/19/85.

Marine Midland Bank NA; Buffalo, NY; 50338560001-004; NS; M; F; 12/19/85.

Massachusetts Cooperative Bank League; Boston, MA; 50255850001-001; S; PS; F; 11/15/85.

McCready & Keene Inc; Indianapolis, IN; 50299181801-001; P; M; F; 10/03/85.

McCready & Keene Inc; Indianapolis, IN; 50399181801-002; NS; M; F; 10/03/85.

McCready & Keene Inc; Indianapolis, IN; 50299181801-003; P; PS; F; 10/03/85.

McCready & Keene Inc; Indianapolis, IN; 50399181801-004; NS; PS; F; 10/03/85.

McCready & Keene Inc; Indianapolis, IN; 50299181801-005; P; T; F; 10/03/85.

McCready & Keene Inc; Indianapolis, IN; 50399181801-006; NS; T; F; 10/03/85.

Medford National Bank; Medford, WI; 50239127001-001; S; PS; F; 10/11/85.

Medford National Bank; Medford, WI; 50239127001-002; S; PS; F; 10/11/85.

Medford National Bank; Medford, WI; 50239127001-003; S; M; F; 10/11/85.

Medford National Bank; Medford, WI; 50239127001-004; S; M; F; 10/11/85.

Medford National Bank; Medford, WI; 50339127001-005; NS; PS; F; 10/11/85.

Medford National Bank; Medford, WI; 50339127001-006; NS; PS; F; 10/11/85.

Medford National Bank; Medford, WI; 50339127001-007; NS; M; F; 10/11/85.

Medford National Bank; Medford, WI; 50339127001-008; NS; M; F; 10/11/85.

Merchants National Bank & Trust Co; Indianapolis, IN; 50239691801-001; P; M; F; 10/03/85.

Merchants National Bank & Trust Co; Indianapolis, IN; 50339691801-002; NS; M; F; 10/03/85.

Merchants National Bank & Trust Co; Indianapolis, IN; 50239691801-003; P; PS; F; 10/03/85.

Merchants National Bank & Trust Co; Indianapolis, IN; 50339691801-004; NS; PS; F; 10/03/85.

Merchants National Bank of Cedar Rapids; Cedar Rapids, IA; 50239731103-001; S; PS; F; 10/18/85.

Merchants National Bank of Cedar Rapids; Cedar Rapids, IA; 50239731103-002; S; M; F; 10/18/85.

Merchants National Bank of Muncie; Muncie, IN; 50239751801-001; P; M; F; 10/03/85.

Merchants National Bank of Muncie; Muncie, IN; 50339751801-002; NS; M; F; 10/03/85.

Merchants National Bank of Muncie; Muncie, IN; 50239751801-003; P; PS; F; 10/03/85.

Merchants National Bank of Muncie; Muncie, IN; 50339751801-004; NS; PS; F; 10/03/85.

Merchants National Bank of Terre Haute; Terre Haute, IN; 50239781801-001; P; M; F; 10/03/85.

Merchants National Bank of Terre Haute; Terre Haute, IN; 50339781801-002; NS; M; F; 10/03/85.

Merchants National Bank of Terre Haute; Terre Haute, IN; 50239781801-003; P; PS; F; 10/03/85.

Merchants National Bank of Terre Haute; Terre Haute, IN; 50339781801-004; NS; PS; F; 10/03/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353401-001; NS; PS; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353401-002; NS; PS; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353401-003; NS; PS; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353401-004; NS; PS; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353401-005; P; PS; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353401-006; NS; M; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353401-007; NS; M; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353401-008; NS; M; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353401-009; NS; M; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353401-010; P; M; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353401-011; P; PS; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353401-012; P; M; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353401-013; S; M; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353401-014; S; PS; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353401-015; S; PS; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353401-016; S; M; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353402-001; NS; D; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50373353402-002; NS; D; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353402-003; S; D; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353402-004; S; D; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353402-005; S; D; F; 10/07/85.

Merchants National Bank of Topeka; Topeka, KS; 50273353402-006; S; D; F; 10/07/85.

Merchants Trust Co; Burlington, VT; 50219530001-001; P; M; F; 11/18/85.

Merchants Trust Co; Burlington, VT; 50219530001-002; P; PS; F; 11/18/85.

Merrill Trust Co; Bangor, ME; 50339830001-001; NS; PS; F; 11/26/85.

Merrill Trust Co; Bangor, ME; 50339830001-002; NS; M; F; 11/26/85.

Merrill Trust Co; Bangor, ME; 50339830001-003; NS; PS; F; 11/26/85.

Merrill Trust Co; Bangor, ME; 50339830001-004; NS; M; F; 11/26/85.

Merrill Trust Co; Bangor, ME; 50239830001-005; P; PS; F; 11/26/85.

Merrill Trust Co; Bangor, ME; 50239830001-006; P; M; F; 11/26/85.

Merrill Trust Co; Bangor, ME; 50239830001-007; S; PS; F; 11/26/85.

Merrill Trust Co; Bangor, ME; 50239830001-008; P; M; F; 11/26/85.

Michigan League of Savings Institutions; Lansing, MI; 50240160001-001; P; PS; F; 12/19/85.

Michigan League of Savings Institutions; Lansing, MI; 50240160001-002; P; M; F; 12/19/85.

Mid South Bank & Trust Co; Murfreesboro, TN; 50241353501-007; P; PS; U; 10/30/85.

Mid South Bank & Trust Co; Murfreesboro, TN; 50241353501-009; P; M; U; 10/30/85.

Middlesex Insurance Co; Stevens Point, WI; 50279616201-001; P; D; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50379616201-002; NS; D; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50279616201-003; P; D; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50379616201-004; NS; D; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50279616202-001; P; PS; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50379616202-002; NS; PS; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50279616202-003; P; M; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50379616202-004; NS; M; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50279616202-005; P; PS; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50279616202-006; P; M; F; 10/31/85.

Middlesex Insurance Co; Stevens Point, WI; 50379616202-007; NS; T; F; 10/31/85.

Midland National Life Insurance Co; Sioux Falls, SD; 50240560001-001; S; PS; U; 12/03/85.

Midland National Life Insurance Co; Sioux Falls, SD; 50240560002-001; S; M; U; 12/03/85.

Midland National Life Insurance Co; Sioux Falls, SD; 50240560003-001; S; D; U; 12/03/85.

Midwest Commerce Banking Co; Elkhart, IN; 50252790001-001; P; PS; F; 12/20/85.

Midwest Commerce Banking Co; Elkhart, IN; 50252790001-002; P; M; F; 12/28/85.

Midwest Commerce Banking Co; Elkhart, IN; 50352790001-003; NS; PS; F; 12/20/85.

Midwest Commerce Banking Co; Elkhart, IN; 50352790001-004; NS; M; F; 12/28/85.

Midwest Commerce Banking Co; Elkhart, IN; 50352790001-005; NS; PS; F; 12/20/85.

Midwest Commerce Banking Co; Elkhart, IN; 50352790001-006; NS; M; F; 12/28/85.

Missouri Restaurant Association; Kansas City, MO; 50373363401-001; NS; PS; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50373363401-002; NS; PS; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50373363401-003; NS; PS; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50373363401-004; NS; PS; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50273363401-005; P; PS; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50373363401-006; NS; M; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50373363401-007; NS; M; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50373363401-008; NS; M; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50373363401-009; NS; M; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50273363401-010; P; M; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50273363401-011; P; PS; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50273363401-012; P; M; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50373363402-001; NS; D; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50373363402-002; NS; D; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50273363402-003; S; D; F; 10/07/85.

Missouri Restaurant Association; Kansas City, MO; 50273363402-004; S; D; F; 10/07/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50299474701-001; S; PS; F; 10/31/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50299474701-002; S; M; F; 10/31/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50399474701-003; NS; PS; F; 10/31/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50399474701-004; NS; M; F; 10/31/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50399474701-005; NS; PS; F; 10/31/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50399474701-006; NS; M; F; 10/31/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50399474702-001; NS; D; F; 10/31/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50399474702-002; NS; D; F; 10/31/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50399474702-003; NS; D; F; 10/31/85.

Modrall Sperling Roehl Harris & Sisk PA; Albuquerque, NM; 50399474702-004; NS; D; F; 10/31/85.

Monona Grove State Bank; Madison, WI; 50240990001-001; S; PS; F; 12/05/85.

Monona Grove State Bank; Madison, WI; 50240990001-002; S; M; F; 12/05/85.

Monona Grove State Bank; Madison, WI; 50240997002-001; S; PS; U; 10/31/85.

Monona Grove State Bank; Madison, WI; 50240997002-002; S; PS; U; 10/31/85.

Monona Grove State Bank; Madison, WI; 50240997002-003; S; M; U; 10/31/85.

Monona Grove State Bank; Madison, WI; 50240997002-004; S; M; U; 10/31/85.

Monona Grove State Bank; Madison, WI; 50340997002-005; NS; PS; U; 10/31/85.

Monona Grove State Bank; Madison, WI; 50340997002-006; NS; PS; U; 10/31/85.

Monona Grove State Bank; Madison, WI; 50340997002-007; NS; M; U; 10/31/85.

Monona Grove State Bank; Madison, WI; 50340997002-008; NS; M; U; 10/31/85.

Mutual Life Insurance Co of New York; New York, NY; 50241430001-001; S; PS; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50341430001-002; NS; PS; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50241430002-001; S; T; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50341430002-002; NS; T; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50241430003-001; S; M; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50341430003-002; NS; M; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50241430004-001; S; D; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50341430004-002; NS; D; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50241430004-003; S; D; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50341430004-004; NS; D; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50341430005-001; NS; D; F; 12/23/85.

Mutual Life Insurance Co of New York; New York, NY; 50341430005-002; NS; D; F; 12/23/85.

Mutual Trust Bank; New Albany, IN; 50341521801-001; NS; M; F; 10/03/85.

Mutual Trust Bank; New Albany, IN; 50341521801-002; NS; PS; F; 10/03/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50380295101-001; NS; M; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50280295101-002; P; M; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50280295101-003; P; M; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50380295101-004; NS; PS; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50280295101-005; P; PS; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50280295101-006; P; PS; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50380295102-001; NS; D; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50380295102-002; NS; D; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50280295102-003; P; D; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50280295102-004; P; D; F; 10/09/85.

Naess & Thomas Special Fund Inc; Valley Forge, PA; 50280295102-005; P; D; F; 10/09/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50341634401-001; NS; D; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50341634401-002; NS; D; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634401-003; P; D; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634401-004; P; D; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634401-005; P; D; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634401-006; P; D; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50341634402-001; NS; PS; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50341634402-002; NS; M; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50341634402-003; NS; T; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50341634402-004; NS; PS; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634402-005; P; PS; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634402-006; P; M; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634402-007; P; T; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634402-008; P; PS; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634402-009; P; M; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634402-010; P; T; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634402-011; P; PS; F; 12/10/85.

National Association of Business People Educators & Professionals; Waltham, MA; 50241634402-012; P; M; F; 12/10/85.

National Association of Realtors; Chicago, IL; 50341660001-001; NS; PS; F; 12/19/85.

National Association of Realtors; Chicago, IL; 50241660001-002; S; PS; F; 12/19/85.

National Association of Realtors; Chicago, IL; 50241660001-003; S; M; F; 12/19/85.

National Association of Realtors; Chicago, IL; 50341660001-004; NS; M; F; 12/19/85.

National Automobile Dealers Association; McLean, VA; 50341680001-001; NS; M; F; 12/28/85.

National Automobile Dealers Association; McLean, VA; 50341680001-002; NS; PS; F; 12/28/85.

National Bank & Trust Co of South Bend; South Bend, IN; 50341730001-001; NS; M; F; 11/04/85.

National Bank & Trust Co of South Bend; South Bend, IN; 50341730001-002; NS; PS; F; 11/04/85.

National Bank & Trust Co of South Bend; South Bend, IN; 50341730002-001; NS; M; F; 11/04/85.

National Bank & Trust Co of South Bend; South Bend, IN; 50341730002-002; NS; M; F; 11/04/85.

National Bank & Trust Co of South Bend; South Bend, IN; 50341730003-001; NS; PS; F; 11/04/85.

National Bank & Trust Co of South Bend; South Bend, IN; 50341730003-002; NS; PS; F; 11/04/85.

National Bank of Commerce; Birmingham, AL; 50266893501-007; P; PS; U; 10/30/85.

National Bank of Commerce; Birmingham, AL; 50266893501-009; P; M; U; 10/30/85.

National Bank of Commerce of Charleston; Charleston, WV; 50341910001-001; NS; PS; F; 12/19/85.

National Bank of Commerce of Charleston; Charleston, WV; 50341910001-002; NS; PS; F; 12/19/85.

National Bank of Commerce of Charleston; Charleston, WV; 50341910002-001; NS; M; F; 12/19/85.

National Bank of Commerce of Charleston; Charleston, WV; 50341910002-002; NS; M; F; 12/19/85.

National Bank of Commerce of Mississippi; Columbus, MS; 50341900001-001; NS; PS; F; 12/26/85.

National Bank of Commerce of Mississippi; Columbus, MS; 50241900001-002; S; PS; F; 12/26/85.

National Bank of Commerce of Mississippi; Columbus, MS; 50341900001-003; NS; M; F; 12/23/85.

National Bank of Commerce of Mississippi; Columbus, MS; 50241900001-004; S; M; F; 12/26/85.

National Bank of Commerce of San Antonio; San Antonio, TX; 50241892202-001; P; PS; F; 12/04/85.

National Bank of Commerce of San Antonio; San Antonio, TX; 50241892202-002; P; M; F; 12/04/85.

National Bank of Greenwood; Greenwood, IN; 50242071801-001; P; M; F; 10/03/85.

National Bank of Greenwood; Greenwood, IN; 50342071801-002; NS; M; F; 10/03/85.

National Bank of Greenwood; Greenwood, IN; 50242071801-003; P; PS; F; 10/03/85.

National Bank of Greenwood; Greenwood, IN; 50342071801-004; NS; PS; F; 10/03/85.

National Enterprise Bank; Washington, DC; 50270310001-001; P; M; F; 10/23/85.

National Enterprise Bank; Washington, DC; 50370310001-002; NS; M; F; 10/23/85.

National Enterprise Bank; Washington, DC; 50270310001-003; P; PS; F; 10/23/85.

National Enterprise Bank; Washington, DC; 50370310001-004; NS; PS; F; 10/23/85.

National Home Life Assurance Co; Valley Forge, PA; 50342486401-001; NS; M; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50242486401-002; S; M; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50342486401-003; NS; PS; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50242486401-004; S; PS; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50342486401-005; NS; PS; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50342486402-001; NS; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50242486402-002; S; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50342486402-003; NS; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50242486402-004; S; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50342486402-005; NS; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50242486402-006; S; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50342486402-007; NS; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50242486402-008; S; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50372986401-001; NS; M; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50272986401-002; S; M; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50372986401-003; NS; PS; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50272986401-004; S; PS; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50372986401-005; NS; PS; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50372986402-001; NS; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50272986402-002; S; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50372986402-003; NS; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50272986402-004; S; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50372986402-005; NS; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50272986402-006; S; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50372986402-007; NS; D; F; 10/03/85.

National Home Life Assurance Co; Valley Forge, PA; 50272986402-008; S; D; F; 10/03/85.

National Liberty Corp; Valley Forge, PA; 50372996401-001; NS; M; F; 10/03/85.

National Liberty Corp; Valley Forge, PA; 50272996401-002; S; M; F; 10/03/85.

National Liberty Corp; Valley Forge, PA; 50372996401-003; NS; PS; F; 10/03/85.

National Liberty Corp; Valley Forge, PA; 50272996401-004; S; PS; F; 10/03/85.

National Liberty Corp; Valley Forge, PA; 50372996401-005; NS; PS; F; 10/03/85.

National Liberty Corp; Valley Forge, PA; 50372996402-001; NS; D; F; 10/03/85.

National Liberty Corp; Valley Forge, PA; 50272996402-002; S; D; F; 10/03/85.
National Liberty Corp; Valley Forge, PA; 50372996402-003; NS; D; F; 10/03/85.
National Liberty Corp; Valley Forge, PA; 50272996402-004; S; D; F; 10/03/85.
National Liberty Corp; Valley Forge, PA; 50372996402-005; NS; D; F; 10/03/85.
National Liberty Corp; Valley Forge, PA; 50272996402-006; S; D; F; 10/03/85.
National Liberty Corp; Valley Forge, PA; 50372996402-007; NS; D; F; 10/03/85.
National Liberty Corp; Valley Forge, PA; 50272996402-008; S; D; F, 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50342726401-001; NS; M; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50242726401-002; S; M; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50342726401-003; NS; PS; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50242726401-004; S; PS; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50342726401-005; NS; M; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50342726402-001; NS; D; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50242726402-002; S; D; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50342726402-003; NS; D; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50242726402-004; S; D; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50342726402-005; NS; D; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50242726402-006; S; D; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50342726402-007; NS; D; F; 10/03/85.
National Standard Life Insurance Co; Orlando, FL; 50242726402-008; S; D; F; 10/03/85.
NCNB National Bank of Florida; Orlando, FL; 50218110002-001; S; PS; F; 12/08/85.
NCNB National Bank of Florida; Orlando, FL; 50318110002-002; NS; PS; F; 12/08/85.
NCNB National Bank of Florida; Orlando, FL; 50218110002-003; S; M; F; 12/08/85.
NCNB National Bank of Florida; Orlando, FL; 50318110002-004; NS; M; F; 12/08/85.
NCNB National Bank of Florida; Tampa, FL; 50218110001-001; P; PS; F; 12/02/85.
NCNB National Bank of Florida; Tampa, FL; 50218110001-002; P; PS; F; 12/02/85.
NCNB National Bank of Florida; Tampa, FL; 50218110001-003; P; M; F; 12/02/85.
NCNB National Bank of Florida; Tampa, FL; 50218110001-004; P; M; F; 12/02/85.
NCNB National Bank of North Carolina; Charlotte, NC; 50243500001-001; P; PS; F; 12/08/85.
NCNB National Bank of North Carolina; Charlotte, NC; 50343500001-002; NS; PS; F; 12/08/85.
NCNB National Bank of North Carolina; Charlotte, NC; 50243500001-003; P; M; F; 12/08/85.
NCNB National Bank of North Carolina; Charlotte, NC; 50343500001-004; NS; M; F; 12/08/85.
New Hampshire Association of Savings Banks; Concord, NH; 50243037501-001; P; PS; F; 10/31/85.
New Hampshire Association of Savings Banks; Concord, NH; 50243037501-002; P; M; F; 10/31/85.
New Hampshire Association of Savings Banks; Concord, NH; 50243037501-003; P; PS; F; 10/31/85.
New Hampshire Association of Savings Banks; Concord, NH; 50243037501-004; P; M; F; 10/31/85.
Neworld Bank for Savings; Harrison, NY; 50243218601-001; S; M; F; 10/09/85.
Neworld Bank for Savings; Harrison, NY; 50243218601-002; S; M; F; 10/09/85.
Neworld Bank for Savings; Harrison, NY; 50343218601-003; NS; M; F; 10/09/85.
Neworld Bank for Savings; Harrison, NY; 50343218601-004; NS; M; F; 10/09/85.
Neworld Bank for Savings; Harrison, NY; 50243218601-005; S; PS; F; 10/09/85.
Neworld Bank for Savings; Harrison, NY; 50243218601-006; S; PS; F; 10/09/85.
Neworld Bank for Savings; Harrison, NY; 50343218601-007; NS; PS; F; 10/09/85.
Neworld Bank for Savings; Harrison, NY; 50343218601-008; NS; PS; F; 10/09/85.
Norstar Bank of Long Island; Glen Cove, NY; 50333000001-001; NS; PS; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50233000001-002; S; PS; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50333000001-003; NS; PS; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50233000001-004; S; PS; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50333000001-005; NS; M; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50233000001-006; S; M; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50333000001-007; NS; M; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50233000001-008; S; M; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50333000001-009; NS; T; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50233000001-010; S; T; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50333000001-011; NS; T; F; 11/19/85.
Norstar Bank of Long Island; Glen Cove, NY; 50233000001-012; S; T; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50343710001-001; NS; PS; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50243710001-002; S; PS; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50343710001-003; NS; PS; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50243710001-004; S; PS; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50343710001-005; NS; M; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50243710001-006; S; M; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50343710001-007; NS; M; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50243710001-008; S; M; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50343710001-009; NS; T; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50243710001-010; S; T; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50243710001-011; S; T; F; 11/19/85.
Norstar Bank of Maine; Portland, ME; 50343710001-012; NS; T; F; 11/19/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50333360001-001; NS; PS; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50233360001-002; S; PS; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50333360001-003; NS; PS; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50233360001-004; S; PS; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50333360001-005; NS; M; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50233360001-006; S; M; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50333360001-007; NS; M; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50233360001-008; S; M; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50333360001-009; NS; T; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50233360001-010; S; T; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50333360001-011; NS; T; F; 11/18/85.
Norstar Bank of the Hudson Valley NA; Charlotte, NY; 50233360001-012; S; T; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50353020001-001; NS; PS; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50253020001-002; S; PS; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50353020001-003; NS; PS; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50253020001-004; S; PS; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50353020001-005; NS; M; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50253020001-006; S; M; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50353020001-007; NS; M; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50253020001-008; S; M; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50353020001-009; NS; T; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50253020001-010; S; T; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50353020001-011; NS; T; F; 11/18/85.
Norstar Bank of Upstate New York; Albany, NY; 50253020001-012; S; T; F; 11/18/85.
North Carolina League of Savings Institutions; Raleigh, NC; 50343512201-001; NS; PS; F; 12/06/85.
North Carolina League of Savings Institutions; Raleigh, NC; 50343512201-002; NS; M; F; 12/06/85.
North Carolina League of Savings Institutions; Raleigh, NC; 50243512202-001; P; PS; F; 12/06/85.
North Carolina League of Savings Institutions; Raleigh, NC; 50243512202-002; P; M; F; 12/06/85.
Northampton Institution for Savings; Harrison, NY; 50243668601-001; S; M; F; 10/09/85.
Northampton Institution for Savings; Harrison, NY; 50243668601-002; S; M; F; 10/09/85.
Northampton Institution for Savings; Harrison, NY; 50343668601-003; NS; M; F; 10/09/85.
Northampton Institution for Savings; Harrison, NY; 50343668601-004; NS; M; F; 10/09/85.
Northampton Institution for Savings; Harrison, NY; 50243668601-005; S; PS; F; 10/09/85.
Northampton Institution for Savings; Harrison, NY; 50243668601-006; S; PS; F; 10/09/85.
Northampton Institution for Savings; Harrison, NY; 50343668601-007; NS; PS; F; 10/09/85.
Northampton Institution for Savings; Harrison, NY; 50343668601-008; NS; PS; F; 10/09/85.
Northeastern Bank of Pennsylvania; Scranton, PA; 50243810003-001; S; T; F; 12/26/85.
Northeastern Bank of Pennsylvania; Scranton, PA; 50343810003-002; NS; T; F; 12/26/85.
Northwood State Bank; Northwood, ND; 50244467001-001; S; PS; F; 10/11/85.
Northwood State Bank; Northwood, ND; 50244467001-002; S; PS; F; 10/11/85.
Northwood State Bank; Northwood, ND; 50244467001-003; S; M; F; 10/11/85.
Northwood State Bank; Northwood, ND; 50244467001-004; S; M; F; 10/11/85.
Northwood State Bank; Northwood, ND; 50344467001-005; NS; PS; F; 10/11/85.
Northwood State Bank; Northwood, ND; 50344467001-006; NS; PS; F; 10/11/85.
Northwood State Bank; Northwood, ND; 50344467001-007; NS; M; F; 10/11/85.
Northwood State Bank; Northwood, ND; 50344467001-008; NS; M; F; 10/11/85.
Nyhart Co; Indianapolis, IN; 50299454501-001; P; PS; F; 10/07/85.
Nyhart Co; Indianapolis, IN; 50399454501-002; NS; PS; F; 10/07/85.
Nyhart Co; Indianapolis, IN; 50299454501-003; P; M; F; 10/07/85.
Nyhart Co; Indianapolis, IN; 50399454501-004; NS; M; F; 10/07/85.
Oak Brook Bank; Oak Brook, IL; 50267240001-001; S; PS; F; 10/23/85.
Oak Brook Bank; Oak Brook, IL; 50267240001-002; S; M; F; 10/23/85.
Oak Brook Bank; Oak Brook, IL; 50267240001-003; S; PS; F; 12/23/85.
Oak Brook Bank; Oak Brook, IL; 50267240001-004; S; M; F; 10/23/85.
Ocean County National Bank; Pt Pleasant Beach, NJ; 50271680001-001; P; PS; F; 12/26/85.
Ocean County National Bank; Pt Pleasant Beach, NJ; 50271680001-002; P; M; F; 12/26/85.
Ohio Valley National Bank; Henderson, KY; 50244771801-001; P; M; F; 10/03/85.
Ohio Valley National Bank; Henderson, KY; 50344771801-002; NS; M; F; 10/03/85.
Ohio Valley National Bank; Henderson, KY; 50244771801-003; P; PS; F; 10/03/85.
Ohio Valley National Bank; Henderson, KY; 50344771801-004; NS; PS; F; 10/03/85.
Ohio Valley National Bank; Henderson, KY; 50244771802-001; S; M; F; 10/03/85.
Ohio Valley National Bank; Henderson, KY; 50244771802-002; S; PS; F; 10/03/85.
Old Kent Bank & Trust Co; Grand Rapids, MI; 50244937601-001; P; PS; F; 10/31/85.

Old Kent Bank & Trust Co; Grand Rapids, MI; 50244937601-002; P; M; F; 10/31/85.

Old Kent Bank & Trust Co; Grand Rapids, MI; 50344937601-003; NS; PS; F; 10/31/85.

Old Kent Bank & Trust Co; Grand Rapids, MI; 50344937601-004; NS; M; F; 10/31/85.

Old Kent Bank of Grand Haven; Grand Haven, MI; 50267397601-001; P; PS; F; 10/31/85.

Old Kent Bank of Grand Haven; Grand Haven, MI; 50267397601-002; P; M; F; 10/31/85.

Old Kent Bank of Grand Haven; Grand Haven, MI; 50367397601-003; NS; PS; F; 10/31/85.

Old Kent Bank of Grand Haven; Grand Haven, MI; 50367397601-004; NS; M; F; 10/31/85.

Old Kent Bank Southwest; Niles, MI; 50245437601-001; P; PS; F; 10/31/85.

Old Kent Bank Southwest; Niles, MI; 50245437601-002; P; M; F; 10/31/85.

Old Kent Bank Southwest; Niles, MI; 50345437601-003; NS; PS; F; 10/31/85.

Old Kent Bank Southwest; Niles, MI; 50345437601-004; NS; M; F; 10/31/85.

Old National Bank in Evansville; Evansville, IN; 50244961801-001; P; M; F; 10/03/85.

Old National Bank in Evansville; Evansville, IN; 50344961801-002; NS; M; F; 10/03/85.

Old National Bank in Evansville; Evansville, IN; 50244961801-003; P; PS; F; 10/03/85.

Old National Bank in Evansville; Evansville, IN; 50344961801-004; NS; PS; F; 10/03/85.

Old National Bank in Evansville; Evansville, IN; 50244961801-005; S; T; F; 10/03/85.

Old National Bank in Evansville; Evansville, IN; 50344961801-006; NS; T; F; 10/03/85.

Olympic Bank; Harrison, NY; 50245098601-001; S; M; F; 10/09/85.

Olympic Bank; Harrison, NY; 50245098601-002; S; M; F; 10/09/85.

Olympic Bank; Harrison, NY; 50345098601-003; NS; M; F; 10/09/85.

Olympic Bank; Harrison, NY; 50345098601-004; NS; M; F; 10/09/85.

Olympic Bank; Harrison, NY; 50245098601-005; S; PS; F; 10/09/85.

Olympic Bank; Harrison, NY; 50245098601-006; S; PS; F; 10/09/85.

Olympic Bank; Harrison, NY; 50345098601-007; NS; PS; F; 10/09/85.

Olympic Bank; Harrison, NY; 50345098601-008; NS; PS; F; 10/09/85.

Orange County Bank; Paoli, IN; 50245241801-001; S; M; F; 10/03/85.

Ouachita National Bank in Monroe; Monroe, LA; 50345370001-001; NS; PS; F; 10/23/85.

Ouachita National Bank in Monroe; Monroe, LA; 50345370001-002; NS; M; F; 10/23/85.

Ouachita National Bank in Monroe; Monroe, LA; 50345370002-001; NS; PS; F; 10/23/85.

Ouachita National Bank in Monroe; Monroe, LA; 50345370002-002; NS; M; F; 10/23/85.

Owen County State Bank; Spencer, IN; 50245421801-001; S; M; F; 10/03/85.

Owensboro National Bank; Owensboro, KY; 50273173501-007; P; PS; U; 10/30/85.

Owensboro National Bank; Owensboro, KY; 50273173501-009; P; M; U; 10/30/85.

Pacesetter Bank & Trust; Owosso, MI; 50245467601-001; P; PS; F; 10/31/85.

Pacesetter Bank & Trust; Owosso, MI; 50245467601-002; P; M; F; 10/31/85.

Pacesetter Bank & Trust; Owosso, MI; 50345467601-003; NS; PS; F; 10/31/85.

Pacesetter Bank & Trust; Owosso, MI; 50345467601-004; NS; M; F; 10/31/85.

Pacesetter Bank & Trust Grand Traverse; Traverse City, MI; 50255657601-001; P; PS; F; 10/31/85.

Pacesetter Bank & Trust Grand Traverse; Traverse City, MI; 50255657601-002; P; M; F; 10/31/85.

Pacesetter Bank & Trust Grand Traverse; Traverse City, MI; 50355657601-003; NS; PS; F; 10/31/85.

Pacesetter Bank & Trust Grand Traverse; Traverse City, MI; 50355657601-004; NS; M; F; 10/31/85.

Palmetto Bank; Laurens, SC; 50307590001-001; NS; PS; F; 10/30/85.

Pennbank; Titusville, PA; 50246218603-001; S; M; F; 10/09/85.

Pennbank; Titusville, PA; 50246218603-002; S; M; F; 10/09/85.

Pennbank; Titusville, PA; 50246218603-003; S; PS; F; 10/09/85.

Pennbank; Titusville, PA; 50246218603-004; S; PS; F; 10/09/85.

Pension Service Design Inc; Suttons Bay, MI; 50277920001-001; P; PS; F; 12/20/85.

Pension Service Design Inc; Suttons Bay, MI; 50277920001-002; P; M; F; 12/20/85.

Pension Service Design Inc; Suttons Bay, MI; 50377920001-003; NS; PS; F; 12/20/85.

Pension Service Design Inc; Suttons Bay, MI; 50377920001-004; NS; M; F; 12/28/85.

Pension Service Design Inc; Suttons Bay, MI; 50377920001-005; NS; PS; F; 12/23/85.

Pension Service Design Inc; Suttons Bay, MI; 50377920001-006; NS; M; F; 12/23/85.

PENTAD Corp; Waltham, MA; 50399444401-001; NS; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50399444401-002; NS; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444401-003; P; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444401-004; P; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444401-00[illegible] P; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444401-006; P; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444401-007; P; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444401-008; P; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444401-009; P; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444401-010; P; D; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50399444402-001; NS; PS; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50399444402-002; NS; M; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50399444402-003; NS; T; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50399444402-004; NS; PS; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-005; P; PS; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-006; P; M; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-007; P; T; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-008; P; PS; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-009; P; M; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-010; P; T; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-011; P; PS; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-012; P; M; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-013; P; T; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-014; P; PS; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-015; P; M; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-016; P; T; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-017; P; PS; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-018; P; M; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-019; P; PS; F; 12/10/85.

PENTAD Corp; Waltham, MA; 50299444402-020; P; M; F; 12/10/85.

Peoples Bank & Trust; Indianapolis, IN; 50246581801-001; P; M; F; 10/03/85.

Peoples Bank & Trust; Indianapolis, IN; 50346581801-002; NS; M; F; 10/03/85.

Peoples Bank & Trust; Indianapolis, IN; 50246581801-003; P; PS; F; 10/03/85.

Peoples Bank & Trust; Indianapolis, IN; 50346581801-004; NS; PS; F; 10/03/85.

Peoples Bank & Trust Co; Mount Vernon, IN; 50246464501-001; P; PS; F; 10/07/85.

Peoples Bank & Trust Co; Mount Vernon, IN; 50346464501-002; NS; PS; F; 10/07/85.

Peoples Bank & Trust Co; Mount Vernon, IN; 50246464501-003; P; M; F; 10/07/85.

Peoples Bank & Trust Co; Mount Vernon, IN; 50346464501-004; NS; M; F; 10/07/85.

Peoples First National Bank & Trust Co; Harrison, NY; 50246788601-001; S; M; F; 10/09/85.

Peoples First National Bank & Trust Co; Harrison, NY; 50246788601-002; S; M; F; 10/09/85.

Peoples First National Bank & Trust Co; Harrison, NY; 50246788601-003; S; PS; F; 10/09/85.

Peoples First National Bank & Trust Co; Harrison, NY; 50246788601-004; S; PS; F; 10/09/85.

Peoples Life Insurance Co; Durham, NC; 50346816401-001; NS; M; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50246816401-002; S; M; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50346816401-003; NS; PS; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50246816401-004; S; PS; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50346816401-005; NS; PS; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50346816402-001; NS; D; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50246816402-002; S; D; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50346816402-003; NS; D; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50246816402-004; S; D; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50346816402-005; NS; D; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50246816402-006; S; D; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50346816402-007; NS; D; F; 10/03/85.

Peoples Life Insurance Co; Durham, NC; 50246816402-008; S; D; F; 10/03/85.

Peoples Loan & Trust Co; Winchester, IN; 50346821801-001; NS; M; F; 10/03/85.

Peoples Loan & Trust Co; Winchester, IN; 50346821801-002; NS; PS; F; 10/03/85.

Peoples Savings Bank of Evansville; Evansville, IN; 50270901801-001; S; M; F; 10/03/85.

Peoples Savings Bank of Evansville; Evansville, IN; 50270901801-002; P; T; F; 10/03/85.

Peoples Savings Bank of Evansville; Evansville, IN; 50270901801-003; P; PS; F; 10/03/85.

Philadelphia Saving Fund Society; Philadelphia, PA; 50247390001-001; P; PS; F; 10/30/85.

Philadelphia Saving Fund Society; Philadelphia, PA; 50247390001-002; P; M; F; 10/30/85.

Phoenix Mutual Life Insurance Co; Hartford, CT; 50347410001-001; NS; PS; F; 11/15/85.

Phoenix Mutual Life Insurance Co; Hartford, CT; 50347410001-002; NS; M; F; 11/15/85.

Phoenix Mutual Life Insurance Co; Hartford, CT; 50347410001-003; NS; T; F; 11/15/85.

Phoenix Mutual Life Insurance Co; Hartford, CT; 50247410001-004; S; PS; F; 11/15/85.

Phoenix Mutual Life Insurance Co; Hartford, CT; 50247410001-005; S; M; F; 11/15/85.

Phoenix Mutual Life Insurance Co; Hartford, CT; 50247410001-006; S; T; F; 11/15/85.

Professional Golfers Association of America; Palm Beach Gardens, FL; 50354350001-001; NS; M; F; 12/23/85.

Provident Bank; Cincinnati, OH; 50348470001-001; NS; PS; F; 10/23/85.

Provident Bank; Cincinnati, OH; 50348470001-002; NS; M; F; 10/23/85.

Provident National Assurance Co; Chattanooga, TN; 50348530001-001; NS; M; F; 10/30/85.

Provident National Assurance Co; Chattanooga, TN; 50248530001-002; P; M; F; 10/30/85.

Provident National Assurance Co; Chattanooga, TN; 50348530001-003; NS; PS; F; 10/30/85.

Provident National Assurance Co; Chattanooga, TN; 50248530001-004; P; PS; F; 10/30/85.

Provident National Assurance Co; Chattanooga, TN; 50348530001-005; NS; T; F; 10/30/85.

Provident National Assurance Co; Chattanooga, TN; 50248530001-006; P; T; F; 10/30/85.

Provident National Assurance Co; Chattanooga, TN; 50348530002-001; NS; D; F; 10/30/85.

Provident National Assurance Co; Chattanooga, TN; 50248530002-002; P; D; F; 10/30/85.

Provident National Assurance Co; Chattanooga, TN; 50348530002-003; NS; D; F; 10/30/85.
Provident National Assurance Co; Chattanooga, TN; 50248530002-004; P; D; F; 10/30/85.
Prudential Insurance Co of America; Newark, NJ; 50248580001-001; P; M; F; 12/28/85.
Prudential Insurance Co of America; Newark, NJ; 50248580001-002; P; PS; F; 12/28/85.
Prudential Insurance Co of America; Newark, NJ; 50248580001-003; S; T; F; 12/28/85.
Prudential Insurance Co of America; Newark, NJ; 50348580001-004; NS; M; F; 12/28/85.
Prudential Insurance Co of America; Newark, NJ; 50348580001-005; NS; PS; F; 12/28/85.
Prudential Insurance Co of America; Newark, NJ; 50348580001-006; NS; T; F; 12/28/85.
Prudential Insurance Co of America; Newark, NJ; 50248580002-001; S; D; F; 12/28/85.
Prudential Insurance Co of America; Newark, NJ; 50248580002-002; S; D; F; 12/28/85.
Prudential Insurance Co of America; Newark, NJ; 50348580002-003; NS; D; F; 12/28/85.
Prudential Insurance Co of America; Newark, NJ; 50348580002-004; NS; D; F; 12/28/85.
Puget Sound National Bank; Tacoma, WA; 50248630001-001; P; PS; F; 12/20/85.
Puget Sound National Bank; Tacoma, WA; 50248630001-002; P; M; F; 12/20/85.
Puget Sound National Bank; Tacoma, WA; 50348630001-003; NS; PS; F; 12/20/85.
Puget Sound National Bank; Tacoma, WA; 50348630001-004; NS; M; F; 12/20/85.
Puget Sound National Bank; Tacoma, WA; 50348630001-005; NS; PS; F; 12/23/85.
Puget Sound National Bank; Tacoma, WA; 50348630001-006; NS; PS; F; 12/23/85.
Purdue National Bank of Lafayette; LaFayette, IN; 50248661801-001; P; M; F; 10/03/85.
Purdue National Bank of Lafayette; LaFayette, IN; 50348661801-002; NS; M; F; 10/03/85.
Purdue National Bank of Lafayette; LaFayette, IN; 50248661801-003; P; PS; F; 10/03/85.
Purdue National Bank of Lafayette; LaFayette, IN; 50348661801-004; NS; PS; F; 10/03/85.
R Meeder & Associates Inc; Columbus, OH; 50324630002-001; NS; PS; F; 12/26/85.
R Meeder & Associates Inc; Columbus, OH; 50324630002-002; NS; PS; F; 12/26/85.
RepublicBank Dallas NA; Dallas, TX; 50349172201-001; NS; PS; F; 12/05/85.
RepublicBank Dallas NA; Dallas, TX; 50349172201-002; NS; M; F; 12/05/85.
RepublicBank Dallas NA; Dallas, TX; 50249172202-001; P; PS; F; 12/05/85.
RepublicBank Dallas NA; Dallas, TX; 50249172202-002; P; M; F; 12/05/85.
RepublicBank Dallas NA; Dallas, TX; 50249172202-003; P; PS; F; 12/05/85.
RepublicBank Dallas NA; Dallas, TX; 50249172202-004; P; M; F; 12/06/85.
Riddell National Bank of Brazil; Brazil, IN; 50249561801-001; S; PS; F; 10/03/85.
Rockland Trust Co; Harrison, NY; 50249748601-001; S; M; F; 10/09/85.
Rockland Trust Co; Harrison, NY; 50249748601-002; S; M; F; 10/09/85.
Rockland Trust Co; Harrison, NY; 50349748601-003; NS; M; F; 10/09/85.
Rockland Trust Co; Harrison, NY; 50349748601-004; NS; M; F; 10/09/85.
Rockland Trust Co; Harrison, NY; 50249748601-005; S; PS; F; 10/09/85.
Rockland Trust Co; Harrison, NY; 50249748601-006; S; PS; F; 10/09/85.
Rockland Trust Co; Harrison, NY; 50349748601-007; NS; PS; F; 10/09/85.
Rockland Trust Co; Harrison, NY; 50349748601-008; NS; PS; F; 10/09/85.
Root River State Bank; Chatfield, MN; 50249797001-001; S; PS; F; 10/11/85.
Root River State Bank; Chatfield, MN; 50249797001-002; S; PS; F; 10/11/85.
Root River State Bank; Chatfield, MN; 50249797001-003; S; M; F; 10/11/85.
Root River State Bank; Chatfield, MN; 50249797001-004; S; M; F; 10/11/85.
Root River State Bank; Chatfield, MN; 50349797001-005; NS; PS; F; 10/11/85.
Root River State Bank; Chatfield, MN; 50349797001-006; NS; PS; F; 10/11/85.
Root River State Bank; Chatfield, MN; 50349797001-007; NS; M; F; 10/11/85.
Root River State Bank; Chatfield, MN; 50349797001-008; NS; M; F; 10/11/85.
Rotan Mosle Inc; Houston, TX; 50253720001-001; S; M; F; 12/28/85.
Rotan Mosle Inc; Houston, TX; 50253720001-002; S; PS; F; 12/28/85.
Salem Bank & Trust Co; Goshen, IN; 50250061801-001; S; PS; F; 10/03/85.
Salem Bank & Trust Co; Goshen, IN; 50350061801-002; NS; PS; F; 10/03/85.
Savings Bank of Utica; Utica, NY; 50276287501-001; P; PS; F; 10/31/85.
Savings Bank of Utica; Utica, NY; 50276287501-002; P; M; F; 10/31/85.
Savings Bank of Utica; Utica, NY; 50276287501-003; P; PS; F; 10/31/85.
Savings Bank of Utica; Utica, NY; 50276287501-004; P; M; F; 10/31/85.
Savings Banks Association of New York State; New York, NY; 50250377501-001; P; PS; F; 10/31/85.
Savings Banks Association of New York State; New York, NY; 50250377501-002; P; M; F; 10/31/85.
Savings Banks Association of New York State; New York, NY; 50250377501-003; P; PS; F; 10/31/85.
Savings Banks Association of New York State; New York, NY; 50250377501-004; P; M; F; 10/31/85.
Securities Fund Trust Co of Florida; St Petersburg, FL; 50370330002-001; NS; PS; F; 11/09/85.
Securities Fund Trust Co of Florida; St Petersburg, FL; 50370330002-002; NS; M; F; 11/09/85.
Security Bank & Trust Co; Vincennes, IN; 50250701801-001; P; M; F; 10/03/85.
Security Bank & Trust Co; Vincennes, IN; 50250701801-002; P; PS; F; 10/03/85.
Security First Group; Los Angeles, CA; 50272200001-001; S; M; F; 10/30/85.
Security First National Bank; Sheboygan, WI; 50250841802-001; P; M; F; 10/03/85.
Security First National Bank; Sheboygan, WI; 50350841802-002; NS; M; F; 10/03/85.
Security First National Bank; Sheboygan, WI; 50250841802-003; P; PS; F; 10/03/85.
Security First National Bank; Sheboygan, WI; 50350841802-004; NS; PS; F; 10/03/85.
Security National Bank; Harrison, NJ; 50250928601-001; S; M; F; 10/09/85.
Security National Bank; Harrison, NJ; 50250928601-002; S; M; F; 10/09/85.
Security National Bank; Harrison, NJ; 50350928601-003; NS; M; F; 10/09/85.
Security National Bank; Harrison, NJ; 50350928601-004; NS; M; F; 10/09/85.
Security National Bank; Harrison, NJ; 50250928601-005; S; PS; F; 10/09/85.
Security National Bank; Harrison, NJ; 50250928601-006; S; PS; F; 10/09/85.
Security National Bank; Harrison, NJ; 50350928601-007; NS; PS; F; 10/09/85.
Security National Bank; Harrison, NJ; 50350928601-008; NS; PS; F; 10/09/85.
Security Norstar Bank; Rochester, NY; 50351220001-001; NS; PS; F; 11/18/85.
Security Norstar Bank; Rochester, NY; 50251220001-002; S; PS; F; 11/13/85.
Security Norstar Bank; Rochester, NY; 50351220001-003; NS; PS; F; 11/18/85.
Security Norstar Bank; Rochester, NY; 50251220001-004; S; PS; F; 11/18/85.
Security Norstar Bank; Rochester, NY; 50351220001-005; NS; M; F; 11/18/85.
Security Norstar Bank; Rochester, NY; 50251220001-006; S; M; F; 11/18/85.
Security Norstar Bank; Rochester, NY; 50351220001-007; NS; M; F; 11/18/85.
Security Norstar Bank; Rochester, NY; 50351220001-009; NS; T; F; 11/18/85.
Security Norstar Bank; Rochester, NY; 50251220001-010; S; T; F; 11/18/85.
Security Norstar Bank; Rochester, NY; 50351220001-011; NS; T; F; 11/18/85.
Security Norstar Bank; Rochester, NY; 50251220001-012; S; T; F; 11/18/85.
Sentry Equity Services Inc; Stevens Point, WI; 50270946202-001; P; D; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50370946202-002; NS; D; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50270946202-003; P; D; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50370946202-004; NS; D; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50270946203-001; P; PS; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50370946203-002; NS; PS; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50270946203-003; P; M; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50370946203-004; NS; M; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50270946203-005; P; PS; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50270946203-006; P; M; F; 10/31/85.
Sentry Equity Services Inc; Stevens Point, WI; 50370946203-007; NS; T; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50279586201-001; P; D; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50379586201-002; NS; D; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50279586201-003; P; D; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50379586201-004; NS; D; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50279586202-001; P; PS; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50379586202-002; NS; PS; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50279586202-003; P; M; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50379586202-004; NS; M; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50279586202-005; P; PS; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50279586202-006; P; M; F; 10/31/85.
Sentry Insurance A Mutual Co; Stevens Point, WI; 50379586202-007; NS; T; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50251456201-001; P; D; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50351456201-002; NS; D; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50251456201-003; P; D; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50351456201-004; NS; D; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50251456202-001; P; PS; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50351456202-002; NS; PS; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50251456202-003; P; M; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50351456202-004; NS; M; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50251456202-005; P; PS; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50251456202-006; P; M; F; 10/31/85.
Sentry Insurance of Illinois Inc; Stevens Point, WI; 50351456202-007; NS; T; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50251466201-001; P; D; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50351466201-002; NS; D; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50251466201-003; P; D; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50351466201-004; NS; D; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50251466202-001; P; PS; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50351466202-002; NS; PS; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50251466202-003; P; M; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50351466202-004; NS; M; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50251466202-005; P; PS; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50251466202-006; P; M; F; 10/31/85.
Sentry Insurance of Michigan Inc; Stevens Point, WI; 50351466202-007; NS; T; F; 10/31/85.

Sentry Investors Life Insurance Co; Stevens Point, WI; 50260666201-001; P; D; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50360666201-002; NS; D; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50260666201-003; P; D; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50360666201-004; NS; D; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50260666202-001; P; PS; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50360666202-002; NS; PS; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50260666202-003; P; M; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50360666202-004; NS; M; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50260666202-005; P; PS; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50260666202-006; P; M; F; 10/31/85.
Sentry Investors Life Insurance Co; Stevens Point, WI; 50360666202-007; NS; T; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50251336201-001; P; D; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50351336201-002; NS; D; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50251336201-003; P; D; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50351336201-004; NS; D; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50251336202-001; P; PS; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50351336202-002; NS; PS; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50251336202-003; P; M; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50351336202-004; NS; M; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50251336202-005; P; PS; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50251336202-006; P; M; F; 10/31/85.
Sentry Life Insurance Co; Stevens Point, WI; 50351336202-007; NS; T; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50251346201-001; P; D; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50351346201-002; NS; D; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50251346201-003; P; D; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50351346201-004; NS; D; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50251346202-001; P; PS; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50351346202-002; NS; PS; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50251346202-003; P; M; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50351346202-004; NS; M; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50251346202-005; P; PS; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50251346202-006; P; M; F; 10/31/85.
Sentry Life Insurance Co of New York; Stevens Point, WI; 50351346202-007; NS; T; F; 10/31/85.
Sentry Savings; Harrison, NY; 50272928601-001; S; M; F; 10/09/85.
Sentry Savings; Harrison, NY; 50272928601-002; S; M; F; 10/09/85.
Sentry Savings; Harrison, NY; 50372928601-003; NS; M; F; 10/09/85.
Sentry Savings; Harrison, NY; 50372928601-004; NS; M; F; 10/09/85.
Sentry Savings; Harrison, NY; 50272928601-005; S; PS; F; 10/09/85.
Sentry Savings; Harrison, NY; 50272928601-006; S; PS; F; 10/09/85.
Sentry Savings; Harrison, NY; 50372928601-007; NS; PS; F; 10/09/85.
Sentry Savings; Harrison, NY; 50372928601-008; NS; PS; F; 10/09/85.
Seymour National Bank; Seymour, IN; 50251391801-001; P; M; F; 10/03/85.
Seymour National Bank; Seymour, IN; 50351391801-002; NS; M; F; 10/03/85.
Seymour National Bank; Seymour, IN; 50251391801-003; P; PS; F; 10/03/85.
Seymour National Bank; Seymour, IN; 50351391801-004; NS; PS; F; 10/03/85.
Shawmut Bank of Boston NA; Boston, MA; 50351474401-001; NS; D; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50351474401-002; NS; D; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474401-003; P; D; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474401-004; P; D; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474401-005; P; D; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474401-006; P; O; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50351474402-001; NS; PS; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50351474402-002; NS; M; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50351474402-003; NS; T; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50351474402-004; NS; PS; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474402-005; P; PS; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474402-006; P; M; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474402-007; P; T; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474402-008; P; PS; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474402-009; P; M; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474402-010; P; T; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474402-011; P; PS; F; 12/10/85.
Shawmut Bank of Boston NA; Boston, MA; 50251474402-012; P; M; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50351524401-001; NS; D; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50351524401-002; NS; D; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524401-003; P; D; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524401-004; P; D; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524401-005; P; D; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524401-006; P; D; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50351524402-001; NS; PS; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50351524402-002; NS; M; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50351524402-003; NS; T; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50351524402-004; NS; PS; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524402-005; P; PS; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524402-006; P; M; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524402-007; P; T; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524402-008; P; PS; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524402-009; P; M; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524402-010; P; T; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524402-011; P; PS; F; 12/10/85.
Shawmut First Bank & Trust Co; Springfield, MA; 50251524402-012; P; M; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50360154402-001; NS; D; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50360154402-002; NS; D; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154402-003; P; D; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154402-004; P; D; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154402-005; P; D; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154402-006; P; D; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50360154403-001; NS; PS; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50360154403-002; NS; M; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50360154403-003; NS; T; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50360154403-004; NS; PS; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154403-005; P; PS; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154403-006; P; M; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154403-007; P; T; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154403-008; P; PS; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154403-009; P; M; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154403-010; P; T; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154403-011; P; PS; F; 12/10/85.
Shawmut Worcester County Bank NA; Worcester, MA; 50260154403-012; P; M; F; 12/10/85.
Shawnee State Bank; Shawnee, KS; 50351563401-001; NS; PS; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50351563401-002; NS; PS; F; 10/07/85.
Shawnee State Bank; Shawnee, KS, 50351563401-003; NS; PS; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50351563401-004; NS; PS; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563401-005; P; PS; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50351563401-006; NS; M; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50351563401-007; NS; M; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50351563401-008; NS; M; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50351563401-009; NS; M; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563401-010; P; M; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563401-011; P; PS; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563401-012; P; M; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563401-013; S; M; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563401-014; S; PS; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563401-015; S; PS; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563401-016; S; M; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50351563402-001; NS; D; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50351563402-002; NS; D; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563402-003; S; D; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563402-004; S; D; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563402-005; S; D; F; 10/07/85.
Shawnee State Bank; Shawnee, KS; 50251563402-006; S; D; F; 10/07/85.
Shearson Lehman Brothers Inc; Atlanta, GA; 50349670001-001; NS; PS; F; 10/30/85.
Southgate Bank; Prairie Village, KS; 50352403401-001; NS; PS; F; 10/07/85.
Southgate Bank; Prairie Village, KS; 50352403401-002; NS; PS; F; 10/07/85.
Southgate Bank; Prairie Village, KS; 50352403401-003; NS; PS; F; 10/07/85.
Southgate Bank; Prairie Village, KS; 50352403401-004; NS; PS; F; 10/07/85.
Southgate Bank; Prairie Village, KS; 50252403401-005; P; PS; F; 10/07/85.
Southgate Bank; Prairie Village, KS; 50352403401-006; NS; M; F; 10/07/85.
Southgate Bank; Prairie Village, KS; 50352403401-007; NS; M; F; 10/07/85.
Southgate Bank; Prairie Village, KS; 50352403401-008; NS; M; F; 10/07/85.
Southgate Bank; Prairie Village, KS; 50352403401-009; NS; M; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403401-010; P; M; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403401-011; P; PS; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403401-012; P; M; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403401-013; S; M; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403401-014; S; PS; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403401-015; S; PS; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403401-016; S; M; F; 10/07/85

Southgate Bank; Prairie Village, KS; 50352403402-001; NS; D; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50352403402-002; NS; D; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403402-003; S; D; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403402-004; S; D; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403402-005; S; D; F; 10/07/85.

Southgate Bank; Prairie Village, KS; 50252403402-006; S; D; F; 10/07/85.

Springfield Institution for Savings; Springfield, MA; 50270610001-001; S; D; F; 10/23/85.

St Cloud National Bank & Trust Co; St Cloud, MN; 50252747003-001; S; PS; F; 10/11/85.

St Cloud National Bank & Trust Co; St Cloud, MN; 50252747003-002; S; PS; F; 10/11/85.

St Cloud National Bank & Trust Co; St Cloud, MN; 50252747003-003; S; M; F; 10/11/85.

St Cloud National Bank & Trust Co; St Cloud, MN; 50252747003-004; S; M; F; 10/11/85.

St Cloud National Bank & Trust Co; St Cloud, MN; 50352747003-005; NS; PS; F; 10/11/85.

St Cloud National Bank & Trust Co; St Cloud, MN; 50352747003-006; NS; PS; F; 10/11/85.

St Cloud National Bank & Trust Co; St Cloud, MN; 50352747003-007; NS; M; F; 10/11/85.

St Cloud National Bank & Trust Co; St Cloud, MN; 50352747003-008; NS; M; F; 10/11/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770001-001; NS; M; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770001-002; NS; M; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770002-001; NS; PS; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770002-002; NS; PS; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770003-001; NS; M; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770003-002; NS; M; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770003-003; NS; PS; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770003-004; NS; PS; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770004-001; NS; M; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770004-002; NS; M; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770004-003; NS; PS; F; 12/02/85.

St Joseph Bank & Trust Co; South Bend, IN; 50352770004-004; NS; PS; F; 12/02/85.

State Bank & Trust Co; Defiance, OH; 50253014501-001; P; PS; F; 10/07/85.

State Bank & Trust Co; Defiance, OH; 50353014501-002; NS; PS; F; 10/07/85.

State Bank & Trust Co; Defiance, OH; 50253014501-003; P; M; F; 10/07/85.

State Bank & Trust Co; Defiance, OH; 50353014501-004; NS; M; F; 10/07/85.

State Bank of De Pere; De Pere, WI; 50253141801-001; S; PS; F; 10/03/85.

State Bank of De Pere; De Pere, WI; 50353141801-002; NS; PS; F; 10/03/85.

State Bank of LaCrosse; LaCrosse, WI; 50253317002-001; S; PS; F; 10/11/85.

State Bank of LaCrosse; LaCrosse, WI; 50253317002-002; S; PS; F; 10/11/85.

State Bank of LaCrosse; LaCrosse, WI; 50253317002-003; S; M; F; 10/11/85.

State Bank of LaCrosse; LaCrosse, WI; 50253317002-004; S; M; F; 10/11/85.

State Bank of LaCrosse; LaCrosse, WI; 50353317002-005; NS; PS; F; 10/11/85.

State Bank of LaCrosse; LaCrosse, WI; 50353317002-006; NS; PS; F; 10/11/85.

State Bank of LaCrosse; LaCrosse, WI; 50353317002-007; NS; M; F; 10/11/85.

State Bank of LaCrosse; LaCrosse, WI; 50353317002-008; NS; M; F; 10/11/85.

State Exchange Bank; Culver, IN; 50253611801-001; S; PS; F; 10/03/85.

State Exchange Bank; Culver, IN; 50353611801-002; NS; PS; F; 10/03/85.

State Street Bank & Trust Co; Boston, MA; 50253850001-001; S; M; F; 10/30/85.

State Street Bank & Trust Co; Boston, MA; 50253850001-002; S; PS; F; 10/30/85.

State Street Bank & Trust Co; Boston, MA; 50253850001-003; P; M; F; 10/30/85.

State Street Bank & Trust Co; Boston, MA; 50253850001-004; P; PS; F; 10/30/85.

State Street Bank & Trust Co; Boston, MA; 50353850001-005; NS; M; F; 10/30/85.

State Street Bank & Trust Co; Boston, MA; 50353850001-006; NS; PS; F; 10/30/85.

Stearns County National Bank; Albany, MN; 50253957001-001; S; PS; F; 10/11/85.

Stearns County National Bank; Albany, MN; 50253957001-002; S; PS; F; 10/11/85.

Stearns County National Bank; Albany, MN; 50253957001-003; S; M; F; 10/11/85.

Stearns County National Bank; Albany, MN; 50253957001-004; S; M; F; 10/11/85.

Stearns County National Bank; Albany, MN; 50353957001-005; NS; PS; F; 10/11/85.

Stearns County National Bank; Albany, MN; 50353957001-006; NS; PS; F; 10/11/85.

Stearns County National Bank; Albany, MN; 50353957001-007; NS; M; F; 10/11/85.

Stearns County National Bank; Albany, MN; 50353957001-008; NS; M; F; 10/11/85.

Stein Roe & Farnham; Chicago, IL; 50253965001-001; P; PS; F; 12/04/85.

Stein Roe & Farnham; Chicago, IL; 50253965001-002; P; M; F; 12/04/85.

Sunwest Bank of Albuquerque NA; Albuquerque, NM; 50270264901-001; S; PS; F; 10/31/85.

Sunwest Bank of Albuquerque NA; Albuquerque, NM; 50270264901-002; S; M; F; 10/31/85.

Sylvania Savings Bank Co; Sylvania, OH; 50354540001-001; NS; PS; F; 11/26/85.

Sylvania Savings Bank Co; Sylvania, OH; 50354540001-002; NS; PS; F; 11/26/85.

Sylvania Savings Bank Co; Sylvania, OH; 50354540001-003; NS; M; F; 11/26/85.

Sylvania Savings Bank Co; Sylvania, OH; 50354540001-004; NS; M; F; 11/26/85.

Sylvania Savings Bank Co; Sylvania, OH; 50254540001-005; P; PS; F; 11/27/85.

Sylvania Savings Bank Co; Sylvania, OH; 50254540001-006; P; M; F; 11/27/85.

Technology Fund Inc; Chicago, IL; 50273298201-001; P; PS; F; 11/14/85.

Technology Fund Inc; Chicago, IL; 50273298201-002; P; M; F; 11/14/85.

Technology Fund Inc; Chicago, IL; 50373298201-003; NS; PS; F; 11/14/85.

Technology Fund Inc; Chicago, IL; 50373298201-004; NS; M; F; 11/14/85.

Terre Haute First National Bank; Terre Haute, IN; 50254701801-001; P; M; F; 10/03/85.

Terre Haute First National Bank; Terre Haute, IN; 50354701801-002; NS; M; F; 10/03/85.

Terre Haute First National Bank; Terre Haute, IN; 50254701801-003; P; PS; F; 10/03/85.

Terre Haute First National Bank; Terre Haute, IN; 50354701801-004; NS; PS; F; 10/03/85.

Third National Bank & Trust Co; Dayton, OH; 50255214505-001; P; PS; F; 10/07/85.

Third National Bank & Trust Co; Dayton, OH; 50355214505-002; NS; PS; F; 10/07/85.

Third National Bank & Trust Co; Dayton, OH; 50255214505-003; P; M; F; 10/07/85.

Third National Bank & Trust Co; Dayton, OH; 50355214505-004; NS; M; F; 10/07/85.

Third National Bank in Nashville; Nashville, TN; 50255193501-007; P; PS; U; 10/30/85.

Third National Bank in Nashville; Nashville, TN; 50255193501-009; P; M; U; 10/30/85.

Thomson McKinnon Asset Management Inc; New York, NY; 50216400001-001; S; PS; F; 11/15/85.

Thomson McKinnon Asset Management Inc; New York, NY; 50216400001-002; S; M; F; 11/15/85.

Tompkins County Trust Co; Harrison, NY; 50255388601-001; S; M; F; 10/09/85.

Tompkins County Trust Co; Harrison, NY; 50255388601-002; S; M; F; 10/09/85.

Tompkins County Trust Co; Harrison, NY; 50355388601-003; NS; M; F; 10/09/85.

Tompkins County Trust Co; Harrison, NY; 50355388601-004; NS; M; F; 10/09/85.

Tompkins County Trust Co; Harrison, NY; 50255388601-005; S; PS; F; 10/09/85.

Tompkins County Trust Co; Harrison, NY; 50255388601-006; S; PS; F; 10/09/85.

Tompkins County Trust Co; Harrison, NY; 50355388601-007; NS; PS; F; 10/09/85.

Tompkins County Trust Co; Harrison, NY; 50355388601-008; NS; PS; F; 10/09/85.

Trust Consultants Inc; Foster City, CA; 50299484801-001; P; D; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50299484801-002; P; D; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50399484801-003; NS; D; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50299484802-001; P; M; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50299484802-002; P; M; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50299484802-003; P; PS; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50299484802-004; P; PS; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50299484802-005; P; T; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50299484802-006; P; T; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50399484802-007; NS; M; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50399484802-008; NS; PS; F; 11/12/85.

Trust Consultants Inc; Foster City, CA; 50399484802-009; NS; T; F; 11/12/85.

Trustees Commingled Fund; Valley Forge, PA; 50380305101-001; NS; M; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50280305101-002; P; M; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50280305101-003; P; M; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50380305101-004; NS; PS; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50280305101-005; P; PS; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50280305101-006; P; PS; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50380305102-001; NS; D; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50380305102-002; NS; D; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50280305102-003; P; D; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50280305102-004; P; D; F; 10/09/85.

Trustees Commingled Fund; Valley Forge, PA; 50280305102-005; P; D; F; 10/09/85.

Trustmark National Bank; Jackson, MS; 50225213501-007; P; PS; U; 10/30/85.

Trustmark National Bank; Jackson, MS; 50225213501-009; P; M; U; 10/30/85.

Tucker Anthony & R L Day Inc; Boston, MA; 50255861401-001; P; M; F; 11/22/85.

Tucker Anthony & R L Day Inc; Boston, MA; 50255861401-002; P; PS; F; 11/22/85.

Tudor Fund; New York, NY; 50262150001-001; S; M; F; 12/02/85.

Twentieth Century Investors Inc; Kansas City, MO; 50255884201-001; P; PS; F; 10/03/85.

Twentieth Century Investors Inc; Kansas City, MO; 50255884201-002; P; PS; F; 10/03/85.

Twentieth Century Investors Inc; Kansas City, MO; 50255884201-003; P; M; F; 10/03/85.

Twentieth Century Investors Inc; Kansas City, MO; 50255884201-004; P; M; F; 10/03/85.

Twentieth Century Investors Inc; Kansas City, MO; 50355884201-005; NS; PS; F; 10/03/85.

Twentieth Century Investors Inc; Kansas City, MO; 50355884201-006; NS; PS; F; 10/03/85.
Twentieth Century Investors Inc; Kansas City, MO; 50355884201-007; NS; M; F; 10/03/85.
Twentieth Century Investors Inc; Kansas City, MO; 50355884201-008; NS; M; F; 10/03/85.
Union Bank & Trust Co; Kokomo, IN; 50256051801-001; P; M; F; 10/01/85.
Union Bank & Trust Co; Kokomo, IN; 50356051801-002; NS; M; F; 10/01/85.
Union Bank & Trust Co; Kokomo, IN; 50256051801-003; P; PS; F; 10/01/85.
Union Bank & Trust Co; Kokomo, IN; 50356051801-004; NS; PS; F; 10/01/85.
Union Bank & Trust Co of Greensburg; Greensburg, IN; 50256074501-001; P; PS; F; 10/07/85.
Union Bank & Trust Co of Greensburg; Greensburg, IN; 50356074501-002; NS; PS; F; 10/07/85.
Union Bank & Trust Co of Greensburg; Greensburg, IN; 50256074501-003; P; M; F; 10/07/85.
Union Bank & Trust Co of Greensburg; Greensburg, IN; 50356074501-004; NS; M; F; 10/07/85.
Union County National Bank; Liberty, IN; 50270911801-001; S; PS; F; 10/03/85.
Union National Bank; Lowell, MA; 50378914401-001; NS; D; F; 12/10/85.
Union National Bank; Lowell, MA; 50378914401-002; NS; D; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914401-003; P; D; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914401-004; P; D; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914401-005; P; D; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914401-006; P; D; F; 12/10/85.
Union National Bank; Lowell, MA; 50378914402-001; NS; PS; F; 12/10/85.
Union National Bank; Lowell, MA; 50378914402-002; NS; M; F; 12/10/85.
Union National Bank; Lowell, MA; 50378914402-003; NS; T; F; 12/10/85.
Union National Bank; Lowell, MA; 50378914402-004; NS; PS; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914402-005; P; PS; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914402-006; P; M; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914402-007; P; T; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914402-008; P; PS; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914402-009; P; M; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914402-010; P; T; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914402-011; P; PS; F; 12/10/85.
Union National Bank; Lowell, MA; 50278914402-012; P; M; F; 12/10/85.
Union Planters National Bank; Memphis, TN; 50356420001-001; NS; PS; F; 12/23/85.
Union Planters National Bank; Memphis, TN; 50356420001-002; NS; PS; F; 12/23/85.
Union Planters National Bank; Memphis, TN; 50256420001-003; P; PS; F; 12/23/85.
Union Planters National Bank; Memphis, TN; 50256420001-004; P; PS; F; 12/23/85.
Union Planters National Bank; Memphis, TN; 50356420001-005; NS; M; F; 12/24/85.
Union Planters National Bank; Memphis, TN; 50356420001-006; NS; M; F; 12/24/85.
Union Planters National Bank; Memphis, TN; 50256420001-007; P; M; F; 12/24/85.
Union Planters National Bank; Memphis, TN; 50256420001-008; P; M; F; 12/24/85.
Union State Bank; Carmel, IN; 50256491801-001; S; M; F; 10/03/85.
Union Trust Co; Union City, IN; 50256601801-001; S; M; F; 10/03/85.
Union Trust Co of Maryland; Baltimore, MD; 50356610001-001; NS; PS; F; 12/19/85.
Union Trust Co of Maryland; Baltimore, MD; 50356610001-002; NS; M; F; 12/19/85.
Union Trust Co of Maryland; Baltimore, MD; 50256610001-003; P; PS; F; 12/19/85.
Union Trust Co of Maryland; Baltimore, MD; 50256610001-004; P; M; F; 12/19/85.
United Bank & Trust Co; Hartford, CT; 50256720001-001; S; PS; F; 11/26/85.
United Bank of Denver NA; Denver, CO; 50356780001-001; NS; PS; F; 12/28/85.
United Bank of Denver NA; Denver, CO; 50356780001-002; NS; M; F; 12/28/85.
United Bank of Denver NA; Denver, CO; 50356780001-003; NS; M; F; 12/28/85.
United Funds Inc; Kansas City, MO; 50257020001-001; P; PS; F; 10/30/85.
United Funds Inc; Kansas City, MO; 50257020001-002; P; M; F; 10/30/85.
United Funds Inc; Kansas City, MO; 50357020002-001; NS; PS; F; 10/30/85.
United Funds Inc; Kansas City, MO; 50357020002-002; NS; M; F; 10/30/85.
United Funds Inc; Kansas City, MO; 50357020002-003; NS; PS; F; 10/30/85.
United Funds Inc; Kansas City, MO; 50357020002-004; NS; M; F; 10/30/85.
United Funds Inc; Kansas City, MO; 50357020002-005; NS; T; F; 10/30/85.
United Funds Inc; Kansas City, MO; 50357020002-006; NS; T; F; 10/30/85.
United Funds Inc; Kansas City, MO; 50357020003-001; NS; D; F; 10/30/85.
United Missouri Bank of Kansas City; Kansas City, MO; 50257234201-001; P; PS; F; 10/03/85.
United Missouri Bank of Kansas City; Kansas City, MO; 50257234201-002; P; PS; F; 10/03/85.
United Missouri Bank of Kansas City; Kansas City, MO; 50257234201-003; P; M; F; 10/03/85.
United Missouri Bank of Kansas City; Kansas City, MO; 50257234201-004; P; M; F; 10/03/85.
United Missouri Bank of Kansas City; Kansas City, MO; 50357234201-005; NS; PS; F; 10/03/85.
United Missouri Bank of Kansas City; Kansas City, MO; 50357234201-006; NS; PS; F; 10/03/85.
United Missouri Bank of Kansas City; Kansas City, MO; 50357234201-007; NS; M; F; 10/03/85.
United Missouri Bank of Kansas City; Kansas City, MO; 50357234201-008; NS; M; F; 10/03/85.
United New Mexico Trust Co; Albuquerque, NM; 50370550001-001; NS; PS; F; 12/16/85.
United New Mexico Trust Co; Albuquerque, NM; 50370550001-002; NS; PS; F; 12/16/85.
United New Mexico Trust Co; Albuquerque, NM; 50370550002-001; NS; M; F; 12/16/85.
United New Mexico Trust Co; Albuquerque, NM; 50370550002-002; NS; M; F; 12/16/85.
United New Mexico Trust Co; Albuquerque, NM; 50370550003-001; NS; PS; F; 12/16/85.
United New Mexico Trust Co; Albuquerque, NM; 50370550003-002; NS; M; F; 12/16/85.
US Boston Investment Management Corp; Burlington, MA; 50280051401-001; P; M; F; 11/22/85.
US Boston Investment Management Corp; Burlington, MA; 50280051401-002; P; PS; F; 11/22/85.
USAA Investment Management Co; San Antonio, TX; 50257931401-001; P; M; F; 11/22/85.
USAA Investment Management Co; San Antonio, TX; 50257931401-002; P; PS; F; 11/22/85.
USAA Investment Management Co; San Antonio, TX; 50257931401-003; P; M; F; 11/22/85.
USAA Investment Management Co; San Antonio, TX; 50257931401-004; P; PS; F; 11/22/85.
Valley Bank & Trust Co; Grand Forks, ND; 50258127001-001; S; PS; F; 10/11/85.
Valley Bank & Trust Co; Grand Forks, ND; 50258127001-002; S; PS; F; 10/11/85.
Valley Bank & Trust Co; Grand Forks, ND; 50258127001-003; S; M; F; 10/11/85.
Valley Bank & Trust Co; Grand Forks, ND; 50258127001-004; S; M; F; 10/11/85.
Valley Bank & Trust Co; Grand Forks, ND; 50358127001-005; NS; PS; F; 10/11/85.
Valley Bank & Trust Co; Grand Forks, ND; 50358127001-006; NS; PS; F; 10/11/85.
Valley Bank & Trust Co; Grand Forks, ND; 50358127001-007; NS; M; F; 10/11/85.
Valley Bank & Trust Co; Grand Forks, ND; 50358127001-008; NS; M; F; 10/11/85.
Valley Fidelity Bank & Trust Co; Knoxville, TN; 50358173502-001; NS; D; F; 10/31/85.
Valley Fidelity Bank & Trust Co; Knoxville, TN; 50358173502-002; NS; D; F; 10/31/85.
Valley Fidelity Bank & Trust Co; Knoxville, TN; 50258173502-003; P; D; F; 10/31/85.
Valley Fidelity Bank & Trust Co; Knoxville, TN; 50258173502-004; P; D; F; 10/31/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50370245101-001; NS; M; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50270245101-002; P; M; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50270245101-003; P; M; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50370245101-004; NS; PS; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50270245101-005; P; PS; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50270245101-006; P; PS; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50370245102-001; NS; D; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50370245102-002; NS; D; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50270245102-003; P; D; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50270245102-004; P; D; F; 10/09/85.
Vanguard Fiduciary Trust Co; Valley Forge, PA; 50270245102-005; P; D; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50380315101-001; NS; M; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50280315101-002; P; M; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50280315101-003; P; M; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50380315101-004; NS; PS; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50280315101-005; P; PS; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50280315101-006; P; PS; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50380315102-001; NS; D; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50380315102-002; NS; D; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50280315102-003; P; D; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50280315102-004; P; D; F; 10/09/85.
Vanguard Fixed Income Securities Fund; Valley Forge, PA; 50280315102-005; P; D; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50380325101-001; NS; M; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50280325101-002; P; M; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50280325101-003; P; M; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50380325101-004; NS; PS; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50280325101-005; P; PS; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50280325101-006; P; PS; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50380325102-001; NS; D; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50380325102-002; NS; D; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50280325102-003; P; D; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50280325102-004; P; D; F; 10/09/85.
Vanguard Index Trust; Valley Forge, PA; 50280325102-005; P; D; F; 10/09/85.
Vanguard Money Market Trust; Valley Forge, PA; 50380335101-001; NS; M; F; 10/09/85.
Vanguard Money Market Trust; Valley Forge, PA; 50280335101-002; P; M; F; 10/09/85.
Vanguard Money Market Trust; Valley Forge, PA; 50280335101-003; P; M; F; 10/09/85.
Vanguard Money Market Trust; Valley Forge, PA; 50380335101-004; NS; PS; F; 10/09/85.
Vanguard Money Market Trust; Valley Forge, PA; 50280335101-005; P; PS; F; 10/09/85.
Vanguard Money Market Trust; Valley Forge, PA; 50280335101-006; P; PS; F; 10/09/85.
Vanguard Money Market Trust; Valley Forge, PA; 50380335102-001; NS; D; F; 10/09/85.
Vanguard Money Market Trust; Valley Forge, PA; 50380335102-002; NS; D; F; 10/09/85.
Vanguard Money Market Trust; Valley Forge, PA; 50280335102-003; P; D; F; 10/09/85.

Vanguard Money Market Trust; Valley Forge, PA; 50280335102-004; P; D; F; 10/09/85.

Vanguard Money Market Trust; Valley Forge, PA; 50280335102-005; P; D; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50380345101-001; NS; M; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50280345101-002; P; M; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50280345101-003; P; M; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50380345101-004; NS; PS; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50280345101-005; P; PS; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50280345101-006; P; PS; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50380345102-001; NS; D; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50380345102-002; NS; D; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50280345102-003; P; D; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50280345102-004; P; D; F; 10/09/85.

Vanguard Qualified Dividend Portfolio I; Valley Forge, PA; 50280345102-005; P; D; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50380355101-001; NS; M; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50280355101-002; P; M; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50280355101-003; P; M; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50380355101-004; NS; PS; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50280355101-005; P; PS; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50280355101-006; P; PS; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50380355102-001; NS; D; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50380355102-002; NS; D; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50280355102-003; P; D; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50280355102-004; P; D; F; 10/09/85.

Vanguard Specialized Portfolios; Valley Forge, PA; 50280355102-005; P; D; F; 10/09/85.

Veterans Life Insurance Co; Valley Forge, PA; 50358426401-001; NS; M; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50258426401-002; S; M; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50358426401-003; NS; PS; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50258426401-004; S; PS; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50358426401-005; NS; PS; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50358426402-001; NS; D; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50258426402-002; S; D; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50358426402-003; NS; D; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50258426402-004; S; D; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50358426402-005; NS; D; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50258426402-006; S; D; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50358426402-007; NS; D; F; 10/03/85.

Veterans Life Insurance Co; Valley Forge, PA; 50258426402-008; S; D; F; 10/03/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50380365101-001; NS; M; F; 10/09/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50280365101-002; P; M; F; 10/09/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50280365101-003; P; M; F; 10/09/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50380365101-004; NS; PS; F; 10/09/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50280365101-005; P; PS; F; 10/09/85.

Compensation Programs Inc; Overland Park, KS; 50299343401-013, P; M; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343401-014 P; PS; 10/07/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50280365101-006; P; PS; F; 10/09/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50380365102-001; NS; D; F; 10/09/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50380365102-002; NS; D; F; 10/09/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50280365102-003; P; D; F; 10/09/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50280365102-004; P; D; F; 10/09/85.

W L Morgan Growth Fund Inc; Valley Forge, PA; 50280365102-005; P; D; F; 10/09/85.

Washington National Trust Co; Evanston, IL; 50258820001-001; S; PS; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50258820001-002; S; PS; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50358820001-003; NS; PS; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50358820001-004; NS; PS; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50258820002-001; S; M; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50258820002-002; S; M; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50358820002-003; NS; M; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50358820002-004; NS; M; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50258820003-001; S; D; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50258820003-002; S; D; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50358820003-003; NS; D; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50358820003-004; NS; D; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50358820003-005; NS; D; F; 12/19/85.

Washington National Trust Co; Evanston, IL; 50358820003-006; NS; D; F; 12/19/85.

Wayne Hummer & Co; Chicago, IL; 50259010001-001; S; PS; F; 10/23/85.

Wayne Hummer & Co; Chicago, IL; 50259010001-002; S; M; F; 10/23/85.

Wayzata Bank & Trust Co; Wayzata, MN; 50359030001-001; NS; PS; F; 10/30/85.

Wayzata Bank & Trust Co; Wayzata, MN; 50359030001-002; NS; M; F; 10/30/85.

Wayzata Bank & Trust Co; Wayzata, MN; 50259030001-003; P; PS; F; 10/30/85.

Wayzata Bank & Trust Co; Wayzata, MN; 50259030001-004; P; M; F; 10/30/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50380375101-001; NS; M; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50280375101-002; P; M; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50280375101-003; P; M; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50380375101-004; NS; PS; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50280375101-005; P; PS; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50280375101-006; P; PS; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50380375102-001; NS; D; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50380375102-002; NS; D; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50280375102-003; P; D; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50280375102-004; P; D; F; 10/09/85.

Wellesley Income Fund Inc; Valley Forge, PA; 50280375102-005; P; D; F; 10/09/85.

William Penn Life Assurance Co of America; Piscataway, NJ; 50212100002-001; P; D; F; 12/23/85.

William Penn Life Assurance Co of America; Piscataway, NJ; 50212100002-002; P; D; F; 12/23/85.

William Penn Life Assurance Co of America; Piscataway, NJ; 50312100002-003; NS; D; F; 12/23/85.

Compensation Programs Inc; Overland Park, KS; 50299343401-015, P; PS; 10/07/85.

Compensation Programs Inc; Overland Park, KS; 50299343401-016; P; M; 10/07/85.

William Penn Life Assurance Co of America; Piscataway, NJ; 50312100002-004; NS; D; F; 12/24/85.

William Penn Life Assurance Co of America; Piscataway, NJ; 50312100002-005; NS; D; F; 12/23/85.

William Penn Life Assurance Co of America; Piscataway, NJ; 50312100002-006; NS; D; F; 12/23/85.

William Penn Life Insurance Co of New York; New Hyde Park, NY; 50259780002-001; P; D; F; 12/23/85.

William Penn Life Insurance Co of New York; New Hyde Park, NY; 50259780002-002; P; D; F; 12/23/85.

William Penn Life Insurance Co of New York; New Hyde Park, NY; 50359780002-003; NS; D; F; 12/23/85.

William Penn Life Insurance Co of New York; New Hyde Park, NY; 50359780002-004; NS; D; F; 12/23/85.

William Penn Life Insurance Co of New York; New Hyde Park, NY; 50259780002-005; P; D; F; 12/23/85.

Windsor Fund Inc; Valley Forge, PA; 50380385101-001; NS; M; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50280385101-002; P; M; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50280385101-003; P; M; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50380385101-004; NS; PS; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50280385101-005; P; PS; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50280385101-006; P; PS; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50380385102-001; NS; D; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50380385102-002; NS; D; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50280385102-003; P; D; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50280385102-004; P; D; F; 10/09/85.

Windsor Fund Inc; Valley Forge, PA; 50280385102-005; P; D; F; 10/09/85.

Winona National & Savings Bank; Winona, MN; 50259927001-001; S; PS; F; 10/11/85.

Winona National & Savings Bank; Winona, MN; 50259927001-002; S; PS; F; 10/11/85.

Winona National & Savings Bank; Winona, MN; 50259927001-003; S; M; F; 10/11/85.

Winona National & Savings Bank; Winona, MN; 50259927001-004; S; M; F; 10/11/85.

Winona National & Savings Bank; Winona, MN; 50359927001-005; NS; PS; F; 10/11/85.

Winona National & Savings Bank; Winona, MN; 50359927001-006; NS; PS; F; 10/11/85.

Winona National & Savings Bank; Winona, MN; 50359927001-007; NS; M; F; 10/11/85.

Winona National & Savings Bank; Winona, MN; 50359927001-008; NS; M; F; 10/11/85.

Worcester County Institution for Savings; Harrison, NY; 50260148601-001; S; M; F; 10/09/85.

Worcester County Institution for Savings; Harrison, NY; 50260148601-002; S; M; F; 10/09/85.

Worcester County Institution for Savings; Harrison, NY; 50360148601-003; NS; M; F; 10/09/85.

Worcester County Institution for Savings; Harrison, NY; 50360148601-004; NS; M; F; 10/09/85.

Worcester County Institution for Savings; Harrison, NY; 50260148601-005; S; PS; F; 10/09/85.

Worcester County Institution for Savings; Harrison, NY; 50260148601-006; S; PS; F; 10/09/85.

Worcester County Institution for Savings; Harrison, NY; 50360148601-007; NS; PS; F; 10/09/85.

Worcester County Institution for Savings; Harrison, NY; 50360148601-008; NS; PS; F; 10/09/85.

York Bank & Trust Co; York, PA; 50260330001-001; S; M; F; 11/26/85.

York Bank & Trust Co; York, PA; 50360330001-002; NS; M; F; 11/26/85.

York Bank & Trust Co; York, PA; 50260330001-003; S; PS; F; 11/26/85.

York Bank & Trust Co; York, PA; 50360330001-004; NS; PS; F; 11/26/85.

First Virginia Bank, Falls Church, VA; 50329270001-002; NS; M; 10/23/85.

Security Norstar Bank; Rochester, NY; 50251220001-008; S; M; F; 11/18/85.

List B

Plans Omitted from Announcement 85-99

General American Life Insurance Co; St Louis, MO; 50330830003–001; NS; PS.

General American Life Insurance Co; St Louis, MO; 50330830003–002; NS; M.

General American Life Insurance Co; St Louis, MO; 50330830004–001; NS; PS.

General American Life Insurance Co; St Louis, MO; 50330830004–002; NS; M.

Mercantile Trust & Savings Bank; Quincy, IL 50239480001–001; S; PS.

Metropolitan Bank of Lima; Lima, OH; 50339940001–003; NS; T.

Availability of Form 8404, Computation of Interest Charge on DISC-Related Deferred Tax Liability

Announcement 86-44

New Form 8404 has been developed for use by shareholders of interest charge domestic international sales corporations (IC-DISCs). IC-DISC shareholders will use Form 8404 to figure the interest charge on DISC-related deferred tax liability based on their share of the IC-DISC's deferred DISC income and to pay the interest charge to the Internal Revenue Service. A copy of Form 8404 and instructions is included with this announcement.

An IC-DISC would first report deferred DISC income to its shareholders at the end of its second tax year that begins after December 31, 1984. The shareholder then will use Form 8404 to determine any interest charge due for the shareholder's tax year for which the deferred DISC income is reported.

For example, an IC-DISC has a short first tax year beginning on January 1, 1985, and ending on January 31, 1985. Its second tax year begins on February 1, 1985, and ends on January 31, 1986, at which time it reports deferred DISC income to its shareholder for the tax year ending January 31, 1986. The tax year of the IC-DISC's principal shareholder also begins on February 1, 1985, and ends on January 31, 1986. Accordingly, the shareholder completes Form 8404 for the tax year ending January 31, 1986, to determine if any interest is due. If interest is due, the shareholder must file Form 8404 and pay the interest charge by the date the shareholder's Federal income tax is due for the tax year ending January 31, 1986. No payments of estimated tax under section 6654 (in the case of individuals) or 6154 (in the case of corporations) are required for the interest charge.

Form 8404 should be available in many Internal Revenue District Offices in early April 1986. If the forms are not available in your Internal Revenue Office at such time, they may be ordered by calling the tax information number in the phone book listed under "United States Government Internal Revenue Service."

Form **8404**
(January 1986)
Department of the Treasury
Internal Revenue Service

Computation of Interest Charge on DISC-Related Deferred Tax Liability

▶ **Do not attach this form to your tax return; file it separately.**

OMB No. 1545-0939
Expires 9-30-88

A Check applicable box to show type of taxpayer:
☐ Corporation
☐ Individual
☐ Estate or trust

Name

Address of shareholder (number and street)

City, state, and ZIP code

B Shareholder's identifying number

C IC-DISC's identifying number

D Shareholder's tax year for which interest charge is required to be paid (see instructions)

E Name of IC-DISC for which identifying number in item C is reported:

1 Taxable income or loss on tax return (actual or estimated)	1	
2 Deferred DISC income from line 2, Part III, Schedule K (Form 1120-IC-DISC)	2	
3 Section 995(f)(2) adjustments to line 1 income or loss (see instructions)	3	
4 Combine lines 1, 2, and 3 (If zero or a loss, see instructions.)	4	
5 Tax liability on line 4 amount (see instructions)	5	
6 Tax liability per return (actual or estimated) (see instructions)	6	
7 DISC-related deferred tax liability—Line 5 less line 6	7	
8 Base period T-bill rate factor (see instructions)	8	
9 **Interest charge due**—Line 7 times line 8 (See instruction on Paying the Interest Charge.)	9	

Please Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

▶ Signature ▶ Date

Paid Preparer's Use Only

Preparer's signature ▶ Date Check if self-employed ▶ ☐ Preparer's social security no.

Firm's name (or yours, if self-employed) and address ▶ E.I. No. ▶ ZIP code ▶

General Instructions

(Section references are to the Internal Revenue Code unless otherwise noted.)

Paperwork Reduction Act Notice.—We ask for this information to carry out the Internal Revenue laws of the United States. We need it to ensure that taxpayers are complying with these laws and to allow us to figure and collect the right amount of interest. You are required to give us this information.

Purpose of Form.—Shareholders of Interest Charge Domestic International Sales Corporations (IC-DISCs) use Form 8404 to figure and report their interest on DISC-related deferred tax liability.

Who Must File.—You must file Form 8404 if you are a shareholder of an IC-DISC and the IC-DISC reports deferred DISC income to you on line 2, Part III of **Schedule K (Form 1120-IC-DISC)**, and the addition of this income would result in increased taxable income if it were included on your tax return for the tax year.

When to File.—File Form 8404 at the time you are required to file your Federal income tax return (excluding extensions) for your tax year which ends with or includes the IC-DISC's tax year end for which the deferred DISC income is reported.

For example, you are a fiscal year corporation with a July 1, 1985, to June 30, 1986, tax year and you are a shareholder in an IC-DISC with a July 1, 1985, to June 30, 1986, tax year that reports deferred DISC income to you for its year ending June 30, 1986. Because your tax year ends with the IC-DISC's tax year, you are required to file Form 8404 on September 15, 1986 (2½ months after your tax year ends).

Where to File.—File Form 8404 with the Internal Revenue Service Center where you are required to file your Federal income tax return. File the form in a separate envelope than that of your income tax return. You should keep a copy for your records.

Paying the Interest Charge.—You must pay the interest charge shown on line 9 by the date your Federal income tax for the tax year is required to be paid. If you are an individual, the interest is due on the 15th day of the fourth month following the close of your tax year. If you are a corporation, the interest is due on the 15th day of the third month following the close of your tax year.

Attach a check or money order for the full amount payable to "Internal Revenue Service." Do not combine the interest charge with any other tax or interest due. Write your identification number and "Form 8404—Interest Due" on it. (Do not use a Federal Tax Deposit Coupon (Form 8109).)

If the interest charge is not paid by the due date, interest, compounded daily, at the rate specified under section 6621, shall be imposed on the amount of unpaid interest from the due date until the date the interest is paid. Payment of estimated tax under section 6654 (individuals) or 6154 (corporations) are not required for the interest charge. See regulations section 1.995(f)-1(j)(3) for other details.

Amended Form 8404.—You are required to file an amended Form 8404 only if the amount of the DISC-related deferred tax liability (line 7) changes as a result of audit adjustments, changes you make by the filing of an amended return, or if estimates were used on your original Form 8404 and changes were made to these estimates when you filed your tax return. See regulations section 1.995(f)-1(j)(4) for details.

Specific Instructions

A. Type of Taxpayer.—Check the applicable box in the upper left portion of Form 8404 to indicate your status as a taxpayer. Shareholders that are partnerships, S corporations, estates or trusts, see regulations section 1.995(f)-1(h) for special rules.

Name and Address.—Enter the name and address as shown on your tax return from which the income or loss on line 1 of Form 8404 is obtained. If the return is a joint return, also enter your spouse's name as shown on Form 1040.

B. Identifying Number.—Individuals enter their social security number. Other filers must enter their employer identification number.

C. IC-DISC's Identifying Number.— Enter the identifying number of the IC-DISC from the Schedule K (Form 1120-IC-DISC) on which the line 2 deferred DISC income was reported to you. If income is reported to you from more than one IC-DISC, enter each IC-DISC's identifying number in item C, each IC-DISC's name in item E, and report the combined income on line 2.

D. Tax Year.—Enter in item D the calendar year or the beginning and ending dates of the tax year shown on your tax return for which the interest charge is figured.

Special Computation Rules

Carrybacks.—The determination of the shareholder's DISC-related deferred tax liability on lines 1 through 7 shall be made without taking into account any net operating loss (NOL) or capital loss carryback; or credit carryback to the tax year.

Carryovers.—The determination of the shareholder's tax liability (line 5) for the tax year is made by disregarding any loss, deduction, or credit to the extent that such loss, deduction, or credit may be carried (either back or forward) by the shareholder to any other tax year.

Note: *If the tax year is the last tax year to which the amount of carryforward (of loss, deduction, or credit) may be carried, the line 3 adjustments and line 5 tax shall be figured with regard to the full amount of such carryforward.*

For example, a shareholder had a NOL carryover to 1986 of $12,000; $10,000 income to which $10,000 of the NOL can be applied; $2,000 allowable NOL carryover to 1987; and $5,000 deferred DISC income for 1986. In this case, for purposes of figuring line 5, the allowed NOL is $10,000. Note: If 1986 were the last tax year to which the $12,000 NOL could be carried, the full $12,000 NOL would be allowed for purposes of figuring line 5 tax liability. The additional $2,000 loss would be entered on line 3.

Other Adjustments.—In figuring line 3 adjustments, take into account any income and expense adjustments that do not result in amounts that may be carried back or forward to other tax years. For example, in the case of an IC-DISC shareholder who is an individual, the amount of medical expenses allowable as a deduction under section 213 must be redetermined for purposes of line 3 adjustments. However, the amount allowable as a charitable deduction under section 170 is not redetermined because this adjustment could result in a carryback or carryover.

See regulations section 1.995(f)-1(d)(1) through (8) for other details regarding these and other special computation rules.

Line-by-Line Instructions

Line 1.—Enter on line 1 the taxable income or loss from your Federal income tax return for your tax year that ends with or includes the IC-DISC's tax year end for which deferred DISC income was reported to you. If you have not yet filed your tax return, estimate your income or loss based on all information available to you.

Line 2.—Enter the deferred DISC income from line 2, Part III of Schedule K (Form 1120-IC-DISC), for the IC-DISC tax year that ends with or within your tax year. If you are a shareholder in more than one IC-DISC that reports deferred DISC income to you, report on line 2 the sum of all deferred DISC income reported to you for the year.

Line 3.—Enter the net amount of all section 995(f)(2) adjustments to taxable income. See Special Computation Rules above for details on the income (loss) and expense adjustments to be made. If more than one adjustment is involved, attach a schedule listing each item and show the computation of the net amount.

Line 4.—Combine amounts on lines 1, 2, and 3. If the line 4 amount is zero or a loss, you do not have to file Form 8404.

Lines 5 and 6.—The tax liability on lines 5 and 6 (with and without the deferred DISC income) means the amount of tax imposed on the IC-DISC shareholder for the tax year by Chapter 1 of the Internal Revenue Code (other than taxes listed below) reduced by allowable credits (other than credits listed below).

The following taxes are not taken into account:

a Section 55 (alternative minimum tax).

b Section 56 (corporate minimum tax).

c Any other provisions described in section 26(b)(2) (relating to certain other taxes treated as not imposed by Chapter 1).

The following credits are not taken into account:

a Section 31 (taxes withheld on wages).

b Section 32 (earned income credit).

c Section 34 (fuels credit).

For individuals, the lines 5 and 6 tax liability is generally line 50 of the 1985 Form 1040 increased by any amount on line 53 and any advance earned income credit payments included in the total for line 56, and reduced by any credit on line 63 of the 1985 Form 1040.

For corporations, the lines 5 and 6 tax liability is generally line 6, Schedule J of the 1985 Form 1120, increased by any amount on line 8 and reduced by payments on line 32e, page 1 of Form 1120.

See Special Computation Rules on carrybacks and carryovers that may affect the line 5 tax computation.

If you have not yet filed your return, estimate the line 6 tax liability based on all information available to you.

Line 8.—The base period T-bill rate is defined in section 995(f)(4). The base period T-bill rate is compounded daily based on the number of days in the shareholder's tax year to determine the base period T-bill rate factor.

The base period T-bill rate for the one year period ending September 30, 1985, is 8.79%. This rate compounded daily for a 365 day tax year produces a factor of .09187, which only applies to tax years beginning in 1985.

Factors for tax years of less or more than 365 days will be published at a later date in the Internal Revenue Bulletin (IRB). If your tax year begins in 1985 and contains 365 days, enter .09187 on line 8. In all other cases, enter the base period T-bill rate factor that appears in the IRB. If you must file before the factor is available, compound 8.79% on a daily basis over the number of days in your tax year, and enter the result on line 8. See regulations sections 1.995(f)-1(b) and (c) for other details.

New base period T-bill rates and factors will be published in the future for tax years ending on or after December 31, 1986.

Line 9.—The interest charge for line 9 is line 7 times the factor on line 8.

See instruction on Paying the Interest Charge for details on when and how to pay the interest.

The annual interest charge is deductible as an interest expense for the tax year it is paid or accrued. See regulations section 1.995(f)-1(j)(2) for details on the tax year of deductibility.

Acquisitions of Insurance Companies to Which Section 338 Applies

Announcement 86-47

The Internal Revenue Service is considering whether the rules of subchapter L of the Internal Revenue Code (and, in the case of life insurance companies, section 1.817-4(d) of the Income Tax Regulations) and/or the "tax benefit" rule require the taxation of income from the release of certain reserves when an election is made under section 338 of the Code to treat the purchase of stock of an insurance company as an asset acquisition. For instance, if the parties to an insurance company acquisition allocate some of the value of the acquired company to an asset (other than goodwill) identified as, for example, "insurance contracts in force," then that allocation reflects the fact that the amount of the reserves of the acquired company exceeds the amount that an unrelated party would require as consideration for agreeing to assume the net liabilities underlying the insurance contracts of the acquired company. The Service is considering whether the acquired company's taxable income is properly increased by the amount of that excess.

Should the Service decide that income is properly increased in this situation, then as an exercise of the Commissioner's authority under section 7805(b) of the Code, the Service will not so increase the income of an acquired insurance company, provided that the acquisition date, as defined in section 338(h)(2) of the Code, occurred before April 7, 1986, the date of publication of this announcement. In addition, under the authority of section 7805(b), the Service will not so increase the income of an acquired insurance company in analogous situations in which former section 334(b)(2) applies to the liquidation of an acquired insurance company.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Patrick H. Diamond	New York, NY	Attorney & Certified Public Accountant	Indefinite from February 10, 1986
Folger P. Gifford	Cold Spring Harbor, NY	Certified Public Accountant	Indefinite from February 11, 1986
Robert Allen Beamer	Wauwatosa, WI	Attorney	Indefinite from February 19, 1986
Robert L. Cummings	Springfield, MO	Certified Public Accountant	Indefinite from February 27, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.103-10, amended.	Definition of "principal user"	1986-12 I.R.B. 19	Apr. 22, 1986
26 CFR 1.103-10, revised.	$40 million limitation on beneficiaries of certain tax-exempt bonds	1986-12 I.R.B. 22	Apr. 22, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

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Key to Abbreviations

RR	Revenue Ruling
RP	Revenue Procedure
TD	Treasury Decision
CD	Court Decision
PL	Public Law
EO	Executive Order
DO	Delegation Order
TDO	Treasury Department Order
TC	Tax Convention
SPR	State of Procedural Rules
PTE	Prohibited Transaction Exemption

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretation.

INCOME TAX

Rev. Rul. 86-52, page 42.

Carryover; reorganization; merger; controlled corporations. A loss corporation *X* formed a wholly owned subsidiary *P* which formed a wholly owned subsidiary *S*. *S* then merged into *X* in a reorganization under sections 368(a)(1)(A) and 368(a)(2)(E) of the Code, with the former *X* shareholders owning *P* stock with a fair market value exceeding 20 percent of the fair market value of the outstanding *X* stock. *X*'s net operating loss carryover is not reduced under section 382(b) before amendment by section 806(e) of the Tax Reform Act of 1976.

Rev. Rul. 86-55, page 47.

Return preparers; potential penalties; invalid assignment of refund checks. A person in a business other than tax return preparation who fills out or reviews income tax returns for its customers may be an income tax return preparer under section 7701(a)(36) of the Code and subject to potential penalties. The assignment of the customers' refund checks before the returns are processed by the Service is not a valid assignment and the Service may mail the checks directly to the taxpayers.

Rev. Proc. 86-20, page 50.

Accounting methods; change; vacation pay. The Tax Reform Act of 1984 amended section 404(b) of the Code to clarify that any plan, method, or arrangement providing deferred benefits (including deferred vacation pay) is a plan, method, or arrangement deferring the receipt of compensation. Rev. Proc. 82-32 obsoleted.

T.D. 8074, page 4.
LR-35-85, page 51.

Temporary and proposed amendments to the regulations relate to international aspects of section 338 of the Code.

Announcement 86-46, page 53.

The time is extended for employers with more than one line of business to combine lines of business under a provision that enables their employees to exclude certain fringe benefits from gross income.

Announcement 86-50, page 53.

This Bulletin contains a list of organizations that no longer qualify as organizations contributions to which are deductible under section 170(c)(2) of the Code.

EMPLOYEE PLANS

Announcement 86-45, page 52.

Final regulations under section 419 of the Code, relating to welfare benefit funds, will clarify the definition of "fund" with respect to certain arrangements between employers and insurance companies.

EXEMPT ORGANIZATIONS

Rev. Rul. 86-53, page 43.

Private foundations; self-dealing; sale to disqualified person. The sale to a disqualified person of stock by a private foundation owned by it continuously since May 26, 1969, but not constituting excess business holdings on that date, is excepted under section 53.4941(d)-4(b)(1) of the regulations from the prohibition against self-dealing under section 4941 of the Code.

ESTATE TAX

Rev. Rul. 86-54, page 44.

Installment method; closely-held business; stock redemption. An explanation is provided of the application of sections 303 and 6166 of the Code when shares of stock are redeemed and an election to pay the estate tax in installments is made. Rev. Rul. 72-188 modified.

Finding Lists begin on page 57.
Announcement of Suspensions & Disbarments begin on page 54.
Announcement of Notice of Proposed Rulemaking on page 56.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 162.—Trade or Business Expenses

26 CFR 1.162-10: Certain employee benefits.

Deductibility of deferred vacation benefits. See Rev. Proc. 86-20, page 50.

Section 303.—Distributions in Redemption of Stock to Pay Death Taxes

26 CFR 1.303-2: Requirements.

Application of section 303 of the Code when shares of stock are redeemed and an election to pay the estate tax in installments is made. See Rev. Rul. 86-54, page 44.

Section 338.—Certain Stock Purchases Treated as Asset Acquisitions

26 CFR 1.338-5T: Internal aspects of section 338 (temporary).

T.D. 8074

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, SUBCHAPTER H, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Temporary Regulations—International Aspects of Section 338.

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to international aspects of section 338 of the Internal Revenue Code of 1954 ("Code"), as added by the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") [Pub. L. 97-248, 1982-2 C.B. 462] and as amended by the Technical Corrections Act of 1982 ("TCA") [Pub. L. 97 448, 1983-1 C.B. 451] and the Tax Reform Act of 1984 ("TRA") [Pub. L. 98-369, 1984-3 C.B.(vol.1) 1]. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations cross-referenced * * * [on page 51, this Bulletin].

DATE: These regulations are effective upon publication in the FEDERAL REGISTER. These temporary regulations generally apply to stock acquisitions made after August 31, 1982.

FOR FURTHER INFORMATION CONTACT: Keith E. Stanley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20024 (Attention: CC:LR:T) (202-566-3458, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document adds new temporary regulations §1.338-5T to Part 1 of Title 26 of the Code of Federal Regulations ("CFR") and amends temporary regulations §§1.338-1T, 1.338-4T, and 1.338(h)(10)-1T. This document also amends the table of OMB control numbers in Part 602 of Title 26 of the CFR to reflect the OMB control number assigned to §1.338-5T.

Section 1.338-1T was published as T.D. 7942 in the FEDERAL REGISTER on February 8, 1984 (49 FR 4722) [1984-1 C.B. 93], and was amended and redesignated (as §1.338-1T) by temporary regulations published as T.D. 7975 in the FEDERAL REGISTER on September 6, 1984 (49 FR 35086) [1984-2 C.B. 81]. Section 1.338-1T also was amended by temporary regulations published as T.D. 8021 in the FEDERAL REGISTER on April 25, 1985 (50 FR 16402) [1985-1 C.B. 96]. The temporary regulations published on April 25, 1985, also added §1.338-4T. Sections 1.338-1T and 1.338-4T were amended by temporary regulations published as T.D. 8068 in the FEDERAL REGISTER on January 8, 1986 [1986-8 I.R.B. 9], and by temporary regulations published as T.D. 8072 in the FEDERAL REGISTER on January 29, 1986 [1986-11 I.R.B. 7]. The temporary regulations published on January 8, 1986, also added §1.338(h)(10)-1T.

New §1.338-5T provides guidance on international aspects of section 338 of the Code, as added by section 224 of TEFRA (Pub. L. No. 97-248; 96 Stat. 485) [1982-2 C.B. 462, 501] and as amended by section 306(a)(8) of the TCA (Pub. L. No. 97-448; 96 Stat. 2402) [1983-1 C.B. 451, 470] and section 712(k) of the TRA (Pub. L. No. 98-369; 98 Stat. 946) [1984-3 C.B. (Vol.1) 1, 456]. The temporary regulations added and amended by this document will remain in effect until superseded by later temporary or final regulations relating to these matters.

GENERAL OPERATION OF SECTION 338

Effect of election under section 338

Under section 338, a corporation ("purchasing corporation" or "P") that acquires the stock of another corporation ("target") in a qualified stock purchase (as defined in section 338(d)(3)) may elect (or may be deemed to elect under the consistency rules of section 338) to have the target treated as if it (1) sold all of its assets (as "old target") at fair market value at the close of the day on which the qualified stock purchase occurred ("acquisition date") and (2) purchased those assets as a new corporation ("new target") at the beginning of the following day for an amount generally equal to the price paid by P for target stock plus the liabilities of target and other relevant items. Section 338(a) and (b). The deemed sale of assets by old target generally is governed by the nonrecognition rule of section 337. The application of section 337 is limited by section 338(c)(1), however. if the maximum percentage (by value) of target stock held by P during a one-year period beginning on the acquisition date is less than 100 percent. In general, the attributes of old target, including old target's earnings and profits, are not available to new target. The net effect of a section 338 election is that P obtains a basis in target assets that generally reflects the price it paid for target stock.

Effect of consistency rules

Section 338 contains rules designed to ensure consistent treatment between stock and asset acquisitions. Consistency issues may involve a target or its target affiliate. A corporation is a "target affiliate" of a target if each of those corporations was a member of the same affiliated group at any time during so much of target's consistency period as ends on its acquisition date. Section 338(h)(6)(A). Section 338(h)(6)(B)(i), however, excludes foreign and certain domestic corporations from the status of target affiliates, except as otherwise provided in regulations (and subject to any conditions specified therein). Section 338 contains two sets of consistency rules: The asset consistency rule of section 338(e) and the stock consistency rules of section 338(f).

If a section 338 election is not made, then, under the asset consistency rule of section 338(e) (as implemented by §1.338-4T(f)), a member of the affiliated group that includes P ("P group") generally is required, pursuant to a protective carryover election actually filed by the P group or pursuant to an affirmative action carryover election deemed made by the P group, to take a carryover basis in an asset acquired from target or its target affiliate during target's consistency period if the asset is acquired in a tainted asset acquisition (as defined in §1.338-4T(f)(6)(i)(A)). For description of consistency period, see section 338(h)(4) and §1.338-4T(g)(1). If a carryover basis is required pursuant to an affirmative action carryover election, however, the District Director is empowered, upon audit, to cause a deemed election for target under section 338(e)(1) (in lieu of a carryover basis in the asset acquired from target or its target affiliate) if a deemed election is appropriate to carry out the purposes of the consistency rules of section 338(e), (f), or (i). See §1.338-4T(f)(1)(ii). The asset consistency rule reflects the view that the P group should not be permitted to obtain, from another affiliated group within the consistency period, both the stock of a corporation (with its historic inside asset basis and other tax attributes intact) and selected assets at a cost basis.

Under the stock consistency rule of section 338(f)(1), a section 338 selection for the first-acquired target ("original target") automatically applies to any target affiliate acquired by the P group in a qualified stock purchase during the consistency period. Under the stock consistency rule of section 338(f)(2), P's failure to make a section 338 election for the original target bars a section 338 election for any target affiliate acquired during the consistency period. The stock consistency rules reflect the view that the P group should not be permitted to selectively step-up the inside asset basis and eliminate the tax attributes of some but not all targets acquired during the consistency period from the same affiliated group.

STATUS OF CORPORATIONS DESCRIBED IN SECTION 338(h)(6)(B)(i) AS TARGET AFFILIATES

Introduction

The general rule prescribed in this document is that a corporation is not excluded from the status of a target affiliate by reason of section 338(h)(6)(B)(i) (relating to exclusion of foreign and certain domestic corporations from target affiliate status). There are exceptions. For purposes of the stock consistency rule of section 338(f)(1), the temporary regulations contain both a "transitional exclusion election" and a prospective "regular exclusion election" pursuant to which certain corporations described in section 338(h)(6)(B)(i) may be excluded from target affiliate status. For purposes of the asset consistency rule of section 338(e)(1), the temporary regulations contain a transitional rule that, in effect, automatically excludes certain corporations described in section 338(h)(6)(B)(i) from target affiliate status. (No prospective exclusion rule is provided for asset consistency purposes.)

The notice of proposed rulemaking published in conjunction with this document proposes that the regular exclusion election be eliminated in the final regulations. Under the proposal, the regular exclusion election generally would be available only if the acquisition date of the original target occured on or before the date of publication of the final regulations. The preamble to the notice contains a discussion of this matter.

Regular exclusion election

In general

If the original target for which an election under section 338(g) ("express election") is made is a domestic corporation, then §1.338-5T(c)(2), as added by this document, permits P in certain cases to make a "regular exclusion election" under which all excludible foreign target affiliates are excluded from the status of target affiliates for purposes of section 338(f)(1). As a consequence, the excludible foreign target affiliates are not subject to deemed elections under section 338(f)(1) by reason of the express election. A foreign corporation is an excludible foreign target affiliate if (1) absent section 338(h)(6)(B), it would be subject to a deemed election under section 338(f)(1) by reason of the express election for the domestic original target and (2) its acquisition date occurs after March 15, 1986 (and does not occur pursuant to a binding contract in effect on February 19, 1986).

Under a transitional exclusion election described below, foreign corporations acquired on or before March 15, 1986 (or after that date but pursuant to a binding contract in effect on February 19, 1986) may be excluded from the status of target affiliates for purposes of section 338(f)(1). Unlike the regular exclusion election, the transitional exclusion election also applies to domestic corporations described in section 338(h)(6)(B)(i) that are acquired during the prescribed period.

The regular exclusion election may be illustrated as follows. Assume that on June 1, 1986, P makes a qualified stock purchase of domestic target ("DT") and that DT directly holds all of the stock of controlled foreign corporations CFCT1, CFCT2, and CFCT3. The June 1, 1986, acquisition does not occur pursuant to a binding contract in effect on February 19, 1986. Each of the CFCs is an excludible foreign target affiliate. All of those excludible foreign target affiliates will be excluded from the status of a target affiliate for purposes of section 338(f)(1) if P makes a regular exclusion election in connection with an express election filed for DT. If the regular exclusion election is made, then the express election for DT will not cause deemed elections under section 338(f)(1) for CFCT1, CFCT2, and CFCT3. Because the normative rule under these temporary regulations is that corporations are not excluded from target affiliate status by reason of section 338(h)(6)(B)(i), each of the CFCs will be subject to a deemed election under section 338(f)(1) by reason of new DT's deemed purchase of their stock if a regular exclusion election is not made in connection with the express election for DT. See section 338(a)(2) and (h)(3)(B).

An elective exclusion from target affiliate status for purposes of section 338(f)(1) is permitted because of the asserted hardship to taxpayers of imposing full stock consistency with respect to foreign corporations. It is recognized that the elective exclusion permits some selectivity and is complex. However, the potential for selectivity is limited since all of the excludible foreign target affiliates automatically are subject to the regular exclusion election.

Special stock basis rules

New DT's basis in the stock of an excludible foreign target affiliate that is subject to a regular exclusion election is determined under a special basis rule if (1) old DT recognizes a section 1248(f) dividend as a result of its deemed sale of that stock (or would have recognized such a dividend if the excludible foreign target affiliate had earnings and profits), (2) the section 1248(f) dividend actually recognized (if any) is less than the gain relaized by DT on its deemed sale of that stock, and (3) any earnings and profits that would have arisen had the regular exclusion election not been made would have increased that section 1248(f) dividend. Under the special basis rule, new DT's basis in that stock is the lesser of two amounts. The first amount is the basis allocable to that stock under the normal basis allocation rules of section 338(b). The second amount is old DT's basis in that stock, increased by the section 1248(f) dividend (if any) recognized by old DT with respect to its deemed sale of that stock. Section 1.338-5T(c)(3). The special basis rule also applies to stock in an excludible foreign target affiliate that is held by any other domestic target that is subject to a deemed election under section 338(f)(1).

Under the rule discussed below, a foreign target that derives a substantial portion of its income from the conduct of a trade or business in the United States may be treated as a domestic target ("FDT") for purposes of the regular exclusion election. An FDT cannot qualify as an excludible foreign target affiliate. Under certain circumstances, however, the special basis rule of §1.338-5T(c)(3) will apply to an actual domestic target that holds stock in an FDT as if that FDT were an excludible foreign target affiliate subject to a regular exclusion election. Section 1.338-5T(c)(3)(iv). Assume, for example, that DT is deemed under section 338(a)(1) to sell all of the stock of FDT. As a result, FDT is subject to a deemed election under section 338(f)(1). If, on its acquisition date, FDT directly (or indirectly through another FDT) holds stock in an excludible foreign target affiliate that is subject to a regular exclusion election, then new DT's basis in FDT stock is determined as if FDT were an excludible foreign target affiliate. A similar basis rule applies to the excludible foreign target affiliate stock held by new FDT.

The purpose of the special basis rule of §1.338-5T(c)(3) is to preserve potential section 1248 dividend consequences with respect to the earnings and profits of the excludible foreign target affiliate that would have been triggered had it been subject to a section 338 election, *i.e.*, the earnings and profits that would have resulted from its deemed sale of assets under section 338(a)(1) ("deemed sale earnings and profits"). As explained more fully below in the discussion of section 1248, the earnings and profits of a controlled foreign corporation that is subject to a section 338 election generally are increased, for purposes of determining the amount of the section 1248 dividend to the transferor, by that controlled foreign corporation's deemed sale earnings and profits.

Assume, for example, that DT holds all of the stock of controlled foreign corporation CFCT1 and that P makes a regular exclusion election (applicable to CFCT1) in connection with an express election for DT. As a result of its deemed sale under section 338(a)(1) of the stock of CFCT1, DT will recognize a section 1248(f) dividend equal to the lesser of the gain realized in the deemed sale of CFCT1 stock or the earnings and profits of CFCT1 that are attributable to that stock under the rules of section 1248. by reason of the regular exclusion election, however, CFCT1's deemed sale earnings and profits will not be triggered since CFCT1 will not be subject to a deemed election under section 338(f)(1). Thus, DT's section 1248(f) dividend with respect to the CFCT1 stock will reflect only the earnings and profits that result from the normal operations of CFCT1.

In addition, absent the special basis rule, new DT's basis in the stock of CFCT1 would approximate, in the typical case, the current fair market value of that stock, so that the gain recognition limitation of section 1248 likely would prevent a section 1248 dividend in the event of new DT's prompt sale of that stock in a transaction with respect to which the purchaser made an election under section 338. Assume, for example, that an unrelated corporation purchases the stock of CFCT1 from DT shortly after DT's acquisition date and makes a section 338 election for CFCT1. CFCT1 presumably will have deemed sale earnings and profits as a result of the section 338 election but, by reason of the gain recognition limitation (and in the absence of the special basis rule), a section 1248 dividend likely will not accrue to DT. Thus, the special basis rule is intended to preserve the possibility of a section 1248 dividend on CFCT1's deemed sale earnings and profits in the event of a post-acquisition date sale of CFCT1 stock by DT.

Carryover basis in certain assets

A carryover basis may be imposed with respect to certain asset acquisitions when a regular exclusion election is made. This rule is discussed below in the section on asset consistency rules.

Invalidation events

A regular exclusion election is not available, or may be invalidated retroactively, if an invalidation event occurs. Each of the two invalidation events provided for in §1.338-5T(c)(2)(iii) involves a factual situation in which a deemed election under section 338(f)(1) for one or more of the excludible foreign target affiliates is considered desirable. In such cases, the "all or nothing" policy underlying the regular exclusion election dictates that *none* of the excludible foreign target affiliates be excluded from the status of a target affiliate pursuant to a regular exclusion election. An invalidation event will be disregarded if, upon the examination of a relevant return, the District Director makes certain determinations described in §1.338-5T(c)(2)(iii)(A). Unless and until those determinations are made, however, the invalidation event is given full effect.

The first invalidation event is a direct acquisition of the stock of an excludible foreign target affiliate by a P group member, provided that the excludible foreign target affiliate was a controlled foreign corporation at any time during so much of the taxable year within which its acquisition date occurs as ends on that acquisition date. (This rule also applies to the direct acquisition of stock in a domestic target described in section 1248(e) if that target holds stock in such an excludible foreign target affiliate.) Assume, for example, that P makes a qualified stock purchase of all of the stock of DT from S. Assume in addition that, during DT's consistency period, P makes a qualified stock purchase of all of the stock of FT, a target affiliate of DT, from S. All of these corporations but FT are domestic corporations. Thus, FT was a controlled foreign corporation during the relevant period. Accordingly, FT cannot be excluded from the status of a target affiliate pursuant to a regular exclusion election because, by reason of P's direct acquisition of the FT stock, a regular exclusion election cannot be made. Thus, FT will be subject to a deemed election under section 338(f)(1) if an express election is made for DT. As a result, the section 1248 dividend recognized by S will reflect FT's deemed sale earnings and profits. If FT were a subsidiary of DT, however, a regular exclusion election could be made so that FT would not be subject to a deemed election under section 338(f)(1). A potential section 1248 dividend reflecting the earnings and profits inherent in FT's asset (*i.e.*, the earnings and profits that would be triggered as deemed sale earnings and profits if FT were subject to a section 338 election) would be preserved, however, by reason of the special stock basis adjustment rule described above.

The purpose of the first invalidation event is to ensure that the section 1248 dividend (if any) recognized by S at the time it disposes of the FT stock reflects the deemed sale earnings and profits inherent in FT's assets. While it is considered appropriate to, in effect, transfer section 1248 dividend consequences associated with deemed sale earnings and profits from old DT to new DT by reason of the stock basis adjustment rule, it is not considered appropriate to transfer such a potential section 1248 dividend from S to P when S is a United States person that satisfies the stock ownership requirements of section 1248(a) with respect to FT. Nor is it practical to defer S's tax with respect to deemed sale earnings and profits until some event occurring after S disposes of the FT stock. The policy considerations underlying these determinations are examined in detail below in connection with the discussion of the "background" pertaining to the operation of section 1248 in the section 338 context.

The second invalidation event occurs if one or more excludible foreign target affiliates holds stock in a domestic corporation and that domestic corporation would be subject to a section 338 election only if the regular exclusion election did not apply. This rule ensures that all domestic targets are subject to the express election made for the domestic original target. Absent this rule, there would be an incentive, in a case in which section 338 treatment was desired for some but not all of the domestic corporations to be acquired, to attempt to shield one or more of those domestic corporations from section 338 treatment by causing a pre-acquisition date transfer of its stock to an excludible foreign target affiliate subject to a regular exclusion election. Since that excludible foreign target affiliate would not be deemed to purchase the stock of the domestic corporation under section 338(a)(2) and (h)(3)(B), section 338 treatment for that domestic corporation would be avoided. Section 367(a) would have discouraged such arrangements only in certain circumstances.

Notwithstanding the occurrence of an invalidation event after the regular exclusion election is filed, an excludible foreign target affiliate will not be made retroactively subject to a deemed election under section 338(f)(1) by reason of the section 338 election for the original target if such a deemed election would directly or indirectly increase the tax liability properly reportable in a return (of any person) with respect to which the time to make an assessment of tax has expired. Section 1.338-5T(c)(2)(iii)(D).

Original target is foreign

As noted above, the prerequisite for a regular exclusion election is a domestic original target. If the original target is a foreign corporation, a special rule may permit P to make an express election for a subsequently acquired domestic target affiliate of that foreign corporation while excluding that foreign corporation from the express election as if it were an excludible foreign target affiliate. Section 1.338-5T(c)(2)(iv). The special rule effectively operates as an exception to section 338(f)(2).

An express election may be made for the subsequently acquired domestic target pursuant to the special rule only if that express election includes a regular exclusion election, which will apply to the foreign original target as if it were an excludible foreign target affiliate. In addition, the special rule is applicable only if a regular exclusion election could have been made in an express election for the domestic target had it actually been the original target and had the foreign original target been a target affiliate of that domestic target. Thus, the special rule is not available if P's direct acquisition of the stock of the foreign original target would constitute an invalidation event under the hypothetical circumstances described in the preceding sentence, *e.g.*, if the original foreign target was a controlled foreign corporation during the relevant period. Absent this rule, the order in which domestic and non-CFC foreign targets are acquired would arbitrarily affect the availability of a regular exclusion election.

Foreign corporation treated as domestic

For purposes of applying the provisions relating to the regular exclusion election, a foreign corporation is treated as a domestic corporation if 50 percent or more of its gross income from all sources for the 3-year period ending with the close of its taxable year that precedes the taxable year in which its acquisition date occurs is effectively connected with the conduct by that corporation of a trade or business in the United States. Section 1.338-5T(c)(5). The 50 percent test is similar to the dividend source rule in section 861(a)(2)(B) with one proviso: The Commissioner may exclude any transactions of a foreign corporation during the last year of this 3-year period from gross income for purposes of this 50 percent test if he determines (on the basis of all the facts and circumstances) that the transactions were entered into pursuant to a plan to treat or avoid treating a foreign corporation as a domestic corporation.

A foreign corporation the stock of which is directly acquired by P will not be treated as a domestic corporation, however, if it was a controlled foreign corporation at any time during so much of the taxable year within which its acquisition date occurs as ends on that acquisition date and if it holds stock in a corporation that would be an excludible foreign target affiliate if FT were treated as a domestic corporation. The exception described in the preceding sentence, which operates to bar a regular exclusion election, is designed to ensure that the deemed sale earnings and profits of the corporation that is or would be an excludible foreign target affiliate (if FT were treated as a domestic corporation) are triggered under these circumstances and are taken into account for purposes of applying section 1248 to the domestic sellers of the foreign corporation since the foreign corporation itself does not generally bear United States tax on a sale or deemed sale of the excludible foreign target affiliate stock. The rationale for this exception is the same as for the first invalidation event, as discussed above.

Transitional exclusion election

In connection with an express election for an original target (whether foreign or domestic), P may make a "transitional exclusion election" under which some or all of the transitional target affiliates are excluded from the status of target affiliates for purposes of section 338(f)(1). A corporation is a transitional target affiliate if (1) it is described in section 338(h)(6)(B)(i), (2) absent section 338(h)(6)(B), it would be subject to a deemed election under section 338(f)(1) by reason of the express election for the original target, and (3) its acquisition date occurs on or before March 15, 1986 (or after that date but pursuant to a binding contract in effect on February 19, 1986). A corporation that is eligible for the more generous transitional exclusion election because it is a transitional target affiliate will not be treated as an excludible foreign target affiliate.

The transitional exclusion election is provided because taxpayers reasonably could have expected during the transitional period that corporations described in section 338(h)(6)(B)(i) would not be treated as target affiliates and therefore would not be made subject to deemed elections under section 338(f)(1) in the event of an express election for the original target. Detailed rules are provided in §1.338-5T(j)(5) for cases in which an overlap exists between the transitional exclusion election and the regular exclusion election.

The following table compares the transitional exclusion election to the regular exclusion election:

	Regular exclusion election (§1.338-5T(c))	*Transitional exclusion election §1.338-5T(j)(1)-(3)*
Targets eligible for election	Foreign targets acquired after 3-15-86	Foreign targets and domestic targets described in section 338(h)(6)(B)(i) acquired on or before 3-15-86
"All or nothing" election	Yes	No[1]
Invalidation events	Yes	No[1]
Special carryover basis rule for stock in targets subject to election	Yes	No
Special carryover basis rule for certain asset acquisitions when election made[2]	Yes	Yes (but more limited than for regular exclusion election)
Special rule for treating foreign corporation as domestic	Yes	No
Section 338 election permitted for corporation other than original target	Yes	Yes

Special asset consistency rules applicable to corporations described in section 338(h)(6)(B)(i)

General rule for target affiliate status

Subject to the transitional rule discussed herein, corporations described in section 338(h)(6)(B)(i) (*i.e.*, foreign and certain domestic corporations) are not excluded from the status of target affiliates for purposes of the asset consistency rule of section 338(e). Thus, an asset acquisition from such a corporation may be a tainted asset acquisition. (Note that if an exclusion election is made, whether regular or transitional, a carryover basis is imposed with respect to certain asset transfers even though those transfers technically do not constitute tainted asset acquisitions. The circumstances in which such a carryover basis is imposed are described in detail below.) The principal abuse against which the asset consistency rule of section 338(e)(1) is directed is the ability to selectively step-up the basis of directly acquired assets while preserving historic asset bases and tax attributes within the target. Because this abuse exists whether or not the transferor is described in section 338(h)(6)(B)(i), corporations described therein are not exempt, prospectively, from the asset consistency rule. The greatest potential hardship resulting from this rule is that a tainted asset acquisition from such a corporation may cause a deemed election under section 338(e) and §1.338-4T(f)(1)(ii). The purchasing corporation may avoid this hardship, however, by filing a protective carryover election.

Transitional rule

Under the transitional rule, an asset acquisition from a corporation described in section 338(h)(6)(B)(i) that occurs on or before March 15, 1986 (or after that date but pursuant to a binding contract in effect on February 19, 1986) will in no case be considered a tainted asset acquisition. Section 1.338-5T(j)(6)(i). Thus, the acquiring P group member does not take a carryover basis in that asset pursuant to the asset consistency rule and, in the absence of a protective carryover election, is not at risk for a deemed election under section 338(e) as a result of that acquisition. This transitional rule exception is provided because taxpayers reasonably could have expected that asset acquisitions during the transitional period from corporations described in section 338(h)(6)(B)(i) would not be subject to the asset consistency rule of section 338(e).

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[1] It should be noted that, while P is permitted to make the transitional exclusion election for less than all of the transitional target affiliates, a transitional exclusion election for any one transitional target affiliate effectively applies automatically to any other corporation that would be a target but for that transitional exclusion election (*i.e.*, a corporation for which a qualified stock purchase would occur only if the transitional target affiliate were deemed under section 338(a)(2) to purchase its assets).

[2] These rules are discussed below in the section on asset consistency rules.

Carryover asset basis: Regular exclusion election

As a general rule, a carryover basis under the authority of section 338 is imposed with respect to asset transfers only when an express election is *not* made, since the requirement is directed toward cases in which P wishes to avoid section 338 treatment and therefore does not make an express election. The only two exceptions to the general rule arise when a regular or transitional exclusion election is made.

If a regular exclusion election is made in connection with an express election for DT, then a P group member that acquires an asset from an excludible foreign target affiliate (or from a non-target foreign target affiliate) during the consistency period must take a carryover basis in that asset as if the acquisition were subject to an affirmative action carryover election if, in the absence of the express election, the asset acquisition would be a tainted asset acquisition. Section 1.338-5T(c)(4). The District Director does not have authority, in this context, to cause a deemed election for an excludible foreign target affiliate in lieu of a carryover basis in the transferred asset. Absent this special asset consistency rule, the P group could make a regular exclusion election for excludible foreign target affiliates but selectively step-up the basis of some assets held by such corporations (or by non-target foreign target affiliates). Under the special asset consistency rule, a carryover basis is retained both with respect to assets that remain inside excludible foreign target affiliates and with respect to assets directly acquired by P group members during the consistency period from such corporations and from non-target foreign target affiliates. Thus, the foreign corporations are treated, in effect, as a separate subgroup with respect to which an express election is not made.

Carryover asset basis: Transitional exclusion election

A carryover basis rule similar to the one applicable in the regular exclusion election context applies to asset acquisitions from (1) a transitional target affiliate for which a transitional exclusion election is made or (2) any other corporation that would be subject to a deemed election under section 338(f)(1) but for a transitional exclusion election. Thus, asset acquisitions from non-target foreign target affiliates are not subject to the carryover basis rule in the transitional exclusion election context. Compare §1.338-5T(j)(6)(iii) with §1.338-5T(c)(4). For a special overlap rule, see §1.338-5T(j)(5)(iv).

TREATMENT OF STOCK DESCRIBED IN SECTION 338(h)(6)(B)(ii)

General rule for section 338(h)(6)(B)(ii) stock

Under section 338(h)(6)(B)(ii), stock held by a target affiliate of target in a foreign corporation, a DISC, or a section 1248(e) corporation is excluded from the operation of section 338 except as otherwise provided in regulations (and subject to any conditions specified therein). Except during a transitional period, the temporary regulations added by this document provide that such stock is *not* excluded from the operation of section 338. Section 1.338-5T(c)(1)(ii) and (j)(7).

The apparent purpose of section 338(h)(6)(B)(ii) is to approximate the treatment that was available under repealed section 334(b)(2). Thus, for example, assume that domestic target DT holds all of the stock of domestic corporation DT1, and that DT1 holds all of the stock of controlled foreign corporation CFCT2. Under repealed section 334(b)(2), in the event of a liquidation of DT, a section 1248(f) dividend would not be triggered to DT1 with respect to its CFCT2 stock unless P also chose to liquidate DT1. In the section 338 context, absent section 338(h)(6)(B)(ii), an express election for DT causes a deemed election for DT1 under section 338(f)(1), and section 1248(f) is triggered by DT1's deemed sale of CFCT2 stock. Section 338(h)(6)(B)(ii) could be applied to bar a section 1248(f) dividend at the DT1 level. By contrast section 338(h)(6)(B)(ii) does not bar a section 1248(f) dividend at the DT level if DT rather than DT1 holds the CFCT2 stock.

Section 338(h)(6)(B)(ii) thus creates an arbitrary distinction between stock in a foreign corporation that is directly held by an original target for which an express election is made (DT in the above example) and stock in a foreign corporation that is held by a domestic target affiliate of the original target (DT1 in the above example). Because there is no reason not to treat CFC2 stock in the above example like any other recapture asset of DT1, the temporary regulations provide that section 338(h)(6)(B)(ii) does not apply except during a transitional period. Thus section 1248(f) consequences with respect to CFCT2 stock will not turn on whether DT1 rather than DT holds the CFCT2 stock (except during the transitional period).

Transitional rule for section 338(h)(6)(B)(ii) stock

Under a transitional rule set out in §1.338-5T(j)(7), stock described in section 338(h)(6)(B)(ii) that is held by a target subject to a deemed election under section 338(f)(1) may be excluded from the operation of section 338 if the acquisition date of the target occurs on or before February 12, 1986 or pursuant to a binding contract in effect on that date ("eligible target"). In order to obtain this treatment, P must make a transitional stock exclusion election in connection with an express election made for the original target. The transitional stock exclusion election may be made for one or more of the eligible targets. The transitional stock exclusion election applies to all excluded stock held by the eligible target for which the election is made, *i.e,* all of the stock described in section 338(h)(6)(B)(ii) that is held by that eligible target at the close of its acquisition date, other than stock of a transitional target affiliate for which a transitional exclusion election is not made. Thus, excluded stock may include stock of a corporation that is not a target affiliate.

If a transitional stock exclusion election is made for an eligible target, then that eligible target is not deemed under section 338(a) to sell and purchase the excluded stock it holds at the close of its acquisition date. Thus, that eligible target will not recognize a section 1248(f) dividend with respect to excluded stock. In addition, that eligible target's basis (as new target) in excluded stock is the same as its basis in that stock as old target.

The transitional stock exclusion election is provided because taxpayers reasonably could have expected during the transitional period that stock described in section 338(h)(6)(B)(ii) would be excluded from the operation of section 338.

SPECIAL RULES FOR OPERATION OF OFFSET PROHIBITION ELECTION IN INTERNATIONAL CONTEXT

Offset prohibition election inapplicable if no U.S. tax to transferor

As noted above, the normative consequence of a tainted asset acquisition under the asset consistency rule of section 338(e) is a carryover basis to the acquiring P group member. If the trainted asset transfer occurs within a P group that does not file consolidated returns ("INA acquisition"), however, the acquiring P group member takes a basis in the transferred asset that is determined without regard to the carryover basis election if an offset prohibition election is made in connection with a protective carryover election. As a consequence of the offset prohibition election, the transferor in an INA acquisition may not offset the gain recognized on the transfer ("INA gain") by any deductions and the tax attributable to INA gain may not be offset by certain tax credits. See §1.338-4T(f)(6)(iv) *Answer 2* (ii). If the tainted asset transfer occurs within a P group that files consolidated returns ("ICA acquisition") and if deferred gain on that transfer if restored because the transferor ceases to be a member of the P group ("remaining ICA gain amount"), then the existence of an offset prohibition election prevents a reduction (by the remaining ICA gain amount) in the transferred asset's basis in the hands of the transferee. As in the case of INA gain, the remaining ICA gain amount may not be offset by deductions of the P group and the tax attributable to that gain may not be offset by certain tax credits available to the P group. See §1.338-4T(f)(6)(iv) *Answer 3* (iv). A carryover basis (or basis reduction) is not imposed when an offset prohibition election applies because, by reason of the limitations on deductions and credits, an appropriate tax on the transferor's gain will be collected.

Under the temporary regulations added by this document, an otherwise effective offset prohibition election does not apply to transfers by foreign and certain other corporations since, in many circumstances, an appropriate U.S. tax cannot be collected from the transferor. If, however, a foreign transferor corporation is required by pay U.S. tax on the transfer because income or gain on that transfer is effectively connected with the conduct by that transferor of a trade or business within the United States, then the offset prohibition election may apply to that asset. Section 1.338-5T(d)(1).

Special limitation on foreign tax credit when offset prohibition election made

The temporary regulations added by this document add a special section 904 limitation for offset prohibition gain. "Offset prohibition gain" is gain that is subject to limitations on deductions and credits by reason of an offset prohibition election. This special limitation ensures an appropriate foreign tax credit for foreign source offset prohibition gain. However, while foreign taxes on other income items and from other taxable years cannot be applied against any excess limitation for offset prohibition gain, foreign taxes attributable to offset prohibition gain ("offset prohibition foreign taxes") that exceed the separate limitation for offset prohibition gain may be credited in the current year to the extent that the otherwise applicable section 904 limitation exceeds the foreign taxes subject to that limitation that are paid or accrued during the current year. Any remaining offset prohibition foreign taxes carryover to other years as excess foreign taxes subject to the otherwise applicable limitation. Section 1.338-5T(d)(2).

SPECIAL EXCEPTIONS TO SECTION 338(e)(1) UNDER THE AUTHORITY OF SECTION 338(e)(2)(D)

The temporary regulations added by this document add two exceptions to the asset consistency rule of section 338(e)(1) under the authority of section 338(e)(2)(D). Asset acquisitions subject to one of these exceptions, accordingly, will not be considered tainted asset acquisitions. The first exception is for an asset transfer in which the transferee takes a stepped-up basis solely by reason of the transferor's recognition of gain under section 367(a). The second exception applies to the transfer of foreign currency in certain cases. Section 1.338-5T(e). For additional exceptions under the authority of section 338(e)(2)(D), see §1.338-4T(f)(5).

OPERATION OF SECTION 1248 IN SECTION 338 CONTEXT

Background

For a foreign target having solely trade or business income that is *not* effectively connected, the manner of taxing is deemed sale gain under section 338(a)(1) raises two questions: First, how should section 1248 be applied in the section 338 context? Second, do policy and administrative considerations regarding this foreign target outweigh policy and administrative considerations, developed in the context of domestic targets, that a purchaser's election under section 338 should not create a tax to a selling group filing consolidated returns?

In connection with the first question, in general, the United States directly taxes trade or business income of a foreign corporation that is effectively connected with its conduct of a trade or business within the United States. If a foreign corporation has neither effectively connected income nor U.S. source income but is a controlled foreign corporation ("CFC"), as defined in section 957, a principal mechanism since 1962 for exacting an indirect United States tax with respect to its income has been section 1248, under which a U.S. person holding at least 10 percent of the stock of the CFC (a "U.S. shareholder") is required to treat gain on the disposition of such stock as a dividend to the extent of the CFC's earnings and profits that are attributable to the transferred stock. If the foreign corporation is not a CFC, foreign personal holding company, foreign investment company, or, in the case of a foreign corporation that is a CFC, if the

U.S. person holds less than 10 percent of its stock, the United States traditionally has declined to exact either a direct or an indirect tax on the foreign corporation's noneffectively connected income unless and until it is actually distributed.

In connection with the second question, a basic policy of section 338 in the domestic context is that P should not be permitted to unilaterally affect the tax liability of the seller of domestic target stock by making a section 338 election. Thus, under section 338(h)(9), a target acquired from a consolidated selling group is disaffiliated for purposes of its deemed sale of assets. As a result, P cannot trigger income reportable in the seller's consolidated return by making a section 338 election for the domestic target. Because deemed sale gain therefore is reported in a return for which new target is liable, P indirectly bears the liability for that tax. (Although an election under 338(h)(10) causes deemed sale gain to be reported in the seller's consolidated return, both the seller and P must agree to that election.) Allowing P (the purchaser of all of the CFC's stock) to unilaterally elect section 338 and thereby affect the section 1248 dividend recognized by the U.S. sellers of the CFC is not consistent with this basic policy.

Allowing P to unilaterally affect the U.S. seller's section 1248 dividend would also create problems of administration. In order for the seller to properly calculate its section 1248 dividend, that seller would need to be notified of the section 338 election. Effective tax administration, moreover, would require that the Internal Revenue Service be notified of the identity of the U.S. sellers that may be affected under section 1248 by the section 338 election.

After reviewing the policy and administrative considerations, the Treasury Department has determined that the United States should indirectly tax under section 1248 the selling U.S. shareholders of CFC stock on the CFC's deemed sale gain under section 338(a)(1). This indirect tax is consistent with the traditional scope for exercising United States taxing jurisdiction of CFCs and would be imposed under the circumstances contemplated by existing law, principally section 1248.

Taxing a U.S. shareholder selling CFC stock on the CFC's deemed sale gain is appropriate. Section 338(a)(1) provides that the deemed sale is treated as if it were a transaction to which section 337 applies. Recapture items that are recognized notwithstanding section 337 increase section 1248 earnings and profits. *See Pielemier v. United States*, 543 F.2d 81 (9th Cir. 1976); *Brigham v. United States*, 539 F.2d 1312 (3d Cir. 1976). This increase in section 1248 earnings and profits reflects an adjustment to the depreciation deductions ordinarily reflected in those earnings and profits. Upon the actual liquidation of a CFC under section 337, the section 1248 dividend reported by a U.S. shareholder takes into account in the single transaction (and subject to a single limitation for the shareholder's recognized gain) both the unadjusted section 1248 earnings and profits and the recapture earnings and profits. The result should be the same when section 337 is treated as applying to the CFC by reason of section 338(a)(1). In contrast, a domestic corporation typically reports its depreciation deductions and any recapture of those deductions in different taxable years.

Taking deemed sale earnings and profits into account in determining the section 1248 dividend to U.S. sellers also increases the likelihood that an appropriate foreign tax credit will be allowed with respect to the deemed sale earnings and profits. The prior deduction of the recaptured item will have decreased the earnings and profits of a prior taxable year of the CFC. Foreign taxes paid with respect to prior years, however, will be deemed paid by the U.S. seller to the extent that the section 1248 dividend derives from earnings and profits from prior years. (If earnings and profits from prior years were previously distributed, foreign taxes may be carried forward five years.) If deemed sale earnings and profits were taxed to the purchaser instead of the U.S. seller, it is unlikely that an appropriate foreign tax credit would be allowed with respect to such income.

Taxing the selling U.S. shareholder on the deemed sale gain yeilds a result analogous to treatment of the deemed sale gain of a domestic target that was not included in a consolidated return of a selling group. That domestic target's deemed sale gain is included with its other income (or loss) in the final income tax return as old target for so much of its regular taxable year that was terminated at the close of its acquisition date. See §1.338-1T(f)(2)(i). Similarly, a CFC's deemed sale gain is taken into account with other income (or loss) in its section 1248 earnings and profits for so much of its regular taxable year that was so terminated.

It is impractical to tax the pruchaser ("P") on the recapture earnings and profits instead of the selling U.S. shareholder. In view of the manner in which the United States traditionally has taxed the earnings of such a foreign target, P (if it were to be taxed) idealy would be taxed on the section 1248 dividend that the U.S. sellers of target stock would have recognized that they been required to take into account the target's deemed sale earnings and profits. Thus, P would have to ascertain whether S was a U.S. shareholder. Moreover, in order to determine the amount of a section 1248 dividend, P would need detailed tax information relating to the holding period and basis of those selling U.S. shareholders in target stock. Even assuming that the correct dividend amount is calculated, taxing P would be a departure from the basic principle of section 1248 of indirectly taxing the shareholders of a CFC, especially since the actual tax effect to P of that dividend likely would differ from the tax effect of that dividend to the U.S. sellers due to differences in foreign tax credit positions and rates of U.S. tax as between P and such sellers. If P were a foreign corporation that did not file U.S. income tax returns, special procedures would be necessary in order to collect *any* tax measured by reference to deemed sale earnings and profits (*e.g.*, a toll charge in the amount of the tax as a condition for a valid section 338 election) which would have the indirect effect of S bearing the tax. Policy, considerations aside, it is certainly more practical to tax S than P on the deemed sale earnings and profits.

In conclusion, these policy and administrative considerations favor imposing an indirect tax on deemed sale gain only on the U.S. sellers of CFC stock and only through existing statutory mechanisms (with certain modifications), principally section 1248. An indirect tax should not be imposed on

P. These policy and administrative considerations outweigh the domestic section 338 policy that P should not be permitted to unilaterally affect the tax liability of the seller of target stock by making a section 338 election.

Application of Section 1248 to sellers of stock in foreign T

Temporary regulations §1.338-5T(g), as added by this document, provides rules for the operation of section 1248 in connection with a section 338 election for a target that is a controlled foreign corporation ("CFCT"). As noted above, the deemed sale of assets under section 338(a)(1) is governed by section 337. Had CFCT actually sold its assets in a sale described in section 337, amounts a domestic corporation would have recognized notwithstanding the operation of section 337 would have been taken into account as earnings and profits for purposes of applying section 1248. See §§1.1248-2(d)(2)(ii) and 1.1248-3(b)(2)(ii). Section 1.338-5T(g)(2)(i) and (3) makes clear that the deemed sale under section 337 also creates earnings and profits ("deemed sale earnings and profits") that must be taken into account by the U.S. persons subject to section 1248 that sell CFCT stock to P on CFCT's acquisition date. However, any gains (or losses) that a domestic corporation would have recognized in the deemed sale of assets by reason of the operation of section 338(c)(1) are disregarded. (As discussed in more detailed below, a tax on section 338(c)(1) gain may be collected from minority CFCT shareholders that do not transfer their CFCT stock to P.)

A special rule under section 1248 is provided for sales of CFCT stock to the P group by U.S. persons during CFCT's 12-month acquisition period but prior to CFCT's acquisition date ("staggered stock sale rule"). The stagged stock sale rule attributes to such CFCT stock the same share of deemed sale earnings and profits that would have been attributed to such stock had it been sold on CFCT's acquisition date, *i.e.*, on the last day of old CFCT's final taxable year. Absent this rule, only a pro rata portion of that share, based on the number of days in old CFCT's final taxable year during which the seller held the CFCT stock, would be attributed to that stock. Moreover, absent the staggered stock sale rule, *none* of the deemed sale earnings and profits would be attributed to that stock if it were sold during the prior taxable year. This staggered stock sale rule also applies to earnings and profits resulting from actual asset sales occurring on or after the first day of CFCT's taxable year in which the particular stock sale occurs and prior to the close of to CFCT's acquisition date. Such an actual asset sale creates earnings and profits for this purpose, however, only to the extent of the gain on the asset sale that would have been recognized by old CFCT had it been a domestic corporation, had it held that asset on its acquistion date, and had the deemed sale price of that asset been equal to the actual amount realized on the sale or exchange of that asset. Section 1.338-5T(g)(2)(i) and (4). The staggered stock sale rule does not apply to stock transfers occurring on or before February 12, 1986 or after that date but pursuant to a binding contract in effect on that date.

Carryover CFCT stock

A special rule under section 1248 also is provided for "carryover CFCT stock," *i.e.*, CFCT stock held by non-P group members on the close of CFCT's acquisition date ("minority stock") and nonrecently pruchased CFCT stock as defined in section 338(b)(6)(B) for which a gain recognition election under section 338(b)(3)(A) is not made. With respect to carryover CFCT stock, the earnings and profits of old CFCT (along with the foreign taxes attributable to such earnings and profits) carryover to new CFCT for purposes of (1) characterizing distributions with respect to carryover CFCT stock as dividends, (2) characterizing gain on the disposition of CFCT stock as a section 1248 dividend, and (3) determining the amount of the foreign tax credit resulting from such dividends. The amount of old CFCT's earnings and profits that may be taken into account with respect to a share of carryover CFCT stock, however, shall not exceed the amount of the section 1248 dividend that the holder of that share would have recognized had it sold that share at fair market value to a member of the P group on CFCT's acquisition date (or, with respect to nonrecently purchased stock, had such stock been subject to a gain recognition election) ("section 1248 amount"). Section 1.338-5T(g)(6).

The carryover CFCT stock rule ensures that appropriate section 1248 consequences will attend a post-acquisition date disposition of such stock. In addition, the rule eliminates the incentive for holders of minority stock to retain such stock until after CFCT's acquisition date, *i.e.*, until after its earnings and profits account is eliminated. Absent this rule, holders of minority stock could avoid a section 1248 dividend measured by older CFCT's earnings and profits simply by waiting until after CFCT's acquisition date to transfer such stock to P. Finally, the carryover CFCT stock rule serves as a mechanism whereby a tax on section 338(c)(1) gain is borne (if at all) only by the persons that caused that gain to exist. Thus, for purposes of determining the section 1248 amount, all of the earnings and profits of old CFCT resulting from gain (or loss) that a domestic corporation would have recognized by reason of the operation of section 338(c)(1) are allocated solely to the carryover CFCT stock that causes section 338(c)(1) to apply to the transaction, *e.g.*, carryover CFCT stock that is minority stock and that is not purchased by a member of the P group during the one-year period beginning on CFCT's acquistion date. The policies underlying the rules for carryover CFCT stock are generally similar to those underlying regulations promulgated under section 367(b).

Special CFC definition

A special definition is provided for determining whether a foreign target is a controlled foreign corporation. Under this definition, for purposes of determining whether a foreign target is a controlled foreign corporation for a relevant taxable year, all sales of its stock that are included in the qualified stock purchase of such stock are deemed to occur on that foreign target's acquisition date if that foreign target ceases to be a CFC solely by reason of the qualified stock purchase of its stock. For example, assume that foreign purchasing corporation FP purchases 60 of the 100 outstanding shares of CFCT stock from domestic corporation S on December 31, 1986, and purchases the remaining 40 shares on January 1, 1987. Absent the special definition, CFCT is not a controlled foreign corporation in 1987 and, therefore, the earnings and profits resulting from its deemed sale or assets are not properly reflected in S's section 1248 dividend. The special definition ensures that such earnings and profits are properly reflected in that dividend.

TREATMENT OF GAIN ON DEEMED SALE AS EFFECTIVELY CONNECTED INCOME AND AS INCOME FROM SOURCES WITHIN THE UNITED STATES

Under temporary regulations §1.338-5T(h)(1), as added by this document, a foreign target's gain on the deemed sale of an item of property under section 338(a)(1) is treated as income that is effectively connected with the conduct of a trade or business within the United States and as income from sources within the United States if, for the three-year period ending with the close of the taxable year preceding old foreign target's final taxable year (or for so much of that 3-year period as that target held the particular item of property), more than 50 percent of the gross income it derived from that item of property was effectively connected income. Similarly, under §1.338-5T(h)(2), a domestic target's gain on the deemed sale of an item of property is treated as income from sources within the United States if, for the three-year period ending with the close of the taxable year preceding old domestic target's final taxable year (or for so much of that 3-year period as that target held the particular item of property), more than 50 percent of the gross income it derived from that item of property was income from sources within the United States. No inference should be drawn regarding the United States tax treatment of gain amounts not described in §1.338-5T(h). These rules are designed to eliminate uncertainty as to the source of and the United States tax with respect to gain arising in the deemed sale of assets.

AMENDMENTS TO §1.338-1T

Special suspension of time eliminated

Prior to publication of this document, §1.338-1T(j) provided that the last day for making an election under section 338 was suspended until the date specified in a Treasury decision setting forth regulations under section 338(h)(6)(B) if (1) the target was a corporation described in section 338(h)(6)(B)(i) that had a target affiliate or (2) the target had a target affiliate that was described in section 338(h)(6)(B)(i) or that held stock in a foreign corporation, a DISC, or a corporation described in section 1248(e). In order to make a section 338 election notwithstanding the suspension, a special declaration was required in the statement of section 338 election.

Under §1.338-1T(c), as amended by T.D. 8068 [1986-8 I.R.B. 9], a section 338 election for any qualified stock purchase occurring after August 31, 1982, need not be filed before the later of the due date specified in section 338(g)(1) or March 15, 1986. Under §1.338-1T(j), as amended by this document, the March 15, 1986, date also applies to corporations described in §1.338-1T(j)(1), and no suspension of time after that date is provided for such corporations.

Under §1.338-1T(j), as amended by this document, the requirement of a special declaration in the statement of section 338 election is retained but applies only to statements of section 338 election that are filed on or before March 14, 1986 and that do not contain a transitional or regular exclusion election or a transitional stock exclusion election.

Prior to amendment by this document, a statement of section 338 election that omitted the special declaration could be perfected only by the timely filing of a perfecting declaration. As amended by this document, however, §1.338-1T(j) provides that such a statement of section 338 election may be perfected either by filing a perfecting declaration on or before March 15, 1986, or by making a timely regular exclusion election, transitional exclusion election, or transitional stock exclusion election. The making of such an election would be inconsistent with an intent *not* to perfect the statement of section 338 election.

The class of acquisitions subject to §1.338-1T(j) is broadened by this document to include targets described in section 338(h)(6)(B)(i) that do *not* have a target affiliate ("stand-alone targets"). Stand-alone targets are included because of the substantial uncertainty that existed, prior to publication of this document, as to the application of section 338 to corporations described in section 338(h)(6)(B)(i). The effect of this rule is that a statement of section 338 election filed for such a corporation on or before March 14, 1986 is valid only if it contains the special declaration (or one of the exclusion elections) or is perfected pursuant to the procedures described above.

Notice to U.S. persons required

As noted above, the section 1248 dividend for a U.S. person that sells stock of a target that is a controlled foreign corporation ("CFCT") to P may be affected by P's decision to file a section 338 election for CFCT. Minority shareholders that retain CFCT stock also may be affected by that election. Accordingly, a new §1.338-1T(k)(7) establishes a notice requirement for such persons. The penalty for failure to provide notices to certain U.S. persons is the invalidation of the section 338 election.

Schedule of corporations

Section 1.338-1T(e) provides that a schedule containing information relating to corporations subject to an election under section 338 must be attached to the statement of section 338 election and to certain returns of targets subject to that election. As amended by this document, §1.338-1T(e) also requires that the schedule contain information on excludible foreign target affiliates that are subject to a regular exclusion election. In addition, the schedule must contain information on the U.S. persons to whom P is required to provide notice under new §1.338-1T(k)(7).

New rules are provided regarding the returns to which the schedule and certain other "required items" must be attached under §1.338-1T(e)(2). If a U.S. person is required to report a section 1248 dividend in its income tax return by reason of its sale of foreign target stock to P, then the required items must be attached to that return. Section 1.338-1T(e)(2)(v)(B). Other U.S. persons that hold stock in foreign target on its acquisition date or on the first day thereafter must attach the required items to the Forms 5471 they are required to file with respect to foreign target for its taxable years that include those days. Section 1.338-1T(e)(2)(v)(C). (As part of the notice requirement, P must provide the required items to the U.S. persons described in the preceding two sentences.) If a foreign target's first return as new target is for a taxable year subsequent to its first taxable year, then the required items must be attached to that return (this is an existing requirement). Section 1.338-1T(e)(2)(v)(D). (Section 1.338-1T(e)(2)(v)(C) and (D) replaces §1.338-1T(k)(6) of the existing regulations, which is removed by this document.)

Under §1.338-1T(e)(3), the standard penalty for failure to comply with the requirements relating to the schedule of corporations is invalidation of the penalty waiver rule of §1.338-1T(h) (automatic waiver of certain penalties). (The penalty will not apply solely by reason of the failure to attach the required items to certain returns over which P may have no control.) Under §1.338-1T(e)(3), as amended by this document, the penalty also applies when amended returns required by reason of the retroactive invalidation of a regular exclusion election are not timely filed.

Miscellaneous amendments

A number of minor technical and clarifying amendments are made to §1.338-1T. (The enumeration in this paragraph is not inclusive.) Section 1.338-1T(d)(2) (relating to the treatment of a common parent as the agent of P for purposes of signing the statement of section 338 election) is amended to make clear that it serves merely as a cross-reference to the relevant consolidated return regulation and is not intended to alter the rules provided therein. A number of amendments are made to §1.338-1T(k). The meaning of "subject to United States tax" in §1.338-1T(k) is clarified. (This change is not intended to be substantive.) Section 1.338-1T(k)(1) is amended to apply to *any* election made under the authority of section 338, *e.g.*, the protective carryover election under §1.338-4T(f)(6). Similarly, section 1.338-1T(k)(5), which exempts certain foreign corporations from the requirement that an employer identification number be furnished, is made applicable to *any* election made under the authority of section 338.

AMENDMENTS TO §1.338-4T

Exception to section 338(e) for property subject to timely disposition

Section 1.338-4T(f)(5) *Answer* (vii) provides that an asset acquisition is subject to an exception to section 338 (e)(1) (and therefore will not be a tainted asset acquisition for purposes of the consistency rule of section 338(e)) if the P group disposes of that asset to an unrelated person (not including a target affiliate of target) on or before the date specified in §1.338-4T(f)(5) *Answer* (vii). This document amends that provision to also prohibit disposition to a target affiliate of an affected target. In addition, this document amends the provision to provide that the asset will be considered disposed of if the P group member holding the asset ceases to be a member of the P group (and ceases to be related to any member of the P group) on or before the specified date. A corporation is not treated as a ceasing to be a member of the P group, however, if it ceases to exist during the consistency period by reason of a transaction described in section 381(a) and if the acquiring corporation (within the meaning of section 381(a)(1)) is a member of the P group.

Amendment to rules relating to P group members that must sign the protective carryover election statement

Under §1.338-4T(f)(6)(ii) *Answer 1* (ii), each corporation included in the P group at any time during so much of the target's consistency period as ends on the day a protective carryover election is filed must join in making that protective carryover election. Under that provision, as amended by this document, a corporation that ceases to be a P group member prior to the day on which the protective carryover electon is filed ("former P group member") need not join in making the protective carryover election if it did not make aa tainted asset acquisition (as defined in §1.338-4T(f)(6)(i)(A)) while a member of the P group. Caution should be exercised when relying on the rule described in the preceding sentence, however, if the former P group member made *any* asset acquisitions during the consistency period from the original target, an affected target, or a target affiliate of one of those targets, since it is not always clear that an acquisition is not a tainted asset acquisition. See, *e.g.*, the exception in §1.338-4T(f)(3) for acquisitions in the ordinary course of trade or business. Note, however, that an asset acquisition that otherwise would be a tainted asset acquisition may be subject to the timely disposition exception of §1.338-4T(f)(5) *Answer* (vii) if the former P group member ceased to be a member within the time specified in §1.338-4T(f)(5) *Answer* (vii).

An additional exception to the requirement that all P group members must join in making the protective carryover election is made for certain foreign P group members, whether or not they are members on the day the protective carryover election is filed. Under this exception, a representative of a foreign P group member is not required to sign the protective carryover election unless that foreign P group member (1) is required to file a United States income tax return for its taxable year in which the protective carryover election is filed, (2) is, at any time during its taxable year in which the protective carryover election is filed, a controlled foreign corporation, a foreign investment company, or a foreign corporation the stock ownership of which is described in section 552(a)(2), (3) purchases any of the stock included in the qualified stock purchase of the target (or of an affected target), or (4) holds stock in a foreign P group member that satisfies one or more of the three preceding conditions. If a foreign P group member is a controlled foreign corporation, its United States shareholders may make the protective carryover election on its behalf.

A foreign P group member subject to the exception described in the preceding paragraph must be identified in the protective carryover election as if it were required to join in making the election. Tainted asset acquisitions made by such a corporation will be subject to the affirmative action carryover basis rules, however, unless the corporation joins in making the election, *i.e.*, unless a representative signs the protective carryover election. The District Director will not have authority under these circumstances to impose a deemed election under section 338 (e)(1) pursuant to §1.338-4T(f)(1)(ii).

Miscellaneous amendments

A number of minor technical and clarifying amendments are made to §1.338-4T. (The enumeration in this paragraph is not inclusive.) A more comprehensive definition of a "tainted asset acquisition" is provided in amended §1.338-4T(f)(6)(i)(A). As amended, that provision also clarifies that the protective carryover election is irrevocable. *Answer 2* (ii)(B) and *Answer 3* (iv)(D) of §1.338-4T(f)(6)(iv) (relating to restrictions on the use of certain credits when an offset prohibition election is made) are clarified. Finally, §1.338-4T(k)(1) *Answer 3* (relating to the operation of section 338(h)(12)) is amended to clarify that nonrecognition on actual asset sales pursuant to section 338(h)(12) is available notwithstanding that a liquidation of target immediately after the plan of complete liquidation was adopted would have been governed by section 332, provided that each corporation that would have been a distributee corporation in that hypothetical liquidation is liquidated under the circumstances described in section 337(c)(3).

A number of typographical errors in §1.338-4T are corrected by this document.

REGULATORY FLEXIBILITY ACT; EXECUTIVE ORDER 12291; AND PAPERWORK REDUCTION ACT OF 1980

A general notice of proposed rulemaking is not required by 5 U.S.C. for temporary regulations. Accordingly, these temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required. The collection of information contained in these regulations has been submitted to the Office of Management and Budget in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements hae been approved by OMB (Control number 1545-0702).

DRAFTING INFORMATION

The principal author of these temporary regulations is Duane H. Pellervo of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * *

Adoption of amendments to the regulations

Accordingly, Parts 1 and 602 of Title 26 of the Code of Federal Regulations are amended as follows:

PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * §§1.338-1T, 1.338-4T, 1.338-5T, and 1.338(h)(10)-1T also issued under 26 U.S.C. 338.

Par. 2. A new §1.338-5T is added immediately after §1.338-4T to read as follows:

§1.338-5T International aspects of section 338 (temporary).

(a) *Introduction*—(1) *Effective date.* Except as otherwise provided in this section, this section applies to stock acquisitions for which the acquisition date (determined without section 224(d)(5) of TEFRA) occurs after August 31, 1982.

(2) *Outline of topics.* In order to facilitate the use of this section, this subparagraph (2) lists the paragraphs, subparagraphs, and subdivisions contained in this section.

(a) Introduction.
(1) Effective date.
(2) Outline of topics.
(3) Application of §1.338-4T to foreign persons and certain domestic corporations.
(4) Procedural rules.
(b) Nomenclature and definitions.
(1) Nomenclature.
(i) Corporations.
(ii) Individuals.
(2) Definitions.
(c) Application of section 338 to corporations and stock described in section 338(h)(6)(B).
(1) General rule.
(2) Elective exclusion of foreign corporations from target affiliate status.
(i) General rule.
(ii) Excludible foreign target affiliate.
(iii) Regular exclusion election not available in certain cases.
(A) General rule.
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(C) Excludible foreign target affiliate holds stock in domestic corporation.
(D) Exception when statute of limitations has expired.
(iv) Special rule if original target is a foreign corporation.
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(B) Foreign target as original target.
(C) Qualifying domestic target affiliate.
(D) Special rule inapplicable if express election for original foreign target filed.
(E) Effect of invalidation event.
(F) Coordination with protective carryover election.
(v) Procedure for making regular exclusion election.
(A) General rule.
(B) Contents of regular exclusion statement.
(C) Transitional rule.
(vi) Annotation on required schedule.
(vii) Procedure if regular exclusion election invalidated subsequent to filing.
(A) Required schedule must be amended.
(B) Filing of amended returns.
(3) Effect of regular exclusion election on basis in excludible foreign target affiliate stock.
(i) General rule.
(ii) Excess basis amount eliminated.
(iii) Subject to section 1248(f)(1).
(iv) Special rules if foreign target treated as domestic.
(v) Cross-reference
(4) Special asset consistency rule if regular exclusion election made.
(i) General rule.
(ii) Deemed election not imposed.
(iii) Relevant target.
(5) Certain foreign corporations treated as domestic corporations.
(i) General rule.
(ii) Event year.
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(6) Examples.
(d) Special rules applicable to offset prohibition electon.
(1) Offset prohibition election inapplicable to certain transfers
(i) General rule.
(ii) Exception for certain foreign transferors

(2) Limit on crediting foreign tax against U.S. tax on offset prohibition gain.

(i) Defintiions.

(A) Offset prohibition gain.

(B) Offset prohibition foreign taxes.

(c) Otherwise applicable section 904 limitation.

(ii) One-way special foreign tax credit limitation for offset prohibition foreign taxes.

(iii) Excess special limitation disregarded for purposes of section 904(c).

(iv) Special rule for creditability of offset prohibition foreign taxes in excess of special limitation.

(v) Coordination with restricted credit provisions of §1.338-4T(f)(6)(iv).

(3) Examples.

(e) Certain transactions subject to an exception to section 338(e)(1) under the authority of section 338(e)(2)(D).

(1) Basis step-up attributable to gain recognized under section 367.

(2) Acquisition of foreign currency.

(i) General rule.

(ii) No inference regarding character of gain or loss

(f) Effect of section 338 on foreign target

(g) Operation of section 1248 if section 338 election made.

(1) Scope.

(2) General rules.

(i) Transfer of CFCT or before acquisition date.

(ii) Effect of gain recognition election.

(iii) Carryover CFCT stock.

(iv) Special rule for determining status as controlled foreign corporation

(v) Section 1248(c)(2) subsidiary

(vi) Special deemed stock sale rule

(3) Enhanced earnings and profits amount if stock transferred on CFCT's acquisition date.

(4) Enhanced earnings and profits amount if stock transferred before CFCT's acquisition date.

(1) General rule.

(ii) Affected taxable year of CFCT.

(iii) CFCT's recapture earnings and profits.

(iv) Recapture amount.

(v) Exception to enhancement rule of paragraph (g)(4)(i) for transitional period stock transfer.

(vi) Section 1248(c)(2) subsidiary with same taxable year as CFCT.

(A) Recapture amounts for subsidiaries.

(B) Earnings and profits of subsidiaries.

(C) Recapture earnings and profits for block.

(D) Application of general rule.

(vii) Section 1248(c)(2) subsidiary with taxable year different from CFCT's.

(5) Section 338(c)(1) inapplicable.

(6) Carryover of old CFCT earnings and profits for purposes of carryover CFCT stock.

(i) General rule.

(ii) Cap on carryover of earnings and profits.

(iii) Section 1248 amount for stock other than section 338(c)(1) stock.

(iv) Section 1248 amount for section 338(c)(1) stock.

(v) Section 338(c)(1) stock.

(vi) Section 338(c)(1) amount.

(vii) Old CFCT earnings and profits unaffected by post-acquisition date deficits.

(viii) Character of CFCT stock as carryover CFCT stock eliminated upon disposition.

(7) Application of principles of this paragraph to section 1246.

(8) Examples.

(h) Treatment of gain in deemed sale of assets as income effectively connected with the conduct of a trade or business within the United States and as from sources within the United States.

(1) Foreign target.

(2) Domestic target.

(3) Measurement period.

(4) No inference regarding transactions not described.

(i) Reserved

(j) Transitional rules for corporations and stock described in section 338(h)(6)(B).

(1) Transitional elective exclusion from target affiliate status.

92) Transitional target affiliate.

(i) General rule.

(ii) Acquired on or before March 15, 1986.

(iii) Hypothetical acquisition date of transitional target affiliate.

(3) Special rule for certain original targets described in section 338(h)(6)(B)(i).

(i) General rule.

(ii) Transitional excludible original target.

(iii) Qualifying target affiliate.

(A) General rule.

(B) Excepted target.

(iv) Coordination with protective carryover election.

(4) Examples.

(5) Relationship between transitional exclusion election and regular exclusion election.

(i) In general.

(ii) Special rule for application of regular exclusion election.

(iii) Limitation on application of paragraph (c)(3) of this section.

(iv) Limitation on application of paragraph (c)(4) of this section.

(v) Overlap between paragraphs (c)(2)(iv) and (j)(3) of this section.

(A) In general.

(B) Illustrative factual situation.

(C) Express election for transitional excludible original target or qualifying target affiliate.

(D) Express election for qualifying domestic target affiliate.

(E) Express election for FT3 bars regular exclusion election.

(F) FT3 is DT3.

(G) FT1 is DT1.

(H) FT2 is DT2.

(I) Effect of invalidation event after express election filed for DT5.

(vi) Examples.

(6) Transitional asset consistency rules for corporations described in section 338(h)(6)(B)(i).

(i) General rule.

(ii) Definitions.

(A) Transitional asset acquisition.

(B) Acquisition made on or before March 15, 1986.

(C) Excluded transferror.

(iii) Special asset consistency rule for acquisition from excluded transferor

(A) General rule.

(B) Deemed election not imposed.

(iv) Examples.

(7) Treatment of stock described in section 338(h)(6)(B)(ii).

(i) Transitional stock exclusion election.

(ii) Section 338(h)(6)(B)(ii) stock.

(iii) Eligible target.

(iv) Effect of exclusion from operation of section 338.

(v) Effect of difference between carryover basis amount and regular basis amount.

(vi) Tacking of old eligible target's holding period.

(vii) Examples.

(8) Transitional section 338(h)(6)(B)

election procedures.

(i) General rule.

(ii) Special procedure if express election filed on or before March 15, 1986.

(iii) Amendment procedure if transitional statement filed on or before March 15, 1986.

(iv) Acquisition date of transitional target affiliate or eligible target occurs after transitional section 338(h)(6)(B) statement filed.

(v) Contents of transitional section 338(h)(6)(B) statement.

(3) *Application of §1.338-4T to foreign persons and certain domestic corporations*. Except as otherwise provided in this section, the provisions of §1.338-4T apply to—

(i) Foreign corporations,

(ii) Domestic corporations described in section 338(h)(6)(B), and

(iii) Individuals that are not U.S. residents or citizens.

(4) *Procedural rules*. For additional procedural rules, see §1.338-1T.

(b) *Nomenclature and definitions*—(1) *Nomenclature*. The nomenclature in §1.338-4T(b)(1) also applies to this section except as follows:

(i) *Corporations*. Each term used in §1.338-4T(b)(1) to refer to a corporation (*e.g.*, "T") is preceded in this section either by the letter "D," connoting a domestic corporation, the letter "F," connoting a foreign corporation (as defined in section 7701(a)(5)), or the letters "CFC," connoting a controlled foreign corporation (as defined in section 957). ("CFC" is used rather than "F" only when the corporation's status as a controlled foreign corporation is significant.) However, the term "P" is used without a prefix when the purchasing corporation's status as a foreign or domestic corporation is not significant. (All terms used in §1.338-4T to refer to corporations are references to domestic corporations.)

(ii) *Individuals*. Each term used in §1.338-4T(b)(1) to refer to an individual (*i.e.*, "A" and "B") is preceded in this section either by the letter "D," connoting a U.S. resident or citizen, or "F," connoting an individual other than a U.S. resident or citizen. (All terms used in §1.338-4T to refer to individuals are references to U.S. residents or citizens.)

(2) *Definitions*. The definitions in §1.338-4T also apply to this section, except that the definition of a domestic corporation in §1.338-4T(b)(6) is applied without the exclusion therein for DISCs, corporations described in section 934(b) or 1248(e), and corporations to which an election under section 936 applies.

(c) *Application of section 338 to corporations and stock described in section 338(h)(6)(B)*—(1) *General rule*. Except as otherwise provided in this paragraph (c) and in paragraph (j) of this section (relating to transitional rules)—

(i) A corporation that would be a target affiliate within the meaning of section 338(h)(6)(A) but for section 338(h)(6)(B)(i) shall be considered a target affiliate for all purposes of section 338 and

(ii) Stock held by a target affiliate in a foreign corporation or in a domestic corporation that is a DISC or that is described in section 1248(e) shall not be excluded from the operation of section 338.

(2) *Elective exclusion of foreign corporations from target affiliate status*—(i) *General rule*. If P files an express election for DT, an original target, then, solely for purposes of the stock consistency rule of section 338(f)(1), P also may elect (in the manner prescribed in paragraph (c)(2)(v) of this section) to exclude all excludible foreign target affiliates from the status of target affiliate ("regular exclusion election"). If the regular exclusion election is not or cannot be made (*e.g.*, because DT is FT or because a section 338 election is not filed for DT), then none of the excludible foreign target affiliates may be excluded from the status of a target affiliate. A section 338 election cannot be made for any excludible foreign target affiliate that is subject to a regular exclusion election. For a special stock basis rule that applies when a regular exclusion election is made, see paragraph (c)(3) of this section. For a special asset consistency rule that applies when a regular exclusion election is made, see paragraph (c)(4) of this section. For treatment of certain foreign corporations as domestic corporations, see paragraph (c)(5) of this section. For transitional rules, see paragraph (j) of this section.

(ii) *Excludible foreign target affiliate*. An "excludible foreign target affiliate" is a foreign corporation that meets two conditions. The first condition is that, absent section 338(h)(6)(B), it would be subject to a deemed election under section 338(f)(1) by reason of the express election for DT. The second condition is that it must not be a transitional target affiliate within the meaning of paragraph (j)(2) of this section, *i.e.*, its acquisition date must not occur on or before March 15, 1986 (or after March 15, 1986, but pursuant to a binding contract in effect on February 19, 1986). See Examples (1) and (2) in paragraph (c)(6) of this section.

(iii) *Regular exclusion election not available in certain cases*—(A) *General rule*. Except as provided in paragraph (c)(2)(iii)(D) of this section (relating to effect of statute of limitations), a regular exclusion election cannot be made (or is retroactively invalidated) if an invalidation event described in this subdivision (iii) occurs and is not disregarded by the District Director. An invalidation event shall be disregarded only if the District Director determines, in connection with the examination of a return that would be affected by the invalidation event, that *(1)* a principal purpose for the transaction that constitutes the invalidation event is avoidance of the regular exclusion election and *(2)* the principles underlying this subdivision (iii) would not be significantly compromised by disregarding the invalidation event. The invalidation event shall be given full effect pursuant to the provisions of this subdivision (iii) unless and until these determinations are made by the District Director.

(B) *Controlled foreign corporation directly acquired*. An invalidation event occurs if, during the consistency period, P (or any other member of the P group) directly acquires (other than by reason of a deemed purchase under section 338(a)(2)) any stock in *(1)* an excludible foreign target affiliate that was a controlled foreign corporation at any time during so much of that excludible foreign target affiliate's taxable year within which its acquisition date occurs (or would occur if a valid regular exclusion election were not made in the express election) as ends on that acquisition date or *(2)* a domestic target described in section 1248(e) that is subject to a section 338 election and that holds stock in an excludible foreign target affiliate described in *(1)* of this subdivision (B). For purposes of determining whether the excludible foreign target affiliate is a controlled foreign corporation during the relevant period, the special rule of paragraph (g)(2)(iv) of this section applies. For purposes of determining whether P directly acquires any stock, the special deemed stock sale rule of paragraph (g)(2)(vi) of this section applies. See Examples (3), (5), and (8) in paragraph (c)(6) of this section.

(C) *Excludible foreign target affiliate holds stock in domestic corporation*. An invalidation event occurs if one or more excludible foreign target affiliates hold stock in a domestic corporation and that domestic corporation would be subject to a section 338 election only if the regular exclusion election did not apply. See Examples (9) through (13) in paragraph (c)(6) of this section.

(D) *Exception when statute of limitations has expired*. If a regular exclusion election is retroactively invalidated by reason of a subsequent invalidation event, and if, as of the day of the invalidation event, the period within which to make an assessment of tax has expired for any return (of any person) that would be affected by treating a particular excludible foreign target affiliate as not subject to the previously made regular exclusion election ("barred target"), then, notwithstanding the invalidation event, the barred target will continue to be treated as subject to a regular exclusion election. Because of the invalidation event, however, excludible foreign target affiliates (other than barred targets) will not be treated as subject to a regular exclusion election. For purposes of this subdivison (D), a return would be affected by treating an excludible foreign target affiliate as not subject to a previously made regular exclusion election if such treatment would have the effect, directly or indirectly, of increasing the tax liability reported in that return.

(iv) *Special rule if original target is a foreign corporation*—(A) *General rule*. This subdivision (iv) applies if the original target is a foreign corporation other than a transitional excludible original target within the meaning of paragraph (j)(3)(ii) of this section, *i.e.*, other than an original target with an acquisition date that occurs on or before March 15, 1986 (or after March 15, 1986, but pursuant to a binding contract in effect on February 19, 1986. If, subsequent to its qualified stock purchase of the stock of such a foreign original target, P (or another member of the P group) makes a qualified stock purchase of the stock of a qualifying domestic target affiliate, then an express election may be made for the qualifying domestic target affiliate as if it were the original target, provided that a regular exclusion election is made in that express election. If the express election and regular exclusion election are made, then the foreign original target and all other foreign corporations that would have been subject to a deemed election under section 338(f)(1) by reason of an express election for that foreign original target will be treated as excludible foreign target affiliates subject to a regular exclusion election. Caution should be exercised when applying this subdivision (iv), since a subsequently acquired domestic target affiliate will not be considered a qualifying domestic target affiliate under paragraph (c)(2)(iv)(C) of this section if, under the hypothetical circumstances described therein, an invalidation event occurs before an express election for that domestic target affiliate (as a deemed original target) is filed. In such a case, the express election may be made only for the foreign original target. If the time to make that express election has expired, then, by reason of section 338(f)(2), the subsequently acquired domestic target affiliate cannot be made subject to section 338. If, by contrast, the invalidation event occurs *after* the express election is filed for the subsequently acquired domestic target affiliate, then that express election will be valid but the otherwise excluded foreign targets also will be subject to that express election. See paragraph (c)(2)(iv)(E) of this section. See also examples (7), (8), and (13) in paragraph (c)(6) of this section. For a similar rule applicable to a transitional excludible original target, see paragraph (j)(3) of this section. For rules governing cases in which the provisions of this subdivision (iv) and paragraph (j)(3) of this section overlap, see paragraph (j)(5)(v) of this section.

(B) *foreign target as original target*. Pursuant to the definition in §1.338-4T(b)(4), a foreign target is an original target if there exists no previously acquired target as to which a section 338 election would cause a deemed election under section 338(f)(1) for the foreign target. For purposes of applying this definition, the section 338 election referred to therein should be considered one with respect to which a regular exclusion election is not made.

(C) *Qualifying domestic target affiliate*. A domestic target is a "qualifying domestic target affiliate" if four conditions are satisfied. The first condition is that the domestic target must be a corporation that would have been subject to a deemed election under section 338(f)(1) had an express election been made for the foreign original target. The second condition is that the qualified stock purchase of the domestic target's stock must not occur by reason of a deemed purchase under section 338(a)(2). The third condition is that a regular exclusion election could have been made in an express election filed for that domestic target had it been the original target, had the foreign original target been a target affiliate of that domestic target, and had the acquisition date of the foreign original target occurred during the consistency period of that domestic target. For purposes of the third condition, an invalidation event occurring after the express election is filed is disregarded. The fourth condition is that there must be no other domestic target that satisfies the first three conditions and that has an earlier acquisition date. If two or more domestic corporations with the same acquisition date satisfy the first three conditions, then P may select any one of them to be the qualifying domestic target affiliate. The selection is made by filing an express election that names one such domestic corporation as the original target. See Examples (7), (8), and (13) in paragraph (c)(6) of this section.

(D) *Special rule inapplicable if express election for original foreign target filed*. An express election for a qualifying domestic target affiliate cannot be made if an express election already has been made for the original foreign target.

(E) *Effect of invalidation event*. If an invalidation event occurs after the express election and regular exclusion election are filed, then, subject to the barred target rule of paragraph (c)(2)(iii)(D) of this section, the original foreign target will be treated as subject to a deemed election under section

338(f)(1) by reason of the express election and no corporation will be excluded from the status of a target affiliate pursuant to the previously filed regular exclusion election.

(F) *Coordination with protective carryover election.* If P wishes to make a protective carryover election under §1.338-4T(f)(6) in lieu of an express election and if an express election could have been made for a target other than the actual original target pursuant to this subdivision (iv) or paragraph (j)(3) of this section, then the protective carryover election need not be filed before the close of the period within which an express election could have been made for a target other than the original target. For all purposes of the protective carryover election other than the time for filing that election, the actual original target is treated as the original target (*e.g.*, for purposes of identifying the original target in the protective carryover election statement).

(v) *Procedure for making regular exclusion election*—(A) *General rule.* The regular exclusion election is made on the Form 8023 filed for DT in the manner shown on the form. If the revised Form 8023 showing the manner for making this election is not available, a statement ("regular exclusion statement") must be attached to the Form 8023. The regular exclusion election, once made, is treated as an integral part of the Form 8023, *e.g.*, for purposes of §1.338-1T(e)(2)(i) (requiring that the Form 8023 be attached to certain returns). The regular exclusion election is irrevocable.

(B) *Contents of regular exclusion statement.* The regular exclusion statement must be identified prominently as a regular exclusion election under §1.338-5T(c)(2) and must contain the following declaration (or a substantially similar declaration): "THE REGULAR EXCLUSION ELECTION IS HEREBY MADE FOR ALL EXCLUDIBLE FOREIGN TARGET AFFILIATES (AS DEFINED IN §1.338-5T(c)(2)(ii) and (iv))." The regular exclusion statement must be signed (in the manner prescribed in §1.338-1T(d)(1)(v)) by a person authorized to act on behalf of P.

(C) *Transitional rule.* If a regular exclusion election is not made in an express election filed on or before March 15, 1986, a regular exclusion election nonetheless may be made if, on or before March 15, 1986, a copy of the previously filed express election (generally Form 8023), with a copy of the regular exclusion statement attached, is filed with the Internal Revenue Service Center(s) with which the express election is required to be filed under §1.338-1T(c) and (d).

(vi) *Annotation on required schedule.* For additional information that must be included on the schedule required by §1.338-1T(e) if a regular exclusion election is made, see §1.338-1T(e)(1)(i)(F).

(vii) *Procedure if regular exclusion election invalidated subsequent to filing*—(A) *Required schedule must be amended.* If, subsequent to the making of a regular exclusion election, that exclusion election is invalidated by reason of an invalidation event described inparagraph (c)(2)(iii) of this section, then the schedule required by §1.338-1T(e) must be amended pursuant to §1.338-1T(e)(1)(ii)(B) and (e)(2)(ii)(B). See Examples (3) and (11) in paragraph (c)(6) of this section.

(B) *Filing of amended returns.* If any returns of P group members (determined as of the day of the invalidation event) need to be amended as a result of an invalidation event, then the penalty prescribed in §1.338-1T(e)(3)(i) (inapplicability of the waiver rule of §1.338-1T(h)) applies unless appropriate amended returns (with a copy of the previously filed Form 8023 and the revised schedule attached) are filed on or before the 120th day after the date of the invalidation event.

(3) *Effect of regular exclusion election on basis in excludible foreign target affiliate stock*—(i) *General rule.* If a domestic target (*i.e.*, DT or a domestic affected target) is subject to section 1248(f)(1) on its deemed sale under section 338(a)(1) of stock in an excludible foreign target affiliate to which a regular exclusion election applies ("EFTA stock"), then the basis of that EFTA stock in the hands of that domestic target, as new domestic target, shall be the lesser of—

(A) The basis amount that, absent this subparagraph (3), is allocable to that EFTA stock under section 338(b) ("regular basis amount") or

(B) Old domestic target's basis in that EPTA stock immediately before its deemed sale of assets under section 338(a)(1), increased by the dividend (if any) included in old domestic target's gross income under section 1248(f)(1) as a result of its deemed sale of that EFTA stock ("special basis amount").

(ii) *Excess basis amount eliminated.* If new domestic target's basis in EFTA stock is determined under this subparagraph (3), then the excess (if any) of the regular basis amount over the special basis amount is eliminated. For purposes of allocating new domestic target's adjusted grossed-up basis among the other assets of new domestic target, however, such excess is treated as if it were an amount allocated to the EFTA stock.

(iii) *Subject to section 1248(f)(1).* A domestic target is considered "subject to section 1248(f)(1)" on its deemed sale of EFTA stock if all of the following three requirements are satisfied:

(A) That target recognizes a section 1248(f) dividend as a result of such deemed sale (or would have recognized such a dividend if the excludible foreign target affiliate had earnings and profits).

(B) The section 1248(f) dividend (if any) actually recognized by that target is less than the gain it is deemed to realize on such deemed sale.

(C) If earnings and profits hypothetically would arise had the regular exclusion election not been made (whether or not they would actually arise), they would increase the section 1248(f) dividend recognized by that target on its deemed sale of that EFTA stock.

(iv) *Special rules if foreign target treated as domestic.* This subdivision (iv) applies if three conditions are satisfied. The first condition is that a domestic target (*i.e.*, DT or a domestic affected target) must be subject to section 1248(f)(1) on its deemed sale under section 338(a)(1) of stock in a foreign target that is treated as a domestic target under paragraph (c)(5) of this section (an "FDT"). (A domestic corporation described in section 1248(e) is considered an FDT for purposes of this subdivision (iv).) For purposes of applying the definition of paragraph (c)(3)(iii) of this section, stock in an FDT is considered EFTA stock. The second condition is that such FDT ("FDT1") must, at the close of its aquisition date, directly or indirectly (through one or more other FDTs ("intermediate FDTs")) hold EFTA stock. The third condition is that, if deemed sale earnings and profits of the excludible foreign target affiliate hypothetically would arise had the regular exclusion election not been made, they would increase the section 1248(f) dividend recognized by the domestic target on its deemed sale of FDT1 stock. If the three conditions are satisfied, then the following consequences apply:

(A) The basis of the domestic target, as new domestic target, in FDT1 stock shall be determined under paragraph (c)(3)(i) of this section as if FDT1 were an excludible foreign target affiliate.

(B) The basis of FDT1, as new FDT1, in directly held EFTA stock shall be the lesser of the following two amounts: The first amount is the regular basis amount (within the meaning of paragraph (c)(3)(i)(A) of this section). The second amount is the basis of old FDT1 in the EFTA stock, increased by an amount equal to the excess of the section 1248(f) dividend (if any) actually recognized by the domestic target on its deemed sale of FDT1 stock over the amount that dividend would have been had *(1)* FDT1 not held the stock of EFTA and *(2)* the gain realized on the deemed sale of the FDT1 stock were not affected by *(1)* of this subdivision (B).

(C) The basis of FDT1 in the stock of an intermediate FDT, and the basis of each intermediate FDT in the stock of another intermediate FDT or in EFTA stock, shall be determined in the same manner as under pararaph (c)(3)(iv)(B) of this section.

(v) *Cross-reference.* For nonapplication of this subparagraph (3) during a transitional period, see paragraph (j)(5)(iii) of this section. For examples of this subparagraph (3), see Examples (15) through (18) in paragraph (c)(6) of this section.

(4) *Special asset consistency rule if regular exclusion election made*—(i) *General rule.* A P group member must take a carryover basis in an asset acquired from an excludible foreign target affiliate or from a foreign target affiliate of a relevant target as if the asset acquisition were subject to an affirmative action carryover election if (A) a regular exclusion election is made and (B) in the absence of an express election, the asset acquisition would be considered a tainted asset acquisition (as defined in §1.338-4T(f)(6)(i)) with respect to any relevant target. See Examples (19) through (21) in paragraph (c)(6) of this section. For guidance on the affirmative action carryover election, see §1.338–4T(f)(6). For a limitation on the rule of this subparagraph (4) in the transitional context, see paragraph (j)(5)(iv) of this section. Except as provided in this subparagraph (4) or in paragraph (j)(6)(iii) of this section (relating to a transitional rule), no asset acquisition shall be treated as a tainted asset acquisition if an express election is made.

(ii) *Deemed election not imposed.* In no event shall the District Director impose a deemed election under section 338(e)(1) for any excludible foreign target affiliate as a result of an asset acquisition described in this subparagraph (4).

(iii) *Relevant target.* A "relevant target" is the actual original target (and not a target deemed to be the original target in the express election actually filed) or any other corporation that, absent section 338(h)(6)(B), would be subject to a deemed election under section 338(f)(1) by reason of an express election for that original target.

(5) *Certain foreign corporations treated as domestic corporations*—(i) *General rule.* A foreign original target is treated as a domestic corporation for purposes of this paragraph (c) if 50 percent or more of its gross income from all sources for the 3-year period ending with the close of its taxable year that precedes its event year (or for so much of that 3-year period as that foreign corporation has been in existence) is effectively connected with the conduct by that corporation of a trade or business in the United States. This 50 percent gross income test also applies to a foreign corporation that otherwise would be an excludible foreign target affiliate (including by reason of the treatment of a foreign original target as a domestic original target pursuant to the preceding sentence). The 50 percent test of this subdivision (i) shall be applied in the same manner as the 50 percent test of section 861(a)(2)(B) (relating to source of certain dividends) except that the Commissioner may exclude any transactions of a foreign corporation during the last year of this 3-year period from gross income for purposes of this 50 percent test if he determines (on the basis of all the facts and circumstances) that the transactions were entered into pursuant to a plan to treat or avoid treating a foreign corporation as a domestic corporation. See Examples (4), (6), and (9) through (13) in paragraph (c)(6) of this section.

(ii) *Event year.* The "event year" of a foreign corporation is the taxable year of that corporation in which its acquisition date occurs (or would occur, absent a regular exclusion election, in the event of an express election for the original target).

(iii) *Exception.* If, during the consistency period, P (or any other member of the P group) directly acquires (other than by reason of a deemed purchase under section 338(a)(2)) any stock in a foreign target (including a foreign corporation that would be a target only if a regular exclusion election were not made in the express election), then that foreign target will in no case be treated as a domestic corporation if (A) it was a controlled foreign corporation at any time during so much of the taxable year within which its acquisition date occurs (or would occur if a regular exclusion election were not made in the express election) as ends on that acquisition date and (B) it holds stock in a corporation that would be an excludible foreign target affiliate if the foreign corporation were treated as a domestic corporation. For purposes of determining whether the corporation is a controlled foreign corporation during the relevant period, the special rule of paragraph (g)(2)(iv) of this section applies. See Examples (4) through (6) and (18) in paragraph (c)(6) of this section.

(6) *Examples.* The provisions of this paragraph (c) may be illustrated by the following examples. In each example, assume unless otherwise expressly indicated that all of the corporations are calendar year corporations and that none of the foreign corporations are treated as domestic corporations under paragraph (c)(5) of this section. Assume also that DS (or FS) has held all of the stock of the corporations it sells to P since those corporations were organized. Finally, assume that none of the invalidation events described in the following examples are subsequently disregarded pursuant to paragraph (c)(2)(iii)(A) of this section.

Example (1). On July 31, 1986, P purchases from DS all of the stock of DT in a qualified stock purchase. DT holds all of the stock of FT1, FT1 holds all of the stock of FT2, and FT2 holds all of the stock of FT3. Because a section 338 election for DT would cause deemed elections under section 338(f)(1) for FT1, FT2, and FT3 in the absence of section 338(h)(6)(B), those foreign corporations are excludible foreign target affiliates under paragraph (c)(2)(ii) of this section. If P makes a regular exclusion election in an express election filed for DT, then that express election will not cause deemed elections under section 338(f)(1) for FT1, FT2, and FT3, since those corporations will not be considered target affiliates for purposes of the stock consistency rule of section 338(f)(1).

Example (2). Assume the same facts as in Example (1). Assume in addition that on August 31, 1986, P also purchases from DS all of the stock of DT4, a domestic corporation, in a qualified stock purchase. DT4 holds all of the stock of FT5. Because a section 338 election for DT would cause a deemed election under section 338(f)(1) for FT5 in the absence of section 338(h)(6)(B), FT5 is an excludible foreign target affiliate under paragraph (c)(2)(ii) of this section. If P makes a regular exclusion election in an express election filed for DT, then that express election will cause a deemed election under section 338(f)(1) for DT4 but not for FT1, FT2, FT3, and FT5. If a regular exclusion election is *not* made in the express election filed for DT, then that express election will cause deemed elections for FT1, FT2, FT34, and FT5, as well as for DT4.

Example (3). Assume the same facts as in Example (2), except that DT4 is FT4, a foreign corporation. Because a section 338 election for DT would cause a deemed election under section 338(f)(1) for FT4 in the absence of a regular exclusion election, FT4 is an excludible foreign target affiliate under paragraph (c)(2)(ii) of this section. Because DS is a domestic corporation, FT4 was a controlled foreign corporation during the period beginning on January 1, 1986, and ending on August 31, 1986. Accordingly, that acquisition is an invalidation event and a valid regular exclusion election cannot be made in an express election filed for DT. See paragraph (c)(2)(iii)(B) of this section. (If a Form 8023 purporting to make a regular exclusion election already has been filed, then that regular exclusion election is retroactively invalidated by the qualified stock purchase of FT4 and the procedures described in paragraph (c)(2)(vii) of this section apply.)

Example (4). (i) Assume the same facts an in Example (3), except that FT4 satisfies the 50 percent gross income test of paragraph (c)(5)(i) of this section for the 3-year period preceding 1986. None of the other foreign corporations satisfy the 50 percent gross income test.

(ii) FT4 is not treated as a domestic corporation even though the 50 percent gross income test is satisfied, however, since the exception of paragraph (c)(5)(iii) of this section applies, *i.e.*, FT4 was directly acquired by P (other than by reason of a deemed purchase under section 338(a)(2)), FT4 was a controlled foreign corporation during the period beginning on January 1, 1986, and ending on August 31, 1986, and FT4 holds the stock of a corporation, FT5, that would be an excludible foreign target affiliate if FT4 were treated as a domestic corporation. Accordingly, the result is the same as in Example (3).

Example (5). Assume the same facts as in Example (3), except that DS is FS. FS is not a controlled foreign corporation. Under these facts, FT4 is not a controlled foreign corporation at any time during the period beginning on January 1, 1986, and ending on August 31, 1986. Because the acquisition of FT4 therefore is not described in paragraph (c)(2)(iii) (B) of this section, P may make a regular exclusion election in an express election filed for DT, and that regular exclusion election will apply to FT1, FT2, FT3, FT4, and FT5.

Example (6). (i) Assume the same facts as in Example (1), except that DT is FT. FT satisfies the 50 percent gross income test of paragraph (c)(5)(i) of this section for the 3-year period preceding 1986. None of the other foreign corporations satisfy the 50 percent gross income test.

(ii) A regular exclusion election cannot be made in an express election filed for FT, since FT is not a domestic original target. See paragraph (c)(2)(i) or this section. FT cannot satisfy the requirements for domestic corporation status under paragraph (c)(5) of this section, since the exception of paragraph (c)(5)(iii) of this section applies, *i.e.*, FT was directly acquired by P (other than by reason of a deemed purchase under section 338(a)(2)), FT was a controlled foreign corporation during the period beginning on January 1, 1986, and ending on July 31, 1986, and FT holds the stock of a corporation, FT1, that would be an excludible foreign target affiliate if FT were treated as a domestic corporation. Because a regular exclusion election cannot be made in an express election for FT, such an express election will cause deemed elections under section 338(f)(1) for FT1, FT2, and FT3.

Example (7). (i) Assume the same facts as in Example (6). Assume in addition that on August 31, 1986, P also purchases the stock of DT4 from DS in a qualified stock purchase. DT4 holds all of the stock of FT5.

(ii) Because a regular exclusion election cannot be made in an express election for FT, such an express election will cause deemed elections under section 338(f)(1) for DT4 and FT5 as well as for FT1, FT2, and FT3.

(iii) An express election cannot be made for DT4 under paragraph (c)(2)(iv) of this section because DT4 is not a qualifying domestic target affiliate within the meaning of paragraph (c)(2)(iv)(C) of this section. DT4 is not a qualifying domestic target affiliate within the meaning of paragraph (c)(2)(iv)(C) of this section because a regular exclusion election could not have been made in an express election for DT4 had DT4 been the original target, had FT been a target affiliate of DT4, and had the acquisition date of FT occurred during the consistency period of DT4. (Under those hypothetical circumstances, P's direct acquisition of FT from DS is an invalidation event under paragraph (c)(2)(iii)(B) of this section, since FT is a controlled foreign corporation during the relevant period.)

Example (8). (i) Assume the same facts as in Example (6), except that DS is FS and FT does not satisfy the 50 percent gross income test of paragraph (c)(5)(i) of this section for the 3-year period preceding 1986. FS is not a controlled foreign corporation. Assume in addition that on August 31, 1986, P also purchases the stock of DT4 from FS in a qualified stock purchase. DT4 holds all of the stock of FT5.

(ii) FT is an original foreign target within the meaning of paragraph (c)(2)(iv)(B) of this section. In addition, DT4 is a qualifying domestic target affiliate within the meaning of paragraph (c)(2)(iv)(C) of this section. DT4 is a qualifying domestic target affiliate because it would be subject to a deemed election under section 338(f)(1) if an express election were made for FT and because a regular exclusion election could have been made in an express election for DT4 had DT4 been the original target, had FT been a target affiliate of DT4, and had the acquisition date of FT occurred during the consistency period of DT4. (Under those hypothetical circumstances, P's direct acquisition of FT is not an invalidation event under paragraph (c)(2)(iii)(B) of this section, since FT is not a controlled foreign corporation during the relevant period.) Accordingly, the special rule of paragraph (c)(2)(iv) of this section applies and an express election may be made for DT4 rather than for FT, provided that a regular exclusion election is made in that express election. If such an express election is made, FT, FT1, FT2, FT3, and FT5 will be treated as excludible target affiliates subject to that regular exclusion election.

Example (9). (i) Assume the same facts as in Example (1), except that FT2 satisfies the 50 percent gross income test of paragraph (c)(5) of this section for the 3-year period preceding 1986 and therefore is treated as a domestic corporation for purposes of this paragraph (c). (1986 is the taxable year of FT2 in which its acquisition date would occur, absent a regular exclusion election, in the event of an express election for DT. See paragraph (c)(5)(ii) of this section.) (The exception of paragraph (c)(5)(iii) of this section is inapplicable because P did not directly acquire any of the stock of FT2.) None of the other foreign corporations satisfy the 50 percent gross income test.

(ii) A valid regular exclusion election cannot be made in an express election filed for DT, since an excludible foreign target affiliate, FT1, holds stock in a "domestic" corporation, FT2, that would be subject to a section 338 election only if the regular exclusion election did not apply. See paragraph (c)(2)(iii)(C) of this section.

Example (10). (i) Assume the same facts as in Example (1), except that both FT1 and FT2 satisfy the 50 percent gross income test of paragraph (c)(5) of this section and therefore are treated as domestic corporations for purposes of this paragraph (c). None of the other foreign corporations satisfy the 50 percent gross income test.

(ii) A regular exclusion election (applicable to FT3 only) may be made in the express election filed for DT, since both FT1 and FT2 are considered domestic corporations under paragraph (c)(5) of this section (and therefore are not excludible foreign target affiliates). Accordingly, there exists no excludible foreign target affiliate that holds stock in a domestic corporation.

Example (11). (i) Assume the same facts as in Example (2), except that FT5 holds all of the stock of FT6 and that FT6 satisfies the 50 percent gross income test of paragraph (c)(5) of this section for the 3-year period preceding 1986 (and therefore is treated as a domestic corporation for purposes of this paragraph (c)). None of the other foreign corporations satisfy the 50 percent gross income test.

(ii) Since an excludible foreign target affiliate, FT5, holds stock in a "domestic" corporation, FT6, that would be subject to a section 338 election only if the regular exclusion election did not apply, the acquisition of DT4 is an invalidation event and a valid regular exclusion election cannot be made in the express election filed for DT. See paragraph (c)(2)(iii)(C) of this section. (If a Form 8023 purporting to make a regular exclusion election already has been filed, then that regular exclusion election is retroactively invalidated by the acquisition of DT4 and the procedures described in paragraph (c)(2)(vii) of this section apply.)

Example (12). Assume the same facts as in Example (9), except that FT1 holds only 10 percent of FT2's only class of outstanding stock while a wholly-owned domestic subsidiary of DT holds the remaining 90 percent. A regular exclusion election (applicable to FT1 and FT3) may be made in the section 338 election filed for DT, since FT2, a "domestic" corporation, will be subject to a section 338 election even though the regular exclusion election is made. See paragraph (c)(2)(iii)(C) of this section.

Example (13). (i) Assume the same facts as in Example (8), except that FT2 satisfies the 50 percent gross income test of paragraph (c)(5) of this section for the 3-year period preceding 1986 and therefore is treated as a domestic corporation for purposes of this paragraph (c). None of the other foreign corporations satisfy the 50 percent gross income test.

(ii) An express election cannot be made for DT4 under the special rule of paragraph (c)(2)(iv) of this section, since a regular exclusion election could not have been made in an express election for DT4 had DT4 been the original target, had FT been a target affiliate of DT4, and had the acquisition date of FT occurred during the consistency period of DT4. Although P's direct acquisition of FT is not an invalidation event under those hypothetical circumstances, since FT is not a controlled foreign corporation for the relevant period, an invalidation event nonetheless occurs because FT1, an excludible foreign target affiliate, holds stock in a "domestic" corporation, FT2. See paragraph (c)(2)(iii)(C) of this section.

(iii) Because the invalidation event occurs before an express election for DT4 could be filed, DT4 is not a qualifying domestic target affiliate within the meaning of paragraph (c)(2)(iv)(C) of this section. Accordingly, the express election can be made only for FT, and a regular exclusion election cannot be made in that express election.

Example (14). Assume that P makes a regular exclusion election under the facts described in Example (2). Notwithstanding that, by reason of section 338(h)(3)(B), new DT and new DT4 are considered to have made qualified stock purchases of FT1 and FT5, respectively, a separate section 338 election cannot be made for either or both of those corporations. See paragraph (c)(2)(i) of this section.

Example (15). (i) Assume that P makes a regular exclusion election under the facts described in Example (1). Assume in addition that old DT's basis in FT1 stock immediately before old DT's deemed sale of assets is $20,000, that old DT realizes gain of $80,000 on the deemed sale of FT1 stock (at a deemed sale price of $100,000), and that old DT must include $55,000 in gross income as a dividend under section 1248(f)(1) as a result of that deemed sale. (That $55,000 does not include a $10,000 dividend under section 78.) Finally, assume that new DT's basis in FT1 absent this paragraph (c) would be $100,000.

(ii) The special stock basis rule of paragraph (c)(3)(i) of this section applies. Old DT is subject to section 1248(f)(1) (within the meaning of paragraph (c)(3)(iii) of this section) on its deemed sale of FT1 stock because (A) DT recognizes a section 1248(f) dividend on that deemed sale, (B) that dividend is less than the gain realized by DT in that deemed sale, and (C) earnings and profits that would have arisen had the regular exclusion election not been made would have increased the section 1248(f) dividend recognized by old DT. (Any earnings and profits that would have accrued to FT1, FT2, or FT3 had section 338 applied to those foreign corporations would have increased old DT's section 1248(f) dividend since each of those corporations is a controlled foreign corporation for the taxable year within which such earnings and profits would have been triggered. See paragraph (g) of this section.)

(iii) New DT's basis in FT1 stock is $75,000, the lesser of the regular basis amount of $100,000 or the special basis amount of $75,000, *i.e.*, $20,000 + $55,000. See paragraph (c)(3)(i) of this section. The $25,000 excess of the regular basis amount over the special basis amount is eliminated for income tax purposes except that, in allocating basis among the other assets of new DT, that $25,000 excess is treated as if it were an amount allocated to the FT1 stock. See paragraph (c)(3)(ii) of this section.

Example (16). (i) Assume the same facts as in Example (15), except that FT1 satisfies the 50 percent gross income test of paragraph (c)(5) of this section for the 3-year period preceding 1986 and therefore is treated as a domestic corporation for purposes of this paragraph (c). None of the other foreign corporations satisfy the 50 percent gross income test. Thus, DT and FT1 are subject to elections under section 338 while FT2 and FT3 are excludible foreign target affiliates subject to the regular exclusion election. Assume further the following: Old DT's section 1248(f)(1) dividend increases from $55,000 to $60,000 as a result of the deemed sale earnings and profits triggered by FT1's deemed sale of assets. Old FT1's basis in FT2 stock is $10,000. Absent paragraph (c)(3) of this section, new FT1's basis in FT2 stock would be $90,000. The earnings and profits of FT2 and FT3 that are attributable to the FT1 stock under section 1248(c)(2) are $15,000 and $20,000, respectively.

(ii) Under these circumstances, the special basis rule of paragraph (c)(3)(iv) of this section applies. Accordingly, DT's basis in FT1 stock is determined under paragraph (c)(3)(i) and (iv)(A) of this section even though FT1 is not an excludible foreign target affiliate. Thus, new DT's basis in FT1 is $80,000 (*i.e.*, $20,000 + $60,000), an amount less than the regular basis amount of $100,000. In addition, new FT1's basis in FT2 stock is the lesser of (A) the regular basis amount of $90,000 or (B) old FT1's $10,000 basis in the FT2 stock, increased by $35,000, *i.e.*, the excess of the section 1248(f) dividend actually recognized by DT, $60,000, over the amount that dividend would have been had FT1 not held the FT2 stock, $25,000 (i.e., $60,000 − ($15,000 + $20,000)). (Had FT1 not held the FT2 stock, the earnings and profits of both FT2 and FT3 would have been disregarded for purposes of calculating the amount of DT's section (f) dividend.)

Example (17). (i) Assume the same facts as in Example (16), except that FT2 also satisfies the 50 percent gross income test of paragraph (c)(5) of this section for the 3-year period preceding 1986 and therefore is treated as a domestic corporation for purposes of this paragraph (c). FT3 does not satisfy the 50 percent gross income test. Thus, DT, FT1, and FT2 are subject to election sunder section 338 while FT3 is an excludible foreign target affiliate subject to the regular exclusion election. Assume further that, as a result of FT2's deemed sale of assets, its earnings and profits that are attributable to the FT1 stock under section 1248(c)(2) increase by $2,000, *i.e.*, from $15,000 to $17,000. (FT3's attributable earnings and profits are the same as in Example (16).) Thus, old DT's section 1248(f)(1) dividend increases from $60,000 to $62,000. Finally, assume that old FT2's basis in FT3 stock is $5,000, and that, absent paragraph (c)(3) of this section, new FT2's basis in FT3 stock would be $30,000.

(ii) New DT's basis in fT1 stock is determined in the same manner as in Example (16). Thus, new DT's basis in FT1 is $82,000 (*i.e.*, $20,000 + $62,000), an amount less than the regular basis amount of $100,000.

(iii) New FT1's basis in FT2 stock is the lesser of (A) the regular basis amount of $90,000 or (B) old FT1's $10,000 basis in the FT2 stock, increased $37,000, *i.e.*, the excess of the section 1248(f) dividend actually recognized by DT, $62,000, over the amount that dividend would have been had FT1 not held the FT2 stock, $25,000 (*i.e.*, $62,000 − ($17,000 + $20,000)).

(iv) New FT2's basis in FT3 stock is the lesser of (A) the regular basis amount of $30,000 or (B) old FT2's $5,000 basis in the FT3 stock, increased by $20,000, *i.e.*, the excess of the section 1248(f) dividend actually recognized by DT ($62,000) over the amount that dividend would have been had FT2 not held the FT3 stock, $42,000 (*i.e.*, $62,000 − $20,000).

Example (18). (i) Assume the same facts as in Example (16), except that DT holds only 80 of the 100 outstanding shares of FT1's only class of stock and that on July 31, 1986, P purchases the remaining 20 shares of FT1 stock from DS.

(ii) FT1 cannot be treated as a domestic corporation since the exception of paragraph (c)(5)(iii) of this section applies, *i.e.*, 20 shares of FT1 stock were directly acquired by P (other than by reason of a deemed purchase under section 338(a)(2)), FT1 was a controlled foreign corporation for the relevant period, and FT1 holds the stock of a corporation, FT2, that would be an excludible foreign target affiliate if FT1 were treated as a domestic corporation. Thus, FT1 also is an excludible foreign target affiliate and P's direct acquisition of its stock is an invalidation event under paragraph (c)(2)(iii)(B) of this section. Accordingly, a valid regular exclusion election cannot be made in an express election for DT, and such an express election will cause deemed elections for FT1, FT2, and FT3.

Example (19). Assume that P makes a regular exclusion election under the facts described in Example (2). Assume in addition that on September 10, 1986, P purchases an asset from FT1 in an acquisition that, absent an express election for DT, would be considered a tainted asset acquisition (as defined in §1.338-4T(f)(6)(i)). Under paragraph (c)(4) of this section, P is required to take a carryover basis in the acquired asset as if the acquisition were subject to an affirmative action carryover election. The result is the same if the asset is acquired by DT, FT2, FT3, DT4, or FT5.

Example (20). Assume the same facts as in example (19), except that DS is FS, a foreign corporation, and that P purchases the asset from FS. The result is the same as in Example (19).

Example (21). Assume the same facts as in example (19), except that P purchases the asset from DT. Because paragraph (c)(4) of this section does not apply to asset acquisitions from targets that are subject to the express election, P's basis in the asset is determined under section 1012. The result is the same if P acquires the asset from DT4.

(d) *Special rules applicable to offset prohibition election*—(1) *Offset prohibition election inapplicable to certain transfers*—(i) *General rule*. The consequences of an offset prohibition election under §1.338-4T(f)(6)(iv) do not apply to a tainted asset acquisition if—

(A) The transferor is a foreign corporation, a corporation described in section 934(b), or a corporation to which an election under section 936 applies or

(B) The transfer is a transaction to which the pricing rules of section 994 (relating to DISC) or section 925 (relating to FSC) apply.

(ii) *Exception for certain foreign transferors*. Paragraph (d)(1)(i) of this section does not apply to an asset transfer by a foreign corporation if the gain recognized by that foreign corporation on the transfer is effectively connected with the conduct by that corporation of a trade or business within the United States.

(2) *Limit on crediting foreign tax against U.S. tax on offset prohibition gain*—(1) *Definitions*—(A) *Offset prohibition gain*. "Offset prohibition gain" is INA gain (or a remaining ICA gain amount) that is subject to an offset prohibition election under §1.338-4T(f)(6)(iv).

(B) *Offset prohibition foreign taxes*. "Offset prohibition foreign taxes" are foreign income taxes paid or accrued with respect to offset prohibition gain, as determined under the principles of §1.904-4(d)(2).

(C) *Otherwise applicable section 904 limitation*. The "otherwise applicable section 904 limitation" is the limitation described in section 904(d)(1) or 907(b)(prior to amendment by section 211(c)(1) of TEFRA) that would have applied to the offset prohibition gain but for this subparagraph (2).

(ii) *One-way special foreign tax credit limitation for offset prohibition foreign taxes*. A special foreign tax credit limitation applies to offset prohibition gain ("special limitation") in lieu of the otherwise applicable section 904 limitation. The special limitation is the limitation in section 904(a), computed by taking into account as foreign source income only offset prohibition gain from sources without the United States.

(iii) *Excess special limitation disregarded for purposes of section 904(c)*. For purposes of carryback or carryover of excess foreign taxes under section 904(c) to the taxable year in which there is offset prohibition gain, any excess special limitation for that taxable year is disregarded. "Excess special limitation" is the special limitation for a taxable year in excess of offset prohibition foreign taxes paid or accrued in that year.

(iv) *Special rule for creditability of offset prohibition foreign taxes in excess of the special limitation*. Offset prohibition foreign taxes in excess of the special limitation for the taxable year in which those taxes are paid or accrued nonetheless are creditable in that year if the otherwise applicable section 904 limitation (determined without regard to offset prohibition gain) exceeds the foreign taxes (not including offset prohibition foreign taxes) that are paid or accrued in that year and that are creditable under the otherwise applicable section 904 limitation in that year. Any remaining offset prohibition foreign taxes carry back or carry over to other taxable years as foreign taxes subject to the otherwise applicable section 904 limitation.

(v) *Coordination with restricted credit provisions of §1.338-4T(f)(6)(iv)*. *Answer 2* (ii) (B) and *Answer 3* (iv)(D) of §1.338-4T(f)(6)(iv) each impose a special limitation on the amount of a restricted credit (as defined therein) allowable as a credit against the tax liability of a corporation (or of an affiliated group filing consolidated returns) for the taxable year in which that corporation (or group) recognizes offset prohibition gain. (The foreign tax credit is not defined as a restricted credit.) The tax liability taken into account for purposes of determining the amount off certain restricted credits (*e.g.*, the investment credit under section 46) is required by statute to be reduced by the foreign tax credit allowed for the year. See section 38(c)(2). Solely for purposes of that reduction, the portion of the foreign tax credit allowed for the year that is creditable under the special limitation of paragraph (d)(2)(ii) of this section is disregarded.

(3) *Examples*. The provisions of paragraph (d)(2) of this section may be illustrated by the following examples.

Example (1). (i) On December 31, 1984, P acquires all of the stock of DT in a qualified stock purchase and timely files a protective carryover election pursuant to §1.338-4T(f)(6)(ii). P makes an offset prohibition election in the protective carryover election. P and DT file separate calendar year returns. On June 1, 1985, P purchases an asset from DT's foreign branch in a tainted asset acquisition subject to the offset prohibition election. See §1.338-4T(f)(6)(iv) *Answer 2* (ii). For 1985, DT recognizes a foreign source offset prohibition gain of $40,000 as a result of the asset transfer and also recognizes $60,000 of other foreign source income. It is assumed for the sake of simplicity that T has no deductions allocable to foreign source income. Absent paragraph (d)(2) of this section, all $100,000 of DT's foreign source income would be subject to the section 904 limitation for income described in section 904(d)(1)(E). A foreign income tax of $20,000 is specifically allocable to the $40,000 offset prohibition gain, and a foreign income tax of $24,000 is specifically allocable to the remaining $60,000 of foreign source income. DT's total taxable income for 1985 from all sources is $200,000, all of which is ordinary income. The United States income tax (before the foreign tax credit) is $81,875. (This tax reflects an equal division of the taxable income bracket amounts between P and DT.) DT has no excess foreign taxes available as a carryover to 1985 under section 904(c).

(ii) DT makes the following foreign tax credit calculations for 1985:

	(A) *Offset prohibition gain* *($40,000)*	*(B)* *Other income* *($60,000)*
(1) Foreign tax	$ 20,000	$ 24,000
(2) Limitation on credit	16,375[1]	24,563[2]
(3) Preliminary amount of foreign tax creditable (lower of line (1) or line (2))	16,375	24,000
(4) Excess foreign tax (line (1) − line (2))	3,625	N/A
(5) Preliminary excess limitation (line (2) − line (1))	N/A	563
(6) Foreign tax in line (4) creditable in current year (lower of line (4) and line (5))	N/A	563
(7) Final creditable foreign tax: (i) By income class (line (3) + line (6)) (ii) Total: $40,938	16,375	24,563
(8) Unused foreign tax available as carryover or carryback to other taxable years (line (4) − line (6))	N/A	3,062

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[1] $81,875 × $40,000/$200,000.

[2] $81,875 × $60,000/$200,000.

The remaining offset prohibition foreign tax, $3,062, will carryback or carryover to other taxable years as a foreign tax allocable to income described in section 904(d)(1)(E). Had the offset prohibition foreign tax been less than the separate limitation for offset prohibition gain, the excess limitation would have been disregarded for purposes of carrying unused foreign taxes to 1985.

Example (2). (i) Assume the same facts as in Example (1), except that a foreign income tax of $15,375 is specifically allocable to the $40,000 offset prohibition gain and a foreign income tax of $25,563 is specifically allocable to the remaining $60,000 of foreign source income.

(ii) DT makes the following foreign tax credit calculations for 1985:

		(A) *Offset prohibition gain* *($40,000)*	*(B)* *Other income* *($60,000)*
(1)	Foreign tax	$15,375	$25,563
(2)	Limitation on credit (same as Example (1))	16,375	24,563
(3)	Preliminary amount of foreign tax creditable (lower of line (1) or line (2))	15,375	24,563
(4)	Excess foreign tax (line (1) − line (2))	N/A	1,000
(5)	Preliminary excess limitation (line (2) − line (1))	N/A[1]	N/A
(6)	Foreign tax in line (4) creditable in current year (lower of line (4) and line (5))	N/A	N/A
(7)	Final creditable foreign tax:		
	(i) By income class (line (3) + line (6))	15,375	24,563
	(ii) Total: $39,938		
(8)	Unused foreign tax available as carryover or carryback to other taxable years (line (4) − line (6))	N/A	1,000

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[1] Note that although the special limitation actually exceeds offset prohibition foreign taxes by $1,000, that excess special limitation is disregarded for all purposes.

Example (3). (i) Assume the same facts as in Example (1), except that foreign taxes paid in 1985 ($44,000) cannot be specifically allocated between the offset prohibition gain and other foreign source income.

(ii) Under the principles of §1.904-4(d)(2)(ii), $17,600 of the total foreign income tax of $44,000 is allocated to offset prohibition gain (*i.e.*, $44,000 × $40,000/$100,000) and the remainder, $26,400, is allocated to the other foreign source income (*i.e.*, $44,000 × $60,000/$100,000). DT makes the following foreign tax credit calculations for 1985:

		(A) Offset prohibition gain ($40,000)	*(B)* Other income ($60,000)
(1)	Foreign tax	$17,600	$26,400
(2)	Limitation on credit (same as Example (1))	16,375	24,563
(3)	Preliminary amount of foreign tax creditable (lower of line (1) or line (2))	16,375	24,563
(4)	Excess foreign tax:		
	(i) By income class (line (1) − line (2))	1,225	1,837
	(ii) Total: $3,062		
(5)[1]	Final creditable foreign tax—		
	(i) By income class (line (3))	16,375	24,563
	(ii) Total: $40,938		
(6)	Unused foreign tax available as carryover or carryback to other taxable years (line (4)(ii))	N/A	3,062

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[1] Note that lines (5) and (6) of the table used in Example (1) are eliminated here. Those lines are unnecessary because there is no excess limitation.

Example (4). (i) Assume the same facts as in Example (1). Assume in addition that for 1985 DT's current year investment credit earned (as calculated before application of the limitation based on amount of tax under section 38(c), is $24,000. Assume also that DT's pre-credit tax liability would be $63,475 if the offset prohibition gain of $40,000 were disregarded.

(ii) DT's investment credit is a restricted credit. Accordingly, for purposes of determining the amount of that credit allowable as a credit against DT's tax in 1985, DT's pre-credit tax liability is calculated as if the offset prohibition gain were not income to DT. See §1.338-4T(f)(6)(iv) *Answer 2* (ii)(B). Because the tax liability taken into account for purposes of determining the amount of the investment credit is required under section 38(c) to be reduced by the foreign tax credit, the special rule of paragraph (d)(2)(v) of this section applies. Accordingly DT must make the following computations:

(1)	Investment credit earned in 1985	$24,000
(2)	Pre-credit U.S. tax liability (disregarding offset prohibition gain)	63,475
(3)	Foreign tax credit as adjusted under paragraph (d)(2)(v) of this section	24,563[1]
(4)	Net tax liability under section 38(c)(2) (line (2) minus line (3))	38,912
(5)	Investment credit allowable as credit against tax for 1985 (lesser of line (1) or line (4)[2])	24,000

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[1] Note that the portion of the foreign tax credit allowed for the year that is creditable under the special limitation of paragraph (d)(2)(ii) of this section, $16,375 (line (7)(i), Col. (A) of table in Example (1)) is disregarded for purposes of the reduction required by section 38(c)(2).

[2] If the investment credit earned in 1985 exceeded $25,000, the maximum amount of that excess that would be allowable as an investment credit for 1985 would be $11,825, *i.e.*, 85 percent of the net tax liability in excess of $25,000. See section 38(c)(1)(B).

(e) *Certain transactions subject to an exception to section 338(e)(1) under the authority of section 338(e)(2)(D)*—(1) *Basis step-up attributable to gain recognized under section 367*. The acquisition of property is subject to an exception to section 338(e)(2)(D) if, solely by reason of the transferor's recognition of gain under section 367(a), the transferee's basis in the transferred asset exceeds the transferor's basis in that asset immediately before the transfer.

(2) *Acquisition of foreign currency*—(i) *General rule*. The acquisition of foreign currency is subject to an exception to section 338(e)(1) under the authority of section 338(e)(2)(D) if the acquisition occurs in the ordinary course of the transferor's trade or business (as determined under principles similar to those in §1.338-4T(f)(3)). Solely for purposes of this subparagraph (2), a transferor is considered to act in the ordinary course of its trade or business when it—

(A) Pays interest or principal on an obligation denominated in foreign currency,

(B) Makes a loan denominated in foreign currency, or

(C) Pays a dividend denominated in foreign currency.

(ii) *No inference regarding character of gain or loss*. No inference should be drawn regarding the character of exchange gain or loss realized on transactions described in this paragraph (e)(2).

(f) *Effect of section 338 on foreign target*. If, for its taxable year that includes its acquisition date and for any other relevant taxable year, a foreign target for which a section 338 election is made has no items of income for which it is taxable under chapter 1 of the Code (including an item of income resulting from the section 338 election), then, in general, the section 338 election results in potential United States tax consequences only for domestic shareholders of that foreign target. Thus, for example, the adjustment to the foreign target's earnings and profits that results from the section 338 election may affect the amount of a distribution that is treated as a dividend for the domestic shareholders. Similarly, if the foreign target is a controlled foreign corporation, section 338 may affect the amount included in the gross income of certain domestic shareholders under section 951 or 1248.

(g) *Operation of section 1248 if section 338 election made*—(1) *Scope*. This paragraph (g) applies section 1248 to the shareholders of a target that is controlled foreign corporation and that is subject to a section 338 election ("CFCT"). The principles of this paragraph (g) also apply if a domestic corporation described in section 1248(e) is involved.

(2) *General rules*—(i) *Transfer of CFCT stock on or before acquisition date*. If a person transfers a block of CFCT stock on or before CFCT's acquisition date but during CFCT's 12-month acquisition period, then, for purposes of determining the amount (if any) treated as a dividend to the transferor under section 1248, old CFCT's earnings and profits attributable to the block is the enhanced earnings and profits amount as determined under paragraph (g)(3) or (4) of this section (as the case may be).

(ii) *Effect of gain recognition election*. If P makes a gain recognition election under §1.338-4T(j)(2) for the nonrecently purchased CFCT stock, then paragraph (g)(2)(i) of this section shall apply to the gain recognized by P under section 338(b)(3)(A) as if the nonrecently purchased CFCT stock were actually sold at the close of CFCT's acquisition date.

(iii) *Carryover CFCT stock*. If on the close of CFCT's acquisition date a non-P group member holds CFCT stock (or if a P group member holds nonrecently purchased CFCT stock that is not subject to a gain recognition election under §1.338-4T(j)(2)) ("carryover CFCT stock"), then, solely for purposes of that carryover CFCT stock, old CFCT's earnings and profits (adjusted to reflect deemed sale of assets under section 338) and the foreign taxes attributable to those earnings and profits shall carry over (in their annual layers) to new CFCT, subject to the special rules and limitations prescribed in paragraph (g)(6) of this section.

(iv) *Special rule for determining status as controlled foreign corporation*. If a foreign target ceases to be a controlled foreign corporation solely by reason of one or more purchases of its stock that constitutes a qualified stock purchase, then all of its stock that is included in that qualified stock purchase is deemed to have been acquired by the purchasing corporation on that foreign target's acquisition date for purposes of determining under this paragraph (g) the period during which that foreign target (and all of its section 1248(c)(2) subsidiaries) are controlled foreign corporations.

(v) *Section 1248(c)(2) subsidiary*. For purposes of this paragraph (g), a "section 1248(c)(2) subsidiary" with respect to a foreign target is any corporation whose earnings and profits may be deemed under section 1248(c)(2) to be included with the earnings and profits of that foreign target.

(vi) *Special deemed stock sale rule*. For all purposes of the Code, a transferor of stock in a controlled foreign corporation is deemed to sell the stock directly to P or a P group member on the transferee's acquisition date if (A) a member of the S group transfers the stock to a domestic member of the S group that becomes a target for which a section 338 election applies, (B) the transfer takes place on or before the transferee's acquisition date and during the consistency period of the original target or an affected target, and (C) the controlled foreign corporation becomes an affected target. The transferor shall not be deemed to sell stock under this subdivision (vi) if it is demonstrated that the transfer was not in anticipation of, or pursuant to a plan to make, a direct or indirect transfer of the transferee's stock to P or a P group member. Thus, for example, there will not be a deemed sale of the stock of a controlled foreign corporation to P or a P group member if, prior to the time the controlled foreign corporation becomes an affected target, section 351(a) applies to the transfer by an S group member of the stock of the controlled foreign corporation to a domestic member of the S group. The Internal Revenue Service may treat a transfer to a foreign member as subject to this subdivision (vi) if such treatment is appropriate to carry out the purposes of this subdivision (vi).

(3) *Enhanced earnings and profits amount if stock transferred on CFCT's acquisition date.* For a block of CFCT stock actually or deemed transferred on CFCT's acquisition date, the enhanced earnings and profit amount is the earnings and profits of CFCT (and any section 1248(c)(2) subsidiary) attributable to the block under the applicable section 1248 regulations. For purposes of this subparagraph (3), earnings and profits of CFCT (and of each section 1248(c)(2) subsidiary) shall be deemed to include the gains and other income amounts that each would have recognized in the deemed sale of assets under section 338(a)(1) had each been a domestic corporation.

(4) *Enhanced earnings and parts amount if stock transferred before CFCT's acquisition date*—(i) *General rule.* For a block of CFCT stock actually or deemed transferred before CFCT's acquisition date, the enhanced earnings and profits amount is the sum of the following amounts:

(A) Old CFCT's earnings and profits attributable to the block under the applicable section 1248 regulations, applied however by not including in CFCT's earnings and profits (accumulated for the taxable year of CFCT in which the stock transfer occurs) the recapture earnings and profits for that year, and

(B) CFCT's recapture earnings and profits for each affected taxable year of CFCT that would have been attributable to the block under the applicable section 1248 regulations had that block been transferred on CFCT's acquisition date.

(ii) *Affected taxable year of CFCT.* An affected taxable year of CFCT is the taxable year of CFCT in which the CFCT stock is transferred and each subsequent taxable year of CFCT up to and including its taxable year that includes CFCT's acquisition date.

(iii) *CFCT's recapture earnings and profits.* CFCT's recapture earnings and profits for an affected taxable year are an amount (not less than zero) equal to (A) CFCT's earnings and profits accumulated for that taxable year, minus (B) such earnings and profits as redetermined by disregarding recapture amounts for that taxable year. The recapture earnings and profits for a taxable year may not, however, exceed the earnings and profits of CFCT accumulated for that taxable year.

(iv) *Recapture amount.* A "recapture amount" for an affected taxable year is—

(A) The amount of gain realized as a result of an actual sale or exchange of an asset during that year, to the extent that such amount would have been recognized by CFCT in the deemed sale of assets under section 338(a)(1) had CFCT been a domestic corporation that held that asset on its acquisition date and had the deemed sale price of that asset been equal to the actual amount realized on the sale or exchange of that asset, and

(B) For the affected taxable year in which the deemed sale of assets under section 338(a)(1) occurs, the gains and other income amounts that would have been recognized by CFCT in the deemed sale of assets had CFCT been a domestic corporation.

(v) *Exception to enhancement rule of paragraph (g)(4)(i) for transitional period stock transfer.* Paragraph (g)(4)(i) of this section does not apply to a stock transfer occurring on or before February 12, 1986 or after that date but pursuant to a contract of sale that is binding on both the acquiring P group member and the seller as of that date. Nevertheless, if such a transfer occurs during old CFCT's final taxable year, then the transferor's ratable share of old CFCT's earnings and profits accumulated for that year under the applicable section 1248 regulations will reflect the earnings and profits resulting from the deemed sale of assets under section 338(a)(1) (pro-rated on a daily basis for the period during which the transferor held the CFCT stock).

(vi) *Section 1248(c)(2) subsidiary with same taxable year as CFCT.* For a block of CFCT stock with respect to which there are one or more section 1248(c)(2) subsidiaries, all of which have the same taxable year as CFCT, the provisions of paragraph (g)(4)(i)(iv) of this section shall apply in the following manner:

(A) *Recapture amounts for subsidiaries.* First, for each affected taxable year, *(1)* determine separately the recapture amounts of CFCT and of each section 1248(c)(2) subsidiary, *(2)* under the applicable section 1248 regulations attribute to the block the amount for CFCT, *(3)* under the principles of section 1248(c)(2) attribute to block the amounts for each such subsidiary, and *(4)* determine for the block the sum of the amount attributed from CFCT and the amounts attributed from the subsidiaries.

(B) *Earnings and profits of subsidiaries.* Second, the earnings and profits accumulated for each affected taxable year of CFCT and of each section 1248(c)(2) subsidiary shall be determined and, under the applicable principles, attributed for that year to the block.

(C) *Recapture earnings and profits for block.* Third, compute the recapture earnings and profits for each affected taxable year for the block as an amount (not less than zero) equal to *(1)* the sum of earnings and profits accumulated for that year of CFCT attributed to the block and of each section 1248(c)(2) subsidiary attributed under (B) of this subdivision (vi) to the block, minus *(2)* such sum as redetermined by disregarding recapture amounts for that year of CFCT and its section 1248(c)(2) subsidiaries. Recapture earnings and profits for a taxable year for the block may not, however, exceed the amount in *(1)* of this subdivision (C).

(D) *Application of general rule*. Fourth, apply the general rule in paragraph (g)(4)(i) of this section by using amounts attributed to the block under paragraph (g)(4)(vi)(B) and (C) of this section instead of the amounts determined solely for CFCT.

(vii) *Section 1248(c)(2) subsidiary with taxable year different from CFCT's*. The principles of paragraph (g)(4)(vi) of this section shall apply if one or more section 1248(c)(2) subsidiaries have a different taxable year than CFCT.

(5) *Section 338(c)(1) inapplicable*. The enhanced earnings and profits amounts under paragraph (g)(3) and (4) of this section are determined without regard to section 338(c)(1) (relating to surrogate tax). For an exception applicable to certain carryover CFCT stock, see paragraph (g)(6)(iv) of this section.

(6) *Carryover of old CFCT earnings and profits for purposes of carryover CFCT stock*—(i) *General rule*. The earnings and profits (and attributable foreign taxes) attributable to old CFCT stock carry over to new CFCT stock under paragraph (g)(2)(iii) of this section solely for purposes of (A) characterizing an actual distribution with respect to a share of carryover CFCT stock as a dividend, (B) characterizing gain on a post-acquisition date transfer of a share of carryover CFCT stock as a dividend under section 1248, and (C) determining the foreign taxes deemed paid under section 902 with respect to the amount thereby treated as a dividend.

(ii) *Cap on carryover of earnings and profits*. The earnings and profits of old CFCT are taken into account with respect to a share of carryover CFCT stock only to the extent of the section 1248 amount for that share.

(iii) *Section 1248 amount for stock other than section 338(c)(1) stock*. The section 1248 amount for a share of carryover CFCT stock other than section 338(c)(1) stock is the amount (if any) of the gain that, under the enhanced earnings and profits provisions of paragraph (g)(3) of this section, would have been included in the shareholder's gross income as a dividend under section 1248 had the shareholder transferred that share to P on CFCT's acquisition date for a consideration equal to the fair market value of that share on that date (or, with respect to nonrecently purchased CFCT stock treated as carryover CFCT stock, had a gain recognition election under section 338(b)(3)(A) applied to that share).

(iv) *Section 1248 amount for section 338(c)(1) stock*. The section 1248 amount for a share of section 338(c)(1) stock is determined in the same manner as for other carryover CFCT stock, except that the earnings and profits attributable to a share of section 338(c)(1) stock for each taxable year of old CFCT under the principles of paragraph (g)(3) of this section (*i.e.*, without regard to section 338(c)(1)) are increased or deceased by the section 338(c)(1) amount for that share for that year.

(v) *Section 338(c)(1) stock*. For purposes of this paragraph (g)(6), "section 338(c)(1) stock" is carryover CFCT stock (other than nonrecently purchased CFCT stock) that is neither—

(A) Purchased by a P group member at any time during the one-year period beginning on CFCT's acquisition date nor

(B) Redeemed by CFCT in a transaction described in section 338(h)(7)(B) during that 1-year period.

(vi) *Section 338(c)(1) amount*. The "section 338(c)(1) amount" for a share of section 338(c)(1) stock is a positive (or negative) amount equal to the net section 338(c)(1) gain or loss of old CFCT for its taxable year, divided by the total number of shares of section 338(c)(1) stock. For purposes of this subparagraph (6), the net section 338(c)(1) amount for a share takes into account the net section 338(c)(1) gain or loss for each section 1248(c)(2) subsidiary that is attributed under the principles of section 1248(c)(2) to the share. (If convenient, the section 338(c)(1) amount may be computed with respect to a block of stock.) Section 338(c)(1) gains or losses are gains or losses that, had CFCT (or the section 1248(c)(2) subsidiary) been a domestic corporation, would have been recognized by it under section 388(c)(1)—

(A) As a result of its deemed sale of assets under section 338(a)(1) or

(B) As a result of its actual sale of assets under the circumstances described in section 338(h)(12) and §1.338-4T(k)(1) *Answer 3* (ii).

(vii) *Old CFCT earnings and profits unaffected by post-acquisition date deficits*. Notwithstanding that new CFCT incurs deficits in earnings and profits, a post-acquisition date distribution with respect to a share of carryover CFCT stock (or gain recognized in a post-acquisition date transfer of a share of carryover CFCT stock when that transfer is governed by section 1248) shall be treated as a dividend at least to the extent of the section 1248 amount for that share, reduced by prior post-acquisition date distributions with respect to that share out of the earnings and profits of old CFCT. Thus, for example, the first distribution by new CFCT with respect to a share of carryover CFCT stock is treated as a dividend by the distributee to the extent of the section 1248 amount for that share, notwithstanding that new CFCT's losses exceed old CFCT's earnings and profits at the close of the acquisition date. A distribution considered made out of old CFCT's earnings and profits pursuant to this subparagraph (6) has no effect on the earnings and profits of new CFCT.

(viii) *Character of CFCT stock as carryover CFCT stock eliminated upon disposition*. A share of CFCT stock is not considered carryover CFCT stock after it is disposed of in a transaction described in section 1248(a)(1) or (f)(1)(B) by the person holding such stock on the close of CFCT's acquisition date, provided that all gain realized on the transfer is recognized at the time of the transfer, or that, if less than all of the realized gain is recognized, the recognized amount equals or exceeds the remaining section 1248 amount for that share.

(7) *Application of principles of this paragraph to section 1246*. The principles of this paragraph (g) also apply to shareholders of a foreign target that are subject to section 1246.

(8) *Examples*. The provisions of this paragraph (g) may be illustrated by the following examples.

Example (1). (i) CFCT is a calendar year foreign corporation. DA, a United States person, has owned 90 of the 100 shares of CFCT's only class of outstanding stock since CFCT was organized on March 13, 1977. P has held the remaining 10 shares of CFCT since CFCT was organized. (Those 10 shares constitute nonrecently purchased CFCT stock in P's hands within the meaning of section 338(b)(6)(B).) On November 1, 1986, P purchases all 90 shares of CFCT stock held by DA for $90,000 in cash and makes an express election for CFCT. Thus, for United States tax purposes, CFCT has a short taxable year ending at the close of November 1, 1986. Assume

DA recognizes gain of $81,000 on the sale of the CFCT stock. All 90 shares of CFCT stock constitute a block of stock in DA's hands within the meaning of §1.1248-2(b) and the conditions of §1.1248-2(c) are satisfied with respect to that block of stock. CFCT has no earnings and profits accumulated (or deficit) for any taxable year prior to 1986. Assume that, if CFCT were a domestic corporation, it would recognize gain of $20,000 on November 1, 1986, by reason of its deemed sale of assets under section 338(a)(1). CFCT's earnings and profits accumulated for its short 1986 taxable year ending on November 1, 1986, without taking into account that $20,000 of gain, total $50,000. P also makes a gain recognition election for CFCT under section 338(b)(3)(A) and §1.338-4T(j)(2).

(ii) DA's sale of CFCT stock to P on November 1, 1986, is a transfer to which section 1248 and paragraph (g)(2)(i) and (3) of this section apply. For purpose of applying section 1248(a) to DA, the earnings and profits accumulated by CFCT for its short taxable year ending on November 1, 1986, are $70,000, *i.e.*, the earnings and profits accumulated for that taxable year as determined under §1.1248-2(b), taking into account the gain of $20,000 that CFCT would have recognized in the deemed sale of assets under section 338(a)(1) had CFCT been a domestic corporation ($50,000 + $20,000). See paragraph (g)(3) of this section. Pursuant to §1.1248-2(e), $63,000 of the $70,000 of earnings and profits accumulated for 1986 are attributable to the block of CFCT stock sold by DA on November 1, 1986 (*i.e.*, $70,000 × 90/100), since that block (A) was held for the entire taxable year ending on November 1, 1986, and (B) includes 90 of the 100 shares of outstanding CFCT stock. Accordingly, $63,000 of DA's gain of $81,000 on the sale of CFCT stock is included under section 1248(a) in DA's gross income as a dividend.

(iii) Assume that P recognizes a gain of $9,000 with respect to the 10 shares of nonrecently purchased CFCT stock by reason of the gain recognition election, which causes a hypothetical acquisition date sale of nonrecently purchased stock. Under paragraph (g)(2)(ii) and (3) of this section, that hypothetical sale is treated as a transfer of CFCT stock by a U.S. person to P on CFCT's acquisition date in a transfer to which section 1248 applies. Thus, under §1.1248-2(e), $7,000 of the $70,000 of earnings and profits accumulated for 1986 are attributable to the block of 10 shares of CFCT stock hypothetically sold by P at the close of November 1, 1986 (*i.e.*, $70,000 × 10/100), since that block (A) was held for the entire taxable year ending on November 1, 1986, and (B) includes 10 of the 100 shares of outstanding CFCT stock. Accordingly, $7,000 of P's gain of $9,000 on the hypothetical sale of 10 shares of CFCT stock is included under section 1248(a) in P's gross income as a dividend.

Example (2) (i) Assume the same facts as in Example (1), except that P does not make a gain recognition election.

(ii) The nonrecently purchased CFCT stock held by P (*i.e.*, the 10 shares owned by P since CFCT was organized) is carryover CFCT stock (and not section 338(c)(1) stock). See paragraph (g)(2)(iii) of this section. Accordingly, the earnings and profits (and attributable foreign taxes) of old CFCT carry over to new CFCT solely for purposes of that block of 10 shares. However, the amount of old CFCT's earnings and profits taken into account with respect to that block in the event of a distribution by new CFCT with respect that block (or in the event of P's sale of that block in a transaction governed by section 1248) may not exceed the section 1248 amount for that block. The section 1248 amount for that block is the amount of the section 1248 dividend P would have a recognized with respect to that block had it made a gain recognition election under section 338(b)(3)(A). Under the facts of Example (1)(iii), P would have recognized a gain of $9,000 with respect to that block, and $7,000 of that amount would have been a section 1248 dividend, *i.e.*, $70,000 × 10/100. Accordingly, the section 1248 amount for the block of 10 shares of nonrecently purchased CFCT stock is $7,000.

Example (3). (i) CFCT is a calendar year foreign corporation. DA, a United States person, has owned all 100 shares of CFCT's only class of outstanding stock since CFCT was organized on March 13, 1977. On August 7, 1986, P purchases 40 of the 100 shares of CFCT stock held by DA for cash. On May 26, 1987, P purchases the remaining 60 shares of CFCT stock from DA for cash and makes an express election for CFCT. Thus, for United States tax purposes, CFCT has a short taxable year ending on May 26, 1987. Assume that gain recognized by DA is $80,000 on the August 7, 1986 sale and $130,000 on the May 26, 1987, sale. The 40 shares and 60 shares of CFCT stock sold by DA constitute two blocks of stock in DA's hands within the meaning of §1.1248-2(b). The conditions of §1.1248-2(c) are satisfied with respect to each block. CFCT has no earnings and profits accumulated (or deficit) for any taxable year prior to 1986. In 1986, CFCT recognizes gain of $30,000 on the sale of used machinery. All of that gain would have been recognized by CFCT in the deemed sale of assets under section 338 as depreciation recapture under section 1245 had CFCT been a domestic corporation that held the machinery on the acquisition date. CFCT's earnings and profits accumulated for 1986 are $120,000 if that $30,000 gain is taken into account. (Accordingly, CFCT's earnings and profits accumulated for 1986, as determined without that $30,000, are $90,000.) If CFCT were a domestic corporation, it would recognize a gain of $20,000 on May 26, 1987, by reason of its deemed sale of assets under section 338(a)(1). CFCT's earnings and profits accumulated for its short 1987 taxable year ending on May 26, 1987, are $80,000 if that $20,000 gain is taken into account. (Accordingly, CFCT's earnings and profits accumulated for 1987, as determined without that $20,000, are $60,000.)

(ii) DA's sales of the blocks of CFCT stock to P are transfers to which section 1248 and paragraph (g)(2)(i), (3), and (4) of this section apply. Under paragraph (g)(4)(ii) of this section, CFCT's 1986 and 1987 taxable years are affected taxable years of CFCT for which CFCT's recapture earnings and profits must be determined. For 1986, CFCT has a recapture amount of $30,000, *i.e.*, the $30,000 of gain recognized by CFCT on the sale of machinery in 1986. See paragraph (g)(4)(iv)(A) of this section. Accordingly, under paragraph (g)(4)(iii) of this section, CFCT's recapture earning profits for 1986 are $30,000, *i.e.*, $120,000 − $90,000. For 1987, CFCT has a recapture amount of $20,000, *i.e.*, the $20,000 of gain hypothetically recognized by CFCT in its deemed sale of assets under section 338(a)(1)) and, accordingly, recapture earnings and profits of $20,000, *i.e.*, $80,000 − $60,000.

(iii) The enhanced earnings and profits of CFCT attributable to the block of 40 shares of CFCT stock sold on August 7, 1986 are determined under paragraph (g)(4) of this section and the applicable section 1248 regulations as follows:

Earnings and profits attributable to block for 1986 (determined without recapture earnings and profits), *i.e.*, $90,000 × 219/365 × 40/100	$21,600
Recapture earnings and profits attributable to block for 1986 *i.e.*, $30,000 × 40/100	12,000
Recapture earnings and profits attributable to block for 1987 under applicable section 1248 regulations, *i.e.*, $20,000 × 40/100	8,000
Total earnings and profits attributable to block	$41,600

Accordingly, $51,600 of DA's $80,000 gain on the sale of the 40 shares of CFCT stock is included under section 1248(a) in DA's gross income as a dividend.

(iv) The enhanced earnings and profits of CFCT attributable to block of 60 shares of CFCT stock sold on May 26, 1987, are determined as follows under paragraph (g)(3) of this section and the applicable section 1248 regulations:

Earnings and profits attributable to block for 1986, *i.e.*, $120,000 × 60/100	$ 72,000
Earnings and profits attributable to block for 1987, *i.e*, $80,000 × 60/100	48,000
Total earnings and profits attributable to block	$120,000

Accordingly, $120,000 of DA's $130,000 gain on the sale of 60 shares of CFCT stock on May 26, 1987, is included in DA's gross income as a dividend.

Example (4). (i) Assume the same facts as in Example (1), except that the 10 shares of CFCT stock not purchased by P from DA on November 1, 1986, are held by DB, a U.S. person, rather than by P. DB has held those shares, at an aggregate basis of $1,000 since CFCT was organized. New CFCT makes no actual distributions to DB. On December 15, 1987, P purchase those 10 shares of CFCT stock from DB for $12,000 in cash, and DB recognizes a gain of $11,000. Assume that the fair market value of those 10 shares on November 1, 1986, is $10,000. Assume in addition that, had CFCT been a domestic corporation, it would have recognized an additional $1,000 of gain in its deemed sale of assets under section 338(a)(1) on November 1, 1986, by reason of section 338(c)(1), for a total deemed sale gain of $21,000. Finally, assume that new CFCT incurs a $100,000 net operating loss for its short taxable year ending on December 31, 1986, and a $50,000 net operating loss for 1987.

(ii) The tax consequences to DA are the same as in Example (1), since deemed sale gain under section 338(c)(1) is disregarded for purposes of determining the earnings and profits attributable to CFCT stock sold during the 12-month acquisition period ending on CFCT's acquisition date. See paragraph (g)(5) of this section.

(iii) The CFCT stock held by DB, a non-P group member, on the close of CFCT's acquisition date is carryover CFCT stock. See paragraph (g)(2)(iii) and (6) of this section. Accordingly, the earnings and profits (and foreign taxes attributable to such earnings and profits) carryover to new CFCT solely for purposes of the CFCT stock held by DB. (Under these facts, DB holds all of the carryover CFCT stock.) In addition, DB's sale of the CFCT stock to P on December 15, 1987, is a transfer to which section 1248 applies. DB's shares of CFCT stock constitute a block of stock in DB's hands within the meaning of §1.1248-2(b) and the conditions of §1.1248-2(c) are satisfied with respect to that block.

(iv) Because of the deficits incurred by new CFCT, DB's gain of $11,000 on the sale of its CFCT stock to P on December 15, 1987, is characterized as a section 1248 dividend only to the extent of the section 1248 amount. See paragraph (g)(6)(vii) of this section. Because the 10 shares held by DB constitute section 338(c)(1) stock (as defined in paragraph (g)(6)(v) of this section), the section 1248 amount is determined under paragraph (g)(6)(iv) of this section. Since each of the 10 shares has the same basis and holding period in DB's hands, it is convenient to do the necessary calculations for the block of 10 shares rather than for each share.

(v) The first step in determining the section 1248 amount is to calculate the gain DB would have recognized had it sold its CFCT stock to P on CFCT's acquisition date for a consideration equal to the fair market value of the stock on that day ("hypothetical stock sale gain"). The fair market value of the 10 shares on that date is assumed to be $10,000. Thus, DB's hypothetical stock sale gain is $9,000, *i.e.*, $10,000 − $1,000.

(vi) The second step in determining the section 1248 amount is to calculate the portion of the hypothetical stock sale gain that would have been a section 1248 dividend. This calculation also involves two steps. First, the earnings and profits attributable to the block for each relevant taxable year of old CFCT must be determined under paragraph (g)(3) of this section. The only relevant year under these facts is the short taxable year ending on November 1, 1986. The earnings and profits attributable to the block for that short year under such paragraph (g)(3) are $7,000, *i.e.*, $70,000 × 10/100. Note that the earnings and profits taken into account under such paragraph (g)(3) do not reflect the $1,000 gain under section 338(c)(1). The second step, in calculating the portion of the hypothetical stock sale gain that would have been a section 1248 dividend, is to increase (or decrease) that $7,000 by the section 338(c)(1) amount attributable to the block. Under these facts, there is a single section 338(c)(1) gain of $1,000. Because the block of stock at issue constitutes the entire amount of section 338(c)(1) stock, the entire $1,000 is the section 338(c)(1) amount attributable to the block. The portion of the hypothetical stock sale gain that would have been a section 1248 dividend therefore is $8,000, *i.e.*, the lesser of the attributable earnings and profits of $8,000 (*i.e.*, $7,000 + $1,000) or the hypothetical stock sale gain of $9,000. Thus, the section 1248 amount for the block of stock sold by DB on December 15, 1987, is $8,000. Accordingly $8,000 of DB's $11,000 gain on the actual December 15, 1987, stock sale is a section 1248 dividend.

(vii) If DB were a corporation it would be eligible for an indirect foreign tax credit on the section 1248 dividend it receives, since foreign taxes attributable to old CFCT's earnings and profits also carryover to new CFCT for purposes of the carryover CFCT stock. (Such deemed paid taxes would be treated as a dividend under section 78.)

Example (5). On December 31, 1986, P purchases from DS all of the stock of DT in a qualified stock purchase. For many years, DT has held as one block all of the stock of CECT1 and CFCT1 has held all of the stock of CFCT2. All corporations use the calendar year as the taxable year and have no earnings and profits (or deficit) accumulated for any taxable year prior to 1986. P makes an express election for DT. A regular exclusion election under paragraph (c)(2) of this section is not made, so that CFCT1 and CFCT2 are subject to deemed elections under section 338(f)(1) as a result of the express election for DT. Pursuant to §1.338-4T(c)(3), the acquisition date of DT and of each of its two subsidiaries is December 31, 1986. For purposes of calculating the amount of the section 1248(f) dividend recognized by DT as a result of its deemed sale of the block of CFCT1 stock, the enhanced earnings and profits attributable to the block are calculated under paragraph (g)(3) of this section in the table below, based upon the facts assumed:

		(A) *CFCT1*	*(B)* *CFCT2*
1.	Earnings and profits accumulated for 1986 under §1.1248-2 attributable to the block	$100	($80)
2.	Deemed sale gain that would have been recognized if it were a domestic corporation	0	$15
3.	Sum of lines 1 and 2	100	(65)
4.	Enhanced earnings and profits attributable to the block (sum of line 3(A) and (B))	35	

Example (6). Assume the same facts as in *Example (5)* except that CFCT1 holds only 80 percent of the single class of outstanding stock of CFCT2. For purposes of calculating the amount of the section 1248(f) dividend recognized by DT as a result of its deemed sale of the block of CFCT1 stock, the enhanced earnings and profits attributable to the block are calculated under paragraph (g)(3) of this section in the table below:

		(A) *CFCT1*	*(B)* *CFCT2*
1.	Line 3 *Example (5)*	$100	($65)
2.	Multiply line 1 (B) by 80/100		(52)
3.	Enhanced earnings and profits attributable to the block (sum of lines 1(A) and 2(B)	48	

(h) *Treatment of gain in deemed sale of assets as income effectively connected with the conduct of a trade or business within the United States and as from sources within the United States*—(1) *Foreign target.* If, during the measurement period, more than 50 percent of the gross income derived by old FT from an item of property is effectively connected with the conduct of a trade or business within the United States, then the gain that old FT would recognize with respect to that item of property in the deemed sale of assets under section 338(a)(1) if it were a domestic target is treated—

(i) as income that is effectively connected with the conduct of a trade or business within the United States and

(ii) as income from sources within the United States.

(2) *Domestic target.* If, during the measurement period, more than 50 percent of the gross income derived by old DT from an item of property is treated as income from sources within the United States, then the gain that old DT recognizes with respect to that item of property in the deemed sale of assets under section 338(a)(1) is treated as income from sources within the United States.

(3) *Measurement period.* The "measurement period" is the 3-year period ending with the close of the taxable year that precedes old target's final taxable year (or so much of that 3-year period as that target held the particular item of property).

(4) *No inference regarding transactions not described.* No inference should be drawn regarding either the

source of or the United States tax with respect to gain arising in the deemed sale of property not described in paragraph (h)(1) or (2) of this section.

(i) Reserved

(j) *Transitional rules for corporations and stock described in section 338(h)(6)(B)*—(1) *Transitional elective exclusion from target affiliate status.* If P files an express election for any original target, then, solely for purposes of the stock consistency rule of section 338(f)(1), P also may elect (in the manner prescribed in paragraph (j)(8) of this section) to exclude some or all of the transitional target affiliates from the status of target affiliate ("transitional exclusion election"). If a transitional exclusion election is not made, then none of the transitional target affiliates may be excluded from the status of a target affiliate. A section 338 election cannot be made for any transitional target affiliate that is subject to a transitional exclusion election.

(2) *Transitional target affiliate*—(i) *General rule.* A "transitional target affiliate" is any corporation described in section 338(h)(6)(B)(i) that is acquired on or before March 15, 1986, and that, absent section 338(h)(6)(B), would be subject to a deemed election under section 338(f)(1) by reason of the express election for the original target. (Under the second condition of paragraph (c)(2)(ii) of this section, status as a transitional target affiliate precludes status as an excludible foreign target affiliate.)

(ii) *Acquired on or before March 15, 1986.* A corporation is considered acquired on or before March 15, 1986, if its acquisition date (or hypothetical acquisition date) occurs on or before March 15, 1986, or after that date but pursuant to a contract of sale that is binding on both the acquiring P group member and the seller as of February 19, 1986. A corporation that is not considered acquired on or before March 15, 1986, is considered acquired after that date.

(iii) *Hypothetical acquisition date of transitional target affiliate.* If the acquisition date of a transitional target affiliate actually would occur only if the transitional exclusion election were not made (*i.e.*, by reason of the operation of section 338(h)(3)(B) and (f)(1)), then that hypothetical acquisitioned ate is treated as the acquisition date for purposes of applying this subparagraph (2).

(3) *Special rules for certain original targets described in section 338(h)(6)(B)(i)*—(i) *General rule.* If the original target is a transitional excludible original target, then the following consequences apply:

(A) An express election may be made for the transitional excludible original target or for any qualifying target affiliate.

(B) Only the corporation for which the express election is made is deemed to be the original target.

(C) An express election for a qualifying target affiliate is valid only if a transitional exclusion election also is made for the following corporations, (which are treated as transitional target affiliates under these circumstances): *(1)* the transitional excludible original target and *(2)* each qualifying target affiliate with an acquisition date occurring before the acquisition date of the qualifying target affiliate for which the express election is made.

(ii) *Transitional excludible original target.* A "transitional excludible original target" is a corporation described in section 338(h)(6)(B)(i) that is an original target acquired on or before March 15, 1986 (within the meaning of paragraph (j)(2)(ii) of this section). For purposes of applying §1.338-4T(b)(4) (definition of original target) to this subdivision (ii), the section 338 election referred to therein is considered one with respect to which a transitional exclusion election is not made.

(iii) *Qualifying target affiliate*—(A) *General rule.* A corporation is a qualifying target affiliate if it is a potential qualifying target affiliate that is not an excepted target. A corporation is a potential qualifying target affiliate if *(1)* it is a target even in the absence of a section 338 election and *(2)* it would be subject to a deemed election under section 338(f)(1) if an express election (and no transitional exclusion election) were made for the transitional excludible original target.

(B) *Excepted target.* A potential qualifying target affiliate is an excepted target and thus is not a qualifying target affiliate if its acquisition date occurs after the acquisition date of a potential qualifying target affiliate that is not a transitional target affiliate. The determination of transitional target affiliate status is made without regard to the provisions of this subparagraph (3).

(iv) *Coordination with protective carryover election.* For guidance in a case in which P wishes to make a protective carryover election under §1.338-4T(f)(6) instead of an express election, see paragraph (c)(2)(iv)(F) of this section.

(4) *Examples.* The provisions of paragraph (j)(1) through (3) of this section may be illustrated by the following examples:

Example (1). On December 31, 1984, P purchases from DS all of the stock of DT in a qualified stock purchase. DT holds all of the stock of FT1, FT1 holds all of the stock of FT2, and FT2 holds all of the stock of FT3. FT1, FT2, and FT3 are transitional target affiliates, since an express election for DT would cause deemed elections under section 338(f)(1) for FT1, FT2, and FT3, and since each of those three corporations is acquired on or before March 15, 1986 (within the meaning of paragraph (j)(2)(ii) of this section). Accordingly, P may elect to exclude FT1, FT2, and/or FT3 from the status of a target affiliate in a transitional exclusion election filed in connection with an express election for DT. Note that a transitional exclusion election for FT1 need not also specify FT2 and FT3, since the benefit of excluding FT1 from the status of a target affiliate (avoidance of a section 338 election for FT1) automatically will apply to FT2 and FT3. (A qualified stock purchase and section 338 election cannot occur for FT2 unless FT1 is deemed to sell its FT2 stock pursuant to an election under section 338. Similarly, a qualified stock purchase and section 338 election cannot occur for FT3 unless FT2 is deemed to sell its FT3 stock pursuant to an election under section 338. See section 338(a)(1) and (h)(3)(B).)

Example (2). (i) Assume the same facts as in Example (1), except that DT is FT. Assume also that P acquires the stock of FT4, FT5, DT6 and FT7 from DS in qualified stock purchases on January 31, 1985, April 1, 1985, June 1, 1985, and July 1, 1985, respectively. Assume in addition that FT4, FT5, DT6, and FT7 were members of the DS group on December 31, 1984. Finally, assume that DT6 is a domestic corporation that is not described in section 338(h)(6)(B)(i).

(ii) FT is a transitional excludible original target within the meaning of paragraph (j)(3)(ii) of this section. FT1, FT2, and FT3 are not qualifying target affiliates because they are not targets in the absence of a section 338 election. See paragraph (j)(3)(iii)(A)*(1)* of this section. (Such corporations would be targets only by reason of the deemed purchase of stock under section 338(a)(1). See section 338(h)(3)(B).) FT4, FT5, and DT6 are qualifying target affiliates within the meaning of paragraph (j)(3)(iii) of this section, since (A) they are targets even in the absence of a section 338 election, (B) they would be subject to deemed elections under section 338(f)(1) if an express election (and no transitional exclusion election) were made for the transitional excludible original target, and (C) they are not excepted targets. FT7 is not a qualifying target affiliate because it is an excepted target, *i.e.*, its acquisition date occurs after the acquisition date of DT6, a qualifying target affiliate that would not be a transitional target affiliate if an express election were made for FT. See paragraph (j)(3)(iii)(B) of this section.

(iii) Under these facts, an express election may be made for FT or, pursuant to paragraph (j)(3) of this section, FT4, FT5, or DT6. The express election cannot be made for FT7, since it is not a qualifying target affiliate. If, for example, P wishes to make an express election for FT4, then that express election will be valid only if a transitional exclusion election is made for FT, the transitional excludible original target that is treated as a transitional target affiliate under these circumstances. If the express election is made, for FT4, then, at P's option, a transitional exclusion election may be made for FT4 and/or FT7. The transitional exclusion election cannot be made for DT6, since DT6 is not a transitional target affiliate. If P wishes to make an express election for FT5, then that express election will be valid only if transitional exclusion elections are made for FT and FT4. At P's option under these circumstances, a transitional exclusion election may be made for FT7.

(5) *Relationship between transitional exclusion election and regular exclusion election*—(i) *In general.* A transitional exclusion election applies only to transitional target affiliates. If a transitional exclusion election is or could be made in connection with an express election, then, in the absence of an invalidation event (within the meaning of paragraph (c)(2)(iii) of this section), a separate regular exclusion election also may be made for all of the exclusible foreign target affiliates.

(ii) *Special rule for application of regular exclusion election.* Under paragraph (c)(2)(i) of this section, a domestic original target is a prerequisite for a regular exclusion election. If the express election is made for a foreign original target with an acquisition date that occurs on or before March 15, 1986 (within the meaning of paragraph (j)(2)(ii) of this section), however, that foreign corporation will be treated as if it were a domestic original target for purposes of applying such paragraph (c)(2)(i).

(iii) *Limitation on application of paragraph (c)(3) of this section.* The special basis rules of paragraph (c)(3) of this section do not apply if the acquisition date of the domestic target occurs on or before March 15, 1986 (within the meaning of paragraph (j)(2)(ii) of this section).

(iv) *Limitation on application of paragraph (c)(4) of this section.* If the acquisition date of the actual (as opposed to a deemed) original target occurs on or before March 15, 1986 (within the meaning of paragraph (j)(2)(ii) of this section) and if a valid regular exclusion election is made, then paragraph (c)(4) of this section (relating to carryover basis in certain asset acquisitions) applies only to asset acquisitions from excludible foreign target affiliates and not from non-target foreign target affiliates. For transitional asset consistency rules, see paragraph (j)(6) of this section.

(v) *Overlap between paragraphs (c)(2)(iv) and (j)(3) of this section*—(A) *In general.* This subdivision (v) provides rules for cases in which there is an overlap between the provisions of paragraphs (c)(2)(iv) and (j)(3) of this section. Those provisions provide prospective and transitional rules, respectively, for making an express election for a corporation other than the original target. In a case in which there are both transitional target affiliates and excludible foreign target affiliates, an express election may be made for (A) the transitional excludible original target, (B) a qualifying target affiliate pursuant to paragraph (j)(3) of this section, or (C) the qualifying domestic target affiliate pursuant to paragraph (c)(2)(iv) of this section, as modified by this subdivision (v).

(B) *Illustrative factual situation.* The rules of this subdivision (v) are set out in the context of the following factual situation: Assume that on April 1, 1985, FS owns all of the stock of FT1, FT2, FT3, FT4, and DT5. Assume in addition that P acquires the stock of those corporations in qualified stock purchases from FS on the dates indicated in the following table (the post-March 15, 1986, acquisitions are not made pursuant to a binding contract in effect on February 19, 1986):

Table

4/1/85	10/1/85	4/1/86	7/1/86	8/1/86
FT1	FT2	FT3	FT4	DT5

(C) *Express election for transitional excludible original target or qualifying target affiliate.* Under paragraph (j)(3) of this section, an express election may be made for FT1, the transitional excludible original target, or for FT2 or FT3, both of which are qualifying target affiliates. An express election is not permitted under paragraph (j)(3) of this section for FT4 or DT5, since those corporations are excepted targets within the meaning of paragraph (j)(3)(iii)(B) of this section. FT4 and DT5 are excepted targets because their acquisition dates occur after the acquisition date of a potential qualifying target affiliate, FT3, that is not a transitional target affiliate. An express election for FT3, for example, is valid only if transitional exclusion elections also are made for FT1 and FT2, which are considered transitional target affiliates under these circumstances. See paragraph (j)(3)(i)(C) of this section.

(D) *Express election for qualifying domestic target affiliate.* Because one of the qualifying target affiliates for which an express election could be made under paragraph (j)(3) of this section (FT3), is a foreign target acquired after March 15, 1986 (within the meaning of paragraph (j)(2)(ii) of this section), this subdivision (v) also permits P to make the express election for DT5 (as the qualifying domestic target affiliate) rather than for FT1, FT2, or FT3 if three conditions are satisified. The first condition is that DT5 must be a corporation that would have been a qualifying domestic target affiliate under paragraph (c)(2)(iv)(C) of this section had FT3 (*i.e.*, a foreign corporation that is a qualifying target affiliate acquired after March 15, 1986) been the actual original target. The second condition is that a valid regular exclusion election under paragraph (c)(2)(iv) of this section must be made in connection with the express election for DT5 is the same manner as if FT3 were the actual original target. (Pursuant to paragraph (c)(2)(iv) of this section, that regular exclusion election applies to FT3 and FT4.) The third condition is that transitional exclusion elections must be made as if the express election had been made for FT3, *i.e.*, transitional exclusion elections must be made for FT1 and FT2. See paragraph (j)(3)(i)(C) of this section.

(E) *Express election for FT3 bars regular exclusion election.* An express election under paragraph (j)(3) of this section for FT3, a foreign corporation acquired after March 15, 1986, bars a regular exclusion election. (Subject to the transitional rule of paragraph (j)(5)(ii) of this section, which is inapplicable on these facts, a regular exclusion election cannot be made if the original target for which the express election is made is a foreign corporation.) Thus, FT4 could not be excluded from the status of a target affiliate if an express election were made for FT3. If, however, an express election under paragraph (j)(3) of this section is made for FT2, a foreign corporation acquired on or before March 15, 1986, then the transitional rule of paragraph (j)(5)(ii) of this section applies and a regular exclusion election may be made (and will not be invalidated retroactively) unless an invalidation event under paragraph (c)(2)(iii) of this section occurs with respect to one of the excludible foreign target affiliates, *i.e.*, FT3 or FT4.

(F) *FT3 is DT3.* If FT3 were DT3, then (whether or not DT3 was described in section 338(h)(6)(B)(i)) an express election could be made only for FT1 or, pursuant to paragraph (j)(3) of this section, FT2 or DT3. Aan express election could not be made for DT5 on these facts because none of the qualifying target affiliates is a foreign corporation acquired after March 15, 1986. See paragraph (j)(5)(V)(D) of this section.

(G) *FT1 is DT1.* If FT1 were DT1, a domestic corporation not described in section 338(h)(6)(B)(i), then the express election could be made only for DT1 since the original target would not be a transitional excludible original target under paragraph (j)(3)(ii) of this section.

(H) *FT2 is DT2.* If FT2 were DT2, a domestic corporation not described in section 338(h)(6)(B)(i), then the express election could be made only for FT1 or DT2, since no corporation acquired after the acquisition date of DT2 is a qualifying target affiliate. See paragraph (j)(3)(iii)(B) of this section.

(I) *Effect of invalidation event after express election filed for DT5.* If an invalidation event occurs after an express election is made for DT5 (*e.g.*, the P group acquires an excludible foreign target affiliate that holds stock in a domestic corporation under the circumstances described in paragraph (c)(2)(iii)(C) of this section), then, subject to the barred target rule of paragraph (c)(2)(iii)(D) of this section, FT3 and FT4 will be subject to deemed elections under section 338(f)(1) by reason of the express election for DT5. See paragraph (c)(2)(iv)(E) of this section. FT1 and FT2 will not be affected by the invalidation event since they are not excludible foreign target affiliates. Accordingly, FT1 and FT2 will not be subject to deemed elections under section 338(f)(1) by reason of the invalidation event.

(vi) *Examples.* The provisions of this subparagraph (5) may be illustrated by the following examples.

Example (1). (i) Assume the same facts as in Example (2) of paragraph (j)(4) of this section, except that the acquisition dates of FT5, DT6, and FT7 occur on June 1, 1985, April 1, 1986, and May 1, 1986, respectively. Assume in addition that a binding contract to acquire DT6 and FT7 is not in effect on February 19, 1986.

(ii) The result is the same as in Example (2) of paragraph (j)(4) of this section, except that FT7 is not a transitional target affiliate and therefore cannot be excluded from the status of a target affiliate pursuant to a transitional exclusion election. In addition, FT7 cannot be excluded from the status of a target affiliate pursant to a regular exclusion election made in connection with an express election for FT, FT4, FT5, or DT6. A regular exclusion election cannot be made (or is retroactively invalidated) because P's acquisition of FT7 is an invalidation event under paragraph (c)(2)(iii)(B) of this section. (That acquisition is an invalidation event because FT7 was a controlled foreign corporation during the relevant period.)

Example (2). Assume the same facts as in Example (1), except that DS is FS. Assume further that FS is not a controlled foreign corporation and that FT7 does not hold stock of a domestic corporation under the circumstances described in paragraph (c)(2)(iii)(C) of this section. Under these facts, FT7 is not a controlled foreign corporation during the relevant period and P's direct acquisition of its stock is not an invalidation event. Accordingly, the results are the same as in Example (1), except that a regular exclusion election (applicable to FT7) may be made in connection with the express election for FT, FT4, FT5, or DT6.

(6) *Transitional asset consistency rules for corporations described in section 338(h)(6)(B)(i)*—(i) *General rule.* A transitional asset acquisition from a corporation that is described in section 338(h)(6)(B)(i) and that is not an excluded transferor shall in no case be treated as a tainted asset acquisition (within the meaning of §1.338-4T(f)(6)(i)) with respect to any target. Accordingly, such an asset acquisition cannot cause an affirmative action carryover election and will not be subject to an otherwise applicable affirmative action or protective carryover election.

(ii) *Definitions*—(A) *Transitional asset acquisition.* A "transitional asset acquisition" is any asset acquisition made by P (or another member of the P group) on or before March 15, 1986, that is not subject to the special asset consistency rule of paragraph (c)(4)(i) of this section (applicable in the case of a regular exclusion election).

(B) *Acquisition made on or before March 15, 1986.* An asset acquisition is considered made on or before March 15, 1986, if the asset actually is acquired on or before March 15, 1986, or if it is acquired after that date but pursuant to a contract of sale that is binding on both the acquiring P group member and the transferor as of February 19, 1986.

(C) *Excluded transferor.* An "excluded transferor" is a corporation that is either *(1)* a transitional target affiliate subject to a transitional exclusion election made in connection with an express election or *(2)* any other corporation that, but for the transitional exclusion election, would be subject to a deemed election under section 338 (f)(1) by reason of the express election.

(iii) *Special asset consistency rule for acquisition from excluded transferor*—(A) *General rule.* A P group member must take a carryover basis in an asset acquired from an excluded transferor as if the asset acquisition were subject to an affirmative action carryover election if, in the absence of an express election, the asset acquisition would be considered a tainted asset acquisition (as defined in §1.338-4T(f)(6)(i)) with respect to any relevant target (as defined in paragraph (c)(4) (iii) of this section). For guidance on the affirmative action carryover election, see §1.338-4T(f)(6). Except as provided in this subdivision (iii) or in paragraph (c)(4) of this section (which contains a similar prospective rule), no asset acquisition shall be treated as a tainted asset acquisition if an express election is made.

(B) *Deemed election not imposed.* In no event shall the District Director impose a deemed election under section 338(e)(1) as a result of an asset acquisition from any excluded transferor.

(iv) *Examples.* The provisions of this subparagraph (6) may be illustrated by the following examples.

Example (1). Assume the same facts as in Example (1) of paragraph (j)(4) of this section. Assume in addition that P makes a protective carryover election for DT in lieu of an express election, and that on January 1, 1985, P purchases for cash an asset from FT1, DT's wholly owned subsidiary. Because the asset is acquired in a transitional asset acquisition, it will in no case be considered a tainted asset acquisition subject to the protective carryover election. Accordingly, P's basis in the asset will be determined under section 1012. (The result is the same if P does not make a protective carryover election.)

Example (2). Assume that P makes an express election for DT under the facts of Example (1) of paragraph (j)(4) of this section. Assume in addition that P makes a transitional exclusion election for FT2 in that express election, and that on January 1, 1985, P purchases an asset from FT2 in a transaction that would be a tainted asset acquisition if an express election were not made. Because FT2 is an excluded transferor within the meaning of paragraph (j)(6)(ii)(C) of this section, P must take a carryover basis in the acquired asset as if the acquisition were subject to an affirmative action carryover election.

Example (3). Assume the same facts as in Example (2), except that the asset is acquired from FT3. Although a transitional exclusion election was not made for FT3, FT3 is a corporation that would have been subject to a deemed election under section 338(f)(1) by reason of the express election for DT had the transitional exclusion election for FT2 not been made. Thus, FT3 is an excluded transferor and the result is the same as in Example (2).

Example (4). Assume the same facts as in Example (2), except that the asset is acquired from FT1. FT1, a transitional target affiliate that is not subject to the transitional exclusion election, is not an excluded transferor. (FT1 is subject to a deemed election under section 338(f)(1) by reason of the express election for DT.) Accordingly, P does not take a carryover basis in the asset under paragraph (j)(6)(iii) of this section but rather takes a basis determined under section 1012.

(7) *Treatment of stock described in section 338 (h)(6)(B)(ii)*—(i) *Transitional stock exclusion election.* If P makes a transitional stock exclusion election in the manner prescribed in paragraph (j)(8) of this section for one or more eligible targets, then the following stock held by such an eligible target at the close of its acquisition date ("affected stock") shall be excluded from the operation of section 338:

(A) All section 338(h)(6)(B)(ii) stock other than stock in a transitional target affiliate (as defined in paragraph (j)(2) of this section) and

(B) All section 338(h)(6)(B)(ii) stock that is stock in a transitional target affiliate for which a transitional exclusion election is made under paragraph (j)(1) of this section.

(ii) *Section 338(h)(6)(B)(ii) stock.* "Section 338(h)(6)(B)(ii) stock" is stock in a foreign corporation or a domestic corporation that is a DISC or that is described in section 1248(e), whether or not the corporation is a target or a target affiliate.

(iii) *Eligible target.* An "eligible target" is a target that is subject to a deemed election under section 338(f)(1) and which is acquired on or before February 12, 1986 or pursuant to a binding contract in effect on that date.

(iv) *Effect of exclusion from operation of section 338.* If a transitional stock exclusion election is made for an eligible target, then—

(A) that eligible target is not deemed under section 338(a) to sell and purchase the affected stock it holds at the close of its acquisition date and

(B) that eligible target's basis as new target in that affected stock is the same as its basis in that stock as old target immediately before its deemed sale of assets under section 338(a)(1) ("carryover basis amount").

(v) *Effect of difference between carryover basis amount and regular basis amount.* If the carryover basis amount for affected stock held by an eligible target (as new eligible target) is less than the basis amount that, absent paragraph (j)(7)(iv) of this section, would be allocable to that stock ("regular basis amount"), then the difference is eliminated. Whether or not the carryover basis amount is less than or exceeds the regular basis amount, however, that regular basis amount is treated as the total amount allocated to the affected stock for purposes of allocating new eligible target's adjusted grossed-up basis among the other asets of new eligible target.

(vi) *Tacking of old eligible target's holding period.* If a transitional stock exclusion election is made for an eligible target and if, subsequent to its acquisition date, that eligible target disposes of affected stock, then, for purposes of applying section 1248 to that disposition, the holding period of new eligible target for that affected stock includes the holding period of old eligible target for that stock.

(vii) *Examples.* The provisions of this paragraph (j)(7) may be illustrated by the following examples. In each example, assume that all of the corporations are calendar year corporations.

Example (1). On December 31, 1984, P purchases all of the stock of DT from DS in a qualified stock purchase and makes an express election for DT. DT holds 20 of the 100 shares of FX's only class of outstanding stock, and DS holds the remaining 80 shares. (Since all of the stock of FX is held by U.S. shareholders, FX is a controlled foreign corporation.) Although the stock of FX is affected stock within the meaning of paragraph (j)(7)(i) of this section and although the acquisition date of DT occurs on or before February 12, 1986, a transitional stock exclusion election applicable to DT cannot be made. An original target (*i.e.*, a target that is not subject to a deemed election under section 338(f)(1)) cannot be an eligible target. See paragraph (j)(7)(iii) of this section.

Example (2). (i) Assume the same facts as in Example (1), except that DT's wholly owned subsidiary, DT1, holds the 20 shares of FX stock. Assume in addition that old DT1's basis in that FX stock is $70 and that, absent paragraph (j)(7)(iv) of this section, new DT1's basis in the FX stock would be $100. Finally assume that DT1 sells the 20 shares of FX stock on January 15, 1985, for $90.

(ii) A transitional stock exclusion election applicable to DT1 (and thus to the FX stock held by DT1) may be made, since DT1 is an eligible target. DT1 is an eligible target because its acquisition date occurs on or before February 12, 1986, and it is subject to a deemed election under section 338(f)(1) by reason of P's express election for DT. If a transitional stock exclusion election is made for DT1, then old DT1 will not include in its gross income a section 1248(f) dividend as a result of its deemed sale of assets, since it will not be deemed to sell the FX stock it holds. See paragraph (j)(7)(iv)(A) of this section. In addition, new DT1's basis in FX stock (*e.g.*, for purposes of DT1's sale of that FX stock on January 15, 1985) shall be the same as old DT1's basis in such stock immediately before DT1's deemed sale of assets, *i.e.*, $70. See paragraph (j)(7)(iv)(B) of this section. For purposes of allocating new DT1's adjusted grossed-up basis among the other assets of new DT1, however, the amount that, absent this paragraph (j)(7), would have been allocated to the FX stock held by DT1 (*i.e.*, $100) shall be deemed to be the amount actually alocated to that stock.

(iii) Accordingly, DT1's gain on the January 15, 1985, sale of FX stock is $20, *i.e.*, the difference between the selling price ($90) and DT1's carryover basis in the FX stock ($70). For purposes of applying section 1248 to that sale, new DT1's holding period in the stock of FX includes old DT1's holding period. Thus, the earnings and profits of FX that accrued during the period while old DT1 held the FX stock must be taken into account under the principles of section 1248 in determining new DT1's section 1248 dividend (if any) on the January 15, 1985, sale.

Example (3). Assume the same facts as in Example (2), except that the 80 shares of FX stock are held by DT2, another wholly owned subsidiary of DT, rather than by DS. Thus, DT1 and DT2 are eligible targets and FX is a transitional target affiliate. Accordingly, a transitional stock exclusion election made for DT1 and/or DT2 will not apply to the stock of FX unless a transitional exclusion election is made for FX.

Example (4). Assume the same facts as in Example (2), except that the 80 shares of FX stock are held by an individual. Accordingly, FX is not a target affiliate of DT or DT1. The result is the same as in *Example (2)*, since affected stock need not be stock in a target affiliate.

(8) *Transitional section 338(h)(6)(B) election procedures*—(i) *General rule.* This subparagraph (8) prescribes procedures for making the transitional exclusion election and the transitional stock exclusion election under paragraph (j)(1) and (7) of this section, respectively ("transitional elections"). The transitional elections are made by attaching a transitional section 338(h)(6)(B) statement to the express election (Form 8023) filed for the original target (including a qualifying target affiliate treated as the original target

under paragraph (j)(3) of this section). The transitional section 338(h)(6)(B) statement, once filed, is treated as an integral part of the Form 8023 (*e.g.*, for purposes of §1.338-1T(e)(2)(i) (requiring that the Form 8023 be attached to certain returns)). The transitional elections are irrevocable.

(ii) *Special procedure if express election filed on or before March 15, 1986.* If a transitional section 338(h)(6)(B) statement is not attached to an express election filed on or before March 15, 1986, a transitional election(s) nonetheless may be made if, on or before that date, a copy of the previously filed express election, with a copy of the transitional section 338(h)(6)(B) statement attached, is filed with the Internal Revenue Service Center(s) with which the express election is required to be filed under §1.338-1T(c) and (d).

(iii) *Amendment procedure if transitional statement filed on or before March 15, 1986.* A transitional section 338(h)(6)(B) statement filed on or before March 15, 1986, may be amended on or before that date for two purposes. First, if only one transitional election was made in the previously filed statement, when an amended statement may be made to include both transitional elections. Second, the previously filed statement may be amended to make additional corporations subject to a transitional election already made. The amended statement is filed pursuant to the procedure described in paragraph (j)(8)(ii) of this section, and a copy of the previously filed section 338(h)(6)(B) statement must be attached.

(iv) *Acquisition date of transitional target affiliate or eligible target occurs after transitional section 338(h)(6)(B) statement filed.* A transitional target affiliate or an eligible target will be subject to a transitional exclusion election or transitional stock exclusion election, respectively, only if such a corporation is named in the transitional section 338(h)(6)(B) statement (including an amended statement), notwithstanding that the acquisition date of such a corpoation occurs after that statement is filed. The failure of the P group to actually acquire a corporation named in the transitional section 338(b)(6)(B) statement pursuant to this subdivision (iv) shall have no effect on the validity of that statement.

(v) *Contents of transitional section 338 (h)(6)(B) statement.* The transitional section 338 (h)(6)(B) statement must—

(A) Be identified prominently as a transitional exclusion election under §1.338-5T(j)(1), as a transitional stock exclusion election under §1.338-5T(j)(7), or both.

(B) Where applicable, indicate that it is an amended statement.

(C) Contain the following declaration (or a substantially similar declaration) if a transitional exclusion election is made: "THE TRANSITIONAL EXCLUSION ELECTION PERMITTED BY §1.338-5T(j)(1) IS HEREBY MADE FOR THE TRANSITIONAL TARGET AFFILIATES IDENTIFIED HEREIN".

(D) Contain the following declaration (or a substantially similar declaration) if a transitional stock exclusion election is made: "THE TRANSITIONAL STOCK EXCLUSION ELECTION PERMITTED BY §1.338-5T(j)(7) IS HEREBY MADE FOR THE ELIGIBLE TARGETS IDENTIFIED HEREIN".

(E) For each of the following corporations contain the name, address, employer identification number (if any), and, for a foreign corporation, the country (and, if relevant, the lesser political subdivision) under the laws of which it is organized. The following corporations are: *(1)* each transitional target affiliate for which a transitional exclusion election is made, with corporations included pursuant to paragraph (j)(8)(iv) of this section so identified (such as by a footnote system), *(2)* each eligible target for which a transitional stock exclusion election is made, with corporations included pursuant to paragraph (j)(8)(iv) of this section so identified, and *(3)* if determinable as of the day of filing, each other corporation that would be subject to the express election absent the transitional elections.

(F) Be signed (in the manner prescribed in §1.338-1T(d)(1)(v)) by a person authorized to act on behalf of P.

Par. 3. Section 1.338-1T is amended as follows—

1. Paragraph (b) is amended by adding a new paragraph (b)(9) to read as set forth below.

2. Paragraph (c) is revised to read as set forth below.

3. Paragraph (d) is amended by—

a. Revising the heading to read as set forth below.

b. Removing, from the first sentence of paragraph (d)(1), the words "statement of election under section 338" and by adding in their place the words "statement of section 338 election".

c. Removing, from the third sentence of paragraph (d)(1), the words "statement of election" and by adding in their place the words "statement of section 338 election".

d. Removing from paragraph (d)(1)(i) the word "target" and by adding in its place the words "original target".

e. Removing the word "and" from paragraph (d)(1)(iv), redesignating paragraph (d)(1)(v) as paragraph (d)(1)(vi), and adding a new paragraph (d)(1)(v) to read as set forth below.

f. Revising paragraph (d)(2) to read as set forth below.

g. Removing, from each place they appear in paragraph (d)(3), the words "statement of election" and by adding in their place the words "statement of section 338 election".

4. Paragraph (e) is amended by—

a. Revising paragraph (e)(1) to read as set forth below.

b. Revising paragraph (e)(2)(i), (ii), and (iii) to read as set forth below.

c. Removing, from the first sentence of paragraph (e)(2)(iv), the words "statement of election" and by adding in their place the words "statement of section 338 election".

d. Adding a new paragraph (e)(2)(v) to read as set forth below.

e. Revising paragraph (e)(3) to read as set forth below.

5. Paragraph (j) is revised to read as set forth below.

6. Paragraph (k) is amended by—

a. Revising paragraph (k)(1) to read as set forth below.

b. Removing from paragraph (k)(2)(i) the words "statement of election" and by adding in their place the words "statement of section 338 election".

c. Revising paragraph (k)(2)(v) to read as set forth below.

d. Removing paragraph (k)(3)(iii).

e. Revising the heading of paragraph (k)(4) to read as set forth below.

f. Removing, from each place they appear in paragraph (k)(4), the words "statement of election" and by adding in their place the words "statement of section 338 election".

g. Revising paragraph (k)(5) to read as set forth below.

h. Removing paragraph (k)(6) and by redesignating paragraph (k)(7) as paragraph (k)(6).

i. Revising subdivisions (i) and (ii) of redesignated paragraph (k)(6) to read as set forth below.

j. Adding a new paragraph (k)(7) to read as set forth below.

§1.338-1T Elections under section 338(g) of the Internal Revenue Code of 1954 (temporary).

* * * * *

(b) *Definitions*—(1) * * *

* * * * *

(9) *Cross-reference*. The definitions in §1.338-4T (as modified by §1.338-5T(b)(2)) also apply for purposes of this section.

(c) *Time and manner of making election*. The purchasing corporation makes an election under section 338(g) for the original target only by filing, not later than the 15th day of the 9th month beginning after the month in which the acquisition date occurs (or if later, March 15, 1986), a statement of section 338 election with the Internal Revenue Service Center with which it files its annual income tax return. If the statement of section 338 election for the original target will cause section 338(a) to apply to other corporations ("affected targets") by reason of section 338(f)(1), a separate statement of section 338 election need not be filed for those affected targets. See paragraph (e)(1) of this section for requirement to attach a schedule containing information relating to the orginal target and the affected targets. See paragraph (k)(7) of this section for a required notice to the domestic shareholders of foreign targets in certain cases. See also paragraph (k) of this section generally for other special rules applicable to certain foreign corporations and DISCs.

(d) *Statement of section 338 election*—(1) * * *

(v) For elections filed after February 19, 1986, specify (if the purchasing corporation or the original target is a foreign corporation) the country (and, if relevant, the lesser political subdivision) under the laws of which it is organized, and

(2) ***Signature requirement if common parent is the agent of purchasing corporation***. If the common parent of an affiliated group filing consolidated returns is the agent of the purchasing corporation under §1.1502-77, then the person authorized to sign the statement of section 338 election pursuant to paragraph (d)(1)(v) of this section is the person authorized to act on behalf of that common parent.

(e) *Schedule; attachments to target returns*—(1) Schedule of information relating to certain corporations and persons—(i) *Required data*. A schedule providing the information specified in the paragraph (e)(1)(i) ("required data") must be attached to the statement of section 338 election. That schedule must satisfy the following requirements:

(A) It must contain the name, address, and employer identification number each includible affected target, *i.e.*, each corporation that, as of the day the statement of section 338 election is filed ("day of filing"), is an affected target subject to that election by reason of section 338(f)(1). For each includible affected target that is a foreign corporation, it must also contain the country (and, if relevant, the lesser political subdivision) under the laws of which it is organized.

(B) It must disclose the fair market value of the consideration paid by the purchasing corporation for the stock of each directly acquired target, *i.e.*, *(1)* the original target, *(2)* each includible affected target, *(3)* each excludible foreign target affiliate identified under paragraph (e)(1)(i)(F) of this section, *(4)* each transitional target affiliate (that is identified in an attached transitional exclusion election pursuant to §1.338-5T(j)(8) and that is actually acquired on or before the day of filing), and *(5)* each other corporation that, as of the day of filing, would be a target but for the transitional exclusion election (if any). For purposes of this subdivision (i), a directly acquired target does not include a corporation the qualified stock purchase of which occurs solely by reason of section 338(a)(2) and (h)(3)(B) (or would so occur if a regular or transitional exclusion election were not made) ("indirectly acquired corporation").

(C) It must identify the portion of the consideration paid for the stock of each directly acquired target that is represented by the following components: *(1)* cash, *(2)* purchase money debt, and *(3)* other components of consideration (with each such other component separately stated).

(D) It must disclose the liabilities (with any tax liability resulting from the deemed sale of assets under section 338(a)(1) separately stated), as of the close of the acquisition date (or as of the close of the day that would be the acquisition date if a regular or transitional exclusion election were not made), of each of the corporations described in paragraph (e)(1)(i)(B) of this section and of each other corporation that would be so described but for the exception therein for indirectly acquired corporations.

(E) If an election under section 338(h)(10 is made, it must clearly identify (such as by a footnote system) each corporation listed on the schedule that is subject to that election, including corporations subject to deemed section 338(h)(10) elections under §1.338(h)(10)-1T(h).

(F) If a regular exclusion election under §1.338-5T(c)(2) is made, the schedule must contain the name, address, and employer identification number (if any) of, and country (and, if relevant, the lesser the political subdivision) under the laws of which is organized, each corporation that, as of the day the schedule is filed, is an excludible foreign target affiliate, with each such corporation clearly identified (such as by a footnote system) as an excludible foreign target affiliate subject to a regular exclusion election.

(G) It must contain the name, address, and identifying number (if available) of each U.S. person to whom notice of the election must be sent as of the day the statement of section 338 election is filed (see paragraph (k)(7) of this section).

(ii) *Corrective statements*—(A) *Transitional rule*. If a statement of section 338 election filed on or before March 15, 1986, does not include the schedule with all of the required data, the requirements of paragraph (e)(1)(i) of this section will be satisified if, on or before March 15, 1986, a corrective statement in the form of the schedule (containing all of the required data, and with a copy of the previously filed statement of section 338 election attached) is filed with the Internal Revenue Service Center(s) with which the statement of section 338 election is required to be filed under paragraphs (c) and (d) of this section.

(B) *Regular exclusion election invalidated.* If, subsequent to the making of a regular exclusion election, that exclusion election is invalidated by reason of an invalidation event described in §1.338-5T(c)(2)(iii) and if, by reason of the invalidation event, a previously filed schedule under this subparagraph (1) incorrectly identifies certain corporations as excludible foreign target affiliates subject to a regular exclusion election, then the requirements of paragraph (e)(1)(i) of this section will be satisfied if, on or before the later of March 15, 1986, or the 120th day after the date of the invalidation event, a corrective statement in the form of an amended schedule (along with a copy of the previously filed statement of section 338 election) is filed with the Internal Revenue Service Center(s) with which the statement of section 338 election is required to be filed under paragraphs (c) and (d) of this section. (The invalidated regular exclusion statement need not be attached.) The revised schedule must clearly identify (such as by a footnote system) the corporations that are no longer treated as excludible foreign target affiliates subject to a regular exclusion election. The following declaration (or a substantially similar declaration) must be set forth on the amended schedule: "THIS SCHEDULE IS AMENDED BY REASON OF THE INVALIDATION UNDER §1.338-5T(c)(2)(iii) OF A REGULAR EXCLUSION ELECTION."

(C) *Schedule must be updated.* The schedule filed as a corrective statement under this subdivision (ii) must contain the required data described in paragraph (e)(1)(i) of this section for each corporation subject to the statement of section 338 election as of the day the schedule is filed.

(2) *Attachments to target returns; additional filings with certain Service Centers*—(i) *Attachments.* The items described in this subdivision (i) ("required items") must be attached to old target's final return and to the first return of new target. For purposes of this subparagraph (2), the term "target" refers to the original target and each affected target subject to the express election for the original target. The required items are—

(A) A copy of the statement of section 338 election (including a copy of any election made by filing a separate statement in connection with the statement of section 338 election) and

(B) The schedule described in paragraph (e)(1)(i) of this section ("schedule").

(ii) *Corrective statements*—(A) *Transitional rule.* If all of the required items (containing all of the information required to be included in those items) are not attached to a final return of old target or a first return of new target that is filed on or before March 15, 1986, the requirements of paragraph (e)(2)(i) of this section will be satisfied if, on or before that date a corrective statement consisting of all of the required items (containing all of the information required to be included in those items) is filed with the Internal Revenue Service Center(s) with which the returns to which the required items should have been attached were filed.

(B) *Special rule if regular exclusion election invalidated.* If, under the circumstances described in paragraph (e)(1)(ii)(B) of this section (relating to invalidation of regular exclusion election), a previously filed schedule under this paragraph (e)(2) incorrectly identifies certain corporations as excludible foreign target affiliates subject to a regular exclusion election, then the requirements of paragraph (e)(2)(i) of this section will be satisfied only if, on or before the 120th day after the date of the invalidation event, a corrective statement in the form of an amended schedule (containing the information and attachment required by paragraph (e)(1)(ii)(B) of this section) is filed with the Internal Revenue Service Center(s) with which the previously filed schedule was required to be filed.

(iii) *Additional filings with certain Service Centers.* On or before the day on which any return or corrective statement described in paragraph (e)(2)(i) or (ii) of this section is filed, the required items also must be filed with the Internal Revenue Service Centers with which the statement of section 338 election is required to be filed under paragraphs (c) and (d) of this section. If a gain recognition election under section 338(b)(3) is made in connection with the statement of section 338 election (so that a copy of the gain recognition statement ("GRS") under §1.338-4T(j)(2) is a required item pursuant to paragraph (e)(2)(i)(A) of this section), then, on or before the day specified in the preceding sentence, the required items also must be filed with each other Service Center with which each affected P group member (determined as of the day of filing) files its annual income tax return. For the definition of "affected P group member," see §1.338-4T(j)(2) *Answer 5* (ii)(A). The required items need not, however, be filed with a Service Center that already has received the identical required items.

* * * * *

(v) *Special rules for returns to which required items must be attached*—(A) *Target subject to section 338(h)(10) election.* If a target is subject to an election under section 338(h)(10), then the required items specified in paragraph (e)(2)(i) of this section are considered filed with the last return of old target if they are attached to the return of the selling consolidated group for the taxable period that includes the acquisition date. For guidance under section 338(h)(10), see §1.338(h)(10)-1T(d).

(B) *Certain returns filed by U.S. persons.* Each U.S. person to whom the purchasing corporation must provide notice under paragraph (k)(7)(ii)(B) of this section (relating to notice of a section 338 election for a foreign target) must attach the required items specified in paragraph (e)(2)(i) of this section to its income tax return in which it is required to report a section 1248 dividend by reason of its sale of stock in the foreign target to the purcashing corporation. In addition, each other U.S. person that is required to file an information return (Form 5471) with respect to the foreign target for a relevant taxable year of that foreign target must attach the required items to that return if *(1)* the purchasing corporation must provide notice under paragraph (k)(7)(ii)(A) to that U.S. person or *(2)* that U.S. person is a member of the affiliated group that includes the purchasing corporation. A foreign target's relevant taxable years are its taxable year that includes its acquisition date and its taxable year that includes the first day thereafter. A

U.S. person that receives a notice pursuant to paragraph (k)(7)(ii) of this section may assume that the required items received from the purchasing corporation as part of that notice are accurate for purposes of the attachment requirement.

(C) *First return of new foreign target after acquisition date.* If a United States income tax return is not required to be filed for new foreign target's taxable period that includes the first day after its acquisition date, then the required items must be attached to the first United States income tax return filed by that target for a subsequent taxable year.

(3) *Consequence of failure to comply with requirements of paragraph (e)(1) and (2) of this section*—(i) *General rule.* If the requirements of paragraph (e)(1) and (2) of this section or of §1.338-5T(c)(2)(vii)(B) (requirement of amended returns if regular exclusion election invalidated) are not satisfied with respect to the original target or any affected target, then the waiver rule of paragraph (h)(1) of this section will not apply to any of those targets. Failure to comply with those requirements will not invalidate a statement of section 338 election or any other election under section 338.

(ii) *Exception for certain returns.* Failure to comply with the provisions of paragraph (e)(2)(v) of this section will not bar the application of the waiver rule of paragraph (h)(1) of this section.

* * * * *

(j) *Special rules for acquisitions affected by regulations under section 338(h)(6)(B)*—(1) *Target subject to special rules.* This paragraph (j) applies to a target—

(i) that is a foreign corporation, a DISC, a corporation described in section 934(b), or a corporation to which section 936 applies or

(ii) that has a target affiliate (as defined in paragraph (k)(3)(ii) of this section) that either (A) is described in paragraph (j)(1)(i) of this section or (B) owns stock in a foreign corporation or a domestic corporation that is a DISC or described in section 1248(e).

(2) *No additional suspension of time to make election for target described in this paragraph.* Pursuant to paragraph (c) this section, the time to make an express election (for an acquisition subject to this section) does not expire before March 15, 1986. Prior to amendment by T.D. 8074, this paragraph (j) provided for an indefinite suspension of time to make an express election for certain targets but permitted an option to make an express election notwithstanding that suspension. Rules applicable to this obsolete option are prescribed in paragraph (j)(3), (4), and (5) of this section.

(3) *Declaration required in statement of section 338 election.* If, on or before March 14, 1986, a statement of section 338 election is filed for a target described in paragraph (j)(1) of this section and if a regular exclusion election, transitional exclusion election, or transitional stock exclusion election (as defined in §1.338-5T(c)(2), (j)(1), and (j)(7), respectively) is not made in that statement of section 338 election, then that statement of section 338 election must include, in addition to the other requirements specified in this section, the following declaration (or a substantially similar declaration): "THIS ELECTION IS MADE PURSUANT TO THE OPTION IN §1.338-1T(j)(2) TO MAKE THE SECTION 338 ELECTION NOTWITHSTANDING THE SUSPENSION."

(4) *Perfecting procedure*—(i) *General rule.* If a statement of section 338 election is required to include the declaration described in paragraph (j)(3) of this section but does not, the election nonetheless shall be valid if—

(A) A timely regular exclusion election, transitional exclusion election, or transitional stock exclusion election is filed or

(B) A timely perfecting declaration is filed.

(ii) *Perfecting declaration.* A "perfecting declaration" is a statement that contains the declaration described in paragraph (j)(3) of this section and that is signed by a person who states under penalties of perjury that he or she is authorized to make the perfecting declaration on behalf of the purchasing corporation. The perfecting declaration must be filed on or before March 15, 1986, with the Internal Revenue Service Center(s) with which the statement of section 338 election is required to be filed under paragraphs (c) and (d) of this section, and a copy of the previously filed statement of section 338 election must be attached.

(5) *Statement of section 338 election filed pursuant to this paragraph (j) is binding.* An election under section 338(g) that is made pursuant to the option in paragraph (j)(2) of this section is subject to all of the provisions of section 338 as well as to the provision of regulations issued or to be issued thereunder, including the regulations under section 338(h)(6).

(k) *Special rules for foreign corporations or DISCs*—(1) *Elections by certain foreign purchasing corporations.* A foreign purchasing corporation that is not required under §1.6012-2(g) (other than subparagraph (2)(i)*(b)(2)* thereof) to file a United States income tax return for its taxable year that includes the acquisition date must file the statement of section 338 election (or any other election under section 338) with the Philadelphia Service Center, Philadelphia, Pennsylvania 19255.

(2) *Election not required until relevant*—(i) *General rule.** * *

* * * * *

(v) *Subject to United States tax.* For purposes of this paragraph (k)(2), a foreign corporation is considered "subject to United States tax"—

(A) For the taxable year for which that corporation is required under §1.6012-2(g) (other than subparagraph (2)(i)*(b)(2)* thereof) to file a United States income tax return and

(B) For the period during which that corporation is a controlled foreign corporation, a foreign investment company, or a foreign corporation the stock ownership of which is described in section 552(a)(2).

* * * * *

(4) *Statement of section 338 election may be filed by United States shareholders in certain cases.** * *

(5) *EIN not required for certain corporations.* If, without regard to section 338 or the requlations thereunder, a corporation is not required to have an employer identification number (EIN) and if such a corporation does not actually have an EIN, then the requirement that an EIN be provided in the statement of section 338 election (or in any other election under section 338) shall not apply to that corporation.

(6) *Special rules for due date of old target's final return.*—(i) *Old target a*

foreign corporation required to file U.S. return. The final return of old target is due on the 15th day of the sixth calendar month following the month in which the acquisition date occurs if old target is a foreign corporation that is required under §1.6012-2(g) (other than subparagraph (2)(i)*(b)(2)* thereof) to file a United States income tax return for its taxable year that includes its acquisition date but that does not have an office or fixed place of business in the United States during such period.

(ii) *Old target a foreign corporation not required to file U.S. return.* A final return of old target is not required if old target is a foreign corporation that is not required under §1.6012-2(g) (other than subparagraph (2)(i)*(b)(2)* thereof) to file a United States income tax return for its taxable year that includes its acquisition date.

(iii) *Old target a DISC.** * *

(7) *Notice requirement for U.S. persons holding stock in foreign target*—(i) *Scope.* This subparagraph (7) provides rules relating to notice to U.S. persons holding stock in a foreign target. For additional information that must be included on the schedule required by §1.338–1T(e) if the notice requirement of this subparagraph (7) applies, see paragraph (e)(1)(i)(G) of this section. For rules applicable to the recipient of the notice, see paragraph (e)(2)(v)(B) of this section.

(ii) *General rule.* If a target subject to an express election (either as the original target or as an affected target) is a foreign corporation, then the purchasing corporation must deliver written notice of the election (with a copy of the statement of section 338 election attached) to—

(A) Each U.S. person (other than a member of the affiliated group that includes the purchasing corporation ("P group")) that, on the acquisition date of the foreign target or at the beginning of the first day after that acquisition date, holds stock in the foreign target and

(B) Each U.S. person (other than a P group member) that sells stock in the foreign target to a P group member during so much of the foreign target's 12-month acquisition period as ends on its acquisition date, provided that the foreign target was a controlled foreign corporation at any time during so much of the taxable year within which its acquisition date occurs as ends on that acquisition date.

(iii) *Form of notice.* The notice to U.S. persons must be identified prominently as a notice of section 338 election and must satisfy all of the following:

(A) The notice must contain the name, address, and employer identification number (if any) of, and the country (and, if relevant, the lesser political subdivision) under the laws of which is organized, the purchasing corporation and the relevant target (*i.e,* the target the stock of which the particular U.S. person held or sold under the circumstances described in paragraph (k)(7)(ii) of this section).

(B) The notice must identify those corporations as the purchasing corporation and the foreign target corporation, respectively.

(C) The notice must contain the following declaration (or a substantially similar declaration): "THIS DOCUMENT SERVES AS NOTICE OF AN ELECTION UNDER SECTION 338 FOR THE ABOVE CITED FOREIGN TARGET THE STOCK OF WHICH YOU EITHER HELD OR SOLD UNDER THE CIRCUMSTANCES DESCRIBED IN TREASURY REGULATIONS §1.338-1T(k)(7)(ii). FOR POSSIBLE UNITED STATES FEDERAL INCOME TAX CONSEQUENCES UNDER SECTION 1248 OF THE INTERNAL REVENUE CODE OF 1954 THAT MAY APPLY TO YOU, SEE TREASURY REGULATIONS §1.338-5T(g). YOU MAY BE REQUIRED UNDER TREASURY REGULATIONS §1.338-1T(e)(2)(v) TO ATTACH THE INFORMATION ATTACHED TO THIS NOTICE TO CERTAIN RETURNS."

(D) The notice must contain (as an attachment) the required items specified in paragraph (e)(2)(i) of this section.

(iv) *Timing of notice.* The notice required by this subparagraph (7) must be delivered to the U.S. person on or before the latest of the dates specified in this subdivision (iv). If notice is delivered by United States mail, the date of the United States postmark is deemed to be the date of delivery. The dates are as follows:

(A) March 15, 1986,

(B) The 120th day after the acquisition date of the particular target, or

(C) The day on which the statement of section 338 election is filed.

(v) *Consequence of failure to comply.* If a statement of section 338 election is filed after March 15, 1986, and if notice under this subparagraph (7) must be given to one or more U.S. persons on or before the day on which the statement of section 338 election is filed, then that statement of section 338 election shall not be valid if timely notice is not given to any such U.S. person. Failure to give notice to U.S. persons under circumstances other than those described in the preceding sentence shall not invalidate the statement of section 338 election, but the waiver rule of paragraph (h)(1) of this section will not apply to the same extent as if the requirements of paragraph (e) of this section were not satisfied.

* * * * *

Par. 4. Section 1.338-4T is amended as follows—

1. Paragraph (a) is amended by—

a. Removing the last sentence of paragraph (a) and by adding in its place the following sentence: "For guidance on international aspects of section 338 and on the extent to which the provisions of this section apply in that context, see §1.338-5T."

b. Adding, immediately after item (f)(1)(ii) of paragraph (a)(3), a new item (f)(2) to read as follows: "(2) Asset acquisition by P (or another member of the P group) from T or T's target affiliate."

c. Removing, from item (f)(6)(iii) of paragraph (a)(3), the misspelled word "acquistions" and by adding in this place the word "acquisitions".

d. Removing, from item (k)(3) of paragraph (a)(3), the words "and 168(d)(92)(B)" and by adding in their place the words "and 168(d)(2)(B)".

e. Removing, from the beginning of item (k)(6) of paragraph (a)(3), the parenthetical "(".

2. Paragraph (b) is amended by—

a. Adding to the end of paragraph (b)(1)(ii) the following sentence: "Except as otherwise provided in this section, T is an original target if a qualified stock purchase is made of its stock."

b. Removing, from paragraph (b)(2), the words "section 338(h)" and by adding in their place the words "section 338".

3. Pararaph (c) is amended by—

a. Removing, from the second sentence of paragraph (c)(1) *Answer 2*, the words "section 338(h)(3)(A)(ii)" and by adding in their place the words "section 338(h)(3)(A)(ii)".

b. Removing, from the third sentence of paragraph (c)(1) *Answer 4* Ex. (4), the words "section 338(h)3)" and by adding in their place the words "section 338(h)(3)."

c. Removing, from paragraph (c)(2) *Question*, the words "section 388(d)(3)" and by adding in their place the words "section 338(d)(3)."

d. Removing, from the first sentence of paragraph (c)(2) *Answer*, the misspelled word "acquistion" and by adding in its place the word "acquisition".

e. Adding a comma immediately after the word "date" in the fourth sentence of paragraph (c)(4) *Answer* Ex. (3).

f. Removing, from the sixth sentence of paragraph (c)(4) *Answer* Ex. (3), the word "that" and by adding in its place the word "the".

g. Removing, from the eighth sentence of paragraph (c)(4) *Answer* Ex. (3), the word "as" and by adding in its place the word "a".

h. Removing, from the second sentence of paragraph (c)(4) *Answer* Ex. (7)(ii), the misspelled word "contitute" and by adding in its place the word "constitute".

i. Removing, from the first sentence of paragraph (c)(5) *Answer* (i)(A), the words "the other of those corporation" and by adding in their place the words "the other of those corporations".

4. Paragraph (f)(1) is amended by—

a. Removing, from paragraph (f)(1)(ii) *Question 2* (ii), the words "target affiliate" and by adding in their place the words "a target affiliate".

b. Removing the colon that follows the word "paragraph" in paragraph (f)(1)(ii) *Question 2* (iv).

5. Paragraph (f)(3) *Answer* Ex. (3) is amended by removing from the third sentence the words "trade of" and by adding in their place the words "trade or".

6. Paragraph (f)(4) *Question 4* (i) is amended by removing the words "exchange asset" and by adding in their place the words "exchanged asset".

7. Paragraph (f)(5) is amended by—

a. Removing, from the title of paragraph (f)(5) *Answer* (vi), the word "*Property*" and by adding in its place the words "*Property acquired*".

b. Removing, from the sixth sentence of paragraph (f)(5) *Answer* (vi) Ex. (2), the words "remaining $28,000" and by adding in their place the words "remaining $18,000".

c. Revising paragraph (f)(5) *Answer* (vii) to read as set forth below.

d. Removing, from paragraph (f)(5) *Answer* (viii), the word "exception" and by adding in its place the words "exception to section".

8. Paragraph (f)(6) is amended by—

a. Revising paragraph (f)(6)(i)(A) to read as set forth below.

b. Revising paragraph (f)(6)(ii) *Answer 1* (i) by adding the following sentence at the end thereof: "For place to file in certain cases if the purchasing corporation is a foreign corporation, see §1.338-1T(k)(1)."

c. Revising paragraph (f)(6)(ii) *Answer 1* (ii) to read as set forth below.

d. Revising paragraph (f)(6)(ii) *Answer 1* (iii)(C) to read as set forth below.

e. Removing, from the first entence of paragraph (f)(6)(ii) *Answer 2* (ii), the words "with the protective" and by adding in their place the words "with which the protective".

f. Removing, from the second sentence of paragraph (f)(6)(iv) *Answer 2* (ii)(A), the words "tax liability.)" and by adding in their place the words "tax liability)."

g. Revising paragraph (f)(6)(iv) *Answer 2* (ii)(B) to read as set forth below.

h. Removing, from the first sentence of paragraph (f)(6)(iv) *Answer 3* (i), the misspelled word "*Answere*" and by adding in its place the word "*Answer*".

i. Removing, from paragraph (f)(6)(iv) *Answer 3* (ii)(C)(*3*), the words "the acquiring" and by adding in their place the words "The acquiring".

j. Revising paragraph (f)(6)(iv) *Answer 3* (iv)(D) to read as set forth below.

k. Removing, from the end of paragraph (f)(6)(iv) *Answer 3* (vi)(B), the word "rule.)" and by adding in its place the word "rule)."

l. Removing, from the fourth sentence of paragraph (f)(6)(iv) *Answer 3* Ex. (1)(ii), the words "January 1, 1985" and by adding in their place the words "January 1, 1986."

m. Removing, from the first sentence of paragraph (f)(6)(iv) *Answer 3* Ex. (1)(iii), the words "§1.150-13(d)(1)" and by adding in their place the words "§1.1502-13(d)(1)".

n. Removing, from the fourth sentence of paragraph (f)(6)(iv) *Answer 3* Ex. (2)(ii), the word "According" and by adding in its place the word "Accordingly".

o. Revising the first three sentences of paragraph (f)(6)(iv) *Answer 3* Ex. (3)(iii) to read as set forth below.

9. Paragraph (g)(2) is amended by—

a. Removing the colon from the first sentence of paragraph (g)(2) *Answer* (i).

b. Removing, from the heading of paragraph (g)(2) *Answer* (ii), the words "*in t*" and by adding in their place the words "*in T*".

c. Removing the colon from the end of paragraph (g)(2) *Answer* (v) and by adding in its place a period.

d. Removing, from the first sentence of paragraph (g)(2) *Answer* Ex. (2)(ii), the misspelled word "satisified" and by adding in its place the word "satisfied".

e. Removing from the sixth sentence of paragraph (g)(2) *Answer* Ex. (2)(ii), the word "than" and by adding in its place the word "then".

f. Removing, from the fourth sentence of paragraph (g)(2) *Answer* Ex. (6), the word "Acquisition" and by adding in its place the word "acquisition".

g. Removing, from the parenthetical at the end of the second sentence of paragraph (g)(2) *Answer* Ex. (7)(ii), the misspelled word "hypotheticl" and by adding in its place the word "hypothetical".

10. Paragraph (h) is amended by—

a. Removing, from the first sentence of paragraph (h)(2)(iii), the word "ASDP" and by adding in its place the word "ADSP".

b. Removing, from the first answer of paragraph (h)(3) *Answer 1* (i), the words "of all old" and by adding in their place the words "of all of old".

c. Removing, from the second sentence of paragraph (h)(3) *Answer 2* (i), the words "of P" and by adding in their place the words "to P".

d. Removing, from the third sentence of paragraph (h)(3) *Answer 2* (i), the words "or T" and by adding in their place the words "for T".

e. Removing, from the second sentence of paragraph (h)(3) *Answer 2* (iii), the words "that fact" and by adding in their place the words "the fact".

f. Removing, from the first sentence of paragraph (h)(3) *Answer 2* (iv), the words "gain an" and by adding in their place the words "gain on".

g. Removing, from the second sentence of paragraph (h)(3) *Answer 2* (vi)(B), the misspelled word "assests" and by adding in its place the word "assets".

h. Removing, from paragraph (h)(3) *Answer 2* (vi)(D), the words "of (section 1245 property)" and by adding in their place the words "of section 1245 property".

i. Removing, from the first line of the formula set out in paragraph (h)(3) *Answer 2* Ex. (1)(ii), the word "ANSP" and by adding in its place the word "ADSP".

j. Removing, from the formula set out in paragraph (h)(3) *Answer 2* Ex. (1)(ii), the words "ADSP = −.46ADSP = $51,816" and by adding in their place the words "ADSP − .46ADSP = $51,816".

k. Removing, from the second sentence of paragraph (h)(3) *Answer 2* Ex. (2), the misspelled word "aquisition" and by adding in its place the word "acquisition".

(l) Removing from the first line of the formula set out in paragraph (h)(3) *Answer 3* Ex. (ii) the letters "x x" and by adding in their place the letter "x".

(m) Removing, from the second sentence of paragraph (h)(3) *Answer 3* Ex. (iii) the words "*i.e.*, $189,422.71 × 1395348" and by adding in their place the words "*i.e.*, $189,422.71 × .1395348".

11. Paragraph (j) is amended by—

a. Removing so much of the first sentence of paragraph (j)(1) as ends after the word "determination" and before the word "new" and by adding in place of the removed language the words "of the total sum ("adjusted grossed-up basis") to be allocated as basis to the assets of".

b. Removing, from the formula set out in paragraph (j)(2) *Answer 4* Ex. (i), the words "ADSP = $75,000 + × $13,616 + (.028 × ADSP − $2,240" and by adding in their place the words "ADSP = $75,000 + $13,616 + (.028 × ADSP) − $2,240".

c. Removing, from paragraph (j)(2) *Answer 5* (ii)(C), the words "§1.338-1T(d)(1)(v)" and by adding in their place the words "§1.338-1T(d)(1)(v))".

12. Paragraph (k) is amended by—

a. Removing, from paragraph (k)(1) *Question 1*, the word "liquidation" and by adding in its place the word "liquidations".

b. Removing, from the end of the third sentence of paragraph (k)(1) *Answer 3* (i), the words "("hypothetical distribution")".

c. Removing the fourth sentence of paragraph (k)(1) *Answer 3* (i) and by adding in its place the following sentence: "However, if section 332 would have applied to a distribution of all of T's assets in a hypothetical complete liquidation immediately after the plan of complete liquidation was adopted, then section 337(c)(2) will apply to bar the operation of section 337 through section 338(h)(12) unless each corporation that would have been a distributee corporation (within the meaning of section 337(c)(3)(B)(i)) with respect to that hypothetical liquidation also is completely liquidated under the circumstances described in section 337(c)(3)."

d. Removing, from the second sentence of paragraph (k)(1) *Answer 3* (ii), the word "applied"and by adding in its place the word "applies".

e. Removing, from paragraph (k)(1) *Question 4* (ii), the words "a causes T" and by adding in their place the words "A causes T".

13. Paragraph (l)(1) *Question* is amended by removing the words "new tax" and by adding in their place the word "tax".

§1.338-4T Questions and answers relating to miscellaneous issues under section 338 (temporary).

* * * * *

(f) ***Application of the asset consistency rule of section 338(e)***—(1) * * *

* * * * *

(5) ***Certain transactions excepted under section 338(e)(2)(D).***

Question: * * *

Answer: (i) * * *

* * * * *

(vii) *Property subject to timely disposition*— (A) *General rule*. The acquisition of property is subject to an exception to section 338(e)(1) under the authority of section 338(e)(2)(D) if, on or before the required disposition date, (*1*) the P group disposes of that property to an unrelated person that is not a target affiliate of T or of an affected target or (*2*) the P group member holding the property ceases to be a member of the P group and ceases to be related to any member of the P group. A P group member is not treated as ceasing to be a member of the P group for purposes of this subdivision (A) if it ceases to exist by reason of a transaction described in section 381(a) and if the acquiring corporation (within the meaning of section 381(a)) is a member of the P group.

(B) *Requiring disposition date*. The "required disposition date" is the latest of the following three dates: (*1*) March 15, 1986, (*2*) the 90th day after the date on which a P group member acquires the property, or (*3*) the 90th day after the acquisition date of T.

* * * * *

(6) *Carryover basis election exception under section 338(e)(2)(D) and (i)*—(i) *Introduction*—(A) *Overview*. If P makes a qualified stock purchase of T stock and, in lieu of an express election, makes a protective carryover basis election for T under this paragraph (f)(6) ("protective carryover election"), then a tainted asset acquisition with respect to T or any affected target will in no case cause a deemed election under section 338(e)(1) for T or any affected target. A "tainted asset acquisition" occurs with respect to T (or with respect to an affected target) if an express election is not made and if, during the consistency period of T (or of the affected target), P group member acquires an asset of T or its target affiliate (or of the affected target or its target affiliate) in an acquisition that is described in section 338(e)(1) and that is not subject to an exception (other than the carryover basis election exception of this paragraph (f)(6)) to section 338(e)(1). The protective carryover election is irrevocable and bars an express election for T and the affected targets. If the P group makes a tainted asset acquisition but does not make a protective carryover election for T, then the tainted asset acquisition will cause a carryover basis election by affirmative action ("affirmative action carryover election") as of the later of the day of the tainted asset acquisition

or the expiration of the period within which to make the protective carryover election for T. Pursuant to paragraph (f)(1)(ii) *Answer 1* of this section, however, the District Director in appropriate cases may cause a deemed election under section 338(e)(1) in lieu of the otherwise applicable affirmative action carryover election. Thus, the only certain way for the P group to avoid a deemed election under section 338(e)(1) in the event of the tainted asset acquisition is to make a timely protective carryover election. Apart from the District Director's authority to override an affirmative action carryover election and impose a deemed election under section 338(e)(1) in lieu thereof, the consequences of a protective carryover election and an affirmative action carryover election are identical, except that an offset prohibition election under this paragraph (f)(6) and the special increase in basis of transferee member stock under paragraph (f)(6)(iv) *Answer 1* (i)(B) of this section are available only if a *protective* carryover election is made. (For a special limitation on the application of the offset prohibition election, see §1.338-5T(d)(1).) Unless otherwise indicated, any reference in this section to the carryover basis election exception of this paragraph (f)(6) is a reference to either the protective carryover election or the affirmative action carryover election.

* * * * *

(ii) *Procedure for making protective carryover election and affirmative action carryover election.*

Question 1: * * *

Answer 1: (i) * * *

(ii) *Corporations required to join in making protective carryover election*—(A) *General rule.* Subject to two exceptions, each corporation included in the P group at any time during so much of T's consistency period as ends on the day the protective carryover election statement is filed is required to join in making the protective carryover election.

(B) *Exception for certain prior P group members.* A corporation that ceases to be a P group member prior to the day on which the protective carryover election statement is filed is not required to join in making the protective carryover election if it did not make a tainted asset acquisition while a member of the P group. (Caution should be exercised when relying on this exception, since it is not always clear whether an asset acquisition is a tainted asset acquisition.)

(C) *Certain foreign P group members.* A foreign P group member is not required to join in making the protective carryover election if (*1*) it is subject to United States tax (within the meaning of §1.338-1T(k)(2)(v)) for its taxable year in which the protective carryover election statement is filed or for any prior taxable year any day of which occurs during the consistency period, (*2*) it purchases any of the stock included in the qualified stock purchase of T or of an affected target, or (*3*) it directly or indirectly (in the manner described in section 958(a)) holds stock in a foreign P group member that satisfies one or both of the two preceding conditions. A foreign P group member that is not required to join in making the protective carryover election ("nonjoining member") nonetheless must be identified in that election as if it were so required (such as by a footnote system). In addition, tainted asset acquisitions by a nonjoining member shall be treated as asset acquisitions subject to an affirmative action carryover election unless that member actually joins in making the election, *i.e.*, unless a representative of that member signs the election on that member's behalf. The District Director shall not have authority, however, to impose a deemed election under section 338(e)(1) in the event of a tainted asset acquisition by a nonjoining member that is treated as subject to an affirmative action carryover basis election pursuant to the preceding sentence.

(D) *U.S. shareholders of CFC P group member may act on its behalf.* A P group member that is a controlled foreign corporation will be considered to have joined in making the protective carryover election if its U.S. shareholders sign the protective carryover election statement in its behalf. For purposes of this subdivision (D), the principles of §1.338-1T(k)(4) (section 338 election made by U.S. shareholders) apply.

(iii) *Contents of protective carryover election statement*—(A) * * *

* * * * *

(C) *Schedule of information relating to corporations subject to protective carryover election.* A schedule providing the information specified in this subdivision (C) ("required data") must be attached to the protective carryover election statement. Failure to attach the schedule, however, will not invalidate the protective carryover election. The schedule must satisfy the following requirements:

(*1*) It must contain the name, address, and employer identification number (if any) of, and (for a foreign corporation) the country (and further political subdivision, if relevant) under the laws of which is organized, each corporation that, as of the day the protective carryover election statement is filed, is an affected target ("includible affected target").

(*2*) It must disclose the fair market value of the consideration paid by the purchasing corporation for the stock of each directly acquired target, *i.e.*, the original target and each includible affected target (other than an includible affected target for which a qualified stock purchase would occur solely by reason of section 338(a)(2) and (h)(3)(B)).

(*3*) It must identify the portion of the consideration paid for the stock of each directly acquired target that is represented by cash, purchase money debt, and other components of consideration (with each such other component separately stated).

(*4*) It must be disclose the liabilities of the original target and each includible affected target (whether or not a directly acquired target) as of the close of the acquisition date (or as of the close of the day that would be the acquisition date if an express election were made).

* * * * *

(iv) *Consequences of protective or affirmative action carryover election.*

Question 1: * * *

* * * * *

Answer 2: (i) * * *

(ii) *Exception if INA acquisition is subject to offset prohibition election*—(A) * * *

(B) *Limitation on application of certain credits.* For purposes of determining the amount of a restricted credit permitted as a credit against N's tax liability for N's taxable year in which there is INA gain subject to the offset prohibition, N's pre-credit tax liability is calculated as if that INA gain were not income to N. "Restricted credits" are credits against tax described in part IV (other than subparts A and C thereof and section 27(a)) of subchapter A of chapter 1 of the Code (*i.e.*, sections 27(b), and 28-30, and 38-41). For a separate restriction applicable to the foreign tax credit and for a special rule coordinating that restriction with this subdivision (B), see §1.338-5T(d)(2).

* * * * *

Answer 3: (i) * * *

* * * * *

(iv) *Limitations if C ceases to be a member and offset prohibition election applies*—(A) *In general.* * * *

* * * * *

(D) *Liitation on application of certain credits.* For purposes of determining the amount of a restricted credit permitted as a credit against the P group's consolidated tax liability for a taxable year in which there is a remaining ICA gain amount subject to the offset prohibition, the P group's pre-credit consolidated tax liability is calculated as if that remaining ICA gain amount were not income to the P group. "Restricted credits" are credits against tax described in part IV (other than subparts A and C thereof and section 27(a)) of subchapter A of chapter 1 of the Code (*i.e.*, sections 27(b), 28-30, and 38-41). For a separate restriction applicable to the foreign tax credit and for a special rule coordinating that restriction with this subdivision (D), see §1.338-5T(d)(2).

* * * * *

Example (1). * * *

* * * * *

Example (3). (i) * * *

* * * * *

(iii) Second, for purposes of determining the amount of any restricted credit (as defined in subdivision (iv)(D) of this *Answer 3*) permitted as a credit against the P group's consolidated tax liability for 1987, the pre-credit consolidated tax liability is calculated as if the remaining ICA gain amount of $4,500 were not income to the P group for 1987. Under these facts, the P group has no income (and therefore no pre-credit tax liability) in 1987 absent the remaining ICA gain amount. Thus, the P group's 1987 tax liability may not be reduced by restricted credits.

* * * * *

Par. 5. Section 1.338(h)(10)-1T is amended as follows—

1. Paragraph (d)(3) is amended by removing "§1.338-1T(e)(1)(i)(D)" and by adding in its place "§1.338-1T(e)(1)(i)(E)".

2. Paragraph (d)(4) is amended by removing "§1.338-1T(e)(2)(i)" and by adding in its place "§1.338-1T(e)(2)(v)(A)".

PART 602 OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 6. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 7. Section 602.101(c) is amended by inserting in the appropriate place in the table "1.338-5T . . . 1545-0702".

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitations of subsection (d) of that section.

This Treasury decision is issued under the authority contained in sections 338 and 7805 of the Internal Revenue Code of 1954 (26 U.S.C. 338 and 7805, respectively).

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved January 21, 1986.

J. ROGER MENTZ,
Acting Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on February 6, 1986, 4:57 p.m., and published in the issue of the Federal Register for February 12, 1986, 51 F.R. 5163. Corrected in the issues of the Federal Register for February 21, 1986, 51 F.R. 6219 and April 1, 1986, 51 F.R. 11016).

Section 382.—Special Limitations on Net Operating Loss Carryover

26 CFR 1.382(b)-1: Change of ownership as the result of a reorganization.

Carryover; reorganization; merger; controlled corporations. A loss corporation *X* formed a wholly owned subsidiary *P* which formed a wholly owned subsidiary *S*. *S* then merged into *X* in a reorganization under sections 368(a)(1)(A) and 368(a)(2)(E) of the Code, with the former *X* shareholders owning *P* stock with a fair market value exceeding 20 percent of the fair market value of the outstanding *X* stock. *X*'s net operating loss carryover is not reduced under section 382(b) before amendment by section 806(e) of the Tax Reform Act of 1976.

Rev. Rul. 86-52

ISSUE

Is the net operating loss carryover of the acquiring corporation reduced under section 382(b) of the Internal Revenue Code, before amendment by section 806(e) of the Tax Reform Act of 1976, 1976-3 (Vol. 1) C.B. 1, 75 (the Act), in the reverse triangular organization described below?

FACTS

X, a corporation engaged in an ongoing business, had common stock that was publicly traded. *X* had net operating loss carryovers. In order to form a holding company structure, *X* caused *P* corporation to be organized. Shortly thereafter, *P* organized a wholly owned subsidiary, *S*, which in 1977 merged into *X* in a transaction qualifying as a reorganization described in sections 368(a)(1)(A) and 368(a)(2)(E) of the Code. *X* acquired all of the assets of *S*. As a newly formed corporation, *S* had no liabilities to be assumed by *X*. Thereafter, the separate corporate existence of *S* ceased and *X* survived the merger. Except for dissenters to the merger, each share of the outstanding stock of *X* was converted into three shares of *P* common stock, and *X*'s outstanding stock certificates thereafter represented shares of *P* common stock. The shares of *S* stock outstanding immediately prior to the merger were cancelled in the merger. For each share of *S* stock held by *P* prior to the merger, 10 shares of new *X* common stock were issued to *P* in the merger. As a result of the reorganization, the former *X* shareholders owned all the outstanding *P* stock and *P* owned all the outstanding *X* stock. The fair market value of the *P* stock, immediately after the reorganization, was equal to the then fair market value of the *X* stock.

LAW AND ANALYSIS

Section 382(b)(1) of the Code, before amendment by the Act (old section 382), provided in part that if, in the case of a reorganization described in section 368(a)(1)(A), the transferor corporation or acquiring corporation has a net operating loss which is a net operating loss carryover to the first taxable year of the acquiring corporation ending after the date of the transfer, and the stockholders (immediately before the reorganization) of such corporation (loss corporation), as the result of owning stock of the loss corporation, own (immediately after the reorganization), less than 20 percent of the fair market value of the outstanding stock of the acquiring corporation, the total net operating loss carryover shall be reduced.

Old section 382(b)(6) of the Code provides in part that if the stockholders of the loss corporation (immediately before the reorganization) own, as a result of the reorganization, stock in a corporation controlling the acquiring corporation, such stock of the controlling corporation shall, for purposes of old section 382(b), be treated as stock of the acquiring corporation in an amount valued at an equivalent fair market value. *X* is the loss corporation and also, because it acquired *S*, the acquiring corporation.

Under old section 382(b)(1) of the Code, if the former stockholders of *X*, as a result of owning stock of *X*, own (immediately after the reorganization), less than 20 percent of the fair market value of the outstanding stock of *X*, the acquiring corporation, *X*'s net operating loss carryover would be reduced. The stockholders of *X* own none of the outstanding stock of *X* after the reorganization, because the former shareholders of *X*, as a result of the reorganization, own stock in *P*. However, because *P* controls *X*, the acquiring corporation, the former *X* shareholders will be treated under old section 382(b)(6) as owning, after the reorganization, stock of *X* in an amount equivalent to the fair market value of the stock of *P* that they hold.

HOLDING

Because the fair market value of the *P* stock the former *X* shareholders own as a result of the reorganization exceeds 20 percent of the fair market value of the outstanding *X* stock, *X*'s net operating loss carryover is not reduced by old section 382(b)(1) of the Code.

Section 404.—Deductions for Contributions of an Employer to an Employees' Trust or Annuity Plan and Compensation under a Deferred-Payment Plan

Deductibility of deferred vacation benefits. See Rev. Proc. 86-20, page 50.

Section 463.—Accrual of Vacation Pay

Deductibility of deferred vacation benefits. See Rev. Proc. 86-20, page 50.

Section 4941.—Taxes on Self-Dealing

26 CFR 53.4941(d)-4: Transitional rules.
(Also Section 4943, 53.4943-1.)

Private foundations; self-dealing, sale to disqualified person. The sale to a disqualified person of stock by a private foundation owned by it continuously since May 26, 1969, but not constituting excess business holdings on that date, is excepted under section 53.4941(d)-4(b)(1) of the regulations from the prohibition against self-dealing under section 4941 of the Code.

Rev. Rul. 86-53

ISSUE

Under the circumstances described below, would the sale to a disqualified person of stock owned by a private foundation continuously since May 26, 1969, but not constituting excess business holdings on that date, be excepted under section 53.4941(d)-4(b)(1) of the Foundation and Similar Excise Tax Regulations from the prohibition against self-dealing under section 4941 of the Internal Revenue Code?

FACTS

The foundation is exempt from federal income tax under section 501(c)(3) of the Code and is a private foundation within the meaning of section 509(a). Since May 26, 1969, the foundation and its disqualified persons, within the meaning of section 4946(a), have at all times owned 100% of the outstanding stock of *M*, a profit-making corporation. During this period of time, the number of shares of *M* stock actually owned by the foundation and the percentage interest of *M* represented by such shares have remained unchanged. *M* has been engaged primarily in the business of leasing real property to *N*, also a profit-making corporation, since May 26, 1969.

N is also a disqualified person with respect to the foundation.

In each of its taxable years prior to 1985, 95 percent or more of *M*'s income consisted of rents from real property as described in section 512(b)(3) of the Code, and during such years *M* was excepted from classification as a "business enterprise" by reason of section 4943(d)(3)(B) of the Code. In 1985, less than 95 percent of *M*'s gross income was derived from real property rentals. The remainder of *M*'s gross income was derived from the leasing of tangible personal property, consisting of commercial and industrial equipment, to unrelated third parties.

Accordingly, in 1985, *M* was no longer excluded from classification as a business enterprise for purposes of section 4943 of the Code. Therefore, the foundation's stock ownership in *M* became an excess business holding subject to tax under section 4943. In order not to be liable for such tax, the foundation proposes to sell all its stock to *N* for an amount equal to its fair market value in a transaction that will not constitute a prohibited transaction within the meaning of section 503(b).

LAW AND ANALYSIS

Section 4941 of the Code imposes a tax on each act of self-dealing between a disqualified person and a private foundation.

Section 4941(d)(1)(A) of the Code defines the term "self-dealing" to include any direct or indirect sale or exchange of property between a private foundation and a disqualified person.

Section 4943(a)(1) of the Code provides for a tax on the excess business holdings of a private foundation equal to 5 percent of the value of such holdings.

Section 4943(c)(1) of the Code provides that the term "excess business holdings" means the amount of stock or other interest in a business enterprise that the foundation would have to dispose of to a person other than a disqualified person for its remaining holdings to be "permitted holdings."

Section 4943(d)(3) of the Code provides that the term "business enterprise" does not include a trade or business at least 95 percent of the gross income of which is derived from "passive sources." Gross income from passive sources includes items excluded by section 512(b)(3).

Section 512(b)(3) of the Code excludes from the definition of the term "unrelated business taxable income" rents from real property. Section 512(b)(3) does not exclude rents from personal property unless leased with and incidental to real property such that less than 50 percent of the total rent is attributable to the personal property.

Section 101(l)(2)(B) of the Tax Reform Act of 1969, P.L. 91-172, 1969-3 C.B. 35, and section 53.4941(d)-4(b)(1) of the regulations provide that section 4941 of the code shall not apply to the sale, exchange, or other disposition of property owned by a private foundation on May 26, 1969, to a disqualified person if the private foundation is required to dispose of such property in order not to be liable for the excess business holdings tax under section 4943 and if the private foundation receives in return an amount which equals or exceeds the fair market value of the property in a transaction that is not a prohibited transaction within the meaning of section 503(b).

Section 53.4941(d)-4(b)(1) of the regulations provides that the determination of whether a private foundation is required to dispose of property in order not to be liable for tax under section 4943 of the Code is to be made without regard to section 4943(c)(2)(C) (relating to the 2 percent *de minimis* rule) and as if every disposition by the foundation were made to a disqualified person.

But for the exception of section 101(l)(2)(B) of the Tax Reform Act of 1969 and section 53.4941(d)-4(b)(1) of the regulations, a sale by the foundation to *N* would constitute self-dealing within the meaning of section 4941(d)(1)(A) of the Code since it would be a direct sale of property by a private foundation to a disqualified person.

The foundation's stock in *M* is clearly property owned by a private foundation on May 26, 1969. Such stock has been owned by the foundation at all times since May 26, 1969, and will be owned until its proposed sale to *N*. Moreover, the proposed disposition is being made in order to avoid liability for tax under section 4943, and the foundation is receiving in return an amount that is not less than the fair market value of the *M* stock being sold to *N*. Thus, the basic requirements for application of section 101(l)(2)(B) of the Tax Reform Act and section 53.4941(d)-4(b)(1) of the regulations appear to be present.

Under these circumstances, the issue is whether, for purposes of the exception to self-dealing provided by section 101(l)(2)(B) of the Tax Reform Act of 1969 and section 53.4941(d)-4(b)(1) of the regulations, the stock owned by the foundation on May 26, 1969, must have been in an entity that, as of such date, constituted a "business enterprise" within the meaning of section 4943(d)(3) of the Code. Sections 101(l)(2)(B) and 53.4941(d)-4(b)(1) do not specifically require that the property owned by a private foundation on May 26, 1969, must have been a holding in a "business enterprise" on that date. These provisions only require that the "property" being disposed of must have been held by a private foundation on May 26, 1969, and must be sold or otherwise disposed of in order not to be liable for tax under section 4943.

Therefore, in this case, the proposed sale of stock by the foundation to *N*, is disqualified person, would be excepted from the provisions of section 4941 of the Code and the disqualified person would not be subject to the self-dealing tax imposed by section 4941.

Since the holdings of the private foundation and its disqualified persons are aggregated in determining the private foundation's excess business holdings position, if any portion of the holdings is sold to its disqualified persons, it would remain in an excess business holdings position for purposes of section 53.4941(d)-4(b)(1) of the regulations until the last scintilla of such holdings is sold. Therefore, the entire holdings of the private foundation in *M* are treated as excess business holdings and may be disposed of under the exception to self-dealing under section 4941 of the Code provided under section 53.4941(d)-4(b)(1). See also Rev. Rul. 75-25, 1975-1 C.B. 359.

HOLDING

Under the circumstances described above, the sale to a disqualified person of stock owned by a private foundation continuously since May 26, 1969, but not constituting an interest in a business enterprise as of such date, is excepted under section 53.4941(d)-4(b)(1) of the regulations from the prohibition against self-dealing under section 4941 of the Code, if the disposition is made in order to avoid the presence of excess business holdings under section 4943.

Section 4943.—Taxes on Excess Business Holdings

26 CFR 53.4943-1: General rule; purpose.

Whether the sale to a disqualified person of stock owned by a private foundation continuously since May 26, 1969, but not constituting excess business holdings under section 4943 of the Code on that date, is excepted from the prohibition against self-dealing under section 4941, if the sale is made to avoid the presence of excess business holdings under section 4943. See Rev. Rul. 86-53, page 43.

Section 6107.—Income Tax Return Preparer Must Furnish Copy of Return to Taxpayer and Must Retain a Copy or List

26 CFR 1.6107-1: Income tax return preparer must furnish copy of return to taxpayer and must retain a copy or list.

Whether a person in a business other than tax return preparation who fills out or reviews income tax returns for its customers may be subject to the penalties imposed under section 6107 of the Code. See Rev. Rul. 86-55, page 47.

Section 6109.—Identifying Numbers

26 CFR 1.6109-2: Furnishing identifying number of income tax return preparer.

Whether a person in a business other than tax return preparation who fills out or reviews income tax returns for its customers may be subject to the penalties imposed under section 6109 of the Code. See Rev. Rul. 86-55, page 47.

Section 6166.—Extension of Time for Payment of Estate Tax Where Estate Consists Largely of Interest in Closely Held Business

26 CFR 20.6166-1: Election of alternate extension of time for payment of estate tax where estate consists largely of interest in closely held business.

(Also Section 303, 1.303-2.)

Installment method; closely-held business; stock redemption. An explanation is provided of the application of sections 303 and 6166 of the Code when shares of stock are redeemed and an election to pay the estate tax in installments is made. Rev. Rul. 72-188 modified.

Rev. Rul. 86-54

ISSUE

In the situation described below, do the redemptions of stock that qualify under section 303 of the Internal Revenue Code constitute distributions or withdrawals for purposes of the acceleration rule of section 6166(g)? Specifically, is section 6166(g)(1)(B), which excludes certain section 303 redemptions from the application of the acceleration rule, to be applied on a "redemption-by-redemption" basis (under which the amount of each section 303 redemption must not exceed the amount of federal estate taxes paid during the "permitted period") or on a "cumulative" basis (under which the total cumulative amount of the current redemption and all prior section 303 redemptions must not exceed the total cumulative amount of all federal estate taxes paid on or before the close of the "permitted period")?

FACTS

D, a citizen of the United States, died in April 1977. Under the terms of *D*'s will, the executors are required to pay the taxes and expenses described in section 303(a) of the Code. A Federal Estate Tax Return, Form 706, was timely filed on January 12, 1978. *D*'s gross estate included an interest in *X* corporation that comprised more than 65% of the adjusted gross estate. Under the then-applicable version of section 6166(a), the interest in *X* qualified as a closely held business interest. Pursuant to section 6166, *D*'s executors elected to pay $1,480*x* of the federal estate tax liability in installments, using the 5-year deferral permitted by section 6166(a)(3). The first installment payment became due on January 12, 1983.

D's executors filed the federal estate tax return and paid nondeferred estate tax of $460*x* on January 12, 1978, when the federal estate tax return was filed. On February 11, 1980, the estate paid state death tax of $320*x*. Beginning on January 12, 1979, and continuing throughout the deferral period, the estate made payments of interest in varying amounts with respect to the deferred federal estate tax. The estate made installment payments of deferred tax beginning on January 12, 1983.

X made a series of redemptions of stock from *D*'s estate as set forth below. Each of the redemptions qualified for treatment as a distribution in full payment in exchange for the stock so redeemed under section 303(a) of the Code.

The series of section 303 redemptions and tax payments are as follows:

Redemption		*Cumulative*	*Payments*			*Cumulative Federal*
Date	*Amount*	*Redemptions*	*Date*	*Nature of Payment*	*Amount*	*Estate Tax Payments*
			1/12/78	Federal Tax	$460x	$460x
1) 1/14/78	$460x	$ 460x	1/12/79	Interest	$ 8x	$468x
		$ 460x	1/12/80	Interest	$ 10x	$478x
2) 2/11/80	$320x	$ 780x	2/11/80	State Tax	$320x	$478x
		$ 780x	1/12/81	Interest	$ 16x	$494x
3) 1/12/82	$ 26x	$ 806x	1/12/82	Interest	$ 28x	$522x
4) 1/12/83	$150x	$ 956x	1/12/83	Installment	$150x	$672x
5) 1/11/84	$150x	$1106x	1/12/84	Installment	$150x	$822x
6) 1/11/85	$150x	$1256x	1/12/85	Installment	$150x	$972

LAW AND ANALYSIS

The Tax Reform Act of 1976, section 2004(a), 1976-3 (Vol. 1) C.B. 1, 338, enacted section 6166 of the Code effective for estates of decedents dying after 1976.

Section 6166(a)(1) of the Code provides that, if the value of an interest is a closely held business that is included in determining the gross estate of a decedent who was (at the date of his death) a citizen or resident of the United States exceeds 35 percent of the adjusted gross estate (65 percent for decedents dying before January 1, 1982), then the executor may elect to pay part or all of the estate tax in 2 or more (but not exceeding 10) equal installments. Generally, under section 6166(a)(2), only the amount of estate tax attributable to the value of the closely held business interest may be paid in installments.

For estates of decedents dying after December 31, 1981, section 6166(g)(1)(A) of the Code (the acceleration rule) provides that the privilege of paying the estate tax in installments ceases and the unpaid tax becomes due immediately, if the sum of (i) the amount of the decedent's closely held business interest that is distributed, sold, exchanged, or otherwise disposed of, and (ii) the amount of withdrawals from the trade or business, exceeds 50 percent of the value of the decedent's interest in the business. For estates of decedents dying on or before December 31, 1981, and after December 31, 1976, the installment privilege ceases to apply if (i) one-third or more in value of the decedent's closely held business interest is distributed, sold, exchanged, or otherwise disposed of, or (ii) the aggregate withdrawals of money and other property from the closely-held business with respect to the decedent's interest, equal or exceed one-third of the value of such trade or business.

Section 6166(g)(1)(B) of the Code, as in effect for estates of decedents dying after 1976 and before 1982, provided:

> (B) In the case of a distribution in redemption of stock to which section 303 (or so much of section 304 as relates to section 303) applies—
>
> > (i) [the acceleration of payment provision for dispositions] does not apply with respect to the stock redeemed; and for purposes of such subparagraph the interest in the closely held business shall be considered to be such interest re-

duced by the value of the stock redeemed, and

(ii) [the acceleration of payment provision for withdrawals] does not apply with respect to withdrawals of money and other property distributed; and for purposes of such subparagraph the value of the trade or business shall be considered to be such value reduced by the amount of money and other property distributed.

This subparagraph shall apply only if, on or before the date prescribed by section 6166(a)(3) for the payment of the first installment which becomes due after the date of the distribution (or, if earlier, on or before the day which is 1 year after the date of the distribution), there is paid an amount of the tax imposed by section 2001 not less than the amount of money and other property distributed.

The general rule under section 6166(g)(1)(A) of the Code is that the decedent's estate may continue paying the estate tax in installments if the aggregate of dispositions and withdrawals does not exceed a specified portion of the value of the decedent's closely held interest. If the aggregate of dispositions and withdrawals exceeds the limitation of section 6166(g)(1)(A), the unpaid tax is "accelerated" and becomes payable. However, section 6166(g)(1)(B) provides a limited exception to this acceleration rule for certain qualifying section 303 redemptions of stock. This exception only applies if by the date of the first installment payment of tax due after the distribution or, if earlier, one year from the date of the distribution, a payment of the estate tax is made that is at least equal to the total amount of money and other property distributed in the section 303 redemption. Payment of interest on the estate tax qualifies as a payment of estate tax for purposes of section 6166. *See* sections 6601(e)(1) and 6601(j). A state death tax payment that is creditable against the federal estate tax is not equivalent to the payment of federal estate tax for purposes of section 6166(g). *See* Rev. Rul. 85-43, 1985-1 C.B. 356.

The matching of the redemption amounts with the estate tax payments as required by section 6166(g)(1)(B) of the Code is discussed in Rev. Rul. 72-188, 1972-1 C.B. 383. That ruling adopts a "cumulative" method of applying section 6166(g)(1)(B). The cumulative method requires a comparison of the cumulative estate tax payments with the cumulative section 303 redemptions; only to the extent that cumulative redemptions exceed cumulative estate tax payments is there an amount not within the section 6166(g)(1)(B) exception to the acceleration rules.

An alternative approach to section 6166(g)(1)(B) of the Code is suggested by regulations interpreting language in now repealed section 6166A of the Code that was identical to the flush language in section 6166(g)(1)(B). Section 20.6166A-3(d)(2) of the Estate Tax Regulations provides, in part, that the exclusion for a section 303 redemption does not apply unless *after* the redemption, but on or before the date prescribed for payment of the first installment that becomes due after the redemption, there is paid an amount of estate tax not less than the amount of money or other property distributed. If there is a series of section 303 redemptions, each redemption is treated separately, and the failure of one redemption to qualify does not necessarily mean that another redemption does not qualify. This method can be characterized as a "redemption-by-redemption" approach.

Thus, under the section 6166A regulations a section 303 redemption qualifies for the exclusion from the acceleration rule if after the redemption and within the permitted period there is paid estate tax not less than the amount of the section 303 redemption. These regulations state that each redemption in a series of redemptions is to be treated separately. Because of the identity of the flush language in section 6166(g)(1)(B) of the Code and former section 6166A(g)(1)(B), the rule in section 20.6166A-3(d)(2) of the regulations is relevant to section 6166 as well as to former section 6166A.

Neither the redemption-by-redemption approach nor the cumulative approach is totally satisfactory to achieve the primary purpose of section 6166 of the Code making it possible to keep together a business enterprise after the death of one of the owners results in the imposition of estate tax. H.R. Rep. No. 2198, 85th Cong., 2d Sess. 7 (1958), 1959-2 C.B. 709, 713. Congress extended the period during which section 303 redemptions are permitted, in order to more closely correlate the rules of section 303 and section 6166 to allow the corporation to use earnings generated throughout the installment payment period for stock redemptions to pay the deferred federal estate tax. H.R. Rep. No. 94-1380, 94th Cong., 2d Sess. 34 (1976) 1976-3 (Vol. 3) C.B. 735, 769-770. Reliance solely on the cumulative method in applying section 6166(g)(1)(B) can produce a result inconsistent with the extension of the period for making redemptions under section 303. A redemption that qualifies under section 303 but does not satisfy the cumulative method may preclude applicability of section 6166(g)(1)(B) to later redemptions, even though such succeeding redemption is followed within the permitted period by the payment of federal estate tax not less than the amount of the redemption. Similarly, in the case of redemptions made on or before the fourth anniversary of the decedent's death, exclusive reliance on the redemption-by-redemption approach can cause acceleration of the deferred tax if nondeferred estate tax payments are made before any section 303 redemptions. In such a situation, one or more of the redemptions might exceed the amount of estate tax paid within the permitted period with the result that the redemption or redemptions in excess of estate tax paid within the permitted period would not be within the section 6166(g)(1)(B) exclusion and would count against the limitation of section 6166(g)(1)(A).

The Internal Revenue Service has reconsidered Rev. Rul. 72-188 and, in light of the Congressional intent behind sections 303 and 6166 of the Code, will permit the cumulative approach and the redemption-by-redemption approach to be used interchangeably. Estates, therefore, may qualify for the exclusion under section 6166(g)(1)(B) if a section 303 redemption (or each of a series of redemptions) qualifies under either approach.

HOLDING

The exclusion in section 6166(g)(1)(B) of the Code applies to a section 303 redemption (the redemption) if (1) the cumulative amount of section 303 redemptions, as of the date of the redemption, is less than or equal to the total amount of estate tax payments as of the due date of the following estate tax payment (or, if earlier, the date which is 1 year after the distribution pursuant to the redemption), or (2) the amount of the redemption is less than or equal to the amount of the estate tax payments made within the permitted period.

Thus, in the situation described above, all of the redemptions of stock under section 303 of the Code are entitled to the exclusion from treatment as a distribution or withdrawal provided by section 6166(g)(1)(B) except that with regard to redemption 2) (the $320x redemption made on 2/11/80), only $34x (the sum of the 1/12/79, 1/12/80, and 1/12/81 interest payments, which are all made on or before the close of the permitted period) is entitled to the exclusion. Redemption 1) qualifies under the cumulative method, redemption 2) qualifies, in part, under the cumulative method, and redemptions 3)-6) qualify under the redemption-by-redemption method.

Because the relevant parts of the acceleration rules have not been amended, this holding applies to all versions of section 6166 and 6166A since the original enactment in 1958.

EFFECT ON OTHER RULINGS

Rev. Rul. 72-188 is modified.

Section 6694.—Understatement of Taxpayer's Liability by Income Tax Return Preparer

26 CFR 1.6694-1: Understatement of taxpayer's liability by income tax return preparer.

Whether a person in a business other than tax return preparation who fills out or reviews income tax returns for its customers may be subject to the penalties imposed under section 6694 of the Code. See Rev. Rul. 86-55, this page.

Section 6695.—Other Assessable Penalties with Respect to the Preparation of Income Tax Returns

26 CFR 1.6695-1: Other assessable penalties with respect to the preparation of income tax returns.

Whether a person in a business other than tax return preparation who fills out or reviews income tax returns for its customers may be subject to the penalties imposed under section 6695 of the Code. See Rev. Rul. 86-55, this page.

Section 7216.—Disclosure or Use of Information by Preparers of Income Tax Returns

26 CFR 301.7216-1: Penalty for disclosure or use of information by preparers of income tax returns.

Whether a person in a business other than tax return preparation who fills out or reviews income tax returns for its customers may be subject to the criminal penalties imposed under section 7216 of the Code. See Rev. Rul. 86-55, below.

Section 7701.—Definitions

26 CFR 301.7701-15: Income tax return preparer.
(Also Sections 6107, 6109, 6694, 6695, 7216; 1.6107-1, 1.6109-2, 1.6694-1, 1.6695-1, 301.7216-1.)

Return preparers; potential penalties; invalid assignment of refund checks. A person in a business other than tax return preparation who fills out or reviews income tax returns for its customers may be an income tax return preparer under section 7701(a)(36) of the Code and subject to potential penalties. The assignment of the customers' refund checks before the returns are processed by the Service is not a valid assignment and the Service may mail the checks directly to the taxpayers.

Rev. Rul. 86-55

ISSUE 1

In the situations described below, if a person in a business other than tax return preparation fills out or reviews income tax returns for the person's customers without charging a separate fee, is the person an income tax return preparer under section 7701(a)(36) of the Internal Revenue Code?

ISSUE 2

If such person is an income tax preparer, then what requirements and potential penalties apply to that person under the Internal Revenue Code?

ISSUE 3

If, under state law, a taxpayer attempts to assign to another person an income tax refund that the taxpayer expects to receive and if the address of that other person is shown on the taxpayer's return as the taxpayer's address, must the Internal Revenue Service send any refund check to that address?

FACTS

Situation 1. X, a used car dealer, advertises that it will fill out and review income tax returns and that any resulting refund will be applied as a down payment on a used car. These services are available to those who purchase a vehicle. *X* or *X*'s employee then either fills out a complete return or reviews a return prepared by the customer for both substantive correctness and mechanical accuracy. *X* does not charge its customers a separate fee for these services. The customer executes a power of attorney authorizing *X* to receive and endorse or negotiate the refund check. The address of *X* is substituted for that of the customer on the return. When *X* receives the customer's refund check, *X* endorses it and applies it as a down payment.

Situation 2. Y is a firm that offers discounted cash payments for tax refunds. *Y* or *Y*'s employee either fills out a complete return or reviews a return prepared by the customer for both substantive correctness and mechanical accuracy. After the return is filled out or reviewed, *Y* pays the customer the amount of the refund requested on the return, less a discount typically equal to 20 to 40 percent of the refund amount requested. As in *situation 1*, the customer executes a power of attorney, and *Y*'s address is substituted on the return for that of the taxpayer. *Y* does not charge a separate fee for its services in filling out or reviewing the return. Upon receipt of the customer's refund check, *Y* endorses the customer's name on the back of the check and deposits it in *Y*'s account.

LAW AND ANALYSIS

ISSUE 1

Section 7701(a)(36)(A) of the Code defines an income tax return preparer as any person who prepares any return of tax, or any claim for refund of tax, imposed by subtitle A, for compensation, or any person who employs one or more persons to prepare such returns or claims for refund for compensation.

Section 301.7701-15(a) of the Regulations on Procedure and Administration provides the general rule that an income tax return preparer is any person who prepares for compensation, or who employs (or engages) one or more persons to prepare for compensation, other than for the person, all or a substantial portion of any return of tax under subtitle A of the Code or any claim for refund of tax under subtitle A.

Section 301.7701-15(a)(4) of the regulations provides that a person must prepare a return or claim for refund for compensation to be an income tax return preparer. A person who prepares a return or claim for refund for a taxpayer with no explicit or implicit statement for compensation is not a preparer.

In *Papermaster v. United States*, No. 79-C-710 (E.D. Wis., Apr. 21, 1980), *aff'd by unpublished order*, No. 80-1612 (7th Cir., June 25, 1982), an individual who was both an attorney and an accountant prepared a taxpayer's individual income tax return. He also prepared a return for a corporation in which the taxpayer was a shareholder. The attorney/accountant received compensation for preparing the corporation return, but was not separately compensated for preparing the taxpayer's individual return. The court held that he was an income tax return preparer under section 7701(a)(36) of the Code with respect to taxpayer's individual return. The court reasoned that he was offering the businessman a "package deal" for preparing the individual return; his compensation was included in the compensation for the corporate return.

In both *situations 1* and *2*, *X* and *Y* either fill out the entire return or review information on returns prepared by others. That action is preparation of the return for purposes of section 7701(a)(36) of the Code. *See* Rev. Rul. 84-3, 1984-1 C.B. 264.

In *situation 1*, although *X* does not charge the customers a separate fee for the preparation of their returns, *X* is offering its customers a "package deal." *X*'s compensation is included in the price of the cars required to be purchased by the customers. Similarly, in *situation 2*, *Y*'s compensation for filling out or reviewing the return is a part of, or is incident to, the various discount charges (ranging from 20 to 40 percent) that *Y* charges its customers for their refund checks.

ISSUE 2

Sections 6694(a) and 6694(b) of the Code provide that any person who is an income tax return preparer with respect to a return or claim for refund may be subject to a penalty if any part of an understatement of liability with respect to that return or claim is due to a negligent or intentional disregard of rules or regulations by that preparer, or if the understatement is due to a willful attempt by that preparer to understate the liability.

Under section 6107(a) of the Code, an income tax return preparer has an obligation to furnish a completed copy of the return to the taxpayer and may be penalized under section 6695(a) for failure to do so. Under section 6107(b), an income tax return preparer has an obligation to retain a copy of the return or a list of taxpayers for whom returns have been prepared and may be penalized under section 6695(d) for failure to do so. When one preparer employs or engages another, the responsibility for these acts falls on the employer. *See* section 1.6107-1(c)(1) of the Income Tax Regulations.

Section 6695(b) of the Code imposes an obligation to sign the return and imposes a penalty for failure to do so. Under section 1.6695-1(b)(2) of the regulations, this obligation falls on the individual preparer with primary responsibility for the overall substantive accuracy of the return.

Section 6109(a)(4) of the Code provides that any return or claim for refund prepared by an income tax return preparer shall bear such identifying number for securing proper identification of such preparer, such preparer's employer, or both, as may be prescribed.

Section 1.6109-2(a) of the regulations requires that a return prepared by an income tax return preparer shall bear the identifying number of the preparer required to sign the return or claim for refund. In addition, if there is a partnership or employment arrangement between two or more preparers the identifying number of the partnership or the person who employs (or engages) one or more other persons to prepare for compensation the return or claim for refund shall also appear on the return or claim for refund. In general, if the preparer is an individual, the preparer's social security number shall be affixed, but if the preparer is a person (whether an individual, corporation, or partnership) that employs (or engages) one or more persons to prepare the return or claim for refund, the preparer's employer identification number shall generally be used. Special rules apply to preparers that are not citizens or residents of the United States.

Under sections 6060 of the Code and 1.6060-1 of the regulations, any person who employs an income tax return preparer to prepare a return or claim for refund other than for that employer must retain a record concerning each preparer so employed and may be penalized under section 6695(e) for failure to do so.

Section 6695(f) of the Code imposes a penalty of $500 on income tax return preparers who endorse or otherwise negotiate refund checks that are issued to taxpayers. There is no reasonable cause exception.

Section 7216 of the Code imposes a criminal penalty for unlawful disclosure or use of return information by persons who prepare or provide services in connection with the preparation of returns.

ISSUE 3

Although *X* and *Y* require their customers to execute powers of attorney authorizing them to receive and endorse or negotiate the refund checks, in both *situation 1* and *situation 2* the assignment of the taxpayers' claims is not valid against the United States. The Anti-Assignment Act, 31 U.S.C. section 3727 (1982), nullifies assignments made *before* a claim is allowed by the Government, the correct amount of the payment is decided, and a warrant (refund check) for payment of the claim has been issued. A purpose of the statute is to protect the Government from having to deal with multiple persons with respect to a claim, in this case a preparer and the preparer's customers. *Patterson v. United States*, 354 F.2d 327 (Ct. Cl. 1965). The statute has been held to be specifically applicable to refunds of overpayments of taxes. *See Wooton v. United States*, 86 F. Supp. 143 (Ct. Cl.1960), *cert. denied*, 339 U.S. 903 (1960); *New York v. Hanley Milling Co.*, 41 F. Supp. 844 (N.D. Ohio, 1941), *aff'd*, 123 F.2d 819 (6th Cir. 1941). The assignment is therefore not valid against the United States. Accordingly, if the Internal Revenue Service determines that the address shown on the return is not the taxpayer's address, any refund checks may be mailed directly to the taxpayer and not to the preparer.

HOLDINGS

ISSUE 1

X and *Y* are income tax return preparers with respect to their customers' income tax returns.

ISSUE 2

As income tax return preparers, *X* and *Y* are subject to the various requirements and potential penalties applicable to preparers, as previously set forth in this ruling. *X* and *Y* are potentially subject to penalties under sections 6694(a) or 6695(b) of the Code if any part of an understatement of liability on a customer's return is due to a negligent or intentional disregard of rules or regulations by the preparer, or if the understatement is due to the preparer's attempt to willfully understate the liability.

X and *Y* are required to furnish copies of the returns to the customers and retain a list of taxpayers for whom returns have been prepared. They may be subject to penalties under sections 6695(a) or 6695(d) of the Code for failure to do so.

The individual preparer with primary responsibility for the overall substantive accuracy of the customer's return is required to sign the return as preparer and is subject to the penalty under section 6695(b) of the Code for failure to do so. *X* and *Y* are required to furnish their identifying numbers on the customers' returns and they may be subject to the penalty under section 6695(c) for failure to do so.

Under section 6060 of the Code, *X* and *Y* must keep records of all persons in their employ that meet the definition of income tax return preparer, and *X* and *Y* are subject to the penalty under section 6695(e) of the Code for failure to do so.

X and *Y* are subject to the penalty under section 6695(f) of the Code when they endorse or otherwise negotiate a customer's refund check.

X and *Y* may be subject to the criminal penalty under section 7216 of the Code if they make unlawful disclosure or use of return information.

ISSUE 3

The assignment of the customers' refund checks before the returns are processed by the Internal Revenue Service is not a valid assignment against the United States. Accordingly, the Service need not mail the checks to the preparers and may mail them directly to the taxpayers in question.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.204: Change in accounting periods and methods of accounting.
(Also Part I, Section 162, 404, 463; 1.162-10.)

Rev. Proc. 86-20

SECTION I. PURPOSE

The purpose of this revenue procedure is to declare that Rev. Proc. 82-32, 1982-1 C.B. 486 is obsolete. Rev. Proc. 82-32 sets forth a procedure for taxpayers that employ the accrual method as their overall method of accounting to obtain expeditious consent to change their method of accounting for deducting vacation pay attributable to fully vested plans.

SEC. 2. BACKGROUND

.01 Section 162(a) of the Internal Revenue Code allows as a deduction all the ordinary and necessary expenses paid or incurred during the tax year in carrying on any trade or business. Section 1.162-10 of the Income Tax Regulations provides that if amounts paid or accrued within the tax year for vacations or a sickness or similar employee benefit plan are ordinary and necessary expenses of the trade or business, they are deductible under section 162(a) unless the plans provide benefits under a deferred compensation plan of the type referred to in section 404 of the Code.

.02 Rev. Proc. 82-32 applies to taxpayers whose vacation benefit plan expenses are deductible under section 162(a) of the Code. In particular, Rev. Proc. 82-32 applies to taxpayers that: (1) employ an accrual method as their overall method of accounting; (2) provide paid vacations for their employees in accordance with fully vested vacation pay plans; (3) pay the amount accrued no later than the close of the tax year succeeding the year of accrual; and (4) desire to change their method of accounting for vacation pay from deducting the vacation pay for the year in which it is paid to deducting the vacation pay for the year in which it becomes fully vested and accrues.

.03 Section 512 of the Tax Reform Act of 1984, 1984-3 (Vol. 1) C.B. 370, amended section 404(b) of the Code to clarify that any plan, method, or arrangement providing deferred benefits (including deferred vacation pay) is a plan, method or arrangement deferring the receipt of compensation. The amendment is effective for amounts paid or incurred for deferred compensation arrangements after July 18, 1984, except for certain extended vacation pay plans in effect on June 22, 1984. Under section 404(b), section 404 does not apply to any vacation benefit to which an election applies under section 463. Thus, in general, unless one of the above exceptions applies, deferred vacation benefits are considered provided under a deferred compensation plan under section 404 of the Code irrespective of whether the taxpayer employs the accrual or the cash method of accounting. Under section 1.404(b)-1T Q&A-2 of the Temporary Income Tax Regulations under the Tax Reform Act of 1984, if vacation benefits are paid on or before the 15th day of the 3rd calendar month after the end of the employer's tax year in which significant services required for payment are performed, the benefits generally are not treated as provided under a deferred compensation plan. Rather, in the case of a taxpayer that uses the accrual method of accounting for vacation pay, the benefits are deductible under section 162(a) of the Code for the tax year preceding payment, if they are otherwise accruable in that year. A taxpayer employing the cash method for vacation pay must deduct its vacation benefits in its tax year of payment.

.04 Section 463 of the Code provides that an accrual basis taxpayer may elect, without the consent of the Commissioner of Internal Revenue, to deduct certain amounts with respect to vacation pay that would not otherwise be deductible.

SEC. 3. INQUIRIES

Inquiries regarding this revenue procedure may be addressed to the Commissioner of Internal Revenue, Attention CC:C:C:1, 1111 Constitution Avenue, N.W., Washington, D.C., 20224.

SEC. 4. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 82-32 is obsolete.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

International Aspects of Section 338

LR-35-84

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary regulations that add a new §1.338-5T, relating to international aspects of section 338, and that amend existing temporary regulations §§1.338-1T, 1.338-4T, and 1.338(h)(10)-1T. Section 1.338-1T contains procedural rules and §1.338-4T provides guidance on miscellaneous substantive matters under section 338, primarily in the domestic context. Section 1.338(h)(10)-1T provides guidance on the operation of section 338(h)(10). Subject to the modifications specifically identified in this document, the text of new §1.338-5T and of the amendments to §§1.338-1T, 1.338-4T, and 1.338(h)(10)-1T also serves as the comment document for this notice of proposed rulemaking.

DATES:

PROPOSED EFFECTIVE DATE

The regulations are proposed to apply generally to stock acquisitions made after August 31, 1982. The regular exclusion election permitted by the temporary regulations that serve as the comment document for this notice of proposed rulemaking would be eliminated for stock acquisitions that occur subsequent to the date of publication of the final regulations (and that do not occur pursuant to a binding contract in effect on or before that date).

DATE FOR COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Written comments and requests for a public hearing must be delivered or mailed by April 14, 1986.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-35-84), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Keith E. Stanley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3458, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

Temporary regulations published * * * [on page 4, this Bulletin] add new temporary regulations §1.338-5T to Part 1 of Title 26 of the Code of Federal Regulations ("CFR") and amend temporary regulations §§1.338-1T, 1.338-4T, and 1.338(h)(10)-1T. The new temporary regulations also amend the table of OMB control numbers in Part 602 of Title 26 of the CFR to reflect the OMB control number assigned to §1.338-5T.

Section 1.338-1T was published as T.D. 7942 in the FEDERAL REGISTER on February 8, 1984 (49 FR 4722) [1984-1 C.B. 93], and was amended and redesignated (as §1.338-1T) by temporary regulations published as T.D. 7975 in the FEDERAL REGISTER on September 6, 1984 (49 FR 35086) [1984-2 C.B. 81]. Section 1.338-1T also was amended by temporary regulations published as T.D. 8021 in the FEDERAL REGISTER on April 25, 1985 (50 FR 16402) [1985-1 C.B. 96]. The temporary regulations published on April 25, 1985, also added §1.338-4T. Sections 1.338-1T and 1.338-4T were amended by temporary regulations published as T.D. 8068 in the FEDERAL REGISTER on January 8, 1986 [1986-8 I.R.B. 9], and by temporary regulations published as T.D. 8072 in the FEDERAL REGISTER on January 29, 1986 [1986-11 I.R.B. 7]. The temporary regulations published on January 8, 1986 also added §1.338(h)(10)-1T.

The final regulations are proposed to be based on the new and amended temporary regulations with certain modifications specifically identified herein. They would be added to Part 1 of Title 26 of the CFR. Those final regulations would provide guidance primarily on international aspects of section 338 of the Code, as added by section 224 of the Tax Equity and Fiscal Responsibility Act of 1982 (Pub. L. No. 97-248; 96 Stat. 485) [1982-2 C.B. 462, 501] and as amended by section 306(a)(8) of the Technical Corrections Act of 1982 (Pub. L. No. 97-448; 96 Stat. 2402) [1983-1 C.B. 451, 470] and section 712(k) of the Tax Reform Act of 1984 (Pub. L. No. 98-369; 98 Stat. 946) [1984-3 C.B. (Vol. 1) 1, 456]. For the text of the new and amended temporary regulations, see T.D. 8074, published * ** [on page 4, this Bulletin]. The preamble to the temporary regulations, as supplemented by this preamble, explains the additions to the regulations.

REGULATION EXCLUSION ELECTION ELIMINATED

It is proposed that the regular exclusion election permitted by §1.338-5T(c)(2) of the temporary regulations published * * * [on page 4, this Bulletin] be eliminated in the final regulations. If this position is adopted in the final regulations, the regular exclusion election will not be available if (1) the acquisition date of the actual original target (as opposed to a deemed original target under §1.338-5T(c)(2)(iv)) occurs subsequent to the date of publication of the final regulations and (2) that acquisition does not occur pursuant to a binding contract in effect on or before that date.

The regular exclusion election under the temporary regulations permits the purchasing corporation to elect, in certain cases, to exclude all foreign corporations (other than foreign corporations treated as domestic corporations under those regulations) from the status of target affiliates for purposes of the stock consistency rule of section 338(f)(1). As a result, such corporations are not subject to a deemed election under section 338(f)(1) when an express election is made for the original target. The preamble to the temporary regulations contains a detailed explanation of the regular exclusion election and of the ancillary consequences of such an election. The temporary regulations provide for a similar exclusion election ("transitional exclusion election") during a transitional period. See §1.338-5T(j). (The provisions of the temporary regulations relating to the transitional exclusion election would be retained in the final regulations.)

The regular exclusion election is a response to the asserted hardship of imposing full stock consistency in the foreign context. It has been claimed, for example, that full stock consistency would create difficult valuation problems, since a valuation of all of the assets of all foreign subsidiaries subject to deemed elections under section 338(f)(1) would be required. It also has been claimed that full stock consistency would exacerbate the mismatch between asset basis as recognized by the Untied States and asset basis as recognized by the foreign taxing jurisdiction, since new foreign target's assets generally would have a stepped-up basis for United States tax purposes as a result of the section 338 election but a carryover basis for foreign tax purposes. (Even if the foreign target is not required to file a United States income tax return, the basis adjustment nevertheless is significant for purposes of calculating that target's earnings and profits in the event of actual or deemed distributions to U.S. persons).

It is not clear, however, that full stock consistency would cause a significant hardship. The assets of foreign subsidiaries presumably would be valued for general accounting purposes in any case. As for the mismatch in asset basis, such a mismatch is not unique to section 338 and in some cases actually may be beneficial to taxpayers. (Increased depreciation deductions by new foreign target as a result of an asset basis step-up would decrease its earnings and profits and correspondingly increase the effective rate of foreign tax on its earnings and profits as calculated for U.S. tax purposes.)

Although the application of section 338 to the foreign branch of a domestic target corporation creates problems similar to those encountered by applying section 338 to a foreign subsidiary, the statute does not contemplate an exclusion of foreign branch operations from section 338 consequences. Thus, the regular exclusion election would result in differing tax consequences depending upon whether a U.S. corporation operated abroad through a foreign subsidiary or through a foreign branch. As a matter of general policy, it is believed that tax considerations should be a neutral factor in determinations regarding the form of foreign operations. See, *e.g.*, the deemed paid foreign tax credit under section 902. The regular exclusion election conflicts with that general policy.

The regular exclusion election also conflicts with the general policy of the consistency rules by permitting the purchasing corporation to exclude all foreign corporations from an express election.

The regular exclusion election adds significantly to the complexity of the temporary regulations. The complexity is necessary in order to preserve appropriate section 1248 consequences and to ensure the proper operation of the consistency rules. See §1.338-5T(c)(2)(iii)(B) and (c)(3)) (provisions related to the consistency rules).

For the foregoing reasons it is proposed that the regular exclusion election be eliminated in the final regulations. Comments on this issue would be particularly helpful.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before these proposed regulations are adopted, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER. The collection of information requirements contained herein have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on the requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests person submitting comments to OMB to also send copies of the comments to the Service.

DRAFTING INFORMATION

The principal author of these proposed regulations is Duane H. Pellervo of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

These regulations are proposed to be issued under the authority contained in sections 338 and 7805 of the Internal Revenue Code of 1954 (26 U.S.C. 338 and 7805, respectively).

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on February 6, 1986, 4:57 p.m., and published in the issue of the Federal Register for February 12, 1986, 51 F.R. 5208)

Clarification of Q&A-3 of Temporary Regulations Section 1.419-1T With Regard to the Definition of a "Fund"

Announcement 86-45

On February 4, 1986, proposed and temporary regulations were issued under section 419 of the Internal Revenue Code relating to welfare benefit funds. 51 FR 4312 (1986), 51 FR 4391 (1986). Q&A-3 of section 1.419-1T of the Temporary Income Tax Regulations contains a definition of the term "fund" under section 419 of the Code and deals with certain arrangements between employers and insurance companies. Questions have been raised about the interpretation of paragraph (c) of Q&A-3, particularly with regard to its application to experience-rated arrangements (including premium stabilization reserves that are part of such arrangements). In view of these questions, the Internal Revenue Service will modify paragraph (c) of Q&A-3 of section 1.419-1T of the temporary regulations to clarify its intended scope. This modification will be effective as if it had been included in the temporary regulations published on February 4, 1986.

Paragraph (c) of Q&A-3 of section 1.419-1T of the temporary regulations was intended, and will be modified, to treat as "funds" under section 419(e)(3)(C) only the following classes of arrangements between employers and insurance companies: (i) certain retired lives reserves, (ii) certain "administrative services only" arrangements, and (iii) certain arrangements between employers and insurance companies (including premium stabilization reserves that are part of such arrangements) under which the employer makes deductible contributions and the employer has, on or before the later of the end of the policy year to which such contributions relate or the time such contributions are made, a contractual right under the arrangement to a dividend, refund, credit, or additional benefit based on the benefit or claims experience, administrative cost experience, or investment experience, administrative cost experience, or investment experience attributable solely to such employer. The temporary regulation was not intended to include and, as modified, will not include within the definition of "fund" those arrangements (including premium stabilization reserves that are part of such arrangements) that are not included within any of the above classes.

Future regulations including additional arrangements between employers and insurance companies within the definition of "fund" under section 419(e)(3)(C) of the Code will be applied only on a prospective basis. The Internal Revenue Service continues to invite comments on the proposed regulations issued February 4, 1986, defining a "fund." The proposed regulations will not be modified pursuant to this announcement.

Fringe Benefits—Extension of Time

Announcement 86-46[1]

The Service has announced a further extension of the deadline for employers with more than one line of business to combine lines of business under a provision which enables their employees to exclude certain fringe benefits from gross income. The election applies to certain qualified employee discounts and certain services provided to employees at no extra cost.

The new deadline will be 60 days after publication of revised regulations under section 4977 of the Code. The Service anticipates publication of regulations under section 4977 in the near future. These regulations will provide additional guidance including details on how to make the election.

In News Release IR-85-120, dated Dec. 19, 1985, the Service extended the time for making this election to March 31, 1986.

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[1] Based on News Release IR-86-34, dated March 26, 1986.

Deletions from Cumulative List of Organizations Contributions to Which Are Deductible Under Section 170 of the Code

Announcement 86-50

The names of organizations that no longer qualify as organizations described in section 170(c)(2) of the Internal Revenue Code of 1954 are listed below.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsibile for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgement has been timely filed, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deductible. Protection under section 7428(c) would begin on April 14, 1986, (the date of publication of this announcement) and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is $1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

Amelia Educational Foundation, Amelia, VA

Besselman Trust, John & Laura, Richmond, IN

Hollywood Hills Geriatric Foundation, Inc., Hollywood, FL

Internation Literary & Art Foundation, Mesquite, TX

Isle of Wight County Educational Foundation, Inc., Isle of Wight, VA

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Robert Allen Beamer	Wauwatosa, WI	Attorney	Indefinite from February 19, 1986
Robert L. Cummings	Springfield, MO	Certified Public Accountant	Indefinite from February 27, 1986
Louis Crown	Bayside, NY	Certified Public Accountant	Indefinite from March 14, 1986
David H. Heilman	Council Grove, KS	Attorney	Indefinite from March 14, 1986
Beryl W. Markwell	Elmhurst, IL	Certified Public Accountant	Twenty-four Months from March 20, 1986
Marc Pozner	Tenafly, NJ	Certified Public Accountant	Indefinite from March 14, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before their Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Thomas G. Abernethy, Jr.	Jackson, MS	Attorney	March 7, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.103-10, amended.	Definition of "principal user"	1986-12 I.R.B. 19	Apr. 22, 1986
26 CFR 1.103-10, revised.	$40 million limitation on beneficiaries of certain tax-exempt bonds	1986-12 I.R.B. 22	Apr. 22, 1986

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

SPECIAL ANNOUNCEMENTS

Announcement 86-49, page 55.

A public hearing will be held on May 21, 1986, on proposed regulations relating to the annuity tables used to compute the portion of the amount received as an annuity that is includible in gross income.

Announcement 86-55, page 56.

The Service invites written comments and suggestions for improving its tax return forms, instructions, and related schedules.

INCOME TAX

Rev. Rul. 86-56, page 4.

LIFO; price indexes; department stores. The January 1986 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, January 31, 1986.

Rev. Rul. 86-57, page 4.

Claims; joint returns; credit against separate tax liability; net operating loss adjustment. A divorced taxpayer is entitled to a refund of tax for the taxpayer's interest in a joint overpayment created by a net operating loss on a former spouse's separately filed return. Rev. Ruls. 75-368 and 80-8 amplified.

Rev. Rul. 86-58, page 7.

Penalties; underpayment; amended return; corporations. In applying the exception to the addition to tax for underpayment of estimated tax, it is the tax shown on the original tax return and not the tax shown on an amended return filed after the due date of the original return that is the basis for the computation. Rev. Rul. 64-138 revoked.

LR-19-80, page 9.

Proposed amendments to the regulations relate to the annuity tables used to compute the portion of the amount received as an annuity that is includible in gross income, and to defined benefit plans.

Announcement 86-48, page 55.

An automatic extension of time to pay the first installment of estimated tax is granted to any U.S. citizen or resident alien individual outside the U.S. and Puerto Rico on April 15, 1986.

Announcement 86-51, page 56.

The temporary regulations under section 338(b) of the Code will be amended to provide a special transitional allocation election relating to the allocation of basis among the assets of a target corporation for stock acquisitions occurring before January 29, 1986, or pursuant to a binding contract entered into on or before that date.

EMPLOYEE PLANS

LR-19-80, page 9.

Proposed amendments to the regulations relate to the annuity tables used to compute the portion of the amount received as an annuity that is includible in gross income, and to defined benefit plans.

ADMINISTRATIVE

Rev. Rul. 86-59, page 6.

Adjusted interest rate; underpayments and overpayments. The adjusted rate of interest on underpayments and overpayments, as determined under section 6621(b) of the Code, will decrease from 10 to 9 percent on July 1, 1986.

Announcement 86-52, page 56.

Form 5330, Return of Excise Taxes Related to Employee Benefit Plans, has been revised to reflect new provisions in the law.

Announcement 86-53, page 56.

Publication 721, Comprehensive Guide to U.S. Civil Service Benefits, has been updated and is now available at most Service offices.

Finding Lists begin on page 60.
Announcement of Disbarments and Suspension begin on page 57.
Announcement of Notice of Proposed Rulemaking on page 59.
Disposition of Declaratory Judgement Proceedings Under Section 7428 on page 56.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 472.—Last-in, First-out Inventories

26 CFR 1.472-1: Last-in, first-out inventories.

LIFO; price indexes; department stores. The January 1986 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, January 31, 1986.

Rev. Rul. 86-56

The following price indexes for January 1986 were issued by the Bureau of Labor Statistics on February 27, 1986 for use by department stores and are accepted by the Internal Revenue Service under section 1.472-1(k) of the Income Tax Regulations and Rev. Proc. 72-21 1972-1 C.B. 745 for appropriate application to inventories of department stores employing the retail inventory and last-in first-out inventory methods for tax years ended on, or with reference to, January 31, 1986.

Indexes are prepared on a national basis for the store total for 20 major groups of departments, and for two special combinations—soft and durable goods. The store total index covers all departments, including some not listed separately, with the following exceptions; candy, foods, liquor, tobacco, paints, and wallpaper, as well as contract departments.

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE
INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS
(January 1941 = 100)

		January 1985	January 1986	Percentage Change from January 1985 to January 1986[1]
I.	Piece Goods	390.8	397.7	1.8
II.	Domestics and Draperies	535.9	532.9	−0.6
III.	Women's and Children's Shoes	534.9	523.5	−2.1
IV.	Men's Shoes	698.7	724.2	3.6
V.	Infants' Wear	478.8	529.0	10.5
VI.	Women's Underwear	422.2	431.2	2.1
VII.	Women's and Girls' Hosiery	234.0	236.1	0.9
VIII.	Women's and Girls' Accessories	436.6	448.5	2.7
IX.	Women's Outerwear and Girls' Wear	324.7	332.0	2.2
X.	Men's Clothing	462.7	469.1	1.4
XI.	Men's Furnishings	466.0	484.1	3.9
XII.	Boys' Clothing and Furnishings	429.6	437.9	1.9
XIII.	Jewelry	673.2	671.1	−0.3
XIV.	Notions	483.3	480.0	−0.7
XV.	Toilet Articles and Drugs	626.6	654.0	4.4
XVI.	Furniture and Bedding	523.6	541.5	3.4
XVII.	Floor Coverings	457.7	461.7	0.9
XVIII.	Housewares	711.1	717.7	0.9
XIX.	Major Appliances	238.8	246.0	3.0
XX.	Radio and Television	107.1	100.7	−6.0
	Groups I–XV: Soft Goods	464.0	473.7	2.1
	Groups XVI–XX: Durable Goods	440.8	446.6	1.3
	Store Total	457.6	466.6	2.0

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[1] Absence of a minus sign before percentage change in this column signifies price increase.

Section 6013.—Joint Returns of Income Tax by Husband and Wife

26 CFR 1.6013-1: Joint returns.

Whether a divorced spouse is entitled to a refund of tax for his/her interest in a joint overpayment attributable to the recomputation of a joint tax liability. See Rev. Rul. 86-57, below.

Section 6402.—Authority to Make Credits or Refunds

26 CFR 301.6402-1: Authority to make credits or refunds.

(Also Sections 6013, 6511; 1.6013-1, 301.6511(a)-1.)

Claims; joint returns; credit against separate tax liability; net operating loss adjustment. A divorced taxpayer

is entitled to a refund of tax for the taxpayer's interest in a joint overpayment created by a net operating loss on a former spouse's separately filed return. Rev. Ruls. 75-368 and 80-8 amplified.

Rev. Rul. 86-57

ISSUE

(1) Is a divorced taxpayer entitled to a refund of tax for the taxpayer's interest in a joint overpayment attributable to the recomputation of a joint tax liability as a result of the carryback of a separate net operating loss of a former spouse to a year in which a joint return was filed?

(2) If so, what is the applicable period of limitations for filing a claim for refund?

FACTS

A and *B*, a married couple residing in a noncommunity property state, filed a joint federal income tax return for calendar year 1981 reporting a tax liability of $3,191. *A* reported $15,000 in taxable income and withholding tax credits of $2,500. *B* reported $5,000 in taxable income and withholding tax credits of $1,000. They received a refund of $309. In 1984 *A* and *B* were divorced. *A* timely filed a separate return for that year claiming a net operating loss of $5,000. No extension was obtained by *A* for filing that return. *A* carried the loss back to 1981 and filed a claim for refund or credit. *B* also filed a claim refund or credit of a portion of the joint overpayment as a result of the recomputation of the joint tax liability. The recomputed liability was $2,034.

LAW AND ANALYSIS

Section 6013 of the Internal Revenue Code provides for the filing of a joint return by a husband and a wife and imposes joint and several liability upon them for the tax computed on their aggregate income.

Section 6402(a) of the Code provides that in the case of an overpayment, the Secretary, within the applicable period of limitations, may credit the amount of the overpayment, including any allowable interest, against any liability in respect of an internal revenue tax on the part of the person who made the overpayment and, subject to certain exceptions, must refund the balance to the person.

Section 6511(a) of the Code provides that a claim for credit or refund of an overpayment of any tax for which the taxpayer is required to file a return must generally be filed by the taxpayer within 3 years from the time the return was filed or 2 years from the time the tax was paid, whichever period expires later, or if no return was filed by the taxpayer, 2 years from the time the tax was paid.

Section 6511(d)(2) of the Code provides a special period of limitations if the claim for credit or refund relates to an overpayment attributable to a net operating loss carryback. In lieu of the 3-year period prescribed in section 6511(a), the period after which a claim may not be filed for the taxable year to which the loss is carried back (the carryback year) is the period ending 3 years after the time prescribed by law for filing the return (including extensions) for the taxable year of the operating loss that results in the carryback (the loss year).

Rev. Rul. 74-611, 1974-2 C.B. 399, holds that when a husband and wife file a joint return each spouse has a separate interest in the jointly reported income and a separate interest in any overpayment.

Rev. Rul. 75-368, 1975-2 C.B. 480, holds that when a net operating loss of an unmarried taxpayer is carried back or carried over to a year in which the taxpayer is married and files a joint return, the net operating loss deduction is carried back or carried over only to reduce the taxpayer's portion of the income shown on the joint return.

Rev. Rul. 80-6, 1980-1 C.B. 296, modifies Rev. Rul. 75-368 by providing that the rules set out in Rev. Rul. 80-7, described below, will be used in calculating the amount of the refund to be paid to the spouse who incurred the net operating loss.

Rev. Rul. 80-7, 1980-1 C.B. 296, provides a formula (the separate tax formula) for determining one spouse's share of a joint tax liability. Under the separate tax formula, a spouse's share is an amount that bears the same ratio to the joint liability as the amount of tax for which the spouse would have been liable if the spouse had filed a separate return bears to the sum of the taxes for which both spouses would have been liable had they filed separately. The ruling also holds that a spouse's share of a joint overpayment is determined by subtracting the spouse's share of the joint liability for the spouse's contribution toward the payment of the joint liability.

In addition, Rev. Rul. 80-7 provides rules for determining each spouse's contribution toward the payment of the joint liability in the absence of agreement or clear evidence as to each spouse's actual contribution. An analogue to the separate tax formula is used to allocate both estimated tax payments and payments with the return. The amount of the overpayment credited or paid to either spouse cannot exceed the amount of the joint overpayment.

Rev. Rul. 80-8, 1980-1 C.B. 298, holds that the Internal Revenue Service will accept a claim for credit or refund filed by a divorced taxpayer with respect to a joint return if the claim form is signed by only one taxpayer and that the Service will issue a refund check in that taxpayer's name alone. The amount of the refund or credit will be computed according to the rules for determining each spouse's share of the joint overpayment set out in Rev. Rul. 80-7.

Rev. Rul. 75-368, as modified by Rev. Rul. 80-6, does not address the question of whether the spouse not suffering the net operating loss is entitled to a refund for a share of the joint overpayment that results when a net operating loss deduction is carried back to a joint return year and the joint tax liability is recomputed. However, Rev. Rul. 80-8 recognizes that each spouse has an interest in any overpayment, and that ruling provides that the allocation rules set out in Rev. Rul. 80-7 must be used to determine the individual refund of each spouse. Thus, the net operating loss is applied only against A's income, as required by Rev. Rul. 75-368 but since application of the rules provided in Rev. Rul. 80-7 and used in Rev. Rul. 80-8 results in allocation of a share of the overpayment to *B*, that amount should be refunded to *B* in the manner described in Rev. Rul. 80-8.

In order to compute *A*'s and *B*'s contributions toward payment, the original refund of $309 must also be allocated under the rules provided in Rev. Rul. 80-7. In allocating this original refund, the separate tax formula is applied using *A*'s and *B*'s income as originally reported on the joint return before the application of the net operating loss. When the separate tax formula is applied to the original 1981 figures, *A*'s share of the joint liability is $2,724; *B*'s share is $467. Because *A*'s share of the joint liability is greater than *A*'s withholding credits of $2,500, the entire refund of $309 is allocated to *B*.

A's and *B*'s respective portions of the overpayment would, thus, be computed as follows:

A's and *B*'s joint liability as originally reported was $3,191. After application of the net operating loss to *A*'s income the joint recomputed liability was $2,034. The total joint refund was $1,157 ($3,191 − $2,034).

A's recomputed separate tax liability is $1598;
B's separate tax liability (which is not affected by the carryback) is $529.
A's recomputed individual liability is:

$$\frac{\underline{\$1{,}598 \text{ (A's separate liability)}}}{\$1{,}598 + \$529 \text{ (A's + B's separate liabilities}} \times \$2{,}034 \text{ (recomputed joint liability)} = \$1{,}528.13$$

B's recomputed individual liability is:

$$\frac{\$529 \text{ (B's separate liability)}}{\$1{,}598 + \$529} \times \$2{,}034 = \$\ 505.87$$

A's contribution toward payment of the joint liability is $2,500—*A*'s withholding credits.

B's contribution toward payment of the joint liability is $691. ($1,000 (withholding credits) — $309 (refund)).

A's individual refund is $971.87 ($2,500 − $1,528.13).
B's individual refund is $185.13 ($691 − $505.87).

Even though *A*'s net operating loss may only be applied against *A*'s portion of the joint income, *B*'s overpayment is directly attributable to *A*'s net operating loss carryback. Therefore, the extended period of limitations provided under section 6511(d)(2) of the Code applies to any claim for refund made by *B*.

HOLDING

Issue (1): Under the facts as presented, a divorced taxpayer is entitled to a refund of tax for the taxpayer's interest in a joint overpayment. *B* is entitled to a refund of $185.13.

Issue (2): the applicable period of limitations is that provided by section 6511(d)(2) of the Code. *B* has until April 15, 1988, to file a claim for refund or credit.

EFFECT ON OTHER
REVENUE RULINGS

Rev. Rul. 75-368 and Rev. Rul. 80-8 are amplified.

Section 6511.—Limitations on Credit or Refund

26 CFR 301.6511(d)-2: Overpayment of income tax on account of net operating loss or capital loss carrybacks.

Whether a divorced spouse is entitled to a refund of tax for his/her interest in a joint overpayment attributable to the recomputation of a joint tax liability. See Rev. Rul. 86-57, page 4.

Section 6621.—Determination of Rate of Interest

26 CFR 301.6621-1: Interest rate.

Adjusted interest rate; underpayments and overpayments. The adjusted rate of interest on underpayments and overpayments, as determined under section 6621(b) of the Code, will decrease from 10 to 9 percent on July 1, 1986

Rev. Rul. 86-59

Section 6621(b) of the Internal Revenue Code provides for semiannual adjustment of the interest rate established under that section. Section 6621(b)(1) requires that these adjustments in the rate be established by October 15 and April 15, and be based on the average prime interest rate for the six-month period ending the previous September 30 or March 31, respectively.

The Board of Governors of the Federal Reserve System has determined that the average prime interest rate for the six-month period ending March 31, 1986, was 9.43 percent. That rate, rounded to the nearest full percent, is 9 percent, a change of 1 percent from the rate of 10 percent in effect under the last determination made by the Internal Revenue Service. *See* Rev. Rul. 85-169, 1985-44 I.R.B. 15. Accordingly, an adjusted rate of interest of 9 percent is established under section 6621(b). The adjusted rate will take effect on July 1, 1986 and will apply to amounts outstanding on that date or arising thereafter.

Daily rates for compound interest for 9 percent were published in Table 15 of Rev. Proc. 83-7, 1983-1 C.B. 583, 598.

Compound interest rates for prior periods are set forth in the following table:

PERIOD	RATE	DAILY RATE TABLE IN 1983-1 C.B.
January 1, 1983–June 30, 1983	16%	Table 22, pg. 605
July 1, 1983–December 31, 1983	11%	Table 17, pg. 600
January 1, 1984–June 30, 1984	11%	Table 41, pg. 625
July 1, 1984–December 31, 1984	11%	Table 41, pg. 625
January 1, 1985–June 30, 1985	13%	Table 19, pg. 602
July 1, 1985–December 31, 1985	11%	Table 17, pg. 600
January 1, 1986–June 30, 1986	10%	Table 16, pg. 599

Section 6655.—Failure by Corporation to Pay Estimated Income Tax

26 CFR 1.6655-1: Addition to the tax in the case of a corporation.

Penalties; underpayment; amended return; corporations. In applying the exception to the addition to tax for underpayment of estimated tax, it is the tax shown on the original tax return and not the tax shown on an amended return filed after the due date of the original return that is the basis for the computation. Rev. Rul. 64-138 revoked.

Rev. Rul. 86-58

ISSUE

For purposes of determining any underpayment of estimated tax by a corporation under section 6655 of the Internal Revenue Code, does the term "tax shown on the return for the taxable year" in section 6655(b) mean only the tax shown on the original tax return filed by the taxpayer or does the term include the tax shown on an amended return filed after the due date of the return, including any extensions?

FACTS

Situation 1

X, a corporation, files its federal income tax return on a calendar year basis. *X* made estimated tax payments of $6,000 during 1984. On March 15, 1985, *X* filed its 1984 tax return showing a tax liability of $20,000 and paid the balance of $14,000. Subsequently, *X* discovered an error and on April 30, 1985, filed an amended return for 1984 showing a reduced tax liability of $8,000.

Situation 2

The facts are the same as in *Situation 1*. In addition, on April 15, 1985 *X* made its first estimated tax payment for 1985. The amount of this payment was $5,000, which is one fourth of what then appeared to be *X*'s 1984 tax liability of $20,000. *X* paid a total of $3,000 as its other 1985 estimated tax payments due in 1985. As a result, the total paid was equal to the reduced tax liability shown on *X*'s 1984 amended return filed April 30, 1985. On March 15, 1986, *X* filed its 1985 return showing a tax liability of $25,000.

LAW AND ANALYSIS

Under section 6154(a) of the Code, every corporation subject to taxation under section 11 or 1201(a), or subchapter L of chapter 1, is required to make payments of estimated tax if it reasonably expects to have an estimated tax liability for the taxable year of $40 or more.

A corporation is subject to an addition to tax under section 6655(a) of the Code on the amount of the underpayment of any estimated tax for the period of the underpayment if the corporation fails to make an estimated tax payment when due. The addition to tax will not be imposed, however, if the corporation comes within an exception under section 6655(d).

Section 6655(b) of the Code provides that the amount of the underpayment is the excess of (1) the amount of the installment that would be required to be paid if the estimated tax were equal to 90 percent of the tax shown on the return for the taxable year or, if no return was filed, 90 percent (80 percent for taxable years beginning before January 1, 1983) of the tax for the year, over (2) the amount, if any, of the installment paid on or before the last date prescribed for payment.

Under section 6655(d) of the Code, the addition to tax with respect to any underpayment of any installment will not be imposed if the total amount of all payments of estimated tax made on or before the last date prescribed for payment of the installment equals or exceeds the amount that would have been required to be paid on or before the date if the estimated tax were based on the lesser of (1) the tax shown on the return of the corporation for the preceding year if a return showing a tax liability was filed and was a taxable year of 12 months, (2) an amount equal to the tax computed at the rates applicable to the taxable year but otherwise on the basis of the facts shown on the return of the corporation for, and the law applicable to, the preceding taxable year, and (3) an amount equal to 90 percent of the tax for the taxable year computed by placing the taxable income for certain shorter periods on an analyzed basis by multiplying each period's taxable income by 12 and dividing the resulting amount by the number of months in the period.

In *Evans Cooperage Co., Inc. v. United States*, 712 F.2d 199 (5th Cir. 1983), through an error a corporation underpaid its estimated tax for 1977, which was based upon the tax shown on the corporation's original 1976 return. In 1979, the corporation amended its 1976 and 1977 tax returns to reflect less tax liability in each year, and argued that on the basis of the tax liability shown on its amended returns, its payment of estimated tax for 1977 was within the "safe harbor" minimum payment provisions of section 6655(d)(1). The appellate court affirmed the judgment of the district court, that dismissed the taxpayer's suit. The appellate opinion stated that "[t]he taxpayer's argument that the ultimate tax liability, rather than the amount reflected on the return, should trigger (or remove) the protection of the safe harbor provision is in the face of express statutory language to the contrary." *Evans Cooperage Co.*, 712 F.2d at 203.

Citing Rev. Rul. 78-256, 1978-1 C.B. 438, the court noted that as a matter of administrative discretion the Commissioner has ruled that an amended return filed on or before the due date of the return for the taxable year, including extensions, is the return for purposes of section 6655(b) of the Code. Similarly, Rev. Rul. 83-36, 1983-1 C.B. 358, holds that an amended return must be filed by the due date of the return for the taxable year to be considered the return for the year for purposes of computing the penalty for underpayment of estimated tax under section 6654(b).

HOLDING

In determining any underpayment of estimated tax by a corporation under section 6655 of the Code, the "tax shown on the return for the taxable year" is the tax shown on the corporation's original tax return for the taxable year, unless an amended return is filed on or before the due date of the original return, including extensions. Thus, in *Situation 1*, for purposes of determining the addition to tax on *X*'s 1984 tax return for underpayment of estimated tax, the underpayment is determined by reference to *X*'s original tax return showing a tax liability of $20,000.

This holding is equally applicable to section 6655(d) of the Code. Therefore, in *Situation 2*, if *X* chooses to rely on section 6655(d)(1) to avoid the addition to tax for an underpayment of estimated tax payments for 1985, *X* must make payments of at least $20,000.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 64-138, 1964-1 (Part 1) C.B. 509, held that the addition to tax on account of an underpayment of estimated tax by a corporation was computed on the corrected tax shown on an amended return. The ruling reasoned that the addition to tax for underpayment of estimated tax by a corporation is based on the corporation's tax liability for the year, as adjusted in the case there considered to take into account the investment credit claimed on an amended return. The amended return reflected a lowered tax liability because of the retroactive application of the investment credit allowed by section 38 of the Code for investment in certain depreciable property. Section 38, added to the Code by the Revenue Act of 1962, 1962-3 C.B. 111, was made retroactive with respect to taxable years ending after December 31, 1961. Because that reasoning is inconsistent with the reasoning set forth above, Rev. Rul. 64-138 is revoked.

Part IV. Items of General Interest

Notice of Proposed Rulemaking Unisex Annuity Tables

LR-19-80

SUMMARY: This document contains proposed regulations relating to the annuity tables used to compute the portion of the amount received as an annuity that is includible in gross income. Questions have arisen concerning the gender distinction in the existing tables and the outdated mortality experience upon which those tables are based. These regulations would affect taxpayers receiving amounts as annuities under annuity, endowment, or life insurance contracts for which they have paid premiums or other consideration and provide them with the guidance needed to determine the amount includible in gross income with respect to such contracts. This document also contains proposed regulations relating to the computations necessary to determine the amount excludable from an employee's gross income by allocation of contributions when the actual employer contributions are not known. This document also proposes to remove certain regulations relating to defined benefit plans that provided benefits for employees who were either self-employed or a shareholder-employee.

DATES: Written comments and requests for a public hearing must be delivered or mailed by May 8, 1986. The amendments to §§1.72-4, 1.72-5, 1.72-6, 1.72-7, 1.72-9, and 1.71-11 are proposed to be effective on July 1, 1986, and to apply to amounts received as an annuity after June 30, 1986. In addition, the proposed amendments to §1.72-6 include transitional rules applicable to amounts received under contracts in which an amount is invested before July 1, 1986. The amendments to §1.403(b)-1(d)(4)(iv) are proposed to be effective for taxable years beginning after July 1, 1986. The removal of §§1.401(a)-18 and 1.401(j)-1 through -6 is proposed to be effective for plan years beginning after December 31, 1983.

ADDRESS: Send comments and requests for a public hearing concerning the proposed amendments relating to the annuity tables to: Commissioner of Internal Revenue, Attention: CC:LR:T [LR-19-80], Washington, D.C. 20224.

ADDRESS: Send comments and requests for a public hearing concerning IRC section 403(b) to Commissioner of Internal Revenue, Attention: CC:LR:T:EE-114-82, Washington, D.C. 20224.

FOR FURTHER INFORMATION CONCERNING THE PROPOSED AMENDMENTS RELATING TO THE ANNUITY TABLES CONTACT: Annette J. Guarisco of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T). Telephone 202-566-3238 (not a toll-free call).

FOR FURTHER INFORMATION CONCERNING IRC sections 401(a)(18), 401(j) or 403(b) CONTACT: Monice Rosenbaum of the Employee Plans and Exempt Organizations Division, Office of Chief counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T:EE-114-82). Telephone 202-566-3422 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) and the Table of OMB Control Numbers (26 CFR Part 602). The proposed amendments would update and gender-neutralize the annuity tables used to determine the exclusion ratio applicable to amounts received as annuities under annuity, endowment, or life insurance contracts. Section 72 permits a taxpayer to exclude from gross income that part of any amount received as an annuity which bears the same ratio to such amount as the investment in the contract as of the annuity starting date bears to the expected return under the contract as of such date. If the expected return depends in whole or in part on the life expectancy of one or more individuals, the statute requires that the expected return be computed with reference to actuarial tables prescribed by the Secretary of the Treasury. Soon after section 72 was enacted in 1954, the Secretary published regulations containing tables based on 1937 individual annuitant mortality and distinguished by gender. The effect of this gender distinction is that women are not entitled to exclude from gross income as high a proportion of the amount received as an annuity as men of the same age.

REVISED ANNUITY TABLES

These proposed amendments provide new tables that eliminate the gender distinction and are based on more recent mortality experience. The proposed tables are based, as are the tables currently in effect, on individual annuitant mortality. The 1983 experience table used to produce the annuity tables proposed in this document was developed by the Society of Actuaries and reflects application of improvement factors to a 1973 individual-annuitant experience table. See Report of the Committee to Recommend a New Mortality Basis for Individual Annuity Valuation (Derivation of the 1983 Table a) Vol. XXXIII, Transactions of the Society of Actuaries 675, 708 (1981). In addition, the proposed unisex tables assume that the population mix of males and females at each age is the same as that of individual annuitants. The individual-annuitant gender mix reflected in the proposed tables is based on the same Society of Actuaries study.

The Service and Treasury would appreciate any comments on these proposed amendments that focus on whether the assumptions used to develop the tables are appropriate for determining life expectancies of taxpayers receiving amounts taxable under section 72, especially those taxpayers who can be expected to use the section 72 annuity tables (rather than, for example, the three-year recovery rule of section 72(d)) to compute an exclusion ratio under section 72(b) and 72(c). In particular, the Service and Treasury would be interested in data, undifferentiated by gender, on the mortality experience of taxpayers receiving amounts to which section 72 applies.

SECTION 72
TRANSITIONAL RULE

The exclusion ratio with respect to amounts received as an annuity after June 30, 1986, would generally be computed using the updated annuity tables proposed in this document. Two transitional rules are provided, however. The first applies to amounts received under a contract in which no amount was invested after June 30, 1986, and provides that the tables in the existing regulations would apply. The second transitional rule applies to contracts in which amounts were invested both before July 1, 1986, and after June 30, 1986. The second transitional rule is optional and would allow a taxpayer either to compute one exclusion ratio using the updated annuity tables, or to compute separate exclusion ratios with respect to the amounts invested in the contract before July 1, 1986, and the amounts invested after June 30, 1986. If the separate computation option were chosen, the tables in the existing regulations would be used to compute the exclusion ratio with respect to portions of the payments under the contract attributable to amounts invested in the contract before July 1, 1986, and the updated tables would be used to compute the exclusion ratio with respect to portions of payments under the contract attributable to amounts invested after June 30, 1986. The amount excludable from gross income would be the sum of the amounts determined by applying the two exclusion ratios to the amount received as an annuity.

The regulations provide that the transitional rules do not apply to an annuity contract with an annuity starting date occurring after June 30, 1986, if the contract provides, at the option of the annuitant or of any other person, for any form of payment or settlement that permits receipt of amounts under the contract in a form other than a life annuity. The transitional rules may not be used, for example, if the contract permits the taxpayer to withdraw the investment in the contract before the annuity starting date, to receive a lump sum in full discharge of the obligation under the contract, or to receive an annuity for a period certain (without regard to life expectancy) or its substantial equivalent. In effect, a contract that provides for these options is treated for purposes of the transitional rules as if the entire investment in the contract were made on the annuity starting date. Thus, the taxpayer must apply the updated, gender-neutral annuity tables proposed in this document to the entire investment in such a contract if the annuity starting date after July 30, 1986.

REMOVAL OF
SECTION 401(J) REGULATIONS

Sections 401(a)(18) and 401(j) provided requirements that applied to defined benefit plans that provided benefits for employees who were either self-employed, within the meaning of section 401(c)(1), or a shareholder-employee within the meaning of former section 1379(d). Sections 237(b) and 238(b) of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) [Pub. L. 97-248, 1982-2 C.B. 462] repealed these sections. Under section 241(a) of TEFRA these amendments were effective for plan years beginning after 1983. The regulation sections under these repealed Code sections (§§1.401(a)-18 and 1.401(j)-6) are, therefore, proposed to be removed from the Code of Federal Regulations. Thus, for plan years beginning after December 31, 1983, these defined benefit plans would no longer be subject to these benefit limitations. These sections, and the regulations would, however, continue to apply to determine whether plan benefits satisfied the requirements for plan years beginning prior to January 1, 1984.

AMENDMENT OF
SECTION 403(B) REGULATIONS

Section 1.403(b)-1(d)(4) provides the computations necessary to determine the amount excludable from an employee's gross income under section 403(b) when the actual employer contributions made on behalf of an employee to a defined benefit plan are not known. The tables in that section have been removed and gender-neutral tables inserted in lieu thereof. The new tables use an interest rate of 8 percent and the mortality table found in Treas. Reg. §20.2031-7 of the Estate Tax Regulations. Accordingly, Rev. Rul. 67-78, 1967-1 C.B. 94, which supplemented Table I at §1.403(b)-1(d)(4)(iv), is made obsolete. The new tables are proposed to be effective for taxable years beginning after May 23, 1986.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact analysis is not required. Although this document is a notice of proposed rulemaking that solicits public comments, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations are not subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

COMMENTS AND REQUESTS
FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act of 1980. Comments on those requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for the Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies to the Service.

DRAFTING INFORMATION

The principal author of the regulations under section 72 is Annette J. Guarisco of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. The principal author of the section 401 and 403 regulations is Monice Rosenbaum of the Employee Plans and Exempt Organizations Division, Office of Chief Counsel, Internal Revenue

Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * * *

Proposed amendments to the regulations

The proposed amendments to 26 CFR Parts 1 and 602 are as follows:

INCOME TAX REGULATIONS
(26 CFR Part 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Sections 1.72-4, 1.72-5, 1.72-6, 1.72-7, 1.72-9, and 1.72-11 also issued under 26 U.S.C. 72(c).

Par. 2. Section 1.72-4 is amended by revising paragraphs (a), (d), and (e) to read as follows:

§1.72-4 Exclusion ratio.

(a) *General rule.* (1)(i) To determine the proportionate part of the total amount received each year as an annuity which is excludable from the gross income of a recipient in the taxable year of receipt (other than amounts received under *(a)* certain employee annuities described in section 72(d) and §1.72-13, or *(b)* certain annuities described in section 72(o) and §1.122-1), an exclusion ratio is to be determined for each contract. In general, this ratio is determined by dividing the investment in the contract as found under §1.72-6 by the expected return under such contract as found under §1.72-5. Where a single consideration is given for a particular contract which provides for two or more annuity elements, an exclusion ratio shall be determined for the contract as a whole by dividing the investment in such contract by the aggregate of the expected returns under all the annuity elements provided thereunder. However, where the provisions of paragraph (b)(3) of §1.72-2 apply to payments received under such a contract, see paragraph (b)(3) of §1.72-6.

In the case of a contract to which §1.72-6(d) (relating to contracts in which amounts were invested both before July 1, 1986, and after June 30, 1986) applies, the exclusion ratio for purposes of this paragraph (a) is determined in accordance with §1.72-6(d) and, in particular, §1.72-6(d)(5)(i).

(ii) The exclusion ratio for the particular contract is then applied to the total amount received as an annuity during the taxable year by each recipient. See, however, paragraph (e)(3) of §1.72.5. Any excess of the total amount received as an annuity during the taxable year over the amount determined by the application of the exclusion ratio to such total amount shall be included in the gross income of the recipient for the taxable year of receipt.

(2) The principles of subparagraph (1) may be illustrated by the following example:

Example. Taxpayer A purchased an annuity contract providing for payments of $100 per month for a consideration of $12,650. Assuming that the expected return under this contract is $16,000, the exclusion ratio to be used by A is $12,650 ÷ $16,000; or 79.1 percent (79.06 rounded to the nearest tenth). If 12 such monthly payments are received by A during this taxable year, the total amount he may exclude from his gross income in such year is $949.20 ($1,200 × 79.1 percent). The balance of $250.80 ($1,200 less $949.20) is the amount to be included in gross income. If A instead received only five such payments during the year, he should exclude $395.50 ($500 × 79.1 percent) of the total amounts received.

For an example of the computation of the exclusion ratio in cases where two annuity elements are acquired for a single consideration, see paragraph (b)(1) of §1.72-6.

(3) The exclusion ratio shall be applied only to amounts received as an annuity within the meaning of that term under paragraph (b)(2) and (3) of §1.72-2. Where the periodic payments increase in amount after the annuity starting date in a manner not provided by the terms of the contract at such date, the portion of such payments representing the increase is not an amount received as an annuity. For the treatment of amounts not received as an annuity, see section 72(e) and §1.72-11. For special rules where paragraph (b)(3) of §1.72-2 applies to amounts received, see paragraph (d)(3) of this section.

(4) After an exclusion ratio has been determined for a particular contract, it shall be applied to any amounts received as an annuity thereunder unless or until one of the following occurs:

(i) The contract is assigned or transferred for a valuable consideration (see section 72(g) and paragraph (a) of §1.72-10);

(ii) The contract matures or is surrendered, redeemed, or discharged in accordance with the provisions of paragraph (c) or (d) of §1.72-11;

(iii) The contract is exchanged (or is considered to have been exchanged) in a manner described in paragraph (e) of §1.72-11.

* * * * *

(d) *Exceptions to the general rule.* (1) Where the provisions of section 72 would otherwise require an exclusion ratio to be determined, but the investment in the contract (determined under §1.72-6) is an amount of zero or less, no exclusion ratio shall be determined and all amounts received under such a contract shall be includible in the gross income of the recipient for the purposes of section 72.

(2) Where the investment in the contract is equal to or greater than the total expected return under such contract found under §1.72-5, the exclusion ratio shall be considered to be 100 percent and all amounts received as an annuity under such contract shall be excludable from the recipient's gross income. See, for example, paragraph (f)(1) of §1.72-5.

In the case of a contract to which §1.72-6(d) (relating to contracts in which amounts were invested both before July 1, 1986, and after June 30, 1986) applies, this paragraph (d)(2) is applied in the manner prescribed in §1.72-6(d) and, in particular, §1.72-6(d)(5)(ii).

(3) (i) If a contract provides for payments to be made to a taxpayer in the manner described in paragraph (b)(3) of §1.72-2, the investment in the contract shall be considered to be equal to the expected return under such contract and the resulting exclusion ratio (100%) shall be applied to all amounts received as an annuity under such contract. For any taxable year, payments received under such a contract shall be considered to be amounts received as an annuity only to the extent that they do not exceed the portion of the investment in the contract which is properly allocable to that year and hence excludable from gross income as a return of premiums or other consideration paid for the contract. The portion of the investment in the contract which is properly allocable to any taxable year shall be determined by dividing the investment in the con-

tract (adjusted for any refund feature in the manner described in paragraph (d) of §1.72-7) by the applicable multiple (whether for a term certain, life, or lives) which would otherwise be used in determining the expected return for such a contract under §1.72-5. The multiple shall be adjusted in accordance with the provisions of the table in paragraph (a)(2) of §1.72-5, if any adjustment is necessary, before making the above computation. If payments are to be made more frequently than annually and the number of payments to be made in the taxable year in which the annuity begins are less than the number of payments to be made each year thereafter, the amounts considered received as an annuity (as otherwise determined under the subdivision) shall not exceed, for such taxable year (including a short taxable year), an amount which bears the same ratio to the portion of the investment in the contract considered allocable to each taxable year as the number of payments to be made in the first year bears to the number of payments to be made in each succeeding year. Thus, if payments are to be made monthly, only seven payments will be made in the first taxable year, and the portion of the investment in the contract allocable to a full year of payments is $600, the amounts considered received as an annuity in the first taxable year cannot exceed $350 ($600 × 7/12). See subdivision (iii) of this subparagraph for an example illustrating the determination of the portion of the investment in the contract allocable to one taxable year of the taxpayer.

(ii) If subdivision (i) of this subparagraph applies to amounts received by a taxpayer and the total amount of payments he receives in a taxable year is less than the total amount excludable for such year under subdivision (i) of this subparagraph, the taxpayer may elect, in a suceeding taxable year in which he receives another payment, to redetermine the amounts to be received as an annuity during the current and succeeding taxable years. This shall be computed in accordance with the provisions of subdivision (i) of this subparagraph except that:

(a) The difference between the portion of the investment in the contract allocable to a taxable year, as found in accordance with subdivision (i) of this subparagraph, and the total payments actually received in the taxable year prior to the election shall be divided by the applicable life expectancy of the annuitant (or annuitants), found in accordance with the appropriate table in §1.72-9 (and adjusted in accordance with paragraph (a)(2) of §1.72-5), or by the remaining term of a term certain annuity, computed as of the first day of the first period for which an amount is received as an annuity in the taxable year of the election; and

(b) The amount determined under *(a)* of this subdivision shall be added to the portion of the investment in the contract allocable to each taxable year (as otherwise found). To the extent that the total periodic payments received under the contract in the taxable year of the election or any succeeding taxable year does not equal this total sum, such payments shall be excludable from the gross income of the recipient. To the extent such payments exceed the sum so found, they shall be fully includable in the recipient's gross income.

See subdivision (iii) of this subparagraph for an example illustrating the redetermination of amounts to be received as an annuity and subdivision (iv) of this subparagraph for the method of making the election provided by this subdivision.

(iii) The application of the principles of paragraph (d)(3)(i) and (ii) of this section may be illustrated by the following example:

Example. Taxpayer A, a 64 year old male, files his return on a calendar year basis and has a life expectancy of 15.6 years on June 30, 1954, the annuity starting date of a contract to which §1.72-2(b)(3) applies and which he purchased for $20,000. The contract provides for variable annual payments for his life. He receives a payment of $1,000 of June 30, 1955, but receives no other payment until June 30, 1957. He excludes the $1,000 payment from his gross income for the year 1955 since this amount is less than $1,324.50, the amount determined by dividing his investment in the contract ($20,000) by his life expectancy adjusted for annual payments, 15.1 (15.6 − 0.5), as of the original annuity starting date. Taxpayer A may elect, in his return for the taxable year 1957, to redetermine amounts to be received as an annuity under his contract as of June 30, 1956. For the purpose of determining the extent to which amounts received in 1957 or thereafter shall be considered amounts received as an annuity (to which a 100 percent exclusion ratio shall apply) he shall add $118.63 to the $1,324.50 originally determined to be receivable as an annuity under the contract, making a total of $1,443.13. This is determined by dividing the difference between what was excludable in 1955 and 1956, $2,649 (2 × $1,324.50) and what he actually received in those years ($1,000) by his life expectancy adjusted for annual payments, 13.9 (14.4 − 0.5), as of his age at his nearest birthday (66) on the first day of the first period for which he received an amount as an annuity in the taxable year of election (June 30, 1956). The result, $1,443.13, is excludable in that year and each year thereafter as an amount received as an annuity to which the 100% exclusion ratio applies. It will be noted that in this example the taxpayer received amounts less than the excludable amounts in two successive years and deferred making his election until the third year, and thus was able to accumulate the portion of the investment in the contract allocable to each taxable year to the extent he failed to receive such portion in both years. Assuming that he received $1,500 in the taxable year of his election, he would include $56.87 in his gross income and exclude $1,443.13 therefrom for that year.

(iv) If the taxpayer chooses to make the election described in subdivision (ii) of this subparagraph, he shall file with his return a statement that he elects to make a redetermination of the amounts excludable from gross income under his annuity contract in accordance with the provisions of paragraph (d)(3) of §1.72-4. This statement shall also contain the following information:

(a) The original annuity starting date and his age on that date,

(b) The date of the first day of the first period for which he received an amount in the current taxable year,

(c) The investment in the contract originally determined (as adjusted for any refund feature), and

(d) The aggregate of all amounts received under the contract between the date indicated in *(a)* of this subdivision and the day after the date indicated in *(b)* of this subdivision to the extent such amounts were excludable from gross income.

He shall include in gross income any amounts received during the taxable year for which the return is made in accordance with the redetermination made under this subparagraph.

(v) In the case of the contract to which §1.72-6(d) (relating to contracts in which amounts were invested both before July 1, 1986, and after June 30, 1986) applies, this paragraph (d)(3) is applied in the manner prescribed in §1.72-6(d) and, in particular, §1.72-6(d)(5)(iii). This application may be illustrated by the following example:

Example. B, a male calendar year taxpayer, purchases a contract which provides for variable annual payments for life and to which §1.72-2(b)(3) applies. The annuity starting date of the contract is June 30, 1990, when B is 64 years old. B receives a payment of $1,000 on June 30, 1991, but receives no other payment until June 30, 1993. B's total investment in the contract is $25,000. B's pre-July 1986 investment in the contract is $12,000. If B makes the election described in §1.72-6(d)(6), separate computations are required to determine the amounts received as an annuity and excludable from gross income with respect to the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract. In the separate computations, B first determines the applicable portions of the total payment received which are allocable to the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract. The portion of the payment received allocable to the pre-July 1986 investment in the contract is $480 ($12,000/$25,000 × $1,000). The portion of the payment received allocable to the post-June 1986 investment in the contract is $520 ($13,000/$25,000 × $1,000). Second, B determines the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract allocable to the taxable year by dividing the pre-July 1986 and post-June 1986 investments in the contract by the applicable life expectancy multiple. The life expectancy multiple applicable to pre-July 1986 investment in the contract is B's life expectancy as of the original annuity starting date adjusted for annual payments and is determined under Table I of §1.72-9 (15.1 (15.6 − 0.5)). The life expectancy multiple applicable to post-June 1986 investment in the contract is determined under Table V of §1.72-9 (20.3 (20.8 − 0.5)). Thus, the pre-July 1986 investment in the contract allocable to each taxable year is $794.70 ($12,000 ÷ 15.1), and the post-June 1986 investment in the contract so allocable is $640.39 ($13,000 ÷ 20.3). Because the applicable portions of the total payment received in 1991 under the contract ($480 allocable to the pre-July 1986 investment in the contract and $520 allocable to the post-June 1986 investment in the contract) are treated as amounts received as an annuity and are excludable from gross income to the extent they do not exceed the portion of the corresponding investment in the contract allocable to 1991 ($794.70 pre-July 1986 investment in the contract and $640.39 post-June 1986 investment in the contract), the entire amount of each applicable portion of the total payment is excludable from gross income. B may elect, in the return filed for taxable year 1993, to redetermine amounts to be received as an annuity under the contract as of June 30, 1992. The extent to which the amounts received in 1993 or thereafter shall be considered amounts received as an annuity is determined as follows:

Pre-July 1986 investment in the contract allocable to taxable years 1991 and 1992 ($794.70 × 2) ..	$1,589.40
Less: Portion of total payments allocable to pre-July 1986 investment in the contract actually received as an annuity in taxable years 1991 and 1992	$ 480.00
	$1,109.40
Divided by: Life expectancy multiple applicable to pre-July 1986 investment in the contract for B, age 66 (14.4 − 0.5)	13.9
	79.81
Plus: Amount originally determined with respect to pre-July 1986 investment in the contract	$ 794.70
Pre-July 1986 amount	$ 874.51
Post-June 1986 investment in the contract allocable to taxable years 1991 and 1992 ($640.39 × 2) ..	$1,280.78
Less: Portion of total payments allocable to post-June 1986 investment in the contract actually received as an annuity in taxable years 1991 and 1992	$ 520.00
	$ 760.78
Divided by: Life expectancy multiple applicable to post-June 1986 investment in the contract for B, age 66 (19.2 − 0.5)	18.7
	40.68
Plus: Amount originally determined with respect to post-June 1986 investment in the contract	$ 640.39
Post-June 1986 amount	$ 681.07

(vi) The method of making an election to perform the separate computations illustrated in paragraph (d)(3)(v) of this section is described in §1.72-6(d)(6).

(e) *Exclusion ratio in the case of two or more annuity elements acquired for a single consideration.* (1)(i) Where two or more annuity elements are provided under a contract described in paragraph (a)(2) of §1.72-2, an exclusion ratio shall be detrmined for the contract as a whole and applied to all amounts received as an annuity under any of the annuity elements. To obtain this ratio, the investment in the contract determined in accordance with §1.72-6 shall be divided by the aggregate of the expected returns found with respect to each of the annuity elements in accordance with §1.72-5. For this purpose, it is immaterial that payments under one or more of the annuity elements involved have not commenced at the time when an amount is first received as an annuity under one or more of the other annuity elements.

(ii) The exclusion ratio found under subdivision (i) of this subparagraph does not apply to:

(*a*) An annuity element payable to a surviving annuitant under a joint and survivor annuity contract to which section 72(i) and paragraphs (b)(3) and (e)(3) of §1.72-5 apply, or to

(*b*) A contract under which one or more of the constituent annuity elements provides for payments described in paragraph (b)(3) of §1.72-2.

For rules with respect to a contract providing for annuity elements described in (*b*) of this subdivision, see subparagraph (2) of this paragraph.

(2) If one or more of the annuity elements under a contract described in paragraph (a)(2) of §1.72-2 provides for payments to which paragraph (b)(3) of §1.72-2 applies:

(i) With respect to the annuity elements to which paragraph (b)(3) of §1.72-2 does not apply, an exclusion ratio shall be determined by dividing the portion of the investment in the entire contract which is properly allocable to all such elements (in the manner provided in paragraph (b)(3)(ii) of §1.72-6) by the aggregate of the expected returns thereunder and such ratio shall be applied in the manner described in subdivision (i) of subparagraph (1); and

(ii) With respect to the annuity elements to which paragraph (b)(3) of §1.72-2 does apply, the investment in the entire contract shall be reduced by the portion thereof found in subdivision (i) of this subparagraph and the resulting amount shall be used to determine the extent to which the aggregate of the payments received during the taxable year under all such elements is excludable from gross income. The amount so excludable shall be allocated to each recipient under such elements in the same ratio that the total of the payments he receives each year bears to the total of the payments received by all such recipients during the year. The exclusion ratio with respect to the amounts so allocated shall be 100 percent. See paragraph (f)(2) of §1.72-5 and paragraph (b)(3) of §1.72-6.

(iii) In the case of a contract to which §1.72-6(d) (relating to contracts in which amounts were invested both before July 1, 1986, and after June 30, 1986) applies, this paragraph (e) is applied in the manner prescribed in §1.72-6(d) and, in particular, §1.72-6(d)(5)(iv).

Par. 3. Section 1.72-5 is amended by revising paragraphs (a), (b), and (e), and adding a new paragraph (g) to read as follows:

§1.72-5 Expected return

(a) *Expected return for but one life.* (1) If a contract to which section 72 applies provides that one annuitant is to receive a fixed monthly income for life, the expected return is determined by multiplying the total of the annuity payments to be received annually by the multiple shown in Table I or V (whichever is applicable) of §1.72-9 under the age (as a annuity starting date) and, if applicable, sex of the measuring life (usually the annuitant's). Thus, where a male purchases a contract before July 1, 1986, providing for an immediate annuity of $100 per month for his life and, as of the annuity starting date (in this case the date of purchase), the annuitant's age at his nearest birthday is 66, the expected return is computed as follows:

Monthly payment of $100 × 12 months equals annual payment of	$1,200
Multiple shown in Table I, male, age 66.	14.4
Expected return ($1,200 × 14.4) . . .	17,280

If, however, the taxpayer had purchased the contract after June 30, 1986, the expected return would be $23,040, determined by multiplying 19.2 (multiple shown in Table V, age 66) by $1,200.

(2)(i) If payments are to be made quarterly, semiannually, or annually, an adjustment of the applicable multiple shown in Table I or V (whichever is applicable) may be required. A further adjustment may be required where the interval between the annuity starting date and the date of the first payment is less than the interval between future payments. Neither adjustment shall be made, however, if the payments are to be made more frequently than quarterly. The amount of the adjustment, if any, is to be found in accordance with the following table:

If the number of whole months from the annuity starting date to the first payment date is—	0–1	2	3	4	5	6	7	8	9	10	11	12
And payments under the contract are to be made: Annually . . .	+0.5	+0.4	+0.3	+0.2	+0.1	0	0	−0.1	−0.2	−0.3	−0.4	−0.5
Semiannually	+.2	+.1	0	0	−.1	−.2	...	...	...	...	...	...
Quarterly . .	+.1	0	−.1	...	...	...	...	...	...	...	...	...

Thus, for a male, age 66, the multiple found in Table I, adjusted for quarterly payments the first of which is to be made one full month after the annuity starting date, is 14.5 (14.4 + 0.1); for semiannual payments the first of which is to be made six full months from the annuity starting date, the adjusted multiple is 14.2 (14.4 − 0.2); for annual payments the first of which is to be made one full month from the annuity starting date, the adjusted multiple is 14.9 (14.4 + 0.5). If the annuitant in the example shown in subparagraph (1) of this paragraph were to receive an annual payment of $1,200 commencing 12 full months after his annuity starting date, the amount of the expected return would be $16,680 ($1,200 × 13.9 [14.4 − 0.5]). Similarly for an annuitant, age 50, the multiple found in Table V, adjusted for quarterly payments the first of which is to be made one full month after the annuity starting date, is 33.2 (33.1 + 0.1); for semi-annual payments the first of which is to be made six full months from the annuity starting date, the adjusted multiple is 32.9 (33.1 − 0.2); for annual payments the first of which is to be made one full month from the annuity starting date, the adjusted multiple is 33.6 (33.1 + 0.5).

(ii) Notwithstanding the table in subdivision (i) of this subparagraph, adjustments of multiples for early or other than monthly payments determined prior to February 19, 1956, under the table prescribed in paragraph 1(b)(4) of T.D. 6118 (19 FR 9897, 1955-1 C.B. 699), approved December 30, 1954, need not be redetermined.

(3) If the contract provides for fixed payments to be made to an annuitant until death or until the expiration of a specified limited period, whichever occurs earlier, the expected return of such temporary life annuity is determined by multiplying the total of the annuity payments to be received annually by the multiple shown in Table IV or VIII (whichever is applicable) of §1.72-9 for the age (as of the annuity starting date) and, if applicable, sex of the annuitant and the nearest whole number of years in the specified period. For example, if a male annuitant, age 60 (at his nearest birthday), is to receive $60 per month for five years or until he dies, whichever is earlier, and there is no post-June 1986, investment in the contract, the expected return under such a contract is $3,456, computed as follows:

Monthly payments of $60 × 12 months equals annual payment of	$720
Multiple shown in Table IV for male, age 60, for term of 5 years	4.8
Expected return for 5 year temporary life annuity of $720 per year ($720 × 4.8)	$3,456

If the annuitant purchased the same contract after June 30, 1986, the expected return under the contract would be $3,528, computed as follows:

Monthly payments of $60 × 12 months equals annual payment of	$720.00
Multiple shown in Table VIII for annuitant, age 60, for term of 5 years	4.9
Expected return for 5-year temporary life annuity of $720 per year ($720 × 4.9)	$3,528.00

The adjustment provided by subparagraph (2) of this paragraph shall not be made with respect to the multiple found in Table IV or VIII (whichever is applicable).

(4) If the contract provides for payments to be made to an annuitant for the annuitant's lifetime, but the amount of the annual payments is to be decreased after the expiration of a specified limited period, the expected return is computed by considering the contract as a combination of a whole life annuity for the smaller amount plus a temporary life annuity for an amount equal to the difference between the larger and the smaller amount. For example, if a male annuitant, age 60, is to receive $150 per month for five years or until his earlier death, and is to receive $90 per month for the remainder of his lifetime after such five years, the expected return is computed as if the annuitant's contract consisted of a whole life annuity for $90 per month plus a five year temporary life annuity of $60 per month. In such circumstances, the expected return if there is no post-June 1986 investment in the contract is computed as follows:

Monthly payments of $90 × 12 months equals annual payment	$ 1,080
Multiple shown in Table I for male, age 60	18.2

Expected return for whole life annuity of $1,080 per year	$19,656
Expected return for 5-year temporary life annuity of $720 per year (as found in subparagraph (3) of this paragraph (a))	$ 3,456
Total expected return	$23,112

If the annuitant purchased the same contract after June 30, 1986, the expected return would be $29,664, computed as follows:

Monthly payments of $90 × 12 months equals annual payment of	$ 1,080
Multiple shown in Table V for annuitant, age 60	24.2
Expected return for whole life annuity of $1,080 per year	$26,136
Plus:	
Expected return for 5-year temporary life annuity of $720 per year (as found in subparagraph (3) of this paragraph (a))	$ 3,528
Total expected return	$29,664

If payments are to be made quarterly, semiannually, or annually, an appropriate adjustment of the multiple found in Table I or V (whichever is applicable) for the whole life annuity should be made in accordance with subparagraph (2) of this paragraph.

(5) If the contract described in subparagraph (4) of this paragraph provided that the amount of the annual payments to the annuitant were to be increased (instead of decreased) after the expiration of a specified limited period, the expected return would be computed as if the annuitant's contract consisted of a whole life annuity for the larger amount minus a temporary life annuity for an amount equal to the difference between the larger and smaller amount. Thus, if the annuitant described in subparagraph (4) of this paragraph were to receive $90 per month for five years or until his earlier death, and to receive $150 per month for the remainder of his lifetime after such five years, the expected return would be computed by subtracting the expected return under a five year temporary life annuity of $60 per month from the expected return under a whole life annuity of $150 per month. In such circumstances, the expected return if there is no post-June 1986 investment in the contract is computed as follows:

Monthly payments of $150 × 12 months equals annual payment of	$1,800
Multiple shown in Table 1 (male, age 60)	18.2
Expected return for annuity for whole life of $1,800 per year	$32,760
Less expected return for 5-year temporary life annuity of $720 per year (as found in subparagraph (3))	$3,456
Net expected return	$29,304

If the annuitant purchased the same contract after June 30, 1986, the expected return would be $40,032, computed as follows:

Monthly payments of $150 × 12 months equals annual payments of	$ 1,800
Multiple shown in Table V (age 60)	24.2
Expected return for annuity for whole life of $1,800 per year	$43,560
Less expected return for 5-year temporary life annuity of $720 per year (as found in subparagraph (3) of this paragraph (a))	$ 3,528
Net expected return	$40,032

If payments are to be made quarterly, semiannually, or annually, an appropriate adjustment of the multiple found in Table I or V (whichever is applicable) for the whole life annuity should be made in accordance with subparagraph (2) of this paragraph.

(b) *Expected return under joint and survivor and joint annuities.* (1) In the case of a joint and survivor annuity contract involving two annuitants which provides the first annuitant with a fixed monthly income for life and, after the death of the first annuitant, provides an identical monthly income for life to a second annuitant, the expected return shall be determined by multiplying the total amount of the payments to be received annually by the multiple obtained from Table II or V! (whichever is applicable) of §1.72-9 under the ages (as of the annuity starting date) and, if applicable, sexes of the living annuitants. For example, a husband purchases a joint and survivor annuity contract providing for payments of $100 per month for life and, after his death, for the same amount to his wife for the remainder of her life. As of the annuity starting date his age at his nearest birthday is 70 and that of his wife at her nearest birthday is 67. If there is no post-June 1986 investment in the contract, the expected return is computed as follows:

Monthly payments of $100 × 12 month equals annual payment of	$1,200
Multiple shown in Table II (male, age 70, female, age 67)	19.7
Expected return ($1,200 × 19.7)	$23,640

If the annuitants purchased the same contract after June 30, 1986, the expected return would be $26,400, computed as follows:

Monthly payments of $100 × 12 equals annual payment of	$ 1,200
Multiple shown in Table VI (ages 70, 67)	22.0
Expected return ($1,200 × 22.0)	$26,400

If payments are to be made quarterly, semiannually, or annually, an appropriate adjustment of the multiple found in Table II or VI (whichever is applicable) should be made in accordance with paragraph (a)(2) of this section.

(2) If a contract of the type described in subparagraph (1) of this paragraph provides that a different (rather than an identical) monthly income is payable to the second annuitant, the expected return is computed in the following manner. The applicable multiple in Table II or VI (whichever is applicable) is first found as in the example in subparagraph (1) of this paragraph. The multiple applicable to the first annuitant is then found in Table I or V (whichever is applicable) as though the contract were for a single life annuity. The multiple from Table I or V is then subtracted from the multiple obtained from Table II or VI and the resulting multiple is applied to the total payments to be received annually under the contract by the second annuitant. The result is the expected return with respect to the second annuitant. The portion of the expected return with respect to payments to be made during the first annuitant's life is then computed by applying the multiple found in Table I or V to the total annual payments to be received by such annuitant under the contract. The expected returns with respect to each of the annuitants separately are then aggregated to obtain the expected return under the entire contract.

Example (1). A husband purchases a joint and survivor annuity providing for payments of $100 per month for his life and, after his death, payments to his wife of $50 per month for her life. As of the annuity starting date his age at his nearest birthday is 70 and that of his wife at her nearest birthday is 67. There is no post-June 1986 investment in the contract.

Multiple from Table II (male, age 70; female, age 67)	19.7
Multiple from Table (male, age 70)	12.1
Difference (multiple applicable to second annuitant)	7.6

Portion of expected return, second annuitant ($600 × 7.6)	$4,560
Portion of expected return, first annuitant ($1,200 × 12.1)	$14,520
Expected return under the contract	$19,080

The expected return thus found, $19,080, is to be used in computing the amount to be excluded from gross income. Thus, if the investment in the contract in this example is $14,310, the exclusion ratio is $14,310 ÷ $19,080; or 75 percent. The amount excludable from each monthly payment made to the husband is 75 percent of $100, or $75, and the remaining $25 of each payment received by him shall be included in his gross income. After the husband's death, the amount excludable by the second annuitant (the surviving wife) would be 75 percent of each monthly payment of $50, or $37.50, and the remaining $12.50 of each payment shall be included in her gross income.

Example (2). If the same contract were purchased after June 30, 1986, the expected return would be $22,800, computed as follows:

Multiple from Table VI (ages 70, 67)	22.0
Multiple from Table V (age 70) ..	16.0
Difference (multiple applicable to second annuitant)	6.0
Portion of expected return, second annuitant ($600 × 6.0)	$ 3,600
Plus Portion of expected return, first annuitant ($1,200 × 16.0) .	19,200
Expected return under the contract	$22,800

If the investment in the contract is $14,310, the exclusion ratio is $14,310 ÷ $22,800, or 62.8 percent. Thus, the husband would exclude $62.80 of each $100 payment received by him. After his death, his wife would exclude 62.8 percent, or $31.40 of each $50 monthly payment.

Example (3). If amounts were invested in the same contract both before July 1, 1986, and after June 30, 1986, and the election described in §1.72-6(d)(6) were made, two exclusion ratios would be determined pursuant to §1.72-6(d). Assume that the husband's total investment in the contract is $14,310 and that $7,310 is the pre-July 1986 investment in the contract. The pre-July 1986 exclusion ratio would be $7,310 ÷ $19,080, or 38.3 percent. The post-June 1986 exclusion ratio would be $7,000 ÷ $22,800, or 30.7 percent. The husband would exclude $69.00 ($38.30 + $30.70) of the $100 monthly payment received by him. The remaining $31.00 would be included in his gross income. After the husband's death, the amount excludable by his wife would be $34.50 (38.3 percent of $50 plus 30.7 percent of $50). The remaining $15.50 would be included in gross income.

The same method is used if the payments are to be increased after the death of the first annuitant. Thus, if the payments to be made until the husband's death were $50 per month and his widow were to receive $100 per month thereafter until her death, the 7.6 multiple in example (1) above would be applied to the $100 payments, yielding an expected return with respect to this portion of the annuity contract of $9,120 ($1,200 × 7.6). An expected return of $7,260 ($600 × 12.1) would be obtained with respect to the payments to be made to the husband, yielding a total expected return under the contract of $16,380 ($9,120 plus $7,260). If payments are to be made quarterly, semiannually, or annually, an appropriate adjustment of the multiples found in Tables I and II or Tables V and VI (whichever is applicable) should be made in accordance with paragraph (a)(2) of this section.

(3) In the case of a joint and survivor annuity contract in respect of which the first annuitant died in 1951, 1952, or 1953, and the basis of the surviving annuitant's interest in the contract was determinable under section 113(a)(5) of the Internal Revenue Code of 1939, such basis shall be considered the "aggregate of premiums or other consideration paid" by the surviving annuitant for the contract. (For rules governing this determination, see 26 CFR (1939) 39.22(b)(2)-2 and 39.113(a)(5)-1 (Regulations 113).) In determining such an annuitant's investment in the contract, such aggregate shall be reduced by any amounts received under the contract by the surviving annuitant before the annuity starting date, to the extent such amounts were excludable from his gross income at the time of receipt. The expected return of the surviving annuitant in such cases shall be determined in the manner prescribed in paragraph (a) of this section, as though the surviving annuitant alone were involved. For this purpose, the appropriate multiple for the survivor shall be obtained from Table I as of the annuity starting date determined in accordance with paragraph (b)(2)(i) of §1.72-4.

(4) If a contract involving two annuitants provides for fixed monthly payments to be made as a joint life annuity until the death of the first annuitant to die (in other words, only as long as both remain alive), the expected return under such contract shall be determined by multiplying the total of the annuity payments to be received annually under the contract by the multiple obtained from Table IIA or VIA (whichever is applicable) of §1.72-9 under the ages (as of the annuity starting date) and, if applicable, sexes of the annuitants. If, however, payments are to be made under the contract quarterly, semiannually, or annually, an appropriate adjustment of the multiple found in Table IIA or VIA shall be made in accordance with paragraph (a)(2) of this section.

(5) If a joint and survivor annuity contract involving two annuitants provides that a specified amount shall be paid during their joint lives and a different specified amount shall be paid to the survivor upon the death of whichever of the annuitants is the first to die, the following preliminary computation shall be made in all cases preparatory to determining the expected return under the contract:

(i) From Table II or VI (whichever is applicable), obtain the multiple under both of the annuitants' ages (as of the annuity starting date) and, if applicable, their appropriate sexes;

(ii) From Table IIA, or VIA (whichever is applicable), obtain the multiple applicable to both annuitants' ages (as of the annuity starting date) and, if applicable, their appropriate sexes;

(iii) Apply the multiple found in subdivision (i) of this subparagraph to the total of the amounts to be received annually after the death of the first to die; and

(iv) Apply the multiple found in subdivision (ii) of this subparagraph to the difference between the total of the amounts to be received annually before and the total of the amounts to be received annually after the death of the first to die.

If the original annual payment is in excess of the annual payment to be made after the death of the first to die, the expected return is the sum of the amounts determined under subdivisions (iii) and (iv) of this subparagraph. This may be illustrated by the following examples:

Example (1). A husband purchases a joint and survivor annuity providing for payments of $100 a month for as long as both he and his wife live, and, after the death of the first to die, payments to the survivor of $75 a month for life. As of the annuity starting date, his age at his nearest birthday is 70 and that of his wife at her nearest birthday is 67. If there is no post-June 1986 investment in the contract, the expected return under the contract is computed as follows:

Multiple from Table II (male, age 70; female, age 67)	19.7
Multiple from Table IIA (male, age 70; female, age 67)	9.3
Portion of expected return ($900 × 19.7—sum per year after first death)	$17,730
Portion of expected return ($300 × 9.3—amount of change in sum at first death)	$ 2,790
Expected return under the contract	$20,520

The total expected return in this example, $20,520, is to be used in computing the amount to be excluded from gross income. Thus, if the investment in the contract is $17,887, the exclusion ratio is $17,887 ÷ $20,520, or 87.2 percent. The amount excludable from each monthly payment made while both are alive is 87.2 percent of $100, or $87.20, and the remaining $12.80 of each payment shall be included in gross income. After the death of the first to die, the amount excludable by the survivor shall be 87.2 percent of each monthly payment of $75, or $65.40, and the remaining $9.60 of each payment shall be included in gross income.

Example (2). Assume the same facts as in example (1), except that the contract is purchased after June 30, 1986.

The expected return under the contract is computed as follows:

Multiple from Table VI (ages 70, 67)	22.0
Multiple from Table VIA (ages 70, 67)	12.4
Portion of expected return ($900 × 22.0—sum per year after first death)	$19,800
Plus: Portion of expected return ($300 × 12.4—amount of change in sum at first death) ..	$ 3,720
Expected return under the contract	$23,520

Thus, if the investment in the contract is $17,887, the exclusion ratio is $17,887 ÷ $23,520, or 76.1 percent. The amount excludable from each monthly payment made while both are alive would be 76.1 percent of $100, or $76.10, and the remaining $23.90 of each payment would be included in gross income. After the death of the first to die, the amount excludable by the survivor would be 76.1 percent of each monthly payment of $75, or $57.08, and the remaining $17.92 of each payment would be included in gross income.

Example (3). Assume the same facts as in examples (1) and (2), except that the total investment in the contract is $17,887, and that the pre-July 1986 investment in the contract is $8,000. Assume also that one of the annuitants makes the election described in §1.72-6(d)(6). Separate computations shall be performed pursuant to §1.72-6(d) to determine the amount excludable from gross income. The pre-July 1986 exclusion ratio would be $8,000 ÷ $23,520, or 34 percent. The post-June 1986 exclusion ratio would be $9,887 ÷ $23,520, or 42 percent. The amount excludable from each monthly payment made while both are alive would be $76 ((.34 × 100) + (.42 × 100)), and the remaining $24 of each $100 payment would be included in gross income. After the death of the first to die, the amount excludable by the survivor would be $57.60 of each monthly payment of $75 ((.34 × 75) + (.42 × 75)), and the remaining $18.00 of each payment would be included in gross income.

If the original annual payment is less than the annual payment to be made after the death of the first to die, the expected return is the difference between the amounts determined under subdivisions (iii) and (iv) of this subparagraph. If, however, payments are to be made quarterly, semiannually, or annually under the contract, the multiples obtained from both Tables II and IIA or Tables VI and VIA (whichever are applicable) shall first be adjusted in a manner prescribed in paragraph (a)(2) of this section.

(6) If a contract provides for the payment of life annuities to two persons during their respective lives and, after the death of one (without regard to which one dies first), provides that the survivor shall receive for life both his own annuity payments and the payments made formerly to the deceased person, the expected return shall be determined in accordance with paragraph (e)(4) of this section.

(7) If paragraph (b)(3) of §1.72-2 applies to payments provided under a contract and this paragraph applies to such payments, the principles of this paragraph shall be used in making the computations described in paragraph (d)(3) of §1.72-4. This may be illustrated by the following examples, examples (1) through (3) of which assume that there is no post-June 1986 investment in the contract:

Example (1). Taxpayer A, a male age 63, pays $24,000 for a contract which provides that the proceeds (both income and return of capital) from eight units of an investment fund shall be paid monthly to him for his life and that after his death the proceeds from six such units shall be paid monthly to B, a female age 55, for her life. The portion of the investment in the contract allocable to each taxable year of A is $955.20 and that allocable to each taxable year of B is $716.40. This is determined in the following manner:

Multiple from Table II (male, age 63; and female, age 55)	28.1
Number of units to be paid, in effect, as a joint and survivor annuity ...	×6
Number of total annual unit payments anticipatable with respect to the joint and survivor annuity element	168.6
Multiple from Table I (male, age 63)	16.2
Number of units to be paid, in effect, as a single life annuity	× 2
Number of total annual unit payments anticipatable with respect to A alone	32.4
Total number of unit payments anticipatable	201
Portion of investment in the contract allocable to unit payments ($24,000 ÷ 201) on an annual basis	$119.40
Number of units payable to A while he continues to live	×8
Portion of the investment in the contract allocable to each taxable year of A	$955.20
Portion of investment in the contract allocable to unit payments ($24,000 ÷ 201) on an annual basis	$119.40
Number of units payable to B for her life after A's death	×6
Portion of the investment in the contract allocable to each taxable year of B	$716.40

For the purpose of the above computation it is immaterial whether or not A lives to or beyond the life expectancy shown for him in Table I.

Example (2). Assume that Taxpayer A in example (1) receives payments for five years which are at least as large as the portion of the investment in the contract allocable to such years, but in the sixth year he receives a total of only $626.40 rather than the $955.20 allocable to such year. A is 69 and B is 61 at the beginning of the first monthly period for which an amount is payable in the seventh taxable year. A makes the election in that year provided under paragraph (d)(3) of §1.72-4. The difference between the portion of the investment in the contract allocable to the sixth year and the amount actually received in that year is $328.80 ($955.20 less $626.40). In this case, 139.2 unit payments are anticipatable (on an annual basis), since the appropriate multiple from Table II of §172-9, 23.2, multiplied by the number of units payable, in effect, as a joint and survivor annuity yields this result (6 × 23.2). A's appropriate multiple from Table I of §1.72-9 for the two units which will cease to be paid at his death is 12.6, and the total number of unit payments anticipatable (on an annual basis) is, therefore, 164.4 (2 × 12.6 plus 139.2). Dividing the difference previously found ($328.80) by the total number of unit payments thus determined (164.4) indicates that A will have an additional allocation of the investment in the contract of $16 to the seventh and every succeeding full taxable year (8 units × $2), and B will have an additional allocation of the investment in the contract of $12 (6 units × $2) to each taxable year in which she receives 12 monthly payments subsequent to the death of A. The total allocable to each taxable year of A is therefore, $971.20, and that allocable to each taxable year of B will be $728.40.

Example (3). If, in example (2), A had died at the end of the fifth year, in the sixth year B would have received a payment of $469.80 (that portion of the $626.40 that A would have received which is in the same ratio that 6 units bear to 8 units) and would thus have received $246.60 less than the portion of the investment in the contract originally determined to be allocable to each of her taxable years. In these circumstances, B would be entitled to elect to redetermine the portion of the investment in the contract allocable to the taxable year of election and all subsequent years. The new amount allocable thereto would be found by dividing the $246.60 difference by her life expectancy as of the first day of the first period for which she received an amount as an annuity in the seventh year of the annuity contract, and adding the result to her originally determined allocation of $716.40.

Example (4). On July 1, 1986, Taxpayer C, age 60, pays $28,000 for a contract which provides that the proceeds (both income and return of capital) from 10 units of an investment fund shall be paid monthly to C for C's life and that after C's death the proceeds from 4 such units shall be paid monthly to D, age 57, for D's life. The portion of the investment in the contract allocable to each taxable year of C is $1,037.00 and that allocable to each taxable year of D is $414.80. This is determined as follows:

Multiple from Table VI (ages 60, 57)	31.2
Number of units to be paid, in effect, as a joint and survivor annuity ...	×4
Number of total annual unit payments anticipatable with respect to the joint and survivor annuity element	124.8
Multiple from Table V (age 60)	24.2
Number of units to be paid, in effect, as a single life annuity	×6
Number of total annual unit payments anticipatable with respect to C alone	145.2
Total number of unit payments anticipatable	270
Portion of investment in the contract allocable to unit payments ($28,000 ÷ 270) on an annual basis	103.70
Number of units payable to C while C continues to live	×10
Portion of the investment in the contract allocable to each taxable year of C	$1,037.00
Portion of investment in the contract allocable to unit payments ($28,000 ÷ 270) on an annual basis	$ 103.70
Number of units payable to D for D's life after C's death	×4
Portion of the investment in the contract allocable to each taxable year of D	$ 414.80

For purposes of the above computation it is immaterial whether or not C lives to or beyond the life expectancy shown in Table V.

Example (5). Assume the same facts as in example (4), except that C's total investment in the contract is $28,000, and C's pre-July 1986 investment in the contract is $16,000. If C makes the election described in §1.72-6(d)(6), separate computations are required to determine the amount excludable from gross income with respect to the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract. The annuitant shall apply the appropriate pre-July 1986 and post-June 1986 life expectancy multiples to the applicable portions of the units to be paid as a joint and survivor annuity, and as a single life annuity.

Pre-July 1986 Computation (all references to unit payments are to the pre-July 1986 applicable portion of such payments):

Multiple from Table II (male, age 60, female, age 57)	27.6
Number of units to be paid, in effect, as a joint and survivor annuity ...	×4
Number of total annual unit payments anticipatable with respect to the joint and survivor annuity element	110.40
Multiple from Table I (male, age 60)	18.2
Number of units to be paid, in effect, as a single life annuity	×6
Number of total annual unit payments anticipatable with respect to C alone	109.20
Total number of unit payments anticipatable	219.6
Portion of pre-July 1986 investment in the contract allocable to unit payments ($16,000 ÷ 219.60) on an annual basis	$ 72.86
Number of units payable to C while C continues to live	×10
Portion of pre-July 1986 investment in the contract allocable to each taxable year of C	728.60
Portion of pre-July 1986 investment in the contract allocable to unit payments ($16,000 ÷ 219.60) on an annual basis	72.86
Number of units payable to D for D's life after C's death	×4
Portion of pre-July 1986 investment in the contract allocable to each taxable year of D	$291.44

Post-June 1986 Computation (all references to unit payments are to the post-June 1986 applicable portion of such payments):

Multiple from Table VI (ages 60, 57)	31.2
Number of units to be paid, in effect, as a joint and survivor annuity ...	×4
Number of total annual unit payments anticipatable with respect to the joint and survivor annuity element	124.80
Multiple from Table V (age 650) ...	24.2
Number of units to be paid, in effect, as a single life annuity	×6
Number of total annual unit payments anticipatable with respect to C alone	145.20
Total number of unit payments anticipatable	270
Portion of post-June 1986 investment in the contract allocable to unit payments ($12,000 ÷ 270) on an annual basis	$ 44.44
Number of units payable to C while C continues to live	×10
Portion of post-June 1986 investment in the contract allocable to each taxable year of C	$444.40
Portion of post-June 1986 investment in the contract allocable to unit payments ($12,000 ÷ 270) on an annual basis	44.44
Number of units payable to D for D's lie after C's death	×4
Portion of post-June 1986 investment in the contract allocable to each taxable year of D	$ 177.78

Total Computation:

Total portion of the investment in the contract allocable to each taxable year of C ($728.60 + $444.40) ..	$1,173.00
Total portion of the investment in the contract allocable to each taxable year of D ($291.44 + $177.78) ..	$ 469.22

Example (6). Assume that taxpayer C in example (4) receives payments for four years which are at least as large as the portion of the investment in the contract allocable to such years, but in the fifth year receives a total of only $600 rather than the $1,037 allocable to such year. C is 65 and D is 62 at the beginning of the first monthly period for which an amount is payable in the sixth taxable year. C makes the election in that year provided under paragraph (d)(3) of §1.72-4. The difference between the portion of the investment in the contract allocable to the fifth year and the amount actually received in that year is $437 ($1,037 − $600). In this case, 106.4 unit payments are anticipatable with respect to the joint and survivor annuity element, since the appropriate multiple from Table VI of §1.72-9, 26.6, multiplied by the number of units payable, in effect, as a joint and survivor annuity yields this result (4 × 26.6). C's appropriate multiple from Table V of §1.72-9 for the six units which will cease to be paid at C's death is 20.0, and the number of unit payments anticipatable with respect to C alone is 120 (6 × 20). The total number of unit payments anticipatable is, therefore, 226.4 (120 plus 106.4). Dividing the difference previously found ($437) by the total number of unit payments thus determined (226.4) indicates that C will have an additional allocation of the investment in the contract of $19.30 to the sixth and every succeeding full taxable year (10 units × $1.93), and D will have an additional allocation of the investment in the contract of $7.72 (4 units × $1.93) to each taxable year in which D receives 12 monthly payments subsequent to the death of C. The total allocable to each taxable year of C is, therefore, $1,056.30, and that allocable to each taxable year of D will be $422.52.

Example (7). If, in example (6), C had died at the end of the fourth year, in the fifth year D would have received a payment of $240 (that portion of the $600 that C would have received which is in the same ratio that 4 units bear to 10 units) and would thus have received $174.80 less than the portion of the investment in the contract allocable to each of D's taxable years. In these circumstances, D would be entitled to elect to redetermine the portion of the investment in the contract allocable to the taxable year of election and all subsequent years. The new amount allocable thereto would be found by dividing the $174.80 difference by D's life expectancy as of the first day of the first period for which D received an amount as an annuity in the sixth year of the annuity contract, and adding the result to D's originally determined allocation of $414.80.

* * * * *

(e) *Expected return where two or more annuity elements providing for fixed payments are acquired for a single consideration.* (1) In the case of a contract described in paragraph (a)(2) of §1.72-2, which provides for specified payments to be made under two or more annuity elements, the expected return shall be found for the contract as a whole by aggregating the expected returns found with respect to each annuity element. If individual life annuity elements are involved (including joint and survivor annuities where the primary annuitant died before January 1, 1954) expected return for each of them shall be determined in the manner prescribed in paragraph (a) of this section. If joint and survivor annuity elements are involved, the expected return for such elements shall be determined under the appropriate subparagraph of paragraph (b) of this section. If terms certain or amounts certain are involved, the expected returns for such elements shall be determined under paragraph (c) or (d) of this section, respectively.

(2) The aggregate expected return found in accordance with the rules set forth in subparagraph (1) of this paragraph shall constitute the expected return for the contract as a whole. The investment in the contract shall be divided by the amount thus determined to obtain the exclusion ratio for the contract as a whole. This exclusion ratio shall be applied to all amounts received as an annuity under the contract by any recipient (in accordance with the provisions of §1.72-4), except in the case of amounts received by a surviving annuitant under a joint and survivor annuity element to which the provisions of section 72(i) and paragraph (b)(3) of this section would apply if it were a separate contract. See subparagraph (3) of this paragraph.

(3) In the case of a contract providing two or more annuity elements, one of which is a joint and survivor annuity element of the type described in section 72(i) and paragraph (b)(3) of this section, the general exclusion ratio for the contract as a whole, for the purpose of computations with respect to all the other annuity elements, shall be determined in accordance with the principles of subparagraphs (1) and (2) of this paragraph. A special exclusion ratio shall thereafter be determined for the surviving annuitant receiving payments under the annuity element described in section 72(i) and paragraph (b)(3) of this section by using the investment in the contract and the expected return determined in accordance with the provisions of paragraph (b)(3) of this section.

(4) In the case of a contract providing for payments to be made to two persons in the manner described in paragraph (b)(6) of §1.72-5, the expected return is to be computed as though there were two joint and survivor annuities under the same contract, in the following manner. First, the multiple appropriate to the ages (as of the annuity starting date) and, if applicable sexes of the annuitants involved shall be found in Table II, or VI (whichever is applicable) of §1.72-9 and adjusted, if necessary, in the manner described in paragraph (a)(2) of this section. Second, the multiple so found shall be applied to the sum of the payments to be made each year to both annuitants. The result is the expected return for the contract as a whole.

(5) For rules relating to expected return where two or more annuity elements are acquired for a single consideration and one or more of such elements does not specify a fixed payment for each period, see paragraph (f) of this section.

* * * * *

(g) *Expected return with respect to contracts subject to §1.72-6(d).* In the case of a contract to which §1.72-6(d) (relating to contracts in which amounts were invested both before July 1, 1986, and after June 30, 1986) applies, an expected return is computed using the multiples in Table I through IV of §1.72-9 with respect to the pre-July 1986 investment in the contract and a second expected return is computed using the multiples in Tables V through VIII of §1.72-9 with respect to the post-June 1986 investment in the contract.

Par. 4. Section 1.72-6 is amended by revising paragraph (b) and adding a new paragraph (d) to read as follows:

§1.72-6 Investment in the contract.

* * * * *

(b) *Allocation of the investment in the contract where two or more annuity elements are acquired for a single consideration* (1) In the case of a contract described in §1.72-2(a)(2) which provides for two or more annuity elements, the investment in the contract determined under paragraph (a) shall be allocated to each of the annuity elements in the ratio that the expected return under each annuity element bears to the aggregate of the expected returns under all the annuity elements. The exclusion ratio for the contract as a whole shall be determined by dividing the investment in the contract (after adjustment for the present value of any or all refund features) by the aggregate of the expected returns under all the annuity elements. This may be illustrated by the following examples:

Example (1). If a contract provides for annuity payments of $1,000 per year for life (with no refund feature) to both A and B, a male and female, respectively, each 70 years of age as of the annuity starting date, such contract is acquired for consideration of $19,575 (without regard to whether paid by A, B, or both), and there is no post-June 1986 investment in the contract, the investment in the contract shall be allocated by determining the exclusion ratio for the contract, as a whole in the following manner:

Expectancy of A under Table I and §1.72-5(a)(2), 11.8 (12.1-0.5), multiplied by $1,000	$11,600
Expectancy of B computed in a similar manner ($1,000 × 14.5 [15.0 − 0.5])	14,500
Total expected return	26,100

The exclusion ratio for both A and B is then $19,575 ÷ $26,100, or 75 percent. A and B shall each exclude from gross income three-fourths ($750) of each $1,000 annual payment received and shall include the remaining one-fourth ($250) of each $1,000 annual payment received in gross income.

Example (2). Assume the same facts as in example (1) except that of the total investment in the contract of $19,575, the pre-July 1986 investment in the contract is $10,000. If the election described in §1.72-6(d)(6) is made with respect to the contract, the investment in the contract shall be allocated by determining an exclusion ratio for the contract as a whole based on separately computed exclusion ratios with respect to the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract in the following manner:

Expectancy of A under Table I and §1.72-5(a)(2), 11.6 (12.1−0.5), multiplied by $1,000	$11,600
Expectancy of B under Table I and §1.72-5(a)(2), 14.5 (15.0 − 0.5), multiplied by $1,000	$14,500
Pre-July 1986 expected return .	$26,100
Expectancy of A under Table V and §1.72–5(a)(2), 15.5 (16.0–0.5), multiplied by $1,000	$15,500
Expectancy of B under Table V and §1.72–5(a)(2), 15.5 (16.0–0.5), multiplied by $1,000	$15.500
Post-June 1986 expected return .	$31,000
Pre-July 1986 exclusion ratio ($10,000 ÷ $26,100)	38.3
Post-June 1986 exclusion ratio ($9,575 ÷ 31,000)	30.9

A and B shall each exclude from gross income $692 (38.3 percent of $1,000 + 30.9 percent of $1,000) of each 41,000

payment and include the remaining $308 in gross income.

(2) In the case of a contract providing for specified annual annuity payments to be made to two persons during their joint lives and the payment of the aggregate of the two individual payments to the survivor for his life, the investment in the contract shall be allocated in accordance with the provisions of subparagraph (1) of this paragraph. For this purpose, the investment in the contract (without regard to the fact that differing amounts may have been contributed by the two annuitants) shall be divided by the expected return determined in accordance with paragraph (e)(4) of §1.72-5. The resulting exclusion ratio shall then be applied to any amounts received as an annuity by either annuitant.

(3) In the case of a contract providing two or more annuity elements, one or more of which provides for payments to be made in a manner described in paragraph (b)(3) of §1.72-2, the investment in the contract shall be allocated to the various annuity elements in the following manner:

(i) If all the annuity elements provide for payments to be made in the manner described in paragraph (b)(3) of §1.72-2, the investment in the contract shall be allocated on the basis of the amounts received by each recipient by apportioning the amount determined to be excludable under that section to each recipient in the same ratio as the total of the amounts received by him in the taxable year bears to the total of the amounts received by all recipients during the same period; and

(ii) If one or more, but not all, of the annuity elements provide for payments to be made in a manner described in paragraph (b)(3) of §1.72-2:

(a) With respect to all annuity elements to which that section does not apply, the investment in the contract for all such elements shall be the portion of the investment in the contract as a whole (found in accordance with the provisions of this section) which is properly allocable to all such elements; and

(b) With respect to all annuity elements to which paragraph (b)(3) of §1.72-2 does apply, the investment in the contract for all such elements shall be the investment in the contract as a whole (found in accordance with the provisions of this section) as reduced by the portion thereof determined under *(a)* of this subdivision.

For the purpose of determining, pursuant to *(a)* of this subdivision, the portion of the investment in the contract as a whole properly allocable to a particular annuity element, reference shall be made to the present value of such annuity element determined in accordance with paragraph (e)(1)(iii)*(b)* of §1.102–2.

(iii) In the case of a contract to which paragraph (d) of this section applies, this paragraph (b) is applied in the manner prescribed in paragraph (d) and, in particular, paragraph (d)(5)(v) of this section.

* * * * *

(d) *Pre-July 1986 and post-June 1986 investment in the contract.* (1) This paragraph (d) applies to an annuity contract if—

(i) The investment in the contract includes a pre-July 1986 investment in the contract and a post-June 1986 investment in the contract (both as defined in §1.72-6(d)(3));

(ii) The use of a multiple found in Tables I through VII of §1.72-9 is required to determine the expected return under the contract; and

(iii) The election described in paragraph (d)(6) of this section is made with respect to the contract.

(2) In the case of an annuity contract to which this paragraph (d) applies—

(i) All computations required to determine the amount excludable from gross income shall be performed separately with respect to the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract as if each such amount were the entire investment in the contract;

(ii) The multiples in Tables I through IV shall be used for computations involving the pre-July 1986 investment in the contract and the multiples in Tables V through VIII shall be used for computations involving the post-June 1986 investment in the contract; and

(iii) The amount excludable from gross income shall be the sum of the amounts determined under the separate computations required by paragraph (d)(2)(i) of this section.

(3) For purposes of the regulations under section 72, the pre-July 1986 investment in the contract and post-June 1986 investment in the contract are determined in accordance with the following rules:

(i)(A) If the annuity starting date of the contract occurs before July 1, 1986, the pre-July 1986 investment in the contract is the total investment in the contract as of the annuity starting date;

(B) If the annuity starting date of the contract occurs after June 30, 1986, and the contract does not provide for a disqualifying form of payment or settlement, the pre-July 1986 investment in the contract is the investment in the contract computed as of June 30, 1986, as if June 30, 1986, had been the later of the annuity starting date of the contract or the date on which an amount is first received thereunder;

(C) If the annuity starting date of the contract occurs after June 30, 1986, and the contract provides, at the option of the annuitant or of any other person (including, in the case of an employee's annuity, an option exercisable only by, or with the consent of, the employer), for a disqualifying form of payment or settlement, the pre-July 1986 investment in the contract is zero (i.e., the total investment in the contract is post-June 1986 investment in the contract).

(ii) The post-June 1986 investment in the contract is the amount by which the total investment in the contract as of the annuity starting date exceeds the pre-July 1986 investment in the contract.

(iii) For purposes of paragraph (d)(3)(i) of this section, a disqualifying form of payment or settlement is any form of payment or settlement (whether or not selected) that permits the receipt of amounts under the contract in a form other than a life annuity. For example, each of the following options provides for a disqualifying form of payment or settlement:

(A) An option to receive a lump sum in full discharge of the obligation under the contract.

(B) An option to receive an amount under the contract after June 30, 1986, and before the annuity starting date.

(C) An option to receive an annuity for a period certain.

(D) An option to receive payments under a refund feature (within the meaning of paragraphs (b) and (c) of this section) that is substantially equivalent to an annuity for a period certain.

(E) An option to receive a temporary life annuity (within the meaning of §1.72-5(a)(3)) that is substantially equivalent to an annuity for a period certain.

An option to receive alternative forms of life annuity is not a disqualifying option for purposes of paragraph (d)(3)(i) of this section. Thus, if the sole options provided under a contract are a single life annuity and a joint and survivor life annuity, paragraph (d)(3)(i)(C) of this section does not apply to such contract.

(iv) For purposes of paragraph (d)(3)(iii) of this section, a refund feature is substantially equivalent to an annuity for a period certain if its value determined under Table VII of §1.72-9 exceeds 50 percent. Similarly, a temporary life annuity is substantially equivalent to an annuity for a period certain if the multiple determined under Table VIII of §1.72-9 exceeds 50 percent of the maximum duration of the annuity.

(4) In any separate computation under this paragraph (d), only the applicable portion of other amounts (such as the total expected return under the contract, or the total amount guaranteed under the contract as of the annuity starting date) shall be taken into account if the use of the entire amount in such computation is inconsistent with the use in the computation of only a portion of the investment in the contract. For example, such use is generally inconsistent if the computation requires a comparison of the investment in the contract and such other amount for the purpose of using the greater (or lesser) amount of the difference between the two. For purposes of the first sentence of this paragraph (d)(4), the applicable portion is the amount that bears the same ratio to the entire amount as the pre-July 1986 investment in the contract or the post-June 1986 investment in the contract, whichever is applicable, bears to the total investment in the contract as of the annuity starting date.

(5) *Application to particular computations.* (i) In the case of a contract to which this paragraph (d) applies, the exclusion ratio for purposes of §1.72-4(a) is the sum of the exclusion ratios separately computed in accordance with this paragraph (d). The exclusion ratio with respect to the pre-July 1986 investment in the contract is determined by dividing the pre-July 1986 investment in the contract by the expected return as found under §1.72-5 by applying the appropriate multiples of Tables I through IV of §1.72-9. Similarly, the exclusion ratio with respect to the post-June 1986 investment in the contract is determined by dividing the post-June 1986 investment in the contract by the expected return as found under §1.72-5 by applying the appropriate multiples in Tables V through VIII of §1.72-9.

(ii) The applicability of §1.72-4(d)(2) to a contract to which this paragraph (d) applies shall be determined separately with respect to the post-June 1986 investment in the contract and the pre-July 1986 investment in the contract and in each such determination only the applicable portion of the total expected return under the contract shall be taken into account. If §1.72-4(d)(2) applies with respect to either such investment in the contract, the separately computed exclusion ratio shall be considered to be the applicable portion of 100 percent.

(iii) If §1.72-4(d)(3) applies to a contract to which this paragraph (d) applies—

(A) The applicable portions (as defined in paragraph (d)(4) of this section) of payments received under the contract for a taxable year shall be separately computed;

(B) The pre-July 1986 investment in the contract and the post-June 1986 investment in the contract shall be separately allocated to the taxable year; and

(C) The separate applicable portions of the payments received under the contract for the taxable year shall be considered to be amounts received as an annuity (for which the exclusion ratio is 100 percent) only to the extent they do not exceed the portions of the corresponding investments in the contract which are properly allocable to that year.

See the example in §1.72-4(d)(3)(v).

(iv) If §1.72-4(e) applies to a contract to which this paragraph (d) applies, the exclusion ratio shall be separately computed with respect to the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract. For purposes of the separate computations under §1.72-4(e)(2)(ii), only the applicable portion of payments received shall be taken into account and the exclusion ratio (100%) shall be applied to the separately computed portion allocated to each participant.

(v) If paragraph (b)(3) of this section applies to a contract to which this paragraph (d) applies, separate allocations are required with respect to the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract. For purposes of the separate computations required to determine the portion of the investment in the contract properly allocable to a particular annuity element, only the applicable portion of the present value of the annuity element determined in accordance with §1.101-2(e)(1)(iii)*(b)* is taken into account.

(vi) If §1.72-7 applies to a contract to which this paragraph (d) applies, separate computations are required to determine the adjustment to the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract. For purposes of such separate computations, only the applicable portions of the amounts described in §1.72-7(b)(3)(ii), (c)(1)(vii)*(b)*, and (d)(1)(ii) are taken into account. Similarly, in the case of computations with respect to the guarantee of a specified amount under §1.72-7(d)(1), only the applicable portion of such amount is taken into account.

(6) This paragraph (d) applies to a contract only if the first taxpayer to receive an amount as an annuity under the contract elects to perform separate computations with respect to the pre-July 1986 investment in the contract and the post-June 1986 investment in the contract as if each such amount were the entire investment in contract. If two or more annuitants receive an amount as an annuity under the contract at the same time (such as under a joint-and-last-survivorship annuity contract), an election by one of the annuitants is treated as an election by each of the annuitants. The election is made by attaching a statement to the first return filed by the taxpayer for the first taxable year in which an amount is received as an annuity under the contract. The statement must indicate that the taxpayer is electing to apply the provisions of paragraph (d) of §1.72-6, and must also contain the name, address, and taxpayer identification number of each annuitant under the contract, and the amount of the pre-July 1986 investment

in the contract.

(7) If the investment in the contract includes a post-June 1986 investment in the contract and the election described in paragraph (d)(6) of this section is not made—

(i) The amount excludable from gross income shall be determined without regard to the separate computations described in this paragraph (d); and

(ii) Only the multiples found in Table V through VIII shall be used in determining the amount excludable from gross income.

Par. 5. Section 1.72-7 is amended by revising paragraphs (b), (c), (d), and (e), and adding a new paragraph (f) to read as follows:

§1.72-7 Adjustment in investment where a contract contains a refund feature.

* * * * *

(b) *Adjustment of investment for the refund feature in the case of a single life annuity.* Where a single life annuity contract to which section 72 applies contains a refund feature and the special rule of paragraph (d) of this section does not apply, the investment in the contract shall be adjusted in the following manner:

(1) Determine the number of years necessary for the guaranteed amount to be fully paid by dividing the maximum amount guaranteed as of the annuity starting date by the amount to be received annually under the contract to the extent such amount reduces the guaranteed amount. The number of years should be stated in terms of the nearest whole year, considering for this purpose a fraction of one-half or more as an additional whole year.

(2) Consult Table III or VII (whichever is applicable) of §1.72-9 for the appropriate percentage under the whole number of years found in subparagraph (1) of this paragraph and the age (as of the annuity starting date) and, if applicant, sex of the annuitant.

(3) Multiply the percentage found in subparagraph (2) of this paragraph by whichever of the following is the smaller: (i) The investment in the contract found in accordance with §1.72-6 or (ii) the total amount guaranteed as of the annuity starting date.

(4) Subtract the amount found in subparagraph (3) of this paragraph from the investment in the contract found in accordance with §1.72-6. The resulting amount is the investment in the contract adjusted for the present value of the refund feature without discount for interest and is to be used in determining the exclusion ratio to be applied to the payments received as an annuity. The percentage found in Table III, or VII shall not be adjusted in a manner described in paragraph (a)(2) of §1.72-5. These principles may be illustrated by the following examples:

Example (1). On January 1, 1954, a husband, age 65, purchased for $21,053, an immediate installment refund annuity payable $100 per month for life. The contract provided that in the event the husband did not live long enough to recover the full purchase price, payments were to be made to his wife until the total payments under the contract equaled the purchase price. The investment in the contract adjusted for the purpose of determining the exclusion ratio is computed in the following manner.

Cost of the annuity contract (investment in the contract, unadjusted)	$21,053
Amount to be received annually	$1,200
Number of years for which payment guaranteed ($21,053 divided by $1,200)	17.5
Rounded to nearest whole number of years	18
Percentage located in Table III for age 65 (age of the annuitant as of the annuity starting date) and 18 (the number of whole years) (percent)	30
Subtract value of the refund feature to the nearest dollar (30 percent of $21,053)	$6,316
Investment in the contract adjusted for the present value of the refund feature without discount for interest	$14,737

Example (2). Assume the same facts as in example (1), except that the total investment in the contract was made after June 30, 1986. The investment in the contract adjusted for the purpose of determining the exclusion ratio is computed as follows:

Cost of the annuity contract (investment in the contract, unadjusted)	$21,053
Amount to be received annually	$1,200
Number of years for which payment guaranteed ($21,053 ÷ $1,200)	17.5
Rounded to nearest whole number of years	18
Percentage in Table VII for age 65 and 18 years (percent)	15
Subtract value of the refund feature to the nearest dollar (15 percent of $21,053)	$3,158
Investment in the contract adjusted for the present value of the refund feature without discount for interest	$17,895

Example (3). Assume the same facts as in example (1), except that the pre-July 1986 investment in the contract is $10,000 and the post-June 1986 investment in the contract is $11,053. If the annuitant makes the election described in §1.72-6(d)(6), separate computations must be performed pursuant to §1.72-6(d) to determine the adjusted investment in the contract. The pre-July 1986 investment in the contract and the post-June 1986 investment in the contract adjusted for the purpose of determining the exclusion ratios are, respectively, $7,000 and $9,395, determined as follows:

Pre-July 1986 investment in the contract (unadjusted)	$10,000
Pre-July 1986 portion of the amount to be received annually ($10,000/$21,053 × $1,200)	$570.00
Number of years for which payment guaranteed ($10,000 ÷ $570)	17.54
Rounded to nearest whole number of years	18
Percentage in Table III for age 65 and 18 years (percent)	30
Subtract value of refund feature to nearest dollar (30 percent of $10,000)	$3,000
Pre-July 1986 investment in the contract adjusted for the present value of the refund feature without discount for interest	$7,000
Post-June 1986 investment in the contract (unadjusted)	$11,053
Post-June 1986 portion of the amount to be received annually ($11,053/$21,053 × $1,200)	$630
Number of years for which payment guaranteed ($11,053 ÷ $630)	17.54
Rounded to nearest whole number of years	18
Percentage in Table VII for age 65 and 18 years (percent)	15
Subtract value of the refund feature to the nearest dollar (15 percent of $11,053)	$1,658
Post-June 1986 investment in the contract adjusted for the present value of the refund feature without discount for interest	$9,395

If, in the above examples, the guaranteed amount had exceeded the investment in the contract (or applicable portion thereof), the percentage found in Table III or VII (whichever is applicable) should have been applied to the lesser of these amounts since any excess of the guaranteed amount over the investment in the contract (as found under §1.72-6) would not have constituted a refund of premiums or other consideration paid. In such a case, however, a different multiple might have been obtained from Table III or VII (whichever is applicable) since the number of years for which payments were guaranteed would have been greater.

(c) *Adjustment of investment for the*

refund feature in the case of a joint and survivor annuity. (1) Where a joint and survivor annuity contract described in paragraph (b)(1) or (6) of §1.72-5 contains a refund feature and the special rule of paragraph (d) of this section does not apply, the investment in the contract shall be adjusted in the following manner.

(i) Determine the number of years necessary for the guaranteed amount to be fully paid by dividing the maximum amount guaranteed as of the annuity starting date by the amount to be received annually under the contract. The number of years should be stated in terms of the nearest whole year, considering for this purpose a fraction of one-half or more as an additional whole year.

(ii) Consult Table III or VII (whichever is applicable) of §1.72-9 for the appropriate percentages under the whole number of years found in subdivision (i) of this subparagraph and the age (as of the annuity starting date) and, if applicable, sex of each annuitant. If Table III applies and the annuitants are not of the same sex, substitute for the female annuitant a male annuitant 5 years younger, or for the male annuitant a female annuitant 5 years older, so that Table III will be entered in both cases with the ages of annuitants of the same sex.

(iii) Find the sum of the two percentages found in accordance with subdivision (ii) of this subparagraph.

(iv) To the age of the elder of the two annuitants (as determined under subdivision (ii) of this subparagraph if Table III applies), add the number of years (indicated in the table below) opposite the number of years by which such annuitants' ages differ:

Number of years difference in age (2 male annuitants or 2 female annuitants if Table III applies)	Addition to older age in years
0 to 1, inclusive	9
2 to 3, inclusive	8
4 to 5, inclusive	7
6 to 8, inclusive	6
9 to 11, inclusive	5
12 to 15, inclusive	4
16 to 20, inclusive	3
21 to 27, inclusive	2
28 to 42, inclusive	1
Over 42	0

(v) Consult Table III or VII (whichever is applicable) for the appropriate percentage under the whole number of years found in subdivision (i) of this subparagraph and the age and, if applicable, sex of the elder annuitant as adjusted under subdivision (iv) of this subparagraph.

(vi) Subtract the percentage obtained in subdivision (v) of this subparagraph from the sum of the percentages found under subdivision (iii) of this subparagraph. If the result is less than one, subdivisions (vii) and (viii) of this subparagraph shall be disregarded and no adjustment made to the investment in the contract.

(vii) Multiply the percentage found in subdivision (vi) of this subparagraph by whichever of the following is the smaller: *(a)* the investment in the contract found in accordance with §1.72-6 or *(b)* the total amount guaranteed as of the annuity starting date.

(viii) Subtract the amount found in subdivision (vii) of this subparagraph from the investment in the contract found in accordance with §1.72-6.

(2) The principles of subparagraph (1) of this paragraph may be illustrated by the following examples:

Example. (1). Prior to July 1, 1986, Taxpayer A, a 70-year old male, purchases a joint and last survivor annuity for $33,050. The contract provides for payments of $100 a month to be paid first to himself for life and then to B, his 40-year-old daughter, if she survives him. The contract further provides that in the event both die before ten years' payments have been made, payments will be continued to C, a beneficiary, or to C's estate, until ten years' payments have been made. If there is no post-June 1986 investment in the contract, the investment in the contract adjusted for the purpose of determining the exclusion ratio is computed in the following manner:

Cost of the annuity contract (investment in the contract unadjusted)	$33,050
Guaranteed amount ($1,200 × 10)	$12,000
Percentage in Table III for male, age 70 (or female, age 75) for duration of the guarantee (10)	21
Percentage in Table III for female, age 40 (or male, age 35) for duration of the guarantee (10)	2
Sum of percentage obtained	23
Difference in years of age between two males, aged 70 and 35 (or 2 females, aged 75 and 40)	35
Addition, in years, to older age	1
Percentage in Table III for male one year older than A	22
Difference between percentages obtained (23 percent less 22 percent)	1
Value of the refund feature to the nearest dollar (1 percent of $12,000)	$120
Investment in the contract adjusted for present value of the refund feature	$32,930

Example (2). The facts are the same as in example (1), except that the total investment in the contract was made after June 30, 1986, and A is 73 years of age. The investment in the contract adjusted for the purpose of determining the exclusion ratio is computed in the following manner:

Cost of the annuity contract (investment in the contract, unadjusted)	$33,050
Guaranteed amount ($1,200 × 10)	$12,000
Percentage in Table VII for age 73 for duration of the guarantee (10)	14
Percentage in Table VII for age 40 for duration of the guarantee (10)	1
Sum of percentages obtained	15
Difference in years of age between two annuitants	33
Addition, in years, to older age	1
Percentage in Table VII for annuitant one year older than A	16
Difference between percentages obtained (16 percent less 15 percent)	1
Value of the refund feature to the nearest dollar (1 percent of $12,000)	$120
Investment in the contract adjusted for present value of the refund feature	$32,930

(d) *Adjustment of investment in the contract where paragraph (b)(3) of §1.72-2 applies to payments.* (1) If paragraph (b)(3) of §1.72-2 applies to payments to be made under a contract and this section also applies because of the provision for a refund feature, an adjustment shall be made to the investment in the contract in accordance with this paragraph before making the computations required by paragraph (d)(3) of §1.72-4 and paragraph (b)(7) of §1.72-5. In the case of the guarantee of a specified amount, the adjustment shall be made by applying the appropriate multiple from Table III or VII (whichever is applicable), as otherwise determined under this section, to the investment in the contract or the guaranteed amount, whichever is the lesser. The guarantee period shall be found by dividing the amount guaranteed by an amount determined by placing the payments received during the first taxable year (to the extent such payments reduce the guaranteed amount) on an annual basis. Thus, if monthly payments are first received by a taxpayer on a calendar year basis in August, his total payments (to the extent that they reduce the guaranteed amount) for the taxable year would be divided by 5 and multiplied by 12. The guaranteed amount would then be divided by the result of this computation to obtain the guarantee period. If the contract merely guarantees that proceeds from a unit or units of a fund shall be paid for a fixed number of years or the life (or lives) of an annuitant (or annuitants), whichever is the longer, the fixed number of years is the guarantee period. The appropriate percentage in Table III or VII shall be applied to whichever of the following is the smaller: (i) the investment in the contract; or (ii) the product of the payments received in the first taxable year, placed on an annual basis, multiplied by the number of years for which payment of the proceeds of a unit or units is guaranteed.

(2) The principles of this paragraph may be illustrated by the following examples:

Example (1). Taxpayer A, a 50-year-old male purchases for $25,000, a contract which provides for variable monthly payments to be paid to him for his life. The contract also provides that if he should die before receiving payments for fifteen years, payments shall continue according to the original formula to his estate or beneficiary until payments have been made for that period. Beginning with the month of September. A receives payments which total $450 for the first taxable year of receipt. This amount, placed on an annual basis, is $1,350 ($450 divided by 4, or $112.50; $112.50 multiplied by 12, or $1,350). If there is no post-June 1986 investment in the contract, the guaranteed amount is considered to be $20,250 ($1,350 × 15), and the multiple from Table III (found in the same manner as in paragraph (b) of this section), 9 percent, applied to $20.250 (since this amount is less than the investment in the contract), results in a refund adjustment of $1,822.50. The latter amount, subtracted from the investment in the contract of $25,000, results in an adjusted investment in the contract of $23,177.50. If A dies before receiving payments for 15 years and the remaining payments are made to B, his beneficiary, B shall exclude the entire amount of such payments from his gross income until the amounts so received by B, together with the amounts received by A and excludable from A's gross income, equal or exceed $25,000. Any excess and any payments thereafter received by B shall be fully includible in gross income.

Example (2). Assume the same facts as in example (1), except that the total investment in the contract was made after June 30, 1986. The applicable multiple found in Table VII is 3 percent. When this is applied to the guaranteed amount of $20,250, it results in a refund adjustment of $607.50. The adjusted investment in the contract is $24,392.50 ($25,000 – $607.50).

(e) *Adjustment of the investment in the contract where more than one annuity element is provided for a single consideration.* In the case of contracts to which paragraph (b) of §1.72-6 applies for the purpose of allocating the investment in the contract to two or more annuity elements which are provided for a single consideration, if one or more of such elements involves a refund feature, the portion of the investment in the contract properly allocable to each such element shall be adjusted for the refund feature before aggregating all the investments in order to obtain the exclusion ratio which is to apply to the contract as a whole.

Example (1). If taxpayer A, an insured 70 years of age, upon maturity of an endowment policy which cost him a net amount of $86,000, elected a dual settlement consisting of (1) monthly payments for his life aggregating $4,146 per year with 10 years' payments certain, and (2) monthly payments for his 60 year old brother, B, aggregating $2,820 per year with 20 years' payments certain, the exclusion ratio to be used by both A and B if there is no post-June 1986 investment in the contract would be determined in the following manner.

A's expected return (A's payments per year of $4,146 multiplied by his life expectancy from Table 1 of 12.1)..	$50,166.60
B's expected return (B's payments per year of $2,820 multiplied by his life expectancy from Table 1 of 18.2)..	$51,324.00
Sum of expected returns to be used in determining exclusion ratio	$101,490.60
Percentage of total expected return attributable to A's expectancy of the ($40,166.60– $101,490.60)..............	49.4
Percentage of total expected return attributable to B's expectancy of the ($51,324- $101,490.60)..............	50.6
Portion of investment in the contract allocable to A's annuity (49.4 percent of $86,000)...	$42,484.00
Portion of investment in the contract allocable to B's annuity (50.6 percent of $86,000)...	$43,516.00
Value of the refund feature with respect to A's annuity (percentage from Table III for male, age 70, and duration 10, or 21 percent, multiplied by lesser of guaranteed amount and allocable portion of investment in the contract $41,460)	$8,707.00
A's allocable portion of the investment in the contract adjusted for refund feature ($42,484 less $8,707.00) ...	$33,777.00
Value of the refund feature with respect to B's annuity (percentage from Table III for male, age 60, and duration 20, or 25 percent, multiplied by lesser of guaranteed amount and allocable portion of investment in the contract, $43,516)	$10,879.00
B's allocable portion of the investment in the contract adjusted for refund feature ($43,516 less $10,879.00) ..	$32,637.00
Sum of A's and B's allocable portions of the investment in the contract after adjustment for the refund feature	$66,414.00
Exclusion ratio for the contract as a whole (total adjusted investment in the contract, $66,414, divided by the total expected return from above, $101,490.60) (percent)	65.4

Example (2). Assume the same facts as in example (1) except that the total investment in the contract was made after June 30, 1986. The exclusion ratio to be used by both A and B would be 56.9 percent, determined as follows:

A's expected return (A's payments per year of $4,146 multiplied by his life expectancy from Table V of 16.0) .	$66,336.00
B's expected return (B's payments per year of $2,820 multiplied by his life expectancy from Table V of 24.2)	$68,244.00
Sum of expected returns to be used in determining exclusion ratio	$134,580.00
Percentage of total expected return attributable to A's expectancy of life ($66,336.00 ÷ $134,580.00).............	49.3
Percentage of total expected return attributable to B's expectancy of life ($68,244.00 ÷ $134,580.00).............	50.7
Portion of investment in the contract allocable to A's annuity (49.3 percent of $86,000)...	$42,398.00
Portion of investment in the contract allocable to B's annuity (50.7 percent of $86,000)...	$43,602.00
Value of the refund feature with respect to A's annuity (percentage from Table VII for age 70 and duration 10, or 11 percent, multiplied by lesser of the guaranteed amount and allocable portion of investment in the contract, $41,460)	$4,560.60
A's allocable portion of the investment in the contract adjusted for refund feature ($42,398 less $4,560.60) ...	$37,837.40
Value of the refund feature with respect to B's annuity (percentage from Table VII for age 60 and duration 20, or 11 percent, multiplied by lesser	

of guaranteed amount and allocable portion of investment in the contract, $43,602) . . .	$4,796.22
B's allocable portion of the investment in the contract adjusted for refund feature ($43,602 less $4,796.22) . . .	$38,805.78
Sum of A's and B's allocable portions of the investment in the contract after adjustment for the refund feature	$76,643.18
Exclusion ratio for the contract as a whole (total adjusted investment in the contract, $76,643.18, divided by the total expected return from above, $134,580.00) (percent)	56.9

(f) *Adjustment of investment in the contract with respect to contracts subject to §1.72-6(d).* In the case of a contract to which §1.72-6(d) (relating to contracts in which amounts were invested both before July 1, 1986, and after June 30, 1986) applies, this section is applied in the manner prescribed in §1.72-6(d) and, in particular, §1.72-6(d)(5)(vi).

Par. 6. Section 1.72-9 is amended by revising the material preceding and following the tables and adding new Tables V, VI, VIA, VII, and VIII to read as follows:

§1.72-9 Tables

The following tables are to be used in connection with computations under section 72 and the regulations thereunder. Tables I, II, IIA, III, and IV are to be used if the investment in the contract does not include a post-June 1986 investment in the contract (as defined in §1.72-6(d)(3)). Tables V, VI, VIA, VII, and VIII are to be used if the investment in the contract includes a post-June 1986 investment in the contract (as defined in §1.72-6(d)(3)). See §1.72-6(d)(3) for rules treating the entire investment in a contract as post-June 1986 investment in the contract if the annuity starting date of the contract is after June 30, 1986, and the contract provides for a disqualifying form of payment or settlement, such as an option to receive a lump sum in full discharge of the obligation under the contract. In addition, see §1.72-6(d) for special rules concerning the tables to be used and the separate computations required if the investment in the contract includes both a pre-July 1986 investment in the contract and a post-June 1986 investment in the contract and the election described in §1.72-6(d)(6) is made with respect to the contract.

* * * * *

TABLE V - ORDINARY LIFE ANNUITIES
ONE LIFE - EXPECTED RETURN MULTIPLES

AGE	MULTIPLE	AGE	MULTIPLE	AGE	MULTIPLE
5	76.6	42	40.6	79	10.0
6	75.6	43	39.6	80	9.5
7	74.7	44	38.7	81	8.9
8	73.7	45	37.7	82	8.4
9	72.7	46	36.8	83	7.9
10	71.7	47	35.9	84	7.4
11	70.7	48	34.9	85	6.9
12	69.7	49	34.0	86	6.5
13	68.8	50	33.1	87	6.1
14	67.8	51	32.2	88	5.7
15	66.8	52	31.3	89	5.3
16	65.8	53	[illegible]	90	5.0
17	64.8	54	29.5	91	4.7
18	63.9	55	28.6	92	4.4
19	62.9	56	27.7	93	4.1
20	61.9	57	26.8	94	3.9
21	60.9	58	25.9	95	3.7
22	59.9	59	25.0	96	3.4
23	59.0	60	24.2	97	3.2
24	58.0	61	23.3	98	3.0
25	57.0	62	22.5	99	2.8
26	56.0	63	21.6	100	2.7
27	55.1	64	20.8	101	2.5
28	54.1	65	20.0	102	2.3
29	53.1	66	19.2	103	2.1
30	52.2	67	18.4	104	1.9
31	51.2	68	17.6	105	1.8
32	50.2	69	16.8	106	1.6
33	49.3	70	16.0	107	1.4
34	48.3	71	15.3	108	1.3
35	47.3	72	14.6	109	1.1
36	46.4	73	13.9	110	1.0
37	45.4	74	13.2	111	.9
38	44.4	75	12.5	112	.8
39	43.5	76	11.9	113	.7
40	42.5	77	11.2	114	.6
41	41.5	78	10.6	115	.5

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	5	6	7	8	9	10	11	12	13	14
5	83.7	83.2	82.9	82.4	82.0	81.6	81.2	80.8	80.6	80.3
6	83.2	82.7	82.3	81.8	81.4	80.9	80.5	80.2	79.9	79.6
7	82.9	82.3	81.9	81.4	80.9	80.4	80.0	79.6	79.3	79.0
8	82.4	81.8	81.4	80.8	80.3	79.9	79.4	79.0	78.7	78.3
9	82.0	81.4	80.9	80.3	79.8	79.3	78.8	78.4	78.1	77.7
10	81.6	80.9	80.4	79.9	79.3	78.8	78.3	77.8	77.5	77.0
11	81.2	80.5	80.0	79.4	78.8	78.3	77.8	77.3	76.9	76.4
12	80.8	80.2	79.6	79.0	78.4	77.8	77.3	76.7	76.3	75.8
13	80.6	79.9	79.3	78.7	78.1	77.5	76.9	76.3	75.9	75.4
14	80.3	79.6	79.0	78.3	77.7	77.0	76.4	75.8	75.4	74.9
15	80.0	79.3	78.6	77.9	77.3	76.6	76.0	75.4	74.9	74.4
16	79.7	79.0	78.3	77.6	76.9	76.2	75.6	75.0	74.5	73.9
17	79.5	78.7	78.0	77.3	76.6	75.9	75.2	74.6	74.0	73.4
18	79.3	78.5	77.9	77.1	76.4	75.6	74.9	74.3	73.7	73.1
19	79.1	78.3	77.6	76.8	76.1	75.3	74.6	73.9	73.3	72.7
20	78.9	78.1	77.4	76.6	75.8	75.0	74.3	73.6	73.0	72.3
21	78.7	77.8	77.1	76.3	75.5	74.8	74.0	73.3	72.6	71.9
22	78.5	77.7	76.9	76.1	75.3	74.5	73.7	73.0	72.3	71.6
23	78.4	77.6	76.8	76.0	75.2	74.3	73.6	72.8	72.1	71.4
24	78.3	77.4	76.6	75.8	74.9	74.1	73.3	72.5	71.8	71.1
25	78.1	77.2	76.5	75.6	74.7	73.9	73.1	72.3	71.6	70.8
26	78.0	77.1	76.3	75.4	74.6	73.7	72.9	72.0	71.3	70.5
27	77.9	77.0	76.2	75.4	74.5	73.6	72.8	71.9	71.2	70.4
28	77.8	76.9	76.1	75.2	74.3	73.4	72.6	71.7	71.0	70.2
29	77.7	76.8	76.0	75.1	74.2	73.3	72.4	71.5	70.8	69.9
30	77.7	76.8	75.9	75.0	74.1	73.2	72.3	71.5	70.7	69.8
31	77.6	76.6	75.8	74.9	74.0	73.1	72.2	71.3	70.5	69.7
32	77.5	76.5	75.7	74.8	73.9	72.9	72.0	71.1	70.4	69.5
33	77.5	76.5	75.7	74.8	73.8	72.9	72.0	71.1	70.3	69.4
34	77.4	76.4	75.6	74.6	73.7	72.8	71.9	71.0	70.1	69.3
35	77.3	76.3	75.5	74.5	73.6	72.7	71.7	70.8	70.0	69.1
36	77.3	76.3	75.5	74.5	73.6	72.7	71.7	70.8	70.0	69.1
37	77.2	76.3	75.4	74.5	73.5	72.6	71.6	70.7	69.9	68.9
38	77.1	76.2	75.3	74.4	73.4	72.5	71.5	70.6	69.7	68.8
39	77.2	76.2	75.3	74.4	73.4	72.5	71.5	70.6	69.7	68.8
40	77.1	76.1	75.2	74.3	73.3	72.4	71.4	70.5	69.6	68.7
41	77.0	76.0	75.2	74.2	73.2	72.3	71.3	70.4	69.5	68.6
42	77.0	76.1	75.2	74.2	73.2	72.3	71.3	70.4	69.5	68.6
43	77.0	76.0	75.1	74.1	73.2	72.2	71.2	70.3	69.4	68.4
44	77.0	76.0	75.1	74.1	73.2	72.2	71.2	70.3	69.4	68.4
45	76.9	75.9	75.0	74.1	73.1	72.1	71.1	70.2	69.3	68.3
46	76.9	75.9	75.0	74.1	73.1	72.1	71.1	70.2	69.3	68.3
47	76.9	75.9	75.1	74.1	73.1	72.1	71.1	70.2	69.3	68.3
48	76.8	75.8	75.0	74.0	73.0	72.0	71.0	70.1	69.2	68.2
49	76.8	75.8	75.0	74.0	73.0	72.0	71.0	70.0	69.2	68.2
50	76.8	75.8	75.0	74.0	73.0	72.0	71.0	70.0	69.2	68.2
51	76.8	75.8	75.0	74.0	73.0	72.0	71.0	70.0	69.1	68.2
52	76.8	75.8	74.9	74.0	73.0	72.0	71.0	70.0	69.1	68.2
53	76.8	75.8	74.9	73.9	73.0	72.0	71.0	70.0	69.1	68.1
54	76.8	75.8	74.9	73.9	72.9	72.0	71.0	70.0	69.1	68.1
55	76.8	75.8	74.9	73.9	72.9	71.9	70.9	70.0	69.1	68.1
56	76.8	75.8	74.9	73.9	72.9	71.9	70.9	69.9	69.0	68.0
57	76.7	75.7	74.8	73.9	72.9	71.9	70.9	69.9	69.0	68.0
58	76.7	75.7	74.8	73.8	72.8	71.8	70.8	69.9	69.0	68.0
59	76.7	75.7	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
60	76.7	75.7	74.8	73.8	72.8	71.9	70.9	69.9	69.0	68.0
61	76.7	75.7	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
62	76.7	75.7	74.8	73.8	72.8	71.8	70.9	69.9	69.0	68.0

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	5	6	7	8	9	10	11	12	13	14
63	76.7	75.7	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
64	76.7	75.7	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
65	76.7	75.7	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
66	76.7	75.7	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
67	76.7	75.7	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
68	76.7	75.7	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
69	76.6	75.6	74.7	73.8	72.8	71.8	70.8	69.8	68.9	67.9
70	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
71	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.9
72	76.6	75.6	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
73	76.6	75.6	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
74	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
75	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
76	76.6	75.6	74.8	73.8	72.8	71.8	70.8	69.8	68.9	67.9
77	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
78	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
79	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
80	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.9	67.9
81	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
82	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
83	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
84	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
85	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
86	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
87	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
88	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
89	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
90	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
91	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
92	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
93	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
94	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
95	76.6	75.6	74.7	73.7	72.7	71.7	70.8	69.8	68.9	67.9
96	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
97	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
98	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
99	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
100	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
101	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
102	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
103	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
104	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
105	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
106	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
107	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
108	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
109	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
110	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
111	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
112	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
113	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
114	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8
115	76.6	75.6	74.7	73.7	72.7	71.7	70.7	69.7	68.8	67.8

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	15	16	17	18	19	20	21	22	23	24
15	73.8	73.3	72.8	72.5	72.1	71.7	71.3	70.9	70.7	70.3
16	73.3	72.8	72.3	71.9	71.5	71.0	70.6	70.2	70.0	69.6
17	72.8	72.3	71.8	71.4	70.9	70.4	70.0	69.6	69.3	68.9
18	72.5	71.9	71.4	70.9	70.4	69.9	69.5	69.1	68.7	68.4
19	72.1	71.5	70.9	70.4	69.9	69.4	68.9	68.4	68.1	67.7
20	71.7	71.0	70.4	69.9	69.4	68.9	68.3	67.9	67.5	67.1
21	71.3	70.6	70.0	69.5	68.9	68.3	67.8	67.3	66.9	66.5
22	70.9	70.2	69.6	69.1	68.4	67.9	67.3	66.8	66.4	65.9
23	70.7	70.0	69.3	68.7	68.1	67.5	66.9	66.4	65.9	65.4
24	70.3	69.6	68.9	68.4	67.7	67.1	66.5	65.9	65.4	64.9
25	70.0	69.3	68.6	68.0	67.3	66.7	66.0	65.4	64.9	64.4
26	69.8	69.0	68.3	67.6	66.9	66.3	65.6	65.0	64.5	63.9
27	69.6	68.8	68.1	67.4	66.7	66.0	65.3	64.7	64.1	63.5
28	69.4	68.6	67.8	67.1	66.4	65.7	65.0	64.3	63.7	63.1
29	69.1	68.3	67.5	66.8	66.1	65.3	64.6	63.9	63.3	62.7
30	69.0	68.2	67.4	66.7	65.9	65.1	64.4	63.7	63.1	62.4
31	68.8	68.0	67.1	66.4	65.6	64.8	64.1	63.3	62.7	62.0
32	68.6	67.8	66.9	66.2	65.4	64.6	63.8	63.0	62.4	61.7
33	68.5	67.7	66.8	66.1	65.2	64.4	63.6	62.9	62.2	61.4
34	68.4	67.5	66.6	65.9	65.0	64.2	63.4	62.6	61.9	61.1
35	68.2	67.3	66.4	65.7	64.8	64.0	63.1	62.3	61.6	60.9
36	68.2	67.3	66.4	65.6	64.7	63.9	63.0	62.2	61.5	60.7
37	68.0	67.1	66.2	65.4	64.5	63.7	62.8	62.0	61.2	60.4
38	67.9	67.0	66.1	65.3	64.4	63.5	62.6	61.8	61.0	60.2
39	67.9	66.9	66.0	65.2	64.3	63.4	62.5	61.7	60.9	60.1
40	67.7	66.8	65.9	65.1	64.2	63.3	62.4	61.5	60.7	59.9
41	67.6	66.7	65.8	64.9	64.0	63.1	62.2	61.3	60.5	59.7
42	67.6	66.7	65.7	64.9	64.0	63.1	62.1	61.2	60.5	59.6
43	67.5	66.5	65.6	64.8	63.8	62.9	62.0	61.1	60.3	59.4
44	67.5	66.5	65.6	64.7	63.8	62.9	61.9	61.0	60.2	59.3
45	67.4	66.4	65.5	64.6	63.7	62.7	61.8	60.9	60.1	59.2
46	67.4	66.4	65.4	64.6	63.6	62.7	61.8	60.8	60.0	59.1
47	67.4	66.4	65.4	64.6	63.6	62.7	61.7	60.8	60.0	59.0
48	67.2	66.3	65.3	64.4	63.5	62.5	61.6	60.6	59.8	58.9
49	67.2	66.3	65.3	64.4	63.5	62.5	61.5	60.6	59.8	58.8
50	67.2	66.2	65.3	64.4	63.4	62.5	61.5	60.6	59.7	58.8
51	67.2	66.2	65.2	64.4	63.4	62.4	61.5	60.5	59.7	58.7
52	67.2	66.2	65.2	64.3	63.4	62.4	61.4	60.5	59.6	58.7
53	67.2	66.2	65.2	64.3	63.3	62.4	61.4	60.4	59.6	58.6
54	67.1	66.1	65.2	64.3	63.3	62.3	61.4	60.4	59.5	58.6
55	67.1	66.1	65.1	64.2	63.3	62.3	61.3	60.3	59.5	58.5
56	67.1	66.1	65.1	64.2	63.2	62.3	61.3	60.3	59.4	58.5
57	67.0	66.0	65.1	64.2	63.2	62.2	61.2	60.2	59.4	58.4
58	67.0	66.0	65.0	64.1	63.1	62.2	61.2	60.2	59.3	58.3
59	66.9	66.0	65.0	64.1	63.1	62.1	61.1	60.1	59.3	58.3
60	67.0	66.0	65.0	64.1	63.1	62.2	61.2	60.2	59.3	58.3
61	66.9	65.9	65.0	64.1	63.1	62.1	61.1	60.1	59.2	58.3
62	67.0	66.0	65.0	64.1	63.1	62.1	61.1	60.2	59.3	58.3
63	66.9	65.9	64.9	64.0	63.0	62.1	61.1	60.1	59.2	58.2
64	66.9	65.9	64.9	64.1	63.1	62.1	61.1	60.1	59.2	58.2
65	66.9	66.0	65.0	64.1	63.1	62.1	61.1	60.1	59.2	58.2
66	66.9	66.0	65.0	64.1	63.1	62.1	61.1	60.1	59.2	58.2
67	66.9	65.9	64.9	64.0	63.1	62.1	61.1	60.1	59.2	58.2
68	66.9	65.9	64.9	64.0	63.0	62.0	61.0	60.0	59.2	58.2
69	66.9	65.9	64.9	64.0	63.0	62.0	61.0	60.0	59.1	58.1
70	66.8	65.8	64.8	63.9	62.9	61.9	61.0	60.0	59.1	58.1
71	66.9	65.9	64.9	64.0	63.0	62.0	61.0	60.0	59.1	58.1
72	66.9	65.9	64.9	64.0	63.0	62.0	61.0	60.0	59.1	58.1

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	15	16	17	18	19	20	21	22	23	24
73	66.9	65.9	64.9	64.0	63.0	62.0	61.0	60.0	59.1	58.1
74	66.8	65.9	64.9	64.0	63.0	62.0	61.0	60.0	59.1	58.1
75	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
76	66.9	65.9	64.9	64.0	63.0	62.0	61.0	60.0	59.1	58.1
77	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
78	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
79	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
80	66.9	65.9	64.9	64.0	63.0	62.0	61.0	60.0	59.1	58.1
81	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
82	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
83	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.1	58.1
84	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
85	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
86	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
87	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
88	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
89	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
90	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
91	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
92	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
93	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
94	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
95	66.9	65.9	64.9	64.0	63.0	62.0	61.0	60.0	59.1	58.1
96	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
97	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
98	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
99	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
100	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
101	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
102	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
103	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
104	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
105	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
106	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
107	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
108	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
109	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
110	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
111	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
112	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
113	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
114	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0
115	66.8	65.8	64.8	63.9	62.9	61.9	60.9	59.9	59.0	58.0

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	25	26	27	28	29	30	31	32	33	34
25	63.8	63.3	62.9	62.5	62.0	61.7	61.3	61.0	60.7	60.4
26	63.3	62.8	62.4	61.9	61.4	61.1	60.7	60.3	60.0	59.7
27	62.9	62.4	61.9	61.4	60.9	60.6	60.1	59.7	59.4	59.1
28	62.5	61.9	61.4	60.9	60.4	60.0	59.5	59.1	58.8	58.4
29	62.0	61.4	60.9	60.4	59.8	59.4	58.9	58.5	58.1	57.7
30	61.7	61.1	60.6	60.0	59.4	59.0	58.5	58.0	57.6	57.2
31	61.3	60.7	60.1	59.5	58.9	58.5	57.9	57.4	57.0	56.6
32	61.0	60.3	59.7	59.1	58.5	58.0	57.4	56.9	56.5	56.0
33	60.7	60.0	59.4	58.8	58.1	57.6	57.0	56.5	56.0	55.5
34	60.4	59.7	59.1	58.4	57.7	57.2	56.6	56.0	55.5	55.0
35	60.1	59.3	58.7	58.0	57.3	56.8	56.1	55.5	55.0	54.5
36	59.9	59.1	58.5	57.8	57.1	56.5	55.8	55.2	54.7	54.1
37	59.6	58.9	58.2	57.4	56.7	56.1	55.4	54.8	54.2	53.6
38	59.4	58.6	57.9	57.1	56.4	55.8	55.0	54.4	53.8	53.2
39	59.2	58.4	57.7	56.9	56.2	55.5	54.8	54.1	53.5	52.8
40	59.0	58.2	57.5	56.7	55.9	55.2	54.5	53.7	53.1	52.4
41	58.8	58.0	57.2	56.4	55.6	54.9	54.2	53.4	52.8	52.1
42	58.7	57.8	57.1	56.3	55.4	54.7	54.0	53.2	52.5	51.8
43	58.5	57.6	56.9	56.0	55.2	54.5	53.7	52.9	52.2	51.5
44	58.4	57.5	56.8	55.9	55.1	54.3	53.5	52.7	52.0	51.2
45	58.2	57.4	56.6	55.7	54.8	54.1	53.3	52.4	51.7	50.9
46	58.2	57.3	56.5	55.6	54.7	54.0	53.1	52.3	51.6	50.7
47	58.1	57.2	56.4	55.5	54.6	53.8	53.0	52.1	51.4	50.6
48	57.9	57.0	56.2	55.3	54.4	53.6	52.7	51.9	51.1	50.3
49	57.9	57.0	56.1	55.2	54.3	53.5	52.6	51.8	51.0	50.1
50	57.8	56.9	56.1	55.1	54.2	53.4	52.5	51.6	50.9	50.0
51	57.8	56.8	56.0	55.1	54.1	53.3	52.4	51.5	50.7	49.9
52	57.7	56.8	55.9	55.0	54.1	53.2	52.3	51.4	50.6	49.7
53	57.7	56.7	55.9	54.9	54.0	53.1	52.2	51.3	50.5	49.6
54	57.6	56.6	55.8	54.8	53.9	53.1	52.1	51.2	50.4	49.5
55	57.5	56.6	55.7	54.8	53.8	53.0	52.0	51.1	50.3	49.4
56	57.5	56.5	55.7	54.7	53.8	52.9	52.0	51.0	50.2	49.3
57	57.4	56.5	55.6	54.6	53.7	52.8	51.9	50.9	50.1	49.2
58	57.4	56.4	55.5	54.6	53.6	52.7	51.8	50.8	50.0	49.1
59	57.3	56.3	55.5	54.5	53.5	52.7	51.7	50.7	49.9	49.0
60	57.3	56.4	55.5	54.5	53.5	52.7	51.7	50.8	49.9	49.0
61	57.3	56.3	55.4	54.4	53.5	52.6	51.6	50.7	49.8	48.9
62	57.3	56.3	55.4	54.5	53.5	52.6	51.6	50.7	49.8	48.9
63	57.2	56.2	55.4	54.4	53.4	52.5	51.5	50.6	49.7	48.7
64	57.2	56.2	55.4	54.4	53.4	52.5	51.5	50.6	49.7	48.7
65	57.2	56.2	55.4	54.4	53.4	52.5	51.5	50.6	49.7	48.7
66	57.2	56.2	55.3	54.4	53.4	52.5	51.5	50.5	49.7	48.7
67	57.2	56.2	55.3	54.3	53.3	52.5	51.5	50.5	49.6	48.6
68	57.2	56.2	55.3	54.3	53.3	52.4	51.4	50.5	49.6	48.6
69	57.1	56.1	55.2	54.3	53.3	52.4	51.4	50.4	49.5	48.5
70	57.1	56.1	55.2	54.2	53.2	52.3	51.3	50.3	49.5	48.5
71	57.1	56.1	55.2	54.2	53.2	52.3	51.3	50.4	49.5	48.5
72	57.1	56.1	55.2	54.2	53.2	52.3	51.3	50.4	49.5	48.5
73	57.1	56.1	55.2	54.2	53.2	52.3	51.3	50.3	49.5	48.5
74	57.1	56.1	55.2	54.2	53.2	52.3	51.3	50.3	49.4	48.4
75	57.0	56.0	55.1	54.2	53.2	52.3	51.3	50.3	49.4	48.4
76	57.1	56.1	55.2	54.2	53.2	52.3	51.3	50.3	49.4	48.4
77	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.4
78	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.4
79	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
80	57.1	56.1	55.2	54.2	53.2	52.3	51.3	50.3	49.4	48.4
81	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
82	57.0	56.0	55.2	54.2	53.2	52.3	51.3	50.3	49.4	48.4

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	25	26	27	28	29	30	31	32	33	34
83	57.1	56.1	55.2	54.2	53.2	52.3	51.3	50.3	49.4	48.4
84	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
85	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
86	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
87	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
88	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
89	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
90	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
91	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
92	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
93	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
94	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
95	57.1	56.1	55.2	54.2	53.2	52.3	51.3	50.3	49.4	48.4
96	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
97	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
98	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
99	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
100	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
101	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
102	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
103	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
104	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
105	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
106	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
107	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
108	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
109	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
110	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
111	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
112	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
113	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
114	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3
115	57.0	56.0	55.1	54.1	53.1	52.2	51.2	50.2	49.3	48.3

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	35	36	37	38	39	40	41	42	43	44
35	53.9	53.5	53.0	52.5	52.2	51.8	51.4	51.1	50.7	50.5
36	53.5	53.1	52.5	52.1	51.7	51.2	50.8	50.5	50.1	49.9
37	53.0	52.5	52.0	51.5	51.1	50.6	50.2	49.8	49.4	49.2
38	52.5	52.1	51.5	50.9	50.5	50.0	49.6	49.2	48.8	48.5
39	52.2	51.7	51.1	50.5	50.1	49.6	49.1	48.7	48.2	47.9
40	51.8	51.2	50.6	50.0	49.6	49.0	48.5	48.1	47.6	47.2
41	51.4	50.8	50.2	49.6	49.1	48.5	47.9	47.5	47.0	46.6
42	51.1	50.5	49.8	49.2	48.7	48.1	47.5	47.1	46.5	46.1
43	50.7	50.1	49.4	48.8	48.2	47.6	47.0	46.5	46.0	45.5
44	50.5	49.9	49.2	48.5	47.9	47.2	46.6	46.1	45.5	45.1
45	50.2	49.5	48.8	48.1	47.5	46.8	46.2	45.6	45.0	44.6
46	50.0	49.3	48.5	47.8	47.2	46.5	45.8	45.3	44.6	44.1
47	49.8	49.1	48.3	47.5	46.9	46.2	45.5	44.9	44.3	43.8
48	49.5	48.8	48.0	47.2	46.6	45.8	45.1	44.5	43.8	43.3
49	49.3	48.6	47.8	47.0	46.3	45.6	44.8	44.2	43.5	42.9
50	49.1	48.4	47.6	46.8	46.1	45.3	44.6	43.9	43.2	42.6
51	49.0	48.2	47.4	46.6	45.9	45.1	44.3	43.6	42.9	42.3
52	48.9	48.1	47.2	46.4	45.7	44.9	44.1	43.4	42.6	42.0
53	48.7	47.9	47.1	46.2	45.5	44.7	43.8	43.1	42.4	41.7
54	48.6	47.8	46.9	46.1	45.3	44.5	43.6	42.9	42.1	41.4
55	48.5	47.7	46.8	45.9	45.1	44.3	43.4	42.7	41.9	41.2
56	48.3	47.5	46.6	45.8	45.0	44.1	43.2	42.5	41.7	41.0
57	48.2	47.4	46.5	45.6	44.8	43.9	43.1	42.3	41.5	40.7
58	48.1	47.3	46.4	45.5	44.7	43.8	42.9	42.1	41.3	40.5
59	48.0	47.2	46.3	45.3	44.5	43.6	42.7	42.0	41.1	40.3
60	48.0	47.2	46.2	45.3	44.5	43.6	42.7	41.9	41.0	40.2
61	47.9	47.1	46.1	45.2	44.4	43.4	42.5	41.7	40.8	40.0
62	47.9	47.0	46.1	45.2	44.3	43.4	42.5	41.7	40.8	40.0
63	47.8	46.9	46.0	45.0	44.2	43.3	42.3	41.5	40.6	39.8
64	47.8	46.9	46.0	45.0	44.2	43.2	42.3	41.4	40.5	39.7
65	47.7	46.9	45.9	45.0	44.1	43.2	42.2	41.4	40.5	39.6
66	47.7	46.8	45.9	44.9	44.1	43.1	42.2	41.3	40.4	39.5
67	47.7	46.8	45.8	44.9	44.0	43.0	42.1	41.2	40.3	39.5
68	47.6	46.7	45.8	44.8	43.9	43.0	42.0	41.2	40.2	39.4
69	47.6	46.7	45.7	44.7	43.9	42.9	41.9	41.1	40.1	39.3
70	47.5	46.6	45.6	44.7	43.8	42.8	41.9	41.0	40.0	39.2
71	47.5	46.6	45.6	44.7	43.8	42.8	41.8	41.0	40.0	39.1
72	47.5	46.6	45.6	44.7	43.8	42.8	41.8	41.0	40.0	39.1
73	47.5	46.6	45.6	44.6	43.7	42.8	41.8	40.9	39.9	39.1
74	47.4	46.6	45.6	44.6	43.7	42.7	41.7	40.9	39.9	39.0
75	47.4	46.5	45.5	44.5	43.7	42.7	41.7	40.8	39.8	39.0
76	47.4	46.5	45.6	44.6	43.7	42.7	41.7	40.8	39.9	39.0
77	47.4	46.5	45.5	44.5	43.6	42.6	41.6	40.7	39.8	38.9
78	47.4	46.5	45.5	44.5	43.6	42.6	41.6	40.7	39.7	38.9
79	47.3	46.4	45.5	44.5	43.6	42.6	41.6	40.7	39.7	38.8
80	47.4	46.5	45.5	44.5	43.6	42.6	41.6	40.8	39.8	38.9
81	47.3	46.5	45.5	44.5	43.6	42.6	41.6	40.7	39.7	38.8
82	47.4	46.5	45.5	44.5	43.6	42.6	41.6	40.7	39.7	38.8
83	47.4	46.5	45.5	44.5	43.6	42.6	41.6	40.7	39.7	38.8
84	47.4	46.5	45.5	44.5	43.6	42.6	41.6	40.7	39.7	38.8
85	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
86	47.3	46.4	45.4	44.4	43.6	42.6	41.6	40.7	39.7	38.8
87	47.3	46.5	45.5	44.5	43.6	42.6	41.6	40.7	39.7	38.8
88	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.7	39.7	38.8
89	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
90	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
91	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.7	38.8
92	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	35	36	37	38	39	40	41	42	43	44
93	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
94	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
95	47.4	46.5	45.5	44.5	43.6	42.6	41.6	40.7	39.7	38.8
96	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
97	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
98	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
99	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
100	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.7	38.8
101	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
102	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
103	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
104	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
105	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
106	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
107	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
108	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
109	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
110	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
111	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
112	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
113	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
114	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7
115	47.3	46.4	45.4	44.4	43.5	42.5	41.5	40.6	39.6	38.7

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	45	46	47	48	49	50	51	52	53	54
45	44.0	43.6	43.1	42.6	42.3	41.9	41.6	41.3	41.0	40.7
46	43.6	43.1	42.7	42.1	41.7	41.4	41.0	40.7	40.3	40.0
47	43.1	42.7	42.2	41.6	41.2	40.8	40.4	40.1	39.7	39.4
48	42.6	42.1	41.6	41.1	40.6	40.2	39.8	39.4	39.0	38.7
49	42.3	41.7	41.2	40.6	40.1	39.7	39.3	38.8	38.5	38.1
50	41.9	41.4	40.8	40.2	39.7	39.2	38.8	38.3	37.9	37.5
51	41.6	41.0	40.4	39.8	39.3	38.8	38.3	37.8	37.4	37.0
52	41.3	40.7	40.1	39.4	38.8	38.3	37.8	37.3	36.9	36.4
53	41.0	40.3	39.7	39.0	38.5	37.9	37.4	36.9	36.4	35.9
54	40.7	40.0	39.4	38.7	38.1	37.5	37.0	36.4	35.9	35.4
55	40.4	39.7	39.1	38.4	37.7	37.1	36.6	36.0	35.5	34.9
56	40.2	39.5	38.8	38.0	37.4	36.8	36.2	35.6	35.0	34.5
57	39.9	39.2	38.5	37.7	37.1	36.4	35.8	35.2	34.6	34.1
58	39.7	39.0	38.3	37.5	36.8	36.1	35.5	34.8	34.2	33.7
59	39.5	38.7	38.0	37.2	36.5	35.8	35.1	34.5	33.9	33.3
60	39.4	38.6	37.9	37.0	36.3	35.6	34.9	34.3	33.6	33.0
61	39.2	38.4	37.6	36.8	36.1	35.3	34.6	34.0	33.3	32.6
62	39.1	38.3	37.5	36.7	35.9	35.2	34.5	33.8	33.1	32.4
63	38.9	38.1	37.3	36.4	35.7	34.9	34.2	33.5	32.8	32.1
64	38.8	38.0	37.2	36.3	35.5	34.8	34.0	33.3	32.6	31.8
65	38.7	37.9	37.1	36.2	35.4	34.6	33.9	33.1	32.4	31.6
66	38.6	37.8	37.0	36.1	35.3	34.5	33.7	32.9	32.2	31.4
67	38.5	37.7	36.9	36.0	35.1	34.3	33.5	32.8	32.0	31.2
68	38.4	37.6	36.8	35.8	35.0	34.2	33.4	32.6	31.8	31.0
69	38.3	37.5	36.6	35.7	34.9	34.1	33.2	32.4	31.6	30.9
70	38.2	37.4	36.5	35.6	34.7	33.9	33.1	32.3	31.5	30.7
71	38.2	37.3	36.5	35.5	34.7	33.9	33.0	32.2	31.4	30.6
72	38.2	37.3	36.4	35.5	34.6	33.8	33.0	32.1	31.3	30.5
73	38.1	37.2	36.4	35.4	34.6	33.7	32.9	32.0	31.2	30.4
74	38.1	37.2	36.3	35.4	34.5	33.6	32.8	31.9	31.1	30.3
75	38.0	37.1	36.2	35.3	34.4	33.5	32.7	31.8	31.0	30.1
76	38.0	37.1	36.2	35.3	34.4	33.5	32.7	31.8	31.0	30.1
77	37.9	37.0	36.1	35.2	34.3	33.4	32.6	31.7	30.8	30.0
78	37.9	37.0	36.1	35.1	34.3	33.4	32.5	31.7	30.8	29.9
79	37.8	37.0	36.1	35.1	34.2	33.3	32.5	31.6	30.7	29.9
80	37.9	37.0	36.1	35.1	34.3	33.4	32.5	31.6	30.8	29.9
81	37.8	36.9	36.1	35.1	34.2	33.3	32.4	31.5	30.7	29.8
82	37.8	37.0	36.1	35.1	34.2	33.3	32.4	31.5	30.7	29.8
83	37.8	36.9	36.1	35.1	34.2	33.3	32.4	31.5	30.6	29.8
84	37.8	36.9	36.0	35.0	34.1	33.3	32.4	31.5	30.6	29.7
85	37.8	36.9	36.0	35.0	34.1	33.2	32.3	31.4	30.5	29.7
86	37.8	36.9	36.0	35.0	34.1	33.2	32.3	31.4	30.6	29.7
87	37.8	36.9	36.0	35.0	34.1	33.2	32.3	31.4	30.5	29.7
88	37.8	36.9	36.0	35.0	34.1	33.2	32.3	31.4	30.5	29.6
89	37.7	36.8	35.9	34.9	34.0	33.1	32.3	31.4	30.5	29.6
90	37.7	36.9	36.0	35.0	34.1	33.2	32.3	31.4	30.5	29.6
91	37.8	36.9	36.0	35.0	34.1	33.2	32.3	31.4	30.5	29.6
92	37.7	36.8	35.9	35.0	34.1	33.2	32.3	31.4	30.5	29.6
93	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
94	37.7	36.8	36.0	35.0	34.1	33.2	32.3	31.4	30.5	29.6
95	37.8	36.9	36.0	35.0	34.1	33.2	32.3	31.4	30.5	29.6
96	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
97	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
98	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
99	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
100	37.8	36.9	36.0	35.0	34.1	33.2	32.3	31.4	30.5	29.6
101	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
102	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	45	46	47	48	49	50	51	52	53	54
103	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
104	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
105	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
106	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
107	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
108	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
109	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
110	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
111	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
112	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
113	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
114	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5
115	37.7	36.8	35.9	34.9	34.0	33.1	32.2	31.3	30.4	29.5

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	55	56	57	58	59	60	61	62	63	64
55	34.5	34.0	33.5	33.1	32.7	32.4	32.0	31.7	31.4	31.1
56	34.0	33.5	33.0	32.5	32.1	31.8	31.4	31.1	30.7	30.5
57	33.5	33.0	32.5	32.0	31.5	31.2	30.8	30.5	30.1	29.8
58	33.1	32.5	32.0	31.5	31.0	30.6	30.2	29.9	29.5	29.2
59	32.7	32.1	31.5	31.0	30.5	30.1	29.6	29.3	28.9	28.5
60	32.4	31.8	31.2	30.6	30.1	29.7	29.2	28.8	28.4	28.0
61	32.0	31.4	30.8	30.2	29.6	29.2	28.7	28.3	27.8	27.4
62	31.7	31.1	30.5	29.9	29.3	28.8	28.3	27.9	27.3	27.0
63	31.4	30.7	30.1	29.5	28.9	28.4	27.8	27.3	26.8	26.4
64	31.1	30.5	29.8	29.2	28.5	28.0	27.4	27.0	26.4	26.0
65	30.9	30.2	29.5	28.9	28.2	27.7	27.1	26.6	26.0	25.5
66	30.7	30.0	29.3	28.6	27.9	27.4	26.7	26.2	25.6	25.1
67	30.5	29.8	29.0	28.3	27.6	27.1	26.4	25.9	25.3	24.7
68	30.3	29.5	28.8	28.1	27.4	26.8	26.1	25.5	24.9	24.4
69	30.1	29.3	28.6	27.8	27.1	26.5	25.8	25.2	24.5	24.0
70	29.9	29.1	28.3	27.6	26.8	26.2	25.5	24.9	24.2	23.6
71	29.8	29.0	28.2	27.4	26.7	26.0	25.3	24.7	24.0	23.4
72	29.7	28.9	28.1	27.3	26.5	25.9	25.1	24.5	23.8	23.1
73	29.5	28.7	27.9	27.1	26.4	25.7	24.9	24.3	23.5	22.9
74	29.4	28.6	27.8	27.0	26.2	25.5	24.7	24.1	23.3	22.7
75	29.3	28.5	27.6	26.8	26.0	25.3	24.5	23.9	23.1	22.4
76	29.3	28.4	27.6	26.8	26.0	25.2	24.4	23.8	23.0	22.3
77	29.1	28.3	27.4	26.6	25.8	25.1	24.2	23.5	22.8	22.1
78	29.1	28.2	27.4	26.5	25.7	25.0	24.1	23.4	22.6	21.9
79	29.0	28.1	27.3	26.4	25.6	24.9	24.0	23.3	22.5	21.8
80	29.0	28.2	27.3	26.4	25.6	24.8	24.0	23.3	22.4	21.7
81	28.9	28.1	27.2	26.3	25.5	24.7	23.9	23.1	22.3	21.6
82	28.9	28.0	27.2	26.3	25.4	24.7	23.8	23.1	22.2	21.5
83	28.9	28.0	27.1	26.3	25.4	24.6	23.8	23.0	22.2	21.4
84	28.8	28.0	27.1	26.2	25.3	24.6	23.7	22.9	22.1	21.3
85	28.8	27.9	27.0	26.1	25.3	24.5	23.6	22.9	22.0	21.2
86	28.8	27.9	27.0	26.1	25.3	24.5	23.6	22.8	22.0	21.2
87	28.8	27.9	27.0	26.1	25.2	24.5	23.6	22.8	21.9	21.2
88	28.7	27.9	27.0	26.1	25.2	24.4	23.5	22.8	21.9	21.1
89	28.7	27.8	26.9	26.0	25.1	24.4	23.5	22.7	21.8	21.0
90	28.7	27.8	26.9	26.0	25.1	24.4	23.5	22.7	21.8	21.0
91	28.7	27.8	26.9	26.0	25.1	24.4	23.5	22.7	21.8	21.0
92	28.7	27.8	26.9	26.0	25.1	24.3	23.4	22.7	21.8	21.0
93	28.6	27.7	26.9	26.0	25.1	24.3	23.4	22.6	21.7	20.9
94	28.7	27.8	26.9	26.0	25.1	24.3	23.4	22.6	21.7	21.0
95	28.7	27.8	26.9	26.0	25.1	24.3	23.4	22.6	21.8	21.0
96	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.6	21.7	20.
97	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.7	20.
98	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.
99	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.
100	28.7	27.8	26.9	26.0	25.1	24.3	23.4	22.6	21.7	20.
101	28.6	27.8	26.9	26.0	25.1	24.3	23.4	22.6	21.7	20.
102	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.
103	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.
104	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.
105	28.6	27.7	26.8	25.9	25.0	24.2	23.4	22.6	21.7	20.
106	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.
107	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.
108	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.
109	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20
110	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20
111	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20
112	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	55	56	57	58	59	60	61	62	63	64
113	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.8
114	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.8
115	28.6	27.7	26.8	25.9	25.0	24.2	23.3	22.5	21.6	20.8

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	65	66	67	68	69	70	71	72	73	74
65	25.1	24.7	24.3	23.9	23.5	23.1	22.8	22.6	22.3	22.
66	24.7	24.2	23.8	23.4	22.9	22.6	22.3	22.0	21.7	21.
67	24.3	23.8	23.3	22.9	22.4	22.0	21.7	21.4	21.1	20.
68	23.9	23.4	22.9	22.4	21.9	21.5	21.2	20.8	20.5	20.
69	23.5	22.9	22.4	21.9	21.5	21.0	20.7	20.3	20.0	19.
70	23.1	22.6	22.0	21.5	21.0	20.5	20.1	19.8	19.4	19.
71	22.8	22.3	21.7	21.2	20.7	20.1	19.7	19.4	19.0	18.
72	22.6	22.0	21.4	20.8	20.3	19.8	19.4	19.0	18.6	18.
73	22.3	21.7	21.1	20.5	20.0	19.4	19.0	18.6	18.1	17.
74	22.0	21.4	20.8	20.2	19.6	19.1	18.6	18.2	17.7	17.
75	21.8	21.2	20.5	19.9	19.3	18.7	18.3	17.8	17.3	16.
76	21.6	21.0	20.4	19.7	19.1	18.5	18.0	17.5	17.0	16.
77	21.4	20.7	20.1	19.4	18.8	18.2	17.7	17.2	16.7	16.
78	21.2	20.6	19.9	19.2	18.6	17.9	17.4	16.9	16.4	15.
79	21.1	20.4	19.7	19.0	18.4	17.7	17.2	16.6	16.1	15.
80	21.0	20.3	19.6	18.9	18.3	17.6	17.0	16.5	15.9	15.
81	20.9	20.1	19.4	18.7	18.0	17.4	16.8	16.2	15.7	15.
82	20.8	20.1	19.3	18.6	17.9	17.2	16.6	16.1	15.5	14.
83	20.7	20.0	19.2	18.5	17.8	17.1	16.5	15.9	15.3	14.
84	20.6	19.9	19.1	18.4	17.7	17.0	16.3	15.7	15.1	14.
85	20.5	19.7	19.0	18.3	17.5	16.8	16.2	15.6	15.0	14.
86	20.5	19.7	19.0	18.2	17.5	16.7	16.1	15.5	14.9	14.
87	20.4	19.7	18.9	18.1	17.4	16.7	16.0	15.4	14.8	14.
88	20.4	19.6	18.8	18.1	17.3	16.6	15.9	15.3	14.6	14.
89	20.3	19.5	18.7	18.0	17.2	16.5	15.8	15.2	14.5	13.
90	20.3	19.5	18.7	18.0	17.2	16.4	15.8	15.1	14.5	13.
91	20.2	19.5	18.7	17.9	17.2	16.4	15.7	15.1	14.4	13.
92	20.2	19.4	18.7	17.9	17.1	16.3	15.7	15.0	14.4	13.
93	20.2	19.4	18.6	17.8	17.0	16.3	15.6	14.9	14.3	13.
94	20.2	19.4	18.6	17.8	17.1	16.3	15.6	14.9	14.3	13.
95	20.2	19.4	18.6	17.8	17.1	16.3	15.6	14.9	14.3	13.
96	20.1	19.3	18.5	17.7	16.9	16.2	15.5	14.8	14.1	13.
97	20.1	19.3	18.5	17.7	16.9	16.1	15.5	14.8	14.1	13.
98	20.1	19.3	18.5	17.7	16.9	16.1	15.4	14.7	14.1	13.
99	20.0	19.2	18.4	17.7	16.9	16.1	15.4	14.7	14.0	13
100	20.1	19.3	18.5	17.7	16.9	16.2	15.5	14.8	14.1	13
101	20.1	19.3	18.5	17.7	16.9	16.1	15.4	14.7	14.1	13
102	20.1	19.3	18.5	17.7	16.9	16.1	15.4	14.7	14.0	13
103	20.0	19.2	18.4	17.6	16.8	16.1	15.4	14.7	14.0	13
104	20.0	19.2	18.4	17.6	16.8	16.0	15.3	14.6	13.9	13
105	20.1	19.3	18.5	17.7	16.9	16.1	15.4	14.7	14.0	13
106	20.0	19.2	18.4	17.6	16.8	16.0	15.3	14.6	14.0	13
107	20.0	19.2	18.4	17.6	16.8	16.0	15.3	14.6	13.9	13
108	20.0	19.2	18.4	17.6	16.8	16.0	15.3	14.6	13.9	13
109	20.0	19.2	18.4	17.6	16.8	16.0	15.3	14.6	13.9	13
110	20.0	19.2	18.4	17.6	16.8	16.0	15.3	14.6	13.9	13
111	20.0	19.2	18.4	17.6	16.8	16.0	15.3	14.6	13.9	13
112	20.0	19.2	18.4	17.6	16.8	16.0	15.3	14.6	13.9	13
113	20.0	19.2	18.4	17.6	16.8	16.1	15.4	14.7	14.0	13
114	20.0	19.2	18.4	17.6	16.8	16.0	15.4	14.7	14.0	13
115	20.0	19.2	18.4	17.6	16.8	16.0	15.3	14.6	13.9	13

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	75	76	77	78	79	80	81	82	83	84
75	16.4	16.1	15.7	15.4	15.1	14.9	14.6	14.4	14.2	14.0
76	16.1	15.8	15.3	15.0	14.7	14.5	14.1	13.9	13.7	13.5
77	15.7	15.3	14.9	14.5	14.2	13.9	13.6	13.4	13.2	12.9
78	15.4	15.0	14.5	14.2	13.8	13.5	13.2	13.0	12.7	12.5
79	15.1	14.7	14.2	13.8	13.4	13.2	12.8	12.5	12.3	12.0
80	14.9	14.5	13.9	13.5	13.2	12.9	12.5	12.2	11.9	11.7
81	14.6	14.1	13.6	13.2	12.8	12.5	12.1	11.8	11.5	11.2
82	14.4	13.9	13.4	13.0	12.5	12.2	11.8	11.5	11.2	10.9
83	14.2	13.7	13.2	12.7	12.3	11.9	11.5	11.2	10.9	10.6
84	14.0	13.5	12.9	12.5	12.0	11.7	11.2	10.9	10.6	10.2
85	13.8	13.3	12.7	12.2	11.7	11.4	10.9	10.6	10.2	9.9
86	13.6	13.1	12.6	12.1	11.6	11.2	10.7	10.4	10.0	9.7
87	13.5	13.0	12.4	11.9	11.4	11.0	10.6	10.2	9.8	9.4
88	13.4	12.9	12.3	11.8	11.3	10.9	10.4	10.0	9.6	9.2
89	13.3	12.7	12.1	11.6	11.1	10.7	10.2	9.8	9.4	9.0
90	13.2	12.7	12.0	11.5	11.0	10.6	10.1	9.6	9.2	8.9
91	13.1	12.6	11.9	11.4	10.9	10.5	9.9	9.5	9.1	8.7
92	13.0	12.5	11.9	11.3	10.8	10.3	9.8	9.4	3.0	8.6
93	12.9	12.4	11.7	11.2	10.7	10.2	9.7	9.3	8.8	8.4
94	12.9	12.4	11.7	11.2	10.6	10.2	9.6	9.2	8.8	8.3
95	12.9	12.4	11.7	11.1	10.6	10.1	9.6	9.1	8.7	8.3
96	12.8	12.2	11.6	11.0	10.4	10.0	9.4	9.0	8.5	8.1
97	12.8	12.2	11.5	10.9	10.4	9.9	9.4	8.9	8.5	8.0
98	12.7	12.1	11.5	10.9	10.3	9.9	9.3	8.8	8.4	7.9
99	12.7	12.1	11.4	10.8	10.3	9.8	9.2	8.8	8.3	7.9
100	12.7	12.1	11.5	10.9	10.3	9.8	9.3	8.8	8.3	7.9
101	12.7	12.1	11.4	10.8	10.3	9.8	9.2	8.7	8.3	7.8
102	12.6	12.1	11.4	10.8	10.2	9.7	9.2	8.7	8.2	7.7
103	12.6	12.0	11.3	10.7	10.2	9.7	9.1	8.6	8.1	7.7
104	12.6	12.0	11.3	10.7	10.1	9.6	9.0	8.6	8.1	7.6
105	12.6	12.0	11.3	10.7	10.2	9.7	9.1	8.6	8.1	7.6
106	12.6	12.0	11.3	10.7	10.1	9.6	9.0	8.5	8.0	7.6
107	12.5	11.9	11.2	10.6	10.0	9.5	9.0	8.5	8.0	7.5
108	12.5	12.0	11.3	10.7	10.1	9.6	9.0	8.5	8.0	7.5
109	12.5	11.9	11.2	10.6	10.0	9.5	8.9	8.4	7.9	7.4
110	12.5	11.9	11.2	10.6	10.0	9.5	8.9	8.4	7.9	7.4
111	12.5	11.9	11.2	10.6	10.0	9.5	8.9	8.4	8.0	7.5
112	12.5	11.9	11.2	10.7	10.1	9.6	9.0	8.5	8.0	7.5
113	12.6	12.0	11.3	10.7	10.1	9.6	9.0	8.5	8.0	7.5
114	12.6	12.0	11.3	10.7	10.1	9.6	9.0	8.5	8.0	7.5
115	12.5	11.9	11.2	10.6	10.0	9.5	8.9	8.4	7.9	7.4

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	85	86	87	88	89	90	91	92	93	94
85	9.6	9.3	9.1	8.8	8.6	8.5	8.3	8.1	8.0	7.9
86	9.3	9.1	8.8	8.6	8.3	8.2	8.0	7.8	7.7	7.6
87	9.1	8.8	8.6	8.3	8.0	7.9	7.7	7.5	7.4	7.3
88	8.8	8.6	8.3	8.0	7.8	7.6	7.4	7.2	7.0	7.0
89	8.6	8.3	8.0	7.8	7.5	7.3	7.1	6.9	6.7	6.6
90	8.5	8.2	7.9	7.6	7.3	7.1	6.9	6.7	6.5	6.4
91	8.3	8.0	7.7	7.4	7.1	6.9	6.7	6.5	6.3	6.2
92	8.1	7.8	7.5	7.2	6.9	6.7	6.5	6.3	6.1	6.0
93	8.0	7.7	7.4	7.0	6.7	6.5	6.3	6.1	5.9	5.7
94	7.9	7.6	7.3	7.0	6.6	6.4	6.2	6.0	5.7	5.6
95	7.8	7.5	7.2	6.9	6.5	6.3	6.1	5.9	5.6	5.5
96	7.7	7.3	7.0	6.7	6.3	6.1	5.9	5.6	5.4	5.3
97	7.6	7.2	6.9	6.6	6.2	6.0	5.7	5.5	5.3	5.1
98	7.5	7.1	6.8	6.5	6.1	5.9	5.6	5.4	5.1	5.0
99	7.4	7.1	6.7	6.4	6.0	5.8	5.5	5.3	5.0	4.9
100	7.4	7.1	6.7	6.4	6.0	5.8	5.5	5.2	5.0	4.8
101	7.3	7.0	6.6	6.3	5.9	5.6	5.4	5.1	4.9	4.7
102	7.3	6.9	6.5	6.2	5.8	5.5	5.3	5.0	4.8	4.6
103	7.2	6.8	6.4	6.1	5.7	5.4	5.2	4.9	4.7	4.5
104	7.1	6.7	6.4	6.0	5.6	5.4	5.1	4.8	4.5	4.4
105	7.1	6.8	6.4	6.0	5.6	5.4	5.1	4.8	4.5	4.4
106	7.1	6.7	6.3	5.9	5.5	5.3	5.0	4.7	4.4	4.3
107	7.0	6.6	6.2	5.8	5.5	5.2	4.9	4.6	4.3	4.1
108	7.0	6.6	6.2	5.9	5.5	5.2	4.9	4.6	4.3	4.1
109	6.9	6.5	6.2	5.8	5.4	5.1	4.8	4.5	4.2	4.0
110	7.0	6.6	6.2	5.8	5.4	5.1	4.8	4.5	4.2	4.0
111	7.0	6.6	6.2	5.8	5.4	5.1	4.8	4.5	4.2	4.0
112	7.0	6.6	6.2	5.8	5.4	5.1	4.8	4.5	4.2	4.0
113	7.0	6.6	6.2	5.8	5.4	5.1	4.8	4.5	4.2	4.0
114	7.0	6.6	6.2	5.8	5.4	5.1	4.8	4.5	4.2	4.0
115	6.9	6.5	6.1	5.7	5.3	5.0	4.7	4.4	4.1	3.9

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	95	96	97	98	99	100	101	102	103	104
95	5.4	5.1	5.0	4.9	4.7	4.7	4.6	4.4	4.3	4.2
96	5.1	4.9	4.7	4.6	4.5	4.4	4.3	4.2	4.0	3.9
97	5.0	4.7	4.6	4.5	4.3	4.3	4.1	4.0	3.9	3.8
98	4.9	4.6	4.5	4.3	4.2	4.1	4.0	3.8	3.7	3.6
99	4.7	4.5	4.3	4.2	4.0	4.0	3.8	3.7	3.5	3.4
100	4.7	4.4	4.3	4.1	4.0	3.9	3.8	3.6	3.5	3.3
101	4.6	4.3	4.1	4.0	3.8	3.8	3.6	3.5	3.3	3.2
102	4.4	4.2	4.0	3.8	3.7	3.6	3.5	3.3	3.2	3.0
103	4.3	4.0	3.9	3.7	3.5	3.5	3.3	3.2	3.0	2.9
104	4.2	3.9	3.8	3.6	3.4	3.3	3.2	3.0	2.9	2.7
105	4.2	3.9	3.7	3.6	3.4	3.3	3.1	3.0	2.8	2.7
106	4.1	3.8	3.6	3.4	3.3	3.2	3.0	2.8	2.7	2.5
107	4.0	3.7	3.5	3.3	3.1	3.1	2.9	2.7	2.5	2.4
108	4.0	3.7	3.5	3.3	3.1	3.0	2.8	2.7	2.5	2.3
109	3.8	3.6	3.4	3.2	3.0	2.9	2.7	2.5	2.4	2.2
110	3.8	3.5	3.4	3.2	3.0	2.9	2.7	2.5	2.3	2.1
111	3.8	3.5	3.3	3.1	2.9	2.9	2.7	2.5	2.3	2.1
112	3.8	3.5	3.3	3.1	2.9	2.8	2.6	2.4	2.3	2.1
113	3.8	3.5	3.3	3.1	2.9	2.8	2.6	2.4	2.2	2.0
114	3.8	3.5	3.3	3.1	2.9	2.8	2.6	2.4	2.2	2.0
115	3.7	3.4	3.2	3.0	2.8	2.7	2.5	2.3	2.1	1.9

TABLE VI - ORDINARY JOINT LIFE AND LAST SURVIVOR ANNUITIES TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	105	106	107	108	109	110	111	112	113	114	115
105	2.6	2.4	2.3	2.2	2.1	2.1	2.0	2.0	1.9	1.9	1.8
106	2.4	2.3	2.1	2.1	1.9	1.9	1.8	1.8	1.7	1.7	1.6
107	2.3	2.1	2.0	1.9	1.8	1.7	1.6	1.6	1.5	1.5	1.4
108	2.2	2.1	1.9	1.8	1.7	1.6	1.6	1.5	1.5	1.4	1.3
109	2.1	1.9	1.8	1.7	1.5	1.4	1.4	1.3	1.3	1.2	1.1
110	2.1	1.9	1.7	1.6	1.4	1.4	1.3	1.2	1.2	1.1	1.0
111	2.0	1.8	1.6	1.6	1.4	1.3	1.2	1.2	1.1	1.0	.9
112	2.0	1.8	1.6	1.5	1.3	1.2	1.2	1.1	1.0	.9	.8
113	1.9	1.7	1.5	1.5	1.3	1.2	1.1	1.0	.9	.8	.7
114	1.9	1.7	1.5	1.4	1.2	1.1	1.0	.9	.8	.7	.6
115	1.8	1.6	1.4	1.3	1.1	1.0	.9	.8	.7	.6	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	5	6	7	8	9	10	11	12	13	14
5	69.5	69.0	68.4	67.9	67.3	66.7	66.1	65.5	64.8	64.1
6	69.0	68.5	68.0	67.5	66.9	66.4	65.8	65.1	64.5	63.8
7	68.4	68.0	67.5	67.0	66.5	66.0	65.4	64.8	64.2	63.5
8	67.9	67.5	67.0	66.6	66.1	65.5	65.0	64.4	63.8	63.2
9	67.3	66.9	66.5	66.1	65.6	65.1	64.6	64.0	63.4	62.8
10	66.7	66.4	66.0	65.5	65.1	64.6	64.1	63.6	63.0	62.5
11	66.1	65.8	65.4	65.0	64.6	64.1	63.6	63.1	62.6	62.1
12	65.5	65.1	64.8	64.4	64.0	63.6	63.1	62.7	62.2	61.7
13	64.8	64.5	64.2	63.8	63.4	63.0	62.6	62.2	61.7	61.2
14	64.1	63.8	63.5	63.2	62.8	62.5	62.1	61.7	61.2	60.7
15	63.4	63.1	62.9	62.6	62.2	61.9	61.5	61.1	60.7	60.2
16	62.7	62.4	62.2	61.9	61.6	61.3	60.9	60.5	60.1	59.7
17	61.9	61.7	61.5	61.2	60.9	60.6	60.3	59.9	59.6	59.2
18	61.2	61.0	60.7	60.5	60.2	60.0	59.7	59.3	59.0	58.6
19	60.4	60.2	60.0	59.8	59.5	59.3	59.0	58.7	58.4	58.0
20	59.6	59.4	59.2	59.0	58.8	58.6	58.3	58.0	57.7	57.4
21	58.8	58.7	58.5	58.3	58.1	57.8	57.6	57.3	57.1	56.8
22	58.0	57.8	57.7	57.5	57.3	57.1	56.9	56.6	56.4	56.1
23	57.2	57.0	56.9	56.7	56.5	56.4	56.1	55.9	55.7	55.4
24	56.3	56.2	56.1	55.9	55.8	55.6	55.4	55.2	55.0	54.7
25	55.5	55.4	55.2	55.1	55.0	54.8	54.6	54.4	54.2	54.0
26	54.6	54.5	54.4	54.3	54.1	54.0	53.8	53.7	53.5	53.3
27	53.8	53.7	53.6	53.4	53.3	53.2	53.0	52.9	52.7	52.5
28	52.9	52.8	52.7	52.6	52.5	52.4	52.2	52.1	51.9	51.7
29	52.0	51.9	51.8	51.7	51.6	51.5	51.4	51.3	51.1	51.0
30	51.1	51.0	51.0	50.9	50.8	50.7	50.6	50.4	50.3	50.2
31	50.2	50.2	50.1	50.0	49.9	49.8	49.7	49.6	49.5	49.3
32	49.3	49.3	49.2	49.1	49.0	49.0	48.9	48.8	48.6	48.5
33	48.4	48.4	48.3	48.2	48.2	48.1	48.0	47.9	47.8	47.7
34	47.5	47.5	47.4	47.4	47.3	47.2	47.1	47.0	47.0	46.8
35	46.6	46.6	46.5	46.5	46.4	46.3	46.3	46.2	46.1	46.0
36	45.7	45.7	45.6	45.6	45.5	45.4	45.4	45.3	45.2	45.1
37	44.8	44.7	44.7	44.6	44.6	44.5	44.5	44.4	44.3	44.3
38	43.9	43.8	43.8	43.7	43.7	43.6	43.6	43.5	43.5	43.4
39	42.9	42.9	42.9	42.8	42.8	42.7	42.7	42.6	42.6	42.5
40	42.0	42.0	42.0	41.9	41.9	41.8	41.8	41.7	41.7	41.6
41	41.1	41.1	41.0	41.0	41.0	40.9	40.9	40.8	40.8	40.7
42	40.2	40.1	40.1	40.1	40.1	40.0	40.0	39.9	39.9	39.8
43	39.2	39.2	39.2	39.2	39.1	39.1	39.1	39.0	39.0	39.0
44	38.3	38.3	38.3	38.3	38.2	38.2	38.2	38.1	38.1	38.1
45	37.4	37.4	37.4	37.3	37.3	37.3	37.3	37.2	37.2	37.2
46	36.5	36.5	36.5	36.4	36.4	36.4	36.4	36.3	36.3	36.3
47	35.6	35.6	35.5	35.5	35.5	35.5	35.5	35.4	35.4	35.4
48	34.7	34.7	34.6	34.6	34.6	34.6	34.6	34.5	34.5	34.5
49	33.8	33.8	33.7	33.7	33.7	33.7	33.7	33.7	33.6	33.6
50	32.9	32.9	32.8	32.8	32.8	32.8	32.8	32.8	32.7	32.7
51	32.0	32.0	31.9	31.9	31.9	31.9	31.9	31.9	31.9	31.8
52	31.1	31.1	31.1	31.0	31.0	31.0	31.0	31.0	31.0	30.9
53	30.2	30.2	30.2	30.2	30.1	30.1	30.1	30.1	30.1	30.1
54	29.3	29.3	29.3	29.3	29.3	29.2	29.2	29.2	29.2	29.2
55	28.4	28.4	28.4	28.4	28.4	28.4	28.4	28.3	28.3	28.3
56	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5
57	26.7	26.7	26.7	26.6	26.6	26.6	26.6	26.6	26.6	26.6
58	25.8	25.8	25.8	25.8	25.8	25.8	25.8	25.7	25.7	25.7
59	24.9	24.9	24.9	24.9	24.9	24.9	24.9	24.9	24.9	24.9
60	24.1	24.1	24.1	24.1	24.1	24.0	24.0	24.0	24.0	24.0
61	23.2	23.2	23.2	23.2	23.2	23.2	23.2	23.2	23.2	23.2
62	22.4	22.4	22.4	22.4	22.4	22.4	22.3	22.3	22.3	22.3

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	5	6	7	8	9	10	11	12	13	14
63	21.5	21.5	21.5	21.5	21.5	21.5	21.5	21.5	21.5	21.5
64	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.7	20.7
65	19.9	19.9	19.9	19.9	19.9	19.9	19.9	19.9	19.9	19.9
66	19.1	19.1	19.1	19.1	19.1	19.1	19.1	19.1	19.1	19.1
67	18.3	18.3	18.3	18.3	18.3	18.3	18.3	18.3	18.3	18.3
68	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5
69	16.8	16.8	16.8	16.7	16.7	16.7	16.7	16.7	16.7	16.7
70	16.0	16.0	16.0	16.0	16.0	16.0	16.0	16.0	16.0	16.0
71	15.3	15.3	15.3	15.3	15.3	15.3	15.3	15.3	15.3	15.2
72	14.6	14.6	14.5	14.5	14.5	14.5	14.5	14.5	14.5	14.5
73	13.9	13.9	13.8	13.8	13.8	13.8	13.8	13.8	13.8	13.8
74	13.2	13.2	13.2	13.2	13.2	13.2	13.2	13.2	13.2	13.2
75	12.5	12.5	12.5	12.5	12.5	12.5	12.5	12.5	12.5	12.5
76	11.9	11.9	11.8	11.8	11.8	11.8	11.8	11.8	11.8	11.8
77	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2
78	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6
79	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0
80	9.5	9.5	9.5	9.5	9.5	9.5	9.5	9.5	9.4	9.4
81	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9
82	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4
83	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9
84	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4
85	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9
86	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5
87	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1
88	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7
89	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
90	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
91	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7
92	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4
93	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
94	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9
95	3.7	3.7	3.7	3.7	3.7	3.7	3.6	3.6	3.6	3.6
96	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4
97	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2
98	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
99	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
100	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7
101	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
102	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
103	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8
113	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
114	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	15	16	17	18	19	20	21	22	23	24
15	59.8	59.3	58.8	58.2	57.6	57.0	56.4	55.8	55.1	54.5
16	59.3	58.8	58.3	57.8	57.2	56.7	56.1	55.5	54.8	54.2
17	58.8	58.3	57.8	57.3	56.8	56.3	55.7	55.1	54.5	53.9
18	58.2	57.8	57.3	56.9	56.4	55.9	55.3	54.7	54.2	53.5
19	57.6	57.2	56.8	56.4	55.9	55.4	54.9	54.4	53.8	53.2
20	57.0	56.7	56.3	55.9	55.4	54.9	54.5	53.9	53.4	52.8
21	56.4	56.1	55.7	55.3	54.9	54.5	54.0	53.5	53.0	52.4
22	55.8	55.5	55.1	54.7	54.4	53.9	53.5	53.0	52.5	52.0
23	55.1	54.8	54.5	54.2	53.8	53.4	53.0	52.5	52.1	51.6
24	54.5	54.2	53.9	53.5	53.2	52.8	52.4	52.0	51.6	51.1
25	53.8	53.5	53.2	52.9	52.6	52.2	51.9	51.5	51.1	50.6
26	53.0	52.8	52.5	52.3	52.0	51.6	51.3	50.9	50.5	50.1
27	52.3	52.1	51.8	51.6	51.3	51.0	50.7	50.3	50.0	49.6
28	51.5	51.3	51.1	50.9	50.6	50.3	50.0	49.7	49.4	49.0
29	50.8	50.6	50.4	50.2	49.9	49.7	49.4	49.1	48.8	48.4
30	50.0	49.8	49.6	49.4	49.2	49.0	48.7	48.4	48.1	47.8
31	49.2	49.0	48.9	48.7	48.5	48.3	48.0	47.8	47.5	47.2
32	48.4	48.2	48.1	47.9	47.7	47.5	47.3	47.1	46.8	46.5
33	47.6	47.4	47.3	47.1	47.0	46.8	46.6	46.3	46.1	45.9
34	46.7	46.6	46.5	46.3	46.2	46.0	45.8	45.6	45.4	45.2
35	45.9	45.8	45.7	45.5	45.4	45.2	45.1	44.9	44.7	44.4
36	45.0	44.9	44.8	44.7	44.6	44.4	44.3	44.1	43.9	43.7
37	44.2	44.1	44.0	43.9	43.8	43.6	43.5	43.3	43.2	43.0
38	43.3	43.2	43.1	43.0	42.9	42.8	42.7	42.5	42.4	42.2
39	42.4	42.4	42.3	42.2	42.1	42.0	41.9	41.7	41.6	41.4
40	41.6	41.5	41.4	41.3	41.2	41.1	41.0	40.9	40.8	40.6
41	40.7	40.6	40.5	40.5	40.4	40.3	40.2	40.1	40.0	39.8
42	39.8	39.7	39.7	39.6	39.5	39.4	39.4	39.3	39.1	39.0
43	38.9	38.9	38.8	38.7	38.7	38.6	38.5	38.4	38.3	38.2
44	38.0	38.0	37.9	37.9	37.8	37.7	37.7	37.6	37.5	37.4
45	37.1	37.1	37.0	37.0	36.9	36.9	36.8	36.7	36.6	36.5
46	36.2	36.2	36.2	36.1	36.1	36.0	35.9	35.9	35.8	35.7
47	35.3	35.3	35.3	35.2	35.2	35.1	35.1	35.0	34.9	34.9
48	34.5	34.4	34.4	34.4	34.3	34.3	34.2	34.2	34.1	34.0
49	33.6	33.5	33.5	33.5	33.4	33.4	33.4	33.3	33.2	33.2
50	32.7	32.7	32.6	32.6	32.6	32.5	32.5	32.4	32.4	32.3
51	31.8	31.8	31.8	31.7	31.7	31.7	31.6	31.6	31.5	31.5
52	30.9	30.9	30.9	30.9	30.8	30.8	30.8	30.7	30.7	30.6
53	30.0	30.0	30.0	30.0	30.0	29.9	29.9	29.9	29.8	29.8
54	29.2	29.2	29.1	29.1	29.1	29.1	29.0	29.0	29.0	28.9
55	28.3	28.3	28.3	28.3	28.2	28.2	28.2	28.2	28.1	28.1
56	27.4	27.4	27.4	27.4	27.4	27.3	27.3	27.3	27.3	27.2
57	26.6	26.6	26.5	26.5	26.5	26.5	26.5	26.5	26.4	26.4
58	25.7	25.7	25.7	25.7	25.7	25.6	25.6	25.6	25.6	25.6
59	24.9	24.8	24.8	24.8	24.8	24.8	24.8	24.8	24.7	24.7
60	24.0	24.0	24.0	24.0	24.0	23.9	23.9	23.9	23.9	23.9
61	23.2	23.2	23.1	23.1	23.1	23.1	23.1	23.1	23.1	23.0
62	22.3	22.3	22.3	22.3	22.3	22.3	22.3	22.2	22.2	22.2
63	21.5	21.5	21.5	21.5	21.5	21.4	21.4	21.4	21.4	21.4
64	20.7	20.7	20.7	20.6	20.6	20.6	20.6	20.6	20.6	20.6
65	19.9	19.8	19.8	19.8	19.8	19.8	19.8	19.8	19.8	19.8
66	19.1	19.0	19.0	19.0	19.0	19.0	19.0	19.0	19.0	19.0
67	18.3	18.3	18.3	18.3	18.2	18.2	18.2	18.2	18.2	18.2
68	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.5	17.4	17.4
69	16.7	16.7	16.7	16.7	16.7	16.7	16.7	16.7	16.7	16.7
70	16.0	16.0	16.0	16.0	16.0	16.0	15.9	15.9	15.9	15.9
71	15.2	15.2	15.2	15.2	15.2	15.2	15.2	15.2	15.2	15.2
72	14.5	14.5	14.5	14.5	14.5	14.5	14.5	14.5	14.5	14.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	15	16	17	18	19	20	21	22	23	24
73	13.8	13.8	13.8	13.8	13.8	13.8	13.8	13.8	13.8	13.8
74	13.2	13.1	13.1	13.1	13.1	13.1	13.1	13.1	13.1	13.1
75	12.5	12.5	12.5	12.5	12.5	12.5	12.5	12.5	12.5	12.5
76	11.8	11.8	11.8	11.8	11.8	11.8	11.8	11.8	11.8	11.8
77	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2
78	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6
79	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0
80	9.4	9.4	9.4	9.4	9.4	9.4	9.4	9.4	9.4	9.4
81	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9
82	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4
83	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.8	7.8
84	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4
85	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9
86	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5
87	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1
88	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7
89	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
90	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
91	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7
92	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4
93	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
94	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9
95	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6
96	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4
97	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2
98	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
99	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
100	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7
101	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
102	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
103	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8
113	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
114	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	25	26	27	28	29	30	31	32	33	34
25	50.2	49.7	49.2	48.6	48.1	47.5	46.9	46.2	45.6	44.9
26	49.7	49.2	48.7	48.2	47.7	47.1	46.5	45.9	45.3	44.6
27	49.2	48.7	48.3	47.8	47.3	46.7	46.2	45.6	45.0	44.3
28	48.6	48.2	47.8	47.3	46.8	46.3	45.8	45.2	44.6	44.0
29	48.1	47.7	47.3	46.8	46.4	45.9	45.4	44.8	44.3	43.7
30	47.5	47.1	46.7	46.3	45.9	45.4	44.9	44.4	43.9	43.3
31	46.9	46.5	46.2	45.8	45.4	44.9	44.5	44.0	43.5	42.9
32	46.2	45.9	45.6	45.2	44.8	44.4	44.0	43.5	43.0	42.5
33	45.6	45.3	45.0	44.6	44.3	43.9	43.5	43.0	42.6	42.1
34	44.9	44.6	44.3	44.0	43.7	43.3	42.9	42.5	42.1	41.6
35	44.2	44.0	43.7	43.4	43.1	42.7	42.4	42.0	41.6	41.1
36	43.5	43.3	43.0	42.7	42.4	42.1	41.8	41.4	41.0	40.6
37	42.8	42.5	42.3	42.1	41.8	41.5	41.2	40.8	40.5	40.1
38	42.0	41.8	41.6	41.4	41.1	40.8	40.6	40.2	39.9	39.5
39	41.3	41.1	40.9	40.7	40.4	40.2	39.9	39.6	39.3	39.0
40	40.5	40.3	40.1	39.9	39.7	39.5	39.2	39.0	38.7	38.4
41	39.7	39.5	39.4	39.2	39.0	38.8	38.5	38.3	38.0	37.7
42	38.9	38.8	38.6	38.4	38.3	38.1	37.8	37.6	37.4	37.1
43	38.1	38.0	37.8	37.7	37.5	37.3	37.1	36.9	36.7	36.4
44	37.3	37.2	37.0	36.9	36.7	36.6	36.4	36.2	36.0	35.8
45	36.5	36.3	36.2	36.1	36.0	35.8	35.6	35.5	35.3	35.1
46	35.6	35.5	35.4	35.3	35.2	35.0	34.9	34.7	34.5	34.4
47	34.8	34.7	34.6	34.5	34.4	34.3	34.1	34.0	33.8	33.6
48	34.0	33.9	33.8	33.7	33.6	33.5	33.4	33.2	33.1	32.9
49	33.1	33.0	33.0	32.9	32.8	32.7	32.6	32.4	32.3	32.2
50	32.3	32.2	32.1	32.1	32.0	31.9	31.8	31.7	31.5	31.4
51	31.4	31.4	31.3	31.2	31.2	31.1	31.0	30.9	30.8	30.6
52	30.6	30.5	30.5	30.4	30.3	30.3	30.2	30.1	30.0	29.9
53	29.7	29.7	29.6	29.6	29.5	29.5	29.4	29.3	29.2	29.1
54	28.9	28.9	28.8	28.8	28.7	28.6	28.6	28.5	28.4	28.3
55	28.1	28.0	28.0	27.9	27.9	27.8	27.8	27.7	27.6	27.5
56	27.2	27.2	27.1	27.1	27.0	27.0	26.9	26.9	26.8	26.7
57	26.4	26.3	26.3	26.3	26.2	26.2	26.1	26.1	26.0	25.9
58	25.5	25.5	25.5	25.4	25.4	25.4	25.3	25.3	25.2	25.1
59	24.7	24.7	24.6	24.6	24.6	24.5	24.5	24.5	24.4	24.3
60	23.9	23.8	23.8	23.8	23.8	23.7	23.7	23.6	23.6	23.5
61	23.0	23.0	23.0	23.0	22.9	22.9	22.9	22.8	22.8	22.7
62	22.2	22.2	22.2	22.1	22.1	22.1	22.1	22.0	22.0	21.9
63	21.4	21.4	21.3	21.3	21.3	21.3	21.3	21.2	21.2	21.2
64	20.6	20.6	20.5	20.5	20.5	20.5	20.5	20.4	20.4	20.4
65	19.8	19.8	19.7	19.7	19.7	19.7	19.7	19.6	19.6	19.6
66	19.0	19.0	19.0	18.9	18.9	18.9	18.9	18.9	18.8	18.8
67	18.2	18.2	18.2	18.2	18.2	18.1	18.1	18.1	18.1	18.1
68	17.4	17.4	17.4	17.4	17.4	17.4	17.4	17.3	17.3	17.3
69	16.7	16.7	16.7	16.6	16.6	16.6	16.6	16.6	16.6	16.6
70	15.9	15.9	15.9	15.9	15.9	15.9	15.9	15.9	15.8	15.8
71	15.2	15.2	15.2	15.2	15.2	15.2	15.2	15.1	15.1	15.1
72	14.5	14.5	14.5	14.5	14.5	14.5	14.5	14.4	14.4	14.4
73	13.8	13.8	13.8	13.8	13.8	13.8	13.8	13.8	13.7	13.7
74	13.1	13.1	13.1	13.1	13.1	13.1	13.1	13.1	13.1	13.1
75	12.5	12.5	12.5	12.4	12.4	12.4	12.4	12.4	12.4	12.4
76	11.8	11.8	11.8	11.8	11.8	11.8	11.8	11.8	11.8	11.8
77	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.1
78	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.5
79	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0
80	9.4	9.4	9.4	9.4	9.4	9.4	9.4	9.4	9.4	9.4
81	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9
82	8.4	8.4	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	25	26	27	28	29	30	31	32	33	34
83	7.8	7.8	7.8	7.8	7.8	7.8	7.8	7.8	7.8	7.8
84	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4
85	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9
86	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5
87	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1
88	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7
89	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
90	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
91	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7
92	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4
93	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
94	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9
95	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6
96	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4
97	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2
98	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
99	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
100	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7
101	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
102	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
103	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8
113	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
114	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	35	36	37	38	39	40	41	42	43	44
35	40.7	40.2	39.7	39.2	38.6	38.0	37.4	36.8	36.2	35.5
36	40.2	39.7	39.3	38.7	38.2	37.7	37.1	36.5	35.9	35.2
37	39.7	39.3	38.8	38.3	37.8	37.3	36.7	36.2	35.6	34.9
38	39.2	38.7	38.3	37.9	37.4	36.9	36.3	35.8	35.2	34.6
39	38.6	38.2	37.8	37.4	36.9	36.4	35.9	35.4	34.9	34.3
40	38.0	37.7	37.3	36.9	36.4	36.0	35.5	35.0	34.5	34.0
41	37.4	37.1	36.7	36.3	35.9	35.5	35.1	34.6	34.1	33.6
42	36.8	36.5	36.2	35.8	35.4	35.0	34.6	34.1	33.7	33.2
43	36.2	35.9	35.6	35.2	34.9	34.5	34.1	33.7	33.2	32.8
44	35.5	35.2	34.9	34.6	34.3	34.0	33.6	33.2	32.8	32.3
45	34.8	34.6	34.3	34.0	33.7	33.4	33.0	32.7	32.3	31.8
46	34.1	33.9	33.7	33.4	33.1	32.8	32.5	32.1	31.8	31.4
47	33.4	33.2	33.0	32.8	32.5	32.2	31.9	31.6	31.2	30.8
48	32.7	32.5	32.3	32.1	31.8	31.6	31.3	31.0	30.7	30.3
49	32.0	31.8	31.6	31.4	31.2	30.9	30.7	30.4	30.1	29.8
50	31.3	31.1	30.9	30.7	30.5	30.3	30.0	29.8	29.5	29.2
51	30.5	30.4	30.2	30.0	29.8	29.6	29.4	29.2	28.9	28.6
52	29.7	29.6	29.5	29.3	29.1	28.9	28.7	28.5	28.3	28.0
53	29.0	28.9	28.7	28.6	28.4	28.2	28.1	27.9	27.6	27.4
54	28.2	28.1	28.0	27.8	27.7	27.5	27.4	27.2	27.0	26.8
55	27.4	27.3	27.2	27.1	27.0	26.8	26.7	26.5	26.3	26.1
56	26.7	26.6	26.5	26.3	26.2	26.1	26.0	25.8	25.6	25.4
57	25.9	25.8	25.7	25.6	25.5	25.4	25.2	25.1	24.9	24.8
58	25.1	25.0	24.9	24.8	24.7	24.6	24.5	24.4	24.2	24.1
59	24.3	24.2	24.1	24.1	24.0	23.9	23.8	23.6	23.5	23.4
60	23.5	23.4	23.4	23.3	23.2	23.1	23.0	22.9	22.8	22.7
61	22.7	22.6	22.6	22.5	22.4	22.4	22.3	22.2	22.1	22.0
62	21.9	21.9	21.8	21.7	21.7	21.6	21.5	21.4	21.3	21.2
63	21.1	21.1	21.0	21.0	20.9	20.8	20.8	20.7	20.6	20.5
64	20.3	20.3	20.2	20.2	20.1	20.1	20.0	20.0	19.9	19.8
65	19.6	19.5	19.5	19.4	19.4	19.3	19.3	19.2	19.1	19.1
66	18.8	18.8	18.7	18.7	18.6	18.6	18.5	18.5	18.4	18.4
67	18.0	18.0	18.0	17.9	17.9	17.9	17.8	17.8	17.7	17.6
68	17.3	17.3	17.2	17.2	17.2	17.1	17.1	17.0	17.0	16.9
69	16.5	16.5	16.5	16.5	16.4	16.4	16.4	16.3	16.3	16.2
70	15.8	15.8	15.8	15.7	15.7	15.7	15.6	15.6	15.6	15.5
71	15.1	15.1	15.1	15.0	15.0	15.0	15.0	14.9	14.9	14.9
72	14.4	14.4	14.4	14.3	14.3	14.3	14.3	14.2	14.2	14.2
73	13.7	13.7	13.7	13.7	13.7	13.6	13.6	13.6	13.6	13.5
74	13.1	13.0	13.0	13.0	13.0	13.0	13.0	12.9	12.9	12.9
75	12.4	12.4	12.4	12.4	12.3	12.3	12.3	12.3	12.3	12.2
76	11.8	11.8	11.7	11.7	11.7	11.7	11.7	11.7	11.6	11.6
77	11.1	11.1	11.1	11.1	11.1	11.1	11.1	11.1	11.0	11.0
78	10.5	10.5	10.5	10.5	10.5	10.5	10.5	10.5	10.5	10.4
79	10.0	10.0	9.9	9.9	9.9	9.9	9.9	9.9	9.9	9.9
80	9.4	9.4	9.4	9.4	9.4	9.4	9.4	9.3	9.3	9.3
81	8.9	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8
82	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3	8.3
83	7.8	7.8	7.8	7.8	7.8	7.8	7.8	7.8	7.8	7.8
84	7.3	7.3	7.3	7.3	7.3	7.3	7.3	7.3	7.3	7.3
85	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9
86	6.5	6.5	6.5	6.5	6.4	6.4	6.4	6.4	6.4	6.4
87	6.1	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
88	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.6	5.6	5.6
89	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
90	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
91	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.6	4.6
92	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	35	36	37	38	39	40	41	42	43	44
93	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
94	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9
95	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6
96	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4
97	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2
98	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
99	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
100	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.6	2.6
101	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
102	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
103	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.9	.8	.8	.8	.8
113	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
114	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	45	46	47	48	49	50	51	52	53	54
45	31.4	30.9	30.5	30.0	29.4	28.9	28.3	27.7	27.1	26.5
46	30.9	30.5	30.0	29.6	29.1	28.5	28.0	27.4	26.9	26.3
47	30.5	30.0	29.6	29.2	28.7	28.2	27.7	27.1	26.6	26.0
48	30.0	29.6	29.2	28.7	28.3	27.8	27.3	26.8	26.3	25.7
49	29.4	29.1	28.7	28.3	27.9	27.4	26.9	26.5	25.9	25.4
50	28.9	28.5	28.2	27.8	27.4	27.0	26.5	26.1	25.6	25.1
51	28.3	28.0	27.7	27.3	26.9	26.5	26.1	25.7	25.2	24.7
52	27.7	27.4	27.1	26.8	26.5	26.1	25.7	25.3	24.8	24.4
53	27.1	26.9	26.6	26.3	25.9	25.6	25.2	24.8	24.4	24.0
54	26.5	26.3	26.0	25.7	25.4	25.1	24.7	24.4	24.0	23.6
55	25.9	25.7	25.4	25.1	24.9	24.6	24.2	23.9	23.5	23.2
56	25.2	25.0	24.8	24.6	24.3	24.0	23.7	23.4	23.1	22.7
57	24.6	24.4	24.2	24.0	23.7	23.5	23.2	22.9	22.6	22.2
58	23.9	23.7	23.5	23.3	23.1	22.9	22.6	22.4	22.1	21.7
59	23.2	23.1	22.9	22.7	22.5	22.3	22.1	21.8	21.5	21.2
60	22.5	22.4	22.2	22.1	21.9	21.7	21.5	21.2	21.0	20.7
61	21.8	21.7	21.6	21.4	21.2	21.1	20.9	20.6	20.4	20.2
62	21.1	21.0	20.9	20.7	20.6	20.4	20.2	20.0	19.8	19.6
63	20.4	20.3	20.2	20.1	19.9	19.8	19.6	19.4	19.2	19.0
64	19.7	19.6	19.5	19.4	19.3	19.1	19.0	18.8	18.6	18.5
65	19.0	18.9	18.8	18.7	18.6	18.5	18.3	18.2	18.0	17.9
66	18.3	18.2	18.1	18.0	17.9	17.8	17.7	17.6	17.4	17.3
67	17.6	17.5	17.4	17.3	17.3	17.2	17.1	16.9	16.8	16.7
68	16.9	16.8	16.7	16.7	16.6	16.5	16.4	16.3	16.2	16.1
69	16.2	16.1	16.1	16.0	15.9	15.8	15.8	15.7	15.6	15.4
70	15.5	15.4	15.4	15.3	15.3	15.2	15.1	15.0	14.9	14.8
71	14.8	14.8	14.7	14.7	14.6	14.5	14.5	14.4	14.3	14.2
72	14.1	14.1	14.1	14.0	14.0	13.9	13.8	13.8	13.7	13.6
73	13.5	13.5	13.4	13.4	13.3	13.3	13.2	13.2	13.1	13.0
74	12.8	12.8	12.8	12.7	12.7	12.7	12.6	12.6	12.5	12.4
75	12.2	12.2	12.2	12.1	12.1	12.1	12.0	12.0	11.9	11.9
76	11.6	11.6	11.6	11.5	11.5	11.5	11.4	11.4	11.3	11.3
77	11.0	11.0	11.0	10.9	10.9	10.9	10.8	10.8	10.8	10.7
78	10.4	10.4	10.4	10.4	10.3	10.3	10.3	10.2	10.2	10.2
79	9.9	9.8	9.8	9.8	9.8	9.8	9.7	9.7	9.7	9.6
80	9.3	9.3	9.3	9.3	9.2	9.2	9.2	9.2	9.1	9.1
81	8.8	8.8	8.7	8.7	8.7	8.7	8.7	8.7	8.6	8.6
82	8.3	8.2	8.2	8.2	8.2	8.2	8.2	8.2	8.1	8.1
83	7.8	7.8	7.7	7.7	7.7	7.7	7.7	7.7	7.7	7.6
84	7.3	7.3	7.3	7.3	7.3	7.2	7.2	7.2	7.2	7.2
85	6.8	6.8	6.8	6.8	6.8	6.8	6.8	6.8	6.8	6.7
86	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.4	6.3	6.3
87	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	5.9
88	5.6	5.6	5.6	5.6	5.6	5.6	5.6	5.6	5.6	5.6
89	5.3	5.3	5.3	5.3	5.3	5.3	5.2	5.2	5.2	5.2
90	5.0	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9	4.9
91	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6	4.6
92	4.4	4.4	4.4	4.3	4.3	4.3	4.3	4.3	4.3	4.3
93	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
94	3.9	3.9	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8
95	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6
96	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4
97	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2
98	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
99	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
100	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
101	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
102	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	45	46	47	48	49	50	51	52	53	54
103	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8
113	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
114	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	55	56	57	58	59	60	61	62	63	64
55	22.7	22.3	21.9	21.4	20.9	20.4	19.9	19.4	18.8	18.3
56	22.3	21.9	21.5	21.1	20.6	20.1	19.6	19.1	18.6	18.0
57	21.9	21.5	21.1	20.7	20.3	19.8	19.3	18.8	18.3	17.8
58	21.4	21.1	20.7	20.3	19.9	19.5	19.0	18.5	18.0	17.5
59	20.9	20.6	20.3	19.9	19.5	19.1	18.7	18.2	17.7	17.3
60	20.4	20.1	19.8	19.5	19.1	18.7	18.3	17.9	17.4	17.0
61	19.9	19.6	19.3	19.0	18.7	18.3	17.9	17.5	17.1	16.7
62	19.4	19.1	18.8	18.5	18.2	17.9	17.5	17.1	16.8	16.3
63	18.8	18.6	18.3	18.0	17.7	17.4	17.1	16.8	16.4	16.0
64	18.3	18.0	17.8	17.5	17.3	17.0	16.7	16.3	16.0	15.6
65	17.7	17.5	17.3	17.0	16.8	16.5	16.2	15.9	15.6	15.3
66	17.1	16.9	16.7	16.5	16.3	16.0	15.8	15.5	15.2	14.9
67	16.5	16.3	16.2	16.0	15.8	15.5	15.3	15.0	14.7	14.5
68	15.9	15.8	15.6	15.4	15.2	15.0	14.8	14.6	14.3	14.0
69	15.3	15.2	15.0	14.9	14.7	14.5	14.3	14.1	13.9	13.6
70	14.7	14.6	14.5	14.3	14.2	14.0	13.8	13.6	13.4	13.2
71	14.1	14.0	13.9	13.8	13.6	13.5	13.3	13.1	12.9	12.7
72	13.5	13.4	13.3	13.2	13.1	12.9	12.8	12.6	12.4	12.3
73	13.0	12.9	12.8	12.7	12.5	12.4	12.3	12.1	12.0	11.8
74	12.4	12.3	12.2	12.1	12.0	11.9	11.8	11.6	11.5	11.3
75	11.8	11.7	11.7	11.6	11.5	11.4	11.3	11.1	11.0	10.9
76	11.2	11.2	11.1	11.0	10.9	10.9	10.8	10.6	10.5	10.4
77	10.7	10.6	10.6	10.5	10.4	10.3	10.3	10.2	10.0	9.9
78	10.1	10.1	10.0	10.0	9.9	9.8	9.8	9.7	9.6	9.5
79	9.6	9.6	9.5	9.5	9.4	9.3	9.3	9.2	9.1	9.0
80	9.1	9.0	9.0	9.0	8.9	8.9	8.8	8.7	8.7	8.6
81	8.6	8.5	8.5	8.5	8.4	8.4	8.3	8.3	8.2	8.1
82	8.1	8.1	8.0	8.0	8.0	7.9	7.9	7.8	7.8	7.7
83	7.6	7.6	7.6	7.5	7.5	7.5	7.4	7.4	7.3	7.3
84	7.2	7.1	7.1	7.1	7.1	7.0	7.0	7.0	6.9	6.9
85	6.7	6.7	6.7	6.7	6.6	6.6	6.6	6.5	6.5	6.5
86	6.3	6.3	6.3	6.3	6.2	6.2	6.2	6.2	6.1	6.1
87	5.9	5.9	5.9	5.9	5.9	5.8	5.8	5.8	5.8	5.7
88	5.6	5.5	5.5	5.5	5.5	5.5	5.5	5.4	5.4	5.4
89	5.2	5.2	5.2	5.2	5.2	5.1	5.1	5.1	5.1	5.1
90	4.9	4.9	4.9	4.9	4.9	4.8	4.8	4.8	4.8	4.8
91	4.6	4.6	4.6	4.6	4.6	4.5	4.5	4.5	4.5	4.5
92	4.3	4.3	4.3	4.3	4.3	4.3	4.3	4.2	4.2	4.2
93	4.1	4.1	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
94	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.8	3.7
95	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.6	3.5	3.5
96	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.3	3.3	3.3
97	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.1	3.1
98	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
99	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
100	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6	2.6
101	2.5	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4
102	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.2
103	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.8	1.8	1.8	1.8	1.8	1.8	1.7	1.7	1.7	1.7
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	55	56	57	58	59	60	61	62	63	64
113	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
114	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	65	66	67	68	69	70	71	72	73	74
65	14.9	14.5	14.1	13.7	13.3	12.9	12.5	12.0	11.6	11.2
66	14.5	14.2	13.8	13.4	13.1	12.6	12.2	11.8	11.4	11.0
67	14.1	13.8	13.5	13.1	12.8	12.4	12.0	11.6	11.2	10.8
68	13.7	13.4	13.1	12.8	12.5	12.1	11.7	11.4	11.0	10.6
69	13.3	13.1	12.8	12.5	12.1	11.8	11.4	11.1	10.7	10.4
70	12.9	12.6	12.4	12.1	11.8	11.5	11.2	10.8	10.5	10.1
71	12.5	12.2	12.0	11.7	11.4	11.2	10.9	10.5	10.2	9.9
72	12.0	11.8	11.6	11.4	11.1	10.8	10.5	10.2	9.9	9.6
73	11.6	11.4	11.2	11.0	10.7	10.5	10.2	9.9	9.7	9.4
74	11.2	11.0	10.8	10.6	10.4	10.1	9.9	9.6	9.4	9.1
75	10.7	10.5	10.4	10.2	10.0	9.8	9.5	9.3	9.1	8.8
76	10.3	10.1	9.9	9.8	9.6	9.4	9.2	9.0	8.8	8.5
77	9.8	9.7	9.5	9.4	9.2	9.0	8.8	8.6	8.4	8.2
78	9.4	9.2	9.1	9.0	8.8	8.7	8.5	8.3	8.1	7.9
79	8.9	8.8	8.7	8.6	8.4	8.3	8.1	8.0	7.8	7.6
80	8.5	8.4	8.3	8.2	8.0	7.9	7.8	7.6	7.5	7.3
81	8.0	8.0	7.9	7.8	7.7	7.5	7.4	7.3	7.1	7.0
82	7.6	7.5	7.5	7.4	7.3	7.2	7.1	6.9	6.8	6.7
83	7.2	7.1	7.1	7.0	6.9	6.8	6.7	6.6	6.5	6.4
84	6.8	6.7	6.7	6.6	6.5	6.4	6.4	6.3	6.2	6.0
85	6.4	6.4	6.3	6.2	6.2	6.1	6.0	5.9	5.8	5.7
86	6.0	6.0	5.9	5.9	5.8	5.8	5.7	5.6	5.5	5.4
87	5.7	5.6	5.6	5.6	5.5	5.4	5.4	5.3	5.2	5.2
88	5.3	5.3	5.3	5.2	5.2	5.1	5.1	5.0	5.0	4.9
89	5.0	5.0	5.0	4.9	4.9	4.8	4.8	4.7	4.7	4.6
90	4.7	4.7	4.7	4.6	4.6	4.6	4.5	4.5	4.4	4.4
91	4.5	4.4	4.4	4.4	4.3	4.3	4.3	4.2	4.2	4.1
92	4.2	4.2	4.1	4.1	4.1	4.1	4.0	4.0	3.9	3.9
93	3.9	3.9	3.9	3.9	3.9	3.8	3.8	3.8	3.7	3.7
94	3.7	3.7	3.7	3.7	3.6	3.6	3.6	3.6	3.5	3.5
95	3.5	3.5	3.5	3.5	3.4	3.4	3.4	3.4	3.3	3.3
96	3.3	3.3	3.3	3.3	3.3	3.2	3.2	3.2	3.2	3.1
97	3.1	3.1	3.1	3.1	3.1	3.1	3.0	3.0	3.0	3.0
98	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.8	2.8
99	2.8	2.8	2.8	2.7	2.7	2.7	2.7	2.7	2.7	2.6
100	2.6	2.6	2.6	2.6	2.6	2.5	2.5	2.5	2.5	2.5
101	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.3	2.3
102	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2
103	2.1	2.1	2.1	2.1	2.1	2.0	2.0	2.0	2.0	2.0
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.7	1.7	1.7	1.7	1.7	1.7	1.7	1.7	1.7	1.7
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.5	1.5
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8
113	.7	.7	.7	.7	.7	.6	.6	.6	.6	.6
114	.6	.6	.6	.6	.6	.6	.5	.5	.5	.5
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	75	76	77	78	79	80	81	82	83	84
75	8.6	8.3	8.0	7.7	7.4	7.1	6.8	6.5	6.2	5.9
76	8.3	8.0	7.8	7.5	7.2	6.9	6.7	6.4	6.1	5.8
77	8.0	7.8	7.5	7.3	7.0	6.8	6.5	6.2	5.9	5.7
78	7.7	7.5	7.3	7.0	6.8	6.6	6.3	6.0	5.8	5.5
79	7.4	7.2	7.0	6.8	6.6	6.3	6.1	5.9	5.6	5.4
80	7.1	6.9	6.8	6.6	6.3	6.1	5.9	5.7	5.5	5.2
81	6.8	6.7	6.5	6.3	6.1	5.9	5.7	5.5	5.3	5.1
82	6.5	6.4	6.2	6.0	5.9	5.7	5.5	5.3	5.1	4.9
83	6.2	6.1	5.9	5.8	5.6	5.5	5.3	5.1	4.9	4.7
84	5.9	5.8	5.7	5.5	5.4	5.2	5.1	4.9	4.7	4.6
85	5.6	5.5	5.4	5.3	5.2	5.0	4.9	4.7	4.6	4.4
86	5.4	5.3	5.1	5.0	4.9	4.8	4.7	4.5	4.4	4.2
87	5.1	5.0	4.9	4.8	4.7	4.6	4.4	4.3	4.2	4.1
88	4.8	4.7	4.6	4.5	4.4	4.3	4.2	4.1	4.0	3.9
89	4.5	4.5	4.4	4.3	4.2	4.1	4.0	3.9	3.8	3.7
90	4.3	4.2	4.2	4.1	4.0	3.9	3.8	3.8	3.7	3.5
91	4.1	4.0	4.0	3.9	3.8	3.7	3.7	3.6	3.5	3.4
92	3.9	3.8	3.7	3.7	3.6	3.6	3.5	3.4	3.3	3.2
93	3.7	3.6	3.6	3.5	3.4	3.4	3.3	3.2	3.2	3.1
94	3.5	3.4	3.4	3.3	3.3	3.2	3.2	3.1	3.0	3.0
95	3.3	3.2	3.2	3.2	3.1	3.1	3.0	3.0	2.9	2.8
96	3.1	3.1	3.0	3.0	3.0	2.9	2.9	2.8	2.8	2.7
97	2.9	2.9	2.9	2.9	2.8	2.8	2.7	2.7	2.6	2.6
98	2.8	2.8	2.7	2.7	2.7	2.6	2.6	2.6	2.5	2.5
99	2.6	2.6	2.6	2.6	2.5	2.5	2.5	2.4	2.4	2.3
100	2.5	2.5	2.4	2.4	2.4	2.4	2.3	2.3	2.3	2.2
101	2.3	2.3	2.3	2.3	2.2	2.2	2.2	2.2	2.1	2.1
102	2.2	2.1	2.1	2.1	2.1	2.1	2.0	2.0	2.0	2.0
103	2.0	2.0	2.0	2.0	1.9	1.9	1.9	1.9	1.9	1.8
104	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.7	1.7	1.7
105	1.7	1.7	1.7	1.7	1.6	1.6	1.6	1.6	1.6	1.6
106	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.4
107	1.4	1.4	1.4	1.4	1.4	1.4	1.3	1.3	1.3	1.3
108	1.3	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.8	.8
112	.8	.8	.8	.7	.7	.7	.7	.7	.7	.7
113	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
114	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	85	86	87	88	89	90	91	92	93	94
85	4.2	4.1	3.9	3.8	3.6	3.4	3.3	3.2	3.0	2.9
86	4.1	3.9	3.8	3.6	3.5	3.3	3.2	3.1	2.9	2.8
87	3.9	3.8	3.6	3.5	3.4	3.2	3.1	3.0	2.8	2.7
88	3.8	3.6	3.5	3.4	3.2	3.1	3.0	2.9	2.8	2.6
89	3.6	3.5	3.4	3.2	3.1	3.0	2.9	2.8	2.7	2.6
90	3.4	3.3	3.2	3.1	3.0	2.9	2.8	2.7	2.6	2.5
91	3.3	3.2	3.1	3.0	2.9	2.8	2.7	2.6	2.5	2.4
92	3.2	3.1	3.0	2.9	2.8	2.7	2.6	2.5	2.4	2.3
93	3.0	2.9	2.8	2.8	2.7	2.6	2.5	2.4	2.3	2.3
94	2.9	2.8	2.7	2.6	2.6	2.5	2.4	2.3	2.3	2.2
95	2.8	2.7	2.6	2.5	2.5	2,4	2.3	2.2	2.2	2.1
96	2.6	2.6	2.5	2.4	2.4	2.3	2.2	2.2	2.1	2.0
97	2.5	2.5	2.4	2.3	2.3	2.2	2.2	2.1	2.0	2.0
98	2.4	2.4	2.3	2.2	2.2	2.1	2.1	2.0	2.0	1.9
99	2.3	2.2	2.2	2.1	2.1	2.0	2.0	1.9	1.9	1.8
100	2.2	2.1	2.1	2.0	2.0	1.9	1.9	1.9	1.8	1.8
101	2.1	2.0	2.0	1.9	1.9	1.9	1.8	1.8	1.7	1.7
102	1.9	1.9	1.9	1.8	1.8	1.8	1.7	1.7	1.6	1.6
103	1.8	1.8	1.8	1.7	1.7	1.7	1.6	1.6	1.5	1.5
104	1.7	1.7	1.6	1.6	1.6	1.5	1.5	1.5	1.5	1.4
105	1.6	1.5	1.5	1.5	1.5	1.4	1.4	1.4	1.4	1.3
106	1.4	1.4	1.4	1.4	1.4	1.3	1.3	1.3	1.3	1.2
107	1.3	1.3	1.3	1.3	1.2	1.2	1.2	1.2	1.2	1.2
108	1.2	1.2	1.2	1.1	1.1	1.1	1.1	1.1	1.1	1.1
109	1.1	1.1	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
110	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
111	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8
112	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
113	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
114	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	95	96	97	98	99	100	101	102	103	104
95	2.0	2.0	1.9	1.8	1.8	1.7	1.6	1.6	1.5	1.4
96	2.0	1.9	1.9	1.8	1.7	1.7	1.6	1.5	1.5	1.4
97	1.9	1.9	1.8	1.7	1.7	1.6	1.6	1.5	1.4	1.3
98	1.8	1.8	1.7	1.7	1.6	1.6	1.5	1.5	1.4	1.3
99	1.8	1.7	1.7	1.6	1.6	1.5	1.5	1.4	1.4	1.3
100	1.7	1.7	1.6	1.6	1.5	1.5	1.4	1.4	1.3	1.3
101	1.6	1.6	1.6	1.5	1.5	1.4	1.4	1.3	1.3	1.2
102	1.6	1.5	1.5	1.5	1.4	1.4	1.3	1.3	1.2	1.2
103	1.5	1.5	1.4	1.4	1.4	1.3	1.3	1.2	1.2	1.1
104	1.4	1.4	1.3	1.3	1.3	1.3	1.2	1.2	1.1	1.1
105	1.3	1.3	1.3	1.2	1.2	1.2	1.2	1.1	1.1	1.0
106	1.2	1.2	1.2	1.2	1.1	1.1	1.1	1.1	1.0	1.0
107	1.1	1.1	1.1	1.1	1.1	1.0	1.0	1.0	1.0	.9
108	1.0	1.0	1.0	1.0	1.0	1.0	1.0	.9	.9	.9
109	1.0	.9	.9	.9	.9	.9	.9	.9	.8	.8
110	.9	.9	.8	.8	.8	.8	.8	.8	.8	.8
111	.8	.8	.8	.8	.8	.7	.7	.7	.7	.7
112	.7	.7	.7	.7	.7	.7	.7	.7	.6	.6
113	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
114	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIA - ANNUITIES FOR JOINT LIFE ONLY
TWO LIVES - EXPECTED RETURN MULTIPLES

AGES	105	106	107	108	109	110	111	112	113	114	115
105	1.0	1.0	.9	.9	.8	.7	.7	.6	.6	.5	.5
106	1.0	.9	.9	.8	.8	.7	.7	.6	.6	.5	.5
107	.9	.9	.8	.8	.7	.7	.7	.6	.6	.5	.5
108	.9	.8	.8	.8	.7	.7	.6	.6	.5	.5	.5
109	.8	.8	.7	.7	.7	.7	.6	.6	.5	.5	.5
110	.7	.7	.7	.7	.7	.6	.6	.6	.5	.5	.5
111	.7	.7	.7	.6	.6	.6	.6	.5	.5	.5	.5
112	.6	.6	.6	.6	.6	.6	.5	.5	.5	.5	.5
113	.6	.6	.6	.5	.5	.5	.5	.5	.5	.5	.5
114	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VII - PERCENT VALUE OF REFUND FEATURE DURATION OF GUARANTEED AMOUNT

AGE	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS	6 YEARS	7 YEARS	8 YEARS	9 YEARS	10 YEARS
5	0	0	0	0	0	0	0	0	0	0
6	0	0	0	0	0	0	0	0	0	0
7	0	0	0	0	0	0	0	0	0	0
8	0	0	0	0	0	0	0	0	0	0
9	0	0	0	0	0	0	0	0	0	0
10	0	0	0	0	0	0	0	0	0	0
11	0	0	0	0	0	0	0	0	0	0
12	0	0	0	0	0	0	0	0	0	0
13	0	0	0	0	0	0	0	0	0	0
14	0	0	0	0	0	0	0	0	0	0
15	0	0	0	0	0	0	0	0	0	0
16	0	0	0	0	0	0	0	0	0	0
17	0	0	0	0	0	0	0	0	0	0
18	0	0	0	0	0	0	0	0	0	0
19	0	0	0	0	0	0	0	0	0	0
20	0	0	0	0	0	0	0	0	0	0
21	0	0	0	0	0	0	0	0	0	0
22	0	0	0	0	0	0	0	0	0	0
23	0	0	0	0	0	0	0	0	0	0
24	0	0	0	0	0	0	0	0	0	0
25	0	0	0	0	0	0	0	0	0	0
26	0	0	0	0	0	0	0	0	0	0
27	0	0	0	0	0	0	0	0	0	0
28	0	0	0	0	0	0	0	0	0	0
29	0	0	0	0	0	0	0	0	0	0
30	0	0	0	0	0	0	0	0	0	0
31	0	0	0	0	0	0	0	0	0	0
32	0	0	0	0	0	0	0	0	0	0
33	0	0	0	0	0	0	0	0	0	0
34	0	0	0	0	0	0	0	0	0	0
35	0	0	0	0	0	0	0	0	0	0
36	0	0	0	0	0	0	0	0	0	0
37	0	0	0	0	0	0	0	0	0	1
38	0	0	0	0	0	0	0	0	0	1
39	0	0	0	0	0	0	0	0	1	1
40	0	0	0	0	0	0	0	1	1	1
41	0	0	0	0	0	0	0	1	1	1
42	0	0	0	0	0	0	1	1	1	1
43	0	0	0	0	0	0	1	1	1	1
44	0	0	0	0	0	1	1	1	1	1
45	0	0	0	0	0	1	1	1	1	1
46	0	0	0	0	1	1	1	1	1	1
47	0	0	0	0	1	1	1	1	1	1
48	0	0	0	0	1	1	1	1	1	1
49	0	0	0	1	1	1	1	1	1	2
50	0	0	0	1	1	1	1	1	1	2
51	0	0	0	1	1	1	1	1	2	2
52	0	0	0	1	1	1	1	1	2	2
53	0	0	1	1	1	1	1	2	2	2
54	0	0	1	1	1	1	1	2	2	2
55	0	0	1	1	1	1	2	2	2	2
56	0	0	1	1	1	1	2	2	2	3
57	0	0	1	1	1	2	2	2	3	3
58	0	1	1	1	1	2	2	2	3	3
59	0	1	1	1	1	2	2	3	3	4
60	0	1	1	1	2	2	2	3	3	4

TABLE VII - PERCENT VALUE OF REFUND FEATURE
DURATION OF GUARANTEED AMOUNT

AGE	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS	6 YEARS	7 YEARS	8 YEARS	9 YEARS	10 YEARS
61	0	1	1	1	2	2	3	3	4	4
62	0	1	1	2	2	2	3	4	4	5
63	0	1	1	2	2	3	3	4	5	5
64	0	1	1	2	2	3	4	4	5	6
65	0	1	2	2	3	3	4	5	6	6
66	1	1	2	2	3	4	5	5	6	7
67	1	1	2	3	3	4	5	6	7	8
68	1	1	2	3	4	5	6	7	8	9
69	1	1	2	3	4	5	6	7	8	10
70	1	2	3	4	5	6	7	8	9	11
71	1	2	3	4	5	6	8	9	10	12
72	1	2	3	4	6	7	8	10	11	13
73	1	2	4	5	6	8	9	11	13	14
74	1	3	4	5	7	9	10	12	14	16
75	1	3	4	6	8	9	11	13	15	17
76	2	3	5	7	9	10	12	15	17	19
77	2	4	5	7	9	12	14	16	18	21
78	2	4	6	8	10	13	15	18	20	23
79	2	4	7	9	11	14	17	19	22	25
80	2	5	7	10	13	15	18	21	24	27
81	3	5	8	11	14	17	20	23	26	29
82	3	6	9	12	15	19	22	25	28	32
83	3	7	10	13	17	20	24	27	31	34
84	4	7	11	15	19	22	26	30	33	37
85	4	8	12	16	20	24	28	32	36	40
86	4	9	13	18	22	27	31	35	39	42
87	5	10	15	20	24	29	33	37	41	45
88	5	11	16	21	26	31	36	40	44	48
89	6	12	18	23	28	33	38	43	47	50
90	7	13	19	25	31	36	41	45	49	53
91	7	14	21	27	33	38	43	48	52	55
92	8	15	22	29	35	40	45	50	54	58
93	9	17	24	31	37	43	48	52	56	60
94	9	18	26	33	39	45	50	54	58	62
95	10	19	27	35	41	47	52	57	60	64
96	11	20	29	36	43	49	54	59	62	66
97	11	21	30	38	45	51	56	61	64	68
98	12	23	32	40	47	53	58	63	66	69
99	13	24	34	42	49	55	60	65	68	71
100	14	26	36	44	52	58	63	67	70	73
101	14	27	38	47	54	60	65	69	72	75
102	15	29	40	49	56	62	67	71	74	77
103	17	31	42	52	59	65	69	73	76	78
104	18	33	45	55	62	67	72	75	78	80
105	19	36	48	58	65	70	74	77	80	82
106	21	38	51	61	68	73	77	79	82	84
107	23	42	55	64	71	75	79	81	84	85
108	25	45	58	67	73	78	81	83	85	87
109	28	49	62	71	76	80	83	85	87	88
110	31	52	66	74	79	82	85	87	88	89
111	34	57	70	77	82	85	87	88	90	91
112	37	61	73	80	84	87	88	90	91	92
113	41	66	77	83	86	88	90	91	92	93
114	45	70	80	85	88	90	92	93	93	94
115	50	75	83	88	90	92	93	94	94	95

TABLE VII - PERCENT VALUE OF REFUND FEATURE DURATION OF GUARANTEED AMOUNT

AGE	11 YEARS	12 YEARS	13 YEARS	14 YEARS	15 YEARS	16 YEARS	17 YEARS	18 YEARS	19 YEARS	20 YEARS
5	0	0	0	0	0	0	0	0	0	0
6	0	0	0	0	0	0	0	0	0	0
7	0	0	0	0	0	0	0	0	0	0
8	0	0	0	0	0	0	0	0	0	0
9	0	0	0	0	0	0	0	0	0	0
10	0	0	0	0	0	0	0	0	0	0
11	0	0	0	0	0	0	0	0	0	0
12	0	0	0	0	0	0	0	0	0	0
13	0	0	0	0	0	0	0	0	0	0
14	0	0	0	0	0	0	0	0	0	0
15	0	0	0	0	0	0	0	0	0	0
16	0	0	0	0	0	0	0	0	0	0
17	0	0	0	0	0	0	0	0	0	0
18	0	0	0	0	0	0	0	0	0	0
19	0	0	0	0	0	0	0	0	0	0
20	0	0	0	0	0	0	0	0	0	1
21	0	0	0	0	0	0	0	0	0	1
22	0	0	0	0	0	0	0	0	1	1
23	0	0	0	0	0	0	0	1	1	1
24	0	0	0	0	0	0	0	1	1	1
25	0	0	0	0	0	0	1	1	1	1
26	0	0	0	0	0	0	1	1	1	1
27	0	0	0	0	0	1	1	1	1	1
28	0	0	0	0	1	1	1	1	1	1
29	0	0	0	0	1	1	1	1	1	1
30	0	0	0	1	1	1	1	1	1	1
31	0	0	0	1	1	1	1	1	1	1
32	0	0	1	1	1	1	1	1	1	1
33	0	0	1	1	1	1	1	1	1	1
34	0	1	1	1	1	1	1	1	1	1
35	0	1	1	1	1	1	1	1	1	1
36	1	1	1	1	1	1	1	1	1	1
37	1	1	1	1	1	1	1	1	1	1
38	1	1	1	1	1	1	1	1	1	2
39	1	1	1	1	1	1	1	1	2	2
40	1	1	1	1	1	1	1	2	2	2
41	1	1	1	1	1	1	2	2	2	2
42	1	1	1	1	1	2	2	2	2	2
43	1	1	1	1	2	2	2	2	2	3
44	1	1	1	2	2	2	2	2	3	3
45	1	1	2	2	2	2	2	3	3	3
46	1	2	2	2	2	2	3	3	3	3
47	1	2	2	2	2	2	3	3	3	4
48	2	2	2	2	2	3	3	3	4	4
49	2	2	2	2	3	3	3	4	4	4
50	2	2	2	3	3	3	3	4	4	5
51	2	2	3	3	3	3	4	4	5	5
52	2	2	3	3	3	4	4	5	5	5
53	2	3	3	3	4	4	5	5	5	6
54	3	3	3	4	4	4	5	5	6	7
55	3	3	4	4	4	5	5	6	7	7
56	3	3	4	4	5	5	6	7	7	8
57	3	4	4	5	5	6	6	7	8	9
58	4	4	5	5	6	6	7	8	9	9
59	4	5	5	6	6	7	8	9	9	10
60	4	5	6	6	7	8	9	10	10	11

TABLE VII - PERCENT VALUE OF REFUND FEATURE
DURATION OF GUARANTEED AMOUNT

AGE	11 YEARS	12 YEARS	13 YEARS	14 YEARS	15 YEARS	16 YEARS	17 YEARS	18 YEARS	19 YEARS	20 YEARS
61	5	6	6	7	8	9	10	10	11	13
62	5	6	7	8	9	10	11	12	13	14
63	6	7	8	9	10	11	12	13	14	15
64	7	8	8	9	10	12	13	14	15	17
65	7	8	9	10	12	13	14	15	17	18
66	8	9	10	12	13	14	15	17	18	20
67	9	10	11	13	14	15	17	18	20	22
68	10	11	13	14	15	17	19	20	22	24
69	11	12	14	15	17	19	20	22	24	26
70	12	14	15	17	19	20	22	24	26	28
71	13	15	17	18	20	22	24	26	28	30
72	15	17	18	20	22	24	26	28	30	32
73	16	18	20	22	24	26	28	31	33	35
74	18	20	22	24	26	28	31	33	35	37
75	19	22	24	26	28	31	33	35	38	40
76	21	24	26	28	31	33	36	38	40	43
77	23	26	28	31	33	36	38	41	43	45
78	25	28	31	33	36	38	41	43	46	48
79	28	30	33	36	38	41	44	46	48	51
80	30	33	36	38	41	44	46	49	51	53
81	32	35	38	41	44	47	49	51	54	56
82	35	38	41	44	47	49	52	54	56	58
83	38	41	44	47	49	52	54	57	59	61
84	40	44	47	49	52	55	57	59	61	63
85	43	46	49	52	55	57	59	62	63	65
86	46	49	52	55	57	60	62	64	66	67
87	48	52	55	57	60	62	64	66	68	69
88	51	54	57	60	62	64	66	68	70	71
89	54	57	60	62	65	67	68	70	72	73
90	56	59	62	64	67	69	70	72	74	75
91	59	62	64	67	69	71	72	74	75	76
92	61	64	66	69	71	72	74	75	77	78
93	63	66	68	70	72	74	75	77	78	79
94	65	68	70	72	74	75	77	78	79	80
95	67	69	72	74	75	77	78	79	81	82
96	69	71	73	75	77	78	80	81	82	83
97	70	73	75	77	78	80	81	82	83	84
98	72	74	76	78	79	81	82	83	84	85
99	74	76	78	79	81	82	83	84	85	86
100	75	78	79	81	82	83	84	65	86	86
101	77	79	81	82	83	84	85	86	87	87
102	79	81	82	83	84	85	86	87	88	88
103	80	82	83	85	86	87	87	88	89	89
104	82	84	85	86	87	88	88	89	90	90
105	84	85	86	87	88	89	89	90	90	91
106	85	86	87	88	89	90	90	91	91	92
107	87	88	89	89	90	91	91	92	92	93
108	88	89	90	90	91	92	92	93	93	93
109	89	90	91	92	92	93	93	93	94	94
110	90	91	92	92	93	93	94	94	94	95
111	92	92	93	93	94	94	95	95	95	95
112	93	93	94	94	95	95	95	96	96	96
113	94	94	95	95	95	96	96	96	96	97
114	95	95	95	96	96	96	97	97	97	97
115	95	96	96	96	97	97	97	97	97	98

TABLE VII - PERCENT VALUE OF REFUND FEATURE
DURATION OF GUARANTEED AMOUNT

AGE	21 YEARS	22 YEARS	23 YEARS	24 YEARS	25 YEARS	26 YEARS	27 YEARS	28 YEARS	29 YEARS	30 YEARS
5	0	0	0	0	0	0	0	0	0	0
6	0	0	0	0	0	0	0	0	0	0
7	0	0	0	0	0	0	0	0	0	0
8	0	0	0	0	0	0	0	0	0	1
9	0	0	0	0	0	0	0	0	1	1
10	0	0	0	0	0	0	0	1	1	1
11	0	0	0	0	0	0	1	1	1	1
12	0	0	0	0	0	0	1	1	1	1
13	0	0	0	0	0	1	1	1	1	1
14	0	0	0	0	1	1	1	1	1	1
15	0	0	0	1	1	1	1	1	1	1
16	0	0	1	1	1	1	1	1	1	1
17	0	0	1	1	1	1	1	1	1	1
18	0	1	1	1	1	1	1	1	1	1
19	1	1	1	1	1	1	1	1	1	1
20	1	1	1	1	1	1	1	1	1	1
21	1	1	1	1	1	1	1	1	1	1
22	1	1	1	1	1	1	1	1	1	1
23	1	1	1	1	1	1	1	1	1	1
24	1	1	1	1	1	1	1	1	1	1
25	1	1	1	1	1	1	1	1	1	1
26	1	1	1	1	1	1	1	1	1	1
27	1	1	1	1	1	1	1	1	1	1
28	1	1	1	1	1	1	1	1	1	2
29	1	1	1	1	1	1	1	1	2	2
30	1	1	1	1	1	1	1	2	2	2
31	1	1	1	1	1	1	2	2	2	2
32	1	1	1	1	1	2	2	2	2	2
33	1	1	1	1	2	2	2	2	2	2
34	1	1	1	2	2	2	2	2	2	2
35	1	1	2	2	2	2	2	2	2	3
36	1	2	2	2	2	2	2	2	3	3
37	2	2	2	2	2	2	2	3	3	3
38	2	2	2	2	2	2	3	3	3	3
39	2	2	2	2	2	3	3	3	3	4
40	2	2	2	2	3	3	3	3	4	4
41	2	2	3	3	3	3	3	4	4	4
42	2	3	3	3	3	3	4	4	4	5
43	3	3	3	3	3	4	4	4	5	5
44	3	3	3	4	4	4	4	5	5	6
45	3	3	4	4	4	4	5	5	6	6
46	3	4	4	4	5	5	5	6	6	7
47	4	4	4	5	5	5	6	6	7	7
48	4	4	5	5	5	6	6	7	7	8
49	4	5	5	5	6	6	7	7	8	9
50	5	5	5	6	6	7	8	8	9	10
51	5	5	6	6	7	8	8	9	10	10
52	5	6	6	7	8	8	9	10	11	11
53	6	7	7	8	8	9	10	11	11	12
54	7	7	8	8	9	10	11	12	13	14
55	7	8	8	9	10	11	12	13	14	15
56	8	9	9	10	11	12	13	14	15	16
57	9	9	10	11	12	13	14	15	16	18
58	9	10	11	12	13	14	15	17	18	19
59	10	11	12	13	14	16	17	18	19	21
60	11	12	13	15	16	17	18	20	21	22

TABLE VII - PERCENT VALUE OF REFUND FEATURE
DURATION OF GUARANTEED AMOUNT

AGE	21 YEARS	22 YEARS	23 YEARS	24 YEARS	25 YEARS	26 YEARS	27 YEARS	28 YEARS	29 YEARS	30 YEARS
61	14	15	16	17	19	20	22	23	25	26
62	15	16	18	19	20	22	23	25	27	28
63	16	18	19	21	22	24	25	27	29	30
64	18	19	21	23	24	26	28	29	31	33
65	20	21	23	25	26	28	30	31	33	35
66	21	23	25	27	28	30	32	34	35	37
67	23	25	27	29	31	32	34	36	38	40
68	25	27	29	31	33	35	37	38	40	42
69	28	29	31	33	35	37	39	41	43	44
70	30	32	34	36	38	40	42	43	45	47
71	32	34	36	38	40	42	44	46	47	49
72	35	37	39	41	43	45	46	48	50	51
73	37	39	41	43	45	47	49	51	52	54
74	40	42	44	46	48	50	51	53	54	56
75	42	44	46	48	50	52	54	55	57	58
76	45	47	49	51	53	54	56	58	59	60
77	47	50	51	53	55	57	58	60	61	62
78	50	52	54	56	57	59	61	62	63	64
79	53	55	56	58	60	61	63	64	65	66
80	55	57	59	60	62	63	65	66	67	68
81	58	59	61	63	64	66	67	68	69	70
82	60	62	63	65	66	68	69	70	71	72
83	62	64	66	67	68	70	71	72	73	74
84	65	66	68	69	70	71	72	73	74	75
85	67	68	70	71	72	73	74	75	76	77
86	69	70	72	73	74	75	76	77	77	78
87	71	72	73	75	76	76	77	78	79	80
88	73	74	75	76	77	78	79	80	80	81
89	74	76	77	78	79	79	80	81	81	82
90	76	77	78	79	80	81	81	82	83	83
91	78	79	79	80	81	82	83	83	84	84
92	79	80	81	82	82	83	84	84	85	85
93	80	81	82	83	83	84	85	85	86	86
94	81	82	83	84	84	85	85	86	86	87
95	82	83	84	85	85	86	86	87	87	88
96	83	84	85	86	86	87	87	88	88	88
97	84	85	86	86	87	87	88	88	89	89
98	85	86	87	87	88	88	89	89	89	90
99	86	87	87	88	88	89	89	90	90	90
100	87	88	88	89	89	90	90	90	91	91
101	88	89	89	90	90	90	91	91	91	92
102	89	89	90	90	91	91	91	92	92	92
103	90	90	91	91	91	92	92	92	93	93
104	91	91	91	92	92	92	93	93	93	93
105	91	92	92	92	93	93	93	94	94	94
106	92	93	93	93	93	94	94	94	94	95
107	93	93	94	94	94	94	95	95	95	95
108	94	94	94	94	95	95	95	95	95	96
109	94	95	95	95	95	95	96	96	96	96
110	95	95	95	96	96	96	96	96	96	96
111	96	96	96	96	96	96	97	97	97	97
112	96	96	96	97	97	97	97	97	97	97
113	97	97	97	97	97	97	97	98	98	98
114	97	97	97	98	98	98	98	98	98	98
115	98	98	98	98	98	98	98	98	98	98

TABLE VII - PERCENT VALUE OF REFUND FEATURE
DURATION OF GUARANTEED AMOUNT

AGE	31 YEARS	32 YEARS	33 YEARS	34 YEARS	35 YEARS	36 YEARS	37 YEARS	38 YEARS	39 YEARS	40 YEARS
5	0	1	1	1	1	1	1	1	1	1
6	0	1	1	1	1	1	1	1	1	1
7	1	1	1	1	1	1	1	1	1	1
8	1	1	1	1	1	1	1	1	1	1
9	1	1	1	1	1	1	1	1	1	1
10	1	1	1	1	1	1	1	1	1	1
11	1	1	1	1	1	1	1	1	1	1
12	1	1	1	1	1	1	1	1	1	1
13	1	1	1	1	1	1	1	1	1	1
14	1	1	1	1	1	1	1	1	1	1
15	1	1	1	1	1	1	1	1	1	1
16	1	1	1	1	1	1	1	1	1	1
17	1	1	1	1	1	1	1	1	1	1
18	1	1	1	1	1	1	1	1	1	2
19	1	1	1	1	1	1	1	1	2	2
20	1	1	1	1	1	1	1	2	2	2
21	1	1	1	1	1	1	2	2	2	2
22	1	1	1	1	1	2	2	2	2	2
23	1	1	1	2	2	2	2	2	2	2
24	1	1	2	2	2	2	2	2	2	2
25	1	2	2	2	2	2	2	2	2	3
26	2	2	2	2	2	2	2	2	3	3
27	2	2	2	2	2	2	2	3	3	3
28	2	2	2	2	2	2	3	3	3	3
29	2	2	2	2	2	3	3	3	3	4
30	2	2	2	3	3	3	3	3	4	4
31	2	2	3	3	3	3	3	4	4	4
32	2	3	3	3	3	3	4	4	4	5
33	3	3	3	3	3	4	4	4	5	5
34	3	3	3	3	4	4	4	5	5	5
35	3	3	3	4	4	4	5	5	5	6
36	3	4	4	4	4	5	5	5	6	6
37	4	4	4	4	5	5	6	6	6	7
38	4	4	5	5	5	6	6	7	7	8
39	4	5	5	5	6	6	7	7	8	8
40	5	5	5	6	6	7	7	8	8	9
41	5	5	6	6	7	7	8	9	9	10
42	6	6	6	7	7	8	9	9	10	11
43	6	7	7	8	8	9	9	10	11	12
44	7	7	8	8	9	10	10	11	12	13
45	7	8	8	9	10	10	11	12	13	14
46	8	9	9	10	11	11	12	13	14	15
47	9	9	10	11	12	12	13	14	15	16
48	9	10	11	12	13	14	15	16	17	18
49	10	11	12	13	14	15	16	17	18	19
50	11	12	13	14	15	16	17	18	20	21
51	12	13	14	15	16	17	19	20	21	22
52	13	14	15	17	18	19	20	21	23	24
53	15	16	17	18	19	20	22	23	24	26
54	16	17	18	19	21	22	23	25	26	28
55	17	18	20	21	22	24	25	27	28	30
56	19	20	21	23	24	26	27	29	30	32
57	20	22	23	25	26	28	29	31	32	34
58	22	24	25	27	28	30	31	33	34	36
59	24	25	27	28	30	32	33	35	36	38
60	26	27	29	31	32	34	35	37	38	40

TABLE VII - PERCENT VALUE OF REFUND FEATURE
DURATION OF GUARANTEED AMOUNT

AGE	31 YEARS	32 YEARS	33 YEARS	34 YEARS	35 YEARS	36 YEARS	37 YEARS	38 YEARS	39 YEARS	40 YEARS
61	28	29	31	33	34	36	37	39	40	42
62	30	32	33	35	36	38	40	41	42	44
63	32	34	35	37	39	40	42	43	45	46
64	34	36	38	39	41	42	44	45	47	48
65	37	38	40	42	43	45	46	47	49	50
66	39	41	42	44	45	47	48	50	51	52
67	41	43	45	46	48	49	50	52	53	54
68	44	45	47	48	50	51	52	54	55	56
69	46	48	49	51	52	53	54	56	57	58
70	48	50	51	53	54	55	57	58	59	60
71	51	52	54	55	56	57	59	60	61	62
72	53	54	56	57	58	59	60	62	62	63
73	55	57	58	59	60	61	62	63	64	65
74	57	59	60	61	62	63	64	65	66	67
75	59	61	62	63	64	65	66	67	68	69
76	62	63	64	65	66	67	68	69	69	70
77	64	65	66	67	68	69	70	70	71	72
78	66	67	68	69	70	70	71	72	73	73
79	67	68	69	70	71	72	73	73	74	75
80	69	70	71	72	73	74	74	75	76	76
81	71	72	73	74	74	75	76	76	77	78
82	73	74	74	75	76	77	77	78	78	79
83	74	75	76	77	77	78	79	79	80	80
84	76	77	77	78	79	79	80	80	81	81
85	78	78	79	79	80	81	81	82	82	83
86	79	80	80	81	81	82	82	83	83	84
87	80	81	81	82	83	83	83	84	84	85
88	82	82	83	83	84	84	85	85	85	86
89	83	83	84	84	85	85	85	86	86	87
90	84	84	85	85	86	86	86	87	87	87
91	85	85	86	86	87	87	87	88	88	88
92	86	86	87	87	87	88	88	88	89	89
93	87	87	87	88	88	88	89	89	89	90
94	87	88	88	88	89	89	89	90	90	90
95	88	88	89	89	89	90	90	90	91	91
96	89	89	89	90	90	90	91	91	91	91
97	89	90	90	90	91	91	91	91	92	92
98	90	90	91	91	91	91	92	92	92	92
99	91	91	91	92	92	92	92	92	93	93
100	91	92	92	92	92	92	93	93	93	93
101	92	92	92	93	93	93	93	93	94	94
102	92	93	93	93	93	94	94	94	94	94
103	93	93	93	94	94	94	94	94	94	95
104	94	94	94	94	94	95	95	95	95	95
105	94	94	95	95	95	95	95	95	95	95
106	95	95	95	95	95	95	96	96	96	96
107	95	95	96	96	96	96	96	96	96	96
108	96	96	96	96	96	96	96	96	97	97
109	96	96	96	97	97	97	97	97	97	97
110	97	97	97	97	97	97	97	97	97	97
111	97	97	97	97	97	97	98	98	98	98
112	97	97	98	98	98	98	98	98	98	98
113	98	98	98	98	98	98	98	98	98	98
114	98	98	98	98	98	98	98	98	98	99
115	98	98	98	99	99	99	99	99	99	99

TABLE VIII - TEMPORARY LIFE ANNUITIES
ONE LIFE - EXPECTED RETURN MULTIPLES

TEMPORARY PERIOD - EXPECTED RETURN MULTIPLES

AGE	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS	6 YEARS	7 YEARS	8 YEARS	9 YEARS	10 YEARS
5	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
6	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
7	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
8	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
9	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
10	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
11	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
12	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
13	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
14	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
15	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
16	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
17	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
18	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
19	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
20	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
21	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
22	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
23	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
24	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
25	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
26	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
27	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
28	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
29	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
30	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
31	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
32	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
33	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
34	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
35	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
36	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	10.0
37	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	9.9
38	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	9.9
39	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0	9.9
40	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	8.9	9.9
41	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	8.9	9.9
42	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	8.9	9.9
43	1.0	2.0	3.0	4.0	5.0	6.0	7.0	7.9	8.9	9.9
44	1.0	2.0	3.0	4.0	5.0	6.0	7.0	7.9	8.9	9.9
45	1.0	2.0	3.0	4.0	5.0	6.0	7.0	7.9	8.9	9.9
46	1.0	2.0	3.0	4.0	5.0	6.0	6.9	7.9	8.9	9.9
47	1.0	2.0	3.0	4.0	5.0	6.0	6.9	7.9	8.9	9.9
48	1.0	2.0	3.0	4.0	5.0	6.0	6.9	7.9	8.9	9.9
49	1.0	2.0	3.0	4.0	5.0	6.0	6.9	7.9	8.9	9.8
50	1.0	2.0	3.0	4.0	5.0	5.9	6.9	7.9	8.9	9.8
51	1.0	2.0	3.0	4.0	5.0	5.9	6.9	7.9	8.9	9.8
52	1.0	2.0	3.0	4.0	5.0	5.9	6.9	7.9	8.8	9.8
53	1.0	2.0	3.0	4.0	5.0	5.9	6.9	7.9	8.8	9.8
54	1.0	2.0	3.0	4.0	4.9	5.9	6.9	7.9	8.8	9.8
55	1.0	2.0	3.0	4.0	4.9	5.9	6.9	7.8	8.8	9.7
56	1.0	2.0	3.0	4.0	4.9	5.9	6.9	7.8	8.8	9.7
57	1.0	2.0	3.0	4.0	4.9	5.9	6.9	7.8	8.8	9.7
58	1.0	2.0	3.0	4.0	4.9	5.9	6.9	7.8	8.7	9.7
59	1.0	2.0	3.0	4.0	4.9	5.9	6.8	7.8	8.7	9.6

TABLE VIII - TEMPORARY LIFE ANNUITIES
ONE LIFE - EXPECTED RETURN MULTIPLES

TEMPORARY PERIOD - EXPECTED RETURN MULTIPLES

AGE	1 YEAR	2 YEARS	3 YEARS	4 YEARS	5 YEARS	6 YEARS	7 YEARS	8 YEARS	9 YEARS	10 YEARS
60	1.0	2.0	3.0	3.9	4.9	5.9	6.8	7.8	8.7	9.6
61	1.0	2.0	3.0	3.9	4.9	5.9	6.8	7.7	8.7	9.6
62	1.0	2.0	3.0	3.9	4.9	5.8	6.8	7.7	8.6	9.5
63	1.0	2.0	3.0	3.9	4.9	5.8	6.8	7.7	8.6	9.5
64	1.0	2.0	3.0	3.9	4.9	5.8	6.7	7.6	8.5	9.4
65	1.0	2.0	3.0	3.9	4.9	5.8	6.7	7.6	8.5	9.3
66	1.0	2.0	2.9	3.9	4.8	5.8	6.7	7.6	8.4	9.3
67	1.0	2.0	2.9	3.9	4.8	5.7	6.6	7.5	8.4	9.2
68	1.0	2.0	2.9	3.9	4.8	5.7	6.6	7.5	8.3	9.1
69	1.0	2.0	2.9	3.9	4.8	5.7	6.6	7.4	8.2	9.0
70	1.0	2.0	2.9	3.9	4.8	5.6	6.5	7.3	8.1	8.9
71	1.0	2.0	2.9	3.8	4.7	5.6	6.5	7.3	8.1	8.8
72	1.0	2.0	2.9	3.8	4.7	5.6	6.4	7.2	8.0	8.7
73	1.0	2.0	2.9	3.8	4.7	5.5	6.3	7.1	7.9	8.6
74	1.0	1.9	2.9	3.8	4.6	5.5	6.3	7.0	7.7	8.4
75	1.0	1.9	2.9	3.8	4.6	5.4	6.2	6.9	7.6	8.3
76	1.0	1.9	2.8	3.7	4.6	5.4	6.1	6.8	7.5	8.1
77	1.0	1.9	2.8	3.7	4.5	5.3	6.0	6.7	7.3	7.9
78	1.0	1.9	2.8	3.7	4.5	5.2	5.9	6.6	7.2	7.7
79	1.0	1.9	2.8	3.6	4.4	5.1	5.8	6.4	7.0	7.5
80	1.0	1.9	2.8	3.6	4.4	5.1	5.7	6.3	6.8	7.3
81	1.0	1.9	2.8	3.6	4.3	5.0	5.6	6.1	6.6	7.0
82	1.0	1.9	2.7	3.5	4.2	4.9	5.4	6.0	6.4	6.8
83	1.0	1.9	2.7	3.5	4.1	4.8	5.3	5.8	6.2	6.5
84	1.0	1.8	2.7	3.4	4.1	4.6	5.2	5.6	6.0	6.3
85	1.0	1.8	2.6	3.3	4.0	4.5	5.0	5.4	5.7	6.0
86	1.0	1.8	2.6	3.3	3.9	4.4	4.8	5.2	5.5	5.7
87	.9	1.8	2.5	3.2	3.8	4.3	4.7	5.0	5.3	5.5
88	.9	1.8	2.5	3.1	3.7	4.1	4.5	4.8	5.0	5.2
89	.9	1.8	2.5	3.1	3.6	4.0	4.3	4.6	4.8	4.9
90	.9	1.7	2.4	3.0	3.4	3.8	4.1	4.4	4.5	4.7
91	.9	1.7	2.4	2.9	3.3	3.7	4.0	4.2	4.3	4.4
92	.9	1.7	2.3	2.8	3.2	3.5	3.8	4.0	4.1	4.2
93	.9	1.7	2.3	2.7	3.1	3.4	3.6	3.8	3.9	4.0
94	.9	1.6	2.2	2.7	3.0	3.3	3.5	3.6	3.7	3.8
95	.9	1.6	2.2	2.6	2.9	3.1	3.3	3.4	3.5	3.6
96	.9	1.6	2.1	2.5	2.8	3.0	3.2	3.3	3.3	3.4
97	.9	1.6	2.1	2.4	2.7	2.9	3.0	3.1	3.2	3.2
98	.9	1.5	2.0	2.4	2.6	2.8	2.9	3.0	3.0	3.0
99	.9	1.5	2.0	2.3	2.5	2.6	2.7	2.8	2.8	2.8
100	.9	1.5	1.9	2.2	2.4	2.5	2.6	2.6	2.6	2.7
101	.8	1.4	1.8	2.1	2.3	2.4	2.4	2.5	2.5	2.5
102	.8	1.4	1.8	2.0	2.1	2.2	2.3	2.3	2.3	2.3
103	.8	1.4	1.7	1.9	2.0	2.1	2.1	2.1	2.1	2.1
104	.8	1.3	1.6	1.8	1.9	1.9	1.9	1.9	1.9	1.9
105	.8	1.3	1.5	1.7	1.7	1.8	1.8	1.8	1.8	1.8
106	.8	1.2	1.4	1.5	1.6	1.6	1.6	1.6	1.6	1.6
107	.7	1.1	1.3	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	.7	1.1	1.2	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	.7	1.0	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	.7	.9	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.6	.8	.9	.9	.9	.9	.9	.9	.9	.9
112	.6	.7	.8	.8	.8	.8	.8	.8	.8	.8
113	.6	.6	.7	.7	.7	.7	.7	.7	.7	.7
114	.5	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIII - TEMPORARY LIFE ANNUITIES
ONE LIFE - EXPECTED RETURN MULTIPLES

TEMPORARY PERIOD - EXPECTED RETURN MULTIPLES

AGE	11 YEARS	12 YEARS	13 YEARS	14 YEARS	15 YEARS	16 YEARS	17 YEARS	18 YEARS	19 YEARS	20 YEARS
5	11.0	12.0	13.0	14.0	15.0	16.0	17.0	18.0	19.0	19.9
6	11.0	12.0	13.0	14.0	15.0	16.0	17.0	18.0	19.0	19.9
7	11.0	12.0	13.0	14.0	15.0	16.0	17.0	18.0	19.0	19.9
8	11.0	12.0	13.0	14.0	15.0	16.0	17.0	18.0	18.9	19.9
9	11.0	12.0	13.0	14.0	15.0	16.0	17.0	18.0	18.9	19.9
10	11.0	12.0	13.0	14.0	15.0	16.0	17.0	18.0	18.9	19.9
11	11.0	12.0	13.0	14.0	15.0	16.0	17.0	17.9	18.9	19.9
12	11.0	12.0	13.0	14.0	15.0	16.0	17.0	17.9	18.9	19.9
13	11.0	12.0	13.0	14.0	15.0	16.0	17.0	17.9	18.9	19.9
14	11.0	12.0	13.0	14.0	15.0	16.0	16.9	17.9	18.9	19.9
15	11.0	12.0	13.0	14.0	15.0	16.0	16.9	17.9	18.9	19.9
16	11.0	12.0	13.0	14.0	15.0	16.0	16.9	17.9	18.9	19.9
17	11.0	12.0	13.0	14.0	15.0	15.9	16.9	17.9	18.9	19.9
18	11.0	12.0	13.0	14.0	15.0	15.9	16.9	17.9	18.9	19.9
19	11.0	12.0	13.0	14.0	15.0	15.9	16.9	17.9	18.9	19.9
20	11.0	12.0	13.0	14.0	14.9	15.9	16.9	17.9	18.9	19.9
21	11.0	12.0	13.0	14.0	14.9	15.9	16.9	17.9	18.9	19.9
22	11.0	12.0	13.0	14.0	14.9	15.9	16.9	17.9	18.9	19.9
23	11.0	12.0	13.0	13.9	14.9	15.9	16.9	17.9	18.9	19.9
24	11.0	12.0	13.0	13.9	14.9	15.9	16.9	17.9	18.9	19.9
25	11.0	12.0	13.0	13.9	14.9	15.9	16.9	17.9	18.9	19.9
26	11.0	12.0	12.9	13.9	14.9	15.9	16.9	17.9	18.9	19.9
27	11.0	12.0	12.9	13.9	14.9	15.9	16.9	17.9	18.9	19.8
28	11.0	12.0	12.9	13.9	14.9	15.9	16.9	17.9	18.9	19.8
29	11.0	12.0	12.9	13.9	14.9	15.9	16.9	17.9	18.8	19.8
30	11.0	11.9	12.9	13.9	14.9	15.9	16.9	17.9	18.8	19.8
31	11.0	11.9	12.9	13.9	14.9	15.9	16.9	17.8	18.8	19.8
32	11.0	11.9	12.9	13.9	14.9	15.9	16.9	17.8	18.8	19.8
33	11.0	11.9	12.9	13.9	14.9	15.9	16.8	17.8	18.8	19.8
34	10.9	11.9	12.9	13.9	14.9	15.9	16.8	17.8	18.8	19.7
35	10.9	11.9	12.9	13.9	14.9	15.8	16.8	17.8	18.8	19.7
36	10.9	11.9	12.9	13.9	14.9	15.8	16.8	17.8	18.7	19.7
37	10.9	11.9	12.9	13.9	14.9	15.8	16.8	17.8	18.7	19.7
38	10.9	11.9	12.9	13.9	14.8	15.8	16.8	17.7	18.7	19.6
39	10.9	11.9	12.9	13.9	14.8	15.8	16.7	17.7	18.7	19.6
40	10.9	11.9	12.9	13.8	14.8	15.8	16.7	17.7	18.6	19.6
41	10.9	11.9	12.9	13.8	14.8	15.8	16.7	17.6	18.6	19.5
42	10.9	11.9	12.8	13.8	14.8	15.7	16.7	17.6	18.6	19.5
43	10.9	11.9	12.8	13.8	14.8	15.7	16.7	17.6	18.5	19.4
44	10.9	11.8	12.8	13.8	14.7	15.7	16.6	17.5	18.5	19.4
45	10.9	11.8	12.8	13.8	14.7	15.7	16.6	17.5	18.4	19.3
46	10.9	11.8	12.8	13.7	14.7	15.6	16.6	17.5	18.4	19.3
47	10.8	11.8	12.8	13.7	14.7	15.6	16.5	17.4	18.3	19.2
48	10.8	11.8	12.7	13.7	14.6	15.6	16.5	17.4	18.3	19.2
49	10.8	11.8	12.7	13.7	14.6	15.5	16.4	17.3	18.2	19.1
50	10.8	11.7	12.7	13.6	14.6	15.5	16.4	17.2	18.1	19.0
51	10.8	11.7	12.7	13.6	14.5	15.4	16.3	17.2	18.0	18.9
52	10.8	11.7	12.6	13.6	14.5	15.4	16.3	17.1	18.0	18.8
53	10.7	11.7	12.6	13.5	14.4	15.3	16.2	17.0	17.9	18.7
54	10.7	11.6	12.6	13.5	14.4	15.3	16.2	16.9	17.8	18.6
55	10.7	11.6	12.5	13.4	14.3	15.2	16.1	16.8	17.6	18.4
56	10.7	11.6	12.5	13.4	14.3	15.1	16.0	16.7	17.5	18.3
57	10.6	11.5	12.4	13.3	14.2	15.1	15.9	16.6	17.4	18.1
58	10.6	11.5	12.4	13.3	14.1	15.0	15.8	16.4	17.2	17.9
59	10.6	11.4	12.3	13.2	14.0	14.9	15.7	16.3	17.0	17.7
60	10.5	11.4	12.3	13.1	13.9	14.7	15.5			

TABLE VIII - TEMPORARY LIFE ANNUITIES
ONE LIFE - EXPECTED RETURN MULTIPLES

TEMPORARY PERIOD - EXPECTED RETURN MULTIPLES

AGE	11 YEARS	12 YEARS	13 YEARS	14 YEARS	15 YEARS	16 YEARS	17 YEARS	18 YEARS	19 YEARS	20 YEARS
61	10.5	11.3	12.2	13.0	13.8	14.6	15.4	16.1	16.8	17.5
62	10.4	11.3	12.1	12.9	13.7	14.5	15.2	15.9	16.6	17.2
63	10.3	11.2	12.0	12.8	13.6	14.3	15.0	15.7	16.3	17.0
64	10.3	11.1	11.9	12.7	13.4	14.1	14.8	15.5	16.1	16.7
65	10.2	11.0	11.8	12.5	13.2	13.9	14.6	15.2	15.8	16.3
66	10.1	10.9	11.6	12.4	13.1	13.7	14.4	14.9	15.5	16.0
67	10.0	10.8	11.5	12.2	12.9	13.5	14.1	14.7	15.2	15.6
68	9.9	10.6	11.4	12.0	12.7	13.3	13.8	14.3	14.8	15.3
69	9.8	10.5	11.2	11.8	12.4	13.0	13.5	14.0	14.4	14.8
70	9.6	10.3	11.0	11.6	12.2	12.7	13.2	13.7	14.0	14.4
71	9.5	10.2	10.8	11.4	11.9	12.4	12.9	13.3	13.6	13.9
72	9.4	10.0	10.6	11.2	11.7	12.1	12.5	12.9	13.2	13.5
73	9.2	9.8	10.4	10.9	11.4	11.8	12.1	12.5	12.7	13.0
74	9.0	9.6	10.1	10.6	11.0	11.4	11.7	12.0	12.3	12.5
75	8.8	9.4	9.9	10.3	10.7	11.0	11.3	11.6	11.8	12.0
76	8.6	9.1	9.6	10.0	10.3	10.6	10.9	11.1	11.3	11.4
77	8.4	8.9	9.3	9.7	10.0	10.2	10.5	10.6	10.8	10.9
78	8.2	8.6	9.0	9.3	9.6	9.8	10.0	10.2	10.3	10.4
79	7.9	8.3	8.7	9.0	9.2	9.4	9.5	9.7	9.8	9.8
80	7.7	8.0	8.3	8.6	8.8	9.0	9.1	9.2	9.3	9.3
81	7.4	7.7	8.0	8.2	8.4	8.5	8.6	8.7	8.8	8.8
82	7.1	7.4	7.6	7.8	8.0	8.1	8.2	8.2	8.3	8.3
83	6.8	7.1	7.3	7.4	7.5	7.6	7.7	7.8	7.8	7.8
84	6.5	6.7	6.9	7.0	7.1	7.2	7.3	7.3	7.3	7.4
85	6.2	6.4	6.6	6.7	6.7	6.8	6.8	6.9	6.9	6.9
86	5.9	6.1	6.2	6.3	6.4	6.4	6.4	6.5	6.5	6.5
87	5.6	5.8	5.9	5.9	6.0	6.0	6.0	6.1	6.1	6.1
88	5.3	5.4	5.5	5.6	5.6	5.6	5.7	5.7	5.7	5.7
89	5.1	5.1	5.2	5.3	5.3	5.3	5.3	5.3	5.3	5.3
90	4.8	4.9	4.9	4.9	5.0	5.0	5.0	5.0	5.0	5.0
91	4.5	4.6	4.6	4.6	4.7	4.7	4.7	4.7	4.7	4.7
92	4.3	4.3	4.3	4.4	4.4	4.4	4.4	4.4	4.4	4.4
93	4.0	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
94	3.8	3.8	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9
95	3.6	3.6	3.6	3.6	3.7	3.7	3.7	3.7	3.7	3.7
96	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4
97	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2
98	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
99	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
100	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7
101	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
102	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
103	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8
113	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
114	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIII - TEMPORARY LIFE ANNUITIES
ONE LIFE - EXPECTED RETURN MULTIPLES

TEMPORARY PERIOD - EXPECTED RETURN MULTIPLES

AGE	21 YEARS	22 YEARS	23 YEARS	24 YEARS	25 YEARS	26 YEARS	27 YEARS	28 YEARS	29 YEARS	30 YEARS
60	18.4	19.0	19.6	20.2	20.7	21.2	21.6	22.0	22.4	22.7
61	18.1	18.7	19.3	19.8	20.3	20.7	21.1	21.5	21.8	22.1
62	17.8	18.4	18.9	19.4	19.9	20.3	20.6	21.0	21.2	21.5
63	17.5	18.1	18.5	19.0	19.4	19.8	20.1	20.4	20.6	20.8
64	17.2	17.7	18.1	18.6	18.9	19.3	19.5	19.8	20.0	20.2
65	16.8	17.3	17.7	18.1	18.4	18.7	18.9	19.2	19.3	19.5
66	16.5	16.9	17.3	17.6	17.9	18.1	18.3	18.5	18.7	18.8
67	16.1	16.4	16.8	17.1	17.3	17.5	17.7	17.9	18.0	18.1
68	15.6	16.0	16.3	16.5	16.7	16.9	17.1	17.2	17.3	17.4
69	15.2	15.5	15.7	16.0	16.1	16.3	16.4	16.5	16.6	16.7
70	14.7	15.0	15.2	15.4	15.5	15.7	15.8	15.8	15.9	15.9
71	14.2	14.4	14.6	14.8	14.9	15.0	15.1	15.2	15.2	15.2
72	13.7	13.9	14.1	14.2	14.3	14.4	14.4	14.5	14.5	14.5
73	13.2	13.3	13.5	13.6	13.7	13.7	13.8	13.8	13.8	13.9
74	12.6	12.8	12.9	13.0	13.0	13.1	13.1	13.1	13.2	13.2
75	12.1	12.2	12.3	12.4	12.4	12.5	12.5	12.5	12.5	12.5
76	11.5	11.6	11.7	11.8	11.8	11.8	11.8	11.9	11.9	11.9
77	11.0	11.1	11.1	11.2	11.2	11.2	11.2	11.2	11.2	11.2
78	10.4	10.5	10.5	10.6	10.6	10.6	10.6	10.6	10.6	10.6
79	9.9	9.9	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0
80	9.4	9.4	9.4	9.4	9.5	9.5	9.5	9.5	9.5	9.5
81	8.8	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9
82	8.3	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4
83	7.8	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9
84	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4
85	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9
86	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5
87	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1
88	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7
89	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
90	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
91	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7
92	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4
93	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
94	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9
95	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7
96	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4
97	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2
98	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
99	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
100	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7
101	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
102	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
103	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8
113	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
114	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

TABLE VIII - TEMPORARY LIFE ANNUITIES
ONE LIFE - EXPECTED RETURN MULTIPLES

TEMPORARY PERIOD - EXPECTED RETURN MULTIPLES

AGE	21 YEARS	22 YEARS	23 YEARS	24 YEARS	25 YEARS	26 YEARS	27 YEARS	28 YEARS	29 YEARS	30 YEARS
5	20.9	21.9	22.9	23.9	24.9	25.9	26.9	27.9	28.9	29.9
6	20.9	21.9	22.9	23.9	24.9	25.9	26.9	27.9	28.9	29.9
7	20.9	21.9	22.9	23.9	24.9	25.9	26.9	27.9	28.9	29.9
8	20.9	21.9	22.9	23.9	24.9	25.9	26.9	27.9	28.9	29.8
9	20.9	21.9	22.9	23.9	24.9	25.9	26.9	27.9	28.9	29.8
10	20.9	21.9	22.9	23.9	24.9	25.9	26.9	27.9	28.8	29.8
11	20.9	21.9	22.9	23.9	24.9	25.9	26.9	27.9	28.8	29.8
12	20.9	21.9	22.9	23.9	24.9	25.9	26.9	27.8	28.8	29.8
13	20.9	21.9	22.9	23.9	24.9	25.9	26.9	27.8	28.8	29.8
14	20.9	21.9	22.9	23.9	24.9	25.9	26.8	27.8	28.8	29.8
15	20.9	21.9	22.9	23.9	24.9	25.9	26.8	27.8	28.8	29.8
16	20.9	21.9	22.9	23.9	24.9	25.8	26.8	27.8	28.8	29.8
17	20.9	21.9	22.9	23.9	24.9	25.8	26.8	27.8	28.8	29.8
18	20.9	21.9	22.9	23.9	24.8	25.8	26.8	27.8	28.8	29.7
19	20.9	21.9	22.9	23.9	24.8	25.8	26.8	27.8	28.8	29.7
20	20.9	21.9	22.9	23.8	24.8	25.8	26.8	27.8	28.7	29.7
21	20.9	21.9	22.9	23.8	24.8	25.8	26.8	27.8	28.7	29.7
22	20.9	21.9	22.8	23.8	24.8	25.8	26.8	27.7	28.7	29.7
23	20.9	21.9	22.8	23.8	24.8	25.8	26.7	27.7	28.7	29.7
24	20.9	21.8	22.8	23.8	24.8	25.8	26.7	27.7	28.7	29.6
25	20.9	21.8	22.8	23.8	24.8	25.7	26.7	27.7	28.6	29.6
26	20.8	21.8	22.8	23.8	24.8	25.7	26.7	27.7	28.6	29.6
27	20.8	21.8	22.8	23.8	24.7	25.7	26.7	27.6	28.6	29.5
28	20.8	21.8	22.8	23.7	24.7	25.7	26.6	27.6	28.6	29.5
29	20.8	21.8	22.8	23.7	24.7	25.7	26.6	27.6	28.5	29.5
30	20.8	21.8	22.7	23.7	24.7	25.6	26.6	27.5	28.5	29.4
31	20.8	21.8	22.7	23.7	24.6	25.6	26.6	27.5	28.4	29.4
32	20.8	21.7	22.7	23.7	24.6	25.6	26.5	27.5	28.4	29.3
33	20.8	21.7	22.7	23.6	24.6	25.5	26.5	27.4	28.4	29.3
34	20.7	21.7	22.7	23.6	24.6	25.5	26.4	27.4	28.3	29.2
35	20.7	21.7	22.6	23.6	24.5	25.5	26.4	27.3	28.2	29.2
36	20.7	21.6	22.6	23.5	24.5	25.4	26.3	27.3	28.2	29.1
37	20.7	21.6	22.6	23.5	24.4	25.4	26.3	27.2	28.1	29.0
38	20.6	21.6	22.5	23.4	24.4	25.3	26.2	27.1	28.0	28.9
39	20.6	21.5	22.5	23.4	24.3	25.2	26.1	27.0	27.9	28.8
40	20.6	21.5	22.4	23.3	24.3	25.2	26.1	27.0	27.8	28.7
41	20.5	21.4	22.4	23.3	24.2	25.1	26.0	26.9	27.7	28.6
42	20.5	21.4	22.3	23.2	24.1	25.0	25.9	26.8	27.6	28.5
43	20.4	21.3	22.2	23.2	24.0	24.9	25.8	26.6	27.5	28.3
44	20.4	21.3	22.2	23.1	24.0	24.8	25.7	26.5	27.3	28.2
45	20.3	21.2	22.1	23.0	23.9	24.7	25.6	26.4	27.2	28.0
46	20.2	21.1	22.0	22.9	23.8	24.6	25.4	26.2	27.0	27.8
47	20.2	21.1	21.9	22.8	23.6	24.5	25.3	26.1	26.8	27.6
48	20.1	21.0	21.8	22.7	23.5	24.3	25.1	25.9	26.6	27.4
49	20.0	20.9	21.7	22.6	23.4	24.2	25.0	25.7	26.4	27.1
50	19.9	20.8	21.6	22.4	23.2	24.0	24.8	25.5	26.2	26.9
51	19.8	20.7	21.5	22.3	23.1	23.8	24.6	25.3	25.9	26.6
52	19.7	20.6	21.4	22.1	22.9	23.6	24.3	25.0	25.7	26.3
53	19.6	20.4	21.2	22.0	22.7	23.4	24.1	24.7	25.3	25.9
54	19.5	20.3	21.0	21.8	22.5	23.2	23.8	24.4	25.0	25.6
55	19.3	20.1	20.8	21.6	22.2	22.9	23.5	24.1	24.6	25.2
56	19.2	19.9	20.6	21.3	22.0	22.6	23.2	23.7	24.3	24.7
57	19.0	19.7	20.4	21.1	21.7	22.3	22.8	23.4	23.8	24.3
58	18.8	19.5	20.2	20.8	21.4	21.9	22.5	22.9	23.4	23.8
59	18.6	19.3	19.9	20.5	21.1	21.6	22.0	22.5	22.9	23.2

TABLE VIII - TEMPORARY LIFE ANNUITIES
ONE LIFE - EXPECTED RETURN MULTIPLES

TEMPORARY PERIOD - EXPECTED RETURN MULTIPLES

AGE	31 YEARS	32 YEARS	33 YEARS	34 YEARS	35 YEARS	36 YEARS	37 YEARS	38 YEARS	39 YEARS	40 YEARS
5	30.8	31.8	32.8	33.8	34.8	35.8	36.8	37.7	38.7	39.7
6	30.8	31.8	32.8	33.8	34.8	35.8	36.8	37.7	38.7	39.7
7	30.8	31.8	32.8	33.8	34.8	35.8	36.7	37.7	38.7	39.7
8	30.8	31.8	32.8	33.8	34.8	35.7	36.7	37.7	38.7	39.7
9	30.8	31.8	32.8	33.8	34.8	35.7	36.7	37.7	38.7	39.6
10	30.8	31.8	32.8	33.8	34.7	35.7	36.7	37.7	38.6	39.6
11	30.8	31.8	32.8	33.8	34.7	35.7	36.7	37.7	38.6	39.6
12	30.8	31.8	32.8	33.7	34.7	35.7	36.7	37.6	38.6	39.6
13	30.8	31.8	32.7	33.7	34.7	35.7	36.6	37.6	38.6	39.5
14	30.8	31.8	32.7	33.7	34.7	35.7	36.6	37.6	38.6	39.5
15	30.8	31.7	32.7	33.7	34.7	35.6	36.6	37.6	38.5	39.5
16	30.8	31.7	32.7	33.7	34.6	35.6	36.6	37.5	38.5	39.4
17	30.7	31.7	32.7	33.7	34.6	35.6	36.5	37.5	38.5	39.4
18	30.7	31.7	32.7	33.6	34.6	35.6	36.5	37.5	38.4	39.4
19	30.7	31.7	32.6	33.6	34.6	35.5	36.5	37.4	38.4	39.3
20	30.7	31.7	32.6	33.6	34.5	35.5	36.4	37.4	38.3	39.3
21	30.7	31.6	32.6	33.6	34.5	35.5	36.4	37.4	38.3	39.2
22	30.6	31.6	32.6	33.5	34.5	35.4	36.4	37.3	38.2	39.2
23	30.6	31.6	32.5	33.5	34.4	35.4	36.3	37.3	38.2	39.1
24	30.6	31.5	32.5	33.5	34.4	35.3	36.3	37.2	38.1	39.0
25	30.6	31.5	32.5	33.4	34.3	35.3	36.2	37.1	38.1	39.0
26	30.5	31.5	32.4	33.4	34.3	35.2	36.2	37.1	38.0	38.9
27	30.5	31.4	32.4	33.3	34.2	35.2	36.1	37.0	37.9	38.8
28	30.5	31.4	32.3	33.3	34.2	35.1	36.0	36.9	37.8	38.7
29	30.4	31.4	32.3	33.2	34.1	35.0	35.9	36.8	37.7	38.6
30	30.4	31.3	32.2	33.1	34.1	35.0	35.8	36.7	37.6	38.5
31	30.3	31.2	32.2	33.1	34.0	34.9	35.8	36.6	37.5	38.3
32	30.3	31.2	32.1	33.0	33.9	34.8	35.6	36.5	37.4	38.2
33	30.2	31.1	32.0	32.9	33.8	34.7	35.5	36.4	37.2	38.0
34	30.1	31.0	31.9	32.8	33.7	34.6	35.4	36.2	37.1	37.9
35	30.1	31.0	31.8	32.7	33.6	34.4	35.3	36.1	36.9	37.7
36	30.0	30.9	31.7	32.6	33.5	34.3	35.1	35.9	36.7	37.4
37	29.9	30.8	31.6	32.5	33.3	34.1	34.9	35.7	36.5	37.2
38	29.8	30.7	31.5	32.3	33.2	34.0	34.7	35.5	36.2	37.0
39	29.7	30.5	31.4	32.2	33.0	33.8	34.5	35.3	36.0	36.7
40	29.6	30.4	31.2	32.0	32.8	33.6	34.3	35.0	35.7	36.4
41	29.4	30.2	31.0	31.8	32.6	33.3	34.1	34.7	35.4	36.0
42	29.3	30.1	30.9	31.6	32.4	33.1	33.8	34.4	35.1	35.7
43	29.1	29.9	30.7	31.4	32.1	32.8	33.5	34.1	34.7	35.3
44	28.9	29.7	30.5	31.2	31.9	32.5	33.2	33.8	34.3	34.9
45	28.8	29.5	30.2	30.9	31.6	32.2	32.8	33.4	33.9	34.4
46	28.5	29.3	30.0	30.6	31.3	31.9	32.4	33.0	33.5	33.9
47	28.3	29.0	29.7	30.3	30.9	31.5	32.0	32.5	33.0	33.4
48	28.1	28.7	29.4	30.0	30.6	31.1	31.6	32.1	32.5	32.9
49	27.8	28.4	29.0	29.6	30.2	30.7	31.1	31.5	31.9	32.3
50	27.5	28.1	28.7	29.2	29.7	30.2	30.6	31.0	31.4	31.7
51	27.2	27.8	28.3	28.8	29.3	29.7	30.1	30.4	30.7	31.0
52	26.8	27.4	27.9	28.4	28.8	29.2	29.5	29.8	30.1	30.3
53	26.5	27.0	27.4	27.9	28.3	28.6	28.9	29.2	29.4	29.6
54	26.1	26.5	27.0	27.4	27.7	28.0	28.3	28.5	28.7	28.9
55	25.6	26.1	26.5	26.8	27.1	27.4	27.6	27.8	28.0	28.1
56	25.2	25.6	25.9	26.2	26.5	26.7	26.9	27.1	27.2	27.3
57	24.7	25.0	25.3	25.6	25.8	26.0	26.2	26.3	26.5	26.5
58	24.1	24.4	24.7	25.0	25.2	25.3	25.5	25.6	25.7	25.7
59	23.6	23.8	24.1	24.3	24.4	24.6	24.7	24.8	24.9	24.9
60	23.0	23.2	23.4	23.6	23.7	23.8	23.9	24.0	24.0	24.1

TABLE VIII - TEMPORARY LIFE ANNUITIES
ONE LIFE - EXPECTED RETURN MULTIPLES
TEMPORARY PERIOD - EXPECTED RETURN MULTIPLES

AGE	31 YEARS	32 YEARS	33 YEARS	34 YEARS	35 YEARS	36 YEARS	37 YEARS	38 YEARS	39 YEARS	40 YEARS
61	22.3	22.5	22.7	22.9	23.0	23.1	23.1	23.2	23.2	23.3
62	21.7	21.9	22.0	22.1	22.2	22.3	22.3	22.4	22.4	22.4
63	21.0	21.1	21.3	21.4	21.4	21.5	21.5	21.6	21.6	21.6
64	20.3	20.4	20.5	20.6	20.6	20.7	20.7	20.7	20.8	20.8
65	19.6	19.7	19.8	19.8	19.9	19.9	19.9	19.9	19.9	20.0
66	18.9	19.0	19.0	19.1	19.1	19.1	19.1	19.1	19.1	19.1
67	18.2	18.2	18.3	18.3	18.3	18.3	18.3	18.3	18.4	18.4
68	17.4	17.5	17.5	17.5	17.5	17.6	17.6	17.6	17.6	17.6
69	16.7	16.7	16.8	16.8	16.8	16.8	16.8	16.8	16.8	16.8
70	16.0	16.0	16.0	16.0	16.0	16.0	16.0	16.0	16.0	16.0
71	15.3	15.3	15.3	15.3	15.3	15.3	15.3	15.3	15.3	15.3
72	14.6	14.6	14.6	14.6	14.6	14.6	14.6	14.6	14.6	14.6
73	13.9	13.9	13.9	13.9	13.9	13.9	13.9	13.9	13.9	13.9
74	13.2	13.2	13.2	13.2	13.2	13.2	13.2	13.2	13.2	13.2
75	12.5	12.5	12.5	12.5	12.5	12.5	12.5	12.5	12.5	12.5
76	11.9	11.9	11.9	11.9	11.9	11.9	11.9	11.9	11.9	11.9
77	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2	11.2
78	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6	10.6
79	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0
80	9.5	9.5	9.5	9.5	9.5	9.5	9.5	9.5	9.5	9.5
81	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9
82	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4	8.4
83	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9
84	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4
85	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9	6.9
86	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5
87	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1
88	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7	5.7
89	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3	5.3
90	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
91	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7
92	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4	4.4
93	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
94	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9	3.9
95	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7
96	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4
97	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2
98	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
99	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8
100	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7
101	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
102	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
103	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1
104	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
105	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
106	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6	1.6
107	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
108	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3
109	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
110	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
111	.9	.9	.9	.9	.9	.9	.9	.9	.9	.9
112	.8	.8	.8	.8	.8	.8	.8	.8	.8	.8
113	.7	.7	.7	.7	.7	.7	.7	.7	.7	.7
114	.6	.6	.6	.6	.6	.6	.6	.6	.6	.6
115	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5

If the terms of the contract (a) involve a life or lives, (b) are such that the above tables cannot be correctly applied, and (c) the amounts received thereunder are at least partly "amounts received as an annuity" under a contract to which section 72 applies, the taxpayer may submit with his return an actuarial computation based upon the applicable annuity table (described below) with ages set back one year, showing the appropriate factors applied in his case, subject to the approval of the Commissioner upon examination of such return. The applicable annuity table is the 1937 Standard Annuity Table (if the investment in the contract does not include a post-June 1986 investment in the contract) or the gender-neutral version of the 1983 Basic Table (if the investment in the contract includes a post-June 1986 investment in the contract). In the case of a contract to which §1.72-6(d) (relating to contracts in which amounts were invested both before July 1, 1986, and after June 30, 1986) applies, the actuarial computation shall be based on both tables in accordance with the principles of §1.72-6(d). Computations involving factors to compensate for the effects of contingencies other than mortality, such as marriage or remarriage, re-employment, recovery from disability, or the like, will not be approved.

Par. 7. Section 1.72-11 is amended by revising paragraph (c) to read as follows:

§1.72-11 Amounts not received as annuity payments.

* * * * *

(c) *Amounts received in the nature of a refund of the consideration under a contract and in full discharge of the obligation thereof.* (1) Any amount received under a contract to which section 72 applies, if it is at least in part a refund of the consideration paid, including amounts payable to a beneficiary after the death of an annuitant by reason of a provision in the contract for a life annuity with minimum period of payments certain or with a minimum amount which must be paid in any event, shall be considered an amount received in the nature of a refund of the consideration paid for such contract. If such an amount is in full discharge of an obligation to pay a fixed amount (whether in a lump sum or otherwise) or to pay amounts for a fixed number of years (including amounts described in paragraph (b)(3)(i) of §1.72-2), it shall be included in the gross income of the recipient only to the extent that it, when added to amounts previously received under the contract which were excludable from gross income under the law applicable at the time of receipt, exceeds the aggregate of premiums or other consideration paid. See section 72(e)(2)(A). This paragraph shall not apply if the total of the amounts to be paid in discharge of the obligation can in any event exceed the total of the annuity payments which would otherwise fully discharge the obligation. For rules to be applied in such a case, see paragraph (e) of this section.

(2) The principles of subparagraph (1) of this paragraph may be illustrated by the following examples:

Example (1). A, a male employee, retired on December 31, 1954, at the age of 60. A life annuity of $75 per month was payable to him beginning January 31, 1955. The annuity contract guaranteed that if A did not live for at least ten years after his retirement his beneficiary, B, would receive the monthly payments for any balance of such ten year period which remained at the date of A's death. Under section 72, A was deemed to have paid $3,600 toward the cost of the annuity. A lived for five years after his retirement receiving a total of $4,500 in annuity payments. After A's death, B began receiving the monthly payments of $75 beginning with the January 31, 1960 payment. B will exclude such payments from his gross income throughout 1960, 1961, and 1962, and will exclude only $18 of the first payment in 1963 from his gross income for that year. Thereafter, B will include the entire amount of all such payments in his gross income for the taxable year of recipt. This result is determined as follows:

A's investment in the contract (unadjusted)	$3,600
Multiple from Table III of §1.72-9 for male, age 60, where duration of guaranteed amount is 10 years (percent)	11
Subtract value of the refund feature to the nearest dollar (11 percent of $3,600)	396
Investment in the contract adjusted for the present value of the refund feature without discount for interest	3,204
Aggregate of premiums or other consideration paid	3,600
A's exclusion ratio ($3,204 ÷ $16,380 [$900 × 18.2]) (percent) . . . . ;	19.6
Subtract amount excludable during five years A received payments (19.6 percent of 44,500 [$999 × 5])	882
Remainder of aggregate of premiums or other consideration paid excludable from gross income of B under section 72(e)	2,718

As a result of the above computation, the number of payments to B which will exhaust the remainder of consideration paid which is excludable from gross income of the recipient is 36 6/25 ($2,718 ÷ $75) and B will exclude the payments from his gross income for three years, then exclude only $18 of the first payment for the fourth year from his gross income, and thereafter include the entire amount of all payments he receives in his gross income.

Example (2). The facts are the same as in example (1), except that B, the beneficiary, elects to receive $50 per month for his life in lieu of the payments guaranteed under the original contractual obligation. Since such amounts will be received as an annuity and may, because of the length of time B may live, exceed the amount guaranteed, they are not amounts to which this paragraph applies. See paragraph (e) of the section.

Example (3). The facts are the same as in example (1), except that B, the beneficiary, elects to receive the remaining guaranteed amount in installments which are larger or smaller than the $75 per month provided until, under the terms of the contract, the guaranteed amount is exhausted. The rule of subparagraph (1) of this paragraph and the computation illustrated in example (1) apply to such installments since the total of such installments will not exceed the original amount guaranteed to be paid at A's death in any event.

Example (4). C pays $12,000 for a contract providing that he is to be paid an annuity of $1,000 per year for 15 years. His exclusion ratio is therefore 80 percent ($12,000 ÷ $15,000). He directs that the annuity is to be paid to D, his beneficiary, if he should die before the full 15 year period has expired. C dies after 5 years and D is paid $1,000 in 1960. D will include $200 ($1,000 − $800 [80 percent of $1,000]) in his gross income for the taxable year in which he receives the $1,000 since section 72*(e)* and this section do not apply to the annuity payments made in accordance with the provisions and during the term of the contract. D will continue with the same exclusion ratio used by C (80 percent).

Example (5). In 1954, E paid $50,000 into a fund and was promised an annual income for life the amount of which would depend in part upon the earnings realized from the investment of the fund in accordance with an agreed formula. The contract also specified that if E should die before ten years had elapsed, his beneficiary, F, would be paid the amounts determined annually under the formula until ten payments had been received by E and F together, E died in 1960, having received five payments totaling $30,000. Assuming that $22,000 of this amount was properly excludable from E's gross income prior to his death. F will exclude from his gross income the payments he receives until the taxable year in which his total receipts from the fund exceeds $28,000 ($50,000 − $22,000). F will include any excess over the $28,000 in his gross income for that taxable year. Thereafter, F will include in his gross income the entire amount of any payments made to him from the fund.

Example (6). Assume the facts are the same as in example (1), except that the total investment in the contract is made after June 30, 1986, that A is to receive payments under the life annuity contract beginning on January 31, 1987, and that B will begin to receive the monthly payments on January 31, 1992. B will exclude the $75 monthly payments from gross income throughout 1992, 1993, and 1994. B will exclude only the first two monthly payments and $21 of the third monthly payment in 1995. This is determined as follows:

A's investment in the contract (unadjusted)	$3,600
Multiple from Table VII, age 60, 10 years (percent)	4
Subtract value of the refund feature (4 percent of $3,600)	$144
Investment in the contract adjusted for the present value of the refund feature without discount for interest	$3,456
Aggregate of premiums or other consideration paid	$3,600.00
A's exclusion ratio ($3,456 ÷ $21,780 [$900 × 24.2]) (percent)	15.9
Subtract amount excludable during five years A received payments (15.9 percent of $4,500 $900 × 5])	$715.00
Remainder of aggregate of premiums or other consideration paid excludable from gross income of B under section 72 (e)	$2,884.50

As a result of the above computation, the number of payments to B which will exhaust the remainder of consideration paid which is excludable from gross income of the recipient is $38\frac{23}{50}$ ($2,884.50 ÷ 75) and B will exclude the payments from gross income for three years, then exclude only the first two monthly payments and $34.50 of the third. Thereafter B shall include the entire amount of all payments received in gross income.

(3) For the purpose of applying the rule contained in subparagraph (1) of this paragraph, it is immaterial whether the recipient of the amount received in full discharge of the obligation is the same person as the recipient of amounts previously received under the contract which were excludable from gross income, except in the case of a contract transferred for a valuable consideration, with respect to which see paragraph (a) of §1.72–10. For the limit on the tax, for taxable years beginning before January 1, 1964, attributable to the receipt of a lump sum to which this paragraph applies, see paragraph (g) of this section.

* * * * *

Par. 8. Subparagraph (4) of section 1.403(b)-1(d) is amended by adding the words "to a defined benefit plan" following the words "employer contributions" in the first sentence.

Par. 9. Subparagraph (4)(ii) of section 1.403(b)-1(d) is amended by removing the words "the employee's sex and the".

Par. 10. Subparagraph (4)(iv) of section 1.403(b)-1(d) is removed and the following new subparagraph (4)(iv) is added:

§1.403(b)-1 Taxability of beneficiary under annuity purchased by section 501(c)(3) organization or public school.

* * * * *

(d) *Exclusion allowance*—(1) * * *

(4) *Determination of excludable amounts by allocation of contributions*.* * *

(iv) The lesser of the number of years of service credited through the end of the taxable year or the number of years that the plan has been in existence at such time.

TABLE I

[Value at normal retirement ages of annuity of $1.00 per annum payable in equal monthly installments during the life of the employee] [For taxable years beginning after July 1, 1986.]

Ages	*Values*
40	11.49
41	11.40
42	11.31
43	11.22
44	11.12
45	11.01
46	10.91
47	10.79
48	10.68
49	10.56
50	10.43
51	10.30
52	10.18
53	10.04
54	9.89
55	9.75
56	9.60
57	9.44
58	9.28
59	9.13
60	8.96
61	8.79
62	8.62
63	8.44
64	8.25
65	8.08
66	7.88
67	7.70
68	7.50
69	7.29
70	7.10
71	6.88
72	6.68
73	6.46
74	6.25
75	6.03
76	5.82
77	5.61
78	5.40
79	5.20
80	4.99

Note. If the normal form of retirement benefit under the plan is other than a straight life annuity, the value from Table I above should be divided by the figure set forth below opposite the normal form of retirement benefit provided by the plan.

Annuity for 5 years certain and life thereafter	0.97
Annuity for 10 years certain and life thereafter	0.90
Annuity for 15 years certain and life thereafter	0.80
Annuity for 20 years certain and life thereafter	0.70
Life annuity with installment refund	0.80
Life annuity with cash refund[1]	0.75

[1] The term "cash refund" refers to refund of accumulated employer contributions, and does not refer to refund of employee contributions only, often referred to as "modified cash refund."

TABLE II

[LEVEL ANNUAL CONTRIBUTION WHICH WILL ACCUMULATE TO $1.00 AT END OF NUMBER OF YEARS]

[For taxable years beginning after July 1, 1986.]

Number of years	*Amount*
1	$1.000
2	.4808
3	.3080
4	.2219
5	.1705
6	.1363
7	.1121
8	.0940
9	.0801
10	.0690
11	.0601
12	.0527
13	.0465
14	.0413
15	.0368
16	.0330
17	.0296
18	.0267
19	.0241
20	.0219
21	.0198
22	.0180
23	.0164
24	.0150
25	.0137
26	$0.0125
27	.0114
28	.0105
29	.0096
30	.0088

31	.0081
32	.0075
33	.0069
34	.0063
35	.0058
36	.0053
37	.0049
38	.0045
39	.0042
40	.0039
41	.0036
42	.0033
43	.0030
44	.0028
45	.0026
46	.0024
47	.0022
48	.0020
49	.0019
50	.0017

Par. 11. Section 1.401(a)-18 is removed.

Par. 12. Sections 1.401(j)-1 through 1.401(j)-6 are removed.

REPORTING AND RECORDKEEPING REQUIREMENTS (26 CFR Part 602)

Par. 13. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 14. Section 602.101(c) is amended by inserting in the appropriate place in the table "§1.72-6 . . . [ ]".

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on March 19, 1986, 10:39 a.m., and published in the issue of the Federal Register for March 24, 1986, 51 F.R. 9978)

Estimated Tax—U.S. Citizens, Resident or Nonresident Aliens—Extension of Time

Announcement 86-48

The Internal Revenue Service has granted to any U.S. citizen or resident alien individual who is outside the United States and Puerto Rico on April 15, 1986, an automatic extension of 2 months to pay the first installment of estimated tax. Thus, the first estimated installment payment otherwise due on April 15, 1986, will be due on June 15, 1986. Since June 15 falls on a Sunday this year, however, the first estimated tax payment date is June 16, 1986. A U.S. citizen or resident alien individual who is outside the U.S. and Puerto Rico on April 15, 1986 and pays the first installment of estimated tax on June 16, 1986, generally must pay one half of the required annual payment at that time. If the required amount is not paid by June 16, then for purposes of the penalty for underpayment of the estimated tax, the period and amount of the underpayment will be calculated without regard to the extension.

A nonresident alien individual who files on a calendar year basis must make the first estimated tax payment by June 15, 1986. Again, since June 15 falls on a Sunday, the first estimated installment payment is due June 16, 1986. If a nonresident alien individual received wages subject to the same withholding rules that apply to U.S. citizens, however, then that individual must meet the usual April 15, 1986, date for the first installment payment. If the first payment is not due until June 16, 1986, the nonresident alien individual must pay one half of the required annual payment at that time.

Information concerning the payment of individual estimated income tax for 1986 can be found in Publication 54 (Rev. Nov. 1985), Tax Guide for U.S. Citizens and Resident Aliens Abroad, and in Publication 519 (Rev. Nov. 1985), U.S. Tax Guide for Aliens.

Unisex Annuity Tables—Public Hearing

Announcement 86-49[1]

SUMMARY: This document provides notice of a public hearing on proposed regulations to the annuity tables used to compute the portion of the amount received as an annuity that is includible in gross income.

DATES: The public hearing will be held on Wednesday, May 21, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Monday, May 5, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, Attn: CC:LR:T (LR-19-80), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: B. Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935, not a toll-free call.

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under section 72 of the Internal Revenue Code of 1954. The proposed regulations appear * * * [on page 9, this Bulletin].

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who submit written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit not later than Monday, May 5, 1986, an outline of the oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions, attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

Transitional Rule for Application of Basis Allocation Regulations Under Section 338

Announcement 86-51

The Temporary Income Tax Regulations under section 338(b) of the Internal Revenue Code will soon be amended. The amendments will provide a special transitional allocation election relating to the allocation of basis among the assets of a target corporation for stock acquisitions occurring on or before January 29, 1986, or pursuant to a binding written contract entered into on or before that date. In general, if a corporation acquires the stock of a target corporation and a section 338 election is made, then the adjusted purchase price for the target's stock must be determined and must be allocated as basis among the target's assets. By temporary regulations published in the Federal Register on January 29, 1986 (T.D. 8072), the Internal Revenue Service prescribed a method of basis allocation for stock acquisitions occurring after August 31, 1982, for which an election under section 338 is made.

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[1] Filed by the Office of the Federal Register on March 19, 1986, 10:39 a.m., and published in the issue of the Federal Register for March 24, 1986, 51 F.R. 10024.

The amendments to the temporary regulations will provide that, under the special transitional allocation election referred to above, an acquiring corporation must allocate basis pursuant to the rules currently applicable when a combination of assets is acquired for a lump sum purchase price. Those rules would ordinarily produce results consistent with the method of allocation required under the temporary regulations. A different allocation of basis could result only if the taxpayer or the Service establishes that the total adjusted purchase price to be allocated differs from the total value of the target's assets. That would depend upon the proper valuation of the assets deemed purchased by the taxpayer, including goodwill and going concern value.

Corporations that elect to allocate basis pursuant to the amendments to the temporary regulations will be required to file a transitional allocation election apprising the Service of the allocation method employed with respect to the target's assets. The amendments to the temporary regulations will prescribe the manner and consequences of making a transitional allocation election.

Revision of Form 5330, Return of Excise Taxes Related to Employee Benefit Plans

Announcement 86-52

Form 5330, Return of Excise Taxes Related to Employee Benefit Plans, was revised January 1986 to reflect new provisions enacted in Public Law 98-369. New parts have been added to the form for two new taxes: the tax on disqualified benefits imposed by section 4976 of the Internal Revenue Code and the tax on excess fringe benefits imposed by section 4977. In addition, a new line was added for the tax on certain ESOP dispositions imposed by section 4978.

To obtain a copy of the form and the instructions, call the Internal Revenue Service forms number listed in your local telephone directory under "United States Government."

Availability of Revised Publication 721

Announcement 86-53

An updated edition of Publication 721 (Rev. Feb. 1986), Comprehensive Tax Guide to U.S. Civil Service Retirement Benefits, is now available from the Service. The publication explains in detail how the federal income, estate, and gift tax rules apply to benefits that retired federal employees, including those disabled, or their survivors receive under the Civil Service Retirement Act.

The publication covers several tax changes, including the new treatment of disability income and the addition of a new actuarial table for figuring the value of an annuity.

The publication may be ordered by calling the "Federal Tax Forms Only" number listed in the phone book under "United States Government, Internal Revenue Service."

Request for Forms Suggestions

Announcement 86-55

As part of its annual forms review process, the Internal Revenue Service is inviting written comments and suggestions for improving its tax return forms, instructions, and related schedules. The comments may apply to any tax form issued by the Internal Revenue Service. However, the Service would particularly appreciate specific suggestions on ways to reduce the reporting burden on the tax forms. The written submissions should be self-explanatory and in enough detail to communicate clearly what is being suggested. Careful consideration will be given to all comments and suggestions received. However, individual responses to the submissions will not be made because of the volume of correspondence expected.

To meet our work schedule and early printing deadlines, we request that written submissions be received by June 2, 1986.

Comments and suggestions should be sent to the Chairman, Tax Forms Coordinating Committee, Room 5577, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. Further information about this notice may be obtained by calling (202) 566-6150.

Notice of Disposition of Declaratory Judgment Proceedings Under Section 7428; Termination of Section 7428(c) Validation of Certain Contributions Made During Pendency of Declaratory Judgment Proceedings

This announcement serves notice to donors that a court has determined that the organization listed below continues to be described in section 170(c)(2) of the Internal Revenue Code through January 1, 1984. Deductibility of contributions to this organization is subject to the normal limitations set forth under section 170 for this period. Commencing January 2, 1984, a court has determined that the organization is no longer described in section 170(c)(2), as more particularly set forth in section 7428(c)(1). Protection under section 7428(c) has terminated effective on the dated indicated.

March 10, 1986

Carolinas Hospital and Health Services, Inc., Charlotte, NC

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Robert Allen Beamer	Wauwatosa, WI	Attorney	Indefinite from February 19, 1986
Robert L. Cummings	Springfield, MO	Certified Public Accountant	Indefinite from February 27, 1986
Louis Crown	Bayside, NY	Certified Public Accountant	Indefinite from March 14, 1986
David H. Heilman	Council Grove, KS	Attorney	Indefinite from March 14, 1986
Beryl W. Markwell	Elmhurst, IL	Certified Public Accountant	Twenty-four Months from March 20, 1986
Marc Pozner	Tenafly, NJ	Certified Public Accountant	Indefinite from March 14, 1986
A. Russel Lucid	Norwell, MA	Attorney	Indefinite from March 26, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before their Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Thomas G. Abernethy, Jr.	Jackson, MS	Attorney	March 7, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.103-10, amended.	Definition of "principal user".	1986-12 I.R.B. 19	Apr. 22, 1986
26 CFR 1.103-10, revised.	$40 million limitation on beneficiaries of certain tax-exempt bonds	1986-12 I.R.B. 22	Apr. 22, 1986

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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______	1930-2	10.00
______	_1931-1_	_4.00_
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______	1932-2	10.00
______	_1933-1_	_3.75_
______	_1933-2_	_4.00_
______	_1934-1_	(**)
______	1934-2	15.00
______	1935-1	8.00
______	_1935-2_	_15.00_
______	_1936-1_	_4.00_
______	_1936-2_	_15.00_
______	_1937-1_	_14.00_
______	1937-2	8.50
______	_1938-1_	_17.00_
______	_1938-2_	_14.00_
______	1939-1-1	9.50
______	1939-1-2	12.00
______	1939-2	10.00
______	1940-1	6.50
______	1940-2	15.00
______	1941-1	8.00
______	_1941-2_	_4.00_
______	1942-1	8.00
______	_1942-2_	_6.50_
______	_1943-(*)_	_11.00_
______	_1944-(*)_	_9.00_
______	1945-(*)	10.00
______	_1946-1_	_3.00_
______	1946-2	6.00
______	_1947-1_	_2.00_
______	1947-2	3.75
______	_1948-1_	_3.50_
______	1948-2	8.50
______	_1949-1_	_8.00_
______	_1949-2_	_3.25_
______	1950-1	7.00
______	_1950-2_	_5.50_
______	_1951-1_	_13.00_
______	_1951-2_	_6.00_
______	_1952-1_	_3.00_
______	1952-2	8.00
______	_1953-1_	_4.75_
______	1953-2	13.00
______	1954-1	13.00
______	1954-2	13.00
______	1955-1	11.00
______	1955-2	14.00
______	1956-1	17.00
______	1956-2	20.00
______	1957-1	18.00
______	1957-2	(**)
______	1958-1	11.00
______	1958-2	(**)
______	1958-3	17.00
______	1959-1	19.00
______	1959-2	11.00
______	1960-1	21.00
______	1960-2	13.00
______	1961-1	15.00
______	1961-2	11.00
______	1962-1	15.00
______	1962-2	14.00
______	1962-3	22.00
______	1963-1	10.00
______	1963-2	12.00
______	1964-1-1	11.00
______	1964-1-2	12.00
______	1964-2	28.00
______	1965-1	19.00
______	1965-2	13.00
______	1966-1	15.00
______	1966-2	15.00
______	1967-1	11.00
______	1967-2	17.00
______	1968-1	15.00
______	1968-2	13.00
______	1969-1	15.00
______	1969-2	7.50
______	1969-3	14.00
______	1970-1	12.00
______	1970-2	(**)
______	1971-1	12.00
______	1971-2	17.00
______	1972-1	15.00
______	1972-2	15.00
______	1973-1	18.00
______	1973-2	15.00
______	1974-1	12.00
______	1974-2	11.00
______	_1974-3_	_9.50_
______	1974-3 Supp.	11.00
______	1975-1	15.00
______	1975-2	14.00
______	1976-1	12.00
______	1976-2	11.00
______	1976-3-1	10.00
______	1976-3-2	18.00
______	1976-3-3	11.00
______	1977-1	12.00
______	1977-2	13.00
______	1978-1	13.00
______	1978-2	14.00
______	1978-3-1	13.00
______	1978-3-2	9.50
______	1979-1	15.00
______	1979-2	17.00
______	1980-1	17.00
______	1980-2	19.00
______	1980-3	11.00
______	1981-1	19.00
______	1981-2	18.00
______	1982-1	17.00
______	1982-2	12.00
______	1983-1	21.00
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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

SPECIAL ANNOUNCEMENT

Announcement 86-57, page 34.
A public hearing will be held on May 22, 1986, on proposed regulations relating to limitations on an employee's right to receive alternative forms of benefit under qualified plans.

INCOME TAX

Rev. Rul. 86-63, page 6.
Charitable contribution; athletic scholarship program. Guidelines concerning whether payments to athletic scholarship programs are charitable contributions under section 170 of the Code when the payments afford the right to purchase preferred seating at a university's home football games. Rev. Rul. 84-132 is clarified, distinguished, and superseded.

T.D. 8078, page 22.
LR-66-85, page 32.
Temporary and proposed regulations under section 6111 of the Code relate to tax shelter registration.

Notice 86-5, page 30.
Merchant Marine Act; capital construction fund; interest rate. The applicable interest rate on the amount of additional tax attributable to any nonqualified withdrawals from a capital construction fund established under section 607 of the Merchant Marine Act is 13.32 percent for withdrawals made in taxable years beginning in 1985.

Notice 86-6, page 31.
Nonconventional source fuel credit; inflation adjustment factor and reference price. In determining the availability of the tax credit for production of fuel from nonconventional sources for the calendar year 1985, the inflation adjustment factor to be used is 1.4211 and the reference price to be used for qualified fuels is $24.08.

Finding Lists begin on page 40.
Announcement Relating to Decisions of the Tax Court on page 5.
Announcement of Disbarments and Suspensions begin on page 36.
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Department of the Treasury
Internal Revenue Service

T22.23:

EXEMPT ORGANIZATIONS

T.D. 8075, page 7.
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Announcement 86-54, page 32.
A list is given of organizations now classified as private foundations.

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Charitable remainder annuity trust; guaranteed annuity; partial interest; assignment of noncharitable interest. The transfer by the grantor life-interest beneficiary and the successive life-interest beneficiary of their annuity interests in a charitable remainder annuity trust to the charitable beneficiary qualifies for the charitable deductions under sections 170 and 2522 of the Code.

EXCISE TAXES

Rev. Rul. 86-61, page 11.
Bow and arrow components; native Indian handicraft. Bow and arrow component parts may not be sold tax free under sections 4221(a)(1) and 4221(d)(6)(A) of the Code for use in the production of bows and arrows as articles of native Indian handicraft by Indian tribes. Rev. Rul. 77-90 distinguished.

Rev. Rul. 86-62, page 12.
Highway use tax; vehicles registered in Canada distinguished. Effective July 1, 1985, highway use tax does not apply to Canadian trucks that are registered in British Columbia and have prorate licenses under the Uniform Vehicle Registration and Reciprocity Agreement. Rev. Rul. 81-86 revoked effective for periods beginning after June 30, 1985.

T.D. 8076, page 13.
Amendments to the regulations under sections 4988 and 4996 of the Code relate to the rules applicable to a net profits interest for purposes of the windfall profit tax on domestic crude oil.

ADMINISTRATIVE

Rev. Proc. 86-21, page 29.
Tip rate allocation; employers and employees; large food and beverage establishments. Guidance is provided to both employers and employees of certain large food and beverage establishments who want to petition the district director for a reduction in the tip rate allocation figure from 8 percent of the gross receipts to a figure

(Continued on page 4)

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Internal Revenue
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Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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not below 2 percent. Rev. Proc. 85-4, as modified by Rev. Proc. 85-10, is amplified and superseded.

T.D. 8079, page 24.

Temporary regulations under section 6867 of the Code relate to illegal activity cash.

T.D. 8080, page 25.

Amendments to the regulations under section 7701 of the Code relate to the classification of investment trusts with multiple classes of ownership.

T.D. 8081, page 17.

Amendments to the regulations under section 6011 of the Code relate to returns required to be filed on magnetic media.

Announcement 86-56, page 34.

All international functions within the Office of Chief Counsel have been consolidated into the Office of Associate Chief Counsel (International) effective March 17, 1986.

Announcement 86-58, page 35.

Effective dates are provided for Rev. Ruls. 86-7 and 86-8.

Announcement Relating to Decisions of the Tax Court

It is the policy of the Internal Revenue Service to announce in the Internal Revenue Bulletin at the earliest practicable date the determination of the Commissioner to acquiesce or not acquiesce in a decision of the Tax Court which disallows a deficiency in tax determined by the Commissioner to be due.

Notice that the Commissioner has acquiesced or nonacquiesced in a decision of the Tax Court relates only to the issue or issues decided adversely to the Government.

Actions of the acquiescense in adverse decisions shall be relied on by Revenue officers and others concerned as conclusions of the Service only to the application of the law to the facts in the particular case. Caution should be exercised in extending the application of the decision to a similar case unless the facts and circumstances are substantially the same, and consideration should be given to the effect of new legislation, regulations, and rulings as well as subsequent court decisions and actions thereon.

Acquiescence in a decision means acceptance by the Service of the conclusion reached, and does not necessarily mean acceptance and approval of any or all of the reasons assigned by the Court for its conclusions.

No announcements are made in the Bulletin with respect to memorandum opinions of the Tax Court.

The announcements published in the weekly Internal Revenue Bulletins are consolidated semiannually and annually. The semiannual consolidation appears in the first Bulletin for July and in the Cumulative Bulletin for the first half of the year and the annual consolidation appears in the first Bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner ACQUIESCES in the following decisions:

Taxpayer	Docket No.	Report	
		Volume	Page
Allied Industrial Cartage Co.[1]	7918-77	72	515
Commercial Security Bank[2]	5652-79	77	145
Goldsboro Arts League, Inc.[3]	8060-80X	75	337
McIntosh, John[4]	21618-81	85	31
Schwartz, Est. of Henry K., Robert Schwartz, Suzanne Schwartz & Mark Stewart, administrators[5]	17918-82	83	943

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[1] Acquiescence relating to whether the rental income received by petitioner from the lease of real estate and trucks to a brother-sister corporation, which is also 100 percent owned by petitioner's sole shareholder, constitutes an amount received as compensation for the right to use corporate property by a shareholder under section 543(a)(6) of the code.

[2] Acquiescence relating to whether Orem State Bank is entitled to deduct accrued but unpaid business liabilities on its final corporate income tax return.

[3] Acquiescence relating to where petitioner, a multifaceted cultural arts and educational organization, operates two art galleries to exhibit and sell the original works of individual artists, whether these operations disqualify petitioner as an organization described in section 501(c)(3) of the Code because operated for a substantial commercial purpose or to serve the private interests of the artists.

[4] Acquiescence relating to whether petitioner's transfer of an undivided one-half interest in ranchland to his former wife, pursuant to a property settlement agreement executed in connection with their divorce, constitutes a taxable disposition.

[5] Acquiescence relating to whether a foreign death tax credit under section 2014 of the Code is allowable when the estate of a U.S. citizen, resident of a foreign country, pays death taxes to that foreign country attributable to a bank account located in that foreign country.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 170.—Charitable, etc., Contributions and Gifts

26 CFR 1.170A-1: Charitable, etc., contributions and gifts, allowance of deduction.

Charitable contribution; athletic scholarship program. Guidelines concerning whether payments to athletic scholarship programs are charitable contributions under section 170 of the Code when the payments afford the right to purchase preferred seating at a university's home football games. Rev. Rul. 84-132 is clarified, distinguished, and superseded.

Rev. Rul. 86-63

ISSUE

Whether payments to athletic scholarship programs are charitable contributions under section 170 of the Internal Revenue Code in situations where the payments afford the right to purchase preferred seating at football games.

FACTS

Situation 1. Taxpayer *A*, an individual, made a payment of $300 to a particular athletic scholarship program maintained by a university, an organization described in section 170(c)(2) of the Code. A minimum payment of $300 is required to become a "member" of the program. The only benefit afforded members is that they are permitted to purchase, by paying the stated price of $120, a season ticket to the university's home football games in a designated area in the stadium. Because the games are regularly sold out well in advance, tickets to the games covered by the season ticket would not have been readily available to *A* if *A* had not made the payment to the program. The $300 membership fee is paid annually, and a member is required to make a separate $300 payment for each season ticket the member purchases. The university did not inform its donors of the fair market value of the right to purchase a season ticket in the designated area.

Situation 2. The facts are the same as in *Situation 1* except that taxpayer *B*, an individual, made a payment of $500 to the program, even though only a $300 payment is required to become a "member" of the program. The additional $200 did not result in any benefit to *B* other than that afforded members who paid $300.

Situation 3. Taxpayer *C*, an individual, made a payment of $300 to an athletic scholarship program of a university, an organization described in section 170(c)(2). This payment entitled *C* to become a "member" of the program and, as a member, to purchase a season ticket, for an additional payment of the stated price, in a designated area in the stadium. Tickets are offered to members before season tickets go on sale to the public. Seating reasonably comparable to that available to *C* as a result of membership in the program would have been readily available to *C* even if *C* had not made the payment to the program.

Situation 4. Taxpayer *D*, an individual, made a payment of $300 to an athletic scholarship program of a university, an organization described in section 170(c)(2). This payment entitled *D* to become a "member" of the program and, as a member, to purchase a season ticket to the university's home football games, for an additional payment of the stated price, in a designated area of the stadium. The membership fee is paid annually and a member is required to make a separate $300 payment for each season ticket the member purchases. Although the games are not regularly sold out, seating reasonably comparable to that available to *D* as a result of membership in the program would not have been readily available to *D* if *D* had not made the payment to the program. The university reasonably estimated that the fair market value of the right to purchase a season ticket in the designated area of the stadium would be x dollars, and advised prospective members that the additional [$300 − x dollars] was being solicited as a contribution. In making the estimate, the university considered the level of demand for tickets, the general availability of seats, the relative desirability of seats based on their types, locations, and views, and other relevant factors.

LAW AND ANALYSIS

Section 170(a) of the Code allows, subject to certain limitations, a deduction for contributions and gifts to or for the use of organizations described in section 170(c), payment of which is made within the taxable year.

A contribution for purposes of section 170 of the Code is a voluntary transfer of money or property that is made with no expectation of procuring financial benefit commensurate with the amount of the transfer. *See* section 1.170A-1(c)(5) of the Income Tax Regulations and H.R. Rep. No. 1337, 83d Cong., 2d Sess. A44 (1954).

Rev. Rul. 67-246, 1967-2 C.B. 104, sets forth various examples concerning the deductibility, as charitable contributions under section 170 of the Code, of payments made by taxpayers in connection with admission to or other participation in fund-raising activities for charitable organizations. The revenue ruling provides that to be deductible as a charitable contribution for federal income tax purposes under section 170, a payment to or for the use of a qualified charitable organization must be a gift. No gift exists for such purposes unless, among other requirements, there is a payment of money or transfer of property without adequate consideration. Where consideration in the form of substantial privileges or benefits is received in connection with payments by patrons of fund-raising activities, there is a presumption that the payments are not gifts. *See also* Rev. Rul. 76-185, 1976-1 C.B. 60.

Rev. Rul. 67-246 explains that, if a charitable contribution deduction is claimed with respect to a payment for which such consideration is received, the burden is on the taxpayer to establish that the amount paid is not the purchase price of the privileges or benefits and that part of the payment, in fact, does qualify as a gift. In showing that a gift has been made, it is essential for the taxpayer to establish that the portion of the payment that is claimed as a gift represents the excess of the total amount paid over the fair market value of any substantial privileges or benefits received in return.

Rev. Rul. 67-246 states that, if payments solicited for a charitable fund-raising activity are designed to be partly a gift and partly the purchase price of certain privileges or benefits, the organization conducting the activity should employ procedures that make clear not only that a gift is being solicited in connection with the activity, but also the amount of the gift being solicited. To do this, the amount properly attributable to the purchase of privileges or benefits and the amount solicited as a gift should be determined in advance of solicitation. In making such a determination, the fair market value of any substantial privileges or benefits attributable to the purchase must be taken into account. After making such a determination the charitable organization should notify its donors of the amounts allocable to each component of the payment.

In the four situations described above taxpayers made payments to athletic scholarship programs of organizations described in section 170(c)(2). Each taxpayer's payment entitled the taxpayer to become a member of an athletic scholarship program. The taxpayer has made a charitable contribution only if, and only to the extent that, the payment made exceeded the value of any substantial privileges or benefits afforded by membership in the program.

HOLDING

In *Situations 1* and *2*, because tickets to the games covered by the season ticket would not otherwise have been readily available to *A* and *B*, the right to purchase a season ticket in a designated area in the stadium was a substantial benefit. This substantial benefit was afforded to *A* and *B* because each paid the minimum membership fee of $300. Accordingly, a presumption arises that the $300 reflects the value of the benefit received. Unless the taxpayer can establish that $300 exceeded the value of the benefit received, no part of the $300 payment is a charitable contribution under section 170 of the Code.

In *Situation 2*, however, the additional $200 contributed by *B* resulted in no additional substantial benefit and thus, is a charitable contribution.

In *Situation 3*, although the taxpayer was entitled to purchase a ticket before tickets went on sale to the public and although the ticket was for seating in a designated area, reasonably comparable seating would have been readily available to *C* even if *C* had not made a payment to the program. Although *C* received the benefit of obtaining a ticket early and of sitting with other program members, the benefit was not substantial. Accordingly, the entire $300 is a charitable contribution.

In *Situation 4*, because reasonably comparable seating would not otherwise have been readily available to *D*, the right to purchase a season ticket in a designated area in the stadium was a substantial benefit. This substantial benefit was afforded to *D* because *D* paid the minimum membership fee of $300. Accordingly, a presumption arises that the $300 reflects the value of the benefit received. The university, however, after taking all relevant facts and circumstances into account, reasonably estimated the fair market value of the benefit as *x* dollars. Because the university solicited the other [$300 − *x* dollars] as a contribution and the *x* dollar figure reflected the fair market value of the benefit provided, [$300 − *x* dollars] of *D*'s $300 payment is a charitable contribution.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 84-132, 1984-2 C.B. 55, is clarified, distinguished, and superseded.

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26 CFR 1.170A-7: contributions not in trust of partial interests in property.

Whether the transfer by a grantor/life-interest beneficiary and the successive life-interest beneficiary to a charitable remainder annuity trust of their annuity interests in the trust qualifies for a charitable deduction under section 170 of the Code. See Rev. Rul. 86-60, page 9.

Section 513.—Unrelated Trade or Business

26 CFR 1.513-6: Certain hospital services not related trade or business.

T.D. 8075

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1—INCOME TAX: TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Treatment of Certain Hospital Services

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the treatment of certain hospital services furnished by one tax-exempt hospital to other such hospitals. Changes to the applicable tax law were made by the Tax Reform Act of 1976. [Pub. L. 94-455, 1976-3 C.B. (Vol. 1)1] The regulations affect those tax-exempt hospitals that furnish the services, and would provide the furnishing hospitals with the guidance needed to determine their unrelated business taxable income.

DATES: The regulations apply to taxable years beginning after December 31, 1983, and are effective after December 31, 1953.

FOR FURTHER INFORMATION CONTACT: Calder L. Robertson, Jr., of the Employee Plans and Exempt Organizations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, (Attention: CC:LR:T:EE-46-78) (202-566-3544) (not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

On December 13, 1982, the Federal Register published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 513(e) of the Internal Revenue Code of 1954 (47 Fed. Reg. 55696) [EE-46-78, 1983-1 C.B. 805]. These proposed amendments conform the regulations to section 1311 of the Tax Reform Act of 1976 (90 Stat. 3526). The regulations are issued under the authority contained in section 513(e) and in section 7805(b) of the Internal Revenue Code of 1954 (90 Stat. 3526, 68A Stat. 917; 26 U.S.C. 513(e), 7805). There was only one request for a public hearing. No public hearing was held because the request was withdrawn. After consideration of all written comments received, the regulations are adopted with minor clarification by this Treasury decision.

EFFECTIVE DATE

The regulations are effective for all taxable years beginning after December 31, 1953.

NON-APPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner has determined that this Treasury decision is not subject to review under Executive Order 12291. Therefore, a Regulatory Impact Analysis is not required.

REGULATORY FLEXIBILITY ACT

Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of this regulation is Charles K. Kerby, III, of the Employee Plans and Exempt Organizations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations, both on matters of substance and style.

PUBLIC COMMENTS

The public comments pertained to issues that were considered by the Internal Revenue Service prior to the publication of the notice of proposed rulemaking.

The majority of public comments considered the 100 inpatient limitation of section 513(e). It was suggested that the limitation was arbitrary, and should be increased or eliminated. The final regulations do not adopt this suggestion because the statute explicitly requires the limitation.

Many commentators sought to temper the rules under section 513(e) which treat a particular service as an unrelated trade or business if the service is provided at a fee above actual cost to even one hospital, or is provided to one hospital with facilities to serve more than 100 inpatients. The approaches suggested involved treating only the excess of fees over actual cost, or the fees from the services provided to hospitals with more than 100 inpatient facilities, as derived from an unrelated trade or business. The final regulations do not adopt these approaches. Treatment of only the services provided to more than 100 inpatient hospitals as an unrelated trade or business was deemed to contradict the wording of the statute under section 513(e)(1) which requires that services be provided "solely" to hospitals that have facilities to serve no more than 100 inpatients. Similarly, treatment of the excess of fees above actual costs as unrelated trade or business income was rejected because section 513(e)(3) specifically requires that services be provided at a fee not in excess of actual costs to escape treatment as an unrelated trade or business under section 513(e). We note that section 513 deals with the characterization of a service as an unrelated or related trade or business. The statute does not directly deal with the characterization of income, and does not address the fragmentation of income suggested. Therefore, if a service fails to meet the requirements of section 513(e)(3), the service is characterized under section 513(e) and the resulting treatment of income derived is governed by section 512.

Many commentators suggested that the regulations' reference to the reasonable cost and rate of return formulations prescribed by 42 U.S.C. 1395x(v)(1)(A) and (B) and the underlying regulations (permitting reimbursement to health care providers for reasonable costs including a reasonable return on equity capital in the Medicare program) was unwarranted. Some commentators felt that a "reasonable cost" fee standard, however determined, should not be adopted. Moreover, several commentators were concerned that many indirect costs of providing services would not be allowed in the Medicare determination of reasonable costs. These commentators generally felt the regulations should be silent on standards for determining fee levels.

After consideration of these comments, it was decided to retain the regulations' reference to the Medicare formulations as a safe harbor for use in complying with section 513(e). The wording of the statute in section 513(e)(3) requires that the services be provided at a fee or cost that *does not exceed* the actual cost of services, not provided *at* actual costs. The statute does not require actual cost fees. The nature of the fees subject to the actual cost limit is left unclear by the statute. The brief legislative history suggests strongly that Congress intended that section 513(e) operate to encourage cost savings to hospitals and their patients which implies a reasonable cost fee standard. S. Rep. No. 94-938, Part 2, 94th Cong., 2d Sess. 95 (1976). Further, the subsequent language of section 513(e)(3) which incorporates into actual costs reasonable allocations for depreciation (determined by the straight-line method) and a return on capital goods used (a reasonable rate of return) reinforces the reasonable cost fee standard adopted in the final regulations.

In addition, it was felt that a uniform standard for determining the fees or costs of services to be charged was necessary in the final regulations. Moreover, after examination of the Medicare regulations and consultation with Social Security Administration officials, it was determined that most direct and indirect costs are included in the determination of reasonable cost of services under the Medicare regulations. Further, it was determined that the cost records kept under the reimbursement method of repayment for Medicare providers would still be necessary under the new prospective payment method for Medicare providers. Thus, no additional recordkeeping would be required to demonstrate compliance with section 513(e).

Although the proposed regulations referred to the rate of return for equity capital in the Medicare regulations, it was not clear that the rate for section 513(e) purposes should change with any corresponding change in rate prescribed in the Medicare regulations. Therefore, the regulations are clarified to indicate that the safe harbor rate of return on equity capital is the rate prescribed in the regulations under 42 U.S.C. 1395x(v)(1)(A) and (B). The rate of return was lowered for periods after April 20, 1983, by a change to the Medicare regulations in October 1984. Concern was expressed over the fairness of applying the lower rate of return for periods before, the regulations are also clarified to make the lower rate applicable only for taxable years beginning 90 days after publication of the final regulations.

Several commentators suggested that the final regulations clarify that the failure of a hospital service under section 513(e) to qualify for the exception from treatment as an unrelated trade or business does not preclude a showing based on all the facts and circumstances that the service provided to one or more hospitals is substantially related to the providing hospital's exempt purpose. Treas. Reg. §1.513-1(d). Nothing in the final regulations precludes a hospital from making the requisite showing under section 1.513-1(d) based on all the facts and circumstances. However, the Service has generally taken the position that the provision of commercially available services by an exempt hospital to other unrelated exempt hospitals is an unrelated trade or business. *See* Rev. Rul. 69-633, 1969-2 C.B. 121. Thus, absent a showing of special facts that indicate the provision of such a service to other unrelated hospitals is substantially related to the providing hospital's exempt purpose (other than through the production of needed income), the provision of such services to other unrelated hospitals will generally be deemed an unrelated trade or business. For these reasons, it was decided to reject any revision of the final regulations that implied as a general and practical matter a contrary result. As noted before, nothing in the final regulations precludes a special showing under section 1.513-1(d).

* * * * *

Adoption of amendments to the regulations

Accordingly, the proposed amendments to 26 CFR Part 1 are hereby adopted as clarified by this Treasury decision.

Amendments to the Regulations

1. These amendments to Part 1 are issued under the authority contained in 26 U.S.C. 7805. The authority citation for Part 1 is unchanged.

2. 26 CFR Part 1 is proposed to be amended by adding the following new §1.513-6 in the appropriate place:

PART 1—[AMENDED]

§1.513-6 Certain hospital services not unrelated trade or business.

(a) *In general.* Under section 513(e), the furnishing of a service listed in section 501(e)(1)(A) by a hospital to one or more other hospitals will not constitute unrelated trade or business if—

(1) The service is provided solely to hospitals that have facilities to serve not more than 100 inpatients,

(2) The service would, if performed by the recipient hospital, constitute an activity consistent with that hospital's exempt purposes, and

(3) The service is provided at a fee not in excess of actual cost, including straight line depreciation and a reasonable rate of return on the capital goods used to provide the service. For purposes of this section, a rate of return on capital goods will be considered "reasonable" provided that it does not exceed, on an annual basis, the percentage described below which is based on the average of the rates of interest on special issues of public debt obligations issued to the Federal Hospital Insurance Trust Fund for each of the months included in the taxable year of the hospital during which the capital goods are used in providing the service. Determinations as to the cost of services and the applicable rate of return should be made as prescribed by 42 U.S.C. 1395x(v)(1)(A) and (B) and the regulations thereunder (permitting a health care facility to be reimbursed under the Medicare program for the "reasonable cost of [its] services," including, in the case of certain proprietary facilities, a "reasonable return on equity capital"). For taxable years beginning on or before [90 days after publication of this regulation in the Federal Register] the rate of return shall be one and one-half times the average of the rates of interest on public debt obligations described above which were in effect on or before April 20, 1983.

(b) *Hospital defined.* As used in this section the word "hospital" means a hospital described in section 170(b)(1)(A)(iii).

(c) *Example.* The provisions of this section are illustrated by the following example:

Example. A large metropolitan hospital provides various services to other hospitals. The hospital furnishes a purchasing service to hospitals N and O, a data processing service to hospitals R and S, and a food service to hospitals X and Y. All the hospitals are described in section 170(b)(1)(A)(iii). All the hospitals have facilities to serve not more than 100 inpatients except hospital N. The services are furnished at cost to all hospitals except that hospital R is charged a fee in excess of cost for its use of the data processing service. The purchasing service constitutes unrelated trade or business because it is not provided solely to hospitals having facilities to serve not more than 100 inpatients.

The data processing service constitutes unrelated trade or business because it is provided at a fee in excess of cost. The food service satisfies all three requirements of paragraph (a) of this section and does not constitute unrelated trade or business.

(d) *Effective date.* Section 513(e) and this section apply to taxable years beginning after December 31, 1953.

The Treasury Decision is issued under the authority contained in sections 513(e) and 7805 of the Internal Revenue Code of 1954 (90 Stat. 1729 68A Stat. 917; 26 U.S.C. 513(e), 7805).

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved January 21, 1986.

J. Roger Mentz,
Acting Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on February 12, 1986, 8:45 a.m., and published in the issue of the Federal Register for February 13, 1986, 51 F.R. 5320)

Section 664.—Definitions

26 CFR 1.664-2: Charitable remainder annuity trust.

Whether the transfer of an annuity interest in a charitable remainder annuity trust by a grantor/life-interest beneficiary to the charitable beneficiary is a transfer to a permissible recipient under section 664 of the Code. See Rev. Rul. 86-60, below.

Section 2522.—Charitable and Similar Gifts

26 CFR 25.2522(c)-3: Transfers not exclusively for charitable, etc., purposes in the case of gifts made after July 31, 1969.
(Also Sections 170, 664; 1.170A, 1.664-2.)

Charitable remainder annuity trust; guaranteed annuity; partial interest; assignment of noncharitable interest. The transfer by the grantor life-interest beneficiary and the successive life-interest beneficiary of their annuity interests in a charitable remainder annuity trust to the charitable beneficiary qualifies for the charitable deductions under sections 170 and 2522 of the Code.

Rev. Rul. 86-60

ISSUE

Under the circumstances described below, if the grantor/life-interest beneficiary and the successive life-interest beneficiary of a charitable remainder annuity trust donate their annuity interest in the trust to the charitable remainder beneficiary, do the donations qualify for the charitable deductions under sections 170 and 2522 of the Internal Revenue Code?

FACTS

Situation 1. In 1980, *A* created a charitable remainder annuity trust (hereinafter, CRAT) described in section 664(d)(1) of the Code. *A* retained the annuity interest in the trust for life. The remainder beneficiary was *X*, a charitable organization described in sections 170(c) and 2522(a). In 1984 *A* transferred the annuity interest in the trust to *X*.

Situation 2. In 1980, *A* created a CRAT described in section 664(d)(1) of the Code. The trust instrument provides that the trustee shall pay the annuity amount annually to *A* for life and upon *A*'s death to *B*, the successive life interest beneficiary, for such time as *B* survives. Upon the death of the survivor of *A* and *B*, the corpus is to be distributed to *X*, a charitable organization that meets the requirements of sections 170(c) and 2522(a). In 1984, *A* and *B* assigned their interests in the trust to the charitable remainder beneficiary.

No property interests were created for the purpose of avoiding the rules of section 170(f)(2) and (f)(3)(A).

LAW AND ANALYSIS

Section 170(a)(1) of the Code allows as an income tax deduction any contribution or gift to or for the use of organizations described in section 170(c), payment of which is made within the taxable year.

Section 170(f)(2)(B) of the Code provides that no charitable contribution deduction is allowed for the value of any interest in property (other than a remainder interest) transferred in trust unless the interest is in the form of a guaranteed annuity or a fixed percentage distributed annually of the fair market value of the trust property, determined annually, and the grantor is treated as the owner of the interest for purposes of applying section 671 (relating to grantor trusts).

Section 170(f)(3)(A) of the Code provides that a contribution (not made by a transfer in trust) of less than the taxpayer's entire interest in property is not allowed as a charitable deduction except to the extent such contribution would have been allowed as a deduction had it been transferred in trust.

Sections 1.170A-6(a)(2) and 1.170A-7(a)(2)(i) of the Income Tax Regulations provide that a deduction is allowed for a contribution of a partial interest in property if such interest is the taxpayer's entire interest in the property, such as an income interest or a remainder interest. If, however, the property in which such partial interest exists was divided in order to create such interest and thus avoid the rules of section 170(f)(2) and (f)(3)(A), the deduction is not allowed.

Section 1.170A-1(c)(1) of the regulations provides that, if a charitable contribution is made in property other than money, the amount of the contribution is generally the fair market value of the property at the time of the contribution.

Section 2501 of the Code imposes a tax on the transfer of property by gift. The gift tax applies, under section 2511, to all transfers by gift, whether the transfer is in trust or otherwise, and whether the gift is direct or indirect.

Section 2522 of the Code provides for a gift tax charitable deduction for the value of property transferred to organizations described in section 2522(a).

However, section 2522(c)(2) of the Code and section 25.2522(c)3-(c)(1) and (2) of the Gift Tax Regulations provide that if a donor transfers an interest in property for charitable purposes and an interest in the same property is retained by the donor, or is transferred or has been transferred (for less than adequate and full consideration) for private purposes, no gift tax deduction is allowed under section 2522 unless the charitable interest is:

(A) an undivided portion of the donor's entire interest,

(B) a remainder interest in a personal residence,

(C) a remainder interest in a farm,

(D) a remainder interest in a charitable remainder trust or a pooled income fund,

(E) a guaranteed annuity interest,

(F) a unitrust interest, or

(G) a qualified conservation contribution.

A guaranteed annuity interest is an irrevocable right to receive a determinable amount periodically, but not less often than annually, for a specified term or for the life or lives of a named individual or individuals, each of whom is living and identifiable at the date of the gift. Section 1.170A-6(c)(2)(i) of the Income Tax Regulations and section 25.2522(c)-3(c)(2)(v) of the Gift Tax Regulations.

Section 1.170A-1(e) of the Income Tax Regulations and section 25.2522(c)-3(b) of the Gift Tax Regulations provide that if, as of the date of the gift, a transfer for charitable purposes is dependent upon the performance of some act or the happening of a precedent event in order that it might become effective, no deduction is allowable unless the possibility that the charitable transfer will not become effective is so remote as to be negligible.

In *Situation 1*, in 1984 *A* transferred *A*'s entire life annuity interest to *X* charity, an organization described in section 170(c) of the Code. Although *A* had previously divided the interest *A* held in the property, the division was not to avoid section 170(f)(2)(A). Thus, under section 1.170A-7(a)(2)(i), *A*'s transfer of *A*'s entire life annuity interest qualifies for an income tax charitable deduction.

A's transfer also qualifies for a gift tax charitable deduction. Following the 1984 transfer, *A* did not retain any interest in the trust, and neither at that time nor at any prior time did *A* make a transfer from the trust for private purposes. Although the transfer of the remainder interest to *X* divided *A*'s prior interest, that transfer was for charitable, not private purposes. Consequently, in order to qualify for a gift tax charitable deduction, *A*'s 1984 transfer to *X* need not be in a form described in section 2522 of the Code and section 25.2522(c)-3(c)(2) of the regulations. Accordingly, *A*'s transfer of the life annuity interest to *X* qualifies for a gift tax deduction under section 2522 of the Code.

In *Situation 2*, *A* transferred to *X* charity *A*'s life annuity interest in 1984. The life annuity interest was the only interest in the charitable remainder annuity trust that *A* owned at the time of the transfer. Although *A* had previously divided the interest *A* held in the property, that division was not to avoid section 170(f)(3)(A). Thus, under section 1.170A-7(a)(2)(i) of the regulations, *A*'s transfer of *A*'s entire life annuity interest qualifies for an income tax deduction.

Further, in 1984, *B* transferred to *X* charity *B*'s secondary life annuity interest, the only interest in the charitable remainder trust that *B* ever owned. Therefore, under section 1.170A-7(a)(2)(i) of the regulations, *B*'s transfer of *B*'s entire secondary life annuity interest qualifies for an income tax deduction.

The transfers by *A* and *B* also qualify for the gift tax charitable deduction. *A* made a completed gift under section 2511 of the Code to *B* of the secondary life annuity interest in the trust in 1980. Because *A* made a completed gift in the trust to a noncharitable beneficiary, the restrictions in section 2522(c)(2) apply. Thus, *Situation 2* differs from *Situation 1*. In *Situation 2* no gift tax deduction is allowed for *A*'s 1984 transfer to *X* of *A*'s life interest in the trust unless it is described in section 25.2522(c)-3(c)(2) of the regulations. Because *A*'s 1984 transfer to *X* is of a right to receive a fixed amount annually for the life of *A* and qualifies as a guaranteed annuity, it is a transfer of a guaranteed annuity interest as described in section 25.2522(c)-3(c)(2)(v). Consequently, the gift qualifies for a gift tax charitable deduction under section 2522.

Further, *B* has made a completed gift under section 2522 of the Code of *B*'s secondary life annuity interest in the trust in 1984. Following this transfer, *B* did not retain any interest in the trust, and at no time had *B* made a transfer of an interest in the trust for a private purpose. Consequently, there is no requirement that *B*'s 1984 transfer to *X* be in one of the forms set out in section 25.2522(c)-3(c)(2) of the regulations in order to qualify for a gift tax charitable deduction. Thus, *B*'s transfer of the secondary life annuity interest to *X* in 1984 qualifies for a gift tax reduction under section 2522.

Sections 1.170A-1(e) and 25.2522(c)-3(b) of the regulations are not applicable to the transfer of these annuities because, immediately after *A* and *B* transferred their respective annuity interests to charity, the interests transferred were not in any way dependent upon the happening of an event or a condition precedent in order that the interests might become effective.

HOLDINGS

In *Situation 1*, the gift by *A*, the grantor, to the remainder beneficiary of *A*'s retained life annuity interest in a charitable remainder annuity trust qualifies for an income tax charitable deduction under section 170 of the Code and a gift tax charitable deduction under section 2522.

In *Situation 2*, where *A* has created a charitable remainder annuity trust with life annuity interest to *A* and survivor life annuity interest to *B*, the gifts by *A* and *B* of their life annuity interests in the trust to the charitable remainder beneficiary qualify for an income tax charitable deduction and a gift tax charitable deduction. *A*'s gift of the life annuity, however, qualified for the gift tax charitable deduction only because the interest that was transferred was in one of the forms set out in section 25.2522(c)-3(c)(2) of the regulations.

Section 4161.—Imposition of Tax

26 CFR 48.4161(b)-1: Imposition and rates of tax; bows and arrows.

The excise tax imposed by section 4161(b)(2) of the Code applies to the sale of bow and arrow component parts to be used in the production of the bows and arrows by an Indian tribe. See Rev. Rul. 86-61, below.

Section 4221.—Certain Tax-Free Sales

26 CFR 48.4221-2: Tax-free sale of articles to be used for, or resold for further manufacture. (Also Sections 4161, 4225; 48.4161(b)-1, 48.4225-1.)

Bow and arrow components; native Indian handicraft. Bow and arrow component parts may not be sold tax free under sections 4221(a)(1) and 4221(d)(6)(A) of the Code for use in the production of bows and arrows as articles of native Indian handicraft by Indian tribes. Rev. Rul. 77-90 distinguished.

Rev. Rul. 86-61

ISSUE

May bow and arrow components be sold tax free under section 4221(a)(1) of the Internal Revenue Code for use in the manufacture by an Indian tribe of bows and arrows that, under section 4225, are exempt from manufacturers excise tax?

FACTS

A manufacturer sells to an Indian tribe various components used in the production of bows and arrows. Utilizing Indians working on an Indian reservation, the Indian tribe produces finished handicraft bows and arrows from the components. The finished bows qualify as native Indian handicraft. The Indian tribe then sells the completed bows and arrows.

LAW AND ANALYSIS

Section 4161(b)(1) of the Code, as amended by the Tax Reform Act of 1984, section 1017, 1984-3 (Vol. 1) C.B. 1, 529, imposes an 11 percent tax on the sale of certain bows and arrows by the manufacturer producer or importer. Section 4161(b)(2)(A) imposes an 11 percent tax on the sale by the manufacturer, producer or importer of parts and accessories suitable for inclusion in or attachment to a bow or arrow described in section 4161(b)(1).

Section 4221(a)(1) of the Code provides that no tax shall be imposed under section 4161 on the sale by the manufacturer of an article for use by the purchaser for further manufacture, or for resale by the purchaser to a second purchaser for use by such second purchaser in further manufacture.

Section 4221(d)(6)(A) of the Code states that an article shall be treated as sold for use in further manufacture if such article is for use by the purchaser as material in the manufacture or production of, or as a component part of, another article taxable under Chapter 32 of the Code to be manufactured or produced by that purchaser.

Section 4225 of the Code states, in pertinent part, that no tax shall be imposed under Chapter 32 on any article of native Indian handicraft manufactured or produced by Indians on Indian reservations.

Section 48.4225-1 of the Manufacturers and Retailers Excise Tax Regulations provides that the exemption under section 4225 of the Code applies to articles taxable under chapter 32 of the Code that are of native Indian handicraft and are manufactured or produced by Indians on Indian reservations.

Rev. Rul. 72-536, 1972-2 C.B. 573, concerns lubricating oil sold for use in the manufacture of light-duty trucks. Effective December 11, 1971, the manufactures excise tax previously imposed on those trucks was repealed. The ruling holds that, effective that date, lubricating oil could not be sold tax free under section 4221(a)(1) for use in the manufacture of those trucks, because they had ceased to be articles subject to the manufacturers excise tax.

Rev. Rul. 77-90, 1977-1 C.B. 334, concerns the sale by a manufacturer of tread rubber for use in the further manufacture of tires that are sold for export prior to any other use. The ruling holds that under section 4221(a)(1) of the Code the sale of the rubber for tire manufacture is exempt from the manufacturers excise tax and the subsequent sale of the tires for export is exempt from tax under section 4221(a)(2).

Section 4221(a)(1) of the Code exempts the sale of articles for further manufacture only if the article sold is to be used as material in the manufacture or production of, or as a component part of, "another article taxable under [chapter 32]." Section 4221(d)(6)(A). As a result of the effect of section 4225, however, qualifying articles of native Indian handicraft that are otherwise taxable under chapter 32 are to have no tax imposed on them under chapter 32. *See* section 48.4225-1 of the regulations. Such articles, therefore, are not taxable under chapter 32, and material or components sold for use in the production of articles of native Indian handicraft are not sold for use in the production of articles taxable under chapter 32. The sale of material and components for that use, therefore, is not exempt under section 4221(a)(1). *See* Rev. Rul. 72-536.

Although the tax on such a sale of material and components may be passed through in the form of higher prices to the producer of native Indian handicraft, the imposition of the tax on the sale does not subvert the purpose of section 4225 of the Code. Any subsequent sale by the producer of the handicraft is exempt from tax. Thus, in the present situation, the handicraft articles produced and sold by the tribe still enjoy an excise tax exemption to the extent that their value was contributed by the tribe's handiwork. It is that handiwork at which the policy of section 4225 is directed.

The present situation is distinguishable from that in Rev. Rul. 77-90. In Rev. Rul. 77-90 the sale of tread rubber by the manufacturer to a tire retreader was exempt from tax under section 4221(a)(1) of the Code as a sale for further manufacture. The retreader's subsequent sale of the tires for export, however, was exempt under section 4221(a)(2), which exempts the sale of any article for export. Tires themselves are normally taxable articles under chapter 32 of the Code. Thus, the exemption for sale for further manufacture of taxable articles applies to the sale of tread rubber to a tire retreader, notwithstanding the exemption of the later sale. In contrast, articles of native Indian handicraft are always tax exempt, regardless of their subsequent disposition, whether abroad or domestic. Accordingly, parts sold for the manufacture of native Indian handicraft are necessarily sold for the manufacture of an article that is not taxable under chapter 32. For this reason, the exemption under section 4221(a)(1) does not apply.

Furthermore the policy behind exempting from tax articles that are sold for export—to encourage United States exports—would not be served by exempting only the value contributed by the last manufacturer in a series of manufacturers. Because that policy is not concerned with who manufactured an article that is sold for export, there is no connection between the policy and the amount of value that is added by the last manufacturer. In contrast, here there is a relation between the policy behind section 4225 of the Code—to encourage Indian hand work—and the value contributed by the producer of native Indian handicraft, who is an Indian on a reservation.

The bows and arrows described above are article native Indian handicraft and, therefore, pursuant to section 4225 of the Code, are not subject to the manufacturers excise tax. Consequently, the sales of bow and arrow component parts to be used in the production of the bows and arrows by the Indian tribe may not be made tax free under section 4221(a)(1) since the parts are not sold for use in the manufacture of another article taxable under chapter 32.

HOLDING

The tax imposed by section 4161(b)(2) of the Code applies to the sale of bow and arrow component parts to Indians for use in the production of bows and arrows that are exempt from the manufacturers excise tax.

EFFECT ON OTHER
REVENUE RULINGS

Rev. Rul. 77-90 is distinguished.

Section 4225.—Exemption of Articles Manufactured or Produced by Indians

26 CFR 48.4225-1: Exemption of articles manufactured or produced by Indians.

Whether, as a result of the effect of section 4225 of the Code, qualifying articles (bows and arrows) of native Indian handicraft that are otherwise taxable under chapter 32 of the Code are exempt from tax. See Rev. Rul. 86-61, page 11.

Section 4481.—Imposition of Tax

26 CFR 41.4481-1: Imposition of tax.

Highway use tax; vehicles registered in Canada. Effective July 1, 1985, highway use tax does not apply to Canadian trucks that are registered in British Columbia and have prorate licenses under the Uniform Vehicle Registration and Reciprocity Agreement. Rev. Rul. 81-86 revoked effective for periods beginning after June 30, 1985.

Rev. Rul. 86-62

Section 41.4481-1(a)(2) of the Highway Use Tax Regulations, as amended by T.D. 8027, 1985-26 I.R.B. 6, concerns any highway motor vehicle that is issued a base plate by a Canadian province under the International Registration Plan (IRP) or similar agreement and has a proportional registration under such agreement to satisfy the registration laws of any of the United States. The section provides that for taxable periods beginning after June 30, 1985, these vehicles are exempt from the tax imposed by section 4481(a) of the Internal Revenue Code.

Rev. Rul. 81-86, 1981-1 C.B. 504, holds, effective July 1, 1981, that the highway use tax imposed by section 4481(a) of the Code applies to certain trucks. The trucks involved are those that are registered (base plated) in the Canadian province of British Columbia and that have "prorate licenses" under the Uniform Vehicle Registration Proration and Reciprocity Agreement (U.V.R.P.R.A.). A prorate license is a special license that, under the U.V.R.P.R.A., allows certain commercial fleet interstate vehicles to satisfy the registration laws of certain U.S. states.

The U.V.R.P.R.A is a reciprocal agreement similar to the IRP, and its prorate licensing constitutes a proportional registration in satisfaction of state laws. Thus, under section 41.4481-1(a)(2) of the regulations, effective July 1, 1985, a Canadian truck that is registered in British Columbia and has a prorate license under the U.V.R.P.R.A. is not subject to the highway use tax imposed by section 4481(a) of the Code.

Rev. Rul. 81-86 is therefore revoked, effective for taxable periods beginning after June 30, 1985.

In *Little Audrey's Transportation Co. v. United States,* 369 F.Supp 329 (D. Neb. 1974), *aff'd mem.*, 508 F.2d 846 (8th Cir. 1974), the court held that, under a reciprocal proration agreement similar to the U.V.R.P.R.A., prorate licensing did not constitute registration. Rev. Rul. 81-86 stated that the Internal Revenue Service would no longer follow the holding. Although Rev. Rul. 81-86 is now revoked, the Service will continue to not follow that holding.

Section 4988.—Windfall Profit; Removal Price

26 CFR 51.4988-2: Net income limitation on windfall profit.
(Also Section 4996; 51.4996-1.)

T.D. 8076

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER D, PART 51—EXCISE TAX REGULATIONS UNDER THE CRUDE OIL WINDFALL PROFIT TAX ACT OF 1980

Net Profits Interests

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final excise tax regulations relating to the rules applicable to a net profits interest for purposes of the windfall profit tax on domestic crude oil. Changes to the applicable law were made by sections 201(h) and 203(c) of the Technical Corrections Act of 1982 [Pub. L. 97-448, 1983-1 C.B. 451, 465, 467]. The regulations provide guidance for determining the portion of crude oil produced from the property attributable to the holder of a net profits interest. These regulations supersede §150.4996-1(b)(3) of the Temporary Excise Tax Regulations under the Crude Oil Windfall Profit Tax Act of 1980 [Pub. L. 96-223, 1980-3 C.B. 1], 26 CFR Part 150, for those net profits interests for which these regulations would be effective. Those temporary regulations remain in effect for those net profits interests for which these regulations are not effective (*e.g.*, a net profits interest established by an agreement entered into before April 1, 1982, which is held by a profit making corporation).

DATE: The amendments are effective generally with respect to net profits agreements entered into (or renewed) after March 31, 1982. However, in the case of a 90 percent or more net profits interest held by an exempt charity or exempt governmental interest, these amendments are effective with respect to crude oil removed after February 29, 1980. For purposes of determining the category of crude oil removed (or deemed removed) from the premises before April 1, 1986, the taxpayer may determine the category of all such oil by allocating it among all categories of crude oil in proportion to the production from that property in each such category that was removed (or deemed removed) from the premises during the calendar quarter immediately preceding the calendar quarter of production.

FOR FURTHER INFORMATION CONTACT: David R. Haglund of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3297).

SUPPLEMENTARY INFORMATION:

BACKGROUND

On August 29, 1984 ,the Federal Register published proposed amendments to the Excise Tax Regulations under the Crude Oil Windfall Profit Tax Act of 1980 (26 CFR Part 51) under sections 4988 and 4996 of the Internal Revenue Code of 1954 (49 FR 34242) [LR-38-82, 1984-2 C.B. 852]. The amendments were proposed to conform the regulations to sections 201(h) and 203(c) of the Technical Corrections Act of 1982. Two comments on the proposed amendments were received. A public hearing was not requested and one was not held. After consideration of all comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

EXPLANATION OF PROVISIONS

The windfall profit tax imposes a tax on the producer of domestic crude oil except exempt oil. Section 4996(a)(1)(A) provides that the term "producer" generally means the holder of an economic interest with respect to the crude oil. The holder of a net profits interest in a property is generally considered to hold an economic interest with respect to the crude oil. Under §150.4996-1(b)(3) of the Temporary Excise Tax Regulations under the Crude Oil Windfall Profit Tax Act of 1980 (promulgated before enactment of the Technical Corrections Act of 1982), the holder of a net profits interest was only treated as the producer of the number of barrels of crude oil equal to the net profits interest holder's share of net profits divided by the removal price of the crude oil. For example, if X received $120 as his share of net profits and the removal price of the crude oil was $30 per barrel, X was treated as the producer of four barrels of crude oil.

Section 201(h) of the Technical Corrections Act of 1982 amended the definition of "producer' in section 4996(a) to provide special rules for producers subject to a net profits interest agreement. These special rules provide that for windfall profit tax purposes the amount of crude oil equal in value to the cost of operating the property (cost recovery oil) will be treated as produced by the net profits interest holder and the person holding the interest burdened by the net profits interest in the same proportion as their respective shares of net profits. Section 201(h) of the Act also amends section 4988(b) by adding a new paragraph (6) which provides that for purposes of the net income limitation the expenses of producing the crude oil will be allocated in the same manner as the cost recovery oil. Thus, the holder of a 10 percent net profits interest is treated as the producer of 10 percent of the barrels of cost recovery oil produced and will be attributed 10 percent of the expenses of producing that crude oil.

In response to comments received the final regulations modify the notice of proposed rulemaking in several respects. One commentator expressed the view that cost recovery oil and other oil (oil attributable to profits) should be treated differently because, in its view, the amount of other oil is governed by the rules applicable for percentage depletion purposes and should be calculated accordingly. This suggestion was not adopted. The Act provided that cost recovery oil shall be treated as shared in the same proportion as other oil is shared under the net profits agreement. Thus, the Act recognizes that other oil is shared according to the sharing ratio in the net profits agreement. Although section 4996(a)(1)(B) only addresses the treatment of cost recovery oil (because the treatment of that oil before the statutory change was the principal cause of distortion in windfall profit tax liabilities), it clearly indicates that other oil and cost recovery oil are to be determined under the same rules. Accordingly, the final regulations emphasize that each barrel of crude oil production covered by a net profits agreement, including all cost recovery oil, shall be treated as produced by the parties to such agreement in proportion to the respective shares (determined after reduction for such cost recovery oil) of the production of the crude oil covered by such agreement.

The final regulations also clarify that state and local property and severance taxes are qualified costs, and point out that a provision in a net profits agreement that reduces net profits by windfall profit tax has no effect on windfall profit tax.

Another modification in the final regulations is made in response to comments that the proposed rule requiring that categories of oil be determined by reference to production in the preceding calendar quarter is unduly burdensome. The final regulations provide simply that a net profits interest holder is the producer of a fraction of each barrel produced. Accordingly, the holder of a net profits interest takes its share of all categories of oil and of all base prices and all removal prices. For oil removed or deemed removed from the premises before April 1, 1986, taxpayers may base categories of crude oil upon the proposed rule.

Commentators suggested that the cost recovery rules should not apply unless there are actual net profits under the agreement. Section 4996(a)(1)(B)(ii) provides that the cost recovery rules shall not apply before payout. Payout is the time at which the holder of the net profits interest is first entitled to income under the net profits agreement. Because of lower production levels or increased costs subsequent to payout the holder of the net profits interest may not be entitled to any net profits. However, the statutory provision relating to the inapplicability of the cost recovery rules before payout would not have been necessary if the cost recovery rules only applied when there are net profits. Therefore, the statute reflects an intention that once payout occurs the holder of a net profits interest is attributed a share of the cost recovery oil even if there are no net profits in such periods. Moreover, this position is consistent with Congressional intent as indicated by the following statement from the Senate report: "[The allocation of cost recovery oil] will be made beginning in the first taxable period with respect to which the owner or owners of the net profits interest receive a share of production remaining after cost recovery and for all taxable periods thereafter regardless of whether or not the property subsequently shows a loss." S. Rep. No. 97-592, 97th Cong., 2nd Sess. 43 (1982) [1983-1 C.B. 492].

SPECIAL ANALYSIS

The Commissioner of the Internal Revenue has determined that these final rules are not major rules as defined in Executive Order 12291. Accordingly, a regulatory impact analysis is not required.

Although a notice of proposed rulemaking which solicits public comments was issued, the Internal Revenue Service concluded that when notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, these final regulations do not constitute regulations subject to the Regulatory Flexibility act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these final regulations is David R. Haglund of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations.

Accordingly, 26 CFR Part 51 is amended as follows:

Paragraph 1. The authority for Part 51 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 51.4996-1(b)(3) is also issued under 26 U.S.C. 4996(a)(1)(B) and 26 U.S.C. 4996(h)(2).

Par. 2. Paragraph (c) of §51.4988-2 is amended by redesignating subparagraphs (4), (5), and (6) as (5), (6), and (7), respectively, and by inserting a new subparagraph (4) to read as set forth below.

§51.4988-2 Net income limitation on windfall profit.

* * * * *

(c) *Special rules.* * * *

(4) *Certain net profits interests.* (i) For purposes of determining the net income limitation under this section in the case of any person treated under paragraph (b)(3) of §51.4996-1 (relating to net profits interests) as the producer of any portion of cost recovery oil (within the meaning of §51.4996-1(b)(3)(iv)) covered by a net profits agreement (within the meaning of §51.4996-1(b)(3)(iii))—

(A) Such person (and only such person) shall include in its gross income from the property the gross income from such portion, and

(B) The qualified costs (within the meaning of §51.4996-1(b)(3)(v)) allocable to such portion shall be treated as paid or incurred by such person (and only by such person).

The determination of cost depletion under paragraph (b)(3) of this section shall be made with regard to the principles of paragraph (b)(3) of §51.4996-1. Thus, a person treated under that paragraph as the producer of any portion of cost recovery oil covered by a net profits agreement computes the cost depletion deduction allowable under paragraph (b)(3) of this section by using as the number of units sold that number of units which such person would have used for income tax purposes if such person's gross income from the property had included the gross income attributable to that portion of the cost recovery oil of which such person is treated as the producer.

(ii) The principles of this subparagraph may be illustrated by the following examples:

Example (1). B owns 100 percent of the working interest in Whiteacre. B's working interest is burdened by a 75 percent net profits interest held by C. The net profits agreement provides that the amount of net profits is determined by subtracting from gross income from the sale of crude oil or gas production from Whiteacre all payments to royalty holders and all operating expenses except the windfall profit tax. Whiteacre produces only taxable crude oil. For the taxable year, 20,000 barrels of crude oil are produced from Whiteacre and sold for $40 per barrel for a total of $800,00. Of this amount, $100,000 is paid to D for his ⅛ royalty interest ($40 × (20,000 × ⅛)). The operating expenses attributable to the production of the taxable crude oil (including state severance taxes) are $100,000. The net profits for the year are $600,000 ($800,000 (gross income) − ($100,000 (royalty payment + $100,000 (expenses). C is entitled to $450,000 ($600,000 × .75). Under §51.4996-1(b)(3), C is treated as the producer of 13,125 barrels of crude oil (20,000 × ⅞ × .75). Thus, for purposes of determining C's hypothetical cost depletion deduction allowable for the taxable year under paragraph (b)(3) of §51.4988-2, C would use the 13,125 barrels as his number of units sold and would attribute $75,000 of the costs ($100,000 × .75) to that production for purposes of calculating the net income limitation.

Example (2). Assume the same facts as example (1) except that the net profits agreement provides that he amount of net profits is reduced by the windfall profit tax. Because qualified costs as defined in §51.4996-1(b)(3)(v) do not include the windfall profit tax, the net profits interest holder's share of production attributable to his share of net profits under the agreement is determined without regard to any reduction in profits attributable to the windfall profit tax. The results are the same as in example (1).

(5) *Computation of the net income limitation for taxable year that includes March 1, 1980.* * * *

(6) *Election to capitalize qualified tertiary injectant expenses.* * * *

(7) *Computation of the net income limitation before October 27, 1981, under notice of proposed rulemaking.* * * *

* * * * *

Par. 3. Paragraph (b)(3) of §51.4996-1 is revised to read as follows:

§51.4996-1 Definitions.

* * * * *

(b) *Producer*. * * *

(3) *Certain net profits interests*—(i) *In general*. In the case of any property (within the meaning of paragraph (i) of this section), each barrel of crude oil production covered by a net profits agreement (within the meaning of paragraph (b)(3)(iii) of this section), including all cost recovery oil (within the meaning of paragraph (b)(3)(iv) of this section), shall be treated as produced by the parties to such agreement in proportion to the respective shares (determined after reduction for such cost recovery oil) of the production of the crude oil covered by such agreement. For example, the holder of a 5 percent net profits interest is the producer of 5 percent of each barrel of crude oil produced (both cost recovery oil and other oil) from the property burdened by the net profits interest. See example (1) of paragraph (b)(3)(viii) of this section. An economic interest in crude oil in place in the ground which is not a working interest (within the meaning of paragraph (d)(2) of §51.4992-1) without regard to this subparagraph shall not be considered a working interest by reason of the allocation of costs to a holder of a net profits interest under this subparagraph. Notwithstanding the preceding provisions of this paragraph (b)(3)(i), in the case of crude oil removed (or deemed removed) from the premises before April 1, 1986, the taxpayer may determine the category of all such oil by allocating it among all categories of crude oil in proportion to the production from that property in each such category that was removed (or deemed removed) from the premises during the calendar quarter immediately preceding the calendar quarter of the production whose category is being determined.

(ii) *General rule inapplicable before payout*. In the case of any property, the provisions of paragraph (b)(3)(i) of this section only shall apply for—

(A) The first taxable period in which, under the agreement with respect to such property, one or more persons receive a share described in paragraph (b)(3)(iii)(B) of this section, and

(B) All subsequent taxable periods to which such agreement applies (whether or not the property shows a loss in such period).

(iii) *Net profits agreement defined*. The term "net profits agreement" means an agreement entered into (or renewed) after march 31, 1982, that provides for sharing part or all of the production of crude oil from a property where—

(A) One or more persons are to be reimbursed for qualified costs (within the meaning of paragraph (b)(3)(v) of this section) by the allocation of cost recovery oil, and

(B) One or more persons are to receive a share of any production of crude oil from the property remaining after reduction for the cost recovery oil referred to in paragraph (b)(3)(iii)(A) of this section.

The term "net profits agreement" shall include an agreement that provides that a party to the agreement is entitled to the greater or lesser of a specified share of production of crude oil from the property remaining after reduction for cost recovery oil or some other amount (such as a specified share of total production or a maximum or minimum amount) provided the requirements of paragraph (b)(3)(iii)(A) and (B) of this section are satisfied. If a party to an agreement described in the preceding sentence receives a share of production other than the specified share of production of crude oil from the property remaining after reduction for cost recovery oil, such party shall be treated as receiving a share of production of crude oil from the property remaining after reduction for cost recovery oil in certain situations. If such party receives a maximum or minimum amount with respect to any crude oil production instead of a specified share of production, such party shall not be treated as receiving a share of production remaining after reduction for cost recovery oil with respect to such crude oil production. However, if such party is entitled to receive the greater of a specified share of production or a specified amount and receives the specified share of production remaining after reduction for cost recovery oil instead of the specified amount, such party shall be treated as receiving a share of production remaining after reduction for cost recovery oil to the extent that the amount of the share received exceeds the specified amount. See example (4) of paragraph (b)(3)(viii) of this section.

(iv) *Cost recovery oil defined*. The

term "cost recovery oil" means crude oil produced from the property that is allocated to a person as reimbursement for qualified costs paid or incurred with respect to the property. Accordingly, cost recovery oil exists to the extent that the agreement provides that qualified costs are chargeable against profits and to the extent that the property has sufficient revenues to reimburse for the expenses (*i.e.*, the amount of cost recovery oil cannot exceed the amount of oil produced). If a net profits agreement provides that net profits are determined from proceeds other than proceeds solely from the production of crude oil, cost recovery oil shall be deemed to exist to the extent that, based on all the facts and circumstances, the expenses paid or incurred in producing the net profits are attributable to the production of crude oil. See example (7) of paragraph (b)(3)(viii) of this section.

(v) *Qualified costs.* The term "qualified costs" means any amount paid or incurred for exploring, developing, or producing natural gas or crude oil from a reservoir on the property. The term includes any overhead or indirect costs paid or incurred that are attributable to the activities described in the preceding sentence. The term includes any state or local property or severance taxes with respect to the oil, but does not include any amount that is paid or incurred with respect to the tax imposed by chapter 45.

(vi) *Scope of agreement.* A net profits agreement shall be treated as covering only shares of production of crude oil held by persons who hold economic interests in the property (determined without regard to paragraph (b)(3)(i) of this section).

(vii) *Effective date for certain governmental entities and certain charities.* If 90 percent or more of the remaining production referred to in paragraph (b)(3)(iii)(B) of this section is to be received by holders of a qualified governmental interest (within the meaning of section 4994(a)) or holders of a qualified charitable interest (within the meaning of section 4994(b)), or both, that do not share in the costs referred to in paragraph (b)(3)(iii)(A) of this section, then the requirement of paragraph (b)(3)(iii) that the agreement be entered into (or renewed) after March 31, 1982, shall not apply. Accordingly, the applicability of the provisions of this subparagraph is determined without regard to the date on which the net profits agreement was entered into.

(viii) The principles of this subparagraph may be illustrated by the following examples:

Example (1). A, an independent producer, holds the working interest in property X which produces tier 1 oil. A's interest is burdened by a 95 percent net profits interest held by B who is neither an independent producer nor an exempt producer. The agreement between A and B provides that the amount of net profits is determined by subtracting from gross income all operating expenses except windfall profit taxes. Property X produces 400 barrels of crude oil during the month of May. A is the producer of 5 percent of each of the 400 barrels produced in May and B is the producer of 95 percent of each of such barrels (totalling 20 barrels and 380 barrels, respectively).

Example (2). C, an independent producer, owns an oil and gas property that is burdened by an overriding royalty interest held by D. The overriding royalty interest agreement provides that D is entitled to the lesser of the proceeds from ¼ of the production from the property or 50 percent of the net profits from the property for a calendar quarter. The property produced 1,000 barrels at $30 per barrel for a calendar quarter and had net profits of $1,400. The proceeds from ¼ of the production for the quarter exceeded 50 percent of the net profits. D is treated as the holder of a 50 percent net profits interest with respect to those barrels of crude oil for which D's share of the proceeds from production is determined by reference to 50 percent of net profits. D is the producer of 500 barrels (50% of each of the 1000 barrels produced).

Example (3). E, an independent producer, owns an oil and gas property that is burdened by a net profits interest (determined before any reduction of the net profits for chapter 45 taxes) held by F. F is entitled to 10 percent of the net profits or $2,200 (or revenue from total production if revenue from production is $2,200 or less per calendar quarter) for a calendar quarter, whichever is greater. For a calendar quarter gross income from the property is $26,010 (867 barrels at $30 each) and expenses are $4,800. F's share of net profits is $2,121 (($26,010 − $4,800) × 10%). F receives $2,200 because this amount exceeds 10 percent of net profits. F is treated as the holder of an 8.45829% royalty interest ($2,200 ÷ $26,010), and is treated as the producer of 73.33337 barrels of crude oil (867 × 8.45829%) with respect to that royalty interest.

Example (4). Assume the same facts as example (3) except that the expenses are $1,200. F's share of net profits is $2,481 (($26,010 − $1,200) × 10%). F is treated as the holder of an 8.45829% royalty interest ($2,000 ÷ $26,010) because F is entitled to the $2,200 without regard to net profits. F is also treated as the holder of a 1,24281% net profits interest because $281 ($2,481 − $2,200) are determined by reference to net profits from production ($281 ÷ ($26,010 − ($1,200 + $2,200))). F is treated as the producer of 84.10853 barrels of crude oil. Of this amount, 73.33337 barrels are attributable to the royalty interest (867 × 8.45829%) and 10.77516 barrels are attributable to the net profits interest (867 × 1.24281%). F is treated as the producer of 1.24281% of the cost recovery oil, and, accordingly, is allocated $14.91372 of expenses (1.24281% × $1,200) for purposes of the net income limitation.

Example (5). On January 1, 1983, G and H enter into an agreement which provides for the following: (1) G will incur all expenses of exploring for and developing property Y, (2) G will receive all production from Y until G has recovered all expenses for exploration and development, and (3) after G has recovered all expenses for exploration and development, G and H will share equally the production remaining after G has recovered operating costs (determined without regard to the tax imposed by chapter 45). Y begins producing crude oil on July 1, 1983. G recovers all expenses for exploration and development as of December 31, 1983, and on January 1, 1984, G and H begin sharing the production from Y remaining after G has recovered operating expenses. For purposes of paragraph (b)(3)(iii)(A) of this section, H is not treated as receiving a share described in paragraph (b)(3)(iii)(B) of this section until January 1, 1984.

Example (6). Assume the same facts as example (6) except that the agreement provides that after G has recovered all expenses for exploration and development, G and H will share equally the revenue and expenses of production from Y. The agreement between G and H is not a net profits agreement because H's share of production after G has recovered all expenses for exploration and development is burdened by the expenses of such production.

Example (7). J, an independent producer, owns property Z which produces tier 1 and tier 2 oil. J's interest is burdened by a 95 percent net profits interest held by K whose interest is a qualified charitable interest. The net profits agreement between J and K provides that the amount of net profits is determined by subtracting from gross income from the sale of crude oil and natural gas production from property Z all operating expenses except the windfall profit tax. The agreement also provides that the proceeds from the production of natural gas shall be used to reimburse J for all operating expenses for the production of crude oil and natural gas from property Z. Fifty percent of the gross income from property Z is attributable to the production of crude oil and 50 percent is attributable to the production of natural gas. However, 80 percent of the operating expenses of property Z are attributable to the production of crude oil while only 20 percent are attributable to the production of natural gas. During January of 1984, property Z produces 900 barrels of crude oil which sell for $27,000 ($30 per barrel) and 10,000 MCF of natural gas which also sell for $27,000. The operating expenses of property Z for that month are $4,500, $3,600 of which are attributable to the production of crude oil land $900 of which are attributable to the production of natural gas. Because 80 percent of the operating expenses are attributable to the production of crude oil, cost recovery oil shall be deemed to exist to the extent of 80 percent of the operating expenses. Accordingly, there are 120 barrels of cost recovery oil ($3,600 (operating expenses attributable to crude oil) ÷ $30 (removal price of each barrel of crude oil)).

* * * * *

JAMES I. OWENS,
Acting Commissioner of Internal Revenue.

Approved December 12, 1985.

RONALD A. PEARLMAN,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on February 18, 1986, 8:45 a.m. and published in the issue of the Federal Register for February 19, 1986, 51 F.R. 5993)

Section 4996.—Other Definitions and Special Rules [Windfall Profit Tax]

26 CFR 51.4996-1: Definitions.

Rules relating to a net profits interest for purposes of the windfall profit tax. See T.D. 8076, page 13.

Section 6011.—General Requirement of Return, Statement, or List

26 CFR 301.6011-2: Required use of magnetic media.

T.D. 8081

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER F, SUBCHAPTER H, PART 301—PROCEDURE AND ADMINISTRATION; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Returns Required on Magnetic Media

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to returns required to be filed on magnetic media. Changes to the applicable law were made by the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462] and the Interest and Dividend Tax Compliance Act of 1983 [Pub. L. 98-67, 1983-2 C.B. 352]. The regulations apply to persons required to file certain returns (other than individual, estate, and trust income tax returns) and provide guidance with respect to the magnetic media filing requirement.

DATES: The regulations are effective as of March 25, 1986 and generally apply to returns filed after December 31, 1986.

FOR FURTHER INFORMATION CONTACT: 1. Magnetic Media Reporting, Internal Revenue Service, National Computer Center, P.O. Box 1359, Martinsburg, West Virginia 25401-1359, 304-263-8700 (not a toll-free call), if the inquiry relates to the waiver procedure or to magnetic media filing for returns required on Form 1098, 1099 series, 5498, 6248, 8027 or W-2G.

2. Magnetic Media Coordinator, Internal Revenue Service, Philadelphia Service Center, P.O. Box 245, Bensalem, Pennsylvania 19020, 214-969-2237 (not a toll-free call), if the inquiry relates to magnetic media filing for returns required on Form 1042S.

3. The following regional magnetic media coordinators of the Social Security Administration, if the inquiry relates to magnetic media filing for returns required on Form W-2 or W-2P:

SSA Regional Office	*For Persons Residing In*
Social Security Administration J.F. Kennedy Building Boston, Mass. 02203 ATTN: Joanne Shulman, Rm. 1109 617-223-4375 (not a toll-free call)	Connecticut Maine Massachusetts New Hampshire Rhode Island Vermont
Social Security Administration 26 Federal Plaza New York, New York 10007 ATTN: Anne Coe, Rm. 4012 212-264-0253 (not a toll-free call)	New Jersey New York Puerto Rico Virgin Islands
Social Security Administration P.O. Box 8788, 3535 Market Street Philadelphia, Penn. 19101 ATTN: Frank O'Brien, Rm. 8490 215-596-0470 (not a toll-free call)	Delaware District of Columbia Maryland Pennsylvania Virginia West Virginia
Social Security Administration P.O. Box 1684, 101 Marietta Tower Atlanta, Ga. 30301 ATTN: Pat McCarron, Suite 1804 404-221-2587 (not a toll-free call)	Alabama Florida Georgia Kentucky Mississippi North Carolina South Carolina Tennessee
Social Security Administration 300 South Wacker Drive Chicago, Illinois 60606 ATTN: Jim Juntunen, 32nd Floor 312-353-6717 (not a toll-free call)	Illinois Indiana Michigan Minnesota Ohio Wisconsin
Social Security Administration 1200 Main Tower, Room 1535 Dallas, Texas 75202 ATTN: Pat Insko 214-767-4311 (not a toll-free call)	Arkansas Louisiana New Mexico Oklahoma Texas
Social Security Administration 601 East 12th Street Kansas City, Mo. 64106 ATTN: Dale Fick, 4th Floor East 816-374-2095 (not a toll-free call)	Iowa Kansas Missouri Nebraska
Social Security Administration Federal Office Building 1961 Stout Street	Colorado Montana North Dakota

SSA Regional Office	*For Persons Residing In*
Denver, Col. 80294 ATTN: Rick Schremp, Rm. 1194 303-837-2364 (not a toll-free call)	South Dakota Utah Wyoming
Social Security Administration 100 Van Ness Avenue San Francisco, Cal. 94102 ATTN: Bill Brees, Systems Branch 415-556-4788 (not a toll-free call)	American Samoa Arizona California Guam Hawaii Nevada
Social Security Administration 2901 Third Avenue Seattle, Wash. 98121 ATTN: Jan Hotson, M/S 302 206-442-0468 (not a toll-free call)	Alaska Idaho Oregon Washington

4. C. Scott McLeod of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T, 202-566-3288 (not a toll-free call), if the inquiry relates to other provisions of the regulations.

SUPPLEMENTARY INFORMATION:

BACKGROUND

On September 18, 1985, the FEDERAL REGISTER published proposed amendments to the Procedure and Administration Regulations (26 CFR Part 301) and to the Table of OMB Control Numbers under the Paperwork Reduction Act (26 CFR Part 602) relating to section 6011(e) of the Internal Revenue Code of 1954 (50 FR 37871) [LR-289-82, 1985-43 I.R.B. 26]. The amendments were proposed to reflect the addition to the Code of section 6011(e) by section 319 of the Tax Equity and Fiscal Responsibility Act of 1982 (Pub. L. 97-248, 96 Stat. 610) [1982-2 C.B. 462, 566] and its amendment by section 109 of the Interest and Dividend Tax Compliance Act of 1983 (Pub. L. 98-67, 97 Stat. 383) [1983-2 C.B. 352, 359]. Twenty-two written comments responding to the notice of proposed rulemaking were received. On December 18, 1985, the Internal Revenue Service held a public hearing on the proposed amendments. Two individuals provided oral comments at the public hearing. After consideration of all comments received, the proposed amendments are adopted as revised by this Treasury decision.

SUMMARY OF PROPOSED AMENDMENTS

Under the proposed amendments, any person that is required to use Form 1042S (Income Subject to Withholding under Chapter 3 of the Internal Revenue Code), 1098 (Mortgage Interest Statement), 5498 (Individual Retirement Arrangement Information), 6348 (Annual Information Return of Windfall Profit Tax), 8027 (Employer's Annual Information Return of Tip Income and Allocated Tips), W-2 (Wage and Tax Statement), W-2G (Statement for Recipients of Certain Gambling Winnings), W-2P (Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments), W-4 (Employee's Withholding Allowance Certificate) or any form in the 1099 series (Information Returns) for the purpose of making a return must provide the information required by such form on magnetic media, unless (1) the person is a low-volume filer with respect to the return or (2) the person is granted a waiver with respect to the return by the Internal Revenue Service. Failure to file a return on magnetic media when required to do so by the regulations would be treated as a failure to file the return and would subject the person to the corresponding penalty.

For calendar years (or annual filing periods) beginning before January 1, 1987, the proposed amendments generally permit the filing of returns on the prescribed paper form for all returns other than those required on Form 1099-DIV, 1099-PATR, 1099-INT, or 1099-OID if fewer than 500 returns were required to be filed on that form for the preceding year (or annual period). For calendar years (or annual filing periods) beginning on or after January 1, 1987, the proposed amendments generally permit the filing of returns on the prescribed paper form for all returns other than those required on Form 1099-DIV, 1099-PATR, 1099-INT, or 1099-OID if fewer than 250 returns were required to be filed on that form for the preceding year (or annual period). The proposed amendments also provide that a person required to file a return on magnetic media may receive a waiver from such requirement in appropriate circumstances upon a showing of hardship.

In addition, under the proposed amendments, persons subject to the magnetic media requirement are required to obtain prior consent to the use of the magnetic medium on which the information is to be submitted. The proposed amendments provide that applications for consent to the use of a magnetic medium and requests for waiver generally must be filed at least 90 days before the filing of the first return for which the consent or waiver is requested. In the case of certain returns (Forms W-2 and W-2P) filed in 1987 and 1988, however, the application for consent or request for waiver is due no later than June 30 of the preceding year.

PUBLIC COMMENTS

I. LOW-VOLUME THRESHOLDS.

Several commentators objected to the low-volume thresholds contained in the proposed amendments (500 returns for calendar years (or annual filing periods) beginning before January 1, 1987; 250 returns for calendar years (or annual filing periods) beginning on or after January 1, 1987). Some of these commentators believe that the low-volume thresholds should be increased, while others believe that the implementation of the 250-return threshold should be postponed until a later year. A few commentators believe that the regulations should establish a different threshold for each type of return based on the degree of difficulty in filing on magnetic media for the type of return. In addition, one commentator believes that the low-volume thresholds should apply on an establishment or location basis rather than on a taxpayer basis. Finally, a few commentators believe that the low-volume thresholds should be revised to take into account part-time workers and employee turnover.

The final regulations do not change the low-volume thresholds that were contained in the proposed amendments (except to clarify that a separate threshold applies to each member of an affiliated group of corporations filing a consolidated return) for a number of reasons. First, the purpose of the low-volume thresholds is to exclude from the magnetic media filing requirement those taxpayers that the Internal Revenue Service believes should be excluded because the volume of returns filed does not justify the incremental cost of filing on magnetic media. Taxpayers filing more than 250 returns during any calendar year (or annual filing period) should be able to comply with the magnetic media requirement without incurring unreasonable costs. Many taxpayers filing over 250 returns use computers in other facets of their business. Other taxpayers that do not utilize computers in their business should be able to contract with a computer service bureau to convert the information to magnetic media at a reasonable cost.

Furthermore, taxpayers that are required to file returns in excess of the low-volume thresholds can request a waiver from the magnetic media requirement. As was stated in the preamble to the proposed regulations, it is anticipated that the waiver authority will be exercised so as not to unduly burden taxpayers lacking the necessary data processing facilities and access at a reasonable cost to computer service bureaus.

The final regulations do not adopt a different low-volume threshold for each type of return because the cost of filing on magnetic media should not vary significantly based on the type of return being filed. In addition, the low-volume threshold is not determined on an establishment or location basis because in many cases an exemption would be inappropriate and hardship cases can be dealt with through the waiver process. Finally, the final regulations do not modify the low-volume threshold to take into account part-time employees and employee turnover because the Internal Revenue Service believes that the volume of returns, and not the number of employees, is the best indicator of the incremental cost of filing on magnetic media.

II. TYPES OF RETURNS REQUIRED ON MAGNETIC MEDIA.

Several commentators indicated that it is inappropriate and confusing to require magnetic media reporting for information contained on Form W-4 because Form W-4 is not a return (as required by section 6011(e)(1)), but rather is a form that is completed by an employe to enable the employer to withhold an approprite amount of Federal income tax from the employee's wages. Other commentators argued that magnetic media reporting is inappropriate for information contained on Form 1099-A or Form 1099-R because the transactions that give rise to a return on such forms occur at irregular intervals throughout the year.

The Internal Revenue Service has determined that magnetic media reporting is unnecessary for returns filed on Form W-4, and, thus, the final regulations exclude returns filed on Form W-4 from the list of returns required on magnetic media. The Internal Revenue Service does not believe that the irregularity of a transaction that gives rise to a return will affect a taxpayer's ability to comply with the magnetic media requirement. Taxpayers filing Form 1099-A or Form 1099-R can compile the information required by such forms at the time of the underlying transaction and periodically transcribe the information on magnetic media without a substantial economic burden. For this reason, the final regulations require magnetic media reporting for information contained on Form 1099-A or Form 1099-R.

III. PERMISSIBLE MEDIA FOR FILING RETURNS.

Commentators also suggested that the regulations permit magnetic media filing of 5-1/4 inch personal computer floppy disks. Although the Social Security Administration and the Internal Revenue Service are currently able to process information submitted on 5-1/4 inch floppy disks, the Social Security Administration has announced that it will have the capability to process such information for returns filed after December 31, 1986, and the Internal Revenue Service anticipates that it will also have the capability to process such information for certain returns filed after December 31, 1986. Persons that plan to file on 5-1/4 inch floppy disks should submit a timely consent application that indicates that choice. If the Internal Revenue Service is unable to process such information for returns required to be filed in 1987, a hardship waiver will ordinarily be granted for such year.

IV. RETURNS OF BROKERS AND BARTER EXCHANGES.

One commentator requested clarification with respect to the application of the low-volume thresholds to returns required on Form 1099-B (Proceeds from Broker and Barter Exchange Transactions). The proposed and final regulations do not apply to returns required on Form 1099-B. Consequently, under section 1.6045-1(l) of the Income Tax Regulations, all returns required on Form 1099-B must be filed on magnetic media unless a hardship waiver is granted with respect to such return.

V. COORDINATION OF RULES APPLICABLE TO RETURNS REQUIRED ON FORMS W-2 AND W-2P WITH RULES APPLICABLE TO RETURNS REQUIRED ON OTHER FORMS.

One commentator suggested that the approval of magnetic media be performed by a single government agency and that the deadlines for the submission of consent and waiver applications for returns required on Form W-2 and W-2P be the same as the deadlines for other returns (at least 90 days before the filing of the first return for which consent or a waiver is requested). The regulations contain different rules for returns required on Form W-2 and W-2P because these returns are submitted to the Social Security Administration where the information on the returns is processed for use by the Social Security Administration and the Internal Revenue Service. The regulations do not permit approval of a magnetic medium by a single agency because the computer capabilities of the Social Security Administration and the Internal Revenue Service currently differ and are likely to differ in the future. The deadlines for the submission of consent and waiver applications are not uniform for the same reason.

VI. IMPOSITION OF FAILURE TO FILE PENALTY FOR FAILURE TO FILE ON MAGNETIC MEDIA.

The proposed regulations provide that if a person fails to file on magnetic media when required to do so by section 6011(e) and the regulations, such person is deemed to have failed to file the return and is subject to the corresponding penalties for failure to file such return. One commentator requested a transition period before the imposition of penalties for the failure to file on magnetic media. In addition, the commentator suggested that the regulations provide that any reasonable cause or due diligence exception to the penalty for failure to file apply in the case of a failure to file on magnetic media. The Internal Revenue Service believes that it is inappropriate to provide a blanket waiver of the penalty for the failure to file on magnetic media for a transition period. The regulations have been clarified, however, to permit the assertion of a reasonable cause or due diligence exception to the imposition of the penalty if the underlying failure to file penalty permits such an exception.

VII. EFFECTIVE DATE.

One commentator requested clarification of the effective date of the regulations. Section 110 of the Interest and Dividend Tax Compliance Act of 1983 provides that in the case of returns required on Form 1099-DIV, 1099-PATR, 1099-INT, or 1099-OID, the magnetic media requirement applies to payments made after December 31, 1983. The final regulations, which follow the proposed regulations, apply to returns filed after December 31, 1986. The final regulations have been clarified, however, to provide that returns required on Form 1099-DIV, 1099-PATR, 1099-INT, or 1099-OID for payments made after December 31, 1983, are subject to the magnetic media requirement even if such returns are filed before January 1, 1987.

VIII. REGUALTORY FLEXIBILITY ANALYSIS.

Two commentators believe that the Internal Revenue Service should have undertaken a regulatory flexibility analysis to assess the impact of the regulation on small businesses and other small entities. Under section 605(b) of title 5 of the United States Code, an initial or final regulatory flexibility analysis is not required if the head of the agency that is proposing a rule certifies that the rule, if promulgated, will not have a significant economic impact on a substantial number of small entities. In the notice of proposed rulemaking that was published oin September 18, 1985 (50 FR 37871 [LR-289-82, 1985-43 I.R.B. 26]), it was certified that the proposed regulations will not have a significant impact on a substantial number of small entities. This certification was based on a determination that the economic impact of the proposed reporting requirements will be minimal in most cases and, in any event, for returns required on Form 1099-DIV, 1099-PATR, 1099-INT, or 1099-OID, is attributable to requirements directly imposed by the statute. The Internal Revenue Service believes that the certification was proper, and thus, a regulatory flexibility analysis is not required.

IX. MISCELLANEOUS COMMENTS.

Finally, a few commentators claimed that the magnetic media requirements was overly budensome but did not suggest any specific modifications to the proposed amendments, and other commentators suggested changes that are outside the scope of this regulation project.

EXECUTIVE ORDER 12291, REGUALTORY FLEXIBILITY ACT AND PAPERWORK REDUCTION ACT

The Commissioner of Internal Revenue has determined that this rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required. It is hereby certified that the regulations adopted in this document will not have a significant impact on a substantial number of small entities (see discussion under the Special Analyses heading in the notice of proposed rulemaking; 50 FR 37872). Accordingly, a regulatory flexibility analysis is not required under the Regulatory Flexibility Act (5 U.S.C. chapter 6).

The collection of information requirements contained in this regulation have been approved by the Office of Management and Budget (OMB) under section 3504(h) of the Paperwork Reduction Act.

DRAFTING INFORMATION

The principal author of these regulations is C. Scott MeLeod of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, on matters of both substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Parts 301 and 602 are amended as follows:

PROCEDURE AND ADMINISTRATION REGULATIONS
(26 CFR Part 301)

Paragraph 1. The authority for Part 301 is amended by adding the following authority citation:

Authority: 26 U.S.C 7805. * * * Section 301.6011-2 also issued under 26 U.S.C. 6011(e).

Par. 2. New §301.6011-2 is added immediately after §301.6011-1 to read as follows:

§301.6011-2 Required use of magnetic media.

(a) *Meaning of terms.* The following definitions apply for purposes of this section:

(1) *Magnetic media.* The term "magnetic media" means any magnetic media permitted under applicable regulations, revenue procedures, or, in the case of returns filed with the Social Security Administration, Social Security Administration publications. These generally include magnetic tape, diskette, cassette, and mini-disk, as well as other media specifically permitted under the applicable regulations or procedures. Use of diskette and cassette may be subject to certain limitations or special rules in the case of returns required on Form W-2 or W-2P.

(2) *Machine-readable paper form.* The term "machine-readable paper form" means—

(i) Optical-scan paper form; or

(ii) Any other machine-readable paper form permitted under applicable regulations, revenue procedures, or Social Security Administrtion publications.

(3) *Person.* The term "person" includes any person that is required to

file a return that is described in paragraph (b) of this section. Thus, the term "person" includes the United States, a State, the District of Columbia, a foreign government, a political subdivision of a State or a foreign government, or an internal organization. In addition, in the case of an affiliated group of corporations filing a consolidated return, each member of the affiliated group is a separate person.

(b) *Returns required on magnetic media.* (1) If the use of Form 1042S, 1098, 1099 series, 5498, 6248, 8027, W-2G, or other form treated as a form specified in this paragraph (b)(1) is required by the applicable regulations or revenue procedures for the purpose of making a return, the information required by such form shall, except as otherwise provided in paragraph (c) of this section, be submitted on magnetic media. Returns on magnetic media shall be made in accordance with applicable review procedures. Pursuant to these procedures, the consent of the Commissioner of Internal Revenue (or other authorized officer or employee of the Internal Revenue Service) to a magnetic medium shall be obtained prior to submitted a return on such magnetic medium. An application for such consent shall be in writing and must be filed at least 90 days after the filing of the first return for which consent is requested.

(2) If the use of Form W-2, W-2P, or other form treated as a form specified in this paragraph (b)(2) is required by the regulations or revenue procedures for the purpose of making a return (not including the copy of Form W-2 or W-2P that is required to be attached to an Individual Income Tax Return), the information required by such form shall, except as otherwise provided in paragraph (c) of this section, be submitted on magnetic media. Returns on magnetic media shall be made in accordance with applicable Social Security Administration procedures. Thus, the consent of the Secretary of Health and Human Services (or other authorized officer or employee of the Department of Health and Human Services) to a magnetic medium shall be obtained prior to submitting a return on such magnetic medium. An application for such consent shall be in writing and must be filed—

(i) On or before June 30, 1986, in the case of returns filed in 1987;

(ii) On or before June 30, 1987, in the case of returns filed in 1988; and

(iii) At least 90 days before the filing of the first return for which consent is requested in all other cases.

(3) The Commissioner may prescribe by revenue procedure that additional forms are treated, for purposes of this section, as forms specified in paragraph (b)(1) or (b)(2) of this section.

(c) *Exceptions*—(1) *Low-volume filers*—(i) *In general.* A person required to make returns on a particular type of form specified in paragraph (b) of this section (other than Form 1099-DIV, 1099-PATR, 1099-INT, or 1099-OID) may make such returns on the prescribed paper form for a calendar year or other applicable annual period (whether such returns are filed during the calendar year or annual period or during the subsequent calendar year or annual period) if—

(A) In the case of the calendar year or annual period beginning before January 1, 1987—

(*1*) On the first day of such calendar year or annual period the person reasonably expects to file fewer than 500 returns on such form for the calendar year or annual period; and

(*2*) The person was not required to file 500 or more returns on such form for the preceding calendar year or annual period; or

(B) In the case of a calendar year or annual period beginning on or after January 1, 1987—

(*1*) On the first day of such calendar year or annual period the person reasonably expects to file fewer than 250 returns on such form for the calendar year of annual period; and

(*2*) The person was not required to file 250 or more returns on such form for the preceding calendar year or annual period.

Alternatively, such persons may make returns on magnetic media in accordance with paragraph (b) of this section.

(ii) *Machine-readable forms.* Returns made on a paper form under this paragraph (c)(1) shall be machine-readable if applicable revenue procedures provide for a machine-readable paper form.

(iii) *Form 1099 series.* Each form within the Form 1099 series is considered a separate type of form for purposes of this paragraph (c)(1). Thus, for example, in the case of a calendar year beginning on or after January 1, 1987, if on the first day of such calendar year a person reasonably expects to file 200 returns on Form 1099-A and 150 returns on Form 1099-MISC and for the preceding calendar year the person was required to file 200 returns on form 1099-A and 150 returns on Form 1099-MISC, the person may make such returns on the prescribed paper form for such calendar year.

(2) *Special rule for Form 1099-DIV, 1099-PATR, 1099-INT, 1099-OID*—(i) *50 or fewer returns.* A person required to make returns on Form 1099-DIV, 1099-PATR, 1099-INT, or 1099-OID may make such returns on a machine-readable paper form for a calendar year if—

(A) On the first day of such calendar year the person reasonably expects to file 50 or fewer returns on such forms for the calendar year; and

(B) The person was not required to file more than 50 returns on such forms for the preceding calendar year.

Alternatively, such persons may make returns on magnetic media in accordance with paragraph (b) of this section.

(ii) *Aggregation of returns.* For purposes of determining the number of returns that a person was required to file or reasonably expects to file on Form 1099-IDV, 1099-PATR, 1099-INT, or 1099-OID, all such returns shall be aggregated. Thus, for example, if a person filed 30 returns on Form 1099-INT and 30 returns on Form 1099-DIV for a calendar year, or reasonably expects to do so for the succeeding calendar year, all returns made by such person or Form 1099-DIV, 1099-PATR, 1099-INT and 1099-OID for the succeeding calendar year must be on magnetic media.

(3) *Provided by regulations*—(i) *In general.* This section does not apply to a return if the regulations relating to such return require reporting on magnetic media.

(ii) *Example.* The following example illustrates the application of the rule in paragraph (c)(3)(i) of this section:

Example. Section 1.6045-1(l), relating to returns of information of brokers and barter exchanges, requires the use of magnetic media as a method of reporting. Thus, this section does not apply to returns required to be filed under section 6045.

(4) *Waiver.* (i) The Commissioner may waive the requirements of this sec-

tion if hardship is shown in an application filed in accordance with this paragraph (c)(4)(i). Such waiver shall specify the type of form and period to which it applies and shall be subject to such terms and conditions regarding the method of reporting as may be prescribed by the Commissioner. In determining whether hardship has been shown, the principal factor to be taken into account will be the amount, if any, by which the cost of filing returns in accordance with this section exceeds the cost of filing the returns on other media. A request for waiver shall be in writing and must be filed—

(A) On or before June 30, 1986, in the case of returns on Form W-2 or W-2P filed in 1987;

(B) On or before June 30, 1987, in the case of returns on Form W-2 or W-2P filed in 1988; and

(C) At least 90 days before the filing of the first return for which a waiver is requested in all other cases.

(ii) The Commissioner may by revenue procedure prescribe rules that supplement the provisions of paragraph (c)(4)(i) of this section.

(d) *Paper form returns.* Returns submitted or paper forms (whether or not machine-readable) permitted under paragraph (c) of this section shall be made in accordance with applicable revenue or Social Security Administration procedures.

(e) *Applicability of current procedures.* Until procedures are prescribed which further implement the mandatory filing on magnetic media provided by this section, a return to which this section applies shall be made in the manner and shall be subject to the requirements and conditions (including the requirement of applying for consent to the magnetic medium) prescribed in the regulations, revenue procedures and Social Security Administration publications relating to the filing of such return on magnetic media. In addition, consent to the use of a magnetic medium obtained in accordance with such regulations, revenue procedures and Social Security Administration publications (regardless of when obtained) will be considered consent to the use of such medium for purposes of paragraph (b) of this section.

(f) *Failure to file.* If a person fails to file a return on magnetic media when required to do so by section 6011(e) of this section, such person is deemed to have failed to file the return. See sections 6652 and 6693 for penalties for failure to file certain returns.

(g) *Effective date.* (1) Except as otherwise provided in paragraph (g)(2) of this section, this section applies to returns filed after December 31, 1986.

(2) Returns required on Form 1099-DIV, 1099-PATR, 1099-INT, or 1099-OID for payments made after December 31, 1983, must be filed on magnetic media except as otherwise provided in paragraph (c) of this section.

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT (26 CFR PART 602)

Par. 3. The authority citation for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Part 4. Section 602.101(c) is amended by inserting in the appropriate place in the table "§301.6011-2 . . . [1545-0387]".

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

Approved March 5, 1986.

ROGER MENTZ,
Acting Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on March 20, 1986, 4:25 p.m., and published in the issue of the Federal Register for March 25, 1986, 51 F.R. 10348)

Section 6053.—Reporting of Tips

26 CFR 31.6053-3T: Reporting by certain large food or beverage establishments with respect to tips.

Guidance is provided to both employers and employees of certain large food and beverage establishments who want to petition the district director for a reduction in the tip rate allocation figure from 8 percent of the gross receipts to a figure not below 2 percent. See Rev. Proc. 86-21, page 29.

Section 6111.—Registration of Tax Shelters

26 CFR 301.6111-1T: Questions and answers relating to tax shelter registration (Temporary).

T.D. 8078

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER F, SUBCHAPTER H, PART 301—PROCEDURE AND ADMINISTRATION; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Tax Shelter Registration

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to tax shelter registration. In addition, the text of the temporary regulations set forth in this document also serves as the text of the proposed regulations cross-referenced * * * [on page 32, this Bulletin]. Changes to the applicable tax law were made by the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1]. The regulations affect organizers, sellers, investors and certain other persons associated with investments that are considered tax shelters.

DATES: The regulations apply to tax shelters in which any interest is first sold after August 31, 1984.

FOR FURTHER INFORMATION CONTACT: Paulette Chernyshev of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention CC:LR:T). Telephone 202-566-3288, (not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document amends the temporary Procedure and Administration Regulations (26 CFR Part 301) published in the FEDERAL REGISTER on August 15, 1984 (49 FR 32712) [T.D. 7964, 1984-2 C.B. 263]. The temporary regulations amended by this document relate to tax shelter registration under section 6111 of the Internal Revenue Code of 1954, as added by section 141 of the Tax Reform Act of 1984 (Pub. L. 98-369, 98 Stat. 678) [1984-3 C.B. (Vol. 1) 1, 190]. This document also amends the Table of OMB Control Numbers (26 CFR Part 602).

The temporary regulations have been drafted in question and answer format. No inference should be shown regarding issues not raised herein or because certain questions and not others are included. The temporary regulations contained in this document will remain in effect until additional temporary or final regulations are published in the Federal Register.

EXPLANATION OF PROVISIONS

Question and answer 45 of the temporary regulations relating to tax shelter registration (§301.6111-1T) provided that a tax shelter organizer is not required to file an amended application for registration if the facts relating to the tax shelter change after the tax shelter has been registered. A number of commentators have requested that tax shelter organizers be allowed to file amended applications for registration. Accordingly, the temporary regulations have been revised to permit, but not require, the filing of amended applications in certain circumstances. However, permission to file an amended application does not alter the requirement to file a complete and accurate initial application by the required date. If the initial application was timely filed and contained complete and accurate information, the filing of an amended application to reflect later developments will not affect the determination as to whether the initial application would be subject to penalty.

Question and answer 52 of the temporary regulations required a person who sells (or otherwise transfers) an interest in a tax shelter to furnish the registration number of the tax shelter to the purchaser (or transferee) at the time of the sale (or transfer) of the interest (or, if later, within 7 days after the seller or transferor receives the registration number). Commentators have requested that sellers be allowed more time to furnish the registration number. Accordingly, the temporary regulations have been amended to provide that the seller (or transferor) must furnish the registration number to the purchaser (or transferee) at the time of sale (or transfer) of the interest (or, if later, within 20 days after the seller or transferor receives the registration number). The regulations continue to provide that a written statement explaining that a registration number has been applied for and providing certain other information must be furnished to the purchaser (or transferee) at the time of the sale if the registration number is not furnished at that time.

EXECUTIVE ORDER 12291, REGULATORY FLEXIBILITY ACT, AND PAPERWORK REDUCTION ACT

The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291 Accordingly, a Regulatory Impact Analysis is not required. A general notice of proposed rulemaking is not required for temporary regulations. Accordingly, the temporary regulations are not subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

The collection of information requirements contained in this regulation have been approved by the Office of Management and Budget (OMB) under section 3507 of the Paperwork Reduction Act.

DRAFTING INFORMATION

The principal author of these regulations is Paulette Chernyshev of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * * *

Amendments to the reguations.

The amendments to 26 CFR Part 301 and 26 CFR Part 602 are as follows:

PROCEDURE AND ADMINISTRATION

(26 CFR Part 301)

Paragraph 1. The authority for Part 301 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Sectioin 301.6111-1T also issued under 26 U.S.C. 6111.

Par. 2. Section 301.6111-1T is amended by revising answers 45 and 52, adding new question and answer 45A, and revising the table of contents to reflect the additional question and answer. The revised and added provisions read as follows:

§301.6111-1T Questions and answers relating to tax shelter registration (Temporary)

* * * * *

Table of Contents

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Information reported on an amended application. . . .45A

* * * * *

Q-45. If the facts relating to a tax shelter change after the tax shelter has been registered, must the tax shelter be registered again or must an amended application for registration be filed by the tax shelter organizer?

A-45. No. The tax shelter organizer, however, is permitted to file an amended application if a material change in facts occurs after the initial registration. A material change in facts is—

(1) A change in the identifying information relating to the tax shelter or tax shelter organizer,

(2) The acquisition or construction of a principal asset not reported on the initial application for registration,

(3) A change in the method of financing a minimum investment unit, or

(4) A change in the principal business activity.

In addition, a change in any tax shelter ratio reported on the initial application for registration that increases or decreases the reciprocal of the tax shelter ratio (*i.e.*, the fraction in which the amount of the applicable investment base is the numerator and the amount of the applicable deductions and credits is the denominator) by 50 percent or more is a material change in facts. For example, if the tax shelter ratio increases from 2 to 1 to 4 to 1, the reciprocal of the tax shelter ratio decreases from 1/2 and 1/4, a 50-percent decrease. Similarly, if the tax shelter ratio decreases from 6 to 1 to 4 to 1, the reciprocal of the tax shelter ratio increases from 1/6 to 1/4, a 50-percent increase. In either case, there is a material change in facts and an amended application could be filed.

Q-45A. What information should be included on an amended application for registration?

A-45A. The tax shelter organizer must include the identifying information requested on Form 8264, Application for registration of a Tax Shelter, and the tax shelter registration number that has been assigned to the tax shelter. In addition, the tax shelter organizer should include any other information requested on Form 8264 (1) that has changed since the tax shelter was registered, or (2) that the tax shelter organizer did not know at the time the tax shelter was registered but has learned of since the registration.

For example, assume that A organizes partnership L, a blind pool that will invest in real estate. Before the real estate is identified or acquired, interests in L will be offered to the public in an offering that must be registered with the Securities and Exchange Commission. Although A does not know what real estate L will acquire and therefore is unable to calculate the tax shelter ratio with certainty, A concludes (based on representations made or to be made) that the tax shelter ratio will exceed 2 to 1 as to some of the investors. Accordingly, A registers L as a tax shelter. A attaches a statement to the application for registration, explaining that L is a blind pool organized to invest in real estate, but that L has not yet acquired any real estate. In addition, A attaches a statement explaining that although the tax shelter ratio is expected to exceed 2 to 1, A cannot compute the tax shelter ratio with certainty because L has not yet acquired any real estate. Several months after L is registered, L acquires a shopping center. A may file an amended application for registration. In addition to reporting the identifying information and the tax shelter registration number on the amended application, A should report the shopping center as the principal asset and the recomputed tax shelter ratio.

As another example, assume that C organizes a limited partnership that is a tax shelter. On the application for registration, C reports that the tax shelter ratio is 2.2 to 1. After the partnership has been registered, C finds that the partnership is unable to attract sufficient investors. To make investing in the partnership more attractive, C decides to offer financing for the purchase of interests in the partnership. As a result of the change in financing, the tax shelter ratio will be 5 to 1. Because there is a change in financing and a change in the tax shelter ratio that decreases the reciprocal of the tax shelter ratio by 50 percent or more, C may file an amended application for registration. In addition to reporting the identifying information and the tax shelter registration number on the amended application, C should report the recomputed tax shelter ratio and information relating to the change in financing.

* * * * *

Q-52. When must the registration number be furnished to purchasers of interests in the tax shelter?

A-52. The person who sells (or otherwise transfers) an interest in a tax shelter must furnish the registration number to the purchaser (or transferee) at the time of sale (or transfer) of the interest (or, if later, within 20 days after the seller or transferor receives the registration number). If the registration number is not furnished at the time of the sale (or other transfer), the seller (or transferor) must furnish the statement described in A-54 to the purchaser (or transferee) at the time of the sale (or other transfer). If interests in a tax shelter were sold before September 1, 1984, all investors who acquired their interests in the tax shelter before September 1, 1984, must be furnished with the registration number of the tax shelter by December 31, 1984. The registration number will be considered furnished to the investor if it is mailed to the investor at the last address of the investor known to the person required to furnish the number.

* * * * *

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

(26 CFR Part 602)

Par. 3. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. Section 602.101(c) is amended by inserting in the appropriate place in the table "§301.6111-1T . . . 1545-0865".

There is need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impractical to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States code or subject to the effective date limitation of subsection (d) of that section.

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

Approved February 11, 1986.

J. ROGER MENTZ,
Acting Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on March 3, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 4, 1986, 51 F.R. 7439)

Section 6867.—Presumptions Where Owner of Large Amount of Cash is Not Identified

26 CFR 301.6867-1T: Illegal activity cash.

T.D. 8079

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER F, PART 301—PROCEDURE AND ADMINISTRATION

Illegal Activity Cash

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to illegal activity cash. Changes to the applicable tax law were made by the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462]. The regulations affect certain persons subject to jeopardy or termination assessments and provide the guidance necessary for Internal Revenue Service personnel who must administer the Act.

DATE: The regulations are effective March 24, 1986.

FOR FURTHER INFORMATION CONTACT: Ewan D. Purkiss of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3238, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains temporary regulations under section 6867 of the Internal Revenue Code of 1954, as added by section 330(a) of the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462, 570]. The temporary regulations contained in this document will remain in effect until additional temporary or final regulations are published in the Federal Register.

Under section 6867, if an individual in physical possession of cash in excess of $10,000 does not claim the cash as the individual's or as that of another person whose identity is readily ascertainable (and who acknowledges ownership of the cash), then for purposes of section 6851 (relating to termination assessments) and section 6861 (relating to jeopardy assessments) it will be presumed that the cash represents gross income of an individual for the taxable year in which the possession occurs, and that the collection of tax will be jeopardized by delay.

Section 6867(d) provides that cash includes cash equivalents. The term "cash equivalents" means foreign currency, any bearer obligation, and any medium of exchange that is of a type frequently used in illegal activities and that is specified in regualtions prescribed by the Commissioner. The temporary regulations specify that coins, precious metals, jewelry, precious stones, and postage stamps are cash equivalents.

EXECUTIVE ORDER 12291; REGULATORY FLEXIBILITY ACT

The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

A general notice of proposed rulemaking is not required for temporary regulations. Accordingly, the temporary regulations are not subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is Ewan D. Purkiss of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * * *

Amendments to the regulations.

The amendments to 26 CFR Part 301 are as follows:

PROCEDURE AND ADMINISTRATION (26 CFR Part 301)

Paragraph 1. The authority for Part 301 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 301.6867-1T also issued under 26 U.S.C. 6867(d)(2)(C)(ii).

Par. 2. A new §301.6867-1T is added to read as follows:

§301.6867-1T Illegal activity cash.

For purposes of section 6867—

(a) *Cash.* The term "cash" includes any cash equivalents.

(b) *Cash equivalent*—(1) *In general.* The term "cash equivalent" includes foreign currency, any bearer obligation, and any medium of exchange that is of a type that has been frequently used in illegal activities and that is listed in paragraph (b)(2) of this section.

(2) *Specific cash equivalents.* The following are also cash equivalents:

(i) Coins,
(ii) Precious metals,
(iii) Jewelry,
(iv) Precious stones, and
(v) Postage stamps.

(3) *Value of cash equivalents.* Any cash equivalent will be taken into account at its fair market value except in the case of a bearer obligation, which will be taken into account at its face amount.

(c) *Effective date.* The provisions of this section are effective March 24, 1986.

There is need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impractical to issue the Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitation of subsection (d) of this section.

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved March 6, 1986.

J. ROGER MENTZ,
Acting Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on March 21, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 24, 1986, 51 F.R. 9949)

Section 7701.—Definitions.

26 CFR 301.7701-4: Trusts.

T.D. 8080

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER F, PART 301—PROCEDURE AND ADMINISTRATION

Classification of Investment Trusts With Multiple Classes of Ownership

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations on Procedure and Administration relating to the classification for federal tax purposes of investment trusts with multiple classes of ownership. The regulations are designed to clarify the application of the classification rules to an investment trust with multiple classes of ownership interests. These regulations provide guidance to taxpayers and Internal Revenue Service personnel.

DATE: The regulations are effective on April 28, 1984, and with respect to trusts, any interests in which are initially issued on or after April 28, 1984.

FOR FURTHER INFORMATION CONTACT: Stuart G. Wessler of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3297, not a toll-free call).

SUPPLEMENTARY INFORMATION

BACKGROUND

On May 2, 1984, the FEDERAL REGISTER published proposed amendments to the Regulations on Procedure and Administration (26 CFR Part 301) under seciton 7701 of the Internal Revenue Code of 1954 (49 FR 18741) [LR-68-84, 1984-1 C.B. 777]. The proposed amendments related to the definition of the term "trust" for federal tax purposes. A public hearing was held on July 31, 1984. After consideration of all comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

EXPLANATION OF PROVISIONS

Section 301.7701-4(c) of the Regulations on Procedure and Administration provides guidance as to the classification for federal tax purposes of certain "investment" trusts. Before its amendment by this Treasury decision, those regulations (the "prior regulations") classified an entity of the type known as a "fixed investment trust" as a trust or as an association (taxable as a corporation), depending upon whether the governing instrument created a power to vary the investment of the certificate holders. The prior regulations did not address whether an investment trust that permitted investors to choose among different classes of ownership interests with varying investment attributes would be classified as a trust for federal tax purposes.

In general, a trust for federal tax purposes is limited to a trust created simply to conserve or protect property for the trust beneficiaries. Ordinarily, the beneficiaries of the trust do no more than accept its benefits and are not its creators or voluntary planners. Certain "investment" trusts, however, are recognized as serving the traditional custodial purposes of an ordinary trust even though interests therein are voluntarily acquired by the beneficiaries. Thus, investment trusts have been treated as trusts for federal tax purposes where employed simply to hold investment assets, albeit for the benefit of voluntary investors. *Commissioner* v. *Chase National Bank*, 122 F.2d 450 (2d Cir. 1941).

Historically, the issue of whether an investment trust serves the mere custodial purpose of holding investment assets has focused on whether the beneficiaries' investment was fixed or could instead be varied under the terms of the trust agreement. The existence of a power to vary the beneficiaries' investment, even though only contingent in form, is sufficient to "turn the venture into a 'business.'" *Commissioner* v. *North American Bond Trust*, 122 F.2d 545, 546 (2d Cir. 1941), *cert. denied*, 314 U.S. 701 (1942). Thus, the prior regulations limited trust classification to "fixed investment trusts" where there was no power under the trust agreement to vary the investment of the certificate holders.

Recently, new forms of investment trusts have been created that involve not only voluntary acquisition of interest by investors but also different classes of beneficial interests with varying investment attributes. These so-called "multiple class trusts" vest no discretionary power in the trustee over investment of the trust assets and thus assertedly satisfy the fixed investment requirement of the prior regulations. At the time the prior regulations were first promulgated, however, the entities commonly known as fixed investment trusts had only one class of investment certificates. The certificates represented undivided interests in the trust property, and were, in form, receipts for the securities held by the trust.[1] Thus, where the trustee had no power to vary investment, a fixed investment trust was little more than a depository arrangement, formed to hold a pool of specific investment assets. Although the trust device permitted individual investors to diversify investment risk, the arrangement in substance provided a form of direct, if common, ownership of the trust assets. This use of a trust to hold investment assets and thereby facilitate direct investment by a pool of investors is consistent with the custodial purposes that have traditionally limited trust classification.

Multiple class trusts depart from the traditional form of fixed investment trust in that the interests of the beneficiaries are not undivided, but diverse. The existence of varied beneficial interests may indicate that the trust is not employed simply to hold investment assets, but serves a significant additional purpose of providing investors with economic and legal interests that could not be acquired through direct investment in the trust assets. Such use of an investment trust introduces the potential for complex allocations of trust income among investors, with correspondingly difficult issues of how such income is to be allocated for tax purposes. These issues are properly foreign to the taxation of trust income, where rules have not developed to accommodate the varied forms of commercial investment, and no comprehensive economic substance requirement governs the allocation of income for tax purposes.

Based on the above considerations, proposed amendments to prior §301.7701-4 would have denied trust classification to investment trusts with multiple classes of ownership. Generally, the final regulations retain this rule. However, in response to public comment, the proposed regulations have been modified to provide that trust classification may be appropriate for a multiple class trust if the trust is formed to serve the traditional custodial purposes of a fixed investment trust and the existence of multiple classes of beneficial interests is incidental to such purposes.

Thus, under the standard contained in the final regulations, the classification of multiple class trusts depends on the purposes for which the trust is formed, and the significance of multiple classes of ownership interests in relation to those purposes. A fixed investment trust with multiple classes of ownership interests, that otherwise possesses the characteristics of a trust, would be classified as a trust if the trust is employed to facilitate direct investment in the assets of the trust, and the existence of multiple classes of ownership interests is incidental to such purpose. Whether the existence of multiple classes of ownership interests is incidental to the use of an investment trust as a vehicle to facilitate direct investment, or instead reflects a purpose to provide investors with diverse interests in the trust assets, generally depends on the extent to which the investment attributes of interests in the trust diverge from direct ownership of the trust assets. The extent of such divergence may, in turn, be reflected by the extent to which the interests of the investors in a multiple class trust could be reproduced without resort to multiple classes of ownership. For example, the creation of a subordinated and preferred class of interests in a trust holding real estate mortgages may be incidental to the purpose of the trust to facilitate direct investment in the mortgages, where the subordinated interest is retained as a security device by the originator of the mortgages, and is in lieu of a direct guarantee to investors. The final regulations provide additional examples of the classification of investment trusts with multiple classes of ownership interests. Further guidance as to the application of the new standard will be provided through the administrative rulings process.

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[1] "The investor [in a fixed trust] . . . has a beneficial undivided interest in specific deposited securities or property. . . . In the fixed trust . . . only one class of security is issued—the certificate of beneficial interest which is, in form, a receipt issued by the trustee for the deposited property." Investment Trusts and Investment Companies, H. R. Doc. 567, 76th Cong., 3d Sess. 8-9 (1940) (footnote omitted).

The final regulations apply only to investment trusts, and hence have no applicability to trusts that would be classified as "ordinary trusts" under existing §301.7701-4(a) or "business trusts" under existing §301.7701-4(b). Moreover, the final regulations are not intended to affect existing standards for classification of fixed investment trusts with a single class of ownership interests.

On May 17, 1984, the Internal Revenue Service announced that the final regulations would not apply to certain state and local government financing arrangements the substance of which is the issuance of a series of separate debt obligations directly by the governmental unit (Announcement 84-62, 1984-24 I.R.B. 29). The Internal Revenue Service will treat those financing arrangements in accordance with that announcement.

One commentator suggested that the proposed amendments to the regulations constituted legislative regulations for which the Service was required to prepare a Regulatory Flexibility Analysis and a Regulatory Impact Analysis. The Service, however, has concluded that these regulations are interpretative regulations not subject to those requirements.

Finally, certain commentators raised other issues that the Service considers to be beyond the scope of the classification issues that these regulations address.

EXECUTIVE ORDER 12291 AND REGULATORY FLEXIBILITY ACT

The Commissioner of Internal Revenue has determined that this final rule is not subject to Executive Order 12291 and the Treasury-OMB implementation of that Order, dated April 29, 1983, because the final rule is not a major legislative rule. Accordingly, a Regulatory Impact Analysis is not required.

Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is Stuart G. Wessler of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and the Treasury Department participated in developing the regulations, on matters of both substance and style.

* * * * *

Adoption of amendments to the regulations.

Accordingly, 26 CFR Part 301 is amended as follows:

Paragraph 1. The authority for Part 301 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 2. Section 301.7701-4 is amended by revising paragraph (c) to read as follows:

§301.7701-4 Trusts.

* * * * *

(c) *Certain investment trusts*—(1) An "investment" trust will not be classified as a trust if there is a power under the trust agreement to vary the investment of the certificate holders. *See Commissioner v. North American Bond Trust*, 122 F.2d 545 (2d Cir. 1941), *cert. denied*, 314 U.S. 701 (1942). An investment trust with a single class of ownership interests, representing undivided beneficial interests in the assets of the trust, will be classified as a trust if there is no power under the trust agreement to vary the investment of the certificate holder. An investment trust with multiple classes of ownership interests will ordinarily be classified as an association or a partnership under §301.7701-2; however, an investment trust with multiple classes of ownership interests, in which there is no power under the trust agreement to vary the investment of the certificate holder, will be classified as a trust if the trust is formed to facilitate direct investment in the assets of the trust and the existence of multiple classes of ownership interests is incidental to that purpose.

(2) The provisions of paragraph (c)(1) of this section may be illustrated by the following examples:

Example (1): A corporation purchases a portfolio of residential mortgages and transfers the mortgages to a bank under a trust agreement. At the same time, the bank as trustee delivers to the corporation certificates evidencing rights to payments from the pooled mortgages; the corporation sells the certificates to the public. The trustee holds legal title to the mortgages in the pool for the benefit of the certificate holders but has no power to reinvest proceeds attributable to the mortgages in the pool or to vary investments in the pool in any other manner. There are two classes of certificates. Holders of class A certificates are entitled to all payments of mortgage principal, both scheduled and prepaid, until their certificates are retired; holders of class B certificates receive payments of principal only after all class A certificates have been retired. The different rights of the class A and class B certificates serve to shift to the holders of the class A certificates, in addition to the earlier scheduled payments of principal, the risk that mortgages in the pool will be prepaid so that the holders of the class B certificates will have "call protection" (freedom for premature termination of their interests on account of prepayments). The trust thus serves to create investment interests with respect to the mortgages held by the trust that differ significantly from direct investment in the mortgages. As a consequence, the existence or multiple classes of trust ownership is not incidental to any purpose of the trust to facilitate direct investment, and accordingly, the trust is classified as an association or a partnership under §301.7701-2.

Example (2): Corporation M is the orginator of a portfolio of residential mortgages and transfers the mortgages to a bank under a trust agreement. At the same time, the bank as trustee delivers to M certificates evidencing rights to payments from the pooled mortgages. The trustee holds legal title to the mortgages in the pool for the benefit of the certificate holders, but has no power to reinvest proceeds attributable to the mortgages in the pool or to vary investments in the pool in any other manner. There are two classes of certificates. Holders of class C certificates are entitled to receive 90 percent of the payments of principal and interest on the mortgages; class D certificate holders are entitled to receive the other ten percent. The two classes of certificates are identical except that, in the event of a default on the underlying mortgages, the payment rights of class D certificates holders are subordinated to the rights of class C certificate holders. M sells the class C certificates to investors and retains the class D certificates. The trust has multiple classes of ownership interests, given the greater security provided to holders of class C certificates. The interests of certificate holders, however, are substantially equivalent to undivided interests in the pool of mortgages, coupled with a limited recourse guarantee running from M to the holders of class C certificates. In such circumstances, the existence of multiple classes of ownership interests in incidental to the trust's purpose of facilitating direct investment in the assets of the trust. Accordingly, the trust is classified as a trust.

Example (3): A promoter forms a trust in which shareholders of a publicly traded corporation can deposit their stock. For each share of stock deposited with the trust, the participant receives two certificates that are initially attached, but may be separated and traded independently of each other. One certificate represents the right to dividends and the value of the underlying stock up to a specified amount; the other certificate represents the right to appreciation in the stock's value above the specified amount. The separate certificates represent two different classes of ownership interest in the trust, which effectively separate divided rights on the stock held by the trust from a portion of the right to appreciation in the value of such stock. The multiple classes of ownership interests are designed to permit investors, by transferring one of the certificates and retaining the other, to fulfill their varying investment objectives of seeking primarily either dividend income or capital appreciation from the stock held by the trust. Given that the trust serves to create investment interests with respect to the stock held by the trust that differ significantly from direct investment in such stock, the trust is not formed to facilitate direct investment in the assets of the trust. Accordingly, the trust is classified as an association or a partnership under §301.7701-2.

Example (4): Corporation N purchases a portfolio of bonds and transfers the bonds to a bank under a trust agreement. At the same time, the trustee delivers to N certificates evidencing interests in the bonds. These certificates are sold to public investors. Each certificate represents the right to receive a particular payment with respect to a specific bond. Under section 1286, stripped coupons and stripped bonds are treated as separate bonds for federal income tax purposes. Although the interest of each certificate holder is different from that of each other certificate holder, and the trust thus has multiple classes of ownership, the multiple classes simply provide each certificate holder with a direct interest in what is treated under section 1286 as a separate bond. Given the similarity of the interests acquired by the certificate holders to the interests that could be acquired by direct investment, the multiple classes of trust interests merely facilitate direct investment in the assets held by the trust. Accordingly, the trust is classified as a trust.

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ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved March 3, 1986.

J. ROGER MENTZ,
Acting Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on March 21, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 24, 1986, 51 F.R. 9950)

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.401: Employment taxes.
(Also Part I, Section 6053; 31.6053-3.)

Rev. Proc. 86-21

SECTION 1. PURPOSE

This revenue procedure pertains to employers and employees of certain large food or beverage establishments. It provides guidelines for such employers and employees who wish to petition the district director for the district in which the establishment is located regarding the percentage of gross receipts required under section 6053(c)(3)(A) of the Internal Revenue Code to be either reported by employees or allocated as tips. They may petition to reduce that percentage from 8 percent to a lower percentage (not below 2 percent). This revenue procedure amplifies and supersedes Rev. Proc. 85-4, 1985-1 C.B. 493, as modified by Rev. Proc. 85-10, 1985-1 C.B. 499. Those revenue procedures together provided guidance to employers for submitting petitions for a tip rate reduction to the district director and stated that additional guidance for employees would be issued upon publication of regulations.

SEC. 2. BACKGROUND

.01 Section 6053(c)(1) of the Code requires an employer of a large food or beverage establishment to report the following information to the Secretary for each calendar year at the time and manner prescribed by regulations:

(a) The gross receipts of the establishment from the provision of food and beverages (other than nonallocable receipts).

(b) The aggregate amount of charge receipts (other than nonallocable receipts).

(c) The aggregate amount of charged tips shown on the charge receipts.

(d) The sum of:

(1) the aggreagate amount reported by employees to the employer under section 6053(a), plus

(2) the amount the employer is required to report under section 6051 with respect to service charges of less than 10 percent.

(e) The amount allocated to each employee under section 6053(c)(3).

.02 Under section 6053(c)(3)(A) of the Code, as added by section 314(a) of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), 1982-2 C.B. 462, 562, an employer of a large food or beverage establishment, for purposes of that reporting, must allocate as tips among employees who perform services during any payroll period and who customarily receive tip income an amount equal to the excess of:

(1) 8 percent of the gross receipts (other than nonallocable receipts) of the establishment for the payroll period, over

(2) the total amount reported by the employees to the employer for the period.

.03 Under section 6053(c)(3)(B) of the Code, the employer must allocate the above amount according to a good faith agreement by the employer and the employees or, in the absence of such an agreement, in the manner determined by regulations.

.04 As originally enacted by TEFRA, section 6053(c)(3)(C) of the Code permitted the Secretary, upon petition of the employer, to reduce (but not below 5 percent) the percentage of gross receipts required to be allocated when the Secretary deternmined that the percentage of gross receipts constituting tips was less than 8 percent. The Tax Reform Act of 1984, section 1072, 1984-3 (Vol. 1) C.B. 1,560, amended section 6053(c)(3)(C), effective July 18, 1984, to include a majority of emnployees in one petitioning process and to allow reduction in the appropriate percentage as low as 2 percent. As amended, section 6053(c)(3)(C) provides that, upon the petition of either the employer or a majority of employees of such employer, the Secretary may reduce (but not below 2 percent) the percentage of gross receipts required to be allocated when the Secretary determines that the percentage of gross receipts constituting tips is less than 8 percent.

.05 Section 6053(c)(4) of the Code defines the term "large food or beverage establishment" to mean any trade or business (1) which provides food or beverages, (2) for which the tipping of employees serving food or beverages is customary, and (3) which normally employed more than 10 employees on a typical business day during the preceding calendar year.

.06 Under section 31.6053-3T(h)(1) and (2) of the Temporary Employment Tax Regulations, an employer or a majority of employees of an employer may petition the district director for the internal revenue district in which the establishment is located to have the percentage of the gross receipts that is used to determine the amount to be allocated under section 6053(c)(3)(A) of the Code reduced from 8 percent to a percentage that the petitioning employer or employees believe to be the actual percentage of the gross receipts that reflects the amount of tips for the establishment. The district director may thereafter reduce the percentage to the percentage the district director determines to be the proper estimate of the actual percentage of gross receipts constituting tips for the establishment, but not below 2 percent. The petition must be in writing and must include sufficient information to allow the district director to determine with reasonable accuracy the actual tip rate of the establishment.

.07 Under section 31.6053-3T(h)(3) of the temporary regulations, 8 percent of the gross receipts must continue to be used for purposes of complying with section 6053(c) of the Code until the district director notifies the employer in writing both of approval of a reduction of the percentage and of the term for which the reduced percentage is effective.

.08 Under section 31.6053-3T(h)(4) of the temporary regulations, a single petition may be made for 2 or more establishments if they are essentially the same type of business, they are located in the same internal revenue region, and a good faith determination has been made by the petitioner that the tip rates of the various establishments are essentially the same. Single petitions shall include the names and locations of the establishments for which a reduction is requested and the information required by section 3 for a typical establishment. A single petition for multi-establishments located in the same internal revenue region must be filed with the district director for the internal revenue district in which the greatest number of establishments included in the petition are located. If two or more districts have the same number of establishments and no other district has more, the petitioner may choose among those districts.

SEC. 3. PROCEDURES

REQUIREMENTS FOR ALL PETITIONS

.01 Employers and employees submitting a petition must clearly demonstrate that a rate less than 8 percent should apply. The petition must be in writing and contain the information listed below. If this information is not applicable or available, the petition should so state and, if necessary, explain why. The following must be contained in, or attached to, the petition:

(a) The employer's name, address, and employer identification number.

(b) The establishment's name, address, and establishment identification number.

(c) A detailed description of the establishment. This description should include any information the employer (or employees) believe would assist in determining the tip rate, such as:

(1) The type of restaurant, for example, lounge, sandwich shop, coffee shop,

(2) The days and hours of operation,

(3) A general description of the operation of the establishment, including the type of service provided by the staff and the type of self-service, if any,

(4) The person to whom the customer pays the check (waiter or waitress, cashier, etc.) and whether the check is paid before or after the meal,

(5) Whether alcoholic beverages are available,

(6) The past year's:

(A) total gross sales,

(B) total amount of charge sales,

(C) total amount of charge sales with charge tips,

(D) total amount of charge tips,

(E) total reported tips,

(F) total carry-out sales,

(G) percentage of sales representing breakfast, lunch, and dinner business,

(H) average dollar amount of the guest check,

(I) service charge, if any, added to the check, and

(J) percentage of sales with a service charge.

(7) Type of clientele.

(d) A copy of a representative menu for each meal.

.02 If an employer or employee files separate petitions in more than one district in the same region for establishments that are not essentially the same type of business, or do not have the same tip rate, each petition filed must indicate the name of any other district in which a petition has been submitted.

.03 Employers or employees of large establishments that may request rate reductions in 2 or more regions must state in each petition the name of any other Service region and district in which they have also submitted a petition so that consistent treatment may be obtained.

.04 The petition must contain the following statement.

"Under penalties of perjury, I/we declare that I/we have examined this petition, including accompanying documents and to the best of my/our knowledge and belief, the facts presented in support of this petition are true, correct, and complete." In the case of an employer petition, it should be signed by a responsible person who is duly authorized to make and sign a return, statement, or other document. An employee petition must be signed by each employee submitting the petition.

EMPLOYER PETITIONS

.05 In addition to the requirements of section 3.01, there must also be attached to employer petitions copies of any Form 8027, Employer's Annual Return of Tip Income and Allocated Tips, filed for the establishment for the three immediately preceding calendar years.

EMPLOYEE PETITIONS

.06 A majority (more than one-half) of all the directly tipped employees must consent to an employee-originated petition. For multi-establishment employers, the employee majority is more than one-half of the total number of directly tipped employees of all the establishments at the time the petition is filed. *See* section 31.6053-3T(h)(2)(iii) of the temporary regulations.

.07 In addition to the requirements of section 3.01, employee petitions must also state both the total number of directly tipped employees employed by the establishment and the total number of directly tipped employees consenting to the application. The employees must supply all necessary information that is available to them. Employees must promptly notify their employer of the petition. Upon receipt of the notification, the employer must promptly submit to the district director copies of any Form 8027 filed for the 3 immediately preceding calendar years. If the employer possesses relevant information, the employer should provide it to the district director upon either the employees' or the district director's request. Any information supplied by the employer during the petitioning process will not be disclosed by the Internal Revenue Service to any employees of the employer nor to representatives of such employees. Section 31.6053-3T-(h)(2)(iii)(B) of the temporary regulations.

SEC. 4. APPEAL RIGHTS

.01 Employers or employees who disagree with the district director's decision may file an administrative appeal stating the reason(s) for disagreement. The Appeals office will consider the appeal and advise the employer (employee) of its determination.

.02 Neither section 6053 of the Code nor any other section provides for administrative or judicial review of Appeals' determination.

SEC. 5. EFFECTIVE DATE

This revenue procedure is effective on April 28, 1986, the date of its publication.

SEC. 6. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 85-4, as modified by Rev. Proc. 85-10, is amplified and, as amplified, is superseded.

Merchant Marine Capital Construction Fund—Applicable Rate of Interest on Nonqualified Withdrawals

Notice 86-5

Under the authority in section 607(h)(4)(B) of the Merchant Marine Act, 1936, as amended (46 U.S.C. 1177(h)(4)(B)), we hereby determine and announce that the applicable rate of interest on the amount of additional tax attributable to any nonqualified withdrawals from a capital construction fund established under section 607 of the Act shall be 13.32 percent, with respect to nonqualified withdrawals made in the taxable year beginning in 1985.

The determination of the applicable rate of interest with respect to nonqualified withdrawals was computed, according to the joint regulations issued under the Act (46 CFR 391.7(e)(2)(ii)), by multiplying eight percent by the ratio which (a) the average yield on 5-year Treasury securities for the calendar year immediately preceding the beginning of such taxable year bears to (b) the average yield on 5-year Treasury securities for the calendar year 1970. The applicable rate so determined was computed to the nearest one-hundredth of one percent.

So ordered by: *Acting Deputy Administrator Maritime Administration.*

Administrator, National Oceanic and Atmospheric Administration.

Assistant Secretary for Tax Policy, *Department of the Treasury.*

Dated: March 3, 1986.

Richard E. Bowman,
Acting Deputy Maritime Administrator.
Anthony J. Galio,
Administrator, National Oceanic and Atmospheric Administration.

J. Roger Mentz,
Acting Assistant Secretary for Tax Policy.

(Filed by the Office of the Federal Register on March 7, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 10, 1986, 51 F.R. 8270)

Nonconventional Source Fuel Credit Notice 86-6

ACTION: Publication of inflation adjustment factor and reference price for calendar year 1985 as required by section 29(d)(2)(A) of the Internal Revenue Code (26 U.S.C. 29(d)(2)(A) (formerly 44D renumbered by the Tax Reform Act of 1984 [Pub.L. 98–369, 1984-3 C.B. (Vol. 1) 1]).

SUMMARY: The inflation adjustment factor and reference price are used in determining the availability of the tax credited for production of fuel from nonconventional sources under section 29 of the Internal Revenue Code.

DATE: The 1985 inflation adjustment factor and reference price apply to qualified fuels sold during calendar year 1985.

INFLATION FACTOR: The inflation adjustment factor for calendar year 1985 is 1.4211.

PRICE: The reference price for all qualified fuels is $24.08 per equivalent barrel for the 1985 calendar year.

Because the above reference price does not exceed $23.50 multiplied by the inflation adjustment factor, the phaseout of credit provided for in section 29(b)(1) of the Internal Revenue Code does not occur for any qualified fuel based on the above reference price.

NOTE.—After December 31, 1984, gas produced from a tight formation that also falls under any of the categories of gas specified in 18 CFR 272.103(a) (as amended) under the Natural Gas Policy Act of 1978 (NGPA) will no longer be eligible for the credit allowed by section 29 (formerly section 44D) of the Internal Revenue Code.

FOR FURTHER INFORMATION CONTACT:

For the information factor—*Robert O'Keefe, PM:PFR:R, 1111 Constitution Avenue, N.W., Internal Revenue Service, Washington, D.C. 20224, Telephone Number (202) 376-0720 (not a toll-free number).*

For the reference price—*Noel J. Sheehan, CC:C:E:1:2, Room 5232, Internal Revenue Service, 1111 Constitute Avenue, N.W., Washington, D.C. 20224, Telephone Number (202) 566-4463 (not a toll-free number).*

Peter K. Scott
Acting Deputy, Associate Chief Counsel (Technical).

(Filed by the Office of the Federal Register on March 7, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 10, 1986, 51 F.R. 8271)

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Tax Shelter Registration

LR-66-85

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary regulations relating to tax shelter registration. The text of those temporary regulations also serves as the comment document for this proposed rulemaking.

DATES: Written comments and requests for a public hearing must be delivered by May 5, 1986. The amendments are proposed to be effective generally with respect to tax shelters in which any interest is first sold after August 31, 1984.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-66-85), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Paulette Chernyshev, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) telephone 202-566-3288 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

The temporary regulations (designated by a "T" following the section citation) * * * [on page 22, this Bulletin] amend Parts 301 and 602 of Title 26 of the Code of Federal Regulations. These amendments change the rules relating to tax shelter registration under section 6111 of the Internal Revenue Code of 1954, as added by section 141 of the Tax Reform Act of 1984 (Pub. L. 98-369, 98 Stat. 678 [1984-3 C.B. (Vol. 1) 1, 190]. For the text of the temporary regulations, see FR Doc. 86-4683 (T.D. 8078) published * * * [on page 22, this Bulletin]. The preamble to the temporary regulations provides a discussion of the rules. The final regulations, which this document proposes to base on those temporary regulations, would amend Parts 301 and 602 of Title 26 of the Code of Federal Regulations.

EXECUTIVE ORDER 12291; REGULATORY FLEXIBILITY ACT

The Commissioner of Internal Revenue has determined that this proposed rule in not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required.

Although this document is a notice of proposed rulemaking that solicits public comments, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Buidling, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies of those comments to the Service.

DRAFTING INFORMATION

The principal author of these regulations is Paulette Chernyshev of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on March 3, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 4, 1986, 51 F.R. 7454)

Foundations Status of Certain Organizations

Announcement 86-54

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

All Housing Inc., Oakland, CA
American Decorative Arts Forum of North Carolina, San Francisco, CA
B.G.S.U. Sig Ep Foundation, Bowling Green, OH
Bashful Unicorn, San Francisco, CA
Bear Valley Springs Pavilion Society, Tehachap, CA
Bible Is Proclaiming, Inc., The, St. Petersburg, FL
Big Brothers/Big Sisters of Fulton County, Inc., Rochester, IN
Books for Special Kids, Inc., San Francisco, CA
Bridge of Life, San Jose, CA
Buhach Pre-School Inc., Merced, CA

C.W. Vanover Evangelistic Association, Waverly, OH
Cadillac Area College Consortium, The, Cadillac, MI
Cal Reentry, Inc., Woodland, CA
Carl Gallion Evangelistic Association, Inc., The, Ashland, KY
Catticus Corporation, Santa Barbara, CA
Central California Association for the Disabled, Bakersfield, CA
Central States Education Fund, Chicago, IL
Chic Street Man's New School for Performance, Santa Barbara, CA
Chicanos in Action, San Jose, CA
Christ Holy Love Mission, Inc., Oakland, CA
Christian Study Center, Youngstown, OH
Cincinnati Gospel Music Workshop, The, Cincinnati, OH
Clearwater High School Marine Corps Junior ROTC Booster Club, Inc., Clearwater, FL
Clive Firefighters Association, Clive, IA
Coal Information Network of Kentucky, Madisonville, KY
Coalition for Handicapped Childrens Education, Inc., Las Vegas, NV
Columbia Band Boosters, Columbia Station, OH
Coming of Age, San Francisco, CA
Commission on Education and Career Development, Oakland, CA
Community Services Agency 202 Program, Inc., Reno, NV
Consensus, Inc., Carson City, NV
Covered Bridge Foundation, Felton, CA
Cristaccia, Inc., Grove City, OH
Cystinosis Foundation of California Inc., Oakland, CA
DPI Education and Research Fund, Inc., Detroit, MI
Donald Allen Danes Family Organization, The, Kuna, ID
Echo-Wood Lake Athletic Booster Club, Inc., Wood Lake, MN
Education and Technology Foundation, Dale City, CA
Eternal Life Evangelistic Association, Canton, OH
Evening Optimist Foundation of Madison, Madison, WI
Faith Community Services, Inc., North Las Vegas, NV
Family and Living Skills Corporation, San Jose, CA
Fellowship Center for Biblical Studies, Bainbridge, PA
Fenix Service Corp., Watsonville, CA
Fisheries Protection Institute, Santa Barbara, CA
Foundation for Independent Living, Berkeley, CA
Foundation for the Educational Development of Monterey Peninsula College, Monterey, CA
Foundation for the Survival of the Handicapped, Columbus, OH
Fountain Gate Christian Home for Children, Inc., Santa Rosa, CA
Friends at the Beloit Library Inc., The, Beloit, WI
Friends of DTA, Las Vegas, NV
Friends of the Freedom Library, Freedom, CA
Friends of the Griffith Quarry, Inc., Penryn, CA
Full Circle Community Center, Inc., Ypsilanti, MI
Gathering Place of Rockford, The, Rockford, IL
Gifted Challenge Institute, Stow, OH
Greenfield, Bainbridge and Waverly Scenic Railroad, Inc., The, Bainbridge, OH
Growth, Achievement, and Progress Corp., Grand Rapids, MI
Handicappers Northwest, Portland, OR
Howard Homes, Inc., Detroit, MI
Hubbard County Food Shelf, Park Rapids, MN
Humane Society of Collinsville Inc., Collinsville, IL
International Medical Institute of San Francisco, San Francisco, CA
Jewish Association of Concerned Citizens, Des Moines, IA
Jewish Council for Retarded Citizens, Inc., The, University Heights, MI
Junior Tennis Council of St. Louis, St. Louis, MO
Just Another Summer Theatre, Newark, OH
Juvenile Diversion Program and Runaway Services of Jackson County, Inc., Jackson, MI
Kings' Kids Club, Inc., The, Legrane, KY
Kiwanis Club of Northville Foundation, Inc., Northville, MI
Knights of Columbus Mental Retardation Foundation of Nebraska, Bellevue, NE
Lincoln Education Action Foundation, Stockton, CA
Little Italy Redevelopment Association, The, Cleveland, OH
Loma Frieta Community Foundation, Cupertino, CA
Lubavitch Foundation, Oak Park, MI
Maacos Amateur Girls Instructional and Competitive Softball Organization, North Highlands, CA
Manitou Society, The, Ann Arbor, MI
Martinez Ensemble Theatre Association, Martinez, CA
Mendocino-Lake Area Agency on Aging, Ukiah, CA
Mercy Riverside Manor, Inc., Red Bluff, CA
Michigan Vietnam Veteran's Leadership Program, Inc., Pontiac, MI
Morning Glory Community Services, Inc., Muskegon, MI
Museum Guild of Southern Nevada, Las Vegas, NV
National League of Cuban American Community-Based Centers, Inc., The, Fort Wayne, IN
National Youth Science Camp Foundation, Inc., Montgomery, WV
Native American Heritage, Inc., Columbus, OH
Nevada Sage Inc., Reno, NV
New Community Inc., Richmond, CA
New Gerlach Hot Springs Inc., Gerlach, NV
New Hope Gardens, Inc., Cincinnati, OH
New Horizon Community Development Corporation, Chicago, IL
Norcal Marching Band Review, Inc., Foster City, CA
North Bay Jewish Community Center, IO49, Santa Rosa, CA
Observer Foundation, Sacramento, CA
On the Job, Inc., Berkeley, CA
Operation Food Basket, Inc. of Paris Bourbon County, Paris, KY
Parental Stress Hotline and Services of Greater San Jose, Inc., San Jose, CA
Pathfinder House, Inc., Lima, OH
Peninsula Addicts/Alcoholics Together, Burlingame, CA
Phoenix Theatre, Inc., Indianapolis, IN
Pleasanton Girls Softball League, Pleasanton, CA
Pocahontas County Senior Citizens, Inc., Marilinton, WV
Private Industry Council of Gary Indiana, Inc., Gary, IN
Professional Athletes Ministry, Inc., Concord, CA
Progressive Young Adult Center, Detroit, MI
Public Interest Advocacy Resource, Chicago, IL

Relief-Line, Inc., Layfayette, IN
Religious Association for Spiritual Betterment, Sacramento, CA
Richmond Little League, Richmond, MO
Roderick Senior Citizens Center, Hayfork, CA
Roosevelt Youth Soccer League, Fresno, CA
St. Nicholas House Foundation, Newport, R.I.
San Francisco Art Glass Guild, San Francisco, CA
San Luis Obispo County Special Games, San Luis Obispo, CA
Santa Barbara County Association for Gifted and Talented Education, Santa Barbara, CA
Santa Barbara Dance Alliance, Santa Barbara, CA
Santa Cruz Film Council, Inc., Santa Cruz, CA
School of Education Alumni Association San Jose State University, San Jose, CA
Smith Gerontological Society, Rio Dell, CA
Sound Foundation, Las Vegas, NV
South Dakota Inventors Congress, Inc., Watertown, SD
South Monterey County Youth Soccer League, Soledad, CA
Spokane Historic Preservation Foundation, Spokane, WA
Starrick Outreach Ministries, Johnston City, IL
State Health Education Council of West Virginia, Charleston, WV
Steven S. Brown Ministries, Hayward, CA
Superior California Humane Society, Inc., Paradise, CA
Supporters of Clawson Scamp, Clawson, MI
Tiger Pride Committee, Inc., Tigard, OR
True Spirit, Inc., Decter, MI
Tuesday Optimist Foundation of Racine, Inc., Racine, WI
United Ministries In Music, Russellville, KY
Universal Christian Fellowship, Southfield, MI
UP-Wingers, Inc., New York, NY
Visionary Performing Artists Inc., Napa, CA
Volunteer Action Center of Dade County, Inc., Miami, FL
Wellspring, Inc., Nashville, TN
West Coast Actors, Theatre, Roseville, CA
Workplace, Inc., The, Mound, MN
Womens Action for Survival Education Fund, Inc., San Francisco, CA
Writers West of Alameda, Alameda, CA
Youth Advocate Program, Eaton Rapids, MI
Youth Orchestra of Monterey County, Seaside, CA
ZebrAwareness, Spokane, WA
Zohar Dance Company, Palo Alto, CA

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Establishment of the Office of the Associate Chief Counsel (International)

Announcement 86-56

The Service has announced that, effective March 17, 1986, all international functions within the Office of Chief Counsel were consolidated into the Office of Associate Chief Counsel (International). Previously, the National Office international legal and technical support responsibilities were divided among various offices within the Chief Counsel's office.

The Office of the Associate Chief Counsel (International) is responsible for addressing issues raised by taxpayers that concern the U.S. taxation of international transactions and is currently attempting to determine the areas in which guidance is needed in the form of regulations or published rulings. Taxpayers and tax practitioners are encouraged to submit issues for consideration either orally or in writing to Kevin Dolan, Associate Chief Counsel (International), Internal Revenue Service, Washington, D.C. 20224, Attn: CC:INTL, Room 3042, (202) 566-9060 (not a toll-free number).

Limitations on Alternative Benefits—Public Hearing

Announcement 86-57[1]

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to certain restrictions on an employee's right to receive alternative forms of benefit under qualified plans.

DATES: The public hearing will be held on Thursday, May 22, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Thursday, May 8, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Chief Counsel Conference Room, Fourth Floor, Room 4415, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, ATTN: CC:LR:T (EE-95-84), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935 (not a toll-free call).

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under sections 401 and 411 of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Thursday, January 30, 1986 (51 FR 3798) [EE-95-84, 1986-9 I.R.B. 25].

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Thursday, May 8, 1986, an outline of the oral comments to be presented at the hearing and the time they wish to devote to each subject.

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[1] Filed by the Office of the Federal Register on April 9, 1986, 8:45 a.m., and published in the issue of the Federal Register for April 10, 1986, 51 F.R. 12340.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions, attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

Effective Dates for Rev. Rul. 86-7 and Rev. Rul. 86-58

Announcement 86-58

The effective date for Rev. Rul. 86-7, 1986-4 I.R.B. 6, is April 18, 1985, the determination date of that ruling.

The effective date for Rev. Rul. 86-8, 1986-4 I.R.B. 6, is April 1, 1985, the determination date of that ruling.

These effective dates will appear with the rulings in the 1986-1 Cumulative Bulletin.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Louis Crown	Bayside, NY	Certified Public Accountant	Indefinite from March 14, 1986
David H. Heilman	Council Grove, KS	Attorney	Indefinite from March 14, 1986
Beryl W. Markwell	Elmhurst, IL	Certified Public Accountant	Twenty-four Months from March 20, 1986
Marc Pozner	Tenafly, NJ	Certified Public Accountant	Indefinite from March 14, 1986
A. Russel Lucid	Norwell, MA	Attorney	Indefinite from March 26, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before their Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Thomas G. Abernethy, Jr.	Jackson, MS	Attorney	March 7, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.72-4, 1.72-5, 1.72-6, 1.72-7, 1.72-9, 1.72-11, 1.403(b)-1(d)(4), 1.403(b)-1(d)(4)(ii), amended; 1.403(b)-1(d)(4)(iv), 1.401(a)-18, 1.401(j)-1 through 1.401(j)-6, removed; 1.403(b)-1(d)(4)(iv), added.	Unisex annuity tables	1986-16 I.R.B. 9	May 8, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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*Denotes entry since last publication

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78-24
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80-42
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81-52
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86-16, 1986-12, I.R.B. **13**

81-62
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86-18, 1986-13 I.R.B. **40**

82-32
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86-20, 1986-15 I.R.B. **50**

83-87
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86-17, 1986-13 I.R.B. **40**

84-36
Modified by
86-17, 1986-13 I.R.B. **40**

84-37
Modified by
86-17, 1986-13 I.R.B. **40**

84-41
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84-81
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86-7, 1986-6 I.R.B. **28**

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86-5, 1986-4 I.R.B. **9**

85-22
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86-3, 1986-1 I.R.B. **26**

85-24
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86-3, 1986-1 I.R.B. **26**

85-27
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86-3, 1986-1 I.R.B. **26**

85-28
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55-650
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86-37, 1986-10 I.R.B. **5**

55-651
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86-37, 1986-10 I.R.B. **5**

56-557
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86-4, 1986-2 I.R.B. **5**

58-114
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86-37, 1986-10 I.R.B. **5**

58-522
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86-37, 1986-10 I.R.B. **5**

58-610
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86-44, 1986-13 I.R.B. **39**

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86-10, 1986-4 I.R.B. **7**

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86-37, 1986-10 I.R.B. **5**

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86-37, 1986-10 I.R.B. **5**

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[1] See footnote at end of list.

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*Denotes entry since last publication

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80-8
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86-57, 1986-16 I.R.B. **4***

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86-9, 1986-4 I.R.B. **6**

81-212
Amplified by
86-47, 1986-14 I.R.B. **4**

82-47
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86-45, 1986-13 I.R.B. **36**

84-80
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86-30, 1986-8 I.R.B. **24**

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

LR-189-84, page 4.

Proposed amendments to the regulations relate to debt instruments with original issue discount, to imputed interest or deferred payment sales or exchanges of property, and to safe haven interest rates for commonly controlled taxpayers.

Finding Lists begin on page 85.
Announcement of Disbarments and Suspensions begin on page 81.
Announcement of Notice of Proposed Rulemaking on page 83.
Monthly Index for April begins on page 88.

Department of the Treasury
Internal Revenue Service

T 22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

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Part IV. Items of General Interest

Notice of Proposed Rulemaking

Debt Instruments With Original Issue Discount; Imputed Interest on Deferred Payment Sales or Exchanges of Property; and Safe Haven Interest Rates for Commonly Controlled Taxpayers

LR-189-84

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to: (1) The tax treatment of debt instruments issued after July 1, 1982, that contain original issue discount, (2) the imputation of and the accounting for interest with respect to sales and exchanges of property occurring after December 31, 1984, and (3) safe haven interest rates for loans or advances between commonly controlled taxpayers and safe haven leases between such taxpayers. Changes to the applicable law were made by the Tax Equity and Fiscal Responsibility Act of 1982 as amended by the Technical Corrections Act of 1982, and the Tax Reform Act of 1984 as amended by Pub. L. 98-612 and Pub. L. 99-121. The regulations would provide needed guidance to taxpayers who must comply with these provisions of the law.

DATES:

Proposed Effective Date: Generally, the regulations contained in this document are proposed to be effective as follows:

§ 1.163-7, §§ 1.1271-1 to 1.1273-2, §§ 1.1275-1 to 1.1275-5—Debt instruments issued after July 1, 1982
§§ 1.483-1 to 1.483-5, §§ 1.1274-1 to 1.1274-7—Sales or exchanges of property occurring after December 31, 1984
§ 1.1274A-1—Certain sales or exchanges of property occurring after June 30, 1985
§ 1.446-2—Lending transactions occurring after May 8, 1986 certain sales or exchanges of property occurring after December 31, 1984
§ 1.482-2—Term loans and advances entered into after and demand loans and advances after such date

Dates for Comments and Request for a Public Hearing: Written comments and request for a public hearing must be delivered or mailed by June 9, 1986.

ADDRESS: Send comments (preferably eight copies) and request for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T, (LR-189-84), 1111 Constitution Avenue, NW., Washington, DC 20224.

FOR FURTHER INFORMATION CONTACT: Theresa E. Bearman (sections 163, 1271, 1272, 1273, 1275 and related matters), Ewan D. Purkiss (sections 446, 483, 1274 and related matters), Susan T. Baker (all matters other than those relating to sections 446, 482 and 483), or Joseph M. Rosenthal (section 482 and related matters) of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC 20224 (Attention: CC:LR:T LR-189-84). Telephone 202-566-3829 (Bearman), 202-566-3238 (Purkiss), 202-566-3294 (Baker), 202-566-3289 (Rosenthal) not a toll-free call).

SUPPLEMENTARY INFORMATION:

I. Background

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part I) under sections 163(e), 446, 482, 483 and 1271 through 1275 of the Internal Revenue Code of 1954. With the exception of the amendments to the regulations under section 446, these amendments are proposed to conform the regulations to section 231 of the Tax Equity and Fiscal Responsibility Act of 1982 (96 Stat. 324, 496), as amended by section 306 of the Technical Corrections Act of 1982 (97 Stat. 448), and sections 41, 42 and 44 of the Tax Reform Act of 1984 (98 Stat. 494, 531) as amended by Pub. L. 98-612 (98 Stat. 3180) and Pub. L. 99-121 (99 Stat. 505). The amendments to the regulations under section 446 are proposed to provide rules to account for interest in transactions outside the scope of the original issue discount rules.

II. Introduction

The regulations under sections 163(e), 483, and 1271 through 1275 provide two principal sets of rules: The imputed interest rules and the original issue discount rules. The imputed interest rules are prescribed by sections 1274 and 483, and the original issue discount rules by sections 163(e), 1271, 1272, 1273 and 1275.

The imputed interest rules of sections 1274 and 483 relate to the measurement of interest and principal for tax purposes in a sale or exchange of property (other than publicly traded property) involving deferred payments. For transactions subject to the imputed interest rules, interest will be imputed to the transaction if a minimum amount of interest is not stated. If a transaction states at least the minimum amount of interest, it is said to provide for adequate stated interest. When interest is imputed to a transaction, a portion of the stated principal amount of the debt instrument is recharacterized as interest for tax purposes. The imputed interest rules do not require an increase in the total amount of payments agreed to by the parties to a transaction. These rules merely recharacterize as interest for Federal tax purposes a portion of the payments denominated as principal by the parties. In the case of transactions to which section 1274 applies, imputed interest is treated as original issue discount and is accounted for under those rules. In the case of transactions subject to section 483, imputed interest (and any stated interest) is subject to a new set of rules provided under section 446 and is accounted for under those rules.

In general, under the original issue discount rules, a portion of the original issue discount on a debt instrument is required to be included in income by the holder and deducted from income by the issuer annually without regard to their regular accounting methods. The total amount of original issue discount is defined as the difference between the debt instrument's stated redemption price at maturity and its issue price and arises in one of three ways. First, in the case of a debt instrument subject to section 1274 that does not provide for adequate stated interest, interest is imputed and is treated as original issue discount. Second, in the case of a debt instrument issued for cash or publicly traded property, original issue discount arises if the debt instrument is issued for less than its face amount. Third, in the case of all debt instruments, original issue discount arises if the debt instrument does not call for interest that is payable currently at a single constant rate over its entire term.

III. The Imputed Interest Rules

A. Applicability

1. Section 1274

Section 1274 applies to any debt instrument issued in exchange for property if neither the debt instrument nor the property is publicly traded and if one or more of the payments under the debt instrument are due more than 6 months after the date of the sale or exchange. Section 1274, however, does not apply to the following:

(a) Certain sales or exchanges by an individual, estate, testamentary trust, or small corporation or partnership of a farm if the sales price of the farm does not exceed $1,000,000;

(b) Any sale or exchange by an individual of the individual's principal residence, regardless of the amount of the sales price;

(c) Any sale or exchange of property if the sum of all the payments (including principal and interest) under any debt instrument and the value of any other consideration does not exceed $250,000;

(d) Any debt instrument issued in a qualified sale within the meaning of section 483(e) if the stated principal amount of the debt instrument does not exceed $500,000; and

(e) Any cash method debt instrument within the meaning of section 1274A(c).

2. Section 483

Section 483 applies to sales or exchanges of non-publicly traded property excepted from the provisions of section 1274. Thus, section 483 applies to: the sale or exchange of a farm if the sales price does not exceed $1,000,000, sales involving total payments of $250,000 or less, sales of principal residences, qualified sales of land, and cash method debt instruments. Unlike section 1274, however, section 483 applies only if the contract for the sale or exchange calls for payments due more than one year from the date of the sale or exchange. Section 483 does not apply to the following:

(a) Any sale or exchange of property if the sales price does not exceed $3,000; and

(b) In the case of a purchaser, any amount that is treated as containing interest under section 163(b).

3. Exceptions From Both Sections 1274 and 483

The imputed interest rules of sections 1274 and 483 do not apply to the following:

(a) Any transaction to the extent any amount is contingent upon the productivity, use, or disposition of property and entitled to capital gain treatment under section 1235, relating to sales or exchanges of patents.

(b) Any annuity under section 72 that is not a debt instrument within the meaning of section 1275(a).

(c) Any issuer (obligor) of a debt instrument issued for property that is personal use property in the hands of the issuer. The imputed interest rules, however, apply to any holder (obligee) of the debt instrument unless the loan incurred in the transaction is a below-market loan of the type described in section 7872(c)(1)(A)–(C). The treatment of the latter class of debt instruments is governed by the provisions of section 7872.

(d) Any debt instrument that evidences demand loan (within the meaning of section 7872(f)(5)) and is a below-market loan of the type described in section 7872(c)(1)(A)–(C). The treatment of these debt instruments is governed by the provisions of section 7872.

B. Stating Adequate Interest To Avoid the Imputation of Interest

1. In General

To prevent the imputation of interest, a debt instrument must provide for adequate stated interest. For this purpose, a debt instrument generally provides for adequate stated interest if it calls for interest over its entire term at a rate no lower than the test rate of interest applicable to the debt instrument. If a debt instrument does not provide for a fixed rate of interest at least equal to the test rate of interest, the adequacy of interest is determined by comparing the stated principal amount involved in the transaction with the sum of present values of all payments due under the debt instrument, determined by discounting the payments at a rate equal to the test rate of interest. A debt instrument generally has adequate stated interest if the stated principal amount of debt instrument is less than or equal to the sum of these present values. However, in the case of a potentially abusive situation as discussed below, the debt instrument does not have adequate stated interest unless the stated principal amount is less than or equal to the fair market value of the property sold or exchanged.

The test rate of interest applicable to a debt instrument generally depends on the amount of seller financing (based on stated principal) involved in the transaction. For sales or exchanges of property (other than new section 38 property) involving seller financing of $2,800,000 or less, the test rate of interest is the lower of the applicable Federal rate or 9 percent, compounded semiannually (or an equivalent rate based on an appropriate compounding period). If the sales price is contingent, the 9 percent rate is not available unless the sales price cannot exceed $2,800,000. For sales or exchanges of property with seller financing in excess of $2,800,000, and all sales or exchanges of new section 38 property, the test rate of interest is 100 percent of the applicable Federal rate. For sales or exchanges of property involved in sale-leaseback transactions, the test rate of interest is 110 percent of the applicable Federal rate. These rules also apply to transactions subject to section 483. Sales or exchanges that are qualified sales, however, are subject to a special lower test rate of interest as discussed below. For sales or exchanges occurring before July 1, 1985, special test rates of interest apply.

The applicable Federal rate is either the Federal short-term rate (for debt instruments with terms not over 3 years), the Federal mid-term rate (for debt instruments, with terms over 3 years but not over 9 years), or the Federal long-term rate (for debt instruments with terms over 9 years). The Federal rates are annual stated rates of interest based on semiannual compounding. The Federal rates are published monthly by the Commissioner in Revenue Rulings along with equivalent annual, quarterly and monthly rates. In general, the appropriate compounding period depends on the intervals between payments. In general, the applicable Federal rate is the lowest of the rates in effect for the first month in which there is a binding written contract or the two preceding two months.

The applicable Federal rates are determined monthly. The Federal rates are based on the yields to maturity of outstanding marketable obligations of the United States of similar maturities (for example, maturities up to 3 years for the Federal short-term rate) for the one-month period ending on the 14th day of the month preceding the month for which the rates are applicable. In certain cases, the applicable Federal rate may be a lower rate based on certain allowable Treasury index rates.

2. Special Rules

a. *Test Rate for Installment Obligations.* The proposed regulations provide special rules for determining whether an installment obligation provides for adequate stated interest. For self-amortizing installment and level-principal obligations, tables are provided under which the test rate of interest may be computed as a blended rate equal to a weighted average of the Federal rates. In general, the rules are designed to allow taxpayers to receive the benefit of the short-term and mid-term rates (which are generally lower than the long-term rate) without having to provide three separate debt instruments.

b. *Contingent Payments.* In general, contingent interest payments are not taken into account in applying the imputed interest rules. Thus, whether a debt instrument states adequate interest will be determined by ignoring any contingent interest payments.

Under a special rule proposed by the regulations, however, the stated principal amount of a debt instrument calling for contingent payments of interest will be respected in certain cases. To qualify for the special rule, the contingent payments of interest must be conditioned on a return from the use of the property. In addition, the debt instrument must call for fixed payments of interest equal to at least 80 percent of the test rate of interest applicable to the debt instrument, and it must be reasonable to expect that the payments of contingent interest will raise the yield on the debt instrument to at least the test rate of interest. If the property acquired for the debt instrument is depreciable or inventoriable property, then, in addition to the requirements noted above, the term of the debt instrument cannot exceed 4 years in the case of 3-year or 5-year property or inventoriable property, or 12 years in the case of any other depreciable property that is not inventoriable property.

The contingent payment rules do not affect whether rights to receive contingent payments constitute debt or equity for Federal tax purposes or whether an instrument evidences a valid indebtedness.

c. *Variable Rate Debt Instruments.* For purposes of determining whether a debt instrument calling for variable interest based on current values of an objective interest index provides for adequate stated interest, the proposed regulations generally treat the debt instrument as if it called for interest at a fixed rate equal to the rate established by the index on the date the test rate of interest is determined. Examples of objective indices include the prime rate, the applicable Federal rate, the average yield on Treasury securities, the LIBOR (London Interbank Offered Rate). If the rate of interest determined by the index is no lower than the test rate of interest, the debt instrument has adequate stated interest. Interest payments based on an index other than an objective interest index are generally treated as contingent payments.

Under the proposed regulations, the applicable Federal rate for a variable rate debt instrument that calls for variable interest payments based on current values of an objective interest index is the Federal rate corresponding to the adjustment interval of the debt instrument. Thus, for example, if the interest rate on a debt instrument is tied to a bank's prime rate and adjusted annually, the adequacy of interest is determined by testing the rate of interest as determined by the index against the Federal short-term rate.

d. *Qualified Sales of Land.* In the case of a debt instrument issued in a qualified sale of land and subject to the rules of section 483(e), the test rate of interest is 6 percent, compounded semiannually. A qualified sale is a sale or exchange of land by an individual to a member of the individual's family. A debt instrument issued in a qualified sale is subject to the rules of section 483(e) if the face amount (stated principal amount) of the debt instrument issued for the land does not exceed $500,000, regardless of the amount of the sales price, and if certain other conditions are satisfied. Thus, the parties are free to structure a sale with two debt instruments, the first having a face amount of $500,000 and a 6 percent interest rate, and the second subject to the rules of section 1274 or section 483, whichever is applicable. If, however, a single debt instrument is issued with a face amount in excess of $500,000, the 6 percent test rate does not apply.

The proposed regulations contain this rule because the Service is concerned with the complexity of rules that would be necessary to apply two different accounting rules to a single debt instrument. The Service invites comments on this proposed rule.

3. Potentially Abusive Transactions

Regardless of the amount of interest stated in a sale or exchange, if the transaction is a potentially abusive transaction, the adequacy of interest is determined by comparing the stated principal amount of the debt instrument with the fair market value of the property sold or exchanged as discussed above. A potentially abusive situation includes any transaction that is a tax shelter (within the meaning of section 6661(b)(2)(C)(ii)), and any situation involving recent sales transactions, nonrecourse financing, and financing with a term in excess of the economic life of the property. In addition, under regulatory authority, the proposed regulations categorize as potentially abusive situations transactions involving foreign currency. The potentially abusive situation rules also may apply to cash method debt instruments (which are described in greater detail below) subject to section 483.

4. Assumptions and Modifications

Sections 1274 and 483 do not apply to a debt instrument assumed or taken subject to in a sale or exchange occurring after June 30, 1985, or a debt instrument issued before October 16, 1985, assumed or taken subject to in a sale or exchange involving a sales price of $100,000,000 or less occurring after December 31, 1984, and before July 1, 1985, unless the debt instrument is modified. The proposed regulations provide special rules for a debt instrument issued after October 15, 1984, or any debt instrument involved in a transaction with a sales price in excess of $100,000,000 that is assumed or taken subject to in a sale or exchange occurring after December 31, 1984, and before July 1, 1985, and that is not modified as part of the sale or exchange.

If a debt instrument assumed or taken subject to is modified, the modification is treated as a separate transaction. In general, a modified debt instrument is treated as a new debt instrument given in exchange for the old debt instrument in a transaction to which section 1274 applies. If a modification is attributable to the seller the modification is treated as occurring immediately before the sale or exchange, and the buyer is treated as assuming the modified debt instrument. Modifications are attributable to the seller unless the seller neither consents to nor participates in the modification. If a modification is attributable to the buyer, the modification is treated as occurring immediately after the sale or exchange.

With certain exceptions, sections 1274 and 483 apply to a debt instrument issued after October 15, 1984, or a debt instrument involved in a transaction with a sales price in excess of $100,000,000 that is assumed or taken subject to and that is not modified as part of a sale or exchange occurring after December 31, 1984, and before July 1, 1985. In these cases, sections 1274 and 483 apply only for purposes of determining the tax consequences of the sale or exchange to the buyer.

C. Imputation of Interest

Under section 1274, if a debt instrument does not provide for adequate stated interest, the issue price of the debt instrument is its imputed principal amount. Except in the case of potentially abusive situations, the imputed principal amount of a debt instrument is the sum of the present values of all the payments due under the instrument determined by discounting the payments at the imputed rate of interest. Generally, for purposes of imputing interest, the imputed rate of interest is the same as the test rate of interest. For sales or exchanges occurring before July 1, 1985, special imputed rates of interest apply.

When interest is imputed, the imputed principal amount becomes the issue price. This issue price is lower than the stated principal amount of the debt instrument, since it reflects the fact that a portion of the stated principal is recharacterized as interest. Thus, the imputed interest is treated as original issue discount. In potentially abusive situations, the imputed principal amount of the debt instrument is the fair market value of the property sold or exchanged.

Under section 483, imputed interest is referred to as unstated interest. Unstated interest is defined as the excess of the deferred payments (all payments of the sales price due more than 6 months after the date of the sale or exchange) over the sum of the present values of the deferred payments and any stated interest. For this purpose, the present values are determined by discounting the payments at the imputed rate of interest. In the case of cash method debt instruments to which the potentially abusive rules apply, the fair market value of the property sold or exchanged is used in place of the present value of the deferred payments and any stated interest.

IV. Accounting for Original Issue Discount

A. In General

Original issue discount is defined as the excess of a debt instrument's stated redemption price at maturity over its issue price. A portion of the original issue discount on a debt instrument is accounted for on a current basis by both the issuer and the holder. The amount of original issue discount that is accounted for on a current basis is the amoaunt that accrues on a constant interest or economic accrual basis, regardless of whether the issuer or holder is an accrual basis taxpayer.

For purposes of determining the accrual of original issue discount, the term of a debt instrument generally is divided into accrual periods of equal length as discussed in greater detail below. Original issue discount is allocated to each accrual period according to a formula based upon the adjusted issue price of the debt instrument at the beginning of the accrual period, the yield of the debt instrument, and the actual interest payments (if any) for that period. To determine the holder's annual inclusion under section 1272, the original issue discount allocated to each accrual period is then apportioned ratably among the days within the accrual period to produce the daily portion of original issue discount for each day during that accrual period. The total amount of original issue discount includible for any taxable year is the sum of the daily portions of original issue discount for each day during the taxable year that the taxpayer held the debt instrument.

Debt instruments excepted from the current inclusion rule are debt instruments with a term of one year or less, tax-exempt obligations, debt instruments issued by a natural person before March 2, 1984, debt instruments purchased at a premium, U.S. savings bonds, certain loans made between natural persons, and debt instruments issued before January 1, 1985, which are not capital assets in the hands of the holder.

In general, the amount of original issue discount deductible by an issuer under section 163(e) is determined in the same manner as the amount includible by the holder under section 1272. The regulations contain several exceptions to this general rule.

B. Paying Interest Currently at Constant Rate To Avoid the Original Issue Discount Rules

In the case of any debt instrument subject to section 1274 that provides for adequate stated interest, or in the case of any debt instrument issued at par for cash or publicly traded property, the original issue discount rules do not apply if all interest is payable currently at a constant rate over the entire term of the debt instrument. For this purpose, interest is considered payable currently if the interest is payable unconditionally and at regular intervals of one year or less. Interest is not considered payable at a constant rate if the debt instrument involves deferred interest (if the debt instrument has a lower initial rate of interest or an interest holiday for an initial period) or prepaid interest (if it has a higher initial rate of interest).

C. Determining the Total Amount of Original Issue Discount

1. Stated Redemption Price at Maturity

Except in the case of installment obligations, the stated redemption price at maturity of a debt instrument is defined as the amount fixed by the last modification of the purchase agreement including interest and other amounts payable at that time. The stated redemption price at maturity does not include any interest based on a fixed or variable rate that is actually and unconditionally payable at intervals of one year or less over the entire term of the debt instrument. These amounts are referred to as qualified periodic interest payments. In the case of an installment obligation, the stated redemption price at maturity equals the sum of all payments under the debt instrument less any qualified periodic interest payments.

2. Determination of Issue Price

If a debt instrument subject to section 1274 states adequate interest, the issue price is the stated principal amount of the debt instrument. If the debt instrument does not state adequate interest as discussed above, the issue price is the imputed principal amount determined according to the provisions of section 1274.

The issue price of a debt instrument not subject to section 1274 is determined as follows:

(a) A debt instrument that is part of an issue of debt instruments publicly offered and issued for cash—the initial price at which a substantial portion of the issue is sold to the public;

(b) A debt instrument that is part of an issue of debt instruments not publicly offered and issued for cash—the price paid by the first buyer;

(c) A debt instrument that is issued for property and is part of an issue of debt instruments a portion of which is traded on an established securities market—the fair market value of that debt instrument determined as of the first trading date after the date of issue of the debt instrument;

(d) A nonpublicly traded debt instrument issued in exchange for publicly traded property—the fair market value of the property; and

(e) A debt instrument that does not fall within the first four categories set forth above and that is not governed by section 1274—its stated redemption price at maturity.

3. De Minimis Rules

In the case of the holder, a debt instrument having a *de minimis* amount of original issue discount is treated as if the original issue discount were zero. Except in the case of an installment obligation, discount is considered *de minimis* if it is less than one-quarter of one percent of the stated redemption price at maturity multiplied by the number of complete years to maturity.

Special rules are provided for installment obligations. To compute the *de minimis* amount of original issue discount allowable on installment obligations generally, taxpayers must utilize a weighted average maturity in lieu of the number of full years from the issue date to final maturity. For debt instruments which are self-amortizing obligations, the proposed regulations provide a safe harbor which allows taxpayers to treat one-sixth of one percent of the stated redemption price at maturity multiplied by the number of complete years to final maturity as *de minimis* original issue discount.

D. Allocation of Original Issue Discount to an Accrual Period

1. In General

The amount of original issue discount allocable to an accrual period generally is equal to the product of the adjusted issue price at the beginning of the accrual period and the yield of the debt instrument, less amounts of stated interest payable during the accrual period. Each of the terms used in this calculation is defined under section 1272 and the proposed regulations as described in the succeeding discussion.

2. Accrual Period

Generally, for debt instruments issued after December 31, 1984, the accrual period is the interval between payment or compounding dates provided by the debt instrument (but in no event longer than one year), with the final accrual period ending on the maturity date of the debt instrument. Rules are provided for debt instruments with irregular payment or compounding intervals. For debt instruments that provide for a single payment at maturity and that have no other payment or compounding dates, the accrual period is the six-month period ending on the date in each calendar year that corresponds to the maturity date of the debt instrument or the date that is six months prior to that date. For debt instruments issued after July 12, 1982, and before January 1, 1985, the accrual period is the one-year period beginning on the issue date and on the corresponding day in each calendar year throughout the term of the debt instrument.

3. Adjusted Issue Price

The adjusted issue price at the beginning of the first accrual period is the issue price. The adjusted issue price at the beginning of each succeeding accrual period is equal to the adjusted issue price at the beginning of the immediately preceding accrual period increased by the amount of original issue discount accrued during that period. In the case of an installment obligation, the adjusted issue price at the beginning of an accrual period is reduced by any payments of principal or interest that are included in the stated redemption price at maturity and that are made during the immediately preceding accrual period.

4. Yield

The yield of a debt instrument is that rate of interest that, when used to determine the present value of all payments of principal and interest to be made under the debt instrument, provides an amount equal to the issue price of the debt instrument. Yield is expressed as an annual interest rate and is determined by compounding at the end of the accrual period. Special rules are provided for certain debt instruments that provide a variable rate of interest with a resulting variable yield as discussed in greater detail below.

5. Acquisition Premium

In determining the amount a holder must include in income, the daily portion of original issue discount is reduced by an appropriate share of any acquisition premium paid by that holder. Acquisition premium arises when a person purchases a debt instrument at a price which is in excess of the revised issue price on the date of purchase, but which is less than the stated redemption price at maturity. For debt instruments issued after July 1, 1982, and purchased before July 19, 1984, the daily portion is reduced ratably by an amount equal to the total acquisition premium divided by the number of days from the date of purchase up to (but not including) the stated maturity date. For debt instruments issued after July 1, 1982, and purchased after July 18, 1984, the daily portion is reduced by a constant fraction equal to the total acquisition premium divided by the total unaccrued original issue discount on the date of purchase.

E. Special Rules

1. Serial Maturity and Installment Obligations

Under regulations published under section 1232 of prior law, single obligations that provided for payments prior to maturity (other than payments of interest at fixed, periodic intervals of one year or less over the entire term of the obligation) were treated as a serial issue with each installment payment representing a separate obligation with its own issue price and stated redemption price at maturity. Original issue discount with respect to a serial issue, where independent issue prices could not be established for each individual series, was apportioned among the series based upon a linear ("bond-years") formula.

Because the OID rules now apply to a much broader class of obligations, including mortgages involving as many as 360 separate payments of principal, the proposed regulations eliminate the prior law treatment of each payment of principal under an installment obligation as a separate debt instrument. Instead, the regulations treat all installment obligations and certain serial maturity obligations as a single installment obligation for all purposes under sections 1271 through 1275. For this purpose, an installment obligation is defined as a debt instrument that provides for payments prior to maturity other than qualified periodic interest payments. Stated redemption price at maturity of an installment obligation is defined as the sum of all payments to be made under the obligation other than qualified periodic interest payments. This rule is effective for installment obligations issued after December 31, 1984 and for debt instruments maturing serially issued after May 8, 1986; the issuer and holder may, however, elect jointly to change this treatment.

2. Variable Rate Debt Instruments

The proposed regulations provide rules for the determination of the amount of original issue discount on debt instruments that provide for a variable rate of interest based on current values of an objective interest rate index. Generally, original issue discount attributable to deferred payments of interest made under these debt instruments is accounted for based upon a variable yield equal to the variable rate fixed by the debt instrument. Any other original issue discount on these debt instruments is determined on the issue date by assuming that the interest rate in effect on that date remains constant over the entire term of the debt instrument and is accounted for on that basis, regardless of the actual interest rate under the debt instrument.

3. Contingent Payments

Under the proposed regulations, contingent payments are generally not taken into account in applying the original issue discount and imputed interest rules. Instead, contingent payments are segregated from noncontingent payments and are accounted for separately. In determining whether a payment is contingent, the Commissioner may disregard remote and incidental contingencies. The parties to a transaction are, however, bound by its form and must treat a payment subject to a stated contingency as contingent. The contingent payment rules do not affect whether rights to receive contingent payments constitute debt or equity for Federal tax purposes or whether an instrument evidences a valid indebtedness.

Under the separate accounting rules for contingent payments, contingent payments may be recharacterized in certain situations. First, any payment of principal made on account of a sale or exchange of nonpublicly traded property that is not accompanied by a payment of adequate stated interest will be recharacterized in part as interest. Second, in the case of a debt instrument that does not provide for adequate stated interest and that accordingly has imputed interest, certain contingent interest payments may be recharacterized in part as principal to restore to basis amounts previously recharacterized as imputed interest. In these cases, a payment subject to recharacterization is treated as a payment of principal in an amount equal to the present value of the payment and as a payment of interest to the extent of the difference between the amount of the payment and the present value of the payment. The amount of all payments characterized as principal, however, cannot exceed the amount of the fixed or maximum stated principal amount under a debt instrument.

Third, a contingent payment made under a debt instrument issued for cash or publicly traded property may be recharacterized in a case in which the issue price of the debt instrument exceeds the sum of all the noncontingent payments due under the debt instrument. In such a case, the noncontingent payments under the debt instrument are treated entirely as principal. Each contingent payment is treated as a payment of interest to the extent of the total interest deemed accrued and not allocated to prior payments, and a payment of principal to the extent of the excess of the amount of the payment over the portion of the payment treated as interest. The total interest deemed accrued for any accrual period is based on an assumed yield to maturity equal to the applicable Federal rate which would have applied had the debt instrument been issued for nonpublicly traded property. Once the sum of all the portions of the contingent payments that are treated as principal under this rule reaches the difference between the issue price of the debt instrument and the sum of all the noncontingent payments under the debt instrument, any additional contingent payments are treated as interest.

If a contingent payment is paid within six months of the date it becomes fixed, the portion of the payment recharacterized as interest is accounted for by both the issuer and the holder when the payment becomes fixed. The proposed regulations provide, however, that if a contingent payment is not paid within six months of the date it becomes fixed, the buyer is treated as having issued a separate debt instrument on the date the payment becomes fixed. The issue price of this deemed debt instrument is determined under section 1274 (regardless of whether the payment arose under a debt instrument that was issued for cash or publicly traded property). An amount equal to the issue price is characterized as principal and interest as discussed above.

In the case of a debt instrument subject to section 1274, special rules are provided for the treatment of payments contingent only with respect to due date but which are payable within a fixed period. Under these rules, the buyer's initial basis and the allocation of interest to accrual periods are determined by assuming that all payments under the debt instrument are made at the latest possible date and in the smallest amount permitted. When payments are made before the end of the fixed period, basis and interest accrual adjustments are made.

4. Put or Call Options

The proposed regulations provide a special rule for the determination of yield, maturity date, and stated redemption price at maturity of a debt instrument that provides for a put or call option or an option to extend the term of the debt instrument. Yield of such a debt instrument is determined as of the issue date by assuming that the holder of the particular option will act in accordance with his own economic interest (as viewed from the issue date) in deciding whether to exercise the option. For example, if the issuer of a debt instrument has a call right and if the yield to the call date (assuming exercise of the call option) would be less than the yield to maturity assuming no exercise of the call, it will be assumed as of the date of issue that the call option will be exercised. The maturity date and the stated redemption price at maturity are then determined according to the presumption of exercise. Special rules are provided for debt instruments issued in a transaction governed by section 1274 that contain such options.

5. Reorganizations

In the case of debt instruments issued after December 13, 1982, in exchange for other debt instruments in a reorganization (within the meaning of section 368(a)), a special rule limits the original issue discount created upon the exchange. If the issue price of the new debt instrument would be less than the adjusted issue price of the old debt instrument but for this rule, then the issue price of the new debt instrument is equal to the adjusted issue price of the old debt instrument.

F. Information Reporting Requirements

Section 1275(c)(1) requires an issuer of publicly offered debt instruments issued after the date of publication of these regulations in final form having original issue discount to set forth on the face of the debt instrument the amount of original issue discount and the issue date. In addition, the proposed regulations require the yield to maturity, the method selected to determine yield for a short accrual period, and the amount of original issue discount allocable to a short accrual period to be set forth on the face of the debt instrument. Similar requirements apply to the first holder of a nonpublicly offered debt instrument, if such holder disposes of the debt instrument before maturity.

Section 1275(c)(2) requires the issuer of a publicly offered debt instrument having original issue discount to furnish the Secretary with certain information. The temporary regulations issued under this section require certain additional items to be furnished to the Secretary and are proposed herein as a part of these regulations with the following amendment: Section 1275(c)(2) shall not apply to issuers of publicly offered debt instruments that are: (1) Certificates of deposit, or (2) stripped bonds and coupons within the meaning of section 1286.

G. Treatment of Amounts Received on Sale, Exchange or Redemption of Debt Instruments

Under the law in effect prior to the Tax Reform Act of 1984, amounts received upon retirement of certain debt instruments held as capital assets were considered to have been received in exchange therefor. Gain on sale, exchange, or retirement was treated as capital gain in the absence of an intention to call the bond before maturity. In the case of a short-term obligation, a portion of the gain was treated as ordinary interest income to the extent of accured discount in the hands of the holder.

The rules of prior law relating to the characterization of gain upon sale, exchange or retirement of a debt instrument issued at a discount have been retained, except that the requirement that the debt instrument be a capital asset in the hands of the holder has been repealed for debt instruments issued at a discount after July 18, 1984.

V. Accounting for Interest

Under the revised section 483, unstated interest is required to be accounted for on an economic accrual basis consistent with the allocation of original issue discount under section 1272(a) and Rev. Rul. 83-84, 1983-1 C.B. 97. Unlike original issue discount, however, unstated interest is not subject to annual periodic inclusion or deduction. The proposed regulations prescribe rules under section 446 governing the method of accounting for interest in lending and deferred payment transactions outside the scope of the original issue discount rules. Thus, these rules apply to the accounting for unstated interest (and any stated interest) in transactions to which section 483 applies. Under the proposed section 446 regulations, interest accrues in generally the same manner as original issue discount. For purposes of determining how accrued interest is allocated to payments under a debt instrument, a payment is treated: First, as a payment of interest to the extent interest has accrued and remains unpaid as of the date of the payment; second, as a prepayment of interest to the extent the parties have allocated more interest to payments than the amount of interest that has accrued as of the date of the payment; and third, as a payment of principal to the extent of the excess of the payment over the sum of the accrued and the prepaid interest. In certain small transactions, however, the allocation of the parties of less interest to a payment than the amount of accrued interest that remains unpaid as of the date of the payment will be respected.

VI. Cash Method Debt Instruments

As noted above, section 483 rather than section 1274 applies to cash method debt instruments. Interest on a cash method debt instrument is accounted for under the cash receipts and disbursements method of accounting. In general, a debt instrument is a cash method debt instrument if the stated principal amount of the debt instrument does not exceed $2,000,000, the lender is neither an accrual method taxpayer nor a dealer with respect to the property, and the borrower and the lender jointly elect the cash method treatment. However, a debt instrument issued in exchange for new section 38 property or a debt instrument issued in a sale-leaseback transaction does not qualify for the cash method treatment. The cash method election is generally binding on successors of the lender and the borrower. If, however, the lender (or a successor thereof) transfers the cash method debt instrument to an accrual method taxpayer, the election does not apply to the successor for any period after the transfer and section 1272 will apply to the successor.

VII. Amendments to Section 482 Regulations

1. In General

In section 44(b)(2) of the Tax Reform Act of 1984, Congress directed the Treasury to amend the safe haven interest rates under the section 482 regulations to provide floating rates consistent with the rates applicable under sections 483 and 1274. These proposed regulations are in response to that directive. In addition, these proposed regulations would make certain other changes to the section 482 regulations. The proposed regulations would reduce the interest-free period on certain intercompany balances between controlled taxpayers under existing § 1.482-2(a)(3) from six months to 60 days. The proposed regulations would also delete the formula method for determining a safe-haven rental charge for leases of tangible depreciable property between related taxpayers under § 1.482-2(c)(2)(ii).

2. Explanation of the Proposed Regulations

a. Safe Haven Interest Rates

Section 1.482-2(a)(2)(iii) of the proposed regulations provides generally that the range of safe haven interest rates on loans or advances between controlled entities will be between 100 percent and 130 percent of the applicable Federal rate (AFR) corresponding to the term of the loan, with adjustments for inadequate interest made at 100 percent of the AFR, compounded semiannually, and adjustments for excessive interest made at 130 percent of the AFR, compounded semiannually. The upper limit of 130 percent of the AFR approximates the interest yield on bonds with a Moody's rating of BAA. Consistent with section 1274(e), the lower limit is 110 percent of the AFR in the case of sale-leaseback transactions. The effective dates of the proposed regulations are described in § 1.482-2(a)(2)(iii)(A) of the proposed regulations.

The proposed regulations continue the rule of the existing regulations that controlled taxpayers may demonstrate that a rate outside the safe haven range is a more appropriate rate under all the facts and circumstances.

Section 1.482-2(a)(3) of the proposed regulations provides that where the interest rate on a loan or advance is subject to adjustment both under section 482 and some other Code section (for example, sections 467, 483, 1274, or 7872), the other Code section is to be applied first, and the provisions of section 482 may then be applied to the loan or advance, as adjusted by the other Code section. If the other Code section does not apply to the loan or advance because of an exception, limitation, or *de minimis* rule contained in the other Code section, the provisions of the section 482 regulations may still be applied to the loan or advance by the district director. Under this arrangement it would be unlikely that actual adjustments would be required under both section 482 and the other Code section. Under certain circumstances, however, both section 482 and the other Code section may apply. For example, if the AFR exceeds 9 percent, and if the related taxpayers use the special 9 percent rate prescribed in section 1274A(a), the transaction may be subject to further adjustment under section 482.

Under proposed § 1.482-2(a)(1)(iii), the interest-free period on certain intercompany balances (six months under the existing regulations) is reduced to 60 days. The proposed regulations continue the rule of the existing regulations that the taxpayer is permitted to use a longer interest-free period if it can demonstrate that it regularly grants uncontrolled parties a longer interest-free period on similar transactions in its trade or business.

b. Leases

Section 1.482-2(c) of the existing regulations provides a formula method for determining a safe haven rental charge for certain leases of tangible depreciable property between controlled entities. There is no minimum or maximum lease period for which the safe haven rental charge can be used. Under the existing regulation taxpayers are never required to use the safe haven formula rental if the taxpayer can establish a more appropriate rental charge. However, in cases where the taxpayer may use the safe haven rental amount, the IRS may not challenge the safe haven amount, even if the amount does not clearly reflect income. Because of these deficiencies in the operation of the safe haven formula, it would be deleted under the proposed regulations. The safe haven rule for subleases under § 1.482-2(c)(2)(iii) would be retained. The effective dates of the proposed regulations are described in § 1.482-2(c)(2)(ii).

VIII. Questions Reserved

The proposed regulations do not revise the definition of intention to call before maturity nor do they address the application of the intention to call rules in the case of debt instruments with indefinite maturities. The Internal Revenue Service is actively considering and welcomes comments specifically directed toward these reserved issues, as well as those directed to the following:

1. How the original issue discount rules should apply to foreign currency transactions, and
2. Whether a portion of the issue price of a debt instrument providing for a conversion feature should properly be

allocated to that conversion feature in a manner similar to the allocation of issue price for investment units under section 1273(c)(2).

Regulatory Flexibility Act

Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

Non-Application of Executive Order 12291

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

Comments and Request for a Public Hearing

Before these proposed regulations are adopted, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the **Federal Register.** The collection of information requirements contained herein have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on the requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, DC 20503. The Internal Revenue Service requests that persons submitting comments to OMB also send copies of the comments to the Service.

Drafting Information

The principal author of the proposed regulations under sections 163, 1271, 1272, 1273, and 1275 is Theresa E. Bearman of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service; the principal author of the regulations under sections 446, 483 and 1274 is Ewan D. Purkiss of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service; and the principal author of the regulations under section 482 is Joseph M. Rosenthal of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and the Treasury Department participated in developing the regulations on matters of both substance and style.

List of Subjects

26 CFR 1.61–1—1.281–4

Income taxes, Taxable income, Deductions, Exemptions.

26 CFR 1.301–1—1.385–6

Income taxes, Corporations, Corporate distributions, Corporate adjustments, Reorganizations.

26 CFR 1.401–0—1.425–1

Income taxes, Employee benefit plan, Pensions, Stock options, Individual retirement accounts, Employee stock ownership plans.

26 CFR 1.441–1—1.483–2

Income taxes, Accounting, Deferred compensation plans.

26 CFR 1.581–1—1.601–1

Income taxes, Banks.

26 CFR 1.611–0—1.638–2

Income taxes, Natural resources, Deductions, Exclusions from income.

26 CFR 1.801–1—1.832–6

Income taxes, Insurance companies.

26 CFR 1.861–1—1.997–1

Income taxes, Aliens, Exports, DISC, Foreign investments in U.S., Foreign tax credit, Sources of income, United States investments abroad.

26 CFR 1.1001–1—1.1102–3

Income taxes, Gain and loss, Basis, Nontaxable exchanges.

26 CFR 1.1271—1.1288

Income taxes, Capital gains and losses, Original issue discount, Applicable Federal rate, Market discount, Short-term obligations, Stripped bonds and stripped coupons, Tax-exempt obligations.

26 CFR 1.1501–1—1.1564–1

Income taxes, Controlled group of corporations, Consolidated returns.

26 CFR 1.6001–1—1.6109–2

Income taxes, Administration and procedure, Filing requirements.

26 CFR 1.9001—1.9101–1

Income taxes, Administration and procedure, Miscellaneous tax acts, Extensions of time for elections.

26 CFR Part 3

Income taxes, Maritime carriers.

26 CFR Part 5f

Income taxes, Tax Equity and Fiscal Responsibility Act of 1982.

26 CFR Part 6a

Bonds, Income taxes, Mortgages, Veterans.

26 CFR Part 25

Gift taxes.

26 CFR Part 514

France, Tax treaties.

Proposed Amendments to the Regulations

Accordingly, 26 CFR Part 1, Part 3, Part 5f, Part 6a, Part 25, and Part 514 are proposed to be amended as follows:

PART 1—INCOME TAX: TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Paragraph 1. The authority citation for Part 1 is amended by adding the following citations: (citations before * * * indicate general rulemaking authoriy)

Authority: 26 U.S.C. 7805. * * * Sections 1.483–1 through 1.483–5 also issued under 26 U.S.C. 483(g). Sections 1.1271–1 through 1.1275–5 also issued under 26 U.S.C. 1275(d). Section 1.1274A–1 also issued under 26 U.S.C. 1274A(e).

Par. 2. Paragraph (c)(3) of § 1.61–6 is revised to read as follows:

§ 1.61–6 Gains derived from dealings in property.

* * * * *

(c) *Character of recognized gain.* * * *

(3) Amounts received on retirement or sale or exchange of debt instruments, section 1271;

* * * * *

§ 1.61–7 [Amended]

Par. 3. In paragraph (d) of § 1.61–7, the third sentence is amended by removing the phrase "section 1232" and adding in its place the phrase "section 1271".

§ 1.163–4 [Amended]

Par. 4. Section 1.163–4 is amended as follows:

1. The heading is revised by adding a comma and the phrase "and before July 2, 1982." after the word "1969".

2. In paragraph (a)(1), the second sentence is amended by removing the phrase "section 1232(b)(1)" and adding in its place the phrase "section 1273(a)(1)", and the second sentence is further amended by removing the phrase "the second sentence thereof" in the parenthetical and adding in its place the phrase "section 1273(a)(3)".

3. Paragraph (b) is amended by removing the phrase "section 1232(b)(1)" from each place that it appears in the paragraph and adding its place the phrase "section 1273(a)(1)", by removing the phrase "the second sentence thereof" from each place it appears in the paragraph and adding in its place the phrase "section 1273(a)(3)", and by removing the phrase "section 1232(a)(3)(A)" from *Example (4)* and adding in its place the phrase "section 1271(a)(3)(A)".

4. Paragraph (d) is amended by adding the phrase "and before July 2, 1982," after the word "1969," each place that it appears.

Par. 5. A new § 1.163-7 is inserted immediately following § 1.163-6T. New § 1.163-7 reads as follows:

§ 1.163-7 Deduction for original issue discount on certain debt instruments issued after July 1, 1982.

(a) *Applicability.* Section 163(e) and this section apply to debt instruments having original issue discount (determined without reference to section 1273(a)(3) and § 1.1273-1(a)(3)) issued after July 1, 1982, other than debt instruments issued by a natural person before March 2, 1984, described in section 1272(a)(2)(D), and debt instruments representing loans between natural persons described in section 1272(a)(2)(E). For purposes of this section, the term "debt instrument" shall have the same meaning as in section 1275(a)(1) and § 1.1275-1(b)(1). A debt instrument subject to this section at the time of issuance continues to be subject to this section notwithstanding an assumption of the debt instrument by a natural person before March 2, 1984.

(b) *General rule.* Except as provided in paragraphs (c) and (d) of this section and in § 1.1275-2(f)(2), an issuer or a transferee may deduct as interest the amount of original issue discount on a debt instrument equal to the sum of the daily portions of original issue discount for all days in the taxable year during which the issuer (or transferee) was primarily liable on the debt instrument. The daily portion shall be determined according to the rules stated in § 1.1272-1(c) except that the following are disregarded—

(1) Any reduction in the amount of original issue discount includible in gross income by subsequent holders by reason of section 1272(a)(6), and

(2) The *de minimis* rule of section 1273 (a)(3) and § 1.1273-(a)(3).

The transfer of a debt instrument by any holder to a subsequent purchaser shall not affect the accrual of deductions under this section.

(c) *Limitations*—(1) *Personal use property.* In the case of a debt instrument whose issue price is determined under section 1273(b) (1), (2), or (3), that is incurred in connection with the acquisition or carrying of personal use property, original issue discount is not deductible until paid, or, if later, when accured. See § 1.1275-2(f).

(2) *Short-term obligations.* In the case of a short-term obligation (as defined in section 1283(a)(1)), the issuer or transferee may deduct original issue discount only when paid, (or, if later, when accrued), if the issuer or transferee uses the cash receipts and disbursements method of accounting.

(3) *Other limitations.* Other sections of the Code may limit the deductibility of original issue discount otherwise allowable under section 163(e) and this section. See, for example, section 163(d) (relating to interest on investment indebtedness) and section 189 (relating to construction period interest).

(d) *De minimis discount deductible on straight-line basis in certain cases.* Notwithstanding paragraph (c)(1) of this section, in the case of an installment obligation which—

(1) Is a self-amortizing installment obligation (within the meaning of § 1.1273-1(b)(2) (iii)) or is a level principal obligation (within the meaning of § 1.1274-6(d)(2)(ii)(D)), and

(2) Has a *de minimis* amount of original issue discount (as determined under § 1.1273-1(a)(3)),

the amount of original issue discount (including points) that is allocated to each payment of principal under the debt instrument shall be the total amount of original issue discount divided by the total number of principal payments. For purposes of paragraph (d)(1) of this section, an obligation shall be considered to be a self-amortizing or level principal obligation if it would be so classified but for the fact that it calls for varying rates of interest over the term of the obligation.

(e) *Recovery or retention of amounts previously deducted.* In any taxable year in which an amount of original issue discount that was deducted as interest under this section is retained or recovered by the taxpayer, such as, for example, by reason of a fine, penalty, forfeiture, or other withdrawal fee, this amount shall be includible in the gross income of the taxpayer for the taxable year.

(f) *Deduction upon repurchase*—(1) Except as provided in paragraph (f)(2) of this section, if a debt instrument is issued and subsequently repurchased at a price in excess of the issue price plus any amount of original issue discount deductible prior to the date of repurchase, or minus any amount of premium returned as income prior to repurchase, the excess of the repurchase price over the issue price adjusted for amortized premium or deductible discount is deductible as interest for the taxable year. For purposes of section 163(e) and paragraph (f) of this section, the term "repurchase" is defined by reference to section 1272(d)(1) and § 1.1272-1(m).

(2) The provisions of paragraph (f)(1) of this section shall not apply to the extent a deduction is disallowed by section 249 (relating to the limitation on deduction of bond premium on repurchase of convertible obligation) and the regulations thereunder.

(g) *Effective date.* Section 1.163-7 applies to debt instruments issued with original issue discount (determined under section 1273 without regard to section 1273(a)(3)) after July 1, 1982. A debt instrument issued after July 1, 1982, pursuant to a written commitment that was binding on July 1, 1982, and at all times thereafter, shall be treated as issued on July 1, 1982, for purposes of this section and § 1.163-4. A written commitment is binding on July 1, 1982, and at all times thereafter if it contains an obligation to issue the debt instruments at a particular price and rate of interest and may be enforced against the issuer under applicable state law. Thus, for example, the rules of section 163(e) and this section do not apply to debt instruments issued pursuant to the exercise of warrants outstanding on July 1, 1982, that were exercisable against the issuer under state law and that prescribe the price and interest rate at which they may be exercised. For rules relating to debt instruments issued with original issue discount on or before July 1, 1982, see section 163(e) as in effect before its amendment by section 231 of the Tax Equity and Fiscal Responsibility Act of 1982 and § 1.163-4.

§ 1.249-1 [Amended]

Par. 6. Section 1.249-1 is amended as follows:

1. In paragraph (c)(2) by removing the phrase "section 1232(b)" and adding in its place the phrase "sections 1273(b) and 1274", and by removing the phrase "§§ 1.163-3 and 1.163-4." and adding in

its place the phrase "§§ 1.163-3, 1.163-4, and 1.163-7.".

2. In paragraph (d)(2), the first sentence, by removing the phrase "§§ 1.163-3, 1.163-4." and adding in its place the phrase "§§ 1.163-3 and 1.163-4, and 1.163-7.".

3. In paragraph (f)(2), the second sentence, by removing the phrase "§§ 1.163-3(c) and 1.163-4(c)." and adding in its place the phrase "§§ 1.163-3(c), 1.163-4(c), and 1.163-7(f).".

Par. 7. Paragraph (b)(1) of § 1.409-1 is amended by removing the word "1232" from the last sentence thereof and adding in its place the phrase "1271 through 1275".

Par. 8. A new § 1.446-2 is added immediately following § 1.446-1. New § 1.446-2 reads as follows:

§ 1.446-2 Method of accounting for interest.

(a) *Applicability*—(1) *In general.* This section prescribes the method of accounting for interest and applies to all interest and amounts treated as interest (whether stated or unstated) in any lending or deferred-payment transaction other than amounts that are taken into account under—

(i) Sections 1272 and 163(e) (relating to current inclusion in income of original issue discount and an allowable deduction for original issue discount),

(ii) Section 467(a)(2) (relating to certain payments for the use of property or services), or

(iii) Section 7872(a) (relating to the treatment of gift and demand loans with below-market interest rates).

Thus, the amounts to which this section applies include the stated and unstated interest in any sale or exchange of property for deferred payments to which section 1274 does not apply. For example, this section applies to interest under a debt instrument described in section 1274A(c)(2) and § 1.1274A-1(c)(2) (relating to debt instruments for which the issuer and holder have made an election to use the cash method of accounting). This section also applies to the interest in any agreement for the use of property or provision of services for deferred payments to the extent section 467(a)(2) does not apply to the agreement. In addition, this section applies to the interest in a lending transaction such as a loan described in section 1272(a)(2)(E) (relating to certain loans between natural persons) to which sections 1272 and 163(e) do not apply by reason of exceptions or safe harbors. Similarly, if section 1272 or 163(e) applies with respect to one party to a transaction but such sections do not apply with respect to the other party to the transaction, this section applies to the interest provided with respect to such other party.

(2) *Effect on other provisions.* Notwithstanding the provisions of this section, interest or an amount treated as interest is not deductible for any taxable year in which such deduction is not allowed by reason of any other provision of the Code. For purposes of such other provision, however, the rules of this section shall be taken into account in determining the taxable year in which such amount is otherwise allowable as a deduction. For circumstances in which interest is not allowable as a deduction for a taxable year, see, for example, section 189 (relating to real property construction period interest), section 163(d) (relating to interest on investment indebtedness) and section 267(a) (relating to losses, expenses, and interest with respect to transactions between related persons).

(b) *Accrual of interest*—(1) *In general.* For purposes of this section, the interest (including any unstated interest determined under section 483) in any lending or deferred-payment transaction (the loan) accrues at a single rate equal to the yield to maturity as defined in paragraph (c)(1) of this section regardless of any contrary formulas that may be stated by the parties to the transaction in any debt instrument or agreement. For this purpose, the interest under all debt instruments issued by a borrower to the same lender as part of a single transaction shall be aggregated and treated as interest in a single lending or deferred-payment transaction. For circumstances in which multiple sales or exchanges are treated as a single sale or exchange, see § 1.1274A-1(d).

(2) *Amount of interest that accrues for an accrual period*—(i) *In general.* The amount of interest that accrues for any accrual period (other than a short first accrual period, or a final accrual period) is equal to the product of—

(A) The outstanding loan balance at the beginning of the accrual period, and

(B) The yield to maturity of the loan, divided by the number of accrual periods in a year.

(ii) *Short first accrual period*—(A) *In general.* (*1*) Except as otherwise provided in this paragraph (b)(2)(ii)(A), the amount of interest that accrues for a short first accrual period shall be determined under the exact method described in paragraph (b)(2)(ii)(B) of this section, and a convention that assumes that a year consists of 12 30-day months shall be used for purposes of determining the fraction (f) with respect to the short period.

(*2*) If section 483 does not apply to the loan (as, for example, in the case of a loan that provides for adequate stated interest within the meaning of § 1.483-2) and the loan provides that interest for the short first accrual period accrues under the approximate method described in paragraph (b)(2)(ii)(C) of this section or any other reasonable method, the amount of interest that accrues for such short period shall be determined under such method. In addition, for purposes of determining the fraction (f) with respect to a short period under paragraph (b)(2)(ii) (B) or (C) of this section, the use of the convention that assumes that a year consists of 12 30-day months is optional if section 483 does not apply to the loan.

(B) *Exact method.* The exact method assumes daily compounding of interest. Under this method, the amount of interest that accrues for the short accrual period is equal to the result of the following formula:

$$I=P\times[(1+i/k)^f-1]$$

In which:

I = The amount of interest that accrues for the short accrual period

P = The outstanding loan balance at the beginning of the short accrual period as determined under paragraph (c)(3)(i) of this section.

i = The yield to maturity of the loan expressed as a decimal

k = The number of accrual periods that are contained in a year

f = A fraction, the numerator of which is the length of the short accrual period, and the denominator of which is the length of a full accrual period.

(C) *Approximate method.* The approximate method assumes simple interest within an accrual period (that is, no compounding during the short accrual period). Under the approximate method, the amount of interest that accrues for the short period is determined by multiplying the amount that would constitute the proper accrual of interest for a full accrual period by a fraction, the numerator of which is the length of the short accrual period and the denominator of which is the length of a full accrual period. Thus, the amount of interest that accrues for the short accrual period is equal to the result of the following formula:

$$I=P\times(i/k)\times f$$

In which:

I = The amount of interest that accrues for the short accrual period

P = The outstanding loan balance at the beginning of the short accrual period as determined under paragraph (c)(3)(i) of this section

i = The yield to maturity of the loan expressed as a decimal

k = The number of accrual periods that are contained in a year

f = A fraction, the numerator of which is the length of the short accrual period, and the denominator of which is the length of a full accrual period.

(iii) *Final accrual period.* The amount of interest that accrues for the final accrual period (including a short final accrual period) is equal to the excess of—

(A) The aggregate amount of interest due under the loan, over

(B) The aggregate amount of accrued interest allocated to all accrual periods preceding the final accrual period.

(c) *Definitions*—(1) *Yield to maturity*—(i) *In general.* The yield to maturity (yield) of a loan is the rate of interest (based on compounding at the end of each accrual period) at which the present value of all payments (including interest and principal) required to be made under the loan is equal to the amount lent. Paragraph (c)(1) (ii) and (iii) of this section provides special rules to allow a simple calculation of yield in certain circumstances. In the case of a loan that has a short first accrual period, the yield shall be computed in a manner consistent with the method used to determine the amount of interest that accrues for such short accural period under paragraph (b)(2) of this section. For rules relating to the determination of present value, see § 1.1274–5.

(ii) *Yield equals stated rate in certain cases.* Except as provided in paragraph (c)(1)(iii) of this section, the yield of a loan is the stated rate of interest provided in the loan if—

(A) The stated rate of interest remains constant over the entire term of the loan (including short periods),

(B) Interest is either paid or compounded at the end of each accrual period, and

(C) No interest other than the stated rate (for example, points or other forms of discount) is provided in the loan.

(iii) *Contracts to which section 483 applies.* Except in the case of a cash method debt instrument received in exchange for property in a potentially abusive situation (see § 1.483-3(a)), the yield of a loan to which section 483 applies (that is, a loan that does not provide for adequate stated interest and is otherwise subject to section 483) is the imputed rate of interest applicable to the loan as determined under § 1.483–4. In the case of a cash method debt instrument received in exchange for property in a potentially abusive situation, the yield shall be determined only as prescribed in paragraph (c)(1)(i) of this section.

(2) *Accrual period*—(i) *Regular payment or compounding at intervals of one year or less.* If a loan calls for more than one payment or compounding date (other that the date of the loan) and all dates on which an amount is either paid or compounded occur at regular intervals of one year or less, the accrual period is such interval. A loan shall not fail to qualify for this rule merely because the interval between the date of the loan and the first payment or compounding date after the date of the loan (the first payment or compounding date) or the interval between the maturity date and the preceding payment or compounding date differs from the interval between other payment or compounding dates.

(ii) *Irregular payment or compounding; intervals of more than one year.* If a loan calls for more than one payment or compounding date (other than the date of the loan) and all dates on which an amount is either paid or compounded do not occur at regular intervals of one year or less, the accrual period is the longest period of not more than one year such that all intervals consist of a whole number of accrual periods. The interval between the date of the loan and the first payment or compounding date and the interval between the maturity date and the preceding payment or compounding date are not taken into account in applying this paragraph (c)(2)(ii) unless the loan calls for only one payment or compounding date between the date of the loan and the maturity date.

(iii) *Loans calling for a single payment.* If a loan calls for a single payment at maturity and for no other payment or compounding dates (other than the date of the loan), the accrual periods are the six-month periods (or the shorter period from the date of the loan) that end on the day in the calendar year that corresponds either to the maturity date or to the date that is six months before the maturity date.

(iv) *Short accrual period.* (A) If the interval between the date of a loan for which the accrual period is determined under paragraph (c)(2) (i) or (ii) of this section and the first payment or compounding date does not consist of a whole number of accrual periods, the first accrual period shall be the short period such that the remainder, if any, of such interval consists of a whole number of accrual periods.

(B) If the interval between the last date before maturity on which an amount is paid or compounded and the maturity date of a loan for which the accrual period is determined under paragraph (c)(2) (i) or (ii) of this section does not consist of a whole number of accrual periods, the final accrual period shall be the short period such that the remainder, if any, of such interval consists of a whole number of accrual periods.

(v) *Date accrual period begins.* The first accrual period beings on the date of the loan and each subsequent accrual period begins on the date after the last day of the preceding accrual period.

(3) *Outstanding loan balance*—(i) *First accrual period.* The outstanding loan balance at the beginning of the first accrual period is equal to—

(A) In the case of a loan to which section 483 applies, the amount described in § 1.483–2(c)(2), or

(B) In any other case, the amount lent.

(ii) *Subsequent accrual periods.* The outstanding loan balance at the beginning of any accrual period other than the first accrual period is equal to—

(A) The sum of—

(*1*) The outstanding loan balance at the beginning of the preceding accrual period, and

(*2*) The amount of interest that accrued for the preceding accrual period,

reduced by

(B) The amount of any payment required to be made during the preceding accrual period.

(d) *Allocation of interest to payments*—(1) *In general.* Except as provided in paragraph (d)(3) of this section, each payment under a loan (other than payments of additional interest or similar charges provided with respect to amounts that are not paid when due) shall be treated—

(i) First, as a payment of interest to the extent of the accrued and unpaid interest (within the meaning of paragraph (d)(2) of this section) as of the date the payment becomes due;

(ii) Second, as a prepayment of interest to the extent (if any) the amount of interest allocated by the parties to the payment exceeds—

(A) The aggregate amount of accrued interest as of the date the payment becomes due, reduced (but not below zero) by

(B) The aggregate amount of interest allocated by the parties to prior payments; and

(iii) Third, as a payment of principal to the extent (if any) the amount of the payment exceeds the sum of the amounts described in paragraph (d)(1) (i) and (ii) of this section.

(2) *Accrued and unpaid interest.* The amount of accrued and unpaid interest as of the date any payment becomes due is the excess, if any, of—

(i) The aggregate amount of accrued interest as of the date the payment becomes due, over

(ii) The aggregate amount previously treated as a payment of interest under paragraph (d)(1) (i) or (ii) of this section.

(3) *Allocation respected in certain small transactions*—(i) *In general.* If the aggregate amount of interest and principal payable under a loan does not exceed $250,000 and section 483 does not apply to the loan (as, for example, in the case of a loan that provides for adequate stated interest within the meaning of § 1.483–2), the allocation of interest and principal shall be respected. Similarly, if section 483 applies to a loan under which the aggregate amount payable does not exceed $250,000, but does not apply to a party to the loan (as, for example, in the case of an obligor under a debt instrument given in consideration for the sale or exchange of personal use property), the allocation of the parties shall be respected for purposes of determining the tax liability of the party not subject to section 483.

(ii) *Prepaid interest.* The amount of interest allocated to any payment under this paragraph (d)(3) shall be treated as prepaid interest to the extent such amount exceeds—

(A) The aggregate amount of accrued interest as of the date the payment becomes due, reduced (but not below zero) by

(B) The aggregate amount of interest allocated to prior payments under this paragraph (d)(3).

(e) *Accounting for prepaid interest.* Prepaid interest must be included in income by a lender when received, regardless of the lender's method of accounting. Except as otherwise provided in section 461(g)(2), prepaid interest is not deductible before such interest accrues (determined under paragraph (b) of this section).

(f) *Special rules*—(1) *Variable rate debt instruments.* In the case of any loan that is a variable rate debt instrument (within the meaning of § 1.1275–5(a)) the amount of interest that accrues for an accrual period shall be determined in a manner consistent with the rules of § 1.1275–5.

(2) *Contingent payments*—(i) *In general.* In the case of a contingent payment (other than a contingent payment to which paragraph (b)(4) of § 1.483–5 (relating to payments contingent with respect to due date but payable within a fixed period) applies), interest does not accrue before the date the payment becomes fixed and the amount of interest that would otherwise have accrued (as determined under paragraph (b) of this section) on or before the date the payment becomes fixed accrues on such date. Any remaining interest with respect to the payment accrues in the manner described in paragraph (b) of this section.

(ii) *Certain contingent payments within a fixed period.* In the case of contingent payments to which paragraph (b)(4) of § 1.483–5 applies, the amount of interest that accrues for an accrual period shall be determined in a manner consistent with the rules of § 1.1275–4(d).

(g) *Examples.* The provisions of this section may be illustrated by the following examples:

Example (1). (i) On July 1, 1986, A sells his personal residence to B for a stated purchase price of $1,297,143.66. The property is not personal use property (within the meaning of section 1275(b)(3) and § 1.1275–2(f)(3)) in the hands of B. Under the loan agreement, B is required to make two installment payments of $648,571.83, the first due on June 30, 1988, and the second due on June 30, 1990.

(ii) The agreement does not provide for adequate stated interest. Thus, section 483 applies to the loan and the yield is the imputed rate of interest determined under § 1.483–4. Assume that under § 1.483–4 the imputed rate of interest is 9.2 percent, compounded annually, and that under § 1.483–3 there is unstated interest of $297,143.66. Under paragraph (c)(2)(ii) of this section the accrual period is one year. Paragraph (c)(2)(iv) of this section does not apply because the first interval (July 1, 1986–June 30, 1988) consists of two annual accrual periods. Accordingly, the first accrual period is a full period.

(iii) Under paragraph (c)(3)(i) of this section, the outstanding loan balance at the beginning of the first accrual period is $1,000,000 (the amount described in § 1.483–2(c)(2) (sales price minus total unstated interest)). Under paragraph (b)(2) of this section, the amount of interest that accrues for the first accrual period is $92,000 ($1,000,000 × .092). At the beginning of the second accrual period the outstanding loan balance is $1,092,000 ($1,000,000 + $92,000). The amount of interest that accrues for the second annual accrual period is $100,464 ($1,092,000 × .092). Thus, as of the date the first payment becomes due, $192,464.00 of interest has accrued.

(iv) Under paragraph (d)(1) of this section, the $648,571.83 payment is treated first as a payment of interest to the extent of $192,464.00. Since the parties have not allocated interest to the payment in excess of the amount of interest that has accrued as of the date the payment becomes due, there is no prepayment of interest and the remainder of the payment ($456,107.83) is treated as a payment of principal.

(v) The outstanding loan balance at the beginning of the third annual accrual period is $543,892.17 (($1,092,000 + $100,464) less $648,571.83). The amount of interest that accrues for the third accrual period is $50,038.08 ($543,892.17 × .092). The amount of interest that accrues for the final accrual period is $54,641.58, the excess of the aggregate amount of interest due under the loan ($297,143.66), over the amount of interest that had accrued for all accrual periods preceding the final accrual period ($242,502.08). As of the date the second payment becomes due, $104,679.66 of interest has accrued. Thus, of the $648,571.83 payment, $104,679.66 is treated as interest and $543,892.17 is treated as principal.

Example (2). (i) The facts are the same as in example (1), except that the sales price is $1,000,000, and the loan agreement calls for adequate stated interest of $297,143.66. Further, the loan agreement provides that the entire payment of interest is allocated to the first installment payment.

(ii) Since the parties have allocated more interest to the first payment ($297,143.66) than the amount of interest that has accrued as of the date the first payment becomes due ($192,464.00), the excess of $104,679.66 is a prepayment of interest. The amount of the prepaid interest must be included in A's income when the first payment is received, but is deductible by B only as it accrues after the date of the prepayment. Thus, B may deduct $50,038.08 ($543,892.17 × .092) of the prepaid interest as it accrues during the third accrual period and the remainder ($54,641.58 ($104,679.66 minus $50,038.08)) as it accrues during the fourth accrual period if such amounts are allowable as deductions.

Example (3). The facts are the same as in example (1), except that the sales price is $100,000 and the loan agreement calls for two installment payments of $64,857.18, each consisting of $50,000 of principal and $14,857.18 of interest. Since the loan provides for adequate stated interest and the total amount payable is less than $250,000, the allocation of principal and interest by A and B is respected even though A and B have allocated less interest to the first installment payment than the amount that has accrued as of the date the payment becomes due.

Example (4). The facts are the same as in example (3), except that the loan agreement provides that the first installment consists of $35,142.82 of principal and $29,714.36 of interest, and the second installment consists entirely of principal. Since the parties have allocated to the first payment more interest ($29,714.36) than the amount of interest that has accrued as of the date the first payment becomes due ($19,246.40 (($100,000 × .092) + ($109,200 × .092)), the excess of $10,467.96 is a prepayment of interest. The amount of the prepaid interest must be included in A's income when the first payment is received, but is deductible by B only as it accrues after the date of the prepayment.

Example (5). The facts are the same as in example (3), except that the sales price is $106,123.37 and the loan agreement provides that each installment consists of $53,055.60 of principal and $11,795.50 of interest. Thus, the loan does not provide for adequate stated interest. Since the loan does not provide for adequate stated interest, the allocation of interest by A and B will not be respected even though the total amount of payments due is less than $250,000. Thus, the first payment is treated as a payment of interest to the extent of $19,246.40.

Example (6). (i) Assume that on June 1, 1986, A sells personal property to B for $145,000. The contract calls for interest payable at 8 percent, compounded annually. Further, the contract calls for B to make annual payments of $36,316.19 beginning on December 31, 1987, and ending with a final payment on December 31, 1991. In addition, the contract calls for a payment of interest on December 31, 1986, of $6,657.95 for the period from June 1, 1986, to December 31, 1986. Thus, under paragraph (c)(2) (i) and (iv) of this section, the accrual period is one year and the first accrual period is a short period of 7 months. The allocation by the parties of interest and principal with respect to each $36,316.19 payment due under the contract is as follows:

Payment	Principal	Interest
1 $36,316.19	$24,716.19	$11,600.00
2. $36,316.19	26,693.49	9,622.70
3 $36,316.19	28,828.96	7,487.23
4 $36,316.19	31,135.28	5,180.91
5 $36,316.19	33,626.10	2,690.09

(ii) If the test and imputed rates of interest are 9.20 percent, compounded annually, the contract does not provide for adequate stated interest. At a rate of 9.20 percent, compounded annually, the present value of the 5 deferred payments and the 6 payments of stated interest is $139,819.50. Thus, if section 483 is otherwise applicable, the contract contains unstated interest equal to $5,180.50 (the excess of $145,000 (the sum of the deferred payments) over $139,819.50 (the sum of the present values of the deferred payments and stated interest)). Under paragraph (c)(3) of this section, the outstanding loan balance ("OLB") at the beginning of the first accrual period (the date of the sale or exchange) is $139,819.50.

(iii) Under § 1.483–3(b) and paragraph (b)(2)(ii) of this section, the exact method must be used to determine the amount of interest that accrues for the short first accrual period. In addition, for purposes of determining the fraction (f) with respect to the short period, a convention that assumes that a year consists of 12 30-day months must be used. Thus, the amount of interest that accrues for the short accrual period from June 1, 1986, through December 31, 1986, is $7,365.75 ($139,819.50 × [(1 + .092) 210/360 − 1]). Since the amount of the payment at the end of the short accrual period ($6,657.95) is less than the amount of accrued interest, the entire payment is treated as interest.

(iv) The amount of interest that accrues for each accrual period following the short period (determined under paragraph (b)(2) of this section) is set forth in the following schedule:

Accrual period	OLB at the beginning of accrual period	Accrued interest
1987	$140,527.30	$12,928.51
1988	117,139.62	10,776.85
1989	91,600.26	8,427.23
1990	63,711.32	5,861.44
1991	33,256.58	3,059.61

(The schedule reflects minor adjustments attributable to rounding.)

(v) A payment of $36,316.19 is due on December 31, 1987. As of the date this payment is due, interest of $20,294.26 will have accrued ($7,365.75 plus $12,928.51). The amount of this payment that is treated as interest is $13,636.31 (total interest accrued ($20,294.26) minus the amount previously treated as interest ($6,657.95)). The four subsequent payments of $36,316.19 are treated as payments of interest to the extent interest accrues during the year prior to the payment.

Example (7). (i) Assume that on January 1, 1986, A sells new section 38 property to B for $30,000 under a contract calling for 10 percent interest, compounded monthly. The contract calls for 24 monthly payments of $1,384.35 (each consisting of 10 percent interest on the unpaid principal balance of the debt under the contract, and partial payment of principal) beginning with a payment on January 31, 1986, and ending with a payment on December 31, 1987. The allocation by the parties of interest and principal with respect to each $1,384.35 payment due under the contract is as follows:

Payment	Principal	Interest
1. $1,384.35	$1,134.35	$250.00
2. 1,384.35	1,143.80	240.55
3. 1,384.35	1,153.33	231.02
4. 1,384.35	1,162.94	221.40
5. 1,384.35	1,172.63	211.71
6. 1,384.35	1,182.41	201.94
7. 1,384.35	1,192.26	192.09
8. 1,384.35	1,202.20	182.15
9. 1,384.35	1,212.21	172.13
10. 1,384.35	1,222.32	162.03
11. 1,384.35	1,232.50	151.85
12. 1,384.35	1,242.77	141.58
13. 1,384.35	1,253.13	131.22
14. 1,384.35	1,263.57	120.78
15. 1,384.35	1,274.10	110.25
16. 1,384.35	1,284.72	99.63
17. 1,384.35	1,295.42	88.92
18. 1,384.35	1,306.22	78.13
19. 1,384.35	1,317.11	67.24
20. 1,384.35	1,328.08	56.27
21. 1,384.35	1,339.15	45.20
22. 1,384.35	1,350.31	34.04
23. 1,384.35	1,361.56	22.79
24. 1,384.35	1,372.91	11.44

(The schedule reflects minor adjustments attributable to rounding.)

(ii) Assume that the contract does not provide for adequate stated interest and that the imputed rate of interest is 12 percent, compounded monthly. Under § 1.483–1(b) the first six payments of principal are not treated as deferred payments since they are not due later than six months from the date of the sale or exchange. At a rate of interest of 12 percent, compounded monthly, the present value of the 18 deferred payments (payments 7 through 24) and 24 stated interest payments is $22,697.31. Thus, if section 483 is otherwise applicable, the contract contains total unstated interest of $353.22 (the excess of $23,050.53 (the sum of the deferred payments) over $22,697.31 (the sum of the present values of the deferred payments and stated interest)). Under paragraph (c)(3) of this section, the outstanding loan balance (OLB) of the contract at the beginning of the first accrual period (the date of the sale or exchange) is $22,697.31. The amount of interest that accrues for each accrual period is set forth in the following schedule:

Accrual period	OLB at the beginning of accrual period	Accrued interest	Payment at end of period
January 1986	$22,697.31	$226.97	$250.00
February 1986	22,674.28	226.74	240.55
March 1986	22,660.46	226.60	231.02
April 1986	22,656.06	226.56	221.40
May 1986	22,661.22	226.61	211.71
June 1986	22,676.12	226.76	201.94
July 1986	22,700.94	227.01	1,384.35
August 1986	21,543.60	215.44	1,384.35
September 1986	20,374.69	203.75	1,384.35
October 1986	19,194.09	191.94	1,384.35
November 1986	18,001.68	180.02	1,384.35
December 1986	16,797.34	167.97	1,384.35
January	15,580.97	155.81	1,384.35
February 1987	14,352.43	143.52	1,384.35
March 1987	13,111.60	131.12	1,384.35
April 1987	11,858.37	118.58	1,384.35
May 1987	10,592.60	105.93	1,384.35
June 1987	9,314.18	93.14	1,384.35
July 1987	8,022.97	80.23	1,384.35
August 1987	6,718.85	67.19	1,384.35
September 1987	5,401.69	54.02	1,384.35
October 1987	4,071.35	40.71	1,384.35
November 1987	2,727.72	27.28	1,384.35
December 1987	1,370.65	13.71	1,384.35

(The schedule reflects minor adjustments attributable to rounding.)

(iii) The amount of the first six payments ($1,356.62, the amount allocated to interest by the parties with respect to the first six payments) is less than the aggregate amount of interest that accrues for the first six months ($1,360.24). Thus, the aggregate amount of the payments is treated as interest. (The fact that a portion of the first three payments represents a prepayment of interest is of no consequence if A and B are both calendar year taxpayers.) As of July 31, 1986, the amount of accrued and unpaid interest is $230.63 (the interest accruing for the seventh accrual period ($227.01) plus the accrued and unpaid interest from the six preceding accrual periods ($3.62)). Thus, the payment of $1,384.35 due on July 31, 1986, is treat as interest to the extent of the accrued and unpaid interest ($230.63), and the remainder of the payment is treated as principal. The seventeen subsequent payments are treated as interest to the extent interest accrues in the month preceding the payment and as principal to extent of any excess.

Example (8). (i) Assume that on January 1, 1987, A sells personal property (other than new section 38 property) to B for $100,000. The contract for sale calls for 10 annual payments of $14,902.95 (each representing a partial payment of the sales price and interest at 8 percent, compounded annually) beginning with a payment on January 1, 1988, and ending with a payment on January 1, 1997. The allocation by the parties of interest and principal with respect to each $14,902.95 payment follows the Rule of 78s. Thus, under the contract the amount of stated interest for each accural period is as follows:

Accrual period	Stated interest payment	Cumulative stated interest payment
1	$8,914.45	$8,914.45
2	8,023.00	16,937.45
3	7,131.56	24,069.01
4	6,240.12	30,309.13
5	5,348.67	35,657.80
6	4,457.23	40,115.03
7	3,565.78	43,680.81
8	2,674.34	46,355.15
9	1,782.89	48,138.04

Accrual period	Stated interest payment	Cumulative stated interest payment
10	891.45	49,029.49

(ii) Assume that the test and imputed rate of interest applicable to this contract is 9.2 percent, compounded annually, and section 483 is otherwise applicable. Thus, the contract contains unstated interest. The outstanding loan balance (OLB), the interest accrued for each annual period, and the cumulative interest at the end of each accrual period are as follows:

Accrual period	OLB at the beginning of accrual period	Accrued interest	Cumulative interest accrual
1	$94,805.80	$8,722.13	$8,722.13
2	88,624.98	8,153.50	16,875.63
3	81,875.53	7,532.55	24,408.18
4	74,505.13	6,854.47	31,262.65
5	66,456.65	6,114.02	37,376.66
6	57,667.71	5,305.43	42,682.09
7	48,070.19	4,422.46	47,104.55
8	37,589.70	3,458.25	50,562.80
9	26,145.00	2,405.34	52,968.14
10	13,647.39	1,255.56	54,223.70

(iii) The stated interest payment for the first annual accrual period ($8,914.45) exceeds the interest that accrues for the first accrual period ($8,722.13) by $192.32. Thus, the first payment is treated as a payment of accrued interest to the extent of $8,722.13, a prepayment of interest to the extent of $192.32, and a payment of principal to the extent of $5,988.50. A has interest income of $8,914.45 with respect to the payment, but B's interest deduction is limited to $8,722.13. B may deduct the prepayment of interest only as interest accrues during the second accrual period.

(iv) As of January 1, 1989, the total amount of accrued interest is $16,875.63. The amount previously treated as interest is $8,914.45. Thus, the second payment consists of accrued interest to the extent of $7,961.18 (the excess of $16,875.63 over $8,914.45). The amount of stated interest included in the second payment ($8,023.00) exceeds the total amount of accrued interest reduced by the amount of stated interest included in the first payment ($16,875.63 − $8,914.45 = $7,961.18). Accordingly, the second payment is treated as a prepayment of interest to the extent of $61.82 (the excess of $8,023.00 over $7,961.18). The balance of $6,879.95 is treated as a payment of principal.

(v) A has interest income of $8,023.00 with respect to the second payment. B may deduct $7,961.18 of accrued interest with respect to the second payment. The prepayment of interest with respect to the second payment ($61.82) is deductible only as interest accrues during the third accrual period.

(vi) As of January 1, 1990, the total amount of accrued interest is $24,408.18. The amount previously treated as interest is $16,937.45 ($8,914.45 plus $8,023.00). Thus, the third payment consists of accrued interest to the extent of $7,470.73 (the excess of $24,408.18 over $16,937.45). Since the amount of stated interest ($7,131.58) does not exceed the total amount of accrued interest reduced by the amount of stated interest included in the first two payments ($24,408.18 − $16,937.45 = $7,470.73) no portion of the third payment is treated as a prepayment of interest and the balance of the payment ($7,432.22) is treated as principal.

(vii) A has interest income of $7,470.73 with respect to the third payment and B may deduct this amount.

(viii) For the seven remaining payments, the accrued interest exceeds the stated interest. Thus, each payment is treated as interest to the extent of the accrued interest for the preceding accrual period and principal to the extent of the balance of the payment.

(h) *Effective date*—(1) *In general.* This section applies with respect to any lending or deferred payment transaction that occurs after May 8, 1986 and is not pursuant to a written contract that was binding on such date and at all times thereafter before the transaction.

(2) *Transactions subject to section 483.* In the case of deferred payment transactions that do not provide adequate stated interest and to which section 483 is otherwise applicable, this section applies with respect to any transaction to which the amendment made by section 41(b) of the Tax Reform Act of 1984 applies. For rules relating to the circumstances in which the amendment made by that section applies to a transaction, see § 1.483–1(e).

Par. 9. In paragraph (d) of § 1.451–1 the heading and text are revised to read as follows:

§ 1.451–1 General rule for taxable year of inclusion.

* * * * *

(d) *Special rule for inclusion of original issue discount.* For inclusion of original issue discount in respect of certain debt instruments issued after May 27, 1969, see section 1272.

* * * * *

Par. 10. Paragraph (b) of § 1.451–2 is amended by removing the eighth and ninth sentences and adding in their place new sentences to read as follows:

§ 1.451–2 Constructive receipt of income.

* * * * *

(b) *Examples of constructive receipt.* * * * However, in the case of certain deposits made after December 31, 1970, in banks, domestic building and loan associations, and similar financial institutions, the inclusion rules of section 1272 apply. See §§ 1.1232–3A and 1.1272–1. * * *

Par. 11. Paragraph (a)(1)(i) of § 1.454–1 is revised to read as follows:

§ 1.454–1 Obligations issued at discount.

(a) *Certain non-interest bearing obligations issued at discount*—(1) *Election to include increase in income currently.* If a taxpayer owns—

(i) A non-interest bearing obligation issued at a discount and redeemable for fixed amounts increasing at stated intervals (other than adebt instrument issued after May 27, 1969, as to which inclusion of original issue discount is required under section 1272), or

* * * * *

Par. 12. Paragraphs (a) and (c)(2) of § 1.482–2 are revised to read as follows:

§ 1.482–2 Determination of taxable income in specific situations.

(a) *Loans or advances*—(1) *Interest on bona fide indebtedness*—(i) *In general.* Where one member of a group of controlled entities makes a loan or advance directly or indirectly to, or otherwise becomes a creditor of, another member of such group and either charges no interest, or charges interest at a rate which is not equal to an arm's length rate of interest (as defined in paragraph (a)(2) of this section) with respect to such loan or advance, the district director may make appropriate allocations to reflect an arm's length rate of interest for the use of such loan or advance.

(ii) *Application of paragraph (a) of this section*—(A) *Interest on bona fide indebtedness.* Paragraph (a) of this section applies only to determine the appropriateness of the rate of interest charged on the principal amount of a bona fide indebtedness between members of a group of controlled entities, including—

(*1*) Loans or advances of money or other consideration (whether or not evidenced by a written instrument), and

(*2*) Indebtedness arising in the ordinary course of business from sales, leases, or the rendition of services by or between members of the group, or any other similar extension of credit.

(B) *Alleged indebtedness.* This paragraph (a) does not apply to so much of an alleged indebtedness which is not in fact a bona fide indebtedness, even if the stated rate of interest thereon would be within the safe haven rates prescribed in paragraph (a)(2)(iii) of this section. For example, paragraph (a) of this section does not apply to payments with respect to all or a portion of such alleged indebtedness where in fact all or a portion of an alleged indebtedness is a contribution to the capital of a corporation or a distribution by a corporation with respect to its shares. Similarly, this paragraph (a) does not apply to payments with respect to an alleged purchase-money debt instrument given in consideration for an alleged sale of property between two controlled entities where in fact the transaction constitutes a lease of the property. Payments made with respect to alleged indebtedness (including alleged stated interest thereon) shall be treated according to their substance. See § 1.482-2(a)(3)(i).

(iii) *Interest period.* The interest period with respect to a bona fide indebtedness between controlled entities commences on the date the indebtedness arises. However, with respect to indebtedness described in paragraph (a)(1)(ii)(A)(2) of this section that is not evidenced by a written instrument requiring payment of interest, the interest period is not required to commence until a date sixty days (six months in the case of such indebtedness arising before [Insert date after date this document is published in the **Federal Register** as a final rule]) after the date the indebtedness arises, or until a later date if the taxpayer is able to demonstrate that either it or others in its industry, as a regular trade practice, permit comparable balances in the case of similar transactions with unrelated parties to remain outstanding for a longer period without charging interest.

(iv) *Payment; book entries.* In determining the period of time for which a balance is outstanding, payments or credits shall be applied first against any accrued interest and then against the earliest balance outstanding; however, the taxpayer may apply such payments or credits in some other order on its books in accordance with an agreement or understanding of the parties if the taxpayer can demonstrate that either it or others in its industry, as a regular trade practice, enter into such agreements or understandings in the case of similar balances with unrelated parties.

(2) *Arm's length interest rate*—(i) *In general.* For purposes of section 482 and paragraph (a) of this section, an arm's length rate of interest shall be a rate of interest which was charged, or would have been charged, at the time the indebtedness arose, in independent transactions with or between unrelated parties under similar circumstances. All relevant factors shall be considered, including the principal amount and duration of the loan, the security involved, the credit standing of the borrower, and the interest rate prevailing at the situs of the lender or creditor for comparable loans between unrelated parties.

(ii) *Funds obtained at situs of borrower.* Notwithstanding the other provisions of paragraph (a)(2) of this section, if the loan or advance represents the proceeds of a loan obtained by the lender at the situs of the borrower, the arm's length rate for any taxable year shall be equal to the rate actually paid by the lender increased by an amount which reflects the costs or deductions incurred by the lender in borrowing such amounts and making such loans, unless the taxpayer establishes a more appropriate rate under the standards set forth in paragraph (a)(2)(i) of this section.

(iii) *Safe haven interest rates for certain loans and advances made after May 8, 1986*—(A) *Applicability*—(*1*) *General rule.* Except as otherwise provided in paragraph (a)(2) of this section, paragraph (a)(2)(iii)(B) applies with respect to the rate of interest charged and to the amount of interest paid or accrued in any taxable year—

(*i*) Under a term loan or advance between members of a group of controlled entities where (except as provided in paragraph (a)(2)(iii)(A)(*2*)(*ii*)) the loan or advance is entered into after May 8, 1986, and

(*ii*) After May 8, 1986 under a demand loan or advance between such controlled entities.

(*2*) *Grandfather rule for existing loans.* The safe haven rates prescribed in paragraph (a)(2)(iii)(B) of this section shall not apply, and the safe haven rates prescribed in 26 CFR § 1.482-2(a)(2)(iii) (revised as of April 1, 1985) shall apply to—

(i) Term loans or advances made before May 9, 1986 proposed rule, and

(ii) Term loans or advances made before August 7, 1986, pursuant to a binding written contract entered into before May 9, 1986.

(B) *Safe haven interest rate based on applicable Federal rate.* Except as otherwise provided in this paragraph (a)(2), in the case of a loan or advance between members of a group of controlled entities, an arm's length rate of interest referred to in paragraph (a)(2)(i) of this section shall be for purposes of Chapter 1 of the Code—

(*1*) The rate of interest actually charged if that rate is—

(i) Not less than 100 percent of the applicable Federal rate (the "lower limit"), and

(ii) Not greater than 130 percent of the applicable Federal rate (the "upper limit"), or

(*2*) If either no interest is charged or if the rate of interest charged is less than the lower limit, then an arm's length rate of interest shall be equal to the lower limit, compounded semiannually, or

(*3*) If the rate of interest charged is greater than the upper limit, then an arm's length rate of interest shall be equal to the upper limit, compounded semiannually,

unless the taxpayer establishes a more appropriate compound rate of interest under paragraph (a)(2)(i) of this section. However, if the compound rate of interest actually charged is greater than the upper limit and less than the rate determined under paragraph (a)(2)(i) of this section, or if the compound rate actually charged is less than the lower limit and greater than the rate determined under paragraph (a)(2)(i), then the compound rate actually charged shall be deemed to be an arm's length rate under paragraph (a)(2)(i). In the case of any sale-leaseback described in section 1274(*e*), the lower limit shall be 110 percent of the applicable Federal rate, compounded semiannually.

(C) *Applicable Federal rate.* For purposes of paragraph (a)(2)(iii)(B) of this section, the term "applicable Federal rate" means, in the case of a loan or advance to which this section applies and having a term of—

(*1*) Not over 3 years, the Federal short-term rate,

(*2*) Over 3 years but not over 9 years, the Federal mid-term rate, or

(*3*) Over 9 years, the Federal long-term rate,

as determined under section 1274(d) in effect on the date such loan or advance is made. In the case of any sale or exchange between controlled entities, the lower limit shall be the lowest of the applicable Federal rates in effect for any month in the 3-calendar-month period ending with the first calendar month in which there is a binding written contract in effect for such sale or exchange (the "lowest 3-month rate", as defined in section 1274(d)(2)). In the case of a demand loan or advance to which this section applies, the "applicable Federal rate" means the Federal short-term rate determined under section 1274(d) (determined without regard to the lowest 3-month short term rate determined under section 1274(d)(2)) in effect for each day on which any amount of such loan or advance (including unpaid accrued interest determined under paragraph (a)(2) of this section) is outstanding.

(D) *Lender in business of making loans.* If the lender in a loan or advance transaction to which paragraph (a)(2) of this section applies is regularly engaged in the trade or business or making loans or advances to unrelated parties, the safe haven rates prescribed in paragraph (a)(2)(iii)(B) shall not apply, and the arm's length interest rate to be used shall be determined under the standards described in paragraph (a)(2)(i), including reference to the interest rates charged in such trade or business by the lender on loans or advances of a similar type made to unrelated parties at and about the time the loan or advance to which paragraph (a)(2) of this section applies was made.

(E) *Foreign currency loans.* The safe haven interest rates prescribed in paragraph (a)(2)(iii)(B) of this section do not apply to any loan or advance the principal or interest of which is expressed in a currency other than U.S. dollars. A loan or advance the interest or principal of which may be repaid at the option of either the lender or the borrower in or by reference to a fixed amount of U.S. dollars is not a loan or advance described in the preceding sentence.

(3) *Coordination with interest adjustments required under certain other Code sections.* If the stated rate of interest on the stated principal amount of a loan or advance between controlled entities is subject to adjustment under section 482 and is also subject to adjustment under any other section of the Code (for example, section 467, 483, 1274 or 7872), section 482 and paragraph (a) of this section may be applied to such loan or advance in addition to such other Code section. After the enactment of the Tax Reform Act of 1984, Pub. L. 98–369, and the enactment of Pub. L. 99–121, such other Code sections include sections 467, 483, 1274 and 7872. The order in which the different provisions shall be applied is as follows:

(i) First, the substance of the transaction shall be determined; for this purpose, all the relevant facts and circumstances shall be considered and any law or rule of law (assignment of income, step transaction, etc.) may apply. Only the rate of interest with respect to the stated principal amount of the bona fide indebtedness (within the meaning of paragraph (a)(1) of this section), if any, shall be subject to adjustment under section 482, paragraph (a) of this section, and any other Code section.

(ii) Second, the other Code section shall be applied to the loan or advance to determine whether any amount other than stated interest is to be treated as interest, and if so, to determine such amount according to the provisions of such other Code section.

(iii) Third, whether or not the other Code section applies to adjust the amounts treated as interest under such loan or advance, section 482 and paragraph (a) of this section may then be applied by the district director to determine whether the rate of interest charged on the loan or advance, as adjusted by any other Code section, is greater or less than an arm's length rate of interest, and if so, to make appropriate allocations to reflect an arm's length rate of interest.

(iv) Fourth, section 482 and paragraphs (b) through (e) of this section, if applicable, may be applied by the district director to make any appropriate allocations, other than an interest rate adjustment, to reflect an arm's length transaction based upon the principal amount of the loan or advance and the interest rate as adjusted under paragraph (a)(3) (i), (ii) or (iii) of this section. For example, assume that two commonly controlled taxpayers enter into a deferred payment sale of tangible property and no interest is provided, and assume also that section 483 is applied to treat a portion of the stated sales price as interest, thereby reducing the stated sales price. If after this recharacterization of a portion of the stated sales price as interest, the recomputed sales price does not reflect an arm's length sales price under the principles of paragraph (e) of this section, the district director may make other appropriate allocations (other than an interest rate adjustment) to reflect an arm's length sales price.

(4) *Examples.* The principles of paragraph (a)(3) of this section may be illustrated by the following examples:

Example (1). An individual, A, transfers $20,000 to a corporation controlled by A in exchange for the corporation's note which bears adequate stated interest. The district director recharacterizes the transaction as a contribution to the capital of the corporation in exchange for preferred stock. Under paragraph (a)(3)(i) of this section, section 1.482–2(a) does not apply to the transaction because there is no bona fide indebtedness.

Example (2). B, an individual, is an employee of Z corporation, and is also the controlling shareholder of Z. Z makes a demand loan of $15,000 to B at a rate of interest that is less than the applicable Federal rate. In this instance the other operative Code section is section 7872. Under section 7872(b), the difference between the amount loaned and the present value of all payments due under the loan using a discount rate equal to 100 percent of the applicable Federal rate is treated as an amount of cash transferred from the corporation to B and such amount is treated as interest. Under paragraph (a)(3)(iii) of this section, section 482 and paragraph (a) of this section may also be applied by the district director to determine if the rate of interest charged on this $15,000 loan (100 percent of the AFR, compounded semiannually, as adjusted by section 7872) is an arm's length rate of interest. Because the rate of interest on the loan, as adjusted by section 7872, is within the safe haven range of 100–130 percent of the AFR, compounded semiannually, no further interest rate adjustments under section 482 and paragraph (a) of this section will be made to this loan.

Example (3). The facts are the same as in example (2) except that the amount lent by Z to B is 9,000, and that amount is the aggregate outstanding amount of loans between Z and B. Under the $10,000 *de minimis* exception of section 7872(c)(3), no adjustment for interest will be made to this $9,000 loan under section 7872. Under paragraph (a)(3)(iii) of this section, the district director may apply section 482 and paragraph (a) of this section to this $9,000 loan to determine whether the rate of interest charged is less than an arm's length rate of interest, and if so, to make appropriate allocations to reflect an arm's length rate of interest.

Example (4). X and Y are commonly controlled taxpayers. At a time when the applicable Federal rate is 12 percent, compounded semiannually, X sells property to Y in exchange for a note with a stated rate of interest of 18 percent, compounded semiannually. Assume that the other applicable Code section to the transaction is section 483. Section 483 does not apply to this transaction because, under section 483(d), there is no total unstated interest under the contract using the test rate of interest equal to 100 percent of the applicable Federal rate. Under paragraph (a)(3)(iii) of this section, section 482 and paragraph (a) of this section may be applied by the district director to determine whether the rate of interest under the note is excessive, that is, to determine whether the 18 percent stated interest rate under the note exceeds an arm's length rate of interest.

Example (5). Assume that A and B are commonly controlled taxpayers and that the applicable Federal rate is 10 percent, compounded semiannually. On June 30, 1986, A sells property to B and receives in exchange B's purchase-money note in the amount of $2,000,000. The stated interest rate on the note is 9%, compounded semiannually, and the stated redemption price at maturity on the note is $2,000,000. Assume that the other applicable Code section to this transaction is section 1274. Because the stated principal amount of B's note does not exceed $2,800,000, the discount rate used for purposes of section 1274 will be 9 percent, compounded semiannually, see section 1274A. Section 1274 does not apply to this transaction because there is adequate stated interest on the debt instrument using a discount rate equal to 9%, compounded semiannually, and the stated redemption price at maturity does not exceed the stated principal amount. Under paragraph (a)(3)(iii) of this section, the district director may apply section 482 and paragraph (a) of this section to this $2,000,000 note to determine whether the 9% rate of interest charged is less than an arm's length rate of interest, and if so, to make appropriate allocations to reflect an arm's length rate of interest.

* * * * *

(c) *Use of tangible property* * * *

(2) *Arm's length charge*—(i) *In general.* For purposes of paragraph (c) of this section, an arm's length rental charge shall be the amount of rent which was charged, or would have been charged for the use of the same or similar property, during the time it was in use, in independent transactions with or between unrelated parties under similar circumstances considering the

period and location of the use, the owner's investment in the property or rent paid for the property, expenses of maintaining the property, the type of property involved, its condition, and all other relevant facts.

(ii) *Safe haven rental charge.* See 26 CFR § 1.482–2(c)(2)(ii) (revised as of April 1, 1985), for the determination of safe haven rental charges in the case of certain leases entered into before May 9, 1986, and for leases entered into before August 7, 1986, pursuant to a binding written contract entered into before May 9, 1986.

(iii) *Subleases.* (A) Except as provided in paragraph (c)(2)(iii)(B) of this section, where possession, use, or occupancy of tangible property, which is leased by the owner (lessee) from an unrelated party is transferred by sublease or other arrangement to the user, an arm's length rental charge shall be considered to be equal to all the deductions claimed by the owner (lessee) which are attributable to the property for the period such property is used by the user. Where only a portion of such property was transferred, any allocations shall be made with reference to the portion transferred. The deductions to be considered include the rent paid or accrued by the owner (lessee) during the period of use and all other deductions directly and indirectly connected with the property paid or accrued by the owner (lessee) during such period. Such deductions include deductions for maintenance and repair, utilities, management and other similar deductions.

(B) The provisions of paragraph (c)(2)(iii)(A) of this section shall not apply if either—

(*1*) The taxpayer establishes a more appropriate rental charge under the general rule set forth in paragraph (c)(2)(i) of this section, or

(*2*) During the taxable year, the owner (lessee) or the user was regularly engaged in the trade or business of renting property of the same general type as the property in question to unrelated persons.

* * * * *

Par. 13. Sections 1.483–1 and 1.483–2 are revised and new §§ 1.483–3 through 1.483–5 are added immediately after § 1.483–2. The revised and added provisions read as follows:

§ 1.483–1 Interest on certain deferred payments.

(a) *Amount constituting interest in certain deferred payment transaction*—(1) *In general.* Section 483 applies, subject to the exceptions and limitations of paragraph (c) (2) and (3) of this section, to a contract for the sale or exchange of property if—

(i) The sale or exchange is described in paragraph (c)(1) of this section,

(ii) The contract provides for payments due more than one year after the date of the sale or exchange, and

(iii) The contract does not provide for adequate stated interest (within the meaning of § 1.483–2).

For purposes of section 483, the term sale or exchange includes any transaction treated as a sale or exchange for tax purposes. Section 483 may apply to a contract whether the contract is express (written or oral) or implied. In general, all payments made after the date of a sale or exchange are considered as made under a contract for that sale or exchange. For purposes of section 483, the term "property" includes debt instruments and investment units, but does not include money, services, or the right to use property. For the treatment of certain payments for use of property or services, see sections 404 and 467.

(2) *Treatment of contracts to which section 483 applies*—(i) *In general.* A contract that does not provide for adequate stated interest contains unstated interest. For rules relating to the treatment of unstated interest, see paragraph (a)(2)(ii) of this section. For rules relating to the determination of the total amount of unstated interest, see § 1.483–3. For rules relating to the method of accounting for interest (including unstated interest) under a contract to which section 483 applies, see § 1.446–2.

(ii) *Treatment of unstated interest.* If section 483 applies to a contract, unstated interest under the contract is treated as interest for tax purposes. Thus, for example, unstated interest is not treated as part of the amount realized from the sale or exchange of property (in the case of the seller) or as part of the cost of the property (in the case of the purchaser), and is generally not included in the basis to the purchaser of any property acquired in the sale or exchange.

(iii) *Certain transactions between related parties.* For rules relating to the determination of basis of property in certain transactions between related parties, see § 1.1012–2.

(b) *Deferred payments*—(1) *In general.* For purposes of section 483, a deferred payment means any payment on account of the sale or exchange that constitutes all or part of the sales price (as defined in paragraph (b)(2) of this section), and that is due more than 6 months after the date of the sale or exchange. A payment may be made in the form of cash, stock or securities, or other property (except as provided in paragraph (b)(3) of this section).

(2) *Meaning of sales price.* For purposes of section 483, the sales price with respect to any sale or exchange means the amount due under the contract (other than interest provided in the contract), and the amount of any liability included in the amount realized from the sale or exchange (see § 1.1001–2). Thus, the sales price with respect to any sale or exchange includes any amount of unstated interest under the contract.

(3) *Treatment of debt instruments.* For purposes of section 483, a debt instrument of a purchaser which is given in consideration for the sale or exchange of property is not a payment, and any payment due under the debt instrument is to be treated as due under the contract for the sale of exchange. For the meaning of the term "debt instrument," see section 1275(a)(1) and § 1.1275–1(b).

(c) *Transactions to which section 483 may apply*—(1) *In general.* Section 483 may apply only in the case of a sale or exchange of property to which section 1274 does not apply by reason of—

(i) Section 1274(c)(4)(A) and § 1.1274–1(b)(2), relating to certain sales or exchanges of farms for $1,000,000 or less;

(ii) Section 1274(c)(4)(B) and § 1.1274–1(b)(3), relating to certain sales or exchanges of principal residences;

(iii) Section 1274(c)(4)(C) and § 1.1274–1(b)(4), relating to sales or exchanges for which the total payments do not exceed $250,000;

(iv) Section 483(e) and § 1.483–4(b)(2), relating to qualified sales; or

(v) Section 1274A(c)(2) and § 1.1274A–1(c), relating to cash method debt instruments.

(2) *Exceptions to the application of section 483*—(i) *Publicly traded debt instruments or property.* Section 483 does not apply to any debt instrument to which section 1273(b)(3) applies. Thus, section 483 does not apply to any contract for the sale of property if the only deferred payments are required under a publicly traded debt instrument. Similarly, section 483 does not apply to any contract for the sale or exchange of publicly traded property.

(ii) *Sales price of $3,000 or less.* Section 483 does not apply to a contract for the sale or exchange of property if it can be determined at the time of the sale or exchange that the sales price (within the meaning of paragraph (b)(2) of this section) cannot exceed $3,000. If it cannot be determined at the time of the sale or exchange that the sales price cannot exceed $3,000, this exception does not apply even if the sales price eventually paid for the property is less than $3,000. For purposes of determining whether the sales price of property exceeds $3,000, all sales or exchanges which are part of the same transaction (or a series of related transactions) shall be aggregated in accordance with the rules in § 1.1274A–1(d).

(iii) *Certain transfers subject to section 1041.* Section 483 does not apply to any transfers of property subject to section 1041 (relating to transfers of property between spouses or incident to divorce).

(3) *Limitations on the application of section 483—*(i) *Carrying charges.* In the case of the purchaser, the tax treatment of amounts paid on account of the sale or exchange of property shall be determined without regard to section 483 if such amounts are treated under section 163(b) (relating to deduction for interest on certain installment purchases) as if they include interest. Thus, the purchaser computes interest deductions with respect to payments under a contract to which section 163(b) applies under that section and without regard to section 483, even though the amount treated as interest under section 163(b) differs from the amount treated as interest income by the seller under section 483.

(ii) *Certain sales of patents.* Section 483 does not apply to any amount payable with respect to a transfer by an individual seller (holder) described in section 1235 (relating to sales or exchanges or patents) that is contingent on the productivity, use, or disposition of the property transferred.

(iii) *Transactions involving personal use property—*(A) *Treatment of obligors.* Section 483 does not apply to an obligor (issuer) under a debt instrument given in consideration for the sale or exchange of property that is personal use property (within the meaning of section 1275(b)(3) and § 1.1275–2(f)(3)) in the hands of the issuer. Thus, in the case of the issuer, the tax treatment of any amount payable under such debt instrument is determined without regard to section 483 and the regulations thereunder.

(B) *Treatment of certain obligees.* Section 483 does not apply to an obligee (holder) under a debt instrument that (1) is given in consideration for the sale or exchange of property that is personal use property (within the meaning of section 1275(b)(3) and § 1.1275–2(f)(3)) in the hands of the issuer, and (2) evidences a loan described in section 7872(c)(1)(A) (relating to gift loans), 7872(c)(1)(B) (relating to compensation-related loans), or 7872(c)(1)(C) (relating to corporation-shareholder loans). For rules relating to the treatment of loans described in the preceding sentence, see section 7872 and the regulations thereunder.

(iv) *Transactions involving certain demand loans.* Section 483 does not apply to any payment under a debt instrument that evidences a demand loan (within the meaning of section 7872(f)(5)) described in section 7872(c)(1)(A) (relating to gift loans), 7872(c)(1)(B) (relating to compensation-related loans), or 7872(c)(1)(C) (relating to corporation-shareholder loans). For rules relating to the treatment of loans described in the preceding sentence, see section 7872 and the regulations thereunder.

(v) *Transactions involving certain annuity contracts.* Section 483 does not apply to any payment under an annuity contract described in section 1275(a)(1)(B) (relating to annuity contracts excluded from the definition of debt instrument).

(d) *Modifications and assumptions.* A modification of a debt instrument shall be treated as a sale or exchange of property for purposes of section 483 if the modified debt instrument would be treated under § 1.1274–1(c) as a new debt instrument given in consideration for the unmodified debt instrument. In addition, debt instruments assumed or taken subject to in connection with a sale or exchange shall be treated for purposes of section 483 in a manner consistent with the rules of § 1.1274–7. Thus, for example, if a debt instrument assumed in connection with a sale or exchange is not modified as part of the sale or exchange, section 483—

(1) Shall not apply to any payment under the debt instrument in the case of a sale or exchange occurring after June 30, 1985, or a debt instrument issued before October 16, 1984; and

(2) Shall apply to payments under the debt instrument (except as provided in § 1.1274–7(b)(3) and section 44(b)(7) of the Tax Reform Act of 1984 (as amended by Pub. L. 98–612)) solely for purposes of determining the tax consequences of the sale or exchange to the buyer in the case of a debt instrument issued after October 15, 1984, and assumed in connection with a sale or exchange occurring before July 1, 1985.

(e) *Effective date.* Sections 1.483–1 through 1.483–5 apply, except as otherwise provided in this paragraph (e), to any sale or exchange occurring after December 31, 1984, unless the sale or exchange is made pursuant to a written contract (including an irrevocable written option) which was binding on March 1, 1984. For this purpose, a sale or exchange is not made pursuant to a written contract which was binding on March 1, 1984, if a substantial modification (within the meaning of § 1.1274–6(e)(1)(iii)) in the terms of a contract occurs after March 1, 1984, and before the sale or exchange. Sections 1.483–1 through 1.483–5 shall not apply to any modification of a debt instrument arising from a sale or exchange unless the debt instrument arises from a sale or exchange to which such sections apply (within the meaning of this paragraph (e)) or the debt instrument is assumed or taken subject to in connection with, and the modification is part of, such a sale. For rules relating to sales or exchanges occurring before January 1, 1985, sales or exchanges pursuant to a written contract (including an irrevocable written option) which was binding on March 1, 1984, and modifications of debt instruments to which §§ 1.483–1 through 1.483–5 do not apply by reason of the preceding sentence, see section 44(b)(3) of the Tax Reform Act of 1984, section 483 as in effect before its amendment by section 41(b) of the Tax Reform Act of 1984, and 26 CFR 1.483–1 and 1.483–2 (revised as of April 1, 1985).

§ 1.483–2 Adequate stated interest.

(a) *In general.* This section prescribes rules for determining whether a contract for the sale or exchange of property provides for adequate stated interest. The rules prescribed by this section apply to any contract whether the contract calls for the payment of principal in a lump sum, the periodic payment of principal, or irregular payments of principal. A contract generally provides for adequate stated interest if it calls for interest on the outstanding principal balance at a rate (with an appropriate compounding period) at least equal to the test rate of interest. For rules relating to the determination of the test rate of interest and rules relating to the appropriate compounding period, see § 1.483–4. Paragraph (b) of this section provides rules for determining adequate stated interest (except with respect to certain cash method debt instruments) if the contract provides for a fixed rate of interest and compounding or payment of interest at regular intervals. Paragraph (c) of this section provides rules for determining adequate stated interest in the case of contracts that do not satisfy the requirements of paragraph (b) of this section. For special rules relating to contracts calling for variable rates of interest, see paragraph (d) of this section. For special rules relating to contracts calling for contingent payments of interest, see paragraph (e) of this section.

(b) *Certain contracts that provide for a stated rate of interest*—(1) *In general.* A contract provides for adequate stated interest if on the date of the sale or exchange—

(i) The contract provides for interest on the outstanding principal balance due under the contract (the stated rate of interest) at a fixed rate;

(ii) The stated rate of interest is no lower than the test rate of interest (based on the appropriate compounding period);

(iii) The contract requires interest to be paid or compounded at the end of each compounding period for the entire term of the contract; and

(iv) In the case of a cash method debt instrument (within the meaning of section 1274A (c)(2) and § 1.1274A–1(c)), such debt instrument is not received in exchange for property in a potentially abusive situation (as defined in § 1.1274–4(g)).

For rules relating to the determination of adequate stated interest in the case of contracts that do not satisfy the requirements of this paragraph (b)(1), see paragraph (c) of this section. For rules relating to the test rate of interest, see § 1.483–4. For rules relating to the appropriate compounding period, see § 1.483–4(c).

(2) *Interest payable for a short period*—(i) *In general.* The stated rate of interest is a fixed rate within the meaning of paragraph (b)(1) of this section only if it also applies for short periods (that is, any period shorter than the compounding period on which the test rate of interest is based). For this purpose, the stated rate of interest applies for short periods if the interest payable for a short period is determined by either of the two alternative methods prescribed by this paragraph (b)(2), or by any other reasonable method.

The methods prescribed by this paragraph (b)(2) are the exact method and the approximate method. An example of another reasonable method is monthly compounding which reflects compounding of interest at the end of each month, with simple interest within a month. For this purpose and for purposes of determining the fraction (f) with respect to a short period under paragraph (b)(2) (ii) and (iii) of this section, a convention that assumes that a year consists of 12 30-day months may be adopted.

(ii) *Exact method.* The exact method assumes daily compounding of interest. Under this method, the amount of interest payable on an outstanding principal amount (P) for any short period is equal to the result of the following formula:

$I=P\times[(1+i/k)^{f}-1]$

In which:

I = Interest payable for the short period
i = The stated rate of interest expressed as a decimal
k = The number of compounding periods on which the stated rate of interest is based that are contained in a year
f = A fraction, the numerator of which is the length of the short period, and the denominator of which is the length of the full compounding period on which the stated rate of interest is based.

For illustrations of the application of the formula for the exact method, see paragraph (b)(3) of this section, examples (4), (6) and (8).

(iii) *Approximate method.* The approximate method is also provided for the convenience of taxpayers who do not desire to use the exact method. The approximate method assumes simple interest within any compounding period and always produces an amount of interest for the short period that is slightly higher than the amount of interest produced under the exact method. Under this method, the amount of interest payable on an outstanding principal amount for a short period is determined by multiplying the amount of stated interest for a full period by a fraction, the numerator of which is equal to the length of the short period and the denominator of which is the length of the full period. Thus, the amount of interest payable on an outstanding principal amount (P) for a short period is equal to the result of the following formula:

$I=P\times(i/k)\times f$

In which:

I = Interest payable for the short period
i = The stated rate of interest expressed as a decimal
k = The number of compounding periods on which the stated rate of interest is based that are contained in a year
f = A fraction, the numerator of which is the length of the short period, and the denominator of which is the length of the full compounding period on which the stated rate of interest is based.

For illustrations of the application of the formula for the appropriate method, see paragraph (b)(3) of this section, examples (5) and (7).

(3) *Examples.* The provisions of paragraph (b) of this section may be illustrated by the following examples:

Example (1). Assume that a contract for the sale of nonpublicly traded personal property calls for a $100,000 payment of principal at the end of a 10–year term and 20 semiannual payments of interest of $4,500 on the outstanding balance of the principal. The appropriate compounding period is semiannual. The test rate of interest is 9 percent based on semiannual compounding. The contract provides for adequate stated interest because it provides for interest equal to the 9 percent test rate of interest payable semiannually, the compounding period for the test rate.

Example (2). The facts are the same as in example (1), except that the debt instrument calls for 10 annual interest payments of $9,000. The appropriate compounding period is annual. The test rate of interest is 9.20 percent based on annual compounding. The contract does not provide for adequate stated interest because it does not provide for interest equal to 9.20 percent compounded annually, the rate of interest equivalent to 9 percent compounded semiannually.

Example (3). On May 1, 1986, A sells B nonpublicly traded personal property under a contract that calls for B to make a principal payment of $200,000 and 9.00 percent interest, $9,000 payable on June 30 and December 31 of each year beginning on December 31, 1986. The compounding period is semiannual. Assume that the debt instrument is a cash method debt instrument that is not received in exchange for property in a potentially abusive situation. The test rate of interest is 9 percent, compounded semiannually. Even though the contract calls for a stated rate of interest no lower than the test rate of interest, the contract does not provide for adequate stated interest because the stated rate of interest does not apply for the short period from May 1, 1986, through June 30, 1986.

Example (4). The facts are the same as in example (3), except that the contract calls for a payment of interest on June 30, 1986, for the period from May 1, 1986, through June 30, 1986 (one-third of a full compounding period). Under the exact method, the contract provides for adequate stated interest (that is, interest of 9 percent compounded semiannually) if the amount of interest payable on the outstanding principal balance for the short period is $2,956.09 determined as follows:

$\$200{,}000\times(1+.09/2)^{1/3}-1]=\$2{,}956.09$

Example (5). The facts are the same as in example (4), except that the amount payable on the outstanding principal balance for the short period is determined under the approximate method. Under the approximate method, the amount of stated interest payable for the short period is $3,000 determined as follows:

$\$200{,}000\times(.09/2)\times 1/3)=\$3{,}000$

Example (6). The facts are the same as in example (4), except that the sale occurs on May 20, 1986. Assume that a convention that assumes that a year consists of 12 30–day months is adopted for purposes of determining the fraction (f) with respect to the short period. Thus, f is 42/180 of the semiannual period. Under the exact method, the interest payable on June 30, 1986, for the short period is $2,064.71 determined as follows:

$\$200{,}000\times[(1+.09/2)42/180-1]=\$2{,}064.71$

Example (7). The facts are the same as in example (6), except that interest payable for the short period is determined under the approximate method. Under this method, the amount of interest payable on June 30, 1986, for the short period is $2,100.00 determined as follows:

$200,000 × (.09/2) × (42/180) = $2,100.00

Example (8). Assume that on July 4, 1986, personal property is sold for $88,000. The contract calls for an $8,000 down payment and monthly payments of $634.51 (consisting of 8.84 percent interest on the unpaid balance of the principal and a partial payment of principal) due on the first of each month for a period of 30 years beginning on September 1, 1986. In addition, the contract calls for an advance interest payment of $549.91 for the period from July 4, 1986, through July 31, 1986. The compounding period is monthly and the test rate of interest based on monthly compounding is 8.84 percent. The contract provides for adequate stated interest because it calls for interest payable at the stated rate of interest (8.84 percent) for the short period calculated under the exact method ($80,000 × [(+.0884/12)28/30 − 1] = $549.91), and interest for the remaining term of the contract at a rate of 8.84 percent payable monthly, the compounding period for the test rate.

(c) *Contracts that do not meet the requirements of paragraph (b)(1) of this section*—(1) *In general.* This paragraph (c)(1) applies to contracts and cash method debt instruments that do not meet the requirements of paragraph (b)(1) of this section.

A contract or cash method debt instrument to which this paragraph (c)(1) applies provides for adequate stated interest only if the sum of the deferred payments due under the contract or debt instrument does not exceed the amount described in paragraph (c)(2) of this section.

(2) *Amount described in paragraph (c)(2) of this section.* The amount described in this paragraph (c)(2) is—

(i) The sum of the present value of the deferred payments and any stated interest payments due under the contract; or

(ii) In the case of a cash method debt instrument (within the meaning of section 1274A(c)(2) and § 1.1274A-1(c)) received in exchange for property in a potentially abusive situation (as defined in § 1.1274-4(g)), the fair market value of such property reduced by the fair market value of any consideration other than the debt instrument.

(3) *Determination of present values.* For purposes of paragraph (c)(2) of this section, the present value of any payment is determined in accordance with the rules of § 1.483-3(b) except that the payment is discounted at the test rate of interest (as defined in § 1.483-4), and the approximate method as prescribed in § 1.1274-5(d)(2)(iii) or any other reasonable method may be used to determine the amount of discount for a short period. In addition, for purposes of determining the fraction (f) with respect to a short period, the use of the convention that assumes that a year consists of 12 30-day months is optional.

(4) *Examples.* The provisions of this paragraph (c) may be illustrated by the following examples:

Example (1). Assume that A sells B nonpublicly traded personal property for $60,000. The contract for sale calls for a lump sum payment of $150,000 (consisting of the $60,000 sales price and a $90,000 payment of interest) due in 10 years. The contract does not call for the compounding of interest at the end of each compounding period over the entire term of the contract. Accordingly, the contract provides for adequate stated interest only if the deferred payment does not exceed the present value of the deferred payment and the interest payment. Based on annual compounding (an appropriate compounding period), the test rate of interest is 9.20 percent. At a discount rate of 9.20 percent, the present value of the deferred payment and the interest payment is $62,210.67. Since the deferred payment of $60,000 does not exceed $62,210.67, the contract provides for adequate stated interest.

Example (2). Assume that in a potentially abusive situation, a contract for the sale of nonpublicly traded personal property calls for the issue of a cash method debt instrument with a stated principal amount of $700,000. No other consideration is given. The debt instrument calls for annual compounding of interest over its entire term at a rate of 9.20 percent (the test rate of interest applicable to the debt instrument). Thus, the present value of the deferred payment and the interest payments is $700,000. The fair market value of the property is $500,000. A cash debt method debt instrument received in exchange for property in a potentially abusive situation provides for adequate stated interest only if the deferred payment does not exceed the fair market value of the property. Since the deferred payment ($700,000) exceeds the fair market value of the property ($500,000), the debt instrument does not provide for adequate stated interest.

(d) *Treatment of contracts calling for variable rates of interest based on an interest index*—(1) *In general.* Except as provided in paragraphs (d) (2) and (3) of this section, a contract that calls for deferred payments under a variable rate debt instrument (within the meaning of § 1.1275-5) shall be treated for purposes of determining whether the contract provides for adequate stated interest as if the rate of interest determined under the index were a fixed rate equal to the rate of interest determined under the index as of the date when the test rate of interest is determined (see § 1.483-4). Thus, for any period in which interest is payable at a rate determined under the index, the rate of interest fixed by the index as of the date the test rate of interest is determined is treated for purposes of paragraph (b) of this section as the stated rate of interest, and is used to determine the amount of any stated interest payment for purposes of paragraph (c) of this section.

(2) *Limitation on increases in rate.* In the case of a contract that limits the number of percentage or basis points by which the rate of interest can vary from one period to the next—

(i) Paragraph (d)(1) of this section shall apply only if, for each period, the limitation permits the rate of interest to increase by at least as many percentage of basis points as such rate is permitted to decrease; and

(ii) Paragraph (a)(2) of § 1.1274-6 shall not apply if, by reason of such limitation, the number of percentage points by which the rate (based on annual compounding) can increase for any period is less than ½ of the number of months in the adjustment interval preceding such period.

For illustrations of the application of this paragraph (d)(2), see § 1.1274-3(d)(1)(v), examples (2), (3), (4) and (5).

(3) *Ceiling on variable rate of interest.* Paragraph (d)(1) of this section shall not apply to any contract that places a ceiling on the maximum rate of interest payable under the debt instrument unless—

(i) The excess of the rate initially fixed by the index over the test rate of interest plus the excess of the maximum rate permitted by the ceiling over the test rate is at least equal to 5 percentage points, and

(ii) In the case of a debt instrument with a term that exceeds 3 years, the maximum rate permitted by the ceiling is at least equal to the test rate of interest determined without regard to § 1.1274-6(a)(2) plus the difference between such rate and the actual test rate of interest.

For illustrations of the application of this paragraph (d)(3), see § 1.1274-3(d)(1)(v), examples (6), (7) and (8).

(4) *Treatment of payment if variable rate of interest rules do not apply.* If paragraph (d)(1) of this section does not apply to a contract, variable payments of interest under the contract are contingent payments of interest subject to the rules of § 1.483-5, but only to the extent such variable payments exceed the minimum payments of interest permitted under the contract. For this purpose, the minimum payment of interest permitted under the contract for any period shall be determined by taking into account any floor on the minimum rate of interest payable under the contract and, in the case of a contract described in paragraph (d)(2) of this section, the maximum permissible decrease in the interest rate for each period during the term of the contract.

(5) *Examples.* The provisions of this paragraph (d) may be illustrated by the following examples:

Example (1). Assume that a contract for the sale of nonpublicly traded property calls for the issue of a debt instrument in the principal amount of $75,000 due in ten years. The debt instrument calls for interest payable semiannually at a rate of 3 percentage points above the yield on 6-month Treasury bills for the mid-point of the semiannual period of the interest payment. The debt instrument is a variable rate debt instrument within the meaning of § 1.1275-5. The test rate of interest applicable to the debt instrument is 9 percent, compounded semiannually. Assume that the yield on 6-month Treasury bills on the date of the binding written contract for the sale is 8.89 percent. Thus, the debt instrument is tested for adequate stated interest as if it provided for a stated rate of interest of 11.89 percent (3 percent plus 8.89 percent), compounded semiannually, payable over its entire term. Since the test rate of interest is 9 percent, compounded semiannually, and the debt instrument is treated as providing for stated interest of 11.89 percent payable semiannually, the debt instrument provides for adequate stated interest.

Example (2). The facts are the same as in example (1), except that the interest payable at a rate equal to 3 percentage points above the yield on 6-month Treasury bills begins in the fourth year of the debt instrument. In the first, second, and third years of the debt instrument interest is payable semiannually at annual rates of 7, 8 and 9 percent, respectively. Thus, the debt instrument is treated as providing interest payable as follows:

Semiannual period	Interest rate [1]	Interest amount per period
1-2	7	$2,625.00
3-4	8	3,000.00
5-6	9	3,375.00
7-20	11.89	4,458.75

[1] Percent.

Since the debt instrument does not provide for interest payable at a rate at least equal to the test rate of 9 percent, compounded semiannually, over its entire term, it has adequate stated interest only if the deferred payment ($75,000) does not exceed the present value of the deferred payment and the interest treated as payable under the debt instrument. The present value of the deferred payment and the stated interest payments, using a discount rate of 9 percent, is $81,459.93. Since the deferred payment does not exceed the present value of the payments, the debt instrument provides for adequate stated interest.

(e) *Contingent interest*—(1) *In general.* Except as provided in this paragraph (e), contingent payments of interest are not taken into account in determining whether a contract provides for adequate stated interest. For additional rules relating to the treatment of contingent payments of interest, see § 1.483-5.

(2) *Special rule.* A contract provides for adequate stated interest if the contract provides for contingent payments of interest described in paragraph (e)(3) of this section, and the contract meets the requirements of paragraph (e)(4) of this section.

(3) *Nature of contingent interest taken into account in determining adequate stated interest.* A contingent payment of interest is described in this paragraph (e)(3) only if it is conditioned on a return from the exploitation of the property acquired under the contract. Such contingent interest payments include payments conditioned on profits, sales, rents, production, or royalties from the property.

(4) *Contingent interest as adequate stated interest*—(i) *In general.* A contract for the sale or exchange of property that does not include any recovery property (within the meaning of section 168(c)(1)) or any property described in section 1221(1) (relating to stock in trade, inventories, and other property held for sale to customers) provides for adequate stated interest if—

(A) The contract would satisfy paragraph (b) or (c) of this section (taking into account the provisions of paragraph (d) of this section) at a test rate equal to 80 percent of the test rate of interest applicable to the contract, and

(B) It is reasonable to expect (as of the date the test rate is determined) that contingent payments of interest described in paragraph (e)(3) of this section will raise the total yield on the contract to at least the test rate of interest applicable to the contract.

For an illustration of circumstances in which it is reasonable to expect that contingent interest will raise the total yield on a contract to at least the test rate of interest, see § 1.1274-3(d)(2)(v), example (1).

(ii) *Depreciable or inventoriable property.* A contract for the sale or exchange of property that includes any recovery property or any property described in section 1221(1) provides for adequate stated interest if—

(A) The contract satisfies the requirements of pararaph (e)(4)(i) of this section, and

(b) The term of the contract does not exceed 12 years (4 years in the case of a contract for the sale or exchange of property that includes any 3-year or 5-year property (within the meaning of section 168(c)) or any property described in section 1221(1)).

(iii) *Entity look-through rule.* For purposes of this paragraph (e)(4), the purchase of an interest in an entity shall be treated as a purchase of the underlying assets of the entity if the bases of the assets are determined, in whole or in part, by reference to the amount paid for such interest. If the entity owns any recovery property or property described in section 1221(1), paragrah (e)(4)(ii) of this section shall apply even with respect to that portion of the purchase price attributable to nonrecovery property that is not described in section 1221(1). For example, if one corporation purchases stock of another corporation owning nonrecovery property that is not described in section 1221(1) and at least one item of 3-year or 5-year property and makes an election under section 338 (relating to certain stock purchases treated as asset acquisitions), the stock purchase shall be treated as a purchase of 3-year or 5-year property for purposes of paragraph (e)(4)(ii) of this section.

(5) *Examples.* The provisions of this paragraph (e) may be illustrated by the following examples.

Example (1). Assume that a contract for the sale of 3-year property held for rent calls for the issue of a debt instrument due in 4 years. The debt instrument calls for interest at 7.5 percent payable annually and contingent interest equal to 5 percent of the gross rents from the property. Assume that the test rate of interest is 9.20 percent, compounded annually, and that it is reasonable to expect that the gross rents will be at least $68,000 per year. Rents of this amount would produce contingent interest payments of $3,400 per year which would raise the yield on the debt instrument to at least the test rate. The contract provides for adequate stated interest because the stated rate of interest is not lower than 80 percent of the test rate, the term of the debt instrument does not exceed 4 years, and it is reasonable to expect that the contingent interest payments will raise the yield to the test rate of interest.

Example (2). The facts are the same as in example (1), except that the debt instrument has a term of 5 years. Since the term of the contract exceeds 4 years and the stated rate of interest (7.5 percent, compounded annually) is lower than the test rate of interest (9.20 percent, compounded annually), the contract does not provide for adequate stated interest.

Example (3). The facts are the same as in example (1), except that the rental property is 19-year property and the term of the debt instrument is 10 years. The contract provides for adequate stated interest because the term of the debt instrument does not exceed 12 years.

§ 1.483-3 Unstated interest.

(a) *In general.* For purposes of section 483, the term "unstated interest" means an amount equal to the excess of—

(1) The sum of the deferred payments due under the contract, over

(2)(i) The sum of the present values of the deferred payments and the present values of any interest payments due under the contract, or

(ii) In the case of a cash method debt instrument (within the meaning of section 1274A(c)(2) and § 1.1274A–1(c)) received in exchange for property in a potentially abusive situation (as defined in § 1.1275–4(g)), the fair market value of such property (reduced by the fair market value of any consideration other than the debt instrument).

(b) *Determination of present values.* The present value of any deferred payment or interest payment is to be determined by discounting the payment from the time it becomes due to the date of the sale or exchange at the imputed rate of interest applicable to the contract in accordance with the provisions of § 1.1274–5. For rules relating to the imputed rate of interest, see § 1.483–4. For purposes of determining the amount of unstated interest when there is a short period (that is, a period shorter than a full compounding period) the exact method as prescribed in § 1.1274–5(d)(2)(ii) shall be used. In addition, for purposes of determining the fraction (f) with respect to a short period, a convention that assumes that a year consists of 12 30-day months shall be used. The exact method and 12 30-day month convention shall also be used for purposes of determining the amount of interest (including unstated interest) that accrues for a short first accrual period. See § 1.446–2.

(c) *Treatment of variable rate of interest in determining total unstated interest.* If paragraph (d)(1) of § 1.483–2 (relating to payments of interest based on an objective interest rate index) applies to a contract, the rate of interest fixed by the index as of the date the imputed rate of interest is determined is treated for purposes of determining the amount of unstated interest as the stated rate of interest for any period in which interest is payable at a rate determined under the index. If paragraph (d)(1) of § 1.483–2 does not apply to a contract (either because it does not call payments under a variable rate debt instrument (within the meaning of § 1.1275–5) or because, for example, the variable rate debt instrument places a nonqualifying ceiling on the variable rate), variable payments of interest under the contract shall be treated as contingent payments to the extent provided in § 1.483–2(d)(4) and shall be subject to the provisions of § 1.483–5.

(d) *Treatment of contingent payments in determining total unstated interest.* In the case of a contract calling for any contingent payment, total unstated interest shall be determined solely by reference to the noncontingent payments. For additional rules relating to the treatment of contingent payments, see § 1.483–5.

(e) *Examples.* The provisions of this section may be illustrated by examples (1), (6), (7) and (8) of § 1.446–2(h) and by the following examples:

Example (1). On January 1, 1986, A sells property to B for $100,000 under a contract for sale that calls for B to make a $100,000 deferred payment on January 1, 1986. The contract does not provide for any interest. The imputed rate of interest based on semiannual compounding is 9 percent. The contract contains unstated interest of $58,535.71 ($100,000 (the deferred payment) minus the present value of the deferred payment ($41,464.29)).

Example (2). The facts are the same as in example (1), except that, in lieu of the $100,000 lump sum payment, the contract calls for B to make a $10,000 payment on January 1 of each year beginning with a payment on January 1, 1987, and ending with a payment on January 1, 1996. The imputed rate of interest based on annual compounding is 9.20 percent. The contract contains unstated interest of $36,384.54 ($100,000 (the sum of the deferred payments) minus the present value of the stream of $10,000 deferred payments ($63,615.46)).

Example (3). The facts are the same as in example (1), except that the contract calls for B to make a payment of interest of $79,084.77 (6 percent interest compounded annually) together with the $100,000 deferred payment due on January 1, 1996. The contract contains unstated interest of $25,726.77 ($100,000 (the deferred payment) minus $74,273.23 (the sum of the present values of the deferred payment ($41,454.29) and the stated interest ($32,791.94))).

Example (4). The facts are the same as in example (1), except that the contract calls for 10 annual installment payments of $13,586.80 (each representing a partial payment of the sales price ($100,000) and interest at 6 percent, compounded annually) beginning with a payment on January 1, 1987, and ending with a payment on January 1, 1996. The contract contains unstated interest of $13,566.95 ($100,000 (the sum of the deferred payments) minus $86,433.05 (the present value of the stream of $13,586.80 payments consisting of deferred payments and stated interest)).

Example (5). On May 31, 1986, A sells property to B for $100,000. The contract calls for 5 annual installment payments of $23,739.64 (each representing a partial payment of the sales price and 6 percent interest, compounded annually) beginning with a payment on December 31, 1987, and ending with a payment on December 31, 1991. In addition, the contract calls for a payment of interest of $3,457.45 on December 31, 1986, for the period from May 31, 1986, to December 31, 1986. Assume the contract does not provide for adequate stated interest and that the imputed rate of interest is 9.20 percent, compounded annually. Since the compounding period for the imputed rate is one year, there is a short period from May 31, 1986, to December 31, 1986. Thus, the fraction (f) with respect to the short period is equal to 210 days/360 days. The present value of the stream of $23,739.64 payments is $87,264.60. The present value of the stated interest payment of $3,457.45 on December 31, 1986, is $3,284.43. Thus, the contract contains unstated interest of $9,450.97 ($100,000 (the sum of the deferred payments) minus $90,549.03 ($87,264.60 + $3,284.43)).

Example (6). The facts are the same as in example (5), except that the $3,457.45 payment of interest for the short period is made on May 31, 1986. The contract contains unstated interest of $9,277.95 (the excess of $100,000 (the sum of the deferred payments) over $90,722.05 (the sum of the present value of the stream of $23,739.64 payments ($87,264.60) and the amount of the stated interest payment of $3,457.45 on May 31, 1986)).

§ 1.483–4 Test and imputed rates of interest applicable to a contract.

(a) *General rule.* Except as provided in paragraph (b) of this section, the test rate and imputed rate of interest for purposes of section 483 shall each be the lower of—

(1) The applicable Federal rate (based on the appropriate compounding period), or

(2) Nine percent, compounded semiannually, or an equivalent rate based on an appropriate compounding period.

The rates equivalent to 9 percent, compounded semiannually, for annual, quarterly and monthly compounding periods are as follows:

Appropriate compounding period	Test and imputed rate (percent)
Annual	9.20
Quarterly	8.90
Monthly	8.84

For rules relating to the determination of the applicable Federal rate, see paragraph (d) of this section. For rules relating to the appropriate compounding period on which the test and imputed rates of interest are to be based, see paragraph (c) of this section.

(b) *Special rates of interest applicable to certain sales*—(i) *Higher rates in certain cases*—(1) *Sales of new section 38 property after June 30, 1985.* In the case of a sale or exchange of new section 38 property (within the meaning of section 48(b) and the regulations thereunder), occurring after June 30, 1985, the test and imputed interest rates shall be equal to 100 percent of the applicable Federal rate.

(ii) *Sale-leaseback transactions occurring after June 30, 1985.* In the case of a debt instrument given in consideration for the sale or exchange of property occurring after June 30, 1985, all or a portion of which, pursuant to a plan, is leased by the transferor of the property or a person related to the transferor (within the meaning of section 168(e)(4)(D)) after the sale or exchange, the test and imputed interest rates shall be equal to 110 percent of the applicable Federal rate.

(iii) *Certain sales of principal residences.* This paragraph (b)(1)(iii) applies to a sale or exchange by an individual of the individual's principal residence (within the meaning of section 1034) if the stated principal amount of the debt instrument given in consideration for the sale or exchange exceeds the qualified amount. For this purpose, the qualified amount is the amount described in § 1.1274A–1(b)(2) in the case of a sale or exchange occurring after June 30, 1985, and $2,000,000 in the case of a sale or exchange occurring before July 1, 1985. In the case of a sale or exchange to which this paragraph (b)(1)(iii) applies, the test and imputed rates of interest shall be equal to—

(A) The applicable Federal rate for sales or exchanges occurring after June 30, 1985; and

(B) The rates determined under §§ 1.1274–3(e)(2)(i)(A)(*2*) and 1.1274–4(b)(2)(i)(B) for sales or exchanges occurring before July 1, 1985.

(iv) *Sales and exchanges occurring before July 1, 1985.* Except as otherwise provided in this paragraph (b), the imputed rate of interest in the case of a sale or exchange occurring before July 1, 1985, shall be 10 percent, compounded semiannually, or an equivalent rate based on an appropriate compounding period. The rates equivalent to 10 percent, compounded semiannually, for annual, quarterly and monthly compounding periods are as follows:

Appropriate compounding period	Imputed rate (percent)
Annual	10.25
Quarterly	9.88
Monthly	9.80

In the case of a sale or exchange of new section 38 property (within the meaning of section 48(b) and the regulations thereunder) occurring before July 1, 1985, the test rate shall be 110 percent of the applicable Federal rate and the imputed interest rate shall be 120 percent of the applicable Federal rate.

(2) *Lower rate for certain sales of land between related parties*—(i) *In general.* This paragraph (b)(2) applies to a debt instrument issued in a sale or exchange of land by an individual to a member of such individual's family (a qualified sale) if—

(A) Such individuals are the only parties to the debt instrument;

(B) The debt instrument is not given in consideration for any property other than land; and

(C) The stated principal amount of the debt instrument, when added to the aggregate stated principal amount of any other debt instruments to which this paragraph (b)(2) applies that were issued in prior qualified sales between such individuals during the same calendar year, does not exceed $500,000.

The rules of section 1274 and the regulations thereunder do not apply to any debt instrument to which this paragraph (b)(2) applies. Such rules apply, however, to any other debt instrument given in consideration for a qualified sale, unless section 1274 is otherwise inapplicable.

(ii) *Rate applicable to qualified sales.* In the case of a debt instrument to which this paragraph (b)(2) applies, the test and imputed rates of interest shall not exceed the semiannual rates prescribed by this paragraph (b)(2)(ii) or equivalent rates based on an appropriate compounding period. The semiannual rates prescribed by this paragraph (b)(2)(ii) and the equivalent rates for annual, quarterly and monthly compounding periods are as follows:

Appropriate compounding period	Test rate; imputed rate for sales or exchanges occurring after June 30, 1985 (percent)	Imputed rate for sales or exchanges occurring before July 1, 1985 (percent)
Annual	6.09	7.12
Semiannual	6.00	7.00
Quarterly	5.96	6.94
Monthly	5.93	6.90

(iii) *Special rules.* The following rules and definitions are applied in determining whether a sale or exchange is a qualified sale:

(A) *Land.* The term "land" does not include any structure (whether or not subject to depreciation or cost recovery allowances), or any permanent improvement or cultivation under, upon, or over real property if such improvement or cultivation is of a nature subject to cost recovery allowances, amortization or allowances for depreciation.

(B) *Definition of family members.* The members of an individual's family include only the individual's brother and sister (whether by the whole or half blood), spouse, ancestors, and lineal descendants. In determining any of these relationships full effect shall be given to a legal adoption. The term "ancestor" includes parents and grandparents, and "lineal descendants" includes children and grandchildren. The members of an individual's family are determined as of the date of the sale or exchange.

(C) *Nonresident aliens.* A sale or exchange is not a qualified sale if any party to the sale or exchange is a nonresident alien individual.

(iv) *Examples.* The provisions of this paragraph (b)(2) may be illustrated by the following examples:

Example (1). Assume that on January 1, 1987, A sells land to B, A's child, for $650,000. The contract for sale calls for B to make a $250,000 down payment and issue a debt instrument with a stated principal amount of $400,000. The sale is a qualified sale and this paragraph (b)(2) applies to the debt instrument.

Example (2). The facts are the same as in example (1), except that on June 1, 1987, A sells additional land to B under a contract that calls for B to issue a debt instrument with a stated principal amount of $100,000. The stated principal amount of this debt instrument ($100,000) when added to the stated principal amount of the prior debt instrument ($400,000) does not exceed $500,000. Thus, this paragraph (b)(2) applies to both debt instruments.

Example (3). The facts are the same as in example (1), except that on June 1, 1987, A sells additional land to B under a contract that calls for B to issue a debt instrument with a stated principal amount of $150,000. Since the stated principal amount of this debt instrument when added to the stated principal amount of the prior debt instrument exceeds $500,000, this paragraph (b)(2) does not apply to the debt instrument issued in the sale of June 1, 1987. Section 1274, if otherwise applicable, applies to the $150,000 debt instrument.

(c) *Appropriate compounding period; conversion of test and imputed rates of interest to an appropriate compounding period.* The test and imputed rates of interest must be based on an appropriate compounding period. The appropriate compounding period for the test rate is determined in accordance with the rules of § 1.1274–3(e)(3), and the appropriate compounding period for the imputed rate of interest is determined in accordance with the rules of § 1.1274–4(c). Test and imputed rates of interest based on the appropriate compounding period shall be determined in accordance with the rules of § 1.1274–3(e)(4) if such rates are not otherwise provided or if rates accurate to more than two decimal places are desired by both parties to the transaction.

(d) *Determination of applicable Federal rate.* For purposes of determining the test and imputed rates of interest, the applicable Federal rate with respect to a contract is the rate that would be determined under § 1.1274–6 if the contract were a debt instrument subject to section 1274.

(e) *Treatment of certain options.* Whether an option described in § 1.1272-1(f)(4) (ii) or (v) (relating to certain put and call options and options to extend) is presumed exercised for purposes of section 483 shall be determined in a manner consistent with the rules of § 1.1274-6(f) (relating to treatment of certain options). Thus, for example, the holder of a debt instrument shall be presumed to exercise a put option or an option to extend for all purposes of section 483 if the amount described in § 1.483-2(c)(2)(i), assuming exercise of the option, exceeds the amount described in § 1.483-2(c)(2)(i), assuming nonexercise of the option.

§ 1.483-5 Contingent payments.

(a) *In general.* This section provides rules for applying section 483 to any contract for the sale or exchange of property (the overall contract) that provides for any contingent payment. This section does not provide guidance concerning whether a contract is properly treated as debt or equity, or whether a contract evidences a valid indebtedness for Federal tax purposes, and no inference may be drawn with respect to these issues from anything in this section.

(b) *General rules*—(1) *Separation of noncontingent and contingent payments.* Except as otherwise provided in section 483 and the regulations thereunder, the noncontingent payments under an overall contract described in paragraph (a) of this section must be separated from the contingent payments under the contract. In such cases, noncontingent payments are subject to the rules of paragraph (b)(2) of this section, and contingent payments are subject to the rules of paragraph (b)(3) of this section. In addition, see paragraph (b)(4) of this section for special rules applicable to an overall contract that provides for certain contingent payments within a fixed period.

(2) *Noncontingent payments treated as separate contract.* The noncontingent payments under an overall contract to which paragraph (b)(1) of this section applies shall be treated for purposes of section 483 as if they were made under a separate contract. The amount of unstated interest with respect to such separate contract shall be determined solely by reference to the noncontingent payments of principal and interest.

(3) *Recharacterization of certain contingent payments*—(i) *In general.* Except as otherwise provided in paragraph (b)(4) of this section, a contingent payment to which this paragraph (b)(3)(i) applies, whether denominated as principal, interest, or both, shall be treated as consisting of—

(A) A payment of principal in an amount equal to the present value of the payment determined by discounting the payment at the test rate of interest applicable to the payment from the date the payment becomes due to the date of the sale or exchange, and

(B) A payment of interest in an amount equal to the excess of the total amount of the payment over the amount treated as principal.

For purposes of this paragraph (b)(3)(i), the present value of a payment is determined in accordance with the rules of § 1.483-3(b) except that the payment is discounted at the test rate of interest applicable to the payment. The test rate of interest applicable to a payment is the text rate of interest applicable to the overall contract under which the payment is made as determined under § 1.483-4. If, however, the test rate of interest applicable to the overall contract is determined by reference to the applicable Federal rate, the test rate of interest applicable to the payment shall be determined by reference to the appropriate Federal rate (for example, the Federal mid-term rate) for the period from the date of the sale or exchange to the date the payment is made.

(ii) *Payments to which paragraph (b)(3)(i) of this section applies.* Paragraph (b)(3)(i) of this section shall apply to—

(A) Any contingent payment of principal for which the contract does not provide adequate stated interest, or

(B) Any contingent payment of interest (other than adequate stated interest provided with respect to a contingent payment of principal) that is made under an overall contract that does not provide for adequate stated interest within the meaning of § 1.483-2 (that is, the contract contains unstated interest within the meaning of § 1.483-3) or that is provided with respect to a contingent payment of principal.

For purposes of this paragraph (b)(3)(ii), adequate stated interest with respect to a contingent payment of principal shall be determined in accordance with § 1.483-2 as if the contingent payment were the only payment of principal due under a contract. Thus, a contract provides for adequate stated interest with respect to a contingent payment of principal if the stated rate of interest is no lower than the test rate of interest applicable to the payment and interest at the stated rate is paid for the period from the date of the sale or exchange to the date the payment is due.

(iii) *Limitation on the characterization of amounts as principal.* If an overall contract calls for a fixed or stated maximum amount of principal, then notwithstanding paragraph (b)(3) (i) and (ii) of this section, the total amount of payments treated as principal (including amounts treatd as principal under this paragraph (b)) shall not exceed the fixed or stated maximum amount of principal.

(iv) *Taxable year of inclusion, deduction, and adjustment to basis.* For rules relating to the method of accounting for the portion of a contingent payment characterized as interest under this paragraph (b)(3), see § 1.446-2(f)(2)(i). In addition, the adjusted basis of the property sold or exchanged shall be increased on the date the payment becomes fixed by the portion of a contingent payment treated as principal.

(4) *Certain contingent payments within a fixed period.* If an overall contract described in paragraph (a) of this section provides for contingent payments described in § 1.1275-4(d) (relating to certain contingent payments within a fixed period), the buyer's basis in the property, and the amount of and the accrual of interest (including unstated interest) attributable to such payments shall be determined in a manner consistent with § 1.1275-4(d). For rules relating to the allocation of such interest to payments, see § 1.446-2(d).

(c) *Definition of contingent payment.* In determining whether a payment called for under a contract is contingent, remote and incidental contingencies may be disregarded by the Commissioner. The parties to a transaction, however, are bound by its form. Thus, neither party may treat any amount under a debt instrument whose payment is subject to a stated contingency as noncontingent. A payment shall not be considered contingent merely because the amount of or the liability for the payment may be impaired by insolvency or default. Variable payments of interest, if made under a contract to which § 1.483-2(d)(1) applies, shall not be treated as contingent, and if made under a contract to which § 1.483-2(d)(1) does not apply, shall be treated as contingent to the extent provided in § 1.483-2(d)(4). In addition, payments of fixed or minimum principal contingent as to due date that call for fixed or (in the case of a contract to which § 1.483-2(d)(1) applies) variable interest at a rate that constitutes adequate stated interest shall not be treated as contingent. Any payment of principal in excess of the minimum amount of principal shall be treated as contingent and, if not accompanied by adequate stated interest or if described in § 1.1275–4(d), shall be subject to the rules of paragraph (b) (3) or (4) of this section.

(d) *Examples.* The provisions of this section may be illustrated by the following examples:

Example (1). (i) On March 1, 1986, A sells rental personal property to B for $100,000. The contract for sale calls for B to make a $20,000 down payment and a single payment of $100,000 due on March 1, 1991. In addition, the contract calls for annual payments, beginning with a payment on March 1, 1987, of noncontingent interest at a rate of 6 percent, compounded annually, and contingent interest equal to a specified percentage of the gross rents from the property for the calendar year preceding the payment.

(ii) Assume that the test rate of interest for this contract is 9.20 percent, compounded annually. Thus, the special rule of § 1.483–2(e) does not apply and the contract does not provide for adequate stated interest. At a test rate of interest of 9.20 percent, compounded annually, the contract contains unstated interest of $12,382.56 (the excess of $100,000 (deferred payments) over $87,617.44 (the sum of the present values of the deferred payments and the noncontingent interest payments)). Thus, B's initial basis in the property is $107,617.44 ($87,617.44 plus the $20,000 down payment).

(iii) Assume that a contingent payment of interest of $3,000 becomes due on March 1, 1987. Since the payment of interest is being made under a contract that does not provide for adequate stated interest (and is not adequate stated interest with respect to a contingent payment of principal), it is subject to recharacterization. Because the test rate was not based on the applicable Federal rate, all payments must be recharacterized based on a discount rate of 9.20 percent, compounded annually. The payment is recharacterized as principal in the amount of $2,747.25 (the present value of the payment) and as interest in the amount of $252.75 (the excess of the payment ($3,000) over the amount of the payment treated as principal ($2,747.25)). On the date the payment becomes fixed, B increases the basis of the property by $2,747.25, the amount of the payment recharacterized as principal.

(iv) Assume that contingent payments of interest for years 1988, 1989, 1990 and 1991 and the amounts recharacterized as interest or principal are as follows:

Year	Payment	Principal	Interest
1988	$2,500	$2,096.50	$403.50
1989	3,200	2,457.44	742.56
1990	3,200	2,250.40	949.60
1991	4,[illegible]	2,704.81	1,495.19

B will increase the basis of the property over the remaining 4 years by an additional $9,509.15.

Example (2). The facts are the same as in example (1), except that the amount of the final contingent payment of interest is $5,000. If subject to unlimited recharacterization, the $5,000 payment would be treated as principal in the amount of $3,220.01 and as interest in the amount of $1,779.99. If the payment is treated as a $3,220.01 payment of principal (when taken together with all other contingent and noncontingent payments treated as principal), principal payments due under the contract would exceed the fixed stated principal amount due under the contract of $100,000. Thus, the amount of the payment treated as principal is limited to $2,830.97 (the excess of the stated principal amount ($100,000) over the sum of noncontingent payment of principal ($87,617.44) and the prior contingent payments treated as principal ($9,551.59)), and the amount of the payment treated as interest is $2,169.03 (the excess of the payment ($5,000) over the amount of the payment treated as principal ($2,830.97)).

Example (3). (i) On March 1, 1986, A sells rental personal property to B under a contract that calls for a $30,000 down payment, and six annual payments equal to 10 percent of the gross rents from the property. The contract further specifies that the maximum of payments under the contract (exclusive of the down payment) cannot exceed $200,000. The contract does not call for the contingent payments to bear any interest. Since it is not certain that any payment other than the $30,000 down payment will be made, B's basis in the property is initially limited to $30,000.

(ii) Since the contract does not provide for adequate stated interest with respect to the contingent payments, each payment is subject to recharacterization. The test rate of interest applicable to the payments is 9.20 percent, compounded annually. Assume that the contingent payments for the years 1987 through 1992 are set forth in column (1) of the following table. The characterization of principal and interest for each payment is set forth in columns (2) and (3) of the table.

Year	Payment (1)	Principal (2)	Interest (3)
1987	$37,000	$33,882.78	$3,117.22
1988	42,000	35,221.19	6,778.81
1989	33,000	25,342.30	7,657.70
1990	29,000	20,394.24	8,605.76
1991	39,000	25,116.05	13,883.95
1992	20,000	11,794.90	8,205.10

§ 1.582–1 [Amended]

Par. 14. In §1.582–1, paragraphs (d) and (e)(3)(i) are amended by removing the phrase "section 1232" from each place that it appears and adding in its place the phrase "sections 1271 through 1275".

§ 1.636–1 [Amended]

Par. 15. In §1.636–1, paragraph (a)(1)(ii) is amended by removing the phrase "section 1232" and adding in its place the phrase "section 1271".

§ 1.818–3 [Amended]

Par. 16. In § 1.818–3, paragraph (f) is amended by removing the phrase "section 1232(a) (relating to the taxation of bonds and other evidences of indebtedness)" and adding in its place the phrase "section 1271 (relating to the treatment of amounts received on retirement or sale or exchange of debt instruments)", and by removing the phrase "section 1232(a)(2)(C)" and adding in its place the phrase "section 1271(d)".

§ 1.861–2 [Amended]

Par. 17. In § 1.861–2, paragraph (a)(4) is amended by removing the phrase "section 1232(b)(1)" and adding in its place the phrase "section 1273(a)(1)".

§ 1.993–1 [Amended]

Par. 18. In § 1.993–1, paragraph (g) is amended by removing the phrase "section 1232" and adding in its place the phrase "section 1272".

§ 1.1001–1 [Amended]

Par. 19. In § 1.1001–1, paragraph (g) is amended by removing the phrase "section 1232(b)" and adding in its place the phrase "section 1273", and by removing the phrase "paragraph (b)(2)(iii)(b) of § 1.1232–3." and adding in its place the phrase "§ 1.1273–2."

§ 1.1012–1 [Amended]

Par. 20. In § 1.1012–1, paragraph (f) is amended by removing the phrase "section 1232(b)" and adding in its place the phrase "section 1273" and by removing the phrase "paragraph (b)(2)(iii)(b) of § 1.1232–3." and adding in its place the phrase "§ 1.1273–2."

Par. 21. Section 1.1012–2 is revised to read as follows:

§ 1.1012–2 Certain sales or exchanges between related parties.

(a) *In general.* In the case of a sale or exchange of property in which the relationship between the seller and the buyer is such that the sale or exchange is not necessarily an arm's-length transaction, the transaction shall be examined to determine whether the value of the consideration provided by the buyer is greater than or less than the value of the property. If the value of the consideration exceeds the value of the property, this excess shall not be treated as relating to the sale or exchange and will be recharacterized according to the relationship between the parties. If the value of the property exceeds the value of the consideration, this excess generally shall be treated as transferred from the seller to the buyer based on the relationship between the parties and not as transferred in exchange for the debt instrument. The preceding sentence shall not apply to any transaction that would be characterized as in part a gift and in part a sale under § 1.170A–4(c)(2) and § 1.1011–2(b) or under § 1.1015–4.

(b) *Value.* In applying this section to any sale or exchange where all or a part of the consideration furnished by the buyer consists of one or more debt instruments issued by the buyer to the seller, then, for purposes of this section—

(1) The value of any such debt instrument to which section 1274 applies or which has adequate stated interest within the meaning of section 1274(c)(2) or § 1.483–2 shall be its issue price;

(2) The value of any such debt instrument issued under a contract to which section 483 applies shall be the amount described in § 1.483–3(a)(2)(i); and

(3) In determining whether the value of the consideration furnished by the buyer exceeds the value of the property, the value of the property shall be determined by reference to the price that an unrelated buyer (having the same creditworthiness as the actual buyer) would be willing to pay for the property in an arm's-length transaction if seller financing (taken into account at its issue price) were offered on the same terms as those offered to the actual buyer.

(c) *Examples.* The provisions of this section may be illustrated by the following examples:

Example (1). (i) On January 1, 1986, Corporation X sells nonpublicly traded property to A, the sole shareholder of X. In consideration for the sale, A makes a down payment of $200,000 and issues a debt instrument calling for a single payment of $1,000,000 due in five years. No interest is provided for in the debt instrument. Because A is the sole shareholder of X, the transaction must be examined to determine whether the value of the property exceeds the value of the consideration furnished by A. For this purpose, the value of the property is its fair market value (determined without regard to any seller financing).

(ii) Assume that the fair market value of the property is $900,000 and that the issue price of the debt instrument under § 1.1274–4 is $643,928. Thus, the value of the consideration furnished by A is $843,928 (the sum of $200,000 (the portion of the consideration attributable to the down payment) and $643,928 (the portion of the consideration attributable to the debt instrument)). Since the value of the property ($900,000) exceeds the valve of the consideration ($843,928), X Corporation is treated as having made a distribution to shareholder A to which section 301 applies. The amount of the distribution is $56,072 (the difference between $900,000 and $843,928). The basis of the property in the hands of A is $900,000 ($843,928 (consideration actually furnished by A) increased by $56,072 (the amount of the section 301 distribution)).

Example (2). The facts are the same as in Example (1) except that the fair market value of the property is $800,000. X is not treated as having made a section 301 distribution to A and A's basis in the property is $800,000. The transaction need not be examined for excessive consideration since a sale from a corporation to a shareholder ordinarily would not be used to disguise a contribution to capital from the shareholder to the corporation.

Example (3). (i) C sells nonpublicly traded property to his employer D for $300,000 in cash and D's debt instrument having a face amount of $1,000,000, payable in 5 years with interest payable semiannually at a rate of 9 percent. Because D is C's employer, the transaction must be examined to determine if a portion of the amount designated as consideration for the property is in fact disguised compensation.

(ii) Assume that the fair market value of the property (assuming no seller financing), is $1,000,000 and that the issue price of D's debt instrument is $1,000,000. Assume further that a buyer unrelated to D and having the same creditworthiness as C would be willing to pay $1,200,000 for the property if allowed to pay $300,000 in cash and $900,000 in the form of a 5-year debt instrument calling for semiannual payments of interest at a rate of 9 percent. The value of the consideration furnished by D is $1,300,000 (cash of $300,000 plus a debt instrument having an issue price of $1,000,000). Since this amount exceeds the value of the property by $100,000, only $200,000 of the $300,000 transferred from D to C is treated as consideration furnished for the property. The remaining $100,000 is treated as compensation. D's basis in the property is $1,200,000 (cash consideration of $200,000 plus a debt instrument with an issue price of $1,000,000).

Example (4). The facts are the same as in Example (3) except that the property could be sold to the unrelated buyer for $1,400,000 (assuming a down payment of $300,000 and 5-year seller financing at 9 percent for the balance of the purchase price). Because the value of the consideration furnished by D ($1,300,000) does not exceed the value of the property ($1,400,000), D is not treated as having paid compensation to C. D's basis in the property is $1,300,000. The transaction need not be examined for insufficient consideration since employees ordinarily do not make bargain sales to their employers.

Par. 22. In § 1.1016–5, paragraph (s) is revised to read as follows:

§ 1.1016–5 Miscellaneous adjustments to basis.

* * * * *

(s) *Original issue discount.* In the case of certain debt instruments issued at a discount after May 27, 1969, the basis shall be increased under section 1272(d)(2) by the amount of original issue discount included in the holder's gross income pursuant to section 1272.

* * * * *

§ 1.1037–1 [Amended]

Par. 23. Section 1.1037–1 is amended as follows:

1. In paragraph (a) by removing the phrase "the first sentence of section 1232(a)(2)(B)." and adding in its place "section 1271(c)(2)(A)", by removing the phrase "section 1232(b)(2)" each place that it appears in *Example* (6) and *Example* (7) and adding in its place the phrase "section 1273(b)(1)", by removing the phrase "section 1232(a)(2)(B)" each place it appears in *Example* (7) and adding in its place the phrase "section 1271(c)(2)(A)", and by removing the phrase "section 1232(a)(2)(B)(ii)" each place it appears in *Example* (6) and *Example* (7) and adding in its place the phrase "section 1271(c)(2)(A)(ii)".

2. In paragraph (b) by removing the phrase "section 1232" from the heading and adding in its place the phrase "section 1271", by removing the phrase "section 1232(a)(2)(B)" each place that it appears and adding in its place the phrase "section 1271(c)(2)(A)", and by removing the phrase "section 1232" from the heading of paragraph (b)(6) and adding in its place the phrase "section 1271".

§ 1.1232–1 [Amended]

Par. 24. Section 1.1232–1 is amended as follows:

1. In paragraph (a) by revising the heading to read "Bonds and other evidences of indebtedness issued before July 2, 1982; scope of section"; by removing the first sentence and adding the following new sentence as the first sentence of the paragraph, and by removing the phrase "after May 27, 1969," from the fourth sentence and adding in its place the phrase "after May 27, 1969, and before July 2, 1982,". The added sentence reads as follows: "Section 1232 as in effect before its repeal by section 42(a) of the Tax Reform Act of 1984 applies to any bond, debenture, note, or certificate of indebtedness (referred to in this section and §§ 1.1232–2 through 1.1232–4 as an obligation) (1) which is a capital asset in the hand of the taxpayer, and (2) which is issued by any corporation, or by any government or political subdivision thereof."

2. In paragraph (c)(3) by removing the phrase "December 31, 1975." from the heading and adding in its place the phrase "December 31, 1975, and before July 2, 1982"; and by adding the phrase "and before July 2, 1982" immediately after the first parenthetical in the first sentence thereof.

§ 1.1232–2 [Amended]

Par. 25. The heading of § 1.1232–2 is revised to read "Retirement of an obligation issued before July 2, 1982."

§ 1.1232–3 [Amended]

Par. 26. Section 1.1232–3 is amended as follows:

1. The heading is amended by adding the phrase "and before July 2, 1982." immediately following the phrase "December 31, 1954."

2. Paragraph (a) is amended by removing the phrase "after May 27, 1969" from the heading and from each place that it appears and adding in its place the phrase "after May 27, 1969, and before July 2, 1982".

3. Paragraph (f), the first sentence, is amended by removing the phrase "after December 31, 1954," and inserting the phrase "after December 31, 1954, and before August 17, 1984," in its place.

§ 1.1232-3A [Amended]

Par. 27. Section 1.1232-3A is amended as follows:

1. The heading and paragraph (a) are amended by removing the phrase "after May 27, 1969," and adding in its place the phrase "after May 27, 1969, and before July 2, 1982."

2. Paragraph (f) is amended by removing the phrase "after December 31, 1975" and by adding in its place the phrase "after December 31, 1975, and before July 2, 1982,".

Par. 28. Sections 1.1271-1 through 1.1275-5 are added in the appropriate place. The new sections read as follows:

§ 1.1271-1 Treatment of amounts received on retirement or sale or exchange of debt instruments.

(a) *Applicability.* Section 1271 and this section provide for the treatment of amounts received on retirement or sale or exchange of a debt instrument (as defined in section 1275(a) and § 1.1275-1(b)) issued after July 1, 1982, other than a debt instrument issued by a natural person as described in § 1.1275-1(g). Section 1271 and this section do not apply to a debt instrument acquired before July 18, 1984, which was not a capital asset in the hands of the holder on July 17, 1984. To determine whether a debt instrument was a capital asset in the hands of the holder, see § 1.1232-1(b). For rules relating to debt instruments issued before July 2, 1982, see § 1.1232-1.

(b) *General rules*—(1) *Retirement.* Amounts received on retirement of a debt instrument to which section 1271 applies are considered as received in exchange for the debt instrument.

(2) *Sale or exchange.* Gain realized upon the sale or exchange of a debt instrument to which section 1271 applies is either capital gain or ordinary income, depending on the character of the debt instrument in the hands of the holder. If the debt instrument is a capital asset in the hands of the holder, gain realized is capital gain unless—

(i) There was an intention to call the debt instrument before maturity, (in which case, all or a portion of the gain realized is treated as ordinary income under section 1271(a)(2)(A)); or

(ii) The debt instrument is a short-term obligation (as defined in section 1283(a)(1)) issued at a discount (in which case, all or a portion of the gain realized may be treated as ordinary income under § 1.1271-3).

(3) *Example.* The rules stated in paragraph (b) of this section may be illustrated as follows:

Example. On November 1, 1985, B, a calendar-year taxpayer, purchases at original issue for cash of $86,235.17, N Corporation's 15-year bond, maturing on October 31, 2000, at a stated redemption price of $100,000. Assume that the bond is a capital asset in B's hands. The bond provides for semiannual payments of interest at 10%. The bond has $13,764.83 of original issue discount (stated redemption price at maturity, $100,000, less issue price, $86,235.17). There is no intention to call the bond before maturity. On November 1, 1986, B sells the bond to C, a calendar-year taxpayer, for cash of $90,000. B has included $1,214.48 of original issue discount in gross income and has increased his basis by that amount to $87,449.65 (see § 1.1272-1(k), Example (4) for the computation of daily portion of original issue discount). B has realized a gain of $2,550.35 (amount realized, $90,000, less adjusted basis, $87,449.65). Since there was no intention to call the bond before maturity at the date of issue, under paragraph (b)(2)(i) of this section all of B's gain, $2,550.35, is capital gain.

(c) *Amounts previously includible in income.* Nothing in section 1271, this section, or §§ 1.1271-2 and 1.1271-3 shall require the inclusion of any amount previously includible in gross income. Thus, if an amount was previously includible in a taxpayer's income on account of a debt instrument issued at a discount and redeemable for fixed amounts increasing at stated intervals, or under section 811(b) (or corresponding provisions of prior law) relating to accrual of discount on bonds or other evidences of indebtedness held by life insurance companies, this amount is not again includible in the taxpayer's gross income. For example, amounts includible in income by a cash receipts and disbursements method taxpayer who has made an election under section 454 (a) or (c) (relating to accounting rules for certain debt instruments issued at a discount to which section 1272 does not apply) are not also includible in gross income upon sale or exchange of the obligation. In the case of a gain which under section 1271(a)(2) would include an amount considered to be ordinary income and a further amount considered to be long-term capital gain, any amount to which this paragraph applies is first used to offset the amount considered to be ordinary income to the extent such previously included income constituted ordinary income.

§ 1.1271-2 Intention to call before maturity [Reserved]

§ 1.1271-3 Gain on disposition of certain short-term obligations.

(a) *Short-term government obligations*—(1) *General rule.* Any gain realized on the sale or exchange of a short-term government obligation issued at a discount which does not exceed an amount equal to the ratable share of the acquisition discount (as defined in paragraph (a)(3) of this section) shall constitute ordinary interest income.

(2) *Short-term government obligation.* For purposes of this section, the term "short-term government obligation" is any obligation of the United States or any of its possessions, or of a State or any political subdivision thereof, or of the District of Columbia, which is payable at a fixed maturity date not more than 1 year from the issue date. This term does not include short-term tax-exempt obligations.

(3) *Ratable share of acquisition discount.* For purposes of this section, the term "ratable share of acquisition discount" means an amount which bears the same ratio to the total acquisition discount (as defined in section 1271(a)(3)(C)) as—

(i) The number of days which the taxpayer holds the obligation, bears to

(ii) The number of days after the date the taxpayer acquired the obligation and up to (and including) the date of maturity of the obligation.

(4) *Election of computation on constant interest rate basis.* In lieu of computing the ratable share of acquisition discount as described in paragraph (a)(3) of this section, the taxpayer may elect to compute acquisition discount with respect to a short-term government obligation (as defined in paragraph (a)(2) of this section) on the basis of daily compounding. The election shall be made by filing a return for the year of the sale or exchange by reporting the transaction on the basis of daily compounding. This election shall be irrevocable and shall be made on an obligation by obligation basis.

(b) *Short-Term nongovernmental obligations issued or or after July 18, 1984*—(1) *In general.* Gain realized on the sale or exchange of a short-term nongovernmental obligation (as defined in paragraph (b)(2) of this section) issued on or after July 18, 1984, which does not exceed an amount equal to the ratable share of original issue discount described in paragraph (b)(3) of this section shall be treated as ordinary interest income.

(2) *Short-term nongovernmental obligations.* For purposes of this section, the term "short-term nongovernmental obligation" means an obligation other than a short-term government obligation described in paragraph (a)(2) of this section, which has a fixed maturity date not more than 1 year from the issue date. This term does not include short-term tax-exempt obligations.

(3) *Ratable share of original issue discount.* For purposes of this section, the ratable share of original issue discount is an amount which bears the same ratio to the total original issue discount (as defined in section 1273(a)(1)) as—

(i) The number of days which the taxpayer holds the obligation, bears to

(ii) The number of days after the issue date and up to (and including) the date of maturity of the obligation.

(4) *Election of computation on constant interest rate basis.* In lieu of computing the ratable share of original issue discount as described in paragraph (b)(3) of this section, the taxpayer may elect to compute original issue discount with respect to a short-term nongovernmental obligation (as defined in paragraph (b)(2) of this section) on the basis of daily compounding. The election shall be made by filing a return for the year of the sale or exchange reporting the transaction on the basis of daily compounding. This election shall be irrevocable and shall be made on an obligation by obligation basis.

(c) *Examples.* The rules stated in paragraphs (a) and (b) of this section may be illustrated as follows:

Example (1). On January 1, 1985, A purchases at original issue for cash of $9,200 a one-year Treasury bill with a stated redemption price at maturity of $10,000. This obligation is a capital asset in A's hands. The Treasury bill is also a short-term government obligation within the meaning of paragraph (a)(2) of this section and has total acquisition discount of $800 (stated redemption price at maturity, $10,000, minus A's basis, $9,200). On August 1, 1985, A sells the bill to B for $9,700, and A realizes a gain of $500 (amount realized, $9,700 minus A's basis, $9,200). The amount of acquisition discount that has accrued on the bill for all days during the taxable year that A held the note is determined under paragraph (a)(3) of this section as follows:

(1) Total amount of acquisition discount	$800.00
(2) Multiplied by: The number of days A held the bill during the taxable year (210) divided by the total number of days after A acquired bill up to and including the date of maturity (360)	.58333
(3) A's ratable share of acquisition discount	$466.67

Since the amount shown on line (3), $466.67, is less than A's gain of $500, only $466.67 of his gain is includible as interest in gross income. The remaining portion, $33.33, is capital gain.

Example (2). (i) On March 1, 1985, A lends $5,000 to B, an individual, in exchange for B's note with an issue price of $5,000, payable in ten months and calling for interest payable at maturity. B's note is a short-term nongovernmental obligation within the meaning of paragraph (b)(2) of this section and is also a capital asset in A's hands. Interest is to accrue at a rate of 12%, compounded monthly, and totals $523.11 at maturity. The stated redemption price at maturity under § 1.1273–1(b)(1) is $5,523.11. The debt instrument has original issue discount of $523.11 (stated redemption price at maturity, $5,523.11, minus issue price, $5,000). On September 1, 1985, A sells the debt instrument to C for $5,325. A realizes a gain on the sale of $325 (amount realized, $5,325, minus A's basis in the debt instrument, $5,000). A's ratable share of original issue discount is computed as follows:

(1) Total original issue discount	$523.11
(2) Multiplied by: number of days A held the note (180) divided by the number of days after the date A acquired the debt instrument up to and including the date of maturity (300)	.60
(3) A's ratable share of original issue discount	$313.87

Since A's gain, $325, is greater than his ratable share of original issue discount, $313.87, only $313.87 of his gain is includable as interest in gross income. The remaining portion, $11.13, is capital gain.

(ii) The facts are the same as in part (i), except that A elects to compute his original issue discount based on daily compounding. A's share of original issue discount for the 180-day period computed on the basis of daily compounding is $307.60. Since A's gain, $325, is greater than his share of original issue discount, $307.60, only $307.60 of his gain is includable as interest in gross income. The remaining portion, $17.40, is capital gain.

(d) *Short-term nongovernmental obligations issued by a corporation after May 27, 1969, and before July 18, 1984*—(1) *In general.* Gain on the sale or exchange of a short-term nongovernmental obligation described in paragraph (b)(2) of this section issued by a corporation after May 27, 1969, and before July 18, 1984, shall be included in gross income as interest to the extent that the gain does not exceed an amount equal to the ratable monthly portion of original issue discount multiplied by the sum of the number of complete months and any fractional part of a month that the taxpayer held the debt instrument.

(2) *Cross-references.* For definition of the term "ratable monthly portion", see § 1.1232–3A(a)(2). For definition of the term "complete month" and the computation of a fractional part of a month, see § 1.1232–3A(a)(3).

§ 1.1272–1 Current inclusion in income of original issue discount on certain debt instruments issued after July 1, 1982.

(a) *Applicability*—(1) *In general.* Section 1272(a) and this section require a holder of a debt instrument (as defined in section 1275(a) and § 1.1275–1(b)) issued at a discount to include as interest in gross income on a constant interest rate basis the amount of original issue discount (as defined in section 1273(a) and § 1.1273–1(a)) on that debt instrument. Section 1272(a) and this section apply only to the holder of a debt instrument issued at a discount after July 1, 1982. See section 1272(b) and §§ 1.1232–1 through 1.1232–3A for rules relating to debt instruments issued at a discount before July 2, 1982.

(2) *Exceptions.* Section 1272 and this section do not apply to the following:

(i) A holder of a debt instrument issued at a discount where the holder had purchased the debt instrument at a premium (as defined in § 1.1275–1(f));

(ii) A holder that is a life insurance company to which section 811(b) or corresponding provisions of prior law apply;

(iii) A holder of a debt instrument issued at a discount before December 31, 1984, in whose hands the debt instrument is not a capital asset;

(iv) Tax-exempt obligations, as defined in section 1275(a)(3) and § 1.1275–1(d);

(v) United States savings bonds;

(vi) Short-term obligations (as defined in section 1283(b));

(vii) Any debt instrument issued by a natural person (as defined in § 1.1275–1(g)) before March 2, 1984; and

(viii) Any loan made by a natural person to another natural person after March 1, 1984, if (A) the loan is not made in the course of a trade or business of the lender, and (B) the amount of the loan (when increased by the outstanding amount of prior loans between the same parties) does not exceed $10,000. For purposes of this paragraph (a)(2)(viii), the term "loan" does not include a stripped bond or stripped coupon within the meaning of section 1286(e). The aggregate amount of loans between natural persons is the sum of the outstanding principal amounts of loans directly between the individuals regardless of the character of the loans, regardless of the interest rate charged on the loans, and regardless of the date on which the loans were made. This paragraph (a)(2)(viii) shall not apply if one of the principal purposes of the interest arrangements of the loan is the avoidance of any Federal tax by either the borrower or the lender. The determination of whether tax avoidance is one of the principal purposes of the loan shall be made by the Commissioner. For purposes of applying the $10,000 limitation of this paragraph (a)(2)(viii), a husband and wife shall be treated as one person with respect to loans made by either husband or wife to a third person or a spouse of that person. The preceding sentence shall not apply to loans made between a husband and wife, nor to loans where the spouses lived apart at all times during the taxable year in which the loan was made.

(3) *Amounts otherwise includible or deductible.* Nothing in section 1272 or this section shall require the double inclusion or permit the double deduction of any amount from gross income. Thus, for example, payments (or portions of payments) denominated as interest under the debt instrument which are included in the stated redemption price at maturity under § 1.1273–1(b)(2)(ii) because they are not qualified periodic interest payments (as defined in § 1.1273–1(b)(1)(ii)) are not also includible under section 61. See also the rules described in § 1.1271–1(c).

(4) *Cross-references.* See § 1.1275–4 for rules relating to the treatment of debt instruments providing for contingent payments. See § 1.1275–5 for rules relating to debt instruments providing for a variable rate of interest.

(b) *Original issue discount included in income on basis of constant interest rate.* The holder of a debt instrument having original issue discount to which this section applies shall include as interest in gross income an amount equal to the sum of the daily portions of the original issue discount for each day during the taxable year that the holder holds the debt instrument. For this purpose, a person holds a debt instrument on the date of its purchase but not on the date of its disposition. The amount included under this section shall be reduced in the case of a holder who pays an acquisition premium for the debt instrument (as described in paragraph (g) of this section).

(c) *Determination of daily portion*—(1) *In general.* The daily portion of original issue discount on a debt instrument is an amount equal to the total original issue discount allocable to the accrual period (as defined in paragraph (d) of this section) divided by the number of days in the accrual period. See § 1.1275–2(e) for rules relating to counting conventions.

(2) *Amount allocable to an accrual period*—(i) *In general.* The amount of original issue discount allocable to an accrual period (other than a short first accrual period described in paragraph (c)(2)(ii) of this section or a final accrual period described in paragraph (c)(2)(iii) of this section) is—

(A) The product of—

(*1*) The adjusted issue price of the debt instrument (as defined in paragraph (e) of this section) at the beginning of the accrual period, and

(*2*) The yield to maturity of the debt instrument (as defined in paragraph (f) of this section), divided by the number of accrual periods in a year;

(B) Reduced (but not below zero) by the sum of amounts payable as qualified periodic interest (as defined in § 1.1273–1(b)(1)(ii)) on the debt instrument during the accrual period.

(ii) *Special rule for short first accrual periods*—(A) *In general.* If the first accrual period is shorter than a full accrual period, the amount of original issue discount allocable to the first accrual period may be determined by either of the two alternative methods prescribed by this paragraph (c)(2)(ii) or by any other reasonable method. The methods prescribed by this paragraph (c)(2)(ii) are the exact method and the approximate method. As an example of a reasonable method other than the exact or approximate method, a taxpayer may determine the amount of original issue discount allocable to the first accrual period by compounding at monthly intervals with simple interest within a month. The choice of any method permissible under this paragraph (c)(2)(ii) requires a corresponding choice for purposes of calculating yield to maturity described in paragraph (f) of this section. The choice of method shall be reported to the Internal Revenue Service in the time and manner provided in §§ 1.1275–3(a)(1) and 1.1275–3(b)(4). If the taxpayer does not allocate original issue discount to a short first accrual period based on a reasonable method, such discount shall be reallocated based on the exact method.

(B) *Exact method.* Under the exact method, the amount of original issue discount allocable to the first accrual period shall be the product of—

(*1*) The issue price of the debt instrument (as defined in section 1273(b) and § 1.1273–2), and

(*2*) The formula:

$[1+i/k^{f}+1]$

In which: i = The yield to maturity, expressed as a decimal;

k-The number of accrual periods in a year (for example, 12, if the accrual period is one month); and

f + A-fraction whose numerator is the number of days in the short first accrual period, and whose denominator is the number of days in a full accrual period;

reduced (but not below zero) by the sum of amounts payable as qualified periodic interest on the debt instrument during the accrual period.

(C) *Approximate method.* Under the approximate method, the amount of original issue discount allocable to the first accrual period is determined as described in paragraph (c)(2)(i) of this section, except that the yield to maturity described in paragraph (c)(2)(i)(B)(2) shall be multiplied by the fraction f as defined in paragraph (c)(2)(ii)(B)(2).

(iii) *Special rule for final accrual period.* The amount of original issue discount allocable to the final accrual period (including a short final accrual period) shall be the excess of the stated redemption price at maturity (as defined in section 1273(a)(2) and § 1.1273–1(b)) over the adjusted issue price at the beginning of the final accrual period. This paragraph (c)(2)(iii) shall not apply to any debt instrument that is an installment obligation (as defined in § 1.1273–1(b)(2)(i)).

(d) *Accrual period*—(1) *Debt instruments issued after December 31, 1984*—(i) *Regular payment or compounding at intervals of one year or less.* If a debt instrument issued after December 31, 1984, calls for more than one payment or compounding date (other than the issue date) and all dates on which an amount is either paid or compounded occur at regular intervals of one year or less, then the accrual period is this interval. A debt instrument shall not fail to qualify for this rule merely because the interval between the issue date and the first payment or compounding date after the issue date or the interval between the maturity date and the preceding payment or compounding date differs from the interval between other payment or compounding dates.

(ii) *Irregular payment or compounding; intervals of more than one year.* if a debt instrument issued after December 31, 1984, calls for more than one payment or compounding date (other than the issue date) and all dates on which an amount is either paid or compounded do not occur at regular intervals of one year or less, the accrual period is the longest period of not more than one year such that all intervals consist of a whole number of accrual periods. For purposes of this paragraph (d)(1)(ii), the interval between the issue date and the first payment or compounding date after the issue date and the interval between the maturity date and the preceding payment or compounding date are not taken into account unless the debt instrument calls for only one payment or compounding date between the issue date and the maturity date.

(iii) *Debt instruments calling for a single payment.* In the case of a debt instrument issued after December 31, 1984, that provides for a single payment at maturity and for no other payment or compounding dates (other than the issue date), the accrual periods are the six-month periods (or the shorter period from the issue date) that end on the day in the calendar year that corresponds either to the stated maturity date of the debt instrument or to the date that is six months before the stated maturity date.

(iv) *Short accrual period.* (A) If the interval between the issue date of a debt instrument for which the accrual period is determined under paragraph (d)(1) (i) or (ii) of this section and the first payment or compounding date does not consist of a whole number of accrual periods, then the first accrual period shall be the short period such that the remainder, if any, of such interval consists of a whole number of accrual periods.

(B) If the interval between the last date before maturity on which an amount is paid or compounded and the maturity date of the debt instrument for which the accrual period is determined under paragraph (d)(1) (i) or (ii) of this section does not consist of a whole number of accrual periods, then the final accrual period shall be the short period such that the remainder, if any, of such interval consists of a whole number of accrual periods.

(v) *Date accrual period begins.* The first accrual period begins on the issue date (as defined in section 1275(a)(2) and § 1.1275–1(c)). Each subsequent accrual period begins on the day following the last day of the preceding accrual period. The final accrual period ends on the stated maturity date.

(vi) *Examples.* The provisions of paragraph (d)(1) of this section may be illustrated as follows:

Example (1). A bond is issued on November 1, 1985, for cash of $85,000, and matures on October 31, 2000, at a stated redemption price of $100,000. The bond provides for quarterly payments of interest at an annual rate of 10%. Under paragraph (d)(1)(i) of this section, the accrual period is the three-month period ending on October 31, July 31, April 30, and January 31 of each calendar year.

Example (2). A debt instrument is issued for $100,000 cash on November 1, 1985, and matures on December 31, 2005. Interest is compounded semiannually from December 31, 1985, but the debt instrument provides for no interest payments during the first five years. Semiannual interest payments are made thereafter at a rate of 13%, compounded semiannually. The interest payments are due on June 30 and December 31 of each calendar year beginning in 1991. Under paragraph (d)(1)(i) of this section, the accrual period is six months. The accrual periods end on June 30 and December 31 of each calendar year. The period from November 1, 1985, to December 31, 1985, is a short accrual period.

Example (3). The facts are the same as in example (2), except that the debt instrument calls for quarterly interest payments on March 31, June 30, September 30, and December 31 of each year during the first five years and semiannual payments on June 30 and December 31 of each succeeding year. Under paragraph (d)(1)(ii) of this section, the longest period such that all intervals between successive payments consist of a whole number of accrual periods is a calendar quarter. The accrual period is therefore the calendar quarter ending on December 31, September 30, June 30, and March 31 of each year.

Example (4). A bond is issued for $75,000, on October 17, 1985, and matures on September 30, 2015, at a stated redemption price of $90,000 with no payments or compounding of interest until maturity. Under paragraph (d)(1)(iii) of this section, the accrual period is six months. The accrual periods end on September 30 and March 31 of each calendar year. The period from October 17, 1985, to March 31, 1986, is a short accrual period.

(2) *Debt instruments issued after July 1, 1982, and before January 1, 1985.* In the case of debt instruments issued at a discount after July 1, 1982 and before January 1, 1985, an accrual period is the one-year period beginning on the day in the calendar year which corresponds to the date of original issue of the debt instrument. The final accrual period ends on the stated maturity date and may constitute a short accrual period.

(e) *Adjusted issue price*—(1) *First accrual period.* The adjusted issue price of a debt instrument at the beginning of the first accrual period is its issue price.

(2) *Subsequent accrual periods*—(i) *In general.* Except as provided in § 1.1275–4(d), the adjusted issue price of the debt instrument at the beginning of each accrual period subsequent to the first accrual period is equal to the adjusted issue price of the debt instrument as of the beginning of the immediately preceding accrual period increased by the amount of original issue discount allocable to that accrual period as determined under paragraph (c)(2) of this section.

(ii) *Special rule for installment obligations.* In the case of a debt instrument that is an installment obligation (as defined in § 1.1273–1(b)(2)(i)), the adjusted issue price of the debt instrument at the beginning of an accrual period subsequent to the first accrual period is the adjusted issue price at the beginning of the immediately preceding accrual period plus the amount of original issue discount allocable to that accrual period determined under paragraph (c)(2) of this section, reduced by the amount of any payment other than a payment of qualified periodic interest (as defined in § 1.1273–1(b)(1)(ii)) made at the end of or during that accrual period. Each payment other than a payment of qualified periodic interest shall be treated first as a payment of original issue discount to the extent accrued as of the date of the payment and not allocated to prior payments, and second as a payment of principal (and no portion thereof shall be treated as prepaid interest).

(f) *Yield to maturity*—(1) *In general.* The term "yield to maturity" (hereinafter "yield") means that interest rate that when used in computing the present value of all payments of principal and interest to be paid in connection with a debt instrument produces an amount equal to the issue price. For purposes of this section, yield shall be determined on the basis of compounding at the end of each accrual period and shall be expressed as an annual interest rate. Yield is determined on the issue date of the debt instrument, and, except in the case of a variable rate debt instrument described in § 1.1275–5, remains constant over the term of the debt instrument. Yield, when expressed as a percentage, shall be calculated to at least two decimal places.

(2) *Short first accrual periods.* In the case of a debt instrument containing a short first accrual period, the taxpayer shall determine yield in a manner consistent with the method chosen for allocating the amount of original issue discount with respect to the short period under section 1272(a)(3) and paragraph (c)(2)(ii) of this section.

(3) *Special rules*—(i) *Application to debt instruments subject to section 1274.* In the case of a debt instrument to which section 1274 applies (other than a debt instrument issued in a potentially abusive situation within the meaning of section 1274(b)(3)(B) and § 1.1274–4(g)) that does not have adequate stated interest (within the meaning of section 1274(c)(2) and § 1.1274–3), the yield is the imputed interest rate (as defined in section 1274(b)(2)(B) and § 1.1274–4(b)).

For example, if the imputed interest rate applied to determine the issue price of a debt instrument under section 1274 is 12%, compounded semiannually, that interest rate also represents the yield of the debt instrument. In a potentially abusive situation, yield shall be determined under paragraph (f)(1) of this section. See § 1.1274-4(h), Example (1).

(ii) *Certain debt instruments with fixed interest rate.* The yield of a debt instrument that has an issue price equal to its stated principal amount, including a debt instrument that has an indefinite maturity (for example, a loan payable on demand), and that calls for a fixed rate of interest over the entire term of the debt instrument compounded at periodic intervals of one year or less, shall be the stated interest rate. For example, if A lends B $100,000, repayable on demand or at a time that is not ascertainable on the issue date, with interest at 12%, compounded semiannually, all interest to be added to principal and payable at maturity, the yield of this loan is 12%, compounded semiannually. See paragraph (k), Example (14) of this section for an illustration of this rule.

(iii) *Debt instrument providing for contingent payments.* The yield of a debt instrument that provides for contingent payments (as described in § 1.1275-4(b)) generally shall be determined for purposes of section 1272 by reference to only the noncontingent payments under the debt instrument. See § 1.1275-4 for rules relating to the treatment of debt instruments providing for contingent payments.

(iv) *Variable rate debt instruments.* The yield of a debt instrument calling for a variable rate of interest based on an objective interest index (as defined in § 1.1275-5(b)) generally is a variable yield. For rules relating to variable rate debt instruments, see § 1.1275-5.

(4) *Yield of debt instrument subject to certain options*—(i) *In general.* The yield of a debt instrument issued for cash or publicly traded property that is subject to a put or call option described in paragraph (f)(4)(ii) of this section or an option to extend described in paragraph (f)(4)(v) of this section shall be determined in accordance with the rules set forth in paragraph (f)(4)(iii) of this section. The yield of a debt instrument issued for nonpublicly traded property and governed by section 1274 that is subject to an option described in paragraph (f)(4) (ii) or (v) of this section shall be determined in accordance with the rule set forth in § 1.1274-6(f). Paragraph (f)(4) of this section shall not apply in a case in which a put or call option is held by a third party. For purposes of paragraph (f)(4) of this section, the term "issuer" shall include a person bearing a relationship to the issuer described in section 108(e)(4).

(ii) *Described options.* An option that is not separately alienable from a debt instrument and that entitles the holder of the option and of the debt instrument to require the issuer to purchase or retire the debt instrument before its stated maturity date is a put option described in paragraph (f)(4) of this section. An option that is not separately alienable from a debt instrument and that entitles the issuer of the option and debt instrument to purchase or retire the debt instrument before its stated maturity date is a call option described in paragraph (f)(4) of this section.

(iii) *Presumption of exercise of option in debt instrument issued for cash or publicly traded property*—(A) *Holders.* The holder of a debt instrument and put option described in paragraph (f)(4)(ii) of this section shall be presumed to exercise this option for purposes of calculating the yield on the debt instrument if, and only if, either—

(*1*) By utilizing the date of exercise of the put option as the maturity date and the amount for which the debt instrument could be sold or retired in accordance with the terms of the put (the put price) as the stated redemption price at maturity, the yield of the debt instrument is greater than it would be if the put option were not exercised, or, equivalently,

(*2*) The put price is greater than the revised issue price (as defined in § 1.1275-1(h)) would be on the date of exercise.

(B) *Issuers.* The issuer of a debt instrument who holds a call option described in paragraph (f)(4)(ii) of this section shall be presumed to exercise this option if, and only if, either—

(*1*) By utilizing the date of exercise of the call as the maturity date and the amount for which the debt instrument could be purchased or retired in accordance with the terms of the call (the call price) as the stated redemption price at maturity, the yield of the debt instrument is lower than it would be if the call option were not exercised, or, equivalently,

(*2*) The call price is less than the revised issue price would be on the date of exercise.

(iv) *Subsequent adjustments.* If a put or call option described in paragraph (f)(4)(ii) of this section is presumed exercised as set forth in paragraph (f)(4)(iii) of this section or § 1.1274-6(f), and is not exercised in fact, the debt instrument shall be treated solely for purposes of sections 1272 and 1273 as if the put or call option were exercised and a new debt instrument were issued on the presumed exercise date for an amount equal to the put price or call price. If, conversely, a put or call option described in paragraph (f)(4)(ii) of this section is presumed not exercised as set forth in paragraph (f)(4)(iii) of this section or § 1.1274-6(f), and is, in fact, exercised, then the debt instrument shall be considered redeemed prior to maturity.

(v) *Options to extend.* If the holder or issuer of a debt instrument has an option to extend the term of the debt instrument on fixed terms and conditions, the debt instrument shall be treated as having a stated maturity date on the latest date on which the debt instrument could be repaid in accordance with such terms and conditions, and the party who may exercise the option to extend shall be treated as having a put option (in the case of the holder of the debt instrument) or a call option (in the case of the issuer of the debt instrument) on the date upon which the debt instrument would be repaid if the option were not exercised. Such put or call option shall be presumed exercised or not exercised in accordance with the rules of paragraph (f)(4) of this section. If the put or call option is presumed exercised, the corresponding option to extend shall be presumed not to be exercised. Conversely, if the put or call option is presumed not exercised, the corresponding option to extend shall be presumed exercised.

(vi) *Variable interest rates.* In the case of a variable rate debt instrument (as defined in § 1.1275-5(a)), the hypothetical yields (as defined in § 1.1275-5(c)(3)(ii)) shall be used for purposes of paragraph (f)(4) of this section.

(g) *Reduction where holder pays acquisition premium*—(1) *Debt instruments purchased after July 18, 1984*—(i) *In general.* If a debt instrument originally issued at a discount after July 1, 1982, is purchased after July 18, 1984, for an amount less than the stated redemption price at maturity but greater than the revised issue price, the purchaser has paid an acquisition premium for the debt instrument. If a purchaser pays an acquisition premium for a debt instrument, the daily portion for any day that the purchaser holds the debt instrument shall be reduced by an amount which is equal to the daily portion for that day (determined without regard to this paragraph (g)(1)(i)) multiplied by the fraction described in paragraph (g)(1)(ii) of this section. For purposes of paragraph (g) of this section, a holder of a debt instrument that was purchased at an acquisition premium includes an original purchaser who acquires the debt instrument for an amount less than the stated redemption price at maturity but greater than the issue price.

(ii) *Determination of fraction.* For purposes of paragraph (g)(1) of this section—

(A) The numerator of the fraction to be determined is the excess (if any) of—

(*1*) The cost of the debt instrument incurred by the purchaser, over

(*2*) The revised issue price (determined without regard to paragraph (g)(1)(i) of this section) of the debt instrument on the date of purchase; and

(B) The denominator of the fraction is the excess of the stated redemption price at maturity over the revised issue price (determined without regard to paragraph (g)(1)(i) of this section) of the debt instrument on the date of purchase.

(2) *Debt instruments purchased before July 19, 1984*—(i) *In general.* If a debt instrument that was originally issued at a discount after July 1, 1982 is purchased before July 19, 1984, for an acquisition premium, the daily portion for any day that the purchaser holds the debt instrument shall be reduced (but not below zero) by the ratable amount of the acquisition premium, determined at the time of purchase.

(ii) *Ratable amount of acquisition premium.* The ratable amount of acquisition premium is equal to—

(A) The excess (if any) of the purchase price over the revised issue price on the date of purchase, divided by

(B) The number of days beginning on the date of purchase and ending on the day before the stated maturity date.

(h) *Transitional rule; binding commitment.* A debt instrument issued pursuant to a written commitment that was binding on July 1, 1982, and at all times thereafter shall be treated as issued on July 1, 1982, and thus is governed by section 1272(b) and § 1.1232–3A. The written commitment must be enforceable against the issuer of the debt instrument under applicable state law and must contain an enforceable obligation to issue the debt instrument at a particular price. Thus, for example, the rules of section 1272(a) and this section do not apply to the exercise of warrants that were outstanding on July 1, 1982, and that were enforceable against the issuer under state law.

(i) [Reserved]

(j) *Basis adjustment.* For purposes of section 1272 and this section, the basis of a debt instrument in the hands of the holder shall be increased by the amount of original issue discount included in the holder's gross income under paragraph (b) of this section, and decreased by the amount of any payment from the issuer to the holder other than a payment of qualified periodic interest with respect to that debt instrument.

(k) *Examples.* The rules stated in paragraphs (b) through (j) of this section may be illustrated by the following examples:

Example (1). On January 1, 1985, A, a calendar-year taxpayer, purchases at original issue for cash of $55,839.48, M Corporation's 5-year zero-coupon bond maturing on January 1, 1990, at a stated redemption price of $100,000. There is no intention to call the bond before maturity. The bond contains $44,160.52 of original issue discount (states redemption price at maturity, $100,000, less issue price, $55,839.48). Since the debt instrument does not provide for payments at regular intervals, under paragraph (d)(1)(iii) of this section, the accrual period is the six-month period ending on December 31 and June 30 of each calendar year. Yield, as determined under paragraph (f) of this section, is 12%, compounded semiannually. The amount of original issue discount allocable to the first accrual period under paragraph (c)(2)(i) of this section is equal to the adjusted issue price at the beginning of the period, which, under paragraph (e)(1) of this section, is the issue price ($55,839.48), multiplied by the semiannual yield factor of 6% (12% divided by 2, the number of accrual periods in a year, under paragraph (c)(2)(i)(A)(*2*) of this section) less the sum of amounts payable as qualified periodic interest (0), or $3,350.37. The adjusted issue price at the beginning of the second accrual period under paragraph (e)(2) of the this section is equal to the issue price plus the amount of original issue discount includible for the first accrual period ($55,839.48 + $3,350.37) or $59,189.85. Under paragraph (c)(2)(i) of this section, the amount of original issue discount allocable to the second accrual period is equal to the adjusted issue price at the beginning of the period, ($59,189.85), multiplied by the semiannual yield factor (6%), less amounts payable as qualified periodic interest (0), or $3,551.39. Since the first and second accrual periods exactly coincide with A's taxable year, A includes in gross income for 1985 the sum of the original issue discount allocable to the first two accrual periods, or $6,901.76. Under paragraph (j) of this section, A increases his basis in the note by the amount of original issue discount taken into gross income for 1985, $6,901.76. A thus has an adjusted basis of $62,741.24. The table below contains the adjusted issue price at the beginning of each accrual period and the amount of original issue discount allocable to each accrual period derived in the same manner as for the first two accrual periods:

Adjusted issue price at beginning of accrual period		OID per accrual period
Jan. 1, 1985	$55,839.48	$3,350.37
July 1, 1985	59,189.85	3,551.39
Jan. 1, 1986	62,741.24	3,764.47
July 1, 1986	66,505.71	3,990.34
Jan. 1, 1987	70,496.05	4,229.76
July 1, 1987	74,725.81	4,483.55
Jan. 1, 1988	79,209.36	4,752.56
July 1, 1988	83,961.92	5,037.72
Jan. 1, 1989	88,999.64	5,339.98
July 1, 1989	94,339.62	5,660.38
Jan. 1, 1990	100,000.00	44,160.52

The sum of the amounts of original issue discount allocable to each accrual period equals the total amount of original issue discount on the bond. Under paragraph (c)(2)(iii) of this section, the amount of original issue discount allocable to the final accrual period is equal to the excess of the stated redemption price at maturity over the adjusted issue price at the beginning of the final accrual period ($100,000–$94,339.62), or $5,660.38.

Example (2). On October 1, 1985, A, a calendar-year taxpayer, purchases at original issue for cash of $55,000, a note of N Corporation with no stated interest maturing on December 31, 1990, at a stated redemption price of $100,000. The bond has $45,000 of original issue discount (stated redemption price at maturity, $100,000, less issue price, $55,000). There is no intention to call the bond before maturity. Since the note does not provide for any payments prior to maturity under paragraph (d)(1)(iii) of this section, the accrual period is the six-month period ending on December 31 and June 30 of each calendar year. The first accrual period is a short accrual period beginning on October 1, 1985, and ending on December 31, 1985. The yield, determined under paragraph (f)(2) of this section using the exact method, is 11.71779%, compounded semiannually. The adjusted issue price at the beginning of the first accrual period under paragraph (e)(1) of this section is the issue price. The amount of original issue discount that A includes in gross income for 1985 is the amount of original issue discount calculated under paragraph (c)(2)(ii)(A) of this section that is allocable to the first accrual period. Since the exact method was used to calculate yield, the exact method must be used to determine the amount of original issue discount that is allocable to the short period. This amount is determined as follows:

(1) Issue price	$55,000.00
(2) Multiplied by: yield factor, the result of the formula in paragraph (c)(2)(ii)(A) of this section [(1 + .117179/2)90/180 − 1]	0.02888
	1,588.40
(3) Less: amounts payable as qualified periodic interest	0
(4) Original issue discount allocable to first accrual period	1,588.40

A includes $1,588.40 of original issue discount in gross income for 1985. Under paragraph (j) of this section, A increases his basis by that amount. A's adjusted basis thus is $56,588.40 ($55,000 + $1,588.40). This amount is also the adjusted issue price at the beginning of the second accrual period determined under paragraph (e)(2)(i) of this section. The amount of original issue discount allocable to the second accrual period is determined as follows:

(1) Adjusted issue price on January 1, 1986	$56,588.40
(2) Multiplied by: yield factor, (.117179/2)	0.05859
	3,315.51
(3) Less: amounts payable as periodic interest	0
(4) Original issue discount allocable to the second accrual period	3,315.51

The adjusted issue price at the beginning of the third accrual period is $59,903.91 ($56,588.40 + $3,315.51).
The amount of original issue discount allocable to the third accrual period is determined as follows:

(1) Adjusted issue price on July 1, 1986	$59,903.91
(2) Multiplied by: yield factor	0.05859
	3,509.77
(3) Less: amounts payable as periodic interest	0
(4) Original issue discount allocable to the third accrual period	3,509.77

The amount of original issue discount which A includes in gross income for 1986 is $6,825.28 ($3,315.51 + $3,509.77). Under paragraph (j) of this section, A increases his basis by that amount. A's adjusted basis thus is $63,413.68 ($56,588.40 + $6,825.28). The amount of original issue discount allocable to the remaining accrual periods may be determined by repeating steps (1) through (4), above, for each accrual period until the final accrual period. The amount of original issue discount allocable to the final accrual period is the excess of the stated redemption price at maturity over the adjusted issue price at the beginning of that period.

Example (3). Assume the same facts as in Example (2), except that the yield under paragraph (f)(2) of this section is determined using the approximate method for the short first accrual period with a resulting yield of 11.70963%, compounded semiannually. Since the approximate method was used to calculate yield, the amount of original issue discount allocable to the first accrual period is determined under the approximate method of paragraph (c)(2)(ii)(B) of this section as follows:

(1) Issue price	$55,000.00
(2) Multiplied by: yield factor, (.1170963/2)	0.05855
	3,220.25
(3) Multiplied by the fraction f (number of days in the first accrual period over number of days in a full accrual period, 90/180)	.50
	1,610.13
(4) Less: amounts payable as qualified periodic interest	0
(5) Original issue discount allocable to the first accrual period	1,610.13

Thus, using the approximate method, A includes $1,610.13 in gross income for 1985 and increases his basis by that amount to $56,610.13, which is also the adjusted issue price at the beginning of the second accrual period.

Example (4). (i) On November 1, 1985, B, a calendar-year taxpayer, purchases at original issue for cash of $86,235.17, N Corporation's 15-year bond, maturing on October 31, 2000, at a stated redemption price of $100,000. The bond provides for semiannual payments of interest at an annual rate of 10% ($5,000 on May 1 and November 1 of each calendar year). There is no intention to call the bond before maturity. The bond has $13,764.83 of original issue discount (stated redemption price at maturity, $100,000, less issue price, $86,235.17). Under the rule prescribed in § 1.1275–2(e)(3), the interest payments due on May 1 and November 1 of each calendar year may be treated as paid on the last day of the preceding month, or on April 30 and October 31 of each calendar year. Assuming this rule is followed, the accrual period, under paragraph (d)(1)(i) of this section, is the interval between payment dates, or the six-month period ending on October 31 and April 30 of each calendar year. Yield under paragraph (f)(1) of this section is 12%, compounded semiannually.

(ii) The amount of original issue discount allocable to the first accrual period is determined as follows:

(1) Issue price	$86,235.17
(2) Multiplied by: yield factor, (.12/2)	.06
	5,174.11
(3) Less: amounts payable as periodic interest	5,000.00
(4) Original issue discount allocable to the first accrual period	174.11

The daily portion of original issue discount for the first accrual period under paragraph (c)(1) of this section is the amount shown on line (4), above, divided by the number of days in the accrual period. Using the 30-day convention described in § 1.1275–2(e), the number of days in a six-month accrual period is 180; therefore, the daily portion of original issue discount for the first accrual period is equal to $174.11/180, or $0.96728. Since B held the bond in 1985 for 60 days, the amount of original issue discount that B includes in gross income for 1985 is equal to 60x$0.96728, or $58.04. The remainder of the original issue discount allocable to the second accrual period, $116.07, is included in gross income for 1986. Under paragraph (j) of this section, B increases his basis by the amount of original issue discount included in gross income for 1985. B's adjusted basis on January 1, 1986, is thus $86,293.21. The adjusted issue price of the bond at the beginning of the second accrual period under paragraph (e)(2) of this section is $86,409.28 (issue price, $86,235.17, plus original issue discount previously includible, $174.11).

(iii) The amount of original issue discount allocable to the second accrual period is determined as follows:

(1) Adjusted issue price on May 1, 1986	$86,409.28
(2) Multiplied by: yield factor	.06
	5,184.56
(3) Less: amounts payable as periodic interest	5,000.00
(4) Original issue discount allocable to the second accrual period	184.56

The adjusted issue price at the beginning of the third accrual period under paragraph (e)(2) of this section is $86,593.84 ($86,409.28 + $184.56). The amount of original issue discount allocable to the third accrual period is determined as follows:

(1) Adjusted issue price on November 1, 1986	$86,593.84
(2) Multiplied by: yield factor	.06
	5,195.63
(3) Less: amounts payable as periodic interest	5,000.00
(4) Original issue discount allocable to the third accrual period	195.63

The daily portion of original issue discount for the third accrual period is $195.63, the amount shown on line (4), above, divided by the number of days in the accrual period (180, using the 30-day convention described in § 1.1275–2(e)), or $1.08683.
B includes in gross income for 1986 only the sum of the daily portions of original issue discount for the number of days in the third accrual period that fall in 1986 for which B held the bond (60 days). Thus, B includes $65.21 for 1986 (60x$1.08683). The remaining original issue discount allocable to the third accrual period, $130.42, is included in gross income for 1987. The total amount of original issue discount includible by B in gross income for 1986 is $365.84 ($116.07 + $184.56 + $65.21).

Example (5). (i) Assume the same facts as in Example (4), except that B sells the bond to C, a calendar-year taxpayer, on November 1, 1988, for cash of $90,000. The revised issue price (as defined in § 1.1275–1(h)) on that date is $87,449.65. Under paragraph (g)(1)(i) of this section, C has purchased the bond at an acquisition premium of $2,550.35 (cost, $90,000, less revised issue price, $87,449.65). The daily portion for any day that C holds the bond shall be reduced under paragraph (g)(1)(i) of this section by an amount equal to the daily portion multiplied by a fraction, described in paragraph (g)(1)(ii) of this section, the numerator of which is the amount of the acquisition premium paid by C, and the denominator of which is $12,550.35, (the excess of the stated redemption price at maturity, $100,000, over the revised issue price, $87,449.65). C thus reduces his daily portion of original issue discount by an amount equal to that daily portion multiplied by the fraction, $2,550.35/$12,550.35, or 0.20321.

(ii) The amount of original issue discount that C includes in gross income for 1988 is determined as follows:

(1) Adjusted issue price on November 1, 1988	$87,449.65
(2) Multiplied by: yield factor	.06
	5,246.98
(3) Less: amounts payable as qualified periodic interest	5,000.00
(4) Original issue discount allocable to accrual period beginning on November 1, 1988	246.98
(5) Divided by: number of days in the accrual period	180
(6) Daily portion of original issue discount	1.37211
(7) Fraction described in paragraph (g)(1)(ii) of this section	0.20321
(8) Line (6) multiplied by line (7)	0.27883
(9) Daily portion of original issue discount includible by C (line (6) minus line (8))	1.09328

Since C holds the bond for only two months in 1988, the amount of original issue discount that C includes in gross income for 1988 is equal to 60x$1.09328, or $65.60. Under paragraph (j) of this section, C increases his basis, $90,000, by that amount. C's adjusted basis as of January 1, 1989 thus is $90,065.60.

(iii) The amount of original issue discount that C includes in gross income for 1989 includes the original issue discount for the remaining 120 days in the accrual period, $131.19 (120x$1.09328), that began on November 1, 1988. The adjusted issue price at the beginning of the next accrual period, however, is determined under paragraph (e)(2) of this section without regard to any adjustments made under paragraph (g) of this section. In determining that adjusted issue price, the full amount of the original issue discount allocable to the immediately preceding accrual period is added to the adjusted issue price at the beginning of the preceding accrual period. The original issue discount allocable to the preceding accrual period (before adjustment for C's acquisition premium) as shown on line (4), above, is $246.98. The adjusted issue price at the beginning of the accrual period beginning on May 1, 1989, is thus $ 63 ($87,449.65 + $246.98).

(iv) The amount of original issue discount includible by C for the accrual period beginning on May 1, 1989, is determined as follows:

(1) Adjusted issue price on May 1, 1989	$87,696.63
(2) Multiplied by: yield factor	.06
	5,261.80
(3) Less: amounts payable as qualified periodic interest	5,000.00
(4) Original issue discount allocable to accrual period beginning on May 1, 1989	261.80
(5) Divided by: number of days in the accrual period	180
(6) Daily portion of original issue discount	1.45444
(7) Fraction described in paragraph (g)(1)(ii) of this section	0.20321
(8) Line (6) multiplied by line (7)	0.29556
(9) Daily portion of original issue discount includible by C (line (6) minus line (8))	1.15888

The total amount of original issue discount includible by C for the accrual period beginning on May 1, 1989, is $208.60 (180×$1.15888). The total amount of original issue discount allocable to the accrual period beginning on May 1, 1989, as shown on line (4) above, is $261.80. The adjusted issue price at the beginning of the next accrual period is thus $87,958.43 ($87,696.63 + $261.80).

(v) The amount of original issue discount includible by C for the accrual period beginning on November 1, 1989, is determined as follows:

(1) Adjusted issue price on November 1, 1989	$87,958.43
(2) Multiplied by: yield factor	.06
	5,277.51
(3) Less: amounts payable as periodic interest	5,000.00
(4) Original issue discount allocable to accrual period	277.51
(5) Divided by: number of days in the accrual period	180
(6) Daily portion of original issue discount	1.54172
(7) Fraction described in paragraph (g)(1)(ii) of this section	0.20321
(8) Line (6) multiplied by line (7)	0.31329
(9) Daily portion of original issue discount includible by C (line (6) minus line(8))	1.22843

Since C holds the bond in 1989 for only two months of the accrual period beginning on November 1, 1989, C includes 60×$1.22843, or $73.71 of original issue discount for the last two months of 1989. The remainder of the original issue discount includible by C for the accrual period beginning on November 1, 1989, is included by him in gross income for 1990.

(vi) The total amount of original issue discount includible by C in gross income for 1989 is $413.50 ($131.19 + $208.60 + $73.71). Under paragraph (j) of this section, C increases his basis by this amount. C's adjusted basis as of December 31, 1989 is $90,479.10 ($90,065.60 + $413.51). The amount of original issue discount includible by C for the remaining accrual periods, assuming he holds the bond to maturity, may be determined by repeating steps (1) through (9), above, for each accrual period until maturity.

Example (6). (i) On November 19, 1985, A, a calendar-year taxpayer, purchases at original issue for cash of $68,088.77, O Corporation's bond maturing on December 31, 1988, at a stated redemption price of $75,000. The bond has $8,390.69 of original issue discount (stated redemption price at maturity, $75,000, less issue price, $66,609.31). There is no intention to call the bond before maturity. The instrument provides for payments of interest at an annual rate of 8%, paid quarterly ($1,500 per quarter). The first interest payment is made on December 31, 1985, and is a full $1,500 payment even though the first accrual period from November 19, 1985, to December 31, 1985, is a short first accrual period. Yield to maturity, determined under paragraph (f)(2) of this section according to the exact method, is 12% compounded quarterly. The accrual period, under paragraph (d)(1)(i) of this section, is the interval between payment dates, or a three-month period ending on December 31, September 30, June 30, and March 31 of each calendar year.

(ii) Using the 30-day convention described in § 1.1275-2 (e), the short period contains 42 days. Therefore, the portion of the $1,500 payment on December 31, 1985 that constitutes qualified periodic interest is the amount of interest payable for a short period of 42 days under the exact method for a debt instrument with an interest rate of 8%, compounded quarterly. This amount is $696.30, which is the result of the following formula: $[1+.08/4)^{42/90}-1]\times\$75{,}000$.

(iii) Under paragraph (e)(1) of this section, the adjusted issue price at the beginning of the first accrual period is the issue price. The amount of original issue discount allocable to the first accrual periods is determined under paragraph (c)(2)(ii)(A) of this section as follows:

(1) Issue price	$68,088.77
(2) Multiplied by: yield factor, the result of the formula in paragraph (c)(2)(ii)(A) of this section $[(1+.12/4)^{42/90}-1]$	.01389
	945.73
(3) Less: amounts payable as periodic interest	696.30
(4) Original issue discount allocable to the first accrual period	249.43

A includes $249.43 of original issue discount in gross income for 1985. A's adjusted issue price at the beginning of the second accrual period under paragraph (e)(2) of this section is determined by increasing A's issue price, $68,088.77, by the amount of original issue discount allocable to the first accrual period, $249.43, and by reducing this sum by the portion of the payment on December 31, 1985, not treated as qualified periodic interest, $803.70. A's adjusted issue price as of January 1, 1986, is thus $67,534.50 ($68,088.77 + $249.43 − $803.70). Under paragraph (j) of this section, this amount is also A's adjusted basis in the debt instrument.

(iv) The amount of original issue discount allocable to the second accrual period is determined as follows:

(1) Adjusted issue price on January 1, 1986	$67,534.50
(2) Multiplied by: yield factor (.12/4)	.03
	2,026.04
(3) Less: amounts payable as qualified periodic interest	1,500.00
(4) Original issue discount allocable to the second accrual period	526.04

(v) Assume the same facts as in part (i), except that A purchases the bond for cash of $68,081.36 and that the yield, determined under paragraph (e)(2) of this section according to the approximate method, is 12%, compounded quarterly. The amount of original issue discount allocable to the first accrual period is determined under paragraph (c)(2)(ii)(B) as follows:

(1) Issue price	$68,081.36
(2) Multiplied by: yield factor (.12/4)	.03
	2,042.44
(3) Multiplied by: the fraction f (number of days in the first accrual period over the number of days in a full accrual period, 42/90)	.46667
	953.14
(4) Less: amounts payable as qualified periodic interest ($1,500x42/90)	700.00
(5) Original issue discount allocable to the first accrual period	253.14

A includes in gross income for 1985 $253.14 of original issue discount. Both A's adjusted issue price and adjusted basis at the beginning of the second accrual period under paragraph (e)(2) of this section is $67,534.50 ($68,081.36 + 253.14 − $800.00); it is also the same as the adjusted issue price at the beginning of the second accrual period in part (i). The amount of original issue discount allocable to the remaining accrual periods to maturity, assuming A holds the bond to maturity, will thus be identical to the amounts determined in part (i).

Example (7). (i) On January 1, 1983, B, a calendar-year taxpayer, purchases at original issue for cash of $86,757.20, M Corporation's 20-year bond maturing on December 31, 2002, at a stated redemption price of $100,000. The bond provides for annual payments of interest at 12%, compounded annually. The bond has $13,242.80 of original issue discount (stated redemption price at maturity, $100,000, less issue price, $86,757.20). There is no intention to call the bond before maturity. The yield determined under paragraph (f)(1) of this section (accurate to two decimal places) is 14.00%, compounded annually. The accrual period, under paragraph (d)(2) of this section is the one-year period beginning on January 1 and ending on December 31 of each calendar year. The adjusted issue price at the beginning of the first accrual period is, under paragraph (e)(2) of this section, the issue price. The amount of original issue discount allocable to the first accrual period is determined under paragraph (c)(2) of this section as follows:

(1) Issue price	$86,757.20
(2) Multiplied by: yield factor	.14
	12,146.01
(3) Less: amounts payable as qualified periodic interest	12,000.00
(4) Original issue discount allocable to the first accrual period	146.01

B includes $146.01 of original issue discount in gross income for 1983. Under paragraph (j) of this section, B increases his basis by this amount. B's adjusted basis thus becomes $86,903.21 ($86,757.20 + $146.01). This amount is also the adjusted issue price at the beginning of the second accrual period under paragraph (e)(2) of this section. The amount of original issue discount allocable to the remaining accrual periods to maturity, determined as in steps (1) through (4), is set forth in the following table:

Accrual period	Adjusted issue price	Original issue discount
1984	$86,903.21	$166.45
1985	87,069.66	189.75
1986	87,259.41	216.32
1987	87,475.73	246.60
1988	87,722.33	281.13
1989	88,003.46	320.48
1990	88,323.94	365.35
1991	88,689.29	416.50
1992	89,105.79	474.81
1993	89,580.60	541.28
1994	90,121.88	617.06
1995	90,738.94	703.45
1996	91,442.39	801.93
1997	92,244.32	914.21
1998	93,158.53	1,042.19
1999	94,200.72	1,188.10
2000	95,388.82	1,354.43
2001	96,743.26	1,544.06
2002	98,287.32	1,712.68

Under paragraph (c) (2) (iii) of this section, the original issue discount allocable to the final accrual period is determined by subtracting the adjusted issue price on January 1, 2002, $98,287.32, from the stated redemption price at maturity, $100,000, for a result of $1,712.68.

(ii) Assume the same facts as in part (i), except that B sells the bond to C on February 1, 1984, for cash of $87,000. The revised issue price of the bond (as defined in § 1.1275–1(h)) on that date is equal to the adjusted issue price of the bond on January 1, 1984, plus the sum of the daily portions of original issue discount for the month of January. The daily portion under paragraph (c) of this section is equal to the amount of original issue discount allocable to the accural period beginning on January 1, 1984, ($166.45 in the table in part (i)) divided by the number of days in the accrual period, (360, using the 30-day convention described in § 1.1275–2(e)). The daily portion is $0.46236. The sum of the daily portions for the month of January is therefore $13.87 ($0.46236 × 30). The revised issue price on February 1, 1984, is $86,917.08 ($86,903.21 + $13.87). Under paragraph (g) of this section, C has purchased the bond at an acquisition premium of $82.92 (cost, $87,000, less revised issue price, $86,917.08). The daily portion of original issue discount for any day that C holds the bond is reduced under paragraph (g)(2) by the ratable amount of the acquisition premium defined in paragraph (g)(2)(ii) as the total acquisition premium ($82.92), divided by the number of days beginning on the date of purchase and ending on the day before the stated maturity date (6,810) using the 30-day convention and 360-day convention described in § 1.1275–2(e). The ratable amount of acquisition premium is thus $0.01218. The daily portion of original issue discount that is includible in gross income for 1984 ($0.46236) is reduced by this amount to result in a daily portion of $0.45018. The amount of original issue discount includible by C in gross income for 1984 is thus $148.56 ($0.45018 x 330). For the remaining accrual periods in the bond's term, the ratable reduction per year will be $4.38 ($0.01218 x 360). The table below sets forth the amount of original issue discount includible in gross income by C for each remaining year in the bond's term, assuming C holds the bond to maturity:

Accrual period	OID allocable	Ratable amount of acquisition premium	CID includable by C
1984	$166.45	$4.02	$162.43
1985	189.75	4.38	185.37
1986	216.32	4.38	211.94
1987	246.60	4.38	242.22
1988	281.13	4.38	276.75
1989	320.48	4.38	316.10
1990	365.35	4.38	360.97
1991	416.50	4.38	412.12
1992	474.81	4.38	470.43
1993	541.28	4.38	536.90
1994	617.06	4.38	612.68
1995	703.45	4.38	699.07
1996	801.93	4.38	797.55
1997	914.21	4.38	909.83
1998	1,042.19	4.38	1,037.81
1999	1,188.10	4.38	1,183.72
2000	1,354.43	4.38	1,350.05
2001	1,544.06	4.38	1,539.68
2002	1,712.68	4.38	1,708.30

Example (8). Assume C, a calendar-year taxpayer, is the holder of a 3-year publicly offered debt instrument which he purchased at original issue on January 1, 1987, for its issue price of $93,803.81. The debt instrument has a face amount of $100,000, and provides for six equal semiannual payments of $19,076.19, the last of which is due on December 31, 1989. Each payment of $19,076.19 represents the semiannual payment necessary to amortize $100,000 at an annual rate of interest of 8%, compounded semiannually, over a 3-year period. Of each payment of $19,076.19, the amounts which represent qualified periodic interest (as defined in § 1.1273–1(b)(1)(iii) are set forth in the table below. The instrument is an installment obligation within the meaning of §1.1273-1(b)(2)(i), and also is a self-amortizing installment obligation within the meaning of § 1.1273-1(b)(2)(iii) of this section and has $6,196.19 of original issue discount (stated redemption price at maturity, $100,000, less issue price, $93,803.81). Yield determined under paragraph (f)(1) of this section, is 12%, compounded semiannually. The accrual period, under paragraph (d)(1)(i) of this section is a six-month period ending on June 30 and December 31 of each calendar year. The adjusted issue price at the beginning of the first accrual period is, under paragraph (e)(1) of this section, the issue price. The amount of original issue discount allocable to the first accrual period is determined under paragraph (c)(2)(i) of this section as follows:

(1) Issue price	$93,803.81
(2) Multiplied by: yield factor	.06
	5,628.23
(3) Less: amount of first interest payment	4,000.00
(4) Original issue discount allocable to the first accrual period	1,628.23

The adjusted issue price at the beginning of the second accrual period is determined under paragraph (e)(2)(ii) of this section by adding to the adjusted issue price ($93,803.81) the amount of original issue discount allocable to the first accrual period ($1,628.23) for a total of $95,432.04, and then decreasing the sum by the amount of the first payment that does not represent qualified periodic interest ($15,076.19). The adjusted issue price at the beginning of the second accrual period is $80,355.85. Note that the same result is obtained by increasing the adjusted issue price ($93,803.81) by the product of this issue price and yield as shown on line (2), above, ($5,628.23) and then by decreasing that sum by the total amount of the first payment ($19,076.19). The amount of original issue discount allocable to the remaining accrual periods may be determined by repeating steps (1) through (4), above, and then determining the new adjusted issue price. The results are set forth in the following table:

Accrual period	Product of adjusted issue price and yield	Qualified periodic interest	OID	Amounts other than qualified periodic interest	Adjusted issue price
1	$5,628.23	$4,000.00	$1,628.23	$15,076.19	$80,355.85
2	4,821.35	3,396.95	1,424.40	15,679.24	66,101.01
3	3,966.06	2,769.78	1,196.28	16,306.41	50,990.89
4	3,059.45	2,117.53	941.92	16,958.66	34,974.15
5	2,098.45	1,439.18	659.27	17,637.01	17,996.41
6	1,079.78	733.70	346.03	18,342.99	

Example (9). (i) On January 1, 1986, A sells B nonpublicly traded property for a stated purchase price of $3,500,000. B pays A $500,000 and gives A a 10-year note for $3,000,000. B's note calls for no interest in the first two years and interest at a rate of 15%, payable annually over the remaining 8 years of the debt instrument, with the first interest payment of $450,000 due on December 31, 1988 and the last such payment due on December 31, 1995, together with the $3,000,000 of principal. Assume that the debt instrument has adequate stated interest. (See § 1.1274-3 (c)(2), Example (1)). The yield of this debt instrument under paragraph (f)(1) of this section is 10.67837%, compounded annually. Since no interest is payable in 1986 or 1987, the payments of interest in years 1988 through 1995 are not qualified periodic interest payments within the meaning of § 1.1273-1(b)(1)(ii). Hence, B's obligation to A is treated as an installment obligation (within the meaning of § 1.1273-1(b)(2) with an issue price of $3,000,000 and a stated redemption price at maturity of $6,600,000 ($3,000,000 stated principal plus 8 payments of $450,000). As a result, B's obligation has original issue discount of $3,600,000 (stated redemption price at maturity, $6,600,000 less issue price, $3,000,000). The amount of original issue discount allocable to 1986 under paragraph (c)(2) of this section is the issue price of $3,000,000 multiplied by the yield, 10.67837%, or $320,351. This produces an adjusted issue price under paragraph (e)(2) of this section as of January 1, 1987 of $3,320,351 (issue price of $3,000,000 plus original issue discount in 1986 of $320,351). The amount of original issue discount allocable to 1987 is the product of this adjusted issue price and the yield of 10.67837%, or $354,560. The adjusted issue price at the beginning of 1988 is thus $3,674,911 ($3,320,351 + $354,560).

(ii) For the years 1988 through 1995, the amount of original issue discount allocable to each year is equal to the adjusted issue price at the beginning of that year multiplied by the yield. Since the aggregate amount of original issue discount accrued as of the end of any accrual period always exceeds the aggregate amount of stated interest as of the end of that accrual period, each $450,000 payment is treated entirely as a payment of original issue discount. The $450,000 payment has no tax consequences other than to reduce the adjusted issue price for future accrual periods under paragraph (e)(2)(ii) of this section. The amount of original issue discount allocable to 1988 is equal to the adjusted issue price of $3,674,911 multiplied by the yield of 10.67837%, or $392,421. The adjusted issue price at the beginning of 1989 is thus $3,617,331 ($3,674,911 + $392,421 – $450,000). The amounts treated as interest and the adjusted issue price for each year of the transaction are set forth in the following table:

Year	Adjusted issue price at beginning of year	Original issue discount
1986	$3,000,000	$320,351
1987	3,320,351	354,560
1988	3,674,911	392,421
1989	3,617,331	386,272
1990	3,553,604	379,467
1991	3,483,071	371,935
1992	3,405,006	363,599
1993	3,318,605	354,373
1994	3,222,978	344,162
1995	3,117,140	332,860

Example (10). A sells Blackacre to B on July 1, 1985, in exchange for cash of $50,000 and B's purchase money obligation having a stated principal amount of $200,000, maturing on June 10, 2015. B's note provides for 360 equal monthly payments of $1,467.53; this amount represents the monthly payment necessary to amortize a loan of $200,000 at an annual rate of interest of 8%, compounded monthly over a 30-year period. Of each payment of $1,467.53 during 1985, the amounts which represent qualified periodic interest payments (as defined in § 1.1273-1(b)(1)(iii)) are set forth in the table below. The note is an installment obligation within the meaning of § 1.1273-2(b)(2)(i) and is a self-amortizing obligation within the meaning of § 1.1273-2(b)(2)(iii) of this section. The stated redemption price at maturity under § 1.1273-2(b)(2)(iii) is the stated principal amount of the obligation, or $200,000. Assume that the transaction is not potentially abusive within the meaning of section 1274(b)(3)(B). Assume also that under section 1274(c)(2) and the regulations thereunder the note does not have adequate stated interest and that the imputed interest rate is 11%, compounded monthly; this is also the yield of the obligation under paragraph (f)(3) of this section. The issue price of the note is the imputed principal amount determined under § 1.1274-4, which is $154,099.87. The note has $45,900.13 of original issue discount (stated redemption price at maturity, $200,000, less issue price, $154,099.87). The accrual period under paragraph (d)(1)(i) of this section, is one month. The adjusted issue price at the beginning of the first accrual period is, under paragraph (e)(1) of this section, the issue price. The amount of original issue discount allocable to the first accural period is determined under paragraph (c)(2)(i) of this section as follows:

(1) Issue price	$154,099.87
(2) Multiplied by: yield factor (.11/12)	.00917
	$1,412.58
(3) Less: amount of first payment that represents qualified periodic interest	-$1,333.33
(4) Original issue discount allocable to the first accrual period	$79.25

The adjusted issue price at the beginning of the second accrual period is determined under paragraph (e)(2)(ii) of this section by adding to the issue price ($154,099.87) the amount of original issue discount allocable to the first accrual period ($79.25) and then decreasing the sum by the amount of the first payment that does not represent qualified periodic interest designated as principal ($134.20). The adjusted issue price at the beginning of the second accrual period is $154,044.92. As stated in Example (8), the same result may be obtained by adding to the issue price ($154,099.87) the product of the adjusted issue price and yield as shown on line (2), ($1,412.58), and then decreasing that sum by the total monthly payment ($1,467.53). The amount of original issue discount allocable to the remaining accrual periods may be determined by repeating steps (1) through (4), and then determining the new adjusted issue price. The results for the first 12 months are set forth in the following table:

Month	Product of adjusted issue price and yield	Qualified periodic interest	OID	Amount other than qualified periodic interest	Adjusted issue price
1	$1,412.58	$1,333.33	$79.25	$134.20	$154,044.92
2	1,412.08	1,332.44	79.64	135.09	153,989.47
3	1,411.57	1,331.54	80.03	135.99	153,933.51
4	1,411.06	1,330.63	80.43	136.90	153,877.04
5	1,410.54	1,329.72	80.82	137.81	153,820.05
6	1,410.02	1,328.80	81.22	138.73	153,762.54
7	1,409.49	1,327.88	81.61	139.65	153,704.50
8	1,408.96	1,326.94	82.02	140.59	153,645.93
9	1,408.42	1,326.01	82.41	141.52	153,586.82
10	1,407.88	1,325.06	82.82	142.47	153,527.17
11	1,407.33	1,324.11	83.22	143.42	153,466.97
12	1,406.78	1,323.16	83.62	144.37	153,406.22

Example (11). (i) On January 1, 1985, A, a calendar-year taxpayer, purchases at original issue for cash of $70,000, M Corporation's 15-year bond, maturing on December 31, 1999, at a stated redemption price of $100,000. Assume that the debt instrument is a capital asset in A's hands. The instrument provides for semiannual payments of interest at an annual rate of 8% ($4,000 semiannually). The bond further provides a put option entitling the holder to require the issuer to retire the bond on December 31, 1994, at a price of $85,000. Yield determined under paragraph (f)(1) of this section without regard to the existence of a put option is 12.47%, compounded semiannually. Yield determined by using December 31, 1994, as the maturity date and $85,000 as the stated redemption price at maturity is 12.56%, compounded semiannually. The revised issue price (as defined in § 1.1275–1(h)) on that date would be $83,736. Under paragraph (f)(4)(iii) (A) of this section, yield is calculated at the time of issue by assuming that A will excise the put option because exercise of the option would increase the overall yield on the instrument from 12.47% to 12.56%, compounded semiannually, or, alternatively, because the put price exceeds the revised issue price as of the date the put becomes exercisable. Since the put option is assumed exercised, the bond is considered to be a 10-year bond with an issue price of $70,000, a stated redemption price at maturity of $85,000, and yield determined under paragraph (f)(1) of this section of 12.56%, compounded semiannually. If the put option is, in fact, not exercised, then under paragraph (f)(4)(iv) of this section the bond is treated, for purposes of sections 1272 and 1273, as if it were retired on the presumed exercise date, December 31, 1994, and M is treated as having issued a new debt instrument to A for an issue price equal to the put price on that date, $85,000. This new debt instrument is treated as maturing on December 31, 1999, at a stated redemption price of $100,000, with yield of 12.08%, compounded semiannually, and providing for payments of interest at an annual rate of 8%, compounded semiannually.

(ii) Assume the same set of facts as in part (i), except that the put price is $82,000. Exercise of the put would result in a yield of 12.34%, compounded semiannually, calculated by using December 31, 1994, as the maturity date and $82,000 as the stated redemption price at maturity. This yield is lower than the yield of 12.47%, compounded semiannually, calculated for the complete 15-year term. It this is assumed at the time of issue, under paragraph (f)(4)(iii)(A) of this section, that A will not exercise the put option, since exercise of the option will result in a lower overall yield or, alternatively, because the put price is less than the revised issue price as of the date the put is exercisable. If the put option is, in fact, exercised, A realizes a capital loss equal to the excess of the revised issue price on the date of exercise ($83,736) over the put price ($82,000), or $1,736. M Corporation will have cancellation of indebtedness income of $1,736 under section 108 as it has redeemed a liability worth $83,736, for only $82,000.

(iii) Assume the same facts as in part (i), except that instead of providing the holder with an option to put the bond, the instrument provides the issuer with the right to call the bond on December 31, 1994, for a call price of $80,000. Exercise of the call would result in a 10-year term, an issue price of $70,000, a stated redemption price at maturity of $80,000, and yield of 12.20%, compounded semiannually. Under paragraph (f)(4)(iii)(B) of this section, it is assumed at the date of issue that the issuer will exercise the call option as it will result in a lower yield, or, alternatively, because the call price is less than the revised issue price as of the date the call is exercisable. If the call option is, in fact, not exercised, then the bond is treated as if it were retired on the presumed exercise date, December 31, 1994, and M is treated as having issued a new debt instrument to A for an issue price equal to the call price on that date, ($80,000). This new debt instrument is treated as having a term of 5 years, a stated redemption price at maturity of $100,000, and a yield of 13.65%, compounded semiannually.

(iv) Assume the same facts as in part (iii), except that call price is $85,000. Exercise of the call would result in a 10-year term, an issue price of $70,000, a stated redemption price at maturity of $85,000, and yield of 12.56%, compounded seminnually. Under paragraph (f)(4)(iii)(B) of this section, it is assumed at the date of issue that the call will not be exercised because it would result in a higher overall yield, or, alternatively, because the call price exceeds the revised issue price as of the date the call is exercisable. If the call is, in fact, exercised, A realizes a capital gain of $1,264 under section 1001 (amount realized, $85,000, less adjusted basis, $83,736). Under § 1.163–7(f), M Corporation is entitled to deduct as interest the excess of the repurchase price ($85,000) over the revised issue price as of the date the call is exercisable ($83,736), or $1,264.

Example (12). (i) The facts are the same as in Example (11), part (i), except that the debt instrument has an initial term of 10 years, a stated redemption price at maturity of $85,000, and the holder, A has an option to extend the term of the debt instrument (as defined in paragraph (f)(4)(v) of this section) for 5 years for a payment of $100,000 at maturity and semiannual interest payments of 8%. Under paragraph (f)(4)(v) of this section, the debt instrument is treated as if it had a term of 15 years and a stated redemption price at maturity of $100,000, and A is treated as having a put option for $85,000 at the end of 10 years. The analysis of the debt instrument is exactly the same as in part (i) of Example (11). Since it was concluded there that the put option will not be exercised, it is similarly concluded that A will not exerise his option to extewnd, and the debt instrument's stated term of 10 years and stated redemption price at maturity of $85,000 will be respected. If the option to extend is exercised, the debt instrument is treated as retired on the presumed exercise date, December 31, 1994, and a new debt instrument is considered issued on that date for a term of 5 years with an issue price equal to the original stated redemption price at maturity of $85,000, a new stated redemption price at maturity of $100,000.

(ii) The facts are the same as in part (i), except that the stated redemption price at maturity is $82,000. The analysis is the same as in part (ii) of Example (eleven). Since it was concluded there that the put option will not be exercised,it is similarly concluded that A will exercise his option to extend. The debt instrument is treated as having a term of 15 years and a stated redemption price at maturity of $100,000. If the option to extend is not exercised, the debt instrument is treated as retired prior to maturity.

Example (13). (i) A debt instrument is issued on March 1, 1987 for $100,000 cash and is redeemable at any time at the option of the holder. The debt instrument calls for interest to accrue at an annual rate of 11%, compounded quarterly, to be paid when the debt instrument is redeemed. Since the debt instrument calls for quarterly compounding of interest, under paragraph (d)(1)(i) of this section, the accrual period is the three-month period ending on May 31, August 31, November 30, and February 28 (or 29) of each calendar year. Pursuant to paragraph (f)(5)(ii) of this section, the yield of the debt instrument is 11%, compounded quarterly.

(ii) Assume that the debt instrument is not redeemed at any time during 1987. The amount of original issue discount allocable to the first accrual period is, under paragraph (c)(2)(i) of this section, the product of the issue price ($100,000) and the yield factor (.11/4), reduced by the sum of amounts payable as qualified periodic interest (0), $2,750.00. The adjusted issue price at the beginning of the second accrual period is, under paragraph (e)(2)(i) of this section, the sum of the issue price and the amount of original issue discount includible for the first accrual period ($100,000 + $2,750), or $102,750. The original issue discount allocable to the second accrual period is the product of the adjusted issue price at the beginning of the second accrual period and the yield factor ($102,750 × 0.0275), or $2,825.63. The original issue discount allocable to subsequent accrual periods is calculated in the same manner as above.

Example (14). (i) On July 1, 1986, A sells Blackacre to B in exchange for B's debt instrument calling for five annual payments each equal to 10% of the gross yield from Blackacre for the immediately preceding fiscal year ending on March 31, 1987. Each payment is to be made on the following June 30, together with interest at a rate of 11%, compounded annually from the issue date, July 1, 1986, to the date of payment. The terms of the debt instrument further specify that if by June 30, 1990, B has not paid at least $5 million to A (exclusive of interest), the payment due on June 30, 1991 shall consist of the excess of $5 million over the sum of all prior payments (exclusive of interest), plus interest at 11%, compounded annually from the issue date. Assume that on July 1, 1986, the Federal short-term rate is 9%, compounded annually, and the Federal mid-term rate is 11%, compounded annually.

(ii) Since B's debt instrument provides for payments of interest on the unpaid principal balance at a fixed rate, the provisions of § 1.1275–4(d) (relating to certain contingent payments within a fixed period) do not apply. B's debt instrument calls for interest at a rate equal to the Federal mid-term rate on the issue date. Under § 1.1274–3(b), therefore, B's debt instrument has adequate stated interest. The issue price of B's debt instrument under § 1.1274–2(b)(1) is thus the stated principal amount, which is the minimum total of principal payments to be made under the debt instrument ($5 million). The accrual period of the debt instrument under paragraph (d)(2) of this section is the one-year period ending on June 30 of each calendar year, and the yield of the debt instrument under paragraph (f)(3)(ii) of this section is 11%, compounded annually. The amount of original issue discount allocable to each annual accrual period under the debt instrument pursuant to paragraph (c)(2)(i) of this section is equal to 11% of the adjusted issue price at the beginning of the accrual period. (Since B is not required to make payments of interest currently and unconditionally at intervals of one year or less over the entire term of the debt instrument, the actual payments of interest are not qualified periodic interest payments within the meaning of § 1.1273–1(b)(1)(ii), and, thus, are original issue discount.

(iii) The gross yield from Blackacre for the fiscal year ending on March 31, 1987 is $13 million; therefore, a payment of $1,300,000 (plus interest of $143,000) is due on June 30, 1987. The amount of original issue discount allocable to the first accrual period is $550,000 (.11 × $5 million). Since all the interest payments under the debt instrument are original issue discount, this amount includes the interest of $143,000 that is actually payable during the first accrual period. The adjusted issue price of the debt instrument at the beginning of the second accrual period, determined under paragraph (e)(2)(ii) of this section, is $4,107,000 (issue price, $5 million, plus original issue discount for the first accrual period, $550,000, minus a payment of $1,443,000).

(iv) The gross yield from Blackacre for the fiscal year ending on March 31, 1988 is $15 million; therefore, a payment of $1,500,000 (plus interest of $348,150) is due on June 30, 1988. The amount of original issue discount allocable to the second accrual period is $451,770 (.11 × $4,107,000). The adjusted issue price of the debt instrument at the beginning of the third accrual period is $2,710,620 (adjusted issue price at beginning of second accrual period, $4,107,000, plus original issue discount for the second accrual period, $451,700, minus a payment of $1,848,150).

(l) [Reserved]

(m) *Purchase*—(1) *Debt instruments issued at a discount after July 18, 1984.* For purposes of section 1272(a) and this section, the term "purchase" means any acquisition of a debt instrument, in which the basis of the debt instrument is not determined in whole or in part by reference to the adjusted basis of the debt instrument in the hands of the persons from whom acquired.

(2) *Debt instruments issued at a discount before July 19, 1984.* For purposes of section 1272(a) and this section, the term "purchase" shall have the same meaning as in paragraph (m)(1) of this section with the additional requirement that the adjusted basis of the debt instrument also not be determined in whole or in part by reference to the adjusted basis of the debt instrument under section 1014 (relating to property acquired from a decedent).

§ 1.1273-1 Determination of amount of original issue discount.

(a) *Definition of original issue discount*—(1) *General rule.* For purposes of sections 1271 through 1275 and the regulations thereunder, the term "original issue discount" means the excess (if any) of [illegible] stated redemption price at maturity (as defined in paragraph (b) of this section) over the issue price (as defined in §§ 1.1273–2 (b) and 1.1274–2(b)).

(2) *Loans with indefinite maturities.* The total amount of original issue discount with respect to a loan with an indefinite maturity date (including a loan payable on demand) is indeterminate. See § 1.1272–1(f)(5)(ii) for rules relating to the determination of yield on certain loans with indefinite maturity dates for purposes of current inclusion of original issue discount. See also § 1.1275–4(d) for rules relating to certain loans calling for payments within a fixed period.

(3) *De minimis rule*—(i) *In general.* If the original issue discount with respect to a debt instrument (other than an installment obligation within the meaning of paragraph (b)(2)(i) of this section) is less than one-fourth of one percent of the stated redemption price at maturity multiplied by the number of full years from the issue date (as defined in section 1275(a)(2) and § 1.1275-1(c)) to final maturity, then the amount of original issue discount shall be considered to be zero.

(ii) *Installment obligations*—(A) *In general.* In the case of an installment obligation, the rule of paragraph (a)(3)(i) of this section shall be applied with the following substitution: In lieu of the number of full years from the issue date to final maturity, there shall be substituted the weighted average maturity of the debt instrument. The weighted average maturity of an installment obligation is the sum of the following amounts (computed for each payment other than a payment of qualified periodic interest described in paragraph (b)(1)(ii) of this section)—

(*1*) The number of full years until a payment is made, multiplied by

(*2*) A fraction, the numerator of which is the amount of the payment and the denominator of which is the stated redemption price at maturity.

(B) *Safe harbor for certain installment obligations.* In the case of an installment obligation that calls for payments of principal no more rapidly than a self-amortizing installment obligation (as defined in paragraph (b)(2)(iii) of this section), in lieu of the rule set forth in paragraph (a)(3)(ii)(B) of this section, the rule set forth in paragraph (a)(3)(i) of this section may be applied by substituting one-sixth of one percent for one-fourth of one percent.

(iii) *Examples.* The provisions of paragraph (a)(3) of this section may be illustrated by the following examples:

Example (1). Assume that a debt instrument providing for a principal payment after ten years of $100 and annual interest payments of $10 is issued for $98. The general rule of paragraph (a)(3)(i) of this section applies because the debt instrument is not an installment obligation. The original issue discount is considered to be zero because the discount of $2 is less than $2.50, which is one-fourth of one percent of the stated redemption price at maturity ($100) multiplied by the number of full years to maturity (10). If this debt instrument were issued for $97.50 or less, however, the original issue discount would not be considered to be zero.

Example (2). Assume that a debt instrument providing for nine annual principal payments of $100, a principal payment of $600 after ten years, and annual interest payments at a rate of 10% of the unpaid principal balance is issued for $1,475. The rule of paragraph (a)(3)(ii)(A) of this section applies because the debt instrument is an installment obligation. The original issue discount is considered to be zero because the discount of $25 is less than $26.25, which is one-fourth of one percent of the stated redemption price at maturity ($1,500) multiplied by the weighted average maturity of the debt instrument determined under paragraph (a)(3)(ii) of this section (7 years).

Example (3). Assume that A issues a debt instrument to B with a 30-year term and a stated principal amount of $100,000, and provides for monthly payments of $1,028.61 over the entire term of the obligation. B charges A four points ($4,000), which are deducted from the total amount of funds disbursed to A. The issue price of the debt instrument is thus $96,000.

Assume further that the stated redemption price at maturity is equal to the stated principal amount. The parties may use the special rule of paragraph (a)(3)(ii)(B) of this section because the debt instrument is a self-amortizing installment obligation. Under this rule, the original issue discount is considered to be zero because the discount of $4,000 is less than $5,000, which is one-sixth of the percent of the stated redemption price at maturity ($100,000) multiplied by the number of full years to maturity (30 years).

Example (4). Assume that a debt instrument is issued for $100,000, providing for a principal payment of $100,000 after 5 years, and calling for annual interest payments of $10,000 for the first 3 years and annual interest payments of $10,600 for the last 2 years. All of the first three interest payments and $10,000 of each of the last two interest payments are qualified periodic interest within the meaning of paragraph (b)(1)(ii) of this section. The remaining $600 of each of the last two interest payments is included in the stated redemption price at maturity. Thus, the rule of paragraph (a)(3)(ii)(A) of this section applies, since the debt instrument is an installment obligation and has a stated redemption price at maturity of $101,200. Pursuant to paragraph (a)(3)(ii)(A) of this section, the weighted average maturity of the debt instrument is 4.994 years [(4 years × $600/$101,200) + (5 years × $100,600/$101,200)]. One-fourth of one percent of the stated redemption price at maturity multiplied by the weighted average maturity ($101,200 × 4.994) is $1,263.50. Since the actual amount of discount, $1,200, is less than this amount, the discount is considered to be zero.

Example (5). A lends B $100,000 for 10 years in consideration for B's note calling for interest to be paid semiannually at a rate of 10% for the first 5 years ($5,000 per semiannual period) and thereafter at a variable rate equal to the prime rate of a designated bank. On the issue date, the prime rate of the designated bank is 10.5%, compounded semiannually. For purposes of applying the *de minimis* rules of paragraph (a)(3) of this section, the debt instrument is treated as though it called for interest at a fixed rate of 10%, compounded semiannually for the first 5 years ($5,000 per period) and at a fixed rate of 10.5%, compounded semiannually for the second 5 years ($5,250 per period). The additional $250 of interest in each of the last ten semiannual periods is not qualified periodic interest within the meaning of paragraph (b)(1)(ii) of this section. The stated redemption price at maturity is thus $102,500 and the total amount of original issue discount is $2,500. The debt instrument is treated as an installment obligation with a weighted average maturity of 9.94 years, calculated as follows:

$250 × 5	=	$1,250
500 × 6	=	3,000
500 × 7	=	3,500
500 × 8	=	4,000
500 × 9	=	4,500
100,250 × 10	=	1,002,500
Total		$1,018,750

($1,018,750/$102,500) = 9.94

One-quarter of one-percent of the weighted average maturity (0.0025 × 9.94) multiplied by the stated redemption price at maturity ($102,500) is $2,546.88. Since the actual amount of discount, $2,500, is less than this amount, the discount is considered to be zero.

(b) *Stated redemption price at maturity*—(1) *Debt instruments other than installment obligations*—(i) *In general.* The term "stated redemption price at maturity" of a debt instrument other than an installment obligation (as defined in paragraph (b)(2)(i) of this section) means the amount payable at maturity as fixed by the last modification of the purchase agreement, including dividends, interest, and any other amounts payable at that time, however designated, other than a qualified periodic interest payment (as defined in paragraph (b)(1)(ii) of this section).

(ii) *Qualified periodic interest payment*—(A) *In general.* The term "qualified periodic interest payment" means any one of a series of payments equal to the product of the outstanding principal balance of the debt instrument and a single fixed rate of interest, or a variable rate tied to a single objective index of market interest rates governed by § 1.1275–5, that is actually and unconditionally payable (as defined in paragraph (b)(1)(iii) of this section), or will be treated as constructively received under section 451 and the regulations thereunder, at fixed, periodic intervals of one year or less during the entire term of a debt instrument (including short periods). A qualified periodic interest payment is not included in determining the stated redemption price at maturity, whether or not payable at maturity.

(B) *Fixed rate followed by variable rate.* Any one of a series of payments based on one fixed rate followed by a variable rate (or another fixed rate determined by reference to a single objective interest index) shall constitute a qualified periodic interest payment, provided that the variable rate (or other fixed rate) is the same as the initial fixed rate on the issue date or as of the first day on which there is a binding written contract for the sale or exchange, whichever is earlier.

(C) *Short periods.* A portion of any payment due at the end of a short period shall be a qualified periodic interest payment only to the extent interest is properly allocable to such period, using the same rate of interest applicable to full periods under the debt instrument. If the debt instrument has original issue discount, such portion shall be calculated in a manner consistent with the determination of yield for the short period under § 1.1272–1(f). A payment at the end of a short final accrual period shall not fail to constitute qualified periodic interest merely because the interval between such payment and the preceding payment differs from the fixed, periodic interval between other payments under the debt instrument. For an example illustrating the provisions of this paragraph (b)(1)(ii)(C), see § 1.1272–1(k), Example (6).

(D) *Short-term obligations.* In the case of a short-term obligation (as defined in section 1283(a)(1)(A)), no payments of interest shall be considered to be qualified periodic interest payments.

(iii) *Unconditionally payable.* Interest is payable unconditionally only if the amount of interest is certain and the failure to pay the interest timely results in consequences to the borrower that are typical in normal lending transactions. For example, interest is payable unconditionally if the failure to pay interest timely results in an acceleration of all amounts due under the debt instrument or if the unpaid interest compounds at a penalty rate that is significantly higher than the interest rate otherwise payable under the terms of the debt instrument. Interest payable upon the occurrence of a contingency (such as the existence of profits) is not unconditionally payable.

(2) *Installment obligations*—(i) *Installment obligation defined.* The term "installment obligation" means a debt instrument providing for the payment of any amount other than a qualified periodic interest payment (as defined in paragraph (b)(1)(ii)) before the final maturity date of the instrument.

(ii) *Stated redemption price at maturity of installment obligation.* The term "stated redemption price at maturity" of an installment obligation means the total of all payments provided by the obligation other than qualified periodic interest payments.

(iii) *Self-amortizing installment obligation defined.* The term "self-amortizing installment obligation" means an installment obligation that calls for equal payments composed of principal and qualified periodic interest that are actually and unconditionally payable (or that will be treated as constructively received under section 451 and the regulations thereunder) at fixed periodic intervals of one year or less during the entire term of the obligation, with no additional payment required at the maturity date of the obligation other than a de minimis amount to adjust for rounding, the timing of payments, and similar circumstances.

(iv) *Stated redemption price at maturity of self-amortizing installment obligations.* The stated redemption price at maturity of a self-amortizing installment obligation (as defined in paragraph (b)(2)(iii) of this section) is the stated principal (as defined in § 1.1274–2(b)(1)) of the obligation. This amount is the sum of all payments made under the debt instrument other than qualified periodic interest payments.

(3) *Debt instruments subject to certain puts and calls.* If a debt instrument contains a put or call option that is not separately tradable and that is presumed exercised under §§ 1.1272–1(f)(4)(iii) or 1.1274–6(f), then the put or call date shall be treated as the maturity date of that debt instrument and the amount payable upon exercise of the put or call shall be treated as the amount payable at maturity. See § 1.1272–1(k), Example (11).

(4) *Examples.* The provisions of paragraph (b) of this section may be illustrated by the following examples:

Example (1). A debt instrument is issued on October 1, 1985, which provides for a payment of $50,000 on December 31, 1994. Interest is payable currently and unconditionally (within the meaning of paragraph (b)(1)(iii) of this section) at a single fixed rate of 10%, compounded semiannually. The interest payment due on December 1, 1985, is $1,250. This payment and each subsequent payment of $2,500 per semiannual period are qualified periodic interest payments within the meaning of paragraph (b)(1)(ii) of this section. Thus, under § 1.1273–1(b)(1)(i), the stated redemption price at maturity is $50,000.

Example (2). A debt instrument is issued for $100,000, on January 1, 1986. The debt instrument calls for payments of $5,000 of interest on January 1 of each year from 1987 through 1995, and a final payment of $200,000 on January 1, 1996. The $5,000 payments in 1987 through 1995 and $5,000 of final payment in 1996 are qualified periodic interest payments within the meaning of paragraph (b)(1)(ii) of this section. Thus, the stated redemption price at maturity is $195,000.

Example (3). A debt instrument with a term of 5 years is issued on January 1, 1986, for a stated principal amount of $500,000. The debt instrument provides for annual payments of $145,641.77 for each of 5 years. Each payment consists of interest at 14%, compounded annually on the unpaid principal balance, and principal as follows:

Year	Principal	Interest payments	Total
1	$75,641.77	$70,000.00	$145,641.77
2	86,231.62	59,410.15	145,641.77
3	98,304.05	47,337.72	145,641.77
4	112,066.62	33,575.15	145,641.77
5	127,755.94	17,885.83	145,641.77
	$500,000.00	$228,208.85	$728,208.85

The payments of interest are payable currently and unconditionally at fixed, periodic intervals of one year during the entire term of the debt instrument. Therefore, they are qualified periodic interest payments. Because the debt instrument provides for equal payments of principal and qualified periodic interest, and because no additional payment is required at the maturity date, the debt instrument is a self-amortizing installment obligation as defined in paragraph (b)(2)(iii) of this section. The stated redemption price at maturity is equal to the stated principal amount of $500,000. This amount can also be derived by subtracting from the total payments of $728,208.87, the $228,208.87 of qualified periodic interest payments.

Example (4). A debt instrument is issued on January 1, 1986, for cash of $10,000, maturing on December 31, 1989, and providing for payments of principal at the end of the second and fourth years of $5,000 each. Payments of interest are provided currently and unconditionally at the end of the first and second years of $1,200 each, and at the end of the third and fourth years of $600 each. The debt instrument is an installment obligation as defined in paragraph (b)(2)(i) of this section. Each payment of interest represents the product of a single, fixed rate of 5% on the outstanding principal balance. Each such payment is, therefore, a qualified periodic interest payment, and is not included in the stated redemption price at maturity under the definition set forth in paragraph (b)(2)(ii) of this section. Under that definition the stated redemption price of an installment obligation is the total of all payments other than qualified periodic interest payments. That total is $10,000.

§ 1.1273–2 Determination of issue price.

(a) *Definitions*—(1) *Property.* The determination of the issue price of a debt instrument depends on whether it is issued for property. For purposes of section 1273, this section, and § 1.1273–1, the term "property" includes debt instruments, investment units, services and the right to use property, but does not include money.

(2) *Publicly offered debt instruments.* The determination of the issue price of a debt instrument also depends on whether it is publicly offered. An issue of debt instruments is publicly offered if it—

(i) Is registered with the Securities and Exchange Commission;

(ii) Would be required to be registered but for the identity of the issuer; or

(iii) Is exempt from registration under section 3 of the Securities Act of 1933.

(b) *Debt instruments not issued for property*—(1) *Publicly offered debt instruments*—(i) *Debt instruments other than Treasury securities.* In the case of an issue of debt instruments other than Treasury securities that is publicly offered (as defined in paragraph (a)(2) of this section) and not issued for property, the term "issue price" under section 1273(b)(1) means the initial offering price to the public at which price a substantial amount of the debt instruments was sold. For this purpose, the term "the public" does not include bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters or wholesalers. The issue price generally is the first price at which debt instruments included in the issue were sold to the public and the issue price will not change if part of the issue is subsequently sold at a different price.

(ii) *Treasury securities.* In the case of an issue of Treasury securities, the issue price is the average price of the debt instruments sold.

(2) *Debt instruments not publicly offered.* In the case of an issue of debt instruments that is not publicly offered and is not issued for property, the issue price of each debt instrument is the price paid by the first buyer of the particular debt instrument, regardless of the amount paid for the remainder of the issue. The rule stated in this paragraph (b)(2) for determining issue price also applies to loans between natural

persons. For rules relating to the treatment of certain cash payments incident to a lending transaction with respect to the determination of issue price, see paragraph (f) of this section.

(3) *Below-market loans subject to section 7872(b).* (i) *In general.* In the case of a below-market loan subject to section 7872(b) (a term loan other than a gift loan), the issue price otherwise determined under this section shall be reduced by the excess amount determined under section 7872(b)(1).

(ii) *Examples.* The provisions of paragraph (b)(3)(i) of this section may be illustrated by the following example:

Example. (i) B is an employee of X Corporation. On July 1, 1986, X loans $80,000 to B. B gives X a note for $100,000, payable in 5 years. Assume that the Federal mid-term rate for July 1986 is 10%, compounded annually. Under the provisions of section 1273(b)(2) and § 1.1273-2(b)(2), the issue price of the note, but for paragraph (b)(3)(i) of this section, would be $80,000.

(ii) The amount loaned from X to B is $80,000. The present value of the payment that is required to be made under the terms of the loan, discounted at 10%, is $62,092.13. Thus, the excess amount described in section 7872(b)(1) is $17,907.87. The issue price of B's debt instrument is thus $62,092.13 ($80,000 paid by X for the debt instrument minus the excess amount of $17,907.87 determined under section 7872(b)(1)).

(c) *Debt instruments issued for property after May 27, 1969*—(1) *Public trading.* If a debt instrument is issued for property after May 27, 1969, and the debt instrument is part of an issue a portion of which is traded on an established securities market, then the issue price of that debt instrument shall be its fair market value determined as of the first date after the issue date that the debt instrument is traded on an established securities market. If a debt instrument (other than a debt instrument described in the preceding sentence) is issued for property after May 27, 1969, and the property is stock or securities that are traded on an established securities market, the issue price of the debt instrument shall be the fair market value of the stock or securities determined as of the issue date of the debt instrument. The fair market value of property for purposes of this paragraph (c)(1)(i) shall be determined as provided in § 20.2031-2 of this chapter (Estate Tax Regulations). If the trading price of the property fails to reflect accurately the value of a debt instrument issued for publicly traded property after May 8, 1986, because of extraordinary circumstances such as the existence of control premium or blockage discount, the issue price of a debt instrument exchanged for such property is determined under section 1274 and the regulations thereunder. Property shall be treated as traded if it is traded on an established securities market on or within 10 trading days after the date it is issued. Trading days are those days on which an established securities market is open. For purposes of this paragraph (c)(1)(i), the term "established securities market" shall have the same meaning as in § 1.453-3(d)(4) (relating to limitations on installment method for purchaser evidences of indebtedness payable on demand or readily tradable). A debt instrument not traded on an established securities market (and not part of an issue a portion of which is so traded) shall not be treated as property that is so traded even if it is convertible into property which is so traded.

(2) *No public trading*—(i) *Debt instruments issued after December 31, 1984.* If a debt instrument is issued after December 31, 1984 and is neither a debt instrument to which section 1273(b) (1), (2), or (3) or paragraph (b) or (c)(1) of this section applies, nor a debt instrument to which section 1274 applies (see § 1.1274-1), then the issue price of the debt instrument under section 1273(b)(4) and this section shall be its stated redemption price at maturity.

(ii) *Debt instruments issued before January 1, 1985.* If a debt instrument is issued for property before January 1, 1985, and is not a debt instrument to which paragraph (c)(1)(i) of this section applies, the issue price of the debt instrument shall be the stated redemption price at maturity. In this case, however, there may be an amount treated as unstated interest under section 483 as it existed prior to its amendment by section 41(b) of the Tax Reform Act of 1984, 98 Stat. 494, and the regulations thereunder. See 26 CFR 1.483-1 and 1.483-2 (revised as of April 1, 1985).

(3) *Reorganization.* For special rules relating to debt instruments issued in a reorganization, see § 1.1275-2(a).

(d) *Investment units issued after May 8, 1986*—(1) *Definition.* An investment unit consists of a debt instrument and a property right, such as a security or option (other than certain options described in § 1.1272-1(f)(4)).

(2) *Allocation of issue price*—(i) *In general.* The issue price of the investment unit shall be allocated between the debt instrument and the property right on the basis of the fair market value of each element of the unit.

(ii) *Publicly-traded debt instrument.* If the debt instrument issued as part of an investment unit is publicly traded, the issue price of the debt instrument shall equal the initial trading price of the debt instrument.

(iii) *Publicly-traded property right.* If the property right issued as part of an investment unit is publicly traded and the debt instrument is not publicly traded, the issue price of the debt instrument shall equal the price paid for the investment unit less the initial trading price of the property right.

(iv) *Nonpublicly-traded property right and debt instrument.* If neither the property right nor the debt instrument issued as part of an investment unit is publicly traded, the issue price of the debt instrument shall equal the present value of all payments under the debt instrument, discounting at a rate agreed to by the issuer and the holder, based on the original yields of other debt instruments with similar maturities and security issued within the previous six months by the issuer. If no such debt instruments were issued, the issuer and the holder may look to comparable debt instruments of other issuers, taking into account (with respect to both the debt instrument in question and comparable debt instruments) the solvency of the issuer, the nature of the issuer's trade or business, the presence and nature of security for the debt instrument, the geographic area in which the loan is made, and any other factors relevant in the circumstances. A debt instrument which is convertible into stock or another debt instrument must not be used as a comparable debt instrument (except where the investment unit contains a debt instrument convertible into stock or another debt instrument). In no event may the yield agreed to by the issuer and the holder be less than the applicable Federal rate on the issue date of the investment unit.

(e) *Convertible debt instruments.* The issue price of a debt instrument which is convertible into stock or another debt instrument of the issuer shall include any amount paid with respect to the conversion privilege.

(f) *Treatment of certain cash payments incident to lending transactions*—(1) *Applicability.* The provisions of paragraph (f) of this section shall apply with respect to cash payments incident to private lending transactions (including seller financing), other than points that are deductible by the borrower under section 461(g)(2). The tax treatment to the lender of any payment to the lender that, when added to other original issue discount arising from the transaction (determined without regard to such payments), produces a total amount of original issue discount which is *de minimis* under the rules of § 1.1273-1(a)(3), shall be governed by principles of tax law other than sections 1272 and 1273 and the regulations thereunder.

(2) *Payments from borrower to lender.* In a lending transaction to which section 1273(b)(2) applies, a payment from the borrower to the lender (other than a payment for services provided by the lender, such as commitment fees or loan processing costs) shall reduce the issue price of the debt instrument evidencing the loan. In a transaction to which section 1274 applies, a payment from the buyer-borrower to the seller-lender designated as points or as interest shall reduce the stated principal amount of the debt instrument evidencing the loan. In addition, the purchase price of the property shall include the amount of any payment from the buyer-borrower to the seller-lender, regardless of how designated.

(3) *Payments from lender to borrower.* A payment from the lender to the borrower in a lending transaction (including a deemed payment within the meaning of paragraph (f)(4) of this section) shall be treated as an amount loaned.

(4) *Payments between lender and third party.* If, as part of a lending transaction, a party other than the borrower (the third party) makes a payment to the lender, that payment may be treated in appropriate circumstances as made from the third party to the borrower followed by a payment in the same amount from the borrower to the lender and governed by the provisions of paragraph (f)(2) of this section. Section 461(g)(2) shall not apply to any deemed payment from the borrower to the lender. Similarly, if the lender makes a payment to a thrid party, that payment may be treated as an additional amount loaned to the borrower and then paid by the borrower to the third party. The character of the deemed payment between the borrower and the third party shall depend on the substance of the transaction.

(5) *Examples.* The provisions of paragraph (f) of this section may be illustrated by the following examples:

Example (1). A lends $100,000 to B for a term of 10 years. At the time the loan is made, B pays $4,000 in points to A. Assume that the points are not deductible by B under section 461(g)(2). The issue price of B's debt instrument is $96,000. Since the $4,000 constitutes more than a *de minimis* amount of original issue discount, under paragraph (f)(2) of this section, the points are accounted for by both A and B as original issue discount under sections 1272 and 1273 and the regulations thereunder.

Example (2). (i) A sells property to B for $1,000,000. In consideration therefor, B gives A $300,000 cash and a $700,000 debt instrument with a term of 5 years, calling for semiannual payments of interest at a rate of 8.5%. In addition to the cash down payment, B pays A $14,000 designated as points on the loan.

(ii) The stated principal amount of B's debt instrument, under paragraph (f)(2) of this section, is $686,000 ($700,000 minus $14,000). Assuming a test rate of 9%, compounded semiannually, the testing amount for B's debt instrument under § 1.1274–3 is $686,158. Thus, under § 1.1274–2, the issue price of B's debt instrument is the stated principal amount of $686,000. B's basis in the property purchased is thus $1,000,000 ($686,000 debt instrument plus $314,000 cash payments).

Example (3). A sells Blackacre to B for $500,000. B makes a cash down payment of $100,000 and borrows $400,000 of the purchase price from a lender, L, repayable in annual installments over a term of 15 years calling for interest at a rate of 9%. As part of the transaction, A makes a payment of $8,000 to L to facilitate the loan to B. Under the provisions of paragraph (f)(2) and (4) of this section, B is treated as having made an $8,000 payment directly to L and a down payment of only $92,000 to A. The payment to L reduces the issue price of B's debt instrument to $392,000. B's basis in Blackacre is $492,000 ($392,000 debt instrument plus $100,000 cash payments). Since the payment to L represents a *de minimis* amount of original issue discount under § 1.1273–1(a)(3), L must account for $8,000 payment without regard to the original issue discount rules. B, however, must account for the payment as original issue discount pursuant to the provisions of § 1.163–7(d).

Example (4). The facts are the same as in example (3), except that the payment from A to L is $20,000. Under the provisions of paragraph (f)(2) and (4) of this section, B is treated as having made a $20,000 payment to L and an $80,000 down payment to A. The issue price of the debt instrument is thus reduced to $380,000. B's basis in Blackacre is $480,000 ($380,000 debt instrument and $100,000 cash payments). B and L both account for the payment as original issue.

Example (5). The facts are the same as in example (4), except that the $20,000 payment is made from L to A. Under paragraph (f) (3) and (4) of this section, L is treated as having made a loan of $420,000 to B and B is treated as having purchased Blackacre for $520,000. Thus, the issue price of B's debt instrument is, under § 1.1273–2(b)(2), the amount loaned, or $420,000. B's basis in Blackacre is $520,000 ($420,000 debt instrument plus $100,000 cash payment).

Example (6). (i) S owns Blackacre, subject to a mortgage held by L with a remaining principal amount of $1,000,000. S sells Blackacre to B in exchange for $2,000,000 cash and B's agreement to assume S's debt to L. As part of the transaction, S, B, and L jointly agree that the terms of the debt instrument will be modified in such a way as to produce an issue price for the modified debt instrument of $900,000. In addition, L agrees to make a cash payment to B of $100,000.

(ii) Under § 1.1274–7, S's debt to L is treated as having been exchanged for a new debt instrument (in a transaction to which section 1274 applies) immediately prior to the sale to B. B is treted as assuming this new debt instrument. With respect to the exchange of debt instruments, B is a third party. Thus, the $100,000 cash payment from L to B is treated as having been made from L to S and then from S to B. The latter payment reduces the net cash payment from B to S to $1,900,000.

(iii) The new debt instrument is treated as having been issued for the old debt instrument plus $100,000 cash. Since the issue price of the new debt instrument is $900,000, the portion of the issue price of the new debt instrument attributable to the old debt instrument is $800,000. Thus, S is treated as having repaid the old debt instrument for $800,000, and, under section 108, has cancellation of indebtedness income of $200,000.

§ 1.1274–1 Debt instruments to which section 1274 applies.

(a) *Types of debt instruments to which section 1274 applies.*—(1) *In general.* Subject to the exceptions and limitations set forth in paragraph (b) of this section, section 1274 and this section apply to any debt instrument given in consideration for the sale or exchange of property unless (i) the debt instrument provides for interest to be paid currently at a constant rate over its entire term, and (ii) the debt instrument provides for adequate stated interest. For purposes of section 1274, the term "sale or exchange" means any transaction treated as a sale or exchange for tax purposes. For purposes of section 1274, the term "property" includes debt instruments and investment units, but does not include money, services, or the right to use property. For the definition of the term "debt instrument," see section 1275(a)(1) and § 1.1275–1(b). For the treatment of debt instruments to which section

1274 and this section apply, see § 1.1274-2. For the treatment of certain payments for the use of property or services, see sections 404 and 467.

(2) *Interest to be paid currently at a constant rate.* A debt instrument provides for interest to be paid currently at a constant rate if all interest provided for in the debt instrument is payable at a single fixed or variable rate and the interest is payable unconditionally and at least annually. For the meaning of the term "payable unconditionally," see § 1.1273-1(b)(1)(iii).

(3) *Adequate stated interest.* To determine if a debt instrument provides for adequate stated interest, the test rate of interest applicable to the debt instrument must be determined. In general, if a debt instrument calls for interest over its entire term at a stated rate (with an appropriate compounding period) no lower than the test rate of interest, the debt instrument provides for adequate stated interest. Special rules, however, are provided for the application of section 1274 to debt instruments involved in potentially abusive situations. See § 1.1274-4(g) for the meaning of the term "potentially abusive situation." For rules relating to the determination of adequate stated interest, see § 1.1274-3. For special rules relating to debt instruments calling for variable rates of interest or for contingent interest, see § 1.1274-3(d).

(b) *Exceptions and limitations to the application of section 1274*—(1) *Debt instruments maturing in 6 months or less.* Section 1274 does not apply to a debt instrument under which none of the payments are due more than six months after the date of the sale or exchange.

(2) *Sales of farms for $1,000,000 or less by certain sellers*—(i) *In general.* Except as provided in paragraph (b)(2)(ii) of this section, section 1274 does not apply to any debt instrument arising from the sale or exchange of a farm (within the meaning of section 6420(c)(2) and the regulations thereunder)—

(A) By an individual, estate, or testamentary trust,

(B) By a corporation which as of the date of the sale or exchange is a small business corporation as defined in section 1244(c)(3) and the regulations thereunder, or

(C) By a partnership which as of the date of the sale or exchange meets requirements similar to those of section 1244(c)(3).

For the purposes of paragraph (b)(2)(i)(C) of this section, a partnership is considered to have met requirements similar to those of section 1244(c)(3) if the partnership is a domestic partnership, and the equity capital invested in the partnership does not exceed $1,000,000. For purposes of the preceding sentence, the equity capital invested in a partnership is the aggregate of all contributions of money to the partnership by its partners, and of all bases to the partnership of property contributed (reduced by the amount of any liability to which the contributed property is subject or which is assumed by the partnership with respect to the contributed property) to it by its partners as determined under section 723. The amount of the equity capital invested in a partnership is not reduced by the amount of any distribution even though the distribution may be considered a capital distribution.

(ii) *Limitation.* Paragraph (b)(2)(i) of this section applies to a sale or exchange of a farm only if it can be determined at the time of the sale or exchange that the sales price cannot exceed $1,000,000, even if the sales price eventually paid for the farm is less than $1,000,000. The determination whether the sales price cannot exceed $1,000,000 is made without regard to any other exception described in paragraph (b) of this section. In addition, the sales price is determined without regard to section 1274 and without regard to any stated interest. The term "sale price" includes the amount of any liability included in the amount realized from the sale or exchange (see § 1.1001-2). For purposes of the determination whether the sales price of a farm cannot exceed $1,000,000, all sales and exchanges which are part of the same transaction (or are part of a series of related transactions) shall be aggregated in accordance with the rules of § 1.1274A-1(d).

(3) *Sales of principal residences.* Section 1274 does not apply to any debt instrument arising from the sale or exchange by an individual of the individual's principal residence (within the meaning of section 1034). Whether the principal residence sold or exchanged by the individual is to be used as the principal residence of the buyer does not affect this determination.

(4) *Sales involving total payments of $250,000 or less*—(i) *In general.* Section 1274 does not apply to any debt instrument arising from the sale or exchange of property if the sum of the following amounts does not exceed $250,000 (determined without regard to any other exception prescribed in paragraph (b) of this section):

(A) The aggregate amount of the payments (including interest and principal) due under the debt instrument and under all other debt instruments received as consideration for the sale or exchange, and

(B) The aggregate value of any other consideration (including any liability assumed or taken subject to) to be received for the sale or exchange.

(ii) *Value of consideration other than the debt instrument.* For purposes of paragraph (b)(4)(i)(B) of this section, any consideration (other than a liability assumed or taken subject to) is taken into account at its fair market value. In the case of any liability assumed or taken subject to, the outstanding principal balance or revised issue price (in the case of an obligation originally issued at a discount) of the obligation assumed or taken subject to is taken into account.

(iii) *Aggregation of transactions.* For purposes of paragraph (b)(4) of this section, all sales or exchanges which are part of the same transaction (or a series of related transactions) shall be aggregated in accordance with the rules of § 1.1274A-1(d).

(iv) *Time when $250,000 limitation applied.* The determination of the amount of payments due under all debt instruments and the amount of other consideration to be received is made as of the date of the sale or exchange, or, if earlier, the contract date as defined in § 1.1274-8(e)(1)(ii). If the precise amount due under any debt instrument or the precise amount of any other consideration to be received cannot be determined as of the date of the sale or exchange, the exception described by paragraph (b)(4) of this section applies only if it can be determined that the maximum of the aggregate amount of payments due under the debt instruments and other consideration to be received cannot exceed $250,000.

(5) *Publicly traded debt instruments or property.* Section 1274 does not apply to any debt instrument to which section 1273(b)(3) applies. Thus, section 1274 does not apply to any publicly traded debt instrument or to any debt instrument issued in consideration for the sale or exchange of publicly traded property.

(6) *Certain sales of patents.* Section 1274 does not apply to any amount payable with respect to a transfer by an individual holder described in section 1235 (relating to sales or exchanges of patents) that is contingent on the productivity, use, or disposition of the property transferred.

(7) *Transactions involving personal use property*—(i) *Treatment of issuers.* Section 1274 does not apply to any borrower (issuer) under a debt instrument given in consideration for the sale or exchange of property that is personal use property (within the meaning of section 1275(b)(3)) in the

hands of the issuer. Thus, the tax treatment of the issuer of any amount payable under such a debt instrument is determined without regard to the provisions of section 1274 and the regulations thereunder.

(ii) *Treatment of certain holders.* Section 1274 does not apply to any lender (holder) of a debt instrument that (A) is given in consideration for the sale or exchange of property that is personal use property (within the meaning of section 1275(b)(3)) in the hands of the issuer and (B) is also a loan described in section 7872(c)(1)(A) (relating to gift loans), 7872(c)(1)(B) (relating to compensation-related loans), or 7872(c)(1)(C) relating to corporation-shareholder loans). For rules relating to the treatment of loans described in the preceding sentence, see section 7872 and the regulations thereunder.

(8) *Transactions involving certain demand loans.* Section 1274 does not apply to any debt instrument that evidences a demand loan (within the meaning of section 7872(f)(5) described in section 7872(c)(1)(A) (rlating to gift loans), 7872(c)(1)(B) (relating to compensation-related loans), or 7872(c)(1)(C) (relating to corporation-shareholder loans). For rules relating to the treatment of loans described in the preceding sentence, see section 7872 and the regulations thereunder.

(9) *Sales or exchanges to which section 483(e) and § 1.483–4(b)(2) apply.* Section 1274 does not apply to any debt instrument to which section 483(e) and § 1.483–4(b)(2) (relating to qualified sales) apply.

(10) *Certain transfers subject to section 1041.* Section 1274 does not apply to any debt instrument issued in consideration for a transfer of property subject to section 1041 (relating to transfers of property between spouses or incident to divorce).

(c) *Modified debt instruments*—(1) *In general.* For purposes of section 1274, if the issuer and holder (or a successor to either) modify a debt instrument, the modified debt instrument shall be treated as a new debt instrument given in consideration for the unmodified debt instrument (the old debt instrument). Thus, for purposes of section 1274 and the regulations thereunder, the old debt instrument is treated as property. A new debt instrument shall not be eligible for the election to use the cash method of accounting described in § 1.1274A–1(c) unless the old debt instrument was a cash method debt instrument. A debt instrument has been modified if the terms of the new debt instrument differ "materially either in kind or in extent," within the meaning of § 1.1001–1(a), from the terms of the old debt instrument. For this purpose, a payment to or from the lender (or a successor) not provided for in the debt instrument shall be treated as a modification of the debt instrument. For rules governing the treatment of payments made in connection with the issuance of a debt instrument, see § 1.1273–2(f). This paragraph (c)(1) shall not apply to modifications described in section 106 of Pub. L. No. 99–121.

(2) *Example.* The provisions of paragraph (c)(1) of this section may be further illustrated by the following example:

Example: On January 1, 1985, B issues a ten-year debt instrument to A for $8,000,000. The debt instrument, as originally issued, provides for annual interest payments at 15 percent. On January 1, 1986, A and B agree to modify the debt instrument by lowering the interest rate to 9 percent. The change in interest rate constitutes a modification under § 1.1001–1(a). Because the debt instrument has been modified, the modified debt instrument is treated as a new debt instrument given by B in consideration for the old debt instrument.

(d) *Excessive interest.* If a debt instrument given in consideration for the sale or exchange of property calls for interest at a rate that, in light of the terms of the debt instrument and the creditworthiness of the borrower, is clearly greater than the arm's-length rate of interest that would have been charged in a cash lending transaction (that is, one not involving a sale of property) between the same two parties, the Commissioner may recharacterize a portion of the stated interest as additional purchase price. The portion of interest to be recharterized as additional purchase price shall be determined in a manner consistent with section 1274 and may be based either on the fair market value of the property sold or on the arm's-length rate described in the preceding sentence. In determining whether recharacterization is appropriate, the Commissioner may consider the relation between the tax advantage derived by the borrower from the overstatement of interest and the tax detriment (if any) to the seller from such overstatement.

(e) *Effective date: transitional rule*—(1) *General rule.* Section 1274 and the regulations thereunder apply, except as otherwise provided in this paragraph (e), to any debt instrument given in consideration for a sale or exchange of property if the sale or exchange occurs after December 31, 1984, unless the sale or exchange is made pursuant to a written contract (including an irrevocable written option) which was binding on March 1, 1984. For this purpose, a sale or exchange is not made pursuant to a written contract which was binding on March 1, 1984, if a substantial modification (within the meaning of § 1.1274–6(e)(1)(iii)) in the terms of the contract occurs after March 1, 1984 and before the sale or exchange. Section 1274 and the regulations thereunder shall not apply to any modifications of a debt instrument arising from a sale or exchange unless the debt instrument arises from a sale or exchange to which section 1274 and the regulations thereunder apply (within the meaning of this paragraph (e)) or the debt instrument is assumed or taken subject to in connection with, and the modification is part of, such a sale. For rules relating to sales or exchanges occurring before January 1, 1985, and sales or exchanges pursuant to a written contract (including an irrevocable written option) which was binding on March 1, 1984, and modification of debt instruments to which section 1274 and the regulations thereunder do not apply by reason of the preceding sentence, see section 44(b)(3) of the Tax Reform Act of 1984, section 483 as in effect before its amendment by section 41(b) of the Tax Reform Act of 1984, and 26 CFR 1.483–1 and 1.483–2 (revised as of April 1, 1985).

(2) *Certain sales or exchanges occurring before July 1, 1985 by cash method buyers and sellers.* Section 1274 does not apply to any debt instrument arising from a sale or exchange of property (other than new section 38 property within the meaning of section 48(b) and the regulations thereunder) occurring before July 1, 1985, if—

(i) The property was used in the active business of farming,

(ii) The stated principal amount of the debt instrument does not exceed $2,000,000, and

(iii) The interest (including unstated interest under section 483) on the debt instrument arising from the sale or exchange is taken into account by the buyer and the seller on the cash receipts and disbursements method of accounting.

All sales or exchanges (other than sales or exchanges of new section 38 property) which are part of the same transaction (or a series of related transactions) shall be aggregated in accordance with the rules of § 1.1274A–1(d), and all debt instruments arising from aggregated sales or exchange shall be treated as one debt instrument. The term "farming" has the same meaning as that term has in section 464(e)(1).

(f) *Examples.* The provisions of this section may be illustrated by the following examples:

Example (1). On July 1, 1985, A, an individual, sells to B land used as a farm within the meaning of section 6420(c)(2). In consideration for the sale, B makes a $250,000 down payment and issues a debt instrument calling for a single $500,000 payment due in 10 years unless profits from the land in each of the 10 years preceding maturity of the debt instrument exceeds a specified amount, in which case B is to make a payment of $800,000. No interest is provided for in the debt instrument. Even though the total payments ultimately payable under the contract may be less than $1,000,000, at the time of the sale or exchange it cannot be determined that the sales price cannot exceed $1,000,000. Thus, the sale of the land used as a farm is not an excepted transaction described in paragraph (b)(2) of this section.

Example (2). On July 1, 1985, A, an individual, sells land (not used as a farm within the meaning of section 6420(c)(2) and the regulations thereunder) to A's child B for $650,000. In consideration for the sale, B issues a debt instrument to A that calls for a payment of $500,000 and a second debt instrument that calls for a payment of $150,000. No other consideration is given. Both debt instruments are due in 10 years. The debt instruments do not provide for interest. The $500,000 debt instrument is subject to section 483(e) and § 1.483–4(b)(2), and is accordingly covered by the exception from section 1274 described in paragraph (b)(9) of this section. Since the exception from section 1274 for debt instruments subject to section 483(e) and § 1.483–4(b)(2) apply to the extent of $500,000, the $150,000 debt instrument is subject to section 1274 even though the total payments under this debt instrument do not exceed $250,000 because the aggregate amount of payments due under the sale, determined without regard to the exception described in paragraph (b)(9) of this section, exceeds $250,000.

Example (3). The facts are the same as in example (2), except that the land sold was land used as a farm within the meaning of section 6420(c)(2) and the regulations thereunder, and was sold for a debt instrument calling for a single payment of $500,000 and a second debt instrument calling for a single payment of $700,000. Both debt instruments are due in 10 years. In this case, the $500,000 debt instrument is subject to section 483(e) and § 1.483–4(b)(2), and is accordingly covered by the exception from section 1274 described in paragraph (b)(9) of this section. Nevertheless, section 1274 applies to the $700,000 debt instrument because this debt instrument arose from a sale of a farm the sales price of which exceeds $1,000,000.

Example (4). F is an entity that is exempt from taxation under section 501(c) of the Code. F holds stock in X Corporation, a privately held company. On July 1, 1986, F sells its stock in X corporation to A, an individual with a regular income flow and a high credit rating who is subject to the highest rate of taxation. In partial consideration for the sale, A gives F a debt instrument with a principal amount of $600,000, calling for interest at a rate of 22 percent. The Commissioner may determine that interest at 22 percent is excessive and recharacterize a portion of the stated interest as additional purchase price.

§ 1.1274-2 Treatment of debt instruments to which section 1274 applies.

(a) *In general.* If section 1274 applies to a debt instrument as provided in § 1.1274–1, section 1274 and this section determine the issue price of the debt instrument for the purpose of sections 1271, 1272, and 1273. The issue price as determined under section 1274 and these regulations generally determines the sales price (in whole or in part) of any property acquired for the debt instrument. Thus, in determining the amount realized from the sale or exchange of property, the amount realized that is attributable to the debt instrument is generally the issue price of the debt instrument. Similarly, in determining the cost basis of property acquired for the debt instrument, the amount of the cost basis of the property attributable to the debt instrument is generally the issue price of the debt instrument. For rules relating to the determination of basis of property in certain transactions between related parties, see § 1.1012–2.

(b) *Issue price*—(1) *Debt instruments that provide for adequate stated interest; stated principal amount.* If section 1274 applies to a debt instrument that provides for adequate stated interest, the issue price of the debt instrument is the stated principal amount of the debt instrument. For purposes of section 1274, the stated principal amount of a debt instrument is the aggregate amount of all payments due under the debt instrument excluding any amount of interest provided for in the debt instrument.

(2) *Debt instruments that do not provide for adequate stated interest; imputed principal amount.* If section 1274 applies to a debt instrument that does not provide for adequate stated interest, the issue price of the debt instrument is the imputed principal amount of the debt instrument. For rules relating to the determination of the imputed principal amount of a debt instrument, see § 1.1274–4.

§ 1.1274-3 Determination whether a debt instrument provides for adequate stated interest.

(a) *In general.* This section prescribes rules for determining whether a debt instrument provides for adequate stated interest. The rules prescribed by this section apply to any debt instrument whether the debt instrument calls for the payment of principal at maturity, the periodic payment of principal, or irregular payments of principal. A debt instrument generally provides for adequate stated interest if it calls for interest on the outstanding principal balance at a rate (with an appropriate compounding period) at least equal to the test rate of interest. For rules relating to the determination of the test rate of interest and rules relating to an appropriate compounding period, see paragraph (e) of this section. Paragraph (b) of this section provides rules for determining adequate stated interest (except with respect to debt instruments involved in a potentially abusive situation) if the debt instrument provides for a stated rate of interest. Paragraph (c) of this section provides rules for determining adequate stated interest in the case of debt instruments that do not satisfy the requirements of paragraph (b) of this section. For special rules relating to debt instruments calling for variable rates of interest or for contingent interest, see paragraph (d) of this section.

(b) *Certain debt instruments that provide for a stated rate of interest)*—(1) *In general.* A debt instrument provides for adequate stated interest if—

(i) The debt instrument provides for interest on the outstanding principal balance of the debt instrument (the stated rate of interest) at a fixed rate;

(ii) The stated rate of interest is no lower than the test rate of interest (based on the appropriate compounding period);

(iii) The debt instrument requires interest to be paid or compounded at the end of each compounding period for the entire term of the debt instrument, and

(iv) The debt instrument is not issued in a potentially abusive situation as defined in § 1.1274–4(g).

For rules relating to debt instruments that do not satisfy the requirements of this paragraph (b)(1), see paragraph (c) of this section.

(2) *Interest payable for a short period*—(i) *In general.* The stated rate of interest is a fixed rate within the meaning of paragraph (a)(1) of this section only if it also applies for short periods (that is, any period shorter than the compounding period on which the test rate of interest is based). For this purpose, adequate stated interest for a short period may be determined by either of the two alternative methods prescribed by this paragraph (b)(2)(i) or by any other reasonable method. The methods prescribed by this paragraph (b)(2)(i) are the exact method and the approximate method. An example of another reasonable method is monthly compounding which reflects compounding at intervals of one month with simple interest within a month. If a debt instrument has original issue discount, the choice of any method

permissible under this paragraph (b)(2) requires a corresponding choice for purposes of determining the amount of original issue discount includible under section 1272 for the short period.

(ii) *Exact method.* The exact method reflects daily compounding of interest. Under this method, an amount of interest payable on an outstanding principal amount (P) for a short period is equal to the result of the following formula:

$I = P \times [(1 + i/k)^f - 1]$

In which:

I = Interest payable for the short period

i = The stated rate of interest expressed as a decimal

k = The number of compounding periods on which the test rate of interest is based contained in a year

f = A fraction, the numerator of which is the length of the short period, and the denominator of which is the length of the compounding period on which the test rate of interest is based

For illustrations of the application of the formula for the exact method, see examples (3) and (5) of paragraph (b)(3) of this section.

(iii) *Approximate method.* The approximate method is also provided for the convenience of taxpayers who do not desire to use the exact method. The approximate method reflects simple interest within any compounding period and always produces an amount of interest for the short period that is slightly higher than that produced under the exact method. Under this method, the amount of interest payable on an outstanding principal amount for a short period is determined by multiplying the amount of stated interest for a full period by a fraction, and numerator of which is equal to the length of the short period and the denominator of which is the length of a full period. Thus, the amount of interest payable on an outstanding principal amount (P) for a short period is equal to the result of the following formula:

$I = P \times (i/k) \times f$

In which:

I = Interest payable for the short period

i = The stated rate of interest expressed as a decimal

k = The number of compounding periods on which the test rate of interest is based contained in a year

f = A fraction, the numerator of which is the length of the short period, and the denominator of which is the length of the compounding period on which the test rate of interest is based

For illustrations of the application of the formula for the approximate method, see examples (4), (6) and (7) of paragraph (b)(3) of this section.

(3) *Examples.* The provisions of paragraph (b) of this section may be illustrated by the following examples:

Example (1). Assume that a debt instrument issued in consideration for the sale of nonpublicly traded property calls for the payment of a principal amount of $1,000,000 at the end of a 10-year term and 20 semiannual interest payments of $60,000 each on the principal balance of the debt instrument. The appropriate compounding period is semiannual. Assume that the test rate of interest is 12 percent, compounded semiannually. The debt instrument provides for adequate stated interest because the debt instrument provides for interest equal to the test rate of 12 percent payable semiannually, the compounding period for the test rate.

Example (2). The facts are the same as in example (1), except that the debt instrument calls for 10 annual interest payments of $123,600 each. The appropriate compounding period for the test rate is annual. The debt instrument provides for adequate stated interest because the debt instrument provides for interest equal to 12.36 percent, the rate of interest based on an annual compounding period equivalent to 12 percent, compounded semiannually, and the interest is payable annually, the compounding period for the test rate.

Example (3). Assume that on May 1, 1986, in consideration for the sale of nonpublicly traded property A issues a debt instrument to B calling for a principal payment of $10,000,000 due December 31, 1996, and 10 percent annual interest, $500,000 payable on June 30 and December 31 of each year, beginning on December 31, 1986. In addition, the debt instrument calls for A to make a payment of interest on June 30, 1986, of $163,963.60 for the period from May 1, 1986, to June 30, 1986. The appropriate compounding period is semiannual. Assume that the test rate of interest is 10 percent, compounded semiannually. Further, assume that a convention that assumes a year consists of 12 30-day months is adopted. The debt instrument provides for adequate stated interest. For each semiannual period beginning on July 1, 1986, the debt instrument provides for interest equal to the test rate of 10 percent payable semiannually, the compounding period for the test rate. For the short period from May 1, 1986, through June 30, 1986 (one-third of a full semiannual period), the amount of stated interest payable on June 30, 1986, under the exact method would be $163,963.60, determined as follows:

$\$10{,}000{,}000 \times [(1 + .10/2)^{1/3} - 1] = \$163{,}963.60$

Example (4). The facts are the same as in example (3), except that the amount of interest payable for the short period is determined under the approximate method. Under the approximate method, the amount of stated interest payable for the short period would be $166,666.70 determined as follows:

$\$10{,}000{,}000 \times (.10/2) \times (1/3) = \$166{,}666.70$

Example (5). The facts are the same as in example (3), except that the debt instrument is issued on May 19, 1986. Assume that a convention that assumes that a year consists of 12 30-day months is adopted. Thus, the short period is 42/180 of the semiannual period. The amount of stated interest payable on June 30, 1986, under the exact method would be $114,494.20 determined as follows:

$\$10{,}000{,}000 \times [(1 + .10/2)^{42/180} - 1] = \$114{,}494.20$

Example (6). The facts are the same as in example (5), except that the amount of interest payable for the short period (May 19, 1986, through June 30, 1986) is determined under the approximate method. Under the approximate method, the amount of stated interest payable for the short period would be $116,666.70 determined as follows:

$\$10{,}000{,}000 \times (.10/2) \times (42/180) = \$116{,}666.70$

Example (7). (i) Assume that on July 4, 1985, A sells nonpublicly traded property to B for $1,400,000. In consideration for the sale, B makes a $400,000 down payment, and issues a debt instrument with a stated principal amount of $1,000,000 with interest payable at 8.84 percent on the unpaid balance of the debt instrument. The debt instrument calls for monthly payments of $7,931.37 (consisting of interest at an annual rate of 8.84 percent on the unpaid balance of the principal amount of the debt instrument, and a partial payment of principal) due on the the first of each month for a period of 30 years beginning on September 1, 1985. The appropriate compounding period is one month. Interest is payable on the first of the month for the preceding month. In addition, on July 4, 1985, B makes an advance payment of interest of $6,875.56 for the period from July 4, 1985, through July 31, 1985.

(ii) Since the sale occurs after June 30, 1985, and the stated principal amount of the debt instrument is less than $2,800,000, the test rate of interest based on a monthly compounding period is 8.84 percent. Assume that a convention that assumes that a year consists of 12 30-day months is adopted. The debt instrument provides for adequate stated interest. For the whole-month periods beginning on August 1, 1985, the debt instrument provides for interest payable at a stated rate of interest equal to the test rate based on monthly compounding (8.84 percent) and the interest is payable monthly, the compounding period for the test rate.

For the short period (the period from July 4, 1985, through July 31, 1985), the amount of stated interest payable under the approximate method is $6,875.56 ($1,000,000 \times (.0884/12) \times (28/30)$).

Example (8). Assume that a debt instrument issued in consideration for the sale of nonpublicly traded property calls for two installment payments of principal, one due in 5 years in the amount of $5,000,000 and a second due in 10 years in the amount of $5,000,000. In addition, the debt instrument calls for 10 semiannual payments of interest of $600,000 each for the first five years, and 10 semiannual payments of interest of $300,000 each for the final five years. The appropriate compounding period is semiannual. Assume that the test rate of interest is 12 percent, compounded semiannually. The debt instrument provides for adequate stated interest because the debt instrument calls for interest on the outstanding principal balance at a rate equal to the test rate of 12 percent payable semiannually, the compounding period for the test rate of interest.

(c) *Debt instruments that do not meet the requirements of paragraph (b) of this section*—(1) In *general.* A debt instrument that does not meet the requirements of paragraph (b) of this section provides for adequate stated interest if the stated principal amount of the debt instrument (as defined in § 1.1274-2(b)) is less than or equal to the testing amount. For this purpose, the term "testing amount" means—

(i) The sum of the present values of all payments (including interest) due under the debt instrument determined by using a discount rate of interest equal to the test rate of interest as determined in paragraph (e) of this section, or

(ii) In the case of a potentially abusive situation (as defined in § 1.1274-4(g)(2)), the fair market value of the property (reduced in the manner prescribed in § 1.1274-4(g)(1)) received in exchange for the debt instrument.

For rules relating to the determination of present value, see § 1.1274-5.

(2) *Examples.* The provisions of paragraph (c) of this section may be illustrated by the following examples:

Example (1). Assume that a debt instrument issued in consideration for the sale of nonpublicly traded property calls for a single payment of $12,100,000 due in two years ($10,000,000 principal and $2,100,000 interest payment). Assume that an annual compounding period is selected. Further, assume that the test rate of interest based on semiannual compounding is 10 percent. The test rate of interest based on an annual compounding period equivalent to 10 percent, compounded semiannually, is 10.25 percent. Since the debt instrument does not call for a fixed rate of interest no lower than the test rate of interest for its entire term, the debt instrument has adequate stated interest if the stated principal amount is less than or equal to the testing amount. The present value of the payment of $12,100,000 (discounted at 10.25 percent, compounded annually) is equal to $9,954,699.95. Thus, since the testing amount is less than the stated principal amount of $10,000,000, the debt instrument does not provide for adequate stated interest.

For the debt instrument to provide for adequate stated interest, the debt instrument must call for a payment of at least $12,155,062.50 at maturity ($10,000,000 principal and $2,155,062.50 interest payment).

Example (2). (i) On January 1, 1986, A sells B nonpublicly traded property for a stated purchase price of $3,500,000. In consideration for the sale, B makes a down payment of $500,000 and issues a 10-year debt instrument with a stated principal amount of $3,000,000. The debt instrument calls for no interest in the first two years and interest at a rate of 15 percent payable annually over the remaining 8 years of the debt instrument. The first interest payment of $450,000 is due on December 31, 1988, and the last such payment is due on December 31, 1995, together with the $3,000,000 payment of principal. Assume that the test rate of interest applicable to the debt instrument is 10.5 percent, compounded annually.

(ii) Since the debt instrument does not call for a fixed rate of interest no lower than the test rate of interest for its entire term, the debt instrument has adequate stated interest if the stated principal amount is less than or equal to the testing amount. To compute the testing amount, all payments due under the debt instrument must be discounted at 10.5 percent, compounded annually, as follows:

(A) The present value of the $3,000,000 principal payment payable on December 31, 1995, is $1,105,347, determined as follows:

$$\$1{,}105{,}347 = \frac{\$3{,}000{,}000}{(1 + .105/1)^{10}}$$

(B)(1) The present value of the eight interest payments of $450,000 as of January 1, 1988, (the interim date) is $2,357,635, determined as follows:

$$\$2{,}357{,}635 = \$450{,}000 \times \frac{1-(1+.105/1)^{-8}}{(.105/1)}$$

(2) The present value of this interim amount as of the January 1, 1986, the computation date, is $1,930,865, determined as follows:

$$\$1{,}930{,}865 = \frac{\$2{,}357{,}635}{(1+.105/1)^{2}}$$

(iii) Thus, the testing amount (that is, the total present value of all payments due under the debt instrument) is $3,036,212 ($1,105,347 + $1,930,865). Since the stated principal amount is less than the testing amount, the debt instrument provides for adequate stated interest. However, since the debt instrument does not call for interest at a constant rate over its entire term, it is subject to section 1274. For the treatment of this debt instrument under section 1272 and the regulations thereunder, see § 1.1272-1(k) example (9).

Example (3). In a transaction that is a potentially abusive situation, nonpublicly traded property is sold for a $1,000,000 down payment and a debt instrument with a stated principal amount of $7,000,000. The debt instrument calls for annual interest payments at 11 percent, the test rate of interest applicable to the debt instrument. The fair market value of the property is $7,000,000. Since the debt instrument is involved in a potentially abusive situation, the debt instrument is tested for adequate stated interest by determining whether the stated principal amount is less than or equal to the testing amount. Thus, the debt instrument does not provide for adequate stated interest because the stated principal amount of the debt instrument ($7,000,000) exceeds the testing amount ($6,000,000), the fair market value of the property reduced by the amount of the down payment.

(d) *Treatment of debt instruments calling for variable rate of interest or contingent interest*—(1) *Variable rates of interest based on an index*—(i) *In general.* Except as provided in paragraph (d)(1) (ii) and (iii) of this section, a variable rate debt instrument (within the meaning of § 1.1275-5) shall be treated for purposes of determining whether the debt instrument provides for adequate stated interest as if the rate of interest determined under the index were a fixed rate equal to the rate of interest determined under the index as of the date when the test rate of interest is determined (within the meaning of §1.1274-6(e)). Thus, for any period in which interest is payable at a rate determined under the index, the rate of interest fixed by the index as of the date the test rate of interest is determined is treated for purposes of paragraph (b) of this section as the stated rate of interest, and is used to determine the amount of any stated interest payment for purposes of paragraph (c) of this section.

(ii) *Limitation on inceases in rate.* In the case of a debt instrument that limits the number of percentage or basis points by which the rate of interest can vary from one period to the next—

(A) Paragraph (d)(1)(i) of this section shall apply only if, for each period, the limitation permits the rate of interest to increase by at least as many percentage or basis points as such rate is permitted to decrease; and

(B) Section 1.1274-6(a)(2) shall not apply if, by reason of such limitation, the number of percentage points by which the rate (based on annual compounding) can increase for any period is less than 1/12 of the number of months in the adjustment interval preceding such period.

(iii) *Ceiling on variable rate of interest.* Paragraph (d)(1)(i) of this section shall not apply to any debt instrument that places a ceiling on the maximum rate of interest payable under the debt instrument unless—

(A) The excess of the rate initially fixed by the index over the test rate of interest plus the excess of the maximum rate permitted by the ceiling over the test rate is at least equal to 5 percentage points; and

(B) In the case of a debt instrument with a term that exceeds 3 years, the maximum rate permitted by the ceiling is at least equal to the test rate of interest determined without regard to § 1.1274–6(a)(2) plus the difference between such rate and the actual test rate of interest.

(iv) *Treatment of payment if variable rate of interest rules do not apply.* If paragraph (d)(1)(i) of this section does not apply to a debt instrument, variable payments of interest under the debt instrument are contingent payments of interest subject to the rules of § 1.1275–4, but only to the extent such variable payments exceed the minimum payments of interest permitted under the debt instrument. For this purpose, the minimum payment of interest permitted under the debt instrument for any period shall be determined by taking into account any floor on the minimum rate of interest payable under the debt instrument and, in the case of a debt instrument described in paragraph (d)(1)(ii) of this section, the maximum permissible decrease in the interest rate for each period during the term of the debt instrument.

(v) *Examples.* The provisions of paragraph (d)(1) of this section may be further illustrated by the following examples:

Example (1). On January 1, 1986, A sells B nonpubliciy traded property. In partial consideration for the sale, B issues a debt instrument in the principal amount of $1,000,000 payable in 5 years. The debt instrument calls for interest payable monthly at a rate of one percentage point above the average prime lending rate of a major bank for the month proceeding the month of the interest payment. Thus, the debt instrument is a variable rate debt instrument within the meaning of § 1.1275–5. Assume that the test rate of interest applicable to the debt instrument is 11.5 percent, compounded monthly. Further, assume that on the date the test rate of interest is determined, one percentage point above the prime lending rate of the designated bank is 12.5 percent. Since the test rate of interest is 11.5 percent, compounded monthly, the debt instrument provides for adequate stated interest.

Example (2). (i) On July 1, 1987, A sells B nonpublicly traded property for a stated purchase price of $5,000,000. In consideration for the sale, B makes a $1,000,000 down payment, and issues a debt instrument calling for a single payment of principal of $4,000,000 due in 10 years. Interest on a debt instrument is payable semiannually on December 31 and June 30 of each year until June 30, 1997. For the first semiannual period, interest is payable at a rate of 9 percent. For subsequent semiannual periods, interest is payable at a rate equal to 3 percentage points above the yield on 6-month Treasury bills for the midpoint of the semiannual period of the interest payment, except that the interest rate cannot increase or decrease by more than one percentage point from the rate payable in the preceding semiannual period. Assume that as of the date the interest rate is determined, the yield on 6-month Treasury bills is 10 percent, compounded semiannually. Further, assume that the Federal short-term rate is 12 percent, compounded semiannually.

(ii) The debt instrument is tested for adequate stated interest by assuming that the index provided in the instrument will remain fixed at the 13 percent rate in effect as of the date the interest rate is determined. Based on this assumption, interest would be payable on the debt instrument as follows:

Semiannual period	Interest rate (percent)	Interest amount
1	9	$180,000
2	10	200,000
3	11	220,000
4	12	240,000
5–20	13	260,000

The testing amount, the sum of the present values (using a discount rate of 12 percent, compounded semiannually) of the assumed interest payments and of the $4,000,000 principal payment due at the end of year 10, is $4,051,100. Since the stated principal amount of $4,000,000 is less than the testing amount, the debt instrument provides for adequate stated interest. Since the interest rate limitation permits rate increases of at least 1 percentage point for each annual adjustment interval, the applicable Federal rate with respect to the debt instrument is determined under § 1.274–6 (a)(2), even though the initial interest rate is fixed at a level below the rate established by the index. Thus, the applicable Federal rate is the Federal short-term rate.

Example (3). On July 1, 1986, A sells nonpublicly traded property to B for $3,000,000. In partial consideration for the sale, B issues a debt instrument that calls for payments of $1,500,000 on July 1, 1989, and July 1, 1992, plus annual interest payments on the outstanding loan balance on July 1 of each year (beginning on July 1, 1987) at 90 percent of the prime rate of a local bank on June 15 of the year of the payment. The debt instrument provides, however, that the rate determined with reference to the bank's prime rate cannot increase or decrease from one year to the next by more than 1 percentage point (100 basis points). Paragraph (d)(l)(i) of this section applies to the debt instrument because the interest rate limitation provided in the debt instrument permits interest rate increases by at least as many percentage points as it permits interest rate decreases. In addition, since the debt instrument permits at least one percentage point increase for each annual adjustment interval, the applicable Federal rate with respect to the debt instrument is determined under § 1.1274–6(a)(2). Thus, the applicable Federal rate is the Federal short-term rate.

Example (4). The facts are the same as in example (3), except that the limitation on the variable rate permits only a one-half percentage point (50 basis point) increase or decrease in the interest rate for each one year adjustment period. Paragraph (d)(l)(i) applies to the debt instrument. However, since the limitation on increases in the interest rate does not permit at least a one percentage point adjustment for each annual adjustment interval, the applicable Federal rate with respect to the debt instrument is determined without regard to § 1.1274–6(a)(2). Thus, the applicable Federal rate is the Federal mid-term rate.

Example (5). The facts are the same as in example (3), except that the limitation on the variable rate applies only to increases in the interest rate. Paragraph (d)(1)(i) of this section does not apply to the debt instrument because the limitation does not permit the interest rate to increase by at least as many percentage points as it permits the interest rate to decrease. Thus, the variable payments of interest are treated in accordance with the rules of paragraph (d)(l)(iv) of this section.

Example (6). On July 1, 1987, A sells nonpublicly traded property to B for $11,000,000. Assume that as the debt instrument is determined, the Federal short-term rate is 10 percent and the Federal long-term rate is 12 percent. In partial consideration for the sale, B issues a debt instrument that calls for payments of $1,000,000 on July 1, 1988, and on each subsequent July 1 until July 1, 1987. Interest on the outstanding principal balance is payable on July 1 of each year at the Federal short-term rate of June of the same year. The debt instrument provides, however, that the interest rate cannot rise above 15 percent. The ceiling provided in the debt instrument satisfies paragraph (d)(l)(iii) of this section because (i) the excess of the rate initially fixed by the index over the test rate (0 percentage points) plus the excess of the maximum rate permitted by the ceiling over the test (5 percentage points) is at least 5 percentage points, and (ii) the maximum rate permitted by the ceiling (15 percent) is greater than the sum of the Federal long-term rate (12 percent) and the difference between that rate and the Federal short-term rate (2-percent). Thus, paragraph (d) (l) (i) of this section applies to this debt instrument.

Example (7). The facts are the same as in example (6), except that the debt instrument calls for interest at a rate equal to 110 percent of the Federal short-term rate for June of the same year and the ceiling specified in the debt instrument is 14 percent. This debt instrument satisfies paragraph (d)(l)(iii) of this section because (i) the excess of the rate initially fixed by the index over the test rate (1 percentage point) plus the excess of the maximum rate permitted by the cap over the test rate (4 percentage points) is at least 5 percentage points, and (ii) the maximum rate permitted by the ceiling (14 percent) is at least equal to the sum of the Federal long-term rate and the difference between such rate and the Federal short-term difference between such rate and the Federal short-term rate. Thus, paragraph (d)(l)(i) of this section applies to the debt instrument.

Example (8). The facts are the same as in example (7), except that the Federal long-term rate is 13 percent. Although the excess of the rate initially fixed by the index over the test rate plus the excess of the maximum rate permitted by the cap over the test rate is at least 5 percentage points, the debt instrument does not satisfy paragraph (d)(1)(iii) of this section because the maximum rate permitted by the ceiling (14 percent) is less than the sum of the Federal long-term rate (13 percent) and the difference between such rate and the Federal short-term rate (3 percent). Thus, paragraph (d)(1)(i) does not apply to this debt instrument and the variable payments of interest are treated in accordance with the rules of paragraph (d)(1)(iv) of this section.

(2) *Contingent payments of interest*—(i) *General rule.* Except as provided in paragraph (d)(2)(ii) of this section, contingent payments of interest are not taken into account in determining whether a debt instrument provides for adequate stated interest.
For additional rules relating to contingent payments, see § 1.1275-4.

(ii) *Special rule.* A debt instrument provides for adequate stated interest if all or part of the contingent payments of interest provided for in the debt instrument are of a nature described in paragraph (d)(2)(iii), and the debt instrument meets the requirements of paragraph (d)(2)(iv) of this section.

(iii) *Nature of contingent interest taken into account in determining adequate stated interest.* Paragraph (d)(2)(ii) of this section applies only to payments of contingent interest if the payments are conditioned on a return from the exploitation of the property acquired for the debt instrument. Such contingent interest payments include payments conditioned on profits, sales, rents, production, or royalties from the property acquired for the debt instrument.

(iv) *Contingent interest as adequate stated interest.* (A) *In general.* A debt instrument given in consideration for property that does not include any recovery property (within the meaning of section 168(c)(1)) or any property described in section 1221(1) (relating to stock in trade, inventories, and other property held for sale to customers) provides for adequate stated interest if—

(*1*) The debt instrument would satisfy paragraph (b) or (c) of this section (taking into account the rule of paragraph (d)(1) of this section) at a test rate of interest equal to 80 percent of the test rate applicable to the debt instrument, and

(*2*) It is reasonable to expect (as of the date the test rate of interest is determined) that contingent payments of interest described in paragraph (d)(2)(iii) will raise the total yield on the debt instrument to at least the test rate of interest applicable to the debt instrument.

(B) *Depreciable or inventoriable property.* A debt instrument given in consideration for property that includes any recovery property or any property described in section 1221(1) provides for adequate stated interest if—

(*1*) The debt instrument satisfies the requirements of paragraph (d)(2)(iv)(A) of this section, and

(*2*) The term of the debt instrument does not exceed 12 years (4 years in the case of a sale or exchange that includes any 3-year or 5-year property (within the meaning of section 168(c)), or any property described in section 1221(1)).

(C) *Entity look-through rule.* For purposes of paragraph (d)(2)(iv) of this section, the purchase of an interest in an entity shall be treated as a purchase of the underlying assets of the entity if the bases of the assets are determined, in whole or in part, by reference to the amount paid for such interest. If the entity owns any recovery property or property described in section 1221(1), paragraph (d)(2)(iv)(B) of this section shall apply even with respect to that portion of the purchase price attributable to nonrecovery property that is not described in section 1221(1). For example, if one corporation purchases stock of another corporation owning nonrecovery property that is not described in section 1221(1) and at least one item of 3-year or 5-year property and makes an election under section 338 (relating to certain stock purchases treated as asset acquisitions), the stock purchase shall be treated as a purchase of 3-year or 5-year property for purposes of paragraph (d)(2)(iv)(B)(*2*) of this section.

(v) *Examples.* The provisions of paragraph (d)(2) of this section may be further illustrated by the following examples:

Example (1). (i) On January 1, 1986, A sells a newly-constructed office building to B for $1,000,000 in cash and a debt instrument with a face amount of $5,000,000. The debt instrument provides for a payment of $5,000,000 on December 31, 1995, plus an interest payment of $400,000 on December 31 of each year. In addition, the debt instrument provides for an additional payment on December 31 of each year equal to 5 percent of the gross rentals derived from the property during the first eleven months of the year. Assume that the test rate of interest (based on annual compounding) applicable to the sale is 10 percent. Thus, under paragraph (d)(2)(i) of this section, the debt instrument does not provide for adequate stated interest.

(ii) Under paragraph (d)(2)(iii) of this section, however, the debt instrument will be deemed to provide adequate interest if (A) the debt instrument states fixed interest at a rate at least equal to 8 percent, (B) it is reasonable to expect the contingent interest will raise the total yield on the debt instrument to at least 10 percent and (C) the term of the debt instrument does not exceed 12 years. The debt instrument satisfies requirements (A) and (C) on its face. It is reasonable to expect the contingent payments to raise the yield of the debt instrument to 10 percent, the debt instrument is deemed to state adequate interest.

(iii) Based on the fair market value of the building, the terms being offered for comparable office space in the vicinity of the building and expectations (based on previous experience with respect to office buildings in the area) as to future vacancy rates, future rentals and initial delays in leasing space in the building, the issuer and holder expect that the contingent payment provisions will result in the following additional payments under the debt instrument:

1986	$30,000
1987	80,000
1988	115,000
1989	125,000
1990	130,000
1991	135,000
1992	140,000
1993	145,000
1994	150,000
1995	155,000

Assuming the contingent payment provision results in these additional payments, the yield of the debt instrument will be 10.23 percent. Because the expectations of the issuer and holder as to future payments under the contingent payment provision are based on an analysis of relevant existing information and reasonable estimates of future events, it is reasonable to expect that the contingent payments will raise the yield on the debt instrument to a rate at least equal to the test rate of interest (10 percent). Thus, under paragraph (d)(2)(iii) of this section, this debt instrument provides for adequate interest.

Example (2). On January 1, 1986, A sells 3-year property to B that is to be held for rent. In partial consideration for the sale, B issues a debt instrument with a term of 3 years in the principal amount of $700,000 calling for fixed payments of interest at 8 percent payable annually, and contingent payments of interest payable annually in an amount equal to 3 percent of the gross rents from the property. Assume that the test rate of interest is 9.2 percent, compounded annually. Further, assume that the contingent payments of interest are such that it is reasonable to expect that the contingent interest payments will raise the total yield on the debt instrument to at least 9.2 percent, compounded annually (taking into account the 8 percent fixed interest payments). Thus, the debt instrument provides for adequate stated interest because the debt instrument calls for stated interest payable at a rate at least equal to 80 percent of the test rate (7.36 percent), and the term of the debt instrument does not exceed 4 years (the appropriate measuring period for a debt instrument given in consideration for the sale of 3-year property).

Example (3). The facts are the same as in example (2), except that the terms of the debt instrument is 5 years. Since, the term of the debt instrument exceeds 4 years and since considering only the fixed payments of interest, the debt instrument does not call for interest at a rate at least equal to the test rate of 9.2 percent, compounded annually, it does not provide for adequate stated interest.

Example (4). The facts are the same as in example (2), except that the rental property is depreciable real property that is 19-year property (within the meaning of section 168 (c)(2)(D)), and the term of the debt instrument is 10 years. The debt instrument provides for adequate stated interest because it calls for stated interest at a rate at least equal to 80 percent of the test rate of interest and the term of the debt instrument does not exceed 12 years.

(e) *Determination of test rate of interest*—(1) *Sales or exchanges occurring after June 30, 1985*—(i) *General rule.* Except as otherwise provided in paragraph (e) of this section, if a sale or exchange occurs after June 30, 1985, the test rate of interest is 100 percent of the applicable Federal rate based on semiannual compounding or an equivalent rate based on an appropriate compounding period (for example, one year, a quarter, or a month). For rules relating to the appropriate compounding period, see paragraph (e)(3) of this section. For rules relating to the determination of the applicable Federal rate, see § 1.1274–6.

(ii) *Qualified debt instruments.* In the case of a qualified debt instrument as defined in § 1.1274A–1(b) the test rate of interest is the lower of—

(*A*) 100 percent of the applicable Federal rate (based on an appropriate compounding period), or

(*B*) 9 percent, compounded semiannually, or an equivalent rate based on an appropriate compounding period.
The rates equivalent to 9 percent, compounded semiannually, for annual, quarterly and monthly compounding periods are as follows:

Compounding period	Equivalent rate
Annual	9.20 percent
Quarterly	8.90 percent
Monthly	8.84 percent

(iii) *Sale-leaseback transactions.* In the case of a debt instrument given in consideration for the sale or exchange of property all or a portion of which, pursuant to a plan, is leased by the transferor of the property or a person related to the transferor (within the meaning of section 168(e)(4)(D)) after the sale or exchange, the test rate of interest is 110 percent of the applicable Federal rate.

(2) *Sales or exchanges occurring before July 1, 1985*—(i) *General rule*—(A) *In general.* In the case of any sale or exchange of property (other than new section 38 property within the meaning of section 48(b) and the regulations thereunder) occurring after December 31, 1984, and before July 1, 1985, the test rate of interest is—

(*1*) If the sale or exchange involves a borrowed amount (within the meaning of paragraph (e)(2)(i)(C) of this section) that does not exceed $2,000,000, 9 percent, compounded semiannually, or an equivalent rate based on an appropriate compounding period, or

(*2*) If the sale or exchange involves a borrowed amount in excess of $2,000,000—

(*i*) The percent set forth in paragraph (e)(i)(A)(1) of this section, plus

(ii) The percent applicable to the borrowed amount in excess of $2,000,000.

(B) *The percent applicable to a borrowed amount in excess of $2,000,000.* The percent applicable to the borrowed amount in excess of $2,000,000 is equal to—

(*1*) The excess of 110 percent of the applicable Federal rate (based on the appropriate compounding period) over the percent set forth in paragraph (e)(2)(i)(A)(1) of this section, multiplied by

(*2*) A fraction, the numerator of which is the excess of the borrowed amount over $2,000,000, and the denominator of which is the borrowed amount.

(C) *Meaning of borrowed amount.* For purposes of paragraph (e)(2)(i) of this section, the term "borrowed amount" means the stated principal amount of a debt instrument as that term is defined in § 1.1274–2(b).

(ii) *New section 38 property.* In the case of any sale or exchange of new section 38 property (within the meaning of section 48(b) and the regulations thereunder) occurring after December 31, 1984, and before July 1, 1985, the test rate of interest is 110 percent of the applicable Federal rate.

(iii) *Special rules for sales or exchanges calling for contingent principal.* If some or all the consideration involved in a sale or exchange taking place before July 1, 1985, consists of contingent payments of principal, then the test rate of interest shall be determined as follows. A stated principal amount shall first be determined by assuming that no contingent principal payments will be made. The test rate of interest for noncontingent payments of principal is then determined in accordance with paragraph (e)(2)(i)(A) of this section. This test rate of interest as so determined shall apply to all fixed payments under the debt instrument. If the fixed stated principal amount is not less than $2,000,000, the test rate of interest that applies to any contingent payment shall be 110 percent of the applicable Federal rate. If $2,000,000 exceeds the fixed stated principal amount, then the test rate of interest that applies to the contingent payments shall be 9 percent, compounded semiannually (or an equivalent rate based on an appropriate compounding period) until the stated principal amount attributable to contingent payments equals this excess. As of the time the stated principal amount equals this excess, the test rate of interest applicable to any subsequent contingent payment is 110 percent of the applicable Federal rate with respect to the contingent payment. For additional rules relating to contingent payments, see § 1.1275–4.

(3) *Selection of the appropriate compounding period*—(i) *In general.* The test rate of interest applicable to a debt instrument must be based on an appropriate compounding period. The longer the compounding period, the higher the annual stated rate of interest. For example, a rate based on annual compounding is slightly higher than the equivalent rate based on semiannual compounding, which in turn is slightly higher than the equivalent rate based on quarterly compounding, monthly compounding, etc.

(ii) *Debt instruments calling for more than one payment or compounding date*—(A) *Regular payment or compounding at intervals of one year or less.* If a debt instrument calls for more than one payment or compounding date (other than the issue date) and all dates on which an amount is either paid or compounded under the debt instrument occur at regular intervals of one year or less, the appropriate compounding period is such interval even if the interval between the issue date and the first payment or compounding date after the issue date or the interval between the maturity date and the preceding payment or compounding date differs from the interval between other payment or compounding dates.

(B) *Irregular payment or compounding; intervals of more than one year.* If a debt instrument calls for more than one payment or compounding date (other than the issue date) and all dates on which an amount is either paid or compounded do not occur at regular intervals of one year or less, the appropriate compounding period is the longest period of not more than one year such that all intervals consist of a whole number of compounding periods. For purposes of this paragraph (e)(3)(ii)(B), the interval between the issue date and the first payment or compounding date after the issue date and the interval between the maturity date and the preceding payment or compounding date are not taken into account unless the debt instrument calls for only one payment or compounding date between the issue date and the maturity date.

(iii) *Debt instruments calling for a single payment.* If a debt instrument calls for a single payment at maturity and for no other payment or compounding dates (other than the issue date), any compounding period of not more than one year may be selected.

(4) *Conversion of a test rate to appropriate compounding period*—(i) *In general.* If the test rate of interest based on an appropriate compounding period (as determined under paragraph (e)(3) of this section) is not provided under paragraph (e) (1) or (2) of this section (as applicable) or § 1.1274–6 (relating to the applicable Federal rate), or if a test rate accurate to more than 2 decimal places is desired by both parties to the transaction, the test rate of interest shall be determined by first determining a test rate of interest based on semiannual compounding, then converting that rate to a rate based on an appropriate compounding period using the procedures prescribed in paragraph (e)(4) (ii) or (iii) of this section (as applicable).

(ii) *Conversion of semiannual test rate of interest to an equivalent rate based on annual compounding.* A test rate of interest based on annual compounding that is equivalent to the test rate based on semiannual compounding may be determined by the application of the following formula:

$r = i + i^2/4$

In which:

r = The equivalent rate of interest based on annual compounding expressed as a decimal

i = The test rate of interest based on semiannual compounding expressed as a decimal

For example, assume that the test rate of interest based on semiannual compounding, is exactly 10 percent. The equivalent rate based on annual compounding is 10.25 percent determined as follows:

$.1025 = .10 + [(.10)^2/4]$

(iii) *Conversion of semiannual test rate of interest to an equivalent rate based on compounding more frequently than semiannually.* A test rate of interest based on compounding more frequently than semiannually that is equivalent to the test rate based on semiannual compounding may be determined by the application of the following formula:

$r = k[(1 + i/2)^{2/k} - 1]$

In which:

r = The equivalent rate based on compounding more frequently than semiannually expressed as a decimal

i = The test rate based on semiannual compounding expressed as a decimal

k = The number of compounding periods in a year on which the annual equivalent rate is to be based (for example, 12, if the equivalent rate is to be based on monthly compounding)

For example, assume that the test rate of interest based on semiannual compounding is exactly 10 percent. The equivalent rate based on quarterly compounding would be 9.8780308 percent determined as follows:

$.098780308 = 4[(1 + .10/2)^{2/4} - 1]$

The equivalent rate based on monthly compounding would be 9.7978152 percent determined as follows:

$.097978152 = 12[(1 + .10/2)^{2/12} - 1]$

The equivalent rate based on semimonthly compounding would be 9.78 percent (accurate to two decimal places) determined as follows:

$.0978 = 24[(1 + .10/2)^{2/24} - 1]$

(5) *Examples.* The provisions of paragraph (e) of this section may be illustrated by the following examples:

Example (1). On January 1, 1985, A sells nonpublicly traded property (other than new section 38 property) to B for $2,300,000. In consideration for the sale, B makes a down payment of $300,000 and issues a debt instrument due in 3 years with a stated principal amount of $2,000,000 calling for annual payments of interest. Thus, the appropriate compounding period for the test rate is annual. The test applicable to the debt instrument is 9.20 percent, compounded annually, since the sale occurred before July 1, 1985, and the borrowed amount (the stated principal amount of the debt instrument) does not exceed $2,000,000.

Example (2). On January 1, 1986, A sells nonpublicly traded property (other than new section 38 property) to B for $3,500,000. In consideration for the sale, B makes a $1,000,000 down payment and issues a debt instrument with a stated principal amount of $2,500,000 due in 10 years and that calls for twenty semiannual payments of interest. Assume that the debt instrument is a qualified debt instrument within the meaning is the lower of 100 percent of the applicable of § 1.1274A–1(b). Thus, the test rate of interest Federal rate or 9 percent, compounded semiannually. Assume that 100 percent of the applicable Federal rate (the Federal long-term rate) is 9.69 percent, compounded semiannually. Thus, the test rate of interest is 9 percent, compounded semiannually.

Example (3). The facts are the same as in example (2), except that the sale takes place on January 1, 1985. On that date, 110 percent of the Federal long-term rate was 12.74, compounded semiannually. Thus, the excess of 110 percent of the applicable Federal rate over 9 percent is 3.74 percent. Since the sale occurred before July 1, 1985, the test rate of interest applicable to the debt instrument is 9.75 percent, compounded semiannually, that is, 9 percent plus the 0.75 percent applicable to the borrowed amount in excess of $2,000,000 ($500,000/$2,500,000 × 3.74 (percent) = 0.75 percent).

Example (4). (i) On April 1, 1985, A sells rental property to B. In consideration for the sale, B issues a debt instrument calling for annual payments of $500,000 for each of the next five years payable on March 31, 1986, through March 31, 1990, plus contingent payments equal to 2 percent of gross rents from the property. The debt instrument has an internal interest clause that calls for each payment (including the noncontingent payments) to be characterized as interest in the smallest amount that would constitute adequate stated interest within the meaning of section 1274. The test rate of interest is determined as follows:

(ii) The borrowed amount (the stated principal amount of the debt instrument) is first determined by assuming that contingent payments will not be made. Pursuant to the internal interest clause, the borrowed amount attributable to the fixed payments is the present value of the 5 payments of $500,000 determined tentatively by using a test rate of 9.20 percent, compounded annually. At that discount rate of interest, the present value of the 5 payments is $1,934,775. Since $2,000,000 exceeds the fixed borrowed amount, the test rate of interest that applies to the fixed payments is 9.20 percent and the tentative calculation of the borrowed amount may be used. (If the tentative calculation of the borrowed amount exceeded $2,000,000, an interrelated calculation would be necessary to compute the actual test rate and borrowed amount.)

(iii) Assume that a contingent payment in the amount of $50,000 is made on March 31, 1986. Pursuant to the internal interest clause, the tentative borrowed amount attributable to that payment is $45,788, the present value of the payment determined by using a discount rate of interest of 9.2 percent. Since this amount is less than $65,225 (the excess of $2,000,000 over the fixed stated principal amount), the test rate applicable to the contingent payment is 9.2 percent, compounded annually and the tentative calculation of the borrowed amount may be used. Thus, the payment is treated as a payment of principal of $45,788 (which gives the buyer additional basis of this amount) and a payment of interest of $4,212.

(iv) Assume that a contingent payment of $30,000 is made on March 31, 1987. Using a discount rate of interest of 9.20 percent, compounded annually, the present value of the payment is $25,158. This amount exceeds $19,437 (the excess of $2,000,000 over the sum of the stated principal amount attributable to the fixed payments and the stated principal amount attributable to the first contingent payment). Thus, the test rate of interest applicable to the payment is 9.20 percent, compounded annually, only with respect to that portion of the payment having a present value of $19,437, and 110 percent of the applicable Federal rate with respect to the remaining portion of the payment (that is, the total amount of the payment less the portion of the payment having a present value of $19,437). The portion of the contingent payment having a present value of $19,437 is $23,178. Thus, the remaining $6,822 of the payment is subject to 110 percent of the applicable Federal rate. One hundred ten percent of the applicable Federal rate (the Federal short-term rate) in effect on April 1, 1985, was 11.43 percent, compounded annually. At the rate of interest pursuant to the internal interest clause, $5,494 of the payment is treated as a payment of principal, and $1,328 of the payment is treated as interest.

(v) Since, as of March 31, 1987, the stated principal amount involved in the transaction is in excess of $2,000,000, all subsequent contingent payments will be subject to a test rate of interest equal to 110 percent of the applicable Federal rate.

§ 1.1274-4 Debt instruments without adequate stated interest.

(a) *In general.* If section 1274 applies to a debt instrument because it does not provide for adequate stated interest (within the meaning of § 1.1274-3), the issue price of the debt instrument is the imputed principal amount of the debt instrument. Except as provided in paragraph (g) of this section, the imputed principal amount of a debt instrument is the sum of the present values of all payments (including interest) due under the debt instrument, determined by using a discount rate equal to the imputed rate of interest as determined under paragraph (b) of this section. For rules relating to the determination of the present value of a payment, see § 1.1274-5.

(b) *Determination of imputed rate of interest*—(1) *General rule.* Except as provided in paragraphs (b) (2) and (3) of this section, the imputed rate of interest applicable to the debt instrument is the same as the test rate of interest as determined in § 1.1274-3(e).

(2) *Special rate for certain sales or exchanges occurring before July 1, 1985*—(i) *In general.* If the test rate of interest applicable to a debt instrument is prescribed in § 1.1274-3(e)(2)(i), the imputed rate of interest is—

(A) If the sale or exchange involves a borrowed amount (as defined in § 1.1274-3(e)(2)(i)(C)) that does not exceed $2,000,000—

(1) 10.00 percent, compounded semiannually, or

(2) An equivalent rate based on an appropriate compounding period. The rates equivalent to 10.00 percent, compounded semiannually, for annual, quarterly and monthly compounding periods are as follows:

Compounding period	Equivalent rate
Annual	10.25 percent
Quarterly	9.88 percent
Monthly	9.80 percent

(B) If the sale or exchange involves a borrowed amount that exceeds $2,000,000—

(1) The percent determined under paragraph (b)(2)(i)(A) of this section, plus

(2) The percent applicable to the borrowed amount in excess of $2,000,000.

(ii) *Percent applicable to the borrowed amount in excess of $2,000,000.* The percent applicable to the borrowed amount in excess of $2,000,000 is equal to—

(A) The excess of 120 percent of the applicable Federal rate (based on the appropriate compounding period) over the percent determined under paragraph (b)(2)(i)(A) of this section, multiplied by

(B) A fraction, the numerator of which is the excess of the borrowed amount over $2,000,000 and the denominator of which is the borrowed amount.

(iii) *Sales calling for contingent principal.* If some or all the consideration involved in a sale or exchange taking place before July 1, 1985, consists of contingent payments of principal, then in determining the imputed rate of interest under paragraph (b)(2) of this section, the rules of § 1.1274-3(e)(2)(iii) shall apply, except that 120 percent shall be substituted for 110 percent in each place it appears.

(3) *Rate applicable to sales or exchanges of new section 38 property occurring after December 31, 1984, and before July 1, 1985.* The imputed rate of interest applicable to a sale or exchange of new section 38 property (within the meaning of section 48(b) and the regulations thereunder) occurring after December 31, 1984, and before July 1, 1985, is 120 percent of the applicable Federal rate.

(c) *Appropriate compounding period; conversion of imputed rate to appropriate compounding period.* The imputed rate of interest must be based on an appropriate compounding period. An appropriate compounding period depends on the intervals between payments or compounding of interest and shall be determined in accordance with the rules of § 1.1274-3(e)(3) except that if a debt instrument calls for a single payment at maturity and for no other payment or compounding dates, the appropriate compounding periods are the six-month periods (or the shorter period from the issue date of the debt instrument) that end on the day in the calendar year that corresponds either to the maturity date or to the date that is six months before the maturity date. Rules analogous to those set forth in § 1.1274-3(e)(4) shall also apply to convert an imputed rate to a rate based on an appropriate compounding period if not otherwise provided, or to a rate accurate to more than two decimal places if such accuracy is desired by both parties to the transaction.

(d) *Determining imputed principal amount with short period.* In determining the imputed principal amount of a debt instrument when there is a short period, the exact method as prescribed in § 1.1274-5(d)(2)(ii) shall be used to discount a payment or a stream of payments for the short period. The exact method shall also be used for purposes of determining the amount of original issue discount includible under section 1272 for the short period (see § 1272-1(c)(2)(ii)(B)). In addition, for purposes of determining the fraction I with respect to a short period, a convention that assumes that a year consists of 12 30-day months shall be used.

(e) *Treatment of variable rate of interest in determining imputed principal amount.* If § 1.1274-3(d)(1) (relating to payments of interest based on an objective interest index) applies to a debt instrument, the rate of interest fixed by the index as of the date the imputed rate of interest is determined is treated for purposes of determining the imputed principal amound of the debt instrument as the stated rate of interest. If § 1.1274-3(d)(1) does not apply to a debt instrument (either because the debt instrument is not a variable rate debt instrument (within the meaning of § 1.1275-5) or, because, for example, the variable rate debt instrument places a nonqualifying ceiling on the variable rate), the payments of interest shall be treated as contingent payments to the extent provided in § 1.1274-3(d)(1)(iv) and shall be subject to the provisions of paragraph (f) of this section and § 1.1275-4.

(f) *Treatment of contingent payments in determining imputed principal amount.* In the case of a debt instrument calling for any contingent payment, the imputed principal amount of the debt instrument shall be determined solely by reference to the noncontingent payments. Thus, the imputed principal amount of a debt instrument calling for contingent payments is the present value of all noncontingent payments. For additional rules relating to contingent payments, see § 1.1275-4.

(g) *Imputed principal amount of a debt instrument equal to fair market value in potentially abusive situations*—(1) *In* *general.* In the case of any potentially abusive situation, the imputed principal amount of a debt instrument issued in consideration for the sale or exchange of property shall be the fair market value of the property reduced by the fair market value of any consideration, other than the debt instrument (for example, a down payment) given in consideration for the sale or exchange.

(2) *Potentially abusive situation defined*—(i) *In general.* For purposes of paragraph (g)(1) of this section, the term "potentially abusive situation" means—

(A) A tax shelter (as defined in section 6661(b)(2)(C)(ii)), or

(B) Any other situation having potential for tax avoidance (within the meaning of paragraph (g)(2)(ii) of this section).

(ii) *Situations having potential for tax avoidance.* For purposes of paragraph (g)(2)(i)(B) of this section, a situation having potential for tax avoidance means a situation involving—

(A) A recent sales transaction,

(B) Nonrecourse financing,

(C) Financing with a term in excess of the economic life of the property, or

(D) A sale in which the purchase price or the interest thereon is denominated in a currency other than U.S. dollar.

(iii) *Sale between related parties.* Notwithstanding paragraph (g)(2) (i) and (ii) of this section, a sale between related parties governed by § 1.1012–2 involving a situation described in paragraph (g)(2) (i) or (ii) of this section shall not be considered a potentially abusive situation. If, however, a sale of property was the subject of a recent sales transaction, the purchase price of the property in the recent sale shall be relevant in determining the value of the property for purposes of § 1.1012–2.

(h) *Examples.* The provisions of this section may be illustrated by the following examples:

Example (1). (i) On April 1, 1986, A sells nonpublicly traded property to B in a transaction that is not excepted under the provisions of section 1274 (c)(3) and § 1.1274–1(b) and is not a potentially abusive situation. As part of the consideration for the sale, B issues a debt instrument calling for a $1,000,000 payment of principal due on December 31, 1995, with an interest payment of $20,000 due on June 30, 1986, and semiannual interest payments of $40,000 due at the end of each semiannual period, beginning with the period ending on December 31, 1986, and terminating with the period ending on December 31, 1995. The appropriate compounding period for the test rate is semiannual.

(ii) Assume that the debt instrument does not provide for adequate stated interest within the meaning of § 1.1274–3. Since the debt instrument does not provide for adequate stated interest, the issue price of the debt instrument is the imputed principal amount of the debt instrument. Further, assume that the imputed rate of interest at which the payments due under the debt instrument are to be discounted is 12 percent, compounded semiannually.

(iii) The present value of all the payments due under the debt instrument may be determined as follows:

(A) The payment of principal of $1,000,000 due on December 31, 1995, is due 9 years and 9 months from the computation date of April 1, 1986. Based on a semiannual compounding period, the payment is due 19 and one-half compounding periods from the computation date. Using the exact method to determine present value for the short period (one-half a compounding period) the present value of the payment is $321,022.61 determined as follows:

$$\$321{,}022.61 = \frac{\$1{,}000{,}000}{(1+.12/2)^{19.5}}$$

(B) The interest payment of $20,000 due on June 30, 1986, is due three months from the April 1, 1986, computation date. Since the compounding period is semiannual, the payment is due on a date that represents one-half a compounding period from the computation date. Using the exact method to determine the present value of the payment, the present value of the payment is $19,425.72 determined as follows:

$$\$19{,}425.72 = \frac{\$20{,}000}{(1+.12/2)^{.5}}$$

(C) The interest payments of $40,000 due at the end of each semiannual period beginning with the period ending December 31, 1986, and ending on December 31, 1995, from the computation date of April 1, 1986, represent of a stream of payments that continues for 19 compounding periods preceded by a short period consisting of one-half of a compounding period. Thus, the present value of the stream of payments is determined by first discounting the stream of payments for the 19 compounding periods to determine an interim amount, and then discounting that interim amount for the short period. The present value of the stream of payments, using the exact method to determine present value for the short period, is determined as follows:

(*1*) The interim amount is determined as follows:

$$\$446{,}324.66 = \$40.000 \times \frac{1-(1+.12/2)^{-19}}{(.12/2)}$$

(*2*) The present value of a single payment of $446,324.66 on June 30, 1986, as of the computation date of April 1, 1986, is determined as follows:

$$\$433{,}508.83 = \frac{\$446.324.66}{(1+.12/2)^{.5}}$$

Thus, the present value of the stream of the $40,000 interest payments on the computation date of April 1, 1986, is $433,508.83.

(iv) The imputed principal amount of the debt instrument is $773,957.16, the sum of the amounts determined under (iii) ($321,022.61 + 19,425.72 + $433,508.83).

Example (2). The facts are the same as in § 1.1274–3(c)(2), example (3). Since the debt instrument was received in a transaction that is a potentially abusive situation, the imputed principal amount of the debt instrument is $6,000,000, the fair market value of the property ($7,000,000) reduced by the amount of the down payment ($1,000,000).

§ 1.1274–5 Determination of present value.

(a) *In general.* This section prescribes rules for the determination of the present value of a payment. The present value of a payment is the amount that, if invested on the computation date at a compound rate of interest equal to the discount rate of interest, would increase in value to the amount of the future payment on the payment date. Paragraph (d) of this section prescribes formulas for determining present value. For purposes of these formulas, a compounding period must be selected, and the rate of interest at which the payment or payments are to be discounted must be based on the same compounding period. See paragraph (b) of this section for rules relating to the selection of a compounding period. The formulas are prescribed for determining the present value of a single payment or a stream of payments. A stream of payments means payments of equal amounts due at the end of each full compounding period for a specified period of time. The formulas for determining the present value of a stream of payments yield the same result as the sum of the separately computed present values of each single payment in the stream.

(b) *Compounding period: compounding period for the discount rate of interest.* To determine the present value of a payment or a stream of payments, a compounding period must be established. A compounding period is established depending on the intervals between payment or compounding dates and is determined in accordance with the rules of § 1.1274-3(e)(3), or, if applicable, § 1.1274-4(c). Whatever the compounding period, the rate of interest used to discount a payment or a stream of payments must be based on the same compounding period. For example, if the compounding period is one month, the discount rate of interest must be based on a monthly compounding period. For rules relating to the conversion of interest rates based on semiannual compounding to equivalent rates based on different compounding periods, see § 1.1274-3(e)(4).

(c) *Meaning of symbols used in formulas.* For the purposes of applying the formulas prescribed in paragraph (d) of this section, the following symbols are assigned the following meanings:

PV = The present value of a payment or a stream of payments to be made in the future.

i = The interest rate (expressed as a decimal) at which the payment, or the stream of payments, is to be discounted.

k = The number of compounding periods contained in a year.

FV = The amount of any single payment to be made in the future.

PMT = The amount of any payment that is one of a stream of equal payments to be made in the future.

n = The number of full compounding periods until a single payment is made, or for which a stream of payments continues.

f = A fraction, the numerator of which is the length of a short period (that is, a period less than a full compounding period) and the denominator of which is the length of a compounding period.

(d) *Formulas for determining present value*—(1) *Single payment; no short period.* The present value of a single payment due on a date in the future that is a whole number of compounding periods from the computation date is determined by application of the following formula:

$$PV = \frac{FV}{(1+i/k)^{n}}$$

(2) *Single payment; short period*—(i) *In general.* The present value of a single payment due on a date in the future that is not a whole number of compounding periods from the computation date (that is, a payment due on a date that marks the end of a short period or on a date that marks the end of a whole number of compounding periods preceded by a short period) is determined under either the exact method or the approximate method as prescribed in paragraph (d)(2) (ii) and (iii) of this section, or under any other reasonable method. For example, it is permissible to use monthly compounding of interest (which reflects compounding at monthly intervals with simple interest within a month).

(ii) *Exact method.* The exact method assumes daily compounding of interest. Under this method, the present value of a payment due on a date in the future that is not a whole number of compounding periods from the computation date is determined by application of the following formula:

$$PV = \frac{FV}{(1+i/k)^{n+f}}$$

If the payment is due on a date that marks the end of only a short period (that is, the payment is due on a date that is less than one whole compounding period from the computation date), the value of "n" is zero.

(iii) *Approximate method.* The approximate method assumes simple interest within a compounding period. Thus, the present value of a payment is determined by discounting the payment to the beginning of the first full compounding period, and then further discounting that amount on a simple interest basis for the short period. Under this method, the present value of a payment due on a date in the future that is not a whole number of compounding periods from the computation date is determined by application of the following formula:

$$PV = \frac{FV}{(1+fxi/k)^{n}\times[(1+fxi)/k]}$$

If the payment is due on a date that marks the end of only a short period (that is, the payment is due on a date that is less than one whole compounding period from the computation date), the value of "n" is zero and the formula is:

$$PV = \frac{FV}{(1+fxi)/k}$$

(3) *Stream of payments; no short period, payment at the end of each full compounding period.* The present value of a stream of payments due on dates in the future that mark intervals equal to full compounding periods from the computation date may be determined by application of the following formula:

$$PV = \frac{PMT\times 1-(1+i/k)^{-n}}{(i/k)}$$

(4) *Stream of payments; short period, full compounding period for which no payment is made.* If a stream of payments due on dates in the future that mark intervals equal to full compounding periods is preceded by an interval other than a full compounding period, the present value of such stream of payments is determined as follows. First, the payments are discounted for the number of full compounding periods for which the stream of payments continues to the date that begins the first such compounding period for which the stream of payments continues (the interim date), as set forth in paragraph (d)(3) of this section. Second, this interim amount is then further discounted to the computation date, as if that amount were a single payment due on the interim date.

(e) *Examples.* The provisions of this section may be further illustrated by the following examples:

Example (1). Assume that a single payment of $1,000,000 is due 15 years from the computation date. Further, assume that an annual compounding period is selected, and that the discount rate of interest based on an annual compounding period is 12 percent. Since the payment is due in 15 years and the compounding period is one year, the payment is due on a date that is 15 whole compounding periods from the computation date. The present value of the payment is $182,696.26 determined as follows:

$$\$182{,}696.26 = \frac{\$1{,}000{,}000}{(1+.12/1)^{15}}$$

Example (2). Assume that a single payment of $1,000,000 is due 2 years and 9 months from the computation date. Further, assume that a monthly compounding period is selected and that the discount rate of interest based on a monthly compounding period is 9 percent. Since the payment is due in 2 years and 9 months, and the compounding period is one month, the payment is due on a date that is 33 whole compounding periods from the computation date. The present value of the payment is $781,471.58 determined as follows:

$$\$781{,}471.58 = \frac{\$1{,}000{,}000}{(1+.09/12)^{33}}$$

Example (3). Assume that a single payment of $1,000,000 is due 3 years, 4 months and 15 days from the computation date. Further, assume that an annual compounding period is selected, and that the discount rate of interest is 10 percent based on an annual compounding period. Since the payment is due in 3 years, 4 months and 15 days, and the compounding period is one year, the payment is due on a date in the future that is not a whole number of compounding periods from the computation date. Thus, the payment is due on a date in the future that is preceded by three full compounding periods and a short period. Assume a convention that assumes that a year consists of 12 30-day months is adopted. Thus, the short period is equal to 135 days (four 30-day months plus 15 days). The short period is .375 of a full compounding period (135 days/360 days). Assume that the exact method is used to discount for the short period. Under the exact method, the present value of the payment is $724,936.03 determined as follows:

$$\$724{,}936.03 = \frac{\$1{,}000{,}000}{(1+.10/1)^{3.375}}$$

Example (4). The facts are the same as in example (3), except that tne approximate method is used to discount for the short period. Under the approximate method, the present value of the payment is $724,158.84 determined as follows:

$$\$724{,}158.84 = \frac{\$1{,}000{,}000}{(1+.10/1)^{3}\times[1+(.375\times.10)/1]}$$

Example (5). Assume that on the computation date, January 1, 1986, a payment schedule calls for payments of $10,000 due at the end of each of the next 5 years. Thus, the first $10,000 payment is due on January 1, 1987, and $10,000 on January 1 of each year thereafter with a final payment on January 1, 1991. The compounding period is one year. Further, assume that the discount rate of interest based on an annual compounding period is 12 percent. Since the payment schedule calls for payments due at the end of full compounding periods, the payment schedule consists of a stream of payments which continues for 5 full compounding periods. The present value of the stream of payments is $36,047.76 determined as follows:

$$\$36{,}047.76 = \$10{,}000 \times \frac{1-(1+.12/1)^{-5}}{(.12/1)}$$

Example (6). Assume that on the computation date, January 1, 1986, a payment schedule calls for payments of $1,000 for 360 months. The first payment is due on February 1, 1986, with a final payment on January 1, 2016. The compounding period is one month. Further, assume that the discount rate of interest based on a monthly compounding period is 12 percent. Since the payment schedule calls for payments due at the end of full compounding periods, the payment schedule consists of a stream of payments which continues for 360 full compounding periods. The present value of the stream of payments is $97,218.33 determined as follows:

$$\$97{,}218.33 = \$1{,}000 \times \frac{1-(1+.12/12)^{-360}}{(.12/12)}$$

Example (7). The facts are the same as in example (6), except that the computation date is November 24, 1985. The present value of the stream of payments is determined by discounting the stream to January 1, 1986, and then further discounting that interim amount for the period consisting of the full compounding period at the end of which no payment is due (December 1985) and the short period (the period beginning after November 24, 1985, and ending on December 1, 1985). In example (6), it was determined that the present value as of January 1, 1986, of this stream of payments is $97,218.33. Assume that the exact method is used to discount the stream of payments for the short period. The present value as of November 24, 1985, of the stream of payments is $96,032.55 determined as follows:

$$\$96{,}032.55 = \frac{\$97{,}218.33}{(1+.12/12)^{1.23333}}$$

Example (8). The facts are the same as in example (7), except that the approximate method is used to discount for the short period. The present value of the stream of payments is $96,031.70 determined as follows:

$$\$96{,}031.70 = \frac{\$97{,}218.33}{(1+.12/12)^{1}\times[1+(.23333\times.12)12]}$$

Example (9). The facts are the same as in example (7), except that the computation date is December 23, 1985. Thus, there is no full compounding period at the end of which no payment is made preceding the compounding period for which the stream of payments begins. Only a short period of seven days precedes the compounding period for which the stream of payments begins. Under the exact method, the present value of the stream of payments is $96,992.88 determined as follows:

$$\$96{,}992.88 = \frac{\$97{,}218.33}{(1+.12/12)\ .23333}$$

Example (10). The facts are the same as in example (9), except that the approximate method is used to discount for the short period. The present value of the stream of payment is $96,992.02 determined as follows:

$$\$96{,}992.02 = \frac{\$97{,}218.33}{[1+(.23333 \times .12)/12]}$$

§ 1.1274-6 Applicable Federal rate.

(a) *Applicable Federal rate defined*—(1) *In general.* Except as otherwise provided in paragraphs (a)(2) or (3) and (d) of this section, the applicable Federal rate means—

(i) The Federal short-term rate if the term of the debt instrument is not over 3 years,

(ii) The Federal mid-term rate if the term of the debt instrument is over 3 years but not over 9 years, or

(iii) The Federal long-term rate if the term of the debt instrument is over 9 years.

The Federal rates are annual rates of interest based on semiannual compounding. Nevertheless, the Commissioner may prescribe equivalent rates based on compounding periods other than a semiannual period (for example, annual compounding, quarterly compounding and monthly compounding). The Federal rates shall be published in Revenue Rulings.

(2) *Variable rate debt instruments.* Except as otherwise provided in § 1.1274-3(d)(1)(ii), in the case of a variable rate debt instrument (within the meaning of § 1.1275-5), the applicable Federal rate shall be determined by reference to the longest adjustment interval of the objective interest index rather than the term of the debt instrument. For this purpose, the period from the issue date to the first adjustment shall be treated as an adjustment interval. Thus, for example, if a debt instrument provides for a rate of interest based on the prime rate and the rate is adjusted annually, the applicable Federal rate is the Federal short-term rate. Similarly, if the rate of interest is adjustable every 5 years, the applicable Federal rate is the Federal mid-term rate.

(3) *Lower rate permitted in certain cases*— (i) *In general.* the applicable Federal rate with respect to a debt instrument shall be the allowable Treasury index rate (within the meaning of paragraph (a)(3)(ii) of this section) if it is demonstrated that—

(A) The yield of the debt instrument (based on semiannual compounding) is not less than such allowable Treasury index rate, and

(B) The issuer of the debt instrument could obtain a loan in the same stated principal amount and with the same yield and terms from a lender not related to the borrower within the meaning of section 168(e)(4)(D) (nor, in a sale transaction subject to section 483 or 1274, to the seller).

This paragraph (a)(3)(i) shall not apply unless it is stated on the face of the debt instrument that it is intended that the debt instrument qualify as having adequate stated interest under section 1274(d)(1)(D) and paragraph (a)(3) of this section, and that the issuer and all successors and assignees thereof agree to treat the debt instrument as having adquate stated interest on all tax returns for which the determination of adequate stated interest is relevant.

(ii) *Allowable Treasury index rates.* The allowable Treasury index rates are rates published weekly in Federal Reserve Statistical Releases G.13 and H.15. The allowable Treasury index rate at any given time shall include the rate (determined under the following rules) for any day within the preceding 15 days or for any weekly period ending within the preceding 15 days. The allowable Treasury index rates shall be—

(A) In the case of debt instruments having a maturity of one year or more for which a rate is published with the same maturity as the debt instrument, the yield on Treasury constant maturities of that maturity as a debt instrument, and

(B) In the case of debt instruments having a maturity of 3 or 6 months, the auction average yield (investment) on the most recently auctioned U.S. Treasury bills of the same maturity as the debt instrument.

If an allowable Treasury index rate is not published for the exact maturity of the debt instrument, the applicable Federal rate shall be a linear interpolation of the allowable Treasury index rates for the next shortest and the next longest maturities for which rates are published. For maturities of 3 months or less, the allowable Treasury index shall be the auction average yield for the most recently auctioned 3-month Treasury bills.

(b) *Determination of the applicable Federal rate*—(1) *In general.* The Federal short-term, mid-term, and long-term rates shall be computed monthly and shall be based on the yield to maturity of outstanding marketable obligations of the United States of similar maturities during the one month period ending on the 14th day of the month preceding the month for which the rates are applicable. Thus, for example, the Federal rates for April 1985 are determined on the basis of yields of obligations outstanding during the one-month period from February 15, 1985, to March 14, 1985.

(2) *Federal rates for January 1985.* For the month of January 1985 the Federal rates shall be the Federal rates in effect for the month of February 1985.

(3) *Special rules for periods before March 1, 1985*—(i) *Period before January 1, 1985.* If the period as of which the applicable Federal rate is determined (within the meaning of 1.1274-6(e)) is before January 1, 1985, the applicable Federal rate shall be determined by reference to Table II as set forth in Rev. Rul. 84-163, 1984-2 C.B. 179.

(ii) *Period after December 31, 1984, and before March 1, 1985*—(A) *Election of higher applicable rate.* If the period as of which the applicable Federal rate is determined (within the meaning of § 1.1274-6(e)) is after December 31, 1984, and before March 1, 1985, the issuer and holder may file a joint election in the manner prescribed in paragraph (b)(3)(ii)(B) of this section to use the higher applicable Federal rate determined by reference to Table I as set forth in Rev. Rul. 84-163, 1984-2 C.B. 179. The election shall be irrevocable and shall be binding on all successors of the issuer and holder.

(B) *Time and manner of election.* The issuer and holder shall make the election described in paragraph (b)(3)(ii)(A) on or before the last day for filing (including extensions) the returns of the issuer and holder for the taxable year of issue of the debt instrument. The election shall be made by attaching to the returns of the issuer and the holder a statement signed by the issuer and holder that includes the following information—

(*1*) The names, addresses and taxpayer identification numbers of the issuer and holder,

(*2*) A clear indication that the statement relates to a joint election to use the higher applicable Federal rate of interest as determined by reference to Table I as set forth in Rev. Rul. 84–163, 1984–2 C.B. 179, and

(*3*) Any other information necessary to establish that the borrower and lender are entitled to make the election.

For sales or exchanges occurring in 1985, the election may be made by filing an amended return if either the borrower or lender filed their returns for the taxable year which includes the date of the sale or exchange prior to May 8, 1986.

(c) *Foreign currency loans.* In the case of a debt instrument the proceeds or repayment of which is denominated in a foreign currency, the applicable Federal rate shall be a foreign currency rate of interest analogous to the applicable Federal rate described in paragraphs (a) and (b) of this section. For purposes of the preceding sentence, an analogous foreign currency rate of interest is a rate of interest based on yields (with an appropriate compounding period) of the highest grade of outstanding marketable obligations denomiated in such currency (excluding any obligations that benefit from special tax exemptions or preferential tax rates not available to debt instruments generally) with due consideration given to the maturities of the obligations.

(d) *Installment obligations*—(1) *Determining adequate stated interest*—(i) *In general.* Except as provided in paragraph (d)(2) of this section, for purposes of applying § 1.1274–3(b) (relating to the determination of adequate stated interest) to an installment obligation (within the meaning of § 1.1273–1(b)(2)(i) and § 1.1275–2(d)), the term of the obligation shall be determined by reference to the last payment of principal. The Commissioner, however, may disregard nominal payments of principal. Paragraph (d)(2) of this section prescribes special rules for determining adequate stated interest in the manner prescribed in § 1.1274–3(b) for certain types of installment obligations. If, in applying the rule of this paragraph (d)(1)(i) or the rule of paragraph (d)(2) of this section, an installment obligation (including an obligation that has a principal payment that is treated as a nominal payment) does not provide for adequate stated interest, the determination of adequate stated interest with respect to the obligation is governed by § 1.1274–3(c) and paragraph (d)(3) of this section. For circumstances in which multiple debt instruments are not treated as an installment obligation, see § 1.1275–2(d).

(ii) *Examples.* The provisions of paragraph (d)(1)(i) of this section may be further illustrated by the following examples:

Example (1). On July 1, 1986, A sells B nonpublicly traded property for $4,500,000. B agrees to pay the principal in 5 annual installments of $300,000 followed by 5 annual installments of $600,000. B is to pay interest semiannually on the outstanding principal balance. For purposes of applying § 1.1274–3(b) to this debt instrument, the test rate of interest is the Federal long-term rate.

Example (2). At a time when the Federal short-term rate is 15 percent and the Federal long-term rate is 12 percent, A sells B nonpublicly traded property for $5,000,000. B agrees to pay the principal in two installments. The first installment consists of $4,750,000 of principal and is payable at the end of 3 years. The second installment of $250,000 is payable at the end of 10 years. The second payment of principal may be treated as nominal by the Commissioner.

(2) *Special rule for certain installment obligations*—(i) *In general.* In the case of a self-amortizing installment obligation (as defined in § 1.1273–1(b)(2)(iii)) or a level-principal obligation (as defined in paragraph (d)(2)(iv) of this section), § 1.1274–3(b) may be applied by using a test rate that is a weighted average of the Federal short-term, mid-term, and long-term rates determined under the table set forth in paragraph (d)(2)(ii) (for self-amortizing installment obligations) or (iii) (for level-principal obligations) of this section. The weighted average is the sum of—

(A) The product of the Federal short-term rate and the short-term percent set forth in column (1) of the applicable table;

(B) The product of the Federal mid-term rate and the mid-term percent set forth in column (2) of the applicable table; and

(C) The product of the Federal long-term rate and the long-term percent set forth in column (3) of the applicable table.

For purposes of applying the tables, the term of a self-amortizing installment or level-principal obligation that is not a whole number of years shall be considered to be equal to the next largest whole number of years.

(ii) *Table for self-amortizing installment obligations.* The table referred to in paragraph (d)(2)(i) for self-amortizing installment obligations is as follows:

Term (years)	(1) Short-term percent	(2) Mid-term percent	(3) Long-term percent
4	59	41	0
5	38	62	0
6	26	74	0
7	19	81	0
8	15	85	0
9	11	89	0
10	8	71	21
11	7	58	35
12	6	47	47
13	5	39	56
14	4	33	63
15	3	28	69
16	3	23	74
17	2	20	78
18	2	17	81
19	1	15	84
20	1	13	86
21	1	11	88
22	1	9	90
23	1	8	91
24	0	8	92
25	0	7	93
26	0	6	94
27	0	5	95
28–29	0	4	96
30–31	0	3	97
32–37	0	2	98
38–47	0	1	99
48 or more	0	0	100

(iii) *Table for level-principal obligations.* The table referred to in paragraph (d)(2)(i) for level-principal obligations is as follows:

Term (years)	(1) Short-term percent	(2) Mid-term percent	(3) Long-term percent
4	61	39	0
5	42	58	0
6	31	69	0
7	24	76	0
8	19	81	0
9	16	84	0
10	14	70	16
11	12	60	28
12	11	52	37
13	10	45	45
14	9	40	51
15	8	36	56
16	7	33	60
17	6	30	64
18	6	27	67
19	5	26	69
20	5	24	71
21	4	23	73
22	4	21	75
23	4	19	77
24	4	18	78
25	3	18	79
26	3	17	80
27	3	16	81
28	3	15	82
29	3	14	83
30	3	13	84
31	2	13	85
32	2	12	86
33	2	12	86
34	2	12	86
35	2	11	87
36	2	11	87
37	2	10	88
38	2	10	88
39	2	10	88
40	2	9	89

(iv) *Meaning of level-principal obligation.* For purposes of paragraph (d)(2) of this section, the term "level-principal obligation" means an obligation calling for (*1*) equal payments of principal at regular intervals of one year or less over the entire term of the obligation and (*2*) each payment of principal to be accompanied by a payment of interest at a fixed rate on the outstanding principal balance.

(v) *Balloon payments.* The special rule of paragraph (d)(2) of this section may be applied to a debt instrument that would constitute a self-amortizing obligation or a level-principal obligation but for the fact that the debt instrument calls for a lump sum or balloon payment of principal at maturity. In applying this paragraph to such a debt instrument, the balloon payment shall be ignored and the term of the debt instrument shall be determined as if the initial payment pattern continued until the principal were fully repaid. If, however, the debt instrument has a maturity of more than 3 years but not more than 9 years (taking into account the balloon), in applying paragraph (d)(2)(i)(C) of this section, the Federal mid-term rate shall be substituted for the Federal long-term rate.

(vi) *Authority to adjust percent table.* The Commissioner may by Revenue Ruling adjust or replace the tables prescribed in paragraph (d)(2) (ii) and (iii) of this section. Any adjustment or replacement shall become effective no earlier than 30 days after publication of the adjusted or replacement table in the Internal Revenue Bulletin.

(vii) *Examples.* The provisions of this paragraph (d)(2) of this section may be illustrated by the following examples:

Example (1). On July 1, 1986, A sells B nonpublicly traded property for $3,000,000. B issues a debt instrument that calls for 15 years of equal monthly payments of $31,617.03, each representing a partial payment of principal and interest at a rate of 9.66 percent on the outstanding principal balance. Assume that as of the date when the test rate of interest is determined the Federal short-term rate is 8 percent compounded monthly, the Federal mid-term rate is 9 percent compounded monthly, and the Federal long-term rate is 10 percent compounded monthly. Using the table prescribed in paragraph (d)(2)(ii) of this section for a self-amortizing installment obligation with a term of 15 years, the test rate of interest for the debt instrument, based on monthly compounding, is 9.66 percent ((.03)(.08) + (.28)(.09) + (.69)(.10)). Since B's debt instrument calls for interest at a rate of 9.66 percent, payable monthly, it provides for adequate stated interest.

Example (2). The facts are the same as in example (1), except that the debt instrument calls for 5 annual payments of $770,677.10 on June 30 of each year from 1987 through 1991. Each payment represents a partial payment of principal and interest a rate of 8.97 percent. Assume that the Federal short-term rate is 8.30 percent, compounded annually, and the Federal mid-term rate is 9.38 percent, compounded annually. The test rate of interest for the debt instrument, based on annual compounding, is 8.9696 percent ((.38)(.0830) + (.62)(.0938)). Since the debt instrument calls for interest at 8.97 percent payable annually, it provides for adequate stated interest.

Example (3). The facts are the same as in example (2), except that the debt instrument calls for 5 equal annual payments of principal of $600,000. Each payment of principal is accompanied by interest at a rate of 8.93 percent on the outstanding principal balance. The payment schedule for the debt instrument is as follows:

Year	Principal	Interest	Total
1987	$600,000	$267,900	$867,900
1988	600,000	214,320	814,320
1989	600,000	160,740	760,740
1990	600,000	107,160	707,160
1991	600,600	53,580	653,580

Using the table prescribed in paragraph (d)(2)(iii) of this section for a level-principal obligation with a term of 5 years, the test rate for the debt instrument, based on annual compounding, is 8.9264 percent ((.42)(.083) + (.58)(.0938)). Since the debt instrument calls for interest payable annually at a rate of 8.93 percent, it provides adequate stated interest.

Example (4). The facts are the same as in example (1), except that, in lieu of the last 5 years of monthly payments, B's debt instrument calls for a balloon payment on June 30, 1996, of $1,499,849.16 (in addition to the regular payment of $31,617.03 due on that date). This balloon payment is equal to the outstanding principal balance on June 30, 1996 (after taking into account the payment of $31,617.03). For purposes of applying paragraph (d)(2) of this section, the debt instrument is treated as a 15-year self-amortizing installment obligation. Thus, the debt instrument, which calls for interest to be paid monthly at a rate of 9.66 percent, provides for adequate stated interest.

Example (5). (i) On July 1, 1986, A sells B nonpublicly traded property for $3,600,000. B issues a debt instrument that calls for semiannual principal payments of $150,000 on January 1, and July 1 of each year from 1987 through 1992. On January 1, 1993, the remaining principal balance of $1,800,000 is required to be paid. The debt instrument calls for interest to be paid semiannually at a rate of 9.89 percent on the outstanding principal balance. Assume that the Federal short-term and mid-term rates applicable to the transaction, based on semiannual compounding, are 9 and 10 percent, respectively.

(ii) In applying paragraph (d)(2) of this section, the debt instrument is treated as a 12-year level principal obligation with a balloon payment after 6 and one-half years. Under paragraph (d)(2)(iii) and (v) of this section, the test rate for the debt instrument is 9.89 percent ((.11)(.09) + (.52)(.10) + (.37)(.10)). Thus, the debt instrument provides for adequate stated interest.

(3) *Obligations not providing for adequate stated interest under paragraph (d) (1) or (2) of this section*—(i) *Testing amount for installment obligations.* An installment obligation that does not provide for adequate stated interest under paragraph (d) (1) or (2) of this section may nevertheless have adequate stated interest under the rules of § 1.1274–3(c) if the stated principal amount of the debt instrument is less than or equal to the testing amount. For purposes of computing the testing amount for an installment obligation, in determining the present values under § 1.1274–3(c)(1), the discount rate shall be—

(A) In the case of principal payments made not more than 3 years from the issue date and interest payments attributable to such principal payments, the Federal short-term rate;

(B) In the case of principal payments made more than 3 years but not more than 9 years from the issue date and interest payments attributable to such principal payments, the Federal mid-term rate; and

(C) In all other cases, the Federal long-term rate.

(iii) *Examples.* The provisions of paragraph (d)(3) of this section may be illustrated by the following examples:

Example (1). (i) On July 1, 1986, A sells B nonpublicly traded property for $5,000,000. The principal is due in two installments: $2,000,000 due on June 30, 1989, and the remaining $3,000,000 due on June 30, 1991. The debt instrument calls for semiannual payments of interest on the outstanding principal balance at a rate of 8.04 percent. Assume that the Federal short-term and mid-term rates applicable to this transaction are 7 percent compounded semiannually and 8.5 percent, compounded semiannually, respectively.

(ii) The debt instrument does not provide for adequate stated interest under the rule of paragraph (d)(1) of this section because interest is not provided at a rate at least equal to the Federal mid-term rate. The debt instrument cannot satisfy the provisions of paragraph (d)(2) of this section because it is neither a self-amortizing installment obligation nor a level-principal obligation. Thus, under paragraph (d)(3) of this section, the determination of adequate stated interest is made under § 1.1274–3(c). The debt instrument provides for adequate stated interest if the stated principal amount of the debt instrument is less than or equal to the testing amount of the debt instrument (the sum of the present values of the payments determined in the manner provided in paragraph (d)(3) of this section).

(iii) The present value of the $2,000,000 principal payment due on June 30, 1989, discounted at the Federal short-term rate of 7.0 percent compounded semiannually, is

$1,627,001.29. Six semiannual interest payments of $80,400 (one-half of 8.04 percent of $2,000,000) are attributable to this first payment of principal. The present value of this stream of 6 interest payments is $428,415.66.

(iv) The present value of the $3,000,000 principal payment due on June 30, 1991, discounted at the mid-term rate of 8.5 percent compounded semiannually is $1,978,611.91. Ten semiannual interest payments of $120,600 are attributable to this second payment of principal. The present value of this stream of 10 interest payments is $966,112.97.

(v) The testing amount of the debt instrument is $5,000,141.84 ($1,627,001.29 + $428,415.66 + $1,978,611.91 + $966,112.97). Since the testing amount exceeds the stated principal amount of $5,000,000, the debt instrument provides for adequate stated interest.

Example (2). (i) On July 1, 1987, A sells B nonpublicly traded property for $4,000,000. B issues a debt instrument that calls for 9 annual principal payments of $200,000 on June 30 of each year from 1988 through 1996 and a principal payment on June 30, 1997, of $2,200,000. The debt instrument also calls for annual payments of interest at a rate of 9.62 percent on the outstanding principal balance. Assume that the Federal short-term, mid-term and long-term rates, based on annual compounding, are 8 percent, 9 percent, and 10 percent, respectively.

(ii) The debt instrument does not provide for adequate stated interest under the rule of paragraph (d)(1) of this section because it calls for interest at a rate lower than the Federal long-term rate. The debt instrument also does not satisfy the provisions of paragraph (d)(2) of this section because, under those provisions, the test rate of interest (using the weighting factors for a 20-year level principal obligation) is 9.65 percent ((.06) (.08) + (.23) (.09) + (.71) (.10)). Thus, under paragraph (d)(3) of this section, the determination of adequate stated interest is made under § 1.1274–3(c). The debt instrument provides for adequate stated interest if the stated principal amount of the debt instrument is less than or equal to the testing amount of the debt instrument (the sum of the present values of the payments determined in the manner provided in paragraph (d)(3) of this section).

(iii) The present values of the first three principal payments, using a discount rate equal to the Federal short-term rate of 8 percent, is $515,419.40. The portions of the interest payments in the years 1988, 1989 and 1990 attributable to these three principal payments are $57,720 (9.62 percent of $600,000), $38,480 (9.62 percent of $400,000) and $19,240 (9.62 percent of $200,000), respectively. The sum of the present values of these three payments is $101,708.17.

(iv) The sum of the present values of the six principal payments in the years 1991 through 1996, using a discount rate equal to the Federal mid-term rate of 9 percent, is $692,790.45. The interest payments attributable to these principal payments and their present values are as follows:

Year	Interest payment	Present value
1988	$115,440	$105,908.26
1989	115,440	97,163.54
1990	115,440	89,140.86
1991	115,440	81,780.61
1992	96,200	62,523.40
1993	76,960	45,888.73
1994	57,720	31,574.82
1995	38,480	19,311.81
1996	19,240	8,858.63
Total		$542,150.66

(v) The balloon principal payment of $2,200,000 due on June 30, 1997, when discounted at the Federal long-term rate of 10 percent, has a present value of $848,195.24. Interest payments of $211,640 (9.62 percent of $2,200,000) in each year from 1988 through 1997 are attributable to the last principal payment. The present value of this stream of payments is $1,300,436.18.

(vi) The testing amount (the sum of the foregoing present values) is $4,000,700.10:

$515,419.40
107,708.17
692,790.45
542,150.66
848,195.24
1,300,436.18

4,000,700.10

Since the stated principal amount of $4,000,000 is less than the testing amount of $4,000,700.10, the debt instrument provides for adequate stated interest.

(4) *Coordination with other provisions*—(i) *Nine percent interest rate.* In the case of a qualified debt instrument (as defined in 1274A(b) and §1,1274A–1(b)), the provisions of paragraph (d)(2) of this section may be applied to determine if the test rate is lower than 9 percent, compounded semiannually. If so, this lower test rate may be used. Similarly, the provisions of paragraph (d)(3) of this section may be applied to determine if the testing amount using the Federal rates is larger than the testing amount computed by using a discount rate of 9 percent, compounded semiannually. If so, the larger testing amount may be used. However, paragraphs (d) (2) and (3) of this section shall not be applied by substituting 9 percent selectively for those Federal rates that exceed 9 percent.

(ii) *Three-month rule.* In applying section 1274 (d)(1) and paragraph (e)(1)(i) of this section (relating to date as of which applicable Federal rate is determined) in conjunction with paragraph (d) (2) or (3) of this section, the test rate of interest or testing amount for each of the months must be computed separately. However, paragraph (d) (2) or (3) of this section shall not be applied by making a single calculation using the lowest Federal short-term rate during the 3-month period, the lowest Federal mid-term rate during this period and the lowest Federal long-term rate during this period if those rates do not all occur in the same month.

(5) *Installment obligations not stating adequate interest.* For purposes of applying §1.1274–4 (relating to the determination of the imputed principal of a debt instrument), the imputed rate of interest shall be determined by reference to the last payment of principal. The Commissioner, however, may disregard nominal payments of principal.

(e) *Rate of interest applicable to a sale or exchange*—(1) *Date as of which applicable Federal rate of interest determined*—(i) *General rule.* Except as provided in paragraph (e)(2) of this section, for purposes of § 1.1274–3 and § 1.1274–4, the applicable Federal rate with respect to a debt instrument is the lowest of the applicable Federal rates in effect during the three-month period ending with the month in which the earlier of the following dates occur—

(A) The contract date, or

(B) The date of the sale or exchange.

(ii) *Contract date.* The contract date is the first day on which there is a binding contract (including an irrevocable option) in writing for the sale or exchange. If there is a substantial modification (as defined in paragraph (e)(1)(iii) of this section) of the terms of the contract before the date of the sale or exchange, the date of the last substantial modification is the contract date.

(iii) *Substantial modification.* For the purposes of paragraph (e)(1)(ii) of this section, the term "substantial modification" means any substantial change in the terms of the contract, including any change in the sales price other than a change in the sales price arising from an independent appraisal, mechanical formula or contingency provided for in the contract.

(iv) *Example.* The provisions of paragraph (e)(1) of this section may be illustrated by the following example:

Example. In April 1985, A enters into a binding written contract to sell nonpublicly traded property to B. The contract calls for B to issue, in partial consideration for sale, a 15-year debt instrument calling for semiannual payments of interest. One hundred ten percent of the Federal long-term rates for February, March and April 1985 are 12.74 percent, compounded semiannually, 12.54 percent, compounded semiannually, and 13.06 percent, compounded semiannually, respectively. For purposes of determining whether the debt instrument has adequate stated interest, the applicable Federal rate is 12.54 percent (the lower of the Federal long-term rates for February, March and April 1985).

(2) *Special rules for determining rates for certain contracts*—(i) *In general.* In the case of contracts to which the special rules of paragraph (e)(2) of this section apply, the applicable Federal rate with respect to a debt instrument is that rate in effect on the earlier of—

(A) The contract date, or

(B) The date of the sale or exchange.

(ii) *Contracts to which special rules apply.* The special rules of paragraph (e)(2) of this section apply—

(A) To any contract with a contract date occurring before January 1, 1985, and

(B) For purposes of determining the imputed principal amount of a debt instrument (within the meaning of § 1.1274–4), to any contract with a contract date occurring after December 31, 1984, and before July 1, 1985.

(f) *Treatment of certain options*—(1) *In general.* Paragraph (f) of this section governs whether a put or call option described in § 1.1272–1(f)(4)(ii) or an option to extend described in § 1.1272–1(f)(4)(v) is presumed exercised for purposes of section 1274 and the regulations thereunder. In the case of an option to which paragraph (f) of this section does not apply (for example, an option to extend with an uncertain maturity date), the option is a contingency to which the payments under the debt instrument are subject. For rules relating to contingent payments, see § 1.1275–4.

(2) *Seller's options.* The holder of a debt instrument (the seller) with a put option or option to extend shall be presumed to exercise the option if the testing amount (determined under § 1.1274–3(c)(1)) of the debt instrument, assuming exercise of the option, exceeds the testing amount of the debt instrument, assuming the option is not exercised.

(3) *Buyer's options.* The issuer of a debt instrument (the buyer) with a call option or an option to extend shall be presumed to exercise the option if the testing amount of the debt instrument, assuming exercise of the option, is less than the testing amount of the debt instrument, assuming the option is not exercised.

(4) *Examples.* Paragraph (f) of this section may be illustrated by the following examples:

Example (1). In partial consideration for the sale on nonpublicly traded property, a debt instrument (other than a debt instrument issued in a potentially abusive situation) with a stated principal amount of $1,000,000 is issued. The debt instrument is due in 10 years and calls for annual payments of interest at 8 percent for the first 5 years and 14 percent for the final five years. In addition, the debt instrument provides the buyer (issuer) with the option to call (prepay) the debt instrument at the end of 5 years for its full face amount of $1,000,000. Assume that the applicable Federal mid-term and long-term rates applicable to the sale based on annual compounding are 9 percent and 10 percent, respectively. Assuming exercise of the call option the testing amount that would be determined under § 1.1274–3(c)(1)(i) of this section is $981,103.49 (the present value of all of the payments due within a 5-year term discounted at a test rate of 9 percent, compounded annually). Assuming nonexercise of the call option the testing amount that would be determined under § 1.1274–3(c)(1)(i) of this section is $1,018,335.46 (the present value of all the payments due within a 10-year term discounted at a test rate of 10 percent, compounded annually). Thus, under paragraph (f)(3) of this section, because the testing amount determined under §1.1274–3(c)(1)(i), assuming exercise of the option, is less than the testing amount determined under § 1.1274–3(c)(1)(i), assuming nonexercise of the option, the option is presumed exercised. The presumption applies for purposes of section 1274 including, for example, whether the debt instrument provides for adequate stated interest. Thus, in this example, the debt instrument does not provide for adequate stated interest.

Example (2). The facts are the same as in example (1), except that the seller (holder) has an option to put the debt instrument and require the buyer to retire the debt instrument at the end of 5 years. Because the testing amount determined under § 1.1274–3(c)(1)(i), assuming nonexercise of the option exceeds the amount determined under § 1.1274–3(c)(1)(i), assuming exercise, the option is presumed not to be exercised for purposes of section 1274. Thus, in this example, the debt instrument provides for adequate stated interest.

§ 1.1274–7 **Assumptions.**

(a) *Assumptions in connection with sales or exchanges after June 30, 1985*—(1) *In general.* Section 1274 shall not apply to a debt instrument assumed or taken subject to in connection with a sale or exchange which occurs after June 30, 1985, unless the debt instrument is modified (within the meaning of § 1.1274–1(c)) as part of the sale or exchange.

(2) *Modifications.* If a debt instrument assumed or taken subject to is modified as part of a sale or exchange, the modification shall be treated as a separate transaction taking place either immediately before or immediately after the sale or exchange. The modification of a debt instrument that is attributable to the seller of the property shall be treated as occurring immediately before the sale or exchange. For this purpose, the modification of the debt instrument shall be attributed to the seller of the property unless the seller of the property neither consents to nor participates in the modification. If a modification is treated as taking place immediately before the sale or exchange, the buyer shall be treated as assuming or taking subject to the modified debt instrument. For rules governing the treatment of modifications of debt instruments, see § 1.1274–1(c).

(3) *Examples.* The provisions of paragraph (a) of this section may be illustrated by example (6) of § 1.1273–2(f) and by the following examples:

Example (1). On July 1, 1986, B sells Blackacre to C for $4,000,000, subject to an existing debt instrument with a face amount of $1,000,000. The terms of the debt instrument are not modified as part of the sale or exchange. Under paragraph (a)(1) of this section, the debt instrument is not subject to section 1274.

Example (2). On July 1, 1986, B sells Blackacre to C for $40,000,000 subject to an existing debt instrument held by A with a face amount of $10,000,000 and a remaining term of 7 years that provides for annual interest payments at 10 percent. The debt instrument by its terms is not assumable. However, A desires to raise the rate of interest on the debt instrument. Thus, as part of the sale or exchange, C and A agree (without B's consent) to raise the interest rate to 11 percent. The change in interest rate constitutes a modification under § 1.1001–1(a). Because the debt instrument has been modified, under § 1.1274–1(c) the modified debt instrument is treated as a new debt instrument given in consideration for the old debt instrument. Because B did not consent to or participate in the modification, the modification is treated as taking place immediately after the sale of the property in a transaction involving C and A.

Example (3). On July 1, 1986, B sells Blackacre to C for $40,000,000 subject to an existing debt instrument held by A with a face amount of $10,000,000 and a remaining term of 10 years. This debt instrument provides for annual interest payments at 8 percent. As part of the sale or exchange, A, B, and C jointly agree that the interest rate will be raised to 11 percent and that payment of the interest which accrues during the two years following the assumption will be deferred until maturity. The change in interest rate and deferral of payments constitute a modification under § 1.1001–1(a). Because the debt instrument has been modified, under § 1.1274–1(c) the modified debt instrument is treated as a new debt instrument given in consideration for the old debt instrument. Because B consented to the modification, the modification is treated as taking place immediately before the sale in a transaction involving B and A. C is treated as having assumed the modified debt instrument.

(b) *Assumptions in connection with sales or exchanges occurring after December 31, 1984, and before July 1, 1985*—(1) *Debt instruments that are modified.* If a debt instrument assumed or taken subject to in connection with a sale or exchange that occurs after

December 31, 1984, and before July 1, 1985, is modified (within the meaning of § 1.1274–1(c)) as part of the sale or exchange, the modification shall be treated in accordance with the rules of paragraph (a)(2) of this section.

(2) *Debt instruments that are not modified*—(i) *Sales price in excess of $100,000,000.* Except as provided in paragraph (b)(3) of this section, if a debt instrument is assumed or taken subject to in connection with a sale or exchange that occurs after December 31, 1984, and before July 1, 1985, in which the sales price exceeds $100,000,000 and the debt instrument is not modified as part of the sale or exchange, section 1274 shall apply to the debt instrument solely for purposes of determining the tax consequences of the sale or exchange to the buyer. The sales price in a sale or exchange shall be determined under rules analogous to those set forth in § 1.1274–1(b)(4) (i), (ii), and (iii).

(ii) *Sales price less than or equal to $100,000,000*—(A) *Debt instruments issued after October 15, 1984.* Except as provided in paragraph (b)(3) of this section and section 44(b)(7) of the Tax Reform Act of 1984 (as amended by Pub. L. No. 98–612), if a debt instrument issued after October 15, 1984, is assumed or taken subject to in connection with a sale or exchange that occurs after December 31, 1984, and before July 1, 1985, in which the sales price is less than or equal to $100,000,000 and the debt instrument is not modified as part of the sale or exchange, section 1274 shall apply to the debt instrument solely for purposes of determining the tax consequences of the sale or exchange to the buyer.

(B) *Debt instruments issued before October 16, 1984.* If a debt instrument issued before October 16, 1984, is assumed or taken subject to in connection with a sale or exchange that occurs after December 31, 1984, and before July 1, 1985, in which the sales price is less than or equal to $100,000,000 and the debt instrument is not modified as part of the sale or exchange, section 1274 shall not apply to the debt instrument.

(3) *Exception.* Notwithstanding paragraph (b)(2) of this section, section 1274 shall not apply to any debt instrument assumed or taken subject to in a sale or exchange that occurs after December 31, 1984, and before July 1, 1985, and in which the debt instrument is not modified, if—

(A) The property is not 3-year or 5-year property (within the meaning of section 168(c)(2)) or property described in section 1221(1) (relating to stock in trade, inventories, and other property held for sale to customers) to the buyer, or

(B) In the case of recovery property (within the meaning of section 168(c)(1)) other than 3 year or 5-year property, the remaining term of the debt instrument exceeds two-thirds of the recovery period for such property.

This paragraph (b)(3) shall not apply to the purchase of an interest in an entity if the bases of the underlying assets of the entity are determined, in whole or in part, by reference to the amount paid for such interest and the underlying assets include a more than nominal amount of recovery property or property described in section 1221(1). For example, if a corporation purchases stock in another corporation owning a more than nominal amount of recovery property or property described in section 1221(1) and makes an election under section 338 (relating to certain stock purchases treated as asset acquisitions), the exception contained in this paragraph (b)(3) shall not apply.

(c) *Wraparound indebtedness.* For purposes of this section, a debt instrument originally issued by the buyer of property to the seller in consideration for the sale of the property shall not be treated as a debt instrument assumed or taken subject to, even if the seller is liable to a third party with respect to an indebtedness secured by the property.

(d) *Consideration attributable to assumed debt*—(1) *In general.* If, as part of the consideration for the sale or exchange of property, the buyer assumes or takes subject to an indebtedness that was issued at a discount (including a debt instrument issued in a prior sale or exchange to which section 1274 applied), the portion of the buyer's basis in the property and the seller's amount realized attributable to the debt instrument shall be equal to the revised issue price of the debt instrument (as defined in § 1.1275–1(h)) as of the date of the sale or exchange.

(2) *Example.* The provisions of paragraph (d)(1) of this section may be further illustrated by the following example:

Example. On July 1, 1986, X sells real property to Y in exchange for $3,500,000 in cash and Y's agreement to assume an existing debt instrument secured by the property. The debt instrument was originally issued at a discount. The face amount of the debt instrument is $1,000,000 and its revised issue price under section 1272 as of the date of the sale is $850,000. The debt instrument is not modified as part of the sale or exchange. Thus, the debt instrument is not subject to section 1274. Y's basis in the property is $4,350,000 (the sum of the cash payment ($3,500,000) and the revised issue price of the debt instrument ($850,000)).

§ 1.1274A–1 Special rules for certain transactions where stated principal amount does not exceed $2,800,000.

(a) *In general.* This section provides special rules applicable to a qualified debt instrument as defined in paragraph (b) of this section. For rules relating to the test and imputed rates of interest applicable to a qualified debt instrument, see § 1.1274–3(e)(1)(ii) and § 1.1274–4(b)(1) (or, in the case of a qualified debt instrument subject to section 483, § 1.483–4(a)).

(b) *Definition of qualified debt instrument*—(1) *In general.* The term "qualified debt instrument" means any debt instrument given in consideration for the sale or exchange of property after June 30, 1985, whose stated principal amount does not exceed the qualified amount as defined in paragraph (b)(2) of this section. The term "qualified debt instrument," however, does not include a debt instrument issued in exchange for new section 38 property (within the meaning of section 48(b) and the regulations thereunder) or a debt instrument issued in a sale-leaseback transaction (within the meaning of § 1.1274–3(e)(1)(iii)).

(2) *Qualified amount.* The term "qualified amount" means—

(i) $2,800,000, or

(ii) In each calendar year after 1989, $2,800,000 increased for inflation in the manner prescribed in paragraph (e) of this section.

(3) *Debt instruments calling for contingent payments.* If all or part of the consideration given in a sale or exchange consists of contingent payments, a debt instrument is a qualified debt instrument only if it can be determined at the time of the sale or exchange that the maximum amount of the stated principal due under the debt instrument cannot exceed the qualified amount as defined in paragraph (b)(2) of this section. For example, assume the facts as in § 1.1274–3(e)(5) example (4) except that the sale takes place in April 1, 1986. Since it cannot be determined at the time of the sale or exchange that the maximum stated principal amount cannot exceed $2,800,000, the debt instrument is not a qualified debt instrument. Thus, the test rate of interest applicable to the sale is the applicable Federal rate as determined under § 1.1274–3(e)(1)(i).

(c) *Election to use cash method in certain cases*—(1) *In general.* Section 1274 does not apply to any cash method debt instrument (within the meaning of paragraph (c)(2) of this section). The interest (including unstated interest under section 483) on a cash method debt instrument shall be taken into account by both the borrower and the lender under the cash receipts and disbursements method of accounting. See § 1.446–2.

(2) *Meaning of cash method debt instrument.* For purposes of paragraph (c) of this section, the term "cash method debt instrument" means a qualified debt instrument as defined in paragraph (b) of this section if—

(i) The stated principal amount of the qualified debt instrument does not exceed the cash method amount as defined in paragraph (c)(3) of this section,

(ii) The lender does not use an accrual method of accounting and is not a dealer with respect to the type of property sold or exchanged,

(iii) Section 1274 would have applied to the debt instrument but for the application of section 1274A(c) and paragraph (c) of this section, and

(iv) An election described in paragraph (c)(4) of this section is made with respect to the debt instrument.

For purposes of this paragraph (c)(2), all sales or exchanges which are part of the same transaction (or a series of related transactions) shall be aggregated in accordance with the rules of paragraph (d) of this section, and all debt instruments arising from the aggregated sales or exchanges shall be treated as one debt instrument.

(3) *Cash method amount.* The term "cash method amount" means—

(i) $2,000,000, or

(ii) In each calendar year after 1989, $2,000,000 increased for inflation in the manner prescribed in paragraph (e) of this section.

(4) *Debt instruments calling for contingent principal.* If all or part of the consideration given in a sale or exchange consists of contingent payments, a debt instrument cannot be a cash method debt instrument unless it can be determined at the time of the sale or exchange that the maximum amount of the stated principal due under the debt instrument cannot exceed the cash method amount as defined in paragraph (c)(3) of this section.

(5) *Election*—(i) *In general.* An election is described in this paragraph (c)(4) if both the borrower (issuer) and the lender (holder) jointly elect to treat the debt instrument as a cash method debt instrument.

(ii) *Time and manner of making election.* The borrower and lender shall make the election described in paragraph (c)(4)(i) on or before the last day for filing (including extensions) the returns of the borrower and the lender for the taxable year of issue of the debt instrument. The election shall be made by attaching to the returns a statement signed by the borrower and lender that includes the following information—

(A) The names, addresses and taxpayer identification numbers of the borrower and lender,

(B) A clear indication that an election is being made under paragraph (c)(4) of this section, and

(C) A statement that the debt instrument with respect to which the election is being made fulfills the requirements of a cash method debt instrument.

For sales or exchanges in 1985, the election may be made by filing an amended return if either the borrower or lender filed their returns for the taxable year which includes the date of the sale or exchange prior to May 8, 1986.

(6) *Successors of electing parties.* Except as otherwise provided in this paragraph (c)(5), paragraph (c)(1) of this section shall apply to any successor of the electing lender or borrower (or any transferee thereof). Thus, for any period after the transfer of a cash method debt instrument, the successor shall take into account the interest (including unstated interest) thereon under the cash receipts and disbursements method of accounting. Nevertheless, if the lender (or any successor thereof) transfers the cash debt instrument to a taxpayer who uses an accrual method of accounting, then paragraph (c)(1) of this section shall not apply to the successor of the lender (or a successor thereof) with respect to the cash method debt instrument for any period after the date of the transfer and section 1272 shall apply.

(7) *Special rules.* [Reserved]

(d) *Aggregation of transactions*—(1) *General rule.* All sales or exchanges which are part of the same transaction or a series of related transactions shall be treated as a single sale or exchange. Whether two or more sales or exchanges are treated as a single sale or exchange depends on all the facts and circumstances surrounding the sales or exchanges.

(2) *Examples.* The following examples illustrate the rules of paragaraph (d) of this section:

Example (1). In two transactions evidenced by separate sales agreements, A sells undivided half interests in Blackacre to B. The sales are pursuant to a plan for the sale of a 100 percent interest in Blackacre to B. These sales or exchanges are part of a series of related transactions and, thus, are treated as a single sale or exchange.

Example (2). Pursuant to a plan, unrelated individuals X and Y purchase undivided half interests in Blackacre from A and subsequently contribute these interests to a partnership in exchange for equal interests in the partnership. These purchases are treated as part of the same transaction and, thus, are treated as a single sale or exchange.

Example (3). Fifteen unrelated individuals own all the stock of X Corporation. Y Corporation makes a tender offer to these 15 shareholders. The terms offered to each shareholder are identical. Shareholders holding a majority of the shares of X Corporation elect to tender their shares pursuant to Y Corporation's offer. These sales are part of the same transaction and, thus, are treated as a single sale or exchange.

Example (4). Pursuant to a newspaper advertisement, X Corporation offers for sale similar condominiums in a single building. The prices of the units vary due to a variety of factors, but the financing terms offered by X Corporation to all buyers are identical. The units are purchased by unrelated buyers who decided whether to purchase units in the building at the price and on the terms offered by X Corporation, without regard to the actions of other buyers. Because each buyer acts individually, the sales are not part of the same transaction or a series of related transactions and, thus, are treated as separate sales or exchanges.

(e) *Inflation adjustment of dollar amounts*—(1) *In general.* For each calendar year after 1989, the qualified amount as defined in paragraph (b)(2) of this section and the cash method amount as defined in paragraph (c)(3) of this section shall be determined by multiplying each of those amounts for the year 1988 by the inflation adjustment for the calendar year. Any amount determined under paragraph (e) of this section shall be rounded to the nearest multiple of $100 (or, if the increase is an odd multiple of $50, the increase shall be increased to the nearest multiple of $100).

(2) *Inflation adjustment.* For purposes of paragraph (e)(1) of this section, the inflation adjustment for any calendar year is the ratio of—

(i) The CPI for the preceding calendar year, to

(ii) The CPI for calendar year 1988.

For purposes of this paragraph (e)(2), the CPI for any calendar year is the average of the Consumer Price Index as of the close of the 12-month period ending on September 30 of the calendar year.

(3) *Publication of increased dollar amounts.* The dollar amounts adjusted for inflation as provided in paragraph (e)(1) and (e)(2) of this section shall be determined after the close of the 12-month period ending on September 30, 1988, and each succeeding calendar year. The increased dollar amount shall be published in Revenue Rulings.

§ 1.1275–1 Definitions relating to treatment of debt instruments.

(a) *Applicability.* The definitions contained in this section are applicable for purposes of sections 163(e) and 1271 through 1275 and the regulations thereunder.

(b) *Debt instrument*—(1) *In general.* Except as provided in paragraph (b)(2) of this section, the term "debt instrument" means a bond, debenture, note, certificate, or other evidence of indebtedness, including all rights to deferred payments under a contract, whether or not evidenced by a formal instrument. The term "debt instrument" also includes face-amount certificates as defined in sections 2(a)(15) and (4) of the Investment Company Act of 1940 (15 U.S.C. 80a–2 and 80a–4) as well as certificates of deposit, time deposits, bonus plans, and other deposit arrangements with banks, domestic building and loan associations, and similar financial institutions. A debt instrument includes an instrument calling for payments in the form of cash, stock, securities, or any other property (other than a debt instrument issued by the same obligor).

(2) *Exception.* The term "debt instrument" does not include any annuity contract to which section 72 applies and which—

(i) Depends (in whole or in substantial part) on the life expectancy of one or more individuals, or

(ii) Is issued by an insurance company subject to tax under subchapter L—

(A) In a transaction in which there is no consideration other than cash or another annuity contract meeting the requirements of paragraph (b)(2)(ii) of this section,

(B) Pursuant to the exercise of an election under an insurance contract by a beneficiary thereof on the death of the insured party under the contract, or

(C) In a transaction involving a qualified pension or employee benefit plan.

(c) *Issue date*—(1) *Publicly offered debt instruments.* In the case of debt instruments that are publicly offered (as described in § 1.1273–2(a)(2)), the term "issue date" means the settlement date.

(2) *Non-publicly offered debt instruments not issued for property.* In the case of debt instruments to which section 1273(b)(2) applies, the term "issue date" means the date on which the debt instrument was sold by the issuer. For purposes of this paragraph (c)(2), this date shall be considered to be the settlement date.

(3) *Other debt instruments.* In the case of debt instruments not described in paragraphs (c)(1) or (c)(2) of this section, the term "issue date" means the date on which the debt instrument is exchanged for property.

(d) *Tax-exempt obligations.* The term "tax-exempt obligation" means a debt instrument with respect to which all of the interest—

(1) Is not included in gross income under section 103, or

(2) Is exempt from tax (without regard to the identity of the holder) under any other provision of law.

(e) *Issue.* Two or more publicly offered debt instruments (as described in § 1.1273–2(a)(2)) are part of the same issue if they have the same credit and payment terms, and are sold at substantially the same time pursuant to a common plan of marketing. Two or more debt instruments that are not publicly offered are part of the same issue if they are issued as part of a single transaction or a series of related transactions.

(f) *Premium.* A debt instrument is purchased at a premium if its purchase price exceeds its stated redemption price at maturity. If, under chapter 1 of the Code, the basis of a debt instrument in the hands of the holder is determined, in whole or in part, by reference to the basis of the debt instrument in the hands of another person who purchased the debt instrument at a premium, then the holder shall be considered to have purchased the debt instrument at a premium. Thus, for example, the donee of a debt instrument purchased at a premium by the donor shall be considered to have purchased the debt instrument at a premium.

(g) *Debt instruments issued by a natural person.* A debt instrument issued by an entity other than a natural person shall not be considered to be issued by a natural person merely because a natural person may be a co-maker and may be jointly liable for the debt instrument's repayment. A debt instrument issued by a partnership is considered to be issued by the partnership as an entity even if the partnership is composed entirely of natural persons.

(h) *Revised issue price.* The term "revised issue price" (as defined in section 1278(a)(4)) means the sum of—

(1) The issue price of the debt instrument (as defined in section 1273(b) and § 1.1273–2), and

(2) The aggregate amount of the original issue discount previously includable in the gross income of all holders (determined without regard to sections 1272 (a)(6) or (b)(4) or § 1.1272–1(g)).

§ 1.1275-2 Special rules relating to debt instruments.

(a) *Reorganizations.* (1) *Debt instruments issued after December 13, 1982.* If a debt instrument (referred to in paragraph (a) of this section as the new debt instrument) is issued after December 13, 1982, pursuant to a plan of reorganization as described in paragraph (a)(3) of this section for another debt instrument (referred to in paragraph (a) of this section as the old debt instrument), and the amount which (but for this paragraph (a)(1)) would have been the issue price of the new debt instrument is less than the revised issue price of the old debt instrument, then the issue price of the new debt instrument shall be treated as equal to the revised issue price of the old debt instrument. For purposes of paragraph (a) of this section, the term "debt instrument" includes an investment unit. See § 1.1273–2(d) for rules relating to the allocation of issue price to an investment unit. For a special rule regarding deductibility of original issue discount by the issuer under paragraph (a) of this section, see section 1275(a)(4)(B)(ii)(II).

(2) *Debt instruments issued before December 14, 1982.* If a new debt instrument is issued before December 14, 1982, pursuant to a plan of reorganization, the issue price of the new debt instrument is equal to its stated redemption price at maturity.

(3) *Reorganization.* For purposes of paragraph (a) of this section, a reorganization includes a reorganization within the meaning of section 368(a)(1) or an insolvency reorganization within the meaning of section 371, 373, or 374. A reorganization does not include a transfer pursuant to section 351.

(4) *Example.* The rule set forth in paragraph (a) of this section may be illustrated by the following example:

Example. On January 1, 1986, in a reorganization transaction (within the meaning of paragraph (a)(3) of this section), N Corporation issues a series of 20-year bonds in exchange for an outstanding issue of original issue discount bonds having a revised issue price on that date of $8,750 and a fair market value of $8,600. The 20-year bonds issued pursuant to the reorganization call for a payment of $10,000 at maturity and for annual payments of interest at a rate of 10%, compounded annually ($1,000). Assume that the outstanding issue of original issue discount bonds is publicly traded. The issue price of the newly issued bonds under paragraph (a)(1) of this section is the revised issue price of the outstanding bonds, $8,750.

(b) [Reserved]

(c) *Debt instruments distributed by corporations with respect to stock*—(1) *In general.* In the case of a debt instrument issued by a corporation with respect to its stock, such debt instrument shall be treated as if it had been issued by the corporation for property.

(2) *Examples.* The rule set forth in paragraph (c)(1) of this section may be illustrated by the following examples:

Example (1). On January 1, 1986, M Corporation distributes to A, a shareholder of the corporation, a bond paying $10,000 at maturity on December 31, 1990, and calling for semiannual interest payments at a rate of 10%, compounded semiannually ($500). Assume that the bond is publicly traded and has a fair market value on that date of $10,000. The issue price of the M Corporation bond is, under section 1273(b)(3) and § 1.1273-2(c)(1), $10,000. A has a dividend of $10,000 upon receipt of the bond.

Example (2). The facts are the same as in example (1), except that the bond is not publicly traded. Assume that the test rate of interest is 11%, compounded semiannually. The issue price of the bond is its imputed principal amount under § 1.1274-4 of $9,273.31, discounting at the test rate of 11%, compounded semiannually. A has a dividend of $9,273.31 upon receipt of the bond.

(d) *Aggregation of debt instruments*—(1) *General rule.* All debt instruments, whether or not issued for property, issued in connection with the same transaction or a series of related transactions or as part of the same issue shall be treated together as a single debt instrument with a single issue price, maturity date, yield, and stated redemption price at maturity for purposes of sections 1271 through 1275 and the regulations thereunder, except as provided in paragraph (d)(2) of this section. A single installment obligation (as defined in § 1.1273-1(b)(2)(i)) shall be subject to the rule described in the preceding sentence. Whether debt instruments are issued in connection with the same transaction or a series of related transactions shall be determined in accordance with all the facts and circumstances surrounding the issuance of the debt instrument. See § 1.1274A-1(d).

(2) *Exception.* Paragraph (d)(1) of this section shall not apply if—

(i) Each debt instrument held by the taxpayer is part of a series that is separately traded on an established securities market, or

(ii) (A) Each debt instrument held by the taxpayer is issued in exchange for property; (B) each instrument calls for interest at the lowest rate (or fixed multiple thereof) that constitutes adequate stated interest within the meaning of section 1274(c)(2) and § 1.1274-3; and (C) all interest under each debt instrument is qualified periodic interest within the meaning of § 1.1273-1(b)(1)(ii).

(3) *Effective date.* In general, the rules stated in paragraph (d) of this section shall apply to all installment obligations issued after December 31, 1984, and to all other debt instruments that are issued on or after May 8, 1986. The issuer and holder may elect jointly, however, to apply these rules to serial debt instruments issued after December 31, 1984. Conversely, the issuer and the holder may elect to treat each payment of principal made under an installment obligation issued after December 31, 1984, and before May 8, 1986, as a separate debt instrument maturing serially. The issuer and the holder shall notify the Secretary of this election on their tax returns for their respective taxable years in which the debt instrument(s) is (are) issued. If no election is made, the rules of paragraph (d) of this section shall apply unless the parties have provided for two or more debt instruments maturing serially, in which case the rules of § 1.1232-3(b)(2)((iv)(e) shall apply.

(4) *Example.* The rules set forth in paragraph (d) of this section may be illustrated by the following example:

Example. On January 1, 1987, A sells property to B in exchange for two debt instruments. The first debt instrument has a stated principal amount (as defined in § 1.1274-2) of $500,000, payable in two years. The debt instrument calls for annual payments of interest at a rate of 20%. The second debt instrument also has a stated principal amount of $500,000, and is payable in 10 years. That debt instrument calls for annual payments of interest at a rate of 10%, compounded annually. Assume that the Federal short-term rate on January 1, 1987 is 8%, compounded annually, and that the Federal long-term rate on that date is 10%, compounded annually. Thus, both instruments have adequate stated interest within the meaning of section 1274 and § 1.1274-3. Under paragraph (d)(1) of this section, the two debt instruments will be treated as a single installment obligation because they are part of a single issue and the debt instruments do not satisfy the requirements of paragraph (d)(2) of this section. The combined debt instrument has an issue price of $1,000,000 and a yield of 12.32%, compounded annually. The debt instrument has $100,000 of original issue discount since one-half ($50,000) of each payment of interest on the 2-year debt instrument is not qualified periodic interest within the meaning of § 1.1273-1(b)(1)(ii) when the two debt instruments are aggregated.

The allocation of original issue discount and principal to each of the ten annual accrual periods under the single installment obligation is set forth in the table below:

Year	Payment	Principal	Interest accrued	Qualified periodic interest	OID
1	$150,000	$26,819.35	$123,180.65	$100,000	$23,180.65
2	650,000	530,122.97	119,877.03	100,000	19,877.03
3	50,000	0	54,576.11	50,000	4,576.11
4	50,000	0	55,139.82	50,000	5,139.82
5	50,000	0	55,772.95	50,000	5,772.95
6	50,000	0	56,484.07	50,000	6,484.07
7	50,000	0	57,282.78	50,000	7,282.78
8	50,000	0	58,179.87	50,000	8,179.87
9	50,000	0	59,187.48	50,000	9,187.48
10	550,000	443,057.68	60,319.20	50,000	10,319.20
	1,700,000	1,000,000.00	700,000.00	600,000	100,000.00

(e) *Counting conventions*—(1) *Whole accrual periods.* All whole accrual periods, whether expressed annually, semiannually, quarterly, or monthly, or with reference to any other time period, shall be treated as having equal length. For example, a leap year shall be treated as having the same number of days as a non-leap year; all whole months shall be treated as having the same number of days.

(2) *Short accural periods.* In computing the length of a short accural period, any reasonable convention may be used. Common conventions are "30 days per month/360 days per year", "actual days per month/actual days per year", and "actual days per month/360 days per year". The examples in the regulations under sections 1271 through 1275 use the "30 days per month/360 days per year" convention.

(3) *Amounts payable on the first day of a month*—(i) *In general.* If a debt instrument calls for amounts payable on the first day or the first business day of a month either party to the debt instrument may treat such amounts as payable on the last day of the preceding month. This treatment shall be applied consistently throughout the entire term of the debt instrument and applies for all Federal tax purposes.

(ii) *Example.* A debt instrument is issued on January 1, 1986, providing for payments of interest on July 1 and January 1 of each calendar year through January 1, 2016. Either party may treat the debt instrument as providing for payments of interest on June 30 and December 31 of each calendar year through December 31, 2015.

(f) *Treatment of certain loans for personal use*—(1) *Sections 1274 and 483 not to apply.* In the case of the obligor under any debt instrument given in consideration for the sale or exchange of property, sections 1274 and 483 shall not apply if such property is personal use property (as defined in paragraph (f)(3) of this section). Sections 1274 and 483 shall not apply to either the obligor or the obligee of a debt instrument described in paragraph (f)(1)(i) of this section if the debt instrument is also described in section 7872(c)(1) (A) through (C) and the regulations thereunder. See §§ 1.1274–1(b)(7) and 1.483–1(c)(3)(iii).

(2) *Original issue discount deducted on cash basis in certain cases*—(i) *In general.* In the case in which—

(A) A debt instrument is incurred in connection with the acquisition or carrying of personal use property.

(B) This debt instrument has original issue discount (determined after the application of paragraph (f)(1) of this section), and

(C) The obligor under this debt instrument uses the cash receipts and disbursements method of accounting.

then notwithstanding section 163(e) and the regulations thereunder, the original issue discount on such debt instrument shall not be deductible prior to the time when the original issue discount is paid. The preceding sentence notwithstanding, if the amount of original issue discount is *de minimis*, the rule of § 1.163–7(d) shall apply.

(ii) *Time when original issue discount treated as paid.* For purposes of section 1275(b) and paragraph (f)(2) of this section, any amount designated as interest by the parties with respect to a debt instrument described in paragraph (f)(2)(i) of this section but treated as original issue discount because this interest is not qualified periodic interest (as defined in § 1.1273–1(b)(1)(ii)) shall be treated as paid solely by reference to the terms of the debt instrument.

(3) *Definition of personal use property.* The term "personal use property" means any property substantially all of the use of which by the taxpayer is not in connection with a trade or business of the taxpayer or an activity described in section 212. The determination whether property is described in the preceding sentence shall be made as of the issue date of the debt instrument.

(4) *Examples.* The provisions of this paragraph (f) may be illustrated by the following examples:

Example (1). The facts are the same as in § 1.1272–1(k), Example (9), except that the property sold is personal use property in B's hands. Accordingly, B is not entitled to deduct original issue discount until paid. Thus, B may not deduct any amount as interest for 1986 or 1987 because no amount of interest is paid during those years. In each of the years 1988 through 1995, the amount B may deduct as interest is the stated interest amount of $450,000.

Example (2). (i) A borrows $100,000 from bank B to purchase a residence. As part of the condition for obtaining the loan, B charges A $4,000 in points. A chooses not to pay the points at closing, but instead borrows the $4,000 from B on the same terms as the $100,000. Accordingly, A becomes obligated to B for a total amount of $104,000. The $104,000 is payable in 360 monthly installments of $1,069.76, each payment consisting of a partial payment of principal and interest at a rate of 12% on the outstanding principal balance. A's debt instrument is a self-amortizing installment obligation (within the meaning of § 1.1273–1(b)(2)(iii)).

(ii) A's debt instrument has a stated redemption price at maturity of $104,000 and an issue price of $100,000. Accordingly, the points that A is obligated to pay to B take the form of original issue discount. Under the safe harbor test of § 1.1273–1(a)(3)(ii)(B), A's debt instrument has a *de minimis* amount of original issue discount. Therefore, under § 1.163–7(d), the amount of original issue discount allocable to each principal payment is $4,000/360=$11.11 (notwithstanding the fact that the earlier principal payments are less than $11.11). In a year in which A makes 12 monthly payments, the amount of original issue discount deductible by A is $133.33.

§ 1.1275–3 Original issue discount information reporting requirements.

(a) *Information required to be set forth on face of debt instrument.* In the case of any debt instrument issued after May 8, 1986, that has original issue discount and is not described in section 1272(a)(2) or § 1.1272–1(a)(2), the issuer shall set forth on the face of the debt instrument the amount of the original issue discount (as defined in section 1273(a)(1) and § 1.1273–1(a)), the issue date (as defined in section 1275(a)(2) and § 1.1275–1(c)), the yield to maturity (as defined in § 1.1272–1(f)) as well as the method used to determine yield where there is a short accrual period, and the amount of original issue discount allocable to the short accrual period. In cases where it is not possible to set forth the information required by this paragraph (a) on the face of the instrument by the issue date, the issuer shall deliver to the holder of the debt instrument a sticker containing this information within 10 days of the issue date. In the case of any debt instrument that is not publicly offered (within the meaning of § 1.1273–1(a)(2)), however, the requirements stated in this paragraph (a) shall apply only upon a disposition of the debt instrument that occurs after May 8, 1986, by the first holder. For rules relating to the penalty imposed for failure to show the information required by this section on the debt instrument, see section 6706(a) and the regulations thereunder.

(b) *Information required to be reported to Secretary*—(1) *In general.* In the case of any issue of publicly offered debt instruments issued after August 16, 1984, that have original issue discount, the issuer (as defined in paragraph (c) of this section) shall make an information return on Form 8281. The preceding sentence shall not apply to: (i) An issue of debt instruments described in section 1272(a)(2), (ii) certificates of deposit, and (iii) unless otherwise required by the Commissioner pursuant to a Revenue Procedure, stripped bonds and coupons (within the meaning of section 1286).

(2) *Information required to be reported.* The following information shall be reported to the Secretary on Form 8281—

(i) The name, address, and taxpayer identification number of the issuer;

(ii) The issue date (as defined in section 1275(a)(2)), maturity date, and CUSIP number of the issue;

(iii) The amount of original issue discount for the entire issue (as defined in section 1273(a));

(iv) The issue price (as defined in section 1273(b)) expressed as a percentage of the principal amount;

(v) The stated redemption price at maturity of the entire issue, or of each debt instrument within the issue if in denominations of other than $1,000;

(vi) The stated interest rate and the interest payment dates;

(vii) A description of the debt instrument, or, in place of the description, a copy of the offering circular or prospectus, which description shall include a statement of any terms and conditions of the instrument that govern—

(A) Whether payments of principal may be made prior to maturity of the debt instrument;

(B) Whether the debt instrument is part of an investment unit;

(C) Whether the debt instrument is issued in an exchange described in section 368(a);

(D) Whether the debt instrument is part of a serial issue; and

(E) Whether the debt instrument is a stripped bond or stripped coupon.

(viii) The method selected for computing the amount of original issue discount allocable to a short accrual period; and

(ix) Such other information as is required by the form.

(3) *Time and manner of filing of information return*—(i) The information return required by paragraph (b)(1) of this section shall be filed on Form 8281 with the Internal Revenue Service at the address specified on the form. This return must be made on Form 8281 regardless of whether other information

returns are filed by use of electronic media.

(ii) Form 8281 shall be filed with respect to each issue of publicly offered debt instruments—

(A) For debt instruments issued after May 31, 1985, within 30 days after the issue date; and

(B) For debt instruments issued after August 16, 1984, and before June 1, 1985, on or before July 1, 1985.

(4) *Penalty.* For rules relating to the penalty provided for failure to make an information return under paragraph (b) of this section, see section 6706 (b) and the regulations under that section.

(c) *Issuer.* For purposes of this section, the term "issuer" includes not only domestic issuers but also any foreign issuer who is otherwise subject to United States income tax law, unless the issue is neither listed on an established securities market (as defined in § 1.453-3(d)(4)) in the United States nor offered for sale or resale in the United States in connection with its original issuance.

§ 1.1275-4 Contingent payments.

(a) *Applicability.* The rules of this section apply to debt instruments that provide for one or more contingent payments (as defined in paragraph (b) of this section). Contingent payments under a debt instrument subject to section 1274 are governed by the provisions of paragraphs (c) or (d), whichever is applicable. Contingent payments under a debt instrument issued for cash or publicly traded property are governed by the provisions of paragraphs (e) or (f) whichever is applicable. Nothing in this section or in the regulations under sections 1271 through 1274 shall influence whether an instrument calling for contingent payments is properly treated as debt or equity, or whether such instrument evidences a valid indebtedness for Federal income tax purposes.

(b) *Definition of contingent payment*—(1) *In general.* In determining whether a payment called for under a debt instrument is a contingent payment, remote and incidental contingencies may be disregarded by the Commissioner. The parties to the transaction, however, are bound by its form. Thus, neither party may treat any amount under a debt instrument whose payment is subject to a stated contingency as noncontingent. A payment shall not be considered a contingent payment merely because the amount of or the liability for the payment may be impaired by insolvency or default. Variable payments of interest based on current values of an objective interest index (as defined in § 1.1275-5), if made under a debt instrument issued for cash or publicly traded property to which § 1.1275-5(a) applies or if made under a debt instrument to which § 1.1274-3(d)(1)(i) applies, shall not be treated as contingent payments, and if made under a debt instrument to which § 1.1274-3(d)(1)(i) does not apply, shall be treated as contingent payments to the extent provided in § 1.1274-3(d)(1)(iv).

(2) *Certain debt instruments providing for payments contingent only as to time.* In the case of a debt instrument that calls for fixed or minimum payments of principal uncertain as to the time of payment, and that calls for payments of interest on the unpaid principal balance at a fixed or variable rate (which, in a transaction subject to section 1274, constitutes adequate stated interest), such payments shall not be treated as contingent payments (within the meaning of paragraph (b) of this section) and the provisions of § 1.1272-1(c) (in the case of a fixed rate) or §§ 1.1272-1(f)(3)(ii) and 1.1275-5(d) (in the case of a variable rate) shall apply to determine the amount of original issue discount allocable to each accrual period under the debt instrument. See §1.1272-1(k), Example (14). Payments of principal in excess of the minimum amount of principal (other than payments of principal accompanied by adequate stated interest), however, shall be treated as contingent payments.

(c) *Debt instruments subject to section 1274*—(1) *Separation into noncontingent and contingent components.* Except as otherwise provided in section 1274 and the regulations thereunder, in the case of a debt instrument (the "overall debt instrument") subject to section 1274 that calls for one or more contingent payments (other than a debt instrument described in paragraph (d) of this section), the noncontingent payments shall be subject to the rules described in paragraph (c)(2) of this section, and the contingent payments shall be accounted for separately under the provisions of paragraph (c)(3) of this section.

(2) *Treatment of noncontingent payments.* The noncontingent payments under an overall debt instrument described in paragraph (c)(1) of this section shall be treated under sections 1271 through 1275 and the regulations thereunder as a separate noncontingent debt instrument. The issue price of this separate noncontingent debt instrument is the issue price of the overall debt instrument, determined under §§ 1.1274-2(b) and 1.1274-3(d)(2) (if applicable). The stated redemption price at maturity is determined under § 1.1273-1(b)(1), and yield is determined under § 1.1272-1(f), both without reference to the contingent payments. The *de minimis* rule of section 1273(a)(3) and § 1.1273-1(a)(3) shall not apply to the noncontingent debt instrument.

(3) *Treatment of contingent payments*—(i) *In general.* Except as provided in paragraph (c)(3)(iii) of this section, the portion of the payment treated as interest is includible in gross income by the holder and deductible from gross income by the issuer in their respective taxable years in which the amount of the payment becomes fixed.

(ii) *Recharacterization of certain contingent payments.* Any contingent payment made under a debt instrument to which section 1274 applies, other than a contingent principal payment accompanied by a payment of adequate stated interest, shall be treated as consisting of—

(A) A payment of principal in an amount equal to the present value of the payment, determined by discounting the payment at the test rate (using the exact method for short periods) from the date that the amount of the payment becomes fixed to the issue date, and

(B) A payment of interest in an amount equal to the excess of the total amount of the payment over the amount treated as principal.

The preceding sentence notwithstanding, the total amount treated as principal under an overall debt instrument to which section 1274 applies that calls for a fixed or a maximum stated principal amount shall not exceed this fixed or maximum stated principal amount. Once the total of the noncontingent principal payments due under the debt instrument and the portion of the contingent payments treated as principal exceeds the amount described in the preceding sentence, any additional contingent payments shall be treated entirely as interest.

(iii) *Certain delayed contingent payments*—(A) *In general.* In the case in which a contingent payment is not due within six months of the date on which the amount of the payment becomes fixed, the parties shall be treated as if the borrower had issued a separate debt instrument on the date the amount of the payment becomes fixed, maturing on the date that the payment is due. This separate debt instrument shall be treated as a debt instrument to which section 1274 applies. The stated principal amount of this separate debt instrument shall be the amount of the payment that becomes fixed. An amount equal to the issue price of this debt instrument shall be characterized as interest or principal under the rules of paragraph (c)(3)(ii) of this section and accounted for under paragraph (c)(3)(i) of this section, as if an amount equal to the issue price had been paid by the borrower to the lender on the date that the amount of the payment becomes fixed. To determine the issue price of the separate debt instrument, all payments under the debt instrument shall be discounted from the maturity date to the date that the amount of the payment becomes fixed. The amount of a contingent payment shall be treated as fixed even if, once fixed, the payment is payable in the future together with interest that is subject to further contingencies.

(B) *Special rules.* In applying section 1274 to a separate debt instrument described in paragraph (c)(3)(iii)(A) of this section, any provision calling for a test rate other than the applicable Federal rate shall apply if, and only if, such provision applies to the overall debt instrument. (For example, the 9 percent maximum discount rate of section 1274A (a) and § 1.1274A–1(a) applies if the overall debt instrument satisfies the test of § 1.1274A–1(b)(3)). The test rates under paragraphs (c)(3)(ii) and (c)(3)(iii)(A) of this section shall be based on the applicable Federal rates in effect on the date of the sale or exchange (or, if applicable, the contract date), and shall be based on a term beginning on the date the overall debt instrument is issued and ending on the date the contingent payment is due.

(4) *Examples.* The provisions of paragraph (c) of this section may be illustrated by the following examples:

Example (1). (i) A owns Blackacre, unencumbered depreciable real estate. On April 1, 1986, A sells Blackacre to B for a stated purchase price of $6,000,000. B makes a down payment of $1,000,000 and issues to A a debt instrument calling for $5,000,000 to be paid in 5 years, with fixed interest of 6% and contingent interest of up to an additional 8%. Both fixed and contingent interest are payable annually on March 31 of each year from 1987 to 1991. The contingent interest payment in each year is calculated according to a formula that depends on the gross rents B receives from Blackacre during the preceding calendar year. Assume that B's debt instrument does not have adequate stated interest under § 1.1274–3, that the Federal short-term rate is 10%, compounded annually, and that the Federal mid-term rate is 11%, compounded annually.

(ii) The issue price of B's noncontingent debt instrument under paragraph (c)(2) of this section is determined by considering only the five fixed interest payments of $300,000 and the principal payment of $5,000,000. The present value, under § 1.1274–5, of the fixed payments under the overall debt instrument, using a discount rate equal to the Federal mid-term rate of 11%, compounded annually, is $4,076,025.75. This amount is also the issue price of the noncontingent debt instrument. B's basis in Blackacre is thus initially limited to $5,076,025.75 ($1,000,000 down payment plus $4,076,025.75 issue price of the noncontingent debt instrument). B's noncontingent debt instrument has imputed interest of $923,974.25 under section 1274, which is treated as original issue discount subject to current inclusion under section 1272 and the regulations thereunder.

(iii) Assume that the amount of contingent interest that becomes fixed as of December 31, 1986, is $100,000. This amount is treated under paragraph (c)(3)(ii)(A) of this section as a payment of principal to the extent of its present value (using a discount rate equal to the Federal short-term rate of 10%, compounded annually, and the exact method for the short period), discounting from December 31, 1986, (the date the amount of the payment becomes fixed) to April 1, 1986 (the issue date of B's debt instrument) which, under § 1.1274–5, is $93,101.24. The remainder of the $100,000 payment, $6,898.76, is treated under paragraph (c)(3)(ii)(B) of this section as interest. The additional amount treated as principal gives B additional basis in Blackacre on December 31, 1986, and, if A is reporting his gain on the installment method under section 453, is an additional amount realized by A when paid. The portion of the payment treated as interest is includible in gross income by A and deductible from gross income by B in their respective taxable years in which December 31, 1986 occurs.

(iv) Assume that the actual amounts of contingent interest that become fixed in years 1986 through 1989, and the amounts recharacterized as principal using a discount rate equal to the short-term rate (10%) for the first three payments and the mid-term rate (11%) for the fourth payment (and the exact method for the short period) under paragraph (c)(3)(ii) of this section are as follows:

Year	Contingent amounts	Amount treated as principal
1986	$100,000	$93,101.24
1987	200,000	169,274.99
1988	400,000	307,772.71
1989	400,000	279,793.37
		$849,942.32

The total amount recharacterized as principal as of December 31, 1989, is $849,942.32. Assume that the contingent amount fixed on December 31, 1990 is $400,000. The present value of this amount (using a discount rate of 11%, compounded annually and the exact method for the short period) as of April 1, 1986, is $254,357.61. Under paragraph (c)(3)(ii)(A) of this section, this amount would be treated as additional principal. However, the maximum amount of this payment that can be characterized as principal under the limitation of paragraph (c)(3)(ii) of this section is $74,031.94, which is the excess of the stated principal amount of the debt instrument ($5,000,000) over the sum of the testing amount of the debt instrument ($4,076,025.75) and amounts previously characterized as principal ($849,942.32). Thus, only $74,031.94 of the last $400,000 payment is treated as principal; the remainder, $325,968.07, is treated as interest which is includible in gross income by A and deductible from gross income by B in their respective taxable years in which December 31, 1990 occurs.

Example (2). (i) The facts are the same as in example (1), except that all contingent interest is payable at maturity on March 31, 1991. The contingent interest amounts bear interest from the time they become fixed until they are due at a rate of 13%, compounded quarterly. Assume that a rate of 13%, compounded quarterly constitutes adequate stated interest for all purposes of this example. The analysis of the noncontingent payments under the noncontingent debt instrument is the same as in part (ii) of example (1). Thus, B's noncontingent debt instrument has $923,974.25 of original issue discount subject to current inclusion under section 1272 and the regulations thereunder.

(ii) Assume that a $100,000 payment of contingent interest becomes fixed as of December 31, 1986. Since this amount is not due within six months of the time it becomes fixed, under paragraph (c)(3)(iii)(A) of this section, a separate debt instrument subject to the provisions of section 1274 is treated as issued by B on the date the payment becomes fixed, December 31, 1986. This debt instrument has a stated principal amount equal to the amount of the payment that becomes fixed, $100,000, and matures on the date the payment is due, March 31, 1991. The separate debt instrument has a stated redemption price at maturity under § 1.1273–1(b)(1) of $172,238.81 ($100,000 principal plus $72,238.81 of deferred interest). Since the payment bears adequate stated interest, under section 1274(a)(1), the issue price of this separate debt instrument is the stated principal amount of $100,000.

(iii) The $100,000 issue price of B's separate debt instrument is treated under paragraph (c)(3)(ii) of this section as principal to the extent of the present value of the payment as of April 1, 1986. Since the contingent payment is due 4 years and 3 months after it becomes fixed, the Federal mid-term rate of 11%, compounded annually, is used in determining its present value under the exact method (even though the $100,000 amount becomes fixed 9 months after the issue date). This present value is $92,471.47. The remainder of the payment, $7,528.53, is treated as interest. The $92,471.47 of principal gives B additional basis in Blackacre on December 31, 1986. The $7,528.53 payment of interest is includible in gross income by A and deductible from gross income by B for their respective taxable years in which December 31, 1986 occurs.

(iv) Since the interest on B's separate debt instrument to A is not payable currently, it is treated as original issue discount under section 1273 and is subject to current inclusion under section 1272 and the regulations thereunder. The accrual period under §1.1272–1(d)(1)(i) of B's separate debt instrument, is a calendar quarter. The amount of original issue discount on B's separate debt instrument allocable to each year under § 1.1272–1(c) is as follows:

Year	Original issue discount
1987	$13,647.60
1988	15,510.17
1989	17,626.93
1990	20,032.57
1991	5,421.54

Year	Original issue discount
	$72,236.81

Example (3). The facts are the same as in example (2), except that the contingent interest amounts do not bear additional interest from the time they become fixed until they are due. Assume that on December 31, 1986, a contingent interest payment of $100,000 becomes fixed; thus, on this date, B is obligated to pay A $100,000 on March 31, 1991. Since the contingent payment is not due within six months after it becomes fixed, under paragraph (c)(3)(iii)(A) of this section, the payment is treated as a separate debt instrument issued by B on December 31, 1986, for a stated principal amount of $100,000, maturing on March 31, 1991, with a stated redemption price at maturity of $100,000. Since this separate debt instrument bears no interest, it does not have adequate stated interest within the meaning of § 1.1274–3. The issue price of the separate debt instrument is the testing amount under § 1.1274–3, which is arrived at, under paragraph (c)(3)(iii)(B) of this section, by discounting all payments under the separate debt instrument at the test rate in effect on April 1, 1986 (the issue date) from the date the payment is due to the date the payment becomes fixed. Discounting $100,000 from March 31, 1991 to December 31, 1986, (using a discount rate of 11%, compounded annually and the exact method for the short period) yields a present value of $64,176.69. B is thus treated as having issued a separate debt instrument to A with an issue price of $64,176.69, bearing interest at a rate of 11%, compounded annually. The issue price of this debt instrument is treated under paragraph (c)(3)(ii) of this section as principal in an amount equal to the present value of $64,176.69, discounting from December 31, 1986 to April 1, 1986, (using a discount rate of 11%, compounded annually and the exact method for the short period), which is $59,345.13. This principal gives B additional basis in Blackacre on December 31, 1986. The remainder of the payment, $4,831.56, is treated as a payment of interest which is includible in gross income by A and deductible from gross income by B in their respective taxable years in which December 31, 1986 occurs. The $35,923.31 of imputed interest on B's separate debt instrument is original issue discount under section 1273 and is subject to the current inclusion rules of section 1272 and the regulations thereunder.

Example (4). The facts are the same as in example (3), except that the amount of contingent interest payable at maturity depends upon a formula relating to B's average profit or loss from Blackacre during the years 1987 through 1990. Because profits in earlier years may be offset by losses in later years, no amount becomes fixed until December 31, 1990. Since the total amount of contingent interest is due within six months from the date that the amount becomes fixed, the payment is not treated as a separate debt instrument once it becomes fixed under paragraph (c)(3)(iii)(A) of this section. Instead, the amount payable at maturity is treated under paragraph (c)(3)(ii) of this section as a payment of principal in an amount equal to the present value of the payment (using a discount rate of 11%, compounded annually) as of April 1, 1986, and as a payment of interest in an amount equal to the remainder. B is not entitled to deduct the amount of this interest payment from gross income until the date that the payment becomes fixed, December 31, 1990, nor does he receive any additional basis in Blackacre until that date. A is not required to include any interest in gross income until the date that the payment becomes fixed, December 31, 1990, and A has no additional amounts realized until maturity, March 31, 1991.

(d) *Certain contingent payments within a fixed period*—(1) *Applicability.* In the case of an overall debt instrument issued in a transaction to which section 1274 applies that—

(i) Calls for fixed or minimum payments within a specified time period, and

(ii) Either—

(A) Does not provide for adequate stated interest, or

(B) Contains a provision that recharacterizes a portion of each payment as interest to an extent sufficient to constitute adequate stated interest, the buyer's basis in the property purchased and the allocation of interest under the debt instrument given in consideration of the sale or exchange of the property, shall be determined pursuant to the provisions of paragraph (d)(2) of this section. Any payments in excess of the minimum payments provided for under the debt instrument shall be treated as contingent payments subject to the provisions of paragraph (c)(3) of this section.

(2) *Determination of buyer's basis and allocation of interest*—(i) *General rule.* For purposes of determining the buyer's basis in the property purchased and the allocation of interest (whether stated or imputed) to the proper accrual periods under the debt instrument, all future payments to be made under the debt instrument shall be presumed to be made at the latest possible date that is permitted under the terms of the debt instrument (taking into account all prior payments), and in the smallest amount permitted (excluding contemporaneous payments of stated interest). The preceding sentence shall not apply for purposes of determining the recovery of basis to the seller as a result of the sale or exchange of the property.

(ii) *Buyer's basis in property purchased*—(A) *Initial basis.* The buyer's basis in the property purchased at the time of the sale or exchange shall be the issue price of the debt instrument (determined pursuant to the general rule of paragraph (d)(2)(i) of this section).

(B) *Subsequent additions to basis.* When a fixed or minimum payment under the debt instrument is made, the buyer's basis in the property purchased shall be increased on that date by the excess of—

(*1*) The present value as of the issue date of the debt instrument of the amount of the payment, including any stated interest (determined under the provisions of paragraph (d)(2)(v) of this section), over

(*2*) The present value as of the issue date of the amount of the payment, including any stated interest (determined pursuant to the rules of paragraph (d)(2)(i) and (v) of this section).

(iii) *Adjusted issue price of the debt instrument.* For purposes of paragraph (d) of this section, the adjusted issue price at the end of an accrual period (as well as at the beginning of the next succeeding accrual period) is the present value as of that date of all future payments to be made under the debt instrument (determined pursuant to the rules of paragraph (d)(2)(i) and (v) of this section).

(iv) *Amount of original issue discount allocable to an accrual period.* The amount of original issue discount allocable to an accrual period shall be the excess of—

(A) The total amount of original issue discount that would have accrued through the end of that accrual period (determined by taking into account the timing of payments that have been made by the end of that accrual period and by treating all remaining future payments as subject to the general rule of paragraph (d)(2)(i) of this section), over

(B) The total amount of original issue discount allocated to prior accrual periods.

An alternate formulation for the amount of original issue discount allocable to an accrual period is the excess of—

(C) The sum of—

(*1*) The amount of the payment (if any) at the end of the accrual period, and

(*2*) The adjusted issue price of the debt instrument at the end of that accrual period, over

(D) The sum of—

(*1*) The amount by which the buyer's basis is increased as result of the payment, if any, (determined pursuant to paragraph (d)(2)(ii)(B) and (v) of this section), and

(*2*) The adjsuted issue price of the debt instrument at the beginning of the accrual period.

(v) *Special rules.* In applying the provisions of paragraph (d)(2)(ii)(B) and (iii) of this section, any provision calling for a test rate other than the applicable

Federal rate shall apply if, and only if, such provision applies to the overall debt instrument. The test rates under paragraph (d)(2)(ii)(B)(*2*) and (iii) of this section shall be based on the term of the overall debt instrument. The test rate under paragraph (d)(2)(ii)(B)(*1*) of this section shall be based on a term beginning on the date the overall debt instrument is issued and ending on the date the contingent payment is made.

(3) *Example.* The provisions of paragraph (d) of this section may be illustrated as follows:

Example. (i) On July 1, 1986, A sells Blackacre to B in exchange for B's debt instrument calling for five annual payments, each payment equal to 10% of the gross yield from Blackacre for the immediately preceding fiscal year ending on March 31. Each payment is to be made on the following June 30. The debt instrument does not provide for any stated interest. The terms of the debt instrument further specify that if by June 30, 1990, B has not paid at least $5 million to A, the payment due on June 30, 1991 shall consist of the excess of $5 million over the sum of all prior payments. Assume that on July 1, 1986, the Federal short-term rate is 9%, compounded annually, and the Federal mid-term rate is 11%, compounded annually.

(ii) Because no portion of the $5 million payment is unconditionally payable prior to June 30, 1991, the issue price of the debt instrument under § 1.1274–4 and paragraph (d)(2)(i) of this section is its imputed principal amount, determined by taking the present value of $5 million payable at the end of the 5-year term and using a discount rate of 11%, compounded annually. This present value is $2,967,257. B's basis in Blackacre is limited initially to this amount.

(iii) The gross yield from Blackacre for the fiscal year ending on March 31, 1987 is $13 million; therefore, a payment of $1,300,000 is due on June 30, 1987. The present value of this payment as of July 1, 1986, using a discount rate equal to the Federal short-term rate of 9%, compounded annually, is $1,192,660. The present value as of July 1, 1986 of a payment of $1,300,000 due on June 30, 1991, discounted at the Federal mid-term rate of 12%, compounded annually, is $771,487. Since the payment of $1,300,000 is actually made at an earlier date than that presumed under the general rule of paragraph (d)(2)(i) of this section, the buyer's basis is increased on the date of the payment under paragraph (d)(2)(ii)(B) of this section by the excess of the present value of the payment actually made over the present value of that amount. Thus, B receives additional basis in Blackacre as a result of the June 30, 1987 payment equal to $421,173 ($1,192,660 – $771,487).

(iv) The adjusted issue price of B's debt instrument at the end of the first accrual period, June 30, 1987, pursuant to paragraph (d)(2)(iii) of this section, is equal to the present value as of June 30, 1987 of a payment of $3,700,000 ($5,000,000 – $1,300,000) due on June 30, 1991, using a discount rate of 11%, compounded annually. This present value is $2,437,305.

(v) The amount of original issue discount allocable to the first accrual period, pursuant to paragraph (d)(2)(iv) of this section, is the sum of the payment actually made at the end of that accrual period ($1,300,000) and the adjusted issue price of the debt instrument at the end of the accrual period ($2,437,305) minus the sum of the amount of additional basis B receives as a result of the payment ($421,173) and the issue price of the obligation ($2,967,257). This amount is $348,875 [($1,300,000 + $2,437,305) – ($421,173 + $2,967,257)].

(vi) Assume that the gross yield from Blackacre for the fiscal year ending March 31, 1988 is $15 million; therefore, a payment of $1,500,000 is due on June 30, 1988. Pursuant to the provisions of paragraph (d)(2)(ii)(B) of this section, B receives additional basis in Blackacre of $372,343, calculated as follows:

Present value of actual $1,500,000 payment at end of second accrual period, using a discount rate of 9%, compounded annually	$1,262,520
Reduced by:	
Present value of a hypothetical $1,500,000 payment at maturity, using a discount rate of 11%, compounded annually	(890,177)
	$372,343

(vii) The adjusted issue price of B's debt instrument at the end of the second accrual period is equal to the present value as of June 30, 1988, of a payment of $2,200,000 ($3,700,000 – $1,500,000) due on June 30, 1991, using a discount rate of 11%, compounded annually. This present value is $1,608,621.

(viii) The amount of original issue discount allocable to the second accrual period is the sum of the payment actually made at the end of that accrual period ($1,500,000) and the adjusted issue price of the debt instrument at the end of the accrual period ($1,608,621) minus the sum of the amount of additional basis B receives as a result of the payment ($372,343) and the adjusted issue price at the beginning of the accrual period ($2,437,305). The amount of original issue discount allocable to the second accrual period is thus $298,973 [($1,500,000 + $1,608,621) – ($372,343 + $2,437,305)].

(ix) Assume that the gross yield from Blackacre for the fiscal year ending on March 31, 1989 is $14 million, and a payment of $1,400,000 is due on June 30, 1989. Assume further that B receives additional basis of $250,225 as a result of that payment, and that the amount of original issue discount allocable to the third accrual period is $190,452. Therefore, by June 30, 1989, B has made total payments to A of exactly $4,200,000 (including the $1,400,000 payment made on that date). The adjusted issue price of B's debt instrument on June 30, 1989 is equal to the present value as of that date of the $800,000 remaining minimum payment (assuming that the payment will be made on June 30, 1991). This present value is $649,298.

(x) Assume that the gross yield from Blackacre for the fiscal year ending on March 31, 1990 is $18 million; therefore, a payment of $1,800,000 is due on June 30, 1990. Since the remaining minimum payment is only $800,000, this payment is subject to the rules of paragraph (d) of this section only to the extent of that minimum payment. The remainder of the payment, $1,000,000, is characterized as interest or principal under the rules of paragraph (c)(3)(ii) of this section. The present value of $800,000 as of the issue date, July 1, 1986, using a discount rate equal to the Federal mid-term rate of 11%, compounded annually, is $526,985. The present value of a payment of $800,000 due on June 30, 1991, using a discount rate of 11%, compounded annually, is $474,761. B thus receives additional basis in Blackacre attributable to the remaining $800,000 minimum payment of $52,224 ($526,985 – $474,761). B also receives additional basis on March 31, 1990, under paragraph (c)(3)(ii) of this section, equal to the present value of the $1,000,000 excess payment, or $658,731. B's total increase in basis is thus $710,955 ($52,224 + $658,731).

(xi) Since the minimum payment requirements of the debt instrument have been satisfied, the adjusted issue price of the debt instrument as of June 30, 1990, defined in paragraph (d)(2)(iii) of this section as the present value of all future fixed or minimum payments to be made under the debt instrument, is zero. The amount of original issue discount allocable to the accrual period beginning on July 1, 1989 and ending on June 30, 1990 is equal to the excess of the minimum payment made at the end of that accrual period ($800,000) over the sum of the additional basis B receives as a result of that portion of the payment ($52,224) and the adjusted issue price of the debt instrument at the beginning of the accrual period ($649,298). The amount of original issue discount allocable to the accrual period ending on June 30, 1990 is thus $98,478 [$800,000 + $649,298)]. The excess of the $1,000,000 portion of the payment over the portion treated as principal, $658,731, which excess is $341,269, is treated as interest and is accounted for on June 30, 1990.

(xii) Assuming that there is an additional payment during the one remaining accrual period, the amount of additional basis received by B is that portion of the payment due at the end of the accrual period that is treated as principal (as determined under paragraph (c)(3)(ii) of this section). This amount is the present value of the payment as of the issue date, using a discount rate of 11%, compounded annually. The amount of original issue discount allocable to that accrual period is that portion of the payment treated as interest. This amount is equal to the excess of the amount of the payment over the portion that is treated as principal.

(e) *Certain debt instruments issued for cash or publicly traded property*—(1) *Separation into noncontingent and contingent components.* In the case of an overall debt instrument issued for cash or publicly traded property in which the sum of all the noncontingent payments under the debt instrument (regardless of whether designated as interest or

principal) is greater than or equal to the issue price of the overall debt instrument, the noncontingent payments shall be subject to the rules described in paragraph (e)(2) of this section, and the contingent payments shall be subject to the rules described in paragraph (e)(3) of this section.

(2) *Treatment of noncontingent payments.* The noncontingent payments under an overall debt instrument described in paragraph (e)(1) of this section shall be treated under sections 1271 through 1275 and the regulations thereunder as a separate noncontingent debt instrument. The issue price of this separate noncontingent debt instrument is the issue price of the overall debt instrument. The stated redemption price at maturity is determined under § 1.1273–1(b)(1); and yield is determined under § 1.1272–1(f), all without reference to the contingent payments. The *de minimis* rule of section 1273(a)(3) and §1.1273–1(a)(3) shall not apply to the noncontingent debt instrument.

(3) *Treatment of contingent payments*—(i) *In general.* The contingent payments under an overall debt instrument described in paragraph (e)(1) of this section shall be treated entirely as interest and, except as provided in paragraph (e)(3)(ii) of this section, shall be includible in gross income by the holder and deductible from gross income by the issuer in their respective taxable years in which the amount of the payment becomes fixed.

(ii) *Certain delayed contingent payments*—(A) *In general.* In the case in which a contingent payment is not due within six months of the date on which the amount of the payment becomes fixed, the parties shall be treated as if the borrower had issued a separate debt instrument on the date the amount of the payment becomes fixed, maturing on the date that the payment is due. The stated principal amount of this separate debt instrument shall be the amount of the payment that becomes fixed. An amount equal to the issue price of this separate debt instrument shall be accounted for as if an amount of interest equal to such issue price had been paid by the borrower to the lender on the date that the amount of the payment becomes fixed. To determine the issue price of the separate debt instrument, all payments under the debt instrument shall be discounted from the date that the payment is due to the date that the payment becomes fixed. The amount of a contingent payment shall be treated as fixed even if, once fixed, the payment is payable in the future together with interest that is subject to further contingencies.

(B) *Special rules.* In applying section 1274 to a separate debt instrument described in paragraph (e)(3)(ii) of this section, (*1*) the test rate shall be based on the term of the overall debt instrument, and (*2*) any provision calling for a test rate other than the applicable Federal rate shall apply if, and only if, such provision would have been applied to the overall debt instrument if it had been issued for nonpublicly traded property.

(4) *Examples.* The provisions of paragraph (e) of this section may be illustrated by the following examples:

Example (1). On April 1, 1986, A sells publicly traded property to B in exchange for B's debt instrument calling for a payment of $5,000,000 in five years with fixed interest of 6% and contingent interest of up to an additional 8% payable annually on March 31 of each year from 1987 to 1991. Assume that the fair market value of the property on April 1, 1986, is $5,000,000. The issue price of the overall debt instrument under section 1273 (b)(3) and § 1.1273 2(c)(1) is $5,000,000. Applying the rules of section 1273 and the regulations, thereunder to only the noncontingent payments under the debt instrument in accordance with paragraph (e)(2) of this section, the issue price of the noncontingent debt instrument is $5,000,000, and its stated redemption price at maturity (under § 1.1273–1(b)(1)) is $5,000,000. Thus, the noncontingent debt instrument has no original issue discount under section 1273(a)(1). Under paragraph (e)(3) of this section, each contingent payment is treated entirely as interest which is accounted for by both A and B in their respective taxable years in which the amount of the payment becomes fixed.

Example (2). (i) The facts are the same as in example (1), except that the contingent interest which becomes fixed on March 31 of each year is not payable until maturity. However, these deferred amounts bear interest at a rate of 13%, compounded quarterly. The analysis of the noncontingent payments under the debt instrument is the same as in example (1).

(ii) Assume that a contingent payment of $100,000 becomes fixed as of December 31, 1986, and is payable on March 31, 1991. Since this amount is not due within six months of the date it becomes fixed, under paragraph (e) (3)(ii)(A) of this section, a separate debt instrument subject to the provisions of section 1274 is treated as issued by B on the date the payment becomes fixed, December 31, 1986. This separate debt instrument has a stated principal amount equal to the amount of the payment as fixed, $100,000, and matures on the date the payment is due, March 31, 1991. The separate debt instrument has a stated redemption price at maturity under § 1.1273–1(b)(1) of $172,238.81 ($100,000 principal plus $72,238.81 of deferred interest). Since the payment bears adequate stated interest, under section 1274(a)(1), the issue price of this separate debt instrument is the stated principal amount of $100,000. The $100,000 issue price of B's separate debt instrument is treated entirely as interest under paragraph (e)(3) of this section, and is accounted for by both A and B in their respective taxable years in which December 31, 1986 occurs.

Example (3). The facts are the same as in example (3), except that the contingent interest amounts do not bear additional interest from the time they become fixed until they are due. Assume that, on December 31, 1986, a contingent interest payment of $100,000 becomes fixed; thus, on this date, B is obligated to pay A $100,000 on March 31, 1991. Since the contingent payment is not due within six months after it becomes fixed, under paragraph (e)(3)(ii)(A) of this section, the payment is treated as a separate debt instrument issued by B on December 31, 1986, for a stated principal amount of $100,000, maturing on March 31, 1991, with a stated redemption price at maturity of $100,000. Since this separate debt instrument bears no interest, it does not have adequate stated interest within the meaning of § 1.1274–3. The issue price of the separate debt instrument is the testing amount under § 1.1274–4, which is calculated, under paragraph (e)(3)(ii)(B) of this section, by discounting all payments under the separate debt instrument at the test rate in effect on April 1, 1986 (the issue date) from the date the payment is due to the date the payment becomes fixed. Discounting $100,000 from March 31, 1991 to December 31, 1986, (using a discount rate of 11%, compounded annually and the exact method for the short period) yields a present value of $64,176.69. B is treated as having issued a separate debt instrument to A with an issue price of $64,176.69, bearing interest at a rate of 11% compounded annually. This issue price is treated entirely as interest under paragraph (e)(3) of this section and the interest on the separate debt instrument is original issue discount.

Example (4). (i) C lends D $1,000,000 for use in D's business on July 1, 1986. D gives C a 5-years debt instrument calling for fixed interest payable semiannually at a rate of 10%, and a repayment of the $1,000,000 principal on June 30, 1991. In addition, the debt instrument calls for an additional contingent interest payment at maturity equal to one percent of the average annual gross sales from D's business during the 5-year period ending on December 31, 1990.

(ii) Analyzing only the noncontingent payments under the debt instrument pursuant to paragraph (e)(2) of this section, the debt instrument has an issue price of $1,000,000 under section 1273(b)(2) and § 1.1273–2(b)(2), and a stated redemption price at maturity under § 1.1273–2(b)(1) of $1,000,000. Thus, the noncontingent debt instrument has no original issue discount under section 1273(a)(1) since the issue price and the stated redemption price at maturity are the same.

(iii) The sales from D's business during 1986 are $3,000,000. Thus, the average annual gross sales during the 5-year period must be at least $600,000 (sales in future years may all be zero but will never be less than zero), and the contingent interest payment at maturity is, therefore, at least $6,000. This amount is the contingent interest payment that becomes fixed as of December 31, 1986. Since the payment is not due within six months of the date that the amount becomes fixed, under paragraph (e)(3)(ii) of this section it is treated as a separate debt instrument subject to section 1274, issued on December 31, 1986, for a stated principal amount of $6,000, and maturing on June 30, 1991 with a stated redemption price at maturity of $6,000. Assume that the test rate of interest on April 1, 1986, is 12%, compounded semiannually. Since the separate debt instrument bears no interest, it does not have adequate stated interest within the meaning of § 1.1274–3. The issue price of the separate debt instrument is, therefore, the testing amount of $3,551.39, determined under § 1.1274–3 using a rate of 12%, compounded semiannually, to discount the $6,000 payment from the date it is due, June 30, 1991, to the date it becomes fixed, December 31, 1986. B's separate debt instrument has a yield of 12%, compounded semiannually. The difference between the stated redemption price at maturity and the issue price of the separate debt instrument is original issue discount. The entire amount of the issue price of B's separate debt instrument, $3,551.39, is treated as interest pursuant to paragraph (e)(3) of this section, and is accounted for by both C and D in their respective taxable years in which December 31, 1986, occurs.

(iv) The sales from D's business during 1987 are $4,000,000. Thus, as of December 31, 1987, it is established that the average annual gross sales from D's business during the 5-year period will be at least $1,400,000 yielding a total payment at maturity of at least $14,000. This represents an additional payment of $8,000 to be made at maturity that becomes fixed on December 31, 1987. The analysis of this payment is the same as in part (iii), except that the testing amount is determined by discounting the $8,000 payment at a rate of 12%, compounded semiannually, from June 30, 1991 to December 31, 1987. This amount is $5,320.46. The entire amount of the issue price of B's separate debt instrument is treated as interest under paragraph (e)(3) of this section and is includible in gross income by C and deductible from gross income by D in their respective taxable years in which December 31, 1987 occurs.

(f) *Certain debt instruments issued for cash or publicly traded property that provide for contingent principal*—(1) *In general.* In the case of a debt instrument issued for cash or publicly traded property that provides for contingent payments, and that fails to provide for total noncontingent payments at least equal to the issue price of the debt instrument (as determined under section 1273(b) and § 1.1273–2), the noncontingent payments shall be treated as payments of principal (without regard to whether designated as interest or principal), and the contingent payments shall be subject to the rules of paragraph (f) (2) and (3) of this section.

(2) *Treatment of contingent payments*—(i) *In general.* Except as provided in paragraph (f)(2)(v) of this section, the portion of the contingent payment treated as interest shall be includible in gross income by the holder and deductible from gross income by the issuer in their respective taxable years in which the amount of the payment becomes fixed.

(ii) *Recharacterization of contingent payments.* Any contingent payment under a debt instrument described in paragraph (f)(1) of this section (other than a contingent payment made at the maturity date) shall be treated as consisting of—

(A) A payment of interest to the extent of interest deemed accrued for the current and all prior accrual periods (as determined under paragraph (f)(2)(iii) of this section) and not allocated to prior payments, and

(B) A payment of principal to the extent of the excess of such payment over the portion treated as interest under paragraph (f)(2)(ii)(A) of this section.

Notwithstanding the preceding sentence, the total amount treated as principal shall be no greater than the excess of the issue price of the debt instrument over the sum of all noncontingent payments to be made under the debt instrument. Once the total of the contingent payments characterized as principal under paragraph (f)(2)(ii)(B) of this section equals this excess, any additional contingent payments shall be treated entirely as interest.

(iii) *Interest deemed accrued.* For purposes of paragraph (f)(2)(ii) of this section, the amount of interest deemed accrued during an accrual period is equal to the product of—

(A) The adjusted issue price (as determined under paragraph (f)(2)(iv) of this section) at the beginning of the accrual period, and

(B) The applicable Federal rate, based upon the due date of the final payment (regardless of whether contingent or noncontingent) under the debt instrument.

For purposes of paragraph (f)(2)(iii)(B) of this section, the applicable Federal rate is that Federal rate that would apply to the debt instrument had it been issued for nonpublicly traded property. In the case of a debt instrument described in paragraph (f)(1) of this section that contains a short accrual period, interest deemed accrued shall be determined according to the exact method under § 1.1272–1(c)(2)(ii)(B).

(iv) *Adjusted issue price.* For purposes of paragraph (f)(2)(iii) of this section, the adjusted issue price of a debt instrument at the beginning of the first accrual period is its issue price. The adjusted issue price of the debt instrument at the beginning of each subsequent accrual period is equal to—

(A) The sum of—

(*1*) The adjusted issue price at the beginning of the immediately preceding accrual period, and

(*2*) The amount of total interest deemed accrued during that accrual period,

(B) Reduced by the amount of all payments (both noncontingent and contingent) due during the immediately preceding accrual period.

(v) *Certain delayed contingent payments*—(A) *In general.* If a contingent payment is not due within six months of the date on which the amount of the payment is fixed, the parties shall be treated as if the borrower had issued a separate debt instrument on the date the amount of the payment becomes fixed, maturing on the date that the payment is due. This separate debt instrument shall be treated as a debt instrument to which section 1274 applies. The stated principal amount of this separate debt instrument shall be the amount of the payment that becomes fixed. An amount equal to the issue price of this debt instrument shall be characterized as interest or principal under the rules of paragraph (f)(2)(ii) of this section and accounted for under paragraph (f)(2)(i) of this section as if an amount equal to the issue price had been paid by the borrower to the lender on the date that the amount of the payment becomes fixed. To determine the issue price of the separate debt instrument, all payments under the debt instrument shall be discounted from the maturity date to the date that the payment becomes fixed. The amount of a contingent payment shall be treated as fixed even if, once fixed, the payment is payable in the future together with interest that is subject to further contingencies.

(B) *Special rules.* In applying section 1274 to a separate debt instrument described in paragraph (f)(2)(iv)(A) of this section, (*1*) the test rate shall be based on the term of the debt instrument described in paragraph (f)(1) of this section, and (*2*) any provision calling for a test rate other than the applicable Federal rate shall apply if, and only if, such provision would have been applied to a debt instrument described in paragraph (f)(1) of this section if it had been issued for nonpublicly traded property.

(3) *Payments at maturity.* If, at the time of final maturity, the outstanding principal balance (issue price less the sum of all prior payments treated as principal under paragraph (f) (1) and (2)(ii) of this section) exceeds the total

amount of the final payment (whether contingent or noncontingent), the entire amount of the final payment shall be treated as principal and the debt instrument shall be treated as retired for such amount. If, conversely, at that time, the total amount of the final payment exceeds the outstanding principal balance, the debt instrument shall be treated as retired for an amount equal to such outstanding principal balance, and the final payment shall be treated as interest to the extent of such excess.

(4) *Examples.* The provisions of paragraph (f) of this section may be illustrated by the following examples:

Example (1). (i) On January 1, 1990, A sells to B publicly traded property having a fair market value on that date of $1,000,000. In exchange therefor, B issues to A a debt instrument maturing on June 30, 1991 for $900,000. The debt instrument also provides for an additional contingent payment at maturity of up to $500,000.

(ii) The issue price of the debt instrument, under section 1273(b)(3) and §1.1273–2(c)(1), is $1,000,000, the fair market value of the property. The sum of the noncontingent payments under the debt instrument is $900,000. Since the sum of the noncontingent payments under the debt instrument is less than its issue price, the noncontingent payments are treated as payments of principal under paragraph (f)(1) of this section, and the contingent payments are characterized as interest or principal under paragraph (f)(2)(ii) of this section.

(iii) Assume that the amount of the contingent payment at maturity is equal to the maximum amount of $500,000. The total payment at maturity is, therefore, $1,400,000. The outstanding principal balance at maturity is equal to the issue price of $1,000,000, since no other payments of principal have been made. Since the amount of the final payment exceeds the outstanding principal balance at maturity, under paragraph (f)(3) of this section, it is treated as a payment of principal to the extent of $1,000,000. The remainder of the final payment, $400,000, is treated as interest and is includible in gross income by A and deductible from gross income by B, under paragraph (f)(1) of this section, in their respective taxable years in which June 30, 1991 occurs.

Example (2). The facts are the same as in example (1), except that the amount of the contingent payment actually made at maturity is $50,000. Under paragraph (f)(3) of this section, since the outstanding principal balance of $1,000,000, exceeds the amount of the $950,000 payment at maturity, the entire $950,000 is treated as principal and the debt instrument is treated as redeemed for this amount. A's basis in B's debt instrument is equal to the amount loaned, $1,000,000, and A's amount realized upon maturity of the debt instrument is $950,000. A, therefore, realizes a loss of $50,000 on the retirement of B's debt instrument on June 30, 1991.

Example (3). (i) On January 1, 1988, C loans D $2,000,000 in exchange for D's 18-month debt instrument maturing on June 30, 1989. The debt instrument provides for three semiannual payments on June 30 and December 31 of $600,000 in addition to three contingent payments in amounts based upon profits from D's business. Assume that the Federal short-term rate on January 1, 1988 is 10%, compounded semiannually. Assume further that the contingent payments, when made on June 30, 1988, December 31, 1988, and June 30, 1989, are in the amounts of 0, $350,000, and $75,000, respectively.

(ii) The issue price of the debt instrument, under section 1273(b)(2) and §1.1273–2(b)(2), is the amount loaned, or $2,000,000. The sum of the noncontingent payments under the debt instrument is $1,800,000. Under paragraph (f)(1) of this section, all of the noncontingent payments are treated as principal. The accrual period, under §1.1272–1(d)(1)(i), is the six-month interval between payment dates, ending on June 30 and December 31 of both years. Total interest deemed accrued, under paragraph (f)(2)(iii) of this section, during the first accrual period is equal to the product of the issue price, $2,000,000, and one-half of the Federal short-term rate, .05, or $100,000. No contingent payment is made as of the end of the accrual period. Therefore, under paragraph (f)(2)(iv) of this section, the adjusted issue price of the debt instrument at the beginning of the second accrual period is equal to the sum of the issue price and the total interest deemed accrued ($2,000,000 + $100,000), reduced by the amount of the noncontingent payment made during the accrual period ($600,000). This amount is $1,500,000.

(iii) Total interest deemed accrued during the second accrual period is equal to the product of the adjusted issue price at the beginning of the accrual period, $1,500,000, and one-half of the Federl short-term rate, .05, or $75,000. The contingent payment of $350,000 is treated, under paragraph (f)(2)(ii)(A) of this section, as a payment of interest to the extent of the total interest deemed accrued as of the end of the accrual period that was not allocated to a previous payment, or $175,000. This amount is includible in gross income by C and deductible from gross income by D, under paragraph (f)(1) of this section, in their respective taxable years in which December 31, 1988 occurs. The remainder of the contingent payment, $175,000, is treated as a payment of principal under paragraph (f)(2)(ii)(B) of this section. The adjusted issue price at the beginning of the third accrual period, under paragraph (f)(2)(iv) of this section, is equal to the sum of the adjusted issue price at the beginning of the second accrual period, $1,500,000, and the total interest deemed accrued during the accrual period, $75,000, reduced by the sum of the payments made during the accrual period, $950,000. This amount is $625,000.

(v) The contingent payment of $75,000 increases the final payment at maturity to $675,000. The outstanding principal balance at maturity is equal to the issue price, $2,000,000, less the sum of amounts previously characterized as principal, $1,375,000, or $625,000. This amount is less than the $675,000 final payment at maturity. Therefore, under paragraph (f)(3) of this section, the debt instrument is deemed retired for an amount equal to the outstanding principal balance of $625,000. The remainder of the final payment, $50,000, is treated as a payment of interest which is includible in gross income by C and deductible from gross income by D in their respective taxable years in which June 30, 1989 occurs.

Example (4). The facts are the same as in example (3), except that the amount of the contingent payment on December 31, 1988 is $500,000. This payment is initially treated, under paragraph (f)(2)(ii)(A) of this section, as interest to the extent of $175,000, which is the interest deemed accrued as of that date under paragraph (f)(2)(iii) of this section. The remainder of the payment, $325,000, is treated as a payment of principal to the extent of the excess of the issue price of the debt instrument, $2,000,000, over the sum of the noncontingent payments under the debt instrument, $1,800,000, or $200,000. The remaining $125,000 is treated as a payment of interest, under paragraph (f)(2)(ii) of this section. The total amount of the second contingent payment treated as interest is, therefore, $300,000 ($175,000 + $125,000). The contingent payment at maturity is treated entirely as interest, since the portion of the contingent payment made at the end of the second accrual period that was treated as principal exactly equals the difference between the issue price and the sum of all noncontingent payments under the debt instrument.

Example (5). (i) The facts are the same as in example (3), except that the contingent amounts under the debt instrument are all payable at maturity, and a contingent amount of $250,000 becomes fixed at the end of the first accrual period. Assume that the contingent payments bear interest from the date they become fixed until they are due at a rate that constitutes adequate stated interest within the meaning of § 1.1274–3, and that such interest is payable at maturity.

(ii) Since the $250,000 contingent amount that becomes fixed on June 30, 1988 is not due within six months of the date it becomes fixed, under paragraph (f)(7)(iii) of this section, a separate debt instrument is treated as issued by D on that date. This debt instrument has a stated principal amount equal to the amount of the payment as fixed, $250,000, and matures on June 30, 1989, the date the payment is due. Since the separate debt instrument provides for adequate stated interest, the issue price is its stated principal amount of $250,000. An amount equal to the issue price is recharacterized under paragraph (f)(7)(ii)(A) of this section as a payment of interest equal to total interest deemed accrued during the first accrual period of $100,000. Thus, the issue price of D's separate debt instrument is treated as a payment of interest to the extent of $100,000. This amount is includible in gross income by C and deductible from gross income by D in their respective taxable years in which June 30, 1988 occurs. The remainder of the issue price, $150,000, is treated as principal. The interest on D's separate debt instrument is original issue discount subject to the inclusion rules of section 1272 and the regulations thereunder.

(iii) The facts are the same as in part (i), except that the contingent payments do not bear interest from the date they become fixed to the date they are due. The stated redemption price at maturity of the separate debt instrument is, therefore, $250,000, under § 1.1273–1(b)(1)(i). Since the separate debt instrument does not have adequate stated interest, its issue price is the testing amount under § 1.1274–3, determined, under paragraph (f)(2)(iv)(B) of this section, by discounting all payments under the separate debt instrument by the test rate of 10%, compounded semiannually. This issue price is $226,757.37. The issue price of the separate debt instrument is recharacterized under paragraph (f)(7)(ii)(A) of this section as a payment of interest equal to the total interest deemed accrued during the first accrual period, $100,000. The issue price is thus treated as a payment of interest of $100,000, which is includible by C and deductible by B in their respective taxable years in which June 30, 1986 occurs. The remainder of the issue price, $126,757.37, is treated as principal.

(g) *Special rules for certain debt instruments*—(1) *In general.* In the case of a debt instrument calling for one or more contingent payments, if the contingent payments are computed in a manner that can be reasonably expected to produce a front-loading or back-loading of interest deductions and, if a principal purpose for such front-loading or back-loading of interest deductions is the avoidance of Federal income tax, then the Commissioner may reallocate interest under the debt instrument in a manner consistent with section 1272 and the regulations thereunder. In determining whether such a purpose exists, the Commissioner shall give considerable weight to whether one of the parties is exempt from Federal income taxation or, if both parties are subject to tax, to the relative tax brackets of the parties. In making a reallocation under this paragraph (g)(1), the Commissioner may make reasonable assumptions as to the amounts of contingent interest that will accrue under the terms of the debt instrument. For example, the Commissioner may look to the actual accruals of contingent interest prior to the date such reallocation is made as a guide to future amounts of contingent interest that will accrue.

(2) *Examples.* The provisions of paragraph (g)(1) of this section may be illustrated by the following examples:

Example (1). (i) X is a public charity not subject to Federal income tax pursuant to section 510(a). On July 1, 1986, X lends $1,000,000 to M, a taxable corporation, in exchange for M's 5-year debt instrument having an issue price, under section 1273(b)(2) and § 1.1273–2(b)(2), of $1,000,000. All of the interest under the debt instrument is contingent upon the profits from M's business, and accrues annually and is payable at maturity. The interest that accrues for each year under the debt instrument is equal to a specified percentage of the profits from M's business during that calendar year. The specified percentages for each year are as follows:

Year	Percentage
1986	4.0
1987	3.2
1988	2.4
1989	1.6
1990	0.8

(ii) Assume that paragraph (g)(1) of this section applies to the debt instrument by virtue of the fact that X is not subject to Federal income taxation. The Commissioner may, therefore, reallocate the interest that accrues under M's debt instrument in a manner consistent with section 1272 and the regulations thereunder. Assume that M's profits for 1986 are $5,000,000. Accordingly, the amount of interest that accrues as of December 31, 1986, is $200,000. Absent special circumstances, the Commissioner may assume that A's profits for the years 1987 through 1990 will remain at $5,000,000. Under this assumption, the amount of interest payable at maturity would be $600,000 ($200,000 + $160,000 + $120,000 + $ 80,000 + $40,000), the stated redemption price at maturity of M's debt instrument would be, under § 1.1273–1(b)(1), $1,600,000, and the yield, under § 1.1272–1(f), would be 9.85615, compounded annually. The Commissioner may, therefore, limit M's interest deduction for M's taxable year in which December 31, 1986 occurs, to $98,561 (the product of this issue price, $1,000,000, and the yield, .098561).

Example (2). The facts are the same as in example (1), except that M lends $1,000,000 to X for a term of 5 years, and the specified percentages of M's profits for each year that are payable as contingent interest are as follows:

Year	Percentage
1986	0
1987	0
1988	5
1989	5
1990	5

Assume that paragraph (g)(1) of this section applies to X's debt instrument, and that M's profits for 1986 are $5,000,000. Assuming that M's profits will remain at this level, the amount of interest payable at maturity would be $750,000 (3x.05x$5,000,000). The yield of the debt instrument under this assumption would be 11.8427%, compounded annually. The Commissioner may, therefore, require M to include in gross income for its taxable year in which December 31, 1986 occurs, $118,427 ($1,000,000x.118427).

§ 1.1275–5 Variable rate debt instruments.

(a) *Applicability.* The rules of this section shall apply to variable rate debt instruments. For purposes of sections 1271 through 1275, a variable rate debt instrument is a debt instrument which states interest based on current values (within the meaning of paragraph (c) of this section) of an objective interest index (within the meaning of paragraph (b) of this section). Payments of interest under a debt instrument that provides for a variable rate of interest that is not based on current values of an objective interest index described in paragraph (b) of this section shall be treated as contingent payments in accordance with the rules of §§1.1274–3(d)(2) and 1.1275–4.

(b) *Objective interest index.* The term "objective interest index" means either—

(1) A rate which, as of the issue date of the debt instrument, is made known publicly and offered currently to unrelated borrowers in private lending transactions by a financial institution, or

(2) A rate reflecting an average (based on a statistically significant sample) of current yields on a class of publicly traded debt instruments.

Examples of objective interest indices include the prime rate of a designated financial institution, LIBOR (London Interbank Offered Rate), the applicable Federal rate, and the average yield on Treasury securities as published in Federal Reserve bulletins. For purposes of this section, interest expressed as a fixed multiple of an objective interest index or as a constant number of percentage or basis points more or less than an objective interest index shall constitute interest based on an objective interest index. However, interest expressed as a fixed multiple of an objective interest index plus or minus a constant number of percentage or basis points shall not constitute interest based on an objective interest index.

(c) *Current values*—(1) *Debt instruments issued after May 8, 1986.* In the case of a debt instrument issued after May 8, 1986, an interest rate shall not be considered to be based on current values of an index unless the rate in effect during any accrual period is based on values of the index in effect—

(i) No later than the close of that accrual period, and

(ii) No earlier than three months prior to the beginning of the first accrual period during which such rate was in effect.

(2) *Debt instruments issued after July 1, 1982, and before May 8, 1986.* In the case of a debt instrument issued after July 1, 1982, and before May 8, 1986, an interest rate shall not be considered to be based on current values of an index unless the rate in effect during any accrual period is based on values of the index in effect—

(i) No later than the close of that accrual period, and

(ii) No earlier than one year prior to the beginning of the first accrual period during which such rate was in effect.

(d) *Original issue discount on variable rate debt instrument*—(1) *Debt instruments for which the issue price equals the stated principal amount*. Except as provided in paragraph (d)(4) of this section, in the case of a variable rate debt instrument for which the issue price equals the stated principal amount but which has original issue discount because some or all of the stated interest under the debt instrument is not qualified periodic interest, the excess of the amount of interest that actually accrues under the terms of the debt instrument during an accrual period over any qualified periodic interest shall constitute original issue discount for this period.

(2) *Debt instruments for which the issue price is less than the stated principal amount*. In the case of a variable rate debt instrument for which the issue price is less than the stated principal amount, the amount of original issue discount allocable to each accrual period shall be equal to the sum of—

(i) The amount of original issue discount allocable to the period as set forth in paragraph (d)(1) of this section (if any), and

(ii) The excess of—

(A) The product of the hypothetical adjusted issue price (as defined in paragraph (d)(3)(i) of this section) at the beginning of the accrual period and the hypothetical yield of the debt instrument (as defined in paragraph (d)(3)(ii) of this section), over

(B) The amount of hypothetical interest (as defined in paragraph (d)(3)(iii) of this section).

(3) *Definitions*—(i) *Hypothetical adjusted issue price*. The hypothetical adjusted issue price of a variable rate debt instrument at the beginning of an accrual period is the amount that would have been the adjusted issue price of the debt instrument under § 1.1272–1(e) had the debt instrument called for fixed interest at a rate equal to the rate established by the objective interest index on the issue date, or, in a transaction to which section 1274 applies and for which there was a binding written contract prior to the issue date, the contract date. See § 1.1274–6(e).

(ii) *Hypothetical yield*—(A) *In general*. The hypothetical yield of a debt instrument (other than a debt instrument to which section 1274 applies that does not have adequate stated interest) is the interest rate that would be the yield if the debt instrument called for a fixed rate of interest equal to the rate established by the objective interest index on the issue date or, if applicable, the contract date.

(B) *Debt instruments to which section 1274 applies that do not have adequate stated interest*. In the case of a variable rate debt instrument to which section 1274 applies that does not have adequate stated interest, the hypothetical yield shall be the imputed interest rate determined under § 1.1274–4.

(iii) *Hypothetical interest*. The hypothetical interest for an accrual period is the amount of interest that would have been paid or accrued with respect to that accrual period had the debt instrument called for a fixed rate of interest equal to the rate established by the objective interest index on the issue date or, if applicable, the contract date.

(4) *Special rule*. In cases in which a debt instrument provides for—

(i) A fixed rate of interest during some accrual periods and a variable rate in other accrual periods, or,

(ii) One variable rate during some accrual periods and one or more variable rates based on a different index or formula in other accrual periods,

any original issue discount on the debt instrument shall be reallocated in a manner consistent with the rules of sections 1272 and 1275 and the regulations thereunder to prevent the front-loading or back-loading of interest.

(5) *Examples*. The provisions of paragraphs (a) through (d) of this section may be illustrated by the following examples:

Example (1). Assume that on January 1, 1986, A lends B $100,000 in exchange for B's note having an issue price of $100,000 repayable in 10 years. A and B are unrelated, cash-method, calendar-year taxpayers. All interest is payable at maturity, compounded on June 30 and December 31 of each year, at a rate equal to the Federal short-term rate in effect on the compounding date. Assume that on June 30, 1986, the Federal short-term rate for that date is 8%, compounded semiannually. The amount of interest that accrues under that debt instrument for the first six-month accrual period is $4,000. This is the amount of original issue discount allocable to the first accrual period under paragraph (d)(1) of this section.

Example (2). (i) On July 1, 1986, A lends B $100,000 in return for B's note to A calling for a payment of $100,000 on June 30, 1990. Interest accrues on the outstanding loan balance at a variable rate based on current values of an objective interest index. The interest rate established is determined on June 30 and December 31 of each year for the preceding semiannual accrual period, and interest calculated under this rate is added to the outstanding loan balance. On each of those same dates, B agrees to make a payment of $9,000 to A (or the entire outstanding loan balance if less) in reduction of the outstanding loan balance. If the loan has not been repaid at the end of 15 years, B is obligated to repay the entire outstanding loan balance at that time.

(ii) None of the interest payments under B's note are qualified periodic interest (within the meaning of § 1.1273–2(b)(1)(ii) (since they are not payable at a fixed or variable rate of interest. The amount of original issue discount thus attributable to each semiannual accrual period is the amount of interest that accrues for that period under the terms of the debt instrument. The semiannual payments of $9,000 are payments other than qualified periodic interest and thus reduce the adjusted issue price at the beginning of the next succeeding accrual period pursuant to § 1.1272–1(e)(2)(ii). The adjusted issue price at the beginning of each accrual period represents the outstanding loan balance at the beginning of that period.

(iii) Assume that the rate of interest established by the index for the semiannual accrual period ending on January 1, 1987 is 10%, compounded semiannually. Thus, $5,000 of interest accrues for the first accrual period and constitutes the amount of original issue discount attributable to that period. The adjusted issue price of the debt instrument at the beginning of the second accrual period is, pursuant to § 1.1272–1(e)(2), $96,000, calculated as follows:

(1) Issue price	$100,000
(2) Original issue discount for the first accrual period	5,000
(3) Line (1) plus line (2)	$105,000
(4) Interest payment at end of first accural period	9,000
(5) Line (3) minus line (4)	$96,000

Example (3). (i) On January 1, 1986, A purchases nonpublicly traded property from B. A and B are cash-method taxpayers. In consideration for the sale, A gives B a 5–year debt instrument, maturing on December 31, 1990, with a stated principal amount of $500,000, calling for annual payments of interest on December 31 of each year, at a rate equal to two points less than the prime rate of a designated bank in effect at the time of payment. The annual payments of interest are qualified periodic interest payments (as defined in § 1.1273–2(b)(1)(ii)). The stated redemption price at maturity determined under § 1.1273–2(b)(1) is $500,000. The accrual period under § 1.1272–1(d)(1) coincides with the calendar year. Assume that on January 1, 1986, the prime rate of the designated bank expressed in terms of a rate based on annual compounding is 12%, and that therefore, the index rate on the issue date is 10%, compounded annually. Assume further that the test rate for this 5–year debt instrument is 12%, compounded annually. Thus, the debt instrument does not provide adequate stated interest under the provisions of § 1.1274–3(d)(1). The issue price is $463,952.24, the imputed principal amount determined under § 1.1274–4(e) by discounting at a rate of 12%, compounded annually, all payments that would be made under the debt instrument if the index rate were to remain constant at 10%, compounded annually. The debt instrument has $36,047.76 of original issue discount (stated redemption price at maturity, $500,000, less issue price, $463,952.24). The hypothetical yield, under paragraph (d)(3)(ii)(B) of this section, is 12%, compounded annually. The hypothetical adjusted issue price at the beginning of the first accrual period is, under § 1.1272–1(e)(1), the issue price.

(ii) The amount of original issue discount allocable to the first accrual period under paragraph (d)(2) of this section is determined as follows:

(1) Issue price	$463,952.24
(2) Hypothetical yield	.12
(3) Line (1) multiplied by line (2)	$55,674.27
(4) Less: hypothetical interest	50,000.00
(5) Line (3) minus line (4) (amount of original issue discount allocable to the first accrual period)	$5,674.27

The hypothetical adjusted issue price at the beginning of the second accrual period is $469,626.51, the sum of the issue price ($463,952.24) and the amount of original issue discount allocable to the first accrual period ($5,674.27). The amount actually paid as interest is includible as interest in gross income by B when received and deductible as interest from gross income by A when paid.

(iii) The amount of original issue discount allocable to the second accrual period is determined as follows:

(1) Hypothetical adjusted issue price on 1/1/87	$469,626.51
(2) Hypothetical yield	.12
(3) Line (1) multiplied by line (2)	$56,355.18
(4) Less: hypothetical interest	50,000.00
(5) Line (3) minus line (4) (amount of original issue discount allocable to the second accrual period)	$6,355.18

The hypothetical adjusted issue price at the beginning of the third accrual period is $475,981.69 ($469,626.51 + $6,355.18).

(iv) The amount of original issue discount attributable to the remaining three accrual periods is determined in a similar manner. The amount of original issue discount attributable to each of the five accrual periods is set forth in the table below:

Accrual period	Original issue discount
1986	$5,674.27
1987	6,355.18
1988	7,117.80
1989	7,971.94
1990	8,928.57

Example (4). (i) The facts are the same as in example (3), except that all interest is compounded annually on December 31 and paid at maturity. Based upon an interest rate of 10%, compounded annually, the amount payable at maturity will be $805,255, composed of $500,000 principal and $305,255 of deferred interest. The issue price is $456,923.31, which is the imputed principal amount determined under §§ 1.1274–3(d)(1) and 1.274–4 (the present value of $805,255, discounting at 12%, compounded annually). The hypothetical yield is 12%, compounded annually.

(ii) Assume that the actual amounts accured as interest under the debt instrument are as follows:

Year	Index rate (percent)	Interest accrued	Loan balance at end of year
1	14	$70,000.00	$570,000.00
2	11	62,700.00	632,700.00
3	9	56,943.00	689,643.00
4	13	89,653.59	779,296.59
5	11	85,722.62	865,019.21

The amount of original issue discount allocable to the first accrual period is determined under paragraph (d)(2) of this section as follows:

(1) Issue price	$456,923.31
(2) Hypothetical yield	.12
(3) Line (1) multiplied by line (2)	$54,830.80
(4) Less: hypothetical interest	50,000.00
(5) Line (3) minus line (4)	$4,830.80
(6) Amount of interest actually accrued	$70,000.00
(7) Line (5) plus line (6) (amount of original issue discount allocable to the first accrual period)	$74,830.80

The hypothetical adjusted issue price at the beginning of the second accrual period is $511,754.11, the sum of the issue price ($456,923.31) and the product of the price and the hypothetical yield of 12% ($54,830.80). The amount of original issue discount allocable to each of the five annual accrual periods is set forth in the following table:

Year	(1) Hypothetical adjusted issue price (HAIP)	(2) Yield × HAIP	(3) Hypothetical interest	(4) Column (2) minus column (3)	(5) Interest accrued	(6) OID column (4) plus column (5)
1	$456,923.31	$54,830.80	$50,000.00	$4,830.80	$70,000.00	$74,830.80
2	511,754.11	61,410.49	55,000.00	6,410.49	62,700.00	69,110.49
3	573,164.60	68,779.75	60,500.00	8,279.75	56,943.00	65,722.75
4	641,944.36	77,033.32	66,550.00	10,483.32	89,653.59	100,136.91
5	718,977.68	86,277.32	73,205.00	13,072.32	85,722.62	98,794.94

Example (5). (i) C lends $1,000,000 to D in exchange for D's 10-year note calling for semiannual payments of interest at a rate equal to the prime rate of a designated bank for the first 5 years, and semiannual payments of interest at a rate equal to 150% of the prime rate of the same bank for the second 5 years. All of the stated interest during the first 5 years and interest during the second 5 years, to the extent it does not exceed the prime rate of the designated bank, is qualified periodic interest within the meaning of § 1.1273–1(b)(1)(ii), and is therefore not subject to reallocation under paragraph (d)(4)(i) of this section. The additional interest of 50% of the prime rate payable in each of the last 5 years is treated as original issue discount and shall be reallocated and accounted for over the entire 10-year term of the debt instrument in a manner consistent with sections 1272 and 1275 and the regulations thereunder.

(ii) Assume that the prime rate of the designated bank on the issue date is 10%, compounded semiannually. If the prime rate were to remain at this rate over the entire term of D's debt instrument, the yield of the debt instrument, under § 1.1272–1(f), would be 11.802%, compounded semiannually, and the debt instrument would have $250,000 of original issue discount. The original issue discount allocable to the first ten semiannual accrual periods would be as follows:

Accrual period	Original issue discount
1	$9,012
2	9,543
3	10,107
4	10,703
5	11,334
6	12,003
7	12,712
8	13,462
9	14,256
10	15,098

C and D must account for these amounts of original issue discount during each of the first 5 years of the debt instrument. For each of the remaining ten accrual periods, the amount of original issue discount allocable to each such period is the amount of interest actually payable for the accrual period, reduced by the portion of the payment treated as qualified periodic interest and by the amount of original issue discount allocated to the corresponding semiannual accrual period during the first 5 years. For example, if the amount of interest payable with respect to the eleventh semiannual accrual period were $70,000, $50,000 would be treated as qualified periodic interest, $9,012 would be treated as a payment of original issue discount already accounted for during the first accrual period, and the remainder, $10,988, would be treated as original issue discount allocable to the eleventh accrual period.

§ 1.6045-1 [Amended]

Par. 29. Paragraph (c) of § 1.6045-1 is amended by removing the phrase "section 1232(b)(1)" every place it appears and adding in its place the phrase "section 1273(a)(1)".

§ 1.6049-4 [Amended]

Par. 30. Paragraph (e)(2) of § 1.6049-4 is amended by removing the phrase "section 1232 (a)(3)" and adding in its place the phrase "section 1271(a)(3)(A)".

Par. 31. Section 1.6049-5 is amended as follows:

1. In paragraph (b)(1)(vi)(B) (*4*) by removing the phrase "section 1232 (b)(1)" and adding in its place the phrase "section 1273 (a)(1)".

2. In paragraph (c) by removing the ninth sentence thereof and by revising the second, fourth and seventh sentences to read as follows:

§ 1.6049-5 Interest and original issue discount subject to reporting after December 31, 1982.

* * * * *

(c) *Original issue discount treated as payment of interest.* * * * In the case of an obligation as to which there is during any calendar year an amount of original issue discount includible in the gross income of any holder (as determined under section 1272 and the regulations thereunder), the issuer of the obligation or a middleman (as defined in § 1.6049-4(f)(4)) shall be treated as having an amount of interest equal to the amount of original issue discount so includible without regard to any reduction by reason of an acquisition premium under section 1272(a)(6) and (b)(4) or a purchase at a premium under section 1272(c)(1) and § 1.1275-1(f). * * * In the case of (1) an obligation to which section 1272 does not apply (for example, a short-term government obligation as defined in section 1271(a)(3)(A)) and (2) an obligation issued on or before December 31, 1982, in bearer form, the amount of original issue discount includible in gross income shall be treated as if paid in the calendar year in which the date of maturity occurs or in which the date of redemption occurs if redemption occurs before maturity. * * * Discount on short term government obligations as defined in section 1271(a)(3)(B), such as Treasury bills, and discount on other obligations with a maturity at the date of issue of not more than 1 year (a short term obligation), including commerical paper, when paid at maturity or redemption if redemption occurs before maturity, shall constitute a payment of interest for purposes of section 6049. * * *

§ 1.6049-6 [Amended]

Par 32. Paragraph (d) of § 1.6049-6 is amended by removing the phrase "section 1232A" and adding in its place the phrase "section 1272 (a)".

Par. 33. Paragraph (e) of § 1.7872-4, as proposed in the **Federal Register** for August 20, 1985, (50 FR 33561) is revised to read as follows:

§ 1.7872-4 Types of below-market loans.

* * * * *

(e) *Tax avoidance loan*—(1) *In general.* A tax avoidance loan is any below-market loan one of the principal purposes for the interest arrangements of which is the avoidance of Federal tax with respect to either the borrower or the lender, or both. For purposes of this rule, tax avoidance is a principal purpose of the interest arrangements if a principal factor in the decision to structure the transaction as a below-market loan (rather than, for example, as a market interest rate loan and a payment by the lender to the borrower) is to reduce the Federal tax liability of the borrower or the lender or both. The purpose for entering into the transaction (for example, to make a gift or to pay compensation) is irrelevant in determining whether a principal purpose of the interest arrangements of the loan is the avoidance of Federal tax.

(2) *Certain loans incident to sales or exchanges.* If, pursuant to a plan that is incident to a sale or exchange of property, a party who is related (within the meaning of section 168(e)(4)(D)) to the seller—

(i) Makes a below-market loan to the buyer of the property, or

(ii) Makes a below-market loan to the seller that is assumed by the buyer in connection with the sale or exchange, then the loan shall be treated as a tax avoidance loan within the meaning of paragraph (e)(1) of this section. There shall be an irrebuttable presumption that such a plan exists if such a loan is made within one year of the sale or exchange.

(3) *Examples.* The provisions of paragraph (e) of this section may be illustrated by the following examples:

Example (1). (i) S and T are each wholly-owned subsidiaries of P. S sells property to an individual, A, for cash of $3,000,000. Three months after the sale, T loans to A $2,000,000 for 10 years at an interest rate of 6%, payable semiannually. On the date the loan is made, the Federal long-term rate is 12%, compounded semiannually.

(ii) The loan from T to A is a tax avoidance loan pursuant to paragraph (e)(2) of this section. The issue price of the debt instrument given in exchange for the loan is $1,311,805, and the total amount of foregone interest is $688,195. On the date the loan is made, A is treated as having received a refund of $688,195 of the purchase price of the property from S, thereby reducing A's basis in the property by this amount. T is treated as having paid a dividend of $688,195 to P, and P is treated as having made a contribution to the capital of S in the same amount.

Example (2). The facts are the same as in example (1), except that T loans the $2,000,000 to S immediately before the sale. A purchases the property for cash of $1,000,000 and assumes S's debt to T. On the date of the sale, the Federal long-term rate is 12%, compounded semiannually. The loan from T to S is a tax-avoidance loan. The issue price of the debt instrument and the amount of foregone interest are the same as in example (1). A's basis in the property is limited to $2,311,805 (see § 1.1274-7(d)). T is treated as having paid a dividend of $688,195 to P, and P is treated as having made a contribution to the capital of S in the same amount.

§ 1.9006-1 [Amended]

Par. 34. Paragraph (c)(1)(vii) of § 1.9006-1 is amended by removing the phrase "May 27, 1969." and adding in its place the phrase "May 27, 1969, and before July 18, 1984."

PART 3—CAPITAL CONSTRUCTION FUND

Par. 35. The authority citation for Part 3 continues to read as follows:

Authority: 26 U.S.C. 7805.

§ 3.2 [Amended]

Par. 36. Paragraph (d) of § 3.2 is amended by removing the phrase "ratable monthly portion" every place it appears and adding in its place the word "amount", and by removing the phrase "section 1232(a)(3)" every place it appears and adding in its place the phrase "section 1272".

§ 3.3 [Amended]

Par. 37. Paragraph (b) of § 3.3 is amended by removing the phrase "section 1232(a)(3)(E)" every place it appears and adding in its place the phrase "section 1272(d)(2)", and by removing the phrase "ratable monthly portion" every place it appears and adding in its place the word "amount".

PART 5f—TEMPORARY INCOME TAX REGULATIONS UNDER THE TAX EQUITY AND FISCAL RESPONSIBILITY ACT OF 1982

Par. 38. The authority citation for Part 5f continues to read as follows:

Authority: 26 U.S.C. 7805.

§ 5f.163-1 [Amended]

Par. 39. Paragraph (f) of § 5f.163-1 is amended by removing the word "1232(d)" from each place that it appears and adding in its place the word "1287", and by removing the phrase "section 1232B" from each place that it appears and adding in its place the phrase "section 1286".

PART 6a—TEMPORARY REGULATIONS UNDER TITLE II OF THE OMNIBUS RECONCILIATION ACT OF 1980

Par. 40. The authority citation for Part 6a continues to read as follows:

Authority: 26 U.S.C. 7805.

§ 6a.103A-2 [Amended]

Par. 41. Paragraph (i)(2)(vi)(B) of § 6a.103A-2 is amended by removing the phrase "section 1232(b)(2)" and adding in its place the phrase "section 1273(b)".

PART 25—GIFT TAX; GIFTS MADE AFTER DECEMBER 31, 1954

Par. 42. The authority for Part 25 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 25.2512-8 also issued under 26 U.S.C. 483(g) and 26 U.S.C. 1275(d).

Par. 43. Section 25.2512-4 is revised to read as follows:

§ 25.2512-4 Valuation of notes.

The fair market value of notes, secured or unsecured, is presumed to be the amount of unpaid principal, plus accrued interest to the date of the gift, unless the donor establishes a lower value. The fair market value of a debt instrument (as defined in § 1.1275-1(b)) whose issue price is determined under section 1273(b) (1), (2), or (3), or section 1274 is presumed to be its revised issue price (as defined in § 1.1275-1(h)). Unless returned at this value, it must be shown by satisfactory evidence that the note is worth less than the unpaid amount (because of the interest rate, or date of maturity, or other cause), or that the note is uncollectible in part (by reason of the insolvency of the party or parties liable, or for other cause), and that the property, if any, pledged or mortgaged as security is insufficient to satisfy it. See § 25.2512-8 and § 1.1012-2 for special rules relating to certain sales or exchanges of property. See § 25.7872-1 for special rules in the case of gift loans (within the meaning of § 1.7872-4(b)) made after June 6, 1984.

Par. 44. Section 25.2512-8 is revised to read as follows:

§ 25.2512-8 Transfers for insufficient or excessive consideration.

Transfers reached by the gift tax are not confined to those only which, being without a valuable consideration, accord with the common law concept of gifts, but embrace as well sales, exchanges, and other dispositions of property for a consideration to the extent that the value of the property transferred by the donor differs from the value in money or money's worth of the consideration given therefor. However, a sale, exchange, or other transfer of property made in the ordinary course of business (a transaction which is bona fide, at arm's length, and free from any donative intent), will be considered as made for consideration in money or money's worth equal to the value of the property transferred. If the buyer issues one or more debt instruments as all or a part of the consideration for the property, then the property and the debt instruments shall be valued in accordance with the rules set forth in § 1.1012-2. A consideration not reducible to a value in money or money's worth, as love and affection, promise of marriage, etc., is to be wholly disregarded, and the entire value of the property transferred constitutes the amount of the gift. Similarly, a relinquishment or promised relinquishment of dower or curtesy, or of a statutory estate created in lieu of dower or curtesy, or of other material rights in the spouse's property or estate, shall not be considered to any extent a consideration "in money or money's worth." See, however, section 2516 and the regulations thereunder with respect to certain transfers incident to a divorce.

PART 514—FRANCE

Par. 45. The authority citation for Part 514 continues to read as follows:

Authority: 26 U.S.C. 7805.

§ 514.23 [Amended]

Par. 46. Section 514.23 is amended by removing the phrase "section 1232(b)" from paragraph (b) every place it appears and adding in its place the phrase "section 1273".

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on April 2, 1986, 8:45 a.m., and published in the issue of the Federal Register for April 8, 1986, 51 F.R. 12022)

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Louis Crown	Bayside, NY	Certified Public Accountant	Indefinite from March 14, 1986
David H. Heilman	Council Grove, KS	Attorney	Indefinite from March 14, 1986
Beryl W. Markwell	Elmhurst, IL	Certified Public Accountant	Twenty-four Months from March 20, 1986
Marc Pozner	Tenafly, NJ	Certified Public Accountant	Indefinite from March 14, 1986
A. Russel Lucid	Norwell, MA	Attorney	Indefinite from March 26, 1986
Gary E. Borushko	Grosse Pointe Wood, MI	Certified Public Accountant	Indefinite from April 7, 1986
Paul Skulsky	Spring Valley, NY	Certified Public Accountant	Indefinite from April 1, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before their Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Thomas G. Abernethy, Jr.	Jackson, MS	Attorney	March 7, 1986
Thomas H. Foxhill, Jr.	Pemberton, NJ	Enrolled Agent	April 12, 1986
Peter Parker	Baltimore, MD	Attorney	April 12, 1986

Announcement of the Suspension, Termination, or Consent to Voluntary Suspension or Termination of Enrollment to Perform Actuarial Services Under the Employee Retirement Income Security Act of 1974

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to indentify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
Robert E. Nemann	Cincinnati, OH	For three months effective April 9, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.72-4, 1.72-5, 1.72-6, 1.72-7, 1.72-9, 1.72-11, 1.403(b)-1(d)(4), 1.403(b)-1(d)(4)(ii), amended; 1.403(b)-1(d)(4)(iv), 1.401(a)-18, 1.401(j)-1 through 1.401(j)-6, removed; 1.403(b)-1(d)(4)(iv), added.	Unisex annuity tables	1986-16 I.R.B. 9	May 8, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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Key to Abbreviations:

RR	Revenue Ruling
RP	Revenue Procedure
TD	Treasury Decision
CD	Court Decision
PL	Public Law
EO	Executive Order
DO	Delegation Order
TDO	Treasury Department Order
TC	Tax Convention
SPR	Statement of Procedural Rules
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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

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A public hearing will be held on June 12, 1986, on proposed regulations relating to information returns, statements, and notifications required when there is a sale or exchange of partnership interests.

Announcement 86-62, page 19.
A public hearing will be held on June 5, 1986, on proposed regulations relating to the recapture of overall foreign losses.

INCOME TAX

Rev. Rul. 86-64, page 6.
Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for May 1986.

Rev. Rul. 86-65, page 5.
Fringe benefits; aircraft valuation formula. For purposes of section 1.61-2T(g) of the temporary regulations, relating to the rule for valuing noncommercial flights on employer-provided aircraft, the Standard Industry Fare Level (SIFL) cents-per-mile rates and the terminal charge in effect on December 31, 1985, are set forth.

Rev. Rul. 86-66, page 5.
Gross income; industrial project; leasing arrangement between corporation and political subdivision. A corporation described in Rev. Rul. 68-590 must include in its gross income amounts received by the bond trustee from the investment of the net bond proceeds during a temporary period and from the investment of the reserve fund if the investment income inures to the benefit of the corporation. Rev. Rul. 68-590 amplified.

Rev. Rul. 86-67, page 6.
Deductions; balance of a decedent's unamortized loan costs. The balance of unamortized loan costs incurred by a taxpayer may be deducted on the final income tax return for the year of the taxpayer's death.

Announcement 86-59, page 16.
Guidance is provided to taxpayers who make an election to accrue vacation pay under section 463 of the Code.

Announcement 86-65, page 19.
The Service will not follow the Tax Court's decision in *Orange and Rockland Utilities*, filed February 18, 1986, and *Public Service Co. of New Hampshire*, 78 T.C. 445 (1982), relating to the accrual of income of utilities.

EMPLOYEE PLANS

Announcement 86-60, page 17.
The dates for application of the provisions of Notice 86-3, relating to relief for certain employee plans that were not timely amended, have been extended. A straight 10-percent-per-month reduction in the number-of-months factor after the applicable compliance date has passed now applies to employer deductions, and additional provisions relate to the scope of relief provided to tax credit ESOP's.

EXCISE TAXES

Rev. Rul. 86-68, page 7.
Taxable sale price; excludability of certain transportation and delivery expenses. The actual transportation and delivery charges for shipping a truck directly from a manufacturer to a retail dealer's customer are includable in the dealer's taxable sale price to the extent that such charges do not exceed the charges that would have been incurred to ship the truck from the manufacturer to the retail dealer through whom the truck was ordered.

Announcement 86-63, page 19.
Taxpayers liable for the manufacturers excise tax on coal should start to report and pay the tax at the increased rate provided in Pub. L. 99-272 for the quarter ending June 30, 1986.

ADMINISTRATIVE

Rev. Proc. 86-22, page 9.
Penalties; substantial understatement; adequate disclosure. For returns required to be filed and that are actually filed in 1986, circumstances are identified under which the disclosure on a taxpayer's return of an item or a position taken, with no specific reference to sec-

(Continued on page 4)

Finding Lists begin on page 27.
Announcement of Disbarments and Suspensions begin on page 23.
Announcement of Notice of Proposed Rulemaking on page 25.

Department of the Treasury
Internal Revenue Service

T22.23:

1986-17

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

T22.23:

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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HIGHLIGHTS OF THIS ISSUE—Continued

ADMINISTRATIVE—Continued

tion 6661 of the Code, is adequate for reducing the understatement of income tax liability on which the penalty is imposed under section 6661.

Treasury Department Order 150-01, page 10.
Designation of Internal Revenue Districts. A complete list of Internal Revenue Districts is provided, including those districts that comprise an entire state and districts within certain states.

Treasury Department Order 150-02, page 12.
Establishment of certain offices in the National Office of the Internal Revenue Service. Certain offices continue as they existed prior to this order. The Appeals Division and the Corporation and Individual Tax Divisions are transferred to the Chief Counsel.

LR-4-86, page 15.
Amendments to the regulations under section 6103(j) of the Code relate to the disclosure of return information to the Bureau of the Census.

Announcement 86-64, page 19.
Form 2032, Contract Coverage Under Title II of the Social Security Act, which is used to enter into the agreement specified in section 3121(l) of the Code to extend coverage under the Social Security Act of U.S. citizens and resident aliens employed abroad by foreign affiliates, has been revised.

Announcement 86-66, page 21.
Form 4789, Currency Transaction Report, has been revised and this revised form must be used after July 1, 1986, for reporting cash transactions of more than $10,000.

Announcement 86-67, page 22.
Excess contributions made to an individual retirement account (IRA), plus earnings on such excess, that are distributed to the participant before the due date of his or her return, including extensions, may be reported by financial institutions and other trustees and issuers on current year Forms W-2P or 1099-R.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 61.—Gross Income Defined

Fringe benefits; aircraft valuation formula. For purposes of section 1.61-2T(g) of the temporary regulations, relating to the rule for valuing noncommercial flights on employer-provided aircraft, the Standard Industry Fare Level (SIFL) cents-per-mile rates and the terminal charge in effect on December 31, 1985, are set forth.

Rev. Rul. 86-65

For purposes of fringe benefit taxation under section 61 of the Internal Revenue Code, section 1.61-2T(g) of the Temporary Income Tax Regulations provides a rule for valuing noncommercial flights on employer-provided aircraft. Section 1.61-2T(g)(5) of the temporary regulations sets forth an aircraft valuation formula to determine the value of such flights. The value of a flight is determined by multiplying the base aircraft valuation formula for the period during which the flight was taken by the appropriate aircraft multiple provided in section 1.61-2T(g)(7) and then adding the applicable terminal charge. The value of a particular flight during the first 6 months of a calendar year is determined by using the base aircraft valuation formula (also known as the Standard Industry Fare Level formula or SIFL) and the terminal charge in effect on December 31 of the preceding year. The value of a particular flight during the last 6 months of a calendar year is determined by using the SIFL formula and terminal charge in effect on June 30 of that year. The SIFL cents-per-mile rates in the formula and the terminal charge are calculated by the Department of Transportation and are revised semi-annually.

The Department of Transportation has determined that the terminal charge in effect on December 31, 1985, is $26.19 and the SIFL formula in effect on December 31, 1985, is $.1433 per mile for the first 500 miles, $.1092 per mile for miles between 501 and 1500, and $.1050 per mile for miles over 1500.

26 CFR 1.61-1: Gross income.
(Also Section 103; 1.103-1.)

Gross income; industrial project; leasing arrangement between corporation and political subdivision. A corporation described in Rev. Rul. 68-590 must include in its gross income amounts received by the bond trustee from the investment of the net bond proceeds during a temporary period and from the investment of the reserve fund if the investment income inures to the benefit of the corportion. Rev. Rul. 68-590 amplified.

Rev. Rul. 86-66

ISSUE

Will the corporation described in Rev. Rul. 68-590, 1968-2 C.B. 66, be required to include in its gross income, under section 61 of the Internal Revenue Code, income received by the bond trustee from the investment of the net bond proceeds during a construction period and from the investment of the reserve fund where the investment income inures to the benefit of the corporation?

FACTS

Rev. Rul. 68-590 describes a typical industrial development bond financing arrangement involving the use of tax-exempt bonds to finance the purchase or construction of a project for a private industrial corporation. The revenue ruling treats the corporation as the owner of the project for federal income tax purposes.

Rev. Rul. 68-590 sets forth eight tax consequences of treating the corporation as owner of the project for federal income tax purposes. However, an additional question has arisen regarding the federal income tax treatment of any investment income received by the bond trustee when the trustee invests the net bond proceeds during the construction period or invests the portion of bond proceeds placed in a reserve fund, where the investment income is used to redeem bonds.

LAW AND ANALYSIS

Section 61(a) of the Code provides that, except as otherwise provided by law, gross income means all income from whatever source derived.

Rev. Rul. 68-590 concludes that the corporation described therein must take into account any premium or discount on the bonds under section 61 of the Code. The ruling also concludes that the corporation may deduct the trustee's fees pursuant to section 162. Thus, the corporation is treated as the owner of the net bond proceeds as well as the owner of the project financed with the bond proceeds. Accordingly, any investment income received by the bond trustee when the trustee invests the net bond proceeds during a temporary period, or invests the portion of bond proceeds placed in a reserve fund, under circumstances in which the investment income inures to the benefit of the corporation, will be considered the gross income of the corporation.

HOLDING

The corporation must include in its gross income, under section 61 of the Code, income received by the bond trustee from the investment of the net bond proceeds during a construction period and from the investment of the reserve fund. However, for industrial development bonds issued after December 31, 1984, an amount required to be paid to the United States under section 103(c)(6)(D) is not gross income and no deduction is allowed for any amount paid to the United States under section 103(c)(6)(D). *See* section 103(c)(6)(G).

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 68-590 is amplified.

Section 103.—Interest on Certain Government Obligations

26 CFR 1.103-1: Interest upon obligations of a State, Territory, etc.

Whether, for industrial development bonds issued after December 31, 1984, an amount required to be paid to the United States under section 103(c)(6)(D) of the Code is gross income. See Rev. Rul. 86-66, this page.

Section 461.—General Rule for Taxable Year of Deduction

26 CFR 1.461-1: General rule for taxable year of deduction.

Deductions; balance of a decedent's unamortized loan costs. The balance of unamortized loan costs incurred by a taxpayer may be deducted on the final income tax return for the year of the taxpayer's death.

Rev. Rul. 86-67

ISSUE

Whether the balance of unamortized mortgage loan costs incurred by a taxpayer may be deducted on the income tax return for the year of the taxpayer's death.

FACTS

A died in 1983. During *A*'s lifetime, *A* purchased a number of single-family homes, townhouses, and condominiums that *A* leased to others. *A* financed each purchase by obtaining a mortgage loan from a financial institution. In order to obtain the mortgages, *A* incurred various loan costs for services provided by the lender, such as appraisal fees, settlement fees, and notary fees. *A* also incurred other expenses in connection with obtaining the mortgages including commissions, abstract fees, and recording fees. None of these expenses were in the nature of "points," that is, charges made for the use or forbearance of money that are considered to be interest. These various expenses were capitalized and amortized over the terms of the mortgage loans to which such expenses related. When *A* died in 1983, there was a total balance of *x* dollars of unamortized loan costs with respect to the mortgages. *A*'s estate continued to make payments on the loans. The balance of the unamortized mortgage loan costs was deducted on *A*'s final income tax return for 1983.

LAW AND ANALYSIS

Expenses incurred to obtain a loan are capital expenditures that must be amortized over the period of the loan. *See Enoch v. Commissioner*, 57 T.C. 781, 794-95 (1972), *acq.* on this issue, 1974-1 C.B. 1, in which the United States Tax Court held that loan expenses must be capitalized and cannot be deducted in the year paid. *See also* Rev. Rul. 70-360, 1970-2 C.B. 103.

In *S. & L. Building Corp. v. Commissioner*, 19 B.T.A. 788 (1930), *acq.* X-1 C.B. 60 (1931), a corporation was allowed to deduct the balance of unamortized loan costs in the year mortgaged property was sold and the mortgage assumed by the purchaser. The court said the mortgage fees were a cost of the use of the borrowed money, rather than a cost of the property securing the mortgage. When a taxpayer no longer bears the burden of a mortgage, a deduction should be allowed for the remaining portion of the associated unamortized mortgage loan fees. In *Longview Hilton Hotel Company v. Commissioner*, 9 T.C. 180 (1947), *acq.* 1947-2 C.B. 3, the taxpayer corporation was allowed a deduction for similar costs upon its dissolution when it transferred the mortgaged property to its eight shareholders who assumed the mortgage indebtedness. In *Anover Realty Corporation v. Commissioner*, 33 T.C. 671 (1960), a transferee corporation that assumed a mortgage on transferred property argued that loan expenses that were incurred by the transferor for the sole purpose of acquiring a business asset (the mortgaged property) should follow the asset when it was transferred. The court stated that the loan expenses were made to obtain the use of the money; the purpose of the loan itself did not matter. "If the debt is assumed by the transferee it merely marks an earlier end to the period for which the borrower had the use of the money, which means the borrower . . . can take the unamortized balance as a deduction in the year of transfer." 33 T.C. at 675.

Expenses incurred to obtain a loan are distinguishable from expenses incurred in connection with the acquisition of an income-producing asset, such as a lease. For example, in *Plaza Investment Co. v. Commissioner*, 5 T.C. 1295 (1945), the taxpayer corporation had paid a commission to a broker who had secured a tenant for a long term lease. Upon dissolution, the corporation transferred the lease to its shareholders and deducted the balance of the commission on its final return. The court indicated that the commission was a capital expenditure to acquire an income-producing asset. The dissolution of the corporation did not terminate the lease, so the benefit of the expense continued until the lease expired resulting in the expense being amortized over the remainder of the lease term. The court distinguished *S. & L. Building Corp.* by pointing out that payments to obtain a loan do not add value to the mortgaged property and do not result in acquiring an income-producing asset; they are expenses in connection with the creation of a liability. *Accord, Wolan v. Commissioner*, 184 F.2d. 101 (10th Cir. 1950), *aff'g* No. 17,250 (T.C.M. 1949). *See also* Rev. Rul. 81-161, 1981-1 C.B. 313.

Although none of the above cited authorities concerns the deduction of unamortized loan costs of a decedent, the principles set forth in these authorities are applicable to the facts here. A taxpayer's death, a corporation's dissolution, or an arm's length sale of mortgaged property—all terminate the use of loan proceeds and mark the appropriate time to deduct the balance of unamortized loan costs. The authorities cited above are not concerned with the nature of the termination of the taxpayer's liability. Here, *A*'s death ends the period during which *A* benefited from the expenses incurred to obtain the loans.

HOLDING

The *x* dollars of unamortized mortgage loan costs *A* incurred is deductible on *A*'s final income tax return for 1983.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of May 1986. See Rev. Rul. 86-64, below.

Section 483.—Interest on Certain Deferred Payments

Federal short-term, mid-term and long-term rates are set forth for the month of May 1986. See Rev. Rul. 86-64, below.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 467, 483, 7872.)

Rev. Rul. 86-64

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of May 1986 are as follows:

	Period for Compounding			
	Annual	Semiannual	Quarterly	Monthly
Short-Term				
AFR	6.95%	6.83%	6.77%	6.73%
110% AFR	7.65%	7.51%	7.44%	7.40%
120% AFR	8.37%	8.20%	8.12%	8.06%
Mid-Term				
AFR	7.43%	7.30%	7.23%	7.19%
110% AFR	8.19%	8.03%	7.95%	7.90%
120% AFR	8.95%	8.76%	8.67%	8.60%
Long-Term				
AFR	7.81%	7.66%	7.59%	7.54%
110% AFR	8.61%	8.43%	8.34%	8.29%
120% AFR	9.40%	9.19%	9.09%	9.02%

Section 4051.—Imposition of Tax on Heavy Trucks and Trailers Sold at Retail

26 CFR 145.4051-1: Imposition of tax on heavy trucks and trailers sold at retail.

Whether certain delivery expenses are includable in taxable sale price as defined in section 4216(a) of the Code for purposes of the retailers excise tax on trucks imposed by section 4051(a)(1) of the Code. See Rev. Rul. 86-68, below.

Section 4052.—Definitions and Special Rules

26 CFR 145.4052-1: Special rules and definitions.
(Also Sections 4051; 4216; 145.4051-1, 48.4216(a)-2.)

Taxable sale price; excludability of certain transportation and delivery expenses. The actual transportation and delivery charges for shipping a truck directly from a manufacturer to a retail dealer's customer are includable in the dealer's taxable sale price to the extent that such charges do not exceed the charges that would have been incurred to ship the truck from the manufacturer to the retail dealer through whom the truck was ordered.

Rev. Rul. 86-68

ISSUE

If a taxable heavy truck is shipped by the manufacturer to a dealer's business location for pickup by the customer, what transportation and delivery expenses are excludable from the price for which the truck is sold by the dealer for purposes of the retailers excise tax imposed on heavy trucks and trailers by section 4051(a)(1) of the Internal Revenue Code? What expenses are excludable by the dealer if the truck is shipped by the manufacturer directly to the customer's location?

FACTS

Situation 1. A trucking company orders a taxable truck from a retail truck dealer. The truck is thereafter shipped by the truck manufacturer to the dealer's business location, where it is picked up by the trucking company. The usual business practice of the dealer is to have trucks delivered to its business premises for eventual customer pickup.

Situation 2. A trucking company orders a taxable truck from a retail truck dealer. Under the contractual arrangement between that dealer and its customer, the trucking company, the truck is shipped by the truck manufacturer from the manufacturer's factory directly to the customer.

LAW AND ANALYSIS

Section 4051(a)(1) of the Code imposes a tax on the first retail sale of certain enumerated articles, including truck chassis and bodies that have a gross vehicle weight of more than 33,000 pounds. The tax is 12 percent of the amount for which the article is sold.

Section 4052(b)(1)(A) of the Code provides that, in determining the price of an article for purposes of the tax on the retail sale of trucks, there shall be included any charge incident to placing the article in condition ready for use.

Section 145.4052-1(d)(1) of the Temporary Excise Tax Regulations provides that the price for which an article is sold includes the total consideration paid for the article, whether the consideration is paid in money, services, or other forms. In addition, there shall be included any charge incident to placing the article in condition ready for use. Similar rules to section 4216(a) of the Code and the regulations thereunder, relating to charges to be included in the price and excluded from the price, shall apply. For example, charges for transportation, delivery, insurance, and installation (other than installation charges to which section 4051(b) applies), and other expenses actually incurred in connection with the delivery of an article to a purchaser pursuant to a bona fide sale, shall be excluded from the price in computing the tax.

Under section 4216(a) of the Code (which defines "price" for purposes of the Chapter 32 manufacturers excise taxes) and section 48.4216(a)-2(b) of the Manufacturers and Retailers Excise Tax Regulations, charges for transportation, delivery, and other expenses actually incurred in connection with the delivery of an article to a purchaser pursuant to a bona fide sale shall be excluded from the sale price in computing the tax. Such charges include all items of transportation, delivery, and similar expense incurred after shipment to a customer begins, in response to the customer's order, pursuant to a bona fide sale. However, costs of such nature incurred by a manufacturer in transporting, in the normal course of business and for its benefit and convenience, articles from a factory or port of entry to a warehouse or other facility (regardless of the location of such warehouse or other facility) are not considered as being incurred in connection with the delivery of an article to a purchaser pursuant to a bona fide sale, and charges therefor cannot be excluded from the sale price in computing tax liability.

Section 48.4216(a)-2(b)(3) of the regulations provides that for purposes of computing the taxable sale price of articles, it is immaterial whether the transportation, delivery, or other services of the type to which that section has application are performed by a common carrier or independent agency for, or on behalf of, the manufacturer, producer, or importer, or are performed by the manufacturer, producer, or importer with the use of its own vehicles or other facilities. In determining whether an expense is an excludable transportation or delivery expense, "only those expenses incurred by reason of the fact that the purchaser accepts delivery at some point other than the manufacturer's place of business shall be considered excludable transportation or delivery expenses."

The rules under section 4216(a) of the Code, and the regulations thereunder, generally apply to determination of price in connection with a sale subject to a manufacturers excise tax, as opposed to a retailer's excise tax. However, as noted above, section 145.4052-1(d)(1) of the temporary regulations provides that similar rules shall apply to determination of price in connection with a sale subject to the retailers excise tax on heavy trucks and trailers.

Most of the concepts employed under section 4216(a) of the Code are directly applicable to the retailer's tax imposed by section 4051. For instance, the "purchaser" under the manufacturers tax plays the same role as the "purchaser" under the retailers tax. On the other hand, other concepts are applicable only in analogue. Thus the taxpayer retailer's place of business takes the place of the taxpayer manufacturer's place of business.

When a customer places a truck order with a retail dealer and the truck is thereafter shipped from the manufacturer to the dealer, all charges for delivery and transportation to the dealer are includable in the taxable sale price of the truck. The exclusion of charges for transportation and delivery under section 145.4052-1(d)(1) of the temporary regulations is not applicable in *Situation 1* because the charges are incurred to deliver the truck to the taxpayer retailer's place of business. *See* section 48.4216(a)-2(b)(3) of the regulations.

Although in *Situation 2* the shipment of the truck is directly from the truck manufacturer to the retail dealer's customer, the exclusion for transportation and delivery charges provided in section 145.4052-1(d)(1) of the temporary regulations and section 48.4216(a)-2(b) of the regulations applies only with respect to actual or constructive shipments *from the taxpayer* (the retailer in the case of section 4051 of the Code, and the manufacturer in the case of section 4216), and not with respect to actual or constructive shipments *to the taxpayer*.

Therefore, in computing the portion of the transportation and delivery charges in *Situation 2* includable in the taxable sale price for purposes of the section 4051(a)(1) retailers excise tax, there is deemed to be an initial constructive shipment of the truck from the manufacturer to the retailer through whom the trucking company customer placed the order. If the actual charge for transportation between the manufacturer and the trucking company customer is greater than the charge would have been for transportation between the manufacturer and the retailer, then only a portion of the actual transportation charge is includable in the sale price. The includable amount is the charge that would have been incurred if the truck had been shipped from the manufacturer to the retailer instead of directly from the manufacturer to the customer. The balance of the actual transportation charge is excludable from the taxable sale price because it was "incurred by reason of the fact that the purchaser accepts delivery at some point other than" the retailer's place of business. If the actual charge for transportation between the maufacturer and the trucking company customer is less than the charge would have been if the truck had been shipped from the manufacturer to the retailer through whom the order was placed, then the entire actual transportation charge for the shipment of the truck from the manufacturer to the customer is includable in the taxable sale price.

HOLDING

In *Situation 1*, the transportation and delivery charges for shipping the truck from the manufacturer to the retail dealer are includable in the taxable sale price.

In *Situation 2*, the actual transportation and delivery charges for shipping the truck directly from the manufacturer to the retail dealer's customer are includable in the taxable sale price to the extent that such charges do not exceed the charges that would have been incurred to ship the truck from the manufacturer to the retail dealer through whom the truck was ordered. The balance (if any) of the actual transportation and delivery charges would be excludable from the taxable sale price.

Section 4216.—Definition of Price

26 CFR 48.4216(a)-2: Charges to be included in sale price.

Whether certain delivery expenses are includable in taxable sale price as defined in section 4261(a) of the Code for purposes of the retailers excise tax on trucks imposed by section 4051(a)(1) of the Code. See Rev. Rul. 86-68, page 7.

Section 6661.—Substantial Understatement of Liability

26 CFR 1.6661-4: Disclosure of certain information.

Guidance is provided, for returns filed in 1986, under which the disclosure on a taxpayer's return of an item or a position taken is adequate disclosure for the purposes of reducing the understatement under section 6661 of the Code. See Rev. Proc. 86-22, page 9.

Section 7872.—Treatment of Loans with Below-Market Interest Rates

Federal short-term, mid-term and long-term rates are set forth for the month of May 1986. See Rev. Rul. 86-64, page 6.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.105: Examination of returns and claims for refund, credit or abatement; determination of correct tax liability.
(Also Part I, Section 6661; 1.6661-4.)

Rev. Proc. 86-22

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to identify, for returns filed in 1986, circumstances under which the disclosure on a taxpayer's return of an item or a position taken, with no specific reference to section 6661 of the Internal Revenue Code, is adequate disclosure for the purpose of reducing the understatement under section 6661.

SEC. 2. BACKGROUND

.01 Section 6661(a) of the Code imposes an addition to tax in situations where there is substantial understatement. A substantial understatement is defined as an understatement of liability for income tax which exceeds the greater of 10 percent of the amount required to be shown on the return or $5,000 ($10,000 in the case of a corporation other than an S corporation or a personal holding company). Under section 6661(b)(2) an understatement is defined as the excess of the amount of tax required to be shown on the return for the taxable year over the amount of the tax imposed which is shown on the return (reduced by any rebate within the meaning of section 6211(b)(2)).

.02 In the case of an item not attributable to a tax shelter, the amount of the understatement is reduced if the taxpayer discloses in the return or an attachment thereto the identity and amount of the item as well as the specific facts or the position taken relevant to the tax treatment of the item. Disclosure on a return of items attributable to a tax shelter does not reduce an understatement.

.03 Under section 6661(c) of the Code, the Secretary may waive all or part of the addition to tax provided by section 6661(a) if the taxpayer shows that there was reasonable cause for the understatement and that the taxpayer acted in good faith.

.04 In general, rules providing guidance on the adequacy of disclosure for purposes of reducing an understatement under section 6661 of the Code are set forth in regulations. Under section 1.6661-4(c) of the Income Tax Regulations, the Commissioner may by revenue procedure prescribe the circumstances in which information provided on the return in accordance with the applicable forms and instructions is adequate disclosure for purposes of section 6661 of the Code. The taxpayer must furnish all required information in accordance with the applicable forms and instructions, and the money amounts entered on these forms must be verifiable. This revenue procedure provides guidelines as to when such disclosure is adequate. Guidance for returns filed in 1983, 1984, and 1985 was provided by Rev. Proc. 83-21, 1983-1 C.B. 680, Rev. Proc. 84-19, 1984-1 C.B. 433, and Rev. Proc. 85-19, 1985-1 C.B. 520.

SEC. 3. PROCEDURE

Additional disclosure of facts relevant to, or positions with respect to, issues involving any of the items set forth below is unnecessary for purposes of reducing any understatement of tax under section 6661 of the Code provided, however, that the forms and attachments are completed in a clear manner and in accordance with the instructions thereto, the money amounts entered on the forms are verifiable, and the information on the return is disclosed in the manner described below. For purposes of this revenue procedure, a number is verifiable if, on audit, the taxpayer can demonstrate the origin of the number (even if that number is not ultimately accepted by the Internal Revenue Service).

(a) Schedule A, Form 1040, Itemized Deductions:

(1) Medical Expenses: Complete lines 1-5 supplying all required information. Line 2c must be itemized listing each item and its cost.

(2) Taxes: Complete lines 6-10 supplying all required information. Line 9 must list each type of tax and amount paid.

(3) Interest Expense: Complete lines 11-14 supplying all required information. Line 13 must list the type of expense and the amount paid. This section 3(a)(3) does not apply to amounts disclosed under section 163(d) of the Code unless Form 4952, Investment Interest Expense Deduction, is completed, or to any amounts disallowed under section 265.

(4) Contributions: Complete lines 15-18 supplying all required information. If a contribution of property other than cash is made, and the claimed value of the contribution exceeds $500, a properly completed Form 8283, Noncash Charitable Contributions, must be attached to the return.

(5) Casualty and Theft Losses: Form 4684, Casualties and Thefts, must be completed and attached to the return; Each item or article for which a casualty or theft loss is claimed must be listed on Form 4684.

(b) Trade or Business Expenses:

(1) Casualty and Theft Losses: The procedure outlined in Section 3(a)(5) above, must be followed.

(2) Legal Fees: The amount paid must be stated.

(3) Specific Bad Debt Charge-off: The amount written off must be stated.

(4) Reserve for Bad Debts: Question K, Form 1120A; Schedule F, Form 1120; or required attached statement, Form 1120S; must be completed, supplying all required information.

(5) Reasonableness of Officers' Compensation: Schedule E, Form 1120 must be completed where required by instructions. The time devoted to business must be expressed as a percentage as opposed to "part" or "as needed". This section 3(b)(5) does not apply to "golden parachute" compensation prohibited by section 280G of the Code.

(6) Repair as Opposed to Capital Expenditure: The amount of repairs stated.

(7) Taxes (other than foreign taxes): The amount of taxes stated.

(c) Schedule M-1, Form 1120, Reconciliation of Income Per Books With Income Per Return:

An item clearly identified on Schedule M-1, Form 1120, but only if—

(1) The amount of the deviation from the financial books and records is not the result of a computation that includes the netting of several items; and

(2) The information provided reasonably may be expected to apprise the Service of the nature of the potential controversy concerning the tax treatment of the item.

(d) Other:

(1) Sale or Exchange of Principal Residence: Complete Form 2119, Sale of Exchange of Principal Residence, or similar statement containing the same information, and attach to the return.

(2) Employee Business Expenses: Complete Form 2106, Employee Business Expenses, or similar statement containing the same information, and attach to the return.

(3) Moving Exenses: Complete Form 3903, Moving Expense Adjustment, or similar statement containing the same information, and attach to the return.

(4) Jobs Credits and WIN credit carryovers: Amounts shown on Line 6, Form 3800, General Business Credit.

(5) Gasoline and special fuels credit: Amounts shown on Form 4136, Computation of Credit for Federal Tax on Gasoline and Special Fuels.

(e) Foreign Tax Items:

(1) International boycott transactions: Transactions disclosed on Form 5713, International Boycott Report.

(2) Subpart F income: Amounts shown on Form 5471, Information Return with Respect to a Foreign Corporation, and Schedule J.

(3) Intercompany transactions: Transactions and amounts shown on Form 5471, Schedule M.

(4) With respect to foreign taxes paid or accrued, additional disclosure is unnecessary if Form 1116, Computation of Foreign Tax Credit, Part II, in the case of individuals, and Form 1118, Computation of Foreign Tax Credit—Corporations, Schedule B, Part I, Item 4, and Schedule C, Item 6, Schedules D, and E, Item 5, as appropriate, are completed, supplying all information called for *and* attaching the evidence required by section 1.905-2 of the regulations (receipts for the payment of the foreign tax or a copy of the foreign tax return).

SEC. 4. EFFECTIVE DATE

This revenue procedure is effective for returns filed in 1986, the due date (regardless of extensions) for filing of which is after December 31, 1985.

Treasury Department Order 150-01[1]

Designation of Internal Revenue Districts

Dated: February 27, 1986

Under the authority given to the President to establish and alter Internal Revenue Districts by section 7621 of the Internal Revenue Code of 1954, as amended, and vested in me as Secretary of the Treasury by Executive Order 10289, approved September 17, 1951, as made applicable to the Internal Revenue Code of 1954 by Executive Order 10574, approved November 5, 1954 [1954-2 C.B. 732], and pursuant to the authority vested in me by section 321(b) of 31 U.S.C., and Reorganization Plan No. 1 of 1952 as made applicable to the Internal Revenue Code of 1954 by section 7804(a) of such Code and by Executive Order 10574, the following Internal Revenue Districts continue as they existed prior to this order, with the changes noted below.

1. Designation of Internal Revenue Districts That Comprise an Entire State

Alabama, headquarters located in Birmingham, Alabama
Alaska, headquarters located in Anchorage, Alaska
Arizona, headquarters located in Phoenix, Arizona
Arkansas, headquarters located in Little Rock, Arkansas
Colorado, headquarters located in Denver, Colorado
Connecticut, headquarters located in Hartford, Connecticut
Delaware, headquarters located in Wilmington, Delaware
Florida, headquarters located in Jacksonville, Florida
Georgia, headquarters located in Atlanta, Georgia
Hawaii, headquarters located in Honolulu, Hawaii
Idaho, headquarters located in Boise, Idaho
Indiana, headquarters located in Indianapolis, Indiana
Iowa, headquarters located in Des Moines, Iowa
Kansas, headquarters located in Wichita, Kansas
Kentucky, headquarters located in Louisville, Kentucky
Louisiana, headquarters located in New Orleans, Louisiana
Maine, headquarters located in Augusta, Maine
Maryland (including the District of Columbia), with headquarters located in Baltimore, Maryland
Massachusetts, headquarters located in Boston, Massachusetts
Michigan, headquarters located in Detroit, Michigan
Minnesota, headquarters located in St. Paul, Minnesota
Mississippi, headquarters located in Jackson, Mississippi
Missouri, headquarters located in St. Louis, Missouri
Montana, headquarters located in Helena, Montana
Nebraska, headquarters located in Omaha, Nebraska
Nevada, headquarters located in Las Vegas, Nevada
New Hampshire, headquarters located in Portsmouth, New Hampshire
New Jersey, headquarters located in Newark, New Jersey
New Mexico, headquarters located in Albuquerque, New Mexico
North Dakota, headquarters located in Fargo, North Dakota
North Carolina, headquarters located in Greensboro, North Carolina
Oklahoma, headquarters located in Oklahoma City, Oklahoma
Oregon, headquarters located in Portland, Oregon
Rhode Island, headquarters located in Providence, Rhode Island
South Dakota, headquarters located in Aberdeen, South Dakota
South Carolina, headquarters located in Columbia, South Carolina
Tennessee, headquarters located in Nashville, Tennessee
Utah, headquarters located in Salt Lake City, Utah
Vermont, headquarters located in Burlington, Vermont
Virginia, headquarters located in Richmond, Virginia
Washington, headquarters located in Seattle, Washington
West Virginia, headquarters located in Parkersburg, West Virginia
Wisconsin, headquarters located in Milwaukee, Wisconsin
Wyoming, headquarters located in Cheyenne, Wyoming

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[1] Filed by the Office of the Federal Register on March 18, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 19, 1986, 51 F.R. 9571.

2. Designation of Internal Revenue Districts Within Certain States

a. California

(1) *Laguna Niguel District.* Shall include the Counties of Imperial, Orange Riverside, San Bernardino, San Diego, and that portion of Los Angeles County serviced by the Carson post of duty, in the State of California, with the headquarters office located in Laguna Niguel, California. (The Carson post of duty services the area of Los Angeles County which is generally bordered by the Artesia Freeway on the north, the Pacific Ocean on the west and south, and the Orange County line on the east, and includes in total the following 1982 zip code areas: 90254, 90274, 90277, 90278, 90501, 90502, 90503, 90504, 90505, 90507, 90508, 90509, 90510, 90701, 90706, 90710, 90712, 90713, 90714, 90715, 90716, 90717, 90731, 90732, 9073, 90744, 90745, 90746, 90747, 90749, 90802, 90803, 90804, 90805, 90806, 90807, 90808, 90809, 90810, 90813, 90814, 90815, 90822, and 90840).

(2) *Los Angeles District.* Shall include the County of Los Angeles, except for that portion serviced by the Carson post of duty, in the State of California, with the headquarters office located in Los Angeles, California.

(3) *San Jose District.* Shall include the Counties of Fresno, Inyo, Kern, Kings, Madera, Mariposa, Merced, Mono, Monterey, San Benito, San Luis Obispo, Santa Barbara, Santa Clara, Santa Cruz, Stanislaus, Tulare, Tuolumne, and Ventura, in the State of California, with the headquarters office located in San Jose, California.

(4) *Sacramento District.* Shall include the Counties of Alpine, Amador, Butte, Calaveras, Colusa, Contra Costa, Del Norte, El Dorado, Glenn, Humboldt, Lake, Lassen, Marin, Mendocino, Modoc, Napa, Nevada, Placer, Plumas, Sacramento, San Joaquin, Shasta, Sierra, Siskiyou, Solano, Sonoma, Sutter, Tehama, Trinity, Yolo, and Yuba in the State of California, with the headquarters office located in Sacramento, California.

(5) *San Francisco District.* Shall include the Counties of Alameda, San Francisco and San Mateo, in the State of California, with the headquarters office located in San Francisco, California.

b. Illinois

(1) *Chicago District.* Shall include the Counties of Boone, Bureau, Carroll, Cook, De Kalb, Du Page, Grundy, Henry, Jo Daviess, Kane, Kankakee, Kendall, Lake, La Salle, Lee, McHenry, Marshall, Mercer, Ogle, Putnam, Rock Island, Stark, Stephenson, Whiteside, Will, and Winnebago within the State of Illinois, with the headquarters office located in Chicago, Illinois.

(2) *Springfield District.* Shall include the Counties of Adams, Alexander, Bond, Brown, Calhoun, Cass, Champaign, Christian, Clark, Clay, Clinton, Coles, Crawford, Cumberland, DeWitt, Douglas, Edgar, Edwards, Effingham, Fayette, Ford, Franklin, Fulton, Gallatin, Greene, Hamilton, Hancock, Hardin, Henderson, Iroquois, Jackson, Jasper, Jefferson, Jersey, Johnson, Knox, Lawrence, Livingston, Logan, McDonough, McLean, Macon, Macoupin, Madison, Marion, Mason, Massac, Menard, Monroe, Montgomery, Morgan, Moultrie, Peoria, Perry, Piatt, Pike, Pope, Pulaski, Randolph, Richland, St. Clair, Saline, Sangamon, Schuyler, Scott, Shelby, Tazewell, Union, Vermilion, Wabash, Warren, Washington, Wayne, White, Williamson, and Woodford within the State of Illinois, with the headquarters office located in Springfield, Illinois.

c. New York

(1) *Brooklyn District.* Shall include the Counties of Kings, Nassau, Queens, and Suffolk within the State of New York, with the headquarters office located in Brooklyn, New York.

(2) *Manhattan District.* Shall include Blackwells Island, Manhattan Island, Staten Island, Randalls Island, and Wards Island; and the Counties of Bronx, Richmond, Rockland, and Westchester within the State of New York, with the headquarters office located in New York, New York.

(3) *Albany District.* Shall include the Counties of Albany, Clinton, Columbia, Dutchess, Essex, Franklin, Fulton, Greene, Hamilton, Montgomery, Orange, Putnam, Rensselaer, Saratoga, Schenectady, Schoharie, St. Lawrence, Sullivan, Ulster, Warren, and Washington within the State of New York, with the headquarters office located in Albany, New York.

(4) *Buffalo District.* Shall include the Counties of Allegany, Broome, Cattaraugus, Cayuga, Chautauque, Chemung, Chenango, Cortland, Delaware, Erie, Genesee, Herkimer, Jefferson, Lewis, Livingston, Madison, Monroe, Niagara, Oneida, Onondaga, Ontario, Orleans, Oswego, Otsego, Schuyler, Seneca, Steuben, Tioga, Tompkins, Wayne, Wyoming, and Yates, within the State of New York with the headquarters office located in Buffalo, New York.

d. Ohio

(1) *Cleveland District.* Shall include the Counties of Allen, Ashland, Ashtabula, Auglaize, Belmont, Carroll, Champaign, Columbiana, Crawford, Cuyahoga, Darke, Defiance, Erie, Fulton, Geauga, Hancock, Hardin, Harrison, Henry, Holmes, Huron, Jefferson, Lake, Logan, Lorain, Lucas, Mahoning, Medina, Mercer, Monroe, Ottawa, Paulding, Portage, Putnam, Richland, Sandusky, Seneca, Shelby, Stark, Summit, Trumbull, Tuscarawas, Van Wert, Wayne, Williams, Wood, and Wyandot within the State of Ohio, with the headquarters office located in Cleveland, Ohio.

(2) *Cincinnati District.* Shall include the Counties of Adams, Athens, Brown, Butler, Clark, Clermont, Clinton, Coshocton, Delaware, Fairfield, Fayette, Franklin, Gallia, Greene, Guernsey, Hamilton, Highland, Hocking, Jackson, Knox, Lawrence, Licking, Madison, Marion, Meigs, Miami, Montgomery, Morgan, Morrow, Muskingum, Noble, Perry, Pickaway, Pike, Preble, Ross, Scioto, Union, Vinton, Warren, and Washington within the State of Ohio, with the headquarters office located in Cincinnati, Ohio.

e. Pennsylvania

(1) *Philadelphia District.* Shall include the Counties of Adams, Berks, Bradford, Bucks, Carbon, Chester, Columbia, Cumberland, Dauphin, Delaware, Juniata, Lackawanna, Lancaster, Lebanon, Lehigh, Luzerne, Lycoming, Monroe, Montgomery, Montour, Northampton, Northumberland, Perry, Philadelphia, Pike, Schuylkill, Snyder, Sullivan, Susquehanna, Tioga, Union, Wayne, Wyoming, and York within the State of Pennsylvania, with the head-

quarters office located in Philadelphia, Pennsylvania.

(2) *Pittsburgh District.* Shall include the Counties of Allegheny, Armstrong, Beaver, Bedford, Blair, Butler, Cambria, Cameron, Centre, Clarion, Clearfield, Clinton, Crawford, Elk, Erie, Fayette, Forest, Franklin, Fulton, Greene, Huntingdon, Indiana, Jefferson, Lawrence, McKean, Mercer, Mifflin, Potter, Somerset, Venango, Warren, Washington, and Westmoreland within the State of Pennsylvania, with the headquarters office located in Pittsburgh, Pennsylvania.

f. Texas

(1) *Austin District.* Shall include the Counties of Aransas, Atascosa, Austin, Bandera, Bastrop, Bee, Bell, Bexar, Blanco, Bosque, Brazos, Brewster, Brooks, Burleson, Burnet, Caldwell, Calhoun, Cameron, Colorado, Comal, Coryell, Culberson, DeWitt, Dimmitt, Duval, Edwards, El Paso, Falls, Fayette, Freestone, Frio, Gillespie, Goliad, Gonzales, Grimes, Guadalupe, Hamilton, Hays, Hidalgo, Hill, Hudspeth, Jackson, Jeff Davis, Jim Hogg, Jim Wells, Karnes, Kendall, Kenedy, Kerr, Kimble, Kinney, Kleberg, Lampasas, LaSalle, Lavaca, Lee, Leon, Limestone, Live Oak, Llano, McCulloch, McLennan, McMullen, Madison, Mason, Matagorda, Maverick, Medina, Milam, Nueces, Pecos, Presidio, Real, Reeves, Refugio, Robertson, San Patricio, San Saba, Somervell, Starr, Terrell, Travis, Uvalde, Val Verde, Victoria, Waller, Washington, Webb, Wharton, Willacy, Williamson, Wilson, Zapata, and Zavala within the State of Texas, with the headquarters office located in Austin, Texas.

(2) *Dallas District.* Shall include the Counties of Anderson, Andrews, Angelina, Archer, Armstrong, Bailey, Baylor, Borden, Bowie, Briscoe, Brown, Callahan, Camp, Carson, Cass, Castro, Cherokee, Childress, Clay, Cochran, Coke, Coleman, Collin, Collingsworth, Comanche, Concho, Cooke, Cottle, Crane, Crockett, Crosby, Dallam, Dallas, Dawson, Deaf Smith, Delta, Denton, Dickens, Donley, Eastland, Ector, Ellis, Erath, Fannin, Fisher, Floyd, Foard, Franklin, Gaines, Garza, Glasscock, Gray, Grayson, Gregg, Hale, Hall, Hansford, Hardeman, Harrison, Hartley, Haskell, Hemphill, Henderson, Hockley, Hood, Hopkins, Houston, Howard, Hunt, Hutchinson, Irion, Jack, Johnson, Jones, Kaufman, Kent, King, Knox, Lamar, Lamb, Lipscomb, Loving, Lubbock, Lynn, Marion, Martin, Menard, Midland, Mills, Mitchell, Montague, Moore, Morris, Motley, Nacogdoches, Navarro, Nolan, Ochiltree, Oldham, Palo Pinto, Panola, Parker, Parmer, Potter, Rains, Randall, Reagan, Red River, Roberts, Rockwall, Runnels, Rusk, Sabine, San Augustine, Schleicher, Scurry, Shackelford, Shelby, Sherman, Smith, Stephens, Sterling, Stonewall, Sutton, Swisher, Tarrant, Taylor, Terry, Throckmorton, Titus, Tom Green, Upshur, Upton, Van Zandt, Ward, Wheeler, Wichita, Wilbarger, Winkler, Wise, Wood, Yoakum, and Young within the State of Texas, with the headquarters office located in Dallas, Texas.

(3) *Houston District.* Shall include the Counties of Brazoria, Chambers, Fort Bend, Galveston, Hardin, Harris, Jasper, Jefferson, Liberty, Montgomery, Newton, Orange, Polk, San Jacinto, Trinity, Tyler, and Walker within the State of Texas, with the headquarters office located in Houston, Texas.

3. The Foreign Operations District is abolished and the functions transferred primarily to the newly established Assistant Commissioner (International). This change shall be implemented upon such date as the Commissioner of Internal Revenue may determine. Effective immediately, the Commissioner of Internal Revenue is authorized to effect, at appropriate times and in an orderly manner, such transfers of functions, personnel, positions, equipment and funds as may be necessary to implement the provisions of this order.

4. *Internal Revenue Districts.* Each district established pursuant to Section 7621 of the Internal Revenue Code of 1954, as amended, shall be known as an internal revenue district and shall be identified by the name of the city or subdivision thereof in which the headquarters office of the District of Internal Revenue is located.

5. *District Director of Internal Revenue.* The title of each District office *shall bear the title "District Director* of Internal Revenue" identified by the name of the city or subdivision thereof, in which the headquarters office is located.

6. *U.S. Territories and Insular Possessions.* The Commissioner shall, to the extent of authority otherwise vested in him, provide for the administration of the United States internal revenue laws in the U.S. territories and insular possessions and other authorized areas of the world.

7. *Effect on Prior Treasury Department Orders.* This order supersedes Treasury Department Orders: 150-105, January 24, 1985, and 150-106, February 8, 1985 [1985-31 I.R.B. 24].

JAMES A. BAKER III,
Secretary of the Treasury.

Treasury Department Order 150-02[1]

Organization of the Internal Revenue Service

Dated: February 27, 1986

By the authority vested in me as Secretary of the Treasury by section 1002 of 31 U.S.C.; section 7801(a) and 7803 of the Internal Revenue Code of 1954, as amended; section 321(b) of 31 U.S.C., and Reorganization Plan No. 1 of 1952 as made applicable to the Internal Revenue Code of 1954 by section 7804(a) of such Code and by Executive Order No. 10574 [1954-2 C.B. 732], approved November 5, 1954; and as provided by section 7802(b) of the Internal Revenue Code of 1954, the following offices continue uninterrupted as they existed prior to this order, with the changes noted below:

1. Establishment and Continuation.

a. Office of the Associate Commissioner (Operations)

The Associate Commissioner (Operations) is the principal advisor to the Commissioner on policy matters affecting operations.

(1) The Associate Commissioner (Operations) is responsible for the following activities:

(a) Serves as the spokesperson for the operating functions, which are: Collection of delinquent accounts and securing of delinquent returns; investigation of criminal fraud involving any internal revenue laws (except those concerning alcohol, tobacco, or firearms); examination of tax returns; approval and subsequent examination of Employee Plans and Exempt Organizations. With this order, also provides guidance on tax treaty administration, international compliance, and foreign tax administration assistance.

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[1] Filed by the Office of the Federal Register on March 18, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 19, 1986, 51 F.R. 9573.

(b) Provides policy guidance and direction to the Assistant Commissioner (Collection), Assistant Commissioner (Examination), Assistant Commissioner (Criminal Investigation), Assistant Commissioner (Employee Plans and Exempt Organizations) and, with this order, the Assistant Commissioner (International).

(c) Represents the Service, as designated by the Commissioner, to the Department of the Treasury, Office of Management and Budget, Congress, foreign tax authorities and the public on major cross-functional issues and discusses or explains the Service's policy formulation and long-term plans.

(2) Under the supervision of the Associate Commissioner (Operations) are the following organizations:

(a) Office of the Assistant Commissioner (Collection)

(b) Office of the Assistant Commissioner (Examination)

(c) Office of the Assistant Commissioner (Criminal Investigation)

(d) Office of the Assistant Commissioner (Employee Plans and Exempt Organizations)

(e) Office of the Assistant Commissioner (International), established with this Order.

b. Office of Associate Commissioner (Policy and Management)

The Associate Commissioner (Policy and Management) is the principal advisor to the Commissioner on policy matters affecting agency administration.

(1) The Associate Commissioner (Policy and Management) is responsible for the following activities:

(a) Serves as the spokesperson for the management functions, which are: Personnel administration; financial management; planning; research; training and employee development; management information systems; management of the Service's physical plant, equipment, property, and support services; disclosure and security; tax forms and publication design printing, and distribution; and operation of the IRS Data Center (payroll and non-tax data processing).

(b) Provides policy guidance and direction to the Assistant Commissioner (Support and Services), the Assistant Commissioner (Human Resources), and the Assistant Commissioner (Planning, Finance, and Research).

(c) Represents the Service, as designated by the Commissioner, to the Department of the Treasury, Office of Management and Budget, Congress and the public on major policy and management issues, and discusses or explains the Service's policy formulation and long-term plans.

(2) Under the supervision of the Associate Commissioner (Policy and Management) are the following organizations:

(a) Office of the Assistant Commissioner (Support and Services)

(b) Office of the Assistant Commissioner (Human Resources)

(c) Office of the Assistant Commissioner (Planning, Finance, and Research)

c. Office of Associate Commissioner (Data Processing)

The Associate Commissioner (Data Processing) is the principal advisor to the Commissioner on policy matters affecting data processing.

(1) The Associate Commissioner (Data Processing) is responsible for the following activities:

(a) Serves as the spokesperson for the data processing functions, which are: processing of tax returns and information documents; accounting for all revenues collected by the Service; maintaining master files of all taxpayer accounts; managing all large-scale tax-processing computers in the Service; the tax information program; and, designing, developing, testing, and maintaining computer software used on large-scale tax-processing computers in the Service.

(b) Provides policy guidance and direction to the Assistant Commissioner (Computer Services), the Assistant Commissioner (Returns and Information Processing), and the Assistant Commissioner (Tax System Redesign).

(c) Represents the Service, as designated by the Commissioner, to the Department of the Treasury, Office of Management and Budget, Congress, and the public on major data processing issues, and discusses or explains the Service's policy formulation and long-term plans.

(2) Under the supervision of the Associate Commissioner (Data Processing) are the following organizations:

(a) Office of the Assistant Commissioner (Computer Services)

(b) Office of the Assistant Commissioner (Returns and Information Processing)

(c) Office of the Assistant Commissioner (Tax System Redesign)

d. Office of Assistant to the Commissioner (Legislative Liaison)

The Assistant to the Commissioner (Legislative Liaison) is the principal advisor to the Commissioner, Deputy Commissioner, and top executives of the Service on all Congressional and legislative matters except those involving appropriation hearings, and is responsible for planning, developing, directing, and evaluating the Congressional Affairs program and activities of the Service.

e. The Assistant Commissioner (Inspection) and the Deputy Assistant Commissioner (Inspection)

The Assistant Commissioner (Inspection) and the Deputy Assistant Commissioner (Inspection) will, to ensure objectivity and integrity, continue to report directly to the Commissioner and Deputy Commissioner.

2. The Appeals Division is transferred to the Chief Counsel, and the Commissioner of Internal Revenue will exercise line supervision over the Chief Counsel for this function. The transfer of such personnel, records, equipment and funds will be determined by the Commissioner of Internal Revenue and Chief Counsel, as appropriate.

3. The Corporation Tax and Individual Tax Divisions are transferred to the Chief Counsel, with the authority to supervise and evaluate the work of all officers and employees of the functions transferred. The transfer of such personnel, records, equipment and funds will be determined by the Commissioner of Internal Revenue and Chief Counsel, as appropriate.

4. The Chief Counsel, pursuant to delegated authority from the General Counsel, is authorized to take necessary action on all personnel and administrative matters pertaining to the Office of Chief Counsel, including but not limited to those for the appointment, classification, promotion, demotion, reassignment, transfer or separation of officers or employees; however, all personnel and administrative matters concerning Senior Executive Service or Performance Management Recognition System employees in the Office of Associate Chief Counsel (International) whose primary duties do not involve litigation or in the Office of Associate Chief Counsel (Technical), shall be approved by the Commissioner of Internal Revenue prior to implementation.

5. The Commissioner will exercise the Service's final authority concerning substantive interpretation of the tax laws as reflected in legislative and regulatory proposals, revenue rulings, letter rulings, and technical advice memoranda.

6. The Office of the Commissioner shall consist of the Commissioner, Deputy Commissioner, Assistants to the Commissioner, Assistant to the Commissioner (Public Affairs), Assistant to the Commissioner (Legislative Liaison), Assistant to the Commissioner (Taxpayer Ombudsman), the Assistant to the Commissioner (Equal Opportunity), and the Assistant to the Deputy Commissioner.

7. Except for the specific positions and titles in Sections 1 and 6 of this order, the Commissioner, Internal Revenue Service, may create, abolish, or modify offices and positions within the Internal Revenue Service as may be necessary to effectively and efficiently provide for the administration of tax laws or other responsibilities assigned to the Internal Revenue Service. The authority of the Commissioner, Internal Revenue Service, to create, abolish, or modify offices under this delegation is subject only to limitations that exist by law or Department of the Treasury rules and regulations.

8. The above changes shall be implemented upon such date as the Commissioner of Internal Revenue may determine. Effective immediately, the Commissioner of Internal Revenue is authorized to effect, at appropriate times and in an orderly manner, such transfers of functions, personnel, positions, equipment and funds as may be necessary to implement the provisions of this order.

9. All offices in existence within the Internal Revenue Service but not mentioned in this order are continued without interruption.

10. *Effect on Other Treasury Department Orders.* This order supersedes Treasury Department Order: 150-103, October 3, 1985.

James A. Baker,
Assistant Secretary
of the Treasury.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Disclosure of Return Information to the Bureau of the Census

LR-4-86

SUMMARY: The Internal Revenue Service is proposing amendments to the Regulations on Procedure and Administration to authorize the disclosure of an additional item of return information to the Bureau of the Census for use in statutory statistical programs, to delete the authority to disclose those items of return information which the Bureau no longer needs for such programs, and to delete the authority of the Federal Trade Commission to obtain return information for certain statistical purposes and transfer such authority to the Bureau of the Census. The amendments to the regulations will provide guidance to Internal Revenue Service personnel responsible for disclosure of this information.

DATES: Written comments and requests for a public hearing must be delivered by May 27, 1986. The amendments to the regulations are proposed to be effective as of the date on which the Treasury decision adopting them is published in the FEDERAL REGISTER.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-4-86), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: David E. Dickinson of the Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington, D.C. 20224, Attention: CC:LR:T, (202) 566-6655 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

Under section 6103(j)(1) of the Internal Revenue Code of 1954, upon written request from the Secretary of Commerce, the Internal Revenue Service is to furnish the Bureau of the Census such tax return information as may be prescribed by Treasury regulations for statutorily authorized statistical activities. An itemized description of such return information is currently provided by §301.6103(j)(1)-1 of the Regulations on Procedure and Administration. Similar disclosures to the Federal Trade Commission for a limited statistical purpose are authorized by section 6103(j)(2) of the Code and §301.6103(j)(2)-1 of the regulations.

Further, because employment tax returns and employment tax return information are filed initially with the Social Security Administration rather than the Internal Revenue Service under the combined annual wage reporting system, the regulations also authorize the Social Security Administration to disclose directly to the Census Bureau and FTC certain employment tax return information, subject to statutory restrictions designed to protect the confidentiality of such information.

Periodically, the disclosure regulations are amended to reflect the changing statistical needs of the Census Bureau for tax information, and this notice of proposed rulemaking updates the regulations.

DESCRIPTION OF PROPOSED AMENDMENTS OF REGULATIONS

In properly conducting economic censuses as part of its economic statistics programs, the Census Bureau needs the employer identification number of each affiliated corporation listed on Form 851.

On the other hand, the Census Bureau no longer uses certain information from employment tax returns.

This notice of proposed rulemaking would amend §301.6103(j)(1)-1 of present regulations to add the above item to the list of disclosable tax return information while deleting those employment tax return items no longer required.

Also, because responsibility for preparation of the Quarterly Financial Report has been shifted from the FTC to the Census Bureau, this notice of proposed rulemaking reflects this shift by deleting present regulatory authority to disclose certain corporation tax return information to the FTC and moving it to the Census Bureau.

NON-APPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

REGULATORY FLEXIBILITY ANALYSIS

Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply.

Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably six copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

DRAFTING INFORMATION

The principal author of these proposed regulations is David E. Dickinson of the Office of the Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations both on matters of substance and style.

* * * * *

Proposed amendments to the regulations

The proposed amendments to 26 CFR Part 301 are as follows:

Paragraph 1. The authority for Part 301 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 301.6103(j)(1)-1 also issued under 26 U.S.C. 6103(j).

Par. 2. Section 301.6103(j)(1)-1 is amended by revising paragraph (b)(2)(iii), by revising paragraph (b)(3)(xi) and (xii) and adding a new paragraph (b)(3)(xiii) immediately thereafter, and by revising paragraph, (b)(5) and adding a new paragraph (b)(6) immediately thereafter. The revised and added provisions read as follows:

§301.6103(j)(1)-1 Disclosures of return information to officers and employees of the Department of Commerce for certain statistical purposes and related activities.

* * * * *

(b) *Disclosure of return information to officers and employees of the Bureau of the Census.* * * *

(2) Officers or employees of the Service will disclose to officers and employees of the Bureau of the Census for purposes of, but only to the extent necessary in, conducting, as authorized by chapter 5 of Title 13, United States Code, demographic, economic, and agricultural statistics programs and censuses and related program evaluation—* * *

(iii) From an employment tax return—

(A) Taxpayer identifying number (as described in section 6109) of the employer,

(B) Total compensation reported,

(C) Master file tax account number,

(D) Taxable period covered by such return,

(E) Employment code,

(F) Document locator number,

(G) Record code,

(H) Total number of individuals employed in the taxable period covered by the return,

(I) Total taxable wages paid for purposes of chapter 21, and

(J) Total taxable tip income reported for purposes of chapter 21; and * * *

(3) * * *

(xi) From Form 1065, including Schedule F, if any, total sales of livestock and produce raised and other farm income and gross and net profits from farming;

(xii) From Form 1120S, the names and taxpayer identifying numbers of, and the number of shares of stock owned by, no more than 10 shareholders of the corporation; and

(xiii) From Form 851, the employer identification number of each corporation named on such return.

* * * * *

(5) Subject to the requirements of paragraph (d) of this section and §301.6103(p)(2)(B)-1, officers or employees of the Social Security Administration to whom the following return information has been disclosed as provided by section 6103(l)(1)(A) or (5) may disclose such return information to officers and employees of the Bureau of the Census for necessary purposes described in paragraph (b)(2) or (3) of this section—

(i) From Form SS-4, all information reflected on such return; and

(ii) From Form 1040, Schedule SE—

(A) Taxpayer identifying number of self-employed individual,

(B) Business activities subject to the tax imposed by chapter 21,

(C) Net earnings from farming,

(D) Net earnings from nonfarming activities,

(E) Total net earnings from self-employment, and

(F) Taxable self-employment income for purposes of chapter 2.

(6) (i) Officers or employees of the Service will disclose the following return information (but not including return information described in section 6103(o)(2)) reflected on the return of a corporation with respect to the tax imposed by chapter 1 to officers and employees of the Bureau of the Census for purposes of, but only to the extent necessary in, developing and preparing, as authorized by law, the Quarterly Financial Report—

(A) From the business master files of the Service—

(1) Taxpayer identity information (as defined in section 6103(b)(6)),

(2) Consolidated return and final return indicators,

(3) Principal industrial activity code,

(4) Partial year indicator,

(5) Annual accounting period,

(6) Gross receipts less returns and allowances,

(7) Net income or loss, and

(8) Total assets; and

(B) From Form SS-4—

(1) Month and year in which such return was executed,

(2) Taxpayer identity information,

(3) Principal industrial activity, geographic, firm size, and reason for application codes.

(ii) Subject to the requirements of paragraph (d) of this section and §301.6103(p)(2)(B)-1, officers or employees of the Social Security Administration to whom return information described in paragraph (b)(6)(i)(B) of this section with respect to a corporation has been disclosed as provided by section 6103(l)(1)(A) may disclose such return information to officers and employees of the Bureau of the Census for a purpose described in this paragraph (b)(6).

* * * * *

Par. 3. Section 301.6103(j)(2)-1 is removed.

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Filed by the Office of the Federal Register on March 27, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 28, 1986, 51 F.R 10635)

Election Under Section 463 Regarding Vested Accrued Vacation Pay

Announcement 86-59

Section 91(i) of the Tax Reform Act of 1984, 1983-1 (Vol. 1) C.B. 117, provides a transitional rule for an election under section 463 of the Internal Revenue Code, relating to the accrual of vacation pay. Only taxpayers to whom a deduction was allowable (other than under section 463) for vested accrued vacation pay for the last taxable year ending on or before July 18, 1984, are eligible to use the section 91(i) transitional rule.

Generally, taxpayers who make an election to accrue vacation pay under section 463 must compute the opening balances in their accrual and suspense accounts under section 463(b). However, eligible taxpayers who make an election under section 463 for the first taxable year ending after July 18, 1984, must compute the opening balance in their accrual and suspense accounts under a special rule provided in section 91(i).

The Internal Revenue Service published temporary regulations on February 4, 1986, that explain how eligible taxpayers make an election under section 463 for their first taxable year ending after July 18, 1984 (51 FR 4329). The regulations also provide guidance on the computation of opening balances in accrual and suspense accounts under the special transitional rule.

This announcement concerns eligible taxpayers who on an income tax return filed on or before May 5, 1986, for the first taxable year ending after July 18, 1984, deducted vested accrued vacation pay under section 463 and computed the opening balances in their accrual and suspense accounts using the section 91(i) transitional rule but who did not make the section 463 election in the manner prescribed by section 1.463-1T(e) of the Temporary Income Tax Regulations. These taxpayers are considered to have elected to accrue vacation pay under section 463, and thus are subject to the section 91(i) transitional rule, if they attached a statement to their income tax return filed for the first taxable year ending after July 18, 1984, clearly indicating their intention to elect to accrue vacation pay under section 463. For example, an eligible taxpayer who made an election consistent with section 10.2 of the Temporary Income Tax Regulations is considered to have elected under section 463 and thus is subject to the section 91(i) transitional rule. Taxpayers must also retain in their books and records all of the information specified by section 1.463-1T(e) of the regulations so that the Service may, upon examination, obtain all of the information necessary to verify the correctness of the taxpayer's deduction.

Eligible taxpayers who attempt after May 5, 1986, to make a section 463 election under the section 91(i) transitional rule may not take advantage of the relief in this announcement but must fully comply with the provisions of section 1.463-1T of the temporary regulations.

Employee Plans Not Timely Amended—7805(b) Relief

Announcement 86-60

In News Release IR-85-89, dated August 30, 1985, the Internal Revenue Service announced an extension, until Nov. 1, 1985, of the time for compliance with the requirements of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), the Tax Reform Act of 1984 (TRA), and the Retirement Equity Act of 1984 (REA), applicable to pension, profit-sharing, stock bonus, and annuity plans. The extension applied to all such plans whose compliance date was before Nov. 1, 1985.

Notice 86-3, 1986-9 I.R.B. 21, described procedures established by the Service for granting partial relief from the sanctions for failure to satisfy the requirements of section 401(a) of the Internal Revenue Code in the case of certain employee plans that were not timely amended to comply with TEFRA, TRA or REA. In the absence of this relief, the applicable sanctions would include the disallowance of the current deduction for employer contributions, the inclusion of such contributions in employees' current income, the loss of the tax-exempt status of the plans' trusts, the loss of favorable tax treatment of distributions from plans, and, in the case of certain employee stock ownership plans, the disallowance of the applicable tax credits. Under Notice 86-3 the extent of the relief from sanctions with respect to (1) deductions or credits for employer contributions was determined by reference to the amount of time that had elapsed between the applicable compliance date and the time of filing a request for a determination letter, and (2) the inclusion of employer contributions in employees' current income and the tax treatment of plan distributions was determined in part by an employee's relative ownership interest in the employer and status as a key employee. Also, under Notice 86-3 the tax-exempt status of the trust was preserved.

This announcement revises Notice 86-3 to (1) provide that, for all plans to which Notice 86-3 applies and whose applicable compliance date is before June 30, 1986, the applicable compliance date is now June 30, 1986; (2) extend the compliance date for certain master or prototype plans as described in the following paragraph; (3) provide for a straight 10-percent-per-month reduction in the number-of-months factor after the applicable compliance date has passed; (4) include additional provisions describing the scope of relief applicable with respect to tax credit employee stock ownership plans that, if they had continued to meet the requirements of section 409 of the Code, would have entitled the employers to the credit provided for in section 41; and (5) correct a printing error.

This announcement extends the compliance date for most master or prototype plans adopted by employers after March 19, 1984, by extending section 12 of Rev. Proc. 84-23, 1984-1 C.B. 457, to those plans.

This is the last extension of compliance dates for TEFRA, TRA and REA, and there will be no further liberalization of the relief provided by Notice 86-3 as herein revised. The absence of a request for a determination letter for a plan with respect to TEFRA, TRA or REA (including a submission in accordance with Notice 86-3 as herein revised) may increase the potential for an examination of the plan by the Service.

The revision of Notice 86-3 will be accomplished by:

1. Replacing, in the first paragraph under *Eligibility*, the connective "and" with "or," immediately before "(3)".

2. Replacing in the second paragraph under *Eligibility*, the last five sentences with:

The compliance date for an individually designed plan (or a master or prototype plan for which continued reliance is not granted pursuant to section 12 of Rev. Proc. 84-23, 1984-1 C.B. 457, or which was adopted after March 19, 1984, and for which the extended compliance date permitted below in this paragraph does not apply) is the last day of the plan year in which the qualification requirement becomes effective for that plan, except that, in the case of a "disqualifying provision" as defined in section 1.401(b)-1(b) of the Income Tax Regulations (which does not apply to changes in qualification requirements due to TRA or REA), the compliance date is the last day of the remedial amendment period as defined in section 1.401(b)-1(c). See Notice 85-5, 1985-1 C.B. 427; Notice 85-14, 1985-33 I.R.B. 16, and Announcement 85-128, 1985-35 I.R.B. 44. The compliance date for a master or prototype plan adopted by an employer on or before March 19, 1984, to which the relief described in these procedures applies, is determined in accordance with section 12 of Rev. Proc. 84-23. The compliance date for a master or prototype plan adopted by an employer after March 19, 1984, will be determined under section 12 of Rev. Proc. 84-23 provided the following conditions are satisfied. The conditions are (1) the sponsor of the master or prototype plan requested an opinion letter in accordance with Rev. Proc. 84-23 on such plan (or a plan that replaced such plan) no later than December 31, 1984, and (2) such plan is first adopted by the employer no later than the last day of the twelfth month after either the Service issued an opinion letter with respect to the master or prototype plan, or the application for an opinion letter with respect to the plan was withdrawn. This notice extends until June 30, 1986, the time for complying with the requirements of TEFRA, TRA and REA applicable to pension, profit-sharing, stock bonus and annuity plans. This extension of time applies to plans with compliance dates before June 30, 1986.

3. Replacing, in the first paragraph under *Conditions for Granting Relief*, the last sentence with:

To take advantage of this procedure, the plan administrator must make the necessary amendments and request a determination letter with respect thereto no later than the last day of the ninth month beginning after the applicable compliance date.

4. Replacing the table under *Scope of Relief* with:

NUMBER-OF-MONTHS-FACTOR (%)

Number of months that have begun after the compliance date and on or before the date of submission

1	2	3	4	5	6	7	8	9
90	80	70	60	50	40	30	20	10

5. Replacing, in *Example (1)*, "Nov. 1, 1985" with "June 30, 1986"; "TEFRA" with "TEFRA, TRA or REA"; "Jan." with "July"; and "two months have ended" with "one month began".

6. Replacing, in *Example (2)*, Jan." with "July"; "Nov. 9, 1986" with "March 9, 1987"; and "nine months have ended" with "eight months began".

7. Adding, at the end of the notice, the following provisions:

PROVISIONS FOR TCESOPS

The following provisions are applicable in the case of a tax credit employee stock ownership plan (TCESOP) of a corporation which would have been eligible for the employee stock ownership credit under section 41 of the Code or former section 48(n) but for the fact that the plan failed to meet the requirements of section 409 as a result of not being timely amended to comply with TEFRA, TRA or REA.

Scope of Relief—With respect to the employer contributions made for a taxable year which ends within or with a taxable year of the plan's trust for which the trust is not exempt under section 501(a) of the Code because of a failure to comply with TEFRA, TRA or REA, the allowable tax credit for that taxable year of the employer or any other taxable year on account of such contributions will be equal to the following amount: the product of the number-of-months factor described above multiplied by the lesser of (a) the amount contributed by the employer, or (b) the limitation under section 41 or former section 48(n) that would apply if the plan met the requirements of section 409. To the extent the tax credit is reduced by application of the preceding sentence, such contributions are treated as contributions for which no credit under section 41 or former section 48(n) had ever been elected, and such contributions are deductible in accordance with section 404(a)(5). The amount includible in the key employees' respective gross incomes will be determined in the same manner as described above as though the employer were a tax-exempt organization.

Instructions to Taxpayers—The same requirements must be satisfied as described above except that references to deductions are deemed to refer also to the tax credit allowed under these procedures.

This revision will be reflected in Notice 86-3 when the notice is reprinted in the Cumulative Bulletin.

Information Returns Relating to Sales or Exchanges of Certain Partnership Interests—Public Hearing

Announcement 86-61[1]

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to information returns, statements, and notifications required where there is a sale or exchange of certain partnership interests.

DATES: The public hearing will be held on Thursday, June 12, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Thursday, May 29, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, ATTN: CC:LR:T (LR-236-84), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935, not a toll-free call.

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under section 6050K of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Monday, December 23, 1985 (50 FR 52332) [LR-236-84, 1986-7 I.R.B. 26].

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Thursday, May 29, 1986, an outline of oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

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[1] Filed by the Office of the Federal Register on April 9, 1986, 8:45 a.m., and published in the issue of the Federal Register for April 10, 1986, 51 F.R. 12340.

Recapture of Overall Foreign Losses—Public Hearing

Announcement 86-62[1]

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to the recapture of overall foreign losses.

DATES: The public hearing will be held on Thursday, June 5, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Thursday, May 22, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, Attn: CC:LR:T (LR-3-77), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Fay Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935 (not a toll-free call).

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under section 904(f) of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Friday, January 24, 1986 (51 FR 3193) [LR-3-77, 1986-10 I.R.B. 14].

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Thursday, May 22, 1986, an outline of oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

Increase in Excise Tax on Coal

Announcement 86-63

The Consolidated Omnibus Budget Reconciliation Act of 1985, Public Law 99-272, has increased the manufacturers excise tax rate on coal. The tax is imposed on domestically mined coal (other than lignite) sold or used by the producer. Effective April 1, 1986, the tax rate is the lesser of (1) $1.10 per ton for coal from underground mines and 55 cents per ton for coal from surface mines, or (2) 4.4 percent of the price for which the coal is sold.

Affected taxpayers should start reporting and paying tax at the new rate on Form 720, Quarterly Federal Excise Return, for the quarter ending June 30, 1986.

The coal tax revenues are appropriated for the Black Lung Disability Trust Fund. The trust fund pays black lung disability benefits to coal miners or their survivors.

Revision of Form 2032, Contract Coverage Under Title II of the Social Security Act

Announcement 86-64

Form 2032, Contract Coverage Under Title II of the Social Security Act, which is used to enter into the agreement specified in section 3121(l) of the Internal Revenue Code to extend coverage under the Social Security Act to U.S. citizens and resident aliens employed abroad by foreign affiliates, has been revised.

The December 1985 revision now permits employers to elect to have the social security rules that became effective after April 20, 1983, apply to agreements in effect on that date. By making this election, employers with preexisting agreements can extend social security coverage to U.S. resident aliens, as well as to U.S. citizens, employed by certain foreign affiliates.

The revised form is now available in Internal Revenue Service distribution centers.

Accrual of Income by Utilities

Announcement 86-65

Introduction

The Internal Revenue Service will not follow the Tax Court's recent decision in *Orange and Rockland Utilities, Inc. v. Commissioner*, 86 T.C. ___ (1986), and its earlier decision in *Public service Co. of New Hampshire v. Commissioner*, 78 T.C. 445 (1982). Furthermore, the Service is studying the possibility of revoking Rev. Rul. 72-114, 1972-1 C.B. 124, effective for tax years beginning on or after the publication of this announcement in the Internal Revenue Bulletin.

The Tax Court's decision in *Orange and Rockland* was filed on February 18 of this year. It held that a group of natural gas and electric utilities which used the accrual method of accounting were not required currently to accrue income from product deliveries occurring between each customer's December meter reading date, or meter estimation date, and the end of the calendar year. Instead, the utilities were permitted to defer accrual of that income until the first meter reading date or estimation date in the succeeding calendar year. In 1982, the Tax Court rendered a similar decision in *Public Service Co. of New Hampshire v. Commissioner*. The Tax Court reached these results even though in both cases (1) the utilities had performed, before the end of the current calendar year, all acts necessary to earn the income in question, (2) the income could be accurately estimated, (3) the utilities accrued and reported the income on their current year financial statements, which were used for reporting operating results to shareholders and the financial community, and (4) the utilities took current year federal income tax deductions for all expenses associated with earning the income.

The Tax Court's *Orange and Rockland* decision was based principally on the following conclusions:

(1) Delivery of electricity and natural gas is the furnishing of a service rather

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[1] Filed by the Office of the Federal Register on April 1, 1986, 8:45 a.m., and published in the issue of the Federal Register for April 2, 1986, 51 F.R. 11323.

than the sale of a good or product;

(2) Income tax accrual accounting rules applicable to service transactions allowed the *Orange and Rockland* utilities to defer accrual of the year-end income in question until the first meter reading date or meter expiration date of the next year;

(3) Since Rev. Rul. 72-114 would have permitted such deferral by the *Orange and Rockland* Utilities if their nontax financial statements had been prepared on a conforming basis, deferral should be allowed regardless of the utilities' nonconforming financial statements because such nonconformity is not an adequate ground for distinguishing between taxpayers. In the opinion of the Internal Revenue Service, the *Orange and Rockland* decision misapplied well-settled rules of income tax accrual accounting and improperly rejected the accounting conformity requirement contained in Revenue Ruling 72-114.

Accrual Accounting

The furnishing of electricity and natural gas constitutes the sale of a product or good rather than the sale of services. Thus, natural gas utilities are required to employ in inventory method of accounting for their gas, Rev. Rul. 78-352, 1978-2 C.B. 168; and gas and electric utilities may defer the reporting of prepaid income upon compliance with regulations governing prepayment for sales of goods. *City Gas Co. of Fla. v. Commissioner*, 47 T.C.M. 971, 975-78 (1984); Rev. Rul. 72-114, 1972-1 C.B. 124. Therefore, the utilities involved in the *Orange and Rockland* case were required to accrue income in accordance with rules applicable to sellers of goods.

The Income Tax Regulations provide that sellers of goods must accrue income "when all the events have occurred which fix the right to receive such income and the amount thereof can be determined with reasonable accuracy." Section 1.446-1(c)(1)((ii)) of the regulations. The income of the *Orange and Rockland* utilities attributable to gas and electricity delivered between the last December meter reading date, or meter estimation date, and the calendar year end could be estimated with reasonable accuracy and accountants for the utilities so certified. Thus, under the regulations quoted above, this income should have been currently accrued for tax purposes if compliance with the "all events" requirement occurred before year end.

The "all events" requirement is satisfied with respect to income when payment is due, when payment is received, or when the income is earned, whichever occurs first. *Schlude v. Commissioner*, 372 U.S. 128 (1963); Rev. Rul. 79-195, 1979-1 C.B. 177, 178. A corollary of this rule is that the "all events" requirement is satisfied no later than the time when income is earned by performance, regardless of when billing is permitted. Section 1.446-1(c)(1)(ii) of the regulations; *Bentley Laboratories, Inc. v. Commissioner*, 77 T.C. 152, 165 (1981); *Western Oaks Building Corp. v. Commissioner*, 49 T.C. 365, 371-72 (1968), *nonacq.*, 1968-2 C.B. 3. Furthermore, even if the utilities in *Orange and Rockland* were considered to be furnishing services instead of goods, there would be no difference in the outcome, because the governing rule for service providers also requires accrual of reasonably estimatable income no later than the time when the income is earned, irrespective of the time when billing is permitted. *Georgia School-Book Depository, Inc. v. Commissioner*, 1 T.C. 463 (1943); Rev. Rul. 74-372, 1974-2 C.B. 147. The date when billing occurs, or is permitted, is relevant in determining whether a right to income is fixed only in cases where the income has not yet been earned through the performance of services or delivery of goods. *See Schlude v. Commissioner*, 372 U.S. 128 (1963); *Cox v. Commissioner*, 43 T.C. 448, 454-58 (1965), *Acq.*, 1965-2 C.B. 4, *nonacq.*, 1965-2 C.B. 7. *Orange and Rockland* was not such a case.

Since the customers of the utilities in *Orange and Rockland* would be required to pay for all gas and electricity delivered through the end of December regardless of when billing was permitted or occurred, the utilities earned the income attributable to that gas and electricity at time of delivery. *See City Gas Co. of Fla. v. Commissioner*, 47 T.C.M. 971, 976 (1984). Consequently, the utilities should have currently accrued all income attributable to gas and electricity deliveries between the last December meter reading date, or meter estimation date, and the end of the calendar year even though state regulatory rules did not allow the customers to be billed until the first meter reading or meter estimation date in the following year. *Bay State Gas Co. v. Commissioner*, 689 F.2d 1, 5 (1st Cir. 1982).

Hybrid Accounting

The utilities in *Orange and Rockland* did not report income at the time required by accrual rules but did deduct expenses under those rules. Thus the accounting method used by the utilities to report their income and deductions was a "hybrid" of tax accounting principles. This particular hybrid is commonly referred to as the "cycle meter reading" method of accounting.

Hybrid tax accounting methods, such as the cycle meter reading method, are not permitted unless they comply with Regulations prescribed under authority granted by section 446(c)(4) of the Internal Revenue Code. To prevent income distortion, the regulations under Internal Revenue Code section 446(c)(4) state that a taxpayer who employs the accrual method of accounting in deducting costs and expenses, as the utilities did in *Orange and Rockland*, must also employ the accrual method in computing income, which those utilities failed to do. Section 1.446-1(c)(1)(iv)(a) of the regulations. *See also Massachusetts Mutual Life Co. v. Commissioner*, 288 U.S. 269, 273-74 (1933). Thus, the hybrid cycle meter reading accounting method of the *Orange and Rockland* utilities would ordinarily not be permissible under the income tax law. *See Connors, Inc. v. Commissioner*, 71 T.C. 913 (1979).

The Revenue Ruling 72-114 Conformity Requirement

Section 1.446-1(c)(2)(ii) of the regulations authorizes the Commissioner to allow a taxpayer's continued employment of an otherwise impermissible accounting method if the method is "consistently used by the taxpayer" and if, *"in the opinion of the Commissioner,* income is clearly reflected by the use of such method." *See Pierce Ditching Co., Inc. v. Commissioner*, 73 T.C. 301 (1979). So long as the Commissioner does not act arbitrarily, his opinion is determinative of whether a particular accounting method clearly reflects income. *Bangor Punta Opera-*

tions, Inc. v. United States, 466 F.2d 930, 935 (7th Cir. 1972).

Pursuant to section 1.446-1(c)(2)(ii) of the regulations, the Commissioner issued Rev. Rul. 72-114, which permits a utility to use the otherwise unacceptable cycle meter reading method if the utility prepares its financial accounting statements on a conforming basis. The Commissioner granted this permission for three reasons. First, the cycle meter reading method had been extensively used in the utility industry's financial statements for many years and requiring the entire industry to adopt a different method for tax purposes would have imposed substantial costs and inconvenience. Second, the industry then had stable year-to-year costs and revenues so that the cycle meter reading method produced little distortion on an industry-wide basis. Third, the cycle meter reading method is theoretically incorrect under generally accepted accounting principles and, therefore, cannot be used for financial accounting purposes if it materially distorts income when compared with results under a strict accrual method. Consequently, a given utility's independent auditors will require the utility to prepare financial statements under accrual principles, rather than under the cycle meter reading method, whenever the cycle meter reading method produces income distortion in excess of the level tolerated by the materiality standard. *See* Accounting Principles Board Statement No. 4, Basic Concepts and Accounting Principles Underlying Financial Statements of Business Enterprises, Chapter 6 (Oct. 1970); Financial Accounting Standards Board, Statement of Financial Accounting Concepts No. 2, Qualitative Characteristics of Accounting Information (May 1980). Thus, as long as a given utility's financial accounting statements conform to its use of the cycle meter reading method in preparing its income tax returns, the Commissioner can be certain that the utility's independent auditors do not view the cycle meter reading method as materially distorting income. While the Service does not accept the accounting profession's materiality standard as the government measure of clear reflection of income for tax purposes, *see All-Steel Equipment, Inc. v. Commissioner*, 54 T.C. 1749, 1751-52 (1970), *Acq. in result*, 1978-2 C.B. 1, *nonacq.*, 1978-2 C.B. 3, *rev'd on other grounds*, 467 F.2d 1184 (7th Cir. 1972), reliance on that standard operates as a check against the extreme income distortion that might otherwise occur in individual cases under the cycle meter reading method.

Obviously, the conformity requirement is crucial to the Commissioner's grant of permission in Revenue Ruling 72-114 to employ an otherwise objectionable accounting method. It allows the Commissioner to rely on independent auditors to verify that no "material" distortion of income, as defined by the accounting profession's materiality standard, results from use of the cycle meter reading method in individual cases. However, when a utility ceases to conform its financial statements to its tax return use of the cycle meter reading method, the Commissioner's ability to rely on the limited protection afforded by the auditor's policing function is lost. The Commissioner must then either withdraw permission to use the method or make periodic case-by-case determinations of whether the method produces a material distortion of income. Since a case-by-case approach would represent a disproportionate and inappropriate use of the Commissioner's audit resources and since the cycle meter reading method is prima facie unacceptable for income tax purposes, Rev. Rul. 72-114 provides that use of the method is contingent on compliance with the conformity requirement. This position is clearly a reasonable exercise of administrative discretion and is also consistent with the holding in *All-Steel Equipment, Inc. v. Commissioner*, 54 T.C. 1749, 1751-58 (1970), *Acq. in result*, 1978-2 C.B. 1, *nonacq.*, 1978-2 C.B. 3, *rev'd on other grounds*, 467 F.2d 1184 (7th Cir. 1972), that a method of accounting which distorts income, as the cycle meter reading method does, is not rendered acceptable for tax purposes by the fact that the distortion is immaterial under financial accounting criteria.

The Orange and Rockland and Public Service Co. of New Hampshire Cases

For reasons given above, the *Orange and Rockland* and *Public Service Co. of New Hampshire* decisions improperly allowed non-conforming utilities to continue using the cycle meter reading method. Accordingly, the Internal Revenue Service will follow neither case.

Revocation of Revenue Ruling 72-114

In 1972, when Rev. Rul. 72-114 was promulgated, the cycle meter reading method was employed by the overwhelming majority of gas and electric utilities in preparing their financial accounting statements. Furthermore, the utility industry was then experiencing stable costs, prices and volumes with the result that costs and revenues were consistent from year-to-year. In these circumstances, use of the cycle meter reading method for tax purposes produced little industry-wide income distortion; and the conformity requirement of Rev. Rul. 72-114 served as a check against material distortions in individual cases. Therefore, the Commissioner made the administrative judgment that it was appropriate to permit utilities to employ the cycle meter reading method for income tax purposes rather than require an entire industry to bear the expense and inconvenience of using an accounting method for income tax purposes that differed from the industry-wide financial accounting method.

The facts which the Commissioner relied on in 1972 have changed substantially. For several years, the utility industry has not had stable year-to-year revenues and costs. As a result, the cycle meter reading method now produces significant, wide-spread income distortions. Furthermore a sizeable and increasing segment of the industry has discontinued use of the cycle meter reading method for financial accounting purposes. Therefore, the Internal Revenue Service is studying the propriety of revoking Rev. Rul. 72-114, effective for tax years beginning on or after the publication of this announcement in the Internal Revenue Bulletin.

Revision of Form 4789, Currency Transaction Report

Announcement 86-66[1]

A revised Form 4789, (December 1985 revision) Currency Transaction Report, for reporting cash transactions of more than $10,000, will become effective on July 1, 1986.

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[1] Based on News Release IR-86-53, dated April 28, 1986.

Until then, financial institutions should continue to use the present Form 4789 but may now order the revised version from Internal Revenue Service Forms Distribution Centers.

These forms should be filed with the Detroit Data Center, P.O. Box 42621, Detroit, MI 48232, Attn: CTR. As of July 1, 1986, all prior forms should be destroyed.

Any institutions wishing to print their own Forms 4789 may obtain reproduction proofs by writing the Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attn: Reproduction Coordinator, PM:S:FM:P:D.

Change in Reporting Distributions of Excess Contributions Made to IRAs

Announcement 86-67

Section 408(d)(4) of the Internal Revenue Code provides that if excess contributions made to an individual retirement account (IRA) plus earnings on such excess are distributed to the participant before the due date of his or her return (including extensions), the earnings are taxable to the participant in the year the excess contributions were made.

The instructions for Form 5498, Individual Retirement Arrangement Information, currently advise financial institutions and other trustees and issuers of IRAs to report these distributions on Form W-2P,, Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments; or on Form 1099-R, Statement for Recipients of Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc., for the year in which the contribution was made.

The Service realizes that it is very difficult for many financial institutions and other trustees and issuers to use a prior year form to report the distribution, made after the close of the year, of earnings attributable to excess contributions that were made in the prior year. Therefore, to ease the burden imposed on these filers, the Service has established a procedure, effective immediately, to permit the reporting of these distributions on a current year Form W-2P or 1099-R. To indicate that the earnings distributed are taxable in the prior year, the filer should enter code "P" in the distribution category box of the appropriate form (Box 14 of Form W-2P or Box 7 of Form 1099-R) if the excess contribution was made in the year just prior to the year of distribution. This code will be added to the list of distribution codes when the instructions for Forms W-2P and 1099-R are revised for 1987. Filers should continue to use code 8 to indicate that the earnings are taxable in the current year if the excess contribution was made and withdrawn in the same year.

This new code will also be added to the magnetic media revenue procedures being developed by the Service for 1986.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Louis Crown	Bayside, NY	Certified Public Accountant	Indefinite from March 14, 1986
David H. Heilman	Council Grove, KS	Attorney	Indefinite from March 14, 1986
Beryl W. Markwell	Elmhurst, IL	Certified Public Accountant	Twenty-four Months from March 20, 1986
Marc Pozner	Tenafly, NJ	Certified Public Accountant	Indefinite from March 14, 1986
A. Russel Lucid	Norwell, MA	Attorney	Indefinite from March 26, 1986
Gary E. Borushko	Grosse Pointe Wood, MI	Certified Public Accountant	Indefinite from April 7, 1986
Paul Skulsky	Spring Valley, NY	Certified Public Accountant	Indefinite from April 1, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before their Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Thomas G. Abernethy, Jr.	Jackson, MS	Attorney	March 7, 1986
Thomas H. Foxhill, Jr.	Pemberton, NJ	Enrolled Agent	April 12, 1986
Peter Parker	Baltimore, MD	Attorney	April 12, 1986

Announcement of the Suspension, Termination, or Consent to Voluntary Suspension or Termination of Enrollment to Perform Actuarial Services Under the Employee Retirement Income Security Act of 1974

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to indentify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
Robert E. Nemann	Cincinnati, OH	For three months effective April 9, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.61-6(c)(3), 1.163-4, 1.451-1(d), 1.451-2(b), 1.454-1(a)(1)(i), 1.482-2(a), 1.482-2(c)(2), 1.483-1, 1.483-2, 1.1016-5(s), 1.1232-2, 25.2512-4, 25.2512-8, revised; 1.163-7, 1.446-2, 1.483-3 through 1.483-5, 1.1271-1 through 1.1275-5, added; 1.61-7(d), 1.249-1, 1.409-1(b)(1), 1.528-1(d), 1.582-1(e)(3)(i), 1.636-1(a)(1)(ii), 1.818-3(f), 1.861-2(a)(4), 1.993-1(g), 1.1001-1(g), 1.1012-1(f), 1.1037-1, 1.1232-1, 1.1232-3A, 1.6045-1(c), 1.6049-5, 1.6049-6(d), 1.9006-1(c)(1)(vii), 3.2(d), 3.3(b), 5f.163-1(f), 6a.103A-2(i)(2)(vi)(B), 514.23, amended; 1.1012-2, removed and new added; 1.7872-4(e), reproposed and revised.	Original issue discount rules, imputed interest rules, and safe haven interest rates	1986-18 I.R.B. 4	June 9, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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8067, 1986-6 I.R.B. **5**
8068, 1986-8 I.R.B. **9**
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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

Finding List of Current Action on Previously Published Rulings[1]

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*Denotes entry since last publication

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74-48
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Rev. Rul. 86-37, 1986-10 I.R.B. 5

74-49
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Rev. Rul. 86-37, 1986-10 I.R.B. 5

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80-42
Superseded by
86-19, 1986-14 I.R.B. 10

81-52
Superseded by
86-16, 1986-12, I.R.B. 13

81-62
Superseded by
86-18, 1986-13 I.R.B. 40

82-32
Obsoleted by
86-20, 1986 15 I.R.B. 50

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Modified by
86-17, 1986-13 I.R.B. 40

84-36
Modified by
86-17, 1986-13 I.R.B. 40

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Modified by
86-17, 1986-13 I.R.B. 40

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86-13, 1986-10, I.R.B. 7

84-81
Superseded by
86-7, 1986-6 I.R.B. 28

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Superseded by
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85-2
Superseded by
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85-34
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86-3, 1986-1 I.R.B. 26

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86-3, 1986-1 I.R.B. 26

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86-37, 1986-10 I.R.B. 5

54-415
Obsoleted by
86-37, 1986-10 I.R.B. 5

55-650
Obsoleted by
86-37, 1986-10 I.R.B. 5

55-651
Obsoleted by
86-37, 1986-10 I.R.B. 5

56-557
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86-4, 1986-2 I.R.B. 5

58-114
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86-37, 1986-10 I.R.B. 5

58-522
Obsoleted by
86-37, 1986-10 I.R.B. 5

58-610
Obsoleted by
86-44, 1986-13 I.R.B. 39

58-577
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86-10, 1986-4 I.R.B. 7

63-41
Obsoleted by
86-37, 1986-10 I.R.B. 5

63-42
Obsoleted by
86-37, 1986-10 I.R.B. 5

63-43
Obsoleted by
86-37, 1986-10 I.R.B. 5

64-138
Revoked by
86-58, 1986-16 I.R.B. 7

66-215
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86-15, 1986-6 I.R.B. 4

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68-231
Obsoleted by
86-44, 1986-13 I.R.B. 39

68-257
Obsoleted by
86-37, 1986-10 I.R.B. 5

68-588
Obsoleted by
86-37, 1986-10 I.R.B. 5

68-613
Obsoleted by
86-37, 1986-10 I.R.B. 5

68-614
Obsoleted by
86-37, 1986-10 I.R.B. 5

68-615
Obsoleted by
86-37, 1986-10 I.R.B. 5

68-627
Obsoleted by
86-37, 1986-10 I.R.B. 5

68-628
Obsoleted by
86-37, 1986-10 I.R.B. 5

71-259
Obsoleted by
86-37, 1986-10 I.R.B. 5

72-188
Modified by
86-54, 1986-15 I.R.B. 44

72-198
Obsoleted by
86-9, 1986-4 I.R.B. 6

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Obsoleted by
86-37, 1986-10 I.R.B. 5

72-482
Obsoleted by
86-37, 1986-10 I.R.B. 5

73-132
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86-37, 1986-10 I.R.B. 5

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Obsoleted by
86-37, 1986-10 I.R.B. 5

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86-36, 1986-10 I.R.B. 4

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86-12, 1986-5 I.R.B. 32

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74-179
Obsoleted by
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86-37, 1986-10 I.R.B. 5

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[1] See footnote at end of list.

Finding List of Current Action on Previously Published Rulings[1]—Continued

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77-90
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77-178
Obsoleted by
86-37, 1986-10 I.R.B. **5**

78-76
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86-9, 1986-4 I.R.B. **6**

80-8
Amplified by
86-57, 1986-16 I.R.B. **4**

80-134
Obsoleted by
86-9, 1986-4 I.R.B. **6**

81-86
Revoked after 6/30/85 by
86-62, 1986-17 I.R.B. **12**

81-212
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86-47, 1986-14 I.R.B. **4**

82-47
Amplified by
86-45, 1986-13 I.R.B. **36**

84-80
Amplified by
86-30, 1986-8 I.R.B. **24**

84-132
Clarified, Distinguished, &
Superseded by
86-63, 1986-17 I.R.B. **6**

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

NOTES

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1937-1	*14.00*
1937-2	8.50
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1938-2	*14.00*
1939-1-1	9.50
1939-1-2	12.00
1939-2	10.00
1940-1	6.50
1940-2	15.00
1941-1	8.00
1941-2	*4.00*
1942-1	8.00
1942-2	*6.50*
1943-(*)	*11.00*
1944-(*)	*9.00*
1945-(*)	10.00
1946-1	*3.00*
1946-2	6.00
1947-1	*2.00*
1947-2	3.75
1948-1	*3.50*
1948-2	8.50
1949-1	*8.00*
1949-2	*3.25*
1950-1	7.00
1950-2	*5.50*
1951-1	*13.00*
1951-2	*6.00*
1952-1	*3.00*
1952-2	8.00
1953-1	*4.75*
1953-2	13.00
1954-1	13.00
1954-2	13.00
1955-1	11.00
1955-2	14.00
1956-1	17.00
1956-2	20.00
1957-1	18.00
1957-2	(**)
1958-1	11.00
1958-2	(**)
1958-3	17.00
1959-1	19.00
1959-2	11.00
1960-1	21.00
1960-2	13.00
1961-1	15.00
1961-2	11.00
1962-1	15.00
1962-2	14.00
1962-3	22.00
1963-1	10.00
1963-2	12.00
1964-1-1	11.00
1964-1-2	12.00
1964-2	28.00
1965-1	19.00
1965-2	13.00
1966-1	15.00
1966-2	15.00
1967-1	11.00
1967-2	17.00
1968-1	15.00
1968-2	13.00
1969-1	15.00
1969-2	7.50
1969-3	14.00
1970-1	12.00
1970-2	(**)
1971-1	12.00
1971-2	17.00
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1972-2	15.00
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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-69, page 4.
Qualified tuition reductions. Amounts excludable from gross income as a qualified tuition reduction under section 117(d)(1) are not subject to the $5,000 limitation of section 127(a)(2).

Rev. Rul. 86-70, page 4.
Carryover; disallowed interest. A carryover of disallowed interest is not available to the extent it exceeds taxable income for the taxable year in which it was paid or accrued.

Rev. Rul. 86-71, page 5.
Deductions; fee for preparation of F.C.C. license application. An amount paid for the preparation of an F.C.C. application for a license to operate a radio system is a capital expenditure and not deductible as an expense under section 212 of the Code. If the application is denied, the fee paid may be deductible at some future date as a loss under section 165.

Rev. Rul. 86-72, page 6.
Installment obligation; cancelled on death of payee. Gain is recognized by the estate of a payee of an installment obligation that is cancelled because of the death of the payee.

Rev. Rul. 86-73, page 7.
Partnerships; termination on sale of interests; effect of section 754 election of deemed distribution to incoming partner. A section 754 election in effect upon the sale of a 50 percent interest in partnership capital and profits applies to the interest of the incoming partner for purposes of determining adjusted basis upon the deemed distribution of partnership assets following a termination under section 708(b)(1)(B).

EMPLOYEE PLANS

Rev. Rul. 86-78, page 11.
Individual retirement arrangements; disclosure. If values under an individual retirement arrangement (IRA) are guaranteed or can be projected, the trustee or issuer must in certain instances disclose to an IRA purchaser the amounts guaranteed or projected to be withdrawable.

EXEMPT ORGANIZATIONS

Rev. Proc. 86-23, page 17.
Information returns; church-affiliated organizations. Certain church-affiliated organizations that are internally supported are relieved from filing annual information returns. Rev. Rul. 83-23 supplemented and Notice 84-2 superseded.

Announcement 86-68, page 36.
A list is given of organizations now classified as private foundations.

ADMINISTRATIVE

Rev. Proc. 86-24, page 18.
Reproduction of Forms W-2, W-2P, and W-3. Specifications are set forth under which substitutes for Forms W-2, W-2P, and W-3 may be privately printed without prior approval by the Service. Rev. Proc. 85-20 superseded.

T.D. 8077, page 8.
Amendments to the regulations under section 7611 of the Code relate to the procedures for conducting church tax inquiries and examinations.

Announcement 86-69, page 37.
Wages of state and local government employees hired after March 31, 1986, are generally subject to the Medicare portion of the social security tax under the recently enacted Consolidated Omnibus Budget Reconciliation Act. To allow employers time to implement the new requirements of the law, the Service will waive penalties on the tax due for April through December 1986 provided the taxes due are paid by February 2, 1987.

Finding Lists begin on page 42.
Announcement of Disbarments and Suspensions begin on page 38.
Announcement of Notice of Proposed Rulemaking on page 40.

Department of the Treasury
Internal Revenue Service

T 22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 117.—Scholarships and Fellowship Grants

(Also Section 127.)

Qualified tuition reductions. Amounts excludable from gross income as a qualified tuition reduction under section 117(d)(1) are not subject to the $5,000 limitation of section 127(a)(2).

Rev. Rul. 86-69

ISSUE

In the case of the graduate student engaged in teaching or research activities at a university described in section 170(b)(1)(A)(ii) of the Internal Revenue Code, is the $5,000 limit of section 127(a)(2) of the Code applicable to a qualified tuition reduction that is excluded from gross income under section 117(d)(1) of the Code?

FACTS

A is a graduate student and a candidate for a Ph.D. degree at *U*, a university described in section 170(b)(1)(A)(ii) of the Code. *A* also is engaged in teaching or research activities for *U*. In 1985, *U* reduced *A*'s tuition by $6,000. *U* does not maintain for its employees an educational assistance program described in section 127(b).

LAW AND ANALYSIS

Section 117(d)(1) of the Code provides that gross income does not include any qualified tuition reduction.

Section 117(d)(2) of the Code provides that the term "qualified tuition reduction" means the amount of any reduction in tuition provided to an employee of an organization described in section 170(b)(1)(A)(ii) for the education (below the graduate level) at such organization (or another organization described in section 170(b)(1)(A)(ii)) of such employee, or any person treated as an employee (or whose use is treated as an employee use) under the rules of section 132(f).

Section 127(a)(1) of the Code provides that gross income of an employee does not include amounts paid or expenses incurred by the employer for educational assistance to the employee if the assistance is furnished pursuant to a program that meets the requirements of section 127(b).

Section 127(a)(2) of the Code provides that if section 127 would otherwise exclude from gross income more than $5,000 of educational assistance furnished to an individual during a calendar year, section 127(a) will apply only to the first $5,000 of such assistance so furnished.

Section 127(c)(6) of the Code provides that section 127 will not be construed to affect the deduction or inclusion in income of amounts (not within the exclusion under section 127) that are paid or incurred, or received as reimbursement, for educational expenses under section 117, 162 or 212.

Section 127(c)(8) of the Code provides that, in the case of the education of an individual who is a graduate student at an educational organization described in section 170(b)(1)(A)(ii) and who is engaged in teaching or research activities for such organization, section 117(d)(2) will be applied as if it did not contain the phrase "(below the graduate level)."

Pursuant to section 127(d), section 127 will not apply to taxable years beginning after December 31, 1985.

Section 127(c)(8) was added to the Internal Revenue Code of section 1(c) of Pub. L. 98-611, 1985-1 C.B. 413. Section 127(c)(8) is effective for taxable years beginning after December 31, 1983, and, in the case of education described in section 127(c)(8), section 117(d) is treated as being in effect on and after January 1, 1984. Sections 1(g)(1) and 1(g)(5) of Pub. L. 98-611, 1985-1 C.B. 413, 414. The legislative history states with reference to section 127(c)(8):

> Under the bill, the exclusion from gross income for income and employment taxes for qualified tuition reductions (sec. 117(d)) is extended to apply to education furnished to graduate students who are employees of certain educational institutions and who perform teaching or research activities for the educational institutions.

H.R. Rep. No. 98-1049, 98th Cong., 2d Sess. 8, 1985-1 C.B. 414, 416.

In the present situation, section 127(c)(8) extends section 117(d) to *U*'s reduction of *A*'s tuition. As indicated in section 127(c)(6) of the Code, the provisions of sections 117(d)(1) and 127(a) are independent of each other, and amounts that would not be excluded from gross income under section 127(a) may, nonetheless, be excluded under section 117(d)(1). Thus, the $5,000 limitation on the annual exclusion for amounts furnished under an educational assistance program (section 127(a)(2)) does not apply to a qualified tuition reduction under section 117(d)(1).

HOLDING

Whether *A* may exclude the $6,000 of tuition reduction received in 1985 from gross income under section 117(d)(1) is determined without regard to the $5,000 limitation under section 127(a)(2). Any amount of tuition reduction received by *A* in taxable years beginning after December 31, 1985, may not be excluded from *A*'s gross income under 117(d)(1) or 127.

Section 127.—Educational Assistance Programs

Whether amounts excludable from gross income as a qualified tuition reduction under section 117(d)(1) of the Code are subject to the $5,000 limitation under section 127(a)(2). See Rev. Rul. 86-69, this page.

Section 163.—Interest

26 CFR 1.163-1: Interest deduction in general.

Carryover; disallowed interest. A carryover of disallowed interest is not available to the extent it exceeds taxable income for the taxable year in which it was paid or accrued.

Rev. Rul. 86-70

ISSUE

Under the circumstances described below, is a carryover of disallowed interest on investment indebtedness under section 163(d)(2) of the Internal Revenue Code to a succeeding taxable year available to a taxpayer to the extent that the disallowed interest exceeds the taxpayer's taxable income for the taxable year in which the interest was paid or accrued?

FACTS

A, an individual taxpayer, had adjusted gross income as defined in section 62 of the Code of \$100*x* in 1984. *A*'s itemized deductions, as defined in section 63(f) (including all investment interest expense) plus *A*'s personal exemptions totaled \$190*x*. *A* had no unused zero bracket amount as defined in section 63(e). *A*'s deductions as determined before application of section 163(d)(1) did not result in a net operating loss for 1984 as defined in section 172(c). *A*'s computation of the limitation on investment interest under section 163(d)(1) resulted in disallowed interest of \$50*x*. Consequently, *A*'s total allowable deductions under section 63 for 1984 were \$140*x* (\$190*x* − \$50*x*), which exceeded *A*'s adjusted gross income by \$40*x*. Thus, *A* had no taxable income for 1984.

LAW AND ANALYSIS

Section 63(b) of the Code defines taxable income, in the case of an individual, as adjusted gross income reduced by the sum of the excess itemized deductions, the deductions for personal exemptions provided by section 151, and the direct charitable deduction.

Section 163(d)(1) of the Code imposes certain limitations on the amount of interest on investment indebtedness that is allowable as a deduction.

Section 163(d)(2) of the Code provides that the amount of disallowed investment interest for any taxable year shall be treated as investment interest paid or accrued in the succeeding taxable year.

Section 163(d)(3)(E) of the Code provides that the term "disallowed investment interest" means that respect to any taxable year, the amount not allowable as a deduction solely by reason of the limitation in section 163(d)(1).

Section 163(d)(3)(E) of the Code was enacted as part of the Tax Reform Act of 1969, section 221, 1969-3 C.B. 10, 60. the report of the Committee on Ways and Means relating to this provision, H.R. Rep. No. 91-413 (Part 1), 91st Cong., 1st Sess. 74 (1969), 1969-3 C.B. 200, 245-46, explains that a carryover of disallowed interest on investment indebtedness is not available to the extent the disallowed interest exceeds the taxpayer's taxable income for the taxable year in which the interest was paid or accrued. In such circumstances, the disallowed interest would not have reduced taxable income even if it had been allowed as a deduction in that year.

In this case, *A*'s allowable deductions under section 63 of the Code in 1984 exceeded *A*'s adjusted gross income for that year by \$40*x* and resulted in no taxable income. Thus, the disallowed interest would not have reduced *A*'s taxable income in 1984 even if it had been allowed in that year. The \$50*x* of disallowed interest is not therefore disallowed *solely* by reason of section 163(d)(1), and that amount does not constitute "disallowed investment interest" that may be carried over to 1985 under section 163(d)(2).

HOLDING

In the circumstances described above, a carryover of disallowed interest under section 163(d)(2) of the Code to a succeeding taxable year is not available to a taxpayer to the extent that the disallowed interest exceeds the taxpayer's taxable income for the taxable year in which the interest was paid or accrued.

Section 165.—Losses

26 CFR 1.165-1: Losses.

The extent to which an individual may deduct as a loss amounts extended in an unsuccessful attempt to obtain a license to operate a cellular radiotelephone system. See Rev. Rul. 86-71, below.

Section 212.—Expenses for Production of Income

26 CFR 1.212-1: Nontrade or nonbusiness expenses.
(Also Sections 165, 263, 461; 1.165-1, 1.263(a)-1, 1.461-1.)

Deductions; fee for preparation of F.C.C. license application. An amount paid for the preparation of an F.C.C. application for a license to operate a radio system is a capital expenditure and not deductible as an expense under section 212 of the Code. If the application is denied, the fee paid may be deductible at some future date as a loss under section 165.

Rev. Rul. 86-71

ISSUE

If a taxpayer pays a person to prepare an application for a Common Carrier Radio Station Construction Permit and License from the Federal Communications Commission (F.C.C.), is the payment deductible as an expense under section 212 of the Internal Revenue Code in the circumstances described below?

FACTS

In November 1984, taxpayer *A*, an individual not otherwise involved in the telecommunications industry, signed a contract with *X*, a corporation engaged in the business of providing engineering, economic, and financial planning in the telecommunications industry. Under the agreement, *X* prepared and filed a Common Carrier Radio Station Application on behalf of *A* in December 1984. The application is guaranteed to satisfy the filing requirements of the F.C.C., although no assurance is provided that the application will be granted. The application is for participation in the F.C.C.'s random selection program to award licenses to operate cellular radio systems. If granted, the license covers a period greater than one year. The F.C.C. procedures did not permit an award of a license in 1984 for the geographic area that *A*'s application covers, and *A*'s application was not, in fact, acted upon in 1984.

X charged a fee of 30*x* dollars for its services. *A* paid the fee in cash in November 1984.

LAW AND ANALYSIS

Section 212 of the Code provides that an individual shall be allowed a deduction for all ordinary and necessary expenses paid or incurred for the production or collection of income, and for the management, conservation, or maintenance of property held for the production of income. Under section 211, these deductions are limited by exceptions provided by sections 261 through 280G. One of these exceptions, contained in section 263 and sections 1.263(a)-1 and 1.263(a)-2 of the Income Tax Regulations, provides that no deduction shall be allowed for capital expenditures. In addition, section 1.212-1(n) of the regulations provides that no deduction is allowed under section 212 for a capital expenditure.

The costs of obtaining a license to operate a cellular radio-telephone system with a useful life greater than one year are costs of obtaining a capital asset and are not currently deductible as ordinary and necessary expenses for the production of income. *See Dustin v. Commissioner*, 53 T.C. 491 (1969), *aff'd*, 467 F.2d 47 (9th Cir. 1972); *KWTX Broadcasting Co., Inc. v. Commissioner*, 31 T.C. 952, *aff'd per curiam*, 272 F.2d 406 (5th Cir. 1959); *Radio Station WBIR, Inc. v. Commissioner*, 31 T.C. 803 (1959). *See also* Rev. Rul. 56-520, 1956-2 C.B. 170.

In the present situation, the fee paid by *A* is to file an application to acquire an operating license, with a useful life greater than one year, that *A* may obtain at some indefinite future date. Accordingly, the expense is related to the cost of acquiring a capital asset, and pursuant to section 263 of the Code and sections 1.263(a)-1, 1.263(a)-2 and 1.212-1(n) of the regulations, *A* is not entitled to deduct the fee paid to *X* under section 212. *See Central Texas Savings & Loan Association v. United States*, 731 F.2d 1181 (5th Cir. 1984).

If, however, *A* is unsuccessful in obtaining the license, a deduction for the application fee may be allowable as a loss under section 165(a) of the Code. *A* will not be allowed to deduct the loss until the tax year in which final action is taken to deny the application. Section 1.165-1(b) of the regulations; Rev. Rul. 71-191, 1971-1 C.B. 77, clarified by Rev. Rul. 79-346, 1979-2 C.B. 84; Rev. Rul. 83-137, 1983-2 C.B. 41; Rev. Rul. 56-520, 1956-2 C.B. 170.

HOLDING

The fee paid by *A* to *X* in 1984 is a capital expenditure within the scope of section 263, and thus is not deductible as as expense under seciton 212 of the Code.

Section 263.—Capital Expenditures

26 CFR 1.263(a)-1: Capital expenditures; in general.

Whether an amount expended to obtain a license to operate a cellular radiotelephone system is a capital expenditure. See Rev. Rul. 86-71, page 5.

Section 453.—Installment Method

26 CFR 1.453-1: Installment method of reporting income.

Whether gain is recognized by a payee's estate if, pursuant to the terms of an installment note, the note is automatically cancelled on the payee's death. See Rev. Rul. 86-72, this page.

Section 453B.—Gain or Loss on Disposition of Installment Obligations

Whether gain is recognized by a payee's estate if, pursuant to the terms of an installment note, the note is automatically cancelled on the payee's death. See Rev. Rul. 86-72, this page.

Section 461.—General Rule For Taxable Year of Deduction

26 CFR 1.461-1: General rule for taxable year of deduction.

When amounts expended to obtain a license to operate a cellular radiotelephone system may be deducted. See Rev. Rul. 86-71, page 5.

Section 691.—Recipients of Income in Respect of Decedents

26 CFR 1.691(a)-1: Income in respect of a decedent.
(Also Sections 453, 453B.)

Installment obligation; cancelled on death of payee. Gain is recognized by the estate of a payee of an installment obligation that is cancelled because of the death of the payee.

Rev. Rul. 86-72

ISSUE

Is gain recognized when an installment obligation terminates because of the death of the payee, and, if so, is the gain recognized by the payee or the payee's estate.

FACTS

On July 1, 1981, *A*, an individual taxpayer, sold property and accepted a cash downpayment and an installment note providing for payment in annual installments over 4 years, plus interest at 11 percent on the unpaid balance. Both the sales agreement and the installment note provided that all sums due on the note were automatically extinguished and cancelled at *A*'s death. *A* reported the gain on the sale on the installment method of accounting under section 453 of the Internal Revenue Code.

On the date of the sale, *A*'s actuarial life expectancy was 21 years, as determined by reference to Table 1.—Ordinary Life Annuities—One Life—Expected Return Multiples, in section 1.72-9 of the Income Tax Regulations. *A* died 2 years after the sale, with 2 installment payments outstanding.

LAW AND ANALYSIS

Section 453 of the Code permits the transferor in an installment sale to take into account ratably over the period during which the installment payments are received, any gain resulting from the sale. Section 453B(a) provides generally that gain or loss shall result from the disposition of an installment obligation. Section 453B(f)(1) treats the cancellation of an installment obligation as a taxable disposition. Section 453B(c) provides that, except as provided in section 691, the disposition rules of section 453B do not apply to the transmission of installment obligations at death.

Section 691(a)(2) of the Code provides that if a right to receive an amount is transferred by the estate of the decedent, there shall be included in the gross income of the estate for the taxable period in which the transfer occurs the fair market value of such right at the time of such transfer plus the amount by which any consideration for the transfer exceeds such fair market value.

Section 691(a)(5) of the Code provides that, for purposes of 691(a)(2), in the case of an installment obligation held by the decedent before the decedent's death and reportable by the decedent under section 453, any cancellation of the obligation at the death of the decedent shall be treated as a transfer by the decedent's estate.

In the present case, *A*'s death cancelled the installment obligation with 2 payments outstanding. Because *A* reported the gain from the sale on the installment method of accounting, recognition of the portion of the gain represented by the outstanding payments was deferred during *A*'s lifetime.

The legislative history indicates that section 691(a)(5) of the code was enacted to clarify prior law, so that the installment obligation disposition rules would apply to obligations that are cancelled or become unenforceable by reason of death of the holder of the obligation. S. Rep. No. 96-1000, 96th Cong., 2d Sess. 26 (1980), 1980-2 C.B. 494, 508.

HOLDING

Under sections 691(a)(2) and 691(a)(5), gain is recognized by and includible in the gross income of *A*'s estate.

Section 708—Continuation of Partnership

26 CFR 1.708-1: Continuation of partnership.
(Also Sections 732, 743, 754, 755; 1.732-2, 1.743-1, 1.754-1, 1.755-1.)

Partnership; termination of sale interests; effect of section 754 election on deemed distribution to incoming partner. A section 754 election in effect upon the sale of a 50 percent interest in partnership capital and profits applies to the interest of the incoming partner for purposes of determining adjusted basis upon the deemed distribution of partnership assets following a termination under section 708(b)(1)(B).

Rev. Rul. 86-73

ISSUE

If a 50 percent interest in a partnership is sold causing the partnership to terminate under section 708(b)(1)(B) of the Internal Revenue Code and a section 754 election is in effect for the taxable year in which the sale occurs, does the election apply with respect to the incoming partner so that the bases of any partnership assets are adjusted prior to their deemed distribution to the partner.

FACTS

T, a 50 percent partner in *PT*, a partnership, sold *T*'s interest to *A*. For the taxable year in which the sale occurred, *PT* had an election in effect under section 754 of the Code, and the fair market value of *PT*'s property exceeded its adjusted basis.

LAW AND ANALYSIS

Section 708(b)(1)(B) of the Code provides that a partnership shall be considered as terminated if within a twelve month period there is a sale or exchange of 50 percent or more of the total interest in partnership capital and profits.

Section 1.708-1(b)(1)(iv) of the Income Tax Regulations provides that if a partnership is terminated by a sale or exchange of an interest, the partnership is deemed to distribute its properties to the purchaser and to the other remaining partners in proportion to their respective interests in the partnership properties. Immediately thereafter, the purchaser and the other remaining partners are deemed to contribute the properties to a new partnership. The last sentence of that provision states that, for an election of basis adjustments by the purchaser and other remaining partners, see sections 732(d) and 743(b) of the Code and the regulations thereunder.

Section 732(b) of the Code provides that the basis of property (other than money) distributed by a partnership to a partner in liquidation of the partner's interest shall be an amount equal to the adjusted basis of such partner's interest in the partnership reduced by any money distributed in the same transaction.

Section 732(c) of the Code provides that the basis of distributed properties to which section 732(b) is applicable generally shall be allocated first to any unrealized receivables and inventory items in an amount equal to the adjusted basis of each such property to the partnership and, to the extent of any remaining basis, to any other distributed properties in proportion to their adjusted based to the partnership.

Section 1.732-2(b) of the regulations provides that in the case of a distribution of property to a partner who acquired any part of an interest in a transfer as to which an election under section 754 of the Code was in effect, then, for the purposes of section 732, the adjusted partnership basis of the distributed property shall take into account the transferee's special basis adjustment for the distributed property under section 743(b).

Section 743(b) of the Code provides that in the case of a transfer of an interest in a partnership by sale or exchange, a partnership as to which the election provided in section 754 is in effect shall (1) increase the adjusted basis of the partnership property by the excess of the basis to the transferee partner of the partner's interest in the partnership over the partner's proportionate share of the adjusted basis of the partnership property, or (2) decrease the adjusted basis of the partnership property by the excess of the transferee partner's proportionate share of the adjusted basis of the partnership property over the basis of the partner's interest in the partnership. Such increase or decrease generally constitutes an adjustment to the basis of partnership property with respect to the transferee partner only.

Section 754 of the Code provides the manner in which a partnership shall file an election to adjust the basis of partnership property under section 743.

Section 755(a) of the Code provides that any increase or decrease in the adjusted basis of partnership property under section 743(b) shall be allocated in a manner which has the effect of reducing the difference between the fair market value and the adjusted basis of partnership properties.

The issue here is whether the section 754 election applies to adjust the basis of partnership assets with respect to the incoming 50 percent partner before the constructive liquidation of the partnership that occurs under section 1.708-1(b)(1)(iv) of the regulations, or whether the sale of the 50 percent interest to the incoming partner extinguishes the section 754 election before it can be applied.

The language of section 1.708-1(b)(1)(iv) of the regulations treats the partnership property as constructively distributed to the incoming purchaser and the remaining partners. This indicates that the purchaser is a partner for the instant before the constructive liquidating distribution is deemed to occur; thus, the purchaser is a partner at least for the purpose of the termination. Since the purchaser is a partner in the instant before termination, the section 754 election applies in that instant, and the incoming partner's basis in the partnership assets is correspondingly adjusted. Upon the deemed distribution-recontribution under section 1.708-1(b)(1)(iv), the special basis adjustment under section 743(b) of the Code is taken into account in applying sections 732(b) and (c). If the new partnership, *PA*, wants to make a section 754 election, it will have to file a new election.

The legislative history of section 743 buttresses the conclusion that the adjustment of basis of partnership assets is made before the deemed liquidating distribution occurs. The report of the Senate Finance Committee, S. Rep. No. 1622, 83d Cong., 2d Sess. 399 (1954), contains an example in which a section 754 election is applied to adjust the basis of partnership assets when a fifty percent interest in a partnership is sold.

HOLDING

If a 50 percent interest in a partnership is sold causing the partnership to terminate under section 708(b)(1)(B) of the Code, a section 754 election that is in effect for the taxable year in which the sale occurs applies with respect to the incoming partner. Therefore, the bases of any partnership assets are adjusted pursuant to sections 743 and 755 prior to their deemed distribution to the incoming partner.

Section 732.—Basis of Distributed Property Other Than Money

26 CFR 1.732-2: Special partnership basis of distributed property.

Whether a section 754 election applies to the transferee of a 50 percent interest in partnership capital and profits for purposes of the deemed distribution following the section 708(b)(1)(B) termination. See Rev. Rul. 86-73, page 7.

Section 743.—Optional Adjustment to Basis of Partnership Property

26 CFR 1.743-1: Optional adjustment to basis of partnership property.

Whether a section 754 election applies to the transferee of a 50 percent interest in partnership capital and profits for purposes of the deemed distribution following the section 708(b)(1)(B) termination. See Rev. Rul. 86-73, page 7.

Section 754.—Manner of Electing Optional Adjustment to Basis of Partnership Property

26 CFR 1.754-1: Time and manner of making election to adjust basis of partnership property.

Whether a section 754 election applies to the transferee of a 50 percent interest in partnership capital and profits for purposes of the deemed distribution following the section 708(b)(1)(B) termination. See Rev. Rul. 86-73, page 7.

Section 755.—Rules for Allocation of Basis

26 CFR 1.755-1: Rules for allocation of basis.

Whether a section 754 election applies to the transferee of a 50 percent interest in partnership capital and profits for purposes of the deemed distribution following the section 708(b)(1)(B) termination. See Rev. Rul. 86-73, page 7.

Section 6011.—General Requirement of Return, Statement or List

Printing of substitutes for Form W-2, Wage and Tax Statement, From W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay or IRA Payments, and Form W-3, Transmittal of Income and Tax Statements. See Rev. Proc. 86-24, page 18.

Section 6033.—Returns by Exempt Organizations

26 CFR 1.6033-2: Returns by exempt organizations; taxable years beginning after December 31, 1969.

Additional class of exempt organizations that is not required to file Form 990. See Rev. Proc. 86-23, page 17.

Section 6041.—Information at Source

26 CFR 1.6041-1: Return of information as to payment of $600 or more.

Printing of substitutes for Form W-2, Wage and Tax Statement, Form W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay or IRA Payments, and Form W-3, Transmittal of Income and Tax Statements. See Rev. Proc. 86-24, page 18.

Section 6047.—Information Relating to Certain Trusts and Annuity and Bond Purchase Plans

26 CFR 1.6047-1: Information to be furnished with regard to employee retirement plan covering an owner-employee.

Printing of substitutes for Form W-2, Wage and Tax Statement, Form W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay or IRS Payments, and Form W-3, Transmittal of Income and Tax Statements. See Rev. Proc. 86-24, page 18.

Section 6051.—Receipts for Employees

26 CFR 31.6051-1: Statements for employees.

Printing of substitutes for Form W-2, Wage and Tax Statement, Form W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay or IRA Payments, and Form W-3, Transmittal of Income and Tax Statements. See Rev. Proc. 86-24, page 18.

26 CFR 31.6051-2: Information returns on Form W-3 and Internal Revenue Service copies of Forms W-2.

Printing of substitutes for Form W-2, Wage and Tax Statement, Form W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay or IRA Payments, and Form W-3, Transmittal of Income and Tax Statements. See Rev. Proc. 86-24, page 18.

Section 6071.—Time for Filing Returns and Other Documents

26 CFR 31.6071(a)-1: Time for filing returns and other documents.

Printing of substitutes for Form W-2, Wage and Tax Statement, Form W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay or IRA Payments, and Form W-3, Transmittal of Income and Tax Statements. See Rev. Proc. 86-24, page 18.

Section 6081.—Extension of Time for Filing Returns

26 CFR 31.6081(a)-1: Extension of time for filing returns.

Printing of substitutes for Form W-2, Wage and Tax Statement, Form W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay or IRA Payments, and Form W-3, Transmittal of Income and Tax Statements. See Rev. Proc. 86-24, page 18.

Section 6091.—Place for Filing Returns of Other Documents

Printing of substitutes for Form W-2, Wage and Tax Statement, Form W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay or IRA Payments, and Form W-3, Transmittal of Income and Tax Statements. See Rev. Proc. 86-24, page 18.

Section 7611.—Restrictions on Church Tax Inquiries and Examinations

26 CFR 301.7611-1. Questions and answers relating to church tax inquiries and examinations.

T.D. 8077

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER F, Part 301—PROCEDURE AND ADMINISTRATION

Restrictions on Church Tax Inquiries and Examinations

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the procedures for conducting church tax inquiries and examinations. Changes to the applicable law were made by the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1]. The regulations provide guidance concerning the procedures described in the Act and affect church tax inquiries and examinations within the scope of section 7611 of the Internal Revenue Code of 1954 as well as certain other requests for information relating directly or indirectly to churches.

DATES: The regulations apply to all church tax inquiries and examinations beginning after December 31, 1984 and are effective after December 31, 1984. Church examinations commenced prior to January 1, 1985, will be conducted pursuant to section 7605(c) of the Internal Revenue Code of 1954.

FOR FURTHER INFORMATION CONTACT: Monice Rosenbaum of the Employee Plans and Exempt Organizations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention CC:EE) Telephone 202-566-3938 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

On March 11, 1985, the Federal Register published proposed amendments to the Procedure and Administration Regulations (26 CFR Part 301), in the form of temporary regulations, under section 7611 of the Internal Revenue Code of 1954 (50 FR 9614) [T.D. 8013, 1985-1 C.B. 390]. The amendments were proposed to conform the regulations to changes made by the addition of section 7611 by section 1033 of the Tax Reform Act of 1984 (Pub. L. 98-369, 98 Stat. 1034-1039) [1984-3 C.B. (Vol. 1) 1, 546]. The temporary regulations were accompanied by a notice of proposed rulemaking published in the Federal Register on March 11, 1985 (50 FR 9678) [EE-1-85, 1985-1 C.B. 628] soliciting public comments.

Public comments on the proposed regulations were received. A public hearing was held on July 16, 1985. After consideration of all comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

PUBLIC COMMENTS

Commentators suggested that the language of Q and A-3, defining what is a "church" for purposes of the section 7611 procedures, was inadequate in the case of an organization which operates at multiple locations or in the case of an organization composed of various functions some of which may or may not be separately incorporated. The text of Q and A-3 is not changed in these final regulations because the application of the section 7611 procedures to any organization "claiming to be a church" is deemed sufficiently broad to cover those situations where the Internal Revenue Service contacts the organization in a manner inconsistent with the section 7611 procedures on the assumption that the entity is not a church. Any organization claiming to be a church, and thus included under the procedures of section 7611, should advise the Internal Revenue Service of its claim when contacted.

Commentators questioned whether Q and A-5, concerning the extent to which the Internal Revenue Service may use third party records, and Q and A-11, concerning circumstances in which the Internal Revenue Service may, in lieu of an examination, propose to revoke an organization's exemption, were to be applied without regard to the procedures of section 7611. Qs and As 5 and 11, that refer to these situations, each contains specific language which requires the Internal Revenue Service to provide the organization with notice and offer of a conference.

Commentators noted that Q and A-15 provides that the Internal Revenue Service may examine records of a year earlier than the year, or years, specified in the examination notice. An examination of records of an earlier year may be made if material to a determination of exempt status during the period under examination or if material to a determination of unrelated business income tax liability. An examination of records of an earlier year may be necessary, for example, in cases concerning adjustments to basis, depreciation or amortization. The number of years under examination or for which an assessment of tax may be made are limited by section 7611(d)(2); however, section 7611(b)(4) authhorizes the examination of any records not specified in the examination notice to the extent necessary to determine tax liability.

Other comments received have been addressed in the Internal Revenue Manual provisions relating to church tax inquiries and examinations.

A change has been made to Q and A-9 in response to a comment suggesting that the Internal Revenue Service be required to request information during the inquiry notice stage in an effort to alleviate the concerns which gave rise to the inquiry.

A change has been made to Q and A-10 in response to a comment that the expansion of an examination should be a result of facts and circumstances which subsequently come to the attention of the Internal Revenue Service after issuance of the notice of examination.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required.

Although a notice of proposed rulemaking soliciting public comments was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these regulations are not subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is Monice Rosenbaum of the Employee Plans and Exempt Organizations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * * *

Adoption of Amendments to the Regulations

Accordingly, after careful consideration of all comments received, 26 CFR Part 301 is amended as follows:

PROCEDURE AND ADMINISTRATION

[26 CFR 301]

Paragraph 1. The authority for Part 301 continues to read in part:

Authority: 26 U.S.C. 7805. * * *.

Par. 2. Section 301.7611-1T is amended by removing "T" from the section number and removing the word "(Temporary)" from the title.

§301.7611 Questions and answers relating to church tax inquiries and examinations

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Par. 3. The last sentence of the first paragraph of A-9 of section 301.7611-1 is amended by removing the words "may also" and adding in their place the words "will generally".

Notice Requirements

Q-9: What satisfies the inquiry notice requirement (first notice) upon commencement of a church tax inquiry?

A-9: Upon commencing a church tax inquiry, the appropriate Regional Commissioner is required to provide written notice to the church of the beginning of the inquiry. This notice will include (1) an explanation of the concerns which gave rise to the inquiry and the general subject matter of the inquiry, which is sufficiently specific to allow the church to understand the particular area of church activities or behavior which is at issue; (2) a general explanation of the provisions of the Internal Revenue Code which authorize the inquiry or which may otherwise be involved in the inquiry; and (3) a general explanation of applicable administrative and constitutional provisions with respect to the inquiry, including the right to a conference with the Internal Revenue Service before an examination of church records is commenced. The inquiry notice (first notice) will generally request information in an effort to alleviate the concerns which gave rise to the inquiry.

However, the Internal Revenue Service is not precluded from expanding its inquiry beyond the concerns expressed in the inquiry notice (first notice) as a result of facts and circumstances which subsequently comes to its attention (including, where appropriate an expansion of an unrelated business income inquiry to include questions of tax-exempt status, and vice-versa).

The inquiry notice requirement (first notice) does not require the Internal Revenue Service to share particular items of evidence with the church, or to identify its sources of information regarding church activities, if providing such information would be damaging to the inquiry or to the sources of information. For example, in an inquiry regarding unrelated business income, the Internal Revenue Service might state that its inquiry was prompted by a local newspaper advertisement regarding a church-owned business. However, the Internal Revenue Service would not be required to reveal the existence or identity of any so-called "informers" within a church (including present or former employees).

Par. 4. the last sentence of the second paragraph of A-10 of section 301.7611-1 is amended by removing the words "(see Q and A-9)". The following new sentence is added to the end of that paragraph:

Q-10: What must be done to satisfy the examination notice requirement (second notice) before commencing an examination of church records or religious activities with respect to an examination conducted under section 7611?

A-10: Where an examination is conducted under section 7611, church records or religious activities of a church may be examined only if, at least 15 days prior to the examination, written notice of the proposed examination is provided to the church and to the appropriate Regional Counsel. This notice is in addition to the notice of commencement of inquiry (first notice) previously provided to the church.

The notice of examination (second notice) is required to include (1) a copy of the church tax inquiry notice (first notice) previously provided to the church; (2) a description of the church records and activities sought to be examined; and (3) a copy of all documents which were collected or prepared by the Internal Revenue Service for use in the examination, and which are required to be disclosed under the Freedom of Information Act (5 U.S.C. 552) as supplemented by section 6103 of the Code (relating to disclosure and confidentiality of tax return information). The documents to be supplied under this provision will be limited to documents specifically concerning the church whose records are to be examined and will not include documents relating to other inquiries or examinations or to Internal Revenue Service practices and procedures in general. Disclosure to the church will be subject to restrictions regarding the disclosure of the existence or identity of informants. Although a description of materials to be examined will be provided in the notice of examination (second notice), the description does not restrict the ability of the Internal Revenue Service to examine church records or religious activities which are not specifically mentioned in the notice of examination (second notice) but which are properly within the scope of the examination. Thus, the Internal Revenue Service is not precluded from expanding its inquiry beyond the concerns expressed in the examination notice (second notice) as a result of facts and circumstances which subsequently come to its attention (including, where appropriate, an expansion of an unrelated business income examination to include questions of tax-exempt status, and vice versa).

At the time the notice of examination (second notice) is provided to the church, a copy of the same notice will be provided to the appropriate Regional Counsel. The Regional Counsel is then allowed 15 days from issuance of the second notice in which to file an advisory objection to the examination. (This is concurrent with the 15-day period during which an examination of church records is prohibited pending a request for a conference.)

As part of the notice of examination (second notice), the church will be offered an opportunity to meet with an Internal Revenue Service official to discuss the concerns which gave rise to the inquiry and the general subject matter of the inquiry. An examination will not begin until 15 days after the mailing of the notice of examination (second notice). The organization may request a conference at any time prior to beginning of the examination and a conference so requested will be scheduled within a reasonable time after the request is made.

The purpose of the conference is to remind the church, in general terms, of the stages of the church tax inquiry and examination procedures and to discuss the relevant issues that may arise as part of the inquiry, in an effort to resolve the issues of tax exemption or liability without the necessity of an examination of church records or activities. Information properly excludable from a written notice of examination (second notice) (including information regarding the identity of third-party witnesses or evidence provided by such witnesses) is not a subject for discussion at, and will not be revealed during, a conference.

Once a conference request is timely made, an examination will begin only following the conference. The conference requirement may not be utilized to delay an examination beyond the time reasonably necessary to prepare for and hold the conference. The holding of one conference with the church will be sufficient to satisfy the requirements of section 7611 and these questions and answers.

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved January 27, 1986.

J. ROGER MENTZ,
Acting Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on February 20, 1986, 8:45 a.m., and published in the issue of the Federal Register for February 21, 1986, 51 F.R. 6219)

Section 408.—Individual Retirement Accounts

26 CFR 1.408-6: Disclosure statements for individual retirement arrangements.

Individual retirement arrangements; disclosure. If values under an individual retirement arrangement (IRA) are guaranteed or can be projected, the trustee or issuer must in certain instances disclose to an IRA purchaser the amounts guaranteed or projected to be withdrawable.

Rev. Rul. 86-78

This ruling provides questions and answers relating to the financial disclosure that must be provided by the trustee or issuer of an individual retirement account or annuity (IRA) to the individual to be benefited by an IRA.

Section 1.408-6(d)(4) of the Income Tax Regulations provides that the trustee or isssuer of an IRA must furnish a disclosure statement to the benefited individual and prescribes the information the statement must contain. Among other things, the statement must satisfy the applicable financial disclosure requirements of section 1.408-6(d)(4)(v), (vi), and (vii) of the regulations. That section requires that where an amount is guaranteed over a period of time, or a projection of growth in value of the IRA can reasonably by made, the disclosure statement must show the amount guaranteed or projected to be made available to the benefited individual if (1) level annual contributions in the amount of $1,000 were made on the first day of each year, and (2) the benefited individual were to withdraw, in a single sum, the entire amount of the IRA at the end of each of the first five years during which contributions are to be made, at the end of the year in which the benefited individual attains the ages of 60, 65, and 70, and at the end of each year during which the increase in the guaranteed available amount is less than the increase in the guaranteed amount available during any preceding year. Similar information must be provided with respect to amounts guaranteed or projected to be made available under an IRA which is to receive only a rollover contribution except the amounts guaranteed or projected to be made available are based on only one $1,000 contribution made in the beginning of the year the rollover contribution occurred.

This ruling is being issued because of the widespread public interest in the amounts that must be shown to be made available on the IRA disclosure statement where the IRA values are either guaranteed or can reasonably be projected. It is important that trustees and issuers of IRAs know the IRS position on these matters because such trustees and issuers can be subject to penalties for failure to conform to IRA disclosure requirements.

No inference should be drawn regarding matters not addressed which may be suggested by a particular question or answer or as to why certain questions and not others are included.

Q–1. What must be taken into account in computing the amounts that are required to be disclosed where the values under the IRA are guaranteed or can be reasonably projected?

A–1. The amount that is shown to be available at any particular time must be the amount actually guaranteed or reasonably projected to be withdrawable after reduction for all charges or penalties that may be applied, including, for example, trustee fees and any penalties for early withdrawal (such as interest forfeiture provisions for early withdrawal for a time deposit). For example, the issuer of an IRA that guarantees or reasonably projects an earnings rate of 10 percent annual interest, but deducts five percent of any amounts withdrawn within five years after the account is established, must show $1,045 ($1,000 × 1.10 × .95) as the amount available if the account is withdrawn at the end of the first year, whether or not such fees and penalties are charged directly to the account or stated separately.

Q–2. In the example given in Q–1, would it be acceptable to show $1,100 as available at the end of the first year and indicate separately that there is a five percent or $55 ($1,100 × .05) deduction for withdrawal at the end of the first year?

A–2. No. The disclosure statement must show the amount that could actually be withdrawn by the benefited individual at the end of the first year after reduction for all applicable charges and penalties.

Q–3. Must guarantees or projections of IRA values available at ages 60, 65, and 70 of the benefited individual be based on the actual age of the benefited individual?

A–3. Yes. Amounts guaranteed or projected for ages 60, 65, and 70 must be computed based on the actual age of the benefited individual as of the date the IRA is established. The requirement to provide the value of the IRA at ages 60, 65, and 70 must be met by providing the values for the particular benefited individual at those ages.

Q–4. May the requirement discussed in Q-3 be met by providing a table that shows the values at those ages based on various ages at the time the IRA is established, including the age of the particular benefited individual at that time?

A–4. Yes. Also, it would be sufficient to provide a table that shows the value of the IRA based on the number of years after the IRA was established if the benefited individual, by knowing how many years it will be until he or she reaches ages 60, 65, and 70, could determine the value of the IRA at those times.

Q–5. If the IRA has a minimum guaranteed earnings rate that is lower than the rate currently being paid on the IRA investments, may the trustee or issuer of the IRA show projected amounts based on the earnings rate actually being paid?

A–5. If the trustee or issuer of the IRA is paying earnings at a greater rate than guaranteed to be paid and it is reasonable to project growth in values, the disclosure statement may show a projected amount available based on the actual greater rate. However, section 1.408-6(d)(4)(v)(A)(1) and (B)(2) of the regulations requires that the disclosure statement clearly identify what amounts are, or are not, guaranteed to be available to the benefited individual.

Q–6. If the earnings rate of the IRA is not guaranteed but a reasonable projection of growth may be made, may the projection use an assumed earnings rate that is greater than the rate being paid at the time the IRA is being established?

A–6. No. Where the values of the IRA are projected and not guaranteed, section 1.408–6(d)(4)(v)(B)(2) of the regulations requires the projection be based on an earnings rate no greater than the rate currently being paid.

Q–7. If the earnings rate of the IRA is not guaranteed but may be projected, may the projection use an assumed earnings rate that is lower than the rate being paid at the time the IRA is being established?

A–7. Yes. In fact, if the trustee or issuer uses the greatest earnings rate allowable in the disclosure statement projections, and the actual earnings rate then falls below that rate, the disclosure statement must be revised before the IRA is offered to other individuals. Thus, trustees or issuers of IRAs may prefer to use more conservative earnings rates than the greatest rate allowable so that small decreases in the earnings rate being paid will not require immediate modification of their disclosure statements.

Example

Bank M provides an IRA that guarantees an interest rate of 6 percent per year compounded daily using a 365/360 day year. However, a withdrawal penalty of 10 percent of the amount in the account is assessed by Bank M if withdrawal takes place within the first 10 years. Currently, the IRA is paying earnings at 8 percent using the same method of compounding as is used for the guaranteed rate. An individual establishes an IRA with Bank M. The disclosure requirements are satisfied if the following instructions and tables are provided to such individual (similar tables would be used for a rollover of $1,000, except that such tables would reflect only one payment of $1,000):

Instructions for Use of the Tables Below

(1) Find your age in the first column of the table.

(2) Look across the table on the same line as your age to determine the projected value of the account at ages 60, 65 and 70, after taking out any withdrawal penalty.

(3) At the top of each table values are shown for the projected account after taking the withdrawal penalty at the end of the first, second, third, fourth and fifth years. Values at the end of the first five years will be the same for all ages.

(4) The first table uses the current rate and the second table uses the guaranteed rate.

(5) The projections used the following assumptions:
   (a) A level contribution of $1,000 annually paid on the first day of the calendar year;
   (b) Interest compounded daily using a 365/360 day year, i.e., using an effective daily rate of interest of 1/360 of the assumed rate and compounding such effective daily rate for 365 days per year.

INTEREST RATE EQUALS 8 PERCENT COMPOUNDED DAILY USING A 365/360 DAY YEAR
TABLE INCLUDES A WITHDRAWAL PENALTY OF 10 PERCENT DURING FIRST 10 YEARS

END OF YEAR	ACCUMULATED AMOUNT
1	976.03
2	2,034.52
3	3.182.44
4	4,427.33
5	5,777.39

AGE AT OPENING	AGE 60	AGE 65	AGE 70
18	406,935.68	616,850.61	931,737.32
19	374,235.20	567,797.65	858,154.54
20	344,082.10	522,565.94	790,303.89
21	316,277.94	480,857.80	727,738.84
22	290,639.74	442,398.75	670,047.64
23	266,998.77	406,935.68	616,850.61
24	245,199.44	374,235.20	567,797.65
25	225,098.29	344,082.10	522,565.94
26	206,563.03	316,277.94	480,857.80
27	189,471.67	290,639.74	442,398.75
28	173,711.74	266,998.77	406,935.68
29	159,179.51	245,199.44	374,235.20
30	145,779.35	225,098.29	344,082.10
31	133,423.07	206,563.03	316,277.94
32	122,029.35	189,471.67	290,639.74
33	111,523.21	173,711.74	266,998.77
34	101,835.50	159,179.51	245,199.44
35	92,902.47	145,779.35	225,098.29
36	84,665.32	133,423.07	206,563.03
37	77,069.85	122,029.35	189,471.67
38	70,066.07	111,523.21	173,711.74
39	63,607.89	101,835.50	159,179.51
40	57,652.81	92,902.47	145,779.35
41	52,161.63	84,665.32	133,423.07
42	47,098.22	77,069.85	122,029.35
43	42,429.25	70,066.07	111,523.21
44	38,123.99	63,607.89	101,835.50
45	34,154.11	57,652.81	92,902.47
46	30,493.49	52,161.63	84,665.32
47	27,118.03	47,098.22	77,069.85
48	24,005.52	42,429.25	70,066.07
49	21,135.48	38,123.99	63,607.89
50	18,489.02	34,154.11	57,652.81
51	14,443.85	30,493.49	52,161.63
52	12,418.67	27,118.03	47,098.22
53	10,551.25	24,005.52	42,429.25
54	8,829.31	21,135.48	38,123.99
55	7,241.50	18,489.02	34,154.11
56	5,777.39	14,443.85	30,493.49
57	4,427.33	12,418.67	27,118.03
58	3,182.44	10,551.25	24,005.52
59	2,034.52	8,829.31	21,135.48
60	976.03	7,241.50	18,489.02
61		5,777.39	14,443.85
62		4,427.33	12,418.67
63		3,182.44	10,551.25
64		2,034.52	8,829.31
65		976.03	7,241.50
66			5,777.39
67			4,427.33
68			3,182.44
69			2,034.52
70			976.03

THE ABOVE TABLE SHOWS THE ACCUMULATION USING RATES THAT ARE NOT GUARANTEED
THE TABLE BELOW SHOWS THE ACCUMULATION USING THE GUARANTEED RATE

ACCUMULATION TABLE FOR IRA ACCOUNT

INTEREST RATE EQUALS 6 PERCENT COMPOUNDED DAILY USING A 365/360 DAY YEAR
TABLE INCLUDES A WITHDRAWAL PENALTY OF 10 PERCENT DURING FIRST 10 YEARS

END OF YEAR	ACCUMULATED AMOUNT
1	956.45
2	1,972.88
3	3,053.06
4	4,200.98
5	5,420.90

AGE AT OPENING	AGE 60	AGE 65	AGE 70
18	214,786.13	297 157.26	408,808.05
19	201 110.50	278,620.49	383,682.19
20	188,241.94	261,177.67	360,039.14
21	176,132.82	244,764.24	337,791.39
22	164,738.32	229,319.45	316,856.59
23	154,016.27	214,786.13	297,157.26
24	143,926.98	201,110.50	278,620.49
25	134,433.11	188,241.94	261,177.67
26	125,499.52	176,132.82	244,764.24
27	117,093.15	164,738.32	229,319.45
28	109,182.88	154,016.27	214,786.13
29	101,739.44	143,926.98	201,110.50
30	94,735.27	134,433.11	188,241.94
31	88,144.45	125,499.52	176,132.82
32	81,942.59	117,093.15	164,738.32
33	76,106.74	109,182.88	154,016.27
34	70,615.29	101,739.44	143,926.98
35	65,447.92	94,735.27	134,433.11
36	60,585.50	88,144.45	125,499.52
37	56,010.04	81,942.59	117,093.15
38	51,704.60	76,106.74	109,182.88
39	47,653.24	70,615.29	101,739.44
40	43,840.98	65,447.92	94,735.27
41	40,253.70	60,585.50	88,144.45
42	36,878.12	56,010.04	81,942.59
43	33,701.75	51,704.60	76,106.74
44	30,712.83	47,653.24	70,615.29
45	27,900.31	43,840.98	65,447.92
46	25,253.77	40,253.70	60,585.50
47	22,763.41	36,878.12	56,010.04
48	20,420.02	33,701.75	51,704.60
49	18,214.93	30,712.83	47,653.24
50	16,139.97	27,900.31	43,840.98
51	12,768.71	25,253.77	40,253.70
52	11,115.16	22,763.41	36,878.12
53	9,559.20	20,420.02	33,701.75
54	8,095.06	18,214.93	30,712.83
55	6,717.32	16,139.97	27,900.31
56	5,420.90	12,768.71	25,253.77
57	4,200.98	11,115.16	22,763.41
58	3,053.06	9,559.20	20,420.02
59	1,972.88	8,095.06	18,214.93
60	956.45	6,717.32	16,139.97
61		5,420.90	12,768.71
62		4,200.98	11,115.16
63		3,053.06	9,559.20
64		1,972.88	8,095.06
65		956.45	6,717.32
66			5,420.90
67			4,200.98
68			3,053.06
69			1,972.88
70			956.45

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.602: Forms and instructions.
(Also Part I, Section 6033; 1.6033-2.)

Rev. Proc. 86-23

SECTION 1. PURPOSE

The purpose of this revenue procedure is to supplement Rev. Proc. 83-23, 1983-1 C.B. 687, and to supersede Notice 84-2, 1984-1 C.B. 331, by establishing an additional class of organizations, affiliated with a church or convention or association of churches and exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code, that is not required to file an annual information return on Form 990, Return of Organization Exempt from Income Tax.

SEC. 2. BACKGROUND

.01 Section 6033(a)(1) of the Code generally requires the filing of annual information returns by exempt organizations.

.02 Section 6033(a)(2)(A) of the Code provides certain mandatory exceptions to this filing requirement.

.03 In addition, section 6033(a)(2)(B) of the Code provides discretionary exceptions from filing such returns where the Secretary "Determines such filing is not necessary to the efficient administration of the internal revenue laws." Section 1.6033-2(g)(6) of the Income Tax Regulations delegates authority to the Commissioner to excuse organizations from the filing requirement. It provides that "the Commissioner may relieve any organization or class of organizations from filing, in whole or in part, the annual return required by section 6033 where he determines that such returns are not necessary for the efficient administration of the internal revenue laws."

.04 Section 1.6033-2(g)(1) of the regulations provides a partial list of organizations that are not required to file annual returns either because they are excepted by statute or because the Commissioner has exercised the authority referred to above in Sec. 2.03. A more complete list is contained in Rev. Proc. 83-23, 1983-1 C.B. 687.

.05 Notice 84-2 contains a list of church-affiliated organizations that are excused from filing Form 990 for tax years beginning after December 31, 1975. Generally, these are organizations that carry out church-related financing, funding, and pension programs. The organizations listed in Notice 84-2 have been excused from filing under the Commissioner's discretionary authority under section 6033(a)(2)(B) of the Code.

.06 From time to time, the Commissioner may excuse organizations from filing Form 990 returns by publishing an announcement in the Internal Revenue Bulletin, or by revising the instructions accompanying Form 990, amending the regulations, or other appropriate publication.

SEC. 3. ORGANIZATIONS EXCUSED FROM FILING

For tax years beginning after December 31, 1975, an organization that is described in sections 501(c)(3) and 509(a)(1), (2), or (3) of the Code, that is affiliated with a church or convention or association of churches as defined in Sec. 4, and that meets the internal support requirement of Sec. 5 of this revenue procedure will not be required to file Form 990.

SEC. 4. AFFILIATED WITH A CHURCH OR CONVENTION OR ASSOCIATION OF CHURCHES

For purposes of Sec. 3, an organization is affiliated with a church or a convention or association of churches if:

1 The organization is covered by a group exemption letter under Rev. Prov. 80-27, 1980-1 C.B. 677, or subsequent revision; or

2 The organization is operated, supervised, or controlled by or in connection with, as defined in section 1.509(a)-4 of the regulations, a church or convention or association of churches; or

3 Relevant facts and circumstances show that it is so affiliated. The factors to be considered include:

(a) The organization's enabling instrument (corporate charter, trust instrument, articles of association, constitution, or similar document) or by-laws affirm that the organization shares common religious doctrines, principles, disciplines, or practices with the church or convention or association of churches.

(b) The church or convention or association of churches has authority to appoint or remove or to control the appointment or removal of at least one of the organization's officers or directors.

(c) The church or convention or association of churches receives reports, at least annually, on the financial and general operations of the organization.

(d) The corporate name of the organization indicates an institutional relationship, which relationship is affirmed by the church or convention or association of churches or a designee thereof; or if the corporate name of the organization does not indicate an institutional relationship, this institutional relationship is affirmed by the church, or convention or association of churches, or designee thereof.

(e) In the event of dissolution, the assets are required to be distributed to the church or convention or association of churches or to an affiliate thereof within the meaning of this revenue procedure.

(f) Any other relevant fact or circumstance.

The absence of one or more of the above factors does not necessarily preclude classification of an organization as being affiliated with a church or convention or association of churches.

SEC. 5. INTERNAL SUPPORT REQUIREMENT

For purposes of Sec. 3, an organization is internally supported within the meaning of this section *unless* it both:

1 offers admissions, goods, services, or facilities for sale, other than on an incidental basis, to the general public (except goods, service, or facilities sold at a nominal charge or substantially less than cost), and

2 normally receives more than 50 percent of its support from a combination of governmental sources; public solicitation of contributions (such as through a community fund drive); and receipts from the sale of admissions, goods, performance of services, or furnishing of facilities in activities that are not unrelated trades or businesses.

SEC. 6. SPECIAL RETURN FILING PROCEDURES

Any section 501(c)(3) church-affiliated organization that failed to file a required return on Form 990 for any tax year ending on or before December 31, 1986, but which files such return or returns on May 15, 1987, on the basis of this revenue procedure, will not be subject to a late filing penalty under section 6652(d)(1) of the Code. Such return should be marked at the top, "Filed under Rev. Proc. 86-23."

SEC. 7. EFFECT ON OTHER DOCUMENTS

.01 Rev. Proc. 83-23 is hereby supplemented.

.02 Notice 84-2 is hereby superseded because the organizations it excuses from filing are excused from filing under this revenue procedure.

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26 CFR 601.602: Forms and instructions.
(Also Part I, Sections 6011, 6041, 6047, 6051, 6071, 6081, 6091; 1.6041-1, 1.6047-1, 31.6051-1, 31.6051-2, 31.6071(a)-1, 31.6081(a)-1.)

Rev. Proc. 86-24

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to state the requirements of the Internal Revenue Service (IRS) and the Social Security Administraiton (SSA) relating to substitutes for Form W-2, Wage and Tax Statement, Form W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay or IRA Payments, and Form W-3, Transmittal of Income and Tax Statements. This revenue procedure also contains general rules for filing Forms W-2, W-2P, and W-3. The IRS provides a six-part Form W-2 and W-2P set. The official Form W-3 is provided as a two-part set.

.02 This revenue procedure supersedes Rev. Proc. 85-20, 1985-1 C.B. 521.

SEC. 2. GENERAL RULES FOR FILING FORMS W-2 AND W-2P

.01 *Employers and payers* (hereafter and where applicable collectively referred to as payers) must use magnetic media for filing tax year (TY) 1986 Forms W-2 (Copy A) and W-2P (Copy A) data with the SSA if the payer files 500 or more of these forms (for TY 1987 magnetic media filing will be required for payers who file 250 or more forms). Requests for additional information concerning magnetic media filing should be directed to the appropriate Regional SSA Magnetic Media Coordinator. Exhibit N contains the addresses and telephone numbers of these coordinators. If filing on magnetic media will result in an undue hardship a waiver of the requirement for one year may be requested from the IRS. Waiver requests for TY 86 should be addressed to: Magnetic Media Reporting, National Computer Center, P.O. Box 1359, Martinsburg, WV 25401-1359. Requests must be submitted by June 30, 1986. Payers who do not comply with the magnetic media requirements and who are not granted a waiver will be subject to a failure to file penalty of $50 per Form W-2/W-2P up to a maximum of $50,000 per calendar year. Since many states and localities accept Forms W-2 and W-2P data on magnetic media, savings may be obtained if magnetic media is used for filing with both the SSA and state or local agencies. Magnetic media users can design their own statements to give to employees, pensioners, annuitants, recipients of retired pay, recipients of IRA (Individual Retirement Account) payments, and recipients of disability income (hereafter and where applicable collectively referred to as payees). Statements designed by payers *must* comply with the requirements of Sections 5, 7, 8 and 9 shown below.

.02 The following Technical Information Bulletins (TIB) contain the specifications and procedures for filing Forms W-2 (Copy A) and W-2P (Copy A) data on magnetic media directly with SSA.

1 TIB-4a—"Magnetic Tape Reporting, Submitting FICA Wage and Tax Data to the Social Security Administration" Form W-2 (Copy A);

2 TIB-4b—"Magnetic Tape Reporting, Submitting Annuity, Pension, Retired Pay or IRA Payments to the Social Security Administration" Form W-2P (Copy A);

3 TIB-4c—"Diskette Reporting, Submitting FICA Wage and Tax Data to the Social Security Administration" Form W-2 (Copy A).

Copies of these publications are available by writing any IRS Service Center; IRS District Office; and SSA, (Reports Preparation Section, P.O. Box 2317, Baltimore, Maryland 21203); or by contacting the Regional SSA Magnetic Media Coordinator.

.03 Payers not using magnetic media must file Copy A of Form W-2 or Copy A of Form W-2P with SSA on either an official form or a privately printed substitute paper form meeting the specifications shown below.

.04 Payers using magnetic media are cautioned to obtain the most recent Technical Information Bulletins and supplements due to possible changes in the specifications and procedures.

SEC. 3. GENERAL RULES FOR FILING FORM W-3

.01 Employers and payers (hereafter and where applicable collectively referred to as payers) required to file Forms W-2 or W-2P must transmit Forms W-2 or W-2P with Form W-3.

.02 Form W-3 must be the same width (i.e. 7 inches, 7.5 inches, or 8 inches) as the Forms W-2 or W-2P filed.

.03 Payers using magnetic media must transmit W-2 or W-2P data with Form 6559, Transmitter Report of Magnetic Media Filing, along with either Form 6560, Employer Summary of Form W-2 Magnetic Media Wage Information, or Form 6561, Payer Summary of Form W-2 Magnetic Media Pension Information. SSA will provide these forms to all approved magnetic media filers. Do not transmit W-2 or W-2P magnetic media with a Form W-3.

SEC. 4. PAPER SUBSTITUTES FOR FORMS W-2 (COPY A), W-2P (COPY A), AND W-3

.01 Paper substitutes *conforming* to the specifications contained in this revenue procedure should be privately printed without the prior approval of the IRS. Proposed substitutes *not conforming totally* to these specifications are not acceptable.

.02 Forms W-2, W-2P, and W-3 are subject to annual review and possible change. Payers are cautioned against overstocking supplies of privately printed substitutes.

.03 Copies of the official form for the reporting year may be obtained from any IRS office. The IRS provides only cut sheet sets with no carbon interleaves for Forms W-2, W-2P, and W-3.

.04 Substitute Forms W-2, W-2P, and W-3 transmitted to the SSA should generally contain only data provided to payees and summary data as requested by the forms' instructions.

.05 Substitute Forms W-2, W-2P, and W-3 may be redesigned as to the spacing for state and local tax data *as long* as the vertical and horizontal spacing for all federal payment and data boxes are in compliance with the specifications contained herein.

.06 All ballot boxes on Forms W-2 (Copy A), W-2P (Copy A), and W-3 must be 8-point boxes.

NOTE: More than 50% of the applicable ballot box must be covered by an "X".

SEC. 5. REQUIREMENTS FOR SUBSTITUTE FORMS FURNISHED TO PAYEES (COPIES B, C, AND 2 OF FORMS W-2 AND W-2P)

.01 All payers, including those filing Copy A using magnetic media, must furnish payees with at least two statements. The dimensions of these copies may be expanded from the dimensions of the official form to allow space for conveying additional information such as withholding from pay for health insurance, union dues, bonds, charity, etc. This may permit the payer to eliminate other statements or notices which would otherwise be furnished to payees. The maximum allowable dimensions are:

1 depth should be no more than five inches;

2 width no more than eight inches.

.02 The paper for all copies should be white. The substitute Copy B (or its equal), that payees are instructed to attach to their Federal income tax return, must be at least 24-pound paper (basis 17 × 22–500), while the other copies furnished the payee should be at least 18-pound paper (basis 17 × 22–500).

.03 Chemical transfer paper is *permitted* only if the following standards are met:

1 All copies must be clearly legible;

2 All copies must have the capability to be photocopied;

3 Fading must not be of such a degree as to preclude legibility and the ability to photocopy.

In general, black chemical transfer inks are preferred; other colors are permitted only if the above standards are met. "Spot carbons" are *not permitted.*

.04 Interleaved carbon must meet the requirements specified in .03 above.

NOTE: chemical transfer paper is permitted for additional payee copies.

.05 Substitute forms for payees need contain only the payment boxes and captions that are applicable (in any desired sequence). Other boxes contained on the official form may be omitted, except that in all cases the payee name, address, social security number and the year must be present. Payment boxes and captions that are applicable must be clearly identified, using where possible the same wording as on the official form. On Form W-2, Copy B, payers *are required* to identify the amount of Federal income tax withheld as "Box 9" and the amount of Wages, tips, other compensation as "Box 10." On Form W-2P, Copy B, payers *are required* to identify the taxable amount as "Box 10" and the amount of Federal income tax withheld as "Box 11." These payment boxes on Copy B *are required* to be outlined in bold 2-point rule (see Exhibit M) or identified in some manner to distinguish these boxes from the rest of the form. If the form contains additional data (e.g., savings bonds withholding, retirement withholding, payroll savings, etc.), there should be a special highlighting of the areas pertaining to (1) Federal income tax withheld, (2) Wages, tips, and other compensation, and (3) Advance EIC payment.

.06 For substitute forms for payees (Copies B, C, and 2 of Forms W-2 and Copies B, C, and 2 of Forms W-2P), the following requirements must be met:

1 All copies of Forms W-2 and W-2P must show both the form number, form title and the year. The title of Form W-2 is "Wage and Tax Statement" The title of Form W-2P is "Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments."

2 If the substitute forms are *not labelled* as to the disposition of the copies, then written notification must be provided to each payee as specified below:

(a) The first copy of the form should be filed with the employee's (or recipient's) Federal tax return.

(b) The second copy of the form should be for the employee's (or recipient's) records.

(c) If applicable, the third copy of the form should be filed with the employee's state, city, or local income tax return.

3 If the substitute forms are *labelled*, then the forms must contain the applicable description.

(a) "Copy B, to be filed with employee's Federal tax return", "Copy C, for employee's records", and the designation "Form W-2 Department of the Treasury—Internal Revenue Service", or

(b) "Copy B, file with recipient's Federal tax return", "Copy C, for recipient's records", and the designation "Form W-2P Department of the Treasury—Internal Revenue Service".

(c) The reference to the Department of the Treasury—Internal Revenue Service should be omitted from other copies provided in the set.

4 Instructions similar to those contained on the back of Copy C of the official form should be provided to each employee (recipient). For Form W-2, the Social Security (FICA) rates applicable for the current tax year must:

(a) appear either on the front or the back of the copy (Copy C) retained by the employee; or

(b) be communicated to the employee via a separate statement.

Note: If you are a Federal employer, you must provide the current rate for hospital insurance benefits (Medicare) for Federal employees.

5 Such substitutes are acceptable and payees should be advised that substitute wage and tax statements are acceptable for filing with their Federal income tax returns.

SEC. 6. REQUIREMENTS FOR SUBSTITUTE "PRIVATELY PRINTED" FORMS W-2 (COPY A), FORMS W-2P (COPY A), AND FORMS W-3 THAT PAYERS SUBMIT TO THE SSA

.01 Payers may file privately printed substitute Forms W-2 and W-2P with the SSA (hereafter referred to as a substitute Copy A). Payers may file privately printed substitute Forms W-3 with the SSA (hereafter referred to as a substitute W-3). The substitute form must be an exact replica of the official repro-proof with respect to layout and contents because it will be read by machines. Spot carbons are *not permitted* for Copy A or for Form W-3 filed with SSA. The dimensions of a substitute form may differ as far as width (see

Section 6.05 below) and the printing of the Government Printing Office (GPO) symbol must be deleted (see Section 6.12 below). The specifications and allowable tolerances for the Copy A of substitute Forms W-2 and W-2P are provided in Exhibits A, B, D, E, F, and G respectively. The specifications and allowable tolerances for Forms W-3 are provided in Exhibits C, H, and I.

NOTE: *Printers of Forms W-2 or W-2P that are wider than 7 inches must provide Forms W-3 that are of the same width as the Forms W-2 or W-2P (i.e., 7 1/2" width Forms W-3 with 7 1/2" width Forms W-2 or W-2P; 8" width Forms W-3 with 8" width Forms W-2 or W-2P).*

.02 Color and quality of paper.

Paper for Copy A and for Form W-3, (cut sheets and continuous pinfeed forms), to be filed with SSA, as specified by JCP 0-25, dated November 29, 1978, must be: White 100% bleached chemical wood, optical character recognition (OCR) bond produced in accordance with the following specifications:

NOTE: Reclaimed fiber in any percentage is permitted, provided the requirements of this standard are met.

1 Acidity: pH value, average,
 not less than 4.5
2 Basis Weight 17 × 22
 1000 cut sheets 32-40
 Metric equivalent grams
 per. sq. meter 75
 A Tolerance of ±5 pct.
 shall be allowed.
3 Stiffness: Average, each
 direction, not less
 than—Gurley miligrams
 ____cross direction 50
 ____machine direction ... 80
4 Tearing strength: Average,
 each direction, not less
 than—grams 40
5 Opacity: Average, not less
 than—percent 82
6 Thickness: Average—
 inch —0.0038
 Metric equivalent—
 mm —0.097
 A tolerance of +0.0005 inch (0.0127 mm) shall be allowed. Paper shall not vary more than 0.0004 inch (0.012 mm) from one edge to the other.
7 Porosity: Average, not less
 than—seconds 10
8 Finish (smoothness): Average,
 each side—seconds 20–55
 For information only,
 the Sheffield
 equivalent—units 170-d100
9 Dirt: Average, each side,
 not to exceed—parts
 per million 8

.03 All printing will be in red OCR dropout ink, as specified, except for the '22222', '55555', or '33333' at the top of the form and the descriptive information at the bottom (see Exhibits J, K, and L) which will be printed in nonreflective black ink. All other printing will be in red OCR dropout ink with or comparable to the specifications below. The screened area of any substitute form (Copy A of Form W-2 and W-2P, and the Form W-3 that is sent to SSA) should generally correspond to that present on the official form. Vertical rules require screening of .05 inches on each side of an inside rule. Horizontal screening should follow the standard format and allow for typewriter spacing. All screened areas are printed in the red OCR dropout ink. The numbered captions are printed as a solid with no screened background. (See Exhibits) Sinclair and Valentine (U.S.) red OCR dropout ink number J-25083 is the preferred ink because it is easier for the forms preparer to read. However, the following inks may be used until your present supply is exhausted:

Ink Manufacturer	Red Ink Identification No.
Gans Ink Co.	CS-310
General Printing Inks Div. (Sun Chemical Corp.)	SS-40B
Ink Masters, Inc. (Chicago)	B-6056
Inmont Canada, Ltd.	4T-39605
Lorilleux Lefranc	U-17410
Sinclair & Valentine (U.S.)	J-24893
Toyo Ink Company	OMB-57

Printing in any other red OCR dropout ink must be cleared by contacting Manager of Media Support, Recognition Equipment, Inc., P.O. Box 660204, Dallas, Texas 75266; telephone number (214) 579-6088.

.04 Typography—Type must be substantially identical in size and shape with corresponding type on the official form. NOTE: The form identifying number must be in OCR A Font.

1 On Copy A of Forms W-2 and W-2P and for Form W-3, all the perimeter rules must be 1-point (0.014 inch), while all other rules must be one-half point (0.007 inch).

2 Vertical rules must be parallel to the left edge of the document; horizontal rules parallel to the top edge.

.05 Dimension—Three official Forms W-2, W-2P (Copy A) or one official Form W-3 are contained on a single page which is 7 inches wide (exclusive of any snap-stubs) by 11 inches deep. The width of privately printed substitute pages must be 7 inches, 7 1/2 inches, or 8 inches exclusive of any left or right snap-stubs, or pin-feed holes, although adherence to the size of the official page is preferred. If a 7 inch form is produced, the image must be an exact copy of the official repro-proof. If the width of the substitute page is increased, the width of specified fields on the substitute page must be increased in accordance with Exhibits D, E, F, G, H, and I. The top margins and the right margin must be 1/4 inch plus or minus .0313 inch and must be free of all printing. For Forms W-2, W-2P and W-3 the combination width of Box 1, "Control number", and the box containing the form identifying number must always be 2.2 inches.

1 When the width of Copy A is increased to 8 inches, exclusive of any left or right snap-stubs or pin-feed holes, the form identifying number must be shown as 222 for Form W-2, 555 for Form W-2P, or 333 for form W-3. This number tells the scan equipment used by SSA which information document it is reading, the width size and the position of individual data fields (see Exhibits D, F, and H).

2 When the width of Copy A is increased to 7 1/2 inches, exclusive of any left or right snap-stubs or pin-feed holes, the form identifying number must be shown as 2222 for Form W-2, 5555 for Form W-2P, or 3333 for Form

W-3. This number tells the scan equipment used by SSA which information document it is reading, the width size and the position of individual data fields (see Exhibits E, G, and I).

.06 The depth of the individual image on a page (for Form W-2 and W-2P) must be the same (3 2/3 inches) as that of the official reproproof. The depth of the Form W-3 on a page must be 3.37 inches.

.07 The words *"Do Not Cut or Separate Forms on This Page"* must be printed in red OCR dropout ink between the three forms W-2 or W-2P (Copy A) (see Exhibits A and B) and must also be present on 7 1/2 inch and 8 inch wide substitute Forms W-2 or W-2P. Perforations are required on all copies (except Copy A) to enable the separation of individual forms.

.08 The words "For Paperwork Reduction Act Notice, see back of Copy D" *must* be printed on the Forms W-2 or W-2P (Copy A) (see Exhibits A and B for format and location) and *must* also be present on 7 1/2 inch and 8 inch wide substitute Forms W-2 or W-2P.

.09 The OMB Number *must* be printed on *each* ply of Form W-2, W-2P, and W-3 (see Exhibits A, B, and C for format and location) and *must* also be present on 7 1/2 inch and 8 inch wide substitute Forms W-2, W-2P, or W-3.

.10 The words *"Please return this entire page to the Social Security Administration address for your State as listed below"* as well as the list of SSA addresses *must* be printed on all Forms W-3 (see Exhibit C) whether Forms W-3 are 7 inches wide, 7 1/2 inches wide, or 8 inches wide.

.11 The Paperwork Reduction Act Notice must be printed on Form W-3 (see Exhibit C for format and location) whether Forms W-3 are 7 inches wide, 7 1/2 inches wide, or 8 inches wide.

.12 *Privately printed continuous substitute Forms W-2 and W-2P (Copy A) must be perforated at each 11" (3-on) page depth. No perforations are allowed between the 3 2/3" forms on a single copy page of Copy A.*

NOTE: Perforations are required between all the other individual copies (Copy 1, B, C, 2, and D) included in the set.

.13 The back of a substitute Copy A must be free of all printing.

.14 Spot carbons are *NOT permitted* for Copy A of Forms W-2 or W-2P or for Form W-3. Interleaved carbon must be of good quality to assure legibility of information on all parts to preclude smudging, and should be black (see Section 5.04).

.15 The use of "chemical transfer paper" on Copy A may be approved after review by IRS and SSA. Submit all requests with a minimum sample of 100 sheets of at least 20-lb. paper (17 × 22–500) to: Internal Revenue Service, Attention: D:R:R:IM, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. The paper will be tested and the results reported to the requester.

.16 Printer's symbol—The GPO symbol must not be placed on substitute Copy A of Forms W-2 and W-2P. In the place of the GPO symbol, the Employer Identification Number (EIN) of the forms printer must be printed in the bottom margin on the face of each individual sheet of Copy A. In addition, the EIN of the forms printer must be printed on the face of the Form W-3 which is filed with SSA.

SEC. 7. ADDITIONAL INSTRUCTIONS

.01 Arrangement of assembly—Except as provided below, if magnetic media is not used for filing with SSA, the substitute copies of Forms W-2 and W-2P assembly should be arranged in the same order as the official Forms W-2 and W-2P. Copy A should be first, followed sequentially by perforated sets (Copies 1, B, C, 2, and D). The substitute form to be filed with SSA by the payer must carry the designation Copy A.

1 Copy D for Employer or Payer. It is not required that privately printed substitute forms contain a copy to be retained by payers although payers must be prepared to verify or duplicate this information if it is requested by the IRS or SSA.

(a) If Copy D *is provided* for the employer or payer, instructions contained on the back of Copy D of the official form *must* appear on the back of the substitute form Copy D.

(b) If Copy D *is not provided* for the employer or payer, instructions contained on the back of Copy D of the official form *must* be furnished on a separate statement to the employer or payer.

2 Additional Copies. Except as provided in the arrangement of the official assemblies, additional copies which may be prepared by papers shall not be placed ahead of the copy "For employee's records," Copy C (Form W-2) or "For Recipient's Records," Copy C (Form W-2P).

3 Notice to Employees. Instructions similar to those contained on the back of Copy C of the official form should be provided to each employee (recipient). For Form W-2, the social security (FICA) rates applicable for the current tax year must:

(a) appear either on the front or the back of the copy (Copy C) retained by the employee; or

(b) be communicated to the employee via a separate statement.

Note: If you are a Federal employer, you must provide the current rate for hospital insurance benefits (Medicare) for Federal employees. The IRS recommends that the other text on the back of the official form Copy C be provided to the employee.

.02 All privately printed Forms W-2 and W-2P (Copy A) must have the tax year printed on the bottom face of each, using identical type to that of the official format.

.03 The substitute Copy B (or its equal), which the payee is instructed to attach to his/her Federal income tax return, must be at least 24-pound paper (basis 17 × 22-500), while the other copies furnished the payee should be at least 18-pound paper (basis 17 × 22-500).

.04 The OCR bond Form W-3 that is filed with SSA must have no printing on the reverse side.

.05 Instructions for Form W-3— Instructions similar to those provided as part of the official form must be provided as part of any substitute Form W-3.

.06 All privately printed Forms W-3 must have the tax year printed on the bottom face of each Form W-3, using identical type to that of the official format.

.07 The copy of the substitute Form W-3 which contains the instructions and is to be retained by the employer should be at least 18-pound paper (basis 17 × 22-500).

SEC. 8. INSTRUCTIONS FOR PAYERS

.01 Only originals or ribbon copies of Copy A of Forms W-2 and W-2P and of Form W-3 may be filed. Carbon copies and photocopies are not acceptable.

.02 The Service requests the cooperation of the payers in typing or machine printing whenever possible and in providing good quality data entries on the forms, i.e., using black ribbon, inserting data in the middle of blocks, well separated from other printing and guidelines, and taking any other measures that will guarantee clear, sharp images. However, payers are not required to acquire equipment solely for the purpose of preparing these forms.

.03 The Employer Identification Number (EIN) may be entered anywhere in Box 2 along with the Payer's name and address on Copy A of Forms W-2 and W-2P. (If this is done, the EIN need not be entered in Box 3 of either Form W-2 or W-2P.) For Forms W-3, the EIN must be entered where prescribed by the Form W-3 Instructions.

.04 The payer's name, address and EIN may be pre-printed.

.05 State agencies—The amounts of wages paid and employee contributions withheld under a State-Federal Agreement, entered into pursuant to Section 218 of the Social Security Act, may be shown in the space on Form W-2 for Social Security Act Wages and Employee Tax. In such cases, the identification number assigned by the Social Security Administration to the state (prefixed by 69) should be shown in the employer name and address area block on Form W-2. This "69" number may be pre-printed.

.06 The optional employer's state number may be pre-printed in the employer's (payer's) name, address, and ZIP code box. If this is done, Box 4 of Forms W-2 and W-2P need not be completed, so long as the applicable state taxing authority does not object.

.07 The preparation and filing instructions for Forms W-2 and W-2P are contained in the 1986 Instructions for Forms W-2 and W-2P. The preparation and filing instructions for Form W-3 are contained as part of the 1986 Form W-3 snap set assembly.

.08 To avoid confusion and questions by payees, payers are encouraged to delete the following items from copies of Forms W-2 and W-2P provided to payees:

(1) Form identifying number (e.g., 22222, 55555);

(2) The words "subtotal" and "void" and their boxes;

(3) Any other captions or box number that would not be of any informational use to payees.

.09 Payers are encouraged to use IRS-supplied labels for affixing to all Forms W-3 filed with SSA.

SEC. 9. OMB REQUIREMENTS

Office of Management and Budget (OMB) Requirements for Substitute Forms

Public Law 96-511 requires: (1) OMB approval of IRS tax forms, (2) that each form (all copies) show the OMB approval number and when appropriate, the form's expiration date, and (3) that the form (or its instructions) state why IRS is collecting the information, how we will use it and whether it must be given to us. The official IRS forms will contain this information.

As it applies to substitute IRS forms this means:

1. All substitute forms (all copies) *must* show the OMB number and any expiration date as they appear on the official IRS form (see Exhibits A, B, and C).

2. The OMB number must be in one or the following formats:

OMB No. 1545-0008 (preferred)
or
OMB #1545-0008

3. You must inform the users of your substitute forms of the reasons for IRS collection, use and requirements, as stated in the instructions for the IRS form.

SEC. 10. REPRODUCTION PROOFS

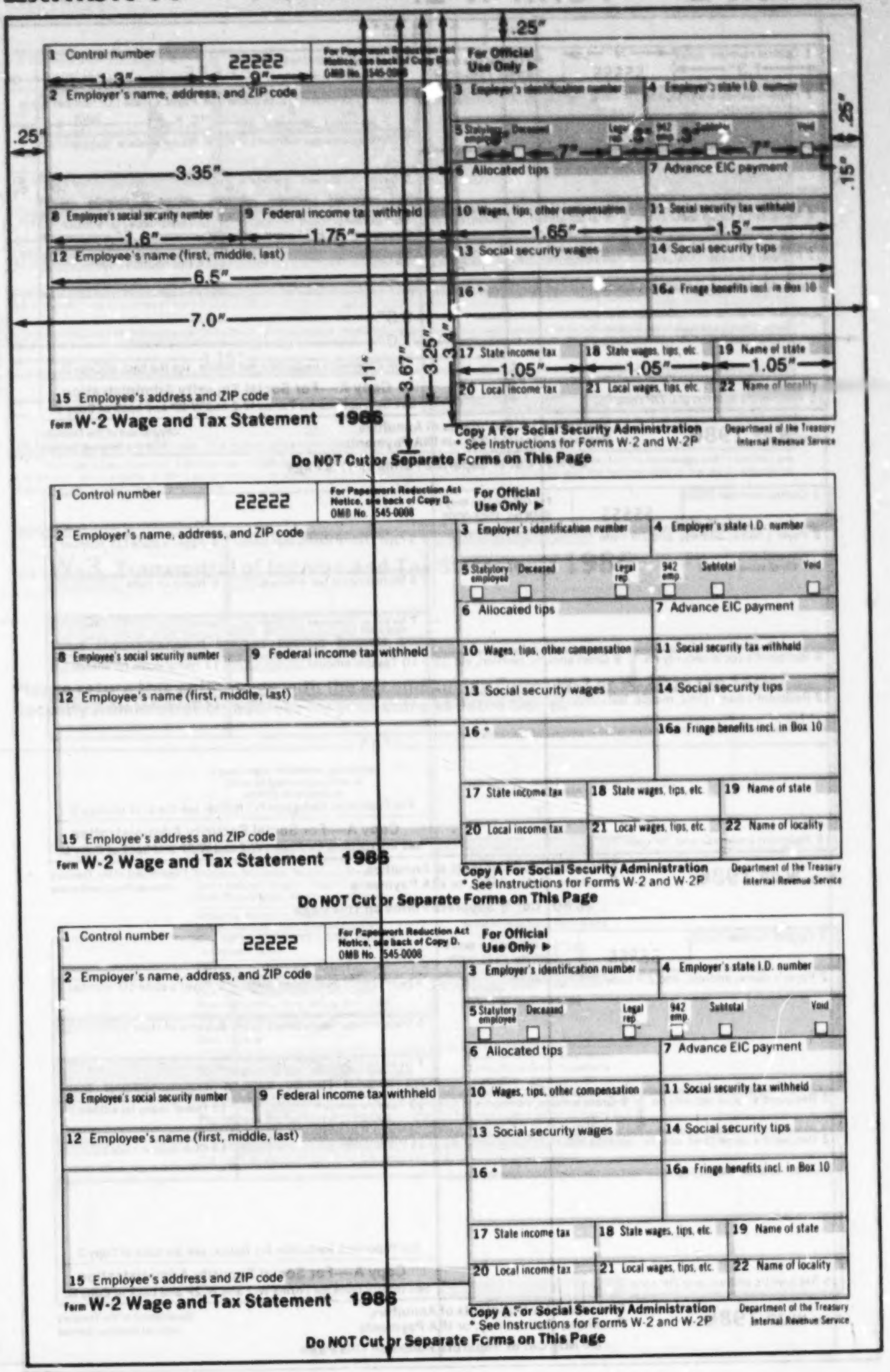
.01 Order blanks for reproduction proofs are mailed annually to requestors of record, and on request to other users. Reproduction copies of Forms W-2 (Copy A), W-2P (Copy A), and W-3 (Page 1) each consists of two parts. Part 1 is line art, i.e., type and ink. Part 2 is a black solid which should be photographically screened by the user to allow a 10%-20% dot pattern when printed in red OCR dropout ink. In some cases where the production method requires the use of something other than a standard dot pattern, the printed value of part 2 must still be 10%-20%. Printers and others wishing to obtain reproduction proofs may send their requests to Internal Revenue Service, Attn: Distribution Manager, PM:S:FM:P—Room 1528, 1111 Constitution Avenue, N.W., Washington, D.C., 20224.

.02 A charge of $1 per page will be made for each reproduction proof regardless of page size. Invoices will be mailed after orders have been filled.

SEC. 11. EFFECT ON OTHER PROCEDURES

Rev. Proc. 85-20, 1985-1 C.B. 521 is superseded.

Exhibit A — Form W-2



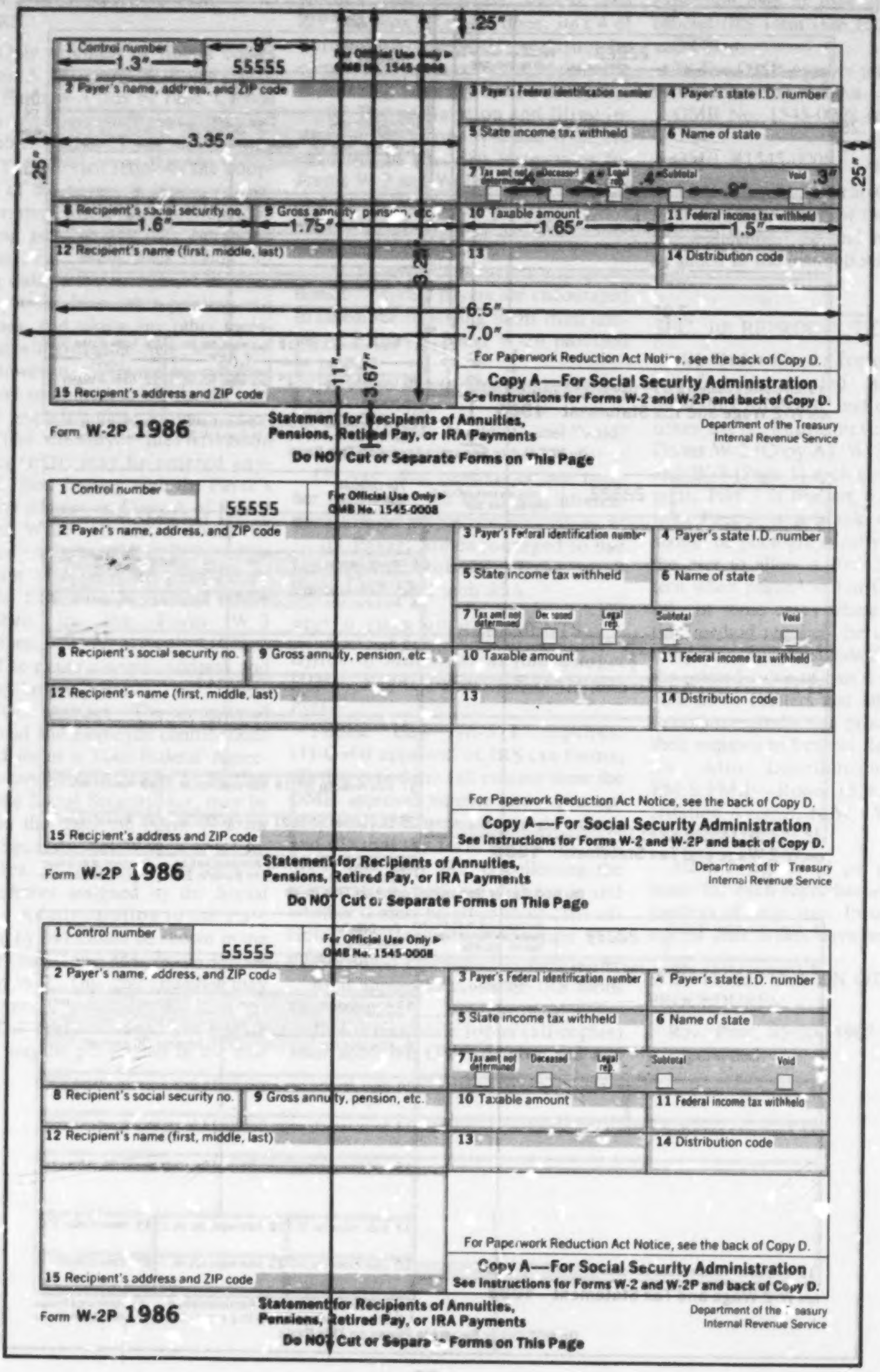
1 Control number
22222
For Paperwork Reduction Act Notice, see back of Copy D. OMB No. 1545-0008
For Official Use Only ►
2 Employer's name, address, and ZIP code
3 Employer's identification number
4 Employer's state I.D. number
5 Statutory employee ☐ Deceased ☐ Legal rep. ☐ 942 emp. ☐ Subtotal ☐ Void ☐
6 Allocated tips
7 Advance EIC payment
8 Employee's social security number
9 Federal income tax withheld
10 Wages, tips, other compensation
11 Social security tax withheld
12 Employee's name (first, middle, last)
13 Social security wages
14 Social security tips
16 *
16a Fringe benefits incl. in Box 10
17 State income tax
18 State wages, tips, etc.
19 Name of state
20 Local income tax
21 Local wages, tips, etc.
22 Name of locality
15 Employee's address and ZIP code
Form **W-2 Wage and Tax Statement 1986**
Copy A For Social Security Administration
* See Instructions for Forms W-2 and W-2P
Department of the Treasury
Internal Revenue Service

Do NOT Cut or Separate Forms on This Page

1 Control number
22222
For Paperwork Reduction Act Notice, see back of Copy D. OMB No. 1545-0008
For Official Use Only ►
2 Employer's name, address, and ZIP code
3 Employer's identification number
4 Employer's state I.D. number
5 Statutory employee ☐ Deceased ☐ Legal rep. ☐ 942 emp. ☐ Subtotal ☐ Void ☐
6 Allocated tips
7 Advance EIC payment
8 Employee's social security number
9 Federal income tax withheld
10 Wages, tips, other compensation
11 Social security tax withheld
12 Employee's name (first, middle, last)
13 Social security wages
14 Social security tips
16 *
16a Fringe benefits incl. in Box 10
17 State income tax
18 State wages, tips, etc.
19 Name of state
20 Local income tax
21 Local wages, tips, etc.
22 Name of locality
15 Employee's address and ZIP code
Form W-2 Wage and Tax Statement 1986
Copy A For Social Security Administration
* See Instructions for Forms W-2 and W-2P
Department of the Treasury
Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

1 Control number
22222
For Paperwork Reduction Act Notice, see back of Copy D. OMB No. 1545-0008
For Official Use Only ►
2 Employer's name, address, and ZIP code
3 Employer's identification number
4 Employer's state I.D. number
5 Statutory employee ☐ Deceased ☐ Legal rep. ☐ 942 emp. ☐ Subtotal ☐ Void ☐
6 Allocated tips
7 Advance EIC payment
8 Employee's social security number
9 Federal income tax withheld
10 Wages, tips, other compensation
11 Social security tax withheld
12 Employee's name (first, middle, last)
13 Social security wages
14 Social security tips
16 *
16a Fringe benefits incl. in Box 10
17 State income tax
18 State wages, tips, etc.
19 Name of state
20 Local income tax
21 Local wages, tips, etc.
22 Name of locality
15 Employee's address and ZIP code
Form W-2 Wage and Tax Statement 1986
Copy A For Social Security Administration
* See Instructions for Forms W-2 and W-2P
Department of the Treasury
Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

Exhibit B — Form W-2P

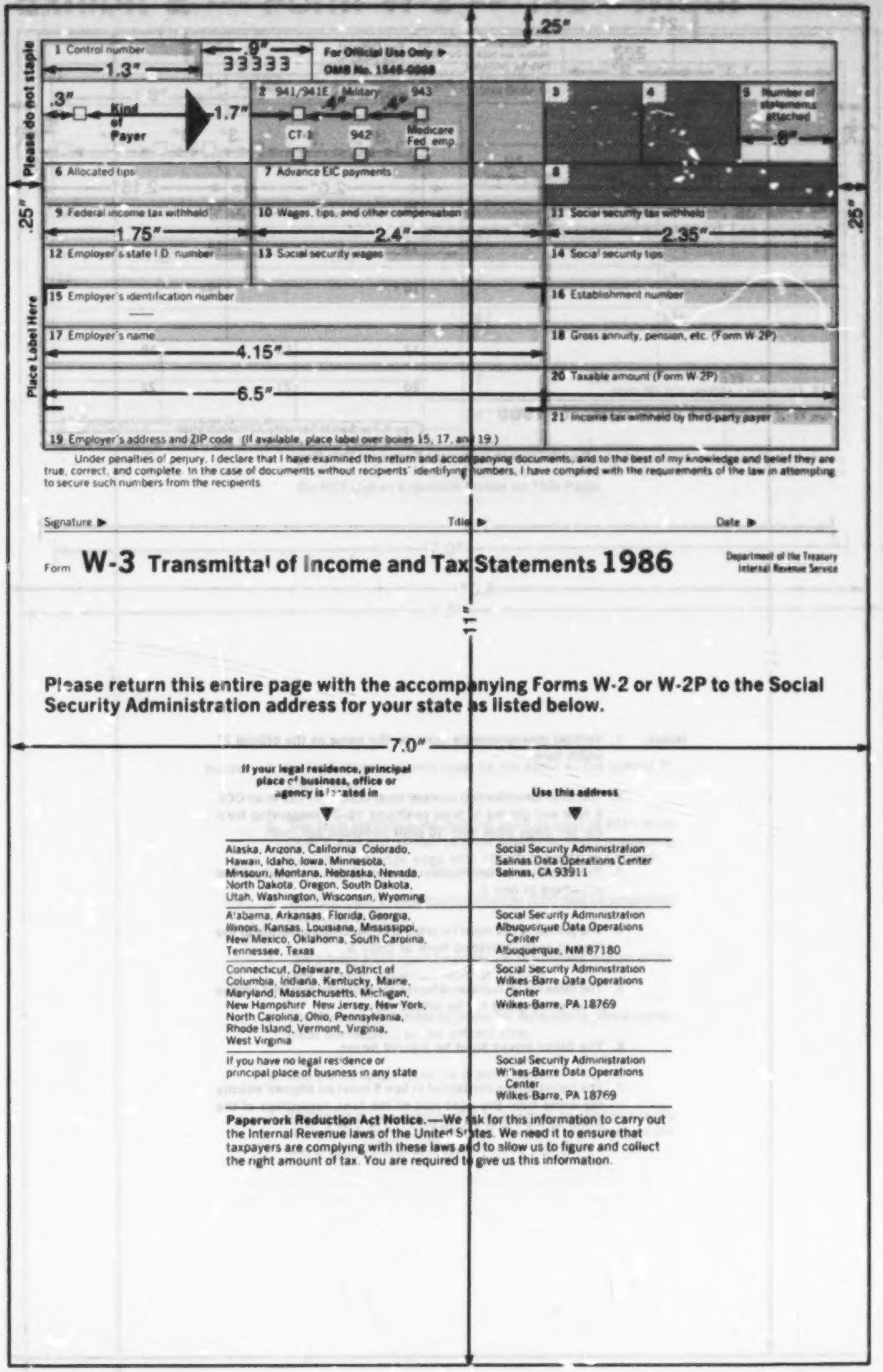


1 Control number
55555
For Official Use Only ▶
OMB No. 1545-0008
2 Payer's name, address, and ZIP code
3 Payer's Federal identification number
4 Payer's state I.D. number
5 State income tax withheld
6 Name of state
7 Tax amt not determined ☐ Deceased ☐ Legal rep. ☐ Subtotal ☐ Void ☐
8 Recipient's social security no.
9 Gross annuity, pension, etc.
10 Taxable amount
11 Federal income tax withheld
12 Recipient's name (first, middle, last)
13
14 Distribution code
15 Recipient's address and ZIP code
For Paperwork Reduction Act Notice, see the back of Copy D.
Copy A—For Social Security Administration
See Instructions for Forms W-2 and W-2P and back of Copy D.
Form **W-2P 1986**
Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments
Department of the Treasury
Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

1 Control number
55555
For Official Use Only ▶
OMB No. 1545-0008
2 Payer's name, address, and ZIP code
3 Payer's Federal identification number
4 Payer's state I.D. number
5 State income tax withheld
6 Name of state
7 Tax amt not determined ☐ Deceased ☐ Legal rep. ☐ Subtotal ☐ Void ☐
8 Recipient's social security no.
9 Gross annuity, pension, etc.
10 Taxable amount
11 Federal income tax withheld
12 Recipient's name (first, middle, last)
13
14 Distribution code
15 Recipient's address and ZIP code
For Paperwork Reduction Act Notice, see the back of Copy D.
Copy A—For Social Security Administration
See Instructions for Forms W-2 and W-2P and back of Copy D.
Form **W-2P 1986**
Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments
Department of the Treasury
Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

1 Control number
55555
For Official Use Only ▶
OMB No. 1545-0008
2 Payer's name, address, and ZIP code
3 Payer's Federal identification number
4 Payer's state I.D. number
5 State income tax withheld
6 Name of state
7 Tax amt not determined ☐ Deceased ☐ Legal rep. ☐ Subtotal ☐ Void ☐
8 Recipient's social security no.
9 Gross annuity, pension, etc.
10 Taxable amount
11 Federal income tax withheld
12 Recipient's name (first, middle, last)
13
14 Distribution code
15 Recipient's address and ZIP code
For Paperwork Reduction Act Notice, see the back of Copy D.
Copy A—For Social Security Administration
See Instructions for Forms W-2 and W-2P and back of Copy D.
Form **W-2P 1986**
Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments
Department of the Treasury
Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

Exhibit C — Form W-3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2.4"
2.35"
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11"
7.0"

Please do not staple

Place Label Here

1 Control number	33333	For Official Use Only ▶ OMB No. 1545-0008	
Kind of Payer	2 941/941E ☐ Military ☐ 943 ☐ CT-1 ☐ 942 ☐ Medicare Fed. emp. ☐	3	4
			5 Number of statements attached
6 Allocated tips	7 Advance EIC payments	8	
9 Federal income tax withheld	10 Wages, tips, and other compensation	11 Social security tax withheld	
12 Employer's state I.D. number	13 Social security wages	14 Social security tips	
15 Employer's identification number		16 Establishment number	
17 Employer's name		18 Gross annuity, pension, etc. (Form W-2P)	
		20 Taxable amount (Form W-2P)	
		21 Income tax withheld by third-party payer	
19 Employer's address and ZIP code (If available, place label over boxes 15, 17, and 19.)			

Under penalties of perjury, I declare that I have examined this return and accompanying documents, and to the best of my knowledge and belief they are true, correct, and complete. In the case of documents without recipients' identifying numbers, I have complied with the requirements of the law in attempting to secure such numbers from the recipients.

Signature ▶ Title ▶ Date ▶

Form **W-3** **Transmittal of Income and Tax Statements 1986**

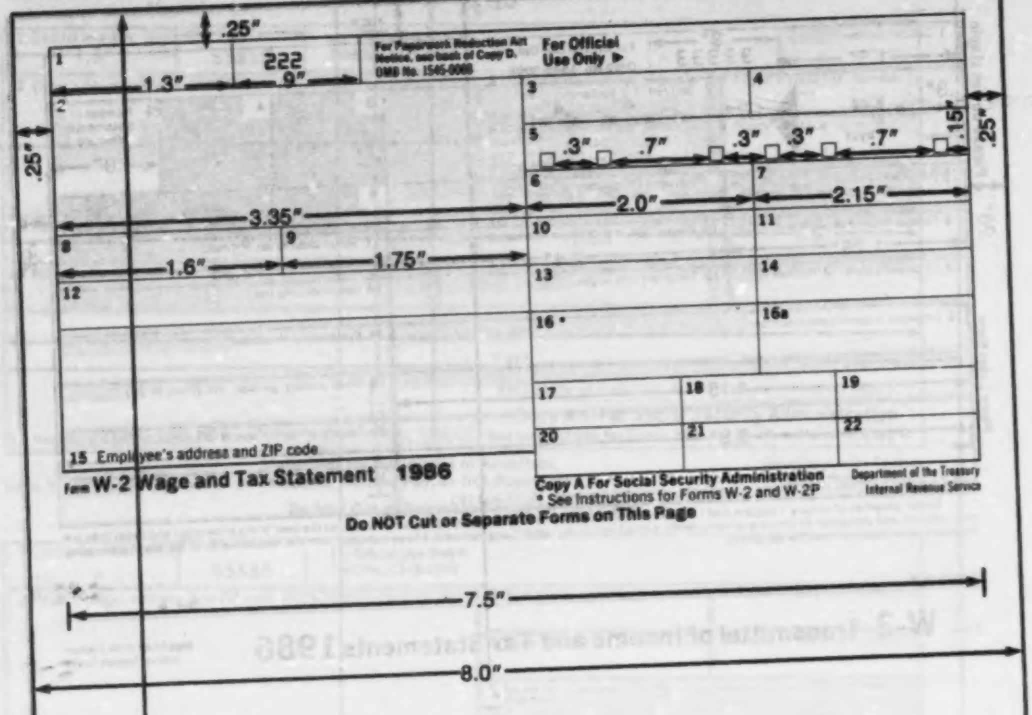
Department of the Treasury
Internal Revenue Service

Please return this entire page with the accompanying Forms W-2 or W-2P to the Social Security Administration address for your state as listed below.

If your legal residence, principal place of business, office or agency is located in ▼	Use this address ▼
Alaska, Arizona, California, Colorado, Hawaii, Idaho, Iowa, Minnesota, Missouri, Montana, Nebraska, Nevada, North Dakota, Oregon, South Dakota, Utah, Washington, Wisconsin, Wyoming	Social Security Administration Salinas Data Operations Center Salinas, CA 93911
Alabama, Arkansas, Florida, Georgia, Illinois, Kansas, Louisiana, Mississippi, New Mexico, Oklahoma, South Carolina, Tennessee, Texas	Social Security Administration Albuquerque Data Operations Center Albuquerque, NM 87180
Connecticut, Delaware, District of Columbia, Indiana, Kentucky, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, Vermont, Virginia, West Virginia	Social Security Administration Wilkes-Barre Data Operations Center Wilkes-Barre, PA 18769
If you have no legal residence or principal place of business in any state	Social Security Administration Wilkes-Barre Data Operations Center Wilkes-Barre, PA 18769

Paperwork Reduction Act Notice.—We ask for this information to carry out the Internal Revenue laws of the United States. We need it to ensure that taxpayers are complying with these laws and to allow us to figure and collect the right amount of tax. You are required to give us this information.

Exhibit D — Form W-2 — 8" Width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222
For Paperwork Reduction Act Notice, see back of Copy D. OMB No. 1545-0008
For Official Use Only ►
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2.15"
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12
13
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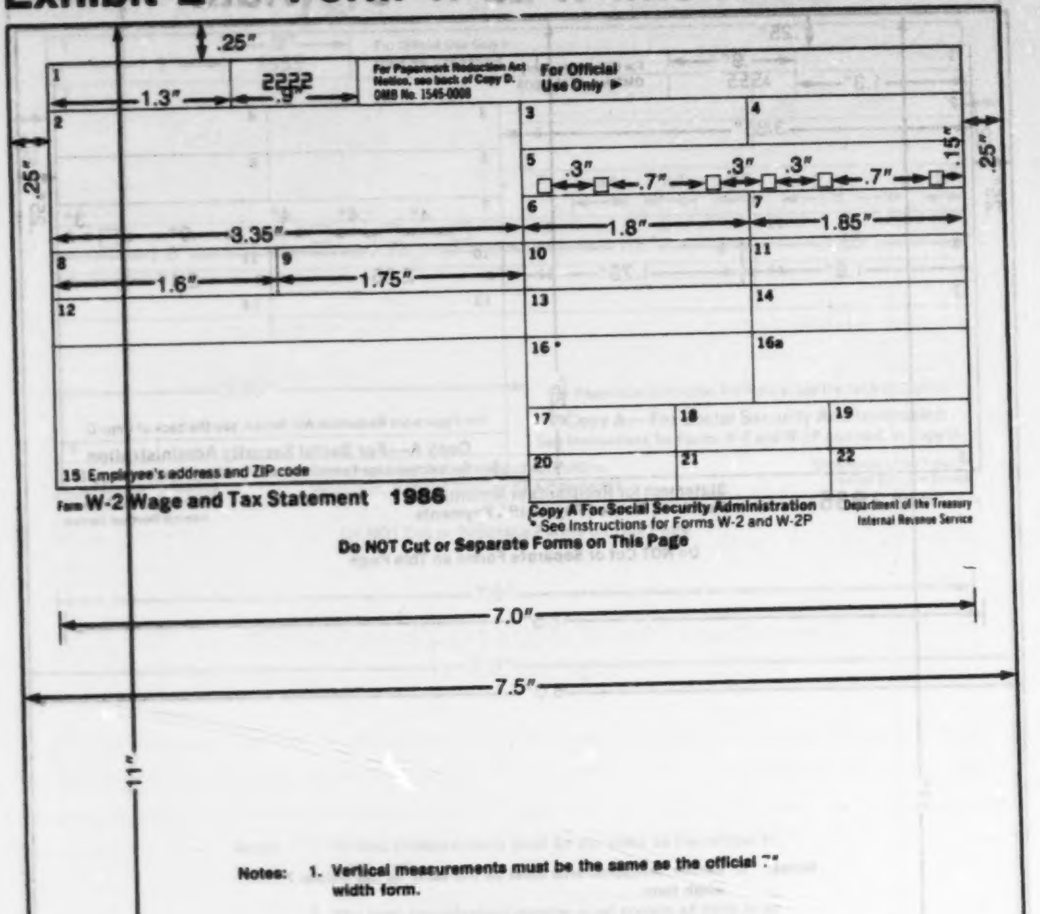
16 *
16a
17
18
19
20
21
22
15 Employee's address and ZIP code
Form W-2 Wage and Tax Statement 1986
Copy A For Social Security Administration
* See Instructions for Forms W-2 and W-2P
Department of the Treasury Internal Revenue Service
Do NOT Cut or Separate Forms on This Page
7.5"
8.0"
11"

Notes:

1. Vertical measurements must be the same as the official 7" width form.
2. The form identification number must consist of 222 in an OCR A font and placed in print positions 19–21 measuring from the left page edge with 10 print positions per inch.
3. The Employer's Identification Number (EIN) may be preprinted anywhere in box 2.
4. The printer's EIN must be printed in the bottom margin of the face of each individual form of Copy A.
5. The titles for all numbered boxes for federally-required entries must correspond to the official form.
6. The ballot boxes must be 8-point boxes.
7. The ballot boxes contained in box 5 must be aligned exactly the same from the right rule of the form regardless of the width of the Form W-2 (i.e., 7", 7½", or 8").

Exhibit E — Form W-2 — 7½″ Width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OMB No. 1545-0008
For Official Use Only ▶
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16a
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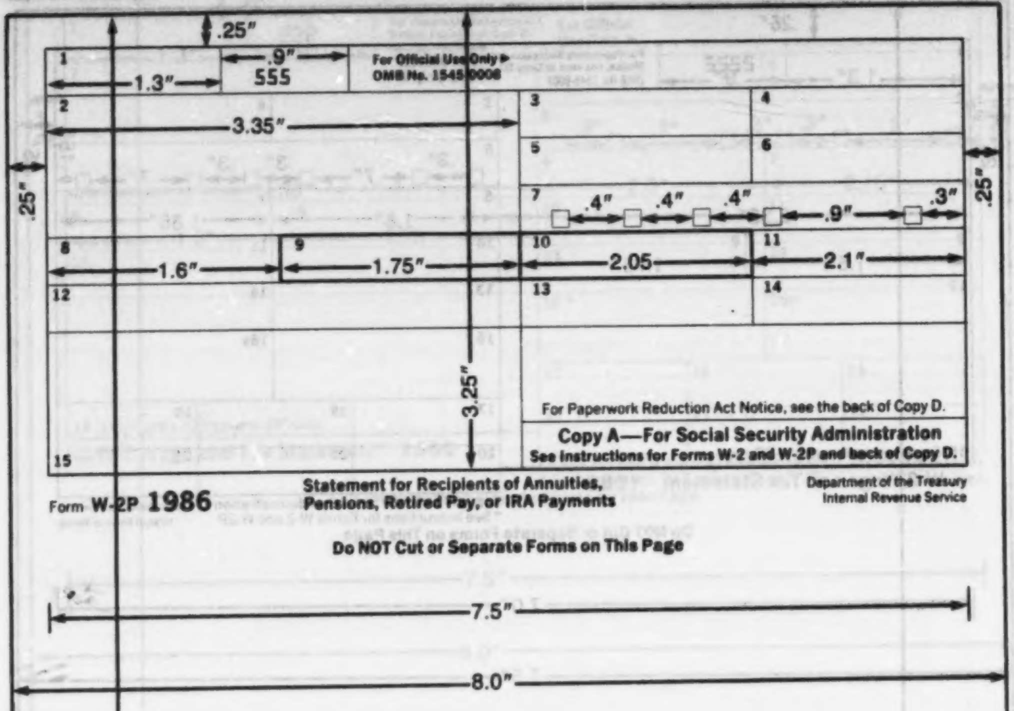
21
22
15 Employee's address and ZIP code
Form W-2 Wage and Tax Statement 1986
Copy A For Social Security Administration
* See Instructions for Forms W-2 and W-2P
Department of the Treasury
Internal Revenue Service
Do NOT Cut or Separate Forms on This Page
7.0″
7.5″
11″

Notes:

1. **Vertical measurements must be the same as the official 7″ width form.**
2. **The form identification number must consist of 2222 in an OCR A font and placed in print positions 19–21 measuring from the left page edge with 10 print positions per inch.**
3. **The Employer's Identification Number (EIN) may be preprinted anywhere in box 2.**
4. **The printer's EIN must be printed in the bottom margin of the face of each individual form of Copy A.**
5. **The titles for all numbered boxes for federally-required entries must correspond to the official form.**
6. **The ballot boxes must be 8-point boxes.**
7. **The ballot boxes contained in box 5 must be aligned exactly the same from the right rule of the form regardless of the width of the Form W-2 (i.e., 7″, 7½″, or 8″).**

Exhibit F — Form W-2P — 8″ Width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For Official Use Only ▶
OMB No. 1545-0008
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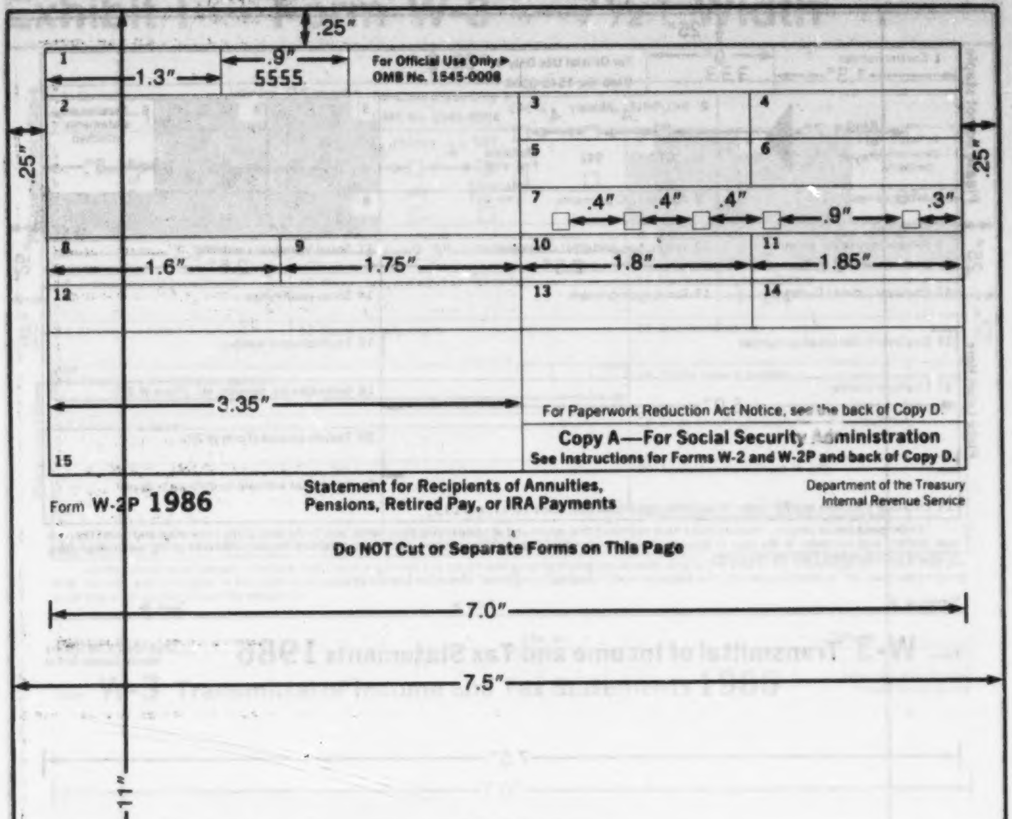
For Paperwork Reduction Act Notice, see the back of Copy D.
Copy A—For Social Security Administration
See Instructions for Forms W-2 and W-2P and back of Copy D.
15
Form W-2P 1986
Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments
Department of the Treasury
Internal Revenue Service
Do NOT Cut or Separate Forms on This Page
7.5″
8.0″
11″

Notes:

1. **Vertical measurements must be the same as the official 7″ width form.**
2. **The form identification number must consist of 555 in an OCR A font and placed in print positions 18–20 measuring from the left page edge with 10 print positions per inch.**
3. **The blank space to the right of box 15 and below boxes 13 and 14 may be used for any additional payee information.**
4. **The Employer's Identification Number (EIN) may be preprinted anywhere in box 2.**
5. **The printer's EIN must be printed in the bottom margin of the face of each individual form of Copy A.**
6. **The titles for all numbered boxes for federally-required entries must correspond to the official form.**
7. **The ballot boxes must be 8-point boxes.**
8. **The ballot boxes contained in box 7 must be aligned exactly the same from the right rule of the form regardless of the width of the Form W-2P (i.e., 7″, 7½″, or 8″).**

Exhibit G — Form W-2P — 7½″ Width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1.3″
.9″
5555
For Official Use Only ▶
OMB No. 1545-0008
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.4″
.4″
.9″
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10
11
1.6″
1.75″
1.8″
1.85″
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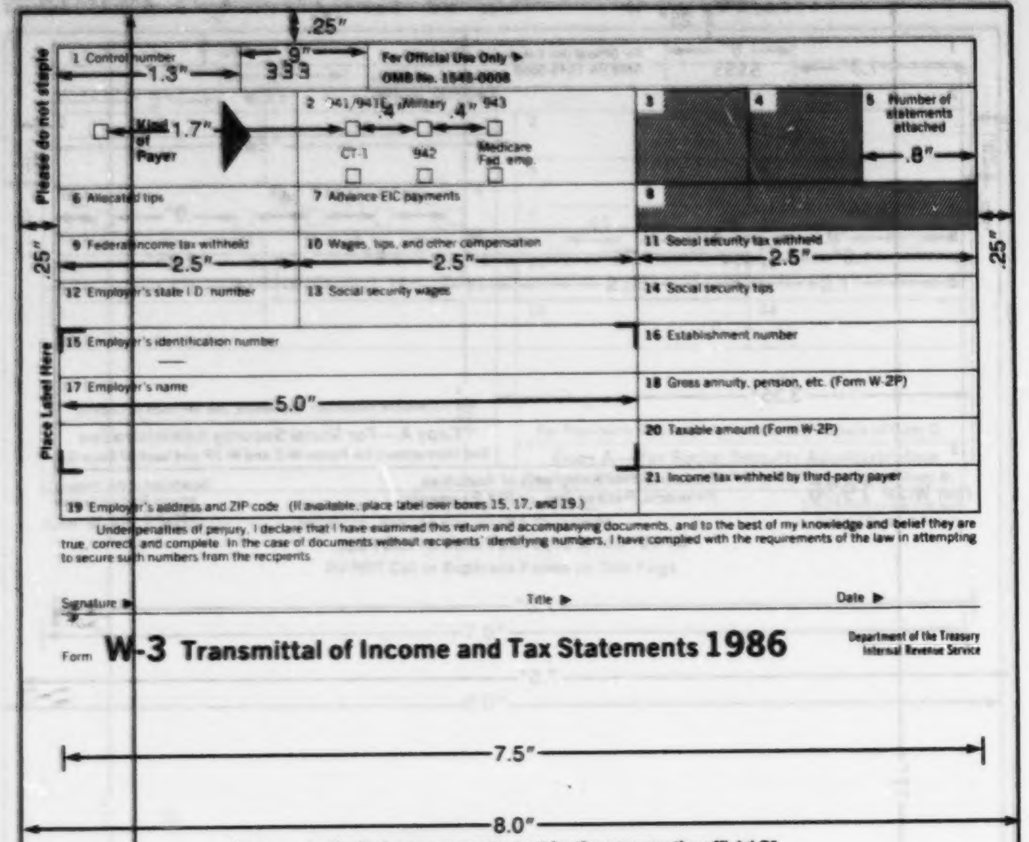
13
14
3.35″
For Paperwork Reduction Act Notice, see the back of Copy D.
Copy A—For Social Security Administration
See Instructions for Forms W-2 and W-2P and back of Copy D.
15
Form W-2P 1986
Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments
Department of the Treasury
Internal Revenue Service
Do NOT Cut or Separate Forms on This Page
7.0″
7.5″
11″

Notes:

1. **Vertical measurements must be the same as the official 7″ width form.**
2. **The form identification number must consist of 5555 in an OCR A font and placed in print positions 18–20 measuring from the left page edge with 10 print positions per inch.**
3. **The blank space to the right of box 15 and below boxes 13 and 14 may be used for any additional payee information.**
4. **The Employer's Identification Number (EIN) may be preprinted anywhere in box 2.**
5. **The printer's EIN must be printed in the bottom margin of the face of each individual form of Copy A.**
6. **The titles for all numbered boxes for federally-required entries must correspond to the official form.**
7. **The ballot boxes must be 8-point boxes.**
8. **The ballot boxes contained in box 7 must be aligned exactly the same from the right rule of the form regardless of the width of the Form W-2P (i.e., 7″, 7½″, or 8″).**

Exhibit H — Form W-3 — 8" Width



Please do not staple

1 Control number

333

For Official Use Only ▶
OMB No. 1545-0008

☐ Kind of Payer

2 941/941E ☐ Military ☐ 943 ☐

CT-1 ☐ 942 ☐ Medicare Fed. emp. ☐

3

4

5 Number of statements attached

6 Allocated tips

7 Advance EIC payments

8

9 Federal income tax withheld

10 Wages, tips, and other compensation

11 Social security tax withheld

12 Employer's state I.D. number

13 Social security wages

14 Social security tips

Place Label Here

15 Employer's identification number

16 Establishment number

17 Employer's name

18 Gross annuity, pension, etc. (Form W-2P)

20 Taxable amount (Form W-2P)

21 Income tax withheld by third-party payer

19 Employer's address and ZIP code (If available, place label over boxes 15, 17, and 19.)

Under penalties of perjury, I declare that I have examined this return and accompanying documents, and to the best of my knowledge and belief they are true, correct, and complete. In the case of documents without recipients' identifying numbers, I have complied with the requirements of the law in attempting to secure such numbers from the recipients.

Signature ▶ Title ▶ Date ▶

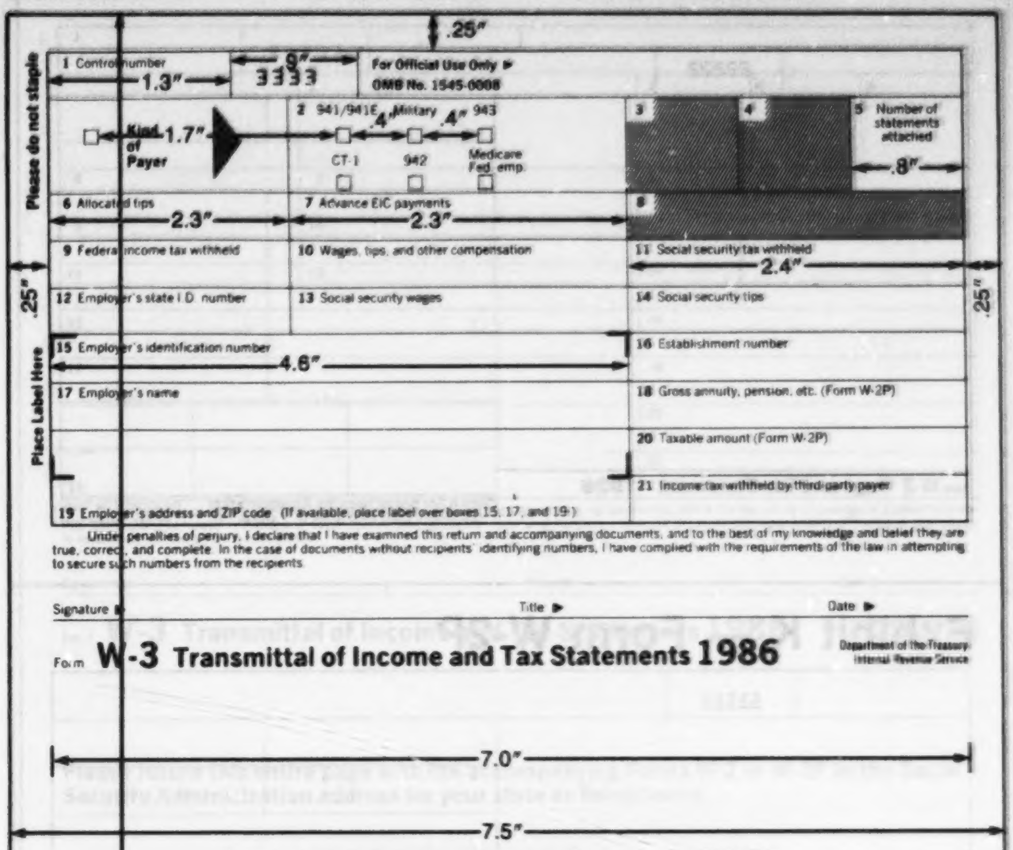
Form **W-3 Transmittal of Income and Tax Statements 1986**

Department of the Treasury
Internal Revenue Service

Notes:

1. **Vertical measurements must be the same as the official 7" width form except the mark sense squares (i.e., ballot boxes) in boxes 2–4 may be moved down to conform to a six line per inch spacing.**
2. **The Form Identification Number must consist of 333 in an OCR A font and placed in print positions 19–21 measuring from the left page edge with 10 print positions per inch.**
3. **The Employer's Identification Number (EIN) may be preprinted anywhere in box 15.**
4. **The printer's EIN must be printed centered below the "signature" line.**
5. **The titles for all numbered boxes must correspond to the official form.**
6. **The ballot boxes must be 8-point boxes.**
7. **The ballot boxes contained in box 2, 3, and 4 must be aligned exactly the same from the right rule of the form regardless of the width of the Form W-3 (i.e., 7", 7½", or 8").**
8. **The words "Please return this entire page to the Social Security Administration address for your State as listed below," and the appropriate SSA addresses must appear on any substitute Form W-3 in the same position as on the official form.**

Exhibit I — Form W-3 — 7½" Width



Please do not staple

Place Label Here

1 Control number	3333	For Official Use Only ▶ OMB No. 1545-0008

☐ Kind of Payer	2 941/941E ☐ Military ☐ 943 ☐ CT-1 ☐ 942 ☐ Medicare Fed. emp. ☐	3	4	5 Number of statements attached
6 Allocated tips	7 Advance EIC payments	8		
9 Federal income tax withheld	10 Wages, tips, and other compensation	11 Social security tax withheld		
12 Employer's state I.D. number	13 Social security wages	14 Social security tips		
15 Employer's identification number		16 Establishment number		
17 Employer's name		18 Gross annuity, pension, etc. (Form W-2P)		
		20 Taxable amount (Form W-2P)		
19 Employer's address and ZIP code (If available, place label over boxes 15, 17, and 19.)		21 Income tax withheld by third-party payer		

Under penalties of perjury, I declare that I have examined this return and accompanying documents, and to the best of my knowledge and belief they are true, correct, and complete. In the case of documents without recipients' identifying numbers, I have complied with the requirements of the law in attempting to secure such numbers from the recipients.

Signature ▶ Title ▶ Date ▶

Form **W-3** **Transmittal of Income and Tax Statements 1986**

Department of the Treasury
Internal Revenue Service

Notes:

1. **Vertical measurements must be the same as the official 7" width form except the mark sense squares (i.e., ballot boxes) in boxes 2–4 may be moved down to conform to a six line per inch spacing.**

2. **The Form Identification Number must consist of 3333 in an OCR A font and placed in print positions 18–21 measuring from the left page edge with 10 print positions per inch.**

3. **The Employer's Identification Number (EIN) may be preprinted anywhere in box 15.**

4. **The printer's EIN must be printed centered below the "signature" line.**

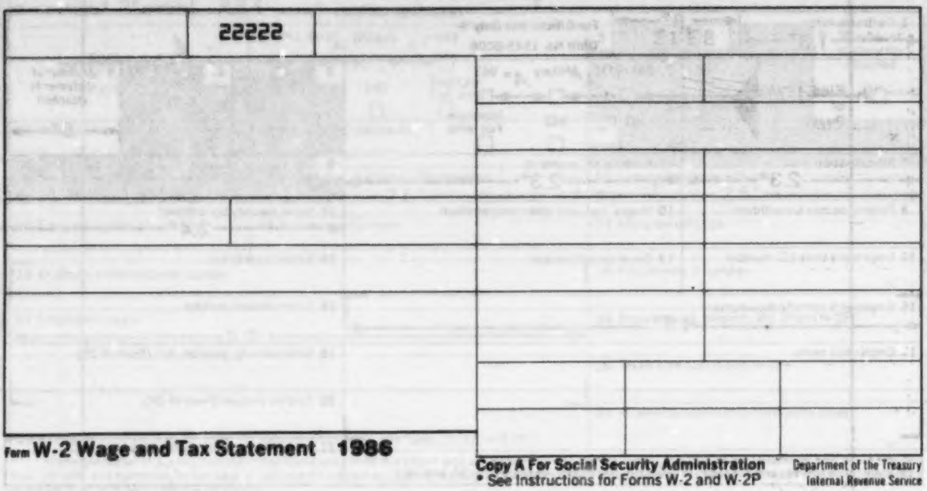
5. **The titles for all numbered boxes must correspond to the official form.**

6. **The ballot boxes must be 8-point boxes.**

7. **The ballot boxes contained in box 2, 3, and 4 must be aligned exactly the same from the right rule of the form regardless of the width of the Form W-3 (i.e., 7", 7½", or 8").**

8. **The words "Please return this entire page to the Social Security Administration address for your State as listed below," and the appropriate SSA addresses must appear on any substitute Form W-3 in the same position as on the official form.**

Exhibit J — Form W-2



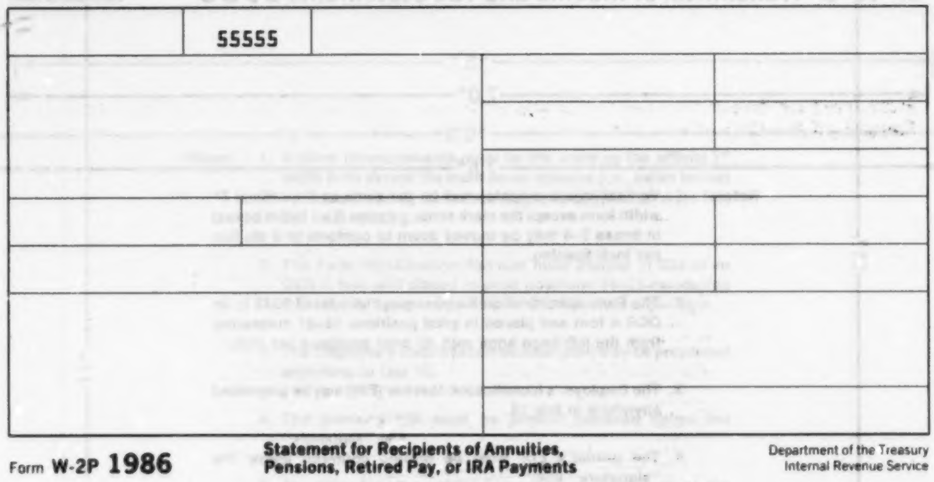
22222

Form W-2 Wage and Tax Statement 1986

Copy A For Social Security Administration
* See Instructions for Forms W-2 and W-2P

Department of the Treasury
Internal Revenue Service

Exhibit K — Form W-2P



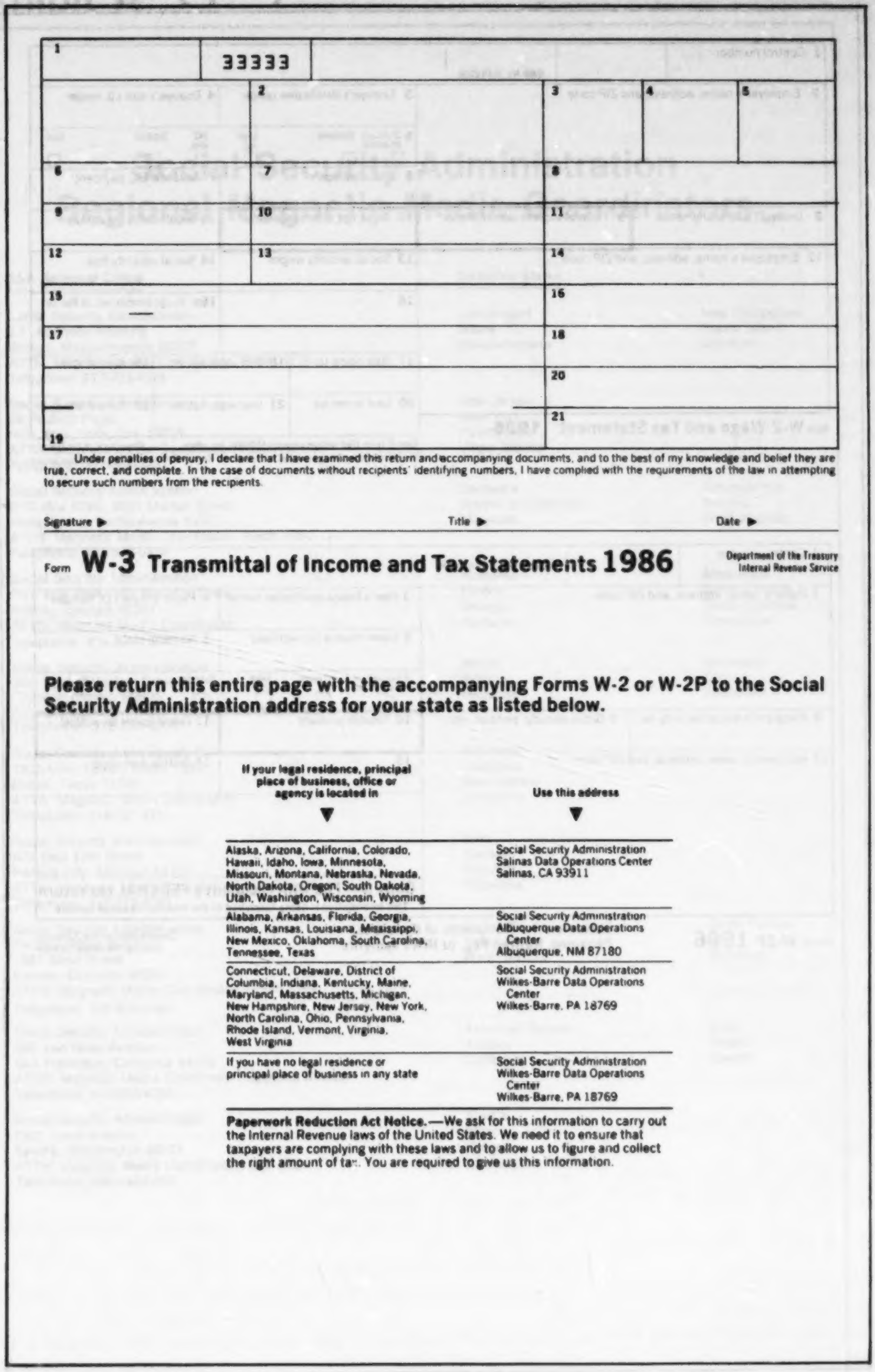
55555

Form W-2P 1986

Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments

Department of the Treasury
Internal Revenue Service

Exhibit L — Form W-3



1	33333				
	2		3	4	5
6	7		8		
9	10		11		
12	13		14		
15 —			16		
17			18		
			20		
— 19			21		

Under penalties of perjury, I declare that I have examined this return and accompanying documents, and to the best of my knowledge and belief they are true, correct, and complete. In the case of documents without recipients' identifying numbers, I have complied with the requirements of the law in attempting to secure such numbers from the recipients.

Signature ▶ Title ▶ Date ▶

Form **W-3 Transmittal of Income and Tax Statements 1986**

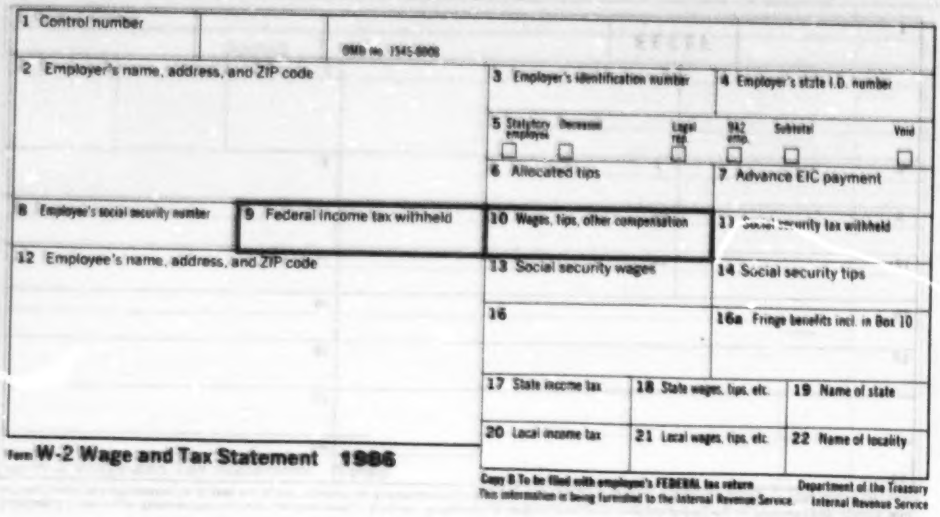
Department of the Treasury
Internal Revenue Service

Please return this entire page with the accompanying Forms W-2 or W-2P to the Social Security Administration address for your state as listed below.

If your legal residence, principal place of business, office or agency is located in ▼	Use this address ▼
Alaska, Arizona, California, Colorado, Hawaii, Idaho, Iowa, Minnesota, Missouri, Montana, Nebraska, Nevada, North Dakota, Oregon, South Dakota, Utah, Washington, Wisconsin, Wyoming	Social Security Administration Salinas Data Operations Center Salinas, CA 93911
Alabama, Arkansas, Florida, Georgia, Illinois, Kansas, Louisiana, Mississippi, New Mexico, Oklahoma, South Carolina, Tennessee, Texas	Social Security Administration Albuquerque Data Operations Center Albuquerque, NM 87180
Connecticut, Delaware, District of Columbia, Indiana, Kentucky, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, Vermont, Virginia, West Virginia	Social Security Administration Wilkes-Barre Data Operations Center Wilkes-Barre, PA 18769
If you have no legal residence or principal place of business in any state	Social Security Administration Wilkes-Barre Data Operations Center Wilkes-Barre, PA 18769

Paperwork Reduction Act Notice.—We ask for this information to carry out the Internal Revenue laws of the United States. We need it to ensure that taxpayers are complying with these laws and to allow us to figure and collect the right amount of tax. You are required to give us this information.

Exhibit M — Form W-2/W-2P (Copy B)



1 Control number

OMB No. 1545-0008

2 Employer's name, address, and ZIP code

3 Employer's identification number

4 Employer's state I.D. number

5 Statutory employee ☐ Deceased ☐ Legal rep. ☐ 942 emp. ☐ Subtotal ☐ Void ☐

6 Allocated tips

7 Advance EIC payment

8 Employee's social security number

9 Federal income tax withheld

10 Wages, tips, other compensation

11 Social security tax withheld

12 Employee's name, address, and ZIP code

13 Social security wages

14 Social security tips

16

16a Fringe benefits incl. in Box 10

17 State income tax

18 State wages, tips, etc.

19 Name of state

20 Local income tax

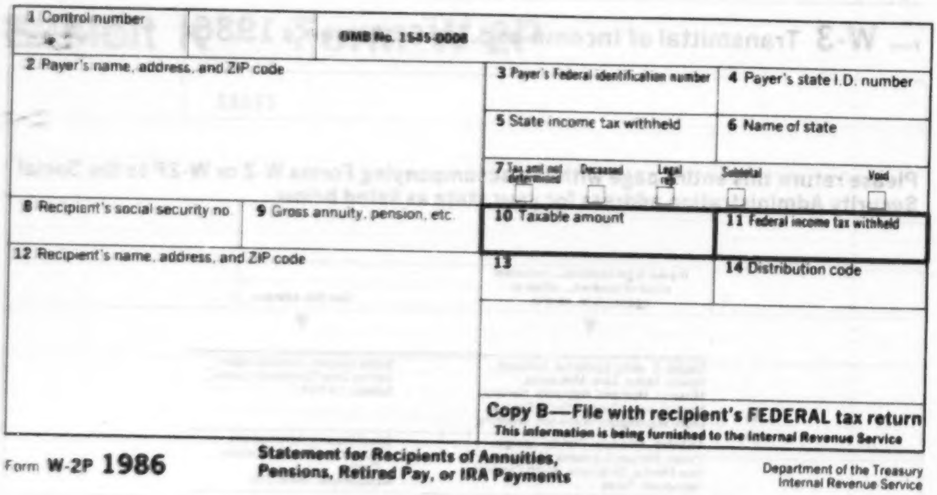
21 Local wages, tips, etc.

22 Name of locality

Form **W-2 Wage and Tax Statement 1986**

Copy B To be filed with employee's FEDERAL tax return
This information is being furnished to the Internal Revenue Service.

Department of the Treasury
Internal Revenue Service



1 Control number

OMB No. 1545-0008

2 Payer's name, address, and ZIP code

3 Payer's Federal identification number

4 Payer's state I.D. number

5 State income tax withheld

6 Name of state

7 Tax amt not determined ☐ Deceased ☐ Legal rep. ☐ Subtotal ☐ Void ☐

8 Recipient's social security no.

9 Gross annuity, pension, etc.

10 Taxable amount

11 Federal income tax withheld

12 Recipient's name, address, and ZIP code

13

14 Distribution code

Copy B—File with recipient's FEDERAL tax return
This information is being furnished to the Internal Revenue Service

Form **W-2P 1986**

Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments

Department of the Treasury
Internal Revenue Service

Exhibit N

Social Security Administration Regional Magnetic Media Coordinators

SSA Regional Office	Inclusive States	
Social Security Administration J.F. Kennedy Building Boston, Massachusetts 02203 ATTN: Magnetic Media Coordinator, Room 1109 Telephone: 617-223-4375	Connecticut Maine Massachusetts	New Hampshire Rhode Island Vermont
Social Security Administration 26 Federal Plaza New York, New York 10278 ATTN: Magnetic Media Coordinator, Room 40-130 Telephone: 212-264-0253	New Jersey New York Puerto Rico Virgin Islands	
Social Security Administration P.O. Box 8788, 3535 Market Street Philadelphia, Pennsylvania 19101 ATTN: Magnetic Media Coordinator, Room 8490 Telephone: 215-596-0474	Delaware District of Columbia Maryland	Pennsylvania Virginia West Virginia
Social Security Administration P.O. Box 1684, 101 Marietta Tower Atlanta, Georgia 30301 ATTN: Magnetic Media Coordinator Telephone: 404-331-2587	Alabama Florida Georgia Kentucky	Mississippi North Carolina South Carolina Tennessee
Social Security Administration 300 South Wacker Drive Chicago, Illinois 60606 ATTN: Magnetic Media Coordinator, 27th Floor Telephone: 312-353-6717	Illinois Indiana Michigan	Minnesota Ohio Wisconsin
Social Security Administration 1200 Main Tower, Room 1535 Dallas, Texas 75202 ATTN: Magnetic Media Coordinator Telephone: 214-767-4311	Arkansas Louisiana New Mexico Oklahoma	
Social Security Administration 601 East 12th Street Kansas City, Missouri 64106 ATTN: Magnetic Media Coordinator, 4th Floor East Telephone: 816-374-2095	Iowa Kansas Missouri Nebraska	
Social Security Administration Federal Office Building 1961 Stout Street Denver, Colorado 80294 ATTN: Magnetic Media Coordinator, Room 1194 Telephone: 303-844-2364	Colorado Montana North Dakota	South Dakota Utah Wyoming
Social Security Administration 100 Van Ness Avenue San Francisco, California 94102 ATTN: Magnetic Media Coordinator, Systems Branch Telephone: 415-556-4788	American Samoa Arizona California	Guam Hawaii Nevada
Social Security Administration 2901 Third Avenue Seattle, Washington 98121 ATTN: Magnetic Media Coordinator, M/S 302 Telephone: 206-442-0468	Alaska Idaho Oregon Washington	

Part IV. Items of General Interest

Foundations Status of Certain Organizations

Announcement 86-68

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

A Just Service, Everett, WA
Alcohol Rehabilitation Corporation, Ukiah, CA
Allied One-Hundred Corporation, Scranton, PA
Allied Two-Hundred Corporation, Scranton, PA
Allied Three-Hundred Corporation, Scranton, PA
Allied Four-Hundred Corporation, Scranton, PA
American Association Christian Egyptians Corps of California, Downey, CA
American Rehabilitation Research Group, Inc., Harrisburg, PA
Anno Domini, Portland, OR
Antelope Valley Community Theatre, Lancaster, CA
Aquaducks Aquatics, Inc., San Leandro, CA
Arkley-Letteria Dalton Manor, Inc., Lima, OH
Armenian-American Support and Educational Center Inc., Cliffside Park, NJ
Asian Business League, San Francisco, CA
Association of Music Personnel In Public Radio, Point Lookout, MD
Bakersfield Police Officers Spouse Association, Bakersfield, CA
Bel Canto Singers Of York, York, PA
Belgian Olympic Committee, Pacific Palisades, CA
Black Business And Professional Association Of Paterson, Inc. Paterson, NJ
Business Executives For Nuclear Arms Control, Philadelphia, PA
Calck Hook Dance Theater, Inc., Langhorne, PA
California Saddlebred In Hand Foundation, Santa Monica, CA
Campbell Fund, The, Succasunna, NJ
Cancer Childrens Recreational Funds, Newark, NJ
Casa De Ninos, Inc., Goleta, CA
Christian Conciliation Service of Orange County, Inc., Garden Grove, CA
Citizens Environmental Resource Center, Inc., New York, NY
City-Wide Non-Denominational Christian Training Institute, Philadelphia, PA
Commonwealth Stage Company, Harrisburg, PA
Contact Oakwood, Dayton, OH
Crisis Pregnancy Center of Santa Cruz, Inc., Santa Cruz, CA
Cyprian Society of America Lampousa, Bergenfield, NJ
Dakota County Veterans Historical Society, Inc., South St. Paul, MN
Dayspring Ministries, Chester, NJ
Delta Christian Foundation, Walnut Creek, CA
Developmental Child Care, Inc., Wilmington, DE
Discovery Bay Productions, Seattle, WA
Ecoan, Philadelphia, PA
Episcopal Theological Education Fund, c/o Trust Department, Lancaster, PA
Essex County Community Foundation, East Orange, NJ
Ewing Township Sesquicentennial Committee, Inc., Trenton, NJ
Families Against Chemical Escape Involved Together (F.A.C.E.I.T.), Media, PA
Felex Foundation, Agaura, CA
Fishermen of the King, Inc., West Terre Haute, IN
Foundation for the Education of Non-Traditional Learners, Philadelphia, PA
Foundation Francaise D'aide Aux. Sports, Beverly Hills, CA
Fourth Angel Ministries, Inc., Willits, CA
Friends & Associates, Inc., Los Angeles, CA
Friends of Multiple Sclerosis of Philadelphia, Inc., The, Philadelphia, PA
Friends of Opera, Inc., Campbell, CA
Gallia Senior Housing, Inc., Rio Grande, OH
Golden Gate Chapter ABC Training Trust Fund, Dublin, CA
Hamities for Survival, Los Angeles, CA
Handicapped Scuba Association, San Clemente, CA
Hope Retirement Housing Corp., South, Glendale, CA
Jamul Regional Recreation Association, Jamul, CA
Jarc Housing Corporation I, Southfield, MI
Jarc Housing Corporation II, Southfield, MI
Kids' Foundation of the Greater Delaware Valley, The, Philadelphia, PA
Lakeville Volunteer Fire Dept. Inc., Petaluma, CA
Loves Gift, Pine Valley, CA
Lucha, Santa Paula, CA
Mack E. Williams Memorial Foundation, Inc., New Brunswick, NJ
Media Foundation West, Inc., Los Angeles, CA
Monaco Counseling Center, Las Vegas, NV
Morris Township Day, Inc., Convent Station, NJ
Murdoc Institute of Personal Development, Seattle, WA
National Association of Retired Senior Volunteer Program RSVP Directors Inc., Bellingham, WA
National Rural Coalition For The Prevention Of Incest And Child Abuse, The, Montfort, WI
Nationalities Service of Central California, Fresno, CA
Nipomo Area Recreation Association, Inc., Nipomo, CA
North Central Drill Team, Mansfield, OH
Northern California Regional Savings and Loan Conference, Inc., Monterey, CA
Nuclear Age Peace Foundation, Santa Barbara, CA
Ohana Me. Kealoha Dancers and Drummers Inc., Stockton, CA

Pacific Retirement Housing Corp., Glendale, CA
Parents Anonymous, Incorporated of Ada County, Boise, ID
Passinart: A Theatre Company, Portland, OR
PICPA Foundation for Education and Research, Philadelphia, PA
Prince Hall Housing Development Fund Company, New York, NY
Princeton Fifth Seven Fund, Inc., The, Princeton, NJ
Psychosynthesis International, Pasadena, CA
Rediscovery Christian Experience to Alleviate Marriage Breakdown, Bakersfield, CA
Romans Club International, Boulder Creek, CA
Route 1 Ministries, Santa Maria, CA
Sacramento Guild for the Performing Arts, Sacramento, CA
Santa Barbara Childrens Television, Santa Barbara, CA
Santa Maria Housing Corp., Santa Maria, CA
Somerset Aquatic Club, Inc., Somerville, NJ
South Bay Independence Center, Los Angeles, CA
Stellar Electric, La Jolla, CA
3-Hour Activity Session, The, Chicago, IL
Today's Kid Stuff, Inc., Jamesville, NY
Tualatin Youth Football Association, Tualatin, OR
United Cerebral Palsy Association of Chester County, Pennsylvania & Area, Inc., West Chester, PA
University of the Philippines Alumni Association In America (UPAAA), Teaneck, NJ
Verdugo Hills Tournament Softball Association Inc., Sunland, CA
Walcott Carey Company Inc., New York, NY
Youth Assistance Association of San Francisco, San Francisco, CA

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Medicare for State and Local Government Employees

Announcement 86-69[1]

Wages of state and local government employees hired after March 31, 1986, are generally subject to the hospital insurance—Medicare—portion of the social security tax under the recently enacted Consolidated Omnibus Budget Reconciliation Act.

Under prior law, state and local government employees were not required to be subject to any portion of the social security tax. However, all the states have made voluntary agreements with the Secretary of Health and Human Services to have certain groups of employees, such as teachers, covered by social security, including Medicare. Payments under these agreements are made and reported to the Social Security Administration (SSA).

Under the law just enacted, employees in such coverage groups will continue to be subject to these agreements, no matter when they are hired to work in the coverage group. States will continue to make and report required payments to the SSA.

In general, under the new law, employees hired after March 31, 1986, will be subject to the Medicare portion of the social security tax if they are in a group not covered by an agreement. Within a few weeks, the Service will send further information to each state and local government employer regarding whether the tax for that employer's employees should be paid to the Service or to the SSA.

The Service will waive penalties to allow employers time to implement the new requirements of the law. If all amounts due to the Service for April through December 1986 are paid by February 2, 1987, the Service will waive any penalties that might otherwise have been due for late payments. The Service will send further details and instructions to all affected employers.

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[1] Based on News Release IR-86-56, dated April 28, 1986.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
A. Russel Lucid	Norwell, MA	Attorney	Indefinite from March 26, 1986
Gary E. Borushko	Grosse Pointe Woods, MI	Certified Public Accountant	Indefinite from April 7, 1986
Paul Skulsky	Spring Valley, NY	Certified Public Accountant	Indefinite from April 1, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before their Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Thomas H. Foxhill, Jr.	Pemberton, NJ	Enrolled Agent	April 12, 1986
Peter Parker	Baltimore, MD	Attorney	April 12, 1986

Announcement of the Suspension, Termination, or Consent to Voluntary Suspension or Termination of Enrollment to Perform Actuarial Services Under the Employee Retirement Income Security Act of 1974

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to indentify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
Robert E. Nemann	Cincinnati, OH	For three months effective April 9, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.61-6(c)(3), 1.163-4, 1.451-1(d), 1.451-2(b), 1.454-1(a)(1)(i), 1.482-2(a), 1.482-2(c)(2), 1.483-1, 1.483-2, 1.1016-5(s), 1.1232-2, 25.2512-4, 25.2512-8, revised; 1.163-7, 1.446-2, 1.483-3 through 1.483-5, 1.1271-1 through 1.1275-5, added; 1.61-7(d), 1.249-1, 1.409-1(b)(1), 1.528-1(d), 1.582-1(e)(3)(i), 1.636-1(a)(1)(ii), 1.818-3(f), 1.861-2(a)(4), 1.993-1(g), 1.1001-1(g), 1.1012-1(f), 1.1037-1, 1.1232-1, 1.1232-3A, 1.6045-1(c), 1.6049-5, 1.6049-6(d), 1.9006-1(c)(1)(vii), 3.2(d), 3.3(b), 5f.163-1(f), 6a.103A-2(i)(2)(vi)(B), 514.23, amended; 1.1012-2, removed and new added; 1.7872-4(e), reproposed and revised.	Original issue discount rules, imputed interest rules, and safe haven interest rates	1986-18 I.R.B. 4	June 9, 1986
26 CFR 301.6103(j)(1)-1, amended; 301.6103(j)(2)-1, removed.	Disclosure of return information to Bureau of the Census	1986-19 I.R.B. 15	May 27, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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1986-21

Internal Revenue

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Highlights of this Issue

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These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-76, page 5.

Income from sources within the United States. Interest income from savings deposits with a domestic branch of a United States bank that is received by a domestic estate and is distributed to nonresident alien beneficiaries in the year of receipt is not from United States sources and is not subject to United States taxation in the hands of the beneficiaries. If such income is not distributed in the year of receipt, it is income to the estate and subject to United States taxation. Rev. Rul. 81-244 amplified.

EMPLOYEE PLANS

Rev. Rul. 86-74, page 4.

Integration with social security; guides. Guidelines for determining whether retirement plans properly integrate with benefits provided by social security are modified pursuant to the Social Security Amendments of 1983 to provide that certain items of deferred compensation are included in the definition of taxable wages and to reflect the change in the age at which unreduced social security benefits might be received. Rev. Rul. 71-446 modified.

Announcement 86-70, page 33.

In accordance with Section 12.02 of Rev. Proc. 84-23, set forth is a list of master and prototype plans closed by the National Office of the Internal Revenue Service as of March 31, 1986.

EXEMPT ORGANIZATIONS

Rev. Rul. 86-75, page 5.

Fraternal beneficiary society; whole life insurance with investment features. Whole life insurance constitutes a life benefit under section 501(c)(8) of the Code even though the policies contain investment features such as cash surrender value and policy loan.

Rev. Rul. 86-77, page 7.

Private foundations; taxable expenditures. A private foundation that made grants to individuals after 45 days from the date it submitted an exemption application in accordance with procedures fully disclosed in its application did not make taxable expenditures under section 4945 of the Code, even though the foundation did not specifically request advance approval of its procedures.

EXCISE TAXES

Rev. Rul. 86-77, page 7.

Private foundations; taxable expenditures. A private foundation that made grants to individuals after 45 days from the date it submitted an exemption application in accordance with procedures fully disclosed in its application did not make taxable expenditures under section 4945 of the Code, even though the foundation did not specifically request advance approval of its procedures.

ADMINISTRATIVE

T.D. 8082, page 8.

LR-205-82, page 12.

Amendments to the regulations under section 6231 of the Code relate to the definition of "partnership item." Proposed amendments relate to certain rules for the tax treatment of partnership items.

Announcement 86-71 page 41.

Form 851, Affiliations Schedule, has been revised to reflect the new definition of an affiliated group in section 1504 of the Code as amended by the Deficit Reduction Act of 1984.

Finding List on page 46.
Announcement of Disbarments and Suspensions begin on page 42.
Announcement of Notice of Proposed Rulemaking on page 44.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 401.—Qualified Pension, Profit-Sharing and Stock Bonus Plans

26 CFR 1.401-3: Requirements as to coverage. (Also Section 7805; 301.7805-1.)

Integration with social security; guides. Guidelines for determining whether retirement plans properly integrate with benefits provided by social security are modified pursuant to the Social Security Amendments of 1983 to provide that certain items of deferred compensation are included in the definition of taxable wages and to reflect the change in the age at which unreduced social security benefits might be received. Rev. Rul. 71-446 modified.

Rev. Rul. 86-74

SECTION 1. PURPOSE

The purpose of this revenue ruling is to modify Internal Revenue Service guidelines for determining whether pension, annuity, profit-sharing, and stock bonus plans integrate with benefits provided by the Social Security Act because of changes made by the Social Security Amendments of 1983, Pub. L. 98-21, 1983-2 C.B. 309.

SEC. 2. BACKGROUND INFORMATION.

Section 3.03 of Rev. Rul. 71-446, 1971-2 C.B. 187, defines compensation for purposes of that ruling as either (1) the amount of compensation that would be subject to tax under section 3101(a) of the Internal Revenue Code without the dollar limitation of section 3121(a)(1) of the Code or (2) the amount of compensation determined according to a restrictive definition such as compensation inclusive or exclusive of bonuses, commissions or overtime pay, or as basic compensation, or as the regular rate of compensation provided that whatever definition is used cannot result in prohibited discrimination.

Service guidelines for determining whether plan benefits integrate with benefits provided under the Social Security Act in Rev. Rul. 71-446 and Rev. Rul. 83-97, 1983-2 C.B. 72, assume that age 65 is the age at which unreduced old-age insurance benefits commence under the Social Security Act.

The Social Security Amendments of 1983 (1) amended the Code to provide that certain items of deferred compensation are included in the definition of taxable wages and (2) changed the age at which unreduced old-age insurance benefits commence under the Social Security Act for those born after January 1, 1938.

SEC. 3. DEFINITION OF COMPENSATION

Except as provided below, for purposes of Rev. Rul. 71-446, deferred compensation is excluded from the definition of "compensation" in section 3.03 of that revenue ruling. However, in accordance with Rev. Rul. 83-89, 1983-1 C.B. 88, and Rev. Rul. 84-74, 1984-1 C.B. 118, elective contributions (1) under a qualified cash or deferred arrangement described in section 401(k) of the Code, or (2) to a tax sheltered annuity described in section 403(b) of the Code may be included in "compensation" under section 3.03 of Rev. Rul. 71-446.

SEC. 4. OFFSET PLANS

Offset plans, as defined in Rev. Rul. 71-446, base the offset upon the old-age insurance benefit payable under the Social Security Act. The application of section 11 (and section 10.02) of Rev. Rul. 71-446 and the application of Rev. Rul. 83-97 to offset plans is based upon age 65 being the age at which unreduced old-age insurance benefits commence under the Social Security Act. Age 65 remains the age at which unreduced old-age insurance benefits commence for individuals born before January 2, 1938. However, because the age at which unreduced old-age insurance benefits commence for individuals born after January 1, 1938, has been increased by the Social Security Amendments of 1983, the application of section 11 (and section 10.02) of Rev. Rul. 71-446 and the application of Rev. Rul. 83-97 to offset plans with respect to individuals born after January 1, 1938, is modified by substituting for age 65 the age at which unreduced old-age insurance benefits commence.

Example 1:

An offset plan established by an employer covers an employee retiring at normal retirement age 65 and for whom age 67 is the age at which unreduced old-age insurance benefits commence. The plan may comply with Rev. Rul. 71-446, as modified herein, using one of the alternatives in section 11.01 for the period from age 65 to 67 and applying the reductions of section 10.02(1) or section 10.02(2) for that same period by substituting age 67 for age 65 wherever it appears in those sections.

Example 2:

An offset plan defines the normal retirement age as age 65 with the offset at age 65 based upon the old-age insurance benefits payable at age 65. For early retirement or other separation from service before age 65, the plan may satisfy the requirements of the preceding paragraph by using either of the alternatives of section 11.01 of Rev. Rul. 71-446 for the period of service between the age of early retirement or separation from service to age 65. in applying the 1/15 and 1/30 factors of section 10.02(1) pursuant to section 11.02 when applicable in this situation, the age at which unreduced old-age insurance benefits commence is substituted for age 65. Accordingly, the offset at age 65 is reduced by the 1/15 and 1/30 factors multiplied by the applicable number of years (including portions thereof) by which the age of early retirement or separation from service precedes age 65. However, the number of years for which the 1/15 factor applies may not exceed five minus the number of years (including portions thereof) by which the age at which unreduced old-age insurance benefits commence exceeds age 65.

SEC. 5. EXCESS PLANS

For excess plans (including step-rate excess plans), no change is required in the otherwise applicable integration limits determined under sections 5 and 6 of Rev. Rul. 71-446.

SEC. 6. PROSPECTIVE APPLICATION FOR CERTAIN PLANS

For plans in existence on May 27, 1986, that satisfy the Service's requirements for integration with social security benefits before the Social Security Amendments of 1983 and the modifications specified herein but fail to satisfy these requirements because of this change in law and these modifications, pursuant to the authority contained in section 7805(b) of the Code, this revenue ruling is effective only with respect to plan years commencing after December 31, 1986, for plan participants having any service after December 31, 1986. The plan amendments necessary for such plans to satisfy the Service's requirements for integration with social security benefits as modified herein must be adopted by the last day of the first plan year commencing after December 31, 1986, to be effective as of the beginning of that plan year. Under section 411(d)(6), such amendments must not reduce any plan participant's accrued benefit as of the later of the date of adoption or the effective date of the amendments. Because of the nature of necessary plan amendments, the accrued benefits of some plan participants may be increased.

For plans other than those described in the preceding paragraph, this revenue ruling is effective for plan years beginning after May 27, 1986.

SEC. 7. EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 71-446 is modified by the changes specified herein.

Section 501.—Exemption From Tax on Corporations, Certain Trusts, Etc.

26 CFR 1.501(c)(8)-1: Fraternal beneficiary societies.

Fraternal beneficiary society; whole life insurance with investment features. Whole life insurance constitutes a life benefit under section 501(c)(8) of the Code even though the policies contain investment features such as cash surrender value and policy loan.

Rev. Rul. 86-75

ISSUE

Does whole life insurance constitute a life benefit under section 501(c)(8) of the Internal Revenue Code?

FACTS

A fraternal beneficiary society operating under the lodge system issues life insurance contracts (as defined in section 7702 of the Code) to its members. The contracts provide a lump-sum death benefit which will be paid to the member's dependents on the death of an insured member. At any time, a member of the organization may borrow against the cash surrender value of the contract or withdraw the cash surrender value and terminate the contract.

LAW

Section 501(c)(8) of the Code provides for the exemption from federal income tax of fraternal beneficiary societies, orders, or associations—

(A) operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and

(B) providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association or their dependents.

Section 1.501(c)(8)-1 of the Income Tax Regulations provides that in order to be exempt under section 501(c)(8) of the Code an organization must have an established system for the payment to its members of their dependents of life, sick, accident, or other benefits.

HOLDING

Whole life insurance constitutes a life benefit under section 501(c)(8) of the Code.

Section 661.—Deduction For Estates and Trusts Accumulating Income or Distributing Corpus

26 CFR 1.661(a)-2: Deduction for distributions to beneficiaries.

Whether interest income from savings deposits with a domestic branch of a U.S. bank that is received by a domestic estate and distributed to nonresident alien beneficiaries in the year of receipt is deductible by the estate under section 661(a)(2) of the Code. See Rev. Rul. 86-76 below.

Section 861.—Income From Sources Within The United States

26 CFR 1.861-2: Interest.
(Also Sections 661, 871, 1441; 1.661(a)-2, 1.871-7, 1.1441-4.)

Income from sources within the United States. Interest income from savings deposits with a domestic branch of a United States bank that is received by a domestic estate and is distributed to nonresident alien beneficiaries in the year of receipt is not from United States sources and is not subject to United States taxation in the hands of the beneficiaries. If such income is not distributed in the year of receipt, it is income to the estate and subject to United States taxation. Rev. Rul. 81-244 amplified.

Rev. Rul. 86-76

ISSUE

Under the circumstances described below, if interest income from a savings deposit account with a domestic branch of a United States bank is received by a domestic estate, is that interest income taxable to the estate or to its nonresident alien beneficiaries?

FACTS

Situation (1). *A* was a resident of the United States who died in 1980. At the time of death, *A* maintained a savings deposit account with a domestic branch of a United States bank. Subsequent to *A*'s death, the savings deposit account was transferred to *E*, the domestic estate of *A*, which is administered by a public administrator. The savings account is the only asset of *E*. All the beneficiaries of *E* are nonresident alien individuals residing in foreign country *FC* with which the United States does not have an income tax treaty.

Pursuant to the terms of *A*'s will, *E* distributes all of the income earned by *E* from the savings deposit account (100*x* dollars) to the nonresident alien beneficiaries in the taxable year of receipt. The interest income is not effectively connected with the conduct by *E* of a trade or business within the United States, and is the only income of *E*.

Situation (2). The facts are the same except that, pursuant to the terms of *A*'s will, *E* does not distribute income received from the savings deposit account (100*x* dollars) to the nonresident alien beneficiaries in the taxable year of receipt (year 1). In the subsequent taxable year (year 2), *E* earns 50*x* dollars of interest and distributes 150*x* dollars to the nonresident alien beneficiaries. The distributable net income of *E* in year 2 is equal to 50*x* dollars under section 643 of the Internal Revenue Code.

LAW AND ANALYSIS

Section 641 of the Code provides for the taxation of estates and trusts, including the computation of their taxable income.

Section 661(a) of the Code provides that an estate is entitled to a deduction in computing taxable income in any taxable year, equal to the sum of (1) any amount of income required to be distributed currently (including any amount required to be distributed which may be paid out of income or corpus to the extent such amount is paid out of income for such taxable year); and (2) any other amounts properly paid or credited or required to be distributed for such taxable year. The deduction is limited to the distributable net income of the estate, as defined under section 643. Distributable net income is the table income of the trust or estate for the taxable year with certain modifications as provided in section 643.

Section 662(a) of the Code provides, in general, that the beneficiaries of the estate must include in gross income (1) amounts specified in section 661(a) required to be distributed currently; and (2) other amounts properly paid, credited, or required to be distributed to them for the taxable year. The amount of income that beneficiaries must include in any particular taxable year is limited to the distributable net income of the estate with respect to such year. Application of section 662 is not limited to citizens or residents of the United States.

Section 662(b) of the Code provides, in general, that the amounts within the scope of section 662(a) shall have the same character in the hands of the beneficiary as in the hands of the estate. Section 1.665(a)-OA(d) of the Income Tax Regulations provides that Subpart D, which contains the "throw-back" rules, does not apply to any estate.

Section 861(a)(1) of the Code provides, in part, that interest from the United States, or the District of Columbia, and interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise, shall be treated as income from sources within the United States. However, section 861(a)(1)(A) further provides that interest on amounts described in section 861(c) received by a nonresident alien individual shall not be treated as income from sources within the United States, if such interest is not effectively connected with the conduct of a trade or business within the United States.

Section 861(c) of the Code provides, in part, that for purposes of section 861(a)(1)(A) the amounts described in section 861(c) are deposits with persons carrying on the banking business, and deposits or withdrawable accounts with savings institutions chartered and supervised as savings and loan or similar associations under federal or state law.

Except in the case of portfolio interest attributable to certain debt obligations, section 871(a)(1)(A) of the Code provides, in part, that a nonresident alien individual is subject to a tax of 30 percent on amounts received as interest from sources within the United States (other than original issue discount as defined in section 1273), but only to the extent the amount so received is not effectively connected with the conduct of a trade or business within the United States.

Section 1441(a) of the Code provides, in part, that any person having control, receipt, custody, disposal, or payment of the items of income specified in section 1441(b) (to the extent that these items constitute gross income from sources within the United States) of any nonresident alien individual, must deduct and withhold from these items a tax of 30 percent. Section 1441(b) lists interest (other than original issue discount as defined in section 1273) as an item of income subject to the withholding of tax under section 1441(a). However, section 1441(c)(9) provides that portfolio interest within the meaning of section 871(h)(2) attributable to certain debt obligations is not subject to the withholding requirements of section 1441(a).

In Rev. Rul. 81-244, 1981-2 C.B. 151, the trustee of a domestic simple trust distributed interest income received from United States bank deposits to the trust's nonresident alien beneficiaries in the year such interest was received. The interest income was not effectively connected with a trade or business in the United States. Rev. Rul. 81-244 holds that the interest income received by the nonresident alien beneficiaries is not United States source income within the meaning of section 861(a)(1)(A) of the Code. *Accord Isidro Martin-Montis Trust v. Commissioner*, 75 T.C. 381 (1980), *acq.* 1981-2 C.B. 2.

Rev. Rul. 81-244 recognizes that Congress intended to incorporate the conduit theory of trust and estate taxation into the 1954 Code. In connection with the taxation of estates and trusts under the 1954 Code, the House Committee on Ways and Means stated:

> The bill adheres to the conduit theory of the existing law. This means that an estate or trust is in general treated as a conduit through which income passes to the beneficiary. [H.R. Rep. No. 1337, 83d Cong., 2d Sess. 61 (1954).]

In *Maximov v. United States*, 373 U.S. 49 (1963), a complex trust created in the United States with beneficiaries resident in the United Kingdom was held to be taxable on capital gains it realized that were not distributed to the beneficiaries by the trust during the same taxable year. An exemption from United States capital gains tax was provided for residents of the United Kingdom under the United States—United Kingdom Income Tax Convention in effect at that time. The Court noted the separate taxable entity status of a trust, apart from its beneficiaries, and that a trust is taxable on income it receives that is not distributed to the beneficiaries, nor otherwise taxable directly to the beneficiaries.

Thus, with respect to Situation 2, the 100*x* dollars of interest that *E* receives in year 1 is includible in *E*'s gross income. The 50*x* dollars of interest received by *E* in year 2 is includible in the gross income of *E* in that year, and is deductible by *E* in computing its taxable income in that year under section 661(a)(2) of the Code. The amount of the 150*x* dollar distribution from *E* potentially includible in the beneficiaries' gross income in year 2 is limited by *E's* distributable net income for such year under section 662(a)(2). Thus, only 50*x* dollars of the 150*x* dollar distribution is potentially includible in the gross income of the beneficiaries in year 2. However, pursuant to section 662(b), the 50*x* dollars will retain its character as interest in the hands of the beneficiaries, and, under sections 861(a)(1)(A) and 861(c), is not United States source income and is not subject to the 30 percent tax and withholding provisions in sections 871 and 1441, respectively. Further, since the 100*x* dollars is not included in the beneficiaries' gross income in year 2, the 100*x* dollars is not subject to the 30 percent tax and withholding provisions in sections 871 and 1441, respectively.

HOLDINGS

Situation (1). Interest from a savings deposit account with a domestic branch of a United States bank received and distributed by a domestic estate to nonresident alien beneficiaries in the same taxable year it is received is includible in the gross income of the estate in the taxable year of receipt, and is deductible by the estate in computing its taxable income in that year under section 661(a)(2) of the Code. The interest in the hands of the beneficiaries is not United States source income by reason of section 861(a)(1)(A), and thus is not subject to the 30 percent tax and withholding provisions in sections 871 and 1441, respectively.

Situation (2). Interest from a savings deposit account with a domestic branch of a United States bank received by a domestic estate in one taxable year and distributed to nonresident alien beneficiaries in a subsequent taxable year is includible in the gross income of the estate in the taxable year of receipt. No deduction is allowable to the estate with respect to such interest under section 661(a)(2), nor is any of such interest includible in the gross income of the nonresident alien beneficiaries under section 662, because no interest was distributed or was required to be distributed by the estate to the nonresident alien beneficiaries in the taxable year of receipt.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 81-244 is amplified.

Section 871.—Tax on Nonresident Alien Individuals

26 CFR 1.871-7: Taxation of nonresident alien individuals not engaged in United States business.

Whether interest income from savings deposits with a domestic branch of a U.S. bank that is received by a domestic estate and subsequently distributed to nonresident alien beneficiaries is subject to U.S. income tax in the hands of such beneficiaries. See Rev. Rul. 86-76, page 5.

Section 1441.—Withholding of Tax on Nonresident Aliens

26 CFR 1.1441-4: Exemptions from withholding.

Whether interest income from savings deposits with a domestic branch of a U.S. bank that is received by a domestic estate and subsequently distributed to nonresident alien beneficiaries is subject to withholding under section 1441. See Rev. Rul. 86-76, page 5.

Section 4945.—Taxes on Taxable Expenditures

26 CFR 53.4945-4: Grants to individuals.

Private foundations; taxable expenditures. A private foundation that made grants to individuals after 45 days from the date it submitted an exemption application in accordance with procedures fully disclosed in its application did not make taxable expenditures under section 4945 of the Code, even though the foundation did not specifically request advance approval of its procedures.

Rev. Rul. 86-77

ISSUE

Did a private foundation make taxable expenditures within the meaning of section 4945(d)(3) of the Internal Revenue Code when it made grants to individuals under the circumstances described below?

FACTS

A newly created nonprofit organization applied for exemption from federal income tax in 1980 as a private foundation under section 501(c)(3) of the Code. The application disclosed its intent to provide scholarship grants to individuals for study at educational institutions under procedures that were fully described in materials submitted as part of the application. The description of the procedures included a detailed statement describing the selection process, a description of the terms and conditions under which the organization ordinarily makes grants, a detailed description of its procedures to supervise grants, and a description of procedures to review grantee reports, investigate possible diversion of grant funds and recover diverted grant funds. While the scholarship program meets the requirements required for the approval of such grants, the application made no specific request for approval of its procedures.

In 1980, the Internal Revenue Service recognized the organization as a private foundation exempt from federal income tax under section 501(c)(3) of the Code. The exemption letter neither expressly approved nor disapproved the organization's procedures for providing grants to individuals. Upon receipt of this letter, the organization began to make grants to individuals in accordance with the procedures described in its application.

LAW AND ANALYSIS

Section 4945 of the Code imposes a tax on each taxable expenditure made by a private foundation.

Section 4945(d)(3) of the Code provides that the term "taxable expenditures" includes any amount paid or incurred by a private foundation as a grant to an individual for travel, study, or other similar purposes except as provided in section 4945(g).

Section 4945(g) of the Code provides that a grant to an individual for study that is made on an objective and nondiscriminatory basis pursuant to a procedure approved in advance by the Secretary is not a taxable expenditure under section 4945(d)(3) if it is demonstrated to the satisfaction of the Secretary that (1) the grant constitutes a scholarship or fellowship grant which is subject to the provisions of section 117(a) and is to be used for study at an educational organization described in section 170(b)(1)(A)(ii); (2) the grant constitutes a prize or award that is subject to the provisions of section 74(b), if the recipient of such prize or award is selected form the general public; or (3) the purpose of the grant is to achieve a specific, objective, produce a report or other similar product, or improve or enhance a literary, artistic, musical, scientific, teaching, or other similar capacity, skill, or talent of the grantee.

Section 53.4945-4(a)(3)(ii) of the Foundation Excise Tax Regulations provides the general rule that grants to individuals for travel, study or similar purposes will be taxable expenditures under section 4945(d)(3) of the Code, unless, among other requirements, the grants are made pursuant to procedures approved in advance by the Commissioner.

Section 53.4945-4(d)(1) of the regulations provides that a request for advance approval of a foundation's grant procedures must fully describe the foundation's procedures for awarding grants and for ascertaining that such grants are used for the proper purposes. The request must contain: (1) a detailed statement describing the selection process; (2) a description of the terms and conditions under which the foundation ordinarily makes grants; (3) a detailed description of the foundation's procedure for exercising supervision over grants; and (4) a description of the foundation's procedures for review of grantee reports, for investigation where diversion of grant funds from their proper purposes is indicated, and for recovery of diverted grant funds.

Section 53.4945-4(d)(3) of the regulations provides that if, by the 45th day after a request for approval of grant procedures has been properly submitted to the Service, the organization has not been notified that such procedures are not acceptable, such procedures shall be considered as approved from the date of submission until receipt of actual notice from the Service that such procedures do not meet the requirements of section 4945(g) of the Code. If a grant to an individual for a purpose described in section 4945(d)(3) is made after notification to the organization by the Service that the procedures under which the grant is made are not acceptable, such grant is a taxable expenditure.

Organizations applying for tax exemption and seeking advance approval of their procedures for grants to individuals may request such approval with their submission of Form 1023, Application for Recognition of Exemption under Section 501(c)(3) of the Code. A full and complete disclosure of an organization's grant-making procedures that includes the information required by section 53.4945-4(d)(1) is considered equivalent to a request for advance approval when submitted in conjunction with an exemption application. However, approval of an organization's exemption application does not in itself constitute approval of the organization's grant procedures unless the exemption letter so provides.

The organization's full disclosure of its grant-making procedures in its exemption application constituted a properly submitted request for approval of grant procedures within the meaning of section 53.4945-4(d) of the regulations. The 1980 approval of its exempt status, however, did not itself constitute an approval of its grant procedures. Nevertheless, because it did not receive, by the 45th day after submission of its application notification that its procedures were not approved, the organization's procedures are considered to have been approved from the date of its application under the provisions of section 53.4945-4(d)(3) of the regulations. Consequently, the organization's grants to individuals were not taxable expenditures under section 4945(d)(3) of the Code.

HOLDING

Under the circumstances described above, the private foundation did not make taxable expenditures within the meaning of section 4945(d)(3) of the Internal Revenue Code when it made grants to individuals.

Section 6231.—Definitions and Special Rules [Partnership Items]

26 CFR 301.6231(a)(3)-1: Partnership items.

T.D. 8082

TITLE 26—INTERNAL REVENUE.—CHAPTER I,—SUBCHAPTER F, PART 301—PROCEDURE AND ADMINISTRATION

Definition of Partnership Item

AGENCY: Internal Revenue Service, Treasury

ACTION: Final regulations.

SUMMARY: This document contains final Regulations on Procedure and Administration relating to the definition of "partnership item" under the rules for the tax treatment of partnership items. The Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462] prescribed those rules. Code section 6231(a)(3) provides that a "partnership item" is any item that must be taken into account for a taxable year of a partnership under any income tax provision to the extent that the regulations provide that the item is more appropriately determined at the partnership level. This document sets forth items that the Service considers to be more appropriately determined at the partnership level than at the partner level. These regulations provide guidance to partners, partnerships, and Internal Revenue Service personnel for compliance with the tax law.

DATES: The regulations shall apply with respect to partnership taxable years beginning after September 3, 1982. However, if a partnership and the Service agree to accelerate the effective date for the consolidated proceedings pursuant to section 407(a)(3) of the Tax Equity and Fiscal responsibility Act of 1982, the regulations shall apply with respect to that partnership for any partnership taxable year ending after September 3, 1982.

FOR FURTHER INFORMATION CONTACT: Cynthia Grigsby of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) Telephone 202-566-3318 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

Prior to the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) there was no mechanism for making tax adjustments at the partnership level since the partnership was not the taxable entity. The Service could not require all partners to join in a single consolidated administrative or judicial proceeding with respect to partnership issues even if the issues were common to all partners. Section 402 of TEFRA added sections 6221-6231 to the Internal Revenue Code to allow for consolidated administrative and judicial proceedings to determine the tax treatment of "partnership items" at th partnership level rather than at the partner level.

Under Code section 6231(a)(3) a "partnership item" is any item that must be taken into account for a taxable year of a partnership under any income tax provision of the Code to the extent that the regulations provide that that item is more appropriately determined at the partnership level than at the partner level. Proposed regulations published in the Federal Register on January 14, 1983 (48 F.R. 1759) [LR-186-82, 1983-1 C.B. 1048] listed the items which the Service considered to be more appropriately determined at the partnership level.

Among the items listed in the proposed regulations were the "distributive share" items that the partnership must allocate to the partners (including partnership liabilities and certain special purpose data such as that necessary to enable partners to compute depletion). Also included were guaranteed payments and partnership-level determinations that have a bearing on transactions affecting particular partners. Four comments were received on these proposed regulations. No public hearing was held because none was requested. After consideration of all comments regarding the proposed regulations, the proposed regulations are adopted as revised by this Treasury decision.

The notice of proposed rulemaking would have added the proposed regulations to the Income Tax Regulations (26 CFR Part 1). Because it is more appropriate to include these provisions in the Regulations on Procedure and Administration (26 CFR Part 301), this Treasury decision redesignates the provisions.

RESPONSE TO COMMENTS

One comment suggested that the regulations make clear that determinations relating to the timing of income, deductions, and credits, including the selection of an accounting method, depreciation, and inventory practices are partnership items. That these items are partnership items was implicit in the assumptions underlying the proposed regulations. For example, the determination of partnership taxable income of necessity includes determinations relating to the timing of income, deductions, and credits, and the accounting method and inventory practices of the partnership. In response to the comment, however, the proposed regulations are amended by adding a new paragraph (b) to make clear that the term "partnership item" includes items that affect the computation of partnership taxable income, such as the method of accounting, inventory method, taxable year, and elections of the partnership. The new paragraph also explicitly states that the term "partnership item" includes the accounting practices and the legal and factual determinations that underlie determinations as to the amount, timing, and characterization of items of income, credit, gain, loss, or deduction (for example, whether an item is currently deductible or must be capitalized, whether partnership activities have been engaged in with the intent of earning a profit for purposes of section 183, or whether the partnership qualifies for the research and development credit under section 30).

It was also suggested that the regulations address whether "coverage" issues (that is, issues that relate to whether the rules apply to a particular entity or item) are themselves partnership items. The most important of these coverage issues is whether the entity in question is a partnership. Section 6233, which was added to the Code by section 714(p)(1) of the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 472], generally provides for extension of the rules for consolidated proceedings to an entity that files a partnership return (or S corporation return). A notice of proposed rulemaking under sections 6221 through 6231 and section 6233 is set forth * * * [on page 12, this Bulletin].

One comment expressed concern that the inclusion of guaranteed payments as a partnership item could eliminate the availability of the "small partnership exception" under section 6231(a)(1)(B) to partnerships that would otherwise qualify as small partnerships. Section 6231(a)(1)(B) requires each partner's share of each partnership item to be the same as the partner's share of every other item. In the case of a guaranteed payment, the recipient's share of that item (100 percent) would be different than the recipient's share of other items. The notice of proposed rulemaking under section 6231(a)(1)(B), set forth * * * [on page 12, this Bulletin], addresses this issue.

One comment suggested that a transferee partner's basis in a partnership interest should not be treated as a partnership item even if the partnership has made election under section 754. The commenter stated that if the partnership disagrees with the transferee partner's determinations regarding amounts paid for the partnership interest (*e.g.*, whether some parts of the consideration were interest rather than principal), the partner should be entitled to dispute the partnership's determination of that item. This suggestion is not adopted in the final regulations. The determination of the transferee partner's basis in his partnership interest is a partnership item because that determination is necessary in order for the partnership to make certain partnership-level determinations with respect to the transferee partner's basis in partnership property. Treating an item as a partnership item does not deprive a partner of the right to disagree with the treatment of that item by the partnership.

The phrase "(including necessary preliminary determinations, such as the partner's basis in the contributed property)" is added to §301.6231(a)(3)-1(c)(2)(iv) to make clear that the partner's basis in property contributed to a partnership is a partnership item.

Two comments pointed out that personal arrangements between a partner and third parties may be relevant in determining to what extent a partner is "at risk" in a partnership activity to which section 465 applies. The commenters expressed concern that proposed §1.6231(a)(3)-1(a)(1)(vi)(c) treated these personal arrangements as "partnership items." The final regulations add the phrase "determinable at the partnership level" to §301.6231(a)(3)-1(a)(1)(vi)(c) to make clear that such personal arrangements are not partnership items.

The final regulations delete an erroneous example in the proposed regulations. That example indicated that the partnership would not need to make any determinations as to the partnership interest constructively owned by a partner with whom the partnership engages in a transaction governed by section 707(a). The partnership may at times need to make a determination with respect to constructive ownership.

The final regulations delete paragraphs (a)(4)(iv), (a)(4)(v), and (b)(4) of proposed §1.6231(a)(3)-1 and instead include determinations with respect to the application of section 751(a) and (b) under §301.6231 (a)(3)-1(a)(1)(vi).

EXECUTIVE ORDER 12291 AND REGULATORY FLEXIBILITY ACT

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required.

Pursuant to 5 U.S.C. 605(b), it is hereby certified that the requirements of the Regulatory Flexibility Act do not apply to this final regulation because it will not have a significant economic impact on a substantial number of small entities. The final regulation does not impose a significant economic burden on taxpayers; the regulation merely defines the items that are within the scope of the new rules for consolidated partnership proceedings.

DRAFTING INFORMATION

The principal author of these regulations is Robert E. Shaw of the Legislation and Regulations Division of the Office of the Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, on matters of both substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 301 is amended as follows:

Paragraph 1. The authority for part 301 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 301.6231(a)(3)-1 also issued under 26 U.S.C. 6230(k) and 6231(a)(3).

Par. 2. There is inserted in the appropriate place the following new section:

§301.6231(a)(3)-1 Partnership items.

(a) *In general.* For purposes of subtitle F of the Internal Revenue Code of 1954, the following items which are required to be taken into account for the taxable year of a partnership under subtitle A of the Code are more appropriately determined at the partnership level than at the partner level and, therefore, are partnership items:

(1) The partnership aggregate and each partner's share of each of the following:

(i) Items of income, gain, loss, deduction, or credit of the partnership;

(ii) Expenditures by the partnership not deductible in computing its taxable income (for example, charitable contributions);

(iii) Items of the partnership which may be tax preference items under section 57(a) for any partner;

(iv) Income of the partnership exempt from tax;

(v) Partnership liabilities (including determinations with respect to the amount of the liabilities, whether the liabilities are nonrecourse, and changes from the preceding taxable year); and

(vi) Other amounts determinable at the partnership level with respect to partnership assets, investments, transactions and operations necessary to enable the partnership or the partners to determine—

(A) The investment credit determined under section 46(a);

(B) Recapture under section 147 of the investment credit;

(C) Amounts at risk in any activity to which section 465 applies;

(D) The depletion allowance under section 613A with respect to oil and gas wells; and

(E) The application of section 751(a) and (b);

(2) Guaranteed payments;

(3) Optional adjustments to the basis of partnership property pursuant to an election under section 754 (including necessary preliminary determinations, such as the determination of a transferee partner's basis in a partnership interest); and

(4) Items relating to the following transactions, to the extent that a determination of such items can be made from determinations that the partnership is required to make with respect to an amount, the character of an amount, or the percentage interest of a partner in the partnership, for purposes of the partnership books and records or for purposes of furnishing information to a partner:

(i) Contributions to the partnership;

(ii) Distributions from the partnership; and

(iii) Transactions to which section 707(a) applies (including the application of section 707(b)).

(b) *Factors that affect the determination of partnership items.* The term "partnership item" includes the accounting practices and the legal and factual determinations that underlie the determination of the amount, timing, and characterization of items of income, credit, gain, loss, deduction, etc. Examples of these determinations are: The partnership's method of accounting, taxable year, and inventory method; whether an election was made by the partnership; whether partnership property is a capital asset, section 1231 property, or inventory; whether an item is currently deductible or must be capitalized; whether partnership activities have been engaged in with the intent to make a profit for purposes of section 183; and whether the partnership qualifies for the research and development credit under section 30.

(c) *Illustrations.* (1) *In general.* This paragraph (c) illustrates the provisions of paragraph (a)(4) of this section. The determinations illustrated in this paragraph (c) that the partnership is required to make are not exhaustive; there may be additional determinations that the partnership is required to make which relate to a transaction listed in paragraph (a)(4) of this section. The critical element is that the partnership needs to make a determination with respect to a matter for the purposes stated; failure by the partnership actually to make a determination (for example, because it does not maintain proper books and records) does not prevent an item from being a partnership item.

(2) *Contributions.* For purposes of its books and records, or for purposes of furnishing information to a partner, the partnership needs to determine:

(i) The character of the amount received from a partner (for example, whether it is a contribution, a loan, or a repayment of a loan);

(ii) The amount of money contributed by a partner;

(iii) The applicability of the investment company rules of section 721(b) with respect to a contribution; and

(iv) The basis to the partnership of contributed property (including necessary preliminary determinations, such as the partner's basis in the contributed property).

To the extent that a determination of an item relating to a contribution can be made from these and similar determinations that the partnership is required to make, therefore, that item is a partnership item. To the extent that that determination requires other information, however, that determination is not a partnership item. For example, it may be necessary to determine whether contribution of the property causes recapture by the contributing partner of the investment credit under section 47 in certain circumstances in which that determination is irrelevant to the partnership.

(3) *Distributions.* For purposes of its books and records, or for purposes of

furnishing information to a partner, the partnership needs to determine:

(i) The character of the amount transferred to a partner (for example, whether it is a distribution, a loan, or a repayment of a loan);

(ii) The amount of money distributed to a partner;

(iii) The adjusted basis to the partnership of distributed property; and

(iv) The character of partnership property (for example, whether an item is inventory or a capital asset).

To the extent that a determination of an item relating to a distribution can be made from these and similar determinations that the partnership is required to make, therefore, the determination is a partnership item. To the extent that that determination requires other information, however, that item is not a partnership item. Such other information would include those factors used in determining the partner's basis for the partnership interest that are not themselves partnership items, such as the amount that the partner paid to acquire the partnership interest from a transferor partner if that transfer was not covered by an election under section 754.

(4) *Transactions to which section 707(a) applies*. For purposes of its books and records, the partnership needs to determine:

(i) The amount transferred from the partnership to a partner or from a partner to the partnership in any transaction to which section 707(a) applies;

(ii) The character of such an amount (for example, whether or not it is a loan; in the case of amounts paid over time for the purchase of an asset, what portion is interest); and

(iii) The percentage of the capital interests and profits interests in the partnership owned by each partner.

To the extent that a determination of an item relating to a transaction to which section 707(a) applies can be made from these and similar determinations that the partnership is required to make, therefore, that item is a partnership item. To the extent that that determination requires other information, however, that item is not a partnership item. An example of such other information is the cost to the partner of goods sold to the partnership.

(d) *Effective date*. This section shall apply with respect to partnership taxable years beginning after September 3, 1982. This section shall also apply with respect to any partnership taxable year ending after September 3,1 982, if with respect to that year there is an agreement entered into pursuant to section 407(a)(3) of the Tax Equity and Fiscal Responsibility Act of 1982.

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved April 14, 1986.

J. Roger Mentz,
Assistant Secretary Designate of the Treasury.

(Filed by the Office of the Federal Register on April 15, 1986, 4:35 p.m., and published in the issue of the Federal Register for April 18, 1986, 51 F.R. 13212)

Section 7805.—Rules and Regulations

26 CFR 301.7805-1: Rules and regulations.

Whether certain provisions of the Social Security Amendments of 1983 may be applied prospectively. See Rev. Rul. 86-74, page 4.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Miscellaneous Provisions Related to the Tax Treatment of Partnership Items

LR-205-82

SUMMARY: This document contains proposed regulations relating to certain rules for the tax treatment of partnership items. The Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462] amended the applicable law. The proposed regulations would clarify miscellaneous provisions related to the tax treatment of partnership items and would provide guidance to partners and partnerships affected.

DATES: Written comments and requests for a public hearing must be delivered or mailed by June 17, 1986.

The regulations relating to consolidated partnership proceedings are proposed to apply with respect to partnership taxable years beginning after September 3, 1982. However, if a partnership and the Service agree to accelerate the effective date for the consolidated proceedings pursuant to section 407(a)(3) of the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462, 597], the regulations are proposed to apply with respect to that partnership for any partnership taxable years ending after September 3, 1982.

The regulations relating to consolidated S corporation proceedings (paragraphs (b) and (c)(2) of proposed §301.6233-1) are proposed to apply with respect to taxable years beginning after December 31, 1982.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-205-82), 1111 Constitution Ave., N.W., Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Cynthia Grigsby of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington, D.C. 20224 (Attention: CC:LR:T LR-205-82). Telephone 202-566-3318 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

Prior to the enactment of the Tax Equity and Fiscal Responsibility Act of 1982 (96 Stat. 324) there was no mechanism for making tax adjustments at the partnership level since the partnership was not the taxable entity. Section 402 of that Act added sections 6221 through 6231 to the Internal Revenue Code to allow for consolidated administrative and judicial proceedings to determine the tax treatment of "partnership items" at the partnership level rather than at the partner level. Final regulations defining "partnership items" are set forth * * * [on page 8, this Bulletin]. Temporary regulations and a notice of proposed rulemaking concerning special enforcement areas under section 6231(c) were published in the FEDERAL REGISTER on December 13, 1984 (49 FR 48536, 48573 [T.D. 7996, 1985-1 C.B. 357, LR-242-84, 1984-2 C.B. 917]). Section 714(p)(1) of the Tax Reform Act of 1984 (98 Stat. 494) [Pub. L. 98-369, 1984-3 C.B. (Vol. 1) 1, 472] added section 6233 to the Internal Revenue Code. Generally, section 6233 extends the rules for consolidated administrative and judicial proceedings to entities filing partnership returns or S corporation returns. Final regulations under section 6232, concerning the tax treatment of partnership items for windfall tax purposes, were published in the FEDERAL REGISTER on October 1, 1985 (50 FR 39,998) [T.D. 8054, 1985-44 I.R.B. 7]. The proposed regulations contained in this document address a variety of issues that arise under Code sections 6221 through 6231 and section 6233.

EXPLANATION OF PROVISIONS

Tax treatment determined at the partnership level.

Section 6221 states that the tax treatment of any partnership item shall be determined at the partnership level. Proposed §301.6221-1 provides that neither the Service nor the taxpayer may make any change to the treatment of a partnership item on the partner's return except as provided in sections 6222 through 6231 and the regulations thereunder. Thus, a partner who treats partnership items on the partner's return in a manner that is consistent with the treatment of those items on the partnership return is generally not subject to an adjustment of those items except through a partnership-level proceeding. Likewise, a taxpayer may not put partnership items in issue in a proceeding relating to nonpartnership items.

Notification of inconsistent treatment

Section 6222 requires the partner to treat partnership items on the partner's return in a manner consistent with the treatment of those items on the partnership return. This rule does not apply if the partner treats an item inconsistently and notifies the Service of the inconsistency.

The proposed regulations provide that the notification of inconsistent treatment of partnership items is to be made by filing the form prescribed by the Service for that purpose (currently, Form 8082) in accordance with the instructions accompanying that form.

If a partner reports the inconsistent treatment of any partnership items in accordance with proposed §301.6222(b)-1, the Service generally may not make an adjustment with respect to that partnership item unless the Service conducts a partnership-level proceeding or notifies the partner under section 6231(b)(1)(A) that all partnership items arising from that partnership will be treated as nonpartnership items with respect to that partner and conducts a separate proceeding. The proposed regulations make clear that adjustments in a separate proceeding with the partner are not limited to conforming adjustments. Likewise, a partner who reports an inconsistent treatment is protected only to the extent of notification. Thus, if the partner fails to point out another inconsistent item on the return, that item is subject to a computational adjustment to conform the treatment of that item on the partner's return to the treatment of the item on the partnership return.

Notice sent to partnership

The date that a notice with respect to a partnership proceeding is mailed to the tax matters partner is a significant event. For instance, a partner is not entitled to notice unless the partner is adequately identified at least 30 days before the notice is mailed to the tax matters partner. Proposed §301.6223(a)-1 provides that a notice is mailed to the tax matters partner on the earlier of the date on which the notice is mailed to the "TAX MATTERS PARTNER" at the address of the partnership or the date on which the notice is mailed to the person who is the tax matters partner at the address of the partner or the partnership.

Notice group

Section 6223 requires the Service to send notice of proceedings to the representative of any group of partners owning at least an aggregate 5-percent profits interest in the partnership (a "notice group") if the group so requests. Proposed §301.6223(b)-1 provides that a notice group may be formed only with respect to partnership taxable years that have ended before the request is filed. However, a request by a notice group may relate to more than one taxable year. The proposed regulations also provide that the notice group may include notice partners entitled to separate notice and that a partner may join a notice group after the formation of the group at any time by providing the Service with the required information. The proposed regulations further provide that a partner cannot be a member of more than one notice group with respect to the same partnership for the same taxable year or withdraw from a notice group. While the proposed rules with respect to notice groups are intended to allow partners flexibility to form and join notice groups, these limitations are necessary for administrative reasons.

The proposed regulations make clear that partners forming a notice group are not necessarily associating themselves as a "5-percent group" for purposes of litigation. The representative of a notice group does not have the power to file a petition for judicial review on behalf of the group. All members of any "5-percent group" must join in filing any petition. The role of the notice group representative is administrative (that is, forwarding notice to the members of the group). He or she is not the legal representative of the group.

Withdrawal of notice of beginning of administrative proceeding

Proposed §301.6223(a)-2 provides that the Service may withdraw a notice of the beginning of an administrative proceeding within 45 days after that notice is mailed to the tax matters partner if the Service decides not to propose any adjustments to the partnership return as filed. If the Service withdraws the notice, neither the Service nor the tax matters partner is required to furnish any notice with respect to that proceeding to any other partner. Proposed §301.6223(a)-2(b) limits the circumstances under which the Service can reissue a notice of the beginning of an administrative proceeding once it has been withdrawn.

Duties of tax matters partner

Proposed §301.6223(g)-1 defines the responsibility of the tax matters partner to furnish information on developments in the proceeding to the partners.

Settlement agreements and unidentified indirect partners

Proposed §301.6224(c)-2 provides that indirect partners who are not separately identified at least 30 days before the settlement are bound by any settlement agreement entered into by the pass-thru partner. This provision allows the Service the same 30-day period for taking identifying information with respect to an indirect partner into account for settlement purposes as well as for for purposes of sending notices to such a partner.

Consistent settlements

Proposed §301.6224(c)-3 provides that any partner desiring settlement terms consistent with the terms of any settlement agreement entered into with any other partner must file with the Internal Revenue Service office that entered into the agreement a statement to that effect no later than the 150th day after the notice of the final partnership administrative adjustment is mailed to the tax matters partner (or, if later, the 60th day after the original settlement was entered into). The proposed regulations clarify that the "consistent settlement" requirement does not apply unless the items subject to the settlement were partnership items with respect to the partner who entered into the original settlement immediately before the settlement and are still partnership items with respect to the requesting partner at the time of the request.

Administrative adjustment requests

Proposed §301.6227(b)-1 provides that an administrative adjustment request that the tax matters partner asks to have treated as a substituted partnership return remains an administrative adjustment request even if the Service decides not to treat the request as a substituted return. Thus, the tax matters partner may file suit under section 6228(a) if the Service fails to take timely action on the request.

An administrative adjustment request filed on behalf of a partner is similar to a claim for refund except that it relates only to partnership items and the partner's right to bring suit on the request is limited. Proposed §301.6227(c)-1 provides that the request must be filed on the form specified by the Service for that purpose (currently, Form 8082), in accordance with the instructions accompanying that form.

Definition of partnership

Section 6231(a)(1) defines the term "partnership" broadly to include any partnership required to file a return under section 6031(a) but provides an exception from the consolidated partnership procedures for certain small partnerships. A partnership qualifies for this exception for any partnership taxable year only if during that taxable year it has 10 or fewer partners and each partner's share of each partnership item is the same as his or her share of every other item. The proposed regulations provide that a partnership does not qualify for the exception if any of its partners is a pass-thru partner (other than partner's estate).

The proposed regulations apply the "10 or fewer" limitation to the aggregate number of individuals who are partners at any one time during the partnership taxable year. Thus, a partnership that never has more than 10 partners at any given moment during the taxable year would be treated as a small partnership even if, because of transfers, 11 or more individuals hold interests in the partnership during the course of the yaxable year. A husband and wife are treated as one partner.

The "same share" requirement excludes from the scope of the small partnership exception any partnership making item allocations (other than special allocations under section 704(c) and certain allocations based on similar concepts). Under this requirement, a partner generally must have the same percentage interest in all items of partnership income or loss. Some items that will be treated as "partnership items" for general purposes under the proposed rules will not be treated as "partnership items" for purposes of the "same share" requirement. The proposed regulations apply the "same share" rule only in the case of specified distributive share partnership items. The same share requirement is satisfied for a taxable year if during all periods within that taxable year each partner's share of each of the enumerated partnership items is the same as the partner's share of each of the other enumerated items during that period (even though the partners share of all enumerated items changes from period to period within that taxable year).

An exempt small partnership may elect to be subject to the new partnership procedures. The proposed regulations provide procedural rules for making this election.

Spouse filing joint return with individual holding separate interest

Generally, proposed §301.6231(a)(2)-1 treats a spouse who files a joint return with an individual holding a separate interest in the partnership as a partner. Thus, the spouse will be permitted to participate in administrative and judicial proceedings. However, the spouse will not be counted as a partner for purposes of applying the special rules for partnerships with more than 100 partners or the exception for small partnerships.

Affected items and computational adjustments

Proposed §301.6231(a)(5)-1 provides that the term "affected item" includes a partner's basis in his or her partnership interest and application of the at-risk limitation, to the extent these items are not partnership items. Additions to tax and additional amounts that are attributable to partnership items or affected items are also affected items. Proposed §301.6231(a)(6)-1 provides that a change in the tax liability of a partner to properly reflect the treatment of a partnership item is made through a computational adjustment. In some cases, a change in tax liability attributable to an affected item may be made through a computational adjustment. However, if a change in the tax liability cannot be made without certain partner-level determinations then the change attributable to such partner-level determinations is made through deficiency procedures and not through a computational adjustment. Certain affected items may require partner-level determinations; for example, a partner's at-risk amount may depend upon the source from which the partner obtained the funds that the partner contributed to the partnership. Other affected items, such as the threshold amount for medical deductions that changes as a result of determinations made at the partnership level, do not require partner-level determinations and can thus be included in a computational adjustment. Proposed §301.6231(a)(6)-1 provides that a computational adjustment may not include any additions to tax or additional amounts.

Designation of a tax matters partner

Section 6231(a)(7) provides that the tax matters partner is the general partner designated as the tax matters partner in the manner prescribed by regulations. The proposed regulations provide that a person may be designated as the tax matters partner only if the person was a general partner at some time during the taxable year for which the designation is made or is a general partner as of the time the designation is made. The proposed regulations provide that the partnership may designate the tax matters partner for a taxable year on the partnership return if the form prescribed for the partnership return (currently, Form 1065) for that taxable year contains a space for the designation of a tax matters partner. If the form does not contain such a space, the designation may be made on a statement filed with the partnership return. Currently, Form 1065 does not contain a space for the designation. The proposed regulations also permit designations in other circumstances. A designated tax matters partner may certify to the Service the selection of a successor. In addition, a tax matters partner may be designated after the filing of the partnership return by general partners with a majority interest (taking into account only interests held by general partners) or, under certain circumstances, by partners with a majority overall interest. The proposed regulations also provide rules for terminating this designation and for determining the tax matters partner when the partnership has not made a designation.

The proposed regulations permit the designation of an alternate tax matters partner if the partnership designates an individual as tax matters partner. The alternate tax matters partner automatically succeeds the designated tax matters partner if the tax matters partner dies or is adjudicated incompetent. The proposed regulations limit the ability of a partnership to designate a tax matters partner who is not a United States person.

Special enforcement areas

Under the rules for consolidated partnership proceedings, if a partner treats partnership items on the partner's return consistently with the treatment of those items on the partnership return, generally no adjustment can be made with respect to a partnership item on that partner's return without conducting a partnership-level proceeding to determine the tax treatment of partnership items with respect to all partners. The requirement of a partnership-level proceeding before an assessment with respect to partnership items can be made would interfere with certain existing tax procedures. For example, a jeopardy assessment may ordinarily be made immediately if the Service believes that the assessment or collection of a deficiency will be jeopardized by delay.

Section 6231(c) lists certain areas that may present special enforcement problems under the rules for consolidated proceedings and authorizes the addition of other areas to the list of special enforcement areas by regulations. The proposed regulations add to the list of special enforcement areas provided in section 6231(c) the following: bankruptcy, receivership, and requests for prompt assessment under section 6501(d). Additional special enforcement problems were addressed in temporary regulations and a notice of proposed rulemaking which were published in the FEDERAL REGIS-

TER on December 13, 1984 (49 F. Reg. 48536, 48573 [T.D. 7996, 1985-1 C.B. 357, LR-242-84, 1984-2 C.B. 917]). The temporary regulations, §§301.6231(c)-1 T and 301.6231(c)-2 T, provide special rules for certain applications for tentative carryback and refund adjustments based on partnership losses, deductions, or credits and for certain refund claims based on losses, deductions, or credits from abusive tax shelter partnerships.

Section 6231(c) provides that to the extent that the regulations provide that the treatment of items as partnership items in these special cases will interfere with the effective and efficient enforcement of internal revenue laws, those items will be treated as nonpartnership items. The proposed regulations state when application of the new rules for treatment of partnership items would interfere with effective tax administration and note the date on which the partnership items become nonpartnership items. For example, when a petition is filed in Bankruptcy Court naming a bankrupt partner as debtor, any action in any court to determine the bankrupt partner's tax liability is stayed. The Bankruptcy Court may exercise its discretion to determine the tax liability of the bankrupt partner but the rules for consolidated partnership proceedings do not confer any jurisdiction over the partnership proceedings. Determining the tax liability of a partner who is named as a debtor in a bankruptcy proceeding under the rules for consolidated partnership proceedings would interfere with the effective and efficient enforcement of the tax laws. Therefore, the proposed regulations provide that all partnership items of such a partner will be treated as nonpartnership items as of the date a petition naming that partner as a debtor is filed in bankruptcy. The proposed regulations do not include foreign partnerships as a special enforcement area. Items treated as nonpartnership items are subject to adjustment in separate proceedings.

Effect of judicial decision on certain proceedings

Section 6231(e) provides that a court decision with respect to a partner's income tax liability not resulting from a partnership proceeding shall not be a bar to further proceedings with respect to that liability because of items which become nonpartnership items after the appropriate time to include them in the earlier court proceeding has passed. Proposed §301.6231(e)-2 makes clear that the Service could issue a later deficiency notice for the same taxable year with respect to that partner and that that partner could bring a refund suit with respect to those items that have become nonpartnership items.

Proposed §301.6231(e)-1 makes clear that a determination with respect to an item in a nonpartnership proceeding with a partner is not controlling in the determination of that item with respect to other partners. For example the finding of a court in a separate proceeding with a partner that a certain partnership expenditure is deductible does not bind either the Service or the other partners in a later partnership proceeding. While this proposition is not specifically spelled out in the statute, it is implicit in the statutory scheme which permits separate proceedings before the conclusion of partnership-level proceedings.

Disallowance of losses and credits in certain cases

Proposed §301.6231(f)-1 provides that the disallowance rule in section 6231(f) applies to both domestic and foreign partnerships. Although the heading of that Code provision refers to "foreign partnerships," the actual statutory language is not so limited. The purpose of the provision is to prevent partners from deriving tax benefits from any partnership, foreign or domestic, that fails to file a required partnership return if either the tax matters partner resides outside the United States or the books and records of the partnership are maintained outside the United States. Either of these circumstances could substantially increase the administrative burden on the Service in auditing the partnership.

The proposed regulations provide that the losses and credits arising from a partnership will be disallowed to a partner only if the partnership fails to file the required return within 60-days after the Service notifies the partner of the problem. Even if the partnership fails to file the return within that 60-day period, the losses or credits may still be allowed in whole or in part if the partner shows that the losses and credits are proper and that the partner has made a good faith effort to have the partnership file the return.

Extension to entities filing a partnership or S corporation return, etc.

Proposed §301.6233-1 provides that the provisions of subchapter C of chapter 63 of the Code ("subchapter C") apply with respect to entities filing a partnership return for taxable years beginning after September 3, 1982 (and certain earlier years to which an election to be included within the rules for consolidated proceedings provisions applies), the entity's items for that taxable year, and to any person holding an interest in the entity for that taxable year. The provisions of subchapter C also apply where a partnership return is filed but it is determined that there is no entity. However, the provisions of subchapter C do not apply to entities for any taxable year in which the entity would qualify for the small partnership exception under proposed §301.6231(a)(1)-1 if the entity were a partnership and for any taxable year for which a partnership return was filed for the sole purpose of making an election under section 761(a).

Proposed §301.6233-1 also provides that the provisions of subchapter D of chapter 63 of the Code ("subchapter D") apply with respect to entities filing a return as an S corporation for taxable years beginning after December 31, 1982, the entity's items for that taxable year, and any person holding an interest in the entity for that taxable year. The provisions of subchapter D also apply where an S corporation return is filed but it is determined that there is no entity. Regulations under subchapter D will be promulgated at a future date.

COMMENT AND PUBLIC HEARING

Before the adoption of these proposed regulations consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20530. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies of those comments to the Service.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis is therefore not required.

Pursuant to 5 U.S.C. 605(b), it is hereby certified that the requirements of the Regulatory Flexibility Act do not apply to this notice of proposed rulemaking because the proposed regulations will not have a significant economic impact on a substantial number of small entities. The definitional rules being proposed apply regardless of the size of the partnership. The procedural rules are designed to keep the reporting burden to the minimum necessary to enable the Internal Revenue Service to administer the law; duplicate filing is required in certain instances to permit the Service to coordinate examinations of partners and partnerships.

DRAFTING INFORMATION

The principal author of these proposed regulations is Robert E. Shaw of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Proposed amendments to the regulations.

It is proposed to amend 26 CFR Part 301 as follows:

Paragraph 1. The authority for Part 301 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 301.6221-1 also issued under 26 U.S.C. 6230(k). Section 301.6222(a)-1 also issued under 26 U.S.C. 6230(k). Section 301.6222(a)-2 also issued under 26 U.S.C. 6230(k). Section 301.6222(b)-1 also issued under 26 U.S.C. 6230(k). Section 301.6222(b)-2 also issued under 26 U.S.C. 6230(k). Section 301.6222(b)-3 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6223(a)-1 also issued under 26 U.S.C. 6230(k). Section 301.6223(a)-2 also issued under 26 U.S.C. 6230(k). Section 301.6223(b)-1 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6223(c)-1 also issued under 26 U.S.C. 6223(c) and 6230(i) and (k). Section 301.6223(e)-1 also issued under 26 U.S.C. 6230(k). Section 301.6223(e)-2 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6223(f)-1 also issued under 26 U.S.C. 6230(k). Section 301.6223(g)-1 also issued under 26 U.S.C. 6223(g) and 6230(i) and (k). Section 301.6223(h)-1 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6224(a)-1 also issued under 26 U.S.C. 6230(k). Section 301.6224(b)-1 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6224(c)-1 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6224(c)-2 also issued under 26 U.S.C. 6230(k). Section 301.6224(c)-3 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6226(a)-1 also issued under 26 U.S.C. 6230(k). Section 301.6226(b)-1 also issued under 26 U.S.C. 6230(k). Section 301.6226(e)-1 also issued under 26 U.S.C. 6230(k). Section 301.6226(f)-1 also issued under 26 U.S.C. 6230(k). Section 301.6227(b)-1 also issued under 26 U.S.C. 6227(b)(3) and 6230(i) and (k). Section 301.6227(c)-1 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6229(b)-1 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6229(e)-1 also issued under 26 U.S.C. 6230(k). Section 301.6230(b)-1 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6230(c)-1 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6230(e)-1 also issued under 26 U.S.C. 6230(i) and (k). Section 301.6231(a)(1)-1 also issued under 26 U.S.C. 6230(k). Section 301.6231(a)(2)-1 also issued under 26 U.S.C. 6230(k) and 6231(a)(12). Section 301.6231(a)(5)-1 also issued under 26 U.S.C. 6230(k). Section 301.6231(a)(6)-1 also issued under 26 U.S.C. 6230(k). Section 301.6231(a)(7)-1 also issued under 26 U.S.C. 6230(k) and 6231(a)(7). Section 301.6231(a)(12)-1 also issued under 26 U.S.C. 6230(k) and 6231(a)(12). Section 301.6231(c)-3 also issued under 26 U.S.C. 6230(k) and 6231(c). Section 301.6231(c)-4 also issued under 26 U.S.C. 6230(k) and 6231(c). Section 301.6231(c)-5 also issued under 26 U.S.C. 6230(k) and 6231(c). Section 301.6231(c)-6 also issued under 26 U.S.C. 6230(k) and 6231(c). Section 301.6231(c)-7 also issued under 26 U.S.C. 6230(k) and 6231(c). Section 301.6231(c)-8 also issued under 26 U.S.C. 6230(k) and 6231(c). Section 301.6231(d)-1 also issued under 26 U.S.C. 6230(k). Section 301.6231(e)-1 also issued under 26 U.S.C. 6230(k). Section 301.6231(e)-2 also issued under 26 U.S.C. 6230(k). Section 301.6231(f)-1 also issued under 26 U.S.C. 6230(i) and (k) and 6231(f). Section 301.6233-1 also issued under 26 U.S.C. 6230(k) and 6233.

Par. 2. There are inserted in the appropriate places the following new sections.

301.6221-1, 301.6222(a)-1,
301.6222(a)-2, 301.6222(b)-1,
301.6222(b)-2, 301.6222(b)-3,
301.6223(a)-1, 301.6223(a)-2,
301.6223(b)-1, 301.6223(c)-1,
301.6223(e)-1, 301.6223(e)-2,
301.6223(f)-1, 301.6223(g)-1,
301.6223(h)-1, 301.6224(a)-1,
301.6224(b)-1, 301.6224(c)-1,
301.6224(c)-2, 301.6224(c)-3,
301.6226(a)-1, 301.6226(b)-1,
301.6226(e)-1, 301.6226(f)-1,
301.6227(b)-1, 301.6227(c)-1,
301.6229(b)-1, 301.6229(e)-1,
301.6230(b)-1, 301.6230(c)-1,
301.6230(e)-1, 301.6231(a)(1)-1,
301.6231(a)(2)-1, 301.6231(a)(5)-1,
301.6231(a)(6)-1, 301.6231(a)(7)-1,
301.6231(a)(12)-1, 301.6231(c)-3,
301.6231(c)-4, 301.6231(c)-5,
301.6231(c)-6, 301.6231(c)-7,
301.6231(c)-8 301.6231(d)-1,
301.6231(e)-1, 301.6231(e)-2,
301.6231(f)-1, and 301.6233-1.

§301.6221-1 Tax treatment determined at partnership level.

(a) *In general.* A partner's treatment of partnership items on the partner's return may not be changed except as provided in sections 6222 through 6231 of the Code and the regulations thereunder. Thus, for example, if a partner treats an item on the partner's return consistently with the treatment of the item on the partnership return, the Internal Revenue Service generally cannot adjust the treatment of that item on the partner's return except through a partnership-level proceeding. Similarly, the taxpayer may not put partnership items in issue in a proceeding relating to nonpartnership items. For example, the taxpayer may not offset a potential increase in taxable income based on changes in nonpartnership items by a potential decrease based on partnership items.

(b) *Restrictions inapplicable after items become nonpartnership items.* Section 6221 and paragraph (a) of this section cease to apply to items arising from a partnership with respect to a partner when those items cease to be partnership items with respect to that partner under section 6231(b).

(c) *Cross reference.* See §§301.6231(c)-1T and 301.6231(c)-2T for special rules relating to certain applications and claims for refund based on losses, deductions, or credits from abusive tax shelter partnerships.

§301.6222(a)-1 Consistent treatment of partnership items.

(a) *In general.* The treatment of a partnership item on the partner's return shall be consistent with the treatment of that item by the partnership in all respects including the amount, timing, and characterization of the item.

(b) *Treatment must be consistent with partnership return.* The treatment of a partnership item on the partner's return shall be consistent with the treatment of that item on the partnership return. Thus, a partner who treats an item consistently with a schedule or other information furnished to the partner by the partnership has not satisfied the requirement of paragraph (a) of this section if the treatment of that item is inconsistent with the treatment of the item on the partnership return actually filed. For rules relating to the election to be treated as having reported the inconsistency where the partner treats an item consistently with an incorrect schedule, see §301.6222(b)-3.

(c) *Examples.* The following examples illustrate the principles set forth in this section.

Example (1). B is a partner of Partnership P. Both B and P use the calendar year as the taxable year. in December 1983, P receives an advance payment for services to be performed in 1984 and reports this amount as income for calendar year 1983. However, B reports B's distributive share of this amount on B's income tax return for 1984 and not on B's return for 1983. B's treatment of this partnership item is inconsistent with the treatment of the item by P.

Example (2). Partnership P incurred certain start-up costs before P was actively engaged in its business. P capitalized these costs. C, a partner in P, deducted C's proportionate share of these start-up costs. C's treatment of the partnership expenditure is inconsistent with the treatment of that item by P.

Example (3). D is a partner in partnership P which reports a loss of $100,000 on its return, $5,000 of which it reports on the Schedule K-1 attached to its return as D's distributive share. However, P reports $15,000 as D's distributive share of P's loss on the Schedule K-1 furnished to D. D reports the $15,000 loss in D's income tax return. D has not satisfied the consistency requirement. See, however, §301.6222(b)-3 for an election to be treated as having reported the inconsistency.

§301.6222(a)-2 Application of consistency and notification rules to indirect partners.

(a) *In general.* The consistency requirement of §301.6222(a)-1 is generally applied with respect to the source partnership. For purposes of this section, the term "source partnership" means the partnership (within the meaning of section 6231(a)(1)) from which the partnership item originates.

(b) *Indirect partner files consistently with source partnership.* An indirect partner who treats an item from a source partnership in a manner which is consistent with the treatment of that item on the return of the source partnership satisfies the consistency requirement of section 6222(a) regardless of whether the indirect partner treats that item in a manner which is consistent with the treatment of that item by the pass-thru partner through which the indirect partner holds the interest in the source partnership. Under these circumstances, therefore, the Service shall not send to the indirect partner the notice described in section 6231(b)(1)(A).

(c) *Indirect partner files inconsistently with source partnership*—(1) *Indirect partner notifies Service of inconsistency.* An indirect partner who—

(i) Treats an item from a source partnership in a manner which is inconsistent with the treatment of that item on the return of the source partnership, and

(ii) Files a statement identifying the inconsistency with the source partnership in accordance with §301.6222(b)-1,

shall not be subject to a computational adjustment to conform the treatment of that item to the treatment of that item on the return of the source partnership.

(2) *Indirect partner does not notify Service of inconsistency.* Except as provided in paragraph (c)(3) of this section, an indirect partner who—

(i) Treats an item from a source partnership in a manner which is inconsistent with the treatment of that item on the return of the source partnership, and

(ii) Fails to file a statement identifying the inconsistency with the source partnership in accordance with §301.6222(b)-1,

is subject to a computational adjustment to conform the treatment of that item to the treatment of that item on the return of the source partnership.

(3) *Indirect partner files consistently with a pass-thru partner that notifies the Service of the inconsistency.* If an indirect partner treats an item from a source partnership in a manner which is consistent with the treatment of that item by a pass-thru partner through which the indirect partner holds the interest in the source partnership and that pass-thru partner—

(i) Treats that item in a manner that is inconsistent with the treatment of that item on the return of the source partnership, and

(ii) Files a statement identifying the inconsistency with the source partnership in accordance with §301.6222(b)-1,

the indirect partner is not subject to a computational adjustment to conform the treatment of that item of the treatment of that item on the return of the source partnership.

(d) *Examples.* The following examples illustrate the principles set forth in this section.

Example (1). One of the partners in Partnership A is Partnership B, which has four equal partners C, D, E, and F. Both A and B are partnerships within the meaning of section 6231(a)(1). On its return, A reports $100,000 as B's distributive share of A's ordinary income. B, however, reports only $80,000 as its distributive share of the income and does not notify the Service of this inconsistent treatment with respect to A. C reports $20,000 as its distributive share of the item. Although C reports the item consistently with B, C is subject to a computational adjustment to conform the treatment of that item on C's return to the treatment of that item on the return of A.

Example (2). Assume the same facts as in example (1) except that B notified the Service of its inconsistent treatment with respect to source partnership A. C is not subject to a computational adjustment.

Example (3). Assume the same facts as in example (1). D reports only $15,000 as D's distributive share of the income and does not report the inconsistency. F reports only $9000 as its distributive share of the item but reports this inconsistency with respect to source partnership A. D is subject to a computational adjustment to conform the treatment of that item on D's return to the treatment of that item on the return of A. F is not subject to a computational adjustment.

Example (4). Assume the same facts as in example (3) except that F reported the inconsistency with respect to B and did not report the inconsistency with respect to source partnership A. F is subject to a computational adjustment to conform the treatment of that item on F's return to the treatment of that item on the return of A.

Example (5). Assume the same facts as in example (1). E reports $25,000 as its distributive share of the item. Regardless of whether E reports the inconsistency between its treatment of the item and that by B, E is neither subject to a computational adjustment to conform E's treatment of that item to that of B nor subject to the notice described in section 6231(b)(1)(A) with respect to any such notification of inconsistent treatment.

§301.6222(b)-1 Notification to Service when partnership items are treated inconsistently.

The statement identifying an inconsistency described in section 6222(b)(1)(B) shall be filed by filing the form prescribed for that purpose in accordance with the instructions accompanying that form.

§301.6222(b)-2 Effect of notification of inconsistent treatment.

(a) *In general.* Generally, if a partner treats a partnership item on the partner's return in a manner which is inconsistent with the treatment of that item on the partnership return the Service may make a computational adjustment to conform the treatment of the item by the partner with the treatment of that item on the partnership reutrn. Any additional tax resulting from that computational adjustment may be assessed without either the commencement of a partnership proceeding or notification tot he partner that all partnership items arising from that partnership will be treated as nonpartnership items. However, if a partner notifies the Service of the inconsistent treatment of a partnership item in the manner prescribed in §301.6222(b)-1, the Service generally may not make an adjustment with respect to that partnership item unless the Service—

(1) Conducts a partnership-level proceeding, or

(2) Notifies the partner under section 6231(b)(1)(A) that all partnership items arising from that partnership will be treated as nonpartnership items.

See, however, §§301.6231(c)-1T and 301.6231(c)-2T for special rules relating to certain applications and claims for refund based on losses, deductions, or credits from abusive tax shelter partnerships.

(b) *Partner protected only to extent of notification.* A partner who reports the inconsistent treatment of partnership items on the partner's return is protected from computational adjustments under section 6222(c) only with respect to those partnership items the inconsistent treatment of which is reported. Thus, if a partner notifying the Service with respect to one item fails to report the inconsistent treatment of another item, the partner is subject to a computational adjustment with respect to that latter item.

Example. Partner A of Partnership P treats a deduction and a capital gain arising from P on A's return in a manner that is inconsistent with the treatment of those items by P. A reports the inconsistent treatment of the deduction but not of the gain. A is subject to a computational adjustment under section 6222(c) with respect to the gain.

(c) *Adjustments in a separate proceeding not limited to conforming adjustments.* If the Service conducts a separate proceeding with a partner whose partnership items are treated as nonpartnership items under section 6231(b), the Service is not limited to making adjustments that merely conform the partner's return to the partnership return.

Example. partnership P allocates to E, one of its partners, a loss of $8,000. E, however, claims a loss of $9,000 and reports the inconsistent treatment. The Service notifies E that it will treat all of E's partnership items arising from P as nonpartnership items. As a result of a separate proceeding with E, the Service may issue a deficiency notice which could include reducing the loss to $3,000.

§301.6222(b)-3 Partner receiving incorrect schedule.

(a) *In general.* A partner shall be treated as having complied with section 6222(b)(1)(B) and §301.6222(b)-1 with respect to a partnership item if the partner—

(1) Demonstrates that the treatment of the partnership item on the partner's return is consistent with the treatment of that item on the schedule prescribed by the Service and furnished to the partner by the partnership showing the partner's share of income, credits, deductions, etc., and

(2) Elects in accordance with the rules prescribed in paragraph (b) of this section to have this section apply with respect to that item.

(b) *Election provisions*—(1) *Time and manner of making election.* The election described in paragraph (a) of this section shall be made by filing a statement with the Internal Revenue Service office issuing the notice of computational adjustment within 30 days after the notice is mailed to the partner.

(2) *Contents of statement.* The statement described in paragraph (b)(1) of this section shall be:

(i) clearly identified as an election under section 6222(b)(2),

(ii) Signed by the partner making the election, and

(iii) Accompanied by copies of the schedule furnished to the partner by the partnership and of the notice of computational adjustment. The partner need not enclose a copy of the notice of computational adjustment, however, if the partner clearly identifies the notice of computational adjustment.

Generally, the requirement described in paragraph (a)(1) of this section will be satisfied by attaching to the statement a copy of the schedule furnished to the partner by the partnership. However, if it is not clear from the information contained on the schedule that the treatment of the partnership item on the schedule is consistent with the partner's treatment of such item on the partner's return the statement shall also include an explanation of how the treatment of such item on the schedule is consistent with the treatment on the partner's return with respect to the characterization, timing, and amount of such item.

§301.6223(a)-1 Notice sent to tax matters partner.

(a) *In general.* For purposes of subchapter C of chapter 63 of the Code, a notice is treated as mailed to the tax matters partner on the earlier of—

(1) The date on which the notice is mailed to "THE TAX MATTERS PARTNER" at the address of the partnership (as provided on the partnership return, except as updated under §301.6223(c)-1), or

(2) The date on which the notice is mailed to the person who is the tax matters partner at the address of that person (as provided on the partner's return, except as updated under §301.6223(c)-1) or the partnership. See §301.6223(c)-1 for rules relating to the information to be used by the Service in providing notices, etc.

(b) *Example.* The provisions of this section may be illustrated by the following example:

Example. Partnership P designates B as its tax matters partner in accordance with §301.6231(a)(7)-1(b). On December 1 a notice of the beginning of an administrative proceeding is mailed to "THE TAX MATTERS PARTNER" at the address of P. On January 10, a copy of the notice is mailed to B at B's address. December 1 is treated as the date that the notice was mailed to the tax matters partner.

§301.6223(a)-2 Withdrawal of notice of the beginning of an administrative proceeding.

(a) *In general.* If the Internal Revenue Service, within 45 days after the day on which the notice specified in section 6223(a)(1) is mailed to the tax matters partner, decides not to propose any adjustments to the partnership return as filed, the Service may withdraw the notice specified in section 6223(a)(1) by mailing a letter to that effect to the tax matters partner within that 45-day period. If the Service withdraws the notice, neither the Service nor the tax matters partner is required to furnish any notice with respect to that proceeding to any other partner. Except as provided in paragraph (b) of this section, a notice specified in section 6223(a)(1) which has been withdrawn shall be treated for purposes of subchapter C of chapter 63 of the Code as if that notice had never been mailed to the tax matters partner.

(b) *Service may not reissue notice except under certain circumstances.* If the notice specified in section 62323(a)(1) was mailed to the tax matters partner with respect to a partnership taxable year and that notice was later withdrawn as provided in paragraph (a) of this section, the Service shall not mail a second notice specified in section 6233(a)(1) by mailing a letter to that effect to the tax matters partner within that 45-day period. If the Service withdraws the notice, neither the Service nor the tax matters partner is required to furnish any notice with respect to that proceeding to any other partner. Except as provided in paragraph (b) of this section, a notice specified in section 6223(a)(1) which has been withdrawn shall be treated for purposes of subchapter C of chapter 63 of the Code as if that notice had never been mailed to the tax matters partner.

(b) *Service may not reissue notice except under certain circumstances.* If the notice specified in section 6223(a)(1) was mailed to the tax matters partner with respect to a partnership taxable year and that notice was later withdrawn as provided in paragraph (a) of this section, the Service shall not mail a second notice specified in section 6233(a)(1) with respect to that taxable year unless:

(1) There is evidence of fraud, malfeasance, collusion, concealment, or misrepresentation of a material fact;

(2) The prior proceeding involved a clearly defined substantial error with respect to an established Service position existing at the time of the previous examination; or

(3) Other circumstances exist which indicate that failure to reissue the notice would be a serious administrative omission.

§301.6223(b)-1 Notice group.

(a) *In general.* If a group of partners having in the aggregate a 5 percent or more interest in the profits of a partnership so requests and designates one of their members to receive the notices described in section 6223(a)(1) and (2), the member so designated shall be treated as a partner to whom section 6223(a) applies. Thus, the designated representative is entitled to receive any notice described in section 6223(a) that is mailed to the tax matters partner 30 days or more after the day on which the Service receives the request from the group.

(b) *Request for notice*—(1) *In general.* The Service shall mail to the member of the notice group designated to receive such notice any notice described in section 6223(a) that is mailed to the tax matters partner 30 days or more after the day on which the Service receives the request for notice from the group if such request for notice is made in accordance with the rules prescribed in this paragraph (b).

(2) *Content of request.* The request for notice from a notice group shall—

(i) Identify the partnership by name, address, and taxpayer identification number,

(ii) Specify the taxable year or years for which the notice group is formed,

(iii) Designate the member of the group to receive the notices,

(iv) Set out the name, address, taxpayer identification number, and profits interest of each member of the group, and

(v) Be signed by all partners comprising the notice group.

(3) *Place for filing.* The request for notice from a notice group generally shall be filed with the service center with which the partnership return is filed. However, if the notice group representative knows that the notice described in section 6223(a)(1) (beginning of an administrative proceeding) has already been mailed to the tax matters partner, the statement shall be filed with the Internal Revenue Service office that mailed that notice.

(4) *Copy to be sent to the tax matters partner.* A copy of the request for notice from a notice group shall be provided to the tax matters partner by the notice group representative within 30 days after the request is filed with th the Service.

(5) *Years covered by request.* A request for notice by a notice group may relate only to partnership taxable years that have ended before the request is filed. A request, however, may relate to more than one partnership taxable year if the 5 percent or more profits interest requirement of section 6223(b)(2) is satisfied for each year to which the request relates.

(c) *Composition of notice group*—(1) *In general.* A notice group shall be comprised only of persons who were partners at some time during the partnership taxable year for which the group is formed. If a notice group is formed for more than one taxable year, each member of the group must have been a partner at some time during at least one of the taxable years for which the group is formed. A notice group may include a partner entitled to separate notice. See section 6231(d) and §301.6231(d)-1 for rules relating to determining the interest of a partner in the profits of a partnership for a partnership taxable year for purposes of section 6223(b). See paragraph (c)(6) of this section for rules relating to indirect and pass-thru partners.

(2) *Partner may be a member of only one group.* A partner cannot be a member of more than one notice group with respect to the same partnership for the same partnership taxable year. See paragraph (c)(6) of this section for rules relating to indirect and pass-thru partners.

(3) *Partner may join group after formation.* A partner may join a notice group at any time after the formation of that group by filing with the Internal Revenue Service office with which the notice group filed its request a statement that it is joining the notice group. The statement shall identify the partner joining the notice group, the partnership, and the members of the notice group by name, address, and taxpayer identification number and shall be signed by the joining partner. A copy of the statement shall be provided by the joining partner to both the tax matters partner and the notice group representative within 30 days after the request is filed with the Service. The partner shall become a member of the notice group for each partnership taxable year for which the group was formed and for which the partner was a partner at any time during such partnership taxable year.

(4) *Date on which a partner becomes a member of notice group.* A partner shall become a member of a notice group on the 30th day after the day on which the Service receives—

(i) A request for notice from a notice group that identifies that partner as a member of that notice group, or

(ii) A statement filed in accordance with paragraph (c)(3) of this section that states that the partner is joining the notice group.

(5) *No withdrawal from notice group.* A partner who has signed a notice group request filed with the Service remains a member of that notice group until the group terminates. A partner cannot withdraw from the notice group.

(6) *Indirect and pass-thru partners—(i) Pass-thru partners and unidentified indirect partners.* A pass-thru partner may become a member of a notice group as provided in this section. For purposes of applying the aggregate interest requirement specified in paragraph (a) of this section to a pass-thru partner, the partnership interest hold by the pass-thru partner shall not include any interest held through the pass-thru partner by an indirect partner that has been identified as provided in section 6223(c)(3) and §301.6223(c)-1 before the date on which the pass-thru partner becomes a member of the notice group.

(ii) *Indirect partners identified before the pass-thru partner joins a notice group.* An indirect partner may become a member of a notice group with respect to a partnership taxable year only if:

(A) The indirect partner held an interest in the partnership (either directly or through one or more pass-thru partners) at some time during that taxable year, and

(B) The indirect partner was identified as provided in section 6223(c)(3) and §301.6223(c)-1 on or before the date on which the pass-thru partner became a member of a notice group.

(d) *Termination of notice group.* Unless the original request for notice from the notice group or a subsequent statement filed by the representative (in accordance with paragraph (b)(3) and (4) of this section) designates a successor to the designated group representative, the group terminates if the representative dies (or, in the case of an entity, if the entity is dissolved), resigns, or is adjudicated incompetent.

(e) *Notice group is not a 5-percent group.* The forming of a notice group under this section does not constitute the forming of a 5-percent group for purposes of litigation. A notice group is formed solely for the purpose of receiving notices. A 5-percent group is formed solely for the purpose of filing a petition for judicial review or appealing a judicial determination. See §301.6226(b)-1. Thus, a member of a notice group may choose not to join a 5-percent group formed by other members of the notice group.

§301.6223(c)-1 Additional information regarding partners furnished to the Service.

(a) *In general.* In addition to the names, addresses, and profits interests as shown on the partnership return, the Service will use additional information as provided in this section for purposes of administering subchapter C of chapter 63 of the Code.

(b) *Procedure for furnishing additional information—*(1) *In general.* Any person may furnish additional information at any time by filing a written statement with the Service. However, the information contained in the statement will be considered for purposes of determining whether a partner is entitled to a notice described in section 6223(a) only if the Service receives the statement at least 30 days before the date on which the Service mails the notice to the tax matters partner. Similarly, information contained in the statement generally will not be taken into account for other purposes by the Service until 30 days after the statement is received.

(2) *Where statement must be filed.* A statement furnished under this section shall generally be filed with the service center with which the partnership return is filed. However, if the person filing the statement knows that the notice described in section 6223(a)(1) (beginning of an administrative proceeding) has already been mailed to the tax matters partner, the statement shall be filed with the Internal Revenue Service office that mailed such notice.

(3) *Contents of statement.* The statement shall—

(i) Identify the partnership, each partner for whom information is supplied, and the person supplying the information by name, address, and taxpayer identification number;

(ii) Explain that the statement is furnished to correct or supplement earlier information with respect to the partners in the partnership;

(iii) Specify the taxable year to which the information relates;

(iv) Set out the corrected or additional information, and

(v) Be signed by the person supplying the information.

(c) *No incorporation by reference to previously furnished documents.* Incorporation by reference of information contained in another document previously furnished to the Internal Revenue Service will not be given effect for purposes of sections 6223(c) or 6229(e). For example, reference to a return filed by a pass-thru partner which contains identifying information with respect to the indirect partners of that pass-thru partner is not sufficient to identify the indirect partners unless a copy of the document referred to is attached to the statement.

(d) *Information supplied by a person other than the tax matters partner.* The Service may require appropriate verification in the case of information furnished by a person other than the tax matters partner. The 30-day period referred to in paragraph (b)(1) of this section shall not begin until that verification is supplied.

(e) *Power of attorney*—(1) *In general.* This paragraph (e) applies to powers of attorney with respect to proceedings under subchapter C of chapter 63 of the Code ("chapter 63C") that begin on or after the date which is 90 days after the date final regulations under this section are published in the FEDERAL REGISTER.

(2) *Specifically for purposes of chapter 63C.* A power of attorney specifically for purposes of chapter 63C shall be furnished in accordance with paragraph (b)(2) of this section.

(3) *Existing power of attorney.* A power of attorney granted to another person by a partner for other tax purposes shall not be given effect for purposes of chapter 63C unless the partner specifically requests that the power be given such effect in a statement furnished to the Service in accordance with paragraph (b) of this section.

(f) *Service may use other information.* In addition to the information on the partnership return and that supplied on statements filed under this section, the Service may use information in its possession (for example, a change in address reflected on a partner's return) in administering subchapter C of chapter 63 of the Code. However, the Service is not obligated to search its records for information not expressly furnished under this section.

§301.6223(e)-1 Effect of Service's failure to provide notice.

(a) *Notice group.* Section 6223(e)(1)(B)(ii) applies with respect to a notice group only if the request for notice described in §301.6223(b)-1 is received by the Service at least 30 days before the notice is mailed to the tax matters partner.

(b) *Indirect partners*—(1) *In general.* For purposes of section 6223(e), the Service's failure to provide notice to a pass-thru partner that is entitled to notice under section 6223(b) is deemed failure to provide notice to indirect partners holding an interest in the partnership through the pass-thru partner. However, this rule does not apply if the indirect partner:

(i) Receives notice from the Service,

(ii) Is identified as provided in section 6223(c)(3) and §301.6223(c)-1 at least 30 days before the notice is mailed to the tax matters partner, or

(iii) Is a member of a notice group entitled to notice under paragraph (a) of this section.

(2) *Examples.* The provisions of paragraph (b)(1) of this section may be illustrated by the following examples:

Example (1). Partnership ABC has as one of its partners, A, a partnership with three partners, X, Y, and Z. ABC does not have more than 100 partners, and partnership A is entitled to notice under section 6223(a). In addition, Z was identified as provided in section 6223(c)(3) and §301.6223(c)-1 on May 1, 1985. The Service mailed notice to the tax matters partner of ABC on July 1, 1985, but failed to provide notice to partnership A. Notwithstanding the Service's notice to the tax matters partner, the Service is deemed to have failed to provide notice to X and Y. The Service's failure to provide notice to A, however, has no effect on Z; whether notice was provided to Z is determined independently.

Example (2). Assume the same facts as in Example (1), except that the Service provided notice to partnership A but did not provide separate notice to Z. Notwithstanding the Service's notice to partnership A, the Service is deemed to have failed to provide notice to Z.

Example (3). Assume the same facts as in Example (1), except that partnership ABC has more than 100 partners and partnership A is entitled to notice under section 6223(b) because it had at least a 1 percent profits interest in partnership ABC. In addition, X became a member of a member of a notice group on June 1, 1985, and the Service mailed notice to the designated member of that notice group. The Service also mailed a separate notice to Z. The Service's failure to provide notice to partnership A only affects Y, who is deemed not to have been provided notice by the Service.

§301.6223(e)-2 Elections if Service fails to provide timely notice.

(a) *Proceeding finished.* If at the time the Internal Revenue Service mails the partner notice of the proceeding—

(1) The period within which a petition for review of a final partnership administrative adjustment under section 6226 may be filed has expired and no petition has been filed, or

(2) The decision of a court in an action begun by such a petition has become final,

the partner may elect in accordance with paragraph (c) of this section to have that adjustment, that decision, or a settlement agreement described in section 6224(c)(2) with respect to the partnership taxable year to which the adjustment relates apply to that partner. If the partner does not make an election in accordance with paragraph (c) of this section, the partnership items of the partner for the partnership taxable year to which the proceeding relates shall be treated as having become nonpartnership items as of the day on which the Service mails the partner notice of the proceeding.

(b) *Proceeding still going on.* If paragraph (a) of this section does not apply, the partner shall be a party to the proceeding unless the partner elects, in accordance with paragraph (c) of this section, to have—

(1) A settlement agreement described in section 6224(c)(2) with respect to the partnership taxable year to which the proceeding relates apply to the partner, or

(2) The partnership items of the partner for the partnership taxable year to which the proceeding relates treated as having become nonpartnership items as of the day on which the Service mails the partner notice of the proceeding.

(c) *Election*—(1) *In general.* The election described in paragraph (a) or (b) of this section shall be made in the manner prescribed in this paragraph (c). The election shall apply to all partnership items for the partnership taxable year to which the election relates.

(2) *Time and manner of making election.* The election shall be made by filing a statement with the Internal Revenue Service office mailing the notice regarding the proceeding within 45 days after the date on which that notice was mailed.

(3) *Contents of statement.* The statement shall—

(i) Be clearly identified as an election under section 6223(e)(2) or (3).

(ii) Specify the election being made

(that is, application of final partnership administrative adjustment, court decision, consistent settlement agreement, or nonpartnership item treatment),

(iii) Identify the partner making the election and the partnership by name, address, and taxpayer identification number,

(iv) Specify the partnership taxable year to which the election relates, and

(v) Be signed by the partner making the election.

§301.6223(f)-1 Duplicate copy of final partnership administrative adjustment.

Section 6223(f) does not prohibit the Service from issuing a duplicate copy of the notice of final partnership administrative adjustment (for example, in the event the original notice is lost).

§301.6223(g)-1 Responsibilities of the tax matters partner.

(a) *Notices described in section 6223(a)*—(1) *Notice of beginning of proceeding.* Except as otherwise provided in §301.6223(a)-2, the tax matters partner shall, within 75 days after the mailing by the Service of the notice specified in section 6223(a)(1), forward a copy of that notice to each partner that is not entitled to notice from the Service under section 6223. See §301.6230(e)-1 for information to be furnished to the Service.

(2) *Notice of final partnership administrative adjustment.* The tax matters partner shall, within 60 days after the mailing by the Service of the notice specified in section 6223(a)(2), forward a copy of that notice to each partner that is not entitled to notice from the Service under section 6223.

(3) *Requirement inapplicable in certain cases.* The tax matters partner is not required to send notice to a partner if—

§301.6223(a)-2 Withdrawal of notice of the beginning of an administrative proceeding.

(a) *In general.* If the Internal Revenue Service, within 45 days after the day on which the notice specified in section 6223(a)(1) is mailed to the tax matters partner, decides not to propose any adjustments to the partnership return as filed, the Service may withdraw the notice specified in section 6223(a)(1) by mailing a letter to that effect to the tax matters partner within that 45-day period. If the Service withdraws the notice, neither the Service nor the tax matters partner is required to furnish any notice with respect to that proceeding to any other partner. Except as provided in paragraph (b) of this section, a notice specified in section 6223(a)(1) which has been withdrawn shall be treated for purposes of subchapter C of chapter 63 of the Code as if that notice had never been mailed to the tax matters partner.

(b) *Service may not reissue notice except under certain circumstances.* If the notice specified in section 6223(a)(1) was mailed to the tax matters partner with respect to a partnership taxable year and that notice was later withdrawn as provided in paragraph (a) of this section, the Service shall not mail a second notice specified in section 6233(a)(1) with respect to that taxable year unless:

(i) Before the expiration of the applicable 75-day or 60-day period the partnership items of that partner have become nonpartnership items (for example, by settlement),

(ii) That partner is an indirect partner and has not been identified to the tax matters partner at least 30 days before the tax matters partner is required to send such notice,

(iii) That partner is treated as a partner solely by virtue of §301.6231(a)(2)-1,

(iv) That partner was a member of a notice group as of the date on which the notice was mailed to the tax matters partner (see §301.6223(b)-1(c)(4) for the date on which a partner becomes a member of a notice group),

(v) The notice has already been provided to that partner by another person, or,

(vi) The notice is withdrawn by the Service under §301.6223(a)-2.

(b) *Other notices or information*—(1) *In general.* The tax matters partner shall furnish to the partners specified in paragraph (b)(2) of this section information with respect to the following:

(i) Closing conference with the examining agent,

(ii) Proposed adjustments, rights of appeal, and requirements for filing of a protest,

(iii) Time and place of any Appeals conference,

(iv) Acceptance by the Service of any settlement offer,

(v) Consent to the extension of the period of limitations with respect to all partners,

(vi) Filing of a request for administrative adjustment (including a request for substituted return treatment under §301.6227(b)-2) on behalf of the partnership,

(vii) Filing by the tax matters partner or any other partner of any petition for judicial review under sections 6226 or 6228(a),

(viii) Filing of any appeal with respect to any judicial determination provided for in sections 6226 or 6228(a), and

(ix) Final judicial redetermination.

(2) *Partners to be notified.* The tax matters partner shall provide information with respect to any action or other matter specified in paragraph (b)(1) of this section to all notice group representatives and all other partners except partners—

(i) Whose partnership items become nonpartnership items before the expiration of the period specified in paragraph (b)(3) of this section for furnishing that information,

(ii) Who are indirect partners and who are not identified to the tax matters partner at least 30 days before the tax matters partner is required to provide the information,

(iii) Who are treated as partners solely by virtue of §301.6231(a)(2)-1,

(iv) Who are members of a notice group as of the date on which the tax matters partner takes that action or receives information with respect to that matter (see §301.6223(b)-1(c)(4) for the date on which a partner becomes a member of a notice group), or

(v) Who have already received information with respect to the action or matter from any other person.

(3) *Time for furnishing information.* The tax matters partner shall furnish information with respect to an action or other matter described in paragraph (b)(1) of this section within 30 days of taking the action or receiving information with respect to that matter.

§301.6223(h)-1 Responsibilities of pass-thru partner.

The pass-thru partner shall, within 30 days of receiving notice or any other information regarding a partnership proceeding from the Internal Revenue

Service, the tax matters partner, or another pass-thru partner, forward a copy of that notice or information to the person or persons holding an interest through the pass-thru partner in the profits or losses of the partnership for the partnership taxable year to which the notice or information relates. In the case of a pass-thru partner which is a partnership within the meaning of section 6231(a)(1), the tax matters partner of such partnership shall forward copies of such notice or information to the partners of such partnership.

§301.6224(a)-1 Participation in administrative proceedings.

Every partner in the partnership, including an indirect partner, has the right to participate in any phase of administrative proceedings. However, except as provided in section 6223 and the regulations thereunder, neither the Service nor the tax matters partner is required to provide notice of any proceeding to partners. Consequently, a partner who wishes, for example, to be present during a preliminary discussion between an examining agent and the tax matters partner should make special arrangements with the tax matters partner to obtain information as to the time and place of the discussion. The Service and the tax matters partner will determine the time and place for all administrative proceedings. Arrangements will generally not be changed merely for the convenience of another partner.

§301.6224(b)-1 Partner may waive rights.

(a) *In general*. A partner may at any time waive any right that that partner has or any restriction on action by the Service under subchapter C of chapter 63 of the Code.

(b) *Form and manner of making waiver*. The waiver described in paragraph (a) of this section shall be made by a written statement. If the Service furnishes a form to be used for this purpose, the partner may make the waiver by completing the form in accordance with the instructions accompanying that form. If such a form is not furnished, the statement shall—

(1) Be clearly identified as a waiver under section 6224(b),

(2) Identify the partner and the partnership by name, address, and taxpayer identification number,

(3) Specify the right or restriction being waived and the taxable year(s) to which the waiver applies,

(4) Be signed by the partner making the waiver, and

(5) Be filed with the service center with which the partnership return is filed. However, if the person filing the statement knows that the notice described in section 6223(a)(1) (beginning of an administrative proceeding) has already been mailed to the tax matters partner, the statement shall be filed with the Internal Revenue Service office that mailed such notice.

§301.6224(c)-1 Tax matters partner may bind non-notice partners.

(a) *In general*. In the absence of a showing of fraud, malfeasance, or misrepresentation of fact, if the tax matters partner enters into a settlement agreement with the Service and expressly states that that agreement shall be binding on the other partners, that agreement shall be binding on all partners except those who—

(1) Are, as of the day on which the agreement is entered into, either notice partners or members of a notice group (see §301.6223(b)-1(c)(4) for the date on which a partner becomes a member of a notice group), or

(2) Have, at least 30 days before the day on which the agreement is entered into, filed with the Service the statement described in paragraph (c) of this section.

(b) *Indirect partners*—(1) *In general*. If, under paragraph (a) of this section, a pass-thru partner is not bound by an agreement entered into by the tax matters partner, all indirect partners holding an interest in the partnership through that pass-thru partner shall not be bound by that agreement. If, however, the pass-thru partner is bound by an agreement entered into by the tax matters partner, paragraph (a) of this section shall be applied separately to each indirect partner holding an interest in the partnership through that pass-thru partner to determine whether the indirect partner is also bound by the agreement.

(2) *Example*. The following example illustrates the principles set forth in this section.

Example. Partnership P has over 100 partners. Partnership J is a partner in partnership P with a profits interest of less than 1 percent. Partnership J has three partners, A, B, and C. A is a member of a notice group with respect to partnership P, but B and C are not. On July 1, 1985, B filed the statement described in paragraph (c) of this section not to be bound by any settlement agreement entered into by the tax matters partner of partnership P. On August 1, 1985, the tax matters partner of partnership P enters into a settlement agreement with the Service and states that the agreement is binding on other partners as provided in section 6224(c)(3). Since partnership J is bound by the settlement agreement, paragraph (a) of this section is applied separately to each of the indirect partners to determine whether they are bound. A is not bound by the agreement because he was a member of a notice group on the day and agreement was entered into and B is not bound because she filed the statement not to be bound at least 30 days before the agreement was entered into. C is bound by the settlement agreement.

(c) *Statement not to be bound*—(1) *Contents of statement*. The statement referred to in paragraph (a)(2) of this section shall—

(i) Be clearly identified as a statement to deny settlement authority to the tax matters partner under section 6224(c)(3)(B),

(ii) Identify the partner and partnership by name, address, and taxpayer identification number,

(iii) Specify the taxable year or years to which the statement applies, and

(iv) Be signed by the partner filing the statement.

(2) *Place where statement is to be filed*. The statement described in paragraph (c)(1) of this section generally shall be filed with the service center with which the partnership return is filed. However, if the partner knows that the notice described in section 6223(a)(1) (beginning of an administrative proceeding) has already been mailed to the tax matters partner, the statement shall be filed with the Internal Revenue Service office that mailed that notice.

(3) *Consolidated statements*. The statement described in paragraph (c)(1) of this section may be filed with respect to more than one partner if the requirements of that paragraph (c)(1)(including signatures) are satisfied with respect to each partner.

§301.6224(c)-2 Pass-thru partner binds indirect partners.

(a) *Pass-thru partner binds unidentified indirect partners*—(1) *In general*. If a pass-thru partner enters into a settlement agreement with the Service with respect to partnership items, that agreement binds all indirect partners holding an interest in that partnership through the pass-thru partner except those indirect partners who have been identified as provided in section 6223(c)(3) and §301.6223(c)-1 at least 30 days before the date on which the agreement is entered into. However, if, in addition to the interest in the partnership held through the pass-thru partner entering into a settlement agreement, an indirect partner holds a separate interest in that partnership, either directly or indirectly through a different pass-thru partner, the indirect partner shall not be bound by that settlement agreement with respect to the interests held directly or indirectly through a pass-thru partner other than the pass-thru partner entering into the settlement agreement.

(2) *Example*. The provisions of paragraph (a)(1) of this section may be illustrated by the following example:

Example. Partnership J is a partner in partnership P. C is a partner in J but has not been identified as provided in section 6223(c)(3) and §301.6223(c)-1. The only interest that C holds in P is through J. The tax matters partner of J enters into a settlement agreement with the Service with respect to partnership items arising from P. C is bound by the settlement agreement entered into by the tax matters partner of J.

(b) *Person in pass-thru partner authorized to enter into settlement agreement that binds indirect partners*. In the case of a pass-thru partner that is—

(1) A partnership within the meaning of section 6231(a)(1), the tax matters partner of that partnership;

(2) A partnership other than a partnership described in paragraph (b)(1) of this section, any general partner of that partnership;

(3) An S corporation subject to the provisions of subchapter D of chapter 63 of the Code, the tax matters person of that S corporation;

(4) An S corporation other than an S corporation described in paragraph (b)(3) of this section, any officer of that S corporation; or

(5) A trust, estate, or nominee, any person authorized in writing to act on behalf of that trust, estate, or nominee may enter into a settlement agreement with the Service on behalf of its respective entity that would bind the unidentified indirect partners that hold a partnership interest through the pass-thru partner.

§301.6224(c)-3 Consistent settlements.

(a) *In general*. If the Service enters into a settlement agreement with any partner with respect to partnership items, the Service shall offer to any other partner who so requests in accordance with paragraph (c) of this section settlement terms which are consistent with those contained in the settlement agreement entered into.

(b) *Requirements for consistent settlements*. "Consistent" settlement terms are those based on the same determinations with respect to partnership items. Settlements with respect to partnership items shall be self-contained; thus, a concession by one party with respect to a partnership item may not be based upon a concession by the other party with respect to a nonpartnership item. Settlements shall be comprehensive, that is, a settlement may not be limited to selected items. The requirement for consistent settlement terms applies only if—

(1) The items were partnership items for the partner entering into the original settlement immediately before the original settlement, and

(2) The items are partnership items for the partner requesting the consistent settlement at the time the partner files the request.

(c) *Time and manner of requesting consistent settlements*—(1) *In general*. A partner desiring settlement terms consistent with the terms of any settlement agreement entered into between any other partner and the Service shall submit a written statement to the Internal Revenue Service office that entered into the settlement.

(2) *Contents of statement*. Except as otherwise provided in instructions to the taxpayer from the Service, the written statement described in paragraph (c)(1) of this section shall—

(i) Identify the statement as a request for consistent settlement terms under section 6224(c)(2),

(ii) Contain the name, address, and taxpayer identification number of the partnership and of the partner requesting the settlement offer (and, in the case of an indirect partner, of the pass-thru partner through which the indirect partner holds an interest),

(iii) Identify the earlier agreement to which the request refers, and

(iv) Be signed by the partner making the request.

(3) *Time for filing request*. The statement shall be filed not later than the later of—

(i) The 150th day after the day on which the notice of final partnership administrative adjustment is mailed to the tax matters partner, or

(ii) The 60th day after the day on which the settlement was entered into.

(d) *Examples*. The following examples illustrate the principles set out in this section.

Example (1). The Service seeks to disallow a $100,000 loss reported by Partnership P. The Service agrees to a settlement with X, a partner in P, in which the Service allows 60 percent of the loss and accepts the treatment of all other partnership items on the partnership return. Partner Y, which owns a 10 percent interest in the partnership, requests settlement terms which are consistent with the settlement made between X and the Service. The items are partnership items for X immediately before X enters into the settlement agreement and partnership items for Y at the time of the request. The Service must offer Y a settlement agreement allowing a $6,000 loss and otherwise reflecting the treatment of partnership items on the partnership return.

Example (2). F files inconsistently with partnership P and reports the inconsistency. The Service notifies F that it will treat all partnership items arising from P as nonpartnership items with respect to F. Later, the Service enters into a settlement agreement with F on these items. The Service is not required to offer the other partners of P settlement terms consistent with the settlement reached between F and the Service because at the time of the settlement the items arising from P are no longer partnership items with respect to F.

Example (3). G, a partner in Partnership P, filed suit under section 6228(b) after the Service failed to allow an administrative adjustment request with respect to a partnership item arising from P for a taxable year. Under section 6231(b)(1)(B), the partnership items of G for the partnership taxable year became nonpartnership items as of the date the suit was filed. After G filed suit, another partner and the Service entered into a settlement agreement with respect to items arising from P in that year. G is not entitled to consistent settlement terms because the items arising from P are no longer partnership items with respect to G.

§301.6226(a)-1 Principal place of business of partnership.

(a) *In general*. The principal place of business of a partnership for purposes of determining the appropriate district court in which a petition for a readjustment of partnership items may be filed is its principal place of business as of the date the petition is filed.

(b) *Example*. The provisions of paragraph (a) of this section may be illustrated by the following example:

Example. The principal place of business of partnership A on the day that the the notice of the final partnership administrative adjustment was mailed to the tax matters partner of A was

Cincinnati, Ohio. However, by the day on which a petition seeking judicial review of that adjustment was filed, A had moved its principal place of business to Louisville, Kentucky. For purposes of section 6226(a)(2), A's principal place of business is Louisville.

§301.6226(b)-1 5-percent group.

All members of a 5-percent group shall join in filing any petition for judicial review. The designation of partner as a representative of a notice group does not authorize that partner to file a petition for a readjustment of partnership items on behalf of the notice group.

§301.6226(e)-1 Jurisdictional requirement for bringing an action in District Court or Claims Court.

(a) *Amount to be deposited*—(1) *In general*. The jurisdictional amount that the filing partner (or, in the case of a petition filed by a 5-percent group, each member of the group) shall deposit is the amount by which the tax liability of the partner would be increased if the treatment of the partnership items on the partner's return were made consistent with the treatment of partnership items on the partnership return, as adjusted by the notice of final partnership administrative adjustment. The partner is not required to pay other outstanding liabilities in order to deposit a jurisdictional amount.

(2) *Example*. The provisions of paragraph (a)(1) of this section may be illustrated by the following example:

Example. A files a petition for readjustment of partnership items in the Claims Court. A's tax liability would be increased by $4,000 if partnership items on his return were conformed to the partnership return, as adjusted by the notice of final partnership administrative adjustment. A has an unpaid liability of $10,000 attributable to nonpartnership items. A is required to deposit only $4,000 in order to satisfy the jurisdictional requirement.

(b) *Deposit taken into account in computing interest*. The amount deposited is treated as a payment of tax for purposes of chapter 67 (relating to interest). Thus, the period of deposit will be treated as a period of payment for purposes of determining the interest due on any overpayment or underpayment and computing any penalty under section 6653(a)(2) or (b)(2).

(c) *Deposit generally not treated as payment of tax*. Except as provided in paragraph (b) of this section, an amount deposited under section 6226(e) shall not be treated as payment of tax. Thus, the Service may proceed against the depositor for a deficiency based on nonpartnership items without regard to this deposit.

(d) *Amount deposited may be applied against assessment*. If the restriction on assessment provided under section 6225(a) lapses with respect to a deficiency attributable to partnership items for a partnership taxable year while an amount is on deposit under section 6226(e) in connection with a petition relating to those items, the Service may apply the amount deposited against any such deficiency that is assessed.

§301.6226(f)-1 Scope of judicial review.

(a) *In general*. A court reviewing a notice of final partnership administrative adjustment has jurisdiction to determine all partnership items for the taxable year to which the notice relates and the proper allocation of such items among the partners. Thus, the review is not limited to the items adjusted in the notice.

(b) *Example*. The provisions of paragraph (a) of this section may be illustrated by the following example.

Example. The Service issues a notice of final partnership administrative adjustment with respect to Partnership ABC in which the only item adjusted is depreciation. A petition for judicial review of that notice is filed. During the judicial proceeding, a partner of ABC, in accordance with the applicable court rules, raises an issue relating to the treatment of intangible drilling costs. The court reviewing the notice has jurisdiction to determine the intangible drilling cost issue as well as the depreciation issue.

§301.6227(b)-1 Administrative adjustment request by the tax matters partner on behalf of the partnership.

(a) *In general*. A request for an administrative adjustment filed by the tax matters partner on behalf of the partnership shall be filed on the form prescribed by the Service for that purpose in accordance with the instructions accompanying that form. Except as otherwise provided in the instructions accompanying that form, the request shall be—

(1) Filed with the service center where the original partnership return was filed,

(2) Signed by the tax matters partner, and

(3) Accompanied by revised schedules showing the effects of the proposed changes on each partner and an explanation of the changes.

(b) *Denied request for treatment as a substituted return remains administrative adjustment request*. An administrative adjustment request filed by the tax matters partner on behalf of the partnership for which substituted return treatment is requested but not granted remains an administrative adjustment request. Thus, for example, the tax matters partner may file suit under section 6228(a) if the Service fails to take timely action on the request.

§301.6227(c)-1 Administrative adjustment request filed on behalf of a partner.

A request for an administrative adjustment on behalf of a partner shall be filed on the form prescribed by the Service for that purpose in accordance with the instructions accompanying that form. Except as otherwise provided in the instructions accompanying that form, the request shall—

(a) Be filed in duplicate, the original copy filed with the partner's amended income tax return (on which the partner computes the amount by which the partner's tax liability should be adjusted if the request is granted) and the other copy filed with the service center where the partnership return is filed,

(b) Identify the partner and the partnership by name, address, and taxpayer identification number,

(c) Specify the partnership taxable year to which the administrative adjustment request applies,

(d) Relate only to partnership items, and

(e) Relate only to one partnership and one partnership taxable year.

§301.6229(b)-1 Extension by agreement.

Any partnership may authorize any person to extend the period described in section 6229(a) with respect to all partners by filing a statement to that effect with the service center with which the partnership return is filed. The statement shall—

(a) Provide that it is an authorization for a person other than the tax matters partner to extend the assessment period with respect to all partners,

(b) Identify the partnership and the person being authorized by name, address, and taxpayer identification number,

(c) Specify the partnership taxable year or years for which the authorization is effective, and

(d) Be signed by all persons who were general partners at any time during the year or years for which the authorization is effective.

§301.6229(e)-1 Information with respect to unidentified partner.

A partner who is not properly identified on the partnership return (including an indirect partner) remains an unidentified partner for purposes of section 6229(e) until identifying information is furnished asprovided in §301.65223(c)-1.

§301.6230(b)-1 Request that correction not be made.

The request that a correction not be made under section 6230(b)(2) shall be in writing and shall—

(a) State that it is a request that a correction not be made under section 6230(b),

(b) Identify the partnership and the partner filing the request by name, address, and taxpayer identification number,

(c) Be signed by the partner filing the request, and

(d) Be filed with the Internal Revenue Service office that provided the notice of the correction of the error.

§301.6230(c)-1 Claim arising out of erroneous computation, etc.

A claim for refund under section 6230(c) shall state the grounds for the claim and shall be filed with the service center with which the partner's return is filed.

§301.6230(e)-1 Tax matters partner required to furnish names.

(a) *In general.* If a notice of the beginning of an administrative proceeding is mailed to the tax matters partner with respect to any partnership taxable year, the tax matters partner shall furnish to the Internal Revenue Service office that issued the notice the name, address, profits interest, and taxpayer identification number of each person who was a partner in the partnership at any time during that taxable year if that information was not provided on the partnership return filed for that year.

(b) *Revised or additional information.* If the tax matters partner discovers that any information furnished to the Service on the partnership return or under paragraph (a) of this section was incorrect or incomplete, the tax matters partner shall furnish revised or additional information to the Service within 15 days of discovering that the information furnished to the Service was incorrect or incomplete.

(c) *Information required with respect to indirect partners.* The requirements of this section for identifying information apply with respect to indirect partners to the extent that the tax matters partner has such information.

§301.6231(a)(1)-1 Exception for small partnerships.

(a) *In general.* For purposes of the exception for small partnerships under section 6231(a)(1)(B) the rules contained in this section shall apply.

(1) *"10 or fewer."* The "10 or fewer" limitation described in section 6231(a)(1)(B)(i)(I) is applied to the number of natural persons (other than nonresident aliens) and estates that were partners at any one time during the partnership taxable year. Thus, for example, a partnership that at no time during the taxable year had more than 10 partners may be treated as a small partnership even if, because of transfers of interests in the partnership, 11 or more natural persons or estates owned interests in the partnership for some portion of the taxable year. For purposes of section 6231(a)(1)(B) and this section, a husband and wife (and their estates) are treated as one person.

(2) *Pass-thru partner.* The exception provided in section 6231(a)(1)(B) does not apply to a partnership for a taxable year if any partner in the partnership during that taxable year is a pass-thru partner. For purposes of this paragraph (a)(2), an estate shall not be treated as a pass-thru partner.

(3) *"Same share."* The requirement of section 6231(a)(1)(B)(i)(II) is satisfied for a taxable year if during all periods within that taxable year each partner's share of each of the partnership items specified in §301.6231(a)(3)-1(a)(1)(i) through (iv) is the same as that partner's share of each of the other partnership items specified in that section during that period (even though the partner's share of all such specified partnership items changes from period to period within that taxable year). Thus, a partner whose share of all such specified partnership items changes as a result of a sale or redemption of a partnership interest (or portion thereof) or a contribution of cash or property to the partnership during the partnership taxable year shall satisfy the same share requirement if during the period before the sale, redemption, or contribution the partner's share of each specified partnership item is the same as all other specified partnership items and during the period after the sale, redemption, on contribution the partner's share of each specified partnership item is the same as all other specified partnership items. For purposes of section 6231(a)(1)(B)(i)(II) and this section, if each partner's share of each partnership item would be the same as his or her share of every other item but for allocations made under section 704(c) or allocations made under similar principles in accordance with applicable regulations the requirement of section 6231(a)(1)(B)(i)(II) shall be considered satisfied. Similarly, special basis adjustments pursuant to sections 754, 743, and 734 shall not be taken into account in determining whether the "same share" requirement is met.

(4) *Determination made annually.* The determination of whether a partnership meets the requirements for the exception for small partnerships under section 6231(a)(1)(B) and this paragraph (a) shall be made with respect to each partnership taxable year. Thus, a partnership that does not qualify as a small partnership in one taxable year may qualify as a small partnership in another taxable year if the requirements for the exception under section 6231(a)(1)(B) and this paragraph (a) are met with respect to that other taxable year.

(b) *Election to have subchapter C of chapter 63 apply*—(1) *General.* Any partnership that meets the requirements set forth in section 6231(a)(1)(B) of the Code and paragraph (a) of this section (relating to the exception for small partnerships) may elect under paragraph (b)(2) of this section to have the provisions of subchapter C of chapter 63 of the Code apply with respect to that partnership.

(2) *Method of election.* A partnership shall make the election described in paragraph (b)(1) of this section by attaching a statement to the partnership

return for the first taxable year for which the election is to be effective. The statement shall be identified as an election under section 6231(a)(1)(B)(ii), shall be signed by all persons who were partners of that partnership at any time during the partnership taxable year to which the return relates, and shall be filed at the time (determined with regard to any extension of time for filing) and place prescribed for filing the partnership return. However, for partnership taxable years for which a partnership return is to be filed before 90 days after the date final regulations under this section are published in the FEDERAL REGISTER the partnership may file the statement described in the preceding sentence on or before the date which is one year before the date specified in section 6229(a) for the expiration of the period of limitations with respect to that partnership (determined with regard to extensions of that period under section 6229(b)).

(3) *Years covered by election*. The election shall be effective for the partnership taxable year to which the return relates and all subsequent partnership taxable years unless revoked with the consent of the Commissioner.

§301.6231(a)(2)-1 Persons whose tax liability is determined indirectly by partnership items.

(a) *Spouse filing joint return with individual holding separate interest*—(1) *In general*. Except as otherwise provided in this paragraph (a), a spouse who files a joint return with an individual holding a separate interest in the partnership shall be treated as a partner for purposes of subchapter C of chapter 63 of the Code. Thus, the spouse who files a joint return with a partner will be permitted to participate in administrative and judicial proceedings.

(2) *Counting rules*. A spouse who files a joint return with an individual holding a separate interest in the partnership shall not be counted as a partner for purposes of applying section 6223(b) (relating to special rules for partnerships with more than 100 partners) and section 6231(a)(1)(B) (relating to the exception for small partnerships).

(3) *Notice rules*—(i) *In general*. Except as provided in paragraph (a)(3)(ii) of this section, for purposes of subchapter C of chapter 63 of the Code, a spouse who files a joint return with an individual holding a separate interest in the partnership shall be treated as receiving any notice received by the individual holding the separate interest.

(ii) *Spouse identified on partnership return or by statement*. Paragraph (a)(3)(i) of this section shall not apply to a spouse who files a joint return with an individual holding a separate interest in the partnership if that spouse:

(A) Is identified on the partnership return; or

(B) Is identified as a partner entitled to notice as provided in §301.6223(c)-1(b).

(4) *Cross-reference*. See §301.6231(a)(12)-1 for special rules relating to spouses holding a joint interest in a partnership.

(b) *Shareholder of C corporation*. A shareholder of a C corporation (as defined in section 1361(a)(2)) is not a partner in a partnership merely because the C corporation is a partner in that partnership.

§301.6231(a)(5)-1 Definition of affected item.

(a) *In general*. The term "affected item" includes items unrelated to the items reflected on the partnership return (for example, an item such as the threshold for the medical expenses deduction under section 213, that varies if there is a change in an individual partner's adjusted gross income).

(b) *Partner's basis in his partnership interest*. A partner's basis in his interest in the partnership is an affected item to the extent it is not a partnership item.

(c) *At-risk limitation*. The application of the at-risk limitation under section 465 to a partner with respect to a loss flowing from partnership is an affected item to the extent it is not a partnership item.

(d) *Addition to tax or additional amount*—(1) *In general*. The term "affected item" includes any addition to tax or additional amount provided by subchapter A of chapter 68 of the Internal Revenue Code of 1954 to the extent provided in this paragraph (d).

(2) *Addition to tax or additional amount without floor*. In the case where an addition to tax or additional amount that does not contain a floor (that is, a threshold amount of underpayment or understatement necessary before the imposition of the addition to tax or additional amount) is imposed on a partner as the result of an adjustment to a partnership item, the term "affected item" shall include the addition to tax or additional amount computed with reference to the entire under payment or understatement.

(3) *Addition to tax or additional amount containing floor*—(i) *Floor exceeded prior to adjustment*. In the case where a partner would have been subject to an addition to tax or additional amount that contains a floor in the absence of an adjustment to a partnership item (that is, the partner's understatement or underpayment exceeded the floor even without an adjustment to a partnership item) the term "affected item" shall include only the addition to tax or additional amount computed with reference to the partnership item (or affected item).

(ii) *Floor not exceeded prior to adjustment*. In the case of an addition to tax or additional amount that contains a floor, if the taxpayer's understatement or underpayment does not exceed the floor prior to an adjustment to a partnership item but does so after such adjustment, the term "affected item" shall include the addition to tax or additional amount computed with reference to the entire underpayment or understatement.

(4) *Examples*. The provisions of this paragraph (d) may be illustrated by the following examples:

Example (1). A, a partner of P, had an aggregate underpayment of $1000 of which $100 is attributable to an adjustment to partnership items. A is negligent in reporting the partnership items. The addition to tax for negligence computed with reference to the entire $1000 underpayment is an affected item.

Example (2). B, a partner in partnership P, understated his income tax liability attributable to nonpartnership items by $6,000. An adjustment to a partnership item resulting from a partnership providing increased B's income tax by an additional $2,000. Prior to the adjustment, B would have been subject to the addition to tax under section 6661 with respect to the $6,000 understatement. The addition to tax under section 6661 computed with reference to the $2,000 increase is an affected item. The addition to tax computed with reference to the $6,000 pre-existing understatement is not an affected item.

Example (3). C, a partner in partnership P, understated his income tax liability attributable to nonpartnership items by $4,000. As a result of adjustment to partnership items, that understatement is increased to $10,000. Prior to the adjustment, C would not have been subject to any addition to tax under section 6661. The section 6661 addition to tax computed with reference to the entire $10,000 underpayment is an affected item.

§301.6231(a)(6)-1 Computational adjustments.

(a) *In general.* A change in the tax liability of a partner to properly reflect the treatment of a partnership item under subchapter C of chapter 63 of the Code is made through a computational adjustment. A computational adjustment may include a change in tax liability that reflects a change in an affected item where that change is necessary to properly reflect the treatment of a partnership item. However, if a change in a partner's tax liability cannot be made without making one or more partner-level determinations, that portion of the change in tax liability attributable to the partner-level determinations shall be made under the provisions of subchapter B of chapter 63 of the Code (relating to deficiency procedures). Thus, changes in a partner's tax liability with respect to affected items that do not require partner-level determinations (such as the threshold amount for medical deductions under section 213 that changes as the result of determinations made at the partnership level) are included in a computational adjustment. However, changes in a partner's tax liability with respect to affected items that require partner-level determinations (such as a partner's at-risk amount that depends upon the source from which the partner obtained the funds that the partner contributed to the partnership) are not included in a computational adjustment.

(b) *Interest.* A computational adjustment includes any interest due with respect to any underpayment or overpayment of tax attributable to adjustments to reflect properly the treatment of partnership items.

(c) *Addition to tax or additional amount.* A computational adjustment shall not include an addition to tax or additional amount. Regardless of whether an addition to tax or additional amount is an affected item within the meaning of section 6231(a)(5) and §301.6231(a)(5)-1, the addition to tax or additional amount shall be subject to the provisions of subchapter B of chapter 63 of the Code (relating to deficiency procedures). See section 6229(a) for the period of limitations for making assessments with respect to affected items.

§301.6231(a)(7)-1 Designation of tax matters partner.

(a) *In general.* A partnership may designate a partner as its tax matters partner for a specific taxable year only as provided in this section. Similarly, the designation of a partner as the tax matters partner for a specific taxable year may be terminated only as provided in this section.

(b) *Persons who may be designated tax matters partner*—(1) *General requirement.* A person may be designated as the tax matters partner of a partnership for a taxable year only if that person—

(i) Was a general partner in the partnership at some time during the taxable year for which the designation is made, or

(ii) Is a general partner in the partnership as of the time the designation is made.

(2) *Limitation on designation of tax matters partner who is not a United States person.* If any United States person would be eligible under paragraph (a) of this section to be designated as the tax matters partner of a partnership for a taxable year, no person who is not a United States person may be designated as the tax matters partner of the partnership for that year without the consent of the Commissioner. For the definition of the term "United States person," see section 7701(a)(30).

(c) *Designation of tax matters partner at time partnership return is filed*—(1) *If the form provided for the partnership return contains space for designation.* If the form provided for the partnership return for a taxable year contains a space for the designation of a tax matters partner, the partnership may designate a tax matters partner for that partnership taxable year on the partnership return in accordance with the instructions for that form.

(2) *If form does not contain space for designation.* If the form provided for the partnership return for a taxable year does not contain a space for the designation of a tax matters partner, the partnership may make the designation by attaching a statement to the partnership return for that year, filed at the time (determined with regard to any extension of time for filing) and place prescribed for filing the partnership return. The statement shall—

(i) Identify the partnership and the designated tax matters partner by name, address, and taxpayer identification number,

(ii) Declare that it is designation of a tax matters partner for the taxable year to which the return relates, and

(iii) Be signed by the partner signing the partnership return.

(d) *Certification by current tax matters partner of selection of successor.* If a partner properly designated as the tax matters partner of a partnership for a partnership taxable year under this section certifies that another partner has been selected as the tax matters partner of the partnership for that taxable year, that other partner is thereby designated as the tax matters partner for that year. The current tax matters partner shall make the certification by filing with the service center with which the partnership return is filed a statement that—

(1) Identifies the partnership, the partner filing the statement, and the successor tax matters partner by name, address, and taxpayer identification number,

(2) Specifies the partnership taxable year to which the designation relates,

(3) Declares that the partner filing the statement has been properly designated as the tax matters partner of the partnership for the partnership taxable year and that that designation is in effect immediately before the filing of the statement,

(4) Certifies that the other named partner has been selected as the tax matters partner of the partnership for that taxable year in accordance with the partnership's procedure for making that selection, and

(5) Is signed by the partner filing the statement.

(e) *Designation by general partners with majority interest.* The partnership may designate a tax matters partner for a partnership taxable year at any time after the filing of a partnership return for that taxable year by filing a statement with the service center with which the partnership return was filed. The statement shall—

(1) Identify the partnership and the designated partner by name, address, and taxpayer identification number,

(2) Specify the partnership taxable year to which the designation relates,

(3) Declare that it is a designation of a tax matters partner for the taxable year specified, and

(4) Be signed by persons who were general partners at the close of the year and were shown on the return for that year to hold more than 50 percent of

the aggregate interest in partnership profits held by all general partners as of the close of that taxable year. For purposes of this paragraph (e)(4), all limited partnership interests held by general partners shall be included in determining the aggregate interest in partnership profits held by such general partners.

(f) *Designation by partners with majority interest under certain circumstances*—(1) *In general*. A tax matters partner may be designated for a partnership taxable year under this paragraph (f) only if, at the time the designation is made, each partner who was a general partner at the close of such partnership taxable year is described in one or more of the following subdivisions of this paragraph (f)(1).

(i) The general partner is dead, or, if the general partner is an entity, has been liquidated or dissolved;

(ii) The general partner has been adjudicated by a court of competent jurisdiction to be no longer capable of managing his or her person or estate;

(iii) The general partner's partnership items have become nonpartnership items under section 6231(b); or

(iv) The general partner is no longer a partner in the partnership.

(2) *Method of making designation*. A tax matters partner for a partnership taxable year may be designated under this paragraph (f) at any time after the filing of the partnership return for such taxable year by filing a written statement with the service center with which the partnership return was filed. The statement shall—

(i) Identify the partnership and the designated tax matters partner by name, address, and taxpayer identification number,

(ii) Specify the partnership taxable year to which the designation relates,

(iii) Declare that is a designation of a tax matters partner for the partnership taxable year specified, and

(iv) Be signed by persons who were partners at the close of such taxable year and were shown on the return for that year to hold more than 50 percent of the aggregate interest in partnership profits held by all partners as of the close of such taxable year.

(g) *Designation of alternate tax matters partner*. If an individual is designated as the tax matters partner of a partnership under paragraph (c), (d), (e), or (f) of this section, the document by which that individuals designated may also designate an alternate tax matters partner who will become tax matters partner upon the occurrence of one or more of the events described in paragraph (l)(1) or (2) of this section. The person designated as the alternate tax matters partner becomes the tax matters partner as of the time the designation of the tax matters partner is terminated under paragraph (l)(1) or (2) of this section. The destination of a person as the alternate tax matters partner shall have no effect in any other case.

(h) *Prior designations superseded*. A designation of a tax matters partner for a partnership taxable year under paragraphs (d), (e), or (f) of this section shall supersede all prior designations of a tax matters partner for that year, including a prior designation of an alternate tax matters partner under paragraph (g) of this section.

(i) *Resignation of designated tax matters partner*. A person designated as the tax matters partner of a partnership under this section may resign at any time by a written statement to that effect. The statement shall specify the partnership taxable year to which the resignation relates and shall identify the partnership and the tax matters partner by name, address, and taxpayer identification number. The statement shall also be signed by the resigning tax matters partner and shall be filed with the service center with which the partnership return was filed.

(j) *Revocation of designation*. The partnership may revoke the designation of the tax matters partner for a partnership taxable year at any time after the filing of a partnership return for that taxable year by filing a statement with the service center with which the partnership return was filed. The statement shall—

(1) Identify by name, address, and taxpayer identification number the partnership and the general partner whose designation as tax matters partner is being revoked,

(2) Specify the partnership taxable year to which the revocation relates,

(3) Declare that it is a revocation of a designation of the tax matters partner for the taxable year specified, and

(4) Be signed by the persons described in paragraph (e)(4) of this section, or, if at the time that the revocation is made, each partner who was a general partner at the close of the partnership taxable year to which the revocation relates is described in one or more of subdivisions (i) through (iv) of paragraph (f)(1) of this section, by the persons described in paragraph (f)(2)(iv) of this section.

(k) *When designation, etc., becomes effective*—(1) *In general*. Except as otherwise provided in paragraph (k)(2) of this section, a designation, resignation, or revocation provided for in this section becomes effective on the day that the statement required by the applicable paragraph of this section is filed.

(2) *Notice of proceeding mailed*. If a notice of beginning of an administrative proceeding with respect to a partnership taxable year is mailed before the date on which a statement of designation, resignation, or revocation provided for in this section with respect to that taxable year is filed, the Service is not required to give effect to such designation, resignation, or revocation until 30 days after the statement is filed.

(l) *Termination of designation*. A designation of a tax matters partner for a taxable year under this section shall remain in effect until—

(1) The death of the designated tax matters partner,

(2) An adjudication by a court of competent jurisdiction that the individual designated as the tax matters partner is no longer capable of managing the individual's person or estate,

(3) The liquidation or dissolution of the tax matters partner, if the tax matters partner is an entity,

(4) The partnership items of the tax matters partner become nonpartnership items under section 6231(c) (relating to special enforcement areas), or

(5) The day on which—

(i) The resignation of the tax matters partner under paragraph (i) of this section,

(ii) A subsequent designation under paragraph (d), (e), or (f) of this section, or

(iii) A revocation of the designation under paragraph (j) of this section becomes effective.

The termination of the designation of a partner as the tax matters partner under this paragraph (l) does not affect the validity of any action taken by that partner as tax matters partner before the designation is terminated. For example, if that tax matters partner had previously consented to an extension of the period for assessment sunder section 6229(b)(1)(B), that extension remains valid even after termination of the designation.

(m) *Tax matters partner where no partnership designation made*—(1) *In general.* The tax matters partner for a partnership taxable year shall be determined under this paragraph (m) if:

(i) The partnership has not designated a tax matters partner under this section for that taxable year; or

(ii) The partnership has designated a tax matters partner under this section for that taxable year, that designation has been terminated under paragraph (l) of this section, and the partnership has not made a subsequent designation under this section for that taxable year.

(2) *General partner having the largest profits interest is the tax matters partner.* The tax matters partner for any partnership taxable year to which this paragraph (m) applies is the general partner having the largest profits interest in the partnership at the close of that taxable year (or where there is more than one such partner, the one of such partners whose name would appear first in an alphabetical listing). For purposes of this paragraph (m)(2), all limited partnership interests held by a general partner shall be included in determining that general partner's profits interest in the partnership.

(3) *Termination of designation.* A designation of a tax matters partner for a partnership taxable year under this paragraph (m) shall remain in effect until the earlier of the occurrance of one or more of the events described in paragraph (l)(1) through (4) or the day on which a designation under paragraph (d), (e), or (f) of this section becomes effective. If a designation of a tax matters partner for a partnership taxable year is terminated under this paragraph (m)(3) and the partnership has not subsequently designated a tax matters partner for that taxable year under paragraph (d), (e), or (f) of this section the tax matters partner for that taxable year shall be determined under paragraph (m)(2) of this section and, for purposes of applying that paragraph (m)(2), the general partner whose designation was so terminated shall be treated as having no profits interest in the partnership for that taxable year.

§301.6231(a)(12)-1 Special rules relating to spouses.

(a) *In general.* For purposes of subchapter C of chapter 63 of the Code, spouses holding a joint interest in a partnership are treated as partners. Thus, both spouses are permitted to participate in administrative and judicial proceedings. The term "joint interest" includes tenancies in common, joint tenancies, tenancies by the entirety, and community property.

(b) *Notice and counting rules*—(1) *In general.* Except as provided in paragraph (b)(2) of this section, for purposes of applying section 6223 (relating to notice to partners of proceedings) and section 6231(a)(1)(B) (relating to the exception for small partnerships), spouses holding a joint interest in a partnership shall be treated as one person. Except as provided in paragraph (b)(2) of this section, the Service or the tax matters partner may send any required notice to either spouse.

(2) *Identified spouse entitled to notice.* For purposes of applying section 6223 (relating to notice to partners of proceeding) for a partnership taxable year an individual who holds a joint interest in a partnership with his or her spouse who is entitled to notice under section 6223 shall be entitled to receive separate notice under section 6223 if such individual:

(i) Is identified as a partner on the partnership return for that taxable year; or

(ii) Is identified as a partner entitled to notice as provided in §301.6223(c)-1(b).

(c) *Cross-reference.* See §301.6231(a)(2)-1(a) for special rules relating to spouses who file joint returns with individuals holding a separate interest in a partnership.

§301.6231(c)-3 Limitation on applicability of §§301.6231(c)-4 through 301.6231(c)-8.

A provision of §§301.6231(c)-4 through 301.6231(c)-8 shall not apply with respect to partnership items arising in a partnership taxable year if, as of the date on which those items would otherwise begin to be treated as nonpartnership items under that provision—

(a) A notice of final partnership administrative adjustment with respect to those items has been mailed to the tax matters partner, and

(b) Either—

(1) The period during which an action with respect to that final partnership administrative adjustment may be brought under section 6226 has expired and no such action has been brought, or

(2) The decision of the court in an action brought under section 6226 with respect to that final partnership administrative adjustment has become final.

§301.6231(c)-4 Termination and jeopardy assessment.

The treatment of items as partnership items with respect to a partner against whom an assessment of income tax under section 6851 (termination assessment) or section 6861 (jeopardy assessment) is made will interfere with the effective and efficient enforcement of the internal revenue laws. Accordingly, partnership items of such a partner arising in any partnership taxable year ending with or within the partner's taxable year for which an assessment of income tax under section 6851 or section 6861 is made shall be treated as nonpartnership items as of the moment before such assessment is made.

§301.6231(c)-5 Criminal investigations.

The treatment of items as partnership items with respect to a partner under criminal investigation for violation of the internal revenue laws relating to income tax will interfere with the effective and efficient enforcement of the internal revenue laws. Accordingly, partnership items of such a partner arising in any partnership taxable year ending on or before the last day of the latest taxable year of the partner to which the criminal investigation relates shall be treated as nonpartnership items as of the date on which the partner is notified that he or she is the subject of a criminal investigation and receives written notification from the Service that his or her partnership items shall be treated as nonpartnership items. The partnership items of a partner who is notified that he or she is the subject of a criminal investigation shall not be treated as nonpartnership items under this section unless and until such partner receives written notification from the Service of such treatment.

§301.6231(c)-6 Indirect method of proof of income.

The treatment of items as partnership items with respect to a partner whose taxable income is determined by use of an indirect method of proof of income will interfere with the effective and efficient enforcement of the internal revenue laws. Accordingly, partnership items of such a partner arising in any partnership taxable year ending on or before the last day of the taxable year of the partner for which a deficiency notice based upon an indirect method of proof of income is mailed to the partner shall be treated as nonpartnership items as of the date on which that hat deficiency notice is mailed to the partner.

§301.6231(c)-7 Bankruptcy and receivership.

(a) *Bankruptcy*. The treatment of items as partnership items with respect to a partner named as a debtor in a bankruptcy proceeding will interfere with the effective and efficient enforcement of the internal revenue laws. Accordingly, partnership items of such a partner arising in any partnership taxable year ending on or before the last day of the latest taxable year of the partner with respect to which the United States could file a claim for income tax due in the bankruptcy proceeding shall be treated as nonpartnership items as of the date the petition naming the partner as debtor is filed in bankruptcy.

(b) *Receivership*. The treatment of items as partnership items with respect to a partner for whom a receiver has been appointed in any receivership proceeding before any court of the United States or of any State or the District of Columbia will interfere with the effective and efficient enforcement of the internal revenue laws. Accordingly, partnership items of such a partner arising in any partnership taxable year ending on or before the last day of the latest taxable year of the partner with respect to which the United States could file a claim for income tax due in the receivership proceeding shall be treated as nonpartnership items as of the date a receiver is appointed in any receivership proceeding before any court of the United States or of any State or the District of Columbia.

§301.6231(c)-8 Prompt assessment.

The treatment of items as partnership items with respect to a partner on whose behalf a request for a prompt assessment of tax under section 6501(d) is filed will interfere with the effective and efficient enforcement of the internal revenue laws. Accordingly, partnership items of such a partner arising in any partnership taxable year ending with or within any taxable year of the partner with respect to which a request for a prompt assessment of tax is filed shall be treated as nonpartnership items as of the date that the request is filed.

§301.6231(d)-1 Time for determining profits interest of partners for purposes of sections 6223(b) and 6231(a)(11).

(a) *Partner owns interest at close of year*. For purposes of section 6223(b) (relating to special rules for partnerships with more than 100 partners) and section 6231(a)(11) (relating to 5-percent groups), except as otherwise provided in this section, the profits interest held by a partner, directly or indirectly through one or more pass-thru partners, in a partnership (the "audit partnership") to which subchapter C of chapter 63 of the Code applies shall be determined at the close of the audit partnership's taxable year.

(b) *Partner does not own interest at close of year*. If the entire direct and indirect interest of a partner in an audit partnership is terminated by virtue of a disposition by such partner of such interest (or by virtue of the disposition of an interest held by one or more pass-thru partners through which the partner holds an interest), then the profits interest of such partner in the audit partnership shall be measured as of the moment before the disposition causing such termination. The preceding sentence shall not apply with respect to a termination if subsequent to such termination and before the close of the audit partnership's taxable year the partner acquires a direct or indirect interest in the audit partnership.

(c) *Disposition of last remaining portion of interest is disposition of entire interest*. If a partner (or a pass-thru partner through which a partner holds an interest) makes several partial dispositions of an interest in an audit partnership during a taxable year of the audit partnership, paragraph (b) of this section will apply with respect to the disposition which causes a termination of the partner's entire direct and indirect interest in the audit partnership.

(d) *No profits interest in certain cases*. If—

(1) The interest of a partner in a partnership is entirely disposed of before the close of the taxable year of the partnership, and

(2) No items of the partnership for that taxable year are required to be taken into account by the partner,

that partner has no profits interest in the partnership for that taxable year. For example, if a partner dies before the close of the taxable year of the partnership, generally no items of the partnership for that taxable year are required to be taken into account on the final return of the deceased partner under §1.706-1(c)(3); consequently, the deceased partner has no profits interest in the partnership for that taxable year.

(e) *Examples*. The provisions of this section may be illustrated by the following examples. Assume in all examples that there have been no reacquisitions prior to the close of the audit partnership's taxable year.

Example (1). B holds an interest in partnership P through T, a pass-thru partner. P uses a fiscal year ending June 30 as P's taxable year; B and T use the calendar year as the taxable year. As of the close of P's taxable year ending June 30, 1985, T holds an interest in P and B holds an interest in P through T. The profits interest held by B in P through T for that year is determined as of June 30, 1985.

Example (2). Assume the same facts as in example (1), except that B sold the entire interest that B held in P through T on November 4, 1984. The profits interest held by B in P through T for P's taxable year ending June 30, 1985, is determined as of the moment before the sale on November 5, 1984.

Example (3) C holds an interest in partnership P through T, a pass-thru partner. C, P, and T all use the calendar year as the taxable year. T disposes of T's interest in P on June 5, 1985. The profits interest held by C in P through T for 1985 is determined as of the moment before the disposition on June 5, 1985.

Example (4) Assume the same facts as in example (3), except that C sold her entire interest in T (and, therefore, her entire interest that she held in P through T) on March 15, 1985. The profits interest held by C in P through T for 1985 is determined as of the moment before the sale on March 15, 1985.

Example (5) On January 1, 1985, D held a 2 percent profits interest in partnership P. Both D and P use the calendar year as the taxable year. On August 1, 1985, D transfers three-fourths of D's profits interest in P to E. On September 1, 1985, D sells his remaining .5 profits interest in P to F. For purposes of sections 6223(b) and 6231(a)(11), D had a .5 percent profits interest in P for 1985.

Example (6) Assume the same facts as in example (5), except that on January 1, 1985, D also held a 1 percent profits interest in partnership P through T, a pass-thru partner which also uses the calendar year as the taxable year. In addition to the sale to E on August 1, 1985, D sold a portion of his interest in T on December 1, 1985, such that after the sale, D held a .2 percent profits interest in P through T. D made no other transfers of interests in either P or T. For purposes of sections 6223(b) and 6231(a)(11), D had a .7 percent profits interest in P for 1985.

§301.6231(e)-1 Effect of a determination with respect to a nonpartnership item on the determination of a partnership item.

The determination of an item after it has become a nonpartnership item with respect to a partner is not controlling in the determination of that item with respect to other partners. Thus, for example, the determination by a court in a separate proceeding relating to a partner that a certain partnership expenditure was deductible does not bind either the Service or the other partners in a later partnership or other proceeding.

§301.6231(e)-2 Judicial decision not a bar to certain adjustments.

A court decision with respect to a partner's income tax liability attributable to nonpartnership items shall not be a bar to further proceedings with respect to that partner's income tax liability if that partner's partnership items become nonpartnership items after the appropriate time to include such nonpartnership items in the earlier court proceeding has passed. Thus, the Service could issue a later deficiency notice for the same taxable year with respect to that partner or that partner could bring a refund suit with respect to those items that have become nonpartnership items.

§301.6231(f)-1 Disallowance of losses and credits in certain cases.

(a) *Application of section.* This section applies if—

(1) A partnership, whether domestic or foreign, that is required to file a return under section 6031 for a taxable year fails to file the return within the time prescribed, and,

(2) At any time after the close of that taxable year, either—

(i) The tax matters partner of that partnership resides outside the United States, or

(ii) The books and records of that partnership are maintained outside the United States.

(b) *Computational adjustment permitted if return is not filed after mailing of notice.* Except as otherwise provided in paragraph (c) of this section, if—

(1) This section applies with respect to a partnership for a partnership taxable year,

(2) The Service mails notice to a partner that the losses and credits arising from that partnership for that year will be disallowed to that partner unless the partnership files a return for that year within 60 days after the date on which the notice is mailed, and

(3) The partnership fails to file a return for that year within that 60-day period,

The Service may, without conducting a partnership-level proceeding, mail a notice of computational adjustment to that partner to reflect the disallowance of any loss (including a capital loss) or credit arising from that partnership for that year.

(c) *Restriction on notices under paragraph (b).* Neither the notice referred to in paragraph (b)(2) of this section nor the notice of computational adjustment referred to in paragraph (b) of this section may be mailed on a day on which—

(1) The tax matters partner of the partnership resides within the United States, and

(2) The books and records of the partnership are maintained within the United States.

Thus, if this section applies with respect to a partnership for a taxable year solely because the tax matters partner of that partnership resided outside the United States for a period after the close of that taxable year and the tax matters partner later takes up residence within the United States, no notice may be mailed under paragraph (b) of this section while the tax matters partner resides within the United States.

(d) *No disallowance in certain circumstances.* If the person to whom the notice referred to in paragraph (b)(2) of this section establishes to the satisfaction of the Service—

(1) That the losses and credits arising from the partnership for the year are proper, and

(2) That the partner has made a good faith effort to have the partnership file the required return,

the Service may allow the losses and credits in whole or in part.

§301.6233-1 Extension to entities filing partnership returns, etc.

(a) ***Entities filing a partnership return.*** Except as provided in paragraph (d)(1) of this section, the provisions of subchapter C of chapter 63 of the Code ("subchapter C") and the regulations thereunder shall apply with respect to any taxable year of an entity for which such entity files a partnership return as well as to such entity's items for that taxable year and to any person holding an interest in such entity at any time during that taxable year. Any final partnership administrative adjustment or judicial determination resulting from a proceeding under subchapter C with respect to such taxable year may include a determination that the entity is not a partnership for such taxable year as well as determinations with respect to all items of the entity which would be partnership items, as defined in section 6231(a)(3) and the regulations thereunder, if such entity had been a partnership in such taxable year (including, for example, any amounts taxable to an entity determined to be an association taxable as a corporation). Thus, a final determination under subchapter C that an entity that filed a partnership return is an association taxable as a corporation will serve as a basis for a computational adjustment reflecting the disallowance of any loss or credit claimed by a purported partner with respect to that entity.

(b) *Entities filing an S corporation return.* Except as provided in paragraph (d)(2) of this section, the provisions of subchapter D of chapter 63 of the Code ("subchapter D") and the regulations thereunder shall apply with respect to any taxable year of an entity for which such entity files a return as an S corporation as well as to such entity's items for that taxable year and to any person holding an interest in such entity at any time during that taxable year. Any final S corporation administrative adjustment or judicial determination resulting from a proceeding under subchapter D with respect to such taxable year may include a determination that the entity is not an S corporation for such taxable year as well as determinations with respect to all items of the entity which would be subchapter S items, as defined in section 6245 and the regulations thereunder, if such entity had been an S corporation for such taxable year (including, for example, any amounts taxable to an entity determined to be taxable as a C corporation).

(c) *Partnership or S corporation return filed but no entity found to exist*—(1) *Partnership return filed.* Paragraph (a) of this section shall apply where a partnership return is filed for a taxable year but it is determined that there is no entity for such taxable year. For purposes of applying paragraph (a) of this section, the partnership return shall be treated as if it was filed by an entity. However, any final partnership administrative adjustment or judicial determination resulting form a proceeding under subchapter C with respect to such taxable year may also include a determination that there is no entity for such taxable year.

(2) *S corporation return filed.* Paragraph (b) of this section shall apply where an S corporation return is filed for a taxable year but it is determined that there is no entity for such taxable year. For purposes of applying paragraph (b) of this section, the S corporation return shall be treated as if it was filed by an entity. However, any final S corporation administrative adjustment or judicial determination resulting from a proceeding under subchapter D with respect to such taxable year may also include a determination that there is no entity for such taxable year.

(d) *Exceptions*—(1) *Partnership proceedings.* Paragraph (a) of this section shall not apply to:

(i) Entities for any taxable year in which such entity would be excepted from the provisions of subchapter C under section 6231(a)(1)(B) and the regulations thereunder (relating to the exception for small partnerships) if such entity were a partnership for such taxable year, and

(ii) Entities for any taxable year for which a partnership return was filed for the sole purpose of making the election described in section 761(a).

(2) *S corporation proceedings.* [RESERVED].

(e) *Effective dates.* Paragraphs (a), (c)(1), and (d)(1) of this section shall apply with respect to any taxable year beginning after September 3, 1982, and with respect to any taxable year beginning on or before and ending after September 3, 1982, if with respect to that taxable year there is an agreement entered into pursuant to section 407(a)(3) of the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462-597]. Paragraphs (b) and (c)(2) of this section shall apply with respect to any taxable year beginning after December 31, 1982.

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on April 15, 1986, 4:35 p.m., and published in the issue of the Federal Register for April 18, 1986, 51 F.R. 13231).

Employee Plans—Lists of Master and Prototype Plans

Announcement 86-70

This Announcement contains two lists of master and prototype (M&P) pension, annuity or profit-sharing plans submitted to the National Office of the Internal Revenue Service during 1984 by sponsoring organizations and mass submitters.

The first list (List A) includes those M&P plans that were timely submitted under Revenue Procedure 84-23, 1984-1 C.B. 457, by December 31, 1984, and were closed or otherwise disposed of by the Service between January 1, 1986, and March 31, 1986.

List A contains the names and addresses of the plans' sponsoring organization or mass submitter, symbols indicating the type of plan, and file folder number. It also shows the date of disposition of the plan and the type of disposition as follows: (1) favorable opinion letter (F), (2) unfavorable/nonopinion letter (U), (3) withdrawal letter (W), or (4) other (O).

Employers that adopted an approved M&P plan and, if appropriate, requested a determination letter on or before March 19, 1984, and received a favorable determination letter, retained reliance on their favorable letter under the provisions of Section 12 of Rev. Proc. 84-23. Other adopting employers will have the provisions of Section 12 of Rev. Proc. 84-23 applied to them also, provided the conditions outlined in Announcement 86-60, 1986-19 I.R.B. are met. In either case, if the approved plan is included in List A, the employer must take further action in order to have continued reliance and to meet the compliance date described in Announcement 86-60.

If List A shows that the plan adopted by the employer received a favorable opinion letter, the employer must, within 12 months after the sponsor received the favorable letter, either (1) amend its existing plan by adopting the sponsor's M&P plan as approved by the Service, or (2) adopt an M&P plan of another sponsor on List A or another quarterly list, that has received a favorable letter (See Announcement 85-130, 1985-36 I.R.B. 58).

If List A shows that the plan was closed other than by issuance of a favorable opinion letter, such employer must either (1) make all amendments required by Section 5 of Rev. Proc. 84-23, including amendments to conform with the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) Pub. L. 97-248, 1962-2 C.B. 462, the Tax Reform Act of 1984 (TRA) Pub. L. 98-369, 1984-3 (Vol. 1) C.B. 1, and the Retirement Equity Act of 1984 (REA) Pub. L. 98-397, 1984-2 C.B. 433, and submit a request for a determination letter to the appropriate key district office, or (2) adopt an M&P plan of a sponsor listed in Announcement 85-99, 1985-28 I.R.B. 4, or List B of Announcement 85-165, 1985-47 I.R.B. 4, List B of Announcement 86-43, 1986-14 I.R.B. 13, or List B of this Announcement, that has received a favorable opinion letter. In order to be afforded continued reliance and to meet the compliance date described in Announcement 86-60 the employer must adopt the amended plan by November 30, 1986.

After amending its existing plan or adopting another M&P plan, an employer must request a determination letter from the appropriate key district office in order to rely on the plan's qualification unless the employer adopts a standardized or paired plans within the meaning of Section 6.01 of Rev. Proc. 84-23.

The second list in this Announcement (List B) includes those M&P plans that were inadvertently omitted from the list published in Announcement 85-99. See Announcement 85-99 regarding when these plans must be amended.

LISTING OF MASTER OR PROTOTYPE PLANS

Abbreviations:

Type of Closing

F = Favorable
U = Unfavorable/nonopinion
W = Withdrawal
O = Other

Type of Plan

P = Paired
S = Standardized (not paired)
NS = Nonstandardized
M = Money Purchase
T = Target Benefit
D = Defined Benefit

Aetna Life Insurance Co; Hartford, CT; 50301770701-001; NS; PS; F; 03/25/86.

Aetna Life Insurance Co; Hartford, CT; 50201770701-002; P; PS; F; 03/25/86.

Aetna Life Insurance Co; Hartford, CT; 50301770701-003; NS; M; F; 03/25/86.

Aetna Life Insurance Co; Hartford, CT; 50201770701-004; P; M; F; 03/25/86.

Aetna Life Insurance Co; Hartford, CT; 50301770703-001; NS; D; F; 03/27/86.

Aetna Life Insurance Co; Hartford, CT; 50301770703-002; NS; D; F; 03/27/86.

Aetna Life Insurance Co; Hartford, CT; 50201770703-003; P; D; F; 03/27/86.

Aetna Life Insurance Co; Hartford, CT; 50201770703-004; P; D; F; 03/27/86.

American Bank & Trust Co; Baton Rouge, LA; 50302420701-001; NS; M; F; 03/26/86.

American Bank & Trust Co; Baton Rouge, LA; 50202420701-002; P; M; F; 03/26/86.

American Bank & Trust Co; Baton Rouge, LA; 50302420701-003; NS; PS; F; 03/26/86.

American Bank & Trust Co; Baton Rouge, LA; 50202420701-004; P; PS; F; 03/26/86.

American National Bank of Vincennes; Vincennes, IN; 50303500001-001; NS; PS; F; 01/16/86.

American National Bank of Vincennes; Vincennes, IN; 50303500001-002; NS; M; F; 01/16/86.

Andrew Jackson Life Insurance Co; Jackson, MS; 50304140002-001; NS; M; F; 03/28/86.

Andrew Jackson Life Insurance Co; Jackson, MS; 50304140002-002; NS; M; F; 03/28/86.

Andrew Jackson Life Insurance Co; Jackson, MS; 50204140003-001; S; M; F; 03/28/86.

Andrew Jackson Life Insurance Co; Jackson, MS; 50204140003-002; S; PS; F; 03/28/86.

Associated Milk Producers Inc; Madison, WI; 50238120001-001; S; PS; F; 01/29/86.

Associated Milk Producers Inc; Madison, WI; 50238120001-002; S; M; F; 01/29/86.

Atlantic National Bank of Florida; Jacksonville, FL; 50204660702-001; P; M; F; 03/25/86.

Atlantic National Bank of Florida; Jacksonville, FL; 50204660702-002; P; PS; F; 03/25/86.

Bancserv Inc; Orlando, FL; 50204970001-001; P; PS; F; 02/03/86.

Bancserv Inc; Orlando, FL; 50204970001-002; P; PS; F; 02/03/86.

Bancserv Inc; Orlando, FL; 50204970001-003; P; M; F; 02/03/86.

Bancserv Inc; Orlando, FL; 50204970001-004; P; M; F; 02/03/86.

Bank of Bentonville; Bentonville, AR; 50305160002-001; NS; PS; F; 01/29/86.

Bank of Bentonville; Bentonville, AR; 50305160002-002; NS; M; F; 01/29/86.

Bank of Kansas City; Kansas City, MO; 50255520001-001; S; PS; F; 01/27/86.

Bank of Kansas City; Kansas City, MO; 50355520001-002; NS; PS; F; 01/27/86.

Bank of Kansas City; Kansas City, MO; 50255520002-001; S; M; F; 01/27/86.

Bank of Kansas City; Kansas City, MO; 50355520002-002; NS; M; F; 01/27/86.

Bank of New York; New York, NY; 50206420001-001; S; M; F; 03/28/86.

Bank of New York; New York, NY; 50206420001-002; S; PS; F; 03/28/86.

Bank of New York; New York, NY; 50206420002-001; S; D; F; 03/28/86.

Bank of Pontiac; Pontiac, IL; 50206630001-001; P; PS; F; 01/27/86.

Bank of Pontiac; Pontiac, IL; 50206630001-002; P; M; F; 01/27/86.

Bank of Toccoa; Toccoa, GA; 50306880701-001; NS; PS; F; 03/25/86.

Bankers Trust Co; New York, NY; 50233110001-002; P; M; F; 02/03/86.

Bar Harbor Banking & Trust Co; Bar Harbor, ME; 50326910001-001; NS; M; F; 01/16/86.

Bar Harbor Banking & Trust Co; Bar Harbor, ME; 50326910001-002; NS; PS; F; 01/16/86.

Barnett Banks Trust Co NA; Jacksonville, FL; 50307700701-001; NS; M; F; 03/26/86.

Barnett Banks Trust Co NA; Jacksonville, FL; 50207700701-002; P; M; F; 03/26/86.

Barnett Banks Trust Co NA; Jacksonville, FL; 50307700701-003; NS; PS; F; 03/26/86.

Barnett Banks Trust Co NA; Jacksonville, FL; 50207700701-004; P; PS; F; 03/26/86.

Batesville Security Bank; Batesville, MS; 50307770001-001; NS; PS; F; 03/28/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50308270001-001; NS; M; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50308270001-002; NS; PS; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50308270001-003; NS; T; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50308270002-001; NS; D; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50308270002-002; NS; D; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50208270003-001; P; M; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50208270003-002; P; PS; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50208270003-003; P; T; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50208270004-001; S; D; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50208270004-002; S; D; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50308270005-001; NS; D; F; 02/06/86.

Berkshire Life Insurance Co; Pittsfield, MA; 50308270005-002; NS; D; F; 02/06/86.

Bloomington National Bank; Bloomington, IN; 50208400001-001; P; M; F; 02/05/86.

Bloomington National Bank; Bloomington, IN; 50208400001-002; P; M; F; 02/05/86.

Bloomington National Bank; Bloomington, IN; 50208400001-003; P; PS; F; 02/05/86.

Bloomington National Bank; Bloomington, IN; 50208400001-004; P; PS; F; 02/05/86.

Busey First National Bank; Urbana, IL; 50309140701-001; NS; M; F; 03/26/86.

Busey First National Bank; Urbana, IL; 50309140701-002; NS; PS; F; 03/26/86.

Canada Life Assurance Co; Atlanta, GA; 50309550701-001; NS; M; F; 03/27/86.

Canada Life Assurance Co; Atlanta, GA; 50209550701-002; P; M; F; 03/27/86.

Canada Life Assurance Co; Atlanta, GA; 50309550701-003; NS; PS; F; 03/27/86.

Canada Life Assurance Co; Atlanta, GA; 50209550701-004; P; PS; F; 03/27/86.

Canada Life Assurance Co; Atlanta, GA; 50309550702-001; NS; D; F; 03/27/86.

Canada Life Assurance Co; Atlanta, GA; 50309550702-002; NS; D; F; 03/27/86.

Canada Life Assurance Co; Atlanta, GA; 50209550702-003; P; D; F; 03/27/86.

Canada Life Assurance Co; Atlanta, GA; 50209550702-004; P; D; F; 03/27/86.

Canada Life Assurance Co; Atlanta, GA; 50309550703-001; NS; T; F; 03/25/86.

Canada Life Assurance Co; Atlanta, GA; 50209550703-002; S; T; F; 03/25/86.

Central Fidelity Bank; Richmond, VA; 50310900001-001; NS; M; F; 02/03/86.

Central Fidelity Bank; Richmond, VA; 50210900001-002; P; M; F; 02/03/86.

Central Fidelity Bank; Richmond, VA; 50310900001-003; NS; PS; F; 02/03/86.

Central Fidelity Bank; Richmond, VA; 50210900001-004; P; PS; F; 02/03/86.

Central Fidelity Bank; Richmond, VA; 50310900001-005; NS; T; F; 02/03/86.

Central Fidelity Bank; Richmond, VA; 50210900001-006; P; T; F; 02/03/86.

Central Jersey Bank & Trust Co; East Brunswick, NJ; 50210800003-001; S; T; F; 02/05/86.

Central Jersey Bank & Trust Co; East Brunswick, NJ; 50310800003-002; NS; T; F; 02/05/86.

Central Life Assurance Co; Des Moines, IA; 50310810001-001; NS; M; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810001-002; NS; M; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810001-003; NS; PS; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810001-004; NS; PS; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810001-005; NS; T; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810001-006; NS; T; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810001-007; S; M; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810001-008; S; M; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810001-009; S; PS; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810001-010; S; PS; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810001-011; S; T; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810001-012; S; T; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810001-013; S; M; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810001-014; S; PS; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810002-001; NS; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810002-002; NS; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810002-003; NS; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810002-004; NS; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50310810002-005; NS; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810002-006; S; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810002-007; S; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810002-008; S; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810002-009; S; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810002-010; S; D; U; 02/24/86.

Central Life Assurance Co; Des Moines, IA; 50210810002-011; S; D; U; 02/24/86.

Central Trust Co; Rochester, NY; 50311100001-001; NS; PS; F; 03/26/86.

Central Trust Co; Rochester, NY; 50311100001-002; NS; PS; F; 03/24/86.

Central Trust Co; Rochester, NY; 50311100001-003; NS; M; F; 03/24/86.

Central Trust Co; Rochester, NY; 50311100001-004; NS; M; F; 03/26/86.

Central Trust Co; Rochester, NY; 50211100001-005; S; PS; F; 03/24/86.

Central Trust Co; Rochester, NY; 50211100001-006; S; PS; F; 03/24/86.

Central Trust Co; Rochester, NY; 50211100001-007; S; M; F; 03/26/86.

Central Trust Co; Rochester, NY; 50211100001-008; S; M; F; 03/26/86.

Century Life of America; Waverly, IA; 50337960703-001; NS; T; F; 03/25/86.

Century Life of America; Waverly, IA; 50237960703-002; S; T; F; 03/25/86.

Champions Life Insurance Co; Richardson, TX; 50311320001-001; NS; D; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50211320001-002; S; D; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50311320001-003; NS; D; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50211320001-004; S; D; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50311320002-001; NS; M; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50211320002-002; S; M; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50311320002-003; NS; M; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50211320002-004; S; M; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50311320002-005; NS; PS; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50211320002-006; S; PS; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50311320002-007; NS; PS; F; 02/03/86.

Champions Life Insurance Co; Richardson, TX; 50211320002-008; S; PS; F; 02/03/86.

Citizens Bank; Columbia, MS; 50372240001-001; NS; PS; F; 02/05/86.

Citizens Bank; Columbia, MS; 50272240001-002; S; PS; F; 02/05/86.

Citizens Bank; Columbia, MS; 50372240001-003; NS; M; F; 03/05/86.
Citizens Bank; Columbia, MS; 50272240001-004; S; M; F; 03/05/86.
Citizens Bank & Trust Co; Glastonbury, CT; 50312190701-001; NS; M; F; 03/26/86.
Citizens Bank & Trust Co; Glastonbury, CT; 50212190701-002; P; M; F; 03/26/86.
Citizens Bank & Trust Co; Glastonbury, CT; 50312190701-003; NS; PS; F; 03/26/86.
Citizens Bank & Trust Co; Glastonbury, CT; 50212190701-004; P; PS; F; 03/26/86.
Citizens Bank & Trust Co of Paducah; Paducah, KY; 50212250001-001; P; PS; F; 02/03/86.
Citizens Bank & Trust Co of Paducah; Paducah, KY; 50212250001-002; P; M; F; 02/03/86.
Citizens State Bank of Corpus Christi; Corpus Christi, TX; 50313260702-001; NS; D; F; 03/27/86.
Citizens State Bank of Corpus Christi; Corpus Christi, TX; 50313260702-002; NS; D; F; 03/27/86.
Citizens State Bank of Corpus Christi; Corpus Christi, TX; 50213260702-003; P; D; F; 03/27/86.
Citizens State Bank of Corpus Christi; Corpus Christi, TX; 50213260702-004; P; D; F; 03/27/86.
Companion Life Insurance Co; New York, NY; 50315540701-001; NS; M; F; 03/25/86.
Companion Life Insurance Co; New York, NY; 50215540701-002; P; M; F; 03/25/86.
Companion Life Insurance Co; New York, NY; 50315540701-003; NS; PS; F; 03/25/86.
Companion Life Insurance Co; New York, NY; 50215540701-004; P; PS; F; 03/25/86.
Companion Life Insurance Co; New York, NY; 50315540703-001; NS; T; F; 03/25/86.
Companion Life Insurance Co; New York, NY; 50215540703-002; S; T; F; 03/25/86.
Connecticut National Bank; Hartford, CT; 50352000003-001; NS; D; F; 02/20/86.
Connecticut National Bank; Hartford, CT; 50252000003-002; S; D; F; 02/20/86.
Connecticut National Bank; Hartford, CT; 50352000003-003; NS; D; F; 02/20/86.
Connecticut National Bank; Hartford, CT; 50252000003-004; S; D; F; 02/20/86.
Connecticut National Bank; Hartford, CT; 50352000003-005; NS; D; F; 12/13/85.
Connecticut National Bank; Hartford, CT; 50252000003-006; S; D; F; 02/20/86.
Connecticut National Bank; Hartford, CT; 50352000003-007; NS; D; F; 02/20/86.
Connecticut National Bank; Hartford, CT; 50252000003-008; S; D; F; 02/20/86.
Connecticut National Bank; Hartford, CT; 50352000004-001; NS; PS; F; 01/16/86.
Delta Life & Annuity Co; Memphis, TN; 50316750001-001; NS; PS; F; 02/20/86.
Delta Life & Annuity Co; Memphis, TN; 50316750001-002; NS; PS; F; 02/20/86.
Delta Life & Annuity Co; Memphis, TN; 50216750001-003; P; PS; F; 02/20/86.
Delta Life & Annuity Co; Memphis, TN; 50216750001-004; P; PS; F; 02/20/86.
Delta Life & Annuity Co; Memphis, TN; 50316750001-005; NS; M; F; 02/20/86.
Delta Life & Annuity Co; Memphis, TN; 50316750001-006; NS; M; F; 02/20/86.
Delta Life & Annuity Co; Memphis, TN; 50216750001-007; P; M; F; 02/20/86.
Delta Life & Annuity Co; Memphis, TN; 50216750001-008; P; M; F; 02/20/86.
Delta Life & Annuity Co; Memphis, TN; 50316750002-001; NS; PS; F; 02/05/86.
Delta Life & Annuity Co; Memphis, TN; 50316750002-002; NS; PS; F; 02/05/86.
Delta Life & Annuity Co; Memphis, TN; 50216750002-003; P; PS; F; 02/05/86.
Delta Life & Annuity Co; Memphis, TN; 50216750002-004; P; PS; F; 02/05/86.
Delta Life & Annuity Co; Memphis, TN; 50316750002-005; NS; M; F; 02/05/86.
Delta Life & Annuity Co; Memphis, TN; 50316750002-006; NS; M; F; 02/05/86.
Delta Life & Annuity Co; Memphis, TN; 50216750002-007; P; M; F; 02/05/86.
Delta Life & Annuity Co; Memphis, TN; 50216750002-008; P; M; F; 02/05/86.
Dreyfuss Trust Co New York; Garden City, NY; 50317130001-001; NS; M; F; 02/14/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130001-002; P; M; F; 02/14/86.
Dreyfuss Trust Co New York; Garden City, NY; 50317130001-003; NS; PS; F; 02/14/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130001-004; P; PS; F; 02/14/86.
Dreyfuss Trust Co New York; Garden City, NY; 50317130001-005; NS; T; F; 02/14/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130001-006; P; T; F; 02/14/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130001-007; P; M; F; 02/14/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130001-008; P; PS; F; 02/14/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130001-009; P; T; F; 02/14/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130002-001; P; D; F; 03/28/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130002-002; P; D; F; 03/31/86.
Dreyfuss Trust Co New York; Garden City, NY; 50317130002-003; NS; D; F; 03/31/86.
Dreyfuss Trust Co New York; Garden City, NY; 50317130002-004; NS; D; F; 03/31/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130002-005; P; D; F; 03/31/86.
Dreyfuss Trust Co New York; Garden City, NY; 50317130002-006; NS; D; F; 03/31/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130002-007; P; D; F; 03/31/86.
Dreyfuss Trust Co New York; Garden City, NY; 50217130002-008; P; D; F; 03/31/86.
Equitable Life Assurance Society of the United States; New York, NY; 50217870001-001; S; PS; F; 01/27/86.
Equitable Life Assurance Society of the United States; New York, NY; 50217870001-002; S; M; F; 01/27/86.
Equitable Life Assurance Society of the United States; New York, NY; 50317870001-003; NS; PS; F; 01/27/86.
Equitable Life Assurance Society of the United States; New York, NY; 50317870001-004; NS; M; F; 01/27/86.
Equitable Life Assurance Society of the United States; New York, NY; 50217870004-002; S; PS; U; 02/17/86.
Equitable Life of Iowa; Des Moines, IA; 50317880701-001; NS; M; F; 03/26/86.
Equitable Life of Iowa; Des Moines, IA; 50217880701-002; P; M; F; 03/26/86.
Equitable Life of Iowa; Des Moines, IA; 50317880701-003; NS; PS; F; 03/26/86.
Equitable Life of Iowa; Des Moines, IA; 50217880701-004; P; PS; F; 03/26/86.
Equitable Life of Iowa; Des Moines, IA; 50317880702-001; NS; D; F; 03/24/86.
Equitable Life of Iowa; Des Moines, IA; 50317880702-002; NS; D; F; 03/25/86.
Equitable Life of Iowa; Des Moines, IA; 50217880702-003; P; D; F; 03/25/86.
Equitable Life of Iowa; Des Moines, IA; 50217880702-004; P; D; F; 03/25/86.
Evergreen Funds; Harrison, NY; 50218000701-001; P; M; F; 03/25/86.
Evergreen Funds; Harrison, NY; 50218000701-002; P; PS; F; 03/25/86.
Farmers & Merchants State Bank of Bushnell; Bushnell, IL; 50218670001-001; P; M; F; 01/15/86.
Farmers & Merchants State Bank of Bushnell; Bushnell, IL; 50318670001-002; NS; M; F; 01/15/86.
Farmers & Merchants State Bank of Bushnell; Bushnell, IL; 50218670001-003; P; PS; F; 01/15/86.
Farmers & Merchants State Bank of Bushnell; Bushnell, IL; 50318670001-004; NS; PS; F; 01/16/86.
Federal Kemper Life Assurance Co; Long Grove, IL; 50219610001-001; S; PS; F; 02/24/86.
Federal Kemper Life Assurance Co; Long Grove, IL; 50219610001-002; S; M; F; 02/24/86.
Federated Life Insurance Co; Owatonna, MN; 50319690701-001; NS; M; F; 03/26/86.
Federated Life Insurance Co; Owatonna, MN; 50219690701-002; P; M; F; 03/26/86.
Federated Life Insurance Co; Owatonna, MN; 50319690701-003; NS; PS; F; 03/26/86.
Federated Life Insurance Co; Owatonna, MN; 50219690701-004; P; PS; F; 03/26/86.
Federated Life Insurance Co; Owatonna, MN; 50319690702-001; NS; D; F; 03/25/86.
Federated Life Insurance Co; Owatonna, MN; 50319690702-002; NS; D; F; 03/25/86.
Federated Life Insurance Co; Owatonna, MN; 50219690702-003; P; D; F; 03/25/86.
Federated Life Insurance Co; Owatonna, MN; 50219690702-004; P; D; F; 03/25/86.
Fidelity Management & Research Co; Boston, MA; 50218740001-001; P; PS; F; 02/03/86.
Fidelity Management & Research Co; Boston, MA; 50218740001-002; P; M; F; 02/03/86.
Fidelity Management & Research Co; Boston, MA; 50218740001-003; P; PS; F; 02/03/86.
Fidelity Management & Research Co; Boston, MA; 50218740001-004; P; M; F; 02/03/86.
Fidelity Management & Research Co; Boston, MA; 50218740001-005; P; PS; F; 02/03/86.
Fidelity Management & Research Co; Boston, MA; 50218740001-006; P; M; F; 02/03/86.
Fidelity Mutual Life Insurance Co; Radnor, PA; 50319920002-001; NS; M; F; 03/31/86.
Fidelity Mutual Life Insurance Co; Radnor, PA; 50319920003-001; NS; PS; F; 03/31/86.
First Interstate Trust Co of Wisconsin; Sheboygan, WI; 50255101901-001; P; PS; F; 02/05/86.
First Interstate Trust Co of Wisconsin; Sheboygan, WI; 50255101901-002; P; M; F; 02/05/86.
First Interstate Trust Co of Wisconsin; Sheboygan, WI; 50355101901-003; NS; PS; F; 02/05/86.
First Interstate Trust Co of Wisconsin; Sheboygan, WI; 50355101901-004; NS; M; F; 02/05/86.
First Mississippi National Bank; Hattiesburg, MS; 50322190002-001; NS; D; F; 03/31/86.
First Mississippi National Bank; Hattiesburg, MS; 50322190002-002; NS; D; F; 03/31/86.
First National Bank Elhart; Elkhart, IN; 50326970001-001; NS; PS; F; 12/02/85.
First National Bank Elhart; Elkhart, IN; 50326970001-002; NS; PS; F; 12/02/85.
First National Bank Elhart; Elkhart, IN; 50326970002-001; NS; M; F; 01/27/86.
First National Bank Elhart; Elkhart, IN; 50326970002-002; NS; M; F; 01/27/86.
First National Bank Elhart; Elkhart, IN; 50326970002-003; NS; PS; F; 12/02/85.
First National Bank in Little Rock; Little Rock, AR; 50327570002-001; NS; PS; F; 01/29/86.
First National Bank in Little Rock; Little Rock, AR; 50327570002-002; NS; M; F; 01/29/86.
First National Bank of Amarillo; Amarillo, TX; 50324070001-001; NS; PS; F; 03/20/86.
First National Bank of Amarillo; Amarillo, TX; 50324070001-002; NS; M; F; 03/20/86.
First National Bank of Amarillo; Amarillo, TX; 50224070002-001; P; M; F; 03/20/86.
First National Bank of Amarillo; Amarillo, TX; 50224070002-002; P; PS; F; 03/20/86.
First National Bank of Arcola; Arcola, IL; 50224140701-001; P; M; F; 03/25/86.
First National Bank of Arcola; Arcola, IL; 50224140701-002; P; PS; F; 03/25/86.
First National Bank Of Batesville; Batesville, AR; 50322960002-001; NS; PS; F; 01/29/86.
First National Bank Of Batesville; Batesville, AR; 50322960002-002; NS; M; F; 01/29/86.
First National Bank Of Berryville; Berryville, AR; 50322930002-001; NS; PS; F; 01/29/86.
First National Bank Of Berryville; Berryville, AR; 50322930002-002; NS; M; F; 01/29/86.
First National Bank of Russellville; Russellville, AR; 50305050002-001; NS; PS; F; 01/29/86.
First National Bank of Russellville; Russellville, AR; 50305050002-002; NS; M; F; 01/29/86.
First State Bank of Decatur; Decatur, IN; 50271950001-001; S; M; F; 02/03/86.
First State Bank of Monticello; Monticello, IL; 50328750001-001; NS; M; F; 02/03/86.
First Vermont Bank & Trust Co; Brattleboro, VT; 50229250003-001; S; T; F; 02/05/86.
First Vermont Bank & Trust Co; Brattleboro, VT; 50329250003-002; NS; T; F; 02/05/86.
First Western Bank; Minot, ND; 50229290001-001; S; PS; F; 02/03/86.
First Western Bank; Minot, ND; 50329290001-002; NS; PS; F; 02/03/86.
First Western Bank; Minot, ND; 50229290001-003; S; PS; F; 02/03/86.

First Western Bank; Minot, ND; 50329290001-004; NS; PS; F; 02/03/86.
First Wisconsin National Bank of Eau Claire; Eau Claire, WI; 50229470001-001; S; PS; F; 02/05/86.
First Wisconsin National Bank of Eau Claire; Eau Claire, WI; 50229470001-002; S; M; F; 02/05/86.
First Wisconsin National Bank of Eau Claire; Eau Claire, WI; 50229470001-003; S; PS; F; 02/05/86.
First Wisconsin National Bank of Eau Claire; Eau Claire, WI; 50229470001-004; S; M; F; 02/05/86.
First Wisconsin National Bank of Eau Claire; Eau Claire, WI; 50329470001-005; NS; PS; F; 02/05/86.
First Wisconsin National Bank of Eau Claire; Eau Claire, WI; 50329470001-006; NS; M; F; 02/05/86.
First Wisconsin National Bank of Eau Claire; Eau Claire, WI; 50329470001-007; NS; PS; F; 02/05/86.
First Wisconsin National Bank of Eau Claire; Eau Claire, WI; 50329470001-008; NS; M; F; 02/05/86.
First Wisconsin National Bank of Madison; Madison, WI; 50229480001-001; S; PS; F; 12/02/85.
First Wisconsin National Bank of Madison; Madison, WI; 50229480001-002; S; M; F; 12/02/85.
First Wisconsin National Bank of Madison; Madison, WI; 50229480001-003; S; PS; F; 12/02/85.
First Wisconsin National Bank of Madison; Madison, WI; 50229480001-004; S; M; F; 01/27/86.
First Wisconsin National Bank of Madison; Madison, WI; 50329480001-005; NS; PS; F; 01/27/86.
First Wisconsin National Bank of Madison; Madison, WI; 50329480001-006; NS; M; F; 12/02/85.
First Wisconsin National Bank of Madison; Madison, WI; 50329480001-007; NS; PS; F; 01/27/86.
First Wisconsin National Bank of Madison; Madison, WI; 50329480001-008; NS; M; F; 01/27/86.
Florida National Bank; Jacksonville, FL; 50329880701-001; NS; M; F; 03/26/86.
Florida National Bank; Jacksonville, FL; 50229880701-002; P; M; F; 03/26/86.
Florida National Bank; Jacksonville, FL; 50329880701-003; NS; PS; F; 03/26/86.
Florida National Bank; Jacksonville, FL; 50229880701-004; P; PS; F; 03/26/86.
Franklin Life Insurance Co; Springfield, IL; 50330310704-001; NS; D; F; 03/27/86.
Franklin Life Insurance Co; Springfield, IL; 50330310704-002; NS; D; F; 03/27/86.
Franklin Life Insurance Co; Springfield, IL; 50230310704-003; P; D; F; 03/27/86.
Franklin Life Insurance Co; Springfield, IL; 50230310704-004; P; D; F; 03/27/86.
General Life insurance Corp of Wisconsin; Milwaukee, WI; 50330860701-001; NS; M; F; 03/26/86.
General Life Insurance Corp of Wisconsin; Milwaukee, WI; 50230860701-002; P; M; F; 03/26/86.
General Life Insurance Corp of Wisconsin; Milwaukee, WI; 50330860701-003; NS; PS; F; 03/26/86.
General Life Insurance Corp of Wisconsin; Milwaukee, WI; 50230860701-004; P; PS; F; 03/26/86.
General Life Insurance Corp of Wisconsin; Milwaukee, WI; 50330860702-001; NS; D; F; 03/25/86.
General Life Insurance Corp of Wisconsin; Milwaukee, WI; 50330860702-002; NS; D; F; 03/25/86.
General Life Insurance Corp of Wisconsin; Milwaukee, WI; 50230860702-003; P; D; F; 03/25/86.
General Life Insurance Corp of Wisconsin; Milwaukee, WI; 50230860702-004; P; D; F; 03/25/86.
Great Country Bank; Ansonia, CT; 50271910001-001; P; PS; F; 03/31/86.
Great Country Bank; Ansonia, CT; 50271910001-002; P; M; F; 03/31/86.
Great Country Bank; Ansonia, CT; 50371910001-003; NS; PS; F; 03/31/86.
Great Country Bank; Ansonia, CT; 50371910001-004; NS; M; F; 03/31/86.
Great Southern National Bank; Jackson, MS; 50370360001-001; NS; PS; F; 03/31/86.
Harris Trust & Savings Bank; Chicago, IL; 50232600001-001; P; PS; F; 02/03/86.
Harris Trust & Savings Bank; Chicago, IL; 50232600001-002; P; M; F; 02/03/86.
High Yield Securities Inc; Houston, TX; 50233340701-001; P; M; F; 03/25/86.
High Yield Securities Inc; Houston, TX; 50233340701-002; P; PS; F; 03/25/86.
Hutton Investment Series; New York, NY; 50217275002-001; S; PS; U; 01/09/86.
Hutton Investment Series; New York, NY; 50217275002-002; S; M; U; 01/09/86.
Illinois National Bank & Trust Co of Rockford; Rockford, IL; 50334170001-001; NS; PS; U; 02/17/86.
Illinois National Bank & Trust Co of Rockford; Rockford, IL; 50334170001-002; NS; M; U; 02/17/86.
Indiana National Bank; Indianapolis, IN; 50334540001-001; NS; PS; F; 02/20/86.
Indiana National Bank; Indianapolis, IN; 50334540001-002; P; PS; F; 02/20/86.
Indiana National Bank; Indianapolis, IN; 50334540001-003; NS; M; F; 02/20/86.
Indiana National Bank; Indianapolis, IN; 50234540001-004; P; M; F; 02/20/86.
Industrial Valley Bank & Trust Co; Philadelphia, PA; 50334630001-001; NS; M; F; 02/10/86.
Industrial Valley Bank & Trust Co; Philadelphia, PA; 50334630001-002; NS; M; F; 02/10/86.
Industrial Valley Bank & Trust Co; Philadelphia, PA; 50334630002-001; NS; PS; F; 02/10/86.
Industrial Valley Bank & Trust Co; Philadelphia, PA; 50334630002-002; NS; PS; F; 02/10/86.
Integon Life Insurance Corp; Winston-Salem, NC; 50334670701-001; NS; M; F; 03/27/86.
Integon Life Insurance Corp; Winston-Salem, NC; 50234670701-002; P; M; F; 03/27/86.
Integon Life Insurance Corp; Winston-Salem, NC; 50334670701-003; NS; PS; F; 03/27/86.
Integon Life Insurance Corp; Winston-Salem, NC; 50234670701-004; P; PS; F; 03/27/86.
Investors Insurance Corp; Tigard, OR; 50235170001-001; P; M; F; 02/03/86.
Investors Insurance Corp; Tigard, OR; 50235170001-002; P; PS; F; 02/03/86.
Janney Montgomery Scott Inc; Philadelphia, PA; 50323780001-001; NS; PS; F; 01/29/86.
Janney Montgomery Scott Inc; Philadelphia, PA; 50323780001-002; NS; M; F; 01/29/86.
Jones Mathers Casamento & Co Inc; Metairie, LA; 50373050702-001; NS; D; F; 03/27/86.
Jones Mathers Casamento & Co Inc; Metairie, LA; 50373050702-002; NS; D; F; 03/27/86.
Jones Mathers Casamento & Co Inc; Metairie, LA; 50273050702-003; P; D; F; 03/27/86.
Jones Mathers Casamento & Co Inc; Metairie, LA; 50273050702-004; P; D; F; 03/27/86.
Kansas City Life Insurance Co; Kansas City, MO; 50335850701-001; NS; M; F; 03/26/86.
Kansas City Life Insurance Co; Kansas City, MO; 50235850701-002; P; M; F; 03/26/86.
Kansas City Life Insurance Co; Kansas City, MO; 50335850701-003; NS; PS; F; 03/26/86.
Kansas City Life Insurance Co; Kansas City, MO; 50235850701-004; P; PS; F; 03/26/86.
Kansas City Life Insurance Co; Kansas City, MO; 50335850702-001; NS; D; F; 03/25/86.
Kansas City Life Insurance Co; Kansas City, MO; 50335850702-002; NS; D; F; 03/25/86.
Kansas City Life Insurance Co; Kansas City, MO; 50235850702-003; P; D; F; 03/25/86.
Kansas City Life Insurance Co; Kansas City, MO; 50235850702-004; P; D; F; 03/25/86.
Kansas City Life Insurance Co; Kansas City, MO; 50335850703-001; NS; T; F; 03/25/86.
Kansas City Life Insurance Co; Kansas City, MO; 50235850703-002; S; T; F; 03/25/86.
Kellogg-Citizens National Bank; Green Bay, WI; 50235930003-001; S; T; F; 02/03/86.
Kellogg-Citizens National Bank; Green Bay, WI; 50335930003-002; NS; T; F; 02/03/86.
Lafayette Life Insurance Co; Lafayette, IN; 50336450001-001; NS; M; U; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50236450001-002; S; M; U; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50336450001-003; NS; PS; U; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50236450001-004; S; PS; U; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50336450002-001; NS; D; U; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50236450002-002; S; D; U; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50336450002-003; NS; D; U; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50236450002-004; S; D; U; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50336450703-001; NS; M; F; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50236450703-002; S; M; F; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50336450703-003; NS; PS; F; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50236450703-004; P; PS; F; 03/26/86.
Lafayette Life Insurance Co; Lafayette, IN; 50336450704-001; NS; D; F; 03/25/86.
Lafayette Life Insurance Co; Lafayette, IN; 50336450704-002; NS; D; F; 03/25/86.
Lafayette Life Insurance Co; Lafayette, IN; 50236450704-003; S; D; F; 03/25/86.
Lafayette Life Insurance Co; Lafayette, IN; 50236450704-004; S; D; F; 03/25/86.
Life Insurance Co of Virginia; Richmond, VA; 50333830701-001; NS; M; F; 03/26/86.
Life Insurance Co of Virginia; Richmond, VA; 50233830701-002; P; M; F; 03/26/86.
Life Insurance Co of Virginia; Richmond, VA; 50333830701-003; NS; PS; F; 03/26/86.
Life Insurance Co of Virginia; Richmond, VA; 50233830701-004; P; PS; F; 03/26/86.
Life Insurance Co of Virginia; Richmond, VA; 50333830702-001; NS; D; F; 03/25/86.
Life Insurance Co of Virginia; Richmond, VA; 50333830702-002; NS; D; F; 03/25/86.
Life Insurance Co of Virginia; Richmond, VA; 50233830702-003; P; D; F; 03/25/86.
Life Insurance Co of Virginia; Richmond, VA; 50233830702-004; P; D; F; 03/25/86.
M&I First National Bank; West Bend, WI; 50326702201-001; NS; PS; F; 03/31/86.
M&I First National Bank; West Bend, WI; 50326702201-002; NS; M; F; 03/31/86.
M&I Marshall & Ilsley Bank; Milwaukee, WI; 50338002201-001; NS; PS; F; 03/31/86.
M&I Marshall & Ilsley Bank; Milwaukee, WI; 50338002201-002; NS; M; F; 03/31/86.
Manufacturers Life Insurance Co; Toronto Canada, ; 50338420002-001; NS; D; F; 02/03/86.
Manufacturers Life Insurance Co; Toronto Canada, ; 50338420002-002; NS; D; F; 02/03/86.
Manufacturers Life Insurance Co; Toronto Canada, ; 50238420002-003; S; D; F; 02/03/86.
Manufacturers Life Insurance Co; Toronto Canada, ; 50238420002-004; S; D; F; 02/03/86.
Marine Midland Bank NA; New York, NY; 50238560002-001; S; PS; F; 01/30/86.
Marine Midland Bank NA; New York, NY; 50238560002-002; S; M; F; 01/30/86.
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50238830003-001; S; D; F; 02/17/86.
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50238830003-002; S; D; F; 02/17/86.
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830003-003; NS; D; F; 02/17/86.
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830003-004; NS; D; F; 02/17/86.
Merchants National Bank & Trust Co of Syracuse; Syracuse, NY; 50339680001-001; NS; PS; F; 02/13/86.
Merchants National Bank & Trust Co of Syracuse; Syracuse, NY; 50339680001-002; NS; PS; F; 02/13/86.
Merchants National Bank & Trust Co of Syracuse; Syracuse, NY; 50339680001-003; NS; M; F; 02/13/86.
Merchants National Bank & Trust Co of Syracuse; Syracuse, NY; 50339680001-004; NS; M; F; 02/13/86.
Merchants National Bank & Trust Co of Syracuse; Syracuse, NY; 50239680001-005; S; PS; F; 02/13/86.
Merchants National Bank & Trust Co of Syracuse; Syracuse, NY; 50239680001-006; S; PS; F; 02/13/86.
Merchants National Bank & Trust Co of Syracuse; Syracuse, NY; 50239680001-007; S; M; F; 02/13/86.
Merchants National Bank & Trust Co of Syracuse; Syracuse, NY; 50239680001-008; S; M; F; 02/13/86.
Michigan Milk Producers Association; Southfield, MI; 50240130001-001; P; M; F; 03/31/86.
Michigan Milk Producers Association; Southfield, MI; 50240130001-002; P; PS; F; 03/31/86.
Michigan National Bank; Grand Rapids, MI; 50340140001-001; NS; PS; F; 02/10/86.
Michigan National Bank; Grand Rapids, MI; 50240140001-002; S; PS; F; 02/10/86.
Michigan National Bank; Grand Rapids, MI; 50340140001-003; NS; M; F; 02/10/86.
Michigan National Bank; Grand Rapids, MI; 50240140001-004; S; M; F; 02/10/86.

Midland Mutual Life Insurance Co; Columbus, OH; 50340510701-001; NS; M; F; 03/25/86.
Midland Mutual Life Insurance Co; Columbus, OH; 50240510701-002; P; M; F; 03/25/86.
Midland Mutual Life Insurance Co; Columbus, OH; 50340510701-003; NS; M; F; 03/25/86.
Midland Mutual Life Insurance Co; Columbus, OH; 50240510701-004; P; PS; F; 03/25/86.
Midland Mutual Life Insurance Co; Columbus, OH; 50340510702-001; NS; D; F; 03/25/86.
Midland Mutual Life Insurance Co; Columbus, OH; 50340510702-002; NS; D; F; 03/25/86.
Millikin National Bank of Decatur; Decatur, IL; 50240750003-001; S; T; F; 02/03/86.
Millikin National Bank of Decatur; Decatur, IL; 50340750003-002; NS; T; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50340900001-001; NS; D; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50340900001-002; NS; D; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50240900001-003; S; D; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50240900001-004; S; D; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50340900001-005; NS; D; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50240900001-006; S; D; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50340900002-001; NS; M; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50240900002-002; S; M; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50340900002-003; NS; M; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50240900002-004; S; M; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50340900002-005; NS; PS; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50240900002-006; S; PS; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50340900002-007; NS; PS; F; 02/03/86.
Modern American Life Insurance Co; Englewood, CO; 50240900002-008; S; PS; F; 02/03/86.
Monroe County Bank; Bloomington, IN; 50241010001-001; P; PS; F; 02/05/86.
Monroe County Bank; Bloomington, IN; 50241010001-002; P; M; F; 02/05/86.
Monroe County Bank; Bloomington, IN; 50241010001-003; P; PS; F; 02/05/86.
Monroe County Bank; Bloomington, IN; 50241010001-004; P; PS; F; 02/05/86.
Mutual Qualified Income Fund Inc; New York, NY; 50241450001-001; S; PS; F; 03/20/86.
Mutual Shares Corp; New York, NY; 50241510001-001; S; PS; F; 03/20/86.
National Bank of Commerce; Memphis, TN; 50341880701-001; NS; M; F; 03/25/86.
National Bank of Commerce; Memphis, TN; 50241880701-002; P; M; F; 03/25/86.
National Bank of Commerce; Memphis, TN; 50341880701-003; NS; PS; F; 03/25/86.
National Bank of Commerce; Memphis, TN; 50241880701-004; P; PS; F; 03/25/86.
National Bank of Commerce of Pine Bluff; Pine Bluff, AR; 50341920001-001; NS; PS; F; 01/16/86.
National Bank of Commerce of Pine Bluff; Pine Bluff, AR; 50341920001-002; NS; PS; F; 01/16/86.
National Bank of Commerce of Pine Bluff; Pine Bluff, AR; 50241920001-003; S; PS; F; 01/16/86.
National Bank of Commerce of Pine Bluff; Pine Bluff, AR; 50241920001-004; S; PS; F; 01/16/86.
National Bank of Commerce of Pine Bluff; Pine Bluff, AR; 50341920002-001; NS; M; F; 01/16/86.
National Bank of Commerce of Pine Bluff; Pine Bluff, AR; 50341920002-002; NS; M; F; 01/16/86.
National Bank of Commerce of Pine Bluff; Pine Bluff, AR; 50241920002-003; S; M; F; 01/16/86.
National Bank of Commerce of Pine Bluff; Pine Bluff, AR; 50241920002-004; S; M; F; 01/16/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50241930001-001; S; PS; F; 01/27/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50241930001-002; S; M; F; 01/27/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50341930001-003; NS; PS; F; 01/27/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50341930001-004; NS; M; F; 01/27/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50341930001-005; NS; PS; F; 01/27/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50241930001-006; S; PS; F; 01/27/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50241930001-007; S; M; F; 01/27/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50341930001-008; NS; PS; F; 01/29/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50341930001-009; NS; M; F; 01/27/86.
National Bank of Commerce Trust & Savings Association; Lincoln, NE; 50341930001-010; NS; PS; F; 01/27/86.
National Bank of Washington; Washington, DC; 50242249301-001; P; M; F; 02/03/86.
National Bank of Washington; Washington, DC; 50242249301-002; P; PS; F; 02/03/86.
National Bank of Washington; Washington, DC; 50242249301-003; P; T; F; 02/03/86.
National Bank of Washington; Washington, DC; 50342249301-004; NS; M; F; 02/03/86.
National Bank of Washington; Washington, DC; 50342249301-005; NS; PS; F; 02/03/86.
National Bank of Washington; Washington, DC; 50342249301-006; NS; T; F; 02/03/86.
New Jersey Council of Savings Institutions; West Orange, NJ; 50250360001-001; P; PS; F; 02/03/86.
New Jersey Council of Savings Institutions; West Orange, NJ; 50250360001-002; P; PS; F; 02/03/86.
New Jersey Council of Savings Institutions; West Orange, NJ; 50250360001-003; P; M; F; 02/03/86.
New Jersey Council of Savings Institutions; West Orange, NJ; 50250360001-004; P; M; F; 02/03/86.
North Carolina Medical Society; Raleigh, NC; 50226950001-001; S; PS; F; 02/03/86.
North Carolina Medical Society; Raleigh, NC; 50326950001-002; NS; PS; F; 02/03/86.
North Carolina Medical Society; Raleigh, NC; 50226950001-003; S; M; F; 02/03/86.
North Carolina Medical Society; Raleigh, NC; 50326950001-004; NS; M; F; 02/03/86.
Northern Life Insurance Co; Seattle, WA; 50343890001-001; NS; PS; U; 01/13/86.
Northern Life Insurance Co; Seattle, WA; 50343890001-002; NS; M; U; 01/13/86.
Northern Life Insurance Co; Seattle, WA; 50243890001-003; S; PS; U; 01/13/86.
Northern Life Insurance Co; Seattle, WA; 50243890001-004; S; M; U; 01/13/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50344170701-001; NS; M; F; 03/25/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50244170701-002; P; M; F; 03/25/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50344170701-003; NS; PS; F; 03/25/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50244170701-004; P; PS; F; 03/25/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50344170702-001; NS; D; F; 03/25/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50344170702-002; NS; D; F; 03/25/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50244170702-003; P; D; F; 03/25/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50244170702-004; P; D; F; 03/25/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50344170703-001; NS; T; F; 03/25/86.
Northwestern Mutual Life Insurance Co; Milwaukee, WI; 50244170703-002; S; T; F; 03/25/86.
NS & T Bank NA; Washington, DC; 50242640003-001; S; T; F; 02/03/86.
NS & T Bank NA; Washington, DC; 50342640003-002; NS; T; F; 02/03/86.
Old Stone Trust Co; Providence, RI; 50345070701-001; NS; M; F; 03/25/86.
Old Stone Trust Co; Providence, RI; 50245070701-002; P; M; F; 03/25/86.
Old Stone Trust Co; Providence, RI; 50345070701-003; NS; PS; F; 03/25/86.
Old Stone Trust Co; Providence, RI; 50245070701-004; P; PS; F; 03/25/86.
Oneida National Bank; Utica, NY; 50345160001-001; NS; PS; U; 02/24/86.
Oneida National Bank; Utica, NY; 50245160001-002; S; PS; U; 02/24/86.
Oneida National Bank; Utica, NY; 50345160001-003; NS; PS; U; 02/24/86.
Oneida National Bank; Utica, NY; 50245160001-004; S; PS; U; 02/24/86.
Oneida National Bank; Utica, NY; 50345160001-005; NS; M; U; 02/24/86.
Oneida National Bank; Utica, NY; 50245160001-006; S; M; U; 02/24/86.
Oneida National Bank; Utica, NY; 50345160001-007; NS; M; U; 02/24/86.
Oneida National Bank; Utica, NY; 50245160001-008; S; M; U; 02/24/86.
Oneida National Bank; Utica, NY; 50345160001-009; NS; T; U; 02/24/86.
Oneida National Bank; Utica, NY; 50245160001-010; S; T; U; 02/24/86.
Oneida National Bank; Utica, NY; 50345160001-011; NS; T; U; 02/24/86.
Oneida National Bank; Utica, NY; 50245160001-012; S; T; U; 02/24/86.
Over The Counter Securities Fund Inc; Oreland, PA; 50245390001-001; P; PS; F; 02/14/86.
Over The Counter Securities Fund Inc; Oreland, PA; 50245390001-002; P; M; F; 02/14/86.
Pan American Bank of Orlando NA; Orlando, FL; 50345770001-001; NS; M; U; 02/17/86.
Pan American Bank of Orlando NA; Orlando, FL; 50345770001-002; NS; PS; U; 02/17/86.
Paul Revere Life Insurance Co; Worcester, MA; 50346050702-001; NS; D; F; 03/25/86.
Paul Revere Life Insurance Co; Worcester, MA; 50346050702-002; NS; D; F; 03/25/86.
Paul Revere Life Insurance Co; Worcester, MA; 50246050702-003; P; D; F; 03/25/86.
Paul Revere Life Insurance Co; Worcester, MA; 50246050702-004; P; D; F; 03/25/86.
Penn Mutual Life Insurance Co; Philadelphia, PA; 50346170701-001; NS; M; F; 03/25/86.
Penn Mutual Life Insurance Co; Philadelphia, PA; 50246170701-002; P; M; F; 03/25/86.
Penn Mutual Life Insurance Co; Philadelphia, PA; 50346170701-003; NS; PS; F; 03/25/86.
Penn Mutual Life Insurance Co; Philadelphia, PA; 50246170701-004; P; PS; F; 03/25/86.
Penn Mutual Life Insurance Co; Philadelphia, PA; 50346170703-001; NS; T; F; 03/25/86.
Penn Mutual Life Insurance Co; Philadelphia, PA; 50246170703-002; S; T; F; 03/25/86.
Pension Administrators Inc; Arlington Heights, IL; 50373070701-001; NS; M; F; 03/25/86.
Pension Administrators Inc; Arlington Heights, IL; 50373070701-002; NS; PS; F; 03/25/86.
Pension Administrators Inc; Arlington Heights, IL; 50373070702-001; NS; D; F; 03/25/86.
Pension Administrators Inc; Arlington Heights, IL; 50373070702-002; NS; D; F; 03/25/86.
Peoples Bank of Bloomington; Bloomington, IL; 50246600001-001; P; PS; F; 01/27/86.
Peoples Bank of Bloomington; Bloomington, IL; 50246600001-002; P; M; F; 01/27/86.
Peoples National Bank of Washington; Seattle, WA; 50247042201-001; P; PS; F; 03/31/86.
Peoples National Bank of Washington; Seattle, WA; 50247042201-002; P; M; F; 03/31/86.
Peoples National Bank of Washington; Seattle, WA; 50247042201-003; P; PS; F; 03/31/86.
Peoples National Bank of Washington; Seattle, WA; 50247042201-004; P; M; F; 03/31/86.
Phoenix Mutual Life Insurance Co; Hartford, CT; 50347410002-001; NS; D; F; 02/05/86.
Phoenix Mutual Life Insurance Co; Hartford, CT; 50347410002-002; NS; D; F; 02/05/86.
Phoenix Mutual Life Insurance Co; Hartford, CT; 50247410002-003; S; D; F; 02/05/86.
Phoenix Mutual Life Insurance Co; Hartford, CT; 50247410002-004; S; D; F; 02/05/86.
Piper Jaffray & Hopwood Inc; Minneapolis, MN; 50247730001-001; P; M; F; 01/16/86.
Piper Jaffray & Hopwood Inc; Minneapolis, MN; 50247730001-002; P; PS; F; 01/16/86.
PNC Trust Co of Florida NA; Scranton, PA; 50258760003-001; S; T; F; 02/03/86.

PNC Trust Co of Florida NA; Scranton, PA; 50028760003-003; NS; T; F; 02/03/86.

Profit Sharing Council of America; Chicago, IL; 50248370001-001; NS; PS; U; 03/19/86.

Prudential Bache Securities Inc; New York, NY; 50238155001-003; P; PS; U; 01/09/86.

Prudential Bache Securities Inc; New York, NY; 50238155001-004; P; M; U; 01/09/86.

Puget Sound National Bank; Tacoma, WA; 50348630002-001; P; D; F; 03/31/86.

Puget Sound National Bank; Tacoma, WA; 50248630002-002; P; D; F; 03/31/86.

Puget Sound National Bank; Tacoma, WA; 50248630002-003; P; D; F; 03/31/86.

Puget Sound National Bank; Tacoma, WA; 50248630002-004; P; D; F; 03/31/86.

Puget Sound National Bank; Tacoma, WA; 50348630002-005; NS; D; F; 03/31/86.

Puget Sound National Bank; Tacoma, WA; 50348630002-006; NS; D; F; 03/31/86.

Puget Sound National Bank; Tacoma, WA; 50348630002-007; NS; D; F; 03/31/86.

Puget Sound National Bank; Tacoma, WA; 50348630002-008; NS; D; F; 03/31/86.

R Meeder & Associates Inc; Columbus, OH; 50324630001-001; NS; M; F; 02/05/86.

R Meeder & Associates Inc; Columbus, OH; 50324630001-002; NS; M; F; 02/05/86.

Rainier National Bank; Seattle, WA; 50248830002-001; P; PS; F; 03/26/86.

Rainier National Bank; Seattle, WA; 50248830002-002; P; PS; F; 03/26/86.

Rainier National Bank; Seattle, WA; 50248830002-003; P; M; F; 03/26/86.

Rainier National Bank; Seattle, WA; 50248830002-004; P; M; F; 03/26/86.

Republic Bank & Trust Co; Louisville, KY; 50249080001-001; P; PS; F; 02/03/86.

Republic Bank & Trust Co; Louisville, KY; 50249080001-002; P; M; F; 02/03/86.

RepublicBank Dallas NA; Dallas, TX; 50349172203-001; NS; D; F; 03/31/86.

RepublicBank Dallas NA; Dallas, TX; 50349172203-002; NS; D; F; 03/31/86.

RepublicBank Dallas NA; Dallas, TX; 50349172203-003; NS; D; F; 03/31/86.

RepublicBank Dallas NA; Dallas, TX; 50349172203-004; NS; D; F; 03/31/86.

RepublicBank Dallas NA; Dallas, TX; 50349172203-005; NS; D; F; 03/31/86.

River Oaks Trust Co; Houston, TX; 50349600001-003; NS; PS; U; 02/03/86.

River Oaks Trust Co; Houston, TX; 50349600001-004; NS; M; U; 02/03/86.

Rochester Community Savings Bank; Rochester, NY; 50271980001-001; P; PS; F; 02/05/86.

Rochester Community Savings Bank; Rochester, NY; 50271980001-002; P; M; F; 02/05/86.

Rochester Community Savings Bank; Rochester, NY; 50371980001-003; NS; PS; F; 02/05/86.

Rochester Community Savings Bank; Rochester, NY; 50371980001-004; NS; M; F; 02/05/86.

Safeco Life Insurance Co; Seattle, WA; 50250050001-001; P; PS; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50250050001-002; P; M; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050002-001; NS; PS; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050002-002; NS; PS; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050002-003; NS; M; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050002-004; NS; M; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050003-001; NS; M; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050003-002; NS; M; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050003-003; NS; PS; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050003-004; NS; PS; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050003-005; NS; T; F; 02/03/86.

Safeco Life Insurance Co; Seattle, WA; 50350050004-001; NS; D; F; 03/24/86.

Safeco Life Insurance Co; Seattle, WA; 50350050004-002; NS; D; F; 03/24/86.

Safeco Life Insurance Co; Seattle, WA; 50350050004-003; NS; D; F; 03/24/86.

Safeco Life Insurance Co; Seattle, WA; 50350050004-004; NS; D; F; 03/24/86.

Security First National Bank; Sheboygan, WI; 50250842701-001; S; PS; F; 01/13/86.

Security First National Bank; Sheboygan, WI; 50350842701-002; S; M; F; 01/13/86.

Security First National Bank; Sheboygan, WI; 50350842701-003; NS; PS; F; 01/13/86.

Security First National Bank; Sheboygan, WI; 50350842701-004; NS; M; F; 01/13/86.

Security Mutual Life Insurance Co of New York; Binghamton, NY; 50350910701-001; NS; M; F; 03/25/86.

Security Mutual Life Insurance Co of New York; Binghamton, NY; 50250910701-002; P; M; F; 03/25/86.

Security Mutual Life Insurance Co of New York; Binghamton, NY; 50350910701-003; NS; PS; F; 03/25/86.

Security Mutual Life Insurance Co of New York; Binghamton, NY; 50250910701-004; P; PS; F; 03/25/86.

Seligman Common Stock Fund Inc; New York, NY; 50351320001-001; NS; PS; F; 02/03/86.

Seligman Common Stock Fund Inc; New York, NY; 50351320001-002; NS; M; F; 02/03/86.

Seligman Common Stock Fund Inc; New York, NY; 50251320001-003; S; PS; F; 02/03/86.

Seligman Common Stock Fund Inc; New York, NY; 50251320001-004; S; M; F; 02/03/86.

South Umpqua State Bank; Roseburg, OR; 50373080701-001; NS; M; F; 03/25/86.

South Umpqua State Bank; Roseburg, OR; 50273080701-002; P; M; F; 03/25/86.

South Umpqua State Bank; Roseburg, OR; 50373080701-003; NS; PS; F; 03/25/86.

South Umpqua State Bank; Roseburg, OR; 50273080701-004; P; PS; F; 03/25/86.

Southern Farm Bureau Life Insurance Co; Jackson, MS; 50352240702-001; NS; M; F; 03/25/86.

Southern Farm Bureau Life Insurance Co; Jackson, MS; 50252240702-002; P; M; F; 03/25/86.

Southern Farm Bureau Life Insurance Co; Jackson, MS; 50352240702-003; NS; PS; F; 03/25/86.

Southern Farm Bureau Life Insurance Co; Jackson, MS; 50252240702-004; P; PS; F; 03/25/86.

Southwestern Life Insurance Co; Dallas, TX; 50352600703-001; NS; T; F; 03/25/86.

Southwestern Life Insurance Co; Dallas, TX; 50252600703-002; S; T; F; 03/25/86.

Standard Security Life Insurance Co of New York; New York, NY; 50352940701-001; NS; M; F; 03/25/86.

Standard Security Life Insurance Co of New York; New York, NY; 50252940701-002; P; M; F; 03/25/86.

Standard Security Life Insurance Co of New York; New York, NY; 50352940701-003; NS; PS; F; 03/25/86.

Standard Security Life Insurance Co of New York; New York, NY; 50252940701-004; P; PS; F; 03/25/86.

Standard Security Life Insurance Co of New York; New York, NY; 50352940702-001; NS; D; F; 03/25/86.

Standard Security Life Insurance Co of New York; New York, NY; 50352940702-002; NS; D; F; 03/25/86.

Standard Security Life Insurance Co of New York; New York, NY; 50252940702-003; P; D; F; 03/25/86.

Standard Security Life Insurance Co of New York; New York, NY; 50252940702-004; P; D; F; 03/25/86.

Suburban Bank; Bethesda, MD; 50254190002-001; S; T; F; 02/05/86.

Suburban Bank; Bethesda, MD; 50354190002-002; NS; T; F; 02/05/86.

Texas Commerce Bancshares Inc; Houston, TX; 50299262601-006; S; PS; U; 03/28/86.

Tri-Continental Corp; New York, NY; 50355690001-001; NS; PS; F; 02/03/86.

Tri-Continental Corp; New York, NY; 50255690001-002; S; M; F; 02/05/86.

Tri-Continental Corp; New York, NY; 50255690001-003; S; PS; F; 02/05/86.

Tri-Continental Corp; New York, NY; 50355690001-004; NS; M; F; 02/05/86.

Unified Management Corp; Indianapolis, IN; 50255985001-001; S; PS; U; 01/09/86.

Unified Management Corp; Indianapolis, IN; 50255985001-002; S; M; U; 01/09/86.

Union Bank & Trust Co; Montgomery, AL; 50373090701-001; NS; M; F; 03/26/86.

Union Bank & Trust Co; Montgomery, AL; 50273090701-002; P; M; F; 03/26/86.

Union Bank & Trust Co; Montgomery, AL; 50373090701-003; NS; PS; F; 03/26/86.

Union Bank & Trust Co; Montgomery, AL; 50273090701-004; P; PS; F; 03/26/86.

Union Bank & Trust Co; Montgomery, AL; 50373090702-001; NS; D; F; 03/26/86.

Union Bank & Trust Co; Montgomery, AL; 50373090702-002; NS; D; F; 03/26/86.

Union Bank & Trust Co; Montgomery, AL; 50273090702-003; P; D; F; 03/26/86.

Union Bank & Trust Co; Montgomery, AL; 50273090702-004; P; D; F; 03/26/86.

Union Trust Co; New Haven, CT; 50356590702-001; NS; D; F; 03/25/86.

Union Trust Co; New Haven, CT; 50356590702-002; NS; D; F; 03/25/86.

Union Trust Co; New Haven, CT; 50256590702-003; P; D; F; 03/25/86.

Union Trust Co; New Haven, CT; 50256590702-004; P; D; F; 03/25/86.

United Jersey Bank; Princeton, NJ; 50257050001-001; S; D; F; 02/05/86.

United Jersey Bank; Princeton, NJ; 50257050001-002; S; D; F; 02/05/86.

United Jersey Bank; Princeton, NJ; 50257050001-003; S; D; F; 02/05/86.

United Jersey Bank; Princeton, NJ; 50257050001-004; S; D; F; 02/05/86.

United Jersey Bank; Princeton, NJ; 50257050001-005; S; D; F; 02/05/86.

United Jersey Bank; Princeton, NJ; 50357050002-001; NS; PS; F; 02/05/86.

United Jersey Bank; Princeton, NJ; 50357050002-002; NS; M; F; 02/05/86.

United Pacific Life Insurance Co; Federal Way, WA; 50257400701-001; P; M; F; 03/25/86.

United Pacific Life Insurance Co; Federal Way, WA; 50257400701-002; P; PS; F; 03/25/86.

United Services Advisers Inc; San Antonio, TX; 50370510001-001; NS; D; U; 02/17/86.

United Services Advisers Inc; San Antonio, TX; 50370510001-002; NS; D; U; 02/17/86.

United States Trust Co of New York; New York, NY; 50357630001-001; NS; PS; F; 02/10/86.

United States Trust Co of New York; New York, NY; 50357630001-002; NS; PS; F; 02/10/86.

United States Trust Co of New York; New York, NY; 50357630001-003; NS; M; F; 02/10/86.

United States Trust Co of New York; New York, NY; 50357630001-004; NS; M; F; 02/10/86.

Unity Mutual Life Insurance Co; Syracuse, NY; 50357730701-001; NS; M; F; 03/25/86.

Unity Mutual Life Insurance Co; Syracuse, NY; 50257730701-002; P; M; F; 03/25/86.

Unity Mutual Life Insurance Co; Syracuse, NY; 50357730701-003; NS; PS; F; 03/25/86.

Unity Mutual Life Insurance Co; Syracuse, NY; 50257730701-004; P; PS; F; 03/25/86.

Unity Mutual Life Insurance Co; Syracuse, NY; 50357730702-001; NS; D; F; 03/25/86.

Unity Mutual Life Insurance Co; Syracuse, NY; 50357730702-002; NS; D; F; 03/25/86.

Unity Mutual Life Insurance Co; Syracuse, NY; 50257730702-003; P; D; F; 03/25/86.

Unity Mutual Life Insurance Co; Syracuse, NY; 50257730702-004; P; D; F; 03/25/86.

Universal Programs Inc; New York, NY; 50271640001-001; P; PS; F; 02/14/86.

Universal Programs Inc; New York, NY; 50271640001-002; P; M; F; 02/14/86.

USAA Life Insurance Co; San Antonio, TX; 50257940001-001; P; M; F; 03/26/86.

USAA Life Insurance Co; San Antonio, TX; 50257940001-002; P; PS; F; 03/26/86.

USAA Life Insurance Co; San Antonio, TX; 50357940002-001; NS; M; U; 03/26/86.

USAA Life Insurance Co; San Antonio, TX; 50357940002-002; NS; M; U; 03/26/86.

USAA Life Insurance Co; San Antonio, TX; 50357940003-001; NS; PS; U; 03/26/86.

USAA Life Insurance Co; San Antonio, TX; 50357940003-002; NS; PS; U; 03/26/86.

USAA Life Insurance Co; San Antonio, TX; 50357940004-001; NS; M; U; 03/27/86.

USAA Life Insurance Co; San Antonio, TX; 50257940004-002; NS; M; U; 03/27/86.
USAA Life Insurance Co; San Antonio, TX; 50257940004-001; NS; PS; U; 03/27/86.
USAA Life Insurance Co; San Antonio, TX; 50257940003-002; NS; PS; U; 03/27/86.
Variable Annuity Life Insurance Co; Houston, TX; 50258340001-001; P; PS; F; 02/12/86.
Variable Annuity Life Insurance Co; Houston, TX; 50258340001-002; P; PS; F; 02/12/86.
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Variable Annuity Life Insurance Co; Houston, TX; 50258340001-004; P; M; F; 02/12/86.
Variable Annuity Life Insurance Co; Houston, TX; 50258340002-001; S; PS; F; 02/12/86.
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Variable Annuity Life Insurance Co; Houston, TX; 50358340002-004; NS; PS; F; 02/12/86.
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Wachovia Bank & Trust Co; Winston Salem, NC; 50258600001-001; S; PS; F; 02/03/86.
Wachovia Bank & Trust Co; Winston Salem, NC; 50258600001-002; NS; PS; F; 02/03/86.
Wachovia Bank & Trust Co; Winston Salem, NC; 50258600001-003; P; M; F; 02/03/86.
Wachovia Bank & Trust Co; Winston Salem, NC; 50258600001-004; NS; M; F; 02/03/86.
Wall Lake Savings Bank; Wall Lake, IA; 50258620001-001; S; PS; U; 02/21/86.
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Wheeling Dollar Savings & Trust Co; Wheeling, WV; 50359660001-001; NS; PS; F; 01/29/86.
Wheeling Dollar Savings & Trust Co; Wheeling, WV; 50359660001-002; NS; M; F; 01/29/86.
Wheeling Dollar Savings & Trust Co; Wheeling, WV; 50359660001-003; NS; PS; F; 01/27/86.
Wheeling Dollar Savings & Trust Co; Wheeling, WV; 50359660001-004; NS; M; F; 01/29/86.
Wheeling Dollar Savings & Trust Co; Wheeling, WV; 50259660002-001; S; PS; F; 01/29/86.
Wheeling Dollar Savings & Trust Co; Wheeling, WV; 50259660002-002; S; M; F; 01/29/86.
Wilmington Trust Co; Wilmington, DE; 50259860001-001; P; PS; F; 01/16/86.
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Wilmington Trust Co; Wilmington, DE; 50259860001-004; P; M; F; 01/16/86.
Woodmen Accident & Life Co; Lincoln, NE; 50260110702-001; NS; D; F; 03/25/86.
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Woodmen Accident & Life Co; Lincoln, NE; 50260110702-003; P; D; F; 03/25/86.
Woodmen Accident & Life Co; Lincoln, NE; 50260110702-004; P; D; F; 03/25/86.
World Life & Health Insurance Co; King Of Prussia, PA; 50260170001-001; S; M; F; 02/03/86.
World Service Life Insurance Co; Fort Worth, TX; 50261370701-001; P; M; F; 03/25/86.
World Service Life Insurance Co; Fort Worth, TX; 50261370701-002; P; PS; F; 03/25/86.
World Service Life Insurance Co; Fort Worth, TX; 50261370702-001; P; D; F; 03/25/86.
World Service Life Insurance Co; Fort Worth, TX; 50261370702-002; P; D; F; 03/25/86.

List B

Plans omitted from Announcement 85-99

Baptist Life Association; Buffalo, NY 50207610001-001; S; M.

First National Bank & Trust Co; Beatrice, NE; 50282150001-001; S; M.

First National Bank & Trust Co of Quincy; Quincy, IL; 50223370001-001; S; PS.

First National Bank of Long Island; Woodbury, NY; 50225470001-001; P; PS.

First National Bank of Long Island; Woodbury, NY; 50225470001-002; P; M.

Revision of Form 851, Affiliations Schedule

Announcement 86-71

Form 851, Affiliations Schedule, has been revised and is now available at most Internal Revenue Service Forms Distribution Centers. This revision replaces the May 1984 version of Form 851.

The revision, dated April 1986, reflects the new definition of an affiliated group in section 1504 of the Internal Revenue Code as amended by the Deficit Reduction Act of 1984 (Act). Under the new law, a corporation is required to own 80% or more of the voting power and 80% or more of the total fair market value of the stock of another corporation for the two corporations to be considered an affiliated group for purposes of filing a consolidated tax return.

The new law is effective for tax years beginning after December 31, 1984. However, a special transitional rule provided by section 60(b)(2) of the Act allows a corporation that was a member of an affiliated group on June 22, 1984, and that was included in the consolidated return of the group for its tax year that included June 22, 1984, to continue as a member of the affiliated group under the rules that existed before the Act was passed. The transitional rule does not apply to corporations that became affiliated after June 22, 1984, or to certain corporations that were affiliated by June 22, 1984, but had a sell-down or issuance of stock after June 22, 1984. For tax years beginning after 1987, all corporations must be affiliated under the revised rules in order to qualify for filing a consolidated return.

If the transitional rule applies to all corporations in an affiliated group, and the group has already filed a consolidated return for 1985 and attached the prior version (May 1984) of Form 851, no further action is required. However, if a 1985 consolidated return was filed and the transitional rule does not apply to corporations in the group, the parent corporation of the group must complete the April 1986 version of Form 851 for the group and send it to the Service Center where the group filed its 1985 consolidated return.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Gary E. Borushko	Grosse Pointe Woods, MI	Certified Public Accountant	Indefinite from April 7, 1986
Paul Skulsky	Spring Valley, NY	Certified Public Accountant	Indefinite from April 1, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Thomas H. Foxhill, Jr.	Pemberton, NJ	Enrolled Agent	April 12, 1986
Peter Parker	Baltimore, MD	Attorney	April 12, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.61-6(c)(3), 1.163-4, 1.451-1(d), 1.451-2(b), 1.454-1(a)(1)(i), 1.482-2(a), 1.482-2(c)(2), 1.483-1, 1.483-2, 1.1016-5(s), 1.1232-2, 25.2512-4, 25.2512-8, revised; 1.163-7, 1.446-2, 1.483-3 through 1.483-5, 1.1271-1 through 1.1275-5, added; 1.61-7(d), 1.249-1, 1.409-1(b)(1), 1.528-1(d), 1.582-1(e)(3)(i), 1.636-1(a)(1)(ii), 1.818-3(f), 1.861-2(a)(4), 1.993-1(g), 1.1001-1(g), 1.1012-1(f), 1.1037-1, 1.1232-1, 1.1232-3A, 1.6045-1(c), 1.6049-5, 1.6049-6(d), 1.9006-1(c)(1)(vii), 3.2(d), 3.3(b), 5f.163-1(f), 6a.103A-2(i)(2)(vi)(B), 514.23, amended; 1.1012-2, removed and new added; 1.7872-4(e), reproposed and revised.	Original issue discount rules, imputed interest rules, and safe haven interest rates	1986-18 I.R.B. 4	June 9, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

***A*—Individual.**
***Acq.*—Acquiescence.**
***B*—Individual.**
***BE*—Beneficiary.**
***BK*—Bank.**
***B.T.A.*—Board of Tax Appeals.**
***C*—Individual.**
***C.B.*—Cumulative Bulletin.**
***CFR*—Code of Federal Regulations.**
***CI*—City.**
***COOP*—Cooperative.**
***Ct.D.*—Court Decision.**
***CY*—County.**
***D*—Decedent.**
***DC*—Dummy Corporation.**
***DE*—Donee.**
***Del. Order*—Delegation Order.**
***DISC*—Domestic International Sales Corporation.**
***DR*—Donor.**
***E*—Estate.**
***EE*—Employee.**
***E.O.*—Executive Order.**
***ER*—Employer.**
***ERISA*—Employee Retirement Income Security Act.**
***EX*—Executor.**
***F*—Fiduciary.**
***FC*—Foreign Country.**
***FICA*—Federal Insurance Contributions Act.**
***FISC*—Foreign International Sales Company.**
***FPH*—Foreign Personal Holding Company.**
***F.R.*—Federal Register.**
***FUTA*—Federal Unemployment Tax Act.**
***FX*—Foreign Corporation.**
***G.C.M.*—Chief Counsel's Memorandum.**
***GE*—Grantee.**
***GP*—General Partner.**
***GR*—Grantor.**
***IC*—Insurance Company.**
***I.R.B.*—Internal Revenue Bulletin.**
***LE*—Lessee.**
***LP*—Limited Partner.**
***LR*—Lessor.**
***M*—Minor.**
***Nonacq.*—Nonacquiescence.**
***O*—Organization.**
***P*—Parent Corporation.**
***PHC*—Personal Holding Company.**
***PO*—Possession of the U.S.**
***PR*—Partner.**
***PRS*—Partnership.**
***PTE*—Prohibited Transaction Exemption.**
***Pub. L.*—Public Law.**
***REIT*—Real Estate Investment Trust.**
***Rev. Proc.*—Revenue Procedure.**
***Rev. Rul.*—Revenue Ruling.**
***S*—Subsidiary.**
***S.P.R.*—Statements of Procedural Rules.**
***Stat.*—Statutes at Large.**
***T*—Target Corporation.**
***T.C.*—Tax Court.**
***T.D.*—Treasury Decision.**
***TFE*—Transferee.**
***TFR*—Transferor.**
***T.I.R.*—Technical Information Release.**
***TP*—Taxpayer.**
***TR*—Trust.**
***TT*—Trustee.**
***U.S.C.*—United States Code.**
***X*—Corporation.**
***Y*—Corporation.**
***Z*—Corporation.**

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

SPECIAL ANNOUNCEMENTS

Announcement 86-72, page 52.
A public hearing will be held on June 26, 1986, on proposed regulations relating to effective dates and certain other issues arising under the employee benefit provisions of the Tax Reform Act of 1984.

Announcement 86-73, page 52.
A public hearing will be held on June 18, 1986, relating to the treatment of qualified real estate agents and direct sellers as nonemployees, the determination of employer liability for income tax withholding and employee social security taxes when an employee is treated as a nonemployee, and information reporting of direct sales and payments of remuneration for services.

INCOME TAX

Rev. Rul. 86-79, page 7.
Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for June 1986.

T.D. 8086, page 4.
Amendments to the regulations under section 103 of the Code relate to the election of the $10 million limitation on exempt small issues of industrial development bonds and to supplemental capital expenditure statements required with respect to certain small issues of tax-exempt industrial development bonds.

EMPLOYEE PLANS

T.D. 8085, page 5.
Amendments to the regulations under section 404(g) of the Code relate to the deduction of employer liability payments.

Finding Lists begin on page 57.
Announcement of Disbarments and Suspensions begin on page 53.
Announcement of Notice of Proposed Rulemaking on page 55.
Index for April and May begin on page 60.

Department of the Treasury
Internal Revenue Service

T22.23:

EXCISE TAXES

Rev. Proc. 86-25, page 9.
Partnership items; windfall profit tax. Temporary procedures for the tax treatment of partnership items to windfall profit tax, which were implemented by Rev. Proc. 84-4, are now found in sections 150.6232(c)-1 through 150.6232(c)-5 of the Temporary Excise Tax Regulations for removal years 1983 and 1984, and sections 51.6232(c)-1 through 51.6232(c)-5 of the Excise Tax Regulations for removal years after 1984. Rev. Proc. 84-4 obsoleted.

ADMINISTRATIVE

Rev. Proc. 86-25, page 9.
Partnership items; windfall profit tax. Temporary procedures for the tax treatment of partnership items to windfall profit tax, which were implemented by Rev. Proc. 84-4, are now found in sections 150.6232(c)-1 through 150.6232(c)-5 of the Temporary Excise Tax Regulations for removal years 1983 and 1984, and sections 51.6232(c)-1 through 51.6232(c)-5 of the Excise Tax Regulations for removal years after 1984. Rev. Proc. 84-4 obsoleted.

Rev. Proc. 86-26, page 9.
Forms; magnetic tape; Forms 940; reporting agents. Conditions are set forth under which reporting agents preparing Form 940, Employer's Federal Unemployment Tax Return, can furnish the required information on magnetic tape instead of paper documents.

Rev. Proc. 86-27, page 34.
Forms; magnetic tape; Forms 941 and 941E; reporting by agents. Requirements are set forth under which reporting agents preparing Form 941, Employer's Quarterly Federal Tax Return, and 941E, Quarterly Return of Withheld Federal Income Tax, can furnish the required information on magnetic tape instead of paper documents. Rev. Proc. 84-11 superseded.

Statement of Procedural Rules, page 49.
Miscellaneous amendments to the Statement of Procedural Rules (SPR) reflect changes in the fees charged for search and duplication services and for copies of returns and return information.

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 103.—Interest on Certain Governmental Obligations

26 CFR 1.103-10: Exemption for certain small issues of industrial development bonds.

T.D. 8086

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, SUBCHAPTER H, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Election of $10 Million Limitation on Exempt Small Issues of Industrial Development Bonds; Supplemental Capital Expenditure Statements

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final rule.

SUMMARY: This document contains regulatory amendments that change the existing regulatory requirement for electing the $10 million limitation for exempt small issues of industrial development bonds and eliminate the existing regulatory requirement to file certain supplemental capital expenditure statements with respect to certain small issues of tax-exempt industrial development bonds. The amendments also conform the regulations on exempt small issues to the increase in the limit on the size of such small issues, enacted by the Revenue Act of 1978 [Pub. 95-600, 1978-3 C.B. (Vol. 1) 1], and clarify rules regarding capital expenditures. The amendments affect issuers and holders of the exempt small issues, and principal users of facilities financed with the proceeds of these issues.

DATES: The elimination of the requirement to file capital expenditure statements implemented by the amendments to §1.103-10(b)(2)(vi) is effective on and after September 3, 1971. The amendments relating to the time for and manner of making the $10 million small issue election under §1.103-10(b)(2)(vi) are effective after May 2, 1986 except that issuers who, before October 29, 1986, make the election in the manner prescribed by §1.103-10(b)(2)(vi) as in effect prior to amendment by this Treasury decision will be treated as having made the election at the time and in the manner prescribed by §1.103-10(b)(2)(vi) as amended by this Treasury decision. The amendments to §1.103-10 relating to the increase in the limit on the size of small issues of industrial development bonds are effective for obligations issued after December 31, 1978, in taxable years ending after such date, and for capital expenditures made after December 31, 1978, with respect to obligations issued before January 1, 1979.

FOR FURTHER INFORMATION CONTACT: John A. Tolleris of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3590).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains amendments to the Income Tax Regulations (26 CFR Part 1) under section 103(b)(6)(D) of the Internal Revenue Code of 1954. These amendments revise the present requirements of §1.103-10(b)(2)(vi) relating to elections and supplemental capital expenditure statements with respect to certain small issues of tax-exempt industrial development bonds.

This Treasury decision was not preceded by a notice of proposed rulemaking soliciting public comments because the Treasury Department has determined that the rules promulgated herein will not adversely affect any taxpayer. Accordingly, it is found unnecessary to issue this Treasury decision with notice and public procedure under section (b) of Section 553 of title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

EXPLANATION OF PROVISIONS

This Treasury decision eliminates the requirement that issuers of exempt small issues of industrial development bonds file a statement with the Service in order to elect the $10 million small issue limitation; however, bond issuers would be required to make the election under section 103(b)(6) by timely making a notation thereof on their books or records with respect to the issue.

This Treasury decision also eliminates the requirement that principal users of facilities financed by certain small issues of tax-exempt industrial development bonds (with respect to which the $10 million limitation has been elected under section 103(b)(6)(D)) file annual supplemental capital expenditure statements concerning such facilities and copies of the election statement with certain income tax returns.

This Treasury decision also contains a provision to conform the Income Tax Regulations to the increase in the limitation, from $5 million to $10 million, in the size of certain exempt small issues, enacted by section 331(a) of the Revenue Act of 1978 (92 Stat. 2839) [Pub. L. 95-600, 1978-3 C.B. (Vol. 1) 1, 73]. This document also contains amendments to clarify rules regarding capital expenditures.

NONAPPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

REGULATORY FLEXIBILITY ACT

A general notice of proposed rulemaking is not required by 5 U.S.C. 553 for final regulations subject to 5 U.S.C. 553(b)(B). Therefore, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

DRAFTING INFORMATION

The principal author of these proposed amendments is John A. Tolleris of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

PAPERWORK REDUCTION ACT

The elimination of the collection of information contained in this regulation has been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. This reduction in the requirements has been approved by OMB under control number 1545-0940.

* * * * *

Adoption of amendments to the regulations.

Accordingly, 26 CFR Parts 1 and 602 are amended as follows:

INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

(26 CFR Part 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.103-10 also issued under 26 U.S.C. 103(b)(6). * * *

Par 2. Section 1.103-10 (relating to exemption for certain small issues of industrial development bonds) is amended as follows:

(1) The phrase "section 103(c)" is removed each place it appears as a reference or part of a reference and the phrase "section 103(b)" is inserted in lieu thereof as a reference or part of a reference.

(2) Paragraph (a) is amended by adding the following new sentence at the end thereof: "For bonds issued before January 1, 1979, in taxable years ending before such date, and for capital expenditures made before January 1, 1979, with respect to such bonds, paragraphs (b), (c), and (d) of this section shall be applied by substituting $5 million for $10 million."

(3) Paragraph (c)(2) is amended by revising the caption to read *"10 million or less refinancing issue."* and by removing "$5" each place it appears and inserting in lieu thereof "$10".

(4) Paragraph (d)(1) is amended by removing "$5" and inserting in lieu thereof "$10".

(5) Paragraph (d)(3)(ii) is amended by removing "$5" each place it appears and inserting in lieu thereof "$10".

(6) Paragraph (b)(2) is amended by revising the heading and subdivisions (i), (ii)*(a)*, and (vi) thereof, to read as follows:

§1.103-10 Exemption for certain small issues of industrial development bonds.

* * * * *

(b) *Small issue exemption.* * * *

(2) *$10 million or less.* (i) Under Section 103(b)(6)(D), the issuing State or local governmental unit may elect to have an aggregate authorized face amount of $10 million or less, in lieu of the $1 million exemption otherwise provided for in section 103(b)(6)(A), with respect to issues of obligations that are industrial development bonds (within the meaning of section 103(b)(2)) issued after October 24, 1968. If the election is made in a timely manner, the bonds will be treated as obligations of a State or local governmental unit described in section 103(a)(1) and §1.103-1 if the sum of—

(a) The aggregate face amount of the issue including the aggregate outstanding face amount of any prior $1 million or $10 million exempt small issues taken into account under section 103(b)(6)(B) and paragraph (d) of this section, and

(b) The aggregate amount of "section 103(b)(6)(D) capital expenditures" (within the meaning of paragraph (b)(2)(ii) of this section),

is $10 million or less. In the case of an issue of obligations that qualified for exemption under section 103(b)(6)(A) and this paragraph, if a section 103(b)(6)(D) capital expenditure made after the date of issue has the effect of making taxable the interest on the issue, under section 103(b)(6)(G) the loss of tax exemption for the interest shall begin only with the date on which the expenditure that caused the issue to cease to qualify under the $10 million limit was paid or incurred. See paragraph (b)(2)(vi) of this section for the time and manner in which the issuer may elect the $10 million exemption. See section 103(b)(6)(H) and paragraph (c)(2) of this section for the treatment of certain refinancing issues of $10 million or less.

(ii) * * *

(a) The capital expenditure was financed other than out of the proceeds of issues to the extent such issues are taken into account under paragraph (b)(2)(i)*(a)* of this section.

* * * * *

(vi) The issuer may make the election provided by section 103(b)(6)(D) and this paragraph (b)(2) (assuming that the bonds otherwise qualify under section 103(b)(6)) by noting the election affirmatively at or before the time of issuance of the issue in question on its books or records with respect to the issue. The term "books or records" includes the bond resolution or other similar legislation for the issue in question as well as the bond transcript or other compilation of bond and bond-related documents. If the issuer fails to make an election at the time and in the manner prescribed in this paragraph (b)(2), the issue will not be treated as described in section 103(b)(6)(D), and interest thereon will be includible in gross income.

* * * * *

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

(26 CFR Part 602)

Par. 3 The authority citation for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805

Par. 4. Section 602.101(c) is amended by inserting in the appropriate place in the table "§1.103-10(b)(2)(vi). . . . 1545-0940".

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved March 28, 1986

J. Roger Mentz,
Acting Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on May 1, 1986, 8:45 a.m., and published in the issue of the Federal Register for May 2, 1986, 51 F.R. 16298)

Section 404.—Deduction for Contributions of an Employer to an Employees' Trust or Annuity Plan and Compensation under a Deferred-Payment Plan

26 CFR 1.404(g)-1: Deduction of employer liability payments.

T.D. 8085

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Deduction of Employer Liability Payments

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations concerning the deduction of employer liability payments. Changes to the applicable tax law were made by the Multiemployer Pension Plan Amendments Act of 1980 [Pub. L. 96-364, 1980-2 C.B. 437]. The regulations will provide the public with additional guidance needed to comply with that Act and will affect all employers that maintain qualified plans.

DATES: The amendments are effective for employer payments made after September 25, 1980.

FOR FURTHER INFORMATION CONTACT: Marjorie Hoffman of the Employee Plans and Exempt Organizations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T). Telephone 202-566-3430 (not a toll free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

On May 20, 1985, the FEDERAL REGISTER published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 404 of the Internal Revenue Code of 1954 (50 FR 20800) [EE-130-80, 1985-1 C.B. 610]. These amendments conform the regulations to section 205 of the Multiemployer Pension Plan Amendments Act of 1980 (94 Stat. 1287) [Pub. L. 96-364, 1980-2 C.B. 437, 446]. No comments were submitted on the proposed amendments. No public hearing on the proposed amendments was requested. Accordingly, the amendments are adopted by this Treasury decision substantially as they appeared in the FEDERAL REGISTER. Typographical errors which were contained in the notice of proposed rulemaking have been corrected.

EXECUTIVE ORDER 12291 AND REGULATORY FLEXIBILITY ACT

The Treasury Department has determined that this regulation is not subject to review under Executive Order 12291 and that a regulatory impact analysis therefore is not required.

Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these final regulations is Marjorie Hoffman of the Employee Plans and Exempt Organizations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 1 is amended as follows:

PART 1—[AMENDED]

Paragraph 1. The authority citation for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 2. The following new §1.404(g)-1 is added immediately after §1.404(e)-1A.

§1.404(g)-1 Deduction of employer liability payments.

(a) *General rule.* Employer liability payments shall be treated as contributions to a stock bonus, pension, profit-sharing, or annuity plan to which section 404 applies. Such payments that satisfy the limitations of this section shall be deductible under section 404 when paid without regard to any other limitations in section 404.

(b) *Employer liability payments.* For purposes of this section, employer liability payments mean:

(1) Any payment to the Pension Benefit Guaranty Corporation (PBGC) for termination or withdrawal liability imposed under section 4062 (without regard to section 4062(b)(2)), 4063, or 4064 of the Employee Retirement Insurance Security Act of 1974 (ERISA) [Pub. L. 93-406, 1974-3 C.B. 1]. Any bond or escrow payment furnished under section 4063 of ERISA shall not be considered as a payment of liability until applied against the liability of the employer.

(2) Any payment to a non-multiemployer plan pursuant to a commitment to the PBGC made in accordance with PBGC Determination of Plan Sufficiency and Termination of Sufficient Plans. See PBGC regulations, 29 CFR 2617.13(b) for rules concerning these commitments. Such payments shall not exceed an amount necessary to provide for, and used to fund, the benefits guaranteed under section 4022 of ERISA.

(3) Any payment to a multiemployer plan for withdrawal liability imposed under part 1 of subtitle E of title IV of ERISA. Any bond or escrow payment furnished under such part shall not be considered as a payment of liability of the employer.

(c) *Limitations, etc.*—(1) *Permissible expenses.* A payment shall be deductible under section 404(g) and this section only if the payment satisfies the conditions of section 162 or section 212. Payments made by an entity which is liable for such payments because it is a member of a commonly controlled group of corporations, or trades or businesses, within the meaning of section 414(b) or (c), shall not fail to satisfy such conditions merely because the entity did not directly employ participants in the plan with respect to which the liability payments were made.

(2) *Qualified plan.* A payment shall be deductible under section 404(g) and this section only if the payment is made in a taxable year of the employer ending within or with a taxable year of the trust for which the trust is exempt under section 501(a). For purposes of this paragraph, the payment timing rules of section 404(a)(6) shall apply.

(3) *Full funding limitation.* (i) If the employer liability payment is to a plan, the total amount deductible for such payment and for other plan contributions may not exceed an amount equal

to the full funding limitation as defined in section 412(c)(7) for the taxable year with respect to which the contributions are deemed made under section 404.

(ii) If the total contributions to the plan for the taxable year including the employer liability payment exceed the amount equal to this full funding limitation, the employer liability payment shall be deductible first.

(iii) Any amount paid in a taxable year in excess of the amount deductible in such year under the full funding limitation shall be treated as a liability payment and be deductible in the succeeding taxable years in order of time to the extent of the difference between the employer liability payments made in each succeeding year and the maximum amount deductible for such year under the full funding limitation.

(4) *Maximum deduction allowable under section 404*. The amount deductible under section 404 is limited to the higher of the maximum amount deductible by the employer under section 404(a) or the amount otherwise deductible under section 404(g). If the contributions are to a plan to which more than one employer contributes, this limit shall apply to each employer separately rather than all employers in the aggregate. Thus, each employer may deduct the greater of its allocable share of the deduction determined under sections 404(a) and 413(b)(7) or 413(c)(6) or its allocable share of the amount deductible under section 404(g).

However, pursuant to the rule in subdivision (ii) of subparagraph (3), in determining each employer's allocable share under section 404(a), the total amount deductible under section 404(a) by all employers shall not exceed the difference between the full funding limitation and the total amount deductible by all employers under section 404(g).

(5) *Example*. The provisions of this paragraph may be illustrated by the following example:

Example. In the 1983 taxable year, Employer *A* makes a withdrawal liability payment of $700,000 to multiemployer Plan *X* to which Employer *A* and Employer *B* are required to contribute. Employer *A*'s allocable share of the deduction allowable under sections 404(a) and 413(b)(7) in the 1983 taxable year is $600,000. Employer *B*'s allocable share of the deduction allowable under section 404(a) and 413(b)(7) in the 1983 taxable year is $400,000.

The full funding limitation for the 1983 taxable year is $1,000,000. Based on paragraph (c)(4) of this section, Employer A may deduct $700,000, the amount of the withdrawal liability payment. However, the deduction of Employer *B* is limited to $300,000, the difference between the full funding limitation and the amount deductible under section 404(g).

(d) *Effective date etc.*—(1) *General rule*. This section is effective for employer payments made after September 25, 1980.

(2) *Transitional rule*. For employer payments made before September 26, 1980, for purposes of section 404, any amount paid by an employer under section 4062, 4063, or 4064 of the Employee Retirement Income Security Act of 1974 [Pub. L. 93-406, 1974-3 C.B. 1, 198-200] shall be treated as a contribution to which section 404 applies by such employer to or under a stock bonus, pension, profit-sharing, or annuity plan.

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

Approved April 14, 1986.

J. ROGER MENTZ,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on May 1, 1986, 8:45 a.m., and published in the issue of the Federal Register for May 2, 1986, 51 F.R. 16297)

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of June 1986. See Rev. Rul. 86-79, below.

Section 483.—Interest on Certain Deferred Payments

Federal short-term, mid-term and long-term rates are set forth for the month of June 1986. See Rev. Rul. 86-79, below.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 467, 483 7872.)

Rev. Rul. 86-79

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of June 1986 are as follows:

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term				
AFR	6.74%	6.63%	6.58%	6.54%
110% AFR	7.42%	7.29%	7.22%	7.18%
120% AFR	8.12%	7.96%	7.88%	7.83%
Mid-Term				
AFR	7.32%	7.19%	7.13%	7.08%
110% AFR	8.07%	7.91%	7.83%	7.78%
120% AFR	8.82%	8.63%	8.54%	8.48%
Long-term				
AFR	7.64%	7.50%	7.43%	7.39%
110% AFR	8.42%	8.25%	8.17%	8.11%
120% AFR	9.20%	9.00%	8.90%	8.84%

Section 3504.—Acts to be Performed by Agents

26 CFR 31.3504-1: Acts to be performed by agents.

Requirements for the filing of Form 940 on magnetic tape by reporting agents. See Rev. Proc. 86-26, page 9.

26 CFR 31.3504-1: Acts to be performed by agents.

Requirements for the filing of Forms 941 and 941E on magnetic tape by reporting agents. See Rev. Proc. 86-27, page 34.

Section 4996.—Other Definitions and Special Rules

26 CFR 51.4996-1: Definitions.

Procedures for the tax treatment of partnership items for windfall profit tax purposes. See Rev. Proc. 86-25, page 9.

Section 4997.—Records and Information; Regulations

26 CFR 51.4997-1: Returns and recordkeeping.

Procedures for the tax treatment of partnership items for windfall profit tax purposes. See Rev. Proc. 86-25, page 9.

Section 6011.—General Requirement of Return, Statement or List

26 CFR 31.6011(a)-1: Returns under Federal Insurance Contributions Act.

Requirements for the filing of Form 940 on magnetic tape by reporting agents. See Rev. Proc. 86-26, page 9.

26 CFR 31.6011(a)-1: Returns under Federal Insurance Contributions Act.

Requirements for the filing of Forms 941 and 941E on magnetic tape by reporting agents. See Rev. Proc. 86-27, page 34.

Section 6232.—Extension of Subchapter To Windfall Profit Tax

26 CFR 51.6232(c)2-1: Partnership authorized to act on behalf of partners for removal year 1983 or 1984.

Procedures for the tax treatment of partnership items for windfall profit tax purposes. See Rev. Proc. 86-25, page 9.

Section 6402.—Authority to Make Credits or Refunds

26 CFR 51.6402-1: Credit or refund of overpayment of windfall profit tax.

Procedures for the tax treatment of partnership items for windfall profit tax purposes. See Rev. Proc. 86-25, page 9.

Section 7872.—Treatment of Loans with Below-Market Interest Rates

Federal short-term, mid-term and long-term rates are set forth for the month of June 1986. See Rev. Rul. 86-79, page 7.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.601: Rules and regulations.
(Also Part I, Sections 4996, 4997, 6232, 6402; 51.4996-1, 51.4997-1, 51.4997-2, 51.6232(c)-1, 150.6232(c)-1, 51.6402-1.)

Rev. Proc. 86-25

Rev. Proc. 84-4, 1984-1 C.B. 363, sets out temporary procedures for the implementation of section 6232 of the Internal Revenue Code relating to the tax treatment of partnership items to the windfall profit tax. That revenue procedure is obsolete. Procedures for the tax treatment of partnership items for windfall profit tax purposes are now found in sections 150.6232(c)-1 through 150.6232(c)-5 of the Temporary Excise Tax Regulations for removal years 1983 and 1984 and sections 51.6232(c)-1 through 51.6232(c)-5 of the Excise Tax Regulations for removal years after 1984. General rules and definitions relating to all years are found in sections 51.6232(a)-1 and 51.6232(a)-2 of the regulations.

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26 CFR 601.602 Tax Forms and instructions.
(Also Part I, Sections 3504, 6011; 31.3504-1, 31.6011(a)-1.)

Rev. Proc. 86-26

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to set forth requirements and conditions under which reporting agents preparing Form 940, Employer's Federal Unemployment Tax Return, for groups of taxpayers can furnish the required information in the form of magnetic tape instead of paper documents.

.02 If a reporting agent is unable to comply with the changes in specifications, he/she should contact the local Magnetic Tape Coordinator for Business Tax Returns for further instructions.

.03 The procedures for filing Form 940 on magnetic tape differ from the procedures for filing Forms 941 and 941E on magnetic tape, principally in the Tax Data Records. Whereas in reporting Form 941, there is one Tax Data "B" Record, in reporting Form 940 there are three types of Tax Data "B" Records, "B1," "B2" and "B3".

The need for three different records was established when the return was analyzed. Form 940 is complex with five different parts. Questions A and B at the top of the form determine which parts are required. In addition, in at least two places the return allows for multiple repeating lists: 1) multiple reasons for exempt payments, and 2) multiple entries of state codes and experience rates in Part 5.

To deal with the multiple list problem without paper attachments or tying up large pieces of record formats with seldom used fields, the specifications allow some record types ("B2" and "B3") to be repeated to take care of virtually all taxpayers.

Furthermore, because information as the states to which credit reduction will apply is not available until November of each year, all states and applicable territories are treated as potential credit reduction states.

In addition, many intermediate fields (i.e. fields resulting from the addition, subtraction and multiplication of primary data fields) have been omitted from the "B" Record specification. The test of the final result field, "Total FUTA Tax," against the generated results of the primary fields (i.e. fields only available from taxpayer records) will be used to determine the accuracy of the calculation of the correct tax by the reporting agent.

If an agent chooses not to develop software for exceptional cases, he/she may choose to file those returns on paper.

SEC. 2. APPLICATION FOR TAPE REPORTING

.01 Agents who desire to file authorized federal tax returns on magnetic tape must first file a letter of application or submit Form 4995, Application for Magnetic Tape Filing of Federal Business Tax Returns (previously known as Application for Magnetic Tape Filing of Form 941, Employer's Quarterly Federal Tax Return). A separate application must be submitted for each type of tax return filed (e.g. 941, 941E, 940). A separate revenue procedure applies to filing Forms 941 or 941E on magnetic tape. The letter of application should be addressed to the Director, Internal Revenue Service Center, Attention: Magnetic Tape Coordinator for Business Tax Returns, of the service center that serves the primary business address of the reporting agent. Addresses of the Internal Revenue Service Centers are shown in Section 9 of this revenue procedure. The letter of application must contain the following:

1. Name, address and EIN (Employer Identification Number) of the person, organization, or firm making the application.
2. Name, title, and telephone number of the person to contact regarding the application.
3. Type and nature of equipment to be used to prepare the tape file, i.e., manufacturer and model of main frame and tape drives, tape width, density (characters per inch), and recording mode (e.g. BCD, EBCDIC and ASCII).
4. List of the taxpayers to be included on the initial establishment of the Magnetic Tape Filing system. The list must be in triplicate with the data shown in the exact order as Exhibit 1. Show each taxpayer's name, complete address (including Zip Code), and EIN. Sort into EIN sequence. See section 6.03 for additional details.
5. The service center where paper tax returns were last filed.
6. Signature of the agent or agent's employee authorized to prepare federal tax returns for taxpayers.
7. An agreement by the reporting agent to keep copies of the Powers of Attorney (POA) on file at the agent's principal place of business for examination by the Service upon request. Such copies must be retained until the statute of limitations for the last return filed under its authority expires.
8. An agreement to fully pay the tax by Federal Tax Deposits.

NOTE: This revenue procedure does not restrict a non-financial organization who performs a payroll or tax service from being a reporting agent. See Rev. Proc. 80-31, 1980-2 C.B. 760, concerning the requirements under which FTDs can be made by the reporting agent.

9. An agreement to fully pay contributions to state unemployment funds on time and to timely file related state unemployment tax returns.
10. The first tax period for which the agent plans to file returns on magnetic tape.

11. The estimated volume of returns the agent plans to file by type of return (e.g. 941, 941E or 940).

SEC. 3. POWER OF ATTORNEY

.01 A POA must be submitted for each filer on the list attached to Form 4995 or the letter of application. The POA may be submitted on Form 2848, Power of Attorney and Declaration of Representative, which is available on request; or any other instrument which clearly states that the reporting agent is granted the authority to file and sign the return. The POA filed under this revenue procedure is not subject to the rules contained in the Conference and Practice Requirements (Treasury Regulation 601.502). The POA may cover the filing of both Forms 940 and 941 if desired.

.02 Both the taxpayer, or his authorized representative, and the reporting agent must sign the POA. The signed document will remain in effect until such time as it is revoked by the taxpayer, terminated by written notification from the reporting agent, or expires under its own terms.

1. The following persons may execute a POA on behalf of a corporation or other business taxpayer:

(a) The individual, if the person required to make the return is an individual;

(b) The president, vice president, or other principal officer, if the person required to make the return is a corporation;

(c) A responsible and duly authorized member or officer having knowledge of its affairs, if the person required to make the return is a partnership or other unincorporated organization.

(d) The fiduciary, if the person required to make the return is a trust or estate; or

(e) An agent who is duly authorized in accordance with section 31.6011(a)-7 of the Employment Tax Regulations.

.03 The scope of the POA for magnetic tape filing will be governed according to the following:

1. POA will delegate to the reporting agent the power to sign and file appropriate federal tax returns.

2. The POA becomes effective for the tax period the agent notifies the Service that the employer or filer is being added to the Magnetic Tape Filing system and remains in effect for subsequent periods until revoked, terminated or expired.

3. The POA is automatically revoked when the reporting agent notifies the Service that a taxpayer is no longer included in the Magnetic Tape Filing system.

4. The receipt of a POA for magnetic tape filing has no effect on prior Powers of Attorney on file for other purposes for a given taxpayer.

5. The POA for magnetic tape filing is a limited power of attorney, i.e., notices, refunds and other output resulting from filing on magnetic tape will be mailed to the taxpayer.

6. Requests from a reporting agent for information or adjustments on an account for which the taxpayer has authorized magnetic tape filing will be honored by the service center.

7. Requests for address changes may not be made by the reporting agent. Requests for address changes for taxpayers that are reported under magnetic tape filing will be processed only if they originate with one of the following:

(a) The taxpayer,

(b) An employee of the Service, or

(c) An attorney-in-fact if the attorney has a full POA for all tax matters concerning a taxpayer, and has filed a copy of the POA with the Service.

SEC. 4. APPROVAL OF AGENTS APPLICATION

.01 The Service will act on applications and notify applicants of authorization or disapproval within 30 days of receipt of Form 4995 or a letter of application as defined in Section 2.

.02 Generally, reporting agents using equipment compatible with the Service's can presume that tape filing will be approved. Compatible tape characteristics are shown in Section 11. If the reporting agent has the capability to prepare several types of tapes, the Service prefers that compatible tapes be prepared.

.03 If the reporting agents propose to submit convertible tapes, i.e., tapes requiring translation, the Service will either translate these tapes or provide translation through other government agencies. Magnetic tape filing will be disapproved when the Service is unable to obtain facilities to translate a reporting agent's file to a compatible form. (See Sections 10 and 11 for specifications.)

.04 Once authorization to file tax data on magnetic tape has been granted to a reporting agent, such approval will continue to effect in succeeding tax periods as long as the requirements of this revenue procedure are met, and there are no equipment changes by the reporting agent. However, new applications are required if users change from compatible tapes to equipment producing tapes that require translation, or if they discontinue magnetic tape filing for one or more periods, then decide to resume this method of reporting.

SEC. 5. EFFECT ON PAPER DOCUMENTS

.01 Authorization to file on magnetic tape does not prohibit the filing on paper tax returns, but merely permits filing of such returns on the Magnetic Tape Filing system. If for some reason (e.g. late receipt of records), an agent prefers to file a paper return for a given taxpayer, the agent may do so even after having been given authorization to file that taxpayer's returns on magnetic tape.

.02 The initial filing of tax returns on magnetic tape will be on trial tapes. Each taxpayer included on the magnetic tape must also be on the paper form until authorized by the Service to discontinue filing returns on paper. The paper returns must be arranged in the same order as the returns reported on the magnetic tape and in the same shipment. In general, the Service will notify the reporting agent to discontinue filing paper returns within 90 days after the initial filing of magnetic tape. The notification will depend upon the feasibility of processing the magnetic tape submitted.

.03 Paper and magnetic tape returns for the same tax period must never be filed by a reporting agent at the same time for the same taxpayer unless the returns are filed during the trial period for the reporting agent described in section 5.02.

SEC. 6. FILING TAPE RETURNS

.01 Packaging, shipping, and mailing instructions will be provided in the letter granting initial approval issued by the Service in response to the letter of application for magnetic tape filing.

.02 The Service will allow a tape return to be submitted for those individually approved magnetic tape filers until the reporting agent formally notifies the Service that specific employers are being deleted from their current magnetic tape filing inventory.

.03 Section 6091(b) of the Internal Revenue Code requires that tax returns be filed at the Internal Revenue district (or service center serving that district) that services the legal residence or principal business address of the taxpayer. Thus, reporting agents must normally file taxpayer's returns at the appropriate service center as described above even if it means submitting magnetic tapes to more than one service center. This rule may not be violated unless a reporting agent has applied for and received permission from the Service to do so. Contact your Magnetic Tape Coordinator for Business Tax Returns for details.

.04 Approval by the Service of Form 4995 or a letter of application allows a reporting agent to file at any Internal Revenue service center that services his/her clients. If a reporting agent wishes to file at additional service centers, he/she should notify the Magnetic Tape Coordinator for Business Tax Returns of the service center where he/she originally applied at least 90 days prior to the initial transmittal to the new service center.

.05 The reporting agent will be provided with a validated copy of the agent's listing for taxpayers authorized to file on magnetic tape. This authorization will contain each taxpayer's EIN, four position alpha Name Control, and the District Office Code. This authorization will be the source of the EIN and Name Control to be used on magnetic tape by the reporting agent as an identification of each taxpayer.

It is imperative that this Name Control be retained in the agent's records and be used in each taxpayer's Tax Data "B1" Record (positions 73-76). It is used by the Service to ensure the correct recording of the taxpayer's return. Failure to use the correct Name Control can result in delays in processing the return and notices of delinquent filing being sent to the taxpayer.

.06 Enclose the following in the first box of the tape shipment to the service center:

1. Form 4996, Magnetic Tape Filing Transmittal for Federal Business Returns (previously known as Magnetic Tape Filing Transmittal for Form 941, Employer's Quarterly Federal Tax Return) or a letter of transmittal containing the information described below. File the Form 4996 or the letter of transmittal in duplicate.

2. The letter of transmittal should include:

a. Name and address of reporting agent

b. Type of tax return filed on the magnetic tape

c. Tax period

d. Number of tax returns filed on accompanying tape

e. Total taxes reported

f. Total taxes deposited

g. Service center in which the POA for filing returns on magnetic tape is located

h. Signature of transmitter, title and date.

3. A control listing identifying actual taxpayers previously approved by the Service for magnetic tape filing that are contained on the current tape file being submitted. List the taxpayers in EIN sequence with each taxpayer's name and address.

4. Only Form 940 data may be present on this magnetic tape. Any Form 941 or 941E data must be on separate tapes.

5. The reporting agent should notify the Magnetic Tape Coordinator for Business Tax Returns if the agent does not receive notification of receipt of the transmittal within 15 days from the date he/she sent the transmittal.

SEC. 7. ADDING AND DELETING FILERS FROM MAGNETIC TAPE FILING SYSTEM

.01 When adding or deleting filers, the Service must receive (in triplicate and in the same format as shown on Exhibit 1) a listing which contains the complete names, addresses and EIN's of the taxpayers the reporting agent wants added or deleted from the Magnetic Tape Filing system. The word "ADDITIONS" or "DELETIONS" should be entered after the title, "Agent's Listing," and the effective date.

.02 The Service will provide a validated copy of the updated agent's listing to the reporting agent. Under no circumstances is a new filer to be included on the Magnetic Tape Filing system until the validated copy is received from the Service.

.03 A POA authorization must be included for each taxpayer to be added to the Magnetic Tape Filing system.

.04 The reporting agent should indicate on the last magnetic tape return submitted for a filer that it is either the "Final Return" or a "Discontinued Filer" in the Tax Data "B" Record.

.05 The reporting agent may not always know that the final magnetic tape return for a particular taxpayer is being submitted at the time the tape is being sent in. When the reporting agent determines that the previous tape contained the last return to be prepared for the individual filer, action should be taken to notify the service center which authorized the magnetic tape filing of one of the following conditions:

1. The taxpayer is out of business (state the effective date) and will no longer be liable for filing returns (Final Return), or

2. The reporting agent will no longer be submitting returns on magnetic tape for the taxpayer who is still in business and is still liable for such returns (Discontinued Filer).

.06 List of proposed (Form 940) filer additions deletions, etc., must be received in the service center prior to the end of November. This will permit the Service to properly validate applications and to respond to the agent within 30 days of receipt of the lists. However, if at the time of filing the agent has not received a validated listing with the additions, he/she should not file a magnetic tape return for those taxpayers because he/she has not received a valid Name Control from the Service.

SEC. 8. DUE DATES

.01 The due dates prescribed for filing paper returns with the Service will also apply to magnetic tape filing of Forms 940.

.02 In no case should returns with more than one due date be included on one tape file.

SEC. 9. ADDITIONAL INFORMATION

Requests for additional copies of this revenue procedure, applications for magnetic tape filing, requests for copies of appropriate input record element specifications, and requests for tape filing information should be addressed to the Director, Internal Revenue Service Center, Attention: Magnetic Tape Coordinator of Business Tax Returns, at one of the following addresses:

1. North-Atlantic Region
   - (a) Andover Service Center
     Project 105 Coordinator (Stop 481)
     310 Lowell Street
     Andover, MA 05501
   - (b) Brookhaven Service Center
     Project 105 Coordinator (Stop 110)
     1040 Waverly Avenue
     Holtsville, NY 11742
2. Mid-Atlantic Region
   - (a) Philadelphia Service Center
     Project 105 Coordinator (Drop Point 433)
     P.O. Box 245
     Bensalem, PA 19020
3. Central Region
   - (a) Cincinnati Service Center
     Project 105 Coordinator
     (CSA:C Stop 43)
     P.O. Box 267
     Covington, KY 41019
4. Southeast Region
   - (a) Atlanta Service Center
     Project 105 Coordinator
     P.O. Box 47-421
     Doraville, GA 30362
   - (b) Memphis Service Center
     Project 105 Coordinator
     P.O. Box 30309
     Airport Mail Facility
     Memphis, TN 38130
5. Midwest Region
   - (a) Kansas City Service Center
     P.O. Box 24551
     Kansas City, MO 64131
6. Southwest Region
   - (a) Austin Service Center
     Management Support Branch
     (Stop 1055)
     P.O. Box 934
     Austin, TX 78767
7. Western Region
   - (a) Ogden Service Center
     1160 West 1200 South
     Ogden, UT 84201
   - (b) Fresno Service Center
     P.O. Box 12866
     Fresno, CA 93779

SEC. 10. CONVENTIONS AND DEFINITIONS

.01 Conventions

Certain conventions may be required by the programming system or equipment used by the reporting agent, with respect to header and trailer labels, record and tape marks. If present, the Service prefers that they adhere to American National Standards Institute (ANSI) X3.27 specifications. The Service will accept other specifications if facilities can be found to accommodate them. The Service reserves the right to reject tapes with other than ANSI X3.27 specifications. The tapes must adhere to the following at a minimum:

(a) Header Label
  (1) The first record on a reel only.
  (2) In accordance with ANSI X3.27, Volume Header Label (VOL1), First File Header Label (HDR1) and Second File Header Label (HDR2) are strongly preferred.

(b) Trailer Label
  (1) The last record on a reel only.
  (2) No restrictions apply as to number of characters or type of characters used.

(c) Record Mark
  (1) No restrictions apply to record marks.

(d) Tape mark

The tape mark should only follow an End of Reel "F" Record or an End of File "E" Record.

.02 Definitions

Element	Description
Reporting Agent	Person or organization preparing and filing magnetic tape equivalents of Federal tax returns.
Taxpayer	Persons or organization liable for the payment of tax. The taxpayer will be held responsible for the completeness, accuracy and timely submission of the magnetic tape files.
b	Denotes a blank position.
EIN	Employer Identification Number.
Record	A group of related fields of information, treated as a unit.
Blocked Records	Two or more records grouped together between interrecord gaps.
Blocking Factors	The number of records grouped together to form a block.
Unblocked Records	Single records written between interrecord gaps.
File	A file consists of all tape records submitted by a reporting agent.
Record Mark	Special character used either to limit the number of characters in data transfer or to separate blocked records on tape.
Tape Mark	Special character that is written on tape.
Special Character	Any character that is not a numeral, letter, or blank.
Reel	A spool of magnetic tape.
FTD	Federal Tax Deposit.
POA	Power of Attorney.

SEC. 11. MAGNETIC TAPE SPECIFICATIONS

.01 These specifications prescribe the required format and content of the records to be included in the file, but not the methods or equipment to be used in their preparation.

A compatible tape file must conform to all of the following:

Type of tape	1/2 inch Mylar base, oxide coated
Recording density	800, 1600 or 6250 CPI (characters per inch)
Parity	Even or odd
Interrecord Gap	3/4 inch
Recording Mode	7 channel binary coded decimal (BCD), 9 channel, EBCDIC, ASCII

.02 An acceptable file will contain, for each reporting agent, the following:

1. An Agent "A" Record,
2. A series of Tax Data "B1," "B2" and "B3" Records,
3. A series of Checkpoint "C" Records, and
4. An End of File "E" Record.
5. Multiple reel files will have an End of Reel "F" Record.

.03 All records including headers and trailers, if used, must be written at the same density.

.04 Affix an external label to each tape with the following information:

1. Name of reporting agent
2. Number of tax returns submitted on this reel of tape
3. Tax year YYMM (Year, Year, month, month) format
4. Density (800, 1600, 6250)
5. Channel (7 or 9)
6. Parity (odd or even)
7. Name of computer manufacturer
8. Computer Type (manufacturer's designation)
9. Tape Drive (manufacturer and type)
10. Sequence number of reel and total number of reels in file (for example, 1 of 3).

.05 Since the Service is not restricting magnetic tape filing to reporting agents with specific types of equipment, or prescribing the methods used to prepare the tape files, the Agent "A" Record, End of Reel "F" Record and End of File "E" Record perform the functions normally assigned to header and trailer labels and related conventions. The End of Reel "F" Record signals that no more Tax Data "B" Records are written on the reel, and the End of File "E" Record indicates that there is no further data to be processed. In addition to the functions stated above, the End of Reel "F" Record is used to balance each reel or each series of Tax Data "B" Records of the reporting agent on a reel.

.06 Record Length

The tape records prescribed in the specifications may be blocked or unblocked subject to the following:

(a) A block may not exceed 12,100 tape positions.

(b) If the use of blocked records would result in a short block at the end of a Tax Data "B" Record and the next record is too large to be included in the block, the remaining positions of the block should be filled with 9's or spaces. No other digits or characters other than 9's or spaces are specified or acceptable for filling (or padding) of any tape input data blocks.

(c) All records, except header and trailer labels, if used, are blocked.

.07 Data

Only character data may be used. This means numeric fields cannot use overpunched signs. Special characters should be limited to -, &, % or / and can only be used in the name line fields and the street address fields of Agent "A" Records and Tax Data "B" Records. Otherwise, characters must be numeric or alphabetic. All money fields should include 2 decimal positions on right.

.08 Agent "A" Record

Identifies the reporting agent who prepared and transmitted the tape file. When multiple reels are required for a single file, the Agent "A" Record must be repeated as the first record (second record if header labels are used) on every succeeding reel in the file, and the reel number must be incremented by 1 for each tape reel after the first reel. A reporting agent may include Tax Data "B" Records (of any type) prepared at more than one location on the same tape, but they must have the same DO Code; however, Tax Data "B" Records prepared at different locations with different DO Codes must be on separate files preceded by an Agent "A" Record. Contact the Magnetic Tape Coordinator for Business Tax Returns for additional details, if necessary.

Form 940 AGENT "A" RECORD

Tape Position	Element Name	Entry or Definition
1	Record Type	Enter "A". Must be first character of each Agent "A" Record.
2-3	District Office Code	Enter two numeric digit District Office Code furnished by the Service.
4-5	Reel Number	Serial number assigned by the reporting agent to each reel, starting with 01. If header labels are used and if they contain a reel sequence number field, this should be the same as reel sequence number.

FORM 940 AGENT "A" RECORD—Continued

Tape Position	Element Name	Entry or Definition
6-14	EIN-reporting agent	Enter the 9 numeric characters of the reporting agent's EIN. Do not include the hyphen.
15-18	"B1" Record Length	Enter the number of positions of the Agent "B1" Record (588). If record marks are used at the end of each record include them in the count. Right justify and zero fill except where noted.
19-22	"B2" Record Length	Enter the number of positions of the Agent "B2" Record (143). If record marks are used at the end of each record include them in the count. Right justify and zero fill except where noted.
23-26	"B3" Record Length	Enter the number of positions of the Agent "B3" Record (693). If record marks are used at the end of each record include them in the count. Right justify and zero fill except where noted.
27-66	Name Line 1—Agent	Enter first name line of reporting agent. Left justify and fill with blanks. (40 positions)
67-106	Name Line 2—Agent	Enter the 2nd name line of reporting agent. Left justify and fill with blanks. If not required, fill with blanks. (40 positions)
107-146	Street Address—reporting agent	Enter street address of reporting agent and blank fill. Fill with blanks if street address not required. (40 positions)
147-166	City—reporting agent	Enter city of reporting agent. Left justify and fill with blanks. (20 positions)
167-168	State Code—Reporting Agent	Enter the official Post Office two position state code. (2 positions)
169-177	Zip Code—Reporting Agent	Enter zip code of reporting agent. If not using extending zip codes, left justify blank fill. (9 positions)
178	Tax Period Year	The last digit of the calendar year for which the reporting agent is filing (i.e. 1 = 81, 2 = 82 etc.).

.09 Form 940 Tax Data "B" Records

1. Contains tax information for each filer reported by the reporting agent. The number of Tax Data "B" Records of any type appearing on one tape reel will depend on the number of taxpayers represented (only one tax return for each EIN).

2. Tax Data "B" Records may be blocked together with record types A, C, E or F or the Tax Data "B" Records may be blocked alone with record types A, C, E and F unblocked. Records should have a blocking factor for which blocks will not exceed 12,100 tape positions. All records must be fixed length and for the current tax period. All money amounts must contain dollars and cents, must be right justified with zero filling on left and must be zero filled if non-significant. Fields identified as indicators should always carry a value. Other non-money fields must be left justified and blank filled on right with blank filling of non-significant fields.

3. Directions for the use of the three types of "B" Records:

A. General Directors

1). A "B1" Record is required for all taxpayers. There can be only one per taxpayer.

2). If the taxpayer has employees in more than one state, then a "B3" Record is required. They must follow "B2" Records (if any are present) of the taxpayer.

3). Each "B3" Record will accommodate up to four additional states. Up to thirteen "B3" Records may be present. They must follow "B2" Records (if any are present) of the taxpayer.

4). A "B2" Record is used only if the taxpayer has more than ten separate reasons for exempting payments to employees from FUTA. The various reasons for exempting payments are defined in Section 13 of this revenue procedure. Up to four "B2" Records may follow a "B1" Record.

5). If any field is too small to accommodate the data, the return must be filed on pape. .

6). The single state filing indicator (position 153 of "B1" Record) is a key to the use of the "B1" and "B3" Records.

If the single state filing indicator is equal to zero, then only a "B1" Record is required and positions 449-588 should be blank and zero filled as appropriate.

If the single state filing indicator is equal to one or three, then only a "B1" Record is required but positions

449-588 will require some significant data.

If the single state filing indicator is equal to two, then at least one "B3" Record is needed in addition to the "B1" Record.

The single state filing indicator has no bearing on "B2" Records.

B. Directors for use of "B1" Record:

1). Positions 1-155 of the "B1" Record must contain significant data for all taxpayers.

2). Positions 156-168 (State Contributions) and 169-183 (State Reporting Number) of the "B1" Record must contain significant data if the employer is required to contribute to state unemployment funds.

3). Positions 184-196 (Total Payments to Employees) of the "B1" Record require data from all taxpayers.

4). Positions 197-209 (Payments in Excess of Maximum Taxable Wages) contain significant information if any employee's wages exceeded the maximum for the year.

5). Positions 210-231 (Total FUTA and Total Taxes Deposited plus Overpayment Credit fields) of the "B1" Record require significant data from all taxpayers.

6). Positions 232-242 (Overpayment From Previous Year) may or may not contain significant data depending on whether the taxpayer requested transfer of the previous year's overpayment.

7). Positions 243-253 (Excess) contain significant data only if Total Taxes Deposited plus Overpayment from Previous Year exceeds Total FUTA Tax.

8). Position 254 (Credit Elect Indicator) enables the taxpayer to make a decision as to whether overpayment will be refunded or transferred to the following year's account.

9). Positions 255-265 (Total Taxes Deposited This Year) should also contain significant data.

10). Positions 266-305 should contain significant data if Total FUTA Tax exceeded $100.00.

11). Positions 306-435 contain ten combinations of a two position exemption code and an 11 position dollar and cents amount of wages exempted. The exemption codes and their meanings may be found in Section 13.

12). Positions 436-448 (Credit Reduction Wages for Unpaid Advances to the States) should have significant data only if the state identified in positions 154-155 is a credit reduction state for a given year.

13). Positions 449-588 are a series of repeating fields which only require entries if more than one state is being reported by the taxpayer or the taxpayer is not required to make contributions to the state unemployment fund of the state in which he/she has employees, or if any part of the taxpayer's total taxable wages is exempt from state unemployment taxes. There are four series of five fields.

The five fields are:

a) Taxable payroll

b) Date experience rate took effect

c) Date experience rate was changed

d) State experience rate

e) Contributions made to state.

At least one series of those fields must be used by those taxpayers who are reporting for more than one state or are not required to make contributions to the state unemployment fund, or if any part of the taxpayer's total taxable wages is exempt from state unemployment taxes. Only if the employer's experience rate changes are the other three series used. If an employer has had more than four experience rates in a given year, the return must be filed on paper.

14). The experience rate group fields (positions 449-588) in the "B1" Record allow up to four different experience rates in a given year (i.e. initial rate and three changes).

15). If the employer was not required to pay contributions to the state unemployment fund of a particular state, only one experience rate group should contain significant data and it should be used in the following manner:

a) Taxable payroll—should have significant data

b) Date experience rate took effect—fill with 0101

c) Date experience rate was changed—fill with 1231

d) State experience rate—fill with five zeroes

e) Contributions paid to state—fill with ten zeroes.

C. Directions on use of "B2" Record:

1) Positions 1-13 must have significant data if a "B2" Record is used.

2) Positions 14-143 are ten groups of two fields. The two fields are exemption code and exemption amount. The exemption codes and their meanings can be found in Section 13 of this revenue procedure.

D. Directions on use of "B3" Record:

1) Positions 1-13 must have significant data if a "B3" Record is used.

2) Positions 14-693 contain four groups of fields. Each group is for a separate state code. Therefore each "B3" Record can accommodate reporting of an additional four states.

Positions 14-183 relate to the first state

Positions 184-353 relate to the second state

Positions 354-523 relate to the third state

Positions 524-693 relate to the fourth state.

3) Each state group in the "B3" Record is 170 positions. The state group is composed of the following fields:

a) State Code (2 positions)

b) Credit Reduction Wages (13 positions)

c) State Reporting Number (15 positions)

d) Four groups of experience rate fields.

The experience rate groups are composed as follows:

a) Taxable payroll (12 positions)

b) Date experience rate took effect (MMDD format)

c) Date experience rate was changed (MMDD format)

d) State experience rate (5 positions—all considered decimal)

e) Contributions paid to state (10 positions).

4) Credit Reduction Wages fields should only be significant if the state referenced in associated state code is a credit reduction state for the year in which the return is filed.

5) The experience rate group fields allow up to four different experience rates in a given year (i.e. an initial rate and three changes).

6) If the employer was not required to pay contributions to the state unemployment fund of a particular state, only one experience rate group should contain significant data and it should be used in the following manner:

a) Taxable payroll—should have significant data

b) Date experience rate took effect—fill with 0101

c) Date experience rate was changed—fill with 1231

d) State experience rate—fill with five zeroes

e) Contributions paid to state—fill with ten zeroes.

FORM 940 TAX DATA "B1" RECORD

Tape Position	Element Name	Entry or Description
1	Record Type	"B" must be the first character of each Form 940 "B1" Record.
2	Record Subtype	Enter "1".
3-37	First Name Line—Employer	First name line of the taxpayer. Left justify and fill with blanks. (35 positions)
38-72	Second Name Line—Employer	Second name line of the taxpayer. If a continuation of the first name line left justify and fill with blanks, otherwise blank fill. (35 positions)
73-76	Name Control	Enter the 4 position alpha/numeric name control from the Name Control furnished by the Service.
77-111	Street Address—Employer	Enter the street address of the employer. Left justify and blank fill. (35 positions)
112-131	City—Employer	Enter the city in which the taxpayer is located. Left justify and fill with blanks. (20 positions)
132-133	State-Code-Employer	Enter the state code for the taxpayer as assigned by the U.S. Postal Service. (2 positions)
134-142	Zip Code—Employer	Enter the Zip Code of the taxpayer. Left justify and blank fill if necessary. (9 positions)
143-151	EIN—Employer	Enter the taxpayer's EIN *Do not* include the hyphen. (9 positions)
152	Magnet Tape Filing Indicator	0—if the taxpayer is a continuing magnetic tape filer. 1—if the taxpayer is a first time magnetic tape filer. 2—if the taxpayer is filing a final magnetic tape return and will use a paper Form 940 in the future. 3—if the taxpayer is filing a final return because of discontinued operations. 4—if the taxpayer is a continuing magnetic tape filer and is changing the address contained in positions 77-142. 5—if the taxpayer is filing a final magnetic tape return, will use a paper Form 940 in the future, and is changing the address contained in positions 77-142. 6—if the taxpayer is filing a final return because of discontinued operations and is changing the address contained in positions 77-142. Note: Name changes (positions 3-72) should be reported directly to the Magnetic Tape Coordinator for Business Tax Returns.
153	Single State Filing Indicator	A one character (numeric) field used to describe the method in which a taxpayer files Form 940. Enter: 0—if the taxpayer has operations in a single state and would be eligible to only complete Parts 1, 2, and 4 of Form 940. 1—if the taxpayer has operations in a single state but would have to complete Parts 1, 3, 4, and 5 of Form 940 because he/she made no contribution to state unemployment funds. 2—if the taxpayer is filing for operations in several states.

FORM 940 TAX DATA "B1" RECORD—Continued

Tape Position	Element Name	Entry or Description
		3—if the taxpayer has operations in a single state and has made all the required contributions to state unemployment funds but would have to complete Parts 1, 3, 4, and 5 of Form 940 because a part of the taxpayer's total taxable wages is exempt from state unemployment taxes. Note: If the return being filed is non-taxable, the single state filing indicator should be set to zero.
154-155	State-Code-Employees	Usually same as positions 132-133. May differ if official business address is in different state than operations of business.
156-168	State Contributions	Enter the amount paid by the taxpayer to the state unemployment agency of the taxpayer's address. (13 positions)
169-183	State Reporting Number	Enter the primary state reporting number for the taxpayer assigned by the state unemployment agency where the taxpayer maintains his/her residence. left justify and blank fill as necessary. (15 positions)
184-196	Total payments including Exempt payments during the calendar year for services of employees	Part 1, line 1. (13 positions)
197-209	Payments in excess of maximum taxable wages	Part 1, Line 3. Maximum taxable wages for employee varies with year. (13 positions)
210-220	Total FUTA Tax	Gross FUTA tax less Total Tentative Credit plus Credit Reduction Amount. (11 positions)
221-231	Total taxes deposited plus overpayment from previous year	FTDs plus overpayment from previous year (if the taxpayer elected to apply the previous year's overpayment to this tax year). (11 positions)
232-242	Overpayment from Previous Year	Enter only if taxpayer made election last year to have overpayment applied to the next return. Enter zeros if no significant amount. Right justify and zero fill if significant. (11 positions)
243-253	Excess	Amount that total taxes deposited plus transfer of overpayment from previous year exceeds Total FUTA Tax. Enter zero if no significant amount. Right justify and zero fill it significant (11 positions).
254	Credit Elect Indicator	Enter zero if credit is to be applied to next return. Enter "1" if amount is to be refunded or if excess is zero.
255-265	Total taxes deposited for this tax year	Actual deposits made. (11 positions)

Note: Positions 266-305 report the quarterly accrual of the tax liability. It must have entries if Total FUTA Tax exceeds $100.00.

266-275	FUTA tax liability for first quarter	Part 4, first quarter tax liability. (10 positions)
276-285	FUTA tax liability for second quarter	Part 4, second quarter tax liability. (10 positions)

FORM 940 TAX DATA "B1" RECORD—Continued

Tape Position	Element Name	Entry or Definition
286-295	FUTA tax liability for third quarter	Part 4, third quarter tax liability. (10 positions)
296-305	FUTA tax liability for fourth quarter	Part 4, fourth quarter tax liability (10 positions)

Note: Positions 306-435 contain ten combinations of a two position exemption code and 11 position dollar and cents amount of wages exempted. The exemption codes to be used are described in Section 13.

Tape Position	Element Name	Entry or Definition
306-307	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
308-318	Exemption Amount	Enter the amount of the exemption for positions 306-307. Enter zeros if the corresponding exemption is blank.
319-320	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
321-331	Exemption Amount	Enter the amount of the exemption for positions 319-320. Enter zeros if the corresponding exemption is blank.
332-333	Exemption Code	Enter the approved 2 character (numeric) exemption code for th exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
334-344	Exemption Amount	Enter the amount of the exemption for positions 332-333. Enter zeros if the corresponding exemption is blank.
345-346	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
347-357	Exemption Amount	Enter the amount of the exemption for positions 345-346. Enter zeros if the corresponding exemption is blank.
358-359	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
360-370	Exemption Amount	Enter the amount of the exemption for positions 358-359. Enter zeros if the corresponding exemption is blank.
371-372	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
373-383	Exemption Amount	Enter the amount of the exemption for positions 371-372. Enter zeros if the corresponding exemption is blank.
384-385	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.

FORM 940 TAX DATA "B1" RECORD—Continued

Tape Position	Element Name	Entry or Definition
386-396	Exemption Amount	Enter the amount of the exemption for corresponding exemption is blank.
397-398	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
399-409	Exemption Amount	Enter the amount of the exemption for positions 397-398. Enter zeros if the corresponding exemption is blank.
410-411	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exenmption is claimed here.
412-422	Exemption Amount	Enter the amount of the exemption for positions 410-411. Enter zeros if the corresponding exemption is blank.
423-424	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exempton is claimed here.
425-435	Exemption Amount	Enter the amount of the exemption for positions 423-424. Enter zeros if the corresponding exemption is blank.

Note: Positions 436-588 relate to the state idenified in positions 154-155 whose reporting number is in positions 169-183. Right justify and zero fill money amounts. Blank fill unneeded date fields.

Tape Position	Element Name	Entry or Definition
436-448	Credit Reduction Wages for unrepaid advances to the states	Enter the wages included on line 6 of Part 1 in the state where the taxpayer maintains an address. (13 positions).

Note: Positions 449-483 relate to the initial experience rate of the state identified in positions 154-155.

Tape Position	Element Name	Entry or Definition
449-460	Taxable payroll as defined in state act	First entry Part 5, column 3.
461-464	Date an experience rate took effect	First entry Part 5, column 4, From-Date. If continued from previous year enter 0101. (Format is MMDD—Enter blanks if not present)
465-468	Date an experience rate was changed	First entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
469-473	State experience rate	First entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. (Expressed as a five position decimal).
474-483	Contributions actually paid to state	Enter Part 5, column 9, first entry.

Note: Positions 484-518 relate to the second experience rate (if asserted) of the state identified in positions 154-155.

Tape Position	Element Name	Entry or Definition
484-495	Taxable payroll as defined in state act	Second entry Part 5, column 3.
496-499	Date an experience rate took effect	Second entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).

FORM 940 TAX DATA "B1" RECORD—Continued

Tape Position	Element Name	Entry or Definition
500-503	Date an experience rate was changed	Second entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Formatt is MMDD—Enter blanks if not present).
504-508	State experience rate	Second entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. (Expressed as a five position decimal).
509-518	Contributions actually paid to state	Enter Part 5, column 9, second entry.

Note: Positions 519-553 relate to the third experience rate (if asserted) of the state identified in positions 154-155.

Tape Position	Element Name	Entry or Definition
519-530	Taxable payroll as defined in state act	Third entry Part 5, column 3.
531-534	Date an experience rate took effect	Third entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).
535-538	Date an experience rate was changed	Third entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
539-543	State experience rate	Third entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. (Expressed as a five position decimal).
544-553	Contributions actually paid to state	Enter Part 5, column 9, third entry.

Note: Positions 554-588 relate to the fourth experience rate (if asserted) of the state identified in positions 154-155.

Tape Position	Element Name	Entry or Definition
554-565	Taxable payroll as defined in state act	Fourth entry Part 5, column 3.
566-569	Date an experience rate took effect	Fourth entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).
570-573	Date an experience rate was changed	Fourth entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
574-578	State experience rate	Fourth entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. (Expressed as a five position decimal).
579-588	Contributions actually paid to state	Enter part 5, column 9, fourth entry.

Note: If more than four rate changes occurred in one year, a paper return must be filed.

FORM 940 TAX DATA "B2" RECORD

Note: Up to 4 Agent "B2" Records may follow a "B1" Record. Each "B2" Record contains ten combinations of a two position exemption code and 11 position dollar and cents amount of wages exempted. The exemption codes to be used are described in Section 13.

Tape Position	Element Name	Entry or Description
1	Record Type	"B" must be the first character of each Form 940 "B2" Record.
2	Record Subtype	Enter "2"
3-11	EIN—Employer	Enter the taxpayer's EIN.
12-13	Sequence Number	A unique two character (numeric) field which indicates the order of records in the agent's tape. The first "B2" Record for the current taxpayer will contain a sequence number of "02" all others will be incremented by 1 by the reporting agent.
14-15	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
16-26	Exemption Amount	Enter the amount of the exemption for positions 14-15. Enter zeros if the corresponding exemption is blank.
27-28	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
29-39	Exemption Amount	Enter the amount of the exemption for positions 27-28. Enter zeros if the corresponding exemption is blank.
40-41	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
42-52	Exemption Amount	Enter the amount of the exemption for positions 40-41. Enter zeros if the corresponding exemption is blank.
53-54	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
55-65	Exemption Amount	Enter the amount of the exemption for positions 53-54. Enter zeros if the corresponding exemption is blank.
66-67	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
68-78	Exemption Amount	Enter the amount of the exemption for positions 66-67. Enter zeros if the corresponding exemption is blank.
79-80	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
81-91	Exemption Amount	Enter the amount of the exemption for positions 79-80. Enter zeros if the corresponding exemptionis blank.

FORM 940 TAX DATA "B2" RECORD—Continued

Tape Position	Element Name	Entry or Definition
92-93	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
94-104	Exemption Amount	Enter the amount of the exemption for positions 92-93. Enter zeros if the corresponding exemption is blank.
105-106	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
107-117	Exemption Amount	Enter the amount of the exemption for positions 105-106. Enter zeros if the corresponding exemption is blank.
118-119	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
120-130	Exemption Amount	Enter the amount of the exemption for positions 118-119. Enter zeros if the corresponding exemption is blank.
131-132	Exemption Code	Enter the approved 2 character (numeric) exemption code for the exemption the taxpayer is claiming. Enter blanks if no exemption is claimed here.
133-143	Exemption Amount	Enter the amount of the exemption for positions 131-132. Enter zeros if the corresponding exemption is blank.

FORM 940 TAX DATA "B3" RECORD

**Note: 1) Up to thirteen (13) Agent "B3" Records may follow a "B1" or "B2" Record.
Right justify and zero fill significant money amounts. Blank fill unneeded date fields.
2) If more than four experience rate changes occurred in one year you must file a paper return for the taxpayer.**

Tape Position	Element Name	Entry or Description
1	Record Type	"B" must be the first character of each Form 940 "B3" Record.
2	Record Subtype	Enter "3".
3-11	EIN—Employer	Enter the taxpayer's EIN. Do not enter the hyphen.
12-13	Sequence Number	A unique two character (numeric) field which indicates the order of records in the agent's tape. The first "B3" Record for the current taxpayer will contain a sequence number computed by adding 1 to the sum of all the taxpyer's "B1" Records and "B2" Records. The others will be incremented by 1.

NOTE: Position 14-183 relate to the first state reported on a "B3" Record (positions 14-15).

Tape Position	Element Name	Entry or Description
14-15	State-Code	The two character state code assigned by the U.S. Postal Service for a state other than that of the taxpayer's residence.

FORM 940 TAX DATA "B3" RECORD—Continued

Tape Position	Element Name	Entry or Description
16-28	Credit reduction wages for unrepaid advances to the states	Enter the wages included on line 6 of Part 1 for the state reported in positions 14-15. (13 positions)
29-43	State reporting number	Enter the primary state reporting number for the taxpayer assigned by the state unemployment agency. Left justify and blank fill as necessary. (15 positions)
NOTE: Positions 44-78 relate to the initial experience rate of the state identified in positions 14-15.		
44-55	Taxable payroll as defined in state act	First entry Part 5, column 3. (12 positions)
56-59	Date an experience rate took effect	First entry Part 5, column 4, From-Date. If continued from previous year enter 0101. (Format is MMDD—Enter blanks if not present).
60-63	Date an experience rate was changed	First entry part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
64-68	State experience rate	First entry part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
69-78	Contributions actually paid to state	Enter Part 5, column 9, first entry.
NOTE: Positions 79-113 relate to the second experience rate (if asserted) of the state identified in positions 14-15.		
79-90	Taxable payroll as defined in state act	Second entry Part 5, column 3. (12 positions)
91-94	Date an experience rate took effect	Second entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).
95-98	Date an experience rate was changed	Second entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
99-103	State experience rate	Second entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
104-113	Contributions actually paid to state	Enter Part 5, column 9, second entry.
NOTE: Positions 114-148 relate to the third experience rate (if asserted) of the state identified in positions 14-15.		
114-125	Taxable payroll as defined in state act	Third entry Part 5, column 3. (12 positions)
126-129	Date an experience rate took effect	Third entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).

FORM 940 TAX DATA "B3" RECORD—Continued

Tape Position	Element Name	Entry or Description
130-133	Date an experience rate was changed	Third entry part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
134-138	State experience rate	Third entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
139-148	Contributions actually paid to state	Enter Part 5, column 9, third entry.

NOTE: Positions 149-183 relate to the fourth experience rate (if asserted) of the state identified in positions 14-15.

Tape Position	Element Name	Entry or Description
149-160	Taxable payroll as defined in state act	Fourth entry Part 5, column 3.
161-164	Date an experience rate took effect	Fourth entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).
165-168	Date an experience rate was changed	Fourth entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
169-173	State experience rate	Fourth entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
174-183	Contributions actually paid to state	Enter Part 5, column 9, fourth entry.

Note: Positions 184-353 relate to the second state (positions 184-185) reported on a "B3" Record. If more than 4 experience rate changes occur in a year, the return must be filed on paper.

Tape Position	Element Name	Entry or Description
184-185	State-Code	The two character state code assigned by the U.S. Postal Service for a state other than that of the taxpayer's residence. if not applicable blank fill.
186-198	Credit reduction wages for unrepaid advances to the states	Enter the wages included on line 6 of Part 1 for the state reported in positions 184-185 (13 positions)
199-213	State reporting number	Enter the primary state reporting number for the taxpayer assigned by the state unemployment agency. Left justify and blank fill as necessary. (15 positions)

Note: Positions 214-248 relate to the initial experience rate of the state reported in positions 184-185.

Tape Position	Element Name	Entry or Description
214-225	Taxable payroll as defined in state act	First entry Part 5, column 3.
226-229	Date an experience rate took effect	First entry Part 5, column 4, From-Date. If continued from previous year enter 0101. (Format is MMDD—Enter blanks if not present).
230-233	Date an experience rate was changed	First entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).

FORM 940 TAX DATA "B3" RECORD—Continued

Tape Position	Element Name	Entry or Description
234-238	State experience rate	First entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
239-248	Contributions actually paid to state	Enter part 5, column 9, first entry.

NOTE: Positions 249-283 relate to the second experience rate (if asserted) of the state identified in positions 184-185.

Tape Position	Element Name	Entry or Description
249-260	Taxable payroll as defined in state act	Second entry part 5, column 3.
261-264	Date an experience rate took effect	Second entry Part 5, column 4, From Date. (Format is MMDD—Enter blanks if not present).
265-268	Date an experience rate was changed	Second entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
269-273	State experience rate	Second entry part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
274-283	Contributions actually paid to state	Enter part 5, column 9, second entry.

NOTE: Positions 284-318 relate to the third experience rate (if asserted) of the state identified in positions 184-185.

Tape Position	Element Name	Entry or Description
284-295	Taxable payroll as defined in state act	Third entry Part 5, column 3.
296-299	Date an experience rate took effect	Third entry Part 5, column 4, From-Date. (format is MMDD—Enter blanks if not present).
300-303	Date an experience rate was changed	Third entry part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
304-308	State experience rate	Third entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
309-318	Contributions actually paid to state	Enter part 5, column 9, third entry.

NOTE: Positions 319-353 relate to the fourth experience rate (if asserted) of the state identified in positions 184-185.

Tape Position	Element Name	Entry or Description
319-330	Taxable payroll as defined in state act	Fourth entry Part 5, column 3.
331-334	Date an experience rate took effect	Fourth entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).

FORM 940 TAX DATA "B3" RECORD—Continued

Tape Position	Element Name	Entry or Description
335-338	Date an experience rate was changed	Fourth entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
339-343	State experience rate	Fourth entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
344-353	Contributions actually paid to state	Enter Part 5, column 9, fourth entry.

NOTE: Positions 354-523 relate to the third state reported on a "B3" Record. If more than 4 experience rate changes occur in a year, the return must be filed on paper.

Tape Position	Element Name	Entry or Description
354-355	State-Code	The two character state code assigned by the U.S. Postal Service for a state other than that of the taxpayer's residence. If not applicable blank fill.
356-368	Credit reduction wages for unrepaid advances to the states	Enter the wages included on line 6 of Part 1 for the state reported in positions 354-355.
369-383	State reporting number	Enter the primary state reporting number for the taxpayer assigned by the state unemployment agency. Left justify and blank fill as necessary.

NOTE: Positions 384-418 relate to the initial experience rate of the state identified in positions 354-355.

Tape Position	Element Name	Entry or Description
384-395	Taxable payroll as defined in state act	First entry Part 5, column 3.
396-399	Date an experience rate took effect	First entry Part 5, column 4, From-Date. If continued from previous year enter 0101. (Format is MMDD—Enter blanks if not present).
400-403	Date an experience rate was changed	First entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
404-408	State experience rate	First entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
409-418	Contributions actually paid to state	Enter Part 5, column 9, first entry.

NOTE: Positions 419-453 relate to the second experience rate (if asserted) of the state identified in positions 354-355.

Tape Position	Element Name	Entry or Description
419-430	Taxable payroll as defined in state act	Second entry Part 5, column 3.
431-434	Date an experience rate took effect	Second entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).

FORM 940 TAX DATA "B3" RECORD—Continued

Tape Position	Element Name	Entry or Description
435-438	Date an experience rate was changed	Second entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
439-443	State experience rate	Second entry part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
444-453	Contributions actually paid to state	Enter Part 5, column 9, second entry.

NOTE: Positions 454-488 relate to the third experience rate (if asserted) of the state identified in positions 354-355.

454-465	Taxable payroll as defined in state act	Third entry Part 5, column 3.
466-469	Date an experience rate took effect	Third entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).
470-473	Date an experience rate was changed	Third entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
474-478	State experience rate	Third entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
479-488	Contributions actually paid to state	Enter Part 5, column 9, third entry.

NOTE: Positions 489-523 relate to the fourth experience rate (if asserted) of the state identified in positions 354-355.

489-500	Taxable payroll as defined in state act	Fourth entry Part 5, column.
501-504	Date an experience rate took effect	Fourth entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).
505-508	Date an experience rate was changed	Fourth entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
509-513	State experience rate	Fourth entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
514-523	Contributions actually paid to state	Enter Part 5, column 9, fourth entry.

NOTE: Positions 524-693 relate to the fourth state reported on a "B3" Record. If more than 4 experience rate changes occur in a year, the return must be filed on paper.

524-525	State-Code	The two character state code assigned by the U.S. Postal Service for a state other than that of the taxpayer's residence. If not applicable blank fill.

FORM 940 TAX DATA "B3" RECORD—Continued

Tape Position	Element Name	Entry or Description
526-538	Credit reduction for unrepaid advances to the states	Enter the wages included on line 6 of Part 1 for the state reported in positions 524-525. (13 positions)
539-553	State reporting number	Enter the primary state reporting number for the taxpayer assigned by the state unemployment agency. Left justify and blank fill as necessary. (15 positions)

Note: Positions 554-588 relate to the initial experience rate of the state reported in positions 524-525.

554-565	Taxable payroll as defined in state act	First entry Part 5, column 3.
566-569	Date an experience rate took effect	First entry Part 5, column 4, From-Date. If continued from previous year enter 0101. (Format is MMDD—Enter blanks if not present).
570-573	Date an experience rate was changed	First entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
574-578	State experience rate	First entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
579-588	Contributions actually paid to state	Enter part 5, column 9, first entry.

Note: Positions 589-623 relate to the second experience rate of the state reported in positions 524-525.

589-600	Taxable payroll as defined in state act	Second entry Part 5, column 3.
601-604	Date an experience rate took effect	Second entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present)
605-608	Date an experience rate was changed	Second entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
609-613	State experience rate	Second entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal
614-623	Contributions actually paid to state	Enter Part 5, column 9, second entry.

Note: Positions 624-658 relate to the third experience rate of the state reported in positions 524-525.

624-635	Taxable payroll as defined in state act	Third entry Part 5, column 3.
636-639	Date an experience rate took effect	Third entry Part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).

FORM 940 TAX DATA "B3" RECORD—Continued

Tape Position	Element Name	Entry or Description
640-643	Date an experience rate was changed	Third entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
644-648	State experience rate	Third entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
649-658	Contributions actually paid to state	Enter Part 5, column 9, third entry.

Note: Positions 659-693 relate to the fourth experience rate of the state reported in positions 524-525.

Tape Position	Element Name	Entry or Description
659-670	Taxable payroll as defined in state act	Fourth entry Part 5, column 3.
671-674	Date an experience rate took effect	Fourth entry part 5, column 4, From-Date. (Format is MMDD—Enter blanks if not present).
675-678	Date an experience rate was changed	Fourth entry Part 5, column 4, To-Date. If the rate is continued to the next calendar year enter 1231. (Format is MMDD—Enter blanks if not present).
679-683	State experience rate	Fourth entry Part 5, column 5. If no state experience rate is assessed by the state and only a flat fee is imposed enter zeroes. If present, express as a five position decimal.
684-693	Contributions actually paid to state	Enter part 5, column 9, fourth entry.

.10 Checkpoint Totals "C" Record

1. Write this record after each 100 or fewer Tax Data "B" Records whether "B1," "B2" or "B3". Each Checkpoint Totals "C" Record must contain a count of each type of Tax Data "B" Record and the sum of Total Taxes on all "B1" Records to this point.

2. The checkpoint totals "C" Record must be followed by a Tax Data "B" Record except as follows: If the Checkpoint totals "C" Record is at the end of the reel, it will be followed by an End of Reel "F" Record. If the Checkpoint Totals "C" Record is at the end of the file, it is followed by an End of file "E" Record.

3. All Checkpoint Totals "C" Records must be fixed length. All money amount fields will contain dollars and cents. The Checkpoint Totals "C" Records cannot be followed by a Tape mark.

FORM 940 AGENT "C" RECORD

Note: All amounts are to be entered right justified and zero filled. This record must follow each group of 100 Tax Data "B" Records or less.

Tape Position	Element name	Entry or Definition
1	Record Type	Enter "C".
2-7	Number of "B1"	Enter the sum of "B1" Records you are reporting since the last "C" Record.
8-13	Number of "B2" Records	Enter the sum of "B2" Records you are reporting since the last "C" Record.

FORM 940 AGENT "C" RECORD—Continued

Tape Position	Element Name	Entry or Definition
14-19	Number of "B3" Records	Enter the sum of "B3" Records you are reporting since the last "C" Record.
20-35	Total "B1" Record Taxes	Enter the sum of the taxes on all "B1" Records you are reporting since the last "C" Record.

.11 End of File "E" Record

1. Write this record after the last Checkpoint totals "C" Record.
2. All money amounts will contain dollars and cents.
3. All End of File "E" Records must be fixed length.
4. This record can be followed only be a tape mark or tape mark and trailer label on a reel.

FORM 940 AGENT "E" RECORD

Note: All amounts are to be entered right justified. This record type must be the last record on the arent's tape file.

Tape Position	Element Name	Entry or Definition
1	Record Type	Enter "E".
2-7	Number of "B1" Records	Enter the sum of "B1" Records you are reporting on the file.
8-13	Number of "B2" Records	Enter the sum of "B2" Records you are reporting on the file.
14-19	Number of "B3" Records	Enter the sum of "B3" Records you are reporting on the file.
20-35	Total "B1" Record Taxes	Enter the sum of the taxes on all "B1" Records on the file.

12 End of Reel "F" Record

1. Write this record when the end of the normal writing area of each reel has been reached, but all records in the file have not been written. This record indicates that there are additional records. Each End of Reel "F" Record must contain a count of each type of "B" Record and the sum of Total Taxes reported for all "B1" Records on that reel.

2. The End of Reel "F" Record cannot be followed by an Agent "A" Record, Tax Data "B" Record, Checkpoint Totals "C" Record or an End of File "E" Record. Only a tape mark or a tape mark and trailer label can follow this record.

3. Do not use this record on the final reel of the file being transmitted.

FORM 940 Agent "F" Record

Note: All amounts are to be entered right justified. This record must be present at the end of each tape reel in a multiple reel file, except the last tape reel which must contain an End of File "E" Record as its last record.

Tape Position	Element Name	Entry or Definition
1	Record Type	Enter "F".
2-7	Number of "B1" Records	Enter the sum of "B1" Records you are reporting on the reel.
8-13	Number of "B2" Records	Enter the sum of "B" Records you are reporting on the reel.
14-19	Number of "B3" Records	Enter the sum of "B3" Records you are reporting on the reel.
20-35	Total "B1" Record Taxes	Enter the sum of the taxes on all "B1" Records on the reel.

SEC. 12. Post Office States Codes

Enter the official two position Post Office State Code abbreviations for States and Territories in the Agent "A" Records and Tax Data "B" Records according to the following:

STATE	CODE
Alabama	AL
Alaska	AK
Arizona	AZ
Arkansas	AR
California	CA
Colorado	CO
Conneticut	CT
Delaware	DE
District of Columbia	DC
Florida	FL
Georgia	GA
Hawaii	HI
Idaho	ID
Illinois	IL
Indiana	IN
Iowa	IA
Kansas	KS
Kentucky	KY
Louisiana	LA
Maine	ME
Maryland	MD
Massachusetts	MA
Michigan	MI
Minnesota	MN
Mississippi	MS
Missouri	MO
Montana	MT
Nebraska	NE
Nevada	NV
New Hampshire	NH
New Jersey	NJ
New Mexico	NM
New York	NY
North Carolina	NC
North Dakota	ND
Ohio	OH
Oklahoma	OK
Oregon	OR
Pennsylvania	PA
Rhode Island	RI
South Carolina	SC
South Dakota	SD
Tennessee	TN
Texas	TX
Utah	UT
Vermont	VT
Virginia	VA
Washington	WA
West Virginia	WV
Wisconsin	WI
Wyoming	WY
Puerto Rico	PR
Virgin Islands	VI
Guam	GU

SEC. 13. EXEMPTION CODES

The following exemption codes are used in the two position fields in the "B1" and "B2" Records.

The following exemption codes are group level exemption codes. If an asterisk is present before the exemption code then a lower level subclassification is present on a later page. If the filing agent cannot provide the subclassification, the higher level classification is sufficient.

Exemption Code	Special classes of employment, special types of payments
01	Agricultural labor
02	Disabled worker's wages paid after year in which worker became entitled to disability benefits under the Social Security Act.
03	Domestic service in college clubs, fraternities and sororoties if employer paid cash wages less than $1000 in any calendar quarter in the current or preceding year.
04	Educational assistance program payments by employer under section 127 of the Code.
05	Employers whose taxibility depends upon number of employees and who meet the requirements set forth in Circular E.
06	Foreign Government and International Organizations.
07	Industrial homeworkers who are statutory employees.
08	Household workers (see Circular E for specifics).
09	Interns working in hospitals.
10	Ministers of churches performing duties as same.
11	Members of religious orders who have taken a vow of poverty and are instructed by the order to perform services for the order, agency of the supervising church or associated institution.
12	Members of religious orders who have not taken a vow of poverty and are instructed by the order to perform services for the order, agency of the supervising church or associated institution.
13	Reimbursement for moving expenses that may be deductible by employee.
14	Newspaper carrier under age 18 delivering to customers.
15	Newspapers and magazine vendors buying at fixed prices and retaining excess from sales to customers.
16	Non-cash payments for household work, agricultural labor and service not in the course of the employer's trade or business.
17	Patients employed by hospitals.

Exemption Code	Special classes of employment, special types of payments
18	Railroads, etc.—Payments subject to Railroad Retirement Tax Act and Railroad Unemployment Insurance Act.
19	Qualified real estate agents and direct sellers.
20	Service not in the course of the employer's trade or business other than on a farm operated for profit (cash payments only).
21	Standby employees (age 65 or over) doing no actual work in period for which paid.
22	Employees of State governments and political subdivisions.
23	Supplemental unemployment compensation plans.
24	Tips over $20 a month (See Circular E for details).
25	Tips less than $20 a month.
*30	Aliens.
*35	Family employees.
*40	Federal employees.
*45	Fishing and related activities.
*50	Foreign service by U.S. citizens.
*55	Insurance agents or soliciters.
*60	Meals and lodging (see Circular E).
*65	Non-profit organizations.
*70	Retirement and pension plans.
*75	Sickness or injury payments.
*80	Students.
	Subdivisions for Aliens classification
31	Resident aliens performing service outside the U.S. and meeting the requirements set down in Circular E.
32	Canadian and Mexican non-resident aliens working in the U.S. who are employed in railroad service.
33	Non-resident alien who is a student, scholar, trainee, teacher, etc. who meets the requirements of a non-immigrant alien under section 101(a)(15)(f) or (j) of Immigration and Naturalization Act.
34	Non-resident alien working on American vessel or aircraft outside U.S. (See Circular E for details).
	Subdivisions for Family Employees classification
36	Son or daughter under 21 employed by parent (or by partnership consisting only of parents); wife employed by husband or husband employed by wife.
37	Parent employed by son or daughter.
	Subdivisions for Federal Employees classifcation
41	Members of uniformed services; Young Adult Conversations Corps, Job Corps, or National Volunteer Antipoverty Program or Peace Corps Volunteers.
42	All others (See Circular E).
	Subdivisions for Fishing and related activities classification
46	First, sponges, etc. other than salmon or halibut on vessels of less than 10 tons.
47	Individual has arrangement with the owner of a boat and is not paid in cash, but receives a share of the catch. This is not applicable to salmon or halibut activities or on vessels greater than 10 tons, or where the operating crew is normally more than 9 persons.
	Subdivisions for Foreign Service classification
51	U.S. Government employee.
52	Employees of foreign subsidiaries of domestic corporations and other private employers.

Exemption Code	Special classes of employment, special types of payments
	Subdivisions for insurance agents or solicitors classification
56	Full-time life insurance salesperson who is not a common law employee and paid soley by commissions.
57	Other salesperson of life, casualty, etc. insurance who is not a common law employee and paid solely by commissions.
	Subdivisions for Meals and Lodging classification
61	Meals furnished for employer's convenience and on the employer's premises.
62	Lodging furnished for employer's convenience and on the employer's premises.
	Subdivisions for non-profit organization classification
66	Religious, educational, charitable, etc. organizations described in section 501(c)(3) of the Code and exempt from income tax under section 501(a).
67	Corporations organized under Act of Congress described in section 501(c)(1) of the Code (See Circular E).
68	Other organizations exempt under section 501(a) of the Code. (See Circular E).
	Subdivisions for retirement and pension plans classification
71	Employer contributions to a simplified employee plan, individual retirement arrangement (SEP-IRA).
72	Employer contributions to section 403(b) of the Code annuity contracts.
73	Retirement and pension plans.
	Subdivisions for sickness or injury payments classification
76	Workmen's compensation law or insurance contract payments.
77	Certain employer plans payments.
78	No employer plans at end of 6 calendar months after calendar month employee last worked for employer.
	Subdivisions for Students classification
81	Student working for private school or university, if enrolled and regularly attending classes.
82	Student performing services for auxiliary nonprofit organization described in section 509(a)(3) of the Code which is organized and operated exclusively for the benefit of and supervised or controlled by a school, college or university at which the student is enrolled and regularly attending classes.
83	Student working for a public school, college or university, if enrolled and regularly attending classes, and student nurse working for a public hospital.
84	Spouse of student provided the conditions set forth in Circular E are met.
85	Student enrolled in a full time program at a nonprofit or public institution. Student service must be taken for credit at the institution and combine academic instruction with work experience. It must be an integral part of the program and the institution must have so certified to the employer. See Circular E for more information.
86	Student nurse working for hospital.

SEC. 14. EFFECTIVE DATE

This revenue procedure is effective January 1, 1986.

Exhibit 1
Agent's Listing

NAME ______________

ADDRESS ______________

ADDRESS ______________

TYPE OF TAX ______________

Employer Identification Number	Name Control	T/P Name & Address	District Office Code	File At Service Center

Note: District Office Code and Filing Service Center are filled in by the Service.

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26 CFR 601.602: Forms and instructions.
(Also Part I, Sections 3504, 6011; 31.3504-1, 31.6011(a)-1.)

Rev. Proc. 86-27

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to provide a means whereby reporting agents preparing Form 941, Employer's Quarterly Federal Tax Return, and Form 941E, Quarterly Return of Withheld Federal Income Tax, for groups of taxpayers can furnish the required information in the form of magnetic tape instead of paper documents.

.02 This revenue procedure reflects the current changes to the tape specifications.

.03 This revenue procedure supersedes Rev. Proc. 84-11, 1984-1 C.B. 414. If a current reporting agent is unable to comply with the changes in specification, he/she should contact the local Magnetic Tape Coordinator for Business Tax Returns for further instructions.

SEC. 2. APPLICATION FOR TAPE REPORTING

.01 Agents who desire to file authorized federal tax returns on magnetic tape must first file a letter of application or submit Form 4995, Application for Magnetic Tape Filing of Federal Business Tax Returns (previously known as Application for Magnetic Tape Filing of Form 941, Employer's Quarterly Federal Tax Return). A separate application must be submitted for each type of tax return filed (e.g. 941, 941E, 940). The letter of application should be addressed to the Director, Internal Revenue Service Center, Attention: Magentic Tape Coordinator for Business Tax Returns, of the service center that serves the primary business address of the reporting agent. Addresses of the Internal Revenue Service Centers are shown in Section 11 of this revenue procedure. The letter of application must contain the following:

1. Name, address and EIN (Employer Identification Number) of the person, organization, or firm making the application.
2. Name, title, and telephone number of the person to contact regarding the application.
3. Type and nature of equipment to be used to prepare the tape file, i.e., manufacturer and model of main frame and tape drives, tape width, density (characters per inch), and recording mode (e.g. Excess 3, Octal, etc.).
4. List of the taxpayers to be included on the initial establishment of the Magnetic Tape Filing system. The list must be in triplicate with the data shown in the exact order as Exhibit 1. Show each taxpayer's name, complete address (including Zip Code), and EIN: sort into EIN sequence. See Section 6.03 for additional details.
5. Service center where paper tax returns were last filed.
6. Signature of the agent or agent's employee authorized to prepare federal tax returns for taxpayers.
7. An agreement by the reporting agent to keep copies of the Powers of Attorney (POA) on file at the agent's principal place of business for examination by the Service upon request. Such copies must be retained until the statute of limitations for the last return filed under its authority expires.
8. An agreement to fully pay the tax by Federal Tax Deposits (FTDs).

NOTE: This revenue procedure does not restrict a non-financial organization who performs a payroll or tax service from being a reporting agent. See Rev. Proc. 80-31, 1980-2 C.B. 760, concerning the requirements under which FTDs can be made by the reporting agent.

9. The first tax period for which the agent plans to file returns on magnetic tape.
10. The estimated volume of returns the agent plans to file by type of return (e.g. 941, 941E or 940).

SEC. 3. POWER OF ATTORNEY

.01 A POA must be submitted for each filer on the list attached to Form 4995 or the letter of application. The POA must be submitted for each filer on the list attached to Form 4995 or the letter of application. The POA may be submitted on Form 2848, Power of Attorney and Declaration of Representative, which is available on request; or any other instrument which clearly states that the reporting agent is granted the authority to file and sign the return. The POA filed under this revenue procedure is not subject to the rules contained in the Conference and Practice Requirements (Treasury Regulation 601.502). The POA may cover the filing of both Forms 940 and 941 if desired.

.02 Both the taxpayer, or his authorized representative, and the reporting agent must sign the POA. The signed document will remain in effect until such time as it is revoked by the taxpayer, terminated by written notification from the reporting agent, or expires under its own terms.

1. The following persons may execute a POA on behalf of a corporation or other business taxpayer:

(a) The individual, if the person required to make the return is an individual;

(b) The president, vice president, or other principal officer, if the person required to make the return is a corporation;

(c) A responsible and duly authorized member or officer having knowledge of its affairs, if the person required to make the return is a partnership or other unincorporated organization;

(d) The fiduciary, if the person required to make the return is a trust or estate; or

(e) An agent who is duly authorized in accordance with section 31.6011(a)-7 of the Employment Tax Regulations.

.03 The scope of the POA for magnetic tape filing will be governed according to the following:

1. The POA will delegate to the reporting agent the power to sign and file appropriate federal tax returns.

2. The POA becomes effective for the tax period the agent notifies the service that the employer or filer is being added to the Magnetic Tape Filing system and remains in effect for subsequent periods until revoked, terminated or expired.

3. The POA is automatically revoked when the reporting agent notifies the Service that a taxpayer is no longer included in the Magnetic Tape Filing system.

4. The receipt of a POA for magnetic tape filing has no effect on prior POA on file for other purposes for a given taxpayer.

5. The POA for magnetic tape filing will be a limited POA, i.e., notices, refunds and other output resulting from filing on magnetic tape will be mailed to the taxpayer.

6. Requests from a reporting agent for information or adjustments or an account for which the taxpayer has authorized magnetic tape filing will be honored by the service center.

7. Requests for address changes may not be made by the reporting agent. Requests for address changes for taxpayers that are reported under magnetic tape filing will be processed only if they originate with one of the following:

(a) The taxpayer,

(b) An employee of the Service, or

(c) An attorney-in-fact if the attorney has a full POA for all tax matters concerning a taxpayer, and has filed a copy of the POA with the Service.

SEC. 4. APPROVAL OF AGENTS APPLICATION

.01 The Service will act on applications and notify applicants of authorization or disapproval within 30 days of receipt of Form 4995 or a letter of application as defined in Section 2.

.02 Generally, reporting agents using equipment compatible with the Service's can presume that tape filing will be approved. Compatible tape characteristics are shown in Section 13. If the reporting agent has the capability to prepare several types of tapes, the Service prefers that compatible tapes be prepared.

.03 If the reporting agents propose to submit convertible tapes, i.e., tapes requiring translation, the Service will either translate these tapes or provide translation through other government agencies. Magnetic tape filing will be disapproved when the Service is unable to obtain facilities to translate a reporting agent's file to a compatible form. (See Sections 12 and 13 for specifications.)

.04 Once authorization to file tax data on magnetic tape has been granted to a reporting agent, such approval will continue to effect in succeeding tax periods as long as the requirements of this revenue procedure are met, and there are no equipment changes by the reporting agent. However, new applications are required if users change from compatible tapes to equipment producing tapes that require translation, or if they discontinue magnetic tape filing for one or more periods, then decide to resume this method of reporting.

SEC. 5. EFFECT ON PAPER DOCUMENTS

.01 Authorization to file on magnetic tape does not prohibit the filing of paper tax returns, but merely permits filing on such returns through the Magnetic Tape Filing system. If for some reason (e.g. late receipt of records), an agent prefers to file a paper return for a given taxpayer, the agent may do so even after having been given authorization to file that taxpayer's return on magnetic tape.

.02 The initial filing of tax returns on magnetic tape will be on a trial basis. Each taxpayer included on the magnetic tape must also be on the paper form until authorized by the Service to discontinue filing returns on paper. The paper returns must be arranged in the same period as the returns reported on the magnetic tape and filed at the same location and in the same shipment. In general, the Service will be able to notify the reporting agent to discontinue filing paper returns within one quarter after the initial filing of magnetic tape. The notification will depend upon the feasibility of processing the magnetic tape submitted.

.03 Paper and magnetic tape returns for the same tax period at the same time must never be filed by a reporting agent for a taxpayer unless the returns are filed during the trial period for the reporting agent described in section 5.02.

.04 Form 941/941E filers are required to transmit with their return, copies of any W-4's claiming 14 or more exemptions. If the reporting agent files magnetic tape 941/941E for a taxpayer, but does not report W-4 information or magnetic tape, the paper W-4's should be submitted to the service center with a cover letter.

SEC. 6. FILING TAPE RETURNS

.01 Packaging, shipping, and mailing instructions will be provided in the letter granting initial approval issued by the Service in response to the letter of application for magnetic tape filing.

.02 The Service will allow a tape return to be submitted for those individually approved magnetic tape filers until the reporting agent formally notifies IRS that specific employers are being deleted from their current magnetic tape filing inventory.

.03 Section 6091(b) of the Internal Revenue Code requires that tax returns be filed at the Internal Revenue District (or service center serving that district) that services the legal residence or principal business address of the taxpayer. Thus, reporting agents must normally file taxpayer's returns at the appropriate service center as described above even if it means submitting magnetic tapes to more than one service center. This rule may not be violated unless a reporting agent has applied for and received permission from the Service to do so. Contact your Magnetic Tape Coordinator for Business Tax Returns for details.

.04 Approval by the Service of Form 4995 or a letter of application allows a reporting agent to file at any service center that services his/her clients. If a reporting agent wishes to file at additional service centers, he/she should notify the Magnetic Tape Coordinator for Business Tax Returns of the service center where he/she originally applied at least 90 days prior to the initial transmittal to the new service center.

.05 The reporting agent will be provided with a validated copy of the agent's listing for taxpayers authorized to file on magnetic tape. This authorization will contain each taxpayer's EIN, four position alpha Name Control, and the DO (District Office) Code. This authorizaiton will be the source of the EIN and Name Control to be used in magnetic tape by the reporting agent as an identification of each taxpayer.

It is imperative that this Name Control be retained in the agent's records and be used in each taxpayer's Tax Data "B" Record (positions 72-75). It is used by the Service to ensure the correct recording of the taxpayer's return. Failure to use the correct Name Control can result in delays in processing the return and notices of delinquent filing being sent to the taxpayer.

.06 Enclose in the first box of the tape shipment to the service center the following:

1. Form 4996, Magnetic Tape Filing Transmittal for Federal Business Returns (previously known as Magnetic Tape Filing Transmittal for Form 941, Employer's Quarterly Federal Tax Return) or a letter of transmittal containing the information described below. File the Form 4996 or the letter of transmittal in duplicate.

2. The letter of transmittal should include:

a. Name and address of reporting agent

b. Type of tax return filed on the magnetic tape

c. Tax period

d. Number of tax returns filed on accompanying tape

e. Total taxes reported

f. Total taxes deposited

g. Service center in which the POA for filing returns on magnetic tape is located.

h. Total forms 941c and other attachments to support adjustments included in this shipment.

i. Signature of transmitter, title and date.

3. A control listing identifying actual taxpayers previously approved by the Service for magnetic tape filing that are contained on the current tape file being submitted. List the taxpayers in EIN sequence with each taxpayer's name and address.

4. The reporting agent should notify the Magnetic Tape Coordinator for Business Tax Returns if the agent does not receive notification of the receipt of the transmittal within 15 days from the date he/she sent the transmittal.

SEC. 7. ADDING AND DELETING FILERS FROM MAGNETIC TAPE FILING SYSTEM

.01. When adding or deleting filers, the Service must receive (in tripliate and in the same format as shown on Exhibit 1) a listing which contains the complete names, addresses and EIN's of the taxpayers the reporting agent wants added or deleted from the Magnetic Tape Filing system. the word "ADDITIONS" or "DELETIONS" should be entered after the title, "Agent's Listing," and the effective date.

.02 The Service will provide a validated copy of the updated agent's listing to the reporting agent. Under no circumstances is a new filer to be included on the Magnetic Tape Filing system until the validated copy is received from the Service.

.03 A POA authorization must be included for each taxpayer to be added to the Magnetic Tape Filing system.

.04 The reporting agent should indicate on the last magnetic tape return submitted for a filer that it is either the "Final Return" or a "Discontinued Filer" in the Tax Data "B" Record.

.05 The reporting agent may not always know that the final magnetic tape return for a particular taxpayer is being submitted at the time the tape is being sent in. When the reporting agent determines that the previous tape contained the last return to be prepared for the individual filer, action should be taken to notify the service center which authorized the magnetic tape filing of one of the following conditions:

1. The taxpayer is out of business (state the effective date) and will no longer be liable for filing returns (Final Return), or

2. The reporting agent will no longer be submitting returns on magnetic tape for the taxpayer who is still in business and is still liable for such returns (Discontinued Filer).

.06 Lists of proposed quarterly (Form 941/941E) filer additions, deletions, etc., must be received in the service center prior to the end of the second month of a quarter. This will permit the Service to properly validate applications and to respond to the agent within 30 days of receipt of the lists. However, at the time of filing, if the agent has not received a validated listing with the additions, he/she should not file a magnetic tape return for those taxpayers because he/she does not have the valid Name Control.

SEC. 8. DUE DATES

.01 The due dates prescribed for filing paper returns with the Service will also apply to magnetic tape filing of Federal business tax returns.

.02 In no case should returns with more than one date be included on one tape file.

SEC. 9. ADJUSTMENTS TO 941 AND 941E RETURNS

.01 Adjustments may be made on returns submitted on magnetic tape.

.02 Positions 329-338 of Tax Data "B" Record are used to report adjustment of social security (FICA) taxes reported. These positions must be used in conjunction with the FICA Adjustment Indicator (position 155) of the Tax Data "B" Record. If there is no adjustment of FICA taxes, the adjustment indicator should be zero. If there is an adjustment of FICA taxes, the adjustment indicator must be set to 1, 2, 3 or 4 depending on the circumstances explained as follows:

The FICA Adjustment Indicator should be set to 1 if the adjustment to FICA taxes consists only of the difference between the total social security taxes (positions 318-327) of the Tax Data "B" Record and the amount actually collected from your employees wages consists only of fractions of cents added or dropped due to rounding.

The FICA Adjustment Indicator should be set to 3 if the Adjustment To FICA Taxes consists only of total uncollected employee social security tax on tips (i.e. employee previously reached maximum limitation through combination of wages and tips).

The FICA Adjustment Indicator should be set to 4 if the Adjustment To FICA Taxes consists only of FICA tax on third-party sick pay for which the employer is not responsible.

If the description for the adjustment to FICA taxes listed above is not applicable or the adjustment to FICA taxes is significant for more than one reason, the FICA Adjustment Indicator should be set to 2, and a statement or Form 941c should be submitted with the tape identifying the taxpayer and explaining the adjustment to FICA tax. If the second reason for a FICA adjustment is "FRACTIONS ONLY," then it may be ignored and either "FICA TIP" or "sick pay" values may be used.

Note: A FICA tax adjustment is valid only on the Form 941 and is not valid on Form 941E.

.03 Adjustments to proceding quarters (income tax withholding adjustments) should be reported in positions 201-210 of the Tax Data "B" Record. Any magnetic tape return with a significant adjustment to preceding quarters should be supported by a statement submitted with the magnetic tape. The statement should identify the taxpayer and explain the adjustment. The Adjustment Indicator for Income Tax Withheld (position 156 of the Tax Data "B" Record) should be set to "1" if there is an adjustment or be set to zero if there is no adjustment.

.04 Adjustments to backup withholding should be reported in positions 356-374 of the Tax Data "B" Record. Any magnetic tape return with a significant adjustment to backup withholding should be supported by a statement submitted with the magnetic tape. The statement should identify the taxpayer and explain the adjustment. The Adjustment Indicator for Backup Withholding (position 157 of the Tax Data "B" Record) should be set to "1" if there is an adjustment or be set to zero if there is no adjustment.

.05 Include all statements and forms 941c with the magnetic tape shipment for approval and subsequent adjustment action.

SEC. 10. FILING FORMS W-2 (COPY A) WITH THE SOCIAL SECURITY ADMINISTRATION

The reporting agents who file Forms 941 on magnetic tape for employers must file the wage information directly with the Social Security Administration on tape or paper documents. For directions for tape filing, you may call or write the appropriate Service Center Magnetic Tape Coordinator for Business Tax Returns, or any Social Security Administration office and ask for Technical Information Bulletin 4a (TIB-4a), or you can write to the following address:

Social Security Administration
Bureau of Data Processing
P.O. Box 2317
Baltimore, MD 21203

SEC. 11. ADDITIONAL INFORMATION

Requests for additional copies of this revenue procedure, applications for magnetic tape filing, requests for copies of appropriate input record element specifications, and requests for tape filing information should be addressed to the Director, Internal Revenue Service Center, Attention: Magnetic Tape Coordinator for Business Tax Returns, at one of the following addresses:

1. North-Atlantic Region
   (a) Andover Service Center
   Project 105 Coordinator (Stop 481)
   310 Lowell Street
   Andover, MA 05501
   (b) Brookhaven Service Center
   Project 105 Coordinator (Stop 110)
   1040 Waverly Avenue
   Holtsville, NY 11742
2. Mid-Atlantic Region
   (a) Philadelphia Service Center
   Project 105 Coordinator (Drop Point 433)
   P.O. Box 245
   Bensalem, PA 19020
3. Central Region
   (a) Cincinnati Service Center
   Project 105 Coordinator
   (CSA:C Stop 43)
   P.O. Box 267
   Covington, KY 41019
4. Southeast Region
   (a) Atlanta Service Center
   Project 105 Coordinator
   P.O. Box 47-421
   Doraville, GA 30362
   (b) Memphis Service Center
   Project 105 Coordinator
   P.O. Box 30309
   Airport Mail Facility
   Memphis, TN 38130
5. Midwest Region
   (a) Kansas City Service Center
   P.O. Box 24551
   Kansas City, MO 64131
6. Southwest Region
   (a) Austin Service Center
   Management Support Branch
   (Stop 1055)
   P.O. Box 934
   Austin, TX 78767
7. Western Region
   (a) Ogden Service Center
   1160 West 1200 South
   Ogden, UT 84201
   (b) Fresno Service Center
   P.O. Box 12866
   Fresno, CA 93779

SEC. 12. CONVENTIONS AND DEFINITIONS

.01 Conventions

Certain conventions may be required by the programming system or equipment used by the reporting agent, with respect to header and trailer labels, record and tape marks. If present, the Service prefers that they adhere to American National Standards Institute (ANSI) X3.27 specifications. The Service will accept other specifications if the facilities to accommodate them can be found. The Service reserves the right to reject tapes with other than ANSI X3.27 specifications. The tapes must adhere to the following at a minimum:

(a) Label

(1) The first record on a reel only.

(2) In accordance with ANSI X3.27, Volume Header Label

(VOL1), First File Header Label (HDR1) and Second File Header Label (HDR2) are strongly preferred.

(b) Trailer Label

(1) The last record on a reel only.

(2) No restrictions apply as to number of characters or type of characters used.

(c) Record Mark

(1) No restrictions apply to record marks.

(d) Tape Mark

The tape mark should only follow an End of Reel "F" Record or an End of File "E" Record.

.02 Definitions

Element	Description
Reporting Agent	Person or organization preparing and filing magntic tape equivalents of Federal tax returns.
Taxpayer	Persons or organizations liable for the payment of tax. The taxpayer will be held responsible for the completeness, accuracy and timely submission of the magnetic tape files.
b	Denotes a blank position.
EIN	Employer Identification Number.
Record	A group of related fields of information, treated as a unit.
Blocked Records	Two or more records grouped together between interrecord gaps.
Blocking Factors	The number of records grouped together to form a block.
Unblocked Records	Single records written between interrecord gaps.
File	A file consists of all tape records submitted by a reporting agent.
Record Mark	Special character used either to limit the number of characters in data transfer or to separate blocked records on tape.
Tape Mark	Special character that is written on tape.
Special Character	Any character that is not a numeral, letter, or blank.
Reel	A spool of magnetic tape.
FTD	Federal Tax Deposit.
POA	Power of Attorney.

SEC. 13. MAGNETIC TAPE SPECIFICATIONS

.01 These specifications prescribe the required format and content of the records to be included in the file, but not the methods or equipment to be used in their preparation. A compatible tape file must conform to all of the following:

Type of tape	½ inch Mylar base, oxide coated
Recording density	800, 1600, or 6250 CPI (characters per inch)
Parity	Even or odd
Interrecord Gap	¾ inch
Recording Mode	7 channel binary coded decimal (BCD), 9 channel, EBCDIC, ASCII

.02 An acceptable file will contain, for each reporting agent, the following:

1. An Agent "A" Record,
2. A series of Tax Data "B" Records,
3. A series of Checkpoint "C" Records, and
4. An End of File "E" Record,
5. Multiple reel files will have an End of Reel "F" Record.

.03 All records including headers and trailers, if used, must be written at the same density.

.04 Affix an external label to each tape with the following information:

1. Name of reporting agent,
2. Number of tax returns submitted on this reel of tape,
3. Payment period in YYMM (Year, Year, month, month) format, for example 8109,
4. Density (800, 1600, 6250),
5. Channel (7 or 9),
6. Parity (odd or even),
7. Name of computer manufacturer,
8. Computer type (manufacturer's designation),
9. Tape Drive (manufacturer and type),
10. Sequence number of reel and total number of reels in file (for example, 1 of 3).

.05 Since the Service is not restricting magnetic tape filing or reporting agents with specific types of equipment, or prescribing the methods used to prepare the tape files, the Agent "A" Record, End of Reel "F" Record and End of File "E" Record perform the functions normally assigned to header and trailer labels and related conventions. The Agent "A" Records are written on the file for a given location of the reporting agent, the End of Reel "F" Record signals that no more Tax Data "B" Records are written on the reel, and the End of File "E" Record indicates that there is no further data to be processed.

.06 Record Length

1. The tape records prescribed in the specifications may be blocked or un-

blocked subject to the following:

(a) A block may not exceed 12,100 tape positions.

(b) If the use of blocked records would result in a short block at the end of a Tax Data "B" Record and the next record is too large to include in the block, the remaining positions of the block should be filled with 9's or spaces. No other digits or characters other than 9's or spaces are specified or acceptable for filling (or padding) any tape input data blocks.

(c) Two forms of blocking are acceptable:

(1) Only Tax Data "B" Records are blocked; all other records are unblocked.

(2) All records, except header and trailer labels, if used, are blocked. In this case, if employers from more than one location are reported on the same tape, the Agent "A" Record cannot be in the middle of a block, but must be the first record in a block.

.07 Data

1. Only character data may be used. This means numeric fields cannot use overpunched signs and should be right justified and zero filled. Special characters should be limited to =, &, % or / and can only be used in the name line fields and the street address fields of Agent "A" Record and Tax Data "B" Record. Otherwise, characters must be numeric or alphabetic.

.08 Agent "A" Record

1. Identifies the reporting agent who prepares and transmits the tape file. When multiple reels are required for a single file, the Agent "A" Record must be repeated at the first record (second record if header labels are used) on every succeeding reel in the file, and the reel number must be incremented by 1 for each tape reel after the first reel. A reporting agent may include Tax Data "B" Records prepared at more than one location, on the same tape, but they must have the same DO Code; however, Tax Data "B" Records prepared at different locations with different DO Codes must be on separate files and preceded by an Agent "A" Record. Contact the Magnetic Tape Coordinator for Business Tax Returns for additional details if necessary.

AGENT "A" RECORD

Tape Position	Element Name	Agent Data Record Entry or Definition
1	Record Type	Enter "A". Must be first character of each Agent "A" Record.
2-3	DO Code	Enter two numeric digit District Office Code furnished by IRS.
4-5	Tax Period	Enter YQ (Year, Qtr.). For example: tax period "14" represents the year 1981 and the fourth quarter of the year.
6-7	Reel Number	Serial number assigned by the reporting agent to each reel, starting with 01. If header labels are used, this should be the same as Reel Sequence Number.
8-16	EIN—Reporting Agent	Enter the 9 numeric characters of the reporting agent's EIN. DO NOT include the hyphen.
17-20	Type of Return	Enter "941b" or "941E" is appropriate. "b" means blank.
21-23	Record Length—Agent "A" Record	Enter number of positions (178) for Agent "A" Record. If a Record mark is used at the end of each record, include it in the count. DO NOT include in count if used only at the end of the block.
24-27	Record Length "B" Record	Enter number of positions (964) for "B" Record. If a record mark is used at the end of each record, include it in the count. DO NOT include in count if used only at the end of the block.
28-67	1st Name Line Reporting Agent	Enter first name line of reporting agent. Left justify and fill with blanks.
68-107	2nd Name Line Reporting Agent	Enter second name line of reporting agent. Left justify and fill with blanks. Fill with blanks if not required.
108-147	Street Address—Reporting Agent	Enter street address of reporting agent. Left justify and fill with blanks. Fill with blanks if street not required.
148-167	City—Reporting Agent	Enter city of reporting agent. Left justify and fill with blanks.

AGENT "A" RECORD—Continued

Tape Position	Element Name	Entry or Description
168-169	State—Reporting Agent	Enter the official Post Office two position state code. See Section 14 for a list of the state code abbreviations.
170-178	Zip Code Reporting Agent	Enter Zip Code of reporting agent. Left justify, and blank fill.

.09 Form 941/941E Tax Data "B" Record

1. Contains tax information reported by the reporting agent. The number of Tax Data "B" Records appearing on one tape reel will depend on the number of taxpayers represented (only one tax return for each EIN).

2. Tax Data "B" Records may be blocked together with Record Types A, C, E, and F unblocked. Records should have a blocking factor for which blocks will not exceed 12,100 tape positions. All records must be fixed length and for the current tax period. All money amount fields must contain dollars and cents, must be right justified with zero filling on left and must be zero filled if non-significant. Fields identified as indicators or signs should always carry a value. Other non-money fields must be left justified and blank filled on right with blank filling of non-significant fields.

TAX DATA "B" RECORD

Tape Position	Element Name	Entry or Definition
1	Record Type	Enter "B". Must be first character of each Form 941/941E Tax Data "B" Record.
2-36	Employer's name first line	Enter 1st name line of taxpayer. Left justify and fill with blanks. First five positions must be filled.
37-71	Employer's name second line	Enter 2nd name line of taxpayer. Left justify and fill with blanks.
72-75	Name Control	Enter the 4 position alpha/numeric name control from the validated Agent's Listing. Blanks may be present in the low order position(s).
76-84	EIN of employer	Enter the 9 numeric characters of the EIN. Do not enter a hyphen. blanks are not acceptable.
85-119	Street address	Enter the street address of the taxpayer. Left justify and blank fill.
120-139	City of employer	Enter the city in which the taxpayer is located. Left justify and fill with blanks. First three positions must be filled.
140-141	State of employer	Enter the official Post Office two position state code. See Section 14.
142-150	Zip Code of employer	Enter the nine (9) position Zip Code if applicable. If not, enter the five (5) position Zip Code left justified and leave the last four positions blank.
151	Address Change-Indicator	Enter zero if taxpayer's address has not changed since previous filing of Form 941/941E return; otherwise enter "1".
152	New Account Indicator	Enter zero if reporting agent has reported the taxpayer on magnetic tape in the prior quarter. Enter "1" if this is the first consecutive quarter the reporting agent is reporting the taxpayer on magnetic tape. (If the taxpayer has been reported on magnetic tape, is discontinued from tape filing for one or more quarters, and this is the first quarter the taxpayer is again being reported under the Magnetic Tape Filing system, enter "1" for a new account.)

TAX DATA "B" RECORD—Continued

Tape Position	Element Name	Entry or Description
153	Final Return Indicator	Enter zero if this is not taxpayer's final return. Enter "1" if this is the taxpayer's final return.
154	Discounted Mag Tape Filer Indicator	Enter zero if reporting agent will be reporting for the taxpayer in the subsequent quarter on magnetic tape. Enter "1" if the taxpayer is being removed from the Magnetic Tape Filing system.
155	Adjustment Indicator FICA	Enter Zero if no adjustments. Enter "3" if "FICA Tip" only (Employee previously reached maximum limitation thru combination of wages and tips). Enter "4" if adjustment only for "third party" sick pay for which the employer is not responsible. Enter "2" for any other FICA adjustments including combinations of "3" and "4". ALL ADMUSTMENTS OF "2" CATEGORY MUST BE SUPPORTED BY PAPER DOCUMENTATION SENT IN WITH MAGNETIC TAPE TRANSMITTAL. Enter "1" if "Fractions Only" (i.e. FICA tax adjustment is only the result of rounding differences between tax collected from employees and Social Security Tax on wages). If FICA tax adjustment is a combination of "1" and "3" or a combination of "1" and "4" reasons, reason "1" (Fractions only) may be ignored and a value of "3" or "4" can be used as appropriate. For Form 941E this field must contain zero.
156	Adjustment Indicator Income Tax Withheld	Enter zero if there is no adjustment. Enter "1" if there is an adjustment
157	Adjustment Indicator Backup Withholding	Enter zero if there is no adjustment. Enter "1" if there is an adjustment.
158-164	Total Number of Employees	Enter the total of employees in pay period that includes March 12. Do not include household employees. Applicable to first quarter only. Otherwise fill with zeros.
165-173	Parent Corporation EIN	Enter the parent corporation EIN if applicable. If not, then enter all spaces.
174-185	Total Wages and Tips	Total wages and tips subject to withholding, plus other compensation.
186-199	Amount of Income Tax Withheld	Total income tax withheld from wages, tips, pensions, annuities, sick pay and gambling.
200	Sign for Adjustment to preceding quarters	Enter "1" if there is a positive adjustment to withholding. Enter zero if there is a negative adjustments. Enter "1" if there is no adjustment.
201-210	Admustment for preceding quarters	Enter zeroes if there is no adjustment. If there is a significant amount, right justify and zero fill.
211	Sign for Adjusted Total Tax Withheld	Enter "1" if there is a positive adjustment to withholding. Enter "1" if there is no adjustment. Enter "1" if there is no significant amount in the Adjusted Total of Income Tax Withheld field.

TAX DATA "B" RECORD—Continued

Tape Position	Element Name	Entry or Description
212-225	Adjusted Total Income Tax Withheld	Enter zeros if there is no significant amount. If there is a significant amount, right justify and zero fill. This field is the result of the addition of the Amount of Income Tax Withheld field and the Adjustment for preceding quarters field.
226-239	Taxable FICA Wages Paid	Wages paid to employees—not taxes. For Form 941E this field must contain zeroes.
240-252	Taxable FICA Wages Paid	Tax paid on Taxable FICA Wages paid to employees. For Form 941E this field must contain all zeroes.
253-262	Taxable Tips Reported	Tips reported by employees—not taxes. For Form 941E this field must contain all zeroes.
263-271	Tax on Taxable Tips Reported	Tax on tips reported in positions 253-262. For Form 941E this field must contain all zeroes.
272-281	Tips Deemed Wages	Amount reported by employer as difference between minimum wage and the actual amount paid. For Form 941E this field must contain all zeroes. NOTE: This field applies to those employees who are subject to the Minimum Wage provisions of the Fair Labor Standard Act.
282-290	Tax on Tips Deemed Wages	Tax on tips reported in position 272-281. For Form 941E this field must contain all zeroes. NOTE: This field applies to those employees who are subject to the Minimum Wage provisions of the Fair Labor Standard Act.
291-304	Taxable hospital insurance benefits wages paid	Amount reported by federal, state and local governmental employers as wages (other than those electing full social security for employees under a section 218 agreement).
305-317	Tax on hospital insurance benefits wages paid	Tax on amount reported in positions 291-304.
318-327	Total FICA Taxes	Total social security taxes. For Form 941E this field must contain all zeroes. This field is a result of the addition of the fields known as Tax on FICA Wages, Tax on Taxable Tips Reported and Tax on Tips Deemed Wages.
328	Sign for Adjustment to FICA Tax	Enter "1" if the adjustment to FICA is positive. Enter zero if Adjustment to FICA is negative. Enter "1" if there is no Adjustment to FICA.
329-338	Adjustment to FICA Tax	Enter zeroes if there is no significant amount. Enter right justified and zero filled if significant. For Form 941E this field represents Adjustment to Tax on hospital insurance benefits wages.
339	Sign for Adjusted Total of FICA Tax	Enter "1" if the Adjusted Total of FICA taxes is positive. Enter zero if the Adjusted Total of FICA taxes is negative. Enter "1" if there is no significant amount in the Adjusted Total of FICA Taxes.
340-349	Adjusted Total of FICA Taxes	Enter zeroes if there is no significant amount. Enter right justified and zero filled if significant. This field is the result of the addition of Total FICA Taxes and the Adjustment to FICA Tax.

TAX DATA "B" RECORD—Continued

Tape Position	Element Name	Entry or Description
350-363	Backup Withholding	Enter zeroes if there is no significant amount. Enter right justified and zero filled if significant.
364	Sign for Adjustment to Backup Withholding	Enter "1" if there is a positive Adjustment to Backup Withholding. Enter zero if there is a negative Adjustment to Backup Withholding. Enter "1" if there is no Adjustment to Backup Withholding.
365-374	Adjustment to Backup Withholding	Enter zeroes if there is no significant amount. Enter right justified and zero filled if significant.
375	Sign for Adjusted Total Backup Withholding	Enter "1" if there is a positive Adjusted Total of Backup Withholding. Enter zero if there is a negative Adjusted Total of Backup Withholding. Enter "1" if there is no Adjusted Total to Backup Withholding.
376-385	Adjusted Total of Backup Withholding	Enter zeroes if there is no significant amount. Enter right justified and zero filled if significant.
386-400	Total Taxes	Enter zeroes if there is no significant amount. Enter right justified and zero filled if significant. Total Taxes is the result of the addition of the fields known as Adjusted Total Tax Withheld, Adjusted Total FICA Taxes, and Adjusted Total of Backup Withholding.
401-410	Advanced Earned Income Credit	Advanced payment of EIC during the quarter. Must contain zeroes if no amount paid.
411-425	Net Taxes	Enter zeroes if there is no significant amount. Enter amount right justified and zero filled if significant. Net taxes is the result of the subtraction of the Advanced Earned Income Credit from Total Taxes.
426-440	Total Taxes Deposited plus overpayment from previous quarter	FTDs plus overpayment from prior quarter.
441-450	Overpayment from Previous Quarter	Enter zeroes if there is no significant amount. Enter right justified and zero filled if significant.
451-461	Excess	Amount that Total Taxes Deposited exceeds Net Taxes.
462	Credit Elect Indicator	Enter zero if credit is to be applied to next return. Enter "1" if amount is to be refunded or if Excess (tape positions 451-461) is zero.
463	Safe Haven Rule Indicator	Enter zero if taxpayer is making deposits using the 95% safe haven rule. Otherwise, enter "1".
464	First Time 3-Banking Day Depositor Indicator	Enter zero if taxpayer is a first time 3-banking day depositor. Otherwise, enter "1".
465-468	Number of FTDs Made	Enter the total number of FTDs made by this taxpayer during the tax period. Right justify and zero fill.
469-483	Total Taxes Deposited for this quarter	Enter the sum of Total Amount of FTDs in dollars and cents from preceding Tax Data "B" Records from the last Agent "A" Record. Right justify and zero fill.

TAX DATA "B" RECORD—Continued

Note: Positions 484-723 are used to report the accrual of the taxpayer's Federal Tax Liability.

1). If the tax liability is less than $500.00, zero fill these fields.

2). If the tax liability is less than $3000.00 in any given month, place the amount in the fields that refer to the last day of the month and zero fill the other fields.

3). If the taxes accrued are greater than $3000.00 for any month, find the eighth-monthly period(s) in which there was a payday and enter the accrued amounts in those fields. Zero fill any unused fields.

Tape Position	Element Name	Entry or Description
484-493	Tax Liability, 3rd Day (1st Month)	Enter the tax liability for the period beginning on the 1st day and ending of the 3rd day of the 1st month.
494-503	Tax Liability, 7th Day (1st Month)	Enter the tax liability for the period beginning on the 4th day and ending on the 7th day of the 1st month.
504-513	Tax Liability, 11th Day (1st Month)	Enter the tax liability for the period beginning on the 8th day and ending on the 11th day of the 1st month.
514-523	Tax Liability, 15th Day (1st Month)	Enter the tax liability for the period beginning on the 12th day and ending on the 15th day of the 1st month.
524-533	Tax Liability, 19th Day (1st Month)	Enter the tax liability for the period beginning on the 16th day and ending on the 19th day of the 1st month.
534-543	Tax Liability, 22nd Day (1st Month)	Enter the tax liability for the period beginning on the 20th day and ending on the 22nd day of the 1st month.
544-553	Tax Liability, 25th Day (1st Month)	Enter the tax liability for the period beginning on the 23rd day and ending on the 25th day of the 1st month.
554-563	Tax Liability, last Day (1st Month)	Enter the tax liability for the period beginning on the 26th day and ending on the last day of the 1st month.
564-573	Tax Liability, 3rd Day (2nd Month)	Enter the tax liability for the period beginning on the 1st day and ending on the 3rd day of the 2nd month.
574-583	Tax Liability, 7th Day (2nd Month)	Enter the Tax liability for the period beginning on the 4th day and ending on the 7th day of the 2nd month.
584-593	Tax Liability, 11th Day (2nd Month)	Enter the tax liability for the period beginning on the 8th day and ending on the 11th day of the 2nd month.
594-603	Tax Liability, 15th Day (2nd Month)	Enter the tax liability for the period beginning on the 12th day and ending on the 15th day of the 2nd month.
604-613	Tax Liability, 19th Day (2nd Month)	Enter the tax liability for the period beginning on the 16th day and ending on the 19th day of the 2nd month.
614-623	Tax Liability, 22nd Day (2nd Month)	Enter the tax liability for the period beginning on the 20th day and ending on the 22nd day of the 2nd month.
624-633	Tax Liability, 25th Day (2nd Month)	Enter the tax liability for the period beginning on the 23rd day and ending on the 25th day of the 2nd month.
634-643	Tax Liability, last Day (2nd Month)	Enter the tax liability for the period beginning on the 26th day and ending on the last day of the 2nd month.
644-653	Tax Liability, 3rd Day (3rd Month)	Enter the tax liability for the period beginning on the 1st day and ending on the 3rd day of the 3rd month.

TAX DATA "B" RECORD—Continued

Tape Position	Element Name	Entry or Description
654-663	Tax Liability, 7th Day (3rd Month)	Ente the tax liability for the period beginning on the 4th day and ending on the 7th day of the 3rd month.
664-673	Tax Liability, 11th Day (3rd Month)	Enter the tax liability for the period beginning on the 8th day and ending on the 11th day of the 3rd month.
674-683	Tax Liability, 15th Day (3rd Month)	Enter the tax liability for the period beginning on the 12th day and ending on the 15th day of the 3rd month.
684-693	Tax Liability, 19th Day (3rd Month)	Enter the tax liability for the period beginning on the 16th day and ending on the 19th day of the 3rd month.
694-703	Tax Liability, 22nd Day (3rd Month)	Enter the tax liability for the period beginning on the 20th day and ending on the 22nd day of the 3rd month.
704-713	Tax Liability, 25th Day (3rd Month)	Enter the tax liability for the period beginning on the 23rd day and ending on the 25th day of the 3rd month.
714-723	Tax Liability, last Day (3rd Month)	Enter the tax liability for the period beginning on the 26th day and ending on the last day of the 3rd month.
724	Schedule A Tax Indicator	Enter zero if the Schedule A Tax Liability amounts have been included on the regular Tax Liability fields (tape pos. 484-723). Enter "1" if the Schedule A Tax Liability amounts have been entered on the Mag Tape Schedule A Tax Liability fields (pos. 725-964). Enter "2" if the paper document Schedule A has been filed.

Note: Positions 725-964 are used to report Backup Withholding if the Schedule A Tax Indicator is set to "1". If Schedule A Tax Indicator is other than 1, zero fill positions 725-964.

1). If tax liability is less than $500.00, zero fill these fields.

2). If tax liability is less than $3000.00 in any given month, place the amount in the fields that refer to the last day of the month and zero fill the other fields.

3). If the taxes accrued are greater than $3000.00 for any month, find the eighth-monthly period(s) in which there was a payday and enter the accrued amounts in those fields. Zero fill any unused fields.

725-734	Schedule A Tax Liability 3rd Day (1st Month)	Enter the Schedule A Tax Liability for the period beginning on the 1st day and ending on the 3rd day of the first month. If none zero fill.
735-744	Schedule A Tax Liability 7th Day (1st Month)	Enter the Schedule A Tax Liability for the period beginning on the 4th day and ending on the 7th day of the first month. If none zero fill.
745-754	Schedule A Tax Liability 11th Day (1st Month)	Enter the Schedule A Tax Liability for the period beginning on the 8th day and ending on the 11th day of the first month. If none zero fill.
755-764	Schedule A Tax Liability 15th Day (1st Month)	Enter the Schedule A Tax Liability for the period beginning on the 12th day and ending on the 15th day of the first month. If none zero fill.
765-774	Schedule A Tax Liability 19th Day (1st Month)	Enter the Schedule A Tax Liability for the period beginning on the 16th day and ending on the 19th day of the first month. If none zero fill.

TAX DATA "B" RECORD—Continued

Tape Position	Element Name	Entry or Description
775-784	Schedule A Tax Liability 22nd Day (1st Month)	Enter the Schedule A Tax Liability for the period beginning on the 20th day and ending on the 22nd day of the first month. If none zero fill.
785-794	Schedule A Tax Liability 25th Day (1st Month)	Enter the Schedule A Tax Liability for the period beginning on the 23rd day and ending on the 25th day of the first month. If none zero fill.
795-804	Schedule A Tax Liability Last Day (1st Month)	Enter the Schedule A Tax Liability for the period beginning on the 26th day and ending on the last day of the first month. If none zero fill.
805-814	Schedule A Tax Liability 3rd Day (2nd Month)	Enter the Schedule A Tax Liability for the period beginning on the 1st day and ending on the 3rd day of the second month. If none zero fill.
815-824	Schedule A Tax Liability 7th Day (2nd Month)	Enter the Schedule A Tax Liability for the period beginning on the 4th day and ending on the 7th day of the second month. If none zero fill.
825-834	Schedule A Tax Liability 11th Day (2nd Month)	Enter the Schedule A Tax Liability for the period beginning on the 8th day and ending on the 11th day of the second month. If none zero fill.
835-844	Schedule A Tax Liability 15th Day (2nd Month)	Enter the Schedule A Tax Liability for the period beginning on the 12th day and ending on the 15th day of the second month. If none zero fill.
845-854	Schedule A Tax Liability 19th Day (2nd Month)	Enter the Schedule A Tax Liability for the period beginning on the 16th day and ending on the 19th day of the second month. If none zero fill.
855-864	Schedule A Tax Liability 22nd Day (2nd Month)	Enter the Schedule A Tax Liability for the period beginning on the 20th day and ending on the 22nd day of the second month. If none zero fill.
865-874	Schedule A Tax Liability 25th Day (2nd Month)	Enter the Schedule A Tax Liability for the period beginning on the 23rd day and ending on the 25th day of the second month. If none zero fill.
875-884	Schedule A Tax Liability Last Day (2nd Month)	Enter the Schedule A Tax Liability for the period beginning on the 26th day and ending on the last day of the second month. If none zero fill.
885-894	Schedule A Tax Liability 3rd Day (3rd Month)	Enter the Schedule A Tax Liability for the period beginning on the 1st day and ending on the 3rd day of the third month. If none zero fill.
895-904	Schedule A Tax Liability 7th Day (3rd Month)	Enter the Schedule A Tax Liability for the period beginning on the 4th day and ending on the 7th day of the third month. If none zero fill.
905-914	Schedule A Tax Liability 11th Day (3rd Month)	Enter the Schedule A Tax Liability for the period beginning on the 8th day and ending on the 11th day of the third month. If none zero fill.

TAX DATA "B" RECORD—Continued

Tape Position	Element Name	Entry or Description
915-924	Schedule A Tax Liability 15th Day (3rd Month)	Enter the Schedule A Tax Liability for the period beginning on the 12th day and ending on the 15th day of the third month. If none zero fill.
925-934	Schedule A Tax Liability 19th Day (3rd Month)	Enter the Schedule A Tax Liability for the period beginning on the 16th day and ending on the 19th day of the third month. If none zero fill.
935-944	Schedule A Tax Liability 22nd Day (3rd Month)	Enter the Schedule A Tax Liability for the period beginning on the 20th day and ending on the 22nd day of the third month. If none zero fill.
945-954	Schedule A Tax Liability 25th Day (3rd Month)	Enter the Schedule A Tax Liability for the period beginning on the 23rd day and ending on the 25th day of the third month. If none zero fill.
955-964	Schedule A Tax Liability Last Day (3rd Month)	Enter the Schedule A Tax Liability for the period beginning on the 26th day and ending on the last day of the third month. If none zero fill.

.10 Checkpoint Totals "C" Record

1. Write this record after each 100 or fewer (if less than 100 remain) Tax Data "B" Records. Each Checkpoint Totals "C" Record must contain a count of Tax Data "B" Records, the sum of Total Taxes, the Total Number of FTDs made and the sum of the Total Amounts of FTDs for all Tax Data "B" Records which have not been summarized in preceding Checkpoint Totals "C" Records.

2. The Checkpoint Totals "C" Record must be followed by a Tax Data "B" Record except as follows: If the Checkpoint Totals "C" Record is at the end of the reel, it will be followed by an End of Reel "F" Record. If the Checkpoint Totals "C" Record is at the end of the file, it will be followed by an End of File "E" Record.

3. All Checkpoint Totals "C" Records must be fixed length. All money amount fields will contain dollars and cents. The Checkpoint Totals "C" Records cannot be followed by a tape mark.

CHECKPOINT TOTALS "C" RECORD

Tape Position	Element Name	Entry or Definition
1	Record Type	Enter "C". Must be first character of the Checkpoint Totals "C" Record.
2-6	Number of Tax Data "B" Records	Enter number of Tax Data "B" Records processed since last Checkpoint Totals "C" Record or Agent "A" Record has been written. Right justify and zero fill if less than five positions are required.
7-22	Total Taxes	Enter the sum of Total Taxes in dollars and cents from Tax Data "B" Records in the preceding 100 or fewer records (tape positions 386-400). Right justify and zero fill.
23-29	Number of FTDs Made	Enter total number of FTDs made during the tax period for Tax Data "B" Records in the preceding 100 or fewer records (tape positions 465-468). Right justify and zero fill.
30-45	Total Amount of FTDs	Enter the sum of the Total Amount of FTDs in dollars and cents for Tax Data "B" Records in the preceding 100 or fewer records (tape positions 469-483). Right justify and zero fill.

11. End of File "E" Record

1. Write this record after the last Checkpoint Totals "C" Record in the file. All money amounts will contain dollars and cents. All End of File "E" Records must be fixed length. This record can be followed only by a tape mark or tape mark and trailer label.

END OF FILE "E" RECORD

Tape Position	Element Name	Entry or Definition
1	Record Type	Enter "E". Must be the first character of the End of File "E" Record.
2-6	Number of Tax Data "B" Records	Enter total number of Tax Data "B" Records (including the reporting agent) which are reported on the tape file. Only one Tax Data "B" Record is permissible for each taxpayer. Right justify and zero fill if less than five positions are required.
7-22	Total Taxes	Enter the sum of Total Taxes in dollars and cents for all Tax Data "B" Records reported on the tape file (tape positions 386-400). This should balance to Total Taxes accumulated in Checkpoint Totals "C" Records (tape positions 7-22). Right justify and zero fill.
23-29	Number of FTDs Made	Enter total number of FTDs made during the tax period for all Tax Data "B" Records reported on the tape file (tape positions 465-468). This should balance to number of FTDs accumulated in Checkpoint Totals "C" Records (tape positions 23-29). Right justify and zero fill.
30-45	Total Amount of FTDs	Enter the sum of the Total Amount of FTDs in dollars and cents from all Tax Data "B" Records on the tape file (tape positions 469-483). This should balance to Total Amount of FTDs accumulated in Checkpoint Totals "C" Records (tape positions 30-45). Right justify and zero fill.

12. End of Reel "F" Record

1. Write this record when the end of the normal writing area of each reel has been reached, but all records in the file have not been written. This record indicates that there are additional reels in the file. Each End of Reel "F" Record must contain a count of Tax Data "B" Records, the sum of Total Taxes, the Total Number of FTDs made and the sum of the Total Amount of FTDs for all Checkpoint Totals "C" Records on that reel.

2. The End of Reel "F" Record cannot be followed by an Agent "A" Record, Tax Data "B" Record, Checkpoin Totals "C" Record or End Of File "E" Record. A tape mark or tape mark anc trailer label only can follow this record.

3. Do not use this record on the fina reel of the file being transmitted.

END OF REEL "F" RECORD

Tape Position	Element Name	Entry or Definition
1	Record Type	Enter "F". Must be the first character of the End of Reel "F" Record.
2-6	Number of Tax Data "B" Records	Enter total number of Tax Data "B" Records contained on this tape reel. Right justify and zero fill.
7-22	Total Taxes	Enter the sum of Total Taxes in dollars and cents from all preceding Tax Data "B" Records from the last Agent "A" Record (tape positions 386-400). Right justify and zero fill.
23-29	Number of FTDs Made	Enter the total number of FTDs made during the tax period from all preceding Tax Data "B" Records from the last Agent "A" Record (tape positions 465-468). Right justify and zero fill.

Tape Position	Element Name	Entry or Definition
30-45	Total Amount of FTDs	Enter the sum of Total Amount of FTDs in dollars and cents from all preceding Tax Data "B" Records from the last Agent "A" Record (tape positions 469-483). Right justify and zero fill!

SEC. 14. POST OFFICE STATES CODES

Enter the official two position Post Office State Code abbreviations for States and Territories in the Agent "A" Records and Tax Data "B" according to the following:

STATE	CODE
Alabama	AL
Alaska	AK
Arizona	AZ
Arkansas	AR
California	CA
Colorado	CO
Connecticut	CT
Delaware	DE
District of Columbia	DC
Florida	FL
Georgia	GA
Hawaii	HI
Idaho	ID
Illinois	IL
Indiana	IN
Iowa	IA
Kansas	KS
Kentucky	KY
Louisiana	LA
Maine	ME
Maryland	MD
Massachusetts	MA
Michigan	MI
Minnesota	MN
Mississippi	MS
Missouri	MO
Montana	MT
Nebraska	NE
Nevada	NV
New Hampshire	NH
New Jersey	NJ
New Mexico	NM
New York	NY
North Carolina	NC
North Dakota	ND
Ohio	OH
Oklahoma	OK
Oregon	OR
Pennsylvania	PA
Rhode Island	RI
South Carolina	SC
South Dakota	SD
Tennessee	TN
Texas	TX
Utah	UT
Vermont	VT
Virginia	VA
Washington	WA
West Virginia	WV
Wisconsin	WI
Wyoming	WY
Puerto Rico	PR
Virgin Islands	VI
Guam	GU

SEC. 15. EFFECT ON OTHER DOCUMENTS

This Revenue Procedure supersedes Rev. Proc. 84-11.

SEC. 16. EFFECTIVE DATE

This Revenue Procedure is effective January 1, 1986.

Exhibit 1
Agent's Listing

NAME ______________________________

ADDRESS ______________________________

ADDRESS

TYPE OF TAX

EMPLOYER IDENTIFICATION NUMBER	NAME CONTROL	T/P NAME & ADDRESS	DISTRICT OFFICE CODE	FILE AT SERVICE CENTER

Note: District Office Code and Filing Service Center filled in by the Service.

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER H, PART 601—STATEMENT OF PROCEDURAL RULES MISCELLANEOUS AMENDMENTS

SUMMARY: This document contains amendments to the Statement of Procedural Rules (SPR) to reflect changes in the fees charged with search and duplication services. The provisions are amended to conform to Department of Treasury Regulations related to the disclosure of records under the Freedom of Information Act and to incorporate a recent change in charges for copies of returns and return information.

EFFECTIVE DATE: April 25, 1983, except section 601.702(f)(5) (regarding charges for copies of returns, etc.) is effective October 1, 1985.

FOR FURTHER INFORMATION CONTACT: Mark S. Jennings of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W. Washington, D.C. 20224; Attention: CC:LR:T (202) 566-3458, not a toll-free number.

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains amendments to the SPR (26 CFR Part 601).

Section 601.702(f) of the SPR, relating to fees for services, is amended to conform with Treasury Department Regulations at 31 CFR §1.6 as amended April 25, 1983, (48 F.R. 12350). The section is also amended to reflect Rev. Proc. 85-56, 1985-46 I.R.B. 45 (modifying Rev. Proc. 66-3, 1966-1 C.B. 601) regarding charges for copies of returns and transcripts.

The Treasury Department amended its regulations implementing the Freedom of Information Act (FOIA). The amendment increased the fees charged for duplication, search, and unpriced printed material to reflect increased costs to the Department. The fee for copying records is $.15 per copy of each page made by photocopy or similar process. The rate of $.15 per copy of each page also applies to preprinted materials, which will no longer be available at reduced rates. The search fee has been increased to $10.00 for each hour or fraction thereof and applies to all searches, including those which take less than one hour. Charges for computer searches will reflect the actual direct cost of the Department, as will fees for computer printouts. Section 601.702(f) of the SPR is amended to reflect these changes.

Rev. Proc. 85-56, 1985-46 I.R.B. 45, modified Rev. Proc. 66-3, 1966-1 C.B. 601 to reflect the implementation of a pre-paid fixed fee system for furnishing taxpayers with photocopies of their tax returns or transcripts of return information. The charge for a photocopy of a tax return is $4.25 and the charge for a transcript of tax information is $2.25. The Revenue Procedure includes instructions for making requests for copies and advance payments. The purpose of the new system is to eliminate the administrative costs involved in billing taxpayers who request copies of returns and return information. Requiring payment in advance will ensure that the total cost of securing and furnishing photocopies will be paid by those individuals who request such information. Section 601.702(f) is amended to add a new paragraph (f)(5) to set forth these rules.

EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required.

PAPERWORK REDUCTION ACT

The collection of information contained in this regulation has been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. This collection has been approved by OMB (Control No. 1545-0429).

DRAFTING INFORMATION

The principal author of these amendments to the Statement of Procedural Rules is Sandra E. Wallach of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service participated in developing the amendments both on matters of substance and style.

* * * * *

Adoption of Amendments to the Statement of Procedure Rules

Accordingly, 26 CFR Part 601 is amended as follows:

PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Paragraph 1. The authority for Part 601 continues to read in part:

Authority: 5 U.S.C. 301 and 502.

Par. 2. Section 601.702 is amended as follows:

1. Paragraphs (f)(3) and (f)(4) are revised to read as set forth below.

2. Paragraphs (f)(5), (6), (7), (8), and (9) are redesignated as paragraphs (f)(6), (7), (8), (9), and (10) respectively, and a new paragraph (f)(5) is added, to read as set forth below.

3. Paragraph (f)(6) as redesignated is amended by removing the first two sentences.

§601.702 Publication and public inspection.

* * * * *

(f) *Fees for services.* * * *

(3) *Search services.* Fees charged for search services are as follows:

(i) Searches other than for computerized records—$10.00 for each hour or fraction thereof for time spent by each clerical, professional, and supervisor in finding the records and information within the scope of the request.

(ii) Searches for computerized records—Actual direct cost of the search. The fee for computer printouts will be actual costs.

(iii) Searches requiring travel or transportation—Shipping charges to transport records from one location to another, or for the transportation of an employee to the site of requested records when it is necessary to locate rather than examine the records, shall be at the rate of the actual cost of such shipping or transportation.

(iv) Other services and materials requested, pursuant to the Freedom of Information Act, which are not covered by this part are chargeable at the actual cost of the Internal Revenue Service.

(4) *Duplication other than for returns, transcripts of return information, and related documents.* Fees charged for duplication other than for returns, transcripts of return information, and related documents are as follows:

(i) $.15 per copy of each page, up to 8½" × 14", made by photocopy or similar process.

(ii) Photographs, films, and other materials—actual cost of reproduction.

(iii) Records may be released to a private contractor for copying and the requester will be charged the actual cost of duplication charged by the private contractor.

(iv) When other duplications not specifically identified above are requested and provided pursuant to the Freedom of Information Act their direct cost to the Internal Revenue Service shall be charged.

(5) *Charges for copies of returns, transcripts of return information, and related documents.* Charges for furnishing copies of returns, transcripts of return information, and related documents are as follows:

(i) A charge of $4.25 will be made for each request for a copy of a return or other related document (other than Employee Plans and Exempt Organization Returns). Payments are to be submitted in advance using IRS Form

4506, Request For Copy Of Tax Form or Individual Income Tax Account Information.

(ii) A charge of $2.25 will be made for each request for a transcript of individual income tax account information. Payments shall be submitted according to procedures prescribed in paragraph (g)(5)(i) of this section.

(iii) A charge of $1.00 for the first page and $.15 for each subsequent page will be made for copies of Employee Plans and Exempt Organizations tax returns and related documents. Payments will be submitted subsequent to receipt of Form 2860, Document Transmittal and Bill.

Par. 3. Section 601.9000(c) is amended by inserting in the appropriate place in the table "§601.702(f)(2) . . . 1545-0429".

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on March 3, 1986, 8:45 a.m., and published in the issue of the Federal Register for March 4, 1986, 51 F.R. 7441)

Part IV. Items of General Interest

Income, Excise, and Estate and Gift Taxes; Effective Dates and Other Issues Arising Under the Employee Benefit Provisions of the Tax Reform Act of 1984—Public Hearing

Announcement 86-72[1]

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to effective dates and certain other issues arising under the employee benefit provisions of the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-3 C.B. (Vol.1) 1].

DATES: The public hearing will be held on Thursday, June 26, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Thursday, June 12, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, Attn: CC:LR:T (EE-96-85), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935 (not a toll-free call).

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under sections 72, 79, 125, 133, 162, 402, 404, 419, 419A, 461(h), 463, 505, 512, 1042, 2039, 4976, 4978 and 7701(a)(46) of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Tuesday, February 4, 1986 (51 FR 4391) [EE-96-85, 1986-13 I.R.B. 48].

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Thursday, June 12, 1986, an outline of oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speaker will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

Treatment of Qualified Real Estate Agents and Direct Sellers as Nonemployees; Determination of Employer Liability for Certain Employment Taxes; Information Reporting of Direct Sales and Payments of Remuneration for Services—Public Hearing

Announcement 86-73[1]

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to the following subjects: (1) The treatment of qualified real estate agents and direct sellers as nonemployees for Federal income and employment tax purposes, (2) the determination of employer liability for income tax withholding and employee social security taxes where the employer treated an employee as a nonemployee for purposes of such taxes, and (3) information reporting of direct sales and payments of remunertion for services.

DATES: The public hearing will be held on Wednesday, June 18, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Wednesday, June 4, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, ATTN: CC:LR:T (LR-214-82), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT:; Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935, not a toll-free call.

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under sections 3508, 3509, and 6041A of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Tuesday, January 7, 1986 (51 FR 619) [LR-214-82, 1986-6 I.R.B. 46].

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Wednesday, June 4, 1986, an outline of oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

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[1] Filed by the Office of the Federal Register on April 28, 1986, 8:45 a.m., and published in the issue of the Federal Register for April 29, 1986, 51 F.R. 15916.

[1] Filed by the Office of the Federal Register on April 9, 1986, 8:45 a.m., and published in the issue of the Federal Register for April 10, 1986, 51 F.R. 12341.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Gary E. Borushko	Grosse Pointe Woods, MI	Certified Public Accountant	Indefinite from April 7, 1986
Paul Skulsky	Spring Valley, NY	Certified Public Accountant	Indefinite from April 1, 1986
Mack I. Frank	Eunice, LA	Attorney	Indefinite from April 1, 1986
Carl Goldfarb	Charlotte, NC	Attorney	Indefinite from April 28, 1986
Dennis M. Hayes	Ann Arbor, MI	Attorney	Indefinite from April 15, 1986
Ronald N. Kief	Warren, MI	Certified Public Accountant	Two Years from June 1, 1986
Richard L. Leopold	Ottawa, OH	Attorney	Three Months from May 1, 1986
Julius Stackel	Flushing, NY	Certified Public Accountant	Thirty Months from April 15, 1986
John Such	Lyndhurst, OH	Enrolled Agent	Eighteen Months from April 22, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by, or sharing fees with, any practitioner disbarred or under suspension from practice before their Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Thomas H. Foxhill, Jr.	Pemberton, NJ	Enrolled Agent	April 12, 1986
Peter Parker	Baltimore, MD	Attorney	April 12, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.61-6(c)(3), 1.163-4, 1.451-1(d), 1.451-2(b), 1.454-1(a)(1)(i), 1.482-2(a), 1.482-2(c)(2), 1.483-1, 1.483-2, 1.1016-5(s), 1.1232-2, 25.2512-4, 25.2512-8, revised; 1.163-7, 1.446-2, 1.483-3 through 1.483-5, 1.1271-1 through 1.1275-5, added; 1.61-7(d), 1.249-1, 1.409-1(b)(1), 1.528-1(d), 1.582-1(e)(3)(i), 1.636-1(a)(1)(ii), 1.818-3(f), 1.861-2(a)(4), 1.993-1(g), 1.1001-1(g), 1.1012-1(f), 1.1037-1, 1.1232-1, 1.1232-3A, 1.6045-1(c), 1.6049-5, 1.6049-6(d), 1.9006-1(c)(1)(vii), 3.2(d), 3.3(b), 5f.163-1(f), 6a.103A-2(i)(2)(vi)(B), 514.23, amended; 1.1012-2, removed and new added; 1.7872-4(e), reproposed and revised.	Original issue discount rules, imputed interest rules, and safe haven interest rates	1986-18 I.R.B. 4	June 9, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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Key to Abbreviations:

RR	Revenue Ruling
RP	Revenue Procedure
TD	Treasury Decision
CD	Court Decision
PL	Public Law
EO	Executive Order
DO	Delegation Order
TDO	Treasury Department Order
TC	Tax Convention
SPR	Statement of Procedural Rules
PTE	Prohibited Transaction Exemption

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______	1928-1	8.00
______	1928-2	10.00
______	1929-1	13.00
______	*1929-2*	*3.50*
______	1930-1	8.50
______	1930-2	10.00
______	*1931-1*	*4.00*
______	1931-2	14.00
______	*1932-1*	*3.25*
______	1932-2	10.00
______	*1933-1*	*3.75*
______	*1933-2*	*4.00*
______	*1934-1*	(**)
______	1934-2	15.00
______	1935-1	8.00
______	*1935-2*	*15.00*
______	*1936-1*	*4.00*
______	*1936-2*	*15.00*
______	*1937-1*	*14.00*
______	1937-2	8.50
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______	1939-1-1	9.50
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______	1960-2	13.00
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Internal Revenue
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These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-80, page 4.
Business expenses; insurance; commodities trader; required contributions to commodities exchange. A commodities trader may not deduct as business expenses funds required by the commodities exchange to be paid to a fund that will pay death benefits to the beneficiary of the trader. Rev. Rul. 70-342 revoked.

T.D. 8087, page 5.
LR-3-86, page 33.
Temporary and proposed amendments to the regulations under sections 367 and 6038B of the Code relate to transfers of property by U.S. persons to foreign corporations.

Finding Lists begin on page 35.
Announcement of Suspensions on page 34.

Department of the Treasury
Internal Revenue Service

T22. 23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

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Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

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Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 162.—Trade or Business Expenses

26 CFR 1.162-1: Business expenses.
(Also Sections 262, 7805; 1.262-1, 301.7805-1.)

Business expenses; insurance; commodities trader; required contributions to commodities exchange. A commodities trader may not deduct as business expenses funds required by the commodities exchange to be paid to a fund that will pay death benefits to the beneficiary of the trader. Rev. Rul. 70-342 revoked.

Rev. Rul. 86-80

ISSUE

If an individual who is engaged in trade or business as a commodities trader is required to make contributions to a Board of Trade Gratuity Fund (Fund) that will pay death benefits to a Fund participant's beneficiaries or estate, may that individual deduct these contributions as business expenses under section 162(a) of the Internal Revenue Code?

FACTS

Taxpayer is a commodities trader and as such is required to become a member of a Board of Trade in order to trade on the floor of a commodities exchange. Every Board of Trade member under age 55 is also required to become a member of the Board of Trade Gratuity Fund and to pay assessments levied yearly by the Fund. The taxpayer is under age 55. The purpose is to provide, upon the death of a participant, an amount that is payable to the participant's beneficiaries or estate. Upon the death of a Board of Trade member, trustees of the Fund, pursuant to the specific provisions of the Board of Trade's constitution, pay out designated amounts to the participant's beneficiaries or estate.

LAW AND ANALYSIS

Section 162 of the Code provides, in part, that there is allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.

Section 262 of the Code provides that, except as expressly provided by the Code, no deduction is allowed for personal, living, or family expenses. Section 1.262-1(b)(1) of the Income Tax Regulations provides that premiums paid for life insurance by an insured are not deductible.

In *Commissioner v. Treganowan*, 183 F.2d 288 (2d Cir. 1950), *cert. denied*, 340 U.S. 853 (1950), the U.S. Court of Appeals for the Second Circuit held that amounts received from the New York Stock Exchange Gratuity Fund by a widow of a deceased member of the Exchange were "proceeds of life insurance." *See also Estate of Edmonds v. Commissioner*, 16 T.C. 110 (1951), which followed *Treganowan.*

In *Estate of Moyer v. Commissioner*, 32 T.C. 515 (1959), *acq. in part*, 1960-2 C.B. 6, the Tax Court held that (1) the Philadelphia-Baltimore Stock Exchange Gratuity Fund, a fund similar to the New York Stock Exchange Gratuity Fund, was a mutual insurance company, (2) the benefits paid to the beneficiaries of deceased members of the Exchange constituted amounts received under life insurance contracts paid by reason of the death of the insured and were excludable from the gross income of the recipients under section 101(a)(1) of the Code, and (3) the payments to the Gratuity Fund constituted "premiums or other consideration" for insurance within the meaning of section 811(g)(2) of the Internal Revenue Code of 1939. *See also* Rev. Rul. 72-463, 1972-2 C.B. 93, which holds that mandatory monthly dues and assessments paid by members of a labor union are deductible business expenses under section 162(a) of the Code, except that the portion of the assessments used to provide death benefits is a nondeductible personal expense.

Rev. Rul. 70-342, 1970-2 C.B. 32, however, reaches a different conclusion concerning payments to the New York Stock Exchange Gratuity Fund, which was maintained for the benefit of families of deceased members of the Exchange. Payments to the Gratuity Fund were mandatory under the Exchange's constitution in order for members to maintain their standing on the Exchange. Upon the death of an Exchange member, trustees of the Gratuity Fund, pursuant to the Exchange constitution, paid designated amounts out of the Gratuity Fund to designated beneficiaries. The ruling holds that payments to the Gratuity Fund by members who are actually engaged in business on the Exchange are deductible business expenses under section 162 of the Code.

The New York Stock Exchange Gratuity Fund, the Philadelphia-Baltimore Stock Exchange Gratuity Fund and the Fund in this case are similar because members of each exchange are required to pay assessments to the respective funds, each fund is maintained and operated exclusively to provide benefits upon the death of a member and the risk of loss from premature death is shifted from the individual to the group of other members of the exchanges. All three funds provide members of the exchanges with life insurance. Therefore, section 262 disallows any deduction for the "premiums" paid by the taxpayer-insured to the Board of Trade Gratuity Fund. This conclusion is equally applicable to the situation described in Rev. Rul. 70-342.

HOLDING

Payments to the Fund by the Board of Trade member are not deductible from gross income under section 162(a) of the Code, but rather are personal expenses under section 262.

PROSPECTIVE APPLICATION

Under the authority of section 7805(b) of the Code, the holding of this revenue ruling will not be applied adversely to amounts paid or incurred before June 9, 1986.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 70-342 is revoked.

Section 262.—Personal, Living, and Family Expenses

26 CFR 1.262-1: Personal, living, and family expenses.

Whether contributions made by a commodities trader to a Board of Trade Gratuity Fund that will pay death benefits to a Fund participant's beneficiaries or estate are deductible business expenses or are personal expenses. See Rev. Rul. 86-80, this page.

Section 367.—Foreign Corporations

26 CFR 1.367(a)-1T: Transfers to foreign corporations subject to section 367(a): In general (temporary).
(Also Section 6038B; 1.6038B-1T.)

T.D. 8087

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER A, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 7—TEMPORARY INCOME TAX REGULATIONS UNDER THE TAX REFORM ACT OF 1976; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Transfers of Property by U.S. Persons to Foreign Corporations

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document provides temporary Income Tax Regulations relating to transfers of property by U.S. persons to foreign corporations. These regulations affect U.S. persons that transfer property to foreign corporations pursuant to the corporate organization, reorganization, or liquidation provisions of the Internal Revenue Code. They provide the public with guidance necessary to comply with the Tax Reform Act of 1984 [Pub. L. 98-369, 1984-1 C.B. (Vol.1) 1]. In addition, the text of the temporary regulations set forth in this document serves as the text of the proposed regulations cross-referenced * * * [on page 33, this Bulletin].

DATES: These temporary regulations are generally applicable for transfers made after December 31, 1984, and are effective June 16, 1986.

FOR FURTHER INFORMATION CONTACT: Charles W. Culmer, of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington, D.C. 20224, Attention: CC:LR:T (202-566-4336, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains temporary Income Tax Regulations (26 CFR Part 1) under section 367 of the Internal Revenue Code of 1954, as amended by section 131 of the Tax Reform Act of 1984 (98 Stat. 662) [Pub. L. 98-368, 1984-3 C.B. (Vol.1) 1, 170]. The temporary regulations are issued under the authority contained in sections 367 (26 USC 367) and 7805 (26 USC 7805) of the Internal Revenue Code of 1954.

DISCUSSION

Statutory provisions

The Tax Reform Act of 1984 substantially revised the rules that apply under section 367 to transfers of property by U.S. persons to foreign corporations. Section 367(a) now provides generally that a foreign corporation will not be considered to be a corporation, for purposes of applying the corporate organization, reorganization, and liquidation rules to a U.S. person's transfer of property to the foreign corporation. Thus, transfers of property to foreign corporations will generally be treated as taxable exchanges. However, an exception is provided for transfers of property that will be used in the active conduct of a trade or business outside of the United States. Such transfers may be made tax-free. On the other hand, certain types of property are specified that may not be transferred free of tax, even if they are to be used in the active conduct of a trade or business. In addition, a special rule requires the recapture of previously deducted losses of a foreign branch, when the branch is transferred to a foreign corporation. New section 367(d) applies a special rule to certain transfers of intangible property to foreign corporations, requiring the U.S. transferor to recognize a U.S.-source deemed payment for the transferred property annually over the useful life of the property. Finally, new section 367(e) provides that liquidating distributions by domestic corporations under section 336 will be taxable under rules similar to those of section 367(a).

Need for temporary regulations

The effective date of the amendments to section 367 is January 1, 1985. The proper application of the section is dependent upon the Service's detailed specification by regulations of the manner in which the general requirements of the statute will be administered. Without this specification, taxpayers will be unable to make transfers to related foreign corporations with certainty as to the U.S. income tax consequences of the transfer. Because of the need for immediate guidance in this regard, for both the public and employees of the Internal Revenue Service, the Service has found it to be impracticable to issue these temporary regulations either with notice and public procedure under section 553(b) of Title 5 of the United States code.

Description of temporary regulations

Section 1.367(a)-1T provides general rules describing the transfer of property that are subject to section 367(a), and explaining the effect of the section upon those transfers. A gain-limitation rule is provided in §1.367(a)-1T(b)(3), ensuring that the gain recognized under section 367(a) upon a transfer of appreciated property is not greater than the gain that would be recognized on a normal taxable exchange. Detailed rules are provided in §1.367(a)-1T(c) concerning various transactions that are considered to include a transfer subject to section 367(a). Relevant definitions are provided in §1.367(a)-1T(d). Section 1.367(a)-1T(e) contains effective date provisions.

Section 1.367(a)-2T provides rules concerning the exception from section 367(a) for transfers of property that will be used in the active conduct of a trade or business outside of the United States. Paragraph (b) of the section separately defines the concepts of "trade or business," "active conduct," and "outside of the United States." Each standard must be met for a transfer to qualify for the exception.

Section 1.367(a)-3T provides rules concerning transfers of stock or securities to a foreign corporation in an exchange described in section 367(a). Paragraph (b) specifies certain transfers of stock that are not subject to section 367(a). Paragraph (c) provides rules concerning transfers of stock of domestic corporations. Such transfers are generally taxable, but several exceptions are provided. Paragraph (d) provides rules concerning transfers of stock of foreign corporations. Again, such transfers are generally taxable, but several exceptions are provided. Paragraphs (e), (f), and (g) provide rules concerning the exceptions that are applicable under paragraphs (c) and (d). Under paragraph (e), a transfer of stock is not subject to section 367(a) if the transfer is for use in the active conduct of a trade or business, as defined in that paragraph. Paragraph (f) provides that a transfer is not subject to section 367(a) if the U.S. transferors of the stock obtain a limited interest in the transferee foreign corporation. Under paragraph (g), a transfer of stock is not subject to section 367(a) if the U.S. transferor agrees to recognize gain upon any subsequent disposition of the stock by the transferee foreign corporation. Finally, paragraph (h) sets forth two anti-abuse rules.

Section 1.367(a)-4T contains a series of special rules concerning the treatment of certain specified transfers of property. Paragraph (b) addresses transfers of depreciated property previously used in the United States, while paragraph (c) concerns property that will be leased by the transferee. Paragraph (d) concerns property to be sold by the transferee. Paragraph (e) specifies the circumstances in which oil and gas working interests will be considered to have been transferred for use in the active conduct of a trade or business. Paragraphs (f) and (g) provide exceptions from section 367(a) for transfers that are required by foreign governments and for transfers to FSCs.

Section 1.367(a)-5T provides rules concerning transfers of property that are subject to taxation by reason of section 367(a) regardless of whether the property will be used in the active conduct of a trade or business. These rules apply to transfers of inventory, installment obligations, foreign currency, intangible property, and leased property.

Section 1.367(a)-6T provides special rules relating to the incorporation of a foreign branch with previously deducted losses. Paragraph (b) provides generally that such losses must be recaptured by recognizing the gain realized on the transfer of the branch's assets. Paragraph (c) specifies the character of, and limitations on, the gain required to be recognized, while paragraphs (d) and (e) provide for adjustments to the amount of losses subject to recapture. Paragraph (f) provides an example. Finally, paragraph (g) defines the term "foreign branch."

Section 1.367(d)-1T provides rules under section 367(d) concerning transfers of intangible property by U.S. persons to foreign corporations. Paragraph (b) specifies the transfers that are subject to section 367(d), while paragraph (c) provides rules concerning the consequences of such a transfer. In general, the U.S. transferor will be treated as receiving payments contingent on productivity or use of the transferred property, over the useful life of the property (regardless of whether such payments are in fact made by the transferee). Under a special transitional rule contained in §1.367(a)-1T(d)(3)(iv), certain foreign marketing intangibles developed by a foreign branch and transferred prior to May 16, 1986 will not be subject to the rules of section 367(d). Transfers of such marketing intangibles made on or after that date are subject to the section 367(d) rules. Paragraphs (d), (e), and (f) provide rules for cases in which there is a later direct or indirect disposition of the intangible property transferred. In general, deemed license payments will continue if a transfer is made to a related person, while gain must be recognized immediately if the transfer is to be an unrelated person. Paragraph (g) provides several special rules, including a rule allowing appropriate adjustments where deemed payments under section 367(d) are not in effect received by the U.S. transferor of the intangible property, and a rule providing for a limited election to treat certain transfers of intangible property as sales at fair market value (in lieu of applying the general useful life-contingent payment rule). In addition, paragraph (g) provides rules coordinating the application of section 367(d) with other relevant Code sections. Finally, paragraph (h) defines the term "related person" for purposes of section 367(d).

Section 1.6038B-1T provides rules concerning the information that is required to be reported under section 6038B with respect to transfers of property to foreign corporations. Paragraph (b) of the section explains when and how to report under section 6038B. Paragraphs (c) and (d) specify the information that is required to be reported with respect to transfers of property described in section 367(a) and (d), respectively. Paragraph (e) is reserved to specify the information required to be reported with respect to transfers subject to section 367(e). Finally, paragraph (f) sets forth the consequences of a failure to comply with the requirements of section 6038B.

The temporary regulations do not provide rules concerning new section 367(e). When such regulations are issued, they will apply only on a prospective basis. The temporary regulations do, however, describe the situations in which section 367(a) will apply to corporate liquidations under section 332.

NONAPPICABILITY OF EXECUTIVE ORDER 12291

The Treasury Department has determined that these temporary regulations are not subject to Executive Order 12291. Accordingly, a Regulatory Impact analysis is not required.

REGULATORY FLEXIBILITY ACT

A general notice of proposed rulemaking is not required by 5 U.S.C. 553(b) for temporary regulations. Accordingly, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply and no Regulatory Flexibility Analysis is required for this rule.

PAPERWORK REDUCTION ACT

These regulations were submitted to The Office of Management and budget for review under the Paperwork Reduction Act and approved under OMB number 1545-0026.

DRAFTING INFORMATION

The principal authors of these regulations are Charles W. Culmer of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, and Robert E. Culbertson, Jr., of the Office of the Associate Chief Counsel (International), Internal Revenue Service. Personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations.

* * * * *

Adoption of amendments to the regulations.

Accordingly, 26 CFR Part 1, Part 7, and Part 602 are amended as follows:

INCOME TAX REGULATIONS

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 USC 7805. * * * Sections 1.367(a)-1T through 1.367(a)-7T also issued under 26 USC 367(a). Section 1.367(d)-1T also issued under 26

USC 367(d). Section 1.6038B-1T also issued under 26 USC 6038B.

Par. 2. Section 1.367(a)-1 is removed.

Par. 3. Section 1.367(a)-4T is redesignated as §1.367(a)-7T.

Par. 4. Sections 1.367(a)-1T through 1.367(a)-6T are added immediately after §1.362-2, to read as follows:

§1.367(a)-1T Transfers to foreign corporations subject to section 367(a): In general (temporary).

(a) *Purpose and scope of regulations.* These regulations set forth rules relating to the provisions of section 367(a) concerning certain transfers of property to foreign corporations. This §1.367(a)-1T provides general rules explaining the effect of section 367(a)(1) and describing the transfers of property that are subject to the rule of that section. Section 1.367(a)-2T provides rules concerning the exception from the rule of section 367(a)(1) for transfers of property to be used in the active conduct of a trade or business outside of the United States. Rules concerning the application of section 367(a)(1) to transfers of stock or securities are provided in §1.367(a)-3T, while §1.367(a)-4T provides special rules regarding other specified transfers of property. Section 1.367(a)-5T describes types of property that are subject to the rule of section 367(a)(1) regardless of whether they are transferred for use in a trade or business. Section 1.367(a)-6T provides rules concerning the application of section 367(a) to the transfer of a branch with previously deducted losses. Finally, §1.367(a)-7T contains transitional rules concerning transfers of intangible property to foreign corporations made after June 6, 1984 and before January 1, 1985. Rules explaining the operation of section 367(d), concerning transfers of intangible property pursuant to an exchange decribed in section 351 or 361, are provided in §1.367(d)-1T. Rules concerning the reporting requirements of section 6038B are provided in §1.6038B-1T.

(b) *General rules*—(1) *Foreign corporation not considered a corporation for purposes of certain transfers.* If a U.S. person transfers property to a foreign corporation in connection with an exchange described in section 332, 351, 354, 355, 356, or 361, then pursuant to section 367(a)(1) the foreign corporation shall not be considered to be a corporation for purposes of determining the extent to which gain shall be recognized on the transfer. Section 367(a)(1) denies nonrecognition treatment only to transfers of items of property on which gain is realized. Thus, the amount of gain recognized because of section 367(a)(1) is unaffected by the transfer of items of property on which loss is realized (but not recognized). The transfers of property that are subject to section 367(a)(1) are further described in paragraph (c) of this section, and relevant definitions are provided in paragraph (d) of this section.

(2) *Cases in which foreign corporate status is not disregarded.* Section 367(a)(1) shall not apply, and a foreign corporate transferee shall, thus, be considered to be a corporation, in the case of any of the following:

(i) The transfer of stock or securities of a foreign corporation which is a party to the exchange or reorganization (as defined in section 368(b));

(ii) The transfer of property for use in the active conduct of a trade or business outside of the United States in accordance with the rules of §§1.367(a)-2T through 1.367(a)-6T; or

(iii) Certain other transfers of property described in §§1.367(a)-2T through 1.367(a)-6T.

For the treatment of a transfer of stock or securities of a foreign corporation which is a party to the exchange or reorganization, see §§1.367(a)-3T(b)(1), 7.367(b)-4, and 7.367(b)-7.

(3) *Limitation of gain required to be recognized*—(i) *In general.* If a U.S. person transfers property to a foreign corporation in a transaction on which gain is required to be recognized under section 367(a) and regulations thereunder, then the gain required to be recognized by the U.S. person shall in no event exceed the gain that would have been recognized on a taxable sale of those items of property if sold individually and without offsetting individual losses against individual gains.

(ii) *Losses.* No loss may be recognized by reason of the operation of section 367.

(iii) *Ordinary income and capital gain.* If section 367(a) and regulations thereunder require the recognition of ordinary income and capital gain in excess of the limitation described in paragraph (b)(3)(i) of this section, then the limitation shall be imposed by making proportionate reductions in the amounts of ordinary income and capital gain, regardless of the character of the gain that would have been recognized on a taxable sale of the property.

(4) *Character, source, and adjustments*—(i) *In general.* If a U.S. person is required to recognize gain under section 367 upon a transfer of property to a foreign corporation, then—

(A) The character and source of such gain shall be determined as if the property had been disposed of in a taxable exchange with the transferee foreign corporation (unless otherwise provided by regulation); and

(B) Appropriate adjustments to earnings and profits, basis, and other affected items shall be made according to otherwise applicable rules, taking into account the gain recognized because of section 367(a)(1). Any increase in the basis of the property received by the foreign corporation resulting from the application of section 367(a) and section 362(a) or (b) shall be allocated over the transferred property with respect to which gain is recognized in proportion to the amount realized by the U.S. person on the transfer of each item of that property. See paragraph (c)(3) of this section for special rules applicable to transfers of partnership interests.

(ii) *Example.* The rules of this paragraph (b)(4) are illustrated by the following example.

Example. Domestic corporation DC transfers inventory with a fair market value of $1 million and adjusted basis of $800,000 to foreign corporation FC in an exchange for stock of FC that is described in section 351(a). Title passes within the U.S. Pursuant to section 367(a), DC is required to recognize gain of $200,000 upon the transfer. Under the rule of this paragraph (b)(4), such gain shall be treated as ordinary income (sections 1201 and 1221) from sources within the U.S. (section 861) arising from a taxable exchange with FC. Appropriate adjustments to earnings and profits, basis, etc., shall be made as if the transfer were subject to section 351. Thus, for example, DC's basis in the FC stock received, and FC's basis in the transferred inventory, will each be increased by the $200,000 gain recognized by DC, pursuant to section 358(a)(1) and 362(a), respectively.

(c) *Transfers described in section 367(a)(1)*—(1) *In general.* A transfer described in section 367(a)(1) is any transfer of property by a U.S. person to a foreign corporation pursuant to an exchange described in section 332, 351, 354, 355, 356, or 361. Section 367(a)(1) applies to such a transfer whether it is made directly, indirectly, or constructively. Indirect or constructive transfers that are described in section 367(a)(1) include the transfers described in subparagraphs (2) through (7) of this paragraph (c). See §1.367(a)-3T(b)(1) for rules relating to the transfer of stock or securities of a foreign corporation that is a party to the exchange or the reorganization.

(2) *Indirect transfers in certain reorganizations*—(i) *Mergers described in section 368(a)(1)(A)*—(A) *In general.* A transfer in connection with a reorganization described in section 368(a)(1)(A) to which either section 368(a)(2)(D) or (E) applies may be an indirect transfer described in section 367(a)(1) if the reorganization involves the merger of two domestic corporations and if stock of a foreign corporation which controls one of such domestic corporations is exchanged in the reorganization. The transfers in connection with such a reorganization that are described in section 367(a)(1) are specified in subdivisions (B) and (C) of this paragraph (c)(2)(i). If a transfer in connection with such a reorganization is described in section 367(a)(1), then the rules of §1.367(a)-3T shall apply to determine whether the U.S. transferor is required to recognize gain with respect to the transfer.

(B) *Mergers to which section 368(a)(2)(D) applies.* A U.S. shareholder of a domestic corporation shall be considered to make a transfer of stock that is described in section 367(a)(1) if—

(1) The domestic corporation transfers substantially all of its properties to another domestic corporation in connection with a reorganization described in section 368(a)(1)(A) to which section 368(a)(2)(D) applies; and

(2) The controlling corporation (within the meaning of section 368(a)(2)(D)) is a foreign corporation.

The indirect transfer of stock by the shareholder shall be subject to the provisions of §1.367(a)-3T.

Example. F, a foreign corporation, owns all the stock of S, a domestic corporation. In a reorganization described in section 368(a)(1)(A) to which section 368(a)(2)(D) applies, S acquires substantially all the properties of W, a domestic corporation, in a merger of W into S. The stock of F is used as consideration. The reorganization is considered to constitute a transfer of stock described in section 367(a)(1) by the shareholders of W that are U.S. persons.

(C) *Mergers described in section 368(a)(1)(A) to which section 368(a)(2)(E) applies.* A shareholder of a domestic corporation that is a U.S. person shall be considered to make a transfer of stock that is described in section 367(a)(1) if—

(1) The domestic corporation acquires substantially all of the properties of another domestic corporation in connection with a reorganization described in section 368(a)(1)(A) to which section 368(a)(2)(E) applies; and

(2) The controlling corporation (within the meaning of section 368(a)(2)(E)) is a foreign corporation.

The indirect transfer of stock by the shareholder shall be subject to the provisions of §1.367(a)-3T.

(ii) *Reorganizations described in section 368(a)(1)(B).* If, in connection with a reorganization described in section 368(a)(1)(B), a U.S. person exchanges stock of a domestic corporation for voting stock of a foreign corporation that is in control (as defined in section 368(c)) of the domestic acquiring corporation, then that U.S. person is considered to make a transfer of stock that is subject to section 367(a)(1). The rule of this paragraph (c)(2)(ii) is illustrated by the following example.

Example. F, a foreign corporation, owns all the stock of S, a domestic corporation. In a reorganization described in section 368(a)(1)(B), S acquires all the stock of domestic corporation Y, and the shareholders of Y receive voting stock of F. The reorganizaiton includes an indirect stock transfer described in section 367(a)(1) by those shareholders of Y who are U.S. persons.

(iii) *Reorganizations described in section 368(a)(1)(C).* A U.S. shareholder of a domestic corporation shall be considered to make a transfer of stock that is subject to section 367(a)(1) if—

(A) The domestic corporation transfers substantially all of its properties to another domestic corporation in connection with a reorganization described in section 368(a)(1)(C); and

(B) The domestic corporation receives voting stock in a foreign corporation that is in control (as defined in section 368(c)) of the acquiring corporation (and distributes the stock to its shareholders in accordance with section 368(a)(2)(G)).

The rule of this paragraph (c)(2)(iii) is illustrated by the following example.

Example. F, a foreign corporation, owns all the stock of S, a domestic corporation. In a reorganization described in section 368(a)(1)(C), S acquires substantially all of the properties of Z, a domestic corporation, and Z receives voting stock of F (and distributes the stock to its shareholders). The reorganization is considered in section 367(a)(1) by the shareholders of Z that are U.S. persons.

(3) *Indirect transfers involving partnerships and interests therein*—(i) *Transfer by partnership treated as transfers by partners*—(A) *In general.* If a partnership (whether foreign or domestic) transfers property to a foreign corporation in an exchange described in section 367(a)(1), then a U.S. person that is a partner in the partnership shall be treated as having transferred a proportionate share of the property in an exchange described in section 367(a)(1). A U.S. person's proportionate share of partnership property shall be determined under the rules and principles of section 701 through 761 and the regulations thereunder. The rule of this paragraph (c)(3)(i)(A) is illustrated by the following example.

Example. P is a partnership having five equal general partners, two of whom are United States persons. P transfers property to F, a foreign corporation, in connection with an exchange described in section 351. The exchange includes an indirect transfer of property by the partners to F. The transfers of property attributable to those partners who are United States persons, that is, 40 percent of each asset transferred to F, are transfers described in section 367(a)(1). The gain (if any) recognized on the transfer of 40 percent of each asset to F is attributable to the two partners who are United States persons.

(b) *Special adjustments to basis.* If a U.S. person is treated under the rule of this paragraph (c)(3)(i) as having transferred a proportionate share of the property of a partnership in an exchange described in section 367(a), and is therefore required to recognize gain upon the transfer, then—

(1) The U.S. person's basis in the partnership shall be increased by the amount of gain recognized by him;

(2) Solely for purposes of determining the basis of the partnership in the stock of the transferee foreign corporation, the U.S. person shall be treated as having newly acquired an interest in the partnership (for an amount equal to the

gain recognized), permitting the partnership to make an optional adjustment to basis pursuant to sections 743 and 754; and

(3) The transferee foreign corporation's basis in the property acquired from the partnership shall be increased by the amount of gain recognized by U.S. persons under this paragraph (c)(3)(i).

(ii) *Transfer of partnership interest treated as transfer of proportionate share of assets*—(A) *In general.* If a U.S. person transfers an interest as a partner in a partnership (whether foreign or domestic) in an exchange described in section 367(a)(1), then that person shall be treated as having transferred a proportionate share of the property of the partnership in an exchange described in section 367(a)(1). Accordingly, the applicability of the exception to section 367(a)(1) provided in §1.367(a)-2T shall be determined with reference to the property of the partnership rather than the partnership interest itself. A U.S. person's porportionate share of partnership shall be determined under the rules and principles of sections 701 through 761 and the regulations thereunder.

(B) *Special adjustments to basis.* If a U.S. person is treated under the rule of paragraph (c)(3)(ii)(A) of this section as having transferred a proportionate share of the property of a partnership in an exchange described in section 367(a), and is therefore required to recognize gain upon the transfer, then—

(1) The U.S. person's basis in the stock of the transferee foreign corporation shall be increased by the amount of gain so recognized by that person;

(2) The transferee foreign corporation's basis in the transferred partnership interest shall be increased by the amount of gain recognized by the U.S. person; and

(3) Solely for purposes of determining the partnership's basis in the property held by it, the U.S. person shall be treated as having newly acquired an interest in the partnership (for an amount equal to the gain recognized), permitting the partnership to make an optional adjustment to basis pursuant to sections 743 and 754.

(c) *Limited partnership interest.* The transfer by a U.S. person of an interest in a partnership shall not be subject to the rules of paragraph (c)(3)(ii)(A) and (B) if—

(1) The interest transferred to a limited partnership interest; and

(2) Such interest is regularly traded on an established securities market.

Instead, the transfer of such an interest shall be treated in the same manner as a transfer of stock or securities. Thus, the consequences of such a transfer shall be determined under the rules of §1.367(a)-3T. For purposes of this section, a limited partnership interest is an interest as a limited partner in a partnership that is organized under the laws of any State of the United States or the District of Columbia. Whether such an interest is regularly traded on an established securities market shall be determined under the provisions of paragraph (c)(3)(ii)(D) of this section.

(D) *Regularly traded on an established securities market—(1) Established securities market.* For purposes of this paragraph (c)(3)(ii), an established securities market is—

(i) A national securities exchange which is registered under section 6 of the Securities Exchange Act of 1934 (15 USC 78f);

(ii) A foreign national securities exchange which is officially recognized, sanctioned, or supervised by governmental authority; and

(iii) An over-the-counter market. An over-the-counter market is any market reflected by the existence of an interdealer quotation system. An interdealer quotation system is any system of general circulation to brokers and dealers which regularly disseminates quotations of stock and securities by identified brokers or dealers, other than by quotation sheets which are prepared and distributed by a broker or dealer in the regular course of business and which contain only quotations of such broker or dealer.

(2) Regularly traded. A class of interest that is traded on an established securities market is considered to be regularly traded if it is regularly quoted by brokers or dealers making a market in such interests. A class of interests shall be presumed to be regularly traded if the entity has a total of 500 or more interest-holders.

(4) *Transfers by trusts and estates*—(i) *In general.* For purposes of section 367(a), a transfer of property by an estate or trust shall be treated as a transfer by the entity itself and not as an indirect transfer by its beneficiaries. Thus, a transfer of property by a foreign trust or estate (as defined in section 7701(a)(31)) is not described in section 367(a)(1), regardless of whether the beneficiaries of the trust or estate are U.S. persons. Similarly, a transfer of property by a domestic trust or estate may be described in section 367(a)(1), regardless of whether the beneficiaries of the trust or estate are foreign persons.

(ii) *Grantor trusts.* A transfer of a portion or all of the assets of a foreign or domestic trust to a foreign corporation in an exchange described in section 367(a)(1) is considered a transfer by any U.S. person who is treated as the owner of any such portion of all of the assets of the trust under sections 671 through 679.

(5) *Termination of election under section 1504(d).* Section 367(a) applies to the constructive reorganization and transfer of property from a domestic corporation to a foreign corporation that occurs upon the termination of an election under section 1504(d), which permits the treatment of certain contiguous country corporations as domestic corporations. The rule of this paragraph (c)(5) is illustrated by the following example.

Example. Domestic corporation Y previously made a valid election under section 1504(d) to have its wholly owned Canadian subsidiary, C, treated as a domestic corporation. On July 1, 1986, C fails to continue to qualify for the election under section 1504(d). A constructive reorganization described in section 368(a)(1)(D) occurs. The resulting constructive transfer of assets by "domestic" corporation C to Canadian corporation C upon the termination of the election is a transfer of property described in section 367(a)(1).

(6) *Changes in classification of an entity.* If a foreign entity is classified as an entity other than an association taxable as a corporation for United States tax purposes, and subsequently a change is made in the governing documents, articles, or agreements of the entity so that the entity is thereafter classified as an association taxable as a corporation, the change in classification is considered a transfer of property to a foreign corporation in connection with an exchange described in section 351. For purposes of section 367(a)(1), the transfer of property is considered as made by the persons determined under the rules set forth in paragraph (c)(3) of this section, with respect to partner-

ships, and paragraph (c)(4)(i) or (ii), with respect to trusts and estates, and the rules of such paragraphs apply in determining whether a transfer described in section 367(a)(1) has been made.

(7) *Contributions to capital.* For rules with respect to the treatment of a contribution to the capital of a foreign corporation as a transfer described in section 367(a)(1), see section 367(c)(2) and the regulations thereunder.

(d) *Definitions.* The following definitions apply for purposes of this section and §1.367(d)-1T.

(1) *United States person.* The term "United States person" includes those persons described in section 7701(a)(30). The term includes a citizen or resident of the United States, a domestic partnership, a domestic corporation, and any estate or trust other than a foreign estate or trust. (For definitions of these terms, see section 7701 and regulations thereunder.) For purposes of this section, an individual with respect to whom an election has been made under section 6013(g) or (h) is considered to be a resident of the United States while such election is in effect. A nonresident alien or a foreign corporation will not be considered a United States person because of its actual or deemed conduct of trade or business within the United States during a taxable year.

(2) *Foreign corporation.* The term "foreign corporation" has the meaning set forth in section 7701(a)(3) and (5) and §301.7701-5.

(3) *Transfer.* For purposes of section 367 and regulations thereunder, the term "transfer" means any transaction that constitutes a transfer for purposes of section 332, 351, 354, 355, 356, or 361, as applicable. A person's entering into a bona fide cost-sharing arrangement under §1.482-2(d)(4) or acquiring rights to intangible property under such an arrangement shall not be considered a transfer of property described in section 367(a)(1). See §1.6038B-1T(b)(3) for the date on which the transfer is considered to be made.

(4) *Property.* For purposes of section 367 and regulations thereunder, the term "property" means any item that constitutes property for purposes of section 332, 351, 354, 355, 356, or 361, as applicable.

(5) *Intangible property*—(i) *In general.* For purposes of section 367 and regulations thereunder, the term "intangible property" means knowledge, rights, documents, and any other intangible item within the meaning of section 936(h)(3)(B) that constitutes property for purposes of section 332, 351, 354, 355, 356, or 361, as applicable. Such property shall be treated as intangible property for purposes of section 367(a) and (d) and the regulations thereunder without regard to whether it is used or developed in the United States or in a foreign country and without regard to whether it is used in manufacturing activities or in marketing activities. A working interest in oil and gas properties shall not be considered to be intangible property for purposes of section 367 and the regulations thereunder.

(ii) *Operating intangibles.* An operating intangible is any intangible property of a type not ordinarily licensed or otherwise transferred in transactions between unrelated parties for consideration contingent upon the licensee's or transferee's use of the property. Examples of operating intangibles may include long-term purchase or supply contracts, surveys, studies; and customer lists.

(iii) *Foreign goodwill or going concern value.* Foreign goodwill or going concern value is the residual value of a business operation conducted outside of the United States after all other tangible and intangible assets have been identified and valued. For purposes of section 367 and regulations thereunder, the value of the right to use a corporate name in a foreign country shall be treated as foreign goodwill or going concern value.

(iv) *Transitional rule for certain marketing intangibles.* For transfers occurring after December 31, 1984, and before May 16, 1986, foreign trademarks, tradenames, brandnames, and similar marketing intangibles developed by a foreign branch shall be treated as foreign goodwill or going concern value.

(e) *Effective date of certain sections*—(1) *In general.* Except as specifically provided to the contrary elsewhere in these sections, §§1.367(a)-1T through 1.367(a)-6T apply to transfers occurring after December 31, 1984.

(2) *Private rulings.* The taxpayer may rely on a private ruling under section 367(a) received by him before June 16, 1986.

(3) *Certain indirect transfers.* Sections 1.367(a)-1T(c)(2)(i) and (iii) and 1.367(a)-1T(c)(3) apply to transfers made after June 16, 1986. For transfers made before that date, see 26 CFR §1.367(a)-1(b) (revised as of April 1, 1986).

§1.367(a)-2T Exception for transfers of property for use in the active conduct of a trade or business (temporary).

(a) *In general.* Section 367(a)(1) shall not apply to property transferred to a foreign corporation if—

(1) Such property is transferred for use by that corporation in the active conduct of a trade or business outside of the United States; and

(2) The U.S. person that transfers the property complies with the reporting requirements of section 6038B and regulations thereunder.

Where there conditions are satisfied, the foreign corporate transferee of the property shall be considered to be a corporation for purposes of determining the extent to which gain or loss is required to be recognized upon the transfer pursuant to section 332, 351, 354 [reserved as to section 355 or so much of section 356 as relates to section 355], 356, or 361. Paragraph (b) of this section provides rules concerning the requirement that property be transferred for use in the active conduct of a trade or business outside of the United States, while paragraph (c) concerns the application of the requirement where the transferee itself re-transfers the property. In addition, §1.367(a)-3T provides rules concerning the treatment of stock or securities transferred to a foreign corporation in an exchange described in section 367(a)(1), and §1.367(a)-4T provides special rules concerning the treatment of other specified types of property. Finally, §§1.367(a)-5T and 1.367(a)-6T provide rules concerning certain transfers of property that are subject to section 367(a)(1) regardless of whether the property is used in the active conduct of a trade or business.

(b) *Active conduct of a trade or business outside the United States*—(1) *In general.* Property qualifies for the exception provided by this section if it is transferred to a foreign corporation for use in the active conduct of a trade or business outside of the United States. Therefore, to determine whether property is subject to the exception provided by this section, four factual determinations must be made:

(i) What is the trade or business of the transferee;

(ii) Do the activities of the transferee constitute the active conduct of that trade or business;

(iii) Is the trade or business conducted outside of the United States; and

(iv) Is the transferred property used or held for use in the trade or business?

Rules concerning these four determinations are provided in paragraph (b)(2), (3), (4), and (5) of this section.

(2) *Trade or business.* Whether the activities of a foreign corporation constitute a trade or business must be determined under all the facts and circumstances. In general, a trade or business is a specific unified group of activities that constitute (or could constitute) an independent economic enterprise carried on for profit. For example, the activities of a foreign selling subsidiary could constitute a trade or business if they could be independently carried on for profit, even though the subsidiary acts exclusively on behalf of, and has operations fully integrated with, its parent corporation. To constitute a trade or business, a group of activities must ordinarily include every operation which forms a part of, or a step in, a process by which an enterprise may earn income or profit. In this regard, one or more of such activities may be carried on by independent contractors under the direct control of the foreign corporation. (However, see paragraph (b)(3) of this section.) The group of activities must ordinarily include the collection of income and the payment of expenses. If the activities of a foreign corporation do not constitute a trade or business, then the exception provided by this section does not apply, regardless of the level of activities carried on by the corporation. The following activities are not considered to constitute by themselves a trade or business for purposes of this section:

(i) Any activity giving rise to expenses that would be deductible only under section 212 if the activities were carried on by an individual; or

(ii) The holding for one's own account of investments in stock, securities, land, or other property, including casual sales thereof.

(3) *Active conduct.* Whether a trade or business is actively conducted must be determined under all the facts and circumstances. In general, a corporation actively conducts a trade or business only if the officers and employees of the corporation carry out substantial managerial and operational activities. A corporation may be engaged in the active conduct of a trade or business even though incidental activities of the trade or business are carried out on behalf of the corporation by independent contractors. In determining whether the officers and employees of the corporation carry out substantial managerial and operational activities, however, the activities of independent contractors shall be disregarded. On the other hand, the officers and employees of the corporation are considered to include the officers and employees of related entities who are made available to and supervised on a day-to-day basis by, and whose salaries are paid by (or reimbursed to the lending related entity by), the transferee foreign corporation. Whether a trade or business that produces rents or royalties is actively conducted shall be determined under the principles of §1.954-2(d)(1) (but without regard to whether the rents or royalties are received from an unrelated person). The rule of this paragraph (b)(3) is illustrated by the following example.

Example. X, a domestic corporation, and Y, a foreign corporation not related to X, transfer property to Z, a newly formed foreign corporation organized for the purpose of combining the research activities of X and Y. Z contracts all of its operational and research activities to Y for an arm's-length fee. Z's activities do not constitute the active conduct of a trade or business.

(4) *Outside of the United States.* Whether a foreign corporation conducts a trade or business outside of the United States must be determined under all the facts and circumstances. Generally, the primary managerial and operational activities of the trade or business must be conducted outside the United States and immediately after the transfer the transferred assets must be located outside the United States. Thus, the exception provided by this section would not apply to the transfer of the assets of a domestic business to a foreign corporation if the domestic business continued to operate in the United States after the transfer. In such a case, the primary operational activities of the business would continue to be conducted in the United States. Moreover, the transferred assets would be located in the United States. However, it is not necessary that every item of property transferred be used outside of the United States. As long as the primary managerial and operational activities of the trade or business are conducted outside of the United States and substantially all of the transferred assets are located outside the United States, incidental items of transferred property located in the United States may be considered to have been transferred for use in the active conduct of a trade or business outside of the United States.

(5) *Use in the trade or business.* Whether property is used or held for use in a trade or business must be determined under all the facts and circumstances. In general, property is used or held for use in a foreign corporation's trade or business if it is—

(i) Held for the principal purpose of promoting the present conduct of the trade or business;

(ii) Acquired and held in the ordinary course of the trade or business; or

(iii) Otherwise held in a direct relationship to the trade or business. Property is considered held in a direct relationship to a trade or business if it is held to meet the present needs of that trade or business and not its anticipated future needs.

Thus, property will not be considered to be held in a direct relationship to a trade or business if it is held for the purpose of providing for future diversification into a new trade or business, future expansion of trade or business activities, future plant replacement, or future business contingencies.

(c) *Property transferred by transferee corporation*—(1) *General rule.* If a foreign corporation receives property in an exchange described in section 367(a)(1) and as part of the same transaction transfers the property to another person, then the exception provided by this section shall not apply to the initial transfer. For purposes of the preceding sentence, a subsequent transfer within six months of the initial transfer shall be considered to be part of the same transaction, and a subsequent transfer more than six months after the initial transfer may be considered to be part of the same transaction upon the application of step-transaction principles.

(2) *Exception.* Notwithstanding paragraph (e)(1) of this section, the active conduct exception provided by this section shall apply to the initial transfer if—

(i) The initial transfer is followed by one or more subsequent transfers described in section 351 or 721; and

(ii) Each subsequent transferee is either a partnership in which the preceding transferor is a general partner or a corporation in which the preceding transferor owns common stock; and

(iii) The ultimate transferee uses the property in the active conduct of a trade or business outside the United States.

(d) *Transitional rule.* Notwithstanding any other provision of this section, property shall be considered to have been transferred for use in the active conduct of a trade or business outside of the United States, if—

(1) The property was transferred after December 31, 1984, and before June 16, 1986;

(2) The property was, or would have been, considered to be transferred for use by the transferee foreign corporation in the active conduct, in any foreign country, of a trade or business, under the principles of section 3.02(1) of Revenue Procedure 68-23, 1968-1 C.B. 821; and

(3) Based on all of the facts and circumstances, it was, or would have been, determined under section 2.02 of Revenue Procedure 68-23 that tax avoidance was not one of the principal purposes of the transaction.

§1.367(a)-3T Treatment of transfers of stock or securities to foreign corporations (temporary).

(a) *In general.* This section provides rules concerning the transfer of stock or securities to a foreign corporation in an exchange described in section 367(a)(1). In general, a transfer of stock or securities by a U.S. person to a foreign corporation in connection with any exchange described in section 332, 351, 354 [reserved as to section 355 and so much of section 356 as relates to section 355], 356, or 361, is subject to section 367(a)(1) (and, therefore, treated as a taxable exchange) unless one of the exceptions set forth in this section applies to the transfer. Paragraph (b) of this section specifies certain transactions that are not subject to section 367(a)(1), while paragraph (c) provides rules concerning the treatment of transfers of stock or securities of domestic corporations pursuant to any exchange described in section 367(a)(1). Paragraph (d) of this section provides rules concerning the transfer of stock of a foreign corporation to another foreign corporation pursuant to section 332 or 351 [reserved as to section 355 and so much of section 356 as relates to section 355]. Finally, paragraphs (e), (f), and (g) provide detailed rules applicable to certain transfers described above and paragraph (h) sets forth anti-abuse rules.

(b) *Transfer to which section 367(a)(1) does not apply*—(1) *Transfers in certain reorganizations of stock or securities of foreign corporations.* If, pursuant to an exchange described in section 354, 361, or so much of section 356 as relates to section 354, a U.S. person transfers to a foreign corporation stock or securities of a foreign corporation that is a party to the reorganization, then section 367(a) shall not apply to the transfer, by reason of the operation of section 367(a)(2) and §1.367(a)-1T(b)(2)(i). Thus, section 367(a)(1) shall not apply to a transfer of stock of a foreign corporation by a United States person to another foreign corporation pursuant to a reorganization described in section 368(a)(1)(B) because the foreign corporation whose stock is transferred is a party to the reorganization. This result follows even though that foreign corporation may not be a party to other types of reorganizations or exchanges for which the transaction also qualifies. For rules concerning the treatment of certain transfers that are described in section 351 as well as one of the above-cited sections, see §§7.367(b)-4 and 7.367(b)-7.

(2) *Compulsory transfers.* For rules regarding a transfer of property (including stock or securities) that is compelled by foreign government action, see §1.367(a)-4T(f).

(c) *Transfer of stock or securities of domestic corporation*—(1) *In general.* The transfer of stock or securities of a domestic corporation to a foreign corporation (in an exchange described in section 367(a)(1)) shall be subject to section 367(a)(1) and shall therefore be treated as a taxable exchange, except in the circumstances set forth in paragraphs (c)(2), (3), (4), (5), and (6) of this section.

(2) *Active conduct of a trade or business.* Section 367(a)(1) shall not apply to a transfer of stock or securities of a domestic corporation if (i) the transfer is described in paragraph (e)(2) of this section (ii) the transferor files an agreement to recognize gain upon the transferee's later disposition of the transferred interest in accordance with the provisions of paragraph (g) of this section. In general, paragraph (e)(2) of this section describes certain transfers of stock or securities for use by the transferee in the active conduct of a trade or business outside of the United States.

(3) *U.S. transferors obtain limited interest in transferee.* Section 367(a)(1) shall not apply to a transfer of stock or securities of a domestic corporation if the transfer is described in paragraph (f) of this section. In general, paragraph (f) of this section describes transfers in which the U.S. transferors of stock or securities obtain only a limited interest in the transferee foreign corporation.

(4) *Transferor files agreement to recognize gain upon later disposition.* Section 367(a)(1) shall not apply to a transfer of stock or securities of a domestic corporation if (i) immediately after the transfer all U.S. transferors own in the aggregate less than fifty percent of both the total voting power and the total value of the stock of the transferee foreign corporation and (ii) the subject transferor files an agreement to recognize gain upon the transferee's later disposition of the transferred interest in accordance with the provisions of paragraph (g) of this section.

(5) *Certain transfers in connection with performance of services.* Section 367(a)(1) shall not apply to a domestic corporation's transfer of its own stock or securities in connection with the performance of services, if the transfer is considered to be to a foreign corporation solely by reason of §1.83-6(d)(1).

(6) *Transfers pursuant to section 355 or so much of section 356 as relates to section 355.* [Reserved.]

(d) *Transfer of stock or securities of foreign corporation pursuant to section 332 or 351 [reserved as to section 355 and so much of section 356 as relates to section 355]*—(1) *In general.* If a

U.S. person transfers stock or securities of a foreign corporation to another foreign corporation in an exchange described in section 332 or 351 [reserved as to section 355 or so much of section 356 as relates to section 355] then section 367(a)(1) shall apply to the transfer (which is therefore treated as a taxable exchange), except in the circumstances set forth in paragraph (d)(2), (3), (4), (5), and (6) of this section. Transfers described in section 351 that are also described in section 368(a)(1)(B) shall be subject to the rules set forth in §§7.367(b)-4 and 7.367(b)-7 and shall not be subject to the rules of this paragraph (d).

(2) *Active conduct of a trade or business.* Section 367(a)(1) shall not apply to a transfer of stock or securities of a foreign corporation if (i) the transfer is described in paragraph (e)(2) or (3) of this section and (ii) the transferor files an agreement to recognized gain upon the transferee's later disposition of the transferred interest in accordance with the provisions of paragraph (g) of this section. In general, paragraph (e) describes transfers of stock or securities for use by the transferee corporation in the active conduct of a trade or business outside of the United States.

(3) *Transfer of stock or securities of foreign corporation to another corporation organized in same country.* Section 367(a)(1) shall not apply to a transfer of stock or securities of a foreign corporation if—

(i) The transferred corporation and the transferee corporation are created or organized under the laws of the same foreign country;

(ii) At least 50 percent of the assets used in the trade or business of the transferred corporation are located in that same foreign country;

(iii) Prior to the transfer, more than 50 percent of the total combined voting power of all classes of stock entitled to vote of the transferred corporation was held by U.S. persons;

(iv) After the transfer, the transferee corporation holds more than 50 percent of the total combined voting power of all classes of stock entitled to vote of the transferred corporation;

(v) After the transfer, the U.S. persons that controlled the transferred corporation before the transfer hold at least 50 percent of the total combined voting power of all classes of stock entitled to vote of the transferee corporation;

(vi) After the transfer, the transferee corporation is a controlled foreign corporation within the meaning of section 957(a); and

(vii) The transferor files an agreement to recognize gain upon the transferee's later disposition of the transferred interest in accordance with the provisions of paragraph (g) of this section.

The provisions of this paragraph (d)(3) shall apply to transfers occurring after June 16, 1986. For other transfers, see section 3.02(1)(a)(iii)(B) of Revenue Procedure 68-23.

(4) *U.S. transferors obtain limited interest in transferee.* Section 367(a)(1) shall not apply to a transfer of stock or securities of a foreign corporation if the transfer is described in paragraph (f) of this section. In general, paragraph (f) of this section describes transfers in which the U.S. transferors of stock or securities obtain only a limited interest in the transferee foreign corporation.

(5) *Transferor files agreement to recognize gain upon later disposition.* Section 367(a)(1) shall not apply to a transfer of stock or securities of a foreign corporation if (i) immediately after the transfer all U.S. transferors own in the aggregate less than fifty percent of both the total voting power and the total value of the stock of the transferee foreign corportion and (ii) the subject transferor files and agreement to recognize gain upon the transferee's later disposition of the transferred interest in accordance with the provisions of paragraph (g) of this section.

(6) *Transfer pursuant to section 355 or so much of section 356 as relates to section 355.* [Reserved.]

(e) *Transfer for use in the active conduct of a trade or business outside of the United States*—(1) *In general.* Section 367(a) shall not apply to a transfer of stock or securities of a corporation if (i) the transfer is described in paragraph (e)(2) or (3) of this section and (ii) the transferor files an agreement to recognize gain upon the transferee's later disposition of the transferred interest in accordance with the provisions of paragraph (g) of this section.

(2) *Stock contituting operating asset.* A transfer of stock or securities of a foreign or domestic corporation to a foreign corporation shall be considered to be for use in the active conduct of a trade or business outside of the United States if the stock or securities are essentially operating assets in the hands of the transferee because ownership of the stock or securities grants material rights to acquire for use in the transferor's trade or business outside the United States products produced by the transferred corporation outside the United States. See *Kaiser Aluminum Chemical Corp. v. Comm'r*, 76 T.C. 325 (1981).

(3) *Consolidation of integrated business*—(i) *In general.* A transfer of stock or securities of a foreign corporation to a foreign corporation shall be considered to be for use in the active conduct of a trade or business outside of the United States if—

(A) Immediately after the transfer, the transferee foreign corporation holds more than 50 percent of the total voting power and more than 50 percent of the total value of stock of the transferred corporation; and

(B) Both immediately before and immediately after the transfer, the transferred corporation and the transferee foreign corporation constitute an integrated business in accordance with the provisions of paragraph (e)(2)(ii) of this section.

(ii) *Integrated business.* For purposes of this paragraph (e)(2), the transferred and transferee corporations shall be considered to constitute an integrated business only if—

(A) Each corporation is engaged, directly or indirectly, in substantial business operations beyond the mere provision of general managerial, financial, or similar services to the other corporation; and

(B) Either the business operations of one corporation are substantially identical to all or the principal part of the operations of the other, or the operations of the two corporations constitute in principal part complementary and mutually interdependent steps in the production and sale or lease of a product or products or in the provision of a service. Substantial identity of business operations requires that the two corporations engage in substantially the same production (or service) and marketing processes or activities for generally the same or similar products (or services).

(f) *U.S. transferors obtain limited interest in transferee*—(1) *In general.*

A transfer of stock or securities of a foreign or domestic corporation by a U.S. person to a foreign corporation shall not be subject to section 367(a)(1) if immediately after the transfer—

(i) All U.S. transferors own in the aggregate less than twenty percent of both the total voting power and the total value of the stock of the transferee foreign corporation; or

(ii) (A) All U.S. transferors own in the aggregate twenty percent or more of either the total voting power or the total value of the stock of the transferee foreign corporation, but less than fifty percent of that total voting power and that total value; and

(B) The subject U.S. transferor owns less than five percent of both the total voting power and the total value of the stock of the transferee foreign corporation.

(2) *Attribution.* Section 958 shall apply in determining the ownership of stock for purposes of this paragraph (f).

(3) *Rule not applicable to stock of holding companies.* The rule of paragraph (f)(1) of this section shall not apply if the assets of the transferred corporation consist principally of stock or securities held as portfolio investments. Stock or securities of a given entity held by the transferred corporation shall be presumed not to constitute a portfolio investment if the transferred corporation holds ten percent or more by value of the outstanding stock and securities of that entity. This presumption may be rebutted by evidence that the stock was held by the transferred corporation as a passive, portfolio investment.

(g) *Transferor's agreement to recognize gain upon later disposition by transferee*—(1) *In general.* A transfer of stock or securities shall not be subject to section 367(a)(1) if—

(i) The transferor complies with the reporting requirements of section 6038B and any regulations thereunder;

(ii) The transferor files a binding agreement to recognize gain upon the transferee corporation's later disposition of the transferred stock or securities, in accordance with the rules of this section; and

(iii) The transfer is described in paragraph (d)(3) or (e) of this section or, immediately after the transfer, all U.S. transferors own in the aggregate less than 50 percent of both the total voting power and the total value of the stock of the transferee foreign corporation.

(2) *Agreement to recognize gain: in general.* A transferor's agreement to recognize gain must be attached to, and filed by the due date of, the information return required under section 6038B. In general, the return must be filed with the transferor's tax return for the taxable year that includes the date of the transfer. However, pursuant to §1.6038B-1T(b)(1), returns with respect to transfers that took place prior to June 16, 1986 are not required to be filed until September 16, 1986. Therefore, an agreement to recognize gain under the rules of this section with respect to any such transfer may be timely filed until that date. The agreement must be signed under penalties of perjury by a trustee, executor, or equivalent fiduciary in the case of a trust or estate, by a responsible officer in the case of a corporation, by a debtor in possession or trustee in a bankruptcy case under Title 11, United States Code, and in the case of an individual, including a partner who is treated as a transferor by virtue of §1.367(a)-1T(c)(3), by the individual himself. An agreement may also be signed by an agent authorized to do so under a general or specific power of attorney. The agreement must set forth the following materials, preferably in paragraphs labeled to correspond with the subparagraphs set forth below:

(i) A statement that the document submitted constitutes the transferor's agreement to recognize gain, in accordance with the requirements of §1.367(a)-3T(g);

(ii) A description of the stock or securities transferred, an estimate of fair market value as of the date of the transfer, and a statement of cost or other basis and any adjustments thereto;

(iii) The transferor's agreement to recognize gain, as described in subparagraph (3) of this paragraph (g);

(iv) A waiver of the period of limitations, as described in subparagraph (4) of this paragraph (g); and

(v) An agreement to file with the transferor's tax returns for the 5 years following the year of the transfer of certification and waiver as described in subparagraph (5) of this paragraph (g).

(3) *Terms of agreement*—(i) *Recognition of gain.* The transferor must agree that if, prior to the close of the fifth taxable year following the taxable year of the transfer, the transferee foreign corporation disposes of the transferred stock in any manner (other than in a liquidation of the transferred corporation), then by the 90th day thereafter the transferor will file an amended return for the year of the transfer and recognize thereon the gain realized but not recognized upon the initial transfer. Such gain shall be computed as if there had been a sale of the stock or securities at fair market value at the time of the initial transfer. Net operating losses or credits against tax that were available in the year of the initial transfer and that have expired unused may be applied (respectively) against any gain recognized or tax owned by reason of this provision, but no other adjustments shall be made with respect to any other items of income or deduction in the year of the transfer or other years. If additional tax is required to be paid, then interest must be paid on that amount at the rates determined under setion 6621, with respect to the period between the date that was prescribed for filing the transferor's income tax return for the year of the transfer and the date on which the additional tax for that year is paid. For special rules applicable to nonrecognition transfers, see subparagraph (7) of this paragraph (g). For special rules applicable when a U.S. transferor that enters into an agreement under this paragraph (g) ceases to exist, see subparagraph (9) of this paragraph (g).

(ii) *Partial disposition.* If the transferee foreign corporation disposes of only a portion of the stock or securities of the transferred corporation, then the U.S. transferor shall be required to recognize a proportionate amount of the gain realized but not recognized upon the initial transfer. The proportion required to be recognized shall be determined by reference to the fair market value of the stock or securities disposed of and the fair market value of those retained. The rule of this paragraph (g)(3)(ii) is illustrated by the following example.

Example. A is a U.S. citizen who owns 100 percent of the outstanding stock of foreign corporation X. In a transaction described in section 351, A exchanges his stock in X for 25 percent of the outstanding stock of foreign corporation Y. A submits an agreement under the rules of this section to recognize gain upon a later disposition. In the following year, Y disposes of 50 percent of the fair market value of the stock of X. Therefore, A is required to recognize 50 percent of the gain he realized but did not recognize upon the initial transfer of the shares of X.

(iii) *Disposition of assets by transferred corporation.* For purposes of paragraph (g)(3)(i) and (ii) of this section, a disposition not in the ordinary course of business by the transferred corporation of all or a substantial portion of its assets (other than a distribution, including a liquidating distribution, to the transferee foreign corporation) shall be treated as a disposition by the transferee foreign corporation of a proportionate amount of stock of the transferred corporation.

(iv) *Disposition of assets after distribution by transferred corporation.* For purposes of paragraph (g)(3)(i) and (ii) of this section, a disposition not in the ordinary course of business by the transferee foreign corporation of all or a substantial portion of the assets received by it in a distribution, including a liquidating distribution, from the transferred corporation shall be treated as a disposition by the transferee foreign corporation of a proportionate amount of stock of the transferred corporation.

(4) *Waiver of period of limitation.* The transferor must file a waiver of the period of limitation on assessment of tax upon the gain realized on the transfer. The waiver shall be executed on such forms as are prescribed therefor by the Commissioner and shall extend the period for assessment of such tax to a date not earlier than the close of the eighth taxable year following the taxable year of the transfer. Such waiver shall also contain such other terms with respect to assessment as may be considered by the Commissioner to be necessary to ensure the assessment and collection of the correct tax liability for each year for which the waiver is required. The waiver must be signed by a person authorized to sign the agreement pursuant to the provisions of paragraph (g)(2) of this section.

(5) *Annual certification and waiver*—(i) *Certification.* The transferor must agree to file with its income tax return for each of the five taxable years following the taxable year of the transfer a certification that the stock or securities transferred have not been disposed by the transferee in a transaction that is considered to be a disposition for purposes of the this paragraph. If either a disposition qualifying under paragraph (g)(1) of this section or a nonrecognition transfer subject to paragraph (g)(7) of this section has occurred, the transferor's certification must provide the information required under the rules of the subject paragraph. The annual certification pursuant to this paragraph (g)(5) must be signed under penalties of perjury by a person authorized to sign the agreement pursuant to the provisions of paragraph (g)(2) of this section. The certification must identify the transfer with respect to which it is given by setting forth the date of the transfer and a description of the stock or securities transferred. If a taxpayer has made more than one transfer subject to the rules of this paragraph (g), the certifications for those transfers may be combined in a single document, but each transfer must be separately identified.

(ii) *Waiver.* The transferor must agree to file with its income tax return for each of the eight taxable years following the taxable year of the transfer a waiver of the period of limitations on assessment as described in paragraph (g)(4) of this section. For the rule extending the period of limitation upon a failure to comply with the reporting requirements of section 6038B and regulations thereunder, see §1.6038B-1T(f)(1)(iii).

(6) *Warranty of information regarding disposition.* The transferor must warrant that arrangements have been made in connection with the transfer of stock or securities to ensure that the transferor will be informed of any subsequent disposition of stock, securities, or assets that would require the recognition of gain under the agreement.

(7) *Treatment of nonrecognition transfers.* If, during the period the agreement is in force, the transferee foreign corporation disposes of the stock or securities of the transferred corporation in a transaction on which gain or loss would not be required to be recognized under U.S. income tax principles, then the U.S. transferor shall not be required to recognize gain under paragraph (g)(3)(i) of this section, provided that the U.S. transferor complies with the requirements of subdivisions (i), (ii), and (iii) of this paragraph (g)(7).

(i) The U.S. transferor must provide a notice of the transfer with its next annual certification under paragraph (g)(5) of this section, setting forth—

(A) A description of the transfer;

(B) The applicable nonrecognition provision; and

(C) The name, address, and identifying number (if any) of the new transferee of the stock or securities of the transferred corporation.

(ii) The U.S. transferor must provide a new agreement to recognize gain (in accordance with the rules of paragraph (g)(2) and (3)(i) of this section) if, prior to the close of the fifth taxable year following the taxable year of the initial transfer, either—

(A) The initial transferee foreign corporation disposes of the interest which it received in exchange for the stock or securities of the transferred corporation (other than in a disposition which itself qualifies under the rules of this paragraph (g)(7)); or

(B) The person that obtained the stock or securities of the transferred corporation disposes of that stock or those securities (other than in a disposition which itself qualifies under the rules of this paragraph (g)(7)).

If a disposition that triggers the recognition of gain under the rules of this paragraph is only a partial disposition of the property, then the U.S. transferor shall be required to recognize a proportionate amount of the gain realized but not recognized upon the initial transfer. The proportion required to be recognized shall be determined by reference to the fair market value of the stock or securities disposed of and the fair market value of those retained as of the date of the disposition.

(iii) The U.S. transferor must warrant that arrangements have been made, in connection withthe nonrecognition transfer, ensuring that the U.S. transferor will be informed of any subsequent disposition with respect to which recognition of gain would be required under the agreement.

(8) *Special rules for indirect transfers*—(i) *Transfers covered.* If a U.S. person that holds an interest in an entity is considered to make an indirect transfer of stock or securities described in section 367(a) under the provisions of §1.367(a)-1T(c), then the rules of this paragraph (g)(8) shall apply to the transfer.

(ii) *Applicable rules.* For purposes of this paragraph (g), the foreign corporation that issued the stock or securities received by the U.S. transferor shall be considered to be the transferee foreign corporation. Any agreement entered into under this paragraph (g) with respect to such a transfer shall require the recognition of gain by the transferor if—

(A) That transferee foreign corporation disposes of the corporation that it controls (regardless of whether that corporation is the transferred corporation itself or another corporation that obtained the stock, securities, or assets of the transferred corporation); or

(B) The corporation that holds the assets of the transferred corporation disposes of all or a substantial portion those assets other than in the ordinary course of business.

The rules of paragraph (g)(7) of this section shall apply if gain or loss would not be required to be recognized under U.S. income tax principles with respect to such a transfer.

(9) *U.S. transferor goes out of existence.* If a U.S. corporation, trust, or estate that has entered into an agreement under this paragraph (g) goes out of existence, and that corporation, trust, or estate is not required to recognize gain under section 367 upon its liquidating transfer of the stock of the transferee foreign corporation, or if an individual transferor that has entered into an agreement under this paragraph (g) dies, then either—

(i) The person winding up the affairs of the transferor must retain assets to meet any possible liability of the transferor under the agreement;

(ii) The person winding up the affiars of the transferor must provide security under subparagraph (10) of this paragraph (g) for any possible liability of the transferor under the agreement; or

(iii) Each person that obtains the stock of the transferee foreign corporation from the transferor must enter into an agreement under this paragraph (g) having the same terms as the agreement entered into by the transferor (but only with respect to that person's proportionate share of the gain realized but not recognized upon the transferor's initial transfer of stock to the transferee foreign corporation).

(10) *Use of security.* The transferor may be required to furnish a bond or other security that satisfies the requirements of §301.7101-1 if the district director determines that such security is necessary to ensure the payment of any tax upon the gain realized upon the transfer. Such bond or security will generally be required only if the stock or securities transferred are the principal asset of the transferor and the director has reason to believe that a disposition of the stock or securities may be contemplated. In addition, if a transferor corporation, trust, or estate ceases to exist, or if an individual transferor dies, then the person winding up the affairs of the transferor (such as a trustee in bankruptcy or an executor) may choose to supply security pursuant to paragraph (g)(9) of this section for the performance of the transferor's obligations under an agreement entered into under this paragraph (g).

(11) *Failure to comply.* If a person that has entered into an agreement under this paragraph (g) fails at any time to comply in any material respect with the requirements of this section or with the terms of any agreement submitted pursuant thereto, then the rule of paragraph (g)(1) of this section shall not apply. Thus, the initial transfer of the stock or securities will become subject to section 367(a)(1) (unless otherwise excepted under the rules of this section) and will be treated as a taxable exchange in the year of the initial transfer. Such a material failure to comply shall extend the period for assessment of tax until three years after the date on which the Internal Revenue Service receives actual notice of the failure to comply.

(12) *Availability of forms.* Any agreement, certification, waiver, or other document required to be filed pursuant to the provisions of this paragraph (g) shall use such forms as may be prescribed therefore by the Commissioner (or a similar statement providing the same information). Until such time as forms are published, all necessary filings may be accomplished by providing the required information to the Service in accordance with the rules of this paragraph.

(13) *Basis adjustments*—(i) If a U.S. transferor is required to recognize gain under this paragraph (g), then in determining for U.S. income tax purposes any gain or loss recognized by the transferee foreign corporation upon its subsequent disposition of the transferred stock or securities, its basis in such interests shall be increased by the amount of gain required to be recognized (but not by any tax or interest required to be paid on such amount).

(ii) If a U.S. transferor is required to recognize gain under this paragraph (g), then the U.S. transferor's basis in the stock of the transferee foreign corporation shall be increased by the amount of gain required to be recognized (but not by any tax or interest required to be paid on such amount).

(h) *Anti-abuse rules*—(1) *Coordination with subpart F.* Notwithstanding the provisions of paragraph (d)(2) or (3) of this section, section 367 (a)(1) shall apply to a transfer of stock or securities of a foreign corporation if either:

(i) The transferred corporation was a controlled foreign corporation within the meaning of section 957(a), and the transferee corporation is not a controlled foreign corporation; or

(ii) Both the transferred and the transferee corporations are controlled foreign corporations within the meaning of section 957(a) but the transferor was a U.S. shareholder of the transferred corporation within the meaning of section 951(b) and is not a U.S. shareholder of the transferee corporation, within the meaning of section 951(b).

However, section 367(a)(1) shall not apply to such a transfer if the transferor enters into an agreement to recognize gain under paragraph (g) of this section.

(2) *Incorporation of property to avoid section 367(a)(1).* Notwithstanding any other provision of this section, section 367(a)(1) shall apply to a transfer of stock or securities of a domestic corporation if:

(i) The domestic corporation holds property that would be subject to section 367(a)(1) if it were transferred directly to a foreign corporation;

(ii) A U.S. person transferred that property to the domestic corporation in a transaction on which gain or loss was not required to be recognized, and

(iii) One of the principal purposes of the incorporation and transfer was avoidance of the provisions of section 367(a).

A transfer of property shall be presumed to have been made to avoid the provisions of section 367(a) if the transfer to the domestic corporation occurred less than two years before the transfer of the stock of the domestic corporation to the foreign corporation, or if it otherwise appears that the transfer of stock to the foreign corporation was planned or contemplated at the time of the transfer of the property to the domestic corporation. The presumption created by the previous sentence may be rebutted by evidence establishing that avoidance of the provisions of section 367(a) was not one of the principal purposes of the incorporation and subsequent transfer.

§1.367(a)-4T Special rules applicable to specified transfers of property (temporary).

(a) *In general*. This section provides special rules for determining the applicability of section 367(a)(1) to specified transfers of property. Paragraph (b) of this section provides a special rule requiring the recapture of depreciation upon the transfer abroad of property previously used in the United States. Paragraphs (c) through (f) of this section provide rules for determining whether certain types of property are transferred for use in the active conduct of a trade or business outside of the United States. Paragraph (g) excepts certain transfers to FSCs from the operation of section 367(a)(1). The treatment of any transfer of property described in this section shall be determined exclusively under the rules of this section.

(b) *Depreciated property used in the U.S.*—(1) *In general*. If a U.S. person transfers U.S. depreciated property (as defined in paragraph (b)(2) of this section) to a foreign corporation in an exchange described in section 367(a)(1), then that person shall include in its gross income for the taxable year in which the transfer occurs ordinary income equal to the gain realized that would have been includible in the transferor's gross income as ordinary income under section 617(d)(1), 1245(a), 1250(a), 1252(a), or 1254(a), whichever is applicable, if at the time of the transfer the transferor had sold the property at its fair market value. Recapture of depreciation under this paragraph (b) shall be required regardless of whether any exception to section 367(a)(1) (such as the exception for property transferred for use in the active conduct of a foreign trade or business) would otherwise apply to the transfer. However, any applicable exception shall apply with respect to realized gain that is not included in ordinary income pursuant to this paragraph (b).

(2) *U.S. depreciated property*. U.S. depreciated property subject to the rules of this paragraph (b) is any property that—

(i) Is either mining property (as defined in section 617(f)(2)), section 1245 property (as defined in section 1245(a)(3)), section 1250 property (as defined in section 1250(c)), farm land (as defined in section 1252(a)(2)), or oil, gas, or geothermal property (as defined in section 1254(a)(3)); and

(ii) Has been used in the United States or has qualified as section 38 property by virtue of section 48(a)(2)(B) prior to its transfer.

(3) *Property used within and without the U.S.* If U.S. depreciated property has been used partly within and partly without the United States, then the amount required to be included in ordinary income pursuant to this paragraph (b) shall be reduced to an amount determined in accordance with the following formula:

$$\text{Full recapture amount X } \frac{\text{U.S. use}}{\text{Total use}}$$

For purposes of the above fraction, the "full recapture amount" is the amount that would otherwise be included in the transferor's income under paragraph (b)(1) of this section. "U.S. use" is the number of months that the property either was used within the United States or qualified as section 38 property by virtue of section 48(a)(2)(B), and was subject to depreciation by the transferor or a related person. "Total use" is the total number of months that the property was used (or available for use), and subject to depreciation, by the transferor or a related person. For purposes of this paragraph (b)(3), property shall not be considered to have been in use outside of the United States during any period in which such property was, for purposes of section 48 or 168, treated as property not used predominantly outside the United States pursuant to the provisions of section 48(a)(2)(B). For purposes of this paragraph (b)(3) the term "related person" shall have the meaning set forth in §1.367(d)-1T (h).

(4) *Transfer followed by section 338 election*. For purposes of paragraph (b)(1) of this section, property that is transferred by a U.S. corporation to a foreign corporation in a transfer described in section 367(a)(1) shall be treated as U.S. depreciated property at the time of the transfer if—

(i) The transferee foreign corporation was a member of the U.S. transferor's affiliated group (determined without regard to the exceptions contained in section 1504(b)) at the time of the transfer; and

(ii) Within three years after the transfer, a purchasing corporation files an express election under section 338(g) for any member of the U.S. corporation's affiliated group (determined without regard to the exceptions contained in section 1504(b)) and files a regular exclusion election under §1.338-5T(c)(2)(v) by virtue of which the transferee foreign corporation is excluded from the status of target affiliate.

(5) *Effective date*. This paragraph (b) applies to transfers occurring on or after June 16, 1986.

(c) *Property to be leased*—(1) *Leasing business of transferee*. Tangible property transferred to a foreign corporation that will be leased to other persons by the foreign corporation shall be considered to be transferred for use in the active conduct of a trade or business outside of the United States only if—

(i) The transferee's leasing of the property constitutes the active conduct of a leasing business;

(ii) The lessee of the property is not expected to, and does not, use the property in the United States; and

(iii) The transferee has need for substantial investment in assets of the type transferred.

The active conduct of a leasing business requires that the employees of the foreign corporation perform substantial marketing, customer service, repair and maintenance, and other substantial operational activities with respect to the transferred property outside of the United States. Tangible property subject to the rules of this paragraph (c) includes real property located outside of the United States. The rules of §1.367(a)-5T(b) shall apply to transfers of property described in that section regardless of satisfaction of the rules of this paragraph (c).

(2) *De minimis leasing by transferee.* Tangible property transferred to a foreign corporation that will be leased to other persons by the foreign corporation and that does not satisfy the conditions of paragraph (b)(1) of this section shall, nevertheless, be considered to be transferred for use in the active conduct of a trade or business if either—

(i) The property transferred will be used by the transferee foreign corporation in the active conduct of a trade or business but will be leased during occasional brief periods when the property would otherwise be idle, such as an airplane leased during periods of excess capacity; or

(ii) The property transferred is real property located outside the United States and—

(A) The property will be used primarily in the active conduct of a trade or business of the transferee foreign corporation; and

(B) Not more than ten percent of the square footage of the property will be leased to others.

(d) *Property to be sold.* Property shall not be considered to be transferred for use in the active conduct of a trade or business and a transfer of stock or securities shall not be excepted from section 367 (a)(1) under the rules of §1.367(a)-3T if, at the time of the transfer, it is reasonable to believe that, in the reasonably foreseeable future, the transferee will sell or otherwise dispose of any material portion of the transferred stock, securities, or other property other than in the ordinary course of business.

(e) *Oil and gas working interests*—(1) *In general.* A working interest in oil and gas properties shall be considered to be transferred for use in the active conduct of a trade or business if—

(i) The transfer satisfies the conditions of paragraph (e)(2) of this section;

(ii) At the time of the transfer, the transferee has no intention to farm out or otherwise transfer any part of the transferred working interest; and

(iii) During the first three years after the transfer there are no farm outs or other transfers of any part of the transferred working interest as a result of which the transferee retains less than a 50 percent share of the transferred working interests.

(2) *Active use of working interest.* Working interests in oil and gas properties shall be considered to be transferred for use in the active conduct of a trade or business if—

(i) The transferor is regularly and substantially engaged in exploration for and extraction of minerals, either directly or through working interests in joint ventures, other than by reason of the property that is transferred;

(ii) The terms of the working interest transferred were actively negotiated among the joint ventures;

(iii) The working interest transferred constitutes at least a five percent working interest;

(iv) Prior to and at the time of the transfer, through its own employees or officers, the transferor was regularly and actively engaged in (A) operating the working interest, or (B) analyzing technical data relating to the activities of the venture;

(v) Prior to and at the time of the transfer, through its own employees or officers, the transferor was regularly and actively involved in decision-making with respect to the operations of the venture, including decisions relating to exploration, development, production, and marketing; and

(vi) After the transfer, the transferee foreign corporation will for the foreseeable future satisfy the requirements of subdivisions (iv) and (v) of this paragraph (d)(2).

(3) *Start-up operations.* Working interests in oil and gas properties that do not satisfy the requirements of paragraph (e)(2) of this section shall, nevertheless, be considered to be transferred for use in the active conduct of a trade or business if—

(i) The working interest was acquired by the transferor immediately prior to the transfer and for the specific purpose of transferring it to the transferee foreign corporation;

(ii) The requirements of paragraph (e)(2)(ii) and (iii) of this section are satisfied; and

(iii) The transferee foreign corporation will for the foreseeable future satisfy the requirements of paragraph (e)(2)(iv) and (v) of this section.

(4) *Other applicable rules.* Oil and gas interests not described in this paragraph (e) may nonetheless qualify for the exception to section 367 (a)(1) contained in §1.367(a)-2T, relating to transfers of property for use in the active conduct of a trade or business outside of the United States. However, a mere royalty interest in oil and gas properties will not be treated as transferred for use in the active conduct of a trade or business outside the United States. Moreover, a royalty or similar interest that constitutes intangible property will be subject to the rules of §1.367(d)-1T, relating to transfers of intangible property.

(f) *Compulsory transfers.* Property shall be presumed to be transferred for use in the active conduct of a trade or business outside of the United States, if—

(1) The property was previously in use in the country in which the transferee foreign corporation is organized; and

(2) The transfer is either:

(i) Legally required by the foreign government as a necessary condition of doing business in that country; or

(ii) Compelled by a genuine threat of immediate expropriation by the foreign government.

(g) *Relationship to other sections.* The rules of §§1.367(a)-5T, 1.367(a)-6T, and 1.367(d)-1T apply to transfers of property whether or not the property is transferred for use in the active conduct of a trade or business outside the United States. See §1.367(d)-1T(g)(2)(ii) for a special election with respect to compulsory transfers of intangible property.

(h) *Transfers of certain propety to FSCs*—(1) *In general.* The provisions of section 367(a) and (d) and the regulations thereunder shall not apply to a transfer of property by a U.S. person to a foreign corporation that constitutes a

FSC, as defined in section 922(a), if—

(i) The transferee FSC uses the property to generate exempt foreign trade income, as defined in section 923(a);

(ii) The property is not excluded property, as defined in section 927(a)(2); and

(iii) The property consists of a corporate name or tangible property that is appropriate for use in the operation of a FSC office.

(2) *Exception.* The general rule in paragraph (g)(1) of this section shall not apply if, within three years after the original transfer, the original transferee FSC (or a subsequent transferee FSC) disposes of the property other than in the ordinary course of business or through a transfer to another FSC. Thus, the U.S. transferor may recognize gain in the taxable year in which the original transfer occurred through the application of section 367 and the regulations thereunder.

§1.367(a)-5T Property subject to section 367(a)(1) regardless of use in trade or business (temporary).

(a) *In general.* Section 367(a)(1) shall apply to a transfer of property described in this section regardless of whether the property is transferred for use in the active conduct of a trade or business. Certain exceptions to the operation of this rule are provided in this section, and a special gain limitation rule is provided in paragraph (e). A transfer of property described in this section is subject to section 367(a)(1) even if the transfer is a compulsory transfer described in §1.367 (a)-4T (f).

(b) *Inventory, etc.* Regardless of use in an active trade or business, section 367(a)(1) shall apply to the transfer of—

(1) Stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business; and

(2) A copyright, a literary, musical, or artistic composition, a letter or memorandum, or similar property, held by—

(i) A taxpayer whose personal efforts created such property;

(ii) In the case of a letter, memorandum, or similar property, a taxpayer for whom such property was prepared or produced; or

(iii) A taxpayer in whose hands the basis of such property is determined, for purposes of determining gain from a sale or exchange, in whole or part by reference to the basis of such property in the hands of a taxpayer described in subdivision (i) or (ii) of this paragraph (b)(2).

For purposes of this section, the term "inventory" includes raw materials and supplies, partially completed goods, and finished products.

(c) *Installment obligations, etc.* Regardless of use in an active trade or business, section 367(a)(1) shall apply to the transfer of installment obligations, accounts receivable, or similar property, but only to the extent that the principal amount of any such obligation has not previously been included by the taxpayer in its taxable income.

(d) *Foreign currency, etc.*—(1) *In general.* Regardless of use in an active trade or business, section 367(a)(1) shall apply to the transfer of foreign currency or other property denominated in foreign currency, including installment obligations, futures contracts, forward contracts, accounts receivable, or any other obligation entitling its payee to receive payment in a currency other than U.S. dollars.

(2) *Exception for certain obligations.* If transferred property denominated in a foreign currency—

(i) Is denominated in the currency of the country in which the transferee foreign corporation is organized; and

(ii) Was acquired in the ordinary course of the business of the transferor that will be carried on by the transferee foreign corporation,

then section 367(a)(1) shall apply to the transfer only to the extent that gain is required to be recognized with respect to previously realized income reflected in installment obligations subject to paragraph (c) of this section. The rule of this paragraph (d)(2) shall not apply to transfers of foreign currency.

(3) *Limitation of gain required to be recognized.* If section 367(a)(1) applies to a transfer of property described in this paragraph, then the gain required to be recognized shall be limited to—

(i) The gain realized upon the transfer of property described in this paragraph (d), minus

(ii) Any loss realized as part of the same transaction upon the transfer of property described in this paragraph (d).

This limitation applies in lieu of the rule in §1.367(a)-1T(b)(1). No loss shall be recognized with respect to property described in this paragraph (d).

(e) *Intangible property.* Regardless of use in an active trade or business, a transfer of intangible property pursuant to section 332 shall be subject to section 367(a)(1), unless it constitutes foreign goodwill or going concern value, as defined in §1.367(a)-1T(d)(5)(iii). For rules concerning transfers of intangible property pursuant to section 351 or 361, see section 367(d) and §1.367(d)-1T.

(f) *Leased tangible property.* Regardless of use in an active trade or business, section 367(a)(1) shall apply to a transfer of tangible property with respect to which the transferor is a lessor at the time of the transfer, unless—

(1) With respect to property that will not be leased by the transferee to third persons, the transferee was the lessee of the property at the time of the transfer; or

(2) With respect to property that will be leased by the transferee to third persons, the transferee satisfies the conditions set forth in §1.367(a)-4T(c)(1) or (2).

§1.367(a)-6T Transfer of foreign branch with previously deducted losses (temporary).

(a) *In general.* This section provides special rules relating to the transfer of the assets of a foreign branch with previously deducted losses. Paragraph (b) of this section provides generally that such losses must be recaptured by the recognition of the gain realized on the transfer. Paragraph (c) of this section sets forth rules concerning the character of, and limitations on, the gain required to be recognized. Paragraph (d) of this section defines the term "previously deducted losses." Paragraph (e) of this section describes certain reductions that are made to the previously deducted losses before they are taken into income under this section. Finally, paragraph (g) of this section defines the term "foreign branch."

(b) *Recognition of gain required*—(1) *In general.* If a U.S. person transfers any assets of a foreign branch to a foreign corporation in an exchange described in section 367(a)(1), then the transferor shall recognize gain equal to—

(i) The sum of the previously deducted branch ordinary losses as defined and reduced in paragraphs (d) and (e) of this section; and

(ii) The sum of the previously deducted branch capital losses as defined and reduced in paragraphs (d) and (e) of this section.

(2) *No active conduct exception.* The rules of this paragraph (b) shall apply regardless of whether the assets of the foreign branch are transferred for use in the active conduct of a trade or business outside the United States.

(c) *Special rules concerning gain recognized*—(1) *Character and source of gain.* The gain described in paragraph (b)(1)(i) of this section shall be treated as ordinary income of the transferor, and the gain described in paragraph (b)(1)(ii) of this section shall be treated as long-term capital gain of the transferor. Gain that is recognized pursuant to the rules of this section shall be treated as income from sources outside the United States. Such recognized gain shall be treated as foreign oil and gas extraction income (as defined in section 907) in the same proportion that previously deducted foreign oil and gas extraction losses bore to the total amount of previously deducted losses.

(2) *Gain limitation.* For a rule limiting the amount of gain required to be recognized under section 367(a) upon any transfer of property to a foreign corporation, including the transfer of assets of a foreign branch with previously deducted losses, see §1.367(a)-1T(b)(3).

(3) *Foreign goodwill and going concern value.* For purposes of this section, the assets of a foreign branch shall include foreign goodwill and going concern value related to the business of the foreign branch, as defined in §1.367(a)-1T(d)(5)(iii). Thus, gain realized upon the transfer of the foreign goodwill or going concern value of a foreign branch to a foreign corporation will be taken into account in computing the limitation on loss recapture under paragraph (c)(2) of this section.

(4) *Transfers of certain intangible property.* Gain realized on the transfer of intangible property (computed with reference to the fair market value of the intangible property as of the date of the transfer) that is an asset of a foreign branch shall be taken into account in computing the limitation on loss recapture under paragraph (c)(2) of this section. For rules relating to the crediting of gain recognized under this section against income deemed to arise by operation of section 367(d), see §1.367(d)-1T(g)(3).

(d) *Previously deducted losses*—(1) *In general.* This paragraph (d) provides rules for determining, for purposes of paragraph (b)(1) of this section, the previously deducted losses of a foreign branch any of whose assets are transferred to a foreign corporation in an exchange described in section 367(a)(1). Initially, the two previously deducted losses of a foreign branch for a taxable year are the total ordinary loss ("previously deducted branch ordinary loss") the total capital loss ("previously deducted branch capital loss") that were realized by the foreign branch in that taxable year (a "branch loss year") prior to the transfer and that were or will be reflected on a U.S. income tax return of the transferor. The previously deducted branch loss year is reduced by expired net ordinary losses under paragraph (d)(2) of this section, while the previously deducted capital loss for each loss year is reduced by expired net capital losses under paragraph (d)(3) of this section. For each branch loss year, the remaining previously deducted branch ordinary loss and the remaining previously deducted branch capital loss are then reduced, proceeding from the first branch loss year to the last branch loss year, to reflect expired foreign tax credits under paragraph (d)(4) of this section. The reductions are made in the order of the taxable years in which the foreign tax credits arose. Finally, similar reductions are made to reflect expired investment credits under paragraph (d)(5) of this section.

(2) *Reduction by expired net ordinary loss*—(i) *In general.* The previously deducted branch ordinary loss for each branch loss year shall be reduced under this paragraph (d)(2) by the amount of any expired net ordinary loss with respect to that branch loss year. Expired net ordinary losses arising in years other than the branch loss year shall reduce the previously deducted branch ordinary loss for the branch loss year only to the extent that the previously deducted branch ordinary loss exceeds the net operating loss, if any, incurred by the transferor in the branch loss year. The previously deducted branch ordinary losses shall be reduced proceeding from the first branch loss year to the last branch loss year. For each branch loss year, expired net operating losses shall be applied to reduce the previously deducted branch ordinary loss for that year in the order in which the expired net ordinary losses arose.

(ii) *Existence of expired net ordinary loss.* An expired net ordinary loss exists with respect to a branch loss year to the extent that—

(A) The transferor incurred a net operating loss (within the meaning of section 172 (c));

(B) That net operating loss arose in the branch loss year or was available for carryover or carryback to the branch loss year under section 172(b)(1);

(C) That net operating loss has neither given rise to a net operating loss deduction (within the meaning of section 172(a)) for any taxable year prior to the year of the transfer, nor given rise to a reduction of any previously deducted branch ordinary loss (pursuant to paragraph (d)(2) of this section) of any foreign branch of the transferor upon a previous transfer to a foreign corporation; and

(D) The period during which the transferor may claim a net operating loss deduction with respect to that net operating loss has expired.

(3) *Reduction by expired net capital loss*—(i) *In general.* The previously deducted branch capital loss for each branch loss year shall be reduced under this paragraph (d)(3) by the amount of any expired net capital loss with respect to that branch loss year. Expired net capital losses arising in years other than the branch loss year shall reduce the previously deducted branch capital loss for the branch loss year only to the extent that the previously deucted branch capital loss exceeds the net capital loss, if any, incurred by the transferor in the branch loss year. The previously deducted branch capital losses shall be reduced proceeding from the first branch loss year to the last branch loss year. For each branch loss year, expired net capital losses shall be applied to reduce the previously deducted branch capital loss for that year in the order in which

the expired net capital losses arose.

(ii) *Existence of expired net capital loss.* An expired net capital loss exists with respect to a branch loss year to the extent that—

(A) The transferor incurred a net capital loss (within the meaning of section 1222(10));

(B) That net capital loss arose in the branch loss year or was available for carryover or carryback to the branch loss year under section 1212;

(C) That net capital loss has neither been allowed for any taxable year prior to the year of the transfer, nor given rise to a reduction of any previously deducted branch capital loss (pursuant to paragraph (d)(3) of this section) of any foreign branch of the transferor upon any previous transfer to a foreign corporation; and

(D) The period during which the transferor may claim a capital loss deduction with respect to that net capital loss has expired.

(4) *Reduction for expired foreign tax credits*—(i) *In general.* The previously deducted branch ordinary loss and the previously deducted branch capital loss for each branch loss year remaining after the reductions described in paragraph (d)(2) and (3) of this section shall be further reduced under this paragraph (d)(4) proportionately by the amount of any expired foreign tax credit loss equivalent with respect to that branch loss year. The previously deducted branch losses shall be reduced proceeding from the first branch loss year to the last branch loss year. For each branch loss year, expired foreign tax credit loss equivalents shall be applied to reduce the previously deducted branch loss for that year in the order in which the expired foreign tax credits arose.

(ii) *Existence of foreign tax credit loss equivalent.* A foreign tax credit loss equivalent exists with respect to a branch loss year if—

(A) The transferor paid, accrued, or is deemed under section 902 or 960 to have paid creditable foreign taxes in a taxable year;

(B) The creditable foreign taxes were paid, accrued, or deemed paid in the branch loss year or were available for carryover or carryback to the branch loss year under section 904(c);

(C) No foreign tax credit with respect to the foreign taxes paid, accrued, or deemed paid has been taken because of the operation of section 904(a) or similar limitations provided by the Code or an applicable treaty, and such taxes have not given rise to a reduction (pursuant to this paragraph (d)(5)) of any previously deducted branch loss of the foreign branch for a prior taxable year or of any previously deducted branch losses of any foreign branch of the transferor upon a prior transfer to a foreign corporation; and

(D) The period during which the transferor may claim a foreign tax credit for the foreign taxes paid, accrued, or deemed paid has expired.

(iii) *Amount of foreign tax credit loss equivalent.* The amount of the foreign tax credit loss equivalent for the branch loss year with respect to the creditable foreign taxes described in paragraph (d)(4)(ii) of this section is the amount of those creditable foreign taxes divided by the highest rate of tax to which the transferor was subject in the loss year.

(5) *Reduction for expired investment credits*—(i) *In general.* The previously deducted branch ordinary loss and the previously deducted branch capital loss for each branch loss year shall be further reduced under this paragraph (d)(5) proportionately by the amount of any expired investment credit loss equivalent with respect to that branch year. The previously deducted branch losses shall be reduced proceeding from the first branch loss year to the last branch loss year. For each branch loss year, expired investment credit loss equivalents shall be applied to reduce the previously deducted branch loss for that year in the order in which the expired investment credits were earned.

(ii) *Existence of investment credit loss equivalent.* An investment credit loss equivalent exists with respect to a branch loss year if—

(A) The transferor earned an investment credit (within the meaning of section 46(a)) in a taxable year;

(B) The investment credit was earned in the branch loss year or was available for carryover or carryback to the branch loss year under section 39;

(C) The investment credit earned by the transferor in the credit year has been denied by section 38(a) or by similar provisions of the Code and has not given rise to a reduction (pursuant to this paragraph (d)(5)) of any previously deducted branch loss of the foreign branch for a preceding taxable year or of the previously deducted losses of any foreign branch of the transferor upon any previous transfer to a foreign corporation; and

(D) The period during which the transferor may claim the investment credit has expired.

(iii) *Amount of investment tax credit loss equivalent.* The amount of the investment credit loss equivalent for the branch loss year with respect to the investment credit described in paragraph (d)(5)(ii) of this section is 85 percent of the amount of that investment credit divided by the highest rate of tax to which the transferor was subject in the loss year.

(e) *Amounts that reduce previously deducted losses subject to recapture*—(1) *In general.* This paragraph (e) describes five amounts that reduce the sum of the previously deducted branch ordinary losses and the sum of the previously deducted branch capital losses before they are taken into income under paragraph (b) of this section. Amounts representing ordinary income shall be applied to reduce first the sum of the previously deducted branch ordinary losses to the extent thereof, and then the sum of the previously deducted branch capital losses to the extent thereof. Similarly, amounts representing capital gains shall be applied to reduce first the sum of the previously deducted capital losses and then the sum of the previously deducted branch ordinary losses.

(2) *Taxable income.* The previously deducted losses shall be reduced by any taxable income of the foreign branch recognized through the close of the taxable year of the transfer, whether before or after any taxable year in which losses were incurred.

(3) *Amounts currently recaptured under section 904(f)(3).* The previously deducted losses shall be reduced by the amount recognized under section 904(f)(3) on account of the transfer.

(4) *Gain recognized under section 367(a).* The previously deducted branch losses shall be reduced by any gain recognized pursuant to section 367(a)(1) (other than by reason of the provisions of this section) upon the transfer of the assets of the foreign branch to the foreign corporation.

(5) *Amounts previously recaptured*

under section 904(f)(3)—(i) *In general*. The previously deducted branch losses shall be reduced by the portion of any amount recognized under section 904(f)(3) upon a previous transfer of property that was attributable to the losses of the foreign branch, provided that the amount did not reduce any gain otherwise required to be recognized under section 367(a)(3)(C) and this section (or Revenue Ruling 78-201, 1978-1 C.B. 91).

(ii) *Portion attributable to the losses of the foreign branch*—(A) *Branch property*. The full amount recognized under section 904(f)(3) upon a previous transfer of property of the branch shall be treated as attributable to the losses of the foreign branch.

(B) *Non-branch property*. The portion of the amount previously recognized under section 904(f)(3) upon a transfer of non-branch property that was attributable to the losses of the foreign branch shall be the sum, over the taxable years in which the transferor sustained an overall foreign loss some portion of which was recaptured on the disposition, of the recaptured portions of those overall foreign losses after multiplication by the following fraction:

$$\frac{\text{Losses of the foreign branch for the year}}{\text{All foreign losses for the year}}$$

For purposes of this fraction, the term "losses of the foreign branch for the year" means the losses of the foreign branch that were taken into account under section 904(f)(2) in determining the amount of the transferor's overall foreign loss for the year, and the term "all foreign losses for the year" means all of the losses of the transferor that were taken into account under section 904(f)(2).

(6) *Amounts previously recognized under the rules of this section*. The previously deducted losses shall be reduced by the amounts previously recognized under the rules of this section upon a previous transfer of assets of the foreign branch.

(f) *Example*. The rules of paragraphs (b) through (e) of this section are illustrated by the following example.

Example. (i) *Facts*. X, a U.S. corporation, is a calendar year taxpayer. On January 1, 1981, X established a branch in foreign country A. On July 1, 1986, X organized corporation Y, a country A subsidiary, and transferred to Y all of the assets of its country A branch, including goodwill and going concern value. During the period from January 1, 1981, through July 1, 1986, X's country A branch earned income and incurred losses in the following amounts:

Country A branch

Year	*Ordinary income (loss)*	*Capital gain (loss)*
1981	(200)	0
1982	(300)	(100)
1983	(400)	0
1984	200	0
1985	(100)	0
1986	50	0

At the time of the transfer of X's country A branch assets to Y, those assets had a fair market value of $2,500 and an adjusted basis of $1,000. For each of the assets, fair market value exceeded adjusted basis. X had no net capital loss or unused investment credit during any taxable year relevant to the transfer. In 1984, X incurred a net operating loss of $400, $200 of which was carried back to prior years. An additional $50 of the 1984 net operating loss was carried over to 1985. The remaining $150 of the 1984 net operating loss was not used in any year prior to the transfer. In 1979, X paid creditable foreign taxes of $330 that could not be claimed as a credit in that year or any earlier year because of section 904. Of those foreign taxes, $100 were carried over and claimed as a credit in 1983, but the remaining $230 were not used in any year prior to the transfer. X was not required to recognize any gain under section 904(f)(3) on account of the 1986 transfer or any prior transfer. X was not required to recognize gain upon the transfer under section 367(a) (other than by reason of the provisions of this section).

(ii) *Previously deducted losses*. The previously deducted losses of X's country A branch are $575 of ordinary losses and $25 of capital losses, computed as follows: Initially, the branch has previously deducted ordinary losses of $1,000 ($200 + $300 + $400 + $100), and previously deducted capital losses of $100. (See paragraph (d)(1) of this section.)

(iii) *Expired losses and credits*. Under the facts of this example, there are no reductions for expired net ordinary losses or expired net capital losses under paragraph (d)(2) or (3) of this section. However, the previously deducted losses are reduced proceeding from the first branch loss year to the last branch loss year to reflect the expired foreign tax credit from 1979. The amount of the foreign tax credit loss equivalent with respect to 1981 is $500 ($230/.46). It reduces the previously deducted losses for 1981 proportionately. Thus, the previously deducted ordinary loss for 1981 is reduced from $200 to $0. (See paragraph (d)(4) of this section.) The amount of the foreign tax credit loss equivalent with respect to 1982 is $300 ($500 − $200, i.e., $138/.46). (See paragraph (d)(4)(ii)(C) of this section.) It reduces the previously deducted losses for 1982 proportionately. Thus, the previously deducted ordinary loss for 1982 is reduced from $300 to $75, and the previously deducted capital loss for 1982 is reduced from $100 to $25.

(iv) *Further reductions*. The previously deducted ordinary losses of $575 and the previously deducted capital losses of $25 are reduced by the taxable income earned by the branch prior to the date of the transfer ($250). (See paragraph (e)(2) of this section.) Since that income was ordinary income, it is applied first to reduce the previously deducted ordinary losses of $575 to $325. (See paragraph (e)(1) of this section.)

(v) *Recapture*. Since the gain realized by X upon its transfer of the branch assets to Y exceeds the sum of the previously deducted branch losses as defined and reduced above ($325 + $25), the limitation in paragraph (c)(2) of this section does not apply. Thus, X is required to recognize $325 of ordinary income and $25 of long-term capital gain upon the transfer. (See paragraph (b) and (c)(1) of this section.)

(g) *Definition of foreign branch*—(1) *In general*. For purposes of this section, the term "foreign branch" means an integral business operation carried on by a U.S. person outside the United States. Whether the activities of a U.S. person outside the United States constitute a foreign branch operation must be determined under all the facts and circumstances. Evidence of the existence of a foreign branch includes, but is not limited to, the existence of a separate set of books and records, and the existence of an office or other fixed place of business used by employees or officers of the U.S. person in carrying out business activities outside the United States. Activities outside the United States shall be deemed to constitute a foreign branch for purposes of this section if the activities constitute a permanent establishment under the terms of a treaty between the United States and the country in which the activities are carried out. Any U.S. person may be treated as having a foreign branch for purposes of this section, whether that person is a corporation, partnership, trust, estate, or individual.

(2) *More than one branch*. If a U.S. person carries on more than one branch operation outside the United States, then the rules of this section must be separately applied with respect to each foreign branch that is transferred to a foreign corporation. Thus, the previously deducted losses of one branch may not be offset, for purposes of determining the gain required to be recognized under the rules of this section, by the income of another branch that is also transferred to a foreign corporation. Similarly, the losses of one branch shall not be recaptured upon a transfer of the assets of a separate branch. Whether the foreign activities of a U.S. person are carried out through more than one branch must be determined under all of the facts and

circumstances. In general, a separate branch exists if a particular group of activities is sufficiently integrated to constitute a single business that could be operated as an independent enterprise. For purposes of determining the combination of activities that constitute a branch operation as defined in this paragraph (g), the nominal relationship among those activities shall not be controlling. Factors suggesting that nominally separate business operations constitute a single foreign branch include a substantial identity of products, customers, operational facilities, operational processes, accounting and record-keeping functions, management, employees, distribution channels, or sales and purchasing forces. For examples of the application of the principles of this paragraph (g)(2), see Revenue Ruling 81 – 82, 1981 – 1 C.B. 127.

(3) *Consolidated group*. For purposes of this section, the activities of each of two domestic corporations outside the United States will be considered to constitute a single foreign branch if—

(i) The two corporations are members of the same consolidated group of corporations; and

(ii) The activities of the two corporations in the aggregate would constitute a single foreign branch if conducted by a single corporation.

Notwithstanding the preceding rule of this paragraph (g)(3), gains of a foreign branch of a domestic corporation arising in a year in which that corporation did not file a consolidated return with a second domestic corporation shall not be applied to reduce the previously deducted losses of a foreign branch of the second corporation (but may be applied to reduce such losses of the foreign branch of the first corporation) upon the transfer of the two branches to a foreign corporation, even though the two domestic corporations file a consolidated return for the year in which the transfer occurs and the two branches are considered at that time to constitute a single foreign branch. For an example of the application of the principles of this paragraph (g)(3), see Revenue Ruling 81-89. 1981-1 C.B. 129.

(4) *Property not transferred*. A U.S. transferor's failure to transfer any property of a foreign branch shall be irrelevant to the determination of the previously deducted losses of the branch subject to recapture under the rules of this section. Thus, if the activities with respect to untransferred property constituted a part of the branch operation under the rules of this paragraph (g), then the losses generated by those activities shall be subject to recapture, notwithstanding the failure to transfer the property. For an example of the application of the principles of this paragraph (g)(4), see Revenue Ruling 80-247, 1980-2 C.B. 127, relating to property abandoned by the U.S. transferor.

(h) *Anti-abuse rule*. If—

(1) A U.S. person transfers property of a foreign branch to a domestic corporation for a principal purpose of avoiding the effect of this section; and

(2) The domestic corporation thereafter transfers the property of the foreign branch to a foreign corporation,

then, solely for purposes of this section, that U.S. person shall be treated as having transferred the property of the branch directly to the foreign corporation. A U.S. person shall be presumed to have transferred property of a foreign branch for a principal purpose of avoiding the effect of this section if the property is transferred to the domestic corporation less than two years prior to the domestic corporation's transfer of the property to a foreign corporation. This presumption may be rebutted by clear evidence that the subsequent transfer of the property was not contemplated at the time of the initial transfer to the domestic corporation and that avoidance of the effect of this section was not a principal purpose for the transaction. A transfer may have more than one principal purpose.

(i) *Basis adjustments*. Basis adjustments reflecting gain recognized pursuant to this section shall be made as described in §1.367(a)-1T(b)(4)(ii).

Par. 5. Section 1.367(d)-1T is added immediately after §1.367(c)-2, to read as follows:

§1.367(d)-1T Transfers of intangible property to foreign corporations (temporary).

(a) *Purpose and scope*. This section provides rules under section 367(d) concerning transfers of intangible property by U.S. persons to foreign corporations pursuant to section 351 or 361. Paragraph (b) of this section specifies the transfers that are subject to section 367(d) and the rules of this section, while paragraph (c) provides rules concerning the consequences of such a transfer. In general, the U.S. transferor will be treated as receiving annual payments contingent on productivity or use of the transferred property, over the useful life of the property (regardless of whether such payments are in fact made by the transferee). Paragraphs (d), (e), and (f) of this section provide rules for cases in which there is a later direct or indirect disposition of the intangible property transferred. In general, deemed annual license payments will continue if a transfer is made to a related person, while gain must be recognized immediately if the transfer is to an unrelated person. Paragraph (g) of this section provides several special rules, including a rule allowing appropriate adjustments where deemed payments under section 367(d) are not in fact received by the U.S. transferor of the intangible property, and a rule providing for a limited election to treat certain transfers of intangible property as sales at fair market value (in lieu of applying the general useful life-contingent payment rule). In addition, paragraph (g) of this section provides rules coordinating the application of section 367(d) with other relevant Code sections. Paragraph (h) of this section defines the term "related person" for purposes of this section. Finally, paragraph (i) of this section provides the effective date of this section. For rules concerning transfers of intangible property pursuant to section 332, see §1.367(a)-5T(e).

(b) *Intangible property subject to section 367(d)*. Section 367(d) and the rules of this section shall apply to the transfer of any intangible property, as defined in §1.367(a)-1T(d)(5)(i). However, section 367(d) and the rules of this section shall not apply to the transfer of foreign goodwill or going concern value, as defined in §1.367(a)-1T(d)(5)(iii), or to the transfer of intangible property described in §1.367(a)-5T(b)(2). However, the transfer of those items to a foreign corporation is subject to the rules set forth in §1.367(a)-6T, and the transfer of intangible property described in §1.367(a)-5T(b)(2) is subject to the rules set forth in §1.367(a)-5T. For a special rule relating to the transfer of operating intangibles, as defined in

§1.367(a)-1T(d)(5)(ii), see paragraph (g)(3) of this section. Transfers of intangible property to foreign corporations pursuant to section 351 or 361 are subject to the rules of this section regardless of whether the property is to be used in the United States, in connection with goods to be sold or consumed in the United States, or in connection with a trade or business outside the United States.

(c) *Deemed payments upon transfer of intangible property to foreign corporation*—(1) *In general.* If a U.S. person transfers intangible property that is subject to section 367(d) and the rules of this section to a foreign corporation in an exchange described in section 351 or 361, then such person shall be treated as having transferred that property in exchange for annual payments contingent on the productivity or use of the property. Such person shall, over the useful life of the property, annually include in gross income an amount that represents an appropriate arms-length charge for the use of the property. The appropriate charged shall be determined in accordance with the provisions of section 482 and regulations thereunder. See §1.482-2(d). The amount of the deemed payment thus calculated shall be reduced by any royalty or other periodic payment made or accrued by the transferee to an unrelated person during that taxable year for the right to use the intangible property. Amounts so included in the transferor's income shall be treated as ordinary income from sources with the United States. For purposes of computing estimated tax payments, deemed payments under this paragraph (c) shall be treated as received by the transferor on the last day of its taxable year.

(2) *Required adjustments.* The following adjustments shall be made with respect to a U.S. person's recognition of a deemed payment for the use of intangible property under this paragraph (c):

(i) For purposes of chapter 1 of the Code, the earnings and profits of the transferee foreign corporation shall be reduced by the amount of such deemed payment; and

(ii) For purposes of subpart F of part III of subchapter N of the Code, the transferee foreign corporation may treat such deemed payment as an expense (whether or not that amount is actually paid), properly allocated and apportioned to gross income subject to subpart F, in accordance with the provisions of §§1.954-1(c) and 1.861-8.

No other special adjustments to earnings and profits, basis, or gross income shall be permitted by reason of the recognition of a deemed payment under this paragraph (c). However, see paragraph (g)(1) of this section for rules permitting the establishment of an account receivable with respect to deemed payments not actually received by the U.S. person.

(3) *Useful life.* For purposes of this section, the useful life of intangible property is the entire period during which the property has value. However, in no event shall the useful life of an item of intangible property be considered to exceed twenty years. If intangible property derives its value from secrecy or from protections afforded by law, the useful life of such property shall terminate when the property is no longer secret or no longer legally protected.

(4) *Blocked income.* No deemed payment included in a taxpayer's income under paragraph (c)(1) of this section shall be treated as deferrable income for purposes of applying rules relating to blocked foreign income. See Revenue Ruling 74-351, 1974-2 C.B. 144.

(d) *Subsequent transfer of stock of transferee foreign corporation to unrelated person*—(1) *Treatment as sale of intangible property.* If a U.S. person transfers intangible property that is subject to section 367(d) and the rules of this section to a foreign corporation in an exchange described in section 351 or 361, and within the useful life of the intangible property that U.S. transferor subsequently disposes of the stock of the transferee foreign corporation to a person that is not a related person (within the meaning of paragraph (h) of this section), then the U.S. transferor shall be treated as having simultaneously sold the intangible property to the person acquiring the stock of the transferee foreign corporation. The U.S. transferor shall be required to recognize gain (but not loss) from sources within the United States in an amount equal to the difference between the fair market value of the transferred intangible property on the date of the subsequent disposition and the U.S. transferor's former adjusted basis in that property (determined as of the original transfer). If the U.S. transferor's disposition of the stock of the transferee foreign corporation is subject to U.S. tax other than by reason of this paragraph (d), then the amount of gain otherwise required to be recognized with respect to the stock of the transferee foreign corporation shall be reduced by the amount of gain recognized with respect to the intangible property pursuant to this paragraph (d).

(2) *Required adjustments.* If a U.S. person disposes of the stock of a transferee foreign corporation, and under paragraph (d)(1) of this section is treated as having simultaneously sold intangible property, then, for purposes of computing basis and earnings and profits, the person acquiring the stock of the transferee foreign corporation shall be deemed to have purchased that property at fair market value and to have immediately thereafter contributed it to the transferee foreign corporation in a transaction not covered by section 367(d). Therefore, for purposes of chapter 1 of the Code—

(i) The transferee foreign corporation's basis in the intangible property will be equal to its fair market value (as calculated for purposes of determining the gain required to be recognized by the U.S. transferor);

(ii) The acquiring person's basis in the stock of the transferee foreign corporation shall be determined as if no portion of the consideration given by the acquiring person for the stock is attributable to the intangible property; and

(iii) The earnings and profits of the transferee foreign corporation will not be affected by the transfer of its stock or the deemed transfer to it of the intangible property.

(e) *Subsequent transfer of stock of transferee foreign corporation to related person*—(1) *Transfer to related U.S. person treated as disposition of intangible property.* If a U.S. person transfers intangible property that is subject to section 367(d) and the rules of this section to a foreign corporation in an exchange desribed in section 351 or 361 and, within the useful life of the transferred intangible property, that U.S. transferor subsequently transfers the stock of the transferee foreign corporation to U.S. persons that are related to the transferor within the meaning of paragraph (h) of this section, then the following rules shall apply:

(i) Each such related U.S. person shall be treated as having received (with the stock of the transferee foreign corporation) a right to receive a proportionate share of the contingent annual payments that would otherwise be deemed to be received by the U.S. transferor under paragraph (c) of this section.

(ii) Each such related U.S. person shall, over the useful life of the property, annually include in gross income a proportionate share of the amount that would have included in the income of the U.S. transferor pursuant to paragraph (c) of this section. Such amounts shall be treated as ordinary income from sources within the United States.

(iii) The amount of income required to be recognized by the U.S. transferor pursuant to the rule of paragraph (d)(1) of this section shall be reduced to the amount determined in accordance with the following formula:

(d) (1) amount X (100% −
(e) percentage)

For purposes of the above formula, the "(d)(1) amount" is the income that would otherwise be required to be recognized by the transferor corporation pursuant to paragraph (d)(1) of this section, and the "(e) percentage" is the percentage of the transferor corporation's total deemed rights to receive contingent annual payments under paragraph (c) of this section that is deemed to be transferred to related U.S. persons under the rules of this paragraph (e).

(iv) The rules of paragraphs (d) and (e) of this section shall be reapplied in the case of any later transfer of the stock of the transferee foreign corporation by a related U.S. person that received such stock in a transfer that was subject to the rules of this paragraph (e). For purposes of reapplying the rules of paragraphs (d) and (e), each such related U.S. person shall be treated as a U.S. transferor of intangible property to the transferee foreign corporation (to the extent of the interest attributed to such person pursuant to subdivision (i) of this paragraph (e)(1)).

(2) *Required adjustments.* If a U.S. person transfers stock of a transferee foreign corporation to a U.S. related person in a transaction that is subject to the rules of paragraph (e)(1) of this section, the following adjustments shall be made:

(i) For purposes of chapter 1 of the Code, the earnings and profits of the transferee foreign corporation shall be reduced by the amount of any payment deemed to be received by a related U.S. person under paragraph (e)(1)(ii) of this section;

(ii) For purposes of subpart F of part III of subchapter N of the Code, the transferee foreign corporation may allocate and apportion such deemed payments (whether or not such payments are actually made) to gross income subject to subpart F to the extent appropriate under the provisions of §§1.954-1(c) and 1.861-8;

(iii) For purposes of reapplying the rules of paragraphs (d) and (e) of this section, if the related U.S. person is deemed to have received a right to contingent annual payments for the use of intangible property, then the U.S. related person shall be deemed to have held a proportionate share of the property with a basis equal to a proportionate share of the U.S. transferor's adjusted basis plus the gain, if any, recognized by the U.S. transferor on the earlier transfer of the stock to the U.S. related person, and then to have transferred that proportionate share of the property to the foreign corporation in a transfer subject to section 367(d); and

(iv) If the U.S. transferor is itself required to recognize gain upon the transfer by reason of the operation of paragraphs (d)(1) and (e)(1)(iii) of this section (because stock of the transferee foreign corporation is also transferred to unrelated persons), then those unrelated persons shall be deemed to have purchased a proportionate share of the transferred intangible property at fair market value and immediately contributed that property to the transferee foreign corporation, consistent with the general rule of paragraph (d)(2) of this section concerning transfers of stock to unrelated persons. Therefore, for purposes of chapter 1 of the Code—

(A) Each unrelated person's basis in the stock of the transferee foreign corporation shall be increased to the extent of the gain recognized by the U.S. transferor upon the deemed purchase of intangible property by that person; and

(B) The transferee foreign corporation will receive an increase in its basis in the transferred intangible property equal to the fair market value of that portion of the intangible property deemed to be contributed to the transferee foreign corporation by unrelated persons (as calculated for purposes of determining the gain required to be recognized by the U.S. transferor).

(3) *Transfer to related foreign person not treated as disposition of intangible property.* If a U.S. person transfers intangible property that is subject to section 367(d) and the rules of this section to a foreign corportion in an exchange described in section 351 or 361, and within the useful life of the transferred intangible property, the U.S. transferor subsequently transfers any of the stock of the transferee foreign corporation to one or more foreign persons that are related to the transferor within the meaning of paragraph (h) of this section, then the U.S. transferor shall continue to include in its income the deemed payments described in paragraph (c) of this section in the same manner as if the subsequent transfer of stock had not occurred. The rule of this paragraph (e)(3) shall not apply with respect to the subsequent transfer by the U.S. person of any of the remaining stock to any related U.S. person or unrelated person.

(4) *Proportionate share.* For purposes of this paragraph (e), any "proportinate share" shall be determined by reference to the fair market value (at the time of the original transfer) of the stock of the transferee foreign corporation that was transferred by the U.S. transferor and the fair market value of all of the stock of the transferee foreign corporation originally received by the U.S. transferor.

(f) *Subsequent disposition of transferred intangible property by transferee foreign corporation*—(1) *In general.* If a U.S. person transfers intangible property that is subject to section 367(d) and the rules of this section to a foreign corporation in an exchange described in section 351 or 361, and within the useful life of the intangible property that transferee foreign corporation subsequently disposes of the intangible property to an unrelated person, then—

(i) The U.S. transferor of the intangible property (or any person treated as such pursuant to paragraph (e)(1) of this section) shall be required to recognize gain from U.S. sources (but not loss) in an amount equal to the difference between the fair market value of the transferred intangible property on the date of the subsequent disposition and the U.S. transferor's former adjusted basis in that property (determined as of the original transfer); and

(ii) The U.S. transferor shall be required to recognize a deemed payment under paragraph (c) of this section for that part of its taxable year that the intangible property was held by the transferee foreign corporation and thereafter shall not be required to recognize any further deemed payments under paragraph (c) or (e)(1) of this section with respect to the transferred intangible property disposed of by the transferee foreign corporation.

(2) *Required adjustments.* If a U.S. transferor is required to recognize gain under paragraph (f)(1) of this section, then—

(i) For purposes of chapter 1 of the Code, the earnings and profits of the transferee foreign corporation shall be reduced by the amount of gain required to be recognized; and

(ii) The U.S. transferor's recognition of gain will permit the establishment of an account receivable from the transferee foreign corporation, in accordance with paragraph (g)(1) of this section.

(3) *Subsequent transfer of intangible property to related person.* The requirement that a U.S. person recognize gain under paragraph (c) or (e) of this section shall not be affected by the transferee foreign corporation's subsequent disposition of the transferred intangible property to a related person. For purposes of any required adjustments, and of any accounts receivable created under paragraph (g)(1) of this section, the related person that receives the intangible property shall be treated as the transferee foreign corporation.

(g) *Special rules*—(1) *Establishment of accounts receivable*—(i) *In general.* If a U.S. person is required to recognize income under the provisions of paragraph (c), (e), or (f) of this section, and the amount deemed to be received is not actually paid by the transferee foreign corporation, then the U.S. person may establish an account receivable from the transferee foreign corporation equal to the amount deemed paid that was not actually paid. A separate account receivable must be established for each taxable year in which payments deemed to be received are not actually made. Payments received from the transferee foreign corporation must be designated as payments upon a particular account and must be deducted from that account. Accounts receivable under this paragraph (g)(1) may be established and paid without further U.S. income tax consequences to the U.S. transferor or the transferee foreign corporation. No interest shall be paid or accrued on an account receivable created under this paragraph (g)(1), nor shall any bad debt deduction be allowed under section 166 with respect to any failure to receive payment on an account.

(ii) *Unpaid receivable treated as contribution to capital.* If any portion of an account receivable established under this paragraph (g)(1) remains unpaid as of the last day of the third taxable year following the taxable year to which the account relates, then—

(A) Such portion shall be deemed to have been paid on that date; and

(B) The U.S. person shall be deemed to have contributed an equivalent amount to the capital of the foreign corporation, and the U.S. person's basis in the stock of the foreign corporation shall, therefore, be increased by that amount.

(2) *Election to treat transfer as sale.* A U.S. person that transfers intangible property to a foreign corporation in a transaction subject to section 367(d) may elect to recognize income in accordance with the rules of this paragraph (g)(2), if—

(i) The intangible property transferred constitutes an operating intangible, as defined in §1.367(a)-1T(d)(5)(ii); or

(ii) The transfer of the intangible property is either legally required by the government of the country in which the transferee corporation is organized as a condition of doing business in that country, or compelled by a genuine threat of immediate expropriation by the foreign government; or

(iii) (A) The U.S. person transferred the intangible property to the foreign corporation within three months of the organization of that corporation and as part of the original plan of capitalization of that corporation;

(B) Immediately after the transfer, the U.S. person owns at least 40 percent but not more than 60 percent of the total voting power and total value of the stock of the transferee foreign corporation;

(C) Immediately after the transfer, at least 40 percent of the total voting power and total value of the stock of the transferee foreign corporation is owned by foreign persons related to the U.S. person;

(D) Intangible property constitutes at least 50 percent of the fair market value of the property transferred to the foreign corporation by the U.S. transferor; and

(E) The transferred intangible property will be used in the active conduct of a trade or business outside of the United States within the meaning of §1.367(a)-2T and will not be used in connection with the manufacture or sale of products in or for use or consumption in the United States.

A person that makes the election under this paragraph (g)(2) shall not be subject to the provisions of paragraphs (c) through (f) of this section. Such person shall instead recognize in the year of the transfer ordinary income from sources within the United States in an amount equal to the difference between the fair market value of the intangible property transferred and its adjusted basis. A U.S. person shall make an election under this paragraph (g)(2) by notifying the Internal Revenue Service of the election in accordance with the requirements of section 6038B and regulations thereunder, and subsequently including the appropriate amounts of gross income in a timely filed tax return for the year of the transfer.

(3) *Intangible property transferred from branch with previously deducted losses.* If income is required to be recognized under section 904(f)(3) and the regulations thereunder or under §1.367(a)-6T upon the transfer of intangible property of a foreign branch that had previously deducted losses, then the income recognized under those sections with respect to that property shall be credited against amounts that would otherwise be required to be recognized with respect to that same property under paragraphs (c) through (f) of this section in either the current or future taxable years. The amount recognized under section 904(f)(3) or

§1.367(a)-6T with respect to the transferred intangible property shall be determined in accordance with the following formula:

$$\text{loss recapture income} \times \frac{\text{gain from intangibles}}{\text{gain from all branch assets}}$$

For purposes of the above formula, the "loss recapture income" is the total amount required to be recognized by the U.S. transferor pursuant to section 904(f)(3) or §1.367(a)-6T. The "gain from intangibles" is the total amount of gain realized by the U.S. transferor pursuant to section 904(f)(3) and §1.367(a)-6T upon the transfer of items of intangible property that are subject to section 367(d). ("Gain from intangibles" does not include gain realized upon the transfer of property described in §1.367(a)-5T(b)(2), foreign goodwill or going concern value, or intangible property with respect to which the taxpayer has made the election provided for in §1.367(d)-1T(g)(2).) The "gain from all branch assets" is the total amount of gain realized by the transferor upon the transfer of items of property of the branch in which gain is realized. The fraction shall not exceed 1.

(4) *Coordination with section 482*—(i) *In general.* Section 367(d) and the rules of this section shall not apply in the case of an actual sale or license of intangible property by a U.S. person to a foreign corporation. If an adjustment under section 482 is required with respect to an actual sale or license of intangible property, then section 367(d) and the rules of this section shall not apply with respect to the required adjustment. If a U.S. person transfers intangible property to a related foreign corporation without consideration, or in exchange for stock or securities of the transferee in a transaction described in sections 351 or 361, no sale or license subject to adjustment under section 482 will be deemed to have occurred. Instead, the U.S. person shall be treated as having made a transfer of the intangible property that is subject to section 367(d).

(ii) *Sham licenses and sales.* For purposes of paragraph (g)(4)(i) of this section, a purported sale or license of intangible property may be disregarded, and treated as a transfer subject to section 367(d) and the rules of this section, if—

(A) The purported sale or license is made to a foreign corporation in which the transferor holds (or is acquiring) an interest; and

(B) The terms of the purported sale or license differ so greatly from the economic substance of the transaction or the terms that would obtain between unrelated persons that the purported sale or license is a sham.

The terms of a purported sale or license, for purposes of applying the rule of this paragraph (g)(4)(ii), shall be determined by reference not only to the nominal terms of the agreement but also to the actual practice of the parties under that agreement. A sale or license of intangible property shall not be disregarded under this paragraph (g)(4)(ii) solely because other property of an integrated business is simultaneously transferred to the foreign corporation by the U.S. transferor in a transaction described in section 367(a)(1) or any statutory or regulatory exception to section 367(a)(1).

(5) *Determination of fair market value.* For purposes of determining the gain required to be recognized immediately under paragraph (d), (f), or (g)(2) of this section the fair market value of transferred property shall be the single payment arm's-length price that would be paid for the property by an unrelated purchaser determined in accordance with the principles of section 482 and regulations thereunder. The allocation of a portion of the purchase price tointangible property agreed to by the parties to the transaction shall not necessarily be controlling for this purpose.

(6) *Anti-abuse rule.* If a U.S. person—

(i) Transfers intangible property to a domestic corporation with a principal purpose of avoiding the effect of section 367(d) and the rules of this section; and

(ii) Thereafter transfers the stock of that domestic corporation to a related foreign corporation,

then solely for purposes of section 367(d) that U.S. person shall be treated as having transferred the intangible property directly to the foreign corporation. A U.S. person shall be presumed to have transferred intangible property for a principal purpose of avoiding the effect of section 367(d) if the property is transferred to the domestic corporation less than two years prior to the transfer of the stock of that domestic corporation to a foreign corporation. The presumption created by the previous sentence may be rebutted by clear evidence that the subsequent transfer of the stock of the domestic transferee corporation was not contemplated at the time the intangible property was transferred to that corporation and that avoidance of section 367(d) and the rules of this section was not a principal purpose of the transaction. A transfer may have more than one principal purpose.

(h) *Related person.* for purposes of this section, persons are considered to be related if—

(1) They are partners or partnerships described in section 707(b)(1) of the Code; or

(2) They are related within the meaning of section 267(b), (c), and (f) of the Code, except that—

(i) "10 percent or more" shall be substituted for "more than 50 percent" each place it appears; and

(ii) Section 1563 shall apply (for purposes of section 267(f)), without regard to section 1563(b)(2).

(i) *Effective date.* Except as specifically provided to the contrary elsewhere in this section, this section applies to transfers occurring after December 31, 1984.

Par. 6. Section 1.6038B-1T is added immediately after §1.6038A-1, to read as follows:

§1.6038B-1T Reporting of transactions described in section 367 (temporary).

(a) *Purpose and scope.* This section sets forth information reporting requirements under section 6038B, concerning certain transfers of property to foreign persons. Paragraph (b) of this section provides general rules explaining when and how to carry out the reporting required under section 6038B. Paragraphs (c) and (d) of this section specify the information that is required to be reported with respect to transfers of property that are described in section 367(a) and (d), respectively. Finally, paragraph (f) of this section sets forth the consequences of a failure to comply with the requirements of section 6038B and this section. Except as specifically provided to the contrary elsewhere in this section, this section applies to transfers occurring after December 31, 1984.

(b) *Time and manner of reporting*—(1) *In general.* Any U.S. person that is required to report pursuant to section 6038B and the rules of this section must attach the required information to Form 926 (Return by Transferor of Property to a Foreign corporation, Foreign Estate or Trust, or Foreign Partnership). Form 926 and the required attachments must be filed at the Internal Revenue Service Center where the U.S. person is required to file its Federal income tax return. Notwithstanding any statement to the contrary on Form 926, the form and attachments must be filed with the transferor's tax return for the taxable year that includes the date of the transfer (as defined in paragraph (b)(3) of this section). However, in the case of a transfer that occurred prior to June 16, 1986, Form 926 and the required attachments must be filed by September 16, 1986, if that date is later than the date the filing would otherwise be required under the preceding sentence. Section 7502 and regulations thereunder shall apply in determining whether the form and attachments are timely filed. Any attachment to Form 926 required under the rules of this section is filed subject to the transferor's declaration under penalties of perjury on Form 926 that the information submitted is true, correct, and complete to the best of the transferor's knowledge and belief.

(2) *Person required to file*—(i) *In general.* Form 926 and the attachments required under the rules of this section must be filed by each U.S. person that makes a transfer described in section 367(a) or (d). No notice shall be required under this section with respect to a distribution described in section 367(e). No notice shall be required under this section with respect to a transfer of stock of securities described in §1.367(a)-3T(f)(1) or with respect to a transfer described in section 367(a)(2). If two or more persons transfer jointly-owned property to a foreign corporation in a transfer with respect to which a notice is required under this section, then each person must report with respect to the particular interest he transferred, specifying the nature and extent of the interest. However, a husband and wife (and their minor children) may jointly file a single information return. If two or more U.S. persons owning stock or securities in a corporation transfer such stock or securities to a foreign corporation in the same translation, then the corporation whose stock or securities are transferred may, at its choice, file the notice required by this section on behalf of its shareholders. In that case, a single form 926, signed by the responsible officer of the corporation, shall be filed, containing the required information with respect to each shareholder, other than shareholders described in §1.367(a)-3T(f)(1).

(ii) *Indirect transfers.* If a U.S. person that holds an interest in an entity is considered to make an indirect transfer (when the entity transfers property to a foreign corporation) under the provisions of—

(A) Section 367(a)-1T(c)(2)(i)(B) (concerning mergers to which section 368(a)(2)(D) applies);

(B) Section 367(a)-1T(c)(2)(i)(C) (concerning mergers to which section 368(a)(2)(E) applies);

(C) Section 367(a)-1T(c)(2)(ii) (concerning reorganizations described in section 368(a)(1)(B));

(D) Section 367(a)-1T(c)(2)(iii) (concerning reorganizations described in section 368(a)(1)(C));

(E) Section 367(a)-1T(c)(3)(i) (concerning transfers of property by a partnership); or

(F) Section 367(a)-1T(c)(4) (concerning transfers of property by a trust or estate),

then the requirements of this section shall apply with respect to each such person. However, the requirements of this section may be satisfied by the entity, on behalf of its interest-holders, by the filing of a single information return containing the required information with respect to each interest-holder (other than persons described in §1.367(a)-3T(f)(1)) that is considered to make a transfer described in section 367(a). If the entity chooses to satisfy the requirements of this section on behalf of its interest-holders, Form 926 must be signed by a responsible officer in the case of a corporation, by a general partner in the case of a partnership, and by a trustee, executor, or equivalent fiduciary in the case of a trust or estate.

(3) *Date of transfer*—(i) *In general.* for purposes of this section, the date of a transfer described in section 367 is the first date on which title to, possession of, or rights to the use of stock, securities, or other property passes pursuant to the plan for purposes of subtitle A of the Internal Revenue Code. A transfer will not be considered to begin with a decision on a board of directors or similar action unless the transaction otherwise takes effect for purposes of subtitle A of the Internal Revenue Code on that date.

(ii) *Termination of section 1504(d) election.* A transfer deemed to occur as a result of the termination of an election under section 1504(d) will be considered to occur on the date the contiguous country corporation first fails to continue to qualify for the election under section 1504(d). The rule of this paragraph (b)(3)(ii) is illustrated by the following example.

Example. Domestic corporation W previously made a valid election under section 1504(d) to have its Mexican subsidiary S treated as a domestic corporation. On August 1, 1986, W disposes of its right, title, and interest in 10 percent of the stock of S by selling such stock to an unrelated United States person who is not a director of S. S first fails to continue to qualify for the election under section 1504(d) on August 1, 1986, since on such date it ceases to be directly or indirectly wholly owned or controlled by W. The construction transfer of assets from "domestic" corporation S to Mexican corporation S is considered to occur on that date.

(iii) *Change in classification.* A transfer deemed to occur as a result of a change in classification of an entity caused by a change in the governing documents, articles, or agreements of the entity (as described in §1.367(a)-1T(c)(6)) will be considered to occur on the date that such changes take effect for purposes of subtitle A of the Internal Revenue Code.

(iv) *U.S. resident under section 6013(g) or (h).* A transfer made by an alien individual who is considered to be a U.S. resident by reason of a timely election under section 6013(g) or (h) will be considered to occur, for purposes of this section (but not for purposes of section 367), on the later of—

(A) The date on which the election under section 6013(g) or (h) is made; or

(B) The date on which the transfer would otherwise be considered to occur under the rules of this paragraph (b)(3).

The rule of this paragraph (b)(3)(iv) is illustrated by the following example.

Example. D is a nonresident alien individual who is married to a United States citizen. On March 1, 1986, D transfers property to a foreign corporation in an exchange described in section 351. On April 15, 1987, D and the spouse timely file with their tax return for the taxable year ended December 31, 1986, an election under section 6013(g) for D to be treated as a United States resident. The election is effective on January 1, 1986. For purposes of section 6038B, the transfer described in section 367(a) made by D in connection with the section 351 exchange is considered to occur on April 15, 1987, the date on which the timely election was made under section 6013(g).

(c) *Information required with respect to transfers described in section 367(a)(1)*. A U.S. person that transfers property to a foreign corporation in an exchange described in section 367(a)(1) (other than a transfer described in section 367(a)(2)) must provide the following information in paragraphs labelled to correspond with the number or letter set forth below. If a particular item is not applicable to the subject transfer, list its heading and state that it is not applicable.

(1) *Transferor*. Provide the name, U.S. taxpayer identification number, and address of the U.S. person making the transfer.

(2) *Transfer*. Provide the following information concerning the transfer:

(i) Name, U.S. taxpayer identification number (if any), address, and country of incorporation of transferee foreign corporation;

(ii) A general description of the transfer, and any wider transaction of which it forms a part, including a chronology of the transfers involved and an identification of the other parties to the transaction to the extent known.

(3) *Consideration received*. Provide a description of the consideration received by the U.S. person making the transfer, including its estimated fair market value and, in the case of stock or securities, the class or type, amount, and characteristics of the interest received.

(4) *Property transferred*. Provide a description of the property transferred. The description must be divided into the following categories, and must include the estimated fair market value and adjusted basis of the property, as well as any additional information specified below.

(i) *Active business property*. Describe any transferred property (other than stock or securities) to be used in the active conduct of a trade or business outside of the United States. Provide here a general description of the business conducted (or to be conducted) by the transferee, including the location of the business, the number of its employees, the nature of the business, and copies of the most recently prepared balance sheet and profit and loss statement. Property listed within this category may be identified by general type. For example, upon the transfer of the assets of a manufacturing operation, a reasonable description of the property to be used in the business might include the categories of office equipment and supplies, computers and related equipment, motor vehicles, and several major categories of manufacturing equipment. However, any property that is includible both in this subdivision (i) and in subdivision (iii) of this paragraph (c)(4) (property subject to depreciation recapture under §1.367(a)-4T(b)) must be identified in the manner required in subdivision (iii). If property is considered to be transferred for use in the active conduct of a trade or business under a special rule in §1.367(a)-4T, specify the applicable rule and provide information supporting the application of the rule. If property is subject to section 367(a)(1) regardless of its use in a trade or business under the rules of §§1.367(a)-4T or 1.367(a)-5T, list the property only in response to subdivision (vii) of this paragraph (c)(4).

(ii) *Stock or securities*. Describe any transferred stock or securities, including the class or type, amount, and chracteristics of the transferred stock or securities, as well as the name, address, place of incorporation, and general description of the corporation issuing the stock. In addition, provide the following information if applicable:

(A) *Active trade or business stock*. If the stock or securities are considered to be transferred for use in the active conduct of a trade or busines soutside of the United States under the rules of §1.367(a)-3T(d)(2), provide information supporting the application of the rule.

(B) *Application of special rules*. If any provision of §1.367(a)-3T applies to except the transfer of stock or securities from the rule of section 367(a)(1), provide information supporting the claimed application of such provision (including information supporting the nonapplicability of either anti-abuse rule under §1.367(a)-3T(h)). If the transferor is entering into an agreement to recognize gain upon a later disposition of the transferred stock by the transferee foreign corporation under §1.367(a)-3T(g), attach the agreement and waiver as required by the rules of that paragraph.

(iii) *Depreciated property*. Describe any property that is subject to depreciation recapture under the rules of §1.367(a)-4T(b). Property within this category must be separately identified to the same extent as was required for purposes of the previously claimed depreciation deduction. Specify with respect to each such asset the relevant recapture provision, the number of months in which such property was in use within the United States, the total number of months the property was in use, the fair market value of the property, a schedule of the depreciation deduction taken with respect to the property, and a calculation of the amount of depreciation required to be recaptured.

(iv) *Property to be leased*. Describe any property to be leased to other persons by the transferee foreign corporation (unless such property is considered to be transferred for use in the active conduct of a trade or business and was thus listed under subdivision (i) of this paragraph (c)(4)). If the rules of §1.367(a)-4T(c)(2) apply to except the transfer from the rule of section 367(a)(1), provide information supporting the claimed application of such provision.

(v) *Property to be sold*. Describe any transferred property that is to be sold or otherwise disposed of by the transferee foreign corporation, as described in §1.367(a)-4T(d).

(vi) *Transfers to FSCs*. Describe any property that is subject to the special rule of §1.367(a)-4T(g) for transfers to FSCs. Provide information supporting the claimed application of that rule.

(vii) *Tainted property*. Describe any property that is subject to §1.367(a)-5T (concerning property that is subject to the rule of section 367(a)(1) regardless of whether it is transferred for use in the active conduct of a trade or business outside of the United States). Such description must be divided into the relevant categories, as follows:

(A) *Inventory, etc.* Property described in §1.367(a)-5T(b);

(B) *Installment obligations, etc.* Property described in §1.367(a)-5T(c);

(C) *Foreign currency, etc.* Property described in §1.367(a)-5T(d);

(D) *Intangible property.* Property described in §1.367(a)-5T(e); and

(E) *Leased property.* Property described in §1.367(a)-4T(c).

If any exception provided in §1.367(a)-5T applies to the transferred property (making section 367(a)(1) not applicable to the transfer), provide information supporting the claimed application of such exception.

(viii) *Foreign loss branch.* Provide the information specified in paragraph (c)(5) of this section.

(ix) *Other intangibles.* Describe any intangible property sold or licensed by the transferor to the transferee foreign corporation, and set forth the general terms of each sale or license.

(5) *Transfer of foreign branch with previously deducted losses.* If the property transferred is property of a foreign branch with previously deducted losses subject to the rule of §1.367(a)-6T, provide the following information:

(i) *Branch operation.* Describe the foreign branch the property of which is transferred, in accordance with the definition of §1.367(a)-6T(g).

(ii) *Branch property.* Describe the property of the foreign branch, including its adjusted basis and fair market value. For this purpose property must be identified with reasonable particularity, but may be identified by category rather than listing every asset separately. Substantially similar property may be listed together for this purpose, and property of minor value may be grouped into functional categories. For example, a reasonable description of the property of a business office might include the following categories: word processing or data processing equipment, other office equipment and furniture, and office supplies.

(iii) *Previously deducted losses.* Set forth a detailed calculation of the sum of the losses incurred by the foreign branch before the transfer, and a detailed calculation of any reduction of such losses, in accordance with §1.367(a)-6T(d) and (e).

(iv) *Character of gain.* Set forth a statement of the character of the gain required to be recognized, in accordance with §1.367(a)-6T(c)(1).

(d) *Transfers subject to section 367(d)*—(1) *Initial transfer.* A U.S. person that transfers intangible property to a foreign corporation in an exchange described in section 351 and 361 must provide the following information in paragraphs labelled to correspond with the number or letter set forth below. If a particular item is not applicable to the subject transfer, list its heading and state that it is not applicable. The information required by subdivisions (i) through (iii) need only be provided if such information was not otherwise provided under paragraph (c) of this section. (Note that the U.S. transferor may subsequently be required to file another return under paragraph (d)(2) of this section.)

(i) *Transferor.* Provide the name, U.S. taxpayer identification number, and address of the U.S. person making the transfer.

(ii) *Transfer.* Provide information concerning the transfer, including:

(A) Name, U.S. taxpayer identification number (if any), address, and country of incorpoartion of the transferee foreign corporation;

(B) A general description of the transfer, and any wider transaction of which it forms a part, including a chronology of the transfer involved and an identification of the other parties to the transaction to the extent known.

(iii) *Consideration received.* Provide a description of the consideration received by the U.S. person making the transfer, including its estimated fair market value and, in the case of stock or securities, the class or type, amount, and characteristics of the interest received.

(iv) *Intangible property transferred.* Provide a description of the intangible property transferred, including its adjusted basis. Generally, each intangible asset must be separately identified. Operating intangibles and foreign goodwill or going concern value, as defined in §1.367(a)-1T(d)(5)(ii) and (iii), should be so identified and classified.

(v) *Annual payment.* Provide and explain the calculation of the annual deemed payment for the use of the intangible property required to be recognized by the transferor under the rules of section 367(d).

(vi) *Election to treat as sale.* List any intangible with respect to which an election is being made under §1.367(d)-1T(g)(2) to treat the transfer as a sale. Include the fair market value of the intangible on the date of the transfer and a calculation of the gain required to be recognized in the year of the transfer by reason of the election.

(vii) *Coordination with loss rules.* List any intangible property subject to section 367(d) the transfer of which also gives rise to the recognition of gain under section 904(f)(3) or §1.367(a)-6T. Provide a calculation of the gain required to be recognized with respect to such property, in accordance with the provisions of §1.367(d)-1T(g)(4).

(viii) *Other intangibles.* Describe any intangible property sold or licensed by the transferor to the transferee foreign corporation, and set forth the general terms of each sale or license.

(2) *Subsequent transfers.* If a U.S. person transfers intangible property to a foreign corporation in an exchange described in section 351 or 361, and at any time thereafter (within the useful life of the intangible property) either that U.S. person disposes of the stock of the transferee foreign corporation or the transferee foreign corporation disposes of the transferred intangible, then the U.S. person must provide the following information in paragraphs labelled to correspond with the number or letter set forth below. The information required by subdivisions (i) and (ii) need only be provided if such information was not otherwise provided in the same return, pursuant to paragraph (c) or (d)(1) of this section. For purposes of determining the date on which a return under this subparagraph (2) is required to be filed, the date of transfer is the date of the subsequent transfer of stock or intangible property.

(i) *Transferor.* Provide the name, U.S. taxpayer identification number, and address of the U.S. person making the transfer.

(ii) *Initial transfer.* Provide the following information concerning the initial transfer:

(A) The date of the transfer;

(B) The name, U.S. taxpayer identification number (if any), address, and country of incorporation of the transferee foreign corporation; and

(C) A general description of the

transfer and any wider transaction of which it formed a part.

(iii) *Subsequent transfer.* Provide the following information concerning the subsequent transfer:

(A) A general description of the subsequent transfer and any wider transaction of which it forms a part;

(B) A calculation of any gain required to be recognized by the U.S. person under the rules of §1.367(d)-1T(d) through (f); and

(C) The name, address, and identifying number of each person that under the rules of §1.367(d)-1T(e) and (f) will be considered to receive contingent annual payments for the use of the intangible property.

(e) *Transfers subject to section 367(e).* [Reserved]

(f) *Failure to comply with reporting requirements*—(1) *Consequences of failure.* If a U.S. person is required to file a notice under §1.6038B-1T(b) and fails to comply with the applicable reporting requirements of section 6038B and this section, then with respect to the particular property as to which there was a failure to comply—

(i) That property shall not be considered to have been transferred for use in the active conduct of a trade or business outside of the United States, for purposes of section 367(a) and regulations thereunder;

(ii) The U.S. person shall pay a penalty equal to 25 percent of the amount of gain realized on the exchange of that property (without regard to whether gain is recognized on the transfer); and

(iii) The period of limitations on assessment of tax upon the transfer of that property shall not begin to run until the date on which the transferor does comply with the applicable reporting requirements.

Thus, the time for assessment of tax is extended indefinitely if the transferor's failure to comply is continued indefinitely.

(2) *Failure to comply.* A failure to comply with the requirements of section 6038B is—

(i) The failure to report at the proper time and in the proper manner any material information required to be reported under the rules of this section; or

(ii) The provision of false or inaccurate information is purported compliance with the requirements of this section.

Thus, a transferor that timely files Form 926 with the attachments required under the rules of this section shall, nevertheless, have failed to comply if, *for example*, the transferor reports therein that property will be used in the active conduct of a trade or business outside of the United States, but in fact such property continues to be used in a trade or business within the United States.

(3) *Reasonable cause exception.* The provisions of paragraph (f)(1) of this section shall not apply if the transferor shows that a failure to comply was due to reasonable cause and not willful neglect. The transferor may do so by providing a written statement to the district director having jurisdiction of the taxpayer's return for the year of the transfer, setting forth the reasons for the failure to comply. Whether a failure to comply was due to reasonable cause shall be determined by the district director under all the facts and circumstances.

Par. 7. The authority for Part 7 is amended by adding the following citation:

Authority: 26 USC 7805. * * * Section 7.367(b)-1 and 7.367(b)-4 also issued under 26 USC 367(b).

Par. 8. Section 7.367(b)-1 is amended by removing the last sentence of paragraph (a) and adding in lieu thereof the following two new sentences.

§7.367(b)-1 Other transfers.

(a) *Scope.* * * * An exchange to which section 367(b) applies is an exchange described in section 367(b) and in section 332, 351, 354, 355, 356, or 361 with respect to which the status of a foreign corporation as a corporation is relevant for determining the extent to which gain shall be recognized and in connection with which there is no transfer described in section 367(a). An election by a domestic corporation under section 1504(d) to treat a corporation organized under the laws of a contiguous foreign country as a domestic corporation shall be considered to be a transfer of property made pursuant to an exchange to which section 367(b) applies.

Par. 9. Section 7.367(b)-4 is amended by revising paragraph (b)(2)(ii) to read as follows:

§7.367(b)-4 Certain exchanges described in more than one Code provision.

* * * * *

(b) *Treatment of certain exchanges described in both section 354 and in either section 351 or 361.*

* * * * *

(2) *Exceptions.* * * *

(ii) *Specified treatment.* If an exchange of stock in a foreign corporation by a U.S. person is an exchange to which the rules under section 367(a) apply, then the gain required to be included in gross income under paragraph (b)(1)(i)(B) or paragraph (b)(1)(ii) of this section shall not be required to be immediately recognized under this paragraph (b), and instead the transaction shall be treated in accordance with the regulations under section 367(a). See §1.367(a)-3T.

Par. 10. The authority citation for Part 602 is as follows:

Authority: 26 USC 7805

Par. 11. Section 602.101(c) is amended by inserting in the appropriate place in the table "§1.367(a)-1T . . . .
1545-0026" "§1.367(a)-2T . . . .
1545-0026" "§1.367(a)-3T . . . .
1545-0026" "§1.367(a)-6T . . . .
1545-0026" "§1.367(d)-1T . . . .
1545-0026" "§1.6038B-1T . . . .
1545-0026"

* * * * *

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved April 29, 1986.

J. ROGER MENTZ,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on May 15, 1986, 8:45 a.m., and published in the issue of the Federal Register for May 16, 1986, 51 F.R. 17936)

Section 6038B.—Notice of Certain Transfers to Foreign Persons

26 CFR 1.6038B-1T: Reporting of transactions described in section 367 (temporary).

Information reporting requirements concerning certain transfers of property to foreign persons. See T.D. 8087, page 5.

Section 7805.—Rules and Regulations

26 CFR 301.7805-1: Rules and regulations.

Nonretroactive application of a revenue ruling relating to whether contributions made by a commodities trader to a Board of Trade Gratuity Fund are deductible as business expenses. See Rev. Rul. 86-80, page 4.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Transfers of Property by U.S. Persons to Foreign Corporations

LR-3-86

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary regulations that add new §§1.367(a)-1T through 1.367(a)-6T, relating to transfers of property by U.S. persons to foreign corporations, new §1.367(d)-1T, relating to transfers of intangible property by U.S. persons to foreign corporations, and new §1.6038B-1T, relating to reporting of transactions described in section 367. The text of the new sections also serves as the comment document for this notice of proposed rulemaking.

DATES: Written comments and requests for a public hearing must be delivered or mailed before July 15, 1986. The regulations are proposed generally to apply to transfers made after December 31, 1984.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T [LR-3-86], Washington, DC 20224.

FOR FURTHER INFORMATION CONTACT: Charles W. Culmer of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC 20224, (Attention: CC:LR:T) (202-566-4336, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

The temporary regulations published * * * [on page 5, this Bulletin] add new §§1.367(a)-1T, 1.367(a)-2T, 1.367(a)-3T, 1.367(a)-4T, 1.367(a)-5T, 1.367(a)-6T, 1.367(d)-1T, and 1.6038B-1T to 26 CFR Part 1. The final regulations that are proposed to be based on these temporary regulations would amend 26 CFR Part 1 by adding these new temporary regulation sections as final regulation sections under sections 367 and 6038B of the Internal Revenue Code of 1954. For the text of the temporary regulations, see FR Doc. 80-10831 [T.D. 8087] published * * * [on page 5, this Bulletin].

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. The Secretary of the Treasury has certified that this rule will not have a significant impact on a substantial number of small entities. Few small entities would be affected by these regulations. A regulatory flexibility analysis, therefore, is not required under the Regulatory Flexibility Act (5 U.S.C. chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER. The collection of information requirements contained herein have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on the requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, DC 20503. The Internal Revenue Service requests persons submitting comments to OMB to also send copies of the comments to the Service.

DRAFTING INFORMATION

The principal author of this regulation is Charles W. Culmer of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of substance and style.

* * * * *

Proposal of regulations

The temporary regulations, FR Doc. 80-10831 [T.D. 8087] published * * * [on page 5, this Bulletin], are hereby also proposed as final regulations under section 367 and 6038B of the Internal Revenue Code of 1954.

ROSCOE L. EGGER JR.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on May 15, 1986, 8:45 a.m., and published in the issue of the Federal Register for May 16, 1986, 51 F.R. 17990)

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Mack I. Frank	Eunice, LA	Attorney	Indefinite from April 1, 1986
Carl Goldfarb	Charlotte, NC	Attorney	Indefinite from April 28, 1986
Dennis M. Hayes	Ann Arbor, MI	Attorney	Indefinnite from April 15, 1986
Ronald N. Kief	Warren, MI	Certified Public Accountant	Two Years from June 1, 1986
Richard L. Leopold	Ottawa, OH	Attorney	Three Months from May 1, 1986
Julius Stackel	Flushing, NY	Certified Public Accountant	Thirty Months from April 15, 1986
John Such	Lyndhurst, OH	Enrolled Agent	Eighteen Months from April 22, 1986

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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____	1927-1	$8.00
____	*1927-2*	*18.00*
____	1928-1	8.00
____	1928-2	10.00
____	1929-1	13.00
____	*1929-2*	*3.50*
____	1930-1	8.50
____	1930-2	10.00
____	*1931-1*	*4.00*
____	1931-2	14.00
____	*1932-1*	*3.25*
____	1932-2	10.00
____	*1933-1*	*3.75*
____	*1933-2*	*4.00*
____	*1934-1*	(**)
____	1934-2	15.00
____	1935-1	8.00
____	*1935-2*	*15.00*
____	*1936-1*	*4.00*
____	*1936-2*	*15.00*
____	*1937-1*	*14.00*
____	1937-2	8.50
____	*1938-1*	*17.00*
____	*1938-2*	*14.00*
____	1939-1-1	9.50
____	1939-1-2	12.00
____	1939-2	10.00
____	1940-1	6.50
____	1940-2	15.00
____	1941-1	8.00
____	*1941-2*	*4.00*
____	1942-1	8.00
____	*1942-2*	*6.50*
____	*1943-(*)*	*11.00*
____	*1944-(*)*	*9.00*
____	1945-(*)	10.00
____	*1946-1*	*3.00*
____	1946-2	6.00
____	*1947-1*	*2.00*
____	1947-2	3.75
____	*1948-1*	*3.50*
____	1948-2	8.50
____	*1949-1*	*8.00*
____	*1949-2*	*3.25*
____	1950-1	7.00
____	*1950-2*	*5.50*
____	*1951-1*	*13.00*
____	*1951-2*	*6.00*
____	*1952-1*	*3.00*
____	1952-2	8.00
____	*1953-1*	*4.75*
____	1953-2	13.00
____	1954-1	13.00
____	1954-2	13.00
____	1955-1	11.00
____	1955-2	14.00
____	1956-1	17.00
____	1956-2	20.00
____	1957-1	18.00
____	1957-2	(**)
____	1958-1	11.00
____	1958-2	(**)
____	1958-3	17.00
____	1959-1	19.00
____	1959-2	11.00
____	1960-1	21.00
____	1960-2	13.00
____	1961-1	15.00
____	1961-2	11.00
____	1962-1	15.00
____	1962-2	14.00
____	1962-3	22.00
____	1963-1	10.00
____	1963-2	12.00
____	1964-1-1	11.00
____	1964-1-2	12.00
____	1964-2	28.00
____	1965-1	19.00
____	1965-2	13.00
____	1966-1	15.00
____	1966-2	15.00
____	1967-1	11.00
____	1967-2	17.00
____	1968-1	15.00
____	1968-2	13.00
____	1969-1	15.00
____	1969-2	7.50
____	1969-3	14.00
____	1970-1	12.00
____	1970-2	(**)
____	1971-1	12.00
____	1971-2	17.00
____	1972-1	15.00
____	1972-2	15.00
____	1973-1	18.00
____	1973-2	15.00
____	1974-1	12.00
____	1974-2	11.00
____	*1974-3*	9.50
____	1974-3 Supp.	11.00
____	1975-1	15.00
____	1975-2	14.00
____	1976-1	12.00
____	1976-2	11.00
____	1976-3-1	10.00
____	1976-3-2	18.00
____	1976-3-3	11.00
____	1977-1	12.00
____	1977-2	13.00
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Internal Revenue

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Highlights of this Issue

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-81, page 12.

Percentage depletion; gross income from mining. If a lessor purchases extracted mineral from a lessee and applies section 614(c)(4)(A) of the Code processes to the mineral before reselling it at a profit, the proceeds are not considered gross income from mining and, therefore, are not subject to depletion.

Rev. Rul. 86-82 page 14.

Grantor trusts; loan from trust to grantor. A grantor-trustee is treated as owner of trust assets where grantor-trustee borrows trust funds and repays the funds with interest in the same year they were borrowed.

T.D. 8088, page 4.

LR-8-86, page 24.

Temporary and proposed regulations under section 338(g) of the Code relate to statements of election and due dates.

Announcement 86-74, page 24.

This Bulletin contains a list of organizations that no longer qualify as organizations contributions to which are deductible under section 170(c)(2) of the Code.

Announcement 86-75, page 25.

Form 3115, Application for Change in Accounting Method, has been revised. The form and its instructions are now available at most Internal Revenue Service district offices.

EXCISE TAXES

T.D. 8084, page 14.

Amendments to the regulations relate to second tier excise taxes.

Notice 86-7, page 23.

Windfall profit tax: inflation adjustment factor. For purposes of computing the windfall profit tax, the inflation adjustment for the quarter ending September 30, 1986, is 0.4614 for tier 1 or tier 2 oil and 0.6721 for tier 3 oil.

ADMINISTRATIVE

Announcement 86-76, page 25.

Guidance is provided to private foundations regarding Part V of the 1985 Form 990PF, Return of Private Foundation.

Announcement 86-77, page 25.

Form 5471, Information Return With Respect to a Foreign Corporation, its instructions, and Schedule M have been revised to reflect a change in the regulations under section 6038 of the Code.

Finding Lists begin on page 29.
Announcement of Suspensions on page 26.
Announcement of Notice of Proposed Rulemaking on page 27.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 338.—Certain Stock Purchases Treated as Asset Acquisitions

26 CFR 1.338-1T: Elections under section 338(g) of the Internal Revenue Code of 1954 (temporary).

T.D. 8088

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Temporary Regulations Under Section 338 of the Internal Revenue Code of 1954; Statements of Election and Due Dates

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations primarily relating to section 338(g) of the Internal Revenue Code of 1954 ("Code") as added by the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") [Pub. L. 97-248, 1982-2 C.B. 462]. The temporary regulations provide additional guidance to taxpayers concerning the filing of certain statements of election on or after December 9, 1985, and on or before July 15, 1986. An amendment to temporary regulations §1.338-4T clarifies the application of the mitigation of limitations provisions. The temporary regulations also extend the time for taking certain actions under section 338. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations cross-referenced * * * [on page 24, this Bulletin].

DATES: The temporary regulations under section 338(g) and the amendments to the temporary regulations generally are effective with respect to stock acquisitions made after August 31, 1982. New paragraph (m) of §1.338-1T is effective only with respect to elections under section 338 filed on or after December 9, 1985, and on or before July 15, 1986.

FOR FURTHER INFORMATION CONTACT: Thomas J. Kane of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) or telephone 202-566-3458 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document amends temporary regulations §§1.338-1T, 1.338-2T, 1.338-4T, 1.338-5T, and 1.338(h)(10)-1T in Part 1 of Title 26 of the Code of Federal Regulations ("CFR"). Section 1.338-1T was published as T.D. 7942 in the FEDERAL REGISTER on February 8, 1984 (49 FR 4722) [1984-1 C.B. 92], and was amended and redesignated (as §1.338-1T) by temporary regulations published as T.D. 7975 in the FEDERAL REGISTER on September 6, 1984 (49 FR 35086) [1984-2 C.B. 81]. Section 1.338-1T also was amended by temporary regulations published as T.D. 8021 in the FEDERAL REGISTER on April 25, 1985 (50 FR 16402) [1985-1 C.B. 96]. The temporary regulations published on April 25, 1985, also added §1.338-4T. Sections 1.338-1T and 1.338-4T were amended by temporary regulations published as T.D. 8068 in the FEDERAL REGISTER on January 8, 1986 [1986-8 I.R.B. 9], and by temporary regulations published as T.D. 8072 in the FEDERAL REGISTER on January 29, 1986 [1986-11 I.R.B. 7]. The temporary regulations published on January 8, 1986, also added §1.338(h)(10)-1T. All these temporary regulations were further amended by temporary regulations published as T.D. 8074 published in the FEDERAL REGISTER on February 12, 1986 [1986-15 I.R.B. 4], which also added §1.338-5T. The temporary regulations amended by this document will remain in effect until superseded by later temporary or final regulations relating to these matters.

The amendments made by this document are primarily under section 338(g). That provision was originally added by section 224 of TEFRA (Pub. L. No. 97-248; 96 Stat. 485) [1982-2 C.B. 462] and was amended by section 712(k) of the Tax Reform Act of 1984 (Pub. L. 98-369; 98 Stat. 946) [1984-3 C.B. (Vol. 1) 1, 456]. Other amendments are briefly discussed at the end of this preamble.

OPERATION OF SECTION 338

In general

Section 338 generally provides that, if a corporation ("target") is acquired by another corporation ("purchasing corporation") in a qualified stock purchase, the purchasing corporation may elect (or may be deemed to elect under certain consistency rules) to have the target treated as if it: (1) sold all of its assets (as "old target") at fair market value at the close of the day on which the qualified stock purchase occurred ("acquisition date") and (2) purchased those assets as a new corporation ("new target") at the beginning of the following day for an amount generally equal to the price paid by the purchasing corporation for target stock plus liabilities of target and other relevant items. Section 338(a) and (b). The deemed sale of assets by old target generally is governed by the nonrecognition rule of section 337. In general, the tax attributes of old target are not available to new target. The net effect of a section 338 election is that the purchasing corporation obtains a basis in target assets that generally reflects the price it paid for target stock.

Effect of section 338 election on taxable year

Once a valid section 338 election has been made, old target's taxable year ends as of the close of business on the acquisition date. If the selling and purchasing groups each file separate returns (as opposed to consolidated returns) and the acquisition date occurs on a day other than the last day of target's regular taxable year, then the Federal income tax return (filed prior to making the section 338 election) for the relevant taxable year which includes the acquisition date should be amended and two separate amended returns should be filed as a result of the section 338 election. The first amended return would cover the portion of that relevant taxable year through the close of business on the acquisition date, which would include any additional Federal tax due because of target's deemed sale of assets under section 338. The second amended return would cover the balance of target's taxable year (relating to target's operations) subsequent to the acquisition date.

The impact of a section 338 election on target's taxable year will be different if old target was a subsidiary in an affiliated group that filed a consolidated return for the period that included the acquisition date and an election under section 338(h)(10) is not made. In such case, the deemed sale will be the only transaction reported on old target's final return (called a "deemed sale return"). The Federal income tax consequences of target's operations through the close of business on the acquisition date shall continue to be reported on the selling group's consolidated return for the taxable period which included the acquisition date. Likewise, the Federal income tax consequences of target's operations for the remainder of target's regular taxable year shall continue to be reported either on the purchasing group's consolidated return or on a separate return for target if the purchaser was not included on a consolidated return.

EXPLANATION OF PROVISIONS

These temporary regulations provide procedures in new paragraph (m) of §1.338-1T for filing and for perfecting certain statements of election under section 338(g) for statements of election filed on or after December 9, 1985, and on or before July 14, 1986. The time for making such an election is extended by these regulations to the later of the 15th day of the ninth month beginning after the month in which the acquisition date occurs or July 15, 1986. See News Release IR-86-18, dated February 27, 1986.

For elections which do not require the filing of a deemed sale return, the procedures in new paragraph (m) condition the election on either filing consents which postpone the expiration of the statute of limitations or filing closing agreements which waive the expiration of the statute of limitations and extend the period for assessment. These new procedures are applicable for each relevant taxable year for which the statute of limitation of assessment has expired or will expire on or before November 15, 1986. A relevant taxable year is one for which a Federal income tax return was filed prior to filing the statement of section 338 election, but only if there would be an increase or decrease in Federal income tax as a result of the election. Additionally, new paragraph (m) conditions an effective section 338 election upon the filing of a closing agreement in situations where a deemed sale return must be filed as a result of the section 338 election. Standard language for these agreements is prescribed in this document for the convenience of both taxpayers and the Internal Revenue Service.

The procedures described in these regulations are required whether the tax for the period affected would be increased or decreased. Increased tax may arise, for example, by reason of income or tax credit recapture caused by the deemed sale by old target and by tax attributes of old target not carrying over to new target. An example that results in a decrease in tax is higher depreciation or a similar deduction for new target that arises by reason of the deemed purchase under section 338(a)(2) by new target of assets that had a tax basis in the hands of old target lower than new target's tax basis.

Statute of limitations

As previously described, the section 338 election may create two taxable periods within a relevant taxable year which otherwise would be properly accounted for as a single taxable year before the statement of election was filed. If new target chooses the same taxable year that old target used, and if target had filed a tax return for the relevant taxable year which includes the acquisition date, the statute of limitations for any short period which may arise (as a consequence of the section 338 election) starts to run under new §1.338-1T(m)(10) on the date on which target is considered to have filed under section 6501(b) its tax return for that relevant taxable year. For example, if target is a calendar year taxpayer and a qualified stock purchase of its stock is made on December 1, 1982, the statute of limitations for target's year ending December 1, 1982 (a short period which results from the section 338 election) would begin to run on the date target is considered to have filed its return for its taxable year ending December 31, 1982.

A deemed sale return cannot be filed prior to the filing of a section 338 election. Accordingly, the statute of limitations will not begin to run until the deemed sale return is filed. See section 6501(a) and section 6501(b)(1). The closing agreements required by new paragraph (m) of §1.338-1T in these situations reflect this rule of law.

Consents to extend statute of limitations

Section 1.338-1T(m) provides for procedures in circumstances when the statement of section 338 election is filed and the statute of limitations for a relevant taxable year of target, affected target, or corporate transferee expires after August 15, 1986, and on or before November 15, 1986. As a condition for making a section 338 election, the target, affected target, or corporate transferee is required to extend under section 6501(c)(4) the period for making an assessment for each such relevant taxable year until May 15, 1987. Unless such requirement is satisfied, the statement of section 338 election is ineffective unless such condition is waived by the District Director.

The extensions required by these regulations are necessary to ensure that taxpayers do not avoid the burdens of a section 338 election while retaining its benefits. The extensions will also have the effect of extending the period to file claim for refund. The extension date of May 15, 1987, was chosen to avoid requiring taxpayers to extend the period within which an assessment can be made for a period of less than 6 months and, for administrative convenience in order to provide a uniform date to which extensions would be made. The consent procedures in §1.338-1T(m) apply only if the statute of limitations on assessment will not otherwise expire on or before August 15, 1986.

Closing agreements— no deemed sale returns

If for a relevant taxable year the statute of limitations has already expired or will expire on or before August 15, 1986, new paragraph (m) of §1.338-1T also provides that an express election filed on or after December 9, 1985, and on or before July 15, 1986, is conditioned upon filing a closing agreement executed by target, affected target or corporate transferee wherein they (1) agree to waive the statute of limitations which has expired or is about to expire, (2) agree to file on or before November 3, 1986, amended returns which reflect the consequences of the deemed sale of assets under section 338(a)(1), and (3) agree to extend the statute of limitations for assessment of any additional tax due as a result of the deemed sale of assets until June 15, 1988. The election will be ineffective unless this condition is satisfied or is waived by the District Director.

It should be noted that even if each of the conditions for an effective election pursuant to this regulation are satisfied, certain adverse consequences may result in the event that an amended return reflecting the deemed sale is filed after July 15, 1986, and on or before November 3, 1986. Section 1.338-1T(h) of the existing temporary regulations generally permits waivers of certain additions to tax and time to act only if any required amended return is filed and certain other corrective action is taken on or before the last day for making an election under section 338. Also, section 1.338-1T(f)(7) permits a new target to adopt on its first return a taxable year other than the one target used before making the section 338 election, but only if that first return is filed on or before the last day for making an express election under section 338.

Except in the event a section 338(h)(10) election is made, the statement of section 338 election will also be ineffective if the amended return described in any closing agreement is not filed on or before the time required by the agreement unless the District Director waives this additional requirement. If a selling group participates in a section 338(h)(10) election, the selling group must agree to file an amended consolidated return which reports the deemed sale gain. However, the section 338 election and the section 338(h)(10) election are not ineffective if the amended consolidated return is not filed. This rule protects target and its purchaser from an act of omission which is beyond their control.

Section 6401(a) provides that any amount of a payment of any internal revenue tax which is assessed or collected after the expiration of the period of limitation properly applicable thereto is an overpayment. By entering into a closing agreement which waives and extends the applicable statute of limitations, any tax reported, paid, and collected as a result of the deemed sale of assets is not an overpayment within the meaning of section 6401(a).

In general, the reasons for these closing agreement procedures are similar to the reasons previously explained in this document for the requirements for consents to extend the statute of limitations. The August 15, 1986, cutoff date for the expiration of the statute of limitations for closing agreements in those cases where a deemed sale return is not required was selected in order to allow the Internal Revenue Service a reasonable amount of time to process the required documents and affix the appropriate signatures and for purposes of taxpayer convenience.

Closing agreements—deemed sale returns or combined deemed sale returns

A closing agreement is also required if a deemed sale return must be filed as a result of a section 338 election. The closing agreement procedures require that a deemed sale return or a combined deemed sale return must be filed on or before November 3, 1986, and that the statute of limitations with respect to a deemed sale return or a combined deemed sale return will not terminate prior to the expiration of three years from the date a deemed sale return or combined deemed sale return is considered filed.

Effective date

After December 6, 1985, the public was on notice that the Internal Revenue Service was going to consider the publication of rules dealing with "elections made in circumstances when the statute of limitations has expired or is about to expire for certain taxable years (such as might be the case for target's taxable year that includes the acquisition date)." See IRS News Release IR-85-115. December 9, 1985, was selected as the effective date for the procedures in new paragraph (m) because it was the first business day following the release of News Release IR-85-115.

Elections for which perfection is required

If a statement of section 338 election filed on or after December 9, 1985, and on or before July 15, 1986, does not meet the requirements in new paragraph (m)(2) of §1.338-1T, which includes the filing of consents to extend the statute of limitations or certain closing agreements, then the election may be perfected by refiling in accordance with those requirements on or before July 15, 1986.

District Director discretion

For a statement of section 338 election filed on or before July 15, 1986, the District Director (or his delegate) has discretion to waive any requirement in new paragraph (m)(2) of §1.338-1T, including the requirement of filing any amended return as prescribed by closing agreement. This discretion is to be exercised in connection with the examination of any Federal income tax return which would be affected by a section 338 election and is to be exercised on the basis of all the relevant facts and circumstances.

Mitigation

In the absence of a section 338(h)(10) election, any tax due in any closed taxable year as the result of a section 338 election made after the close of such year may be collected through the operation of the mitigation provisions (sections 1311-1314). Section 1.338-4T(l)(5), added by this document, points out that old target and new target are the same "taxpayer" for purposes of the mitigation provisions. Although section 338(a)(2) treats target as a "new corporation" for the purpose of having "purchased all the assets" of old target "as of the beginning of the day after the acquisition date", the legislative history makes it clear that new target and old target may be regarded as the same taxpayer for purposes of carrying out the intent of the statute, *e.g.*, nonrecognition treatment for minority shareholders who retain their stock interest in target and the requirement that new target must report as income on its return any additional recapture income arising from an adjustment of the deemed sale price to old target due to an event or events occurring after old target files its final return. See H. Rep. No. 97-760 (Conf. Rep.), 97th Cong., 2d Sess. 537 [1982-2 C.B. 600, 632]. The treatment of old target and new target as the same taxpayer is appropriate in view of the legislative history.

Postponement of due date

The temporary regulations extend the time for taking certain actions under section 338. Thus, in temporary regulations §§1.338-1T, 1.338-2T, 1.338-4T, 1.338-5T, and 1.338(h)(10)-1T, all references to "March 15, 1986" with respect to the time for making elections or taking certain other actions under section 338 will be changed to "July 15, 1986." However, references to "March 15, 1986" will not be amended where the applicability of certain rules depends on whether the acquisition date occurs after March 15, 1986.

REGULATORY FLEXIBILITY ACT; EXECUTIVE ORDER 12291; AND PAPERWORK REDUCTION ACT OF 1980

A general notice of proposed rulemaking is not required by 5 U.S.C. 553 for temporary regulations. Accordingly, these temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required. The collection of information contained in the regulations refer to requirements that have been submitted to the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1980, and have been approved by OMB (Control Number 1545-070).

DRAFTING INFORMATION

The principal author of these temporary regulations is Thomas J. Kane of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 1 is amended as follows:

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * * Sections 1.338-1T, 1.338-2T, 1.338-4T, 1.338-5T, and 1.338(h)(10)-1T also issued under 26 U.S.C. 338.

Par. 2. Section 1.338-1T is amended as follows:

1. Paragraph (c) is amended by—

a. Removing from the first sentence the word "March" and by adding in its place the word "July".

b. Adding a new sentence at the end of paragraph (c) to read as set forth below.

2. Paragraph (e) is amended by:

a. Removing, from each place it appears in paragraph (e)(1)(ii)(A) and (B), the word "March" and by adding in its place the word "July".

b. Removing, from paragraph (e)(2)(ii)(A), the word "March" and by adding in its place the word "July".

3. Paragraph (f)(7)(ii) is amended by removing the word "March" and by adding in its place the word "July".

4. Paragraph (h) is amended by:

a. Removing, from each place it appears in paragraph (h)(1) and (2), the word "March" and by adding in its place the word "July".

b. Removing, from each place it appears in *Example (1)* of paragraph (h)(4), the word "March" and by adding in its place the word "July".

c. Removing, from the third sentence of paragraph (h)(4) *Example (2)*, the word "March" and by adding in its place the word "July".

5. Subparagraphs (2) and (4) of paragraph (j) are amended by removing, from each place it appears, the word "March" and by adding in its place the word "July".

6. Paragraph (k) is amended by—

a. Adding a new sentence at the end of paragraph (k)(1) to read as set forth below.

b. Removing from each place it appears in subdivisions (iv) and (v) of paragraph (k)(7) the word "March" and by adding in its place the word "July".

7. Adding at the end thereof new paragraph (m) to read as set forth below.

§1.338-1T Elections under section 338(g) of the Internal Revenue Code of 1954 (temporary).

* * * * *

(c) *Time and manner of making election.* * * * For special rules applicable to certain statements of section 338 election filed on or after December 9, 1985, and on or before July 15, 1986, see paragraph (m) of this section.

* * * * *

(k) *Special rules for foreign corporations or DISCs*—(1) *Election by certain foreign purchasing corporations.* * * * However, the items required under paragraph (m) of this section to be filed by such a foreign purchasing corporation with the District Director shall be filed with the District Director of the Foreign Operations District (Attention: Chief of Examination), 1325 K Street, N.W., Washington, D.C. 20225.

* * * * *

(m) *Statements of section 338 election filed on or after December 9, 1985, and on or before July 15, 1986*—(1) *General rule.* A statement of section 338 election filed on or after December 9, 1986, and on or before July 15, 1986, is not effective unless—

(i) It meets the applicable requirements prescribed in paragraph (m)(2) of this section when it is filed,

(ii) It is perfected by refiling in accordance with paragraph (m)(4)(ii) of this section, or

(iii) The District Director or his delegate waives, under paragraph (m)(13) of this section, the applicable requirements contained in paragraph (m)(2) of this section.

(2) *Applicable requirements.* The requirements of this subparagraph (2) are that—

(i) The statement of section 338 election meets the filing, documentation, and Form 872 requirements of paragraph (m)(4), (5), and (6) of this section for each relevant taxable year (within the meaning of paragraph (m)(3) of this section) for which the statute of limitations on making an assessment is considered under paragraph (m)(10) of this section to expire after August 15, 1986, and on or before November 15, 1986,

(ii) The statement of section 338 election meets the filing, documentation, and closing agreement requirements of paragraph (m)(4), (5), and (7) of this section for each relevant taxable year (within the meaning of paragraph (m)(3) of this section) for which the statute of limitations on making assessment is considered under paragraph (m)(10) of this section to expire on or before August 15, 1986, and

(iii) The statement of section 338 election meets the filing and closing agreement requirements of paragraph (m)(4) and (7)(v) of this section if a deemed sale return is required to be filed and the acquisition date occurred on or before November 15, 1983.

(3) *Relevant taxable year*. For purposes of this paragraph (m), a taxable year is relevant if it is one for which a Federal income tax return was filed prior to filing the statement of section 338 election, but only if it is also—

(i) A taxable year of target (or an affected target) which includes its acquisition date, or

(ii) Any subsequent taxable year of target (or an affected target) or an affected taxable year of an affected corporation (within the meaning of paragraph (m)(12) of this section).

(4) *Filing procedures*—(i) *In general*. The statement of section 338 election and any documents, Forms 872, and closing agreements to which paragraph (m)(2) of this section applies shall all be filed in one envelope with the District Director (Attention: Chief of Examination) for the internal revenue district where original target had its principal place of business or where its principal office or agency was located on the acquisition date.

(ii) *Perfection rule*. A statement of section 338 election filed on or after December 9, 1985, and on or before July 15, 1986, that does not comply with the applicable procedures prescribed in paragraph (m)(2) of this section is perfected by refiling in accordance with those procedures the statement of election on or before July 15, 1986, along with a copy of the previously filed statement of election.

(5) *Documents required under paragraph (m)(2) of this section*. The documents required by this subparagraph (5) for each relevant taxable year are—

(i) A photocopy of the face page of the income tax return (and of any amended return or returns) filed for the taxable year, and

(ii) A photocopy of any extension, consent, or other document previously entered into or filed which extended the statute of limitations on assessment for the year.

(6) *Contents of Form 872*—(i) *In general*. For purposes of paragraph (m)(2)(i) of this section, for each relevant taxable year a Form 872 must be properly completed and executed in duplicate on behalf of each target or any affected corporation and must agree to extend until May 15, 1987, the period for making an assessment with respect to any tax due as a result of the deemed sale under section 338(a)(1) by the target. A photocopy of Form 872 (including one on white paper) may be used instead of a copy supplied by the Internal Revenue Service.

(ii) *Restrictive language*—(A) *General language*. The following restrictive language shall be inserted as numbered paragraph (4) on the face page of any Form 872 to which this subparagraph (6) applies: "THIS CONSENT AND AGREEMENT IS LIMITED TO ANY FEDERAL TAX DUE FROM TAXPAYER (INCLUDING ACCRUED INTEREST THEREON) AS A RESULT OF THE DEEMED SALE OF ASSETS UNDER SECTION 338(A)(1) OF THE INTERNAL REVENUE CODE BY TAXPAYER" [if taxpayer is not the target, substitute name of target instead of last word].

(B) *Year which includes the acquisition date*. If the relevant taxable year of target includes the acquisition date, the Form 872 for that relevant taxable year shall contain the following language inserted as numbered paragraph (5): "THIS CONSENT AND AGREEMENT COVERS THE ENTIRE PERIOD ENDING ON THE DATE SET FORTH IN PARAGRAPH (1) OF THIS AGREEMENT, AS WELL AS ALL SHORT PERIODS WHICH RESULT AS A CONSEQUENCE OF THE SECTION 338 ELECTION AND WHICH END WITH OR WITHIN THAT ENTIRE PERIOD".

(7) *Closing agreements*—(i) *In general*. For purposes of paragraph (m)(2)(ii) and (iii) of this section, a separate closing agreement under section 7121 shall be submitted on Form 906 and must be properly completed and executed on behalf of each target or any affected corporation. For guidelines on preparation of closing agreements, see Rev. Proc. 68-16, 1968-1 C.B. 770. A photocopy of Form 906 (including one on white paper) may be used instead of a copy supplied by the Internal Revenue Service. In addition, a separate closing agreement under the provisions of paragraph (m)(2)(ii) of this section must be executed in triplicate for each relevant taxable year and contain the applicable language prescribed in paragraph (m)(7)(ii), (iii), and (iv) of this section. For special rules for applying the provisions of paragraph (m)(2)(iii) of this section with respect to a deemed sale return or a combined deemed sale return, see paragraph (m)(7)(v) of this section.

(ii) *Waiver of statute of limitations*—(A) *In general*. Each closing agreement required by paragraph (m)(2)(ii) of this section must contain an express waiver of the statute of limitations on assessment (under section 6501(a)) and credit (under section 6402(a)) with respect to any Federal tax (including accrued interest thereon) required to be reported on any return or claim for refund for the relevant taxable year of the taxpayer, using the following language: "TAXPAYER AND COMMISSIONER AGREE TO WAIVE THE STATUTE OF LIMITATIONS FOR ASSESSMENT AND CREDIT WHICH (HAS EXPIRED or WILL EXPIRE) ON [insert expiration date] FOR ANY FEDERAL TAX DUE OR REFUNDABLE (INCLUDING ACCRUED INTEREST THEREON) AS A RESULT OF THE DEEMED SALE OF ASSETS UNDER SECTION 338(a)(1) OF THE INTERNAL REVENUE CODE BY TAXPAYER" [if taxpayer is not the target, substitute name of target instead of last word].

(B) *Year which includes the acquisition date*. If the relevant taxable year is a taxable year of target which includes the acquisition date, the closing agreement for that relevant taxable year shall contain the following language in addition to the language contained in subdivision (m)(7)(ii)(A) of this section: "TAXPAYER ACKNOWLEDGES THAT THIS CLOSING AGREEMENT COVERS THE ENTIRE PERIOD DESCRIBED IN THE PRECEDING SENTENCE, AS WELL AS ALL SHORT PERIODS WHICH RESULT AS A CONSEQUENCE OF THE SECTION 338 ELECTION AND WHICH END WITH OR WITHIN THAT ENTIRE PERIOD".

(iii) *Amended returns*—(A) *In general*. Each closing agreement must contain an express agreement on behalf of the taxpayer to file an amended Federal income tax return or returns on or before November 3, 1986, for each relevant taxable year, and an acknowledgement that the statement of section 338 election will not be effective in the event of a failure to timely file any such amended return, unless the requirement of filing an amended return is waived by the District Director or his delegate.

(B) *Relevant taxable year which includes acquisition date*. For the relevant taxable year which includes the acquisition date, the following language shall be inserted in the closing agreement: "FOR THE RELEVANT TAXABLE YEAR COVERED BY THIS CLOSING AGREEMENT, TAXPAYER AGREES TO FILE ON OR BEFORE NOVEMBER 3, 1986 (IF NOT ALREADY FILED), THE FOLLOWING FEDERAL INCOME TAX RETURN[S]: (*1*) AN AMENDED RETURN AS OLD TARGET'S FINAL RETURN, AND (*2*) AN AMENDED RETURN FOR NEW TARGET'S FIRST TAXABLE YEAR ENDING ON [insert date]. TAXPAYER ACKNOWLEDGES THAT A STATEMENT OF ELECTION UNDER SECTION 338 WILL NOT BE EFFECTIVE IF THE FEDERAL INCOME TAX RETURN(S) COVERED BY THIS CLOSING AGREEMENT (IS) (ARE) NOT FILED ON A TIMELY BASIS, UNLESS SUCH REQUIREMENT IS WAIVED IN WRITING BY THE DISTRICT DIRECTOR OR HIS DELEGATE." If the acquisition date occurs on the last day of target's relevant taxable year or if new target does not have a taxable year that terminates within the relevant taxable year, then the language in *(2)* of this subdivision (B) shall be omitted. If new target has more than one taxable year ending within the relevant taxable year covered by a closing agreement governed by this subdivision (B), then appropriate language referring to the amended returns for those years shall be added to the closing agreement, using the format set forth in this subdivision (B).

(C) *Other relevant taxable years*. For a relevant taxable year which does not include the acquisition date, the following language shall be inserted in the closing agreement. "TAXPAYER AGREES TO FILE AN AMENDED FEDERAL INCOME TAX RETURN ON OR BEFORE NOVEMBER 3, 1986, FOR THE RELEVANT TAXABLE YEAR COVERED BY THIS CLOSING AGREEMENT. TAXPAYER ACKNOWLEDGES THAT A STATEMENT OF ELECTION UNDER SECTION 338 WILL NOT BE EFFECTIVE IF ANY FEDERAL INCOME TAX RETURN COVERED BY THIS CLOSING AGREEMENT IS NOT FILED ON OR BEFORE NOVEMBER 3, 1986, UNLESS SUCH REQUIREMENT IS WAIVED IN WRITING BY THE DISTRICT DIRECTOR OR HIS DELEGATE."

(D) *Section 338(h)(10) election*. The second quoted sentence in subdivision (iii)(B) and (C) of this paragraph (m)(7) shall be omitted from any closing agreement for a relevant taxable year of a selling group referred to in paragraph (m)(11)(ii)(A) of this section (relating to section 338(h)(10) election).

(E) *Waiver of certain additions to tax and time to act*. See §1.338-1T(h) for rules applicable to the waiver of certain additions to tax and time to act.

(iv) *Consent to extend expiration date*. Each closing agreement must contain an express consent to extend until June 15, 1988, the period for further assessment (under section 6501(a)) or credit (under section 6402(a)) of any tax due or refundable (including accrued interest thereon) for any relevant taxable year resulting from the deemed sale under section 338(a)(1), using the following language: "TAXPAYER AND COMMISSIONER AGREE TO EXTEND UNTIL JUNE 15, 1988, THE PERIOD FOR MAKING ANY FURTHER ASSESSMENT OR CLAIMING ANY CREDIT OF ANY FEDERAL TAX DUE OR REFUNDABLE (INCLUDING ACCRUED INTEREST THEREON) AS A RESULT OF THE DEEMED SALE OF ASSETS UNDER SECTION 338(a)(1) BY TAXPAYER" [if taxpayer is not the target, substitute name of target instead of last word].

(v) *Special rule for deemed sale return or combined deemed sale return*—(A) *In general*. For purposes of paragraph (m)(2)(iii) of this section, if a target is required to file a deemed sale return (as defined in paragraph (f)(3)(i) of this section), then a separate closing agreement with respect to that deemed sale return must be filed in triplicate in order to make an effective election under section 338. The closing agreement shall contain the following language: "TAXPAYER AGREES TO FILE ON OR BEFORE NOVEMBER 3, 1986 (IF NOT ALREADY FILED), A DEEMED SALE RETURN REFLECTING THE CONSEQUENCES OF THE DEEMED SALE OF ASSETS BY TAXPAYER [if taxpayer is not the target, substitute the name of target instead of last word] UNDER SECTION 338. TAXPAYER ACKNOWLEDGES THAT A STATEMENT OF ELECTION UNDER SECTION 338 WILL NOT BE EFFECTIVE IF THE DEEMED SALE RETURN IS NOT FILED ON A TIMELY BASIS, UNLESS SUCH REQUIREMENT IS WAIVED IN WRITING BY THE DISTRICT DIRECTOR OR HIS DELEGATE. TAXPAYER FURTHER AGREES THAT THE STATUTE OF LIMITATIONS ON ASSESSMENT FOR ANY FEDERAL TAX DUE AS A RESULT OF THE DEEMED SALE OF ASSETS BY TAXPAYER [if taxpayer is not the target, substitute the name of target instead of last word] UNDER SECTION 338 WILL NOT TERMINATE PRIOR TO THE EXPIRATION OF THREE YEARS FROM THE DATE THE DEEMED SALE RETURN IS ACTUALLY FILED."

(B) *Combined deemed sale return*. All targets which are eligible to file a combined deemed sale return (as defined in section 338(h)(15) and §1.338-4T(k)(6)) may join together in a combined deemed sale closing agreement, instead of filing a separate closing agreement for each target under paragraph (m)(7)(v)(A) of this section. If a combined deemed sale closing agreement is filed, then a combined deemed sale return must be filed. The combined deemed sale closing agreement shall contain the language prescribed in paragraph (m)(7)(v)(A) of this section, except that the words "COMBINED DEEMED SALE RETURN" shall be substituted for "DEEMED SALE RETURN," the word "TAXPAYER" shall be expressed in the singular or plural (as the case may be), and each target's name shall be inserted in place of "TAXPAYER", if appropriate. A list containing the name address, and employer identification number of each target which is joining in the combined deemed sale closing agreement shall be included in the text of the combined deemed sale closing agreement. If the targets included in the combined deemed sale closing agreement constitute a single affiliated group within the meaning of section 1504(a), the combined deemed sale closing agreement shall be signed by an officer of the common parent of that group. Otherwise, the combined deemed sale closing agreement must be signed by an officer of each target included in the combined deemed sale closing agreement.

(8) *Execution of Form 872 or Form 906*—(i) *On behalf of Commissioner*. Any Form 872 or Form 906 properly submitted pursuant to the requirements in this paragraph (m) will be executed on behalf of the Commissioner of Internal Revenue and an executed copy of each Form 872 and each Form 906 will be returned to the originating party.

(ii) *On behalf of target*. If target was included on a consolidated return filed by the purchasing group for a relevant taxable year, the common parent of the purchasing group shall be the proper party to execute any Form 872 or Form 906 required by this paragraph (m) for that year. See §1.1502-77(a).

(9) *Exceptions*. This paragraph (m) shall not apply—

(i) If the statement of section 338 election has been filed before December 9, 1985, or after July 15, 1986,

(ii) If there is no relevant taxable year of a target, affected target, or affected corporation for which the statute of limitations expires on or before November 15, 1986,

(iii) With respect to the taxable year of a selling group that files a consolidated return for the period that includes the acquisition date, if the binding contract rule in paragraph (l) of this section applies, or

(iv) With respect to the taxable year of a person that includes the acquisition date of a target, if (A) the target is a DISC, a controlled foreign corporation, or a domestic corporation described in section 1248(e) and (B) the person actually transfers the target stock (as distinguished from being treated under section 338(a)(1) as having sold it).

(10) *Statute of limitations on assessment*—(i) *General rule*. For purposes of applying this paragraph (m), the statute of limitations on assessment is considered to begin to run for a relevant taxable year, and any short period of target which may result as a consequence of a section 338 election that ends with or within that relevant taxable year, on the date target is considered under section 6501(b) to have filed its return for that relevant taxable year.

(ii) *Deemed sale return*. If old target's final return is a deemed sale return (within the meaning of paragraph (f)(3)(i) of this section) or a combined deemed sale return (within the meaning of section 338(h)(15)), then the period for assessment under section 6501 does not begin to run until such deemed sale return or combined deemed sale return is filed.

(11) *Section 338(h)(10)*—(i) *Scope*. This subparagraph (11) provides rules for applying this paragraph (m) as a condition for electing to report the consequences of old target's deemed sale of its assets under section 338(a)(1) on the selling group's consolidated return under section 338(h)(10).

(ii) *Application*. If this subparagraph (11) applies, then—

(A) A relevant taxable year under paragraph (m)(3) of this section is considered to include the period for which a consolidated return of the selling group is filed that includes the acquisition date.

(B) Any document executed or item submitted by the common parent of the selling group on behalf of that entire group with respect to that relevant taxable year is considered to be on behalf of old target (see §1.1502-77(a)).

(12) *Affected taxable years of affected corporations*. For purposes of this paragraph (m)—

(i) *Affected taxable year*. A taxable year is affected by the section 338 election if Federal tax for that year is increased or decreased as a result of the section 338 election. For example, an affected taxable year may arise if target originally filed a return for a period which ended on or after the acquisition date and the deemed sale of assets results in additional Federal tax due from target for that period, or if consideration for stock included in a qualified stock purchase is contingent and receipt of that consideration subsequent to the acquisition date is reported on new target's return under §1.338(b)-3T(h).

(ii) *Affected corporation*. An affected corporation is a corporation that has a basis in an asset transferred to it by a new target or another affected corporation that is determined in whole or in part by reference to the asset's basis in the hands of the transferor.

(13) *Discretion of the District Director*—(i) *General standard*. In exercising discretion to waive any of the requirements prescribed under this paragraph (m) for any statement of section 338 election or amended returns, the District Director or his delegate shall consider all of the relevant facts and circumstances.

(ii) *Time when discretion is exercised*. The discretion of the District Director or his delegate under this paragraph (m) can be exercised at any time in connection with the examination of any Federal income tax return which would be affected by a section 338 election.

(14) *Applicability of the mitigation provisions*. For application of the mitigation provisions contained in sections 1311-1314, see §1.338-4T(l)(5).

(15) *Examples*. The provisions of this paragraph (m) may be illustrated by the following examples.

Example (1). (i) T is an unaffiliated corporation filing income tax returns on the basis of a fiscal year ending February 28. At the close of January 20, 1983, P acquires all of T's stock in a qualified stock purchase. P does not file consolidated returns. On May 15, 1983, T timely files an income tax return (without extensions) for its taxable year beginning on March 1, 1982, and ending February 28, 1983. On May 14, 1986, P files a statement of election under section 338 which (if effective) would cause T's taxable year ending on February 28, 1983, to be divided into two periods. The first period for "old T" ends on the close of the acquisition date (January 20, 1983), and the second period for "new T" begins the next day. For T's taxable year ending February 28, 1983, the statute of limitations expires on May 15, 1986. In order for the section 338 election to be effective, the statement of election must be filed in accordance with the requirements of paragraph (m)(2)(ii) of this section. Thus, for example, there must be filed with the election, in the form prescribed in paragraph (m)(7) of this section, a closing agreement for T's taxable year ending on February 28, 1983, for which T's return was filed on May 15, 1983, extending the time within which assessments can be made until June 15, 1988. This closing agreement will cover the two periods into which that taxable year has now been divided. Additionally, the closing agreement must provide that on or before November 3, 1986, T must file old target's final return for the taxable year ending on January 20, 1983, and an amended return for the taxable year ending on February 28, 1983. The section 338 election will be ineffective unless the closing agreement procedures are followed and T files on or before November 3, 1986, the required returns, unless the District Director, in his discretion, waives any failure by P or T to comply with these requirements. However, in order for the waiver provisions contained in paragraph (h) of this section to apply, the amended returns must be filed on or before the last day for making an election under section 338, *i.e.*, July 15, 1986.

(ii) T also timely filed an income tax return (without extensions) on May 15, 1984, for its taxable year beginning on March 1, 1983, and ending on February 29, 1984. Since the statute of limitations on assessment for the income tax return filed on May 15, 1984, expires on May 15, 1987, which is after November 15, 1986, the provisions contained in paragraph (m) of this section are not applicable with respect to that taxable year.

Example (2). Assume the same facts as in *Example (1)* except that P files the statement of election on April 1, 1986, and that filing does not comply with the requirements of paragraph (m)(2)(ii) of this section. On July 6, 1986, under paragraph (m)(1)(ii) of this section, P perfects the election by refiling the election in accordance with the requirements of paragraph (m)(2)(ii) and (4)(ii) of this section. As long as T timely files on or before November 3, 1986, the returns which relate to the periods covered by the closing agreement (*i.e.*, T's taxable years ending on January 20, 1983, and February 28, 1983), the section 338 election will be valid.

Example (3). Assume the same facts as in *Example (2)* except that P does not perfect the election. Under paragraph (m)(1)(iii) and (13) of this section, the election is ineffective unless the District Director waives the requirements of paragraph (m)(2) of this section.

Example (4). Assume the same facts as in *Example (2)* except that T does not timely file the returns covered by the closing agreement. The section 338 election is ineffective under paragraph (m)(13) of this section unless the District Director waives the timely filing requirement for the amended returns.

Example (5). Assume the same facts as in *Example (1)*. Assume further that T owns all the stock of T1 and that T11 uses the same taxable year as T. For the election to be effective, P must also file a closing agreement for T1 and T1 must file on or before November 3, 1986, the returns for the periods covered by T1's closing agreement unless those requirements are waived by District Director.

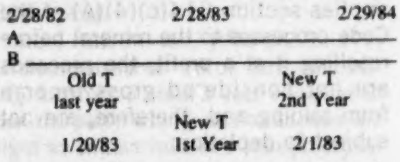
Example (6). Assume the same facts as in *Example (2)* except that T reports its income on the basis of a taxable year ending June 30. Assume further that on September 15, 1983, T timely filed an income tax return (without extensions) for its taxable year ending June 30, 1983, and that the statute of limitations for that year expires on September 15, 1986. In order for the section 338 election to be effective, the statement of election must be filed in accordance with the requirements of paragraph (m)(2)(i) of this section. Thus, for example, there must be filed with the election, in the form prescribed in paragraph (m)(6) of this section, a Form 872 for T's taxable year ending June 30, 1983, for which T's return was filed on September 15, 1983, extending the time within which assessments can be made until May 15, 1987. This Form 872 will cover both periods into which the taxable year has been divided. However, in order for the waiver provisions contained in §1.338-1T(h) to apply, T must file the amended returns on or before the last day for making an election under section 338, *i.e.*, July 15, 1986. In any event, old target's final return and an amended return for the taxable year ending June 30, 1983, should be filed on or before May 15, 1987.

Example (7). Assume the same facts as in *Example (1)* except that T files its income tax returns on the basis of the calendar year and actually filed its returns for calendar year 1983 on March 3, 1984. No Form 872 or closing agreement is required for T's 1983 calendar year if the statute of limitations for that year expires after November 15, 1986. See paragraph (m)(1) and (9)(ii) of this section. The statute of limitations for new T's first taxable year and old T's period ending on the close of the acquisition date (January 20, 1983) did not start to run until the due date for T's 1983 return (March 15, 1984), and therefore cannot expire prior to March 15, 1987. See section 6501(b)(1) and paragraph (m)(10) of this section.

Example (8). (i) Assume the same facts as in *Example (1)*, except that T, on its first tax return as new T filed on or before July 15, 1986, adopts a taxable year ending on January 31. The closing agreement referred to in *Example (1)* for the taxable year ending on February 28, 1983, will also operate to waive and extend the statute of limitations on assessment for new T's first taxable year which begins January 21, 1983, and ends on January 31, 1983. If T filed its first tax return as new T after July 15, 1986, it would not be permitted to adopt a taxable year different from the year T used before making the section 338 election. See paragraph (f)(7)(ii) of this section.

(ii) The tax consequences of new T's operations for the period that begins on February 1, 1983, and ends on February 28, 1983, will now have to be reported on an amended return which should be filed by new T for its second taxable year which begins on February 1, 1983, and ends on January 31, 1984. The statute of limitations on assessment for new T's second taxable year is controlled by the due date of the return T originally filed (without regard to the section 338 election) on May 15, 1984, for its taxable year ending February 29, 1984, which includes the last day of new T's second taxable year (*i.e.*, January 31, 1984). Because the statute of limitations on assessment for the taxable year ending on February 29, 1984 does not expire until may 15, 1987, the provisions of paragraph (m) does not apply to new T's second taxable year.

(iii) The results of this example may be summarized with time lines. Line A represents taxable years of T for which returns were filed prior to the time that a section 338 statement of election was filed. Line B represents taxable years of old T and new T reflecting such election. Arrows show dates on Line A when T's tax returns were filed, which started the statute of limitations running for the taxable periods shown on Line B.



Example (9). Assume the same facts as in *Example (1)*, except that T, on its first tax return as new T filed on or before July 15, 1986, adopts a taxable year ending on April 30. The closing agreement referred to in *Example (1)* for the taxable year ending on February 28, 1983, will waive and extend the statute of limitations on assessment only for old T's taxable year ending on January 20, 1983. The tax consequences of new T's operations for new T's taxable year which begins on January 20, 1983, and ends on April 30, 1983, will have to be reported on an amended return filed for that period. The statute of limitations on assessment for new T's first taxable year is controlled by the due date of the return T originally filed (without regard to the section 338 election) on May 15, 1984, for its taxable year ending February 29, 1984, which includes the last day of new T's first taxable year, (*i.e.*, April 30, 1983). Because the statute of limitations on assessment for the taxable year ending on February 29, 1984, does not expire until May 15, 1987, the provisions of paragraph (m) do not apply to new T's first taxable year.

Example (10). All of T's stock is owned by S, which is included in a consolidated return that is filed for the S group on the basis of a fiscal year ending January 31. At the close November 15, 1982, P acquired all of T's stock in a qualified stock purchase. P is the common parent of an affiliated group that files consolidated returns on the basis of a calendar year. On July 1, 1986, P files a statement of election under section 338 for T. As a result of the acquisition, the results of T's operations through the close of business on November 15, 1982, was originally reported on the consolidated return for the S group which was timely filed on April 15, 1983. The results of T's operations from November 16, 1982, through December 31, 1982, were originally reported on the consolidated return for the P group, which was timely filed on March 15, 1983. Because T must file a deemed sale return (within the meaning of paragraph (f)(3)(i) of this section) and the acquisition date occurred on or before November 15, 1983, in order for the section 338 election to be effective, the closing agreement and other procedures required by paragraph (m)(2)(iii) and (7)(v) of this section must be followed and the deemed sale return must be filed on or before November 3, 1983 unless those requirements are waived by the District Director.

Par. 3. Section 1.338-2T is amended by removing, from each place they appear in *Example (1)* and *Example (2)* of paragraph (j), the words "August 23, 1985" and by adding in their place the words "July 15, 1986".

Par. 4. Section 1.338-4T is amended as follows:

1. Paragraph (a)(3) is amended by adding immediately after item (l)(4) a new item (l)(5) to read as follows: "(5) Application of mitigation provisions."

2. Paragraph (a)(4) is amended by adding in the second table immediately after the line "1248(e) . . . (b)(6) the following new line: "1311 . . . (l)(5)".

3. Paragraph (l) is amended by adding at the end thereof new subparagraph (5) to read as set forth below.

4. Paragraph (f)(6)(iv) Answer 1 (i)(C)*(1)* is amended by removing the word "March" and by adding in its place the word "July".

5. Paragraph (j)(2) Answer 5(i) is amended by removing from the third sentence the word "March" and by adding in its place the word "July".

§1.338-4T Questions and answers relating to miscellaneous issues under section 338 (temporary).

* * * * *

(l) *Miscellaneous matters affecting new T.* * * *

* * * * *

(5) *Application of mitigation provisions.*

Question: For purposes of applying sections 1311-1314 (relating to the mitigation of the effect of limitations), in the absence of a section 338(h)(10) election, are old T and new T to be treated as being the same taxpayer?

Answer: Yes.

Par. 5. Section 1.338-5T is amended as follows:

1. Paragraph (a)(2) is amended by removing from the outline of topics at both (j)(8)(ii) and (iii) the word "March" and by adding in both places the word "July".

2. Paragraph (c)(2)(v)(C) is amended by removing, from each place it appears, the word "March" and by adding in its place the word "July".

3. Subdivisions (ii) and (iii) of paragraph (j)(8) are each amended by removing from the heading and from the text the word "March" and by adding in both places in each such subdivision the word "July".

Par. 6. Section 1.338(h)(10)-1T (d) is amended by—

1. Removing, from each place it appears in subparagraph (7)(i) and (ii), the word "March" and by adding in its place the word "July".

2. Adding at the end thereof new subparagraph (9) to read as follows:

§1.338(h)(10)-1T Elective recognition by selling consolidated group of deemed sale gain or loss on target's assets (temporary).

* * * * *

(d) *Time and manner of making section 338(h)(10) election.* * * *

(9) *Special rules.* See §1.338-1T(m)(11) for special rules applicable to certain statements of section 338 election filed on or after December 9, 1985, and on or before July 15, 1986.

* * * * *

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved May 5, 1986.

J. Roger Mentz,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on May 15, 1986, 8:45 a.m., and published in the issue of the Federal Register for May 16, 1986, 51 F.R. 17929)

Section 611.—Allowance of Depletion for Depletion

Whether a lessee receives an economic interest upon entering into a lease under which the lessee must follow the lessors engineering plans and must sell ore extracted under the lease to the lessor at a fair market price? See Rev. Rul. 86-81, below.

Section 613.—Percentage Depletion

26 CFR 1.613-1: Percentage depletion; general rule.

Whether under section 613 of the Code a lessor of coal properties is entitled to percentage depletion on royalty proceeds received from the lessee? See Rev. Rul. 86-81, below.

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26 CFR 1.613-4: Gross income from the property in the case of minerals other than oil and gas. (Also Sections 611, 631; 1.613-1, 1.631-3).

Percentage depletion; gross income from mining. If a lessor purchases extracted mineral from a lessee and applies section 614(c)(4)(A) of the Code processes to the mineral before reselling it at a profit, the proceeds are not considered gross income from mining and, therefore, are not subject to depletion.

Rev. Rul. 86-81

ISSUE

If (1) the owner of coal properties purports to lease those properties to an operator-lessee in exchange for royalties equal to a reasonable percentage of sales proceeds of the coal mined, (2) the operator-lessee agrees to follow the owner-lessor's engineering plans for the mining operation, and (3) the owner-lessor retains an option to purchase, at the then-prevailing fair market price, the unprocessed coal so mined, then what is the proper tax treatment of the owner lessor's income from that transaction when the owner-lessor applies section 613(c)(4)(A) processes to that coal prior to its resale at a profit?

FACTS

W, a lessor of coal properties located in the United States, leased a part of those coal properties to *Z*, a coal operator. *Z*, as lessee, has the exclusive right to mine coal for a specified period of years or until the designated coal reserves are exhausted. Under the terms of the lease, *Z* is required to follow plans, maps, and projections for the mining and operation of the coal properties as provided by *W*'s engineer. *Z*'s obligation to follow the plans, maps, and projections assures *W* that extraction will not be done in a manner that renders unextractable an unnecessarily large portion of the mineral in place. At the option of *W*, failure by *Z* to follow these plans, maps, and projections will result in either: (1) payment of the "royalty" on any coal that was not mined because of this failure and that is deemed "lost" by *W*, or (2) cancellation of the lease.

W will receive two "royalty" payments that are dependent upon the extraction of the coal. These royalty payments are described as a production royalty of 10*x* percent of the amount *Z* receives for the coal, and an engineering royalty of *x* percent of the amount *Z* receives for the coal, which is to compensate *W* for the plans, maps, and projections provided by its engineer. Both royalties are reasonable in amount.

Z agrees to sell all coal mined to *W* and will deliver the coal to *W*'s tipple as directed by *W*. *Z* may sell coal to others on such days that *W* cannot accept coal mined. *W* purchases the coal from *Z* at prevailing "market ramp prices," a fair market price for coal extracted as it comes from the mine. *W* will further process the coal by applying only the processes named in section 613(c)(4)(A) of the Internal Revenue Code. After application of these processes, *W* is able to sell the cleaned coal at a price greater than the "market ramp price" received by *Z*.

LAW AND ANALYSIS

Section 611(a) of the Code allows a reasonable deduction for depletion in computing taxable income. Section 611(b)(1) provides that in the case of a lease, the deduction must be equitably apportioned between the lessor and lessee.

Section 1.611-1(b)(1) of the Income Tax Regulations provides that the depletion deduction shall be allowed only to the owner of an economic interest in mineral deposits.

Section 613(b) of the Code provides a depletion allowance for coal mines of 10 percent of the gross income from the property, excluding from the gross income an amount equal to any returns or royalties paid or incurred by the taxpayer in respect of the property. With respect to coal, section 613(c)(1) defines gross income from the property as the gross income from mining. In the case of coal, section 613(c)(4) provides that cleaning, breaking, sizing, dust allaying, treatment to prevent freezing, and loading for shipment shall be considered as mining where applied by the mine owner or operator to the ore or mineral in respect of which he is entitled to a deduction for depletion under section 611.

Section 631(c) of the Code provides that in the case of the disposal of coal mined in the United States, held for more than 6 months before disposal, by the owner under any form of contract by which the owner retains an economic interest in the coal, the difference between the amount realized from the disposal of the coal and the adjusted depletion basis plus the deductions disallowed for the tax year under section 272 shall be considered as though it were a gain or loss, as the case may be, on the sale of the coal. The owner is not entitled to the allowance for percentage depletion provided in section 613 with respect to the coal. The term "owner" means any person who owns an economic interest in coal in place, including a sublessor. However, this subsection specifies that it shall not apply to income realized by an owner as a co-adventurer, partner, or principal in the mining of the coal.

Before the lease, *W* as owner of the coal had the right to all income from the extraction and sale of the coal and therefore had an economic interest. Through the lease, *W* granted to *Z* the right to mine all the coal for a specified term or to exhaustion. *Z* is to dispose of the extracted but unprocessed coal by transferring it to *W* at a fair market price. Therefore, *Z* shares in income from the extraction of the coal and has acquired an economic interest in the coal in place. *W* has retained as its economic interest the right to receive royalties based upon production because the production royalty for the coal and the engineering royalty for the engineering services are payable only if coal is produced and the amount of such royalties is related to the value of the coal produced.

Although the agreement provides that *W* is to receive from *Z* all the extracted coal and is to subject such coal to processes named in section 613(c)(4)(A) of the Code, these processes should not be treated as mining processes because *W* is not the "mine owner or operator" when it processes the coal. The substance of the agreement must prevail over its form. *See* Rev. Rul. 74-568, 1974-2 C.B. 183. Here, in substance, *W* had not retained an interest in the coal other than *W*'s royalty interests; rather, *W* through the lease has disposed of its entire interest in the coal in return for retained royalty interests, and has also agreed to purchase from *Z* the coal extracted under the lease.

Helvering v. Bankline Oil Co., 303 U.S. 362 (1938), 1938-1 C.B. 306, established that a taxpayer who merely has the benefit of purchasing or processing minerals does not have an economic interest in the minerals. Since *W* acquires no economic interest in the coal it purchases from *Z*, *W* is entitled to no depletion deduction with respect to income derived from its processing of the coal.

Rev. Rul. 74-469, 1974-2 C.B. 177, is distinguishable. To be sure, that ruling involves a similar fact situation in that the party who grants to another the right to extract minerals also processes the extracted minerals. In that ruling, however, the taxpayer-grantor did not retain a royalty interest to compensate it for granting the right to extract the minerals. Rather, both the taxpayer that granted the right to extract minerals and the taxpayer who received such right directly shared in the ultimate sales price of the processed mineral. In contrast, here *W* and and *Z* do not share in the sales price of the coal because *Z* sells the extracted coal to *W* for its fair market value. Except for *W*'s royalty interests, only *Z* shares in the risks of fluctuations in the value of coal in place. In purchasing the extracted but unprocessed coal from *Z*, *W* is no different than any other purchaser of extracted coal.

The next question is whether income received by *W* is subject to treatment under section 631(c) of the Code as capital gain or loss. Clearly, *W* was the owner of the coal before entering into the agreement with *Z*, and it retained as its economic interest the right to production and engineering royalties. Accordingly, *W* should receive section 631(c) treatment unless it is deemed to be a co-adventurer, partner, or principal in the mining of the coal.

The purpose of denying section 631(c) treatment to a co-adventurer, partner, or principal in the mining of coal is to distinguish between the passive interest of a lessor who retains an economic interest and the direct interest of a participant in the operation of a mine who shares in the risk and control of the venture. *See* Rev. Rul. 73-33, 1973-1 C.B. 307.

Because *W* does not process the extracted coal as a mine owner or operator but is instead a purchaser of the coal who applies nominating processes, *W*'s processing of the coal does not constitute a sharing in the risk and control of the mining operation. Therefore, *W*'s processing of the coal does not affect its right to treat its royalty income under section 631(c). *W*'s providing plans, maps, and projections, which *Z* is to follow in mining the coal, raises the question of whether *W* had such risk and control of the mining operation as to warrant treating it as a co-adventurer, partner, or principal in the mining of coal.

The engineering services here, in the form of plans, maps, and projections, are designed to afford *W* some safeguard that the property will be developed according to the plans; in this case they are merely incidental to the extraction of the coal and, as such, do not make *W* a direct participant as a co-adventurer, partner, or participant in the mining operation. Under the lease

agreement, *W* is entitled to a production royalty of 10*x* percent of the amount *Z* receives for the coal and an engineering services royalty of *x* percent of the amount *Z* receives for the coal. The *x* percent is reasonable compensation for the incidental engineering services that are part and parcel of the lease itself. Therefore, considering the lease as a whole, amounts received under it as production royalties and engineering royalties should receive section 631(c) treatment.

HOLDING

Because *W* is not a principal in the mining of coal, *W* is entitled to capital gains treatment under section 631(c) of the Code on both the production royalties and the engineering services royalties. The income derived by *W* from the resale of coal purchased from *Z* is not income from mining and consequently not subject to depletion.

Section 631.—Gain or Loss in the Case of Timber, Coal or Domestic Iron Ore

26 CFR 1.631-3: Gain or loss upon the disposal of coal or domestic iron ore with a retained economic interest.

Whether royalties received by the lessor upon the lease of coal are subject to section 631(c) of the Code capital gains treatment when the royalties are segregated into two categories, one designated as payment for conveyance of an operating interest and the other designated as payment for engineering services? See Rev. Rul. 86-81, page 12.

Section 671.—Trust Income, Deductions, and Credits Attributable to Grantors and Others as Substantial Owners

26 CFR 1.671-3: Attribution or inclusion of income, deductions, and credits against tax.

A grantor-trustee is taxable on all trust income earned in the year the grantor-trustee borrowed the entire trust corpus. See Rev. Rul. 86-82, below

Section 675.—Administrative Powers

26 CFR 1.675-1: Administrative powers.
(Also Section 671; 1.671-3.)

Grantor Trusts; loan from trust to grantor. A grantor-trustee is treated as owner of trust assets where grantor-trustee borrows trust funds and repays the funds with interest in the same year they were borrowed.

Rev. Rul. 86-82

ISSUE

If the grantor of a trust borrows the entire trust corpus and makes complete repayment of principal and interest within the same year, is that grantor treated as owner of the trust under section 675(3) of the Internal Revenue Code?

FACTS

On May 11, 1985, *A* created an irrevocable trust for the benefit of *A*'s children. The trust instrument names *A* trustee and gives *A* power to borrow trust corpus or income at the market rate of interest with adequate security. On June 11, 1985, *A* borrowed 100*x* dollars from the trust in compliance with these requirements. The borrowed funds comprised the entire trust corpus. On November 3, 1985, *A* repaid the loan plus interest. Both *A* and the trust are calendar year taxpayers.

LAW AND ANALYSIS

Section 671 of the Code provides that if any section of subpart E of subchapter J treats the grantor as the owner of any portion of the trust, then the grantor must include in computing taxable income those items of income, deductions, and credits which are attributable to that portion of the trust.

Section 675(3) of the Code provides that, generally, the grantor of a trust will be treated as the owner of any portion of a trust in respect to which the grantor has borrowed the corpus or income and has not completely repaid the loan, including any interest, before the beginning of the taxable year.

In *Mau* v. *United States*, 355 F. Supp. 909 (D. Hawaii 1973), the taxpayer established five separate trusts, with the taxpayer disgnated trustee of each. In 1965, the taxpayer borrowed money from each of the trusts. These amounts were not repaid until 1969. The taxpayer argued that section 675(3) of the Code did not cause the taxpayer-grantor to be liable for federal income tax on the trusts' 1965 income because the loans were not outstanding at the beginning of the year. The court rejected this interpretation of the statute, reasoning that section 675(3) was enacted to prevent the shifting of taxable income in situations where a grantor retained control and use of trust properties through borrowing. Therefore, the court held that the borrowing of trust corpus or income by a grantor at any time during a taxable year would result in the grantor being taxed on trust income for that entire year under section 675(3). The court concluded that the taxpayer was taxable on income of the trusts in 1965, the year the borrowing occurred, even though the loans were made after the beginning of the year. If section 675(3) otherwise applies for a given year, its effect is n[illegible]voided by making repayment before the year closes. *Mau* therefore stands for the principle that section 675(3) applies for any year during any part of which a loan by a trust to the grantor-trustee is outstanding.

In the present case, *A* borrowed the entire trust corpus during calendar 1985. Accordingly, *A* is treated as the owner of the entire trust under section 675(3) of the Code in spite of the fact that *A* made full payment of principal and interest before the close of 1985. *See* section 1.671-3(b)(3) of the regulations. Hence, under section 671, *A* must include in gross income all income earned by the trust in 1985.

HOLDING

Under section 675(3) of the Code, a grantor-trustee who has both borrowed the entire trust corpus and repaid the borrowed funds plus interest in the same year will be treated for federal income tax purposes as the owner of the entire trust for that year.

Section 4941.—Taxes on Self-Dealing

26 CFR 53.4941(e)-1: Definitions.
(Also Sections 4942, 4943, 4944, 4945, 4961, 4963, 4971, 4975, 6212, 6213, 6503, 7422; 53.4942(a)-1, 53.4943-2, 53.4944-5, 53.4945-1, 53.4961-1, 53.4963-1, 54.4971-1, 54.4975-1, 301.6212-1, 301.6213-1, 301.6503(a)-1, 301.7422-1.)

T.D. 8084

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER D, PART 53—FOUNDATION AND SIMILAR EXCISE TAXES; PART 54—PENSION EXCISE TAX REGULATIONS; PART 141—TEMPORARY EXCISE TAX REGULATIONS UNDER THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974; PART 301—PROCEDURE AND

ADMINISTRATION; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Second Tier Excise Taxes

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document provides final regulations relating to second tier excise taxes. Changes to the applicable tax law were made by Pub. L. No. 96-596 [1980-2 C.B. 653]. The regulations will affect private foundations, black lung benefit trusts, pension plans, and disqualified persons with respect to the foregoing, who may become liable for second tier taxes within the meaning of section 4963(b) of the Internal Revenue Code of 1954.

DATES: The amendments to the C.F.R. are effective upon publication in the Federal Register. The amendments to §§53.4941(e)-1(a)(1), 53.4942(a)-1(c)(1)(ii), 53.4943-9(a)(1), 53.4944-5(a)(1), and 53.4963-1(e)(7) apply to first tier taxes imposed under sections 4941, 4942, 4943, and 4944 after December 31, 1969. Under §53.4951-1(a) and (f), the amendment to §53.4941(e)-1(a)(1) applies to first tier taxes imposed under section 4951 after December 31, 1977. The amendments to §§54.4971-1(e) and §53.4963-1(e)(7) apply to first tier taxes imposed under section 4971 after September 2, 1974. The amendments to §54.4975-1(d) apply to first tier taxes imposed under section 4975 after December 31, 1974. The amendments relating to second tier taxes (as defined in section 4963(b)) apply to second tier taxes assessed after December 24, 1980.

FOR FURTHER INFORMATION CONTACT: George B. Baker of the Employee Plans and Exempt Organizations Division, Office of the Chief counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T:EE-16-81, 202-566-3422 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

On February 13, 1984, the Federal Register published proposed amendments to the Foundation and Similar Excise Taxes Regulations (26 CFR Part 53), to the Pension Excise Taxes Regulations (26 CFR Part 54), to the Temporary Excise Tax Regulations under the Employee Retirement Income Security Act of 1974 (26 CFR Part 141) [Pub. L. 93-406, 1974-3 C.B. 1], and to the Procedure and Administration Regulations (26 CFR Part 301), under sections 4941, 4942, 4943, 4944, 4945, 4961, 4962, 4971, 4975, 6213, 6503, 6861, and 7422 [EE-16-81, 1984-1 C.B. 572]. One correction was published in the issue of Friday, March 2, 1984, at page 7836. The amendments were proposed to conform the regulations to section 2 of the Act of December 24, 1980 (Pub. L. No. 96-596, 94 Stat. 3469) [1980-2 C.B. 653]. No comments were received; no public hearing was requested or held. The amendments are therefore adopted as revised by this treasury decision.

EXPLANATION OF PROVISIONS

FINAL REGULATIONS

The amendments conform the regulations to the changes to the Internal Revenue Code made by section 2 of Pub. L. No. 96-596. The Code imposes excise taxes in two tiers to insure compliance with certain provisions of the Code by private foundations, black lung benefit trusts, pension trusts, and disqualified persons with respect to the foregoing entities. A first tier excise tax is imposed automatically if the foundation, trust, or disqualified person engages in a prohibited act (such as self-dealing between a disqualified person and a private foundation), or fails to perform a required act (such as a private foundation's failure to distribute the amount described in section 4942). The Code provides for a much larger second tier excise tax which is imposed at the end of a "taxable period," which begins with the event giving rise to the tax and ends on the earliest of (i) the date a notice of deficiency with respect to the first tier tax is mailed, or (ii) the date the first tier tax is assessed if no proficiency notice is mailed, or (iii) (in some cases) the date the taxable act is corrected. Although the second tier tax is imposed at the end of the taxable period, it is not assessed until after a notice of deficiency is mailed (see sections 6211 through 6216) unless a termination assessment (section 6851) or jeopardy assessment (section 6861) is made.

Under new section 4961, if the taxpayer corrects the act (or failure to act) giving rise to the second tier tax within a "correction period," the tax is not to be assessed, and if assessed, it is to be abated, and if collected, it is to be credited or refunded as an overpayment. See §53.4961-1. The correction period begins on the day the taxable event occurs and ends 90 days after the date of mailing of a notice of deficiency with respect to the second tier tax, but may be extended in certain cases. See §53.4963-1.

Other provisions relate to court proceedings concerning the amount of tax and the timeliness of correction, as well as deferral of assessment or collection during certain court actions. See §53.4961-2.

CHANGES TO NOTICE OF PROPOSED RULEMAKING

The notice of proposed rulemaking proposed deleting or revising a special rule for determining the end of the taxable period and invited comments on this aspect of the proposal. Although no comments were received, upon reconsideration, the Internal Revenue Service has determined to retain the existing special rule. The rule is also incorporated explicitly in regulations for chapter 43 excise taxes (relating to pension plans) in light of the revision of §141.4975-13 and in the interest of promoting procedural uniformity between chapter 42 and 43 taxes.

Under the special rule, the taxable period ends upon filing of a waiver of the restrictions on assessment and collection of a deficiency in first tier tax. This rule does not apply under section 4945 because the taxable period does not affect the amount of the first or second tier tax under section 4945.

Thus, the following provisions are not deleted or revised, as originally proposed: §53.4941(e)-1(a)(3); Example 3 of §53.4941(e)-1(a)(4); §53.4942(a)-1(c)(1)(ii); §53.4943-9(a)(2); and §53.4944-5(a)(2). In addition, a clarifying change has been made to §53.4961-2, proposed new section 53.4963-1 has been adopted as §53.4963-1, and cross references to section 4963 have been adopted as cross references to section 4963.

STUDY OF §53.4943-9(a)(1)(ii)

The Internal Revenue Service believes that §53.4943-9(a)(1)(ii), which provides that the taxable period ends upon elimination of excess business holdings, may not be consistent with the statute. The Service is studying the provision and expects to propose a conforming change.

REGULATORY FLEXIBILITY ACT

Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

NON-APPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

PAPERWORK REDUCTION ACT

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB under control number 1545-0024.

DRAFTING INFORMATION

The principal author of these regulations was George B. Baker of the Employee Plans and Exempt Organizations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments of the regulations

Accordingly, amendments to 26 CFR parts 53, 54, 141, 301, and 602 are adopted as set forth below:

FOUNDATION AND SIMILAR EXCISE TAXES

[26 CFR Part 53]

Paragraph 1. The authority for Part 53 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 2. In §53.4941(b)-1, paragraph (a) is amended by removing the language "correction period (as defined in §53.4941(e)-1(d))." and adding in its place the language "taxable period (as defined in §53.4941(e)-1(a)).".

Par. 3. Section 53.4941(e)-1 is amended as follows:

1. In paragraph (b)(3) and in Example (2) of paragraph (e)(2)(ii), the words "correction period" are removed and the words "taxable period" are added in their place; and

2. Paragraph (a)(1), Example (4) of paragraph (b)(4) and paragraph (d) are revised to read as set forth below.

§53.4941(e)-1 Definitions.

(a) *Taxable period*—(1) *In general*. For purposes of any act of self-dealing, the term "taxable period" means the period beginning with the date on which the act of self-dealing occurs and ending on the earliest of:

(i) The date of mailing of a notice of deficiency under section 6212 with respect to the tax imposed by section 4941(a)(1),

(ii) the date on which correction of the act of self-dealing is completed, or

(iii) The date on which the tax imposed by section 4941(a)(1) is assessed.

* * * * *

(b) *Amount involved*. * * *

(4) *Examples*. * * *

Example (4). D, a disqualified person with respect to private foundation T, purchases 100 shares of stock from T for $5,000 on June 15, 1982. The fair market value of the 100 shares of stock on that date is $4,800. D sells the 100 shares of stock on December 20, 1983, for $6,000. On December 27, 1983, a notice of deficiency with respect to the taxes imposed under subsections (a) and (b) of section 4941 is mailed to D and the taxable period ends. D fails to correct during the taxable period. Between June 15, 1982, and the end of the taxable period, the stock was quoted on the New York Stock Exchange at a high of $67 per share. The amount involved with respect to the tax imposed under subsection (a) is $5,000, and the amount involved with respect to the tax imposed under subsection (b) for failure to correct is $6,700 (100 shares at $67 per share), the highest fair market value during the taxable period.

* * * * *

(d) *Cross reference*. For rules relating to taxable events that are corrected within the correction period, defined in section 4963(e), see section 4961(a), and the regulations thereunder.

* * * * *

Par. 4. Section 53.4942(a)-1 is amended as follows:

1. In paragraph (a)(2), the language "correction period" and "paragraph (c)(3)" is removed and the language "taxable period" and "paragraph (c)(1)", respectively, is added in its place;

2. In paragraph (c)(4), Example (3) is removed; and

3. Paragraph (a)(4), paragraph (c)(1)(i), and paragraph (c)(3) are revised to read as set forth below.

§53.4942(a)-1 Taxes for failure to distribute income.

(a) *Imposition of tax*. * * *

(4) *Examples*. The provisions of this paragraph may be illustrated by the following examples:

Example (1). *M*, a private foundation which uses the calendar year as its taxable year, has at the end of 1981, $50.000 of undistributed income (as defined in paragraph (a) of §53.4942(a)-2) for 1981. As of January 1, 1983, $40,000 is still undistributed. On August 15, 1983, a notice of deficiency with respect to the excise taxes imposed by section 4942(a) and (b) is mailed to *M* under section 6212(a) and the taxable period ends. Thus, under these facts, an initial excise tax of $6,000 (15 percent of $40,000) is imposed upon *M*. An additional excise tax of $40,000 (100 percent of $40,000) is imposed by section 4942(b). Under section 4961(a), however, if the undistributed income is reduced to zero during the correction period, this latter tax will not be assessed, and if assessed, it will be abated, and if collected, it will be credited or refunded as an overpayment.

Example (2). Assume the facts as stated in example (1), except that the notice of deficiency is mailed to *M* on September 7, 1984, and as of January 1, 1984, only $10,000 of the $50,000 of undistributed income with respect to 1981 is undistributed. Therefore, initial excise taxes of $6,000 (15 percent of $40,000, *M*'s undistributed income from 1981, as of January 1, 1983) and $1,500 (15 percent of $10,000, *M*'s undistributed income from 1981 as of January 1, 1984) are imposed by section 4942(a). If the $10,000 remains undistributed as of September 7, 1984, the end of the taxable period, an additional excise tax of $10,000 (100 percent of $10,000, *M*'s undistributed income from 1981, as of September 7, 1984) is imposed by section 4942(b).

* * * * *

(c) *Certain periods*. For purposes of this section—

(1) *Taxable period.* (i) The term "taxable period" means with respect to the undistributed income of a private foundation for any taxable year, the period beginning with the first day of the taxable year and ending on the earlier of:

(A) The date of mailing of notice of deficiency under section 6212(a) with respect to the initial excise tax imposed under section 4942(a), or

(B) The date on which the initial excise tax imposed under section 4942(a) is assessed.

For example, assume M, a private foundation which uses the calendar year as the taxable year, has $15,000 of undistributed income for 1981. A notice of deficiency is mailed to M under section 6212(a) on June 1, 1983. With respect to the undistributed income of M for 1981, the taxable period began on January 1, 1981, and ended on June 1, 1983.

* * * * *

(3) *Cross reference.* For rules relating to taxable events that are corrected within the correction period, defined in section 4963(e), see section 4961(a) and the regulations thereunder.

* * * * *

Par. 5. In §53.4942(a)-3, Example (2) of paragraph (d)(3) is revised to read as follows:

§53.4942(a)-3 Qualifying distributions defined.

* * * * *

(d) *Treatment of qualifying distributions.* * * *

(3) *Examples.* * * *

Example (2). M, a private foundation which uses the calendar year as the taxable year, has undistributed income of $300 for 1981, $200 for 1982, and $400 for 1983. On January 14, 1983, *M* makes its first qualifying distribution in 1983 when it sets aside (within the meaning of paragraph (b) of this section $700 for construction of a hospital. On February 24, 1983 a notice of deficiency with respect to the excise taxes imposed by section 4942(a) and (b) in regard to *M*'s undistributed income for 1981 is mailed to *M* under section 6212(a). *M* notifies the Commissioner in writing on March 24, 1983, that it is making an election under subparagraph (2) of this paragraph to have its distribution of January 14th applied first against its undistributed income for 1982, next against its undistributed income for 1981, and last against its undistributed income for 1983. Thus, $200 of the $700 qualifying distribution is treated as made out of the undistributed income for 1982; $300, out of undistributed income for 1981; and $200 ($700 less the sum of $200 and $300), out of the undistributed income for 1983. Thus, an initial excise tax of $45 (15 percent of $300) is imposed under section 4942(a). Since *M* made the election described above, the $300 (treated as distributed out of undistributed income for 1981) corrects (within the meaning of section 4963(d)(2)) the taxable act because the undistributed income for 1981 is reduced to zero. Furthermore, correction is effected within the correction period (as defined in section 4963(e)(1) and §53.4963-1(e)). Therefore, under the provisions of section 4961(a), the additional tax imposed by section 4942(b) will not be assessed.

* * * * *

Par. 6. In §53.4943-2, paragraph (b) is revised to read as follows:

§53.4943-2 Imposition of tax on excess business holdings of private foundations.

* * * * *

(b) *Additional tax.* In any case in which the initial tax is imposed under section 4943(a) with respect to the holdings of a private foundation in any business enterprise, if, at the close of the taxable period (as defined in section 4943(d)(2) and §53.4943-9) with respect to such holdings the foundation still has excess business holdings in such enterprise, there is imposed a tax under section 4943(b) equal to 200 percent of the value of such excess holdings as of the last day of the taxable period.

Par. 7. In §53.4943-9, paragraph (a)(1) and paragraph (b) are revised to read as set forth below.

§53.4943-9 Business holdings; certain periods.

(a) *Taxable period—*(1) *In general.* For purposes of section 4943, the term "taxable period" means, with respect to any excess business holdings of a private foundation in a business enterprise, the period beginning with the first day on which there is such excess business holdings and ending on the earliest of:

(i) The date of mailing of a notice of deficiency under section 6212 with respect to the tax imposed on the holdings by section 4943(a);

(ii) The date on which the excess is eliminated; or

(iii) The date on which the tax imposed by section 4943(a) is assessed.

For example, *M*, a private foundation, first has excess business holdings in *X*, a corporation, on February 5, 1972. A notice of deficiency is mailed under section 6212 to *M* on June 1, 1974. With respect to *M*'s excess business holdings in *X*, the taxable period begins on February 5, 1972, and ends on June 1, 1974.

* * * * *

(b) *Cross reference.* For rules relating to taxable events that are corrected within the correction period, defined in section 4963(e), see section 4961(a) and the regulations thereunder.

* * * * *

Par. 8. Section 53.4944-2 is amended as follows:

1. In paragraph (a), the words "correction period" are removed from the first and third sentences and the words "taxable period" are added in their place, and the language "4944(e)(3)" is removed from the first sentence and the language "4944(e)(1)" is added in its place; and

2. At the end of paragraph (b), in the fourth sentence of Example (1) in paragraph (c), and in the first and second sentences of Example (3) in paragraph (c), the words "correction period" are removed and the words "taxable period" are added in their place.

Par. 9. In §53.4944-5, paragraphs (a)(1) and (d) are revised to read as set forth below.

§53.4944-5 Definitions.

(a) *Taxable period—*(1) *In general.* For purposes of section 4944, the term "taxable period" means, with respect to any investment which jeopardizes the carrying out of a private foundation's exempt purposes, the period beginning with the date on which the amount is invested and ending on the earliest of:

(i) The date of mailing of a notice of deficiency under section 6212 with respect to the tax imposed on the making of the investment by section 4944(a)(1);

(ii) The date on which the amount invested is removed from jeopardy; or

(iii) The date on which the tax imposed by section 4944(a)(1) is assessed.

* * * * *

(d) *Cross reference.* For rules relating to taxable events that are corrected within the correction period, defined in section 4963(e), see section 4961(a) and the regulations thereunder.

Par. 10. Section 53.4945-1 is

amended as follows:

1. In the first sentence of paragraph (b)(1), the words "correction period" are removed and the words "taxable period" are added in their place; and

2. Example (2) in paragraph (c)(3) and paragraph (e) are revised to read as set forth below.

§53.4945-1 Taxes on taxable expenditures.

* * * * *

(c) *Special rules.* * * *

(3) *Examples.* * * *

Example (2). Assume the same facts as in example (1). Further assume that within the taxable period A makes a motion to correct the taxable expenditure at a meeting of the board of directors. The motion is defeated by a two-to-one vote, A voting for the motion and B and C voting against it. In these circumstances an additional tax is imposed on the private foundation in the amount of $100,000 (100 percent of $100,000). The additional tax imposed on B and C is $10,000 (50 percent of $100,000 subject to a maximum of $10,000). B and C are jointly and severally liable for the $10,000, and this sum may be collected by the Service from either of them.

* * * * *

(e) *Certain periods*—(1) *Taxable period.* For purposes of section 4945, the term "taxable period" means, with respect to any taxable expenditure, the period beginning with the date on which the taxable expenditure occurs and ending on the earlier of:

(i) The date of mailing of a notice of deficiency under section 6212 with respect to the tax imposed on taxable expenditures by section 4945(a)(1); or

(ii) The date on which the tax imposed by section 4945(a)(1) is assessed.

(2) *Cross reference.* For rules relating to taxable events that are corrected within the correction period, defined in section 4963(e), see section 4961(a) and the regulations thereunder.

Par. 11. Sections 53.6001-1 through 53.7101-1 (Subpart K) of Part 53 are redesignated subpart L, and a new subpart K is added to read as follows:

SUBPART K—SECOND TIER EXCISE TAXES

Sec.

53.4961-1 Abatement of second tier taxes for correction within correction period.
53.4961-2 Court proceedings to determine liability for second tier tax.
53.4963-1 Definitions.

§53.4961-1 Abatement of second tier taxes for correction within correction period.

If any taxable event is corrected during the correction period for the event, then any second tier tax imposed with respect to the event shall not be assessed. If the tax has been assessed, it shall be abated. If the tax has been collected, it shall be credited or refunded as an overpayment. For purposes of this section, the tax imposed includes interest, additions to the tax and additional amounts. For definitions of the terms "second tier tax," "taxable event," "correct," and "correction period," see §53.4963-1.

§53.4961-2 Court proceedings to determine liability for second tier tax.

(a) *Introduction.* Under section 4961(b) and (c), the period of limitations on collection may be suspended and assessment or collection of first or second tier tax may be prohibited during the pendency of administrative and judicial proceedings conducted to determine a taxpayer's liability for second tier tax. This section provides rules relating to the suspension of the limitations period and the prohibitions on assessment and collection. In addition, this section describes the administrative and judicial proceedings to which these rules apply.

(b) *Initial proceeding*—(1) *Defined.* For purposes of subpart K, an initial proceeding means a proceeding described in subparagraph (2) or (3).

(2) *Tax Court proceeding before assessment.* A proceeding is described in this subparagraph (2) if it is a proceeding with respect to the taxpayer's liability for second tier tax and is commenced in accordance with section 6213(a).

(3) *Refund proceeding commenced before correction period ends.* A proceeding is described in this subparagraph (3) if it is a proceeding commenced under section 7422, in accordance with the provisions of §53.4963-1(e)(4) and (5) (relating to prerequisites to extension of the correction period during certain refund proceedings), and with respect to the taxpayer's liability for second tier tax.

(c) *Supplemental proceeding*—(1) *Jurisdiction.* If a determination in an initial proceeding that a taxpayer is liable for a second tier tax has become final, the court in which the initial proceeding was commenced shall have jurisdiction to conduct any necessary supplemental proceeding to determine whether the taxable event was corrected during the correction period.

(2) *Time for beginning proceeding.* The time for beginning a supplemental proceeding begins on the day after a determination in an initial proceeding becomes final and ends on the 90th day after the last day of the correction period.

(d) *Restriction on assessment during Tax Court proceeding.* If a supplemental proceeding described in section 4961(b) and §53.4961-2(c) is commenced in the Tax Court, the provisions of the second and third sentences of section 6213(a) and the first and third sentences of §301.6213-1(a)(2) apply with respect to a deficiency in second tier tax until the decision of the Tax Court in the supplemental proceeding is final.

(e) *Suspension of period of collection for second tier tax*—(1) *Scope.* Except as provided in subparagraph (6), this paragraph (e) applies to the second tier tax assessed with respect to a taxable even tif a claim described in subparagraph (2) is filed.

(2) *Claim for refund.* A claim for refund is described in this subparagraph (2) if, no later than 90 days after the day on which the second tier tax is assessed with respect to a taxable event, the taxpayer—

(i) Pays the full amount of first tier tax for the taxable period, and

(ii) Files a claim for refund of the amount paid.

(3) *Collection prohibited.* No levy or proceeding in court for the collection of the second tier tax shall be made, begun, or prosecuted until the end of the collection prohibition period described in subparagraph (5). Notwithstanding section 7421(a), the collection by levy or proceeding may be enjoined during the collection prohibition period by a proceeding in the proper court.

(4) *Suspension of running of period of limitations on collection.* With respect to a second tier tax to which this paragraph (e) applies, the running of the period of limitations provided in section 6502 (relating to collection of tax by levy or by a proceeding in court) shall be suspended for the collection

prohibition period described in subparagraph (5).

(5) *Collection prohibition period.* The collection prohibition period begins on the day the second tier tax is assessed and ends on the latest of:

(i) The day a decision in a refund proceeding commenced before the 91st day after denial of the claim described in subparagraph (2) of this paragraph (including any supplemental proceeding under §53.4961-2(c)) becomes final;

(ii) The 90th day after the claim referred to in subparagraph (2) is denied; or

(iii) The 90th day after the second tier tax is assessed.

(6) *Jeopardy collection.* If the Secretary makes a finding that the collection of the second tier tax is in jeopardy, nothing in this paragraph (e) shall prevent the immediate collection of such tax.

(f) *Finality*—(1) *Tax Court proceeding.* For purposes of this subpart K, section 7481 applies in determining when a decision in a Tax Court proceeding becomes final.

(2) *Refund proceeding.* For purposes of this subpart K, §301.7422-1 applies in determining when a decision in a refund proceeding becomes final.

§53.4963-1 Definitions.

(a) *First tier tax.* The purposes of this subpart K, the term "first tier tax" means any tax imposed by subsection (a) of section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4971, or 4975. A first tier tax may also be referred to as an "initial tax" in parts 53 and 54.

(b) *Second tier tax.* For purposes of this subpart K, the term "second tier tax" means any tax imposed by subsection (b) of section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4971, or 4975. A second tier tax may also be referred to as an "additional tax" in parts 53 and 54.

(c) *Taxable event.* For purposes of this subpart K, the term "taxable event" means any act, or failure to act, giving rise to liability for tax under section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4971, or 4975.

(d) *Correct*—(1) *In general.* Except as provided in subparagraph (2), the term "correct" has the same meaning for purposes of this subpart K as in the section which imposes the second tier tax or the regulations thereunder.

(2) *Special rules.* The term "correct" means—

(i) For a second tier tax imposed by section 4942(b), reducing the amount of the undistributed income to zero,

(ii) For a second tier tax imposed by section 4943(b), reducing the amount of the excess business holdings to zero, and

(iii) For a second tier tax imposed by section 4944(b), removing the investment from jeopardy.

(e) *Correction period*—(1) *In general.* The correction period with respect to any taxable event shall begin with the date on which the taxable event occurs and shall end 90 days after the date of mailing of a notice of deficiency under section 6212 with respect to the second tier tax imposed with respect to the taxable event.

(2) *Extensions of correction period.* The correction period referred to in subparagraph (1) of this paragraph shall be extended by any period in which a deficiency cannot be assessed under section 6213(a). In addition, the correction period referred to in subparagraph (1) of this paragraph (e) shall be extended in accordance with subparagraphs (3), (4), and (5) of this paragraph except that subparagraph (4) and (5) shall not operate to extend a correction period with respect to which a taxpayer has filed a petition with the United States Tax Court for redetermination of a deficiency within the time prescribed by section 6213(a).

(3) *Extensions by Commissioner.* The correction period referred to in subparagraph (1) of this paragraph may be extended by any period which the Commissioner determines is reasonable and necessary to bring about correction (including, for taxes imposed by section 4975, equitable relief sought by the Secretary of Labor) of the taxable event. The Commissioner ordinarily will not extend the correction period unless the following factors are present:

(i) The taxpayer on whom the second tier tax is imposed, the Secretary of Labor (for taxes imposed by section 4975), or an appropriate State officer (as defined in section 6104(c)(2)) is actively seeking in good faith to correct the taxable event;

(ii) Adequate corrective action cannot reasonably be expected to result during the unextended correction period;

(iii) For taxes imposed by section 4975, the Secretary of Labor requests the extension because subdivision (ii) applies; and

(iv) For taxes imposed by chapter 42 (other than taxes imposed by section 4940), the taxable event appears to have been an isolated occurrence so that it appears unlikely that similar taxable events will occur in the future.

(4) *Extension for payment of first tier tax.* If, within the unextended correction period, the taxpayer pays the full amount of the first tier tax imposed with respect to the taxable event the Commissioner shall extend the correction period to the later of—

(i) Ninety days after the payment of the first tier tax, or

(ii) The last day of the correction period determined without regard to this paragraph.

(5) *Extensions for filing claim for refund or refund suit.* If prior to the expiration of the correction period (including extensions) a claim for refund is filed with respect to payment of the full amount of the first tier tax imposed with rspect to the taxable event, the Commissioner shall extend the correction period during the pendency of the claim plus an additional 90 days. If within that time a suit or proceeding referred to in section 7422(g) with respect to the claim is filed, the Commissioner shall extend the correction period until the determination in the suit for refund (determined without regard to a supplemental proceeding under section 4961(b)) is final, determined under §301.7422-2(a).

(6) *End of correction period if waiver accepted.* If the notice of deficiency referred to in paragraph (1) is not mailed because there is a waiver of the restrictions on assessment and collection of the deficiency or because the deficiency is paid, the correction period will end of the collection prohibition period described in §53.4961-2(e)(5).

(7) *Date on which taxable event occurs.* For purposes of subparagraph (1), the taxable event shall be treated as occurring—

(i) Under section 4942, on the first day of the taxable year for which there is undistributed income,

(ii) Under section 4943, on the first day on which there are excess business holdings,

(iii) Under section 4971, on the last day of the plan year in which there is an accumulated funding deficiency, and

(iv) In all other cases, the date on which the event occurred.

(f) *Effective date*. The provisions of this subpart K are effective with respect to second tier taxes assessed after December 24, 1980. The preceding sentence shall not be construed to permit the assessment of a tax in a case to which, on December 24, 1980, the doctrine of res judicata applied.

PENSION EXCISE TAX REGULATIONS
[26 CFR Part 54]

Par. 12. The authority for Part 54 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 13. Section 54.4971-1 is added immediately after the authority citation for Part 54 to read as follows:

§54.4971-1 General rules relating to excise tax on failure to meet minimum funding standards.

(a) [Reserved]

(b) [Reserved]

(c) *Additional tax*. Section 4971(b) imposes an excise tax in any case in which an initial tax is imposed under section 4971(a) on an accumulated funding deficiency and the accumulated funding deficiency is not corrected within the taxable period (as defined in section 4971(c)(3)). The additional tax is 100 percent of the accumulated funding deficiency to the extent not corrected.

(d) [Reserved]

(e) *Definition of taxable period*—(1) *In general*. For purposes of any accumulated funding deficiency, the term "taxable period" means the period beginning with the end of the plan year in which there is an accumulated funding deficiency and ending on the earlier of:

(i) The date of mailing of a notice of deficiency under section 6212 with respect to the tax imposed by section 4971(a), or

(ii) The date on which the tax imposed by section 4971(a) is assessed.

(2) *Special rule*. Where a notice of deficiency referred to in paragraph (e)(1)(i) of this section is not mailed because a waiver of the restrictions on assessment and collection of a deficiency has been accepted or because the deficiency is paid, the date of filing of the waiver or the date of such payment, respectively, shall be treated as the end of the taxable year.

Par. 14. Section 54.4975-1 is added immediately after §54.4974-1 to read as follows:

§54.4975-1 General rules relating to excise tax on prohibited transactions.

(a) *Scope*. This section provides general rules for the imposition of the excise taxes on prohibited transactions.

(b) *Initial tax*. Section 4975(a) imposes an initial tax on each prohibited transaction. The initial tax is 5 percent of the amount involved with respect to the prohibited transaction for each year (or part thereof) in the taxable period.

(c) *Additional tax*. Section 4975(b) imposes an excise tax in any case in which an initial tax is imposed under section 4975(a) on a prohibited transaction and the prohibited transaction is not corrected within the taxable period (as defined in paragraph (d) of this section). The additional tax is 100 percent of the amount involved with respect to the prohibited transaction.

(d) *Taxable period*—(1) In general. For purposes of any prohibited transaction, the term "taxable period" means the period beginning with the date on which the prohibited transaction occurs and ending on the earliest of:

(i) The date of mailing of a notice of deficiency under section 6212 with respect to the tax imposed by section 4975(a);

(ii) The date on which correction of the prohibition transaction is completed; or

(iii) The date on which the tax imposed by section 4975(a) is assessed.

(2) *Special rule*. Where a notice of deficiency referred to in paragraph (d)(1)(i) of this section is not mailed because a waiver of the restrictions on assessment and collection of a deficiency has been accepted or because the deficiency is paid, the date of filing of the waiver or the date of such payment, respectively, shall be treated as the end of the taxable period.

TAXABLE EXCISE TAX REGULATIONS UNDER THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974
[26 CFR Part 141]

Par. 15. The authority for Part 141 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 16. In §141.4975-13, the title is revised to read as set forth below, and the language "4975(f)(2), (4), (5) and (6)" is removed and the language "4975(f)(4) and (5)" is added in its place.

§141.4975-13 Definition of "amount involved" and "correction".

* * * * *

PROCEDURE AND ADMINISTRATION
[26 CFR Part 301]

Par. 17. the authority for Part 301 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 18. In §301.6212-1 the following two sentences are added at the end of paragraph (c):

§301.6212-1 Notice of deficiency.

* * * * *

(c) *Further deficiency letters restricted.* * * * Solely for purposes of applying the restriction of section 6212(c), a notice of deficiency with respect to second tier tax under chapter 43 shall be deemed to be a notice of deficiency for the taxable year in which the taxable event occurs. See §53.4963-1(e)(7)(iii) or (iv) for the date on which the taxable event occurs.

Par. 19. In §301.6213-1, the first sentence of paragraph (e) is revised to read as follows:

§301.6213-1 Restrictions applicable to deficiencies; petition to Tax Court.

* * * * *

(e) *Suspension of filing period for certain chapter 42 and chapter 43 taxes.* The period prescribed by section 6213)(a) for filing a petition in the Tax Court with respect to the taxes imposed by section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4971, or 4975, shall be suspended for any other period which the Commissioner has allowed for making correction under §53.4963-1(e)(3). * * *

Par. 20. Paragraph (a) of §301.6503(a)-1 is amended by adding a new subparagraph (3) to read as follows:

§301.6503(a)-1 Suspension of running of period of limitation; issuance of statutory notice of deficiency.

(a) *General rule.* * * *

(3) For provisions relating to suspension of the running of the period of

limitation with respect to collection of "second tier" excise taxes (as defined in section 4963) until final resolution of a refund proceeding described in sections 4961 and 7422 for the determination of the taxpayer's liability for the second tier taxes, see §53.4961-2(e)(4).

* * * * *

Par. 21. Section 301.6503(g)-1 is amended by removing all of the text that follows the word "correction" and adding the language "under section 4963(e)(1)(B)." in its place.

Par. 22. In §301.6861-1, paragraph (g) is amended by removing the last sentence.

Par. 23. Section 301.7422-1 is revised to read as follows:

§301.7422-1 Special rules for certain excise taxes imposed by chapter 42 or 43.

(a) *Finality of refund proceeding.* For purposes of sections 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4961, 4963, 4971, and 4975, and the regulations thereunder, a decision in a suit for refund instituted under the provisions of this section shall be final—

(1) Upon the expiration of the time allowed for filing a notice of appeal from a decision of the United States Claims Court or the United States District Court, if no timely notice of appeal is filed; or

(2) Upon the expiration of the time allowed for filing a petition for certiorari from a decision of the United States Claims Court, or from a decision of the United States District Court, which has been affirmed or the appeal dismissed by the United States Court of Appeals, if no timely petition for certiorari is filed; or

(3) If a petition for certiorari has been filed, thirty days from the denial of such petition; or

(4) Thirty days from the date of a decision of the United States Supreme Court if no timely petition for rehearing is filed; however, if a timely petition for rehearing from such a decision is filed, and is denied, thirty days from the denial thereof; or

(5) If a decision is entered upon a rehearing or if a decision is modified or reversed as the result of a decision of higher court, upon the expiration, with respect to the decision or rehearing or the modified or reversed decision, of periods similar to those provided in subparagraphs (1) through (4).

(b) *Right to bring action.* With respect to any taxable event, payment of the full amount of first tier tax for the taxable period shall constitute sufficient payment in order to maintain an action under this section with respect to the second tier tax.

(c) *Limitation on suit for refund.* No suit may be maintained under this section for the credit or refund of any tax imposed under section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4971, or 4975 with respect to any taxable event unless—

(1) No other suit has been maintained for credit or refund of any tax imposed by such sections with respect to such taxable event; and

(2) No petition has been filed in the Tax Court with respect to a deficiency in any tax imposed by such sections with respect to such taxable event.

(d) *Final determination of issues.* For purposes of this section, any suit for the credit or refund of any tax imposed under ection 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4971, or 4975, together with a supplemental proceeding (if any) under section 4961(b), with respect to any taxable event, shall constitute a suit to determine all questions with respect to any other tax imposed with respect to such taxable event under such sections. Consequently, failure by the parties to the suit to bring before the Court any question described in the preceding sentence shall constitute a bar to the question.

(e) *Definitions.* For definitions of the terms "taxable event," "first tier tax," and "second tier tax," see §53.4963-1.

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

[26 CFR Part 602]

Par. 24. Part 602 is amended as follows:

1. The authority citation for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805

2. Section 602.101(c), is amended by inserting in the appropriate places in the tables "53.4961-2(e)(2) . . . . 1545-0024," and "53.4963-1(e)(5) . . . . 1545-2024".

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved April 3, 1986.

J. ROGER MENTZ,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on May 1, 1986, 8:45 a.m., and published in the issue of the Federal Register for May 2, 1986, 51 F.R. 16300)

Section 4942.—Taxes on Failure to Distribute Income

26 CFR 53.4942(a)-1: Taxes for failure to distribute income.

Second tier excise tax imposed on private foundations. See T.D. 8084, page 14.

Section 4943.—Taxes on Excess Business Holdings

26 CFR 53.4943-2: Imposition of tax on excess business holdings of private foundations.

Second tier excise tax imposed on private foundations. See T.D. 8084, page 14.

Section 4944.—Taxes on Investments Which Jeopardize Charitable Purpose

26 CFR 53.4944-5: Definitions.

Second tier excise tax imposed on private foundations. See T.D. 8084, page 14.

Section 4945.—Taxes on Taxable Expenditures

26 CFR 4945-1: Taxes on taxable expenditures.

Second tier excise tax imposed on private foundations. See T.D. 8084, page 14.

Section 4961.—Abatement of Second Tier Taxes Where There is Correction

26 CFR 53.4961-1: Abatement of second tier taxes for correction within correction period.

Second tier excise tax imposed on private foundations. See T.D. 8084, page 14.

Section 4963.—Definitions

26 CFR 53.4963-1: Definitions.

Second tier excise tax imposed on private foundations. See T.D. 8084, page 14.

Section 4971.—Taxes on Failure to Meet Minimum Funding Standards

26 CFR 54.4971-1: General rules relating to excise tax on failure to meet minimum funding standards.

Second tier excise tax imposed on qualified pension, etc., plans. See T.D. 8084, page 14.

Section 4975.—Tax on Prohibited Transactions

26 CFR 54.4975-1: General rules relating to excise tax on prohibited transactions.

Second tier excise tax imposed on qualified pension, etc., plans. See T.D. 8084, page 14.

Section 6212.—Notice of Deficiency

26 CFR 301.6212-1: Notice of deficiency.

Second tier excise tax imposed on qualified pension, etc., plans. See T.D. 8084, page 14.

Section 6213.—Restrictions Applicable to Deficiencies; Petition to Tax Court

26 CFR 301.6213-1: Restrictions applicable to deficiencies; petition to Tax Court.

Second tier excise tax imposed on private foundations and qualified pension, etc., plans. See T.D. 8084, page 14.

Section 6503.—Suspension of Running of Period of Limitation

26 CFR 301.6503(a)-1: Suspension of running of period of limitation; issuance of statutory notice of deficiency.

Second tier excise tax imposed on private foundations and qualified pension, etc., plans. See T.D. 8084, page 14.

Section 7422.—Civil Actions for Refund

26 CFR 301.7422-1: Special rules for certain excise taxes imposed by chapter 42 or 43.

Second tier excise tax imposed on private foundations and qualified pension, etc., plans. See T.D. 8084, page 14.

Part III. Administrative, Procedural, and Miscellaneous

Inflation Adjustment for Computation of Windfall Profit Tax

Notice 86-7

Section 4989(b) of the Internal Revenue Code requires the determination of an inflation adjustment factor for use in computing the windfall profit tax.

The Service has determined that, for oil removed during the July-September quarter of 1986, the inflation adjustments are as follows:

Tier 1 or Tier 2 oil	0.4614
Tier 3 oil	0.6721

Worksheets for computation of the windfall profit tax are included in the Instructions for Form 6047, Windfall Profit Tax, and an explanation of the inflation adjustment may be found in the Specific Instructions for Line 4 of the worksheets.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Section 338(g)—Statements of Election

LR-8-86

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking by cross-reference to temporary regulations.

SUMMARY: * * * [T]he Internal Revenue Service is amending temporary regulations relating to section 338(g) of the Internal Revenue Code of 1954 ("Code") as added by the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") [Pub. L. 97-248, 1982-2 C.B. 462]. The amendments provide additional guidance to taxpayers concerning the filing of certain statements of election under section 338 on or after December 9, 1985, and on or before July 15, 1986. An amendment to temporary regulation §1.338-4T also clarifies the application of the mitigation of limitations provisions. The temporary regulations also extend the time for taking certain actions under section 338. The text of the new and revised sections also serves as the comment document for this notice of proposed rulemaking.

DATES:

PROPOSED EFFECTIVE DATE

The regulations are proposed to apply generally to stock acquisitions made after August 31, 1982. Certain provisions would only apply with respect to elections under section 338 filed on or after December 9, 1985, and on or before July 15, 1986.

DATES FOR COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Written comments and requests for a public hearing must be delivered or mailed by July 15, 1986.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T [LR-8-86], Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Thomas J. Kane of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) or telephone 202-566-3458 (not a toll-free call).

SUPPLEMENTARY INFORMATION: BACKGROUND

Temporary regulations published * * * [on page 4, this Bulletin] amend temporary regulations §§1.338-1T, 1.338-2T, 1.338-4T, 1.338-5T, and 1.338(h)(10)-1T in Part 1 of Title 26 of the Code of the Federal Regulations ("CFR"). The final regualtions that are proposed to be based on the amended temporary regulations would be added to Part 1 of Title 26 of the CFR. Those final regulations would provide guidance on filing certain statements of election under section 338(g) of the Internal Revenue Code. Section 338(g) was added by section 224 of TEFRA (Pub. L. No. 97-248; 96 Stat. 485) [Pub. L. 97-248, 1982-2 C.B. 462, 501] and was amended by section 712(k) of the Tax Reform Act of 1984 (Pub. L. No. 98-369; 98 Stat. 948) [1984-3 C.B. (Vol. 1) 1, 456]. For the text of the amendments to the temporary regulations, see T.D. 8088, published * * * [on page 4, this Bulletin]. The preamble to the temporary regulations explains the additions to the regulations.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required.

COMMENTS AND REQUEST FOR A PUBLIC HEARING

Before these proposed regulations are adopted, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

DRAFTING INFORMATION

The principal author of these proposed regulations is Thomas J. Kane of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on May 15, 1986, 8:45 a.m., and published in the issue of the Federal Register for May 16, 1986, 51 F.R. 17989)

Deletions from Cumulative List of Organizations Contributions to Which Are Deductible Under Section 170 of the Code

Announcement 86-74

The names of organizations that no longer qualify as organizations described in section 170(c)(2) of the Internal Revenue Code of 1954 are listed below.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgment has been timely filed, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deductible. Protection under section 7428(c) would begin on June 16, 1986, (the date of publication of this announcement) and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is $1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

Creative Learning Institute, Inc., Atlanta, GA

National Institute of Christian Education, Tulsa, OK

Peoria J. Woods Center for Senior Citizens and the Blind, Inc., Atlanta, GA

Form 3115, Application for Change in Accounting Method, Revised

Announcement 86-75

Form 3115, Application for Change in Accounting Method, has been revised.

The revised form includes a new section for use by contractors who want to change to the "completed contract" method of accounting provided by section 1.451-3(d) of the regulations. The form also includes updated referencs to the appropriate revenue procedure (now Rev. Proc. 84-74) governing changes in accounting methods.

The form and its instructions, which are now issued separately, have a revision date of April 1986. They are now available at most Internal Revenue Service district offices.

Form 990-PF, Return of Private Foundation

Announcement 86-76

The Service has received a number of inquiries regarding Part V of the 1985 Form 990-PF, Return of Private Foundation. Exempt domestic foundations use this new Part V, Qualification Under Section 4940(e) for Reduced Tax on Net Investment Income, to determine whether they met a two-part test qualifying them to be taxed on their net investment income at a one percent tax rate for 1985 rather than at the normal two percent rate.

The threshold test, which is included in the heading of Part V, is that the foundation may not have been liable for section 4942 tax with respect to the distributable amount of any year in a base period consisting of the five preceding years. This test differs from the threshold test contained in section 4940(e)(2)(B) as enacted in 1984 (a five percent minimum payout rate over the base period) but follows the amendment initially contained in the proposed Technical Corrections Act of 1985 (H.R. 1800 and S. 814). This technical amendment of section 4940(e) still has not been enacted, but the provision is noncontroversial and its eventual enactment is certain. The Service has been assured by the staff of the Joint Committee on Taxation that the amendment, when enacted, will be retroactive to tax years beginning in 1985.

The Service designed Part V of the 1985 Form 990-PF anticipating this law change to obviate the need for the filing of amended returns by foundations that qualified for the one percent tax reduction under either the original provision or the provision as amended, but not under both. The Joint Committee staff and the Department of Treasury endorsed the Service's proposal to print the 1985 form incorporating the pending amendment of section 4940(e).

Foundations, therefore, should prepare Part V of the 1985 Form 990-PF in accordance with the form and instructions and without regard to current section 4940(e)(2)(B).

Form 5471 Series, Information Return With Respect to a Foreign Corporation, Revised

Announcement 86-77

Form 5471, Information Return With Respect to a Foreign Corporation, its instructions, and Schedule M have been revised to reflect a change to the regulations under section 6038 of the Internal Revenue Code. Although Schedules N and O (Form 5471) were not revised, the entire Form 5471 series was reprinted with a revision date of January 1986 and is now available in most IRS Distribution Centers.

The regulations now require the reporting of transactions between foreign corporations owned by the same U.S. person. As a result, taxpayers who control more than one foreign corporation must now report the activities between these corporations on Schedule M (Form 5471). Taxpayers are also now required to file a duplicate copy of Form 5471 and any appropriate schedule with the Philadelphia Service Center, as well as with their income tax returns.

Taxpayers whose tax years began before August 24, 1985, may use the prior version of the form, the January 1985 revision. In addition, any taxpayer whose tax year began in 1985 but after August 23 may also use the 1985 version of Form 5471; however, they must use the 1986 version of Schedule M. For tax years starting 1986 the 1986 version of Form 5471, including Schedule M, must be used.

Additionally, since regulations section 1.6038-2(g) allows the use of attached statements prepared in accordance with generally accepted accounting principles, taxpayers using the 1986 revision of Form 5471 may continue to use these attached statements in lieu of completing Schedules C, D, E, F, and I. The instructions to the 1986 revision of Form 5471 requiring the completion of these schedules may be disregarded if the attached statements are used. However, taxpayers are encouraged to complete the lines of the schedules so they can be more easily processed.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Mack I. Frank	Eunice, LA	Attorney	Indefinite from April 1, 1986
Carl Goldfarb	Charlotte, NC	Attorney	Indefinite from April 28, 1986
Dennis M. Hayes	Ann Arbor, MI	Attorney	Indefinnite from April 15, 1986
Ronald N. Kief	Warren, MI	Certified Public Accountant	Two Years from June 1, 1986
Richard L. Leopold	Ottawa, OH	Attorney	Three Months from May 1, 1986
Julius Stackel	Flushing, NY	Certified Public Accountant	Thirty Months from April 15, 1986
John Such	Lyndhurst, OH	Enrolled Agent	Eighteen Months from April 22, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 301.6221-1, 301.6233-1 and intermediate sections, added.	Tax treatment of partnership items	1986-21 I.R.B. 12	June 17, 1986
26 CFR 1.367(a)-1, removed; 1.367(a)-4T, redesignated as 1.367(a)-7T; 1.367(a)-1T through 1.367(a)-6T, 1.367(d)-1T, 1.6038B-1T, added; 7.367(b)-1, 7.367(b)-4, amended; published as temporary regulations in T.D. 8087, page 5, 1986-23 I.R.B.	Transfers of property by U.S. persons to foreign corporations	1986-23 I.R.B. 33	July 15, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] See footnote at end of list.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

Finding List of Current Action on Previously Published Rulings[1]

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*Denotes entry since last publication

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78-1
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68-257
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68-590
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68-627
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71-446
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86-74, 1986-21 I.R.B. **4**

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[1] See footnote at end of list.

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86-76, 1986-21 I.R.B. **5**

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86-45, 1986-13 I.R.B. **36**

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86-30, 1986-8 I.R.B. **24**

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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TD 4.12/2:

NOTICES TO AIRMEN
CONTENT CRITERIA
Revised 1985

ALL AIRPORTS

TABLE 1

Information Category	Content Criteria
Airports	Abandonments (If currently listed in Airport/Facility Directory), Openings, Closings.
Runways	Openings, Closings, Commissionings, Permanent Closures.

NOTAM D AIRPORTS

TABLE 2

Information Category	Content Criteria
Airport Operating Restriction	CFR, ACR, etc.
Approach Light Systems	Commissionings, Changes, Decommissionings, Outages (with Effective Dates), Pilot Control (Commissionings, Decommissionings, Outages (with Effective Dates)).
Control Zones	Hours of Operation (in Local Time).
Displaced Thresholds	Implementation and Changes.
Runways	Ident Changes, Length, Width, Surface Composition Changes.
Runway Light Systems	Commissionings, Changes, Outages (with Effective Dates), Pilot Control (Commissionings, Decommissionings, Outages (with Effective Dates)).

NAVAIDS, COMMUNICATIONS, OTHER SERVICES

TABLE 3

Information Category	Content Criteria
Navigational Facilities	Commissionings (including Ident and Frequency), Decommissionings (including Ident and Frequency), Frequency Changes, Changes in Monitoring Facility and/or Status, Restrictions, Outages (with Effective Dates).
Air Traffic Control Towers, Approach Controls	Commissionings (including Frequencies), Hours of Operation, Decommissionings.
Flight Service Stations	Commissionings, Decommissionings, Hours of Operation; Commissionings, Decommissionings of RCO; Changes in Monitoring Status of RCO; Outages of RCO (with Effective Dates).
Weather	AWOS (System and Frequency).

FOREWORD

The primary references for changes to the National Airspace System (NAS) are Aeronautical Charts and Airport/Facility Directories (A/FD) published for the affected area(s). Ideally, most changes to the NAS that meet NOTAM criteria are known sufficiently in advance to allow publication in these publications. When this cannot be done, changes are carried in the Notices to Airman Class II publication, or as a last resort, on the Service A telecommunications system as a NOTAM D item.

NOTAM D information printed in this publication will not be included on the Service A system and will not be provided during pilot briefings unless specifically requested by the pilot.

National Flight Data Center (FDC) NOTAMs primarily reflect changes to Standard Instrument Approach Procedures (SIAPs), Flight Restrictions, and aeronautical chart revisions. The last FDC NOTAM included in this issue is indicated by number and date above. This information insures that subsequent FDC NOTAMs, issued after the cutoff date, can be identified.

The Class II publication contains information of a temporary nature, which is expected to remain for an extended period. This temporary information is carried until it expires or is cancelled. Data of a permanent nature is sometimes carried in the Class II publication as an interim step prior to publication on the appropriate charts or in the A/FD.

The Class II publication is issued every 14 days. The A/FD is published every 56 days. Data in the Class II publication that is current on the effective date of the next A/FD will be transferred to the A/FD and removed from the Class II publication.

Facilities are responsible for forwarding data to the National Flight Data Center (NFDC). Data, still current for the next available Class II publication date, will be published.

This publication is divided into two sections:

1. Section One contains information divided into four categories:

a. GENERAL

b. AIRWAYS

c. FLIGHT RESTRICTIONS

d. AIRPORTS / FACILITIES / PROCEDURAL NOTAMS

The first subsection is listed in descending FDC NOTAM numerical order. The second and third subsections are listed by state. The fourth subsection is ordered by state, city, and airport name.

2. The second section contains special notices that are too long or that concern a wide or unspecified geographical area (which may overlap several states) and are not suitable for inclusion in the first section.

The content of these notices vary widely and are included because of their significant impact on flight safety.

NOTES

1. All times are indicated as UTC or local. During periods of Daylight Savings Time, effective hours in local time will be one hour earlier than shown. All states observe Daylight Savings Time except Arizona, that portion of Indiana in the Eastern Time Zone, Puerto Rico, and the Virgin Islands.

2. (|) Vertical line items indicate new information.

FDC NOTAM LEGEND

Code	Explanation
5/103	Accountability number assigned to the message originator.
FI/T	Flight information of a temporary nature.
FI/P	Flight information of a permanent nature.

NOTICES TO AIRMEN

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31 JUL 86	16 JUL 86	26 JUN 86
14 AUG 86	30 JUL 86	10 JUL 86
28 AUG 86	13 AUG 86	24 JUL 86
11 SEP 86	27 AUG 86	07 AUG 86
25 SEP 86	10 SEP 86	21 AUG 86
09 OCT 86	24 SEP 86	04 SEP 86
23 OCT 86	08 OCT 86	18 SEP 86
06 NOV 86	22 OCT 86	02 OCT 86
20 NOV 86	05 NOV 86	16 OCT 86
04 DEC 86	19 NOV 86	30 OCT 86
18 DEC 86	03 DEC 86	13 NOV 86
01 JAN 87	17 DEC 86	27 NOV 86
15 JAN 87	31 DEC 86	11 DEC 86
29 JAN 87	14 JAN 87	25 DEC 86

(A) Information for Section 1 should be submitted to the National Flight Data Center (ATO-250).
(B) Camera-ready copy for Section 2 should be submitted to ATO-200.

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NOTICES TO AIRMEN
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SECTION TWO

1. SPECIAL NOTICES .... S—1

ABBREVIATIONS

The following abbreviations are those most commonly used within this publication. Other abbreviations may be found in the Contraction Handbook, 7340.1.

Note: An "s" may be added for plural. Abbreviations used in FDC NOTAMs are italicized.

A

/	and
AAS	Airport Advisory Service
A/C	Approach Control
acft	aircraft
ACR	Air Carrier
ADF	Automatic Direction Finder
AER	Approach End Runway
AGL	above ground level
AIM	Airmen's Information Manual
ALS	Approach light system
ALSF-1	Standard 2400' High-intensity Approach Lighting System with Sequenced Flashers, Category I Configuration
ALSF-2	Standard 2400' High-intensity Approach Lighting System with Sequenced Flashers, Category II Configuration
alt	altitude
altm	altimeter
altn	alternate
ALSTG	altimeter setting
amdt	amendment
apch	approach
apchg	approaching
aprx	approximate
arpt	airport
arr	arrive or arrival
ARSR	Air Route Surveillance Radar
ARTCC	Air Route Traffic Control Center
ASDE	airport surface detection equipment
ASR	Arpt Surveillance Radar
ATC	air traffic control
ATCT	air traffic control tower
ATIS	Automatic Terminal Information Service
avbl	available
awy	airway

B

BC	back course
bcn	beacon
bcst	broadcast
bldg	building
brg	bearing
btn	between
byd	beyond

C

cat	category
CFR	crash fire rescue
clnc	clearance
clsd	closed
cmsnd	commissioned
cntr	center
cntrln	centerline
Comlo	Compass locator
const	construction
cpty	capacity
crs	course
ctc	contact
CTLZ	Control Zone

D

dalgt	daylight
dcmsnd	decommissioned
degs	degrees
dep	depart, departure
DF	direction finder
DH	decision height
DME	UHF standard TACAN compatible distance measuring equipment
dsplcd	displaced
dstc	distance
durg	during
DVFR	Defense Visual Flight Rule

E

E	east
EFAS	Enroute Flight Advisory Service
elev	elevation
emerg	emergency
equip	equipment
excp	except

F

FAF	final approach fix
FAR	Federal Aviation Regulation
FDC	Flight Data Center
FI/P	flight information (permanent)
FI/T	flight information (temporary)
FL	Flight Level
FM	from
freq	frequency
FSS	Flight Service Station
ft	feet/foot

G

govt	government
GS	glide slope
GWT	gross weight

H

HAA	height above airport
HAT	height above touchdown
HIRL	High intensity Runway Lights
hol	holiday
hwy	highway

I

IAF	initial approach fix
IAP	initial approach procedure
ident	identification
IF	intermediate fix
IFR	Instrument Flight Rules
IFSS	International Flight Service Station
ILS	instrument landing system
info	information
inop	inoperative
int	intersection
intl	International
intst	intensity
ISMLS	Interim Standard Microwave Landing System

J

J-bar	jet runway barrier

K

kHz	kilohertz

L

L	left (used only to designate rwys) eg. rwy 12L
lat	latitude
lb	pounds (weight)
lctd	located
LDA	Localizer type directional aid
LDIN	Lead-in Lighting System
lgtd	lighted
LMM	compass locator at middle marker ILS
lndg	landing
loc	localizer
LOM	compass locator at outer marker ILS
long	longitude

M

MAA	maximum authorized altitude
mag	magnetic
maint	maintain, maintenance
MALS	Medium Intensity Approach Light System
MALSR	Medium Intensity Approach Light System with Runway Alignment Indicator Lights
MAP	missed approach point
max	maximum
MCA	minimum crossing altitude
MDA	minimum descent altiturle
MEA	minimum enroute IFR altitude
MHz	megahertz
min	minimum or minute
MIRL	Medium Intensity Runway Edge Lights
MLS	Microwave Landing System
MM	middle marker ILS
MOCA	minimum obstruction clearance altitude
MRA	minimum reception altitude
MSA	minimum safe altitude
MSL	mean sea level
muni	municipal

N

N	north
NA	not authorized
natl	national
navaid	navigational aid
NDB	Non-directional Radio Beacon
NM	nautical mile(s)
NOPT	no procedure turn required
Nr	number

O

obstn	obstruction
ODALS	Omnidirectional Approach Lighting System
OM	outer marker ILS
oper	operate
opn	operation
orig	original
OTS	Out of Service
ovrn	overrun

P

PAR	Precision Apch Radar
pat	pattern
permly	permanently
PPR	Prior Permission Required
proc	procedure

Q

quad	quadrant

R

R	right (used only to designate rwys) eg. rwy 19R
RAPCON	radar approach control (USAF)
RCAG	Remote Center air/ground
RCLS	Runway Centerline Lights System
RCO	Remote Communications Outlet
rcv	receive
rcvg	receiving
REIL	Runway End Identifier Lights
req	request
RNAV	Area Navigation
RRP	Runway Reference Point
rstrd	restricted
RTS	returned to service
RVR	runway visual range
RVRM	Runway Visual Range Midpoint
RVRT	Runway Visual Range Touchdown
RVRR	Runway Visual Range Rollout
RVV	runway visibility values
rwy	Runway

S

S	south/snow
SDF	Simplified Directional Facility
sec	second
sfc	surface
SFL	Sequenced Flashing Lights
SI	straight-in approach
SM	statute mile(s)
SR	sunrise
SS	sunset
SSAFL	Simplified Short Approach Lighting System with Sequenced Flashers
SSALS	Simplified Short Approach Lighting System
SSALR	Simplified Short Approach Lighting System with Runway Alignment Indicator Lights
STOL	Short take-off & landing runway
svc	service

T

T	true (after a bearing)
TAC	Terminal Area Chart
TACAN	UHF navigational facility—omnidirectional course and distance information
TCA	Terminal Control Area
TCH	Threshold Crossing Height
tfc	traffic
thr	threshold
thru	through
tkof	take-off
tmprly	temporarily
tmpry	temporary
TPA	Traffic Pattern Altitude
TRACON	Terminal Radar approach control
trml	terminal
TRSA	Terminal Radar Service Area
tsnt	transient
TWEB	transcribed weather bcst
twr	tower
twy	taxiway

U

UHF	Ultra high frequency
unavbl	unavailable
unlgtd	unlighted
unmon	unmonitored
unusbl	unusable

V

VASI	Visual Approach Slope Indicator
VDP	visual descent point
VFR	visual flight rules
VHF	Very high frequency
vis	visibility
VOR	VHF Omni-Directional Radio Range
VORTAC	Combined VOR and TACAN System
VOT	a VOR Receiver testing facility
vsby	visibility

W

W	west
wea	weather
wkday	weekday
wkend	weekend
wp	waypoint
wt	weight

Z

Z	Coordinated Universal Time (UTC)

GENERAL

FDC 6/2036 FI/P CORRECT U.S. SECTIONAL CHART FOR SEATTLE. 31ST EDITION, DTD 3 JUL 86. CHANGE BAKER FSS /BKE/FREQ 122.4 TO FREQ 122.2.

FDC 6/1601 FI/P HI CORRECT U.S. SECTIONAL CHART HAWAIIAN ISLANDS 34TH EDITION DATED 5 JUN 86.. CHANGE BRADSHAW NDB IDENT /BSF/FREQ 349 TO FREQ 339.

FDC 6/995 U.S. CUSTOMS REGULATORY CHANGES. AIRCRAFT PENETRATING THE INNER ADIZ FM ANYWHERE IN THE WESTERN HEMISPHERE SOUTH OF THE U.S. MEXICAN BORDER, SOUTH OF 33 DEG NORTH LATITUDE ON THE PACIFIC COAST, SOUTH OF 30 DEGREES NORTH LATITUDE ON THE ATLANTIC COAST, OR SOUTH OF THE INNER ADIZ ON THE GULF COAST, MUST PROVIDE U.S. CUSTOMS AT LEAST ONE HOUR ADVANCE NOTICE OF PENETRATION OF U.S. AIRSPACE, EFFECTIVE APRIL 30. THIS REQUIREMENT WILL BE EXTENDED TO AIRCRAFT THAT HAVE NOT LANDED IN A FOREIGN PLACE AND AIRCRAFT FROM PUERTO RICO THAT ARE NOT FLYING UNDER IFR FLIGHT RULES. FILING A FLIGHT PLAN WITH THE NOTATION 'ADCUS' WITH THE U.S. FAA AT LEAST ONE HOUR IN ADVANCE OF PENETRATION OF THE ADIZ WILL SATISFY THIS REQUIREMENT. CONTRACTING U.S. CUSTOMS AT 305-536-6591, MIAMI, FL, OR 714-351-6674, RIVERSIDE, CA, AT LEAST ONE HOUR IN ADVANCE WILL ALSO MEET THE REQUIREMENT. LANDING AND INSPECTION REQUIREMENTS FOR AIRCRAFT ARRIVING FROM FOREIGN PLACES REMAIN UNCHANGED.

FDC 6/201 FI/P CORRECT U.S. GOVT WORLD AERONAUTICAL CHART CG21, 16TH EDITION DTD OCT 24, 1985. CHANGED HARRIS VORTAC /HRS/ FREQ 111.6 CHANNEL 053 TO FREQ 109.8 CHANNEL 035.

FDC 5/2508 AUTOMATED VOICE AIRPORT RESERVATION SYSTEM../AVARS/. IN ORDER TO IMPROVE THE AVARS CAPACITY THE FAA HAS INSTALLED TWO ADDITIONAL NON-TOLL FREE NUMBERS..617-275-4837/8. EFFECTIVE NOVEMBER 1 1985 TWO ADDITIONAL TOLL FREE LINES WILL BE AVAILABLE TO BE PART OF 1-800-FAA-1212 NUMBER. FAA PLANS TO CONTINUE THE DUAL /ARO/SYSTEM USING THE AUTOMATED SYSTEM ON 1-800-FAA-1212 AND THE MANUAL ARO SYSTEM WITH NEW YORK 718-632-7806/ CHICAGO 312-263-2575 AND WASHINGTON DC 202-426-9347 UNTIL FURTHER NOTICE. IN AREAS WHERE TOUCH TONE PHONE SYSTEMS ARE NOT AVAILABLE USERS MAY EITHER CONTACT THE NEAREST FAA FLIGHT SERVICE STATION OR THE /ARO/ AT THE NUMBERS LISTED ABOVE AND REQUEST A RESERVATION. USERS DEPARTING A TRANS-ATLANTIC AIRPORT FOR ARRIVAL TO A HIGH DENSITY AIRPORT SHOULD CONTINUE TO USE THE PROCEDURES OUTLINED IN ADVISORY CIRCULAR AC 90-43F PARA 5 DATED APRIL 22 1985 WHICH STATES CONTACT THE NEAREST FLIGHT SERVICE STATION.

FDC 5/594 AIRPORT RESERVATION OFFICE/ARO/ OPERATIONS... EFF APR 1, 1985...THE FOLLOWING GUIDELINES SHALL BE IN EFFECT... /ARO/WILL ACCEPT RSVNS FOR WASHINGTON NATIONAL AIRPORT /DCA, JOHN F. KENNEDY INTL ARPT /JFK, LA GUARDIA ARPT/LGA, AND CHICAGO O HARE INTL ARPT /ORD BEGINNING 48 HRS PRIOR TO THE PROPOSED TIME OF OPERATION AT THE AFFECTED ARPT. E.G REQ FOR 11 A.M. OPERATION ON THURSDAY WILL BE ACCEPTED STARTING 11 A.M. ON THE PRECEDING TUESDAY. AN EXCEPTION TO THE 48 HR LIMITATION IS MADE FOR WEEKENDS TO RECOGNIZE NORMAL BUSINESS HOURS. A RSVN REQ FOR AN IFR OPERATION ON MONDAY WILL BE ACCEPTED ON THE PREVIOUS THURSDAY STARTING AT THE PROPOSED HR OF OPERATION. REQUESTS FOR IFR OPERATION ON TUESDAY WILL BE ACCEPTED ON THE PREVIOUS FRIDAY STARTING AT THE PROPOSED HR OF OPERATION. E.G. REQ FOR 11 A.M. RSVN ON TUESDAY WOULD BE ACCEPTED BEGINNING 11 A.M. ON FRIDAY. IF THE PREVIOUS FRIDAY IS AN OBSERVED HOLIDAY THE PROCEDURE WILL BE IN EFFECT ON THURSDAY. A MAXIMUM OF TWO RSVNS PER PHONE CALL WILL BE ACCEPTED. E.G. A PILOT MAY REQ A RSVN

FOR ARRIVAL AND DEPARTURE DURING THE SAME PHONE CALL PROVIDING BOTH FALL ON THE SAME CALENDAR DAY. E.G. A RSVN REQ FOR 11 A.M. ARRIVAL ON FRIDAY AND 4 P.M. DEPARTURE ON THE SAME DAY MAY BE MADE BEGINNING AT 11 A.M. ON WEDNESDAY.

AIRWAYS

Alabama

FDC 6/2128 FI/T /AWYS/AL. V20/V56 TUSKEGEE AL VORTAC /TGE/ TO MONTGOMERY AL VORTAC /MGM/USE MGM R-061 MEA/MRA 2000.

Arizona

FDC 6/2959 FI/P AWYS AZ. CHART CORRECTION ENROUTE H2 PANEL G. RADIAL 147 SRP VORTAC TO TOTEC AZ INT SHOULD READ J11 IN LIEU OF J50. DELETE REFERENCE TO J4 FROM TOTEC AZ INT TO SSO VORTAC.

Alaska

FDC 6/2650 FI/T /AWYS/ AK. V531 FROM BERJO DME FIX TO POINT HOPE/PHO/NDB NA.

FDC 6/1370 FI/T /AWY/ AK. G8 NABESNA /AES/NDB TO GLENALLEN /GLA/NDB AIRWAY NA WHEN /ORT/ NORTHWAY FSS CLSD.

Florida

FDC 6/594 FI/T /AWYS/FL. V579 SRQ-VIOLA INT MEA 3000.

Florida, Georgia

FDC 6/2503 FI/T /AWY/ FL/GA..V267 MATEO FL INT TO BAXLY GA INT MOCA 2100..V37 JAX VORTAC TO SSI VORTAC MEA 2100..V1 JAX VORTAC TO STARY GA INT MOCA 2100..V51 ASTOR FL INT TO JAX VORTAC MEA 2100.

FDC 6/2051 FI/T /AWY/ FL/GA. J89 UNUSABLE FROM LAKELAND FL VORTAC TO PAULL GA INT.

Georgia, South Carolina

FDC 6/2100 FI/T /AWYS/ GA/SC..V185 V417 MILEN INT GA TO AGS VORTAC UNUSBL. V155 AGS VORTAC TO WIDER INT SC, V56 AGS VORTAC TO SAMMI INT SC AND V18 AGS VORTAC TO NORMS INT SC UNUSABLE BLO 13000.

Illinois

FDC 6/2676 FI/T /AWY/ V7-V97-V422 MEA 2100 FROM CGT VORTAC TO NILES IL INT.

Iowa

FDC 6/131 FI/T /AWY/IA. V-159 BETWEEN SUX VORTAC AND HURLY INT. MEA 4500 FT MSL.

Kansas

FDC 6/2126 FI/T /AWYS/ KS. V4 HILL CITY, KS VORTAC TO WESAL INT, KS. RAISE MOCA TO 4000 FEET.

Louisiana

FDC 6/2527 FI/T /AWY/LA. V222 MAXON INT LA TO WRACK INT LA MOCA 1600. V566 MUSHE INT LA TO WRACK INT LA MOCA 1600.

FDC 6/1452 FI/T /AWY/ LA. V566 FISTY INT TO WRACK INT MEA 1600. V222 MOGAN INT TO LESTE INT MEA 1600.

Maine, Massachusetts, New Hampshire

FDC 6/2570 FI/T /AWY/ME/MA V139/V451. SEEDY INT TO TONNI INT MEA 5000.

Maine, New Hampshire

FDC 6/1879 FI/T /AWY/V-451 SEEDY INT NH TO BRUNSWICK VORTAC ME NA.

Massachusetts, New Hampshire

FDC 6/2568 FI/T /AWY/ NH/MA V205. PSM VOR TO SCUPP INT MRA SILVE INT 5000.

FDC 6/2569 FI/T /AWY/MA V205/V431. BOSTON VORTAC TO WETTR INT. MRA WIMPY INT AND WETTR INT 5000.

Massachusetts, New York

FDC 6/2228 FI/T /AWY//MA/NY. J97 BOS VORTAC, MA TO PLB VORTAC, NY, RUMMY INT, NH, NA.

Massachusetts, Rhode Island

FDC 6/2567 FI/T /AWY/ RI/MA V139-451. PVD VORTAC TO TONNI INT. MRA TONNI INT 5000.

Michigan

FDC 6/2740 FI/T /AWYS/MI..DEXER INT, 14 NM WEST OF SVM VORTAC ON V116- V221. DME OR RADAR REQUIRED.

Missouri

FDC 6/441 FI/T /AWYS/, MO, V50, ST JOSEPH, MO VORTAC TO KIRKSVILLE, MO. VORTAC MOCA, 2400 FEET.

New Hampshire, New York

FDC 6/2229 FI/T /AWY/ NY/NH. J49 FROM ALB VORTAC, NY TO SQUAM DME FIX, NH, NA. RUMMY INT, NH, NA.

New Jersey

FDC 6/1561 FI/T /AWY/NJ. V433 KILMA INT NJ AND AMBOY INT NJ MRA 3000.

FDC 6/1559 FI/T /AWY/NJ. SELFF INT AND SCOPE INT. MRA 4000.

New Jersey, New York

FDC 6/1560 FI/T /AWY/NJ/NY. V157 FROM COL VORTAC NJ TO NYACK INT NY, MEA 4000.

FDC 5/1343 FI/T /AWYS/ NJ/NY V213 SAX VORTAC NJ TO ALB VORTAC NY NA.

New York

FDC 6/3135 FI/T AWYS NY V164 CANADIAN BORDER TO BUFFALO NY VORTAC MEA 2800.

FDC 6/3134 FI/T AWY NY V36 ISTON INT NY TO BUFFALO NY VORTAC MEA 2800.

New Mexico

FDC 5/1098 FI/T /AWY/NM/WHEN DEMING, NEW MEXICO FSS NOT IN OPERATION, THE FOLLOWING APPLIES..V94 DMN VORTAC TO CRATT INT MOCA 9000. V66 DUG VORTAC TO ANIMA INT NA, V202 SVC VORTAC TO TCS VORTAC MEA 12000, V16 V66 CUS VORTAC TO CIE VORTAC MEA 11000.

North Carolina

FDC 6/3079 FI/T AWY/NC, V409 FROM LOCAS, NC INT TO MERIL, NC INT RADAR REQUIRED.

FDC 6/934 FI/T /AWYS/NC. V266 FROM SUNNS NC. FIX TO ELIZABETH CITY NC. /ECG/VOR/DME MEA 4000 DELETE MOCA. V266 FROM ELIZABETHS CITY NC. /ECG/VOR/DME TO WRIGHT BROTHERS NC. /RBX/ VOR/DME MEA 4000 DELETE MOCA/ V310 FROM TAR RIVER NC. /TYI/VORTAC TO ELIZABETH CITY /ECG/ VOR/DME MEA 4000 DELETE MOCA. V472 FROM ELIZABETH CITY NC. /ECG/VOR/DME TO BERTI NC. FIX MEA 4000 DELETE MOCA. AR8 FROM WEEKSVILLE NC. /EKV/NDB TO BACUS NC. FIX MEA 4000.

FDC 6/128 FI/T /AWY/NC. V409 FROM LOCAS NC FIX NE TO 40NM SW OF RALEIGH/DURHAM NC VORTAC /RDU/A NAVIGATION GAP EXISTS. USE RADAR VECTORING THRU THIS AREA.

North Carolina, South Carolina, Virginia

FDC 6/1450 FI/T/AWYS/ VA/NC/SC. J37 GORDENSVILLE VA. /GVE/VORTAC TO SPARTANSBURG SC. /SPA/ VORTAC MEA 37000.

Oklahoma

FDC 6/1228 FI/T /AWYS/OK/ V161 TUL VORTAC TO NOVEL INT MEA 3000.

South Carolina

FDC 6/1990 FI/T /AWYS SC. CHATT INT SC ..NORMS INT SC..SALLY INT SC..AND ERNIE INT SC..DME ONLY BELOW 13000.

Texas

FDC 6/2998 FI/T AWYS/TX. V-556 VUH VORTAC TO KEEDS INT, MEA 3000.

FDC 6/2904 FI/T /AWYS/TX V-17 BETWEEN BPR VORTAC AND DUC VORTAC MEA 3000.

FDC 6/2425 FI/T AWYS TX. V17 BRO VORTAC TO HRL VORTAC MEA 2000.

FDC 6/2349 FI/P CHART CORRECTION AWY TX/EL PASO, TX SECTIONAL 37TH EDITION DTD AUG 28, 1986. CHANGE V280 FROM ELP VORTAC TX RADIAL 065 TO RADIAL 058.

FDC 6/969 FI/T /AWYS/ TX. WHEN COLLEGE STATION FSS CLSD THE FOLLOWING APPLIES..V212 WEMAR INT TO IDU VORTAC NA. V558 PODDS INT TO IDU VORTAC NA. V66/77/222 IDU VORTAC TO SEALY INT NA. V306 COUTH INT TO TNV VORTAC MEA 2500. V306 TNV VORTAC TO DOGLEG NA. V548 BARBA INT TO CLL VORTAC NA. V548 CLL VORTAC TO SEALY INT NA. V571 TEAKY INT TO LOA VORTAC NA. V198/556 WEMAR INT TO ELA VOR/DME MEA 2500. V68/222 CRAYS INT TO IDU VORTAC MEA 2500. V198/558 ELA VOR/DME TO BLUMS INT MEA 2500. V222 SEALY INT TO IAH VORTAC NA. V68/76/548 SEALY INT TO HUB VORTAC NA.

FDC 5/1156 FI/T /AWY/TX. WHEN WINK TX FSS NOT IN OPERATION THE FOLLOWING APPLIES: V68 HOB VORTAC MAF VORTAC MEA 5200. V94/546 INK VORTAC TO MAF VORTAC MEA 5500, V222 COP TO FST VORTAC MEA 8000,

AIRWAYS

V198 HUP VORTAC TO FST VORTAC NA, V16 INK VORTAC TO BGS VORTAC MEA 6300.

Virginia

FDC 6/2843 FI/T /AWY/ /VA/ V1/V139. DELETE MOCA ORF VORTAC TO CCV VORTAC.

FDC 5/2570 FI/T /AWY/ VA. V286 DME OR RADAR REQUIRED TO IDENTIFY OKFEI INT.

AIRWAYS

FDC 5/2569 FI/T /AWY/ VA. V128 DME OR RADAR REQUIRED TO IDENTIFY LURAY INT.

FDC 6/2332 FI/T /AWY/ VA V286 FROM LVL VORTAC VA TO MAZON INT VA NA.

FLIGHT RESTRICTIONS

ONLY NOTICES OF SIGNIFICANT DURATION ARE LISTED. (7/85)

AIRPORTS / FACILITIES / PROCEDURAL NOTAMS

ALABAMA

ANNISTON

Anniston-Calhoun County Anniston

FDC 6/552 /ANB/ FI/T ANNISTON-CALHOUN COUNTY ANNISTON AL. LOC RWY 5 AMDT 8. MSA FROM TDG VORTAC 4000.

AUBURN

Auburn-Opelika Robert G. Pitts

FDC 6/2954 /AUO/FI/T AUBURN-OPELIKA ROBERT G. PITTS. AUBURN AL. LOC RWY 36 AMDT 1. MSA FROM AU LOM 2800. VOR RWY 28 AMDT 7. MSA FROM CSG VORTAC 3500. VOR/DME-A AMDT 5. MSA FROM TGE VORTAC 2800.

FDC 6/1355 /AUO/ FI/T AUBURN-OPELIKA ROBERT G. PITTS, AUBURN, AL. RNAV RWY 36 AMDT 2, MISSED APCH.CLIMB TO 2800 TO RUMAN WPT AND HOLD N, LT, 178 INBOUND.

BESSEMER

Bessemer

FDC 6/3001/2A3/FI/P BESSEMER, BESSEMER, AL. VOR RWY 5 AMDT 4. CORRECT US GOVT CHART CHANGE NOTICE, AL-6260 PAGE B DATED 23 OCT 1986. CHART HOLDING AT DABRO INT, W, RT, 075 INBOUND.

BREWTON

Brewton Muni

FDC 6/2789 /12J/ FI/T BREWTON MUNI, BREWTON, AL. VOR RWY 30 AMDT 4, DME RQRD.

ENTERPRISE

Enterprise Muni

RWY 23 VASI OTS INDEFLY. (10/86)

EVERGREEN

Evergreen

FDC 6/2437 /39J/ FI/T EVERGREEN, EVERGREEN, AL. VOR/DME RWY 9 AMDT 1 PROC NA.

FAIRHOPE

Fairhope Muni

RWY 01/19 NOW 6600 FT BY 75 FT. (10/86)

RWYS 01 & 19 VASI DCMSND. (11/86)

HUNTSVILLE

Huntsville-Madison Co, Carl T. Jones Fld

ILS RWY 18R (I-HSV) AND RWY 36L (I-ELL) RTS. (11/86)

JASPER

Walker County-Bevill Field

FDC 5/2949 /L02/ FI/T WALKER COUNTY-BEVILL FIELD, JASPER, AL. VOR/DME-A AMDT 1. MSA FROM VUZ VORTAC 3700.

MOBILE

Bates Field

ARPT NOW OPEN. (11/86)

PELL CITY

St Clair County

RWY 02/20 LIRL CHANGED TO MIRL. (10/86)

TROY

Troy Muni

FDC 6/1490 /TOI/ FI/T TROY MUNI, TROY, AL. ILS RWY 7 AMDT 5. PROC NA.

TUSCALOOSA

Tuscaloosa Muni

FDC 6/2934 /TCL/FI/P TUSCALOOSA MUNI, TUSCALOOSA, AL. NDB RWY 4 AMDT 7; ILS RWY 4 AMDT 9. TRML ROUTE OKW VORTAC TO TC LOM 256 DEG. VOR RWY 22 AMDT 10, TRML ROUTE OKW VORTAC /IAF/TO HOLTY INT/NOPT/301. THIS IS NDB RWY 4 AMDT 8; ILS RWY 4 AMDT 10; VOR RWY 22 AMDT 11.

TUSKEGEE

Moton Field

FDC 6/2953 /06A/ FI/T MOTON FIELD..TUSKEGEE AL. VOR-A AMDT 2. MSA FROM TGE VORTAC 2800.

ALASKA

AMBLER

Ambler

FDC 2/684 /Z60/ FI/T AMBLER, AMBLER, AK NDB RWY 36 ORIG ALTN MINS NA.

ANIAK

Aniak

FDC 5/2831 /ANI/ FI/T ANIAK, ANIAK, AK. NDB RWY 28 AMDT 8, NDB/DME RWY 28 AMDT 1, ILS/DME RWY 10 AMDT 4. ADD NOTE: WHEN ANIAK ALTIMETER SETTING NOT AVAILABLE PROC NA.

FDC 5/2500 /ANI/ FI/T ANIAK ANIAK AK. NDB RWY 28 AMDT 8..NDB/DME RWY 28 AMDT 1 AND ILS/DME RWY 10 AMDT 4. CHG PCL NOTE TO ACTVT MALSR RWY 10..HIRL RWY 10/28 AND VASI RWY 28 CTAF.

BIG LAKE

Big Lake

FDC 6/2965 /BIG/ FI/P BIG LAKE, BIG LAKE, AK. VOR RWY 6 AMDT 4 DELETE BGQ 3.5 DME STEPDOWN FIX. DELETE DME MINIMUMS. THIS IS VOR RWY 6 AMDT 5.

COLD BAY

Cold Bay

FDC 4/713 /CDB/ FI/T COLD BAY, COLD BAY, AK. NDB RWY 14 AMDT 9, ILS RWY 14 AMDT 12, LOC/DME BC RWY 32 AMDT 4, VOR RWY 14 AMDT 10, VORTAC-A AMDT 3, CAT D CIRCLING NA WEST OF RWY 14-32.

DEADHORSE

Deadhorse

FDC 6/1579 /SCC/ FI/T DEADHORSE, DEADHORSE, AK. NDB-A AMDT 1..ILS/DME RWY 4 AMDT 5.. LOC/DME RWY 22 AMDT 5..VOR RWY 4 AMDT 2.. VOR/DME RWY 4 AMDT 1..CAT A CIRCLING MDA 520/HAA 463.

DELTA JUNCTION FT GREELY

Allen AAF

FDC 6/2917 /BIG/ FI/T ALLEN AAF, DELTA JUNCTION FT GREELY, AK VOR RWY 18 AMDT 6..SI MDA 1720 HAT 475 ALL CATS. VIS 1 1/4 CAT C, 1 1/2 CAT D. CIRCLING MDA 1720 HAA 443 CAT A.

DILLINGHAM

Dillingham

FDC 6/3018 /DLG/FI/T DILLINGHAM/DILLINGHAM, AK. LOC/DME RWY 19 AMDT 2..VOR/DME RWY 19 AMDT 4..STRAIGHT-IN VIS 1 1/4 CAT D.

FAIRBANKS

Fairbanks Intl

FDC 6/3035 /FAI/FI/P FAIRBANKS INTERNATIONAL, FAIRBANKS, AK. CORRECT U.S. GOVT CHART, ALASKA TERMINAL, PAGE XV DATED 23 OCTOBER 1986. IFR TKOF MINS AND DEP PROCS ADD TKOF MINS: RWY 19L/R ADD IL/R STANDARD. IFR DEP PROC: W AND N BOUND (190 DEG CLKWS 020 DEG), RWY 1L/R TURN RIGHT, CLIMB ON HEADING 020 DEG TO 2000, RWY 19L/R CLIMB RWY HEADING TO 2000. THENCE CLIMB VIA ASSIGNED ROUTE.

FDC 3/1716 /FAI/ FI/T FAIRBANKS INTL FAIRBANKS AK. ILS RWY 19R AMDT 19 HI-ILS RWY 19R DSTC MM TO THR 0.5 NM ALT A MM 634 FT DELETE AI COMPASS LOCATOR AT MM /FREQ 215 KHZ/. NDB RWY 19R AMDT 16 DELETE COMPASS LOCATOR AT MM.

FT GREELY

Allen AAF Delta Junction

FDC 6/2966 /BIG/FI/T ALLEN AAF DELTA JUNCTION/FT GREELY AK. NDB-A AMDT 2. CIRCLING MDA 1720/HAA 443 ALL CATS. VOR/DME OR TACAN RWY 18 AMDT 1 SI MDA 1660/HAT 415 ALL CATS. VIS 1 1/4 CATS C/D. CIRCLING MDA 1720/HAA 443 CAT A.

FORT YUKON

Fort Yukon

FDC 6/2883 /FYU/ FI/T FORT YUKON, FORT YUKON, AK. NDB RWY 21 AMDT 6..VOR RWY 21 AMDT 3. SI VSBY 1 1/4 CAT C AND 1 1/2 CAT D. VOR RWY 3 AMDT 3. SI VSBY CAT D 1 1/4. VOR/DME OR TACAN RWY 21 ORIG. SI VSBY 1 1/4 CAT C/D.

FDC 5/2832 /FYU/ FI/T FORT YUKON, FORT YUKON, AK. NDB RWY 21 AMDT 6, VOR RWY 3 AMDT 3, VOR RWY 21 AMDT 3, VOR/DME OR TACAN RWY 3, VOR/DME OR TACAN RWY 21 ORIG. ADD NOTE: WHEN FORT YUKON ALTIMETER SETTING NOT AVAILABLE PROC NA.

GALENA

Galena

FDC 6/3017 /GAL/FI/T GALENA, GALENA, AK. VOR RWY 25 AMDT 9..HI-VOR/DME OR TACAN RWY 25 AMDT 1..STRAIGHT-IN VIS 1 1/4 CATS D/E.

FDC 6/1206 /GAL/ FI/T GALENA/GALENA/AK. NDB-A AMDT 14. VOR RWY 25 AMDT 8. VOR/DME OR TACAN RWY 7 AMDT 5. ALTERNATE NA WHEN MCGRATH FSS CLOSED.

JUNEAU

Juneau Intl

FDC 4/2183 /JNU/ FI/T JUNEAU INTL, JUNEAU, AK. LDA-1 RWY 8 AMDT 6 TRML ROUTE SSR VORTAC TO LYNNS INT 001 DEGS VICE 360 DEGS.

MC GRATH

Mc Grath

FDC 6/1207 /MCG/ FI/T MCGRATH/MCGRATH/AK. NDB-B ORIG. LOC/DME RWY 16 AMDT 1. VOR-A AMDT 8. VORTAC RWY 16 AMDT 5. ALTERNATE NA WHEN MCGRATH FSS CLOSED.

MIDDLETON ISLAND

Middleton Island

FDC 5/2833 /MDO/ FI/T MIDDLETON ISLAND, MIDDLETON ISLAND, AK. NDB-A AMDT 6, VOR RWY 1 AMDT 1, VOR/DME RWY 19 AMDT 4: ADD NOTE: WHEN MIDDLETON ISLAND ALTIMETER SETTING NOT AVAILABLE PROC NA.

MINCHUMINA

Minchumina

FDC 6/1208 /MHM/ FI/T MINCHUMINA/MINCHUMINA/AK. NDB RWY 2 AMDT 2. ALTERNATE NA WHEN MCGRATH FSS CLOSED.

NOME

Nome

FDC 6/3092 /OME/FI/T NOME, NOME, AK. LOC/DME BC RWY 9 AMDT 1. PROC NA.

FDC 6/3019 /OME/FI/T NOME, NOME, AK. NDB RWY 27 AMDT 3..SI VIS 1 1/4 CAT C, 1 1/2 CAT D. VOR RWY 27 AMDT 11..SI VIS 1 1/2, DME VIS CAT C 1 1/4, VOR/DME RWY 9 AMDT 4..SI VIS CAT D 1 1/4.

NORTHWAY

Northway

FDC 6/1371 /ORT/ FI/T NORTHWAY..NORTHWAY AK. NDB RWY 4 ORIG..NDB RWY 22 ORIG..VOR-B AMDT 3.. VOR/DME-A ORIG. ALTERNATE MINS NA WHEN ORT FSS CLSD.

POINT HOPE

Point Hope

FDC 6/2649 /PHO/ FI/T POINT HOPE, POINT HOPE AK. NDB RWY 1 ORIG..NDB RWY 19 ORIG..PROCS NA.

FDC 2/683 /PHO/ FI/T POINT HOPE, POINT HOPE, AK. NDB RWY 1 ORIG AND NDB RWY 19 ORIG ALTN MINS NA.

ALASKA

ST MARYS

St Marys Andreafsky

FDC 6/834 /KSM/ FI/T ST MARYS ANDREAFSKY ST MARYS AK. ILS/DME RWY 16 AMDT 3 ILS SI-16 NA.

SAND POINT

Sand Point

FDC 5/440 /SDP/ FI/T SAND POINT, SAND POINT, AK. NDB-B AMDT 1, NDB/DME-A AMDT 2, NDB/DME RWY 33 AMDT 1, ADD NOTE: WHEN SAND POINT ALTM NOT AVBL PROC NA.

SELAWIK

Selawik

FDC 5/2501 /WLK/ FI/T SELAWIK SELAWIK AK. VOR RWY 9 ORIG..VOR RWY 27 ORIG AND VOR/DME RWY 9 ORIG. CHG PCL NOTE TO ACTVT LIRL RWY 9/27 122.7..VASI RWY 9 CTAF.

FDC 5/1096 /WLK/ FI/T SELAWIK, SELAWIK, AK. VOR RWY 9 ORIG, VOR RWY 27 ORIG AND VOR/DME RWY 9 ORIG. PROCS NA AT NIGHT.

SITKA

Sitka

FDC 5/470 /SIT/ FI/T SITKA, SITKA AK. NDB-A ORIG..CHG FAP CRS TO SIT 002 BRG. VOR-A AMDT 7 TRML RTE BRG/ DSTC SIT NDB TO BKA VORTAC..CHG TO SIT 018 BRG 0.3 NM.

SOLDOTNA

Soldotna

FDC 4/2865 /SXQ/ FI/T SOLDOTNA, SOLDOTNA, AK RNAV RWY 7..ORIGINAL N.A.

UNALAKLEET

Unalakleet

FDC 5/2499 /UNK/ FI/T UNALAKLEET UNALAKLEET AK. NDB RWY 14 AMDT 1..LOC RWY 14 AMDT 1..VOR-C AMDT 4..VOR/DME-A AMDT 6 AND VOR/DME-D AMDT 2. CHG PCL NOTE TO ACTVT MIRL RWY 8/26 AND 14/32..VASI RWY 14/ 32..MALSR RWY 14 AND REIL RWY 32 CTAF.

VALDEZ

Valdez NO2

FDC 6/1392 /VDZ/ FI/T VALDEZ NO2, VALDEZ AK. MLS/ STOL-1 RWY 6 AMDT 2. PROC NA.

YAKUTAT

Yakutat

FDC 6/1883 /YAK/ FI/T YAKUTAT, YAKUTAT, AK. LOC/DME BC RWY 29 ORIGINAL. ADD NOTE; DISREGARD GLIDE SLOPE INDICATIONS.

ARIZONA

BULLHEAD CITY

Bullhead Laughlin

ARPT CLSD TO AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS OPERATING AT APCH SPEEDS IN EXCESS OF 110 KT AND WITH WIND COND AT THE ARPT EX CEEDING A CROSSWIND COMPONENT OF 15 KT EXCEPT 24 HOURS PPR CALL 602-754-3922.(11/86)

COOLIDGE

Coolidge

RWY 17/35 NOW OPEN. (11/86)

FLAGSTAFF

Pulliam

FDC 5/941 /FLG/PULLIAM FLAGSTAFF, AZ. VOR-A AMDT 3 ADD NOTE ACTIVATE MIRL AND VASI RWYS 3-21 AND REIL RWY 21 CTAF.

FORT HUACHUCA/SIERRA VISTA

Libby AAF/Sierra Vista Muni

FDC 6/516 /FHU/ FI/T LIBBY AAF/SIERRA VISTA MUNI, FT HUACHUCA-SIERRA VISTA, AZ. NDB RWY 26 ORIG. TERMINAL ROUTE TUS VORTAC TO DAO NDB CHANGE RADIAL TO 124.

FDC 6/512 /FHU/ FI/T LIBBY AAF/SIERRA VISTA MUNI. FT HUACHUCA SIERRA VISTA, AZ. RADAR-1 AMDT 2. CHANGE PAR RWY 29 MINS AS FOLLOWS..DH 4808 ALL CATS. CHANGE CIRCLING MINIMUMS AS FOLLOWS.. CAT A MDA 5100 HAA 384..CATS B/C MDA 5180 HAA 464..CAT D MDA 5280 HAA 564..CHANGE ARPT ELEV TO 4716..CHANGE ASR RWY 29 HAT TO 452 ALL CATS..ADDITIONAL FLIGHT DATA..CHANGE RWY 29 TDZE TO 4608. NOTES..CHANGE CIRCLING NOTE TO..CIRCLING NOT AUTHORIZED SOUTH OF RWY 8-26. CHANGE MISSED APPROACH AS FOLLOWS..PAR RWY 29 CLIMB TO 5000 THEN CLIMBING RIGHT TURN TO 9500 VIA FHU VOR R-019 TO TOMBS INT AND HOLD. ASR RWY 29 CLIMBING RIGHT TURN TO 9500 VIA FHU VOR R-019 TO TOMBS INT AND HOLD. HOLDING..CHANGE TO HOLD S, RT, 019 INBOUND.

KINGMAN

Kingman

FDC 6/3200 /IGM/FI/T KINGMAN, KINGMAN AZ. VOR RWY 21 AMDT 5..PROCEDURE NA.

MESA

Falcon Fld

MIRL RWY 04R/22L AND RWYS 04R & 22L REIL & VASI OPERATE DUSK-2100 LCL; AFTER 2100 LCL REILS TURNED OFF.(10/86)

PHOENIX

Phoenix Sky Harbor Intl

FDC 6/2254 PHX/ PHOENIX SKY HARBOR INTL, PHOENIX, AZ. VOR RWY 26L AMDT 20. DME MINIMUMS NA. CRANE 1366 MSL IN DME FINAL APCH AREA.

TUCSON

Tucson

FDC 6/3010 /TUS/FI/T TUCSON INTL,, TUCSON, AZ. HI-ILS OR TACAN RWY 11L, HI-LOC/DME BC OR TACAN RWY 29R, HI-VOR/DME OR TACAN RWY 29R, HI-VOR/DME RWY 11L. PROC NA.

WINSLOW

Winslow RCO

FREQ 122.1R DCMSND. (10/86)

ARIZONA

YUMA PROVING GROUND

Laguna AAF

FDC 6/1360 /LGF/ FI/T LAGUNA AAF, YUMA PROVING GROUND, AZ.. NDB-A ORIG..HAT 738 ALL CATS, VIS CAT B 1, CAT C 2, CAT D 2 1/4. COPTER NDB 070 ORIG..HAL 675.

FDC 6/1189 /LGF/ FI/T LAGUNA AAF. YUMA PROVING GROUND, AZ. VOR RWY 6 AMDT 2, ARPT 422. RWY 6 TDZE 377. S-6 HAT 903 ALL CATS. CIRCLING HAA 858 ALL CATS. DME MINIMA CHANGES. S-6 HAT 603 ALL CATS. CIRCLING HAA 618 ALL CATS.

ARKANSAS

ASH FLAT

Cherokee Village NDB

(CVK) OTS INDEFLY. (11/86)

FLAGLER

Flagler

ARPT NAME CHANGED TO FLAGLER AVIATION SERVICE.(11/86)

HARRISON

Harrison FSS

FREQ 122.1R DCMSND. (10/86)

JONESBORO

Jonesboro Muni

RWY 05/23 ODALS CMSND. (10/86)

RWY 18/36 CLSD INDEFLY. (11/86)

MAGNOLIA

Magnolia NDB

(AGO) RTS. (10/86)

MALVERN

Malvern NDB

(MVO) RTS. (11/86)

PINE BLUFF

Grider Field

FDC 6/893 /PBF/ FI/T GRIDER FIELD PINE BLUFF AR. VOR RWY 17 AMDT 18..S-17 VIS 1 MILE CAT D. ADD NOTE..S-17 CAT D VIS INCREASED 1/4 MILE FOR INOP MALSR.

SPRINGDALE

Springdale Muni

FDC 6/2506 /ASG/ FI/T SPRINGDALE MUNI, SPRINGDALE, AR. ILS RWY 18 ORIG..VOR RWY 18 AMDT 10..VOR/DME RWY 36 AMDT 4..ADD NOTE..CIRCLING NOT AUTHORIZED EAST OF RWY 18/36.

FDC 6/1187 /H37/ FI/T SPRINGDALE MUNI, SPRINGDALE, AR. ILS RWY 18 ORIG. NOTE: DH NOT INCREASED FOR INOP MM.

ARKANSAS

TEXARKANA

Texarkana Muni-Webb Field

ARPT NAME CHANGED TO TEXARKANA REGIONAL-WEBB FIELD.(11/86)

FDC 6/679 /TXK/ FI/T TEXARKANA MUNI-WEBB FIELD, TEXARKANA, AR. ILS RWY 22, AMDT 12. S-ILS-22 DH 634 ALL CATS. VIS 3/4 CAT D.

CALIFORNIA

BISHOP

Bishop

RWYS 12/30 & 16/34 MIRL CHANGED TO HIRL. ACTIVATE HIRL RWYS 12/30 & 16/34 AND VASI RWYS 12, 30, 16 & 34 122.0. (11/86)

CALIPATRIA

Calipatria Muni

RWY 08/26 NOW 3440 FT BY 50 FT. RWY 08 THR NO LONGER DSPLCD. (11/86)

CONCORD

Buchanan Field

CTLZ HRS 0600-2200 LCL. (11/86)

DELANO

Delano Muni

RWY 32L REIL CMSND. (11/86)

FAIR OAKS

Phoenix Field

FACILITY ABANDONED. (10/86)

FREMONT

Fremont

FACILITY ABANDONED. (10/86)

FRESNO

Fresno Air Terminal

FDC 6/3020 /FAT/FI/P FRESNO AIR TERMINAL/FRESNO/CA. LOC BC RWY 11L AMDT 6. CORRECT US GOVT CHART SW, VOL 1, PAGE XXXV, DATED 25 SEP 1986. ALTN MINS 800-2 3/4 CAT E.

RWY 11R/29L CLSD INDEFLY. (11/86)

Pinedale VORTAC

(RPI) EFFECTIVE 12 FEB 87 NAV IDENTIFIER TO BE CHANGED TO CZQ AND NAME CHANGED TO CLOVIS. (10/86)

FULLERTON

Fullerton Muni

FDC 6/482 /FUL/ FI/T FULLERTON MUNI FULLERTON CA. WHEN CTLZ NOT IN EFFECT USE SANTA ANA CA. ALSTG. LOC RWY 24 AMDT 1..S-24 CIRCLING AND LOC/DME MINIMA S-24 CIRCLING... INCREASE MDA 40 FEET CATS A/B. VOR-A AMDT 4...CIRCLING AND DUAL VOR OR VOR/DME MINIMA CIRCLING..INCREASE MDA 40 FEET CATS A/B.

FDC 5/1985 /FUL/ FI/T FULLERTON MUNI FULLERTON CA. LOC RWY 24 AMDT 1. SNA R-342 NA TO IDENTIFY QEWTI INT. DME OR RADAR REQUIRED.

FDC 5/618 /FUL/ FI/T FULLERTON MUNI FULLERTON CA VOR-A AMDT 4...DUAL VOR MINS NA. TESIA INT USES THE SLI 3.7 DME ONLY.

LAKEPORT

Skylark Seaplane Base

FACILITY ABANDONED.(10/86)

LIVERMORE

Livermore Muni

FDC 6/2145 /LVK/ FI/T LIVERMORE MUNI, LIVERMORE CA. ILS RWY 25 AMDT 3...CHANGE MSA ALTITUDES AND BEARING FROM LV LOM TO: 090-190 5400 FEET, 190-340 4900 FEET, 340-090 4000 FEET.

LONG BEACH

Daugherty Field

FDC 6/484 /LGB/ FI/T DAUGHERTY FIELD LONG BEACH CA. WHEN CTLZ NOT IN EFFECT USE SANTA ANA CA ALSTG. NDB RWY 30 AMDT 8 S-30 INCREASE MDA 60 FEET ALL CATS. INCREASE VIS 1/4 MILE CATS C/D CIRCLING...INCREASE MDA 60 FEET ALL CATS... INCREASE VIS 1/4 MILE CATS C/D. ILS RWY 30 AMDT 31..S-ILS-30 INCREASE DH 60 FEET ALL CATS. S-LOC-30 INCREASE MDA 60 FEET ALL CATS. INCREASE VIS 1/4 MILE CATS C/ D..CIRCLING-INCREASE MDA 60 FEET ALL CATS. INCREASE VIS 1/4 MILE CATS C/D. VOR OR TACAN RWY 30 AMDT 6...INCREASE MDA 60 FEET ALL CATS...CIRCLING INCREASE MDA 60 FEET ALL CATS...INCREASE VIS 1/4 MILE CATS C/D.

LOS ALAMITOS

Los Alamitos AAF

FDC 6/483 /SLI/ FI/T LOS ALAMITOS AAF LOS ALAMITOS CA. WHEN CTLZ NOT IN EFFECT USE SANTA ANA CA ALSTG. NDB-A AMDT 1...CIRCLING-INCREASE MDA 40 FEET ALL CATS... INCREASE VIS 1/4 MILE CAT C. VOR OR TACAN RWY 22L S-22L CIRCLING..DME OR RADAR S-22L CIRCLING INCREASE MDA 40 FEET ALL CATS.

FDC 5/781 /SLI/ FI/T LOS ALAMITOS AAF, LOS ALAMITOS, CA. VOR OR TACAN RWY 22L AMDT 4. ACELL INT IDENTIFIED SLI 12.8 DME OR RADAR REQUIRED. REMPS INT IDENTIFIED SLI 9 DME OR NZJ-NDB BEARING 307. KRUST INT IDENTIFIED SLI 6 DME OR NZJ-NDB BEARING 296. DME OR ADF REQUIRED.

FDC 3/1093 /SLI/ FI/T LOS ALAMITOS AAF LOS ALAMITOS CA. VOR OR TACAN RWY 22L AMDT 4. PROC AUTH FOR VOR ONLY.

LOS BANOS

Los Banos Muni

FDC 6/702 /LSN/ FI/T LOS BANOS MUNI, LOS BANOS CA. VOR/DME RWY 14 AMDT 2. PROC NA.

MADERA

Madera Muni

FDC 6/2878 /MAE/ FI/T MADERA MUNI, MADERA, CA. VOR RWY 30 AMDT 4...TERMINAL ROUTES RPI VORTAC TO PARSE INT: COURSE 276 AND PARSE INT TO KREAM INT: COURSE 276. FAC: 276.

MERCED

Merced Muni

CTLZ HRS 0800-1700 LCL. (9/86)

FDC 6/2836 /MCE/ FI/T MERCED MUNI, MERCED, CA. LOC BC RWY 12 AMDT 6...VOR RWY 12 AMDT 4...CIRCLING CAT A MDA 560/HAA 407, CAT C MDA 680/HAA 527. MSA ALTITUDE MCE R-080 TO R-170 3500. CHANGE NOTE TO: ACTIVATE MALSR RWY 30, HIRL RWY 12-30 - CTAF.

Merced Muni ILS/DME

(I-MCE) RWY 30 ILS MONITORED CONTINUOUS. (10/86)

MONTAGUE

Siskiyou County

FDC 6/2709 /SIY/ FI/T SISKIYOU COUNTY, MONTAGUE, CA..VOR-B AMDT 5...PROC NA. IFR DEPARTURE...PROC NA.

NEEDLES

Needles

ARPT CLSD TO AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS WEEKEND AND 1700-0800 LCL WKDAY EXCEPT PPR CALL 619-254-2422. (11/86)

OAKLAND

Metropolitan Oakland Intl

FDC 6/2844 /OAK/ FI/T METROPOLITAN OAKLAND INTL, OAKLAND, CA. NDB RWY 27R, AMDT 3. CASES OM/DME MINIMUMS NA.

ORLAND

Haigh Fld

FDC 6/1042 /037/ FI/T HAIGH FLD, ORLAND, CA. VOR-A AMDT 1 CIRCLING MDA 1100/HAA 880 ALL CATS. VIS CAT A 1, CAT B 1 1/4, CAT C 2 1/2, CAT D 2 3/4.

PETALUMA

Petaluma Muni

ACTIVATE MIRL RWY 11/29 122.8. (10/86)

REDDING

Redding Muni

FDC 6/2792 /RDD/ FI/T REDDING MUNI, REDDING, CA. NDB RWY 34 AMDT 4. ILS RWY 34 AMDT 9. LOC/DME BC RWY 16 AMDT 4: WHEN ATCT NOT IN OPERATION, ALTERNATE MINS NA.

SACRAMENTO

Sacramento Metropolitan

FDC 6/3147 /SMF/FI/T SACRAMENTO METROPOLITAN, SACRAMENTO CA. NDB RWY 34 AMDT 2...S-34 MDA ALL CATS 420 HAT 398.

SANTA ANA

John Wayne Arpt-Orange County

FDC 6/597 /SNA/ FI/T JOHN WAYNE ARPT-ORANGE COUNTY, SANTA ANA CA. ILS RWY 19R AMDT 10...LOC/DME OR LOC/VOR MINIMUMS CIRCLING 680-1 CAT A/B, 680-1 1/2 CAT C. 680-2 CAT D. LOC BC RWY 1L AMDT 9...CIRCLING 680-1 CAT A/B, 680-1 1/2 CAT C, 680-2 CAT D. VOR RWY 1L AMDT 2...CIRCLING 680-1 CAT A/B, 680-1 1/2 CAT C, 680-2

CALIFORNIA

CAT D. VOR RWY 19R AMDT 23 DUAL VOR MINIMUMS..S-19R 520-1/2 CAT A/B, 520-3/4 CAT C, 580-1 CAT D. CIRCLING 680-1 CAT A/B, 680-1 1/2 CAT C, 680-2 CAT D.

FDC 5/614 /SNA/ FI/T JOHN WAYNE ARPT-ORANGE CO SANTA ANA CA VOR RWY 1L AMDT 2 HOLDING AT NEWPO INT/RADAR REQUIRED. TERMINAL ROUTE MINOE TO NEWPO INT/RADAR REQUIRED.

FDC 5/613 /SNA/ FI/T JOHN WAYNE ARPT-ORANGE CO SANTA ANA CA. IFR DEPARTURE PROC RWY 19L/19R COMPLY WITH SANTA ANA SID OR RADAR VECTORS.SANTA MARIA

Guadalupe VOR

(GLJ) UNUSABLE 300-325 BYD 10 NM BELOW 3000 FT. (11/86)

Santa Maria Public

FDC 6/2557 /SMX/ FI/T SANTA MARIA PUBLIC..SANTA MARIA CA. VOR RWY 12 AMDT 12. TERMINAL ROUTE FROM AVILA INT TO GLJ VOR NA.

SANTA YNEZ

Santa Ynez

FDC 6/1617 /IZA/ FI/T SANTA YNEZ SANTA YNEZ, CA. NDB RWY 8 ORIG PROC NA.

VISALIA

Visalia Muni

FDC 6/1129 /VIS/ FI/T VISALIA MUNI..VISALIA CA. ILS RWY 30 AMDT 3. ADD NOTE: DME REQUIRED FOR PROCEDURE TURN.

Visalia Muni ILS

(I-VIS) RWY 30 VILIA LOM IDENT VI OTS INDEFLY. (10/86)

WATSONVILLE

Watsonville Muni

RWY 08/26 NOW 3999 FT BY 90 FT. RWY 01/19 NOW 4501 FT BY 150 FT. (10/86)

COLORADO

ALAMOSA

Alamosa RCO

COLOCATED WITH ALAMOSA VORTAC, FREQ 121.5 CMSND.(11/86)

DENVER

Front Range

ACTIVATE MIRL RWY 17/35 122.7. (10/86)

Jeffco

FDC 6/3189 /BJC/FI/T JEFFCO DENVER CO. ILS RWY 29R AMDT 9..RNAV RWY 29R AMDT 8. CIRCLING MDA 6140 HAA 482 CAT A/B/C. MDA 6240 HAA 582 CAT D.

Stapleton Intl

RWY 17R REIL DCMSND. (11/86)

DENVER TERMINAL CONTROL AREA (TCA). TCA DME BOUNDARIES ARE BASED ON RWY 26L ILS/DME I-DEN 110.3 CHAN 40. (10/86)

COLORADO

FDC 6/2321 DEN/STAPLETON INTL/DENVER, CO. ILS/DME RWY 08R AMDT 3 I-GQW. SIDESTEP RWY 08L NA. 5393 MSL CRANE 394533N/1045338W.

DURANGO

Durango La Plata County

FDC 6/2387 /DRO/ FI/T DURANGO LA PLATA COUNTY, DURANGO, CO. ILS/DME RWY 2 AMDT 1, VOR-A AMDT 5. VOR/DME RWY 2 AMDT 3: WHEN CTLZ NOT IN EFFECT, EXCEPT FOR OPERATORS WITH APPROVED WEATHER REPORTING SERVICE. ALTN MINS AND PROC NA.

EAGLE

Eagle County

RWY 25 PAPI CMSND (PAPI ONLY VISIBLE TO 6 DEGS LEFT OF CNTRLN DUE TOTERRAIN.(11/86)

HAXTUN

Haxton Muni

AIRPORT NOW OPEN.(10/86)

HAYDEN

Yampa Valley

RWY 10/28 NOW 10000 FT BY 150 FT. RWY 10 THR DSPLCD 500 FT. (11/86)

ACTIVATE HIRL RWY 10/28 AND REILS RWYS 10 & 28. (11/86)

HUGO

Hugo VORTAC

(HGO) FREQ 112.10 EFFECTIVE 18 DEC 86. (10/86)

MONTE VISTA

Monte Vista Muni

RWY 01/19 CHANGED TO 02/20. (11/86)

NUCLA

Hopkins Field

RWY 01/19 CLSD PERMLY. (11/86)

PUEBLO

Pueblo Memorial

FDC 6/1170 /PUB/ FI/T PUEBLO MEMORIAL, PUEBLO, CO. HI-VOR RWY 26R TAC ORIGINAL. VOR RWY 26R TAC AMDT 25 INCREASE ALTITUDE AT PUB VORTAC TO 5500 FEET. STRAIGHT IN MINIMUMS NA.

RIFLE

Garfield County LOC/DME

(I-RIL) RWY 26 LOC FREQ 110.9, DME CHANNEL 046X CMSND EFFECTIVE 18 DEC 86. (11/86)

SALIDA

Harriet Alexander Field

RWY 06 THRESHOLD DISPLACED 267 FEET.(10/86)

RWY 06 DSPLCD THR MARKED BY THRESHOLD LIGHTS FOR NIGHT OPERATIONS ONLY.(11/86)

CONNECTICUT

BRIDGEPORT

Igor I. Sikorsky Memorial

FDC 6/690 /BDR/ FI/T IGOR I SIKORSKY MEMORIAL, BRIDGEPORT, CT. ILS RWY 6 AMDT 5. SI ILS VIS 1 ALL CATS.

GROTON/NEW LONDON–

Groton-New London

FDC 6/2233 /GON/ FI/T GROTON-NEW LONDON, GROTON/ NEW LONDON CT. ILS RWY 5 AMDT 7..VOR RWY 5 AMDT 3..VOR RWY 23 AMDT 5... MSA TMU VOR 360 CW-270 2000, 270 CW-360 2600.

HARTFORD

Hartford-Brainard

FDC 6/2234 /HFD/ FI/T HARTFORD-BRAINARD, HARTFORD CT. NDB RWY 2 ORIG..MSA HDS NDB 060 CW-240 2600, 240 CW-060 3100.

HAYDEN

Yampa Valley ILS/DME

(I-HDN) RWY 10 CMSND EFFECTIVE 18 DEC 86.(10/86)

MERIDEN

Meriden Markham Muni

FDC 6/2182 /MMK/ FI/T MERIDEN MARKHAM MUNI.MERIDEN CT. NDB RWY 36 AMDT 4..VOR RWY 36 ORIG. NIGHT MINS NA. CIRCLING MINS NA.

NEW HAVEN

Tweed-New Haven

FDC 6/1258 /HVN/ FI/T TWEED-NEW HAVEN AIRPORT ..NEW HAVEN CT. ILS RWY 2 AMDT 12. S-ILS ALL CATS VIS 1..S-LOC CATS A/B/C VIS 1. INOPERATIVE TABLE DOES NOT APPLY. VOR RWY 2 AMDT 19.. S-2 CATS A/B/C VIS 1. INOPEATIVE TABLE DOES NOT APPLY. TAKEOFF MINIMUMS RWY 2 300-1..RWY 20 STANDARD..RWY 32 400-1.. RWY 14 300-1 OR STANDARD WITH A MINIMUM CLIMB OF 240 FEET PER NM TO 300.

NUCLA

Hopkins Field

RWY 01/19 CLSD INDEFLY.(10/86)

SAGUACHE

Saguache Muni

ARPT CLSD TO PUBLIC USE. (10/86)

WILLIMANTIC

Windham

FDC 6/2230 /5B0/ FI/T WINDHAM, WILLIMANTIC, CT. VOR-A AMDT 5..MSA ORW VORTAC 170 CW-180 2300. 1800 CW-270 2600.

WINDSOR LOCKS

Bradley Intl

FDC 6/1944 /BDL/ FI/T BRADLEY INTL, WINDSOR LOCKS, CT. NDB RWY 6 AMDT 24. ILS RWY 6 AMDT 28. MISSED APCH: CLIMBING RT TO 4000 DIRECT HFD VORTAC AND HOLD SE, RT 334 INBOUND.

CONNECTICUT

FDC 5/308 /BDL/ FI/T BRADLEY INTL, WINDSOR LOCKS, CT. NDB RWY 6 AMDT 25 PENNA INT. RADAR RQD. HFD VORTAC R-322 NOT AUTHORIZED.

Bradley VORTAC

(BDL) DME UNUSABLE 040-085 BYD 13 NM BLO 2000 FT; 130-150 BYD 10 NM BLO 3000 FT; 170-195 BYD 14 NM BLO 3000 FT; 250-290 BYD 18 NM BLO 6000 FT. (10/86)

(BDL) VOR PORTION UNUSABLE 100-170 BYD 10 NM BELOW 6000 FT; 260-290 BYD 15 NM BELOW 6000 FT. VOR PORTION RTS. (10/86)

DELAWARE

WILMINGTON

Greater Wilmington-New Castle County

FDC 6/1537 /ILG/ FI/T GREATER WILMINGTON NEW CASTLE COUNTY WILMINGTON, DE..ILS RWY 1 AMDT 18..SI ILS DH 332/HAT 256 ALL CATS. VIS RVR 4000 ALL CATS. SI LOC VIS RVR 4000 CATS A/B. TKOF MINS RWY 19 300-1.

FDC 5/1577 /ILG/ FI/T GREATER WILMINGTON-NEW CASTLE COUNTY WILMINGTON, DE. VOR RWY 19 AMDT 3. SI MDA 680/HAT 609 ALL CATS. VIS 1 3/4 CAT C/2 CAT D. CIRCLING MDA 680/HAA 600 ALL CATS.

DISTRICT OF COLUMBIA

Dulles Intl

FDC 6/3090 /IAD/ FI/T DULLES INTL, WASHINGTON, DC. NDB RWY 1R AMDT 14, SI MDA 800/HAT 487 ALL CATS. RADAR-1 AMDT 11, ASR RWY 1R, MDA 800/HAT 487 ALL CATS. VIS RVR 4000 CAT C. ASR RWY 30. MDA 800/HAT 511 ALL CATS. VIS 1 1/2 CAT C/D. ILS RWY 1R AMDT 18 CAT 2. DH 473/423 HAT 160/110 ALL CATS. CAT 3A NA.

FDC 6/1540 /IAD/DULLES INTL/WASHINGTON/DC. RNAV RWY 12 AMDT 8. TRML ROUTE EEY VORTAC /IAF/ TO SENIC WPT NA.

Washington National

FDC 6/2932 /DCA/ FI/T WASHINGTON NATIONAL, WASHINGTON, D.C., RADAR-1 AMDT 25 ASR RWY 15. SI MDA 740/HAT 725 ALL CATS. VIS 2 CAT C, 2 1/4 CAT D. CIRCLING MDA 740/HAA 724 ALL CATS.

Washington National LDA/DME

(I-ASO) RWY 18 LOC USABLE. (11/86)

FLORIDA

AVON PARK

Avon Park Muni

RWYS 04 & 22 VASI CMSND. (11/86)

CRESTVIEW

Bob Sikes

FDC 6/3145 /CEW/FI/T BOB SIKES CRESTVIEW FL. LOC RWY 17 ORIG..NDB RWY 17 ORIG..MSA WITHIN 25 NM OF SIKKS / CE/NDB 2300. VOR-A AMDT 6..MSA WITHIN 25 NM OF CEW VORTAC 2300.

DAYTONA BEACH

Daytona Beach Regional

FDC 6/2409 /DAB/ FI/T DAYTONA BEACH REGIONAL, DAYTONA BEACH, FL. VOR RWY 16 AMDT 16..MISSED APCH: CLIMB TO 4000 VIA OMN R-161 TO SMYRA INT AND HOLD. LOC BC RWY 25R AMDT 12, 18 DME ARC UNUSBL R-151 CLKWS R-161 BLO 4000. ILS RWY 7L AMDT 26, 18 DME ARC UNUSBL R-161 CLKWS R-166 BLO 4000.

FORT LAUDERDALE

Fort Lauderdale-Hollywood Intl

FDC 6/2286 FLL/FT LAUDERDALE-HOLLYWOOD INTL/FORT LAUDERDALE, FL. ILS RWY 27R AMDT 1. SI ILS VIS 3/4 ALL CATS. SI LOC MDA 460/HAT 452 ALL CATS. VIS 1 CATS A/B..1 1/4 CAT C.. 1 1/2 CAT D. INOP TABLE DOES NOT APPLY.

FDC 6/1053 /FLL/ FI/T FT LAUDERDALE-HOLLYWOOD INTL, FORT LAUDERDALE, FL. ILS RWY 09L AMDT 11..TRML ROUTE FLL VOR/DME TO PIONN INT/FLL 10.8 DME NA. LOC RWY 09R AMDT 1.. TRML ROUTE FLL VOR/DME TO CIBEL INT/FLL 6.6 DME NA. VOR RWY 27R AMDT 8..MISSED APCH. CLIMB TO 3000 VIA HDG 270 WITHIN 15 NM. ILS RWY 27R AMDT 1..MISSED APCH. CLIMB TO 3000 VIA HDG 270 WITHIN 15 NM.

KEY WEST

Key West RCO

DCMSND. (10/86)

KISSIMMEE

Kissimmee Muni

FDC 6/268 /ISM/ FI/T KISSIMMEE MUNI/KISSIMMEE/FL. VOR/DME-A AMDT 5. PROC NA.

LAKELAND

Lakeland Muni ATCT

ATCT HRS 0700-2100 LCL. (11/86)

MELBOURNE

Melbourne Regional

RWY 09L/27R MIRL CMSND. (11/86)

FDC 6/3080 /MLB/FI/T MELBOURNE REGIONAL, MELBOURNE FL. ILS RWY 9R AMDT 7..VOR RWY 27L AMDT 10..LOC BC RWY 27L AMDT 7..CORRECT MERCS INT/OM TO VRB R332. VOR RWY 9R AMDT 17..CORRECT TRING INT TO VRB R323 AND MISSED APPROACH HOLDING TO HEADING 143 INBOUND.

FDC 6/2493 /MLB/ FI/T MELBOURNE REGIONAL, MELBOURNE, FL. NDB RWY 9R AMDT 12 MSA FROM SQT NDB 060 CW TO 330 DEGREES 2100 WITH 25 NM. VOR RWY 9R AMDT 17, VOR RWY 27L AMDT 10, LOC BC RWY 27L AMDT 7. ILS RWY 9R AMDT 7, MSA FROM MLB VOR/DME 060 CW TO 330 2100 WITHIN 25 NM.

MIAMI

Miami Intl

FDC 6/2214 /MIA/ FI/T MIAMI INTL, MIAMI, FL. TKOF-MINS RWY 27L, 300-1.

FDC 6/437 /MIA/ FI/T MIAMI INTL..MIAMI FL. ILS RWY 12 ORIG..LOC RWY 30 AMDT 3..VOR RWY 30 AMDT 5..VOR RWY 12 AMDT 26. PROC NA. 27R 300-1.

NAPLES

Naples Muni ATCT

ATCT HRS 0600-2200 LCL. (11/86)

ORLANDO

Orlando Intl

FDC 6/2871 /MCO/ FI/T ORLANDO INTL, ORLANDO FL. VOR/ DME RWY 18L AMDT 4..SI MDA 460/HAT 364 ALL CATS. VOR/DME RWY 18R AMDT 4..SI MDA 460/HAT 368 ALL CATS.

PANAMA CITY

Panama City-Bay County

FDC 6/1858 /PFN/ FI/T PANAMA CITY-BAY COUNTY, PANAMA CITY, FL. VOR OR TACAN-A AMDT 13. CIRCLING MDA 700/HAA 679 ALL CATS. VIS 2 CAT C, 2 1/4 CAT D. ALTN MINS 800-2 1/4 CAT D. NDB RWY 14 AMDT 3. CIRCLING AND DME MINS CIRCLING MDA 700/HAA 679 CAT D. VIS 2 1/4 CAT D. ILS RWY 14 AMDT 13. CIRCLING MDA 700/HAA 679 CAT D. VIS 2 1/4 CAT D. VOR OR TACAN RWY 14 AMDT 15. CIRCLING AND DME MINS CIRCLING MDA 700/HAA 679 CAT D. VIS 2 1/4 CAT D. ALTN MINS 800 2 1/4 CAT D. VOR OR TACAN RWY 32 AMDT 10. CIRCLING MDA 700/HAA 679 CAT D. VIS 2 1/4 CAT D. ALTN MINS 800 2 1/4 CAT D. RADAR-1 ORIG. CIRCLING MDA 700/HAA 679 CAT D. VIS 2 1/4 CAT D. ALTN MINS 800 2 1/4 CAT D.

PENSACOLA

Pensacola Regional

FDC 6/292 /PNS/ FI/T PENSACOLA REGIONAL, PENSACOLA, FL. LOC BC 34 AMDT 10. PROC NA.

PLACIDA

Rotonda

ARPT CLSD TO PUBLIC USE. (11/86)

PORT ST. JOE

Costin

ARPT OPEN TO PUBLIC USE. (11/86)

PUNTA GORDA

Charlotte Co

FDC 6/2028 /PGD/ FI/T PUNTA GORDA/CHARLOTTE CO PUNTA GORDA FL. VOR RWY 21 AMDT 1..CIRCLING MDA CAT B/C 540/HAA 515. VOR RWY 33 AMDT 1..DME CIRCLING MDA CAT B/C 540/HAA 515. RNAV RWY 27 AMDT 2..CIRCLING MDA CAT B/C 540/HAA 515.

FLORIDA

ST PETERSBURG/CLEARWATER

St Petersburg-Clearwater Intl

FDC 6/2442 /PIE/ FI/T ST PETERSBURG-CLEARWATER INTL, ST PETERSBURG-CLEARWATER FL. TKOF MINS RWY 9 300-1. REASON..TMPRY CRANE 159MSL .5NM SE RWY 27 THLD.

FDC 5/2126 /PIE/ FI/T ST PETERSBURG-CLEARWATER INTL ST PETERSBURG-CLEARWATER FL. ILS RWY 17L AMDT 18 LOC BC RWY 35R AMDT 13 NDB RWY 17L AMDT 19 VOR RWY 17L AMDT 10. CIRCLING MDA 560/HAA 549 CATS A/B/C. REASON..TMPRY 245 CRANE 1.2 NM EAST OF ARPT.

TALLAHASSEE

Tallahassee Muni

RWY 09R/27L CLSD WHEN ATCT CLSD. (11/86)

FDC 6/1881 /TLH/ FI/T TALLAHASSEE MUNI, TALLAHASSEE, FL. ILS RWY 36 AMDT 22. NDB RWY 36 AMDT 18. FEEDER ROUTE TLH VORTAC TO WAKUL LOM USE 178 BRG TO TL LOM.

FDC 6/1863 /TLH/ FI/T TALLAHASSEE MUNI..TALLAHASSEE FL. HI-ILS RWY 36 AMDT 3. FEEDER ROUTE SANDA TO TL NDB AUTH FOR TACAN ONLY. HI-VOR/DME OR TACAN RWY 36 AMDT 1. AUTH FOR TACAN ONLY ILS RWY 27L AMDT 2. SPADD INT NA.

FDC 6/528 /TLH/ FI/T TALLAHASSEE MUNI TALLAHASSEE FL. ILS RWY 36 AMDT 22 LOC MINIMUMS NA.

TAMPA

Tampa Intl

RWY 09/27 MIRL CHANGED TO HIRL. (10/86)

RWY 36L VASI DCMSND. (10/86)

FDC 6/2186 /TPA/ FI/T TAMPA INTL..TAMPA FL. VOR RWY 9 AMDT 7 DME MINS RADAR-1 AMDT 11 ASR RWY 9. MDA 500/HAT 479 ALL CATS.

TITUSVILLE

Space Center Executive

RWY 18/36 MIRL CHANGED TO HIRL. (11/86)

VENICE

Venice Muni

RWY 04 VASI CMSND. MIRL RWYS 04/22 & 13/31 & REIL RWYS 13,31 & 22 AND VASI RWYS 04, 22, 13 & 31 OPERATE DUSK-2400 LCL, AFTER 2400 LCL ACTIVATE 122.7. (10/86)

WEST PALM BEACH

Palm Beach County Park

RWY 21 THR NO LONGER DSPLCD. (11/86)

GEORGIA

ATHENS

Athens Muni ATCT

DURING TEMPORARY CLOSURE BROADCAST POSTION/INTENTIONS/ADVISORIES ON FREQ 123.0.(11/86)

GEORGIA

Athens Muni LOC

(I-AHN) RWY 27 CMSND. (10/86)

Bulldog NDB

(BJT) FREQ 221, OPERATIONAL CONTINUOUS, PUBLIC USE, CONTROLLING FSS ATL, CMSND.(10/86)

ATLANTA

Dekalb-Peachtree

FDC 6/2470 /PDK/ FI/T DEKALB-PEACHTREE ATLANTA, GA. NDB RWY 9 ORIG. PROC NA.

AUGUSTA

Bush Field

FDC 6/1491 /AGS/ FI/T BUSH FIELD, AUGUSTA, GA. ILS RWY 17 AMDT 5. CHANGE NOTE 2 TO READ... ALTN MINS NA.

FDC 6/496 /AGS/ FI/T BUSH FIELD AUGUSTA, GA. VOR-A AMDT 20. PROC NA. NDB RWY 35 AMDT 25 AND ILS RWY 35 AMDT 24. TERMINAL ROUTE AGS VORTAC TO AG LOM NA. MISSED APPROACH CLIMB TO 3000 DIRECT EMR NDB AND HOLD N, RT 170 INBOUND.

FDC 5/1194 /AGS/ FI/T BUSH FIELD, AUGUSTA, GA. NDB RWY 17 AMDT 12. TRML ROUTE AGS VORTAC TO SMELL INT NA. ILS RWY 17 AMDT 5. TRML ROUTE AGS VORTAC TO CARDO INT NA.

Daniel Field

FDC 6/749 /DNL/ FI/T DANIEL FLD, AUGUSTA GA. NDB RWY 10 ORIG...MISSED APCH: CLIMB TO 3000 THEN LEFT TURN DIRECT EMR NDB AND HOLD N, RT 170 INBOUND.

FDC 6/501 /DNL/ FI/T DANIEL FIELD, AUGUSTA GA. VOR-B AMDT 14..RNAV RWY 10 AMDT 4..PROC N/A. NDB/DME-C ORIG. TERMINAL ROUTE AGS VORTAC TO AG LOM NA. TERMINAL ROUTE BEANS INT TO AL LOM NA. RADAR REQUIRED.

BRUNSWICK

Glynco Jetport

FDC 6/2473 /BQK/ FI/T GLYNCO JETPORT, BRUNSWICK, GA. ILS RWY 7 AMDT 5 USE BRUNSWICK ALTIMETER SETTING. WHEN NOT AVAILABLE USE JAX ALTIMETER SETTING AND INCREASE DH AND MDAS 200 FEET. NDB RWY 7 AMDT 7 VOR/DME-B AMDT 4, RNAV RWY 7 AMDT 4. RNAV RWY 25 AMDT 4 USE BRUNSWICK ALTIMETER SETTING. WHEN NOT AVAILABLE USE JAX ALTIMETER SETTING AND INCREASE ALL MDAS 200 FEET.

Malcolm McKinnon

FDC 6/2474 /SSI/ FI/T MALCOLM MCKINNON, BRUNSWICK, GA. NDB RWY 4 AMDT 2. NDB RWY 22 AMDT 2. VOR RWY 4 AMDT 12. RNAV RWY 22 AMDT 3. USE BRUNSWICK ALTIMETER SETTING. WHEN NOT AVAILABLE USE JAX ALTIMETER SETTING AND INCRASE ALL MDAS 200 FEET. ALT MINS NA.

COLUMBUS

Columbus Metropolitan

FDC 6/2640 /CSG/ FI/T COLUMBUS METROPOLITAN, COLUMBUS, GA. RADAR-1 AMDT 7..ASR RWY 5. SI VIS RVR 4000 CATS A/B. ASR RWYS 12 AND 23....SI VIS 1 1/4 CATS A/B...CIRCLING VIS 1 1/4 CATS A/B.

FDC 6/263 /CSG/ FI/T COLUMBUS GA. LOC BC RWY 23 AMDT 11, PROC NA.

Lawson AAF-Fort Benning

FDC 6/226 /LSF/ FI/T LAWSON AAF FORT BENNING (COLUMBUS) GA. RADAR-1 AMDT 12 RADAR-2 AMDT 2. DELETE NOTE..VISUAL APCH TO RWY 32 NA.

EASTMAN

Eastman-Dodge County

AFTER 2300 LCL ACTIVATE MIRL RWY 02/20 122.9. (11/86)

JEKYLL ISLAND

Jekyll Island

FDC 6/2471 /09J/ FI/T JEKYLL ISLAND, JEKYLL ISLAND, GA. VOR-A AMDT 6 USE BRUNSWICK ALTIMETER SETTING WHEN NOT AVAILABLE USE JAX FL. ALTIMETER SETTING AND INCREASE ALL MDAS 180 FEET.

JESUP

Jesup-Wayne County

FDC 6/3114 /JES/FI/T JESUP-WAYNE COUNTY..JESUP GA. NDB RWY 18 AMDT 4. PROC NA.

FDC 6/2472 /JES/ FI/T JESUP-WAYNE COUNTY, JESUP, GA. NDB RWY 10 AMDT 4. USE BRUNSWICK ALTIMETER SETTING. WHEN NOT AVAILABLE USE SAVANNAH ALTIMETER SETTING AND INCREASE ALL MDAS 60 FEET.

LA GRANGE

Callaway

RWY 13/31 NOW 5600 FT BY 150 FT (11/86)

MOULTRIE

Moultrie Muni

FDC 6/2428 /MGR/ FI/T MOULTRIE MUNI, MOULTRIE, GA. RNAV RWY 22 AMDT 1, NA.

NEWNAN

Newnan-Coweta

FDC 6/3050 /CCO/FI/T NEWNAN-COWETA..NEWNAN GA. IFR DEPARTURE PROCEDURE RWY 32...LEFT TURN..CLIMB ON HEADING 275 TO 2500 BEFORE PROCEEDING ON COURSE.

ROME

Richard B Russell

FDC 6/1732 /RMG/ FI/T RICHARD B. RUSSELL, ROME, GA. NDB-A AMDT 3 ALTN MINS NA.

SAVANNAH

Savannah International

FDC 6/2296 SAV/SAVANNAH INTL/SAVANNAH, GA. RNAV RWY 18 AMDT 5..TRML ROUTE REBUS INT /IAF/ TO STILT WPT/ NOPT/ MIN ALT 2100.

SYLVANIA

Plantation Airpark

FDC 6/2608 /56J/ FI/T PLANTATION ARPK, SYLVANIA, GA. NDB RWY 23 ORIG. PROC NA AT NIGHT.

VALDOSTA

Valdosta Regional ATCT

ATCT HRS 0900-1700 LCL MON-FRI. (10/86)

HAWAII

HONOLULU

Honolulu Intl

FDC 6/1927 /HNL/ FI/T HONOLULU INTL, HONOLULU, HI. NDB RWY 8L AMDT 18/ILS RWY 4R AMDT 10/HI-ILS RWY 8L AMDT 5/ILS RWY 8L AMDT 20/LDA/DME RWY 26L AMDT 4/ VOR OR TACAN-A ORIG/VOR/DME OR TACAN-B ORIG. CAT D CIRCLING MDA 760 HAT 747 VIS 2 1/1. (REASON 450 FT. MSL TOWER 1.9 NM EAST RWY 26L)

IDAHO

BURLEY

Burley Muni

RWY 02/20 NOW 4094 FT BY 80 FT. RWY 02 THR DSPLCD 620 FT. RWY 06/24 NOW 4067 FT BY 100 FT. RWY 06 THR DSPLCD 410 FT. (11/86)

CASCADE

Cascade

RWY 11/29 CHANGED TO 12/30.

COEUR D'ALENE

Coeur D'Alene

CTLZ HRS 0700-1900 LCL MON-FRI. (10/86)

JEROME

Jerome County

FDC 6/944 /U73/ FI/T JEROME COUNTY..JEROME ID. VOR/ DME-A ORIG MDA 4840 HAT 793 ALL CATS. VISIBILITY CAT B 1 1/4 ..CAT C 2 1/4..CAT D 2 1/2. ADD NOTE: INCREASE MDA ADDITIONAL 60 FT WHEN USING TWIN FALLS ALTIMETER.

REXBURG

Rexburg-Madison County

RWY 17/35 NOW 4203 FT BY 75 FT.(11/86)

TWIN FALLS

Twin Falls Sun Valley Reg Joslin Field

FDC 1/1899 /TWF/ FI/T TWIN FALLS CITY-COUNTY ARPT JOSLIN FLD/ TWIN FALLS/ ID. NDB RWY 25 AMDT 4/ ILS RWY 25 AMDT 5. WHEN TWF ATCT NOT IN OPN ALTN MINS NA.

ILLINOIS

ALTON/ST LOUIS

St Louis Regional

FDC 6/2973 /ALN/ FI/T ILS RWY 29, AMDT 8: MINIMUMS S-ILS 29 DH 787, HAT 250 ALL CATS.

ILLINOIS

CHICAGO

Chicago Midway

FDC 6/2675 /MDW/ FI/T CHICAGO MIDWAY..CHICAGO IL NDB RWY 31L AMDT 10 AND ILS RWY 31L AMDT 1..CHANGE MINIMUM ALTITUDE AT RUNTS INT/GLEAM INT/AND HILLS INT FROM 2000 FT TO 2100 FT WHEN AUTHORIZED BY ATC.

Chicago-O'Hare Intl

RWY 32L SSALR CHANGED MALSR. (10/86)

FDC 6/1420 /ORD/ FI/T CHICAGO-O'HARE INTERNATIONAL AIRPORT. CHICAGO, IL. ILS RWY 9L. AMDT 6 MINS: S-ILS 9L: DH 908. VIS RVR 4000/HAT 250 ALL CATS. S-LOC 9L: CAT A VIS RVR 4000. ORD 3 DME MINS: S-LOC 9L CATS A/B VIS RVR 4000.

FDC 5/2768 /ORD/ FI/T CHICAGO-OHARE INTL..CHICAGO IL ILS RWY 9R AMDT 12. AUTOPILOT COUPLED APCH NA.

EFFINGHAM

Effingham County Memorial

RWY 29 REIL CMSND. (10/86)

ACTIVATE REILS RWYS 01 & 29 122.8. (10/86)

EPROA

Mount Hawley Auxiliary

RWY 35 VASI CMSND. (11/86)

GIBSON CITY

Gibson City Muni

RWYS 18, 36 & 27 THR NO LONGER DSPLCD. RWY 09 THR DSPLCD 453 FT. (10/86)

LACON

Marshall County

RWY 08/26 CLSD INDEFLY. (10/86)

MOLINE

Quad-City

FDC 6/2629 /MLI/ FI/T QUAD-CITY, MOLINE, IL. RNAV RWY 30 AMDT 7 NOW RNAV RWY 31 AMDT 7. RADAR-1 AMDT 6: ASR MINS RWYS 12, 30 NOW RWYS 13, 31.

MOWEAQUA

Rainbow

FACILITY ABANDONED. (11/86)

PEORIA

Greater Peoria

FDC 5/2511 /PIA/ FI/T GREATER PEORIA, PEORIA, IL. NDB RWY 31, AMDT 12, ILS RWY 13, AMDT 3, ILS RWY 31, AMDT 3, VOR/DME OR TACAN RWY 31, AMDT 6, AND VOR RWY 13 / TAC/, AMDT 20. MSA INCREASE 2400 TO 2800.

PRINCETON

Piper

ARPT CLSD TO PUBLIC USE. (11/86)

ILLINOIS

QUINCY

Qunicy Muni Baldwin Field

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT PPR CALL 217-885-3285. (10/86)

ROCKFORD

Greater Rockford

FDC 6/3151 /RFD/FI/T GREATER ROCKFORD ROCKFORD, IL. NDB RWY 36 AMDT 22 AND ILS RWY 36 AMDT 25. TERMINAL ROUTE RUSLL INT TO GILMY LOM ALTITUDE 2300.

FDC 6/2716 /RFD/ FI/T GREATER ROCKFORD, ROCKFORD IL. NDB RWY 36 AMDT 22..ILS RWY 36 AMDT 25..LOC BC RWY 18 AMDT 12..VOR RWY 12 AMDT 1..WHEN CONTROL TOWER CLOSED, ACTIVATE SSALR RWY 36 - CTAF, TO INCREASE INTENSITY HIRL RWY 18-36 AND ACTIVATE MIRL RWYS 6-24 AND 12-30 CONTACT RFD FSS.

ROMEOVILLE

Lewis University

FDC 6/2169 /LOT/ FI/T LEWIS UNIVERSITY ROMEOVILLE IL. VOR RWY 9 AMDT 1..CIRCLING CAT C MDA 1480 HAA 808 VIS 2 1/4.

SULLIVAN

Jean Wood

FACILITY ABANDONED. (11/86)

INDIANA

CARMEL

Helicopter Airways of Ind. Heliport

FACILITY ABANDONED. (11/86)

CRAWFORDSVILLE

Crawfordsville NDB

(CFJ) OTS INDEFLY. (10/86)

FORT WAYNE

Fort Wayne Muni/Baer Fld/

RWY 04 MALSR OTS TIL 31 DEC 86. (10/86)

FDC 6/2427 /FWA/ FI/T FORT WAYNE MUNI (BAER FIELD), FORT WAYNE, IN. ILS RWY 31 AMDT 23; NDB RWY 31 AMDT 20; LOC BC RWY 13 AMDT 10; VOR RWY 13 AMDT 13. RWY 13/31 NOW RWY 14/32.

Fort Wayne Muni/Baer Fld/ILS

(I-CHN) RWY 04 GS/MM/OM SHUTDOWN 13 OCT TO 31 DEC 86. (10/86)

FRENCH LICK

Oranj NDB

(RRJ) CONTROLLING FSS HUF.(10/86)

GARY

Gary Muni

FDC 6/2761 /GYY/ FI/T GARY MUNI GARY IN. IFR TAKEOFF MINIMUMS RWY 12 300-1. RWY 30/02/20 STANDARD.

REASON..CRANE 714 FT MSL LOCATED AT 413624N 0872328W.

INDIANAPOLIS

Greenwood BOAC

ARPT NAME CHANGED TO GREENWOOD MUNI. (11/86)

Indianapolis Downtown Heliport

ACTIVATE NSTD VASI 123.05. (10/86)

Indianapolis Intl

RWY 31 RVR OTS 07 JAN 87. (11/86)

Indianapolis Intl ILS

(I-COA) RWY 31 LOC & OM OTS TIL 12 JAN 87. (11/86)

Indianapolis Terry

FDC 5/279 /I52/ FI/T INDIANAPOLIS-TERRY, INDIANAPOLIS, IN. ILS RWY 36 AMDT 1..LOC/GS UNUSBL MM INBND.

Skyway

ARPT NAME CHANGED TO GREENWOOD BOAC. (11/86)

JEFFERSONVILLE

Clark County

FDC 6/3101 /JVY/FI/T CLARK COUNTY, JEFFERSONVILLE, IN..VOR RWY 18 ORIG..SI MINS NA AT NIGHT.

PLYMOUTH

Plymouth Muni

FDC 6/2659 /C65/ FI/T PLYMOUTH MUNI, PLYMOUTH, IN. VOR RWY 10 AMDT 9. DME RQRD.

SOUTH BEND

Michiana Regional

RWY 18/36 NO LONGER CLSD NIGHTS. (10/86)

FDC 6/2705 /SBN/ FI/T MICHIANA REGIONAL, SOUTH BEND IN. NDB RWY 27 AMDT 25..ILS RWY 27 AMDT 31..RADAR RWY 27 AMDT 6..CHANGE MISSED APPROACH TO READ CLIMB TO 1500 THEN CLIMBING LEFT TURN TO 3000 DIRECT TO GSH VORTAC AND HOLD. HOLD E, LT, 272 INBOUND.

TERRE HAUTE

Hulman Regional

FDC 6/1066 /HUF/ FI/T HULMAN REGIONAL..TERRE HAUTE IN. LOC BC RWY 23 AMDT 17. PROC NA.

VALPARAISO

Porter County Muni

RWY 17/35 NOW 1797 FT BY 50 FT. (11/86)

FDC 6/3107 VPZ/FI/T PORTER COUNTY MUNI, VALPARAISO, IN..TAKEOFF MINIMUMS/DEPARTURE PROCEDURES. TKOF MINS..RWYS 9, 17, 27, 35..STANDARD. IFR DEPARTURE PROC. RWY 27..CLIMB TO 1000 FT BEFORE TURNING SOUTH. RWY 17..CLIMB TO 1000 FT BEFORE TURNING WEST. CRANE 120 FT AGL SW OF AIRPORT.

FDC 5/2547 /VPZ/ FI/T PORTER COUNTY MUNI, VALPARAISO, IN. NDB RWY 27 AMDT 4, ILS RWY 27 ORIG. RNAV RWY 9 AMDT 1: ACTIVATE MALS RWY 27 AND HIRL RWY 9-27 - CTAF.

WINCHESTER

Randolph County

FDC 6/2386 /I22/ FI/T RANDOLPH COUNTY, WINCHESTER, IN. NDB RWY 25 AMDT 3. S-25 AND CIRCLING MDA 1760 HAT/HAA 642 CATS A/B/C VIS CATS A/B 1, CAT C 1 3/4. USE DAYTON ALSTG. VOR-A AMDT 7 CIRCLING MDA CAT A 1720/HAA 602 CATS B/C MDA 1740/HAA 622 VIS CAT A 1, CAT B 1 1/4, CAT C 1 3/4. USE DAYTON ALSTG.

IOWA

AMANA

Amana

RWY E/W CHANGED TO 08/26, 2750 FT BY 110 FT. (10/86)

AMES

Ames Muni

RWY 01/19 NOW 4600 FT BY 100 FT, CONC, MIRL. (10/86)

ACTIVATE MIRLS RWYS 01/19 & 13/31 126.0.(10/86)

FDC 5/105 /AMW/ FI/T AMES MUNI AMES IA. LOC RWY 31 AMDT 4 NDB RWY 31 AMDT 8 CAT A/B SI-31 VIS 1 MILE. ADD NOTE..INOPERATIVE TABLE DOES NOT APPLY TO MALS. VOR RWY 31 AMDT 7 CAT A SI-31 VIS 1 MILE. ADD NOTE..INOPERATIVE TABLE DOES NOT APPLY TO MALS.

BOONE

Boone Muni

RWY 14 REIL CMSND.(10/86)

ACTIVATE REIL RWYS 14 & 32 123.0. (10/86)

BURLINGTON

Burlington Muni

FDC 6/3025 /BRL/FI/T BURLINGTON MUNI, BURLINGTON, IA. ILS RWY 36 AMDT 6; NDB RWY 36 AMDT 6; VOR RWY 30 AMDT 9; VOR/DME RWY 12 AMDT 2. DELETE BURLINGTON FSS PROC NOTE. OBTAIN LOCAL ALTM ON CTAF. VOR/DME RWY 12 AMDT 2; VOR RWY 30 AMDT 9. SI MINS NA AT NIGHT.

FDC 6/3021 /BRL/FI/T BURLINGTON MUNI BURLINGTON IA. IFR DEPARTURE PROCEDURE: RWY 30-CLIMB RUNWAY HEADING TO 1200 FT BEFORE TURNING NORTH..RWY 36-CLIMB RUNWAY HEADING TO 1200 FT BEFORE TURNING WEST.

FDC 6/2323 BRL/BURLINGTON MUNI/BURLINGTON,IA. ILS RWY 36 AMDT 6..VOR RWY 30 AMDT 9..VOR/DME RWY 12 AMDT 2..CIRCLING CAT D MDA 1380/HAA 682 VIS 2 1/4. ALTN MINS..CAT D 800-2 1/4. NDB RWY 36 AMDT 6. CIRCLING CAT D MDA 1380/HAA 682 VIS 2 1/4.

CEDAR RAPIDS

Cedar Rapids Muni

FDC 6/3023 /CID/FI/T CEDAR RAPIDS MUNI..CEDAR RAPIDS IA. IFR DEPARTURE PROCEDURE: RWY 9 - WHEN VISIBILITY BELOW 3 MILES AND/OR CEILING BELOW 500 FT..CLIMB RUNWAY HEADING TO 1300 FT BEFORE TURNING NORTH.

CHARLES CITY

Charles City Muni

ACTIVATE MIRL RWY 12/30 122.8. (10/86)

IOWA

COUNCIL BLUFFS

Council Bluffs Muni

RWY 17/35 NOW OPEN. (10/86)

FORT DODGE

Fort Dodge Muni

FDC 6/2687 /FOD/ FI/T FORT DODGE MUNI, FORT DODGE, IA..ILS RWY 6 AMDT 5..ALTERNATE MINS NA.

FDC 6/26 /FOD/ FI/T FORT DODGE MUNI, FORT DODGE, IA. ILS RWY 6, AMDT 5, ALTERNATE MINIMUMS NA.

IOWA CITY

Iowa City Muni

RWY 24 THR DSPLCD 150 FT. RWYS 30 & 35 THR NO LONGER DSPLCD. (10/86)

IOWA FALLS

Iowa Falls Muni

ACTIVATE VASI RWY 13 122.8. (10/86)

JEFFERSON

Jefferson Muni

RWY 18/36 NOW 2000 FT BY 200 FT. (10/86)

KNOXVILLE

Knoxville

RWYS 15 & 33 REIL DCMSND. (10/86)

MAQUOKETA

Maquoketa Muni

FDC 5/2933 /C[illegible]3/ FI/T MAQUOKETA MUNI MAQUOKETA IA. NDB RWY 15 AMDT 1 S-15 MDA 1660/HAT 890 ALL CATS VIS CATS A/B 1 1/4 CAT C 2 3/4 CAT D 3. CIRCLING MDA 1660/ HAA 890 ALL CATS VIS CATS A/B 1 1/4 CAT C 2 3/4 CAT D 3.

MUSCATINE

Muscatine Muni

FDC 5/2622 /MUT/ FI/T MUSCATINE MUNI MUSCATINE IA. VOR RWY 23 AMDT 4 DME MINS SI MDA 920/HAT 375 ALL CATS.

NEVADA

Nevada Muni

FACILITY ABANDONED. (11/86)

NEWTON

Newton Muni

RWY 06/24 NOW 2600 FT BY 150 FT. (10/86)

PELLA

Pella Muni

RWYS 16 & 34 VASI CERTIFIED. (10/86)

SIBLEY

Sibley Muni

ACTIVATE LIRL RWY 17/35 122.8. (10/86)

IOWA

SIOUX CITY

Salix NDB

(SU) Controlling FSS OLU.(10/86)

Sioux City Muni

FDC 5/2927 /SUX/ FI/T SIOUX CITY MUNI, SIOUX CITY, IA. VOR/DME RWY 13, AMDT 17: VOR RWY 31, AMDT 25, RNAV RWY 17, AMDT 3, RNAV RWY 35, AMDT 6, NA. NDB RWY 13, AMDT 15, SUX VORTAC TRANSITION ROUTE TO OI LOM NA. MISSED APPROACH CLIMB TO 2900 DIRECT TO SU LOM AND HOLD SE, 312 INBOUND, RT, 1 MINUTE. NDB RWY 31, AMDT 23 MAP CLIMBING LEFT TURN TO 2900 DIRECT SU LOM AND HOLD SE, 312 INBOUND, RT, 1 MINUTE. ILS RWY 13, AMDT 1, SUX VORTAC TRANSITION TO OI LOM NA, CW AND CCW 19 DME ARC INITIAL SEGMENTS NA. MISSED APPROACH CLIMB TO 2900 DIRECT SU LOM AND HOLD, SE, 312 INBOUND, RT, 1 MINUTE. ILS RWY 31, AMDT 24, MAP CLIMBING LT TO 2900 DIRECT SU LOM AND HOLD SE, 312 INBOUND, RT, 1 MINUTE. TACAN PROCEDURES UNCHANGED.

SPENCER

Spencer Muni

ACTIVATE MIRL RWYS 12/30 & 18/36 123.0.

FDC 6/2436 /SPW/ FI/T SPENCER MUNI SPENCER IA. VOR RWY 12 ORIG VOR/DME RWY 30 ORIG AND VOR RWY 30 ORIG. PROC NA.

STORM LAKE

Storm Lake Muni

ACTIVATE REIL RWYS 17 & 35 122.7. (11/86)

KANSAS

CHANUTE

Chanute Martin Johnson

RWY 18/36 NOW 4238 FT BY 75 FT. (11/86)

DODGE CITY

Dodge City Muni

ACTIVATE MIRL RWY 14/32 & REIL RWYS 14 & 32 123.65. (10/86)

EMPORIA

Emporia FSS

FREQ 122.2 DCMSND. (10/86)

Emporia RCO

FSS ICT, OPERATIONAL HRS CONTINUOUS, FREQ 122.3 CMSND. (10/86)

FORT LEAVENWORTH

Fort Leavenworth RCO

ICT FSS, OPERATIONAL HRS CONTINUOUS, FREQ 122.35 CMSND. (10/86)

FREQ 255.4 CMSND. (10/86)

GREAT BEND

Great Bend Muni

ACTIVATE VASI & MALS RWY 35 122.8. (11/86)

KANSAS

LAWRENCE

Lawrence Muni

FDC 6/2495 /SLA/ FI/T LAWRENCE MUNI LAWRENCE, KS. NDB-B MSA FROM LWC NDB 3100.

ST JOHN

Schulz Field

FACILITY ABANDONED. (11/86)

SALINA

Salina Muni

RWY 04/22 NOW 3630 FT BY 75 FT. (10/86)

ARPT CLOSED TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS 2300-0600 LCL MON-FRI; 2300 LCL FRI-0800 LCL SAT; 1600 LCL SAT-0800 LCL SUN; 2400 LCL SUN-0600 LCL MON; EXCEPT 24 HOURS PPR CALL 913-827-3914. CFR SERVICE FOR NON-AIR CARRIER INCLUDING MILITARY AVAILABLE 0600-2300 LCL WEEKDAY; 0800-1600 LCL SAT; 0800-2400 LCL SUN; OTHER TIMES WITH 24 HOUR PPR CALL 913-827-3914. (10/86)

TOPEKA

Philip Billard Muni

FDC 6/1417 /TOP/ FI/T PHILLIPS BILLARD MUNI, TOPEKA KS. ILS RWY 13 AMDT 29..THE INITIAL APPROACH VIA TOP VORTAC R-071. COUNTERCLOCKWISE. 12 DME ARC. 2800 FEET NA. THE ONLY TRANSITION TO THE ILS LOCALIZER COURSE IS VIA THE BILOY LOM. BEARING 308 OUTBOUND PROCEDURE TURN.

Topeka RCO

FREQ 255.40 CMSND. (10/86)

WELLINGTON

Wellington Muni

FDC 6/2162 /H77/ FI/T WELLINGTON MUNI WELLINGTON KS.. NDB RWY 17 AMDT 2..SI MDA 1880/HAT 607 ALL CATS. VIS CAT C 1 3/4, CAT D 2. CIRCLING MDA 1880/HAA 607 ALL CATS. VIS CAT C 1 3/4, CAT D 2. OBTAIN LOCAL ALSTG ON CTAF. WHEN NOT AVAILABLE USE WICHITA ALSTG AND INCREASE ALL MDA/S 80 FT. VOR/DME RWY 17 ORIG..SI MDA 1780/HAT 507 ALL CATS. VIS CAT B 1, CAT D 1 1/2. CIRCLING MDA CATS A/B/C 1780/HAA 507, CAT D MDA 1840/HAA 567. VIS CAT B 1, CAT D 1 1/2. CAT D MDA 1840/HAA 567. VIS CAT B 1, CAT D 1 1/2. OBTAIN LOCAL ALSTG ON CTAF. WHEN NOT AVAILABLE USE WICHITA ALSTG AND INCREASE ALL MDA/S 80 FT.

WICHITA

Wichita Mid-Continent

FDC 5/2893 /ICT/ FI/T WICHITA MID-CONTINENT WICHITA KS. LOC BC RWY 19L AMDT 13. DISREGARD GLIDE SLOPE INDICATIONS.

KENTUCKY

ASHLAND

Ashland-Boyd County

FDC 6/2191 /I28/ FI/T ASHLAND-BOYD COUNTY, ASHLAND KY. TKOF MINS RWY 10/28..600-3 OR STANDARD WITH A MIN CLIMB OF 335 FEET PER NM TO 1100. IFR DEP PRC: RWY 10 - CLIMBING LT TO 1300 VIA HDG 060 BEFORE PROCEEDING ON CRS.

COVINGTON/CINCINNATI

Greater Cincinnati Intl

FDC 6/2996 /CVG/FI/T GREATER CINCINNATI INTL, COVINGTON, KY. ILS RWY 36 AMDT 31. DSTC TO THR FROM 150 HAT 2038, FROM 100 HAT 1084.

FDC 6/2995 FI/T /CVG/GREATER CINCINNATI INTL, COVINGTON KY. ILS RWY 9R AMDT 10; ILS RWY 18 AMDT 14; ILS RWY 27L AMDT 8: ILS RWY 36 AMDT 31; RADAR-1 AMDT 20. CIRCLING MDA 1360/HAA 469 CAT A. DAYLIGHT HRS ONLY. 1057 CRANE 867 FT NORTH OF RWY 27R THR.

GREENVILLE

Muhlenberg County

RWY 23 REIL & VASI RTS. MIRL RWY 05/23 AND VASI & REIL RWYS 05 & 23 OPERATE DUSK-2300 LCL; ACTIVATE AFTER 2300 LCL 123.0.(10/86)

LEXINGTON

Blue Grass

RWY 22 VASI DCMSND. (11/86)

LOUISVILLE

Bowman Field

FDC 6/1815 /LOU/ FI/T BOWMAN FIELD, LOUISVILLE, KY. VOR RWY 24 AMDT 1. DUAL VOR MINS, SI MDA 1080/HAT 534 ALL CATS. VIS 1 1/2 CAT C, 1 3/4 CAT D. CIRCLING MDA 1140/HAA 594 ALL CATS. NDB RWY 32 AMDT 10/VOR RWY 1 AMDT 1 VOR/NDB MINS/ VOR RWY 14 AMDT 6/VOR RWY 32 AMDT 11 VOR/NDB OR DME MINS. CIRCLING MDA 1140/HAA 594 ALL CATS. TKOF MINS..RWY 1 AND RWY 6 400-1 OR STANDARD WITH MIN CLIMB OF 320 FEET PWE NM TO 1000.

Standiford Field

FDC 5/2292 /SDF/STANDIFORD FIELD, LOUISVILLE, KY. ILS RWY 1 AMDT 7 AUTOPILOT COUPLED APPROACHES NA BELOW 880 MSL. CAT TWO APPROACHES NA.

LOUISIANA

ALEXANDRIA

Alexandria RCO

LAT 312130N LONG 0921746W, FSS DRI. EFFECTIVE 18 DEC 86 FREQ 122.2 DCMSND. (11/86)

Alexandria RCO

COLOCATED WITH ALEXANDIRA VORTAC, DCMSND EFFECTIVE 18 DEC 86. (11/86)

Alexandria RCO

LAT 311523.2N LONG 0923002.0W, FSS DRI, OPERATIONAL HRS CONTINUOUS, FREQS 122.55, 121.5, 243.0 AND 255.4 CMSND EFFECTIVE 18 DEC 86. (11/86)

Alexandria VORTAC

(AEX) EFFECTIVE 18 DEC 86 CONTROLLING FSS DRI. (11/86)

Esler VOR/DME

(ESF) EFFECTIVE 18 DEC 86 CONTROLLING FSS DRI. (11/86)

BASTROP

Morehouse Memorial

REIL RWY 34 RTS. MIRL RWY 16/34 PRESET LOW, INCREASE INTSTY 122.8 5 TIMES FOR MEDIUM & 7 TIMES FOR HIGH. ACTIVATE REIL RWY 34 122.8. (11/86)

BATON ROUGE

Baton Rouge Metro, Ryan Field

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS 2400-0600 LCL EXCEPT 24 HOURS PPR CALL 504-355-2068; 0333. CFR SERVICE FOR NON-AIR CARRIER OPERATIONS 2400-0600 LCL CALL CTAF OR UNICOM. (11/86)

FDC 4/2344 /BTR/ FI/T BATON ROUGE METROPOLITAN, RYAN FIELD, BATON ROUGE, LA. ILS RWY 22, AMDT 3, ALTN MINS NA WHEN CONTROL TOWER NOT IN OPERATION.

BOGALUSA

George R Carr Memorial Air Fld

RWYS 18 & 36 VASI CHANGED TO SAVASI. (10/86)

MIRL RWY 18/36 PRESET LOW, TO INCREASE INTENSITY KEY 122.8 FIVE TIMES MEDIUM, SEVEN TIMES HIGH. ACTIVATE REIL RWY 18 122.8. (10/86)

COVINGTON

Greater St. Tammany

MIRL RWY 17/35 PRESET LOW, INCREASE INTSTY 122.8 5 TIMES FOR MEDIUM, 7 TIMES FOR HIGH. (11/86)

DE QUINCY

De Quincy NDB

(DQU) EFFECTIVE 18 DEC 86 CONTROLLING FSS DRI. (11/86)

DE RIDDER

Beauregard Parish

RWY 36 REIL RTS. ACTIVATE REIL RWY 36 122.8.(10/86)

MIRL RWY 18/36 PRESET LOW, TO INCREASE INTENSITY KEY 122.8 FIVE TIMES FOR MEDIUM, SEVEN TIMES HIGH.(10/86)

Parish NDB

(DSR) CONTROLLING FSS DRI. (11/86)

EUNICE

Eunice

MIRL RWY 16/34 PRESET LOW, TO INCREASE INTENSITY KEY 122.9 THREE TIMES FOR MEDIUM, FIVE TIMES HIGH. ACTIVATE REIL RWY 34 122.9.(10/86)

FARMERVILLE

Farmerville

REIL RWY 34 OTS INDEFLY. (10/86)

FDC 6/3088 /F87/FI/T FARMERVILLE..FARMERVILLE LA. VOR/DME-A AMDT 1. PROC NA.

FORT POLK

Gator NDB

(GUV) EFFECTIVE 18 DEC 86 CONTROLLING FSS DRI. (11/86)

North Fan Marker

EFFECTIVE 18 DEC 86 CONTROLLING FSS DRI. (11/86)

Polk VOR

(FXU) CONTROLLING FSS DRI. (11/86)

GRAND ISLE

Grand Isle

FDC 4/2113 /GNI/ FI/T GRAND ISLE, GRAND ISLE LA. NDB-B AMDT 6. CIRCLING MDA 680, HAA 680 CATS A/B/C VIS CAT C 2. VOR-A AMDT 5 MIN ALT LEV R-046/5 DME 780. VOR CIRCLING MDA 760 HAA 760 CATS A/B/C, VIS CAT B 11/4 CAT C 21/4. DME MINIMA. CIRCLING MDA 600, HAA 600 CATS A/B/C. VOR/DME-C AMDT 4, CIRCLING MDA 600, HAA 600, CATS A/B/C. CHANGE NOTES FOR ALL PROCS TO READ: USE LEEVILLE ALSTG, WHEN NOT AVBL USE NAS NEW ORLEANS ALSTG AND INCREASE ALL MDAS 100 FEET.

HAMMOND

Hammond Muni

FDC 4/1526 /0R9/ FI/T HAMMOND MUNI HAMMOND LA. ILS RWY 18 ORIG SI ILS DH 429/HAT 385 ALL CATS VIS CAT D 1 1/4. CIRCLING MDA 640/HAA 596 CATS A/B/C. ALTN MISSED APCH WHEN DIRECTED BY ATC CLIMBING LEFT TURN TO 2000 VIA PCU R-262 TO MACAW INT. VOR RWY 31 AMDT 1 CIRCLING MDA 640/HAA 596 CATS A/B/C. DELETE NOTE..STRAIGHT-IN MIN NA AT NIGHT. ILS RWY 18 ORIG/ NDB RWY 18 ORIG/VOR RWY 31 AMDT 1/VOR RWY 18 ORIG ADD NOTE..ACTIVATE MIRL RWYS 13-31/18-36 REIL RWY 31 AND MALSR RWY 18 CTAF/UNICOM.

JENNINGS

Jennings

RWY 08/26 NOW OPEN. (10/86)

FDC 6/478 /3R7/ FI/T JENNINGS JENNINGS LA. TKOF MINS RWY 4, 31 STANDARD. RWY 13, 22, 8, 26 300-1 OR STANDARD WITH MINIMUM CLIMB OF 225 FEET PER NM TO 300 RWY 17, 35 NA.

Jennings NDB

(JNZ) EFFECTIVE 18 DEC 86 CONTROLLING FSS DRI. (11/86)

LAFAYETTE

LaFayette Regional

FDC 6/2210 /LFT/ FI/T LAFAYETTE REGIONAL LAFAYETTE, LA. NDB RWY 21 AMDT 1. ALTERNATE MINIMUMS AUTHORIZED WHEN TOWER CLOSED.

FDC 6/2049 /LFT/ FI/T LAFAYETTE REGIONAL LAFAYETTE LA. ILS RWY 21 AMDT 1..S-ILS-21 DH 288/HAT 250 ALL CATS. VIS 1 ALL CATS. S-LOC-21 VIS 1 ALL CATS. INOP TABLE DOES NOT APPLY.

FDC 5/2876 /LFT/ FI/T LAFAYETTE REGIONAL LAFAYETTE LA. NDB RWY 10 AMDT 1..NDB RWY 21 AMDT 1..ILS RWY 21 AMDT 1... STANDARD ALTERNATE MINS AUTHORIZED.

LAKE CHARLES

Lake Charles FSS

DCMSND EFFECTIVE 30 JAN 87. (11/86)

Lake Charles Muni

FDC 5/2148 /LCH/ FI/T LAKE CHARLES MUNI, LAKE CHARLES LA. LOC BC RWY 33 AMDT 16. TERMINAL ROUTE

LCH VORTAC TO BROWN INT NA. ADD NOTE: RADAR REQUIRED.

Lake Charles RCO

LFSS DRI, OPERATIONAL HOURS CONTINUOUS, FREQS 121.5, 122.3, 243.0 AND 255.4 CMSND EFFECTIVE 18 DEC 86. (11/86)

Lake Charles VORTAC

(LCH) CONTROLLING FSS DRI. (11/86)

LEEVILLE

Leeville Heliport

FACILITY ABANDONED. (11/86)

MARKSVILLE

Marksville Muni

FDC 5/1874 /LA26/MARKSVILLE MUNI/MARKSVILLE/LA. NDB RWY 4 ORIG..PROCEDURE NA SATURDAYS/SUNDAYS/ HOLIDAYS AND FROM 6 PM TO 7 AM LOCAL TIME MONDAY THROUGH FRIDAY.

Marksville NDB

(MKV) EFFECTIVE 18 DEC 86 CONTROLLING FSS DRI. (11/86)

MINDEN

Minden-Webster

FDC 6/3136 /F24/FI/T MINDEN-WEBSTER..MINDEN LA. VOR/ DME-A AMDT 2. CIRCLING MDA 1100/HAA 810..VIS 2 1/4 CAT C..2 1/2 CAT D.

MONROE

Monroe Regional

FDC 6/1250 /MLU/ FI/T MONROE REGIONAL, MONROE, LA. VOR RWY 22 AMDT 2. S-22 MDA 720/HAT 642 ALL CATS. VIS 1 3/4 CAT C. 2 CAT D. CIRCLING MDA 720/HAA 641 ALL CATS. VIS 1 3/4 CAT C, 2 CAT D.

FDC 6/845 /MLU/ FI/T MONROE REGIONAL, MONROE, LA. ILS RWY 22 AMDT 1. ADDD TERMINAL ROUTE FROM R-259 MLU VORTAC CLKWS /IAF/ TO I-MZR LOC /NOPT/..COURSE AND DISTANCE..12 DME ARC /MLU R-031 LR/..ALT 2000.

FDC 4/3223 /MLU/ FI/T MONROE REGIONAL, MONROE, LA. ILS RWY 22, AMDT 1, VOR RWY 22, AMDT 2, VOR/DME RWY 22, AMDT 7. CHANGE MISSED APPROACH TO..CLIMB TO 3000 VIA MLU R-218 TO TYRON INT/ 12 DME AND HOLD.

NATCHITOCHES

Natchitoches Muni

MIRL RWY 16/34 PRESET LOW INTENSITY; TO INCREASE INTENSITY KEY 122.8 FIVE TIMES MEDIUM, SEVEN TIMES HIGH.(10/86)

NEW ORLEANS

Lakefront

RWY 18R/36L NOW 6700 FT BY 150 FT. RWY 18R THR DSPLCD 250 FT, RWY 36L THR DSPLCD 650 FT. (11/86)

PORT SULPHUR

Port Sulphur Seaplane Base

FDC 4/1936 /5R9/ FI/T PORT SULPHUR SEAPLANE BASE, PORT SULPHUR, LA. VOR/DME-A, AMDT 3, MDA 640, HAA 640 CAT A AND B. CHANGE NOTE TO READ..USE BOOTHVILLE ALTIMETER SETTING, WHEN NOT AVAILABLE USE NAS NEW ORLEANS ALTIMETER SETTING AND INCREASE ALL MDA 60 FT. VOR/DME-B AMDT 2 MDA 620, HAA 620 CAT A AND B. CHANGE NOTE TO READ..USE BOOTHVILLE ALTIMETER SETTING, WHEN NOT AVAILABLE USE NAS NEW ORLEANS ALTIMETER SETTING AND INCREASE ALL MDA 60 FT.

RAYVILLE

Rayville Muni

RWY 18/36 NOW 3700 FT BY 50 FT. RWY 36 THR NO LONGER DSPLCD. MIRL RWY 18/36 PRESET LOW, INCREASE INTSTY 122.8 5 TIMES FOR MEDIUM, 7 TIMES FOR HIGH. ACTIVATE REIL RWYS 18 & 36 122.8. (11/86)

SHREVEPORT

Shreveport Downtown

RWY 05 THR NOW DSPLCD 292 FT. (10/86)

Shreveport Regional

FDC 6/515 /SHV/ FI/T SHREVEPORT REGIONAL, SHREVEPORT, LA. ILS RWY 14 AMDT 19, ILS RWY 14 CAT II AMDT 19. ADD TO PROFILE VIEW ONGOO INT, MINIMUM ALTITUDE 2500.

SLIDELL

Slidell

RWY 35 VASI OTS INDEFLY. (10/86)

MIRL 17/35 PRESET LOW; TO INCREASE INTENSITY KEY 122.8 FIVE TIMES FOR MEDIUM, SEVEN TIMES HIGH.(10/86)

THIBODAUX

Thibodaux Muni

MIRL RWY 08/26 PRESET LOW, INCREASE INTSTY KEY 122.8 5 TIMES FOR MEDIUM AND 7 TIMES FOR HIGH. (11/86)

WELSH

Welsh

FDC 5/993 /6R1/WELSH, WELSH, LA. VOR/DME RWY 6 AMDT 1.. CIRCLING MDA 580/HAA 561 CATS A/B.

MAINE

BANGOR

Bangor Intl

FDC 6/328 /BGR/ FI/T BANGOR INTL, BANGOR, ME VOR-A AMDT 1, VOR/DME RWY 15 AMDT 2..MSA FROM BGR VORTAC 360 CLKWS 090 3100. ILS RWY 33 AMDT 9, NDB RWY 33 AMDT 4. MSA FROM BG/LOM 360 CLKWS 180 3100.

BIDDEFORD

Biddeford Muni

FDC 5/820 /B19/BIDDEFORD MUNI, BIDDEFORD, ME. VOR-A AMDT 4, HOLDING SE ON ENE R-266 NA RADAR REQUIRED. MISSED APPROACH CLIMB TO 800 THEN CLIMBING LEFT TURN TO 2300 DIRECT ENE VORTAC AND HOLD E, LT, 262 INBOUND.

CARIBOU

Caribou Muni

RWY 29 THR DSPLCD 390 FT.(10/86)

MAINE

FDC 6/3174 /CAR/ FI/T CARIBOU MUNI CARIBOU ME. RADAR-1 AMDT 2. ASR RWY 11 AND ASR RWY 29 PROC NA.

ELIOT

Littlebrook Airpark

FDC 6/583 /3B4/ FI/T LITTLEBROOK AIRPARK ELIOT ME. RADAR-1 AMDT 1 S-30 MDA 520 HAT 390 CAT A/B.

FORT KENT

Fort Kent Muni

ARPT CLSD INDEFLY. (10/86)

GREENVILLE

Greenville Muni

FDC 6/2447 /3B1/ FI/T GREENVILLE MUNI GREENVILLE ME. NDB RWY 14 AMDT 2 TERMINAL ROUTE AUG VORTAC TO XQA NDB NA. GREENVILLE ALTIMETER SETTING MINIMUNS NA.

Greenville Seaplane Base

FDC 6/2446 /52B/ FI/T GREENVILLE SEAPLANE BASE GREENVILLE ME. NDB-A AMDT 2 TERMINAL ROUTE AUG VORTAC TO XQA NDB NA. GREENVILLE ALTIMETER SETTING MINIMUMS NA.

LINCOLN

Lincoln Regional

FDC 6/2065 /64B/ FI/T LINCOLN REGIONAL, LINCOLN, ME. VOR/DME-A ORIG. MDA 1420/HAA 1212 ALL CATS. TKOF MINS RWY 17, 800-2.

PHILLIPS

Raymond

FACILITY ABANDONED. (11/86)

RANGELEY

Rangeley Muni

FDC 6/2950 /8B0/ FI/P RANGELEY MUNI, RANGELEY ME. NDB-A ORIG. TRML ROUTES BML VOR/DME TO RQM NDB AND HXK NDB TO RQM NDB ALT 4800. TRML ROUTE AUG VORTAC TO RQM NDB ALT 600. THIS IS NDB-A AMDT 1.

Rangeley NDB

(RQM) UNUSABLE BYD 18 NM.(10/86)

WATERVILLE

Waterville Robert Lafleur

FDC 6/3133 /WVL/FI/T WATERVILLE ROBERT LAGLEUR WATERVILLE ME. VOR/DME RWY 5 AMDT 5..S-5 HAT 452 ALL CATS. 492 WHEN USING AUGUSTA ALTIMETER SETTING MINIMUMS. MISSED APPROACH POINT AUG R-040/13.3 DME. DISTANCE FAF TO MAP 5.3.

MARYLAND

BALTIMORE

Baltimore-Washington Intl

RWY 15L CLSD TO LANDING; RWY 33R CLSD TO TKOF 2200-0700 LCL. (10/86)

FDC 6/3157 /BWI/FI/T BALTIMORE-WASHINGTON INTL/ BALTIMORE/MD. RADAR-1 AMDT 9. ASR RWY 15R MDA 660/ HAT 520 ALL CATS. VIS RVR 5000 CAT C. RVR 6000 CAT D.

FDC 6/795 /BWI/ FI/T BALTIMORE-WASHINGTON INTL BALTIMORE, MD. RADAR-1 AMDT 9 ASR RWY 22. SI MDA 640 /HAT 499 ALL CATS.

Martin State ATCT

FREQ 116.6T USED FOR ATIS DCMSND. (11/86)

CAMBRIDGE

Cambridge-Dorchester

FDC 6/465 /CGE/ FI/T CAMBRIDGE-DORCHESTER..CAMBRIDGE MD. VOR-A AMDT 4. PROC NA.

LEONARDTOWN

St Marys County

FDC 6/2769 /2W6/ FI/T ST. MARYS COUNTY, LEONARDTOWN MD. VOR RWY 11 AMDT 2..CIRCLING MDA 620/HAA 478 CAT B. VOR RWY 29 AMDT 3...SI MDA 580/HAT 438 CATS A/B. CIRCLING MDA 580/HAA 438 CAT A. MDA 620/ HAA 178 CAT B.

NOTTINGHAM

Nottingham VORTAC

(OTT) DME UNUSABLE WITHIN 30 NM BELOW 4500 FEET.(10/86)

SALISBURY

Salisbury-Wicomico Co Regional

FDC 5/2673 /SBY/ FI/T SALISBURY-WICOMICO CO REGIONAL SALISBURY MD. LOC BC RWY 14 AMDT 2. PROC NA.

MASSACHUSETTS

BARRE /BARRE PLAINS/

Barre/Hiller

ARPT NAME CHANGED TO TANNER-HILLER. (10/86)

BEDFORD

Laurence G. Hanscom Fld

RWY 29 REIL DCMSND. (11/86)

FDC 6/1376 /BED/ FI/T LAURENCE G. HANSCOM FLD BEDFORD MA ILS RWY 29 AMDT 1..PROC NA.

FDC 5/2197 /BED/ FI/T LAURENCE G HANSCOM FLD, BEDFORD, MA. ILS RWY 11 AMDT 20/VOR RWY 23 AMDT 7/ NDB RWY 11 AMDT 17. CIRCLING MDA 700/HAA 567 CAT C/ MDA 780/HAA 647 CAT D.

FDC 5/95 /BED/ FI/T LAURENCE G. HANSCOM FLD, BEDFORD, MA. NDB RWY 11 AMDT 17. TRML ROUTE ANNOT INT TO BE LOM ALT 2400. PT REQUIRED.

FDC 4/2679 /BED/ FI/T LAURENCE G. HANSCOM FLD/ BEDFORD/MA. NDB RWY 29 AMDT 3 MDA ALL CATS 800/HAT 672/HAA 667. VIS CAT C 2 CAT D 2 1/4.

BOSTON

General Edward Lawrence Logan Intl

FDC 6/2122 /BOS/ FI/T GENERAL EDWARD LAWRENCE LOGAN INTL AIRPORT, BOSTON, MA. ILS RWY 22L, AMDT 2. S-LOC-22L MDA ALL CATS 500 VIS CATS A/B/C RVR 6000 CAT D 1 1/2. HAT ALL CATS 484.

FDC 5/2736 /BOS/ FI/T GENERAL EDWARD LAWRENCE LOGAN INTL AIRPORT, BOSTON MA. NDB RWY 4R AMDT 21..S-4R ALL CATS MDA 1060 HAT 1042, VIS CAT A RVR 4000, CAT B RVR 5000, CAT C 2 1/2, CAT D 2 3/4. CIRCLING ALL CATS MDA 1060 HAA 1040, VIS CAT A 1 1/4, CAT B 1 1/2, CAT C/D 3. CAT C/D CIRCLING NA W RWYS 4L/15R. NDB RWY 22L AMDT 8..S-22L ALL CATS MDA 880 HAT 864 VIS CAT A RVR 5000, CAT B RVR 6000, CAT C 2 CAT D 2 1/2. CIRCLING ALL CATS MDA 880 HAA 860 VIS CAT A 1, CAT B 1 1/4, CAT C 2 1/2, CAT D 2 3/4, CAT C/D CIRCLING NA W RWYS 4L/15R. ILS RWY 4R AMDT 4, ILS RWY 22L AMDT 2, ILS/DME RWY 15R AMDT 9, ILS/DME RWY 27 AMDT 1, ILS/DME RWY 33L AMDT 20, VOR/DME RWY 15R AMDT 15, VOR/DME RWY 27 AMDT 1, VOR/DME RWY 33L ADMT 18, CAT C/D CIRCLING NA W RWYS 4L/15R.

FDC 4/1542 /BOS/ FI/T GENERAL EDWARD LAWRENCE LOGAN INTL, BOSTON MA. VOR/DME RWY 15R AMDT 15, VOR/DME RWY 27 AMDT 1, VOR RWY 33L AMDT 18 PROCS NA.

CHATHAM

Chatham Muni

FDC 6/677 /OB6/ FI/T CHATHAM MUNI CHATHAM MA. VOR-A AMDT 8. MISSED APCH: CLIMBING LT TO 2000 VIA HDG 250 AND HYA R-113 TO HYA VORTAC AND HOLD.

FITCHBURG

Fitchburg Muni

FDC 6/1204 /FIT/ FI/T FITCHBURG MUNI FITCHBURG MA. NDB RWY 20 ORIG AND NDB RWY 32 ORIG CHANGE FIT NDB FREQUENCY TO 365 KHZ. NDB RWY 32 ORIG STRAIGHT IN MINIMUMS NA.

GARDNER

Gardner Muni

ACTIVATE MIRL RWY 18/36 122.8. (11/86)

GREAT BARRINGTON

Great Barrington

FDC 6/1939 /GBR/ FI/T GREAT BARRINGTON, GREAT BARRINGTON, MA. NDB-A AMDT 3. DME RQRD FOR STELA INT AND MOLDS INT. TRML ROUTE HIDAL INT TO GBR NDB NA.

HYANNIS

Barnstable Muni-Boardman/Polando Field

FDC 6/773 /HYA/ FI/T BARNSTABLE MUNI-BOARDMAN/ POLANDO FIELD. HYANNIS MA. VOR RWY 24 AMDT 8..PROC NA. VOR RWY 6 AMDT 3.. MISSED APCH: CLIMB TO 1700 VIA RWY HEADING. THEN DIRECT HYA VORTAC AND HOLD.

LAWRENCE

Lawrence Muni

RWY 05/23 NOW OPEN. (10/86)

MARSHFIELD

Marshfield

FDC 5/492 /3B2/MARSHFIELD, MARSHFIELD, MA. NDB RWY 6 ORIG. TRML ROUTE HYANNIS /HYA/ VORTAC TO MARSHFIELD /IMR/ NDB NA.

NANTUCKET

Nantucket Memorial

FDC 6/237 /ACK/ FI/T NANTUCKET MEMORIAL, NANTUCKET, MA. NDB RWY 24, AMDT 7 CHANGE CTLZ NOTES TO: WHEN CONTROL TOWER CLOSED (A) USE OTIS AFB ALTIMETER SETTING. (B) INCREASE ALL MDAS 120 FEET. (C) S-24 CATS A AND B VIS 3/4, CAT C VIS 1 1/4, CAT D VIS 1 1/2. (D) ALS SEQUENCED FLASHING LIGHTS INOP.

FDC 6/236 /ACK/ FI/T NANTUCKET MEMORIAL, NANTUCKET, MA. ILS RWY 24 AMDT 11 DELETE CAT D VIS NOTE. ADD NOTES: WHEN CONTROL TOWER OPEN AND MM INOPERATIVE INCREASE CAT D S-LOC VIS TO RVR 5000. WHEN CONTROL TOWER CLOSED: (A) USE OTIS AFB ALTIMETER SETTING. (B) INCREASE ALL DH/MDAS 140 FEET. (C) ALS SEQUENCED FLASHING LIGHTS INOPERATIVE. (D) INOPERATIVE TABLE DOES NOT APPLY TO VISIBILITY. (E) S-ILS ALL CATS VIS 3/4. (F) S-LOC CATS A,B, AND C VIS 3/4, CAT D VIS 1 1/4. VOR RWY 24, AMDT 9 CHANGE CTLZ NOTES TO: WHEN CONTROL TOWER CLOSED: (A) USE OTIS AFB ALTIMETER SETTING. (B) INCREASE ALL MDAS 120 FEET. (C) S-24 VIS CATS A,B, AND C 3/4, CAT D 1 1/4. (D) ALS SEQUENCED FLASHING LIGHTS INOPERATIVE.

NEW BEDFORD

New Bedford Muni

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT PPR CALL 617-992-2264. (10/86)

NORTHHAMPTON

Northhampton

FDC 6/1938 /7B2/ FI/T NORTHAMPTON, NORTHAMPTON, MA. VOR-A AMDT 1. DME OR RADAR RQRD FOR ADARE INT MISSED APCH: CLIMBING LEFT TURN TO 3500 DIRECT BAF VORTAC AND HOLD S, RT, 039 INBOUND. VOR/DME-B AMDT 1. MISSED APCH: CLIMB TO 3500 DIRECT BAF VORTAC AND HOLD S, RT, 039 INBOUND.

NORWOOD

Norwood Memorial

FDC 6/2933 /OWD/ FI/T NORWOOD MEMORIAL, NORWOOD, MA. TKOF MINS: RWY 17, 900-1 OR STANDARD WITH MIN CLIMB OF 350 FT PER NM TO 900. RWY 35, 1400-1 OR STANDARD WITH MIN CLIMB OF 270 FT PER NM TO 1400.

ORANGE

Orange Muni

FDC 6/1205 /ORE/ FI/T ORANGE MUNI ARPT/MA. NDB-B AMDT 3 PROCEDURE NA. VOR-A AMDT 5 VOR/NDB MINIMUMS NA.

PITTSFIELD

Pittsfield Muni

FDC 6/1937 /PSF/ FI/T PITTSFIELD MUNI, PITTSFIELD, MA. LOC RWY 26 ORIG. NDB RWY 26 ORIG. TRML ROUTES HIDAL INT TO DXT NDB AND CTR VORTAC TO DXT NDB NA. STELA INT AND GRISY INT DME RQRD.

MASSACHUSETTS

PLYMOUTH

Plymouth Muni

FDC 6/866 /PYM/ FI/T PLYMOUTH MUNI.PLYMOUTH MA. NDB RWY 6 AMDT 7. TRML ROUTE HYA VORTAC TO PYM NDB. USE PYM NDB 312 BRG FOR CRS GUIDANCE. HYA VORTAC R312 UNUSABLE BEYOND 5 NM. SI VIS 1 1/2 CAT C.

PROVINCETOWN

Provincetown Muni

FDC 6/1829 /PVC/ FI/T PROVINCETOWN MUNI PROVINCETOWN MA. ILS RWY 7 AMDT 1. PHONY INT/I-VQO 4.8 DME. TRML ROUTE WOMEK INT TO PHONY INT/I-VQO 4.8 DME 10.0 MAP 4.1 AFTER PASSING PHONY INT OR AT 0.7 DME. DSTC FAF TO THLD 4.1. GS ALT AT PHONY INT 1396. SI LOC AND PHONY INT DME OR RADAR RQRD. MISSED APCH CLIMB TO 600 THEN CLIMBING LT TO 2000 TO RZP NDB AND HOLD W, RT 076 INBOUND TRML ROUTE DRUNK INT TO WOMEK INT DSTC 10.7. NDB-A AMDT 5. TRML ROUTE HYA VORTAC TO RZP NDB. USE RZP NDB BRG 192 FOR CRS GUIDANCE. TRML ROUTE DRUNK INT TO RZP NDB 109/18.6. NDB RWY 25 AMDT 1. PROC NA.

STOW

Minute Man Airfield

FDC 5/2194 /6B6/ FI/T MINUTE MAN AIRFIELD, STOW, MA. NDB-A AMDT 6..CIRCLING MDA 1400/HAA 1132 CATS A/B. VIS 1 1/4 CAT A/ 1 1/2 CAT B. TKOF MINS RWY 21..1200-2 OR STANDARD WITH MIN CLIMB OF 310 FEET PER NM TO 1500. RWYS 12/30 NA.

WESTFIELD

Barnes Muni

FDC 6/1943 /BAF/ FI/T BARNES MUNI, WESTFIELD, MA. NDB RWY 20 AMDT 13. TRML ROUTE CTR VORTAC TO BA LOM NA. TRML ROUTES CTR VORTAC TO BA LOM, GDM VORTAC /IAF/TO LEADS INT AND LEADS INT TO BA LOM/NOPT/NA. VOR RWY 20 AMDT 18. TRML ROUTE CTR VORTAC TO KLYDE INT 5.3 DME NA. DME OR RADAR RQRD FOR KLYDE INT 5.3 DME. VOR OR TACAN RWY 2 AMDT 2. DME OR RADAR RQRD FOR DECAR INT.

FDC 6/1332 /BAF/ FI/T BARNES MUNI, WESTFIELD, MA. ILS RWY 20 AMDT 3..S-ILS ALL CATS DH 520 HAT 250 VIS 1. S-LOC CATS A/B VIS 1. INOPERATIVE TABLE DOES NOT APPLY TO VISIBILITY. WHEN MALSR INOPERATIVE INCREASE S-LOC CATS C/D VIS 1/2 MI...VOR RWY 20 AMDT 18...S-20 CATS A/B VIS 1. INOPERATIVE TABLE DOES NOT APPLY TO CATS A/B. NDB RWY 20 AMDT 13...S-20 CATS A/B VIS 1. WHEN MALS INOPERATIVE CAT A VIS 1, CAT B VIS 1 1/4/. CAT C VIS 2 1/4, AND CAT D 2 1/2. TAKE-OFF MINIMUMS...RWY 20 FAR 135 VISIBILITY REDUCTION NOT AUTHORIZED.

Barnes Muni ATCT

ATIS & ATCT HRS 0800-2300 LCL. (11/86)

MICHIGAN

ADRIAN

Lenawee County

RWY 05 VASI CMSND.(10/86)

BATTLE CREEK

Kellogg Regional

FDC 6/1322 /BTL/ FI/T W. K. KELLOGG REGIONAL/BATTLE CREEK, MI. NDB RWY 23 AMDT 15..ILS RWY 23 AMDT 15..VOR RWY 5 /TAC/AMDT 17...VOR RWY 23 /TAC/AMDT 15..VOR RWY 31 /TAC/AMDT 12..HI- TACAN RWY 23 AMDT 4. WHEN CONTROL TOWER CLOSED ACTIVATE REIL RWY 13 - CTAF.

BAY CITY

James Clements Muni

RWY 09/27 CLSD TIL SUMMER 87. (11/86)

CARO

Caro Muni

FDC 6/2394 /78D/ FI/T CARO MUNI..CARO MI. VOR/DME A AMDT 2. CIRCLING MDA 1340 HAT 640 ALL CATS.

DETROIT

Detroit Metropolitan Wayne County

FDC 6/3045/DTW/FI/P DETROIT METROPOLITAN WAYNE COUNTY..DETROIT MI. RNAV RWY 21R ORIG, CORRECT U.S. GOVT CHART EC VOL 1 PAGE 64 DATED 25 SEP 1986. IN PROFILE CHANGE DISTANCE FROM BARGO WPT TO 5.1 NM FROM MAP WPT TO 3 MI.

FDC 6/3008 /DTW/FI/T DETROIT METROPOLITAN, WAYNE COUNTY, DETROIT, MI. NDB RWY 3C AMDT 8. PROC NA.

FDC 6/2683 /DTW/ FI/T DETROIT METROPOLITAN WAYNE COUNTY, DETROIT, MI..NDB RWY 3L AMDT 7...ILS RWY 3L AMDT 9...ILS RWY 21R AMDT 21...RNAV RWY 21R OIRG...MISSED APPROACH - CLIMB TO 3000 THEN DIRECT SVM VORTAC AND HOLD NW, LT 114 INBOUND. VOR RWY 9 AMDT 11...PROC NA.

Willow Run

FDC 6/3152 /YIP/FI/T WILLOW RUN DETROIT MI. ILS RWY 5R AMDT 11. S-ILS 5R DH 965 HAT 250 ALL CATS. INOPERATIVE TABLE DOES NOT APPLY TO DH FOR INOPERATIVE MM.

DETROIT/GROSSE ILE

Grosse Ile Muni

RWY 03/21 NOW 4978 FT BY 100 FT. RWY 03 THR DSPLCD 568 FT. RWY 21 THR DSPLCD 838 FT. RWY 17/35 NOW 3752 FT BY 75 FT. (10/86)

ESCANABA

Delta Co

CTLZ HRS 0600-2300 LCL MON-FRI, 0630-1500 LCL SAT, 1100-2300 LCL SUN. (11/86)

FREMONT

Fremont Muni

FDC 6/3039 /3FM/ FI/T FREMONT MUNI, FREMONT, MI. VOR RWY 36 AMDT 4..BAKSY INT-DME OR RADAR REQUIRED. DELETE WHITE CLOUD /HIC/ R-226.

FDC 6/2667 /3FM/ FI/T FREMONT MUNI, FREMONT, MI. VOR-A AMDT 8, VOR RWY 36 AMDT 4. ACTIVATE MIRL RWYS 9-27, 18-36, REIL RWYS 18-36 AND VASI RWY 36 - CTAF.

GRAYLING

Grayling AAF

RWY 05/23 CLSD TO AIRCRAFT 12500/OVER.(11/86)

INDIAN RIVER

Calvin Campbell Muni

ARPT CLSD TIL 01 JUNE 87. (10/86)

IRON MOUNTAIN/KINGSFORD

Ford

CTLZ HRS 0600-2200 LCL SUN-FRI, 0600-1800 LCL SAT. (11/86)

FDC 6/3046 /IMT/FI/T FORT/IRON MOUNTAIN MI. ILS RWY 1 AMDT 7 RADAR REQUIRED. MISSED APPROACH: CLIMB TO 4200 FT VIA NORTH COURSE OF LOC THEN RIGHT TURN CLIMB TO 5000 FT VIA HEADING 140 AND ESC R-278 TO GERLA INT AND HOLD. HOLD WEST..RT..098 INBOUND. ESC FREQ 110.8 CHAN 45. LOC/DME BC RWY 19 AMDT 8..VOR RWY 1 AMDT 10..VOR RWY 19 AMDT 5..VOR RWY 31 AMDT 12..VOR/DME RWY 1 ORIG. VOR/DME RWY 19 ORIG..VOR/DME RWY 31 ORIG. NOT AUTHORIZED.

IRONWOOD

Gogebic County

CTLZ HOURS 0500-1700 LCL SUN-FRI, 0500-0900 AND 1300-1600 LCL SAT. (10/86)

JACKSON

Jackson County-Reynolds Field

RWY 06 THR DSPLCD 438 FT. RWY 32 THR DSPLCD 305 FT. (11/86)

MT PLEASANT

Mt Pleasant Muni

FDC 6/2101 /MOP/ FI/T MT PLEASANT MUNI MI.VOR RWY 27 AMDT 10..ACTIVATE MIRL RWY 9-27, REIL RWY 27, AND VASI RWY 27 - CTAF.

NILES

Jerry Tyler Meml

RWY 03/21 NOW 3300 FT BY 50 FT. (10/86)

OWOSSO

Owosso Community

FDC 6/2666 /5D3/ FI/T OWOSSO COMMUNITY, OWOSSO, MI. VOR RWY 28 AMDT 4. ACTIVATE HIRL RWY 10-28 - CTAF.

SAGINAW

Browne NDB

(HYX), FREQ 385, HOURS OF OPERATION CONTINUOUS, OPERATIONAL VFR-ONLY, PUBLIC USE, CONTROLLING FSS MBS. (11/86)

Harry W. Browne

FDC 6/2431 /3SG/ FI/T HARRY W. BROWNE, SAGINAW, MI. VOR/DME-A AMDT 2, AFTER 2200 LOCAL ACTIVATE MIRL AND REIL RWYS 5-23, 9-27 AND VASI RWYS 9-27-CTAF.

SAULT STE MARIE

Chippewa County Intl

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT 24 HRS PPR CALL 906-495-5656. (10/86)

STURGIS

Kirsch Muni

RWY 06/24 NOW 3441 FT BY 75 FT. RWY 18/36 NOW 5899 FT BY 75 FT.(11/86)

MINNESOTA

BAUDETTE

Baudette International

FDC 6/2301 BDE/BAUDETTE INTL/ BAUDETTE,MN. VOR RWY 30 AMDT 6... VOR/DME RWY 12 AMDT 1...USE INTERNATIONAL FALLS ALSTG AND INCREASE ALL MDA'S 80 FT.

BEMIDJI

Bemidji-Beltrami County

RWY 07/25 NOW OPEN. (11/86)

BENSON

Benson Muni

RWY 05/23 CLSD PERMLY. (11/86)

BOZEMAN

Gallatin Fld

FOR MIRL RWY 12/30 CONTACT BZN FSS 123.6. (11/86)

BRAINERD

Brainerd-Crow Wing Co/Walter F. Wieland Fld

FDC 6/2306 BRD/ BRAINERD-CROW WING/WALTER F. WIELAND FLD/ BRAINERD, MN. NDB RWY 23, AMDT 2...ILS RWY 23 AMDT 2...VOR RWY 30 AMDT 9...VOR/DME RWY 12 AMDT 5...WHEN CTLZ NOT IN EFFECT, EXCEPT FOR OPERATORS WITH APPROVED WEATHER REPORTING SERVICE, PROC NA.

CAMBRIDGE

Cambridge Muni

FDC 6/1467 /CBG/ FI/T CAMBRIDGE MUNI, CAMBRIDGE MN. NDB RWY 34 AMDT 3...TERMINAL ROUTE ALTITUDE FROM GOPHER VOR/GEP/TO CAMBRIDGE NDB /CBG/3000.

DULUTH

Sky Harbor

ACTIVATE MIRL RWY 14/32 & REIL & PAPI RWYS 14 & 32 122.8. (10/86)

ELY

Ely Muni

ACTIVATE MIRL RWY 12/30 122.8. (10/86)

EVELETH

Eveleth-Virginia Muni

FDC 6/2768 /EVM/ FI/T EVELETH-VIRGINIA MUNI, EVELETH MN. VOR RWY 27 AMDT 8...ACTIVATE MIRL RWYS 9-27 AND 14-32 AND REIL 27 ON CTAF.

FAIRMONT

Fairmont Muni

FDC 6/2197 /FRM/ FI/T FAIRMONT MUNI, FAIRMONT, MN. VOR RWY 31 AMDT 6..S-31 VIS 1 CATS A/B/C. VOR/DME RWY 31 ORIG..S-31 VIS 1 CATS A/B/C. INOPERATIVE COMPONENTS TABLE DOES NOT APPLY.

FDC 5/896 /FRM/FAIRMONT MUNI, FAIRMONT, MN. VOR RWY 13 AMDT 3/ VOR RWY 31 AMDT 6/ VOR/DME RWY 13 ORIG/ VOR/DME RWY 31 ORIG. ALTN MINS NA.

GRAND RAPIDS

Grand Rapids Itasca County

FDC 6/435 /GPZ/ FI/T GRAND RAPIDS ITASCA COUNTY GRAND RAPIDS MN. MLS RWY 34 (INTERIM) ORIG.. PROC NA.

HIBBING

Chisholm-Hibbing

FDC 6/2764 /HIB/ FI/T CHISHOLM-HIBBING HIBBING MN. ILS RWY 31 AMDT 9. S-ILS-31 DH 1593 HAT 250 ALL CATS. DH NOT INCREASED FOR INOP MM.

INTERNATIONAL FALLS

Falls Intl

FDC 6/1247 /INL/ FI/T FALLS INTL INTERNATIONAL FALLS MN. VOR RWY 13 AMDT 11 S-13 AND CIRCLING CAT A/B/C/D MDA 1740 HAT/HAA 555. LOC/DME BC RWY 13 AMDT 7 S-13 AND CIRCLING CAT A/B/C/D MDA 1760 HAT/HAA 575.

LANCASTER

Lancaster Muni

FACILITY ABANDONED. (11/86)

MINNEAPOLIS

Anoka County-Blaine (Janes Field)

VASI RWYS 17 & 35 CMSND. (10/86)

Anoka County-Blaine (Janes Field) ATCT

FDC 6/2010 /ANE/ FI/T MINNEAPOLIS/ANOKA CO BLAINE ARPT RNAV RWY 17 ORIG..S-17 MDA 1340 HAT 431 ALL CATS VIS CATS A/B 1 CAT C 11 1/4 CAT D 1 1/2.

Flying Cloud

ACTIVATE VASI RWY 09R AND WHEN ATCT CLSD ALS RWY 09R 118.1. (10/86)

Minneapolis-St Paul Intl/Wold Chamberlain

FDC 5/2769 /MSP/ FI/T MINNEAPOLIS-ST. PAUL INTL/WOLD CHAMBERLAIN/MINNEAPOLIS MN. NDB RWY 4 AMDT 15..ILS RWY 4 AMDT 21.. ILS RWY 11R AMDT 2..ILS RWY 29L AMDT 38. CIRCLING CAT A/B/C MDA 1360/HAA 519. LOC BC RWY 11L AMDT 6..LOC/VOR OR RADAR MINIMUMS CIRCLING CAT A/B/C MDA 1360/HAA 519.

ORR

Orr Regional

FDC 5/1997 /ORB/ FI/T ORR REGIONAL.ORR MN. NDB RWY 13 AMDT 4. ACTIVATE MIRL RWY 13/31 CTAF.

PARK RAPIDS

Park Rapids Muni

FDC 6/2302 PKD/PARK RAPIDS MUNI/PARK RAPIDS, MN. NDB RWY 31 AMDT 2..MLS RWY 31 (INTERIM) AMDT 2..VOR RWY 31 AMDT 10..VOR/DME RWY 13 AMDT 5..OBTAIN LOCAL ALSTG ON CTAF; WHEN NOT AVAILABLE PROC NA.

RED WING

Red Wing Muni

FDC 6/635 /RGK/ FI/T RED WING MUNI, RED WING, MN. NDB RWY 8 ORIG. CHANGED TO READ NDB RWY 9 ORIG.

REDWOOD FALLS

Redwood Falls Muni

RWY 05/23 CLSD WINTER MONTHS.(10/86)

ROCHESTER

Rochester Muni

FDC 6/1201 /RST/ FI/T ROCHESTER MUNICIPAL, ROCHESTER, MN. ILS RWY 13, AMDT 3, VOR RWY 2, AMDT 13; AND VOR/DME RWY 20. AMDT 11: MSA 270 DEGREES THRU 090 DEGREES IS 3300.

ROSEAU

Roseau Muni

FDC 6/2303 ROX/ROSEAU MUNI/ROSEAU, MN. VOR-A AMDT 4.. VOR RWY 16 AMDT 3..USE WARROAD ALSTG; WHEN NOT AVBL PROC NA.

FDC 5/2578 /ROX/ FI/T ROSEAU MUNI, ROSEAU, MN. VOR-A AMDT 4 AND VOR RWY 16, AMDT 3: ACTIVATE MIRL AND REIL RWY 16/34 - CTAF.

ST. CLOUD

St. Cloud Muni

FDC 6/2863 /STC/ FI/T ST. CLOUD MUNI, MN. VOR RWY 31 AMDT 5..VOR/DME RWY 13 AMDT 2..CAT D CIRCLING MDA 1600.

ST PAUL

St Paul Downtown Holman Fld

FDC 6/2064 /STP/ FI/T ST PAUL DOWNTOWN HOLMAN FLD, ST PAUL, MN. MLS RWY 30 (INTERIM) AMDT 6. S-MLS-30 DH 1250/HAT 546 ALL CATS VIS CATS A/B 1, CAT C 1 1/2, CAT D 1 3/4. CIRCLING MDA 1640/HAA 936 CATS A/B/C VIS CATS A/B 1 1/4. CAT C 2 3/4. MISSED APCH: CLIMB TO 1700 THEN CLIMBING RT TO 2700 DIRECT BONDY LOM/I-STP 6.8 DME AND HOLD. LOC RWY 30 AMDT 10. NDB RWY 30 AMDT 4. CIRCLING MDA 1640/HAA 936 CATS A/B/C VIS. CATS A/B 1 1/4, CAT C 2 3/4, 1310 FOOT MSL CRANE AT 445655N/ 093054W. 16-34 - CTAF.

STAPLES

Staples Muni

FDC 6/2304 SAZ/STAPLES MUNI/STAPLES, MN. NDB RWY 14 AMDT 2 .. USE ALEXANDRIA ALSTG AND INCREASE ALL MDA'S 60 FEET.

MINNESOTA

THIEF RIVER FALLS

Thief River Falls Regional

FDC 5/500 /TVF/ FI/T THIEF RIVER FALLS REGIONAL, THIEF RIVER FALLS MN. ILS RWY 31 ORIG. ALTERNATE MINIMUMS NA.

WORTHINGTON

Worthington Muni

RWY 14/32 CLSD INDEFLY. (11/86)

MISSISSIPPI

COLUMBIA

Columbia-Marion County

FDC 6/1688 /ORO/ FI/T COLUMBIA-MARION COUNTY, COLUMBIA, MS. VOR/DME RWY 23 AMDT 3. MSA FROM LBY VORTAC 2400.

GREENVILLE

Greenville Muni ILS

(I-GLH) RWY 17L GS & MM OTS INDEFLY. (11/86)

GREENWOOD

Greenwood-Leflore

RWY 05/23 MIRL DCMSND. (10/86)

FDC 6/2627 /GWO/ FI/T GREENWOOD-LEFLORE, GREENWOOD, MS..VOR RWY 5 AMDT 8..NIGHT SI MINS NA.

GULFPORT

Gulfport Biloxi Rgnl

FDC 6/2383 /GPT/ FI/T GULFPORT-BILOXI RGNL, GULFPORT/MS. ILS RWY 13 AMDT 10. AUTO COUPLED APCH NA.

FDC 6/1536 /GPT/ FI/T GULFPORT BILOXI RGNL, GULFPORT, MS.. NDB RWY 13 AMDT 8..ILS RWY 13 AMDT 10...MSA FROM GP LOM 2800.

JACKSON

Allen C. Thompson Field

FDC 6/2938 /JAN/ FI/T ALLEN C. THOMPSON FLD, JACKSON, MS. VOR OR TACAN RWY 15L AMDT 2; VOR RWY 15 R (TAC) AMDT 5; VOR/DME RWY 33 L (TAC) AMDT 9; VOR/DME RWY 33R (TAC) AMDT 2. VOR APCHS NA.

MERIDIAN

Key Field

FDC 6/2215 /MEI/ FI/T KEY FIELD, MERIDIAN, MS. NDB RWY 1 AMDT 17. ALTN MINS NA WHEN TOWER CLSD OR WHEN MEI FSS CLSD. VOR-A AMDT 12, RNAV RWY 19 AMDT 2, ILS RWY 1 AMDT 22. ALTN MINS NA WHEN MEI FSS CLSD.

NATCHEZ

Hardy-Anders Field Natchez-Adams Co

FDC 6/1633 /HEZ/ FI/T HARDY-ANDERS FIELD NATCHEZ-ADAMS COUNTY, NATCHEZ, MS. NDB RWY 17 AMDT 2, LOC RWY 17 AMDT 2. MSA FROM HE LOM 2300. VOR RWY 17 AMDT 8, VOR/DME RWY 13 ORIG. MSA FROM HEZ VOR/DME 2300.

MISSISSIPPI

OKOLONA

Okolona Muni-Richard Stovall Field

FDC 6/1609 /5A4/ FI/T OKOLONA MUNI-RICHARD STOVALL FIELD, OKOLONA MS VOR/DME RWY 18 AMDT 1..MSA 25 NM FROM TUP VOR/DME 3400.

OXFORD

University-Oxford

FDC 6/2247 UOX/UNIVERSITY-OXFORD/ OXFORD, MS. RNAV RWY 9 AMDT 1..VOR/DME-A AMDT 2..RNAV RWY 27 AMDT 1.. ALTN MINS NA EXCEPT FOR OPERATORS WITH APPROVED WEATHER REPORTING SERVICE.

TUPELO

C. D. Lemons Muni

FDC 6/2320 /TUP/ FI/T C.D. LEMONS MUNI TUPELO MS. VOR-A ORIG. PROC NA.

Industrial Airpark

FDC 6/1002 /MS80/INDUSTRIAL AIRPARK TUPELO MS.. VOR RWY 11 AMDT 1..PROC NA.

MISSOURI

CABOOL

Cabool Memorial

FDC 6/2198 /H74/ FI/T CABOOL MEMORIAL, CABOOL MO. RWY 3 AMDT 1..NDB RWY 21 AMDT 1..FEEDER ROUTE WEST PLAINS NDB TO TVB NDB NA.

CAPE GIRARDEAU

Cape Girardeau Muni

RWY 20 VASI CMSND. (10/86)

CHARLESTON

Mississippi County

RWY 18/36 NOW 3200 FT BY 60 FT. VASI RWY 18 OTS INDEFLY.(10/86)

COLUMBIA

Columbia Regional

AIRPORT CLOSED TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS 2300-0700 LCL EXCEPT PRIOR PERMISSION CALL SAFETY OFFICE 314-443-2811. CFR SERVICE NON-AIR CARRIER. OPERATIONS NOT AVAILABLE 2300-0700 LCL EXCEPT PRIOR ARRANGEMENT CALL SAFETY OFFICE 314-443-2811.(10/86)

FDC 6/77 /COU/ FI/T COLUMBIA REGIONAL, COLUMBIA MO. NDB RWY 2 AMDT 6..ILS RWY 2. AMDT 10....LOC BC RWY 20 AMDT 8..WHEN ATCT CLSD, ALTERNATE MINIMUMS NA.

FDC 5/2538 /COU/ FI/T COLUMBIA REGIONAL, COLUMBIA MO. VOR RWY 13 AMDT 3..FAF ALTITUDE/AFBAR INT/2200. STRAIGHT IN MDA 1900, HAT 1012 ALL CATS. CIRCLING MDA 1900, HAA 1011 ALL CATS. DUAL VOR MINS UNCHANGED.

Cotton Woods Memorial

FDC 6/388 /K24/ FI/T E. W. COTTON WOODS MEMORIAL..COLUMBIA MO. VOR-A AMDT 4. MSA FROM CBI VOR/DME 3000. VOR-B AMDT 1. MSA FROM HLV VORTAC 3000.

MISSOURI

CUBA

Cuba Muni

FDC 6/2999 /UBX/ FI/T CUBA MUNI, CUBA, MO. NDB RWY 36 AMDT 1 SI MDA 1760/HAT 738 CATS A/B/C. VIS CAT C 2 MILES. CIRCLING MDA 1760/HAA 738 CATS A/B/C, VIS CAT C 2 MILES.

FT LEONARD WOOD

Forney AAF

FDC 6/326 /TBN/ FI/T FORNEY AAF FT. LEONARD WOOD, MO. NDB RWY 32 AMDT 4, LOC RWY 14 AMDT 5, VOR RWY 14 AMDT 4, VOR RWY AMDT 4 PRIOR PERMISSION REQUIRED. CONTACT AIRFIELD OPERATIONS AREA CODE 314-368-2166.

FULTON

Fulton Muni

FDC 6/1710 /H65/ FI/T FULTON MUNI, FULTON, MO. RNAV RWY 23 ORIG..S-23 MDA 1600/HAT 719 CATS A/B/C. CIRCLING MDA 1600/HAA 714 CATS A/B/C.

FDC 6/373 /H65/ FI/T FULTON MUNI, FULTON, MO. VOR-A, AMDT 1, MSA FROM HLV VORTAC 3000. NDB RWY 5, ORIG, NDB RWY 23, ORIG, MSA FROM FTT NDB 310-180 2900, 180-310 3800.

GRAVOIS MILLS

Wulff Harbor

ARPT CLSD INDEFLY. (10/86)

HANNIBAL

Hannibal Muni

FDC 6/1155 /HAW/ FI/T HANNIBAL MUNI, HANNIBAL, MO. VOR/DME AMDT 1. MSA FROM UIN VORTAC 2700. NDB RWY 35 AMDT 2 MSA FROM HAE NDB 2700.

KAISER/LAKE OZARK/

Lee C Fine Memorial

RWY 03 VASI CMSND. ACTIVATE VASI RWYS 03 & 21 122.8.(11/86)

KANSAS CITY

Kansas City Downtown

RWY 03 THR DSPLCD 377 FT. (10/86)

FDC 6/2692 /MKC/ FI/T KANSAS CITY DOWNTOWN..KANSAS CITY MO. VOR RWY 21 AMDT 11. DUAL VOR MINIMA NA.

FDC 6/1551 /MKC/ FI/T KANSAS CITY DOWNTOWN, KANSAS CITY MO. NDB RWY 19 AMDT 15..S-19 MDA 1460 HAT 702 ALL CATS. CIRCLING MDA 1460 HAA 702 ALL CATS. BLUFF FM MINIMA NA.

FDC 6/1487 /MKC/ FI/T KANSAS CITY DOWNTOWN, KANSAS CITY, MO. ILS RWY 19 AMDT 17 S-ILS-19 DH 1036 HAT 278 ALL CATS. S-LOC-19 MDA 1400 HAT 642 ALL CATS.

FDC 6/167 /MKC/ FI/T KANSAS CITY DOWNTOWN, KANSAS CITY, MO. ILS RWY 19 AMDT 17 BLUFF FM MINIMA S-LOC MDA 1280 HAT 522 ALL CATS VIS CAT C 1 1/2. CRANE .8 NM WEST.

Richards-Gebaur

FDC 6/2033 /GVW/ FI/T RICHARDS-GEBAUR..KANSAS CITY MO. ILS RWY 36 AMDT 2..CHANGE NOTE..WHEN CONTROL TOWER CLOSED ACTIVATE ALSF-1 RWY 36/VASI AND HIRL RWY 18-36 - CTAF.

KENNETT

Kennett NDB

(TKX) CONTROLLING FSS CGI. (11/86)

ST LOUIS

EFFECTIVE FOR APRXLY ONE YEAR, TWY F CONVERTED TO RWY 13/31, 6300 FT BY 75 FT, ASPH. RWY 31 THR DSPLCD 1880 FT. (10/86)

Spirit of St Louis

FDC 6/495 /SUS/ FI/T SPIRIT OF ST LOUIS, ST LOUIS, MO. NDB RWY 8R AMDT 7, ALTERNATE NA.

STE GENEVIEVE

Ste Genevieve Flying Club

ARPT CLSD TO PUBLIC USE. (10/86)

SEDALIA

Sedalia Memorial

FDC 5/1699 /DMO/ FI/T SEDALIA MEMORIAL SEDALIA MO. NDB RWY 18, AMDT 5..CAT C CIRCLING MDA 1400 HAA 491.

SIKESTON

Sikeston Meml Muni

FDC 6/3096 /SIK/FI/T SIKESTON MEML MUNI, SIKESTON, MO. NDB RWY 20 AMDT 6. MSA SIK NDB 2200. SILENT HILL FM MINS NA. TMRL ROUTE UPONS INT (IAF) TO SILENT HILL FM (NOPT) NA. CGI VOR TO UPONS INT NA.

SPRINGFIELD

Springfield Regional

FOR HIGH INTSTY AFTER 2300 LCL CONTACT SGF FSS. ACTIVATE VASI RWYS 01, 19 & 13 2330-0530 LCL 119.9. (11/86)

FDC 6/2791 /SGF/ FI/T SPRINGFIELD REGIONAL, SPRINGFIELD, MO. NDB RWY 1, AMDT 14: ILS RWY 1, AMDT 15: VOR RWY 19, AMDT 14: RNAV RWY 13, AMDT 3: ADD NOTE: WHEN CONTROL TOWER CLOSED, ACTIVATE SSALR RWY 1 CTAF.

TRENTON

Trenton Muni

FDC 6/2720 /TRX/ FI/T TRENTON MUNI, TRENTON MO. NDB RWY 17 AMDT 5 NOW NDB RWY 18 AMDT 5..NDB RWY 35 AMDT 7 NOV NDB RWY 36 AMDT 7..RWY 17/35 REDESIGNATED RWY 18/36.

WHEATLAND

Skyriders

ARPT CLSD TO PUBLIC USE. (10/86)

MONTANA

BILLINGS

Billings Logan Intl

FDC 6/1272 /BIL/ FI/T BILLINGS LOGAN INTL, BILLINGS, MT. LOC BC RWY 27R AMDT 7 PROCEDURE NA.

MONTANA

BOZEMAN

Gallatin Fld

FOR MIRL RWY 12/30 AFTER 2100 LCL CONTACT BZN FSS 123.6. (10/86)

FDC 6/2781 /BZN/ FI/T GALLATIN FLD, BOZEMAN MT. NDB RWY 12 AMDT 4..ILS RWY 12 AMDT 5..VOR/DME RWY 12 AMDT 1..CIRCLING CAT A MDA 4920/HAA 446 CATS B/C CIRCLING MDA 4940/HAA 466 CAT D CIRCLING MDA 5040/HAA 566. VOR RWY 12 AMDT 12..ALL CATS CIRCLING HAA 626.

BUTTE

Bert Mooney

FOR MIRL RWYS 11/29 & 15/33 AND VASI RWYS 29 & 33 AFTER 2200 LCL CONTACT FSS 123.6. (11/86)

FDC 6/1554 /BTM/ FI/T BERT MOONEY, BUTTE MT. ILS RWY 15 AMDT 2..CIRCLING HAA 1435 ALL CATS. LOC/DME RWY 15 AMDT 4...CIRCLING HAA 1435 ALL CATS. VOR-B ORIG..CIRCLING HAA 1355 ALL CATS. VOR/DME-A AMDT 2..CIRCLING HAA 2995 ALL CATS.

GREAT FALLS

Great Falls Intl

FDC 6/3009 /GTF/FI/T GREAT FALLS INTL, GREAT FALLS, MT. VOR RWY 21 AMDT 8. PROC TURN COMPLETION ALT 5800 FT. GTF 13 DME ARC CCW FROM CTF R-103 AND CW FROM GTF R-274 TO GTF R-026 MIN ALT 5800 FT.

HELENA

Helena Regional

FDC 4/74 /HLN/ FI/T HELENA REGIONAL HELENA MT. STANDARD INSTRUMENT DEPARTURE- STAKK ONE DEPARTURE/PILOT NAV/PROC NA FOR RWY 26 DEPARTURES.

KALISPELL

Glacier Park Intl

FDC 6/2593 /FCA/ FI/T GLACIER PARK INTL, KALISPELL, MT..ILS RWY 1 AMDT 3...ALTN MINS NA.

KALISPELL

Glacier Park Intl

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT PPR CALL 406-257-5994 OR 755-5575. (11/86)

LEWISTOWN

Lewistown Muni

FDC 6/980 /LWT/ FI/T LEWISTOWN MUNI.LEWISTOWN MT. VOR RWY 7 AMDT 9. ADD NOTE: WHEN CTLZ NOT IN EFFECT ..EXCEPT FOR OPERATORS WITH APPROVED WEATHER REPORTING SERVICE..PROCEDURE AND ALTERNATE MINIMUMS NA.

MISSOULA

Missoula County

FDC 6/2572 /MSO/ FI/T MISSOULA MT. ILS-1 RWY 11 AMDT 8 AND ILS-3 RWY 11 AMDT 4 DME ARC FROM MSO R-337 ALTITUDE 10500. DME ARC FROM MSO R-255 ALTITUDE 10000.

NEBRASKA

AINSWORTH

Ainsworth RCO

LAT 423409N LONG 0995920W DCMSND. (10/86)

Ainsworth RCO

COLOCATED WITH AINSWORTH VOR-DME, FSS OLU, FREQ 122.25 CMSND. (10/86)

Ainsworth VOR/DME

(ANW) CONTROLLING FSS OLU. (10/86)

ALLIANCE

Alliance RCO

COLOCATED WITH ALLIANCE VOR-DME, FSS OLU. (10/86)

Alliance VOR/DME

(AIA) CONTROLLING FSS OLU. (10/86)

BASSETT

Rock County NDB

(RBE) CONTROLLING FSS OLU. (10/86)

BLOOMFIELD

Bloomfield Muni

FSS OLU. (11/86)

CEDAR RAPIDS

Cedar Rapids Muni

FACILITY ABANDONED. (11/86)

CHADRON

Chadron Muni

ACTIVATE MIRL RWYS 02/20 & 11/29, REIL & VASI RWYS 02 & 20 123.6.(11/86)

Chadron RCO

LAT 42-50-15.3N LONG 103-05-41.8W DCMSND.(10/86)

Chadron RCO

COLLOCATED WITH CHADRON VOR-DME, FSS OLU, FREQUENCY 122.15 CMSND.(10/86)

Chadron VOR/DME

(CDR) CONTROLLING FSS OLU. (10/86)

(CDR) DME MONITORED CONTINUOUSLY. (11/86)

Whitney NDB

(HIN) CONTROLLING FSS OLU. (10/86)

CHAPPELL

Chappell Muni

RWY 12/30 NOW 4000 FT BY 45 FT. (11/86)

COLUMBUS

Columbus FSS

CMSND, OPERATIONAL CONTINUOUS, FREQS 122.4, 122.1R, 121.5, 243.0, AND 255.4. FSS LOCATED ON COLUMBUS MUNI ARPT. (10/86)

Columbus Muni

ARPT CLSD TO AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT 24 HOURS PPR CALL 402-564-7377. CFR SERVICE NOT AVAILABLE.(10/86)

Columbus RCO

LAT 412649N LONG 0972030.1W DCMSND. (10/86)

Columbus RCO

COLOCATED WITH COLUMBUS VOR-DME, FSS OLU, FREQ 122.4. (10/86)

Columbus VOR/DME

(OLU) CONTROLLING FSS OLU. (10/86)

(OLU) DME MONITORED CONTINUOUSLY. (11/86)

Platte Center NDB

(PLT) CONTROLLING FSS OLU. (10/86)

FREMONT

Fremont NDB

(FET) CONTROLLING FSS OLU. (10/86)

GORDON

Gordon NDB

(GRN) CONTROLLING FSS OLU.(10/86)

GRAND ISLAND

Grand Island RCO

COLOCATED WITH GRAND ISLAND VORTAC, FSS OLU. (10/86)

Grand Island VORTAC

(GRI) CONTROLLING FSS OLU. (10/86)

HASTINGS

Hastings RCO

COLOCATED WITH HASTINGS VOR-DME, FSS OLU. (10/86)

Hastings VOR/DME

(HSI) CONTROLLING FSS OLU. (10/86)

(HSI) DME MONITORED CONTINUOUSLY. (11/86)

HAYES CENTER

Hayes Center RCO

COLOCATED WITH HAYES CENTER VORTAC, FSS OLU. (10/86)

Hayes Center VORTAC

(HCT) CONTROLLING FSS OLU. (10/86)

JACKSON

Tommi NDB

(OI) CONTROLLING FSS OLU. (10/86)

KIMBALL

Kimball Muni

RWY 10/28 MIRL CMSND. (10/86)

ACTIVATE MIRL RWY 10/28 122.8. (11/86)

FDC 6/2620 /4V7/ FI/T KAMBALL MUNI, KIMBALL, NE. NDB RWY 29 ORIG SI MINS NA. PROC NA AT NIGHT.

LINCOLN

Lincoln RCO

COLOCATED WITH LINCOLN VORTAC, FSS OLU. (10/86)

Lincoln VORTAC

(LNK) CONTROLLING FSS OLU. (10/86)

MC COOK

Mc Cook RCO

COLOCATED WITH MC COOK VOR, FSS OLU. (10/86)

Mc Cook VOR

(MCK) CONTROLLING FSS OLU. (10/86)

MILLARD

Millard NDB

(MLE) CONTROLLING FSS OLU. (10/86)

NORFOLK

Norfolk RCO

FSS OLU. (10/86)

Norfolk VOR

(OFK) CONTROLLING FSS OLU. (10/86)

NORTH PLATTE

North Platte RCO

COLOCATED WITH NORTH PLATTE VORTAC, FSS OLU. (10/86)

North Platte VORTAC

(LBF) CONTROLLING FSS OLU. (10/86)

OMAHA

Eppley Airfield

FDC 6/914 /OMA/ FI/T OMAHA/EPPLEY FIELD, OMAHA NE. VOR RWY 32L AMDT 8..RNAV RWY 32L AMDT 4..SI MDA 2000 HAT 1021 ALL CATS. VIS 3/4 CAT A, 1 CAT B, 2 1/2 CATS C/D. CIRCLING MDA 2000, HAA 1017 ALL CATS. VIS 1 1/4 CAT A, 1 1/2 CAT B, 3 CATS C/D. ALTERNATE MINIMUMS: 1100/3 CATS C/D.

Gerfi NDB

(OM) CONTROLLING FSS OLU. (10/86)

Omaha FSS

DCMSND.(10/86)

O'NEILL

O'Neill RCO

COLOCATED WITH O'NEILL VORTAC, FSS OLU. (10/86)

O'Neill VORTAC

(ONL) CONTROLLING FSS OLU. (10/86)

NEBRASKA

PAWNEE CITY

Pawnee City RCO

COLOCATED WITH PAWNEE CITY VORTAC, FSS OLU. (10/86)

Pawnee City VORTAC

(PWE) CONTROLLING FSS OLU. (10/86)

PLATTSMOUTH

Platsmouth NDB

(PMV) CONTROLLING FSS OLU. (10/86)

SCOTTSBLUFF

Scottsbluff RCO

COLOCATED WITH SCOTTSBLUFF VORTAC, FSS OLU. (10/86)

Scottsbluff VORTAC

(BFF) CONTROLLING FSS OLU. (10/86)

SIDNEY

Sidney FSS

DCMSND. (11/86)

Sidney Muni

ARPT CLSD TO AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT PPR CALL 308-879-4360/254-5668. (10/86)

Sidney RCO

COLOCATED WITH SIDNEY VORTAC, FSS OLU. (10/86)

Sidney VORTAC

(SNY) CONTROLLING FSS OLU. (10/86)

TEKAMAH

Tekamah VOR

(TQE) CONTROLLING FSS OLU.(10/86)

VALENTINE

Valentine NDB

(VTN) CONTROLLING FSS OLU.(10/86)

WAYNE

Wayne NDB

(LCG) CONTROLLING FSS OLU.(10/86)

WOLBACH

Wolbach RCO

COLOCATED WITH WOLBACH VORTAC, FSS OLU.(10/86)

Wolbach VORTAC

(OBH) CONTROLLING FSS OLU.(10/86)

NEVADA

ELY

Moorman Ranch

FACILITY ABANDONED. (10/86)

NEVADA

RENO

Cannon VOR/DME

(RGS) DCMSND EFFECTIVE 18 DEC 86. (11/86)

Reno Cannon Intl

FDC 6/2951 /RNO/ FI/T RENO CANNON INTL RENO, NV. HI-ILS RWY 16R ORIG AND HI-LOC 1 RWY 16R AMDT 4. PROCEDURES NA.

Reno/Stead

RWY 14/32 NOW OPEN. (10/86)

WELLS

Harriet Field

FDC 3/212 /LWL/ FI/T HARRIET FLD WELLS, NV. VOR RWY 8 AMDT 1 PROC NA.

WINNEMUCCA

Winnemucca Muni

FDC 5/2969 /WMC/ FI/T WINNEMUCCA MUNI WINNEMUCCA NV. NDB-A ORIG. ALTN MINS CAT A STANDARD..CAT B 1300-2.. CAT C 1300-3..CAT D 2200-3.

FDC 5/2885 /WMC/ FI/T WINNEMUCCA MUNI/WINNEMUCCA/ NV. NDB-A ORIG INCREASE CIRCLING MINIMUMS TO..MDA 5580 HAA 1277 VIS 1 1/2 CAT B. MDA 5580 HAA 1277 VIS 3 CAT C. MDA 6420 HAA 2117 VIS 3 CAT D. CHANGE MISSED APPROACH TO.. CLIMBING RIGHT TURN TO 9000 DIRECT EMC NDB AND HOLD.

NEW HAMPSHIRE

CLAREMONT

Claremont Muni

FDC 6/3198 /CNH/FI/T CLAREMONT MUNI, CLAREMONT NH. NDB-A AMDT 3..TRML ROUTE JAMMA INT TO CNH NDB NA.

FDC 6/2355 CNH/CLAREMONT MUNI/CLAREMONT, NH. NDB-1 AMDT 3..PROC NA AT NIGHT. IFR TKOF MINS/DEPARTURE PROC NA.

LACONIA

Laconia Muni

FDC 6/3199 /LCI/FI/T LACONIA MUNI, LACONIA NH. NDB RWY 8 AMDT 7...TRML ROUTE BILLS INT TO BLO NDB NA. LOC RWY 8 AMDT 8..TRML ROUTES BILLS INT TO BLO NDB, CON VORTAC /IAF/TO TIEGR INT /NOPT/, TIEGR INT TO BLO NDB NA.

LEBANON

Lebanon Muni

FDC 6/3193 /LEB/LEBANON MUNI, LEBANON NH. NDB-B AMDT 2..TRML ROUTE LEB VOR/DME TO LAH NDB NA. ILS RWY 7 AMDT 4..TRML ROUTES LEB VOR/DME TO IVV NDB, JAMMA INT /IAF/ TO HONES INT, HONES INT TO GS INTERCEPT /NOPT/NA. LOC RWY 7 ORIG...TRMLS ROUTE LEB VOR/DME TO IVV NDB, JAMMA INT /IAF/TO HONES INT, HONES INT TO IVV /NOPT/NA.

MANCHESTER

Manchester Airport-Grenier Industrial Airpark

FDC 6/3146 /MHT/ FI/T MANCHESTER AIRPORT-GRENIER INDUSTRIAL AIRPARK MANCHESTER NH. ILS RWY 35 AMDT

NEW HAMPSHIRE

14..S-ILS ALL CATS VIS 3/4. INOPERATIVE TABLE DOES NOT APPLY TO MALSR. S-LOC CATS A/B VIS 3/4. CATS A/B S-LOC VIS INCREASED 1/4 MILE FOR INOPEATIVE MALSR. VOR RWY 35 AMDT 12..S-35 CATS A/B VIS 3/4. CATS A/B S-35 VIS INCREASED 1/4 MILE FOR INOPERATIVE MALSR.

NASHUA

Boire Field

FDC 6/2677 /ASH/ FI/T BOIRE FIELD..NASHUA NH. ILS RWY 14 AMDT 1. BEGINNING 0700 MON THROUGH 1600 FRI..SI ILS MINS NA. SI LOC VIS 1 ALL CATS. INOP TABLE DOES NOT APPLY. INCREASE CAT D VIS 1/4 MILE FOR INOP ALS. NDB RWY 14 AMDT 1. SI VIS 1 CATS A/B. INOP TABLE DOES NOT APPLY TO CATS A/B.

ROCHESTER

Skyhaven

RWY 14/32 CHANGED TO RWY 15/33, 4000 FEET BY 100 FEET.(10/86)

FDC 6/3031 /6BI/ FI/P SKYHAVEN, ROCHESTER, NH. NDB RWY 32 AMDT 1, DEP PROCS/TKOF MINS ORIG. CHANGE ALL REFERENCES TO RWY 14/32 TO READ RWY 15/33. THIS IS NDB RWY 33 AMDT 2, DEP PROC/TKOF MINS AMDT 1.

WHITEFIELD

Whitefield Regional

FDC 6/3195 /HIB/FI/T WHITEFIELD REGIONAL, WHITEFIELD NH. LOC RWY 10 AMDT 2..NDB RWY 10 AMDT 5..TRML ROUTE LEB VOR/DME TO GMA NDB NA.

NEW JERSEY

ATLANTIC CITY

Atlantic City

ARPT NAME CHANGED TO ATLANTIC CITY INTERNATIONAL. (10/86)

Atlantic City Muni/Bader Field

FDC 6/1709 /AIY/ FI/T ATLANTIC CITY MUNI/BADER FIELD. ATLANTIC CITY, NJ. VOR-A AMDT 1....CIRCLING MDA 800/HAA 791 CATS A/B. VIS 1 1/4 CAT B. DME MINS CIRCLING MDA 740/HAA 731 CATS A/B. VOR RWY 11 AMDT 1...RNAV RWY 11 AMDT 8... SI MDA 700/HAT 691 CATS A/B. VIS 1 CAT B. CIRCLING MDA 740/HAA 731 CATS A/B. VIS 1 CAT B. WHEN CTLZ NOT IN EFFECT EXCEPT FOR OPERATORS WITH APPROVED WEATHER REPORTING SERVICE. USE ATLANTIC CITY ALSTG AND INCREASE ALL MDAS 20 FEET.

BELMAR-FARMINGDALE

Allaire

FDC 6/675 /BLM/ FI/T ALLAIRE BELMAR-FARMINGDALE NJ. SDF RWY 14 AMDT 2. PROCS NA.

FDC 5/651 /BLM/ FI/T ALLAIRE BELMAR-FARMINGDALE NJ. VOR-A AMDT 10 PROC NA.

CROSS KEYS

Cross Keys

FDC 6/2619 /17N/ FI/T CROSS KEYS, CROSS KEYS, NJ. VOR RWY 9 AMDT 2. SI AND CIRCLING MDA 720/HAT-HAA 556 CATS A/B.

NEW JERSEY

LINDEN

Linden

RWY 09 VASI RTS. (11/86)

LUMBERTON

Flying W

FDC 6/541 /N14 FLYING W..LUMBERTON NJ. VOR-A ORIG. MSA FROM RBV VORTAC 080-260 1700.

MATAWAN

Marlboro

FDC 4/1839 /2N8/ FI/T MARLBORO, MATAWAN, NJ. IFR DEP PROC RWY 9..CLIMB RWY HEADING TO 600 BEFORE TURNING.

MILLVILLE

Millville Muni

RWY 01.19 CLSD TO ALL JET ACFT, TURBO ACFT & ACFT 12500 LBS AND OVER. (11/86)

MORRISTOWN

Morristown Muni

FDC 6/3016 /MMU/FI/P MORRISTOWN MUNI, MORRISTOWN, NJ. ILS RWY 23 AMDT 4. CORRECT U.S. GOVT CHART NE, VOL 3, AL-931, PAGE 173, DATED 25 SEP 1986. BOONI INT HOLD NE, LT, 241 INBOUND.

FDC 6/2552 /MMU/ FI/T MORRISTOWN MUNI..MORRISTOWN NJ. IFR TKOF MINS. RWY 30..1100-1.

MOUNT HOLLY

Burlington County

FDC 6/540 /7MY/ FI/T BURLINGTON COUNTY..MOUNT HOLLY NJ. VOR RWY 26 AMDT 1. MSA FROM RBV VORTAC 080-260 1700.

NEWARK

Newark Intl

FDC 6/471 /EWR/ FI/T NEWARK INTL, NEWARK NJ. ILS RWY 4L AMDT 7...SI ILS DH 261/HAT 250 ALL CATS.

OLD BRIDGE

Old Bridge

FDC 6/538 /3NG/ FI/T OLD BRIDGE..OLD BRIDGE NJ. VOR RWY 24 AMDT 1. MSA FROM RBV VORTAC 080-260 1700.

ROBBINSVILLE

Trenton-Robbinsville

FDC 6/539 /N87/ FI/T TRENTON-ROBBINSVILLE..ROBBINSVILLE NJ. VOR RWY 29 AMDT 8. MSA FROM RBV VORTAC 080-260 1700.

SOMERVILLE

Somerset

FDC 4/3261 /N52/ FI/T SOMERSET, SOMERVILLE NJ VOR-A AMDT 1 PROC NA.

NEW JERSEY

SUSSEX

Sussex

FDC 6/2788 /N63/ FI/T SUSSEX ARPT, SUSSEX, NJ. VOR-A AMDT 4, MISSED APCH: CLIMBING RT TO 3000 TO SAX VORTAC AND HOLD. CIRCLING MINS: MDA 2000/HAA 1580 ALL CATS.

TETERBORO

Teterboro

FDC 6/2377 TEB/TETERBORO ARPT/TETERBORO, NJ. VOR RWY 24 AMDT 2, CURRO INT, ANGLE INT, DME REQUIRED. VOR-B AMDT 1, TELLO INT, DME RQRD.

TOMS RIVER

Robert J. Miller Air Park

FDC 6/1557 /N44/ FI/T ROBERT J. MILLER AIR PARK. TOMS RIVER NJ. VOR RWY 24 AMDT 2. TRML ROUTE FROM COL VORTAC TO PICKE INT/ 15.7 DME NA. DUAL VOR OR DME MINS NA.

TRENTON

Mercer County

CTLZ HRS 0600-2400 LCL. (10/86)

NEW MEXICO

ALBURQUERQUE

Alburquerque Intl

FDC 6/200 /ABQ/ FI/T ALBUQUERQUE INTL/ALBUQUERQUE/ NM. VORTAC-A ORIG/NDB RWY 35 AMDT 6/ILS RWY 8 AMDT 4/VOR RWY 8 (TAC) AMDT 18/RADAR-1 AMDT 20..RAISE ALL CAT D CIRCLING MDAS TO 6000/ HAA 648. REASON..5695 MSL CRANE 2.24 NM E OF AER 26.

BRIDGETON

Li Calzi

ARPT OPEN TO PUBLIC USE. (10/86)

FARMINGTON

Four Corners Regional

FDC 6/2549 /FMN/ FI/T FOUR CORNERS REGIONAL/ FARMINGTON/NM. IFR TAKOFF MINIMUMS RWY 5. 1500-2 OR STANDARD WITH MINIMUM CLIMB OF 230 FT PER NM TO 7000 FT. REASON..5955 FT TOWER 2.6 NM NE OF AIRPORT.

FDC 6/2307 FMN/FARMINGTON/FOUR CORNERS REGIONAL/FARMINGTON, NM. VOR RWY 25 AMDT 4 VOR/ DME MINIMA NOT AUTHORIZED FOR S-25. ILS RWY 25 ORIG. DME MINS NOT AUTHORIZED FOR S-LOC 25.

GALLUP

Gallup Municipal

RWY 06/24 NOW 6300 FT BY 100 FT. (11/86)

LAS VEGAS

Las Vegas Muni

FDC 6/2737 /LVS/ FI/T LAS VEGAS MUNI, LAS VEGAS, NM. VOR RWY 20 AMDT 3..VOR RWY 2 AMDT 6..ADD NOTE..WHEN CONTROL ZONE NOT IN EFFECT - PROC NA.

NEW MEXICO

TRUTH OR CONSEQUENCES

Truth or Consequences Muni

FDC 5/2979 /TCS/ FI/T TRUTH OR CONSEQUENCES MUNI, TRUTH OR CONSEQUENCES NM. VOR-1 AMDT 8 ACTIVATE MIRL RWY 13/31 - 122.8.

NEW YORK

AKRON

Akron

FDC 6/433 /9G3/ FI/T AKRON AKRON NY. VOR/DME RWY 24 AMDT 2..PROC NA.

ALBANY

Albany County

FDC 5/63 /ALB/ FI/T ALBANY COUNTY, ALBANY, NY. VOR RWY 28 AMDT 5, TRML ROUTE R-152 ALB VORTAC CCW TO R-095 ALB VORTAC VIA 12 DME ARC NA. VOR RWY 1 AMDT 16, VOR/DME RWY 1, AMDT 8. MISSED APCH: CLIMB TO 2000 DIRECT TO HAWKY LOM AND HOLD NORTH, RT, 191 INBOUND. ADD NOTE: ADF REQUIRED.

ARCADE

Arcade Airpark

ARPT CLSD TO PUBLIC USE. (11/86)

BINGHAMTON

Edwin A Link Field-Broome County

NO CFR AVAILABLE 2300-0700 LCL WITHOUT PRIOR NOTICE. RWY 10 REIL DCMSND. (10/86)

BUFFALO

Buffalo Airpark

FDC 6/3119 /9G0/FI/T BUFFALO AIRPARK/BUFFALO/NY. VOR RWY 24 AMDT 6..MSA 270-090 2800.

Greater Buffalo Intl

FDC 6/3118 /BUF/FI/T GREATER BUFFALO INTL/BUFFALO/ NY. ILS RWY 5 AMDT 13..NDB RWY 5 AMDT 10..TERMINAL ROUTE GANIS TO GB LOM 2800, MSA 180CW-090 3100..ILS RWY 23 AMDT 27..NDB RWY 23 AMDT 14..MSA 270-090 2800. VOR-A AMDT 17, MAP HOLD ALTITUDE 2800/MSA 270-090 2800. RNAV RWY 32 AMDT 5, MAP HOLD ALTITUDE 2800.

CALVERTON

Calverton Naval Weapons Industrial Reserve

FDC 6/1203 /CTO/ FI/T CALVERTON NAVAL WEAPONS INDUSTRIAL RESERVE. CALVERTON, NY. VOR/DME OR TACAN RWY 32 AMDT 1. STRAIGHT-IN MINIMUMS R-32 NOT AUTHORIZED. MINIMUM ALTITUDE 4 DME FIX 1200.

FDC 6/395 /CTO/ FI/T CALVERTON NAVAL WEAPONS INDUSTRIAL RESERVE CALVERTON NY. VOR/DME OR TACAN RWY 32 AMDT 1 VOR/DME OR TACAN-A AMDT 1. MSA FROM CCC VORTAC 360-180 1800..180-360 2100.

CORTLAND

Cortland County-Chase Field

FDC 6/1875 /NO3/ FI/T CORTLAND COUNTY-CHASE FIELD. CORTLAND, NY. VOR RWY 6 ORIG..MISSED APCH: CLIMB TO 3500 VIA ITH R-068 TO GCT VORTAC AND HOLD W, RT, 085 IBND.

FDC 6/1796 /NO3/ FI/T CORTLAND COUNTY-CHASE FIELD, CORTLAND, NY VOR RWY 06 ORIG..MISSED APCH. CLIMB TO 3500 VIA ITH R-068 TO GGT VORTAC AND HOLD W. RT. 085 INBOUND.

EAST HAMPTON

East Hampton

RWY 04/22 NOW 2501 FT BY 100 FT. RWY 10/28 NOW 4242 FT BY 75 FT. RWY 16/34 NOW 2220 FT BY 75 FT. (10/86)

ELMIRA

Elmira/Corning Regional

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT 30 MIN PPR CALL 607-739-5621. (10/86)

ENDICOTT

Tri-Cities

RWY 03/21 NOW 3900 FT BY 75 FT. ACTIVATE MIRL RWY 03/21 122.8. (11/86)

FARMINGDALE

Republic

FDC 6/2987 /FRG/ FI/T REPUBLIC FARMINGDALE NY. ILS RWY 14 AMDT 4 RADAR REQUIRED. MISSED APPROACH..CLIMB TO 500 THEN CLIMBING LEFT TURN TO 3000 VIA HEADING 010 FOR RADAR VECTORS TO FINAL APPROACH COURSE. TERMINAL ROUTE DPK VORTAC TO FR LOM NA. LOC BC RWY 32 AMDT 4 RADAR REQUIRED. MISSED APPROACH..CLIMBING RIGHT TURN TO 3000 VIA HEADING 020 FOR RADAR VECTORS TO FINAL APPROACH COURSE. TERMINAL ROUTE DPK VORTAC TO FISLA INT NA. NDB RWY 1 AMDT 12. TERMINAL ROUTE DPK TO BRN NDB NA.

FISHERS ISLAND

Elizabeth Field

FDC 6/2231 /0B8/ FI/T ELIZABETH FIELD, FISHERS ISLAND NY VOR-A AMDT 4 MSA TMU VOR 360 CW-270 2000, 270 CW-360 2600.

GLENS FALLS

Glens Falls VORTAC

(GFL) VOR PORTION UNUSABLE 175-200.(10/86)

Warren County

FDC 6/673 /GFL/ FI/T WARREN COUNTY, GLENS FALLS, NY. ILS RWY 1 AMDT 3. ALDEN INT GF LOM 179 BRG. ADF RQRD. VOR/DME RWY 19 AMDT 6. MISSED APCH: CLIMB TO 4000 DRCT GF LOM AND HOLD S, RT, 012 IBND. ADF RQRD. VOR RWY 1 AMDT 9, VOR/DME RWY 1 AMDT 3, RNAV RWY 1 AMDT 1. PROCS NA.

ISLIP

Long Island Mac Arthur

FDC 6/1634 /ISP/ FI/T LONG ISLAND MAC ARTHUR, ISLIP, NY. ILS RWY 24 ORIG. SI ILS VIS 3/4 ALL CATS. SI LOC VIS 3/4 CATS A/B.

New York FSS

AAS FREQUENCY 119.3 DCMSND.(10/86)

ITHACA

Ithaca VORTAC

(ITH) VOR PORTION UNUSABLE 360-150 BYD 25 NM BELOW 3800 FT. (10/86)

NEW YORK

John F. Kennedy Intl

FDC 6/2990 /JFK/ FI/T JOHN F KENNEDY INTL NEW YORK NY. VOR RWY 13L/13R AMDT 16 MISSED APPROACH..AT OR BEYOND MAP CLIMB TO 4000 VIA HEADING 100 FOR RADAR VECTORS TO FINAL APPROACH COURSE. VOR/DME OR TACAN RWY 22L AMDT 3 TERMINAL ROUTE DPK VORTAC TO CAPIT INT JFK 10 DME NA. VOR-D AMDT 8 TERMINAL ROUTE DPK VORTAC TO OJONE NA. DME REQUIRED FOR OJONE AND HELIN INTS. ILS RWY 31R AMDT 11 TERMINAL ROUTE DPK VORTAC TO LORAC I-RTH 11.5 DME NA. DME REQUIRED FOR LORAC AND MALDE INTS. ILS RWY 31L AMDT 5 TERMINAL ROUTE DPK VORTAC TO ZACHS INT I-MOH 11.9 DME NA. DME REQUIRED. ILS RWY 22L AMDT 20 TERMINAL ROUTE DPK VORTAC TO ROSLY INT I-IWY 11.7 DME NA. DME REQUIRED.

FDC 6/2989 /JFK/ FI/T JOHN F KENNEDY INTL NEW YORK NY. ILS RWY 4L AMDT 5 RADAR REQUIRED. MISSED APPROACH..CLIMB TO 2000 THEN RIGHT TURN VIA JFK R-062 FOR RADAR VECTORS TO FINAL APPROACH COURSE. ILS RWY 4R AND CAT II/CAT III A AMDT 27 RADAR REQUIRED. MISSED APPROACH..CLIMB TO 500 THEN CLIMBING RIGHT TURN TO 4000 VIA HEADING 100 FOR RADAR VECTORS TO FINAL APPROACH COURSE. VOR RWY 4L/R AMDT 14 RADAR REQUIRED. MISSED APPROACH..CLIMBING RIGHT TURN TO 4000 VIA HEADING 100 FOR RADAR VECTORS TO FINAL APPROACH COURSE. ILS RWY 13L AND CAT II AMDT 12 MISSED APPROACH..CLIMB TO 500 THEN CLIMBING LEFT TURN TO 4000 VIA JFK R-078 FOR RADAR VECTORS TO FINAL APPROACH COURSE.

FDC 6/2963 /JFK/ FI/T JOHN F KENNEDY INTL, NEW YORK, NY. ILS RWY 22L AMDT 20. ILS RWY 22R AMDT 5, ILS RWY 31L AMDT 5, VOR-D AMDT 8. VOR/DME RWY 31L AMDT 11. VOR/DME OR TACAN RWY 22L AMDT 3. MISSED APPROACH ALTITUDE REVISED TO 4000.

FDC 6/1586 /JFK/ FI/T JOHN F. KENNEDY INTL, NEW YORK, NY.. ILS RWY 31R AMDT 11..MISSED APPROACH..CLIMB TO 2000 THEN LEFT TURN DIRECT CRI VOR/DME. AFTER CRI VOR/DME CLIMB TO 4000 VIA CRI R-225 TO COL VORTAC AND HOLD.

La Guardia

FDC 6/2988 /LGA/ FI/T LA GUARDIA NEW YORK NY. NDB RWY 22 AMDT 10 AND ILS RWY 22 AMDT 16 DME REQUIRED FOR YOMAN INT. VOR-A AMDT 12 DME REQUIRED FOR RUBYE INT. VOR-C AMDT 5 DME REQUIRED FOR CORVE INT.

La Guardia ILS/DME

(I-GDI) RWY 13 GS USABLE. (10/86)

NIAGARA FALLS

Niagara Falls Intl

FDC 6/3120 /IAG/FI/T NIAGARA FALLS INTL/NIAGARA FALLS/NY. ILS RWY 28R AMDT 21..NDB RWY 28R AMDT 15. TERMINAL ROUTE GANIS TO IA LOM 2800, MSA 205-295 2800. TAKEOFF MINIMUMS IFR DEPARTURE PROCEDURE..RWYS 24/10R AND 10L..CLIMB TO 1700 ON RWY HEADING BEFORE TURNING SOUTHBOUND.

PENN YAN

Penn Yan

RWY 18/36 NOW 1640 FT BY 60 FT. RWY 17/35 NOW 1730 FT BY 55 FT. PCL LIRL RWY 10/28 DCMSND. (11/86)

PLATTSBURGH

Clinton Co

ACTIVATE MIRL RWYS 01/19 & 14/32 122.7. RWY 10/28 CLSD INDEFLY. (10/86)

Plattsburgh VORTAC

(PLB) EFFECTIVE 18 DEC 86 VOR PORTION UNUSABLE 350-355 BYD 15 NM BELOW 4000 FT; DME UNUSABLE 025-050 BYD 30 NM BELOW 4000 FT; 250-330 BYD 25 NM BELOW 8000 FT; 331-350 BYD 20 NM BELOW 8000 FT. (10/86)

POTSDAM

Potsdam Muni/Damon Fld/

ARPT OPEN TO IFR NIGHT OPERATIONS. (10/86)

POUGHKEEPSIE

Dutchess County

RWY 06 VASI DCMSND. (10/86)

RWY 24 REIL DCMSND. (10/86)

FDC 6/1244 /POU/ FI/T DUTCHESS COUNTY POUGHKEEPSIE NY. ILS RWY 6 AMDT 4 S-ILS ALL CATS VIS 1 S-LOC CATS A/B/C VIS 1. INOPERATIVE TABLE DOES NOT APPLY. WHEN MALSR INOPERATIVE S-LOC CAT C VIS 1 1/4 CAT D VIS 1 1/2. VOR/DME RWY 6 AMDT 5 S-6 CATS A/B VIS 1. INOPEATIVE TABLE DOES NOT APPLY TO CATS A/B.

RED HOOK

Sky Park

RWY 01/19 NOW 2666 FT BY 20 FT. (10/86)

SENECA AAF (ROMULUS)

Seneca Army Depot

FDC 6/2712 /SSN/ FI/P SENECA AAF, SENECA ARMY DEPOT (ROMULUS) NY..NDB-A AMDT 4 - CORRECT US GOVT CHART DOD, VOL-9, PAGE 265, AL-997.01. DATED 25 SEP 1986. TRML ROUTE REEPS INT TO SSN NDB 130/9.3.

SOUTH DAYTON

South Dayton

ARPT CLSD TO PUBLIC USE. (11/86)

SPRING VALLEY

Ramapo Valley

FDC 6/2443 /N24/ FI/T RAMAPO VALLEY SPRING VALLEY NY. VOR RWY 8 ORIG. PROC NA.

UTICA

Oneida County

RWY 15 REIL DCMSND. (11/86)

WALLKILL

Wallkill

ARPT CLSD TO PUBLIC USE. (10/86)

WELLSVILLE

Halos NDB

(EL) RTS. (11/86)

Wellsville Muni/Tarantine Fld

RWY 10 THR NO LONGER DSPLCD. (10/86)

RWYS 10 & 28 VASI DCMSND. (10/86)

FDC 6/2663 /ELZ/ FI/T WELLSVILLE MUNI ARPT TARANTINE FLD WELLSVILLE NY..LOC RWY 28 AMDT 2..RADAR RQRD. MISSED APCH..CLIMBING RT TO 4100 DIRECT ELZ VORTAC AND HOLD S RT 025 INBOUND.

FDC 5/2262 /ELZ/WELLSVILLE MUNI ARPT, TARANTINE FIELD, WELLSVILLE, NY. LOC RWY 28 AMDT 2...NDB RWY 28 AMDT 5 S-28 CATS A/B VIS 1 MI. CHANGE LIGHT NOTE TO READ...ACTIVATE MIRL RWY 10/28 CTAF. CHANGE INOP TABLE NOTE TO READ...INOP TABLE DOES NOT APPLY. VOR-A AMDT 4 CHANGE LIGHT NOTE TO READ...ACTIVATE MIRL RWY 10/28 CTAF.

Wellsville Muni, Tarantine Fld LOC

(I-ELZ) RWY 28 LOM RTS.(11/86)

WESTHAMPTON BEACH

Suffolk County

FDC 4/1815 /FOK/ FI/T SUFFOLK COUNTY, WESTHAMPTON BEACH, NY. LOC BC RWY 6 AMDT 3 PROC NA.

NORTH CAROLINA

ALBEMARLE

Stanly County

FDC 6/283 /8A6/ FI/T STANLY COUNTY, ALBEMARLE, NC. NDB RWY 4 AMDT 1. DELETE TRML ROUTES FROM DRATT INT TO SWY NDB AND FROM NESTE INT TO SWY NDB. ADD TRML ROUTE LOCAS INT TO SWY NDB 053/17.7, 2700.

CHARLOTTE

Charlotte/Douglas Intl

FDC 6/2899 /CLT/FI/T CHARLOTTE/DOUGLAS INTL, CHARLOTTE, NC. VOR RWY 36R AMDT 4, S-36R MDA 1140/HAT 404 ALL CATS. VIS 3/4 MI CAT C.

FDC 6/2097 /CLT/ FI/T CHARLOTTE/DOUGLAS INTL CHARLOTTE NC. NDB RWY 5 AMDT 29..NDB RWY 23 AMDT 5..ILS RWY 5 AMDT 31.. ILS RWY 18R AMDT 4..ILS RWY 36L AMDT 3..VOR RWY 36R AMDT 4.. VOR/DME RWY 18L AMDT 4..VOR/DME RWY 18R AMDT 4..RADAR 1 AMDT 17. CIRCLING MINIMUMS, NA FOR RWYS 18L/36R AND 05/23.

Charlotte/Douglas Intl ILS

(I-DQG) RWY 36L GLIDE SLOPE RTS.(11/86)

Charlotte/Douglas Intl ILS/DME

(I-BQC) RWY 36R GS UNUSABLE 5 DEGS LEFT LOC COURSE. (11/86)

DRAKE

Drake Muni

ARPT CLSD TO PUBLIC USE. (11/86)

NORTH CAROLINA

EDEN

Rockingham County Heliport

NEWLY REPORTED FACILITY. OPEN TO PUBLIC USE. HELIPAD 60 FT BY 60 FT, MIRL. HELIPAD VASI CMSND. (10/86)

ELIZABETH CITY

Elizabeth City CG Air Station/Muni

FDC 6/932 /ECG/ FI/T ELIZABETH CITY CG AIR STATION/ MUNI ELIZABETH CITY NC..NDB-A AMDT 8..VOR RWY 1 AMDT 8.. VOR RWY 19 AMDT 7..PROC/S NA WHEN TETHERED BALLOON LCTD APPROXIMATELY 2 MI SE OF ARPT IS ALOFT.

FORT BRAGG

Simmons AAF

FDC 6/1013 /FBG/ FI/T SIMMONS AAF..FORT BRAGG NC. VOR RWY 27 AMDT 9..NDB RWY 27 AMDT 6. SI AND CIRCLING MDA 760/HAT 533/HAA 518 ALL CATS. VIS SI 1 1/2 CAT C. RADAR-1 AMDT 8. ASR RWY 27. SI AND CIRCLING MDA 760/HAT 533/HAA 518 ALL CATS. VIS ASR RWY 27 1 1/2 CAT C.

GREENSBORO

Greensboro-High Point-Winston Salem Regional

FDC 6/3142 /GSO/FI/T GREENSBORO - HIGH POINT - WINTSTON SALEM REGNL, GREENSBORO, NC..ILS RWY 23 AMDT 5..SI ILS VIS RVR 1800 CATS A/B/C, RVR 2000 CAT D.

HICKORY

Barretts Mountain VOR/DME

(BZM) CMSND EFFECTIVE 18 DEC 86.(10/86)

Hickory Muni

FDC 5/862 /HKY/HICKORY MUNI, HICKORY, NC. ILS RWY 24, AMDT 5. RADAR REQUIRED FOR TRANSITION ROUTE BZM TO SIBEL INT AND SANFI INT TO SIBEL INT.

LEXINGTON

Lexington Muni

FDC 6/2830 /EXX/ FI/T LEXINGTON MUNI, LEXINGTON, NC. VOR-A AMDT 2..CIRCLING MDA 1380/HAA 654 ALL CATS. VIS CAT C 1 3/4.

LUMBERTON

Lumberton Muni

FDC 6/2970 /LBT/ FI/T LUMBERTON MUNI, LUMBERTON NC. VOR RWY 13 AMDT 6. SI MINS NA AT NIGHT.

FDC 6/2787 /LBT/ FI/T LUMBERTON MUNI, LUMBERTON, NC..VOR RWY 5 AMDT 6..VOR RWY 13 AMDT 6..TRML ROUTES TROCK INT TO LBT VOR AND WILDS INT TO LBT VOR 3000.

MANTEO

Dare County Regional

RWY 10/28 CLSD PERMLY. (11/86)

RWY 04/22 NOW 3850 FT BY 75 FT. (11/86)

FDC 6/1367 /MQI/ FI/T DARE COUNTY REGIONAL..MANTEO NC. VOR RWY 16 AMDT 1. PROC NA.

NORTH CAROLINA

MORGANTON

Morganton-Lenoir

RWY O3 VASI CMSND. (11/86)

ROCKY MOUNT

Rocky Mount-Wilson

FDC 6/1684 /RWI/ FI/T ROCKY MOUNT-WILSON ROCKY MOUNT NC. IFR DEPARTURE PROCEDURE RWY 22-FLY RUNWAY HEADING UNTIL 2500 FEET BEFORE TURNING WEST. NDB RWY 4 AMDT 5/ILS RWY 4 AMDT 10. MSA WITHIN 25 NM RW LOM 3400. LOC BC RWY 22 AMDT 2. MSA WITHIN 25 NM TYI VORTAC 3400.

FDC 6/858 /RWI/ FI/T ROCKY MOUNT-WILSON, ROCKY MOUNT, NC. ILS RWY 4 AMDT 10. S-ILS 4 DH 408 VIS 3/4 HAT 250 ALL CATS. INOP TABLE DOES NOT APPLY TO MALSR. S-LOC 4 VIS 3/4 CAT A/B/C. VIS INCREASED 1/4 MILE FOR INOP MALSR CAT A/B/C.

RUTHERFORDTON

Rutherford County

FDC 6/2213 /57A/ FI/T RUTHERFORD COUNTY, RUTHERFORDTON, NC. NDB RWY 36 AMDT 2, S-36 MDA 1560 HAT 484 ALL CAT. CIRCLING MDA 1560 HAA 482 CAT A, B, C. VOR RWY 36 AMDT 1 S-36 MDA 1520 HAT 444 ALL CAT. CIRCLING MDA 1560 HAA 482 CAT A, B, AND C.

SALISBURY

Rowan VOR/DME

(RUQ) RTS. (10/86)

TABOR CITY

Rogers Field

FACILITY ABANDONED. (11/86)

WILKESBORO

Wilkes County

MIRL RWY 06/24 & REIL RWY 24 PRESET LOW INTSTY DUSK-2200 LCL, AFTER 2200 LCL INCREASE INTSTY & ACTIVATE VASI RWY 24 123.0. (11/86)

WILSON

Wilson Muni

FDC 6/1662 /WO3/ FI/T WILSON MUNI WILSON NC. NDB RWY 3 AMDT 4 FEEDER ROUTE RDU VORTAC TO RW LOM ALT 3200. MSA WITHIN 25 NM RW LOM 3400.

NORTH DAKOTA

BISMARCK

Bismarck Muni

ACTIVATE MALS RWY 13 AND MALSR RWY 31 118.3. (10/86)

FDC 6/3078 /BIS/FI/T BISMARCK MUNI, BISMARCK ND. ILS RWY 31 AMDT 31..TERMINAL ROUTE R-263 BIS VOR/DME CCW TO R-180 BIS VOR/DME VIA 16 DME ARC, ALTITUDE 4700.

NORTH DAKOTA

DICKINSON

Dickinson Muni

FDC 6/2997 /DIK/ FI/T DICKINSON MUNI, DICKINSON, ND. ILS/DME RWY 32 AMDT 1. ALT AT OM 4918, MM 2780. TCH 59.

FARGO

Hector International

FDC 6/3175 /FAR/FI/T HECTOR INTERNATIONAL, FARGO ND. DEPARTURE PROCEDURES/TAKEOFF MINIMUMS. TAKEOFF MINIMUMS: RWY 13 300-1. DEPARTURE PROCEDURES: RWYS 17 AND 21 CLIMB RWY HEADING TO 1300 BEFORE TURNING. 1067 FOOT CRANE AT 465348N/964814W.

GRAFTON

Grafton NDB

(GAF) DCMSND. (10/86)

GRAND FORKS

Grand Forks-Mark Andrews Intl

FDC 6/2642 /GFK/ FI/T GRAND FORKS-MARK ANDREWS INTL..GRAND FORKS ND. VOR RWY 35L AMDT 4. DME MINIMUMS S-35L MDA 1220 HAT 376 ALL CATS.

JAMESTOWN

Jamestown

FDC 4/2544 /JMS/ FI/T JAMESTOWN MUNICIPAL, JAMESTOWN, ND. ILS RWY 30, AMDT 5, LOC/DME BC RWY 12, AMDT 5, VOR RWY 12, AMDT 5, VOR RWY 30, AMDT 6, NDB RWY 30, AMDT 4. PROC NA WHEN JMS FSS CLSD.

MAKOTI

Makoti

ARPT CLSD TO PUBLIC USE. (10/86)

MINOT

Minot Intl

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT PPR CALL 701-857-4724.(10/86)

MOHALL

Mohall Muni

FDC 6/3084 /HBC/ FI/T MOHALL MUNI, MOHALL, NORTH DAKOTA. VOR/DME RWY 31 AMDT 1, S-31 MDA 2600, HAT 950 ALL CATS. VIS CAT A/B 2, CAT C 2 3/4. CIRCLING MDA 2600, HAA 952 ALL CATS. VIS CAT C 2 3/4.

WADSWORTH

Wadsworth Muni

RWY 20 REIL & VASI CMSND. RWY 02 REIL CMSND. (10/86)

WILLISTON

Sloulin-Field International

FDC 6/2632 /ISN/ FI/T SLOULIN FLD INTL, WILLISTON, ND. IFR TAKEOFF MINIMUMS RWY 02 300-1. TEMPORARY 2100 FOOT MSL DRILLING RIG 3/10 MILE FROM AER 20.

OHIO

AKRON

Akron-Canton Regional

RWY 05/23 NOW 7598 BY 150 FT, MIRL CHANGED TO HIRL. (10/86)

FDC 6/3158 /CAK/FI/T AKRON-CANTON REGIONAL/AKRON/OH. ILS RWY 23 AMDT 5 FINAL APCH CRS - 234 DEG MAGNETIC. DIST MM TO THR 0.4NM. ELEV OF GS AT MM 1412 FEET MSL. S-ILS-23 DH 1428 HAT 200 ALL CATS.

ATHENS/ALBANY

Ohio University LOC

(I-UNI) RWY 25 CMSND. (10/86)

University NDB

(UNI) NAV IDENT CHANGED TO UGS. (10/86)

BOWLING GREEN

Wood County

RWY 18 THR DSPLCD 540 FT. (10/86)

CLEVELAND

Burke Lakefront

FDC 6/3171 /BKL/FI/T BURKE LAKEFRONT, CLEVELAND OH. NDB RWY 24R AMDT 5..LOC RWY 24R AMDT 6..STRAIGHT - IN MINIMUMS RWY 24R AND 24L NOT AUTHORIZED. CAUTION: 694 MSL CRANE LOCATED 1600 FEET FROM AER 24R CENTERLINE.

COLUMBUS

Port Columbus Intl

FDC 6/2674 /CMB/ FI/T PORT COLUMBUS INTL..COLUMBUS OH. LOC/BC RWY 28R AMDT 4. MSA FROM APE VORTAC 4000 WITHIN 25 NM.

MANSFIELD

Mansfield Lahm Muni

FDC 6/3115 /MFD/ FI/T MANSFIELD LAHM MUNI, MANSFIELD OH. ILS RWY 32 AMDT 13..DISTANCE MM TO RWY 32 - 0.5 NM ELEVATION OF GLIDE SLOPE AT MM - 1488 FEET MSL.

FDC 6/2417 /MFD/ FI/T MANSFIELD LAHM MUNI MANSFIELD OH..NDB RWY 32 AMDT 9..ILS RWY 32 AMDT 13..LOC (BC) RWY 14 AMDT 5..VOR RWY 14 AMDT 11..VOR RWY 32 AMDT 4..RNAV RWY 5 ORIG..RNAV RWY 23 AMDT 4..HI-VOR/DME OR TACAN RWY 14 AMDT 2..RADAR-1 AMDT 1..WHEN CONTROL TOWER CLOSED, ACTIVATE SSALR RWY 32, HIRL RWY 14-32, REIL RWY 14 - CTAF. WHEN CONTROL TOWER CLOSED. EXCEPT FOR OPERATORS WITH APPROVED WEATHER REPORTING SERVICE. USE CLEVELAND HOPKINS ALSTG.

MEDINA

Freedom Field

FDC 6/2635 /1G5/ FI/T FREEDOM FIELD, MEDINA, OH..NDB RWY 27 AMDT 6..PROC NA.

NEWARK

Newark-Heath

FDC 6/2673 /2J8/ FI/T NEWARK-HEATH..NEWARK OH. VOR-A AMDT 8. MSA FROM APE VORTAC 4000 WITHIN 25 NM.

OHIO

SPRINGFIELD

Springfield-Beckley Muni

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT PPR CALL 513-325-6100. (10/86)

TOLEDO

Metcalf Field

FDC 6/1893 /TDZ/ FI/T METCALF FIELD, TOLEDO, OH. VOR RWY 4 AMDT 7 VOR/DME RWY 4 ORIG. ACTIVATE REIL RWY 22 CTAF.

Toledo Express

FDC 6/840 /TOL/ FI/T TOLEDO EXPRESS, TOLEDO OH. ILS RWY 7. AMDT 21: S-ILS 7 DH 932/HAT 250 ALL CATS. INOP TABLE DOES NOT APPLY TO DH FOR INOP MM. HI-ILS RWY 7, AMDT 3, DH 932/ HAT 250 ALL CATS.

YOUNGSTOWN

Youngstown Executive

ARPT CLSD FRI & SAT 1600-2300 LCL APR-OCT EXCEPT PPR THRU UNICOM. (10/86)

FDC 6/3026 /YNG/FI/T YOUNGSTOWN MUNLYOUNGSTOWN OH. ILS RWY 14 AMDT 3..ILS RWY 32 AMDT 22..NDB RWY 32 AMDT 16..VOR RWY 19 AMDT 16..RADAR-1 AMDT 9. CIRCLING MDA 1640/HAA 444 CAT A. RADAR-1 AMDT 9. S-23 MDA 1600/HAT 409 ALL CATS. VIS CAT C 1 1/4. VOR RWY 19 AMDT 16 SI MDA 1600/HAA 404 ALL CATS. VIS CAT C 1 1/4.

OKLAHOMA

ARDMORE

Downtown Ardmore Executive

RWYS 17 & 35 REIL CMSND. (11/86)

BARTLESVILLE

Frank Phillips

FDC 6/1231 /BVO/ FI/T FRANK PHILLIPS, BARTLESVILLE, OK. NDB RWY 17 ORIG..LOC RWY 17 AMDT 1 MSA 3100 WITHIN 25 NM OF BV LOM. VOR RWY 17 AMDT 9. VOR/DME RWY 35 AMDT 4. MSA 3100 WITHIN 25 NM OF BVO VORTAC.

DUNCAN

Halliburton Field

FDC 6/3161 /DUC/ FI/T HALLIBURTON FIELD..DUNCAN OK. LOC RWY 35 AMDT 1. SI MDA 1480/HAT 383 ALL CATS. CIRCLING MDA 1560/HAA 447 CAT A. VOR RWY 35 AMDT 7..S-I MDA 1480/HAT 383 ALL CATS. CIRCLING MDA 1560/HAA 447 CATS A.

HOBART

Hobart FSS

HOURS OF OPERATION 0800-1600 LCL; OTHER HOURS CONTACT MCALESTER FSS.(10/86)

HOBART

Hobart Muni

CTLZ HRS 0800-1600 LCL. (11/86)

OKLAHOMA

IDABEL

Idabel

EFFECTIVE THROUGH 04 JUNE 87, ON AN INTERMITTENT BASIS, AEROBATIC FLIGHTS FOR AN AREA ENCOMPASSING TWO NAUTICAL MILES DUE WEST OF THE ENTIRE LENGTH OF RWY 17/35 FROM THE SURFACE TO 5000 FEET AGL. (7/86)

MC ALESTER

FDC 5/2322 /MLC/ FI/T MC ALESTER MUNI, MC ALESTER, OK. NDB RWY 1, AMDT 1, LOC RWY 1, AMDT 1, ALTERNATE MINIMUMS NA.

MIAMI

Miami Muni

RWY 35 THR NO LONGER DSPLCD. (11/86)

NORMAN

David Jay Perry

RWYS 13 & 31 VASI DCMSND. (11/86)

University of Oklahoma Westheimer Airpark ATCT

ATCT HRS 0800-2000 LCL. (11/86)

PRYOR CREEK

Mid-America Industrial

VASI RTS. (11/86)

SAND SPRINGS

Eagles Nest

FACILITY ABANDONED. (11/86)

SHAWNEE

Shawnee Muni

FDC 6/228 /SNL/ FI/T SHAWNEE MUNI, SHAWNEE, OK. NDB RWY 17 AMDT 5. INCREASED SI AND CIRCLING MDAS 1800, HAT/HAA 728 ALL CATS. VIS CAT C SI AND CIRCLING, 2 MILES. RNAV RWY 17 AMDT 2. INCREASE SI MDAS 1720, HAT 648 ALL CATS. VIS CAT C 1 3/4 MILES. CIRCLING MDAS 1760, HAA 688 ALL CATS. VIS CAT C 2 MILES.

FDC 5/1763 /SNL/ FI/T SHAWNEE MUNI, SHAWNEE, OK. IFR TKOF MINS RWY 17 300-1 OR STANDARD WITH MIN CLIMB OF 250 FT PER NM TO 1200. TMPRY OIL RIG 2522 FT S/588 FT E OF APPROACH END RWY 35.

STILLWATER

Stillwater Muni

ACTIVATE MIRL RWY 04/22 BY PPR 122.7. RWY 22 REIL CMSND. RWY 17/35 RWY NOW 6002 FT BY 100 FT. (10/86)

STROUD

Stroud Muni

ARPT CLSD INDEFLY. (10/86)

OKLAHOMA

TULSA

Tulsa International

RWY 35R ALSF1 CHANGED TO ALSF2. RWY 17L SSALR CHANGED TO MALSR. (11/86)

FDC 6/1229 /TUL/ FI/T TULSA INTERNATIONAL, TULSA, OKLAHOMA NDB RWY 17L AMDT 6, ILS RWY 17L AMDT 7, TERMINAL ROUTE FROM MURNA INT NA. MSA 3100 270 DEGREES TO 090 DEGREES WITHIN 25 NM OF DW LOM. NDB RWY 35R AMDT 17. ILS RWY 35R AMDT 26. MSA 3200 180 DEGREES TO 090 DEGREES WITHIN 25 NM OF TU LOM.

OREGON

ASTORIA

Astoria RCO

EFFECTIVE 18 DEC 86 FSS MMV. (10/86)

Astoria VOR/DME

(AST) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

Karpen NDB

(PEN) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

AURORA

Prahl NDB

(PLV) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

BAKER

Baker Muni

FDC 4/386 /BKE/ FI/T BAKER MUNICIPAL, BAKER, OR. VOR/DME RWY 12, AMDT 9, PROCEDURE TURN NA.

CAPE KIWANDA

Cape Kiwanda Marine NDB

(K) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

CONDON

Condon State

RWYS 04/22 & 11/29 CLSD PERMLY. (11/86)

CORVALLIS

Corvallis Muni

FDC 6/2957 /CVO/ FI/P CORVALLIS MUNI, CORVALLIS, OR. ILS RWY 17 ORIG. CHANGE EUGENE ALTIMETER SETTING NOTE TO READ: INOPERATIVE TABLE DOES NOT APPLY TO MM. S-ILS 17 VIS INCREASED 1/2 MILE FOR INOPERATIVE MALSR WHEN USING EUGENE ALTIMETER SETTING. ADD NOTE: OBTAIN LOCAL ALTIMETER SETTING ON CTAF. WHEN NOT AVAILABLE USE EUGENE ALTIMETER SETTING. GLIDE SLOPE HEIGHT AT LWG NDB IS 2449 FT. THIS IS AMDT 1.

Corvallis RCO

COLOCATED WITH CORVALLIS VOR-DME DCMSND EFFECTIVE 18 DEC 86.(10/86)

Corvallis VOR/DME

(CVO) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

OREGON

Lewisburg NDB

(LWG) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

EUGENE

Eugene RCO

COLOCATED WITH EUGENE VORTAC, FREQ 122.1R DCMSND EFFECTIVE 18 DEC 86.(10/86)

Eugene RCO

EFFECTIVE 18 DEC 86 FSS SEA.(10/86)

Eugene VORTAC

(EUG) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

Mahlon Sweet Field

FDC 6/475 /EUG/ FI/T MAHLON SWEET FIELD EUGENE, OR. NDB RWY 16, AMDT 27, ILS RWY 16, AMDT 31, VOR/DME OR TACAN RWY 16, AMDT 2, AND VOR/DME OR TACAN RWY 34, AMDT 2. CIRCLING MDA CAT A/B/C 840.

KLAMATH FALLS

Kingsley Field

FDC 1/2769 /LMT/ FI/T KINGSLEY FLD, KLAMATH FALLS, OR. VOR /DME RWY 14 /TAC/ ORIG AND VOR /DME RWY 32 / TAC/ ORIG. CAT A AND B CIRCLING MDA 4980/HAA 886/ VSBY 1 1/4 CAT C CIRCLING MDA 4980/HAA 888 VSBY 2 3/4.

MC MINNVILLE

McMinnville FSS

OPERATIONAL HRS CONTINUOUS, FREQUENCIES 121.5, 243.0, 122.45, 122.6 & 122.0 CMSND EFFECTIVE 18 DEC 86. FSS LOCATED ON MC MINNVILLE ARPT. (10/86)

MEDFORD

Medford-Jackson County

FDC 6/1864 /MFR/ FI/T MEDFORD-JACKSON COUNTY MEDFORD OR. ILS/DME RWY 14 AMDT 12...TERMINAL ROUTES FROM BROKN AND AZURE NA. FAF IS PUMIE LOM/ I-MFR 5.8 DME.

NEWBERG

Newberg RCO

COLOCATED WITH NEWBERG VORTAC DCMSND EFFECTIVE 18 DEC 86. (10/86)

Newberg RCO

COLOCATED WITH NEWBERG VORTAC FSS (MMV), OPERATIONAL HRS CONTINUOUS, FREQUENCY 121.5 CMSND EFFECTIVE 18 DEC 86.(11/86)

Newberg VORTAC

(UBG) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

PORTLAND

Hood VOR/DME

(HDR) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

OREGON

Laker NDB

(IA) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

Portland FSS

EFFECTIVE 18 DEC 86 FREQUENCIES 122.0 AND 122.2 DCMSND. (10/86)

Portland Intl

FDC 6/2824 /PDX/ FI/T PORTLAND INTL, PORTLAND, OR. LOC BC RWY 10L, AMDT 11..PROC NA.

Portland RCO

COLOCATED WITH PORTLAND VORTAC DCMSND EFFECTIVE 18 DEC 86. (10/86)

Portland VORTAC

(PDX) EFFECTIVE 18 DEC 86 CONTROLLING FSS SEA. (11/86)

Ontario Muni

FDC 6/1747 /ONO/ FI/T ONTARIO MUNI..ONTARIO OR. NDB RWY 32 AMDT 3. TERMINAL ROUTES FROM BOI VORTAC..EMETT INT.. HOVEL INT AND PARMO INT NA. HOSTS INT TO ONO NDB 22.6 NM.

REDMOND

Roberts Field

FDC 3/242 /RDM/ FI/T ROBERTS FIELD REDMOND, OR. ILS RWY 22 ORIG TRML RTE R-346 RDM VORTAC CW TO LOC COURSE VIA RDM VORTAC 22 DME ARC ALT 7800.

SALEM

Salem RCO

FSS MMV EFFECTIVE 18 DEC 86. (10/86)

SCAPPOOSE

Portland RCO

FSS MMV, OPERATIONAL HOURS CONTINUOUS, FREQUENCY 122.6 CMSND EFFECTIVE 18 DEC 86.(11/86)

Scappoose Industrial Airpark

RWY 15/33 NOW 3999 FT BY 150 FT. (11/86)

Vancouver RCO

FSS SEA, OPERATIONAL HOURS CONTINUOUS, FREQUENCY 122.2 CMSND EFFECTIVE 18 DEC 86. (11/86)

THE DALLES

The Dalles FSS

EFFECTIVE 18 DEC 86 OPERATIONAL HRS 0600-2200 LCL, OTHER HRS CONTACT MC MINNVILLE FSS. (10/86)

The Dalles Muni

FDC 5/2255 /DLS/ FI/T THE DALLES MUNI, THE DALLES, OR. VOR/ DME-A, AMDT 2. MDA 1940/HAA 1697 ALL CATS. VIS CAT A 1 1/4, CAT B 1 1/2, CAT C/D 3. ALTERNATE MINS..CAT A/B 1700-2, CAT C/D 1700-3.

The Dalles RCO

COLOCATED WITH THE DALLES VORTAC, EFFECTIVE 18 DEC 86 FSS SEA. EFFECTIVE 18 DEC 86 FREQUENCY 122.1R DCMSND. (10/86)

The Dalles VORTAC

(DLS) EFFECTIVE 18 DEC 86 CONTROLLING FSS SEA. (11/86)

OREGON

TILLAMOOK

Tillamook

FDC 6/1866 /S47/ FI/T TILLAMOOK, TILLAMOOK, OR. NDB-A ORIG PROC NA. IFR DEP PROC NA.

Wilson NDB

(TKW) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

YAQUINA HEAD

Yaquina Head Marine NDB

(W) EFFECTIVE 18 DEC 86 CONTROLLING FSS MMV. (11/86)

PACIFIC

MARIANA ISLANDS

Obyan/Saipan Intl

FDC 6/3002 /GSN/ FI/P OBYAN/SAIPAN INTL, MARIANNA IS. NDB RWY 7 AMDT 3; NDB/DME RWY 7 AMDT 1; NDB/DME RWY 25 AMDT 1; ILS/DME RWY 7 AMDT 2. STANDARD ALTN MINS AUTHORIZED. THIS IS NDB RWY 7 AMDT 4; NDB/DME RWY 7 AMDT 2; NDB/DME RWY 25 AMDT 2; ILS/DME RWY 7 AMDT 3.

MOEN ISLAND/TRUST TERRITORY

Truk International

FDC 6/2686 /TKK/FI/T MOEN ISLAND/TRUK INTL, TT NDB-A ORIG..NDB-B AMDT 2..NDB/DME RWY 1 ORIG..NDB/DME RWY 22 ORIG..ALTERNATE MINS 800-3.

PONAPE ISLAND/TRUST TERRITORY

Pohnpei Intl

FDC 6/1364 /PNI/ FI/T POHNPEI INTL/PONAPE ISLAND/ TRUST TERRITORY NDB/DME RWY 9 ORIG. STRAIGHT IN AND CIRCLING MINS..CAT A MDA 560 VIS 2 HAT/HAA 550. CAT B/C MDA 700 VIS 2 HAT/HAA 690. CAT D MDA 700 VIS 2 1/4 HAT/HAA 690.

PAGO PAGO AMERICAN SAMOA

Pago Pago Intl

FDC 6/2430 /PPG/ FI/T PAGO PAGO INTL, PAGO PAGO AMERICAN SAMOA. VOR/DME OR TACAN B AMDT 3. MIN ALT TUT 4.5 DME 1500 FT.

PENNSYLVANIA

ALTOONA

Altoona-Blair County

FDC 6/1623 /AOO/ FI/T ALTOONA-BLAIR COUNTY, ALTOONA PA. ILS RWY 20 AMDT 3..SI ILS DH 1737/HAT 250. VIS 3/4 ALL CATS. INOP TABLE DOES NOT APPLY. SI LOC VIS 3/4 CAT A.

Altoona FSS

FREQ 123.65 DCMSND. (10/86)

BEDFORD

Bedford

FDC 5/2981 /4G9/ FI/T BEDFORD AIRPORT BEDFORD PA. VOR/DME-A AMDT 1. MDA 2300/HAA 1107. CONTROLLED

AIRSPACE ENDS AT 3490 MSL. MISSED APPROACH CLIMBING RIGHT TURN TO 3000 VIA HEADING 320, THEN CLIMBING LEFT TURN TO 3700 VIA THS R-296 TO CAIF 22 DME AND HOLD. OBTAIN LOCAL ALTIMETER ON CTAF. WHEN NOT AVAILABLE USE ALTOONA ALTIMETER SETTING AND INCREASE MDA TO 2700 AND VISIBILITY TO 3 MILES.

BLOOMSBURG

Bloomsburg Muni

RWY 07W/25W CLOSED INDEFLY.(10/86)

CLEARFIELD

Clearfield-Lawrence

VASI RWY 12 OTS INDEFLY. (11/86)

CERES

Ceres

ARPT CLSD TO PUBLIC USE. (11/86)

CONNELLSVILLE

Connellsville

FDC 5/1127 /2G3/ FI/T CONNELLSVILLE CONNELLSVILLE PA. LOC RWY 5 ORIG..CIRCLING MDA 2040/HAA 773 CAT A/MDA 2220/HAA 953 CAT B/MDA 2280/HAA 1013 CAT C/MDA 2620/HAA 1353 CAT D. VIS 1 1/2 CAT B. MSA FROM VV NDB 360-270/4400..270-360/3600. VOR-A ORIG.. CIRCLING MDA 2220/HAA 953 CAT B/MDA 2280/HAA 1013 CAT C/MDA 2620/HAA 1353 CAT D. VIS 1 1/2 CAT B.

DUBOIS

DuBois-Jefferson County

ARPT CLSD TO AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT PPR CALL 814-328-2533. (11/86)

FDC 6/1195 /DUJ/ FI/T DU BOIS-JEFFERSON COUNTY, DU BOIS, PA. ILS RWY 25 AMDT 6. TRML ROUTE PARDY INT TO DU LOM NA. PROC TURN NA. MISSED APCH: CLIMB TO 4000 DIRECT CIP VORTAC AND HOLD SOUTH, RT, 015 INBOUND.

FACTORYVILLE

Seamans Field

RWY 04/22 NOW 2000 FEET BY 28 FEET. REIL RWYS 04 AND 22 DCMSND.(10/86)

FRANKLIN

Chess-Lamberton

RWY 20 REIL CMSND. ACTIVATE REIL RWY 20 122.7. (10/86)

Franklin

ARPT CLSD TO PUBLIC USE. (11/86)

FREEDOM

Kindelberger Landing Strip

ARPT CLSD TO PUBLIC USE. (11/86)

GREENVILLE

Greenville Muni

RWY 04/22 NOW 2492 FT BY 310 FT. (11/86)

HAZLETON

Hazelton Muni

RWY 10/28 NOW 4900 FT BY 100 FT. (10/86)

FDC 6/3072 /HZL/FI/T HAZELTON MUNI, HAZELTON PA. LOC RWY 28 AMDT 3..TERMINAL ROUTE ABE VORTAC TO WEISS INT. MEA 5000 FEET.

HONESDALE

Cherry Ridge

RWY 35 THR DSPLCD 50 FT. (11/86)

INDIANA

Indiana County, Jimmy Stewart Fld

FDC 5/1311 /IDI/ FI/T INDIANA COUNTY /JIMMY STEWART FLD. INDIANA PA. NDB-A AMDT 4. CIRCLING MDA 2220/HAA 816 CAT C. VIS 2 1/2 CAT C. MSA FROM INP NDB 315-045-045 3300, 045-315 4200. LOC B AMDT 1. LOC/NDB CIRCLING MDA 2100/HAA 696 CATS A/B..MDA 2220/HAA 816 CAT C VIS 2 1/2 CAT C. MSA FROM INP NDB 315-045 3300, 045-315 4200.

JERSEY SHORE

Jersey Shore

ARPT OPEN TO PUBLIC USE. (10/86)

LANCASTER

Lancaster

FDC 6/3165 /LNS/FI/T LANCASTER, LANCASTER, PA. ILS RWY 8 AMDT 10..S-ILS-8 DH 649/HAT 250/VIS 1 MILE ALL CATS. S-LOC-8 VIS 1 MILE CATS A/B/C. INOP TABLE DOES NOT APPLY TO MALSR. FOR INOP MALSR INCREASE S-LOC-8 VIS CATS C 1/4 MILE CAT D 1/2 MILE. MSA 110 CLKWS 200 2500. VOR RWY 8 AMDT 16 S-8 VIS 1 MILE CATS A/B. FOR INOP MALSR INCREASE S-8 VIS 1/4 MILE CATS A/B. MSA 110 CLKWS 200 2500. VOR RWY 31 AMDT 12 PROCEDURE TURN ALTITUDE 2500. MSA 110 CLKWS 200 2500. VOR/DME RWY 26 AMDT 4 AND VOR/DME RWY 31 ORIG MSA 110 CLKWS 200 2500. VOR/DME OR TACAN RWY 8 AMDT 1 S-8 VIS 1 MILE CATS A/B/C. FOR INOP MALSR S-8 CATS A/B VIS REMAIN 1 MILE INCREASE S-8 CAT C VIS 1/4 MILE. MSA 110 CLKWS 200 2500.

LATROBE

Westmoreland County

FDC 6/1375 /LBE/ FI/T WESTMORELAND COUNTY AIRPORT, LATROBE PA. ILS RWY 23 AMDT 11..MISSED APPROACH..CLIMB TO 4000 VIA BHU 233 BEARING, THEN CLIMBING LEFT TURN TO 5000 DIRECT /IHD/ VORTAC AND HOLD E, RT, 278 INBOUND.

FDC 5/2732 /LBE/ FI/T WESTMORELAND COUNTY, LATROBE PA. IFR DEP PROCS RWY 03..CLIMB RWY HDG TO 2000 THEN CLIMBING LEFT TURN TO 4000 VIA HDG 360 TO INTERCEPT IHD R-002. RWY 05..CLIMB RWY HDG TO 1600, THEN CLIMBING LEFT TURN TO 4000 VIA HEADING 360 TO INTERCEPT IHD R-002. RWY 21..CLIMBING RIGHT TURN TO 4000 VIA HDG 260 TO INTERCEPT BHU NDB 233. RWY 23..CLIMB TO 4000 VIA BHU NDB 233.

MEADVILLE

Port Meadville

REIL RWY 07 OTS INDEFLY. (10/86)

MIDDLETOWN

Harrisburg Intl-Olmsted Field

FDC 6/981 /MDT/ FI/T MIDDLETOWN/HARRISBURG INTL AIRPORT-OLMSTED FLD MIDDLETOWN PA. RADAR-1 AMDT 6 ASR RWY 13 AND ASR RWY 31. PROCS NA.

MT JOY/MARIETTA

Donegal Springs Airpark

FDC 6/3154 /N71/FI/T DONEGAL SPRINGS AIRPARK MT JOY/MARIETTA PA. VOR RWY 27 ORIG. MSA FROM LRP VORTAC 110 CLKWS 200 2500.

NEW CASTLE

New Castle Muni

RWY 05/23 NOW 3993 FT BY 75 FT. RWY 31 THR DSPLCD 400 FT. (10/86)

FDC 6/1659 /2G7/ FI/T NEW CASTLE MUNI NEW CASTLE PA. NDB RWY 23 AMDT 1. NDB/VOR MINS. SI MDA 1740/HAT 710 ALL CATS. CIRCLING MDA 1740/HAA 68 ALL CATS SI AND CIRCLING VIS 2 CAT C 2 1/4 CAT D. TRML ROUTES CUTTA INT TO UCP NDB 3100 VOLAN INT TO UCA NDB 3300 CAPEL INT TO UCP NDB 3400.

PHILADELPHIA

Philadelphia Intl ILS/DME

(I-GLC) RWY 27L OM DCMSD. (10/86)

PHILIPSBURG

Mid-State

FDC 6/2398 /PSB/ FI/T MID-STATE AIRPORT..PHILIPSBURG PA. VOR RWY 24 AMDT 14. PROC NA.

PITTSBURGH

Allegheny County

FDC 6/1724 /AGC/ FI/T ALLEGHENY COUNTY/PITTSBURGH/ PA. TKOF MINS RWY 23 300-1 OR STANDARD WITH A MIN CLIMB OF 320 FEET PER NM TO 1500.

Campbell

RWY 13/31 NOW 5000 FT BY 70 FT. RWYS 13 & 31 REIL DCMSND. (11/86)

Greater Pittsburgh Intl

RWY 10C/28C NOW 8642 FT BY 150 FT. RWY 28C THR DSPLCD 593 FT. RWY 28R VASI DCMSND. (10/86)

FDC 6/327 /PIT/ FI/T GREATER PITTSBURGH INTL, PITTSBURGH, PA. ILS RWY 10L AMDT 21, ILS RWY 10R AMDT 2, ILS RWY 28L AMDT 2, ILS RWY 28R AMDT 3, ILS RWY 32 AMDT 6..CIRCLING MDA 1860/HAA 657 CAT E. VIS 2 1/4 CAT E.

PORT ALLEGANY

Johnson

ARPT CLSD TO PUBLIC USE. (11/86)

PUNXSUTAWNEY

Punxsutawney Muni

FDC 6/1106 /N35/ FI/T PUNXSUTAWNEY MUNI, PUNXSUTAWNEY, PA. VOR/DME-A ORIG. CONTROLLED AIRSPACE ENDS AT 3130 MSL.

FDC 5/1990 /N35/ FI/T PUNXSUTAWNEY MUNI, PUNXSUTAWNEY, PA. IFR DEP PROC/TKOF MINS. RWYS 19/ 24: 300-1. RWY 01: 600-1.

QUAKERTOWN

Quakertown

RWY 11 VASI OTS INDEFLY. (11/86)

ST MARYS

St Marys Muni

FDC 6/2778 /8G5/ FI/T ST MARYS MUNI, ST MARYS, PA.TKOF MINS RWY 28 - 300-1.

SALTSBURG

J & W Landing Strip

ARPT CLSD TO PUBLIC USE. (11/86)

SCHWENKVILLE

Sunset Strip

ARPT CLSD TO PUBLIC USE. (11/86)

SHAMOKIN

Northumberland County

ACTIVATE MIRL RWY 08/26 122.8. (11/86)

SHARON

Hermitage

ARPT CLSD TO PUBLIC USE. (11/86)

SILVERDALE

I G Rosenberger Inc

ARPT CLSD TO PUBLIC USE. (11/86)

WELLSBORO

Oregon Hill

FACILITY ABANDONED. (11/86)

WEST CHESTER

Brandywine

RWY 27 THR DSPLCD 280 FT. (11/86)

WEST GROVE

Ginns

ARPT CLSD TO PUBLIC USE. (11/86)

WILKES-BARRE/SCRANTON

Wilkes-Barre/Scranton Intl

RWY 04/22 NOW 7501 FT BY 150 FT. (11/86)

FDC 6/2009 /AVP/ FI/T WILKES-BARRE/SCRANTON INTL WILKES-BARRE PA..ILS RWY 4 AMDT 31..SI ILS NA. SI LOC VIS CAT A 1 1/4 CAT B 1 1/2 CAT C/D 3. BARTY -LOM/DME MINS..SI LOC VIS CAT A/B 1 1/4 CAT C 2 1/2 CAT D 2 3/4. DELETE ALL NOTES..WHEN ATCT CLSD...NDB-A AMDT 14...DELETE ALL NOTES..WHEN ATCT CLSD...RADAR-1 AMDT 10...ASR RWY 4 VIS CAT A 1 1/4 CAT B 1 1/2 CATS C/D 3.

PENNSYLVANIA

YARDLEY

Yardley VORTAC

(ARD) VOR PORTION UNUSABLE 250-265 BYD 17 NM BELOW 2500 FT; 265-280 BYD 10 NM BELOW 2500 FT; 280-300 BYD 17 NM BELOW 3000 FT; 300-353 BYD 35 NM BELOW 3000 FT. (11/86)

PUERTO RICO

SAN JUAN

Luis Munoz Marin Intl ILS

FDC 6/2542 /SJU/ FI/T LUIS MUNOZ MARIN INTL, SAN JUAN, PR. ILS RWY 10 AMDT 4. ILS UNUSABLE FROM MM INBOUND.

RHODE ISLAND

NORTH KINGSTOWN

Quonset State

FDC 6/3063 /OQU/FIT/QUONSET STATE, NORTH KINGSTOWN, RI. ILS RWY 16 AMDT 2, PROC NA. VOR RWY 34 AMDT 3, PROC NA. TAKEOFF MINIMUMS RWY 16: 300-1.

FDC 5/2797 /OQU/ FI/T QUONSET STATE, NORTH KINGSTOWN RI. RADAR-1 AMDT 3 ASR RWY 34 MDA 460/ HAT 441 ALL CATS. VIS 1 1/2 CAT D.

PROVIDENCE

Theodore Francis Green State

FDC 6/2867 /PVD/ FI/T THEODORE FRANCIS GREEN STATE, PROVIDENCE, RI. VOR/DME RWY 23L AMDT 5. SI VIS RVR 4000 CATS A/B/C. INOP TABLE DOES NOT APPLY. WHEN MALSR INOP SI VIS RVR 5000 CATS A/B/C.

WESTERLY

Westerly State

FDC 6/2244 WST/ WESTERLY STATE, WESTERLY RI. LOC RWY 07 AMDT 2..VOR-A AMDT 8..MSA TMU VOR 360 CW-270 2000. 270CW-360 2600. NDB RWY 07 ORIG..MSA RLS NDB 270CW-090 2600. 090CW-270 1500.

SOUTH CAROLINA

ABBEVILLE

Davis Field

ARPT CLSD TO PUBLIC USE. (11/86)

CHARLESTON

Charleston Executive

FDC 6/156 /JZI/ FI/T CHARLESTON EXECUTIVE..CHARLESTON SC. VOR-A AMDT 7. PROC NA.

CHESTER

Chester Muni

FDC 6/1483 /9A6/ FI/T CHESTER MUNI, CHESTER, SC. VOR/ DME RWY 23 AMDT 3. S-23 MINS NA. CIRCLING ONLY.

SOUTH CAROLINA

GREENVILLE

Greenville Downtown

FDC 6/225 /GMU/ FI/T GREENVILLE DOWNTOWN GREENVILLE SC. ILS RWY 36 AMDT 26. SI ILS DH 1302/HAT 266 ALL CATS. CHANGED TO 521 KHZ.

HILTON HEAD ISLAND

Hilton Head

RWY 03 REIL CMSND. (10/86)

NORTH MYRTLE BEACH

Grand Strand

ACTIVATE REIL RWY 05 124.6. (10/86)

CTLZ HRS 0700-1900 LCL. (10/86)

FDC 6/2926 /CRE/ FI/P GRAND STRAND, NORTH MYRTLE BEACH, SC. NDB RWY 23 AMDT 7; ILS RWY 23 AMDT 6; VOR RWY 5 AMDT 16; VOR RWY 23 AMDT 15; VOR/DME OR TACAN RWY 5 AMDT 2; VOR/DME OR TACAN RWY 23 AMDT 1; ACTIVATE MALSR RWY 23, REIL RWY 5 AND HIRL RWY 5/ 23 CTAF. THIS IS NDB RWY 23 AMDT 8; ILS RWY 23 AMDT 7; VOR RWY 5 AMDT 17; VOR RWY 23 AMDT 16; VOR/DME OR TACAN RWY 5 AMDT 3; VOR/DME OR TACAN RWY 23 AMDT 2.

Grand Strand ATCT

EFFECTIVE 18 DEC 86 ATCT HRS 0700-1920 LCL.(11/86)

Strand FSS

EFFECTIVE 18 DEC 86 OPERATIONAL HRS 0700-1900 LCL. OTHER HRS CONTACT FLORENCE FSS. (11/86)

ORANGEBURG

Orangeburg Muni

ACTIVATE ODALS & REIL RWY 04 122.7. (11/86)

FDC 6/3143 /OGB/FI/T ORANGEBURG MUNI, ORANGEBURG, SC..NDB-A AMDT 6..PROC NA.

Orangeburg NDB

(OGB) DCMSND. (11/86)

SUMMERVILLE

Dorchester County

NEWLY REPORTED FACILITY. OPEN TO PUBLIC USE. RWY 05/23 3700 FT BY 75 FT, ASPH, MIRL. (10/86)

J. E. Locklair Memorial

FACILITY ABANDONED. (11/86)

WALTERBORO

Walterboro Muni

RWY 17 THR NO LONGER DSPLCD. (10/86)

SOUTH DAKOTA

BELLE FOURCHE

Belle Fourche Muni

NEWLY REPORTED FACILITY. OPEN TO PUBLIC USE. RWY 14/32 4500 FT BY 75 FT, ASPH, MIRL CMSND. RWY 18/36

SOUTH DAKOTA

3600 FT BY 150 FT, TURF. ACTIVATE MIRL RWY 14/32 122.8. (11/86)

HURON

Huron Regional ILS/DME

(I-HON) RWY 12 GS UNMONITORED. (11/86)

TENNESSEE

CHATTANOOGA

Lovell Field

FDC 6/217 /CHA/ FI/T LOVELL FIELD/CHATTANOOGA/TN. ILS RWY 20 AMDT 33. WHEN ATCT CLSD SI ILS VIS RVR 2400 ALL CATS.

MADISONVILLE

Monroe County

FDC 6/255 /MNV/ FI/T MONROE COUNTY/MADISONVILLE/ TN. NDB RWY 5 AMDT 2. SI AND CIRCLING MDA 2160/HAT-HAA 1129 ALL CATS. SI AND CIRCLING VIS 1 1/2 CAT B/3 CAT C.

MEMPHIS

Memphis Intl ILS

(I-MEM) RWY 09 USABLE. (10/86)

MORRISTOWN

Ha-Le-Copters Inc Heliport

NEWLY REPORTED FACILITY. OPEN TO PUBLIC USE. HELIPAD 20 FT BY 20 FT, ASPH. (11/86)

NASHVILLE

Nashville Metropolitan

RWY 31 REIL CMSND.(10/86)

FDC 6/2960 /BNA/ FI/T NASHVILLE METROPOLITAN, NASHVILLE, TN. ILS RWY 31 AMDT 5 S-ILS DH 826/HAT 250 VIS 3/4 ALL CATS. S-LOC VIS 3/4 CATS A/B.

FDC 6/2942 /BNA/ FI/T NASHVILLE METROPOLITAN, NASHVILLE, TN. EFFECTIVE MON THRU SAT 0600 TO 1800 LOCAL EXCEPT WHEN ATC ADVISES CRANE IS DOWN. RADAR-1 AMDT 20... ASR RWY 2L... SI MDA 1040/HAT 441 ALL CATS. CIRCLING MDA 1100/HAA 501 CATS A/B. NDB RWY 20R AMDT 4 DME MINS...VOR RWY 31 AMDT 25 DME MINS...ILS RWY 20R AMDT 4 DME OR RADAR MINS...ILS RWY 2L AMDT 5...ILS RWY 31 AMDT 5...VOR/DME RWY 13 AMDT 10...VOR/DME RWY 20L AMDT 2...VOR/DME RWY 20R AMDT 4...CIRCLING MDA 1100/HAA 501 CATS A/B.

FDC 6/2808 /BNA/ FI/T NASHVILLE METROPOLITAN, NASHVILLE, TN. VOR/DME RWY 20L AMDT 2. EFFECTIVE MON-FRI 0600 TO 1700 LCL. SI MDA 1000/HAT 410 ALL CATS. SI VIS 1 1/4 CAT C.

ONEIDA

Oneida/Scott Muni

FDC 6/1526 /SCX/ FI/T ONEIDA/SCOTT MUNI, ONEIDA, TN. SDF RWY 23, AMDT 1. NDB RWY 23, AMDT 1. DISTANCE FAF TO MAP AND THR 6.9 NM.

TENNESSEE

PULASKI

Abernathy Field

FDC 6/1899 /GZS/ FI/T ABERNATHY FIELD, PULASKI, TN. NDB RWY 15 AMDT 2...SI MINS NA. GZS NDB LOCATED EAST OF RWY 15/33.

SOMERVILLE

Fayette County

RWY 18/36 OPEN. MIRL RWY 18/36 OTS INDEFLY.(11/86)

TEXAS

ABILENE

Abilene Muni

WHEN ATCT CLSD CONTACT ABI APCH ON 120.1 FOR CFR SERVICE. (10/86)

AMARILLO

Amarillo Intl

FDC 6/2669 /AMA/ FI/T AMARILLO INTL, AMARILLO, TX. IFR TAKEOFF MINIMUMS RWY 31. TURN RIGHT AFTER TAKEOFF TO AVOID 5047 FOOT TOWER 8.2 NM NW OF ARPT.

Tradewind

FDC 6/2668 /TDW/ FI/T TRADEWIND, AMARILLO, TX. IFR TAKE-OFF MINIMUMS RWYS 5, 23, 35: 600-2 OR STANDARD WITH MINIMUM CLIMB OF 300 FT PER NM TO 6000 FT.

ANGLETON/LAKE JACKSON

Brazoria County

FDC 6/862 /LBX/ FI/T ANGLETON/LAKE JACKSON/ BRAZORIA COUNTY TX. ILS RWY 17 AMDT 1...NDB RWY 17 AMDT 1.. INCREASE TRML RTE /VUH/VORTAC 256 RADIAL TO FREEP LOM TO ALT 3000.

AUSTIN

Lakeway Airpark

FDC 6/2762 /3R9/ FI/T LAKEWAY AIRPARK AUSTIN TX. VOR/ DME-C ORIG TERMINAL ROUTE FROM R-008 AUS VORTAC CCW /IAF/TO R-277 27 DME ARC 4100. FROM 27 DME ARC TO DONHO 20 DME AUS R-277/7 3100.

Robert Mueller Muni

RWY 13L/31R NOW 4000 FT BY 75 FT, MIRL CMSND. (11/86)

BRENHAM

Brenham Muni

FDC 6/962 /11R/ FI/T BRENHAM MUNI, BRENHAM, TX. NDB RWY 16 AMDT 2. ADD NOTE...WHEN COLLEGE STATION ALTIMETER SETTING NOT AVAILABLE USE HOUSTON INTERCONTINENTAL ALTIMETER SETTING AND INCREASE ALL MDAS 160 FT.

BRIDGEPORT

Bridgeport VORTAC

(BPR) VOR PORTION UNUSABLE 270-300 BYD 15 NM BLO 4000 FT; 300-330 BYD 15 NM BLO 3000 FT; 330-360 BYD 30 NM BLO 3000 FT. (10/86)

BROWNSVILLE

Brownsville/South Padre Island Intl

RWY 13L/31R CLSD TIL 01 JAN 87. (10/86)

RWY 35 VASI CMSND. (11/86)

BRYAN

Coulter Field

FDC 6/961 /CFD/ FI/T COULTER FIELD, BRYAN TX. VOR/DME-A AMDT 1. ADD NOTE..WHEN COLLEGE STATION ALTIMETER SETTING NOT AVAILABLE USE HOUSTON INTERCONTINENTAL ALTIMETER SETTING AND INCREASE ALL MDAS 300 FT.

CALDWELL

Caldwell Muni

FDC 6/2486 / 14R/ CALDWELL MUNI, CALDWELL, TX. VOR/DME-A ORIG..MSA CLL VORTAC 360-100 3100. 100-360 1900.

FDC 6/963 /14R/ FI/T CALDWELL MUNI, CALDWELL, TX. VOR/DME-A ORIGINAL. ADD NOTE..WHEN COLLEGE STATION ALTIMETER SETTING NOT AVAILABLE PROCEDURE NA.

CANADIAN

Hemphill County

RWY 18/36 THR DSPLCD 95 FT. (11/86)

CARRIZO SPRINGS

Dimmet Co.

FDC 5/2117 /CZT/ FI/T DIMMET CO. CARRIZO SPRINGS TX. NDB RWY 30 ORIG REDESIGNATE NDB RWY 31 ORIG. IFR DEPARTURE PROC..RWY 31 CLIMB ON RWY HEADING TO 1200 PRIOR TO LEFT TURN.

CASTROVILLE

Castroville Muni

FDC 5/2347 /T89/ FI/T CASTROVILLE MUNI, CASTROVILLE TX NDB RWY 33 ORIG. MSA FROM CVB NDB 270-090 4100 FEET, 090-270 2600 FEET.

CLEBURNE

Cleburne Muni

FDC 5/2913 /F18/ FI/T CLEBURNE MUNI CLEBURNE TX. RNAV RWY 33 ORIG..CIRCLING MDA 1340/HAA 483 ALL CATS.

COLLEGE STATION

Easterwood Field

FDC 6/959 /CLL/ FI/T EASTERWOOD FIELD, COLLEGE STATION, TX. NDB RWY 34 AMDT 6/ILS RWY 34 AMDT 6/LOC BC RWY 16 AMDT 1/ VOR RWY 28 AMDT 7/VOR OR TACAN RWY 10 AMDT 15. ADD NOTE. WHEN COLLEGE STATION FSS NOT IN OPERATION THE FOLLOWING APPLIES..USE HOUSTON INTERCONTINENTAL ALTIMETER SETTING AND INCREASE ALL DHS AND MDAS 300 FT..ALTERNATE MINIMUMS NA.

CORPUS CHRISTI

Cabaniss Field NALF

CTLZ HRS 0800-2330 LCL MON-FRI EXCEPT HOLIDAYS.(10/86)

Corpus Christi Intl

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS 2400-0530 LCL EXCEPT PPR CALL 512-289-0226. CFR SERVICE UNAVAILABLE TO NON-AIR CARRIER AIRCRAFT 2400-0530 LCL EXCEPT BY PPR. (10/86)

RWY 17/35 CLSD TIL 15 JAN 87. (11/86)

DALHART

Dalhart Muni

FDC 6/2419 /DHT/ FI/T DALHART MUNI DALHART TX.VOR RWY 17 AMDT 10..IFR TKOF MINS RWY 3 600-2.

DALLAS

Dallas-Ft Worth Intl

ILS/DME RWY 13R (I-LWN) CMSND. LOC FREQ 109.5 & GS FREQ 332.6. (9/86)

NEW RWY 13R/31L 9300 FT BY 150 FT, HIRL. RWY 13R MALS CMSND.(10/86)

FDC 6/3047 /DFW/FI/T DALLAS/FORT WORTH INTERNATIONAL..DALLAS FORT WORTH TX. ILS RWY 31R AMDT 5. AUTO-PILOT COUPLED APCHS NA.

FDC 6/249 /DFW/ FI/T DALLAS-FT WORTH INTL, DALLAS TX. ILS RWY 31R AMDT 4..AUTO-PILOT COUPLED APCHS NA.

FDC 6/1813 /DAL/ FI/T DALLAS-LOVE FIELD, DALLAS, TX. ILS 31L AMDT 15, S-ILS 31L NA. S-LOC 31L MDA 1600, HAT 1125 ALL CATS. CIRCLING 1600 HAA 1113 ALL CATS. ENTRA DME FIX RELOCATED LUE 4.1 DME. REASON: 889 AGL 1339 AMSL CRANE 3.9 NM SE OF AIRPORT.

DEVINE

Devine NDB

(HHH) OUT OF SERVICE INDEFLY. (10/86)

DUMAS

Durrett NDB

(DUX) CONTROLLING FSS AMA. (10/86)

EL CAMPO

El Campo NDB

(ECE) CONTROLLING FSS CXO. (10/86)

EL PASO

West Texas

RWY 08/26 NOW 4100 FT BY 50 FT. (10/86)

FORT WORTH

Mangham Fld

FACILITY ABANDONED. (11/86)

GEORGETOWN

Georgetown Muni

FDC 6/2763 /TO4/ FI/T GEORGETOWN MUNI GEORGETOWN TX. NDB RWY 18 AMDT 2 TERMINAL ROUTE FROM KATES INT TO GUO NDB 090/29.3 4100. MSA FROM GUO NDB 360-240 3100 240-360 4200.

GRANBURY

Granbury Muni

FDC 5/1588 /F55/ FI/T GRANBURY MUNI, GRANBURY, TX. IFR TAKEOFF MIN RWY 14 300-1. RWY 32 STANDARD.

GREENVILLE

Majors

FDC 6/114 /GVT/ FI/T MAJORS, GREENVILLE, TX. ILS RWY 17, AMDT 2. CHANGE CTLZ NOTE TO: WHEN CTLZ NOT IN EFFECT, USE DALLAS LOVE FIELD ALTIMETER SETTING AND INCREASE ALL DH/MDAS 200 FEET.

GRUVER

Gruver NDB

(GVX) CONTROLLING FSS AMA. (10/86)

HARLINGEN

Rio Grande Valley Intl

FDC 6/2445 /HRL/ FI/T RIO GRANDE VALLEY INTL, HARLINGEN TX. VOR RWY 13 AMDT 9 MISSED APPROACH.CLIMB TO 2000 LEFT TURN DIRECT HRL VOR/ DME AND HOLD. PROCEDURE TURN RIGHT SIDE OF COURSE 287 OUTBOUND 2000 FT WITHIN 10 MI OF HRL VOR/PT NA CAT E/.

HASKELL

Haskell Muni

FDC 6/438 /15F/ FI/T HASKELL MUNI.HASKELL TX. NDB RWY 18 AMDT 1. ACTIVATE MIRL RWY 18/36 122.8.

HIGGINS

Higgins-Lipscomb Co

RWY 18 THR DSPLCD 180 FT.(11/86)

HOUSTON

Baytown

FDC 6/1894 /HPY/ FI/T BAYTOWN, HOUSTON, TX. NDB RWY 13 ORIG. NDB RWY 31 AMDT 2. VOR RWY 13 ORIG. VOR RWY 31 AMDT 1 PROC NA.

David Wayne Hooks Memorial

FDC 6/250 /DWH/ FI/T DAVID WAYNE HOOKS MEM. HOUSTON TX. NDB RWY 17R AMDT 9...S-I MDA 580 HAT 430 ALL CATS VIS CAT D 1 1/2 MILES.

Ellington Fld

RWY 04/22 HIRL CMSND. (11/86)

FDC 5/2866 /EFD/ FI/T ELLINGTON FIELD, HOUSTON, TX. ILS RWY 35, ORIG NOW ILS RWY 35L, ORIG: VOR/DME OR

TACAN RWY 35, ORIG NOW VOR/DME OR TACAN RWY 35L, ORIG: ILS RWY 17, ORIG NOW ILS RWY 17R, ORIG: VOR/DME OR TACAN RWY 17, ORIG: NOW VOR/DME OR TACAN RWY 17R, ORIG. ILS RWY 17R, VOR/DME OR TACAN 17R, ILS RWY 35L, VOR/DME OR TACAN RWY 35L, VOR/DME OR TACAN RWY 4, ORIG. VOR/DME OR TACAN RWY 22, ORIG: CHANGE NOTE TO: CIRCLING NOT AUTHORIZED WEST OF RWYS 17R-35L.

Houston Intercontinental

FDC 6/1186 /IAH/ FI/T HOUSTON INTERCONTINENTAL, HOUSTON, TX. NDB RWY 8, AMDT 9. SI MDA 580, HAT 483 ALL CATS.

KILLEEN

Killeen Muni

FDC 6/2782 /ILE/ FI/T KILLEEN MUNI/KILLEEN/TX. ILS RWY 1 ORIG..NDB RWY 1 ORIG..NDB RWY 1 AMDT 3...MSA FROM IL LOM 360-180 3600/ 180-360 4200. VOR-A AMDT 2 MSA FROM GRK VOR/DME 360-180 3100/ 180-360 4200.

LAREDO

Laredo Intl

REIL RWY 35L OTS INDEFLY. (11/86)

FDC 6/1870 /LRD/ FI/T LAREDO INTERNATIONAL, LAREDO, TX. VOR/DME OR TACAN RWY 14 AMDT 5. S-14 MDA 920 HAT 412 ALL CATS VIS CAT C 1 1/4. CIRCLING MDA 980 HAA 472 CAT A. ILS RWY 17R AMDT 7. VOR OR TACAN RWY 32 AMDT 6. CIRCLING MDA 980 HAA 472 CAT A.

FDC 5/2551 /LRD/ FI/T LAREDO INTERNATIONAL, LAREDO, TX. LOC BC RWY 35L, ORIGINAL, PROCEDURE NA.

LUBBOCK

Lubbock Intl

FDC 6/3042 /LBB/ FI/T LUBBOCK INTL, LUBBOCK, TX. NDB RWY 8 ORIG...NDB RWY 17R AMDT 14...NDB RWY 26 AMDT 1...ILS RWY 17R AMDT 15...ILS RWY 26 AMDT 1...LOC BC RWY 35L AMDT 12...VOR A AMDT 4...VOR/DME OR TACAN RWY 26 AMDT 7...RNAV RWY 8 AMDT 1...RADAR 1 AMDT 6...CIRCLING CAT A MDA 3720, HAA 439.

LUFKIN

Angelina County

FDC 6/3089 /LFK/FI/T ANGELINA COUNTY..LUFKIN TX. LOC RWY 7 ORIG. NDB RWY 7 ORIG...CHANGE MISSED APPROACH TO READ: CLIMB TO 2000 THEN RIGHT TURN DIRECT FLUFY /LF/LOM.

MCKINNEY

Mc Kinney Muni

FDC 5/2720 /TKI/ FI/T MCKINNEY MUNI MCKINNEY TX. NDB RWY 17 AMDT 1 SI-17 MDA 1480 HAT 902 ALL CATS. VIS CAT A 1 1/4 CAT C 2 3/4 MI. CIRCLING MDA 1480 HAA 900 ALL CATS. VIS CAT A 1 1/4 CAT C 2 3/4 MI.

NAVASOTA

Navasota Muni

RWY 17/35 NOW 3180 FT BY 60 FT. RWY 17/35 LIRL DCMSND. (11/86)

FDC 6/960 /GOR/ FI/T NAVASOTA MUNI, NAVASOTA, TX. VOR-A AMDT 1. ADD NOTE..WHEN COLLEGE STATION ALTIMETER SETTING NOT AVAILABLE USE HOUSTON INTERCONTINENTAL ALTIMETER SETTING AND INCREASE ALL MDAS 140 FT.

FDC 5/2693 /60R/ FI/T NAVASOTA MUNI NAVASOTA TX. VOR-A AMDT 1 PROCEDURE NA.

ORANGE

Orange County

RWYS 03 & 21 VASI DCMSND. (10/86)

PARIS

Paris VOR

(PRX) DME CMSND. (10/86)

PERRYTON

Perryton Ochiltree County

RWY 17/35 NOW 5000 FT BY 75 FT. (11/86)

SABINE PASS

Sabine Pass RCO

COLOCATED WITH SABINE PASS VORTAC DCMSND. (11/86)

Sabine Pass VORTAC

(SBI) CONTROLLING FSS CXO. (11/86)

SAN ANGELO

Mathis Field

RWYS 18 & 36 VASI OTS TIL 01 JAN 87. (10/86)

SAN ANTONIO

Elm Creek VOR/DME

(XEC) VOR DCMSND.(10/86)

San Antonio Intl

RWY 03/21 NOW 7505 FT BY 150 FT. RWY 12L/30R NOW 5437 FT BY 100 FT. RWY 12R/30L NOW 8502 FT BY 150 FT. (11/86)

FDC 6/3034 /SAT/ FI/T SAN ANTONIO INTL, SAN ANTONIO, TX. VOR RWY 21 AMDT 1, VOR RWY 3 ORIG..PROCEDURES NA. RADAR-1 AMDT 22; ASR RWY 21: FAF 5.6 NM FROM THR, MIN ALT 2900, MIN ALT 3 MI. FIX 1920, MANDATORY, FINAL APCH CRS 207. RECOMMENDED ALT 5 MI. 2680, 4 MI., 2300, 3 MI. 1920 MANDATORY, 2 MI, 1540.

FDC 5/2453 /SAT/ FI/T SAN ANTONIO INTL SAN ANTONIO TX. NDB RWY 3 AMDT 35 NDB RWY 12R AMDT 19 NDB RWY 30L AMDT 8 ILS RWY 3 AMDT 13 ILS RWY 12R AMDT 9 ILS RWY 30L AMDT 6 VOR-A AMDT 3 MSA FROM SA NDB/AN NDB/SAT VORTAC 270-090 4100/090-270 3200.

FDC 5/2052 /SAT/ FI/T SAN ANTONIO INTL..SAN ANTONIO, TX. NDB RWY 3 AMDT 35 SI MDA 1420 HAT 636 ALL CATS. VIS CAT C 1 3/4 CAT D 2. CIRCLING MDA 1420/HAA 611 ALL CATS. VIS CAT C 1 3/4. ILS RWY 3 AMDT 13..S-ILS DH 1034/ HAT 250 ALL CATS. S-LOC MDA 1180/HAT 396 ALL CATS. VIS CAT D 1 1/4. CIRCLING CATS A/B/C 1320/HAA 511. RADAR 1 AMDT 22 ASR RWY 3 MDA 1360 /HAT 576 ALL CATS. VIS CAT C 1 1/2. CAT D 1 3/4 ASR RWY 12R MDA 1260/HAT 471 ALL CATS CIRCLING MDA 1360/HAA 551 CATS A/B/C. INOP TABLE DOES NOT APPLY TO MALS RWY 3 FOR CAT C. RNAV 30L AMDT 8 CIRCLING MDA 1320/HAA 511 CATS A/B/C. IFR TAKEOFF MINS RWY 21 300-2. TEMPORARY CONSTRUCTION CRANES 1020..1105 MSL 0.5NM SW OF AIRPORT...1019 MSL 1.6NM NORTH AER 12R.

SAN MARCOS

San Marcos Muni

FDC 6/2701 /T98/ FI/T SAN MARCOS MUNI, SAN MARCOS, TX..ILS RWY 12 AMDT 1...MISSED APPROACH - CLIMB TO 2000, THEN CLIMBING LEFT TURN TO 3200 DIRECT GARYS LOM/INT AND HOLD. S-12 VIS ALL CATS 3/4. S-LOC 12 CATS A/B 1, CAT C/D 1 1/2, CAT E 1 3/4. DISREGARD ACTIVATE MALSR RWY 12 - CTAF NOTE.

SHERMAN-DENISON

Grayson County

RWY 17R/35L PERMANENTLY CLSD. RWY 17L/35R CHANGED TO 17/35. ARPT HAS LIMITED FAR PART 139 CERTIFICATE FOR OPERATIONS ON RWY 17/35. (11/86)

TEMPLE

Draughon-Miller Muni

RWY 15/33 HIRL CHANGED TO MIRL. (11/86)

FDC 6/3024 /TPL/FI/T DRAUGHON-MILLER MUNI, TEMPLE, TX. LOC/DME BC RWY 33 ORIG. SI MDA 1040/HAT 365; VIS 1 1/4 CAT D. VOR RWY 15 AMDT 13; LOC/DME RWY 33 ORIG; ILS RWY 15 AMDT 7; CIRCLING MDA 1120/HAA 438 CAT A.

THROCKMORTON

Throckmorton Muni

ARPT CLSD INDEFLY. (10/86)

VERNON

Wilbarger County

RWY 20 VASI CMSND. (11/86)

ACTIVATE VASI RWY 20 KEY 122.8.(10/86)

WACO

Tsti-Waco

FDC 6/2469 /CNW/ FI/T TSTI-WACO, WACO, TX. NDB 17L, AMDT 7, SI-MDA 980, HAT 511 ALL CATS, VIS CAT C 1 1/2. CIRCLING MDA 980, HAA 511 CATS A/B.(REASON: 662 TOWER 1.7 NM NW AER 17L)

Waco-Madison Cooper

RWY 05/23 CLSD PERMLY. (11/86)

FDC 5/1961 /ACT/ FI/T WACO-MADISON COOPER, WACO, TX. ILS RWY 19 AMDT 11..FEEDER ROUTE BOSEL INT TO COFFI LOM MIN ALT 2800.

WHEELER

Wheeler Muni

RWY 17/35 NOW 3500 FT BY 60 FT. RWY 35 THR NO LONGER DSPLCD. (11/86)

TEXAS

WICHITA FALLS

Kickapoo Downtown Airpark

FDC 6/2640 /T47/ FI/T KICKAPOO DOWNTOWN AIRPARK.WICHITA FALLS TX. NDB-A AMDT 4. CHANGE MISSED APPROACH TO ..CLIMB TO 2000 THEN CLIMBING LEFT TURN TO 3000 DIRECT TO SPS VORTAC.

Wichita Falls Muni

FDC 6/3041 /SPS/ FI/T SHEPPARD AFB, WICHITA FALLS MUNI, WICHITA FALLS, TX. TAKEOFF MINIMUMS: RWY 33L/33R/35 STANDARD RWYS 15L/15R/17 600-2 OR STANDARD WITH MINIMUM CLIMB OF 290 FT PER NM TO 2100 FT. IFR DEPARTURE PROCEDURES: COMPLY WITH RADAR VECTORS OR; PLAN DEPARTURE TO AVOID 2043 FT TOWER 4.3 NM SSW OF AIRPORT OR MAINTAIN A MINIMUM CLIMB OF 290 FT PER NM TO 2100 FT.

UTAH

BLANDING

Blanding Muni

FDC 6/2747 /BDG/ FI/T BLANDING MUNI, BLANDING, UT. NDB RWY 35 AMDT 4..PROC NA.

BONNEVILLE

Bonneville VORTAC

(BVL) CONTROLLING FSS CDC. (11/86)

CEDAR CITY

Cedar City Muni

FDC 6/650 /CDC/ FI/T CEDAR CITY MUNI, CEDAR CITY UT. TAKEOFF MINIMUMS RWYS 2-20-26, STANDARD. RWY 8, 3500-3. IFR DEPARTURE PROCEDURE, RWY 20 AND 26 TURN RIGHT, RWYS 2 AND 8 TURN LEFT, CLIMB DIRECT CDC VOR/DME. CONTINUE CLIMB TO 9000 VIA R-348. NORTHBOUND CONTINUE ON COURSE. ALL OTHERS REVERSE COURSE AND CLIMB TO CROSS CDC VOR/DME AT OR ABOVE MCA FOR DIRECTION OF FLIGHT.

DELLE

Delle RCO

FREQ 122.2 DCMSND. FREQ 122.5 CMSND. (11/86)

LOGAN

Logan-Cache

FDC 6/2746 /LGU/ FI/T LOGAN-CACHE, LOGAN, UT. NDB-B AMDT 4..PROC NA.

MOAB

Canyonlands Field

RWY 03/21 NOW 5999 FT BY 75 FT. (11/86)

OGDEN

Ogden Muni

ARPT CLSD TO AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS EXCEPT PPR CALL 801-399-8251. (11/86)

PRICE

Carbon VOR/DME

(PUC) CONTROLLING FSS CDC. (11/86)

UTAH

PROVO

Provo Muni

FDC 6/3160 /PVH/FI/T PROVO MUNI, PROVO, UT. TAKEOFF MINIMUMS RWY 6 NOT AUTHORIZED..RWYS 13 & 18..2600-2 OR STANDARD WITH MIN CLIMB OF 285 FT/NM TO 8000...RWY 24 STD..RWYS 31 & 36...3200-2 OR STANDARD WITH MIN CLIMB OF 330 FT/NM TO 7200...IFR DEPARTURE PROCEDURE RWYS 13 & 18...TURN RIGHT..RWYS 24/31/36 TURN LEFT CLIMB VIA PVU R-228 TO CROSS PVU 16 DME (FFU R-185) AT OR ABOVE 7600 THEN CLIMBING RIGHT TURN VIA FFU R-215 TO FFU VORTAC. ACFT N-BOUND V21 CLIMB ON COURSE. ALL OTHERS CLIMB IN HOLDING PATTERN (HILD S, RT, 346 INBOUND) TO DEPART FFU VORTAC AT OR ABOVE MCA FOR DIRECTION OF FLIGHT. CONTINUE CLIMB ON COURSE TO MEA OR ASSIGNED ALTITUDE.

FDC 4/3006 /PVU/ FI/T PROVO MUNI, PROVO, UTAH. ILS RWY 13 AMDT 1, S-ILS-13 VIS ONE MILE ALL CATS. S-LOC 13, VIS ONE MILE CATS ABC VOR/DME RWY 13, AMDT 2, S-13 VIS ONE MILE CATS ABC ADD NOTE: INOPERATIVE TABLE DOES NOT APPLY.

VERMONT

BARRE-MONTPELIER

Edward F. Knapp State

FDC 6/3196 /MPV/FI/T EDWARD F KNAPP STATE, BARRE-MONTEPELIER VT. NDB RWY 35 AMDT 2...TRML ROUTE DAVID INT TO MWX NDB NA. VOR RWY 35 AMDT 1...TRML ROUTE LEB VOR/DME /IAF/TO MPV VOR/DME /NOPT/NA.

FDC 6/903 /MPV/ FI/T EDWARD F KNAPP STATE, BARRE-MONTPELIER, VT. ILS RWY 17 AMDT 1. SI ILS VIS 3/4 ALL CATS. LOC RWY 17 AMDT 3. OM MINIMA SI VIS 3/4 CATS A/B.

BENNINGTON

Bennington State

FDC 6/1942 /5B5/ FI/T BENNINGTON STATE, BENNINGTON, VT. VOR-A AMDT 7. GRISY INT DME RQRD.

BURLINGTON

Burlington Intl

FDC 6/2993 /BTV/ FI/T BURLINGTON INTL BURLINGTON VT. HI-ILS/DME 1 RWY 15 AMDT 4 PROC NA.

FDC 5/2942 /BTV/ FI/T BURLINGTON INTL, BURLINGTON, VT. RADAR-1 AMDT 3, ASR RWY 1 MDA 1220/HAT 887. VIS 1 1/4 CAT A, 2 3/4 CAT C, 3 CAT D.

HIGHGATE

Franklin County State

FDC 5/2875 /1B7/ FI/T FRANKLIN COUNTY STATE, HIGHGATE, VT. VOR-A AMDT 2. DME MINS NA.

RUTLAND

Dyer NDB

(DYO) UNUSABLE 330-180 BYD 12 NM; 180-330 BYD 15 NM. (10/86)

Rutland State

FDC 6/3197 /RUT/FI/T RUTLAND STATE, RUTLAND VT. LDA RWY 19 AMDT 3...TRML ROUTE EDERT INT TO IRA NDB NA.

VERMONT

SPRINGFIELD

Hartness State (Springfield)

FDC 6/3194 /VSF/FT/T HARTNESS STATE /SPRINGFIELD/, SPRINGFIELD, VT. NDB-A AMDT 4...LOC-A AMDT 3...LOC/DME RWY 5 AMDT 2...TRML ROUTE JAMMA INT TO SXD NDB NA.

WEST DOVER

Mount Snow

FDC 6/1936 /4V8/ FI/T MOUNT SNOW, WEST DOVER, VT. NDB RWY 1 ORIG. TRML ROUTE BRATS INT TO VWD NDB NA.

VIRGIN ISLANDS

CHRISTIANSTED ST. CROIX

Alexander Hamilton

FDC 5/2987 /STX/ FI/T ALEXANDER HAMILTON CHRISTANSTED ST. CROIX V.I. ILS RWY 9 AMDT 4...TERMINAL ROUTE SNOOZ INT TO PESTE LOM NA.

VIRGINIA

ABINGDON

Virginia Highlands

FDC 6/2115 /6A8/ FI/T VIRGINIA HIGHLANDS, ABINGDON, VA. VOR/DME-B AMDT 4. CIRCLING MDAS 2920/HAA 860 CATS A/B.

BLACKSBURG

Virginia Tech

FDC 6/1419 /BCB/ FI/T VIRGINIA TECH, BLACKSBURG, VA. NDB-A ORIG. CHANGE NOTE TO READ: OBTAIN LCL ALSTG ON UNICOM, WHEN NOT AVBL USE ROANOKE ALSTG AND INCREASE ALL MDAS TO 3640 AND VIS CATS A/B TO 3.

BROOKNEAL

Campbell County

FDC 6/1114 /OV4/ FI/T BROOKNEAL/CAMPBELL COUNTY BROOKNEAL VA..VOR/DME-A ORIG. PROC NA.

CHARLOTTESVILLE

Charlottesville-Albemarle

ARPT CLSD TO AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS, SUN-FRI 2230-0500 LCL; SAT 2130-0530 LCL EXCEPT 8 HRS PPR CALL 804-973-8341. (10/86)

FDC 5/2651 /CHO/ FI/T CHARLOTTESVILLE-ALBEMARLE. CHARLOTTESVILLE VA. RNAV RWY 3 AMDT 4 PROC NA.

CHASE CITY

Chase City Muni

FDC 6/998 /CXE/ FI/T CHASE CITY MUNI..CHASE CITY VA. NDB RWY 36 AMDT 1. SI MDA 1220/HAT 717 ALL CATS. VIS 2 CAT C..2 1/4 CAT D. CIRCLING MDA 1220/HAA 717 CATS A/B/C. VIS 2 CAT C.

CULPEPER

Culpeper County T. I. Martin Field

ARPT NAME CHANGED TO CULPEPER COUNTY. (10/86)

VIRGINIA

GORDONSVILLE

Gordonsville Muni

FDC 6/1054 /GVE/ FI/T GORDONSVILLE MUNI, GORDONSVILLE VA. VOR-A AMDT 2...PROC NA.

MARTINSVILLE

Bales NDB

(VDB) EFFECTIVE 18 DEC 86 NAV IDENTIFIER TO BE CHANGED TO UV. (11/86)

Blue Ridge SDF

(UVM) EFFECTIVE 18 DEC 86 OM/LOM, LOM FREQ 396, CMSND. (11/86)

NEWPORT NEWS .

Patrick Henry Intl

ARPT CLSD TO UNSCHEDULED AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS WHEN TWR CLSD EXCEPT 15 MIN PPR CALL 804-877-0221. (10/86)

FDC 6/2589 /PHF/ FI/T PATRICK HENRY INTL, NEWPORT NEWS VA..LOC BC RWY 25 AMDT 12...BACK CRS UNUSABLE BEYOND 15 NM, BACK CRS DME UNRESTRICTED.

NORFOLK

Norfolk Intl

FDC 6/2717 /ORF/ FI/T NORFOLK INTL..NORFOLK VA. ILS RWY 5 AMDT 21. S-ILS 5..S-LOC 5 RVR ALL CATS 4000. INOPERATIVE TABLE DOES NOT APPLY TO S-ILS 5. INCREASE S-LOC 5 VISIBILITY CATS A/B/C TO RVR 5000.CAT D TO RVR 6000 FOR INOPERATIVE MALSR. TEMP CRANE 112 FT MSL .2NM WEST OF AIRPORT.

FDC 6/527 /ORF/ FI/T NORFOLK INTL, NORFOLK, VA. VOR/DME RWY 14 AMDT 1 AND RNAV RWY 14 AMDT 4. PROCS NA.

ORANGE COUNTY

Orange County

FDC 6/1055 /W93/ FI/T ORANGE COUNTY, ORANGE COUNTY, VA VOR/DME-A AMDT 2...PROC NA.

RICHMOND

Richmond Intl/Byrd Field

FDC 6/2718 /RIC/ FI/T RICHMOND INTL/BYRD FIELD..RICHMOND VA. VOR RWY 34 AMDT 19..S-34 DME MINS MDA 600 HAT 438 ALL CATS. VIS CAT C RVR 4000. DELETE INOPERATIVE TABLE NOTE. RADAR-1 AMDT 9..ASR-34 MDA 600 HAT 438 ALL CATS. VIS CAT C RVR 4000. TEMP CRANE 332 FT MSL 3/4 MI SW ARPT.

FDC 6/1731 /RIC/ FI/T RICHMOND INTL/BYRD FIELD. RICHMOND VA. MLS RWY 2 AMDT 1 PROC NA.

ROANOKE

Roanoke Regional/Woodrum Field

FDC 6/3057 /ROA/FI/T ROANOKE REGIONAL/WOODRUM FIELD, ROANOKE, VA..LDA RWY 5 AMDT 5...PROCEDURE TURN ALTITUDE 5100 MSL.

VIRGINIA

STAUNTON/WAYNESBORO/HARRISONBURG

Shenandoah Valley

REIL RWY 23 OTS INDEFLY. (10/86)

TANGIER

Tangier Island

FDC 6/1381 /TGI/ FI/T TANGIER ISLAND TANGIER VA. VOR/DME RWY 2 AMDT 5..PROC NA AT NIGHT.

WASHINGTON

ALMIRA

J-Z

ARPT CLSD WINTER MONTHS. (10/86)

AUGSPURGER MOUNTAIN

Augspurger Mountain RCO

FSS SEA. (11/86)

BREMERTON

Bremerton National

RWY 01 REIL DCMSND. (10/86)

RWY 16/34 NOW 5122 FT BY 150 FT. RWY 16 THR DSPLCD 140 FT, RWY 34 THR DSPLCD 181 FT AND RWY 19 THR DSPLCD 1190 FT. (11/86)

FDC 6/1069 /PWT/ FI/T BREMERTON NATIONAL..BREMERTON WA. ILS RWY 19..AMDT 10. S-LOC AND CIRCLING MINIMUMS NA.

EASTON

Easton State

ARPT CLSD 01 OCT THRU 01 JUN. (10/86)

ELLENSBURG

Ellensburg RCO

COLOCATED WITH ELLENSBURG VORTAC, FREQUENCY 122.1R DCMSND EFFECTIVE 15 JAN 87. (11/86)

EPHRATA

Ephrata Muni

FDC 4/1529 /EPH/ FI/T EPHRATA MUNI EPHRATA WA. VOR RWY 20 AMDT 17/SI RWY 20 MDA 1660/HAT 388 ALL CATS. WHEN CTLZ NOT EFF SI RWY 20 MDA 1800/HAT 528 ALL CATS VIS CAT C 1 1/2.

Ephrata RCO

COLOCATED WITH EPHRATA VORTAC DCMSND EFFECTIVE 15 JAN 87.(11/86)

EVERETT

Snohomish County (Paine Fld)

RWY 29 THR DSPLCD 275 FT. (10/86)

FRIDAY HARBOR

Friday Harbor

FDC 6/1619 /S19/ FI/T FRIDAY HARBOR FRIDAY HARBOR, WA. IFR TAKE-OFF MINS: CHANGE RWY 33 TO RWY 34.

WASHINGTON

FDC 3/1352 /S19/ FI/T FRIDAY HARBOR ARPT FRIDAY HARBOR WA. ASR ORIG MISSED APCH PROC CLIMBING RT TO 2000 VIA HEADING 130 FOR RADAR VECTORS.

HOQUIAM

Bowerman

ACTIVATE MIRL RWY 06/24 & REIL RWY 06 123.6. (11/86)

FDC 6/2308 HQM/HOQUIAM/BOWERMAN/ HOQUIAM, WA. WHEN HQM VORTAC IS OTS THE FOLLOWING APPLIES: IFR DEP PROC RWY 24 CLIMB TO 2000 VIA 238 BEARING FROM HQ LOM THEN LT DIRECT HQ LOM. RWY 6 CLIMBING RT TO INTERCEPT 238 BEARING FROM HQ LOM. CONTINUE CLIMB TO 2000 THEN LT DIRECT HQ LOM. ALL ACFT CLIMB IN HQ LOM HOLDING PATTERN (HOLD NE, RT, 238 INBD) TO 7100. SUBROUTE V-27 SE BND 7100. SUBROUTE V-204 E BND 7300, V-112 SE BND NA.

FDC 5/1736 /HQM/ FI/T BOWERMAN HOQUIAM WA LOC RWY 24 AMDT 2/ VOR RWY 6 AMDT 12/VOR/DME RWY 24 AMDT 3 NA WHEN HQM FSS CLSD.

Hoquiam

CTLZ HOURS 0800-1600 LCL.(10/86)

LESTER

Lester State

ARPT CLSD 01 OCT THRU 01 JUN. (10/86)

MAZAMA

Lost River Resort

ARPT CLSD 01 NOV THR 01 APR. (10/86)

OLYMPIA

Olympia

FDC 3/754 /OLM/ FI/T OLYMPIA OLYMPIA, WA. VOR/DME RWY 35 AMDT 10..TRML RTE WINLO INT TO CETRA INT NA.

Olympia RCO

COLOCATED WITH OLYMPIA VORTAC DCMSND EFFECTIVE 15 JAN 87. (11/86)

OROVILLE

Dorothy Scott

RWY 15/33 NOW 4000 FT BY 50 FT. (10/86)

PULLMAN/MOSCOW, ID

Pullman/Moscow Regional

RWY 23 THR DSPLCD 790 FT. (11/86)

SEATTLE

Boeing Fld/King County Intl

FDC 6/844 /BFI/ FI/T BOEING FIELD/KING COUNTY INTL/SEATTLE/ WA. NDB-A AMDT 7 MINIMUM ALTITUDE AT MIDDLE MARKER 1360.

FDC 5/2526 /BFI/ FI/T SEATTLE/BOEING FIELD/KING COUNTY INTL SEATTLE WASHINGTON. NEEDLE FOUR DEPARTURE/VECTOR/CHANGE NOTE TO: THIS SID REQUIRES A MIN CLIMB OF 310 FT PER NM TO 1300 FT OR 1100 FT CEILING AND 2 MILES VIS.

WASHINGTON

SPOKANE

Spokane Intl

FDC 5/653 /GEG/ FI/T SPOKANE INTERNATIONAL SPOKANE WA. ILS RWY 21 AMDT 18..WHEN GEG VORTAC OTS ALTN MISSED APCH. CLIMBING RIGHT TURN TO [illegible]000 DIRECT TO PHORT LOM AND HOLD NORTHEAST RIGHT TURNS 205 INBOUND.

VANCOUVER

Pearson Airpark

RWY 26 NTSD VASI CMSND. (10/86)

FDC 6/2823 /60S/ FI/T PEARSON AIRPARK, VANCOUVER, WA LDA BC RWY 8, AMDT 2..PROC NA.

WENATCHEE

Pangborn Field

RWY 07/25, 4362 FT BY 150 FT, CLOSED INDEFLY. (11/86)

Wenatchee RCO

COLOCATED WITH WENATCHEE VOR-DME DCMSND EFFECTIVE 15 JAN 87. (11/86)

Wenatchee VOR/DME

(EAT) VOR/DME UNUSABLE 300-070 BYD 20 NM; 071-115 BYD 25 NM BELOW 5500 FT; 116-150 BYD 15 NM BELOW 14500 FT; 151-240 BYD 15 NM; 241-260 BYD 35 NM BELOW 12000 FT. (11/86)

YAKIMA

Yakima Air Terminal

RWY 04/22 NOW 4292 FT BY 150 FT. RWY 22 THR DSPLCD 458 FT. (11/86)

Yakima RCO

COLOCATED WITH YAKIMA VORTAC FREQUENCY 122.1R DCMSND EFFECTIVE 15 JAN 87. (11/86)

WEST VIRGINIA

BECKLEY

Raleigh County Memorial

REIL RWY 01 OTS INDEFLY. (11/86)

CHARLESTON

Yeager

ARPT CLSD TO AIRCRAFT WITH MORE THAN 30 PASSENGER SEATS 0030-0600 LCL EXCEPT ONE HR PPR CALL 304-357-5220. (10/86)

CLARKSBURG

Benedum

FDC 5/2608 /CKB/ FI/T BENEDUM CLARKSBURG WV. ILS RWY 21 AMDT 8..SI ILS VIS ALL CATS INCREASED 1/2 MILE FOR INOP MALSR. SI LOC CATS A/B INOP TABLE DOES NOT APPLY.

FDC 5/1901 /CKB/ FI/T BENEDUM ARPT CLARKSBURG WV. DEPARTURE PROCEDURES/TAKEOFF MINIMUMS: TAKEOFF MINIMUMS RWY 31, 300-1.

WEST VIRGINIA

FDC 4/963 /CKB/BENEDUM, CLARKSBURG WV. ILS RWY 21 AMDT 8. TRML ROUTE CKB VOR/DME TO ARCAT INT. DME OR RADAR REQUIRED. WHEN CTLZ IN OPN TRML ROUTES METZE INT TO ARCAT INT AND TYGAR INT TO ARCAT INT RADAR REQUIRED. WHEN CTLZ NOT IN OPN TRML ROUTES METZE INT TO ARCAT INT AND TYGAR INT TO ARCAT INT NA.

Clarksburg VOR/DME

(CKB) FREQ 112.80, CHANNEL 073X, CMSND EFFECTIVE 18 DEC 86. (11/86)

FAIRMONT

Fairmont Muni

FDC 6/2812 /4G7/ FI/T FAIRMONT MUNI, FAIRMONT, WV. DEP PROCS/TKOF MINS. TKOF MINS RWY 22. 800-2 OR STANDARD WITH A MINIMUM CLIMB OF 320 FEET PER NM TO 2400.

HUNTINGTON

Tri-State/Walker-Long Field/

RWY 03/21 CLSD TO AIR CARRIER OPERATIONS WITH MORE THAN 30 PASSENGER SEATS. (10/86)

MARTINSBURG

Eastern West Virginia Regional/Shepherd

FDC 6/2719 /MRB/ FI/T EASTERN WEST VIRGINIA REGIONAL/SHEPHERD FLD, MARTINSBURG WV. VOR-A AMDT 6..CIRCLING CAT A MDA 1060, HAA 503.

FDC 6/2423 /MRB/ FI/T EASTERN WV REGIONAL AIRPORT/ SHEPHERD FIELD MARTINSBURG WV..ILS RWY 26 AMDT 4..MISSED APCH: CLIMB TO 1000 THEN CLIMBING LT TO 3000 DIRECT MRB VORTAC AND HOLD E, LT, 290 INBOUND. VOR-A AMDT 6..MISSED APCH: CLIMBING LT TO 3000 DIRECT MRB VORTAC AND HOLD E, LT, 290 INBOUND.

FDC 6/2408 /MRB/ FI/T EASTERN WV REGIONAL AIRPORT/ SHEPHERD FIELD MARTINSBURG, WV. ILS RWY 26 AMDT 4. SI LOC MDA 1060 HAT 513 ALL CATS. VIS 1 CAT C 1 1/4 CAT D. DELETE NOTE.CAT D S-LOC VIS INCREASED 1/4 MILE FOR INOP MALSR OR MM. CIRCLING MDA 1060/HAA 503 CAT A.

MORGANTOWN

Morgantown Muni-Walter L. Bill Hart Fld

FDC 5/2507 /MGW/ FI/T MORGANTOWN MUNI-WALTER L BILL HART FLD MORGANTOWN WV. ILS RWY 18 AMDT 7..SI ILS DH 1490/ HAT 250 ALL CATS VIS 3/4 ALL CATS. INOP TABLE DOES NOT APPLY FOR SI ILS. SI LOC VIS 3/4 CATS A/ B. VIS CATS A/B INCREASED TO 1 MILE FOR INOP MALSR. VOR/DME RWY 18 AMDT 4.. SI VIS 3/4 CATS A/B. VIS CATS A/B INCREASED TO 1 MILE FOR INOP MALSR.

PARKERSBURG

Wood County Arpt-Gill Robb Wilson Fld

FDC 5/2412 /PKB/ FI/T WOOD COUNTY AIRPORT-GILL ROBB WILSON FLD PARKERSBURG, WV. ILS RWY 3, AMDT 7, GS UNUSBL BLO 940. TCH 50.

PETERSBURG

Grant County

RWYS 13 & 31 VASI DCMSND. RWY 31 REIL DCMSND. (11/86)

WEST VIRGINIA

RAVENSWOOD

Jackson County

RWY 21 REIL CMSND. ACTIVATE REIL RWY 21 122.8. (11/86)

SUMMERSVILLE

Nicholas NDB

(IJZ) UNMONITORED. (11/86)

Summersville

FDC 5/1435 /I07/ FI/T SUMMERSVILLE SUMMERSVILLE WV. NDB RWY 4 AMDT 1. SI MDA 2600/HAT 779 CATS A/B/C. VIS 1 1/4 CAT B, 2 1/4 CAT C. CIRCLING MDA 2600/HAA 779 CATS A/B. CIRCLING VIS 1 1/4 CAT B. SDF RWY 4 AMDT 1. MISSED APCH: CLIMB TO 2500 THEN CLIMBING RT TO 4500 DIR IJZ NDB AND HOLD.

Summersville SDF

(SXL) RWY 04 OTS. (11/86)

WHEELING

Wheeling Ohio Co

RWY 09/27 CONVERTED TO TWY PERMLY. (10/86)

FDC 6/1622 /HLG/ FI/T WHEELING OHIO CO., WHEELING, WV. ILS RWY 3 AMDT 17. SI ILS DH 1422/HAT 250 ALL CATS.

WHITE SULPHUR SPRINGS

Greenbrier

FDC 5/1643 /SSU/ FI/T GREENBRIER, WHITE SULPHUR SPRINGS, WV..VOR-A AMDT 8..PROC NA.

WISCONSIN

AMERY

Ameron NDB

(AHH) RTS. (10/86)

APPLETON

Outagamie County

FDC 6/2[illegible]05 /ATW/FI/T APPLETON/OUTAGAMIE COUNTY, APPLETON WI. LOC BC RWY 21 AMDT 4, PROC NA.

FDC 6/1963 /ATW/ FI/T OUTAGAMIE COUNTY APPLETON, WI. NDB RWY 29 AMDT 3..NASHA FIX MINIMUMS S-29 MDA 1320/ HAT 431 ALL CATS. VIS CAT C 1 1/4 CAT D 1 1/2. RNAV RWY 29 AMDT 3 S-29 MDA 1260/HAT 371 ALL CATS. GREEN BAY ALSTG MINIMUMS S-29 MDA 1380/HAT 491 ALL CATS. VIS CAT C 1 1/4 CAT D 1 1/2.

CLINTONVILLE

Clintonville Muni

RWY 09/27 NOW 2156 FT BY 170 FT. (10/86)

GREEN BAY

Austin Straubel Field

RWY 18/36 CHANGED TO 18R/36L, 6200 FT BY 150 FT. RWY 18L/36R NOW 3400 FT BY 75 FT, MIRL CMSND. (11/86)

WISCONSIN

JANESVILLE

Rock County

FDC 6/339 /JVL/ FI/T ROCK COUNTY..JANESVILLE WI. VOR/ DME RWY 22 /TAC/ AMDT 2. PROC NA.

Rock County ATCT

EFFECTIVE 16 NOV ATIS & ATCT HRS 0600-2100 LCL. (10/86)

JUNEAU

Dodge County

RWYS 02 & 20 REIL CMSND. RWY 08/26 NOW 3300 FT BY 100 FT, MIRL CMSND. MIRL RWY 08/26 PRESET LOW INTST, TO INCREASE INTSTY ACTIVATE LIRL AND REILS RWY 02/20 - 122.7.(10/86)

LA CROSSE

La Crosse Muni

ACTIVATE VASI RWY 31 2100-0600 LCL - 124.3. (10/86)

LADYSMITH

Rusk County

FDC 6/2706 /RCX/ FI/T RUSK COUNTY, LADYSMITH WI. NDB RWY 32 ORIG..S-32 MINIMUMS CATS A/B MDA 1900 VIS 1 HAT 667. CAT C MDA 1900 VIS 1 3/4 HAT 667. CIRCLING MINIMUMS CATS A/B. MDA 1900 VIS 1 HAT 662. CAT C MDA 1900 VIS 1 3/4 HAA 662.

FDC 6/1780 /RCX/ FI/T RUSK COUNTY, LADYSMITH, WI. NDB RWY 32 ORIG. PROC NA AT NIGHT.

MANITOWOC

Manitowoc

FDC 6/1179 /MTW/ FI/T MANITOWOC COUNTY, MANITOWOC, WI. ILS RWY 17 ORIG. PROCEDURE TURN LEFT SIDE OF COURSE 349 OUTBOUND 2500 FT. REMAIN WITHIN 15 NM OF MTW VOR.

MEDFORD

Taylor County

MIRL RWY 15/33 PRESET LOW INTSTY, INCREASE INTSTY KEY 122.8, 5 TIMES MEDIUM & 7 TIMES HIGH. ACTIVATE VASI RWYS 15 & 33 AND REIL RWY 33 122.8. (11/86)

MILWAUKEE

General Mitchell Field

FDC 6/1021 /MKE/ FI/T GENERAL MITCHELL FIELD. MILWAUKEE, WI. IFR TAKEOFF MINIMUMS RWY 13 300-1.

PLATTEVILLE

Platteville

ARPT CLSD TO PUBLIC USE. (11/86)

WATERTOWN

Watertown Muni

RWY 05 THRESHOLD DSPLCD 2[illegible]0 FT. RWY 23 THRESHOLD DSPLCD 75 FT.(10/86)

WISCONSIN

WAUPACA

Waupaca Muni

RWY 06/24 NOW 1500 FT BY 110 FT. (11/86)

WYOMING

CASPER

Natrona County Intl

FDC 1/1567 /CPR/ FI/T NATRONA COUNTY INTL/ CASPER WY. ILS RWY 7 AMDT 21. SI CAT D NA.

DOUGLAS

Converse County

RWY 10/28 NOW 6755 FT BY 100 FT. (11/86)

FORT BRIDGER

Fort Bridger

RWY 04/22 NOW 6370 FT BY 60 FT. RWY 06/24 NOW 4090 FT BY 60 FT. RWY 16/34 NOW 4664 FT BY 100 FT. (10/86)

WYOMING

FDC 6/2870 /FBR/ FI/T FORT BRIDGER, FORT BRIDGER WY. VOR RWY 22 ORIG. S-22 ALL CATS 382 HAT, CIRCLING CAT A 357 HAA/CATS B/C 7500 MDA 467 HAA/CAT D 7600 MDA 567 HAA. DME MINIMA S-22 ALL CATS 302 HAT. CIRCLING CAT A 387 HAA/CATS B/C 7500 MDA 467 HAA/CAT D 7600 MDA 567 HAA.

JACKSON

Jackson VOR/DME

(JAC) RESTRICTED TO AIRWAYS; HOLDING; MISSED APCH AND APCH USE ONLY.(11/86)

LUSK

Lusk Muni

RWY 10 VASI DCMSND. RWY 28 VASI CMSND. (10/86)

RAWLINS

Rawlins Muni

RWY 10/28 CLSD DURING WINTER MONTHS. (10/86)

[illegible]

LA CROSSE

[illegible]

Rock County

[illegible]

HAZARDOUS INFLIGHT WEATHER ADVISORY SERVICE (HIWAS)

HIWAS is a national program for broadcasting hazardous weather information (SIGMET's, convective SIGMET's, Center Weather Advisories (CWA), AIRMET's, and urgent PIREP's) on a continuous basis over selected VOR's. The program is operational in the Jacksonville, Miami, and Houston Air Route Traffic Control Center (ARTCC) areas. The chart on the following page identifies the current broadcast outlet locations and frequencies. Frequencies shown in the Atlanta ARTCC area are for planning purposes only. HIWAS will be expanded on an ARTCC by ARTCC basis.

Pilots should be aware that:

* Flight service stations broadcast information on hazardous weather not yet covered by an advisory and make an announcement on their frequencies that new HIWAS information is available.

* Controllers in ARTCC's and air traffic control terminals announce updates to HIWAS information on all appropriate frequencies.

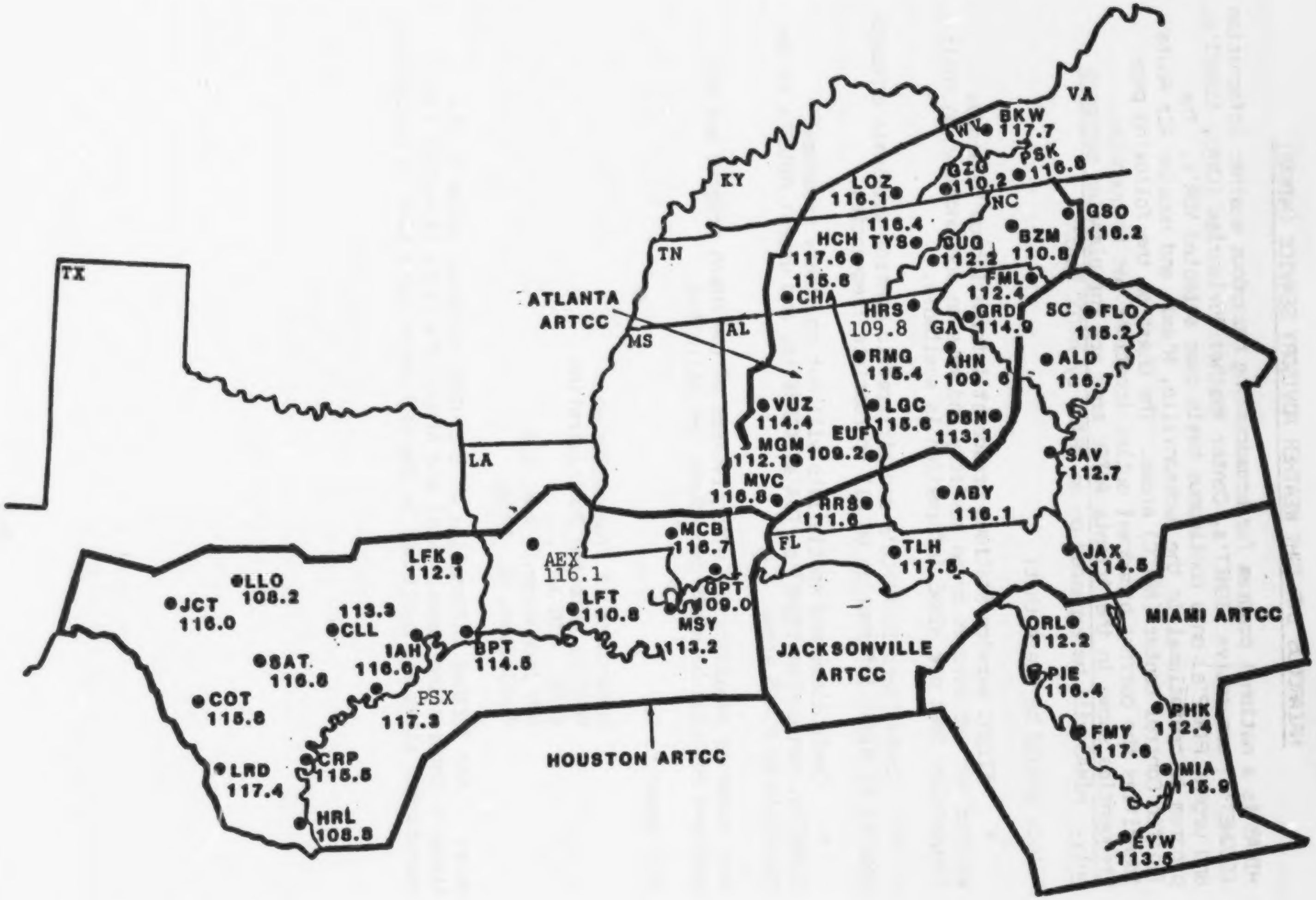
* Controllers and specialists will not routinely broadcast SIGMET's, convective SIGMET's, CWA's, AIRMET's, and urgent PIREP's in the commissioned HIWAS areas.

User comments regarding the effectiveness of the HIWAS program and any proposed revision to HIWAS procedures are solicited.

Mail comments to:

Department of Transportation
Federal Aviation Administration
ATTN: ATO-360
800 Independence Ave. S.W.
Washington, DC 20591

Note: For further information on the HIWAS program, refer to the Airman's Information Manual (AIM) and Airport/Facility Directory (AFD). Operational sites are published in the AFD under radio aids to navigation.


VA
WV
BKW 117.7
PSK 116.8
GZG 110.2
KY
LOZ 116.1
NC
GSO 116.2
116.4 TYS
HCH 117.6
BZM 110.8
SUG 112.2
TN
FML 112.4
115.8 CHA
HRS 109.8
GRD 114.9
SC
FLO 115.2
GA
ATLANTA ARTCC
MS
AL
RMG 115.4
AHN 109.6
ALD 116.7
VUZ 114.4
LGC 115.6
DBN 113.1
EUF 109.2
MGM 112.1
SAV 112.7
MVC 116.8
RRS 111.6
ABY 116.1
TX
LA
MCB 116.7
FL
TLH 117.5
JAX 114.5
LFK 112.1
AEX 116.1
GPT 109.0
LFT 110.8
MSY 113.2
MIAMI ARTCC
LLO 108.2
JCT 116.0
113.3 CLL
IAH 116.6
BPT 114.5
JACKSONVILLE ARTCC
ORL 112.2
PIE 116.4
SAT 116.8
COT 115.8
PSX 117.3
HOUSTON ARTCC
PHK 112.4
FMY 117.6
MIA 115.9
LRD 117.4
CRP 115.5
HRL 108.8
EYW 113.5

AIRPORT RADAR SERVICE AREAS (ARSA)

The National Airspace Review Terminal Airspace Task Group 1-2.2 recommended the ARSA Program as a replacement for the existing Terminal Radar Service Area Program and the FAA has adopted that recommendation. ARSA designations have been made, and effective dates established, for the locations listed below. The following is a summary of the pilot requirements and the ATC procedures for ARSA's. Graphic depictions of each ARSA are also included.

Unless otherwise authorized or required by ATC, the following provisions apply to aircraft operating within an ARSA:

1. Aircraft approaching that would penetrate the ARSA must establish two-way radio communications with ATC prior to entering the ARSA and maintain that communication while operating within the ARSA.
2. Aircraft departing the primary airport within the ARSA must establish two-way communications with ATC prior to departur and maintain that communication while operating within the ARSA. Aircraft departing a satellite airport within the ARSA must contact ATC as soon as practicable after takeoff.
3. Except in an emergency, all operations must be in complianc with ATC clearances and instructions.
4. All arrivals and departures within the ARSA must be in compliance with FAA arrival and departure traffic patterns.
5. Ultralight vehicles and parachute operations may not be conducted within the ARSA except under the terms of an ATC authorization.
6. NOTAM's pertaining to flight within the ARSA must be reviewed as a part of preflight action required by FAR 91.5

Within ARSA's, ATC will provide the following services:

1. Radar sequencing of all arrivals.
2. Standard separation between all instrument flight rules (IFR) flights.
3. Traffic advisories and safety advisories to all aircraft.
4. Resolve any potential conflict between an aircraft operatin IFR and an aircraft operating under visual flight rules by application of conflict resolution procedures.

An ARSA has been designated at the following location to be effective November 20, 1986.

Louisville, KY, Standiford Field.

ARSA's have been established at the following locations to be effective December 18, 1986.

Mobile, AL, Bates Field

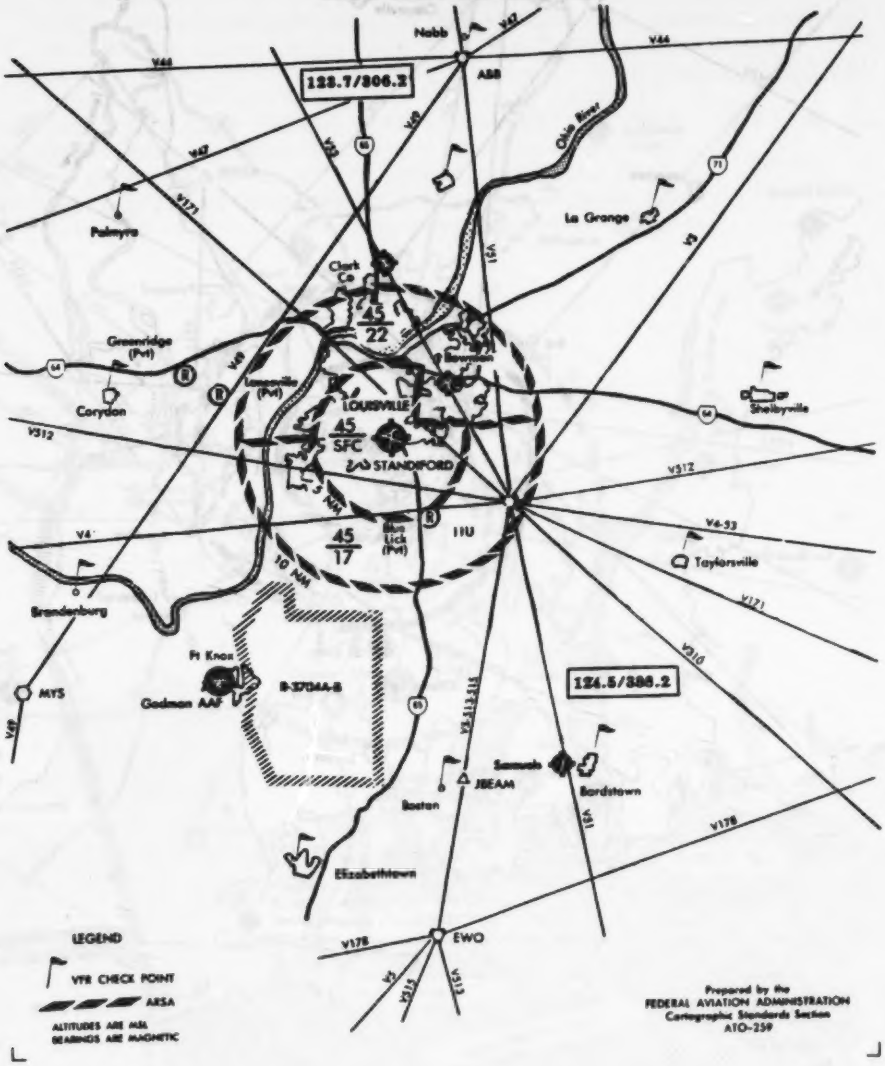
Providence, RI, Theodore Francis Green State Airport.

An ARSA has been designated at the following airport to become effective on November 20, 1986

AIRPORT RADAR SERVICE AREA

(NOT TO BE USED FOR NAVIGATION)

LOUISVILLE, KENTUCKY
STANDIFORD FIELD
FIELD ELEV. 497' MSL


Nabb
V47
V44
ABB
123.7/306.2
V53
V171
Palmyra
Ohio River
71
La Grange
V5
Clark Co
45
22
V51
Greenridge (Pvt)
64
Corydon
Lanesville (Pvt)
V49
LOUISVILLE
Bowman
45
SFC
STANDIFORD
V512
5 NM
45
17
Blue Lick (Pvt)
IIU
V4
V4-53
Taylorsville
Shelbyville
10 NM
Brandenburg
Ft Knox
Godman AAF
R-3704A-B
MYS
V49
65
V5-512-215
124.5/386.2
V310
Samuels
Bardstown
JBEAM
Boston
V178
Elizabethtown
EWO
V5
V215
V512
LEGEND
VFR CHECK POINT
ARSA
ALTITUDES ARE MSL
BEARINGS ARE MAGNETIC

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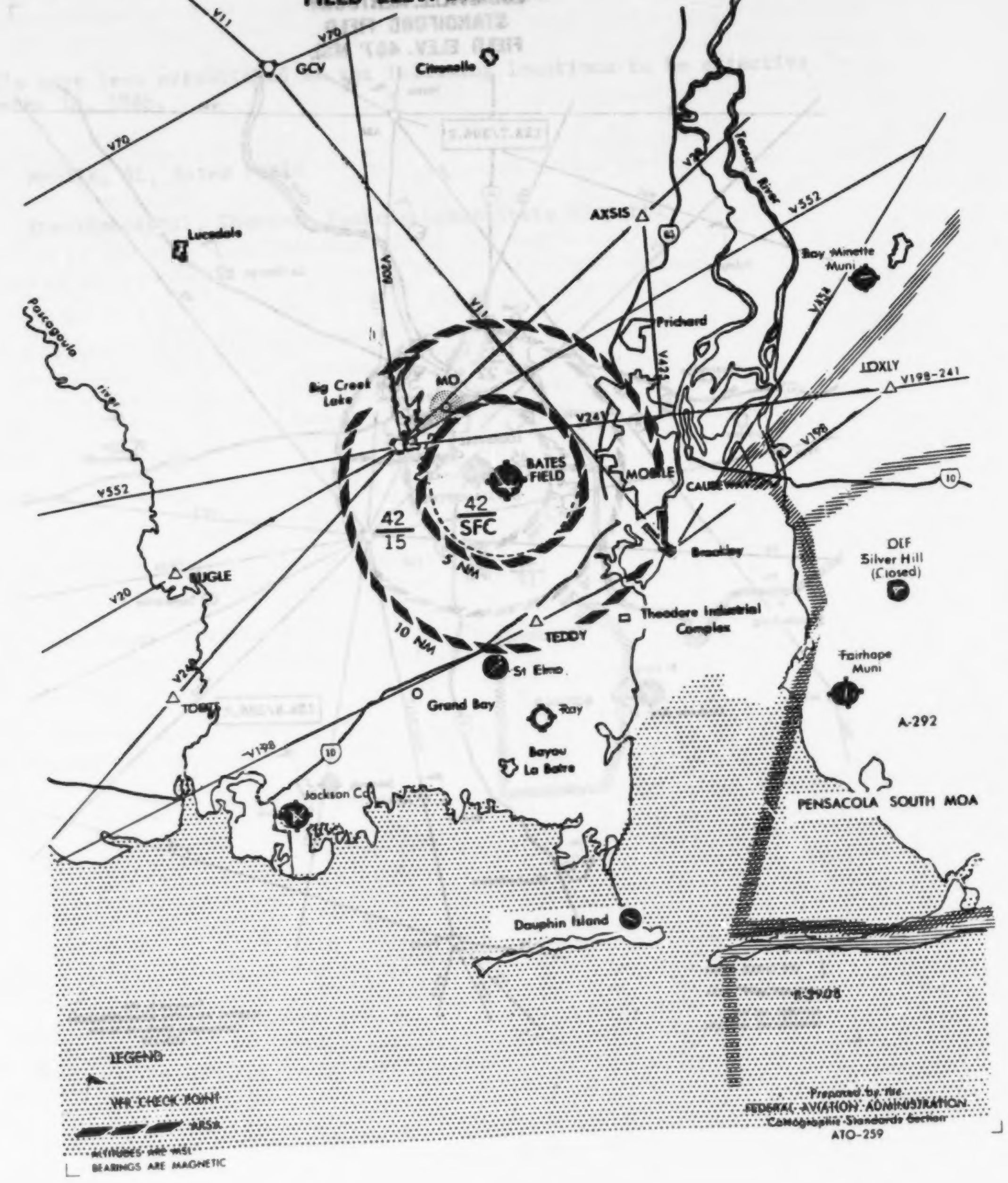
Cartographic Standards Section
ATO-259

AIRPORT RADAR SERVICE AREA
(NOT TO BE USED FOR NAVIGATION)

MOBILE, ALABAMA
BATES FIELD
FIELD ELEV. 218' MSL


V11
V70
GCV
Citronelle
V70
Lucedale
Pascagoula River
AXSIS
65
Tensaw River
V552
Bay Minette Muni
Prichard
V11
LOXLY
V198-241
V241
V198
MO
Big Creek Lake
BATES FIELD
MOBILE
CAUSEWAY
10
42
15
42
SFC
5 NM
10 NM
Brookley
V552
BUGLE
V20
OLF
Silver Hill
(Closed)
Theodore Industrial Complex
TEDDY
St Elmo
Grand Bay
Ray
Fairhope Muni
A-292
V198
10
Bayou La Batre
Jackson Co
PENSACOLA SOUTH MOA
Dauphin Island
R-2908
LEGEND
VFR CHECK POINT
ARSA
ALTITUDES ARE MSL
BEARINGS ARE MAGNETIC

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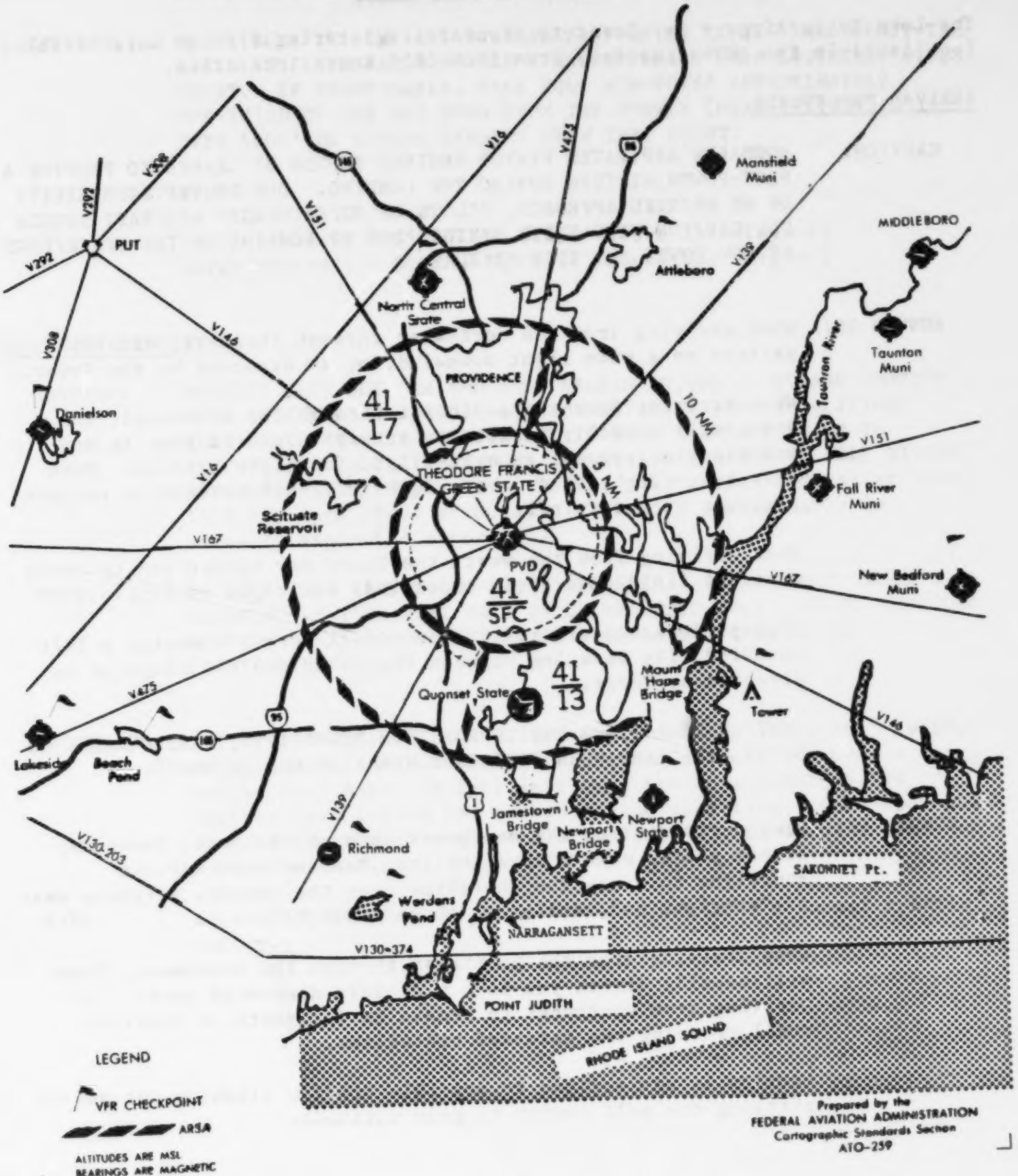
AIRPORT RADAR SERVICE AREA

(NOT TO BE USED FOR NAVIGATION)

PROVIDENCE, RHODE ISLAND
THEODORE FRANCIS GREEN STATE AIRPORT
FIELD ELEV. 56' MSL


PUT
V292
V308
V146
V16
V151
V475
V130
V167
V139
V130-203
V130-374
Mansfield Muni
MIDDLEBORO
Attleboro
North Central State
Taunton Muni
Taunton River
PROVIDENCE
41/17
10 NM
5 NM
Danielson
THEODORE FRANCIS GREEN STATE
Scituate Reservoir
Fall River Muni
PVD
41/SFC
New Bedford Muni
41/13
Quonset State
Mount Hope Bridge
Tower
Lakeside
Beach Pond
Jamestown Bridge
Newport Bridge
Newport State
Richmond
Wordens Pond
SAKONNET Pt.
NARRAGANSETT
POINT JUDITH
RHODE ISLAND SOUND
LEGEND
VFR CHECKPOINT
ARSA
ALTITUDES ARE MSL
BEARINGS ARE MAGNETIC

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Cartographic Standards Section
ATO-259

TERMINAL AREA GRAPHIC NOTICE
(NOT TO BE USED FOR NAVIGATION)

SOUTH LAKE TAHOE, CALIFORNIA
LAKE TAHOE AIRPORT

The Lake Tahoe Airport is closed to aircraft registering 77.1 or more decibles (as listed in FAA AC36-3 series) from 2000-0800 hours local time.

ARRIVAL PROCEDURES:

CAUTION: NORMALLY ASPIRATED PISTON ENGINES SHOULD BE LEANED TO PROVIDE A BEST-POWER MIXTURE DURING THE LANDING. DUE TO THE POSSIBILITY OF AN ABORTED APPROACH, PILOTS OF SUPERCHARGED AIRCRAFT SHOULD USE CAUTION WITH THEIR MIXTURE DUE TO FOULING OF THE SPARKPLUGS AT LOW POWER AND RICH MIXTURE.

RUNWAY 36: When arriving from the northwest through the east, enter the pattern on a wide right downwind, or as directed by the Tower.

When arriving from the southeast through the southwest, the Tower will normally direct you straight-in. If that is not practicable, request an over-flight for right traffic. Make your over-flight at or above 8000' MSL, and descend to pattern altitude on crosswind.

When arriving from the west, the Tower may direct you to cross over the field (mid-field crosswind) for right traffic.

High performance aircraft: Tower will normally assign a left downwind, fly base leg between the river and the ridge or as directed by Tower.

NOTE: CAUTION IS ADVISED DUE TO POSSIBLE DOWNDRAFTS, PARTICULARLY ON SHORT FINAL AND WHEN NORTHERLY WINDS EXCEED 15 KNOTS.

RUNWAY 18: When arriving from the northwest through the east, Tower may direct you to make a straight in. Descend north of the shoreline to cross the shoreline over the meadow, slightly west of "straight in", and at or above 7500' MSL.

When arriving from the southeast through the southwest, Tower will usually direct you to a wide left down-wind entry. If arriving from southwest to remain as far south as feasible until crossing the extended centerline.

Caution is advised due to possible traffic climbing out and/or circling the golf course to gain altitude.

When arriving from the west, Tower normally will advise you to make a straight in. Make your "base" leg north of the shoreline, and turn final at or above 7500' MSL.

CAUTION: ROTOR ACTIVITY (UP AND DOWN-DRAFTS) OFTEN EXISTS THROUGHOUT THE BASIN AND ESPECIALLY ON THE FINAL APPROACH WHEN SOUTHERLY WINDS EXIST. IF PRACTICABLE, MAKE YOUR AIM-POINT APPROXIMATELY ONE-THIRD OF THE WAY DOWN FROM THE RUNWAY (NEAR TAXIWAY "E"). OVER 5000' OF RUNWAY REMAINS FROM THAT POINT.

PATTERN ALTITUDES:

Small aircraft - 7500' MSL (1236' above the airport)
Large aircraft - 8000' MSL (1736' above the airport)

DEPARTURE PROCEDURES:

CAUTION: DENSITY ALTITUDE CAN AND DOES EXCEED 10,000'. PLEASE COMPUTE YOUR PERFORMANCE FACTORS ACCORDINGLY, USE DENSITY ALTITUDE LEANING TECHNIQUES APPROPRIATE TO YOUR AIRCRAFT PRIOR TO TAKEOFF AND ENSURE THAT YOUR WEIGHT AND BALANCE IS WELL WITHIN LIMITATIONS. (Suggestion: Reduce your useful load by at least 2.5% for each 1000' of density altitude, particularly in normally aspirated aircraft.)

NOTE: WE LIVE IN A VERY NOISE-SENSITIVE AREA. PLEASE HELP US BY CLIMBING AT YOUR BEST RATE OF CLIMB SPEED (Vy), AND BY REDUCING TO YOUR CLIMB-POWER SETTING AS SOON AS YOU FEEL IT IS PRACTICABLE.

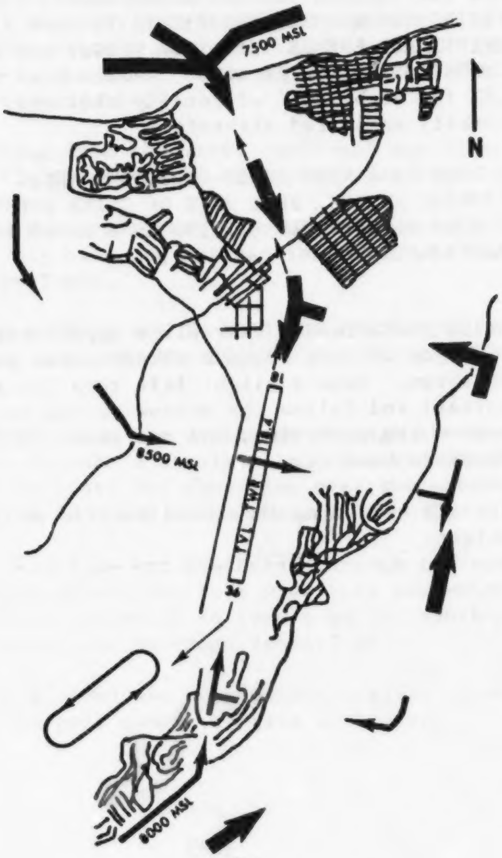
RUNWAY 36: Follow the extended centerline approximately 3/4 mile. At that point you will be abeam a white-fenced pasture and over a large red arrow. Make a slight left turn (to approximately 320 degrees) and follow the meadow to the shoreline. Once you have crossed the shoreline, and are above 7500' MSL turn to your departure heading.

NOTE: Aircraft remaining in closed traffic may make a normal traffic pattern.

RUNWAY 18:

CAUTION: **ALL TERRAIN SOUTH OF THE AIRPORT IS ABOVE THE AIRPORT ELEVATION. DOWNDRAFTS IN EXCESS OF 500FPM OFTEN EXIST THROUGHOUT THE DEPARTURE AREA. CHECK YOUR CLIMB GRADIENT AND OTHER PERFORMANCE FIGURES ACCORDINGLY.**

After clearing the airport boundary, make a slight right turn to follow the river. If making a downwind departure, do not turn crosswind until reaching 7500' MSL, make a wide downwind turn. If you need additional altitude, advise the Tower you will be climbing over the golf course. Use a right-turn climbing pattern, watch out for other traffic, and advise the Tower when you depart the golf course. Downdrafts often exist near the mountains - stay over the golf course.



HIGH ALTITUDE/EN ROUTE FLIGHT ADVISORY SERVICE (HA/EFAS)

HA/EFAS is an expansion of the current EFAS program (See AIM, paragraph 503). When fully implemented, it will provide a discrete frequency for each of the Air Route Traffic Control Center (ARTCC) areas for use by aircraft flying at altitudes of 18,000 feet and above within the center's area. The service expansion was initiated in July 1986 in the Salt Lake City ARTCC area on a frequency of 133.025 mHz.

As service in other areas becomes available the information will be published on charts located on the inside back cover of the Airport Facility Directories.

ALTOONA, PA, AUTOMATED FLIGHT SERVICE STATION

THE ALTOONA, PA AUTOMATED FLIGHT SERVICE STATION (AFSS WAS COMMISSIONED ON AUGUST 26, 1986. ALL SERVICES PROVIDED BY THE ALTOONA FLIGHT SERVICE STATION (FSS) HAVE BEEN TRANSFERRED TO THE AFSS. ALTOONA AFSS HAS ALSO ASSUMED CONTROL OF REMOTE COMMUNICATIONS OUTLET (RCO), AND VERY-HIGH OMNI (VOR) VOICE FREQUENCIES FORMERLY CONTROLLED BY AOO FSS , AS WELL AS ALL FACILITIES CONTROLLED BY PHILIPSBURG, PA FLIGHT SERVICE STATION.

AREA SERVED: THE ALTOONA AFSS'S GEOGRAPHIC AREA OF RESPONSIBILITY IS SW PENNSYLVANIA FOR ALL SERVICES EXCEPT EFAS.

RADIO AIDS

A. NAVIGATIONAL AIDS WITH VOICE CAPABILITY, (PILOTS TRANSMIT ON 122.1 AND RECEIVE ON THE VOR FREQUENCY.)

ALTOONA (AOO)	108.8
REVLCC (REC)	110.6
JOHNSTOWN (JST)	113.0
TYRONE (TON)	114.9
ST. THOMAS (THS)	115.0
PHILIPSBURG (PSB)	115.5
KEATING (ETG)	116.0

REMOTE COMMUNICATIONS OUTLETS (RCO'S)

VHF	
PHILIPSBURG (PSB)	122.2
PHILIPSBURG (PSB)	122.6

UHF	
PHILIPSBURG (PSB)	255.4

EMERGENCY	
PHILIPSBURG (PSB)	121.5
PHILIPSBURG (PSB)	243.0

NOTE 1: THE ALTOONA-BLAIR COUNTY AIRPORT ADVISORY FREQUENCY 123.65 MHZ WILL BE DECOMMISSIONED ON AUGUST 26. THE NEW COMMON TRAFFIC ADVISORY FREQUENCY (CTAF) FOR ALTOONA-BLAIR CO. AIRPORT WILL BE 122.9 MHZ.

LORAN-C STATUS INFORMATION

LORAN-A service has been terminated in the U.S. coastal confluence region. Prerecorded telephone answering service messages pertaining to LORAN-C are available as follows:

RATE	CHAIN	TELEPHONE
5930	Canadian East Coast	709-454-3261*
7980	Southeast U.S.	904-569-5241
8970	Great Lakes	607-869-5395
9960	Northeast U.S.	607-869-5395

*St. Anthony, Newfoundland, Canada

Information can also be obtained directly from the office of the Coordinator of Chain Operations (COCO) for each chain. The following telephone numbers are for each COCO office:

RATE	CHAIN	TELEPHONE	LOCATION
4990	Central Pacific	808-247-5591	Kaneohe, HI.
5930	Canadian East Coast	709-454-2392	St. Anthony, Nfld.
5990	Canadian West Coast	707-987-2911	Middletown, CA.
7930	North Atlantic	**	London, U.K.
7960	Gulf of Alaska	907-487-5583	Kodiak, AK.
7970	Norwegian Sea	**	London, U.K.
7980	Southeast U.S.	904-569-2223	Malone, FL.
7990	Mediterranean Sea	**	London, U.K.
8970	Great Lakes	607-869-5393	Seneca, NY.
9940	U.S. West Coast	707-987-2911	Middletown, CA.
9960	Northeast U.S.	607-869-5393	Seneca, NY.
9970	Northwest Pacific	415-437-3224	San Francisco, CA.
9990	North Pacific	907-487-5583	Kodiak, AK.

**011-44-1-409-4758

COLORADO SKI COUNTRY AIRPORTS
SPECIAL AIR TRAFFIC MANAGEMENT PROGRAM

In anticipation of the large number of aircraft operating into and out of Colorado Ski Country Airports during the 1986-1987 ski season, the following procedures have been implemented to enhance safety and minimize traffic delays during this ski season.

These procedures for Colorado Ski Country Airports shall be in effect from November 14, 1986, through April 13, 1987.

FLIGHT PLANS

For the purpose of flight planning the Colorado Ski Country includes the following airports:

Aspen, Colorado
    Aspen-Pitkin County/Sardy Field Airport (ASE)

Eagle, Colorado
    Eagle County Airport (EGE)

Gunnison, Colorado
    Gunnison County Airport (GUC)

Rifle, Colorado
    Garfield County Airport (RIL)

Hayden, Colorado
    Yampa Valley Airport (HDN)

Pilots are urged to file IFR flight plans at least 4 hours prior to proposed time of departure with the nearest flight service station.

Air filed flight plans and flight plans filed less than 4 hours prior to proposed departure times, may experience delays awaiting integration into the IFR system while this program is in effect.

(Revised 11/19/86)

PREFERRED ARRIVAL ROUTING

Unscheduled IFR flights operating into a Colorado Ski Country Airport should file an appropriate preferred route during the hours 1400 UTC and 0300 UTC (0700 MST-2000 MST) daily.

To Aspen, Colorado (ASE) and Rifle, Colorado (RIL)

Route 1	From over fixes between DEN clockwise to COS; file via DEN..DBL..ASE/RIL
Route 2	From over fixes between COS clockwise to HBU; file via HBU..DBL..ASE/RIL
Route 3	From over fixes between GUC clockwise to DEN; file via DBL..ASE/RIL

To Eagle, Colorado (EGE)

Route 1	From over fixes between CHE clockwise to IOC; file via RLG.RLG189R.STUPE ..EGE
Route 2	From over fixes between IOC clockwise to FMN; file via HBU.V421.HAMPS..EGE
Route 3	From over fixes between FMN clockwise to PUC; file via JNC.V134.DBL.V421 .HAMPS..EGE
Route 4	From over fixes between PUC clockwise to CHE; file via EKR.V200.RLG.RLG189R .STUPE..EGE

To Gunnison, Colorado (GUC)

Via Airways

Exception: TRAFFIC WILL NOT BE ROUTED DEN J10/J128 HBU.

(Revised 11/19/86)

IFR ARRIVAL/DEPARTURE/PROCEDURES FOR ASPEN

Denver Air Route Traffic Control Center (ARTCC) Traffic Management Unit (TMU) may assign a control departure time (CDT) for IFR flights arriving or departing Aspen-Pitken County/Sardy Field (ASE) whenever marginal weather conditions exist.

Implementation of this part of the special Traffic Management Program will be by special notice. Pilots may obtain current delay information during preflight and inflight briefings. During marginal weather conditions, pilots are encouraged to contact the tower or flight service station prior to engine startup to obtain latest information.

To ensure the success of this special Traffic Management Program, aircraft inbound to ASE are urged to depart within plus or minus 5 minutes of CDT.

GENERAL INFORMATION

Advise ATC of alternate airport prior to starting approach.

Additional routing may be assigned by ATC based on weather and traffic density.

Pilots destined for Ski Country Airports are encouraged to plan their arrivals Monday through Thursday to avoid extensive arrival delays.

Extensive arrival delays can be anticipated between the hours of 1900 UTC and 0100 UTC (1200 MST - 1800 MST) Friday, Saturday, and Sunday.

Pilots may obtain additional traffic management information from the nearest flight service station.

(Revised 11/19/86)

SPECIAL USE AIRSPACE
(Military Operations Area)

Effective December 10, 1986

Camp Swift Temporary MOA, TX [New]

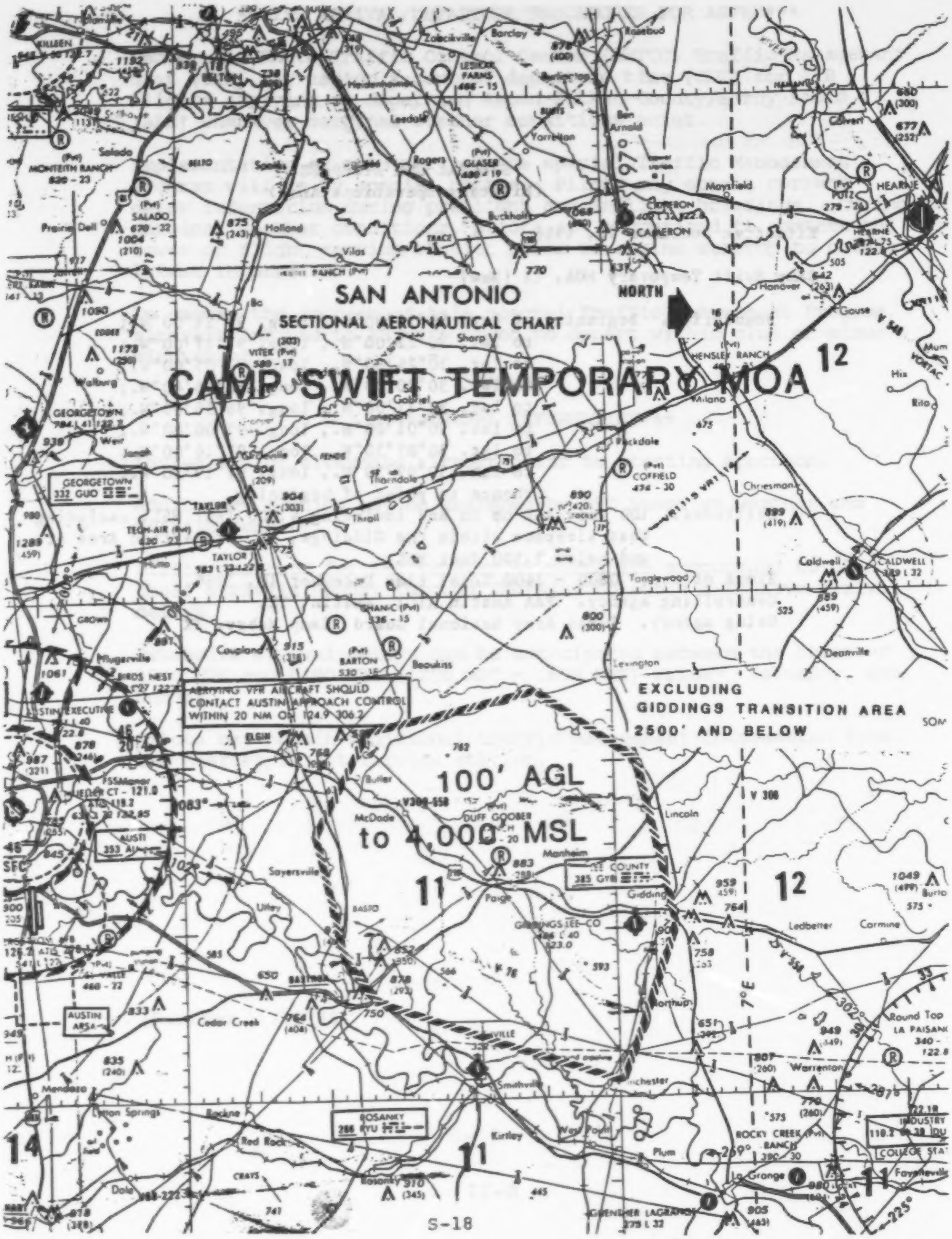
Boundaries. Beginning at lat. 30°16'00"N., long. 97°21'00"W.;
to lat. 30°22'00"N., long. 97°17'00"W.;
to lat. 30°24'00"N., long. 97°05'00"W.;
to lat. 30°20'00"N., long. 96°58'40"W.;
to lat. 30°11'00"N., long. 96°56'00"W.;
to lat. 30°01'00"N., long. 97°00'00"W.;
to lat. 30°05'30"N., long. 97°16'00"W.;
to lat. 30°09'30"N., long. 97°19'30"W.;
thence to point of beginning.

Altitudes. 100 feet AGL up to and including 4,000 feet MSL, excluding that airspace within the Giddings, TX, Transition Area at and below 2,500 feet MSL.

Times of use. 0800 - 2400 local time December 10, 1986.

Controlling agency. FAA Austin ATCT, Austin, TX.

Using agency. Texas Army National Guard, Camp Mabry, TX


SAN ANTONIO
SECTIONAL AERONAUTICAL CHART
CAMP SWIFT TEMPORARY MOA
NORTH
100' AGL
to 4,000' MSL
EXCLUDING
GIDDINGS TRANSITION AREA
2500' AND BELOW
ARRIVING VFR AIRCRAFT SHOULD CONTACT AUSTIN APPROACH CONTROL WITHIN 20 NM ON 124.9 306.2
11
12
14
KILLEEN
BELTON
Rosebud
Zabcikville
Barclay
Heidenheimer
Leedale
Rogers
Ben Arnold
Yarrelton
Salado
SALADO
MONTEITH RANCH
Prairie Dell
Holland
Buckholts
CAMERON
Maysfield
HEARNE
Calvert
Hanover
Gause
Vilas
Sharp
HENSLEY RANCH
Milano
Hix
Rita
Walburg
GEORGETOWN
Weir
Jonah
Thorndale
Rockdale
COFFIELD
Chriesman
Thrall
TAYLOR
TECH-AIR (Pvt)
Hutto
Tanglewood
Caldwell
CALDWELL
Deanville
Pflugerville
BIRDS NEST
Coupland
BARTON
Lexington
AUSTIN EXECUTIVE
ELGIN
Butler
McDade
DUFF GOOBER
Lincoln
LEE COUNTY
Giddings
Sayersville
Utley
Paige
GIDDINGS-LEE CO
Ledbetter
Carmine
AUSTIN ARSA
Cedar Creek
BASTROP
Northrup
Round Top
LA PAISANO
Warrenton
Smithville
Winchester
INDUSTRY
Mendoza
Lytton Springs
Rockne
ROSANKY
Red Rock
Kirtley
West Point
Plum
ROCKY CREEK (Pvt) RANCH
La Grange
Fayetteville
Rosanky
Dale
GRENDNER LAGRANGE
V 306
7°E
V 548

U.S. GOVERNMENT PRINTING OFFICE : 1986 O - 168-213

FLIGHT INFORMATION PUBLICATION
Notices To Airmen (Class II)

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Safety

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1986-26

Internal Revenue bulletin

June 30, 1986
Bulletin No. 1986–26

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Highlights of this Issue

INCOME TAX

Notice 86-8, page 7.
Guidance is provided to certain shareholders of American Telephone and Telegraph Company with respect to claiming refunds of tax paid on the distribution of stock of Pacific Telesis Group.

ESTATE TAX

Rev. Rul. 86-85, page 5.
Special use value; farms; interest rates. The 1986 interest rates to be used in computing the special use value of farm real property for which an election is made under section 2032A of the Code are listed for estates of decedents.

ADMINISTRATIVE

Rev. Proc. 86-29, page 9.
Rulings; classification as fixed investment trust. Ruling or determination letters will now be issued concerning the classification of an arrangement as a fixed investment trust when the arrangement has multiple classes of equitable ownership. Rev. Proc. 86-3 modified.

Rev. Proc. 86-30, page 9.
Reproduction of forms; Forms 1096, 1098, 1099 series, 5498, and W-2G. Requirements are set forth for reproducing paper subsitutes for Forms 1096, 1098, 1099 series, 5498, and W-2G, and for furnishing substitute statements to forms recipients. Rev. Procs. 85-25 and 85-52 superseded.

Rev. Proc. 86-31, page 31.
Information returns; magnetic media. Guidance is provided to filers of certain information returns about procedures for requesting approval for filing such returns on a particular form of magnetic medium, or for requesting a waiver of the magnetic media filing requirements of section 6011(e) of the Internal Revenue Code and section 1.6045-1 of the Income Tax Regulations.

Announcement 86-78, page 35.
Form 56, Notice of Fiduciary Relationship, has been revised to incorporate the notice requirements for qualification as an executor or receiver under section 6036 of the Code.

Announcement 86-79, page 35.
Form 926, Return by a Transferor of Property to a Foreign Corporation, Foreign Estate or Trust, or Foreign Partnership, has been revised to reflect the provisions of section 1.6038B-1T of the regulations.

Announcement 86-80, page 35.
A correction should be made to Publication 509, Tax Calendars for 1986.

Announcement 86-81, page 35.
Publication 597, Information on the United States-Canada Income Tax Treaty (revised March 1986) is now available. The explanatory text is directed primarily to individual U.S. citizens and residents who receive Canadian sourced income.

Announcement 86-82, page 35.
The Office of Chief Counsel encourages submission of prospectuses and/or other written descriptions of new financial products that are being created and sold to investors in public offerings. The submitter is also encouraged to point out any tax issues presented by the transaction.

Announcement 86-83, page 36.
Publication 1212, List of Original Issue Discount Instruments (Rev. Dec. 85), is supplemented to provide information to banks, brokers, and other middlemen regarding Treasury bills issued at a discount and maturing during 1986.

Finding Lists begin on page 42.
Announcement Relating to Decisions of the Tax Court on page 4.
Announcement of Disbarments and Suspensions begin on page 38.
Announcement of Notice of Proposed Rulemaking on page 40.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Announcement Relating To Decision of the Tax Court

It is the policy of the Internal Revenue Service to announce in the Internal Revenue Bulletin at the earliest practicable date the determination of the Commissioner to acquiesce or not acquiesce in a decision of the Tax Court which disallows a deficiency in tax determined by the Commissioner to be due.

Notice that the Commissioner has acquiesced or nonacquiesced in a decision of the Tax Court relates only to the issue or issues decided adversely to the Government.

Actions of acquiescences in adverse decisions shall be relied on by Revenue officers and other concerned as conclusions of the Service only to the application of the law to the facts in the particular case. Caution should be exercised in extending the application of the decision to a similar case unless the facts and circumstances are substantially the same, and consideration should be given to the effect of new legislation, regulations, and rulings as well as subsequent court decisions and actions thereon.

Acquiescence in a decision means acceptance by the Service of the conclusion reached, and does ot necessarily mean acceptance and approval of any or all of the reasons assigned by the Court for its conclusions.

No announcements are made in the Bulletin with respect to memorandum opions of the Tax Court.

The announcements published in the weekly Internal Revenue Bulletins are consolidated semiannually and annually. The semiannual consolidation appears in the first Bulletin for July and in the Cumulative Bulletin for the first half of the year and the annual consolidation appears in the first Bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner ACQUIESCES in the following decisions:

Taxpayer	Docket No.	Report	
		Volume	Page
Moden, John B., et ux[1]	16201–79)	85	731
Vanicek, Edward, Deceased & Sara Vanicek[1]	16187-79)		
Woods Investment Co.[2]	6237-83	85	274

The Commissioner does NOT ACQUIESCE in the following decision:

Taxpayer	Docket No.	Report	
		Volume	Page
Sutherland, Robert D., d/b/a Sutherland Rocky Mountain Lumber Co.[3]	9971-78R	78	395

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[1] Acquiescence relating to whether the fair rental value of lodging furnished to petitioners by their employer, the Forest Preserve District of Cook County, Illinois, is excludable from gross income under section 119 of the Code.

[2] Acquiescence relating to whether, upon selling the stock of its subsidiaries, the petitioner must reduce its basis in that stock by the excess of accelerated over straight-line depreciation.

[3] Nonacquiescence relating to whether, for purposes of testing the coverage requirements of section 410(b)(1) of the Code, employees of two controlled corporations must be aggregated with the controlling corporation pursuant to section 414(c), when the controlled corporations are suffering substantial financial losses.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 408.—Individual Retirement Accounts

26 CFR 1.408-7: Reports on distributions from individual retirement plans.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 2032A.—Valuation of Certain farm, etc., Real Property

26 CFR 20.2032A-4: Method of valuing farm real property.

Special use value; farms; interest rates. The 1986 interest rates to be used in computing the special use value of farm real property for which an election is made under section 2032A of the Code are listed for estates of decedents.

Rev. Rul. 86-85

This revenue ruling contains a list of the average annual effective interest rates on new Federal Land Bank loans. Under section 2032A(e)(7)(A)(ii) of the Internal Revenue Code, rates on new Federal Land Bank loans are used in computing the special use value of real property used as a farm for which an election is made under section 2032A. This revenue ruling also contains a list of the states within each land bank district. The rates in this revenue ruling may be used by estates that value farmland under section 2032A as of a date in 1986.

Average annual effective interest rates, calculated in accordance with section 2032A(e)(7)(A) of the Code and section 20.2032A-4(e) of the Estate Tax Regulations, to be used under section 2032A(e)(7)(A)(ii) are as follows:

Federal Land Bank District in which property is located	Year of valuation 1986
Baltimore	12.82
Columbia	12.14
Texas (Formerly Houston)	11.71
Louisville	12.86
Jackson (Formerly New Orleans)	12.30
Omaha	12.99
Sacramento	12.31
St. Louis	12.65
St. Paul	12.46
Spokane	12.51
Springfield	12.20
Wichita	12.77

Federal Land Bank District:

District	States
Baltimore	Delaware, District of Columbia, Maryland, Pennsylvania, Virginia, West Virginia.
Columbia	Florida, Georgia, North Carolina, South Carolina.
Texas	Texas.
Louisville	Indiana, Kentucky, Ohio, Tennessee.
Jackson	Alabama, Louisiana, Mississippi.
Omaha	Iowa, Nebraska, South Dakota, Wyoming.
Sacramento	Arizona, California, Hawaii, Nevada, Utah.
St. Louis	Arkansas, Illinois, Missouri.
St. Paul	Michigan, Minnesota, North Dakota, Wisconsin.
Spokane	Alaska, Idaho, Montana, Oregon, Washington.
Springfield	Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island, Vermont.
Wichita	Colorado, Kansas, New Mexico, Oklahoma.

Rev. Rul. 81-170, 1981-1 C.B. 454, which sets forth rates for several prior years, contains an illustrative computation of an average annual effective interest rate. The rates applicable in the case of valuations for 1982 are listed in Rev. Rul. 82-104, 1982-1 C.B. 129. The rates applicable in the case of valuations for 1983 are listed in Rev. Rul. 83-71, 1983-1 C.B. 227. The rates applicable in the case of valuations for 1984 are listed in Rev. Rul. 84-119, 1984-2 C.B. 193, and for valuations in 1985 in Rev. Rul. 85-92, 1985-2 C.B. 198.

Section 6011.—General Requirement of Return, Statement, or List

26 CFR 301.6011-2: Required use of magnetic media.

Guidance is provided to filers of certain information returns about the procedures for requesting approval for filing such information returns on a particular form of magnetic medium, or for requesting a waiver of the magnetic media filing requirements of section 6011(e) of the Code and section 1.6045-1(l) of the regulations. See Rev. Proc. 86-31, page 31.

Section 6041.—Information at Source

26 CFR 1.6041-1: Return of information as to payments of $600 or more.

Printing of substitutes for Forms 1096, 1098, 1099, 5498, and W-2G. See Rev. Proc. 86-30, page 9.

26 CFR 7.6041-1: Return of information as to payments of winnings from bingo, keno, and slot machines.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6041A.—Returns Regarding Payments of Renumerations for Services and Direct Sales

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6042.—Returns Regarding Payments of Dividends and Corporate Earnings and Profits

26 CFR 1.6042-2: Returns of information as to dividends paid in calendar years after 1962.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6043.—Returns Regarding Liquidation, Dissolution, Termination, or Contraction

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6044.—Returns Regarding Payments of Patronage Dividends

26 CFR 1.6044-2: Returns of information as to payments of patronage dividends with respect to patronage occurring in taxable years beginning after 1962.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6045.—Returns of Brokers

26 CFR 1.6045-1: Returns of information of brokers and barter exchanges.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

26 CFR 5f.6045-1: Returns of information of brokers and barter exchanges.

Printing of substitutes for Forms 1096, 1098, 1099, 5498, and W-2G. See Rev. Proc. 86-30, page 9.

Section 6047.—Information Relating to Certain Trusts and Annuity Plans

26 CFR 1.6047-1: Information to be furnished with regard to employee retirement plan covering an owner-employee.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6049.—Returns Regarding Payments of Interest

26 CFR 1.6049-4: Returns of information as to interest paid and original issue discount includible in gross income after December 31, 1982.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6050A.—Reporting Requirements of Certain Fishing Boat Operators

26 CFR 1.6050A-1: Reporting requirements of certain fishing boat operators.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6050B.—Returns Relating to Unemployment Compensation

26 CFR 1.6050B-1: Information returns by persons making unemployment compensation payments.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6050D.—Returns Relating to Energy Grants and Financing

26 CFR 1.6050D-1: Information returns relating to energy grants and financing.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6050E.—State and Local Income Tax Refunds

26 CFR 1.6050E-1: Reporting of state and local income tax refunds.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6050H. Returns Relating to Mortgage Interest Received in a Trade or Business from Individuals

26 CFR 1.6050H—IT: Questions and answers concerning information returns relating to mortgage interest received in a trade or business from individuals.

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Section 6050J.—Returns Relating To Foreclosures and Abandonments of Security

Printing of substitutes for Forms 1096, 1098, 1099, 5498 and W-2G. See Rev. Proc. 86-30, page 9.

Part III. Administrative, Procedural, and Miscellaneous

Refunds for AT&T Shareholders

Notice 86-8[1]

In Notice 725 (1-85), sent to all AT&T shareholders of record as of December 30, 1983, the Internal Revenue Service stated that an additional 39 cents per share must be reported in income as a taxable dividend in 1984 (resulting from the receipt of Pacific Telesis Group stock in the AT&T divestiture).

On April 17, 1986, the Tax Court of the United States in *Edna Louise Dunn Trust v. Commissioner*, 86 T.C. ___ (1986), ruled that no portion of the Pacific Telesis stock distributed by AT&T on January 1, 1984, represents a taxable dividend. In accordance with an agreement between the Service and AT&T, the Service will not appeal this ruling. Therefore, this decision disposes of this issue with regard to AT&T shareholders. On April 29, 1986, a News Release, IR-86-59, was issued stating that the Service was developing special procedures for claiming refunds of overpaid tax resulting from shareholders' treating a portion of the AT&T distribution as a taxable dividend. The purpose of this Notice is to describe those procedures.

Notice 773 (5-86) will be mailed to the taxpayers whom the Service had previously sent Notice 725 or other letters advising taxpayers to report the dividend as taxable income for tax year 1984. Notice 773 will describe in detail the procedures for filing a claim for refund of any additional tax that the taxpayer might have paid as a result of reporting the dividend as taxable income for tax year 1984. Accompanying Notice 773 will be a special Form 1040X overprinted with the annotation "AT&T Claim," Form 1040X instructions, and a special bar-coded return envelope. Taxpayers receiving the notices should use the bar-coded envelope provided and file their claims with the service center indicated without regard to where the original return was filed. Notice 773 will also have a detachable slip at the bottom containing a summary of the taxpayer's information. This slip should be attached to and returned with the taxpayer's completed Form 1040X.

All taxpayers who reported the Pacific Telesis stock as a taxable dividend for tax year 1984 who receive Notice 773 should use the special Form 1040X and should follow the procedures set forth in Notice 773 to claim a refund of any additional tax that resulted from reporting such dividend income. Form 843 should not be used for this purpose. The taxpayer should indicate on page 2, Part II of Form 1040X ("Explanation of Changes to Income, Deductions, and Credits") that it is an AT&T claim. Taxpayers who reported dividend income as a result of receiving pacific Telesis stock who do not receive Notice 773 should obtain and complete a regular Form 1040X (marking "AT&T Claim" on the upper left portion of the form) and mail it to the service center where the original return had been filed, indicating "AT&T Claim" on the envelope. Nominees should advise their beneficial holders to also file a regular Form 1040X with "AT&T Claim" clearly printed on the upper left corner of the form. The normal three year statute of limitations will apply to AT&T refund claims.

As a result of the Tax Court decision, some AT&T shareholders may also have to reallocate their tax basis in their AT&T stock held before the divestiture between their shares of AT&T stock and their shares in the seven regional companies that they received in the divestiture.

At the time or shortly after the divestiture, AT&T mailed a pamphlet, titled "Divestiture Tax Information for AT&T Shareowners," to its shareholders explaining how to allocate tax basis. In the pamphlet, AT&T discussed two methods of allocating basis depending on whether the shareholder reported dividend income as a result of receiving the Pacific Telesis stock. The two methods were (1) the "IRS Method," where the shareholder reported the dividend income and (2) the "Alternative method," where the shareholder did not report the dividend income. Based on the decision of the Tax Court, taxpayers who owned common stock of AT&T as of December 30, 1983, who used the "IRS Method" will have to recalculate their basis in the stock of AT&T and the seven regional companies using the "Alternative Method." The allocation factors based on the relative fair market values of such stock incorporated into "Alternative Method" may be relied on by taxpayers for allocating basis. An example demonstrating the calculation of basis under the "Alternative Method" and a worksheet are reproduced below.

In addition to recalculating basis, those shareholders of record as of December 30, 1983, who used the "IRS Method" to allocate basis and who have sold shares of AT&T common stock or stock of one or more of the seven regional companies will also have to recalculate the gain(s) or loss(es) resulting from the sale(s) using the new bases calculated under the "Alternative Method." Sales affected would include all sales of stock by such shareholders consummated subsequent to January 1, 1984, including (1) sales through the exercise of an option given to AT&T shareholders pursuant to the plan of divestiture to have the distribution agent sell shares of one or more of the regional companies and reinvest the proceeds in shares of one or more of the other companies (which would have been shown on Form 1099-B received in 1984); (2) sales resulting in shareholders receiving cash in lieu of fractional share interests in the seven regional companies; and (3) sales by independent brokers or agents. If a sale occurred in a tax year for which a tax return has been filed, taxpayers should file a Form 1040X for the year of sale to accurately report the gain or loss from such sale using the new bases calculated according to the "Alternative Method." Taxpayers who sold stock during the tax year 1984 who are also filing a claim for refund of taxes paid with respect to the reporting of dividend income from their receipt of Pacific Telesis stock should use the same Form 1040X for both, attaching (where applicable) a revised Schedule D showing the recalculation of gain(s) or loss(es) from such sale(s). Taxpayers who sold stock subsequent to tax year 1984 should also file a separate Form 1040X for the year of sale to accurately report the gain(s) or loss(es) from such sale(s) using the new bases calculated according to the "Alternative method."

If taxpayers have any questions, they

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[1] Also released as News Release IR-86-78, dated June 12, 1986.

may call the Internal Revenue Service tax assistance telephone number listed in their local directory.

Example for Method 2: The Alternative Method

Here is an example to help you calculate your new tax basis using the tax-free alternative method.

John Smith's tax basis in old AT&T was $50 per share.

(1) Mr. Smith writes $50 (his old tax basis) in the blank spaces of column C.

(2) Next, he calculates column D-the allocation factors in column B times his old tax basis in column C.

(3) In Column E the tax basis for a share of new AT&T is th esame number as in column D. However, for the regional companies, the new tax basis per share is 10 times column D. This is because Mr. Smith, like you, received one-tenth of a share in each of the regional companies for every share of old AT&T he owned.

(4) For Mr. Smith column E represents his new tax basis per share in AT&T and each of the seven regional companies.

You can also use Method 2 to determine your new tax basis for the fractional shares sold for you at divestiture or sold through the divestiture consolidation option process.

A Companies	B Allocation factors	C "Old" tax basis	D Allocation per share of "old" AT&T (B × C)	E New tax basis per share
AT&T (new)	.2850	X$50 =	$14.250 × 1 =	$14.25
Ameritech	.1033	× 50 =	5.165 × 10 =	51.65
Bell Atlantic	.1049	× 50 =	5.245 × 10 =	52.45
BellSouth	.1353	× 50 =	6.765 × 10 =	67.65
NYNEX	.0984	× 50 =	4.920 × 10 =	49.20
PacTel Group	.0888	× 50 =	4.440 × 10 =	44.40
Southwestern Bell	.0949	× 50 =	4.745 × 10 =	47.45
US WEST	.0894	× 50 =	4.470 × 10 =	44.70

Method 2
Alternative Method of Allocating Tax Basis

My tax basis in "old" AT&T was $____ per share

A Companies	B Allocation factors	C "Old" tax basis	D Allocation per share of "old" AT&T (B × C)	E New tax basis per share
AT&T (new)	.2850	×___ =	___ × 1 =	___
Ameritech	.1033	×___ =	___ × 10 =	___
Bell Atlantic	.1049	×___ =	___ × 10 =	___
BellSouth	.1353	×___ =	___ × 10 =	___
NYNEX	.0984	×___ =	___ × 10 =	___
PacTel Group	.0888	×___ =	___ × 10 =	___
Southwestern Bell	.0949	×___ =	___ × 10 =	___
US WEST	.0894	×___ =	___ × 10 =	___

26 CFR 601.201: Ruling and determination letters.

Rev. Proc. 86-29

SECTION 1. BACKGROUND

Rev. Proc. 86-3, 1986-1 I.R.B. 26, provides a list of those areas of the Internal Revenue Code under the jurisdiction of the Associate Chief Counsel (Technical) that are under extensive study and in which ruling or determination letters will not be issued until the Service resolves the issue through publication of a revenue ruling, revenue procedure, regulations, or otherwise. A list of those areas is set forth in section 5 of the revenue procedure.

SEC. 2. PROCEDURE.

Rev. Proc. 86-3 is modified by deleting from section 5 the following subsection:

> .37 Section 7701.—Definitions.—The classification of an arrangement as a fixed investment trust when the arrangement has multiple classes of equitable ownership.

SEC. 3. EFFECTIVE DATE

This revenue procedure is effective June 30, 1986, the date of its publication.

SEC. 4. EFFECTIVE ON OTHER DOCUMENTS

Rev. Proc. 86-3 is modified.

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26 CFR 601.602: Forms and instructions. (Also Part I, Sections 408, 6041, 6041A, 6042, 6043, 6044, 6045, 6047, 6049, 6050A, 6050B, 6050D, 6050E, 6050H, 6050J; 1.408-7, 7.6041-1, 1.6042-2, 1.6044-2, 1.6045-1, 1.6047-1, 1.6049-4, 1.6050A-1, 1.6050B-1, 1f.6050E-1, 1.6050D-1, 1.6050H-1T.)

Rev. Proc. 86-30

PART A. GENERAL

SEC. 1. PURPOSE

.01 The purpose of the revenue procedure is to state the requirements for: (1) reproducing paper substitutes of the forms shown below, covering payments made during the 1986 calendar year (for Forms 5498, contributions made for 1986), that are required to be filed with the Internal Revenue Service (IRS), and (2) for furnishing substitute statements to forms recipients (see Section 4.01 for definition). This revenue procedure contains specifications for the following:

(a) Form 1098, Mortgage Interest Statement.

(b) Form 1099-A, Acquisition or Abandonment of Secured Property.

(c) Form 1099-B, Proceeds from Broker and Barter Exchange Transactions.

(d) Form 1099-DIV, Dividends and Distributions.

(e) Form 1099-G, Certain Government Payments.

(f) Form 1099-INT, Interest Income.

(g) Form 1099-MISC, Miscellaneous Income.

(h) Form 1099-OID, Original Issue Discount.

(i) Form 1099-PATR, Taxable Distributions Received from Cooperatives.

(j) Form 1099-R, Total Distributions from Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc.

(k) Form W-2G, Certain Gambling Winnings.

(l) Form 5498, Individual Retirement Arrangement Information.

(m) Form 1096, Annual Summary and Transmittal of U.S. Information Returns.

.02 For the purpose of this revenue procedure, a substitute form is one that is not printed by IRS. In order for a substitute form to be acceptable to the IRS it must conform to the official form and the specifications outlined in this revenue procedure. DO NOT submit any substitutes for APPROVAL. Only those forms that conform to the official form and comply with the specifications set forth herein are acceptable. See Part A, Section 8 for the specifications that apply to form recipient statements (Copy B).

.03 This revenue procedure supersedes Revenue Procedures 85-25 and 85-52.

SEC. 2. NATURE OF CHANGES

.01 Ink color for Forms 1098, 1099 and 5498 has been changed.

.02 Specifications for substitute form recipient copies.

.03 Various editorial changes have been made.

.04 Form W-3G is now obsolete.

.05 Two additional copies for Forms W-2G and 1099-R are included.

.06 Substitute forms that do not totally conform to the specifications in this revenue procedure are not acceptable. IRS will no longer review proposed substitutes for acceptability. NO DEVIATIONS will be allowed. However, IRS will continue to clarify and resolve issues involving specifications.

.07 Where to file completed paper forms or magnetic media has been clarified.

.08 Improperly printed or prepared forms are subject to penalties.

.09 Specifications for recipient copies have been clarified.

.10 The importance of quality control for ink density has been stressed for acceptability of forms.

.11 New requirements for filing all forms with IRS on magnetic media have been added.

.12 Postal indicia "boxes" specification added.

SEC. 3. REQUIREMENTS FOR ACCEPTABLE SUBSTITUTE FORMS 1096, 1098, 1099, 5498 AND W-2G.

.01 Paper substitutes for Forms 1098, 1099, 5498, W-2G, (Copy A data) and Forms 1096 that totally conform to the specifications contained in this procedure may be privately printed and filed as returns with the IRS. DO NOT submit any substitutes for general approval (except for Carbonless paper listed in .05 below). Only those forms that conform with the official form and the specifications contained herein are acceptable.

SEC. 3. REQUIREMENTS FOR ACCEPTABLE SUBSTITUTE FORMS 1096, 1098, 1099, 5498, AND W-2G. (cont)

If you are uncertain of any specification set forth herein and want that specification clarified, you may submit a letter citing the specification in question, your interpretation of the specification, and an example of the form with your understanding of the specification to:

Internal Revenue Service
ATTN: D:R:R:IM
1111 Constitution Avenue, NW
Washington, DC 20224

You must identify the specification in question as general approval of forms is not available.

.02 Copy B (Form 1098 For Payer, other Forms 1099 For Recipient, Form 5498 For Participant, Form 1099-A For Borrower) and Copy C (Form W-2G For Winner's Records) must contain the information specified in section 8 in order to rise to the level of a "statement" or "official form" under the applicable provisions of the Internal Revenue Code. The format of this information is at the discretion of the filer with the exception of the composite Form 1099 form recipient statement specified in section 8.04.

.03 Proposed substitutes for Copy A that do not conform to these specifications are not acceptable.

.04 No IRS office is authorized to allow deviations from this revenue procedure.

.05 The use of chemical transfer paper on Copy A may be approved after review by IRS. Submit all requests with a minimum sample of 100 blank sheets of 20 lb. paper (17 × 22 − 500) to Internal Revenue Service, Attn: D:R:R:IM, 1111 Constitution Avenue, N.W., Washington, DC 20224. The paper will be tested and the results reported to the requester.

.06 Forms 1096, 1098, 1099, 5498 and W-2G are subject to annual review and possible change. Filers are cautioned, therefore, against overstocking supplies of privately printed substitutes. The specifications contained in this revenue procedure apply to 1986 forms only.

.07 Copies of the official forms for the reporting year may be obtained from most Internal Revenue offices. IRS provides only cut sheets (no carbon interleaves) of these forms. If they are not available at your local IRS District Office you may ask them to order copies for you. You should receive your order within 10 days.

.08 Only original or ribbon copies that are typed or machine printed with *black carbon based ink* may be filed with IRS. Carbon copies and photocopies are not acceptable.

SEC. 4. DEFINITIONS

.01 The term "taxpayer (form recipient) identification number (TIN)" for an individual means the individual's social security number (SSN). The SSN consists of nine digits separated by hyphens as follows: 000-00-0000. For all other form recipients, the term "taxpayer (form recipient) identification number" means the employer identification number (EIN). The EIN consists of nine digits separated by one hyphen as follows: 00-0000000. A sole proprietor may have both an EIN and a SSN.

.02 In the past the terms payee and recipient were usually synonymous. The addition of new forms to the information returns family requires different terminology to identify the recipient of a copy of the form filed with IRS (*i.e.*, 1098 is payer, 1099-A is borrower, 5498 is participant). Therefore, to alleviate any possibility of confusion, the person who is required by law to reeive a copy of the official form or information statement will be referred to as the "form recipient". The name of the appropriate form recipient (*i.e.*, person or organization whose TIN has been provided) must be shown as the first entry in the area on the form provided for the form recipient name and address. (See Section 6 for guidelines on listing the form recipient's name and TIN). No descriptive information or other name is to precede the form recipient's name. ONLY one form recipient name should appear on the first line of the form (lined up with the arrow on the left). If more than one form recipient's name must be entered, place the responsible form recipient (person or organization whose TIN is provided) on the first line. Place other form recipient's names on the succeeding name lines (up to 3 name lines are allowable).

.03 The term "filer" means the person or organization required by law to file with IRS a form listed in section 1.01 above.

.04 A corrected and/or amended return is one that corrects previously reported information. Place an "X" within the box to left of the word "Corrected".

.05 The term "substitute form" means a paper substitute of Copy A of an official form listed in section 1.01 above that totally conforms to the provisions of this revenue procedure.

.06 The term "form recipient statement" means a paper statement of the information reported on a form listed in section 1.01 above that must be furnished to a person, as so defined (form recipient) under the applicable provisions of the Internal Revenue Code.

.07 A composite statement is a substitute form recipient copy of official Forms 1099-DIV, INT, OID and PATR, in the aggregate or in any combination thereof. A filer may use a composite statement when such reporting payments are paid to the same form recipient during the calendar year. If the filer does not use a composite statement for these payments the filer must provide each respective statement to the form recipient as the case may be. A composite statement is one form (although the form itself may comprise more than one page) that contains all the requisite Form 1099 information (for the payments enumerated above). A composite statement may contain any combination of the above Form 1099 information. A composite Form 1099 can not be filed with IRS.

SEC. 5. INSTRUCTIONS FOR PREPARING SUBSTITUTE FORMS THAT WILL BE FILED WITH THE IRS

.01 The form recipient's name, street address, city, state, and ZIP code information must be TYPED OR MACHINE PRINTED IN BLACK INK on separate lines. The city, state, and ZIP code must be on the same line.

.02 The box below the form recipient's name and address may be used for the account designation number. This information is not required; however, special caution must be taken if an account designation number is being printed. This number must be unique and MUST NOT appear anywhere on the form other than in the box specified for this use. If window envelopes are used this number must not show through the window because the Postal Service may not accept them for metered mail.

.03 Filers must TYPE OR MACHINE PRINT data entries on the forms, use carbon-base BLACK ribbon, insert data in the middle of blocks well separated from other printing and guidelines, and take other measures to guarantee a clear, dark black, sharp image.

.04 Machine printed forms should be printed using a 6 lines/inch option. The first name line should be typed to the right of the arrow and the first address line should be printed on the fourth line from the arrow. This can be achieved by using double spacing.

.05 Machine printed forms should be printed in 10 pitch (*i.e.*, 10 print characters per inch).

.06 On corrected returns, an "X" must be placed within the check box located at the top of the form to the left of the word "CORRECTED". The accompanying Form 1096 for a submission of corrected returns should also contain an "X" within the "CORRECTED" box at the top of the form following its form identifier number. DO NOT type the words CORRECTED RETURN on the Form 1096, 1098, 1099, 5498 or W-2G as required in the past. All required data blocks must be completed on a corrected return since it replaces and supersedes the information return previously filed.

.07 For corrected or voided documents, enter an "X" within the appropriate box using only computer print, typewriter or #2 pencil. DO NOT use a ball-point pen or felt tip marker. The machine used to "read" paper forms generally cannot "read" these ink types.

.08 Substitute forms prepared in continuous or strip form must be burst and stripped to conform to the size specified for a single sheet before they are filed with IRS. The size specified *does not include pinfeed holes*. Pinfeed holes MUST NOT be present on forms filed with IRS.

.09 Money amounts should be printed without dollar signs ($), ampersands (&), asterisks (*), commas (,) or other special characters. However, use decimal points to indicate dollars and cents.

.10 DO NOT FOLD Forms 1096, 1098, 1099, or 5498 mailed to IRS. Mail these forms flat in an appropriately sized envelope or box. Folded documents cannot be readily moved through the scanner transport used in IRS processing.

.11 *DO NOT STAPLE* Forms 1096 to the returns being transmitted. Staple holes in the vicinity of the return code number reduce our ability to machine scan the return code number which is used to identify the type of document being processed.

.12 MAIL completed paper forms addressed in this revenue procedure to the IRS service center specified in the *Instructions for Forms 1099, 1098, 5498 1096, and W-2G.*

.13 Filers who submit privately printed or incorrectly prepared forms and IRS determines they are not acceptable may be subject to penalties under section 6652 of the Internal Revenue code. The penalty is $50 for each form which the IRS cannot accept as a return under the provisions set out in this revenue procedure.

SEC. 6. TAXPAYER IDENTIFICATION NUMBERS

.01 Under section 6109 of the Internal Revenue Code, a person with respect to whom a return, statement, or other document is required to be made by another person must furnish his taxpayer identification number (TIN) to such other person. The number must be furnished to the filer whether or not the form recipient is required to file a tax return or is covered by Social Security. Section 6109 also requires filers to request the TIN's and place them on returns required to be filed with IRS.

.02 Filers must provide correct TIN's on all forms submitted. It is particularly important that correct social security and employer identification numbers for form recipients be provided on magnetic media or paper forms submitted to IRS.

.03 Section 6676 of the Internal Revenue code imposes a $50 penalty on filers for each return filed with an incorrect or missing TIN. For payments of interest and dividends, the penalty is self-assessable on Form 8210, Self-Assessed Penalties Return.

.04 The TIN furnished to IRS depends primarily upon the manner in which the account is maintained in the filer's records. The TIN provided must be that of the owner of record. If an account is recorded as a joint account, *i.e.*, more than one person is listed on the account, furnish the TIN and name of the first person listed on the record. For individuals, the TIN is the SSN (those individuals operating a business as a sole proprietorship may have both an EIN and a SSN). A nonresident alien will generally have a TIN that is similar in format to a SSN. For other entities, it usually is an EIN.

.05 Sole proprietors who are reporting as filers should show their EIN on the return if required to have an EIN. If not, they should show their SSN. However, if the sole proprietor is a form recipient, then the SSN should be used.

.06 The charts below will help you determine the TIN to be furnished to IRS.

Chart 1. Guidelines for Social Security Numbers

Type of account	For Form Recipient TIN enter the Social Security number of	On the 1st Name Line of the Form Recipient Portion of the Return Enter the Name of
1. An individual's account.	The individual.	The individual.
2. A joint account (two or more individuals, husband and wife, adult and minor).	The actual owner of account. (If more than one owner, the first individual on the account).	The individual whose SSN is entered.
3. Account in the name of a guardian or committee for a designated ward, minor, or incompetent person.	The ward, minor, or incompetent person.	The individual whose SSN is entered.
4. Custodian account of a minor (Uniform Gift to Minors Act).	The minor.	The minor.
5. The usual revocable savings trust account (grantor is also trustee).	The grantor-trustee.	The grantor-trustee.

Chart 1. Guidelines for Social Security Numbers—Continued

Type of account	For Form Recipient TIN enter the Social Security number of	On the 1st Name Line of the Form Recipient Portionof the Return Enter the Name of
6. So-called trust account that is not a legal or valid trust under state law.	The actual owner.	The actual owner.
7. Sole proprietorship.	The owner.	The owner.

Chart 2. Guidelines for Employer Identification Numbers

For this type of account	For Form Recipient TIN enter the Employer Identification number of	On the 1st Name Line of the Form Recipient Portion of the Return Enter the Name of
1. A valid trust, estate, or pension trust.	Legal entity. (Do not furnish the identification number of the personal representative or trustee unless the name of the representative or trustee is used in the account title).	The legal trust, estate, or pension trust.
2. A Corporate account.	The corporation.	The corporation.
3. An association, club, religious, charitable, or educational or other tax exempt organization.	The organization.	The organization.
4. A partnership account held in the name of the business.	The partnership.	The partnership.
5. A broker or registered nominee/middleman.	The broker or nominee/middleman.	The broker or nominee/middleman.
6. Account with the Department of Agriculture in the name of a public entity, such as a state or local government, school district, or prison, that receives agriculture program payments.	The public entity.	The public entity.

SEC. 7. MAGNETIC MEDIA FILING

.01 IRS encourages all filers or nominees (hereafter collectively referred to as filers) to file information returns on magnetic media instead of paper forms. All forms listed in Sec. 1.01 may be filed on magnetic media.

.02 Any person who is required to file more than 50 Forms 1099-DIV (for dividend reportable under section 6042 of the IRC), 1099-INT (except for interest reportable under section 6049), 1099-OID or 1099-PATR in any combination, for a calendar year MUST file these returns on magnetic media. This requirement applies to any person for any period unless such person establishes that this requirement would result in undue hardship and requests a waiver from the filing requirements. To request a waiver from filing on magnetic media, submit a waiver request 90 days before the due date of the return *and send it to the following address:* Magnetic Media Reporting, Internal Revenue Service, National Computer Center, P.O. Box 1359, Martinsburg, WV 25401-1359. Effective January 1, 1986, *all* requests for relief should be sent to the National Computer Center address.

.03 Regulations section 1.6045-1(1) requires brokers and barter exchanges to use magnetic media in reporting any Form 1099-B data to IRS. Generally, new brokers and new barter exchanges may request an undue hardship exception by filing a waiver request, by the end of the second month following the month in which they become a broker or barter exchange, with the IRS National Computer Center. Effective January 1, 1986, *all* requests for relief should be sent to the National Computer Center address.

.04 Regulations section 301.6011-2 requires the use of magnetic media for filing Forms 1098, 1099-A, 1099-G, 1099-MISC, 1099-R, 5498 and W-2G for payments to 500 or more form recipients for any calendar year beginning after December 31, 1985, (250 or more form recipients for any calendar beginning after December 31, 1986). This requirement applies to any person filing after the above stated periods unless such person establishes that this requirement would result in undue hardship. A request for a waiver should be submitted 90 days before the due date of the return and directed to the following address: Magnetic Media Reporting, Internal Revenue Service, National Computer Center, P.O. Box 1359, Martinsburg, WV 25401-1359. Effective January 1, 1986, all requests for relief should be sent to the National Computer Center address.

.05 Specifications for filing information returns on tape, 8 inch and 5¼ inch diskette, cassette or mini-disk are contained in various revenue procedures relating to Requirements and conditions for Filing Information Returns on Magnetic Media. Copies of these procedures may be obtained from any Internal Revenue District office or by contacting the IRS National Computer Center. Filers or agents who are required to, or want to file information returns on magnetic media, must file Form 4419, Application for Magnetic Media Reporting of Information Returns. Forms 4419, must be filed prior to submitting returns on magnetic media. IRS will provide a written reply to the applicant and further instructions at the time of approval. The application must be filed at the following address: Magnetic Media Reporting, Internal Revenue Service, National Computer Center, P.O. Box 1359, Martinsburg, WV 25401-1359. Effective January 1, 1986, the magnetic media program was centralized at the National Computer Center and all applications and information returns filed on magnetic media should be sent to the National Computer Center address in 1986.

.06 Since many states accept information returns filed on magnetic media, savings may be obtained if similar media is used for filing with IRS and state tax agencies. For information regarding state magnetic media filing requirements, filers should contact the respective state tax authority.

SEC. 8. STATEMENT TO FORM RECIPIENTS AND FORM RECIPIENT COPIES

.01 For payments of reportable interest and dividends (reportable on Forms 1099-DIV (for dividends reportable under section 6042 of the IRC), 1099-INT (except for interest reportable under section 6041), 1099-OID or 1099-PATR made in 1984 and subsequent years, an official Form 1099 must be furnished to a form recipient either in a separate first-class mailing or in person. These forms may be mailed or provided to the form recipient with other Forms 1098, 1099 or 5498 form recipient statements, or with Form W-9 and Form W-8 solicitations. However, no other information may be mailed with the form recipient statement or provided in person with the form recipient statement without violating the separate mailing requirements.

.02 The requirement to furnish form recipients with an official form *1099-DIV, INT, OID and PATR,* may be met by furnishing a substitute Form 1099 (form recipient copy) if it contains language substantially similar to that of the official form such as the aggregate amount paid to (or received from) the form recipient, any amount of tax withheld under IRC section 3406, the name, address and TIN of the person making the return and any other information required by the official form. Generally, information not required by the official form should not be included on the form because it may violate the separate mailing requirements. In addition, the form recipient copy of interest, dividends, patronage dividends and original issue discount paid to the form recipient must contain the information listed below.

1 All money amounts required to be reported to the form recipient must be titled and numbered on the form recipient copy in substantially the same manner as those of the official form. For instance, dividend income must be labeled as "qualifying" or "not qualifying for exclusion".

2 The form recipient copy must contain all applicable form recipient instructions provided on the official form.

3 Form recipient copies covering reportable interest, dividends, patronage dividends and original issue discount must contain the following statement, in bold and conspicuous type, "This is important tax information and is being furnished to the Internal Revenue Service. If you are required to file a return, a negligence penalty or other sanction will be imposed on you if this income is taxable and IRS determines that it has not been reported."

4 The form recipient copy must contain the Office of Management and Budget (OMB) number prescribed on the official form.

5 The form recipient copy must show the title of the official Form 1099 for which it substitutes.

.03 If the form recipient copy contains all the information listed above, layout and format of the form is at the discretion of the filer.

.04 A composite form recipient copy is permitted for reportable payments of interest, dividends, patronage dividends, and/or original issue discount (Forms 1099-DIV, INT, OID or PATR) when one filer is reporting any or all of these payments during a calendar year to the same form recipient. Although the composite form recipient copy may be on one form, the format of the composite form recipient copy must satisfy the following requirements in addition to the requirements listed in .02 above.

1 All information pertaining to a particular type of payment must be located and blocked together on the form and must be separate from any information covering other types of payments included on the form.

2 The title of the official form or forms for which this form recipient copy substitutes must be shown at the beginning of each appropriate block of information.

3 Any information required by the official form that would otherwise be repeated in each information block is only required to be listed once in the first information block of the composite form. For example, there is no requirement to report the name of the filer in each information block.

.05 Statements to form recipients of other reportable payments on Forms 1098, 1099-A, 1099-B, 1099-G, 1099-MISC (except payments reportable under section 6045), 1099-R, 5498, 1099-DIV (except for payments reportable under section 6047), 1099-INT (for payments reportable under section 6041) and W-2G as cited in Part A, Section 1 should meet the following requirements:

1. The filer and form recipient information required on the statement must be included.

2. All money amounts and information required to be reported to the form recipient must be titled on the form recipient statement in substantially the same manner as those on the official form.

3. Form recipient statements must contain the following statement, "This information is being furnished to the Internal Revenue Service."

4. Appropriate instructions to the form recipient, similar to those on the official form, must be provided to aid in the proper reporting of the items on the form recipients' income tax returns. For payments reported on For

1099-B, the requirement to include on the statement furnished to form recipients instructions that are substantially similar to those on the official form, may be satisfied by providing form recipients with a single set of instructions with respect to all statements required to be furnished in a calendar year.

.06 Statements specified in .05 above, may contain information other than that required by the official form. However, if other information is included, such statments cannot be mailed with Forms 1099-DIV, INT, OID or PATR or their substitutes without violating the separate mailing requirements.

.07 A composite form recipient statement specified in .05 above is permitted when one filer is reporting any or all of these payments during a calendar year to the same form recipient. A composite statement is not allowable for a combination of forms listed in .05 above and forms listed in .04 above. For example, a composite statement of Form 1098 and 1099-INT (for interest reportable under section 6049) is not allowable. Although the composite form recipient copy may be on one form the format of the composite form recipient copy must satisfy the following requirements listed in .05 above.

1. All information pertaining to a particular type payment must be located and blocked together on the form and must be separate from any information covering other types of payments included on the form.

2. The title of the official form or forms for which the form recipient statement substitutes must be shown at the beginning of the appropriate block of information.

3. Any information required by the official form that would otherwise be repeated in each information block is only required to be listed once in the first information block on the composite form. For example, there is no requirement to report the name of the filer in each information block.

PART B—SUBSTITUTE FORM FORMAT REQUIREMENTS (EXCLUDING FORM W-2G)

SEC. 1. GENERAL

.01 The following specifications prescribe the format requirements of Forms 1098 (Copy A), 1099 (Copy A), 5498 (Copy A), and 1096.

.02 The form identifying number (*e.g.*, 9191 for Forms 1099-DIV) must be printed in non-reflective black carbon-based ink in print positions 25 through 29 using an OCR A font. The ballot boxes located to the right of the form identifying number must be 10-point boxes.

Note: If the ballot box is checked indicating a corrected return or a "void" return, more than 50% of the box must be covered by an "X." *Do not type* "CORRECTED RETURN" on the top of the form. All required data must be completed on the corrected form since it replaces and supersedes the information return previously filed.

SEC. 2. SPECIFICATIONS FOR FORMS 1096, AND COPY A OF FORMS 1098, 1099 AND 5498

.01 The substitute form must be an exact replica of the official reproduction proof with respect to layout and contents. "Spot Carbons" are *not permitted* for Copy A. The printing of the Government Printing Office (GPO) symbol must be deleted. Specifications for Copy A are provided in Exhibits A thru O.

.02 Color and quality of paper. Paper for Copy A (cut sheets and continuous pinfeed forms) as specified by JCP 0-25, dated November 29, 1978, must be: White 100% bleached chemical wood, optical character recognition (OCR) bond produced in accordance with the following specifications:

NOTE: Reclaimed fiber in any percentage is permitted, provided the requirements of this standard are met.

1	Acidity: pH value, average, not less than	4.5
2	Basis Weight 17 × 22	
	500 cut sheets	20
	Metric equivalent—g/m2	75
	A Tolerance of ±5 pct. shall be allowed	
3	Stiffness: Average, each direction, not less than—milligrams	50
4	Tearing strength: Average, each direction, not less than—grams	40
5	Opacity: Average, not less than—percent	82
6	Thickness: Average—inch—0.0038	
	Metric equivalent—mm—0.097	
	A tolerance of +0.0005 inch (0.0127mm) shall be allowed.	
	Paper shall not vary more than 0.0004 inch (0.0102 mm) from one edge to the other.	
7	Porosity: average, not less than—seconds	10
8	Finish (smoothness): Average, each side—seconds	20-55
	For information only, the Sheffield equivalent—units	170-100
9	Dirt: Average, each side, not to exceed—parts per million	8

.03 All printing will be in maroon OCR dropout ink except for Forms 1096 (see .04 below), as specified, except for the 4-digit form identifying numbers appearing in the upper middle left margin on the official IRS form, which will be printed in nonreflective carbon-based black ink. All other printing will be in maroon OCR dropout ink with or comparable to the specifications below. The screened area of any substitute form should generally correspond to that present on the official form. Separation between fields must be 0.1 inch including screen. The numbered captions are printed as a solid with no screened background. The maroon OCR dropout ink must be Sinclair-Valentine J-31359 or an exact match. Horizontal screening should follow the standard format and allow for typewriter spacing.

OCR Specifications

Contractor must have or initiate a quality control program to assure OCR ink density. In addition he must have at or adjacent to his production area either a MacBeth PCM tester or a Kidder 082A tester in order that testing may be accomplished at regular intervals throughout a shift.

Paper and Ink

Readings will be made when printed on approved 20 lb. White OCR bond with a reflectance of not less than 85%. Black ink used must not have a reflectance greater than 15%. These readings are based on requirements of the "REI Input 80 Model C1 or D" Optical Scanner using Sinclair and Valentine J-31859 Maroon ink or equal.

MacBeth PCM II Tester

The tested Print Contrast Signal (PCS) values when using the McBeth PCM-II tester on the "C" scale must range from .13 minimum to .19 maximum.

Kidder 082A Tester

The tested Print Contrast Signal (PCS) values when using the Kidder 082A tester on the Infra Red (IR) scale must range from .32 minimum to .38 maximum. White calibration disc must be 100%, sensitivity must be set at one (1).

Alternative Tester

If an alternative tester is used it must be approved by Government so that tested (PCS) values can be established with this equipment. Approval may be obtained by writing to the following address:

Commissioner of Internal Revenue
Attn: PM:S:FM:P Room 1237
Al Thoren or Larry Porter
1111 Constitution Avenue N.W.
Washington, DC 20224

Printing exceeding the maximum screen density will cause the forms to be nonprocessable. If this happens the filer will be required to refile on acceptable forms and will be subject to a $50 penalty for each form printed or prepared that is filed in a nonprocessable format.

.04 For Forms 1096, all printing will be in red OCR dropout ink, as specified, except for the 4-digit form identifying number appearing in the upper middle margin on the official IRS form, which will be printed in nonreflective black carbon-based ink. All other printing will be in red OCR dropout ink with or comparable to the specifications below. The screened area of any substitute form should generally correspond to that present on the official form. Separation between fields must be 0.1 inch including screen. Horizontal screening should follow the standard format and allow for typewriter spacing.

OCR Specifications

Contractor must have or initiate a quality control program to assure OCR ink density. In addition he must have at or adjacent to his production area either a MacBeth PCM tester or a Kidder 082A tester in order that testing may be accomplished at regular intervals throughout a shift.

Paper and Ink

Readings will be made when printed on approved 20 lb. White OCR bond with a reflectance of not less than 85%. Black ink used must not have a reflectance greater than 15%. These readings are based on requirements of the "REI Input 80 Model C1 & D" Optical Scanner using Sinclair and Valentine J-6983 Red ink or equal.

MacBeth PCM II Tester

The tested Print Contrast Signal (PCS) values when using the MacBeth PCM-II tester on the "C" scale must range from .01 minimum to .06 maximum.

Kidder 082A Tester

The tested Print Contrast Signal (PCS) values when using the Kidder 082A tester on the Infra Red (IR) scale must range from .12 minimum to .21 maximum. White calibration disc must be 100%, sensitivity must be set at one (1).

Alternative Tester

If an alternative tester is used it must be approved by Government so that tested (PCS) values can be established with this equipment. Approval may be obtained by writing to the following address:

Commissioner of Internal Revenue
Attn: PM:S:FM:P Room 1237
Al Thoren or Larry Porter
1111 Constitution Avenue N.W.
Washington, DC 20224

The red OCR dropout ink must be Sinclair-Valentine J-6983 or an exact match.

.05 Typography—Type must be substantially identical in size and shape with corresponding type on the official form. All rules are either 1-point or ½-point. Rules must be identical to that on the official IRS form. NOTE: The form identifying number must be nonreflective carbon-based black ink in OCR A font.

.06 Dimension—Three official Forms 1098, 1099 or 5498 (Copy A) are contained on a single page which is 8 inches wide (exclusive of any snapstubs and/or pinfeed holes) by 11 inches deep. The top margins must be 2/6 inch, and the right margin must be ¼ inch plus or minus .0313 inch. If the right and top margins are properly aligned the left margin for all forms will be correct. All margins must be free of all printing.

.07 The depth of the individual trim size of each form on a page must be the same (3⅔ inches) as that of the official reproduction proof.

.08 Perforations are required between forms on all copies (except Copy A) to enable the separation of individual forms.

.09 The words "For Paperwork Reduction Act Notice and instructions for completing this form, see *Instructions for forms 1099, 1098, 5498, 1096 and W-2G" must* be printed on Copy A and Copy C.

.10 The OMB Number *must* be printed on *each* ply in the same location as on the official form.

.11 *Privately printed continuous substitute forms (Copy A) must be perforated at each 11" (3-on) page depth. No perforations are allowed between the 3⅔" forms on a single copy page of Copy A.*

.12 *The words "Do NOT cut or Separate forms on This Page"* must be printed in maroon dropout ink (as required by form specifications) between the three forms. NOTE: Perforations are required between all of the other individual copies (Copies B and C) included in the set.

.13 The back of a substitute Copy A must be free of all printing.

.14 Carbonized. *"Spot carbons"* and *not permitted* for Copy A. Interleaved carbon must be of good quality to assure legibility of information on all parts to preclude smudging and should be black. "Chemical transfer paper" is now permitted (see Section 3.05 of Part A above).

.15 Printer's symbol—The GPO symbol must not be placed on substitute Copy A. *In place of the GPO symbol*, the employer identification number (EIN) of the forms printer must be printed in the bottom margin on the face of each individual form of Copy A.

.16 In the past, substitute Forms 1098, 1099 and 5498 were approved allowing a *black postal indicia* box in the nonscanned upper right hand corner of the form. Because of the difficulty IRS has experienced in processing these forms this deviation is NO LONGER ACCEPTABLE. However, you may use a postal indicia if it meets the following cirtiera: a) it is printed in the OCR ink color prescribed for the form; b) no part of the indicia is within 1 print position of the scannable area; c) there is a 2/6 inch head margin; and d) there is a ¼ inch right margin.

PART C. SUBSTITUTE FORM FORMAT REQUIREMENTS FOR FORM W-2G ONLY

SEC. 1. GENERAL

.01 The following specifications prescribe the format requirements of Form W-2G—COPY A ONLY.

.02 A filer may file a substitute Form W-2G with IRS (hereinafter referred to as substitute Copy A). Substitute forms submitted to IRS must be exact replicas of the official forms with respect to layout and contents. The Government Printing Office symbol must be deleted.

SEC. 2. SPECIFICATIONS FOR COPY A FOR FORMS W-2G

.01 Color and Quality of Paper.

1 Paper for Copy A must be white chemical wood bond, or equivalent, 20 pound (basis 17 × 22 — 500), plus or minus 5 percent. The paper must consist of principally bleached chemical woodpulp and be free from unbleached or ground woodpulp or recycled printed paper. It also must be suitably sized to accept ink without feathering.

2 Copies B and C (to be filed with tax return and for Winner's records) and D (For Payer) are provided in the official assembly solely for the convenience of the filer. Filers may choose the format, design, color and quantity of the paper used for these copies.

3 Copies 1 and 2 are provided to file with the state. Some states have requested the addition of these two plys and they have been included solely for the convenience of the filer.

.02 Color and Quality of Ink—All printing must be in a high quality nongloss black ink. Bar codes should be free from picks and voids.

.03 Typography—Type must be substantially identical in size and shape with corresponding type on the official form. All rules on the document are either 1-point (0.015 inch) or 3 point (0.045). Vertical rules must be parallel to the left edge of the document; horizontal rules, parallel to the top edge.

.04 Dimensions—The official form is 8 inches wide × 3⅔ inches deep, exclusive of a ⅔ inch snap stub on the left side of the form. The snap feature is not required on substitutes. The top and right margins must be ¼ inch plus or minus .0313. If the top and right margins are properly aligned the left margin for all forms will be correct. All margins must be free of all printing. If the substitute forms are in continuous or strip form, they must be burst and stripped to conform to the size specified for a single form before they are filed with IRS.

1 The width of a substitute Copy A must be 8 inches. The left margin must be free of all printing other than that shown on the official form.

2 The depth of a substitute Copy A must be 3⅔ inches.

.05 Clear Area—The back of Copy A must be free of all printing.

.06 Carbonized forms or "spot carbons"—Carbonized forms and "spot carbons" are not permitted. Interleaved carbons, if used, must be of good quality to preclude smudging and should be black.

.07 Printer's Symbol—The Government Printing Office symbol must not be printed on substitute Forms W-2G. In place thereof, the printer's employer identification number should appear in the same place on such substitute forms.

PART D. ADDITIONAL INSTRUCTIONS FOR FORMS 1098, 1099, 5498 and W-2G

SEC. 1. OTHER COPIES

.01 Copies 1 and 2, B, C and D for Forms W-2G are included in the official assembly for the convenience of the filer. Although there is no requirement that privately printed substitute forms include these copies, Copy B (and C for Form W-2G) will satisfy the requirement of law and regulations concerning the statement of information that is required to be furnished to the form recipient. Copy C (D for Forms W-2G) may be desired as a filer record copy.

.02 Arrnagement of Assembly—Except as provided in paragraph .03 below, the parts of the assembly shall be arranged, from top to bottom, as follows: Forms 1099 (except 1098, 1099-A, 1099-R, 5498, and W-2G) Copy A (Original), "For Internal Revenue Service Center"; Copy B "For Recipient"; Copy C "For Payer". Form 1098 Copy A (original), "For Internal Revenue Service Center"; Copy B "For Payer"; Copy C "For Recipient". Form 1099-A Copy A (Original), "For Internal Revenue Service Center"; Copy B "For Borrower"; Copy C "For Lender", Form 1099-R Copy A (Original), "For Internal Revenue Service", Copy 1, "For State Tax Department", Copy B, "For Recipient", Copy 2, "To be filed with recipient's state income tax return", Copy C, "For Payer", Form W-2G Copy A (Original), "For Internal Revenue Service Center"; Copy 1, "For state tax department", Copy B and C "For Winner's Records"; Copy 2 "To be filed with winners state income tax returns"; copy D "For Payer"; Form 5498 Copy A (Original), "For Internal Revenue Service Center"; copy B "For Participant"; Copy C "For Trustee or Issuer".

SEC. 2. REPRODUCTION PROOFS

.01 Reproduction Proofs—Order blanks for reproduction proofs are mailed annually to requestors of record, and to other users upon request. Printers and others wishing to obtain reproduction proofs may send their requests to:

Internal Revenue Service
Attn: Distribution Manager
PM:S:FM:P—Room 1528
1111 Constitution Avenue, N.W.
Washington, DC 20224

.02 A charge of $1.00 per printed page will be made for each reproduction proof regardless of page size. Invoices will be made after orders are filled.

SEC. 3. OMB REQUIREMENTS

.01 Office of Management and

Budget (OMB) Requirements for Substitute Forms—Pub. L. 96-511 requires: (1) OMB approval of Internal Revenue Service Tax forms, (2) that each form show (in the upper right corner) the OMB approval number and any expiration date (on continuous use forms only), and (3) the form (or its instructions) state why IRS is collecting the information, how we will use it and whether it must be given to us. The official IRS forms will contain this information.

.02 As it applies to substitute Service forms this means:

1 All substitute forms must show the OMB number and any expiration date as it appears on the official IRS form.

2 For Copy A, the OMB number must appear exactly as shown on the official IRS form.

3 For any copy other than Copy A, the OMB number must use one of the following formats:

a OMB No. XXXX-XXXX (preferred) or;

b OMB # XXXX-XXXX

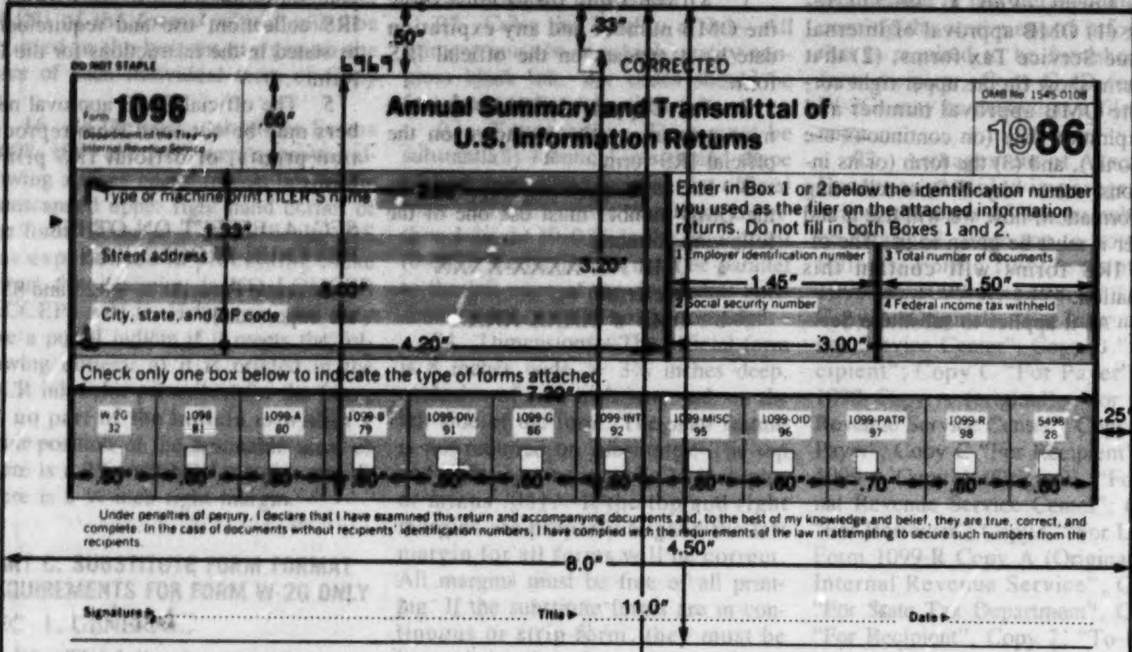
4 You must inform the users of your substitute forms of the reasons for IRS collection, use and requirements, as stated in the instructions for the IRS form.

5 The official OMB approval numbers may be obtained from reproduction proofs, or official IRS printed forms.

SEC. 4. EFFECT ON OTHER REVENUE PROCEDURES

Revenue Procedures 85-25 and 85-52 are superseded.

Exhibit A



DO NOT STAPLE

☐ CORRECTED

Form **1096**
Department of the Treasury
Internal Revenue Service

Annual Summary and Transmittal of U.S. Information Returns

OMB No. 1545-0108

1986

▶ Type or machine print FILER'S name

Street address

City, state, and ZIP code

Enter in Box 1 or 2 below the identification number you used as the filer on the attached information returns. Do not fill in both Boxes 1 and 2.

1 Employer identification number	3 Total number of documents
2 Social security number	4 Federal income tax withheld

Check only one box below to indicate the type of forms attached.

W-2G 32	1098 81	1099-A 80	1099-B 79	1099-DIV 91	1099-G 86	1099-INT 92	1099-MISC 95	1099-OID 96	1099-PATR 97	1099-R 98	5498 28
☐	☐	☐	☐	☐	☐	☐	☐	☐	☐	☐	☐

Under penalties of perjury, I declare that I have examined this return and accompanying documents and, to the best of my knowledge and belief, they are true, correct, and complete. In the case of documents without recipients' identification numbers, I have complied with the requirements of the law in attempting to secure such numbers from the recipients.

Signature ▶ .... Title ▶ .... Date ▶ ....

Please return this entire page to the Internal Revenue Service. Photocopies are NOT acceptable.

Paperwork Reduction Act Notice

We ask for this information to carry out the Internal Revenue laws of the United States. We need it to ensure that taxpayers are complying with these laws and to allow us to figure and collect the right amount of tax. You are required to give us this information.

Instructions

Changes You Should Note.—If you have received a preprinted label from IRS, place it in the name and address area of the form using the brackets as indicators. Make any necessary corrections on the label.

Do not mark in the boxes at the bottom of this page. The boxes are for use by Internal Revenue Service only.

For 1986 and later years, transmit Forms W-2G and 1099-R to IRS with Form 1096.

The box for the number of forms without TINs has been eliminated. In Box 4, enter the total Federal income tax withheld as shown on Forms 1099 or W-2G filed with this Form 1096.

Purpose of Form.—Use this form to transmit Forms W-2G, 1098, 1099, and 5498 to the Internal Revenue Service.

Completing Form 1096.—If you are not using a preprinted label, enter the filer's name, address, and taxpayer identification number (TIN) in the spaces provided on the form. A filer includes a payer, a recipient of mortgage interest payments, a broker, a barter exchange, a trustee or issuer of an individual retirement arrangement (including an IRA, SEP, or DEC), and a lender who acquires an interest in secured property or who has reason to know that the property has been abandoned. Individuals not in a trade or business should enter their social security number in Box 2; sole proprietors and all others should enter their employer identification number in Box 1. However, sole proprietors who are not required to have an employer identification number should enter their social security number in Box 2.

Group the forms by form number and submit each group with a separate Form 1096. For example, if you must file both Forms 1099-DIV and Forms 1099-INT, complete one Form 1096 to transmit your Forms 1099-DIV and another Form 1096 to transmit your Forms 1099-INT.

In Box 3, enter the number of forms you are transmitting with this Form 1096. Do not include blank or voided forms in your total. Enter the number of correctly completed forms, not the number of pages, being transmitted. For example, if you send one page of three-to-a-page Forms 5498 with a Form 1096 and you have correctly completed two Forms 5498 on that page, enter 2 in Box 3 of Form 1096. Check the appropriate box to indicate the type of form you are transmitting.

If you are transmitting forms that include TINs and others with no TINs, you may submit them with one Form 1096, as long as they are all the same form number. Show the total number of documents being transmitted in Box 3.

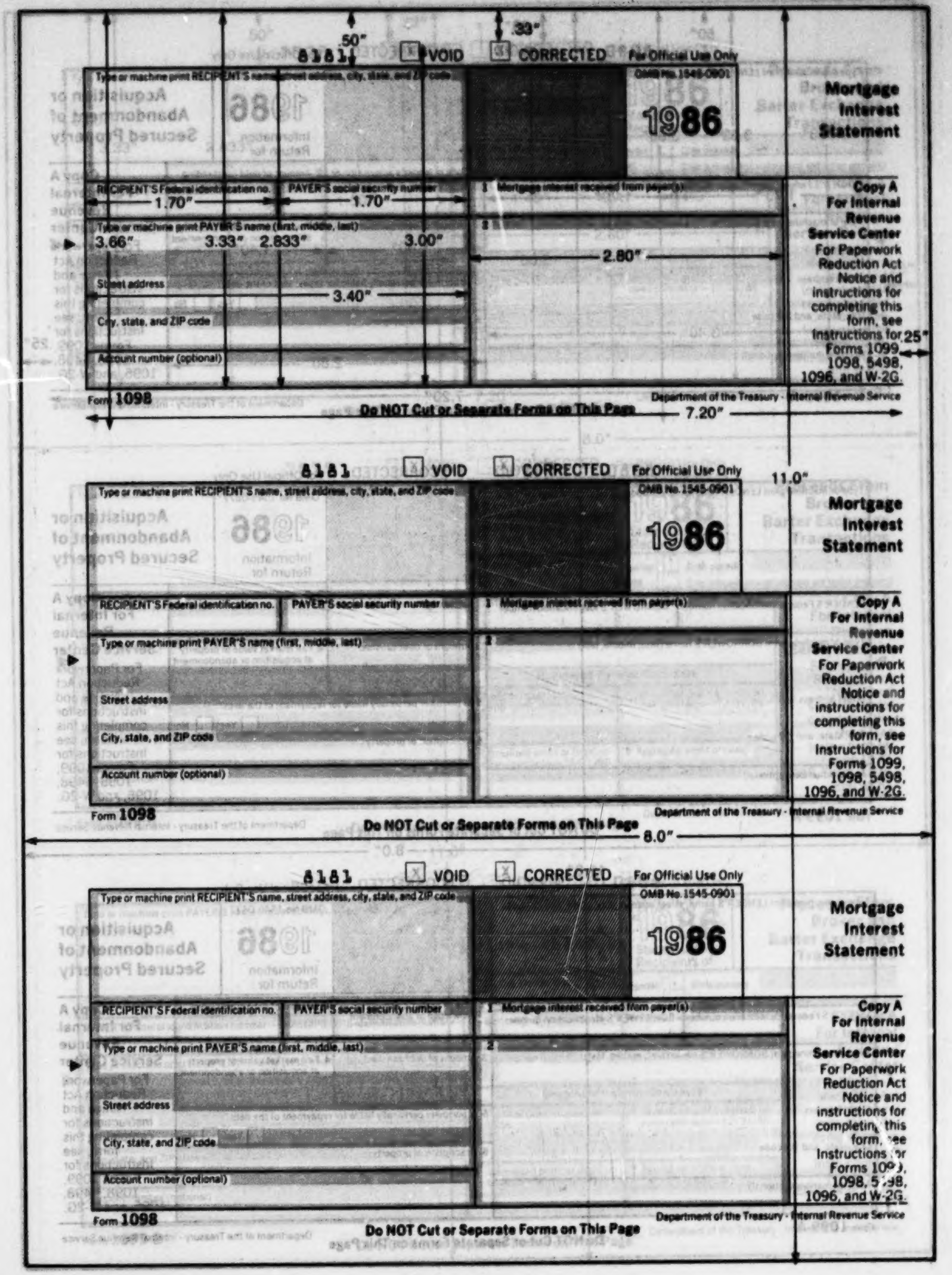
If you are filing a Form 1096 for corrected information returns, mark over the "X" in the CORRECTED box at the top of this form.

For more information about filing, see the separate Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

☐ ☐☐☐☐☐ **For Official Use Only**

Form **1096** (1986)

Exhibit B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8181 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print RECIPIENT'S name, street address, city, state, and ZIP code		OMB No. 1545-0901 1986	**Mortgage Interest Statement**
RECIPIENT'S Federal identification no.	PAYER'S social security number	1 Mortgage interest received from payer(s)	**Copy A For Internal Revenue Service Center** For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Type or machine print PAYER'S name (first, middle, last) Street address City, state, and ZIP code Account number (optional)		2	

Form **1098** Department of the Treasury - Internal Revenue Service

Do NOT Cut or Separate Forms on This Page

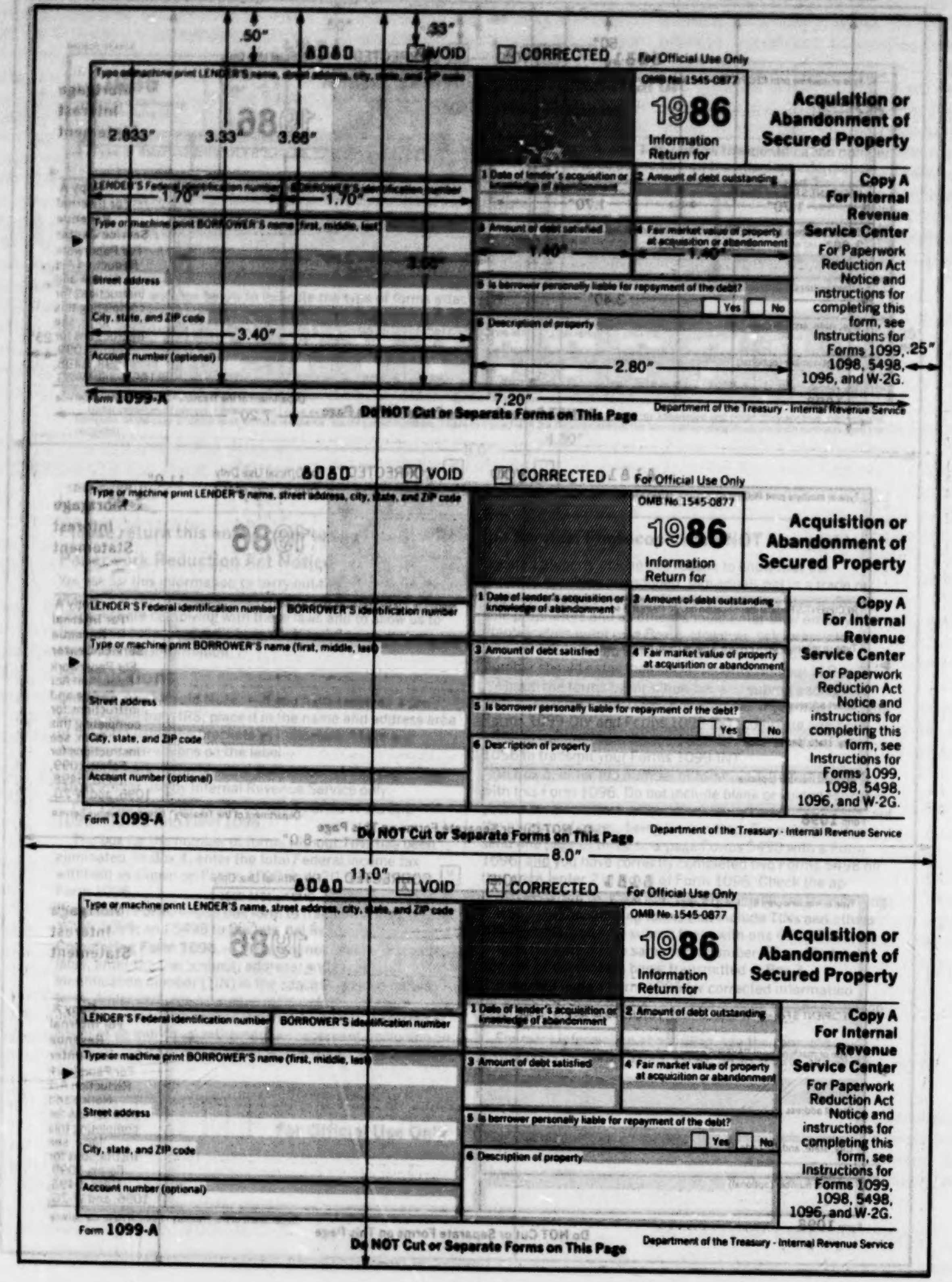
8181 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print RECIPIENT'S name, street address, city, state, and ZIP code
OMB No. 1545-0901
1986
Mortgage Interest Statement
RECIPIENT'S Federal identification no.
PAYER'S social security number
1 Mortgage interest received from payer(s)
Copy A For Internal Revenue Service Center For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Type or machine print PAYER'S name (first, middle, last)
2
Street address
City, state, and ZIP code
Account number (optional)
Form 1098 Department of the Treasury - Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

8181 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print RECIPIENT'S name, street address, city, state, and ZIP code
OMB No. 1545-0901
1986
Mortgage Interest Statement
RECIPIENT'S Federal identification no.
PAYER'S social security number
1 Mortgage interest received from payer(s)
Copy A For Internal Revenue Service Center For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Type or machine print PAYER'S name (first, middle, last)
2
Street address
City, state, and ZIP code
Account number (optional)
Form 1098 Department of the Treasury - Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

Exhibit C



8080 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print LENDER'S name, street address, city, state, and ZIP code

OMB No. 1545-0877

1986

Information Return for

Acquisition or Abandonment of Secured Property

LENDER'S Federal identification number

BORROWER'S identification number

Type or machine print BORROWER'S name (first, middle, last)

Street address

City, state, and ZIP code

Account number (optional)

1 Date of lender's acquisition or knowledge of abandonment

2 Amount of debt outstanding

3 Amount of debt satisfied

4 Fair market value of property at acquisition or abandonment

5 Is borrower personally liable for repayment of the debt? ☐ Yes ☐ No

6 Description of property

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **1099-A**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

8080 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print LENDER'S name, street address, city, state, and ZIP code

OMB No. 1545-0877

1986

Information Return for

Acquisition or Abandonment of Secured Property

LENDER'S Federal identification number

BORROWER'S identification number

Type or machine print BORROWER'S name (first, middle, last)

Street address

City, state, and ZIP code

Account number (optional)

1 Date of lender's acquisition or knowledge of abandonment

2 Amount of debt outstanding

3 Amount of debt satisfied

4 Fair market value of property at acquisition or abandonment

5 Is borrower personally liable for repayment of the debt? ☐ Yes ☐ No

6 Description of property

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **1099-A**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

8080 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print LENDER'S name, street address, city, state, and ZIP code

OMB No. 1545-0877

1986

Information Return for

Acquisition or Abandonment of Secured Property

LENDER'S Federal identification number

BORROWER'S identification number

Type or machine print BORROWER'S name (first, middle, last)

Street address

City, state, and ZIP code

Account number (optional)

1 Date of lender's acquisition or knowledge of abandonment

2 Amount of debt outstanding

3 Amount of debt satisfied

4 Fair market value of property at acquisition or abandonment

5 Is borrower personally liable for repayment of the debt? ☐ Yes ☐ No

6 Description of property

Copy A For Internal Revenue Service Center

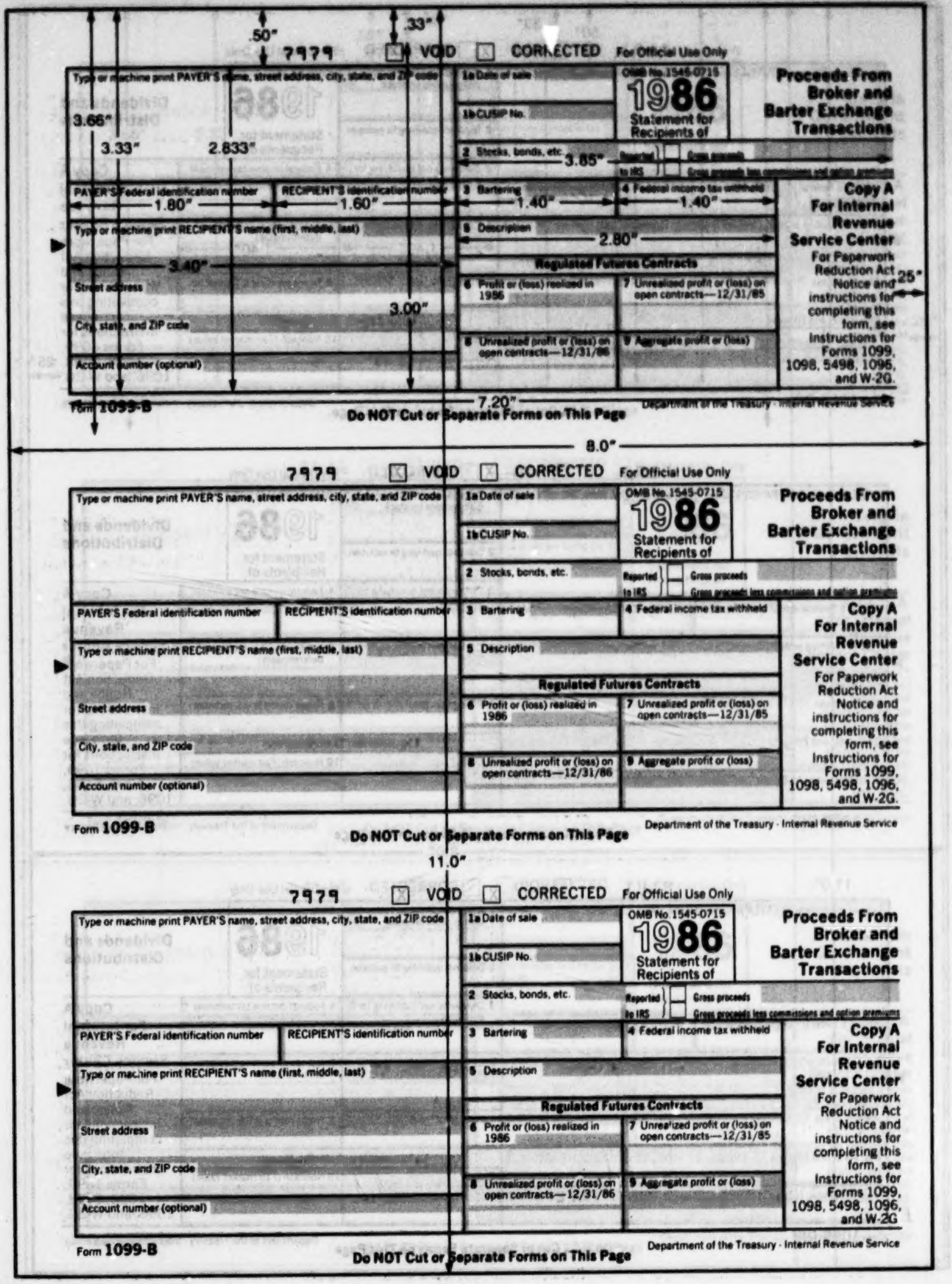
For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **1099-A**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

Exhibit D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7979 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

1a Date of sale

1b CUSIP No.

OMB No. 1545-0715

1986

Statement for Recipients of

Proceeds From Broker and Barter Exchange Transactions

2 Stocks, bonds, etc. Reported to IRS ☐ Gross proceeds ☐ Gross proceeds less commissions and option premiums

PAYER'S Federal identification number

RECIPIENT'S identification number

3 Bartering

4 Federal income tax withheld

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Type or machine print RECIPIENT'S name (first, middle, last)

5 Description

Street address

Regulated Futures Contracts

6 Profit or (loss) realized in 1986

7 Unrealized profit or (loss) on open contracts—12/31/85

City, state, and ZIP code

8 Unrealized profit or (loss) on open contracts—12/31/86

9 Aggregate profit or (loss)

Account number (optional)

Form 1099-B

Department of the Treasury - Internal Revenue Service

Do NOT Cut or Separate Forms on This Page

7979 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

1a Date of sale

1b CUSIP No.

OMB No. 1545-0715

1986

Statement for Recipients of

Proceeds From Broker and Barter Exchange Transactions

2 Stocks, bonds, etc. Reported to IRS ☐ Gross proceeds ☐ Gross proceeds less commissions and option premiums

PAYER'S Federal identification number

RECIPIENT'S identification number

3 Bartering

4 Federal income tax withheld

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Type or machine print RECIPIENT'S name (first, middle, last)

5 Description

Street address

Regulated Futures Contracts

6 Profit or (loss) realized in 1986

7 Unrealized profit or (loss) on open contracts—12/31/85

City, state, and ZIP code

8 Unrealized profit or (loss) on open contracts—12/31/86

9 Aggregate profit or (loss)

Account number (optional)

Form 1099-B

Department of the Treasury - Internal Revenue Service

Do NOT Cut or Separate Forms on This Page

7979 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

1a Date of sale

1b CUSIP No.

OMB No. 1545-0715

1986

Statement for Recipients of

Proceeds From Broker and Barter Exchange Transactions

2 Stocks, bonds, etc. Reported to IRS ☐ Gross proceeds ☐ Gross proceeds less commissions and option premiums

PAYER'S Federal identification number

RECIPIENT'S identification number

3 Bartering

4 Federal income tax withheld

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Type or machine print RECIPIENT'S name (first, middle, last)

5 Description

Street address

Regulated Futures Contracts

6 Profit or (loss) realized in 1986

7 Unrealized profit or (loss) on open contracts—12/31/85

City, state, and ZIP code

8 Unrealized profit or (loss) on open contracts—12/31/86

9 Aggregate profit or (loss)

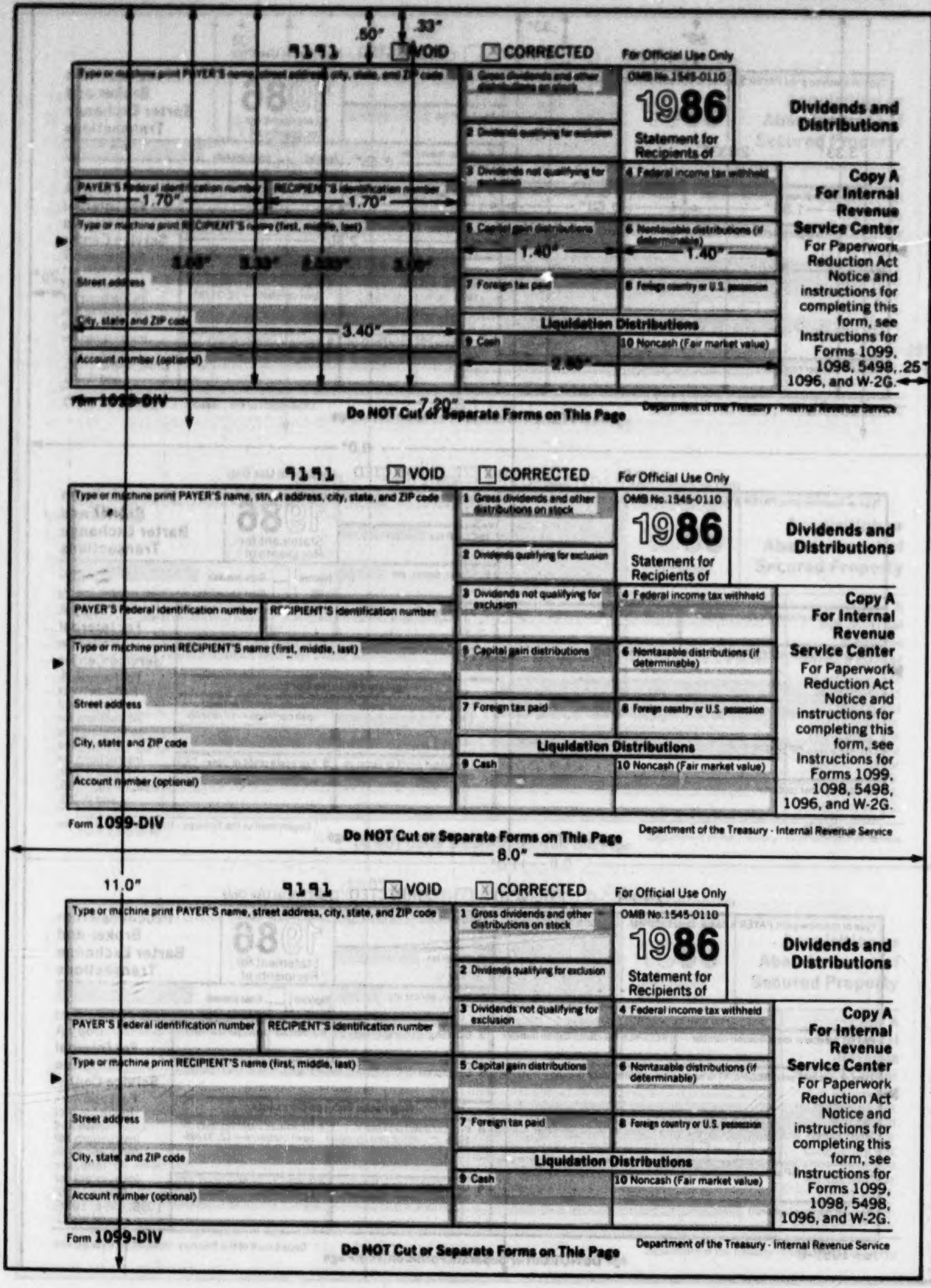
Account number (optional)

Form 1099-B

Department of the Treasury - Internal Revenue Service

Do NOT Cut or Separate Forms on This Page

Exhibit E



9191 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code	1 Gross dividends and other distributions on stock	OMB No. 1545-0110 1986 Statement for Recipients of	Dividends and Distributions
	2 Dividends qualifying for exclusion		
PAYER'S Federal identification number / RECIPIENT'S identification number	3 Dividends not qualifying for exclusion	4 Federal income tax withheld	Copy A For Internal Revenue Service Center For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Type or machine print RECIPIENT'S name (first, middle, last)	5 Capital gain distributions	6 Nontaxable distributions (if determinable)	
Street address	7 Foreign tax paid	8 Foreign country or U.S. possession	
City, state, and ZIP code	Liquidation Distributions		
	9 Cash	10 Noncash (Fair market value)	
Account number (optional)			

Form 1099-DIV

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Department of the Treasury - Internal Revenue Service

9191 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code	1 Gross dividends and other distributions on stock	OMB No. 1545-0110 1986 Statement for Recipients of	Dividends and Distributions
	2 Dividends qualifying for exclusion		
PAYER'S Federal identification number / RECIPIENT'S identification number	3 Dividends not qualifying for exclusion	4 Federal income tax withheld	Copy A For Internal Revenue Service Center For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Type or machine print RECIPIENT'S name (first, middle, last)	5 Capital gain distributions	6 Nontaxable distributions (if determinable)	
Street address	7 Foreign tax paid	8 Foreign country or U.S. possession	
City, state, and ZIP code	Liquidation Distributions		
	9 Cash	10 Noncash (Fair market value)	
Account number (optional)			

Form 1099-DIV

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Department of the Treasury - Internal Revenue Service

9191 ☒ VOID ☒ CORRECTED For Official Use Only

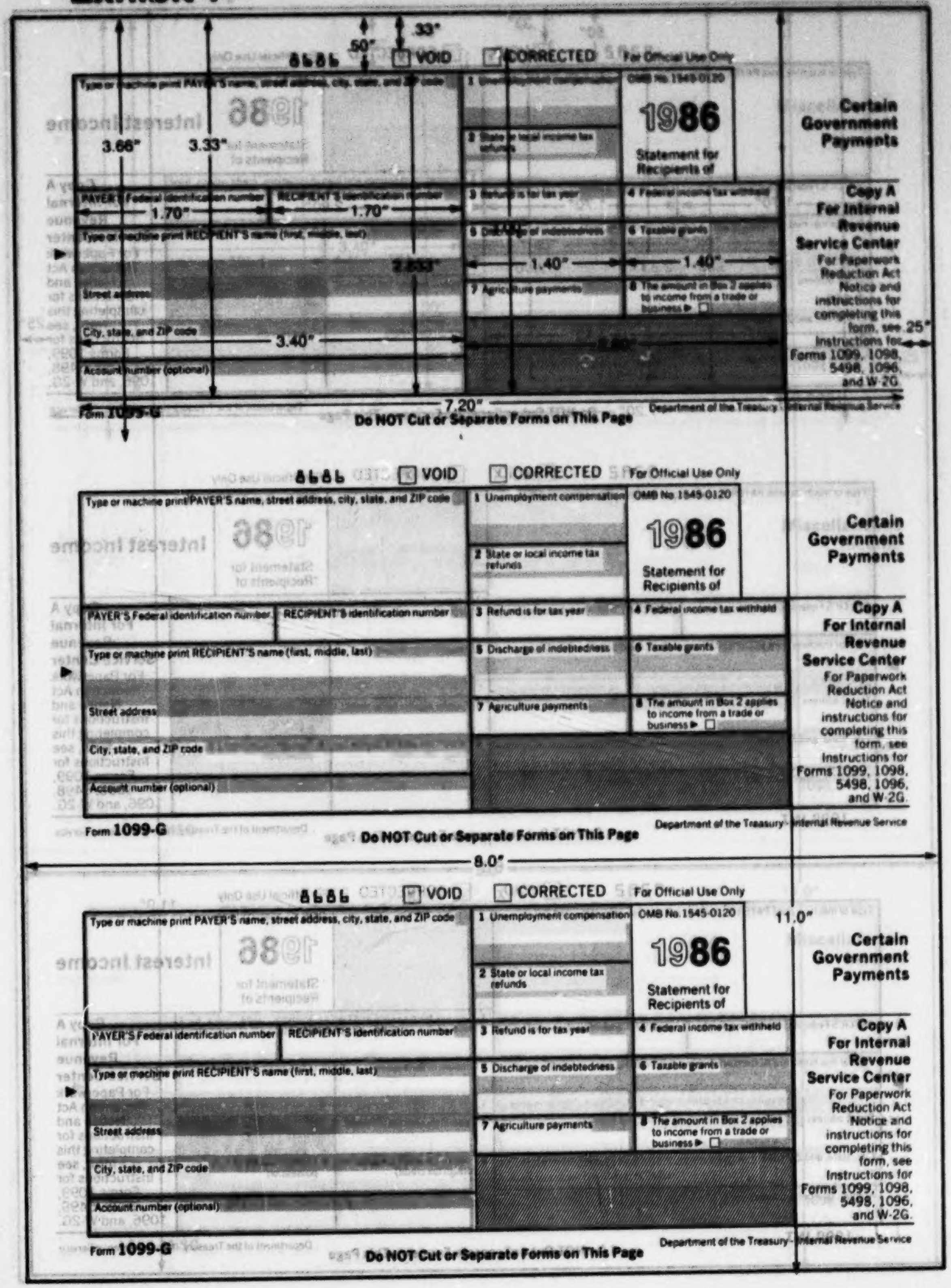
Type or machine print PAYER'S name, street address, city, state, and ZIP code	1 Gross dividends and other distributions on stock	OMB No. 1545-0110 1986 Statement for Recipients of	Dividends and Distributions
	2 Dividends qualifying for exclusion		
PAYER'S Federal identification number / RECIPIENT'S identification number	3 Dividends not qualifying for exclusion	4 Federal income tax withheld	Copy A For Internal Revenue Service Center For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Type or machine print RECIPIENT'S name (first, middle, last)	5 Capital gain distributions	6 Nontaxable distributions (if determinable)	
Street address	7 Foreign tax paid	8 Foreign country or U.S. possession	
City, state, and ZIP code	Liquidation Distributions		
	9 Cash	10 Noncash (Fair market value)	
Account number (optional)			

Form 1099-DIV

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

Exhibit F



8686 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code		1 Unemployment compensation 2 State or local income tax refunds	OMB No. 1545-0120 1986 Statement for Recipients of
PAYER'S Federal identification number	RECIPIENT'S identification number	3 Refund is for tax year	4 Federal income tax withheld
Type or machine print RECIPIENT'S name (first, middle, last)		5 Discharge of indebtedness	6 Taxable grants
Street address		7 Agriculture payments	8 The amount in Box 2 applies to income from a trade or business ▶ ☐
City, state, and ZIP code			
Account number (optional)			

Certain Government Payments

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **1099-G**

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Department of the Treasury - Internal Revenue Service

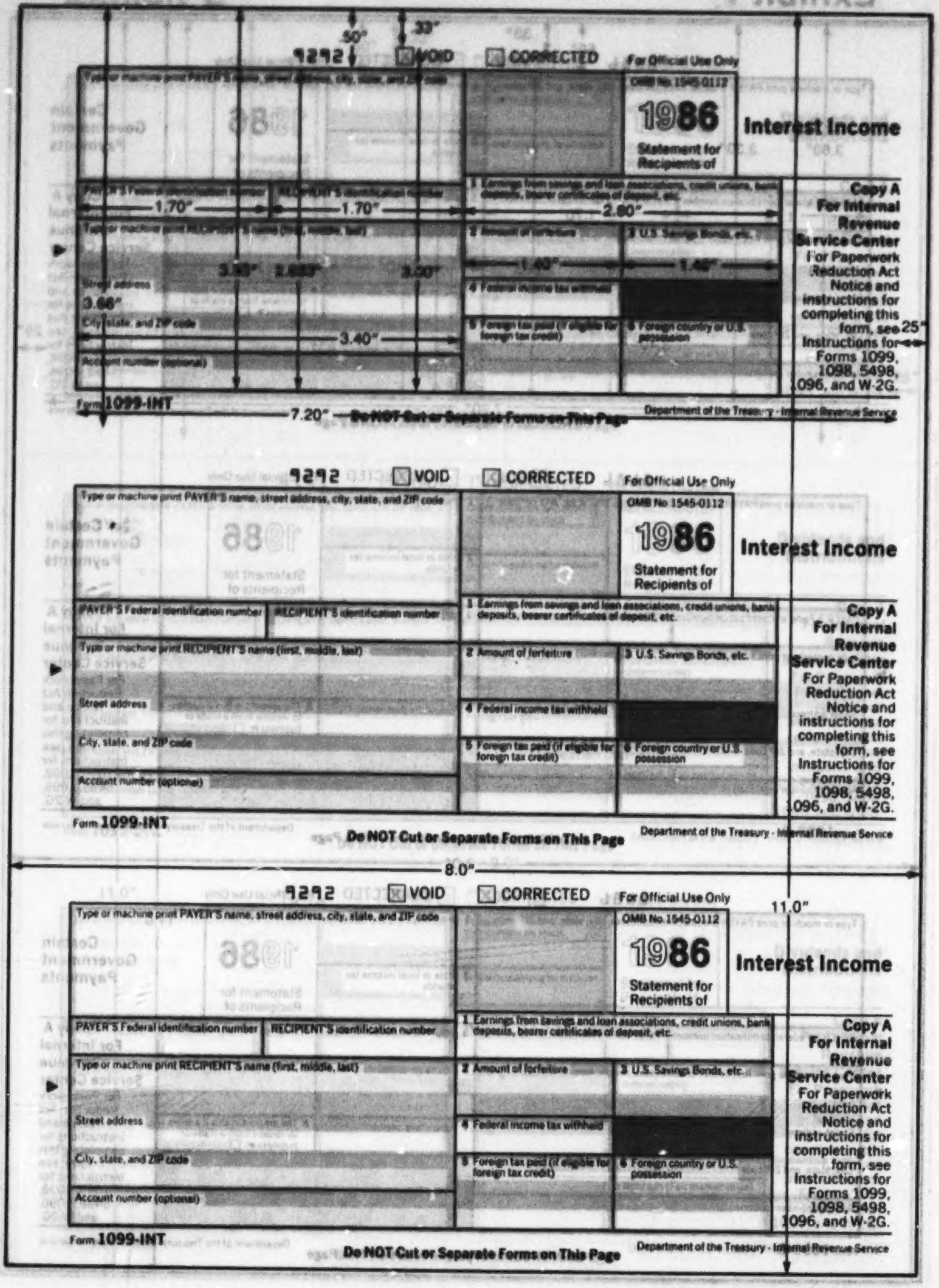
8686 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code
1 Unemployment compensation
OMB No. 1545-0120
1986
Statement for Recipients of
Certain Government Payments
2 State or local income tax refunds
PAYER'S Federal identification number
RECIPIENT'S identification number
3 Refund is for tax year
4 Federal income tax withheld
Copy A For Internal Revenue Service Center
Type or machine print RECIPIENT'S name (first, middle, last)
5 Discharge of indebtedness
6 Taxable grants
For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Street address
7 Agriculture payments
8 The amount in Box 2 applies to income from a trade or business ▶ ☐
City, state, and ZIP code
Account number (optional)
Form 1099-G
Do NOT Cut or Separate Forms on This Page
Department of the Treasury - Internal Revenue Service

8686 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code
1 Unemployment compensation
OMB No. 1545-0120
1986
Statement for Recipients of
Certain Government Payments
2 State or local income tax refunds
PAYER'S Federal identification number
RECIPIENT'S identification number
3 Refund is for tax year
4 Federal income tax withheld
Copy A For Internal Revenue Service Center
Type or machine print RECIPIENT'S name (first, middle, last)
5 Discharge of indebtedness
6 Taxable grants
For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Street address
7 Agriculture payments
8 The amount in Box 2 applies to income from a trade or business ▶ ☐
City, state, and ZIP code
Account number (optional)
Form 1099-G
Do NOT Cut or Separate Forms on This Page
Department of the Treasury - Internal Revenue Service

Exhibit G



9292 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

OMB No. 1545-0112

1986

Statement for Recipients of

Interest Income

PAYER'S Federal identification number	RECIPIENT'S identification number	1 Earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposit, etc.
Type or machine print RECIPIENT'S name (first, middle, last)	2 Amount of forfeiture	3 U.S. Savings Bonds, etc.
Street address	4 Federal income tax withheld	
City, state, and ZIP code	5 Foreign tax paid (if eligible for foreign tax credit)	6 Foreign country or U.S. possession
Account number (optional)		

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **1099-INT**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

9292 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

OMB No. 1545-0112

1986

Statement for Recipients of

Interest Income

PAYER'S Federal identification number | RECIPIENT'S identification number | 1 Earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposit, etc.

Type or machine print RECIPIENT'S name (first, middle, last) | 2 Amount of forfeiture | 3 U.S. Savings Bonds, etc.

Street address | 4 Federal income tax withheld

City, state, and ZIP code | 5 Foreign tax paid (if eligible for foreign tax credit) | 6 Foreign country or U.S. possession

Account number (optional)

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form 1099-INT

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

9292 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

OMB No. 1545-0112

1986

Statement for Recipients of

Interest Income

PAYER'S Federal identification number | RECIPIENT'S identification number | 1 Earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposit, etc.

Type or machine print RECIPIENT'S name (first, middle, last) | 2 Amount of forfeiture | 3 U.S. Savings Bonds, etc.

Street address | 4 Federal income tax withheld

City, state, and ZIP code | 5 Foreign tax paid (if eligible for foreign tax credit) | 6 Foreign country or U.S. possession

Account number (optional)

Copy A For Internal Revenue Service Center

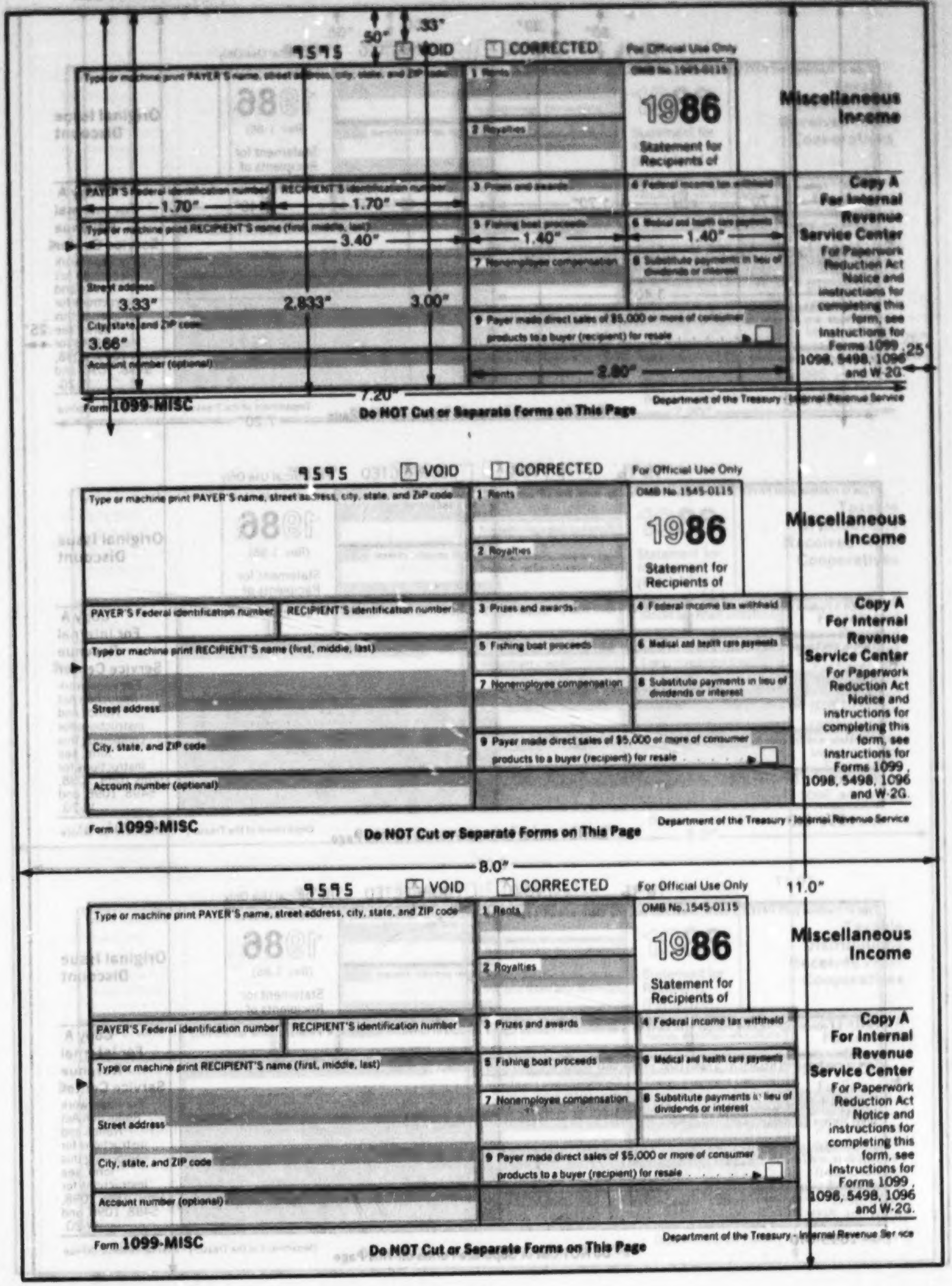
For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form 1099-INT

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

Exhibit H



9595 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code	1 Rents 2 Royalties	OMB No. 1545-0115 1986 Statement for Recipients of	**Miscellaneous Income**
PAYER'S Federal identification number / RECIPIENT'S identification number	3 Prizes and awards	4 Federal income tax withheld	**Copy A For Internal Revenue Service Center** For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096 and W-2G.
Type or machine print RECIPIENT'S name (first, middle, last)	5 Fishing boat proceeds	6 Medical and health care payments	
Street address	7 Nonemployee compensation	8 Substitute payments in lieu of dividends or interest	
City, state, and ZIP code	9 Payer made direct sales of $5,000 or more of consumer products to a buyer (recipient) for resale ▶ ☐		
Account number (optional)			

Form **1099-MISC** **Do NOT Cut or Separate Forms on This Page** Department of the Treasury - Internal Revenue Service

9595 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code	1 Rents 2 Royalties	OMB No. 1545-0115 1986 Statement for Recipients of	**Miscellaneous Income**
PAYER'S Federal identification number / RECIPIENT'S identification number	3 Prizes and awards	4 Federal income tax withheld	**Copy A For Internal Revenue Service Center** For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096 and W-2G.
Type or machine print RECIPIENT'S name (first, middle, last)	5 Fishing boat proceeds	6 Medical and health care payments	
Street address	7 Nonemployee compensation	8 Substitute payments in lieu of dividends or interest	
City, state, and ZIP code	9 Payer made direct sales of $5,000 or more of consumer products to a buyer (recipient) for resale ▶ ☐		
Account number (optional)			

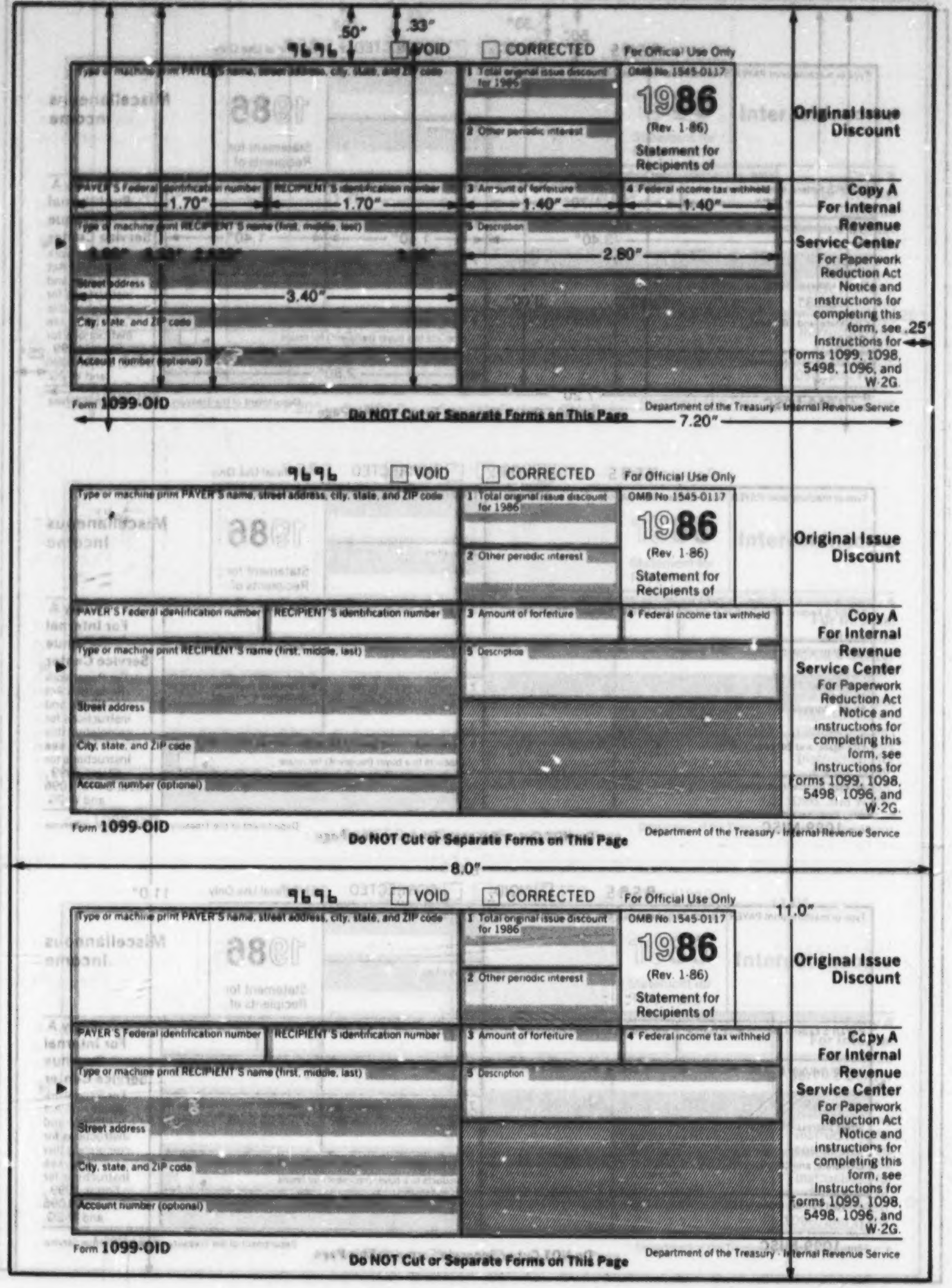
Form **1099-MISC** **Do NOT Cut or Separate Forms on This Page** Department of the Treasury - Internal Revenue Service

9595 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code	1 Rents 2 Royalties	OMB No. 1545-0115 1986 Statement for Recipients of	**Miscellaneous Income**
PAYER'S Federal identification number / RECIPIENT'S identification number	3 Prizes and awards	4 Federal income tax withheld	**Copy A For Internal Revenue Service Center** For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096 and W-2G.
Type or machine print RECIPIENT'S name (first, middle, last)	5 Fishing boat proceeds	6 Medical and health care payments	
Street address	7 Nonemployee compensation	8 Substitute payments in lieu of dividends or interest	
City, state, and ZIP code	9 Payer made direct sales of $5,000 or more of consumer products to a buyer (recipient) for resale ▶ ☐		
Account number (optional)			

Form **1099-MISC** **Do NOT Cut or Separate Forms on This Page** Department of the Treasury - Internal Revenue Service

Exhibit I



9696 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code	1 Total original issue discount for 1986 2 Other periodic interest	OMB No. 1545-0117 **1986** (Rev. 1-86) Statement for Recipients of	**Original Issue Discount**
PAYER'S Federal identification number	RECIPIENT'S identification number	3 Amount of forfeiture	4 Federal income tax withheld
Type or machine print RECIPIENT'S name (first, middle, last) Street address City, state, and ZIP code Account number (optional)	5 Description		**Copy A For Internal Revenue Service Center** For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **1099-OID** Department of the Treasury - Internal Revenue Service

Do NOT Cut or Separate Forms on This Page

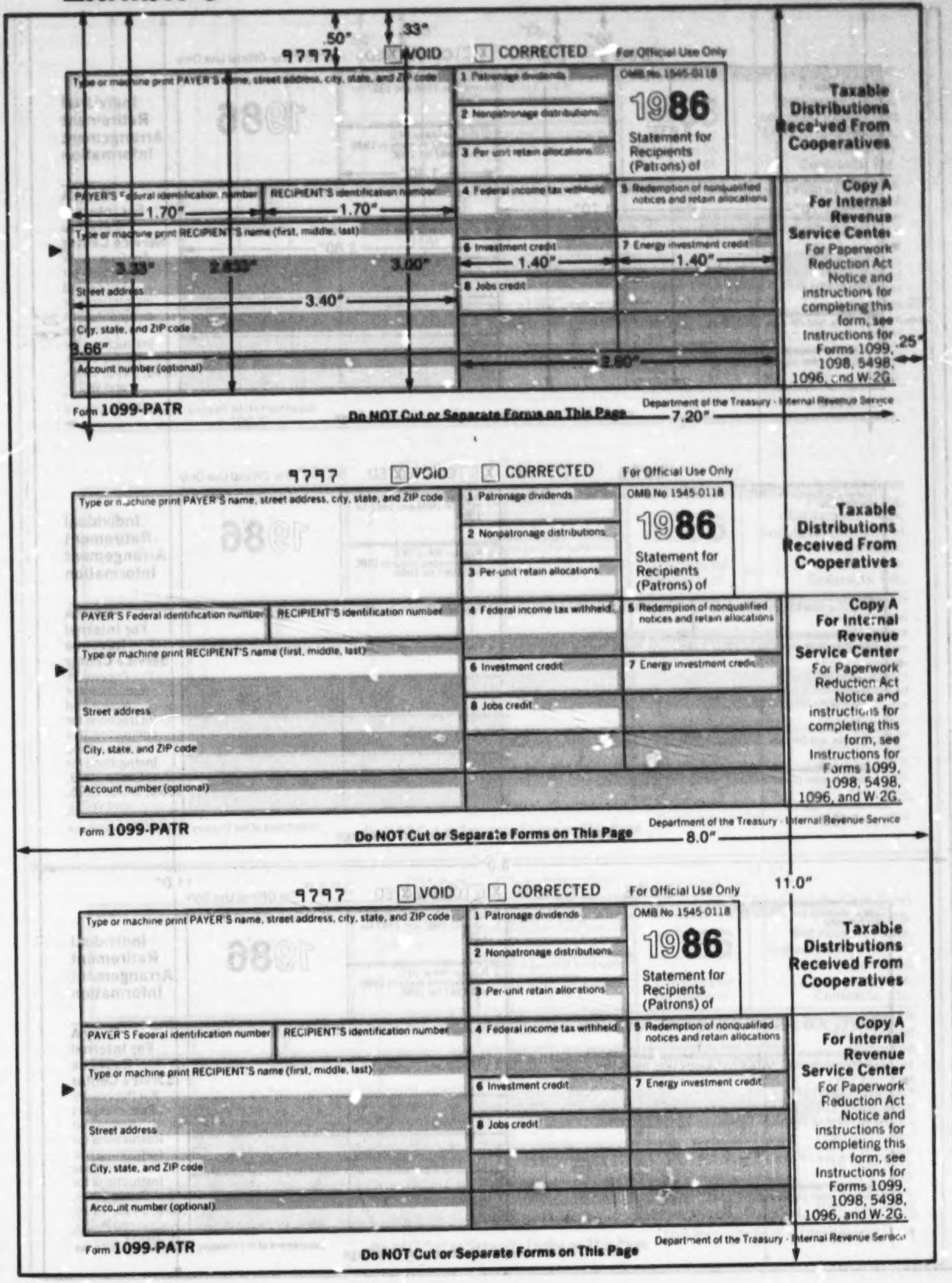
9696 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code
1 Total original issue discount for 1986
2 Other periodic interest
OMB No. 1545-0117
1986 (Rev. 1-86)
Statement for Recipients of
Original Issue Discount
PAYER'S Federal identification number
RECIPIENT'S identification number
3 Amount of forfeiture
4 Federal income tax withheld
Copy A For Internal Revenue Service Center
Type or machine print RECIPIENT'S name (first, middle, last)
5 Description
Street address
City, state, and ZIP code
Account number (optional)
For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Form 1099-OID Department of the Treasury - Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

9696 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code
1 Total original issue discount for 1986
2 Other periodic interest
OMB No. 1545-0117
1986 (Rev. 1-86)
Statement for Recipients of
Original Issue Discount
PAYER'S Federal identification number
RECIPIENT'S identification number
3 Amount of forfeiture
4 Federal income tax withheld
Copy A For Internal Revenue Service Center
Type or machine print RECIPIENT'S name (first, middle, last)
5 Description
Street address
City, state, and ZIP code
Account number (optional)
For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Form 1099-OID Department of the Treasury - Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

Exhibit J



9797 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

1 Patronage dividends

2 Nonpatronage distributions

3 Per-unit retain allocations

OMB No 1545-0118

1986

Statement for Recipients (Patrons) of

Taxable Distributions Received From Cooperatives

PAYER'S Federal identification number

RECIPIENT'S identification number

4 Federal income tax withheld

5 Redemption of nonqualified notices and retain allocations

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Type or machine print RECIPIENT'S name (first, middle, last)

6 Investment credit

7 Energy investment credit

Street address

8 Jobs credit

City, state, and ZIP code

Account number (optional)

Form **1099-PATR**

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Department of the Treasury - Internal Revenue Service

9797 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

1 Patronage dividends

2 Nonpatronage distributions

3 Per-unit retain allocations

OMB No 1545-0118

1986

Statement for Recipients (Patrons) of

Taxable Distributions Received From Cooperatives

PAYER'S Federal identification number

RECIPIENT'S identification number

4 Federal income tax withheld

5 Redemption of nonqualified notices and retain allocations

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Type or machine print RECIPIENT'S name (first, middle, last)

6 Investment credit

7 Energy investment credit

Street address

8 Jobs credit

City, state, and ZIP code

Account number (optional)

Form **1099-PATR**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

9797 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

1 Patronage dividends

2 Nonpatronage distributions

3 Per-unit retain allocations

OMB No 1545-0118

1986

Statement for Recipients (Patrons) of

Taxable Distributions Received From Cooperatives

PAYER'S Federal identification number

RECIPIENT'S identification number

4 Federal income tax withheld

5 Redemption of nonqualified notices and retain allocations

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Type or machine print RECIPIENT'S name (first, middle, last)

6 Investment credit

7 Energy investment credit

Street address

8 Jobs credit

City, state, and ZIP code

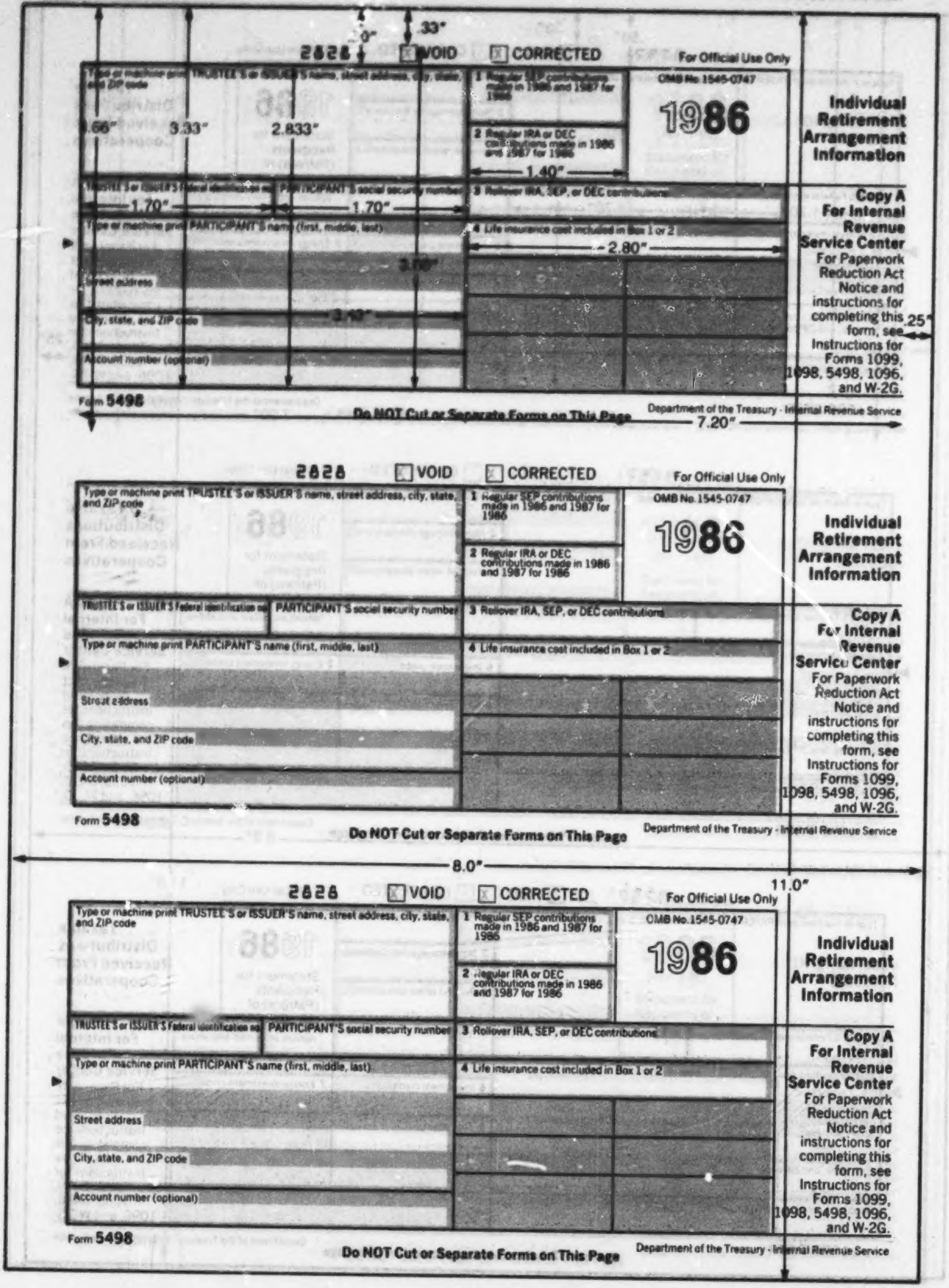
Account number (optional)

Form **1099-PATR**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

Exhibit K



2828 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print TRUSTEE'S or ISSUER'S name, street address, city, state, and ZIP code

1 Regular SEP contributions made in 1986 and 1987 for 1986

2 Regular IRA or DEC contributions made in 1986 and 1987 for 1986

OMB No. 1545-0747

1986

Individual Retirement Arrangement Information

TRUSTEE'S or ISSUER'S Federal identification no.

PARTICIPANT'S social security number

3 Rollover IRA, SEP, or DEC contributions

Type or machine print PARTICIPANT'S name (first, middle, last)

4 Life insurance cost included in Box 1 or 2

Street address

City, state, and ZIP code

Account number (optional)

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **5498**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

2828 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print TRUSTEE'S or ISSUER'S name, street address, city, state, and ZIP code

1 Regular SEP contributions made in 1986 and 1987 for 1986

2 Regular IRA or DEC contributions made in 1986 and 1987 for 1986

OMB No. 1545-0747

1986

Individual Retirement Arrangement Information

TRUSTEE'S or ISSUER'S Federal identification no.

PARTICIPANT'S social security number

3 Rollover IRA, SEP, or DEC contributions

Type or machine print PARTICIPANT'S name (first, middle, last)

4 Life insurance cost included in Box 1 or 2

Street address

City, state, and ZIP code

Account number (optional)

Copy A For Internal Revenue Service Center

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **5498**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

2828 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print TRUSTEE'S or ISSUER'S name, street address, city, state, and ZIP code

1 Regular SEP contributions made in 1986 and 1987 for 1986

2 Regular IRA or DEC contributions made in 1986 and 1987 for 1986

OMB No. 1545-0747

1986

Individual Retirement Arrangement Information

TRUSTEE'S or ISSUER'S Federal identification no.

PARTICIPANT'S social security number

3 Rollover IRA, SEP, or DEC contributions

Type or machine print PARTICIPANT'S name (first, middle, last)

4 Life insurance cost included in Box 1 or 2

Street address

City, state, and ZIP code

Account number (optional)

Copy A For Internal Revenue Service Center

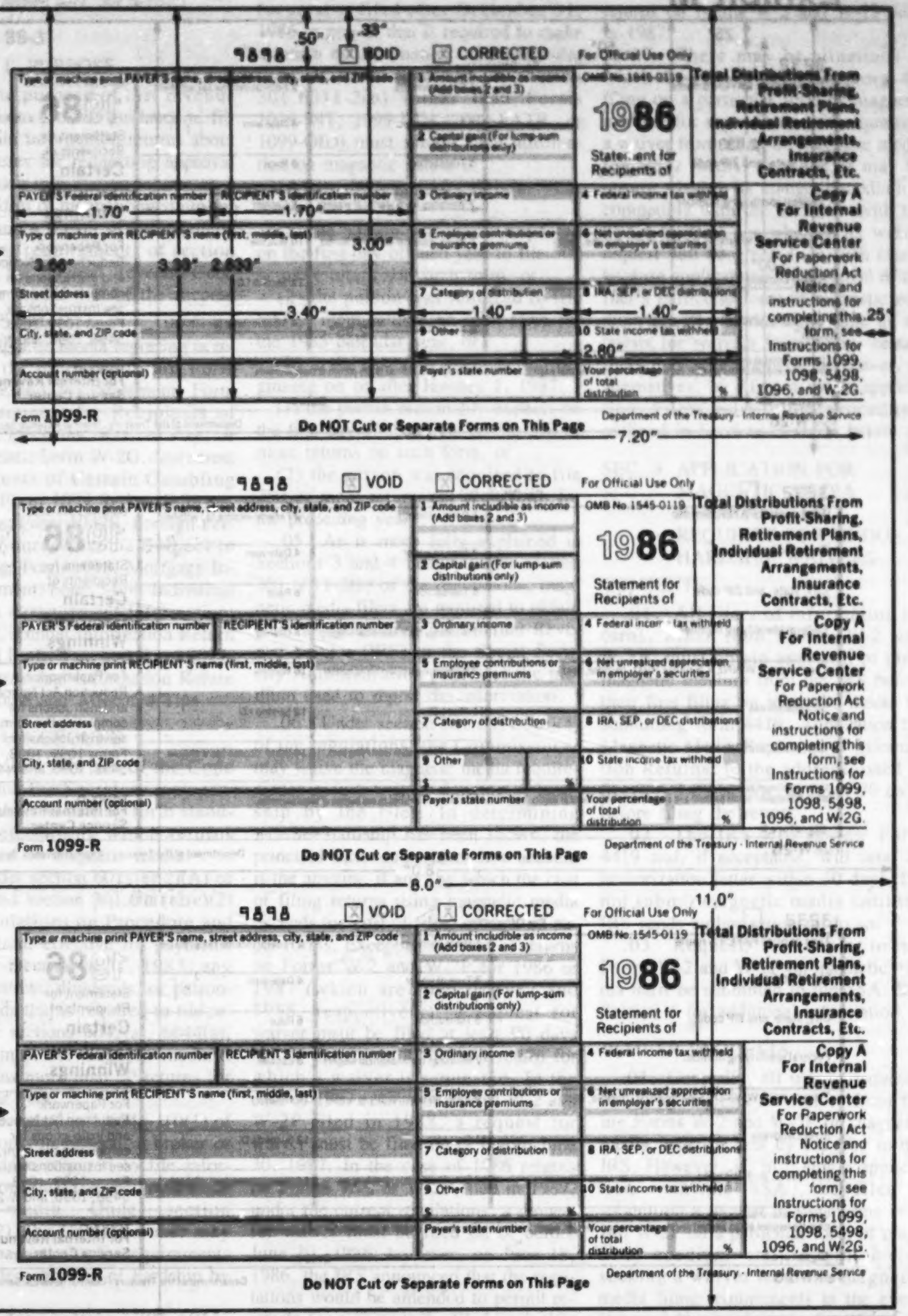
For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **5498**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

Exhibit L


.50"
.33"
1.70"
1.70"
3.00"
3.66"
3.33"
2.833"
3.40"
1.40"
1.40"
.25"
2.80"
7.20"
8.0"
11.0"

9898 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code		1 Amount includible as income (Add boxes 2 and 3) 2 Capital gain (For lump-sum distributions only)	OMB No. 1545-0119 **1986** Statement for Recipients of	**Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc.**
PAYER'S Federal identification number	RECIPIENT'S identification number	3 Ordinary income	4 Federal income tax withheld	**Copy A For Internal Revenue Service Center** For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Type or machine print RECIPIENT'S name (first, middle, last)		5 Employee contributions or insurance premiums	6 Net unrealized appreciation in employer's securities	
Street address		7 Category of distribution	8 IRA, SEP, or DEC distributions	
City, state, and ZIP code		9 Other $ %	10 State income tax withheld	
Account number (optional)		Payer's state number	Your percentage of total distribution %	

Form **1099-R** Department of the Treasury · Internal Revenue Service

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9898 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code | 1 Amount includible as income (Add boxes 2 and 3) | 2 Capital gain (For lump-sum distributions only) | OMB No. 1545-0119 | 1986 | Statement for Recipients of | Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc.
PAYER'S Federal identification number | RECIPIENT'S identification number | 3 Ordinary income | 4 Federal income tax withheld | Copy A For Internal Revenue Service Center For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Type or machine print RECIPIENT'S name (first, middle, last) | 5 Employee contributions or insurance premiums | 6 Net unrealized appreciation in employer's securities
Street address | 7 Category of distribution | 8 IRA, SEP, or DEC distributions
City, state, and ZIP code | 9 Other $ % | 10 State income tax withheld
Account number (optional) | Payer's state number | Your percentage of total distribution %
Form 1099-R Department of the Treasury · Internal Revenue Service
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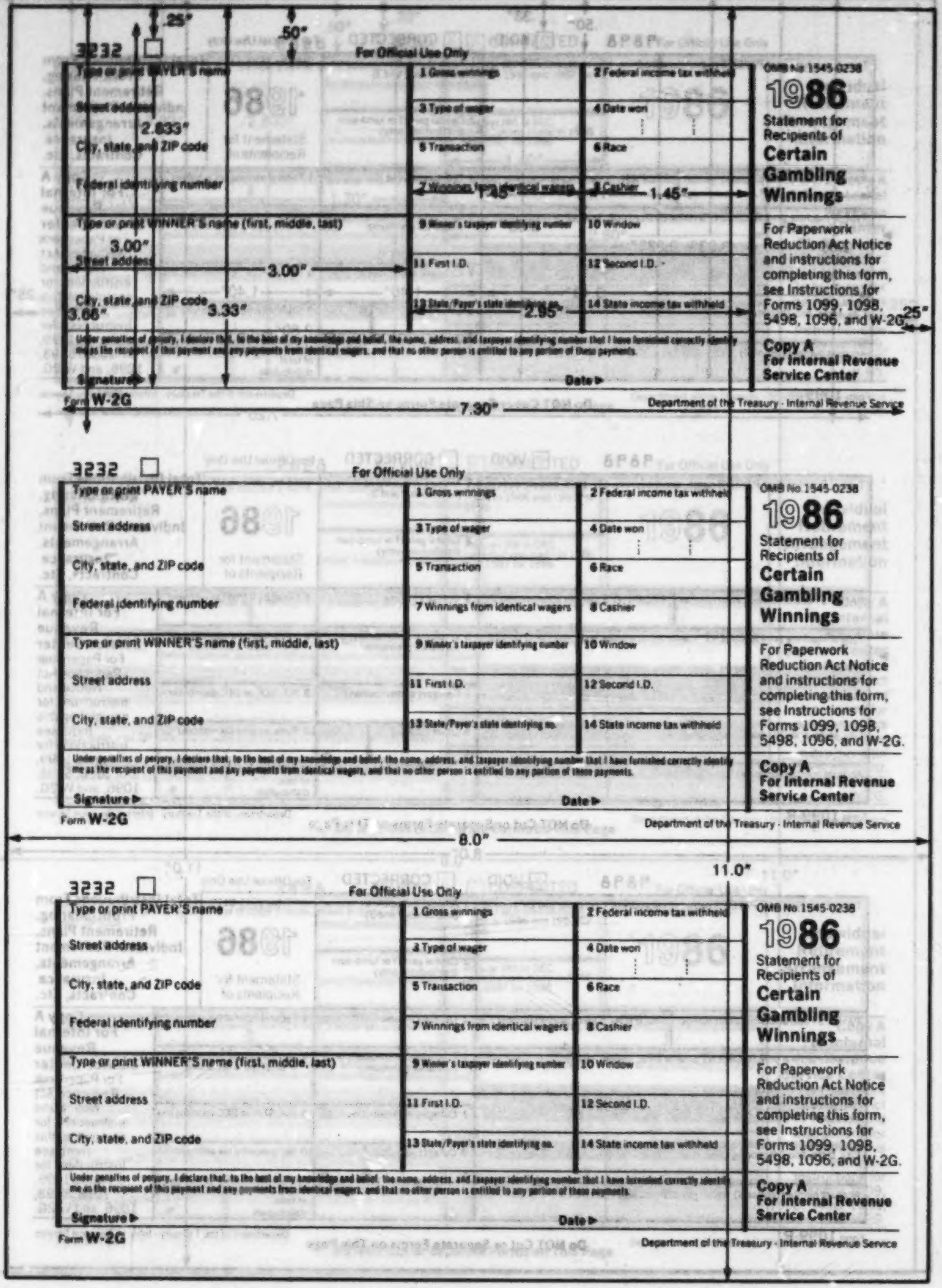
9898 ☒ VOID ☒ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code | 1 Amount includible as income (Add boxes 2 and 3) | 2 Capital gain (For lump-sum distributions only) | OMB No. 1545-0119 | 1986 | Statement for Recipients of | Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc.
PAYER'S Federal identification number | RECIPIENT'S identification number | 3 Ordinary income | 4 Federal income tax withheld | Copy A For Internal Revenue Service Center For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.
Type or machine print RECIPIENT'S name (first, middle, last) | 5 Employee contributions or insurance premiums | 6 Net unrealized appreciation in employer's securities
Street address | 7 Category of distribution | 8 IRA, SEP, or DEC distributions
City, state, and ZIP code | 9 Other $ % | 10 State income tax withheld
Account number (optional) | Payer's state number | Your percentage of total distribution %
Form 1099-R Department of the Treasury · Internal Revenue Service
Do NOT Cut or Separate Forms on This Page

Exhibit M



3232 ☐

For Official Use Only

Type or print PAYER'S name

Street address

City, state, and ZIP code

Federal identifying number

Type or print WINNER'S name (first, middle, last)

Street address

City, state, and ZIP code

1 Gross winnings	2 Federal income tax withheld
3 Type of wager	4 Date won
5 Transaction	6 Race
7 Winnings from identical wagers	8 Cashier
9 Winner's taxpayer identifying number	10 Window
11 First I.D.	12 Second I.D.
13 State/Payer's state identifying no.	14 State income tax withheld

OMB No. 1545-0238

1986

Statement for Recipients of Certain Gambling Winnings

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Copy A For Internal Revenue Service Center

Under penalties of perjury, I declare that, to the best of my knowledge and belief, the name, address, and taxpayer identifying number that I have furnished correctly identify me as the recipient of this payment and any payments from identical wagers, and that no other person is entitled to any portion of these payments.

Signature ▶ Date ▶

Form W-2G Department of the Treasury - Internal Revenue Service

3232 ☐

For Official Use Only

Type or print PAYER'S name

Street address

City, state, and ZIP code

Federal identifying number

Type or print WINNER'S name (first, middle, last)

Street address

City, state, and ZIP code

1 Gross winnings | 2 Federal income tax withheld
3 Type of wager | 4 Date won
5 Transaction | 6 Race
7 Winnings from identical wagers | 8 Cashier
9 Winner's taxpayer identifying number | 10 Window
11 First I.D. | 12 Second I.D.
13 State/Payer's state identifying no. | 14 State income tax withheld

OMB No. 1545-0238

1986

Statement for Recipients of Certain Gambling Winnings

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Copy A For Internal Revenue Service Center

Under penalties of perjury, I declare that, to the best of my knowledge and belief, the name, address, and taxpayer identifying number that I have furnished correctly identify me as the recipient of this payment and any payments from identical wagers, and that no other person is entitled to any portion of these payments.

Signature ▶ Date ▶

Form W-2G Department of the Treasury - Internal Revenue Service

3232 ☐

For Official Use Only

Type or print PAYER'S name

Street address

City, state, and ZIP code

Federal identifying number

Type or print WINNER'S name (first, middle, last)

Street address

City, state, and ZIP code

1 Gross winnings | 2 Federal income tax withheld
3 Type of wager | 4 Date won
5 Transaction | 6 Race
7 Winnings from identical wagers | 8 Cashier
9 Winner's taxpayer identifying number | 10 Window
11 First I.D. | 12 Second I.D.
13 State/Payer's state identifying no. | 14 State income tax withheld

OMB No. 1545-0238

1986

Statement for Recipients of Certain Gambling Winnings

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Copy A For Internal Revenue Service Center

Under penalties of perjury, I declare that, to the best of my knowledge and belief, the name, address, and taxpayer identifying number that I have furnished correctly identify me as the recipient of this payment and any payments from identical wagers, and that no other person is entitled to any portion of these payments.

Signature ▶ Date ▶

Form W-2G Department of the Treasury - Internal Revenue Service

26 CFR 601.602: Tax forms and instructions.
(Also Part I, Section 6011, 301.6011-2.)

Rev. Proc. 86-31

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to provide guidance to filers of certain information returns about the procedures for requesting approval for filing such information returns on a particular form of magnetic medium, or for requesting a waiver of the magnetic media filing requirements of section 6011(e) of the Internal Revenue Code and section 1.6045-1(l) of the Income Tax Regulations.

.02 Magnetic media reporting is required for the following forms: Form W-2, Wage and Tax Statement; Form W-2P, Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments; Form W-2G, Statement for Recipients of Certain Gambling Winnings; Form 1099 Series, Information Returns; Form 1042S, Foreign Person's US Source Income Subject to Withholding; Form 1098, Mortgage Interest Statement; Form 5498, Individual Retirement Arrangement Information; Form 6248, Annual Information Return of Windfall Profit Tax; and Form 8027, Employer's Annual Information Return on Tip Income and Allocated Tips.

SEC. 2. BACKGROUND

.01 Section 6011(e) of the Code provides that the Secretary may prescribe regulations setting forth standards for determining which returns must be filed on magnetic media.

.02 Under section 6011(e)(2)(A) of the Code and section 301.6011-2(c)(2) of the Regulations on Procedure and Administration, effective for payments made after December 31, 1983, any payor of interest, dividends, or patronage dividends that is required to file returns under sections 6042(a), 6044(a), or 6049(a) must use magnetic media if the payor has more than 50 returns for any calendar year.

.03 Under section 1.6045-1(l)(1) of the regulations, in general, a broker or barter exchange required to file information returns must file such returns on magnetic media. Under section 1.6045(l)(2), the Commissioner may waive the magnetic media requirements upon a written showing of hardship by the filer.

.04 Under section 301.6011-2(c)(1)(i) of the regulations, effective for returns filed after December 31, 1986, a person that is required to make a return of information on a particular type of form specified in section 301.6011-2(b) (other than Forms 1099-INT, 1099-DIV, 1099-PATR, or 1099-OID) must submit such information on magnetic media if:

(A) in the case of calendar year 1986,

(1) the person reasonably expected on the first day of such year to file 500 or more return son such form, or

(2) the person was required to file 500 or more returns on such form for the 1985 calendar year, or

(B) in the case of a calendar year beginning on or after January 1, 1987,

(1) the person reasonably expects on the first day of such year to file 250 or more returns on such form, or

(2) the person was required to file 250 or more returns on such form for the preceding year.

.05 As is more fully explained in Sections 3 and 4 below, under section 301.6011-2(b) of the regulations, magnetic media filers are required to obtain prior approval from the Internal Revenue Service (IRS) or the Social Security Administration (SSA) of the medium used to report the information.

.06 Under section 301.6011-2(c)(4) of the regulations, the Commissioner may waive the magnetic media requirements upon a written showing of hardship by the filer. In determining whether hardship has been shown, the principal factor to be taken into account is the amount, if any, by which the cost of filing returns using magnetic media exceeds the cost of filing returns on paper forms. Except in the case of returns on Forms W-2 and W-2P for 1986 or 1987 (which are filed in 1987 and 1988, respectively), a request for waiver msut be filed at least 90 days before the filing of the first return for which a waiver is requested. In the case of 1987 returns on Forms W-2 and W-2P filed in 1988, a request for waiver must be filed on or before June 30, 1987. In the case of 1986 returns on Forms W-2 or W-2P filed in 1987, under the current regulations, a request for waiver must be filed on or before June 30, 1986; however, on June 18, 1986, the IRS announced that the regulations would be amended to permit requests for waiver to be filed on or before July 31, 1986, in the case of 1986 returns on Forms W-2 and W-2P filed in 1987.

.07 There may be situations in which the filer is seeking approval for filing on a particular form of magnetic medium for some forms and requesting a waiver from filing on magnetic media for other forms, or the filer may be unsure whether its mangetic medium is compatible with the IRS's or with the SSA's systems, or whether its waiver request will be granted. In such cases, because applications for approval of the filer's particular form of magnetic medium are due at the same time as requests for waivers from filing, certain filers may seek approval or waiver, as alternatives, by filing a single application. Filers must follow procedures outlined in Sections 3 and 4 below.

SEC. 3. APPLICATION FOR MAGENTIC MEDIA REPORTING AND REQUESTS FOR UNDUE HARDSHIP WAIVERS

CONSENTS

.01 All filers of information returns, *other than Forms W-2 and W-2P*, must obtain approval of their magnetic medium from the IRS before their first filing on magnetic media by submitting form 4419, Application for Magnetic Media Reporting of Information Returns, to the address listed in Section 3.05 below, at least 90 days before filing the return.

.02 The IRS will review Form 4419 and, if acceptable, will send an authorization letter within 30 days. Do not submit magnetic media until the IRS sends authorization to do so.

.03 Requests for consent to file Forms W-2 and W-2P on magnetic media *must* be submitted to the SSA. See Section 4 for additional information.

WAIVER REQUESTS

.04 Generally, all waiver requests, including requests for waiver from filing Forms W-2 and W-2P on magnetic media, *must* be sent by the filer to the IRS. However, if, in a single application with the SSA, the filer is submitting a request to file Forms W-2 and W-2P on a particular form of magnetic medium and, alternatively, seeking a waiver from the magnetic media filing requirements in the event approval is not granted, the SSA will forward the waiver request to the IRS. See Section 4 below.

.05 Effective January 1, 1986, magnetic media processing for all the IRS service centers was centralized at the national Computer Center. Forms 4419 and waiver requests should be directed to the following address:

Magnetic Media Reporting
Internal Revenue Service
National Computer Center
P.O. Box 1359
Martinsburg, WV 25401-1359

.06 Filers must submit a written statement requesting a waiver for a specific period, *not to exceed one year*. Waivers are granted on a case-by-case basis, and filers may not apply for a waiver for more than one year at a time. Separate waiver requests must be filed for each type of form. Form 8508, Request for Waiver From Filing Information Returns on Magnetic Media, may be used for this purpose. If it is not used, a written statement shoudl be filed containing the following information:

(a) The filer's name and address.

(b) The filer's taxpayer identification number.

(c) The tax year for which the waiver is requested.

(d) The name and telephone number of a person to contact who is familiar with the information contained in the waiver request.

(e) The form number for which the waiver is requested.

(f) The type and expected volume of each return for the tax year for which a waiver is requested and the number and type of returns to be filed on magnetic media, if any.

(g) If the filer does not currently have a magnetic media system, a cost analysis that shows the cost to convert from the filer's current paper system to a magnetic media system compatible with the IRS's or SSA's systems. Specify the type of magnetic medium considered, such as tape, cartridge, cassette, mini-disk or diskette, and

(1) a copy of a written cost estimate for magnetic media filing from two service bureaus, or

(2) written statements from at least two service bureaus indicating that they will not handle the volume of documents required by the filer.

(h) If the filer has a magnetic media system that is incompatible with the IRS's or SSA's system, or is currently in the process of installing a magnetic media system:

(1) a firm date by which the filer's system will be capable of providing a form of magnetic medium that is compatible, or

(2) a written commitment of a date from a service bureau that will convert the returns to magnetic media.

(i) In the case of Form W-2 filers, the number of permanent employees for whom Forms W-2 will be filed and the total number of employees, if different, for whom Forms W-2 will be filed.

.07 The waiver request must contain the following statement signed by a responsible person who is duly authorized to make and sign a return, statement, or other document:

> "Under penalties of perjury, I declare that I have examined this request, including accompanying documents, and to the best of my knowledge and belief the facts presented in support of this request are true, correct and complete."

.08 The IRS will notify the filer whether the request is granted or denied.

.09 With respect to returns filed on forms other than Forms W-2 and W-2P, if the filer is seeking, in a single application, approval for filing the returns on a particular form of magnetic medium and alternatively, a waiver from the magnetic media filing requirements if approval is not granted, Forms 4419 and 8508 (or a written request) should both be submitted to the IRS.

SEC. 4. PROCEDURES FOR CONSENTS/WAIVERS FOR WAGE AND PENSION INFORMATION

.01 Forms W-2 and W-2P *must* be filed with the SSA. The SSA will accept magnetic media filing for forms W-2 and W-2P and has issued the following Specification booklets: TIB-4a, "Magnetic Tape Reporting, Submitting FICA Wage and Tax Data to the Social Security Administration," TIB-4b, "Magnetic Tape Reporting, Submitting Annuity, Pension, Retired Pay or IRA Payment to the Social Security Administration," and TIB-4c, "Diskette Reporting, Submitting FICA Wage and Tax Data to the Social Security Administration." all filers must obtain approval of their magnetic medium before their first filing on magnetic media by submitting an SSA authorization request. The authorization request forms appear in TIBs-4a, 4b, and 4c. Copies of these publications are available from the SSA Regional Magnetic Media Coordinators. Filers must send authorization requests to:

Social Security Administration
P.O. Box 2317
Baltimore, MD 21203
Attn: Magnetic Media Group

.02 Upon receipt of the authorization request, the SSA will review the application and notify the filer in writing within 30 days whether its particular form of magnetic medium has been approved. In no event should a report be submitted before the SSA has approved the authorization.

.03 If the filer is seeking approval for filing on a particular form of magnetic medium and alternatively, requesting a waiver from the magnetic media filing requirements in a single application, Form 8508 (or a written waiver request) should be submitted with the authorization request. The SSA will forward the waiver request to the IRS for its consideration.

.04 A filer may submit form 8508 (or a written waiver request) directly to the IRS.

.05 Under the current regulations, the authorization request and/or the waiver request must be filed with the appropriate agency on or before June 30, 1986, in the case of 1986 Forms W-2 and W-2P to be filed in 1987; however, on June 18, 1986, the IRS announced that the regulations would be amended to permit authorization requests and/or waiver requests to be filed on or before July 31, 1986, in the case of 1986 returns on Forms W-2 and W-2P filed in 1987. The authorization request and/or the waiver request must be filed on or beofre June 30, 1987, in the case of the 1987 Forms W-2 and W-2P to be filed in 1988.

SEC. 5 APPLICABLE PENALTIES

If a filer fails to file on magnetic media when required to do so, and has not received a waiver from the filing requirements, the filer is subject to the penalties for failure to file a return under sections 6652 and 6693.

SEC. 6. EFFECTIVE DATE

This revenue procedure is effective June 18, 1986, for returns filed after December 31, 1986.

Form **4419**
(Rev. March 1986)

Department of the Treasury – Internal Revenue Service

Application for Magnetic Media Reporting of Information Returns

IRS Use Only

OMB No. 1545-0387
Expires: 7-31-88

1. Name and address of organization *(street, city, State and ZIP code)*

2. Person to contact about this request
Name:
Title:
Telephone number: *(include area code)*

3. Employer identification number

4. Tax year for which you are requesting authorization to file on magnetic media

5. **Documents To Be Reported** *(Check all that you wish to file on magnetic media)*

Form	Form	Form	Form
☐ W-2G	☐ 1099-B	☐ 1099-OID	☐ 8027
☐ W-4	☐ 1099-DIV	☐ 1099-PATR	☐
☐ 1042S	☐ 1099-G	☐ 1099-R	☐
☐ 1098	☐ 1099-INT	☐ 5498	☐
☐ 1099-A	☐ 1099-MISC	☐ 6248	☐

Do NOT file Forms W-2 or W-2P with IRS. Submit that information to the Social Security Administration.

6. **Kind of equipment on which media will be prepared**

Please check the type of media you plan to file and provide the requested information for that type of media.

Type of Media	Main Frame	Drive Unit	Recording Mode	Track	Software
☐ Magnetic Tape 1/2″ Only			☐ EBCDIC ☐ ASCII ☐ BCD	☐ 7 ☐ 9	
☐ 8″ Diskette			☐ EBCDIC Only		
☐ 5-1/4″ Diskette			☐ ASCII Only		
☐ Cassette	Burroughs Only		☐ EBCDIC ☐ ASCII		
☐ Mini-Disk	Burroughs Only		☐ ASCII Only		

7. If you are acting as transmitter, please list the name and employer identification number of each filer for whom you will prepare magnetic media on a separate sheet and attach it to this application.

8. Person responsible for preparation of tax reports	Name *(type or print)*	Title
	Signature	Date

For Paperwork Reduction Act Notice, see back of this form.

Form **4419** (Rev. 3-86)

Instructions for Form 4419

File Form 4419 to request authorization to file any of the forms shown in Block 5 on magnetic media. Please be sure to complete all appropriate blocks. For further information, contact a magnetic media coordinator at the National Computer Center address given below under "Filing Your Application," or by telephone at (304) 263-8700.

Block 1

Enter the name and complete address of the person or organization that will prepare and submit the magnetic media.

Block 4

Show the tax year for which you are requesting authorization to file on magnetic media.

Block 5

Check the boxes next to all of the returns you will file with IRS on magnetic media.

Block 6

Note: The only type of magnetic media on which you can report Forms 1042-S, 6248, 8027 and W-4 is 1/2 inch magnetic tape.

Enter the information requested for the type of magnetic media you intend to submit. Check the appropriate boxes. Enter the name of the manufacturer and the model number or name under "Main Frame" and "Drive Unit." Under "Software," indicate whether the software was purchased or is self-programmed. If purchased, provide the name of the software company.

Block 7

If you will be preparing returns on magnetic media for filers other than yourself, attach to your application a list of names and employer identification numbers of the other filers. If you add or delete any names from your file, submit an updated list to IRS.

Block 8

The form must be signed and dated by an official of the company or organization requesting authorization to report on magnetic media.

Filing Your Application

1. Mail the completed application and any attached lists 90 days before the due date of the returns to:

If by Postal Service,
Magnetic Media Reporting
Internal Revenue Service
National Computer Center
P.O. Box 1359
Martinsburg, WV 25401-1359

If by truck or air freight,
Magnetic Media Reporting
Internal Revenue Service
National Computer Center
Route 9 and Needy Road
Martinsburg, WV 25401

2. IRS will approve or disapprove your application within 30 days of its receipt. Do not submit magnetic media until you receive an authorization letter.

3. After authorization is received, we encourage new filers to submit test data on magnetic media before the filing season. If you want to submit test data, contact the magnetic media coordinator.

4. Your authorization will be valid as long as the magnetic media submitted conforms to the specifications of the applicable revenue procedures. A new application is not required in following years unless magnetic media filing has been discontinued and you wish to resume it.

PAPERWORK REDUCTION ACT NOTICE

We ask for this information to carry out the Internal Revenue laws of the United States. We need it to ensure that the magnetic media you are using will be compatible with our processing equipment. The information is also used to more efficiently schedule and manage its processing at the National Computer Center. You are required to give us this information.

Part IV. Items of General Interest

Revision of Form 56, Notice Concerning Fiduciary Relationship

Announcement 86-78

Form 56, Notice Concerning Fiduciary Relationship, has been revised to incorporate the notice requirements for qualification as executor or receiver under section 6036 of the Internal Revenue Code.

Every receiver, trustee in a bankruptcy case, assignee for the benefit of creditors, other fiduciary, or executor can now use Form 56 to notify IRS that a fiduciary relationship has been created or terminated.

The revised form also includes a new part that constitutes the notice of revocation or termination required by section 6903 of the Internal Revenue Code.

Form 56 (Rev. April, 1986) will be available in many Internal Revenue Service offices beginning July 1986. If the form is not available in your Internal Revenue Servie office, it may be ordered by calling the tax information number in the phone book listed under "United States Government, Internal Revenue Service."

Revision of Form 926, Return by a Transferor of Property to a Foreign Corporation, Foreign Estate or Trust, or Foreign Partnership.

Announcement 86-79

Form 926, Return by a Transferor of Property to a Foreign Corporation, Foreign Estate or Trust, or Foreign Partnership, has been revised to reflect the provisions of Temporary regulations section 1.6038B-1T. The regulations, which were published in the Federal Register on May 16, 1986, provide that a U.S. person who tranfers property to a foreign corporation under section 367, or who elects to apply the principles of section 367 to a transfer, must furnish information about the transfer to the Internal Revenue Service. The form will continue to be used to report transfers of property to foreign entities and to pay any excise tax due under section 1491.

The information that must be provided includes: identifying information about the transferor and the transferee, a description of the property transferred, the amount of consideration received, and a description of how the property will be used in the transferee's trade or business.

The information must be attached to Form 926 and filed with the transferor's income tax return. Taxpayers who made such transfers after 1984 and before June 16, 1986, have until the later of September 16, 1986, or when their income tax returns are due to file Form 926 and the required information. Taxpayers who are not filing section 6038B information (and Form 926) with their income tax returns should file Form 926 and the required information with the service center where they file their income tax returns.

Form 926 (Rev. May 1986) will be available at IRS distribution centers by July 15, 1986. The instructions for the form provide more information on this new use of Form 926.

Correction to Publication 509 (Rev. 10-85)

Announcement 86-80

Publication 509, *Tax Calendars for 1986*, contains an error on page 5. The following correction should be made.

In the third column on page 5, the last entry under the date "August 11" should be placed under the date of August 12. This entry, titled "Social security and withheld income tax," states "Deposit the tax for the period ending August 7, if $3,000 or more."

Publication 597, Information on the United States—Canada Income Tax Treaty, has been Revised

Announcement 86-81

Publication 597, Information on the United States—Canada Income Tax Treaty (revised March 1986), is now available. The publication contains an explanatory discussion, as well as the full text, of the new U.S.—Canada income tax treaty, which is generally effective for tax years beginning after 1984. (For taxes withheld at the source on dividends, interest, royalties, and pensions, the new treaty is effective beginning October 1, 1984. Overall, wherever any greater relief from tax would be provided by the old U.S.—Canada treaty, that treaty continued to have effect for the first tax year beginning in 1985.) The explanatory text is directed primarily to individual U.S. citizens and residents who receive Canadian sourced income.

New Financial Products

Announcement 86-82[1]

The Office of Chief Counsel is in the process of developing a program to identify and analyze new financial products that are being created and sold to investors in public offerings. The Office believes that early identification and analysis of these new products will be useful to the Office in fulfilling its mission of providing guidance to taxpayers concerning the tax consequences of their transactions through the issuance of revenue rulings and regulations.

To assist the Office in identifying and analyzing new financial products as they emerge in the marketplace, the Office encourages taxpayers and tax practitioners to submit to the Office prospectuses and/or other written descriptions of current investment transactions. The individual submitting information is encouraged to point out the tax issues he or she believes are presented by the transaction, as well as any other facts known to the individual concerning market reaction to the product or concerning the underlying financial or tax considerations relevant to its creation or marketability. If after reviewing such submission, the Office determines that additional information or futher clarification of the facts may be helpful in understanding a particular transaction, the Office may contact the sender and request that such additional information or clarification be provided in writing or at a personal meeting. Submissions should be sent to Peter K. Scott, Associate Chief Counsel (Technical), Attention CC:I, Room 4008, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224.

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[1] Also released as News Release IR-86-83 dated June 20, 1986.

Supplemental Information on Treasury Bills for Publication 1212

Announcement 86-83

Banks, brokers, and other middlemen who report discount on Treasury bill redemptions on Form 1099-INT must use the owner's purchase price, where available, to determine the amount of discount to report. Usually this information can be obtained from the owner's or middleman's records. However, if the owner's purchase price is *not* available from existing records, the middleman must report the discount as if the holder had purchased the Treasury bill at its original issue price. In this case, the middleman must use as the original issue price the noncompetitive issue price for the longest-maturity Treasury bill maturing on that date.

For Treasury bill redemptions in cases where the owner's purchase price *cannot* be determined, a list of the noncompetitive issue prices and corresponding amounts of discount to be reported on Form 1099-INT for Treasury bills maturing in 1986 appears below. This list, which should also help middlemen determine any amounts subject to backup withholding, supplements the list that appears in Publication 1212, *List of Original Issue Discount Instruments* (Rev. Dec. 1985) and Announcement 86-7, 1986-4 I.R.B. 67.

SHORT TERM UNITED STATES TREASURY BILLS ISSUED AT A DISCOUNT AND MATURING DURING 1986

CUSIP Number	Maturity Date	Issue Date	Noncompetitive Issue Price (% of Principal Amount)	Dollar Amount of Discount to be Reported as Interest for 1986 (Per $1,000 of Maturity Value)
912794JL	01/02/86	07/05/85	96.440	35.60
JM	01/09/86	07/11/85	96.461	35.39
JN	01/16/86	07/18/85	96.360	36.40
JP	01/23/86	01/24/85	91.517	84.83
JQ	01/30/86	08/01/85	96.259	37.41
JR	02/06/86	08/08/85	96.198	38.02
JS	02/13/86	08/15/85	96.279	37.21
JT	02/20/86	02/21/85	91.446	85.54
JU	02/27/86	08/29/85	96.355	36.45
JV	03/06/86	09/05/85	96.309	36.91
JW	03/13/86	09/12/85	96.264	37.36
JX	03/20/86	03/21/85	90.657	93.43
JY	03/27/86	09/26/85	96.436	35.64
JZ	04/03/86	10/03/85	96.340	36.60
KA	04/10/86	10/10/85	96.299	37.01
KB	04/17/86	04/18/85	91.466	85.34
KC	04/24/86	10/24/85	96.299	37.01
KD	05/01/86	10/31/85	96.274	37.26
KE	05/08/86	11/07/85	96.309	36.91
KF	05/15/86	05/16/85	91.972	80.28
KG	05/22/86	11/21/85	96.330	36.70
NH	05/29/86	11/29/85	96.350	36.50
KJ	06/05/86	12/05/85	96.330	36.70
KK	06/12/86	06/13/85	92.740	72.60
KL	06/19/86	12/19/85	96.456	35.44
KM	06/26/86	12/26/86	96.436	35.64
912794KV	07/03/86	01/02/86	96.426	35.74
KN	07/10/86	07/11/85	92.831	71.69
KW	07/17/86	01/16/86	96.320	36.80
KX	07/24/86	01/23/86	96.390	36.10
KY	07/31/86	01/30/86	96.446	35.54
KP	08/07/86	08/08/85	92.316	76.84
KZ	08/14/86	02/13/86	96.345	36.55
LA	08/21/86	02/20/86	96.446	35.54
LB	08/28/86	02/27/86	96.461	35.39

SHORT TERM UNITED STATES TREASURY BILLS—Continued
ISSUED AT A DISCOUNT AND MATURING DURING 1986

CUSIP Number	Maturity Date	Issue Date	Noncompetitive Issue Price (% of Principal Amount)	Dollar Amount of Discount to be Reported as Interest for 1986 (Per $1,000 of Maturity Value)
912794KQ	09/04/86	09/05/85	92.558	74.42
LC	09/11/86	03/13/86	96.694	33.06
LD	09/18/86	03/20/86	96.689	33.11
LE	09/25/86	03/27/86	96.749	32.51
KR	10/02/86	10/03/85	92.589	74.11
LF	10/09/86	04/10/86	96.881	31.19
LG	10/16/86	04/17/86	97.002	29.98
LH	10/23/86	04/24/86	97.032	29.68
KS	10/30/86	10/31/85	92.407	75.93
LJ	11/06/86	05/08/86	96.921	30.79
LK	11/13/86	05/15/86	96.916	30.84
LL	11/20/86	05/22/86	96.825	31.75
KT	11/28/86	11/29/85	92.589	74.11
LM	12/04/86	06/05/86	96.759	32.41
LN	12/11/86	06/12/86	96.770	32.30
LP	12/18/86	06/19/86	96.876	31.24
KU	12/26/86	12/26/85	92.842	71.58

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Mack T. Frank	Eunice, LA	Attorney	Indefinite from April 1, 1986
Carl Goldfarb	Charlotte, NC	Attorney	Indefinite from April 28, 1986
Dennis M. Hayes	Ann Arbor, MI	Attorney	Indefinnite from April 15, 1986
Ronald N. Kief	Warren, MI	Certified Public Accountant	Two Years from June 1, 1986
Richard L. Leopold	Ottawa, OH	Attorney	Three Months from May 1, 1986
Julius Stackel	Flushing, NY	Certified Public Accountant	Thirty Months from April 15, 1986
John Such	Lyndhurst, OH	Enrolled Agent	Eighteen Months from April 22, 1986

Name	Address	Designation	Term of Suspension
Henry L. Creel	Cleveland, OH	Certified Public Accountant	Indefinite from May 15, 1986
J. Thomas Jones	Augusta, GA	Certified Public Accountant	Indefinite from June 1, 1986
Michael D. Sherman	Pound Ridge, NY	Enrolled Agent	Indefinite from May 27, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and address of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolld actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the Weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Earl M. Walker	Port Neches, TX	Certified Public Accountant	May 19, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.367(a)-1, removed; 1.367(a)-4T, redesignated as 1.367(a)-7T; 1.367(a)-1T through 1.367(a)-6T, 1.367(d)-1T, 1.6038B-1T, added; 7.367(b)-1, 7.367(b)-4, amended; published as temporary regulations in T.D. 8087, page 5, 1986-23 I.R.B.	Transfers of property by U.S. persons to foreign corporations	1986-23 I.R.B. 33	July 15, 1986
26 CFR 1,338-1T, 1.338-2T, 1.338-4T, 1.338-5T, 1,338(h)(10)-1T, amended; published as temporary regulations in T.D. 8088, page 4, 1986-24 I.R.B.	Section 338(g) statements of election	1986-24 I.R.B. 24	July 15, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1985-26 through 1985-52 will be found in Internal Revenue Bulletin 1986-1, dated January 6, 1986.

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_____	*1936-2*	*15.00*
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_____	1947-2	3.75
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_____	1948-2	8.50
_____	*1949-1*	*8.00*
_____	*1949-2*	*3.25*
_____	1950-1	7.00
_____	*1950-2*	*5.50*
_____	*1951-1*	*13.00*
_____	*1951-2*	*6.00*
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_____	1952-2	8.00
_____	*1953-1*	*4.75*
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_____	1954-2	13.00
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_____	1955-2	14.00
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_____	1956-2	20.00
_____	1957-1	18.00
_____	1957-2	(**)
_____	1958-1	11.00
_____	1958-2	(**)
_____	1958-3	17.00
_____	1959-1	19.00
_____	1959-2	11.00
_____	1960-1	21.00
_____	1960-2	13.00
_____	1961-1	15.00
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_____	1964-1-2	12.00
_____	1964-2	28.00
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_____	1965-2	13.00
_____	1966-1	15.00
_____	1966-2	15.00
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_____	1967-2	17.00
_____	1968-1	15.00
_____	1968-2	13.00
_____	1969-1	15.00
_____	1969-2	7.50
_____	1969-3	14.00
_____	1970-1	12.00
_____	1970-2	(**)
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_____	1972-2	15.00
_____	1973-1	18.00
_____	1973-2	15.00
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_____	*1974-3*	*9.50*
_____	1974-3 Supp.	11.00
_____	1975-1	15.00
_____	1975-2	14.00
_____	1976-1	12.00
_____	1976-2	11.00
_____	1976-3-1	10.00
_____	1976-3-2	18.00
_____	1976-3-3	11.00
_____	1977-1	12.00
_____	1977-2	13.00
_____	1978-1	13.00
_____	1978-2	14.00
_____	1978-3-1	13.00
_____	1978-3-2	9.50
_____	1979-1	15.00
_____	1979-2	17.00
_____	1980-1	17.00
_____	1980-2	19.00
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1986-27

July 7, 1986
Bulletin No. 1986–27

Internal Revenue bulletin

HIGHLIGHTS OF THIS ISSUE

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A list is given of organizations now classified as private foundations.

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Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

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Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Cumulative List of Announcements Relating to Decisions of the Tax Court Published in the Internal Revenue Bulletin from January 1, 1986 thru June 30, 1986

It is the policy of the Internal Revenue Service to announce in the Internal Revenue Bulletin at the earliest practicable date the determination of the Commissioner to acquiesce or not acquiesce in a decision of the Tax Court which disallows a deficiency in tax determined by the Commissioner to be due.

Notice that the Commissioner has acquiesced or nonacquiesced in a decision of the Tax Court relates only to the issue or issues decided adversely to the Government.

Actions of acquiescences in adverse decisions shall be relied on by Revenue officers and others concerned as conclusions of the Service only to the application of the law to the facts in the particular case. Caution should be exercised in extending the application of the decision to a similar case unless the facts and circumstances are substantially the same, and consideration should be given to the effect of new legislation, regulations, and rulings as well as subsequent court decisions and actions thereon.

Acquiescence in a decision means acceptance by the Service of the conclusion reached, and does not necessarily mean acceptance and approval of any or all of the reasons assigned by the court for its conclusions.

No announcements are made in the Bulletin with respect to memorandum opinions of the Tax Court.

The announcements published in the weekly Internal Revenue Bulletins are consolidated semiannually and annually. The semiannual consolidation appears in the first Bulletin for July and in the Cumulative Bulletin for the first half of the year and the annual consolidation appears in the first Bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner ACQUIESCES in the following decisions:

Taxpayer	Docket No.	*Report* Volume	Page
Allied Industrial Cartage Co.[1]	7918–77	72	515
Commercial Security Bank[2]	5652–79	77	145
Gamble, Launce E. & Joan L.[3]	1617–76	68	972
Goldsboro Arts League, Inc.[4]	8060–80X	75	337
McIntosh, John[5]	21618–81	85	31
Moden, John B., et ux[6]	16201–79	85	731
Schwartz, Est. of Henry K., Robert Schwartz, Suzanne Schwartz & Mark Stewart, administrators[7]	17918–82	83	943
Vanicek, Edward, Deceased & Sara Vanicek[6]	165187–79	85	731
Woods Investment Co.[8]	6237–83	85	274

The Commissioner does NOT ACQUIESCE in the following decision:

Taxpayer	Docket No.	*Report* Volume	Page
Sutherland, Robert D., d/b/a Sutherland Rocky Mountain Lumber Co.[9]	9971–78R	78	395

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[1] Acquiescence relating to whether the rental income received by petitioner from the lease of real estate and trucks to a brother-sister corporation, which is also 100 percent owned by petitioner's sole shareholder, constitutes an amount received as compensation for the right to use corporate property by a shareholder under section 543(a)(6) of the Code.

[2] Acquiescence relating to whether Orem State Bank is entitled to deduct accrued but unpaid business liabilities on its final corporate income tax return.

[3] Acquiescence in the issues relating to (1) whether petitioners must report as ordinary trade or business income, the gain on the sale of a thoroughbred colt which was 16½ months old, and (2) what portion, if any, of the purchase price of a mare in foal must be allocated to the foal. See Rev. Rul. 86–24, 1986–8 I.R.B. 7.

[4] Acquiescence relating to whether petitioner, a multifaceted cultural arts and educational organization, operates two art galleries to exhibit and sell the original works of individual artists, whether these operations disqualify petitioner as an organization described in section 501(c)(3) of the Code because operated for a substantial commercial purpose or to serve the private interests of the artists.

[5] Acquiescence relating to whether petitioner's transfer of an undivided one-half interest in ranchland to his former wife, pursuant to a property settlement agreement executed in connection with their divorce, constitutes a taxable disposition.

[6] Acquiescence relating to whether the fair rental value of lodging furnished to petitioners by their employer, the Forest Preserve District of Cook County, Illinois, is excludable from gross income under section 119 of the Code.

[7] Acquiescence relating to whether a foreign death tax credit under section 2014 of the Code is allowable when the estate of a U.S. citizen, resident of a foreign country, pays death taxes to that foreign country attributable to a bank account located in that foreign country.

[8] Acquiescence relating to whether, upon selling the stock of its subsidiaries, the petitioner must reduce its basis in that stock by the excess of accelerated over straight-line depreciation.

[9] Nonacquiescence relating to whether, for purposes of testing the coverage requirements of section 410(b)(1) of the Code, employees of two controlled corporations must be aggregated with the controlling corporation pursuant to section 414(c), when the controlled corporations are suffering substantial financial losses.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term and long-term rates are set forth for the month of July 1986. See Rev. Rul. 86-86, page 34.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of July 1986. See Rev. Rul. 86-86, page 34.

Section 468.—Special Rules for Mining and Solid Waste Reclaimation and Closing Costs

Federal short-term, mid-term and long-term rates are set forth for the month of July 1986. See Rev. Rul. 86-86, page 34.

Section 483.—Interest on Certain Deferred Payments

Federal short-term, mid-term and long-term rates are set forth for the month of July 1986. See Rev. Rul. 86-86, page 34.

Section 936.—Puerto Rico and Possession Tax Credit

T.D. 8090

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER A, PART I—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Possessions Tax Credit: Definition of Product, Significant Business Presence Test, and Cost Sharing and Profit Split Elections

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the possessions tax credit. The regulations provide rules for determining whether a possessions corporation has a significant business presence with respect to a product. These regulations also provide rules which implement the cost sharing and profit split elections. This action is necessary because of changes to the applicable tax law made by the Tax Equity and Fiscal Responsibility Act of 1982 [Pub. L. 97-248, 1982-2 C.B. 462].

DATES: The amendments are effective for taxable years of possessions corporations beginning on or after January 1, 1983.

FOR FURTHER INFORMATION CONTACT: Jacob Feldman of the Office of Associate Chief Counsel (International), Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T LR-194-82, telephone 202-566-3289 (not a toll-free call), concerning intangible property income in the absence of an election under section 936(h)(5), the cost sharing and profit split elections, and covered intangibles (§§1.936-4, 1.936-6, and 1.936-7); or Carol Doran Klein of the same office concerning the definition of product, the significant business presence test, and contract manufacturing (§1.936-5), telephone 202-566-6419.

SUPPLEMENTARY INFORMATION:

BACKGROUND

On January 10, 1984, the FEDERAL REGISTER published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 936(h) of the Internal Revenue Code of 1954 (49 F.R. 1227) [1984-1 C.B. 733]. The amendments were proposed to conform the regulations to changes made to the Internal Revenue Code by section 213 of the Tax Equity and Fiscal Responsibility Act of 1982 (the Act) (Pub.L. 97-248, 96 Stat. 452) [1982-2 C.B. 462, 486]. A public hearing was held on April 3, 1984. After consideration of all comments received regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

DISCUSSION OF COMMENTS AND REVISED AMENDMENTS

Section 1.936-4

Intangible Property Income in the Absence of an Election out

Commenter suggested that in situations in which there is no intangible property income, a taxpayer should not be limited in computing its taxable income to cost sharing, profit split or the method under section 936(h)(1) to (h)(3). It was decided, in situations in which there is no intangible property income, to permit a taxpayer to compute its income using the appropriate method as provided under section 482 and the regulations thereunder.

Commenter suggested that the covered intangible exception should apply not only if cost sharing is elected, but also in the absence of an election out. The suggestion was rejected because there is no statutory support for permitting the covered intangible exception if the taxpayer elects to compute its income under section 936(h)(1) to (h)(3). The covered intangible exception is permitted under section 936(h)(5)(c)(i)(II), a provision dealing only with the cost sharing election.

Section 1.936-5(a)

Definition of the Term "Product"

Commenters suggested that the term "product" not be defined by means of the phrase "manufacturing process" because of possible confusion with the section 954(d)(1)(A) definition of manufacturing. They suggested broader terms such as produced, transformed, incorporated or assembled. This suggestion was adopted. For these purposes, it is intended that production, transformation, incorporation or assembly be given a broad meaning.

Commenters also suggested that the phrase "transformation, incorporation, assembly" be used instead of the phrase "further transformation." This suggestion was also adopted.

The final regulations clarify that a possessions corporation may treat the end-product form as its possession product even though the final stage or stages of production occur outside of a possession.

The final regulations provide that if a possessions corporation produces a product that is sometimes sold to unrelated parties without further processing and is sometimes sold to unrelated parties after further processing, then the possessions corporation generally must choose to treat the same item of property as its possession product, even though it is in some cases an integrated product and in some cases a component product.

Commenters suggested that the proposed regulations required taxpayers to choose either the component product, the integrated product, or the end-product form as their possession product and to apply that choice consistently for all purposes of section 936. Many possessions corporations, however, sell both an integrated product and a component contained in the integrated product. The regulations, when adopted, should not limit the possessions corporation to a return on only one of these products when both are produced in the possessions.

In response to the comments, the final regulations provide that a possessions corporation may designate a different product at each stage of the production process, if the product is sold at the end of that stage to unrelated parties. The possessions corporation's product must be defined consistently for all products sold at the same stage in the production process. Thus, if a possessions company produces a component in a possession and finishes some of the components in the possession and transfers some to an affiliate for finishing in the United States, then, for all finished products sold to third parties, the possessions company must designate either the component or the integrated product as its possession product. Furthermore, if the possessions company produces a product in a possession, sells the product to third parties, and also subjects the product to further processing before sale to third parties, then the possessions corporation may designate two possession products.

Commenters suggested that the final regulations permit taxpayers to designate their possession product by listing those components that are not included in the possession product. This suggestion was adopted.

Grouping of Products

Commenters raised several questions with respect to grouping of products. In response to those comments the final regulations clarify that products that are grouped are treated as one product, and that, if a taxpayer's grouping is disallowed, the effect of the disallowance is to require each of the products that is removed from the group and the remaining group without the excluded products to satisfy separately the significant business presence test. The final regulations also make clear that the determination of whether the production processes involved in producing the products that are to be grouped are similar is based on the production processes of the components that are included in the possession product.

Commenters stated that the usefulness of the grouping rules was limited because of the discretion given the Commissioner to require grouping or to disallow a taxpayer's grouping. The final regulations do not allow the Commissioner to require the taxpayer to group products. A primary purpose of permitting grouping is to allow taxpayers to reduce their recordkeeping burden. Because this is the case, the Commissioner will not require the taxpayer to group products.

The final regulations also provide that a taxpayer may not include in a group an item of property that is not produced in whole or in part in a possession.

Commenters suggested that the final regulations clarify whether the general rules concerning grouping apply to pharmaceuticals. The final regulations apply the general rules to pharmaceuticals. The reason for this change is that a purpose of grouping is to ease the taxpayer's recordkeeping burden with respect to isolating production costs for a particular product. If the production processes involved in producing two items are not similar, then the taxpayer should be able to separate its production costs for those items. Thus, the rules for grouping pharmaceuticals should be the same as the rules for grouping other products. These revisions also clarify that pharmaceuticals may be grouped even though they contain different active or inert ingredients so long as the production processes are similar.

Interim Period and Transitional Period Rules

The proposed regulations provided that a possessions corporation which produced a product in a possession on September 3, 1982, need not satisfy the significant business presence test with respect to that product until taxable years beginning on or after January 1, 1986. For purposes of determining the product produced in the possessions, only the activities actually performed in the possession are to be taken into account. If a possessions corporation would claim a return on intangibles associated with the portion of the product produced outside of the possession, then the possessions corporation must satisfy the significant business presence test with respect to that larger product.

Commenters objected to these rules stating that the statute waives the significant business presence test with respect to products produced in the possession on date of enactment, but the effect of the proposed rules is to impose a significant business presence test on products produced on date of enactment. Commenters also claim that Congress intended to treat "old" products more favorably than, or at least as favorably as "new" products. New products are not immediately subject to the full significant business presence test but rather are entitled to a phase-in of the significant business presence test. If "old" products are to be subject to a significant business presence test prior to January 1, 1986 commenters stated that the "old" products should be allowed the benefit of phasing in the test. Furthermore, no test should apply for taxable year 1983 because the proposed regulations were not published until 1984 and, therefore, taxpayers had no opportunity to arrange their affairs so that they could satisfy this test.

These various comments were rejected for the following reasons. First, requiring the product to be produced in a possession within the meaning of section 954(d)(1)(A) does not impose a significant business presence test on products produced in a possession on the date of enactment. The regulations must provide guidance as to the meaning of the phrase "produces a product . . . in a possession on the date of enactment." Under the interpretative authority granted the Secretary, the Treasury has determined that this phrase means the product that is produced within the meaning of section 954(d)(1)(A). Second, the commenters claim that Congress intended to treat products produced in a possession on the date of enactment more favorably than products first produced in a possession after that date. There is no basis for this claim either in the statute or in the legislative history.

Section 936(h)(5)(B)(iii)(I) provides that, if a possessions corporation produced a product in a possession on the date of enactment, then, with respect to such product, the possessions corporation is not required to meet the significant business presence test for its taxable years beginning before January 1, 1986. Section 936(h)(5)(B)(iv)(I) provides that the Secretary may prescribe regulations setting forth an appropriate transitional (but not in excess of three taxable years) significant business presence test for commencement in a possession of operations with respect to products or types of service after date of enactment and not described in section 936(h)(5)(B)(iii)(I). Thus, the Code states that the Secretary has authority to prescribe regulations adopting a transitional rule in all cases except those which are covered by the statutory exemption from the significant business presence test.

It may be more advantageous to the taxpayer to satisfy a reduced significant business presence test with respect to an integrated product than to be exempted from the significant business presence test and be permitted to determine income under the cost sharing or profit split option only with respect to the component product or the end-product form. The reason that a possessions corporation might be in a better position if it could take advantage of the reduced significant business presence test is that, if the possessions corporation is able to satisfy the reduced test with respect to an integrated product, then the possessions corporation will be entitled to a return on intangibles associated with the integrated product. If, however, the possessions corporation is exempt from the significant business presence test, then the corporation will only be entitled to a return on the intangibles associated with the product produced in the possessions. Thus the income attributable to the more narrowly defined product, and against which credit will be granted, will be less. Correspondingly, the income taxed to the U.S. affiliates will be increased.

The interpretation adopted in the final regulations is consistent with the legislative history. The conference report states that:

> The conferees also intend that the *provision be administered in a fashion so as to encourage increased Puerto Rican employment and investment in depreciable property at as low a cost to the Treasury as possible.*
>
> The conferees are concerned about Puerto Rican job creation and there is continuing concern that the provision may not be adequately targeted towards that goal. (Emphasis added).

H.R. REP. No. 760, 97th Cong., 2nd Sess., at 505 (1982) [1982-2 C.B. 600, 617].The legislative history also indicates the transitional rules described above only apply to future operations and future possession products and possession services. *General Explanation of the Revenue Provisions of the Tax Equity and Fiscal Responsibilty Act of 1982*; H.R. 4961, Pub. L. 97-248, at 89 (1982). If these two parts of the legislative history are read together, it is apparent that Congress intended to encourage new possessions employment and investment by providing an incentive for corporations to move new operations into the possessions after the date of enactment. Corporations which were already operating in the possessions should not get the benefit of this provision, with respect to such operations, because allowing them these benefits would not encourage new employment and investment in the possessions and would result in substantial revenue loss to the Treasury. Thus, it is believed that Congress intended to provide the benefit of a reduced significant business presence test only to corporations starting new operations in the possessions.

Different Product for Export Sales

The proposed regulations provided that a possessions corporation could not define its product differently for export sales than for domestic sales. Commenters stated that the separate election for export sales should be interpreted in such a manner that the possessions corporation's product may be defined differently for export sales than for domestic sales. They further state that foreign countries frequently require some local processing in order to avoid tariff or other import restrictions. Further, requiring the possessions corporation to define consistently its product for export and domestic sales will discourage investment in the possessions. If a company will not be allowed any return on intangibles associated with finishing a product for the domestic market there will be no incentive to set up new finishing operations in the possessions. The final regulations permit a possessions corporation to define its product differently for export sales than for domestic sales.

Section 1.936-5(b)

Significant Business Presence Test General Rules

The final regulations make clear that two related possessions corporations may not aggregate their production or direct labor costs for purposes of determining whether they satisfy the significant business presence test with respect to a single product.

Production Costs

Commenters suggested that the phrase "production costs" should be used if the regulations intended that the words be defined in the same manner as under section 471. This suggestion was adopted. The final regulations use the phrase "production costs" because it is intended that this phrase be defined consistently for purposes of sections 471 and 936. Production costs do not, however, include direct material costs and interest.

Commenters requested that the final regulations clarify whether taxpayers are permitted to include in production costs those costs that they did not include in inventoriable costs for purposes of section 471. The final regulations clarify that taxpayers may not include such costs for purposes of section 936.

The final regulations clarify that a possessions corporation may not include a cost as a production cost unless all members of the affiliated group include that cost as a production cost. Also, with respect to production costs, the final regulations clarify that taxpayers should use their current year's production costs to determine whether they satisfy the significant business presence test regardless of whether they use the FIFO or LIFO method of accounting.

Direct Labor Cost

Commenters stated that the proposed regulations were unclear as to whether the direct labor costs involved in processes that are not considered to be manufacturing under section 954(d)(1)(A) (for example, packaging) could be included in the direct labor costs of the possessions corporation. The final regulations provide that, so long as the cost in includable under section 471 in inventoriable costs, the cost may be considered a direct labor cost of the possessions corporation even though the activity would not constitute manufacturing under section 954(d)(1)(A).

Commenters suggested that the term "direct labor" should include personnel, quality control, maintenance, research and development, accounting, treasury and other functions to the extent these activities take place in the possessions. This suggestion was generally rejected because indirect labor costs are taken into account under the value added test. However, the labor associated with quality control will be considered direct labor if that quality control is an integral part of the production process.

One commenter recommended that, for purposes of the value added test, the amount of gross receipts should be reduced by any excise tax paid by the possessions corporation on units of the product sold for use or consumption in the possession. Because the term "gross receipts" is defined in the same manner as possession sales and the possession sales amount does not include these excise taxes, the gross receipts amount does not include these excise taxes either.

The proposed regulations provided that inspection and testing are indirect production costs. Therefore, the labor costs associated with inspection and testing may not be considered direct labor costs. Commenters stated that quality control is an integral part of the production process and, therefore, the labor costs associated therewith should be considered direct labor costs. This suggestion was adopted in those cases in which quality control is an integral part of the production process.

Commenters suggested that taxpayers should be able to get the benefit of the start-up significant business presence test if they begin operations at a new site in the same possession. This suggestion was rejected because starting up operations in a new possession presents more difficulties than starting at a new site within the same possession.

Commenters suggested that base period construction costs should include the costs associated with the installation of section 1245 property and that any base year that the corporation was not in existence should not be taken into account. Both of these suggestions were rejected.

Commenters recommended that the Secretary adopt additional significant business presence tests. This recommendation was rejected.

Section 1.936–5(c)

Contract Manufacturing

The proposed regulations defined the term "contract manufacturing" to include any arrangement between a possessions corporation (or another member of the affiliated group) and an unrelated person if the unrelated person uses intangibles that are related to its product and the intangibles are owned or licensed by a member of the affiliated group. Commenters stated that this part of the definition was too broad. In response to these comments, the definition of contract manufacturing has been narrowed. Contract manufacturing will only include use of an intangible if the intangible is a patent and the product produced under the patent is included in the possession product or if the intangible is a manufacturing intangible and it is established that the arrangement has the effect of materially distorting the application of the significant business presence test. The reason for these rules is to prevent taxpayers from earning intangible income attributable to the patent or other intangibles without taking into account, for purposes of the significant business presence test, the costs associated with producing the patented product. For example, if a taxpayer enters into a contract with an unrelated party whereby the unrelated party produces the patented product for the taxpayer and sells that product to the taxpayer, the unrelated party would earn a return on the manufacturing activities it performed. If the taxpayer incorporated that product into its possession product and then marketed it to the public, the income from the patent would be earned by the taxpayer without any performance of activity by the taxpayer with respect to the patented item. Therefore, the cost of producing the patented product should be taken into account. The regulations provide that these rules shall not apply to such contract manufacturing performed in taxable years beginning before January 1, 1986, nor shall the rules apply to binding contracts for the performance of such contract manufacturing entered into before June 13, 1986.

The proposed regulations treat the entire cost of contract manufacturing performed outside of the possessions as direct labor of the affiliated group performed outside of the possessions. Commenters claim that this unfairly penalizes taxpayers as the supplier's cost of materials, production costs and profit will be considered direct labor of the affiliated group. If the U.S. affiliates had performed identical manufacturing activities, only the direct labor element of the total costs would be counted against the possessions corporation. The final regulations retain this rule because it is intended to have the protested effect.

Section 1.936–6(a)(1)

Product Area Research

Commenter suggested that product area research should apply only to those expenses with respect to which a tax benefit was obtained. This suggestion was rejected since it is inconsistent with the statutory language under section 936(h)(5)(C)(i)(I)(*a*) which defines product area research very broadly and beyond deductible expenses.

Commenter suggested that the cost of acquisition of nonamortizable intangible property should not be included in product area research in the year of acquisition, but instead should either not be included or included over a longer period. The regulation has been amended to include the cost of acquisition of nonamortizable intangibles ratably over a 5-year period. Non-inclusion of nonamortizable intangibles was rejected because section 936(h)(5)(C)(i)(I)(*a*) specifically requires an inclusion of "a proper allowance for amounts incurred in the acquisition of any of the items specified in subsection (h)(3)(B)(i)" (manufacturing intangibles).

Commenters suggested that the regulations make clear that payments described in section 30(b) and other payments made for amortizable and nonamortizable intangibles apply only to those payments made for the acquisition of manufacturing intangible property. This suggestion is in conformity with the statute and the suggested clarification has been made.

Commenter suggested that product area research expenditures be reduced by the income received by a possessions corporation from the sale of a manufacturing intangible to a person outside the affiliated group. The suggestion was adopted. However, the income from the sale does not reduce product area research in the year of the sale, but instead is treated as royalty payments made ratably over the remaining useful life of the intangible. If the intangible is nonamortizable, then product area research is reduced ratably over a 5-year period.

Commenter suggested that product area research not include research and development expenses incurred by a member of an affiliated group pursuant to a contract with an unrelated person who is entitled to exclusive ownership of the technology resulting from the expenditures. The suggestion was adopted. The final regulations provide that, to the extent the product area research expenditures can be allocated solely to the technology produced for an unrelated person, such expenditures will not be included in product area research provided that the unrelated person has exclusive ownership of the technology and that no member of the affiliated group has a right to use any of the technology.

Commenter requested clarification on the computation of product area research where the component product and integrated product fall within different product areas. The final regulations clarify the issue. If the component product and integrated product are in separate SIC codes and if the component product is included in the definition of the possession product, then the product area research expenditures are aggregated. If the component product is not included in the definition of possession product, then the product area research expenditures are not aggregated and the product area research expenditures incurred with respect to the component product are not included in product area research.

§1.936-6(a)(2)

Possession sales and total sales

Commenter suggested that pre-TEFRA sales should be excluded from the numerator and denominator of the cost sharing fraction. The suggestion was adopted.

Commenter suggested a clarification of the sales price of a component product and an end-product form. In response to the comment the regulations have been redrafted to provide as follows. With respect to a component product, an independent sales price from comparable uncontrolled transactions must be used if such price can be determined in accordance with §1.482-2(e)(2). With respect to an end-product form, the sales price is the difference between the third party price of the integrated product and the independent sales price of the excluded component product(s) from comparable uncontrolled transactions. If an independent sales price from comparable uncontrolled transactions cannot be obtained, then the sales price of the component product shall be deemed to be equal to the transfer price, determined under the appropriate section 482 method, which the possessions corporation uses under the cost sharing method in computing the income it derives with respect to the component product. Alternatively, the possessions corporation may determine the sales price for the component product using a production cost ratio, but if this method is used, then the transfer price used by the possessions corporation in computing its income may not be greater than such sales price. A similar rule deals with an end-product form. The method chosen in the final regulations is preferable to merely using the production cost ratio since the transfer price will be used by the taxpayer in computing income and therefore, should, if possible, also be reflected in the numerator of the cost sharing fraction.

Commenter suggested that the regulations provide that excise taxes paid by the possessions corporation when the product is for ultimate use or consumption in the possession not be included in possession sales. The suggestion was adopted. The final regulations provide that the amount of excise tax is excluded from both the numerator and denominator of the cost sharing fraction.

Commenter suggested that rules be provided to permit cost sharing with respect to sales of possession products to members of the affiliated group which includes the possessions corporation where the possession product is not sold outside of the affiliated group and where the affiliate leases the product to unrelated persons. The suggestion was adopted. The final regulations provide that if an independent sales price for the possession product can be determined under 1.482-2(e)(2), then possessions corporation may use the cost sharing method with respect to a possession product which it sells to its affiliate if the affiliate leases such product to unrelated persons or uses the possession product in its own trade or business. If the possession product is a component product or an end-product form where there is not a comparable uncontrolled price, then the taxpayer may determine the sales price of the component product or end-product form under rules provided elsewhere in the regulation.

For taxable years beginning after June 13, 1986, a possessions corporation will not be entitled to the benefits of the cost sharing method with respect to units of a possession product which the possessions corporation sells to an affiliate where the affiliate then leases such units to an unrelated person or uses them in its own trade or business, unless the affiliate agrees to be treated for all tax purposes as having sold such units to an unrelated party at the time they were first leased or otherwise placed in service by such affiliate.

§1.936-6(a)(3)

Credits against cost sharing payments

Commenter suggested that payments made under cost sharing arrangements with related persons should be creditable against cost sharing payments. This suggestion was not adopted since it is contrary to section 936(h)(5)(C)(i)(I) which specifically sets forth the criteria which must be satisfied for a payment to be treated as a credit against the cost sharing payment.

§1.936-6(a)(5)

Effect of election under the cost sharing method

Commenter suggested that the reduction in deductions under the cost sharing method are limited to the deductions taken by the affiliates which incurred the product area research expenditures. This suggestion was not adopted since it might result in a possessions corporation being treated as the owner of a manufacturing intangible without any appropriate reduction in deductions of a related affiliate.

§1.936-6(b)(1)

Profit split computation of combined taxable income

Commenter suggested that the regulations should be modified and that the general principles under §1.861-8 should be followed without modification for allocating marketing and distribution expenses. In response to comments, the rules for allocations of marketing and other distribution expenses have been modified to permit separately identifiable expenses related solely to a specific product or group of products to be allocated to the class of gross income defined by that specific product or group of products. The rules for apportionment of these deductions remain unchanged. The rules for allocation and apportionment of other expenses are also unchanged.

Commenter raised the issue as to how samples should be treated. The final regulations take the position that samples are to be treated as a marketing expense and not as inventoriable costs. However, for taxable years beginning prior to January 1, 1986, the taxpayer at its option may treat the cost of samples as either inventoriable costs or as a marketing expense.

Commenter suggested that the regulations take the position that the non-possessions corporation's share of the profit split should be deemed to accrue on the last day of the taxable year for estimated tax purposes. The suggestion was adopted.

Commenter suggested that in allocating one-half of the combined taxable income under the profit split option to the appropriate member of the affiliated group the first allocation should be made to U.S. affiliates which have gross income with respect to the product produced in whole or in part in the possession. The suggestion was adopted.

Commenter suggested a clarification of the sales price of a component product or an end-product form in computing combined taxable income. In response to the comment, the regulations have been redrafted to provide as follows. With respect to a comparable product, an independent sales price from comparable uncontrolled transactions must be used if such price can be determined in accordance with §1.482–(e)(2). With respect to an end-product form, the sales price is the difference between the third party price of the integrated product and the independent sales price of the component product from comparable uncontrolled transactions. If an independent sales price from comparable uncontrolled transactions cannot be obtained, then the taxpayer may use the production cost ratio in computing the sales price for the component product and the end-product form.

Commenter suggested that rules be provided to permit profit split with respect to sales of possession products to U.S. members of the affiliated group of corporations which includes the possession corporation where the possession product is sold to the U.S. affiliate for use in its own trade or business or the U.S. affiliate leases the product to unrelated persons or foreign affiliates. The suggestion was adopted. The final regulations provide that if an independent sales price for the possession product can be obtained, then a possession corporation may use the profit split method with respect to a possession product which it sells to its affiliate if the affiliate leases such product to unrelated persons or uses the possession product in its own trade or business. If the possession product is a component product or an end-product form where there may not be a comparable uncontrolled price, then the taxpayer may determine the sales price of the component or end-product form under rules provided elsewhere in the regulation.

Commenters raised issues with respect to a U.S. affiliate which includes purchases of the possession product in a dollar-value LIFO inventory pool. The proposed regulations failed to convert costs into sales revenue. The regulations have been amended with special rules for determining both costs and sales revenue for purchases and sales of possession products where the U.S. affiliate uses the dollar-value LIFO inventory pool for the possession product. The sales revenue determined in this manner also applies for the cost sharing option.

§1.936–6(c)

Covered intangibles

Commenter suggested that a covered manufacturing intangible should not be required to be obtained directly from an unrelated person and that obtaining it indirectly from an unrelated person through an affiliate should be permitted. The suggestion was not adopted. However, the regulation has been modified to permit a manufacturing intangible to qualify as a covered intangible if it was both acquired by an affiliate from an unrelated person and transferred to the possessions corporation by the affiliate prior to September 3, 1982.

Commenter suggested that licensing of an intangible from a related party should give rise to a covered intangible. The suggestion was not adopted since the statute requires that the intangible be "acquired" from an unrelated person. A license, even an exclusive license, does not constitute an acquisition of the intangible.

§1.936–7(a)

Manner of making election

Commenter suggested that the requirement that all affiliates consent to the election should be replaced by a blanket consent by the parent. The suggestion was not adopted. However, the consent rules have been liberalized.

Commenter suggested that the election out should be on a product-by-product basis rather than a product area basis. The suggestion was not adopted.

Commenter suggested that the one-time change in election should be applicable retroactively and should apply to the absence of an election out under section 936(h)(5). The suggestion was adopted. Therefore, the taxpayer will be permitted to make a one-time change of election for all prior and subsequent years or merely for all subsequent years without the consent of the Commissioner.

Commenter suggested that, with respect to a product that does not satisfy the significant business presence test, the provisions of section 936(h)(1) through (4) should apply and the cost sharing payment should be reduced. The suggestion was not adopted. The provisions of section 936(h)(1) through (4) will apply with respect to the product, but the cost sharing payment required with respect to other products will not be reduced.

Commenter suggested that, in situations in which intangible property income of a subsidiary possessions corporation is included in the gross income of a parent possessions corporation, the distribution made under section 936(h)(4) should not be considered in determining whether the parent possessions corporation satisfies the gross income requirements of section 936(a)(2). The suggestion was adopted.

EXECUTIVE ORDER 12291 AND REGULATORY FLEXIBILITY ACT

The Commissioner of Internal Revenue has determined that these regulations are not major regulations as defined in Executive Order 12291 and, therefore, a regulatory impact analysis is not required. Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and, thus, the notice and public comment procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

PAPERWORK REDUCTION ACT OF 1980

The collection of information requirements contained in this regulation have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB under control number 1545–0215.

DRAFTING INFORMATION

The principal authors of this regulation are Jacob Feldman and Carol Doran Klein of the Office of Associate Chief Counsel (International), Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of substance and style.

LIST OF SUBJECTS IN 26 CFR §§1.861–1 THROUGH 1.997–1

Income taxes, Aliens, Exports, DISC, FSC, Foreign investments in U.S., Foreign tax credit, Sources of income, United States investment abroad.

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 1, and Part 602 are amended as follows:

INCOME TAX REGULATIONS

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805.***

Sections 1.936–4 through –7 also issued under 26 U.S.C. 936(h)."

Par. 2. 26 CFR Part 1 is amended by

the addition of the following new §§1.936–4 through 1.936–7 immediately after §1.936–1.

§1.936–4 Intangible property income in the absence of an election out.

The rules in this section apply for purposes of section 936(h) and also for purposes of section 934(e), where applicable.

Question 1: If a possessions corporation and its affiliates do not make an election under either the cost sharing or 50/50 profit split option, what rules will govern the treatment of income attributable to intangible property owned or leased by the possessions corporation?

Answer 1: Intangible property income will be allocated to the posssessions corporation's U.S. shareholders with the proration of income based on shareholdings. If a shareholder of the possessions corporation is a foreign person or a tax-exempt person, the possessions corporation will be taxable on that shareholder's pro rata amount of the intangible property income. If any class of the stock of a possessions corporation is regularly traded on an established securities market, then the intangible property income will be taxable to the possessions corporation rather than the corporation's U.S. shareholders. For these purposes, a United States shareholder includes any shareholder who is a United States person as described under section 7701(a)(30). The term "intangible property income" means the gross income of a possessions corporation attributable to any intangible property other than intangible property which has been licensed to such corporation since prior to 1948 and which was in use by such corporation on September 3, 1982.

Question 2: What is the source of the intangible property income described in question 1?

Answer 2: The intangible property income in U.S. source, whether taxed to U.S. shareholders or taxed to the possessions corporation. Such intangible property income, if treated as income of the possessions corporation, does not enter into the calculation of the 80-percent possession source test or the 65-percent active trade or business test of section 936(a)(2)(A) and (B).

Question 3: How will the amount of income attributable to intangible property be measured?

Answer 3: Income attributable to intangible property includes the amount received by a possessions corporation from the sale, exchange, or other disposition of any product or from the rendering of a service which is in excess of the reasonable costs it incurs in manufacturing the product or rendering the service) (other than costs incurred in connection with intangibles) plus a reasonable profit margin. A reasonable profit margin shall be computed with respect to direct and indirect costs other than (i) costs incurred in connection with intangibles, (ii) interest expense, and (iii) the cost of materials which are subject to processing or which are components in a product manufactured by the possessions corporation. Notwithstanding the above, certain taxpayers who have been permitted by the Internal Revenue Service in taxable years beginning before January 1, 1983, to use the cost-plus method of pricing without reflecting a return from intangibles, but including the cost of materials in the cost base, will not be precluded from doing so. (Sec. 3.02(3), Rev. Proc. 63–10, 1963–1 C.B. 490.) Thus, the Internal Revenue Service may continue in appropriate cases to permit such taxpayers to continue to report their income as they have been under existing procedures described in the previous sentence if it is appropriate under all the facts and circumstances and does not distort the income of the taxpayer.

Question 4: If there is no intangible property related to a product produced in whole or in part by a possessions corporation, what method may the possessions corporation use to compute its income?

Answer 4: The taxpayer may compute its income using the appropriate method as provided under section 482 and the regulations thereunder. The taxpayer may also elect the cost sharing or profit split method.

§1.936–5 Intangible property income when an election out is made: Product, business presence, and contract manufacturing.

The rules in this section apply for purposes of section 936(h) and also for purposes of section 934(e), where applicable.

(a) *Definition of product.*

Question 1: What does the term "product" mean?

Answer 1: The term "product" means an item of property which is the result of a production process. The term "product" includes component products, integrated products, and end-product forms. A component product is a product which is subject to further processing before sale to an unrelated party. A component product may be produced from other items of property, and if it is so produced, may be treated as including or not including (at the choice of the possessions corporation) one or more of such other items of property for all purposes of section 936(h)(5). An integrated product is a product which is not subject to any further processing before sale to an unrelated party and which includes all component products from which it is produced. An end-product form is a product which—

(1) Is not subject to any further processing before sale to an unrelated party;

(2) Is produced from a component product or products; and

(3) Is treated as not including certain component products for all purposes of section 936(h)(5).

A possessions corporation may treat a component product, integrated product, or end-product form as its possession product even though the final stage or stages of production occur outside the possession. Further processing includes transformation, incorporation, assembly, or packaging.

Question 2: If a possessions corporation produces both a component product and an integrated product (which by definition includes the end-product form), may the possessions corporation use the options under section 936(h)(5) to compute its income with respect to either the component product, the integrated product or the end-product form?

Answer 2: Yes. The possessions corporation may choose to treat the component product, the integrated product, or the end-product form as the product for purposes of determining whether the possessions corporation satisfies the significant business presence test. The possessions corporation must treat the same item of property as its product (the possessions product) for all purposes of section 936(h)(5) for that taxable year, including the significant business presence test under section 936(h)(5)(B)(ii), the possessions sales calculation under section 936(h)(5)(C)(i)(I), the determination of income under section 936(h)(5)(C)(i)(II), and the combined taxable income computations under section 936(h)(5)(C)(ii). Although the possessions corporation must treat the same item of property as its product for all purposes of section 936(h)(5) in a particular taxable year, its choice of the component product, integrated product or end-product form may be different from year to year. The possessions corporation must specify the possession product on a statement attached to its return (Schedule P of Form 5735). The possessions corporation may specify its choice by either listing the components that are included in the possession product or the components that are excluded from the possession product. The possession corporation must file a separate Schedule P with respect to each possession product. The possessions corporation must attach to each Schedule P detailed computations indicating how the significant business presence test is satisfied with respect to the possession product identified in that Schedule P.

QUESTION 3: A possessions corporation produces a product that is sometimes sold to unrelated parties without further processing and is sometimes sold to unrelated parties after further processing. May the possessions corporation choose to treat the same item of property as the possession product even though in some cases it is an integrated product and in some cases it is a component product?

ANSWER 3: Yes. Except as provided in questions and answers 4 and 5, the possessions corporation must designate a single possession product even though it is sometimes a component product and sometimes an integrated product.

QUESTION 4: A possessions corporation produces a product that is sometimes sold without further processing by any member of the affiliated group to unrelated parties or to related parties for their own consumption and is sometimes sold after further processing by any member of the affiliated group to unrelated parties or to related parties for their own consumption. May the possessions corporation designate two products as possession products?

ANSWER 4: The possessions corporation may designate two or more possession products. The possessions corporation must use a consistent definition of the possession product for all items of property that are sold to unrelated parties or consumed by related parties at the same stage in the production process. The significant business presence test shall apply separately to each product designated by the possessions corporation. The possessions corporation shall compute its income separately with respect to each product.

QUESTION 5: A possessions corporation produces a product in one taxable year and does not sell all of the units that it produced. In the next taxable year the possessions corporation produces a product which includes the product produced in the prior year. The possessions corporation could not have satisfied the significant business presence test with respect to the units produced the first taxable year if the larger possession product had been designated. May the possessions corporation designate two possession products in the second year?

ANSWER 5: Yes. The possessions corporation may designate two possession products. However, once a product has been designated for a particular year all sales of units produced in that year must be defined in the same manner. In addition, the taxpayer must maintain a significant business presence in a possession with respect to that product. Sales shall be deemed made first out of the current year's production. If all of the current year's production is sold and some inventory is liquidated, then the taxpayer's method of inventory accounting shall be applied to determine what year's layer of inventory is liquidated.

Example (1). A possessions corporation S, manufactures a bulk pharmaceutical in a possession. S transfers the bulk pharmaceutical to its U.S. parent, P, for encapsulation and sale by P to customers. S satisfies the significant business presence test with respect to the bulk pharmaceutical (the component product) and the combination of the bulk pharmaceutical and the capsule (the integrated product). S may use the cost sharing or profit split method to compute its income with respect to either the component product or the integrated product.

Example (2). The facts are the same as in example (1) except that S does not satisfy the significant business presence test with respect to the integrated product. S may use the cost sharing or profit split method to compute its income only with respect to the component product. However, if in a later taxable year S satisfies the significant business presence test with respect to the integrated product, then S may use the cost sharing or profit split method to compute its income with respect to that integrated product for that later taxable year.

Example (3). P, a domestic corporation, produces in bulk form in the United States the active ingredient for a pharmaceutical product. P transfers the bulk form to S, a wholly owned possessions corporation. S uses the bulk form to produce in Puerto Rico the finished dosage form drug. S transfers the drug in finished dosage form to P, which sells the drug to unrelated customers in the U.S. The direct labor costs incurred in Puerto Rico by S during its taxable year in formulating, filling and finishing the dosage form are at least 65 percent of the total direct labor costs incurred by the affiliated group in producing the bulk and finished forms during that period. S manufactures (within the meaning of section 954(d)(1)(A)) the finished dosage form. S has elected out under section 938(h)(5) under the profit split option for the drug product area (SIC 283). P and S may treat the bulk and finished dosage forms as parts of an integrated product. Since S satisifes the significant business presence requirement with respect to the integrated product, it is entitled to 50 percent of the combined taxable income on the integrated product.

Example (4). A possessions corporation, S, produces the keyboard of an electric typewriter and incorporates the keyboard with components acquired from a related corporation into finished typewriters. S does not satisfy the significant business presence test with respect to the typewriters (the integrated product). Therefore, S may use the cost sharing or profit split method to compute its income only with respect to a component product or end-product form. For taxable year 1983, S specifies on a statement attached to its return (Schedule P of Form 5735) that the possession product is the end-product form. The statement indentifies the components—for example, the keyboard structure and frame—which are included in the possession product. S's definition of the possession product will apply to all units of the electric typewriters which S produces in whole or in part in the possession and which are sold in 1983. Thus, all units of a given component incorporated into such typewriters will be treated in the same way. For example, all keyboards and all frames will be included in the possession product, and all electric drive mechanisms and rollers will be excluded from the possession product.

Example (5). Possessions corporation A produces printed circuit boards in a possession. The printed circuit boards are sold to unrelated parties. A also uses the boards to produce personal computers in the possession. A may designate two possession products: printed circuit boards and personal computers. The significant business presence test applies separately with respect to each of these products. Thus, for those printed circuit boards that are sold to unrelated parties, only the costs of the possessions corporation and other members of the affiliated group that are incurred with respect to units of the printed circuit boards which are produced in whole or in part in the possessions and sold to third parties shall be taken into account. Conversely, with respect to personal computers, only the costs incurred with respect to the personal computers shall be taken into account. This would include the costs with respect to printed circuit boards that are incorporated into personal computers but not the costs incurred with respect to printed circuit boards that are sold without further processing to unrelated parties.

Example (6). Possessions corporation S produces integrated circuits in a possession. P, an affiliate of S, produces circuit boards in the United States. P transfers the circuit boards to S. S assembles the integrated circuits and the circuit boards. S sells some of the loaded circuit boards to third parties. S retains some of the loaded circuit boards and incorporates them into central processing units. The central processing units are then sold to third parties. S may designate two possession products. S must use a consistent definition of the possession product for all units that are sold at the same stage in the production process. Thus, with respect to those units sold after assembly of the integrated circuits and the printed circuits boards, if S cannot satisfy the significant business presence test with respect to all the loaded circuit boards (the integrated product), then S must designate a lesser product, either the integrated circuit (the component product) or the loaded circuit board less the printed circuit board (the end-product form) as its possession product. With respect to the central processing units sold the same rule would apply. Thus, if S cannot satisfy the significant business presence test with respect to the entire central processing unit for all of the central processing units sold, S must designate some lesser product as its possession product.

Example (7). S is a possessions corporation. In 1985, S produced 100 units of product X. Those units were

finished into product Y in 1985 by affiliates of S. Product X is a component of product Y. In 1985, S satisfies the direct labor test with respect to product X but not with respect to product Y. S designates the component product X as its possession product. In 1986 S produces 100 units of product X and finishes those units into product Y. S would have satisfied the significant business presence test with respect to product X if S had designated product X as its possession product in 1986. In addition, in 1986 S satisfies the significant business presence test with respect to the integrated product Y. In 1986, S sells 150 units of Y. One hundred of those units would be deemed to be produced in 1986. With respect to those units S may designate the integrated product Y as its possession product. Under S's method of inventory accounting the remaining 50 units were determined to have been produced in 1985. With respect to those units S must define its possession product as it did for the taxable year in which those units were produced. Thus, S's possession product would be the component product X.

Question 6: May an affiliated group establish groupings of possession products and treat the groupings as single products?

Answer 6: An affiliated group may establish reasonable groupings of possession products based on similarities in the production processes of the possession products. Possession products that are grouped shall be treated as a single product. The determination of whether the production processes involved in producing the products that are to be grouped are similar is based on the production processes of the components that are included in the possession product. The affiliated group may establish new groupings each year. Any grouping which materially distorts a taxpayer's income or the application of the significant business presence test may be disallowed by the Commissioner. The mere fact that a grouping results in an increased allocation of income to the possessions corporation does not, of itself, create a material distortion of income. If the Commissioner determines that the taxpayer's grouping is improper with respect to one or more products in a group, then those products shall be excluded from the group. The effect of excluding a product or products from the group is that the taxpayer must demonstrate that the group without the excluded products (and each excluded product itself) satisfies the significant business presence test. If the group without the excluded products, or any of the excluded products themselves, fails to satisfy the significant business presence test, then the possessions corporation's income from those products shall be determined under section 936(h)(1) through (4) and the regulations thereunder.

Example (1). The following are examples of possession products; the processes of production of which are sufficiently similar that they may be grouped and treated as a single product:

(A) Beverage bases or concentrates for different soft drinks or soft drink syrups, regardless of whether some include sweeteners and some do not;

(B) Different styles of clothing;

(C) Different styles of shoes;

(D) Equipment which relies on gravity to deliver solutions to patients intravenously;

(E) Equipment which relies on machines to deliver solutions to patients intravenously;

(F) Video game cartridges, even though the concept and design of each game title is, in part, protected against infringement by separate copyrights;

(G) All integrated circuits;

(H) All printed circuit boards; and

(I) Hardware and software if the software is one of several alternative types of software offered by the manufacturer and sold only with the hardware, and a purchaser of the hardware would ordinarily purchase one or more of the manufacturer-provided alternative types of software. In all other cases, hardware and software may not be grouped and treated as a single product.

Groupings (D) and (E) do not include any solutions which are delivered through the equipment described therein.

Example (2). A possessions corporation produces in Puerto Rico non-programmable, interactive cathode ray tube computer terminals that vary in price. These terminals all interact with a computer or controller to perform their functions of data entry, graphics word processing, and program development. The terminals can be purchased with options that include a built-in printer, different language keyboards, specialized cathode ray tubes, and different power supply features. All terminals are produced in one integrated process requiring the same skills and operations. The differences in the production of the terminals include differences in the number of printed circuit boards incorporated in each terminal, the use of unique keyboards, and the installation and testing of the built-in printer.

Some difference in direct labor time to manufacture the terminals occurs, primarily due to the differing number and complexity of printed circuit boards incorporated into each terminal. Different model numbers are assigned to various computer terminals. A grouping by the taxpayer of all of the terminals as one product will be respected by the Service, unless the Service establishes that substantial distortion results. This grouping is proper because the processes of producing each of the terminals are similar.

Examples (3). A possessions corporation, S produces several models of serial matrix impact printers and teleprinters. These products have differing performance standards based on such factors as speed (in characters per second), numbers of columns, and cost. The production process for all types of printers involves production of three basic elements: electronic circuitry, the printing head, and the mechanical parts. The process of producing all the printers is similar. Thus, all printers could be grouped and treated as a single product. S purchases electronic circuitry and mechanical parts from a U.S. affiliate. S performs manufacturing functions relative to the printing head and assembles and tests the finished printers. S does not satisfy the significant business presence test with respect to the integrated products. S therefore specifies on a statement attached to its return (Schedule P of Form 5735) that the possession product for both the serial matrix printers and the teleprinters is the end-product form. The statement identifies the components which are included in each possession product. S may group and treat as a single product the serial matrix printers and the teleprinters if both end-product forms include and exclude similar components. Thus, if the end-product form for both the serial matrix printers and the teleprinter includes the mechanical parts and excludes the electronic circuitry, then S may group and treat a single product the two end-product forms. If, however, the end-product forms for the two items of property contain components that are not similar and as a result of this definition of the end-product forms the production processes involved in producing the two end-product forms are not similar, then S may not group the end-product forms.

Question 7: Is the affiliated group permitted to include in a group an item of property that is not produced in whole or in part in a possession?

Answer 7: No.

Example (1). Possessions corporation S produces 70 units of product A in a possession. P, an affiliate of S, produces 30 units of product A entirely in the United States. All of the units are sold to unrelated parties. The affiliated group is not permitted to group the 30 units of product A produced in the United States with the 70 units produced in the possession because those units are not produced in whole or in part in a possession.

Example (2). The facts are the same as in example (1) except that the 30 units of product A are transferred to possessions corporation S. S incorporates the 100 units of product A into product B. This incorporation takes place in the possession. S may group and treat as a single product all of the units of product B even though some of those units contain units of product A that were produced in the possession and some that were produced in the United States.

Question 8: What factors should be disregarded in determining whether a particular grouping of similar items of property is reasonable?

Answer 8: In general, differences in the following factors will be disregarded in determining whether a particular grouping of items of property is reasonable:

(1) Differences in testing requirements (*e.g.*, some products sold for military use may require more extensive or different testing than products sold for commerical use);

(2) Differences in the product specifications that are designed to accommodate the product to its area of use or for conditions under which used (*e.g.*, electrical products designed for ultimate use in the United States differ from electrical products designed for ultimate use in Europe);

(3) Differences in packaging or labeling (*e.g.*, differences in the number of units of the items shipped in one package); and

(4) Minor differences in the operations of the items of property.

Question 9: What rules apply for purposes of determining whether pharmaceutical products are properly grouped and treated as a single product?

Answer 9: The rules contained in questions and answers 6 through 8 of this section shall apply. Thus, an affiliated group may establish reasonable groupings based on similarities in the production processes of two or more possession products. In establishing a group the affiliated group may only compare the production processes involved in producing the possession products. The fact that two pharmaceutical products contain different active or inert ingredients is not relevant to the determiniation of whether the pharmaceutical products may be grouped. For example, if the possession products are bulk chemicals and the production processes involved in producing the bulk chemicals are similar, those bulk chemicals may be grouped and treated as a single product even though they contain different active or inert ingredients. The affiliated group may also group and treat as a single product the finished dosage form drug as long as the production processes involved in producing the finished dosage forms are similar. For these purposes, the production processes involved in producing the following classes of items shall be considered to be sufficiently similar that possession products delivered in a form described in one of the categories may be grouped with other possession products delivered in a form described in the same category. The categories are:

(1) Capsules, tablets, and pills;

(2) Liquids, ointments, and creams; or

(3) Injectable and intravenous preparations.

No distinctions should be based on packaging, list numbers, or size of dosage. The affiliated group may group and treat as a single product the integrated product (combination of the bulk and the delivery form) only if all the production processes involved in producing the integrated products are similar. The rules of this question and answer are illustrated by the following examples.

Example (1). Possessions corporation S produces two chemical active ingredients X and Y. Both chemical ingredients are produced through the process of fermentation. The affiliated group is permitted to group and treat as a single product the two chemical ingredients.

Example (2). The facts are the same as in example (1) and possessions corporation S finishes chemical ingredient X into tablets and chemical ingredient Y into capsules. The affiliated group is permitted to group and treat as a single product the combination of the bulk pharmaceutical and the finishing because the production processes involved in producing the integrated products are similar.

Example 3. Possessions corporation S produces in a possession a bulk chemical X by fermentation. A United States affiliate, P, produces in the United States a bulk chemical, Y, by fermentation. Both bulk chemicals are finished by S in the possession. The finished dosage form of X is in pill form. The finished dosage form of Y is in injectable form. If S's possession product is the integrated product or the end-product form then S may not group X and Y because the production processes involved in producing the finished dosage form of X and Y are not similar. If S's possession product is the component then S may not group X and Y because the bulk chemical Y is not produced in whole or in part in a possession.

Question 10: Will the fact that a manufacturer of a drug must submit a New Drug Application ("NDA") or a supplemental NDA to the Food and Drug Administration have any effect on the definition or grouping of a product?

Answer 10: No.

Question 11: A possessions corporation which produced a product or rendered a type of service in a possession on or before September 3, 1982, is not required to meet the significant business presence test in a possession with respect to such product or type of service for its taxable years beginning before January 1, 1986 (the interim period). During such interim period, how will the term "product" be defined for purposes of allocating income under the cost sharing or profit split methods?

Answer 11: During the interim period the product will be determined based on the activities performed by the possessions corporation within a possession on September 3, 1982. During the interim period the possessions corporation may compute its income under the cost sharing or profit split method only with respect to the product that is produced or manufactured within the meaning of section 954(d)(1)(A) within the possession. If the product is manufactured from a component or components produced by an affiliated corporation or a contract manufacturer, then the product will not be treated as including such component or components for purposes of the computation of income under the cost sharing or profit split methods. Thus, the possessions corporation is not entitled to any return on the intangibles associated with the component or components. Notwithstanding the preceding sentences, for taxable years beginning beforee January 1, 1986, a possessions corporation may compute its income under the cost sharing or profit split method with respect to a product which includes a component or components produced by an affiliated corporation or contract manufacturer if the possessions corporation satisfies with respect to such product the significant business presence test described in section 936(h)(5)(B)(ii) and the regulations thereunder.

Example (1). A possessions corporation, S, was manufacturing (within the meaning of section 954(d)(1)(A)) integrated circuits in a possession on September 3, 1982. S transferred those integrated circuits to related corporation P. P incorporated the integrated circuits into central processing units (CPUs in the United States) and sold the CPUs to unrelated parties. S continued to manufacture integrated circuits in the possession through January 1, 1986. For taxable years beginning before January 1, 1986. S may compute its income under the cost sharing or profit split method with respect to the integrated circuits regardless of whether S satisfies the significant business presence test. However, unless S satisfies the significant business presence test with respect to the central processing units. S may not compute its income under the cost sharing or profit split methods with respect to the CPUs, and thus, S is not entitled to any return on manufacturing intangibles associated with CPUs to the extent that they are not related to the integrated circuits produced by S, nor (except as provided in the profit split method), to any return on marketing intangibles.

Example (2). A possessions corporation, S, was engaged on September 3, 1982, in the manufacture (within the meaning of section 954(d)(1)(A)) of a bulk pharmaceutical in Puerto Rico from raw materials. S sold the bulk pharmaceutical to its U.S. parent, P, for encapsulation and sale by P to customers as the product X. Because S was not engaged in the encapsulation of X, S is not considered to have manufactured the integrated product, X, in Puerto Rico. During the interim period, S may compute its income under the cost sharing or profit split methods with respect to the integrated product, X, only if S satisfies the signfiicant business presence test with respect to X. S may compute its income under the cost sharing or profit split methods with respect to the component product (the bulk pharmaceutical).

Example (3). P is a domestic corporation that is not a possessions corporation. P manufactures a bulk pharmaceutical in the United States. P transfers the bulk pharmaceutical to its wholly owned subsidiary, S, a possessions corporation. On September 3, 1982, S was engaged in the encapsulation of the bulk pharmaceutical in Puerto Rico in a manner which satisfies the test of section 954(d)(1)(A). For taxable years beginning before January 1, 1986. S may compute its income under the cost sharing or profit split methods with respect to the end-product form (the encapsulated drug) regardless of whether S meets the significant business presence test. However, unless S satisfies the significant business presence test with respect to the integrated product, S may not compute its income under the cost sharing or profit split methods with respect to the integrated product, and thus, S is not entitled to any return on the intangibles associated with the bulk pharmaceutical.

Question 12: On September 3, 1982, a possessions corporation, S, was engaged in the manufacture (within the meaning of section 954(d)(1)(A)) of X in a possession. During the interim period, after September 3, 1982, but before January 1, 1986. S produced Y, which differs from X in terms of minor design features. S did not produce Y in a possession on September 3, 1982. Will S be considered to have commenced production of a new product after September 3, 1982, for purposes of the application of the significant business presence test for the interim period?

Answer 12: No. X and Y will be considered to be a single product, and therefore S will not be required to satisfy the business presence test separately with respect to Y during the interim period. In all cases in which the items of property produced on or before September 3, 1982 and the items of property produced after that date could have been grouped together under the guidelines provided in §1.936–5(a) questions and answers 6 through 10, the possessions corporation will not be considered to manufacture a new product after September 3, 1982.

Question 13: May the term "product" be defined differently for export sales than for domestic sales?

Answer 13: Yes. For rules concerning the application of the separate election for export sales see §1.936–7(b).

(b) *Requirement of significant business presence*—

(1) *General rules.*

Question 1: In general, a possessions corporation may compute its income under the cost sharing or profit split methods with respect to a product only if the possessions corporation has a significant business presence in a possession with respect to that product. When will a possessions corporation be considered to have a significant business presence in a possession?

Answer 1: For purposes of the cost sharing method, the significant business presence test is met if the possessions corporation satisfies either a value added test or a direct labor test. For purposes of the profit split method, the significant business presence test is met if the possessions corporation satisfies either a value added test or a direct labor test and also manufactures the product in the possession within the meaning of section 954(d)(1)(A).

Question 2: How may a possessions corporation satisfy the direct labor test with respect to a product?

Answer 2: The possessions corporation will satisfy the direct labor test with respect to a product if the direct labor costs incurred by the possessions corporation as compensation for services performed in a possession are greater than or equal to 65 percent of the direct labor costs of the affiliated group for units of the possession product produced during the taxable year in whole or in part by the possessions corporation.

Question 3: How may a possessions corporation satisfy the value added test?

Answer 3: In order to satisfy the value added test, the production costs of the possessions corporation incurred in the possession with respect to units of the possession product produced in whole or in part by the possessions corporation in the possession and sold or otherwise disposed of during the taxable year by the affiliated group to unrelated parties must be greater than or equal to twenty-five percent of the difference between gross receipts from such sales or other affiliated group for materials purchased for such units from unrelated parties.

Question 4: Must the significant business presence test be met with respect to all units of the product produced during the taxable year by the affiliated group?

Answer 4: No. The significant business presence test must be met with respect to only those units of the product produced during the taxable year in whole or in part by the possessions corporation in a possession.

Question 5: For purposes of determining whether a possessions corporation satisfies the significant business presence test, how shall the possessions corporation treat the cost of components transferred to the possessions corporation by a member of the affililated group?

Answer 5: The treatment of the cost of components transferred from an affiliate depends on whether the possession product is treated as including the components for purposes of section 936(h). If it is, then for purposes of the value added test, the production costs associated with the component shall be treated as production costs of the affiliated group that are not incurred by the possessions corporation. Those production costs, other than the cost of materials, shall not be treated as a cost of materials. For purposes of the direct labor test and the alternative significant business presence test, the direct labor costs associated with such components shall be treated as direct labor costs of the affiliated group that are not incurred by the possessions corporation. If the possession product is treated as not including such component for purposes of section 936(h), then, solely for purposes of determining whether the possessions corporation satisfies the value added test, the cost of the component shall not be treated as either a cost of materials or as a production cost. For purposes of the direct labor test and the alternative significant business presence test, the direct labor costs associated with such component shall not be treated as direct labor costs of the affiliated group. If the possession product is treated as not including such component, then the possessions corporation shall not be entitled to any return on the intangibles associated with the manufacturing or marketing of the component.

Question 6: May two or more related possessions corporations aggregate their production or direct labor costs for purposes of determining whether they satisfy the significant business presence test with respect to a single product?

Answer 6: No.

Question 7: A possessions corporation, S, purchases raw materials and components from an unrelated corporation which conducts business outside of a possession. The unrelated corporation is not a contract manufacturer. What is the treatment of such raw materials and components for purposes of the significant business presence test?

Answer 7: Where Company S purchases raw materials or components from an unrelated corporation which is not a contract manufacturer, the raw materials and components are treated as materials, and the costs related thereto are treated as a cost of materials.

(2) *Direct labor costs.*

Question 1: How is the term "direct labor costs" to be defined?

Answer 1: The term "direct labor costs" has the same meaning which it has for purposes of §1.417–11(b)(2)(i). Thus, direct labor costs include the cost of labor which can be identified or associated with particular units or groups of units of a specific product. The elements of direct labor include such items as basic compensation, overtime pay, vacation and holiday pay, sick leave pay (other than payments pursuant to a wage continuation plan under section 105(d)), shift differential, payroll taxes, and payments to a supplemental unemployment benefit plan paid or incurred on behalf of employees engaged in direct labor.

Question 2: May a taxpayer treat a cost as a direct labor cost if it is not included in inventoriable costs under section 471 and the regulations thereunder?

Answer 2: No. A cost may be treated as a direct labor cost only if it is included in inventoriable costs. However, a cost may be considered a direct labor cost even though the activity to which it relates would not constitute manufacturing under section 954(d)(1)(A) as long as the cost is included in inventoriable costs.

Question 3: May the members of the affiliated group include as direct labor costs the labor element in indirect production costs?

Answer 3: No. The labor element of indirect production costs may not be considered as part of direct labor costs.

Question 4: Do direct labor costs include the costs which can be identified or associated with particular units or groups of units of a specific product if those costs could also be described as quality control and inspection?

Answer 4: Yes. Direct labor costs include costs which can be identified or associated with particular units or groups of units of a specific product. Thus, if quality control and inspection is an integral part of the production process, then the labor associated with that quality control and inspection shall be considered direct labor. For example, integrated circuits are soldered to printed circuit boards by passing the boards over liquid solder. Employees inspect each of the boards and repair any imperfectly soldered joints discovered on that inspection. The labor associated with this process is direct labor. However, if a person performs random inspections on limited numbers of products, then that labor associated with those inspections shall be considered quality control and therefore indirect labor.

Question 5: Do direct labor costs of the possessions corporation include only the costs which were actually incurred or do they take into account, in addition, any labor savings which result because the activities were performed in a possession rather than in the United States?

Answer 5: Direct labor costs include only the costs which were actually incurred.

Question 6: For purposes of determining whether a possessions corporation satisfies the significant business presence test for a taxable year with respect to a product, how shall the possessions corporation compute its direct labor costs of units of the product?

Answer 6: The direct labor test shall be applied separately to products produced in whole or in part by the possessions corporation in the possession during each taxable year. Sales shall be deemed to be made first out of the current year's production. If sales are made only out of the current year's production, then the direct labor costs of producing those units that are sold shall be the pro rata portion of the total direct labor costs of producing all the units that are produced in whole or in part in the possession by the possessions corporation during the current year. If all of the current year's production is sold and some inventory is liquidated, then the direct labor test shall be applied separately to the current year's production and the liquidated inventory. The direct labor costs of producing the liquidated inventory shall be the pro rata portion of the total direct labor costs that were incurred in producing all the units that were produced in whole or in part by the possessions corporation in the possessions in the layer of liquidated inventory determined under the member's method of inventory accounting.

Example. S is a cash basis calendar year taxpayer that has made an election under section 936(a). In 1985 S produced 100 units of product X. Fifty percent of the direct labor costs of the affiliated group were incurred by S and were compensation for services performed in the possession. Thus, S did not satisfy the significant business presence test with respect to product X in taxable year 1985. During 1986 S produced 100 units of product X. One hundred percent of the direct labor costs of the affiliated group were incurred by S and were compensation for services performed in the possession. In 1986 S sells 150 units of product X. One hundred of those units are deemed to be from the units produced in 1986. With respect to those units S satisfies the significant business presence test. Under S's method of inventory accounting the remaining 50 units were determined to be produced in 1985. With respect to those units S does not satisfy the significant business presence test because only 50% of the direct labor costs incurred in producing those units were incurred by S and were compensation for services performed in the possession.

Question 7: What is the result if in a particular taxable year the possessions corporation satisfies the significant business presence test with respect to units of the product produced in one year and fails the significant business with respect to units produced in another year?

Answer 7: For those units of the product with respect to which the possession corporation satisfies the significant business presence test, the possessions corporation may compute its income under the provisions of section 936(h)(5). For those units of the product with respect to which the possessions corporations fails the significant business presence test, the possessions corporation must compute its income under section 936(h)(1) through (4).

Question 8: Do direct labor costs include costs incurred in a prior taxable year with respect to units of the possessions product that are finished in a later taxable year?

Answer 8: Yes.

(3) *Direct material costs.*

Question 1: How is the term "direct material costs" to be defined?

Answer 1: Direct material costs include the cost of those materials which become an integral part of the specific product and those materials which are consumed in the ordinary course of manufacturing and can be identified or associated with particular units or groups of units of the product. See §1.471–3 for the elements of direct material costs.

Question 2: May a taxpayer treat a cost as a direct material cost if it is not included in inventoriable costs under section 471 and the regulations thereunder?

Answer 2: A taxpayer may not treat such costs as direct material costs.

(4) *Production costs.*

Question 1: How is the term "production costs" defined?

Answer 1: The term "production costs" has the same meaning which it has for purposes of §1.471–11(b) except that the term does not include direct material costs and interest. Thus, production costs include direct labor costs and fixed and variable indirect production costs (other than interest).

Question 2: With respect to indirect production costs described in §1.471–11(c)(2)(ii) and (iii), may a possessions corporation include these costs in production costs for purposes of section 936, if they are not included in inventoriable costs under section 471 and the regulations thereunder?

Answer 2: No. A possessions corporation may include these costs only if they are included for purposes of section 471 and the regulations thereunder. If a possessions corporation and the other members of the affiliated group include and exclude different indirect production costs in their inventoriable costs, then, for purposes of the significant business presence test, the possessions corporation shall compute its production costs and the production costs of the other members of the affiliated group by subtracting from the production costs of each member all indirect costs included by that member that are not included in production costs by all other members of the affiliated group.

Question 3: Does a change in a taxpayer's method of accounting for purposes of section 471 affect the taxpayer's computation of production costs for purposes of section 936?

Answer 3: Yes. If a taxpayer changes its method of accounting for purposes of section 471, then the same change shall apply for purposes of section 936.

Question 4: For purposes of determining whether a possessions corporation satisfies the significant business presence test for a taxable year with respect to a product, how shall the possessions corporation compute its costs of producing units of the product sold or otherwise disposed to unrelated parties during the taxable year?

Answer 4: All members of the affiliated group may elect to use their current year production costs regardless of whether the members use the FIFO or LIFO method of inventory accounting. If some or all of the current year's production of a product is sold, then the production costs of producing those units sold shall be the pro rata portion of the total production costs of producing all the units produced in the current year. If all of the current year's production of a product is sold and some inventory is liquidated, then the production costs of producing the liquidated inventory shall be the pro rata portion of the production costs incurred in producing the layer of liquidated inventory as determined under the member's method of inventory accounting.

Question 5: How should the members of the affiliated group determine the portion of their production costs that is allocable to units of the product sold or otherwise disposed of during the taxable year?

Answer 5: The members of the affiliated group may use either standard production costs (so long as variances are not material), average production costs, or FIFO production costs to determine the production costs that will be considered to be attributable to units of the product sold or otherwise disposed of during the taxable year. However, all members of the affiliated group must use the same method.

Question 6: When is the quality control and inspection of a product considered to be part of the production activity for that product?

Answer 6: Quality control and inspection of a manufactured product before its sale or other disposition by the manufacturer, or before its incorporation into other products, is considered to be part of the indirect production activity for that initial product. Subsequent testing of a product to ensure that the product is compatible with other products is not a part of the production activity for the initial product. When a component is incorporated into an end-product form and the end-product form is then tested, the latter testing will be considered to be a part of the indirect production activity for the end-product form and will not be considered to be a part of the production activity for the component.

Question 7: For purposes of the significant business presence test and the allocation of income to a possessions corporation, what is the treatment of the cost of installation of a product?

Answer 7: For purposes of the significant business presence test and the allocation of income to a possessions corporation, product installation costs need not be taken into account as costs incurred in the manufacture of that product, if the taxpayer keeps such permanent books of account or records as are sufficient to establish the fair market price of the uninstalled product. In such a case, the cost of installation materials, the cost of the labor for installation, and a reasonable profit for installation will not be included in the costs and income associated with the possession product. If the taxpayer does not keep such permanent books of account or records, then the cost of installation materials and the cost of labor for installation shall be treated as costs associated with the possession product and income will be allocated to the possessions corporation and its affiliates under the rules provided in these regulations.

Question 8: For purposes of the significant business presence test and the allocation of income to a product or service, what is the treatment of the cost of servicing and maintaining a possession product that is sold to an unrelated party?

Answer 8: The cost of servicing and maintaining a possession product after it is sold is not associated with the production of that product.

Question 9: For purposes of the significant business presence test and the allocation of income to a possessions corporation, what is the treatment of the cost of samples?

Answer 9: The cost of producing samples will be treated as a marketing expense and not as inventoriable costs for these purposes. However, for taxable years beginning prior to January 1, 1986, the cost of producing samples may be treated as either a marketing expense or as inventoriable costs.

(5) *Gross receipts.*

Question 1: How shall the affiliated group determine gross receipts from sales or other dispositions by the affiliated group to unrelated parties of the possession product?

Answer 1: Gross receipts shall be determined in the same manner as possession sales under the rules contained in §1.936-6(a)(2).

(6) *Manufacturing within the meaning of section 954(d)(1)(A).*

Question 1: What is the test for determining, within the meaning of section 954(d)(1)(A), whether a product is manufactured or produced by a possessions corporation in a possession?

Answer 1: A product is considered to have been manufactured or produced by a possessions corporation in a possession within the meaning of section 954(d)(1)(A) and §1.954-3(a)(4) if—

(i) The property has been substantially transformed by the possessions corporation in the possession;

(ii) The operations conducted by the possessions corporation in the possession in connection with the property are substantial in nature and are generally considered to constitute the manufacture or production of property; or

(iii) The conversion costs sustained by the possession corporation in the possession, including direct labor, factory burden, testing of components before incorporation into an end product and testing of the manufactured product before sales account for 20 percent or more of the total cost of goods sold of the possessions corporation.

In no event, however, will packaging, repackaging, labeling, or minor assembly operations constitute manufacture or production of property. See particularly examples (2) and (3) of §1.954-3(a)(4)(iii).

Question 2: Does the requirement that a possession product be produced or manufactured in a possession within the meaning of section 954(d)(1)(A) apply to taxable years beginning before January 1, 1986?

Answer 2: A possessions corporation must satisfy this requirement for taxable years beginning before January 1, 1986, in the following cases:

(i) If the posssesions corporation makes a separate election under section 936(h)(5)(F)(iv)(II) with respect to export sales;

(ii) If the possessions corporation is electing as its possession product a product that is subject to the interim period rules of §1.936-5(a) question and answer (10); or

(iii) If the possessions corporation is electing as its possession product a product that is not subject to the interim period rules of §1.936-5(a) question and answer (10) and the possessions corporation computes its income under the profit split method with respect to that product.

For rules concerning products first produced in a possession after September 3, 1982, see §1.936-5(b)(7) question and answer (2).

(7) *Start-up operations.*

Question 1: With respect to products not produced (and types of services not rendered) in the possession on or before September 3, 1982, when must a possessions corporation first satisfy the 25 percent value added test or the 65 percent direct labor test?

Answer 1: A transitional period is established such that a possessions corporation engaged in start-up operations with respect to a product or service need not satisfy the 25 percent value added test or the 65 percent labor test until the third taxable year following the taxable year in which such product is first sold by the possessions corporation or such service is first rendered by the possessions corporation. During the transitional period, the applicable percentages for these tests will be as follows:

	Any year after 1982		
	1	2	3
Value added test	10	15	20
Labor test	35	45	55

Question 2: Does the requirement that a possession product be produced or manufactured in a possession within the meaning of section 954(d)(1)(A) apply to a product if the possessions corporation is engaged in start-up operations with respect to that product?

Answer 2: The possessions corporation must produce or manufacture the possessions product within the meaning of section 954(d)(1)(A) if the possessions corporation computes its income with respect to the product under the profit split method.

Question 3: When will a possessions corporation be considered to be engaged in start-up operations?

Answer 3: A possessions corporation is engaged in start-up operations if it begins operations in a possession with respect to a product or type of service after September 3, 1982. Subject to the further provisions of this answer, a possessions corporation will be considered to begin operations with respect to a product if, under the rules of §1.936-5(a) questions and answers (6) through (10), such product could not be grouped with any other item of property manufactured in whole or in part in the possessions by any member of the affiliated group in any preceding taxable year. Any improvement or other change in a possession product which does not substantially change the production process would not be deemed to create a new product. A change in the division of manufacturing activity between the possessions corporation and its affiliates with respect to an item of property will not give rise to a new product. If a possessions corporation was producing a possession product that was either a component product or an end-product form and the possessions corporation expands its operations in the same possession so that it is now producing a product that includes the earlier possession product, the possessions corporation will not be entitled to use the start-up significant business presence test unless the production costs incurred by the possessions corporation in the possession in producing a unit of its new possession product are at least double the production costs incurred by the possessions corporation in the possession in producing a unit of the earlier possession product. If any member of an affiliated group actually groups two or more items of property then, solely for the purposes of determining whether any item of property in that group is a new product, that grouping shall be respected. However, the fact that an affiliated group does not actually group two or more items of property shall be disregarded in determining whether any item of property is a new product. Notwithstanding the above, if a possessions corporation is producing a possession product in one possession and such corporation or a member of its affiliated group begins operations in a different possession, regardless of whether the items of property could be grouped, the affiliated group may treat the units of the item of property produced at the new site of operations in the different possession as a new product.

(8) *Alternative significant business presence test.*

Question 1: Will the Secretary adopt a significant business presence test other than those set forth in section 936(h)(5)(B)(ii)?

Answer 1: Yes. The following significant business presence test is adopted both for the transitional period and thereafter. A possessions corporation will have a significant business presence in a possession for a taxable year with respect to a product or type of service if—

(i) No less than 50 percent of the direct labor costs of the affiliated group for units of the product produced, in whole or in part, during the taxable year by the possessions corporation or for the type of service rendered by the possessions corporation during the taxable year are incurred by the possessions corporation as compensation for services performed in the possession; and

(ii) The direct labor costs of the possessions corporation for units of the product produced or the type of service rendered plus the base period construction costs are no less than 70 percent of the sum of such base period construction costs and the direct labor costs of the affiliated group for such units of the product produced or the type of service rendered.

Notwithstanding satisfaction of the above test, for purposes of determining whether a possessions corporation may compute its income under the profit split method, a possessions corporation will not be treated as having a signficant business presence in a possession with respect to a product unless the possessions corporation manufactures the product in the possession within the meaning of section 954(d)(1)(A).

Question 2: How is the term "base period construction costs" defined?

Answer 2: The term "base period construction costs" means the average construction costs incurred by or on behalf of the possessions corporation for services in the possession during the taxable year and the preceding four taxable years for section 1250 property (as defined in section 1250(c) and the regulations thereunder) that is used for the production of the product or the rendering of the service in the possession, and which represents the original use of the section 1250 property. For purposes of the proceeding sentence, if the possessions corporation was not in existence during one or more of the four preceding taxable years, its construction costs for that year or years shall be deemed to be zero. Construction costs include architects' and engineers' fees, labor costs, and overhead and profit (if the construction is performed by a person that is not a member of the affiliated group).

(c) *Definition and treatment of contract manufacturing.*

Question 1: For purposes of determining whether a possessions corporation satisfies the significant business presence test with respect to a product, the costs incurred by the possessions corporation or by any of its affiliates in connection with contract manufacturing which is related to that product and is performed outside the possession shall be treated as direct labor costs of the affiliated group and shall not be treated as production costs of the possessions corporation or as material costs. How is the term "contract manufacturing" to be defined?

Answer 1: The term "contract manufacturing" includes any arrangement between a possessions corporation (or another member of the affiliated group) and an unrelated person if the unrelated person:

(1) Performs work on inventory owned by a member of the affiliated group for a fee without the passage of title;

(2) Performs production activities (including manufacturing, assembling, finishing, or packaging) under the direct supervision and control of a member of the affiliated group; or

(3) Does not undertake any significant risk in manufacturing its product (*e.g.*, it is paid by the hour).

Question 2: Does an arrangement between a member of the affiliated group and an unrelated party constitute contract manufacturing if the unrelated party uses an intangible owned or licensed by a member of the affiliated group?

Answer 2: Such an arrangement will be treated as contract manufacturing if the unrelated party makes use of a patent owned or licensed by a member of the affiliated group in producing the product which becomes part of the possession product of the possessions corporation. In addition, such use of manufacturing intangibles other than patents may be treated as contract manufacturing if it is established that the arrangement has the effect of materially distorting the application of the significant business presence test. However, the preceding sentence shall not apply if the possessions corporation establishes that the arrangement was entered into for a substantial business purpose (e.g., to obtain the benefit of special expertise of the manufacturer or economies of scale). These rules shall not apply to such contract manufacturing performed in taxable years beginning before January 1, 1986, nor shall the rules apply to binding contracts for the performance of such contract manufacturing entered into before June 13, 1986.

Question 3: For purposes of the significant business presence test, how shall a possessions corporation treat the cost of contract manufacturing performed within a possession?

Answer 3: If the possessions corporation uses the value added test, it will be permitted to treat the cost of the contract manufacturing performed in a possession, not including material costs, as a production cost of the possessions corporation. If it uses the direct labor test or the alternative significant business presence test set forth in §1.936–5(b)(8), it is permitted to treat the direct labor costs of the contract manufacturer associated with such contract manufacturing as a cost of direct labor of the possessions corporation. The allowable amount of the direct labor cost shall be determined in accordance with question and answer 4 below.

Question 4: How are the amounts paid by a possessions corporation to a contract manufacturer for services rendered in a possession to be treated by the possessions corporation in computing the direct labor cost of the product to which such contract manufacturing relates?

Answer 4: If the possessions corporation can establish the contract manufacturer's direct labor cost which was incurred in the possession, such cost will be treated as incurred by the possessions corporation as compensation for services performed in the possession. If the possessions corporation cannot establish such cost, then 50 percent of the amount paid to such contract manufacturer may be treated as incurred by the possessions corporation as compensation for services performed in the possession: provided, that not more than 50 percent of the fair market value of the product manufactured by the contract manufacturer is attributable to articles shipped into the possession, and the possessions corporation receives a statement from the contract manufacturer that this test has been satisfied. If this fair market value test is not satisfied, then the cost of contract manufacturing performed within a possession shall not be treated as a production cost or a direct labor cost of either the possessions corporation or the affiliated group.

Question 5: For purposes of the significant business presence test, what is the treatment of costs which are incurred by a member of the affiliated group (including the possessions corporation) for contract manufacturing performed outside of the possession with respect to an item of property which is a component of the possession product?

Answer 5: If the possession product is treated as including such component, the cost of the contract manufacturing shall be treated as a direct labor cost of members of the affiliated group other than the possessions corporation for purposes of the direct labor test and the alternative significant business presence test, and shall not be treated as a production cost of the possessions corporation or as a cost of materials for purposes of the value added test. If the possession product is treated as not including such component, the cost of the contract manufacturing shall not be treated as a direct labor cost of any member of the affiliated group for purposes of the direct labor test and the alternative significant business presence test, and shall not be treated as a production cost of the possessions corporation or as a cost of materials for purposes of the value added test.

§1.936–6 Intangible property income when an election out is made: cost sharing and profit split options; covered intangibles.

The rules in this section apply for purposes of section 936(h) and also for purposes of section 934(e), where applicable.

(a) *Cost sharing option*—(1) *Product area research.*

Question 1: Cost sharing payments are based on research undertaken by the affiliated group in the "product area" which includes the possession product. The term "product area" is defined by reference to the three-digit classification under the Standard Industrial Classification (SIC) code. Which governmental agency has jurisdiction to decide the proper SIC category for any specific product?

Answer 1: Solely for the purpose of determining the tax consequences of operating in a possession, the Secretary of his delegate has exclusive jurisdiction to decide the proper SIC category under which a product is classified. For this purpose, the product area under which a product is classified will be determined according to the 1972 edition of the SIC code. From time to time and in appropriate cases, the

Secretary may prescribe regulations or issue rulings determining the proper SIC category under which a particular product is to be classified, and may prescribe regulations for aggregating two or more three-digit classifications of the SIC code and for classifying product areas according to a system other than under the SIC code.

Question 2: How is the term "affiliated group" defined for purposes of the cost sharing option?

Answer 2: For purposes of the cost sharing option, the term "affiliated group" means the possessions corporation and all other organizations, trades or businesses (whether or not incorporated, whether or not organized in the United States, and whether or not affiliated) owned or controlled directly or indirectly by the same interests within the meaning of section 482.

Question 3: Are research and development expenditures that are included in product area research limited to research and development expenditures that are deductible under section 174 or that are incurred by U.S. affiliates?

Answer 3: No, product area research is not limited to product area research expenditures deductible under section 174 or to expenses incurred by U.S. affiliates. Product area research also includes deductions permitted under section 168 with respect to research property which are not deductible under section 174: qualified research expenses within the meaning of section 30(b); payments (such as royalties) for the use of, or right to use, a patent, invention, formula, process, design, pattern or know-how: and a proper allowance for amounts incurred in the acquisition of manufacturing intangible property. In the case of an acquisition of depreciable or amortizable manufacturing intangible property, the annual amount of product area research shall be equal to the allowable depreciation or amortization on the intangible property for the taxable year. In the case of an acquisition of nondepreciable or nonamortizable manufacturing intangible property, the amount expended for the acquisition shall be deemed to be amortized over a five year period and included in product area research in the year of the deemed amortization. Any contingent payment made with respect to the acquisition of nonamortizable manufacturing intangible property shall be treated as amounts incurred in the acquisition of nonamortizable manufacturing intangible property when paid or accrued.

Question 4: Does royalty income from a person outside the affiliated group with respect to the manufacturing intangibles within a product area reduce the product area research pool within the same product area?

Answer 4: Yes.

Question 5: Does income received from a person outside the affiliated group from the sale of a manufacturing intangible reduce the product area research pool within the same product area?

Answer 5: In determining product area research, the income from the sale attributable to noncontingent payments will reduce product area research ratably over the remaining useful life of the property in the case of an amortizable intangible and ratably over a 5-year period in the case of anonamortizable intangible. Any income attributable to contingent amounts received with respect to the sale of manufacturing intangible property shall be treated as amounts received from the sale of the manufacturing intangible property in the year in which such contingent amounts are received or accrued.

Question 6: If a member of an affiliated group incurs research and development expenses pursuant to a contract with an unrelated person who is entitled to exclusive ownership of all the technology resulting from the expenditures, is the amount of product area research reduced by the amount of such expenditures?

Answer 6: To the extent that the product area research expenditures can be allocated solely to the technology produced for the unrelated person, such expenditures will not be included in product area research expenditures provided, however, that the unrelated person has exclusive ownership of all the technology resulting from these expenditures, and further that no member of the affiliated group has a right to use any of the technology.

Question 7: What is the treatment of product area research expenditures attributable to a component where the component and the integrated product fall within different product areas?

Answer 7: For purposes of the computation of product area research expenditures in the product area by the affiliated group, the product area in which the component falls is aggregated with the product area in which the integrated product falls. However, if the component product and integrated product are in separate SIC codes and if the component product is not included in the definition of the possession product, then the product area research expenditures are not aggregated. The same rule applies where the taxpayer elects a component product which encompasses another component product and the two component products fall into separate SIC codes. In such case, the product area in which the first component falls is aggregated with the product area in which the second component falls.

(2) *Possession sales and total sales.*

Question 1: The cost sharing payment is the same proportion of the total cost of product area research which the amount of "possession sales" of the affiliated group bears to the "total sales" of the affiliated group within the product area. How are "possession sales" defined for purposes of the cost sharing fraction?

Answer 1: The term "possession sales" means the aggregate sales or other dispositions of the possession product to persons who are not members of the affiliated group, less returns and allowances and less indirect taxes imposed on the production of the product, for the taxable year. Except as otherwise indicated in §1.936–6(a)(2), the sales price to be used is the sales price received by the affiliated group from persons who are not members of the affiliated group.

Question 2: For purposes of the numerator of the cost sharing fraction, how are possession sales computed where the possession product is a component product or an end-product form?

Answer 2: (i) The sales price of the component product or end-product form is determined as follows. With respect to a component product, an independent sales price from comparable uncontrolled transactions must be used if such price can be determined in accordance with §1.482–2(e)(2). If an independent sales price of the component product from comparable uncontrolled transactions cannot be determined, then the sales price of the component product shall be deemed to be equal to the transfer price, determined under the appropriate section 482 method, which the possessions corporation uses the cost sharing method in computing the income it derives from the active conduct of a trade or business in the possession with respect to the component product. The possessions corporation in lieu of using the transfer price determined under the preceding sentence may treat the sales price for the component product as equal to the same proportion of the third party sales price of the integrated product which the production costs attributable to the component product bear to the total production cost for the integrated product. Production cost will be the sum of direct and indirect production costs as defined in §1.936–5(b)(4). If the possessions corporation determines the sales price of the component product using the production cost ratio, the transfer price used by the possessions corporation in computing its income from the component product under the cost sharing method may not be greater than such sales price.

(ii) With respect to an end-product form, the sales price of the end-product form is equal to the difference between the third party sales price of the integrated product and the independent sales price of the excluded component(s) from comparable uncontrolled transactions, if such price can be determined under §1.482–2(e)(2). If an independent sales price of the excluded component(s) from uncontrolled transactions cannot be determined, then the sales price of the end-product form shall be deemed to be equal to the transfer price, determined under the appropriate section 482 method, which the possessions corporation uses under the cost sharing method in computing the income it derives from the active conduct of a trade or business in the possession with respect to such end-product form.

The possessions corporation in lieu of using the transfer price determined under the preceding sentence may use the production cost ratio method described above to determine the sales price of the end-product from (*i.e.*, the same proportion of the third party sales price of the integrated product which the production costs attributable to the end-product form bear to the total production costs for the integrated product). If the possessions corporation determines the sales price of the end-product form using the production cost ratio, the transfer price used by the possessions corporation in computing its income from the end-product form under the cost sharing method may not be greater than such sales price. For similar rules applicable to the profit split option see §1.936–6(b)(1), question and answer 12.

Question 3: For purposes of determining possessions sales in the numerator of the coal sharing fraction, will the replacement part price of the product be treated as a price from comparable uncontrolled transactions?

Answer 3: Prices for replacement parts are generally higher than prices for equipment sold as part of an original system. Thus, prices for replacement parts cannot generally be used directly as prices for comparable uncontrolled transactions. However, replacement part prices may be used for estimating comparable uncontrolled prices where the price differential can be reasonably determined and taken into account under §1.482–2(e)(2).

Question 4: For purposes of determining possession sales in the cost sharing fraction, what is the treatment of components that are purchased by one possessions corporation from an affiliated possessions corporation and which are incorporated into a possession product where the transferor possessions corporation treats the transferred component as a possession product?

Answer 4: When one possessions corporation purchases components from a second possessions corporation which is an affiliated corporation, the purchase price of the components paid to the second possessions corporation shall be subtracted from the sales proceeds of the product produced in the possession by the first possessions corporation, and only the remainder is included in the numerator of the cost sharing formula for the first corporation. For example, assume that N corporation manufactures a component for sale to O corporation for $100 (a price which reflects prices in comparable uncontrolled transactions). Both N and O are affiliated possessions corporations. N has designated that component product as its possession product. O then incorporates that product into a second product which is sold to customers for $300. N and O must make separate cost sharing payments. The cost sharing payment of N corporation is determined by including $100 as possession sales, and the payment of O is determined by subtracting that $100 purchase price from the $300 received from customers. Thus, the possessions sales amount of O is $200. This rule is intended to prevent the double counting of the sales of a component produced by one possessions corporation and incorporated into another product by an affiliated possessions corporation.

Question 5: Are pre-TEFRA sales included in the cost sharing fraction?

Answer 5: No. Pre-TEFRA sales are sales of products produced by the possessions corporation and transferred to an affiliate prior to a possessions corporation's first taxable year beginning after December 31, 1982. Pre-TEFRA sales are not included in either the numerator or denominator of the cost sharing fraction. If the U.S. affiliate uses the FIFO method of costing inventory, the pre-TEFRA inventory will be treated as the first inventory sold by the U.S. affiliate during the first year in which sections 936(h) applies. If the U.S. affiliate uses the LIFO method of costing inventory (either dollar-value or specific goods LIFO), pre-TEFRA inventory will be treated as inventory sold by the U.S. affiliate in the year in which the U.S. affiliate's LIFO layer containing pre-TEFRA LIFO inventory is liquidated.

Question 6: How are "possession sales" determined under the cost sharing formula if members of the affiliated group (other than the possessions corporation) include purchases of the possession product, X, in a dollar-value LIFO inventory pool (as provided under §1.472-8)?

Answer 6: Possession sales may be determined by applying the revenue identification method provided under paragraph (b)(1) Question and Answer 18 of this section.

Question 7: Do possession sales include excise taxes paid by the possessions corporation when the product is sold for ultimate use or consumption in the possession?

Answer 7: No. The amount of excise taxes is excluded from both the numerator and denominator of the cost sharing fraction.

Question 8: How are "total sales" defined for purposes of the cost sharing fraction?

Answer 8: The term "total sales" means aggregate sales or other dispositions of products in the same product area as the possession product, less returns and allowances and less indirect taxes imposed on the production of the product, for the taxable year to persons who are not members of the affiliated group. The sales price to be used is the sales price received by the affiliated group from persons who are not members of the affiliated group.

Question 9: In computing the cost sharing payment, how are "total sales" computed if the dollar-value LIFO inventory pool includes some products which are not included in the product area (determined under the 3-digit SIC code) on which the denominator of the cost sharing fraction is based?

Answer 9: In such case, the amount of the total sales within the product area to persons who are not members of the affiliated group by persons who are members of the affiliated group is determined by multiplying the total sales of the products within the dollar-value LIFO inventory pool by a fraction. The numerator of the fraction includes the dollar-value of purchases by members of the affiliated group (including the possessions corporation) of products within the product area made during the year, plus any added production costs (as defined in §1.471–11(b), (c), and (d) but not including the costs of materials) incurred by the affiliates during the same period. The denominator of the fraction includes the dollar-value of purchases by members of the affiliated group (including the possessions corporation) of products within the dollar-value LIFO inventory pool made during the same period (including any production costs, as described above, incurred by the affiliate during the same period). For these purposes, purchases of a possession product are determined on the basis of the possessions corporation's cost for its inventory purposes.

Question 10: May a possessions corporation compute its income under the cost sharing method with respect to a possession product which the possessions corporation sells to a member of its affiliated group and which that member then leases to an unrelated person or uses in its own trade or business?

Answer 10: Yes, provided that an independent sales price for the possession product from comparable uncontrolled transactions can be determined in accordance with §1.482–2(e)(2), and, provided further, that such member complies with the requirements of §1.936–6(a)(2), question and answer 14. If, however, there is a comparable uncontrolled price for an integrated product and the possession product is a component product or end-product form thereof, the possessions corporation may, if such member complies with the requirements of §1.936–6(a)(2), question and answer 14, compute its income under the cost sharing method with respect to such possession product. In that case, the cost sharing payment shall be computed under the following question and answer.

Question 11: How are possession sales and total sales to be determined for purposes of computing the cost sharing payment with respect to a possession product which the possessions corporation sells to a member of its affiliated group where that member then leases the possession product to unrelated persons or uses it in its own trade or business?

Answer 11: If the possessions corporation is entitled to compute its income from such sales of the possession product under the cost sharing method, both possession sales and total sales shall be determined as if the possession product had been sold by the affiliate to an unrelated person at the time the possession product was first leased or otherwise placed in service by the affiliate. The sales price on such deemed sale shall be equal to the independent sales price from comparable uncontrolled transactions determined in accordance with §1.482–2(e)(2), if any. If the possession product is a component product or an end-product form for which there is no such independent sales price but there is a comparable uncontrolled price for the integrated product which includes the possession product, the deemed sales price of the possession product shall be computed under the rules of §1.936–6(a)(2) question and answer 2. The full amount of income received under the lease shall be treated as income of (and taxed to) the affiliate and not the possessions corporation.

Question 12: When may a possessions corporation take into account in computing total sales under the cost sharing method products in the same product area as the possession product (other than the possession product itself) where such products are leased by members of the affiliated group to unrelated persons or used by any such member in its own trade or business?

Answer 12: For purposes of computing total sales under the cost sharing method, the possessions corporation may take into account products in the same product area as the possession product itself where such products are leased by members of the affiliated group to unrelated persons or used in the trade or business of any such member, but only if an independent sales price for such products from comparable uncontrolled transactions may be determined under §1.482–2(e)(2). In such cases, the units of such products which are leased or otherwise used internally by members of the affiliated group may be treated as sold to unrelated persons for such independent sales price for purposes of computing total sales.

Question 13: Assuming that a possessions corporation is entitled to compute its income under the cost sharing method with respect to sales of a possession product to affiliates in cases where those affiliates lease units of the possession product to unrelated persons or use them internally, is the possessions corporation's income from the possession product any different than if the affiliates had sold the product to unrelated parties?

Answer 13: No.

Question 14: If a possessions corporation sells units of a possession product to a member of its affiliated group and that affiliate then leases those units to an unrelated person or uses the units in its own trade or business, what requirements must the affiliate meet in order for the possessions corporation to be entitled to the benefits of the cost sharing method with respect to such units?

Answer 14: (i) For taxable years of the possessions corporation beginning on or before June 13, 1986, the affiliate need not meet any special requirements in order for the possessions corporation be entitled to the benefits of the cost sharing method with respect to such units. Thus, the affiliate's basis in such units shall be equal to the transfer price used for computing the possessions corporation's gross income with respect to such units under section 936(h)(5)(C)(i)(II), and the income derived by the affiliate from such lease or internal use shall be reported by the affiiate when and to the extent actually derived. The affiliate shall not be deemed to have sold such units to an unrelated party at the time they were first leased or otherwise placed in service for any purpose other than the computation of possession sales and total sales. A similar rule applies to other products in the same product area as the possession product which are sold by any member in its own trade or business and which the possessions corporation takes into account in computing total sales under the cost sharing method.

(ii) For taxable years of the possessions corporations beginning after June 13, 1986, a possessions corporations will not be entitled to the benefits of the cost sharing method with respect to units of the possession product which the possessions corporation sells to an affiliate where the affiliate then leases such units to an unrelated person or uses them in its own trade or business, unless the affiliate agrees to be treated for all tax purposes as having sold such units to an unrelated party at the time they were first leased or otherwise placed in service by such affiliate.

The affiliate must demonstrate such agreement by reporting its income from such units as if: (A) it had sold such units to an unrelated person at such time at a price equal to the price used to compute possessions sales under §1.936–6(a)(2), question and answer 11; (B) it had immediately repurchased such units for the same price; and (C) its basis in such units for all subsequent purposes was equal to its cost basis from such deemed repurchase. For treatment of other products in the same product area as the possession product see §1.936–6(a)(2), question and answer 12.

(iii) The principles contained in question and answers 11, 12, 13, and 14 are illustrated by the following example:

Example. Possessions corporation S and its affiliate A are calendar year taxpayers. In 1985, S manufactures 100 units of possession product X. S sells 50 units of X to unrelated persons in arm's length transactions for $20 per unit. In applying the cost sharing method to determine the portion of its gross income from such sales which qualifies for the possessions tax credit, S determines that $8 of the $10 sales price may be taken into account. S sells the remaining 50 units of X to A, and A then leases such units to unrelated persons. In 1985, A also manufactures 100 units of product Y, the only other product in the same product area as X manufactured or sold by any member of the affiliated group. A manufactured the 100 units of Y at a cost of $15 per unit, sold 50 units of Y to unrelated persons in arm's length transactions for $20 per unit, and leased the remaining 50 units of Y to unrelated persons.

S may compute its income under the cost sharing method with respect to the 50 units of X it sold to A because S can determine an independent sales price of X from comparable uncontrolled transactions under §1.482–2(e)(2). For purposes of computing both possessions sales and total sales, the 50 units of X sold to A will be deemed to have been sold by A to an unrelated person for $10 per unit. The income of S qualifying for the possessions tax credit from the sale of those 50 units of X to A, and A's basis in those units, will both be determined using the $8 transfer price determined under section 936(h)(5)(C)(i)(II). For purposes of computing total sales in the denominator of the cost sharing fraction, S may also take into account the 50 units of Y leased by A to unrelated persons, as if A had sold those units for $20 per unit. A's basis in those units of Y will continue to be its actual cost basis of $15 per unit.

If all of the above transactions had occurred in 1987, S would be entitled to compute its income under the cost sharing method with respect to the 50 units of X it sold to A only if A agreed to be treated for all tax purposes as if it had sold such units for $10 per unit, realized income on such deemed sale of $2 per unit, repurchased such units immediately for $10 per unit, and then leased such units, which would then have a $10 per unit basis in A's hands. For purposes of computing total sales, S would be entitled to take into account the 50 units of X leased by A to unrelated persons as if A had sold such units for $20 per unit.

(3) *Credits against cost sharing payments.*

Question 1: Is the cost of product area research paid or accrued by the possessions corporation in a taxable year creditable against the cost sharing payment?

Answer 1: Yes, if the cost of the product area research is paid or accrued solely by the possessions corporation. Thus, payments by the possessions corporation under cost sharing arrangements with, or royalties paid to, unrelated persons are so creditable. Amounts (such as royalties) paid directly or indirectly to, or on behalf of, related persons and amounts paid under any cost sharing agreements with related persons are not creditable against the cost sharing payment.

Question 2: Do royalties or other payments made by an affiliate of the possessions corporation to another member of the affiliated group reduce the cost sharing payment if such royalities or other payments are based, in part, on activity of the possessions corporation?

Answer 2: No. Payments made between affiliated corporations do not reduce the cost sharing payment. Thus, for example, if a possessions corporation sells a component to a foreign affiliate for incorporation by the foreign affiliate into an integrated product sold to unrelated persons, and the foreign affiliate pays a royalty to the U.S. parent of the possessions corporation based on the total value of the integrated product, the cost sharing payment of the possessions corporation is not reduced.

(4) *Computation of cost sharing payment.*

Question 1: S is a possessions corporation engaged in the manufacture and sale of four products (A, B, C, and D) all of which are classified under the same three-digit SIC code. S sells its production to a U.S. affiliate, P, which resells it to unrelated parties in the United States. P's third party sales of each of these products produced in whole or in part by S (computed as provided under paragraph (a)(2) of §1.936–6) are $1 million or a total of $4 million for A, B, C, and D. P's other sales of products in the same SIC code are $3,000.000; and the defined worldwide product area research of the affiliated group is $350,000. How should S compute the cost sharing amount for products A, B, C, and D?

Answer 1: The cost sharing amount is computed separately for each product on Schedule P of Form 5735. S should use the following formula for each of the products A, B, C, and D:

$$\frac{\text{Sales to unrelated persons of possession product}}{\text{Total sales of products in SIC code}} \times \text{Worldwide product area research}$$

$$\frac{\$1,000,000}{\$7,000,000} \times \$350,000 = \$50,000$$

Question 2: The facts are the same as in question 1 except that S manufactures product D under a license from an unrelated person. S pays the unrelated party an annual license fee of $20,000. Thus, the worldwide product area research expense of the affiliated group is $370,000. How should the cost sharing payment be adjusted?

Answer 2: The cost sharing fee should be reduced by the $20,000 license fee made as a direct annual payment to a third party on account of product D. The cost sharing payment with respect to product D in this example will be adjusted as follows:

$$\frac{\text{Sales to unrelated persons of possession product}}{\text{Total sales of products in SIC code}} \times \text{World-wide product area research} - \text{Amount paid by the possessions corporation to an unrelated party}$$

$$\frac{\$1,000,000}{\$7,000,000} \times \$370,000 - \$20,000 = \$32,857$$

Question 3: The facts are the same as in question 1 except that S also manufactures and exports product E to a foreign affiliate, which resells it to unrelated persons for $1 million. S makes a separate election for its export sales. How should S compute the cost sharing amount for product E?

Answer 3: The numerator of the cost sharing fraction is the aggregate sales or other dispositions by members of the affiliated group of the units of product E produced in whole or in part in the possession to persons who are not members of the affiliated group. The cost sharing amount for product E would be computed as follows:

$$\frac{\text{Export sales of E}}{\text{Total sales of products in SIC code (In this example, U.S. Sales of A, B, C, and D + export sales of E)}} \times \text{Worldwide product area research}$$

or

$$\frac{\$1{,}000{,}000}{(\$7{,}000{,}000 + \$1{,}000{,}000)} \times \$350{,}000 = \$43{,}750$$

Question 4: The facts are the same as in question 1, except that S also receives $10,000 in royalty income from unrelated persons for the licensing of certain manufacturing intangible property rights. What is the amount of the product area research that must be allocated in determining the cost sharing amount?

Answer 4: If the affiliated group receives royalty income from unrelated persons with respect to manufacturing intangibles in the same product area, then the product area research to be considered shall be first reduced by such royalty income. In this case, the amount of product area research to be used in determining S's cost sharing payment should be reduced by the $10,000 royalty payment received to $340,000.

Question 5: May a possessions corporation redetermine the amount of its required cost sharing payment after filing its tax return?

Answer 5: If after filing its tax return, a possessions corporation files an amended return, or if an adjustment is made on audit, either of which affects the amount of the cost sharing payment required, then a redetermination of the cost sharing payment must be made. See, however, section 936(h)(5)(C)(i)(III)(*a*) with respect to the increase in the cost sharing payment due to interest imposed under section 6601(a).

(5) *Effect of election under the cost sharing method.*

Question 1: What is the effect of the cost sharing method?

Answer 1: The cost sharing payment reduces the amount of deductions (and the amount of reductions in earnings and profits) otherwise allowable to the U.S. affiliates (other than tax-exempt affiliates) within the affiliated group as determined under section 936(h)(5)(C)(i)(I)(*b*) which have incurred research expenditures (as defined in §1.936-6(a)(1), question and answer 3) in the same product area for which the cost sharing option is elected, during the taxable year in which the cost sharing payment accrues. If there are no such U.S. affiliates, the reductions with respect to deductions and earnings and profits, as the case may be, are made with respect to foreign affiliates within the same affiliated group which have incurred product area research expenditures in such product area attributable to a U.S. trade or business. If there are no affiliates which have incurred research expenditures in such product area, the reductions are then made with respect to any other U.S. affiliate and, if there is no such U.S. affiliate, then to any other foreign affiliate. The allocations of these reductions in each case shall be made in proportion to the gross income of the affiliates. In the case of foreign affiliates, the allocation shall be made in proportion to gross income attributable to the U.S. trade or business or worldwide gross income, as the case may be. With respect to each group above, the reduction of deductions shall be applied first to the deductions under section 174, then to deductions under section 162, and finally to any other deductions on a pro rata basis.

Question 2: For purposes of estimated tax payments, when is the cost sharing amunt deemed to accrue?

Answer 2: The cost sharing amount is deemed to accrue to the appropriate affiliate on the last day of the taxable year of each such affiliate in which or with which the taxable year of the possessions corporation ends.

Question 3: If the cost sharing method is elected and the year of accrual of the cost sharing payment to the appropriate affiliate (described in question and answer 1 of this paragraph (a)(5)) differs from the year of actual payment by the possessions corporation, in what year are the deductions of the recipients reduced?

Answer 3: In the year the cost sharing payment has accrued.

Question 4: What is the treatment of income from intangibles under the cost sharing method?

Answer 4: Under the cost sharing method, a possessions corporation is treated as the owner, for purposes of obtaining a return thereon, of manufacturing intangibles related to a possession product. The term "manufacturing intangible" means any patent, invention, formula, process, design, pattern, or knowhow. The possessions corporation will not be treated as the owner, for purposes of obtaining a return thereon, of any manufacturing intangibles related to a component product produced by an affiliated corporation and transferred to the possessions corporation for incorporation into the possession product, except in the case that the possession product is treated as including such component product for all purposes of section 936(h)(5). Further, the possessions corporation will not be treated as the owner, for purposes of obtaining a return thereon, of any marketing intangibles except "covered intangibles." (See §1.936-6(c).)

Question 5: If the cost sharing option is elected, is it necessary for the possessions corporation to be the legal owner of the manufacturing intangibles related to the possession product in order for the possessions corporation to receive a full return with respect to such intangibles?

Answer 5: No. There is no requirement that manufacturing intangibles be owned by the possessions corporation.

Question 6: How is income attributable to marketing intangibles treated under the cost sharing method?

Answer 6: Except in the case of "covered intangibles" (see §1.936-6(c)), the possessions corporation is not treated as the owner of any marketing intangibles, and income attributable to marketing intangibles of the possessions corporation will be allocated to the possessions corporation's U.S. shareholders with the proration of income based on shareholders. If a shareholder of the possessions corporation is a foreign person or is otherwise tax exempt, the possessions corporation is taxable on that shareholder's pro rata amount of the intangible property income. If the possessions corporation is a corporation any class of the stock of which is regularly traded on an established securities market, then the income attributable to marketing intangibles will be taxable to the possessions corporation rather than the corporation's U.S. shareholders.

Question 7: What is the source of the intangible property income described in question and answer 6?

Answer 7: The intangible property income is U.S. source whether taxed to the U.S. shareholder or taxed to the possessions corporation and section 863(b) does not apply for this purpose. However, such intangible property income, if treated as income of the possessions corporation, does not enter into the calculation of the 80-percent possession source test or the 65-percent active trade or business test.

Question 8: May marketing intangible income, if any, be allocated to the possessions corporation with respect to custom-made products?

Answer 8: No. If the cost sharing option is elected, then income attributable to marketing intangibles (other than "covered intangibles" described in §1.936-6(c)) will be taxed as discussed in questions and answers 6 and 7 of paragraph (a)(5) of this section. It is immaterial whether the product is custom-made.

Question 9: In order to sell a pharmaceutical product in the United States, a New Drug Application ("NDA") for the product must be approved by the U.S. Food and Drug Administration. Is an NDA considered a manufacturing or marketing intangible for purposes of the allocation of income under the cost sharing method?

Answer 9: A manufacturing intangible.

Question 10: Can a copyright be, in whole or in part, a manufacturing intangible for purposes of the allocation of income under the cost sharing method?

Answer 10: In general, a copyright is a marketing intangible. See section 936(h)(3)(B)(ii). However, copyrights may be treated either as manufacturing intangibles or nonmanufacturing intangibles (or as partly each) depending upon the function or the use of the copyright. If the copyright is used in manufacturing, it will be treated as a manufacturing intangible; but if it is used in marketing, even if it is also classified as know-how, it will be treated as a marketing intangible.

Question 11: If the cost sharing option is elected and a patent is related to the product produced by the possessions corporation, does the return to the possessions corporation with respect to the manufacturing intangible include the make, use, and sell elements of the patent?

Answer 11: Yes. A patent confers an exclusive right for 17 years to sell a product covered by the patent. During this period, the return to the possessions corporation includes the make, use and sell elements of the patent.

Question 12: For purposes of the cost sharing option, may a safe haven rule be applied to determine the amount of marketing intangible income?

Answer 12: No. The amount of marketing intangible income is determined on the basis of all relevant facts and circumstances. The section 482 regulations will continue to apply except to the extent modified by the election. Rev. Proc. 63-10 and Rev. Proc. 66-22 do not apply for this purpose.

Question 13: If a product covered by the cost sharing election is sold by a possessions corporation to an affiliated corporation for resale to an unrelated party, may the resale price method under section 482 be used to determine the intercompany price of the possessions corporation?

Answer 13: In general, the resale price method may be used if (a) no comparable uncontrolled price for the product exists, and (b) the affiliated corporation does not add a substantial amount of value to the product by manufacturing or by the provision of services which are reflected in the sales price of the product to the customer. The possessions corporation will not be denied use of the resale price method for purposes of such intercompany pricing merely because the reseller adds more than an insubstantial amount to the value of the product by the use of intangible property.

Question 14: If a possessions corporation makes the cost sharing election and uses the cost-plus method under section 482 to determine the arm's-length price of a possession product, will the cost base include cost of materials which are subject to processing or which are components in the possession product?

Answer 14: A taxpayer may include the cost of materials in the cost base if it is appropriate under the regulations under §1.482-2(e)(4).

Question 15: If the possessions corporation computes its income with respect to a product under the cost sharing method, and the price of the product is determined under the cost-plus method under section 482, does the cost base used in computing cost-plus under section 482 include the amount of the cost sharing payment?

Answer 15: The amount of the cost sharing payment is included in the cost base. However, no profit with respect to the cost sharing payment will be allowed.

Question 16: If a member of the affiliated group transfers to a possessions corporation a component which is incorporated into a possession product, how will the transfer price for the component be determined?

Answer 16: The transfer price for the component will be determined under section 482, and as follows. If the possession product is treated as not including such component for purposes of section 936(h)(5), the transfer price paid for the component will include a return on all intangibles related to the component product. If the possession product is treated as including such component for purposes of section 936(h)(5), then the transfer price paid for the component by the possessions corporation will not include a return on any manufacturing intangible related to the component product, and the possessions corporation will obtain the return on the manufacturing intangibles associated with the component.

Question 17: If the possessions corporation computes its income with respect to a product under the cost sharing method, with respect to which units of the product shall the possessions corporation be treated as owning intangible property as a result of having made the cost sharing election?

Answer 17: The possessions corporation shall not be treated as owning intangible property, as a result of having made the cost sharing election, with respect to any units of a possession product which were not taken into account by the possessions corporation in applying the significant business presence test for the current taxable year or for any prior taxable year in which the possessions corporation also had a significant business presence in the possession with respect to such product.

(b) *Profit split option*—(1) *Computation of combined taxable income.*

Question 1: In determining combined taxable income from sales of a possession product, how are the allocations and apportionments of expenses, losses, and other deductions to be determined?

Answer 1: (i) Expenses, losses, and other deductions are to be allocated and apportioned on a "fully-loaded" basis under §1.861-8 to the combined gross income of the possessions corporation and other members of the affiliated group (other than foreign affiliates). For purposes of the profit split option, the term "affiliated group" is defined the same as under §1.936-6(a)(1) question and answer 2. The amount of research, development, and experimental expenses allocated and apportioned to combined gross income is to be determined under §1.861-8(e)(3). The amount of research, development and experimental expenses and related deductions (such as royalties paid or accrued with respect to manufacturing intangibles by the possessions corporation or other domestic members of the affiliated group to unrelated persons or to foreign affiliates) allocated and apportioned to combined gross income shall in no event be less than the amount of the cost sharing payment that would have been required under the rules set forth in section 936(h)(5)(C)(i)(II) and paragraph (a) of this section if the cost sharing option had been elected. Other expenses which are subject to §1.861–8(e) are to be allocated and apportioned in accordance with that section. For example, interest expense (including payments made with respect to bonds issued by the Puerto Rican Industrial, Medical and Environmental Control Facilities Authority (AFICA)) is to be allocated and apportioned under §1.861–8(e)(2). With the exception of marketing and distribution expenses discussed below, the other remaining expenses which are definitely related to a class of gross income shall be allocated to that class of gross income and shall be apportioned on the basis of any reasonable method, as described in §1.861–8(b)(3) and (c)(1). Examples of such methods may include, but are not limited to, those specified in §1.861–8(c)(1)(i) through (vi).

(ii) The class of gross income to which marketing and distribution expenses relate and shall be allocated is generally to be defined by the same "product area" as is determined for the relevant research, development, and experimental expenses (*i.e.*, the appropriate 3-digit SIC code), but shall include only gross income generated or reasonably expected to be generated from the geographic area or areas to which the expenses relate. It shall be presumed that marketing and distribution expenses relate to all product sales within the same product area. If, however, it can be established that any of these expenses are separately identifiable expenses, such as advertising, and relate, directly or indirectly, solely to a specific product or a specific group of products, such expenses shall be allocated to the class of gross income defined by the specific product or group of products. Thus, advertising and other separately identifiable marketing expenses which relate specifically and exclusively to a particular product must be allocated entirely to the gross income from that product, even though the taxpayer or other members of an affiliated group which includes the taxpayer produce and market other products in the same 3-digit SIC code classification. The mere display of a company logo or mention of a company name solely in the context of identifying the manufacturer shall not prevent an advertisement from relating specifically and exclusively to a particular product or group of products.

(iii) If marketing and distribution expenses are allocated to a class of gross income which consists both of income from sales of possession products (the statutory grouping) and other income such as from sales by U.S. affiliates of products not produced in the possession (the residual grouping), then these marketing and distribution expenses shall be apportioned on a "fully loaded" basis which reflects, to a reasonably close extent, the factual relationship between these deductions and the statutory and residual groupings of gross income. Apportionment methods based upon comparisons of amounts incurred before ultimate sale of a product (including apportionment on a comparison of costs of goods sold, other expenses incurred, or other comparisons set forth in §1.861–8(c)(1)(v), such as time spent) are not on a "fully-loaded" basis and do not reflect this required factual relationship. These deductions shall be apportioned on a basis of comparison of the amount of gross sales or receipts or another method if it is established that such method similarly reflects the required factual relationship. Thus, for example, a comparison of units sold may be used only where the units are of the same or similar value and are, thus, in fact comparable.

(iv) The rules for allocation and apportionment of marketing and distribution expenses may be illustrated by the following examples:

Example (1). Assume that possessions corporation A manufactures prescription pharmaceutical product #1 for resale by P, its U.S. parent corporation, in the United States. Additionally, assume that P manufactures prescription pharmaceutical products #2 and #3 in the United States for sale there. Further, assume that all three products are within the same product area, and that marketing and distribution expenses are internally divided by P among the three products on the basis of time spent by sales persons of P on marketing of the three products, as follows:

Product #1— 50X
Product #2— 80X
Product #3—110X
Total—240X

These expenses of 240X are allocated to gross income generated by all three products and shall be apportioned on the basis of gross sales or receipts of product #1 as compared to products #2 and #3 or another method which similarly reflects the factual relationship between these expenses and gross income derived from product #1 and products #2 and #3. Thus, if a sales method were used and sales of product #1 accounted for one-third of sales receipts from the three products, 80X (240 ÷ 3) of marketing and distribution expenses would be apportioned to the combined gross income from product #1.

Example (2). Corporation B produces and sells Brand W whiskey, in the United States. B's subsidiary, S, which is a possessions corporation, produces soft drink extract in Puerto Rico which it sells to independent bottlers to produce Brand S soft drinks for sale in the United States. Corporation B's advertisements and other promotional materials for Brand W whiskey make no reference to Brand S soft drinks (or any other Corporation B products), and Brand S soft drink advertisements and other promotional materials make no reference to Brand W whiskey (or any other corporation B products). For purposes of section 936(h), the advertising and other promotional expenses for Brand W whiskey must be allocated entirely to the gross income from sales of Brand W whiskey and the advertising and other promotional expenses for Brand S soft drink must be allocated entirely to the gross income from the sales of soft drink extract, notwithstanding the fact that whiskey and soft drink extract are both included in SIC code 208. A similar result would apply, for example, to separately identifiable advertising and other marketing expenses which relate specifically and exclusively to one or the other of the following pairs of products: chewing gum and granulated sugar (SIC code 206); canned tuna fish and freeze-dried coffee (SIC code 209); children's underwear and ladies' brassieres (SIC code 234); aspirin tablets and prescription antibiotic tablets (SIC code 283); floor wax and perfume (SIC code 284); adhesives and inks (SIC code 289); semiconductors and cathode-ray tubes (SIC code 367); batteries and extension cords (SIC code 369); bandages and dental supplies (SIC code 384); stainless steel flatware and jewelry parts (SIC code 391); children's toys and sporting goods (SIC code 394); hair curlers and zippers (SIC code 396); and paint brushes and linoleum tiles (SIC code 399).

Example (3). Assume the same facts as in Example (1) and that possessions corporation A also manufactures aspirin, a non-prescription product, for resale by its U.S. parent corporation, P. Further, assume that the advertising and separately identifiable marketing expenses which relate specifically and exclusively to aspirin sales total $100 and that these expenses are allocable solely to gross income derived from aspirin sales. The sales method continues to be used to apportion the marketing and distribution expenses related, directly or indirectly, to products #1, #2, and #3, and the apportionment of such expenses to product #1 for purposes of determining combined taxable income from product #1 will remain as stated in Example (1). None of the advertising and other separately identifiable marketing expenses which relate specifically and exclusively to aspirin will be taken into account in allocating and apportioning the marketing and distribution expenses relating to the gross income attributable to products #1, #2, and #3. Gross income attributable to aspirin will be considered as a separate class of gross income, and all the advertising and separately identifiable marketing expenses which relate specifically and exculsively to aspirin sales of $100 will be allocated to the class of gross income derived from aspirin sales. Similarly, none of the marketing and distribution expenses, directly or indirectly, related solely to the group of products #1, #2, and #3 will be taken into account in determining the combined taxable income from aspirin sales. The remaining marketing and distribution expenses which do not, directly or indirectly, relate solely to any specific product or group of products (*e.g.*, the salaries of a Vice-President of Marketing who has responsibility for marketing all products and his staff) shall be allocated and apportioned on the basis of the gross receipts from the sales of all of the products (or a similar method) in determining combined taxable income of any product.

Question 2: How may the allocation and apportionment of expenses to combined gross income be verified?

Answer 2: Substantiation of the allocation and apportionment of expenses will be required upon audit of the possessions corporation and affiliates. Detailed substantiation may be necessary, particularly where the entities are engaged in multiple lines of business involving distinct product areas. Sources of substantiation may include certified financial reports. Form 10-K's, annual reports, internal production reports, product line assembly work papers, and other relevant materials. In this regard, see §1.861–8(f)(5).

Question 3: Does section 936(h) override the moratorium provided by section 223 of the Economic Recovery Tax Act of 1981 and any subsequent similar moratorium?

Answer 3: Yes. Thus, the allocation and apportionment of product area research described in question and answer 1 must be made without regard to the moratorium.

Question 4: Is the cost of samples treated as a marketing expense?

Answer 4: Yes. The cost of producing samples will be treated as a marketing expense and not as inventoriable costs for purposes of determining combined taxable income (and compliance with the significant business presence test). However, for taxable years beginning prior to January 1, 1986, the cost of producing samples may be treated as either a marketing expense or as inventoriable costs.

Question 5: If a possessions corporation uses the profit split method to determine its taxable income from sales of a product, how does it determine its gross income for purposes of the 80-percent possession source test and the 85-percent active trade or business test of section 936(a)(2)?

Answer 5: One-half of the deductions of the affiliated group (other than foreign affiliates) which are used in determining the combined taxable income from sales of the product are added to the portion of the combined taxable income allocated to the possessions corporation in order to determine the possessions corporation's gross income from sales of such product.

Question 6: How will income from intangibles related to a possession product be treated under the profit split method?

Answer 6: Combined taxable income of the possessions corporation and affiliates from the sale of the possession product will include income attributable to all intangibles, including both manufacturing and marketing intangibles, associated with the product.

Question 7: Can a possessions corporation apply the profit split option to a possession product if no U.S. affiliates derive income from the sale of the possession product?

Answer 7: Yes.

Question 8: With respect to the factual situation discussed in question and answer 7, how is combined taxable income computed?

Answer 8: The profit split option is applied to the taxable income of the possessions corporation from sales of the possession product to foreign affiliates and unrelated persons. Fifty percent of that income is allocated to the possessions corporation, and the remainder is allocated to the appropriate affiliates as described in question and answer 13 of this paragraph (b)(1).

Question 9: May a possessions corporation compute its income under the profit split method with respect to units of a possession product which it sells to a U.S. affiliate if the U.S. affiliate leases such units to unrelated persons or to foreign affiliates or uses such units in its own trade or business?

Answer 9: Yes, provided that an independent sales price for the possession product from comparable uncontrolled transactions can be determined in accordance with §1.482–2(e)(2). If, however, there is a comparable uncontrolled price for an integrated product and the possession product is a component product or end-product from thereof, the possessions corporation may compute its income under the profit split method with respect to such units. In either case, the possessions corporation shall compute combined taxable income with respect to such units under the following question and answer.

Question 10: If a possessions corporation is entitled to use the profit split method in the situation described in Question 9, how should it compute combined taxable income with respect to such units?

Answer 10: Combined taxable income shall be computed as if the U.S. affiliate had sold the units to an unrelated person (or to a foreign affiliate) at the time the units were first leased or otherwise placed in service by the U.S. affiliate. The sales price on such deemed sale shall be equal to the independent sales price from comparable uncontrolled transactions determined in accordance with §1.482–2(e)(2), if any. If the possession product is a component product or an end-product form for which there is no such independent sales price but there is a comparable uncontrolled price for the integrated product which includes the possession product, the deemed sales price of the possession product shall be computed under the rules of §1.936–6(b)(1) question and answer 12. The full amount of income received under the lease shall be treated as income of (and taxed to) the U.S. affiliate and not the possessions corporation.

Question 11: In the situation described in question 9, how does the U.S. affiliate determine its basis in such units for purposes of computing depreciation and similar items?

Answer 11: The U.S. affiliate shall be treated, for purposes of computing its basis in such units, as if it had repurchased such units immediately following the deemed sales described in question 10, at the same independent sales price, or other price computed with respect to a component product or end-product form referred to in that question.

The principles of questions and answers 10 and 11 are illustrated by the following example.

Example: Possessions corporation S manufactures 100 units of possession product X. S sells 50 units of X to an unrelated person in an arm's length transaction for $10 per unit. S sells the remaining 50 units to its U.S. affiliate, A, which leases such units to unrelated persons. The combined taxable income for the 100 units of X is computed below on the basis of the given production, sales, and cost data:

Sales	
1. Total sales by S to unrelated persons (50 × $10)	$ 500
2. Total deemed sales by A to unrelated persons (50 × $10)	500
3. Total gross receipts (line 1 plus line 2)	1,000
Total Costs	
4. Material Costs	200
5. Production costs	300
6. Research expenses	0
7. Other expenses	100
8. Total (add lines 4 through 7)	600
Combined taxable income attributable to the 100 units of X:	
9. Combined taxable income (line 3 minus line 8)	400
10. Share of combined taxable income apportioned to S (50% of line 9)	200
11. Share of combined taxable income apportioned to A (line 9 minus line 10)	200
A's basis in 50 units of X leased by it to unrelated persons:	
12. 50 units times $10 deemed repurchase price	500

*Subsequent leasing income is entirely taxed to A.

Question 12: If the possession product is a component product or an end-product form, how is the combined taxable income for such product to be determined?

Answer 12: (i) In computing combined taxable income, the sales price of the component product or end-product form is determined as follows. With respect to a component product, an independent sales price from comparable uncontrolled transactions must be used if such price can be determined in accordance with §1.482-2(e)(2). If an independent sales price of the component product from comparable uncontrolled transactions cannot be determined, then the possessions corporation must treat the sales price for the component product as equal to the same proportion of the third party sales price of the integrated product which the production costs attributable to the component product bear to the total production costs for the integrated product. Production costs will be the sum of direct and indirect production costs as defined in §1.936-5(b)(4).

(ii) With respect to an end-product form, the sales price of the end-product form is equal to the difference between the third party sales price of the integrated product and the independent sales price of the excluded component(s), from comparable uncontrolled transactions, if such price can be determined under §1.482-2(e)(2). If an independent sales price of the excluded component(s) from uncontrolled transactions cannot be determined, then the possessions corporation must use the production cost ratio method described above to determine the sales price of the excluded component(s) (*i.e.*, the same proportion of the third party sales price of the integrated product which the production costs attributable to the excluded component(s) bear to the total production costs for the integrated product). If the production cost ratio is used, the sales price of the end-product form is the difference between the third party sales price of the integrated product and the sales price of the excluded component(s) determined using the production cost ratio. The possessions corporation will determine its costs (other than costs incurred for materials purchased from a U.S. affiliate) attributable to the possession product and its expenses allocable and apportionable to the possession product under §1.861-8, as described in question and answer 1 of this paragraph (b)(1).

Each member of the affiliated group that is a United States person, other than the possessions corporation, shall determine its costs (other than costs incurred for materials purchased from a U.S. affiliate) attributable to the possession product, and its expenses allocable and apportionable to the integrated product under §1.861-8, as described in question and answer 1 of this paragraph (b)(1). Each such United States person (other than the possessions corporation) shall apportion to the possession product, on the basis of the ratio of the production costs for the possession product to the total production costs for the integrated product, the expenses that such affiliate allocated and apportioned to the integrated product. Production costs will be the sum of direct and indirect production costs as defined in question and answer 1 of §1.936-5(b)(4).

Example: A possessions corporation, S, is engaged in the manufacture of microprocessors. S obtains a component from a U.S. affiliate, O. S sells its production to another U.S. affiliate, P, which incorporates the microprocessors into central processing units (CPUs). P transfers the CPUs to a U.S. affiliate, Q, which incorporates them into computers for sale to unrelated customers. S chooses to define the possession product as the CPUs. The combined taxable income for the CPUs is computed below on the basis of the given production, sales, and cost data:

Production costs (excluding costs of materials):	
1. O's costs for the component	75
2. S's costs for the microprocessors	400
3. P's costs for the CPUs	125
4. Q's costs for the computers	150
5. Total (add lines 1 through 4)	750
6. Combined production costs for the CPUs (add lines 1 through 3)	600
7. Ratio of production costs for the CPUs (the possession product) to the production costs for the computers (the integrated product)	0.8
Sales:	
8. Total sales by O to unrelated customers and foreign affiliates of computers containing microprocessors produced by S	5,000
9. Sales value of the CPUs (determined under the comparable uncontrolled price method of §1.936-6(a)(2) question and answer 2)	4,200
Total costs of S (excluding costs of materials obtained from U.S. affiliates):	
10. Production costs of S (enter from line 2)	400
11. Materials costs (excluding materials obtained from U.S. affiliates)	100
12. General and administrative expenses	250
13. Other expenses interest, etc.	250
14. Total (add lines 10 through 13)	1,000
Research expenses of the affiliated group allocable and apportionable to the CPUs:	
15. Total sales in the 3-digit SIC code	8,000
16. Possession sales (enter from line 9)	4,200
17. Cost sharing fraction (divided line 16 by line 15)	0.525
18. Research expenses incurred by the affiliated group in the 3-digit SIC code	600
19. Cost sharing amount (multiply line 17 by line 18)	315
20. Research of the affiliated group (other than foreign affilates) allocable and apportionable under §1.861-8(e)(3) to the computers (the integrated product)	350
21. Research apportionable to the CPUs (multiply line 20 by line 7)	280
22. Enter the greater of line 19 or line 21	315
Other expenses of the affiliated group (other than S and foreign affilates) allocable or apportionable to the CPUs:	
23. Marketing general and administrative, interest and other expenses of the affiliated group (other than S and foreign affiliates) which are allocable and apportionable to the computers or to any components thereof	500
24. Expenses apportionable to the CPUs (multiply line 23 by line 7)	400
Combined taxable income attributable to the CPUs:	
25. Combined taxable income (line 9 minus lines 1, 3, 14, 22 and 24)	2,285
26. Share of combined taxable income apportioned to S (50% of line 25)	1,142.5
27. Adjustment to research expense (Enter the greater of zero or line 19 minus line 21)	35
28. Adjusted combined taxable income (line 27 plus line 25)	2,320
29. Share of combined taxable income apportioned to U.S. affiliates of S (line 28 less line 26)	1,177.5

Question 13: If the profit split option is elected, how is the portion of combined taxable income not allocated to the possessions corporation to be treated?

Answer 13: The income shall be allocated (i) to U.S. affiliates (other tax exempt affiliates) within the group (as determined under section 482) which derive income with respect to the product produced in whole or in part in the possession; or (ii) if there are no such U.S. affiliates, to U.S. affiliates (other than tax-exempt affiliates) which derive income from the active conduct of a trade or business in the same product area as the possession product; or (iii) if there are no such affiliates as described in (i) or (ii) above, then to other U.S. affiliates (other than tax-exempt affiliates); or (iv) if there are no U.S. affiliates (other than tax-exempt affiliates), to foreign affiliates which derive from the active conduct of a U.S. trade or business in the same product area as the possesion product (or, if the foreign members are resident in a country with which the U.S. has an income tax convention, then to those foreign members which have a permanent establishment in the United States which derives income in the same area as the possession product); or (v) if there are no affiliates described in (i) through (iv) above, then to all other affiliates. The allocations made under (i) shall be made on the basis of the relative gross income derived by each such affiliate with respect to the product produced in whole or in part in the possession, the allocations made under (ii) and (iv) above shall be made on the basis of the relative gross income derived by each such affiliate from the active conduct of the trade or business in the same product area, and allocations made under (iii) and (v) above shall be made on the basis of the relative total gross income of each such affiliate before allocating income under this section. Income allocated to affiliates shall be treated as U.S. source and section 863 (b) does not apply for this purpose. For purposes of determining an affiliate's estimated tax liability with respect to income thus allocated, the income shall be deemed to be received on the last day of the taxable year of each such affiliate in which or with which the taxable year of the possessions corporation ends.

Question 14: What is the source of the portion of combined taxable income allocated to the possessions corporations?

Answer 14: Income allocated to the possessions corporation shall be treated as possession source income and as derived from the active conduct of a trade or business within the possession.

Question 15: How is the profit split option to be applied to properly account for costs incurred in a year with respect to products which are sold by the possessions corporation to a U.S. affiliate during such year, but are not resold by the U.S. affiliate to persons who are not members of the affiliated group or to foreign affiliates until a later year?

Answer 15: The rules under §1.994–1(c)(5) are to be applied. Incomplete transactions will not be taken into consideration in computing combined taxable income. Thus, for example, if in 1983, A, a possessions corporation, sells units of a product with a cost to A of $5000 to B corporation, its U.S. affiliate, which uses the dollar-value LIFO method of costing inventory, and B sells units with a cost of $4000 (representing A's cost) to C corporation, a foreign affiliate, only $4000 of such costs shall be taken into consideration in computing the combined taxable income of the possessions corporation and U.S. affiliates for 1983. If a specific goods LIFO inventory method is used by B, the determination of whether A's goods remain in B's inventory shall be based on whether B's specific goods LIFO grouping has experienced an increment or decrement for the year on the specific LIFO cost of such units, rather than on an average unit cost of such units. If the FIFO method of costing inventory is used by B, transfers may be based on the cost of the specific units transferred or on the average unit production cost of the units transferred, but in each case a FIFO flow assumption shall be used to identify the units transferred. For a determination of which goods are sold by taxpayers using the LIFO method, see question and answer 19.

Question 16: If a possessions corporation purchases materials from an affiliate and computes combined taxable income for a possession product which includes such materials, how are those materials to be treated in the possessions corporation's inventory?

Answer 16: The cost of those materials is considered to be equal to the affiliate's cost using the affiliate's method of costing inventory.

Question 17: If the possessions corporation uses the FIFO method of costing inventory and the U.S. affiliate uses the LIFO method of costing inventory, or *vice versa*, what method of costing inventory should be used in computing combined taxable income?

Answer 17: The transferor corporation's method of costing inventory determines the cost of inventory for purposes of combined taxable income while the transferee corporation's method of costing inventory determines the flow. Assume, for example, that X corporation, a possessions corporation, using the FIFO method of costing inventory purchases materials from Y corporation, a U.S. affiliated, also using the FIFO method. X corporation produces a product which it transfers to Z corporation, another U.S. affiliate using the LIFO method. Assume also that the final product satisfies the significant business presence test. Under these facts, the cost of the materials purchased by X from Y is Y's FIFO cost. The costs of the inventory transferred by X to Z are determined under X's FIFO method of accounting as is the flow of the inventory from X to Z. The costs added by Z are determined under Z's LIFO method of inventory, as is the flow of the inventory from Z to unrelated persons or foreign affiliates.

Question 18: How are the costs of a possession product and the revenues derived from the sale of a possession product determined if the U.S. affiliate includes purchases of the possession product in a dollar-value LIFO inventory pool (as provided under §1.472–8)?

Answer 18: The following method will be accepted in determining the revenues derived from the sale of a possession product and the costs of a possession product if the U.S. affiliate includes purchases of the possession product in a dollar-value LIFO inventory pool. The rules apply solely for the cost sharing and profit split options under section 936(h).

(i) *Revenue Identification:* The identification of revenues derived from sales of a possession product must generally be made on a specific identification basis. The particular method employed by a taxpayer for valuing its inventory will have no impact on the determination of what units are sold or how much revenue is derived from such sales. Thus, if a U.S. affiliate sells both item A (a possession product) and item B (a non-possession product), the actual sales revenues received by the U.S. affiliate from item A sales would constitute possession product revenue for purposes of the profit split option and possession sales for purposes of the cost sharing option regardless of whether the U.S. affiliate values its inventories on the FIFO or the LIFO method. In instances where sales of item A (*i.e.*, the possession product) cannot be determined by use of specific identification (for example, in cases where items A and B are identical except that one is produced in the possession (item A) and the other (item B) is produced outside of the possession and it is not possible to segregate these items in the hands of the U.S. affiliate), it will be necessary to identify the portion of the combined sales of items A and B (which together can be identified on a specific identification basis) which is attributed to item A sales and the portion which is attributed to item B sales. The determination of the portion of aggregated sales attributable to item A and item B is independent of the LIFO method used to determine the cost of such

sales and may be made under the following approach. A taxpayer may, for purposes of this section of the regulations, use the relative purchases (in units) of items A and B by the U.S. affiliate purchases (in units) of items A and B by the U.S. affiliate during the taxable year (or other appropriate measuring period such as the period during the taxable year used to determine current-year costs, *i.e.*, earliest acquisitions period, latest acqusitions period, etc.) in determining the ratio to apply against the combined items A and B sales revenue. If the sales exceed current purchases, the taxpayer can use a FIFO unit approach which identifies actual unit sales on a first-in, first-out basis. Revenue determination where specific identification is not possible is illustrated by the following example:

Example. **At the end of year 1, there are 600 units of combined items A and B which are to be allocated between A and B on the basis of annual purchases of A and B units during year 1. During year 1, 1,000 units of item A, a possession product, and 2,000 units of item B, a non-possession product, were purchased. Thus, the 600 units in year 1 ending inventory are allocated 200 (i.e. 1/3) to item A units and 400 (i.e. 2/3) to item B units based on the relative purchases of A (1,000) and B (2,000) in year 1. These units appear as beginning inventory in year 2.**

In year 2, 1,500 units of item A are purchased and 1,500 units of item B are purchased. However, 3,300 units of items A and B in the aggregate are sold for $600,000. The relative proportion of the $600,000 attributable to item A and to item B sales would be determined as follows:

Year 2 sales	***Item A***	***Item B***
Unit sales from Opening inventory	**200**	**400**
Unit sales from Current-year purchases	**1,350**	**1,350**
Total unit sales	**1,550**	**1,750 = 3,300**
Percentage	**47%**	**53%**

Revenues from item A sales $281,818 $(\$600{,}000 \times \frac{1550}{3300})$

Revenues from item B sales $318,182 $(\$600{,}000 \times \frac{1750}{3300})$

Year 2 Closing Inventory	***Units***
Item A	**150**
Item B	**150**

Thus, revenues from Item A sales for purposes of computing possession sales for the cost sharing option and revenues for the profit split option are $281,818.

(ii) *Cost Identification:* The determination of the cost of possession product sales by the U.S. affiliate must be based on the LIFO inventory method of the U.S. affiliate. The LIFO cost of possession product sales will, for purposes of this section of the regulations, be determined by maintaining a separate LIFO cost for possession products in a taxpayer's opening and closing LIFO inventory and using this cost to calculate an independent cost of possession product sales. This separate LIFO cost for possession products in the LIFO pool of a taxpayer is to be determined as follows:

(A) Determine the base-year cost of possession products in ending inventory in a LIFO pool.

(B) Determine the percentage of the base-year cost of possession products in the pool as compared to the total base-year cost of all items in the pool.

(C) Multiply the percentage determined in step (B) above by the ending LIFO inventory value of the pool to determine the deemed LIFO cost attributable to possession products in the pool.

Example: **Assume that item A is a possession product and item B is a non-possession product and also assume the inventory and purchases with respect to the LIFO pool as provided below:**

The year 2 LIFO cost of possession product A sales will be calculated as follows:

Year 1 Ending Inventory

	Number of Units	***Base-Year Cost/Unit***	***Base-Year Cost***	***%***
Item A	**100**	**$2.00**	**$200**	**20%**
Item B	**200**	**4.00**	**800**	**80%**

Year 1—LIFO Value

	Base-Year Cost	***Index***	***LIFO Cost***
Increment Layer 2	**$ 300**	**3.0**	**$ 900**
Increment Layer 1	**400**	**2.0**	**800**
Base layer	**300**	**1.0**	**300**
Pool total	**$1,000**		**$2,000**

Year 1—LIFO Value Per Item

	Base-Year Cost	***LIFO Value***
Total Pool	**$1,000**	**$2,000**
Item A	**200**	**400**
Item B	**800**	**1,600**

Year 2—Purchases

	Total Purchases
Item A	**$6,000**
Item B	**4,000**

Year 2—Ending Inventory

	Number of Units	***Base-Year Cost/Unit***	***Base-Year Cost***	***%***
Item A	**200**	**$2.00**	**$400**	**50%**
Item B	**100**	**4.00**	**400**	**50%**

Year 2—LIFO Value

	Base-Year Cost	***Index***	***LIFO Cost***
Increment layer 2	**$100**	**3.0**	**$ 300**
Increment layer 1	**400**	**2.0**	**800**
Base layer	**300**	**1.0**	**300**
Pool total	**$800**		**$1,400**

(1) Base-year cost of item in year 2 ending inventory = $400

(2) Percentage of item A base-year cost to total base-year cost ($400 + $800) = 50%

(3) LIFO value of item A ($1,400 × 50%) = $700

(4) LIFO cost of item A sales is determined by adding to the beginning inventory in year 2 the purchases of item A in year 2 and subtracting from this amount the ending inventory in year 2 ($400 + $6000 − $700 = $5700). The beginning inventory in year 2 is determined by multiplying the LIFO cost of the year 1 ending inventory by a percentage of item A base-year cost to the total base-year cost in year 1. The ending inventory in year 2 is determined under (3) above.

Question 19: **If a possession product is purchased from a possessions corporation by a U.S. affiliate using the dollar-value LIFO method of costing its inventory and is included in a LIFO pool of the U.S. affiliate which includes products purchased from the possessions corporation in pre-TEFRA years, how should the LIFO index computation of the U.S. affiliate be made in the first year in which section 936(h) applies and in subsequent taxable years?**

Answer 19: The U.S. affiliate should treat the first taxable year for which section 936(h) applies as a new base year in accordance with procedures provided by regulations under section 472. Thus, the opening inventory for the first year for which section 936(h) applies (valuing possession products purchased from the possessions corporation on the basis of the cost of such possession products), would equal the new base year cost of the inventory of such pool of the U.S. affiliate. Increments and decrements at new base year cost would be valued for LIFO purposes pursuant to the procedures provided by regulations under section 472.

Question 20: If the possessions corporation computes its income with respect to a product under the profit split method, with respect to which units of the product shall the profit split method apply?

Answer 20: The profit split method shall apply to units of the possession product produced in whole or in part by the possessions corporation in the possession and sold during the taxable year by members of the affiliated group (other than foreign affiliates) to unrelated parties or to foreign affiliates. In no event shall the profit split method apply to units of the product which were not taken into account by the possessions corporation in applying the significant business presence test for the current taxable year or for any prior taxable year in which the possessions corporation also had a significant business presence in the possession with respect to such product.

(2) *Pre-TEFRA inventory.*

Question 1: How is pre-TEFRA inventory to be determined if the profit split option is elected and the FIFO method of costing inventory is used by the U.S. affiliate?

Answer 1: Pre-TEFRA inventory is inventory which was produced by the possessions corporation and transferred to a U.S. affiliate prior to the possessions corporation's first taxable year beginning after December 31, 1982. Pre-TEFRA inventory will not be included for purposes of the profit split option. If the U.S. affiliate uses the FIFO method of costing inventory, the pre-TEFRA inventory will be treated as the first inventory sold by the U.S. affiliate during the first year in which section 936(h) applies and will not be included in the computation of combined taxable income for purposes of the profit split option. The treatment of pre-TEFRA inventory when FIFO costing is used by both the U.S. affiliate and the possessions corporation is illustrated by the following example in which FIFO unit costing is used:

Example. Assume the following:

	X		Y	
	Possessions corporation		U.S. affiliate	
	Number of units	Cost per unit	Number of units	Cost per unit
Beginning inventory	500	$150	200	$225
Units produced during 1983	1,000	200	....	....
Ending inventory	400	200	300	....

In 1983, the beginning inventory of X, a possessions corporation, is 500 units with a unit cost of $150 and the beginning inventory of Y, the U.S. affiliate, is 200 units with a unit cost of $225, which represents the section 482 price paid by Y. Y's beginning inventory in 1983 represents purchases made in 1982 of products produced by X in that year. Y sells all the units it purchases from X to Z, a foreign affiliate. In 1983, X produces 1000 units at a unit cost of $200 and sells 1100 units to Y (the difference between 1500 units, representing X's 1983 beginning inventory (500) and the units produced by X in 1983 (1000), and X's ending inventory of 400 units). Of the 1100 units sold by X to Y in 1983, only 800 units (and not 1000 units) which were sold by Y to Z are taken into consideration in computing combined taxable income for 1983. Since FIFO costing by the possessions corporation is used, the cost is $150 per unit for the first 500 units and $200 per unit for the remaining 300 units. The 200 units sold by X to Y in 1982 are pre-TEFRA inventory and are not included in the computation of combined taxable income for 1983. They are also treated as the first units sold by Y to Z in 1983. This inventory has a unit cost of $225, which reflects the section 482 transfer price from X to Y in 1982. Y's 1983 ending inventory of 300 units will not be taken into consideration in computing the combined taxable income of X and Y for 1983 because the units have not been sold to a foreign affiliate or to persons who are not members of the affiliated group. In a subsequent year when the units are sold to Z, the cost to X and selling price to Z of these units will enter into the computation of combined taxable income for that year.

(c) *Covered Intangibles.*

Question 1: What are "covered intangibles" under section 936(h)(5)(C)(i)(II)?

Answer 1: The term "covered intangibles" means (1) intangible property developed in a possession solely by the possessions corporation and owned by it, (2) manufacturing intangible property (described in section 936(h)(3)(B)(i) which is acquired by the possessions corporation from unrelated persons, and (3) any other intangible property (described in section 936(h)(3)(B)(ii) through (v), to the extent not described in section 936(h)(3)(B)(i)) which relates to sales of products or services to unrelated persons for ultimate consumption or use in the possession in which the possessions corporation conducts its business. The possessions corporation is treated as the owner of covered intangibles for purposes of obtaining a return thereon.

Question 2: Do covered intangibles include manufacturing intangible property which is acquired by an affiliate and subsequently transferred to the possessions corporation?

Answer 2: No. In order for a manufacturing intangible to be treated as a covered intangible, the intangible property must be acquired directly by an unrelated person, unless the manufacturing intangible was acquired by an affiliate from an unrelated person and was transferred to the possessions corporation by the affiliate prior to September 3, 1982.

Question 3: If a possessions corporation licenses a manufacturing intangible from an unrelated party, will the licensed intangible be treated as a covered intangible?

Answer 3: No.

Question 4: How is ultimate consumption or use determined for purposes of the definition of covered intangibles?

Answer 4: A product will be treated as having its ultimate use or consumption in a possession if it is sold by the possessions corporation to a related or unrelated person in a possession and is not resold or used or consumed outside of the possession within one year after the date of the sale.

Question 5: Are sales of products that relate to covered intangibles excluded from the cost sharing fraction?

Answer 5: If no manufacturing intangibles other than covered intangibles are associated with the possession product, then sales of such product will be excluded from the cost sharing fraction. If both covered and non-covered manufacturing intangibles are associated with the possession product, then sales of such product will be included in the cost sharing fraction.

Question 6: If the cost sharing option is elected, is it necessary for the possessions corporation to be the legal owner of covered intangibles described in section 936(h)(5)(C)(i)(II)(*c*) related to the product in order for the possessions corporation to receive a full return with respect to such intangibles?

Answer 6: No. For purposes of section 936(h), it is immaterial whether such covered intangibles are owned by the possessions corporation or by another member of the affiliated group. Moreover, if the legal owner of such covered intangibles which are subject to section 936(h)(5) is an affiliate of the possessions corporation, such person will not be required to charge an arm's length royalty under section 482 to the possessions corporation.

§1.936-7 Manner of making election under section 936(h)(5); special election for export sales; revocation of election under section 936(a).

The rules in this section apply for purposes of section 936(h) and also for purposes of section 934(e), where applicable.

(a) *Manner of making election.*

Question 1: How does a possessions corporation make an election to use the cost sharing method or profit split method?

Answer 1: A possessions corporation makes an election to use the cost sharing or profit split method by filing Form 5712-A and attaching it to its tax return. Form 5712-A must be filed on or before the due date (including extensions) of the tax return of the possessions corporation for its first taxable year beginning after December 31, 1982. The electing corporation must set forth on the form the name and the taxpayer identification number or address of all members of the affiliated group (including foreign affiliates not required to file a U.S. tax return). All members of the affiliated group must consent to the election. An authorized officer of the electing corporation must sign the statement of election and must declare that he has received a signed statement of consent from an authorized officer, director, or other appropriate official of each member of the affiliated group. The election is not valid unless all affiliates consent. However, a failure to obtain an affiliate's written consent will not invalidate the election out if the possessions corporation made a good faith effort to obtain all the necessary consents or the failure to obtain the missing consent was inadvertent. Subsequently created or acquired affiliates are bound by the election. If an election out is revoked under section 936(h)(5)(F)(iii), a new election out with respect to that product area cannot be made without the consent of the Commissioner. The possessions corporation shall file an amended Form 5712-A with its timely filed income tax return to reflect any changes in the names or number of the members of the affiliated group for any taxable year after the first taxable year to which the election out applies. By consenting to the election out, all affiliates agree to provide information necessary to compute the cost sharing payment under the cost sharing method or combined taxable income under the profit split method, and failure to provide such information shall be treated as a request to revoke the election out under section 936(h)(5)(F)(iii).

Question 2: May the "election out" under section 936(h)(5) be made on a product-by-product basis, or must it be made on a wider basis?

Answer 2: An electing corporation is required to treat products in the same product area in the same manner. Similarly, all possessions corporations in the same affiliated group that produce any products or render any services in the same product area must make the same election for all products that fall within the same product area. However, §1.936-7(b) provides that the electing corporation may make a different election for export sales than for domestic sales. The electing corporation or corporations may also make different elections for products that fall within different product areas.

Question 3: May the possessions corporation elect to define product area more narrowly than the 3-digit SIC code?

Answer 3: No. Certain alternatives, such as the 4-digit SIC code, would not be permitted under the statute. However, other methods for defining product area may be considered by the Commissioner in the future.

Question 4: May a possessions corporation make an election out under the cost sharing method with respect to a product area if the affiliated group incurs no research, development or experimental costs in that product area?

Answer 4: Yes. In that case the cost sharing payment will be zero.

Question 5: If the significant business presence test is not satisfied for a product or type of service within the product area covered by the election out under section 936(h)(5) what rules will apply with respect to that product?

Answer 5: With respect to the product which does not satisfy the significant business presence test, the provisions of section 936(h)(1) through (h)(4) will apply to the allocation of income. However, if a cost sharing or a profit split election has been made with respect to the product area, the cost sharing payment or the research and development floor under section 936(h)(5)(C)(ii)(II) will not be reduced.

Question 6: Is a taxpayer permitted to make a change of election with respect to the cost sharing and profit split methods?

Answer 6: In general, once the election is properly made, it is binding for the first year in which it applies and all subsequent years (including upon any later created or acquired affiliates), and revocation is only permitted with the consent of the Commissioner of Internal Revenue. However, a taxpayer will be permitted to change its election once from the cost sharing method to the profit split method or *vice versa*, or from the method permitted under section 936(h)(1) through (h)(4) to cost sharing or profit split or *vice versa*, without the consent of the Commissioner if the change is made on the taxpayer's return for its first taxable year ending after June 13, 1986. Such change will apply to such taxable year and all subsequent taxable years, and, at the taxpayer's option, may also apply to all prior taxable years for which section 936(h) was in effect. A change of election will be treated as an election subject to the procedures set forth above and to section 481 of the Internal Revenue Code.

Question 7: If the Commissioner determines that a possessions corporation does not meet the 80-percent possession source test or the 65-percent active trade or business test (the "qualification tests") for any taxable year beginning after 1982, under what circumstances is the possessions corporation permitted to make a distribution of property after the close of its taxable year to meet the qualification tests?

Answer 7: A possessions corporation may make a pro rata distribution of property to its shareholders after the close of the taxable year if the Commissioner determines that the possessions corporation does not satisfy the qualification tests (a) by reason of the exclusion from gross income of intangible income under section 936(h)(1)(B) or section 936(h)(5)(C)(i)(II) or (b) by reason of the allocation to the shareholders of the possessions corporation of income under section 936(h)(5)(C)(ii)(III); provided, however, that the determination of the Commissioner does not contain a finding that the failure of such corporation to satisfy the qualification tests was due, in whole or in part, to fraud with intent to evade tax or willful neglect on the part of the possessions corporation. The possessions corporation must designate the distribution at the time the distribution is made as a distribution to meet qualification requirements, and it will be subject to the provisions of section 936(h)(4). Such distributions will not qualify for the dividends received deduction.

Question 8: If a possessions corporation owns stock in a subsidiary possessions corporation, any intangible property income allocated to the parent possessions corporation under section 936(h) will be treated as U.S. source income and taxable to the parent possessions corporation. Is the intangible property income taken into consideration in determining whether the parent possessions corporation meets the income tests of section 936(a)(2)?

Answer 8: While taxable to the parent possessions corporation, the intangible property income does not enter into the calculation of the 80-percent possession source test or the 65-percent active trade or business test of section 936(a)(2)(A) and (B). This would also be the case if the subsidiary possessions corporation made a qualifying distribution under section 936(h)(4).

(b) *Separate election for export sales.*

Question 1: What methods of computing income can a possessions corporation use under the separate election for export sales?

Answer 1: The only two methods which are available under the separate election for export sales are the cost sharing method and the profit split method.

Question 2: What is the definition of export sales for purposes of the separate election for export sales?

Answer 2: The determination of export sales is based upon the destination of the product, *i.e.*, where it is to be used or consumed. If the product is sold to a U.S. affiliate, it will be treated as an export sale only if resold or otherwise transferred abroad to a foreign person (including a foreign affiliate or foreign branch of a U.S. affiliate) within one year from the date of sale to theU.S. affiliate for ultimate use or consumption outside the United States as provided under §1.954–3(a)(3)(ii).

Question 3: Assume that a possessions corporation sells a product to both foreign affiliates and foreign branches of U.S. affiliates. In addition, it sells the product to its U.S. parent for resale in the U.S. The possessions corporation makes a profit split election for domestic sales and a cost sharing election for export sales. Will the sales to foreign branches of U.S. affiliates be treated as exports subject to the cost sharing method or as domestic sales subject to the profit split method?

Answer 3: The sales to a foreign branch of a U.S. corporation are exports if for ultimate use or consumption outside of the United States as provided under §1.954–3(a)(3)(ii).

Question 4: Under what circumstances may a possessions corporation make the separate election under section 936(h)(5)(F)(iv)(II) for computing its income from products exported to a foreign person when the income derived by such foreign person on the resale of such products is included in foreign base company income under section 954(a)?

Answer 4: If the income derived by a foreign person on the resale of products manufactured, in whole or in part, by a possessions corporation is included in foreign base company income under section 954(a), then the possessions corporation may make the separate export election under section 936(h)(5)(F)(iv)(II) for computing its income from such products only if such foreign person has been formed or is availed of for substantial business reasons that are unrelated to an affiliated corporation's U.S. tax liability. For purposes of the preceding sentence, a foreign person will be considered to be formed or availed of for such substantial business reasons if the foreign person in the normal course of business purchases substantial quantities of products from both the possessions corporation and its affiliates for resale, and, in addition, provides support services for affiliated companies such as centralized testing, marketing of products, management of local currency exposures, or other similar services. However, a foreign person that purchases and resells products only from a possessions corporation is presumed to be formed or availed of for other than such substantial business reasons, even if the foreign person provides additional services.

Question 5: When will the "manufacturing" test set forth in subsection (d)(1)(A) of section 954 be applicable to the export sales of a product of a possessions corporation which makes a separate election for export sales?

Answer 5: An electing corporation will be required to meet the"manufacturing" test set forth in subsection (d)(1)(A) of section 954 with respect to export sales of its product in each taxable year in which the separate election for export sales is in effect.

(c) *Revocation of election under section 936(a).*

Question 1: When may an election under section 936(a) be revoked?

Answer 1: An election under section 936(a) may be revoked during the first ten years of section 936 status only with the consent of the Commissioner, and without the Commissioner's consent after that time. The Commissioner hereby consents to all requests for revocation that are made with respect to the taxpayer's first taxable year beginning after December 31, 1982 provided that the section 936(a) election was in effect for the corporation's last taxable year beginning before January 1, 1983, if the taxpayer agrees not to re-elect section 936(a) prior to its first taxable year beginning after December 31, 1988. A taxpayer that wishes to revoke a section 936(a) election under the terms of the blanket revocation must attach a "Statement of Revocation—Section 936" to the taxpayer's timely filed return (including extensions) and must state that inrevoking the election the taxpayer agrees not to re-elect section 936(a) prior to its first taxable year beginning after December 31, 1988. Other requests to revoke not covered by the Commissioner's blanket consent should be addressed to the District Director having jurisdiction over the taxpayer's tax return.

Par. 3. The authority citation for part 602 is as follows:

Authority: 26 U.S.C. 7805.

Par. 4. Section 602.101 (c) is amended by inserting in the appropriate place in the table "§1.936–7 . . . 1545–0215

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved June 2, 1986.

J. Roger Mentz,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on June 9, 1986, 1:30 p.m., and published in the issue of the Federal Register for June 13, 1986, 51 F.R. 21518)

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 280G, 467, 468, 483, 7872.)

Rev. Rul. 86-86

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of July 1986 are as follows:

	Period for Compounding			
	Annual	***Semiannual***	***Quarterly***	***Monthly***
Short-Term				
AFR	**7.23%**	**7.10%**	**7.04%**	**7.00%**
110% AFR	**7.96%**	**7.81%**	**7.74%**	**7.69%**
120% AFR	**8.70%**	**8.52%**	**8.43%**	**8.37%**
Mid-Term				
AFR	**8.02%**	**7.87%**	**7.79%**	**7.74%**
110% AFR	**8.85%**	**8.66%**	**8.57%**	**8.51%**
120% AFR	**9.66%**	**9.44%**	**9.33%**	**9.26%**
Long-Term				
AFR	**8.04%**	**7.88%**	**7.80%**	**7.75%**
110% AFR	**8.86%**	**8.67%**	**8.58%**	**8.52%**
120% AFR	**9.68%**	**9.46%**	**9.35%**	**9.28%**

Section 7872.—Treatment of Loans with Below-Market Interest Rates

Federal short-term, mid-term and long-term rates are set forth for the month of July 1986. See Rev. Rul. 86-86, this page.

Part IV. Items of General Interest

Foundations Status of Certain Organizations

Announcement 86–84

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

Access-Westminster, Los Angeles, CA
Actors Guild Ltd., New York, NY
Acts Christian Transitional Service, Philadelphia, PA
Adair County Rural Fire District #1 Inc., Kirksville, MO
After School Workshop Inc., The, Westfield, NJ
Alternative Arts Association, Portland, OR
Ambassadors For Christ, Second Chance, Inc., Indianapolis, IN
American Hungarian Action Committee Inc., New York, NY
American Residential Architecture Foundation, Warren, VT
Amious House of Lawrence County, New Castle, PA
Anchorage Hospice, Inc., Anchorage, AK
Animal Survival Clinic, Inc., Cherry Hill, NJ
Anthroposophical Society in Greater Boston Inc., Belmont, MA
Appletree System, Inc., The, Bridgewater, NJ
Arcane Theatricks, Chicago, IL
Area I. Region II. Professional, Madison, NJ
Atlantis Research Foundation, Chicago, IL
B.T. Halbrooks Evangelistic Association, Inc., Milwaukee, WI
Baharat Cultural Society, North Bergen, NJ
Bentown Philadelphia, Inc., Philadelphia, PA
Bereaved Parents, St. Albans, WV
Big Brothers and Sisters of Crawford County, Inc., Meadville, PA
Black Hills Alliance, Rapid City, SD
Blackstone Valley Educational Foundation, Inc., Uxbridge, MA
Block Foundation for Nutritional Research Inc., The, Evanston, IL
Bogan Baseball League, Oak Park, IL
Brocton Housing Development Fund Co. Inc., Mayville, NJ
Burlington Boxing Club Inc., Burlington, IA
CIBC Residences, Blue Bell, PA
Career Youth Development Inc., Milwaukee, WI
Carpinteria Community Theatre, Inc., Carpinteria, CA
Center for Celebration, Inc., New York, NY
Center for Human Resource Development, The, Lincoln, NE
Central Dauphin Band Boosters Association, Harrisburg, PA
Chamber Musicians Alliance Inc., The Arts Council of Greater N.H., New Haven, CT
Cherry Hill Soccer Club, Cherry Hill, NJ
Childefense Inc., Danvers, MA
Citizens for Connecticut's Future, Inc., Naugatuck, CT
Clark Savage Foundation, Arroyo Grande, CA
Community Action Photography Services, Inc., Philadelphia, PA
Community Energy Systems, Springfield, IL
Community Learning Institute Inc., Milford, DE
Comptex Associates, Inc., Washington, DC
Concerned Parents of Camden Corp., The, Collingswood, NJ
Conestoga Place, Inc., Los Angeles, CA
Connecticut Legal Fund Inc., Canaan, CT
Connecticut Neurological Foundation, Inc., New Haven, CT
Council of the Advancement of Consumer Policy, Washington, DC
Crosswicks Creek Conservation Foundation, Inc., Crosswicks, NJ
Cultural Survival Productions, Inc., Cambridge, MA
Cumberland Law Day Committee, Inc., Vineland, NJ
Dance Rep, Inc., New York, NY
Debbie Smith Memorial Trust, Glen Rock, NJ
Delaware County Law Library Society, Media, PA
Delaware Office of Youth Camp Safety, Inc., Dover, DE
Dream Inc., Mays Landing, NJ
East End Historical Society Inc., Bridgeport CT
East St. Louis Neighborhood Development Corp., East St. Louis, IL
Eastern Illinois Foodbank, Champaign, IL
Eau Claire Musical Arts Society Ltd., Eau Claire, WI
Egyptian American Association of Central Jersey, The, Newark, NJ
Elizabeth Avenue Arts and Culture Group, Newark, NJ
Ellen Webb Dance Company, Inc., The, New York, NY
Environmental Research Foundation, Lawrenceville, NJ
Erthel Green Walker Memorial Foundation Inc., The, St. Albans, NY
Everyday Clothes, Inc., Sioux Falls, SD
Farmers Hall of Fame, Inc., West Fargo, ND
Fear Anonymous, San Francisco, CA
Friends of Disabled of Malden, Inc., Malden, MA
Friends of Prisoners Foundation, Inc., Philadelphia, PA
Friends of Reconstructive Surgery Research, Beverly Hills, CA
Gaujarati Smaj, The, King of Prussia, PA
Global Competitiveness Council, The, Boston, MA
Gluten Intolerance Society of California, Santa Ana, CA
Golden Apple Foundation, Inc., The, New York, NY
Good Neighbors Unlimited, Inc., Annapolis, MD
Good Samaritan #2 Charitable Trust, The, New Holland, PA
Grace Church Music Series, The, Manchester, NH
Greater Hartford Arts Festival Inc., Hartford, CT
Greater Milwaukee Billy Graham Crusade, Inc., Milwaukee, WI
Hackett Senior Housing Foundation, Inc., Los Angeles, CA
Harriet Jenkins Memorial Trust, Rockville, MD
Health Education Associates, Inc., Willow Grove, PA
Health Policy International, Inc., Princeton, NJ
Hospice St. Louis Inc., St. Louis, MO
Huron Theater, The, Chicago, IL
Hyannis Knights of Columbus Educational Trust, Hyannis, MA

Icograda 1978 Chicago Congress Inc., Chicago, IL
Indochinese American Association of Omaha, Omaha, NE
Inn-Dwelling, Philadelphia, PA
Institute for Community Education Inc., The, Milwaukee, WI
Institute for Invention and Innovation, Inc., The, St. Paul, MN
Iowa City Community School District Foundation, Iowa City, IA
Jeffrey Neal Kaplan Scholarship Fund Trust, Framingham, MA
Jewish Campus Activities Board, Philadelphia, PA
Jewish Scholarship Foundation, The, New York, NY
Joans County Public Health Agency, Anamosa, IA
John Henry Belter Society, Inc., The, Whitestone, NY
Kerri, Kattar Memorial Fund, Inc., Lawrence, MA
Kostmayer Jobs Task Force, Doylestown, PA
La Cienega—Cadillac Community Association, Los Angeles, CA
Light The Bridge Committee, Inc., Harrisburg, PA
Little Feet Day Care Center, Inc., Philadelphia, PA
London Regional Children's Museum, London, Ontario
Ludlow Neighborhood Advisory Committee, Philadelphia, PA
Madison Senior Housing Corporation, Los Angeles, CA
Management Support Associates of Milwaukee, Inc., Milwaukee, WI
Marcrobiotic Center of Princeton, Inc., Princeton, NJ
Maryland Ensemble Theatre Assn. Inc., The, Baltimore, MD
McGuffey Manor Senior Housing Inc., Oakmont, PA
Media Commentary Council Inc., New York, NY
Mel Davis Youth Foundation, The, Chicago, IL
Metropolitan Washington Petowners Associates, Inc., The, Washington, DC
Michael Landsman Ministries, Inc., Gardena, CA
Milwaukee Southwest Kiwanis Foundation, Inc., West Allis, WI
Miscarriage Infant Death and Stillbirth (M I D S), Parsippany, NJ
Missouri Solar Energy Association, St. Louis, MO
Mobile Health Services, Inc., Woodruff, WI
N C. C. Health Care, Inc., Newark, NJ
NPL Provedent Fund of Iowa, Des Moines, IA
National Administrative Law Judge Foundation, Midwest City, OK
National Forum on Criminal Justice Center for Legal Studies, Springfield, IL
National Naval Officers Association, Inc., Washington, DC
National Sports Museum, The, Washington, DC
Neighbors Network, Bismarck, ND
New Castle County Lazers Soccer Association, Newark, DE
New Community Urban Renewal Corp., Newark, NJ
New High, Inc., Prineville, OR
New Horizons Ministries International, Paterson, NJ
New Jersey Friends of F. A. N. A., Inc., East Windsor, NJ
New Jersey Vietnam Veterans Leadership Program, Inc., Jersey City, NJ
New Jewish Agenda, Philadelphia Chapter, Philadelphia, PA
New Majority Leadership Seminars Inc., Moorhead, MN
New Virginia Review, Inc. Richmond, VA
Noah's Ark Child Care Center, Inc., White Sulphur Springs, MT
Northeast Star Inc., Kirksville, MO
Northeast Wisconsin Skilled Trades Improvement Program, Inc., Green Bay, WI
Northern New Jersey John Wesley White Crusade, Inc., Cresskill, NJ
Northwest Bergen Crime Stoppers, Inc., Ramsey, NJ
Northwestern Cardiology Research Fund, Inc., Chicago, IL
OIC Community Revitalization, Inc., Philadelphia, PA
Operation Search, St. Louis, MO
Organization of Latino Affiliates, Inc., Milwaukee, WI
Pasada Del Sol, Inc., Kansas City, MO
Pasticcio Dance Ensemble, Inc., Eden Prairie, MN
Paterson Regional Arts Housing Inc., Paterson, NJ
Peace Research Associates, Merion Station, PA
Pennsylvania District Attorneys Institute, The, Harrisburg, PA
People Place of Greater Harrisburg, The, Harrisburg, PA
Philadelphia Solar Energy Association, Philadelphia, PA
Philadelphia Town Watch Council, Philadelphia, PA
Pierce County Riverman Drum and Bugle Corps, The, Sumner, WA
Pinewood Manor, Inc., Los Angeles, CA
Pocono Child Care Inc., Chinchilla, PA
Police Shield, The, Bristol, PA
Princeton Endowment for the Arts, Princeton, NJ
Project Peru, Inc., Dover, NJ
Public Employees Roundtable, Washington, DC
Putnam Community Cultural and Recreational Center, Inc., Mahopac, NY
Raritan River Friends of Clearwater, North Brunswick, NJ
Region III Head Start Association, Inc., Wilmington, DE
Regional Recreation Committee, Inc., Grafton, ND
Reiki Center of Los Angeles, Los Angeles, CA
Rosscare, Bangor, ME
Sadie E. Brewer Scholarship Foundation for the Arts, Los Angeles, CA
St. Joseph Ecumenical Help Care, Inc., St. Joseph, MO
Saran Enterprises, Inc., Inglewood, CA
Satellite Square Club, Inc., Philadelphia, PA
Schizophrenic Care & Treatment Society, St. Louis, MO
Scott County Citizens for Better Housing, Gate City, VA
Second Wind Harmonica Bank, The, Bovey, MN
Shared Living, Inc., Columbus, OH
Sidney Kay's School of the Theatre, Swarthmore, PA
Sleepy Hollow Land Conservancy, The, Elgin, IL
Source Telecommunications System (STS), Washington, DC
South Jersey Council On Alcoholism, Inc., Sewell, NJ
South Surburban Foundation Park, Forest, IL
South West Coalition of Community Organizers, Philadelphia, PA
Southeast Missouri Research Association for Specific Perceptual Motor Disabilities Inc., Cape Girardeau, MO
Southern California Health Resources Center, Tustin, CA
Speech and Learning Associates, Inc., South Orange, NJ
Sports Nine Skating Club, Morganville, NJ
Spring Child Workshop, Inc., Mays Landing, NJ
Sunny Slope Business Association, Kansas City, MO
Sunset Views, Inc., Los Angeles, CA
Survival Phase One, Inc., Rockville, MD

Thought Movement Motor, Inc., New York, NY
Tommy Simone Memorial Scholarship Fund, The, Kansas City, MO
Trans-World Christian Fellowship, Inc., Billings, MT
UCC Apartments, Inc., Los Angeles, CA
United States Junior Tennis Foundation, Inc., Little Silver, NJ
Universe Productions, Falls Church, VA
Van Saun Zoological Society, Inc., Paramus, NJ
Venture Foundation Ltd., Nanvet, NY
Wallace Pyawasit Memorial Center, Inc., The, Milwaukee, WI
Walter Briehl Human Rights Foundation, Los Angeles, CA
Warren Hospital Foundation, Inc., Phillipsbury, NJ
Washington Civic Opera Association, Washington, DC
Westchester Repertory Theatre, Inc., White Plains, NY
Western Illinois Agency on Aging, Inc., Rock Island, IL
White Terrace Conservancy, Newark, NJ
Wildcats Youth Organization, Philadelphia, PA
Wyckoff Torpedoes Soccer Club, Wyckoff, NJ

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Termination of Section 7428(c) Validation of Certain Contributions Made During Pendency of Declaratory Judgment Proceedings

This announcement serves notice to potential donors that a court has determined that the organization listed below is no longer described in section 170(c)(2) of the Internal Revenue Code, as more particularly set forth in section 7428(c)(1). Protection under section 7428(c) has terminated effective on the date indicated.

Church of Gospel Ministry, Inc.
May 30, 1986
Chula Vista, CA.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Henry L. Creel	Cleveland, OH	Certified Public Accountant	Indefinite from May 15, 1986
J. Thomas Jones	Augusta, GA	Certified Public Accountant	Indefinite from June 1, 1986
Michael D. Sherman	Pound Ridge, NY	Enrolled Agent	Indefinite from May 27, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and address of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the Weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Earl M. Walker	Port Neches, TX	Certified Public Accountant	May 19, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.367(a)–1, removed; 1.367(a)–4T, redesignated as 1.367(a)–7T; 1.367(a)–1T through 1.367(a)–6T, 1.367(d)–1T, 1.6038B–1T, added; 7.367(b)–1, 7.367(b)–4, amended; published as temporary regulations in T.D. 8087, page 5, 1986–23 I.R.B.	Transfers of property by U.S. persons to foreign corporations	1986–23 I.R.b. 33	July 15, 1986
26 CFR 1.338–1T, 1.338–2T, 1.338–4T, 1.338–5T, 1.338(h)(10)–1T, amended; published as temporary regulations in T.D. 8088, page 4, 1986–24 I.R.B.	Section 338(g) statements of election	1986–24 I.R.B. 24	July 15, 1986

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[1] See footnote at end of list.

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Key to Abbreviations:

RR	Revenue Ruling
RP	Revenue Procedure
TD	Treasury Decision
CD	Court Decision
PL	Public Law
EO	Executive Order
DO	Delegation Order
TDO	Treasury Department Order
TC	Tax Convention
SPR	Statement of Procedural Rules
PTE	Prohibited Transaction Exemption

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  - Livestock, cows carrying transplanted embryos, subsequently born (RR 24) 8, *7*
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Proposed regulations: Continued
- 26 CFR 1.46-3(e), revised; 1.47–1, 1.48–9, 1.167(a)–11, amended; recapture of investment credit for mass assets (LR–92–73) 4, *42*
- 26 CFR 1.61–2T, removed; new 1.61–2T, added; 1.132–1T, removed; new 1.132–1T, added; 1.132–2T through 1.132–8T, added; 1.162–25T, 1.274–5T, 1.274–6T, amended; taxation of fringe benefits and exclusions from gross income for certain fringe benefits (LR–216–84) 3, *40*
- 26 CFR 1.61–6(c)(3), 1.163–4, 1.451–1(d), 1.451–2(b), 1.454(a)(1)(i), 1.482–2(a), 1.482–2(c)(2), 1.483–1, 1.483–2, 1.1016–5(s), 1.1232–2, 25.2512–4, 25.2512–8, revised; 1.163–7, 1.446–2, 1.483–3 thru 1.483–5, 1.1012–2, 1.1271–1 thru 1.1275–5, added; 1.61–7(d), 1.249–1, 1.409–1(b)(1), 1.582–1(d), 1.582–1(e)(3)(i), 1.636–1(a)(1)(ii), 1.818–3(f), 1.861–2(a)(4), 1.993–1(g), 1.1001–1(g), 1.1012–1(f), 1.1037–1, 1.1232–1, 1.1232–3A, 1.6045–1(c), 1.6049–5, 1.6049–6(d), 1.9006–1(c)(1)(vii), 3.2(d), 3.3(b), 5f. 163–1(f), 6a.103A–2(i)(2)(vi)(B), 514.23, amended; 1.1012–2, removed; 1.7872–4(e), reproposed & revised; debt instruments with original issue discount, imputed interest on deferred payment sales or exchanges of property, safe haven interest rates for commonly controlled taxpayers (LR–189–84) 18, *4*
- 26 CFR 1.72–4, 1.72–5, 1.72–6, 1.72–7, 1.72–9, 1.72–11, 1.403(b)–1(d)(4), 1.403(b)–1(d)(4)(ii), amended; 1.403(b)–1(d)(4)(iv), 1.401(a)–18, 1.401(j)–1 through 1.401(j)–6, removed; 1.403(b)–1(d)(4)(iv), added; unisex annuity tables (LR–19–80) 16, *9*
- 26 CFR 1.72(e)–1T, 1.79–4T, 1.125–2T, 1.133–1T, 1.162–10, 1.402(a)(5)–1T, 1.404(a)–1T, 1.404(a)(8)–1T, 1.404(b)–1T, 1.404(d)–1T, 1.404(k)–1T, 1.419–1T, 1.419A–1T, 1.461(h)–4T, 1.463–1T, 1.505(c)–1T, 1.512(a)–5T, 1.1042–1T, 20.2039–1T, 54.4976–1T, 54.4978–1T, 301.7701–17T, added; 1.404(d)–1, removed; effective dates and other issues under employee benefit provisions of Tax Reform Act of 1984 (EE–96–85) 13, *48*

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- 26 CFR 1.103–10, revised and amended; $40 million limitation on beneficiaries of certain tax-exempt bond issues, definition of term "principal user" (LR–157–84) 12, *22*; (LR–59–74) 12, *19*
- 26 CFR 1.338–1T, 1.338–2T, 1.338–4T, 1.338–5T, 1.338(h)(10)–1T, amended; statements of elections and due dates (LR–8–86) 24, *24*
- 26 CFR 1.338–1T, 1.338–4T, 1.338(h)(10)–1T, amended; 1.338(b)–1T, 1.338(b)–2T, 1.338(b)–3T, added; determination of basis of assets of a target corporation (LR–191–82) 11, *28*
- 26 CFR 1.338–5T, added; 1.338–1T, 1.338–4T, 1.338(h)(10)–1T, amended; international aspects of section 338 (LR–35–84) 15, *51*
- 26 CFR 1.338(h)(10)–1T, 1.1502–75T, added; 1.338–1T, 1.338–4T, amended; elections under section 338(h)(10), extension of time for certain elections (LR–218–83) 8, *35*
- 26 CFR 1.367(a)–1, removed; 1.367(a)–4T, redesignated as 1.367(a)–7T; 1.367(a)–1T through 1.367(a)–6T, 1.367(d)–1T, 1.6038B–1T, added; 7.367(b)–1, 7.367(b)–4, amended; transfers of property by U.S. persons to foreign corporations (LR–3–86) 23, *33*
- 26 CFR 1.401(a)–4, 1.411(d)–4, added; limitations on alternative benefits under qualified plans (EE–95–84), 9, *25*
- 26 CFR 1.451–3, amended; accounting for long-term contracts, corporations filing consolidated returns with a contractor (LR–121–85) 6, *55*
- 26 CFR 1.904(f)–1 through 1.904(f)–6, 1.1502–9, added; recapture of foreign losses (LR–3–77) 10, *14*
- 26 CFR 1.936–2, 1.936–3, 1.936–3A, added; 7.936–1, removed; qualified possession source investment income (LR–106–77) 8, *33*
- 26 CFR 1.6031–1, revised; partnership returns (LR–198–82) 9, *30*
- 26 CFR 1.6041–3, amended; information reporting of allowances, or reimbursements, or charges for travel and other expenses of public employees (LR–59–85) 7, *26*
- 26 CFR 1.6041A–1, added; information reporting of direct sales and payments of renumeration for services (LR–214–82) 6, *46*

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- 26 CFR 1.6050K–1T, added; information returns relating to sales or exchanges of partnership interests (LR–236–84) 7, *26*
- 26 CFR 301.6103(j)(1)–1, amended; 301.6103(j)(2)–1, removed; disclosure of return information to the Bureau of the Census (LR–4–86) 19, *15*
- 26 CFR 301.6111–1T, amended; tax shelter registration (LR–66–85) 17, *32*
- 26 CFR 301.6221–1, 301.6233–1 & intermediate sections, added; certain rules for the tax treatment of partnership items (LR–205–82) 21, *12*

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- 26 CFR 1.58–3T, added; treatment of non-alternative tax itemized deductions by trusts and estates (TD 8083) 25, *4*
- 26 CFR 1.61–2T, removed; new 1.61–2T, added; 1.132–1T, removed; new 1.132–1T added; 1.132–2T through 1.132–8T, added; 1.162–25T, 1.274–5T, 1.274–6T, amended; taxation of fringe benefits and exclusions from gross income for certain fringe benefits (TD 8063) 3, *4*
- 26 CFR 1.72(e)–1T, 1.79–4T, 1.125–2T, 1.133–1T, 1.162–10, 1.402(a)(5)–1T, 1.404(a)–1T, 1.404(a)(8)–1T, 1.404(b)–1T, 1.404(d)–1T, 1.404(k)–1T, 1.419–1T, 1.419A–1T, 1.461(h)–1T, 1.463–1T, 1.505(c)–1T, 1.512(a)–5T, 1.1042–1T, 20.2039–1T, 54.4976–1T, 54.4978–1T, 301.7701–17T, added; 1.404(d)–1, removed; effective dates and other issues under employee benefit provisions of Tax Reform Act of 1984 (TD 8073) 13, *4*
- 26 CFR 1.103–10, amended; election of $10 million limitation on exempt small issues, supplemental capital expenditure statements (TD 8086) 22, *4*
- 26 CFR 1.166–1, 1.166–4, 1.381(c)(4)–1(a)(1)(ii), amended; 1.166–10,

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added; bad debts, treatment of reserves for certain guaranteed debt obligations (TD 8071) 11, *4*
26 CFR 1.167(a)–5, 1.170A–7, amended; 1.170A–14, added; qualified conservation contributions (TD 8069) 9, *4*
26 CFR 1.338–1T, 1.338–2T, 1.338–4T, 1.338–5T, 1.338(h)(10)–1T, amended; statements of elections and due dates (TD 8088) 24, *4*
26 CFR 1.338–1T, 1.338–4T, 1.338(h)(10)–1T, amended; 1.338(b)–1T, 1.338(b)–2T, 1.338(b)–3T, added; determination of basis of assets of a target corporation (TD 8072) 11, *7*
26 CFR 1.338–5T, added; 1.338–1T, 1.338–4T, 1.338(h)(10)–1T, amended; international aspects of section 338 (TD 8074) 15, *4*
26 CFR 1.338(h)(10)–1T, 1.1502–75T, added; 1.338–1T, 1.338–4T, amended; elections under section 338(h)(10), extension of time for certain elections (TD 8068) 8, *9*
26 CFR 1.367(a)–1, removed; 1.367(a)–4T, redesignated as 1.367(a)–7T; 1.367(a)–1T through 1.367(a)–6T, 1.367(d)–1T, 1.6038B–1T, added; 7.367(b)–4, amended; transfers of property by U.S. persons to foreign corporations (TD 8087) 23, *5*
26 CFR 1.404(g)–1, added; deduction of employer liability payments (TD 8085) 22, *5*
26 CFR 1.446–1(c)(1)(ii), 1.451–3, 1.471–11(c), amended; 1.451–5(b), 1.471–10, revised; contracts, long-term, accounting methods (TD 8067) 6, *5*
26 CFR 1.513–6, added; treatment of certain hospital services furnished by one exempt hospital to other such hospitals (TD 8075) 17, *7*
26 CFR 1.704–1, amended; determination of partner's distributive share of partnership income, gain, loss, deduction, or credit (TD 8065) 5, *4*
26 CFR 1.1092(b)–1T, 1.1092(b)–2T, amended; 1.1092(b)–5T(n), revised;

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26 CFR 1.6050K–1T, added; information returns relating to sales or exchanges of partnership interests (TD 8064) 7, *18*
26 CFR 301.6011–2, added; returns required to be filed on magnetic media (TD 8081) 17, *17*
26 CFR 301.6111–1T, amended; tax shelter registration (TD 8078) 17, *22*
26 CFR 301.6231(a)(3)–1, added; definition of "partnership item" (TD 8082) 21, *8*
26 CFR 301.6867–1T, added; illegal activity cash (TD 8079) 17, *24*
26 CFR 301.7611–1, amended; procedures for conducting church tax inquiries and examinations (TD 8077) 20, *8*
26 CFR 301.7701–4, amended; classification of investment trusts with multiple classes of ownership (TD 8080) 17, *25*
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INTERNAL REVENUE CUMULATIVE BULLETINS

______	1927-1	$8.00
______	*1927-2*	*18.00*
______	1928-1	8.00
______	1928-2	10.00
______	1929-1	13.00
______	*1929-2*	*3.50*
______	1930-1	8.50
______	1930-2	10.00
______	*1931-1*	*4.00*
______	1931-2	14.00
______	*1932-1*	*3.25*
______	1932-2	10.00
______	*1933-1*	*3.75*
______	*1933-2*	*4.00*
______	*1934-1*	(**)
______	1934-2	15.00
______	1935-1	8.00
______	*1935-2*	*15.00*
______	*1936-1*	*4.00*
______	*1936-2*	*15.00*
______	*1937-1*	*14.00*
______	1937-2	8.50
______	*1938-1*	*17.00*
______	*1938-2*	*14.00*
______	1939-1-1	9.50
______	1939-1-2	12.00
______	1939-2	10.00
______	1940-1	6.50
______	1940-2	15.00
______	1941-1	8.00
______	*1941-2*	*4.00*
______	1942-1	8.00
______	*1942-2*	*6.50*
______	*1943-(*)*	*11.00*
______	*1944-(*)*	*9.00*
______	1945-(*)	10.00
______	*1946-1*	*3.00*
______	1946-2	6.00
______	*1947-1*	*2.00*
______	1947-2	3.75
______	*1948-1*	*3.50*
______	1948-2	8.50
______	*1949-1*	*8.00*
______	*1949-2*	*3.25*
______	1950-1	7.00
______	*1950-2*	*5.50*
______	*1951-1*	*13.00*
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Internal Revenue

bulletin

July 14, 1986

Bulletin No. 1986-28

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-87, page 7.

Investment credit; leased automobiles. Rules are provided for a lessee of a passenger automobile who, for purposes of claiming an investment tax credit, is treated as having acquired the automobile.

Rev. Rul. 86-89, page 4.

Involuntary conversion; replacement property; basis. The basis of new section 38 property acquired to replace property destroyed in a casualty must be reduced for purposes of computing the investment tax credit by the amount of gain deferred under section 1033(a)(2) of the Code. Rev. Rul. 68-356 modified.

T.D. 8089, page 4.

Amendments to the regulations under section 46 of the Code relate to the limitation on the investment credit with respect to the "synchronization of interest" and the "zero-cost capital" method under the ratable flow-through method of accounting for public utility property.

EMPLOYMENT TAX

Rev. Rul. 86-88, page 10.

FICA; hospital insurance; extension to state and political subdivision employees. Guidelines, in question and answer form, relate to the amendment of section 3121(u) of the Code that extends the hospital insurance (medicare) tax portion of the Federal Insurance Contribution Act (FICA) to wages of newly hired employees of states and political subdivisions.

EXEMPT ORGANIZATIONS

Rev. Rul. 86-90, page 12.

Private foundations; taxable expenditures; scholarship grants. Grants awarded by a private foundation under an employer-related programs are scholarships under section 117(a) of the Code even though the grants will be awarded without regard to the percentage guidelines of section 4.08 of Rev. Proc. 76-47. Therefore, grants awarded under the program will be described in section 4945(g)(1) and will not be taxable expenditures under section 4945(d)(3).

ADMINISTRATIVE

T.D. 8091, page 14.

Amendments to the regulations under sections 7602 and 7609 of the Code relate to administrative summonses.

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Finding List on page 22.
Announcement of Disbarments and Suspensions on page 19.
Announcement of Notice of Proposed Rulemaking on page 20.

Department of the Treasury
Internal Revenue Service

T22.23:

1986-28

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

T22.23:

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 38.—General Business Credit

Whether the basis of new section 38 property acquired to replace property destroyed in a casualty must be reduced for purposes of computing the investment tax credit by the amount of gain deferred under section 1033(a)(2) of the Code. See Rev. Rul. 86-89, below.

Section 46.—Amount Of Credit

26 CFR 1.46-3: Qualified investment.
(Also Sections 38, 1033; 1.1033(b)-1.)

Involuntary conversion; replacement property; basis. The basis of new section 38 property acquired to replace property destroyed in a casualty must be reduced for purposes of computing the investment tax credit by the amount of gain deferred under section 1033(a)(2) of the Code. Rev. Rul. 68-356 modified.

Rev. Rul. 86-89

ISSUE

Should the basis of new section 38 property acquired to replace property destroyed in a casualty be reduced, for purposes of computing the investment tax credit, by the amount of gain deferred under section 1033(a)(2) of the Internal Revenue Code?

FACTS

In 1983 the taxpayer's factory was destroyed by fire. The adjusted basis of section 38 property destroyed was 1,000x dollars. The amount of insurance proceeds attributable to the destroyed section 38 property was 12,000x dollars. Therefore, the gain attributable to the destroyed section 38 property due to the casualty was 11,000x dollars.

In 1983 the factory was rebuilt, and the taxpayer elected to defer the gain under section 1033(a)(2)(A) of the Code. The cost of the replacement section 38 property, which was new section 38 property, was 20,000x dollars. The taxpayer claimed investment tax credit on the replacement section 38 property for 1983, the year the replacement property was placed in service.

LAW AND ANALYSIS

Section 38 of the Code provides for a credit against federal income tax for qualified investment in section 38 property.

Section 46(a)(2)(B) of the Code provides that the regular amount of the credit is 10 percent of the qualified investment.

Section 46(c)(1)(A) of the Code provides that the qualified investment in new section 38 property is the basis of the property multiplied by a percentage to be determined under section 46(c)(2).

Section 1.46-3(c) of the Income Tax Regulations provides that the "basis of any section 38 property shall be determined in accordance with the general rules for determining the basis of property. Thus, the basis of property would *generally* be its cost (see section 1012). . . ." (Emphasis added.)

Use of the word "generally" in the regulation indicates that the basis of new section 38 property for investment tax credit purposes will not always be the cost of the property. The first sentence of the regulation, in providing that the basis of any new section 38 property is to be determined "in accordance with the general rules for determining the basis of property," refers a taxpayer to specific statutory rules. Section 1033 of the Code is one of the general rules for determining basis.

Section 1033(b) of the Code provides that in the case of property purchased by the taxpayer in a transaction described in section 1033(a)(2) that resulted in the nonrecognition of any part of the gain realized as the result of a compulsory or involuntary conversion, the basis shall be the cost of the property decreased in the amount of gain not so recognized.

HOLDING

The basis of new section 38 property acquired to replace property destroyed in a casualty must be reduced for purposes of computing the investment tax credit by the amount of gain deferred under section 1033(a)(2) of the Code.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 68-356, 1968-2 C.B. 17, concerns the determination of the basis of section 38 property acquired to replace destroyed property in factual circumstances similar to the present situation. The revenue ruling concludes that the basis of the replacement section 38 property is its cost decreased by the amount of the gain realized but not recognized under section 1033.

Rev. Rul 68-356 also concerns a section of the Code that was repealed by the Revenue Act of 1971, 1972-1 C.B. 443 (former section 46(c)(4)). The portion of Rev. Rul. 68-356 dealing with that section is obsolete. However, there have not been any substantive legislative changes affecting the portion of the revenue ruling dealing with section 1033 of the Code, although certain subsections of section 1033 cited in Rev. Rul. 68-356 have been redesignated. Thus, the holding of Rev. Rul. 68-356 with respect to section 1033 remains correct.

Rev. Rul. 68-356 is modified to reflect the redesignated subsections of section 1033 of the Code and to reflect that a portion of that ruling is obsolete.

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26 CFR 1.46-6: Limitation in case of certain regulated companies.
T.D. 8089

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER A PART—1 INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Limitation on investment credit in the case of certain regulated companies; synchronization of interest

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the limitation on the investment credit in the case of certain regulated companies. Questions have arisen concerning the permissibility of "synchronization of interest" and the "zero-cost capital" method under the ratable flow-through method of accounting for the investment credit with respect to public utility property. The regulations provide guidance on these issues and affect regulated companies that use the ratable flow-through method of accounting for the investment credit with respect to public utility property.

DATES: The regulations are generally effective with respect to public utility property constructed or acquired by the taxpayer after August 15, 1971.

FOR FURTHER INFORMATION CONTACT: Paulette Chernyshev of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention CC:LR:T, 202-566-3288, not a toll-free call.

SUPPLEMENTARY INFORMATION:

BACKGROUND

On June 26, 1985, proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 46(f) of the Internal Revenue Code were published in * * * [LR 227-84, 1985-2 C.B. 837]. The amendments were proposed to clarify the manner in which the limitation imposed by section 46 (f) applies in the case of regulated companies that use the ratable flow-through method of accounting for the investment credit with respect to public utility property.

Many written comments were received with respect to the proposed amendments, and a public hearing on the amendments was held on August 28, 1985. After consideration of all comments and testimony received on the proposed amendments, the amendments are adopoted as revised by this Treasury decision.

INTEREST SYNCHRONIZATION

Section 46(f)(2) permits the use of a ratable flow-through method of accounting for the investment credit with respect to public utility property. Under this method of accounting, the taxpayer's cost of service for ratemaking purposes may be reduced by a ratable portion of the investment credit. The credit is disallowed, however, if the taxpayer's cost of service is reduced by more than a ratable portion of the credit or if the base to which the taxpayer's rate of return for ratemaking purposes is applied ("rate base") is reduced by any portion of the credit.

In determining whether a credit has been used to reduce rate base, §1.46-6(b)(3) of the regulations requires reference to "any accounting treatment that affects the permitted return on investment by treating the credit in any way other than as though it were capital supplied by common shareholders to which a 'cost of capital' rate is assigned that is not less than the taxpayer's overall cost of capital rate." This requirement appears only in the definition of rate base and it is unclear whether the credit also must be treated as capital provided by common shareholders in determining cost of service. As a result, the Service has received a number of ruling requests asking whether a portion of the return on the rate base attributable to the credit may be characterized as interest expense and taken into account in computing Federal income tax expense for ratemaking purposes ("interest synchronization" or "synchronization of interest").

This issue is addressed, either directly or indirectly, in several cases reviewing rate orders. Although the permissibility of synchronization of interest was an issue in these reviews, the Internal Revenue Service was not a party to the cases and the decisions did not determine the actual tax liability of the regulated companies. Two Federal Courts of Appeal have determined that interest synchronization does not violate section 46(f)(2) or the existing regulations. *Union Electric v. FERC*, 668 F.2d 389 (8th Cir. 1981); *Nepco Municipal Rate Commission v. FERC*, 668 F.2d 1327 (D.C. Cir. 1981); *Public Service of New Mexico v. FERC*, 653 F.2d 681 (D.C. Cir. 1981). In addition, several state courts have approved the use of interest synchronization in ratemaking proceedings. *See, e.g., Narragansett Electric Company v. Burke*, 475 A.2d 1379 (R.I. 1984); *New England Telephone & Telegraph Company v. Public Utilities Commission*, 448 A.2d 272 (Me. 1982). Other courts, however, have concluded that synchronization of interest is not permitted under section 46(f)(2) and the existing regulations. *See, e.g., Utilities Commission v. Carolina Telephone & Telegraph*, 300 S.E. 2d 395 (Ct. App. N.C. 1983).

The proposed regulations provided that interest synchronization would not constitute a reduction in cost of service for purposes of section 46(f)(2), thus generally permitting interest synchronization for purposes of the ratable flow-through method of accounting for the investment credit. The preamble of the notice of proposed rulemaking set forth two reasons for this provision. The first was the Service's conclusion that synchronization of interest does not result in a reduction of cost of service that is attributable to the credit. This conclusion is consistent with financial market realities since, in the absence of the credit, the additional capital needed to finance the investment property generally would be obtained from a similar proportion of debt and equity as in the existing capital structure of the utility. Synchronization of interest properly takes account of the additional interest expense that would have been incurred in those circumstances.

In addition, the Service believed that synchronization of interest under section 46(f)(2) would result in an appropriate accounting for the credit in establishing rates. The basis for this conclusion may be illustrated by a comparison of the rates that would be established without synchronization of interest with the rates that would be established if the credit were unavailable. Under certain factual circumstances (e.g., long-lived assets with respect to which the credit was allowed), the rates that would be established without synchronization of interest may actually exceed in one or more service years the rates that would be established if the credit were unavailable. In contrast, the rates that would be established with synchronization of interest cannot exceed in any year the rates that would be established if the credit were unavailable.

The Service received a number of comments from public service commissions and other regulatory authorities generally supporting the position in the proposed regulations. On the other hand, the Service also received many comments from regulated public utilities and their representatives, which, with some exceptions, opposed interest synchronization on the ground that it constitutes an impermissible reduction in cost of service under section 46(f)(2). After careful consideration of all comments received, the Service has concluded that interest synchronization should be permitted for the reasons stated in the preamble of the notice of proposed rulemaking. Accordingly, the final regulations clarify that interest synchronization is permitted under a ratable flow-through method of accounting.

ZERO-COST CAPITAL

Another issue addressed by the public comments concerned the effect of "zero-cost capital" on the rate of return assigned to the credit. The issue arises if, for example, the reserve for deferred taxes established under sections 167 and 168 is included in rate base as no-cost capital, as permitted under section 1.167-(l) of the regulations. The issue may similarly arise, for example, if non-interest-bearing liabilities such as customer deposits are included in a taxpayer's rate base. In such situations, a ratemaking commission may reduce the overall rate of return on account of the zero-cost capital (*e.g.*, deferred taxes or non-interest-bearing liabilities) included in rate base. The issue raised by the public comments is whether the rate of return assigned to the credit under section 46(f)(2)(B) may also be reduced on account of such zero-cost capital.

The proposed regulations provided that the cost of capital assigned to the credit must be at least equal to the overall cost of the capital, determined on the basis of a weighted average, that would have been provided by common and preferred shareholders and long-term creditors if the credit were unavailable. Under the proposed regulations, the composition of such capital depended, generally on all the relevant facts and circumstances; however, a safe-harbor provision permitted determinations that additional capital would have been provided in the same proportions and at the same rates of return as the capital actually provided by shareholders and long-term creditors. Neither the general rule nor the safe-harbor provision of the proposed regulations would have permitted any reduction in the rate of return assigned to the investment credit on account of zero-cost capital. This position was based on the assumption that items of zero-cost capital would not increase if the credit were unavailable.

After consideration of the comments the Service has concluded that, although this assumption regarding zero-cost capital is generally true, it is not strictly correct in certain situations. For example, if the basis of a utility's property has been reduced under section 48(q), the additional capital provided if the credit were unavailable would include not only equity and long-term debt, but also deferred taxes. This occurs because the utility's basis in the property would increase if the credit were unavailable, eventually resulting in a greater amount of deferred taxes. Accordingly, the final regulations permit zero-cost capital to be taken into account for purposes of determining the cost of capital assigned to the credit, but only to the extent that additional amounts of such capital would be provided if the credit were unavailable. In the case of a utility that has a basis reduction under section 48(q), for example, the amount of capital provided in the form of deferred taxes will, as explained above, generally be less in each period than the amount of deferred taxes that would be provided if the credit were unavailable. For any period, the difference between these two amounts is the amount of additional deferred taxes that would be provided if the credit were unavailable. The regulations provide that only the amount of additional deferred taxes for a period may be taken into account in determining the rate of return assigned to the credit for that period. Thus, the deferred taxes actually included in the utility's rate base may not be taken into account for this purpose. Under the regulations, any amount of additional zero-cost capital must also be taken into account for purposes of determining the amount of additional interest that the taxpayer would pay or accrue if the credit were unavailable, thus reducing the amount subject to interest synchronization.

The Service continues to believe that additional capital typically would be provided primarily in the form of equity and long-term debt if the credit were unavailable. Accordingly, the safe-harbor provision of the proposed regulations is generally unchanged, except to clarify that the safe harbor applies only if it is used to determine both the cost of capital assigned to the credit and the amount subject to interest synchronization.

HYPOTHETICAL CAPITAL STRUCTURE

An additional issue raised by the public comments concerned the effect of using a hypothetical capital structure to determine a utility's overall rate of return. A hypothetical capital structure may be used if, for example, a regulatory commission determines that the actual capital structure of a utility does not include sufficient debt and imputes debt of a parent holding company to the utility. The issue in such cases is whether the composition of the capital that would be provided if the credit were unavailable is determined by reference to the change that would occur in the actual capital structure of the utility or, instead, by reference to the change in the hypothetical capital structure used by the ratemaking commission. The final regulations clarify that it is the change in the hypothetical capital structure that is taken into account for this purpose.

TRANSITIONAL RULE

The Service received a number of inquiries requesting clarification of the transitional rule in §1.46-6(b)(iii) of the proposed regulations. In general, this rule (as revised by this Treasury decision) provides that rate orders put into effect before June 23, 1986, do not violate section 46(f) if they satisfy the requirements of either the amended regulations or the regulations in effect before the amendment. This is significant because the regulations in effect before the amendment provided that the overall cost of capital rate depends on the practice of the regulatory body. The Internal Revenue Service is aware that certain ratemaking commissions, relying on this language, have required utilities to use zero-cost capital in determining the earnings rate to be assigned to the credit in a manner inconsistent with the amended regulations. The use of zero-cost capital in such cases will not be treated as a violation of section 46(f)(2) under the regulations in effect before the amendments.

AMENDMENTS NOT COVERED BY THESE PROPOSED REGULATIONS

The amendments do not reflect amendments made to section 46 after the enactment of the Revenue Act of 1971, other than the redesignation of section 46(e) as section 46(f) by the Tax Reduction Act of 1975. In addition, the regulations do not reflect the amendment made to section 167(l)(2)(C) by section 209(d)(3) of the Economic Recovery Tax Act of 1981 (Pub. L. 97-34; 95 Stat. 227). That amendment has the effect of eliminating the special rule for immediate flow-through under section 46(f)(3) for property placed in service after December 31, 1980.

REGULATORY FLEXIBILITY ACT; EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required. Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, the final regulations are not subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is Paulette Chernyshev of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

Amendments to the Regulations

Accordingly, 26 CFR Part 1 is amended as follows:

INCOME TAX REGULATIONS
(26 CFR Part 1)

Paragraph 1. The authority for Part I is amended by adding the following citation:

Authority: 26 U.S.C. 7805. *** Section 1.46-6 also issued under 26 U.S.C. 46(f)(7).

Par. 2. Section 1.46-6 is amended by revising paragraph (b)(2)(i), (3) and (4)(ii) to read as follows:

§1.46-6 Limitation in case of certain regulated companies.

* * * * *

(b) *Definitions.* ***

(2) *Cost of service.* (i) (A) For purposes of this section, "cost of service" is the amount required by a taxpayer to provide regulated goods or services. Cost of service includes operating expenses (including salaries, cost of materials, etc.) maintenance expenses, depreciation expenses, tax expenses, and interest expenses. For purposes of this section, any effect on a taxpayer's permitted return on investment that results from a reduction in the taxpayer's rate base does not constitute a reduction in cost of service, even though, as a technical ratemaking term, "cost of service" ordinarily includes a permitted return on investment. In addition, taking into account a deduction for the additional interest that the taxpayer would pay or accrue if the credit were unavailable in determining Federal income tax expense ("synchronization of interest") does not constitute a reduction in cost of service for purposes of section 46(f)(2). This adjustment to Federal income tax expense may be taken into account in determining cost of service for the regulated accounting period or periods that include the taxable year to which the adjustment relates or for any subsequent regulated accounting period.

(B) See paragraph (b)(3)(ii)(B) of this section for rules relating to the amount of additional interest that the taxpayer would pay or accrue if the credit were unavailable.

* * * * *

(3) *Rate base.* (i) For purposes of this section, "rate base" is the monetary amount that is multiplied by a rate of return to determine the permitted return on investment.

(ii) (A) In determining whether, or to what extent, a credit has been used to reduce rate base, reference shall be made to any accounting treatment that affects rate base. In addition, in those cases in which the rate of return is based on the taxpayer's cost of capital, reference shall be made to any accounting treatment that reduces the permitted return on investment by treating the credit less favorably than the capital that would have been provided if the credit were unavailable. Thus, the credit may not be assigned a "cost of capital" rate that is less then the overall cost of capital rate, determined on the basis of a weighted average, for the capital that would have been provided if the credit were unavailable.

(B) For purpose of determining the cost of capital rate assigned to the credit and the amount of additional interest that the taxpayer would pay or accrue, the composition of the capital that would have been provided if the credit were unavailable may be determined—

(1) On the basis of all the relevant facts and circumstances; or

(2) By assuming for both such purposes that such capital would be provided solely by common shareholders, preferred shareholders, and long-term creditors in the same proportions and at the same rates of return as the capital actually provided to the taxpayer by such shareholders and creditors.

For purposes of this section, capital provided by long-term creditors does not include deferred taxes as described in section 167(l)(3)(G) or 168(e)(3)(B)(ii).

(C) If a taxpayer's overall rate of return is based on a deemed or hypothetical capital structure, paragraph (b)(3)(ii)(B) of this section shall be applied by treating the deemed or hypothetical capital as if it were the capital actually provided to the taxpayer and determining the composition of the capital that would have been provided if the credit were unavailable in a manner consistent with such treatment.

(iii) Whether, or to what extent, a credit has been used to reduce rate base for any period to which pre-June 23, 1986 rates apply will be determined under 26 CFR 1.46-6(b)(3) and (4) (revised as of April 1, 1985) if such a determination avoids disallowance of a credit that would be disallowed under paragraph (b)(3)(ii) or (4)(ii) of this section. For this purpose, a period to which pre-June 23, 1986 rates apply is any period for which the effect of the credit on rate base for ratemaking purposes is established under a determination put into effect (within the meaning of paragraph (f) of this section) before June 23, 1986.

(4) *Indirect reductions to cost of service or rate base.****

(ii) One type of such indirect reduction is any ratemaking decision in which the credit is treated as operating income (subject to ratemaking regulation) or is treated less favorably than the capital that would have been provided if the credit were unavailable. For example, if the credit is accounted for as nonoperating income on a company's regulated books of account but a ratemaking decision has the effect of treating the credit as operating income in determining rate of return to common shareholders, then cost of service has been indirectly reduced by reason of the credit.

* * * * *

Roscoe L. Egger, Jr.
Commissioner of
Internal Revenue.

Approved May 5, 1986.

J. Roger Mentz,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on May 21, 1986, 8:45 a.m., and published in the issue of the Federal Register for May 22, 1986, 51 F.R. 18775)

Section 117.—Scholarships and Fellowship Grants

26 CFR 1.117-1: Exclusion of amounts received as a scholarship or fellowship grant.

Whether certain grants made by private foundations for the education of children of employees of particular companies are scholarships within the meaning of section 117(a) for purposes of determining whether the foundation's grant program satisfies section 4945(g)(1) of the Code. See Rev. Rul. 86-90, page 12.

Section 280F.—Limitation of Investment Tax Credit and Depreciation for Luxury Automobiles; Limitation Where Certain Property Used for Personal Purposes

26 CFR 1.280F-5T: Leased property.

Investment credit; leased automobiles. Rules are provided for a lessee of a passenger automobile who, for purposes of claiming an investment tax credit, is treated as having acquired the automobile.

Rev. Rul. 86–87

This revenue ruling provides rules under section 280F of the Internal Revenue Code for a lessee of a passenger automobile who, for purposes of claiming an investment tax credit, is treated as having acquired the automobile. Taxpayers may rely on these rules until the Temporary Income Tax Regulations under section 280F, published in the Federal Register on October 24, 1984, and amended on November 6, 1985, are further amended to incorporate the provisions of this revenue ruling.

BACKGROUND

As added by section 179 of the Tax Reform Act of 1984 ("the 1984 Act"), 1984–3 (Vol.1) C.B. 221, and amended by section 4 of the Repeal of the Contemporaneous Recordkeeping Requirements (the "1985 Act"), 1985–2 C.B. 350, section 280F of the Code limits the amount of investment tax credit and annual depreciation deductions allowed for a passenger automobile placed in service or leased after June 18, 1984. Section 280F also provides for the Internal Revenue Service to prescribe tables that impose on lessees of passenger automobiles limitations "substantially equivalent" to the limitations imposed on similarly situated owners of passenger automobiles.

On October 19, 1984, pursuant to this requirement, the Service issued section 1.280F–5T of the temporary regulations. Section 1.280F–5T(d)(1) of the temporary regulations requires a lessee of a passenger automobile to include in gross income an amount based on the fair market value of the automobile and the lessee's amount of business use. By offsetting the lessee's deduction for lease payments, this inclusion approximates the present value of the limitations imposed on the investment tax credit and annual depreciation deductions of a similarly situated owner.

The 1985 Act further limited the amount of investment tax credit and annual depreciation deductions allowable for passenger automobiles placed in service after April 2, 1985. The limitations on lessees, therefore, were correspondingly made more stringent by amendments to the temporary regulations under section 280F published in the Federal Register on November 6, 1985. The new limitations, which are contained in section 1.280F–5T(e), are applicable to passenger automobiles leased after April 2, 1985.

Neither the limitations issued in October 1984 nor the limitations issued on November 1985 account for situations in which a lessor elects under section 48(d) to treat the lessee as having acquired the automoble, thus allowing the lessee to claim the investment credit. The limitations applicable under section 280F to lessees of passenger automoblies to whom lessors pass through the investment credit are set forth in this revenue ruling.

For purposes of this revenue ruling, the terms "lease term" and "fair market value" shall have the meanings provided by section 1.280F–5T(h) of the temporary regulations.

HOLDINGS

Section 1.

This section applies to any taxpayer—

(a) Who leased a passenger automobile after June 18, 1984, but before April 3, 1985, unless (1) a binding contract to lease the passenger automobile was in effect on June 18, 1984, and at all times thereafter, and (2) the lessee first used the automobile before January 1, 1985, and

(b) Who claims the investment tax credit with respect to that automobile.

Instead of the amount determined under section 1.280F–5T(d)(1)(i), the inclusion amount for each of the first three taxable years during which the automobile is leased is 3.5 percent of the excess of the automobile's fair market value over $16,500, multiplied by the percentage of business use for the taxable year and prorated for the number of days of the lease term included in the taxable year. The inclusion amounts for the years subsequent to the third taxable year during which such automobile is leased are determined under subdivisions (ii), (iii), and (iv), and the flush provisions of section 1.280F–5T(d)(1).

Section 2.

(a) This section applies to any taxpayer—

(1) Who leases a passenger automobile after April 2, 1985, unless (i) a binding contract to lease the passenger automobile was entered into no later than April 2, 1985, and was in effect at all times thereafter, and (ii) the lessee first used the automobile before August 1, 1985, and

(2) Who claims the investment tax credit with respect to that automobile.

(b) The inclusion amount for each of the first three taxable years during which the automobile is leased is based on the fair market value of the automobile, the lessee's amount of business use, the quarter of the taxable year during which the automobile is first used under the lease. For any passenger automobile that has a fair market value not greater than $50,000, this inclusion amount is determined by using the table below instead of the table provided in section 1.280F–5T(e)(2) of the temporary regulations. The inclusion amount is computed as follows:

(1) For the appropriate range of fair market values, select the dollar amount from the column for the quarter of the taxable year in which the automobile is first used under the lease,

(2) Prorate the dollar amount for the number of days of the lease term included in the taxable year, and

(3) Multiply the prorated dollar amount by the percentage of business use for the taxable year.

INCLUSION AMOUNTS: YEARS 1–3

Fair Market Value			Taxable year quarter		
Greater than	But not greater than	Fourth	Third	Second	First
$11,250	$11,500	$ 0	$ 0	$ 0	$ 0
11,500	11,750	0	0	0	0
11,750	12,000	0	0	0	0
12,000	12,250	0	0	0	0
12,250	12,500	0	0	0	0
12,500	12,750	0	0	0	0
12,750	13,000	0	0	0	0
13,000	13,250	0	0	0	0
13,250	13,500	9	8	7	6
13,500	13,750	21	18	16	15
13,750	14,000	33	29	26	24
14,000	14,250	45	40	36	32
14,250	14,500	57	51	45	41
14,500	14,750	69	61	55	50
14,750	15,000	81	72	65	59

INCLUSION AMOUNTS: YEARS 1–3 (Continued)

Fair Market Value		Taxable year quarter			
Greater than	But not greater than	Fourth	Third	Second	First
15,000	15,250	94	83	74	68
15,250	15,500	106	94	84	76
15,500	15,750	118	105	94	85
15,750	16,000	130	115	103	94
16,000	16,250	142	126	113	103
16,250	16,500	154	137	123	111
16,500	16,750	166	148	132	120
16,750	17,000	179	158	142	129
17,000	17,500	197	175	156	142
17,500	18,000	221	196	176	160
18,000	18,500	245	218	195	177
18,500	19,000	270	239	214	195
19,000	19,500	294	261	234	212
19,300	20,000	318	282	253	230
20,000	20,500	343	304	272	247
20,500	21,000	367	325	291	265
21,000	21,500	391	347	311	283
21,500	22,000	416	369	330	300
22,000	23,000	452	401	359	326
23,000	24,000	501	444	398	362
24,000	25,000	549	487	436	397
25,000	26,000	598	530	475	432
26,000	27,000	646	573	513	467
27,000	28,000	695	616	552	502
28,000	29,000	744	659	591	537
29,000	30,000	792	703	629	572
30,000	31,000	841	746	668	607
31,000	32,000	889	789	706	642
32,000	33,000	938	832	745	677
33,000	34,000	987	875	784	713
34,000	35,000	1035	918	822	748
35,000	36,000	1084	961	861	783
36,000	37,000	1132	1004	899	818
37,000	38,000	1181	1047	938	853
38,000	39,000	1230	1090	977	888
39,000	40,000	1278	1134	1015	923
40,000	41,000	1327	1177	1054	958
41,000	42,000	1375	1220	1092	993
42,000	43,000	1424	1263	1131	1028
43,000	44,000	1473	1306	1170	1064
44,000	45,000	1521	1349	1208	1099
45,000	46,000	1570	1392	1247	1134
46,000	47,000	1618	1435	1285	1169
47,000	48,000	1667	1478	1324	1204
48,000	49,000	1716	1521	1363	1239
49,000	50,000	1764	1565	1401	1274

(c) For any passenger automobile which has a fair market value greater than $18,000, but not greater than $50,000, and for which the lessee claims the investment credit, the inclusion amounts for the fourth, fifth, and sixth taxable years during which the automobile is leased are determined under section 1.280F–5T(e)(3) of the temporary regulations.

(d) For any passenger automobile which has a fair market value greater than $50,000 and for which the lessee claims the investment credit, the inclusion amount for the first three taxable years during which the automobile is leased is determined according to the formulas below instead of those provided in section 1.280F–5T(e)(4)(ii)(A) through (D) of the temporary regulations.

(1) The inclusion amount is computed as follows:

(i) Determine the dollar amount by using the appropriate formula below,

(ii) Prorate the dollar amount for the number of days of the lease term included in the taxable year.

(iii) Multiply this dollar amount by the percentage of business use for the taxable year.

(2) The dollar amount is computed as follows:

(i) If the automobile is first used under the lease in the fourth quarter of a taxable year, the dollar amount for each of the first three taxable years during which the automobile is leased is 5 percent of the excess of the automobile's fair market value over $13,200.

(ii) If the automobile is first used under the lease in the third quarter of a taxcble year, the dollar amount for each of the first three taxable years during which the automobile is leased is 4.5 percent of the excess of the automobile's fair market value over $13,200.

(iii) If the automobile is first used under the lease in the second quarter of a taxable year, the dollar amount for each of the first three taxable years during which the automobile is leased is 4 percent of the excess of the automobile's fair market value over $13,200.

(iv) If the automobile is first used under the lease in the first quarter of a taxable year, the dollar amount for each of the first three taxable years during which the automobile is leased is 3.5 percent of the excess of the automobile's fair market value over $13,200.

(e) For any passenger automobile which has a fair market value greater than $50,000 and for which the lessee claims the investment credit, the inclusion amounts for the fourth, fifth, and sixth taxable years during which the automobile is leased are determined under section 1.280F–5T(e)(4)(ii)(E), (F), and (G), respectively, of the temporary regulations.

(f) (1) For any passenger automobile which has a fair market value less than or equal to $32,400 and for which the lessee claims the investment credit, the inclusion amount for the seventh and subsequent taxable years during which the automobile is leased is zero.

(2) For any passenger automobile which has a fair market value greater than $32,400 and for which the lessee claims the investment credit, the inclusion amount for the seventh and subsequent taxable years during which the automobile is leased is determined under section 1.280F–5T(e)(5)(ii) of the temporary regulations.

Section 1033.—Involuntary Conversions

26 CFR 1.1033(b)–1: Basis of property acquired as a result of an involuntary conversion.

Whether the basis on new section 38 property acquired to replace property destroyed in a casualty must be reduced for purposes of computing the investment tax credit by the amount of gain deferred under section 1033(a)(2) of the Code. See Rev. Rul. 86–89, page 4.

Section 3101.—Rate Of Tax

26 CFR 31.3101–2: Rates and computation of employee tax.

Extension of the hospital insurance (medicare) tax to the wages of newly hired employees of states and political subdivisions. See Rev. Rul. 86–88, below.

Section 3111.—Rate Of Tax

26 CFR 31.3111–2: Rates and computation of employer tax.

Extension of the hospital insurance (medicare) tax to the wages of newly hired employees of states and political subdivisions. See Rev. Rul. 86–88, below.

Section 3121.—Definitions

(Also Sections 3101, 3111; 31.3101–2, 31.3111–2.)

FICA; hospital insurance; extension to state and political subdivision employees.

Guidelines, in question and answer form, relate to the amendment of section 3121(u) of the Code that extends the hospital insurance (medicare) tax portion of the Federal Insurance Contribution Act (FICA) to wages of newly hired employees of states and political subdivisions.

Rev. Rul. 86–88

Section 13205 of the Consolidated Omnibus Budget Reconciliation Act of 1985 (the Act), amended section 3121(u) of the Internal Revenue Code. In general, the amendment applies sections 3101(b) and 3111(b), the hospital insurance (medicare) tax portion of the Federal Insurance Contributions Act (FICA), to wages for services rendered after March 31, 1986, by newly hired employees of states and political subdivisions. Previously most employees of states and political subdivisions were not covered under the FICA, as their services were excepted from the term "employment" by section 3121(b)(7).

This revenue ruling provides guidelines concerning the applicability of the medicare tax to employees of states and political subdivisions.

For purposes of this revenue ruling, the term "state" includes the Commonwealth of Puerto Rico, the Virgin Islands, and the District of Columbia.

For purposes of this revenue ruling, the term "political subdivision" has the same meaning that it has under section 218(b)(2) of the Social Security Act, 42 U.S.C. section 418(b)(2). Thus, "political subdivision" ordinarily includes a county, city, town, village, or school district. In many states, depending upon the manner in which such entities are created under state law, "political subdivision" includes a sanitation, utility, reclamation, improvement, drainage, irrigation, flood control, or similar district.

For purposes of this revenue ruling, the term "state employer" of a state includes the state and any agency or instrumentality of that state that is a separate employer for purposes of withholding, paying, and reporting the federal income taxes of employees. The term "political subdivision employer" of a political subdivision includes the political subdivision and any agency or instumentality of that political subdivision that is a separate employer for purposes of withholding, reporting, and paying the federal income taxes of employees.

Services Subject to the Medicare Tax

Q1. What services are subject to the medicare tax under the Act?

A1. As a general rule, services performed for a state employer or political subdivision employer by an employee hired by the state employer or political subdivision employer after March 31, 1986, are subject to the medicare tax. The following services, however, are *not* subject to the medicare tax even though the services are performed by an employee hired after March 31, 1986:

(1) services covered by an agreement between the state and the Secretary of Health and Human Services entered into pursuant to section 218 of the Social Security Act, 42 U.S.C. section 418 (218 agreement) providing for social security coverage including medicare,

(2) services excluded from the definition of employment under any provision of section 3121(b) of the Code other than section 3121(b)(7),

(3) services performed by an individual who is employed by a state employer (except for a District of Columbia employer) or a political subdivision employer to relieve the individual of unemployment,

(4) services performed in a hospital, home, or other institution by a patient or inmate thereof as an employee of a state employer or a political subdivision employer,

(5) services performed by an individual as an employee of a state employer or a political subdivision employer serving on a temporary basis in case of fire, storm, snow, earthquake, flood, or other similar emergency, or

(6) services performed by any individual as an employee included under section 5351(2) of title 5, United States Code (relating to certain interns, student nurses, and other student employees of the District of Columbia government), other than as a medical or dental intern or a medical or dental resident in training.

The Continuing Employment Exception

Q2. If an employee was hired before April, 1986, by a state employer or political subdivision employer and services are performed for the state employer or political subdivision employer by that employee after March 31, 1986, are those services subject to the medicare tax?

A2. Services are not subject to the tax if they are performed after March 31, 1986, for a state employer or political subdivision employer by an employee who was hired by the state employer or the political subdivision employer before April 1, 1986, and if the employee meets the following requirements:

(i) the employee was performing regular and substantial services for remuneration for the state employer or political subdivision employer before April 1, 1986,

(ii) the employee was a bona fide employee of that employer on March 31, 1986,

(iii) the employment relationship with that employer was not entered into for purposes of avoiding the medicare tax, and

(iv) the employment relationship of the employee with that employer has not been terminated after March 31, 1986 (other than as provided in the rules described in Q&A7 below, which concern employees who transfer from one state employer, or one political subdivision employer, to another).

Section 3121(u)(2)(C) of the Code.

For purposes of this revenue ruling, this exception to the medicare tax is called the "continuing employment exception."

Q3. An employee signed an employment contract before April 1, 1986, but did not begin to perform services until after March 31, 1986. Does the employee qualify for the continuing employment exception?

A3. No. The employee does not qualify for the continuing employment exception because the employee was not performing regular and substantial services for remuneration before April 1, 1986. Section 3121(u)(2)(C)(ii)(I) of the Code.

Q4. Before April 1, 1986, an individual was performing services for remuneration as a substitute teacher on an "as needed" basis for a state employer or a political subdivision employer, as the individual continued performing those services on that basis after March 31, 1986. Does the individual qualify for the continuing employment exception?

A4. No. The individual does not qualify for the continuing employment exception. Even though the services performed may have been substantial, the services were not regular because they were performed on an "as needed" basis. Section 3121(u)(2)(C)(ii)(I) of the Code.

Q5. *A* was a state employee performing regular and substantial services for remuneration prior to April 1, 1986. *A*'s employment relationship with the state employer was terminated after March 31, 1986, but *A* was later rehired by the state employer. Does the continuing employment exception apply to *A*?

A5. No. Section 3121(u)(2)(C)(iii) of the Code.

Q6. How is termination of employment defined for purposes of determining whether the medicare tax is applicable?

A6. The question of whether an employment relationship has terminated is a question of fact that must be determined on the basis of all the relevant facts and circumstances. Great weight, however, will be given to the personnel rules of the state employer or political subdivision employer to determine if an employment relationship has been terminated.

Q7. An employee who was hired before April 1, 1986, by a state employer transferred after March 31, 1986, to another state employer of that state. The transfer was made without a termination of the employee's overall employment relationship with that state. Does the employee qualify for the continuing employment exception?

A7. Yes. An employee hired before April 1, 1986, by a state employer who transfers after March 31, 1986, to another state employer of that state may qualify for the continuing employment exception, provided the transfer was made without a termination of the employee's overall employment relationship with that state. The same rule applies to an employee hired before April 1, 1986, by a political subdivision employer, who transfers after March 31, 1986, to another political subdivision employer of that political subdivision.

On the other hand, an employee hired before April 1, 1986, does not qualify for the continuing employment exception if after March 31, 1986, the employee transfers from a state employer to a political subdivision employer or from a political subdivision employer to a state employer. Likewise, an employee does not qualify for the exception if the employee transfers from a political subdivision employer in one political subdivision to a political subdivision employer in a different political subdivision, or from a state employer in one state to a state employer in a different state. Section 3121(u)(2)(D) of the Code.

Different rules, however, control whether a transfer affects an employee's status for purposes of the medicare tax wage base. In the case of an employee who is subject to the medicare tax, even if the employee transfers from one state employer to another state employer of that state or from one political subdivision employer to another political subdivision employer of that political subdivision, a new medicare tax wage base applies to wages received from the second employer. Thus, the rules that determine whether there is a new medicare tax wage base are the same as those applicable to employees of private employers.

Services Excluded from Employment

Q8. What services are excluded from the definition of employment?

A8. See sections 3121(b)(1)–(6), (8)–(20) of the Code for a list of services that are excluded from the definition of employment for purposes of the social security taxes, including the medicare portion of the taxes.

Q9. A 218 agreement may contain terms optionally excluding from social security coverage certain types of employment. 42 U.S.C. section 418(c)(3). If employment is optionally excluded from coverage under the terms of a 218 agreement, is that employment subject to the medicare tax if services are performed by an individual otherwise subject to the medicare tax under the rules of Q&A1 and Q&A2?

A9. Yes. The optionally excluded services are subject to the medicare tax if they are performed by an individual otherwise subject to the tax under the rules of Q&A1 and Q&A2 above.

Q10. A student is hired by school, college, or university after March 31, 1986, to perform services of the school, college, or university. The student is in a group optionally excluded from coverage under the terms of an applicable 218 agreement. Are the services performed by the student subject to the medicare tax?

A10. Services performed by a student employed by a school, college, or university are not subject to the medicare tax *if* the student is enrolled and regularly attending classes at the school, college, or university. Section 3121(b)(10) of the Code. Services of a student that are subject to contributions under a 218 agreement continue to be subject to such contributions.

Definition of Wages

Q11. Is the definition of wages for medicare tax purposes the same as the definition of wages for making social security contributions under 218 agreements?

A11. No, not in all cases. The term "wages" for purposes of paying medicare tax is defined by section 3121(a) of the Code. The term "wages" for purposes of making contributions under a 218 agreement is defined by section 209 of the Social Security Act. 42 U.S.C. section 409. Questions concerning the definition of wages (and employment) for purposes of paying medicare tax should be directed to the Service. Questions concerning the definition of wages (and employment) for purposes of making 218 contributions should be directed to the Social Security Administration (SSA).

Rules for Reporting and Payment of Medicare Tax

Q12. Is the medicare tax reported and paid to the Internal Revenue Service or to the SSA?

A12. The medicare tax is reported and paid to the Service (1) by a state employer of a state if on April 7, 1986, *no* employee of any state employer of that state was covered under a 218 agreement, and (2) by a political subdivision employer of a political subdivision if on April 7, 1986, *no* employee of any political subdivision employer of a political subdivision employer of that political subdivision was covered under a 218 agreement.

The medicare tax is reported and paid to the state Social Security Administrator (1) by a state employer of a state if on April 7, 1986, *any* employee of any state employer of that state was covered under a 218 agreement, and (2) by a political subdivision employer of a political subdivision if on April 7, 1986, *any* employee of any political subdivision employer of that political subdivision was covered under a 218 agreement.

Q13. A 218 agreement was in effect with state *X* on or before April 7, 1986. The agreement provided for coverage of employees of a political subdivision employer of political subdivision *A* but not for coverage of any employee of any political subdivision employer of political subdivision *B*. After April 7, 1986, a modification of the 218 agreement was executed providing for coverage of some, but not all, employees of a political subdivision employer of political subdivision *B*. The effective date of the new coverage was April 1, 1986. When that political subdivision employer of political subdivision *B* reports and pays the medicare tax on wages for services performed by those of its employees who are not subject to the modification, is the tax reported and paid to the state Social Security Administrator or to the Internal Revenue Service?
A13. The tax is reported and paid to the Internal Revenue Service. Modifying a 218 agreement after April 7, 1986, to extend coverage on a retroactive basis does not change the agency to which the employer must report and pay the medicare tax for services performed by employees who are subject to the medicare tax.

Q14. How is the medicare tax reported and paid to the Internal Revenue Service?
A14. Taxable wages must be reported on line 6 of Form 941E, Quarterly Return of Withheld Federal Income Tax and Hospital Insurance (Medicare) Tax. The reporting, depositing, and paying of the medicare tax are subject to the same rules applicable to private employers. These rules are similar to those applicable to income tax withholding.

Q15. How is the medicare tax reported and paid to the SSA?
A15. The medicare tax is reported and paid to the SSA just as contributions under a 218 agreement are reported and paid to the SSA.

Q16. Will all penalties for failure to pay the medicare tax and failure to make timely deposits of the tax be assessed against state and political subdivision employers?
A16. The Service will waive penalties for failure to pay and for failure to make timely deposits of the medicare tax with respect to services performed through the fourth quarter of 1986, so long as all payments due for April through December of 1986 are paid by February 2, 1987. If all payments due for April through December 1986 are not paid by February 2, 1987, this automatic waiver of penalties is not applicable, even with respect to amounts paid by February 2, 1987. Penalties may be waived, however, if the employer shows reasonable cause for failure to pay and failure to make timely deposits of the tax. See sections 6651 and 6656 of the Code. A state employer or political subdivision employer should not report any medicare tax wages on line 6 of Form 941E for the second or third quarter unless appropriate deposits and/or payments are made for that quarter.

Q17. If a state employer or a political subdivision employer has federal employees on the state or political subdivision payroll, how should that employer report the full social security tax or the medicare portion of the social security tax, whichever is applicable?
A17. The state employer or political subdivision employer should use Form 941E to report the full social security taxes and/or the medicare portion of the taxes. For those federal employees subject to the *full* social security taxes, the tax must be included with the withheld federal income tax on line 3 of Form 941E, with an attached supporting statement showing the amount of wages subject to the social security taxes, the amount of the taxes withheld, and the employer's share of the taxes. For those federal employees subject *only* to the medicare portion of the social security taxes, the medicare tax must be reported on line 6 of Form 941E.

Q18. If a state employer or a political subdivision employer must report and pay the medicare tax to the Service as explained in Q&A12, how should the employer transmit Copy A of Forms W-2 for newly hired employees who are subject to the medicare tax?
A18. For newly hired employees subject to the medicare tax, the employer should transmit Copy A of Forms W-2 with a Form W-3, Transmittal of Income and Tax Statements, and should check the "Medicare Fed. emp." checkbox in Box 2 on the Form W-3. This checkbox will be changed to "Medicare government employee" on the 1987 Form W-3 to reflect the extension of the medicare tax to state and political subdivision employees. For employees not subject to the medicare tax, the employers should follow the current practice of transmitting Copy A of Forms W-2 with a Form W-3, checking the "941/941E" checkbox in Box 2 on the Form W-3.

Q19. If a state employer or a political subdivision employer must report and pay the medicare tax to the state Social Security Administrator as explained in Q&A12, how should the employer transmit Copy A of Forms W-2 for newly hired employees subject to the medicare tax?
A19. For newly hired employees subject to the medicare tax, the employer should transmit Copy A of Forms W-2 with a Form W-3 S&L, Transmittal of Income and Tax Statements for State and Local Governmental Employers, and should check the "Medicare Government Employee" checkbox on the Form W-3 S&L *in addition to* the "Section 218" checkbox. For those employees covered under a 218 agreement, the state employer or the political subdivision employer should follow the current practice of transmitting the Forms W-2 with a Form W-3 S&L, checking the "Section 218" checkbox in Box 2 on the Form W-3 S&L. If the employer also has employees who are not covered under the 218 agreement and who were hired before April 1, 1986, then for those employees, the employer should transmit Forms W-2 with a Form W-3 and should check the "941/941E" box on the Form W-3.

Section 4945.—Taxes on Taxable Expenditures

26 CFR 53.4945-4: Grants to individuals.
(Also Section 117; 1.117-1.)

Private foundations; taxable expenditures; scholarship grants. Grants awarded by a private foundation under an employer-related program are scholarships under section 117(a) of the Code even though the grants will be awarded without regard to the percentage guidelines of section 4.08 of Rev. Proc. 76-47. Therefore, grants awarded under the program will be described in section 4945(g)(1) and will not be taxable expenditures under section 4945(d)(3).

Rev. Rul. 86-90

ISSUE

Are grants awarded under the program described below scholarships under section 117(a) of the Internal Revenue Code and, therefore, not taxable expenditures under section 4945(d)(3), even though the grants are awarded without regard to the percentage guidelines of section 4.08 of Rev. Proc. 76–47, 1976–2 C.B. 670?

FACTS

Foundation *X* is exempt from federal income tax under section 501(c)(3) of the Code and is a private foundation within the meaning of section 509(a). *X* has applied under section 4945(g) for approval of its proposed college scholarship program. *X* proposes to award one grant per year to a student to attend an educational organization described in section 170(b)(1)(A)(ii). The grant is a small, fixed amount and may be used to pursue any course of study leading to a degree. The student will be selected from the children of employees of company *M* on an objective basis using the criteria of financial need or academic ability. *M* has 3,000 employees of diverse ages and occupations. No fact about *M* or the plan, such as seasonal employment, extensive use of independent contractors, or an unusually large number of employees without children of qualifying age, disqualifies a significant number of persons who serve the company.

X's program will be conducted in accordance with the guidelines of sections 4.01 through 4.07 of Rev. Proc. 76–47. However, *X* will award its one grant per year without regard to the percentage limitation guidelines of section 4.08 of Rev. Proc. 76–47. *X* cannot guarantee that the program will meet these guidelines each year. *X* reasonably believes that the program will satisfy the ten percent test of section 4.08 each year, but has not determined whether the program will in fact meet that test, because although it knows the number of employees' children who graduate from high school, it does not know how many of those enter a degree program. Further, *X* reasonably believes that the expense involved in making the determination of the number of children of employees entering a degree program is not justified in light of the small amount awarded in the grant program. Although *X* will undertake reasonable efforts to secure sufficient applications to satisfy the 25 percent test of section 4.08, *X* also anticipates that in some years the number of eligible applicants will be insufficient to satisfy that test because its program provides only one grant annually of a small, fixed amount. *X* has demonstrated that its applicants and grantees will not be drawn from a specific group of employees.

LAW

Section 4945 of the Code imposes a tax on each taxable expenditure made by a private foundation.

Section 4945(d)(3) of the Code provides that the term "taxable expenditure" includes any amount paid or incurred by a private foundation as a grant to an individual for study or other similar purpose, except as provided in section 4945(g).

Section 4945(g)(1) of the Code provides that a grant to an individual for study that is made on an objective and nondiscriminatory basis pursuant to a procedure approved in advance by the Secretary is not a taxable expenditure under section 4945(d)(3) if it is demonstrated to the satisfaction of the Secretary that the grant constitutes a scholarship or fellowship grant which is subject to the provisions of section 117(a) and is to be used for study at an educational organization described in section 170(b)(1)(A)(ii).

Section 117(a) of the Code provides, with certain limitations, that an individual's gross income does not include any amount received and expended as a scholarship at an educational organization described in section 170(b)(1)(A)(ii) or as a fellowship grant.

Rev. Proc. 76–47, 1976–2 C.B. 670, provides guidelines for determining whether a grant made by a private foundation under an employer-related grant program to a child of an employee of the particular employer to which the program relates is a scholarship or fellowship grant subject to the provisions of section 117(a) of the Code.

Section 4.08 of Rev. Proc. 76–47 provides a percentage test guidelines. It states that in the case of a program that awards grants to children of employees of a particular employer, the program meets the percentage test if the number of grants awarded under that program in any year to such children does not exceed 25 percent of the number of employees' children who (i) were eligible, (ii) were applicants for such grants, and (iii) were considered by the selection committee in selecting the recipients of grants in that year; or ten percent of the number of employees' children who can be shown to be eligible for grants (whether or not they submitted an application) in that year.

As stated in section 4 of Rev. Proc. 76–47, if a private foundation's program satisfies the seven conditions set forth in sections 4.01 through 4.07, but does not meet the percentage test of section 4.08 applicable to grants to employees' children, the question whether the grants are scholarships or fellowship grants subject to the provisions of section 117(a) of the Code will be resolved on the basis of all the facts and circumstances. In making this determination, the Service will consider as a substitute for the percentage test of section 4.08 all the relevant facts and circumstances to determine whether the primary purpose is to educate recipients in their individual capacities. These facts and circumstances will be considered in the context of the probability that a grant will be available to any eligible applicant.

Such relevant facts and circumstances may include: the likelihood that the program may be used for employee recruitment or to retain employees, the independence of the selection committee, standards for scholarship eligibility and selection, limitations on the recipient's choice of course of study, the number of grants available, the number of children of employees who would be eligible for them, the percentage of eligible children of employees applying for grants who normally (*i.e.*, on an average basis) receive grants under the program, and whether and how many grants are awarded to individuals who are not children of employees.

ANALYSIS

In applying Rev. Proc. 76–47, it is assumed that the program is conducted on an objective and nondiscriminatory basis (within the meaning of section 4945(g) of the Code section 53.4945–4(b) of the Foundation and Similar Excise Tax Regulations) except insofar as that conclusion may be affected by the failure of the education grants to be scholarships or fellowships subject to the provisions of section 117(a) and the reason for such failure. The grant program described above satisfies the conditions of sections 4.01 through 4.07 of Rev. Proc. 76–47, but does not meet the percentage test of section 4.08. As a substitute for the percentage test, all the relevant facts and circumstances must be considered to determine whether the primary purpose of the grant is to educate recipients in their individual capacities or to compensate employees.

In this instance, the relevant facts and circumstances indicate that the primary purpose of *X's* grant program is to educate recipients in their individual capacities rather than to compensate employees. As required by Rev. Proc. 76–47, the selection committee is independent of *X* and *M* and awards the grants using the objective criteria of academic performance and financial need. *X* has demonstrated that the company's employees and the plan have no unusual characteristics that would bear on the likelihood that a grant will be available to any specific subgroup of eligible applicants or that a significant number of children of persons who serve the company will be disqualified. The grant is a small fixed amount. It does not limit the grantee significantly in choosing a course of study or school. Only one grant per year will be awarded among the children of 3,000 employees. *X's* inability to show whether it will meet the ten percent test is reasonable, because the expense of determining whether the test is met is greatly out of proportion to the small grant program. These facts indicate that overall there is no significant degree of probability that a grant will be available to the child of any particular employee or to a child selected from any particular group of employees. (The fact that this situation involves only one grant per year among the children of employees does not preclude the possibility that if several grants were awarded, there still would be no significant degree of probability that a grant would be available to any particular employee's child.)

HOLDING

Under the facts set forth above, grants awarded under this program satisfy the requirements of Rev. Proc. 76–47 and constitute scholarships under section 117(a) of the Code. Therefore, grants awarded under the program will be described in section 4945(g)(1) and will not be taxable expenditures under section 4945(d)(3).

Section 7602.—Examinations of Books and Witnesses

26 CFR 301.7602–1: Examination of books and witnesses.
(Also Section 7609; 301.7609–1 through 301.7609–5.)

T.D. 8091

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER F; PART 301—PROCEDURE AND ADMINISTRATION

Administrative Summonses

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to administrative summonses. Changes to the applicable tax law were made by the Tax Equity and Fiscal Responsibility Act of 1982 [1982–2 C.B. 462]. The regulations provide the public with the guidance needed to comply with that Act and affect persons who receive summonses, third party recordkeepers who receive summonses, and persons with respect to whose tax liability a summons is issued.

DATES: The regulations pertaining to section 7602 of the Code are effective after September 3, 1982. The regulations pertaining to section 7609 of the Code apply to summonses served after December 31, 1982.

FOR FURTHER INFORMATION CONTACT: Bruce H. Jurist of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, (Attention: CC:LR:T) 202-566-3238, not a toll-free call.

SUPPLEMENTARY INFORMATION:

BACKGROUND

On June 12, 1985, the FEDERAL REGISTER published proposed amendments (50 FR 24655) to the Procedure and Administration Regulations (26 CFR Part 301) under sections 7602 and 7609 of the Internal Revenue Code of 1954 [LR–10–83, 1985–2, C.B. 797]. These amendments were proposed to conform the regulations to sections 331, 332, and 333 of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) (96 Stat. 620).

Two written comments responding to the notice of proposed rulemaking were received. No requests for a public hearing were received and accordingly none was held. After consideration of all written comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

PUBLIC COMMENTS

Under section 7602, no summons may be issued or enforced with respect to any person if a Justice Department referral is in effect with respect to that person. Section 301.7602–1(c)(2)(ii) of the proposed regulations provides that a referral is in effect with respect to any person when the Attorney General, the Deputy Attorney General, or an Assistant Attorney General under the authority of section 6103(h)(3)(B) requests that the Service disclose taxpayer information relating to the person. The request must state that the need for disclosure is for tax administration purposes. One commentator suggested that the rule be clarified so as to state that a referral is in effect only if the request for disclosure is made with respect to a criminal investigation or prosecution. This suggestion is adopted in the final regulations.

The proposed regulations contain a number of examples illustrating that for purposes of the rule prohibiting the issuance or enforcement of a summons if a Justice Department referral is in effect, each taxable period and taxes imposed by different chapters of the Code are treated seperately. One comment suggested the addition of an example dealing with tax shelter promoter penalties when a referral relating to income tax is in effect. Accordingly, the final regulations include an example clarifying that the Service may issue an administrative summons with respect to a person's liability under section 6700 (tax shelter promoter penalty) even though a referral is in effect for the taxable year with respect to that person's income tax liability.

One commentator suggested that the time period under section 7609 during which the Service is proscribed from issuing or enforcing summonses be changed from 20 days to 20 business days. In addition, the commentator suggested that the Secretary be required to issue the certificates described in section 7609(i)(2) rather than being allowed to issue such certificates as a matter of discretion. Because these comments are inconsistent with the language of section 7609, they are not adopted in the final regulations.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

Although a notice of proposed rulemaking soliciting public comments was issued, the Internal Revenue Service has concluded that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these regulations are not subject to the Regulatory

Flexibility Act (5 U.S.C. Chapter 6).

The Commissioner of Internal Revenue has determined that these final regulations are not major rules under Executive Order 12291 or the Treasury and OMB implementation of the order dated April 29, 1983. Accordingly, a Regulatory Impact Analysis is not required.

DRAFTING INFORMATION

The principal author of these proposed regulations is Bruce H. Jurist of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

Accordingly, 26 CFR Part 301 is amended as follows:

PROCEDURE AND ADMINSTRATION REGULATIONS

(26 CFR Part 301)

Paragraph 1. The authority for Part 301 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 2. Section 301.7602–1 is amended by revising paragraphs (a) and (b) and adding new paragraphs (c) and (d). The amended section reads as follows:

§301.7602–1 Examination of books and witnesses.

(a) *In general.* For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax (including any interest, additional amount, addition to the tax, or civil penalty) or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, collecting any such liability, or inquiring into any offense connected with the administration or enforcement of the internal revenue laws, any authorized officer or employee of the Internal Revenue Service may examine any books, papers, records or other data which may be relevant or material to such inquiry; and take such testimony of the person concerned, under oath, as may be relevant to such inquiry.

(b) *Summons.* For the purposes described in paragraph (a) of this section the Commissioner is authorized to summon the person liable for tax or required to perform the act, or any officer or employee of such person or any persons having possession, custody, or care of books of accounts containing entries relating to the business of the person liable for tax or required to perform the act, or any other person deemed proper, to appear before a designated officer or employee of the Internal Revenue Service at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under oath, as may be relevant or material to such inquiry; and take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry. This summons power may be used in an investigation of either civil or criminal tax-related liability. The Commissioner may designate any employee of the Internal Revenue Service as the individual before whom a person summoned pursuant to section 6420(e)(2), 6421(f)(2), 6424(d)(2), 6427(e)(2), or 7602 shall appear. Any such employee, when so designated in a summons, is authorized to take testimony under oath of the person summoned and to receive and examine books, papers, records, or other data produced in compliance with the summons.

(c) *Proscription on issuing of administrative summons when a Justice Department referral is in effect.*

(1) *In general.* The Commissioner may neither issue a summons under this title nor initiate a proceeding to enforce a previously issued summons by way of section 7604 with respect to any person whose tax liability is in issue, if a Justice Department referral is in effect with respect to that person for that liability.

(2) *Justice Department referral in effect.* A Justice Department referral is in effect with respect to any person when:

(i) The Secretary recommends, within the meaning of this paragraph, that the Attorney General either commence a grand jury investigation of or criminal prosecution of such person for any alleged offense connected with the administration or enforcement of the internal revenue laws, or

(ii) The Attorney General (or Deputy Attorney General or Assistant Attorney General) under section 6103(h)(3)(B) requests in writing that the Secretary disclose a return of, or return information relating to, such person. The request must set forth that the need for disclosure is for the purpose of a grand jury investigation of or potential or pending criminal prosecution of such person for any alleged offense connected with the administration or enforcement of the internal revenue laws.

The referral is effective at the time the document recommending criminal prosecution or grand jury investigation is signed by the Secretary or upon the Secretary's receipt of the section 6103(h)(3)(B) request.

(3) *Cessation of Justice Department referral.* A Justice Department referral ceases to be in effect with respect to a person:

(i) When the Secretary receives written notification from the Attorney General that the Justice Department:

(A) Will not prosecute that person for any offense connected with the administration or enforcement of the internal revenue laws that gave rise to the referral under paragraph (2)(i) of this section, or

(B) Will not authorize a grand jury investigation of that person with respect to such offense, or

(C) Will discontinue any grand jury investigation of that person with respect to such offense;

(ii) When a final disposition with respect to a criminal proceeding brought against that person has been made; or

(iii) When the Secretary receives written notification from the Attorney General, Deputy Attorney General, or an Assistant Attorney General, that the Justice Department will not prosecute such person for any offense connected with the administration or enforcement of the internal revenue laws, based upon a previous request for disclosure under section 6103(h)(3)(B).

(4) *Taxable years and taxes imposed by separate chapters of the Code treated separately*—(i) *In general.* For purposes of this section, each taxable period (or, if there is no taxable period, each taxable event) and each tax imposed by a separate chapter of the Code is treated separately.

(ii) *Examples.* The following examples illustrate the application of this paragraph (c)(4):

Example (1). A Justice Department referral is in effect for D's criminal evasion of income tax for the taxable year 1979. The Commissioner may issue a summons respecting D's 1980 criminal and/or civil tax liability. The Commissioner may not issue a summons respecting D's 1979 income tax liability.

Example (2). A referral has been made out to the Department of Justice for the criminal prosecution of F with regard to F's income tax liability for the taxable year 1978. The Commissioner may issue a summons respecting F's gift tax liability for the taxable year 1978.

Example (3). A referral has been made to the Department of Justice for a grand jury investigation respecting G's 1980 income tax liability. The Commissioner may issue a summons related to an investigation of G's liability for Federal Insurance Contribution Act (FICA) taxes for the taxable year 1980.

Example (4). A referral has been made to the Department of Justice respecting J's criminal evasion of windfall profit tax for all quarters of the calendar year 1982. The Commissioner may issue a summons respecting J's liability for highway motor vehicle use tax covering the same periods.

Example (5). A referral has been made to the Department of Justice for a grand jury investigation respecting L's 1983 income tax liability. The Commissioner may issue a summons related to the investigation of L's liability under sections 6700 (abusive tax shelter promoter penalty) and 7408 of the Code for his conduct during 1983.

(d) *Effective date*. This section is effective after September 3, 1982. For rules effective on or before September 3, 1982, see 26 CFR 301.7602–1 (revised as of April 1, 1984).

Par. 3. Section 301.7609–1 is amended by designating the original text as paragraph (a), revising redesignated paragraph (a), and adding a new paragraph (b). The amended section reads as follows:

§301.7609–1 Special procedures for third-party summonses.

(a) *In general*. Section 7609 requires the Internal Revenue Service to follow special procedures when summoning the records of persons defined by section 7609(a)(3) as "third-party recordkeepers." Under these special procedures, the person about whom information is being gathered must be notified in advance in many cases. If the person about whom information is being gather has been given notice, that person has the right to institute, until and including the 20tn day following the day such notice was served on or mailed to such notified person, a proceeding to quash the summons. During the time the validity of the summons is being litigated, the statutes of limitations are suspended under section 7609(e). Section 7609 does not restrict the authority under section 7602 (or under any other provision of law) to examine records and witnesses without serving a summons and without giving notice of an examination. Sections 301.7609–1 through 301.7609–5 relate to section 7609; §301.7609–2, discusses matters under sections 7609(a)(3) and 7609(i) relating to third-party recordkeepers; §301.7609–3 discusses matters under section 7609(b), relating to intervention rights; §301.7609–4 and the institution of a proceeding to quash; §301.7609–4 discusses matters under section 7609(c), relating to summonses excepted from the section 7609 procedures; and §301.7609–5 discusses matters under section 7609(e), relating to the suspension of the statute of limitations.

(b) *Effective dates*. This section applies to summonses served after December 31, 1982. For the rules applicable to summonses issued on or after March 1, 1977 and served before January 1, 1983, see 26 CFR 301.7609–1 (revised as of April 1, 1984).

Par. 4. Section 301.7609–2 is amended by adding new paragraphs (c) and (d). The amended section reads as follows:

§301.7609–2 Third-party recordkeepers.

* * * * *

(c) *Duty of third-party recordkeeper*—(1) *In general*. Upon receipt of a summons, the third-party recordkeeper ("recordkeeper") must begin to assemble the summoned records. The recordkeeper must be prepared to produce the summoned records on the date which the summons states the records are to be examined regardless of the institution or anticipated institution of a proceeding to quash or the recordkeeper's intervention (as allowed under section 7609(b)(2)(C)) into a proceeding to quash.

(2) *Disclosing recordkeepers not liable*—(i) *In general*. A recordkeeper, or an agent or employee thereof, who makes a disclosure of records as required by this section, in good faith reliance on the certificate of the Secretary (as defined in paragraph (c)(2)(ii) of this section) or an order of a court requiring production of records, will not be liable for such disclosure to any customer, or to any party with respect to whose tax liablility the summons was issued, or to any other person.

(ii) *Certificate of the Secretary*. The Secretary may issue to the recordkeeper a certificate stating both:

(A) That the 20-day period, within which a notified person may institute a proceeding to quash the summons, has expired; and

(B) That no proceeding has been properly instituted within that period. The Secretary may also issue a certificate to the recordkeeper if the taxpayer, with respect to whose tax liability the summons was issued, expressly consents to the examination of the records summoned.

(3) *Reimbursement of costs*. Recordkeepers may be entitled to reimbursement of their costs of assembling and preparing to produce summoned records, to the extent allowed by section 7610, even if the summons ultimately is not enforced.

(d) *Effective dates*. This section, with the exception of paragraph (c), applies generally to all summonses issued on or after March 1, 1977. Paragraph (c) applies only to summonses served after December 31, 1982.

Par. 5. Section 301.7609–3 is amended by revising paragraphs (a), (b), (c), and by adding new pararaph (d). The amended section reads as follows:

§301.7609–3 Right to intervene; right to institute a proceeding to quash.

(a) *Notified person*. Under section 7609(a), the Internal Revenue Service must give a notice of summons to any person, other than the person summoned, who is identified in the description of the books and records contained in the summons in order that such person may contest the right of the Service to examine the summoned records by instituting a proceeding to quash the summons. Thus, if the Service issues a summons to a bank requesting checking account records of more than one person all of whom are identified in the description of the records contained in the summons, then all such persons are notified persons entitled to notice under section 7609(a). Therefore, if the Service requests the records of a joint bank account of A and B both of whom are named in the summons, then both A and B are notified persons entitled to notice under section 7609(a).

(b) *Right to institute a proceeding to quash*—

(1) *In general*. Section 7609(b) grants a notified person the right to institute a proceeding to quash the summons in the United States district court for the district within which the person summoned resides or is found. Jurisdiction of the court is based on section 7609(h). The act of filing a petition in district court does not in and of itself institute a proceeding to quash under section 7609(b)(2). Rather, the filing of the petition must be coupled with notice as required by section 7609(b)(2)(B).

(2) *Elements of institution of a proceeding to quash*. In order to institute a proceeding to quash a summons the notified person (or the notified person's agent, nominee, or other person acting under the

direction or control of the notified person) must, not later than the 20th day following the day the notice of the summons was served on or mailed to such notified person:

(i) File a petition to quash in the name of the notified person in a district court having jurisdiction,

(ii) Notify the Service by sending a copy of that petition by registered or certified mail to the Service employee and office designated to receive the copy in the notice of summons that was given to the notified person, and

(iii) Notify the recordkeeper by sending to that recordkeeper by registered or certified mail a copy of the petition.

Failure to give timely notice to either the summoned party of the Service in the manner described in this paragraph means that the notified person has failed to institute a proceeding to quash and the district court has no jurisdiction to hear the proceeding. Thus, for example, if the notified person mails a copy of the petition to the summoned person but not to the designated Service employee and office, the notified person has failed to institute a proceeding to quash. Similarly, if the notified person mails a copy of such petition to the summoned person but, instead of sending a copy of the petition by registered or certified mail to the designated employee and office, the notified person gives the designated employee and office the petition by some other means, the notified person has failed to institute a proceeding to quash.

(3) *Failure to institute a proceeding to quash.* If the notified person fails to institute a proceeding to quash within 20 days following the day the notice of the summons was served on or mailed to such notified person, the Service may examine the summoned records following the 23rd day after notice of the summons was served on or mailed to the notified person (see section 7609(d)(1)).

(c) *Presumption no notice has been mailed.* Section 7609(b)(2)(B) permits a notified person to institute a proceeding to quash by filing a petition in district court and notifying both the Service and the summoned person. Unless the notified person has notified both the Service and the summoned person in the appropriate manner, the notified person has failed to institute a proceeding to quash. If the copy of the petition has not been delivered to the summoned person or the person and office designated to receive the notice on behalf of the Service within 3 days from the close of the 20-day period allowed to institute a proceeding to quash, it is presumed that the notification has not been timely mailed.

(d) *Effective date.* This section applies to summonses served after December 31, 1982. For the rules applicable to summonses issued on or after March 1, 1977 and served before January 1, 1983, see 26 CFR 301.7609-3 (revised as of April 1, 1984).

Par. 6. Section 301.7609-4 is amended by adding new paragraph (c). The amended section reads as follows:

§301.7609-4 Summons excepted from section 7609 procedures.

* * * * *

(c) *Effective date.* This section applies to all summonses issued after February 28, 1977.

Par. 7. Section 301.7609-5 is amended by revising paragraphs (b) and (c) and by adding new paragraph (d). The amended section reads as follows:

§301.7609-5 Suspension of statutes of limitation.

* * * * *

(b) *Period during which a proceeding, etc., is pending.* Under section 7609(e), the statute of limitations may be suspended for the period during which a proceeding, and appeals therein, with respect to the enforcement of such summons is pending. This period begins on the date the petition to quash the summons is filed in district court. The period continues until all appeals are disposed of, or until the expiration of the period in which an appeal may be taken or a request for a rehearing may be made. Full compliance, partial compliance, and noncompliance have no effect on the suspension provisions. Of course, if the notified person takes no action provided in subsection (b) of section 7609, no suspension of the statutes of limitations takes place. The periods of limitations which are suspended under section 7609(e) are those which apply to the taxable periods to which the summons relates.

(c) *Taking of action as provided in section 7609(b).* Section 7609(b) allows intervention by a notified person as a matter of right upon compliance with the Federal Rules of Civil Procedure. The phrase "takes any action as provided in subsection (b)", found in section 7609(e), includes any intervention, whether or not section 7609(b) is specifically mentioned in the order of the court allowing intervention. The phrase also includes the fulfilling of only part of the requirements of section 7609(b)(2), relating to the right of a person to institute a proceeding to quash. Thus, for instance, if a notified person notifies a person who has been summoned by sending a copy of the petition by registered or certified mail but does not mail a copy of that notice to the appropriate person and office under section 7609(b)(2)(B), the notified person has taken an action under section 7609(e).

(d) *Effective dates.* This section applies to summonses served after December 31, 1982. For the rules applicable to summonses issued on or after March 1, 1977, and before January 1, 1983, see 26 CFR 301.7609-5 (revised as of April 1, 1984).

James I. Owens,
Acting Commissioner of
Internal Revenue.

Approved May 28, 1986.

J. Roger Mentz,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on June 24, 1986, 8:45 a.m., and published in the issue of the Federal Register for June 25, 1986, 51 F.R. 23052)

Section 7609.—Special Procedures for Third-party Summonses

26 CFR 301.7609-1: Special procedures for third-party summonses.

Guidance for persons who receive summonses, third party recordkeepers who receive summonses, and persons with respect to whose tax liability a summons is issued. See T.D. 8091, page 14.

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26 CFR 301.7609-3; Right to intervene; right to institute a proceeding to quash.

Guidance for persons who receive summonses, third party recordkeepers who receive summonses, and persons with respect to whose tax liability a summons is issued. See T.D. 8091, page 14.

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26 CFR 301.7609-4: Summons excepted from section 7609 procedures.

Guidance for persons who receive summonses, third party recordkeepers who receive summonses, and persons with respect to whose tax liability a summons is issued. See T.D. 8091, page 14.

26 CFR 301.7609-5: *Suspension of statute of limitations.*

Guidance for persons who receive summonses, third party recordkeepers who receive summonses, and persons with respect to whose tax liability a summons is issued. See T.D. 8091, page 14.

26 CFR 301.7609-2: *Third-party recordkeepers.*

Guidance for persons who receive summonses, third party recordkeepers who receive summonses, and persons with respect to whose tax liability a summons is issued. See T.D. 8091, page 14.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Henry L. Creel	Cleveland, OH	Certified Public Accountant	Indefinite from May 15, 1986
J. Thomas Jones	Augusta, GA	Certified Public Accountant	Indefinite from June 1, 1986
Michael D. Sherman	Pound Ridge, NY	Enrolled Agent	Indefinite from May 27, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and address of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the Weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Earl M. Walker	Port Neches, TX	Certified Public Accountant	May 19, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 1.367(a)–1, removed; 1.367(a)–4T, redesignated as 1.367(a)–7T; 1.367(a)–1T through 1.367(a)–6T, 1.367(d)–1T, 1.6038B–1T, added; 7.367(b)–1, 7.367(b)–4, amended; published as temporary regulations in T.D. 8087, page 5, 1986–23 I.R.B.	Transfers of property by U.S. persons to foreign corporations	1986–23 I.R.B. 33	July 15, 1986
26 CFR 1.338–1T, 1.338–2T, 1.338–4T, 1.338–5T, 1.338(h)(10)–1T, amended; published as temporary regulations in T.D. 8088, page 4, 1986–24 I.R.B.	Section 338(g) statements of election	1986–24 I.R.B. 24	July 15, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor.
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federral Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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Bulletin No. 1986–29
July 21, 1986

Internal Revenue bulletin

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

ADMINISTRATIVE

Pub. L. 99–272, page 4.
Portions of the Consolidated Omnibus Budget Reconciliation Act of 1985 are reproduced.

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DEPOSITORY 376

Findings Lists begin on page 73.
Announcement of Disbarments and Suspensions begin on page 78.

Department of the Treasury
Internal Revenue Service

T22.23: 1984-29

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part II. Treaties and Tax Legislation

Subpart B.—Legislation and Related Committee Reports

Public Law 99–272 99th Congress, H.R. 3128[1] April 7, 1986:

An Act to provide for reconciliation pursuant to section 2 of the first concurrent resolution on the budget for fiscal year 1986 (S. Con. Res. 32, Ninety-ninth Congress).

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SHORT TITLE

Section 1.—This Act may be cited as the "Consolidated Omnibus Budget Reconciliation Act of 1985".

• • • • •

TITLE X—PRIVATE HEALTH INSURANCE COVERAGE

Section 10001.—Employers Required to Provide Certain Employees and Family Members with Continued Health Insurance Coverage at Group Rates (Internal Revenue Code Amendments)

(a) *Denial of Deduction for Employer Contribution to Plan.*—Subsection (i) of section 162 of the Internal Revenue Code of 1954 (relating to deduction for trade or business expenses with respect to group health plans) is amended by redesignating paragraph (2) as paragraph (3) and by inserting after paragraph (1) the following new paragraph:

"(2) *Plans must provide continuation coverage to certain individuals.*—

"(A) *In general.*—No deduction shall be allowed under this section for expenses paid or incurred by an employer for any group health plan maintained by such employer unless all such plans maintained by such employer meet the continuing coverage requirements of subsection (k).

"(B) *Exception for certain small employers, etc.*—Subparagraph (A) shall not apply to any plan described in section 106(b)(2).".

(b) *Denial of Exclusion for Highly Compensated Individuals.*—Section 106 of the Internal Revenue Code of 1954 (relating to contributions by employer to accident and health plans) is amended by inserting "(a) *In General.*—" before "Gross" and by inserting at the end thereof the following new subsection:

"(b) *Exception for Highly Compensated Individuals Where Plan Fails To Provide Certain Continuation Coverage.*—

"(1) *In general.*—Subsection (a) shall not apply to any amount contributed by an employer on behalf of a highly compensated individual (within the meaning of section 105(h)(5)) to a group health plan maintained by such employer unless all such plans maintained by such employer meet the continuing coverage requirements of section 162(k).

"(2) *Exception for certain plans.*—Paragraph (1) shall not apply to any—

"(A) group health plan for any calendar year if all employers maintaining such plan normally employed fewer than 20 employees on a typical business day during the preceding calendar year,

"(B) governmental plan (within the meaning of section 414(d)), or

"(C) church plan (within the meaning of section 414(e)). Under regulations, rules similar to the rules of subsections (a) and (b) of section 52 (relating to employers under common control) shall apply for purposes of subparagraph (A).

"(3) *Group health plan.*—For purposes of this subsection, the term 'group health plan' has the meaning given such term by section 162(i)(3).".

(c) *Continuation Coverage Requirements.*—Section 162 of the Internal Revenue Code of 1954 is amended by redesignating subsection (k) as subsection (l) and by inserting after subsection (j) the following new subsection:

"(k) *Continuation Coverage Requirements of Group Health Plans.*—

"(1) *In general.*—For purposes of subsection (i)(2) and section 106(b)(1), a group health plan meets the requirements of this subsection only if each qualified beneficiary who would lose coverage under the plan as a result of a qualifying event is entitled to elect, within the election period, continuation coverage under the plan.

"(2) *Continuation coverage.*—For purposes of paragraph (1), the term 'continuation coverage' means coverage under the plan which meets the following requirements:

"(A) *Type of benefit coverage.*—The coverage must consist of coverage which, as of the time the coverage is being provided, is identical to the coverage provided under the plan to similarly situated beneficiaries under the plan with respect to whom a qualifying event has not occurred.

"(B) *Period of coverage.*—The coverage must extend for at least the period beginning on the date of the qualifying event and ending not earlier than the earliest of the following.

"(i) *Maximum period.*—In the case of—

"(I) a qualifying event described in paragraph (3)(B) (relating to terminations and reduced hours), the date which is 18 months after the date of the qualifying event, and

"(II) any qualifying event not described in subclause (I), the date which is 36 months after the date of the qualifying event.

"(ii) *End of plan.*—The date on which the employer ceases to provide any group health plan to any employee.

"(iii) *Failure to pay premium.*—The date on which coverage ceases under the plan by reason of a failure to make timely payment of any premium required under the plan with respect to the qualified beneficiary.

"(iv) *Reemployment of medicare eligibility.*—The date on which the qualified beneficiary first becomes, after the date of the election—

"(I) a covered employee under any other group health plan, or

"(II) entitled to benefits under title XVIII of the Social Security Act.

"(v) *Remarriage of spouse.*—In the case of an individual who is a qualified beneficiary by reason of being the spouse of a covered employee, the date on which the beneficiary remarries and becomes covered under a group health plan.

"(C) *Premium requirements.*—The plan may require payment of a premium for any period of continuation coverage, except that such premium—

"(i) shall not exceed 102 percent of the applicable premium for such period, and

"(ii) may, at the election of the payor, be made in monthly installments.

If an election is made after the qualifying event, the plan shall permit payment for continuation coverage during the period preceding the election to be made within 45 days of the date of the election.

"(D) *No requirement or insurability.*—

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[1] This publication of the law, Senate Report No. 99–146, page 38, and Conference Report No. 99–453, page 53, is restricted to excerpts involving tax matters. House Report No. 99–241 is not published.

The coverage may not be conditioned upon, or discriminate on the basis of lack of, evidence of insurability.

"(E) *Conversion option.*—In the case of a qualified beneficiary whose period of continuation coverage expires under subparagraph (B)(i), the plan must, during the 180-day period ending on such expiration date, provide to the qualified beneficiary the option of enrollment under a conversion health plan otherwise generally available under the plan.

"(3) *Qualifying event.*—For purpose of this subsection, the term 'qualifying event' means, with respect to any covered employee, any of the following events which, but for the continuation coverage required under this subsection, would result in the loss of coverage of a qualified beneficiary:

"(A) The death of the covered employee.

"(B) The termination (other than by reason of such employee's gross misconduct), or reduction of hours, of the covered employee's employment.

"(C) The divorce or legal separation of the covered employee from the employee's spouse.

"(D) The covered employee becoming entitled to benefits under title XVIII of the Social Security Act.

"(E) A dependent child ceasing to be a dependent child under the generally applicable requirements of the plan.

"(4) *Applicable premium.*—For purposes of this subsection—

"(A) *In general.*—The term 'applicable premium' means, with respect to any period of continuation coverage of qualified beneficiaries, the cost to the plan for such period of the coverage for similarly situated beneficiaries with respect to whom a qualifying event has not occurred (without regard to whether such cost is paid by the employer or employee).

"(B) *Special rule for self-insured plans.*—To the extent that a plan is a self-insured plan—

"(i) *In general.*—Except as provided in clause (ii), the applicable premium for any period of continuation coverage of qualified beneficiaries shall be equal to a reasonable estimate of the cost of providing coverage for such period for similarly situated beneficiaries which—

"(I) is determined on an actuarial basis, and

"(II) takes into account such factors as the Secretary may prescribe in regulations.

"(ii) *Determination on basis of past cost.*—If a plan administrator elects to have this clause apply, the applicable premium for any period of continuation coverage of qualified beneficiaries shall be equal to—

"(I) the cost to the plan for similarly situated beneficiaries for the same period occurring during the preceding determination period under subparagraph (C), adjusted by

"(II) the percentage increase or decrease in the implicit price deflator of the gross national product (calculated by the Department of Commerce and published in the Survey of Current Business) for the 12-month period ending on the last day of the sixth month of such preceding determination period.

"(iii) *Clause (ii) not to apply where significant change.*—A plan administrator may not elect to have clause (ii) apply in any case in which there is any significant difference, between the determination period and the preceding determination period, in coverage under, or in employees covered by, the plan. The determination under the preceding sentence for any determination period shall be made at the same time as the determination under subparagraph (C).

"(C) *Determination period.*—The determination of any applicable premium shall be made for a period of 12 months and shall be made before the beginning of such period.

"(5) *Election.*—For purposes of this subsection—

"(A) *Election period.*—The term 'election period' means the period which—

"(i) begins not later than the date on which coverage terminates under the plan by reason of a qualifying event.

"(ii) is of at least 60 days' duration, and

"(iii) ends not earlier than 60 days after the later of—

"(I) the date described in clause (i), or

"(II) in the case of any qualified beneficiary who receives notice under paragraph (6)(D), the date of such notice.

"(B) *Effect of election on other beneficiaries.*—Except as otherwise specified in an election, any election by a qualified beneficiary described in clause (i)(I) or (ii) of paragraph (7)(B) shall be deemed to include an election of continuation coverage on behalf of any other qualified beneficiary who would lose coverage under the plan by reason of the qualifying event.

"(6) *Notice requirements.*—In accordance with regulations prescribed by the Secretary—

"(A) the group health plan shall provide, at the time of commencement of coverage under the plan, written notice to each covered employee and spouse of the employee (if any) of the rights provided under this subsection.

"(B) the employer of an employee under a plan must notify the plan administrator of a qualifying event described in subparagraph (A), (B), or (D) of paragraph (3) with respect to such employee within 30 days of the date of the qualifying event.

"(C) each covered employee or qualified beneficiary is responsible for notifying the plan administrator of the occurrence of any qualifying event described in subparagraph (C) or (E) of paragraph (3), and

"(D) the plan administrator shall notify—

"(i) in the case of a qualifying event described in subparagraph (A), (B) or (D) of paragraph (3), any qualified beneficiary with respect to such event, and

"(ii) in the case of a qualifying event described in subparagraph (C) or (E) of paragraph (3) where the covered employee notifies the plan administrator under subparagraph (c), any qualified beneficiary with respect to such event, of such beneficiary's rights under this subsection.

For purposes of subparagraph (D), any notification shall be made within 14 days of the date on which the plan administrator is notified under subparagraph (B) or (C), whichever is applicable, and any such notification to an individual who is a qualified beneficiary as the spouse of the covered employee shall be treated as notification to all other qualified beneficiaries residing with such spouse at the time such notification is made.

"(7) *Definitions.*—For purposes of this subsection—

"(A) *Covered employee.*—The term 'covered employee' means an individual who is (or was) provided coverage under a group health plan by virtue of the individual's employment or previous employment with an employer

"(B) *Qualified beneficiary.*—

"(i) *In general.*—The term 'qualified beneficiary' means, with respect to a covered employee under a group health plan, any other individual who, on the day before the qualifying event for that employee, is a beneficiary under the plan—

"(I) as the spouse of the covered employee, or

"(II) as the dependent child of the employee.

"(ii) *Special rule for terminations and reduced employment.*—In the case of the qualifying event described in paragraph (3)(B), the term 'qualified beneficiary' includes the covered employee.

"(C) *Plan administrator.*—The term 'plan administrator' has the meaning given the term 'administrator' by section 3(16)(A) of the Employee Retirement Income Security Act of 1974.".

(d) *Conforming amendment.*—Paragraph (1) of section 162(i) is amended by striking out "*General rule*" in the heading thereof and inserting in lieu thereof "*Coverage relating to end stage renal disease*".

(e) *Effective dates.*—

(1) *General rule.*—The amendments made by this section shall apply to plan years beginning on or after July 1, 1986.

(2) *Special rule for collective bargaining agreements.*—In the case of a group health plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified before the date of the enactment of this Act, the amendments made by this section shall not apply to plan years beginning before the later of—

(A) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension thereof agreed to after the date of the enactment of this Act), or

(B) January 1, 1987.

For purposes of subparagraph (A), any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added by this section shall not be treated as a termination of such collective bargaining agreement.

Section 10002.—Temporary Extension of Coverage at Group Rates for Certain Employees and Family Members (ERISA Amendments)

(a) *In general.*—Subtitle B of title I of the Employee Retirement Income Security Act of 1974 is amended by adding at the end thereof the following new part:

"Part 6—Continuation Coverage Under Group Health Plans

Section 601.—Plans Must Provide Continuation Coverage to Certain Individuals

"(a) *In General.*—The plan sponsor of each group health plan shall provide, in accordance with this part, that each qualified beneficiary who would lose coverage under the plan as a result of a qualifying event is entitled, under the plan, to elect, within the election period, continuation coverage under the plan.

"(b) *Exception for Certain Plans.*—Subsection (a) shall not apply to any group health plan for any calendar year if all employers maintaining such plan normally employed fewer than 20 employees on a typical business day during the preceding calendar year. Under regulations, rules similar to the rules of subsections (a) and (b) of section 52 of the Internal Revenue Code of 1954 (relating to employers under common control) shall apply for purposes of this subsection.

Section 602.—Continuation Coverage

"For purposes of section 601, the term 'continuation coverage' means coverage under the plan which meets the following requirements:

"(1) *Type of benefit coverage.*—The coverage must consist of coverage which, as of the time the coverage is being provided, is identical to the coverage provided under the plan to similarly situated beneficiaries under the plan with respect to whom a qualifying event has not occurred.

"(2) *Period of coverage.*—The coverage must extend for at least the period beginning on the date of the qualifying event and ending not earlier than the earliest of the following:

"(A) *Maximum period.*—In the case of—

"(i) a qualifying event described in section 603(2) (relating to terminations and reduced hours), the date which is 18 months after the date of the qualifying event, and

"(ii) any qualifying event not described in clause (i), the date which is 36 months after the date of the qualifying event.

"(B) *End of plan.*—The date on which the employer ceases to provide any group health plan to any employee.

"(C) *Failure to pay premium.*—The date on which coverage ceases under the plan by reason of a failure to make timely payment of any premium required under the plan with respect to the qualified beneficiary.

"(D) *Reemployment or medicare eligibility.*—The date on which the qualified beneficiary first becomes, after the date of the election—

"(i) a covered employee under any other group health plan, or

"(ii) entitled to benefits under title XVIII of the Social Security Act.

"(E) *Remarriage of spouse.*—In the case of an individual who is a qualified beneficiary by reason of being the spouse of a covered employee, the date on which the beneficiary remarries and becomes covered under a group health plan.

"(3) *Premium requirements.*—The plan may require payment of a premium for any period of continuation coverage, except that such premium—

"(A) shall not exceed 102 percent of the applicable premium for such period, and

"(B) may, at the election of the payor, be made in monthly installments.

If an election is made after the qualifying event, the plan shall permit payment for continuation coverage during the period preceding the election to be made within 45 days of the date of the election.

"(4) *No requirement of insurability.*—The coverage may not be conditioned, upon, or discriminate on the basis of lack of, evidence of insurability.

"(5) *Conversion option.*—In the case of a qualified beneficiary whose period of continuation coverage expires under paragraph (2)(A), the plan must, during the 180-day period ending on such expiration date, provide to the qualified beneficiary the option of enrollment under a conversion health plan otherwise generally available under the plan.

Section 603.—Qualifying Event

"For purposes of this part, the term 'qualifying event' means, with respect to any covered employee, any of the following events which, but for the continuation coverage required under this part, would result in the loss of coverage of a qualified beneficiary:

"(1) The death of the covered employee.

"(2) The termination (other than by reason of such employee's gross misconduct), or reduction of hours, of the covered employee's employment.

"(3) The divorce or legal separation of the covered employee from the employee's spouse.

"(4) The covered employee becoming entitled to benefits under title XVIII of the Social Security Act.

"(5) A dependent child ceasing to be a dependent child under the generally applicable requirements of the plan.

Section 604.—Applicable Premium

"For purposes of this part—

"(1) *In general.*—The term 'applicable premium' means, with respect to any period of continuation coverage of qualified beneficiaries, the cost to the plan for such period of the coverage for similarly situated beneficiaries with respect to whom a qualifying event has not occurred (without regard to whether such cost is paid by the employer or employee).

"(2) *Special rule for self-insured plans.*—To the extent that a plan is a self-insured plan—

"(A) *In general.*—Except as provided in subparagraph (B), the applicable premium for any period of continuation coverage of qualified beneficiaries shall be equal to a reasonable estimate of the cost of providing coverage for such period for similarly situated beneficiaries which—

"(i) is determined on an actuarial basis, and

"(ii) takes into account such factors as the Secretary may prescribe in regulations.

"(B) *Determination on basis of past cost.*—If an administrator elects to have this subparagraph apply, the applicable premium for any period of continuation coverage of qualified beneficiaries shall be equal to—

"(i) the cost to the plan for similarly situated beneficiaries for the same period occurring during the preceding determination period under paragraph (3), adjusted by

"(ii) the percentage increase or decrease in the implicit price deflator of the gross national product (calculated by the Department of Commerce and published in the Survey of Current Business) for the 12-month period ending on the last day of the sixth month of such preceding determination period.

"(C) *Subparagraph (B) not to apply where significant change.*—An administrator may not elect to have subparagraph (B) apply in any case in which there is any significant difference, between the determination period and the preceding determination period, in coverage under, or in employees covered by, the plan. The determination under the preceding sentence for any determination period shall be made at the same time as the determination under paragraph (3).

"(3) *Determination period.*—The determination of any applicable premium shall be made for a period of 12 months and shall be made before the beginning of such period.

Section 605.—Election

"For purposes of this part—

"(1) *Election period.*—The term 'election period' means the period which—

"(A) begins not later than the date on which coverage terminates under the plan by reason of a qualifying event,

"(B) is of at least 60 days' duration, and

"(C) ends not earlier than 60 days after the later of—

"(i) the date described in subparagraph (A), or

"(ii) in the case of any qualified beneficiary who receives notice under section 606(4), the date of such notice.

"(2) *Effect of election on other beneficiaries.*—Except as otherwise specified in an election, any election by a qualified beneficiary described in subparagraph (A)(i) or (B) of section 607(3) shall be deemed to include an election of continuation coverage on behalf of any other qualified beneficiary who would lose coverage under the plan by reason of the qualifying event.

Section 606.—Notice Requirements

"In accordance with regulations prescribed by the Secretary—

"(1) the group health plan shall provide, at the time of commencement of coverage under the plan, written notice to each covered employee and spouse of the employee (if any) of the rights provided under this subsection,

"(2) the employer of an employee under a plan must notify the administrator of a qualifying event described in paragraph (1), (2), or (4) of section 603 within 30 days of the date of the qualifying event,

"(3) each covered employee or qualified beneficiary is responsible for notifying the administrator of the occurrence of any qualifying event described in paragraph (3) or (5) of section 603, and

"(4) the administrator shall notify—

"(A) in the case of a qualifying event described in paragraph (1), (2), or (4) of section 603, any qualified beneficiary with respect to such event, and

"(B) in the case of a qualifying event described in paragraph (3) or (5) of section 603 where the covered employee notifies the administrator under paragraph (3), any qualified beneficiary with respect to such event, of such beneficiary's rights under this subsection.

For purposes of paragraph (4), any notification shall be made within 14 days of the date on which the administrator is notified under paragraph (2) or (3), whichever is applicable, and any such notification to an individual who is a qualified beneficiary as the spouse of the covered employee shall be treated as notification to all other qualified beneficiaries residing with such spouse at the time such notification is made.

Section 607.—Definitions

"For purposes of this part—

"(1) *Group health plan.*—The term 'group health plan' means an employee welfare benefit plan that is a group health plan (within the meaning of section 162(i)(3) of the Internal Revenue Code of 1954).

"(2) *Covered employee.*—The term 'covered employee' means an individual who is (or was) provided coverage under a group health plan by virtue of the individual's employment or previous employment with an employer.

"(3) *Qualified beneficiary.*—

"(A) *In general.*—The term 'qualified beneficiary' means, with respect to a covered employee under a group health plan, any other individual who, on the day before the qualifying event for that employee, is a beneficiary under the plan—

"(i) as the spouse of the covered employee, or

"(ii) as the dependent child of the employee.

"(B) *Special rule for terminations and reduced employment.*—In the case of a qualifying event described in section 603(2), the term "qualified beneficiary' includes the covered employee.

Section 608.—Regulations

"The Secretary may prescribe regulations to carry out the provisions of this part.".

(b) *Penalty for Failure to Provide Notice.*—Section 502(c) of such Act (29 U.S.C. 1132(c)) is amended by inserting after "Any administrator" the following: "(1) who fails to meet the requirements of paragraph (1) or (4) of section 606 with respect to a participant or beneficiary, or (2)".

(c) *Clerical amendments.*—The table of contents in section 1 of such Act is amended by inserting after the item relating to section 514 the following new items:

Part 6—Continuation Coverage Under Group Health Plans

"Sec. 601. Plans must provide continuation coverage to certain individuals.
"Sec. 602. Continuation coverage.
"Sec. 603. Qualifying event.
"Sec. 604. Applicable premium.
"Sec. 605. Election.
"Sec. 606. Notice requirements.
"Sec. 607. Definitions.
"Sec. 608. Regulations.".

(d) *Effective Dates.*—

(1) *General rule.*—The amendments made by this section shall apply to plan years beginning on or after July 1, 1986.

(2) *Special rule for collective bargaining agreements.*—In the case of a group health plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified before the date of the enactment of this Act, the amendments made by this section shall not apply to plan years beginning before the later of—

(A) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension thereof agreed to after the date of the enactment of this Act), or

(B) January 1, 1987.

For purposes of subparagraph (A), any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added by this section shall not be treated as a termination of such collective bargaining agreement.

(e) *Notification to Covered Employees.*—At the time that the amendments made by this section apply to a group health plan (within the meaning of section 607(1) of the Employee Retirement Income Security Act of 1974), the plan shall notify each covered employee, and spouse of the employee (if any), who is covered under the plan at that time of the continuation coverage required under part 6 of subtitle B of title I of such Act. The notice furnished under this subsection is in lieu of notice that may otherwise be required under section 606(1) of such Act with respect to such individuals.

Section 10003.—Continuation of Health Insurance for State and Local Employees who Lost Employment-Related Coverage (Public Health Service Act Amendments)

(a) *In General.*—The Public Health Service Act is amended by adding at the end the following new title:

TITLE XXII—REQUIREMENTS FOR CERTAIN GROUP HEALTH PLANS FOR CERTAIN STATE AND LOCAL EMPLOYEES

Section 2201.—State and Local Governmental Group Health Plans Must Provide Continuation Coverage to Certain Individuals

"(a) *In General.*—In accordance with regulations which the Secretary shall prescribe, each group health plan that is maintained by any State that receives funds under this Act, by any political subdivision of such a State, or by any agency or instrumentality of such a State or political subdivision, shall provide, in accordance with this title, that each qualified beneficiary who would lose coverage under the plan as a result of a qualifying event is entitled, under the plan, to elect, within the election period, continuation coverage under the plan.

"(b) *Exception for Certain Plans.*—Subsection (a) shall not apply to—

"(1) any group health plan for any calendar year if all employers maintaining such plan normally employed fewer than 20 employees on a typical business day during the preceding calendar year, or

"(2) any group health plan maintained for employees by the government of the District of Columbia or any territory or possession of the United States or any agency or instrumentality.

Under regulations, rules similar to the rules of subsections (a) and (b) of section 52 of the Internal Revenue Code of 1954 (relating to employers under common control) shall apply for purposes of paragraph (1).

Section 2202.—Continuation Coverage

"For purposes of section 2201, the term 'continuation coverage' means coverage under the plan which meets the following requirements:

"(1) *Type of benefit coverage.*—The coverage must consist of coverage which, as of the time the coverage is being provided, is identical to the coverage provided under the plan to similarly situated beneficiaries under the plan with respect to whom a qualifying event has not occurred.

"(2) *Period of coverage.*—The coverage must extend for at least the period beginning on the date of the qualifying event and ending not earlier than the earliest of the following:

"(A) *Maximum period.*—In the case of—

"(i) a qualifying event described in section 2203(2) (relating to terminations and reduced hours), the date which is 18 months after the date of the qualifying event, and

"(ii) any qualifying event not described in clause (i), the date which is 36 months after the date of the qualifying event.

"(B) *End of plan.*—The date on which the employer ceases to provide any group health plan to any employee.

"(C) *Failure to pay premium.*—The date on which coverage ceases under the plan by reason of a failure to make timely payment of any premium required under the plan with respect to the qualified beneficiary.

"(D) *Reemployment or medicare eligibility.*—The date on which the qualified beneficiary first becomes, after the date of the election—

"(i) a covered employee under any other group health plan, or

"(ii) entitled to benefits under title XVIII of the Social Security Act.

"(E) *Remarriage of spouse.* In the case of an individual who is a qualified beneficiary by reason of being the spouse of a covered employee, the date on which the beneficiary remarries and becomes covered under a group health plan.

"(3) *Premium requirements.*—The plan may require payment of a premium for any period of continuation coverage, except that such premium—

"(A) shall not exceed 102 percent of the applicable premium for such period, and

"(B) may, at the election of the payor, be made in monthly installments.

If an election is made after the qualifying event, the plan shall permit payment for continuation coverage during the period preceding the election to be made within 45 days of the date of the election.

"(4) *No requirement of insurability.*—The coverage may not be conditioned upon, or discriminate on the basis of lack of, evidence of insurability.

"(5) *Conversion option.*—In the case of a qualified beneficiary whose period of continuation coverage expires under paragraph (2)(A), the plan must, during the 180-day period ending on such expiration date, provide to the qualified beneficiary the option of enrollment under a conversion health plan otherwise generally available under the plan.

Section 2203.—Qualifying Event

"For purposes of this title; the term 'qualifying event' means, with respect to any covered employee, any of the following events which, but for the continuation coverage required under this title, would result in the loss of coverage of a qualified beneficiary:

"(1) The death of the covered employee.

"(2) The termination (other than by reason of such employee's gross misconduct), or reduction of hours, of the covered employee's employment.

"(3) The divorce or legal separation of the covered employee from the employee's spouse.

"(4) The covered employee becoming entitled to benefits under title XVIII of the Social Security Act.

"(5) A dependent child ceasing to be a dependent child under the generally applicable requirements of the plan.

Section 2204.—Applicable Premium

"For purposes of this title—

"(1) *In general.*—The term 'applicable premium' means, with respect to any period of continuation coverage of qualified beneficiaries, the cost to the plan for such period of the coverage for similarly situated beneficiaries with respect to whom a qualifying event has not occurred (without regard to whether such cost is paid by the employer or employee).

"(2) *Special rule for self-insured plans.*—To the extent that a plan is a self-insured plan—

"(A) *In general.*—Except as provided in subparagraph (B), the applicable premium for any period of continuation coverage of qualified beneficiaries shall be equal to a reasonable estimate of the cost of providing coverage for such period for similarly situated beneficiaries which—

"(i) is determined on an actuarial basis, and

"(ii) takes into account such factors as the Secretary may prescribe in regulations.

"(B) *Determination on basis of past cost.*—If a plan administrator elects to have this subparagraph apply, the applicable premium for any period of continuation coverage of qualified beneficiaries shall be equal to—

"(i) the cost to the plan for similarly situated beneficiaries for the same period occurring during the preceding determination period under paragraph (3), adjusted by

"(ii) the percentage increase or decrease in the implicit price deflator of the gross national product (calculated by the Department of Commerce and published in the Survey of Current Business) for the 12-month period ending on the last day of the sixth month of such preceding determination period.

"(C) *Subparagraph (B) not to apply where significant change.*—A plan administrator may not elect to have subparagraph (B) apply in any case in which there is any significant difference, between the determination period and the preceding determination period, in coverage under, or in employees covered by, the plan. The determination under the preceding sentence for any determination period shall be made at the same time as the determination under paragraph (3).

"(3) *Determination period.*—The determination of any applicable premium shall be made for a period of 12 months and shall be made before the beginning of such period.

Section 2205.—Election

"For purposes of this title—

"(1) *Election period.*—The term 'election period' means the period which—

"(A) begins not later than the date on which coverage terminates under the plan by reason of a qualifying event,

"(B) is of at least 60 days' duration, and

"(C) ends not earlier than 60 days after the later of—

"(i) the date described in subparagraph (A), or

"(ii) in the case of any qualified beneficiary, who receives notice under section 2206(4), the date of such notice.

"(2) *Effect of election on other beneficiaries.*—Except as otherwise specified in an election, any election by a qualified beneficiary described in subparagraph (A)(i) or (B) of section 2208(3) shall be deemed to include an election of continuation coverage on behalf of any other qualified beneficiary, who would lose coverage under the plan by reason of the qualifying event.

Section 2206.—Notice Requirements

"In accordance with regulations prescribed by the Secretary—

"(1) the group health plan shall provide, at the time of commencement of coverage under the plan, written notice to each covered employee and spouse of the employee (if any) of the rights provided under this subsection.

"(2) the employer of an employee under a plan must notify the plan administrator of a qualifying event described in paragraph (1), (2), or (4) of section 2203 within 30 days of the date of the qualifying event,

"(3) each covered employee or qualified beneficiary is responsible for notifying the plan administrator of the occurrence of any qualifying event described in paragraph (3) or (5) of section 2203, and

"(4) the plan administrator shall notify—

"(A) in the case of a qualifying event described in paragraph (1), (2), or (4) of section 2203, any qualified beneficiary with respect to such event, and

"(B) in the case of a qualifying event described in paragraph (3) or (5) of section 2203 where the covered employee notifies the plan administrator under paragraph (3), any qualified beneficiary with respect to such event,

of such beneficiary's rights under this subsection.

For purposes of paragraph (4), any notification shall be made within 14 days of the date on which the plan administrator is notified under paragraph (2) or (3), whichever is applicable, and any such notification to an individual who is a qualified beneficiary as the spouse of the covered employee shall be treated as notification to all other qualified beneficiaries residing with such spouse at the time such notification is made.

Section 2207.—Enforcement

"Any individual who is aggrieved by the failure of a State, political subdivision, or agency or instrumentality thereof, to comply with the requirements of this title may bring an action for appropriate equitable relief.

Section 2208.—Definitions

"For purposes of this title—

"(1) *Group health plan.*—The term 'group health plan' has the meaning given such term in section 162(i)(3) of the Internal Revenue Code of 1954.

"(2) *Covered employee.*—The term 'covered employee' means an individual who is (or was) provided coverage under a group health plan by virtue of the individual's employment or previous employment with an employer.

"(3) *Qualified beneficiary.*—

"(A) *In general.*—The term 'qualified

beneficiary' means, with respect to a covered employee under a group health plan, any other individual who, on the day before the qualifying event for that employee, is a beneficiary under the plan—

"(i) as the spouse of the covered employee, or

"(ii) as the dependent child of the employee.

"(B) *Special rule for terminations and reduced employment.*—In the case of a qualifying event described in section 2203(2), the term 'qualified beneficiary' includes the covered employee.

"(4) *Plan administrator.*—The term 'plan administrator' has the meaning given the term 'administrator' by section 3(16)(A) of the Employee Retirement Income Security Act of 1974."

(b) *Effective Dates.*—

(1) *General rule.*—The amendments made by this section shall apply to plan years beginning on or after July 1, 1986.

(2) *Special rule for collective bargaining agreements.*—In the case of a group health plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers ratified before the date of the enactment of this Act, the amendments made by this section shall not apply to plan years beginning before the later of—

(A) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension thereof agreed to after the date of the enactment of this Act), or

(B) January 1, 1987.

For purposes of subparagraph (A), any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added by this section shall not be treated as a termination of such collective bargaining agreement.

(c) *Notification to Covered Employees.*—At the time that the amendments made by this section apply to a group health plan (covered under section 2201 of the Public Health Service Act), the plan shall notify each covered employee, and spouse of the employee (if any), who is covered under the plan at that time of the continuation coverage required under title XXII of such Act. The notice furnished under this subsection is in lieu of notice that may otherwise be required under section 2206(1) of such Act with respect to such individuals.

Title XI—Single-Employer Plan Termination Insurance System Amendments

Section 11001.—Short Title and Table of Contents

This title may be cited as "Single-Employer Pension Plan Amendments Acts of 1986".

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Section 11002.—Findings and Declaration of Policy

(a) *Findings.*—The Congress finds that—

(1) single-employer defined benefit pension plans have a substantial impact on interstate commerce and are affected with a national interest;

(2) the continued well-being and retirement income security of millions of workers, retirees, and their dependents are directly affected by such plans;

(3) the existence of a sound termination insurance system is fundamental to the retirement income security of participants and beneficiaries of such plans; and

(4) the current termination insurance system in some instances encourages employers to terminate pension plans, evade their obligations to pay benefits, and shift unfunded pension liabilities onto the termination insurance system and the other premium-payers.

(b) *Additional Findings.*—The Congress further finds that modification of the current termination insurance system and an increase in the insurance premium for single-employer defined benefit pension plans—

(1) is desirable to increase the likelihood that full benefits will be paid to participants and beneficiaries of such plans;

(2) is desirable to provide for the transfer of liabilities to the termination insurance system only in cases of severe hardship;

(3) is necessary to maintain the premium costs of such system at a reasonable level; and

(4) is necessary to finance properly current funding definciencies and future obligations of the single-employer pension plan termination insurance system.

(c) *Declaration of Policy.*—It is hereby declared to be the policy of this title—

(1) to foster and facilitate interstate commerce;

(2) to encourage the maintenance and growth of single-employer defined benefit pension plans;

(3) to increase the likelihood that participants and beneficiaries under single-employer defined benefit pension plans will receive their full benefits;

(4) to provide for the transfer of unfunded pension liabilities onto the single-employer pension plan termination insurance system only in cases of severe hardship;

(5) to maintain the premium costs of such system at a reasonable level; and

(6) to assure the prudent financing of current funding deficiencies and future obligations of the single-employer pension plan termination insurance system by increasing termination insurance premiums.

Section 11003.—Amendment of the Employee Retirement Income Security Act of 1974

Whenever in this title an amendment or repeal is expressed in terms of an amendment to or repeal of a section or other provision, the reference is to a section of other provision of the Employee Retirement Income Security Act of 1974, unless otherwise specified.

Section 11004.—Definitions

(a) *In General.*—Section 4001(a) (29 U.S.C. 1301(a)) is amended—

(1) by striking out paragraph (2) and inserting in lieu thereof the following new paragraph:

"(2) 'substantial employer', for any plan year of a single-employer plan, means one or more persons—

"(A) who are contributing sponsors of the plan in such plan year,

"(B) who, at any time during such plan year, are members of the same controlled group, and

"(C) whose required contributions to the plan for each plan year constituting one of—

"(i) the two immediately preceding plan years, or

"(ii) the first two of the three immediately preceding plan years, total an amount greater than or equal to 10 percent of all contributions required to be paid to or under the plan for such plan year;";

(2) in paragraph (11), by striking out "and";

(3) in paragraph (12), by striking out "corporation." and inserting in lieu thereof "corporation;"; and

(4) by adding after paragraph (12) the following new paragraphs:

"(13) 'contributing sponsor', of a single-employer plan, means a person—

"(A) who is responsible, in connection with such plan, for meeting the funding requirements under section 302 of this Act or section 412 of the Internal Revenue Code of 1954, or

"(B) who is a member of the controlled group of a person described in subparagraph (A), has been responsible for meeting such funding requirements, and has employed a significant number (as may be defined in regulations of the corporation) of participants under such plan while such person was so responsible;

"(14) in the case of a single-employer plan—

"(A) 'controlled group' means, in connection with any person, a group consisting of such peson and all other persons under common control with such person; and

"(B) the determination of whether two or more persons are under 'common control' shall be made under regulations of the corporation which are consistent and coextensive with regulations prescribed for similar purposes by the Secretary of the Treasury under subsections (b) and (c) of section 414 of the Internal Revenue Code of 1954;

"(15) 'single-employer plan' means any defined benefit plan (as defined in section 3(35)) which is not a multiemployer plan;

"(16) 'benefit commitments', to a participant or beneficiary as of any date under a single-employer plan, means all benefits provided by the plan with respect to the participant or beneficiary which—

"(A) are guaranteed under section 4022,

"(B) would be guaranteed under section 4022, but for the operation of subsection 4022(b), or

"(C) constitute—

"(i) early retirement supplements or subsidies, or

"(ii) plant closing benefits,

irrespective of whether any such supplements, subsidies, or benefits are benefits guaranteed under section 4022, if the participant or beneficiary has satisfied, as of such date, all of the conditions required of him or her under the provisions of the plan to establish entitlement to the benefits, except for the submission of a formal application, retirement, completion of a required waiting period subsequent to application for benefits, or designation of a beneficiary;

"(17) 'amount of unfunded guaranteed benefits', of a participant or beneficiary as of any date under a single-employer plan, means an amount equal to the excess of—

"(A) the actuarial present value (determined as of such date on the basis of assumptions prescribed by the corporation for purposes of section 4044) of the benefits of the participant or beneficiary under the plan which are guaranteed under section 4022, over

"(B) the current value (as of such date) of the assets of the plan which are required to be allocated to those benefits under section 4044;

"(18) 'amount of unfunded benefit commitments', of a participant or beneficiary as of any date under a single-employer plan, means an amount equal to the excess of—

"(A) the actuarial present value (determined as of such date on the basis of assumptions prescribed by the corporation for purposes of section 4044) of the benefit commitments to the participant or beneficiary under the plan, over

"(B) the current value (as of such date) of the assets of the plan which are required to be allocated to those benefit commitments under section 4044;

"(19) 'outstanding amount of benefit commitments', of a participant or beneficiary under a terminated single-employer plan, means the excess of—

"(A) the actuarial present value (determined as of the termination date on the basis of assumptions prescribed by the corporation for purposes of section 4044) of the benefit commitments to such participant or beneficiary under the plan, over

"(B) the actuarial present value (determined as of such date on the basis of assumptions prescribed by the corporation for purposes of section 4044) of the benefits of such participant or beneficiary which are guaranteed under section 4022 or to which assets of the plan are required to be allocated under section 4044;

"(20) 'person' has the meaning set forth in section 3(9);

"(21) 'affected party' means, with respect to a plan—

"(A) each participant in the plan,

"(B) each beneficiary under the plan who is a beneficiary of a deceased participant or who is an alternate payee (within the meaning of section 206(d)(3)(K)) under an applicable qualified domestic relations order (within the meaning of section 206(d)(3)(B)(i)),

"(C) each employee organization representing participants in the plan, and

"(D) the corporation,

except that, in connection with any notice required to be provided to the affected party, if an affected party has designated, in writing, a person to receive such notice on behalf of the affected party, any reference to the affected party shall be construed to refer to such person.".

(b) *Technical Correction of Error in Multiemployer Pension Plan Amendments Act of 1980.*—Section 4001 is further amended by striking out the amendments made by section 402(a)(1)(F) of the Multiemployer Pension Plan Amendments Act of 1980 (94 Stat. 1297) (adding new paragraphs after a subsection (c)(1)), and, in lieu thereof, in subsection (b), by inserting "(1)" after "(b)" and by adding at the end of such subsection the following new paragraph:

"(2) For purposes of subtitle E—

"(A) except as otherwise provided in subtitle E, contributions or other payments shall be considered made under a plan for a plan year if they are made within the period prescribed under section 412(c)(10) of the Internal Revenue Code of 1954 (determined, in the case of a terminated plan, as if the plan had continued beyond the termination date), and

"(B) the term 'Secretary of the Treasury' means the Secretary of the Treasury or such Secretary's delegate.".

Section 11005.—Single-Employer Plan Termination Insurance Premiums.

(a) *Premium Increase*—

(1) *General rule.*—Section 4006 (a)(3)(A)(i) (29 U.S.C. 1306(a)(3)(A)(i)) is amended by striking out "for plan years beginning after December 31, 1977, an amount equal to $2.60" and inserting in lieu thereof "for plan years beginning after December 31, 1985, an amount equal to $8.50".

(2) *Conforming amendment with respect to plan years after 1977.*—Section 4006(c)(1) (29 U.S.C. 1306(c)(1)) is amended by striking out subparagraph (A) and inserting in lieu thereof the following new subparagraph:

"(A) in the case of each plan which was not a multiemployer plan in a plan year—

"(i) with respect to each plan year beginning before January 1, 1978, an amount equal to $1 for each individual who was a participant in such plan during the plan year, and

"(ii) with respect to each plan year beginning after December 31, 1977, an amount equal to $2.60 for each individual who was a participant in such plan during the plan year, and".

(b) *Incorporation of Certain Former Provisions in Lieu of Cross Reference Thereto.*—Section 4006(a) (29 U.S.C. 1306(a)) is amended—

(1) in paragraph (1), by striking out the last sentence; and

(2) by adding at the end thereof the following new paragraph:

"(6)(A) In carrying out its authority under paragraph (1) to establish premium rates and bases for basic benefits guaranteed under section 4022 with respect to single-employer plans, the corporation shall establish such rates and bases in coverage schedules in accordance with the provisions of this paragraph.

"(B) The corporation may establish annual premiums for single-employer plans composed of the sum of—

"(i) a charge based on a rate applicable to the excess, if any, of the present value of the basic benefits of the plan which are guaranteed over the value of the assets of the plan, not in excess of 0.1 percent, and

"(ii) an additional charge based on a rate applicable to the present value of the basic benefits of the plan which are guaranteed.

The rate for the additional charge referred to in clause (ii) shall be set by the corporation for every year at a level which the corporation estimates will yield total revenue approximately equal to the total revenue to be derived by the corporation from the charges referred to in clause (i) of this subparagraph.

"(C) The corporation may establish annual premiums for single-employer plans based on—

"(i) the number of participants in a plan, but such premium rates shall not exceed the rates described in paragraph (3),

"(ii) unfunded basic benefits guaranteed under this title, but such premium rates shall not exceed the limitations applicable to charges referred to in subparagraph(B)(i), or

"(iii) total guaranteed basic benefits, but such premium rates shall not exceed the rates for additional charges referred to in subparagraph (B)(ii).

If the corporation uses two or more of the rate bases described in this subparagraph, the premium rates shall be designed to produce approximately equal amounts of aggregate premium revenue from each of the rate bases used.

"(D) For purposes of this paragraph, the corporation shall by regulation define the terms 'value of assets' and 'present value of the benefits of the plan which are guaranteed' in a manner consistent with the purposes of this title and the provisions of this section.".

(c) *Approval by Joint Resolution of Recommendations of the Pension Benefit Guaranty Corporation.*—Title IV is amended as follows:

(1) The last sentence of subsection (a)(2) of section 4006 (29 U.S.C. 1306(a)(2)) is amended by striking out "the Congress approves such revised schedule by a concurrent resolution" and inserting in lieu thereof "a joint resolution approving such revised schedule is enacted".

(2) Subsection (a)(4) of section 4006 (29 U.S.C. 1306(a)(4)) is amended by striking out "approval by the Congress" and inserting in lieu thereof "the enactment of a joint resolution".

(3) Subsection (b)(3) of section 4006 (29 U.S.C. 1306(b)(3)) is amended by striking out "concurrent" and inserting in lieu thereof "joint", by striking out "That the Congress favors the" and inserting in lieu thereof "The", and by inserting "is hereby approved" before the period preceding the quotation marks.

(4) Subsection (f)(2)(B) of section 4022A (29 U.S.C. 1322(a)(f)(2)(B)) is amended by striking out "Congress by concurrent resolution" and inserting in lieu thereof "the enactment of a joint resolution".

(5) Subsection (f)(2)(C) of section 4022A (29 U.S.C. 1322a(f)(2)(C)) is amended by striking out "approved" and inserting in lieu thereof "so enacted".

(6) Subsection (f)(3)(B) of section 4022A (29 U.S.C. 1322a(f)(3)(A)) is amended by striking out "Congress by a concurrent resolution" and inserting in lieu thereof "enactment of a joint resolution".

(7) Subsection (f)(4)(A) of section 4022A (29 U.S.C. 1322a(f)(4)(A)) is amended by striking out "concurrent" and inserting in lieu thereof "joint".

(8) Subsection (f)(4)(B) of section 4022A (29 U.S.C. 1322a(f)(4)(B)) is amended by striking out "concurrent" each place it appears and inserting in lieu thereof "joint", by striking out "That the Congress favors the" and inserting in lieu thereof "The", and by inserting "is hereby approved" immediately before the period preceding the quotation marks.

(9) Subsection (f)(4)(C) of section 4022A (29 U.S.C. 1322a(f)(4)(C)) is amended by striking out "concurrent" and inserting in lieu thereof "joint".

(10) Subsection (g)(4)(A)(ii) of section 4022A (29 U.S.C. 1322a(g)(4)(A)(ii)) is amended by striking out "concurrent" and inserting in lieu thereof "joint", and by striking out "adopted" and inserting in lieu thereof "enacted".

(11) Subsection (g)(4)(B) of section 4022A (29 U.S.C. 1322a(g)(4)(B)) is amended by striking out "concurrent" each place it appears and inserting in lieu thereof "joint", by striking out "That the Congress disapproves the" and inserting in lieu thereof "The", and by inserting "is hereby disapproved" immediately before the period preceding the quotation marks.

(12) Subsection (g)(4)(D) of section 4022A (29 U.S.C. 1322a(g)(4)(D)) is amended by striking out "concurrent" and inserting in lieu thereof "joint".

(d) *Effective Dates.*—

(1) *General rule.*—Except as provided in paragraph (2), the amendments made by this section shall be effective for plan years commencing after December 31, 1985.

(2) *Special rule.*—The amendments made by subsection (b) shall be effective as of the date of the enactment of the

Multi-employer Pension Plan Amendments Act of 1980.

(c) *Transitional rule.*—

(1) *Notice of premium increase.*—Not later than 30 days after the date of the enactment of this Act, the Pension Benefit Guaranty Corporation shall send a notice to the plan administrator of each single-employer plan affected by the premium increase established by the amendment made by subsection (a)(1). Such notice shall describe such increase and the requirements of this subsection.

(2) *Due date for unpaid Premiums.*—With respect to any plan year beginning during the period beginning on January 1, 1986, and ending 30 days after the date of the enactment of this Act, any unpaid amount of such premium increase shall be due and payable no later than the earlier of 60 days after the date of the enactment of this Act or 30 days after the date on which the notice required by paragraph (1) is sent, except that in no event shall the amount of the premium increase established under the amendment made by subsection (a)(1) be due and payable for a plan year earlier than the date on which premiums for the plan would have been due for such plan year had this Act not been enacted.

(3) *Enforcement.*—For purposes of enforcement, the requirements of paragraphs (1) and (2) shall be considered to be requirements of sections 4006 and 4007 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1306 and 1307).

Section 11006.—Notice of Significant Reduction in Benefit Accruals

(a) *In General.*—Section 204 (29 U.S.C. 1054) is amended—

(1) by redesignating subsection (h) as subsection (i); and

(2) by inserting after subsection (g) the following new subsection:

"(h) A single-employer plan may not be amended so as to provide for a significant reduction in the rate of future benefit accrual, unless, after adoption of the plan amendment and not less than 15 days before the effective date of the plan amendment, the plan administrator provides a written notice, setting forth the plan amendment and its effective date, to—

"(1) each participant in the plan,

"(2) each beneficiary who is an alternate payee (within the meaning of section 206(d)(3)(K)) under an applicable qualified domestic relations order (within the meaning of section 206(d)(3)(B(i)), and

"(3) each employee organization representing participants in the plan,

except that such notice shall instead be provided to a person designated, in writing, to receive such notice on behalf of any person referred to in paragraph (1), (2), or (3).".

(b) *Effective Date.*—The amendments made by subsection (a) shall apply with respect to plan amendments adopted on or after January 1, 1986, except that, in the case of plan amendments adopted on or after January 1, 1986, and on or before the date of the enactment of this Act, the requirements of section 204(h) of the Employee Retirement Income Security Act of 1974 (as added by this section) shall be treated as met if the written notice required under such section 204(h) is provided before 60 days after the date of the enactment of this Act.

Section 11007.—General Requirements Relating to Termination of Single-Employer Plans by Plan Administrators

(a) *In General.*—Section 4041 (29 U.S.C. 1341) is amended by striking out subsections (a) through (c) and inserting in lieu thereof the following:

"Sec. 4041. (a) General Rules Governing Single-Employer Plan Terminations.—

"(1) *Exclusive means of plan termination.*—Except in the case of a termination for which proceedings are otherwise instituted by the corporation as provided in section 4042, a single-employer plan may be terminated only in a standard termination under subsection (b) or a distress termination under subsection (c).

"(2) *60-day notice of intent to terminate.*—Not less than 60 days before the proposed termination date of a standard termination under subsection (b) or a distress termination under subsection (c), the plan administrator shall provide to each affected party (other than the corporation in the case of a standard termination) a written notice of intent to terminate stating that such termination is intended and the proposed termination date. The written notice shall include any related additional information required in regulations of the corporation.

"(3) *Adherence to collective bargaining agreements.*—The corporation shall not proceed with a termination of a plan under this section if the termination would violate the terms and conditions of an existing collective bargaining agreement. Nothing in the preceding sentence shall be construed as limiting the authority of the corporation to institute proceedings to involuntarily terminate a plan under section 4042.".

(b) *Definitions Relating to Sufficiency.*—Section 4041(d) (29 U.S.C. 1341(d)) is amended to read as follows:

"(d) *Sufficiency.*—For purposes of this section—

"(1) *Sufficiency for benefit commitments.*—A single-employer plan is sufficient for benefit commitments if there is no amount of unfunded benefit commitments under the plan.

"(2) *Sufficiency for Guaranteed Benefits.*—A single-employer plan is sufficient for guaranteed benefits if there is no amount of unfunded guaranteed benefits under the plan.".

Section 11008.—Standard Termination of Single-Employer Plans

(a) *In General.*—Section 4041 (as amended by section 11007 of this Act) is further amended by inserting after subsection (a) the following new subsection:

"(b) *Standard Termination of Single-Employer Plans.*—

"(1) *General requirements.*—A single-employer plan may terminate under a standard termination only if—

"(A) the plan administrator provides the 60-day advance notice of intent to terminate to affected parties required under subsection (a)(2),

"(B) the requirements of subparagraphs (A) and (B) of paragraph (2) are met,

"(C) the corporation does not issue a notice of noncompliance under subparagraph (C) of paragraph (2), and

"(D) when the final distribution of assets occurs, the plan is sufficient for benefit commitments (determined as of the termination date).

"(2) *Termination procedure.*—

"(A) *Notice to the Corporation.*—As soon as practicable after the date on which the notice of intent to terminate is provided pursuant to subsection (a)(2), the plan administrator shall send a notice to the enrolled actuary—

"(i) certification by an enrolled actuary—

"(I) of the projected amount of the assets of the plan (as of a proposed date of final distribution of assets),

"(II) of the actuarial present value (as of such date) of the benefit commitments (detemined as of the proposed termination date) under the plan, and

"(III) that the plan is projected to be sufficient (as of such proposed date of final distribution) for such benefit commitments,

"(ii) such information as the corporation may prescribe in regulations as necessary to enable the corporation to make determination under subparagraph (C), and

"(iii) certification by the plan administrator that the information on which the enrolled actuary based the certification under clause (i) and the information provided to the corporation under clause (ii) are accurate and complete.

"(B) *Notice to Participants and Beneficiaries of Benefit Commitments.*—No later than the date on which a notice is sent by the plan administrator under subparagraph (A), the plan administrator shall send a notice to each person who is a participant or beneficiary under the plan—

"(i) specifying the amount of such person's benefit commitments (if any) as of the proposed termination date and the benefit form on the basis of which such amount is determined, and

"(ii) including the following information used in determining such benefit commitments:

"(I) the length of service,

"(II) the age of the participant or beneficiary,

"(III) wages,

"(IV) the assumptions, including the interest rate, and

"(V) such other information as the corporation may require.

Such notice shall be written in such manner as is likely to be understood by the participant or beneficiary and as may be prescribed in regulations of the corporation.

"(C) *Notice from the corporation of noncompliance.*—

"(i) *In general.*—Within 60 days after receipt of the notice under subparagraph (A), the corporation shall issue a notice of noncompliance to the plan administrator if—

"(I) it has reason to believe that any requirement of subsection (a)(2) or subparagraph (A) or (B) has not been met, or

"(II) it otherwise determines, on the basis of information provided by affected parties or otherwise obtained by the corporation, that there is reason to believe that the plan is not sufficient for benefit commitments.

"(ii) *Extension.*—The corporation and the plan administrator may agree to extend the 60-day period referred to in clause (i) by a written agreement signed by the corporation and the plan administrator before the expiration of the 60-day period. The 60-day period shall be extended as provided in the agreement and may be further extended by subsequent written agreements signed by the corporation and the plan administrator made before the expiration of a previously agreed upon extension of the 60-day period. Any extension may be made upon such terms and conditions (including the payment of benefits) as are agreed upon by the corporation and the plan administrator.

"(D) *Final distribution of assets in absence of notice of noncompliance.*—The plan administrator shall commence the final distribution of assets pursuant to the standard termination of the plan as soon as practicable after the expiration of the 60-day (or extended) period referred to in subparagraph (C), but such final distribution may occur only if—

"(i) the plan administrator has not received during such period a notice of noncompliance from the corporation under subparagraph (C), and

"(ii) when such final distribution occurs, the plan is sufficient for benefit commitments (determined as of the termination date).

"(3) *Methods of final distribution of assets.*—

"(A) *In general.*—In connection with any final distribution of assets pursuant to the standard termination of the plan under this subsection, the plan administrator shall distribute the assets in accordance with section 4044. In distributing such assets, the plan administrator shall—

"(i) purchase irrevocable commitments from an insurer to provide the benefit commitments under the plan and all other benefits (if any) under the plan to which assets are required to be allocated under section 4044, or

"(ii) in accordance with the provisions of the plan and any applicable regulations of the corporation, otherwise fully provide the benefit commitments under the plan and all other benefits (if any) under the plan to which assets are required to be allocated under section 4044.

"(B) *Certification to the corporation of final distribution of assets.*—Within 30 days after the final distribution of assets is completed pursuant to the standard termination of the plan under this subsection, the plan administrator shall send a notice to the corporation certifying that the assets of the plan have been distributed in accordance with the provisions of subparagraph (A) so as to pay the benefit commitments under the plan and all other benefits under the plan to which assets are required to be allocated under section 4044.

"(4) *Continuing authority.*—Nothing in this section shall be construed to preclude the continued exercise by the corporation, after the termination date of a plan terminated in a standard termination under this subsection, of its authority under section 4003 with respect to matters relating to the termination. A certification under paragraph (3)(B) shall not affect the corporation's obligations under section 4022.".

(b) *Conforming Amendment.*—Section 4041(f) (29 U.S.C. 1341(f)) is amended to read as follows:

"(f) *Limitation on the Conversion of a Defined Benefit Plan to a Defined Contribution Plan.*—The adoption of an amendment to a plan which causes the plan to become a plan described in section 4021(b)(1) constitutes a termination of the plan. Such an amendment may take effect only after the plan satisfies the requirements for standard termination under subsection (b) or distress termination under subsection (c).".

(c) *Authority for 60-day Extension.*—In the case of a standard termination of a plan under section 4041(b) of the Employee Retirement Income Security Act of 1974 (as amended by this section) with respect to which a notice of intent to terminate is filed before 120 days after the date of the enactment of this Act, the Pension Benefit Guaranty Corporation may, without the consent of the plan administrator, extend the 60-day period under section 4041(b)(2)(C)(i) of such Act (as so amended) for a period not to exceed 60 days.

(d) *Special Temporary Rule.*—

(1) *Requirements to be met before final distribution of assets.*—In the case of the termination of a single-employer plan described in paragraph (2) with respect to which the amount payable to the employer pursuant to section 4044(d) exceeds $1,000,000 (determined as of the proposed date of final distribution of assets), the final distribution of assets pursuant to such termination may not occur unless the Pension Benefit Guaranty Corporation—

(A) determines that the assets of the plan are sufficient for benefit commitments (within the meaning of section 4041(d)(1) of the Employee Retirement Income Security Act of 1974 (as amended by section 11007) under the plan, and

(B) issues to the plan administrator a written notice setting forth the determination described in subparagraph (A).

(2) *Plans to which subsection applies.*—A single-employer plan is described in this paragraph if—

(A) the plan administrator has filed a notice of intent to terminate with the Pension Benefit Guaranty Corporation, and—

(i) the filing was made before January 1, 1986, and the Corporation has not issued a notice of sufficiency for such plan before the date of the enactment of this Act, or

(ii) the filing is made on or after January 1, 1986, and before 60 days after the date of the enactment of this Act and the Corporation has not issued a notice of sufficiency for such plan before the date of the enactment of this Act, and

(B) of the persons who are (as of the termination date) participants in the plan, the lesser of 10 percent or 200 have filed complaints with the Corporation regarding such termination—

(i) in the case of plans described in subparagraph (A)(i), before 15 days after the date of the enactment of this Act, or

(ii) in any other case, before the later of 15 days after the date of the enactment of this Act or 45 days after the date of the filing of such notice.

(3) *Consideration of complaints.*—The Corporation shall consider and respond to such complaints not later than 90 days after the date on which the Corporation makes the determination described in paragraph (1)(A). The Corporation may hold informal hearings to expedite consideration of such complaints. Any such hearing shall be exempt from the requirements of chapter 5 of title 5, United States Code.

(4) *Delay on issuance of notice.*—

(A) *General rule.*—Except as provided in subparagraph (B), the Corporation shall not issue any notice described in paragraph (1)(B) until 90 days after the date on which the Corporation makes the determination described in paragraph (1)(A).

(B) *Exception in cases of substantial business hardship.*—Except in the case of an acquisition, takeover, or leveraged buyout, the preceding provisions of this subsection shall not apply if the contributing sponsor demonstrates to the satisfaction of the Corporation that the contributing sponsor is experiencing substantial business hardship. For purposes of this subparagraph, a contributing sponsor shall be considered as experiencing substantial business hardship if the contributing sponsor has been operating, and can demonstrate that the contributing sponsor will continue to operate, at an economic loss.

Section 11009.—Distress Termination of Single-Employer Plans

(a) *In General.*—Section 4041 (as amended by sections 11007 and 11008 of this Act) is further amended by inserting after subsection (b) the following new subsection:

"(c) *Distress Termination of Single-Employer Plans.*—

"(1) *In general.*—A single-employer plan may terminate under a distress termination only if—

"(A) the plan administrator provides the 60-day advance notice of intent to terminate to affected parties required under subsection (a)(2),

"(B) the requirements of subparagraph (A) of paragraph (2) are met, and

"(C) the corporation determines that the requirements of subparagraph (B) of paragraph (2) are met.

"(2) *Termination requirements.*—

"(A) *Information submitted to the corporation.*—As soon as practicable after the date on which the notice of intent to terminate is provided pursuant to subsection (a)(2), the plan administrator shall provide the corporation, in such form as may be prescribed by the corporation in regulations, the following information:

"(i) such information as the corporation may prescribe by regulation as necessary to make determinations under subparagraph (B) and paragraph (3);

"(ii) certification by an enrolled actuary of—

"(I) the amount (as of the proposed termination date) of the current value of the assets of the plan,

"(II) the actuarial present value (as of such date) of the benefit commitments under the plan,

"(III) whether the plan is sufficient for benefit commitments as of such date,

"(IV) the actuarial present value (as of such date) of benefits under the plan guaranteed under section 4022, and

"(V) whether the plan is sufficient for guaranteed benefits as of such date;

"(iii) in any case in which the plan is not sufficient for benefit commitments as of such date—

"(I) the name and address of each participant and beneficiary under the plan as of such date, and

"(II) such other information as shall be prescribed by the corporation by regulation as necessary to enable the corporation (or its designee under section 4049(b)) to be able to make payments to participants and beneficiaries as required under section 4049; and

"(iv) certification by the plan administrator that the information on which the enrolled actuary based the certifications under clause (ii) and the information provided to the corporation under clauses (i) and (iii) are accurate and complete.

"(B) *Determination by the corporation of necessary distress criteria.*—Upon receipt of the notice of intent to terminate required under subsection (a)(2) and the information required under subparagraph (A), the corporation shall determine whether the requirements of this subparagraph are met as provided in clause (i), (ii), or (iii). The requirements of this subparagraph are met if each person who is (as of the termination date) a contributing sponsor of such plan or a substantial member of such sponsor's controlled group meets the requirements of any of the following clauses:

"(i) *Liquidiation in bankruptcy or insolvency proceedings.*—The requirements of this clause are met by a person if—

"(I) such person has filed or has had filed against such person, as of the termination date, a petition seeking liquidation in a case under title 11, United States Code, or under any similar law of a State or political subdivision of a State, and

"(II) such case has not, as of the termination date, been dismissed.

"(ii) *Reorganization in bankruptcy or insolvency proceedings.*—The requirements of this clause are met by a person if—

"(I) such person has filed, or has had filed against such person, as of the termination date, a petition seeking reorganization in a case under title 11, United States Code, or under any similar law of a State or political subdivision of a State (or a case described in clause (i) filed by or against such person has been converted, as of such date, to such a case in which reorganization is sought),

"(II) such case has not, as of the termination date, been dismissed, and

"(III) the bankruptcy court (or other appropriate court in a case under such similar law of a State or political subdivision) approves the termination.

"(iii) *Termination required to enable payment of debts while staying in business or to avoid unreasonably burdensome pension costs caused by declining workforce.*—The requirements of this clause are met by a person if such person demonstrates to the satisfaction of the corporation that—

"(I) unless a distress termination occurs, such person will be unable to pay such person's debts when due and will be unable to continue in business, or

"(II) the costs of providing pension coverage have become unreasonably burdensome to such person, solely as a result of a decline of such person's workforce covered as participants under all single-employer plans of which such person is a contributing sponsor.

"(C) *Substantial member.*—For purposes of subparagraph (B), the term 'substantial member' of a controlled group means a person whose assets comprise 5 percent or more of the total assets of the controlled group as a whole.

"(D) *Notification of determinations by the corporation.*—The corporation shall notify the plan administrator as soon as practicable of its determinations made pursuant to subparagraph (B).

"(3) *Termination procedure.*—

"(A) *Determinations by the corporation relating to plan sufficiency for guaranteed benefits and for benefit commitments.*—If the corporation determines that the requirements for a distress termination set forth in paragraphs (1) and (2) are met, the corporation shall—

"(i) determine that the plan is sufficient for guaranteed benefits (as of the termination date) or that the corporation is unable to make such determination on the basis of information made available to the corporation,

"(ii) determine that the plan is sufficient for benefit commitments (as of the termination date) or that the corporation is unable to make such determination on the basis of information made available to the corporation, and

"(iii) notify the plan administrator of the determinations made pursuant to this subparagraph as soon as practicable.

"(B) *Implementation of termination.*—After the corporation notifies the plan administrator of its determinations under subparagraph (A), the termination of the plan shall be carried out as soon as practicable, as provided in clause (i), (ii), or (iii).

"(i) *Cases of sufficiency for benefit commitments.*—In any case in which the corporation determines that the plan is sufficient for benefit commitments, the plan administrator shall proceed to distribute the plan's assets, and make certification to the corporation with respect to such distribution, in the manner described in subsection (b)(3), and shall take such other actions as may be appropriate to carry out the termination of the plan.

"(ii) *Cases of sufficiency for guaranteed benefits without a finding of sufficiency for benefit commitments.*—In any case in which the corporation determines that the plan is sufficient for guaranteed benefits, but further determines that it is unable to determine that the plan is sufficient for benefit commitments on the basis of the information made available to it—

"(I) the plan administrator shall proceed to distribute the plan's assets in the manner described in subsection (b)(3), make certification to the corporation that the distribution has occurred, and take such actions as may be appropriate to carry out the termination of the plan, and

"(II) the corporation shall establish a separate trust in connection with the plan for purposes of section 4049.

"(iii) *Cases without any finding of sufficiency.*—In any case in which the corporation determines that it is unable to determine that the plan is sufficient for guaranteed benefits on the basis of the information made available to it—

"(I) the corporation shall commence proceedings in accordance with section 4042, and

"(II) the corporation shall establish a separate trust in connection with the plan for purposes of section 4049 unless the corporation determines that all benefit commitments under the plan are benefits guaranteed by the corporation under section 4022.

"(C) *Finding after authorized commencement of termination that plan is unable to pay benefits.*—

"(i) *Finding with respect to benefit commitments which are not guaranteed benefits.*—If, after the plan administrator has begun to terminate the plan as authorized under subparagraph (B)(i), the plan administrator finds that the plan is unable, or will be unable, to pay benefit commitments which are not benefits guaranteed by the corporation under section 4022, the plan administrator shall notify the corporation of such finding as soon as practicable thereafter. If the corporation concurs in the finding of the plan administrator (or the corporation itself makes such a finding) the corporation shall take the actions set forth in subparagraph (B)(ii)(II) relating to the trust established for purposes of section 4049.

"(ii) *Finding with respect to guaranteed benefits.*—If, after the plan administrator has begun to terminate the plan as authorized by subparagraph (B)(i) or (ii), the plan administrator finds that the plan is unable, or will be unable, to pay all benefits under the plan which are guaranteed by the corporation under section 4022, the plan administrator shall notify the corporation of such finding as soon as practicable thereafter. If the corporation concurs in the finding of the plan administrator (or the corporation itself makes such a finding), the corporation shall institute appropriate proceedings under section 4042.

"(D) *Administration of the plan during interim period.*—

"(i) *In general.*—The plan administrator shall—

"(I) meet the requirements of clause (ii) for the period commencing on the date on which the plan administrator provides a notice of distress termination to the corporation under subsection (a)(2) and ending on the date on which the plan administrator receives notification from the corporation of its determinations under subparagraph (A), and

"(II) meet the requirements of clause (ii) commencing on the date on which the plan administrator or the corporation makes a finding under subparagraph (C)(ii).

"(ii) *Requirements.*—The requirements of this clause are met by the plan administrator if the plan administrator—

"(I) refrains from distributing assets or taking any other actions to carry out the proposed termination of this subsection,

"(II) pays benefits attributable to employer contributions, other than death benefits, only in the form of an annuity,

"(III) does not use plan assets to purchase irrevocable commitments to provide benefits from an insurer, and

"(IV) continues to pay all benefit commitments under the plan, but, commencing on the proposed termination date, limits the payment of benefits under the plan to those benefits which are guaranteed by the corporation under section 4022 or to which assets are required to be allocated under section 4044.

In the event the plan administrator is later determined not to have met the requirements for distress termination, any benefits which are not paid solely by reason of compliance with subclause (IV) shall be due and payable immediately (together with interest, at a reasonable rate, in accordance with regulations of the corporation).".

(b) *Conforming Amendments.*—Section 4041 (as amended by the preceding provisions of this title) is further amended—

(1) by striking out subsection (e); and

(2) by redesignating subsection (f) as subsection (e).

Section 11010.—Termination Proceedings; Duties of the Corporation

(a) *Mandatory Commencement of Proceedings Upon Inability of Single-Employer Plan To Pay Benefits That Are Currently Due.*—

(1) *In general.*—Section 4042(a) (29 U.S.C. 1342(a)) is amended—

(A) in paragraph (2), by striking out "is" and inserting in lieu thereof "will be"; and

(B) by inserting at the beginning of the matter following paragraph (4) the following new sentence: "The corporation shall as soon as practicable institute proceedings under this section to terminate a single-employer plan whenever the corporation determines that the plan does not have assets available to pay benefits which are currently due under the terms of the plan".

(2) *Conforming amendments.*—

(A) Section 4042(b)(1) (29 U.S.C. 1342(b)(1)) is amended, in the first sentence, by inserting "or is required under subsection (a) to institute proceedings under this section," after "to a plan".

(B) Section 4042(c) (29 U.S.C. 1342(c)) is amended in the first sentence by striking out "If the corporation" and all that follows down through "has determined" and inserting in lieu thereof the following: "If the corporation is required under subsection (a) of this section to commence proceedings under this section with respect to a plan or, after issuing a notice under this section to a plan administrator, has determined".

(b) *Establishment of Section 4049 Trust.*—Section 4042 is further amended by adding at the end thereof the following new subsection:

"(i) In any case in which a plan is terminated under this section in a termination proceeding initiated by the corporation pursuant to subsection (a), the corporation shall establish a separate trust in connection with the plan for purposes of section 4049, unless the corporation determines that all benefit commitments under the plan are benefits guaranteed by the corporation under section 4022 or that there is no amount of unfunded benefit commitments under the plan.".

(c) *Conforming Amendment.*—The heading for section 4042 is amended to read as follows:

"Institution of Termination Proceedings by the Corporation".

Section 11011.—Amendments to liability provisions; liabilities relating to benefit commitments in excess of benefits guaranteed by the corporation

(a) *Liability for Distress Terminations and Terminations by the Corporation.*—Section 4062 (29 U.S.C. 1362) is amended—

(1) by redesignating subsection (e) as subsection (f); and

(2) by striking out so much as precedes subsection (f) (as redesignated) and inserting in lieu thereof the following:

"Liability for Termination of Single-Employer Plans Under A Distress Termination or a Termination by the Corporation

"Sec. 4062. (a) *In General.*—In any case in which a single-employer plan is terminated in a distress termination under section 4041(c) or a termination otherwise instituted by the corporation under section 4042, any person who is, on the termination date, a contributing sponsor of the plan or a member of such a contributing sponsor's controlled group shall incur liability under this section. The liability under this section of all such persons shall be joint and several. The liability under this section consists of—

"(1) liability to the corporation, to the extent provided in subsection (b),

"(2) liability to the trust established pursuant to section 4041(c)(3)(B) (ii) or (iii) or section 4042(i), to the extent provided in subsection (c), and

"(3) liability to the trustee appointed under subsection (b) or (c) of section 4042, to the extent provided in subsection (d).

"(b) *Liability to the Corporation.*—

"(1) *Amount of liability.*—

"(A) *In general.*—Except as provided in subparagraph (B), the liability to the corporation of a person described in subsection (a) shall consist of the sum of—

"(i) the lesser of—

"(I) the total amount of unfunded guaranteed benefits (as of the termination date) of all participants and beneficiaries under the plan, or

"(II) 30 percent of the collective net worth of all persons described in subsection (a),

and

"(ii) the excess (if any) of—

"(I) 75 percent of the amount described in clause (i)(I), over

"(II) the amount described in clause (i)(II),

together with interest (at a reasonable rate) calculated from the termination date in accordance with regulations prescribed by the corporation.

"(B) *Special rule in case of subsequent insufficiency.*—For purposes of subparagraph (A), in any case described in section 4041(c)(3)(C)(ii), actuarial present values shall be determined as of the date of the notice to the corporation (or the finding by the corporation) described in such section.

"(2) *Payment of liability.*—

"(A) *In general.*—Except as provided in subparagraph (B), the liability to the corporation under this subsection shall be due and payable to the corporation as of the termination date, in cash or securities acceptable to the corporation.

"(B) *Special rule.*—Payment of the liability under paragraph (1)(A)(ii) shall be made under commercially reasonable terms prescribed by the corporation. The parties involved shall make a reasonable effort to reach agreement on such commercially reasonable terms. Any such terms prescribed by the corporation shall provide for deferral of 50 percent of any amount of liability otherwise payable for any year under this subparagraph if a person subject to such liability demonstrates to the satisfaction of the corporation that no person subject to such liability has any individual pre-tax profits for such person's fiscal year ending during such year.

"(3) *Alternative arrangements.*—The corporation and any person liable under this section may agree to alternative arrangements for the satisfaction of liability to the corporation under this subsection.

"(c) *Liability to Section 4049 Trust.*—

"(1) *Amount of liability.*—

"(A) *In general.*—In any case in which

there is an outstanding amount of benefit commitments under a plan terminated under section 4041(c) or 4042, a person described in subsection (a) shall be subject to liability under this subsection to the trust established under section 4041(c)(3)(B) (ii) or (iii) or section 4042(i) in connection with the terminated plan. Except as provided in subparagraph (B), the liability of such person under this subsection shall consist of the lesser of—

"(i) 75 percent of the total outstanding amount of benefit commitments under the plan, or

"(ii) 15 percent of the actuarial present value (determined as of the termination date on the basis of assumptions prescribed by the corporation for purposes of section 4044) of all benefit commitments under the plan.

"(B) *Special rule in case of subsequent insufficiency.*—For purposes of subparagraph (A)—

"(i) *Plans insufficient for guaranteed benefits.*—In any case described in section 4041(c)(3)(C)(ii), actuarial present values shall be determined as of the date of the notice to the corporation (or the finding by the corporation) described in such section.

"(ii) *Plans sufficient for guaranteed benefits but insufficient for benefit entitlements.*—In any case described in section 4041(c)(3)(C)(i) but not described in section 4041(c)(3)(C)(ii), actuarial present values shall be determined as of the date on which the final distribution of assets is completed.

"(2) *Payment of Liability.*—

"(A) *General rule.*—Except as otherwise provided in this paragraph, payment of a person's liability under this subsection shall be made for liability payment years under commercially reasonable terms prescribed by the fiduciary designated by the corporation pursuant to section 4049(b)(1)(A). Such fiduciary and the liable persons assessed liability under this subsection shall make a reasonable effort to reach agreement on such commercially reasonable terms.

"(B) *Special rule for plans with low amounts of liability.*—In any case in which the amount described in paragraph (1)(A) is less than $100,000, the requirements of subparagraph (A) may be satisfied by payment of such liability over 10 liability payment years in equal annual installments (with interest at the rate determined under section 6621(b) of the Internal Revenue Code of 1954). The corporation may, by regulation, increase the dollar amount referred to in this subparagraph as it determines appropriate, taking into account reasonable administrative costs of trusts established under section 4041(c)(3)(B) (ii) or (iii) or section 4042(i).

"(C) *Deferral of payments.*—The terms for payment provided for under subparagraph (A) or (B) shall also provide for deferral of 75 percent of any amount of liability otherwise payable for any liability payment year if a person subject to such liability demonstrates to the satisfaction of the corporation that no person subject to such liability has any individual pre-tax profits for such person's fiscal year ending during such year. The amount of liability so deferred is payable only after payment in full of any amount of liability under subsection (b) in connection with the termination of the same plan which has been deferred pursuant to terms provided for under subsection (b)(2)(B).

"(d) *Liability to Section 4042 Trustee.*—A person described in subsection (a) shall be subject to liability under this subsection to the trustee appointed under subsection (b) or (c) of section 4042. The liability of such person under the subsection shall consist of—

"(1) the outstanding balance of the accumulated funding deficiencies (within the meaning of section 302(a)(2) of this Act and section 412(a) of the Internal Revenue Code of 1954) of the plan (if any) (which, for purposes of this subparagraph, shall include the amount of any increase in such accumulated funding deficiencies of the plan which would result if all pending applications for waivers of the minimum funding standard under section 303 of this Act or section 412(d) of such Code and for extensions of the amortization period under section 304 of this Act or section 412(e) of such Code with respect to such plan were denied and if no additional contributions (other than those already made by the termination date) were made for the plan year in which the termination date occurs or for any previous plan year),

"(2) the outstanding balance of the amount of waived funding deficiencies of the plan waived before such date under section 303 of this Act or section 412(d) of such Code (if any), and

"(3) the outstanding balance of the amount of decreases in the minimum funding standard allowed before such date under section 304 of this Act or section 412(e) of such Code (if any), together with interest (at a reasonable rate) calculated from the termination date in accordance with regulations prescribed by the corporation. The liability under this subsection shall be due and payable to such trustee as of the termination date, in cash or securities acceptable to such trustee.

"(e) *Definitions.*—

"(1) *Collective net worth of persons subject to liability.*—

"(A) *In general.*—The collective net worth of persons subject to liability in connection with a plan termination consists of the sum of the individual net worths of all persons who—

"(i) have individual net worths which are greater than zero, and

"(ii) are (as of the termination date) contributing sponsors of the terminated plan or members of their controlled groups.

"(B) *Determination of net worth.*—For purposes of this paragraph, the net worth of a person is—

"(i) determined on whatever basis best reflects, in the determination of the corporation, the current status of the person's operations and prospects at the time chosen for determining the net worth of the person, and

"(ii) increased by the amount of any transfers of assets made by the person which are determined by the corporation to be improper under the circumstances, including any such transfers which would be inappropriate under title 11, United States Code, if the person were a debtor in a case under chapter 7 of such title.

"(C) *Timing of determination.*—For purposes of this paragraph, determinations of net worth shall be made as of a day chosen by the corporation (during the 120-day period ending with the termination date) and shall be computed without regard to any liability under this section.

"(2) *Pre-tax profits.*—The term 'pre-tax profits' means—"(A) except as provided in subparagraph (B), for any fiscal year of any person, such person's consolidated net income (excluding any extraordinary charges to income and including any extraordinary credits to income) for such fiscal year, as shown on audited financial statements prepared in accordance with generally accepted accounting principles, or

"(B) for any fiscal year of an organization described in section 501(c) of the Internal Revenue Code of 1954, the excess of income over expenses (as such terms are defined for such organizations under

generally accepted accounting principles),
before provision for or deduction of Federal or other income tax, any contribution to any single-employer plan of which such person is a contributing sponsor at any time during the period beginning on the termination date and ending with the end of such fiscal year, and any amounts required to be paid for such fiscal year under this section. The corporation may be regulation require such information to be filed on such forms as may be necessary to determine the existence and amount of such pre-tax profits.

"(3) *Liability payment years.*—The liability payment years in connection with a terminated plan consist of the consecutive one-year periods following the last plan year preceding the termination date, excluding the first such year in any case in which the first such year ends less than 180 days after the termination date.".

(b) *Clerical Amendment.*—Subsection (f) of section 4062 (as redesignated by subsection (a)(1)) is amended by inserting "*Treatment of Substantial Cessation of Operations.*—" after "(f)".

(c) *Amendments to the Internal Revenue Code of 1954.*—

(1) *Time for deduction of certain employer liability payments.*—Paragraph (3) of section 404(g) of the Internal Revenue Code of 1954 (relating to certain employer liability payments considered as contributions) is amended to read as follows:

"(3) *Timing of deduction of contributions.*—

"(A) *In general.*—Except as otherwise provided in this paragraph, any payment described in paragraph (1) shall (subject to the last sentence of subsection (a)(1)(A)) be deductible under this section when paid.

"(B) *Contributions under standard terminations.*—Subparagraph (A) shall not apply (and subsection (a)(1)(A) shall apply) to any payments described in paragraph (1) which are paid to terminate a plan under section 4041(b) of the Employee Retirement Income Security Act of 1974 to the extent such payments result in the assets of the plan being in excess of the total amount of benefits under such plan which are guaranteed by the Pension Benefit Guaranty Corporation under section 4022 of such Act.

"(C) *Contributions to certain trusts.*—Subparagraph (A) shall not apply to any payment described in paragraph (1) which is made under section 4062(c) of such Act and such payment shall be deductible at such time as may be prescribed in regulations which are based on principles similar to the principles of subsection (a)(1)(A).".

(2) *References to ERISA.*—Subsection (g) of section 404 of the Internal Revenue Code of 1954 is amended by adding at the end thereof the following new paragraph:

"(4) *References to employee retirement income security act of 1974.*—For purposes of this subsection, any reference to a section of the Employee Retirement Income Security Act of 1974 shall be treated as a reference to such section as in effect on the date of the enactment of the Single-Employer Pension Plan Amendments Act of 1986.".

(3) *Effective date.*—The amendments made by this subsection shall apply to payments made after January 1, 1986, in taxable years ending after such date.

Section 11012.—Distribution to Participants and Beneficiaries of Liability Payments to Section 4049 Trust

(a) *In General.*—Subtitle C of title IV is amended by adding at the end thereof the following new section:

"Distribution to Participants and Beneficiaries of Liability Payments to Section 4049 Trust

"Section 4049. (a) Trust Requirements.—The requirements of this section apply to a trust established by the corporation in connection with a terminated plan pursuant to section 4041(c)(3)(B) (ii) or (iii). The trust shall be used exclusively for—

"(1) receiving liability payments under section 4062(c) from the persons who were (as of the termination date) contributing sponsors of the terminated plan and members of their controlled groups,

"(2) making distributions as provided in this section to the persons who were (as of the termination date) participants and beneficiaries under the terminated plan, and

"(3) defraying the reasonable administrative expenses incurred in carrying out responsibilities under this section.

The trust shall be maintained for such period of time as is necessary to receive all liability payments required to be made to the trust under section 4062(c) with respect to the terminated plan and to make all distributions required to be made to participants and beneficiaries under this section with respect to the terminated plan.

"(b) *Designation of Fiduciary by the Corporation.*—

"(1) *Purposes for Designation of Fiduciary.*—

"(A) *Collection of Liability.*—The corporation shall designate a fiduciary (within the meaning of section 3(21)) to serve as trustee of the trust for purposes of conducting negotiations and assessing and collecting liability pursuant to section 4062(c).

"(B) *Administration of Trust.*—

"(i) *Corporation's Functions.*—Except as provided in clause (ii), the corporation shall serve as trustee of the trust for purposes of administering the trust, including making distributions from the trust to participants and beneficiaries.

"(ii) *Designation of Fiduciary if Cost-Effective.*—If the corporation determines that it would be cost-effective to do so, it may designate a fiduciary (within the meaning of section 3(21)), including the fiduciary designated under subparagraph (A), to perform the functions described in clause (i).

"(2) *Fiduciary Requirements.*—A fiduciary designated under paragraph (1) shall be—

"(A) independent of each contributing sponsor of the plan and the members of such sponsor's controlled group, and

"(B) subject of the requirements of part 4 of subtitle B of title I (other than section 406(a)) as if such trust were a plan subject to such part.

"(c) *Distributions From Trust.*—

"(1) *In General.*—Not later than 30 days after the end of each liability payment year (described in section 4062(e)(3)) with respect to a terminated single-employer plan, the corporation, or its designee under subsection (b), shall distribute from the trust maintained termination date) a participant or beneficiary under the plan—

"(A) in any case not described in subparagraph (B), and amount equal to the outstanding amount of benefit commitments to such person under the plan (including interest calculated from the termination date), to the extent not previously paid under this paragraph, or

"(B) in any case in which the balance in the trust at the end of such year which is in cash or may be prudently converted to cash (after taking into account liability payments received under subsection (a)(1) and administrative expenses paid under subsection (a)(3)) is less than the total of all amounts described in subparagraph (A) in connection with all persons who were (as of the termination date) participants and beneficiaries under the terminated plan, the product derived by multiplying—

"(i) the amount described in subparagraph (A) in connection with each such person, by

"(ii) a fraction—

"(I) the numerator of which is such balance in the trust, and

"(II) the denominator of which is equal of the total of all amounts described in subparagraph (A) in connection with all persons who were (as of the termination date) participants and beneficiaries under the terminated plan.

"(2) *Carry-Over or Minimal Payment Amounts.*—The corporation, or its designee under subsection (b), may withhold a payment to any person under this subsection in connection with any liability payment year (other than the last liability payment year with respect to which payments under paragraph (1) are payable) if such payment does not exceed $100. In any case in which sdch a payment is so withheld, the payment to such person in connection with the next following liability payment year shall be increased by the amount of such withheld payment.

"(d) *Regulations.*—The corporation may issue such regulations as it considers necessary to carry out the purposes of this section.".

(b) *Tax-Exempt Status for Trusts Described in Section 4049 of ERISA.*—Subsection (c) of section 501 of the Internal Revenue Code of 1954 (relating to list of tax-exempt organizations) is amended by adding at the end thereof the following new paragraph:

"(24) A trust described in section 4049 of the Employee Retirement Income Security Act of 1974 (as in effect on the date of the enactment of the Single-Employer Pension Plan Amendments Act of 1986).".

(c) *Rollovers of Payments from Trust Allowed.*—Paragraph (6) of section 402(a) of such Code (relating to special rollover rules) is amended by adding at the end thereof the following new subparagraph:

"(G) *Payments from Certain Pension Plan Termination Trusts.*—If—

"(i) any amount is paid or distributed to a recipient from a trust described in section 501(c)(24),

"(ii) the recipient transfers any portion of the property received in such distribution to an eligibile retirement plan described in subclause (I) or (II) of paragraph (5)(E)(iv), and

"(iii) in the case of a distribution of property other than money, the amount so transferred consists of the property distributed,

then the portion of the distribution so transferred shall be treated as a distribution described in paragraph (5)(A).".

(d) *Special Delayed Payment Rule.*—In the case of a distress termination under section 4041(c) of the Employee Retirement Income Security Act of 1974 (as amended by section 11009) pursuant to a notice of intent to terminate filed before January 1, 1987, no payment of liability otherwise payable as provided in section 4062(c)(2)(B) of such Act (as amended by this section) shall be required to be made before January 1, 1989.

Section 11013.—Treatment of Transactions to Evade Liability; Effect of Corporate Reorganization

(a) *In General.*—Subtitle D of title IV is amended by adding at the end thereof the following new section:

"Treatment of Transactions to Evade Liability; Effect of Corporate Reorganization

"Section 4069. (a) Treatment of Transactions to Evade Liability.—If a principal purpose of any person in entering into any transaction is to evade liability to which such person would be subject under this subtitle and the transaction becomes effective within five years before the termination date of the termination on which such liability would be based, then such person and the members of such person's controlled group (determined as of the termination date) shall be subject to liability under this subtitle in connection with such termination as if such person were a contributing sponsor of the terminated plan as of the termination date. This subsection shall not cause any person to be liable unde this subtitle in connection with such plan termination for any increases or improvements in the benefits provided under the plan which are adopted after the date on which the transaction referred to in the preceding sentence becomes effective.

"(b) *Effect of Corporate Reorganization.*—For purposes of this subtitle, the following rules apply in the case of certain corporate reorganizations:

"(1) *Change of Identity, Form, Etc.*—If a person ceases to exist by reason of a reorganization which involves a mere change in identify, form, or place of organization, however effected, a successor corporation resulting from such reorganization shall be treated as the person to whom this subtitle applies.

"(2) *Liquidation into Parent Corporation.*—If a person ceases to exist by reason of liquidation into a parent corporation, the parent corporation shall be treated as the person to whom this subtitle applies.

"(3) *Merger, Consolidation, or Division.*—If a person ceases to exist by reason of a merger, consolidation, or division, the successor corporation or corporations shall be treated as the person to whom this subtitle applies.".

(b) *Effective Date.*—Section 4069(a) of the Employee Retirement Income Security Act of 1974 (as added by subsection (a)) shall apply with respect to transactions becoming effective on or after January 1, 1986.

Section 11014.—Enforcement Authority Relating to Terminations of Single-Employer Plans

(a) *Private Rights of Action.*—Subtitle D of title IV (as amended by section 11013) is further amended by adding at the end thereof the following new section:

"Enforcement Authority Relating to Termination of Single Employer Plans

"Section 4070. (a) In General.— Any person who is with respect to a single-employer plan a fiduciary, contributing sponsor, member of a contributing sponsor's controlled group, participant, or beneficiary, and is adversely affected by an act or practice of any party (other than the corporation) in violation of any provision of section 4041, 4042, 4049, 4063, 4064, or 4069, or who is an employee organization representing such a participant or beneficiary so adversely affected for purposes of collective bargaining with respect to such plan, may bring an action—

"(1) to enjoin such act or practice, or

"(2) to obtain other appropriate equitable relief (A) to redress such violation or (B) to enforce such provision.

"(b) *Status of Plan as Party to Action and With Respect to Legal Process.*—A single-employer plan may be sued under this section as an entity. Service of summons, subpoena, or other legal process of a court upon a trustee or an administrator of a single-employer plan in such trustee's or administrator's capacity as such shall constitute service upon the plan. If a plan has not designated in the summary plan description of the plan an individual as agent for the service of legal process, service upon any contributing sponsor of the plan shall constitute such service. Any money judgment under this section against a single-employer plan shall be enforceable only against the plan as an entity and shall not be enforceable against any other person unless liability against such person is established in such person's individual capacity.

"(c) *Jurisdiction and Venue.*— The district courts of the United States shall have exclusive jurisdiction of civil actions under this section. Such actions may be brought in the district where the plan is administered, where the violation took place, or where a defendant resides or may be found, and process may be served in any other district where a defendant resides or may be found. The district courts of the United States shall have jurisdiction, without regard to the amount in controversy or the citizenship of the parties, to grant the relief provided for in subsection (a) in any action.

"(d) *Right of Corporation to Intervene.*—A copy of the complaint or notice of appeal in any action under this section shall be served upon the corporation by certified mail. The corporation shall have the right in its discretion to intervene in any action.

"(e) *Awards of Costs and Expenses.*—

"(1) *General Rule.*—In any action brought under this section, the court in its discretion may award all or a portion of the costs and expenses incurred in connection with such action, including reasonable attorney's fees, to any party who prevails or substantially prevails in such action.

"(2) *Exemption for Plans.*—Notwithstanding the preceding provision of this subsection, no plan shall be required in any action to pay any costs and expenses (including attorney's fees).

"(f) *Limitation on Actions.*—

"(1) *In General.*—Except as provided in paragraph (3), an action under this section may not be brought after the later of—

"(A) 6 years after the date on which the cause of action arose, or

"(B) 3 years after the applicable date specified in paragraph (2).

"(2) *Applicable Date.*—

"(A) *General Rule.*— Except as provided in subparagraph (B), the applicable date specified in this paragraph is the earliest date on which the plaintiff acquired or should have acquired actual knowledge of the existence of such cause of action.

"(B) *Special Rule for Plaintiffs Who are Fiduciaries.*—In the case of a plaintiff who is a fiduciary bringing the action in the exercise of fiduciary duties, the applicable date specified in this paragraph is the date on which the plaintiff became a fiduciary with respect to the plan if such date is later than the date described in subparagraph (A).

"(3) *Cases of Fraud or Concealment.*— In the case of fraud or concealment, the period described in paragraph (1)(B) shall be extended to 6 years after the applicable date specified in paragraph (2).".

(b) *Civil Actions Involving the Pension Benefit Guaranty Corporation.*—

(1) *Actions Against the Corporation.*— Section 4003(f) (29 U.S.C. 1303(f)) is amended to read as follows:

"(f)(1) Except with respect to withdrawal liability disputes under part 1 of subtitle E, any person who is a fiduciary, employer, contributing sponsor, member of a contributing sponsor's controlled group, participant, or beneficiary, and is adversely affected by any action of the corporation with respect to a plan in which such person has an interest, or who is an employee organization representing such a participant or beneficiary so adversely affected for purposes of collective bargaining with respect to such plan, may bring an action against the corporation for appropriate equitable relief in the appropriate court.

"(2) For purpose of this subsection, the term 'appropriate court' means—

"(A) the United States district court before which proceedings under section 4041 or 4042 are being conducted,

"(B) if no such proceedings are being conducted, the United States district court for the judicial district in which the plan has its principal office, or

"(C) the United States District Court for the District of Columbia.

"(3) In any action brought under this subsection, the court may award all or a portion of the costs and expenses incurred in connection with such action to any party who prevails or substantially prevails in such action.

"(4) This subsection shall be the exclusive means for bringing actions against the corporation under this title, including actions against the corporation in its capacity as a trustee under section 4042 or 4049.

"(5)(A) Except as provided in subparagraph (C), an action under this subsection may not be brought after the later of—

"(i) 6 years after the date on which the cause of action arose, or

"(ii) 3 years after the applicable date specified in subparagraph (B).

"(B)(i) Except as provided in clause (ii), the applicable date specified in this subparagraph is the earliest date on which the plaintiff acquired or should have acquired actual knowledge of the existence of such cause of action.

"(ii) In the case of a plaintiff who is a fiduciary bringing the action in the exercise of fiduciary duties, the applicable date specified in this subparagraph is the date on which the plaintiff became a fiduciary with respect to the plan if such date is later than the date specified in clause (i).

"(C) In the case of fraud or concealment, the period described in subparagraph (A)(ii) shall be extended to 6 years after the applicable date specified in subparagraph (B).

"(6) The district courts of the United States have jurisdiction of actions brought under this subsection without regard to the amount in controversy.

"(7) In any suit, action, or proceeding in which the corporation is a party, or intervenes under section 4301, in any State court, the corporation may without bond or security, remove such suit, action, or proceeding from the State court to the United States district court for the district or division in which such suit, action, or proceeding is pending by following any procedure for removal now or hereafter in effect.".

(2) *Limitation on Actions by the Corporation.*—Section 4003(e) (29 U.S.C. 1303(e)) is amended by adding at the end thereof the following new paragraph:

"(6)(A) Except as provided in subparagraph (C), an action under this subsection may not be brought after the later of—

"(i) 6 years after the date on which the cause of action arose, or

"(ii) 3 years after the applicable date specified in subparagraph (B).

"(B)(i) Except as provided in clause (ii), the applicable date specified in this subparagraph is the earliest date on which the corporation acquired or should have acquired actual knowledge of the existence of such cause of action.

"(ii) If the corporation brings the action as a trustee, the applicable date specified in this subparagraph is the date on which the corporation became a trustee with respect to the plan if such date is later than the date described in clause (i).

"(C) In the case of fraud or concealment, the period described in subparagraph (A)(ii) shall be extended to 6 years after the applicable date specified in subparagraph (B).".

(3) *Effective Date.*—The amendments made by this subsection shall apply with respect to actions filed after the date of the enactment of this Act.

Section 11015.—Provisions relating to waivers of minimum funding standard and extensions of amortization period

(a) *Security for Waivers.*—

(1) *ERISA amendment.*—

(A) *In general.*—Part 3 of subtitle B of title I is amended.—

(i) by redesignating section 306 (29 U.S.C. 1086) as section 307; and

(ii) by inserting after section 305 (29 U.S.C. 1085) the following new section:

"Security for waivers of minimum funding standard and extensions of amortization period

"Sec. 306 (a) *Security May Be Required.*—

"(1) *In general.*—Except as provided in subsection (c), the Secretary of the Treasury may require an employer maintaining a defined benefit plan which is a single-employer plan (within the meaning of section 4001(a)(15)) to provide security to such plan as a condition for granting or modifying a waiver under section 303 or an extension under section 304.

"(2) *Special rules.*—Any security provided under paragraph (1) may be perfected and enforced only by the Pension Benefit Guaranty Corporation or, at the direction of the Corporation, by a contributing sponsor (within the meaning of section 4001(a)(13)) or a member of such sponsor's controlled group (within the meaning of section 4001(a)(14)).

"(b) *Consultation With the Pension Benefit Guaranty Corporation.*—Except as provided in subsection (c), the Secretary of the Treasury shall, before granting or modifying a waiver under section 303 or an extension under section 304 with respect to a plan described in subsection (a)(1)—

"(1) provide the Pension Benefit Guaranty Corporation with—

"(A) notice of the completed application for any waiver, extension, or modification, and

"(B) an opportunity to comment on such application within 30 days after receipt of such notice, and

"(2) consider—

"(A) any comments of the Corporation under paragraph (1)(B), and

"(B) any views of any employee organization representing participants in the plan which are submitted in writing to the Secretary of the Treasury in connection with such application.

Information provided to the corporation under this subsection shall be considered tax return information and subject to the safeguarding and reporting requirements of section 6103(p) of the Internal Revenue Code of 1954.

"(c) *Exception for Certain Waivers and Extensions.*—

"(1) *In general.*—The preceding provisions of this section shall not apply to any plan with respect to which the sum of—

"(A) the outstanding balance of the accumulated funding deficiencies (within the meaning of section 302(a)(2) of this Act and section 412(a) of the Internal Revenue Code of 1954) of the plan,

"(B) the outstanding balance of the amount of waived funding deficiencies of the plan waived under section 303 of this Act or section 412(d) of such Code, and

"(C) the outstanding balance of the amount of decreases in the minimum funding standard allowed under section 304 of this Act or section 412(e) of such Code, is less than $2,000,000.

"(2) *Accumulated funding deficiencies.*—For purposes of paragraph (1)(A), accumulated funding deficiencies shall include any increase in such amount which would result if all applications for waivers of the minimum funding standard under section 303 of this Act or section 412(d) of the Internal Revenue Code of 1954 and for extensions of the amortization period under section 304 of this Act or section 412(e) of such Code which are pending with respect to such plan were denied.".

(B) *Conforming amendment.*—Section 211(c)(1) is amended by striking out "306(c)" and inserting in lieu thereof "307(c)".

(c) *Clerical amendment.*—The table of sections in section 1 is amended by striking out the item relating to section 306 and inserting in lieu thereof the following new items:

"Sec. 306. Security for waivers of minimum funding standard and extensions of amortization period.

"Sec. 307. Effective dates."

(2) *Amendments to the Internal Revenue Code of 1954.*—

(A) *In general.*—Subsection (f) of section 412 of the Internal Revenue Code of 1954 (relating to requirement that benefits may not be increased during waiver or extension period) is amended by adding at the end thereof the following new paragraph:

"(3) *Security for waivers and extensions; consultations.*—

"(A) *Security may be required.*—

"(i) *In general.*—Except as provided in subparagraph (C), the Secretary may require an employer maintaining a defined benefit plan which is a single-employer plan (within the meaning of section 4001(a)(15) of the Employee Retirement Income Security Act of 1974) to provide security to such plan as a condition for granting or modifying a waiver under subsection (d) or an extension under subsection (e).

"(ii) *Special Rules.*—Any security provided under clause (i) may be perfected and enforced only by the Pension Benefit Guaranty Corporation, or at the direction of the Corporation, by a contributing sponsor (within the meaning of section 4001(a)(13) of such Act), or a member of such sponsor's controlled group (within the meaning of section 4001(a)(14) of such Act).

"(B) *Consultation with the Pension Benefit Guaranty Corporation.*—Except as provided in subparagraph (C), the Secretary shall, before granting or modifying a waiver under subsection (d) or an extension under subsection (e) with respect to a plan described in subparagraph (A)(i)—

"(i) provide the Pension Benefit Guaranty Corporation with—

"(I) notice of the completed application for any waiver, extension, or modification, and

"(II) an opportunity to comment on such application within 30 days after receipt of such notice, and

"(ii) consider—

"(I) any comments of the Corporation under clause (i)(II), and

"(II) any views of any employee organization (within the meaning of section 3(4) of the Employee Retirement Income Security Act of 1974) representing participants in the plan which are submitted in writing to the Secretary in connection with such application.

Information provided to the corporation under this subparagraph shall be considered tax return information and subject to the safeguarding and reporting requirements of section 6103(p).

"(C) *Exception for Certain Waivers and Extensions.*—

"(i) *In general.*—The preceding provisions of this paragraph shall not apply to any plan with respect to which the sum of—

"(I) the outstanding balance of the accumulated funding deficiencies (within the meaning of subsection (a) and section 302(a) of such Act) of the plan,

"(II) the outstanding balance of the amount of waived funding deficiencies of the plan waived under subsection (d) or section 303 of such Act, and

"(III) the outstanding balance of the amount of decreases in the minimum funding standard allowed under subsection (e) or section 304 of such Act,

is less than $2,000,000.

"(ii) *Accumulated Funding Deficiences.*—For purposes of clause (i)(I), accumulated funding deficiencies shall include any increase in such amount which would result if all applications for waivers of the minimum funding standard under subsection (d) or section 303 of such Act and for extensions of the amortization period under subsection (e) or section 304 of such Act which are pending with respect to such plan were denied.".

(D) *Conforming amendments.*—Section 412(f) of the Internal Revenue Code of 1954 is amended—

(i) by striking out the heading thereof and inserting in lieu thereof:

"(f) *Requirements Relating to Waivers and Extensions.*—", and

(ii) by striking out the heading of paragraph (1) thereof and inserting in lieu thereof:

"(1) *Benefits may not be increased during waiver or extension period.*—".

(3) *Effective Dates.*—The amendments made by this subsection shall apply with respect to applications for waivers, extensions, and modifications filed on or after the date of the enactment of this Act.

(b) *Applicable Interest Rate Under Arrangements Providing for Waivers and Extensions.*—

(1) *Amendments to ERISA.*—

(A) *Variances from the minimum funding standard.*—Section 303(a) (29 U.S.C. 1083(a)) is amended by adding at the end thereof the following new sentence: "The interest rate used for purposes of computing the amortization charge described in section 302(b)(2)(C) for a variance granted under this subsection shall be the rate determined under section 6621(b) of the Internal Revenue Code of 1954.".

(B) *Extenions of the amortization period.*—Section 304(a) (29 U.S.C. 1084(a)) is amended by adding after and below paragraph (2) followig new sentence:

"The interest rate applicable under any arrangement entered into by the Secretary in connection with an extension granted under this subsection shall be the rate determined under section 6621(b) of the Internal Revenue Code of 1954.".

(2) *Amendments to Internal Revenue Code.*—

(A) *Variances from the Minimum Funding Standard.*—Paragraph (1) of section 412(d) of the Internal Revenue Code of 1954 (relating to waivers in case of substantial business hardship) is amended by adding at the end thereof the following new sentence: "The interest rate used for purposes of computing the amortization charge described in section 412(b)(2)(C) for a variance granted under this subsection shall be the rate determined under section 6621(b).".

(B) *Extensions of the amortization period.*—Subsection (e) of section 412 of such Code (relating to extension of amortization period) is amended by adding after and below paragraph (2) the following new sentence:

"The interest rate applicable under any arrangement entered into by the Secretary in connection with an extension granted under this subsection shall be the rate determined under section 6621(b).".

Section 11016.—Conforming, Clarifying, Technical, and Miscellaneous Amendments

(a) *Conforming Amendments Relating to Plan Terminations.*—

(1) *Estimated Benefits for Certain Single-Employer Plans.*—Section 4005(b)(2) (29 U.S.C. 1305(b)(2)) is amended—

(A) by striking out "and" at the end of subparagraph (C);

(B) by striking out the period at the end of subparagraph (D) and inserting in lieu thereof ", and"; and

(C) by adding at the end thereof the following:

"(E) to pay to participants and beneficiaries the estimated amount of benefits which are guaranteed by the corporation under this title and estimated amount of other benefits to which plan assets are allocated under section 4044, under single-employer plans which are unable to pay benefits when due or which are abandoned.".

(2) *Credits to revolving fund.*—Section 4005(b)(1) (29 U.S.C. 1305(b)(1)) is amended—

(A) by striking out "and" at the end of subparagraph (E);

(B) by redesignating subparagraph (F) as subparagraph (G); and

(C) by inserting after subparagraph (E) the following new subparagraph:

"(F) attorney's fees awarded to the corporation, and".

(3) *Restoration of plans.*—Section 4047 (29 U.S.C. 1347) is amended—

(A) in the first sentence, by inserting "under section 4041 or 4042" after "terminated" each place it appears; and

(B) in the second sentence, by striking out "section 4042" and inserting in lieu thereof "section 4041 or 4042".

(4) *Termination date.*—Section 4048(a) (29 U.S.C. 1348(a)) is amended—

(A) by striking out "date of termination" and inserting in lieu thereof "termination date";

(B) by redesignating paragraphs (1) through (3) as paragraphs (2) through (4), respectively;

(C) in paragraph (2) (as redesignated), by inserting "in a distress termination" after "terminated" and by striking out "section 4041" and inserting in lieu thereof" "section 4041(c)";

(D) by inserting before paragraph (2) (as redesignated) the following new paragraph:

"(1) in the case of a plan terminated in a standard termination in accordance with the provisions of section 4041(b), the termination date proposed in the notice provided under section 4041(a)(2),";

and

(E) in paragraph (4) (as redesignated), by striking out "in accordance with the provisions of either section" and inserting in lieu thereof "under section 4041(c) or 4042".

(5) *Conforming amendments to special liability rules relating to certain single-employer plans under multiple controlled groups.*—

(a) *Liability of substantial employer for withdrawal.*—

(i) Section 4063(a) (29 U.S.C. 1363(a)) is amended—

(I) by striking out "plan under which more than one employer makes contributions (other than a multiemployer plan)" and inserting in lieu thereof "single-employer plan which has two or more contributing sponsors at least two of whom are not under common control";

(II) in paragraph (1), by striking out "withdrawal of a substantial employer" and inserting in lieu thereof "withdrawal during a plan year of a substantial employer for such plan year";

(III) in paragraph (2), by striking out "of such employer" and all that follows and inserting in lieu thereof "of all persons with respect to the withdrawal of the substantial employer.";

(IV) by striking out "whether such employer is liable for any amount under this subtitle with respect to the withdrawal" and inserting in lieu thereof "whether there is liability resulting from the withdrawal of the substantial employer"; and

(V) by striking out "notify such employer" and inserting in lieu thereof "notify the liable persons".

(ii) Section 4063(b) (29 U.S.C. 1363(b)) is amended—

(I) by striking out "an employer" and all that follows down through "shall be liable" and inserting in lieu thereof "any one or more contributing sponsors who withdraw, during a plan year for which they constitute a substantial employer, from a single-employer plan which has two or more contributing sponsors at least two of whom are not under common control, shall upon notification of such contributing sponsors by the corporation as provided by subsection (a), be liable, together with the members of their controlled groups,";

(II) by striking out "such employer's";

(III) by striking out "the employer's withdrawal" and inserting in lieu thereof "the withdrawal referred to in subsection (A)(1)";

(IV) in paragraph (1), by striking out "such employer" and inserting in lieu thereof "such contributing sponsors";

(V) in paragraph (2), by striking out "all employers" and inserting in lieu thereof "all contributing sponsors"; and

(VI) by striking out "the liability of each such employer" and inserting in lieu thereof "such liability".

(iii) Section 4063(c) (29 U.S.C. 1363(c)) is amended—

(I) in paragraph (1), by striking out "In lieu of payment of his liability under this section the employer" and inserting in lieu thereof "In lieu of payment of a contributing sponsor's liability under this section, the contributing sponsor";

(II) in paragraph (2), by inserting "under section 4041(c) or 4042" after "terminated", by striking out "of such employer", and by striking out "to the employer (or his bond cancelled)" and inserting in lieu thereof "(or the bond cancelled)"; and

(III) in paragraph (3), by inserting "under section 4041(c) or 4042" after "terminates" and by striking out "employer" in subparagraph (C) and inserting in lieu thereof "contributing sponsor".

(iv) Section 4063(d) (29 U.S.C. 1363(d)) is amended—

(I) by striking out "Upon a showing by the plan administrator of a plan (other than a multiemployer plan) that the withdrawal from the plan by any employer or employers has resulted" and inserting in lieu thereof "Upon a showing by the plan administrator of the plan that the withdrawal from the plan by one or more contributing sponsors has resulted";

(II) by striking out "by employers";

(III) in paragraph (2) by striking out "their employer's" and inserting in lieu thereof "the"; and

(IV) in paragraph (2), by striking out "termination" and inserting in lieu thereof "plan terminated under section 4042".

(v) Section 4063(e) (29 U.S.C. 1363(e)) is amended—

(I) by striking out "to any employer or plan adminstrator"; and

(II) by striking out "all other employers" and inserting in lieu thereof "contributing sponsors".

(vi) The heading for section 4063 is amended by adding at the end thereof the following "*from single employer plans under multiple controlled groups.*".

(B) *Allocation of liability upon termination of certain single-employer plans.*—

(i) Section 4064(a) (29 U.S.C. 1364(a)) is amended—

(I) by striking out "all employers who maintain a plan under which more than one employer makes contributions (other than a multiemployer plan)" and inserting in lieu thereof "all contributing sponsors of a single-employer plan which has two or more contributing sponsors at least two of whom are not under common control"; and

(II) by inserting "under section 4041(c) or 4042" after "terminated".

(ii) Section 4064(b) (29 U.S.C. 1364(b)) is amended to read as follows:

"(b) The corporation shall determine the liability with respect to each contributing sponsor and each member of its controlled group in a manner consistent with section 4062, except that—

"(1) the amount of the liability determined under section 4062(b)(1) with respect to the entire plan—

"(A) shall be determined without regard to clauses (i)(II) and (ii) of section 4062(b)(1)(A), and

"(B) shall be allocated to each controlled group by multiplying such amount by a fraction—

"(i) the numerator of which is the amount required to be contributed to the plan for the last 5 plan years ending prior to the termination date by persons in such controlled group as contributing sponsors, and

"(ii) the denominator of which is the total amount required to be contributed to the plan for such last 5 plan years by all persons as contributing sponsors, and clauses (i)(II) and (ii) of section 4062(b)(1)(A) shall be applied separately with respect to each such controlled group, and

"(2) the amount of the liability determined under section 4062(c)(1) with respect to the entire plan shall be allocated to each controlled group by multiplying such amount by the fraction described in paragraph (1)(B) in connection with such controlled group.

The corporation may also determine the liability of each such contributing sponsor and member of its controlled group on any other equitable basis prescribed by the corporation in regulations.".

(iii) The heading for section 4064 is amended to read as follows:

"*Liability on termination of single-employer plans under multiple controlled groups*".

(C) *Annual notification to substantial employers.*

Section 4066 (29 U.S.C. 1366) is amended—

(i) by striking out "each plan under which contributions are made by more than one employer (other than a multiemployer plan)" and inserting in lieu thereof "each single-employer plan which has at least two contributing sponsors at least two of whom are not under common control";

(ii) by striking out "any employer making contributions under that plan" and inserting in lieu thereof "contributing sponsor of the plan"; and

(iii) by striking out "that he is a substantial employer" and inserting in lieu thereof "that such contributing sponsor (alone or together with members of such contributing sponsor's controlled group) constitutes a substantial employer".

(6) *Additional amendments relating to recovery of amounts of liability.*—

(A) Section 4067 (29 U.S.C. 1367) is amended—

(i) in the heading, by striking out "*employer*";

(ii) by striking out "employer or employers" and inserting in lieu thereof "contributing sponsors and members of their controlled groups"; and

(iii) by inserting "of amounts of liability to the corporation accruing as of the termination date" after "deferred payment".

(B) Section 4068 (29 U.S.C. 1368) is amended—

(i) in the heading, by striking out "*of employer*";

(ii) in subsection (a), by striking out "employer or employers" the first place it appears and inserting in lieu thereof "person", by striking out "neglect or refuse" and inserting in lieu thereof "neglects or refuses", by inserting "to the extent of an amount equal to the unpaid amount described in section 4062(b)(1)(A)(i)" after "liability" and after "corporation" the second place it appears, and by striking out "employer or employers" and inserting in lieu thereof "person";

(iii) in subsection (d)(1), by striking out "employer" and inserting in lieu thereof "liable person";

(iv) in subsection (d)(2), by striking out "employer" each place it appears and inserting in lieu thereof "liable person";

(v) in subsection (e), by striking out "employer or employers" and inserting in lieu thereof "liable person"; and

(vi) by striking out subsection (c)(1) (29 U.S.C. 1368(c)(1)) and inserting in lieu thereof the following:

"(c)(1) Except as otherwise provided under this section, the priority of a lien imposed under subsection (a) shall be determined in the same manner as under section 6323 of the Internal Revenue Code of 1954 (as in effect on the date of the enactment of the Single-Employer Pension Plan Amendments Act of 1986). Such section 6323 shall be applied for purposes of this section by disregarding subsection (g)(4) and by substituting—

"(A) 'lien imposed by section 4068 of the Employee Retirement Income Security Act of 1974' for 'lien imposed by section 6321' each place it appears in subsections (a), (b), (c)(1), (c)(4)(B), (d), (e), and (h)(5);

"(B) 'the corporation' for 'the Secretary' in subsections (a) and (b)(9)(C);

"(C) 'the payment of the amount on which the section 4068(a) lien is based' for 'the collection of any tax under this title' in subsection (b)(3);

"(D) 'a person whose property is subject to the lien' for 'the taxpayer' in subsections (b)(8), (c)(2)(A)(i) (the first place it appears), (c)(2)(A)(ii), (c)(2)(B), (c)(4)(B), and (c)(4)(C) (in the matter preceding clause (i));

"(E) 'such person' for 'the taxpayer' in subsections (c)(2)(A)(i) (the second place it appears) and (c)(4)(C)(ii);

"(F) 'payment of the loan value of the amount on which the lien is based is made to the corporation' for 'satisfaction of a levy pursuant to section 6332(b)' in subsection (b)(9)(C);

"(G) 'section 4068(a) lien' for 'tax lien' each place it appears in subsections (c)(1), (c)(2)(A), (c)(2)(B), (c)(3)(B)(iii), (c)(4)(B), (d), and (h)(5); and

"(H) 'the date on which the lien is first filed' for 'the date of the assessment of the tax' in subsection (g)(3)(A).".

(b) *Clarification of Description of Certain Information Required To Be Filed in Annual Report.*—

(1) *In general.*—Section 103(d)(6) (29 U.S.C. 1023(d)(6)) is amended to read as follows:

"(6) Information required in regulations of the Pension Benefit Guaranty Corporation with respect to:

"(A) the current value of the assets of the plan,

"(B) the present value of all nonforfeitable benefits for participants and beneficiaries receiving payments under the plan,

"(C) the present value of all nonforfeitable benefits for all other participants and beneficiaries,

"(D) the present value of all accrued benefits which are not nonforfeitable (including a separate accounting of such benefits which are benefit commitments, as defined in section 4001(a)(16)), and

"(E) the actuarial assumptions and techniques used in determining the values described in subparagraphs (A) through (D).".

(2) *Conforming amendment.*—Section 104(a)(2)(A) (29 U.S.C. 1024(a)(2)(A)) is amended by striking out the second sentence.

(3) *Transition rules.*—Any regulations, modifications, or waivers which have been issued by the Secretary of Labor with respect to section 103(d)(6) of the Employee Retirement Income Security Act of 1974 (as in effect immediately before the date of the enactment of this Act) shall remain in full force and effect until modified by any regulations with respect to such section 103(d)(6) prescribed by the Pension Benefit Guaranty Corporation.

(c) *Additional Amendments.*—

(1) *Definition for title I.*—Section 3(37)(A) (29 U.S.C. 1002(37)(A)) is amended by inserting "pension" before "plan".

(2) *Notice of request for waivers of minimum funding standards and right to submit relevant information.*—Section 303 (29 U.S.C. 1083) is amended by inserting after subsection (d) the following new subsection:

"(e)(1) The Secretary of the Treasury shall, before granting a waiver under this section, require each applicant to provide evidence satisfactory to such Secretary that the applicant has provided notice of the filing of the application for such waiver to each employee organization representing employees covered by the affected plan.

"(2) The Secretary of the Treasury shall consider any relevant information provided by a person to whom notice was given under paragraph (1).".

(3) *Notice of request for extensions of amortization period and right to submit relevant information.*—Section 304 (29 U.S.C. 1084) is amended by adding at the end thereof the following new subsection:

"(c)(1) The Secretary of the Treasury shall, before granting an extension under this section, require each applicant to provide evidence satisfactory to such Secretary that the applicant has provided notice of the filing of the application for such extension to each employee organization representing employees covered by the affected plan.

"(2) The Secretary of the Treasury shall consider any relevant information provided by a person to whom notice was given under paragraph (1).".

(4) *Amendment to the internal revenue code of 1954.*—Subsection (f) of section 412 of the Internal Revenue Code of 1954 (relating to benefits may not be increased during waiver or extension period), as amended by the preceding provisions of this title, is further amended by adding at the end thereof the following new paragraph:

"(4) *Additional requirements.*—

"(A) *Advance notice.*—The Secretary shall, before granting a waiver under subsection (d) or an extension under subsection (e), require each applicant to provide evidence satisfactory to the Secretary that the applicant has provided notice of the filing of the application for such waiver or extension to each employee organization representing employees covered by the affected plan.

"(B) *Consideration of relevant information.*—The Secretary shall consider any relevant information provided by a person to whom notice was given under subparagraph (A)".

(5) *Audit of plans terminated in standard termination.*—Section 4003(a) (29 U.S.C. 1303(a)) is amended by adding at the end thereof the following new sentence: "The corporation shall annually audit a statistically significant number of plans terminating under section 4041(b) to determine whether participants and beneficiaries have received their benefit commitments. Each audit shall include a statistically significant number of participants and beneficiaries.".

(6) *Repeal of expired authority.*—Section 4004 (29 U.S.C. 1304) is repealed.

(7) *Voting by corporation of stock paid as liability.*—Section 4005 (29 U.S.C. 1305) is amended by adding at the end thereof the following new subsection:

"(g) Any stock in a person liable to the corporation under this title which is paid to the corporation by such person or a member of such person's controlled group in satisfaction of such person's liability under this title may be voted only by the custodial trustees or outside money managers of the corporation or fiduciaries with respect to trusts to which the requirements of section 4049 apply.".

(8) *Effective years.*—Section 4022(b)(7) (29 U.S.C. 1322(b)(7)) is amended by striking out "following" and inserting in lieu thereof "beginning with".

(9) *Treatment of qualified preretirement survivor annuities.*—Section 4022 (29 U.S.C. 1322) is amended by adding at the end thereof the following new subsection:

"(d) For purposes of subsection (a), a qualified preretirement survivor annuity (as defined in section 205(e)(1)) with respect to a participant under a terminated single-employer plan shall not be treated as forfeitable solely because the participant has not died as of the termination date.".

(10) *Clarification of power to collect amounts due the corporation.*—Section 4042(d)(1)(B)(ii) (29 U.S.C. 1342(d)(1)(B)(ii)) is amended by inserting after "amounts due the plan" the following: ", including but not limited to the power to collect from the persons obligated to meet the requirements of section 302 or the terms of the plan".

(11) *Conforming amendment.*—Section 4042(d)(3) (29 U.S.C. 1342(d)(3)) is amended by striking out "same duties as a trustee appointed under section 47 of the Bankruptcy Act" and inserting in lieu thereof "same duties as those of a trustee under section 704 of title 11, United States Code".

(12) *Conforming amendment.*—Section 4044(a) (29 U.S.C. 1344(a)) is amended by striking out "defined benefit".

(13) *Clerical corrections.*—Section 4044(a)(4) (29 U.S.C. 1344(a)(4)(A)) is amended—

(A) in subparagraph (A), by striking out "section 4022(b)(5)" and inserting in lieu thereof "section 4022B(a)"; and

(B) in subparagraph (B), by striking out "section 4022(b)(6)" and inserting in lieu thereof "section 4022(b)(5)".

(14) *Release of lien.*—Section 4068(e) (29 U.S.C. 1368(e)) is amended by striking out ", with the consent of the board of directors,".

(d) *Studies by Comptroller General.*—

(1) *In general.*—The Comptroller General of the United States may, pursuant to the request of any Member of Congress, study employee benefit plans, including the effects of such plans on employees, participants, and their beneficiaries.

(2) *Access to books, documents, etc.*—For the purpose of conducting studies under this subsection, the Comptroller General, or any of his duly authorized representatives, shall have access to and the right to examine and copy any books, documents, papers, records, or other recorded information—

(A) within the possession or control of the administrator, sponsor, or employer of and persons providing services to any employee benefit plan, and

(B) which the Comptroller General or his representative finds, in his own judgment, pertinent to such study.

The Comptroller General shall not disclose the identity of any individual or employer in making any information obtained under this subsection available to the public.

(3) *Definitions.*—For purposes of this subsection, the terms "employee benefit plan", "participant", "administrator", "beneficiary", "plan sponsor", "employee", and "employer" are defined in section 3 of the Employee Retirement Income Security Act of 1974.

(4) *Effective date.*—The preceding provisions of this subsection shall be effective on the date of the enactment of this Act.

(e) *Amendments to the Table of Contents of ERISA.*—The table of contents in section 1 is amended—

(1) by striking out the item relating to section 4004;

(2) by striking out the item relating to section 4042 and inserting in lieu thereof the following new item:

"Sec. 4042. Institution of termination proceedings by the corporation.";

(3) by inserting after the item relating to section 4048 the following new item:

"Sec. 4049. Distribution to participants and beneficiaries of liability payments to section 4049 trust.";

and

(4) by striking out the items relating to subtitle D of title IV and inserting in lieu thereof the following new items:

"Subtitle D—Liability

"Sec. 4061. Amounts payable by the corporation.
"Sec. 4062. Liability for termination of single-employer plans under a distress termination or a termination by the corporation.
"Sec. 4063. Liability of substantial employer for withdrawal from single-employer plans under multiple controlled groups.
"Sec. 4064. Liability on termination of single-employer plans under multiple controlled groups.
"Sec. 4065. Annual report of plan administrator.
"Sec. 4066. Annual notification of substantial employers.
"Sec. 4067. Recovery of liability for plan termination.
"Sec. 4068. Lien for liability.
"Sec. 4069. Treatment of transactions to evade liability; effect of corporate reorganization.
"Sec. 4070. Enforcement authority relating to terminations of single-employer plans.".

Section 11017.—Studies

(a) *Single-Employer Pension Plan Termination Insurance Premium Study.*—

(1) *In general.*—As soon as practicable after the date of the enactment of this Act, the Pension Benefit Guaranty Corporation shall conduct a study of the premiums established under the single-employer pension plan termination insurance program under title IV of the Employee Retirement Income Security Act of 1974.

(2) *Matters to be studied.*—The Corporation shall specifically consider in its study the following matters:

(A) the effect of the amendments made by this title on the long-term stability of the single-employer pension plan termination insurance program under title IV of the Employee Retirement Income Security Act of 1974,

(B) alternatives to the current statutory mechanism with respect to proposals for changes in the premium levels under such program,

(C) the methods currently used by the Corporation in projecting future program costs of the single-employer pension plan termination insurance program,

(D) alternative methods of projecting such future program costs and an evaluation of each such alternative method,

(E) the methods currently used by the Corporation in determining premiums needed to allocate and adequately fund such future program costs,

(F) alternative methods of making such premium determinations and an evaluation of each such alternative method, and

(G) alternative premium bases upon which some or all of such projected future program costs would be allocated on an exposure-related or risk-related computation, which may take into account the different exposures or risks imposed on the Corporation by plan sponsors with different histories and under different circumstances.

(3) *Submission of corporation's report.*—Not later than one year after the date of the enactment of this Act, the Corporation shall report the results of its study, together with any recommendations for statutory changes, to an advisory council, to be appointed by the chairmen of the Committee on Education and Labor and the Committee on Ways and Means of the House of Representatives and the Committee on Labor and Human Resources and the Committee on Finance of the Senate. The advisory council shall be composed of representatives of single-employer plan sponsors, employee organizations representing single-employer plan participants, and members of the general public who are experts in the matters to be considered in the study. The members of the advisory council shall serve without compensation.

(4) *Submission of council's report to congress.*—Not later than 180 days after the date of the submission of the Corporation's report to the advisory council under paragraph (3), the advisory council shall submit the results of the Corporation's study and the Corporation's recommendations, together with the recommendations of the council, to the Speaker of the House of Representatives and the President pro tempore of the Senate.

(5) *Cooperation by the pension benefit guaranty corporation and other federal agencies.*—The Corporation shall cooperate with the advisory council in reviewing the results of the Corporation's study and recommendations. In order to avoid unnecessary expense and duplication, to the extent not otherwise prohibited by law, the Corporation and any other Federal agency shall provide to the advisory council any data, analyses, or other relevant information related to the matters under review.

(b) *Overfunded Pension Plan Study.*—

(1) *In general.*—As soon as practicable after the date of enactment of this Act, the Secretary of Labor shall conduct a study of terminations resulting in residual assets under section 4044(d) of the Employee Retirement Income Security Act of 1974.

(2) *Report.*—No later than May 1, 1986, the Secretary of Labor shall submit a report on the study conducted under paragraph (1), together with any recommendations for statutory changes, to the chairmen of the Committee on Education and Labor and the Committee on Ways and Means of the House of Representatives and the Committee on Labor and Human Resources and the Committee on Finance of the Senate.

Section 11018.—Limitation on Regulations

(a) *Regulatory Treatment of Assets of Real Estate Entities.*—

(1) *In general.*—Except as a defense, no rule or regulation adopted pursuant to the Secretary's proposed regulation defining "plan assets" for purposes of the Employee Retirement Income Security Act of 1974 (50 Fed. Reg. 961, January 8, 1985, as modified by 50 Fed. Reg. 6361, February 15, 1985), or any reproposal thereof prior to the adoption of the regulations required to be issued in accordance with subsection (d), shall apply to an asset of a real estate entity in which a plan, account, or arrangement subject to such Act invests if—

(A) any interest in the entity is first offered to a plan, account, or arrangement subject to such Act investing in the entity (hereinafter in this section referred to as a "plan investor") on or before the date which is 120 days after the date of publication of such rule or regulation as a final rule or regulation;

(B) no plan investor acquires an interest in the entity from an issuer or underwriter at any time on or after the date which is 270 days after the date of publication of such rule or regulation as a final rule or regulation (except pursuant to a contract or subscription binding on the plan investor and entered into, or tendered, before the expiration of such 270-day period, or pursuant to the exercise, on or before December 31, 1990, of a warrant which was the subject of an effective registration under the Securities Act of 1933 (15 U.S.C. 77q et seq.) prior to the date of the enactment of this section); and

(C) every interest in the entity acquired by a plan investor (or contracted for or subscribed to by a plan investor) before the expiration of such 270-day period is a security—

(i) which is part of an issue or class of securities which upon such acquisition or at any time during the offering period is held by 100 or more persons;

(ii) the economic rights of ownership in respect of which are freely transferable;

(iii) which is registered under the Securities Act of 1933; and

(iv) which is part of an issue or class of securities which is registered under the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) (or is so registered within three years of the effective date of the registration statement of such securities for purposes of the Securities Act of 1933: *Provided,* That the issuer provides plan investors with such reports with respect to such period by the Securities and Exchange Commission under such Acts and the rules and regulations promulgated thereunder).

In the case of partnerships organized prior to enactment of this section, the requirements of subparagraphs (iii) and (iv) shall not apply to initial limited partnership interests in an entity otherwise described above: *Provided,* That such entity was the subject of an effective registration under the Securities Act of 1933 prior to the date of the enactment of this section, such interests were issued solely for partnership organizational purposes in compliance with State limited partnership laws, and such interest has a value as of the date of issue of less than $20,000 and represents less than one percent of the total interests outstanding as of the completion of the offering period.

(2) *Maintenance of current regulatory treatment.*—No asset of any real estate

entity described in paragraph (1) shall be treated as an asset of any plan investor for any purpose of the Employee Retirement Income Security Act of 1974 if the assets of such entity would not have been assets of such plan investor under the provisions of—

(A) Interpretive Bulletin 75-2 (29 CFR 2509 750-2); or

(B) the regulations proposed by the Secretary of Labor and published—

(i) on August 28,1979, at 44 Fed. Reg. 50363;

(ii) on June 6, 1980, at 45 Fed. Reg. 38084;

(iii) on January 8, 1985, at 50 Fed. Reg. 961; or

(iv) on February 15, 1985, at 50 Fed. Reg. 6361, without regard to any limitation of any effective date proposed therein.

(b) *Definitions and Special Rules.*—For purposes of this section—

(1) The term "real estate entity" means an entity which, at any time within two years after the closing of its offering period has invested or has contracted to invest at least 75 percent of the value of its net assets available for investment in direct or indirect ownership of "real estate assets" or "interests in real property".

(2) The term "real estate asset" means real property (including an interest in real property) and any share of stock or beneficial interest, partnership interest, depository receipt, or any other interest in any other real estate entity.

(3) The term "interest in real property" includes, directly or indirectly, the following:

(A) the ownership or co-ownership of land or improvements thereon;

(B) any mortgage (including an interest in or co-ownership of any mortgage, leasehold mortgage, pool of mortgages, deed of trust, or similar instrument) on land or improvements thereon,

(C) any leasehold of land or improvements thereon; and

(D) any option to acquire any of the foregoing, but does not include any mineral, oil, or gas royalty interest.

(4) Whether the economic rights of ownership with respect to a security are "freely transferable" shall be determined based upon all the facts and circumstances, but ordinarily none of the following, alone or in any combination, shall cause the economic rights of ownership to be considered not freely transferable—

(A) any requirement that not less than a minimum number of shares or units of such security be transferred or assigned by any investor: *Provided,* That such requirement does not prevent transfer of all of the then remaining shares or units held by an investor;

(B) any prohibition against transfer or assignment of such security or rights in respect thereof to an ineligible or unsuitable investor;

(C) any restriction on or prohibition against any transfer or assignment which would either result in a termination or reclassification of the entity for Federal or State tax purposes or which would violate any State or Federal statute, regulation, court order, judicial decree, or rule of law;

(D) any requirement that reasonable transfer or administrative fees be paid in connection with a transfer or assignment;

(E) any requirement that advance notice of a transfer or assignment be given to the entity and any requirement regarding execution of documentation evidencing such transfer or assignment (including documentation setting forth representations from either or both of the transferor or transferee as to compliance with any restriction or requirement described in this section or requiring compliance with the entity's governing instruments);

(F) any restriction on substitution of an assignee as a limited partner of a partnership, incuding a general partner consent requirement: *Provided,* That the economic benefits of ownership of the assignor may be transferred or assigned without regard to such restriction or consent (other than compliance with any other restriction described in this section);

(G) any administrative procedure which establishes an effective date, or an event such as the completion of the offering, prior to which a transfer or assignment will not be effective; and

(H) any limitation or restriction on transfer or assignment which is not created or imposed by the issuer or any person acting for or on behalf of such issuer.

(c) *No Effect on Secretary's Authority Other Than As Provided.*—Except as provided in subsection (a), nothing in this section shall limit the authority of the Secretary of Labor to issue regulations or otherwise interpret section 3(21) of the Employee Retirement Income Security Act of 1974.

(d) *Time Limit for Final Regulations.*—The Secretary of Labor shall adopt final regulations defining "plan assets" by December 31, 1986.

Section 11019.—Effective Date of Title; Temporary Procedures

(a) *In General.*—Except as otherwise provided in this title, the amendments made by this title shall be effective as of January 1, 1986, except that such amendments shall not apply with respect to terminations for which—

(1) notices of intent to terminate were filed with the Pension Benefit Guaranty Corporation under section 4041 of the Employee Retirement Income Security Act of 1974 before such date, or

(2) proceedings were commenced under section 4042 of such Act before such date.

(b) *Transitional Rules.*—

(1) *In general.*—In the case of a single-employer plan termination for which a notice of intent to terminate was filed with the Pension Benefit Guaranty Corporation under section 4041 of the Employee Retirement Security Act of 1974 (as in effect before the amendments made by this title) on or after January 1, 1986, but before the date of the enactment of this Act, the amendments made by this title shall apply with respect to such termination, as modified by paragraphs (2) and (3).

(2) *Deemed compliance with notice requirements.*—The requirements of subsections (a)(2), (b)(1)(A), and (c)(1)(A) of section 4041 of the Employee Retirement Income Security Act of 1974 (as amended by this title) shall be considered to have been met with respect to a termination described in paragraph (1) if—

(A) the plan administrator provided notice to the participants in the plan regarding the termination in compliance with applicable regulations of the Pension Benefit Guaranty Corporation as in effect on the date of the notice, and

(B) the notice of intent to terminate provided to the Pension Benefit Guaranty Corporation in connection with the termination was filed with the Corporation not less than 10 days before the proposed date of termination specified in the notice.

For purposes of section 4041 of such Act (as amended by this title), the proposed date of termination specified in the notice of intent to terminate referred to in subparagraph (B) shall be considered the proposed termination date.

(3) *Special termination procedures.*—

(A) *In general.*—This paragraph shall apply with respect to any termination described in paragraph (1) if, within 90 days after the date of enactment of this Act, the plan administrator notifies the Corporation in writing—

(i) that the plan administrator wishes the termination to proceed as a standard termination under section 4041(b) of the Employee Retirement Income Security Act of 1974 (as amended by this title) in accordance with subparagraph (B),

(ii) that the plan administrator wishes the termination to proceed as a distress termination under section 4041(c) of such Act (as amended by this title) in accordance with subparagraph (C), or

(iii) that the plan administrator wishes to stop the termination proceedings in accordance with subparagraph (D).

(B) *Terminations proceeding as standard termination.*—

(i) *Terminations for which sufficiency notices have not been issued.*—

(I) *In general.*—In the case of a plan termination described in paragraph (1) with respect to which the Corporation has been provided the notification described in subparagraph (A)(i) and with respect to which a notice of sufficiency has not been issued by the Corporation before the date of the enactment of this Act, if during the 90-day period commencing on the date of the notice required in subclause (II), all benefit commitments under the plan have been satisfied, the termination shall be treated as a standard termination under section 4041(b) of such Act (as amended by this title).

(II) *Special notice regarding sufficiency for terminations for which notices of sufficiency have not been issued as of date of enactment.*—

In the case of a plan termination described in paragraph (1) with respect to which the Corporation has been provided the notification described in subparagraph (A)(i) and with respect to which a notice of sufficiency has not been issued by the Corporation before the date of the enactment of this Act, the Corporation shall make the determinations described in section 4041(c)(3)(A) (i) and (ii) (as amended by this title) and notify the plan administrator of such determinations as provided in section 4041(c)(3)(A)(iii) (as amended by this title).

(ii) *Terminations for which notices of sufficiency have been issued.*—In the case of a plan termination described in paragraph (1) with respect to which the Corporation has been provided the notification described in subparagraph (A)(i) and with respect to which a notice of sufficiency has been issued by the Corporation before the date of the enactment of this Act, clause (i)(I) shall apply, except that the 90-day period referred to in clause (i)(I) shall begin on the date of the enactment of this Act.

(C) *Terminations proceeding as distress termination.*—In the case of a plan termination described in paragraph (1) with respect to which the Corporation has been provided the notification described in subparagraph (A)(ii), if the requirements of section 4041(c)(2)(B) of such Act (as amended by this title) are met, the termination shall be treated as a distress termination under section 4041(c) of such Act (as amended by this title).

(D) *Termination of proceedings by plan administrator.*—

(i) *In general.*— Except as provided in clause (ii), in the case of a plan termination described in paragraph (1) with respect to which the Corporation has been provided the notification described in subparagraph (A)(iii), the termination shall not take effect.

(ii) *Terminations with respect to which final distribution of assets has commenced.*— Clause (i) shall not apply with respect to a termination with respect to which the final distribution of assets has commenced before the date of the enactment of this Act unless, within 90 days after the date of the enactment of this Act, the plan has been restored in accordance with procedures issued by the Corporation pursuant to subsection (c).

(E) *Authority of corporation to extend 90-day periods to permit standard termination.*—The Corporation may, on a case-by-case basis in accordance with subsection (c), provide for extensions of the applicable 90-day period referred to in clause (i) or (ii) of subparagraph (B) if it is demonstrated to the satisfaction of the Corporation that—

(i) the plan could not otherwise, pursuant to the preceding provisions of this paragraph, terminate in a termination treated as a standard termination under section 4041(b) of the Employee Retirement Income Security Act of 1974 (as amended by this title), and

(ii) the extension would result in a greater likelihood that benefit commitments under the plan would be paid in full, except that any such period may not be so extended beyond one year after the date of the enactment of this Act.

(c) *Authority to Prescribe Temporary Procedures.*—The Pension Benefit Guaranty Corporation may prescribe temporary procedures for purposes of carrying out the amendments made by this title during the 180-day period beginning on the date described in subsection (a).

TITLE XII—INCOME SECURITY AND RELATED PROGRAMS

Subtitle A—Old-Age, Survivors, and Disability Insurance Program

* * * * *

Section 12110.—State Coverage Agreements

(a) *Maximum Period of Retroactive Coverage.*—Section 218(f)(1) of the Social Security Act is amended by striking out "is agreed to by the Secretary and the State" and inserting in lieu thereof "is mailed or delivered by other means to the Secretary".

(b) *Positions Compensated Solely on Fee Basis.*—Section 218(u)(3) of such Act is amended by striking out "is agreed to by the Secretary and the State" and inserting in lieu thereof "is mailed or delivered by other means to the Secretary".

(c) *Effective Date.*—The amendments made by this section shall apply with respect to agreements and modifications of agreements which are mailed or delivered to the Secretary of Health and Human Services (under section 218 of the Social Security Act) on or after the date of the enactment of this Act.

Section 12111—Effect of Early Delivery of Benefit Checks

(a) *For OASDI Purposes.*—Section 708 of the Social Security Act is amended by adding at the end thereof the following new subsection:

"(c) For purposes of computing the 'OASDI trust fund ratio' under section 201(l), the 'OASDI' fund ratio' under section 215(i), and the 'balance ratio' under section 709(b), benefit checks delivered before the end of the month for which they are issued by reason of subsection (a) of this section shall be deemed to have been delivered on the regularly designated delivery date."

(b) *For Income Tax Purposes.*—Section 86(d) of the Internal Revenue Code of 1954 (relating to taxation of social security and tier 1 railroad retirement benefits) is amended by adding at the end thereof the following new paragraph:

"(5) *Effect of Early Delivery of Benefit Checks.*—For purposes of subsection (a), in any case where section 708 of the Social Security Act causes social security benefit checks to be delivered before the end of

the calendar month for which they are issued, the benefits involved shall be deemed to have been received in the succeeding calendar month.".

(c) *Effective Date.*—The amendments made by this section shall apply with respect to benefit checks issued for months ending after the date of the enactment of this Act.

Section 12112. Exempt from Social Security Coverage for Retired Federal Judges on Active Duty

(a) *Amendment to Social Security Act.*—Section 209 of the Social Security Act is amended in the third to the last paragraph thereof (added by section 101(c)(1) of the Social Security Amendments of 1983) by striking out "shall, subject to the provisions of subsection (a) of this section, include" and inserting in lieu thereof "shall not include".

(b) *Amendment to Internal Revenue Code.*—Section 3121(i)(5) of the Internal Revenue Code of 1954 is amended by striking out "shall, subject to the provisions of subsection (a)(1) of this section, include" and inserting in lieu thereof "shall not include".

(c) *Effective Date.*—The amendments made by this section shall be effective with respect to service performed after December 31, 1983.

Section 12113. Recovery of Overpayments

(a) *OASDI Payments.*—Section 204(a) of the Social Security Act is amended—

(1) by inserting "(1)" after "204(a)";

(2) by redesignating paragraph (1) and (2) as subparagraphs (A) and (B); and

(3) by adding at the end thereof the following new paragraph:

"(2) Notwithstanding any other provision of this section, when any payment of more than the correct amount is made to or on behalf of an individual who has died, and such payment—

"(A) is made by direct deposit to a financial institution;

"(B) is credited by the financial institution to a joint account of the deceased individual and another person; and

"(C) such other person was entitled to a monthly benefit on the basis of the same wages and self-employment income as the deceased individual for the month preceding the month in which the deceased individual died,

the amount of such payment in excess of the correct amount shall be treated as a payment of more than the correct amount to such other person.".

(b) *SSI Payments.*—Section 1631(b) of the Social Security Act is amended by redesignating paragraphs (2) through (4) as paragraphs (3) through (5), and by inserting after paragraph (1) the following new paragraph:

"(2) Notwithstanding any other provision of this section, when any payment of more than the correct amount is made to or on behalf of an individual who has died, and such payment—

"(A) is made by direct deposit to a financial institution;

"(B) is credited by the financial institution to a joint account of the deceased individual and another person; and

"(C) such other person is the surviving spouse of the deceased individual, and was eligible for a payment under this title (including any State supplementation payment paid by the Secretary) as an eligible spouse (or as either member of an eligible couple) for the month in which the deceased individual died,

the amount of such payment in excess of the correct amount shall be treated as a payment of more than the correct amount to such other person.".

(c) *Effective Date.*—The amendments made by this section shall apply only in the case of deaths of which the Secretary is first notified on or after the date of the enactment of this Act.

Section 12114. Coverage of Connecticut State Police

Notwithstanding any provision of section 218 of the Social Security Act, the Secretary of Health and Human Services shall, upon the request of the Governor of Connecticut, modify the agreement under such section between the Secretary and the State of Connecticut to provide that service performed after the date of the enactment of this Act by members of the Division of the State Police within the Connecticut Department of Public Safety, who are hired on or after May 8, 1984, and who are members of the tier II plan of the Connecticut State Employees Retirement System, shall be covered under such agreement.

Section 12115. General Effective Date of Subtitle

Except as otherwise specifically provided, the preceding provisions of this subtitle, including the amendments made thereby, shall take effect on the first day of the month following the month in which this Act is enacted.

* * * * *

Subtitle D—Provisions Relating to Unemployment Compensation

Section 12401. Recovery of Unemployment Benefit Overpayments

(a) *In General.*—(1) Section 303(a)(5) of the Social Security Act is amended by inserting before "; and" at the end thereof the following: "; *Provided further,* That amounts may be deducted from unemployment benefits and used to repay overpayments as provided in subsection (g)".

(2) Section 303 of such Act is amended by adding at the end thereof the following new subsection:

"(g)(1) A State may deduct from unemployment benefits otherwise payable to an individual an amount equal to any overpayment made to such individual under an unemployment benefit program of the United States or of any other State, and not previously recovered. The amount so deducted shall be paid to the jurisdiction under whose program such overpayment was made. Any such deduction shall be made only in accordance with the same procedures relating to notice and opportunity for a hearing as apply to the recovery of overpayments of regular unemployment compensation paid by such State.

"(2) Any State may enter into an agreement with the Secretary of Labor under which—

"(A) the State agrees to recover from unemployment benefits otherwise payable to an individual by such State any overpayments made under an unemployment benefit program of the United States to such individual and not previously recovered, in accordance with paragraph (1), and to pay such amounts recovered to the United States for credit to the appropriate account, and

"(B) the United States agrees to allow the State to recover from unemployment benefits otherwise payable to an individual under an unemployment benefit program of the United States any overpayments made by such State to such individual under a State unemployment benefit program and not previously recovered, in accordance with the same procedures as apply under paragraph (1).

"(3) For purposes of this subsection, 'unemployment benefits' means unemployment compensation, trade adjustment allowances, and other unemployment assistance.".

(b) *Conforming Amendments.*—(1) Section 3304(a)(4) of the Internal Revenue Code of 1954 is amended—

(A) by striking out "and" at the end of subparagraph (B);

(B) by adding "and" at the end of subparagraph (C); and

(C) by adding at the end thereof the following new subparagraph:

"(D) amounts may be deducted from unemployment benefits and used to repay overpayments as provided in section 303(g) of the Social Security Act;".

(2) Section 3306(f) of such Code is amended—

(A) by striking out "and" at the end of paragraph (1);

(B) by striking out the period at the end of paragraph (2) and inserting in lieu thereof ",and"; and

(C) by adding at the end thereof the following new paragraph:

"(3) amounts may be deducted from unemployment benefits and used to repay overpayments as provided in section 303(g) of the Social Security Act.".

(c) *Effective Date.*—The amendements made by this section shall apply to recoveries made on or after the date of the enactment of this Act and shall apply with respect to overpayments made before, on, or after such date.

Section 12402. Supplement Unemployment Compensation for Certain Individuals

(a) *In General.*—If—

(1) an individual was receiving Federal supplemental compensation for the week which includes March 31, 1985, or a series of consecutive weeks which began with such week, and

(2) such individual did not meet the consecutive-week eligibility requirements of the Federal Supplemental Compensation Act of 1982 during any period of 1 or more subsequent weeks by reason of performing temporary disaster services described in subsection (e),

weeks in such period, shall be disregarded for purpose of the consective-week requirement of section 602(f)(2)(B) of such Act, and, notwithstanding the requirements of State law relating to the availability for work, the active search for work, or the refusal to accept work, such individual shall be entitled to payment of Federal supplement compensation for each week of unemployment which is described in subsection (b) and for which a certification of unemployment is made by such individual in accordance with subsection (c).

(b) *Weeks for Which Payment Shall Be Made.*—A week of unemployment for which payment shall be made under subsection (a) is a week which occurred during the period which commences with the first week beginning after the close of the period described in subsection (a)(2) and ends with the beginning of the first week in which the individual was employed after the close of such period.

(c) *Certification.*—The certification of unemployment referred to in subsection (a) shall be a certification—

(1) that is made on a form provided by the State agency concerned and signed by the individual; and

(2) that identifies the weeks of unemployment for which the individual is making the certification.

(d) *Limitation on Amount of Payment.*—In no case may the total amount paid to an individual under subsection (a) exceed the amount remaining in the account established for such individual undersection 602(e) of the Federal Supplemental Compensation Act of 1982 after payments were made from such account for weeks of unemployment beginning before the period described in subsection (a)(2).

(e) *Definition.*—For purposes of subsection (a), the term "temporary disaster services" means services performed as a member of the National Guard after being called up by the Governor of a State to perform services related to a major disaster that was declared on June 3, 1985, by the President of the United States under the Disaster Relief Act of 1974.

(f) *Modification of Agreement.*—(1) The Secretary of Labor shall, at the earliest possible date after the date of the enactment of this Act, propose to any state concerned a modification of the agreement that the Secretary has with such State under section 602 of the Federal Supplemental Compensation Act of 1982 in order to carry out this section.

(2) Pending modification of the agreement, the State may make payment in accordance with the provisions of this section and shall be reimbursed in accordance with the provisions of section 604(a) of the Federal Supplemental Compensation Act of 1982. For purposes of carrying out this paragraph, the term "this subtitle" in such section 604(a) shall include this section.

(g) *Effective Date.*—The provisions of this section shall apply to weeks beginning after March 31, 1985.

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TITLE XIII—REVENUES, TARDE, AND RELATED PROGRAMS

* * * * *

Subtitle B—General Revenue Provisions

Section 13200.—Amendment of 1954 Code

Except as otherwise expressly provided, whenever in this subtitle an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1954.

Section 13201.—Increase in Tax on Cigarettes Made Permanent

(a) Subsection (c) of section 283 of the Tax Equity and Fiscal Responsibility Act of 1982 (relating to increase in tax on cigarettes) is amended by striking out all that follows "December 31, 1982" and inserting in lieu thereof a period.

(b) For purposes of all Federal and State laws, the amendment made by subsection (a) shall be treated as having taken effect on March 14, 1986.

Section 13202.—Tax on Smokeless Tobacco

(a) *In General.*—Section 5701 (relating to rate of tax) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

"(e) *Smokeless Tobacco.*—On smokeless tobacco, manufactured in or imported into the United States, there shall be imposed the following taxes:

"(1) *Snuff.*—On snuff, 24 cents per pound and a proportionate tax at the like rate on all fractional parts of a pound.

"(2) *Chewing tobacco.*—On chewing tobacco, 8 cents per pound and a proportionate tax at the like rate on all fractional parts of a pound.".

(b) *Conforming Amendments.*—

(1) The heading of chapter 52 is amended by inserting "SMOKELESS TOBACCO," after "CIGARETTES,".

(2) Section 5702(c) (defining tobacco products) is amended by striking out "and cigarettes" and inserting in lieu thereof ", cigarettes, and smokeless tobacco".

(3) Section 5702(d) (defining manufacturers of tobacco products) is amended by striking out "cigars or cigarettes" each place it appears and inserting in lieu thereof

"cigars, cigarettes, or smokeless tobacco".

(4) Section 5702 is amended by adding at the end thereof the following new subsection:

"(r) *Definitions Relating to Smokeless Tobacco.*—

"(1) *Smokeless tobacco.*—The term 'smokeless tobacco' means any snuff or chewing tobacco.

"(2) *Snuff.*—The term 'snuff' means any means any finely cut, ground, or powdered tobacco that is not intended to be smoked.

"(3) *Chewing tobacco.*—The term 'chewing tobacco' means any leaf tobacco that is not intended to be smoked.".

(c) *Effective Date.*—

(1) *In general.*—The amendments made by this section shall apply to smokeless tobacco removed after June 30,1986.

(2) *Transitional rule.*—Any person who—

(A) on the date of the enactment of this Act, is engaged in business as a manufacturer of smokeless tobacco, and

(B) before July 1, 1986, submits an application under subchapter B of chapter 52 of the Internal Revenue Code of 1954 to engage in such business, may, notwithstanding such subchapter B, continue to engage in such business pending final action on such application. Pending such final action, all provisions of chapter 52 of such Code shall apply to such applicant in the same manner and to the same extent as if such applicant were a holder of a permit to manufacture smokeless tobacco under such chapter 52.

Section 13203.—Increase in Excise Tax on Coal

(a) *Increase in Tax.*—Subsections (a) and (b) of section 4121 (relating to imposition of tax on coal) are amended to read as follows:

"(a) *Tax Imposed.*—

"(1) *In general.*—There is hereby imposed on coal from mines located in the United States sold by the producer, a tax equal to the rate per ton determined under subsection (b).

"(2) *Limitation on tax.*—The amount of the tax imposed by paragraph (1) with respect to a ton of coal shall not exceed the applicable percentage (determined under subsection (b)) of the price at which such ton of coal is sold by the producer.

"(b) *Determination of Rates and Limitation on Tax.*—For purposes of subsection (a), in the case of sales during any calendar year beginning after December 31, 1985—

"(1) the rate of tax on coal from underground mines shall be $1.10,

"(2) the rate of tax on coal from surface mines shall be $.55, and

"(3) the applicable percentage shall be 4.4 percent.".

(b) *5-year Moratorium on Interest Accruals With Respect to the Indebtedness of the Black Lung Disability Trust Fund.*—No interest shall accrue for the period beginning on October 1, 1985, and ending on September 30, 1990, with respect to any repayable advance to the Black Lung Disability Trust Fund.

(c) *Existing Reduction in Rates for Period After Temporary Increase Retained.*—So much of subsection (e) of section 4121 (relating to temporary increase in amount of tax) as precedes paragraph (2) is amended to read as follows:

"(e) *Reduction in Amount of Tax.*—

"(1) *In general.*—Effective with respect to sales after the temporary increase termination date, subsection (b) shall be applied—

"(A) by substituting '$.50' for '$1.10,'

"(B) by substituting '$.25' for '$.55,' and

"(C) by substituting '2 percent' for '4.4 percent'.".

(d) *Effective Date.*—The amendments made by this section shall apply to sales after March 31, 1986.

Section 13204.—Only Railroad Retirement Benefits Equivalent to Social Security Benefits Treated as Tier 1 Benefits.

(a) *In General.*—Paragraph (4) of section 86(d) (defining Social security benefits) is amended to read as follows:

"(4) *Tier 1 railroad retirement benefit.*—For purposes of paragraph (1), the term 'tier 1 railroad retirement benefit' means—

"(A) the amount of the annuity under the Railroad Retirement Act of 1974 equal to the amount of the benefit to which the taxpayer would have been entitled under the Social Security Act if all of the service after December 31, 1936, of the employee (on whose employment record the annuity is being paid) had been included in the term 'employment' as defined in the Social Security Act, and

"(B) a monthly annuity amount under section 3(f)(3) of the Railroad Retirement Act of 1974.".

(b) *Effective Date.*—The amendment made by subsection (a) shall apply to any monthly benefit for which the generally applicable payment date is after December 31, 1985.

Section 13205.—Medicare Coverage of, and Application of Hospital Insurance Tax to, Newly Hired State and Local Government Employees

(a) *Application of Hospital Insurance Tax to Newly Hired Employees of State and Local Governments.*—

(1) *In general.*—Subsection (u) of section 3121 (relating to application of hospital insurance tax to Federal employment) is amended to read as follows:

"(u) *Application of Hospital Insurance Tax to Federal, State, and Local Employment.*—

"(1) *Federal employment.*—For purposes of the taxes imposed by sections 3101(b) and 3111(b), subsection (b) shall be applied without regard to paragraph (5) thereof.

"(2) *State and local employment.*—For purposes of the taxes imposed by sections 3101(b) and 3111(b)—

"(A) *In general.*—Except as provided in subparagraphs (B) and (C), subsection (b) shall be applied without regard to paragraph (7) thereof.

"(B) *Exception for certain services.*—Service shall not be treated as employment by reason of subparagraph (A) if—

"(i) the service is included under an agreement under section 218 of the Social Security Act, or

"(ii) the service is performed—

"(I) by an individual who is employed by a State or political subdivision thereof to relieve him from unemployment,

"(II) in a hospital, home, or other institution by a patient or inmate thereof as an employee of a State or political subdivision thereof or of the District of Columbia,

"(III) by an individual, as an employee of a State or political subdivision thereof or of the District of Columbia, serving on a temporary basis in case of fire, storm, snow, earthquake, flood or other similar emergency, or

"(IV) by any individual as an employee included under section 5351(2) of title 5, United States Code (relating to certain interns, student nurses, and other student employees of hospitals of the District of Columbia Government), other than as a medical or dental intern or a medical or dental resident in training.

As used in this subparagraph, the terms 'State' and 'political subdivision' have the meanings given those terms in section 218(b) of the Social Security Act.

"(C) *Exception for current employment which continues.*—Service performed for an employer shall not be treated as employment by reason of subparagraph (A) if—

"(i) such service would be excluded from the term 'employment' for purposes of this chapter if subparagraph (A) did not apply;

"(ii) such service is performed by an individual—

"(I) who was performing substantial and regular service for remuneration for that employer before April 1, 1986,

"(II) who is a bona fide employee of that employer on March 31, 1986, and

"(III) whose employment relationship with that employer was not entered into for purposes of meeting the requirements of this subparagraph; and

"(iii) the employment relationship with that employer has not been terminated after March 31, 1986.

"(D) *Treatment of agencies and instrumentalities.*—

For purposes of subparagraph (C), under regulations—

"(i) All agencies and instrumentalities of a State (as defined in section 218(b) of the Social Security Act) or of the District of Columbia shall be treated as a single employer.

"(ii) All agencies and instrumentalities of a political subdivision of a State (as so defined) shall be treated as a single employer and shall not be treated as described in clause (i).

"(3) *Medicare qualified government employment.*—For purposes of this chapter, the term 'medicare qualified government employment' means service which—

"(A) is employment (as defined in subsection (b)) with the application of paragraphs (1) and (2), but

"(B) would not be employment (as so defined) without the application of such paragraphs."

(2) *Conforming amendments.*—

(A)(i) Section 3125 (relating to returns in the case of governmental employees in Guam, American Samoa, and the District of Columbia) is amended by redesignated subsections (a), (b), and (c) as subsections (b), (c), and (d), respectively, and by inserting before subsection (b) (as so redesignated) the following new subsection:

"(a) *States.*—Except as otherwise provided in this section, in the case of the taxes imposed by sections 3101(b) and 3111(b) with respect to service performed in the employ of a State or any political subdivision thereof (or any instrumentality of any one or more of the foregoing which is wholly owned thereby), the return and payment of such taxes may be made by the head of the agency or instrumentality having the control of such service, or by such agents as such head may designate. The person making such return may, for convenience of administration, make payments of the tax imposed under section 3111 with respect to the service of such individuals without regard to the contribution and benefit base limitation in section 3121(a)(1)."

(ii) The section heading for such section 3125 is amended by inserting "STATES," before "GUAM".

(iii) The item relating to section 3125 in the table of sections for subchapter C of chapter 21 is amended by inserting "States," before "Guam".

(B) Subsection (b) of section 1402 is amended by striking out "medicare qualified Federal employment (as defined in section 3121(u)(2))" and inserting in lieu thereof "medicare qualified government employment (as defined in section 3121 (u)(3))".

(C) Section 3122 (relating to Federal service) is amended by striking out "including service which is medicare qualified Federal employment (as defined in section 3121(u)(2))" and inserting in lieu thereof "including such service which is medicare qualified government employment (as defined in section 3121(u)(3))".

(D) Subsection (a) of section 6205 (relating to special rules applicable to certain employment taxes) is amended by adding at the end thereof the following new paragraph:

"(5) *States and political subdivisions as employer.*—For purposes of this subsection, in the case of remuneration received from a State or any political subdivision thereof (or any instrumentality of any one or more of the foregoing which is wholly owned thereby) during any calendar year, each head of an agency or instrumentality, and each agent designated by either, who makes a return pursuant to section 3125 shall be deemed a separate employer."

(E)(i) Section 6413(a) (relating to adjustment of certain employment taxes) is amended by adding at the end thereof the following new paragraph:

"(5) *States and political subdivisions as employer.*—For purposes of this subsection, in the case of remuneration received from a State or any political subdivision thereof (or any instrumentality of any one or more of the foregoing which is wholly owned thereby) during any calendar year, each head of an agency or instrumentality, and each agent designated by either, who makes a return pursuant to section 3125 shall be deemed a separate employer."

(ii) Section 6413(c)(2) (relating to special refunds of certain employment taxes) is amended—

(I) by striking out "3125(a)", "3125(b)", and "3125(c)" in subparagraphs (D), (E), and (F), respectively, and inserting in lieu thereof "3125(b)", "3125(c)", and "3125(d)", respectively, and

(II) by adding at the end thereof the following new subparagraph:

"(G) *Employees of states and political subdivisions.*—In the case of remuneration received from a State or any political subdivision thereof (or any instrumentality of any one or more of the foregoing which is wholly owned thereby) during any calendar year, each head of an agency or instrumentality, and each agent designated by either, who makes a return pursuant to section 3125(a) shall, for purposes of this subsection, be deemed a separate employer."

(b) *Entitlement to Hospital Insurance Benefits.*—

(1) *Revision of definition of medicare qualified government employment.*—Section 210(p)) of the Social Security Act (42 U.S.C. 410(p)) is amended to read as follows:

"*Medicare Qualified Government Employment*

"(p)(1) For purposes of sections 226 and 226A, the term 'medicare qualified government employment' means any service which would constitute 'employment' as defined in subsection (a) of this section but for the application of the provisions of—

"(A) subsection (a)(5), or

"(B) subsection (a)(7), except as provided in paragraphs (2) and (3).

"(2) Service shall not be treated as employment by reason of paragraph (1)(B) if the service is performed—

"(A) by an individual who is employed by a State or political subdivision thereof to relieve him from unemployment,

"(B) in a hospital, home, or other institution by a patient or inmate thereof as an employee of a State or political subdivision thereof or of the District of Columbia,

"(C) by an individual, as an employee of a State or political subdivision thereof or of the District of Columbia, serving on a temporary basis in case of fire, storm, snow, earthquake, flood or other similar emergency, or

"(D) by any individual as an employee included under section 5351(2) of title 5, United States Code (relating to certain interns, student nurses, and other student employees of hospitals of the District of Columbia Government), other than as a medical or dental intern or a medical or dental resident in training.

As used in this paragraph, the terms 'State' and 'political subdivision' have the meanings given those terms in section 218(b).

"(3) Service performed for an employer shall not be treated as employment by reason of paragraph (1)(B) if—

"(A) such service would be excluded from the term 'employment' for purposes of this section if paragraph (1)(B) did not apply;

"(B) such service is performed by an individual—

"(i) who was performing substantial and regular service for remuneration for that employer before April 1, 1986,

"(ii) who is a bona fide employee of that employer on March 31, 1986, and

"(iii) whose employment relationship with that employer was not entered into for purposes of meeting the requirements of this subparagraph; and

"(C) the employment relationship with that employer has not been terminated after March 31, 1986.

"(4) For purposes of paragraph (3), under regulations (consistent with regulations established under section 3121(u)(2)(D) of the Internal Revenue Code of 1954)—

"(A) all agencies and instrumentalities of a State (as defined in section 218(b)) or of the District of Columbia shall be treated as a single employer, and

"(B) all agencies and instrumentalities of a political subdivision of a State (as so defined) shall be treated as a single employer and shall not be treated as described in subparagraph "(A)."

(2) *Entitlement to hospital insurance benefits.*—

(A) *For individuals age 65 or older and for disabled individuals.*—Section 226 of such Act (42 U.S.C. 426) is amended by striking out "medicare qualified Federal employment' in subsections (a)(2)(C)(i) and (b)(2)(C)(ii)(I) and inserting in lieu thereof "medicare qualified government employment".

(B) *For individuals with end-stage renal disease.*—Section 226A(a) of such Act (42 U.S.C. 426-1(a)) is amended by striking out "medicare qualified Federal employment" in paragraphs (1)(A)(ii) and (1)(B)(iii) and inserting in lieu thereof "medicare qualified government employment".

(C) *Conforming amendments.*—

(i) Section 1811 of such Act (42 U.S.C. 1395c) is amended by striking out "Federal employment" in clauses (1) and (2) and inserting in lieu thereof "government employment".

(ii) Section 226(g) of such Act (42 U.S.C. 426(g)) is amended by striking out "medicare qualified Federal employment" and inserting in lieu thereof "medicare qualified government employment by virtue of service described in section 210(a)(5)".

(c) *Optional Medicare Coverage of Current Employees.*—Section 218 of the Social Security Act (42 U.S.C. 418) is amended by adding at the end the following new subsection:

"(v)(1) The Secretary shall, at the request of any State, enter into or modify an agreement with such State under this section for the purpose of extending the provisions of title XVIII, and sections 226 and 226A, to services performed by employees of such State or any political subdivision thereof who are described in paragraph (2).

"(2) This subsection shall apply only with respect to employees—

"(A) whose services are not treated as employment as that term applies under section 210(p) by reason of paragraph (3) of such section; and

"(B) who are not otherwise covered under the State's agreement under this section.

"(3) Payments by the State required under subsection (e) with respect to employees covered under this subsection shall be limited to amounts equivalent to the sum of the taxes which would be imposed by sections 3101(b) and 3111(b) of the Internal Revenue Code of 1954 if such services for which wages were paid to such employees constituted 'employment' as defined in section 3121 of such Code.

"(4) For purposes of sections 226 and 226A of this Act, services covered under an agreement pursuant to this subsection shall be treated as 'medicare qualified government employment'.

"(5) Except as otherwise provided in this subsection, the provisions of this section shall apply with respect to services covered under the agreement pursuant to this subsection.

"(w) Notwithstanding sections 3125(a), 6205(a)(5), 6413(a)(5), and 6413(c)(2)(G) of the Internal Revenue Code of 1954, any State shall make payments of the taxes imposed with respect to services of employees of such State and of a political subdivision thereof under sections 3101(b) and 3111(b) of such Code, and reports of such services, under the same procedures as apply to payments and reports under subsection (e) of this section, but only if any employees of such State or of such political subdivision thereof respectively are covered under an agreement pursuant to this section.".

(d) *Effective Dates.*—

(1) *Hospital insurance taxes.*—The amendments made by subsection (a) shall apply to services performed after March 31, 1986.

(2) *Medicare coverage.*—

(A) *In general.*—The amendments made by subsection (b) shall be effective after March 31, 1986, and the amendments made by paragraph (3) of that subsection shall apply to services performed (for medicare qualified government employment) after that date.

(B) *Treatment of certain disabilities.*—For purposes of establishing entitlement to hospital insurance benefits under part A of title XVIII of the Social Security Act pursuant to the amendments made by subsection (b), no individual may be considered to be under a disability for any period beginning before April 1, 1986.

(3) *Optional coverage of current employees.*—The amendment made by subsection (c) shall apply to services performed after March 31, 1986.

Section 13206.—Full-time Students Not Eligible for Income Averaging

(a) *In General.*—Subsection (d) of section 1303 (defining eligible individuals for income averaging) is amended to read as follows:

"(d) *Eligible Individuals Not To Include Full-Time Students.*—

"(1) *In general.*—For purposes of this part, an individual shall not be an eligible individual for the computation year if, at any time during any base period year, such individual was a student.

"(2) *Exception for married students providing 25 percent or less of joint income.*—Paragraph (1) shall not apply to any individual for any computation year if—

"(A) the individual makes a joint return for the computation year, and

"(B) not more than 25 percent of the aggregate adjusted gross income of such individual and the spouse of such individual for such computation year is attributable to such individual. In applying subparagraph (B), amounts which constitute earned income (within the meaning of section 911(d)(2)) and are community income under community property laws applicable to such income shall be taken into account as if such amounts did not constitute community income.

"(3) *Student defined.*—For purposes of this subsection, the term 'student' means, with respect to a taxable year, an individual who during each of 5 calendar months during such taxable year—

"(A) was a full-time student at an educational organization described in section 170(b)(1)(A)(ii); or

"(B) was pursuing a full-time course of institutional on-farm training under the supervision of an accredited agent of an educational organization described in section 170(b)(1)(A)(ii) or of a State or political subdivision of a State.".

(b) *Repeal of Non-Full-Time Student Support Exception.*—Paragraph (2) of section 1303(c) (relating to individuals receiving support from others) is amended—

(1) by striking out subparagraph (A),

(2) by redesignating subparagraphs (B) and (C) as subparagraphs (A) and (B), and

(3) by striking out "subparagraph (C)" in the second sentence and inserting in lieu thereof "subparagraph (B)".

(c) *Effective Date.*—The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1985.

Section 13207.—Application of Fringe Benefits Rules to Airlines and Their Affiliates

(a) *Parents of Airline Employees Treated as Employees in Applying Fringe Benefit Rules.*—

(1) *In general.*—Section 132(f) (relating to certain individuals treated as employees with respect to certain fringe benefits) is amended by adding at the end thereof the following new paragraph:

"(3) *Special rule for parents in the case of air transportation.*—Any use of air transportation by a parent of an employee (determined without regard to paragraph (1)(B)) shall be treated as use by the employee.".

(2) *Effective date.*—The amendment made by this subsection shall take effect on January 1, 1985.

(b) *Line of Business Test for Affiliates Providing Airline-Related Services.*—

(1) *In general.*—Section 132(h) (relating to special rules) is amended by adding at the end thereof the following new paragraph:

"(6) *Special Rule for Affiliates of Airlines.*—

"(A) *In General.*—If—

"(i) a qualified affiliate is a member of an affiliated group another member of which operates an airline, and

"(ii) employees of the qualified affiliate who are directly engaged in providing airline-related services are entitled to no-additional-cost service with respect to air transportation provided by such other member, then, for purposes of applying paragraph (1) of subsection (a) to such no-additional-cost service provided to such employees, such qualified affiliate shall be treated as engaged in the same line of business as such other member.

"(B) *Qualified Affiliate.*—For purposes of this paragraph, the term 'qualified affiliate' means any corporation which is predominantly engaged in airline-related services.

"(C) *Airline-related services.*—For purposes of this paragraph, the term 'airline-related services' means any of the following services provided in connection with air transportation:

"(i) Catering.

"(ii) Baggage handling.

"(iii) Ticketing and reservations.

"(iv) Flight planning and weather analysis.

"(v) Restaurants and gift shops located at an airport.

"(vi) Such other similar services provided to the airline as the Secretary may prescribe.

"(D) *Affiliated Group.*—For purposes of this paragraph, the term 'affiliated group' has the meaning given such term by section 1504(a)."

(2) *Effective date.*—The amendment made by this subsection shall take effect on January 1, 1985.

(c) *Transitional Rule for Determination of Line of Business in Case of Affiliated Group Operating Airline.*—If, as of September 12, 1984—

(1) an individual—

(A) was an employee (within the meaning of section 132 of the Internal Revenue Code of 1954, including subsection (f) thereof) of one member of an affiliated group (as defined in section 1504 of such Code), hereinafter referred to as the "first corporation" and

(B) was eligible for no-additional-cost service in the form of air transportation provided by another member of such affiliated group, hereinafter referred to as the "second corporation",

(2) at least 50 percent of the individuals performing service for the first corporation were or had been employees of, or had previously performed services for, the second corporation, and

(3) the primary business of the affiliated group was air transportation of passengers, then, for purposes of applying paragraphs (1) and (2) of section 132(a) of the Internal Revenue Code of 1954, with respect to no-additional-cost services and qualified employee discounts provided after December 31, 1984, for such individual by the second corporation, the first corporation shall be treated as engaged in the same air transportation line of business as the second corporation. For purposes of the preceding sentence, an employee of the second corporation who is performing services for the first corporation shall also be treated as an employee of the first corporation.

(d) *Special Rule for Services Related to Providing Air Transportation.*—Section 531 of the Tax Reform Act of 1984 is amended by redesignating subsections (g) and (h) as subsections (h) and (i), respectively, and by inserting after subsection (f) the following new subsection:

"(g) *Special Rule for Certain Services Related to Air Trasportation.*—

"(1) *General.*—If—

"(A) an individual performs services for a qualified air transportation organizatioin, and

"(B) such services are performed primarily for persons engaged in providing air transportation and are of the kind which (if performed on September 12, 1984) would qualify such individual for no-additional-cost services in the form of air transportation then, with respect to such individual, such qualified air transportation organization shall be treated as engaged in the line of business of providng air transportation.

"(2) *Qualified air transportation orga-*

nization.—For purposes of paragraph (1), the term 'qualified air transportation organization' means any organization—

"(A) if such organization (or a predecessor) was in existence on September 12, 1984,

"(B) if—

"(i) such organization is described in section 501(c)(6) of the Internal Revenue Code of 1954 and the membership of such organization is limited to entities engaged in the transportation by air of individuals or property for compensation or hire, or

"(ii) such organization is a corporation all the stock of which is owned entirely by entities referred to in clause (i), and

"(C) if such organization is operated in furtherance of the activities of its members or owners.".

Section 13208.—Certain Insolvent Taxpayers Allowed to Reduce Capital Gains Preference Item for Purposes of the Individual Minimum Tax

(a) *In General*.—Paragraph (9) of section 57(a) (relating to capital gains as items of tax preference) is amended by adding at the end thereof the following new subparagraph:

"(E) *Special rule for certain insolvent taxpayers*.—

"(i) *In general*.—The amount of the tax preference under subparagraph (A) shall be reduced (but not below zero) by the excess (if any) of—

"(I) the applicable percentage of gain from any farm insolvency transaction, over

"(II) the applicable percentage of any loss from any farm insolvency transaction which offsets such gain.

"(ii) *Reduction limited to amount of insolvency*.—

The amount of the reduction determined under clause (i) shall not exceed the amount by which the taxpayer is insolvent immediately before the transaction (reduced by any portion of such amount previously taken into account under this clause).

"(iii) *Farm insolvency transaction*.—For purposes of this subparagraph, the term 'farm insolvency transaction' means—

"(I) the transfer by a farmer of farmland to a creditor in cancellation of indebtedness or

"(II) the sale or exchange by the farmer of property described in subclause (I) under the threat of foreclosure, but only if the farmer is insolvent immediately before such transaction.

"(iv) *Insolvent*.—For purposes of this subparagraph, the term 'insolvent' means the excess of liabilities over the fair market value of assets.

"(v) *Applicable percentage*.—For purposes of this subparagraph, the term 'applicable percentage' means that percentage of net capital gain with respect to which a deduction is allowed under section 1202(a).

"(vi) *Farmland*.—For purposes of this subparagraph, the term 'farmland' means any land used or held for use in the trade or business of farming (within the meaning of section 2032A(e)(5)).

"(vii) *Farmer*.—For purposes of this subparagraph, the term 'farmer' means any taxpayer if 50 percent or more of the average annual gross income of the taxpayer for the 3 preceding taxtable years is attributable to the trade or business of farming (within the meaning of section 2032A(e)(5))."

(b) *Effective Date*.—The amendment made by this section shall apply to transfers or sales or exchanges made after December 31, 1981, in taxable years ending after such date.

Section 13209.—Treatment of Certain Pollution Control Bonds

(a) *General Rule*.—For purposes of subparagraph (F) of section 103(b)(4) of the Internal Revenue Code of 1954 (relating to pollution control facilities), any obligation issued after December 31, 1985, shall be treated as described in such subparagraph if it is part of an issue substantially all of the proceeds of which are used by a qualified regional pollution control authority to acquire existing air or water pollution control facilities which the authority itself will operate in order to maintain or improve control of pollutants. The provisios of section 103(b)(17) of such Code (relating to prohibition on acquisition of existing property not permitted) shall not apply to any obligation described in the preceding sentence.

(b) $200,000,000 *Limitations*.—The aggregate amount of obligations to which subsection (a) applies shall not exceed $200,000,000, except that the amount of such obligations issued during calendar year 1986 to which subsection (a) applies shall not exceed $100,000,000.

(c) *Restrictions*.— Subsection (a) shall apply only if—

(1) the amount paid (directly and indirectly) for the facilities does not exceed their fair market value,

(2) the fees or charges imposed (directly or indirectly) on any seller for the use of any facilities after the sale are not less than the amounts charged for the use of such facilities to persons other than the seller,

(3) the original use of the facilities acquired with the proceeds of such obligations commenced before September 3, 1982, and

(4) no person other than the qualified regional pollution control authority is considered after the sale as the owner of the facilities for purposes of Federal income taxes.

(d) *Qualified Regional Pollution Control Authority Defined*.—For purposes of this section, the term "qualified regional pollution control authority" means an authority which—

(1) is a political subdivision created by State law to control air or water pollution.

(2) has within its jurisdictional boundaries all or part of at least 2 counties (or equivalent political subdivision),

(3) operates air or water pollution control facilities, and

(4) was created on September 1, 1969.

(e) *Repeal on Section 103(b)(11)*.—Paragraph (11) of section 103(b) is hereby repealed.

Section. 13210.—Treatment of the Netting of Gains and Losses by Cooperatives

(a) *In General*.—Section 1388 (relating to definitions and special rules applicable to cooperatives) is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:

"(j) *Special Rules for the Netting of Gains and Losses by Cooperatives*.—For purposes of this subchapter, in the case of any organization to which part I of this subchapter applies—.

"(1) *Optional netting of patronage gains and losses permitted*.— The net earnings of such organization may, at its option, be determined by offsetting patronage losses (including any patronage loss carried to such year) which are attributable to 1 or more allocation units (whether such units are functional, divisional, departmental, geographic, or otherwise) against patronage earnings of 1 or more other such allocation units.

"(2) *Certain netting permitted after section 381 transactions*.—If such an organization acquires the assets of another such organization in a transaction described in section 381(a), the acquiring organization may, in computing its net earnings for taxable years ending after the date of acquisition, offset losses of 1 or more allocation units of the acquiring or acquired organization against earnings of the acquired or acquiring organization, respectively, but only to the extent—

"(A) such earnings are properly allocable to periods after the date of acquisition, and

"(B) such earnings could have been offset by such losses if such earnings and losses had been derived from allocation units of the same organization.

"(3) *Notice requirements.*—

"(A) *In general.*—In the case of any organization which exercises its option under paragraph (1) for any taxable year, such organization shall, on or before the 15th day of the 9th month following the close of such taxable year, provide to its patrons a written notice which —

"(i) states that the organization has offset earnings and losses from 1 or more of its allocation units and that such offset may have affected the amount which is being distributed to its patrons,

"(ii) states generally the identity of the offsetting allocation units, and

"(iii) states briefly what rights, if any, its patrons may have to additional financial information of such organization under terms of its charter, articles of incorporation, or bylaws, or under any provision of law.

"(B) *Certain information need not be provided.*—An organization may exclude from the information required to be provided under clause (ii) of subparagraph (A) any detailed or specific data regarding earnings or losses of such units such organization determines would disclose commercially sensitive information which—

"(i) could result in a competitive disadvantage to such organization, or

"(ii) could create a competitive advantage to the benefit of a competitor of such organization.

"(C) *Failure to provide sufficient notice.*—If the Secretary determines that an organization failed to provide sufficient notice under this paragraph—

"(i) the Secretary shall notify such organization, and

"(ii) such organization shall, upon receipt of such notification, provide to its patrons a revised notice meeting the requirements of this paragraph.

Any such failure shall not affect the treatment of the organization under any provision of this subchapter or sectio 521.

"(4) *Patronage earnings or losses defined.*—For purposes of this subsection, the terms 'patronage earnings' and 'patronage losses' means earnings and losses, respectively, which are derived from business done with or for patrons of the organization."

(b) *Tax-Exempt Status Not Affected By Netting.*—Section 521(b) (relating to applicable rules) is amended by adding at the end thereof the following new paragraph:

"(6) *Netting of losses.*—Exemption shall not be denied any such association because such association computes its net earnings for purposes of determining any amount available for distribution to patrons in the manner described in paragraph (1) of section 1388(j)."

(c) *Effective Date.*—

(1) *In General.*—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 1962.

(2) *Notification requirement.*—The provisions of section 1388(j)(3) of the Internal Revenue Code of 1954 (as added by subsection (a)) shall apply to taxable years beginning on or after the date of the enactment of this Act.

(3) *No inference.*—Nothing in the amendments made by this section shall be construed to infer that a change in law is intended as to whether any patronage earnings may or not be offset by nonpatronage losses, and any determination of such issue shall be made as if such amendments had not been enacted.

Section 13211.—Allocation Under Section 861 of Research and Experimental Expenditures

Subsection (c) of section 126 of the Deficit Reducation Act of 1984 is amended—

(1) by striking out "1985" and inserting in lieu thereof "1986"; and

(2) by striking out "3rd" each place it appears and inserting in lieu thereof "4th".

Section 13212.—Limitation on Issuance of United States Bonds

Subsection (a) of section 3102 of title 31, United States Code, is amended by striking out "$200,000,000,000" and inserting in lieu thereof "$250,000,000,000".

Section 13213.—Authorization of Additional Funds to Internal Revenue Service for Revenue Enforcement and Related Purposes, etc

(a) *Authorization.*—There is authorized to be appropriated $46,500,000 for each of the fiscal years 1986, 1987, and 1988 for the use of the Internal Revenue Service to employ 1,550 additional agents and examination employees.

(b) *Restoration of Proposed Cuts.*—It is the sense of the Congress that—

(1) the restoration of the cuts in the budget for the Internal Revenue Service for fiscal year 1986, and

(2) the further increase in such budget total, recommended by the Committee on Appropriations of the House of Representatives are necessary for the efficient operation of the Government and to carry out the purposes of this Act.

Subtitle C—Provisions Relating to Unemployment Taxes

Section 13301. Railroad Unemployment Repayment Tax

(a) *Rate of Tax.*—Subsection (c) of section 3321 of the Internal Revenue Code of 1954 (relating to rate of railroad unemployment repayment tax) is amended to read as follows:

"(c) *Rate of Tax.*—For purposes of this section—

"(1) *In General.*—The application percentage for any taxable period shall be the sum of—

"(A) the basic rate for such period, and

"(B) the surtax rate (if any) for such period.

"(2) *Basic rate.*—For purposes of paragraph (1)—

"(A) *For periods before 1989.*—The basic rate shall be—

"(i) 4.3 percent for the taxable period beginning on July 1, 1986, and ending on December 31, 1986.

"(ii) 4.7 percent for the 1987 taxable period, and

"(iii) 6 percent for the 1988 taxable period.

"(B) *For periods after 1988.*—For any taxable period beginning after December 31, 1988, the basic rate shall be the sum of—

"(i) 2.9 percent, plus

"(ii) 0.3 percent for each preceding taxable period after 1988.

In no event shall the basic rate under this subparagraph exceed 5 percent.

"(3) *Surtax Rate.*—For purpose of paragraph (1), the surtax rate shall be—

"(A) 3.5 percent for any taxable period if, as of September 30 of the preceding calendar year, there was a balance of transfers (or unpaid interest thereon) made after September 30, 1985, to the railroad unemployment insurance account under section 10(d) of the Railroad Unemployment Insurance Act, and

"(B) zero for any other taxable period.

"(4) *Basic rate not to apply to rail wages paid after September 30, 1990.*—The basic rate under paragraph (1)(A) shall not apply to rail wages paid after Septebmer 30, 1990"

(b) *Base of Tax To Be Compensation Used for Railroad Retirement Tax Purposes.*—Subsection (b) of section 3323 of such Code (defining rail wages) is amended to read as follows:

"(b) *Rail Wages.*—

"(1) *In general.*—For purposes of this chapter, the term 'rail wages' means compensation (as defined in section 3231(e) for purposes of the tax imposed by section 3201(a)) with the modifications specified in paragraph (2).

"(2) *Modifications.*—In applying subsection (e) of section 3231 for purposes of paragraph (1)—

"(A) *Only employment covered by railroad unemployment insurance act taken into account.*—Such subsection (e) shall be applied—

"(i) by substituting 'rail employment' for 'services' each place it appears,

"(ii) by substituting 'rail employer' for 'employer' each place it appears, and

"(iii) by substituting 'rail employee' for 'employee' each place it appears.

"(B) *$7,000 wage base.*—Such subsection (e) shall be applied by substituting for 'the applicable base' in paragraph (2)(A)(i) thereof—

"(i) except as provided in clauses (ii) and (iii), '$7,000',

"(ii) '$3,500' for the taxable period beginning on July 1, 1986, and ending on December 31, 1986,and

"(iii) for purposes of applying the basic rate under section 3321(c)(1)(A), '$5,250' for the taxable period beginning on January 1, 1990.

"(C) *Successor employers.*—for purposes of this subsection, rules similar to the rules applicable under section 3231(e)(2)(C) shall apply."

(c) *Use of Taxes.*—

(1) *In general.*—Paragraph (2) of section 232(a) of the Railroad Retirement Revenue Act of 1983 (relating to tax used to repay loans made to railroad unemployment insurance account) is amended to read as follows:

"(2) *Taxes credited against loans to railroad unemployment insurance account.*—

"(A) *Taxes attributable to basic rate to reduce railroad unemployment loans made before October 1, 1985.*—So much of the amount transferred under paragraph (1) as is attributable to the basic rate under section 3321(c)(1)(A) of the Internal Revenue Code of 1954 shall be credited against, and operate to reduce, the outstanding balance of railroad unemployment loans made before October 1, 1985.

"(B) *Taxes attributable to surtax rate to reduce railroad unemployment loans made after September 30, 1985.*—So much of the amount transferred under paragraph (1) as is attributable to the surtax rate under section 3321(c)(1)(B) of such Code shall be credited against, and operate to reduce, the outstanding balance of railroad unemployment loans made after September 30, 1985."

(2) *Transfers to railroad unemployment fund after loan repaid.*—Subsection (c) of section 232 of such Act is amended—

(A) by striking out "the amount" in paragraph (1) and inserting in lieu thereof "the amount described in subparagraph (A) or (B) of subsection (a)(2)", and

(B) by inserting before the comma at the end of paragraph (2) "against which the amount described in such subparagraph may be credited under such subparagraph".

(d) *Technical Amendments.*—

(1) Subsection (a) of section 3322 of such Code (relating to taxable period) is amended—

(A) by adding "and" at the end of paragraph (1), and

(B) by striking out paragraphs (2) and (3) and inserting in lieu thereof the following:

"(2) each calendar year after 1986."

(2) Subsection (b) of section 3322 of such Code (relating to earlier termination if loans to rail unemployment fund repaid) is amended—

(A) by striking out "The tax imposed by this chapter shall not apply" and inserting in lieu thereof "The basic rate under section 3321(c)(1)(A) of the tax imposed by section 3321 shall not apply", and

(B) by inserting "made before October 1, 1985," after "no balance of transfers" in paragraph (1) thereof.

Section 13302.—Extension of Borrowing Authority Under the Railroad Unemployment Insurance Act

Section 10(d) of the Railroad Unemployment Insurance Act is amended by striking out the last sentence thereof.

Section 13303.—Certain Exemptions from the Federal Unemployment Tax Act

(a) *Certain Agricultural Labor.*—Paragraph (1)(B) of section 3306(c) of the Internal Revenue Code of 1954 (defining employment) is amended by striking out "January 1, 1986," and inserting in lieu thereof "January 1, 1988".

(b) *Full-Time Students Employed by Summer Camps.*—Notwithstanding paragraph (3) of section 276(b) of the Tax Equity and Fiscal Responsibility Act of 1982, the amendments made by paragraphs (1) and (2) of such section 276(b) shall also apply to remuneration paid after September 19, 1985.

(c) *Services Performed on Certain Fishing Boats.*—

(1) *In general.*—Section 822(b) of the Economic Recovery Tax Act of 1981 is amended to read as follows:

"(b) *Effective Date.*—The amendments made by subsection (a) shall apply to remuneration paid after December 31, 1980.".

(2) *Technical amendment.*—Paragraph (20) of section 312(b) of such Code (defining employment for purposes of Federal Insurance Contributions Act) is amended by inserting "(other than service described in paragraph (3)(A))" after "service".

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CONSOLIDATED OMNIBUS BUDGET RECONCILIATION ACT OF 1985

October 2 (legislative day, September 30), 1985

Mr. Domenici, from the Committee on the Budget, submitted the following report to accompany S. 730[1]

The Committee on the Budget, to which were submitted recommendations pursuant to section 2 of the First Concurrent Resolution on the Budget for Fiscal Year 1986 (S. Con. Res. 32, Ninety-ninth Congress), having considered the same, reports favorably thereon and recommends that the bill embodying those recommendations do pass.

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[327] D. SOCIAL SECURITY

1. Coverage of Senior Status Federal Judges Current law.—

Federal judges are appointed for life. Once a judge qualifies for retirement, he continues to receive his annual pay, regardless of whether he chooses to continue on active duty in the judiciary. Prior to enactment of P.L. 98–21, Federal judges, like all Federal employees, were excluded from Social Security coverage so the question of Social Security taxes did not arise. Additionally, the amounts received by judges who had achieved senior (retired) status had been determined not to be wages for purposes of the earnings test.

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[1] Public Law 99-272, page 4

The 1983 Social Security Amendments (Public Law 98–21) provided that the wages of all active Federal judges would be subject to Social Security taxes beginning January 1, 1984. This provision applied to both current and future judges. P.L. 98–21 also specifically provided that amounts received by judges who achieve senior (retired) status but who continue on active duty would be subjet to Social Security taxes on so much of their pay as was attributable to periods when they were performing judicial services. Those earnings would also cause reductions in the judges' benefits under the Social Security retirement test. (Subsequently, P.L. 98–118 delayed the effective date of this provision until January 1, 1986.)

Explanation of provision.—For purposes of the Social Security Act, the provision would exclude the amounts received by Federal judges who meet the criteria for retirement on salary (e.g. age 65 with 15 years of service or age 70 with 10 years of service), retire, and perform active duty, from the definition of wages. The effect of this exclusion would be to exempt their pay from Social Security taxes and to preclude it from being counted for Social Security earnings test purposes.

Effective date.—Effective for services performed after December 31, 1983.

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[357] K. PENSION BENEFIT GUARANTY CORPORATION

1. Increase Pensin Benefit Guaranty Corporation Premiums

Current law.—The Employee Retirement Income Security Act of 1974 (ERISA) established a program of insurance for employee benefits under most tax-qualified, private, domestic, defined benefit pension plans.[1] The insurance program is administered by the Pension Benefit Guaranty Corporation (PBGC), a Federal corporation within the Department of Labor. The Board of Directors of the PBGC consists of the Secretary of the Treasury, the Secretary of Labor, and the Secretary of Commerce. The Secretary of Labor is the Chairman of the Board. Receipts and disbursements of the PBGC are included in the budget of the United States.

Under present law, a defined benefit plan that is subject to the insurance program is required to pay annual premiums to the Pension Benefit Guaranty Corporation (PBGC). The PBGC is required by ERISA to maintain four separate premium rate and base schedules under the program. Under the Act, the PBGC maintains separate schedules for basic and nonbasic benefits under single-employer plans and corresponding schedules for multiemployer plans.[2] Insurance of basic benefits under a plan is mandatory.

Basic benefits under a single-employer plan (generally consisting of nonforfeitable retirement benefits) are insured by the PBGC up to the lessor of $750 per month, adjusted for inflation since 1974 ($1,687.50 for 1985) or a participant's average monthly compensation for the period of five years for which that compensation is the highest. The insurance of benefits is generally phased in over a five-year period.

ERISA provides that the annual per-participant premium for insurance of basic benefits under a single-employer plan is $2.60.[3] The annual per-participant premium for insurance of basic benefits under a multiemployer plan is $1.80 for plan years beginning in 1985 or 1986, $2.20 for plan years beginning in 1987 or 1988, and $2.60 [358] for plan years beginning thereafter. Special rules are provided for cases in which an employee participates in more than one single-employer plan maintained by the same employer. Similar rules apply to employees with multiple coverage under multiemployer plans. Generally, the level of benefits guaranteed by the PBGC is lower under a multiemployer plan than under a single-employer plan.

The PBGC is authorized by ERISA to revise the premium rate and base schedules for basic benefits under single-employer plans and multiemployer plans whenever it determines that revision is necessary. Approval by the Congress is required, however, for per-participant annual premiums in excess of $2.60. A proposed change in a schedule is to be submitted to the Committee on Ways and Means and the Committee on Education and Labor of the House of Representatives and to the Committee on Finance and the Committee on Labor and Human Resources of the Senate. ERISA requires that premium rates prescribed by the PBGC must be uniform for all single-employer plans with respect to basic benefits. The PBGC is authorized by ERISA to provide a risk-related premium (within limits) for single-employer and multiemployer plans but this authority has not been exercised.

The PGBC maintains a trust fund and a revolving fund for insurance of benefits under terminated plans. Separate funds are maintained for single-employer plans and multiemployer plans. The funds maintained by the PBGC to provide benefits under terminated single-employer plans are the sole Federal source of guaranteed benefits for single-employer plans. The funds maintained by the PGBC to provide guaranteed benefits under multiemployer plans are the sole Federal source of guaranteed benefits for those plans. The PBGC is authorized to borrow up to $100 million from the Treasury of the United States.

Reasons for change.—The Budget Messge of the President for 1986 indicated that under current law, the deficit of the Pension Benefit Guaranty Corporation is expected to increase. According to the Message, the budget reflects the Administration's request that the Congress approve an increase in the single-employer premium to a level sufficient to cover projected claims, and amortize the current deficit over a reasonable period of time. The Message indicates that the Administration also supports "legislation to revise the insurance program for single-employer plans in order to close loopholes in the Employee Retirement Income Security Act of 1974 that allow unwarranted assignment to the Corporation of liabilities for unfunded benefits".

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[1] A defined benefit pension plan specifies a participant's benefits independently of an account for contributions, etc. (e.g., an annual benefit of two percent of average pay for each year of employee service.) A church pension plan is generally exempt from the insurance program unless the plan has elected to be subject to ERISA standards. Exclusions are also provided for plans of small professional service employers and certain other employers.

[2] Under ERISA, a plan is a multiemployer plan if (1) more than one employer is required to make plan contributions, (2) the plan is maintained pursuant to one or more collective bargaining agreements between one or more employee organizations and more than one employer, and (3) the plan meets such other requirements as the Secretary of Labor may prescribe by regulations. In determining whether a plan is a multiemployer plan, employers under common control are treated as one employer. Special rules are provided for terminated plans and for transition cases (Code sec. 414(f) and ERISA sec. 4001(a)(3)). A single-employer plan is a pension plan that is not a multiemployer plan.

[3] The annual, per-participant premium for single-employer plans was initially set by ERISA at $1.00. That premium was increased by Public Law 95–214 to $2.60, effective for plan years beginning after December 31, 1977. Public Law 96–364 increased premiums for multiemployer plans from $.50 to the levels presently provided.

The PBGC presently estimates that its deficit will be $679 million at the end of the 1986 fiscal year.[4] The PBGC estimates that the deficit in its single-employer program will be $721 million at that time.

The Board of Directors of the PBGC has requested that the annual, per-participant premium for single-employer plans be increased to $7.50 from $2.60, effective for plan years beginning on or after [359] January 1, 1985. In a letter of April 9, 1985, the Acting Executive Director of the PBGC stated on behalf of the Board of Directors that:

> Our current request for a $7.50 premium reflects the need to fund properly existing liabilities of approximately $1.6 billion for future losses, expected to average $185 million per year, over the next 15 years. The immediate need for the increase is now even more apparent that it was in the last session of the Congress. Sometime early in FY 1985, PBGC's cash flow, as reflected in the Federal Budget accounts, turned negative, and PBGC for the first time began adding to the size of the Federal deficit. Such a trend would accelerate alarmingly in succedding years should an increase not be adopted.

The PBGC has indicated that an annual per-participant premium of $8.10, effective for plan years beginning after December 31, 1985, is equivalent to a premium of $7.50 effective for plan years beginning after December 31, 1984.

After considering the request of the Administration, the committee determined that the premium for single-employer plans should be increased to $8.10 for plan years beginning after December 31, 1985. The premium increase was made prospective because of the administrative burdens that would be imposed on plans if a retroactive increase were adopted and because the PBGC has indicated that this brief deferral will not jeopardize benefits under the program.

Because of concerns over premium levels under the guarantee program for single-employer plans, the committee has directed the Secretary of Labor to make recommendations to the Committee on Finance and to the House Committee on Ways and Means with respect to appropriate premiums for single-employer plans by July 1, 1987. The recommendations of the Secretary are to be provided to the American Academy of Actuaries so that the Academy may attach its comments to the recommendations before they are submitted to the Committee on Finance and to the House Committee on Ways and Means.

The committee expects that the report of the Secretary will include (1) an explanation of the methods used by the PBGC in determining liability under the single-employer termination insurance program; (2) an evaluation of alternative methods of determining that liability; (3) an explanation of the methods used by the PBGC to determine the premium needed to adequately fund its liability under the single-employer termination insurance program, together with an estimae of the required premium under each of the alternative methods; (4) the recommended premium needed to adequately fund the liabilities of the PBGC; and (5) an evaluation of the feasibility of establishing a risk-related premium.

Explanation of provision.—Under the bill, the annual per-participant premium for single-employer plans is increased to $8.10 effective for plan years beginning after December 31, 1985. The bill does not modify the premiums for multiemployer plans.

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[361] *L. REVENUES*

1. Full-time Students Not Eligible for Income Averaging

Present law.—An individual whose income fluctuates sharply from year to year, or whose income increases rapidly over a short period, may have a greater aggregate income tax liability over a period of years than another individual earning the same total amount, who has relatively constant earnings on an annual basis. This result derives from two aspects of the income tax—the annual accounting period and the progressive rate schedule.

The rules for income averaging address this disparity by permitting individuals with fluctuating annual incomes partially to avoid the effects of rate progressivity in high-income years. Under these rules, eligible individuals may reduce their tax liabilities during a year for which their income is at least 40 percent greater than the average income for the immediately preceding three years (the "base years"). In such a case, the income averaging provision reduces tax liability by applying a lower marginal rate than would be used under the regular tax system to a portion of a current year's income.

In order to be eligible to use income averaging, an individual (1) must meet one of several alternative standards generally intended to restrict the availability of income averaging to individuals who were self-supporting during the base years, and (2) must have been a United States citizen or resident during the taxable year and the three base years. Under these rules, an individual may be eligible for income averaging, even if he or she has not been self-supporting during one or more of the base years, if he or she has attained the age of 25 and was not a full-time student during at least four years after attaining the age of 21.

In effect, the liability of an individual eligible to use income averaging for a year is calculated in three steps:

First, the taxpayer determines tax liability as if the current year's taxable income equaled a lower amount, i.e., 140 percent of the average income during the base years; this portion of income for the current year is taxed at the rates that would have applied if it had constituted all of the taxpayer's income for the year.

Second, the individual computes the increase in tax liability over the amount determined according to the first step which would result if 25 percent of the remaining income (i.e., total income less 140 percent of average base period income) were added to the portion of income described in the first step.

[362] Third, this increase is multiplied by four and added to the tax liability calculated in the first step in order to determine the individual's tax liability for the current year.[1]

Each of these tax liability computations is performed using the current year's rate schedules.

Reasons for change.—The committee believes that income averaging is intended primarily to benefit taxpayers with widely fluctuating incomes. Under current law, however, taxpayers with sharp but sustained increases in income, typically young persons entering the job market for the first time, may qualify for income averaging and benefit substantially from it.

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[4] The Budget Message of the President estimated that the deficit of the PBGC would be $853 million at the end of the 1986 fiscal year. This projection has been revised in light of more complete information with respect to the 1984 fiscal year.

The committee also believes that the availability of income averaging to individuals who were full-time students during the base period is a source of complexity. Determining whether a taxpayer was self-supporting when he or she was a full-time student is difficult and has been a frequent source of contention between taxpayers and the Internal Revenue Service. The case-by-case determinations that are required represent an administrative burden and impede fair and consistent application of the eligibility rules for income averaging.

Explanation of the provision.—Under the bill, a taxpayer who was a full-time student in any base year is not eligible for income averaging. This rule, however, does not apply if an individual files a joint return and 25 percent or less of the adjusted gross income reportable on the joint return is attributable to that individual. Thus, the benefits of income averaging would be available in situations where one spouse was a full-time student during one or more of the base years but had a relatively insubstantial amount of income during the current year.

Consistent with these changes, the exception to the requirement that an eligible individual must be self-supporting during each of the base years, applying to individuals who are 25 years of age or older and were not full-time students during at least four years after they reached 21 years of age, is repealed.

Effective date.—The provision relating to income averaging is effective for taxable years beginning after December 31, 1985.

2. *Employers Required to Provide Certain Employees and Family Members With Continued Health Insurance Coverage at Group Rates*

Present law.—Present tax law includes several incentives designed to encourage employers to provide health benefits to their employees. Employer contributions to a plan providing accident or health coverage, and certain benefits actually paid under such plans, are not subject to income tax, social security tax, or unemployment tax. At the same time, employer contributions to fund such excludable medical benefits are deductible, within limits.

A deduction is allowed to an employer for compensation paid to employees in the form of contributions to or benefits paid under a [363] health plan, provided such costs constitute ordinary and necessary business expenses (sec. 162).

Effective for taxable years beginning after 1981, no deduction is permitted for expenses paid or incurred by an employer for a group health plan if the plan differentiates in the benefits it provides between individuals having end stage renal (kidney) disease and other individuals (sec. 162(i)(1)). Thus, no deductions are permitted for contributions to a group health plan that differentiates directly or indirectly on the basis of the existence of end stage renal disease or the need for renal dialysis.

There are no Federal requirements that employer-based group health insurance plans provide continuation options for any individuals who lose coverage in the health plan under any circumstances.

Under present law, an employer's contributions to a plan providing accident or health benefits, whether insured or self-insured, are excludable from the employee's income (sec. 106). Reimbursements to employees under an employer's health plan for costs incurred for medical expenses (within the meaning of sec. 213), and payments unrelated to absence from work, are excluded from the employee's gross income (sec. 105(b)). Similar exclusions apply for employment tax purposes.

Other benefits actually paid under accident and health plans, such as certain disability benefits, generally are includible in the employee's gross income to the extent attributable to employer contributions (sec. 105(a)). In the case of a self-insured medical reimbursement plan (sec. 105(h)), no exclusion is provided for benefits paid to any employee who is among the five highest-paid officers, a 10-percent shareholder, or among the 25-percent highest-paid employees if the program discriminates in favor of this group as to either eligibility to participate or the medical benefits actually provided under the plan.

Reasons for change.—The committee was concerned that certain spouses and dependent children may be deprived of health benefits due to an unexpected change in family status. To provide an opportunity for these individuals to secure health benefits, the committee believes it is appropriate to require that employer group health plans offer qualified beneficiaries an election to continue coverage for a limited period of time.

Explanation of provision.—Under the bill, generally effective for plan years beginning after June 30, 1986, no deduction is permitted for employer contributions to any group health plan if that plan or any other plan of the employer fails to provide qualified beneficiaries a continuation coverage election. The election must be provided for previously covered family members of deceased, divorced, or Medicare eligible workers, employees who have separated from service (and their dependents), and certain children who would otherwise lose coverage under the terms of the plan upon attainment of majority.

In addition, no income exclusion is permitted under the bill for any highly compensated individual if the plan in which the individual participates or any other group health plan maintained by the employer fails to provide continuation coverage.

[364] As under present law, a group health plan is any employer-provided plan to provide medical care to employees, former employees, or the families of such employees or former employees directly or through insurance reimbursement or otherwise.

Under the bill, no employer will be permitted to deduct contributions to any insured or self insured group health plan (sec. 106) if that plan or any other group health plan maintained by the employer fails to provide qualified beneficiaries a continuation coverage election.

The bill generally requires that continuation coverage be provided under any employer-provided group health plan. However, no continuation coverage would be required in a plan established and maintained by (1) an employer that normally employed 25 or fewer employees during the preceding calendar year, (2) the Government of the United States, the government of any State or political subdivision thereof, or any agency or instrumentality of any of the foregoing entities, or (3) a church or convention or association of churches, or a tax-exempt organization that is operated, supervised, or controlled by any of the foregoing.

Under the bill, any highly compensated individual covered by any insured or self-insured group health plan would be denied the income exclusion for employer

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[1] For example, if 140 percent of the average income in the base years equals $40,000, and the taxable income for the current year equals $80,000, then the portion of the income between $40,000 and $80,000 is all taxed at the marginal rate applying under the regular rate schedules between $40,000 and $50,000.

contributions to the plan (sec. 106) if that plan, or any other group health plan maintained by the employer, fails to provide qualified beneficiaries a continuation coverage election.

The bill defines a highly compensated individual as any employee who is among the five highest-paid officers, a 10-percent shareholder, or among the 25-percent highest-paid employees.

Under the bill, all qualified beneficiaries who would otherwise lose coverage as a result of a qualifying event must have the right to elect, within the 60-day period beginning on the date of the qualifying event, to continue coverage. Qualifying events include (1) the death of the covered employee; (2) the separation from service of the covered employee (whether voluntary or involuntary); (3) the divorce or legal separation of the covered employee from the employee's spouse; (4) the covered employee's commencement of Medicare coverage; or (5) the cessation of dependent child coverage under the terms of the plan (e.g., upon attainment of majority).

Under the bill, an employer is required to provide notice of the election to continue coverage at such time and in such manner as the Secretary of the Treasury shall prescribe. The committee intends that the employer should be required to provide notice of the election to all covered employees no later than the date on which the employee becomes entitled to coverage under the plan.

In addition, a qualified beneficiary must, under the bill, elect continuation coverage no later than 60 days after the date of the qualifying event. Provided the qualified beneficiary elects to continue coverage within the 60-day period, the continuation coverage must be effective as of the date of the qualifying event.

In general, the continuation coverage for which a qualified beneficiary must be offered an election is coverage identical to the coverage provided immediately before the qualifying event. For example, if, under the plan, the covered employee had the right to select among several levels of coverage, the qualified beneficiary [365] generally would be entitled to continue whatever level of coverage the employee had selected for the beneficiary prior to the qualifying event.

That coverage could be modified by the employer if such coverage is modified for all similarly situated beneficiaries for whom a qualifying event has not occurred. In addition, if the plan otherwise permits employees and beneficiaries to modify coverage, the qualified beneficiary must be entitled to modify coverage at the same time and in the same manner as other similarly situated beneficiaries.

The applicable level of continuation coverage generally must be provided for a period not less than (1) 18 months immediately following the qualifying event, or (2) such shorter period elected by the qualified beneficiary. However, if the qualified beneficiary initially elects to continue coverage for less than 18 months, the beneficiary need not be granted a subsequent election to extend the coverage for the remainder of the 18-month period. This 18-month period includes, and is not in addition to, any continuation period presently permitted by the plan or required under local law. Thus, for example, if the plan presently provides that dependent coverage ceases one month after the date of an employee's death, the bill would require that beneficiaries be entitled to elect continuation coverage for up to 18 months following the date of death, not the 18-month period beginning with the actual cessation of coverage one month after the employee's death.

Similarly, if there are multiple "qualifying events," the 18-month period begins on the date of the earliest event. For example, if a covered employee terminates employment and is subsequently divorced one month later, the 18-month continuation period applicable to the divorced spouse commences on the date of termination rather than the divorce.

However, coverage need not be provided beyond the date on which the employer ceases to provide any group health plan to employees. If the employer maintains more than one plan, continuation must be provided so long as any plan is offered by the employer.

The bill authorizes the Secretary of the Treasury to prescribe rules defining the appropriate continuation coverage for qualified beneficiaries under a plan terminated in connection with a plant closing. The committee intends that continuation coverage be required notwithstanding the plant closing if the employer continues to maintain any other health plan. The required continuation coverage generally would be that coverage in effect immediately prior to the closing. However, the regulations are to include rules precluding an employer from reducing or eliminating coverage in anticipation of the plant closing.

Under the bill, some or all of the cost of continuation coverage (including reasonable administrative costs of processing the election) could be charged to the qualified beneficiary. The entire premium could be charged to the qualified beneficiary whether or not the employer otherwise subsidizes some or all of the premiums for covered employees. However, in no event may the cost charged to the qualified beneficiary exceed 102 percent of the applicable premium. The applicable premium is defined as the cost to the plan [366] for the period of coverage for a similarly situated beneficiary with respect to whom a qualifying event has not occurred (without regard to whether such cost is paid by the employer or employee).

In the case of a self-insured plan, the bill defines the applicable premium for any year as the cost for a similarly situated beneficiary for the preceding calendar year, adjusted to reflect cost-of-living increases as measured by the GNP deflator. If there has been a significant change affecting a self-insured plan (e.g., a modification of covered benefits, a significant change in the number or composition of the covered workforce, etc.), the employer must determine the cost under regulations to be prescribed by the Secretary of the Treasury, on the basis of a reasonable actuarial estimate.

If the qualified beneficiary elects to continue coverage within 60 days of the qualifying event, the coverage is effective as of the date of the qualifying event. A qualifying beneficiary who elects coverage may be charged for the cost of coverage during the 60-day period.

In addition, the employer may require the qualified beneficiary to pay the applicable premium either directly to the insurer, if any, or to the employer. However, at the election of the qualified beneficiary, premiums may be payable in monthly installments. Of course, a qualified beneficiary who fails to make required premium payments could be denied continuation coverage.

The bill also provides that continuation coverage may not be conditioned directly or indirectly upon insurability of the designated beneficiary.

The bill generally defines qualified beneficiaries to include the spouse and dependent children of an employee entitled to coverage under the terms of the group health plan. In addition, the covered employee is a qualified beneficiary entitled to elect continuation coverage upon termination of employment.

However, the provision intends to extend prior coverage rather than create new classes of covered employees. Thus, no employee, spouse, or child will be considered a qualified beneficiary unless, on the date before the qualifying event, that individual was a beneficiary under the plan. Thus, for example, no employee who had opted not to be covered by a contributory group health plan could elect continuation coverage upon termination of employment. Similarly, if a covered employee had elected not to receive dependent coverage, no spouse or child subsequently is entitled to elect continuation coverage upon the occurrence of a qualifying event.

If there are multiple "qualifying events," the status of an individual as a qualified beneficiary is determined on the day before the occurrence of the earliest qualifying event. For example, if a covered participant terminates employment without electing continuation coverage, no beneficiary could subsequently elect continatuion coverage, e.g., upon the participant's death.

If there are multiple "qualified beneficiaries," only one election generally is required. Where the covered employee terminates employment, for example, no spouse or child would receive continuation coverage unless the employee elects to continue coverage. Similarly, upon the employee's death, divorce, or becoming eligible for Medicare, continuation coverage is to be provided only if the [367] spouse so elects. In that instance, the spouse effectively decides whether coverage will be continued for the children.

The only exceptions to this rule occur where the child is the only qualified beneficiary (e.g., where the spouse is not entitled to coverage under the plan, or with respect to children attaining majority).

Effective date.—The bill generally applies for plan years beginning after June 30, 1986. In the case of a group health plan maintained pursuant to one or more collective bargaining agreements, the bill does not apply to plan years beginning before the earlier of (1) the date the last of the collective bargaining agreements terminate, or (2) January 1, 1987.

3. Application of Fringe Benefit Rules to Airlines and Their Affiliates

Present law.—The Code defines gross income for purposes of the income tax and the tax on self-employment income as including "all income from whatever source derived" and specifies that it includes "compensation for services" (sec. 61). Similarly, the social security and unemployment insurance payroll taxes (FICA and FUTA) and income tax withholding generally apply to all remuneration for employment, including noncash remuneration. Any fringe benefit that does not qualify for exclusion under a specific statutory provision is includible in gross income, and subject to employment taxes, at the excess of its fair market value over any amount paid by the employee for the benefit.

Under the Deficit Reduction Act of 1984 (P.L. 98-369), certain miscellaneous fringe benefits provided by an employer on a nondiscriminatory basis are excluded from the recipient employee's gross income for Federal income tax purposes and from the wage and benefit bases for purposes of social security and other employment taxes, effective January 1, 1985. The fringe benefits excluded under Code section 132 include "no-additional-cost" services and qualified employee discounts provided by an employer to an employee for the use of the employee[2] or for the use of the employee's spouse or dependent children (as defined in sec. 132(f)(2)(B)).

To be excluded as a no-additional-cost benefit, a service must be the same type of service which is sold to the public in the ordinary course of the line of business of the employer in which the employee is performing services. For this purpose, all employees of all corporations in a controlled group of corporations, or all employees of certain commonly controlled businesses, are treated as employed by a single employer.

Under this limitation, for example, an employer which provides both airline services and hotel services to the general public is considered to consist of two separate lines of business. As a consequence, [368] the employees of the airline business of the employer may not exclude, as no-additional-cost services, the fair market value of free or discounted hotel rooms provided to them by their employer (or by any other employer under a reciprocal agreement with their employer); likewise, the employees of the hotel business of the employer may not exclude the fair market value of free or discounted airline tickets provided to them by their employer (or by any other employer under a reciprocal agreement with their employer).

A similar line-of-business limitation applies under the statutory exclusion for qualified employee discounts.

Under an elective grandfather rule, the line-of-business limitation generally does not apply to no-additional-cost services or qualified employee discounts which were provided by an employer to all its employees in all its lines of businesses on and after January 1, 1984. Accordingly, in the example above, free standby flights to the hotel employees would be tax-free if the company provided such services to all its employees since January 1, 1984.

An employer electing this grandfather coverage is subject to a 30-percent excise tax on the excess for the year of (1) the aggregate fair market value of all excludable no-additional-cost service benefits and qualified employee discount benefits provided to all its employees over (2) one percent of the total taxable compensation paid to all its employees (sec. 4977).

Reasons for change.—The committee believes that the parents of an employee who performs services in the business of providing commercial air transporation should receive the same tax treatment, for purposes of the section 132 exclusions, as the spouse and dependent children of that employee. Also, the committee concluded that statutory rules for applying the line-of-business limitation under section 132 should be provided in the case of (1) certain employees of Pan American World Services who were employed by that company on September 12, 1984 and (2) employees of certain airline affiliates who are directly engaged in providing airline-related services.

Explanation of provisions.—The bill amends section 132(f) to provide that any use of commercial air transportation by a parent of an employee is treated as used by the employee, effective January 1, 1985. For purposes of this rule, the term employee does not include an individual who is an employee solely by reason of section 132(f)(1)(B).

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[2] Sec. 132(f)(1) provides that, for purposes of the exclusions for no-additional-cost services and qualified employee discounts, with respect to a line of business of an employer, the term employee means, in addition to an individual who is currently employed by the employer in that line of business, (1) an individual who was formerly employed by the employer in that line of business and who separated from service with the employer in that line of business by reason of retirement or disability; (2) a widow or widower of an individual who died while employed by the employer in that line of business; and (3) a widow or widower of a former employee of that line of business who had separated from service with the employer in that line of business by reason of retirement or disability.

The bill provides a special rule applicable if (1) a corporation that is predominantly engaged in airline-related services is a member of an affiliated group (with in the meaning of sec. 1504(a)) another member of which operates an airline and (2) employees of the first corporation who are directly engaged in providing airline-related services are entitled to no-additional-cost services with respect to air transportation provided by such other members. If this rule applies, the first corporation is treated as engaged in the air transportation line of business of the affiliate which operates the airline, for purposes of determining whether the employees who are directly engaged in providing airline-related services are eligible for the no-additional-cost service exclusion in section 132(a)(1). This provision is effective January 1, 1985.

[369] The term "airline-related services" means any of the following services provided in connection with commercial air transportation:[2] (i) catering; (ii) baggage handling; (iii) ticketing and reservations; (iv) flight planning and weather analysis; (v) restaurants located at an airport and gift shops located at an airport; and (vi) such other similar services provided to airlines as may be prescribed by Treasury regulations. (Flight planning and weather analysis generally means activities such as the provision of computerized and specialized flight plans, the provision of weather information to airlines and notams (notices to airmen), and the provision of computer packages related to those services.) The Treasury may include in category (vi) as similar services only services that directly benefit airlines, and cannot include in category (vi) services (whether or not furished at airports) that are for the convenience of airline passengers, such as hotels, car rentals, and magazine publishing.

The bill also provides a transitional rule for persons employed, as of September 12, 1984, by an airline affiliate under certain circumstances. The transitional rule applies to an individual if, as of September 12, 1984, all of the following conditions are met:

(1) The individual was an employee (within the meaning of sec. 132, including sec. 132(f)) of one member of an affiliated group (as defined in sec. 1504), referred to as the "first corporation," and was eligible for no-additional-cost services in the form of air transportation provided by another member of the affiliated group, referred to as the "second corporation";

(2) at least 50 percent of the individuals performing service for the first corporation were or had been employees of, or had previously performed services for, the second corporation; and

(3) the primary business of the affiliated group was commercial air transportation of passengers.

If all three conditions are met, the first corporation is treated as engaged in the same air transportation line of business as the second corporation for purposes of applying paragraphs (1) and (2) of Code section 132(a), with respect to no-additional-cost services and qualified employee discounts provided for such individuals by the second corporation, and an individual of the second corporation who is performing services for the first corporation is also treated as an employee of the first corporation.

This provision applies to certain benefits provided after December 31, 1984. The intended beneficiaries of the provision are employees of Plan American World Services, Inc. who meet the requirements of the provision.

4. Tax Treatment of Qualified Campus Lodging

Present law.—Section 119 excludes from an employee's gross income the value of lodging provided by the employer if (1) the lodging is furnished for the convenience of the employer, (2) the lodging is on the business premises of the employer, and (3) the employee is required to accept the lodging as a condition of employment.

Several court decisions have held that on-campus housing furnished to faculty or other employees by an educational institution does not qualify for the section 119 exclusion. Therefore, the fair [370] rental value of the housing (less any amounts paid for the housing by the employee) was includable in the employee's gross income and constituted wages for income tax withholding and employment tax purposes in those cases.[3]

Deficit Reduction Act of 1984.—Section 531(g) of the Deficit Reduction Act of 1984 (P.L. 98-369) prohibits the Treasury Department from issuing, prior to January 1, 1986, any income tax regulations that would provide for inclusion in gross income of the excess of the fair market value of qualified campus lodging over the greater of (1) the operating costs paid in furnishing the lodging or (2) the rent received. This moratorium on regulations applies only with respect to qualified campus lodging furnished after December 31, 1983 and before January 1, 1986.

Qualified campus lodging means lodging furnished by a school, college, or university to any of its employees, including nonfaculty employees, or to the employee's spouse or dependents. The moratorium applies only with respect to employer-furnished lodging, that is located on a campus of, or in close proximity to a campus of, the educational institution. Under the Act, the moratorium does not apply with respect to any amount of the value of lodging if such amount was treated as wages or included in income when furnished.

The purpose of providing for the moratorium in the 1984 Act was to allow further time for consideration of arguments by schools and universities that special tax rules governing treatment of housing furnished to their employees should be provided by statute.

Reasons for change.—The committee believes that valuation rules should be provided to resolve continuing disagreements between education institutions and the Internal Revenue Service as to the treatment of qualified campus lodging.

Explanation of provision.—The bill provides that for Federal tax purposes, the fair market value of use (on an annualized basis) of qualified campus lodging furnished by, or on behalf of, an educational institution (within the meaning of sec. 170(b)(1)(A)(ii))[4] shall not be treated as greater than five percent of the appraised value for the year of the lodging provided that an independent appraisal is obtained by a qualified appraiser. (Thus, the appraiser must be qualified to make appraisals of housing, and the appraisal cannot be made by the employer institution or any officer, trustee, or employee thereof.) The committee does not intend that a new appraisal must be obtained each year. However, the committee intends that the appraisal be reviewed annually, in a manner prescribed by [371] Treasury regulations, but that such review should not impose undue cost on the educational institution. Accordingly, under this safe-harbor valuation rule, if the rent paid for qualified campus lodging is equal to or exceeds on an annualized basis five percent of the value determined by each on an appraisal, no amount is included, on account of such housing, in the employee's gross income for income tax purposes or in the wage or benefit base for social security and other employment tax purposes.

The provision applies to lodging furnished to any employee of the educational institution (or to the employee's spouse or dependents), including nonfaculty employees, for use as a residence, if the employer-furnished lodging is located on a campus of, or in the proximity of, the educational institution.

If no appraisal is obtained that meets the requirements of the provision, then the fair rental value for tax purposes is to be determined in the manner as would be done absent a special rule, taking into account all the relevent facts and circumstances. This does not preclude a taxpayer whose appraisal is found defective from subsequently obtaining a qualified appraisal and using the safe-harbor rule. For purposes of applying the first sentence of this paragraph to determine the fair rental value of campus lodging, the average of the rentals paid by individuals (other than employees or students of the educational institution) during such year for lodging provided by the educational institution that is comparable to the campus lodging provided to the employee is to be considered the fair rental value.

The new provision relating to qualified campus lodging does not affect the applicability of section 119(a) to lodging that qualifies for the exclusion in section 119(a).

Effective date.—The provisions of the bill apply for taxable years or periods beginning after December 31, 1985.

For prior taxable years, it is intended (1) that the IRS is to follow the safe-harbor valuation rule of the bill as if in effect for those years (except with respect to any amount of value of campus lodging that was treated by the taxpayer as wages or included in income when furnished), and (2) that the value of the property as assessed by State or local tax authorities for State or local property tax purposes is to be treated as if it were the value determined by a qualified appraisal.

5. Certain Insolvent Taxpayers Allowed to Reduce Capital Gains Preference Item for Individual Minimum Tax Purposes

Present law.—Individuals are subject to a minimum tax, applying at a 20 percent rate to a base determined by adding certain preferences to the taxpayer's regular taxable income (in addition to certain other adjustments). Minimum tax liability is payable only to the extent that it exceeds the taxpayer's regular tax liability. Among the minimum tax preference items is the portion of net capital gain excluded for regular tax purposes under section 1202.

Reasons for change.—The committee believes that under the present-law minimum tax rules, significant hardships have arisen in certain circumstances where an insolvent individual sells appreciated business realty in satisfaction of indebtedness. Such an [372] individual may be subject to the minimum tax with respect to the portion of capital gain excluded for regular tax purposes, particularly if he or she uses other tax preferences. For example, this problem has arisen in the case of certain farmers who have been compelled to transfer appreciated farm land in satisfaction of indebtedness arising as a consequence of farming losses, and who are subject to minimum tax in part because of the use of investment tax credits.

Explanation of provision.—Under the bill, an insolvent taxpayer who transferred real property used in the active conduct of a trade or business of the taxpayer to a creditor in cancellation of indebtedness, or to any third party under threat of foreclosure, would not be required to treat certain capital gain, excluded from income for regular tax purposes under section 1202, as a minimum tax preference. For this purpose, real property would be determined under State law.

The bill would apply only to transfers by individuals. The bill would not apply to a transfer of property being held for investment purposes, or to a transfer of property not used by the individual in the active conduct of a business, as when the individual did not materially participate in management or provide substantial personal services with regard to the trade or business being conducted on the property. Thus, for example, a transfer of farm property by a farming syndicate (as defined in sec. 464(c)) is not within the scope of the bill. For a transfer to which the bill applied, the amount of the reduction in the taxpayer's minimum tax preference for capital gains could not exceed the amount of the taxpayer's insolvency immediately prior to the transfer.

The question of whether, and in what amount, a taxpayer was insolvent would be determined under a standard similar to that set forth in section 108(d)(3), which provides that "the term 'insolvent' means the excess of liabilities over the fair market value of assets." However, the Treasury would have the authority, through regulations or rulings, to determine whether, and to what extent, nonrecourse debt would be treated under the bill in the same manner as under section 108(d)(3).

In the case of a taxpayer who made one or more transfers to which the bill applied, the calculation of the taxpayer's tax preference under section 57(a)(9)(A) (defining the minimum tax capital gain preference for individuals) would be made in several stages. First, the taxpayer would determine the amount of his or her section 1202 net capital gain deduction (as determined for regular tax purposes without making any adjustment for transfers made while insolvent). Second, the taxpayer would determine the amount of his or her net capital gain, if any, with respect to each transfer to which the bill applied. For each such transfer, this amount would be multiplied by the percentage applied in determining the section 1202 deduction (60 percent under present law). The amount derived from this calculation, to the extent not in excess of the amount of the taxpayer's insolvency immediately before the transfer, would then be subtracted from the amount of the taxpayer's regular tax deduction under section 1202. However, "double-counting" would not be allowed with respect to the amount of insolvency. Thus, for example, if a taxpayer made two transfers qualifying under the bill during the same taxable year, the amount of the taxpayer's [373] insolvency for purposes of the second transfer would be reduced by the amount subtracted (for purposes of section 57(a)(9))

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[3] *Bob Jones Univ. v. U.S.*, 670 F.2D 167 (Ct. Cl. 1982); *Goldsboro Christian Schools, Inc. v. U.S.*, 79-1 CCH USTC para. 9266, E.D.N.C. 1978 (value of lodging furnished to faculty constitutes wages subject to income tax, FICA, and FUTA withholding, in light of "long and constent history of regulations and rulings, expressly and explicitly applying withholding taxes to lodging not furnished for the employer's convenience***"), *aff'g* order entered in *Goldsboro Christian Schools, Inc. v. U.S.*, 436 F.Supp. 1314 (E.D.N.C. 1977), *aff'd* per curiam in unpublished opinion (4th Cir. 1981), aff'd 103 S.Ct. 2017 (1983); *Winchell v. U.S.*, 564 F.Supp. 131 (D.Neb. 1983) (value of campus home taxed to college president); and *Coulbourn H. Tyler*, 44 CCH Tax Ct. Mem. 1221 (1982).

[4] An educational organization is described in sec. 170(b)(1)(A)(ii)) "if its primary function is the presentation of formal instruction and it normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. The term includes institutions such as primary, secondary, preparatory, or high schools, and colleges and universities," and includes both public and private schools (Treas. Reg. sec. 1.170A-9(b)(1)).

from the taxpayer's regular tax deduction under section 1202 as a result of the first transfer.

In the case of a taxpayer who, during the same taxable year, realized gain on some transfers to which the provision applied, and loss on other such transfers, the bill would apply only to the extent that such gain exceeded such losses. (In any event, the adjustment made under the bill to the amount of a taxpayer's capital gain preference would still be limited to the relevant amounts of insolvency). It is expected that Treasury regulations would set forth the mechanics of the bill's application in this and all other respects.

The bill would have no effect on the application of other rules of tax law, including the rules for measurement of debt discharge income and for the reduction of tax attributes (such as credit carryovers and net operating losses) pursuant to section 108.

Effective date.—The provision is effective for dispositions made after December 31, 1981.

6. Treatment of Certain Pollution Control Bonds

Present law.—Interest on State and local government obligations generally is exempt from Federal income tax. However, since 1968, tax exemption has not been permitted for interest on industrial development bonds (IDBs). A State or local government bond is an IDB if (1) all or a major portion of the proceeds of the issue are to be used in any trade or business of a person other than a State or local government or tax-exempt organization (described in sec. 501(c)(3)), and if (2) payment of principal or interest is secured by an interest in, or derived from payments with respect to, property or borrowed money used in a trade or business. Exceptions to this general rule in IDBs are provided for certain activities, including the financing of air or water pollution control facilities.

The use of tax-exempt IDBs to acquire facilities generally is prohibited if a substantial user of the facilities before the acquisition will be a substantial user after the acquisition. Additionally, use of IDBs to finance the acquisition of existing property is prohibited unless an amount equal to at least 15 percent of the bond proceeds is spent for rehabilitation of the property.

The aggregate volume of most IDBs and all student loan bonds issued by a State (and local issuer therein) may not exceed the greater of $150 per resident of the State or $200 million.

In 1982, the Congress enacted a limited provision permitting the Gulf Coast Waste Disposal Authority to acquire certain existing air or water pollution control facilities to be owned and operated by the Authority in order to maintain or improve the control of pollutants.

Reasons for change.—The committee believes that modifications to certain of the restrictions contained in the 1982 legislation permitting the Gulf Coast Authority to issue bonds for acquisition of existing pollution control facilities are needed to permit implementation of that 1982 provision. The committee determined, however, that bonds issued pursuant to that provision should be subject to the State volume limitations applicable to most IDBs as well as [374] most other present Code restrictions on such bonds. Additionally, the intent of this provision makes it appropriate to limit its application to facilities the acquisition of which was contemplated at the time of the 1982 legislation.

Explanation of provision.—The bill permits tax-exempt IDBs to be issued, under certain conditions, for use by the Gulf Coast Waste Disposal Authority to acquire existing air or water pollution control facilities which the authority itself will operate. These conditions are (1) that the bonds will be subject to the applicable State volume limitation for private activity bonds and all other restrictions currently applicable to similar IDBs (other than the restriction on acquisition of existing property); (2) that the purchase price of the facilities will not exceed their fair market value; (3) that the fees imposed on any seller for use of any facilities after the sale will not be less than the amounts charged for comparable use of such facilities to persons other than the seller; (4) that no person other than the Authority be considered the owner of the facilities for Federal income tax purposes; and (5) that the total volume of bonds issued for this purpose not exceed $200 million (no part of which will be issued before 1986, and no more than $100 million of which will be issued before 1987).

In addition, the committee determined that only those facilities the acquisition of which was contemplated at the time of the 1982 legislation should qualify for tax-exempt financing. Therefore, bonds issued under this provision may be used only for acquisition of facilities the original use of which commenced before September 3, 1982. The committee understands that the only qualifying facilities are the following:

Armco Steel
13609 Industrial Road
Houston, Texas

Dow Chemical Company
Battleground Road
La Porte, Texas 77571

Ethyl
1000 North South Street
Pasadena, Texas 77503

GAF
Highway 145 at Industrial Road
Texas City, Texas 77590

Lubrizol Corp
41 Tidal Road
Deer Park, Texas 77536

Marathon Petroleum Corp
Foot of Sixth Street
Texas City, Texas 77590

[375] Phillips Chemical Co.
1400 Jefferson Street
Pasadena, Texas 77501

Shell Oil
Shell Chemical
Hwy. 225 at Center Street
Deer Park, Texas 77536

Diamond Shamrock
Tidal Road
Deer Park, Texas 77536

E.I. du Pont
11701 Strang Road
La Port, Texas 77571

Exxon
2800 Decker Drive
Baytown, Texas 77520

Goodyear
2000 Goodyear Drive
Houston, Texas 77017

Lyondell Petrochemical Co.
12000 Lawndale
Houston, Texas 77252–2451

Pasadena Chemicals
Hwy 225
Pasadena, Texas

Rohm & Haahs
Private Road off Hwy. 225
Deer Park, Texas 77536

Stauffer Chemical
1000 Jefferson
Houston, Texas

St. Regis Paper
11611 Fifth Street
Sheldon, Texas 77044

Texas City Refining
Loop 197 South at 14th St
Texas City, Texas 77017

U.S. Industrial Chemicals
1515 Miller Cutoff Road
Deer Park, Texas 77536

U.S. Steel
FM 1405
Baytown, Texas 77520

Texas Alkyls
730 Battleground Road
Deer Park, Texas 77536

Texas Petrochemicals
8600 Parkplace Blvd.
Houston, Texas 77017

USS Chemicals
9822 La Porte Freeway
Houston, Texas 77017

Effective date.—The provision is effective on the date of enactment.

7. Netting for Cooperatives

Present law.—In general, present law permits any corporation operating on a cooperative basis, including a so-called tax-exempt farmers' cooperative, to exclude from taxable income amounts paid as patronage dividends or certain other amounts paid or allocated to members, to the extent of net income generated from transactions with members (sec. 1382). In addition, tax-exempt farmers' cooperatives generally may exclude such amounts to the extent of all net income, and also may exclude to a limited extent dividends paid on common stock (sec. 521).

Patronage dividends are amounts paid or allocated by the cooperative to a patron (a) based on the quantity or value of business done with or for such patron, (b) under a pre-existing obligation of the cooperative to distribute such amounts, and (c) which are determined by reference to the net earnings of the organization from business done with or for its patrons (sec. 1388(a)).

In general, a tax-exempt farmers' cooperative is specifically defined in section 521(b) as a farmers', fruit growers', or like association organized and operated on a cooperative basis either for the purpose of marketing the products of its members or others, or for the purpose of purchasing supplies and equipment for members or other persons. In the case of a tax-exempt farmers' cooperative that markets products, the proceeds of sale by the cooperative less necessary expenses of sale are turned over to the members or other [376] producers on the basis of the quantity or value of the products furnished; in the case of a tax-exempt farmers' cooperative that purchases supplies and equipment, the purchased goods are to be made available at the cooperative's cost, plus necessary expenses.

The Internal Revenue Service has asserted that netting gains and losses from purchasing and marketing operations or from operations in different products or geographic areas may be inconsistent with the statutory definition of a tax-exempt farmers' cooperative, particularly if management has broad discretion over decisions regarding such netting, and members of the cooperative are not informed of the practice. The IRS also has asserted that such netting may be improper for purposes of computing a cooperative's net income, and also may be inconsistent with the statutory requirement that the payment of patronage dividends must be pursuant to a pre-existing obligation.

The Tax Court has addressed some of these issues in three different factual settings. In *Associated Milk Producers*, 68 T.C. 729 (1977), the IRS asserted that a cooperative was not entitled to carry over a net operating loss deduction where doing so would offset patronage income in a taxaxble year with losses from a prior year. However, the court held that the carry over was allowed in circumstances that the court considered reasonable for management to offset the income and loss. In *Ford-Iroquois FS, Inc.*, 74 T.C. 1213 (1980), the IRS asserted that a non-exempt cooperative was not entitled to carry over a net operating loss deduction to the extent that losses from prior years' marketing and storage operations would offset patronage income from farm supply operations. However, the court allowed the carryover, noting that there was substantial overlap of the patrons of the two operations and the allocations otherwise were fair. In *Lamesa Cooperative Gin*, 78 T.C. 894 (1982), the IRS asserted that an exempt cooperative was required to account separately for its purchasing and marketing operations, and included in the cooperative's income certain patronage dividends to the extent income from the cooperative's purchasing operation offset losses from its marketing operation. The court nevertheless held that the cooperative could net the income and loss where the purchasing operation was so small that it would have been unreasonable to account for it separately.

Reasons for change.—The committee believes that netting of earnings and losses is an appropriate practice for both tax-exempt farmers' cooperatives and other cooperatives. In addition, the committee believes that, in the future, cooperatives that net earnings and losses should be required to notify their members of the practice.

Explanation of provision.—The bill provides that a cooperative is not ineligible for treatment as a tax-exempt farmers' cooperative if it offsets certain earnings and losses in determining any amount available for distribution to patrons. For this purpose, the losses that are attributable to one or more allocation units (including a loss that is carried over from another year), may be offset against earnings of one or more other allocation units, but only to the extent such earnings and losses are derived from business done with or for patrons. Such earnings and losses, also called patronage earnings and losses, may be offset without regard to whether the [377] allocation units whose earnings or losses are offset are functional, divisional, departmental, geographic, or otherwise.

The bill also provides that the offsetting of earnings and losses, as described above, may at the option of the cooperative be used for determining the net earnings of the cooperative for the purpose of paying patronage dividends. Moreover, the option of a cooperative to offset earnings and losses is not taken into account for the purpose of determining whether amounts distributed to a patron are distributed pursuant to a pre-existing obligation.

The committee intends that these provisions do not affect a cooperative's ability to use net operating loss deductions available under present law. Moreover, the committee intends no inference regarding the treatment under present law of the offsetting of patronage earnings and losses other than patronage losses. Nevertheless, the committee approves of the result in *Farm Service Cooperative* v. *Comm'r*, 619 F.2d 718 (8th Cir. 1980), which held that a non-exempt cooperative could not offset patronage losses against nonpatronage earnings.

The bill provides that a cooperative that offsets earnings and losses must notify members who may have been affected by such offsetting. The committee intends that the notice must be sent to all such patrons regardless of whether any patronage dividends were in fact distributed, so long as the offsetting may have affected any amount which the patron may otherwise have received in the current or future year, whether in the form of patronage dividend, per-unit retain allocation, notice of allocation, or any other amount distributed or allocated to the member. The notice must be sent to such members by no later than the 15th day of the 9th month following the close of the cooperative's taxable year.

The notice must state that the cooperative has offset earnings and losses of one or more of its allocation units and that such offset has affected the amount that is being distributed to the patron. The notice must state generally the identity of the offsetting allocation units. The notice also must state briefly what rights, if any, that such patron may have to additional financial information of such organization under the terms of its charter, articles of incorporation, bylaws, and any provision of law. Although the notice must specify the identity of the offsetting allocation units (but not which unit's earnings were offset with which unit's losses), the cooperative is not required to disclose in the notice any detailed or specific data that it considers to be commercially sensitive. The committee intends that the cooperative's determination of what information must be considered commercially sensitive for this purpose must be reasonable. The committee also intends that the notice requirement should not place a great burden on a cooperative, and that ordinarily an adequate notice need not exceed one page in length.

Failure to comply with this notice requirement, upon notification of such failure by the Secretary, will require a cooperative to provide a notice that meets the statutory requirements to all patrons who previously received the inadequate notice, but will have no other tax consequences for the cooperative. A cooperative that does not offset gains and losses of any allocation units will not be sub ject to the notice requirement. The committee intends that a [378] cooperative that merely "pools" withing a single allocation unit will not be subject to the notice requirement.

Effective date.—The provisions of the bill relating to cooperatives generally are effective for taxable years beginning after December 31, 1962. However, the provision relating to the notification of cooperative members is effective for taxable years beginning after the date of enactment.

8. Allocation Under Section 861

Present law.—All income has either a U.S. source or a foreign source. The foreign tax credit can offset tax on foreign-source taxable income but not U.S.-source taxable income. (This is known as the foreign tax credit limitation.) A shift in the source of income from foreign to U.S. may increase U.S. tax by reducing the amount of foreign tax that a taxpayer may credit.

In determining foreign-source taxable income for purposes of computing the foreign tax credit limitation, and for other tax porposes, Code sections 861–863 require taxpayers to allocate or apportion expenses between foreign-source income and U.S.-source income. A shift in the allocation of expenses from U.S.- to foreign-source gross income decreases foreign-source taxable income. This decrease may increase U.S. tax by reducing the amount of foreign tax that a taxpayer may credit.

Treasury regulation sec. 1.861–8 (published in 1977) sets forth detailed rules for allocating and apportioning several categories of expenses, including deductible research and experimental expenditures ("research expenses"). The regulation provides that research expenses are ordinarily considered definitely related to all gross income reasonably connected with one or more of 32 product categories based on two-digit classifications of the Standard Industrial Classification ("SIC") system. Research expenses are not traced solely to the income generated by the particular product which benefited from the research activity. Instead these expenses are associated with all the income within the SIC product group in which the product is classified.

Research expenses identified with an SIC product group are generally apportioned to foreign-source income based on the ratio of total foreign-source sales receipts (or, at the taxpayer's option and subject to certain conditions, total foreign-source gross income) within the SIC product group to the taxpayer's total worldwide sales receipts (or gross income) within the SIC product group. However, research expenses incurred to meet legal requirements imposed with respect to improvement or marketing of specific products or processes are allocable entirely to one geographic source if the research and development cannot reasonably be expected to generate income (beyond de minimis amounts) outside that geographic source.

In addition, the regulation provides that 30 percent of research expense is apportioned to income from the geographic source where over half of the taxpayer's research and development is performed. A taxpayer can choose to apportion to the geographic source where research and development is performed a percentage of research expense significantly greater than 30 percent if he establishes tha the higher percenage is warranted because the [379] research and development is reasonably expected to have a very limited or long-delayed application outside that geographic source. Treas. Reg. sec 1.861–8 generally requires a smaller allocation of research expenses to foreign-source income than a predecessor regulation proposed in 1973 would have required.[5]

The Economic Recovery Tax Act of 1981 (ERTA) provided that, for a taxpayer's first two taxable years beginning after the date of its enactment (August 13, 1981), all research and experimental expenditures (within the meaning of Code sec. 174) which were paid or incurred in those taxable years for research activities conducted in the United States were to be allocated or apportioned to income from sources within the United States (sec. 223 of ERTA). This two-year moratorium on the application of the research and experimental expense allocation rules of Treas. Reg. sec. 1.861–8 was effectively extended for two additional years by the Tax Reform Act of 1984. Under the 1984 Act (sec. 126), for taxable years beginning generally after August 13, 1983, and before August 1, 1985, all of a taxpayer's research and experimental expenditures (within the meaning of Code sec. 174) attributable to research activities conducted in the United States are to be allocated to sources within the United States for purposes of computing taxable income from U.S. sources and from sources partly within and partly without the United States.

One reason Congress cited for enacting the original two-year moratorium was that some foreign countries do not allow deductions under their tax laws for expenses of research activities conducted in the United States. Taxpayers argued that this disallowance resulted in unduly high foreign taxes and that, absent changes in the foreign tax credit limitation, U.S. taxpayers would lose foreign tax credits. Because those taxpayers could take their deductions if the research occurred in the foreign country, taxpayers argued that there was incentive to shift their research expenditures to those foreign countries whose laws disallow tax deductions for researcch activities conducted in the United States but allow tax deductions for research expenditures incurred locally.

Accordingly, Congress concluded that the Treasury Department should study the impact of the allocation of research expenses under Treas. Reg. sec. 1.861–8 on U.S.-based research activities and on the availability of the foreign tax credit. While that study was being conducted by the Treasury and considered by Congress, Congress concluded that expenses should be charged to the cost of generating U.S.-source income, whether or not such research was a direct or indirect cost of producing foreign-source income.

In June 1983 the Department of the Treasury submitted its report on the mandated study to the Senate Committee on Finance and the House Committee on Ways and Means.[6] In summary, the Treasury report concluded that:

> Had Treas. Reg. sec. 1.861–8 fully been in effect in 1982, the Treasury Department estimated that the $37 billion in privately financed domestic research and development spending in [380] 1982 would have been reduced by approximately $40 million to $260 million as a result of the increased U.S. tax costs just described. Most of the reduction would have represented a net reduction in overall research and development undertaken by U.S. corporations and their foreign affiliates, rather than a transfer of research and development abroad.
>
> The moratorium reduced U.S. tax liabilities. If the research and development rules of Treas. Reg. sec. 1.861–8 had been in effect in 1982, the Treasury Department estimated that U.S. tax liabilities of U.S. firms would have been $100 million to $240 million higher.
>
> The moratorium reduced the tax liabilities only of firms with excess foreign tax credits. Whether or not a firm had excess foreign tax credits did not seem to be closely related to the level of its research and development efforts.
>
> The moratorium had its most significant effect on large, mature multinationals as opposed to small, relatively young high-technology companies. Of the $100 million to $240 million estimated increase in U.S. tax liabilities for calendar 1982 that would have occurred had Treas. Reg. sec. 1.861–8 been fully in effect, about 85 percent was estimated to be accounted for by 24 U.S. firms on the list of the 100 largest U.S. industrial corporations compiled by *Fortune Magazine*.
>
> An allocation of research and development expense to foreign income could increase a taxpayer's worldwide tax liability if the foreign government did not allow the apportioned expense as a deduction. Some allocation to foreign income, however, was appropriate on tax policy grounds when domestic research and development was exploited in a foreign market and generated foreign income. If an allocation were not made, foreign-source taxable income would be too high and the higher limitation could allow the credit for foreign tax to reduce U.S. tax on domestic-source income.
>
> The research and development rules of Treas. Reg. sec. 1.861–8 reflected significant modifications of the 1973 proposed version of the regulation in response to taxpayer comments. Compared to the 1973 version of the regulations, these modifications allowed less research and development expense to be allocated to foreign income and recognized that research and development conducted in the United States might be most valuable in the domestic market.

On the ground that a reduction in research and development might adversely affect the competitive position of the United States, the 1983 Treasury report recommended the two-year extension of the moratorium that was ultimately enacted by Congress last year. The extension was intended to allow Congress to consider further the results of the Treasury study on the Treasury research expense allocation rules.

Reasons for change.—The committee believes that a further extension of the present temporary moratorium is warranted to allow Congress to examine further the issues involved.

Explanation of provision.—The bill extends for one year the moratorium on the application of the research and experimental expense allocation rules of Treas. Reg. sec. 1.861–8. Under the bill, for taxable years beginning on or before August 1, 1986, all of a taxpayer's research and experimental expenditures (within the meaning of Code sec. 174) attributable to research activities conducted in the United States will be allocated to sources within the United States for purposes of computing [381] taxable income from U.S. sources and from sources partly within and partly without the United States.

This special allocation rule applies only to the allocation of research and experimental expenditures for the purposes of geographic sourcing of income. It does not apply for other purposes, such as the computation of combined taxable income of a DISC (or FSC) and its related supplier.

The extension of the moratorium does not apply to any expenditure for the acquisition or improvement of land, or for the acquisition or improvement of depreciable or depletable property to be used in connection with research or experimentation.

The committee requests the Treasury to consider this allocation issue in connection with its ongoing review of the tax laws and proposals for reform.

Effective date.—The extension of the moratorium on the application of the Treasury's research and experimental expense allocation regulation will apply to a taxpayer's taxable years beginning on or before August 1, 1986 only.

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[389] *12. Medicare Coverage of State and Local Governmental Employment*

Present law.—Under the Old Age, Survivors, and Disability Insurance program (commonly referred to as social security) and the Hospital Insurance program (commonly referred to as Medicare), coverage for State and local government employes is optional. An election for coverage under the Social Security Act includes both programs. A State controls the option for itself and its subdivisions; however, most often State governments allow their political subdivisions to make their own choices.

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[5] See 38 Fed. Reg. 15,840 (1973).

[6] See Department of the Treasury, The Impact of the Section 861–8 Regulation on U.S. Research and Development (June 1983).

[390] When elected, coverage is provided on a group basis through agreements between the State and the Secretary of Health and Human Services. Coverage can be provided even when the State or local government already has a retirement system in place. When there is no retirement system in place, the State or local government entity, not the employees, has the option to choose social security. However, if there is a system already in place, then the Governor or a designee must conduct a referendum of the employees involved.

Until April 1983, the law permitted the termination of coverage for employees covered under an agreement, if the State or local entity (through the State) had given two-years' advance notice. This provision, however, was repealed in the Social Security Amendments of 1983.

Reasons for change.—Individuals who have worked in State and local government employment that is excluded from social security coverage often acquire insured status and thus still may qualify for social security and Medicare benefits. They qualify as a result of work performed in other employment covered under the program or through the entitlement of a spouse. By and large, individuals who qualify after having worked in excluded State and local government employment have contributed significantly less in social security FICA taxes than others and who become entitled to benefits who have had comparable lifetime earnings. They therefore represent a financial drain on the system, and especially on the Medicare hospital insurance program.

Unlike monthly social security benefits, where minimal covered earnings and tax contributions result in minimal benefit amounts, entitlement to Medicare is entitlement for the full range of benefits. The benefits are the same regardless of whether the insured worker has made significant tax contributions over his or her working lifetime or whether the individual has qualified with the minimum number of quarters of coverage. The committee believes that this anomaly should be corrected.

Explanation of provision.—The provision extends Hospital Insurnace (Medicare) coverage to current and new employees of State and local governments. The employers and their employees will become liable for the hospital insurance portion of the FICA tax, which is to be collected as in the case of a private employer, and the employees will earn credit toward Medicare eligibility based on their covered earnings. Mandatory coverage is extended only for Medicare and only for employment not otherwise covered under voluntary State coverage agreements.

Under the provision, State and local government employees who perform service during and before October 1986, would be given credit toward Medicare eligibility for past State and local government employment.

The provision also permits individuals who have worked for State and local governments to obtain Medicare benefits if they file and meet the insured status and other disability eligibility requirements of the social security disability cash benefits program, even though no such cash benefits would otherwise be payable. The Medicare application would be treated as an application for disability benefits (for purposes of determining eligibility to Medicare).

[391] *Effective date.*—The provision is effective with respect to service performed after September 30, 1986, by employees of a State or local government who would not otherwise be covered under social security and Medicare on the basis of voluntary agreements.

13. Railroad Unemployment Repayment Tax

Present law.—Present law provides a railroad unemployment compensation program that is separate from and different than the regular Federal-State unemployment compensation system. Most workers in other industries are covered under the Federal-State unemployment compensation system.

The Railroad Unemployment Insurance (RRUI) program is administered by the Railroad Retirement Board (RRB), which collects the unemployment taxes directly from rail employers. Legislation enacted in 1959 provided the Railroad Unemployment Insurance Account with the authority to borrow from the Railroad Retirement Account when funds in the RRUI Account are not sufficient to meet benefit payments. This borrowing authority expires September 30, 1985. On that date, the outstanding debt to the retirement account is estimated to be $783 million, of which $526 million is principal and $257 million is accumulated interest.

There is no automatic mechanism in the law to repay loans from the retirement account as they occur. Loans are repaid out of basic contributions to the unemployment account when the Railroad Retirement Board determines that there are sufficient funds in the unemployment account to make a repayment.

The Railroad Retirement Solvency Act of 1983 established a repayment tax scheduled to begin on July 1, 1986 and to expire on September 30, 1990. The tax rate will begin at 2.0 percent and increase by 0.3 percentage points a year up to a maximum of 3.2 percent in 1990. The tax is scheduled to expire on September 30, 1990. The tax is paid on the first $7,000 in wages paid annually to a rail employee.

Reasons for change.—The loan repayment tax contained in the 1983 Railroad Retirement Solvency Act is not sufficient to repay the loans made to the Railroad Unemployment Insurance Account and to meet current and projected unemployment insurance benefit payments. The committee believes that an increase in the repayment tax, combined with a surcharge on new borrowing and a temporary one percent diversion of railroad retirement taxes to the Railroad Unemployment Account, will help avert an impending cash-flow crisis and strengthen the system's financial condition in the long run.

Explanation of provision.—The loan repayment tax, scheduled to begin on July 1, 1986 at a 2 percent rate with increases of 0.3% a year, is increased under the bill as follows:

[Tax rate (%)]

	Calendar year				
	1986	1987	1988	1989	1990
Current law	2.0	2.3	2.6	2.9	3.2
Proposed rate	4.3	4.7	6.0	2.9	3.2

The bill also extends the RRUI Account's authority to borrow from the Railroad Retirement Account, effective October 1, 1985. Under the bill, an automatic surcharge of 3.5 percent on an annual wage base of $7,000 will be levied if the RRUI Account has to borrow from the retirement account. The surcharge will be used to repay such loans.

Also, effective January 1, 1986, a portion of the tier 2 railroad retirement tax on employees equal to one percent of the payroll subject to the tax is directed under the bill from the railroad retirement account to the railroad unemployment insurance account. These revenues would then be returned to the railroad retirement account to help repay the loans (plus accumulated interest) which the railroad retirement account made to the unemployment account in the past. The diversion will end on April 1, 1990.

Effective date.—These provisions are effective October 1, 1985, except as otherwise noted above.

14. Termination of Repayable Advances to Black Lung Disability Trust Fund

Present law.—A manufacturers excise tax is imposed on domestically mined coal (other than lignite) that is sold or used by the producer of the coal. The rate of tax is $1 per ton for coal from underground mines and 50 cents per ton for coal from surface mines, but the tax cannot exceed four percent of the price for which the coal is sold.[7]

Status of Black Lung Disability Trust Fund.—The following table shows the receipts and expenses (in millions of dollars) of the Black Lung Disability Trust Fund for fiscal years 1978–1984.

	[393] Receipts			Expenses		
Fiscal year	Coal excise tax	Interest	Advances from general fund (deficit)	Benefit payments	Administrative expenses	Interest on advances
1978	92.1	1.2	18.9	76.8	35.3	....
1979	221.6	.1	400.8	582.0	32.1	7.7
1980	272.3	....	535.8	721.7	34.2	52.5
1981	236.6	....	554.8	644.3	35.6	109.5
1982	490.7	.3	283.0	578.2	35.8	160.6
1983	493.7	.3	357.8	623.1	34.8	193.3
1984	518.5	.4	346.1	594.2	36.6	234.5
Total	2,325.5	2.3	2,497.2	3,820.5	244.6	748.1

Source: Fourth Annual Report on the Financial Condition and Results of Operations of the Black Lung Disability Trust Fund (Department of Treasury, Sept. 30, 1981) and Budget of the U.S. Government Appendixes for fiscal years 1984, 1985, and 1986.

At the end of the fiscal year 1984, the Trust Fund had a cumulative deficit of approximately $2.5 billion; this amount represents advances from the general revenues which are repayable with interest. The Department of Labor estimates that, under present law, this deficit could reach $30 billion by 2010.[8]

Reasons for change.—The committee is concerned with the growing total of general revenue advances to the Black Lung Disability Trust Fund, which aggregated $2.5 billion at the end of fiscal 1984.

The committee, in its version of the Black Lung Benefits Revenue Act of 1981 (S. 1957, 97th Cong.), had included a provision to terminate the borrowing authority of the Trust Fund after fiscal year 1985, in light of the doubling of the coal excise tax which the committee had approved as part of that bill. The Department of Labor had projected that the "temporary" doubling of the excise tax in 1981, together with changes recommended by DOL in the program's eligibility standards, would eliminate the need for advances from the Treasury after fiscal 1985. Instead, the current deficit is estimated by the Department of Labor to reach $30 billion by 2010.

The committee concluded that the Trust Fund is operating in a manner not anticipated or intended by the Congress, in that the level of expenditures continues to necessitate advances from general revenues with no reasonable prospect (according to DOL projections) of repaying principal and interest. Accordingly, the committee agreed to terminate the borrowing authority of the Trust Fund as of September 30, 1986. This delayed effective date will enable the Congress to examine the black lung benefit program and its financing.

Explanation of provision.—The bill terminates, as of September 30, 1986, the authorization under Code section 9501(c) of appropriations to the Black Lung Disability Trust Fund, as repayable advances, of such sums as from time to time are necessary to make the expenditures described in section 9501(d). Thus, no advance out of general revenues is to be made to the Trust Fund after September 30, 1986. Under the provision, the Trust Fund may not borrow prior to October 1, 1986 amounts to be used to make expenditures after September 30, 1986 or during post-1986 years.

The provision does not affect the automatic appropriation to the Trust Fund of amounts equal to the revenues collected from the coal excise tax and from certain excise taxes applicable with respect to black lung benefit trusts, either before or after October 1, 1986.

Effective date.—The provision is effective on the date of enactment. The section 9501(c) authorization would terminate as of September 30, 1986.

15. Certain Permanent Exemptions From the Federal Unemployment Tax Act

a. Remuneration paid to certain fishing boat crew members

Present law.—For purposes of social security taxes and income tax withholding, members of the crew on a boat in a fishing operation engaged in catching fish or other forms of aquatic animal life are considered to be self-employed if (1) their remuneration is a share of the boat's catch (or cash proceeds from the sale of a share of the catch and no other cash remuneration is provided), (2) their share depends on the amount of the boat's catch, and (3) the crew of the boat normally is made up of fewer than ten individuals. If these requirements are met, remuneration paid to these crew members is exempt from the Federal Insurance Contributions Act (FICA) tax and income tax withholding, and is subject to the Self-Employment Contributions Act (SECA) tax (Code secs. 3121(b)(20), 3401(a)(17), and 1402(c)(2)(F)).

Prior to the Economic Recovery Tax Act of 1981 (ERTA), remuneration paid to fishing boat crew members generally was exempt from tax under the Federal Unemployment Tax Act (FUTA), except that the exemption did not apply with respect to the services performed in connection with catching halibut or salmon for commercial purposes or services performed on a vessel of more than ten net tons (sec. 3306(c)(17)).

Section 822 of ERTA amended the definition of employment for purposes of FUTA taxes to exempt from FUTA taxes remuneration paid during 1981 to fishing boat crew members who were treated as self-employed for social security tax purposes and thus exempt from FICA (sec. 3306(c)(18)). Section 203 of the Miscellaneous Revenue Act of 1982 (P.L. 97–362) amended ERTA to provide that the exemption from FUTA taxes also was effective for remuneration paid in 1982.

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[7] On the earlier of January 1, 1996, or any January 1 after 1981 on which there is no balance of repayable advances to the Trust Fund and no unpaid interest on such advances, the tax rates are scheduled to return to the pre-1982 rates, which were one-half the current rates (i.e., 50 cents/ton for underground mines and 25 cents/ton for surface mines, limited to two percent of the price for which the coal was sold).

[8] Testimony of Susan Meisinger, Deputy Undersecretary for Employment Standards, Department of Labor, before the House Committee on Ways and Means, June 19, 1985.

Section 1074 of the Deficit Reduction Act of 1984 (P.L. 98–369) extended the exemption from FUTA for remuneration paid to fishing boat crew members who are exempt from FICA to remuneration paid in 1983 and 1984.

[395] *Reasons for change.*—For reasons of simplicity and administrative convenience, the committee believes that fishing boat crew members who are treated as self-employed for purposes of the social security and income tax withholding should also be treated as self-employed for purposes of the unemployment tax. The committee believes that experience with this FUTA exemption since 1981 supports making the exemption permanent.

Explanation of provision.—The FUTA exemption relating to remuneration paid to certain fishing boat crew members, first enacted in section 822(b) of ERTA, is made permanent. Therefore, fishing boat crew members who are treated as self-employed for social security tax and income tax purposes are also to be treated as self-employed for purposes of the Federal Unemployment Tax Act. The bill also provides that spouses or children employed by such a fishing boat crew member (who is their spouse or parent) are not subject to the SECA tax.

Effective date.—The amendments made by the provision apply to remuneration paid after December 31, 1980.

b. *Remuneration paid to certain camp counselors*

Prior law.—In section 276(b) of the Tax Equity and Fiscal Responsibility Act of 1982 (P.L. 97–248), the Congress enacted a one-year FUTA exemption for remuneration paid to full-time students for employment by certain summer camps.

Reasons for change.—The committee believes that work performed by a full-time student in a summer camp does not involve the kind of employment relationship that should be covered by the unemployment insurance system. Therefore, the committee believes that wages paid for such employment should not be taxable under the Federal unemployment compensation law.

Explanation of provision.—The exemption from FUTA set forth in section 276(b) of P.L. 97–248 is reinstated on a permanent basis.

Effective date.—The provision applies to remuneration paid after September 19, 1985.

c. *Remuneration for services of certain nonresidential farmworkers*

Present law.—FUTA generally applies to remuneration paid by farm operators who employ 10 or more agricultural workers in 20 weeks, or have a quarterly payroll for agricultural services of at least $20,000. However, an exemption applies for wages paid for agricultural labor performed by aliens admitted to the United States pursuant to sections 214(c) and 101(a)(15)(H) of the Immigration and Nationality Act (Code sec. 3306(c)(1)(B)). This exemption from FUTA is scheduled to expire on December 31, 1985.

Reasons for change.—Sections 214(c) and 101(a)(15)(H) of the Immigration and Nationality Act pertain to residents of foreign countries who do not intend to abandon such residency and who are admitted to the United States to work for a temporary period of time during peak agricultural crop seasons. They are admitted only after the Secretary of Labor has determined and certified to the Secretary of State and to the Attorney General that there are not sufficient workers in the United States who are available to do the specific work the nonresident workers are admitted to perform. These farmworkers return to their countries and, therefore, are not able to collect unemployment compensation to which they might be entitled as a result of their employment in the United States. [396] Accordingly, the committee believes that remuneration paid to such workers should not be subject to unemployment taxes.

Explanation of provision.—The bill makes permanent the FUTA exemption in Code section 3306(c)(1)(B) for remuneration paid to certain alien farm workers.

Effective date.—The provision is effective on enactment.

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[397] *18. Limitations on Awarding of Court Costs and Certain Fees Modified*

Present law.—Under present law, a taxpayer who prevails over the Federal Government in a civil tax action in the U.S. Tax Court, the U.S. Claims Court, or any other Federal court may be awarded reasonable litigation costs, including attorneys' fees, at the discretion of the court (Code sec. 7430). An award is available only if the taxpayer shows that the position of the Government in the case was unreasonable. The amount of the award may not exceed $25,000.

Section 7430 was enacted in the Tax Equity and Fiscal Responsibility Act of 1982, effective for proceedings commenced after February 28, 1983. Under present law, the provision will not apply to tax proceedings commenced after December 31, 1985.

Reasons for change.—The committee believes that the Code provision allowing awards of court costs and fees in certain circumstances should be continued, with modifications intended to carry out more effectively the objectives of the provision and to achieve greater conformity with statutory provisions governing awards of court costs and fees in Federal nontax cases.

Explanation of provision.—The bill makes permanent the authorization of court costs and fees under Code section 7430, and makes the following modifications to that provision:

(1) Where it is determined that the taxpayer prevailed in litigation, the burden of proof in an awards request rests on the Federal Government to show that its position was substantially justified or that special circumstances exist which make an award of litigation costs unjust;

(2) The "substantially justified" standard is applicable to the administrative action or inaction by the Federal Government upon which such proceeding is based;

(3) No award is allowed to a prevailing party who unreasonably protracted the proceedings; and

(4) The $25,000 cap is eliminated.

Also, the bills limits the amount recoverable as attorneys' fees to $75 per hour unless the court determines that a higher rate is justified on the basis of an increase in the cost of living, or special [398] factors such as the limited availability of qualified attorneys for the particular proceeding.

As under present law, only reasonable litigation costs are recoverable by the taxpayer. The bill specifies that prevailing market rates are to be applied to determine reasonable attorneys' fees, reasonable expenses of expert witnesses, and reasonable costs of any study, analysis, or other project necessary for the preparation of the taxpayer's case. The bill also provides that amounts awarded for expert witness fees cannot exceed the highest rate of compensation for expert witnesses paid by the Federal Government.

Effective date.—The modifications to section 7430 apply to actions commencing after December 31, 1985.

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Conference Report No. 99–453
1st Session
[Bracketed numerals indicate official report page numbers]

CONSOLIDATED OMNIBUS BUDGET RECONCILIATION ACT OF 1985

December 19, 1985

Mr. Gray of Pennsylvania, from the committee on conference, submitted the following conference report to accompany H.R. 3128[1]

The committee of conference on the disagreeing votes of the two Houses on the amendment of the House to the amendment of the Senate to the text of the bill (H.R. 3128) to make changes in spending and revenue provisions for purposes of deficit reduction and program improvement, consistent with the budget process, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the Senate recede from its disagreement to the amendment of the House and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the House amendment insert the following: *SHORT TITLE*

Section 1.—This Act may be cited the "Consolidated Omnibus Budget Reconciliation Act of 1985".

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[561] Title X— Continued Health Coverage

a. Employers required to provide continuation coverage; sanction for noncompliance

Present law

There is no requirement in the Internal Revenue Code or other Federal law that an employer-provided group health plan must include continuation or conversion options in order for favorable tax rules to apply or in order to comply with other statutory requirements.

House bill

H. R. 3128—Covered Employers—The bill amends the Internal Revenue Code to require that an employer-provided group health plan must provide continuation coverage for qualified beneficiaries. Although the bill includes no explicit exclusions for churches, or tax-exempt or governmental employers, the applicable sanction—denial of the employer's tax deduction—has no impact on such employers.

H. R. 3500—This bill amends the Employee Retirement Income Security Act (ERISA), rather than the Internal Revenue Code, to cover all employee welfare benefit plans. Although the bill includes no explicit exclusions for churches or governmental employers, its amendment of ERISA effectively excludes churches (but not other tax-exempt entities), as well as Federal, State and local governments.

[562] *Sanction for Noncompliance*—If any group health plan maintained by an employer fails to provide continuation coverage, H.R. 3128 denies a tax deduction for employer contributions to any health plan; and H.R. 3500 permits employees, beneficiaries and the Secretary of Labor to sue the employer to enforce compliance. In addition, an employer may be liable under ERISA for certain monetary penalties.

Senate amendment

Covered Employers—Title VII of the Senate amendment generally follows H.R. 3128 by amending the Internal Revenue Code although it does include tax-exempt employers because of the additional sanction imposed on highly compensated employees. However, this provision of the Senate amendment provides explicit exclusions for churches, Federal, State, and local governments and small employers. For this purpose, a small employer is defined as an employer that normally employs 25 or fewer employees.

Title IX of the Senate amendment amends the Public Health Services Act to require that each employer subject to the Fair Labor Standards Act must provide continuation coverage. This title provides explicit exclusions generally following Title VII of the Senate amendment. Despite the exclusion, no State or political subdivision with more than 25 employees could receive Federal funds under certain public health service programs unless plans maintained by such entities provide continuation coverage.

Sanction for Noncompliance—In addition to following H.R. 3128, Title VII of the Senate amendment denies an income exclusion to any highly compensated employee. An employee is considered highly compensated if the employee is one of the 5 highest paid officers, a 10-percent shareholder, or among the highest paid 25 percent of all employees.

Title IX generally permits suits for injunctive relief and imposes civil penalties on employers who fail to provide continuation coverage.

Conference agreement

Covered Employers—The conference agreement generally follows the House bill and the Senate amendment, by amending ERISA, the Code, and the Public Health Service Act. Under the agreement, the changes to the Code and ERISA do not apply to churches, Federal, State and local governments, and small employers. Small employers are defined as those with fewer than 20 employees. In addition, the amendments to the Public Health Service Act apply only with respect to State and local governments (other than those with fewer than 20 employees.)

To avoid the issuance of duplicate and perhaps inconsistent regulations, the conferees authorized the Secretary of Labor to promulgate regulations implementing the disclosure and reporting [563] requirements, and the Secretary of the Treasury to issue regulations defining required coverage, deductions, and income inclusions. The Secretary of Health and Human Services is to issue regulations regarding the requirement that State and local governments provide continuation coverage for qualified beneficiaries. The conferees intend that any regulations issued by the Secretary of Health and Human Services will conform (in terms of actual requirements) with those regulations issued by the Secretary of the Treasury and Labor. Under the agreement, enforcement of the requirements imposed through the Public Health Service Act will be through suits for equitable relief filed by qualified beneficiaries. Of course, as under present law, all affected agencies will have the opportunity to comment before regulations are issued.

Sanctions for Noncompliance—Any regulations issued pursuant to these changes are to be effective after the date of issuance. However, pending the promulgation of regulations, employers are required to operate in good faith compliance with a reasonable interpretation of these substantive rules, notice requirements etc.

The conference agreement generally follows H.R. 3500 and the Senate amendment except that the only sanction imposed on covered State and local governments under the Public Health Service Act are suits for equitable relief.

b. Required coverage

Present law Otherwise deductible expenses paid or incurred by an employer for a group health plan are disallowed if the plan differentiates in benefits between individuals having end stage renal (kidney) disease and other individuals (Code sec. 162(i)).

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[1] Public Law 99–272, page 4.

House bill

Qualified beneficiaries—Both H.R. 3128 and H.R. 3500 provide that qualified beneficiaries include widows, divorced spouses and persons whose spouse becomes eligible for Medicare, as well as dependent children of such beneficiaries.

Type of benefit coverage

House bill Both H.R. 3128 and H.R. 3500 require that the continuation coverage for which a qualified beneficiary must be offered an election is coverage identical to the coverage provided under the plan to similarly situated beneficiaries.

Period of coverage—Both H.R. 3128 and H.R. 3500 require that continuation coverage be provided for 5 years. However, no coverage need be provided [564] after the qualified beneficiary becomes eligible for coverage under another plan as a result of reemploymernt or remarriage.

Cost of coverage—Both H.R. 3128 and H.R. 3500 provide that some or all of the cost of continuation coverage could be charged to the qualified beneficiary, whether or not the employer otherwise subsidizes some or all of the premiums for covered employees. However, in no event may the cost charged to the qualified beneficiary exceed the total applicable premium. The applicable premium is defined as the cost to the plan for the period of coverage for a similarly situated beneficary with respect to whom a qualifying event has not occurred (without regard to whether such cost is paid by the employer or employee).

Senate amendment

Qualified beneficiaries—In addition to those classes of qualified beneficiaries described in the House bill, Title VII of the Senate amendment provides that (1) employees are qualified beneficiaries upon termination of employment (voluntary and involuntary) and (2) dependent children are also separately considered to be qualified beneficiaries when they cease to be covered as dependents under the plan.

Title IX of the Senate amendment further expands the classes of qualified beneficiaries listed to include employees whose hours are reduced, resulting in a loss of coverage. It provides that no coverage is required for employees who are terminated for cause.

Title VII of the Senate amendment requires that the continuation coverage for which a qualified beneficiary must be offered an election is coverage identical to the coverage provided immediately before the qualifying event. In addition, if the plan otherwise permits employees and beneficiaries to modify coverage, the qualified beneficiary must be entitled to modify coverage, the qualified beneficiary must be entitled to modify coverage at the same time and in the same manner as other similarly situated beneficiaries.

Title IX of the Senate amendment follows the House bill.

Duration of coverage—Title VII of the Senate amendment provides that continuation coverage must be provided for 18 months.

Title IX of the Senate amendment provides that continuation coverage must be provided for 3 years (18 months with respect to terminated employees and reduced hour workers), and provides cutoff dates similar to those in the House bill.

Cost of coverage—Although Title IX of the Senate amendment follows the House bill, Title VII provides that the cost must not exceed 102 percent of the applicble premium and provides specific rules for calculating the "cost" of the applicable premium in self-insured plans.

[565] Conference agreement

Qualified Beneficiaries—The conference agreement generally follows the House bill and the Senate amendment except that no continuation coverage is required for terminated employees if the termination occurs by reason of the employee's gross misconduct.

Type of benefit coverage—The conference agreement generally follows the House bill with a modification so that the type of benefit coverage is identical, as of the time the coverage is being provided, to the coverage provided under the plan to similarly situated beneficiaries under the plan with regard to whom a qualifying event has not occurred.

Duration of Coverage—The conference agreement generally follows Title IX of the Senate amendment, requiring that continuation coverage provided to widows, divorced spouses, spouses of Medicare-eligible employees, and dependent children who become ineligible for coverage under the plan be provided for 3 years, while coverage for terminated employees and employees with reduced hours must be provided for 18 months. The agreement provides that the coverage period begins with the date of the qualifying event. As under the House bill and Title IX of the Senate amendment, no coverage need be provided after (1) failure to make timely payment under the plan, (2) the qualified beneficiary is covered under another group health plan as a result of employment, reemployment, or remarriage, and (3) the qualified beneficiary becomes entitled to Medicare benefits. In addition, as under the House bill and Title VII of the Senate amendment, no coverage need be provided after the employer ceases to maintain any group health plan.

Cost of Coverage—The conference agreement generally follows Title VII of the Senate amendment. For a self-insured plan, the conferees agreed that the "applicable" premium for any year generally is equal to a reasonable estimate of the cost of providing coverage for such period for a similarly situated beneficiary. The cost is to be determined on an actuarial basis and takes into account such factors as the Secretary may prescribe in regulations. Alternatively, unless there has been a significant change affecting a self-insured plan (e.g., a modification of covered benefits, a significant change in the number or composition of the covered workforce, etc.), the employer may elect to use as the applicable premium, the cost for a similarly situated beneficiary for the preceding year, adjusted to reflect cost-of-living increases as measured by the GNP deflator.

In general, similarly situated individuals are those individuals defined by the plan (consistent with Treasury regulations) to be similarly situated and with respect to which no qualifying event has occurred. The Secretary of the Treasury is to define similarly situated individuals by taking into account the plan under which the coverage is provided (e.g., high or low option), the type of coverage (single or family coverge) and, if appropriate, regional differences in health costs. The conferees do not intend that similarly situated mean medically identical (for example, all employees with heart problems); nor do the conferees intend that plans can define similarly situated beneficiaries by reference to classifications that are in violation of Title VII of the Equal Pay Act.

In addition, the conferees intend that Treasury regulations defining a plan should preclude an employer from grouping employees to inappropriately increase the cost of continuation coverage for qualified beneficiaries who are rank-and-file employees (or their beneficiaries).

c. Notice requirements; election period

Present law

No provision.

House bill

Both H.R. 3128 and H.R. 3500 require that notice of the option to continue health coverage be provided in the summary plan description. In addition, the bills require that notice of a qualifying event be given to the plan administrator (1) by the employer, in the event of the employee's death; (2) by the employee, in the event that the employee is divorced, separated, or becomes eligible for Medicare.

Under both bills, the period during which a qualified beneficiary may elect continuation coverage does not expire before 60 days after the later of (1) the termination date of coverage, or (2) the date the beneficiaries receive notice of the right to elect.

Senate amendment

Title VII of the Senate amendment provides that the Secretary of the Treasury is to prescribe notice requirements pursuant to regulations and establishes a 60-day notice period commencing with the qualifying event.

Title IX

Title IX of the Senate amendment provides that the Secretary of Health and Human Services is to prescribe notice requirements pursuant to regulations. Such regulations are to prescribe notice consistent with that required by the House bill.

Conference agreement

The conference agreement generally follows the House bill. Thus, notice of the option to continue health coverage must be provided in the summary plan description. In addition, in the event of an employee's death, separation from service, or Medicare eligibility, the employer is required to notify the plan administrator within 30 days of the qualifying event who will in turn notify the qualified beneficiary within 14 days.

In the event of other qualifying events (e.g., divorce, legal separation, or the child's becoming ineligible) the employee or qualified beneficiary affected by that event is required to notify the plan administrator. Unless the qualified beneficiary is the party providing notice, the plan administrator is in turn required to notify the qualified beneficiary. The election period begins not later than the later of (1) the date on which coverage terminates, or (2) the date on which the qualified beneficiary receives notice of the right to elect continuation coverage. Any election by a qualified beneficiary is con sidered an election by other qualified beneficiaries who would otherwise lose coverage by reason of the same qualifying event.

The conferees intend that the Secretary of Labor will issue regulations defining what notice will be adequate for this provision. The conferees intend that notice by mail to the qualified beneficiary's last known address is to be adequate; however, mere posting is not to be adequate. In addition, in applying these requirements to multiemployer plans, the conferees intend the the Secretary of Labor should take into account the special problems faced by those plans.

d. Conversion option

Present law

No provision.

House bill

Both H.R. 3128 and H.R. 3500 require that a conversion option be offered to qualified beneficiaries if under the plan the conversion option is otherwise available.

Senate amendment

Although Title IX of the Senate amendment follows the House bill, Title VII does not require that a conversion option be offered.

Conference agreement

The conference agreement generally follows the House bill and Title IX of the Senate amendment. Under the agreement, a qualified beneficiary must be offered a conversion option from any plan (including a self-insured plan) only if such an option is otherwise available under the plan to other participants.

Effective Date.—These provisions are effective for plan years beginning after June 30, 1986. In the case of a group health plan maintained pursuant to one or more collective bargaining agreements, the bill does not apply to plan years beginning before the later of (1) the date the last of the collective bargainning agreements terminate, or (2) January 1, 1987.

Title XI.—Pension Benefit Guaranty Corporation Provision

1. Insurance Premiums

Present law

A private defined benefit provision plan must generally pay to the Pension Benefit Guaranty Corporation ("PBGC") an annual [568] perparticipant premium of $2.60. The Employee Retirement Income Security Act of 1974 (ERISA) permits the PBGC to provide for a risk-related premium (within limits).

House bill—H.R. 3128.

The premium is increased to $8.00 for plan years beginning after December 31, 1985, and before January 1, 1989. For plan years beginning after December 31, 1988, the premium level returns to $2.60. The bill also provides for a study by the Treasury Department with respect to risk-related premiums.

House bill—H.R. 3500

The premium is increased to $8.50 for all plan years beginning after December 31, 1985.

Senate amendment—Title VII

The premium is increased to $8.10 for all plan years beginning after December 31, 1985. The bill also provides for a study by the Department of Labor (DOL) with respect to risk-related premiums.

Senate amendment—Title IX

No provision.

Conference agreement

The conference agreement follows H.R. 3500 except that the conferees agreed generally to require the PBGC to study the premium structure (including the feasibility of a risk-related premium) and make recommendations for change, if necessary. An advisory group appointed by the Chairman of the House Committees on Education and Labor and Ways and Means and the Senate Committees on Labor and Human Resources and Finance is required to analyze and critique the study. The study is to be filed with the Congress no later than one year from the date of enactment and the advisory group's report is due no later than six months after the PBGC submits its report to the Advisory Council.

2. Single Employer Pension Plan Amendment Act

a. Clarification of authority to freeze plans

Present law

Under present law, a plan may be amended to freeze future benefit accruals and to freeze other factors used to calculate benefits, such as compensation taken into account. In the absence of a contractual obligation, an employer is not required to provide participants with advance notice of a freeze.

House bill—H.R. 3128

No provision.

[569] House bill—H.R. 3500

Under the bill, an amendement freezing accruals is not effective unless, subsequent to the adoption of the amendment and at least 60 days prior to the effective date of the amendment, the plan administrator gives written notice to each affected party. The term "affected party" is defined under the bill as each participant in the plan, each beneficiary of a deceased participant, each beneficiary who is an alternate payee under a qualified domestic relations order, and each employee organization representing participants in the plan and the PBGC.

Senate amendment—Title VII

No provision.

Senate amendment—Title IX

Although the bill contains no specific provisions covering plan freezes, the proposed first stage of plan termination covers similar situations (see Voluntary plan terminations—Senate amendment).

Conference agreement

The conference agreement provides that an amendment to reduce significantly future benefit accruals under a plan is not effective unless, subsequent to the adoption of the amendment and at least 15 days prior to the effective date of the amendment, the plan administrator gives written notice of the reduction of each participant in the plan, each beneficiary under the plan who is beneficiary of a deceased participant, each beneficiary who is an alternate payee under a qualified domestic relations order, and each employee organization representing participants in the plan. This notice does not apply to any amendment (or portion thereof) to retroactively reduce plan benefits (Sec. 412(c)(8) of the Code and Section 302(c)(8) of ERISA).

The conference agreement does not affect the requirements for qualification of a plan under the Code. For example, the agreement does not change the requirement of minimum benefit accruals under a frozen top-heavy plan.

b. Voluntary plan terminations

Present law

Restrictions on plan termination.—Under present law, an employer's continued maintenance of a defined benefit pension plan is not required by statute. Thus, subject to contractual obligations, the employer generally may terminate a plan at any time upon satisfaction of the procedural requirements described below.

Employer liability under a terminated plan.—If a single-employer defined benefit pension plan is terminated with assets sufficient to pay benefits at the level guaranteed by the PBGC (described below), the employer has no further liability to the PBGC.

If a single-employer defined benefit pension plan is terminated with insufficient assests to pay benefits at the level guaranteed by the PBGC, then the employer is liable to the PBGC for the insufficiency. However, the employer's liability is limited to 30 percent of [570] the employer's net worth (determined as of date of termination). The 30-percent limit applies whether or not the employer remains in business after the plan is terminated. All trades or businesses under common control are treated as a single employer.

In computing the extent to which assets are insufficient to pay guaranteed benefits, the value of any accumulated funding deficiency or outstanding waived liability under the minimum funding standard of the plan (discounted for likelihood of payment) is treated as a receivable of the plan and, thus, as a plan asset. An employer' liability for amounts due to the plan under the minimum funding standards of ERISA is not limited to 30 percent of net worth.

The full amount of the employer's liability to the PBGC is generally due and payable as of the date of plan termination. However, the PBGC, in its descretion, may grant deferred payment terms for employer liability.

PBGC guaranteed benefits.—Subject to limits, the PBGC guaranteed basic benefits under a plan. Basic benefits consist of nonforfeitable retirement benefits other than those benefits that become nonforfeitable solely on account of the termination of the plan. Guaranteed benefits are limited to basic benefits of $750 per month adjusted for inflation since 1974 ($1,687.50 for 1985).

Guarantees do not apply with respect to benefits in effect for fewer then 60 months at the time of plan termination unless the PBGC finds substantial evidence that the plan was terminated for a reasonable business purpose and not for the purpose of securing increased guaranteed benefits for participants. In cases in which they apply, guaranteed benefits are phased in at the rate of $20 per month or 20 percent per year (whichever is greater) for (1) basic benefits that have been in effect for less than 60 months at the time the plan terminates, or (2) any increase in the amount of basis benefits under a plan resulting from a plan amendment within 60 months before the date of the plan termination.

Notice of termination.—Under present law, an employer must file a Notice of Intent to Terminate (NOIT) a plan with the PBGC not less than 10 days prior to the proposed date of termination. Participants and beneficiaries must be notified of the termination no later than the date that the NOIT is filed with the PBGC.

Distribution.—Under present law, at least 30 days prior to the proposed date of distribution, the plan administrator must submit projected asset and liability data demonstrating that the plan holds sufficient assets to pay guaranteed benefits as of the propose date of distribution. Under certain circumstances, the plan administrator also has the option of establishing the plan's sufficiency by certification of an enrolled actuary.

Within 90 days after the proposed termination date, the PBGC is to notify the plan administrator as to whether plan assets are sufficient to satisfy plan obligations. This period may be extended by mutual agreement of the plan administrator and the PBGC. The plan administrator may distribute plan assets 30 days after the notice of sufficiency is issued. If the PBGC fails to issue a notice of sufficiency during the 90-day statutory period and the

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[1] Note: H.R. 3500 as passed by the House was added as an amendment to H.R. 3128 as amended by the Senate. The PBGC provisions of both H.R. 3128 and H.R. 3500 as passed by the House are mentioned separately to indicate the legislative background of the separate House bill provisions.

parties fail to agree to extend the 90-day period, the employer may distribute plan assest upon the expiration of the 90-day period.

[571] *Post-distribution audit.*—Within 60 days of the date of distribution, the plan administrator must certify to the PBGC that plan assets have been allocated and distributed in accordance with the requirements of ERISA. The PBGC may, in its discretion, conduct a post-distribution audit of a terminated plan.

House bill—H.R. 3128

Restrictions on plan termination.—No provision.

Employer liability upon plan termination.—Unless the employer terminating a plan goes out of business, the employer is liable to the PBGC for (1) the full amount of any funding deficiency, plus (2) the full amount of any unfunded guaranteed benefits (determined by treating any funding deficiency as an available plan asset of the terminated plan). A funding deficiency consists of any accumulated funding deficiency and the outstanding balance of any waived funding deficiency. If an employer goes out of business, its liability for the unfunded guaranteed benefits described in (2) is limited to 30 percent of the employer's net worth.

The bill also provides that the liability of an employer to the PBGC upon plan termination is the joint and several liability of all members of the controlled group of the employer. "Controlled group" is defined as all persons who are treated as a single employer under subsections (b), (c), (m) or (o) of section 414 of the Internal Revenue Code ("Code").

The bill generally provides that the full amount of the liability to the PBGC is normally due and payable as of the date of plan termination, unless the employer elects a deferred payment schedule. An employer may pays it liability to the PBGC (1) in a lump sum payment, (2) over a period of five years, or (3) over a period of 15 years. If the employer elects deferred payments over a 5- or 15-year period, liability payments include interest. Security is required in the 15-year schedule is elected and can be required if the 5-year schedule is elected. In addition, as under present law, the employer and the PBGC may agree to a special schedule of payments. The schedule may, for example, reflect the ability of the employer to pay the liability, as well as the hazards of litigation.

Procedural requirements.—No provision.

House bill—H.R. 3500

Restrictions on plan termination.—Under the bill, an employer may only terminate a single-employer defined benefit pension plan under which benefits are guaranteed by the PBGC in a "standard termination" or in a "distress termination." A standard termination is permitted only if the plan holds assets sufficient to pay all benefit entitlements.

Under the bill, "benefit entitlements" include all guaranteed benefits and all benefits that would be guaranteed but for the insurance limits on the amount or value of the benefit, or the length of time that the benefit has been in effect. In addition, benefit entitlements include certain addition benefits for which a participant has satisfied all conditions of entitlement prior to termination, irrespective of whether those benefits are guaranteed. These additional benefits are (1) early retirement supplements or subsidies, (2) plant closing benefits, and (3) death benefits. The general definition of [572] benefit entitlements excludes those benefits have become nonforfeitable solely by virtue of the plan's termination.

A plan with assests insufficient to provide benefit entitlements may be terminated in a "distress termination" only if the PBGC determines that (1) funding waivers have been granted with respect to the termination date, and such a waiver has been granted to each other single employer plan maintained by each contributing sponsor (as that term is defined in the bill) of the terminating plan and each substantial member (as defined in the bill) of each contributing sponsor's controlled group in any one of the three plan years preceding the termination date; (2) a petition has been filed in bankruptcy or state insolvency proceedings seeking liquidation of each contributing sponsor of the plan and each substantial member of their controlled groups, and has not been dismissed or converted to a petition for reorganization; (3) unless a distress termination occurs, each contributing sponsor of the plan and each substantial member of each contributing sponsor's controlled group will be unable to pay its debts when due and will be unable to continue in business; or (4) as a result of the decline in the number of employees covered as participants under all of the plans maintained by the contributing sponsor's controlled group, the costs of providing pension coverage have become unreasonably burdensome. The bill contains an objective test of "burdensomeness" relating to plan costs, payroll costs, and gross income level of contributing sponsors and members of their controlled groups.

Employer liability under a terminated plan.—If an employer terminates a plan pursuant to a standard termination, with assets sufficient to fund all benefit entitlements, the employer has no further liability to the PBGC or plan participants.

Liability to the PBGC.—If a plan is terminated pursuant to a distress termination (or if the termination is instituted by the PBGC), each contributing sponsor of the plan and each member of the controlled group of a contributing sponsor is jointly and severally liable to the PBGC for (1) any unfunded guaranteed benefits, plus (2) the full amount of any funding deficiency. A funding deficiency consists of any accumulated funding deficiency and the balance of any waived funding deficiency.

Under the bill, the full amount is normally due and payable to the PBGC as of the date of plan termination. However, where the amount of unfunded guaranteed benefits exceeds 30 percent of the collective net worth of the persons subject to liability, liability for the excess amount may be satisfied by payments to the PBGC each year, over a 10-year period (specified in the bill) following the plan's termination. The required payment in any year is 10 percent of the sum of the individual annual pretax profits (if any) of all persons subject to liability in connection with the plan termination. Liability to the PBGC ceases after the earlier of the tenth annual payment or the time when the liability to the PBGC is paid in full.

Liability to participants.—If a plan has assets insufficient to fund nonguaranteed benefit entitlements, each contributing sponsor to the plan and each member of the contributing sponsor's controlled group is jointly and severally liable for payments for a 10-year [573] period (specified in the bill) following the plan's termination, of 5 percent of the sum of the individual annual pretax profits (if any) of all persons subject to liability in connection with the plan termination. They payments are to be made to a special trustee appointed by the PBGC. Employer liability to the special trustee ceases after the earlier of the tenth annual payment or the time when the nonguaranteed benefits are fully funded. The special trust makes benefit payments to participants and beneficiaries.

Notice of termination.—Not less than 60 days prior to a proposed plan termination date, a plan administrator is required to give written notice of the proposed termination to the PBGC, plan participants and beneficiaries and unions representing the participants.

Related adjudicatory proceeding.—If, during the period between the date notice is given and the proposed termination date, the plan administrator learns of a "related adjudicatory proceeding" (as defined in the bill), the plan administrator is required to suspend the termination or to structure the termination so that the plan could be restored if it were later determined that the termination violated the contractural or statutory right of any affected person. The payment of benefits is restricted during the suspension period.

Distribution.—As soon as practicable after the proposed termination date, the plan administrator is required to provide the PBGC with certification by an enrolled actuary of the plan's sufficiency as of the plan's proposed date of distribution.

The plan administrator is permitted to distribute plan assets upon the expiration of the 60-day period following the date the certification of sufficiency is filed with the PBGC, provided that the PBGC has not issued a notice of noncompliance with respect to the plan, and the parties have not agreed to extend that period. The plan administrator is also required to notify each participant and beneficiary of such person's benefit entitlement at least 60 days prior to the plan's proposed date of distribution.

Post-distribution audit.—The plan administrator is required, within 30 days after the final distribution of assests, to file a notice with the PBGC certifying that assets have been allocated and distributed in accordance with the requirements of ERISA.

Senate amendment—Title VII

No provision.

Senate amendment—Title IX

Restrictions on plan termination.—Under the bill, an employer may only terminate a single employer defined benefit pension plan under which benefits are guaranteed by the PBGC in a "standard termination" or in a "distress termination."

A standard termination consists of two distinct stages: (1) a cessation of accruals stage, and (2) a liquidation or "closeout" stage. If the plan has sufficient assets to fund all "final benefit obligations" of the plan, the two stages may occur simultaneously If assets are insufficient to fund final benefit obligations the plan may not complete the second stage until such obligations are fully funded or the plan qualifies for liquidation under the distress termination rules. [574] A plan in the first stage of termination is a frozen plan to which the present-law rules regarding vesting apply. The bill also provides that the required annual contribution, during the stage-one period, is an amount not less than benefits currently due.

Under the bill, final benefit obligations include all "benefit entitlements" as defined under H.R. 3500, plus (1) benefits which come nonforfeitable solely by virtue of the plan's termination, and (2) certain ancillary benefits for which a participant satisfies the conditions of entitlement subsequent to the plan's termination.

In order to terminate a plan in a distress termination, a plan administrator is required to demonstrate that (1) a petition in bankruptcy or other State insolvency proceedings has been filed seeking liquidation of each contributing sponsor (as defined in the bill) of the plan and each substantial member (as defined in the bill) of the contributing sponsors' controlled groups, and that the petition has not been dismissed or converted to one seeking reorganization; (2) a petition in a bankruptcy or State insolvency proceeding has been filed seeking reorganization of each contributing sponsor of the plan and each substantial member of their controlled groups, and the bankruptcy court has approved the plan termination; or (3) unless a distress termination occurs, each of the contributing sponsors and the substantial members of their controlled groups will be unable to pay its debts when due, and will be unable to continue in business.

Employer liability under a terminated plan.—These provisions of the bill are substantially the same as H.R. 3500, except that the contributing sponsors and members of their controlled groups are liable to plan participants for unfunded nonguaranteed "final benefit obligations" rather than benefit entitlements, and payment of those benefits is made directly by the employer to plan participants and beneficiaries, rather than through a special termination trust.

Notice.—Not less than 10 days prior to a "stage one" termination, a plan administrator is required to give written notice of the termination to the PBGC, plan participants and beneficiaries, and unions representing the participants.

Notice to the same parties is required at least 30 days prior to the second, closeout stage. If stages one and two occur simultaneously, the 30-day notice applies. In any event, if the plan is maintained pursuant to a collective bargaining agreement, the plan administrator is required to notify unions representing participants at least 30 days prior to a stage one freeze or a stage two closeout filing.

Related adjudicatory proceeding.—No provision.

Distribution.—At least 30 days prior to the distribution of plan assets, the plan administrator is required to provide the PBGC with certification by an enrolled actuary of the plan's sufficiency as of the plan's proposed date of distribution. The plan administrator is permitted to distribute plan assets upon the expiration of the 30-day period, provided that the PBGC has not issued during that period a notice of noncompliance with respect to the plan.

Notice of benefit computations to participants.—At the same time as the plan administrator notifies each participant or beneficiary of the benefits to which the participant or beneficiary is entitled, the plan administrator must also notify the participant or beneficiary [575] of the information used in computing the amount of such benefits, including (1) the length of service, (2) the age of the participant or beneficiary, (3) wages, and (4) such other information as the PBGC may require.

Post-distribution audit.—The PBGC is required to audit annually all participants in terminated plans after the final distribution of assets.

Conference agreement

The conference agreement generally follows the structure of H.R. 3500.

Restrictions on terminations.—Under the agreement, as under H.R. 3500, an employer may only terminate a single-employer defined benefit pension plan under which benefits are guaranteed by the PBGC in a standard termination or in a distress termination. An employer is permitted to terminate a plan in a standard termination only if the plan holds sufficient assets to pay all "benefit commitments" under the plan. Benefit commitments are defined under the conference agreement as all guaranteed benefits (including qualified preretirement survivor annuities) and all benefits that would be guaranteed but for the insurance limits on the amounts or value of the benefit, or the length of time that the benefit has been in effect. In addition, benefit commitments include certain additional benefits for which a participant has satisfied all conditions of entitlement prior to termination. These additional benefits, irrespective of whether they are guaranteed, are (1) early retirement supplements or subsidies, and (2) plant closing benefits.

With respect to the circumstances under which an employer may terminate a plan in a distress termination, the bill generally follows Title IX of the Senate amendment except that it provides an additional criteria permitting "distress" termination if pension costs become unreasonably burdensome due to a declining workforce. In addition, the conference agreement makes it clear that different members of a controlled group may separately satisfy different criteria for distress termination.

As under present law, to the extent a pension plan is an executory contract included within the scope of Section 365 (11 USC 365) or is included within the scope of Section 1113 of the Bankruptcy Code (11 USC 1113), these Bankruptcy Code Provisions are applicable to the court's decision on whether to approve the termination of the pension plan. The distress termination criteria are not intended to make any substantive changes in the bankruptcy laws. The conferees take no position on when or whether a pension plan is an executory contract.

Employer liability under a terminated plan.—Upon the termination of a plan, pursuant to a standard termination in which all benefit commitments are fully funded, the employer has no further liability to the PBGC or to plan participants.

Liability to PBGC.—Upon the termination of a plan pursuant to a distress termination, if the PBGC determines that plan assets are insufficient to fund guaranteed benefits, the PBGC is required to institute trusteeship proceedings for the plan. Each contributing sponsor of the plan and each member of the controlled group of each contributing sponsor is jointly and severally liable to the [576] PBGC for the sum of (1) the total amount of all unfunded guaranteed benefits, up to 30 percent of the collective net worth of those persons liable to the PBGC; (2) an amount equal to the excess (if any) of (a) 75 percent of the total amount of all unfunded guaranteed benefits over (b) the amount described in (1); and (3) interest on the amount due calculated from the termination date. The total amount of unfunded guaranteed benefits is computed by treating any accumulated funding deficiency and the balance of any waived funding deficiency as a receivable of the plan and, thus, as a plan asset.

The full amount of the liability to the PBGC is generally due and payable as of the date of plan termination. However, if the liability to the PBGC for unfunded guaranteed benefits exceeds 30 percent of the collective net worth of the parties that are liable to the PBGC, the payment of that excess amount is to be made under commercially reasonable terms prescribed by the PBGC. The parties are to make a reasonable effort to reach agreement on such terms. Under the conference agreement, any terms prescribed by the PBGC must provide for the deferral of 50 percent of any amount of liability otherwise payable for any year if the PBGC determines that no person subject to such liability has individual pretax profits for the fiscal year ending during such year.

If a plan terminates pursuant to a distress termination and is subject to PBGC trusteeship proceedings, then each contributing sponsor and each member of their controlled groups is liable to the PBGC for the sum of (1) the outstanding balance of any accumulated funding deficiency, and (2) the balance of the amount of any waived funding deficiencies. The full amount of such liability is due and payable to the PBGC as of the date of plan termination.

The conferees take no position with respect to the treatment in bankruptcy of PBGC claims and liens. Deletion of the amendments to section 4068 that appeared in S. 1730 is not intended to express any view on the meaning of the present language in section 4068. Section 4068 has been amended, however, to assure that it applies only to the liability that was covered by section 4068 prior to these amendments, i.e., the value of unfunded guaranteed benefits up to 30 percent of the employer's net worth. Section 4068 does not apply to liability being added to section 4062 by these amendments for amounts in excess of the 30 percent of net worth cap.

Liability to participants.—If the PBGC determines that there is an outstanding amount of benefit commitments, the PBGC is required to appoint a fiduciary with respect to the termination trust. The fiduciary must be independent of the contributing sponsors (and members of a controlled group including sponsors) and generally is subject to the fiduciary requirements of ERISA (other than the prohibited transaction rules). The "outstanding amount of benefit commitments" under a plan is defined as the excess of (1) the actuarial present value of the benefit commitments of each participant and beneficiary over (2) the actuarial present value of the benefits of each participant and beneficiary that are guaranteed by the PBGC or to which assets of the plan have been allocated under the distribution procedures of section 4044 of ERISA. Each contributing sponsor of the plan and each member of the controlled group of a contributing sponsor is jointly and severally liable to the [577] termination trust for the lesser of (1) 75 percent of the total amount of outstanding benefit commitments under the plan, or (2) 15 percent of the total amount of benefit commitments under the plan. The termination trust generally will be administered by the PBGC except in cases in which PBGC determines that delegation of this responsibility is cost effective.

Under the conference agreement, payment of liability is to be made under commercially reasonable terms prescribed by the fiduciary of the termination trust. The parties are required to make a reasonable effort to reach agreement on such terms. In addition, the conference agreement provides that if liability to the termination trust is less than $100,000, the payment of liability to the trust over 10 years in equal annual installments (with interest at the applicable rate determined under sec. 6621(b) of the Code) will satisfy this requirement even if the terms are not commercially reasonable. The PBGC is permitted to increase, by regulation, the $100,000 ceiling. To phase in this $100,000 rule, the conference agreement provides that no payment under this provision is required before January 1, 1989.

The conference agreement also provides that any payment schedule is to provide for the deferral of 75 percent of the liability otherwise payable to the termination trust for any year if no person subject to liability to the termination trust has any individual pre-tax profits for such person's fiscal year ending during such year. However, the conferees intend that the fact that one person has minimal profits should not make the benefits of deferral totally unavailable. The required payments in any year should not exceed 50 percent of the otherwise payable amount plus profits. The amount of liability so deferred is payable only after payment of any liability to the PBGC arising in connection with the terminated plan.

The conference agreement provides rules governing the allocation and distribution of assets of the termination trust to participants and beneficiaries.

Under the conference agreement, a participant or beneficiary who receives distributions from a termination trust is, subject to certain requirements, permitted to roll over the distributions to an IRA or qualified plan.

Deductibility of payments.—The conference agreement provides rules as to the deductibility of payments to the PBGC and the termination trust.

Notice.—The conference agreement follows H.R. 3500.

Related adjudicatory proceedings.—The conference agreement contains no provision dealing with related adjudicatory proceedings. However, the conference agreement provides that the PBGC is not to proceed with the voluntary termination of a plan if the termination would violate the terms and conditions of a collective bargaining agreement.

Distributions.—The conference agreement generally follows H.R. 3500. As under H.R. 3500, the conference agreement provides that the assets of a terminated plan may be distributed if the PBGC fails to issue a notice of noncompliance within 60 days after receipt of a NOIT. As under H.R. 3500, the conference agreement provides that the 60-day period may be extended by PBGC and the plan administrator and that the extension may be subject to conditions to [578] which they have agreed. The conference agreement does not change the rules of the Code for determining the qualified status of a plan (or of a trust forming a part of a plan), or the application of the minimum funding standard to a plan. Accordingly, the conference agreement does not authorize the PBGC to waive, or otherwise modify, the requirements of the Code.

Notice of benefit computations to participants.—The conference agreement generally follows Title IX of the Senate amendment except that, in adddition to the other information specified in the Senate amendment, the plan administrator must supply to participants and beneficiaries the actuarial assumptions used in computing plan benefits (including, but not limited to, the interest rate assumption).

Post-distribution audit.—The conference agreement generally follows H.R. 3500. In addition, under the conference agreement the PBGC is required to perform annually an audit of a statistically significant sample of terminated plans to determine whether participants and beneficiaries have received the benefits to which they are entitled. For each plan selected for audit, the benefits of a statistically significant sample of participants and beneficiaries are to be verified.

In addition, the conference agreement authorizes the Comptroller General of the General Accounting Office to examine certain plan documents. Any information gathered under this authority shall not be available to the public.

3. Involuntary plan termination

Present law

Under present law, the PBGC is permitted, but not required, to commence proceedings to terminate a plan under a variety of circumstances including the inability of the plan to pay benefits when due.

House bill—H.R. 3128

No provision.

House bill—H.R. 3500

Under the bill, the PBGC is required to commence termination proceedings if the plan does not have assets available to pay benefits that are currently due under the terms of the plan.

Senate amendment—Title VII

No provision.

Senate amendment—Title IX

As under present law, the PBGC is permitted, but not required, to terminate a plan under certain circumstances. In addition, the PBGC may appoint a temporary receiver if the plan fails to meet minimum funding requirements, is not able to pay current benefits when due, or has been abandoned.

Conference agreement

The conference agreement follows H.R. 3500.

[579] 4. Waiver of funding standard

Present law

Present law authorizes the Internal Revenue Service to waive the requirements of the minimum funding standard no more frequently than 5 times in any 15-year period. In addition, the amortization period for liabilities under defined benefit pension plans may be extended, and a waiver previously granted by the IRS may be modified.

The IRS may grant a waiver on condition that appropriate requirements are met.

House bill—H.R. 3128

The IRS is authorized to require that security be provided as a condition of granting a waiver of the minimum funding standard, an extension of an amortization period and modifications of a previously granted waiver. The IRS is required to notify the PBGC before granting a waiver and is to consider the comments of the PBGC. The PBGC has a 15-day comment period after the date of receipt of notice.

The new provisions apply to waivers, extensions, and modifications granted on or after the date of enactment of the bill.

House bill—H.R. 3500

The bill is similar to H.R. 3128, except that (1) a "reasonable period" rather than a 15-day comment period is provided, and (2) the security, notice, and comment provisions do not apply to cases involving less than $1 million of outstanding waived liability. The bill requires that an employer that submits a request for a waiver of the minimum funding standard notify each affected party. The term "affected party" is defined under the bill as a plan participant, a beneficiary of a deceased participant, a beneficiary that has been designated as an alternate payee pursuant to a qualified domestic relations order, an employee organization representing participants in the plan and the PBGC.

Senate amendment—Title VII

No provision.

Senate amendment—Title IX

No provision.

Conference agreement

The conference agreement clarifies that the IRS is authorized to require that security be provided as a condition of granting a waiver of the minimum funding standard, the extension of an amortization period, or modification of a previously granted waiver of the minimum funding standard with respect to a single employer defined benefit plan. The conference agreement requires that, before granting an application for a waiver, extension or modification to a single employer defined benefit plan, the IRS notify the PBGC of the receipt of a completed application for a waiver, extension, or modification, and consider the views of any interested party, including the PBGC, submitted in writing. The PBGC has a [580] 30-day period after the date of receipt of notice to submit to the IRS comments on the application.

The conference agreement provides that the notice of the application and any other information or materials relating to the application that is sent to the PBGC by the IRS constitutes tax return information and is subject to the safeguarding and reporting requirements of section 6103(p) of the Code.

Under the conference agreement, the security, notice, and comment provisions do not apply if, with respect to the plan for which a waiver is requested, the sum of (a) the accumulated funding deficiencies (including the amount of any increase in the accumulated funding deficiency that would result if the request for a waiver were denied); (b) the outstanding balance of any previously waived funding deficiencies; and (c) the outstanding balance of any decreases in the minimum funding standard allowed under section 303 of ERISA, is less than $2 million. As under current law, the mere creation of a security interest at the direction of the Secretary of the Treasury as a condition for granting a waiver does not by itself constitute a prohibited transaction. The provisions of the conference agreement relating to security are intended by the conferees to provide appropriate rules for the future. The conferees intend that no inference is to be drawn from this provision with respect to the application of present law to such transactions.

The conference agreement also contains an amendment to the Code requiring that if the IRS grants a request for a waiver, extension, or modification, the interest on the waived amount must be computed by using a rate prescribed in section 6621(b) of the Code.

Finally, under the conference agreement, an employer that submits an application for a waiver of the minimum funding standard is required to notify any employee organization representing participants in the plan of the application.

5. Special enforcement rules

House bill—H.R. 3128

A nondeductible excise tax applies if termination liability payments are not made as required.

The initial tax is 5 percent of any payment not made when due. The tax increases by an additional 5 percent of any portion of such payment that is not made within 90 days of the payment's due date, and increases by an additional 5 percentage points for each 30-day period thereafter that the amount remains unpaid. The total additional tax imposed on any unmade payment is limited to the amount of such payment that has not been made within 90 days of the payment's due date.

There is allowed as a credit against the excise tax (up to the amount of the excise tax) any amount paid by the employer to the PBGC, with respect to the employer's termination liability, no later than two years after the final determination of that liability. Liability for the excise tax is the joint and several liability of the controlled group.

[581] House bill—H.R. 3500

The bill adds a new section to ERISA that would expressly confer, upon an adversely affected plan fiduciary, employer, employee organization representing plan participants, contributing sponsor, participant or beneficiary, a private right of action to enjoin certain acts or practices of any party in violation of the employer liability provisions. Other appropriate equitable relief could also be provided by a court.

Under the bill, district courts have exclusive jurisdiction over these actions. A plan could be sued as an entity under these provisions. The bill also provides for venue and for awards of attorney's fees and expenses under certain circumstances.

A copy of the complaint in any action under these provisions would be served on the PBGC. The PBGC could intervene in the action.

Senate amendment—Title VII

No provision.

Senate amendment—Title IX

No provision.

Conference agreement

The conference agreement generally follows H.R. 3500.

6. Evasion of employer liability

House bill—H.R. 3128

Certain transactions undertaken by a person would not be treated as transferring employer liability away from that person or any member of a controlled group including that person. This treatment would apply to transactions undertaken within 10 years before the date of termination of single-employer defined benefit pension plan if a principal purpose of the transaction was to fraudulently evade any employer liability to the PBGC.

House bill—H.R. 3500

If a principal purpose of any person in entering into any transaction is to evade employer liability in connection with the termination of a single-employer defined benefit pension plan, and the transaction becomes effective within 5 years before the termination date, then that person and the members of that person's controlled group (determined as of the termination date) are subject to employer liability in connection with the termination as if that person were a contributing sponsor of the terminated plan as of the termination date. Post-transaction benefit increases or improvements would not be taken into account in computing the liability of such an entity.

Senate amendment—Title VII

No provision.

[582] Senate amendment—Title IX

Rules would be provided for tracing liability in the case of certain corporate reorganizations.

Conference agreement

The conference agreement generally follows H.R. 3500, except that the conference agreement provision is effective only with respect to transactions occurring on or after the earlier January 1, 1986, or the date of enactment. The provisions of the conference agreement relating to evasive transactions are intended by the conferees to provide appropriate rules for the future. The conferees intend that no inference is to be drawn from these provisions with respect to the application of present law to such transactions. In addition, the conference agreement makes it clear that only contributing sponsors (and members of a controlled group including the contributing sponsors) are affected by this provision.

7. Special rule for pending cases

House bill—H.R. 3128

No provision.

House bill—H.R. 3500

No provision.

Senate amendment—Title VII

No provision.

Senate amendment—Title IX

In the case of an employer that (1) had filed an NOIT with the PBGC prior to the date of enactment and had not yet recieved a notice of sufficiency or (2) files an NOIT in a standard termination subsequent to the date of enactment and prior to March 1, 1986, the bill requires that the processing of the plan be delayed if the lesser of 10 or 10 percent of plan participants file complaints with respect to the termination.

The plan administrator of such a plan is not permitted to distribute plan assets until final benefit obligations are fully funded and the PBGC issues a notice of sufficiency with respect to the plan. The PBGC generally is not permitted to issue a notice of sufficiency to the plan until 90 days subsequent to the date that the PBGC determines the plan to be sufficient, except if the employer demonstrates that it is experiencing substantial business hardship. During this additional 90-day period, the PBGC is required to consider and respond to participants' complaints. (Under a special rule, the processing of a plan can be delayed no more than 14 days if the PBGC was previously granted an extension of the period in which to determine the plan's sufficiency because of circumstances wholly within the control of the PBGC.)

Conference agreement

The conference agreement generally follows Title IX of the Senate amendment, except that (1) the processing of a plan is delayed only if the employer is to receive a reversion of surplus [583] assets in excess of $1 million, and the lesser of 200 or 10 percent of plan participants file complaints with respect to the termination; and (2) the PBGC is not permitted to issue a notice of sufficiency for 90 days after the plan is determined to have assets sufficient to fund all benefit commitments, even if an extension period within which PBGC must determine the plan's sufficiency was granted at the request of the PBGC and because of circumstances wholly within the control of the PBGC.

8. Plan assets

Present law

As a general rule, the assets of an employee benefit plan must be held in trust for the exclusive benefit of plan participants. Those individuals or entities with discretion over the management and disposition of plan assets are subject to a number of fiduciary duties enumerated in ERISA. In addition, ERISA prohibits any transaction in which the assets of a plan inure to the benefit of the employer, plan fiduciaries or other interested parties enumerated in ERISA.

Proposed regulations issued by DOL define plan assets for purposes of the fiduciary duty and prohibited transactions rules of ERISA. Under the regulations, if a plan acquires an equity interest in certain types of entities, the investing plan's assets are considered to include both its investment and an undivided interest in each of the underlying assets of the entity. The regulation is effective for purposes of identifying plan assets on or after 90 days after publication of the final regulation.

House bill—H.R. 3128

No provision.

House bill—H.R. 3500

No provision.

Senate amendment—Title VII

No provision.

Senate amendment—Title IX

The bill provides to certain publicly held real estate entities transitional relief from final regulations, to be issued by DOL, defining "plan assets."

Conference agreement

The conference agreement generally follows Title IX of the Senate amendment. Except as a defense, no rule or regulation adopted after date of enactment that defines the term plan assets for purposes of ERISA shall apply to any asset of certain public real estate programs if investments by plan investors in such programs occur prior to the expiration of a specified period of time following the issuance of such rule or regulation. A plan investor is any plan, account, or arrangement (including an individual retirement account).

[584] The conference agreement does not contain a substantive amendment to ERISA but, rather, provides transitional relief in connection with plan asset regulations that are to be issued under ERISA. This will enable public real estate programs to avoid the disruption of normal business arrangements during the development of final regulations by the DOL.

The transitional relief provided in the conference agreement for certain real estate entities is limited to regulations which the DOL currently has under consideration. The conferees have instructed, and expect, the Secretary to adopt final regulations pursuant to the proposal by December 31, 1986.

The transitional relief provided applies to a real estate program that meets certain conditions, including the requirement that the economic rights of ownership with respect to a security issued by such program are "freely transferable." Whether a particular security is "freely transferable" is to be determined based upon all the facts and circumstances; however, the conference agreement also lists several kinds of restrictions which, absent unusual circumstances, will not (either alone or in any combination) cause a security to fail to be freely transferable. The categories are based upon restrictions commonly found in public offerings of securities of real estate entities which are imposed in order to comply with State and Federal laws, to assure continued eligibility for favorable tax treatment, and to avoid certain practical administrative problems. The conferees understand that such restrictions do not, alone or in combination, present any substantial impediment to the ability of investors to readily dispose of their investments and do not prevent such securities from being described as "freely transferable" in prospectuses required under the Federal securities laws. Such a description need not be included in a prospectus in order for a security offered or acquired thereunder to be considered "freely transferable" for purposes of this section.

One of the factors listed is the requirement that transfer or administrative fees be reasonable. It is intended that a fee will not be unreasonable if it does not exceed the cost of effecting transfers of interest on the program's books and the cost of complying with State filing requirements.

It is the intention of the conferees that the requirement that every interest in a real estate entity must be registered under Federal securities laws shall not apply to interest issued to initial limited partners solely for partnership organizational purposes in compliance with State limited partnership laws, provided that such interests are nominal in amount when compared to all other interests in the partnership as of the date of the completion of the offering of such entity, and such partnership was organized prior to enactment. Generally, an interest will be considered nominal if the interest has a value as of the date of issue of less than $20,000 and represents less than one percent of the total interests outstanding as of the completion of the offering period.

Although this section only covers certain public real estate entities, no inference should be drawn concerning the status of any other entity.

[585] 9. Additonal studies

House bill—H.R. 3128

No provision.

House bill—H.R. 3500

No provision.

Senate amendment—Title VII

No provision.

Senate amendment—Title IX

The bill requires that DOL conduct a study of terminations of overfunded pension plans. DOL is required to submit a report on the study, together with any recommendations for statutory changes, to the House Committee on Education and Labor, the Senate Finance Committee, and the Senate Committee on Labor and Human Resources by February 1, 1986.

The bill also requires that the PBGC conduct a study on the purchase of insurance contracts from an insurer in satisfaction of all final benefit obligations under ERISA. THE PBGC is required to submit a report on the study to various committes of Congress by one year from the date of enactment.

Conference agreement

The conference agreement requires the Secretary of Labor to conduct a study of terminations of overfunded pension plans. The report, together with any recommendations for statutory change, must be submitted to the Committees named above by February 1, 1986.

10. Effective dates

The provisions of the conference agreement relating to amendments to reduce significantly future benefit accruals apply to amendments adopted on or after the earlier of January 1, 1986, or the date of enactment.

The provisions of the conference agreement relating to voluntary plan terminations apply to terminations for which a NOIT is filed on or after the earlier of January 1, 1986, or the date of enactment. The provisions relating to involuntary plan terminations apply to terminations for which termination proceedings are instituted on or after the earlier of January 1, 1986, or the date of enactment.

The provisions relating to waivers of the minimum funding standard apply to applications for waivers, extensions of an amortization period, and modifications of a previously granted waiver, submitted to the IRS on or after the earlier of January 1, 1986, or the date of enactment.

The provisions of new ERISA section 4070 relating to enforcement apply to actions filed on or after the earlier of January 1, 1986, or the date of enactment.

As noted above, the provisions of the conference agreement relating to evasion of liability apply to transactions becoming effective on or after the earlier of January 1, 1986, or the date of enactment.

[586] Special effective dates, as described above, are provided for the provisions of the conference agreement relating to PBGC premiums, the special processing rule for pending cases, the DOL plan asset regulations, and the studies authorized.

Title XII—Income Security and Related Programs

* * * * *

[587] (c) Taxation of Social Security Benefits Recieved by Certain Citizens of Possessions of the United States (Section 762 of the Senate amendment)

Present law

Citizens of American Samoa are treated as non-resident aliens and are subject to withholding of taxes from their social security benefits at a 15-percent rate. Citizens of other U.S. territories are exempt from the withholding requirement.

House bill

No provision.

Senate amendment

Eliminates U.S. tax withholding on social security payments to citizens of American Samoa, to make it consistent with the tax treatment of citizens of other U.S. possessions.

Effective date.—Applies to benefits received after December 31, 1983, in taxable years ending after such date.

Revenue effect (in millions):

Fiscal years:	
1986	−$1
1987	−1
1988	−1
3-year total	−3

Conference agreement

House recedes to the Senate amendment.

* * * * *

[590] (j) State Coverage Agreements (Section 769 of the Senate amendment)

Present law

Coverage of State and local employees under social security is, in most cases, effective on the date that an agreement is mailed by the State to the Secretary of Health and Human Services. However, for workers paid on a fee basis and for those whose coverage is retroactive, the agreement becomes effective on the date it is signed by both parties, which may result in complications and loss of coverage for some employees.

House bill

No provision.

[591] Senate amendment

Makes all agreements and modifications of agreements effective on the date the agreement is mailed or delivered by other means to the Secretary.

Effective date.—For agreements or modifications mailed or delivered on or after the date of enactment.

Outlay effect.—None.

Conference agreement

House recedes to the Senate amendment.

(k) Effect of Early Delivery of Benefit Checks (Section 769A of the Senate amendment)

Present law

When the normal delivery date for social security benefits (the thrid day of the month) falls on a Saturday, Sunday or legal holiday, checks must be delivered on the nearest preceding banking day. This may result in checks being delivered in the previous month. If this situation arises at the end of a year, it could cause distortion of year-end trust fund balances, possibly making them low enough to trigger the stabilizer provision, which could effect the amount of cost-of-living increases. This could also result in exaggerated beneficiary tax liability in the earlier year and reduced tax liability in the later year.

House bill

No provision.

Senate amendment

Eliminates these problems by providing that, for purposes of asset-expenditure ratio calculations and taxation of benefits, Social Security benefits delivered prior to their scheduled delivery date would be deemed to have been paid on the regular delivery date.

Effective date.—For benefit checks issued for months ending after the date of enactment.

Outlay effect.—None.

Conference agreement

House recedes to the Senate amendment.

2. Exemption from Social Security coverage for retired Federal judges on active duty (Section 769C of the Senate amendment)

Present law

The 1983 Social Security Amendments (Public Law 98-21) provided that the wages of all active Federal judges would be subject to Social Security taxes beginning January 1, 1984. This provision applied to both current and future judges. P.L. 98-21 also specifically provided that amounts received by judges who achieve senior (retired) status but who continue on active duty would be subject to Social Security taxes on so much of their pay as was attributable to periods when they were performing judicial services. Those earnings would also cause reductions in the judges' benefits under the [592] social security retirement test. (Subsequently, P.L. 98-118 delayed the effective date of this provision until January 1, 1986.)

House bill

No provision.

Senate amendment

Excludes, from the definition of wages for Social Security purposes, the amounts received by Federal judges who meet the criteria for retirement on salary (e.g., age 65 with 15 years of service or 70 with 10 of service), who retire, and who perform active duty. The effect of this exclusion would be to exempt their pay from Social Security taxes and to preclude it from being counted for Social Security earnings test purposes.

Effective date.—Effective for services performed after December 31, 1983.

Outlay effect.—None.

Conference agreement

House recedes to the Senate amendment.

* * * * *

[593] 5. Coverage of Connecticut State police (Section 769H of the Senate amendment)

Present law

Under the Social Security Act, only States specifically listed in the Act may extend social security coverage to policemen who are [594] covered under other retirement programs. Connecticut is not listed. Listed States may only extend coverage in one of two ways: (1) by covering all current and future employees of the affected group; or (2) by covering all future employees and those current employees who desire coverage.

House bill

No provision.

Senate amendment

Allows Connecticut, if the Governor so requests, to cover State police hired on or after May 8, 1984 without conducting a referendum.

Effective date.—Applies to individuals hired on or after May 8, 1984 who are members of the Tier II plan of the Connecticut State Employee Retirement System, with respect to services performed after enactment of this Act.

Revenue effect (in millions):

Fiscal years:	
1986	([1])
1987	$1
1988	1
3-year total	2

[1] Less than $500,000.

Conference agreement

House recedes to the Senate amendment.

* * * * *

[631] 1. Railroad unemployment repayment tax

Present law

Loan authority.—The railroad unemployment insurance (RRUI) program, which provides unemployment and sickness benefits, is funded by unemployment taxes paid by rail employers. The RRUI program can borrow from the railraod retirement program as needed to pay benefits. Such loans are repaid when the Railroad Retirement Board determines that the RRUI account has sufficient funds to make such a repayment. The program's authority to borrow additional funds from the railroads retirement program is scheduled to expire after December 19, 1985.

Loan repayment tax.—The Railroad Retirement Solvency Act of 1983 established a repayment tax scheduled to begin on July 1, 1986 and to expire on September 30, 1990 (Code secs. 3321-3323). The present-law tax rate, applicable to the first $7,000 in wages paid annually to a rail employee, is as follows (sec. 3321):

	Percent
1986	2.0
1987	2.3
1988	2.6
1989	2.9
1990	3.2

House bill

Loan authority.—The House bill makes permanent the authority of the RRUI program to borrow from the railroad retirement program.

Loan repayment tax.—The rate of the present-law loan repayment tax is modified under the House bill to be as follows, beginning July 1, 1986 and expiring September 30, 1990:

	Percent
1986	4.3
1987	4.7
1988	6.0
1989	2.9
1990	3.2

Loan surtax.—Under the House bill, an automatic surcharge of 3.5 percent on the loan repayment tax base will be levied if the RRUI program must borrow from the retirement program. The surtax proceeds are to be used to repay such loans made after September 30, 1985, and is in effect for any year if on September 30 of [632] the prior year any principal or interest from a loan after September 30, 1985 remains unpaid.

Effective date.—The tax provisions will apply to remuneration paid after June 30, 1986. The extension of borrowing authority is effective on enactment.

Senate amendment

The Senate amendment includes the same provisions on loan authority, loan repayment tax, and loan surtax as in the House bill.

In addition, under the Senate amendment a portion of the tier 2 railroad retirement tax equal to one percent of the payroll subject to that tax will be diverted from the railroad retirement program to the RRUI program. These revenues would then be returned to the railroad retirement program to help repay the principal and interest on loans made prior to October 1, 1985. This diversion provision will apply effective January 1, 1986 and will terminate on April 1, 1990.

Conference agreement

The conference agreement is the same as the House bill.

2. Extension of Medicare coverage, hospital insurance tax to State and local government employees

Present law

State and local government employees are covered for social security and Medicare benefits, and such employees and their employers are subject to the FICA tax (including the hospital insurance portion), only pursuant to voluntary agreement between the State and the Secretary of Health and Human Services (Code sec. 3121(b)(7)). Governmental units whose employees have such coverage pursuant to voluntary agreement may not later withdraw their employees from coverage.

Medicare coverage (and the corresponding hospital insurance payroll tax) is mandatory for Federal employees.

For wages paid after 1985, the employer-employee hospital insurance tax rate will be 2.9 percent of the first $42,000 of wages (sec. 3101, 3111, and 3121(a)).

House bill

The House bill extends Medicare coverage on a mandatory basis to State and local government employees hired after December 31, 1985, for service performed after that date. These employees and their employers will be liable for the hospital insurance portion of the FICA tax.

Under the House bill, Medicare coverage and the hospital insurance tax are not extended to individuals hired by a State or political subdivision to relieve unemployment; patients or inmates working in a hospital, home, or other institution; temporary workers hired for certain emergencies; or certain students working in District of Columbia hospitals.

The House bill makes technical changes relating to payment of hospital insurance taxes and definition of Medicare-qualified government employment.

[633] Senate amendment

The Senate amendment extends Medicare coverage on mandatory basis to all current and new State and local government employees, effective for service performed after September 30, 1986. These employees and their employers will be liable for the hospital insurance portion of the FICA tax. Under the Senate amendment, employees who perform State or local government service during and before October 1986 will be given credit toward Medicare eligibility for such past State or local government employment.

The Senate amendment provides that hospital insurance taxes for Medicare qualified State or local government employment are to be collected in the same manner as in the case of such taxes paid by nongovernmental employers.

Conference agreement

The conference agreement follows the House bill, except that a State may extend Medicare coverage (without extending coverage under social security cash benefits) to State and local government employees hired prior to 1986 by voluntary agreement with the Secretary of Health and Human Services. Such employees and their employers would also be liable for the hospital insurance portion of the FICA tax. Under this provision, the collection of Medicare contributions for State and local government employees who are newly covered by this bill will be carried out by the State social security office in cases where the local jurisdiction (or State government) currently has in effect an agreement covering some employees of the jurisdiction under social security. Those jurisdictions (e.g., a city, county, or other government subdivision) within a State that have no employees currently covered under a section 218 agreement will be required to make their payments for Medicare coverage of their employees under the same procedures as private employers currently follow.

3. Tobacco excise tax provisions

a. Extension of present cigarette excise tax rates

Present law

A manufacturers' excise tax equal to $8 per thousand is imposed on small cigarettes; this produces a tax of 16 cents on a pack of 20 cigarettes. Large cigarettes (those weighing more than 3 pounds per thousand) are taxed at $16.80 per thousand. These tax rates are scheduled to decrease by one-half after December 19, 1985.

House bill

The House bill makes permanent the present cigarette excise tax rates (e.g., 16 cents per pack of 20 small cigarettes).

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

The conference agreement follows the House bill and the Senate amendment.

[634] b. Exise taxes on smokeless tobacco

Present law

Present law does not impose any excise taxes on smokeless tobacco products (e.g., chewing tobacco and snuff).

House bill

No provision.

Senate amendment

The Senate amendment imposes an excise tax of 8 cents per pound on chewing tobacco and 24 cents per pound on snuff, effective for taxable products removed after September 30, 1985.

Conference agreement

The conference agreement follows the Senate amendment with a modification providing that the excise taxes on chewing tobacco and snuff are effective for taxable products removed after March 31, 1986.

c. Tobacco Equalization Trust Fund

Present law

Revenues from the cigarette excise tax are deposited in the Treasury as part of general revenues.

House bill

The House bill dedicates a portion of the cigarette excise tax revenues to a new trust fund to assist in defraying the costs of the tobacco price support program, through September 30, 1990.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the Senate amendment.

4. Coal excise tax; Black Lung Disability Trust Fund repayable advances

a. Coal excise tax

Present law

A manufacturers excise tax is imposed on domestically mined coal (other than lignite) sold or used by the producer (Code secs. 4121, 4218).

The tax rate is the lesser of (1) $1 per ton for coal from underground mines and 50 cents per ton for coal from surface mines, or (2) four percent of the price for which the coal is sold. These rates are to revert to pre-1982 rates (50 cents/25 cents per ton; two percent ceiling) on January 1, 1996, or, if earlier, on the January 1 as of which all principal and interest owed the Treasury by the Trust Fund have been paid.

[635] ***House bill***

The House bill increases the coal excise tax rate and sales price ceiling as follow, effective for sales of taxable coal on or after January 1, 1986:

For calendar years 1986–1990, the tax on underground coal will be $1.50 per ton, the tax on surface coal will be $0.75 per ton, and the ceiling will be six percent of the sales price.

For calendar years 1991–1995, the tax on underground coal will be $1.60 per ton, the tax on surface coal will be $0.80 per ton, and the ceiling will be 6.4 percent of the sales price.

For 1996 and later years, the tax on underground coal will be $1.50 per ton, the tax on surface coal will be $0.75 per ton, and the ceiling will be six percent of the sales price. However, the 1985 rates ($1/0.50 per ton; four percent ceiling) will be reinstated for 1996 or any later calendar year if throughout the two most recent fiscal years ending before the beginning of such calendar year there was no balance of repayable advances made to the Trust Fund, and no unpaid interest on such advances.

Senate agreement

No provision.

Conference agreement

The conference agreement will increase the coal excise tax rate, effective January 1, 1986 through December 31, 1995, to the lesser of (1) $1.10 per ton for coal from underground mines and 55 cents per ton for coal from surface mines, or (2) 4.4 percent of the sales price.

b. Black Lung Disability Trust Fund repayable advances

Present law

Amounts equal to the coal excise tax revenues are automatically appropriated to the Black Lung Disability Trust Fund. The Trust Fund pays black lung disability benefits to coal miners (or their survivors) who have been totally disabled by black lung disease in cases where no coal mine operator is found responsible for the individual miner's disease.

Present law includes an unlimited authorization for advances, repayable with interest, from general revenues to the Trust Fund (sec. 9501(c)).

House bill

No provision.

Senate amendment

Under the Senate amendment, no further advances from general revenue to the Black Lung Disability Trust Fund may be made after September 30, 1986. Under the provision, the Trust Fund may not borrow prior to October 1, 1986, amounts to be used to make expenditures after September 30, 1986, or during post-1986 years.

Conference agreement

The conference agreement follows the House bill, except that a one-time, five-year forgiveness of the current interest payments on the cumulative indebtedness of the Trust Fund is provided.

6. Certain exemptions from FUTA tax

a. Certain nonresident farm workers

Present law

An exemption from FUTA is provided for wages paid for agricultural labor performed by aliens admitted to the United States pursuant to section 214(c) and 101(a)(15)(H) of the Immigration and Nationality Act (Code sec. 3306(c)(1)(B)). This exemption is scheduled to expire on December 31, 1985.

House bill

No provision.

Senate amendment

The FUTA exemption for certain nonresident farm workers is extended on a permanent basis for wages paid on or after January 1, 1986.

Conference agreement

The conference agreement follows the Senate amendment, except that the FUTA exemption is extended only for wages paid before January 1, 1988.

b. Summer camp counselors

Present law

A one-year exemption from FUTA was provided for wages paid for 1983 by certain summer camps for employees who were full-time students (sec. 276(b) of P.L. 97–248).

House bill

No provision.

Senate amendment

The Senate amendment provides a permanent FUTA exemption for wages paid to summer camp counselors who are full-time students, effective for wages paid after September 19, 1985.

Conference agreement

The conference agreement follows the Senate amendment.

c. Fishing boat crew members

Present law

An exemption from FUTA was allowed for remuneration paid during 1981–84 to certain fishing boat crew members. This exemption applied only if the remuneration depended on the boat's catch [637] and the crew normally consisted of fewer than 10 members (sec. 822(b) of P.L. 97–34).

House bill

No provision.

Senate Amendment

The Senate amendment provides a permanent FUTA exemption for wages paid to certain fishing boat crew members, effective for wages paid after December 31, 1980.

Conference agreement

The conference agreement follows the Senate amendment.

7. Tax treatment of railroad retirement benefits

Present law

Under present law (Code sec. 86), a portion of Railroad Retirement system benefits computed by using the social security benefit formula (tier 1) is subject to Federal income tax in the same manner as social security benefits, i.e., for individuals whose incomes exceed certain levels (generally, $25,000 for unmarried individuals and $32,000 for married individuals filing a joint return). These benefits may be available at an earlier age under the Railroad Retirement system than under the social security system. Other benefits under the Railroad Retirement system are subject to Federal income tax for all recipients to the extent the payments exceed the amount of the individual's previously taxed contributions to the plan.

House bill

The portion of tier 1 Railroad Retirement benefits that is taxable in the same manner as social security benefits will be limited to the portion of tier 1 benefits that equals the social security benefits to which the individual would have been entitled if all of the individual's employment on which the annuity is based had been employment for social security benefit purposes. In addition, a minimum monthly annuity benefit (described in sec. 3(f)(3) of the Railroad Retirement Act of 1974) will be taxed in the same manner as social security benefits. Other tier 1 Railroad Retirement benefits will be taxed under the rules that apply to all other payments under the Railroad Retirement system.

These provisions will be effective for monthly benefits for which the generally applicable payment date is after December 31, 1985.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill. The conferees expect that the IRS will exercise its authority to waive penalties for failure to make estimated tax payments for 1986, to the extent such failure is solely attributable to increased tax liability of the taxpayer resulting from the amendments made by this provision, [638] in light of the short time between enactment of this bill and the effective date of this provision.

8. Income averaging for former full-time students

Present law

An individual whose income in a year is more than 40 percent higher than his or her average income during the prior three years may use income averaging to reduce tax liability (Code sec. 1301).

To be eligible for income averaging, the individual must have been self-supporting during each of the prior three years. Subject to this requirement, an individual beginning full-time employment after completing college or graduate school is eligible for income averaging.

House bill

No provision.

Senate amendment

The Senate amendment provides that an individual is not eligible for income averaging for a year if he or she was a full-time student during any of the prior three years.

This rule does not apply to a married individual who files a joint return if 25 percent or less of the adjusted gross income of the return is attributable to that individual. Thus, income averaging will remain available where one spouse had been a full-time student during the base period, but did not contribute substantially to the current-year income to be averaged.

This provision is effective for taxable years beginning after December 31, 1985.

Conference agreement

The conference agreement follows the Senate amendment.

9. Fringe benefit provisions

a. Parents of airline employees-airline affiliate employees

Present law

Under the Deficit Reduction Act of 1984, the value of "no-additional-cost" services provided by an employer for use by the employee, or the employee's spouse or dependent children, is excluded from income and wages if certain conditions are met, including a line-of-business limitation (Code sec. 132).

House bill

No provision.

Senate amendment

Parents.—Under the Senate amendment, the value of the use of free or discounted airline passes by parents of an airline employee is excluded from the employee's income and wages on the same basis as where such benefits are used by the employee's spouse or dependent children, effective January 1, 1985.

[639] Airline affiliates.—The Senate amendment excludes from income and wages the value of the use of airline passes by certain individuals who are directly engaged in providing airline-related services. This treatment applies to employees of a corporation predominantly engaged in airline-related services that is a member of an affiliated group which includes an airline. The exclusion applies on the same basis as in the case of employees of the airline corporation who perform airline services. The term airline-related service means (i) catering; (ii) baggage handling; (iii) ticketing and reservations; (iv) flight planning and weather analysis; (v) restaurants located at an airport; (vi) gift shops located at an airport; and (vii) such other similar services provided to and directly benefiting airlines as may be prescribed by Treasury regulations.

Also, a grandfather exception is provided to the line-of-business limitation for tax-free treatment of airline passes furnished (after 1984) to individuals employed, as of September 12, 1984, by Pan American World Services, Inc.

These provisions relating to certain airline affiliate employees are effective January 1, 1985.

Conference agreement

The Conference agreement follows the Senate amendment, with a modification to reflect the House airline affiliate technical corrections provisions (in H.R. 3838).

b. Faculty housing

Present law

Several court cases have held that on-campus housing furnished to faculty or other employees by an educational institution does not qualify for the exclusion under Code section 119 (certain lodging furnished for the convenience of the employer), and that therefore the rental value of the housing (less any amounts paid by the employee) is includible in income and wages.

The Deficit Reduction Act of 1984 prohibits Treasury from issuing, prior to 1986, regulations treating as income the excess of the value of qualified campus lodging over the greater of (1) the operating cost paid in furnishing the lodging, or (2) the rent received, in the case of such lodging furnished in 1984 or 1985.

House bill

No provision.

Senate amendment

The Senate amendment provides that the rental value of qualified campus lodging for a year may not be treated as greater than five percent of the appraised value for the year of the lodging, provided that an independent appraisal is obtained by a qulaified appraiser. Thus, the value of the lodging will be excluded from the employee's income and wages if the rent paid by him or her to the educational institution equals or exceeds (on an annualized basis) five percent of the appraised value. Also, rents charged by an educational institution to nonemployees for comparable lodging may be used to define fair rental value.

This safe-harbor valuation rule will apply for post-1985 taxable years. For prior years, the IRS also is to follow the valuation rule, except that the assessed valuation of the property for local real estate tax purposes would be treated as meeting the requirement of a qualified appraisal.

Conference agreement

The conference agreement follows the House bill.

10. Minimum tax on certain capital gains of insolvent individuals

Present law

Individuals are subject to an alternative minimum tax (Code sec. 55), applying at a 20 percent rate to a base determined by adding certain preferences to the taxpayer's regular taxable income (in addition to certain other adjustments). The minimum tax preference items include the portion of net capital gain excluded for regular tax purposes under section 1202.

House bill

No provision.

Senate amendment

The Senate amendment provides that an insolvent individual who transfers real property used in the active conduct of a trade or business of the taxpayer is not required to treat certain capital gain on the transfer as a minimum tax preference if the transfer was made to a creditor in cancellation of indebtedness or to a third party under threat of foreclosure. The amount of the capital gain exclusion that is not treated as a preference item pursuant to the new rule may not exceed the amount of the individual's insolvency immediately prior to the transfer.

The amendment is effective for transfers of real property occurring after December 31, 1981.

Conference agreement

The conference agreement generally follows the Senate amendment, except that the provision will apply only to farmers and not to other taxpayers. For this purpose, a farmer is defined as an individual more than 50 percent of whose gross income over the past three years was derived from farming. In addition, the provision applies only to transfers of farmland, not of all real property.

11. Tax-exempt bonds for a regional pollution control authority

Present law

Tax-exempt industrial development bonds (IDBs) generally may not be used to acquire a facility, if a substantial user of the facility before acquisition remains as such thereafter (Code sec. 103). Additionally, under a rule enacted in the Deficit Reduction Act of 1984, IDBs may not be used to acquire any existing facilities unless a rehabilitation requirement is satisfied.

[641] A provision enacted in 1982 permitted the Gulf Coast Waste Disposal Authority to acquire certain existing air or water pollution control facilities with the proceeds of IDBs.

House bill

No provision.

Senate amendment

The Senate amendment authorizes up to $200 million of IDBs for acquisition of 23 specific pollution control facilities for the Gulf Coast Waste Disposal Authority. This provision perfects the authorization for these bonds as originally enacted in 1982.

Conference agreement

The conference agreement follows the Senate amendment.

12. Netting of gains and losses by cooperatives

Present law

Cooperatives may exclude from their taxable income amounts distributed to patrons in the form of patronage dividends, and certain other amounts paid or allocated to patrons, to the extent of the net earnings of the cooperative from business done with or for patrons, provided that there is a pre-existing obligation to distribute such amounts (Code sec. 1382). Cooperatives that qualify as tax-exempt farmers' cooperatives also may exclude such amounts from income to the extent of all net income, and also may deduct to a limited extent dividends paid on common stock (sec. 521).

The Code does not contain any explicit provisions regarding whether a cooperative may offset the earnings and losses of its various allocation units in computing its net earnings for the purpose of determining the amounts to be distributed or allocated to patrons, or providing that a cooperative that so computes its net earnings may qualify as a tax-exempt farmers' cooperative. Under present law, the Code does not require a cooperative to notify its patrons that it has offset earnings and losses of its various allocation in computing its net earnings.

House bill

No provision.

Senate amendment

Netting.—The Senate amendment provides that a cooperative is not ineligible for treatment as a tax-exempt farmers' cooperative if it offsets certain earnings and losses in determining any amount available for distribution to patrons. For this purpose, the losses that are attributable to one or more allocation untis (including a loss that is carried over from another year) may be offset against earnings of one or more other allocation units, but only to the extent such earnings and losses are derived from business done with or for patrons. Such patronage earnings and losses may be offset without regard to whether the allocation units whose earnings or losses are offset are functional, divisional, departmental, geographic, or otherwise.

[642] The Senate amendment also provides that the offsetting of earning and losses may be used, at the option of the cooperative, for computing its net earnings in determining the amount of patronage dividends to be paid or allocated to patrons. In addition, the Senate amendment provides that if a cooperative acquires the assets of another cooperative in a transaction specified in section 381(a) and exercises its option to offset earnings and losses, the acquiring cooperative may not, in computing its net earnings for taxable years ending after the date of acquisition, offset losses of one or more of the allocation units of the acquiring or acquired cooperative against earnings of the acquired or acquiring cooperative, respectively, to the extent that (a) the earnings that are offset are not properly allocable to periods after the date of acquisition, and (b) such earnings and losses could not have been offset if derived from allocation units of the same cooperative.

The provisions relating to netting generally are effective for taxable years beginning after December 31, 1962.

Notice requirement.—Cooperatives that engage in the practice of offsetting earnings and losses are required to notify their members that the amount of the member's distribution or allocation may have been affected by the cooperative's netting, effective for taxable years beginning after the date of enactment of the bill. The notice also must specify the identity of the allocation units whose earnings and losses have been offset, as well as what additional information the member is entitled to under governing law.

Conference agreement

The conference agreement generally follows the Senate amendment with modifications.

The conference agreement clarifies that if a cooperative acquires the assets of another cooperative in a transaction described in section 381(a) and exercises its option to offset earnings and losses, the acquiring cooperative may, in computing its net earnings for taxable years ending after the date of acquisition, offset losses of one or more allocation units of the acquiring or acquired cooperative against earnings of the acquired or acquiring cooperative, respectively, but only to the extent that (a) such earnings are properly allocable to periods after the date of acquisition,[1] and (b) such earnings could have been offset by such losses if such earnings and losses had been derived from allocation units of the same cooperative.

13. Extension of moratorium on application of research and experimental expense allocation regulation

Present law

The foreign tax credit is limited so that it cannot offset U.S. tax on U.S. source taxable income. In general, the Code requires allocation of all expenses between U.S. and foreign source gross income to determine U.S. and foreign source taxable income. A Treasury Regulation (sec. 1.861–8) rule generally requires taxpayers with foreign source income from products in a product area in which the taxpayers do U.S. research to allocate part of their U.S. research and experimental expense against their foreign source income. In 1981, the Congress suspended this rule for two years, so that research expenditures made for research conducted in the United States were allocated against U.S. source gross income only. In 1984, the Congress extended the moratorium for two additional years. The moratorium generally expired for taxable years beginning after August 1, 1985.

House bill

No provision.

Senate amendment

The Senate amendment effectively extends for one year the moratorium on the application of the research and experimental expense allocation rules of Treas. Reg. sec. 1.861–8. For taxable years beginning on or before August 1, 1986, all of a taxpayer's research and experimental expenditures attributable to research activities conducted in the United States will be allocated to U.S. source gross income for purposes of computing U.S. source and foreign taxable income and taxable income from sources partly within and partly without the United States. The extension of the moratorium applies only to the allocation of research expenses for the purpose of geographic sourcing of income. It does not apply for other purposes, such as the computation of combined taxable income of a FSC (or DISC) and its related supplier.

Conference agreement

The conference agreement follows the Senate amendment.

* * * *

15. Awards of attorneys fees and other court costs in tax litigation

Present law

Attorneys fees for tax litigation and other court costs of up to $25,000 may be awarded to a taxpayer who prevails in the litigation in a Federal court if the taxpayer shows that the Government's position in the litigation was unreasonable (Code sec. 7430). Under present law, this provision will not apply to court proceedings commenced after December 31, 1985.

House bill

No provision.

Senate amendment

The Senate amendment makes permanent the authorization of attorneys fees and other court costs for tax litigation under section 7430. Also, the Senate amendment makes the following modifications which would apply to court proceedings commencing after December 31, 1985:

(1) If it is determined that the taxpayer prevailed in the tax litigation, the burden is on the Government to show that its position was substantially justified or that special circumstances exist that make an award of litigation costs unjust;

(2) Whether an award is made is determined based upon a "substantially justified" standard;

(3) No award is allowd to a prevailing party who unreasonably protracted the proceedings;

(4) The $25,000 cap of present law is eliminated (as under present law, recoverable costs would not include costs of the administrative process); and

(5) Limits are imposed on hourly charges by attorneys and expert witness fees recoverable under the provision.

Conference agreement

The conference agreement follows the House bill (i.e., contains no provision).

* * * * *

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[1] Where an acquisition takes place during a taxable year, the conferees intend that the cooperative's earnings for the entire year are to be allocated pro rata between the pre-acquisition and post-acquisition periods.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Henry L. Creel	Cleveland, OH	Certified Public Accountant	Indefinite from May 15, 1986
J. Thomas Jones	Augusta, GA	Certified Public Accountant	Indefinite from June 1, 1986
Michael D. Sherman	Pound Ridge, NY	Enrolled Agent	Indefinite from May 27, 1986
Trevor Adel	Silver Spring, MD	Certified Public Accountant	Indefinite from June 2, 1986
John H. Peimann	Ottawa, KS	Certified Public Accountant	Twenty-One Months from June 1, 1986
John D. Raikos	Indianapolis, IN	Attorney	Indefinite from May 20, 1986
Vernon Rubel	Hickory, NC	Enrolled Agent	Indefinite from May 28, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and address of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the Weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Earl M. Walker	Port Neches, TX	Certified Public Accountant	May 19, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor.
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federral Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

Bulletins 1986–27 through 1986–28

Announcements:
86–84, 1986–27 I.R.B. *35*

Revenue Rulings:
86–86, 1986–27 I.R.B. *34*
86–87, 1986–28 I.R.B. *7*
86–88, 1986–28 I.R.B. *10*
86–89, 1986–28 I.R.B. *4*
86–90, 1986–28 I.R.B. *12*

Treasury Decisions:
8089, 1986–28 I.R.B. *4*
8090, 1986–27 I.R.B. *5*
8091, 1986–28 I.R.B. *14*

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

Finding List of Current Action on Previously Published Rulings[1]

Bulletins 1986–27 through 1986–28

***Denotes entry since last publication**

Revenue Rulings:
68–356
Modified by
86–89, 1986–28 I.R.B. 4*

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[1] **A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.**

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CUMULATIVE BULLETINS

The contents of the weekly Bulletin are consolidated semiannually into a permanent, indexed, Cumulative Bulletin. These are sold on a single copy basis and *are not* included as part of the subscription to the Internal Revenue Bulletin. Subscribers to the weekly Bulletin are notified when copies of the Cumulative Bulletin are available. Certain issues of Cumulative Bulletins are out of print and are not available. Persons desiring available Cumulative Bulletins, which are listed on the reverse, may purchase them from the Superintendent of Documents.

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Internal Revenue bulletin

Bulletin No. 1986-30
July 28, 1986

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-92, page 5.
Investment trust; tax classification. A limited power to substitute certain investment contracts for contracts that fail during the first 90 days of an investment trust is not a power to vary the beneficiaries investment; accordingly, such power will not cause the trust to be classified as an association taxable as a corporation.

Announcement 86-85, page 7.
This Bulletin contains a list of organizations that no longer qualify as organizations contributions to which are deductible under section 170(c)(2) of the Code.

EMPLOYEE PLANS

Announcement 86-86, page 7.
In accordance with Section 12 of Rev. Proc. 84-23, set forth is a list of master and prototype plans closed or disposed of by the National Office of the Internal Revenue Service between April 1, 1986, and June 30, 1986, and a list of plans inadvertently omitted from Announcement 85-99.

EXEMPT ORGANIZATIONS

Announcement 86-89, page 17.
A list is given of organizations now classified as private foundations and organizations that are not private operating foundations.

EXCISE TAXES

Rev. Rul. 86-91, page 5.
Alcohol used in fuels; application of partial exemption to ethanol derived from ethane. The partial exemption for alcohol fuels provided under section 4041(m)(1)(A) of the Code applies to ethanol produced through the process of thermally cracking ethane that is a constituent of natural gas. Rev. Rul. 85-18 clarified.

ADMINISTRATIVE

Announcement 86-87, page 16.
Publication 560, Self-Employed Retirement Plans, has been revised and is now available from the Service.

Announcement 86-88, page 16.
A new form, Form 1041S, U.S. Fiduciary Income Tax Return for Nontaxable Simple Trusts, has been developed for use by trusts that have no capital gains or losses and have an income distribution deduction that is equal to the amount of income that the trust is required to distribute currently. This form will be available in January 1987.

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Announcement of Disbarments and Suspensions on page 20.
Announcement Relating to Decisions of the Tax Court on page 4.

Department of the Treasury
Internal Revenue Service

T 22.23: 1986-30

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Announcement Relating to Decisions of the Tax Court

It is the policy of the Internal Revenue Service to announce in the Internal Revenue Bulletin at the earliest practicable date the determination of the commissioner to acquiesce or not acquiesce in a decision of the Tax Court which disallows a deficiency in tax determined by the Commissioner to be due.

Notice that the Commissioner has acquiesced or nonacquiesced in a decision of the Tax Court relates only to the issue or issues decided adversely to the Government.

Actions of acquiescences in adverse decisions shall be relied on by Revenue officers and others concerned as conclusions of the Service only to the application of the law to the facts in the particular case. Caution should be exercised in extending the application of the decision to a similar case unless the facts and circumstances are substantially the same, and consideration should be given to the effect of new legislation, regulations, and rulings as well as subsequent court decisions and actions thereon.

Acquiescence in a decision means acceptance by the Service of the conclusion reached, and does not necessarily mean acceptance and approval of any or all of the reasons assigned by the Court for its conclusions.

No announcements are made in the Bulletin with respect to memorandum opinions of the Tax Court.

The announcement published in the weekly Internal Revenue Bulletins are consolidated semiannually and annually. The semiannual consolidation appears in the first Bulletin for July and in the Cumulative Bulletin for the first half of the year and the annual consolidation appears in the first Bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner ACQUIESCES in the following decision:

		Report	
Taxpayer	**Docket No.**	**Volume**	**Page**
Greene, Martin I., et ux[1]	**25789-83**	**85**	**1024**

The Commissioner does NOT ACQUIESCE in the following decision:

		Report	
Taxpayer	**Docket No.**	**Volume**	**Page**
St. Joseph Farms of Indiana[2]	**27830-81**	**85**	**9**

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[1] Acquiescence in result relating to whether taxpayer's surrender of an annuity contract held with one insurance company followed by the reinvestment of the proceeds thereof in an annuity contract with another company was a nontaxable exchange under section 1035 of the Code. Acquiescence "in result" means acceptance of the Court but disagreement with some or all the reasons assigned for the decision.

[2] Nonacquiescence relating to whether, for purposes of section 513(a)(1) of the Code, "uncompensated labor" exception from the definition of "unrelated trade or business," Catholic brothers subject to vows of poverty and obedience who receive room, board, and various benefits while operating a large farm are performing services without compensation.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 4041.—Imposition of Tax

26 CFR 48.4041-18: Fuels containing alcohol.

Alcohol used in fuels; application of partial exemption to ethanol derived from ethane. The partial exemption for alcohol fuels provided under section 4041(m)(1)(A) of the Code applies to ethanol produced through the process of thermally cracking ethane that is a constituent of natural gas. Rev. Rul. 85–18 clarified.

Rev. Rul. 86–91

Section 4041(a)(2) of the Internal Revenue Code imposes a tax of 9 cents a gallon on the sale or use of certain special motor fuels. Section 4041(b)(2) exempts from the tax imposed by section 4041(a) qualified methanol or ethanol fuel, which is defined as any liquid at least 85 percent of which consists of methanol, ethanol, or other alcohol produced from a substance other than petroleum or natural gas.

Rev. Rul. 85–18, 1985–1 C.B. 15, holds that since the ethanol by-product of the ethylcellulose manufacturing process described therein is derived from ethane (a constituent of natural gas) or crude oil, the ethanol does not qualify as alcohol for purposes of the alcohol fuels provisions of sections 40, 4041(b)(2), 4041(k) and 4081(c) of the Code.

Under section 4041(m)(1)(A) of the Code, as added by section 913(a) of the Tax Reform Act of 1984, 1984–3 (Vol. 1) C.B. 1, 516, effective August 1, 1984, the sale or use of any "partially exempt methanol or ethanol fuel" will be subject to a tax per gallon of 4½ cents rather than 9 cents under section 4041(a)(2). The term "partially exempt methanol or ethanol fuel" is defined in section 4041(m)(2) as meaning any liquid at least 85 percent of which consists of methanol, ethanol, or other alcohol produced from natural gas.

Thus, to the extent that the ethanol described in Rev. Rul. 85–18 is produced through the process of thermally cracking ethane that is a constituent of natural gas, the ethanol is produced from natural gas and qualifies for the partial exemption provided under section 4041(m)(1)(A) of the Code, effective August 1, 1984.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 85–18 is clarified.

Section 7701.—Definitions

26 CFR 301.7701-4: Trusts.

Investment trust; tax classification. A limited power to substitute certain investment contracts for contracts that fail during the first 90 days of an investment trust is not a power to vary the beneficiaries investment; accordingly, such power will not cause the trust to be classified as an association taxable as a corporation.

Rev. Rul. 86–92

ISSUE

If contracts to purchase certain bonds are deposited in an investment trust and, in the event the specified bonds cannot be obtained, the trust agreement permits the sponsor of the trust to provide instead different bonds of the same character and quality as those specified in the contracts or to provide no bonds at all, then for purposes of section 301.7701–4(c) of the Regulations on Procedure and Administration, does the sponsor possess a power to vary the investment of the certificate holders?

FACTS

A securities broker, as sponsor, formed an investment trust with a bank as trustee. The sponsor deposited in the trust certain tax-exempt bonds and contracts to purchase tax-exempt bonds (contracts to purchase). In exchange for these contributions, the sponsor received certificates representing a single class of undivided beneficial ownership in the assets of the trust. The sponsor then sold all of the certificates to investors.

The contracts to purchase permit the trust to purchase bonds on a "when, as, and if issued" basis. The contracts to purchase provide that all bonds subject to the contracts must be transferred to the trust within 90 days of the creation of the trust. If bonds subject to the contracts to purchase are not transferred to the trust within the 90-day period and if this failure is due to reasons beyond the control of the sponsor or the trustee, the sponsor has 20 days within which to transfer to the trust different bonds of substantially the same character and quality as those covered by the "failed" contracts to purchase. If the sponsor does not do so, the trustee must refund to the certificate holders on the next payment date that portion of the sales charge, principal, and accrued interest attributable to the failed contracts to purchase.

Any bond acquired to replace a bond in a "failed" contract to purchase (1) must be tax-exempt, (2) must have a fixed maturity date no later than the date of maturity of the bond it replaces, (3) must have a fixed interest rate not less than that of the bond it replaces and a yield to maturity at least equal to that of the bond it replaces, (4) must have a rating at least equal to the bond it replaces, (5) must have a purchase price no greater than the principal attributable to the bond it replaces, and (6) must not be a "when, as, and if issued" bond.

LAW AND ANALYSIS

Section 301.7701–4(c) of the regulations provides that an investment trust will not be classified as a trust if there is a power under the trust agreement to vary the investment of the certificate holders. *See Commissioner v. North American Bond Trust,* 122 F.2d 545 (2d Cir. 1941), *cert. denied,* 314 U.S. 701 (1942). An investment trust with a single class of ownership interests, representing undivided beneficial interests in the assets of the trust, will be classified as a trust and not as an association taxable as a corporation if there is no power under the trust agreement to vary the investment of the certificate holders.

A power to vary the investment of the certificate holders exists if there is a managerial power under the trust instrument that enables a trust to take advantage of market variations to improve the investment of the investors. *See North American Bond Trust,* 122 F.2d at 546; Rev. Rul. 75–192, 1975–1 C.B. 384; and Rev. Rul. 78–149, 1978–1 C.B. 448.

Under the trust agreement in the present revenue ruling, neither the trustee nor the sponsor has the power to take advantage of market variations to improve the investment of the certificate holders. The trustee may only accept bonds specified in the contracts to purchase or bonds of substantially the same character and quality selected by the sponsor, and even the latter may be done only if bonds are not furnished under one of the contracts to purchase. Should a contract to purchase fail, the sponsor has only the power to provide bonds of the same character and quality as those specified in the failed contract to purchase, or simply to fail to provide some bonds. In the latter case, the trustee must refund to the certificate holders that portion of the sales charge, principal, and accrued interest that is attributable to the failed contract. The powers at issue here are unlike those in Rev. Rul. 78–149, where reinvestment was used to take advantage of variations in the market over a twenty-year period. The powers in the present case are merely incidental to the organization of the trust during its first 110 days and do not constitute a power to vary the investment of the certificate holders. Once the bonds are placed in the trust, there is no change in the make-up of the trust corpus and no additional investment.

HOLDING

For purposes of section 301.7701–4(c) of the regulations, an investment trust agreement does not contain a power to vary the investment of the certificate holders solely because the governing instrument of an investment trust provides that, in the event of a contract failure, the sponsor may provide bonds of substantially the same character and quality as those bonds specified in the contracts to purchase that were deposited in the trust. Accordingly, under the facts set forth above, the trust is classified for federal income tax purposes as a trust and not as an association taxable as a corporation.

Part IV. Items of General Interest

Deletions from Cumulative List of Organizations Contributions to Which Are Deductible Under Section 170 of the Code

Announcement 86-85

The names of organizations that no longer qualify as organizations described in section 170(c)(2) of the Internal Revenue Code of 1954 are listed below.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgment has been timely filed, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deductible. Protection under section 7428(c) would begin on July 28, 1986, and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is $1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

Educational Guidance Foundation, Garden Grove, CA

Johnny Walker Boys Ranch, Trenton, NE

Michigan Crime Investigation Commission, Plymouth, MI

Reservoir Hill Community Association, Inc., Baltimore, MD

Young Peoples Organization, Inc., Fresno, CA

Lists of Master and Prototype Plans Closed or Otherwise Disposed of between April 1, 1986 and June 30, 1986, and Plans Inadvertently Omitted from Announcement 85-99

Announcement 86-86

This Announcement contains two lists of master and prototype (M&P) pension, annuity or profit-sharing plans submitted to the National Office of the Internal Revenue Service during 1984 by sponsoring organizations and mass submitters.

The first list (List A) includes those M&P plans that were timely submitted under Revenue Procedure 84-23, 1984-1 C.B. 457, by December 31, 1984, and were closed or otherwise disposed of by the Service between April 1, 1986, and June 30, 1986.

List A contains the names and addresses of the plans' sponsoring organization or mass submitter, symbols indicating the type of plan, and file folder number. It also shows the date of disposition of the plan and the type of disposition as follows: (1) favorable opinion letter(F), (2) unfavorable/nonopinion letter(U), (3) withdrawal letter(W), or (4) other(O).

Employers that adopted an approved M&P plan and, if appropriate, requested a determination letter on or before March 19, 1984, and received a favorable determination letter, retained reliance on their favorable letter under the provisions of Section 12 of Rev. Proc. 84-23. Other adopting employers will have the provisions of Section 12 of Rev. Proc. 84-23 applied to them also, provided the conditions outlined in Announcement 86-60, 1986-19 I.R.B. 17 are met. In either case, if the approved plan is included in List A, the employer must take further action in order to have continued reliance and to meet the compliance date described in Announcement 86-60.

If List A shows that the plan adopted by the employer received a favorable opinion letter, the employer must, within 12 months after the sponsor received the favorable letter, either (1) amend its existing plan by adopting the sponsor's M&P plan as approved by the Service, or (2) adopt an M&P plan of another sponsor on List A or another quarterly list, that has received a favorable letter (See Announcement 85-130, 1985-36 I.R.B. 58).

If List A shows that the plan was closed other than by issuance of a favorable opinion letter, such employer must either (1) make all amendments required by Section 5 of Rev. Proc. 84-23, including amendments to conform with the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) Pub. L. 97-248, 1982-2 C.B. 462, the Tax Reform Act of 1984 (TRA) Pub. L. 98-369, 1984-3 (Vol. 1) C.B. 1, and the Retirement Equity Act of 1984 (REA) Pub. L. 98-397, 1984-2 C.B. 433, and submit a request for a determination letter to the appropriate key district office, or (2) adopt an approved M&P plan of a sponsor that has received a favorable opinion letter and is listed in either Announcement 85-99, 1985-28 I.R.B. 4, or List B of this or the following Announcements: 85-165, 1985-47 I.R.B. 4; 86-43, 1986-14 I.R.B. 13, or 86-70, 1986-21 I.R.B. 33. In order to be afforded continued reliance and to meet the compliance date described in Announcement 86-60 the employer must adopt the amended plan by January 31, 1987.

After amending its existing plan or adopting another M&P plan, an employer must request a determination letter from the appropriate key district office in order to rely on the plan's qualification unless the employer adopts a standardized or paired plans within the meaning of Section 6.01 of Rev. Proc. 84-23.

The second list in this Announcement (List B) includes those M&P plans that were inadvertently omitted from the list published in Announcement 85-99. See Announcement 85-99 regarding when these plans must be adopted.

LISTING OF MASTER OR PROTOTYPE PLANS

Abbreviations:

Type of Closing
F = Favorable
U = Unfavorable/nonopinion
W = Withdrawal
O = Other

Type of Plan
P = Paired
S = Standardized (not paired)
NS = Nonstandardized
M = Money Purchase
T = Target Benefit
D = Defined Benefit

Sponsors of Master and Prototype Plans

Academy Life Insurance Co; Valley Forge, PA; 50201580001-001; S; PS; F; 06/02/86

Allstate Life Insurance Co; Northbrook, IL; 50202160001-001; S; M; F; 05/23/86

Allstate Life Insurance Co; Northbrook, IL; 50202160001-002; S; PS; F; 05/23/86

American Bank & Trust Co; Walnut Creek, CA; 50302868402-001; NS; D; F; 05/30/86

American Bank & Trust Co; Walnut Creek, CA; 50202868402-002; P; D; F; 05/30/86

American Bank & Trust Co; Walnut Creek, CA; 50302868403-001; NS; M; F; 05/30/86

American Bank & Trust Co; Walnut Creek, CA; 50202868403-002; P; M; F; 05/30/86

American Bank & Trust Co; Walnut Creek, CA; 50302868403-003; NS; PS; F; 05/30/86

American Bank & Trust Co; Walnut Creek, CA; 50202868403-004; P; PS; F; 05/30/86

American Bank of Commerce; El Paso, TX; 50302490001-001; NS; PS; F; 06/13/86

American Bank of Commerce; El Paso, TX; 50302490001-002; NS; PS; F; 06/13/86

American Bank of Commerce; El Paso, TX; 50302490002-001; NS; M; F; 06/13/86

American Bank of Commerce; El Paso, TX; 50302490002-002; NS; M; F; 06/13/86

American Capital Marketing Inc; Houston, TX; 50302820001-001; NS; M; F; 05/19/86

American Capital Marketing Inc; Houston, TX; 50302820003-001; NS; PS; F; 05/19/86

American Medical Association; Chicago, IL; 50272080001-001; S; M; F; 04/14/86

American Trust Co of Hawaii Inc; Honolulu, HI; 50203910001-001; P; M; F; 05/15/86

American Trust Co of Hawaii Inc; Honolulu, HI; 50203910001-002; P; PS; F; 05/15/86

Andrew Jackson Life Insurance Co; Jackson, MS; 50304140001-001; NS; PS; F; 04/14/86

Andrew Jackson Life Insurance Co; Jackson, MS; 50304140001-002; NS; PS; F; 04/14/86

Associated Builders & Contractors of Western Washington; Bellevue, WA; 50270580001-001; S; PS; U; 04/28/86

BancMidwest McLean County NA; Bloomington, IL; 50341800002-001; NS; PS; F; 04/10/86

BancMidwest McLean County NA; Bloomington, IL; 50341800002-002; NS; M; F; 04/10/86

BancMidwest McLean County NA; Bloomington, IL; 50241802203-001; P; PS; F; 06/13/86

BancMidwest McLean County NA; Bloomington, IL; 50241802203-002; P; M; F; 06/13/86

Bank of Boston Norfolk; Wellesley, MA; 50244880001-001; P; M; F; 05/15/86

Bank of Boston Norfolk; Wellesley, MA; 50244880001-002; P; PS; F; 05/14/86

Bank of Galesburg; Galesburg, IL; 50273020701-001; P; M; F; 04/14/86

Bank of Galesburg; Galesburg, IL; 50273020701-002; P; PS; F; 04/14/86

Bank of Honolulu; Honolulu, HI; 50260990001-001; S; PS; U; 06/18/86

Bank of New England Trust Co NA; West Palm Beach, FL; 50225800001-001; S; M; F; 04/14/86

Bank of New England Trust Co NA; West Palm Beach, FL; 50225800001-002; S; PS; F; 04/14/86

Bank of New Hampshire NA; Concord, NH; 50206340001-001; S; PS; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50306340001-002; NS; PS; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50206340001-003; S; PS; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50306340001-004; NS; PS; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50206340001-005; S; M; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50306340001-006; NS; M; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50206340001-007; S; M; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50306340001-008; NS; M; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50206340002-001; S; PS; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50306340002-002; NS; PS; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50206340002-003; S; PS; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50306340002-004; NS; PS; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50206340002-005; S; M; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50306340002-006; NS; M; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50206340002-007; S; M; F; 06/02/86

Bank of New Hampshire NA; Concord, NH; 50306340002-008; NS; M; F; 06/02/86

Bank of Virginia; Richmond, VA; 50306961801-001; NS; M; F; 05/19/86

Bank of Virginia; Richmond, VA; 50306961801-002; NS; PS; F; 05/19/86

Bank of Virginia; Richmond, VA; 50206970001-001; P; M; F; 04/18/86

Bank of Virginia; Richmond, VA; 50206970001-002; P; PS; F; 04/18/86

Bank of Ysleta; El Paso, TX; 50370570001-001; NS; PS; F; 05/01/86

Bank Service Association; Tupelo, MS; 50376400701-001; NS; M; F; 04/14/86

Bank Service Association; Tupelo, MS; 50276400701-002; P; M; F; 04/14/86

Bank Service Association; Tupelo, MS; 50376400701-003; NS; PS; F; 04/14/86

Bank Service Association; Tupelo, MS; 50276400701-004; P; PS; F; 04/14/86

Bankers Life Insurance Co of Nebraska; Lincoln, NE; 50307460001-001; NS; D; F; 06/16/86

Bankers Life Insurance Co of Nebraska; Lincoln, NE; 50307460001-002; NS; D; F; 06/16/86

Bankers Life Insurance Co of Nebraska; Lincoln, NE; 50307460002-001; NS; M; F; 06/16/86

Bankers Life Insurance Co of Nebraska; Lincoln, NE; 50307460002-002; NS; PS; F; 06/16/86

Bellingham National Bank; Bellingham, WA; 50208080001-001; S; PS; F; 06/23/86

Bellingham National Bank; Bellingham, WA; 50208080001-002; S; PS; F; 06/23/86

Beneficial Mutual Savings Bank; Philadelphia, PA; 50208120001-001; P; PS; F; 04/14/86

Beneficial Mutual Savings Bank; Philadelphia, PA; 50208120001-002; P; PS; F; 04/14/86

Bessemer Trust Co NA; New York, NY; 50208280001-001; S; M; F; 04/14/86

Bessemer Trust Co NA; New York, NY; 50208280001-002; S; PS; F; 04/14/86

Bessemer Trust Co of Florida; Palm Beach, FL; 50227450001-001; S; M; F; 04/14/86

Bessemer Trust Co of Florida; Palm Beach, FL; 50227450001-002; S; PS; F; 04/14/86

Birr Wilson Securities Inc; San Francisco, CA; 50208350001-001; P; PS; F; 06/19/86

Birr Wilson Securities Inc; San Francisco, CA; 50208350001-002; P; M; F; 06/19/86

Boone County National Bank; Columbia, MO; 50208580001-001; P; PS; F; 04/24/86

Boone County National Bank; Columbia, MO; 50208580001-002; P; M; F; 04/24/86

Boone County National Bank; Columbia, MO; 50308580002-001; NS; PS; F; 04/24/86

Boone County National Bank; Columbia, MO; 50308580002-002; NS; PS; U; 04/24/86

Boone County National Bank; Columbia, MO; 50308580002-003; NS; M; F; 04/24/86

Boone County National Bank; Columbia, MO; 50308580002-004; NS; M; U; 04/24/86

Capital Trust Co of Delaware; Wilmington, DE; 50280398501-001; P; PS; U; 04/14/86

Capital Trust Co of Delaware; Wilmington, DE; 50280398501-002; P; M; U; 04/14/86

Capital Trust Co of Delaware; Wilmington, DE; 50280398502-001; P; D; U; 04/14/86

Capital Trust Co of Delaware; Wilmington, DE; 50280398502-002; P; D; U; 04/14/86

Catholic Order of Foresters; Naperville, IL; 50210090701-001; S; M; F; 04/07/86

Central Bancorporation Inc; Denver, CO; 50210490001-001; P; PS; F; 04/24/86

Central Bancorporation Inc; Denver, CO; 50210490001-002; P; M; F; 04/24/86

Central Bank & Trust Co; Lexington, KY; 50310530001-001; NS; PS; F; 04/24/86

Central Bank & Trust Co; Lexington, KY; 50310530001-002; NS; PS; F; 04/24/86

Central Bank & Trust Co; Lexington, KY; 50310530001-003; NS; M; F; 04/24/86

Central Bank & Trust Co; Lexington, KY; 50310530001-004; NS; M; F; 04/24/86

Central Bank of Denver; Denver, CO; 50310630001-001; NS; PS; F; 04/10/86

Central Bank of Denver; Denver, CO; 50310630001-002; NS; M; F; 04/10/86

Central Bank of Denver; Denver, CO; 50210630001-003; P; PS; F; 04/10/86

Central Bank of Denver; Denver, CO; 50210630001-004; P; M; F; 04/10/86

Central Corp; Monroe, LA; 50314790701-001; NS; PS; F; 04/14/86

Central Corp; Monroe, LA; 50214790701-002; P; PS; F; 04/14/86

Central Corp; Monroe, LA; 50314790701-003; NS; M; F; 04/14/86

Central Corp; Monroe, LA; 50214790701-004; P; M; F; 04/14/86

Central Life Assurance Co; Des Moines, IA; 50310810703-001; NS; M; F; 04/14/86

Central Life Assurance Co; Des Moines, IA; 50210810703-002; P; M; F; 04/14/86

Central Life Assurance Co; Des Moines, IA; 50310810703-003; NS; PS; F; 04/14/86

Central Life Assurance Co; Des Moines, IA; 50210810703-004; P; PS; F; 04/14/86

Central Life Assurance Co; Des Moines, IA; 50310810704-001; NS; D; F; 04/14/86

Central Life Assurance Co; Des Moines, IA; 50310810704-002; NS; D; F; 04/14/86

Central Life Assurance Co; Des Moines, IA; 50210810704-003; P; D; F; 04/14/86

Central Life Assurance Co; Des Moines, IA; 50210810704-004; P; D; F; 04/14/86

Central Plains Insurance Co; Los Angeles, CA; 50380208401-001; NS; M; F; 05/30/86

Central Plains Insurance Co; Los Angeles, CA; 50280208401-002; P; M; F; 05/30/86

Central Plains Insurance Co; Los Angeles, CA; 50380208401-003; NS; PS; F; 05/30/86

Central Plains Insurance Co; Los Angeles, CA; 50280208401-004; P; PS; F; 05/30/86

Central Plains Insurance Co; Los Angeles, CA; 50380208402-001; NS; D; F; 05/30/86

Central Plains Insurance Co; Los Angeles, CA; 50280208402-002; P; D; F; 05/30/86

Chartered Protection Life; Los Angeles, CA; 50380218401-001; NS; M; F; 05/30/86

Chartered Protection Life; Los Angeles, CA; 50280218401-002; P; M; F; 05/30/86

Chartered Protection Life; Los Angeles, CA; 50380218401-003; NS; PS; F; 05/30/86

Chartered Protection Life; Los Angeles, CA; 50280218401-004; P; PS; F; 05/30/86

Chartered Protection Life; Los Angeles, CA; 50380218402-001; NS; D; F; 05/30/86

Chartered Protection Life; Los Angeles, CA; 50280218402-002; P; D; F; 05/30/86

Chester Bank; Chester, CT; 50271690001-001; P; M; F; 05/02/86

Chester Bank; Chester, CT; 50271690001-002; P; PS; F; 05/02/86

Cigna Securities Inc; Bloomfield, CT; 50311797101-001; NS; M; F; 04/04/86

Cigna Securities Inc; Bloomfield, CT; 50211797101-002; P; M; F; 04/04/86

Cigna Securities Inc; Bloomfield, CT; 50311797101-003; NS; PS; F; 04/04/86

Cigna Securities Inc; Bloomfield, CT; 50211797101-004; P; PS; F; 04/04/86

Cigna Securities Inc; Bloomfield, CT; 50311797102-001; NS; D; F; 06/18/86

Cigna Securities Inc; Bloomfield, CT; 50311797102-002; NS; D; F; 06/18/86

Cigna Securities Inc; Bloomfield, CT; 50211797102-003; P; D; F; 06/18/86

Cigna Securities Inc; Bloomfield, CT; 50211797102-004; P; D; F; 06/18/86

Cigna Securities Inc; Bloomfield, CT; 50311797103-001; NS; T; F; 04/04/86

Cigna Securities Inc; Bloomfield, CT; 50211797103-002; S; T; F; 04/04/86

Citizens National Bank of Danville; Danville, KY; 50212850001-001; S; PS; F; 04/14/86

Citizens National Bank of Danville; Danville, KY; 50212850001-002; S; PS; F; 04/14/86

Citizens National Bank of Danville; Danville, KY; 50212850002-001; S; M; F; 04/14/86

Citizens National Bank of Danville; Danville, KY; 50212850002-002; S; M; F; 04/14/86
Citizens National Bank of Decatur; Decatur, IL; 50312860001-001; NS; PS; F; 04/10/86
Citizens National Bank of Decatur; Decatur, IL; 50312860001-002; NS; M; F; 04/10/86
Citizens National Bank of Decatur; Decatur, IL; 50212860002-001; P; PS; F; 04/21/86
Citizens National Bank of Decatur; Decatur, IL; 50212860002-002; P; M; F; 04/21/86
Citizens National Bank of Evans City; Lyndora, PA; 50312870001-001; NS; PS; F; 06/27/86
Citizens National Bank of Evans City; Lyndora, PA; 50312870001-002; NS; PS; F; 06/27/86
Citizens State Bank of Corpus Christi; Corpus Christi, TX; 50313260701-001; NS; M; F; 06/09/86
Citizens State Bank of Corpus Christi; Corpus Christi, TX; 50213260701-002; P; M; F; 06/09/86
Citizens State Bank of Corpus Christi; Corpus Christi, TX; 50313260701-003; NS; PS; F; 06/09/86
Citizens State Bank of Corpus Christi; Corpus Christi, TX; 50213260701-004; P; PS; F; 06/09/86
Citizens Trust Co; Coudersport, PA; 50213451901-001; P; M; F; 06/20/86
Citizens Trust Co; Coudersport, PA; 50213451901-002; P; PS; F; 06/20/86
City National Bank; Beverly Hills, CA; 50313638401-001; NS; M; F; 05/30/86
City National Bank; Beverly Hills, CA; 50213638401-002; P; M; F; 05/30/86
City National Bank; Beverly Hills, CA; 50313638401-003; NS; PS; F; 05/30/86
City National Bank; Beverly Hills, CA; 50213638401-004; P; PS; F; 05/30/86
City National Bank; Beverly Hills, CA; 50313638402-001; NS; D; F; 05/30/86
City National Bank; Beverly Hills, CA; 50213638402-002; P; D; F; 05/30/86
Colonial Bank; Waterbury, CT; 50214190003-001; P; M; F; 05/02/86
Colonial Bank; Waterbury, CT; 50214190003-002; P; PS; F; 05/02/86
Colorado Bank & Trust Co of La Junta; La Junta, CO; 50214310001-001; P; PS; F; 04/14/86
Colorado Bank & Trust Co of La Junta; La Junta, CO; 50214310001-002; P; M; F; 04/14/86
Colorado Bank & Trust Co of La Junta; La Junta, CO; 50314310001-003; NS; PS; F; 04/14/86
Colorado Bank & Trust Co of La Junta; La Junta, CO; 50314310001-004; NS; M; F; 04/14/86
Colorado State Bank; Denver, CO; 50214380001-001; P; PS; F; 04/14/86
Colorado State Bank; Denver, CO; 50214380001-002; P; M; F; 04/14/86
Columbus Mutual; Columbus, OH; 50214544001-001; P; M; F; 06/06/86
Columbus Mutual; Columbus, OH; 50214544001-002; P; PS; F; 06/06/86
Columbus Mutual; Columbus, OH; 50314544001-003; NS; M; F; 06/06/86
Columbus Mutual; Columbus, OH; 50314544001-004; NS; PS; F; 06/06/86
Columbus Mutual; Columbus, OH; 50214544002-001; P; D; F; 06/06/86
Columbus Mutual; Columbus, OH; 50214544002-002; P; D; F; 06/06/86
Columbus Mutual; Columbus, OH; 50314544002-003; NS; D; F; 06/06/86
Columbus Mutual; Columbus, OH; 50314544002-004; NS; D; F; 06/06/86
Companion Fund Inc; Bloomfield, CT; 50372907101-001; NS; M; F; 04/04/86
Companion Fund Inc; Bloomfield, CT; 50272907101-002; P; M; F; 04/04/86
Companion Fund Inc; Bloomfield, CT; 50372907101-003; NS; PS; F; 04/04/86
Companion Fund Inc; Bloomfield, CT; 50272907101-004; P; PS; F; 04/04/86
Companion Fund Inc; Bloomfield, CT; 50372907102-001; NS; D; F; 06/18/86
Companion Fund Inc; Bloomfield, CT; 50372907102-002; NS; D; F; 06/18/86
Companion Fund Inc; Bloomfield, CT; 50272907102-003; P; D; F; 06/18/86
Companion Fund Inc; Bloomfield, CT; 50272907102-004; P; D; F; 06/18/86
Companion Fund Inc; Bloomfield, CT; 50372907103-001; NS; T; F; 04/04/86
Companion Fund Inc; Bloomfield, CT; 50272907103-002; S; T; F; 04/04/86
Connecticut Bank & Trust Co NA; Hartfort, CT; 50215630002-001; S; M; F; 04/14/86
Connecticut Bank & Trust Co NA; Hartfort, CT; 50215630002-002; S; PS; F; 04/14/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50315627101-001; NS; D; F; 06/18/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50315627101-002; NS; D; F; 06/18/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50215627101-003; P; D; F; 06/18/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50215627101-004; P; D; F; 06/18/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50215627102-001; P; M; F; 04/04/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50315627102-002; NS; M; F; 04/04/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50215627102-003; P; PS; F; 04/04/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50315627102-004; NS; PS; F; 04/04/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50315627103-001; NS; T; F; 04/04/86
Connecticut General Life Insurance Co; Bloomfield, CT; 50215627103-002; S; T; F; 04/04/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50315670701-001; NS; M; F; 04/04/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50215670701-002; P; M; F; 04/04/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50315670701-003; NS; PS; F; 04/04/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50215670701-004; P; PS; F; 04/04/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50315670702-001; NS; D; F; 06/09/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50315670702-002; NS; D; F; 06/09/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50215670702-003; P; D; F; 06/09/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50215670702-004; P; D; F; 06/09/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50315670703-001; NS; T; F; 04/04/86
Connecticut Mutual Life Insurance Co; Hartford, CT; 50215670703-002; S; T; F; 04/04/86
Consolidated Financial Services Inc; Wilmington, DE; 50280418501-001; P; PS; U; 04/14/86
Consolidated Financial Services Inc; Wilmington, DE; 50280418501-002; P; M; U; 04/14/86
Consolidated Financial Services Inc; Wilmington, DE; 50280418502-001; P; D; U; 04/14/86
Consolidated Financial Services Inc; Wilmington, DE; 50280418502-002; P; D; U; 04/14/86
Consolidated Money Management Inc; Valley Forge, PA; 50280408501-001; P; PS; U; 04/14/86
Consolidated Money Management Inc; Valley Forge, PA; 50280408501-002; P; M; U; 04/14/86
Consolidated Money Management Inc; Valley Forge, PA; 50280408502-001; P; D; U; 04/14/86
Consolidated Money Management Inc; Valley Forge, PA; 50280408502-002; P; D; U; 04/14/86
Copley Tax Managed Fund Inc; Fall River, MA; 50215930001-001; S; PS; F; 05/19/86
Copley Tax Managed Fund Inc; Fall River, MA; 50215930001-002; S; PS; F; 05/19/86
Corporation Co of Delaware; Wilmington, DE; 50280428501-001; P; PS; U; 04/14/86
Corporation Co of Delaware; Wilmington, DE; 50280428501-002; P; M; U; 04/14/86
Corporation Co of Delaware; Wilmington, DE; 50280428502-001; P; D; U; 04/14/86
Corporation Co of Delaware; Wilmington, DE; 50280428502-002; P; D; U; 04/14/86
Criterion Funds; Houston, TX; 50268955001-003; P; PS; F; 04/14/86
Criterion Funds; Houston, TX; 50268955001-004; P; M; F; 04/14/86
Criterion Funds; Houston, TX; 50268955001-005; P; PS; F; 04/14/86
Criterion Funds; Houston, TX; 50268955001-006; P; M; F; 04/14/86
Criterion Funds; Houston, TX; 50268955001-007; P; PS; F; 04/14/86
Criterion Funds; Houston, TX; 50268955001-008; P; M; F; 04/14/86
Criterion Funds; Houston, TX; 50268955001-009; P; PS; F; 04/14/86
Criterion Funds; Houston, TX; 50268955001-010; P; M; F; 04/14/86
Crocker National Bank; San Diego, CA; 50216290001-001; P; PS; F; 04/28/86
Crocker National Bank; San Diego, CA; 50216290001-002; P; M; F; 04/28/86
Dain Bosworth Inc; Minneapolis, MN; 50216410002-001; S; PS; F; 04/17/86
Dain Bosworth Inc; Minneapolis, MN; 50216410002-002; S; PS; F; 04/17/86
Dain Bosworth Inc; Minneapolis, MN; 50216410003-001; S; M; F; 04/17/86
Dain Bosworth Inc; Minneapolis, MN; 50216410003-002; S; M; F; 04/17/86
De Kalb Bank; De Kalb, IL; 50316650001-001; NS; PS; F; 04/10/86
De Kalb Bank; De Kalb, IL; 50316650001-002; NS; M; F; 04/10/86
De Kalb Bank; De Kalb, IL; 50216652202-001; P; PS; F; 05/30/86
De Kalb Bank; De Kalb, IL; 50216652202-002; P; M; F; 05/30/86
Delaware Charter Co; Wilmington, DE; 50280438501-001; P; PS; U; 04/14/86
Delaware Charter Co; Wilmington, DE; 50280438501-002; P; M; U; 04/14/86
Delaware Charter Co; Wilmington, DE; 50280438502-001; P; D; U; 04/14/86
Delaware Charter Co; Wilmington, DE; 50280438502-002; P; D; U; 04/14/86
Delaware Charter Guarantee & Trust Co; Wilmington, DE; 50216680001-001; P; PS; F; 04/14/86
Delaware Charter Guarantee & Trust Co; Wilmington, DE; 50216680001-002; P; M; F; 04/14/86
Delaware Charter Guarantee & Trust Co; Wilmington, DE; 50216680002-001; P; D; F; 04/14/86
Delaware Charter Guarantee & Trust Co; Wilmington, DE; 50216680002-002; P; D; F; 04/14/86
Delaware Charter Insurance Inc; Wilmington, DE; 50280458501-001; P; PS; U; 04/14/86
Delaware Charter Insurance Inc; Wilmington, DE; 50280458501-002; P; M; U; 04/14/86
Delaware Charter Insurance Inc; Wilmington, DE; 50280458502-001; P; D; U; 04/14/86
Delaware Charter Insurance Inc; Wilmington, DE; 50280458502-002; P; D; U; 04/14/86
Delaware Incorporators Trust Co; Wilmington, DE; 50280448501-001; P; PS; U; 04/14/86
Delaware Incorporators Trust Co; Wilmington, DE; 50280448501-002; P; M; U; 04/14/86
Delaware Incorporators Trust Co; Wilmington, DE; 50280448502-001; P; D; U; 04/14/86
Delaware Incorporators Trust Co; Wilmington, DE; 50280448502-002; P; D; U; 04/14/86
Delaware Management Co Inc; Philadelphia, PA; 50216710001-001; P; PS; F; 04/14/86
Delaware Management Co Inc; Philadelphia, PA; 50216710001-002; P; M; F; 04/14/86
Delaware Management Co Inc; Philadelphia, PA; 50316710002-001; NS; PS; F; 04/14/86
Delaware Management Co Inc; Philadelphia, PA; 50316710003-001; NS; M; F; 04/14/86
Educators Life Insurance Co of America; Los Angeles, CA; 50372917101-001; NS; M; F; 04/04/86
Educators Life Insurance Co of America; Los Angeles, CA; 50272917101-002; P; M; F; 04/04/86
Educators Life Insurance Co of America; Los Angeles, CA; 50372917101-003; NS; PS; F; 04/04/86
Educators Life Insurance Co of America; Los Angeles, CA; 50272917101-004; P; PS; F; 04/04/86
Educators Life Insurance Co of America; Los Angeles, CA; 50372917102-001; NS; D; F; 06/18/86
Educators Life Insurance Co of America; Los Angeles, CA; 50372917102-002; NS; D; F; 06/18/86
Educators Life Insurance Co of America; Los Angeles, CA; 50272917102-003; P; D; F; 06/18/86
Educators Life Insurance Co of America; Los Angeles, CA; 50272917102-004; P; D; F; 06/18/86
Educators Life Insurance Co of America; Los Angeles, CA; 50372917103-001; NS; T; F; 04/04/86
Educators Life Insurance Co of America; Los Angeles, CA; 50272917103-002; S; T; F; 04/04/86
Fahnestock & Co Inc; New York, NY; 50218180001-001; P; M; F; 06/18/86
Fahnestock & Co Inc; New York, NY; 50218180001-002; P; PS; F; 06/18/86

Farmers Bank & Trust Co; Madisonville, KY; 50271540001-001; S; PS; F; 04/14/86
Farmers Bank & Trust Co; Madisonville, KY; 50271540001-002; S; PS; F; 04/14/86
Farmers Bank & Trust Co; Madisonville, KY; 50271540002-001; S; M; F; 04/14/86
Farmers Bank & Trust Co; Madisonville, KY; 50271540002-002; S; M; F; 04/14/86
Farmers New World Life Insurance Co; Mercer Island, WA; 50219100001-001; S; M; F; 04/17/86
Farmers State Bank; Fort Morgan, CO; 50319440001-001; NS; PS; F; 05/26/86
Farmers State Bank; Fort Morgan, CO; 50319440002-001; NS; M; F; 05/26/86
Farmers State Savings Bank; Independence, IA; 50281466901-001; S; PS; F; 06/23/86
Federal Home Life Insurance Co; Battle Creek, MI; 50319600001-001; NS; PS; F; 04/24/86
Federal Home Life Insurance Co; Battle Creek, MI; 50319600001-002; NS; PS; F; 04/24/86
Federal Home Life Insurance Co; Battle Creek, MI; 50319600002-001; NS; M; F; 04/24/86
Federal Home Life Insurance Co; Battle Creek, MI; 50319600002-002; NS; M; F; 04/24/86
Fidelity Bank; Philadelphia, PA; 50319760001-001; NS; PS; F; 04/14/86
Fidelity Bank; Philadelphia, PA; 50319760001-002; NS; M; F; 04/14/86
Fidelity Bank; Philadelphia, PA; 50219760002-001; P; PS; F; 04/07/86
Fidelity Bank; Philadelphia, PA; 50219760002-002; P; M; F; 04/07/86
Fidelity Bankers Life Insurance Co; Richmond, VA; 50219844001-001; P; M; F; 06/06/86
Fidelity Bankers Life Insurance Co; Richmond, VA; 50219844001-002; P; PS; F; 06/06/86
Fidelity Bankers Life Insurance Co; Richmond, VA; 50319844001-003; NS; M; F; 06/06/86
Fidelity Bankers Life Insurance Co; Richmond, VA; 50319844001-004; NS; PS; F; 06/06/86
Fidelity Bankers Life Insurance Co; Richmond, VA; 50219844002-001; P; D; F; 06/06/86
Fidelity Bankers Life Insurance Co; Richmond, VA; 50219844002-002; P; D; F; 06/06/86
Fidelity Bankers Life Insurance Co; Richmond, VA; 50319844002-003; NS; D; F; 06/06/86
Fidelity Bankers Life Insurance Co; Richmond, VA; 50319844002-004; NS; D; F; 06/06/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50373010701-001; NS; M; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010701-002; S; M; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50373010701-003; NS; PS; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010701-004; S; PS; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50373010702-001; NS; D; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50373010702-002; NS; D; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010702-003; S; D; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010702-004; S; D; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50373010703-001; NS; T; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010703-002; S; T; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50373010704-001; NS; M; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010704-002; P; M; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010704-003; P; M; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50373010704-004; NS; PS; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010704-005; P; PS; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010704-006; P; PS; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50373010705-001; NS; D; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50373010705-002; NS; D; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010705-003; P; D; F; 04/04/86
Fidelity Federal Savings & Loan Association; Glendale, CA; 50273010705-004; P; D; F; 04/04/86
Fidelity Mutual Life Insurance Co; Radnor, PA; 50319920001-001; NS; D; F; 06/27/86
Fidelity Mutual Life Insurance Co; Radnor, PA; 50319920001-002; NS; D; F; 06/27/86
Fidelity Mutual Life Insurance Co; Radnor, PA; 50219920001-003; P; D; F; 06/27/86
Fidelity Mutual Life Insurance Co; Radnor, PA; 50219920001-004; P; D; F; 06/27/86
Fidelity Mutual Life Insurance Co; Radnor, PA; 50219920002-002; P; M; F; 04/10/86
Fidelity Mutual Life Insurance Co; Radnor, PA; 50219920002-004; P; PS; F; 04/10/86
Financial Security Life Insurance Co; Lincoln, NE; 50320130001-001; NS; PS; F; 06/20/86
Financial Security Life Insurance Co; Lincoln, NE; 50320130002-001; NS; M; F; 06/20/86
First Benefit Trust Co of Texas; Dallas, TX; 50321230701-001; NS; PS; F; 04/14/86
First Benefit Trust Co of Texas; Dallas, TX; 50321230701-002; NS; M; F; 04/11/86
First Benefit Trust Co of Texas; Dallas, TX; 50221230001-003; P; PS; U; 04/28/86
First Benefit Trust Co of Texas; Dallas, TX; 50221230001-004; P; PS; U; 05/01/86
First Benefit Trust Co of Texas; Dallas, TX; 50321230702-001; NS; D; F; 04/14/86
First Benefit Trust Co of Texas; Dallas, TX; 50321230702-002; NS; D; F; 04/14/86
First Colony Life Insurance Co; Lynchburg, VA; 50274094001-001; P; M; F; 06/06/86
First Colony Life Insurance Co; Lynchburg, VA; 50274094001-002; P; PS; F; 06/06/86
First Colony Life Insurance Co; Lynchburg, VA; 50374094001-003; NS; M; F; 06/06/86
First Colony Life Insurance Co; Lynchburg, VA; 50374094001-004; NS; PS; F; 06/06/86
First Colony Life Insurance Co; Lynchburg, VA; 50274094002-001; P; D; F; 06/06/86
First Colony Life Insurance Co; Lynchburg, VA; 50274094002-002; P; D; F; 06/06/86
First Colony Life Insurance Co; Lynchburg, VA; 50374094002-003; NS; D; F; 06/06/86
First Colony Life Insurance Co; Lynchburg, VA; 50374094002-004; NS; D; F; 06/06/86
First International Bank of Watford City; Watford City, ND; 50281476901-001; S; PS; F; 06/23/86
First Interstate Bank of Denver; Denver, CO; 50321950001-001; NS; PS; F; 04/14/86
First Interstate Bank of Denver; Denver, CO; 50321950001-002; NS; M; F; 04/14/86
First Interstate Bank of Denver; Denver, CO; 50321950001-003; NS; M; F; 04/14/86
First Investors Corp; New York, NY; 50222020001-001; P; PS; F; 04/09/86
First Investors Corp; New York, NY; 50222020001-002; P; M; F; 04/09/86
First National Bank & Trust Co; Enid, OK; 50324820001-001; NS; PS; U; 05/30/86
First National Bank in Champaign; Champaign, IL; 50323550001-001; NS; PS; F; 04/28/86
First National Bank in Champaign; Champaign, IL; 50323550001-002; NS; M; F; 04/21/86
First National Bank in Champaign; Champaign, IL; 50223550002-001; P; PS; F; 04/18/86
First National Bank in Champaign; Champaign, IL; 50223550002-002; P; M; F; 04/18/86
First National Bank of Boston; Boston, MA; 50305190001-001; NS; M; F; 05/15/86
First National Bank of Boston; Boston, MA; 50205190001-002; P; M; F; 05/15/86
First National Bank of Boston; Boston, MA; 50205190001-003; P; M; F; 05/15/86
First National Bank of Boston; Boston, MA; 50305190001-004; NS; PS; F; 05/15/86
First National Bank of Boston; Boston, MA; 50205190001-005; P; PS; F; 05/15/86
First National Bank of Boston; Boston, MA; 50205190001-006; P; PS; F; 05/15/86
First National Bank of Gainesville; Gainesville, GA; 50324000702-001; NS; D; F; 06/09/86
First National Bank of Gainesville; Gainesville, GA; 50324000702-002; NS; D; F; 06/09/86
First National Bank of Gainesville; Gainesville, GA; 50224000702-003; P; D; F; 06/09/86
First National Bank of Gainesville; Gainesville, GA; 50224000702-004; P; D; F; 06/09/86
First National Bank of Huntingburg; Huntingburg, IN; 50270400001-001; P; PS; F; 05/12/86
First National Bank of Huntingburg; Huntingburg, IN; 50270400001-002; P; M; F; 05/12/86
First National Bank of Huntingburg; Huntingburg, IN; 50370400001-003; NS; PS; F; 05/12/86
First National Bank of Huntingburg; Huntingburg, IN; 50370400001-004; NS; M; F; 05/12/86
First National Bank of Mobile; Mobile, AL; 50225650001-001; P; PS; U; 06/30/86
First National Bank of Mobile; Mobile, AL; 50225650001-002; P; M; U; 06/30/86
First National Bank of Tipton; Tipton, IA; 50283866901-001; S; PS; F; 06/23/86
First National Montana Bank; Missoula, MT; 50371942201-001; NS; PS; F; 04/03/86
First National Montana Bank; Missoula, MT; 50371942201-002; NS; M; F; 04/03/86
First Trust & Savings Bank of Kankakee; Kankakee, IL; 50329040001-001; NS; PS; F; 04/10/86
First Trust & Savings Bank of Kankakee; Kankakee, IL; 50329040001-002; NS; M; F; 04/10/86
First Trust & Savings Bank of Kankakee; Kankakee, IL; 50229040002-001; P; PS; F; 04/18/86
First Trust & Savings Bank of Kankakee; Kankakee, IL; 50229040002-002; P; M; F; 04/18/86
First Trust Co; Jackson, MS; 50273030701-001; S; PS; U; 04/03/86
First Trust Corp; Denver, CO; 50229130001-001; P; PS; F; 05/30/86
First Trust Corp; Denver, CO; 50229130001-002; P; M; F; 05/30/86
First Trust Corp; Denver, CO; 50329130001-003; NS; PS; F; 05/30/86
First Trust Corp; Denver, CO; 50329130001-004; NS; M; F; 05/30/86
First Trust Corp; Denver, CO; 50329130001-005; NS; PS; F; 05/30/86
First Trust Corp; Denver, CO; 50329130001-006; NS; T; U; 04/30/86
First Valley Bank; Bethlehem, PA; 50229210001-001; P; PS; F; 05/30/86
First Valley Bank; Bethlehem, PA; 50229210001-002; P; M; F; 05/30/86
FMB-First Michigan Bank; Zeeland, MI; 50222150001-001; P; PS; F; 05/07/86
FMB-First Michigan Bank; Zeeland, MI; 50222150001-002; P; M; F; 05/07/86
FMB-Lumbermans Bank; Muskegon, MI; 50237940001-001; P; PS; F; 05/07/86
FMB-Lumbermans Bank; Muskegon, MI; 50237940001-002; P; M; F; 05/07/86
General American Life Insurance Co; St Louis, MO; 50330830001-001; NS; M; F; 04/14/86
General American Life Insurance Co; St Louis, MO; 50330830001-002; NS; T; F; 04/14/86
General American Life Insurance Co; St Louis, MO; 50330830001-003; NS; PS; F; 04/14/86
General American Life Insurance Co; St Louis, MO; 50230830001-004; P; M; F; 04/14/86
General American Life Insurance Co; St Louis, MO; 50230830001-005; P; T; F; 04/14/86
General American Life Insurance Co; St Louis, MO; 50230830001-006; P; PS; F; 04/14/86
General American Life Insurance Co; St Louis, MO; 50330830002-001; NS; D; F; 04/21/86
General American Life Insurance Co; St Louis, MO; 50330830002-002; NS; D; F; 04/21/86
General American Life Insurance Co; St Louis, MO; 50330830002-003; NS; D; F; 04/21/86
General American Life Insurance Co; St Louis, MO; 50230830002-004; P; D; F; 04/21/86
General American Life Insurance Co; St Louis, MO; 50230830002-005; P; D; F; 04/21/86
General American Life Insurance Co; St Louis, MO; 50230830002-006; P; D; F; 04/21/86
General American Life Insurance Co; St Louis, MO; 50330830003-001; NS; PS; F; 04/14/86
General American Life Insurance Co; St Louis, MO; 50330830003-002; NS; M; F; 04/14/86
General American Life Insurance Co; St Louis, MO; 50330830004-001; NS; PS; F; 04/14/86
General American Life Insurance Co; St Louis, MO; 50330830004-002; NS; M; F; 04/14/86
General Fidelity Life Insurance; Los Angeles, CA; 50380228401-001; NS; M; F; 05/30/86
General Fidelity Life Insurance; Los Angeles, CA; 50280228401-002; P; M; F; 05/30/86

General Fidelity Life Insurance; Los Angeles, CA; 50380228401-003; NS; PS; F; 05/30/86

General Fidelity Life Insurance; Los Angeles, CA; 50280228401-004, P; PS; F; 05/30/86

General Fidelity Life Insurance; Los Angeles, CA; 50380228402-001; NS; D; F; 05/30/86

General Fidelity Life Insurance; Los Angeles, CA; 50280228402-002; P; D; F; 05/30/86

Great West Life Assurance Co; Englewood, CO; 50231620002-001; P; PS; F; 05/09/86

Great West Life Assurance Co; Englewood, CO; 50231620002-002; P; M; F; 05/09/86

Great West Life Assurance Co; Englewood, CO; 50331620002-003; NS; PS; F; 05/09/86

Great West Life Assurance Co; Englewood, CO; 50331620002-004; NS; M; F; 05/09/86

Great West Life Assurance Co; Englewood, CO; 50331620002-005; NS; T; F; 05/09/86

Great Western Bank & Trust; Phoenix, AZ; 50331618401-001; NS; M; F; 05/30/86

Great Western Bank & Trust; Phoenix, AZ; 50231618401-002; P; M; F; 05/30/86

Great Western Bank & Trust; Phoenix, AZ; 50331618401-003; NS; PS; F; 05/30/86

Great Western Bank & Trust; Phoenix, AZ; 50231618401-004; P; PS; F; 05/30/86

Great Western Bank & Trust; Phoenix, AZ; 50331618402-001; NS; D; F; 05/30/86

Great Western Bank & Trust; Phoenix, AZ; 50231618402-002; P; D; F; 05/30/86

Guarantee Mutual Life Co; Omaha, NE; 50331920001-001; NS; M; F; 04/11/86

Guarantee Mutual Life Co; Omaha, NE; 50331920001-002; NS; M; F; 04/11/86

Guarantee Mutual Life Co; Omaha, NE; 50331920001-003; NS; PS; F; 04/11/86

Guarantee Mutual Life Co; Omaha, NE; 50331920001-004; NS; PS; F; 04/11/86

Guarantee Mutual Life Co; Omaha, NE; 50331920001-005; NS; PS; F; 04/11/86

Guarantee Mutual Life Co; Omaha, NE; 50331920001-006; NS; T; F; 04/11/86

Guarantee Mutual Life Co; Omaha, NE; 50231924002-001; P; M; F; 06/06/86

Guarantee Mutual Life Co; Omaha, NE; 50231924002-002; P; PS; F; 06/06/86

Guarantee Mutual Life Co; Omaha, NE; 50331924002-003; NS; M; F; 06/06/86

Guarantee Mutual Life Co; Omaha, NE; 50331924002-004; NS; PS; F; 06/06/86

Guarantee Mutual Life Co; Omaha, NE; 50231924003-001; P; D; F; 06/06/86

Guarantee Mutual Life Co; Omaha, NE; 50231924003-002; P; D; F; 06/06/86

Guarantee Mutual Life Co; Omaha, NE; 50331924003-003; NS; D; F; 06/06/86

Guarantee Mutual Life Co; Omaha, NE; 50331924003-004; NS; D; F; 06/06/86

Guaranty Bank & Trust Co; Alexandria, LA; 50332030001-001; NS; PS; F; 05/22/86

Guaranty Bank & Trust Co; Alexandria, LA; 50332030001-002; NS; PS; F; 05/22/86

Guaranty Bank & Trust Co; Alexandria, LA; 50332030001-003; NS; PS; F; 05/22/86

Guaranty Bank & Trust Co; Alexandria, LA; 50332030001-004; NS; M; F; 05/22/86

Guaranty Bank & Trust Co; Alexandria, LA; 50332030001-005; NS; M; F; 05/22/86

Guaranty Bank & Trust Co; Alexandria, LA; 50332030001-006; NS; M; F; 05/22/86

Guaranty Bank & Trust Co; Lafayette, LA; 50332040001-001; NS; PS; F; 05/19/86

Guaranty Bank & Trust Co; Lafayette, LA; 50232040001-002; P; PS; F; 05/19/86

Guaranty Bank & Trust Co; Lafayette, LA; 50332040001-003; NS; M; F; 05/19/86

Guaranty Bank & Trust Co; Lafayette, LA; 50232040001-004; P; M; F; 05/19/86

Guaranty Bank & Trust Co; Lafayette, LA; 50332040001-005; NS; T; F; 05/19/86

Gulf Life Insurance Co; Jacksonville, FL; 50232240001-001; S; M; F; 06/19/86

Gulf Life Insurance Co; Jacksonville, FL; 50232240001-002; S; PS; F; 06/19/86

Gulf Life Insurance Co; Jacksonville, FL; 50332240001-003; NS; M; F; 06/19/86

Gulf Life Insurance Co; Jacksonville, FL; 50332240001-004; NS; PS; F; 06/19/86

Hamilton Bank; Lancaster, PA; 50232350001-001; P; PS; F; 04/14/86

Hamilton Bank; Lancaster, PA; 50232350001-002; P; M; F; 04/14/86

Hamilton Bank; Lancaster, PA; 50332350001-003; NS; PS; F; 04/14/86

Hamilton Bank; Lancaster, PA; 50332350001-004; NS; M; F; 04/14/86

Hamilton Bank; Lancaster, PA; 50232350001-005; P; PS; F; 04/14/86

Hamilton Bank; Lancaster, PA; 50232350001-006; P; M; F; 04/14/86

Hamilton Bank; Lancaster, PA; 50332350001-007; NS; PS; F; 04/14/86

Hamilton Bank; Lancaster, PA; 50332350001-008; NS; M; F; 04/14/86

Harbor Trust Co; Hoboken, NJ; 50263440002-001; P; PS; F; 05/09/86

Harbor Trust Co; Hoboken, NJ; 50263440002-002; P; M; F; 05/09/86

Harbor Trust Co; Hoboken, NJ; 50363440002-003; NS; PS; F; 05/09/86

Harbor Trust Co; Hoboken, NJ; 50363440002-004; NS; M; F; 05/09/86

Hibernia National Bank in New Orleans; New Orleans, LA; 50233280002-001; P; PS; U; 06/13/86

Hibernia National Bank in New Orleans; New Orleans, LA; 50233280002-002; P; M; U; 06/13/86

Hibernia National Bank in New Orleans; New Orleans, LA; 50333280002-003; NS; PS; U; 06/13/86

Hibernia National Bank in New Orleans; New Orleans, LA; 50333280002-004; NS; M; U; 06/13/86

Home Bank & Trust Co; Meriden, CT; 50333540701-001; NS; M; F; 04/11/86

Home Bank & Trust Co; Meriden, CT; 50233540701-002; P; M; F; 04/11/86

Home Bank & Trust Co; Meriden, CT; 50333540701-003; NS; PS; F; 04/11/86

Home Bank & Trust Co; Meriden, CT; 50233540701-004; P; PS; F; 04/11/86

Home Fed Trust; San Diego, CA; 50371770001-001; NS; PS; F; 05/22/86

Home Fed Trust; San Diego, CA; 50371770001-002; NS; PS; F; 05/22/86

Home Fed Trust; San Diego, CA; 50371770001-003; NS; PS; F; 05/22/86

Home Fed Trust; San Diego, CA; 50371770001-004; NS; M; F; 05/22/86

Home Fed Trust; San Diego, CA; 50371770001-005; NS; M; F; 05/22/86

Home Fed Trust; San Diego, CA; 50371770001-006; NS; M; F; 05/22/86

Home Life Insurance Co; New York, NY; 50233630001-001; P; D; F; 06/13/86

Home Life Insurance Co; New York, NY; 50233630001-002; P; D; F; 06/13/86

Home Loan Associates; Chicago, IL; 50233670001-001; P; M; U; 06/02/86

Home Loan Associates; Chicago, IL; 50233670001-002; P; PS; U; 06/02/86

Horace Mann Life Insurance Co; Springfield, IL; 50333867101-001; NS; M; F; 04/04/86

Horace Mann Life Insurance Co; Springfield, IL; 50233867101-002; P; M; F; 04/04/86

Horace Mann Life Insurance Co; Springfield, IL; 50333867101-003; NS; PS; F; 04/04/86

Horace Mann Life Insurance Co; Springfield, IL; 50233867101-004; P; PS; F; 04/04/86

Horace Mann Life Insurance Co; Springfield, IL; 50333867102-001; NS; D; F; 06/18/86

Horace Mann Life Insurance Co; Springfield, IL; 50333867102-002; NS; D; F; 06/18/86

Horace Mann Life Insurance Co; Springfield, IL; 50233867102-003; P; D; F; 06/18/86

Horace Mann Life Insurance Co; Springfield, IL; 50233867102-004; P; D; F; 06/18/86

Horace Mann Life Insurance Co; Springfield, IL; 50333867103-001; NS; T; F; 04/04/86

Horace Mann Life Insurance Co; Springfield, IL; 50233867103-002; S; T; F; 04/04/86

Housatonic Bank & Trust Co; Ansonia, CT; 50271660001-001; P; M; F; 05/02/86

Housatonic Bank & Trust Co; Ansonia, CT; 50271660001-002; P; PS; F; 05/02/86

Howard Bank; Burlington, VT; 50233931902-001; S; PS; F; 04/21/86

Howard Bank; Burlington, VT; 50233931902-002; S; M; F; 04/21/86

Illinois Bankers Association; Chicago, IL; 50234110001-001; S; PS; F; 05/23/86

Illinois Bankers Association; Chicago, IL; 50234110001-002; S; PS; F; 05/23/86

Illinois Bankers Association; Chicago, IL; 50334110001-003; NS; PS; F; 05/23/86

Illinois Bankers Association; Chicago, IL; 50334110001-004; NS; PS; F; 05/23/86

Illinois Bankers Association; Chicago, IL; 50234110002-001; S; M; F; 05/23/86

Illinois Bankers Association; Chicago, IL; 50234110002-002; S; M; F; 05/23/86

Illinois Bankers Association; Chicago, IL; 50334110002-003; NS; M; F; 05/23/86

Illinois Bankers Association; Chicago, IL; 50334110002-004; NS; M; F; 05/23/86

Illinois Bankers Association; Chicago, IL; 50334110003-001; NS; D; F; 05/23/86

Illinois Bankers Association; Chicago, IL; 50334110003-002; NS; D; F; 05/23/86

Illinois Mutual Life & Casualty Co; Peoria, IL; 50334150701-001; NS; M; F; 04/04/86

Illinois Mutual Life & Casualty Co; Peoria, IL; 50234150701-002; P; M; F; 04/04/86

Illinois Mutual Life & Casualty Co; Peoria, IL; 50334150701-003; NS; PS; F; 04/04/86

Illinois Mutual Life & Casualty Co; Peoria, IL; 50234150701-004; P; PS; F; 04/04/86

Illinois National Bank of Springfield; Springfield, IL; 50334190001-001; NS; PS; F; 04/10/86

Illinois National Bank of Springfield; Springfield, IL; 50334190001-002; NS; M; F; 04/10/86

Illinois National Bank of Springfield; Springfield, IL; 50234190002-001; P; PS; F; 04/18/86

Illinois National Bank of Springfield; Springfield, IL; 50234190002-002; P; M; F; 04/18/86

INA Life Insurance Co; Los Angeles, CA; 50372887101-001; NS; M; F; 04/04/86

INA Life Insurance Co; Los Angeles, CA; 50272887101-002; P; M; F; 04/04/86

INA Life Insurance Co; Los Angeles, CA; 50372887101-003; NS; PS; F; 04/04/86

INA Life Insurance Co; Los Angeles, CA; 50272887101-004; P; PS; F; 04/04/86

INA Life Insurance Co; Los Angeles, CA; 50372887102-001; NS; D; F; 06/18/86

INA Life Insurance Co; Los Angeles, CA; 50372887102-002; NS; D; F; 06/18/86

INA Life Insurance Co; Los Angeles, CA; 50272887102-003; P; D; F; 06/18/86

INA Life Insurance Co; Los Angeles, CA; 50272887102-004; P; D; F; 06/18/86

INA Life Insurance Co; Los Angeles, CA; 50372887103-001; NS; T; F; 04/04/86

INA Life Insurance Co; Los Angeles, CA; 50272887103-002; S; T; F; 04/04/86

INA Life Insurance Co of New York; New York, NY; 50334307101-001; NS; M; F; 04/04/86

INA Life Insurance Co of New York; New York, NY; 50234307101-002; P; M; F; 04/07/86

INA Life Insurance Co of New York; New York, NY; 50334307101-003; NS; PS; F; 04/07/86

INA Life Insurance Co of New York; New York, NY; 50234307101-004; P; PS; F; 04/07/86

INA Life Insurance Co of New York; New York, NY; 50334307102-001; NS; D; F; 06/18/86

INA Life Insurance Co of New York; New York, NY; 50334307102-002; NS; D; F; 06/18/86

INA Life Insurance Co of New York; New York, NY; 50234307102-003; P; D; F; 06/18/86

INA Life Insurance Co of New York; New York, NY; 50234307102-004; P; D; F; 06/18/86

INA Life Insurance Co of New York; New York, NY; 50334307103-001; NS; T; F; 04/07/86

INA Life Insurance Co of New York; New York, NY; 50234307103-002; S; T; F; 04/04/86

Independence Bank; Encino, CA; 50334350001-001; NS; PS; U; 06/12/86

Independence Bank; Encino, CA; 50334350002-001; NS; M; U; 06/12/86

Indianapolis Life Insurance Co; Indianapolis, IN; 50234574001-001; P; M; F; 06/06/86

Indianapolis Life Insurance Co; Indianapolis, IN; 50234574001-002; P; PS; F; 06/06/86

Indianapolis Life Insurance Co; Indianapolis, IN; 50334574001-003; NS; M; F; 06/06/86

Indianapolis Life Insurance Co; Indianapolis, IN; 50334574001-004; NS; PS; F; 06/06/86
Indianapolis Life Insurance Co; Indianapolis, IN; 50234574002-001; P; D; F; 06/06/86
Indianapolis Life Insurance Co; Indianapolis, IN; 50234574002-002; P; D; F; 06/06/86
Indianapolis Life Insurance Co; Indianapolis, IN; 50334574002-003; NS; D; F; 06/06/86
Indianapolis Life Insurance Co; Indianapolis, IN; 50334574002-004; NS; D; F; 06/06/86
InterOcean Insurance Co; Cincinnati, OH; 50265760001-001; P; PS; F; 06/16/86
InterOcean Insurance Co; Cincinnati, OH; 50265760001-002; P; M; F; 06/16/86
InterOcean Insurance Co; Cincinnati, OH; 50265760001-003; P; T; F; 06/16/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50335197101-001; NS; M; F; 04/04/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50235197101-002; P; M; F; 04/04/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50335197101-003; NS; PS; F; 04/04/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50235197101-004; P; PS; F; 04/04/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50335197102-001; NS; D; F; 06/18/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50335197102-002; NS; D; F; 06/18/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50235197102-003; P; D; F; 06/18/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50235197102-004; P; D; F; 06/18/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50335197103-001; NS; T; F; 04/04/86
Investors Life Insurance Co of North America; Philadelphia, PA; 50235197103-002; S; T; F; 04/04/86
Iowa Bankers Association; Des Moines, IA; 50335220002-001; NS; D; F; 06/30/86
Iowa Bankers Association; Des Moines, IA; 50335220002-002; NS; D; F; 06/30/86
Iowa State Bank; Algona, IA; 50235232201-003; S; PS; F; 04/07/86
Iowa State Bank; Algona, IA; 50235232201-004; S; M; F; 04/07/86
Irwin Union Bank & Trust Co; Columbus, IN; 50235310001-001; P; PS; F; 05/19/86
Irwin Union Bank & Trust Co; Columbus, IN; 50235310001-002; P; M; F; 05/19/86
Irwin Union Bank & Trust Co; Columbus, IN; 50335310001-003; NS; PS; F; 05/19/86
Irwin Union Bank & Trust Co; Columbus, IN; 50335310001-004; NS; M; F; 05/19/86
Istel Fund Inc; New York, NY; 50235340701-001; P; M; F; 04/11/86
Istel Fund Inc; New York, NY; 50235340701-002; P; PS; F; 04/11/86
Janus Fund Inc; Denver, CO; 50235515001-001; P; PS; F; 04/21/86
Janus Fund Inc; Denver, CO; 50235515001-002; P; M; F; 04/21/86
Jefferson Bank & Trust Co; Lakewood, CO; 50235540001-001; P; PS; F; 04/14/86
Jefferson Bank & Trust Co; Lakewood, CO; 50235540001-002; P; M; F; 04/14/86
Jefferson Bank & Trust Co; Lakewood, CO; 50335540001-003; NS; PS; F; 04/14/86
Jefferson Bank & Trust Co; Lakewood, CO; 50335540001-004; NS; M; F; 04/14/86
Jefferson National Life Insurance Co; Indianapolis, IN; 50235570001-001; S; M; F; 05/26/86
Jefferson National Life Insurance Co; Indianapolis, IN; 50235570001-002; S; PS; F; 05/26/86
Jefferson National Life Insurance Co; Indianapolis, IN; 50335570001-003; NS; M; F; 05/26/86
Jefferson National Life Insurance Co; Indianapolis, IN; 50335570001-004; NS; PS; F; 05/26/86
Jefferson National Life Insurance Co; Indianapolis, IN; 50235570002-001; S; D; F; 05/26/86
Jefferson National Life Insurance Co; Indianapolis, IN; 50235570002-002; S; D; F; 05/26/86
Jefferson National Life Insurance Co; Indianapolis, IN; 50335570002-003; NS; D; F; 05/26/86
Jefferson National Life Insurance Co; Indianapolis, IN; 50335570002-004; NS; D; F; 05/26/86
John Alden Life Insurance Co of New York; New York, NY; 50365870001-001; NS; M; F; 06/02/86
John Hancock Distributors Inc; Boston, MA; 50235660001-001, S; M; F; 04/14/86
John Hancock Distributors Inc; Boston, MA; 50235660001-002; S; T; F; 04/14/86
Jones Mathers Casamento & Co Inc; Metairie, LA; 50373050701-001; NS; M; F; 04/11/86
Jones Mathers Casamento & Co Inc; Metairie, LA; 50273050701-002; P; M; F; 04/11/86
Jones Mathers Casamento & Co Inc; Metairie, LA; 50373050701-003; NS; PS; F; 04/11/86
Jones Mathers Casamento & Co Inc; Metairie, LA; 50273050701-004; P; PS; F; 04/11/86
Kemper Financial Services Inc; Chicago, IL; 50235999201-001; S; PS; U; 06/05/86
Kemper Financial Services Inc; Chicago, IL; 50235999201-002; S; M; U; 06/05/86
Kemper Financial Services Inc; Chicago, IL; 50335999201-003; NS; PS; U; 06/05/86
Kemper Financial Services Inc; Chicago, IL; 50335999201-004; NS; M; U; 06/05/86
Kentucky Central Life Insurance Co; Lexington, KY; 50336090701-001; NS; M; F; 06/11/86
Kentucky Central Life Insurance Co; Lexington, KY; 50236090701-002; P; M; F; 06/11/86
Kentucky Central Life Insurance Co; Lexington, KY; 50336090701-003; NS; PS; F; 06/11/86
Kentucky Central Life Insurance Co; Lexington, KY; 50236090701-004; P; PS; F; 06/11/86
Keystone National Bank; Punxsutawney, PA; 50271760001-001; P; PS; F; 05/02/86
Keystone National Bank; Punxsutawney, PA; 50271760001-002; P; M; F; 05/02/86
Lakeside National Bank of Lake Charles; Lake Charles, LA; 50236590001-001; S; PS; F; 04/18/86
Lakeside National Bank of Lake Charles; Lake Charles, LA; 50236590001-002; S; PS; F; 04/18/86
Lakeside National Bank of Lake Charles; Lake Charles, LA; 50336590001-003; NS; PS; F; 04/18/86
Lakeside National Bank of Lake Charles; Lake Charles, LA; 50336590001-004; NS; PS; F; 04/18/86
Lamar Life Insurance Co; Jackson, MS; 50336640701-001; NS; M; F; 06/09/86
Lamar Life Insurance Co; Jackson, MS; 50236640701-002; P; M; F; 06/09/86
Lamar Life Insurance Co; Jackson, MS; 50336640701-003; NS; PS; F; 06/09/86
Lamar Life Insurance Co; Jackson, MS; 50236640701-004; P; PS; F; 06/09/86
Life Insurance Co of North America; Philadelphia, PA; 50337347102-001; NS; D; F; 06/18/86
Life Insurance Co of North America; Philadelphia, PA; 50337347102-002; NS; D; F; 06/18/86
Life Insurance Co of North America; Philadelphia, PA; 50237347102-003; P; D; F; 06/18/86
Life Insurance Co of North America; Philadelphia, PA; 50237347102-004; P; D; F; 06/18/86
Life Insurance Co of North America; Philadelphia, PA; 50337347103-001; NS; T; F; 04/09/86
Life Insurance Co of North America; Philadelphia, PA; 50237347103-002; S; T; F; 04/09/86
Life Insurance Co of North America; Philadelphia, PA; 50337347104-001; NS; M; F; 04/09/86
Life Insurance Co of North America; Philadelphia, PA; 50237347104-002; S; M; F; 04/09/86
Life Insurance Co of North America; Philadelphia, PA; 50337347104-003; NS; PS; F; 04/09/86
Life Insurance Co of North America; Philadelphia, PA; 50237347104-004; P; PS; F; 04/09/86
Life Insurance of Cincinnati; Cincinnati, OH; 50266160001-001; P; PS; F; 06/16/86
Life Insurance of Cincinnati; Cincinnati, OH; 50266160001-002; P; M; F; 06/16/86
Life Insurance of Cincinnati; Cincinnati, OH; 50266160001-003; P; T; F; 06/16/86
Lincoln Benefit Life Co; Lincoln, NE; 50337480001-001; NS; PS; F; 06/20/86
Lincoln Benefit Life Co; Lincoln, NE; 50337480002-001; NS; M; F; 06/20/86
Lincoln Life & Casualty Co; Lincoln, NE; 50337550001-001; NS; PS; F; 06/20/86
Lincoln Life & Casualty Co; Lincoln, NE; 50337550002-001; NS; M; F; 06/20/86
Lincoln Mutual Life Insurance Co; Lincoln, NE; 50237560001-001; S; M; F; 06/02/86
Loomis Sayles & Co Inc; Boston, MA; 50237775001-001; P; PS; F; 04/21/86
Manufacturers & Traders Trust Co; Buffalo, NY; 50338380001-001; NS; M; F; 04/14/86
Manufacturers & Traders Trust Co; Buffalo, NY; 50338380001-002; NS; M; F; 04/14/86
Manufacturers & Traders Trust Co; Buffalo, NY; 50338380001-003; NS; PS; F; 04/14/86
Manufacturers & Traders Trust Co; Buffalo, NY; 50338380001-004; NS; PS; F; 04/14/86
Maryland National Bank; Baltimore, MD; 50338750001-001; NS; PS; F; 06/20/86
Maryland National Bank; Baltimore, MD; 50338750001-002; NS; PS; F; 06/20/86
Maryland National Bank; Baltimore, MD; 50338750002-001; NS; M; F; 06/20/86
Maryland National Bank; Baltimore, MD; 50338750002-002; NS; M; F; 06/20/86
Maryland National Bank; Baltimore, MD; 50238750003-001; P; PS; F; 06/23/86
Maryland National Bank; Baltimore, MD; 50238750003-002; P; M; F; 06/23/86
Massachusetts Financial Services Co; Boston, MA; 50238800001-001; P; PS; F; 05/26/86
Massachusetts Financial Services Co; Boston, MA; 50338800001-002; NS; PS; F; 05/26/86
Massachusetts Financial Services Co; Boston, MA; 50238800001-003; P; M; F; 05/26/86
Massachusetts Financial Services Co; Boston, MA; 50338800001-004; NS; M; F; 05/26/86
Massachusetts Investors Trust; Boston, MA; 50238774401-001; P; D; F; 05/09/86
Massachusetts Investors Trust; Boston, MA; 50238774401-002; P; D; F; 05/09/86
Massachusetts Investors Trust; Boston, MA; 50238774401-003; P; D; F; 05/09/86
Massachusetts Investors Trust; Boston, MA; 50238774401-004; P; D; F; 05/09/86
Massachusetts Investors Trust; Boston, MA; 50238774402-001; P; PS; F; 05/09/86
Massachusetts Investors Trust; Boston, MA; 50238774402-002; P; PS; F; 05/09/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830001-001; NS; PS; F; 04/18/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830001-002; NS; M; F; 04/18/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830002-001; NS; PS; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830002-002; NS; PS; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50238830002-003; S; PS; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50238830002-004; S; PS; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830002-005; NS; M; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830002-006; NS; M; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50238830002-007; S; M; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50238830002-008; S; M; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830002-009; NS; T; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50338830002-010; NS; T; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50238830002-011; S; T; F; 04/28/86
Massachusetts Mutual Life Insurance Co; Springfield, MA; 50238830002-012; S; T; F; 04/28/86
Master Life Insurance Co; Phoenix, AZ; 50372897101-001; NS; M; F; 04/04/86
Master Life Insurance Co; Phoenix, AZ; 50272897101-002; P; M; F; 04/04/86
Master Life Insurance Co; Phoenix, AZ; 50372897101-003; NS; PS; F; 04/04/86
Master Life Insurance Co; Phoenix, AZ; 50272897101-004; P; PS; F; 04/04/86
Master Life Insurance Co, Phoenix, AZ; 50372897102-001; NS; D; F; 06/18/86
Master Life Insurance Co; Phoenix, AZ; 50372897102-002; NS; D; F; 06/18/86
Master Life Insurance Co; Phoenix, AZ; 50272897102-003; P; D; F; 06/18/86
Master Life Insurance Co; Phoenix, AZ; 50272897102-004; P; D; F; 06/18/86
Master Life Insurance Co; Phoenix, AZ; 50372897103-001; NS; T; F; 04/04/86
Master Life Insurance Co; Phoenix, AZ; 50272897103-002; S; T; F; 04/04/86
MBank Bassett NA; El Paso, TX; 50307760001-001; NS; M; F; 05/01/86

MBank Bassett NA; El Paso, TX; 50307760002-001; NS; PS; F; 05/01/86

MBank El Paso NA; El Paso, TX; 50353760001-001; NS; M; F; 05/01/86

MBank El Paso NA; El Paso, TX; 50353760002-001; NS; PS; F; 05/01/86

MBank El Paso West NA; El Paso, TX; 50353800001-001; NS; M; F; 05/01/86

MBank El Paso West NA; El Paso, TX; 50353800002-001; NS; PS; F; 05/01/86

MBank Franklin NA; El Paso, TX; 50330320001-001; NS; M; F; 05/01/86

MBank Franklin NA; El Paso, TX; 50330320002-001; NS; PS; F; 05/01/86

MBank Odessa NA; Odessa, TX; 50355350001-001; NS; PS; F; 04/21/86

MBank Vista Hills NA; El Paso, TX; 50360830001-001; NS; M; F; 05/01/86

MBank Vista Hills NA; El Paso, TX; 50360830002-001; NS; PS; F; 05/01/86

MedServ Inc; Hartford, CT; 50271700001-001; S; M; F; 05/02/86

MedServ Inc; Hartford, CT; 50271700001-002; S; PS; F; 05/02/86

Merchants State Bank; Dallas, TX; 50263970001-001; P; PS; F; 05/09/86

Merchants State Bank; Dallas, TX; 50263970002-001; P; M; F; 05/09/86

Michigan Hospital Association Service Corp; Lansing, MI; 50370530001-001; NS; D; F; 05/26/86

Michigan Hospital Association Service Corp; Lansing, MI; 50370530001-002; NS; D; F; 05/26/86

Michigan Hospital Association Service Corp; Lansing, MI; 50370530001-003; NS; D; F; 05/26/86

Michigan National Bank of Detroit; Detroit, MI; 50340150001-001; NS; PS; F; 05/07/86

Michigan National Bank of Detroit; Detroit, MI; 50240150001-002; S; PS; F; 05/07/86

Michigan National Bank of Detroit; Detroit, MI; 50340150001-003; NS; M; F; 05/07/86

Michigan National Bank of Detroit; Detroit, MI; 50240150001-004; S; M; F; 05/07/86

Midwestern United Life Insurance Co; Fort Wayne, IN; 50340670001-001; NS; PS; F; 04/14/86

Midwestern United Life Insurance Co; Fort Wayne, IN; 50340670001-002; NS; M; F; 04/14/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400001-001; NS; M; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400001-002; NS; M; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50241400001-003; S; M; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50241400001-004; S; M; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400002-001; NS; PS; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400002-002; NS; PS; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50241400002-003; S; PS; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50241400002-004; S; PS; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400003-001; NS; T; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400003-002; NS; T; F; 06/02/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400004-001; NS; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400004-002; NS; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400004-003; NS; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400004-004; NS; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400004-005; NS; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400004-006; NS; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50341400004-007; NS; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50241400004-008; S; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50241400004-009; S; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50241400004-010; S; D; F; 06/30/86

Mutual Benefit Life Insurance Co; Newark, NJ; 50241400004-011; S; D; F; 06/30/86

Mutual Benefit Trust Co; Providence, RI; 50266840001-001; P; PS; F; 04/10/86

Mutual Benefit Trust Co; Providence, RI; 50266840001-002; P; M; F; 04/10/86

National Federation of Independent Business; San Mateo, CA; 50342420001-001; NS; PS; F; 06/02/86

National Federation of Independent Business; San Mateo, CA; 50342420001-002; NS; PS; F; 06/02/86

National Federation of Independent Business; San Mateo, CA; 50342420001-003; NS; M; F; 06/02/86

National Federation of Independent Business; San Mateo, CA; 50342420001-004; NS; M; F; 06/02/86

National Federation of Independent Business; San Mateo, CA; 50342420001-005; NS; T; F; 06/02/86

National Federation of Independent Business; San Mateo, CA; 50342420001-006; NS; T; F; 06/02/86

National Federation of Independent Business; San Mateo, CA; 50342420002-001; NS; D; F; 06/30/86

National Federation of Independent Business; San Mateo, CA; 50342420002-002; NS; D; F; 06/30/86

New Milford Bank & Trust Co; New Milford, CT; 50243110001-001; P; M; F; 05/02/86

New Milford Bank & Trust Co; New Milford, CT; 50243110001-002; P; PS; F; 05/02/86

North American Bank & Trust Co; Stratford, CT; 50243360001-001; P; M; F; 05/02/86

North American Bank & Trust Co; Stratford, CT; 50243360001-002; P; PS; F; 05/02/86

Northwest National Bank of Chicago; Chicago, IL; 50244066902-001; P; M; F; 04/03/86

Northwest National Bank of Chicago; Chicago, IL; 50244066902-002; P; PS; F; 04/03/86

Ohio Co; Columbus, OH; 50244685002-003; P; PS; F; 04/11/86

Ohio Co; Columbus, OH; 50244685002-004; P; M; F; 04/11/86

Ohio State Life Insurance Co; Columbus, OH; 50244764001-001; P; M; F; 06/06/86

Ohio State Life Insurance Co; Columbus, OH; 50244764001-002; P; PS; F; 06/06/86

Ohio State Life Insurance Co; Columbus, OH; 50344764001-003; NS; M; F; 06/06/86

Ohio State Life Insurance Co; Columbus, OH; 50344764001-004; NS; PS; F; 06/06/86

Ohio State Life Insurance Co; Columbus, OH; 50244764002-001; P; D; F; 06/06/86

Ohio State Life Insurance Co; Columbus, OH; 50244764002-002; P; D; F; 06/06/86

Ohio State Life Insurance Co; Columbus, OH; 50344764002-003; NS; D; F; 06/06/86

Ohio State Life Insurance Co; Columbus, OH; 50344764002-004; NS; D; F; 06/06/86

Olney Trust Bank; Olney, IL; 50273060701-001; S; PS; F; 06/09/86

Olney Trust Bank; Olney, IL; 50373060701-002; NS; PS; U; 06/09/86

Ozark National Life Insurance Co; Kansas City, MO; 50245440001-001; S; M; F; 06/16/86

Ozark National Life Insurance Co; Kansas City, MO; 50245440001-002; S; PS; F; 06/16/86

Ozark National Life Insurance Co; Kansas City, MO; 50345440002-001; NS; M; F; 06/16/86

Pacific Century Group; Los Angeles, CA; 50380238401-001; NS; M; F; 05/30/86

Pacific Century Group; Los Angeles, CA; 50280238401-002; P; M; F; 05/30/86

Pacific Century Group; Los Angeles, CA; 50380238401-003; NS; PS; F; 05/30/86

Pacific Century Group; Los Angeles, CA; 50280238401-004; P; PS; F; 05/30/86

Pacific Century Group; Los Angeles, CA; 50380238402-001; NS; D; F; 05/30/86

Pacific Century Group; Los Angeles, CA; 50280238402-002; P; D; F; 05/30/86

Pacific Mutual Life Insurance Co; Newport Beach, CA; 50245564003-001; P; M; F; 06/06/86

Pacific Mutual Life Insurance Co; Newport Beach, CA; 50245564003-002; P; PS; F; 06/06/86

Pacific Mutual Life Insurance Co; Newport Beach, CA; 50345564003-003; NS; M; F; 06/06/86

Pacific Mutual Life Insurance Co; Newport Beach, CA; 50345564003-004; NS; PS; F; 06/06/86

Pacific Mutual Life Insurance Co; Newport Beach, CA; 50245564004-001; P; D; F; 06/06/86

Pacific Mutual Life Insurance Co; Newport Beach, CA; 50245564004-002; P; D; F; 06/06/86

Pacific Mutual Life Insurance Co; Newport Beach, CA; 50345564004-003; NS; D; F; 06/06/86

Pacific Mutual Life Insurance Co; Newport Beach, CA; 50345564004-004; NS; D; F; 06/06/86

Packers National Bank in Omaha; Omaha, NE; 50345640001-001; NS; PS; F; 06/30/86

PHF Life Insurance Co; Battle Creek, MI; 50347340001-001; NS; PS; F; 04/24/86

PHF Life Insurance Co; Battle Creek, MI; 50347340001-002; NS; PS; F; 04/24/86

PHF Life Insurance Co; Battle Creek, MI; 50347340002-001; NS; M; F; 04/24/86

PHF Life Insurance Co; Battle Creek, MI; 50347340002-002; NS; M; F; 04/24/86

Pioneer Bank & Trust Co; St Louis, MO; 50247610001-001; S; PS; F; 06/02/86

Pioneer Bank & Trust Co; St Louis, MO; 50247610001-002; S; PS; F; 06/02/86

Pioneer Bank & Trust Co; St Louis, MO; 50347610001-003; NS; PS; F; 06/02/86

Pioneer Bank & Trust Co; St Louis, MO; 50347610001-004; NS; PS; F; 06/02/86

Pioneer Bank & Trust Co; St Louis, MO; 50247610002-001; S; M; F; 06/02/86

Pioneer Bank & Trust Co; St Louis, MO; 50247610002-002; S; M; F; 06/02/86

Pioneer Bank & Trust Co; St Louis, MO; 50347610002-003; NS; M; F; 06/02/86

Pioneer Bank & Trust Co; St Louis, MO; 50347610002-004; NS; M; F; 06/02/86

Providence Life Insurance Co; Johnston, RI; 50271720001-001; S; M; F; 06/18/86

Providence Life Insurance Co; Johnston, RI; 50271720001-002; S; PS; F; 06/18/86

Putnam Trust Co of Greenwich; Greenwich, CT; 50248700001-001; P; M; F; 05/02/86

Putnam Trust Co of Greenwich; Greenwich, CT; 50248700001-002; P; PS; F; 05/02/86

Rainier Bank Alaska NA; Anchorage, AK; 50346430001-001; NS; PS; F; 04/18/86

Rainier Bank Alaska NA; Anchorage, AK; 50346430001-002; NS; PS; F; 04/18/86

Rainier Bank Alaska NA; Anchorage, AK; 50346430001-003; NS; M; F; 04/18/86

Rainier Bank Alaska NA; Anchorage, AK; 50346430001-004; NS; M; F; 04/18/86

Rainier Bank Alaska NA; Anchorage, AK; 50246430001-005; S; PS; F; 04/18/86

Rainier Bank Alaska NA; Anchorage, AK; 50246430001-006; S; PS; F; 04/18/86

Rainier Bank Alaska NA; Anchorage, AK; 50246430001-007; S; M; F; 04/18/86

Rainier Bank Alaska NA; Anchorage, AK; 50246430001-008; S; M; F; 04/18/86

Resources Life Insurance Co; Fort Lee, NJ; 50367870001-001; NS; M; F; 06/23/86

Resources Life Insurance Co; Fort Lee, NJ; 50367870001-002; NS; M; F; 06/23/86

Resources Life Insurance Co; Fort Lee, NJ; 50367870002-001; NS; PS; F; 06/23/86

Resources Life Insurance Co; Fort Lee, NJ; 50367870002-002; NS; PS; F; 06/23/86

Resources Life Insurance Co; Fort Lee, NJ; 50367870003-001; NS; D; F; 05/29/86

Resources Life Insurance Co; Fort Lee, NJ; 50367870003-002; NS; D; F; 05/29/86

Resources Life Insurance Co; Fort Lee, NJ; 50367870004-001; NS; T; F; 06/23/86

Resources Life Insurance Co; Fort Lee, NJ; 50367870004-002; NS; T; F; 06/23/86

Resources Life Insurance Co; Fort Lee, NJ; 50267870005-001; S; M; F; 06/18/86

Resources Life Insurance Co; Fort Lee, NJ; 50267870005-002; S; PS; F; 06/18/86

Resources Trust Co; Englewood, CO; 50249410001-001; P; PS; F; 04/14/86

Resources Trust Co; Englewood, CO; 50249410001-002; P; M; F; 04/14/86

Resources Trust Co; Englewood, CO; 50349410001-003; NS; PS; F; 04/14/86

Resources Trust Co; Englewood, CO; 50349410001-004; NS; M; F; 04/14/86

Resources Trust Co; Englewood, CO; 50349410001-005; NS; T; F; 04/14/86

San Diego Trust & Savings Bank; San Diego, CA; 50250110001-001; P; M; F; 04/17/86

San Diego Trust & Savings Bank; San Diego, CA; 50250110001-002; P; M; F; 04/17/86

San Diego Trust & Savings Bank; San Diego, CA; 50250110001-003; P; PS; F; 04/18/86

San Diego Trust & Savings Bank; San Diego, CA; 50250110001-004; P; PS; F; 04/18/86

San Diego Trust & Savings Bank; San Diego, CA; 50350110001-005; NS; M; F; 04/18/86

San Diego Trust & Savings Bank; San Diego, CA; 50350110001-006; NS; M; F; 04/18/86

San Diego Trust & Savings Bank; San Diego, CA; 50350110001-007; NS; PS; F; 04/18/86

San Diego Trust & Savings Bank; San Diego, CA; 50350110001-008; NS; PS; F; 04/18/86

San Diego Trust & Savings Bank; San Diego, CA; 50250110002-001; P; D; F; 06/20/86

San Diego Trust & Savings Bank; San Diego, CA; 50250110002-002; P; D; F; 06/20/86

San Diego Trust & Savings Bank; San Diego, CA; 50250110002-003; P; D; F; 06/20/86

San Diego Trust & Savings Bank; San Diego, CA; 50350110002-004; NS; D; F; 06/20/86

San Diego Trust & Savings Bank; San Diego, CA; 50350110002-005; NS; D; F; 06/20/86

San Diego Trust & Savings Bank; San Diego, CA; 50350110002-006; NS; D; F; 06/20/86

Savings Fund Society of Germantown & Its Vicinity; Bala Cynwyd, PA; 50231070001-001; P; PS; F; 06/02/86

Savings Fund Society of Germantown & Its Vicinity; Bala Cynwyd, PA; 50231070001-002; P; M; F; 06/02/86

Seattle First National Bank; Seattle, WA; 50350570001-001; NS; M; F; 06/23/86

Seattle First National Bank; Seattle, WA; 50350570001-002; NS; M; F; 06/23/86

Seattle First National Bank; Seattle, WA; 50350570001-003; NS; PS; F; 06/23/86

Seattle First National Bank; Seattle, WA; 50350570001-004; NS; PS; F; 06/23/86

Seattle First National Bank; Seattle, WA; 50350570001-005; NS; M; F; 06/23/86

Seattle First National Bank; Seattle, WA; 50350570001-006; NS; M; F; 06/23/86

Seattle First National Bank; Seattle, WA; 50350570001-007; NS; PS; F; 06/23/86

Seattle First National Bank; Seattle, WA; 50350570001-008; NS; PS; F; 06/23/86

Seattle First National Bank; Seattle, WA; 50250570002-001; S; PS; F; 06/23/86

Seattle First National Bank; Seattle, WA; 50250570002-002; S; M; F; 06/23/86

Security Benefit Life Insurance Co; Topeka, KS; 50350810701-001; NS; M; F; 04/04/86

Security Benefit Life Insurance Co; Topeka, KS; 50250810701-002; P; M; F; 04/04/86

Security Benefit Life Insurance Co; Topeka, KS; 50350810701-003; NS; PS; F; 04/04/86

Security Benefit Life Insurance Co; Topeka, KS; 50250810701-004; P; PS; F; 04/04/86

Security Benefit Life Insurance Co; Topeka, KS; 50350810702-001; NS; D; F; 04/04/86

Security Benefit Life Insurance Co; Topeka, KS; 50350810702-002; NS; D; F; 04/04/86

Security Benefit Life Insurance Co; Topeka, KS; 50250810702-003; P; D; F; 04/04/86

Security Benefit Life Insurance Co; Topeka, KS; 50250810702-004; P; D; F; 04/04/86

Security Benefit Life Insurance Co; Topeka, KS; 50350810703-001; NS; T; F; 04/04/86

Security Benefit Life Insurance Co; Topeka, KS; 50250810703-002; S; T; F; 04/04/86

Security National Bank of Sioux City Iowa; Sioux City, IA; 50250980001-001; S; PS; U; 08/23/85

Security National Bank of Sioux City Iowa; Sioux City, IA; 50250980001-002; S; PS; U; 08/23/85

Security National Bank of Sioux City Iowa; Sioux City, IA; 50250980001-003; S; M; U; 08/23/85

Security National Bank of Sioux City Iowa; Sioux City, IA; 50250980001-004; S; M; U; 08/23/85

Security National Bank of Sioux City Iowa; Sioux City, IA; 50250980002-001; S; PS; U; 08/23/85

Security National Bank of Sioux City Iowa; Sioux City, IA; 50250980002-002; S; PS; U; 08/23/85

Security National Bank of Sioux City Iowa; Sioux City, IA; 50250980002-003; S; M; U; 08/23/85

Security National Bank of Sioux City Iowa; Sioux City, IA; 50250980002-004; S; M; U; 08/23/85

Security Pacific Investment Managers Inc; Los Angeles, CA; 50380258401-001; NS; M; F; 05/30/86

Security Pacific Investment Managers Inc; Los Angeles, CA; 50280258401-002; P; M; F; 05/30/86

Security Pacific Investment Managers Inc; Los Angeles, CA; 50380258401-003; NS; PS; F; 05/30/86

Security Pacific Investment Managers Inc; Los Angeles, CA; 50280258401-004; P; PS; F; 05/30/86

Security Pacific Investment Managers Inc; Los Angeles, CA; 50380258402-001; NS; D; F; 05/30/86

Security Pacific Investment Managers Inc; Los Angeles, CA; 50280258402-002; P; D; F; 05/30/86

Security Pacific National Bank; Los Angeles, CA; 50351028401-001; NS; M; F; 05/30/86

Security Pacific National Bank; Los Angeles, CA; 50251028401-002; P; M; F; 05/30/86

Security Pacific National Bank; Los Angeles, CA; 50351028401-003; NS; PS; F; 05/30/86

Security Pacific National Bank; Los Angeles, CA; 50251028401-004; P; PS; F; 05/30/86

Security Pacific National Bank; Los Angeles, CA; 50351028402-001; NS; D; F; 05/30/86

Security Pacific National Bank; Los Angeles, CA; 50251028402-002; P; D; F; 05/30/86

Security Pacific National Trust Co; Los Angeles, CA; 50380248401-001; NS; M; F; 05/30/86

Security Pacific National Trust Co; Los Angeles, CA; 50280248401-002; P; M; F; 05/30/86

Security Pacific National Trust Co; Los Angeles, CA; 50380248401-003; NS; PS; F; 05/30/86

Security Pacific National Trust Co; Los Angeles, CA; 50280248401-004; P; PS; F; 05/30/86

Security Pacific National Trust Co; Los Angeles, CA; 50380248402-001; NS; D; F; 05/30/86

Security Pacific National Trust Co; Los Angeles, CA; 50280248402-002; P; D; F; 05/30/86

Security Savings Bank; Marshalltown, IA; 50251046901-001; P; PS; F; 06/23/86

Security Savings Bank; Marshalltown, IA; 50251046901-002; P; M; F; 06/23/86

Sentry Equity Services Inc; Stevens Point, WI; 50270940001-001; S; M; F; 04/25/86

Sentry Life Insurance Co; Stevens Point, WI; 50251330003-001; S; M; F; 04/25/86

Shenandoah Life Insurance Co; Roanoke, VA; 50251664001-001; P; M; F; 06/06/86

Shenandoah Life Insurance Co; Roanoke, VA; 50251664001-002; P; PS; F; 06/06/86

Shenandoah Life Insurance Co; Roanoke, VA; 50351664001-003; NS; M; F; 06/06/86

Shenandoah Life Insurance Co; Roanoke, VA; 50351664001-004; NS; PS; F; 06/06/86

Shenandoah Life Insurance Co; Roanoke, VA; 50251664002-001; P; D; F; 06/06/86

Shenandoah Life Insurance Co; Roanoke, VA; 50251664002-002; P; D; F; 06/06/86

Shenandoah Life Insurance Co; Roanoke, VA; 50351664002-003; NS; D; F; 06/06/86

Shenandoah Life Insurance Co; Roanoke, VA; 50351664002-004; NS; D; F; 06/06/86

Sigma Investment Shares Inc; Wilmington, DE; 50251740001-001; P; PS; F; 04/14/86

Sigma Investment Shares Inc; Wilmington, DE; 50251740001-002; P; M; F; 04/14/86

Smith Moore & Co; St Louis, MO; 50251800001-001; P; M; F; 04/30/86

Smith Moore & Co; St Louis, MO; 50251800001-002; P; PS; F; 04/30/86

Southern Life Insurance Co; Greensboro, NC; 50252304001-001; P; M; F; 06/06/86

Southern Life Insurance Co; Greensboro, NC; 50252304001-002; P; PS; F; 06/06/86

Southern Life Insurance Co; Greensboro, NC; 50352304001-003; NS; M; F; 06/06/86

Southern Life Insurance Co; Greensboro, NC; 50352304001-004; NS; PS; F; 06/06/86

Southern Life Insurance Co; Greensboro, NC; 50252304002-001; P; D; F; 06/06/86

Southern Life Insurance Co; Greensboro, NC; 50252304002-002; P; D; F; 06/06/86

Southern Life Insurance Co; Greensboro, NC; 50352304002-003; NS; D; F; 06/06/86

Southern Life Insurance Co; Greensboro, NC; 50352304002-004; NS; D; F; 06/06/86

Sovran Bank NA; Norfolk, VA; 50358510001-001; NS; PS; F; 06/26/86

Sovran Bank NA; Norfolk, VA; 50358510001-002; NS; M; F; 06/26/86

Sovran Bank NA; Norfolk, VA; 50258510001-003; P; PS; F; 06/26/86

Sovran Bank NA; Norfolk, VA; 50258510001-004; P; M; F; 06/26/86

Sovran Bank NA; Norfolk, VA; 50358510001-005; NS; T; F; 06/26/86

Standard Insurance Co; Portland, OR; 50252884001-001; P; M; F; 06/06/86

Standard Insurance Co; Portland, OR; 50252884001-002; P; PS; F; 06/06/86

Standard Insurance Co; Portland, OR; 50352884001-003; NS; M; F; 06/06/86

Standard Insurance Co; Portland, OR; 50352884001-004; NS; PS; F; 06/06/86

Standard Insurance Co; Portland, OR; 50252884002-001; P; D; F; 06/06/86

Standard Insurance Co; Portland, OR; 50252884002-002; P; D; F; 06/06/86

Standard Insurance Co; Portland, OR; 50352884002-003; NS; D; F; 06/06/86

Standard Insurance Co; Portland, OR; 50352884002-004; NS; D; F; 06/06/86

State Firemen & Fire Marshals Association of Texas; Austin, TX; 50268250001-001; P; PS; U; 05/13/86

State Firemen & Fire Marshals Association of Texas; Austin, TX; 50268250001-002; P; M; U; 05/13/86

State Firemen & Fire Marshals Association of Texas; Austin, TX; 50268250001-003; P; M; U; 05/13/86

State Firemen & Fire Marshals Association of Texas; Austin, TX; 50268250002-001; P; D; U; 05/13/86

State Life Insurance Co; Indianapolis, IN; 50253674001-001; P; M; F; 06/06/86

State Life Insurance Co; Indianapolis, IN; 50253674001-002; P; PS; F; 06/06/86

State Life Insurance Co; Indianapolis, IN; 50353674001-003; NS; M; F; 06/06/86

State Life Insurance Co; Indianapolis, IN; 50353674001-004; NS; PS; F; 06/06/86

State Life Insurance Co; Indianapolis, IN; 50253674002-001; P; D; F; 06/06/86

State Life Insurance Co; Indianapolis, IN; 50253674002-002; P; D; F; 06/06/86

State Life Insurance Co; Indianapolis, IN; 50353674002-003; NS; D; F; 06/06/86

State Life Insurance Co; Indianapolis, IN; 50353674002-004; NS; D; F; 06/06/86

State Mutual Insurance Co of Georgia; Rome, GA; 50253694001-001; P; PS; F; 06/06/86

State Mutual Insurance Co of Georgia; Rome, GA; 50253694001-002; P; M; F; 06/06/86

State Mutual Insurance Co of Georgia; Rome, GA; 50353694001-003; NS; M; F; 06/06/86

State Mutual Insurance Co of Georgia; Rome, GA; 50353694001-004; NS; PS; F; 06/06/86

State Mutual Insurance Co of Georgia; Rome, GA; 50253694002-001; P; D; F; 06/06/86

State Mutual Insurance Co of Georgia; Rome, GA; 50253694002-002; P; D; F; 06/06/86

State Mutual Insurance Co of Georgia; Rome, GA; 50353694002-003; NS; D; F; 06/06/86

State Mutual Insurance Co of Georgia; Rome, GA; 50353694002-004; NS; D; F; 06/06/86

Stifel Nicolaus & Co; St Louis, MO; 50254030001-001; P; M; F; 04/30/86

Stifel Nicolaus & Co; St Louis, MO; 50254030001-002; P; PS; F; 04/30/86

Stratton Management Co; Blue Bell, PA; 50254120001-001; P; PS; F; 05/02/86

Stratton Management Co; Blue Bell, PA; 50254120001-002; P; M; F; 05/02/86

Summit Bank; Fort Wayne, IN; 50234500001-001; P; PS; F; 05/19/86

Summit Bank; Fort Wayne, IN; 50234500001-002; P; M; F; 05/19/8

Summit Bank; Fort Wayne, IN; 50334500001-003; NS; PS; F; 05/19/86

Summit Bank; Fort Wayne, IN; 50334500001-004; NS; M; F; 05/19/86

Summit Bank; Fort Wayne, IN; 50334500001-005; NS; PS; F; 05/19/86

Summit Bank; Fort Wayne, IN; 50334500001-006; NS; M; F; 05/19/86

Surety Savings Association; El Paso, TX; 50354420001-001; NS; PS; F; 05/02/86

Surety Savings Association; El Paso, TX; 50354420001-002; NS; M; F; 05/02/86

Sutro & Co Inc; San Francisco, CA; 50254490001-001; P; M; F; 06/13/86

Sutro & Co Inc; San Francisco, CA; 50254490001-002; P; PS; F; 06/13/86

Sponsors of Master and Prototype Plans

T Rowe Price Associates Inc; Baltimore, MD; 50254560001-001; P; PS; U; 06/05/86
T Rowe Price Associates Inc; Baltimore, MD; 50254560001-002; P; M; U; 06/05/86
Texas South Life Insurance Co; La Grange, TX; 50270500001-001; S; M; U; 04/14/86
Third National Bank of Ashland; Ashland, KY; 50255220001-001; P; PS; F; 04/14/86
Third National Bank of Ashland; Ashland, KY; 50255220001-002; P; PS; F; 04/14/86
Third National Bank of Ashland; Ashland, KY; 50255220002-001; S; M; F; 04/14/86
Third National Bank of Ashland; Ashland, KY; 50255220002-002; P; M; F; 04/14/86
Travelers Insurance Co; Hartford, CT; 50255640001-001; P; D; F; 06/23/86
Travelers Insurance Co; Hartford, CT; 50355640001-002; NS; D; F; 06/23/86
Travelers Insurance Co; Hartford, CT; 50255640001-003; P; D; F; 06/23/86
Travelers Insurance Co; Hartford, CT; 50355640001-004; NS; D; F; 06/23/86
Travelers Insurance Co; Hartford, CT; 50255640002-001; P; M; F; 06/23/86
Travelers Insurance Co; Hartford, CT; 50355640002-002; NS; M; F; 06/23/86
Travelers Insurance Co; Hartford, CT; 50255640002-003; P; PS; F; 06/23/86
Travelers Insurance Co; Hartford, CT; 50355640002-004; NS; PS; F; 06/23/86
Travelers Insurance Co; Hartford, CT; 50255640002-005; P; T; F; 06/23/86
Travelers Insurance Co; Hartford, CT; 50355640002-006; NS; T; F; 06/23/86
Trust Co of America; Boulder, CO; 50355790001-001; NS; PS; F; 04/07/86
Trust Co of America; Boulder, CO; 50355790001-002; NS; M; F; 04/07/86
UFB Insurance Co; Indianapolis, IN; 50336610001-001; NS; PS; U; 04/09/86
UFB Insurance Co; Indianapolis, IN; 50236610001-002, S; M; F; 04/14/86
UFB Insurance Co; Indianapolis, IN; 50336610001-003; NS; M; F; 04/14/86
Union Bank; Los Angeles, CA; 50256010005-001; P; PS; F; 04/14/86
Union Bank; Los Angeles, CA; 50256010005-002; P; M; F; 04/14/86
Union Bank; Los Angeles, CA; 50256010006-001; S; PS; F; 04/14/86
Union Bank; Los Angeles, CA; 50256010006-002; S; M; F; 04/14/86
Union Bank & Trust Co; Kokomo, IN; 50256051801-001; P; M; F; 05/23/86
Union Bank & Trust Co; Kokomo, IN; 50356051801-002; NS; M; F; 05/23/86
Union Bank & Trust Co; Kokomo, IN; 50256051801-003; P; PS; F; 05/23/86
Union Bank & Trust Co; Kokomo, IN; 50356051801-004; NS; PS; F; 05/23/86
Union Central Life Insurance Co; Cincinnati, OH; 50356200001-001; NS; PS; F; 04/14/86
Union Central Life Insurance Co; Cincinnati, OH; 50356200001-002; NS; M; F; 04/14/86
Union Central Life Insurance Co; Cincinnati, OH; 50256200001-003; S; M; F; 04/14/86
Union Central Life Insurance Co; Cincinnati, OH; 50256200001-004; S; PS; F; 04/14/86
Union National Bank of Macomb; Macomb, IL; 50269222701-001; S; PS; F; 06/05/86
Union National Bank of Pittsburgh; Pittsburgh, PA; 50256410001-001; P; PS; F; 05/02/86
Union National Bank of Pittsburgh; Pittsburgh, PA; 50256410001-002; P; M; F; 05/02/86
Union Trust Co; New Haven, CT; 50356590701-001; NS; M; F; 04/04/86
Union Trust Co; New Haven, CT; 50256590701-002; P; M; F; 04/04/86
Union Trust Co; New Haven, CT; 50356590701-003; NS; PS; F; 04/04/86
Union Trust Co; New Haven, CT; 50256590701-004; P; PS; F; 04/04/86
United Bank & Trust Co; Hartford, CT; 50256720002-001; P; M; F; 05/02/86
United Bank & Trust Co; Hartford, CT; 50256720002-002; P; PS; F; 05/02/86
United Bank of Denver NA; Denver, CO; 50256780002-001; S; D; F; 06/30/86
United Bank of Denver NA; Denver, CO; 50256780002-002; S; D; F; 06/30/86
United Bank of Illinois NA; Rockford, IL; 50356810001-001, NS; PS; F; 04/10/86
United Bank of Illinois NA; Rockford, IL; 50356810001-002; NS; M; F; 04/10/86
United Bank of Illinois NA; Rockford, IL; 50256810003-001; P; PS; F; 04/18/86
United Bank of Illinois NA; Rockford, IL; 50256810003-002; P; M; F; 04/21/86
United Illinois Bank of Cobden; Cobden, IL; 50224530001-001; P; M; F; 04/30/86
United Illinois Bank of Cobden; Cobden, IL; 50224530001-002; P; PS; F; 04/30/86
United Illinois Bank of Dahlgren; Dahlgren, IL; 50219420001-001; P; M; F; 04/30/86
United Illinois Bank of Dahlgren; Dahlgren, IL; 50219420001-002; P; PS; F; 04/30/86
United Illinois Bank of New Athens; New Athens, IL; 50253410001-001; P; M; F; 04/30/86
United Illinois Bank of New Athens; New Athens, IL; 50253410001-002; P; PS; F; 04/30/86
United Illinois Bank of Troy; Troy, IL; 50255740001-001; P; PS; F; 04/30/86
United Illinois Bank of Troy; Troy, IL; 50255740001-002; P; M; F; 04/30/86
United Olympic Life Insurance Co; Bellevue, WA; 50355990001-001; NS; M; F; 05/19/86
United Olympic Life Insurance Co; Bellevue, WA; 50355990002-001; NS; PS; F; 05/19/86
United States Trust Co of New York; New York, NY; 50357630002-001; NS; D; F; 05/21/86
United States Trust Co of New York; New York, NY; 50357630002-002; NS; D; F; 05/22/86
US Trust Middlesex; Cambridge, MA; 50271990001-001; S; M; U; 04/07/86
US Trust Middlesex; Cambridge, MA; 50271990001-002; S; PS; U; 04/07/86
US Trust Norfolk; Milton, MA; 50272000001-001; S; M; U; 04/07/86
US Trust Norfolk; Milton, MA; 50272000001-002; S; PS; U; 04/07/86
Valencia Bank; Irvine, CA; 50358030001-001; NS; PS; F; 05/22/86
Valencia Bank; Irvine, CA; 50358030001-002; NS; PS; F, 05/22/86
Valencia Bank; Irvine, CA; 50358030001-003; NS; PS; F; 05/22/86
Valencia Bank; Irvine, CA; 50358030001-004; NS; M; F; 05/22/86
Valencia Bank; Irvine, CA; 50358030001-005; NS; M; F; 05/22/86
Valencia Bank; Irvine, CA; 50358030001-006; NS; M; F; 05/22/86
Valley American Bank & Trust Co; South Bend, IN; 50202020001-001; S; PS; F; 04/25/86
Valley American Bank & Trust Co; South Bend, IN; 50202020001-002; S; M; F; 04/25/86
Valley National Bank of Arizona; Phoenix, AZ; 50358210001-001; NS; PS; F; 05/29/86
Valley National Bank of Arizona; Phoenix, AZ; 50358210001-002; NS; PS; F; 05/29/86
Valley National Bank of Arizona; Phoenix, AZ; 50358210001-003; NS; M; F; 05/29/86
Valley National Bank of Arizona; Phoenix, AZ; 50358210001-004; NS; M; F; 05/29/86
Valley National Bank of Arizona; Phoenix, AZ; 50258210001-005; S; M; F; 05/29/86
Valley National Bank of Arizona; Phoenix, AZ; 50258210001-006; S; PS; F; 05/29/86
Valley National Bank of Arizona; Phoenix, AZ; 50358210002-001; NS; PS; F; 05/29/86
Valley National Bank of Arizona; Phoenix, AZ; 50358210002-002; NS; M; F; 05/29/86
Valley National Bank of Arizona; Phoenix, AZ; 50358218403-001; NS; M; F; 05/30/86
Valley National Bank of Arizona; Phoenix, AZ; 50258218403-002, P; M; F; 05/30/86
Valley National Bank of Arizona; Phoenix, AZ; 50358218403-003; NS; PS; F; 05/30/86
Commercial National Bank of Peoria; Peoria, IL; 50215090002-002; P; M. 04/18/86
Valley National Bank of Arizona; Phoenix, AZ; 50258218403-004; P; PS; F; 05/30/86
Valley National Bank of Arizona; Phoenix, AZ; 50358218404-001; NS; D; F; 05/30/86
Valley National Bank of Arizona; Phoenix, AZ; 50258218404-002; P; D; F; 05/30/86
Value Line Securities Inc; New York, NY; 50270375001-003; P; PS; F; 04/11/86
Value Line Securities Inc; New York, NY; 50270375001-004; P; M; F; 04/11/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50358540001-001; NS; PS; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50258540001-002; S; PS; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50358540001-003; NS; M; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50258540001-004; S; M; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50358540001-005; NS; PS; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50258540001-006; S; PS; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50358540001-007; NS; M; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50258540001-008; S; M; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50358540002-001; NS; D; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50258540002-002; S; D; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50358540002-003; NS; D; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50258540002-004; S; D; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50358540002-005; NS; D; U; 04/09/86
Volunteer State Life Insurance Co; Chattanooga, TN; 50258540002-006; S; D; U; 04/09/86
Wells Fargo Bank NA; San Francisco, CA; 50259140001-001; P; PS; F; 04/18/86
Wells Fargo Bank NA; San Francisco, CA; 50259140001-002; P; M; F; 04/18/86
Wells Fargo Bank NA; San Francisco, CA; 50359140002-001; NS; M; F; 05/26/86
Wells Fargo Bank NA; San Francisco, CA; 50359140002-002; NS; PS; F; 05/26/86
Western Farm Bureau Life Insurance Co; Denver, CO; 50259370001-001; P; PS; F; 05/09/86
Western Farm Bureau Life Insurance Co; Denver, CO; 50259370001-002; P; M; F; 05/09/86
Western Farm Bureau Life Insurance Co; Denver, CO; 50359370001-003; NS; PS; F; 05/09/86
Western Farm Bureau Life Insurance Co; Denver, CO; 50359370001-004; NS; M; F; 05/09/86
Western-Southern Life Insurance Co; Cincinnati, OH; 50259274001-001; P; M; F; 06/06/86
Western-Southern Life Insurance Co; Cincinnati, OH; 50259274001-002; P; PS; F; 06/06/86
Western-Southern Life Insurance Co; Cincinnati, OH; 50359274001-003; NS; M; F; 06/06/86
Western-Southern Life Insurance Co; Cincinnati, OH; 50359274001-004; NS; PS; F; 06/06/86
Western-Southern Life Insurance Co; Cincinnati, OH; 50259274002-001; P; D; F; 06/06/86
Western-Southern Life Insurance Co; Cincinnati, OH; 50259274002-002; P; D; F; 06/06/86
Western-Southern Life Insurance Co; Cincinnati, OH; 50359274002-003; NS; D; F; 06/06/86
Western-Southern Life Insurance Co; Cincinnati, OH; 50359274002-004; NS; D; F; 06/06/86
Wilton Savings Bank; Wilton, IA; 50359880001-001; NS; M; F; 06/13/86
Wilton Savings Bank; Wilton, IA; 50359880001-002; NS; M; F; 06/13/86
Wilton Savings Bank; Wilton, IA; 50359880001-003; NS; PS; F; 06/13/86
Wilton Savings Bank; Wilton, IA; 50359880001-004; NS; PS; F; 06/13/86
Windsor Bank & Trust Co; Windsor, CT; 50271650001-001; P; M; F; 05/02/86
Windsor Bank & Trust Co; Windsor, CT; 50271650001-002; P; PS; F; 05/02/86
Commercial National Bank of Peoria; Peoria, IL; 50215090002-001; P; PS. 04/18/86

List B

Plans Omitted from Announcement 85–99

First National Bank of Long Island; Woodbury, NY; 50225470001–003; P; PS.

First National Bank of Long Island; Woodbury, NY; 50225470001–004; P; M.

Ohio Life Insurance Co; Hamilton, OH; 50344730001–002; NS; M.

Ohio Life Insurance Co; Hamilton, OH; 50344730003–001; NS; PS.

Ohio Life Insurance Co; Hamilton, OH; 50344730003–002; NS; PS.

Ohio Life Insurance Co; Hamilton, OH; 50344730005–001; NS; T.

Ohio Life Insurance Co; Hamilton, OH; 50344730005–002; NS; T.

Publication 560 Self-Employed Retirement Plans, Revised

Announcement 86–87

An updated edition (revised June 1986) of Publication 560, Self-Employed Retirement Plans, is now available from the Internal Revenue Service. The publication discusses retirement plans for self-employed persons, including certain partners in partnerships. These plans are sometimes called Keogh or H.R. 10 plans.

The publication has been revised to cover tax rule changes, including those made by the Tax Reform Act of 1984 and the Retirement Equity Act of 1984.

The publication may be ordered by calling the "Federal Tax Forms Only" number listed in the telephone book under "United States Government, Internal Revenue Service."

New Form 1041S, U.S. Fiduciary Income Tax Return for Nontaxable Simple Trusts

Announcement 86–88

New Form 1041S, U.S. Fiduciary Income Tax Return for Nontaxable Simple Trusts, has been developed for use by trusts that have no capital gains or losses and have an income distribution deduction that is equal to the amount of income the trust is required to distribute currently. A copy of the new form follows.

Use of the Form 1041S, rather than the longer Form 1041, is optional. However, filing the Form 1041S will substantially reduce the reporting burden for simple trusts that are eligible to file the form.

Form 1041S and related instructions will be available in many Internal Revenue Service offices beginning in January 1987. It may be filed for tax years beginning in 1986.

Form **1041S**

Department of the Treasury
Internal Revenue Service

U.S. Fiduciary Income Tax Return for Nontaxable Simple Trusts

For the calendar year 1986 or fiscal year beginning , 1986, and ending , 19

OMB No. 1545-0960

1986

Name of simple trust	Employer identification number
Name and title of fiduciary	Date trust created
Address of fiduciary (number and street)	Check applicable box(es):
City, state, and ZIP code	☐ Amended return ☐ Final return

Income

1	Dividends (enter full amount before exclusion)	1	
2	Interest income	2	
3	Income or (losses) from partnerships, estates, or other trusts	3	
4	Net rent and royalty income or (loss) (attach Schedule E (Form 1040))	4	
5	Net business and farm income or (loss) (attach Schedules C and F (Form 1040))	5	
6	Ordinary gain or (loss) (attach Form 4797)	6	
7	Other income (state nature of income)	7	
8	Total income (add lines 1 through 7)	8	

Deductions

9	Interest	9			
10	Taxes	10			
11	Fiduciary fees	11			
12	Accountant, attorney, and return preparer fees	12			
13	Other deductions (itemize on a separate sheet)	13			
14	Total (add lines 9 through 13)			▶ 14	
15	Adjusted total income or (loss) (Subtract line 14 from line 8)			15	
16	Income distribution deduction (attach Schedule K-1 (Form 1041))			16	
17	Balance (subtract line 16 from line 15) (see instructions)			▶ 17	

Other Information

		Yes	No
1	If the fiduciary's name or address has changed enter the old information		
2	Did the trust receive tax-exempt income? (If "Yes," attach a computation of the allocation of expenses)		
3	Did the trust receive all or any part of the earnings (salary, wages, and other compensation) of any individual by reason of a contract assignment or similar arrangement?		
4	Was the trust the grantor of, or transferor to, a foreign trust which existed during the current tax year, whether or not the trust has any beneficial interest in it? (If "Yes," you may have to file Form 3520, 3520-A, or 926)		
5	At any time during the tax year, did the trust have an interest in or a signature or other authority over a financial account in a foreign country (such as a bank account, securities account, or other financial account)? (See the instructions for question 5.) If "Yes," write the name of the foreign country		
6	Check this box if this trust is required to file Form 8264, Application for Registration of a Tax Shelter	▶ ☐	

Please Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than fiduciary) is based on all information of which preparer has any knowledge.

▶ Signature of fiduciary or officer representing fiduciary ▶ Date

Paid Preparer's Use Only

Preparer's signature ▶	Date	Check if self-employed ▶ ☐	Preparer's social security no.
Firm's name (or yours, if self-employed) and address		E.I. No. ▶	
		ZIP code ▶	

For Paperwork Reduction Act Notice, see page 1 of the instructions.

Form 1041S (1986)

Foundations Status of Certain Organizations

Announcement 86–89

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

A.I.D.D., Inc., Klamath Falls, OR
Academy of Dental Materials, Chicago, IL
Adolescent Care Centers, Inc., Los Angeles, CA
Aggrey Development Association, Rockford, IL
Agudas Israel of St. Louis, University City, MO
Alliance of Barrington Communities for Drug Education, Inc., Barrington, IL
Ankeny-Polk County, Ankeny, IA
Assistance, Inc., Rapid City, SD
Association for the Advancement of Medical Instrumentation Foundation, Arlington, VA
Association of Black Laboratories Employees Inc., The, Summit, NJ
Austrian Cultural Roundtable, Chicago, IL
Bachar, St. Paul, MN
Be . . . Love Unlimited, Olympia, WA
Behavior Disorder Interventions Corp., Oak Brook, IL
Ben Fuller Museum Association, Hinsdale, IL
Benton Park Arts Council, St. Louis, MO
Best of Friends Auxiliary of the Childrens Memorial Hospital, Inc., Chicago, IL
Binai Brith Jewish Community Center Corp., Lancaster, PA
Birthright of West Plains, West Plains, MO
Brainchild Incorporated, Chicago, IL
Brimson Area Volunteer Fire Department, Brimson, MN
Brooklyn Community Betterment, Brooklyn, IA
Brunswick Gallery, Inc., The, Missoula, MT
Business Task Force for School District 205, Rockford, IL
Butler County Council on Housing for The Elderly & Handicapped, Inc., Poplar Bluff, MO
Center for Victims of Domestic Abuse, Inc., Menasha, WI
Chicago National Alliance of Postal and Federal Employees, Elderly Towers, Inc., Chicago, IL
Children's Health Systems, Inc., San Diego, CA
Children's Home Health Network of Illinois, Chicago, IL
Christ Love Missions, Chicago, IL
Christian Service Council of Grant County, Milbank, SD
Clearinghouse for Nurse Certification Information, Chicago, IL
Columbia Historic Preservation Society, Columbia, PA
Committee on Decent Unbiased Campaign Tactics, St. Louis, MO
Communities United for Tomorrow, Chicago, IL
Community Homes of Prince Georges and Montgomery Counties, Inc., Silver Spring, MD
Community Housing & Preservation Corp., Milwaukee, WI
Community Housing Resource Board—Caldwell, Nampa, Emmett Valley, Payette County and Mahleur County, Caldwell, ID
Congressional Award Council, Eighth District Illinois, Inc., Chicago, IL
Council for Responsible Church Administration, Santa Ana, CA
Dakota County Advocates for The Mentally Ill, Inc., Minneapolis, MN
Des Moines Japanese Tea House and Garden Association, Inc., Des Moines, IA
Developmental Disabilities Service Center, Inc., Kenosha, WI
Drug and Alcohol Abuse Referral Exchange Inc., Lees Summit, MO
East Area Homebound Meals Association, St. Paul, MN
East Coast Bobsled Association Inc., Englewood, NJ
East St. Louis Charities Day Organization, East St. Louis, IL
Eastern Communication Association, Philadelphia, PA
Ecumenical Refugee Council Inc., Milwaukee, WI
Educational Network and Associates, Chicago, IL
Elderly Assistance Team, Wheaton, IL
Emergency Communications Help Organization Inc., Springfield, MO
Endyre, Kearney, NE
Epic Teen Center, Inc., Minneapolis, MN
European Immigrant Benevolent Fund, Philadelphia, PA
Evening Baptist Ministers Conference, Inc., The, Philadelphia, PA
Finch Kingdom Junior Avicultural Society, Irvine, CA
Fox Valley Community Housing Board, Appleton, WI
Frank Palumbo Memorial Association, The, Philadelphia, PA
Friends of the Schaumburg Cultural Center, Schaumburg, IL
Girls Club of Independence Missouri, Inc., Independence, MO
Glenside Landmarks Society, North Hills, PA
Global Competitiveness Council, The, Boston, MA
Grand Bahama Charitable Foundation, Inc., Washington, DC
Greater Works Ministries, Minneapolis, MN
H.S.C. No. 2 Housing Development Fund Company, Inc., Huntington, NY
Hays Foundation For Youth, Inc., The, Ridgefield, CT
Health Care International, Inc., White Bear Lake, MN
Help Emergency Food Parties, Inc., Joliet, IL
Henry M. Dodge Memorial Fund, Inc., Keshena, WI
Historic Chandler House, Inc., Waykesha, WI
Holmen Community Theatre, Inc., Holmen, WI
Holy Angels Neighborhood Association, Milwaukee, WI
Hope Unlimited, Kirkwood, MO
Houston 85, Springfield, MO
Human Services Consulting Inc., Sacramento, CA
In the Child's Best Interest A Better Way, St. Louis, MO
Indian Enterprises, Inc., Oskaloosa, IA
Internal Festival For Peace, St. John, ND
International Consortium for The Study of Neurological and Psychological Reactions to Cardiac Surgery, Inc., Milwaukee, WI
Iowa Great Lake Maritime Museum, Arnolds Park, IA
Jane Dent Feamon Apartments, Inc., Chicago, IL

Jesus First Ministries, Inc., Kansas City, MO
Joy Evangelistic Association, Inc., Macks Creek, MO
Keen-Teen, Chicago, IL
Korean Blind Foundation in The USA, Philadelphia, PA
LaSalle Drive Association, Chicago, IL
Lake Zurich Quarterback Club, Lake Zurich, IL
Lakes Area Coalition for Battered Women, Inc., Detroit Lakes, MN
Leisure Acres—Phase II Housing Corp., East Peoria, IL
Light-A-Lamp Educational Foundation, Chicago, IL
Little Earth Residents Association Inc., Minneapolis, MN
Little Falls Celebrity Golf Tournament, Inc., Little Falls, MN
Lodge Grass-Wyola Community Ambulance Service, Lodge Grass, MT
Logan-Rogersville Volunteer Fire Department, Inc., Rogersville, MO
Longevity Research Foundation of La Jolla, Huntington Beach, CA
Medical Research Charitable Foundation, Mt. Prospect, IL
Messenger of Memorial Hospital of Lafayette County, The, Darlington, WI
Metro Towers, Inc., Kansas City, MO
Mid America Foundation for Agriculture and the Gifted, Chatham, IL
Mid-Penn Football Clinic, Inc., Harrisburg, PA
Midwest Institute for Design Research, Inc., Milwaukee, WI
Milwaukee Community Radio, Inc., Milwaukee, WI
Minneapolis Writers' Workshop, Inc., Minneapolis, MN
Minnesota Pheasants Inc., Rice County Chapter, Faribault, MN
Minnesota Reviews, Inc., St. Paul, MN
Minnesota Youth Intervention Programs Association, Forest Lake, MN
Mohawk Valley Apartments, Inc., Clinton, NY
Motion Pictur-TV Rank and File Legal Services Foundation, Beverly Hills, CA
Mt. Zion Land Development Corporation II, Milwaukee, WI
Multiplication of The Loaves Project, Inc., Omaha, NE
Mustangs, Inc., Philadelphia, PA
National Retirement Association, Northfield, IL
Natural Family Planning Awareness Center of Lake Park Inc., Lake Park, MN
Nebraska County Music Foundation, Holstein, NE
Nebraska Head Injury Association, The, Omaha, NE
Neighborhood Enterprise Corporation of Hunting Park West, Philadelphia, PA
New Covenant Seniors, Chicago, IL
New Jersey Black Issues Convention, Inc., Newark, NJ
Ni Mi Win, Inc., Duluth, MN
Nina Place Redevelopment Corp., St. Louis, MO
North American Ginseng Association Inc., Chicago, IL
North Hennepin Writers Guild, Dayton, MN
Northeastern Wisconsin Christian Television, Inc., Suring, WI
Northern Minnesota Area Assembly, Moorhead, MN
Northwest Textile Center, Salem, OR
Oakland Meals on Wheels, Inc., Oakland, MD
Olmsted Citizens for A Better Community Inc., Rochester, MN
Omega Outreach Ministries, San Gabriel, CA
One Nation under God, Inc., Fargo, ND
Oregon Legal Foundation, Portland, OR
Peninsula Task Force on Child Sexual Abuse (aka ReUnion), Port Angeles, WA
Pilot Know Arts Council, Inc., Forest City, IA
Putnam Community Cultural and Recreational Center, Inc., Mahopac, NY
R D C Educational and Defense Fund, Inc., Anchorage, AK
Raptor Fund, Inc., The, Oak Park, IL
Reach, Inc., Chicago, IL
Redemptive Farms Inc., Phoenixville, PA
Regeneration of Children, Inc., Helena, MT
Rock and Roll Conservatory Inc., Wilmington, DE
St. Benedict Abby Foundation, Scotch Plains, NJ
Salem County Abbey House, Penns Grove, NJ
Sauk County Task Force Domestic Abuse Inc., Baraboo, WI
Seattle-Tashkent Sister City Committee, Bellevue, WA
Senior Citizens of Logan County, Inc., Lincoln, IL
Seoul National University Alumni Association, Inc., Evergreen Park, IL
Shepherds Center of Greater Des Moines, Des Moines, IA
Sheridan Park Boxing Club, Des Moines, IA
Sioux Residential Services, Inc., Sioux Falls, SD
Society for The Study of Hispanic and Lusophone Contemporary Revolutionary Literatures, Inc., Minneapolis, MN
South Nassau Counseling Service Inc., Baldwin, NY
Southside Activities Development, Peoria, IL
Spectator #442, Los Angeles, CA
Staples Area Food Shelf, Inc., Staples, MN
Stark City Volunteer Fire Dept., Stark City, MO
Suamico Elderly Housing Corp., Green Bay, WI
Sunday Line Communications, Bellingham, WA
The Way, The Truth and The Life Ministries, Kent, WA
Threshold, Inc., St. Louis, MO
Tri State Black Media Coalition, Inc., Philadelphia, PA
Trinity Acres Housing Corp., Chicago, IL
Trinity Community Housing Corp., Chicago, IL
Triumphant Living through Christ Jesus, Inc., Philadelphia, PA
Twin Cities Committee for Ethiopian Jewry, St. Paul, MN
Twin City Seventh Day Adventist Scholarship Association, St. Paul, MN
Union Baptist Plaza, Inc., Springfield, IL
Waconia Heritage Association, Waconia, MN
Webster County Young Farmers Educational Association, Inc., Fort Dodge, IA
Westside Catholic Scholarship Fund, Inc., Oak Park, IL
Wisconsin Theatre for Children, Inc., Thiensville, WI
Woodstock Academy, Woodstock, IL
Yes and Productions, Chicago, IL
Young-Afro-American Society of Minneapolis, Inc., Minneapolis, MN

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

The following organizations, which have been treated as private operating foun-

dations described in section 4942(j)(3) of the Code, have now been classified as organizations that are not private operating foundations. Grantors and contributors may no longer rely upon rulings or determinations that these organizations are private operating foundations. The organizations are:

American Heritage Ministries, Inc., The, Long Beach, CA
Camellia Information Fund, Inc., Los Angeles, CA
Historical Research Institute, San Diego, CA
Humanity International Foundation, Los Angeles, CA
Loma Linda Institute of Medical Research, Relands, CA
Vox Foundation, The, Riverside, CA

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Trevor Adel	Silver Spring, MD	Certified Public Accountant	Indefinite from June 2, 1986
John H. Peimann	Ottawa, KS	Certified Public Accountant	Twenty-One Months from June 1, 1986
John D. Raikos	Indianapolis, IN	Attorney	Indefinite from May 20, 1986
Vernon Rubel	Hickory, NC	Enrolled Agent	Indefinite from May 28, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

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Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor.
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federral Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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CUMULATIVE BULLETINS

The contents of the weekly Bulletin are consolidated semiannually into a permanent, indexed, Cumulative Bulletin. These are sold on a single copy basis and *are not* included as part of the subscription to the Internal Revenue Bulletin. Subscribers to the weekly Bulletin are notified when copies of the Cumulative Bulletin are available. Certain issues of Cumulative Bulletins are out of print and are not available. Persons desiring available Cumulative Bulletins, which are listed on the reverse, may purchase them from the Superintendent of Documents.

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Internal Revenue

bulletin

Bulletin No. 1986-31
August 4, 1986

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-94, page 20.
Federal short-term, mid-term, and long-term rates; blended annual rate. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for August 1986. For purposes of section 7872(e)(2) of the Code, the blended annual rate for 1986 is 7.77 percent.

T.D. 8094, page 4.
LR-18-85, page 22.
Temporary and proposed regulations related to special rules relating to nuclear decommissioning costs.

Announcement 86-91, page 25.
Mortgage subsidy bonds; average area purchase price. Issuers of mortgage subsidy bonds may continue to rely on the "average area purchase price" safe harbor limitations contained in Rev. Proc. 85-42, 1985-2 C.B. 496, until new safe harbor limitations are published.

EXEMPT ORGANIZATIONS

Announcement 86-90, page 22.
A list is given of organizations now classified as private foundations.

EXCISE TAXES

Rev. Rul. 86-93, page 20.
Sale price of truck; tire exclusion; use of cost comparison formula. For purposes of computing the taxable sale price of a highway vehicle under section 4052(b) of the Code, a cost comparison formula may be used to determine the amount that may be excluded as the fair market value at retail of the tires.

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Finding Lists begin on page 28.
Announcement of Disbarments and Suspensions on page 26.

Department of the Treasury
Internal Revenue Service

T22.23:1986-31

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing cur Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 88.—Certain Amounts with Respect to Nuclear Decommissioning Costs

26 CFR 1.88-1T: Nuclear decommissioning costs (temporary).
(Also Section 468A)

T.D. 8094

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER A, SUBCHAPTER H, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Special Rules Relating to Nuclear Decommissioning Costs

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to the Federal income tax treatment of nuclear decommissioning costs. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations for the notice of proposed rulemaking [page 22, this Bulletin]. Changes to the applicable law were made by the Tax Reform Act of 1984. The regulations affect all taxpayers that include nuclear decommissioning costs in cost of service for ratemaking purposes.

DATES: The regulations are effective on July 18, 1984, and apply with respect to taxable years ending on or after such date.

FOR FURTHER INFORMATION CONTACT: C. Scott McLeod of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T, 202-566-3288 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document amends the Income Tax Regulations (26 CFR Part 1) and the Table of OMB Control Numbers (26 CFR Part 602) to provide rules under sections 88 and 468A of the Internal Revenue Code of 1954. Section 88 was added to the Code by section 91(f) of the Tax Reform Act of 1984 (Pub. L. 98–369, 98 Stat. 607) and section 468A was added to the Code by section 91(c) of the Tax Reform Act of 1984 (Pub. L. 98–369, 98 Stat. 604).

EXPLANATION OF PROVISIONS

Section 88 requires taxpayers that are engaged in the furnishing or sale of electric energy generated by a nuclear power plant to include in gross income the amount of nuclear decommissioning costs that are included in cost of service for ratemaking purposes for any taxable year. The regulations clarify that the amount of nuclear decommissioning costs directly or indirectly charged to the customers of a taxpayer, whether paid to the taxpayer, a nuclear decommissioning fund or other entity, must be included in the gross income of such taxpayer in the same manner as amounts charged for electric energy, even though the taxpayer does not control the investment or current expenditure of the amount. In addition, the regulations provide general guidance on the effective date of section 88.

Section 468A provides an elective method for taking into account nuclear decommissioning costs for Federal income tax purposes. In general, an eligible taxpayer that elects the application of section 468A is allowed a deduction for the amount of cash payments made to a nuclear decommissioning fund during any taxable year. Taxpayers using an accrual method of accounting that do not elect the application of section 468A are not allowed a deduction for nuclear decommissioning costs prior to the taxable year in which economic performance occurs with respect to such costs (see section 461(h)).

Section 468A(b) limits the amount of deductible cash payments that can be made to a nuclear decommissioning fund during any taxable year to the lesser of (1) the amount of nuclear decommissioning costs allocable to the fund that is included in the taxpayer's cost of service for ratemaking purposes for such taxable year, or (2) the ruling amount applicable to the fund for such taxable year. Cash payments made to a nuclear decommissioning fund during any taxable year that exceed the limitation are not deductible by the taxpayer and may cause a disqualification of the fund.

Section 468A(d) provides that a taxpayer must request and receive a schedule of ruling amounts from the Internal Revenue Service in order for amounts paid to a nuclear decommissioning fund to be allowed as a deduction. The schedule of ruling amounts is a schedule of annual amounts that the Internal Revenue Service determines to be necessary to fund, at a rate no more rapid than level funding, the portion of the total estimated cost of decommissioning that is attributable to the remaining estimated useful life of the nuclear power plant as of the date the nuclear decommissioning fund is established. The schedule of ruling amounts is required to be reviewed by the Internal Revenue Service at least once during the estimated useful life of the nuclear power plant or more frequently at the request of the taxpayer.

Section 468A(e)(1) provides that a nuclear decommissioning fund is to be established by the taxpayer for each nuclear power plant to which the section 468A election applies. The assets of a nuclear decommissioning fund are to be used exclusively (1) to satisfy, in whole or in part, the liability of the electing taxpayer for decommissioning costs of the nuclear power plant to which the nuclear decommissioning fund relates, (2) to pay administrative costs and other incidental expenses of the nuclear decommissioning fund, and (3) to the extent that the assets of the nuclear decommissioning fund are not required for the aforementioned purposes, to invest in public debt securities of the United States, obligations of a State or local government, or time or demand deposits. In addition, section 468A(e)(5) and (6) contains special rules to discourage acts of self-dealing between the nuclear decommissioning fund and certain disqualified persons. If a nuclear decommissioning fund fails to comply with the qualification requirements or engages in an act of self-dealing, it may be disqualified by the Internal Revenue Service and treated as having distributed its assets on the date of disqualification.

Section 468A(e)(2) provides that the gross income of a nuclear decommissioning fund is subject to tax at the maximum rate in effect under section 11(b). In determining the gross income of a nuclear decommissioning fund for purposes of this tax, the amount of any payment to the fund that is deductible by the taxpayer under section 468A is excluded from the gross income of the fund and the amount of administrative costs and other incidental expenses of the fund paid by the fund to any person other than the taxpayer is deductible by the fund if such amount would be deductible in determining the taxable income of a corporation. Finally, for purposes of subtitle F of the Code (relating to procedure and administration), a nuclear decommissioning fund is treated as a corporation and any tax imposed on the income of the nuclear decommissioning fund is treated as a tax imposed by section 11.

In general, the amount of any actual distribution from a nuclear decommissioning fund must be included in the gross income of the taxpayer for the taxable year in which the distribution occurs. Thus, the amount of any distribution from a nuclear decommissioning fund used to satisfy, in whole or in part, any liability for the decommissioning of a nuclear power plant must be included in gross income of the taxpayer. The amount of an actual distribution from a nuclear decommissioning fund to pay administrative costs or other incidental expenses of the nuclear decommissioning fund is not included in the gross income of the taxpayer, however, unless such amount is paid to the taxpayer. In addition, the amount of any deemed distribution must be included in the gross income of the taxpayer for the taxable year in which the deemed distribution occurs. A deemed distribution from a nuclear decommissioning fund generally occurs upon the disqualification of the fund, a disposition of an interest in the nuclear power plant to which the fund relates or the substantial completion of the decommissioning of the nuclear power plant to which the fund relates.

The regulations under section 468A specify those taxpayers that are eligible for, and the manner of making, the election under section 468A. In addition, the regulations provide specific guidance on the manner of requesting a schedule of ruling amounts and the factors to be taken into account in determining a schedule of ruling amounts. Finally, the regulations provide guidance on the nuclear decommissioning fund qualification requirements, the consequences if a nuclear decommissioning fund is disqualified, the treatment of the selling and purchasing taxpayer in the case of a disposition of an interest in a nuclear power plant, the effective date of section 468A and the transitional rules applicable to taxpayers that elect section 468A for taxable years beginning before January 1, 1987.

EXECUTIVE ORDER 12291, REGULATORY FLEXIBILITY ACT AND PAPERWORK REDUCTION ACT

The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required. A general notice of proposed rulemaking is not required by 5 U.S.C. 553 for temporary regulations. Accordingly, the temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

The collection of information requirements contained in this regulation have been approved by the Office of Management and Budget (OMB) under Section 3507 of the Paperwork Reduction Act.

DRAFTING INFORMATION

The principal author of these regulations is C. Scott McLeod of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * * *

Amendments to the regulations

The amendments to 26 CFR Part 1 and Part 602 are as follows:

INCOME TAX REGULATIONS
(26 CFR Part 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.468A-5T also issued under 26 U.S.C. 468A(e)(5).

Par. 2. The following new section is added immediately after §1.85–1 to read as follows:

§1.88–1T Nuclear decommissioning costs (temporary)

(a) *In general.* Section 88 provides that the amount of nuclear decommissioning costs directly or indirectly charged to the customers of a taxpayer that is engaged in the furnishing or sale of electric energy generated by a nuclear power plant must be included in the gross income of such taxpayer in the same manner as amounts charged for electric energy. For this purpose, amounts payable to any other person (such as a trust or State government) shall be treated as if payable to the taxpayer. Thus, the amount of nuclear decommissioning costs directly or indirectly charged to the customers of a taxpayer, whether paid to the taxpayer, a nuclear decommissioning fund or other entity, is required to be included in gross income under section 88 and this section, even though the taxpayer does not control the investment or current expenditure of the amount and the amount will not be paid to the taxpayer at the time decommissioning costs are incurred.

(b) *Example.* The following example illustrates the application of the principles of paragraph (a) of this section:

Example. X corporation, an accrual method taxpayer engaged in the sale of electric energy generated by a nuclear power plant owned by X, is authorized by the public utility commission of State A to collect nuclear decommissioning costs from ratepayers residing in State A. With respect to the sale of electric energy, X includes in income amounts that have been billed to customers as well as estimated unbilled amounts that relate to energy provided by X after the previous billing but before the end of the taxable year ("accrued unbilled amounts"). The decommissioning costs are included in the monthly bills provided by X to its ratepayers and the entire amount billed is remitted directly to X. Under paragraph (a) of this section, the decommissioning costs must be included in the gross income of X in the same manner as amounts charged for electric energy (*i.e.*, by including in income decommissioning costs that relate to amounts billed as well as decommissioning costs that relate to accrued unbilled amounts). The same rule would apply if the decommissioning costs charged to ratepayers were separately billed and the amounts billed were remitted to State A to be held in trust for the purpose of decommissioning the nuclear power plant owned by X. In that case, X must include in gross income decommissioning costs that relate to amounts billed as well as decommissioning costs that relate to accrued unbilled amounts.

(c) *Cross reference.* For special rules relating to the deduction for amounts paid to a nuclear decommissioning fund, see §1.468A–1T through §1.468A–8T.

(d) *Effective date.* (1) Section 88 and this section apply to nuclear decommissioning costs directly or indirectly charged to the customers of a taxpayer on or after July 18, 1984, and with respect to taxble years ending on or after such date.

(2) If the amount of nuclear decommissioning costs directly or indirectly charged to the customers of a taxpayer before July 18, 1984, is includible in gross income in a different manner than amounts charged for electric energy, such amount

must be included in gross income for the taxable year in which includible in gross income under the method of accounting of the taxpayer that was in effect when such amount was charged to customers.

Par. 3. The following new sections are added in the appropriate places:

§1.468A-1T Nuclear decommissioning costs; general rules (temporary)

(a) *Introduction.* Section 468A provides an elective method for taking into account nuclear decommissioning costs for Federal income tax purposes. In general, an eligible taxpayer that elects the application of section 468A pursuant to the rules contained in §1.468A-7T is allowed a deduction (as determined under §1.468A-2T) for the taxable year in which the taxpayer makes a cash payment to a nuclear decommissioning fund. Taxpayers using an accrual method of accounting that do not elect the application of section 468A are not allowed a deduction for nuclear decommissioning costs prior to the taxable year in which economic performance occurs with respect to such costs (see section 461(h)).

(b) *Definitions.* The following terms are defined for purposes of §§1.468A-1T through 1.468A-8T:

(1) The term "eligible taxpayer" means any taxpayer that possesses a direct ownership interest in a nuclear power plant (including a nuclear power plant that is under construction). Such term includes a taxpayer that owns an interest in a nuclear power plant as a tenant in common or joint tenant, but does not include a taxpayer that owns stock in a corporation which owns a nuclear power plant or a taxpayer that is a partner in a partnership which owns a nuclear power plant. Thus, in the case of a partnership that owns a nuclear power plant, the election under section 468A must be made by the partnership and not by the partners. In the case of an unincorporated organization described in §1.761-2(a)(3) that elects under section 761(a) to be excluded from the application of subchapter K, each taxpayer that is a co-owner of the nuclear power plant is eligible to make a separate election under section 468A.

(2) The term "nuclear decommissioning fund" means a fund that satisfies the requirements of §1.468A-5T.

(3) The term "nuclear power plant" means any nuclear power reactor that is used predominantly in the trade or business of the furnishing or sale of electric energy, if the rates for such furnishing or sale, as the case may be, have been established or approved by a public utility commission. Each unit (*i.e.*, nuclear reactor) located on a multi-unit site is a separate nuclear power plant.

(4) The term "nuclear decommissioning costs" or "decommissioning costs" means all otherwise deductible expenses to be incurred in connection with the entombment, decontamination, dismantlement, removal and disposal of the structures, systems and components of a nuclear power plant that has permanently ceased the production of electric energy. Such term includes all otherwise deductible expenses to be incurred in connection with the preparation for decommissioning, such as engineering and other planning expenses, and all otherwise deductible expenses to be incurred after the actual decommissioning occurs, such as physical security and radiation monitoring expenses. Such term does not include otherwise deductible expenses to be incurred in connection with the disposal of spent nuclear fuel under the Nuclear Waste Policy Act of 1982 (Pub. L. 97-425). An expense is otherwise deductible for purposes of this paragraph (b)(4) if it would be deductible under chapter 1 of the Internal Revenue Code without regard to section 280B.

(5) The term "public utility commission" means any State or political subdivision thereof, any agency, instrumentality or judicial body of the United States, or any judicial body, commission or other similar body of the District of Columbia or of any State or any political subdivision thereof that establishes or approves rates for the furnishing or sale of electric energy.

§1.468A-2T Treatment of electing taxpayer (temporary)

(a) *In general.* An eligible taxpayer that elects the application of section 468A pursuant to the rules contained in §1.468A-7T (an "electing taxpayer") is allowed a deduction for the taxable year in which the taxpayer makes a cash payment (or is deemed to make a cash payment as provided in paragraph (c) of this section) to a nuclear decommissioning fund. The amount of the deduction for any taxable year equals the total amount of cash payments made (or deemed made) by the electing taxpayer to a nuclear decommissioning fund (or nuclear decommissioning funds) during such taxable year. A payment may not be made (or deemed made) to a nuclear decommissioning fund before the first taxable year in which all of the following conditions are satisfied:

(1) The construction of the nuclear power plant has commenced.

(2) Nuclear decommissioning costs of the nuclear power plant to which the nuclear decommissioning fund relates are included in the taxpayer's cost of service for ratemaking purposes (see paragraph (b) of this section).

(3) A ruling amount is applicable to the nuclear decommissioning fund (see §1.468A-3T).

(b) *Limitation on payments to a nuclear decommissioning fund*—(1) *In general.* For purposes of paragraph (a) of this section, the maximum amount of cash payments made (or deemed made) to a nuclear decommissioning fund during any taxable year shall not exceed the lesser of—

(i) The cost of service amount applicable to the nuclear decommissioning fund for such taxable year (as defined in paragraph (b)(2) of this section); or

(ii) The ruling amount applicable to the nuclear decommissioning fund for such taxable year (as determined under §1.468A-3T).

If the amount of cash payments made (or deemed made) to a nuclear decommissioning fund during any taxable year exceeds the limitation of this paragraph (b)(1), the excess is not deductible by the electing taxpayer. In addition, see paragraph (c) of §1.468A-5T for rules which provide that the Internal Revenue Service may disqualify a nuclear decommissioning fund if the amount of cash payments made (or deemed made) to a nuclear decommissioning fund during any taxable year exceeds the limitation of this paragraph (b)(1).

(2) *Cost of service amount.* (i) For purposes of section 468A and the regulations thereunder, the "cost of service amount applicable to a nuclear decommissioning fund for a taxable year" is the amount of decommissioning costs included in the electing taxpayer's cost of service for ratemaking purposes for such taxable year that is properly allocable to the nuclear power plant to which the nuclear decommissioning fund relates. The allocation of the amount of decommissioning costs included in cost of service to each of the nuclear power plants of the electing taxpayer must be performed on a reasonable and consistent basis taking into account the assumptions and determinations, if any,

used by the public utility commission(s) in establishing or approving the amount of decommissioning costs included in cost of service.

(ii) Decommissioning costs shall generally not be considered included in cost of service for purposes of this section unless—

(A) The order or opinion of the applicable public utility commission identifies the amount of decommissioning costs that is included in cost of service for ratemaking purposes; or

(b) The written records of the ratemaking proceeding clearly and unambiguously indicate the amount of decommissioning costs that is included in cost of service of ratemaking purposes.

(c) *Deemed payment rules.* (1) The amount of any cash payment made by an electing taxpayer to a nuclear decommissioning fund on or before the 15th day of the third calendar month after the close of any taxable year (the "deemed payment deadline date") shall be deemed made during such taxable year if the electing taxpayer irrevocably designates the amount as relating to such taxable year on its timely filed Federal income tax return for such taxable year (see paragraph (b) (4) (iv) of §1.468A–7T for rules relating to such designation).

(2) The amount of any cash payment made by a customer of an electing taxpayer to a nuclear decommissioning fund of such electing taxpayer shall be deemed made by the electing taxpayer if the amount is included in the gross income of the electing taxpayer in the manner prescribed by section 88 and §1.88–1T.

(d) *Treatment of distributions*—(1) *In general.* Except as otherwise provided in paragraph (d)(2) of this section, the amount of any actual or deemed distribution from a nuclear decommissioning fund shall be included in the gross income of the electing taxpayer for the taxable year in which the distribution occurs. A distribution from a nuclear decommissioning fund shall include an expenditure from the fund or the use of the fund's assets—

(i) To satisfy, in whole or in part, the liability of the electing taxpayer for decommissioning costs of the nuclear power plant to which the fund relates; or

(ii) To pay administrative costs and other incidental expenses of the fund.

See paragraphs (c) and (d) of §1.468A–5T for rules relating to the deemed distribution of the assets of a nuclear decommissioning fund in the case of a disqualification or termination of the fund. In addition, see paragraph (a) of §1.468A–6T for rules relating to the deemed distribution of the assets of a nuclear decommissioning fund in the case of a disposition of an interest in a nuclear power plant.

(2) *Exceptions to inclusion in gross income*—(i) *Payment of administrative costs and incidental expenses.* The amount of any payment by a nuclear decommissioning fund for administrative costs or other incidental expenses of such fund (as defined in paragraph (a)(3)(ii)(A) of §1.468A–5T) shall not be included in the gross income of the electing taxpayer unless such amount is paid to the electing taxpayer (in which case the amount of the payment is included in the gross income of the electing taxpayer under section 61).

(ii) *Withdrawals of excess contributions.* The amount of a withdrawal of an excess contribution (as defined in paragraph (c)(2)(ii) of §1.468–5T) by an electing taxpayer pursuant to the rules of paragraph (c)(2) of §1.468A–5T shall not be included in the gross income of the electing taxpayer. See paragraph (b)(1) of this section, which provides that the payment of such amount of the nuclear decommissioning fund is not deductible by the electing taxpayer.

(iii) *Actual distributions of amounts included in gross income as deemed distributions.* If the amount of a deemed distribution is included in the gross income of the electing taxpayer for the taxable year in which the deemed distribution occurs, no further amount is required to be included in gross income when the amount of the deemed distribution is actually distributed by the nuclear decommissioning fund. The amount of a deemed distribution is actually distributed by a nuclear decommissioning fund as the first actual distributions are made by the nuclear decommissioning fund on or after the date of the deemed distribution.

(iv) *Distributions upon substantial completion of decommissioning.* The amount of a deemed distribution of the assets of a nuclear decommissioning fund upon termination of the fund (see paragraph (d) of §1.468A–5T) shall not be included in the gross income of the electing taxpayer for the taxable year in which the termination occurs to the extent that the amount is refunded to ratepayers within one calendar year after the termination of the fund. Thus, an amended return may be required if an amount is refunded within the one-year period but after the filing of the original return for the taxable year in which the termination occurs.

(e) *Deduction when economic performance occurs.* An electing taxpayer using an accrual method of accounting is allowed a deduction for nuclear decommissioning costs no earlier than the taxable year in which economic performance occurs with respect to such costs (see section 461(h)(2)). The amount of nuclear decommissioning costs that is deductible under this paragraph (e) is determined without regard to section 280B (see paragraph (b)(4) of §1.468A–1T). A deduction is allowed under this paragraph (e) whether or not a deduction was allowed with respect to such costs under section 468A(a) and paragraph (a) of this section for an earlier taxable year (see paragraph (a)(2) of §1.468A–8T, however, for the effective date applicable to this paragraph (e)).

(f) *Effect of interim rate orders and retroactive adjustments to such orders*—(1) *In general.* (i) The amount of decommissioning costs included in cost of service for any taxable year that ends before the date of a retroactive adjustment to an interim rate order or interim determination of a public utility commission shall include amounts authorized pursuant to such interim rate order or interim determination unless a taxpayer elects the application of paragraph (f)(2) of this section for such taxable year.

(ii) If a retroactive adjustment to an interim rate order or interim determination reduces the amount of decommissioning costs included in cost of service for one or more taxable years ending before the date of the adjustment, the amount of such reduction shall be subtracted from the amount of decommissioning costs included in cost of service (as determined under paragraph (b)(2) of this section) for one or more taxable years ending on or after the date of the adjustment. For this purpose, the amount of such reduction shall be taken into account in the following manner:

(A) If the retroactive order reduces the amount of decommissioning costs included in cost of service for one taxable year ending before the date of the adjustment, the total amount of the reduction shall be taken into account for the taxable year that includes the date of the adjustment.

(B) If the retroactive order reduces the amount of decommissioning costs included in cost of service for two taxable years ending before the date of the adjustment, one-half of the total amount of the reduction shall be taken into account for each of the first two taxable years ending on or after the date of the adjustment.

(C) If the retroactive order reduces the amount of decommissioning costs included in cost of service for three or more taxable years ending before the date of the adjustment, one-third of the total amount of the reduction shall be taken into account for each of the first three taxable years ending on or after the date of the adjustment.

(2) *Special rule permitting withdrawal of excess contribution that results from retroactive adjustment to interim rate order.* (i) If a retroactive adjustment that reduces the amount of decommissioning costs included in cost of service for a taxable year occurs on or before the date prescribed by law (including extensions) for filing the return of the nuclear decommissioning fund for such taxable year, a taxpayer may elect the application of this paragraph (f)(2) for such taxable year by—

(A) Including in the amount of decommissioning costs included in cost of services for such taxable year only the amount of decommissioning costs authorized for such taxable year under the retroactive ajustment; and

(B) Withdrawing any excess contribution that results from such treatment in accordance with the rules of paragraph (c)(2) of §1.468A-5T.

(ii) If a taxpayer elects the application of this paragraph (f)(2) for any taxable year, the retroactive adjustment shall not be treated for purposes of paragraph (f)(1)(ii) of this section as a reduction in the amount of decommissioning costs included in cost of service for such taxable year.

(3) *Revised schedule of ruling amounts.* If the rules provided in this paragraph (f) result in a cost of service amount applicable to a nuclear decommissioning fund for any taxable year that is less than the cost of service amount applicable to the nuclear decommissioning fund for the immediately preceding taxable year, the taxpayer is generally required to request a revised schedule of ruling amounts for the period beginning with the taxable year in which the taxpayer's request must be filed (see paragraph (i)(1)(iii)(C) of §1.468A-3T). If a taxpayer has made an election under paragraph (f)(2) of this section and is required to request a revised schedule of ruling amounts by reason of the cost of service limitation described in paragraph (f)(2)(i)(A) of this section, the taxpayer must file a request for a revised schedule on or before the 90th day following the date that the excess contribution is withdrawn from the nuclear decommissioning fund.

(4) *Example.* The following example illustrates the application of the principles of this paragraph (f):

Example. X corporation is a calendar year, accrual method taxpayer engaged in the sale of electric energy generated by a nuclear power plant owned by X. During 1989, X is authorized pursuant to an interim rate order issued by the public utility commission of State A to collect nuclear decommissioning costs of $500,000 per year beginning on January 1, 1990. On July 1, 1992, the public utility commission of State A issues a final rate order that authorizes X to collect decommissioning costs of $400,000 per year as of January 1, 1990. The excess decommissioning costs of $250,000 collected between January 1, 1990, and July 1, 1992, must be refunded to the ratepayers of State A by X.

If X elects the application of paragraph (f)(2) of this section for the 1991 taxable year, the amount of decommissioning costs included in cost or service for such taxable year is $400,000. If X made a contribution of $500,000 to a nuclear decommissioning fund for the 1991 taxable year, X must withdraw $100,000 from the nuclear decommissioning fund on or before the date prescribed by law (including extensions) for filing the return of the nuclear decommissioning fund for the 1991 taxable year (see paragraph (c)(2) of §1.468A-5T).

In addition, under paragraph (f)(1)(i) of this section, the amount of decommissioning costs included in cost of service for the 1990 taxable year is $500,000, and, under paragraph (f)(1)(ii) of this section, the amount of decommissioning costs included in cost of service for the 1992 taxable year is $300,000. Because the cost of service amount for the 1991 taxable year ($400,000) is less than the cost of service amount for the 1990 taxable year ($500,000) (and because the Internal Revenue Service was not notified of the decrease in the taxpayer's most recent request for a schedule of ruling amounts), paragraph (i)(1)(iii)(C) of §1.468A-3T applies and X must file a request for a revised schedule of ruling amounts for the period beginning with the 1992 taxable year on or before the 90th day following the date that the excess contribution for 1991 is withdrawn from the nuclear decommissioning fund.

Alternatively, if X does not elect the application of paragraph (f)(2) of this section for the 1991 taxable year, under paragraph (f)(1)(i) of this section, the amount of decommissioning costs included in cost of service for the 1990 and 1991 taxable years is $500,000, and, under paragraph (f)(1)(ii) of this section, the amount of decommissioning costs included in cost of service for the 1992 and 1993 taxable years is $300,000. Because the cost of service amount for the 1992 taxable year ($300,000) is less than the cost of service amount for the 1991 taxable year ($500,000) (and because the Internal Revenue Service was not notified of the decrease in the taxpayer's most recent request for a schedule of ruling amounts), paragraph (i)(1)(iii)(C) of §1.468A-3T applies and X must file a request for a revised schedule of ruling amounts for the period beginning with the 1993 taxable year on or before June 29, 1993.

§1.468A-3T Ruling amount (temporary)

(a) *In general.* (1) An electing taxpayer is allowed a deduction under section 468A(a) for the taxable year in which the taxpayer makes a cash payment (or is deemed to make a cash payment) to a nuclear decommissioning fund only if the taxpayer has received a schedule of ruling amounts for the nuclear decommissioning fund that includes a ruling amount for such taxable year. A schedule of ruling amounts for a nuclear decommissioning fund ("schedule of ruling amounts") is a ruling (within the meaning of paragraph (a)(2) of §601.201) specifying the annual payments ("ruling amounts") that, over the taxable years remaining in the "funding period" as of the date the schedule first applies, will result in a projected balance of the nuclear decommissioning fund as of the last day of the funding period equal to (and in no event greater than) the "amount of decommissioning costs allocable to the fund." The projected balance of a nuclear decommissioning fund as of the last day of the funding period shall be calculated by taking into account the fair market value of the assets of the fund as of the first day of the first taxable year to which the schedule of ruling amounts applies and the estimated rate of return to be earned by the assets of the fund after payment of the estimated administrative costs and incidental expenses to be incurred by the fund (as defined in paragraph (a)(3)(ii)(A) of §1.468A-5T), including all Federal, State and local income taxes to be incurred by the fund (the "after-tax rate of return"). See paragraph (c) of this section for a definition of funding period and paragraph (d) of this section for guidance with respect to the amount of decommissioning costs allocable to a fund.

(2) To the extent consistent with the principles and provisions of this section, each schedule of ruling amounts shall be based on the reasonable assumptions and determinations used by the applicable public utility commission(s) in establishing or approving the amount of decommissioning costs included in cost of service for ratemaking purposes. Thus, for example, each schedule of ruling amounts shall be based on the public utility commission's reasonable assumptions concerning the after-tax rate of return to be earned by the nuclear decommissioning

fund and the reasonable assumptions concerning the total estimated cost of decommissioning the nuclear power plant.

(3) The Internal Revenue Service shall provide a schedule of ruling amounts that is identical to the schedule of ruling amounts proposed by the taxpayer in connection with the taxpayer's request for a schedule of ruling amounts (see paragraph (h)(2)(viii) of this section), but no schedule of ruling amounts shall be provided unless the taxpayer's proposed schedule of ruling amounts is consistent with the principles and provisions of this section. If a proposed schedule of ruling amounts is not consistent with the principles and provisions of this section, the taxpayer may propose an amended schedule of ruling amounts that is consistent with such principles and provisions.

(4) The Internal Revenue Service may, in its discretion, provide a schedule of ruling amounts that is determined on a basis other than the rules of paragraphs (a) through (g) of this section if—

(i) In connection with its request for a schedule of ruling amounts, the taxpayer explains the need for special treatment and sets forth an alternative basis for determining the schedule of ruling amounts; and

(ii) The Internal Revenue Service determines that special treatment is consistent with the purpose of section 468A.

(b) *Level funding limitation*—(1) The ruling amount specified in a schedule of ruling amounts for any taxable year in the level funding limitation period shall not be less than the ruling amount specified in such schedule for any earlier taxable year.

(2) For purposes of this section, the level funding limitation period for a nuclear decommissioning fund is the period that—

(i) Begins on the first day of the first taxable year for which a deductible payment is made (or deemed made) to such nuclear decommissioning fund (see paragraph (a)(1) of §1.468A-2T for rules relating to the first taxable year for which a payment may be made (or deemed made) to a nuclear decommissioning fund); and

(ii) Ends on the last day of the taxable year that includes the estimated date on which the nuclear power plant to which the nuclear decommissioning fund relates will no longer be included in the taxpayer's rate base for ratemaking purposes (see paragraph (e)(2) of this section).

(3) The ruling amount specified in a schedule of ruling amounts for a taxable year after the end of the level funding limitation period may be less than the ruling amount specified in such schedule for an earlier taxable year.

(c) *Funding period*—(1) *General rule*. For purposes of this section, the funding period for a nuclear decommissioning fund is that period that—

(i) Begins on the first day of the first taxable year for which a deductible payment is made (or deemed made) to such nuclear decommissioning fund (see paragraph (a)(1) of §1.468A-2T for rules relating to the first taxable year for which a payment may be made (or deemed made) to a nuclear decommissioning fund); and

(ii) Ends on the later of—

(A) The last day of the taxable year that includes the estimated date on which decommissioning costs of the nuclear power plant to which the nuclear decommissioning fund relates will no longer be included in the taxpayer's cost of service for ratemaking purposes (see paragraph (e)(1) of this section); or

(B) The last day of the taxable year that includes the estimated date on which the nuclear power plant to which the nuclear decommissioning fund relates will no longer be included in the taxpayer's rate base for ratemaking purposes (see paragraph (e)(2) of this section).

(2) *Examples*. The following examples illustrate the application of the principles of paragraphs (a), (b) and (c) of this section:

Example (1). (i) X corporation is a calendar year, accrual method taxpayer engaged in the sale of electric energy generated by power plants owned by X. On March 15, 1995, X commences the construction of a nuclear power plant in State A. On May 15, 1995, the public utility commission of State A issues a final rate order for the four-year period beginning on January 1, 1995, that authorizes X to collect decommissioning costs from ratepayers residing in State A. For the 1995 taxable year, X is authorized to collect decommissioning costs of $500,000, and, for each taxable year during the remainder of the period to which the rate order applies, X is authorized to collect decommissioning costs in an amount equal to 105 percent of the amount authorized to be collected for the preceding taxable year.

In determining the amount of decommissioning costs to be collected from ratepayers residing in State A, the public utility commission assumes that (A) decommissioning costs will be included in cost of service for each taxable year in the period that begins with 1995 and ends with 2025 and (B) decommissioning costs collected pursuant to subsequent rate orders will increase in the same manner as amounts collected pursuant to the rate order issued on May 15, 1995. In addition, in determining the rate of return to be earned by X with respect to the nuclear power plant, the public utility commission assumes that the nuclear power plant will be included in rate base for each year in the period that begins with 2000 and ends with 2025.

(ii) X requests a schedule of ruling amounts in accordance with the rules of paragraph (h) of this section for the period beginning with the 1995 taxable year. In determining the level funding limitation period and the funding period, the Internal Revenue Service shall assume that a deductible payment will be made to a nuclear decommissioning fund for the 1995 taxable year. Thus, under paragraph (b) of this section, the level funding limitation period begins on January 1, 1995, and ends on December 31, 2025. Under paragraph (c)(1) of this section, the funding period begins on January 1, 1995, and ends on December 31, 2025.

(iii) In its request for a schedule of ruling amounts, X proposes a ruling amount for each taxable year in the funding period that corresponds to the projected cost of service amount for such taxable year. If (A) the assumptions and determinations used by the public utility commission in establishing the amount of decommissioning costs included in cost of service are reasonable and (B) the amounts collected pursuant to the proposed schedule, combined with the after-tax earnings on such amounts, will result in a projected balance of the nuclear decommissioning fund as of December 31, 2025, equal to the amount of decommissioning costs allocable to the fund, then, under paragraph (a)(3) of this section, each ruling amount in the initial schedule of ruling amounts shall equal the ruling amount proposed by X in connection with its request for a schedule of ruling amounts. Thus, the ruling amount for the 1995 taxable year would be $500,000, and the ruling amount for each subsequent taxable year would be 105 percent of the ruling amount for the preceding taxable year.

Example (2). (i) Assume the same facts as in Example (1), except that on May 15, 1995, the public utility commission of State A issues a final rate order for the four-year period beginning on January 1, 1995, that authorizes X to collect decommissioning costs of $600,000 per year from ratepayers residing in State A. In determining the amount of decommissioning costs to be collected from ratepayers residing in State A, the public utility commission assumes that decommissioning costs of $600,000 will be collected for each taxable year in the period that begins with 1995 and ends with 2004 and that decommissioning costs of $200,000 will be collected for each taxable year in the period that begins with 2005 and ends with 2025.

(ii) X requests a schedule of ruling amounts in accordance with the rules of paragraph (h) of this section for the period beginning with the 1995 taxable year. In determining the level funding limitation period and the funding period, the Internal Revenue Service shall assume that a deductible payment will be made to a nuclear decommissioning fund for the 1995 taxable year. Thus, under paragraph (b) of this section, the level funding limitation period begins on January 1, 1995, and ends on December 31, 2025. Under paragraph (c)(1) of this section, the funding period begins on January 1, 1995, and ends on December 31, 2025.

(iii) In its request for a schedule of ruling amounts, X proposes a ruling amount for each taxable year in the funding period that corresponds to the projected cost of service amount for such taxable year. A schedule of ruling amounts based on the projected cost of service amount would be inconsistent with the level funding limitation of paragraph (b) of this section because the projected cost of service amount for 2025 is less than the projected cost of service amount for 2004. Consequently, under paragraph (a)(3) of this section, no schedule of ruling amounts shall be provided to X unless X proposes an amended schedule of ruling amounts that is consistent with the level funding limitation and the other principles and provisions of this section.

(iv) Assume that X proposes an amended schedule of ruling amounts that provides for ruling amounts of $400,000 for each taxable year in the funding period. If (A) the schedule of ruling amounts proposed by X is based on the reasonable assumptions and determinations used by the public utility commission in establishing the amount of decommissioning costs included in cost of service and (B) the amounts collected pursuant to the proposed schedule, combined with the after-tax earnings on such amounts, will result in a projected balance of the nuclear decommissioning fund as of December 31, 2025, equal to the amount of decommissioning costs allocable to the fund, then, under paragraph (a)(3) of this section, each ruling amount in the initial schedule of ruling amounts shall equal the ruling amount proposed by X in connection with its request for a schedule of ruling amounts. Thus, the ruling amount for the 1995 taxable year and for each subsequent taxable year through 2025 would be $400,000.

(v) Under section 468A(b) and paragraph (b)(1) of §1.468A–2T, the maximum amount of cash payments that X can make to a nuclear decommissioning fund for any taxable year shall not exceed the lesser of (A) the cost of service amount for such taxable year or (B) the rulng amount for such taxable year. If the projected cost of service amount that was assumed in determining rates under the rate order that was issued on May 15, 1995, is the actual cost of service amount for each taxable year in the funding period and the ruling amounts provided in the initial schedule of ruling amounts are not changed by a subsequent schedule of ruling amounts, then X would be allowed to make a deductible contribution of $400,000 to a nuclear decommissioning fund for each taxable year in the period that begins with 1995 and ends with 2004 and to make a deductible contribution of $200,000 to such nuclear decommissioning fund for each taxable year in the period that begins with 2005 and ends with 2025.

Example (3). (i) Y corporation is a calendar year, accrual method taxpayer engaged in the sale of electric energy generated by power plants owned by Y. On June 1, 1990, a nuclear power plant owned by Y began commercial operations in State B. In the first ratemaking proceeding in which the nuclear power plant was included in rate base, the public utility commission of State B assumed that the nuclear power plant would be included in rate base for each year in the period that began with 1990 and ended with 2020. In addition, for each taxable year in the period that began with 1990 and ended with 2017, Y made a deductible contribution of $750,000 to a nuclear decommissioning fund established by Y. The $750,000 contribution equalled the cost of service amount and the ruling amount for each taxable year in the 27-year period.

(ii) On August 30, 2017, the public utility commission of State B issues a final rate order for the six-year period beginning on January 1, 2018, that authorizes Y to collect decommissioning costs of: (A) $500,000 for 2018, 2019, and 2020; (B) $1,500,000 for 2021; (C) $1,000,000 for 2022; and (D) $750,000 for 2023. In determining the amount of decommissioning costs to be collected from ratepayers residing in State B, the public utility commission assumes that decommissioning costs will no longer be included in cost of service after 2023. In addition, in determining the rate of return to be earned by Y with respect to the nuclear power plant, the public utility commission assumes that the nuclear power plant will no longer be included in rate base after 2020.

(iii) Under paragraph (i)(1) of this section, Y is required to request a revised schedule of ruling amounts on or before June 29, 2018. Assume that on March 15, 2018, Y requests a revised schedule of ruling amounts in accordance with the rules of paragraph (h) of this section. In its request, Y proposes a ruling amount for each taxable year in the period that begins with 2018 and ends with 2023 that corresponds to the amount of decommissioning costs to be included in cost of service under the rate order of August 30, 2017.

(iv) Under paragraph (b) of this section, the level funding limitation period begins on January 1, 1990, and ends on December 31, 2020. Under paragraph (c)(1) of this section, the funding period begins on January 1, 1990, and ends on December 31, 2023.

(v) If (A) the assumptions and determinations used by the public utility commission in establishing the amount of decommissioning costs included in cost of service are reasonable and (B) the projected balance of the nuclear decommissioning fund as of December 31, 2023 (taking into account the fair market value of the assets of the fund as of January 1, 2018, and the estimated after-tax rate of return to be earned by the assets of the fund) will equal the amount of decommissioning costs allocable to the fund, then, under paragraph (a)(3) of this section, each ruling amount in the revised schedule of ruling amounts shall equal the ruling amount proposed by Y in connection with its request for a schedule of ruling amounts. Thus, the ruling amount for 2018, 2019 and 2020 would be $500,000, the ruling amount for 2021 would be $1,500,000, the ruling amount for 2021 would be $1,500,000, the ruling amount for 2022 would be $750,000. Although the ruling amount specified in the revised schedule of ruling amounts for 2018, 2019, and 2020 is less than a ruling amount specified in a prior schedule of ruling amounts for years prior to 2018, the revised schedule of ruling amounts is consistent with the level funding limitation. Under paragraph (i)(3) of this section, a ruling amount specified in a revised schedule of ruling amounts for any taxable year in the level funding limitation period can be less than one or more ruling amounts specified in a prior schedule of ruling amounts for a prior taxable year. In addition, although the ruling amount specified in the revised schedule of ruling amounts for 2021, 2022 and 2023 is less than a ruling amount specified in such schedule for a prior taxable year, the revised schedule of ruling amounts is consistent with the level funding limitation because the level funding limitation period ends on December 31, 2020.

(d) *Decommissioning costs allocable to a fund*. The amount of decommissioning costs allocable to a nuclear decommissioning fund is determined for purposes of this section by applying the following rules and definitions:

(1) *General rule*. The amount of decommissioning costs allocable to a nuclear decommissioning fund is the taxpayer's share of the total estimated cost of decommissioning the nuclear power plant to which the fund relates, multiplied by the qualifying percentage.

(2) *Total estimated cost of decommissioning*. (i) The total estimated cost of decommissioning a nuclear power plant is the reasonably estimated cost of decommissioning used by the applicable public utility commission in establishing or approving the amount of decommissioning costs included in cost of service for ratemaking purposes. If the estimated costs used by the applicable public utility commission are expected to be paid in any taxable year other than the taxable year that includes the last day of the funding period or the immediately succeeding taxable year, such costs must be adjusted (decreased or increased, as the case may be) by discounting or compounding such costs at the assumed after-tax rate of return from the date such costs are expected to be paid to the last day of the funding period.

(3) *Taxpayer's share*. The taxpayer's share of the total estimated cost of decommissioning a nuclear power plant equals the total estimated cost of decommissioning such nuclear power plant multiplied by the percentage of such nuclear power plant that is directly owned by the taxpayer (see paragraph (b)(1) of §1.468A–1T for circumstances in which a taxpayer possesses a direct ownership interest in a nuclear power plant).

(4) *Qualifying percentage*. (i) Except as otherwise provided in paragraph (b)(5)(i) of §1.468A–8T (relating to a special transitional rule), the qualifying percentage for any nuclear decommissioning fund is equal to the fraction, the numerator of which is the number of taxable years in the estimated period for which the nuclear decommissioning fund is to be in effect and the denominator of which is the number of taxable years in the estimated useful life of the applicable nuclear power plant.

(ii) Except as otherwise provided in paragraph (b)(5)(ii) of §1.468A–8T (relating to a special transitional rule), the estimated period for which a nuclear decommissioning fund is to be in effect—

(A) Begins on the later of—

(1) The first day of the first taxable year for which a deductible payment is made (or deemed made) to such nuclear decommissioning fund; or

(2) The first day of the taxable year that includes the date that the nuclear power plant to which such nuclear decommissioning fund relates begins commercial operations; and

(B) Ends on the last day of the taxable year that includes the estimated date on which the nuclear power plant to which such nuclear decommissioning fund relates will no longer be included in the taxpayer's rate base for ratemaking purposes (see paragraph (e)(3) of this section).

(iii) The estimated useful life of a nuclear power plant—

(A) Begins on the first day of the taxable year that includes the date that the nuclear power plant begins commercial operations; and

(B) Ends on the last day of the taxable year that includes the estimated date on which the nuclear power plant will no longer be included in the taxpayer's rate base for ratemaking purposes (see paragraph (e)(3) of this section).

(e) *Determination of estimated dates.*

(1) For purposes of paragraph (c)(1)(ii)(A) of this section (relating to the funding period), the estimated date on which decommissioning costs of the nuclear power plant to which the nuclear decommissioning fund relates will no longer be included in the taxpayer's cost of service for ratemaking purposes is determined under the ratemaking assumptions that were used to determine the last rates (whether interim or final) that were established or approved by the applicable public utility commission prior to the filing of the current request for a schedule of ruling amounts.

(2) For purposes of paragraph (b)(2)(ii) and (c)(1)(ii)(B) of this section (relating to the level funding limitation period and the funding period), the estimated date on which the nuclear power plant to which the nuclear decommissioning fund relates will no longer be included in the taxpayer's rate base for ratemaking purposes is determined under the ratemaking assumptions that were used to determine the last rates (whether interim or final) that were established or approved by the applicable public utility commission prior to the filing of the current request for a schedule of ruling amounts.

(3) For purposes of paragraph (d)(4)(ii)(B) of this section (relating to the qualifying percentage), the estimated date on which the nuclear power plant to which the nuclear decommissioning fund relates will no longer be included in the taxpayer's rate base for ratemaking purposes is determined under the ratemaking assumptions used by the applicable public utility commission in establishing or approving rates during the first ratemaking proceeding in which the nuclear power plant was included in the taxpayer's rate base.

(f) *Special rules in the case of rates established or approved by two or more public utility commissions.* If two or more public utility commissions establish or approve rates for electric energy generated by a single nuclear power plant, the following rules shall apply in determining the schedule of ruling amounts for the nuclear decommissioning fund that relates to such nuclear power plant:

(1) A schedule of ruling amounts shall be separately determined pursuant to the rules of paragraphs (a) through (e) of this section for each public utility commission that has determined the amount of decommissioning costs to be included in cost of service for ratemaking purposes with respect to such nuclear power plant (see paragraph (g) of this section).

(2) The separate determination with respect to a public utility commission shall be based on the reasonable assumptions and determinations used by such public utility commission and shall take into account only that portion of the total estimated cost of decommissioning the nuclear power plant that is properly allocable to the ratepayers whose rates are established or approved by such public utility commission.

(3) The ruling amount applicable to the nuclear decommissioning fund for any taxable year is the sum of the ruling amounts for such taxable year determined under the separate schedules of ruling amounts.

(4) The schedule of ruling amounts for the nuclear decommissioning fund is the schedule of the ruling amounts determined under paragraph (f)(3) of this section.

(g) *Requirement of determination by public utility commission of decommissioning costs to be included in cost of service.* The Internal Revenue Service will not provide a taxpayer with a schedule of ruling amounts for any nuclear decommissioning fund unless a public utility commission that establishes or approves rates for electric energy generated by the nuclear power plant to which the nuclear decommissioning fund relates has determined the amount of decommissioning costs of such nuclear power plant to be included in the taxpayer's cost of service for ratemaking purposes.

(h) *Manner of requesting schedule of ruling amounts*—(1) *In general.* (i) In order to receive a ruling amount for any taxable year, a taxpayer must file a request for a schedule of ruling amounts that complies with the requirements of this paragraph (h), the applicable procedural rules set forth in paragraph (e) of §601.201 (Statement of Procedural Rules) and the requirements of any applicable revenue procedure that is in effect on the date the request is filed.

(ii) A separate request for a schedule of ruling amounts is required for each nuclear decommissioning fund established by a taxpayer (see paragraph (a) of §1.468A-5T for rules relating to the number of nuclear decommissioning funds that a taxpayer can establish).

(iii) A request for a schedule of ruling amounts must not contain a request for a ruling on any other issue, whether the issue involves section 468A or another section of the Internal Revenue Code.

(iv) A request for a schedule of ruling amounts must be mailed or delivered to the Internal Revenue Service, Associate Chief Counsel (Technical), Attention CC:C:E, 1111 Constitution Avenue, N.W., Washington, D.C. 20224.

(v) Except as otherwise provided in paragraph (b)(1) of §1.468A-8T, the Internal Revenue Service shall not provide a taxpayer with a ruling amount applicable to any taxable year that ends before the taxable year in which a request for a schedule of ruling amounts is filed. In addition, except as otherwise provided in paragraph (b)(1) of §1.468A-8T, a taxpayer should file a request for a schedule of ruling amounts on or before the 180th day of a taxable year to assure receipt of the schedule of ruling amounts on or before the deemed payment deadline date (within the meaning of paragraph (c)(1) of §1.468A-2T) applicable to such taxable year. If a request for a schedule of ruling amounts (other than a request required by reason of an election under paragraph (f)(2) of §1.468A-2T) is filed after the 180th day of a taxable year, the Internal Revenue Service may be unable to provide the taxpayer with a schedule of ruling amounts on or before the deemed payment deadline date applicable to such taxable year. In determining the date when a request is filed, the principles of sections 7502 and 7503 shall apply.

(vi) Except as provided in paragraph (h)(1)(vii) of this section, a request for a schedule of ruling amounts shall be considered filed only if such request complies substantially with the requirements of this paragraph (h).

(vii) If a request does not comply substantially with the requirements of this paragraph (h), the Internal Revenue Service shall notify the taxpayer of this fact. If the information or materials necessary to comply substantially with the requirements of this paragraph (h) are provided to the Internal Revenue Service within 60 days after such notification, the request shall be considered filed on the date of original submission. If the information or materials necessary to comply substantially with the requirements of this paragraph (h) are not provided within 60 days after such notification, the request shall be considered filed on the date that all information or materials necessary to comply substantially with the requirements of this paragraph (h) are provided.

(2) *Information required.* A request for a schedule of ruling amounts must contain the following information:

(i) The taxpayer's name, address and taxpayer identification number.

(ii) Whether the request is for an initial schedule of ruling amounts, a mandatory review of the schedule of ruling amounts (see paragraph (i)(1) of this section) or an elective review of the schedule of ruling amounts (see paragraph (i)(2) of this section).

(iii) The name and location of the nuclear power plant with respect to which a schedule of ruling amounts is requested.

(iv) A description of the taxpayer's ownership interest in the nuclear power plant and the percentage of such nuclear power plant that is directly owned by the taxpayer.

(v) An identification of each public utility commission that establishes or approves rates for the furnishing or sale by the taxpayer of electric energy generated by the nuclear power plant and, for each public utility commission identified—

(A) Whether the public utility commission has determined the amount of decommissioning costs to be included in the taxpayer's cost of service for ratemaking purposes; and

(B) Whether a proceeding is pending before the public utility commission that may result in an increase or decrease in the amount of decommissioning costs included in the taxpayer's cost of service.

(vi) For each public utility commission that has determined the amount of decommissioning costs to be included in the taxpayer's cost of service for ratemaking purposes—

(A) The amount of decommissioning costs that are to be included in the taxpayer's cost of service for each taxable year under the current determination;

(B) A description of the assumptions, estimates and other factors that were used in determining the amounts described in paragraph (h)(2)(vi)(A) of this section, including each of the following if applicable—

(*1*) A description of the proposed method of decommissioning the nuclear power plant (for example, prompt removal/dismantlement, safe storage entombment with delayed dismantlement, or safe storage mothballing with delayed dismantlement);

(*2*) The estimated year in which substantial decommissioning costs will first be incurred;

(*3*) The estimated year in which the decommissioning of the nuclear power plant will be substantially complete (see paragraph (d)(2) of §1.468A–5T for a definition of substantial completion of decommissioning);

(*4*) The total estimated cost of decommissioning expressed in current dollars (*i.e.*, based on price levels on the date that the request for a schedule of ruling amounts is made);

(*5*) The total estimated cost of decommissioning expressed in future dollars (*i.e.*, based on anticipated price levels when expenses are expected to be paid);

(*6*) For each taxable year in the period that begins with the year specified in paragraph (h)(2)(vi)(B)(*2*) of this section ("the estimated year in which substantial decommissioning costs will first be incurred") and ends with the year specified in paragraph (h)(2)(vi)(B)(*3*) of this section ("the estimated year in which the decommissioning of the nuclear power plant will be substantially complete"), the estimated cost of decommissioning expressed in future dollars;

(*7*) A description of the methodology used in converting the estimated cost of decommissioning expressed in current dollars to the estimated cost of decommissioning expressed in future dollars;

(*8*) The assumed after-tax rate of return to be earned by the amounts collected for decommissioning;

(*9*) The proposed period over which decommissioning costs will be included in the cost of service of the taxpayer and the projected amount that will be included in cost of service for each taxable year in the proposed period;

(*10*) The estimated date on which the nuclear power plant will no longer be included in the taxpayer's rate base for ratemaking purposes as determined under the ratemaking assumptions that were used to determine the last rates (whether interim or final) that were established or approved by the applicable public utility commission prior to the filing of the current request for a schedule of ruling amounts; and

(*11*) The estimated date on which the nuclear power plant will no longer be included in the taxpayer's rate base for ratemaking purposes as determined under the ratemaking assumptions that were used by the applicable public utility commission in establishing or approving rates during the first ratemaking proceeding in which the nuclear power plant was included in the taxpayer's rate base.

(C) A copy of the public utility commission's most recent determination that includes decommissioning costs in cost of service; and

(D) A copy of each engineering or cost study that was relied on or used by the taxpayer or the public utility commission in determining the amount of decommissioning costs to be included in the taxpayer's cost of service under the current determination.

(vii) For each proceeding pending before a public utility commission that may result in an increase or decrease in the amount of decommissioning costs included in the taxpayer's cost of service—

(A) A description of the stage of the proceeding;

(B) The amount of decommissioning costs that are proposed to be included in the taxpayer's cost of service for each taxable year;

(C) A description of the assumptions, estimates and other factors that were used in determining the amount of decommissioning costs that are proposed to be included in the taxpayer's cost of service for each taxable year, including each of the items described in paragraph (h)(2)(vi)(B) of this section if applicable; and

(D) A copy of each engineering or cost study that was relied on or used by the taxpayer or the public utility commission in determining the amount of decommissioning costs that are proposed to be included in the taxpayer's cost of service.

(viii) A proposed schedule of ruling amounts for each taxable year remaining in the funding period as of the date the schedule of ruling amounts will first apply.

(ix) A description of the assumptions, estimates and other factors that were used in determining the proposed schedule of ruling amounts, including each of the following—

(A) The level funding limitation period (as such term is defined in paragraph (b)(2) of this section);

(B) The funding period (as such term is defined in paragraph (c) of this section);

(C) The assumed after-tax rate of return to be earned by the assets of the nuclear decommissioning fund;

(D) The fair market value of the assets (if any) of the nuclear decommissioning fund as of the first day of the first taxable year to which the schedule of ruling amounts will apply;

(E) The amount expected to be earned by the assets of the nuclear decommissioning fund (based on the after-tax rate of return applicable to the fund) over the period that begins on the first day of the first taxable year to which the schedule of ruling amounts will apply and ends on the last day of the funding period;

(F) The amount of decommissioning costs allocable to the nuclear decommissioning fund (as such term is defined in paragraph (d) of this section);

(G) The total estimated cost of decommissioning (as such term is defined in paragraph (d)(2) of this section);

(H) The taxpayer's share of the total estimated cost of decommissioning (as such term is defined in paragraph (d)(3) of this section);

(I) The qualifying percentage (as such term is defined in paragraph (d)(4)(i) of this section);

(J) The estimated period for which the nuclear decommissioning fund is to be in effect (as such term is defined in paragraph (d)(4)(ii) of this section); and

(K) The estimated useful life of the nuclear power plant (as such term is defined in paragraph (d)(4)(iii) of this section).

(x) If applicable, an explanation of the need for a schedule of ruling amounts determined on a basis other than the rules of paragraphs (a) through (g) of this section and a description of an alternative basis for determining a schedule of ruling amounts (see paragraph (a)(3) of this section).

(xi) Any other information required by the Internal Revenue Service that may be necessary or useful in determining the schedule of ruling amounts.

(3) *Administrative procedures.* The Internal Revenue Service may prescribe administrative procedures that supplement the provisions of paragraphs (h)(1) and (h)(2) of this section. In addition, the Internal Revenue Service, in its discretion, can waive the requirements of paragraph (h)(1) and (h)(2) under appropriate circumstances.

(i) *Review and revision of schedule of ruling amounts*—(1) *Mandatory review.* (i) Any taxpayer that has obtained a schedule of ruling amounts pursuant to paragraph (h) of this section must file a request for a revised schedule of ruling amounts on or before the 180th day of the 10th taxable year following the close of the taxable year in which the most recent schedule of ruling amounts was received. In addition, if any of the events specified in paragraph (i)(1)(iii) of this section occurs, the taxpayer must file a request for a revised schedule of ruling amounts on or before the 180th day of the taxable year following the taxable year in which the event occurs. See paragraph (f)(3) of §1.468A–2T for an exception to the 180-day requirement in the case of certain retroactive adjustments to interim rate orders. See, also, paragraph (a)(2) of §1.468A–6T for rules requiring a revised schedule of ruling amounts in the case of a sale, exchange or other disposition of a portion of an electing taxpayer's direct ownership interest in a nuclear power plant.

(ii) A request for a schedule of ruling amounts required by paragraph (i)(1)(i) of this section must be made in accordance with the rules of paragraph (h) of this section. If a taxpayer does not properly file a request for a revised schedule of ruling amounts by the date provided in paragraph (i)(1)(i) of this section or paragraph (f)(3) of §1.468A–2T, the taxpayer's ruling amount for the taxable year that includes such date and for all succeeding taxable years until a new schedule is obtained shall be zero unless, in its discretion, the Internal Revenue Service provides otherwise in such new schedule of ruling amounts.

(iii) A taxpayer is required to request a revised schedule of ruling amounts in accordance with the rules of paragraph (h) of this section if—

(A) Any public utility commission that establishes or approves rates for the furnishing or sale of electric energy generated by a nuclear power plant to which a nuclear decommissioning fund relates increases the proposed period over which decommissioning costs of such nuclear power plant will be included in cost of service for ratemaking purposes and the Internal Revenue Service was not notified of the increase in the taxpayer's most recent request for a schedule of ruling amounts;

(B) Any public utility commission that establishes or approves rates for the furnishing or sale of electric energy generated by a nuclear power plant to which a nuclear decommissioning fund relates adjusts the estimated date on which such nuclear power plant will no longer be included in the taxpayer's rate base for ratemaking purposes and the Internal Revenue Service was not notified of the adjustment in the taxpayer's most recent request for a schedule of ruling amounts; or

(C) The cost of service amount applicable to the nuclear decommissioning fund for any taxable year (as defined in paragraph (b)(2) of §1.468A–2T) is less than the cost of service amount applicable to the nuclear decommissioning fund for the immediately preceding taxable year and the Internal Revenue Service was not notified of the decrease in the taxpayer's most recent request for a schedule of ruling amounts.

(2) *Elective review.* Any taxpayer that has obtained a schedule of ruling amounts pursuant to paragraph (h) of this section can request a revised schedule of ruling amounts. Such a request must be made in accordance with the rules of paragraph (h) of this section; thus, the Internal Revenue Service generally will not provide a revised ruling amount applicable to any taxable year that ends before the taxable year in which the request for a revised schedule of ruling amounts is filed (see paragraph (h)(1)(v) of this section).

(3) *Determination of revised schedule of ruling amounts.* A revised schedule of ruling amounts for a nuclear decommissioning fund shall be determined under this section without regard to any schedule of ruling amounts for such nuclear decommissioning fund that was issued prior to such revised schedule. Thus, a ruling amount specified in a revised schedule of ruling amounts for any taxable year in the level funding limitation period can be less than one or more ruling amounts specified in a prior schedule of ruling amounts for a prior taxable year.

§1.468A–4T Treatment of nuclear decommissioning fund (temporary)

(a) *In general.* A nuclear decommissioning fund is subject to tax on all of its modified gross income (as defined in paragraph (b) of this section) for any taxable year at a single rate equal to the maximum rate in effect under section 11(b) (determined without regard to the amendment to section 11(b) made by the Tax Reform Act of 1984). Such tax is in lieu of any other tax that may be imposed under subtitle A of the Internal Revenue Code on the income earned by the assets of the nuclear decommissioning fund.

(b) *Modified gross income*. For purposes of this section, the term "modified gross income" means gross income as defined under section 61 computed with the following modifications:

(1) The amount of any payment to the nuclear decommissioning fund with respect to which a deduction is allowed under section 468A(a) is excluded from gross income.

(2) A deduction is allowed for the amount of administrative costs and other incidental expenses of the nuclear decommissioning fund (including taxes, legal expenses, accounting expenses, actuarial expenses and trustee expenses, but not including decommissioning costs) that are otherwise deductible and that are paid by the nuclear decommissioning fund to any person other than the electing taxpayer. An expense is otherwise deductible for purposes of this paragraph (b)(2) if it would be deductible under chapter 1 of the Internal Revenue Code in determining the taxable income of a corporation. For example, because Federal income taxes are not deductible under chapter 1 of the Internal Revenue Code in determining the taxable income of a corporation, the tax imposed by section 468A(e)(2) and paragraph (a) of this section is not deductible in determining the modified gross income of a nuclear decommissioning fund. Similarly, because certain expenses allocable to tax-exempt interest income are not deductible under section 265 of the Internal Revenue Code in determining the taxable income of a corporation, such expenses are not deductible in determining the modified gross income of a nuclear decommissioning fund.

(3) A deduction is allowed for the amount of otherwise deductible losses that are sustained by the nuclear decommissioning fund in connection with the sale, exchange or worthlessness of an investment described in paragraph (a)(3)(i)(C) of §1.468A-5T. A loss is otherwise deductible for purposes of this paragraph (b)(3) if such a loss would be deductible by a corporation under section 165(f) or (g) and sections 1211(a) and 1212(a).

(4) A deduction is allowed for the amount of an otherwise deductible net operating loss of the nuclear decommissioning fund. For purposes of this paragraph, the net operating loss of a nuclear decommissioning fund for a taxable year is the amount by which the deductions allowable under paragraph (b)(2) and (3) of this section exceed the gross income of the nuclear decommissioning fund computed with the modification described in paragraph (b)(1) of this section. A net operating loss is otherwise deductible for purposes of this paragraph (b)(4) if such a net operating loss would be deductible by a corporation under section 172(a).

(c) *Special rules*—(1) *Period for computation of modified gross income*. The modified gross income of a nuclear decommissioning fund must be computed on the basis of the taxable year of the electing taxpayer. If an electing taxpayer changes its taxable year, each nuclear decommissioning fund of the electing taxpayer must change to the new taxable year. See section 442 and §1.442-1 for rules relating to the change to a new taxable year.

(2) *Recognition of gain or loss upon distribution of property by a fund*. A distribution of property by a nuclear decommissioning fund (whether an actual distribution or a deemed distriubtion) shall be considered a disposition of property by the nuclear decommissioning fund for purposes of section 1001. In determining the amount of gain or loss from such disposition, the amount realized by the nuclear decommissioning fund shall be the fair market value of the property on the date of disposition. Except as otherwise provided in paragraph (b)(3) of this section, a nuclear decommissioning fund must include in modified gross income the amount of any gain or loss realized on the disposition of the property notwithstanding any provision of the Internal Revenue Code that provides that the gain or loss is not realized or recognized.

(3) *Denial of credits against tax*. The tax imposed on the modified gross income of a nuclear decommissioning fund under paragraph (a) of this section is not to be reduced or offset by any credits against tax provided by part IV of subchapter A of chapter 1 of the Internal Revenue Code other than the credit provided by section 31(c) for amounts withheld under section 3406 (back-up withholding).

(4) *Other corporate taxes inapplicable*. Although the modified gross income of a nuclear decommissioning fund is subject to tax at a rate equal to the maximum rate in effect under section 11(b) (determined without regard to the amendment to section 11(b) made by the Tax Reform Act of 1984), a nuclear decommissioning fund is not subject to the other taxes imposed on corporations under subtitle A of the Internal Revenue Code. For example, a nuclear decommissioning fund is not subject to the corporate minimum tax imposed by section 56, the accumulated earnings tax imposed by section 531, the personal holding company tax imposed by section 541, and the alternative tax imposed on a corporation under section 1201(a).

(d) *Treatment as corporation for purposes of subtitle F*. For purposes of subtitle F of the Internal Revenue Code and the regulations thereunder, a nuclear decommissioning fund is to be treated as if it were a corporation and the tax imposed by section 468A(e)(2) and paragraph (a) of this section is to be treated as a tax imposed by section 11. Thus, for example, the following rules apply:

(1) A nuclear decommissioning fund must file a return with respect to the tax imposed by section 468A(e)(2) and paragraph (a) of this section for each taxable year (or portion thereof) that the fund is in existence even though no amount is included in the gross income of the fund for such taxable year. The return is to be made on Form 1120-ND. For purposes of this paragraph (d)(1), a nuclear decommissioning fund is in existence for the period that—

(i) Begins on the date that the first deductible payment is actually made to such nuclear decommissioning fund; and

(ii) Ends on the date of termination (see paragraph (d) of §1.468A-5T), the date of disqualification (see paragraph (c) of §1.468A-5T) or the date that the electing taxpayer disposes of its entire direct ownership interest in the nuclear power plant to which the nuclear decommissioning fund relates (see paragraph (a) of §1.468A-6T), whichever is applicable.

(2) For each taxable year of the nuclear decommissioning fund, the return described in paragraph (d)(1) of this section must be filed on or before the 15th day of the third month following the close of such taxable year unless the nuclear decommissioning fund is granted an extension of time for filing under section 6081. If such an extension is granted for any taxable year, the return for such taxable year must be filed on or before the ex-

tended due date for such taxable year. In no event will the filing of the initial return of a nuclear decommissioning fund be required before January 7, 1987.

(3) A nuclear decommissioning fund must provide its employer identification number on returns, statements and other documents as required by the forms and instructions relating thereto. The employer identification number is obtained by filing a Form SS-4 in accordance with the instructions relating thereto.

(4) A nuclear decommissioning fund must make payments of estimated tax during its taxable year as provided in section 6154(b) if its estimated tax for such taxable year can reasonably be expected to be $40 or more. For purposes of section 6154 and this section, the estimated tax of a nuclear decommissioning fund for any taxable year is the amount that the nuclear decommissioning fund estimates as the amount of tax imposed by section 468A(e)(2) and paragraph (a) of this section for such taxable year.

(5) A nuclear decommissioning fund must deposit all payments of tax imposed by section 468A (e)(2) and paragraph (a) of this section (including any payments of estimated tax) with an authorized government depositary in accordance with §1.6302-1.

(6) A nuclear decommissioning fund is subject to the addition to tax imposed by section 6655 in case of a failure to pay estimated income tax. For purposes of section 6655 and this section—

(i) The tax with respect to which the amount of the underpayment is computed in the case of a nuclear decommissioning fund is the tax imposed by section 468A(e)(2) and paragraph (a) of this section; and

(ii) A nuclear decommissioning fund is to be considered a large corporation under section 6655(i) if such nuclear decommissioning fund had modified gross income (as defined in paragraph (b) of this section) of $1,000,000 or more for any taxable year during the testing period.

§1.468A-5T Nuclear decommissioning fund qualification requirements; prohibitions against self-dealing; disqualification of nuclear decommissioning fund; and termination of fund upon substantial completion of decommissioning (temporary)

(a) *Qualification requirements*—(1) *In general.* A nuclear decommissioning fund must be a trust established or organized and maintained at all times in the United States for the exclusive purpose of providing funds for the decommissioning of a nuclear power plant. A separate nuclear decommissioning fund is required for each electing taxpayer and for each nuclear power plant with respect to which an electing taxpayer possesses a direct ownership interest. An electing taxpayer can maintain only one nuclear decommissioning fund for each nuclear power plant with respect to which the taxpayer elects the application of section 468A.

(2) *Limitation on contributions.* Except as otherwise provided in paragraph (b)(1)(ii) of §1.468A-6T (relating to the acquisition of an interest in a nuclear power plant from a taxpayer that maintained a nuclear decommissioning fund with respect to such nuclear power plant), a nuclear decommissioning fund is not permitted to accept any contributions in cash or property other than cash payments with repect to which a deduction is allowed under section 468A(a) and paragraph (a) of §1.468A-2T. Thus, for example, securities may not be contributed to a nuclear decommissioning fund even if the taxpayer or a fund established by the taxpayer previously held such securities for the purpose of providing funds for the decommissioning of a nuclear power plant.

(3) *Limitation on use of fund*—(i) *In general.* The assets of a nuclear decommissioning fund are to be used exclusively—

(A) To satisfy, in whole or in part, the liability of the electing taxpayer for decommissioning costs of the nuclear power plant to which the nuclear decommissioning fund relates;

(B) To pay administrative costs and other incidental expenses of the nuclear decommissioning fund; and

(C) To the extent that the assets of the nuclear decommissioning fund are not currently required for the purposes described in paragraph (a)(3)(i)(A) or (B) of this section, to invest in—

(1) Public debt securities of the United States;

(2) Obligations of a State or local government that are not in default as to principal or interest; or

(3) Time or demand deposits in a bank (as defined in section 581) or an insured credit union (within the meaning of section 101(6) of the Federal Credit Union Act, 12 U.S.C. 1752 (7) (1982)), located in the United States.

(ii, *Terms defined.* For purposes of paragraph (a)(3)(i) of this section:

(A) The term "administrative costs and other incidental expenses of a nuclear decommissioning fund" means all ordinary and necessary expenses incurred in connection with the operation of the nuclear decommissioning fund. Such term includes the tax imposed by section 468A(e)(2) and paragraph (a) of §1.468A-4T, any State or local tax imposed on the income or the assets of the fund, legal expenses, accounting expenses, actuarial expenses and trustee expenses. Such term does not include decommissioning costs. Such term also does not include the excise tax imposed on the trustee or other disqualified person under section 4951 or the reimbursement of any expenses incurred in connection with the assertion of such tax unless such expenses are considered reasonable and necessary under section 4951(d)(2)(C) and it is determined that the trustee or other disqualified person is not liable for the excise tax.

(B) The term "public debt securities of the United States" means obligations that are taken into consideration for purposes of the public debt limit.

(C) The term "obligations of a State of local government" means the obligations of a State or local governmental unit the interest on which is exempt from tax under section 103(a).

(D) The term "time or demand deposits" includes checking accounts, savings accounts, certificates of deposit or other time or demand deposits. The term does not include common or collective trust funds, such as a common trust fund as defined in section 584.

(b) *Prohibitions against self-dealing*—(1) *In general.* Except as otherwise provided in this paragraph (b), the excise taxes imposed by section 4951 shall apply to each act of self-dealing between a disqualified person and a nuclear decommissioning fund.

(2) *Self-dealing defined.* For purposes of this paragraph (b), the term "self-dealing" means any act described in section 4951(d), except—

(i) A payment by a nuclear decommissioning fund for the purpose of satisfying, in whole or in part, the liability of the electing taxpayer for decommissioning costs of the nuclear power plant to which the nuclear decommissioning fund relates;

(ii) A withdrawal of an excess contribution by the electing taxpayer pursuant to the rules of paragraph (c)(2) of this section;

(iii) A payment of amounts remaining in a nuclear decommissioning fund to the electing taxpayers after the termination of such fund (as determined under paragraph (d) of this section); or

(iv) Any act described in section 4951(d)(2)(B) or (C).

(3) *Disqualified person defined.* For purposes of this paragraph (b), the term "disqualified person" includes each person described in section 4951(e)(4) and paragraph (d) of §53.4951–1.

(c) *Disqualification of nuclear decommissioning fund*—(1) *In general.* Except as otherwise provided in paragraph (c)(2) of this section, if at any time during a taxable year of a nuclear decommissioning fund—

(i) The nuclear decommissioning fund does not satisfy the requirements of paragraph (a) of this section, or

(ii) The nuclear decommissioning fund and a disqualified person engage in an act of self-dealing (as defined in paragraph (b)(2) of this section),

the Internal Revenue Service may, in its discretion, disqualify all or any portion of the fund as of the date that the fund does not satisfy the requirements of paragraph (a) of this section or the date on which the act of self-dealing occurs, whichever is applicable, or as of any subsequent date ("date of disqualification"). The Internal Revenue Service shall notify the electing taxpayer of the disqualification of a nuclear decommissioning fund and the date of disqualification by registered or certified mail to the last known address of the electing taxpayer (the "notice of disqualification").

(2) *Exception to disqualification*—(i) *In general.* A nuclear decommissioning fund will not be disqualified under paragraph (c)(1) of this section by reason of an excess contribution or the withdrawal of such excess contribution by an electing taxpayer if the amount of the excess contribution is withdrawn by the electing taxpayer on or before the date prescribed by law (including extensions) for filing the return of the nuclear decommissioning fund for the taxable year to which the excess contribution relates.

(ii) *Excess contribution defined.* For purposes of this section, an excess contribution is the amount by which cash payments made (or deemed made) to a nuclear decommissioning fund during any taxable year exceed the payment limitation contained in section 468A(b) and paragraph (b) of §1.468A–2T.

(iii) *Taxation of income attributable to an excess contribution.* The income of a nuclear decommissioning fund attributable to an excess contribution is required to be included in the gross income of the nuclear decommissioning fund under paragraph (b) of §1.468A–4T.

(3) *Effect of disqualification.* If all or any portion of a nuclear decommissioning fund is disqualified under paragraph (c)(1) of this section, the portion of the nuclear decommissioning fund that is disqualified is treated as distributed to the electing taxpayer on the date of disqualification. Such a distribution shall be treated for purposes of section 1001 as a disposition of property held by the nuclear decommissioning fund (see paragraph (c)(2) of §1.468A–4T). In addition, the electing taxpayer must include in gross income for the taxable year that includes the date of disqualification an amount equal to the product of—

(i) The fair market value of the assets of the fund determined as of the date of disqualification, reduced by—

(A) The amount of any excess contribution that was not withdrawn before the date of disqualification if no deduction was allowed with respect to such excess contribution; and

(B) The amount of any deemed distribution that was not actually distributed before the date of disqualification (as determined under paragraph (c)(2)(iii) of §1.468A–2T) if the amount of the deemed distribution was included in the gross income of the electing taxpayer for the taxable year in which the deemed distribution occurred;

and

(ii) The fraction of the nuclear decommissioning fund that was disqualified under paragraph (c)(1) of this section.

Contributions made to a disqualified fund after the date of disqualification are not deductible under section 468(a) and paragraph (a) of §1.468A–2T, or, if the fund is disqualified only in part, are deductible only to the extent provided in the notice of disqualification. In addition, if any assets of the fund that are deemed distributed under this paragraph (c)(3) are held by the fund after the date of disqualification (or if additional assets are acquired with nondeductible contributions made to the fund after the date of disqualification), the income earned by such assets after the date of disqualification must be included in the gross income of the electing taxpayer (see section 671) to the extent that such income is otherwise includible under chapter 1 of the Internal Revenue Code. An electing taxpayer can establish a nuclear decommissioning fund to replace a fund that has been disqualified in its entirely only if the Internal Revenue Service specifically consents to the establishment of a replacement fund in connection with the issuance of an initial schedule of ruling amounts for such replacement fund.

(d) *Termination of nuclear decommissioning fund upon substantial completion of decommissioning*—(1) *In general.* Upon substantial completion of the decommissioning of a nuclear power plant to which a nuclear decommissioning fund relates, such nuclear decommissioning fund shall be considered terminated and treated as having distributed all of its assets on the date the termination occurs. Such a distribution shall be treated for purposes of section 1001 as a disposition of property held by the nuclear decommissioning fund (see paragraph (c)(2) of §1.468A–4T). In addition, unless the exception provided in paragraph (d)(2)(iv) of §1.468A–2T applies, the electing taxpayer shall include in gross income for the taxable year in which the termination occurs an amount equal to the fair market value of the assets of the fund determined as of the date of termination. Contributions made to a nuclear decommissioning fund after the termination date are not deductible under section 468A(a) and paragraph (a) of §1.468A–2T. In addition, if any assets are held by the fund after the termination date, the income earned by such assets after the termination date must be included in the gross income of the electing taxpayer (see section 671) to the extent that such income is otherwise includible under chapter 1 of the Internal Revenue Code. Finally, an electing taxpayer using an accrual method of accounting is allowed a deduction for nuclear decommissioning costs that are incurred during any taxable year (see paragraph (e) of §1.468A–2T) even if such costs are incurred after substantial completion of decommissioning (*e.g.*, expenses incurred to monitor or safeguard the plant site).

(2) *Substantial completion of decommissioning defined.* (i) For purposes of this paragraph (d), the substantial completion of the decommissioning of a nuclear power

plant occurs at the time that the maximum acceptable radioactivity levels mandated by the Nuclear Regulatory Commission (or its successor) with respect to a decommissioned nuclear power plant are satisified.

(ii) The Internal Revenue Service may prescribe administrative procedures that clarify the definition of substantial completion of decommissioning to take into account technological change or amendments to the rules issued by the Nuclear Regulatory Commission (or its successor).

§1.468A–6T Disposition of an interest in a nuclear power plant (temporary)

(a) *Treatment of selling taxpayer*—(1) *In general.* In the case of any sale, exchange or other disposition of any portion of a direct ownership interest in a nuclear power plant with respect to which the taxpayer maintains a nuclear decommissionng fund, the portion of the nuclear decommissioning fund that relates to the direct ownership interest sold, exchanged or otherwise disposed of is treated as distributed to the taxpayer on the date of such disposition. (Such a distribution shall be treated for purposes of section 1001 as a disposition of property held by the nuclear decommissioning fund (see paragraph (c)(2) of §1.468A–4T)). In addition, the electing taxpayer must include in gross income for the taxable year in which the disposition of the interest in the nuclear power plant occurs an amount equal to the product of—

(i) The fair market value of the assets of the fund determined as of the date of disposition, reduced by—

(A) The amount of any excess contribution that was not withdrawn before the date of disposition if no deduction was allowed with respect to such excess contribution; and

(B) The amount of any deemed distribution that was not actually distributed before the date of disposition (as determined under paragraph (c)(2)(iii) of §1.468A–2T) if the amount of the deemed distribution was included in the gross income of the electing taxpayer for the taxable year in which the deemed distribution occurred;

and

(ii) The fraction of the taxpayer's direct ownership interest sold, exchanged or otherwise disposed of in such transaction.

Such amount must be included in gross income even if no gain was recognized or realized on the sale, exchange or other disposition of the interest in the nuclear power plant. Thus, for example, such amount must be included in gross income even if the exchange of the interest in the nuclear power plant is described in section 351, 368, 721 or 1031. In addition, if any assets of the fund that are deemed distributed under this paragraph (a)(1) are held by the fund after the date of disposition, the income earned by such assets after the date of disposition must be included in the gross income of the taxpayer (see section 671) to the extent that such income is otherwise includible under chapter 1 of the Internal Revenue Code.

(2) *Revised schedule of ruling amounts required.* If the taxpayer retains a direct ownership interest in the nuclear power plant after the sale, exchange or other disposition of a portion of its former direct ownership interest and does not file a request for a revised schedule of ruling amounts on or before the 90th day after the date of disposition, the ruling amount applicable to the nuclear decommissioning fund to which the nuclear power plant relates for the taxable year in which such disposition occurs and all succeeding taxable years until a new schedule is obtained shall be zero unless, in its discretion, the Internal Revenue Service provides otherwise in such new schedule of ruling amounts.

(b) *Treatment of purchasing taxpayer*—(1) *In general.* (i) A taxpayer that purchases or otherwise acquires a direct ownership interest in a nuclear power plant (a "purchasing taxpayer") from a taxpayer that on the date of acquisition maintains a nuclear decommissioning fund with respect to such nuclear power plant can elect to make a deductible contribution to a nuclear decommissioning fund established by the purchasing taxpayer in an amount not greater than the amount included in the gross income of the selling taxpayer under paragraph (a)(1) of this section. Such contribution must be made (or deemed made under paragraph (c)(1) of §1.468A–2T) during the purchasing taxpayer's taxable year in which the date of acquisition occurs. The amount of any contribution made to a nuclear decommissioning fund pursuant to this paragraph (b)(1)(i) is not taken into account in applying the payment limitation of paragraph (b) of §1.468A–2T and the taxpayer is not required to obtain a ruling amount with respect to such contribution.

(ii) A deductible contribution made by a purchasing taxpayer under paragraph (b)(1)(i) of this section may be made in cash. In addition, for purposes of paragraph (b)(1)(i) of this section only, a purchasing taxpayer may contribute property described in paragraph (a)(3)(i)(C) of §1.468A–5T to a nuclear decommissioning fund established by the purchasing taxpayer if the property—

(A) Was owned by the nuclear decommissioning fund of the selling taxpayer immediately before the sale, exchange or other disposition of an interest in the nuclear power plant;

(B) Was distributed to the selling taxpayer under paragraph (a)(1) of this section; and

(C) Was acquired by the purchasing taxpayer as part of the same transaction in which the interest in the nuclear power plant was acquired.

If the purchasing taxpayer contributes property to a nuclear decommissioning fund under this paragraph (b)(1)(ii), the amount of the contribution (and the basis of the property to the nuclear decommissioning fund) shall equal the fair market value of the property on the date that the property was distributed to the selling taxpayer under paragraph (a)(1) of this section and no gain or loss shall be recognized by the purchasing taxpayer with respect to the transfer of the property to the nuclear decommissioning fund. In addition, no gain or loss shall be recognized by the selling taxpayer with respect to the transfer of such property to the purchasing taxpayer, even if the purchasing taxpayer does not contribute the property to a nuclear decommissioning fund. The nuclear decommissioning fund of the selling taxpayer shall recognize gain or loss on the distribution of such property by the fund (see paragraph (a)(1) of this section). Finally, if the purchasing taxpayer does not contribute the property to a nuclear decommissioning fund under this paragraph (b)(1)(ii), the basis of the property to the purchasing taxpayer shall be the fair market value of the property on the date that the property was distributed to the selling taxpayer under paragraph (a)(1) of this section.

(iii) Except as provided in paragraph (b)(1)(i) of this section, a purchasing taxpayer is allowed a deduction under section 468A(a) for the taxable year in which the taxpayer makes a cash payment (or is deemed to make a cash payment) to a nuclear decommissioning fund only if the taxpayer has received a schedule of ruling amounts for the nuclear decommissioning fund that includes a ruling amount for such taxable year (see §1.468A–3T).

(2) *Manner of making election.* A purchasing taxpayer is allowed a deduction under paragraph (b)(1)(i) of this section only if the Election Statement (as required by §1.468A–7T) for the taxable year in which the acquisition occurs indicates that an election is made under paragraph (b) of §1.468A–6T. In addition, the Election Statement must include—

(i) The name, address and taxpayer identification number of the selling taxpayer;

(ii) The date of the sale, exchange or other disposition;

(iii) The amount included in the gross income of the selling taxpayer under paragraph (a) of this section;

(iv) The amount of the cash payment made (or deemed made) to the nuclear decommissioning fund pursuant to this paragraph (b); and

(v) The fair market value of the property contributed to the nuclear decommissioning fund pursuant to paragraph (b)(1)(ii) of this section determined as of the date that the property was distributed to the selling taxpayer.

§1.468A–7T Manner of and time for making election (temporary)

(a) *In general.* An eligible taxpayer is allowed a deduction for the taxable year in which the taxpayer makes a cash payment (or is deemed to make a cash payment) to a nuclear decommissioning fund only if the taxpayer elects the application of section 468A. A separate election under section 468A is required for each nuclear power plant and for each taxable year with respect to which a deductible cash payment is made to a nuclear decommissioning fund. The election under section 468A for any taxable year is irrevocable and must be made by attaching a statement ("Election Statement") and a copy of the schedule of ruling amounts provided pursuant to the rules of §1.468A–3T to the taxpayer's Federal income tax return for such taxable year. Except as otherwise provided in paragraph (b)(3) of §1.468A–8T, the return to which the Election Statement and a copy of the schedule of ruling amounts is attached must be filed on or before the time perscribed by law (including extensions) for filing the return for the taxable year with respect to which section 468A is to apply.

(b) *Required information.* The Election Statement must include the following information:

(1) The legend "Election Under Section 468A" typed or legibly printed at the top of the first page.

(2) The taxpayer's name, address and taxpayer identification number.

(3) The taxable year for which the election is made.

(4) For each nuclear power plant with respect to which an election is made—

(i) The name and location of the nuclear power plant;

(ii) The name and employer identification number of the nuclear decommissioning fund;

(iii) The total amount of actual cash payments made to the nuclear decommissioning fund during the taxable year that were not treated as deemed cash payments under paragraph (c)(1) of §1.468A–2T for a prior taxable year;

(iv) The total amount of cash payments deemed made to the nuclear decommissioning fund under paragraph (c)(1) of §1.468A–2T for the taxable year; and

(v) The cost of service amount for the taxable year (see paragraph (b)(2) of §1.468A–2T).

§1.468A–8T Effective date and transitional rules (temporary)

(a) *Effective date*—(1) *In general.* Section 468A and §1.468A–1T through §1.468A–8T are effective on July 18, 1984, with respect to taxable years ending on or after such date.

(2) *Cut-off method applicable to electing taxpayers.* Any amount of nuclear decommissioning costs taken into account before July 18, 1984, for a taxable year beginning before such date, is not allowable as a deduction after July 17, 1984, under section 468A(c)(2) and paragraph (e) of §1.468A–2T.

(b) *Transitional rules*—(1) *Time for filing request for schedule of ruling amounts.* If a taxpayer files a request for a schedule of ruling amounts under paragraph (h) of §1.468A–3T on or before July 10, 1987, and the requirement of paragraph (g) of §1.468A–3T is satisfied before the date the request is filed, the limitations contained in paragraph (h)(1)(v) of §1.468A–3T shall not apply with respect to, and the Internal Revenue Service will provide a ruling amount for, any taxable year that ends on or after July 18, 1984, and begins before January 1, 1987.

(2) *Time for making payment to a nuclear decommissioning fund.* The amount of any cash payment to a nuclear decommissioning fund that relates to a taxable year that ends on or after July 18, 1984, and begins before January 1, 1987, shall be deemed made during such taxable year if—

(i) The taxpayer makes such payment on or before the 30th day after the date the taxpayer receives a ruling amount applicable to such taxable year; and

(ii) The taxpayer irrevocably designates the amount of such payment as relating to such taxable year on the Election Statement attached to its Federal income tax return (or amended return) for such taxable year.

(3) *Manner of and time for making election.* A taxpayer can elect the application of section 468A for a taxable year that ends on or after July 18, 1984, and begins before January 1, 1987, by attaching the Election Statement and a copy of the schedule of ruling amounts to an amended return for such taxable year that is filed on or before the 90th day after the date that the taxpayer receives a ruling amount for such taxable year.

(4) *Determination of cost of service limitation.* For purposes of section 468A(b)(1) and paragraph (b)(2) of §1.468A–2T, the cost of service amount applicable to a nuclear decommissioning fund for the taxable year that includes July 18, 1984, is the amount determined under paragraph (b)(2) of §1.468A–2T multiplied by a fraction, the numerator of which is the amount of nuclear decommissioning costs that is directly or indirectly charged to customers in such taxable year and that is included in the taxable income of the taxpayer for such taxable year and the denominator of which is the amount of nuclear decommissioning costs that is directly or indirectly charged to customers in such taxable year and that would have been includible in the gross income of the taxpayer if such amount was taken into account by the taxpayer in the same manner as amounts charged for electric energy (see §1.88–1T). Under the preceding sentence, an amount of decommissioning costs is included in the taxable income of a taxpayer for the taxable year that includes July 18, 1984, if the amount is included in gross income for such taxable year and no deduction (other than a deduction allowed under section 468A(a) and paragraph (a) of

§1.468A–2T) is claimed with respect to such amount for such taxable year.

(5) *Determination of qualifying percentage.* (i) In the case of a nuclear power plant that began commercial operations before July 18, 1984, and whose estimated useful life for ratemaking purposes was adjusted by a public utility commission before July 18, 1984—

(A) If a taxpayer requests a schedule of ruling amounts for such nuclear power plant on or before July 10, 1987, the qualifying percentage equals the percentage of total depreciation costs (determined without regard to capitalized decommissioning costs) with respect to the nuclear power plant that remains to be recovered for ratemaking purposes as of the first day of the taxable year that includes July 18, 1984; or

(B) If a taxpayer does not request a schedule of ruling amounts for such nuclear power plant on or before July 10, 1987, the qualifying percentage equals the percentage of total depreciation costs (determined without regard to capitalized decommissioning costs) with respect to the nuclear power plant that remains to be recovered for ratemaking purposes as of the first day of the first taxable year for which a deductible payment is made to the nuclear decommissioning fund that relates to such nuclear power plant.

(ii) In the case of a nuclear power plant that began commercial operations on or before July 10, 1986 (other than a plant described in paragraph (b)(5)(i) of this section (*i.e.,* a plant that began such operations, and whose estimated useful life was adjusted, before July 18, 1984)), if a taxpayer requests a schedule of ruling amounts for such nuclear power plant on or before July 10, 1987, the estimated period for which the nuclear decommissioning fund to which the nuclear power plant relates is to be in effect for purposes of paragraph (d)(4)(ii) of §1.468A–3T begins on the later of—

(A) The first day of the taxable year that includes the date that the nuclear power plant began commercial operations; or

(B) The first day of the taxable year that includes July 18, 1984.

(6) *Limitation on payments to a nuclear decommissioning fund*—(i) The limitation on payments to a nuclear decommissioning fund (see section 468A(b) and paragraph (b) of §1.468A–2T) for a taxable year that ends on or after July 18, 1984, and begins before January 1, 1987, shall be determined under paragraph (b)(6)(ii) of this section if—

(A) The electing taxpayer receives a ruling amount applicable to such taxable year after the deemed payment deadline date for such taxable year; and

(b) The requirements of paragraph (b)(6)(iii) of this section are satisfied.

(ii) If the limitation on payments to a nuclear decommissioning fund for a taxable year is determined under this paragraph (b)(6)(ii), the maximum amount of cash payments made (or deemed made) to the nuclear decommissioning fund during such taxable year shall not exceed the sum of—

(A) The amount determined under section 468A(b) and paragraph (b) of §1.468A–2T (*i.e.,* the lesser of the cost of service amount or the ruling amount) after application of the transitional rules contained in paragraph (b)(4) and (5) of this section; and

(b) The amount of after-tax earnings that would have accumulated to the date of actual payment to the nuclear decommissioning fund if the amount described in paragraph (b)(6)(ii)(A) of this section had been contributed to the nuclear decommissioning fund on the deemed payment deadline date for such taxable year.

In determining the after-tax earnings that would have accumulated to the date of payment, an electing taxpayer must use the after-tax rate of return of the nuclear decommissioning fund that was used in determining the schedule of ruling amounts.

(iii) In order to compute the payment limitation under paragraph (b)(6)(ii) of this section, an electing taxpayer must—

(A) Indicate on the Election Statement for the taxable year that the amount of the deductible payment is greater than the amount determined under section 468A(b) and paragraph (b) of §1.468A–2T because paragraph (b) (6) of §1.468A–8T applies; and

(b) Not claim any interest under section 6611 with respect to any overpayment of tax that is attributable to a deduction allowed with respect to such payment (see paragraph (b)(7) of this section).

(iv) The following example illustrates the application of the principles of paragraph (b)(6) of this section:

Example. **X corporation is a calendar year, accrual method taxpayer engaged in the sale of electric energy generated by a nuclear power plant owned by X. On September 15, 1986, X receives a schedule of ruling amounts from the Internal Revenue Service that includes a ruling amount of $1,000,000 for the 1985 taxable year. For purposes of this example, assume that the cost of service amount applicable to the nuclear decommissioning fund for the 1985 taxable year is also $1,000,000 and that the after-tax rate of return of the nuclear decommissioning fund that was used in determining the schedule of ruling amounts is 10 percent compounded semi-annually. On September 15, 1986, X makes a contribution of $1,050,000 to a nuclear decommissioning fund established by X. Under paragraph (b)(6)(ii) of this section, this contribution does not exceed the limitation on payments for the 1985 taxable year and the entire amount of the contribution is deductible for such year. The additional $50,000 deductible payment that is allowed under this paragraph (b)(6) reflects the foregone earnings of the fund for the six-month period beginning on the deemed payment deadline date for the 1985 taxable year (March 15, 1986) and ending on the date of the contribution (September 15, 1986).**

(7) *Denial of interest on overpayment.* If a deduction is allowed by reason of paragraph (b)(2) of this section for the amount of any payment made after the 15th day of the third calendar month after the close of the taxable year to which such payment relates, no interest shall be allowed or paid under section 6611 with respect to any overpayment attributable to such deduction for any period before the date the amended return claiming the deduction is filed.

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

(26 CFR Part 62)

Par. 4. The authority citation for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 5. Section 602.101(c) is amended by inserting in the appropriate place in the table

"§1.468A–3T . . . 1545–0954", "§1.468A–4T . . . 1545–0954", "§1.468A–6T . . . 1545–0954", §1.468A–7T . . . 1545–0954", and "§1.468A–8T . . . 1545–0954".

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

Approved June 30, 1986

J. Roger Mentz,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on July 9, 1986, 8:45 a.m., and published in the issue of the Federal Register for July 10, 1986, 51 F.R. 25033)

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term and long-term rates are set forth for the month of August, 1986. See Rev. Rul. 86–94, this page.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of August, 1986. See Rev. Rul. 86–94, this page.

Section 468.—Special Rules for Mining and Solid Waste Reclamation and Closing Costs

Federal short-term, mid-term and long-term rates are set forth for the month of August, 1986. See Rev. Rul. 86–94, this page.

Section 468A.—Special Rules for Nuclear Decommissioning Costs

The elective method for taking into account nuclear decommissioning costs. See T.D. 8094, page 4.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 280G, 467, 468, 7872)

Rev. Rul. 86–94

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of August 1986 are as follows:

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term				
AFR	6.79%	6.68%	6.63%	6.59%
110% AFR	7.49%	7.35%	7.28%	7.24%
120% AFR	8.18%	8.02%	7.94%	7.89%
Mid-Term				
AFR	7.44%	7.31%	7.24%	7.20%
110% AFR	8.20%	8.04%	7.96%	7.91%
120% AFR	8.96%	8.77%	8.68%	8.61%
Long-Term				
AFR	7.51%	7.37%	7.30%	7.26%
110% AFR	8.27%	8.11%	8.03%	7.96%
120% AFR	9.04%	8.84%	8.74%	8.68%

As described in Rev. Rul. 86–17, 1986–6 I.R.B. 26, for purposes of section 7872(e)(2) of the Code, the "blended annual rate" for 1986 is 7.77 percent.

Section 4051.—Imposition of Tax on Heavy Trucks and Trailers Sold at Retail

Whether a cost comparison formula may be used to determine the amount of the tire exclusion for purposes of computing the taxable sale price of a highway vehicle under section 4052(b)(1)(B)(iii) of the Code. See. Rev. Rul. 86–93, this page.

Section 4052.—Definitions and Special Rules

26 CFR 145.4052–1: Special rules and definitions.
(Also Section 4051.)

Sale price of truck; tire exclusion; use of cost comparison formula. For purposes of computing the taxable sale price of a highway vehicle under section 4052(b) of the Code, a cost comparison formula may be used to determine the amount that may be excluded as the fair market value at retail of the tires.

Rev. Rul. 86–93

ISSUE

For purposes of the retailers excise tax on heavy trucks and trailers imposed by section 4051(a) of the Internal Revenue Code, may a dealer, in computing taxable sale price, exclude as the fair market value at retail of the tires an amount determined under a cost comparison formula?

FACTS

X, a vehicle dealer, sells at retail trucks and truck trailers that are subject to the tax imposed by section 4051(a)(1) of the Code. *X* mounts on some of these vehicles tires purchased from tire manufacturers *Y* and *Z*. *X* does not ordinarily make separate sales of *Y* or *Z* tires. In accordance with Federal Trade Commission (FTC) rules under 16 C.F.R. section 228.16 (1985), pertaining to the advertising of tire warranties, *Y* publishes a predetermined price list that reflects the average selling price for which its dealers sell *Y* tires. *Z* does not publish a predetermined price list under the FTC rules, and neither *Y* nor *Z* publishes manufacturers suggested retail price lists.

LAW AND ANALYSIS

Section 4051(a)(1) of the Code imposes on the first retail sale of certain truck and trailer chassis and bodies (including in each case parts or accessories sold on or in connection therewith or with the sale thereof) a tax of 12 percent of the amount for which the article is so sold.

Section 4052(b)(1)(B)(iii) of the Code provides that in determining the price for which an article is sold, there shall be excluded the fair market value (including any tax imposed by section 4071) at retail of any tires (not including any metal rim or rim base).

Section 145.4052–1(d)(2)(iii) of the Temporary Excise Tax Regulations, as amended by T.D. 8050, 50 Fed. Reg. 37350, 37351 (1985), provides that the fair market value at retail of tires shall be determined by the lowest established price for which the vehicle retailer would sell such tires at retail in the ordinary course of trade. The lowest established price is the lowest price for which the vehicle retailer sells, or offers to sell, a single tire to an independent purchaser who would not ordinarily be expected to buy more than one. If the vehicle retailer has no lowest established price, the Commissioner will accept any price, provided that, under the facts and circumstances, such price is not unreasonable. For vehicles sold on or after April 1, 1983, and before October 15, 1985, a price will not be considered unreasonable if it is no more than an amount equal to 50 percent of the manufacturer's suggested retail price.

X does not ordinarily make separate sales of *Y* or *Z* tires and thus does not have, within the meaning of section 145.4052–1(d)(2)(iii) of the temporary regulations, a lowest established price for which it sells, or offers to sell, such tires to independent purchasers. In the case of *X*'s sale of *Y* tires mounted on *X*'s trucks, the Commissioner will accept as the fair market value at retail of the tires *Y*'s predetermined price as computed under 16 C.F.R. section 228.16(b)(3). *See* Rev. Rul. 86–28, 1986–8 I.R.B. 22.

In those instances in which *X* purchases competitive tires of a comparable size from manufacturers *Y* and *Z* and only *Y* publishes a predetermined price list, *X* may use the amount determined under the following formula as the fair market value at retail (FMV) of *Z* tires:

$$\text{FMV } Z = \frac{\text{Cost } Z \times \text{FMV } Y}{\text{Cost } Y}$$

This formula is based on the assumption that the percentage mark-up from cost to fair market value is the same for both the *Y* and the *Z* tires. In other words, the ratio that the actual cost to *X* of a *Z* tire bears to the actual cost to *X* of a comparable *Y* tire is assumed to be the same as the ratio that the fair market value at retail of a *Z* tire bears to the fair market value at retail (predetermined price under 16 C.F.R. section 228.16(b)(3)) of a *Y* tire. For example, if the actual cost to *X* of a *Y* tire is $300, the actual cost to *X* of a *Z* tire is $280, and the fair market value at retail of a *Y* tire is $320, the fair market value of a *Z* tire can be determined to be $298.67, as seen below.

$$\text{FMV } Z = \frac{\$280 \times \$320}{\$300} = \$298.67$$

HOLDING

For purposes of determining the taxable sale price of a highway vehicle under section 4052(b) of the Code, *X* may exclude an amount for the fair market value at retail of the tires as determined under the cost comparison formula set forth above.

Section 7872.—Treatment of Loans with Below-market Interest Rates

The "blended annual rate" is set forth for 1986. See Rev. Rul. 86–94, page 20.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Special Rules Relating to Nuclear Decommissioning costs

LR–18–85

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary regulations that provide special rules relating to nuclear decommissioning costs. The text of the temporary regulations also serves as the comment document for this notice of proposed rulemaking.

DATES: Written comments and requests for a public hearing must be delivered or mailed by SEPTEMBER 8, 1986. The regulations are proposed to take effect on July 18, 1984, and to apply with respect to taxable years ending on or after such date.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR–18–85), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: C. Scott McLeod of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washintgon, D.C. 20224 (Attention: CC:LR:T), (202) 566-3288 (not a toll-free call).

SUPPLEMENTARY INFORMATION

BACKGROUND

The temporary regulations (designated by a "T" following the section citation) in the Rules and Regulations section of this issue of the FEDERAL REGISTER amend Parts 1 and 602 of Title 26 of the Code of Federal Regulations to provide rules relating to sections 88 and 468A of the Internal Revenue Code of 1954, as added by subsections 91 (c) and (f) of the Tax Reform Act of 1984 (Pub. L. 98–369, 98 Stat. 604, 607). This document proposes to adopt those temporary regulations as final regulations; accordingly, the text of the temporary regulations serves as the comment document for this notice of proposed rulemaking. In addition, the preamble to the temporary regulations provides a discussion of the proposed and temporary rules.

For the text of the temporary regulations, see * * * [T.D. 8094, page 4, this bulletin].

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required. Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before these proposed regulations are adopted, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504 (h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitteing comments on these requirements to OMB also send copies of those comments to the Service.

DRAFTING INFORMATION

The principal author of these proposed regulations is C. Scott McLeod of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

LIST OF SUBJECTS IN 26 CFR 1.61–1 through 1.281–4

Income taxes, Taxable income, Deductions, Exemptions.

LIST OF SUBJECTS IN 26 CFR 1.441–1 through 1.483–2

Income taxes, Accounting, Deferred compensation plans.

LIST OF SUBJECTS IN 26 CFR 602

Reporting and recordkeeping requirements.

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on July 9, 1986, 8:45 a.m., and published in the issue of the Federal Register for July 10, 1986, 51 F.R. 25070)

Foundations Status of Certain Organizations

Announcement 86–90

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

A Better You, Duluth, MN
Acument Inc., Chicago, IL
Ad Hoc Singers Inc., Columbia, MO
Adult Abuse Community Serivce Inc., Grand Forks, ND
Advocacy Office for Children and Youth, Inc., Omaha, NE

African Aid, Inc., Mitchell, SD
Agape Word Fellowship, Smithville, MD
AGC of Greater Milwaukee Education & Research Foundation, Inc., Milwaukee, WI
Age In Action, Newark, NJ
Al Raham Community Restoration Corp., Philadelphia, PA
Alternative Work Site Inc., Omaha, NE
Apple Foundation for Quality Education, Crystal Lake, IL
Arrowhead Regional Arts Council, Duluth, MN
Artemis of Duluth, Duluth, MN
Association for Retarded Citizens of Franklin & Williamson, Energy, IL
Association of Corporate Art Curators, Chicago, IL
Bethlehem Center, Carol Stream, IL
Birthright of Pottstown, Pottstown, PA
Black Missionary Foundation, Normal, IL
Break Through Inc., Minneapolis, MN
Breakaway, Inc., Minneapolis, MN
Bridge Educational Fund, Eugene, OR
Bureau of Indo Pacific Economic Development, Inc., Chicago, IL
C I B C Foundation, Media, PA
C.K.S. Enterprises Inc., St. Louis, MO
Cache Handicap Action Council, Logan, UT
Cambodian Association of Wisconsin, Inc., Madison, WI
C/Born, Omaha, NE
Center for Christian Information, Robbinsdale, MN
Center for Contextual Family Therapy, Inc., King of Prussia, PA
Central California Chinese Culture Center, Inc., Fresno, CA
Central California Forum on Refugee Affairs, Fresno, CA
Central Coast Nursing Cooperative Council, San Luis Obispo, CA
Central Ward Coalition of Youth Agencies, Inc., The, Newark, NJ
Central Wisconsin Special Education Resources, Inc., Wausau, WI
Chicago Early Music Consort Inc., Morton Grove, IL
Chicago North Wholistic Health Center, Inc., Chicago, IL
Chicago Swing Society, Northbrook, IL
Child Advocacy Network, Philadelphia, PA
Childbirth Education Assoc. of Neenah-Menasha, Inc., Neenah, WI
Childrens Help in Living Daily Limited, Edwards, MO
Children's Movement, The, Klamath Falls, OR
Chinese-American Culture Center, Sacramento, CA
Choral Arts Ensemble of Kansas City, Kansas City, MO
Chore Corps Minneapolis, Minneapolis, MN
Christian Church of Universal Philosophy, Seattle, WA
Christian County Manor, Inc., Ozark, MO
Christian Outreach Association, Reno, NV
Christians for Life Society, St. Louis, MO
Citizen Technical Development, Fremont, NE
Citizens for Clear Conscience Giving, St. Joseph, MO
City Square Association, Inc., Fort Dodge, IA
Coalition for Social Justice, Marshalltown, IA
Commercial Street Historical Society Corp., Springfield, MO
Committee Against Domestic Abuse, Chicago, IL
Community Reform Resource Network, Inc., Mankato, MN
Contemporary Theater Experiences for Youth, Chicago, IL
Continuum Minnesota, Inc., Minneapolis, MN
Cottonwood Rivers Arts Council, Inc., New Ulm, MN
Covrin Ballet, Inc., The, Lambertville, NJ
Creative Arts & Expression Laboratory, Olivette, MO
Crossing A Mountain With Stepping Stone, Inc., Saddlebrook, NJ
Dahcotah Institute of Development Economics, Sioux Falls, SD
Dr. James W. Sinder Scholarship Fund, Kennett Square, PA
Elgin Area Arts Council, Elgin, IL
Epilepsy Federation Auxiliary Inc., St. Louis, MO
Eppic, Camarillo, CA
Faith Life Ministries, Jamestown, ND
Family Abuse Care Treatment Shelter, Inc., Superior, WI
Fire and Rain, Chicago, IL
First State Fine Art Committee, Delaware Division of Libraries, Dover, DE
Forham Productions, Inc., Chicago, IL
Foundation for The Advancment of World Peace, Florham Park, NJ
Foundation for The Development of Health Care Management, West Chester, PA
Free Lao Neutralist Front Assoc., of USA FLNFA-USA, Minneapolis, MN
Friendship Force of Greater Des Moines, Inc., The, Des Moines, IA
George Pasero Scholarship Fund, Inc., Portland, OR
Golden Age Foundation Inc., Kansas City, MO
Goods in Abundance of Alaska, Inc., Anchorage, AK
Grandma Letters, Evanston, IL
Great Plains Railroad and Great Plains Museum, The, Omaha, NE
Greater Pontiac Area Consortium Private Industry Council, Inc., Pontiac, MI
Greater Tri-City Lions Sight and Hearing Conservation Trust, Richland, WA
Guatemalan Childrens Fund, Naperville, IL
H.A.R.C. (Haitian American Resource Center), Newark, NJ
Heartland Christian Broadcasters, Inc., Brainerd, MN
Henry Morgan Brown Charitable Fund Inc., Columbia, MO
Henry Primakoff Lectureship Trust, Department of Mayaics, Philadelphia, PA
Hidden Hollow Association, Hegin, PA
Hispanic Parent Advisory Council of Madison, Inc., Madison, WI
Historical Review Committee Inc., The, Columbus, NE
Holy Light & Martin Luther King Out-Reach, Inc., Milwaukee, WI
Humane Society of Illinois, Chicago, IL
Illinois Head Injury Assn., Peoria, IL
Illinois Welfare Rights Coalition Inc., Chicago, IL
Innergrowth Inc., Osseo, MN
Institute for the Research and Development of Holistic Designs, The, Evanston, IL
International Childrens Benefit Fund, Chicago, IL
Iowa Museum Association, Inc., Des Moines, IA
Iowa Network of Community Youth Services, Des Moines, IA
Jake Gittlen Memorial Golf Tournament, Harrisburg, PA
Jim Mugg Global Outreach, Springfield, MO
Judaeo Christian Ministries, Chicago, IL
Kate Kuper Inc., Chicago, IL
Keystone Ceramic Association, Hegins, PA
LCL of Wisconsin, Madison, WI
Laclede County Assoc. for Retarded Citizens, Lebanon, MO
Lane County Clients Council, Eugene, OR
League for Religious Services Inc., St. Louis, MO
Lee Epstein Institute, The, Chicago, IL
Lehigh Valley Lesbian and Gay Community Center, Allentown, PA

Love Unlimited, Decatur, IL
Maclaurin Institute for Inter-disciplinary Studies, St. Paul, MN
Marcom, Inc., Richmond, MO
Maries County Manor, Inc., Vienna, MD
Martin Luther King Broadcasting, Rock Island, IL
McLeod County Arts, Inc., Hutchinson, MN
Med-Ship Inc., Bakersfield, CA
Mens Place Men Working Together to End Violence Against Women, Inc., Madison, WI
Mesabi Family Center, Inc., Virginia, MN
Miami Valley Research Institute, Dayton, OH
Mid-States Ceta Directors Assn., Springfield, MO
Milwaukee Jazz Alliance, Milwaukee, WI
Minnesota Creative Arts Team, Inc., Minneapolis, MN
Missouri State Old Time Fiddlers Assn., Columbia, MO
Montana Intercountry Adoption, Inc., Bozeman, MT
Multiple Sclerosis Service Organization, Sayreville, NJ
Nhhi-Blooming Barrier Free Housing Corp., Minneapolis, MN
National Institute for Adolescent Pregnancy Services, Wilmington, DE
Nebraska Military History Club, Grand Island, NE
Neenah Menasha Dental Clinic, Neenah, WI
Neighborhood Family Services and Community Center, Inc., Philadelphia, PA
Neurological & Psychiatric Research & Treatment Foundation, Skokie, IL
New Berlin Parents for Expanded Education, New Berlin, WI
New Blind Parrot Productions, Chicago, IL
New Cinema Cooperative, Omaha, NE
New Connection, The, Jamestown, ND
New Horizons Ministry, Inc., Princeton, MN
New Olympic Dance Team, Minneapolis, MN
New Zoo Foundation, Chicago, IL
Newark Tim Still Memorial Foundation, Newark, NJ
Northeast Nebraska Council on Alcoholism and Drug Abuse, Pilger, NE
Northern Forest Industry Institute, Inc., Green Bay, WI
Northern Minnesota Area Assembly, Moorehead, MN
Northwest Institute for Architecture and Urban Studies in Italy, Seattle, WA
Northwoods Players Ltd., Park Falls, WI
Nottingham Recreation Center for the Physically Limited, The, Trenton, NJ
Nova Dance Company, Burnsville, MN
Oak Forest Soccer Boosters Club, Oak Forest, IL
One Fourth, Inc., Chicago, IL
Open Circle Theatre Co., Chicago, IL
Opera Ensemble of Portland, Portland, OR
Operation Sunshine for the Aged, Davenport, IA
Opus Association, Racine, WI
Our Youth of Today, Inc., Milwaukee, WI
Owl Creek Foundation, Inc., Missoula, MT
Ozarks Veterans Community Center, Inc., Springfield, MO
PKU Organization of Illinois, Chicago, IL
Paid In Full Ministries, Phoenixville, PA
Paper City Homes, Inc., Mosinee, WI
Penn Valley Park Fitness Trail Association Inc., Kansas City, MO
Performing America Inc., Chicago, IL
Philadelphia Child Abuse/Neglect Resource Center, Inc., Philadelphia, PA
Prairie Foundation for Alternative Energy Studies, Champaign, IL
Project Charlie III Richfield, Inc., Richfield, MN
Propaganda Research Institute, Chicago, IL
Protestant Committee on Urban Ministry Inc., Minneapolis, MN
Public Access Theatre, Inc., Chicago, IL
Public Affairs Media Center, DNC., The, Madison, WI
R.O.W. Inc., Weehawken, NJ
Racine Local Economic Development Inc., Racine, WI
Rape-Sexual/Assault Intervention Program, Dubuque, IA
Rebuild Resources Inc., Minneapolis, MN
Rock Island County Area Product Inc., Rock Island, IL
Royal Shake-Speare Revels, Ojai, CA
SBD Corporation, Minneapolis, MN
St. Louis Association for the Performing Arts, Inc., St. Louis, MO
St. Louis Ballet Company, The, Clayton, MO
St. Louis Ensemble, St. Louis, MO
St. Louis Neighborhood Resource Center, Inc., St. Louis, MO
Saints Alive Inc., Independence, MO
Save the Brockhouse Animal Collection A Not for Profit South, Sioux Falls, SD
Sence Saving Established Neighborhood by Community, St. Paul, MN
Senti-Jensen Evangelical Assn., Bismark, ND
Shalya Foundation, Inc., St. Louis Park, MN
Share and Care Foundation for India, Ramsey, NJ
Shaw Community Corp., St. Louis, MO
Shekinah Mountain Minstry, Inc., Crystal, MN
Signs of Life, Inc., Appleton, WI
Siouxland Ice Arena, Assn., Sioux City, IA
Smiksmak Theatre, Minneapolis, MN
Social Development Associates, Inc., Vadnais Heights, MN
Social Effects Liberating Families, Chicago, IL
Socialization Recreation Athletics for Disabled Youth, Inc., Yeadon, PA
Sojourners, Inc., The, Loyal, WI
Solaris Two Theatre Productions Inc., Madison, WI
Solid Rock Ministries, Mason City, IA
Someplace Else, Inc., Clearbrook, MN
Sonoma County Friends of the Blind, Santa Rosa, CA
Southeastern Wisconsin Center for Independent Living, Inc., Milwaukee, WI
Southside Child Care Committee Inc., Minneapolis, MN
Space Place Private Club, Chicago, IL
Spectalce, Inc., Chicago, IL
Spindrift Inc., Schaumburg, IL
Spiritus Inc., St. Louis, MO
Spring Creek Farm for Youths, Inc., Doniphan, MO
Stained Glass Players, Springfield, MO
Study of Kenneth and Ellis Lewis Plantation, Inc., Kenneth Square, PA
Sue West Dancers, Inc., Billings, MT
Susquehanna Society for Therapy and Rehabilitation through Horticulture, Kingsley, PA
Theatre Development Team, The, Rush City, MN
Tim Davidson Ministries Inc., Bismarck, ND
Transition Integration Corp., Eau Claire, WI
Twin City Youth Alliance Inc., Minneapolis, MN
U-HELP Mothers of Sorrow, Philadelphia, PA
United Cursillo Community of Minnesota, Minneapolis, MN
United Legal Foundation, Chicago, IL
Vietnamese Voluntary Foundation, Inc., Santa Clara, CA
Walker Point House, Inc., Milwaukee, WI
Watsontown Area Senior Citizens Housing Corp., Watsontown, PA

Waukesha County Christmas Clearing Council Inc., Waukesha, WI

Wausau Area Youth Unlimited, Wausau, WI

Wellington Historical Society, Chicago, IL

Wescope Research Corp., Waterloo, IA

West of Broad Street Coalition, Philadelphia, PA

Western Southern Dakota Family & Child Dev. Program, Rapid City, SD

Will County Parents Anonymous, Bolingbrook, IL

Wisconsin Directors of Religious Education Federation, Inc., Greendale, WI

Young Peoples Workshop, Fort Madison, IA

Youth for Patriotism, Inc., Minneapolis, MN

XMas-365 Foundation, Inc., Jeffersonville, IN

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Average Area Purchase Price Safe Harbor Limitations

Announcement 86–81

Issuers of mortgage subsidy bonds may continue to rely on the "average area purchase price" safe harbor limitations contained in Rev. Proc. 85–42, 1985–2 C.B. 496, until new safe harbor limitations are published.

Section 103(a) of the Internal Revenue Code provides that gross income does not include interest on (1) the obligations of a state or its political subdivisions, and (2) qualified scholarship funding bonds. Section 103A(a) provides, with certain exceptions, that any mortgage subsidy bond will be treated as an obligation not described in section 103(a)(1) or (2). Thus, the interest on mortgage subsidy bonds ordinarily is not excluded from gross income by section 103(a). A mortgage subsidy bond is an obligation that is issued as part of an issue a significant portion of the proceeds of which is to be used to provide mortgages on owner-occupied residences. However, under section 103A(b)(2)(A), a "qualified mortgage bond" will not be treated as a mortgage subsidy bond, and the interest on qualified mortgage bonds will be excluded from gross income.

In order to qualify as a qualified mortgage bond, certain requirements must be satisfied. One requirement is that the acquistion cost of each residence to be financed with the proceeds of qualified mortgage bonds may not exceed a certain percentage of the average area purchase price for the residence. The average area purchase price is the average purchase price of single-family residences (in the statistical area in which the residence is located) that were purchased during the most recent 12-month period for which sufficient statistical information is available. Under section 6a.103A-2(g)(6)(iii) of the Temporary Income Tax Regulations, for purposes of meeting the average area purchase price requirement, an issuer may rely on the average area purchase price safe harbor limitations published by the Department of the Treasury for the statistical area in which the residence is located. The safe harbor limitations are effective during the period stated at the time of publication. An issuer may use a limitation different from the published safe harbor limitations if the issuer has more accurate and comprehensive data.

Rev. Proc. 85–42 stated that the list of safe harbor limitations published in that procedure could be relied on for the period beginning August 2, 1985, and ending August 1, 1986. The Internal Revenue Service will release new safe harbor limitations to replace those listed in Rev. Proc. 85–42 as soon as new statistical information is available. After August 1, 1986, issuers of mortgage subsidy bonds may rely on the safe harbor limitations in Rev. Proc. 85–42, until new safe harbor limitations are published.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Tevor Adel	**Silver Springs, MD**	**Certified Public Accountant**	**Indefinite from June 2, 1986**
John H. Peimann	**Ottawa, KS**	**Certified Public Accountant**	**Twenty-One Months from June 1, 1986**
John D. Raikos	**Indianapolis, IN**	**Attorney**	**Indefinite from May 20, 1986**
Vernon Rubel	**Hickory, NC**	**Enrolled Agent**	**Indefinite from May 28, 1986**
Wayne Boyer	**Southfield, MI**	**Enrolled Agent**	**Eight Months from May 12, 1986**
Thomas McPhee	**McAllen, TX**	**Enrolled Agent**	**Indefinite from June 15, 1986**
Glen R. Verber	**Houston, TX**	**Certified Public Accountant**	**Ninety Days from May 19, 1986**
Beverly Worth	**Winona Lake, IN**	**Enrolled Agent**	**Five Years from June 17, 1986**

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor.
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federral Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

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86–88, 1986–30 I.R.B. *16*
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Treasury Decisions:

8089, 1986–28 I.R.B. *4*
8090, 1986–27 I.R.B. *5*
8091, 1986–28 I.R.B. *14*

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[1] **A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.**

Finding List of Current Action on Previously Published Rulings[1]

Bulletins 1986–27 through 1986–30

***Denotes entry since last publication**

Revenue Rulings:

68–356
Modified by
86–89, 1986–28 I.R.B. 4

85–18
Clarified by
86–91, 1986–30 I.R.B. 5*

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

NOTES

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CUMULATIVE BULLETINS

The contents of the weekly Bulletin are consolidated semiannually into a permanent, indexed, Cumulative Bulletin. These are sold on a single copy basis and *are not* included as part of the subscription to the Internal Revenue Bulletin. Subscribers to the weekly Bulletin are notified when copies of the Cumulative Bulletin are available. Certain issues of Cumulative Bulletins are out of print and are not available. Persons desiring available Cumulative Bulletins, which are listed on the reverse, may purchase them from the Superintendent of Documents.

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August 11, 1986

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Announcement 86-92, page 46.
The application of the proposed original issue discount regulations to debt instruments with payments denominated in foreign currency is clarified.

EXEMPT ORGANIZATIONS

Rev. Rul. 86-95, page 4.
Exemption; public forums; congressional candidates. The conduct of public forums involving qualified congressional candidates in the manner described, by an organization otherwise exempt under section 501(c)(3) of the Code, will not constitute participation or intervention in any political campaign within the meaning of section 501(c)(3). Rev. Rul. 66-256 amplified.

EXCISE TAXES

Rev. Rul. 86-96, page 5.
Coal; effect of moisture content on tonnage determination. The Service will allow a calculated reduction of the taxable weight of coal for the weight of excess moisture. Rev. Rul. 82-222 modified.

ADMINISTRATION

Rev. Proc. 86-32, page 6.
Information returns; magnetic media reporting. Requirements and conditions for filing information return Forms 1098, 1099, 5498, and W-2G on 5¼ inch magnetic diskette are set forth.

Finding Lists begin on page 49.
Announcement of Disbarments and Suspensions on page 47.
Announcement of Notice of Proposed Rulemaking on page 48.

Department of the Treasury
Internal Revenue Service

T 22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 501.—Exemption from Tax on Corporations, Certain Trusts, Etc.

26 CFR 1.501(c)(3)–1: Organizations organized and operated for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals.

Exemption; public forums; congressional candidates. The conduct of public forums involving qualified congressional candidates in the manner described, by an organization otherwise exempt under section 501(c)(3) of the Code, will not constitute participation or intervention in any political campaign within the meaning of section 501(c)(3). Rev. Rul. 66–256 amplified.

Rev. Rul. 86–95

ISSUE

Would the conduct of public forums involving qualified congressional candidates by an organization otherwise described in section 501(c)(3) of the Internal Revenue Code, in the manner described below, constitute participation or intervention in any political campaign within the meaning of section 501(c)(3)?

FACTS

The organization is an educational membership organization exempt from federal income tax under section 501(c)(3) of the Code. As one of its programs, the organization monitors and reports on legislative, judicial, administrative, and other governmental activities and developments considered to be of important interest to its members.

The organization proposes to conduct a series of public forums. These forums will be conducted in congressional districts during congressional election campaigns. All legally qualified candidates for the House of Representatives from the congressional districts in question will be invited to participate in a forum.

The agenda at each of the forums will cover a broad range of issues, including, but not limited to, those issues considered to be of important educational interest to the organization's members. Questions to forum participants will be prepared and presented by a nonpartisan, independent panel of knowledgeable persons composed of representatives of the media, educational organizations, community leaders, and other interested persons. Each candidate will be allowed an equal opportunity to present his or her views on each of the issues discussed. The organization will select a moderator for each forum whose sole function will be limited to assuring that the general ground rules are followed. At both the beginning and end of each forum, the moderator will state that the views expressed are those of the candidates and not those of the organization and that the sponsorship of the forum is not intended as an endorsement of any candidate.

LAW AND ANALYSIS

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable or educational purposes, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting to influence legislation, (except as otherwise provided in section 501(h)), and which do not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

Section 1.501(c)(3)–1(c)(3)(i) of the Income Tax Regulations states that an organization is not operated exclusively for one or more exempt purposes if it is an "action" organization. Section 1.501(c)(3)–1(c)(3)(iii) defines an "action" organization as an organization that participates or intervenes, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office. The regulations further provide that activities that constitute participation or intervention in a political campaign on behalf of or in opposition to a candidate include, but are not limited to, the publication or distribution of written statements or the making of oral statements on behalf of or in opposition to such a candidate.

Rev. Rul. 66–256, 1966–2 C.B. 210, holds that a nonprofit organization formed to conduct public forums at which lectures and debates on social, political, and international matters are presented qualifies for exemption from federal income tax under section 501(c)(3) of the Code.

Rev. Rul. 74–574, 1974–2 C.B. 160, holds that a section 501(c)(3) organization operating a broadcast station is not participating in political campaigns on behalf of public candidates by providing reasonable amounts of air time equally available to all legally qualified candidates for election to public office in compliance with the reasonable access provisions of the Communications Act of 1934, 47 U.S.C. §312(a)(7), (1982).

Whether an organization is participating or intervening, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office depends upon all of the facts and circumstances of each case. For example, certain "voter education" activities conducted in a non-partisan manner may not constitute prohibited political activities under section 501(c)(3) of the Code. Other so-called "voter education" activities may be proscribed by the statute. Rev. Rul. 78–248, 1978–1 C.B. 154, contrasts several situations illustrating when an organization that publishes a compilation of a candidate's position or voting record has or has not engaged in prohibited political activities based on whether the questionnaire or voting guide in content or structure shows a bias or preference with respect to the views of a particular candidate. See also Rev. Rul. 80–282, 1980–2 C.B. 178, that amplified Rev. Rul. 78–248 regarding the timing and distribution of voter education materials.

The presentation of public forums or debates is a recognized method of educating the public. See Rev. Rul. 66–256. Providing a forum for candidates is not, in and of itself, prohibited political activity. See Rev. Rul. 74–574. However, a forum for candidates could be operated in a manner that would show a bias or preference for or against a particular candidate. This could be done, for example, through biased questioning procedures. On the other hand, a forum held for the purpose of educating and informing the voters, which provides fair and impartial treatment of candidates, and which does not promote or advance one candidate over another, would not constitute participation or intervention in any political campaign on behalf of or in opposition to any candidate for public office.

The facts and circumstances of this case establish that both the format and content of the proposed forums will be presented in a neutral manner. All legally qualified congressional candidates will be invited to participate in the forum. The questions will be prepared and presented by a nonpartisan, independent panel. The topics discussed will cover a broad range of issues of interest to the public, notwithstanding that the issues discussed may include issues of particular importance to the organization's members. Each candidate will receive an equal opportunity to present his or her views on each of the issues discussed. Finally, the moderator selected by the organization will not comment on the questions or otherwise make comments that imply approval or disapproval of any of the candidates. In view of these facts, the organization will not be considered to be engaged in prohibited political activity.

This conclusion is based on the totality of the circumstances described. The presence or absence of a particular fact here in other similar situations is not determinative of other cases but would have to be considered in light of all the surrounding factors in that case.

HOLDING

The conduct of public forums involving qualified congressional candidates in the manner described above, by an organization otherwise described in section 501(c)(3) of the Code, will not constitute participation or intervention in any political campaign within the meaning of section 501(c)(3).

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 66-256 is amplified.

Section 4121.—Imposition of Tax

26 CFR 48.4121-1: Imposition and rate of tax on coal.

Coal; effect of moisture content on tonnage determination. The Service will allow a calculated reduction of the taxable weight of coal for the weight of excess moisture. Rev. Rul. 82-222 modified.

Rev. Rul. 86-96

Rev. Rul. 82-222, 1982-2 C.B. 295, holds that the federal excise tax imposed by section 4121 of the Internal Revenue Code on a producer's sale of coal applies to the full amount of coal sold by the producer. This amount was to be determined at the point of sale with no reduction for moisture content.

In *A.J. Taft Coal Co. v U.S.*, 605 F. Supp. 366 (N.D. Ala. 1984), *aff'd without opinion*, 760 F.2d 280 (11th Cir. 1985), the court held that, for purposes of section 4121 of the Code, the term "coal" does not include water that is in excess of the coal's inherent moisture content and that is reasonably measurable.

For purposes of the tax imposed by section 4121 of the Code, the Internal Revenue Service will follow the *Taft Coal Co.* decision regarding the moisture content of coal. The Service will allow a calculated reduction of the taxable weight of coal for the weight of excess moisture, but only where the taxpayer can demonstrate through competent evidence that there is a reasonable basis for its determination of the existence, and amount, of excess moisture.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 82-222 is modified.

26 CFR 601.602: Forms and instructions.

Rev. Proc. 86–32

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NOTE: THIS REVENUE PROCEDURE MAY ONLY BE USED TO PREPARE 5¼ INCH MAGNETIC DISKETTE SUBMISSIONS FOR TAX YEAR 1986 RETURNS. UPDATED COPIES ARE PUBLISHED EACH YEAR. PLEASE READ THIS PUBLICATION CAREFULLY. **PERSONS REQUIRED TO FILE MAY BE SUBJECT TO PENALTIES FOR FAILURE TO FOLLOW THE INSTRUCTIONS IN THIS REVENUE PROCEDURE.** THESE INCLUDE PENALTIES OF $50 PER DOCUMENT FOR EACH DOCUMENT SUBMITTED WITHOUT A TAXPAYER IDENTIFICATION NUMBER (TIN) OR WITH AN INCORRECT TIN. YOU MAY ALSO BE SUBJECT TO AN ADDITIONAL $50 PENALTY PER DOCUMENT FOR EACH DOCUMENT NOT SUBMITTED ON MAGNETIC MEDIA IF YOU ARE REQUIRED TO FILE THIS WAY OR IF YOU FILE LATE. THE MAXIMUM PENALTY IS $50,000 (THERE IS NO MAXIMUM FOR CERTAIN FORMS 1099–INT, 1099–DIV, 1099–OID, 1099–PATR, 5498 OR IF THE FAILURE TO FILE IS DUE TO INTENTIONAL DISREGARD OF THE FILING REQUIREMENTS). IRS STRONGLY ENCOURAGES FILERS TO REVIEW THEIR DATA FOR ACCURACY BEFORE SUBMISSION TO PREVENT ERRONEOUS NOTICES TO PERSONS FOR WHOM REPORTS ARE FILED.

PART A.—GENERAL

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to provide the requirements and conditions for filing information return Forms 1098, 1099, 5498, and W–2G on 5¼ inch magnetic diskette. Other revenue procedures provide instructions for filing on magnetic tape, 8 inch magnetic diskette, and cassette or mini-disk. **THIS REVENUE PROCEDURE IS TO BE USED FOR THE PREPARATION OF TAX YEAR 1986 INFORMATION RETURNS ONLY.** THIS PROCEDURE IS UPDATED YEARLY TO REFLECT NECESSARY CHANGES. PLEASE READ THIS PUBLICATION CAREFULLY. Specifications for filing the following forms are contained in this procedure:

(a) Form 1098, Mortgage Interest Statement.

(b) Form 1099–A, Information Return for Acquisition or Abandonment of Secured Property.

(c) Form 1099–B, Statement for Recipients of Proceeds from Broker and Barter Exchange Transactions.

(d) Form 1099–DIV, Statement for Recipients of Dividends and Distributions.

(e) Form 1099–G, Statement for Recipients of Certain Government Payments.

(f) Form 1099–INT, Statement for Recipients of Interest Income.

(g) Form 1099–MISC, Statement for Recipients of Miscellaneous Income.

(h) Form 1099–OID, Statement for Recipients of Original Issue Discount.

(i) Form 1099–PATR, Statement for Recipients (Patrons) of Taxable Distributions Received From Cooperatives.

(j) Form 1099–R, Statement for Recipients of Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc.

(k) Form 5498, Individual Retirement Arrangement Information.

(l) Form W–2G, Statement for Recipients of Certain Gambling Winnings.

Specifications for filing Forms 1042S, 6248, 8027, W–2 and W–2P are contained in separate publications.

.02 Section 1.6045–1(1) of the Income Tax Regulations requires brokers and barter exchanges to use magnetic media to report **ALL** Form 1099–B data to IRS. **THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS.** Section 6011(e) of the Internal Revenue Code as amended by the Interest and Dividend Tax Compliance Act of 1983, Pub. L. 98–67, 1983–2 C.B. 352, 359, requires that any person, including corporations, partnerships, individuals, estates and trusts, required to file more than 50 information returns **in the aggregate** for payments of certain interest (Forms 1099–INT and 1099–OID), dividends (Form 1099–DIV), or patronage dividends (Form 1099–PATR), for any calendar year, must file such returns on magnetic media. **THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS.** For example, if you must file 30 Forms 1099–DIV and 25 Forms 1099–INT, filing on magnetic media is required whether these are original or corrected returns. In addition, for returns filed in 1987 (for tax year 1986), magnetic media reporting is required if you file 500 or more of **each** of the following forms: Forms W–2, W–2P, W–2G, 1098, 1099–A, 1099–G, 1099–MISC, 1099–R, 5498, 1042S, 6248 and 8027. **THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS.** Form W–2c is not included in these filing requirements. The 500 or more requirement for these forms will drop to 250 or more for returns (original or corrected) filed in 1988 (for tax year 1987) and later years. Forms W–2 and W–2P are filed with Social Security Administration (SSA), **NOT** the Internal Revenue Service (IRS). At this time, corrected returns filed on Form W–2c with SSA are not required on magnetic media. The requirements shall not apply if you establish that it will cause you undue hardship. Refer to Part A, Sec. 5.

.03 This procedure also provides the requirements and specifications for magnetic diskette filing under the Combined Federal/State Filing Program. Refer to Part A, Sec. 14.

.04 The following revenue procedures and publications provide more detailed filing procedures for certain information returns:

(a) 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" provide further information on filing returns with IRS. These instructions are available at IRS offices.

(b) Rev. Proc. 84–24, 1984–1 C.B. 465, regarding preparation of transmittal documents (Forms 1096 and 4804) for information returns.

(c) Rev. Proc. 84–33, 1984–1 C.B. 502, regarding the optional method for agents to report and deposit backup withholding.

(d) Publication 1179, Specifications for Paper Substitutes for Forms 1096, 1098, 1099, 5498, and W–2G.

.05 Refer to Part A, Sec. 15 for definitions of terms used in this publication.

SEC. 2. BACKGROUND—PRIOR YEAR CHANGES (TAX YEAR 1985)

TAX YEAR 1986 IS THE FIRST YEAR THAT A REVENUE PROCEDURE HAS BEEN PUBLISHED FOR SUBMITTING INFORMATION RETURNS ON 5¼ INCH DISKETTE. IN FUTURE TAX YEARS, THIS SECTION WILL CONTAIN CHANGES THAT OCCURRED IN THE PRIOR YEAR.

SEC. 3. NATURE OF CHANGES—CURRENT YEAR (TAX YEAR 1986)

.01 The following information must be incorporated into your programs for tax year 1986. Tax year 1986 is the first year that a revenue procedure has been published for submitting information returns on 5¼ inch diskette. If you have filed on other types of magnetic media or if this is the first time that you have filed on magnetic media, this section will list the changes that have occurred between tax year 1985 and 1986.

.02 GENERAL CHANGES ARE AS FOLLOWS:

(a) The note on the cover and which follows the table of contents will alert filers that their data should be reviewed for accuracy before submission to prevent erroneous notices to the person for whom reports are filed.

(b) Part A, Sec 1.01 lists the forms described in this revenue procedure that must be filed on magnetic media. **THESE REQUIREMENTS APPLY TO BOTH ORIGINAL AND CORRECTED RETURNS.** Corrected returns filed on Form W–2c with SSA are not required at this time on magnetic media.

(c) A note in Part A, Sec. 4.01 alerts filers that applications to file Forms W–2 and W–2P on magnetic media are requested from SSA; however, requests for magnetic media related undue hardship waivers and extensions of time to file Forms W–2 and W–2P on magnetic media are requested from the IRS National Computer Center. Waiver requests for these forms must be filed by June 30 for the tax year requested.

(d) Transmitter Control Codes may be alpha/numeric. This has been noted in several places within the publication.

(e) The dates for submission of "test" files have changed. Part A, Sec. 5 indicates that "test" files should be submitted between August 15 and December 15 each year. Also, "test" data for the "A" Record must be actual data, not fictitious information.

(f) Part A, Sec. 5.04 alerts filers that a transmittal Form 4804, 4802 or computer generated substitute must accompany "test" files. The transmittal Form 4804 and 4802 have been updated for 1986. Agencies who produce a computer generated substitute must follow the format of the updated forms. The Form 4804 now includes a Checkbox 1 to indicate the type of file (e.g., original, correction, replacement, test).

(g) Part A, Sec. 5 includes new information concerning undue hardship waiver requests. Filers are now required to submit Form 8508, Request for Waiver From Filing Information Returns on Magnetic Media. **THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS WITH THE EXCEPTION OF FORM W–2c.**

(h) Part A, Sec. 6 includes the retention requirements for information returns and the new affidavit requirements for transmittal documents.

(i) For documents filed on paper with the appropriate service center, it is no longer necessary to note on the transmittal Form 1096 that a portion of the returns are being filed on magnetic media.

(j) Part A, Sec. 6.08 indicates that reports from different branches for one payer, **if submitted on the same file,** must be consolidated under one "A" Record for each type of information return.

(k) Part A, Sec. 7 indicates that Form 5498 is used to report amounts contributed during or after the calendar year but not later than April 15.

(l) Part A, Sec. 8 (h) informs persons who file extension requests for multiple payers that the request must include a list of all payers and their TINs (SSN or EIN).

(m) Part A, Sec. 10 alerts filers that the magnetic media filing requirements apply to both original and corrected returns with the exception of Form W–2c filed with SSA. Refer to Part A, Sec. 1 for the filing requirements. Corrected returns should be aggregated and submitted as soon as possible but not later than October 1 of each year. Also, corrections should be submitted only for the returns filed in error, not the entire file.

(n) Part A, Sec. 10.01 indicates that diskette position 6 is the corrected return indicator. Sec. 10, Guidelines, also reflects this information.

(o) Transmittal Form W–3G is now obsolete. This form was used to transmit paper Forms 1099–R and W–2G. These two forms are now to be transmitted to the service center with Form 1096. References to Form W–3G have been deleted from all publications.

(p) Two new charts were added to the publications last year to provide instructions for filing corrections on magnetic media and on paper forms. Chart 2, Guidelines for Filing Corrected Returns on Paper Forms, has been deleted. The instructions for filing corrections on paper forms are now available in the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G."

(q) Part A, Sec. 10 Guidelines have been revised. If a return was filed with NO Payee TIN (SSN or EIN), or the return was filed with an incorrect Payee TIN, only one transaction is now necessary to make the correction.

(r) Part A, Sec. 12 has been completely revised. Refer to this section for specific changes.

(s) Service center addresses have been deleted from these publications. They are available in the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G."

(t) Part A, Sec. 14.02 informs filers of the authorization to sign consent Form 6847. Filers who have received approval to file on the Combined Federal/State Program in prior years may be required to resubmit a consent Form 6847 signed by each payer. Refer to Part A, Sec. 14.02 for specific information.

(u) The dollar criteria in Table 2 of Part A, Sec. 14 has changed. For the state of Minnesota, Form 5498 must now be reported. Also, two footnotes for Minnesota have now been deleted: $10.01 for Savings and Loan Associations and Credit Unions; and $600.01 for Rents and Royalties.

(v) Acceptable foreign country codes are listed in Part A, Sec. 16 to assist you in developing the address field.

(w) A note appears in Part B, Sec. 1.02 concerning the consistency in the use of recording codes and density.

(x) Part B, Sec. 1.05 indicates changes made to the external media labels. Form 5064 is the external media label and has been updated for tax year 1986. You must use the updated label for 1986. These will be included in your magnetic media reporting packages.

.03 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE PAYER/TRANSMITTER "A" RECORD.

(a) A note in Part B, Sec. 3.03 indicates that all alpha characters should be uppercase.

(b) Diskette positions 3-5 contain the Diskette Sequence Number. The description of this field has been clarified.

(c) Form 1099–MISC, Amount Code "8", Direct Sales Indicator, NOTE 1, has been clarified.

(d) Form 1099–OID, the title of Amount Code 2 has been changed from "Stated interest" to "Other periodic interest."

(e) Form 1099–R, the term "Insurance Contracts" have been added to the title of the form and insurance premiums has been added to Amount Code "5.".

(f) Amount Code "7" has been added to Form 1099–R to report "State income tax withheld."

(g) A note has been added for reporting distributions from KEOGH plans on Form 1099–R.

(h) Form 5498, Amount Code "1" has been changed to report "Regular SEP contributions made in 1986 and 1987 for 1986." The regular SEP contributions have been deleted from Amount Code "3" and now appear separately as Amount Code "1."

(i) Form 5498, the title of Amount Code "4" has been changed to "Life insurance cost included in codes 1 or 3 (for endowment contracts only)."

(j) Amount Code "3" has been added for Form W–2G to report "State income tax withheld."

(k) The First Payer Name Line has been clarified for those reporting on Form 1098, "Mortgage Interest Statement." **Refer to the First Payer Name Line field description for specific information.**

.04 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE PAYEE "B" RECORD:

(a) A note has been added to Part B, Sec. 5.03 concerning invalid addresses.

(b) A note in Part B, Sec. 5.08 indicates that all alpha characters should be uppercase.

(c) The Document Specific Code field length has been increased from 1 to 2 positions. Diskette positions 4-5 represent this coding. This change was necessary due to multiple coding required in certain cases for Form 1099–R.

(d) Additional coding and clarification appear in the Document Specific Code for Form 1099–R. A Code "9" represents PS 58 Costs; Code "P" represents excess contributions refunded plus earnings on such excess contributions taxable in 1985; Code "A" represents distributions that qualify for 10-year averaging; Code "B" represents distributions that qualify for the death benefit exclusion; and Code "C" indicates that the distribution qualifies for both "A" and "B."

(e) The Document Specific Code, Direct Sales indicator has been clarified.

(f) Diskette position 6 is the corrected return indicator.

(g) Examples have been added to assist you in the development of the Name Control Field.

(h) The Type of TIN indicator field has been clarified for those accounts that are questionable. Code "9" has been deleted.

(i) The Payer's Account Number for the Payee field has been clarified.

(j) The First Payee Name Line field description has been clarified for those reporting Form 1098, "Mortgage Interest Statement." **Refer to the First Payee Name Line field description for specific information.**

(k) The Payee City, Payee State, and Payee ZIP Code are three separate fields.

If the payee lives outside of the United States, insert a "1" in position "241" of the Payee City field and spell out the name in the remaining positions. Use the appropriate Country Code as shown in Part A, Sec. 16 in the Payee State field. Some foreign countries utilize alpha characters in the ZIP Code. The use of alpha characters is only acceptable if there is a "1" in position "241" of the Payee City field.

.05 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE END OF PAYER "C" RECORD:

(a) Part B, Sec. 13.03 clarifies the totals required in the "C" Record.

(b) Part B, Sec. 13.04 provides instructions to assist you in the development of the "C" Record.

.06 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE END OF TRANSMISSION "F" RECORD:

(a) The Number of Payers field name and description has been reworded.

(b) The Number of Reels field description has been reworded.

SEC. 4. WAGE AND PENSION INFORMATION FILED WITH SSA

.01 Section 8(b), Pub. L. 94–202, 1976–1 C.B. 503, enacted in January 1976, authorized the combined reporting of FICA detailed information in one consolidated annual W–2 (Copy A) to the Federal government. AS A RESULT, FORMS W–2 and W–2P ARE TO BE FILED WITH SSA, NOT WITH IRS. Applications to file Forms W–2 and W–2P on magnetic media are to be mailed to SSA; however, undue hardship waivers and extensions of time to file Forms W–2 and W–2P are to be requested from the IRS National Computer Center, NOT from SSA. Requests for undue hardship exemption for these two forms must be filed with the IRS National Computer Center by July 31, 1986, for tax year 1986, for returns to be filed in 1987. Refer to Part A, Sec. 13 for the address and Part A, Sec. 5.08 and Sec. 8 for the required information.

.02 SSA will accept magnetic media filing of Forms W–2 and W–2P and has issued the following concerning this: TIB–4a, "**Magnetic Tape Reporting,** Submitting FICA Wage and Tax Data to the Social Security Administration; TIB–4b, "**Magnetic Tape Reporting,** Submitting Annuity, Pension, Retired Pay or IRA Payment to the Social Security Administration"; and TIB–4c, "**Diskette Reporting,** Submitting FICA Wage and Tax Data to the Social Security Administration." Applications for filing Forms W–2 and W–2P on magnetic media appear in TIBs–4a, 4b, and 4c.

.03 Copies of Social Security Administration publications TIB–4a, 4b, and 4c are available from any local Social Security Administration office or the SSA Regional Magnetic Media Coordinators.

SEC. 5. APPLICATION FOR MAGNETIC MEDIA REPORTING AND REQUESTS FOR UNDUE HARDSHIP WAIVERS

.01 For purposes of this revenue procedure, the **PAYER** includes the person making payments, a recipient of mortgage interest payments, a broker, a barter exchange, a trustee or issuer of an IRA, SEP or DEC, or a lender who acquires an interest in secured property or who has reason to know that the property has been abandoned. The **TRANSMITTER** is the organization preparing the magnetic diskette file. The payer and transmitter may be the same organization. Payers or their transmitters are required to complete Form 4419, Application for Magnetic Media Reporting of Information Returns. A copy of this form, for your use, can be found at the end of this publication. Requests for additional information or forms related to magnetic media processing should be addressed to the National Computer Center. Beginning January 1, 1986, magnetic media processing was centralized at the National Computer Center. The address is listed in Part A, Sec. 13.

.02 Applications should be filed with the National Computer Center before "**test**" files are submitted. ("Test" files must be submitted between August 15 and December 15 each year.) IRS will act on an application and notify the applicant, in writing, of authorization to file. A five character alpha/numeric **Transmitter Control Code** will be assigned and included in an acknowledgement letter within 30 days of receipt of the application. Magnetic diskette returns may not be filed with IRS until the application has been approved. Do not enter blanks in the "A" Record Transmitter Control Code field; enter the five character alpha/numeric Transmitter Control Code that is assigned to you by IRS after you have filed an application and it has been approved. Applications for approval to file Forms W–2 and W–2P on magnetic media must be filed with SSA, not with IRS. Refer to Part A, Sec. 4.

.03 After you have received approval to file on magnetic media, you do not need to reapply each year; however, notify IRS in writing if:

(a) there are hardware or software changes that would affect the characteristics of the magnetic media submission (e.g., changing from diskette to tape filing or vice versa), a new Transmitter Control Code may be necessary or,

(b) you discontinue filing on magnetic media for a year (your five character alpha/numeric Transmitter Control Code may be reassigned).

If either of these conditions applies to you, you should contact IRS for clarification. In *ALL* correspondence, refer to your current five character alpha/numeric Transmitter Control Code to assist IRS in locating your files.

.04 IRS will assist new filers with their initial magnetic diskette submission by reviewing "*test*" files submitted in advance of the filing season. The "*test*" data should be actual data, for the "A" Record, not fictitious information. This applies to all records submitted in the "*test*" file. Approved payers or transmitters should submit "*test*" files to the National Computer Center. You *MUST* submit a "*test*" file in order to participate in the Combined Federal/State Program; however, you are encouraged to submit "*test*" files if you are a new filer on magnetic media. As a guideline, IRS prefers that all "*test*" files be submitted between August 15 and December 15 each year. Refer to Part A, Sec. 13 for the address. Do not submit "*test*" files after December 15. If you are unable to submit your "*test*" file by this date, you may *only* send a sample hardcopy printout or diskette dump to the National Computer Center that shows a sample of each type of record (A, B, C, K, and F) *used.* Clearly mark the hardcopy printout or diskette dump as "TEST DATA" and include identifying information such as name, address, and telephone number of someone familiar with the "*test*" print or diskette dump who may be contacted to discuss its acceptability. With all "*test*" data, include a transmittal Form 4804, 4802 or computer generated substitute marked as "TEST DATA" that identifies your five character alpha/numeric Transmitter Control Code and total record and money amounts. The transmittal Form 4804 and 4802 have been updated for tax year 1986. Agencies that produce a computer generated substitute must include the additional information required on these forms. The Form 4804 now includes a Checkbox 1 to indicate the type of file (*e.g.*, original, correction, replacement, test). The "*test*" data must be a sample of *actual* data coded according to the proper revenue procedure.

.05 If your magnetic media files have been prepared for you in the past by a service agency, and you now have computer equipment compatible with that of IRS and wish to prepare your own files, you must request your own five character alpha/numeric Transmitter Control Code by filing an application, Form 4419, as described above.

.06 If you as an individual or organization are an approved filer on magnetic media and you change the name of your organization, please notify the National Computer Center, in writing, so that your file may be updated to reflect the proper name.

.07 In accordance with section 1.6041-7(b) of the Income Tax Regulations, payments to providers of medical and health care services from separate departments of a health care carrier may be reported as separate returns on magnetic media. In this case, the headquarters office will be considered to be the transmitter, and the individual departments of the company filing reports will be considered to be payers. A *single* application form covering *all* the departments that will be filing on magnetic diskette should be submitted. One five character alpha/numeric Transmitter Control Code may be used for all departments.

.08 Any person required to file original or corrected returns on magnetic media may request a waiver from the filing requirements by submitting Form 8508, Request for Waiver From Filing Information Returns on Magnetic Media, with the IRS National Computer Center if filing on magnetic media would be an undue hardship. Requests for waivers for Forms W-2 and W-2P are due by July 31, 1986, for tax year 1986, for returns filed in 1987. For all other returns required to be filed on magnetic media, waiver requests must be filed at least 90 days before the returns are due. This waiver, if approved, will only provide exemption from magnetic media filing for one tax year. Filers may not apply for a waiver for more than one tax year at a time. You must reapply each year that a waiver is necessary. Copies of Form 8508 may be obtained from the IRS National Computer Center. See Part A, Sec. 13 for the address.

.09 Section 1.6045-1(1) of the Income Tax Regulations requires brokers and barter exchanges to use magnetic media in reporting *ALL* Form 1099-B data to IRS. *THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS.* Generally, *NEW* brokers and *NEW* barter exchanges may request an undue hardship exemption by filing a request for waiver from the IRS National Computer Center, by the end of the second month following the month in which they became a broker or barter exchange.

.10 *All* requests for magnetic media related undue hardship exemptions should be submitted to the IRS National Computer Center at least 90 days before the due date of the return except as stated in Sec. 5.09. All magnetic media related undue hardship requests for Forms W-2 and W-2P are to be filed with the IRS National Computer Center, not SSA and must be filed by July 31, 1986, for tax year 1986, for returns filed in 1987. Refer to Part A, Sec. 13 for the address.

.11 If you request a waiver from filing on magnetic media and it *is* approved, *do not send a copy of the approved waiver to the service center where you file your paper returns.* Keep the waiver for your records. Do *not* staple, paperclip or use rubberbands on any scannable forms. Paper information returns are read by an optical scanner (OCR) at the service centers.

.12 Waivers are granted on a case-by-case basis and may be approved at the discretion of the National Computer Center.

.13 If you are required to file on magnetic media but fail to do so, and you do not have an approved waiver on record, you may be subject to a failure to file penalty. Refer to Sec. 6.01 below.

.14 *An approved waiver from filing information returns on magnetic media does not provide exemption from filing; you MUST still file your information returns on acceptable paper forms.*

.15 A magnetic media reporting package, which includes all the necessary transmittals, labels, and instructions will be mailed to the last known address of all approved filers each year.

SEC. 6. FILING OF MAGNETIC MEDIA REPORTS AND RETENTION REQUIREMENTS

.01 If you do not file your returns on time, you may be subject to a $50 per document failure to file penalty. If you file without following the instructions in this revenue procedure, you may also be subject to a $50 per document failure to file penalty. The maximum penalty is $50,000. However, there is no maximum penalty for returns of 1099-INT, 1099-OID, 1099-DIV, 1099-PATR, 5498 or if the failure to file is due to intentional disregard of the filing requirements.

.02 Generally, you are now subject to a $50 penalty for *each* failure to include the payee's correct TIN on an information return unless the payer can demonstrate that the payer met the due diligence requirements. Refer to Part A, Sec. 11.

.03 Rev. Proc. 84-24, 1984-1 C.B. 465, gives detailed information on preparing transmittal documents (Forms 1096 and 4804) for information returns and is available at IRS offices. Specific guidelines are given on how to report the payer's name, address, and TIN on transmittal documents and information returns. Instructions for multiple transmittals and the submission of transmittals by service bureaus or agents are also covered.

.04 *THE MAGNETIC DISKETTE RECORDS ARE TO BE SUBMITTED TO THE NATIONAL COMPUTER CENTER; HOWEVER, PAPER INFORMATION RETURNS ARE TO CONTINUE TO BE FILED WITH THE SERVICE CENTERS.* Form 4804, Transmittal of Information Returns Reported on Magnetic Media, must accompany magnetic diskette submissions. If you file for multiple payers and have the authority to sign the affidavit on Form 4804, you should also submit Form 4802, Transmittal for Multiple Magnetic Media Reporting. *For IRS to ensure that your actual data records were formatted following THIS revenue procedure, include a hardcopy printout, fast print or diskette dump of the first five and last five blocks of the data that shows a sample of each type of record (A, B, C, K and F) used on the diskette.* This will be reviewed prior to actual processing to ensure that the data is in the proper format. *Be sure to include Form 4804, 4802 or computer generated substitute with your diskette shipment. DO NOT MAIL THE DISKETTES AND THE TRANSMITTAL DOCUMENTS SEPARATELY.* IRS encourages the use of a computer generated Form 4804 which includes *all* necessary information requested on the actual form.

Paper information returns must be transmitted to the appropriate service center using Form 1096, Annual Summary and Transmittal of U.S. Information Returns. *Do not send information returns filed on paper forms to the National Computer Center.*

.05 The affidavit for Form 4804 should be signed by the payer; however, the transmitter, service bureau, paying agent, or disbursing agent may sign the affidavit on behalf of the payer if all of the following conditions are met:

(a) It has the authority to sign the affidavit under an agency agreement (either oral, written, or implied) that is valid under the state law.

(b)(i) It has the responsibility (either oral, written or implied) conferred on it by the payer to request the TINs of recipients (or others for whom information is being reported),

OR

(ii) If the return of more than one payer is included in a single diskette submission, covered by a single Form 4804, each payer has attested by affidavit to the transmitter, service bureau, paying agent, or disbursing agent that the payer has complied with the law in attempting to secure correct TINs.

(c) It signs the affidavit and adds the caption "For: (name of payer)."

.06 Although a duly authorized agent signs the affidavit, the payer is held responsible for the accuracy of the Form 4804, and the payer will be liable for penalties for failure to comply with filing requirements.

.07 DO NOT REPORT THE SAME INFORMATION ON PAPER FORMS THAT YOU REPORT ON MAGNETIC MEDIA. IF YOU REPORT PART OF YOUR RETURNS ON PAPER AND PART ON MAGNETIC MEDIA, BE SURE THAT DUPLICATE RETURNS, WITH THE SAME INFORMATION, ARE NOT INCLUDED ON BOTH. This does not mean that corrected documents are not to be filed. If a return has been prepared and submitted improperly, you must file a corrected return as soon as possible. Refer to Part A, Sec. 10 for requirements and instructions on filing corrected returns.

.08 Reports from different branches or locations for one payer, if submitted on the same file, *MUST* be consolidated under one Payer/Transmitter "A" Record for each type of information return. For example, all Forms 1099-INT for the same payer on a single file must be sorted together under one Payer/Transmitter "A" Record followed by the appropriate "B" Records and one "C" Record.

.09 Payers are required to retain a copy of the information returns filed with IRS or the ability to reconstruct the data for at least three years.

.10 Before submitting magnetic media files, include the following:

(a) A signed Form 4804 or computer generated substitute.

(b) A Form 4802 (if you transmit for multiple payers).

(c) A hard copy printout or listing of the first five and last five blocks of your file. The listing should show a sample of each type of record (A, B, C, K, and F) used on the magnetic media being submitted.

(d) The magnetic media with an external identifying label as described in Part B, Sec. 1.

(e) On the outside of the shipping container, include a Form 4801 or a substitute for the form which reads "DELIVER UNOPENED TO TAPE LIBRARY—MAGNETIC MEDIA REPORTING—BOX ■ of ■." If there is only one container, mark the outside as Box *1* of *1*. For multiple containers, include the sequence (*e.g.*, Box *1* of *33*, *2* of *33*, etc.).

(f) If you were granted an extension, include a copy of the approval letter with the magnetic media shipment.

.11 IRS will not pay or accept "Collect on Delivery" or "Charged to IRS" shipments of reportable tax information that an individual or organization is legally required to submit.

.12 Files returned to you due to coding or format errors are to be corrected and returned to IRS within 30 days of your receipt or the payer may be subject to a failure to file penalty.

SEC 7. FILING DATES

.01 The dates prescribed for filing paper returns with IRS also apply to magnetic media filing. Magnetic media reporting to IRS for Forms 1098, 1099, and W-2G must be on a calendar year basis. Form 5498 is used to report amounts contributed during or after the calendar year but not later that April 15.

.02 Information returns filed on magnetic media for Forms 1098, all types of Forms 1099, and W-2G must be submitted to IRS and postmarked by February 28. The due date for furnishing the required copy or statement to the recipient is January 31.

.03 Information returns filed on magnetic media for Form 5498 must be submitted to IRS and postmarked by May 31. Copies of this form or statements are due to the participant by May 31 for contributions made to IRAs and SEPs for the prior calendar year; however, *participant* copies or statements for DECs are due at the time the contribution is made or January 31, whichever is later. Form 5498 is filed for contributions to be applied to 1986 that are made between January 1, 1986, and April 15, 1987.

SEC. 8. EXTENSIONS OF TIME TO FILE

.01 If a payer or transmitter of returns *on magnetic media* filed with IRS or SSA is unable to submit their magnetic media file by the dates prescribed in Sec. 7.02 and 7.03 above, submit a letter requesting an extension of up to 30 days to file, as soon as you are aware that an extension will be necessary. In order to be considered, the request *MUST* be filed *before* the due date of the return; otherwise, you will be subject to a late filing penalty. The letter should be sent to the attention of the Magnetic Media Reporting Program at the IRS National Computer Center. See Part A, Sec. 13 for the address. The request should include:

(a) The filer's (or transmitter's, if filing for multiple payers) name and address.

(b) The filer's Taxpayer Identification Number (SSN or EIN).

(c) The tax year for which the extension of time is requested: tax year 1986.

(d) The name and telephone number of a person to contact who is familiar with the request.

(e) The type of returns and expected volume (*e.g.*, 5000 Forms 1099-INT).

(f) The five character alpha/numeric Transmitter Control Code assigned to the organization or individual requesting the extension (if a number has been assigned).

(g) The reason for the delay and date that you *will* be able to file.

(h) If you file for multiple payers, the request must include a list of all payers and their TINs (SSN or EIN).

An approved extension *for magnetic media filing* does not provide additional time for supplying a copy to the payee.

02. If an extension of time to file on magnetic media is granted by the National Computer Center, a *copy* of the letter *granting the extension MUST* be attached to the transmittal Form 4804 or computer generated substitute when the file is submitted.

SEC. 9. PROCESSING OF MAGNETIC MEDIA RETURNS

01. All data received at the National Computer Center for processing will be

given the same protection as individual returns (1040), and will be returned to the originator after processing. Files that are received timely by the National Computer Center will be returned to the filers by August 15 of the year in which submitted.

.02 *Due to the volume of input received and the cost to return special containers, special shipping containers should not be used for transmitting data to the National Computer Center since IRS cannot guarantee return of such containers.*

.03 Files will be returned to you for correction if they are unprocessable due to format or coding errors, or by the request of the filer. Unprocessable files must be corrected and returned to the National Computer Center within 30 days of your receipt or the payer may be subject to a failure to file penalty. The corrected files will be returned to the filer by the National Computer Center within 6 months of receipt. PLEASE BE SURE THAT YOUR FORMAT AND CODING COMPLY WITH THIS REVENUE PROCEDURE. *THIS REVENUE PROCEDURE IS TO BE USED FOR THE PREPARATION OF TAX YEAR 1986 INFORMATION RETURNS ONLY.* LEGISLATIVE AND FORMS CHANGES AFFECTING INFORMATION RETURNS MAY OCCUR EACH YEAR. THESE PROCEDURES ARE UPDATED TO REFLECT NECESSARY CHANGES. PLEASE READ THIS PUBLICATION CAREFULLY.

SEC. 10. HOW TO FILE CORRECTED RETURNS

.01 The filing requirements listed in Part A, Sec. 1 apply to both original and corrected returns. Corrections should be aggregated and filed as soon as possible but not later than October 1 of each year. *ALL FIELDS OR BOXES MUST BE COMPLETED WITH THE CORRECT INFORMATION, NOT JUST THE DATA FIELDS NEEDING CORRECTION.* Submit corrections only for the returns filed in error, not the entire file. If your complete file is in error, contact the National Computer Center immediately. There are numerous types of errors. It may require more than one transaction to properly correct the initial error. In prior years, position 5 of the "B" Record was used as the corrected return indicator. This has now been changed to position 6. You are strongly encouraged to read this *ENTIRE* section before attempting to make *ANY* correction. If the initial return was filed as an aggregate, you must consider this in filing the corrected return.

.02 Corrected returns submitted to IRS on magnetic media, using a "G" coded Payee "B" Record, may be submitted on the same diskette as those returns submitted without the "G" code; however, they must be submitted using a separate "A" Record. Corrected returns for different tax years may *not* be submitted on the same file. Corrected returns are to be identified as corrections on the transmittal document and the *EXTERNAL* affixed label of the file.

.03 The instructions that follow will provide information on how to file corrected returns on magnetic media. The 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" provide more specific instructions for filing corrections on paper forms and are available from IRS.

.04 *If you are not required to file your corrections on magnetic media and you file them on paper forms, do not submit the paper returns to the National Computer Center. All paper returns, whether original or corrected, must be filed with the appropriate service center. Corrected returns filed on magnetic media must be filed with the National Computer Center.* Refer to Part A, Sec. 13 for the address.

.05 Statements to the recipient or participant should be identified as "CORRECTED" and should be provided to them as soon as possible.

.06 If you file corrected returns on paper forms, use IRS forms or acceptable OCR scannable paper substitutes. Pinhole feeds on the forms are not acceptable. Always submit Copy A to the appropriate service center. *NOTE:* Form W–2G is not required to be in OCR scannable format. Publication 1179, "Specifications for Paper Substitutes for Forms 1096, 1098, 1099, 5498, and W-2G" provides requirements and instructions.

.07 For instructions on filing information returns with IRS, refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G." If these instructions are not included in your magnetic media reporting packages, request a copy from IRS.

.08 Type or machine print in black carbon based ink all information on returns filed on paper. Print money amounts without dollar signs ($), ampersands (&), asterisks (*), commas(,), or other special characters. Use decimal points (.) to indicate dollars and cents on paper forms only, not on magnetic media.

.09 Use the proper form. If you are in doubt, review the instructions noted in .07 above or contact IRS.

.10 Use only the boxes provided on the paper forms. Do not add additional boxes.

.11 Do not change the title of any box on any forms and do not insert data in the untitled shaded areas.

.12 Use the same name and TIN (SSN or EIN) for the filer on the Form 1096 transmittal form and all related forms that follow.

.13 A separate transmittal Form 1096 is required for each *type* of paper information return filed in the 1098, 5498. W–2G, and 1099 series. DO NOT USE THE SAME TRANSMITTAL DOCUMENT TO FILE ORIGINAL AND CORRECTED RETURNS WHETHER ON PAPER FORMS *OR* MAGNETIC MEDIA. A transmittal Form 4804 or computer generated substitute is used to transmit magnetic media. A Form 4802 is a *continuation* form for a Form 4804. Please utilize a Form 4802 if you file on magnetic media for multiple payers and are an authorized agent for the payers.

.14 Do not cut, staple, fold, paperclip, tape, or use rubberbands on any paper information returns filed with IRS. This could impair the OCR scanning process. No photocopies of any forms are allowable.

.15 Use the correct tax year's forms to file information returns with IRS (*i.e.,* do not submit tax year 1986 returns using 1985 forms). The same is true for magnetic media filing. You must submit your returns filed on magnetic media using the revenue procedure for the tax year of the returns. Forms and revenue procedures are normally updated each year to include necessary changes.

.16 Most information returns contain a "VOID" box and a "CORRECTED" box. The "VOID" box is used only if you make an error while typing or printing the paper forms. Mark this box ONLY when you wish the return to be disregarded or passed over. The OCR scanner at the service centers *will not read* a "VOID" return; it will pass over it a go to the next form if the "VOID" box is marked. Do not confuse the "VOID" box and the "CORRECTED" box.

.17 On magnetic media files, the Payee "B" Record provides space to enter a Payer's Account Number for the Payee.

This same account number may be provided on paper forms. In order to properly file corrected returns, this number will help identify the appropriate incorrect return. DO NOT ENTER A TIN (SSN OR EIN). ***A PAYER'S ACCOUNT NUMBER FOR THE PAYEE MAY BE A CHECKING ACCOUNT NUMBER, SAVINGS ACCOUNT NUMBER, SERIAL NUMBER OR ANY OTHER NUMBER ASSIGNED TO THE PAYEE BY THE PAYER, THAT WILL DISTINGUISH THE SPECIFIC ACCOUNT. THIS NUMBER MUST APPEAR ON THE INITIAL RETURN AND ON THE CORRECTED RETURN IN ORDER TO IDENTIFY AND PROCESS THE CORRECTION PROPERLY.***

.18 REVIEW THE GUIDELINES THAT FOLLOW. The types of errors made will *normally* fall under one of the three categories listed. Next to each *type* of error made, you will find a list of instructions to tell you how to *properly* file the corrected return for *that* type of error. READ ALL OF THE INSTRUCTIONS LISTED AND FOLLOW THEM FOR THE TYPE OF ERROR MADE ON THE INITIAL RETURN. *IN SOME CASES TWO TRANSACTIONS ARE REQUIRED TO PROPERLY FILE CORRECTIONS. IF THE ORIGINAL RETURN WAS FILED AS AN AGGREGATE, YOU MUST CONSIDER THIS IN FILING CORRECTED RETURNS.*

Guidelines for Filing Corrected Returns On Magnetic Media

(PLEASE READ SEC. 10.01 THROUGH 10.18 OF THIS PUBLICATION BEFORE MAKING *ANY* CORRECTIONS)

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
1. Original return was filed with *NO* Payee TIN (SSN or EIN), *OR* the return was filed with an *INCORRECT* Payee TIN.	**A. *Form 4804 and 4802 (or computer generated substitute)* 1. Prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers) or a computer generated substitute, that includes information related to this new file. 2. Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute. 3. Provide *ALL* requested information correctly. 4. Include a hardcopy print, listing or diskette dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format*. 5. If you are a Combined Federal/State filer, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer. B. *1098, 1099 Series, 5498 and W–2G Returns* 1. Prepare a new file. 2. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported. The information in the "A" Record will be the same as it was in the original submission. 3. The Payee "B" Record must contain exactly the same information as submitted previously *EXCEPT:* insert a "G" code in diskette position 6 of the "B" Record and supply the correct TIN (SSN or EIN). (In prior years, position 5 was used as the corrected return indicator. This has now been changed to position 6.) 4. Corrected returns submitted to IRS using a "G" coded "B" Record may be submitted on the same diskette as those returns submitted *without* the "G" code; however, separate "A" Records are required. 5. Mark the *EXTERNAL* label of the diskette "MAGNETIC MEDIA CORRECTION." 6. Submit the diskette(s), a diskette dump showing sample records coded for this type of filing, and the transmittal document to the National Com-**

Guidelines for Filing Corrected Returns On Magnetic Media—Continued

(PLEASE READ SEC. 10.01 THROUGH 10.18 OF THIS PUBLICATION BEFORE MAKING *ANY* CORRECTIONS)

Error Made on the Original Return Filed on Magnetic Media | **How To File the Corrected Return on Magnetic Media**

puter Center. (Refer to Part A, Sec. 13 for the address.)

2. Original return was filed with an incorrect money amount(s) in the Payee "B" Record, *OR* a money amount was reported using an incorrect Payment Amount Indicator in the original Payer/Transmitter "A" Record. Correct *Type of Return* indicator was used in the "A" Record. (NOTE: If the wrong *Type Of Return* indicator was used, see number 3 of this chart.)

A. *Form 4804 and 4802 (or computer generated substitute)*

1. **Prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers), or a computer generated substitute, that includes information related to this new file.**
2. **Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in upper case letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute.**
3. **Provide *ALL* requested information correctly.**
4. **Include a hardcopy print, listing or diskette dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format*.**
5. **If you are a Combined Federal/State filer, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer.**

B. *1098, 1099 Series, 5498 and W–2G Returns*

1. **Prepare a *new* file.**
2. **Use a separate Payer/Transmitter "A" Record for each *type* of return being reported. The information in the "A" Record will be the same as it was in the original submission EXCEPT, the *correct* Amount Indicators will be used.**
3. **The Payee "B" Record must contain exactly the same information as submitted previously *EXCEPT:* insert a "G" code in diskette position 6 of the "B" Record *AND* report the correct payment amounts as they should have been reported on the initial return. (In prior years, position 5 was used as the corrected return indicator. This has now been changed to position 6.)**
4. **Corrected returns submitted to IRS using a "G" coded "B" Record may be submitted on the same diskette as those returns submitted *without* the "G" code; however, separate "A" Records are required.**
5. **Mark the *EXTERNAL* label of the diskette "MAGNETIC MEDIA CORRECTION."**
6. **Submit the diskette(s), a diskette dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for the address.)**

3. Original return was filed using the WRONG *Type of Return* indicator in the Payer/Transmitter "A" Record. (For example, a return was coded using the *Type of Return* indicator for 1099–DIV and it should have been coded 1099 INT.) THIS WILL REQUIRE TWO SEPARATE TRANSACTIONS TO MAKE THE CORRECTION PROPERLY. READ AND FOLLOW *ALL* INSTRUCTIONS FOR *BOTH* TRANSACTIONS 1 AND 2.

***TRANSACTION 1:* Identify return submitted with an incorrect Type of Return indicator**

A. *Form 4804 and 4802 (or computer generated substitute)*

1. **Prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers), or a computer generated substitute, that includes information related to this new file.**
2. **Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is**

Guidelines for Filing Corrected Returns On Magnetic Media—Continued

(PLEASE READ SEC. 10.01 THROUGH 10.18 OF THIS PUBLICATION BEFORE MAKING *ANY* CORRECTIONS)

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media

not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute.

3. Provide *ALL* requested information correctly.
4. Include a hardcopy print, listing or diskette dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format.*
5. If you are a Combined Federal/State filer, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer.

B. *1098, 1099 Series, 5498 and W–2G Returns*

1. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported. The information in the "A" Record will be exactly the same as it was in the original submission using the same incorrect type of return indicator.
2. The corrected Payee "B" Record must contain the same information as submitted previously *EXCEPT:* insert a "G" code in diskette position 6 of the "B" Record and for *ALL* payment amounts *used,* enter "0" (zero). (In prior years, position 5 was used as the corrected return indicator. This has now been changed to position 6.)
3. Corrected returns submitted to IRS using a "G" coded "B" Record may be submitted on the same diskette as those returns submitted *without* the "G" code; however, separate "A" Records are required.
4. Mark the *EXTERNAL* label of the diskette "MAGNETIC MEDIA CORRECTION."
5. Submit the diskette(s), a diskette dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for the address.)

TRANSACTION 2: Report correct information

A. *Form 4804 and 4802 (or computer generated substitute)*

1. If you submit records with the corrected information on a separate diskette from those that are "G" coded, prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers), or a computer generated substitute, that includes information related to this new file.
2. Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute.
3. Provide *ALL* requested information correctly.
4. Include a hardcopy print, listing or diskette dump exhibiting a small sample of each type of *record*

Guidelines for Filing Corrected Returns On Magnetic Media—Continued

(PLEASE READ SEC. 10.01 THROUGH 10.18 OF THIS PUBLICATION BEFORE MAKING *ANY* CORRECTIONS)

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
	(A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format.* 5. If you are a Combined Federal/State filer, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer. B. *1098, 1099 Series, 5498 and W–2G Returns* 1. Prepare a *new* file with the correct information in *ALL* records. 2. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported and use the correct Type of Return indicator. 3. *Do not code the Payee "B" Record as a corrected return for this type of correction.* 4. Provide all of the correct information. 5. Mark the *EXTERNAL* label of the diskette "MAGNETIC MEDIA CORRECTION." 6. Submit the diskette(s), a diskette dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for the address.)

SEC. 11. TAXPAYER IDENTIFICATION NUMBERS

.01 Under section 6109 of the Internal Revenue Code, recipients of all reportable payments on information returns are required to furnish taxpayer identification numbers (TINs) to the payer. The number must be furnished to the payer whether or not the payee is required to file a tax return or is covered by social security. Refer to Part A, Sec. 15 for a definition of taxpayer identification number (TIN).

.02 The recipient's TIN is used to associate and verify amounts reported to IRS with corresponding amounts on tax returns. Therefore, it is particularly important that correct social security and employer identification numbers for payees be provided on magnetic media or paper forms submitted to IRS. *DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS.*

.03 Under section 6676 of the Internal Revenue Code, a *$50 penalty* applies for each failure to furnish a TIN to another person who is required to file an information return, and for each failure to include a TIN on an information return. The penalty applies unless the failure to comply is due to reasonable cause and not willful neglect.

.04 With respect to all payers of interest and dividends, section 6676 of the Internal Revenue Code provides that the payer must self-assess a *$50 penalty* for each failure to include a payee's TIN or each inclusion of an incorrect TIN on an information return, unless the payer can demonstrate that the payer met the due diligence requirements in attempting to acquire correct TINs for payees. Use Form 8210, Self-Assessed Penalties Return.

.05 For any reportable payment, if the payee fails to provide a TIN to the payer then backup withholding must be instituted for that payee. If the payer receives another TIN in the manner required from the payee within 30 days of notice from IRS, no backup withholding is required. If the payee has applied for a TIN, the payee may certify to this on Form W–9 by noting "Applied For" in the TIN block and by signing the form. This form then becomes an "awaiting-TIN certificate." If the TIN is not received and certified, if required, within 60 days, begin withholding and continue until you receive a TIN in the manner required.

.06 The TIN to be furnished to IRS depends primarily upon the manner in which the account is maintained or set up on the payer's record. The TIN to be provided must be that of the owner of the account. If the account is recorded in more than one name, furnish the TIN and name of one of the owners of the account. The TIN provided must be associated with the name of the payee provided in the first name line of the Payee "B" Record. For individuals, including sole proprietors, the payee TIN is the payee's social security number. For other entities, the payee TIN is the payee's employer identification number.

.07 Sole proprietors who are payers should show their employer identification number in the Payer/Transmitter "A" Record. However, sole proprietors who are not otherwise required to have an employer identification number should use their social security number.

.08 Sole proprietors' social security numbers must be used in the Payee "B" Record.

.09 The charts below will help you determine the number to be furnished to IRS for recipients of reportable payments (payees).

CHART 1. *Guidelines for Social Security Numbers*

For this type of account—	In the Taxpayer Identification Number field of the Payee "B" Record, enter the SSN of—	In the First Payee Name Line of the Payee "B" Record, enter the name of—
1. An individual's account.	The individual.	The individual.
2. A joint account (Two or more individuals, husband and wife).	The actual owner of the account. (If more than one owner, the first individual on the account.)	The individual whose SSN is entered.
3. Account in the name of a guardian or committee for a designated ward, minor, or incompetent person.	The ward, minor, or incompetent person.	The individual whose SSN is entered.
4. Custodian account of a minor (Uniform Gift to Minors Act).	The minor.	The minor.
5. The usual revocable savings trust account (grantor is also trustee).	The grantor-trustee.	The grantor-trustee.
6. A so-called trust account that is not a legal or valid trust under state law.	The actual owner.[1]	The actual owner.
7. A sole proprietorship.	The owner.	The owner.

CHART 2. *Guidelines for Employer Identification Numbers*

For this account type—	In the Taxpayer Identification Number field of the Payee "B" Record, enter the EIN of—	In the First Payee Name Line of the Payee "B" Record, enter the name of—
1. A valid trust, estate, or pension trust.	Legal entity.[1]	The legal trust, estate, or pension trust.
2. A corporate account.	The corporation.	The corporation.
3. An association, club, religious, charitable, educational or other tax-exempt organization.	The organization.	The organization.
4. A partnership account held in the name of the business.	The partnership.	The partnership.
5. A broker or registered nominee/middleman.	The broker or nominee/middleman.	The broker or nominee/middleman.
6. Account with the Department of Agriculture in the name of a public entity such as state or local government, school district or prison that receives agriculture program payments.	The public entity.	The public entity.

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[1] Do not furnish the identification number of the personal representative or trustee unless the name of the representative or trustee is used in the account title.

SEC. 12. EFFECT ON PAPER RETURNS

.01 Magnetic diskette reporting of the information returns listed in Part A, Sec. 1 applies only to the original (Copy A).

.02 For payments of dividends or interest (reported on Forms 1099–DIV, 1099–PATR, 1099–INT or 1099–OID), the payer is required to furnish an official Form 1099 to a payee either in a separate mailing by First-Class mail or in person. These forms may not be combined or mailed with other information furnished to the recipient except Forms W–8, W–9, or other Forms 1099. The payer may use substitute Forms 1099 if they utilize the proper language, are substantially similar to the official forms and if the payer complies with all revenue procedures relating to substitute Forms 1099 in effect at the time (see Publication 1179). Copy B (For Recipient) of the substitute forms must contain the statement "This is important tax information and is being furnished to IRS. If you are required to file a return, a negligence penalty will be imposed on you if this income is taxable and IRS determines that it has not been reported." The substitute form must contain instructions substantially similar to those on the back of Copy B of the official form.

.03 Statements to recipients for Forms 1098, 1099–A, 1099–B, 1099–G, 1099–MISC (except for substitute payments in lieu of dividends and tax-exempt interest), 1099–R, 5498 or W–2G need not be a copy of the paper form filed with IRS. It is important that income items be properly classified for Federal tax purposes on the statement the payer gives to recipients. The message "This information is being furnished to IRS" must appear on the statements. In addition, Form 1098 statements must contain the message, "The amount shown is deductible by you for Federal income tax purposes only to the extent it was actually paid by you and not reimbursed by another person." The space provisions on official paper forms do not agree with those used in magnetic media. The amount of space on paper forms is less than that allowed on magnetic media. Filers may wish to seek a substitute form for Copy B (For Recipient) that accommodates the space provisions used in magnetic media. Payers are permitted considerable flexibility in designing Copy B of the information return to be furnished to the payee. The payer may combine the information return data with other reports or financial or commercial notices so long as all required information is present and worded properly and the payee's copy is conducive to proper reporting of income on tax returns. (This does not apply to Forms 1099–INT, 1099–OID, 1099–DIV, and 1099–PATR. See .02 above for the requirements for these four forms.) However, when information not requested on the official form is included on these substitute statements, they can no longer be mailed with recipient copies of Form 1099–DIV, INT, OID, or PATR without violating the separate mailing requirements.

.04 If a portion of the returns is reported on magnetic diskette and the remainder is reported on paper forms, those returns not submitted on magnetic diskette (including corrected returns) may require a waiver depending on the type of return and volume. Returns filed on paper must be filed on official forms or on acceptable paper substitutes meeting the specifications in Publication 1179.

Do not submit proposed substitutes of Copy A to the National Computer Center.

Your proposed substitutes must comply to the official form and the specifications outlined in Publication 1179. Do not submit any substitutes for approval. Only those forms that comply with the official form and the specifications in Publication 1179 are acceptable.

SEC. 13. TO CONTACT THE IRS NATIONAL COMPUTER CENTER

.01 Effective January 1, 1986, magnetic media processing for all service centers was centralized at the IRS National Computer Center. *Please direct all requests for IRS magnetic media related publications, information, undue hardship waivers, extensions or forms to the following addresses* (if Postal Service or land carrier):

Magnetic Media Reporting
Internal Revenue Service
National Computer Center
Post Office Box 1359
Martinsburg, WV 25401-1359

or

Magnetic Media Reporting
Internal Revenue Service
National Computer Center
Route 9 & Needy Road
Martinsburg, WV 25401

Hours of operation at this address will be 8:30 A.M. until 8:00 P.M. Eastern Time Zone. The telephone number is (304) 263-8700.

Requests for paper returns, publications or forms not related to magnetic media processing should be requested from local IRS offices or by calling the toll-free number in your area.

.02 The National Computer Center will process returns filed on magnetic media only. *All information returns, including corrections, filed on paper forms should be submitted to the appropriate service center, not the National Computer Center.* Organizations that file their information returns on magnetic media but that submit their corrected returns on *paper forms,* refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" for the service center addresses.

SEC. 14. COMBINED FEDERAL/STATE FILING

.01 The Combined Federal/State Program was established to simplify information returns filing for the taxpayer. IRS will accept, upon prior approval, magnetic diskette files containing state reporting information only for those states listed in Table 1 in this section. *FORMS 1098, 1099–A, 1099–B, AND W–2G CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.*

.02 To request approval to participate in the Combined Federal/State Program, a *"test"* file, *coded for this program,* must be submitted by the transmitter to the IRS National Computer Center between August 15 and December 15 using the revenue procedure that will be used for the actual data files. Blanket approval will not be given to software packages. The *"test"* file is only required for the first year. Once you are approved, you do not need to resubmit "tests" each year, except when notified by IRS. Refer to Part A, Sec. 13 for the address. See Part A, Sec. 5.04 for general guidelines on submission of *"test"* files. Each record, both in the *"test"* file and actual data file, must be 360 positions in length, and the file must conform *exactly* to the revenue procedure for the tax year of the *actual* data. Combined Federal/State records must be coded using each state's dollar criteria from Table 2 of this section for each *type* of return.

If the *"test"* file is determined to be acceptable, IRS will return it to the filer with Form 6847, Consent for Internal Revenue Service to Release Tax Information. The payer *must* complete Form 6847. The five character alpha/numeric Transmitter Control Code must be included on the form. The form should then be returned to IRS before IRS will release tax information to any of the participating states.

Form 6847 must be signed by one of the individuals listed at the bottom of the form. If the form is signed by an attorney-in-fact, the written consent from the taxpayer to the attorney-in-fact must be included with the Form 6847. This consent by language and/or scope must clearly indicate that the attorney-in-fact is empowered to authorize release of the information document returns to the state(s). A separate Form 6847 is required for each payer. A transmitter may not combine payers on one Form 6847 even though acting as attorney-in-fact for several payers. Form 6847 may be photocopied if you receive an insufficient number of the form. If you have filed on this program in the past and have not met these requirements, you must resubmit the Form 6847 with the proper signatures as specified. If you file for multiple payers, only code the records to go to the state(s) for those payers that participate and have properly submitted Form 6847. Do not submit *actual* data records coded for the Combined Federal/State Program without prior approval from IRS.

.03 States that participate in this program and the valid state code assigned to each are listed in Table 1 of this section. If the state that you wish information released to does *not* participate in the program, do *not* code your records for that state. If the state participates, if you have received prior approval, and if all other conditions are met, IRS will forward the tax information to the participating state at no charge to the filer. You do not need to reapply each year.

.04 *IF CORRECTIONS MUST BE MADE, IRS WILL NOT TRANSMIT CORRECTED RETURNS TO THE STATES; THIS WILL BE THE RESPONSIBILITY OF THE FILER.*

.05 IRS will make no attempt to process files with any deviations. Approval to participate in the Combined Federal/State Program will be revoked if any files are submitted that do not *totally* conform.

.06 IRS is acting as a forwarding agent *ONLY*. Some participating states require separate notification that you are filing in this manner. It is your responsibility to contact the appropriate state(s) for further information.

.07 The appropriate state code should be entered for those documents which meet that state's filing requirements. *It is the filer's responsibility* to determine the state code to be used and to obtain the filing requirements from the appropriate state(s).

.08 If you meet all of the requirements for this program, you *must* provide the state totals from the "K" Record on a separate Form 4804, Transmittal of Information Returns on Magnetic Media (or Form 4802, Transmittal For Multiple Magnetic Media Reporting) or computer generated substitute for each state, *or* you must include a listing which identifies each state and the "K" Record totals for each.

.09 If you have met *ALL* of the above conditions:

(a) You must submit all records using 360 positions which indicate the appropriate coding related to this program.

(b) The "C" Record *must* be followed by a "K" Record for each state. The "K" Record indicates the number of payees being reported to each particular state.

(c) Payment amount totals and the valid participating state code(s) must be included in the state totals "K" Record(s). Refer to Part B, Sec. 7 for a description for the "K" Record.

(d) The "K" Record is followed by an end of transmission "F" Record (if this is the last record of the entire file).

.10 Only those states listed in Table 1 below will receive information from IRS. *It is the filer's responsibility to file information returns with states that do not participate in this program.*

TABLE 1. PARTICIPATING STATES AND THEIR CODES

State	*Code*	*State*	*Code*	*State*	*Code*
Alabama	01	Iowa	19	New York	36
Arizona	04	Kansas	20	North Carolina	37
Arkansas	05	Maine	23	North Dakota	38
California	06	Massachusetts	25	Oregon	41
Delaware	10	Minnesota	27	South Carolina	45
District of Columbia	11	Mississippi	28	Tennessee	47
Georgia	13	Missouri	29	Wisconsin	55
Hawaii	15	Montana	30		
Idaho	16	New Jersey	34		
Indiana	18	New Mexico	35		

.11 To simplify filing, several of the participating states have provided lists of their information return reporting requirements (see Table 2). This cumulative list is for information purposes only and represents dollar criteria. For complete information on state filing requirements, contact the appropriate state tax agencies.

TABLE 2. DOLLAR CRITERIA

STATE	*1099–R*	*1099–DIV*	*1099–INT*	*1099–MISC*	*1099–PATR*	*1099–G*	*1099–OID*	*5498*
Alabama	1500	1500	1500	1500	1500	NR	1500	NR
Arizona[a]	300	300	300	300	300	300	300	NR
Arkansas	2500	100	100	2500	2500	2500	2500	g
District of Columbia[b]	600	600	600	600	600	600	600	NR
Hawaii	600	10	10[c]	600	10	all	10	g
Idaho	600	10	10	600	10	10	10	g
Iowa	1000	100	1000	1000	1000	1000	1000	NR
Minnesota	600	10	10	600	10	10	10	g
Missouri	NR	NR	NR	1200[d]	NR	NR	NR	NR
Montana	600	10	10	600	10	10	10	g
New Jersey	1000	1000	1000	1000	1000	1000	1000	NR

TABLE 2. DOLLAR CRITERIA—Continued

STATE	*1099–R*	*1099–DIV*	*1099–INT*	*1099–MISC*	*1099–PATR*	*1099–G*	*1099–OID*	*5498*
New York	600	NR	600	600[e]	NR	600	NR	NR
North Carolina	100	100	100	600	100	100	100	g
Oregon	600[f]	10	10	600	10	10	10	NR
Tennessee	NR	25	25	NR	NR	NR	NR	NR
Wisconsin	500	100	100	100	100	NR	NR	NR

NR—No filing requirement.

Footnotes:

- **a. These requirements apply to individuals and business entities.**
- **b. Amounts are for aggregates of several types of income from the same payroll.**
- **c. State regulation changing filing requirement from $600 to $10 is pending.**
- **d. The state would prefer those returns filed with respect to non-Missouri residents to be sent directly to the state agency.**
- **e. Aggregate of several types of income.**
- **f. Return required for state of Oregon residents only.**
- **g. Same as Federal requirement for this type of return.**

*** NOTE: Filing requirements for any state in Table 1 not shown on the above chart are the same as the Federal requirement.**

SEC. 15. DEFINITIONS OF TERMS

Element	*Description*
b	Denotes a blank position. Enter blank(s) when this symbol is used (do *not* enter the letter "b"). This appears in numerous areas throughout the record descriptions.
Coding Range	Indicates the allowable codes for a particular type of statement.
EIN	Employer Identification Number that has been assigned by IRS.
Excess Golden Parachute Payment	Parachute payments (also called "golden parachutes") are certain payments in the nature of compensation that corporations make to key individuals, often in excess of their usual compensation, in the event that ownership or control of the corporation changes.
File	For purposes of this procedure, a file consists of all magnetic diskette records submitted by a Payer or Transmitter.
Payee	Person(s) or organization(s) receiving payments from the Payer, or for whom an information return must be filed.
Payer	Includes the person making payments, a recipient of mortgage interst payments, a broker, a barter exchange, a trustee or issuer of an IRA, SEP or DEC, or a lender who acquires an interest in secured property or who has reason to know that the property has been abandoned. The Payer will be held responsible for the completeness, accuracy and timely submission of magnetic diskette files.
Special Character	Any character that is not a numeral, a letter or a blank.
SSA	Social Security Administration.
SSN	Social Security Number.
Taxpayer Identification Number (TIN)	May be either an EIN or SSN.
Transfer Agent	The transfer agent or paying agent is the entity (Paying Agent) who has been contracted or authorized by the payer to perform the services of paying and reporting backup withholding (Form 941). The payer must submit to IRS a Form 2678, Employer Appointment of Agent under section 3504, which notifies IRS of the transfer agent relationship.
Transmitter	Person or organization preparing magnetic diskette file(s). May be Payer or agent of Payer.
Transmitter Control Code (TCC)	A *five* character alpha/numeric number assigned by IRS to the transmitter prior to actual filing on magnetic media. This number is inserted in the "A" Record of your files and *must* be present before the file can be processed. An application Form 4419 must be filed with IRS to receive this number. See Part A, Sec. 5. (Abbreviation for this term is TCC.)

SEC. 16. U.S. POSTAL SERVICE STATE AND COUNTRY ABBREVIATIONS

.01 You *MUST* use the following U.S. Postal Service state abbreviations and foreign country codes when developing the state code portion of address fields. (This table provides state abbreviations only and does not represent those states participating in the Combined Federal/State Program. For a list of states that participate in the Combined Federal/State Program, refer to Part A, Sec. 14.10.)

State	Code	State	Code	State	Code
Alabama	AL	Kentucky	KY	North Dakota	ND
Alaska	AK	Louisiana	LA	Ohio	OH
Arizona	AZ	Maine	ME	Oklahoma	OK
Arkansas	AR	Maryland	MD	Oregon	OR
California	CA	Massachusetts	MA	Pennsylvania	PA
Colorado	CO	Michigan	MI	Rhode Island	RI
Connecticut	CT	Minnesota	MN	South Carolina	SC
Delaware	DE	Mississippi	MS	South Dakota	SD
District of Columbia	DC	Missouri	MO	Tennessee	TN
Florida	FL	Montana	MT	Texas	TX
Georgia	GA	Nebraska	NE	Utah	UT
Hawaii	HI	Nevada	NV	Vermont	VT
Idaho	ID	New Hampshire	NH	Virginia	VA
Illinois	IL	New Jersey	NJ	Washington	WA
Indiana	IN	New Mexico	NM	West Virginia	WV
Iowa	IA	New York	NY	Wisconsin	WI
Kansas	KS	North Carolina	NC	Wyoming	WY

.02 The following list represents Canadian Provinces and the corresponding code to be associated with each.

Province	Code	Province	Code	Province	Code
Alberta	AB	British Columbia	BC	Labrador	LB
Manitoba	MB	Nova Scotia	NS	New Brunswick	NB
Newfoundland	NF	Prince Edward Island	PE	Northwest Territories	NT
Ontario	ON			Saskatchewan	SK
Quebec	PQ				
Yukon Territories	YK				

.03 The following list represents foreign countries and the corresponding code to be associated with each.

Foreign Country	Code	Foreign Country	Code	Foreign Country	Code
Afghanistan	AF	Barbados	BB	Bulgaria	BU
Albania	AL	Belgium	BE	Burma	BM
Algeria	AG	Belize (Formerly British Honduras)	BH	Burundi	BY
American Samoa	AQ	Benin (Formerly Dahomey)	DM	Cambodia	CB
Andorra	AN	Bermuda	BD	Cameroon	CM
Angola	AO	Bhutan	BT	Canada	CA
Antarctica	AY	Bolivia	BL	Canton & Enderbury Islands	EQ
Antigua & Barbuda	AC	Botswana	BC	Canary Islands	SP
Argentina	AR	Brazil	BR	Cape Verde, Republic of	CV
Australia	AS	British Indian Ocean Territory	IO	Cayman Islands	CJ
Austria	AU	British Virgin Islands	VI	Central Africa Republic	CT
Azores	PO	Brunei	BX	Chad	CD
Bahamas, The	BF			Channel Islands	OC
Bahrain	BA			Chile	CI
Bangladesh	BG				

Foreign Country	Code
China (Peking)	CH
China (Taiwan)	TW
Christmas Island	KT
Cocos (Kneeling) Islands	CK
Colombia	CO
Comoros	CN
Congo	CF
Cook Islands	CW
Costa Rica	CS
Cuba	CU
Cyprus	CY
Czechoslovakia	CZ
Denmark	DA
Djibouti (Formerly Afars & Issas)	DJ
Dominica	DO
Dominican Republic	DR
Ecuador	EC
Egypt	EG
El Salvador	ES
England	UK
Equatorial Guinea	EK
Ethiopia	ET
Falkland Islands (Also known as Islas-Malvinas)	FA
Faroe Islands	FO
Fiji	FJ
Finland	FI
France	FR
French Guiana	FG
French Polynesia	FP
French Southern & Antarctic Lands	FS
Gabon	GB
Gambia, The	GA
German Democratic Republic (East Germany)	GC
Germany, Federal Republic of (West Germany)	GE
Ghana	GH
Gibraltar	GI
Gilbert Islands	GS
Greece	GR
Greenland	GL
Grenada	GJ
Guadeloupe	GP
Guam	GQ
Guatemala	GT
Guinea	GV
Guinea-Bissau	PU
Guyana	GY
Haiti	HA
Heard Island & McDonald Island	HM
Honduras	HO

Foreign Country	Code
Hong Kong	HK
Hungary	HU
Iceland	IC
India	IN
Indonesia	ID
Iran (Also known as Persia)	IR
Iraq	IZ
Ireland	EI
Isle of Man	OC
Israel	IS
Italy	IT
Ivory Coast	IV
Jamaica	JM
Japan	JA
Johnston Atoll	JQ
Jordan	JO
Kenya	KE
Korea, Democratic Peoples Republic of (North Korea)	KN
Korea, Republic of (South Korea)	KS
Kuwait	KU
Laos	LA
Lebanon	LE
Lesotho	LT
Liberia	LI
Libya	LY
Liechtenstein	LS
Luxembourg	LU
Macao	MC
Madagascar	MA
Malawi	MI
Malaysia	MY
Maldives	MV
Mali	ML
Malta	MT
Martinique	MB
Mauritania	MR
Mauritius	MP
Mexico	MX
Midway Islands	MQ
Monaco	MN
Mongolia	MG
Montserrat	MH
Morocco	MO
Mozambique	MZ
Nauru	NR
Navassa Island	BQ
Nepal	NP
Netherlands (Also called Holland)	NL
Netherlands Antilles	NA
New Caledonia	NC
Vanuata (Also called New Hebrides)	NH
New Zealand	NZ

Foreign Country	Code
Nicaragua	NU
Niger	NG
Nigeria	NI
Niue	NE
Norfolk Islands	NF
Northern Ireland	UK
Norway	NO
Oman	MU
Pakistan	PK
Panama	PN
Papua-New Guinea	PP
Paracel Islands	PF
Paraguay	PA
Peru	PE
Philippines	RP
Pitcairn	PC
Poland	PL
Portugal	PO
Portuguese Timor	PT
Puerto Rico	RQ
Qatar	QA
Reunion	RE
Romania	RO
Rwanda	RW
St. Christopher-Nevis-Anguilla (Also called St. Kitts)	SC
St. Helena	SH
St. Lucia	ST
St. Pierre & Miquelon	SB
St. Vincent	VC
San Marino	SM
Sao Tome and Principe	TP
Saudi Arabia	SA
Scotland	UK
Senegal	SG
Seychelles	SE
Sierra Leone	SL
Singapore	SN
Solomon Islands	BP
Somalia	SO
South Africa	SF
Southern Rhodesia	RH
South-West Africa (Also called Namibia)	WA
Spain	SP
Spratly Islands	PG
Sri Lanka (Also called Ceylon)	CE
Sudan	SU
Surinam	NS
Svalbard & Jan Mayen	JS
Swaziland	WZ
Sweden	SW
Switzerland	SZ
Syria	SY
Tanzania	TZ
Thailand	TH

Foreign Country	Code	Foreign Country	Code	Foreign Country	Code
Togo	TO	Uganda	UG	Virgin Islands of the U.S.	VQ
Tokelau Islands	TL	Union of Soviet Socialist Republics	UR	Wake Island	WQ
Tonga	TN	United Arab Emirates	TC	Wales	UK
Trinidad & Tobago	TD	United Kingdom	UK	Wallis & Futana	WF
Trust Territory of the Pacific Islands	TQ	United States	US	Western Samara	WI
Tunisia	TS	Upper Volta	UV	Western Samoa	WS
Turkey	TU	Uruguay	UY	Yemen (South)	YS
Turks & Caicos Islands	TK	Vatican City	VT	Yemen (North)	YE
Tuvalu (Also called Ellice Islands)	TV	Venezuela	VE	Yugoslavia	YO
		Vietnam	VM	Zaire	CG
				Zambia	ZA
				Zimbabwe	RH

PART B. 5¼ INCH DISKETTE SPECIFICATIONS

SECTION 1. GENERAL

.01 The specifications contained in this part of the revenue procedure define the required format and contents of the records to be included in the diskette file. These specifications must be adhered to unless deviations have been specifically granted by IRS.

.02 To be compatible, a diskette file must meet the following specifications:

(a) 5¼ inches in diameter

(b) data must be recorded in standard ASCII code

(c) records must be fixed length, 360 bytes per record

(d) delimiter characters comma (,) and carriage return/feed (cr/lf) must not be used

(e) diskettes must meet one of the following specifications:

Capacity	Tracks	Sides/Density	Sector Size	Operating System
1.2 mb	96tpi	ds/dd	512	MS/PC-DOS 3.0
360 kb	48tpi	ds/dd	512	MS/PC-DOS 2.X
320 kb	48tpi	ds/dd	512	MS/PC-DOS 1.X
180 kb	48tpi	ss/dd	512	MS/PC-DOS 2.X
160 kb	48tpi	ss/dd	512	MS/PC-DOS 1.X

NOTE: If you use a 5¼ inch diskette format not listed above but feel it may be compatible, see Part A, Sec. 5.04 for instructions on sending a "*test*" diskette to IRS. No effort will be made to convert and process non-compatible diskettes. An IBM PC/XT, PC/AT, 3270 PC or compatible PC equipment should produce an acceptable diskette.

.03 Deviations from the prescribed formats will not be acceptable. Under no circumstances may diskettes deviating from the specifications in this revenue procedure be submitted without prior approval from IRS. If you file under the Combined Federal/State Program, your files must conform totally to this revenue procedure.

.04 An external affixed label, Form 5064, must appear on each diskette submitted for processing. The following information is needed:

(a) The transmitter's name.

(b) The five character alpha/numeric Transmitter Control Code.

(c) State of sender (*e.g.*, NY).

(d) Tape density (for magnetic tape filers only).

(e) Checkbox (for magnetic tape filers only).

(f) Track (for magnetic tape filers only).

(g) Recording code (enter ASCII).

(h) The tax year of the data (*e.g.*, 1986).

(i) Document types (*e.g.*, 1099-INT).

(j) The total number of "B" Records after each "A" Record (this figure is taken from the "C" Records).

(k) A number assigned by the transmitter to the diskette.

(l) The sequence of each diskette (*e.g.*, 001 of 008).

.05 The external media label, Form 5064, was updated for tax year 1986. You must use the updated label. This information will assist IRS in processing the file or in locating a file, should the transmitter request that it be returned due to errors. *IRS advises that special shipping containers not be used for transmitting data since it cannot be guaranteed that they will be returned.*

SEC. 2. DISKETTE HEADER LABEL

.01 The header label on the diskette must be formatted as shown in the following layout:

HDR1	BLANK	DATA SET NAME (FOR TRANSMITTER'S USE)	BLANK	SECTOR LENGTH	BLANK	BEGINNING OF EXTENT (BOE)
(a)	(b)	(c)	(b)	(d)	(b)	(e)
1-4	5	6-13	14-22	23-27	28	29-33

BLANK	END OF EXTENT (EOE)	BLANK	BYPASS DATA SET	DATA SET ACCESSIBILITY	WRITE PROTECT	BLANK
(b)	(f)	(b)	(g)	(h)	(i)	(b)
34	35-39	40	41	42	43	44

MULTI-VOLUME	BLANK	EXPIRATION DATE YYMMDD	VERIFY MARK	BLANK	END OF DATA
(j)	(b)	(k)	(l)	(b)	(m)
45	46-66	67-72	73	74	75-79

(a) Header 1—Positions 1 through 4; enter HDR1.

(b) Unused—Any field marked blank is unused and should contain only blanks.

(c) Data Set Name—Positions 6 through 13; you can use this field to identify your data set.

(d) Sector Length—Positions 23 through 27; enter the sector length 512, right-justify and fill positions 23 and 24 with zeros.

(e) Beginning of Extent (BOE)—Positions 29–33; enter the five-digit address designated for the first record of this data set. For example, if the first record is to go in track 01, sector 02, enter 01002, or xx0yy where xx is the track number and yy is the sector number.

(f) End of Extent (EOE)—Positions 35 through 39; enter the five-digit address of the last position of the disk reserved for this data set. For example, to reserve the entire disk for a data set, enter 73026.

(g) Bypass Data Set—Position 41; enter B if you want to bypass this data set; otherwise, enter a blank.

(h) Data Set Accessibility—Position 42, enter a blank. Any other character in this field causes the equipment to refuse the disk.

(i) Write Protect—Position 43; this field defines the protected status of the associated data set. P = read only; blank = read/write. With P in this position, you can only select the Update (U) mode.

(j) Multi-Volume—Position 45; this field indicates whether a complete data set is on a disk. Blank = data set complete; C = data set continued on another disk; L = last disk of a multi-disk data set.

(k) Expiration Date—Positions 67 through 72; may be used to contain the date that the data set expires. The format is YYMMDD where YY is the year; MM is the month and DD is the day.

(l) Verify Mark—Position 73; this single character field shows if the data set is verified. If it is, enter V, if it is not verified, enter a blank.

(m) End of Data (EOD)—Positions 75–79; enter the track number in positions 75 and 76, enter a "0" (zero) in position 77 and enter the sector number in positions 78 and 79.

SEC. 3. PAYER/TRANSMITTER "A" RECORD

.01 Identifies the payer and transmitter of the diskette file and provides parameters for the succeeding Payee "B" Records. IRS computer programs rely on the absolute relationship between the parameters and data fields in the "A" Record and the data fields in the "B" Records to which they apply.

.02 The number of "A" Records appearing on a diskette will depend on the number of payers and the different types of returns being reported. After the header label on the diskette, the first record appearing in the file must be an "A" Record. For magnetic diskette filing, the *actual* record lengths for the "A" and "B" Records must be 360 positions. A transmitter may include Payee "B" Records for more than one payer on a diskette; however, each GROUP of Payee "B" Records must be preceded by an "A" Record. A single diskette may also contain different types of returns, but the types of returns *must* not be intermingled. A separate "A" Record is required for each payer and each type of return being reported.

.03 All alpha characters entered in the "A" Record should be uppercase.

.04 *WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*

RECORD NAME: PAYER/TRANSMITTER "A" RECORD

Diskette Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "A".
2	Payment Year	1	REQUIRED. Must be the right most digit of the year for which information is being reported. (*e.g.*, if payments were made in 1986, enter "6".) Must be incremented each year.
3-5	Diskette Sequence Number	3	REQUIRED. The diskette sequence number incremented by 1, for each diskette on the file starting with 001 (Blanks are acceptable or all zeros.)
6-14	Payer's Federal EIN	9	REQUIRED. Must be the *valid* 9-digit number assigned to the payer by IRS. DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS. (Also see Part A, Sec. 11.07.)
15	Blank	1	REQUIRED. Enter Blank.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
16	Combined Federal/State Filer	1	REQUIRED. Enter the appropriate code from the table below. *Prior approval* is required. A consent Form 6847 *must* be submitted to IRS before tax information will be released to the states. Refer to Part A, Sec. 14.11 for money criteria. Not all states participate in this program. If the Payer/Transmitter is not participating in the Combined Federal/State Filing Program, enter blanks. (Refer to Part A, Sec. 14 for the requirements that *must* be met *prior* to actual participation in this program.) Forms 1098, 1099–A, 1099–B, and W–2G cannot be filed on this program. Filers who participate in this program must incorporate state totals into corresponding "K" Records as described in Part B, Sec. 15. *Code* — *Meaning* 1 — Participating in the Combined Federal/State Filing Program. Blank — Not participating.
17	Type of Return	1	REQUIRED. Enter appropriate code from table below: *Type of Return* — *Code* 1098 — 3 1099–A — 4 1099–B — B 1099–DIV — 1 1099–G — F 1099–INT — 6 1099–MISC — A 1099–OID — D 1099–PATR — 7 1099–R — 9 5498 — L W–2G — W
18-26	Amount Indicators	9	REQUIRED. *In most cases, the boxes or Amount Indicators on paper information returns correspond with the Amount Codes used to file on magnetic media; however, should you notice discrepancies between this revenue procedure and paper forms, please disregard them and program according to this revenue procedure for your returns filed on magnetic media.* For specific instructions on information to be reported in each Amount Code, refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G." The amount indicators entered for a given type of return indicate type(s) of payment(s) which were made. For each Amount Code entered in this field, a corresponding payment amount must appear in the Payee "B" Record. Example: If position 17 of the Payer/Transmitter "A" Record is "7" (for 1099–PATR) and positions 18-26 are "247bbbbbb," this indicates that 3 actual payment amounts are present in all of the following Payee "B" Records. The first payment amount in the Payee "B" Record will represent Nonpatronage distributions, the second will represent Federal income tax withheld, and the third will repre-Energy investment credit.
	Amount Indicators (continued)		Enter the Amount Indicators in ASCENDING SEQUENCE (*i.e.*, 247bbbbbb), left-justify, filling unused positions with blanks. For any further clarification of the Amount Indicator codes, you may contact the National Computer Center.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks	
	Amount Indicators Form 1098—Mortgage Interest Statement		For Reporting Interest Received from Payers on Form 1098:	
			Amount Code	Amount Type
			1	Mortgage interest received from payer(s)
			2	Optional field for items such as real estate taxes or insurance paid from escrow.

NOTE: THE PERSON FOR WHOM YOU ARE RECEIVING THE INTEREST NEED NOT FILE FORM 1098, AND NO ADDITIONAL REPORTING IS REQUIRED FOR THE TRANSFER OF THE INTEREST FROM THE SERVICING BANK TO THE LENDER.

Diskette Position	Field Title	Length	Description and Remarks	
	Amount Indicators Form 1099–A—Acquisition or Abandonment of Secured Property		For Reporting the Acquisition or Abandonment of Secured Property on Form 1099–A:	
			Amount Code	Amount Type
			2	Amount of debt outstanding
			3	Amount of debt satisfied
			4	Fair market value of property at acquisition or abandonment
	Amount Indicators Form 1099–B—Proceeds From Broker and Barter Exchange Transactions		For Reporting Payments on Form 1099–B:	
			Amount Code	Amount Type
			2	Stocks, bonds, etc. (For Forward Contracts see NOTE below.)
			3	Bartering
			4	Federal income tax withheld
			6	Profit or (loss) realized in 1986
			7	Unrealized profit or (loss) on open contracts—12/31/85
			8	Unrealized profit or (loss) on open contracts—12/31/86
			9	Aggregate profit or (loss)

NOTE: The Payment Amount field associated with Amount Code 2 may be used to represent a loss when the reporting is for Forward Contracts. Refer to Payee "B" Record-General Field Descriptions, Payment Amount Fields, for instructions in reporting negative amounts.

Diskette Position	Field Title	Length	Description and Remarks	
	Amount Indicators Form 1099–DIV—Dividends and Distributions		For Reporting Payments on Form 1099–DIV:	
			Amount Code	Amount Type
			1	Gross dividends and other distributions on stock
			2	Dividends qualifying for exclusion
			3	Dividends not qualifying for exclusion
			4	Federal income tax withheld
			5	Capital gain distributions
			6	Nontaxable distributions (if determinable)
			7	Foreign tax paid
			8	Cash liquidation distributions
			9	Noncash liquidation distributions (Show fair market value)
	Amount Indicators Form 1099–G—Certain Government Payments		For Reporting Payments on Form 1099–G:	
			Amount Code	Amount Type
			1	Unemployment compensation
			2	State or local income tax refunds
			4	Federal income tax withheld

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
			5 Discharge of indebtedness 6 Taxable grants 7 Agriculture payments
	Amount Indicators Form 1099–INT—Interest Income		For Reporting Payments on Form 1099–INT:

Amount Code	Amount Type
1	Earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposit, etc.
2	Amount of forfeiture
3	Federal income tax withheld
4	Foreign tax paid (if eligible for foreign tax credit)
5	U.S. Savings Bonds, etc.

Diskette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–MISC—Miscellaneous Income (See Notes 1, 2 and 3)		For Reporting Payments on Form 1099–MISC:

Amount Code	Amount Type
1	Rents
2	Royalties
3	Prizes and awards
4	Federal income tax withheld
5	Fishing boat proceeds
6	Medical and health care payments
7	Nonemployee compensation
8	Direct sales "*indicator*" (see NOTE 1)
9	Substitute payments in lieu of dividends or interest (see NOTE 2)

NOTE 1: Use Amount Code "8" to report that *direct sales* of consumer products of $5,000 or more to the payee on a buy-sell, deposit-commission, or any other basis *for resale* were made. (Do not use this indicator for sales of less than $5,000.) The use of Amount Code "8" actually reflects an *indicator of direct sales* and not an actual payment amount or amount code. The corresponding payment amount field in the Payee "B" Record MUST be reflected as 0000000100. This does not mean that a payment of $1.00 was made or is being reported. The use of Amount Code "8" relates directly to diskette position "4," Document Specific Code and NOTE 2 of the Payment Amount Field in the Payee "B" Record. (If you use Amount Code "8" in the "A" Record, you will enter a "1" in diskette position "4" of the "B" Record. For any other 1099–MISC Amount Codes, you will enter a "0" (zero) in diskette position "4" of the "B" Record.)

NOTE 2: Brokers are subject to a reporting requirement for payments received after 1984. Brokers who transfer securities of a customer for use in a short sale must use Amount Code 9 to report the aggregate payments received in lieu of dividends or tax-exempt interest on behalf of a customer while the short sale was open. Generally, for substitute payments in lieu of dividends, a broker is required to file a Form 1099–MISC for each affected customer who is *not* an individual. Refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W-2G" for detailed information. The instructions are available from IRS offices.

NOTE 3: If you are reporting Excess Golden Parachute Payments, use paper forms 1099–MISC. Do not report these payments on magnetic media. See Part A, Sec. 15 for a definition of an Excess Golden Parachute Payment.

Diskette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–OID—Original Issue Discount		For Reporting Payments on Form 1099–OID:

Amount Code	Amount Type
1	Total original issue discount for 1986
2	Other periodic interest (the regular interest paid on this obligation without regard to any original issue discount)
3	Amount of forfeiture
4	Federal income tax withheld

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks	
	Amount Indicators Form 1099–PATR—Taxable Distributions Received From Cooperatives		For Reporting Payments on Form 1099–PATR:	
			Amount Code	Amount Type
			1	Patronage dividends
			2	Nonpatronage distributions
			3	Per-unit retain allocations
			4	Federal income tax withheld
			5	Redemption of nonqualified notices and retain allocations
			6	Investment credit (See NOTE)
			7	Energy investment credit (See NOTE)
			8	Jobs credit (See NOTE)

NOTE: The amounts shown for Amount Indicators "6," "7" and "8" must be reported to the payee; however, since these amounts are not taxable, they need not be reported to IRS.

Diskette Position	Field Title	Length	Description and Remarks	
	Amount Indicators Form 1099–R—Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc. (See NOTE)		For Reporting Payments on Form 1099–R:	
			Amount Code	Amount Type
			1	Amount includible as income (add amounts in codes 2 and 3)
			2	Capital gain (for lump-sum distributions only)
			3	Ordinary income
			4	Federal income tax withheld
			5	Employee contributions (profit-sharing or retirement plans) or insurance premiums
			6	IRA, SEP or DEC distributions
			7	State income tax withheld
			8	Net unrealized appreciation in employer's securities
			9	Other

NOTE: A distribution from a KEOGH plan should be reported in Amount Codes 1, 2, and 3 as appropriate.

Diskette Position	Field Title	Length	Description and Remarks	
	Amount Indicators Form 5498—Individual Retirement Arrangement Information		For Reporting Payments on Form 5498:	
			Amount Code	Amount Type
			1	Regular SEP contributions made in 1986 and 1987 for 1986. Include only employer contributions here. Enter any employee contributions to a SEP in Code 3.
			2	Rollover IRA, SEP or DEC contributions
			3	Regular IRA or DEC contributions made in 1986 and 1987 for 1986
			4	Life insurance cost included in code 1 or 3 (for endowment contracts only)

NOTE: Form 5498 is filed for contributions to be applied to 1986 that are made between January 1, 1986, and April 15, 1987.

Diskette Position	Field Title	Length	Description and Remarks	
	Amount Indicators Form W–2G—Certain Gambling Winnings		For Reporting Payments on Form W–2G:	
			Amount Code	Amount Type
			1	Gross winnings
			2	Federal income tax withheld
			3	State income tax withheld
			7	Winnings from identical wagers
27	Blank	1	REQUIRED. Enter blank.	

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
28-30	"A" Record Length	3	REQUIRED. Enter 360 (the number of positions used for the "A" Record).
31-33	"B" Record Length	3	REQUIRED. Enter 360 (the number of positions used for the "B" Record.)
34	Blank	1	REQUIRED. Enter blank.
35-39	Transmitter Control Code (TCC)	5	REQUIRED. Enter the five character alpha/numeric Transmitter Control Code assigned by IRS. See Part A, Sec. 15 for a definition of Transmitter Control Code (TCC). You must have a TCC to file *actual* data on this program.
40	Blank	1	REQUIRED. Enter blank.
41-80	First Payer Name	40	REQUIRED. Must be present or files will be returned for correction. Enter the name of the payer in the manner in which it is used in normal business. Any extraneous information must be deleted from the name line. Left-justify and fill with blanks. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
81-119	Second Payer Name	39	REQUIRED. The contents of this field are dependent upon the TRANSFER AGENT INDICATOR in position 120 of this record. If the Transfer Agent Indicator contains a "1," this field will contain the name of the Transfer Agent. If the Transfer Agent Indicator contains a "0" (zero), this field will contain either a continuation of the First Payer Name field or blanks. Left-justify and fill unused positions with blanks. IF NO ENTRIES ARE PRESENT FOR THIS FIELD FILL WITH BLANKS. (See Part A, Sec. 15 for a definition of Transfer Agent.)
120	Transfer Agent Indicator	1	REQUIRED. Identifies the entity in the Second Payer Name field. (See Part A, Sec. 15 for a definition of Transfer Agent.) *Code* — *Meaning* 1 — The entity in the Second Payer Name field is the Transfer Agent. 0 (zero) — The entity shown is *not* the Transfer Agent (*i.e.*, the Second Payer Name field contains either a continuation of the First Payer Name field or blanks).
121-160	Payer Shipping Address	40	REQUIRED. If the TRANSFER AGENT INDICATOR in position 120 is a "1" enter the shipping address of the Transfer Agent. Otherwise, enter the shipping address of the payer. Left-justify and fill with blanks.
161-200	Payer City, State and ZIP Code	40	REQUIRED. If the TRANSFER AGENT INDICATOR in position 120 is a "1" enter the City, State and ZIP Code of the Transfer Agent. Otherwise, enter the City, State and ZIP Code of the payer. Left-justify and fill with blanks.
201-280	Transmitter Name	80	REQUIRED. Enter the name of the transmitter in the manner in which it is used in normal business. The name of the transmitter *must* be constant through the entire file. Left-justify and fill with blanks.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
281-320	Transmitter Mailing Address	40	REQUIRED. Enter the mailing address of the transmitter. Left-justify and fill with blanks.
321-360	Transmitter City, State and ZIP Code	40	REQUIRED. Enter the City, State, and ZIP Code of the transmitter. Left-justify and fill with blanks.

SEC. 4. PAYER/TRANSMITTER "A" RECORD—RECORD LAYOUT

RECORD TYPE	PAYMENT YEAR	DISKETTE SEQUENCE NUMBER	PAYER'S FEDERAL EIN	BLANK	COMBINED FEDERAL/STATE FILER	TYPE OF RETURN
1	2	3-5	6-14	15	16	17

AMOUNT INDICATORS	BLANK	"A" RECORD LENGTH	"B" RECORD LENGTH	BLANK	TRANSMITTER CONTROL CODE	BLANK	FIRST PAYER NAME	SECOND PAYER NAME
18-26	27	28-30	31-33	34	35-39	40	41-80	81-119

TRANSFER AGENT INDICATOR	PAYER SHIPPING ADDRESS	PAYER CITY, STATE AND ZIP CODE	TRANSMITTER NAME	TRANSMITTER MAILING ADDRESS	TRANSMITTER CITY, STATE AND ZIP CODE
120	121-160	161-200	201-280	281-320	321-360

SEC. 5. PAYEE "B" RECORD—GENERAL FIELD DESCRIPTIONS

.01 The Payee "B" Record contains the payment information from the individual statements. When filing information documents on 5 ¼ inch diskette(s), the format for the Payee "B" Records will remain constant. There are nine payment amount fields in the "B" Record. In those amount fields where no money amount is to be reported, enter zeros. For example, if you are reporting 1099-PATR, position 17 of the Payer/Transmitter "A" Record will be coded with a "7". If the Amount Indicators used to report these dividends are Amount Codes "2," "4," and "7," then diskette positions 18-26 of the "A" Record will be coded "247bbbbbb" (b represents a *blank* position). To correspond with Amount Indicators "2," "4," and "7," of the "A" Record, the "B" Record will contain three actual payment amounts. Diskette positions 31-40 of the "B" Record will contain the payment amount to be reported for Amount Code "2" (Nonpatronage distributions); diskette positions 41-50 of the "B" Record would contain the payment amount to be reported for Amount Code "4" (Federal income tax withheld); and diskette positions 51-60 of the "B" Record would contain the payment amount to be reported for Amount Code "7" (Energy investment credit). Positions 61 through 120 must be zero filled. The First Payee Name Line will always begin in diskette position 121.

.02 All records must be a fixed length of 360 positions.

.03 All payee records *must contain correct payee name and address information* entered in the fields prescribed in this section. Records containing an invalid TIN (SSN or EIN) and having no address data present may be returned for correction. In searching for a payee address, if your efforts fail and you know that the address is invalid, supply the invalid address rather than leave the field blank.

.04 IRS must be able to identify the surname associated with the TIN (SSN or EIN) furnished on a statement. The specifications below include a field in the payee records called "Name Control" in which the first four alphabetic characters of the payee's surname or last name are to be entered by the payers. The surname or last name should appear first in the First Payee Name Line of all Payee "B" Records; however, if your records have been developed using the first name first, IRS programs will accept this but a blank must appear between the first and last name.

.05 If payers are unable to provide the first four characters of the surname, the Name Control Field may be left blank; however, compliance with the following will facilitate IRS computer programs in generating the Name Control.

(a) The surname of the payee whose TIN (SSN or EIN) is shown in the Payee "B" Record should always appear first. If, however, you enter the first name first, you must leave a blank space between the first and last name.

(b) In the case of multiple payees, only the surname of the payee whose TIN (SSN or EIN) is shown in the Payee "B" Record, must be present in the First Payee Name Line. Surnames of any other payees in the record must be entered in the Second Payee Name Line.

.06 Provision is also made in these specifications for data entries required by state or local governments. This should minimize the Payer/Transmitter's programming burden should payers desire to report on diskette to state or local governments. See Part A, Sec. 14, for the Combined Federal/State filing requirements.

.07 For those filers participating in the Combined Federal/State Filing Program, positions 359 and 360 in the Payee "B" Records must contain the appropriate state code for the state to receive the information. The file should also meet the money criteria described in Part A, Sec. 14.11. Do not code for the states unless prior approval to participate has been granted by IRS. See Part A, Sec. 14 for a list of the valid participating state codes. *FORMS 1098, 1099–A, 1099–B, AND W–2G CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.* Your files must meet all of the requirements specified in Part A, Sec. 14.10 in order to participate in this progam.

.08 All alpha characters entered in the "B" Record should be upper-case.

.09 *IRS STRONGLY ENCOURAGES FILERS TO REVIEW THEIR DATA FOR ACCURACY BEFORE SUBMISSION TO PREVENT ERRONEOUS NOTICES TO PERSONS FOR WHOM REPORTS ARE FILED. FILERS SHOULD BE ESPECIALLY CAREFUL THAT THEIR TAXPAYER NAMES, SOCIAL SECURITY NUMBERS (SSNs), ACCOUNT NUMBERS, TYPES OF INCOME, AND INCOME AMOUNTS ARE CORRECT. ALTHOUGH IRS ENCOURAGES PAYERS TO FILL IN THE PAYER'S ACCOUNT NUMBER FOR THE PAYEE FIELD, THEY SHOULD NOT INCLUDE EXTRANEOUS DIGITS AS THIS FIELD IS LIMITED, IN MAGNETIC MEDIA FILING, TO 10 POSITIONS.*

.10 *WHEN REPORTING FORM 1098 "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*

RECORD NAME: PAYEE "B" RECORD

Diskette Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "B".
2-3	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported (*e.g.*, if payments were made in 1986 enter "86"). Must be incremented each year.
4-5	Document Specific Code (In prior years, position 5 was used as a corrected return indicator. This position was needed for the Document Specific Code. Position 6 now represents a corrected return.)	2	REQUIRED for Forms 1099–R, 1099–MISC, 1099–G, and W–2G. For *Form 1099–R*, enter the appropriate code for the Category of Total Distribution. For *Form 1099–MISC*, enter the appropriate code for Direct Sales. For *Form 1099–G*, enter the year of income tax refund. For *Form W–2G* enter the Type of Wager. FOR ALL OTHER FORMS, ENTER BLANK. If only one code is used, left-justify and blank fill.
	Category of Total Distribution (Form 1099–R only)		Use only for reporting on *Form 1099–R* to identify the Category of Total Distribution. You may select two codes except when using Code 9. Enter the applicable code from the table below. Code 7 below is *not required* for Amount Indicators 1, 2 and 3. A "0" (zero) is not a valid code for Form 1099–R. If you are reporting a distribution from a KEOGH plan, or from any other distribution, to which the following codes do not apply, enter blanks in this field.

Category	*Code*
Premature distribution (other than codes 2, 3, 4, 5, 8, or P)	1
Rollover	2
Disability	3
Death (includes payments to a beneficiary)	4
Prohibited transaction	5
Other	6
Normal IRA, SEP or DEC distributions	7
Excess contributions refunded plus earnings on such excess contributions	8
PS 58 Costs (See NOTE)	9
Excess contributions refunded plus earnings on such excess contributions taxable in 1985	P

RECORD NAME: PAYEE "B" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
			Qualifies for 10-year, averaging A Qualifies for death benefit exclusion B Qualifies for *both* A and B C
			NOTE: PS 58 Costs may be reported on Form 1099–R; however, Form W–2P (filed with SSA) is preferable. Since this is not actually a total distribution, a separate "B" Record is required to report PS 58 Costs. These costs may not be reported in combination with a total distribution. Refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G," available from IRS offices.
	Direct Sales (Form 1099–MISC only)		Use only for direct sales reporting on *Form 1099–MISC*. If sales to the recipient of consumer products on a buy-sell, deposit-commission, or any other basis for resale, have amounted to $5,000 or more, ENTER "1". If you are filing 1099–MISC, with an Amount Indicator of "8" in the "A" Record, you must enter a code "1" in this field. For all other 1099–MISC Amount Codes in the "A" Record enter a "0" (zero) in this field. In Part B, Sec. 3, information concerning the direct sales indicator can be found under Amount Indicators, Form 1099–MISC, NOTE 1 in the "A" Record. This code should appear in position 4. Position 5 will be blank.
	Refund is for Tax Year (Form 1099–G only)		Use only for reporting the tax year for which the refund was issued. If the payment amount field associated with Amount Indicator 2, Income Tax Refunds, contains a refund, credit or offset that is attributable to an income tax that applies exclusively to income from a trade or business and is not of general application, then enter the ALPHA equivalent of the year of refund from the table below. Otherwise, enter the NUMERIC Year for which the Refund was issued. This code should appear in position 4. Position 5 will be blank. *Year for which Refund was Issued* *Alpha Equivalent* 1 A 2 B 3 C 4 D 5 E 6 F 7 G 8 H 9 I 0 J
	Type of Wager (Form W–2G only)		Use only for reporting the Type of Wager on *Form W–2G*. This code will appear in position 4. Position 5 will be blank. *Category* *Code* Horse Race Track (or Off Track Betting of a Horse Track nature) 1 Dog Race Track (or Off Track Betting of a Dog Track nature) 2 Jai-alai 3 State Conducted Lottery 4 Keno 5 Casino Type Bingo. DO NOT use this code for any other type of Bingo winnings (*i.e.*, Church, Fire Dept., 6

RECORD NAME: PAYEE "B" RECORD—Continued

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td></td><td></td><td></td><td>etc.).
<table>
<tr><td>Slot Machines</td><td>7</td></tr>
<tr><td>Any other types of gambling winnings. This includes Church Bingo, Fire Dept., Bingo, unlabeled winnings, etc.</td><td>8</td></tr>
</table></td></tr>
<tr><td>6</td><td>Blank or Corrected Return Indicator</td><td>1</td><td>REQUIRED. Enter blank. (Reserved for IRS use). Diskette position 6 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using magnetic media. IN PRIOR YEARS, POSITION 5 WAS USED AS THE CORRECTED RETURN INDICATOR. THIS HAS NOW CHANGED TO POSITION 6. YOU MUST ADJUST YOUR PROGRAMS.</td></tr>
<tr><td>7-10</td><td>Name Control</td><td>4</td><td>REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (–) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the Name Control:
<table>
<tr><th><i>Name</i></th><th><i>NAME CONTROL</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE*</td></tr>
<tr><td>James P. En Sr.</td><td>EN*</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must be left-justified and blank filled.</td></tr>
<tr><td>11</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identification Number (TIN) in positions 12-20 as either an Employer Identification Number, a Social Security Number, or the reason no number is shown. Enter the appropriate code from the following table.
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, enter a blank. If a number is unobtainable due to legitimate cause; <i>e.g.</i>, number applied for but not received, enter a blank.</td></tr>
</table></td></tr>
<tr><td>12-20</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the payee (SSN or EIN, as appropriate). Where an identification number has been applied for but not received or</td></tr>
</table>

RECORD NAME: PAYER "B" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
			where there is any other legitimate cause for not having an identification number, *enter blanks*. Refer to Part A, Sec. 11. *DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS.* Any record containing an invalid identifying number in this field will be returned for correction.
21-30	Payer's Account Number for Payee	10	REQUIRED. Payer may use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payer's file should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. An account number can be any account number assigned by the payer to the payee (*i.e.*, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any number that will help identify the particular transaction that you are reporting. If a number is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.
	Payment Amount Fields (Must be numeric)		The number of *actual* payment amounts is dependent upon the number of Amount Indicators present in positions 18-26 of the "A" Record. For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in position 18 of the Payer/Transmitter "A" Record, then you will actually enter one, ten position, right-justified payment amount in Payment Amount 1, positions 31-40 of the "B" Record. The remaining eight, ten position payment amounts, Payment Amounts 2 through 8, will be zero filled. The First Payee Name Line will always begin in position 121. Each payment field must contain 10 numeric characters (see NOTE 1). Enter zeros in the payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS* (except those items that reflect a loss on Form 1099–B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "247bbbbbb," the Payee "B" Records will have only 3 *actual* payment amounts entered in Payment Amount 1, 2 and 3. The remaining 6 payment amounts, Payment Amounts 4 through 9, will be zeros. If Amount Indicators in the "A" Record are reflected as "12367bbbb," the "B" Records will have only 5 *actual* payment amounts in Payment Amounts 1 through 5. The remaining 4 payment amounts, Payment Amount 6 through 9, will be zeros. Payment amounts MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE 1: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee.

RECORD NAME: PAYEE "B" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
			NOTE 2: If you file 1099–MISC and use Amount Code "8" in the Amount Indicator field of the Payer/Transmitter "A" Record, you must enter 0000000100 in the corresponding Payment Amount Field. This will not represent an actual money amount; this is an indicator of direct sales. (Refer to Part B, Sec. 3, NOTE 1, of the Amount Indicators, Form 1099–MISC, for clarification.)
31-40	Payment Amount 1	10	This amount is identified by the indicator in position 18 of the Payer/Transmitter "A" Record. *This amount must always be present.*
41-50	Payment Amount 2	10	This amount is identified by the indicator in position 19 of the Payer/Transmitter "A" Record. If position 19 is blank, enter zeros for this payment amount.
51-60	Payment Amount 3	10	This amount is identified by the indicator in position 20 of the Payer/Transmitter "A" Record. If position 20 is blank, enter zeros for this payment amount.
61-70	Payment Amount 4	10	This amount is identified by the indicator in position 21 of the Payer/Transmitter "A" Record. If position 21 is blank, enter zeros for this payment amount.
71-80	Payment Amount 5	10	This amount is identified by the indicator in position 22 of the Payer/Transmitter "A" Record. If position 22 is blank, enter zeros for this payment amount.
81-90	Payment Amount 6	10	This amount is identified by the indicator in position 23 of the Payer/Transmitter "A" Record. If position 23 is blank, enter zeros for this payment amount.
91-100	Payment Amount 7	10	This amount is identified by the indicator in position 24 of the Payer/Transmitter "A" Record. If position 24 is blank, enter zeros for this payment amount.
101-110	Payment Amount 8	10	The amount is identified by the indicator in position 25 of the Payer/Transmitter "A" Record. If position 25 is blank, enter zeros for this payment amount.
111-120	Payment Amount 9	10	This amount is identified by the indicator in position 26 of the Payer/Transmitter "A" Record. If position 26 is blank, enter zeros for this payment amount.
121-160	First Payee Name Line	40	REQUIRED. *Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 12-20 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required for the name, utilize the Second Payee Name Line field below. If there are multiple payees, only the name of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
161-200	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees, (*e.g.*, partners or joint owners) this field may be used for those payees' names who are not associated with the Taxpayer Identification Number provided in positions 12-20 above. *Do not enter*

RECORD NAME: PAYEE "B" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
			address information in this field. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
201-240	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
241-269	Payee City	29	REQUIRED. Enter the City, left-justified and fill the unused positions with blanks. *Do not enter State and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "241" of this field and spell out the name of the city in the remaining positions.)
270-271	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You MUST use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "241" of the Payee City field.
272-280	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "241" in the Payee City field is a "1."

PAYEE "B" RECORD — FORMS 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R AND 5498

NEXT FIELD AFTER PAYEE ZIP CODE:

Diskette Position	Field Title	Length	Description and Remarks
281-358	Special Data Entries	78	REQUIRED. This portion of the Payee "B" Record may be used to record information for state or local government reporting or for other purposes. Payers should contact their state or local revenue departments for their filing requirements. If this field is not utilized, ENTER BLANKS.
359-360	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states NOT participating in this program or for Form 1098, ENTER BLANKS.

SEC. 6. PAYEE "B" RECORD—RECORD LAYOUT FOR FORMS 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R AND 5498

RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK OR CORRECTED RETURN INDICATOR	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2-3	4-5	6	7-10	11	12-20

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
21-30	31-40	41-50	51-60	61-70	71-80	81-90

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8	PAYMENT AMOUNT 9	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY
91-100	101-110	111-120	121-160	161-200	201-240	241-269

PAYEE STATE	PAYEE ZIP CODE	SPECIAL DATA ENTRIES	STATE CODE
270-271	272-280	281-358	359-360

SEC. 7. PAYEE "B" RECORD — FORM 1099-A

.01 See Sec. 5 for the format to be followed for diskette positions 1-280.

.02 For detailed explanations of the following fields see the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W-2G" available at IRS offices.

RECORD NAME: PAYEE "B" RECORD
FORM 1099-A

NEXT FIELD AFTER PAYEE ZIP CODE:

Diskette Position	Field Title	Length	Description and Remarks
281	Blank	1	REQUIRED. Enter blank.
282-287	Lender's Date of Acquisition or Abandonment	6	REQUIRED *FOR FORM 1099-A ONLY*. Enter the date of your acquisition of the secured property or the date you first knew or had reason to know that the property was abandoned in the format MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.
288	Liability Indicator	1	REQUIRED *FOR FORM 1099-A ONLY*. Enter the appropriate indicator from table below: *Indicator* — *Usage* 1 — Borrower is personally liable for repayment of the debt. Blank — Borrower is *not* liable for repayment of the debt.
289-325	Description	37	REQUIRED *FOR FORM 1099-A ONLY*. Enter a brief description of the property. For example, for real property, enter the address, section, lot, and block. For personal property, enter the type, make and model (*e.g.*, Car-1986 Buick Regal or Office Equipment, etc.).
326-360	Blank	35	REQUIRED. Enter blanks.

SEC. 8. PAYEE "B"—RECORD LAYOUT FORM 1099–A

RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK OR CORRECTED RETURN INDICATOR	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2-3	4-5	6	7-10	11	12-20

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
21-30	31-40	41-50	51-60	61-70	71-80	81-90

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8	PAYMENT AMOUNT 9	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY
91-100	101-110	111-120	121-160	161-200	201-240	241-269

PAYEE STATE	PAYEE ZIP CODE	BLANK	LENDER'S DATE OF ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION	BLANK
270-271	272-280	281	282-287	288	289-325	326-360

SEC. 9. PAYEE "B" RECORD—FORM 1099–B

.01 See Sec. 5 for the format to be followed for diskette positions 1-280.

.02 For detailed explanations of the following fields see 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" available at IRS offices.

NEXT FIELD AFTER PAYEE ZIP CODE:

Diskette Position	Field Title	Length	Description and Remarks
281-317	Blank	37	REQUIRED. Enter Blanks.
318	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date Blank — Date of Sale is the trade date or this is an aggregate transaction
319-324	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
325-332	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. En-

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
			ter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
333-358	Description	26	REQUIRED *FORM FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
359-360	Blank	2	REQUIRED. Enter blanks.

SEC. 10. PAYEE "B" RECORD—RECORD LAYOUT FORM 1099–B

RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK OR CORRECTED RETURN INDICATOR	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2-3	4-5	6	7-10	11	12-20

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
21-30	31-40	41-50	51-60	61-70	71-80	81-90

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8	PAYMENT AMOUNT 9	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY
91-100	101-110	111-120	121-160	161-200	201-240	241-269

PAYEE STATE	PAYEE ZIP CODE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
270-271	272-280	281-317	318	319-324	325-332	333-358	359-360

SEC. 11. PAYEE "B" RECORD—FORM W–2G

.01 See Sec. 5 for the format to be followed for diskette positions 1-280.

.02 For detailed explanations of the following fields see the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" available at IRS offices.

NEXT FIELD AFTER PAYEE ZIP CODE:

Diskette Position	Field Title	Length	Description and Remarks
281-292	Blank	12	REQUIRED. Enter blanks.
293-298	Date Won	6	REQUIRED *FOR FORM W–2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.

RECORD NAME: PAYEE "B" RECORD—Continued
FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
299-313	Transaction	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number or any other information that will help identify the winning transaction. If no entry, enter blanks.
314-318	Race	5	REQUIRED *FOR FORM W-2G ONLY*. The race (or game) applicable to the winning ticket. If no entry, enter blanks.
319 323	Cashier	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
324-328	Window	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.
329-343	First ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
344-358	Second ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
359-360	Blank	2	REQUIRED. Enter blanks.

SEC. 12. PAYEE "B" RECORD—RECORD LAYOUT FORM W-2G

RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK OR CORRECTED RETURN INDICATOR	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2-3	4-5	6	7-10	11	12-20

PAYER'S ACCOUNT NUMBER OF PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
21-30	31-40	41-50	51-60	61-70	71-80	81-90

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8	PAYMENT AMOUNT 9	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY
91-100	101-110	111-120	121-160	161-200	201-240	241-269

PAYEE STATE	PAYEE ZIP CODE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER	WINDOW
270-271	272-280	281-292	293-298	299-313	314-318	319-323	324-328

PAYEE "B" RECORD—RECORD LAYOUT—Continued
FORM W-2G

FIRST ID	SECOND ID	BLANK
329-343	344-358	359-360

SEC. 13. END OF PAYER "C" RECORD

.01 The Control Total fields have been expanded from 12 to 15 positions.

.02 The End of Payer "C" Record is a summary record for a type of return for a given payer. It *MUST* be 360 positions in length.

.03 The "C" Record will contain the total number of payees and the totals of the payment amount fields filed by a given payer. The "C" Record must be written after the last Payee "B" Record for each type of return for a given payer. For each "A" Record and group of "B" Records on the file, there must be a corresponding "C" Record.

.04 In developing the "C" Record, for example, if you used Amount Codes 1, 3 and 6 in the "A" Record, the totals from the "B" Records will appear in Control Totals, 1, 2, and 3 of the "C" Record. Positions 53-142 would be zero filled and positions 143-360 would be blank filled.

.05 Payers/Transmitters must verify the accuracy of the totals in the "C" Record and must enter the totals on the transmittal, Form 4804, 4802 or computer generated substitute, which will accompany the shipment. The lines used on Forms 4804 and 4802 to record payment amounts correspond with the Amount Codes used in the "A" Record. These forms have been updated for 1986.

RECORD NAME: END OF PAYER "C" RECORD

Diskette Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "C."
2-7	Number of Payees	6	REQUIRED. Enter the total number of Payee "B" Records covered by the preceding Payer/Transmitter "A" Record. Right-justify and zero fill.
8-22	Control Total 1	15	REQUIRED. Please note that all Control Total fields have been expanded from 12 to 15 positions. Enter accumulated totals from Payment Amount 1. Right-justify and zero fill each Control Total amount. IF LESS THAN NINE AMOUNT FIELDS ARE BEING REPORTED, ZERO-FILL UNUSED CONTROL TOTAL FIELDS.
	If any corresponding Payment Amount fields are present in the Payee "B" Records, accumulate into the appropriate Control Total field. ZERO FILL UNUSED CONTROL TOTAL FIELDS. Please note that all Control Total fields have been expanded from 12 to 15 positions.		
23-37	Control Total 2	15	
38-52	Control Total 3	15	
53-67	Control Total 4	15	
68-82	Control Total 5	15	
83-97	Control Total 6	15	
98-112	Control Total 7	15	
113-127	Control Total 8	15	
128-142	Control Total 9	15	
143-360	Blank	218	REQUIRED. Enter blanks.

SEC. 14. END OF PAYER "C" RECORD—RECORD LAYOUT

RECORD TYPE	NUMBER OF PAYEES	CONTROL TOTAL 1	CONTROL TOTAL 2	CONTROL TOTAL 3	CONTROL TOTAL 4	CONTROL TOTAL 5	CONTROL TOTAL 6
1	2-7	8-22	23-37	38-52	53-67	68-82	83-97

CONTROL TOTAL 7	CONTROL TOTAL 8	CONTROL TOTAL 9	BLANK
98-112	113-127	128-142	143-360

SEC. 15. STATE TOTALS "K" RECORD

.01 The Control Total fields have been expanded from 12 to 15 positions.

.02 The State Totals "K" Record is a summary for a given payer and a given state in the Combined Federal/State Filing Program, used ONLY when state reporting approval has been granted. *IT MUST BE 360 POSITIONS IN LENGTH.*

.03 The "K" Record will contain the total number of payees and the totals of the payment amount fields filed by a given payer for a given state. The "K" Record(s) must be written after the "C" Record for the related "A" Record.

.04 There MUST be a separate "K" Record for *each state* being reported.

.05 Refer to Part A, Sec. 14 for the requirements and conditions that *MUST* be met to file on this program.

RECORD NAME: STATE TOTALS "K" RECORD

Diskette Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "K."
2-7	Number of Payees	6	REQUIRED. Enter the total number of Payee "B" Records being coded for this state. Right-justify and zero fill.
8-22	Control Total 1	15	REQUIRED. Please note that all Control Total fields have been expanded from 12 to 15 positions. Enter accumulated total from Payment Amount 1. Right-justify and zero fill each Control Total amount. IF LESS THAN NINE AMOUNT FIELDS ARE BEING REPORTED, ZERO FILL UNUSED CONTROL TOTAL FIELDS.
	If any corresponding Payment Amount fields are present in the Payee "B" Records, accumulate into the appropriate Control Total field. ZERO FILL UNUSED CONTROL TOTAL FIELDS. Please note that all Control Total fields have been expanded from 12 to 15 positions.		
23-37	Control Total 2	15	
38-52	Control Total 3	15	
53-67	Control Total 4	15	
68-82	Control Total 5	15	
83-97	Control Total 6	15	
98-112	Control Total 7	15	
113-127	Control Total 8	15	
128-142	Control Total 9	15	
143-358	Reserved	216	REQUIRED. Reserved for IRS use. Enter blanks.
359-360	State Code	2	REQUIRED. Enter the code assigned to the state which is to receive the information. Refer to Part A, Sec. 14.10.

SEC. 16. STATE TOTALS "K" RECORD—RECORD LAYOUT

RECORD TYPE	NUMBER OF PAYEES	CONTROL TOTAL 1	CONTROL TOTAL 2	CONTROL TOTAL 3	CONTROL TOTAL 4	CONTROL TOTAL 5	CONTROL TOTAL 6
1	2-7	8-22	23-37	38-52	53-67	68-82	83-97

CONTROL TOTAL 7	CONTROL TOTAL 8	CONTROL TOTAL 9	RESERVED	STATE CODE
98-112	113-127	128-142	143-358	359-360

SEC. 17. END OF TRANSMISSION "F" RECORD

.01 The "F" Record is a summary of the number of payers and diskettes in the entire file.

.02 This record should be written after the last "C" Record (or "K" Record, when applicable) of the entire file.

RECORD NAME: END OF TRANSMISSION "F" RECORD

Diskette Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "F."
2-5	Number of "A" Records	4	REQUIRED. You may enter the total number of Payer/Transmitter "A" Records in this transmission. Right-justify and zero fill or enter all zeros.
6-8	Number of Diskettes	3	REQUIRED. You may enter the total number of diskettes in this transmission. Right-justify and zero fill or enter all zeros.
9-30	Zero	22	REQUIRED. Enter zeros.
31-360	Blank	330	REQUIRED. Enter blanks.

SEC. 18. END OF TRANSMISSION "F" RECORD—RECORD LAYOUT

RECORD TYPE	NUMBER OF "A" RECORDS	NUMBER OF DISKETTES	ZERO	BLANK
1	2-5	6-8	9-30	31-360

Form **4419**
(Rev. March 1986)

Department of the Treasury – Internal Revenue Service

Application for Magnetic Media Reporting of Information Returns

IRS Use Only

OMB No. 1545-0387
Expires: 7-31-88

1. Name and address of organization *(street, city, State and ZIP code)*

2. Person to contact about this request
Name:
Title:
Telephone number: *(include area code)*

3. Employer identification number

4. Tax year for which you are requesting authorization to file on magnetic media

5. **Documents To Be Reported** *(Check all that you wish to file on magnetic media)*

Form	Form	Form	Form
☐ W-2G	☐ 1099-B	☐ 1099-OID	☐ 8027
☐ W-4	☐ 1099-DIV	☐ 1099-PATR	☐
☐ 1042S	☐ 1099-G	☐ 1099-R	☐
☐ 1098	☐ 1099-INT	☐ 5498	☐
☐ 1099-A	☐ 1099-MISC	☐ 6248	☐

Do NOT file Forms W-2 or W-2P with IRS. Submit that information to the Social Security Administration.

6. **Kind of equipment on which media will be prepared**

Please check the type of media you plan to file and provide the requested information for that type of media.

Type of Media	Main Frame	Drive Unit	Recording Mode	Track	Software
☐ Magnetic Tape 1/2" Only			☐ EBCDIC ☐ ASCII ☐ BCD	☐ 7 ☐ 9	
☐ 8" Diskette			☐ EBCDIC Only		
☐ 5-1/4" Diskette			☐ ASCII Only		
☐ Cassette	Burroughs Only		☐ EBCDIC ☐ ASCII		
☐ Mini-Disk	Burroughs Only		☐ ASCII Only		

7. If you are acting as transmitter, please list the name and employer identification number of each filer for whom you will prepare magnetic media on a separate sheet and attach it to this application.

8. Person responsible for preparation of tax reports	Name *(type or print)*	Title
	Signature	Date

For Paperwork Reduction Act Notice, see back of this form.

Form **4419** (Rev. 3-86)

Instructions for Form 4419

File Form 4419 to request authorization to file any of the forms shown in Block 5 on magnetic media. **Please be sure to complete all appropriate blocks.** For further information, contact a magnetic media coordinator at the National Computer Center address given below under "Filing Your Application," or by telephone at (304) 263-8700.

Block 1

Enter the name and complete address of the person or organization that will prepare and submit the magnetic media.

Block 4

Show the tax year for which you are requesting authorization to file on magnetic media.

Block 5

Check the boxes next to all of the returns you will file with IRS on magnetic media.

Block 6

Note: The only type of magnetic media on which you can report Forms 1042-S, 6248, 8027 and W-4 is 1/2 inch magnetic tape.

Enter the information requested for the type of magnetic media you intend to submit. Check the appropriate boxes. Enter the name of the manufacturer and the model number or name under "Main Frame" and "Drive Unit." Under "Software," indicate whether the software was purchased or is self-programmed. If purchased, provide the name of the software company.

Block 7

If you will be preparing returns on magnetic media for filers other than yourself, attach to your application a list of names and employer identification numbers of the other filers. If you add or delete any names from your file, submit an updated list to IRS.

Block 8

The form must be signed and dated by an official of the company or organization requesting authorization to report on magnetic media.

Filing Your Application

1. **Mail the completed application and any attached lists 90 days before** the due date of the returns to:

If by Postal Service,
Magnetic Media Reporting
Internal Revenue Service
National Computer Center
P.O. Box 1359
Martinsburg, WV 25401-1359

If by truck or air freight,
Magnetic Media Reporting
Internal Revenue Service
National Computer Center
Route 9 and Needy Road
Martinsburg, WV 25401

2. **IRS will approve or disapprove your application within 30 days** of its receipt. **Do not submit magnetic media until you receive an authorization letter.**

3. After authorization is received, **we encourage new filers to submit** test data on magnetic media before the filing season. **If you want to submit** test data, contact the magnetic media coordinator.

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Part IV. Items of General Interest

Application of Proposed Original Issue Discount Regulations to Foreign Currency Denominated Debt Instruments

Announcement 86–92

The Internal Revenue Service today clarified the application of the proposed original issue discount regulations to debt instruments with payments denominated in a foreign currency.

The Service stated that it was not intended that the rules contained in proposed Treas. Reg. §1.1275-4 be applied to lending transactions merely because some or all of the payments are denominated in or determined by reference to the value of one or more foreign currencies. The Service is actively considering the application of the original issue discount rules to foreign currency borrowings and solicits the comments of interested practitioners and taxpayers.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Tevor Adel	Silver Spring, MD	Certified Public Accountant	Indefinite from June 2, 1986
John H. Peimann	Ottawa, KS	Certified Public Accountant	Twenty-One Months from June 1, 1986
John D. Raikos	Indianapolis, IN	Attorney	Indefinite from May 20, 1986
Vernon Rubel	Hickory, NC	Enrolled Agent	Indefinite from May 28, 1986
Wayne Boyer	Southfield, MI	Enrolled Agent	Eight Months from May 12, 1986
Thomas McPhee	McAllen, TX	Enrolled Agent	Indefinite from June 15, 1986
Glen R. Verber	Houston, TX	Certified Public Accountant	Ninety Days from May 19, 1986
Beverly Worth	Winona Lake, IN	Enrolled Agent	Five Years from June 17, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section Affected	Subject	Published in the Bulletin	Expiration Date for Submission of Views
26 CFR 1.88–1, 1.468A–1 through 1.468A–8 added	**Nuclear decommissioning costs**	**1986–31 I.R.B. 22**	**Sept. 8, 1986**

Numerical Finding List[1]

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8094, 1986–31 I.R.B. *4*

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

Finding List of Current Action on Previously Published Rulings[1]

Bulletins 1986–27 through 1986–31

***Denotes entry since last publication**

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86–89, 1986–28 I.R.B. *4*

85–18
Clarified by
86–91, 1986–30 I.R.B. *5*

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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1986-33

Internal Revenue bulletin

Bulletin No. 1986-33
August 18, 1986

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-97, page 4.
Qualified nonpersonal use vehicles. Guidelines are set forth to determine whether a pickup truck or van meets the definition of a "qualified nonpersonal use vehicle."

EXEMPT ORGANIZATIONS

Rev. Rul. 86-98, page 5.
Qualification; individual practice association. An individual practice association that provides health services through written agreements with health maintenance organizations does not qualify for exemption from federal income tax as a social welfare organization under section 501(c)(4) of the Code or as a business league under section 501(c)(6).

ESTATE TAX

Rev. Rul. 86-99, page 6.
Special use valuation; farm used in conjunction with grazing permit. Two methods are described for valuing farmland for federal estate tax purposes where the farm is used in conjunction with a grazing permit on nearby federal land.

ADMINISTRATIVE

Rev. Proc. 86-33, page 8.
Federal tax deposit payments; reporting agents. Requirements and conditions are set forth for reporting agents who perform a payroll service and who, in connection with this service, submit employment federal tax deposit payments for their clients. Rev. Proc. 80-31 modified and superseded.

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Finding Lists begin on page 25.

Department of the Treasury
Internal Revenue Service

T 22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 274.—Disallowance of certain entertainment, etc., expenses

26 CFR 1.274-5T: Substantiation requirements (temporary).

Qualified nonpersonal use vehicles. Guidelines are set forth to determine whether a pickup truck or van meets the definition of a "qualified nonpersonal use vehicle."

Rev. Rul. 86-97

SECTION 1. PURPOSE

The purpose of this revenue ruling is to set forth guidelines for determining when the Internal Revenue Service will recognize certain specially modified pickup trucks or vans as "qualified nonpersonal use vehicles" for purposes of section 1.274-5T(k)(7) of the Temporary Income Tax Regulations. If these guidelines are met, gross income will not include the value of the use by an employee of the employer's "qualified nonpersonal use vehicle."

SEC. 2. BACKGROUND

Section 132(a)(3) of the Code provides that gross income shall not include any fringe benefit which qualifies as a working condition fringe.

Section 132(d) of the Code defines a "working condition fringe" as any property or services provided to an employee of the employer to the extent that, if the employee paid for such property or services, such payment would be allowable as a deduction under section 162 or 167.

Section 1.132-5T(h) of the Temporary Income Tax Regulations provides that 100 percent of the value of the use of a qualified nonpersonal use vehicle (as described in section 1.274-5T(k)) is excluded from gross income as a working condition fringe benefit, if in the case of a vehicle described in paragraph (k)(3) through (7) of section 1.274-5T, the use of the vehicle conforms to the requirements of that paragraph.

Section 274(d) of the Code provides, in part, that a deduction incurred with respect to "listed property" (as defined in section 280F(d)(4)) will be disallowed unless substantiated by adequate records or sufficient corroborative evidence. Listed property generally includes any passenger automobile or any other property used as a means of transportation. Section 274(d) does not apply to any qualified nonpersonal use vehicle as defined in section 274(i).

Section 274(i) of the Code provides that the term "qualified nonpersonal use vehicle" means any vehicle which, by reason of its nature, is not likely to be used more than a de minimis amount for personal purposes.

Section 1.274-5T(k)(1) of the regulations excepts a "qualified nonpersonal use vehicle" from the substantiation requirements of section 274(d) of the Internal Revenue Code.

Section 1.274-5T(k)(2) of the regulations provides that for purposes of section 274(d) of the Code and the regulations the term "qualified nonpersonal use vehicle" means any vehicle which, by reason of its nature (that is, design), is not likely to be used more than a de minimis amount for personal purposes.

Section 1.274-5T(k)(2)(ii)(C) of the regulations provides that any vehicle designed to carry cargo with a loaded gross vehicle weight over 14,000 pounds is a qualified nonpersonal use vehicle.

Section 1.274-5T(k)(7) of the regulations provides that the substantiation requirements of section 274(d) of the Code will not apply to any pickup truck or van only if it has been specially modified with the result that it is not likely to be used more than a de minimis amount for personal purposes.

The exception from the substantiation requirements of section 274(d) of the Code and the exclusion from gross income as a working condition fringe benefit under section 132 apply to the use of a qualified nonpersonal use vehicle because of its design and not because of the nature of the employee's services (such as being on 24-hour call).

SEC. 3. GUIDELINES

.01 A pickup truck with a loaded gross vehicle weight not over 14,000 pounds is a qualified nonpersonal use vehicle if it falls into one of the following two categories:

1. The vehicle is clearly marked with permanently affixed decals or with special painting or other advertising associated with the employer's trade, business, or function and is equipped with at least one of the following: a hydraulic lift gate, permanently installed tanks or drums, permanently installed side boards or panels materially raising the level of the sides of the bed of the pickup truck, or other heavy equipment, such as an electric generator, welder, boom, or crane used to tow automobiles and other vehicles.

2. The vehicle is clearly marked with permanently affixed decals or with special painting or other advertising associated with the employer's trade, business, or function, is actually used primarily for transporting a particular type of load other than over the public highway in connection with a construction, manufacturing, processing, farming, mining, drilling, timbering, or other similar operation, and has been specially designed or modified to a significant degree for such use.

.02 A van with a loaded gross vehicle weight not over 14,000 pounds is a qualified nonpersonal use vehicle if it is clearly marked with permanently affixed decals or with special painting or other advertising associated with the employer's trade, business, or function, it has a seat only for the driver or the driver and one other person, and either permanent shelving has been installed that fills most of the cargo area or the cargo area is open and the van constantly (during both working and nonworking hours) carries merchandise, material, or equipment used in the employer's trade, business, or function.

SEC. 4. APPLICATION

.01 As stated in Sec. 3 above, the Internal Revenue Service will recognize a pickup truck as a qualified nonpersonal use vehicle for purposes of section 1.274-5T(k)(7) of the regulations if the pickup truck meets either of the two categories in Sec. 3.01 of this revenue ruling. Similarly, the Service will recognize a van as a qualified nonpersonal use vehicle if the van meets Sec. 3.02 of this revenue ruling. In such cases, the exception from the substantiation requirements of section 274(d) of the Code and the exclusion from gross income as a working condition fringe benefit under section 132 apply to the employee's use of the qualified nonpersonal use vehicle.

.02 A pickup truck or van that does not meet the criteria in Sec. 3 of this revenue ruling may still be a qualified nonpersonal use vehicle if, based upon the particular facts, it satisfies requirements similar to those of this revenue ruling. In such cases, the taxpayer should contact the local district director for further guidance.

.03 The vehicles described in Sec. 3 of this revenue ruling are those owned or leased by employers, including governmental units or any agency or instrumentality thereof.

SEC. 5. EFFECTIVE DATE

For purposes of both sections 132(a)(3) and 274(d) of the Code, this ruling is effective for vehicle use occurring on or after January 1, 1985.

Section 501.—Exemption From Tax On Corporations, Certain Trusts, Etc.

26 CFR 1.501(c)(4)–1: Civic organizations and local associations of employees. (Also Sections 1.501(c)(6)–1.)

Qualification; individual practice association. An individual practice association that provides health services through written agreements with health maintenance organizations does not qualify for exemption from federal income tax as a social welfare organization under section 501(c)(4) of the Code or as a business league under section 501(c)(6).

Rev. Rul. 86–98

ISSUE

Does the individual practice association described below qualify for exemption from federal income tax as a social welfare organization under section 501(c)(4) of the Internal Revenue Code or as a business league under section 501(c)(6)?

FACTS

M, a nonprofit membership corporation, is an individual practice association (IPA) described in section 1302(5) of the Health Maintenance Organization Act of 1973, 42 U.S.C.A. section 300e–1(5) (1982). M's stated purpose is to arrange for the delivery of health services through written agreements negotiated with health maintenance organizations (HMOs).

M's membership is limited to licensed physicians who are engaged in the active practice of medicine and who are members of a specified county medical society. The activities of M are managed by an executive committee which is elected by the membership of M. The bylaws of M require that a majority of the executive committee be members of M.

M's members generally maintain a private medical practice in addition to performing services for M. All members are required to enter into written service contracts with M which provide:

(1) that the members shall provide their professional services to HMO patients in accordance with a compensation arrangement negotiated between M and the HMOs.

(2) that the members shall, to the extent feasible, share medical and other records, equipment, and professional, technical, and administrative staff, and

(3) that the members will limit referrals of HMO patients, to the extent feasible, to other participating members.

M's primary activities are to serve as a bargaining agent for its members in dealing with HMOs, and to perform the administrative claims services required by the agreements negotiated with the HMOs. M is paid a capitation amount by each HMO based on the number of HMO subscribers entitled to receive medical services. Members bill M for services rendered to the HMO subscribers and accept claims payment for M as payment for services rendered. Members agree to reimbursement by M on a fee-for-service basis according to a fee schedule established by the board of directors of M. The fee schedule reflects the usual customary fees charged by the member-physicians in their private medical practice.

M initially pays its members eighty-five percent of the amount stated in the fee schedule. The remaining fifteen percent is credited to the account of each member on M's books. At the end of each year, the difference between what M has received from the HMOs and what it has paid out to members and for administrative costs is paid to the members in proportion to the amounts credited in their accounts. If the amounts received by M from the HMOs, less administrative costs, are not sufficient to pay the total amounts billed by its members, the members have no further recourse. Members may look to patients for payment only for services not covered by the contracts between M and the HMOs. M has made no provisions for waiving the medical fees charged to patients who are unable to pay for services not covered by the contracts between M and the HMOs.

M's income is derived from its contracts with HMOs and its expenditures are for administrative costs and payments to its members.

LAW AND ANALYSIS

Section 501(c)(4) of the Code provides for the exemption from federal income tax of civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare.

Section 1.501(c)(4)–1(a)(2)(i) of the Income Tax Regulations provides that an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the community. An organization embraced within this section is one that is operated primarily for the purpose of bringing about civic betterments and social improvements.

Section 501(c)(6) of the Code provides for the exemption of business leagues, not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(6)–1 of the Regulations provides that a business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit. Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons.

The main functions of M are to provide an available pool of physicians who will abide by its fee schedule when rendering medical services to the subscribers of an HMO, and to provide its members with access to a large group of patients, the HMO subscribers, who generally may not be referred to nonmember-physicians. M negotiates contracts on behalf of its members with various HMOs, administers the claims received from its members, and pays them according to its reimbursement agreement. These facts indicate that M is akin to a billing and collection service, and a collective bargaining representative negotiating on behalf of its member-physicians with HMOs. In addition, M does not provide to HMO patients access to medical care which would not have been available but for the establishment of M, nor does it provide such care at fees below what is customarily and reasonably charged by members in their private practices.

Thus, M operates in a manner similar to organizations carried on for profit, and its primary beneficiaries are its member-physicians rather than the community as a whole. See Rev. Rul. 75-199, 1975-1 C.B. 160, and the authorities cited therein, and Rev. Rul. 81-58, 1981-1 C.B. 331, which provides examples of mutual, self-interest organizations that do not qualify for exemption under section 501(c)(4) of the Code. Accordingly, M is not operated exclusively for the promotion of social welfare within the meaning of section 501(c)(4).

In addition, because the billing and collection services provide an economy or convenience to M's members relating to the operation of their private medical practices, M is primarily performing particular services for its members. See Rev. Rul. 71-175, 1971-1 C.B. 153. Thus, the organization is rendering particular services for individual persons as distinguished from the improvement of business conditions in the medical profession and public health area generally. Membership in the organization is restricted to physicians who are subject to M's written service contract. Thus, M does not better conditions for all physicians in a particular community, but, instead, is devoted to maximizing fees for its members. See *National Muffler Dealers Association, Inc. v. U.S.*, 440 U.S. 472 (1979). Therefore, M is not operated as a business league within the meaning of section 1.501(c)(6)-1 of the regulations.

HOLDING

The individual practice association described above does not qualify for exemption from federal income tax as a social welfare organization under section 501(c)(4) of the Code or as a business league under section 501(c)(6).

Section 501.—Exemption from Tax on Corporations, Certain Trusts, Etc.

26 CFR 1.501(c)(6)-1: Business leagues, chambers of commerce, real estate boards, and boards of trade.

Whether an individual practice association qualifies for exemption from federal income tax as a business league under section 501(c)(6) of the Code.

See Rev. Rul. 86-98, page 5.

Section 2031.—Definition of Gross Estate.

26 CFR 20.2031-1: Definition of gross estate; valuation of property. (Also sections 2032A; 20.2032A-4.)

Two methods are described for valuing farmland for federal estate tax purposes where the farm is used in conjunction with a grazing permit on nearby federal land. See Rev. Rul. 86-99, this page.

Section 2032A.—Valuation of Certain Farmland, Etc., Real Property

26 CFR 20.2032A-4: Method of valuing farm real property. (Also sections 2031; 20.2031-1.)

Special use valuation; farm used in conjunction with grazing permit. Two methods are described for valuing farmland for federal estate tax purposes where the farm is used in conjunction with a grazing permit on nearby federal land.

Rev. Rul. 86-99

ISSUE

For federal estate tax purposes, how is farmland valued if the farmland is used in conjunction with a grazing permit on nearby federal land?

FACTS

Situation 1.

A, a United States citizen, died in 1984. At the time of *A*'s death, *A* had owned and operated a ranch for more than six years. The ranching operation consisted of two parcels of grazing land. One parcel was owned by *A* in fee simple. The other parcel was owned by the Federal Government and was used by *A* under a federal grazing permit issued by a federal agency.

The permit enables the owner of *A*'s ranch to graze a specified number of animals on the federal parcel for five months of each year. The two parcels have been used as a single integrated ranching unit for many years. The grazing permit had been renewed periodically by the Federal Government, although the government retained the discretion to refuse to renew the permit. The grazing permit specifies the permissible uses of the grazing land and will remain in effect for *A*'s heirs during the remaining term of the permit after *A*'s death. Although the federal statutes that authorize grazing permits state that such permits do not create any right, title, or interest in federal lands, in many cases grazing permits are continually renewed and remain a valuable asset that enhance the value of nearby farmland. When farmland is sold, the owner waives any grazing rights attributable to such farmland; however, the purchaser generally takes into consideration the existence of the grazing permit in determining the purchase price of the farmland, because a purchaser who otherwise qualifies generally will be able to obtain a new grazing permit.

The annual fees paid to the Federal Government under the grazing permit as of *A*'s death are less than the rates that would be paid for grazing rights on comparable land between unrelated individuals in an arm's length commercial transaction. Consequently, the grazing permit represents a valuable right to *A* and to *A*'s heirs.

As of *A*'s death, the fair market value of the parcel of farmland owned by *A* was $800,000. This value represents the price at which the parcel would sell between a hypothetical willing buyer and seller in an arm's length transaction. The $800,000 price is based in part on the fact that a buyer of *A*'s parcel would expect to be able to obtain renewals of the grazing permit on the nearby federally owned parcel on the same basis that *A* had done for many years. If there had been no federal grazing permit on the nearby federal land, the fair market value of the parcel owned by *A* would have been only $600,000.

The executor for *A*'s estate will not make a special use valuation election on the estate tax return to be filed.

Situation 2.

The facts are the same as in Situation 1, except that *A*'s executor plans to make a special use valuation election under section 2032A of the Internal Revenue Code. *A*'s farmland satisfied the requirements described in section 2032A(b) relating to qualified real property. The excess of the average annual gross cash rentals over the average annual state and local real estate taxes for land located in the locality and comparable to the land owned by *A* is $20,000. However, the excess of the average annual gross cash rentals over the average annual state and local real estate taxes for land located in the locality and comparable to *A*'s land, and including a grazing permit on federal land comparable to the land subject to *A*'s grazing permit, is $30,000. The average annual effective interest rate for Federal Land Bank loans for the region in which *A*'s ranch is located is 11.93 percent.

LAW AND ANALYSIS

Section 2031 of the Code provides in part that the value of the gross estate of a decedent shall be determined by including property in the gross estate on the basis of the fair market value of such property as of the date of the decedent's death, unless the executor elects the alternative valuation method under section 2032 of the Code. Section 20.2031-1(b) of the Estate Tax Regulations provides in part that the fair market value of property is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.

Section 2032A of the Code provides that, under certain conditions, an executor may elect to value farm or business real property based upon its current use rather than its fair market value as determined under otherwise applicable estate tax valuation rules. For property to qualify for "special use" valuation under section 2032A, the property must be "qualified real property" described in section 2032A(b) of the Code.

Section 2032A(e)(7)(A) of the Code provides, in general, that the value of a farm for farming purposes shall be determined by dividing (i) the excess of the average annual gross cash rental for comparable land used for farming purposes and located in the locality of such farm over the average annual state and local real estate taxes for such comparable land, by (ii) the average annual effective interest rate for all new Federal Land Bank loans. Further, each average annual computation shall be made on the basis of the five most recent calendar years ending before the date of the decedent's death.

Although a grazing permit does not create any right, title, or interest in the federal land affected by the permit, it is a valuable component part of the nearby farmland and has been recognized as having value to the holder in several court decisions. *See Estate of Cronin v. Cronin*, 89 S.D. 632, 237 N.W. 2d 171 (1975); *United States v. Jaramillo*, 190 F.2d 300 (10th Cir. 1951). *See also Board of Supervisors of County of Modoc v. Archer*, 18 Cal. App.3d 717, 726, 96 Cal. Rptr. 379, 386 (1971), which held that a federal grazing permit was a possessory interest under California law, i.e., "an interest in real property which exists as a result of possession, exclusive use, or a right to possession or exclusive use of land . . . unaccompanied by the ownership of a fee simple or life estate in the property"; and *Ruelas v. Ruelas*, 7 Ariz. App. 98, 436 P.2d 490, 493 (1968), which held that a federal grazing permit "has an economic value which affects the value of the patented land to which the permit is an adjunct." Accordingly, the federal grazing permit is a valuable asset attached to the land owned in fee by the decedent and is thus an element of the value of the land owned in fee.

In Situation 1, the fair market value of the land owned in fee by the decedent should reflect the fair market value of the grazing permit, because the value of the grazing permit would be taken into consideration in determining the price at which the land owned in fee would change hands in a sale between a willing buyer and a willing seller. Therefore, for purposes of section 2031 of the Code, the value of *A*'s farmland includible in the gross estate is $800,000. Moreover, these facts indicate that the grazing permit has no value independent of the ownership of *A*'s farmland; thus, the grazing permit is not separately includible in *A*'s gross estate.

In Situation 2, the value of the grazing permit must be reported as part of the value of the land owned by the decedent in fee simple. In valuing the farmland under section 2032A(e)(7) of the Code, only land comparable to the land being valued under section 2032A may be used. Where the farmland to be valued under section 2032A is used in conjunction with a grazing permit on nearby federal land, an example of comparable farmland for purposes of section 2032A would be a parcel of farmland (similar to that owned by the decedent) that is used in conjunction with a second parcel (similar to that used under the decedent's federal permit) and that is rented as a combined unit to a third party.

The special use value of *A*'s farmland, computed with the formula provided in section 2032A(e)(7) of the Code, is $251,467 ($30,000 excess average annual rental value divided by 11.93 percent average annual interest rate).

HOLDINGS

Situation 1.

For federal estate tax purposes, the fair market value of *A*'s farmland, which is used in conjunction with a grazing permit on nearby federal land, must reflect the value of the permit.

Situation 2.

Under section 2032A of the Code, the special use value of *A*'s farmland is computed by taking into account the total rent that an owner receives for a parcel of land comparable to the decedent's farmland consisting of a fee simple parcel and a grazing permit over nearby federal land.

Section 6302.—Mode or Time of Collection

26 CFR 31.6302(c)-1: Use of government depositaries in connection with taxes under Federal Insurance Contributions Act and income tax withheld.

Requirements and conditions for reporting agents who perform a payroll service and submit federal tax deposit payments for their clients. See Rev. Proc. 86-33, page 8.

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26 CFR 31.6302(c)-3: Use of government depositaries in connection with tax under the Federal Unemployment Tax Act.

Requirements and conditions for reporting agents who perform a payroll service and submit federal tax deposit payments for their clients. See Rev. Proc. 86-33, page 8.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.602: Forms and instructions. (Also Part I, Section 6302; 31.6302(c)-1. 31.6302(c)-3.)

Rev. Proc. 86-33

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to outline the requirements and instructions for reporting agents who perform a payroll service and who, in connection with this service, submit employment federal tax deposit payments for their clients. These payments are described in the Employment Tax Regulations (26 CFR Part 31) under section 6302 of the Internal Revenue Code. All federal tax deposit payments are required to be deposited through a qualified federal tax depositary, as defined in 31 CFR Part 203.

.02 Under the provisions of this revenue procedure, qualifying agents may request permission to prepare magnetic tapes for federal tax deposits instead of using the preprinted forms provided by the Internal Revenue Service (IRS). Authorization will extend only to those agents who have a minimum of 250 clients and who satisfy all the requirements of this revenue procedure.

SEC. 2. BACKGROUND

.01 The IRS furnishes federal tax deposit forms to those taxpayers who can reasonably be expected to make tax deposits. These forms are preprinted with essential identifying information for processing the payment data to the appropriate tax account. Many payroll and tax preparation businesses do not have the preprinted deposit forms for making the required tax deposits and, in most instances, this occurs because the agent has not requested that the client forward the deposit forms furnished by the IRS. Some of these reporting agents have mailed deposits directly to an Internal Revenue Service office when the forms were not available to them. This practice is not in conformity with Section 31.6302(c)-1(a)(2) of the Employment Tax Regulations.

.02 Authorization for preparing Form FTD 501, Federal Tax Deposit, Withheld Income and FICA Taxes (FTDs), first appeared in Rev. Proc. 75-112, 1975-1 C.B. 653. The authority to prepare federal tax deposit magnetic tapes is not dependent on the authority to file Form 941, Employer's Quarterly Federal Tax Return, on magnetic tape.

SEC. 3. FTD PAYMENTS SUBMITTED BY REPORTING AGENTS

.01 All FTD payments prepared by an authorized agent must be submitted through a qualified federal tax depository or Federal Reserve Bank. The only acceptable agent-prepared deposit tapes are those relating to Forms 941, 940, and 943. All FTD tapes prepared by an authorized agent must be submitted to the service center of jurisdiction, Attention: Service Center Computer Branch Tape Library. Addresses are shown on pages 16 and 17. Form 2284, Advice of Credit (AOC), facsimile must be transmitted to the Federal Reserve Bank of jurisdiction.

.02 Deposits for other taxes and for clients who have not been accepted and validated by the IRS for this program must be made to a depositary by means of the pre-printed forms provided by IRS. Reporting agents authorized under this program who mail payments directly to an IRS office will have their remittances returned to them with instructions that they obtain the appropriate deposit forms from their client and that they submit the payments through a qualified federal tax depositary, as required. Taxpayers whose payments are returned to their reporting agent may be subject to appropriate penalty and interest charges. Reporting agents must not assume the responsibility for making tax deposits on behalf of a client for any deposit that may become due before the client is actually under this program.

.03 Agent-prepared FTD deposits must be submitted through a qualified depositary.

SEC. 4. APPLICATION TO SUBMIT FTD TAPES

.01 Agents who wish to submit FTD information on magnetic tape must first file a letter of application with the Director of the Internal Revenue Service Center where the deposits will be processed. In most cases this will be the same service center that processes the related tax forms. See pages 14 and 15 for a list of service centers and their respective addresses. The letter of application should include all the following information:

1. The full name, address, and employer identification number of the firm making the application. If the reporting agent will prepare tapes at more than one branch or location, each location must be identified in the letter of application.

2. The name, title, and telephone number of a person the service center can contact regarding the application. In most cases, any problem with the letter of application can be resolved by telephone and this will expedite processing by the service center.

3. The name, address, Federal Reserve Bank Code, bank identification number/check digit code, and branch code of the federal tax depositary. Prior to submitting the letter of application, the reporting agent must have an agreement with a depositary that the depositary will allow the agent to utilize its Treasury Tax and Loan Account (TT&L). A copy of the agreement should accompany the application.

4. A listing of the taxpayers who will have their FTD payments prepared by the reporting agent. See Section 5 for the information required on this listing. See Exhibit 1 for an example of a list of clients.

5. A power of attorney (POA) for each taxpayer on the listing. See Section 6 for information concerning the power of attorney. See Exhibit 2 for an example of a properly prepared power of attorney.

.02 Applications containing a listing of less than 250 clients will be denied. If an agent has previously been preparing FTDs under the provisions of Rev. Proc. 75-12 before supersession by Rev. Proc. 79-15, 1979-1 C.B. 498, the agent is exempt from this qualification.

SEC. 5. LISTING OF CLIENTS

.01 Each letter of application must include a listing of the taxpayers who will have their FTDs prepared by the reporting agent. The listing must include each taxpayer's complete business name, address (including zip code), federal employer identification number (EIN) and a customer identification number assigned to the client by the agent. For each client, the listing must specify the types of taxes that will be prepared.

.02 The listing must be double spaced to allow room for notations by the service center. The clients must be listed in EIN number sequence. A duplicate listing must be submitted so that the Service can maintain a file of taxpayers accepted under this program. See Section 8 for updates to the initial listing of clients. See Exhibit 1 for an example of the format of the listing.

SEC. 6. POWER OF ATTORNEY

.01 A power of attorney must be submitted for each client on the listing. The power of attorney may be submitted on Form 2848, Power of Attorney and Declaration of Representative, which is available on request. A sample power of attorney is set forth in Exhibit 2. If this form is not used, the power of attorney must clearly state that it is a limited power of attorney granting the authority to prepare and submit FTDs for Forms 940, 941, 943 Employment Taxes and must include the following information.

(a) The client's name, address and employer identification number

(b) The reporting agent's name and address

(c) Type of tax, Employment Taxes, Forms 940, 941, 943

(d) A specific period of time, i.e., 1986–1991

(e) Both the taxpayer or authorized representative, and the reporting agent must sign the POA.

(f) If the reporting agent would like to receive copies of notices the POA must specify authorization as a "designee" of the taxpayer under section 6103 of the Code to receive copies of notices and correspondence with regard to these payments.

(g) Agents should be cautioned that if their client already has a POA on file with the IRS, the automated centralized POA file will accept the latest date and revoke prior POA's unless noted on the limited POA to retain all existing POA's on file.

.02 If a power of attorney is already on file for full tax reporting, it is not necessary to execute a new agreement. If a power of attorney is already on file for magnetic tape filing of Form 941, it does not need to be revoked, however, a new power of attorney must be submitted to cover any federal tax deposits not already covered.

.03 The power of attorney for agent-prepared FTDs will be a limited power of attorney. Refunds, tax forms, notices and other output will be mailed to the taxpayer. Requests from a reporting agent for information or adjustments on an account will be honored by the IRS only to the extent covered by the power of attorney.

.04 Requests for taxpayer name and address changes may not be made by a reporting agent with a limited power of attorney. The only requests that will be honored will be those originating from the taxpayer, or an attorney-in-fact, if the attorney has a full power of attorney for all tax matters concerning a taxpayer and has filed a copy of the full power of attorney with the IRS center.

.05 The reporting agent must keep copies of the power of attorney on file at the agent's principal place of business for examination by the IRS upon request. If the power of attorney includes the authority to sign and file tax returns, it must be retained until the statute of limitations for the last return filed under its authority expires.

.06 The power of attorney will remain in effect until such time as it is revoked by the taxpayer, terminated by written notification by the reporting agent, or expires under its own terms.

.07 The power of attorney is automatically revoked when the reporting agent notifies the Service that the taxpayer will no longer have FTD payments submitted by the agent. It is also automatically revoked when the Service notifies the reporting agent that the requirements of this revenue procedure have not been adhered to and the Service will no longer accept the agent-prepared FTD payments from the agent.

.08 Any time a power of attorney has been terminated or revoked a new power of attorney will be required if a client reenters this program. The new power of attorney must be signed and dated subsequent to the revocation.

SEC. 7. ACCEPTANCE OF AGENT'S APPLICATION

.01 The IRS will process each letter of application within thirty days of receipt. The authorization letter will include a two digit identifying number, which the IRS will assign to the reporting agent. If the reporting agent will prepare tapes at more than one location or branch, each location or branch will be assigned a separate identifying number. After an agent has been assigned an identifying number, all communication regarding the preparation FTD tapes should include this number. Updates to the agent's listing of clients must always contain the identifying number of the location or branch handling the particular client's records. The agent-identifying number must be in tape positions 52–53, on both the AOC and FTD records.

.02 One copy of the listing of the reporting agent's clients will be returned with the authorization letter. The Service will verify each client's employer identification number and will provide the client's name control. The name control must appear in tape positions 14–17 on the FTD records. An IRS office code will be provided to the agent for each taxpayer and must appear in tape positions 18–19 of the FTD record. If there is a discrepancy, the IRS will also provide the business name as it is maintained on record with the IRS. Corrections will be indicated by a line through the agent's information with the corrected information written above.

.03 Reporting agents must not change the validated employer identification number, name control, or service center code except when notified to do so by the Internal Revenue Service.

.04 All discrepancies in taxpayer filing requirements will be resolved by telephone if a contact is established in the letter of application. If, for any reason, a particular taxpayer whose name is recited on the agent's list is not accepted by the IRS under this program, the name of the taxpayer will be circled out and the reason for non-acceptance will be stated in the acceptance letter.

.05 Payroll agents who submit data on magnetic tape and are located in IRS regions having more than one IRS center will have the option to consolidate and file FTDs at only one service center. Only those agents using magnetic tape are allowed this option. If an agent deals with more than one regional service center and wishes to consolidate, the agent must write to the Director of the IRS center and obtain approval prior to beginning to file with only one service center.

SEC. 8. UPDATES TO THE AGENT'S LIST OF CLIENTS

.01 After acceptance of the reporting agent's initial list of clients, all additions and deletions must be reported to the service center. New clients must not be included in the preparation of FTDs by a reporting agent until they are accepted and the entity information (EIN, name control, service center code, and filing requirements) is validated and provided by the IRS. If the reporting agent chooses to make FTDs for a new client prior to being accepted, the agent must use the IRS preprinted forms and deposit the payment with a qualified depositary separate from the agent-magnetic tape.

Note: When the additions or deletions list exceeds 500, that listing must be sent to the service center within one week. If the additions and deletions are less than 500, submit no later than the first day of the last month of the quarter.

.02 The IRS will process updates to the agent's addition listing within two weeks of receipt. The update listing should be in the same format as the initial listing, with the additions preceding and on a separate page from the deletions. Two copies of this listing should be submitted to enable the Service to maintain a file copy. The service center will process the additions on an expedite basis and in the same manner as the initial listing. Deletions will be acknowledged to the reporting agent within 30 days.

.03 Once a client has been deleted under this program, the reporting agent may not request to re-enter that client until the next quarter. For example, if a client is deleted in the first quarter of the year (Jan., Feb., Mar.), the client may not be added back onto the accepted list of clients until the second quarter of the year (Apr., May, June). A new power of attorney must be submitted when the request to re-enter the program is sent to the Service.

.04 The reporting agent must send a consolidated listing of their clients currently accepted by the Service within 14 days after the end of each quarter. This listing must not include current additions or deletions which must be sent separately. The consolidated listing is for information only and will not be returned to the agent.

SEC. 9. PREPARATION OF THE MAGNETIC TAPE DATA

.01 Tape must be: a. 9 Track b. ASCII c. 1600BPI

.02 Instructions for the record layouts of the Advice of Credit, Form 2284, and the Federal Tax Deposits are included in this revenue procedure as Exhibits 3 & 4. Exhibit 5 is the FTD Data Tape record layout. Each tape must be clearly labeled as agent prepared (state agent name), FTD Tape.

.03 The Advice of Credit record layout is an 81 character record and must include the following:

1. Problem Code, 1 position, Always Zero

2. Service Center code, 2 positions, must be numeric and is assigned by the IRS.

3. Federal Reserve Bank code, 2 positions, must be numeric and is also assigned by the IRS.

4. Bank account number, 8 positions, is the routing and transmittal number authorized by the depositary bank.

5. Check digit, 1 position, and is for the routing and transmittal number.

6. Branch code, 3 positions, and represents the depositary branch code, under which the agent is authorized to submit FTD data.

7. Transmittal Serial number, 3 positions, must be numeric. Must be separate for each AOC and in incrementing order, beginning with 001 and ending with 999. The number must not be duplicated within two calendar months.

8. Deposit Date, 6 positions, in MMDDYY format. The deposit date must agree with the deposit date in the FTD data record.

9. Number of FTDs, 3 positions, numeric, in groups up to 440. If less than 100, zero fill, right justify.

10. Amount, 11 positions, numeric, and must represent the total of the related FTD's.

11. Agent code, 2 positions, numeric. This number will be assigned by IRS upon approval of the application.

12. Microfilm number, 6 positions and will always be filled with 999999.

13. Record type ID code, 1 position, and is a constant 3.

.04 The Federal Tax Deposit record is an 81 character record and must include the following information.

1. Problem Code, 1 position, always zero.

2. The taxpayer identification, name control, service center code, and agent code must be from the information provided and verified by the IRS. No change should be made to this information for a particular client unless the IRS notifies the reporting agent to do so.

3. Name Control, 4 positions, Name control is provided by the IRS center on the approved client list.

4. Service Center Code, 2 positions, must be numeric and is assigned by the IRS.

5. Tax class code, 1 position, and must be a "1" for withholding, "8" for unemployment, "6" for agriculture withholding or a "5" for backup withholding.

6. Tax period, 2 positions, Month/Year format. NOTE: December =& (Ampersand) November = - (hyphen).

7. Payment date, 4 positions in MMDD format, must be numeric. It is essential that the payment date reflect the date the taxpayer's liability must be paid. Also the payment date must agree with the deposit date in the related AOC. In no case should these dates be different.

8. Amount, 12 positions, zero fill, right justify and must reflect the taxpayer's liability due and balance to the AOC.

9. Agent code, 2 positions, a unique code assigned by IRS to identify magnetic tape filers and to accumulate statistical data.

10. Customer ID number, is 6 positions, numeric, zero fill, right justify. If the customer ID number is alpha/numeric it is not acceptable by the program. You must use the AOC serial number, 3 positions (001–999) and the FTD sequence number. 3 positions (001–440) in this field.

SEC. 10. SUBMISSION OF AGENT-PREPARED FEDERAL TAX DEPOSITS

01. Prior to submission of the first tapes sent to the service center, each agent must provide:

(a) A tape of test data for validation by the service center. The tape must be in the tape format in Exhibits 4 and 5 and must be 9 Track, ASCII, 1600 BPI. The test tape will be verified and returned with the authorization letter.

(b) New agents will be accepted to begin filing new client data at the beginning of a quarter only.

(c) A yearly schedule calendar showing the schedule shipment dates and the number of magnetic tapes the agent expects to ship each week.

The funds must be deposited in the Treasury Tax and Loan Account of an authorized depositary within 24 hours after the date of deposit. The transaction data must be received at the IRS service center within 5 workdays of the date of credit to the Treasury Tax and Loan account of the authorized depositary. If an agent fails to meet the deposit criteria above a cautionary letter will be issued, which may result in termination of authority. The IRS will schedule to process the FTD data not later than 2 workdays from the date of service center receipt.

.02 The magnetic tape data must be accompanied by a summary list of the Advice of Credit, in transmittal order and must provide the following information:

1. Transmittal number,

2. Count of FTD's,

3. Dollar amount of each Advice of Credit.

.03 Within 14 days after deposit date:

1. A listing must be provided giving specific deposit information. This data must

be provided on microfiche. The listing should be titled FTD PROOF LIST, and contain the agent name and code on the title line. The listing must contain the following header information:

(a) Deposit date, 6 positions, MMDDYY format,

(b) Advice of Credit (AOC) serial number, 3 positions,

NOTE: The Advice of Credit serial number must appear on each page that has FTD client data for that AOC,

(c) FTD sequence, number 3 positions (beginning with 001, not to exceed 440),

(d) Federal Employer Number, 10 positions in the following format: NN-NNNNNNN,

(e) Name Control, 4 positions,

(f) Deposit type, 3 positions (form number),

(g) Deposit period, 5 positions, MM/YY,

(h) FTD Amount, 11 positions, See Exhibit 7.

2. A microfiche copy of the AOC transmittal must be provided. Each page must have a heading showing:

(a) Agent name and code,

(b) From and to, AOC serial numbers,

(c) Deposit date, MMDDYY format. See Exhibit 6.

Note: Microfiche data must be received by the service center within 14 days after the deposit date.

.04 Form 8482, Transmittal of Magnetic Tape of Federal Tax Depostis, will be used for transmitting tapes, and microfiche data between the service center and the agent. The initial supply of Form 8482 will be provided upon approval of the agents application to prepare deposit tapes. Additional supply will be obtained from the service center of jurisdiction. See Exhibit 8

.05 Each tape must be clearly identified by affixing a completed Form 3298, File Identity Label, (initial supply provided by the service center). Each tape box must have an expedite label. The label must state:

EXPEDITE
FEDERAL TAX DEPOSIT
ON MAGNETIC TAPE
DELIVER UNOPENED TO
TAPE LIBRARY

See Exhibit 9

.06 Tapes will be retained at the IRS service center for 14 days for data verification purposes and then returned to the agent.

.07 The agent will receive an acknowledgement of receipt of the deposit tapes within seven days of receipt by the service center. Nonreceipt of the acknowledgement transmittal should be reported to the service center Interagency Coordinator immediately.

SEC. 11. TERMINATION OF THIS AUTHORIZATION

The Service reserves the right to terminate this agreement with reporting agents because of possible systemic changes which may preclude the use of magnetic tapes, or an agent's failure to comply with the requirements of this procedure. If the reporting agent cannot modify processing to accommodate these changes or continuously neglects the revenue procedure requirements, the agreement may be terminated with sixty days notice. Requests for additional copies of this revenue procedure, applications to prepare FTD, and update listings of authorized clients, should be addressed to the Director, Internal Revenue Service Center, Attn: FTD Coordinator, at one of the following addresses:

1. NORTH-ATLANTIC REGION
   (a) Andover Service Center
   P.O. Box 4082
   Woburn, MA 01888
   (b) Brookhaven Service Center
   P.O. Box 950
   Holtsville, NY 11742
2. MID-ATLANTIC REGION
   Philadelphia Service Center
   11601 Rossevelt Blvd.
   Philadelphia, PA 19255
3. CENTRAL REGION
   Cincinnati Service Center
   P.O. Box 2345
   Cincinnati, Ohio 45201
4. SOUTHEAST REGION
   (a) Atlanta Service Center
   P.O. Box 47421
   Doraville, GA 30309
   (b) Memphis Service Center
   P.O. Box 2500
   Memphis, TN 38101
5. MIDWEST REGION
   Kansas City Service Center
   P.O. Box 337
   Kansas City, MO 64141
6. SOUTHWEST REGION
   (a) Austin Service Center
   P.O. Box 2925
   Austin, TX 78777
   (b) Ogden Service Center
   P.O. Box 9950 Stop 6264
   Ogden, UT 84409
7. WESTERN REGION
   Fresno Service Center
   P.O. Box 12147
   Fresno, CA 93776

Shipments of agent-prepared FTD tapes should be addressed to the Director, Internal Revenue Service Center, Computer Branch Tape Library at one of the following addresses:

1. NORTH-ATLANTIC REGION
   (a) Andover Service Center
   310 Lowell Street
   Andover, MA 01810
   (b) Brookhaven Service Center
   1040 Waverly Ave. Stop 486
   Holtsville, NY 11742.
2. MID-ATLANTIC REGION
   Philadelphia Service Center
   1106 Roosevelt Blvd.
   Philadelphia, PA 19255
3. CENTRAL REGION
   Cincinnati Service Center
   201 W. Second St.
   Covington, Kentucky 41019
4. SOUTHEAST REGION
   (a) Atlanta Service Center
   4800 Buford Hwy
   Chamblee, GA 30341
   (b) Memphis Service Center
   3131 Democrat Road
   Memphis, TN 37501
5. MIDWEST REGION
   Kansas City Service Center
   2306 East Bannister Road
   Kansas City, MO 64131.
6. SOUTHWEST REGION
   (a) Austin Service Center
   3571 South IH 35
   Austin, TX 78741
   Ogden Service Center
   1160 West 1200 South
   Ogden, UT 84207
7. WESTERN REGION
   Fresno Service Center
   5045 E. Bulter Ave.
   Fresno, CA 93888

SEC. 12 EFFECTIVE DATE

This revenue procedure is effective on an optional basis from August 18, 1986, and will be mandatory after February 18, 1987.

SEC. 13 EFFECT ON OTHER DOCUMENTS

Rev. Proc. 80-31 is modified and, as modified is superseded.

EXHIBIT 1

Agent Identifying Number: (assigned by IRS)
Agent EIN:
Type of List:

DATE OF LIST:
Name of Reporting Agent:
Address of Reporting Agent:

Client Account #	EIN	Name Control	Client Business Name and Address	Type of Tax		
				941	940	943
01234	11-1111111		Blossom Corp. 16 Tulip Blvd. Flower, CA 91111	X	X	
01235	99-9999999		Animal Farm Rural Rt. 1 Orwell, CA 93333		X	

1. **Heading data may be positioned differently but must contain all and only the requested information.**
2. **Sort by EIN number assigned to client by IRS.**
3. **Leave Name Control field blank—this will be entered by IRS.**
4. **Double-space between entries of clients.**
5. **Indicate the type of tax in the appropriate column.**

EXHIBIT 2

Form **2848**
(Rev. October 1983)
Department of the Treasury
Internal Revenue Service

Power of Attorney and Declaration of Representative

▶ See separate instructions

OMB No. 1545-0150

PART I.— Power of Attorney

Taxpayer(s) name, identifying number, and address including ZIP code (Please type or print)

Client's name, address and employee identification number.

For IRS Use Only		
File So.		
Level		
Receipt		
Powers		
Blind T.		
Action		
Ret.Ind.		

hereby appoints (name(s), CAF number(s), address(es), including ZIP code(s), and telephone number(s) of individual(s)) *

Reporting agents' name and address.

as attorney(s)-in-fact to represent the taxpayer(s) before any office of the Internal Revenue Service for the following tax matter(s) (specify the type(s) of tax and year(s) or period(s) (date of death if estate tax)):

Type of tax (Individual, corporate, etc.)	Federal tax form number (1040, 1120, etc.)	Year(s) or period(s) (Date of death if estate tax)
Employment Taxes	940,941,943	1986-1991 (See Sec. 6)

The attorney(s)-in-fact (or either of them) are authorized, subject to revocation, to receive confidential information and to perform any and all acts that the principal(s) can perform with respect to the above specified tax matters (excluding the power to receive refund checks, and the power to sign the return (see regulations section 1.6012-1(a)(5), Returns made by agents), unless specifically granted below).

Limited to: Prepare and submit Federal Tax Deposit for employment taxes and receive copies of notices and correspondence with regard to these employment tax payments.

Send copies of notices and other written communications addressed to the taxpayer(s) in proceedings involving the above tax matters to:

1 ☐ the appointee first named above, or
2 ☐ (names of not more than two of the above named appointees) ....

Initial here ▶ .... if you are granting the power to receive, but not to endorse or cash, refund checks for the above tax matters to:

3 ☐ the appointee first named above, or
4 ☐ (name of one of the above designated appointees) ▶ ....

This power of attorney revokes all earlier powers of attorney and tax information authorizations on file with the Internal Revenue Service for the same tax matters and years or periods covered by this power of attorney, except the following:

....

(Specify to whom granted, date, and address including ZIP code, or refer to attached copies of earlier powers and authorizations.)

Signature of or for taxpayer(s)

(If signed by a corporate officer, partner, or fiduciary on behalf of the taxpayer, I certify that I have the authority to execute this power of attorney on behalf of the taxpayer.)

.... (Signature) .... (Title, if applicable) .... (Date)

(Also type or print your name below if signing for a taxpayer who is not an individual.)

.... (Signature) .... (Title, if applicable) .... (Date)

* You may authorize an organization, firm, or partnership to receive confidential information, but your representative must be an individual who must complete Part II.

For Privacy Act and Paperwork Reduction Act Notice, see page 1 of the instructions.

Form **2848** (Rev. 10-83)

EXHIBIT 3

Advice of Credit Record Layout

(Form 2284)

Element Number	Name	Start Position	Length	Remark
1	Problem—Code	1	1	Always zero
2	Service Center Code	2	2	Numeric
3	Federal Reserve Bank Code	4	2	Numeric
4	Bank Account Number	6	8	Numeric
5	Check Digit	14	1	Numeric
6	Branch Code	15	3	Numeric
7	Transmittal Serial Number	18	3	Numeric
8	Filler	21	1	Blank
9	Deposit Date	22	6	MMDDYY Format
10	Filler	28	1	Blank
11	Number of FTDs	29	3	Numeric in groups of 440 If less than 100, zero fill, right justify.
12	Amount	32	11	Numeric, zero fill right justify
13	Filler	43	9	Blank
14	Agent Code	52	2	Numeric, Assigned by IRS
15	Microfilm Number	54	6	Numeric, 999999
16	Filler	60	1	Blank
17	Record Type ID Code	61	1	Always 3
18	Filler	62	20	Blank

EXHIBIT 4
Federal Tax Deposit Record Layout

Element Number	Name	Start Position	Length	Remark
1	Problem Code	1	1	Always zero
2	Filler	2	3	Blank
3	Taxpayer Identification Number	5	9	Numerics
4	Name Control	14	4	First Four Characters of Taxpayers business name. Can be alpha numeric, -, &, or blank.
5	Service Center Code	18	2	Numeric
6	Tax Class Code	20	1	1 = Withholding 8 = Unemployment 6 = Agricultural Withholding 5 = Backup Withholding
7	Tax Period	21	2	Month/Year Format NOTE: December = & November = -
8	Filler	23	4	Blank
9	Payment Date	27	4	MMDD Format, Numeric
10	Filler	31	9	Blank
11	Amount	40	12	Numeric, zero fill right justify.
12	Agent Code	52	2	Numeric, assigned by IRS
13	Customer ID #	54	6	Numeric, zero fill right justify.
14	Filler	61	21	Blank

EXHIBIT 5
FDA DATA TAPE
FILE ID FTD 5101

The following is the label sequence for this file:

1. **VOL1**
2. **HDR1**
3. **HDR2**
4. **FILEMARK**
5. **DATA BLOCKS**
   - **A)** **Record length = 81 characters**
   - **B)** **Block length = 20 Records per block.** **(1620 characters)**
6. **FILEMARK**
7. **EOF1**
8. **EOF2**
9. **FILEMARK**
10. **FILEMARK**

LABEL FORMAT

VOL1 LABEL

	POSITION VALUE
1–4	"VOL1"
5–10	"6" digit reel number
11–79	"blanks"
80	"1"

HDR1 LABEL

1–4	"HDR1"
5–12	"FTD5101"
13–21	"blanks"
22–27	"6" digit reel number
28–31	"0001"
32–35	"0001"
36–39	"0001"
40–41	"00"
42	"blank"
43–47	creation date, format = YYDDD (YY = Year, DDD = 3 pos. julian date)
48	"blank"
49–53	creation date, format = YYDDD
54	"1"
55–60	"6 zeroes"
61–80	"blanks"

HDR2 LABEL:

POSITION	VALUE
1–4	"HDR2"
5	"F"
6–10	block length, value = "01620"
11–15	record length, value = "00081"
16–50	"blanks"
51–52	"00"
53–80	"blanks"

EOF1 LABEL

Format is the same as the HDR1 LABEL except Pos. 1–4 = "EOF1"

EOF2 LABEL

Format is the same as the HDR2 LABEL except Pos. 1–4 = "EOF2"

EXHIBIT 5

12. **RECORD LAYOUT**
(80 Positions)

13. REFERENCE

1. PROJECT NAME

2. PROJECT NO.

3. PUBLIC.

4. SEC. NO.

5. PART OF

6. PROGRAM - SYSTEM

7. OPER. PERIOD

8. PREP. BY

9. APPROV. UNITS

10. ORG. CODE

11. DATE

14. REMARKS
FTD-DATA TAPE

DATA-ASCII; 1600 BPI, 9 TRACK

16. RECORD NAME: VOL 1
18. REEL NUMBER 6 DIGIT (positions 5–10)
19. V O L 1

16. RECORD NAME: HDR 1
18. REEL NUMBER 6 DIGIT (positions 22–27); CREATE DATE YYDDD (positions 43–47); CREATE DATE YYDDD (positions 49–53)
19. H D R 1 F T D S 1 0 1 b̸ → b̸ | REEL NUMBER | 0 0 0 1 0 0 0 1 0 0 0 1 0 0 b̸ | CREATE DATE | b̸ | CREATE DATE | 1 0 0 0 0 0 0 b̸ → b̸

16. RECORD NAME: HDR 2
19. H D R 2 F 0 1 6 2 0 0 0 0 8 1 b̸ → b̸ 0 0 b̸ → b̸

16. RECORD NAME: EOF 1
18. REEL NUMBER 6 DIGIT (positions 22–27); CREATE DATE YYDDD (positions 43–47); CREATE DATE YYDDD (positions 49–53); BLOCK COUNT (positions 55–60)
19. E O F 1 F T D S 1 0 1 b̸ → b̸ | REEL NUMBER | 1 0 0 1 0 0 0 1 0 0 0 1 0 0 b̸ | CREATE DATE | b̸ | CREATE DATE | 1 | BLOCK COUNT | b̸ → b̸

16. RECORD NAME: EOF 2
19. E O F 2 F 0 1 6 2 0 0 0 0 8 1 b̸ → b̸ 0 0 b̸ → b̸

TRANSMITTAL NO.

8" FOLD →

OFFICIAL USE ONLY

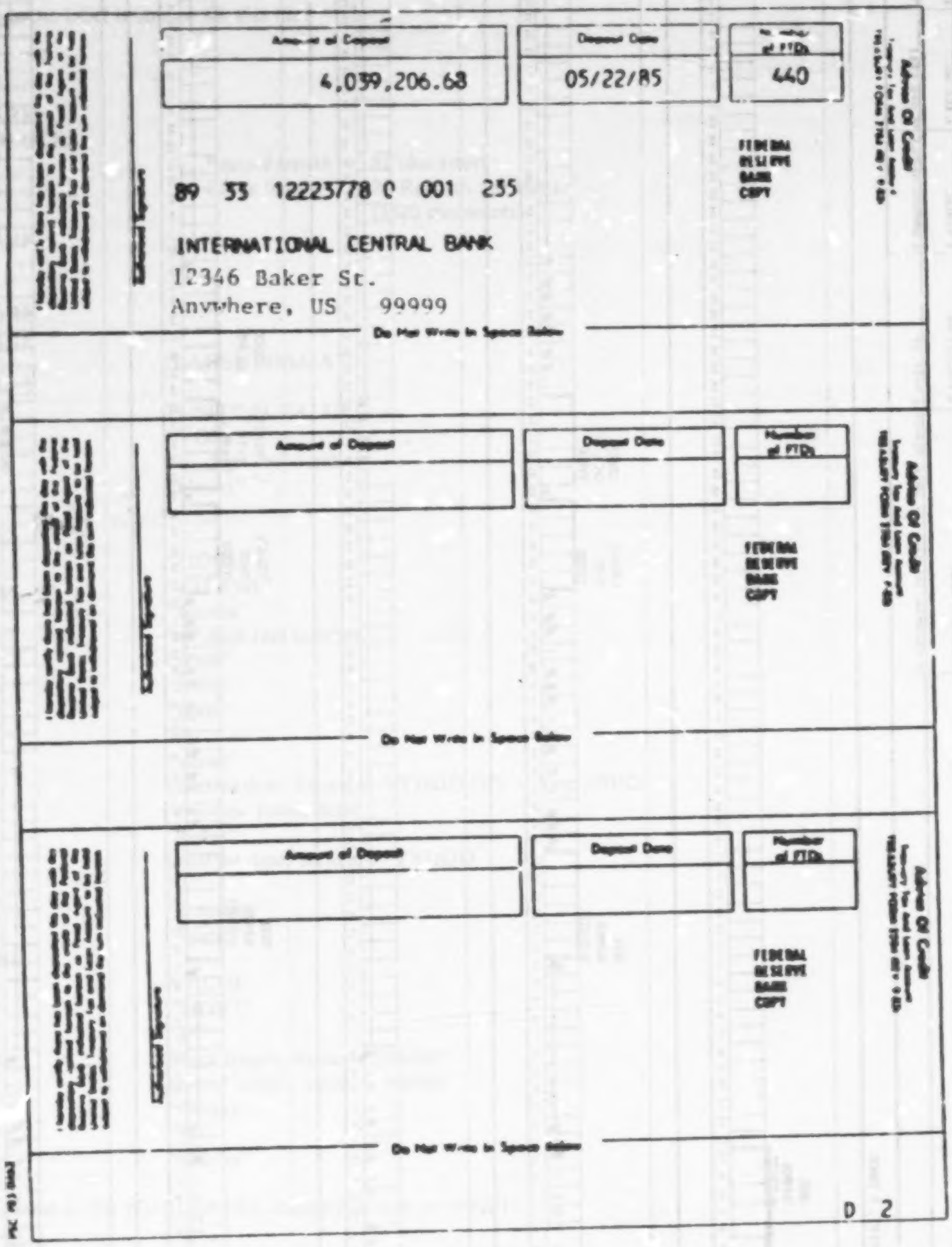
PAGE NO.

U. S. TREASURY DEPARTMENT - INTERNAL REVENUE SERVICE

GPO 918-133

FORM 3667 (REV. 11-66)

EXHIBIT 6



Advice Of Credit
Treasury Tax and Loan Account

Amount of Deposit	Deposit Date	Number of FTDs
4,039,206.68	05/22/85	440

FEDERAL RESERVE BANK COPY

89 33 12223778 0 001 235

INTERNATIONAL CENTRAL BANK
12346 Baker St.
Anywhere, US 99999

Do Not Write In Space Below

Advice Of Credit
Treasury Tax and Loan Account

Amount of Deposit	Deposit Date	Number of FTDs

FEDERAL RESERVE BANK COPY

Do Not Write In Space Below

Advice Of Credit
Treasury Tax and Loan Account

Amount of Deposit	Deposit Date	Number of FTDs

FEDERAL RESERVE BANK COPY

Do Not Write In Space Below

D 2

EXHIBIT 7
FTD TAPE PROOFLIST
DATA PROCESSING—IRS AGENT 5

AOC SERIAL NUMBER	FTD SEQUENCE NUMBER	EIN	FEDERAL SHORT-NAME	DEPOSIT TYPE	DEPOSIT PERIOD	FTD AMOUNT
227	409	32-0265898	TURN	941	06/85	8,812.09
	410	32-0269368	WY	941	06/85	22,381.32
	411	32-2070342	TUBA	941	06/85	3,078.06
	412	32-0271625	CUST	941	06/85	3,244.13
	413	32-0275886	ARIZ	941	06/85	17,032.56
	414	32-2076625	SWAR	941	06/85	4,986.40
	415	32-0285857	ELRI	941	06/85	60,340.23
	416	32-0290033	PHOE	941	06/85	28,166.80
	417	32-0293335	SWEE	941	06/85	9,289.19
	418	32-0296979	C&LI	941	06/85	5,733.72
	419	32-0297697	SW	941	06/85	25,225.85
	420	32-0299782	GMHO	941	06/85	28,242.38
	421	32-0307537	JCSG	941	06/85	8,060.32
	422	32-0308295	CRAI	941	06/85	13,330.67
	423	32-0309855	SC	941	06/85	4,744.93
	424	32-0313495	BUDW	941	06/85	14,996.39
*** AOC SUB-TOTAL *** 89 33 12223778 0 001 227						
228	001	32-0338622	LAKE	941	06/85	7,665.32
	002	32-0340417	MESA	941	06/85	9,512.14
	003	32-0342149	SPEE	941	06/85	4,358.36
	004	32-0349974	WOND	941	06/85	5,265.58
	005	32-0354348	DAVI	941	06/85	3,594.11
	006	32-0357093	PQ	941	06/85	5,343.17
	007	32-0357559	TQ	941	06/85	4,065.02

EXHIBIT 8

MASS STORAGE MEDIA

☐ CHARGE-OUT
☐ REMOTE LOG
☐ TRANSMITTAL

MAGNETIC TAPE OF FEDERAL TAX DEPOSITS

REPORTING AGENTS NAME AND ADDRESS (STREET, CITY, STATE AND ZIP CODE)

AGENT CONTACT:

NAME: ______________________

TELEPHONE: (   )   -

CYCLE:

I/O	TC	TAPE I.D. NUMBER	JOB-RUN-FILE-ID (FROM)	MEDIA SEQUENCE	DEPOSIT DATE	RETENTION (days)	STATUS	PROG. NO.	BLOCK COUNT	ERRORS	DR

ROUTING/REMARKS

SCHEDULING CONTROLS

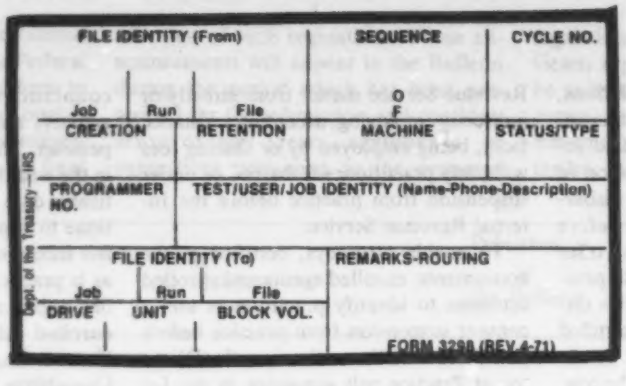
SIGNATURE

SHIP DATE:

Form **8482** (1-86)

☆ U.S. GOVERNMENT PRINTING OFFICE: 1986-491-486/41549   E.I. NO. 43-1110208

EXHIBIT 9



FILE IDENTITY (From)		SEQUENCE	CYCLE NO.
Job Run File		O F	
CREATION	RETENTION	MACHINE	STATUS/TYPE
PROGRAMMER NO.	TEST/USER/JOB IDENTITY (Name-Phone-Description)		
FILE IDENTITY (To)		REMARKS-ROUTING	
Job Run File			
DRIVE	UNIT	BLOCK VOL.	

Dept. of the Treasury—IRS

FORM 3298 (REV.4-71)

EXPEDITE

FEDERAL TAX DEPOSIT
ON MAGNETIC TAPE

DELIVER UNOPENED TO TAPE LIBRARY

BOX ____/____ OF ____/____

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Tevor Adel	Silver Spring, MD	Certified Public Accountant	Indefinite from June 2, 1986
John H. Peimann	Ottawa, KS	Certified Public Accountant	Twenty-One Months from June 1, 1986
John D. Raikos	Indianapolis, IN	Attorney	Indefinite from May 20, 1986
Vernon Rubel	Hickory, NC	Enrolled Agent	Indefinite from May 28, 1986
Wayne Boyer	Southfield, MI	Enrolled Agent	Eight Months from May 12, 1986
Thomas McPhee	McAllen, TX	Enrolled Agent	Indefinite from June 15, 1986
Glen R. Verber	Houston, TX	Certified Public Accountant	Ninety Days from May 19, 1986
Beverly Worth	Winona Lake, IN	Enrolled Agent	Five Years from June 17, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section Affected	Subject	Published in the Bulletin	Expiration Date for Submission of Views
26 CFR 1.88–1, 1.468A–1 through 1.468A–8 added	Nuclear decommissioning costs	1986–31 I.R.B. 22	Sept. 8, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor.
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federral Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

Finding List of Current Action on Previously Published Rulings[1]

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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Bulletin No. 1986–34
August 25, 1986

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

ADMINISTRATIVE

Rev. Proc. 86–34, page 4.
Information returns; magnetic media reporting. Requirements and conditions for filing information return Forms 1098, 1099, 5498, and W–2G on 8-inch magnetic diskette are set forth. Rev. Proc. 85–47 superseded.

Rev. Proc. 86–35, page 166.
Forms; bulk quantities to practitioners; charges. The handling and shipping charge for furnishing bulk quantities of forms to practitioners is adjusted. Rev. Proc. 84–38 superseded.

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Finding Lists begin on page 169.
Announcement of Suspensions on page 167.
Announcement of Notice of Proposed Rulemaking on page 168.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.602: Tax forms and instructions.

Rev. Proc. 86–34

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NOTE: THIS REVENUE PROCEDURE MAY ONLY BE USED TO PREPARE 8 INCH MAGNETIC DISKETTE SUBMISSIONS FOR TAX YEAR 1986 RETURNS. UPDATED COPIES ARE PUBLISHED EACH YEAR. PLEASE READ THIS PUBLICATION CAREFULLY. **PERSONS REQUIRED TO FILE MAY BE SUBJECT TO PENALTIES FOR FAILURE TO FOLLOW THE INSTRUCTIONS IN THIS REVENUE PROCEDURE.** THESE INCLUDE PENALTIES OF $50 PER DOCUMENT FOR EACH DOCUMENT SUBMITTED WITHOUT A TAXPAYER IDENTIFICATION NUMBER (TIN) OR WITH AN IN-

CORRECT TIN. YOU MAY ALSO BE SUBJECT TO AN ADDITIONAL $50 PENALTY PER DOCUMENT FOR EACH DOCUMENT NOT SUBMITTED ON MAGNETIC MEDIA IF YOU ARE REQUIRED TO FILE THIS WAY OR IF YOU FILE LATE. THE MAXIMUM PENALTY IS $50,000 (THERE IS NO MAXIMUM FOR CERTAIN FORMS 1099–INT, 1099–DIV, 1099–OID, 1099–PATR OR 5498 OR IF THE FAILURE TO FILE IS DUE TO INTENTIONAL DISREGARD OF THE FILING REQUIREMENTS). IRS **STRONGLY ENCOURAGES** FILERS TO REVIEW THEIR DATA FOR ACCURACY BEFORE SUBMISSION TO PREVENT ERRONEOUS NOTICES BEING MAILED TO PERSONS FOR WHOM REPORTS ARE FILED.

PART A.—GENERAL

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to provide the requirements and conditions for filing information return Forms 1098, 1099, 5498, and W–2G on 8 inch magnetic diskette. Other revenue procedures provide instructions for filing on magnetic tape, 5¼ inch magnetic diskette, and cassette or mini-disk. *THIS REVENUE PROCEDURE IS TO BE USED FOR THE PREPARATION OF TAX YEAR 1986 INFORMATION RETURNS ONLY.* THIS PROCEDURE IS UPDATED YEARLY TO REFLECT NECESSARY CHANGES. PLEASE READ THIS PUBLICATION CAREFULLY. Specifications for filing the following forms are contained in this procedure:

(a) Form 1098, Mortgage Interest Statement.

(b) Form 1099–A, Information Return for Acquisition or Abandonment of Secured Property.

(c) Form 1099–B, Statement for Recipients of Proceeds from Broker and Barter Exchange Transactions.

(d) Form 1099–DIV, Statement for Recipients of Dividends and Distributions.

(e) Form 1099–G, Statement for Recipients of Certain Government Payments.

(f) Form 1099–INT, Statement for Recipients of Interest Income.

(g) Form 1099–MISC, Statement for Recipients of Miscellaneous Income.

(h) Form 1099–OID, Statement for Recipients of Original Issue Discount.

(i) Form 1099–PATR, Statement for Recipients (Patrons) of Taxable Distributions Received From Cooperatives.

(j) Form 1099–R, Statement for Recipients of Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc.

(k) Form 5498, Individual Retirement Arrangement Information.

(l) Form W–2G, Statement for Recipients of Certain Gambling Winnings.

Specifications for filing Forms 1042S, 6248, 8027, W–2, and W–2P are contained in separate publications.

.02 Section 1.6045–1(1) of the Income Tax Regulations requires brokers and barter exchanges to use magnetic media to report *ALL* Form 1099–B data to IRS. *THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS.* Section 6011(e) of the Internal Revenue Code as amended by the Interest and Dividend Tax Compliance Act of 1983, Pub. L. 98–67, 1983–2 C.B. 352, 359, requires that any person, including corporations, partnerships, individuals, estates, and trusts, required to file more than 50 information returns *in the aggregate* for payments of certain interest (Forms 1099–INT and 1099–OID), dividends (Form 1099–DIV), or patronage dividends (Form 1099–PATR), for any calendar year, must file such returns on magnetic media. *THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS.* For example, if you must file 30 Forms 1099–DIV and 25 Forms 1099–INT, filing on magnetic media is required. In addition, for returns filed in 1987 (for tax year 1986), magnetic media reporting is required if you file 500 or more of *each* of the following forms: Forms W–2, W–2P, W–2G, 1098, 1099–A, 1099–G, 1099–MISC, 1099–R, 5498, 1042S, 6248, and 8027. THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS. Form W–2c is not included in these filing requirements. The 500 or more requirement for these forms will drop to 250 or more for returns filed in 1988 (for tax year 1987) and later years. Forms W–2 and W–2P are filed with the Social Security Administration (SSA), *NOT* Internal Revenue Service (IRS). At this time, corrected returns filed on Form W–2c with SSA are not required on magnetic media. These requirements shall not apply if you establish that it will cause you undue hardship. Refer to Part A, Sec. 5.

.03 This procedure also provides the requirements and specifications for diskette filing under the Combined Federal/State Filing Program. Refer to Part A, Sec. 14.

.04 The following revenue procedures and publications provide more detailed filing procedures for certain information returns:

(a) 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" provide further information on filing returns with IRS. These instructions are available at IRS offices.

(b) Rev. Proc. 84–24, 1984–1 C.B. 465, regarding preparation of transmittal documents (Forms 1096 and 4804) for information returns.

(c) Rev. Proc. 84–33, 1984–1 C.B. 502, regarding the optional method for agents to report and deposit backup withholding.

(d) Publication 1179, Specifications for Paper Substitutes for Forms 1096, 1098, 1099, 5498, and W–2G.

.05 This procedure supersedes the following revenue procedure: Rev. Proc. 85–47, 1985–2 C.B. 512, also published in Publication 1255 (Rev. 9–85), Requirements and Conditions for Filing Information Returns in the Forms 1098, 1099, 5498, and W–2G Series on Magnetic Diskette.

.06 Refer to Part A, Sec. 15 for definitions of terms used in this publication.

SEC. 2 BACKGROUND—PRIOR YEAR CHANGES (TAX YEAR 1985)

DUE TO NUMEROUS LEGISLATIVE AND FORMS CHANGES BETWEEN TAX YEARS 1984 AND 1985, CHANGES WERE NOT LISTED INDIVIDUALLY UNDER THIS SECTION. THE ENTIRE PUBLICATION WAS REVISED. FOR TAX YEAR 1985, SEE REV. PROC. 85–47, 1985–2 C.B. 512 FOR SPECIFIC CHANGES.

SEC. 3. NATURE OF CHANGES—CURRENT YEAR (TAX YEAR 1986)

.01 The following changes must be incorporated into your programs for tax year 1986.

.02 GENERAL CHANGES ARE AS FOLLOWS:

(a) The note on the cover and which follows the table of contents was revised to alert filers that their data should be reviewed for accuracy before submission to prevent erroneous notices to the persons for whom reports are filed.

(b) Part A, Sec. 1.02 lists the forms described in this revenue procedure that must be filed on magnetic media. *THESE REQUIREMENTS APPLY TO BOTH ORIGINAL AND CORRECTED RETURNS.* Corrected returns filed on Forms W–2c with SSA are not required at this time on magnetic media.

(c) A note was added to Part A, Sec. 4.01 to alert filers that applications to file Forms W–2 and W–2P on magnetic media are requested from SSA; however, requests for magnetic media related undue hardship waivers and extensions of time to file Forms W–2 and W–2P on magnetic media are requested from the IRS National Computer Center. Waiver requests for these forms must be filed by July 31, 1986, for tax year 1986 for returns to be filed in 1987.

(d) Transmitter Control Codes may be alpha/numeric. This has been noted in several places within the publication.

(e) The dates for submission of "test" files have been revised in Part A, Sec. 5. "Test" files should be submitted between August 15 and December 15 each year. Also, "test" data for the "A" Record must be actual data, not fictitious information.

(f) Part A, Sec. 5.04 has been revised to alert filers that a transmittal Form 4804, 4802 or computer generated substitute must accompany "test" files. The transmittal Form 4804 and 4802 have been updated for 1986. Agencies who produce a computer generated substitute must update their format for these forms. The Form 4804 now includes a checkbox 1 to indicate the type of file (*e.g.*, original, correction, replacement, test).

(g) Part A, Sec. 5 includes new information concerning undue hardship waiver requests. Filers are now required to submit Form 8508, Request for Waiver From Filing Information Returns on Magnetic Media. *THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS WITH THE EXCEPTION OF FORM W–2c.*

(h) Part A, Sec. 6 has been updated to include the retention requirements for information returns and the new affidavit requirements for transmittal documents.

(i) For documents filed on paper with the appropriate service center, it is no longer necessary to note on the transmittal Form 1096 that a portion of the returns are being filed on magnetic media. This has been deleted from Part A, Sec. 6.07.

(j) Part A, Sec. 6.08 has been reworded to clarify that reports from different branches for one payer, *if submitted on the same file,* must be consolidated under one "A" Record for each type of information return.

(k) A note has been added to Part A, Sec. 7 that Form 5498 is used to report amounts contributed during or after the calendar year but not later than April 15.

(l) Part A, Sec. 8 (h) has been added to inform filers who file extension requests for multiple payers that the request must include a list of all payers and their TINs (SSN or EIN).

(m) Part A, Sec. 10 alerts filers that the magnetic media filing requirements apply to both original and corrected returns with the exception of Form W–2c filed with SSA. Refer to Part A, Sec. 1 for the filing requirements. Corrected returns should be aggregated and submitted as soon as possible but not later than October 1 of each year. Also, corrections should be submitted only for the returns filed in error, not the entire file.

(n) In prior years, diskette position 6 of the "B" Record was used as the corrected return indicator. Part A, Sec. 10.01 indicates that this has now been changed to position 7. The Guidelines in Sec. 10 have also been updated to reflect this change. You must adjust your programs. This change was necessary to facilitate the need for a second position in the "B" Record, Document Specific Code field.

(o) Transmittal Form W–3G is now obsolete. This form was used to transmit paper Forms 1099–R and W–2G. These two forms are now to be transmitted to the service center with Form 1096.

(p) Two new charts were added to the publication last year to provide instructions for filing corrections on magnetic media and on paper forms. Chart 2, Guidelines for Filing Corrected Returns on Paper Forms has been deleted. The instructions for filing corrections on paper forms are now available in the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G."

(q) Part A, Sec. 10, Guidelines have been revised. If a return was filed with *NO* Payee TIN (SSN or EIN), or the return was filed with an incorrect Payee TIN, only one transaction is now necessary to make the correction.

(r) Part A, Sec. 12 has been completely revised. Refer to this section for specific changes.

(s) Service center addresses have been deleted from this publication. They are available in the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G."

(t) Part A, Sec. 14.02 has been revised to inform filers of the authorization to sign consent Form 6847. Filers who have received approval to file on this program in prior years may be required to resubmit a consent Form 6847 signed by each payer. Refer to Part A, Sec. 14.02 for further information.

(u) The dollar criteria in Table 2 of Part A, Sec. 14 has changed. For the state of Minnesota, Form 5498 must now be reported. Also, two footnotes for Minnesota have now been deleted: $10.01 for Savings and Loan Associations and Credit Unions; and $600.01 for Rents and Royalties.

(v) Acceptable foreign country codes have been added to Part A, Sec. 16 to assist you in developing the address field.

(w) Part B, Sec. 1.04 has been revised to indicate changes made to the external media labels. Form 5064 is the external media label and has been updated for tax year 1986. You must use the updated label for 1986. These will be included in your magnetic media reporting packages.

.03 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE PAYER/TRANSMITTER "A" RECORD:

(a) A note has been added to Part B, Sec. 3.03 to indicate that all alpha characters should be uppercase.

(b) Form 1099–MISC, Amount Code "8," Direct Sales Indicator, NOTE 1, has been clarified.

(c) Form 1099–OID, the title of Amount Code 2 has been changed from "Stated interest," to "Other periodic interest."

(d) Form 1099–R, the term "Insurance Contracts" has been added to the title of the form and insurance premiums has been added to Amount Code "5."

(e) Amount Code "7" has been added to Form 1099–R to report "State income tax withheld."

(f) A note has been added for reporting distributions from KEOGH plans on Form 1099–R.

(g) Form 5498, Amount Code "1" has been changed to report "Regular SEP contributions made in 1986 and 1987 for 1986." The regular SEP contributions have been deleted from Amount Code "3" and now appear separately as Amount Code "1."

(h) Form 5498, the title of Amount Code "4" has been changed to "Life insurance cost included in codes 1 or 3 (for endowment contracts only)."

(i) Amount Code "3" has been added for Form W–2G to report "State income tax withheld."

(j) The First Payer Name Line has been clarified for those reporting Form 1098, "Mortgage Interest Statement." *Refer to the First Payer Name Line field description for specific information.*

.04 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE PAYEE "B" RECORD:

(a) A note has been added to Part B, Sec. 5.03 concerning invalid addresses.

(b) A note has been added to Part B, Sec. 5.08 to indicate that all alpha characters should be uppercase.

(c) The Document Specific Code field length has been increased from 1 to 2 positions. Diskette positions 5–6 now represent this coding. This change was necessary due to multiple coding required in certain cases for Form 1099–R.

(d) Additional coding and clarification has been added to the Document Specific Code for Form 1099–R. A Code "9" represents PS 58 Costs; Code "P" represents excess contributions refunded plus earnings on such excess contributions taxable in 1985; Code "A" represents distributions that qualify for 10-year averaging; Code "B" represents distributions that qualify for the death benefit exclusion; and Code "C" indicates that the distribution qualifies for both "A" and "B."

(e) The Document Specific Code, Direct Sales indicator has been clarified.

(f) In prior years, diskette position 6 was used as the corrected return indicator. This has now changed to position 7. You must adjust your programs.

(g) Examples have been added to assist you in the development of the Name Control field.

(h) The Type of TIN indicator field has been clarified for those accounts that are questionable. Code "9" has been deleted.

(i) The Payer's Account Number for the Payee field has been clarified.

(j) The First Payee Name Line field description has been clarified for those reporting Form 1098, "Mortgage Interest Statement." *Refer to the First Payee Name Line field description for specific information.*

(k) The Payee City, Payee State, and Payee ZIP Code are three separate fields. If the payee lives outside of the United States, insert a "1" in position "1" of the Payee City field and spell out the name in the remaining positions. Use the appropriate Country Code as shown in Part A, Sec. 16 in the Payee State field. Some foreign countries utilize alpha characters in the ZIP Code. The use of alpha characters is only acceptable if there is a "1" in position "1" of the Payee City field.

.05 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE END OF PAYER "C" RECORD:

(a) Part B, Sec. 14 clarifies the totals required in the "C" Record.

(b) Part B, Sec. 14.03 provides instructions to assist you in the development of the "C" Record.

.06 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE END OF TRANSMISSION "F" RECORD:

(a) The Number of Payers field name and description have been reworded.

(b) The Number of Reels field description has been reworded.

.07 A new section has been added to the revenue procedure for filers who wish to submit double density 8 inch diskettes which contain sectors of 256 bytes instead of 128 bytes. Refer to Part C, Sec. 1 through Sec. 17 for Field Description and Record Layout information.

SEC. 4. WAGE AND PENSION INFORMATION FILED WITH SSA

.01 Section 8(b), Pub. L. 94–202, 1976–1 C.B. 503, enacted in January 1976, authorized the combined reporting of FICA detailed information in one consolidated annual W–2 (Copy A) to the Federal government. AS A RESULT, FORMS W–2 AND W–2P ARE TO BE FILED WITH SSA, NOT WITH IRS. Applications to file Forms W–2 and W–2P on magnetic media are to be mailed to SSA; however, undue hardship waivers and extensions of time to file Forms W–2 and W–2P are to be requested from the IRS National Computer Center, *NOT* from SSA. Requests for undue hardship exemption for these two forms must be filed with the IRS National Computer Center by July 31, 1986, for tax year 1986 for returns to be filed in 1987. Refer to Part A, Sec. 13 for the address and Part A, Sec. 5.08 and Sec. 8 for the required information.

.02 SSA will accept magnetic media filing of Forms W–2 and W–2P and has issued the following concerning this: TIB-4a, "*Magnetic Tape Reporting,* Submitting FICA Wage and Tax Data to the Social Security Administration"; TIB–4b, "*Magnetic Tape Reporting,* Submitting Annuity, Pension, Retired Pay or IRA Payment to the Social Security Administration"; and TIB–4c, "*Diskette Reporting,* Submitting FICA Wage and Tax Data to the Social Security Administration." Applications for filing Forms W–2 and W–2P on magnetic media appear in TIBs–4a, 4b, and 4c.

.03 Copies of Social Security Administration publications TIB–4a, 4b, and 4c are available from any local Social Security Administration office or the SSA Regional Magnetic Media Coordinators.

SEC. 5. APPLICATION FOR MAGNETIC MEDIA REPORTING AND REQUESTS FOR UNDUE HARDSHIP WAIVERS

.01 For purposes of this revenue procedure, the *PAYER* includes the person making payments, a recipient of mortgage interest payments, a broker, a barter exchange, a trustee or issuer of an IRA, SEP or DEC, or a lender who acquires an interest in secured property or who has reason to know that the property has been abandoned. The *TRANSMITTER* is the organization preparing the diskette file. The payer and transmitter may be the same organization. Payers or their transmitters are required to complete Form 4419, Application for Magnetic Media Reporting of Information Returns. A copy of this form, for your use, is included in this publication. Requests for additional information or forms relating to magnetic media processing should be addressed to the National Computer Center. Beginning January 1, 1986, magnetic media processing was centralized at the National Computer Center. The address is listed in Part A, Sec. 13.

.02 Applications should be filed with the National Computer Center before "test" files are submitted. ("Test" files must be submitted between August 15 and December 15 each year.) IRS will act on an application and notify the applicant, in writing, of authorization to file. A five character alpha/numeric *Transmitter Control Code* will be assigned and included in an acknowledgement letter within 30 days of receipt of the application. Diskette returns may not be filed with IRS until the application has been approved. Do not enter blanks in the "A" Record Transmitter Control Code field; enter the five character alpha/numeric Transmitter Control Code that is assigned to you by IRS after you have filed an application and it has been approved. Applications for approval to file Forms W–2 and W–2P on magnetic media must be filed with SSA, *NOT* with IRS. Refer to Part A, Sec. 4.

.03 After you have received approval to file on magnetic media, you do not need to reapply each year; however, notify IRS in writing if:

(a) there are hardware or software changes that would affect the characteristics of the magnetic media submission (*e.g.*, changing from diskette to tape filing or vice versa) a new Transmitter Control Code may be necessary or,

(b) you discontinue filing on magnetic media for a year (your five character alpha/numeric Transmitter Control Code may be reassigned.)

If either of these conditions applies to you, you should contact IRS for clarification. In *ALL* correspondence, refer to your current five character alpha/numeric Transmitter Control Code to assist IRS in locating your files.

.04 IRS will assist new filers with their initial diskette submission by reviewing "*test*" files submitted in advance of the filing season. The "test" data should be *actual* data for the "A" Record, not fictitious information. This applies to all records submitted in the "test" file. Approved payers or transmitters should submit "*test*" files to the National Computer Center. You *MUST* submit a "*test*" file in order to participate in the Combined Federal/State Program; however, you are encouraged to submit "*test*" files if you are a new filer on magnetic media. As a guideline, IRS prefers that all "*test*" files be submitted between August 15 and December 15 each year. Refer to Part A, Sec. 13 for the address. Do not submit "*test*" diskettes after December 15. If you are unable to submit your "*test*" file by this date, you may *only* send a sample hardcopy printout or diskette dump that shows a sample of each type of record (A, B, C, K, and F) *used* to the National Computer Center. Clearly mark the hardcopy printout or diskette dump as "TEST DATA" and include identifying information such as name, address, and telephone number of someone familiar with the "*test*" print or diskette dump who may be contacted to discuss its acceptability. With all "*test*" data, include a transmittal Form 4804, 4802 or computer generated substitute marked as "TEST DATA" that identifies your five character alpha/numeric Transmitter Control Code and total record and money amounts. The "*test*" data must be a sample of *actual* data coded according to the proper revenue procedure. The transmittal Form 4804 and 4802 have been updated for tax year 1986. Agencies who produce a computer generated substitute must include the additional information required on these forms. The Form 4804 now includes a checkbox 1 to indicate the type of file (*e.g.*, original, correction, replacement, test).

.05 If your magnetic media files have been prepared for you in the past by a service agency, and you now have computer equipment compatible with that of IRS and wish to prepare your own files, you must request your own five character alpha/numeric Transmitter Control Code by filing an application, Form 4419, as described above.

.06 If you as an individual or organization are an approved filer on magnetic media and you change your name or the name of your organization, please notify the National Computer Center, in writing, so that your file may be updated to reflect the proper name.

.07 In accordance with section 1.6041–7(b) of the Income Tax Regulations, payments to providers of medical and health care services from separate departments of a health care carrier may be reported as separate returns on magnetic media. In this case, the headquarters office will be considered to be the transmitter, and the individual departments of the company filing reports will be considered to be payers. A *single* application form covering *all* the departments that will be filing on diskette should be submitted. One five character alpha/numeric Transmitter Control Code may be used for all departments.

.08 Any person required to file original or corrected returns on magnetic media may request a waiver from the filing requirements by submitting Form 8508, Request for Waiver From Filing Information Returns on Magnetic Media, with the IRS National Computer Center if filing on magnetic media would be an undue hardship. Requests for waivers for Forms W–2 and W–2P are due by July 31, 1986, for tax year 1986 for returns to be filed in 1987. For all other returns required to be filed on magnetic media, waiver requests must be filed at least 90 days before the returns are due. This waiver, if approved, will only provide exemption from magnetic media filing for one tax year. Filers may not apply for a waiver for more than one tax year at a time. You must reapply each year that a waiver is necessary. Copies of Form 8508 may be obtained from the IRS National Computer Center. See Part A, Sec. 13 for the address.

.09 Section 1.6045–1(l) of the Income Tax Regulations requires brokers and barter exchanges to use magnetic media in reporting *ALL* Form 1099–B data to IRS. Generally, *NEW* brokers and *NEW* barter exchanges may request an undue hardship exemption by filing a request for waiver with the National Computer Center by the end of the second month following the month in which they became a broker or barter exchange.

.10 *All* requests for magnetic media related undue hardship exemptions should be submitted to the IRS National Computer Center at least 90 days before the due date of the return except as stated in Sec. 5.09. All magnetic media related undue hardship requests for Forms W–2 and W–2P are to be filed with the IRS National Computer Center, not SSA and must be filed by July 31, 1986, for tax year 1986 for returns to be filed in 1987. Refer to Part A, Sec. 13 for the address.

.11 If you request a waiver from filing on magnetic media and it *is* approved, *do not send a copy of the approved waiver to the service center where you file your paper returns.* Keep the waiver for your records. Do *not* staple, paperclip or use rubberbands on any scannable forms. Paper information returns are read by an optical scanner (OCR) at the service centers.

.12 Waivers are granted on a case-by-case basis and may be approved at the discretion of the National Computer Center. Refer to Part A, Sec. 13 for the address.

.13 If you are required to file on magnetic media but fail to do so, and you do not have an approved waiver on record, you may be subject to a failure to file penalty. Refer to Sec. 6.01 below.

.14 *An approved waiver from filing information returns on magnetic media does not provide exemption from filing; you MUST still file your information returns on acceptable paper forms.*

.15 A magnetic media reporting package, which includes all the necessary transmittals, labels, and instructions, will be mailed to the last known address of all approved filers each year.

SEC. 6. FILING OF MAGNETIC MEDIA REPORTS AND RETENTION REQUIREMENTS

.01 If you do not file your returns on time, you may be subject to a $50 per document failure to file penalty. If you file without following the instructions in this revenue procedure, you may also be subject to a $50 per document failure to file penalty. The maximum penalty is $50,000. However, there is no maximum penalty for returns of 1099–INT, 1099–OID, 1099–DIV, 1099–PATR, 5498 or if the failure to file is due to intentional disregard of the filing requirements.

.02 Generally, you are now subject to a $50 penalty for *each* failure to include the payee's correct TIN on an information return unless the payer can demonstrate that the payer met the due diligence requirements. Refer to Part A, Sec. 11.

.03 Rev. Proc. 84–24, 1984–1 C.B. 465, gives detailed information on preparing transmittal documents (Forms 1096 and 4804) for information returns and is available at IRS offices. Specific guidelines are given on how to report the payer's name, address, and TIN on transmittal documents and information returns. Instructions for multiple transmittals and the submission of transmittals by service bureaus or agents are also covered.

.04 *THE DISKETTE RECORDS ARE TO BE SUBMITTED TO THE NATIONAL COMPUTER CENTER; HOWEVER, PAPER INFORMATION RETURNS ARE TO CONTINUE TO BE FILED WITH THE APPROPRIATE SERVICE CENTERS.* Form 4804, Transmittal of Information Returns Reported on Magnetic Media, must accompany diskette submissions. If you file for multiple payers and have the authority to sign the affidavit on Form 4804, you should also submit Form 4802, Transmittal for Multiple Magnetic Media Reporting.

For IRS to ensure that your actual data records were formatted following THIS revenue procedure, include a hardcopy printout, fast print or diskette dump of the first five and last five blocks of the data that shows a sample of each type of record (A, B, C, K, and F) used on the diskette. This will be reviewed prior to actual processing to ensure that the data is in the proper format. *Be sure to include Form 4804, 4802 or computer generated substitute with your diskette shipment. DO NOT MAIL THE DISKETTES AND THE TRANSMITTAL DOCUMENTS SEPARATELY.* IRS encourages the use of a computer generated Form 4804 which includes *all* necessary information requested on the actual form.

Paper information returns must be transmitted to the appropriate service center using Form 1096, Annual Summary and Transmittal of U.S. Information Returns. *Do not send information returns filed on paper forms to the National Computer Center.*

.05 The affidavit for Form 4804 should be signed by the payer; however, the transmitter, service bureau, paying agent, or disbursing agent may sign the affidavit on behalf of the payer if all of the following conditions are met:

(a) It has the authority to sign the affidavit under an agency agreement (either oral, written or implied) that is valid under the state law.

(b)(i) It has the responsibility (either oral, written or implied) conferred on it by the payer to request the TINs of recipients (or others for whom information is being reported),

OR

(ii) If the return of more than one payer is included in a single tape submission, covered by a single Form 4804, each payer has attested by affidavit to the transmitter, service bureau, paying agent or disbursing agent that the payer has complied with the law in attempting to secure correct TINs

(c) It signs the affidavit and adds the caption "For: (name of payer)."

.06 Although a duly authorized agent signs the affidavit, the payer is held responsible for the accuracy of the Form 4804, and the payer will be liable for penalties for failure to comply with filing requirements.

.07 DO NOT REPORT THE SAME INFORMATION ON PAPER FORMS THAT YOU REPORT ON MAGNETIC MEDIA. IF YOU REPORT PART OF YOUR RETURNS ON PAPER AND PART ON MAGNETIC MEDIA, BE SURE THAT DUPLICATE RETURNS, WITH THE SAME INFORMATION, ARE NOT INCLUDED ON BOTH. This does not mean that corrected documents are not to be filed. If a return has been prepared and submitted improperly, you must file a corrected return as soon as possible. Refer to Part A, Sec. 10 for requirements and instructions on filing corrected returns.

.08 Reports from different branches or locations for one payer, if submitted on the same file, *MUST* be consolidated under one Payer/Transmitter "A" Record for each type of information return. For example, all Forms 1099–INT for the same payer on a single file must be sorted together under one Payer/Transmitter "A" Record followed by the appropriate "B" Records and one "C" Record.

.09 Payers are required to retain a copy of the information returns filed with IRS or the ability to reconstruct the data for at least three years.

.10 Before submitting magnetic media files, include the following:

(a) A signed Form 4804 or computer generated substitute.

(b) A Form 4802 (if you transmit for multiple payers).

(c) A hard copy printout or listing of the first five and last five blocks of your file. The listing should show a sample of each type of record (A, B, C, K, and F) used on the magnetic media being submitted.

(d) The magnetic media with an external identifying label as described in Part B, Sec. 1.

(e) On the outside of the shipping container, include a Form 4801 or a substitute for the form which reads "DELIVER UNOPENED TO TAPE LIBRARY—MAGNETIC MEDIA REPORTING—BOX ■■ of ■■." If there is only one container, mark the outside as Box *1* of *1*. For multiple containers, include the sequence (*e.g.*, Box *1* of *33*, *2* of *33*, etc.).

(f) If you were granted an extension, include a copy of the approval letter with the magnetic media shipment.

.11 IRS will not pay or accept "Collect on Delivery" or "Charged to IRS" shipments of reportable tax information that an individual or organization is legally required to submit.

.12 Files returned to you due to coding or format errors are to be corrected and returned to IRS within 30 days of your receipt or the payer may be subject to a failure to file penalty.

SEC. 7. FILING DATES

.01 The dates prescribed for filing paper returns with IRS also apply to magnetic media filing. Magnetic media reporting to IRS for Forms 1098, 1099, and W–2G must be on a calendar year basis. Form 5498 is used to report amounts contributed during or after the calendar year but not later than April 15.

.02 Information returns filed on magnetic media for Forms 1098, all types of Forms 1099, and W–2G must be submitted to IRS and postmarked by February 28. The due date for furnishing the required copy or statement to the recipient is January 31.

.03 Information returns filed on magnetic media for Form 5498 must be submitted to IRS and postmarked by May

31. Copies of this form or statements are due to the participant by May 31 for contributions made to IRAs and SEPs for the prior calendar year; however, participant copies or statements for DECs are due at the time the contribution is made or January 31, whichever is later. Form 5498 is filed for contributions to be applied to 1986 that are made between January 1, 1986, and April 15, 1987.

SEC. 8. EXTENSIONS OF TIME TO FILE

.01 If a payer or transmitter of returns *on magnetic media* filed with IRS or SSA is unable to submit their magnetic media file by the dates prescribed in Sec. 7.02 and 7.03 above, submit a letter requesting an extension of up to 30 days to file, as soon as you are aware that an extension will be necessary. In order to be considered, the request *MUST* be filed *before* the due date of the return; otherwise, you will be subject to the late filing penalty. The letter should be sent to the attention of the Magnetic Media Reporting Program at the IRS National Computer Center. See Part A, Sec. 13 for the address. The request should include:

(a) The filer's (or transmitter's, if filing for multiple payers) name and address.

(b) The filer's Taxpayer Identification Number (SSN or EIN).

(c) The tax year for which the extension of time is requested: Tax Year 1986.

(d) The name and telephone number of a person to contact who is familiar with the request.

(e) The type of returns and expected volume (*e.g.*, 5000 Forms 1099-INT).

(f) The five character alpha/numeric Transmitter Control Code assigned to the organization or individual requesting the extension (if a number has been assigned).

(g) The reason for the delay and date that you *will* be able to file.

(h) If you file for multiple payers, the request must include a list of all payers and their TIN (SSN or EIN).

An approved extension *for magnetic media filing* does not provide additional time for supplying a copy to the payee.

.02 If an extension of time to file on magnetic media is granted by the National Computer Center, a *copy* of the letter *granting the extension MUST* be attached to the transmittal Form 4804 or computer generated submission when the file is submitted.

SEC 9. PROCESSING OF MAGNETIC MEDIA REPORTS

.01 All data received at the National Computer Center for processing will be given the same protection as individual returns (1040), and will be returned to the originator after processing. Files that are received timely by the National Computer Center will be returned to the filers by August 15 of the year in which submitted.

.02 *Due to the volume of input received and the cost to return special containers, special shipping containers should not be used for transmitting data to the National Computer Center since IRS cannot guarantee return of such containers.*

.03 Files will be returned to you for correction if they are unprocessable due to format or coding errors, or by the request of the filer. Unprocessable files must be corrected and returned to the National Computer Center within 30 days of your receipt or the payer may be subject to a failure to file penalty. The corrected files will be returned to the filer by the National Computer Center within 6 months of receipt. PLEASE BE SURE THAT YOUR FORMAT AND CODING COMPLY WITH THIS REVENUE PROCEDURE. *THIS REVENUE PROCEDURE IS TO BE USED FOR THE PREPARATION OF TAX YEAR 1986 INFORMATION RETURNS ONLY.* LEGISLATIVE AND FORMS CHANGES AFFECTING INFORMATION RETURNS MAY OCCUR EACH YEAR. THIS PROCEDURE IS UPDATED TO REFLECT NECESSARY CHANGES. PLEASE READ THIS PUBLICATION CAREFULLY.

SEC. 10. HOW TO FILE CORRECTED RETURNS

.01 The filing requirements listed in Part A, Sec. 1 apply to both original and corrected returns. Corrections should be aggregated and filed as soon as possible but not later than October 1 of each year. *ALL FIELDS OR BOXES MUST BE COMPLETED WITH THE CORRECT INFORMATION, NOT JUST THE DATA FIELDS NEEDING CORRECTION.* Submit corrections only for the returns filed in error, not the entire file. If your complete file is in error, contact the National Computer Center immediately. If you file corrected returns on paper forms, submit Copy A to the appropriate service center. There are numerous types of errors. It may require more than one transaction to properly correct the initial error. In prior years, diskette position 6 of Sector 1 of the "B" Record was used as the corrected return indicator. This has now been changed to position 7. You must adjust your program. You are strongly encouraged to read this *ENTIRE* section before attempting to make *ANY* correction. If the initial return was filed as an aggregate, you must consider this in filing the corrected return.

.02 Corrected returns submitted to IRS on magnetic media, using a "G" coded Payee "B" Record, may be submitted on the same diskette as those corrections submitted *without* the "G" code; however, they must be submitted using a separate "A" Record. Corrected returns for different tax years may *not* be submitted on the same file. Corrected returns are to be identified as corrections on the transmittal document and the *EXTERNAL* affixed label of the file.

.03 The instructions that follow will provide information on how to file corrected returns on magnetic media. The 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W-2G" provide more specific instructions for filing corrections on paper forms and are available from IRS.

.04 *If you are not required to file your corrections on magnetic media and you file them on paper forms, do not submit the paper returns to the National Computer Center. All paper returns, whether original or corrected, must be filed with the appropriate service center. Corrected returns filed on magnetic media must be filed with the National Computer Center.* Refer to Part A, Sec. 13 for the address.

.05 Statements to the recipient or participant should be identified as "CORRECTED" and should be provided to them as soon as possible.

.06 If you file corrected returns on paper forms, use IRS forms or acceptable OCR scannable paper substitutes. Pinhole feeds on the forms are not acceptable. Always submit Copy A to the appropriate service center. *NOTE:* Form W-2G is not required to be in OCR scannable format. Publication 1179, "Specifications for Paper Substitutes for Forms 1096, 1098, 1099, 5498, and W-2G" provides requirements and instructions.

.07 For instructions on filing information returns with IRS, refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W-2G." If these instructions are not included in your magnetic media reporting packages, request a copy from IRS.

.08 Type or machine print in black carbon based ink all information on returns filed on paper. Print money amounts without dollar signs ($), ampersands (&), asterisks (*), commas (,), or other special characters. Use decimal points (.) to indicate dollars and cents on paper forms only.

.09 Use the proper form. If you are in doubt, review the instructions noted in .07 above or contact IRS.

.10 Use only the boxes provided on the paper forms. Do not add additional boxes.

.11 Do not change the title of any box on any forms and do not insert data in the untitled shaded areas.

.12 Use the same name and TIN (SSN or EIN) for the filer on the Form 1096 transmittal form and all related forms that follow.

.13 A separate transmittal Form 1096 is required for each *type* of paper information return filed in the 1098, 5498, W–2G, and 1099 series. DO NOT USE THE SAME TRANSMITTAL DOCUMENT TO FILE ORIGINAL AND CORRECTED RETURNS WHETHER ON PAPER FORMS *OR* MAGNETIC MEDIA. A transmittal Form 4804 or computer generated substitute is used to transmit magnetic media. A Form 4802 is a *continuation* form for a Form 4804. Please utilize a Form 4802 if you file on magnetic media for multiple payers and are an authorized agent for the payers.

.14 Do not cut, staple, fold, paperclip, tape, or use rubberbands on any paper information returns filed with IRS. This could impair the OCR scanning process. No photocopies of any forms are allowable.

.15 Use the correct tax year's forms to file information returns with IRS (*i.e.*, do not submit tax year 1986 returns using 1985 forms). The same is true for magnetic media filing. You must submit your returns filed on magnetic media using the revenue procedure for the tax year of the returns. Forms and revenue procedures are normally updated each year to include necessary changes.

.16 Most information returns contain a "VOID" box and a "CORRECTED" box. The "VOID" box is used only if you make an error while typing or printing the paper forms. Mark this box ONLY when you wish the return to be disregarded or passed over. The OCR scanner at the service centers *will not read* a "VOID" return; it will pass over it and go to the next form if the "VOID" box is marked. Do not confuse the "VOID" box and the "CORRECTED" box.

.17 On magnetic media files, the Payee "B" Record provides space to enter a Payer's Account Number for the Payee. This same account number may be provided on paper forms. In order to properly file corrected returns, this number will help identify the appropriate incorrect return. DO NOT ENTER A TIN (SSN OR EIN). *A PAYER'S ACCOUNT NUMBER FOR THE PAYEE MAY BE A CHECKING ACCOUNT NUMBER, SAVINGS ACCOUNT NUMBER, SERIAL NUMBER OR ANY OTHER NUMBER ASSIGNED TO THE PAYEE BY THE PAYER, THAT WILL DISTINGUISH THE SPECIFIC ACCOUNT. THIS NUMBER MUST APPEAR ON THE INITIAL RETURN AND ON THE CORRECTED RETURN IN ORDER TO IDENTIFY AND PROCESS THE CORRECTION PROPERLY.*

.18 REVIEW THE GUIDELINES THAT FOLLOW. The types of errors made will *normally* fall under one of the three categories listed. Next to each *type* of error made, you will find a list of instructions to tell you how to *properly* file the corrected return for *that* type of error. READ ALL OF THE INSTRUCTIONS LISTED AND FOLLOW THEM FOR THE TYPE OF ERROR MADE ON THE INITIAL RETURN. *IN SOME CASES TWO TRANSACTIONS ARE REQUIRED TO PROPERLY FILE CORRECTIONS. IF THE ORIGINAL RETURN WAS FILED AS AN AGGREGATE, YOU MUST CONSIDER THIS IN FILING THE CORRECTED RETURNS.*

Guidelines for Filing Corrected Returns on Magnetic Media

(PLEASE READ SEC. 10.01 THROUGH 10.18 OF THIS PUBLICATION BEFORE MAKING *ANY* CORRECTIONS)

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
1. Original return was filed with *NO* Payee TIN (SSN or EIN), *OR* the return was filed with an *INCORRECT* Payee TIN.	A. *Form 4804 and 4802 (or computer generated substitute)* 1. Prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers), or a computer generated substitute, that includes information related to this new file. 2. Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute. 3. Provide *ALL* requested information correctly. 4. Include a hardcopy print, listing or diskette dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format.* 5. If you are a Combined Federal/State filer, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer.

Guidelines for Filing Corrected Returns on Magnetic Media—Continued

(PLEASE READ SEC. 10.01 THROUGH 10.18 OF THIS PUBLICATION BEFORE MAKING *ANY* CORRECTIONS)

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
	B. *1098, 1099 Series, 5498 and W-2G Returns* 1. Prepare a new file. 2. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported. The information in the "A" Record will be the same as it was in the original submission. 3. The Payee "B" Record must contain exactly the same information as submitted previously *EXCEPT* insert a "G" code in diskette position 7 of the "B" Record and supply the correct TIN (SSN or EIN). (In prior years, diskette position 6 of Sector 1 of the "B" Record was used as the corrected return indicator. This has now been changed to position 7. You must adjust your programs.) 4. Corrected returns submitted to IRS using a "G" coded "B" Record may be submitted on the same diskette as those returns submitted *without* the "G" code; however, separate "A" Records are required. 5. Mark the *EXTERNAL* label of the diskette "MAGNETIC MEDIA CORRECTION." 6. Submit the diskette(s), a diskette dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for the address.)
2. Original return was filed with an incorrect money amount(s) in the Payee "B" Record, *OR* a money amount was reported using an incorrect Payment Amount Indicator Code in the original Payer/Transmitter "A" Record. Correct *Type Of Return* indicator was used in the "A" Record. (NOTE: If the wrong *Type Of Return* indicator was used, see number 3 of this chart.)	A. *Form 4804 and 4802 (or computer generated substitute)* 1. Prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers), or a computer generated substitute, that includes information related to this new file. 2. Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute. 3. Provide *ALL* requested information correctly. 4. Include a hardcopy print, listing or diskette dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format*. 5. If you are a Combined Federal/State filer, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer. B. *1098, 1099 Series, 5498 and W-2G Returns* 1. Prepare a *new* file. 2. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported. The information in the "A" Record will be the same as it was in the original submission EXCEPT, the *correct* Amount Indicators will be used. 3. The Payee "B" Record must contain exactly the same information as submitted previously *EXCEPT*: insert a "G" code in diskette position 7 of the "B" Record *AND* report the correct payment amounts as they should have been reported on the initial return. (In prior years, diskette position 6 of Sector 1 of the "B" Record was used as the corrected return indicator. This has now

Guidelines for Filing Corrected Returns on Magnetic Media—Continued

(PLEASE READ SEC. 10.01 THROUGH 10.18 OF THIS PUBLICATION BEFORE MAKING *ANY* CORRECTIONS)

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
	been changed to position 7. You must adjust your programs.) 4. Corrected returns submitted to IRS using a "G" coded "B" Record may be submitted on the same diskette as those returns submitted *without* the "G" code; however, separate "A" Records are required. 5. Mark the *EXTERNAL* label of the diskette "MAGNETIC MEDIA CORRECTION." 6. Submit the diskette(s), a diskette dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for the address.)
3. Original return was filed using the WRONG *Type of Return* indicator in the Payer/Transmitter "A" Record. (For example, a return was coded using the *Type of Return* indicator for 1099–DIV and it should have been coded 1099–INT.) THIS WILL REQUIRE TWO SEPARATE TRANSACTIONS TO MAKE THE CORRECTION PROPERLY. READ AND FOLLOW *ALL* INSTRUCTIONS FOR *BOTH* TRANSACTIONS 1 AND 2.	*TRANSACTION 1:* Identify return submitted with an incorrect Type Of Return indicator A. *Form 4804 and 4802 (or computer generated substitute)* 1. Prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers), or a computer generated substitute, that includes information related to this new file. 2. Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute. 3. Provide *ALL* requested information correctly. 4. Include a hardcopy print, listing or diskette dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format.* 5. If you are a Combined Federal/State filer, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer. B. *1098, 1099 Series, 5498 and W–2G Returns* 1. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported. The information in the "A" Record will be exactly the same as it was in the original submission using the same incorrect type of return indicator. 2. The corrected Payee "B" Record must contain the same information as submitted previously *EXCEPT:* insert a "G" code in diskette position 7 of the "B" Record and for *ALL* payment amounts *used,* enter "0" (zero). (In prior years, diskette position 6 of Sector 1 of the "B" Record was used as the corrected return indicator. This has now been changed to position 7. You must adjust your programs.) 3. Corrected returns submitted to IRS using a "G" coded "B" Record may be submitted on the same diskette as those returns submitted *without* the "G" code; however, separate "A" Records are required. 4. Mark the *EXTERNAL* label of the diskette "MAGNETIC MEDIA CORRECTION." 5. Submit the diskette(s), a diskette dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for the address.)

Guidelines for Filing Corrected Returns on Magnetic Media—Continued

(PLEASE READ SEC. 10.01 THROUGH 10.18 OF THIS PUBLICATION BEFORE MAKING *ANY* CORRECTIONS)

Error Made on the Original Return Filed on Magnetic Media

How To File the Corrected Return on Magnetic Media

TRANSACTION 2: Report correct information

A. *Form 4804 and 4802 (or computer generated substitute)*

1. If you submit records with the corrected information on a separate diskette from those that are "G" coded, prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers), or a computer generated substitute, that includes information related to this new file.
2. Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute.
3. Provide *ALL* requested information correctly.
4. Include a hardcopy print, listing or diskette dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format.*
5. If you are a Combined Federal/State filer, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer.

B. *1098, 1099 Series, 5498 and W–2G Returns*

1. Prepare a *new* file with the correct information in *ALL* records.
2. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported and use the correct Type Of Return indicator.
3. *Do not code the Payee "B" Record as a corrected return for this type of correction.* (Remove the "G" Code.)
4. Provide all of the correct information.
5. Mark the *EXTERNAL* label of the diskette "MAGNETIC MEDIA CORRECTION."
6. Submit the diskette(s), a diskette dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for the address.)

SEC. 11. TAXPAYER IDENTIFICATION NUMBERS

.01 Under section 6109 of the Internal Revenue Code, recipients of all reportable payments on information returns are required to furnish taxpayer identification numbers (TINs) to the payer. The number must be furnished to the payer whether or not the payee is required to file a tax return or is covered by social security. Refer to Part A, Sec. 15 for a definition of taxpayer identification number (TIN).

.02 The recipient's TIN is used to associate and verify amounts reported to IRS with corresponding amounts on tax returns. Therefore, it is particularly important that correct social security and employer identification numbers for payees be provided on magnetic media or paper forms submitted to IRS. *DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS.*

.03 Under section 6676 of the Internal Revenue Code, a $50 penalty applies for each failure to furnish a TIN to another person who is required to file an information return, and for each failure to include a TIN on an information return. The penalty applies unless the failure to comply is due to reasonable cause and not willful neglect.

.04 With respect to all payers of interest and dividends, section 6676 of the Internal Revenue Code provides that the payer must self-assess a *$50 penalty* for each failure to include a payee's TIN or each inclusion of an incorrect TIN on an information return, unless the payer can demonstrate the payer met the due diligence requirements in attempting to acquire correct TINs for payees. Use Form 8210, Self-Assessed Penalties Return.

.05 For any reportable payment, if the payee fails to provide a TIN to the payer, then backup withholding must be instituted for that payee. If the payer receives another TIN in the manner required from the payee within 30 days of notice from IRS, no backup withholding is required. If the payee has applied for a TIN, the payee may certify to this on Form W–9 by noting "Applied For" in the TIN block and by signing the form. This form then becomes an "awaiting-TIN certificate." If the TIN is not received and certified, if required, within 60 days, begin withholding and continue until you receive a TIN in the manner required.

.06 The TIN to be furnished to IRS depends primarily upon the manner in which the account is maintained or set up on the payer's record. The TIN to be provided must be that of the owner of the account. If the account is recorded in more than one name, furnish the TIN and name of one of the owners of the account. The TIN provided must be associated with the name of the payee provided in the first name line of the Payee "B" Record. For individuals, including sole proprietors, the payee TIN is the payee's social security number. For other entities, the payee TIN is the payee's employer identification number.

.07 Sole proprietors who are payers should show their employer identification number in the Payer/Transmitter "A" Record. However, sole proprietors who are not otherwise required to have an employer identification number should use their social security number.

.08 Sole proprietors' social security numbers must be used in the Payee "B" Record.

.09 The charts below will help you determine the number to be furnished to IRS for recipients of reportable payments (payees).

CHART 1. Guidelines for Social Security Numbers

For this type of account—	In the Taxpayer Identification Number field of the Payee "B" Record, enter the SSN of—	In the First Payee Name Line of the Payee "B" Record, enter the name of—
1. An individual's account.	The individual.	The individual.
2. A joint account (Two or more individuals, husband and wife).	The actual owner of the account. (If more than one owner, the first individual on the account.)	The individual whose SSN is entered.
3. Account in the name of a guardian or committee for a designated ward, minor, or incompetent person.	The ward, minor, or incompetent person.	The individual whose SSN is entered.
4. Custodian account of a minor (Uniform Gift to Minors Act).	The minor.	The minor.
5. The usual revocable savings trust account (grantor is also trustee).	The grantor-trustee.	The grantor-trustee.
6. A so-called trust account that is not a legal or valid trust under state law.	The actual owner.	The actual owner.
7. A sole proprietorship.	The owner.	The owner.

CHART 2. Guidelines for Employer Identification Numbers

For this account type—	In the Taxpayer Identification Number field of the Payee "B" Record, enter the EIN of—	In the First Payee Name Line of the Payee "B" Record, enter the name of—
1. A valid trust, estate, or pension trust.	Legal entity.[1]	The legal trust, estate, or pension trust.
2. A corporate account.	The corporation.	The corporation.
3. An association, club, religious, charitable, educational or other tax-exempt organization.	The organization.	The organization.
4. A partnership account held in the name of the business.	The partnership.	The partnership.
5. A broker or registered nominee/middleman.	The broker or nominee/middleman.	The broker or nominee/middleman.

CHART 2. Guidelines for Employer Identification Numbers—Continued

For this account type—	In the Taxpayer Identification Number field of the Payee "B" Record, enter the EIN of—	In the First Payee Name Line of the Payee "B" Record, enter the name of—
6. Account with the Department of Agriculture in the name of a public entity, such as state or local government, school district or prison, that receives agriculture program payments.	The public entity.	The public entity.

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[1] Do not furnish the identification number of the personal representative or trustee unless the name of the representative or trustee is used in the account title.

SEC. 12. EFFECT ON PAPER RETURNS

.01 Diskette reporting of the information returns listed in Part A, Sec. 1 applies only to the original (Copy A).

.02 For payments of dividends or interest (reported on Forms 1099–DIV, 1099–PATR, 1099–INT or 1099–OID), the payer is required to furnish an official Form 1099 to a payee either in a separate mailing by First-Class mail or in person. These forms may not be combined or mailed with other information furnished to the recipient except Forms W–8, W–9, or other Forms 1099. The payer may use substitute Forms 1099 if they utilize the proper language, are substantially similar to the official forms and if the payer complies with all revenue procedures relating to substitute Forms 1099 in effect at the time (see Publication 1179). Copy B (For Recipient) of the substitute forms must contain the statement "This is important tax information and is being furnished to IRS. If you are required to file a return, a negligence penalty or other sanction will be imposed on you if this income is taxable and IRS determines that it has not been reported." The substitute form must contain instructions substantially similar to those on the back of Copy B of the official form.

.03 Statements to recipients for Forms 1098, 1099–A, 1099–B, 1099–G, 1099–MISC (except for substitute payments in lieu of dividends and tax-exempt interest), 1099–R, 5498, or W–2G need not be a copy of the paper form filed with IRS. It is important that income items be properly classified for Federal tax purposes on the statement the payer gives to recipients. The message "This information is being furnished to IRS" must appear on the statements. In addition, Form 1098 statements must contain the message "The amount shown is deductible by you for Federal income tax purposes only to the extent it was actually paid by you and not reimbursed by another person. The space provisions on official paper forms do not agree with those used in magnetic media. The amount of space on paper forms is less than that allowed on magnetic media. Filers may wish to seek a substitute form for Copy B (For Recipient) that accommodates the space provisions used in magnetic media. Payers are permitted considerable flexibility in designing Copy B of the information return to be furnished to the payee. The payer may combine the information return data with other reports or financial or commercial notices as long as all required information is present and worded properly and the payee's copy is conducive to proper reporting of income on tax returns. (This does not apply to Forms 1099–INT, 1099–OID, 1099–DIV, and 1099–PATR. See .02 above for the requirements for these four forms.) However, when information not requested on the official form is included on these substitute statements, they can no longer be mailed with recipient copies of 1099–DIV, INT, OID, or PATR without violating the separate mailing requirements.

.04 If a portion of the returns is reported on diskette and the remainder is reported on paper forms, those returns not submitted on diskette (including corrected returns) may require a waiver depending on the type of return and volume. Returns filed on paper must be filed on official forms or on acceptable paper substitutes meeting the specifications in Publication 1179.

Do not submit proposed substitutes of Copy A to the National Computer Center.

Your proposed substitutes must comply to the official form and the specifications outlined in Publication 1179. Request a copy of Publication 1179 from an IRS office for information concerning paper substitutes. Do not submit any substitutes for approval. Only those forms that comply with the official form and the specifications in Publication 1179 are acceptable.

SEC. 13. TO CONTACT THE IRS NATIONAL COMPUTER CENTER

.01 Effective January 1, 1986, magnetic media processing for *all* service centers was centralized at the IRS National Computer Center. *Please direct all requests for magnetic media related publications, information, undue hardship waivers, extensions, or forms to the following addresses* (if Postal Service or land carrier):

Magnetic Media Reporting
Internal Revenue Service
National Computer Center
Post Office Box 1359
Martinsburg, WV 25401-1359

or

Magnetic Media Reporting
Internal Revenue Service
National Computer Center
Route 9 & Needy Road
Martinsburg, WV 25401

Hours of operation at this address will be 8:30 A.M. until 8:00 P.M. Eastern Time Zone. The telephone number is (304) 263-8700.

Requests for paper returns, publications or forms not related to magnetic media processing should be requested from local IRS offices or by calling the toll-free number in your area.

.02 The National Computer Center will process returns filed on magnetic media only. *All information returns, including corrections, filed on paper forms should be submitted to the appropriate service center, not the National Computer Center.* Organizations who file their information returns on magnetic media but who submit their corrected returns on *paper forms*, refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" for the service center addresses.

SEC. 14. COMBINED FEDERAL/STATE FILING

.01 The Combined Federal/State Program was established to simplify information returns filing for the taxpayer. IRS will accept, upon prior approval, diskette files containing state reporting information only for those states listed in Table 1 in this section. *FORMS 1098, 1099–A, 1099–B, AND W-2G CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.*

.02 To request approval to participate in the Combined Federal/State Program, a "*test*" file, *coded for this program,* must be submitted by the transmitter to the IRS National Computer Center between August 15 and December 15 using the revenue procedure that will be used for the actual data files. Blanket approval will not be given to software packages. The "*test*" file is only required for the first year. Once you are approved, you do not need to resubmit "*tests*" each year, except when notified by IRS. Refer to Part A, Sec. 13 for the address. See Part A, Sec. 5.04 for general guidelines on submission of "*test*" files. Each record, both in the "*test*" file and actual data file, must conform *exactly* to the revenue procedure for the tax year of the *actual* data. Combined Federal/State records must be coded using each state's dollar criteria from Table 2 of this section for each *type* of return.

If the "*test*" diskette is determined to be acceptable, IRS will return it to the filer with Form 6847, Consent for Internal Revenue Service to Release Tax Information. The payer *must* complete Form 6847. The five character alpha/numeric Transmitter Control Code must be included on the form. The form should then be returned to IRS before IRS will release tax information to any of the participating states.

Form 6847 must be signed by one of the individuals listed at the bottom of the form. If the form is signed by an attorney-in-fact, the written consent from the taxpayer to the attorney-in-fact must be included with the Form 6847. This consent by language and/or scope must clearly indicate that the attorney-in-fact is empowered to authorize release of the information document returns to the state(s). A separate Form 6847 is required for each payer. A transmitter may not combine payers on one Form 6847 even though acting as attorney-in-fact for several payers. Form 6847 may be photocopied if you receive an insufficient number of the form. If you have filed on this program in the past and have not met these requirements, you must resubmit the Form 6847 with the proper signatures as specified. If you file for multiple payers, only code the records to go to the state(s) for those payers that participate and have properly submitted Form 6847. Do not submit *actual* data records coded for the Combined Federal/State Program without prior approval from IRS.

.03 States that participate in this program and the valid state code assigned to each are listed in Table 1 of this section. If the state that you wish information released to does *not* participate in the program, do *not* code your records for that state. If the state participates, if you have received prior approval, and if all other conditions are met, IRS will forward the tax information to the participating state at no charge to the filer.

.04 *IF CORRECTIONS MUST BE MADE, IRS WILL NOT TRANSMIT CORRECTED RETURNS TO THE STATES. THIS WILL BE THE RESPONSIBILITY OF THE FILER.*

.05 IRS will make no attempt to process files with any deviations. Approval to participate in the Combined Federal/State Program will be revoked if any files are submitted that do not *totally* conform.

.06 IRS is acting as a forwarding agent *ONLY*. Some participating states require separate notification that you are filing in this manner. It is your responsibility to contact the appropriate state(s) for further information.

.07 The appropriate state code should be entered for those documents which meet the state's filing requirements. *It is the filer's responsibility* to determine the state code to be used and to obtain the filing requirements from the appropriate state(s).

.08 If you meet all of the requirements for this program, you *must* provide the state totals from the "K" Record on a separate Form 4804, Transmittal of Information Returns on Magnetic Media (or Form 4802, Transmittal For Multiple Magnetic Media Reporting) or computer generated substitute for each state, *or* you must include a listing which identifies each state and the "K" Record totals for each.

.09 If you have met *ALL* of the above conditions:

(a) You must submit all records using 128 or 256 position sectors which indicate the appropriate coding related to this program.

(b) The "C" Record *must* be followed by a "K" Record for each state. The "K" Record indicates the number of payees being reported to each particular state.

(c) Payment amount totals and the valid participating state code must be included in the state totals "K" Record. Refer to Part B, Sec. 16 (or Part C, Sec. 14) for a description of the "K" Record.

(d) The "K" Record is followed by an end of transmission "F" Record (if this is the last record of the entire file).

.10 Only those states listed in Table 1 below will receive information from IRS. *It is the filer's responsibility to file information returns with states that do not participate in this program.*

TABLE 1. PARTICIPATING STATES AND THEIR CODES

State	*Code*	*State*	*Code*	*State*	*Code*
Alabama	01	Iowa	19	New York	36
Arizona	04	Kansas	20	North Carolina	37
Arkansas	05	Maine	23	North Dakota	38
California	06	Massachusetts	25	Oregon	41
Delaware	10	Minnesota	27	South Carolina	45
District of Columbia	11	Mississippi	28	Tennessee	47
Georgia	13	Missouri	29	Wisconsin	55
Hawaii	15	Montana	30		
Idaho	16	New Jersey	34		
Indiana	18	New Mexico	35		

.11 To simplify filing, several of the participating states have provided lists of their information return reporting requirements (see Table 2). This cumulative list is for information purposes only and represents dollar criteria. For complete information on state filing requirements, contact the appropriate state tax agencies.

TABLE 2. DOLLAR CRITERIA

STATE	1099-R	1099-DIV	1099-INT	1099-MISC	1099-PATR	1099-G	1099-OID	5498
Alabama	1500	1500	1500	1500	1500	NR	1500	NR
Arizona[a]	300	300	300	300	300	300	300	NR
Arkansas	2500	100	100	2500	2500	2500	2500	g
District of Columbia[b]	600	600	600	600	600	600	600	NR
Hawaii	600	10	10[c]	600	10	all	10	g
Idaho	600	10	10	600	10	10	10	g
Iowa	1000	100	1000	1000	1000	1000	1000	NR
Minnesota	600	10	10	600	10	10	10	g
Missouri	NR	NR	NR	1200[d]	NR	NR	NR	NR
Montana	600	10	10	600	10	10	10	g
New Jersey	1000	1000	1000	1000	1000	1000	1000	NR
New York	600	NR	600	600[e]	NR	600	NR	NR
North Carolina	100	100	100	600	100	100	100	g
Oregon	600[f]	10	10	600	10	10	10	NR
Tennessee	NR	25	25	NR	NR	NR	NR	NR
Wisconsin	500	100	100	100	100	NR	NR	NR

NR—No filing requirement.

Footnotes:

a. These requirements apply to individuals and business entities.

b. Amounts are for aggregates of several types of income from the same payroll.

c. State regualtion changing filing requirement from $600 to $10 is pending.

d. The state would prefer those returns filed with respect to non-Missouri residents to be sent directly to the state agency.

e. Aggregate of several types of income.

f. Return required for state of Oregon residents only.

g. Same as Federal requirement for this type of return.

*NOTE: Filing requirements for any state in Table 1 not shown on the above chart are the same as the Federal requirement.

SEC. 15. DEFINITIONS OF TERMS

Element	Description
b	Denotes a blank position. Enter blank(s) when this symbol is used (do *not* enter the letter "b"). This appears in numerous areas throughout the record descriptions.
Coding Range	Indicates the allowable codes for a particular type of statement.
EIN	Employer Identification Number that has been assigned by IRS.
Excess Golden Parachute Payment	Parachute payments (also called "golden parachutes") are certain payments in the nature of compensation that corporations make to key individuals, often in excess of their usual compensation, in the event that ownership or control of the corporation changes.
File	For purposes of this procedure, a file consists of all diskette records submitted by a Payer or Transmitter.
Payee	Person(s) or organization(s) receiving payments from the Payer, or for whom an information return must be filed.
Payer	Includes the person making payments, a recipient of mortgage interest payments, a broker, a barter exchange, a trustee or issuer of an IRA, SEP or DEC, or a lender who acquires an interest in secured property or who has reason to know that the property has been abandoned. The Payer will be held responsible for the completeness, accuracy and timely submission of diskette files.
Special Character	Any character that is not in numeral, a letter or a blank.
SSA	Social Security Administration.
SSN	Social Security Number.

Element	Description
Taxpayer Identification Number (TIN)	May be either an EIN or SSN.
Transfer Agent (Paying Agent)	The transfer agent or paying agent is the entity who has been contracted or authorized by the payer to perform the services of paying and reporting backup withholding (Form 941). The payer must submit to IRS a Form 2678, Employer Appointment of Agent under section 3504, which notifies IRS of the transfer agent relationship.
Transmitter	Person or organization preparing diskette file(s). May be Payer or agent of Payer.
Transmitter Control Code (TCC)	A *five* character alpha/numeric number assigned by IRS to the transmitter prior to actual filing on magnetic media. This number is inserted in the "A" Record of your files and *must* be present before the file can be processed. An application Form 4419 must be filed with IRS to receive this number. See Part A, Sec. 5. (Abbreviation for this term is TCC.)

SEC. 16. U.S. POSTAL SERVICE STATE AND COUNTRY ABBREVIATIONS

.01 You *MUST* use the following U.S. Postal Service state abbreviations and foreign country codes when developing the state code portion of address fields. (This table provides state abbreviations only and does not represent those states participating in the Combined Federal/State Program. For a list of states that participate in the Combined Federal/State Program, refer to Part A, Sec. 14.10.)

State	Code	State	Code	State	Code
Alabama	AL	Kentucky	KY	North Dakota	ND
Alaska	AK	Louisiana	LA	Ohio	OH
Arizona	AZ	Maine	ME	Oklahoma	OK
Arkansas	AR	Maryland	MD	Oregon	OR
California	CA	Massachusetts	MA	Pennsylvania	PA
Colorado	CO	Michigan	MI	Rhode Island	RI
Connecticut	CT	Minnesota	MN	South Carolina	SC
Delaware	DE	Mississippi	MS	South Dakota	SD
District of Columbia	DC	Missouri	MO	Tennessee	TN
Florida	FL	Montana	MT	Texas	TX
Georgia	GA	Nebraska	NE	Utah	UT
Hawaii	HI	Nevada	NV	Vermont	VT
Idaho	ID	New Hampshire	NH	Virginia	VA
Illinois	IL	New Jersey	NJ	Washington	WA
Indiana	IN	New Mexico	NM	West Virginia	WV
Iowa	IA	New York	NY	Wisconsin	WI
Kansas	KS	North Carolina	NC	Wyoming	WY

.02 The following list represents Canadian Provinces and the corresponding code to be associated with each.

Province	Code	Province	Code	Province	Code
Alberta	AB	British Columbia	BC	New Brunswick	NB
Manitoba	MB	Nova Scotia	NS	Northwest Territories	NT
Newfoundland	NF	Prince Edward Island	PE	Saskatchewan	SK
Ontario	ON	Labrador	LB		
Quebec	PQ				
Yukon Territories	YK				

.03 The following list represents foreign countries and the corresponding code to be associated with each.

Foreign Country	Code
Afghanistan	AF
Albania	AL
Algeria	AG
American Samoa	AQ
Andorra	AN
Angola	AO
Antarctica	AY
Antigua & Barbuda	AC
Argentina	AR
Australia	AS
Austria	AU
Azores	PO
Bahamas, The	BF
Bahrain	BA
Bangladesh	BG
Barbados	BB
Belgium	BE
Belize (Formerly British Honduras)	BH
Benin (Formerly Dahomey)	DM
Bermuda	BD
Bhutan	BT
Bolivia	BL
Botswana	BC
Brazil	BR
British Indian Ocean Territory	IO
British Virgin Islands	VI
Brunei	BX
Bulgaria	BU
Burma	BM
Burundi	BY
Cambodia	CB
Cameroon	CM
Canada	CA
Canton & Enderbury Islands	EQ
Canary Islands	SP
Cape Verde, Republic of	CV
Cayman Isands	CJ
Central Africa Republic	CT
Chad	CD
Channel Islands	OC
Chile	CI
China (Peking)	CH
China (Taiwan)	TW
Christmas Island	KT
Cocos (Kneeling) Islands	CK
Columbia	CO
Comoros	CN
Congo	CF
Cook Islands	CW
Costa Rica	CS
Cuba	CU
Cyprus	CY
Czechoslovakia	CZ
Denmark	DA
Djibouti (Formerly Afars & Issas)	DJ
Dominica	DO
Dominican Republic	DR
Ecuador	EC
Egypt	EG
El Salvador	ES
England	UK
Equatorial Guinea	EK
Ethiopia	ET
Falkland Islands (Also called Islas Malvinas)	FA
Faroe Islands	FO
Fiji	FJ
Finland	FI
France	FR
French Guiana	FG
French Polynesia	FP
French Southern & Antarctic Lands	FS
Gabon	GB
Gambia, The	GA
German Democratic Republic (East Germany)	GC
Germany, Federal Republic of (West Germany)	GE
Ghana	GH
Gibraltar	GI
Gilbert Islands	GS
Greece	GR
Greenland	GL
Grenada	GJ
Guadeloupe	GP
Guam	GQ
Guatemala	GT
Guinea	GV
Ginea-Bissau	PU
Guyana	GY
Haiti	HA
Heard Island & McDonald Island	HM
Honduras	HO
Hong Kong	HK
Hungary	HU
Iceland	IC
India	IN
Indonesia	ID
Iran (Also called Persia)	IR
Iraq	IZ
Ireland	EI
Isle of Man	OC
Israel	IS
Italy	IT
Ivory Coast	IV
Jamaica	JM
Japan	JA
Johnston Atoll	JQ
Jordan	JO
Kenya	KE
Korea, Democratic Peoples Republic of (North Korea)	KN
Korea, Republic of (South Korea)	KS
Kuwait	KU
Laos	LA
Lebanon	LE
Lesotho	LT
Liberia	LI
Libya	LY
Liechtenstein	LS
Luxemburg	LU
Macao	MC
Madagascar	MA
Malawi	MI
Malaysia	MY
Maldives	MV
Mali	ML
Malta	MT
Martinique	MB
Mauritania	MR
Mauritius	MP
Mexico	MX
Midway Islands	MQ
Monaco	MN
Mongolia	MG
Montserrat	MH
Morocco	MO
Mozambique	MZ
Nauru	NR
Navassa Island	BQ
Nepal	NP
Netherlands (Also called Holland)	NL
Netherlands Antilles	NA
New Caledonia	NC
Vanuata (Also called New Hebrides)	NH
New Zealand	NZ
Nicaragua	NU
Niger	NG
Nigeria	NI
Niue	NE
Norfolk Island	NF
Northern Ireland	UK
Norway	NO
Oman	MU

Foreign Country	Code
Pakistan	PK
Panama	PN
Papua-New Guinea	PP
Paracel Islands	PF
Paraguay	PA
Peru	PE
Philippines	RP
Pitcairn	PC
Poland	PL
Portugal	PO
Portuguese Timor	PT
Puerto Rico	RQ
Qatar	QA
Reunion	RE
Romania	RO
Rwanda	RW
St. Christopher-Nevis-Anguilla (Also called St. Kitts)	SC
St. Helena	SH
St. Lucia	ST
St. Pierre & Miquelon	SB
St. Vincent	VC
San Marino	SM
Sao Tome and Principe	TP
Saudi Arabia	SA
Scotland	UK
Senegal	SG
Seychelles	SE
Sierra Leone	SL
Singapore	SN
Solomon Islands	BP
Somalia	SO
South Africa	SF
Southern Rhodesia	RH
South-West Africa (Also called Namibia)	WA
Spain	SP
Spratly Islands	PG
Sri Lanka (Also called Ceylon)	CE
Sudan	SU
Surinam	NS
Svalbard & Jan Mayen	JS
Swaziland	WZ
Sweden	SW
Switzerland	SZ
Syria	SY
Tanzania	TZ
Thailand	TH
Togo	TO
Tokelau Islands	TL
Tonga	TN
Trinidad & Tobago	TD
Trust Territory of the Pacific Islands	TQ
Tunisia	TS
Turkey	TU
Turks & Caicos Islands	TK
Tuvalu (Also called Ellice Islands)	TV
Uganda	UG
Union of Soviet Socialist Republics	UR
United Arab Emirates	TC
United Kingdom	UK
United States	US
Upper Volta	UV
Uruguay	UY
Vatican City	VT
Venezuela	VE
Vietnam	VM
Virgin Islands of the U.S.	VQ
Wake Island	WQ
Wales	UK
Wallis & Futuna	WF
Western Sahara	WI
Western Samoa	WS
Yemen (South)	YS
Yemen (North)	YE
Yugoslavia	YO
Zaire	CG
Zambia	ZA
Zimbabwe	RH

PART B. SINGLE DENSITY DISKETTE SPECIFICATIONS

SECTION 1. GENERAL

.01 The specifications contained in this part of the revenue procedure define the required format and contents of the records to be included in a single density diskette file. These specifications must be adhered to unless deviations have been specifically granted by IRS.

.02 To be compatible, a single density diskette file must meet the following specifications in total:

(a) 8 inches in diameter.

(b) recorded in EBCDIC.

(c) contain 77 tracks of which:

(1) Track 0 is the index track (the operating system reserves track 0 for the directory information and writes the file name and location in the directory; *data* cannot be written in track 0).

(2) Tracks 1 through 73 are data tracks.

(3) Track 74 is unused.

(4) Tracks 75 and 76 are alternate data tracks.

(d) each Track must contain 26 sectors.

(e) each Sector must contain 128 bytes.

(f) data must be recorded on only one side of the diskette.

(g) IRS can process single sided, single density, soft sectored diskettes as well as double sided, double density, soft sectored diskettes. Part C provides specifications for double density diskettes which have sectors of 256 bytes.

(h) an IBM 5360 compatible diskette would meet the above specifications. Hard sectored diskettes are not compatible.

.03 Payers who can substantially conform to these specifications, but who require some minor deviations, MUST contact the National Computer Center. Under no circumstances may diskettes deviating from the specifications in this revenue procedure be submitted without prior approval from IRS. If you file under the Combined Federal/State Program, your files must conform totally to this revenue procedure.

.04 An external affixed label, Form 5064, must appear on each diskette submitted for processing. The following information is needed:

(a) The transmitter's name.

(b) The five character alpha/numeric Transmitter Control Code.

(c) State of sender (*e.g.*, NY).

(d) Density (used by magnetic tape filers only).

(e) Check box (used by magnetic tape filers only).

(f) Track (used by magnetic tape filers only).

(g) Recording code (*e.g.*, EBCDIC or ASCII). Diskette filers enter EBCDIC.

(h) The tax year of the data (*e.g.*, 1986).

(i) Document types (*e.g.*, 1099–INT).

(j) The total number of "B" Records after each "A" Record (this figure is taken from the "C" Records).

(k) A number assigned by the transmitter to the diskette.

(l) The sequence of each diskette (*e.g.*, 001 of 008).

The external media label, From 5064, was updated for tax year 1986. You must use the updated label. This information will assist IRS in processing the file or in locating a file, should the transmitter request that it be returned due to errors. *IRS advises that special shipping containers not be used for transmitting data since it cannot be guaranteed that they will be returned.*

SEC. 2. DISKETTE HEADER LABEL

The header label on the diskette must be formatted as shown in the following layout: (If your system automatically creates a header label, this is not necessary).

HDR1	Blank	Data Set Name (For Transmitter's Use)	Blank	Sector Length	Blank	Beginning of Extent (BOE)
(a)	(b)	(c)	(b)	(d)	(b)	(e)
1–4	5	6–13	14–22	23–27	28	29–33

Blank	End of Extent (EOE)	Blank	Bypass Data Set	Data Set Accessibility	Write Protect	Blank
(b)	(f)	(b)	(g)	(h)	(i)	(b)
34	35–39	40	41	42	43	44

Multi-Volume	Blank	Expiration Date YYMMDD	Verify Mark	Blank	End of Data (EOD)
(j)	(b)	(k)	(l)	(b)	(m)
45	46–66	67–72	73	74	75–79

(a) Header 1—Positions 1 through 4; enter HDR1.

(b) Unused—Any field marked blank is unused and should contain only blanks.

(c) Data Set Name—Positions 6 through 13; you can use this field to identify your data set.

(d) Sector Length—Positions 23 through 27; enter the sector length 128, right-justify and fill positions 23 and 24 with zeros.

(e) Beginning of Extent (BOE)—Positions 29 through 33; enter the five-digit address designated for the first record of this data set. For example, if the first record is to go in track 01, sector 02, enter 01002, or xx0yy where xx is the track number and yy is the sector number.

(f) End of Extent (EOE)—Positions 35 through 39; enter the five-digit address of the last position of the disk reserved for this data set. For example, to reserve the entire disk for a data set, enter 73026.

(g) Bypass Data Set—Position 41; enter B if you want to bypass this data set; otherwise, enter a blank.

(h) Data Set Accessibility—Positions 42; enter a blank. Any other character in this field causes the equipment to refuse the disk.

(i) Write Protect—Position 43; this field defines the protected status of the associated data set. P = read only; blank = read/write. With P in this position, you can only select the Update (U) mode.

(j) Multi-Volume—Position 45; this field indicates whether a complete data set is on a disk. Blank = data set complete; C = data set continued on another disk; L = last disk of a multi-disk data set.

(k) Expiration Date—Positions 67 through 72; *may* be used to contain the date that the data set expires. The format is YYMMDD where YY is the year, MM is the month and DD is the day.

(l) Verify Mark—Position 73; this single character field shows if the data set is verified. If it is, enter V, if it is not verified, enter a blank.

(m) End of Data (EOD)—Positions 75–79; enter the track number in positions 75 and 76, enter a "0" (zero) in position 77 and enter the sector number in positions 78 and 79.

SEC. 3. PAYER/TRANSMITTER "A" RECORD

.01 Identifies the payer and transmitter of the diskette and provides parameters for the succeeding Payee "B" Records. IRS computer programs rely on the absolute relationship between the parameters and data fields in the "A" Record and the data fields in the "B" Records to which they apply.

.02 The number of "A" Records appearing on a diskette will depend on the number of payers and the different types of returns being reported. After the header label on the diskette, the first record appearing in the file must be an "A" Record. For diskette filing, the *actual* record lengths for the "A" and "B" Records must agree with whatever is entered in diskette positions 29–31 and 32–34 of the "A" Record.

A transmitter may include Payee "B" Records for more than one payer on a diskette; however, each GROUP of Payee "B" Records must be preceded by an "A" Record. A single diskette may also contain different types of returns, but the returns *MUST* not be intermingled. A separate "A" Record is required for each payer and each type of return being reported. An "A" Record may be blocked with "B" Records; however, the initial record on a *file* must be an "A" Record. The IRS will accept an "A" Record after a "C" Record.

.03 All alpha characters entered in the "A" Record should be upper-case.

.04 ***WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.***

RECORD NAME: PAYER/TRANSMITTER "A" RECORD

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". It is used to sequence the sectors making up a Service Record.
2	Record Type	1	REQUIRED. Enter "A".
3	Payment Year	1	REQUIRED. Must be the right most digit of the year for which information is being reported (*e.g.*, if payments were made in 1986, enter "6"). Must be incremented each year.
4–6	Diskette Sequence Number	3	REQUIRED. Sequence number assigned by the Transmitter to each diskette starting with 001. (Blanks are acceptable or all zeros.)
7–15	Payer's Federal EIN	9	REQUIRED. Must be the *valid* 9-digit number assigned to the payer by IRS. DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS. (Also see Part A, Sec. 11.07.)
16	Blank	1	REQUIRED. Enter blank.
17	Combined Federal/State Filer	1	REQUIRED. Enter the appropriate code from the table below. *Prior approval* is required. A Consent Form 6847 *must* be submitted to IRS before tax information will be released to the states. Refer to Part A, Sec. 14.11 for money criteria. Not all states participate in this program. If the Payer/Transmitter is not participating in the Combined Federal/State Filing Program, enter blanks. (Refer to Part A, Sec. 14 for the requirements that *must* be met *prior* to actual participation in this program.) Forms 1098, 1099–A, 1099–B, and W–2G cannot be filed on this program. Filers who participate in this program must incorporate state totals into corresponding "K" Records as described in Part B, Sec. 16.

Code	*Meaning*
1	Participating in the Combined Federal/State Filing Program
blank	Not participating

Diskette Position	Field Title	Length	Description and Remarks
18	Type of Return	1	REQUIRED. Enter appropriate code from table below:

Type of Return	*Code*
1098	3
1099–A	4
1099–B	B
1099–DIV	1
1099–G	F
1099–INT	6
1099–MISC	A
1099–OID	D
1099–PATR	7
1099–R	9
5498	L
W–2G	W

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
19–27	Amount Indicators	9	REQUIRED. *In most cases, the boxes or Amount Indicators on paper information returns correspond with the Amount Codes used to file on magnetic media; however, should you notice discrepancies, between this revenue procedure and paper forms, please disregard them and program according to this revenue procedure for your returns filed on magnetic media.* For specific instructions on information to be reported in each Amount Code, refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G." The amount indicators entered for a given type of return indicate type(s) of payment(s) which were made. For each Amount Code entered in this field, a corresponding payment amount must appear in the Payee "B" Record. Example: If position 18 of the Payer/Transmitter "A" Record is "6" (for 1099–INT) and positions 19–27 are "123bbbbbb", this indicates that 3 payment amount fields are present in all of the following Payee "B" Records. The first payment amount field in the Payee "B" Record will represent Earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposit, etc., the second will represent Amount of forfeiture, and the third will represent Federal income tax withheld. Enter the Amount Indicators in ASCENDING SEQUENCE, (*i.e.*, 1247bbbbb), left-justify, filling unused positions with blanks. For any further clarification of the Amount Indicator codes, you may contact the IRS National Computer Center.
	Amount Indicators Form 1098–Mortgage Interest Statement		For Reporting Mortgage Interest Received from Payer(s) on Form 1098:

Amount Code	Amount Type
1	Mortgage interest received from payer(s)
2	Optional field for items such as real estate taxes or insurance paid from escrow

NOTE: THE PERSON FOR WHOM YOU ARE RECEIVING THE INTEREST NEED NOT FILE FORM 1098, AND NO ADDITIONAL REPORTING IS REQUIRED FOR THE TRANSFER OF THE INTEREST FROM THE SERVICING BANK TO THE LENDER.

Diskette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–A—Acquisition or Abandonment of Secured Property		For Reporting the Acquisition or Abandonment of Secured Property on Form 1099–A:

Amount Code	Amount Type
2	Amount of debt outstanding
3	Amount of debt satisified
4	Fair market value of property at acquisition or abandonment

Diskette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–B—Proceeds From Broker and Barter Exchange Transactions		For Reporting Payments on Form 1099–B:

Amount Code	Amount Type
2	Stocks, bonds, etc. (For Forward Contracts see NOTE below.)
3	Bartering
4	Federal income tax withheld
6	Profit or loss realized in 1986

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks

SECTOR 1 (Continued)

7	Unrealized profit (or loss) on open contracts-12/31/85
8	Unrealized profit (or loss) on open contracts-12/31/86
9	Aggregate profit (or loss)

NOTE: The Payment Amount field associated with Amount Code 2 may be used to represent a loss when the reporting is for Forward Contracts. Refer to Payee "B" Record-General Field Descriptions, Payment Amount Fields, for instructions in reporting negative amounts.

Amount Indicators Form 1099–DIV—Dividends and Distributions

For Reporting Payments on Form 1099–DIV:

Amount Code	Amount Type
1	Gross dividends and other distributions on stock
2	Dividends qualifying for exclusion
3	Dividends not qualifying for exclusion
4	Federal income tax withheld
5	Capital gain distributions
6	Nontaxable distributions (if determinable)
7	Foreign tax paid
8	Cash liquidation distributions
9	Noncash liquidation distributions (Show fair market value)

Amount Indicators Form 1099–G—Certain Government Payments

For Reporting Payments on Form 1099–G:

Amount Code	Amount Type
1	Unemployment compensation
2	State or local income tax refunds
4	Federal income tax withheld
5	Discharge of indebtedness
6	Taxable grants
7	Agriculture payments

Amount Indicators Form 1099–INT—Interest Income

For Reporting Payments on Form 1099–INT:

Amount Code	Amount Type
1	Earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposit, etc.
2	Amount of forfeiture
3	Federal income tax withheld
4	Foreign tax paid (if eligible for foreign tax credit)
5	U.S. Savings Bonds, etc.

Amount Indicators Form 1099–MISC—Miscellaneous Income (See Notes 1, 2 and 3)

For Reporting Payments on Form 1099–MISC:

Amount Code	Amount Type
1	Rents
2	Royalties
3	Prizes and awards
4	Federal income tax withheld

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			

5	Fishing boat proceeds
6	Medical and health care payments
7	Nonemployee compensation
8	Direct sales "*indicator*" (see NOTE 1)
9	Substitute payments in lieu of dividends or interest (see NOTE 2)

NOTE 1: Use Amount Code "8" to report that *direct sales* of consumer products of $5,000 or more to the payee on a buy-sell, deposit-commission, or other basis *for resale* were made. Do not use this indicator for sales of less than $5,000. The use of Amount Code "8" actually reflects an *indicator of direct sales* and not an actual payment amount or amount code. The corresponding payment amount field in the Payee "B" Record MUST be reflected as 0000000100. This does not mean that a payment of $1.00 was made or is being reported. The use of Amount Code "8" relates directly to Sector 1, diskette position "5", Document Specific Code and NOTE 2 of the Payment Amount Field in the Payee "B" Record. (If you use Amount Code "8" in the "A" Record, you will enter a "1" in diskette position "5" of Sector 1 of the "B" Record. For any other 1099–MISC Amount Codes, you will enter a "0" (zero) in diskette position "5" of Sector 1 of the "B" Record.)

NOTE 2: Brokers are subject to a reporting requirement for payments received after 1984. Brokers who transfer securities of a customer for use in short sale must use Amount Code 9 to report the aggregate payments received in lieu of dividends or tax-exempt interest on behalf of a customer while the short sale was open. Generally, for substitute payments in lieu of dividends, a broker is required to file a Form 1099–MISC for each affected customer who is *not* an individual. Refer to the 1986 "Instructions for Form 1099, 1098, 5498, 1096, and W–2G" for detailed information. The instructions are available from IRS offices.

NOTE 3: If you are reporting Excess Golden Parachute Payments, use paper forms 1099–MISC. Do not report these payments on magnetic media. See Part A, Sec. 15 for a definition of an Excess Golden Parachute Payment.

Amount Indicators
Form 1099–OID—
Original Issue
Discount

For Reporting Payments on Form 1099–OID:

Amount Code	Amount Type
1	Total original issue discount for 1986
2	Other periodic interest (the regular interest paid on this obligation without regard to any original issue discount)
3	Amount of forfeiture
4	Federal income tax withheld

Amount Indicators
Form 1099–PATR—
Taxable Distributions
Received From
Cooperatives

For Reporting Payments on Form 1099–PATR:

Amount Code	Amount Type
1	Patronage dividends
2	Nonpatronage distributions
3	Per-unit retain allocations
4	Federal income tax withheld
5	Redemption of nonqualified notices and retain allocations
6	Investment credit (See NOTE)
7	Energy investment credit (See NOTE)
8	Jobs credit (See NOTE)

NOTE: The amount shown for Amount Indicators "6," "7" and "8" must be reported to the payee; however, since these amounts are not taxable, they need not be reported to IRS.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
	Amount Indicators Form 1099-R—Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, etc., (See NOTE)		For Reporting Payments on Form 1099-R:

Amount Code	Amount Type
1	Amount includable as income (add amounts in codes 2 and 3)
2	Capital gain (for lump-sum distributions only)
3	Ordinary income
4	Federal income tax withheld
5	Employee contributions (profit-sharing or retirement plans) or insurance premiums
6	IRA, SEP or DEC distributions
7	State income tax withheld
8	Net unrealized appreciation in employer's securities
9	Other

NOTE: A distribution from a KEOGH plan should be reported in Amount Codes 1, 2, and 3 as appropriate.

Diskette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 5498—Individual Retirement Arrangement Information		For Reporting Payments on Form 5498:

Amount Code	Amount Type
1	Regular SEP contributions made in 1986 and 1987 for 1986. Include only employer contributions here. Enter any employee contributions to a SEP in Code 3.
2	Rollover IRA, SEP or DEC contributions
3	Regular IRA or DEC contributions made in 1986 and 1987 for 1986
4	Life insurance cost included in code 1 or 3 (for endowment contracts only)

NOTE: Form 5498 is filed for contributions to be applied to 1986 that are made between January 1, 1986, and April 15, 1987.

Diskette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form W-2G—Certain Gambling Winnings		For Reporting Payments on Form W-2G:

Amount Code	Amount Type
1	Gross winnings
2	Federal income tax withheld
3	State income tax withheld
7	Winnings from identical wagers

Diskette Position	Field Title	Length	Description and Remarks
28	Blank	1	REQUIRED. Enter blank.
29-31	"A" Record Length	3	REQUIRED. This indicates the Record Length, *NOT* the Sector Length. Enter 360.
32-34	"B" Record Length	3	REQUIRED. This indicates the Record Length, *NOT* the Sector Length. Enter 360.
35	Blank	1	REQUIRED. Enter blank.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
36-40	Transmitter Control Code (TCC)	5	REQUIRED. Enter the five character alpha/numeric Transmitter Control Code assigned by IRS. See Part A, Sec. 15 for a definition of Transmitter Control Code (TCC). You must have a TCC to file *actual* data on this program.
41	Blank	1	REQUIRED. Enter blank.
42-81	First Payer Name	40	REQUIRED. Must be present or files will be returned for correction. Enter the name of the payer in the manner in which it is used in normal business. Any extraneous information must be deleted from the name line. Left-justify and fill with blanks. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
82-120	Second Payer Name	39	REQUIRED. The contents of this field are dependent upon the TRANSFER AGENT INDICATOR in position 121 of this record. If the Transfer Agent Indicator contains a "1", this field will contain the name of the Transfer Agent. If the Transfer Agent Indicator contains a "0" (zero), this field will contain either a continuation of the First Payer Name field or blanks. Left-justify and fill unused positions with blanks. IF NO ENTRIES ARE PERSENT FOR THIS FIELD, FILL WITH BLANKS. (See Part A, Sec. 15 for a definition of Transfer Agent.)
121	Transfer Agent Indicator	1	REQUIRED. Identifies the entity in the Second Payer Name field. (See Part A, Sec. 15 for a definition of Transfer Agent.) *Code* — *Meaning* 1 — The entity in the Second Payer Name field is the Transfer Agent. 0 (zero) — The entity shown is *not* the Transfer Agent (*i.e.*, the Second Payer Name field contains either a continuation of the First Payer Name field or blanks).
122-128	Blank	7	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service Record.
2	Record Type	1	REQUIRED. Enter "A". Must be the second position of each PAYER/TRANSMITTER Record.
3-42	Payer Shipping Address	40	REQUIRED. If the TRANSFER AGENT INDICATOR in position 121 of Sector 1 is a "1", enter the shipping address of the Transfer Agent. Otherwise, enter the shipping address of the payer. Left-justify and fill with blanks.
43-82	Payer City, State and ZIP Code	40	REQUIRED. If the TRANSFER AGENT INDICATOR in position 121 of Sector 1 is a "1", enter the City, State and ZIP Code of the Transfer Agent. Otherwise, enter the City, State and ZIP Code of the payer. Left-justify and fill with blanks.
83-128	Blank	46	REQUIRED. Enter blanks.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
ADDITIONALLY, IF THE PAYER AND THE TRANSMITTER ARE THE SAME, THE "A" RECORD MAY BE TERMINATED WITH SECTOR 2 AS DESCRIBED ABOVE. HOWEVER, IF THE PAYER AND THE TRANSMITTER ARE NOT THE SAME OR THE TRANSMITTER INCLUDES FILES FOR MORE THAN ONE PAYER OR THIS IS A COMBINED FEDERAL/STATE FILING PAYER, THE FOLLOWING ITEMS ARE REQUIRED.			
83-122	First Name Line of Transmitter	40	REQUIRED. Enter the name of the transmitter in the manner in which it is used in normal business. The name of the transmitter *must* be constant through the entire file. Left-justify and fill with blanks.
123-128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3	(Only used if you are transmitting for someone other than yourself or if you participate in the Combined Federal/State Program.)		
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service Record.
2	Record Type	1	REQUIRED. Enter "A". Must be the second position of each PAYER/TRANSMITTER Record.
3-42	Second Name Line of Transmitter	40	REQUIRED. Enter the second name line of the transmitter. Left-justify and fill with blanks. IF NO ENTRIES ARE PRESENT FOR THIS FIELD, FILL WITH BLANKS.
43-82	Transmitter Mailing Address	40	REQUIRED. Enter the mailing address of the transmitter. Left-justify and fill with blanks.
83-122	Transmitter City, State and ZIP Code	40	REQUIRED. Enter the City, State, and ZIP Code of the transmitter. Left-justify and fill with blanks.
123-128	Blank	6	REQUIRED. Enter blanks.

SEC. 4 PAYER/TRANSMITTER "A" RECORD—RECORD LAYOUT

PAYER/TRANSMITTER "A" RECORD—RECORD LAYOUT

Sector 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DISKETTE SEQUENCE NUMBER	PAYER'S FEDERAL EIN	BLANK	COMBINED FEDERAL/STATE FILER	TYPE OF RETURN
1	2	3	4—6	7—15	16	17	18

Sector 1 (Continued)

AMOUNT INDICATORS	BLANK	"A" RECORD LENGTH	"B" RECORD LENGTH	BLANK
19—27	28	29—31	32—34	35

PAYER/TRANSMITTER "A" RECORD—RECORD LAYOUT—Continued

Sector 1 (Continued)

TRANSMITTER CONTROL CODE	BLANK	FIRST PAYER NAME	SECOND PAYER NAME	TRANSFER AGENT INDICATOR	BLANK
36—40	41	42—81	82—120	121	122—128

Sector 2

RECORD SEQUENCE	RECORD TYPE	PAYER SHIPPING ADDRESS	PAYER CITY, STATE AND ZIP CODE	BLANK
1	2	3—42	43—82	83—128

IF THE PAYER AND THE TRANSMITTER ARE THE SAME, THE "A" RECORD MAY BE TERMINATED WITH SECTOR 2 AS ILLUSTRATED ABOVE. HOWEVER, IF THE PAYER AND THE TRANSMITTER ARE NOT THE SAME, OR THE TRANSMITTER INCLUDES FILES FOR MORE THAN ONE PAYER OR THIS IS A COMBINED FEDERAL/STATE PAYER, THE FOLLOWING ITEMS ARE REQUIRED.

Sector 2

RECORD SEQUENCE	RECORD TYPE	PAYER SHIPPING ADDRESS	PAYER CITY, STATE AND ZIP CODE	FIRST NAME LINE OF TRANSMITTER	BLANK
1	2	3—42	43—82	83—122	123—128

Sector 3 (Only used if you are transmitting for someone other than yourself or if you participate in the Combined Federal/State Program.)

RECORD SEQUENCE	RECORD TYPE	SECOND NAME LINE OF TRANSMITTER	TRANSMITTER MAILING ADDRESS	TRANSMITTER CITY, STATE AND ZIP CODE	BLANK
1	2	3–42	43—82	83—122	123—128

SEC. 5. PAYEE "B" RECORDS—GENERAL INFORMATION FOR ALL FORMS

.01 This section contains the general information concerning the Payee "B" Record for all information returns. For a detailed description of the record refer to the following:

(a) Sec. 6. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORMS 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R, and 5498.

(b) Sec. 8. PAYEE "B" RECORD—FIELD DESCRIPTIONS FOR FORMS 1099–A.

(c) Sec. 10. PAYEE "B" RECORD—FIELD DESCRIPTIONS FOR FORM 1099–B.

(d) Sec. 12. PAYEE "B" RECORD—FIELD DESCRIPTIONS FOR FORM W–2G.

.02 The Payee "B" Record contains the payment information from the individual statements. When filing information documents on diskette(s), the format for the Payee "B" Records will vary in relation to the number of payment amount fields being reported. The number of payment amount fields will depend upon the number of Payment Amount Indicator Codes used in positions 19–27 of the Payer/Transmitter "A" Record. For example, if you are reporting 1099–INT, position 18 of the Payer/Transmitter "A" Record will be coded with a "6." If the Amount Indicators used to report this interest are Amount Codes "1," "2," and "3," then diskette positions 19–27 of the "A" Record will be coded "123bbbbbb" (b represents a *blank* position). To correspond with Amount Indicators "1," "2," and "3" of the "A" Record, the "B" Record will contain three payment amount fields. Diskette positions 32–41 of the Payee "B" Record will contain the payment amount to be reported for Amount Code "1" (earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposits, etc.); diskette positions 42–51 of the "B" Record would contain the payment amount to be reported for Amount Code "2" (amount of forfeiture); and diskette positions 52–61 of the "B" Record would contain the payment amount to be reported for Amount Code "3" (Federal income tax withheld). The First Payee Name Line *must* begin immediately after the last payment amount *that is indicated as being used.* In this example, the First Payee Name Line would begin in diskette position 62.

.03 All payee records *must contain correct payee name and address information* entered in the fields prescribed in this section. Records containing an invalid TIN (SSN or EIN) and having no address data present may be returned for correction. In searching for a payee address, if your efforts fail and you know that the address is invalid, supply the invalid address rather than leave the field blank.

.04 IRS must be able to identify the surname associated with the TIN (SSN or EIN) furnished on a statement. The specifications below include a field in the payee records called "Name Control" in which the first four alphabetic characters of the payee's surname or last name are to be entered by the payers. The surname or last name should appear first in the First Payee Name Line of all Payee "B" Records; however, if your records have been developed using the first name first, IRS programs will accept this but a blank must appear between the first and last name.

.05 If payers are unable to provide the first four characters of the surname, the Name Control Field may be left blank; however, compliance with the following will facilitate IRS computer programs in generating the Name Control.

(a) The surname of the payee whose TIN (SSN or EIN) is shown in the Payee "B" Record should always appear first. If, however, you enter the first name first, you must leave a blank space between the first and last name.

(b) In the case of multiple payees, only the surname of the payee whose TIN (SSN or EIN) is shown in the Payee "B" Record must be present in the First Payee Name Line. Surnames of any other payees in the record must be entered in the Second Payee Name Line.

.06 Provision is also made in these specifications for data entries required by state or local governments. This should minimize the Payer/Transmitter's programming burden should payers desire to report on diskette to state or local governments. See Part A, Sec. 14, for the Combined Federal/State filing requirements.

.07 For those filers participating in the Combined Federal/State Filing Program, positions 127 and 128 or 255 and 256 in the Payee "B" Record Sector 2 or 3 *must* contain the appropriate state code for the state to receive the information. The file should also meet the money criteria described in Part A, Sec. 14.11. Do not code for the states unless prior approval to participate has been granted by IRS. See Part A, Sec. 14 for a list of the valid participating state codes. *FORMS 1098, 1099–A, 1099–B, AND W–2G CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.* Your files must meet all of the requirements specified in Part A, Sec. 14 in order to participate in this program.

.08 All alpha characters entered in the "B" Record should be upper-case.

.09 *IRS STRONGLY ENCOURAGES FILERS TO REVIEW THEIR DATA FOR ACCURACY BEFORE SUBMISSION TO PREVENT ERRONEOUS NOTICES BEING MAILED TO PERSONS FOR WHOM REPORTS ARE FILED. FILERS SHOULD BE ESPECIALLY CAREFUL THAT THEIR TAXPAYER NAMES, SOCIAL SECURITY NUMBERS (SSNs), ACCOUNT NUMBERS, TYPES OF INCOME, AND INCOME AMOUNTS ARE CORRECT. ALTHOUGH IRS ENCOURAGES PAYERS TO FILL IN THE PAYER'S ACCOUNT NUMBER FOR THE PAYEE FIELD, THEY SHOULD NOT INCLUDE EXTRANEOUS DIGITS AS THE FIELD IS LIMITED, IN MAGNETIC MEDIA FILING, TO 10 POSITIONS.*

10. *WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*

SEC. 6. PAYEE "B" RECORD—FIELD DESCRIPTIONS FOR FORMS 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R, AND 5498

.01 This section contains the general payment information from individual statements for Forms 1098, 1099–A, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R, and 5498.

.02 In most instances each Payee "B" Record will be composed of two sectors on the diskette with positions 1-41 being a constant format and the variance occurring in positions 42-128 of the first sector and the entire second sector. In those instances where six or more payment amount fields are reported, each Payee "B" Record will be composed of three sectors on the diskette with positions 1-41 of the first sector being a constant format and the variance occurring in positions 42-128 of the first sector and the entire second and third sectors.

RECORD NAME: PAYEE "B" RECORD

Diskette Position	Field Title	Length	Description and Remarks
ECTOR 1			
	Record Sequence	1	REQUIRED. Must be a "1". It is used to sequence the sectors making up a Service PAYEE Record.
	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
-4	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported (*e.g.*, if payments were made in 1986, enter "86"). Must be incremented each year.
-6	Document Specific Code	2	REQUIRED for Forms 1099–R, 1099–MISC, and 1099–G. For *Form 1099–R,* enter the appropriate code for the Category of Total Distribution. For *Form 1099–MISC*, enter the appropriate code for Direct Sales. For *Form 1099–G*, enter the year of income tax refund.

RECORD NAME: PAYEE "B" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
(In prior years, diskette position 6 was used as a corrected return indicator. This position was needed for the Document Specific Code. Diskette position 7 now represents a corrected return. You must adjust your programs.)			**FOR ALL OTHER FORMS, ENTER BLANK. If only one code is used, left-justify and blank fill.**
	Category of Total Distribution (Form 1099–R only)		Use only for reporting on *Form 1099–R* to identify the category of Total Distribution. You may select two codes except when using Code 9. Enter the applicable code from the table below. Code 7 below is *not required* for Amount Indicators 1, 2, and 3. A "0" (zero) is not a valid code for Form 1099–R. If you are reporting a distribution from a KEOGH plan, or from any other distribution, to which the following codes do not apply, enter blanks in this field. *Category* — *Code* Premature distribution (other than codes 2, 3, 4, 5, 8, or P) — 1 Rollover — 2 Disability — 3 Death (includes payments to a beneficiary) — 4 Prohibited transaction — 5 Other — 6 Normal IRA, SEP or DEC distributions — 7 Excess contributions refunded plus earnings on such excess contributions — 8 PS 58 Costs (see NOTE) — 9 Excess contributions refunded plus earnings on such excess contributions taxable in 1985 — P Qualifies for 10-year averaging — A Qualifies for death benefit exclusion — B Qualifies for *both* A and B — C NOTE: PS 58 Costs may be reported on Form 1099–R; however, Form W–2P (filed with SSA) is preferable. Since this is not actually a total distribution, a separate "B" Record is required to report PS 58 Costs. These costs may not be reported in combination with a total distribution. Refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G," available from IRS offices.
	Direct Sales (Form 1099–MISC only)		Use only for direct sales reporting on *Form 1099–MISC*. If sales to the recipient of consumer products on a buy-sell, deposit-commission, or any other basis for resale, have amounted to $5,000 or more, ENTER "1". If you are filing 1099–MISC, with an Amount Indicator of "8" in the "A" Record, you must enter a code "1" in this field. For all other 1099–MISC Amount Codes in the "A" Records, enter a "0" (zero) in this field. In Part B, Sec. 3, information concerning the direct sales indicator can be found under Amount Indicators, Form 1099–MISC, NOTE 1 in the "A" Record. This code will appear in position 5. Position 6 will be blank.
	Refund is for Tax Year (Form 1099–G only)		Use only for reporting the tax year for which the refund was issued. If the payment amount field associated with Amount Indicator 2, Income Tax Refunds, contains a refund, credit or offset that is attributable to an income tax which applies exclusively to income

RECORD NAME: PAYEE "B" RECORD—Continued

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td></td><td></td><td></td><td>from a trade or business and is not of general application, then enter the ALPHA equivalent of the year of refund from the table below. Otherwise, enter the NUMERIC Year for which the Refund was issued. This code should appear in position 5. Position 6 will be blank.
<table>
<tr><th><i>Year for which Refund was Issued</i></th><th><i>Alpha Equivalent</i></th></tr>
<tr><td>1</td><td>A</td></tr>
<tr><td>2</td><td>B</td></tr>
<tr><td>3</td><td>C</td></tr>
<tr><td>4</td><td>D</td></tr>
<tr><td>5</td><td>E</td></tr>
<tr><td>6</td><td>F</td></tr>
<tr><td>7</td><td>G</td></tr>
<tr><td>8</td><td>H</td></tr>
<tr><td>9</td><td>I</td></tr>
<tr><td>0</td><td>J</td></tr>
</table></td></tr>
<tr><td></td><td>Blank or Corrected Return Indicator</td><td>1</td><td>REQUIRED. Enter blank. (Reserved for IRS use.) Diskette position 7 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using magnetic media. IN PRIOR YEARS, DISKETTE POSITION 6 WAS USED AS THE CORRECTED RETURN INDICATOR. THIS HAS NOW CHANGED TO POSITION 7. <i>YOU MUST ADJUST YOUR PROGRAMS.</i></td></tr>
<tr><td>–11</td><td>Name Control</td><td>4</td><td>REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (-) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the name control:
<table>
<tr><th><i>Name</i></th><th><i>Name Control</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE*</td></tr>
<tr><td>James P. En Sr.</td><td>EN*</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must be left-justified and blank filled.</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identification Number (TIN) in positions 13–21 as either an Employer Identification Number, a Social Security Number, or the reason no number is shown. Enter the appropriate code from the following table:
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, enter a blank. If the number is unobtainable due to legitimate cause; <i>e.g.</i>, number applied for but not received, enter a blank.</td></tr>
</table></td></tr>
<tr><td>13–21</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the payee (SSN or EIN, as appropriate). Where an identification number has been applied for but not received or where there is any other legitimate cause for not having an identification number, <i>enter blanks</i>. Refer to Part A, Sec. 11.

<i>DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS</i>. Any record containing an invalid identification number in this field will be returned for correction.</td></tr>
<tr><td>22–31</td><td>Payer's Account Number for Payee</td><td>10</td><td>REQUIRED. Payer may use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payers' file should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. An account number can be any account number assigned by the payer to the payee. (<i>e.g.</i>, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any number that will help identify the particular transaction that you are reporting. If a number is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.</td></tr>
<tr><td></td><td>Payment Amount Fields (must be numeric)</td><td></td><td>The number of payment amounts is dependent upon and must agree with the number of Amount Indicators present in positions 19–27 of Sector 1 of the "A" Record. <i>THE FIRST PAYEE NAME LINE MUST APPEAR IMMEDIATELY AFTER THE LAST PAYMENT AMOUNT INDICATED AS BEING USED</i>. For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one ten position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE 1). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or <i>NEGATIVE PAYMENTS</i> (except those items that reflect</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			a loss on Form 1099-B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "123bbbbbb", the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb", the "B" Records must have only 5 payment amount fields. Payment amounts MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE 1: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee. NOTE 2: If you file 1099-MISC and use Amount Code "8" in the Amount Indicator field of the Payer/Transmitter "A" Record, you must enter 0000000100 in the corresponding Payment Amount Field. This will not represent an actual money amount; this is an indicator of direct sales. (Refer to Part B, Sec. 3, NOTE 1, of the Amount Indicators, Form 1099–MISC, for clarification.)
32–41	Payment Amount 1	10	This amount is identified by the indicator in position 19 of Sector 1 of the Payer/Transmitter "A" Record. *This amount must always be present.*

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF SECTOR 1 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–128 OF SECTOR 1, POSITIONS 1–128 OF SECTOR 2 AND POSITIONS 1–128 OF SECTOR 3, IF NEEDED, OF THE PAYEE "B" RECORD. USE THE APROPRIATE FORMAT AS REQUIRED. SECTOR 3 IS ONLY APPLICABLE IN THE PAYEE "B" RECORD IF YOU USE SIX OR MORE PAYMENT AMOUNT FIELDS.

Diskette Position	Field Title	Length	Description and Remarks
42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
122–128	Blank	7	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
43–71	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "43" of this field and spell out the name of the city in the remaining positions.)
72–73	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "43" of the Payee City field.
74–82	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "43" in the Payee City field is a "1".
83–126	Blank	44	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)

SECTOR 1			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 of Sector 1. If fewer then 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE*

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.
92–128	**Blank**	**37**	**REQUIRED. Enter blanks.**
SECTOR 2			
1	**Record Sequence**	**1**	**REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.**
2	**Record Type**	**1**	**REQUIRED. Enter "B". Must be the second position of each PAYEE Record.**
3–42	**Second Payee Name Line**	**40**	**REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.**
43–82	**Payee Mailing Address**	**40**	**REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.**
83–111	**Payee City**	**29**	**REQUIRED. Enter the City, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)**
112–113	**Payee State**	**2**	**REQUIRED. Enter the abbreviation for the state or foreign county. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.**
114–122	**Payee ZIP Code**	**9**	**REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".**
123–126	**Blank**	**4**	**REQUIRED. Enter blanks.**
127–128	**State Code**	**2**	**REQUIRED. If this payee record is to be forwarded to a state agency as part of the combined Federal/Stae Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.**

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
42–51	**Payment Amount 2**	**10**	**This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.**
52–61	**Payment Amount 3**	**10**	**This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.**

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
62–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediatel after the last payment amount indicated as being used. Do not ente address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appear in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space i required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
102–128	Blank	27	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion o the name only in this field.* If there are multiple payees (*e.g.*, partner or joint owners), this field may be used for those payees' *name* who are not associated with the taxpayer identification number i positions 13–21 of Sector 1. *Do not enter address information in thi field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fil unused positions with blanks. The address MUST be present. Thi field MUST NOT contain any data other than the payee's mailin address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information i this field.* (If the payee lives outside of the United States, insert "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviations for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as show in Part A, Sec. 16. Use this field for state or country informatio *only*. If the code used is for a foreign country, insert a "1" in positio "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Cod *only*. For foreign countries, alpha characters are acceptable as lon as position "83" in the Payee City field is a "1".

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
123–126	Blank	4	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)

SECTOR 1			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–111	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line below. If there are multiple payees, *only the name* of the payee whose taxpayer indentification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
112–128	Blank	17	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–126	Blank	4	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)

SECTOR 1

42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–121	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF*

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.
122–128	Blank	7	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP code assigned by the U.S. Postal Service. If ony the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–126	Blank	4	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1 of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE “B” RECORD (USING SIX PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter “A” Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter “A” Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter “A” Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter “A” Record.
92–128	Blank	37	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a “2”. Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter “B”. Must be the second position of ea PAYEE Record.
3–42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the l payment amount indicated as being used. Do not enter address i formation in this field.* Enter the name of the payee (preferab surname first) whose taxpayer identification number appears in p sitions 13–21 of Sector 1. If fewer than 40 characters are require left-justify and fill unused positions with blanks. If more space required *for the name,* utilize the Second Payee Name Line fie below. If there are multiple payees, *only the name* of the pay whose taxpayer identification number has been provided can entered in this field. The names of the other payees may be enter in the Second Payee Name Line field. *NOTE: WHEN REPOR ING FORM 1098, “MORTGAGE INTEREST STATEMENT THE “A” RECORD WILL REFLECT THE NAME OF TH RECIPIENT OF THE INTEREST. THE “B” RECORD WIL REFLECT THE INDIVIDUAL PAYING THE INTEREST AN THE AMOUNT PAID.*
43–82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is ava able in the First Payee Name Line, *enter the remaining portion the name only in this field.* If there are multiple payees (*e.g.*, partn or joint owners), this field may be used for those payees' *nam* who are not associated with the taxpayer identification number positions 13–21 of Sector 1. *Do not enter address information in t field.* Left-justify and fill unused positions with blanks. FILL WIT BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIEL
83–122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and unused positions with blanks. The address MUST be present. T field MUST NOT contain any data other than the payee's mail address.
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a “3”. Used to sequence the sectors mak up a Service PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)—Continued

iskette osition	Field Title	Length	Description and Remarks
ECTOR 3 (Continued)			
	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
-31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
2–33	Payee State	2	REQUIRED. Enter the abbreviations for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
4–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".
3–126	Blank	84	REQUIRED. Enter blanks.
27–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)

ECTOR 1			
2–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
2–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
2–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
2–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
2–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
–101	Payment Amount 7	10	This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.
2–123	Blank	27	REQUIRED. Enter blanks.
ECTOR 2			
	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
3–42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. ***NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.***
43–82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
83–122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviations for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
34–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP code *only*. For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
43–126	Blank	84	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING EIGHT PAYMENT FIELDS)

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–101	Payment Amount 7	10	This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.
102–111	Payment Amount 8	10	This amount is identified by the amount indicator in position 26, Sector 1, of the Payer/Transmitter "A" Record.
112–128	Blank	17	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*

RECORD NAME: PAYEE "B" RECORD (USING EIGHT PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
43–82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
83–122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
34–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".
43–126	Blank	84	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING NINE PAYMENT FIELDS)

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE "B" RECORD (USING NINE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–101	Payment Amount 7	10	This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.
102–111	Payment Amount 8	10	This amount is identified by the amount indicator in position 26, Sector 1, of the Payer/Transmitter "A" Record.
112–121	Payment Amount 9	10	This amount is identified by the amount indicator in position 27, Sector 1, of the Payer/Transmitter "A" Record.
122–128	Blank	7	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
43–82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
83–122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain and data other than the payee's mailing address.
123–128	Blank	6	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING NINE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
34–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".
43–126	Blank	84	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

SEC. 7. PAYEE "B" RECORD—RECORD LAYOUTS FOR FORMS 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R AND 5498

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	BLANK
22–31	32–41	42–81	82–121	122–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–42	43–71	72–73	74–82	83–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–91	92–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–42	43–82	83–111	112–113	114–122	123–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–101	102–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

SECTOR 2 (Continued)

BLANK	STATE CODE
123–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)—Continued

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–111	112–128

SECTOR 2 (Continued)

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

SECTOR 2 (Continued)

BLANK	STATE CODE
123–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USNG FIVE PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–81	82–121	122–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–42	43–82	83–111	112–113	114–122	123–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

PAYEE "B" RECORD—RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)—Continued

ECTOR 1 (Continued)

BLANK
92–128

ECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–128

ECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–31	32–33	34–42	43–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING SEVEN PAYMENT AMOUNT FIELDS)

ECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

ECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	BLANK
92–101	102–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–31	32–33	34–42	43–126	127–128

PAYEE “B” RECORD—RECORD LAYOUT (USING EIGHT PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8	BLANK
92–101	102–111	112–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–31	32–33	34–42	43–126	127–128

PAYEE “B” RECORD—RECORD LAYOUT (USING NINE PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8	PAYMENT AMOUNT 9	BLANK
92–101	102–111	112–121	122–128

PAYEE "B" RECORD—RECORD LAYOUT (USING NINE PAYMENT AMOUNT FIELDS)—Continued

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–31	32–33	34–42	43–126	127–128

SEC. 8. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM 1099–A

01. This section contains the general payment information from individual statements for Form 1099–A. For detailed explanations of the 1099–A fields request a copy of the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W-2G" available from IRS offices.

02. For Form 1099–A, SECTOR 3 will be required if there is more than one payment field to be reported in the Payee "B" Record.

03. FORM 1099–A CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.

RECORD NAME: PAYEE "B" RECORD
FORM 1099–A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–4	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported (*e.g.*, if payments were made in 1986, enter "86"). Must be incremented each year.
5–6	Document Specific Code	2	REQUIRED. For Form 1099–A, enter blanks.
7	Blank or Corrected Return Indicator	1	REQUIRED. Enter blank. (Reserved for IRS use). Diskette position 7 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using either magnetic media or paper forms. IN PRIOR YEARS, DISKETTE POSITION 6 WAS USED AS THE CORRECTED RETURN INDICATOR. THIS HAS NOW CHANGED TO POSITION 7. *YOU MUST ADJUST YOUR PROGRAMS.*
8–11	Name Control	4	REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (-) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the Name Control:

RECORD NAME: PAYEE "B" RECORD—Continued

FORM 1099-A

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td></td><td></td><td></td><td>
<table>
<tr><th><i>Name</i></th><th><i>Name Control</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE*</td></tr>
<tr><td>James P. En Sr.</td><td>EN*</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*NOTE: Name Controls of less than four (4) significant characte must be left-justified and blank filled.
</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identi cation Number (TIN) in positions 13–21 as either an Employ Identification Number, a Social Security Number, or the reason number is shown. Enter the appropriate code from the followi table:
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, er a blank. If the number is unobtainable to legitimate cause; <i>e.g.</i>, number applied but not received, enter a blank.</td></tr>
</table>
</td></tr>
<tr><td>13–21</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Nu ber of the payee (SSN or EIN, as appropriate). Where an ide fication number has been applied for but not received or wh there is any other legitimate cause for not having an identifica number, <i>enter blanks</i>. Refer to Part A, Sec. 11.

<i>DO NOT ENTER HYPHENS, ALPHA CHARACTERS, AL OR ALL ZEROS</i>. Any record containing an invalid identifica number in this field will be returned for correction.</td></tr>
<tr><td>22–31</td><td>Payer's Account Number for Payee</td><td>10</td><td>REQUIRED. Payer may use this field to enter the payee's acc number. The use of this item will facilitate easy reference to spe records in the payer's file should any questions arise. DO N ENTER A TAXPAYER IDENTIFICATION NUMBER IN T FIELD. Enter blanks if the Payer's Account Number for Pay not to be entered in this field. An account number can be account number assigned by the payer to the payee (<i>i.e.</i>, chec account, savings account, etc.). THIS NUMBER WILL HEL DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT W YOU AND SHOULD BE UNIQUE TO IDENTIFY THE CIFIC TRANSACTION MADE WITH THE ORGANIZAT SHOULD MULTIPLE RETURNS BE FILED. This inform will be particularly necessary if you need to file a corrected re You are strongly encouraged to use this field. You may use number that will help identify the particular transaction tha are reporting. If a number is not determinable, enter blan</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued

FORM 1099-A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			fewer than ten characters are required, right-justify filling the remaining positions with blanks.
	Payment Amount Fields (must be numeric)		The number of payment amounts is dependent upon and must agree with the number of Amount Indicators present in positions 19–27 of Sector 1 of the "A" Record. The First Payee Name Line *must* appear immediately after the last payment amount indicated as being used. For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one ten position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE 1). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS* (except those items that reflect a loss on Form 1099–B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "123bbbbbb," the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb," the "B" Records must have only 5 payment amount fields. Payment amounts MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE 1: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)

FORM 1099–A

SECTOR 1 (Continued)			
32–41	Payment Amount 1	10	This amount is identified by the indicator in position 19 of Sector 1 of the Payer/Transmitter "A" Record. *This amount must always be present.*

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF SECTOR 1 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–128 OF SECTOR 1, POSITIONS 1–128 OF SECTOR 2 AND POSITIONS 1–128 OF SECTOR 3, IF NEEDED, OF THE PAYEE "B" RECORD. *FOR FORM 1099–A SECTOR 3 WILL BE REQUIRED IF THERE IS MORE THAN ONE PAYMENT FIELD TO BE REPORTED IN THE PAYEE "B" RECORD.* USE THE APPROPRIATE FORMAT AS REQUIRED.

42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued
FORM 1099-A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion o the name only in this field*. If there are multiple payees (*e.g.*, partner or joint owners), this field may be used for those payees' *name* who are not associated with the taxpayer identification number i positions 13–21 above. *Do not enter address information in this field*. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
122–128	Blank	7	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–42	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fil unused positions with blanks. The address MUST be present. Thi field MUST NOT contain any data other than the payee's mailin address.
43–71	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused po sitions with blanks. *Do not enter state and ZIP Code information i this field*. (If the payee lives outside of the United States, insert "1" in position "43" of this field and spell out the name of the cit in the remaining positions.)
72–73	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign coun try. You *MUST* use valid U.S. Postal Service abbreviations as show in Part A, Sec. 16. Use this field for state or country informatio *only*. If the code used is for a foreign country, insert a "1" in positio "43" of the Payee City field.
74–82	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S Postal Service. If only the first 5 digits are known, left-justify an *fill the unused positions with blanks*. Use this field for the ZIP Cod *only*. For foreign countries, alpha characters are acceptable as lon as position "43" in the Payee City field is a "1".
83–88	Lender's Date of Acquisition or Abandonment	6	REQUIRED *FOR FORM 1099–A ONLY*. Enter the date of you acquisition of the secured property or the date you first knew o had reason to know that the property was abandoned in the forma MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.
89	Liability Indicator	1	REQUIRED *FOR FORM 1099–A ONLY*. Enter the appropriat indicator from table below: *Indicator* — *Usage* 1 — Borrower is personally liable for repaymen of the debt. Blank — Borrower is *not* liable for repayment of th debt.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued

FORM 1099-A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
90-126	Description	37	REQUIRED *FOR FORM 1099-A ONLY*. Enter a brief description of the property. For example, for real property, enter the address, section, lot and block. For personal property, enter the type, make and model (*e.g.*, Car-1986 Buick Regal or Office Equipment, etc.).
127–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)

FORM 1099–A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
92–128	Blank	37	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	2	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)

RECORD NAME: PAYEE “B” RECORD (USING TWO PAYMENT FIELDS)—Continued

FORM 1099-A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign cou try. You *MUST* use valid U.S. Postal Service abbreviations as show in Part A, Sec. 16. Use this field for state or country informatio *only*. If the code used is for a foreign country, insert a “1” in positio “83” of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S Postal Service. If only the first 5 digits are known, left-justify an *fill the unused positions with blanks*. Use this field for the ZIP Cod *only*. For foreign countries, alpha characters are acceptable as lon as position “83” in the Payee City field is a “1”.
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a “3”. Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter “B”. Must be the second position of eac PAYEE Record.
3–82	Blank	80	REQUIRED. Enter blanks.
83–88	Lender’s Date of Acquisition or Abandonment	6	REQUIRED *FOR FORM 1099-A ONLY*. Enter the date of you acquisition of the secured property or the date you first knew o has reason to know that the property was abandoned in the forma MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.
89	Liability Indicator	1	REQUIRED *FOR FORM 1099-A ONLY*. Enter the appropriat indicator from table below: *Indicator* — *Usage* 1 — Borrower is personally liable for repaymen of the debt. Blank — Borrower is *not* liable for repayment of th debt.
90–126	Description	37	REQUIRED *FOR FORM 1099-A ONLY*. Enter a brief descriptio of the property. For example, for real property, enter the addres section, lot and block. For personal property, enter the type, mak and model (*e.g.*, Car–1986 Buick Regal or Office Equipment, etc.)
127–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE “B” RECORD (USING THREE PAYMENT FIELDS)

FORM 1099-A

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter “A” Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter “A” Record.
62–101	First Payee Name Line	40	REQUIRED. *The first Payee Name Line must appear immedia after the last payment amount indicated as being used. Do not en address information in this field.* Enter the name of the payee (p erably surname first) whose taxpayer identification number appe in positions 13–21 above. If fewer than 40 characters are requi

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

FORM 1099-A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
102–128	Blank	27	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–82	Blank	80	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued
FORM 1099-A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
83–88	Lender's Date of Acquisition or Abandonment	6	REQUIRED *FOR FORM 1009–A ONLY*. Enter the date of you acquisition of the secured property or the date you first knew o had reason to know that the property was abandoned in the form MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.
89	Liability Indicator	1	REQUIRED *FOR FORM 1099–A ONLY*. Enter the appropriat indicator from the table below: *Indicator* — *Usage* 1 — Borrower is personally liable for repayment of th debt. Blank — Borrower is *not* liable for repayment of the debt.
90–126	Description	37	REQUIRED *FOR FORM 1099–A ONLY*. Enter a brief descrip tion of the property. For example, for real property, enter th address, section, lot and block. For personal property, enter th type, make and model (*e.g.*, Car–1986 Buick Regal or Office Equip ment, etc.).
127–128	Blank	2	REQUIRED. Enter blanks.

SEC. 9. PAYEE "B" RECORD—RECORD LAYOUT FOR FORM 1099–A

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)
FORM 1099–A

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	BLANK
22–31	32–41	42–81	82–121	122–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–71	72–73	74–82

SECTOR 2 (Continued)

LENDER'S DATE OF ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION	BLANK
83–88	89	90–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

FORM 1099–A

ECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–91	92–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	LENDER'S DATE OF ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION
1	2	3–82	83–88	89	90–126

SECTOR 3 (Continued)

BLANK
127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

FORM 1099–A

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–101	102–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–128

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)—Continued
FORM 1099-A

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	LENDER'S DATE OR ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION
1	2	3–82	83–88	89	90–126

SECTOR 3 (Continued)

BLANK
127–128

SEC. 10. PAYEE "B" RECORDS—FIELD DESCRIPTION FOR FORM 1099–B

.01 This section contains the general payment information from individual statements for Form 1099–B. For detailed explanations of the 1099-B fields request a copy of the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" available from IRS offices.

.02 For Form 1099–B, SECTOR 3 will be required if there is more than one payment field to be reported in the Payee "B" Record.

.03 FORM 1099–B CANNOT B FILED UNDER THE COMBINE FEDERAL/STATE FILING PROGRAM.

RECORD NAME: PAYEE "B" RECORD
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1." Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B." Must be the second position of ea PAYEE Record.
3–4	Payment Year	2	REQUIRED. Must be the last two digits of the year for whi payments are being reported (*e.g.*, if payments were made in 198 enter "86"). Must be incremented each year.
5–6	Document Specific Code	2	REQUIRED. For Form 1099–B, enter blanks.
7	Blank or Corrected Return Indicator	1	REQUIRED. Enter blank. (Reserved for IRS use.) Diskette p sition 7 is used to indicate a corrected return. Refer to Part A, Se 10 for specific instructions on how to file corrected returns usi either magnetic media or paper forms. IN PRIOR YEARS, DI KETTE POSITION 6 WAS USED AS THE CORRECTED R TURN INDICATOR. THIS HAS NOW CHANGED T POSITION 7. *YOU MUST ADJUST YOUR PROGRAMS.*
8–11	Name Control	4	REQUIRED. Enter the first 4 letters of the surname of the pay Surnames of less than four (4) letters should be left-justified, fill the unused positions with blanks. Special characters and imbedd blanks should be removed. IF THE NAME CONTROL IS N DETERMINABLE BY THE PAYER, SUCH AS IN THE CA OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A d (-) or ampersand (&) are the only acceptable special charact The following examples may be helpful to you in developing Name Control:

RECORD NAME: PAYEE "B" RECORD—Continued

FORM 1099-B

<table>
<tr><th>iskette
osition</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">ECTOR 1 (Continued)</td></tr>
<tr><td></td><td></td><td></td><td>
<table>
<tr><th><i>Name</i></th><th><i>Name Control</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE *</td></tr>
<tr><td>James P. En Sr.</td><td>EN *</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL–R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must be left-justified and blank filled.
</td></tr>
<tr><td>12</td><td>Type of
TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identification Number (TIN) in positions 13–21 as either an Employer Identification Number, a Social Security Number, or the reason no number is shown. Enter the appropriate code from the following table:
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, enter a blank. If the number is unobtainable due to legitimate cause; <i>e.g.</i>, number applied for but not received, enter a blank.</td></tr>
</table>
</td></tr>
<tr><td>13–21</td><td>Taxpayer
Identification
Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the payee (SSN or EIN, as appropriate). Where an identification number has been applied for but not received or where there is any other legitimate cause for not having an identification number, <i>enter blanks</i>. Refer to Part A, Sec. 11.

<i>DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS.</i> Any record containing an invalid identification number in this field will be returned for correction.</td></tr>
<tr><td>22–31</td><td>Payer's
Account Number
for Payee</td><td>10</td><td>REQUIRED. Payer may use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payer's file, should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. Enter blanks if the Payer's Account Number for Payee is not to be entered in this field. An account number can be any account number assigned by the payer to the payee (<i>i.e.</i>, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099-B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			number that will help identify the particular transaction that yo are reporting. If a number is not determinable, enter blanks. I fewer than ten characters are required, right-justify filling the remaining positions with blanks.
	Payment Amount Fields (must be numeric)		The number of payment amounts is dependent on the number of Amount Indicators present in positions 19–27 of Sector 1 of the "A" Record. The First Payee Name Line *must* appear after the las payment amount indicated as being used. For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one te position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE 1). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS* (except those items that reflect a loss on Form 1099-B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "123bbbbbb," the Payee "B" Records must have only 3 payment amount fields. I Amount Indicators are reflected as "12367bbbb," the "B" Records must have only 5 payment amount fields. Payment amounts MUS be right-justified and unused positions MUST be zero filled. Federa income tax withheld is not reported as a negative amoun NOTE: 1 If any one payment amount exceeds "9999999999" (do lars and cents), as many SEPARATE Payee "B" Records as ne essary to contain the total amount MUST be submitted for th Payee.
32–41	Payment Amount 1	10	This amount is identified by the indicator in position 19 of Sect 1 of the Payer/Transmitter "A" Record. *This amount must alwa be present.*

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE " RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN PO TIONS 19–27 OF SECTOR 1 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FO COMPLETING POSITIONS 42–128 OF SECTOR 1, POSITIONS 1–128 OF SECTOR 2, AND POSITIONS 1–128 OF SECTO 3, IF NEEDED, OF THE PAYEE "B" RECORD. *FOR FORM 1099–B, SECTOR 3 WILL BE REQUIRED IF THERE MORE THAN ONE PAYMENT FIELD TO BE REPORTED IN THE PAYEE "B" RECORD.* USE THE APPROPRIA FORMAT AS REQUIRED.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)
FORM 1099-B

SECTOR 1 (Continued)			
42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immedia after the last payment amount indicated as being used. Do not e address information in this field.* Enter the name of the payee (p erably surname first) whose taxpayer identification number app in positions 13–21 above. If fewer than 40 characters are requi left-justify and fill unused positions with blanks. If more spac required *for this name,* utilize the Second Payee Name Line below. If there are multiple payees, *only the name* of the pa

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued
FORM 1099-B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners) this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
122–128	Blank	7	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED Must be a "2." Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B." Must be the second position of each PAYEE Record.
3–42	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
43–71	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "43" of this field and spell out the name of the city in the remaining positions.)
72–73	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "43" of the Payee City field.
74–82	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "43" in the Payee City field is a "1".
83–85	Blank	3	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transaction
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued
FORM 1099-B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
93–100	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Com mittee on Uniform Security Identification Procedures) number o the items reported for Amount Indicator "2" (Stocks, bonds, etc Enter blanks if this is an aggregate transaction. Enter "0" (zero if the number is not available. For CUSIP numbers with more tha 8 characters, supply the *first* 8.
101–126	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief descriptio of the item or services for which the proceeds are being reported If fewer than 26 characters are required, left-justify and fill unuse positions with blanks. For regulated futures contracts, enter RFC Enter blanks if this is an aggregate transaction.
127–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)
FORM 1099–B

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20 Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediatel after the last payment amount indicated as being used. Do not ente address information in this field*. Enter the name of the payee (pref erably surname first) whose taxpayer identification number appear in positions 13–21 above. If fewer than 40 characters are required left-justify and fill unused positions with blanks. If more space i required *for the name*, utilize the Second Payee Name Line below If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
92–128	Blank	37	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avail able in the First Payee Name Line, *enter the remaining portion o the name only in this field*. If there are multiple payees (*e.g.*, partner or joint owners) this field may be used for those payees' *names* wh are not associated with the taxpayer identification number in po sitions 13–21 of Sector 1. *Do not enter address information in thi field*. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fil unused positions with blanks. The address MUST be present. Thi field MUST NOT contain any data other than payee's mailing address.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued

FORM 1099-B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is a foreign country, insert a "1" in position "83" of the Payee City field.
114-122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–85	Blank	83	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transaction
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
93–100	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedure) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
101–126	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
127–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20 Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21 Sector 1, of the Payer/Transmitter "A" Record.
62–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediatel after the last payment amount indicated as being used. Do not ente address information in this field.* Enter the name of the payee (pref erably surname first) whose taxpayer identification number appear in positions 13–21 above. If fewer than 40 characters are required left-justify and fill unused positions with blanks. If more space i required *for the name,* utilize the Second Payee Name Line fiel below. If there are multiple payees, *only the name* of the paye whose taxpayer identification number has been provided can b entered in this field. The names of the other payees may be entere in the Second Payee Name Line field.
102–128	Blank	27	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avai able in the First Payee Name Line, *enter the remaining portion o the name only in this field.* If there are multiple payees (*e.g.*, partner or joint owners), this field may be used for those payees' *name* who are not associated with the taxpayer identification number i positions 13–21 of Sector 1. *Do not enter address information in th field.* Left-justify and fill unused positions with blanks. FILL WIT BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and f unused positions with blanks. The address MUST be present. Th field MUST NOT contain any data other than the payee's mailin address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused p sitions with blanks. *Do not enter state and ZIP Code information i this field.* (If the payee lives outside of the United States, insert "1" in position "83" of this field and spell out the name of the ci in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign cou try. You *MUST* use valid U.S. Postal Service abbreviations as show in Part A, Sec. 16. Use this field for state or country informatio *only*. If the code used is for a foreign country, insert a "1" in positio "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U. Postal Service. If only the first 5 digits are known, left-justify a *fill the unused positions with blanks*. Use this field for the ZIP Co *only*. For foreign countries, alpha characters are acceptable as lo as position "83" in the Payee City field is a "1".

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

FORM 1099-B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
–85	Blank	83	REQUIRED. Enter blanks.
36	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099-B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transaction
37–92	Date of Sale	6	REQUIRED *FOR FORM 1099-B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
03–100	CUSIP No.	8	REQUIRED *FOR FORM 1099-B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
01–126	Description	26	REQUIRED *FOR FORM 1099-B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
27–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)

FORM 1099-B

ECTOR 1 (Continued)			
2–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
2–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
2–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
2–111	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

FORM 1099-B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
112–128	Blank	17	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–85	Blank	83	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued
FORM 1099-B

iskette sition	Field Title	Length	Description and Remarks
ECTOR 3 (Continued)			
	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099-B ONLY.* Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date. blank — Date of Sale is the trade date or this is an aggregate transaction.
-92	Date of Sale	6	REQUIRED *FOR FORM 1099-B ONLY.* Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
-100	CUSIP No.	8	REQUIRED *FOR FORM 1099-B ONLY.* Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
01–126	Description	26	REQUIRED *FOR FORM 1099-B ONLY.* Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
27–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)
FORM 1099-B

ECTOR 1 (Continued)			
2–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
2–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
2–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
2–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
2–121	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
122–128	Blank	7	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)—Continued
FORM 1099-B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avai able in the First Payee Name Line, *enter the remaining portion o the name only in this field.* If there are multiple payees (*e.g.*, partner or joint owners), this field may be used for those payees' *name* who are not associated with the taxpayer identification number i positions 13–21 of Sector 1. *Do not enter address information in thi field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fi unused positions with blanks. The address MUST be present. Thi field MUST NOT contain any data other than payee's mailing a dress.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused po sitions with blanks. *Do not enter state and ZIP Code information i this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the ci in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Pa A, Sec. 16. Use this field for state or country information *only*. I the code used is for a foreign country, insert a "1" in position "8 of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S Postal Service. If only the first 5 digits are known, left-justify an *fill the unused positions with blanks.* Use this field for the ZIP Co *only*. For foreign countries, alpha characters are acceptable as lon as position "83" in the Payee City field is a "1".
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors maki up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of ea PAYEE Record.
3–85	Blank	83	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate dicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement d blank — Date of Sale is the trade date or this i aggregate transaction

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)—Continued

FORM 1099-B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
93–100	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters supply the *first* 8.
101–126	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
127–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)

FORM 1099–B

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–128	Blank	37	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the last payment amount indicated as being used. Do not enter address information in the field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name line field.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)—Continued
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
43–82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion o* *the name only in this field.* If there are multiple payees (*e.g.*, partner or joint owners), this field may be used for those payees' *name* who are not associated with the taxpayer identification number i positions 13–21 of Sector 1. *Do not enter address information in thi* *field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
83–122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fil unused positions with blanks. The address MUST be present. Thi field MUST NOT contain any data other than the payee's mailin address.
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information i* *this field.* (If the payee lives outside of the United States, insert "1" in position "3" of this field and spell out the name of the cit in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You MUST use valid U.S. Postal Service abbreviations as show in Part A, Sec. 16. Use this field for state or country informatio *only*. If the code used is for a foreign country, insert a "1" in positio "3" of the Payee City field.
34–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S Postal Service. If only the first 5 digits are known, left-justify an *fill the unused positions with blanks.* Use this field for the ZIP Cod *only*. For foreign countries, alpha characters are acceptable as lo as position "3" in the Payee City field is a "1".
43–85	Blank	43	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement dat blank — Date of Sale is the trade date or this is aggregate transaction
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date o the actual settlement date of the transaction in the format MMDDY Enter blanks if this is an aggregate transaction. DO NOT ENTE HYPHENS OR SLASHES.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)—Continued
FORM 1099–B

skette sition	Field Title	Length	Description and Remarks
CTOR 3 (Continued)			
-100	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY.* Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
1–126	Description	26	REQUIRED FOR *FORM 1099–B ONLY.* Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
7–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)
FORM 1099–B

ECTOR 1 (Continued)			
-51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
-61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
-71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
-81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
-91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
-101	Payment Amount 7	10	This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.
2–128	Blank	27	REQUIRED. Enter blanks.
CTOR 2			
	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
42	First Payee Name Line	40	REQUIRED. *The First Payee Name line must appear after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued

FORM 1099-B1

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
43–82	Second Payee Name Line	40	**REQUIRED**. If the payee name requires more space than is avail- able in the First Payee Name Line, *enter the remaining portion of the name only in this field*. If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 of Sector 1. *Do not enter address information in this field*. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
83–122	Payee Mailing Address	40	**REQUIRED**. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
123–128	Blank	6	**REQUIRED**. Enter blanks.
SECTOR 3			
1	Record Sequence	1	**REQUIRED**. Must be a "3". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	**REQUIRED**. Enter "B". Must be the second position of eac PAYEE Record.
3–31	Payee City	29	**REQUIRED**. Enter the city, left-justified and fill the unused po sitions with blanks. *Do not enter state and ZIP Code information i this field*. (If the payee lives outside of the United States, insert "1" in position "3" of this field and spell out the name of the ci in the remaining positions.)
32–33	Payee State	2	**REQUIRED**. Enter the abbreviation for the state or foreign cou try. You *MUST* use valid U.S. Postal Service abbreviations as show in Part A, Sec. 16. Use this field for state or country informati *only*. If the code used is for a foreign country, insert a "1" in positi "3" of the Payee City field.
34–42	Payee ZIP Code	9	**REQUIRED**. Enter the valid 9 digit ZIP Code assigned by the U. Postal Service. If only the first 5 digits are known, left-justify a *fill the unused positions with blanks*. Use this field for the ZIP Co *only*. For foreign countries, alpha characters are acceptable as lo as position "3" in the Payee City field is a "1".
43–85	Blank	43	**REQUIRED**. Enter blanks.
86	Date of Sale Indicator	1	**REQUIRED** *FOR FORM 1099–B ONLY*. Enter appropriate dicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement d blank — Date of Sale is the trade date or this i aggregate transaction
87–92	Date of Sale	6	**REQUIRED** *FOR FORM 1099–B ONLY*. Enter the trade dat the actual settlement date of the transaction in the format MMDD Enter blanks if this is an aggregate transaction. DO NOT ENT HYPHENS OR SLASHES.
93–100	CUSIP No.	8	**REQUIRED** *FOR FORM 1099–B ONLY*. Enter the CUSIP (C mittee on Uniform Security Identification Procedures) numb the items reported for Amount Indicator "2" (Stocks, bonds, e

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued

FORM 1099–B1

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
			Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
101–126	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or service for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
127–128	Blank	2	REQUIRED. Enter blanks.

SEC. 11. PAYEE "B" RECORD—RECORD LAYOUT FOR FORM 1099–B

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	BLANK
22–31	32–41	42–81	82–121	122–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–71	72–73	74–82	83–85

SECTOR 2 (Continued)

DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
86	87–92	93–100	101–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)—Continued

FORM 1099-B

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–91	92–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–85	86	87–92	93–100	101–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–101	102–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–85	86	87–92	93–100	101–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CON-TROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–111	112–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–85	86	87–92	93–100	101–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING FIVE PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–81	82–121	122–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–85	86	87–92	93–100	101–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6	BLANK
22–31	32–41	42–51	52–61	62–71	72–81	82–91	92–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE
1	2	3–31	32–33	34–42	43–85	86	87–92

SECTOR 3 (Continued)

CUSIP NO.	DESCRIPTION	BLANK
93–100	101–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING SEVEN PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATIO NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMEN AMOUN
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	BLANK
92–101	102–128

PAYEE "B" RECORD—RECORD LAYOUT (USING SEVEN PAYMENT AMOUNT FIELDS)—Continued
FORM 1099–B

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–31	32–33	34–42	43–85

SECTOR 3 (Continued)

DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
86	87–92	93–100	101–126	127–128

SEC. 12. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM W–2G

.01 This section contains the general payment information from individual statements for Form W–2G. For detailed explanations of the W–2G fields, see the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G."

.02 When reporting information for Form W–2G, the Payee "B" Records must contain 3 Sectors.

.03 FORM W–2G CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.

RECORD NAME: PAYEE "B" RECORD
FORM W–2G

Diskette Position	Field Title	Length	Description anf Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–4	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported (*e.g.*, if payments were made in 1986, enter "86"). Must be incremented each year.
5–6	Document Specific Code Type of Wager (Form W–2G only)	2	REQUIRED for Form W–2G. Use only for reporting the Type of Wager on *Form W–2G*. This code will appear in position 5. Position 6 will be blank.

Category	*Code*
Horse Race Track (or Off Track Betting of a Horse Track nature)	1
Dog Race Track (or Off Track Betting of a Dog Track nature)	2
Jai-alai	3
State Conducted Lottery	4
Keno	5
Casino Type Bingo. DO NOT use this code for any other type of Bingo winnings (*i.e,* Church, Fire Dept., etc.).	6

RECORD NAME: PAYEE "B" RECORD—Continued
FORM W-2G

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td></td><td></td><td></td><td><table><tr><td>Slot Machines</td><td>7</td></tr><tr><td>Any other type of gambling winnings. This includes Church bingo, Fire Dept. Bingo, unlabeled winnings, etc.</td><td>8</td></tr></table></td></tr>
<tr><td>7</td><td>Blank or Corrected Return Indicator</td><td>1</td><td>REQUIRED. Enter blank. (Reserved for IRS use). Diskette po sition 7 is used to indicate a corrected return. Refer to Part A, Se 10 for specific instructions on how to file corrected returns usin either magnetic media or paper forms. IN PRIOR YEARS, DI KETTE POSITION 6 WAS USED AS THE CORRECTED R TURN INDICATOR. THIS HAS NOW CHANGED T POSITION 7. *YOU MUST ADJUST YOUR PROGRAMS.*</td></tr>
<tr><td>8–11</td><td>Name Control</td><td>4</td><td>REQUIRED. Enter the first 4 letters of the surname of the paye Surnames of less than four (4) letters should be left-justified, filli the unused positions with blanks. Special characters and imbedd blanks should be removed. IF THE NAME CONTROL IS N DETERMINABLE BY THE PAYER, SUCH AS IN THE CA OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A d (-) or ampersand (&) are the only acceptable special charact The following examples may be helpful to you in developing Name Control:
<table><tr><th>*Name*</th><th>*Name Control*</th></tr><tr><td>John Brown</td><td>BROW</td></tr><tr><td>John A. Lee</td><td>LEE*</td></tr><tr><td>James P. En Sr.</td><td>EN*</td></tr><tr><td>John O'Neill</td><td>ONEI</td></tr><tr><td>Mary Van Buren</td><td>VANB</td></tr><tr><td>John Diben Edetto</td><td>DIBE</td></tr><tr><td>Juan De Jesus</td><td>DEJE</td></tr><tr><td>John A. El-Roy</td><td>EL-R</td></tr><tr><td>Mr. John Smith</td><td>SMIT</td></tr><tr><td>Joe McCarthy</td><td>MCCA</td></tr><tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr><tr><td>Mark D'Allesandro</td><td>DALL</td></tr></table>*Name Controls of less than (4) significant characters must be justified and blank filled.</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Ide cation Number (TIN) in positions 13–21 as either an Emp Identification Number, a Social Security Number, or the reas number is shown. Enter the appropriate code from the follo table:
<table><tr><th>*Type of TIN*</th><th>*TIN*</th><th>*Type of Account*</th></tr><tr><td>1</td><td>EIN</td><td>A business or an orgainzation</td></tr><tr><td>2</td><td>SSN</td><td>An individual</td></tr><tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, e blank. If the number is unobtainable d legitimate cause; *e.g.*, number applied f not received, enter a blank.</td></tr></table></td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued
FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
13-21	Taxpayer Identification Number	9	REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the payee (SSN or EIN, as appropriate). Where an identification number has been applied for but not received or where there is any other legitimate cause for not having an identification number, *enter blanks*. Refer to Part A, Sec. 11. *DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS.* Any record containing an invalid identifying number in this field will be returned for correction.
22-31	Payer's Account Number for Payee	10	REQUIRED. Payer may use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payer's file should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. An account number can be any account number assigned by the payer to the payee (*i.e*, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use the field. You may use any number that will help identify the particular transaction that you are reporting. If a number is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.
	Payment Amount Fields (must be numeric)		The number of payment amounts is dependent on the number of Amount Indicators present in positions 19–27 of Sector 1 of the "A" Record. The First Payee Name Line *must* appear immediately after the last payment amount indicated as being used. For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one ten position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE 1). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS* (except those items that reflect a loss on Form 1099–B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "123bbbbbb", the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb", the "B" Records must have only 5 payment amount fields. Payment amounts MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE 1: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee.
32-41	Payment Amount 1	10	This amount is identified by the indicator in position 19 of Sector 1 of the Payer/Transmitter "A" Record. *This amount must always be present.*

RECORD NAME: PAYEE "B" RECORD—Continued
FORM W–2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF SECTOR 1 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–128 OF SECTOR 1, POSITIONS 1–128 OF SECTOR 2, AND POSITIONS 1–128 OF SECTOR 3 OF THE PAYEE "B" RECORD. *WHEN REPORTING INFORMATION FOR FORM W–2G THREE SECTORS MUST BE USED TO MAKE UP A PAYEE "B" RECORD.* USE THE APPROPRIATE FORMAT AS REQUIRED.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)
FORM W–2G

SECTOR 1			
42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediatel after the last payment amount indicated as being used. Do not ente address information in this field.* Enter the name of the payee (pre- erably surname first) whose taxpayer identification number appear in positions 13–21 above. If fewer than 40 characters are required left-justify and fill unused positions with blanks. If more space i required *for the name,* utilize the Second Payee Name Line fiel below. If there are multiple payees, *only the name* of the pa whose taxpayer identification number has been provided can b entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avail- able in the First Payee Name Line, *enter the remaining portion o the name only in this field.* If there are multiple payees (*e.g.*, partner or joint owners), this field may be used for those payees' *name* who are not associated with the taxpayer identification number i positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD
122–128	Blank	7	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–42	Payee Mailing Address	29	REQUIRED. Enter mailing address of payee. Left-justify and fi unused positions with blanks. The address MUST be present. Thi field MUST NOT contain any data other than the payee's mailin address.
43–71	Payee City	40	REQUIRED. Enter the city, left-justified and fill the unused po- sitions with blanks. *Do not enter state and ZIP Code information i this field.* (If the payee lives outside of the United States, insert a "1" in position "43" of this field and spell out the name of the cit in the remaining positions.)
72–73	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign coun- try. You *MUST* use valid U.S. Postal Service abbreviations as show in Part A, Sec. 16. Use this field for state or country informatio

RECORD NAME: PAYEE “B” RECORD (USING ONE PAYMENT FIELD)—Continued
FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
			only. If the code used is for a foreign country, insert a “1” in position “43” of the Payee City field.
74–82	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position “43” in the Payee City field is a “1”.
83–128	Blank	46	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a “3”. Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter “B”. Must be the second position of each PAYEE Record.
3–60	Blank	58	REQUIRED. Enter blanks.
61–66	Date Won	6	REQUIRED *FOR FORM W-2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.
67–81	Transaction	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number or any other information that will help identify the winning transaction. If no entry, enter blanks.
82–86	Race	5	REQUIRED *FOR FORM W-2G ONLY*. The race (or game) applicable to the winning ticket. If no entry, enter blanks.
87–91	Cashier	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
92–96	Window	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.
97–111	First ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
112–126	Second ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
127–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE “B” RECORD (USING TWO PAYMENT FIELDS)
FORM W-2G

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter “A” Record.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued

FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immedia after the last payment amount indicated as being used. Do not en address information in this field.* Enter the name of the payee (pr erably surname first) whose taxpayer identification number appea in positions 13–21 above. If fewer than 40 characters are requir left-justify and fill unused positions with blanks. If more space i required *for the name,* utilize the Second Payee Name Line fi below. If there are multiple payees, *only the name* of the pay whose taxpayer identification number has been provided can b entered in this field. The names of the other payees may be enter in the Second Payee Name Line field.
92–128	Blank	37	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors maki up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of ea PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is ava able in the First Payee Name Line, *enter the remaining portion the name only in this field.* If there are multiple payees (*e.g.*, partne or joint owners), this field may be used for those payees' *nam* who are not associated with the taxpayer identification number positions 13–21 of Sector 1. *Do not enter address information in th field.* Left-justify and fill unused positions with blanks. FILL WIT BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIEL
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and unused positions with blanks. The address MUST be present. Th field MUST NOT contain any data other than payee's mailing a dress.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused p sitions with blanks. *Do not enter state and ZIP Code information this field.* (If the payee lives outside of the United States, inser "1" in position "83" of this field and spell out the name of the c in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state of foreign cou try. You *MUST* use valid U.S. Postal Service abbreviations as sho in Part A, Sec. 16. Use this field for state or country informa *only*. If the code used is for a foreign country, insert a "1" in posi "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U Postal Service. If only the first 5 digits are known, left-justify a *fill the unused positions with blanks.* Use this field for the ZIP Co *only*. For foreign countries, alpha characters are acceptable as lo as position "83" in the Payee City field is a "1".
123–128	Blank	6	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued
FORM W–2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-60	Blank	58	REQUIRED. Enter blanks.
61–66	Date Won	6	REQUIRED *FOR FORM W–2G ONLY*. Enter the date of the winning event in MMDDYY FORMAT. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.
67–81	Transaction	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number or any other information that will help identify the winning transaction. If no entry, enter blanks.
82–86	Race	5	REQUIRED *FOR FORM W–2G ONLY*. The race (or game) applicable to the winning ticket. If no entry, enter blanks.
87–91	Cashier	5	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
92–96	Window	5	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.
97–111	First ID	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
112–126	Second ID	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
127–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)
FORM W–2G

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

FORM W–2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
102–128	Blank	27	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of ea PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avai able in the First Payee Name Line, *enter the remaining portion the name only in this field.* If there are multiple payees (*e.g.*, partne or joint owners), this field may be used for those payees' *name* who are not associated with the taxpayer identification number positions 13–21 of Sector 1. *Do not enter address information in th field.* Left-justify and fill unused positions with blanks. FILL WIT BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIEL
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and unused positions with blanks. The address MUST be present. Th field MUST NOT contain any data other than the payee's maili address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused p sitions with blanks. *Do not enter state and ZIP Code information this field.* (If the payee lives outside of the United States, inser "1" in position "83" of this field and spell out the name of the c in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign cou try. You *MUST* use valid U.S. Postal Service abbreviations as sho in Part A, Sec. 16. Use this field for state or country informati *only*. If the code used is for a foreign country, insert a "1" in positi "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U Postal Service. If only the first 5 digits are known, left-justify a *fill the unused positions with blanks*. Use this field for the ZIP Co *only*. For foreign countries, alpha characters are acceptable as lo as position "83" in the Payee City field is a "1".
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors mak up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of e PAYEE Record.
3–60	Blank	58	REQUIRED. Enter blanks.
61–66	Date Won	6	REQUIRED *FOR FORM W–2G ONLY*. Enter the date of winning event in MMDDYY format. This is not the date the mo was paid, if paid after the date of the race (or game). DO N ENTER HYPHENS OR SLASHES.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued
FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
67–81	Transaction	15	REQUIRED *FOR FORM W-2G ONLY.* If applicable, the ticket number, card number (and color, if applicable), machine serial number or any other information that will help identify the winning transaction. If no entry, enter blanks.
82–86	Race	5	REQUIRED *FOR FORM W-2G ONLY.* The race (or game) applicable to the winning ticket. If no entry, enter blanks.
87–91	Cashier	5	REQUIRED *FOR FORM W-2G ONLY.* If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
92–96	Window	5	REQUIRED *FOR FORM W-2G ONLY.* If applicable, the location of the person paying the winnings. If no entry, enter blanks.
97–111	First ID	15	REQUIRED *FOR FORM W-2G ONLY.* If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
112–126	Second ID	15	REQUIRED *FOR FORM W-2G ONLY.* If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
127–128	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)
FORM W-2G

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–111	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positons 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
112–128	Blank	17	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avai able in the First Payee Name Line, *enter the remaining portion o the name only in this field*. If there are multiple payees (*e.g.*, partner or joint owners), this field may be used for those payees' *name* who are not associated with the taxpayer identification number i positions 13–21 of Sector 1. *Do not enter address information in th field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fi unused positions with blanks. The address MUST be present. Thi field MUST NOT contain any data other than the payee's mailin address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information i this field.* (If the payee lives outside of the United States, insert "1" in position "83" of this field and spell out the name of the cit in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as show in Part A, Sec. 16. Use this field for state or country informatio *only*. If the code used is for a foreign country, insert a "1" in positio "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit Zip Code assigned by the U.S Postal Service. If only the first 5 digits are known, left-justify an *fill the unused positions with blanks*. Use this field for the ZIP Cod *only*. For foreign countries, alpha characters are acceptable as lon as position "83" in the Payee City field is a "1".
123–128	Blank	6	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of ea PAYEE Record.
3–60	Blank	58	REQUIRED. Enter blanks.
61–66	Date Won	6	REQUIRED *FOR FORM W-2G ONLY*. Enter the date of t winning event in MMDDYY format. This is not the date the mon was paid, if paid after the date of the race (or game). DO N ENTER HYPHENS OR SLASHES.
67–81	Transaction	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the tic number, card number (and color, if applicable), machine se number or any other information that will help identify the winn transaction. If no entry, enter blanks.
82–86	Race	5	REQUIRED *FOR FORM W-2G ONLY*. The race (or game) plicable to the winning ticket. If no entry, enter blanks.
87–91	Cashier	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the init of the cashier and/or the window number making the winning p ment. If no entry, enter blanks.

RECORD NAME: PAYEE “B” RECORD (USING FOUR PAYMENT FIELDS)—Continued
FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
92–96	Window	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable the location of the person paying the winnings. If no entry, enter blanks.
97–111	First ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
112–126	Second ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
127–128	Blank	2	REQUIRED. Enter blanks.

SEC. 13. PAYEE “B” RECORD—RECORD LAYOUTS FOR FORM W-2G

PAYEE “B” RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)
FORM W-2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER’S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	BLANK
22–31	32–41	42–81	82–121	122–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–71	72–73	74–82	83–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–60	61–66	67–81	82–86	87–91

SECTOR 3 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
92–96	97–111	112–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

FORM W-2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–91	92–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–60	61–66	67–81	82–86	87–91

SECTOR 3 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
92–96	97–111	112–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

FORM W-2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–101	102–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–128

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)—Continued
FORM W–2G

ECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–60	61–66	67–81	82–86	87–91

ECTOR 3 (Continued)

WINDOW	FIRST iD	SECOND ID	BLANK
92–96	97–111	112–126	127–128

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)
FORM W–2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–111	112–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–128

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–60	61–66	67–81	82–86	87–91

SECTOR 3 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
92–96	97–111	112–126	127–128

SEC. 14. END OF PAYER "C" RECORD

.01 The Control Total fields have been expanded from 12 to 15 positions. Adjust your programs accordingly.

.02 The End of Payer "C" Record is a summary record for a type of return for a given payer. This record will contain the total number of payees and the totals of the payment amount fields filed by a given payer. The "C" Record must be written after the last "B" Record for each type of return for a given payer. For each "A" Record and group of "B" Records on the file, there must be a corresponding "C" Record.

.03 In developing the "C" Record, for example, if you used Amount Codes 1, 3, and 6 in the "A" Record, the totals from the "B" Records will appear in Control Totals 1, 2, and 3 of the "C" Record. Positions 54–128 would be zero filled in this example.

.04 Payers/Transmitters must verify the accuracy of the totals in the "C" Record and must enter the totals on the transmittal Form 4804, 4802 or computer generated substitute, which will accompany the shipment. The lines used on Forms 4804 and 4802 to record payment amounts correspond with the Amount Codes used in the "A" Record. These forms have been updated for 1986.

.05 The End of Payer "C" Record must be followed by a State Totals "K" Record (if any), or new Payer/Transmitter "A" Record for the next Payer (if any), or an End of Transmission "F" Record.

RECORD NAME: END OF PAYER "C" RECORD

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Enter "1". Must be the first character of each EN OF PAYER RECORD.
2	Record Type	1	REQUIRED. Enter "C".
3–8	Number of Payees	6	REQUIRED. Enter the total number of Payee "B" Records co ered by the preceding Payer/Transmitter "A" Record. Right-justi and zero fill.
9–23	Control Total 1	15	REQUIRED. Please note that all Control Total fields have be expanded from 12 to 15 positions. Enter accumulated totals fro Payment Amount 1. Right-justify and zero fill. IF LESS THA NINE AMOUNT FIELDS ARE BEING REPORTED, ZER FILL UNUSED CONTROL TOTAL FIELDS.

If any corresponding Payment Amount Fields are present in the Payee "B" Records, accumulate into t appropriate Control Total field. ZERO FILL UNUSED CONTROL TOTAL FIELDS. Please note that Control Total fields have been expanded from 12 to 15 positions.

24–38	Control Total 2	15
39–53	Control Total 3	15
54–68	Control Total 4	15
69–83	Control Total 5	15
84–98	Control Total 6	15
99–113	Control Total 7	15
114–128	Control Total 8	15

Sector 2 is only applicable in the End of Payer "C" Record if you use more than eight payment amount fields.

SECTOR 2			
1	Record Sequence	1	REQUIRED. Enter "2".
2	Record Type	1	REQUIRED. Enter "C".
3–17	Control Total 9	15	REQUIRED. Enter accumulated totals from Payment Amoun Right-justify and zero fill.
18–128	Blank	111	REQUIRED. Enter blanks.

SEC. 15. END OF PAYER "C" RECORD—RECORD LAYOUT

END OF PAYER "C" RECORD—RECORD LAYOUT

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	NUMBER OF PAYEES	CONTROL TOTAL 1	CONTROL TOTAL 2	CONTROL TOTAL 3	CONTRO TOTAL 4
1	2	3–8	9–23	24–38	39–53	54–68

END OF PAYER "C" RECORD—RECORD LAYOUT—Continued

SECTOR 1 (Continued)

CONTROL TOTAL 5	CONTROL TOTAL 6	CONTROL TOTAL 7	CONTROL TOTAL 8
69–83	84–98	99–113	114–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	CONTROL TOTAL 9	BLANK
1	2	3–17	18–128

SEC. 16. STATE TOTALS "K" RECORD

.01 The Control Total fields have been expanded from 12 to 15 positions. Adjust your programs accordingly.

.02 The State Totals "K" Record is a summary for a given payer and a given state in the Combined Federal/State Filing Program, used ONLY when state reporting approval has been granted.

.03 The "K" Record will contain the total number of payees and the totals of the payment amount fields filed by a given payer for a given state. The "K" Record(s) must be written after the "C" Record for the related "A" Record.

.03 There MUST be a separate "K" Record for *each state* being reported.

.04 Refer to Part A, Sec. 14 for the requirements and conditions that *MUST* be met to file on this program.

RECORD NAME: STATE TOTALS "K" RECORD

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Enter "1". Must be the first character for each STATE TOTALS "K" RECORD.
2	Record Type	1	REQUIRED. Enter "K".
3-8	Number of Payees	6	REQUIRED. Enter the total number of Payee "B" Records being coded for this state. Right-justify and zero fill.
9–23	Control Total 1	15	REQUIRED. Please note that all Control Total fields have been expanded from 12 to 15 positions. Enter accumulated totals from Payment Amount 1. Right-justify and zero fill. IF LESS THAN NINE AMOUNT FIELDS ARE BEING REPORTED, ZERO FILL UNUSED CONTROL TOTAL FIELDS.
	If any corresponding Payment Amount fields are present in the Payee "B" Records, accumulate into the appropriate Control Total field. ZERO FILL UNUSED CONTROL TOTAL FIELDS. Please note that all Control Total fields have been expanded from 12 to 15 positions.		
24–38	Control Total 2	15	
39–53	Control Total 3	15	
54–68	Control Total 4	15	
69–83	Control Total 5	15	
84–98	Control Total 6	15	
99–113	Control Total 7	15	
114–128	Control Total 8	15	
Sector 2 is required in all State Totals "K" Records			
SECTOR 2			
1	Record Sequence	1	REQUIRED. Enter "2".
2	Record Type	1	REQUIRED. Enter "K".

RECORD NAME: STATE TOTALS "K" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
3–17	Control Total 9	15	REQUIRED. Enter accumulated totals from Payment Amount 9. Right-justify and zero fill. Enter zeros if you have less than nin payment amount fields.
18–126	Blank	109	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. Enter the code assigned to the state which is to receive the information. Refer to Part A, Sec. 14.10.

SEC. 17. STATE TOTALS "K" RECORD—RECORD LAYOUT

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	NUMBER OF PAYEES	CONTROL TOTAL 1	CONTROL TOTAL 2	CONTROL TOTAL 3	CONTROL TOTAL 4
1	2	3–8	9–23	24–38	39–53	54–68

CONTROL TOTAL 5	CONTROL TOTAL 6	CONTROL TOTAL 7	CONTROL TOTAL 8
69–83	84–98	99–113	114–128

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	CONTROL TOTAL 9	BLANK	STATE CODE
1	2	3–17	18–126	127–128

SEC. 18. END OF TRANSMISSION "F" RECORD

.01 The "F" Record is a summary of the number of payers and diskettes in the entire file.

.02 This record should be written after the last "C" Record (or "K" Record, when applicable) of the entire file.

END OF TRANSMISSION "F" RECORD

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Type	1	REQUIRED. Enter "F". Must be first character of END TRANSMISSION RECORD.
2–5	Number of "A" Records	4	REQUIRED. You may enter the total number of Payer/Transm "A" Records for this transmission. Right-justify and zero f enter all zeros.
6–8	Number of Diskettes	3	REQUIRED. You may enter the total number of diskettes i transmission. Right-justify and zero fill or enter all zeros.
9–30	Zero	22	REQUIRED. Enter zeros.
31–128	Blank	98	REQUIRED. Enter blanks.

SEC. 19. END OF TRANSMISSION "F" RECORD—RECORD LAYOUT

SECTOR 1

RECORD TYPE	NUMBER OF "A" RECORDS	NUMBER OF DISKETTES	ZERO	BLANK
1	2–5	6–8	9–30	31–128

PART C. DOUBLE DENSITY DISKETTE SPECIFICATIONS

SECTION 1. GENERAL

.01 The specifications contained in this part of the revenue procedure prescribe the required format and contents of the records to be included in a double density diskette file. These specifications must be adhered to unless deviations have been specifically granted by IRS.

.02 To be compatible, a double density diskette file must meet the following specifications in total:

(a) 8 inches in diameter.

(b) Recorded in EBCDIC.

(c) Contains 77 cylinders (A cylinder refers to both of the tracks available to the read/write heads at any of the 77 locations on the double sided, double density diskette.

(1) Cylinder 00 is the index cylinder (the operating system reserves cylinder 00 for the directory information and writes the file name and location in the directory; *data* cannot be written in cylinder 00).

(2) Cylinders 1–74 are the primary data cylinders.

(3) Cylinders 75 and 76 are reserved for alternative cylinder assignment.

(d) Each Track contains 26 sectors; therefore, each cylinder contains 52 sectors.

(e) Each sector must contain 256 bytes.

(f) Data may be recorded on both sides of the diskette.

(g) IRS can process single sided, single density, soft sectored diskettes as well as double sided, double density, soft sectored diskettes. Part B provides specifications for single density diskettes which have sectors of 128 bytes.

(h) An IBM 5360 compatible diskette would meet the above specifications. If using other processers, data should be recorded in the Basic Data Exchange format. Hard sectored diskettes are not compatible.

.03 Refer to Part B, Sec. 1.03 through Sec. 2 for further information concerning diskette requirements which apply to both single and double density diskettes.

SEC. 2 PAYER/TRANSMITTER "A" RECORD

Refer to Part B, Sec. 3.01 through Sec. 3.03 for a description of the Payer/Transmitter "A" Record.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". It is used to sequence the sectors making up a Service Record.
2	Record Type	1	REQUIRED. Enter "A".
3	Payment Year	1	REQUIRED. Must be the right most digit of the year for which information is being reported (*e.g.*, if payments were made in 1986, enter "6"). Must be incremented each year.
4–6	Diskette Sequence Number	3	REQUIRED. Sequence number assigned by the Transmitter to each diskette starting with 001. (Blanks are acceptable or all zeros.)
7–15	Payer's Federal EIN	9	REQUIRED. Must be the *valid* 9-digit number assigned to the payer by IRS. DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS. (Also see Part A, Sec. 11.07.)
16	Blank	1	REQUIRED. Enter blank.
17	Combined Federal/State Filer	1	REQUIRED. Enter the appropriate code from the table below. *Prior approval* is required. A Consent Form 6847 *must* be submitted to IRS before tax information will be released to the states. Refer to Part A, Sec. 14.11 for money criteria. Not all states participate in this program. If the Payer/Transmitter is not participating in the Combined Federal/State Filing Program, enter blanks. (Refer to Part A, Sec. 14 for the requirements that *must* be met *prior* to actual participation in this program.) Forms 1098, 1099–A, 1099–B, and W–2G cannot be filed on this program. Filers who participate in this program must incorporate state totals into corresponding "K" Records as described in Part B, Sec. 16.

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RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			

Code	*Meaning*
1	Participating in the Combined Federal/State Fil Program
blank	Not participating

Diskette Position	Field Title	Length	Description and Remarks
18	Type of Return	1	REQUIRED. Enter appropriate code from table below:

Type of Return	*Cod*
1098	3
1099–A	4
1099–B	B
1099–DIV	1
1099–G	F
1099–INT	6
1099–MISC	A
1099–OID	D
1099–PATR	7
1099–R	9
5498	L
W–2G	W

Diskette Position	Field Title	Length	Description and Remarks
19–27	Amount Indicators	9	REQUIRED. *In most cases, the boxes or Amount Indicators o paper information returns correspond with the Amount Codes use to file on magnetic media; however, should you notice discrepancie between this revenue procedure and paper forms, please disregar them and program according to this revenue procedure for you returns filed on magnetic media.* For specific instructions on infor mation to be reported in each Amount Code, refer to the 19 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G." Th amount indicators entered for a given type of return indicate type(of payment(s) which were made. For each Amount Code entere in this field, a corresponding payment amount must appear in th Payee "B" Record. Example: If position 18 of the Payer/Transmitte "A" Record is "6" (for 1099–INT) and positions 19–27 ar "123bbbbbb," this indicates that 3 payment amount fields are pre ent in all of the following Payee "B" Records. The first paymen amount field in the Payee "B" Record will represent Earnings fro savings and loan associations, credit unions, bank deposits, beare certificates of deposit, etc., the second will represent Amount o forfeiture, and the third will represent Federal income tax withheld Enter the Amount Indicators in ASCENDING SEQUENCE (*i.e.* 1247bbbbb), left-justify, filling unused positions with blanks. F any further clarification of the Amount Indicator codes, you m contact the IRS National Computer Center.
	Amount Indicators Form 1098–Mortgage Interest Statement		For Reporting Mortgage Interest Received from Payer(s) on For 1098:

Amount Code	Amount Type
1	Mortgage interest received from payer(s)
2	Optional field for items such as real estate taxes o insurance paid from escrow

NOTE: THE PERSON FOR WHOM YOU ARE RECEIVING THE INTEREST NEED NOT FILE FOR 1098, AND NO ADDITIONAL REPORTING IS REQUIRED FOR THE TRANSFER OF INTERES FROM THE SERVICING BANK TO THE LENDER.

pages tightly bound

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
	Amount Indicators Form 1099–A–Acquisition or Abandonment of Secured Property		For Reporting the Acquisition or Abandonment of Secured Property on Form 1099–A: Amount Code / Amount Type 2 Amount of debt outstanding 3 Amount of debt satisfied 4 Fair market value of property at acquisition or abandonment
	Amount Indicators Form 1099–B–Proceeds From Broker and Barter Exchange Transactions		For Reporting Payments on Form 1099–B: Amount Code / Amount Type 2 Stocks, bonds, etc. (For Forward Contracts see NOTE below.) 3 Bartering 4 Federal income tax withheld 6 Profit or loss realized in 1986 7 Unrealized profit (or loss) on open contracts—12/31/85 8 Unrealized profit (or loss) on open contracts—12/31/86 9 Aggregate profit (or loss)

NOTE: The Payment Amount field associated with Amount Code 2 may be used to represent a loss when the reporting is for Forward Contracts. Refer to Payee "B" Record-General Field Descriptions, Payment Amount Fields, for instructions in reporting negative amounts.

Diskette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–DIV–Dividends and Distributions		For Reporting Payments on Form 1099–DIV: Amount Code / Amount Type 1 Gross dividends and other distributions on stock 2 Dividends qualifying for exclusion 3 Dividends not qualifying for exclusion 4 Federal income tax withheld 5 Capital gain distributions 6 Nontaxable distributions (if determinable) 7 Foreign tax paid 8 Cash liquidation distributions 9 Noncash liquidation distributions (Show fair market value)
	Amount Indicators Form 1099–G–Certain Government Payments		For Reporting Payments on Form 1099–G: Amount Code / Amount Type 1 Unemployment compensation 2 State or local income tax refunds 4 Federal income tax withheld 5 Discharge of indebtedness 6 Taxable grants 7 Agriculture payments
	Amount Indicators Form 1099–INT–Interest Income		For Reporting Payments on Form 1099–INT: Amount Code / Amount Type 1 Earnings from savings and loan associations, credit unions, bank deposits, bearer certificate of deposit, etc.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			

2	Amount of forfeiture
3	Federal income tax withheld
4	Foreign tax paid (if eligible for foreign tax credit)
5	U.S. Savings Bonds, etc.

Amount Indicators Form 1099–MISC– Miscellaneous Income (See Notes 1, 2 and 3)

For Reporting Payments on Form 1099–MISC:

Amount Code	Amount Type
1	Rents
2	Royalties
3	Prizes and awards
4	Federal income tax withheld
5	Fishing boat proceeds
6	Medical and health care payments
7	Nonemployee compensation
8	Direct sales "*indicator*" (see NOTE 1)
9	Substitute payments in lieu of dividends or interes (see NOTE 2)

NOTE 1: Use Amount Code "8" to report that *direct sales* of consumer products of $5,000 or more to th payee on a buy-sell, deposit-commission, or other basis *for resale* were made. Do not use this indicator for sal of less than $5,000. The use of Amount Code "8" actually reflects an *indicator* of *direct sales* and not an actu payment amount or amount code. The corresponding payment amount field in the Payee "B" Record MUST be reflected as 0000000100. This does not mean that a payment of $1.00 was made or is being reported. Th use of Amount Code "8" relates directly to diskette position "5," Document Specific Code and NOTE 2 the Payment Amount Field in the Payee "B" Record. (If you use Amount Code "8" in the "A" Record, yo will enter a "1" in diskette position "5" of the "B" Record. For any other 1099–MISC Amount Codes, yo will enter a "0" (zero) in diskette position "5" of the "B" Record.)

NOTE 2: Brokers are subject to a reporting requirement for payments received after 1984. Brokers who transf securities of a customer for use in a short sale must use Amount Code 9 to report the aggregate paymen received in lieu of dividends or tax-exempt interest on behalf of a customer while the short sale was ope Generally, for substitute payments in lieu of dividends, a broker is required to file a Form 1099–MISC for ea affected customer who is *not* an individual. Refer to the 1986 "Instructions for Form 1099, 1098, 5498, 10 and W–2G" for detailed information. (The instructions are available from IRS offices.)

NOTE 3: If you are reporting Excess Golden Parachute Payments, use paper Forms 1099–MISC. Do not repo these payments to magnetic media. See Part A, Sec. 15 for a definition of an Excess Golden Parachute Paymen

Amount Indicators Form 1099–OID– Original Issue Discount

For Reporting Payments on Form 1099–OID:

Amount Code	Amount Type
1	Total original issue discount for 1986
2	Other periodic interest (the regular interest paid o this obligation without regard to any original iss discount)
3	Amount of forfeiture
4	Federal income tax withheld

Amount Indicators Form 1099–PATR– Taxable Distributions Received From Cooperatives

For Reporting Payments on Form 1099–PATR:

Amount Code	Amount Type
1	Patronage dividends
2	Non patronage distributions
3	Per-unit retain allocations
4	Federal income tax withheld
5	Redemption of nonqualified notices and retain allocations

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

iskette osition	Field Title	Length	Description and Remarks

ECTOR 1 (Continued)

6	Investment credit (See NOTE)
7	Energy investment credit (See NOTE)
8	Jobs credit (See NOTE)

NOTE: The amounts shown for Amount Indicators "6," "7" and "8" must be reported to the payee; however, since these amounts are not taxable, they need not be reported to IRS.

Amount Indicators
Form 1099–R–
Total Distributions
from Profit-Sharing,
Retirement Plans,
Individual Retirement
Arrangements,
Insurance Contracts, Etc.
(See NOTE)

For Reporting Payments on Form 1099–R:

Amount Code	Amount Type
1	Amount includable as income (add amounts in codes 2 and 3)
2	Capital gain (for lump-sum distributions only)
3	Ordinary income
4	Federal income tax withheld
5	Employee contributions (profit-sharing or retirement plans) or insurance premiums
6	IRA, SEP or DEC distributions
7	State income tax withheld
8	Net unrealized appreciation in employer's securities
9	Other

NOTE: A distribution from a KEOGH plan should be reported in Amount Codes 1, 2, and 3 as appropriate.

Amount Indicators
Form 5498–
Individual Retirement
Arrangement
Information

For Reporting Payments on Form 5498:

Amount Code	Amount Type
1	Regular SEP contributions made in 1986 and 1987 for 1986. Include only employer contributions here. Enter any employee contributions to a SEP in Code 3.
2	Rollover IRA, SEP or DEC contributions
3	Regular IRA or DEC contributions made in 1986 and 1987 for 1986
4	Life insurance cost included in code 1 or 3 (for endowment contracts only)

NOTE: Form 5498 is filed for contributions to be applied to 1986 that are made between January 1, 1986, and April 15, 1987.

Amount Indicators
Form W–2G–
Certain Gambling
Winnings

For Reporting Payments on Form W–2G:

Amount Code	Amount Type
1	Gross winnings
2	Federal income tax withheld
3	State income tax withheld
7	Winnings from identical wagers

8	Blank	1	REQUIRED. Enter blank.
9–31	"A" Record Length	3	REQUIRED. This indicates the Record Length, *NOT* the Sector Length. Enter 360.
2–34	"B" Record Length	3	REQUIRED. This indicates the Record Length, *NOT* the Sector Length. Enter 360.
5	Blank	1	REQUIRED. Enter blank.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
36–40	Transmitter Control Code (TCC)	5	REQUIRED. Enter the five character alpha/numeric Transmitter Control Code assigned by IRS. See Part A, Sec. 15 for a definition of Transmitter Control Code (TCC). You must have a TCC to file *actual* data on this program.
41	Blank	1	REQUIRED. Enter blank.
42–81	First Payer Name	40	REQUIRED. Must be present or files will be returned for correction. Enter the name of the payer in the manner in which it is used in normal business. Any extraneous information must be deleted from the name line. Left-justify and fill with blanks. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
82–120	Second Payer Name	39	REQUIRED. The contents of this field are dependent upon the TRANSFER AGENT INDICATOR in position 121 of this record. If the Transfer Agent Indicator contains a "1", this field will contain the name of the Transfer Agent. If the Transfer Agent Indicator contains a "0" (zero), this field will contain either a continuation of the First Payer Name field or blanks. Left-justify and fill unused positions with blanks. IF NO ENTRIES ARE PRESENT FOR THIS FIELD, FILL WITH BLANKS. (See Part A, Sec. 15 for a definition of Transfer Agent.)
121	Transfer Agent Indicator	1	REQUIRED. Identifies the entity in the Second Payer Name field. (See Part A, Sec. 15 for a definition of Transfer Agent.) *Code* — *Meaning* 1 — The entity in the Second Payer Name field is th Transfer Agent. 0 (zero) — The entity shown is *not* the Transfer Agent (*i.e.*, th Second Payer Name field contains either a continu tion of the First Payer Name field or blanks.).
122–161	Payer Shipping Address	40	REQUIRED. If the TRANSFER AGENT INDICATOR in position 121 is a "1", enter the shipping address of the Transfer Agent. Otherwise, enter the shipping address of the payer. Left-justify and fill with blanks.
162–201	Payer City, State and ZIP Code	40	REQUIRED. If the TRANSFER AGENT INDICATOR in position 121 is a "1", enter the City, State and ZIP Code of the Transfer Agent. Otherwise, enter the City, State and ZIP Code of the payer. Left-justify and fill with blanks.
202–256	Blank	55	REQUIRED. Enter blanks.

ADDITIONALLY, IF THE PAYER AND THE TRANSMITTER ARE THE SAME, THE "A"' RECORD MAY BE TERMINATED AS DESCRIBED ABOVE. HOWEVER, IF THE PAYER AND THE TRANSMITTER ARE NOT THE SAME OR THE TRANSMITTER INCLUDES FILES FOR MORE THAN ONE PAYER OR THIS IS A COMBINED FEDERAL/STATE FILING PAYER, THE FOLLOWING ITEMS ARE REQUIRED.

Diskette Position	Field Title	Length	Description and Remarks
202–241	First Name Line of Transmitter	40	REQUIRED. Enter the name of the transmitter in the manner i which it is used in normal business. The name of the transmitter *must* be constant through the entire file. Left-justify and fill wit blanks.
242–256	Blank	15	REQUIRED. Enter blanks.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

iskette osition	Field Title	Length	Description and Remarks
ECTOR 2	(Only used if you are transmitting for someone other than yourself or if you participate in the Combined Federal/ State Program.)		
	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service Record.
	Record Type	1	REQUIRED. Enter "A". Must be the second position of each PAYER/TRANSMITTER Record.
-42	Second Name Line of Transmitter	40	REQUIRED. Enter the second name line of the transmitter. Left-justify and fill with blanks. IF NO ENTRIES ARE PRESENT FOR THIS FIELD, FILL WITH BLANKS.
3-82	Transmitter Mailing Address	40	REQUIRED. Enter the mailing address of the transmitter. Left-justify and fill with blanks.
3-122	Transmitter City, State and ZIP Code	40	REQUIRED. Enter the City, State, and ZIP Code of the transmitter. Left-justify and fill with blanks.
23-256	Blank	134	REQUIRED. Enter blanks.

EC. 3. PAYER/TRANSMITTER "A" RECORD—RECORD LAYOUT

PAYER/TRANSMITTER "A" RECORD—RECORD LAYOUT

ECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DISKETTE SEQUENCE NUMBER	PAYER'S FEDERAL EIN	BLANK	COMBINED FEDERAL/STATE FILER	TYPE OF RETURN
1	2	3	4–6	7–15	16	17	18

ECTOR 1 (Continued)

AMOUNT INDICATORS	BLANK	"A" RECORD LENGTH	"B" RECORD LENGTH	BLANK	TRANSMITTER CONTROL CODE	BLANK
19–27	28	29–31	32–34	35	36–40	41

ECTOR 1 (Continued)

FIRST PAYER NAME	SECOND PAYER NAME	TRANSFER AGENT INDICATOR	PAYER SHIPPING ADDRESS	PAYER CITY, STATE AND ZIP CODE	BLANK
42–81	82–120	121	122–161	162–201	202–256

IF THE PAYER AND THE TRANSMITTER ARE THE SAME, THE "A" RECORD MAY BE TERMINATED WITH ECTOR 1 AS ILLUSTRATED ABOVE. HOWEVER, IF THE PAYER AND THE TRANSMITTER ARE NOT THE AME, OR THE TRANSMITTER INCLUDES FILES FOR MORE THAN ONE PAYER OR THIS IS A COMBINED EDERAL/STATE PAYER, THE FOLLOWING ITEMS ARE REQUIRED.

ECTOR 1 (continued)

FIRST NAME LINE OF TRANSMITTER	BLANK
202–241	242–256

SECTOR 2 (Only used if you are transmitting for someone other than yourself or if you participate in the Combined Federal/State Program.)

RECORD SEQUENCE	RECORD TYPE	SECOND NAME LINE OF TRANSMITTER	TRANSMITTER MAILING ADDRESS	TRANSMITTER CITY, STATE AND ZIP CODE	BLANK
1	2	3–42	43–82	83–122	123–256

SEC. 4. PAYEE "B" RECORDS—GENERAL INFORMATION AND FIELD DESCRIPTIONS FOR FORMS 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R, and 5498.

Refer to Part B, Sec. 5.01 through Sec. 5.08 for a description of the Payee "B" Record. This section contains the general payment information from the individual statements for Forms 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R, and 5498.

RECORD NAME: PAYEE "B" RECORD

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". It is used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–4	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported (*e.g.*, if payments were made in 1986, enter "86"). Must be incremented each year.
5–6	Document Specific Code	2	REQUIRED for Forms 1099–R, 1099–MISC, and 1099–G. For *Form 1099–R,* enter the appropriate code for the Category of Total Distribution. For *Form 1099–MISC,* enter the appropriate code for Direct Sales. For *Form 1099–G,* enter the year of income tax refund. FOR ALL OTHER FORMS, ENTER BLANK. If only one code is used, left-justify and blank fill.

(In prior years, diskette position 6 was used as a corrected return indicator. This position was needed for the Document Specific Code. Diskette position 7 now represents a corrected return. You must adjust your programs.)

	Field Title		Description and Remarks
	Category of Total Distribution (Form 1099–R only)		Use only for reporting on *Form 1099–R* to identify the category of Total Distribution. You may select two codes except when using Code 9. Enter the applicable code from the table below. Code below is *not required* for Amount Indicators 1, 2, and 3. A "0" (zero) is not a valid code for Form 1099–R. If you are reporting distribution from a KEOGH plan, or from any other distribution to which the following codes do not apply, enter blanks in this field.

Category	*Code*
Premature distribution (other than codes 2, 3, 4, 5, 8 or P)	1
Rollover	2
Disability	3
Death (includes payments to a beneficiary)	4

RECORD NAME: PAYEE "B" RECORD—Continued

iskette osition	Field Title	Length	Description and Remarks
ECTOR 1 (Continued)			
			Prohibited transaction 5 Other 6 Normal IRA, SEP or DEC distributions 7 Excess contributions refunded plus earnings on such excess contributions 8 PS 58 Costs (see NOTE) 9 Excess contributions refunded plus earnings on such excess contributions taxable in 1985 P Qualified for 10-year averaging A Qualifies for death benefit exclusion B Qualifies for *both* A and B C NOTE: PS 58 Costs may be reported on Form 1099–R; however, Form W–2P (filed with SSA) is preferable. Since this is not actually a total distribution, a separate "B" Record is required to report PS 58 Costs. These costs may not be reported in combination with the total distribution. Refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" available from IRS offices.
	Direct Sales (Form 1099–MISC only)		Use only for direct sales reporting on *Form 1099–MISC*. If sales to the recipient of consumer products on a buy-sell, deposit-commission, or any other basis for resale, have amounted to $5,000 or more, ENTER "1". If you are filing 1099–MISC, with an Amount Indicator of "8" in the "A" Record, you must enter a code "1" in this field. For all other 1099–MISC Amount Codes in the "A" Records, enter a "0" (zero) in this field. In Part B, Sec. 3, information concerning the direct sales indicator can be found under Amount Indicators, Form 1099–MISC, NOTE 1 in the "A" Record. This code will appear in position 5. Position 6 will be blank.
	Refund is for Tax Year (Form 1099–G only)		Use only for reporting the tax year for which the refund was issued. If the payment amount field associated with Amount Indicator 2, Income Tax Refunds, contains a refund, credit or offset that is attributable to an income tax which applies exclusively to income from a trade or business and is not of general application, then enter the ALPHA equivalent of the year of refund from the table below. Otherwise, enter the NUMERIC Year for which the Refund was issued. This code should appear in position 5. Position 6 will be blank. *Year for which Refund was Issued* — *Alpha Equivalent* 1 — A 2 — B 3 — C 4 — D 5 — E 6 — F 7 — G 8 — H 9 — I 0 — J
	Blank or Corrected Return Indicator	1	REQUIRED. Enter blank. (Reserved for IRS use). Diskette position 7 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using either magnetic media or paper forms. IN PRIOR YEARS, DISK-

RECORD NAME: PAYEE "B" RECORD—Continued

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td>SECTOR 1 (Continued)</td><td></td><td></td><td></td></tr>
<tr><td></td><td></td><td></td><td>ETTE POSITION 6 WAS USED AS THE CORRECTED RE- TURN INDICATOR. THIS HAS NOW CHANGED TO POSITION 7. <i>YOU MUST ADJUST YOUR PROGRAMS.</i></td></tr>
<tr><td>8–11</td><td>Name Control</td><td>4</td><td>REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (—) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the name control:
<table>
<tr><th><i>Name</i></th><th><i>Name Control</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE*</td></tr>
<tr><td>James P. En Sr.</td><td>EN*</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must be left-justified and blank filled.</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Ident fication Number (TIN) in positions 13–21 as either an Employ Identification Number, a Social Security Number, or the reason number is shown. Enter the appropriate code from the followi table:
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, ente blank. If the number is unobtainable due legitimate cause: <i>e.g.</i>, number applied for not received, enter a blank.</td></tr>
</table></td></tr>
<tr><td>13–21</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Nu ber of the payee (SSN or EIN, as appropriate). Where an ide fication number has been applied for but not received or wh there is any other legitimate cause for not having an identificat number, <i>enter blanks</i>. Refer to Part A, Sec. 11. <i>DO NOT ENTER HYPHENS, ALPHA CHARACTERS, AL OR ALL ZEROS.</i> Any record containing an invalid identifica number in this field will be returned for correction.</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
22-31	**Payer's Account Number for Payee**	10	REQUIRED. Payer may use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payer's file should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. An account number can be any account number assigned by the payer to the payee (*i.e.*, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any number that will help identify the particular transaction that you are reporting. If a number is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.
	Payment Amount Fields (must be numeric)		The number of payment amounts is dependent upon and must agree with the number of Amount Indicators present in positions 19–27 of Sector 1 of the "A" Record. *THE FIRST PAYEE NAME LINE MUST APPEAR IMMEDIATELY AFTER THE LAST PAYMENT AMOUNT INDICATED AS BEING USED.* For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one ten position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE 1). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS* (except those items that reflect a loss on Form 1099–B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "123bbbbbb", the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb", the "B" Records must have only 5 payment amount fields. Payment amounts MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE 1: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee. NOTE 2: If you file 1099-MISC and use Amount Code "8" in the Amount Indicator field of the Payer/Transmitter "A" Record, you must enter 0000000100 in the corresponding Payment Amount Field. This will not represent an actual money amount; this is an indicator of direct sales. (Refer to Part B, Sec. 3, NOTE 1, of the amount Indicators, Form 1099–MISC, for clarification.)
-41	**Payment Amount 1**	10	This amount is identified by the indicator in position 19 of Sector 1 of the Payer/Transmitter "A" Record. *This amount must always be present.*

RECORD NAME: PAYEE "B" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (continued)			

DETEMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF SECTOR 1 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–256 OF SECTOR 1 AND POSITION 1–256 OF SECTOR 2, IF NEEDED, OF THE PAYEE "B" RECORD. USE THE APPROPRIATE FORMAT AS REQUIRED. SECTOR 2 IS ONLY APPLICABLE IN THE PAYEE "B" RECORD IF YOU SEE SEVEN OR MORE PAYMENT AMOUNT FIELDS.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)

SECTOR 1 (Continued)			
42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediatel after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (pref- erably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avail- able in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
122–161	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fi unused positions with blanks. The address MUST be present. Th field MUST NOT contain any data other than the payee's mailin address.
162–190	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused p sitions with blanks. *Do not enter state and ZIP Code information this field.* (If the payee lives outside of the United States, insert "1" in position "162" of this field and spell out the name of the ci in the remaining positions.)
191–192	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign co try. You *MUST* use valid U.S. Postal Service abbreviations as sho in Part A, Sec. 16. Use this field for state or country informati *only*. If the code used is for a foreign country, insert a "1" in positi "162" of the Payee City field.
193–201	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U Postal Service. If only the first 5 digits are known, left-justify *fill the unused positions with blanks.* Use this field for the ZIP C

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			only. For foreign countries, alpha characters are acceptable as long as position "162" in the Payee City field is a "1".
202–254	Blank	53	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
92–131	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
132–171	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
172–200	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "172" of this field and spell out the name of the city in the remaining positions.)
01–202	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "172" of the Payee City field.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
203–211	Payee Zip Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code only. For foreign countries, alpha characters are acceptable as long as position "172" in the Payee City field is a "1".
212–254	Blank	43	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)

SECTOR 1 (Continued)

42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediatel after the last payment amount indicated as being used. Do not ente address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appear in positions 13–21 above. If fewer than 40 characters are required left-justify and fill unused positions with blanks. If more space i required *for the name*, utilize the Second Payee Name Line fiel below. If there are multiple payees, *only the name* of the paye whose taxpayer identification number has been provided can b entered in this field. The names of the other payees may be entere in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT, THE "A" RECORD WILL REFLECT THE NAME OF TH RECIPIENT OF THE INTEREST. THE "B" RECORD WIL REFLECT THE INDIVIDUAL PAYING THE INTEREST AN THE AMOUNT PAID.*
102–141	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avai able in the First Payee Name Line, *enter the remaining portion the name only in this field*. If there are multiple payees (*e.g.*, partne or joint owners), this field may be used for those payees' *nam* who are not associated with the taxpayer identification number positions 13–21 above. *Do not enter address information in this fiel* Left-justify and fill unused positions with blanks. FILL WIT BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIEL
142–181	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and unused positions with blanks. The address MUST be present. T field MUST NOT contain any data other than the payee's maili address.
182–210	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused sitions with blanks. *Do not enter state and ZIP Code information this field*. (If the payee lives outside of the United States, inser

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			"1" in position "182" of this field and spell out the name of the city in the remaining positions.)
211–212	Payee State	2	REQUIRED. Enter the abbreviations for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "182" of the Payee City field.
213–221	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "182" in the Payee City field is a "1".
222–254	Blank	33	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–111	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
112–151	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.*

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
152–191	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
192–220	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "192" of this field and spell out the name of the city in the remaining positions.)
221–222	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbrevations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "192" of the Payee City field.
223–231	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "192" in the Payee City field is a "1".
232–254	Blank	23	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–121	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM*

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.
122–161	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
162–201	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
202–230	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "202" of this field and spell out the name of the city in the remaining positions.)
231–232	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "202" of the Payee City field.
233–241	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "202" in the Payee City field is a "1".
242–254	Blank	13	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If the payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
152–191	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
192–220	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "192" of this field and spell out the name of the city in the remaining positions.)
221–222	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbrevations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "192" of the Payee City field.
223–231	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "192" in the Payee City field is a "1".
232–254	Blank	23	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–121	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM*

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.
122–161	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
162–201	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
202–230	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "202" of this field and spell out the name of the city in the remaining positions.)
231–232	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "202" of the Payee City field.
233–241	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "202" in the Payee City field is a "1".
242–254	Blank	13	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If the payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–131	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
132–171	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
172–211	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
212–240	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "212" of this field and spell out the name of the city in the remaining positions.)
241–242	Payee State	2	REQUIRED. Enter the abbreviations for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "212" of the Payee City field.
243–251	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "212" in the Payee City field is a "1".
252–254	Blank	3	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–101	Payment Amount 7	10	This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.
102–141	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
142–181	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
182–221	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
222–250	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "222" of this field and spell out the name of the city in the remaining positions.)
251–252	Payee State	2	REQUIRED. Enter the abbreviations for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "222" of the Payee City field.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
253–256	Blank	4	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–11	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "222" in the Payee City field is a "1".
12–254	Blank	243	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING EIGHT PAYMENT FIELDS)

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–101	Payment Amount 7	10	This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.
102–111	Payment Amount 8	10	This amount is identified by the amount indicator in position 26, Sector 1, of the Payer/Transmitter "A" Record.
112–151	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediatel after the last payment amount indicated as being used. Do not ente address information in this field.* Enter the name of the payee (pref erably surname first) whose taxpayer identification number appear in positions 13–21 above. If fewer than 40 characters are required left-justify and fill unused positions with blanks. If more space i required *for the name,* utilize the Second Payee Name Line fiel below. If there are multiple payees, *only the name* of the paye whose taxpayer identification number has been provided can b entered in this field. The names of the other payees may be entere in the Second Payee Name Line field. *NOTE: WHEN REPOR ING FORM 1098, "MORTGAGE INTEREST STATEMENT, THE "A" RECORD WILL REFLECT THE NAME OF TH*

RECORD NAME: PAYEE "B" RECORD (USING EIGHT PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.
152–191	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
192–231	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
232–256	Blank	25	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
34–42	Payee ZIP CODE	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".
43–254	Blank	212	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

RECORD NAME: PAYEE "B" RECORD (USING NINE PAYMENT FIELDS)

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE "B" RECORD (USING NINE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–101	Payment Amount 7	10	This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.
102–111	Payment Amount 8	10	This amount is identified by the amount indicator in position 26, Sector 1, of the Payer/Transmitter "A" Record.
112–121	Payment Amount 9	10	This amount is identified by the amount indicator in position 27, Sector 1, of the Payer/Transmitter "A" Record.
122–161	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
162–201	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
202–241	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
242–256	Blank	15	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING NINE PAYMENT FIELDS)—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
3-31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32-33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
34-42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".
43-254	Blank	212	REQUIRED. Enter blanks.
255-256	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.

SEC. 5. PAYEE "B" RECORD—RECORD LAYOUTS FOR FORMS 1098, 1099-DIV, 1099-G, 1099-INT, 1099-MISC, 1099-OID, 1099-PATR, 1099-R AND 5498

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3-4	5-6	7	8-11	12	13-21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE
22-31	32-41	42-81	82-121

SECTOR 1 (Continued)

PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
122-161	162-190	191-192	193-201	202-254	255-256

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS
22–31	32–41	42–51	52–91	92–131	132–171

SECTOR 1 (Continued)

PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
172–200	201–202	203–211	212–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–101	102–141

SECTOR 1 (Continued)

PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
142–181	182–210	211–212	213–221	222–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	FIRST PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–71	72–111

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)—Continued

SECTOR 1 (Continued)

SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
112–151	152–191	192–220	221–222	223–231

SECTOR 1 (Continued)

BLANK	STATE CODE
232–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING FIVE PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	FIRST PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–71	72–81	82–121

SECTOR 1 (Continued)

SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
122–161	162–201	202–230	231–232	233–241	242–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

PAYEE "B" RECORD—RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)—Continued

SECTOR 1 (Continued)

FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS
92–131	132–171	172–211

SECTOR 1 (Continued)

PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
212–240	241–242	243–251	252–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING SEVEN PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7
92–101

SECTOR 1 (Continued)

FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS
102–141	142–181	182–221

SECTOR 1 (Continued)

PAYEE CITY	PAYEE STATE	BLANK
222–250	251–252	253–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–11	12–254	255–256

PAYEE “B” RECORD—RECORD LAYOUT (USING EIGHT PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER’S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8
92–101	102–111

SECTOR 1 (Continued)

FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
112–151	152–191	192–231	232–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–31	32–33	34–42	43–254	255–256

PAYEE “B” RECORD—RECORD LAYOUT (USING NINE PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER’S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8	PAYMENT AMOUNT 9
92–101	102–111	112–121

PAYEE "B" RECORD—RECORD LAYOUT (USING NINE PAYMENT AMOUNT FIELDS)—Continued

SECTOR 1 (Continued)

FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
122–161	162–201	202–241	242–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE
1	2	3–31	32–33	34–42	43–254	255–256

SEC. 6. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM 1099–A

.01 This section contains the general payment information from individual statements for Form 1099–A. For detailed explanations of the 1099–A fields request a copy of the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" available from IRS offices.

.02 FORM 1099–A CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.

RECORD NAME: PAYEE "B" RECORD
FORM 1099–A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–4	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported (*e.g.*, if payments were made in 1986, enter "86"). Must be incremented each year.
5–6	Document Specific Code	2	REQUIRED. For Form 1099–A, enter blanks.
7	Blank or Corrected Return Indicator	1	REQUIRED. Enter blank. (Reserved for IRS use). Diskette position 7 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using either magnetic media or paper forms. IN PRIOR YEARS, DISKETTE POSITION 6 WAS USED AS THE CORRECTED RETURN INDICATOR. THIS HAS NOW CHANGED TO POSITION 7. *YOU MUST ADJUST YOUR PROGRAMS.*
8–11	Name Control	4	REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (-) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the Name Control:

Name	*Name Control*
John Brown	BROW
John A. Lee	LEE *
James P. En Sr.	EN *

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099-A

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td></td><td></td><td></td><td>
<table>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must be left-justified and blank filled.</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identification Number (TIN) in positions 13–21 as either an Employer Identification Number, a Social Security Number, or the reason no number is shown. Enter the appropriate code from the following table:
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, enter a blank. If the number is unobtainable due to legitimate cause; <i>e.g.</i>, number applied for but not received, enter a blank.</td></tr>
</table></td></tr>
<tr><td>13–21</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the payee (SSN or EIN, as appropriate). Where an identification number has been applied for but not received or where there is any other legitimate cause for not having an identification number, <i>enter blanks</i>. Refer to Part A, Sec. 11.

<i>DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS.</i> Any record containing an invalid identification number in this field will be returned for correction.</td></tr>
<tr><td>22–31</td><td>Payer's Account Number for Payee</td><td>10</td><td>REQUIRED. Payer may use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payer's file should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. Enter blanks if the Payer's Account Number for Payee is not to be entered in this field. An account number can be entered in this field. An account number can be any account number assigned by the payer to the payee (<i>i.e.</i>, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any number that will help identify the particular transaction that you are reporting. If a number is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099–A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
	Payment Amount Fields (must be numeric)		The number of payment amounts is dependent upon and must agree with the number of Amount Indicators present in positions 19–27 of Sector 1 of the "A" Record. The First Payee Name Line *must* appear immediately after the last payment amount indicated as being used. For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one ten position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE 1). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS* (except those items that reflect a loss on Form 1099–B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "123bbbbbb", the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb", the "B" Records must have only 5 payment amount fields. Payment amounts MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE 1: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)
FORM 1099–A

SECTOR 1 (Continued)			
32–41	Payment Amount 1	10	This amount is identified by the indicator in position 19 of Sector 1 of the Payer/Transmitter "A" Record. *This amount must always be present.*

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF SECTOR 1 OF THE PAYER/TANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–256 OF SECTOR 1 AND POSITIONS 1–256 OF SECTOR 2, IF NEEDED, OF THE PAYEE "B" RECORD. *FOR FORM 1099–A SECTOR 2 WILL BE REQUIRED IF THERE IS MORE THAN ONE PAYMENT FIELD TO BE REPORTED IN THE PAYEE "B" RECORD.* USE THE APPROPRIATE FORMAT AS REQUIRED.

42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued
FORM 1099–A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payee's *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
122–161	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
162–190	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "162" of this field and spell out the name of the city in the remaining positions.)
191–192	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "162" of the Payee City field.
193–201	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "162" in the Payee City field is a "1".
202–210	Blank	9	REQUIRED. Enter blanks.
211–216	Lender's Date of Acquisition or Abandonment	6	REQUIRED *FOR FORM 1099–A ONLY. Enter the date of your acquisition of the secured property or the date you first knew or had reason to know that the property was abandoned in the format MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.*
217	Liability Indicator	1	REQUIRED *FOR FORM 1099–A ONLY.* Enter the appropriate indicator from table below: *Indicator* — *Usage* 1 — Borrower is personally liable for repayment of the debt. Blank — Borrower is *not* liable for repayment of the debt.
218–254	Description	37	REQUIRED *FOR FORM 1099–A ONLY.* Enter a brief description of the property. For example, for real property, enter the address, section, lot and block. For personal property, enter the type, make and model (*e.g.*, Car-1986 Buick Regal or Office Equipment, etc.).
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued

FORM 1099-A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, only the name of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
92–131	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
132–171	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
172–200	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "172" of this field and spell out the name of the city in the remaining positions.)
201–202	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "172" of the Payee City field.
203–211	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "172" in the Payee City field is a "1".
212–256	Blank	45	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–210	Blank	208	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued
FORM 1099–A

iskette osition	Field Title	Length	Description and Remarks
ECTOR 2 (Continued)			
11–216	Lender's Date of Acquisition or Abandonment	6	REQUIRED *FOR FORM 1099–A ONLY*. Enter the date of your acquisition of the secured property or the date you first knew or had reason to know that the property was abandoned in the format MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.
17	Liability Indicator	1	REQUIRED *FOR FORM 1099–A ONLY*. Enter the appropriate indicator from table below: *Indicator* — *Usage* 1 — Borrower is personally liable for repayment of the debt. Blank — Borrower is *not* liable for repayment of the debt.
218–254	Description	37	REQUIRED *FOR FORM 1099–A ONLY*. Enter a brief description of the property. For example, for real property, enter the address, section, lot and block. For personal property, enter the type, make and model (*e.g.*, Car—1986 Buick Regal or Office Equipment, etc.)
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)
FORM 1099–A

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
102–141	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
142–181	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

FORM 1099–A

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
182–210	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "182" of this field and spell out the name of the city in the remaining positions.)
211–212	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "182" of the Payee City field.
213–221	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "182" in the Payee City field is a "1".
222–256	Blank	35	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–210	Blank	208	REQUIRED. Enter blanks.
211–216	Lender's Date of Acquisition or Abandonment	6	REQUIRED *FOR FORM 1099–A ONLY*. Enter the date of your acquisition of the secured property or the date you first knew or had reason to know that the property was abandoned in the format MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.
217	Liability Indicator	1	REQUIRED *FOR FORM 1099–A ONLY*. Enter the appropriate indicator from the table below: *Indicator* — *Usage* 1 — Borrower is personally liable for repayment of the debt. Blank — Borrower is *not* liable for repayment of the debt.
218–254	Description	37	REQUIRED *FOR FORM 1099–A ONLY*. Enter a brief description of the property. For example, for real property, enter the address, section, lot and block. For personal property, enter the type, make and model (*e.g.*, Car—1986 Buick Regal or Office Equipment, etc.).
255–256	Blank	2	REQUIRED. Enter blanks.

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)

FORM 1099–A

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE
22–31	32–41	42–81	82–121	122–161	162–190	191–192

SECTOR 1 (Continued)

PAYEE ZIP CODE	BLANK	LENDER'S DATE OF ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION	BLANK
193–201	202–210	211–216	217	218–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

FORM 1099–A

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE
22–31	32–41	42–51	52–91	92–131

SECTOR 1 (Continued)

PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
132–171	172–200	201–202	203–211	212–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	BLANK	LENDER'S DATE OF ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION
1	2	3–210	211–216	217	218–254

SECTOR 2 (Continued)

BLANK
255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)
FORM 1099–A

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–101	102–141

SECTOR 1 (Continued)

PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
142–181	182–210	211–212	213–221	222–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	BLANK	LENDER'S DATE OF ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION
1	2	3–210	211–216	217	218–254

SECTOR 2 (Continued)

BLANK
255–256

SEC. 8. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM 1099–B

.01 This section contains the general payment information from individual statements for Form 1099–B. For detailed explanations of the 1099–B fields request a copy of the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" available from IRS offices.

.02 FORM 1099–B CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.

RECORD NAME: PAYEE "B" RECORD
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–4	Payment Year	2	REQUIRED. Must be the last two digits of the year for whic payments are being reported (e.g., if payments were made in 198 enter "86"). Must be incremented each year.
5–6	Document Specific Code	2	REQUIRED. For Form 1099–B, enter blanks.

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099–B

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td>7</td><td>Blank or Corrected Return Indicator</td><td>1</td><td>REQUIRED. Enter blank. (Reserved for IRS use.) Diskette position 7 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using either magnetic media or paper forms. IN PRIOR YEARS, DISKETTE POSITION 6 WAS USED AS THE CORRECTED RETURN INDICATOR. THIS HAS NOW CHANGED TO POSITION 7. <i>YOU MUST ADJUST YOUR PROGRAMS.</i></td></tr>
<tr><td>8-11</td><td>Name Control</td><td>4</td><td>REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (-) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the Name Control:
<table>
<tr><th><i>Name</i></th><th><i>Name Control</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE *</td></tr>
<tr><td>James P. En Sr.</td><td>EN *</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must be left-justified and blank filled.</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identification Number (TIN) in positions 13–21 as either an Employer Identification Number, a Social Security Number, or the reason no number is shown. Enter the appropriate code from the following table:
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, enter a blank. If the number is unobtainable due to legitimate cause; <i>e.g.</i>, number applied for but not received, enter a blank.</td></tr>
</table></td></tr>
<tr><td>13-21</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the payee (SSN or EIN, as appropriate). Where an identification naumber has been applied for but not received or where there is any other legitimate cause for not having an identification number, <i>enter blanks</i>. Refer to Part A, Sec. 11.</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS. Any record containing an invalid identification number in this field will be returned for correction.
22–31	Payer's Account Number for Payee	10	REQUIRED. Payer may use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payer's file, should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. Enter blanks if the Payer's Account Number for Payee is not to be entered in this field. An account number can be any account number assigned by the payer to the payee (*i.e.*, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any number that will help identify the particular transaction that you are reporting. If a number is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.
	Payment Amount Fields (must be numeric)		The number of payment amounts is dependent on the number of Amount Indicators present in positions 19–27 of Sector 1 of the "A" Record. The First Payee Name Line *must* appear immediately after the last payment amount indicated as being used. For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one ten position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE 1). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS* (except those items that reflect a loss on Form 1099–B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "123bbbbbb," the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb," the "B" Rec ords must have only 5 payment amount fields. Payment amount MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE: 1 If any one payment amount exceeds "9999999999" (dol lars and cents), as many SEPARATE Payee "B" Records as ne essary to contain the total amount MUST be submitted for th Payee.
32–41	Payment Amount 1	10	This amount is identified by the indicator in position 19 of Secto 1 of the Payer/Transmitter "A" Record. *This amount must alwa be present.*

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF SECTOR 1 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–256 OF SECTOR 1, AND POSITIONS 1–256 OF SECTOR 2, IF NEEDED, OF THE PAYEE "B" RECORD. *FOR FORM 1099–B, SECTOR 2 WILL BE REQUIRED IF THERE ARE MORE THAN TWO PAYMENT FIELDS TO BE REPORTED IN THE PAYEE "B" RECORD.* USE THE APPROPRIATE FORMAT AS REQUIRED.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)
FORM 1099–B

SECTOR 1 (Continued)

42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identifying number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
122–161	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
162–190	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position in "162" of this field and spell out the name of the city in the remaining positions.)
191–192	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "162" of the Payee City field.
193–201	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "162" in the Payee City field is a "1".

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
202–213	Blank	12	REQUIRED. Enter blanks.
214	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transaction
215–220	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
221–228	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
229–254	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)
FORM 1099–B

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
92–131	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field*. If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.

RECORD NAME. PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
132–171	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
172–200	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "172" of this field and spell out the name of the city in the remaining positions.)
201–202	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "172" of the Payee City field.
203–211	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "172" in the Payee City field is a "1".
212–213	Blank	2	REQUIRED. Enter blanks.
214	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transaction
215–220	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
221–228	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
229–254	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)

FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
102–141	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
142–181	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
182–210	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "182" of this field and spell out the name of the city in the remaining positions.)
211–212	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "182" of the Payee City field.
213–221	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "182" in the Payee City field is a "1".
222–256	Blank	35	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

FORM 1099–B

iskette osition	Field Title	Length	Description and Remarks
ECTOR 2 (Continued)			
-213	Blank	211	REQUIRED. Enter blanks.
14	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY.* Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transaction
15–220	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY.* Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
21–228	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY.* Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
29–254	Description	26	REQUIRED *FOR FORM 1099–B ONLY.* Enter a brief description of the item or service for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
55–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)

FORM 1099–B

ECTOR 1 (Continued)			
2–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
2–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
2–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
2–111	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
12–151	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
152–191	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
192–220	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "192" of this field and spell out the name of the city in the remaining positions.)
221–222	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "192" of the Payee City field.
223–231	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "192" in the Payee City field is a "1".
232–256	Blank	25	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–213	Blank	211	REQUIRED. Enter blanks.
214	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transaction
215–220	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
221–228	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedure) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

FORM 1099–B

iskette osition	Field Title	Length	Description and Remarks
ECTOR 2 (Continued)			
29–254	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)

FORM 1099–B

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–121	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
122–161	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
162–201	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
202–230	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United states, insert a "1" in position "202" of this field and spell out the name of the city in the remaining positions.)

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)—Continued
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
231–232	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "202" of the Payee City field.
233–241	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "202" in the Payee City field is a "1".
242–256	Blank	15	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–213	Blank	211	REQUIRED. Enter blanks.
214	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transcation
215–220	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
221–228	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
229–254	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)
FORM 1090–B

SECTOR 1 (Continued)

42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)—Continued

FORM 1099-B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–131	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
132–171	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
172–211	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
212–256	Blank	45	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You MUST use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use the field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)—Continued
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
34–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".
43–213	Blank	171	REQUIRED. Enter blanks.
214	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlemnt date blank — Date of Sale is the trade date or this is an aggregate transaction
215–220	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
221–228	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
229–254	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer then 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)
FORM 1099–B

SECTOR 1 (Continued)

42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–101	Payment Amount 7	10	This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued
FORM 1099–B

iskette osition	Field Title	Length	Description and Remarks
ECTOR 1 (Continued)			
02–141	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
42–181	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
82–221	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
22–256	Blank	35	REQUIRED. Enter blanks.
ECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32-33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
34-42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".
3-213	Blank	171	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued
FORM 1099–B

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
214	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transaction
215–220	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
221–228	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
229–254	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or service for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
255–256	Blank	2	REQUIRED. Enter blanks.

SEC. 9. PAYEE "B" RECORD—RECORD LAYOUTS FOR FORM 1099–B

PAYEE "B" RECORD—RECORD LAYOUT—(USING ONE PAYMENT AMOUNT FIELD)
FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY
22–31	32–41	42–81	82–121	122–161	162–190

SECTOR 1 (Continued)

PAYEE STATE	PAYEE ZIP CODE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION
191–192	193–201	202–213	214	215–220	221–228	229–254

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)—Continued

FORM 1099–B

ECTOR 1 (Continued)

BLANK
255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

FORM 1099–B

ECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

ECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS
22–31	32–41	42–51	52–91	92–131	132–171

ECTOR 1 (Continued)

PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.
172–200	201–202	203–211	212–213	214	215–220	221–228

ECTOR 1 (Continued)

DESCRIPTION	BLANK
229–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

FORM 1099–B

ECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

ECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–101	102–141

ECTOR 1 (Continued)

PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
142–181	182–210	211–212	213–221	222–256

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)—Continued

FORM 1099-B

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–213	214	215–220	221–228	229–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)

FORM 1099-B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–71	72–111	112–151

SECTOR 1 (Continued)

PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
152–191	192–220	221–222	223–231	232–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATION	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–213	214	215–220	221–228	229–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING FIVE PAYMENT AMOUNT FIELDS)

FORM 1099-B

SECTOR 1

RECORD SEQUENCE	RECORD YEAR	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	FIRST PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–71	72–81	82–121

PAYEE "B" RECORD—RECORD LAYOUT (USING FIVE PAYMENT AMOUNT FIELDS)—Continued
FORM 1099-B

SECTOR 1 (Continued)

SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
122–161	162–201	202–230	231–232	233–241	242–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–213	214	215–220	221–228	229–254	255–256

PAYEE "B" RECORD —RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)
FORM 1099-B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6	FIRST PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–71	72–81	82–91	92–131

SECTOR 1 (Continued)

SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
132–171	172–211	212–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE
1	2	3–31	32–33	34–42	43–213	214	215–220

SECTOR 2 (Continued)

CUSIP NO.	DESCRIPTION	BLANK
221–228	229–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING SEVEN PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYEE'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7
92–101

SECTOR 1 (Continued)

FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
102–141	142–181	182–221	222–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–31	32–33	34–42	43–213

SECTOR 2 (Continued)

DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
214	215–220	221–228	229–254	255–256

SEC. 10. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM W–2G

.01 This section contains the general payment information from individual statements for Form W–2G. For detailed explanations of the W–2G fields, see the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G."

.02 FORM W–2G CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.

RECORD NAME: PAYEE "B" RECORD

FORM W–2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.

RECORD NAME: PAYEE "B" RECORD—Continued
FORM W–2G

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td>3–4</td><td>Payment Year</td><td>2</td><td>REQUIRED. Must be the last two digits of the year for which payments are being reported (<i>e.g.</i>, if payments were made in 1986, enter "86"). Must be incremented each year.</td></tr>
<tr><td>5–6</td><td>Document Specific Code Type of Water (Form W–2G only)</td><td>— 2</td><td>REQUIRED for W–2G.
Use only for reporting the Type of Wager on <i>Form W–2G</i>. This code will appear in position 5. Position 6 will be blank.
<table>
<tr><th><i>Category</i></th><th><i>Code</i></th></tr>
<tr><td>Horse Race Track (or Off Track Betting of a Horse Track nature)</td><td>1</td></tr>
<tr><td>Dog Race Track (or Off Track Betting of a Dog Track nature)</td><td>2</td></tr>
<tr><td>Jai-alai</td><td>3</td></tr>
<tr><td>State Conducted Lottery</td><td>4</td></tr>
<tr><td>Keno</td><td>5</td></tr>
<tr><td>Casino Type Bingo. DO NOT use this code for any other type of Bingo winnings <i>i.e.</i>, Church, Fire Dept., etc.</td><td>6</td></tr>
<tr><td>Slot Machines</td><td>7</td></tr>
<tr><td>Any other types of gambling winnings. This includes Church Bingo, Fire Dept. Bingo, unlabeled winnings, etc.</td><td>8</td></tr>
</table></td></tr>
<tr><td>7</td><td>Black or Corrected Return Indicator</td><td>1</td><td>REQUIRED. Enter blank. (Reserved for IRS use). Diskette position 7 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using either magnetic media or paper forms. IN PRIOR YEARS, DISKETTE POSITION 6 WAS USED AS THE CORRECTED RETURN INDICATOR. THIS HAS NOW CHANGED TO POSITION 7. <i>YOU MUST ADJUST YOUR PROGRAMS.</i></td></tr>
<tr><td>8–11</td><td>Name Control</td><td>4</td><td>REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (-) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the Name Control.
<table>
<tr><th><i>Name</i></th><th><i>Name Control</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE *</td></tr>
<tr><td>James P. En Sr.</td><td>EN *</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table></td></tr>
</table>

RECORD NAME: PAYEE “B” RECORD—Continued
FORM W-2G

<table>
<tr><th>Diskette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td>SECTOR 1 (Continued)</td><td></td><td></td><td></td></tr>
<tr><td></td><td></td><td></td><td>*Name Controls of less than four (4) significant characters must be left-justified and blank filled.</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identification Number (TIN) in positions 13–21 as either an Employer Identification Number, a Social Security Number, or the reason no number is shown. Enter the appropriate code from the following table:
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, enter a blank. If the number is unobtainable due to legitimate cause; <i>e.g.</i>, number applied for but not received, enter a blank.</td></tr>
</table></td></tr>
<tr><td>13–21</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the payee (SSN or EIN, as appropriate). Where an identification number has been applied for but not received or where there is any other legitimate cause for not having an identification number, <i>enter blanks</i>. Refer to Part A, Sec. 11.

<i>DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS.</i> Any record containing an invalid identifying number in this field will be returned for correction.</td></tr>
<tr><td>22–31</td><td>Payer’s Account Number for Payee</td><td>10</td><td>REQUIRED. Payer may use this field to enter the payee’s account number. The use of this item will facilitate easy reference to specific records in the payer’s file should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. An account number can be any account number assigned by the payer to the payee (<i>i.e.</i>, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE’S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any number that will help identify the particular transaction that you are reporting. If a number is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.</td></tr>
<tr><td></td><td>Payment Amount Fields (must be numeric)</td><td></td><td>The number of payment amounts is dependent on the number of Amount Indicators present in positions 19–27 of Sector 1 of the “A” Record. The First Payee Name Line <i>must</i> appear immediately after the last payment amount indicated as being used. For example, if you are reporting 1099–INT and you used only Amount Indicator “3” in the Payer/Transmitter “A” Record, then you will only use one ten position payment amount in the Payee “B” Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE 1). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Trans-</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued
FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			mitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS* (except those items that reflect a loss on Form 1099-B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "123bbbbbb", the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb", the "B" Record must have only 5 payment amount fields. Payment amounts MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE 1: If any one payment exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee.
32–41	Payment Amount 1	10	This amount is identified by the indicator in position 19 of Sector 1 of the Payer/Transmitter "A" Record. *This amount must always be present.*

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF SECTOR 1 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–256 OF SECTOR 1, AND POSITIONS 1–256 OF SECTOR 2 OF THE PAYEE "B" RECORD. *WHEN REPORTING INFORMATION FOR FORM W-2G TWO SECTORS MUST BE USED TO MAKE UP A PAYEE "B" RECORD.* USE THE APPROPRIATE FORMAT AS REQUIRED.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)
FORM W-2G

SECTOR 1 (Continued)			
42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
122–161	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued

FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
162–190	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "162" of this field and spell out the name of the city in the remaining positions.)
191–192	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "162" of the Payee City field.
193–201	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "162" of the Payee City field is a "1".
202–256	Blank	55	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–188	Blank	186	REQUIRED. Enter blanks.
189–194	Date Won	6	REQUIRED *FOR FORM W-2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.
195–209	Transaction	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number or any other information that will help identify the winning transaction. If no entry, enter blanks.
210–214	Race	5	REQUIRED *FOR FORM W-2G ONLY*. The race (or game) applicable to the winning ticket. If no entry, enter blanks.
215–219	Cashier	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
220–224	Window	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.
225–239	First ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable the first identification number of the person receiving the winnings. If no entry, enter blanks.
240–254	Second ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)

FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
92–131	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
132–171	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
172–200	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "172" of this field and spell out the name of the city in the remaining positions.)
201–202	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "172" of the Payee City field.
203–211	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "172" in the Payee City field is a "1".
212–256	Blank	45	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–188	Blank	186	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued
FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
189–194	Date Won	6	REQUIRED *FOR FORM W-2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.
195–209	Transaction	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number or any other information that will help identify the winning transaction. If no entry, enter blanks.
210–214	Race	5	REQUIRED *FOR FORM W-2G ONLY*. The race (or game) applicable to the winning ticket. If no entry, enter blanks.
215–219	Cashier	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
220–224	Window	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.
225–239	First ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
240–254	Second ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)
FORM W-2G

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
102–141	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.*

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued
FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
142–181	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
182–210	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "182" of this field and spell out the name of the city in the remaining positions.)
211–212	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "182" of the Payee City field.
213–221	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "182" in the Payee City field is a "1".
222–256	Blank	35	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–188	Blank	186	REQUIRED. Enter blanks.
189–194	Date Won	6	REQUIRED *FOR FORM W-2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.
195–209	Transaction	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number or any other information that will help identify the winning transaction. If no entry, enter blanks.
210–214	Race	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the race (or game) applicable to the winning ticket. If no entry, enter blanks.
215–219	Cashier	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
220–224	Window	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
225–239	First ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
240–254	Second ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
255–256	Blank	2	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)

FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–111	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose taxpayer identification number appears in positions 13–21 above. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose taxpayer identification number has been provided can be entered in this field. The names of the other payees may be entered in the Second Payee Name Line field.
112–151	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the taxpayer identification number in positions 13–21 above. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
152–191	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fil unused positions with blanks. The address MUST be present. Thi field MUST NOT contain any data other than the payee's mailin address.
192–220	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused po sitions with blanks. *Do not enter state and ZIP Code information i this field.* (If the payee lives outside of the United States, insert "1" in position "192" of this field and spell out the name of the cit in the remaining positions.)
221–222	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign coun try. You *MUST* use valid U.S. Postal Service abbreviations as show in Part A, Sec. 16. Use this field for state or country informatio

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

FORM W-2G

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			only. If the code used is for a foreign country, insert a "1" in position "192" of the Payee City field.
223–231	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "192" in the Payee City field is a "1".
232–256	Blank	25	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–188	Blank	186	REQUIRED. Enter blanks.
189–194	Date Won	6	REQUIRED *FOR FORM W-2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.
195–209	Transaction	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number or any other information that will help identify the winning transactions. If no entry, enter blanks.
210–214	Race	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the race (or game) applicable to the winning ticket. If no entry, enter blanks.
215–219	Cashier	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
220–224	Window	5	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the location of the person paying the winnings. If not entry, enter blanks.
225–239	First ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
240–254	Second ID	15	REQUIRED *FOR FORM W-2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
255–256	Blank	2	REQUIRED. Enter blanks.

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)
FORM W-2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE
22–31	32–41	42–81	82–121

SECTOR 1 (Continued)

PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
122–161	162–190	191–192	193–201	202–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–188	189–194	195–209	210–214	215–219

SECTOR 2 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
220–224	225–239	240–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)
FORM W-2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE
22–31	32–41	42–51	52–91

SECTOR 1 (Continued)

SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
92–131	132–171	172–200	201–202	203–211	212–256

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)—Continued

FORM W–2G

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–188	189–194	195–209	210–214	215–219

SECTOR 2 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
220–224	225–239	240–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

FORM W–2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–101

SECTOR 1 (Continued)

SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
102–141	142–181	182–210	211–212	213–221	222–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–188	189–194	195–209	210–214	215–219

SECTOR 2 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
220–224	225–239	240–254	255–256

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)

FORM W–2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)—Continued
FORM W-2G

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	FIRST PAYEE NAME LINE
22–31	32–41	42–51	52–61	62–71	72–111

SECTOR 1 (Continued)

SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
112–151	152–191	192–220	221–222	223–231	232–256

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–188	189–194	195–209	210–214	215–219

SECTOR 2 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
220–224	225–239	240–254	255–256

SEC. 12. END OF PAYER "C" RECORD

.01 The Control Total fields have been expanded from 12 to 15 positions. Adjust your programs accordingly.

.02 The End of Payer "C" Record is a summary record for a type of return for a given payer. This record will contain the total number of payees and the totals of the payment amount fields filed by a given payer. The "C" Record must be written after the last "B" Record for each type of return for a given payer. For each "A" Record and group of "B" Records on the file, there must be a corresponding "C" Record. For example, if you used Amount Codes 1, 3, and 6 in the "A" Record, the totals from the "B" Records will appear in Control Totals 1, 2, and 3 of the "C" Record.

.03 Payers/Transmitters must verify the accuracy of the totals in the "C" Record and must enter the totals on the transmittal Form 4804, 4802 or computer generated substitute, which will accompany the shipment. The lines used on Forms 4804 and 4802 to record payment amounts correspond with the Amount Codes used in the "A" Record. These forms have been updated for 1986.

.04 The End of Payer "C" Record must be followed by a State Totals "K" Record (if any), or new Payer/Transmitter "A" Record for the next Payer (if any), or an End of Transmission "F" Record.

RECORD NAME: END OF PAYER "C" RECORD

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Enter "1". Must be the first character of each END OF PAYER RECORD.
2	Record Type	1	REQUIRED. Enter "C".
3–8	Number of Payees	6	REQUIRED. Enter the total number of Payee "B" Records covered by the preceding Payer/Transmitter "A" Record. Right-justify and zero fill.
9–23	Control Total 1	15	REQUIRED. Please note that all Control Total fields have been expanded from 12 to 15 positions. Enter accumulated totals from Payment Amount 1. Right-justify and zero fill. IF LESS THAN NINE AMOUNT FIELDS ARE BEING REPORTED, ZERO FILL UNUSED CONTROL TOTAL FIELDS.

RECORD NAME: END OF PAYER "C" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
	If any corresponding Payment Amount Fields are present in the Payee "B" Records, accumulate into the appropriate Control Total field. ZERO FILL UNUSED CONTROL TOTAL FIELDS. Please note that all Control Total fields have been expanded from 12 to 15 positions.		
24–38	Control Total 2	15	
39–53	Control Total 3	15	
54–68	Control Total 4	15	
69–83	Control Total 5	15	
84–98	Control Total 6	15	
99–113	Control Total 7	15	
114–128	Control Total 8	15	
129–143	Control Total 9	15	
144–256	Blank	113	REQUIRED. Enter blanks.

SEC. 13. END OF PAYER "C" RECORD—RECORD LAYOUT

END OF PAYER "C" RECORD—RECORD LAYOUT

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	NUMBER OF PAYEES	CONTROL TOTAL 1	CONTROL TOTAL 2	CONTROL TOTAL 3	CONTROL TOTAL 4
1	2	3–8	9–23	24–38	39–53	54–68

SECTOR 1 (Continued)

CONTROL TOTAL 5	CONTROL TOTAL 6	CONTROL TOTAL 7	CONTROL TOTAL 8	CONTROL TOTAL 9	BLANK
69–83	84–98	99–113	114–128	129–143	144–256

SEC. 14. STATE TOTALS "K" RECORD

.01 The Control Total fields have been expanded from 12 to 15 positions. Adjust your programs accordingly.

.02 The State Totals "K" Record is a summary for a given payer and a given state in the Combined Federal/State Filing Program, used ONLY when state reporting approval has been granted.

.03 The "K" Record will contain the total number of payees and the totals of the payment amount fields filed by a given payer for a given state. The "K" Record(s) must be written after the "C" Record for the related "A" Record.

.04 There MUST be a separate "K" Record for *each state* being reported.

.05 Refer to Part A, Sec. 14 for the requirements and conditions that *MUST* be met to file on this program.

RECORD NAME: STATE TOTALS "K" RECORD

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Enter "1". Must be the first character for each STATE TOTALS "K" RECORD.
2	Record Type	1	REQUIRED. Enter "K".
3–8	Number of Payees	6	REQUIRED. Enter the total number of Payee "B" Records being coded for this state. Right-justify and zero fill.
9–23	Control Total 1	15	REQUIRED. Please note that all Control Total fields have been expanded from 12 to 15 positions. Enter accumulated totals from Payment Amount 1. Right-justify and zero fill. IF LESS THAN

RECORD NAME: STATE TOTALS "K" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			NINE AMOUNT FIELDS ARE BEING REPORTED, ZERO FILL UNUSED CONTROL TOTAL FIELDS.
	If any corresponding Payment Amount fields are present in the Payee "B" Records, accumulate into the appropriate Control Total field. ZERO FILL UNUSED CONTROL TOTAL FIELDS. Please note that all Control Total fields have been expanded from 12 to 15 positions.		
24–38	Control Total 2	15	
39–53	Control Total 3	15	
54–68	Control Total 4	15	
69–83	Control Total 5	15	
84–98	Control Total 6	15	
99–113	Control Total 7	15	
114–128	Control Total 8	15	
129–143	Control Total 9	15	
144–254	Blank	111	REQUIRED. Enter blanks.
255–256	State Code	2	REQUIRED. Enter the code assigned to the state which is to receive the information. Refer to Part A, Sec. 14.10.

SEC. 15. STATE TOTALS "K" RECORD—RECORD LAYOUT

STATE TOTALS "K" RECORD—RECORD LAYOUT

SECTOR 1 (Please note that all Control Total fields have been expanded from 12 to 15 positions.)

RECORD SEQUENCE	RECORD TYPE	NUMBER OF PAYEES	CONTROL TOTAL 1	CONTROL TOTAL 2	CONTROL TOTAL 3	CONTROL TOTAL 4
1	2	3–8	9–23	24–38	39–53	54–68

CONTROL TOTAL 5	CONTROL TOTAL 6	CONTROL TOTAL 7	CONTROL TOTAL 8	CONTROL TOTAL 9	BLANK	STATE CODE
69–83	84–98	99–113	114–128	129–143	144–254	255–256

SEC. 16. END OF TRANSMISSION "F" RECORD

.01 The "F" Record is a summary of the number of payers and diskettes in the entire file.

.02 This record should be written after the last "C" Record (or "K" Record, when applicable) of the entire file.

END OF TRANSMISSION "F" RECORD

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Type	1	REQUIRED. Enter "F". Must be first character of END OF TRANSMISSION RECORD.

END OF TRANSMISSION "F" RECORD—Continued

Diskette Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
2–5	Number of "A" Records	4	REQUIRED. You may enter the total number of Payer/Transmitter "A" Records for this transmission. Right-justify and zero fill or enter all zeros.
6–8	Number of Diskettes	3	REQUIRED. You may enter the total number of diskettes in this transmission. Right-justify and zero fill or enter all zeros.
9–30	Zero	22	REQUIRED. Enter zeros.
31–256	Blank	226	REQUIRED. Enter blanks.

SEC. 17. END OF TRANSMISSION "F" RECORD—RECORD LAYOUT

RECORD TYPE	NUMBER OF "A" RECORDS	NUMBER OF DISKETTES	ZERO	BLANK
1	2–5	6–8	9–30	31–256

26 CFR 601.602: Tax forms and instructions.

Rev. Proc. 86–35

SECTION 1. PURPOSE

This Revenue Procedure establishes a handling and shipping charge for processing requests for bulk quantities of tax forms. This charge only applies to those engaged in the preparation of tax returns for private gain.

SEC. 2. CHARGES

.01 Charges for tax forms will be established on the basis of each 100 printed units ordered. The schedule of charges for handling and shipping bulk quantities of tax forms will be based on a rate of $1.00 per hundred printed units, or fraction thereof. However, all bulk orders for tax forms will be subject to a minimum charge of $3.00.

.02 No charge will be made to practitioners or their firms who order no more than 15 "information" copies of any tax form nor more than 2 "information" copies of any instruction or taxpayer information publication. Additionally, no charge will be made to practitioner firms who order bulk quantities of optically scanned information returns.

.03 No charge will be made to a bank, post office, public library or other organization for any quantity of forms and instructions intended for the convenience and use of the taxpayer, so long as such organization is not engaged in the preparation of tax returns for private gain.

.04 Single copies of Publications 17 and 334 will be provided without charge. Multiple copies of either publication will not be provided to individuals or organizations except where the Regional Commissioner or District Director determines that such distribution will further the interests of taxpayer service or education. A user charge of $.50 per copy will apply to all approved multiple copy requests. Regional Commissioners, District Directors and appropriate National Office officials may continue to provide multiple copies without charge for use in Service-sponsored programs (e.g. Understanding Taxes and VITA). Additionally, in an effort to reduce the number of separate orders, multiple copies (one per employee) of Publications 17 and 334 may be issued to practitioner firms, without regard to the user charge. Priority must be given to filling single copy requests for Publications 17 and 334. Requests for bulk quantities of either publication which jeopardize the Service's ability to respond on a timely basis to such single copy demand should not be honored. For individuals who wish for their own purposes to print copies of Publications 17 or 334, the Service will provide page negatives of either publication for a user charge of $3.00 per page negative.

.05 All user charges will be commensurate with the prevailing postage and handling costs and will be established by the Assistant Commissioner (Human Resources).

.06 All requestors that are subject to the user charge as outlined above will be sent a bill to cover shipping and handling charges for processing bulk orders.

SEC. 3. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 84–38, 1984–1 C.B. 514, is superseded.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Tevor Adel	Silver Spring, MD	Certified Public Accountant	Indefinite from June 2, 1986
John H. Peimann	Ottawa, KS	Certified Public Accountant	Twenty-One Months from June 1, 1986
John D. Raikos	Indianapolis, IN	Attorney	Indefinite from May 20, 1986
Vernon Pubel	Hickory, NC	Enrolled Agent	Indefinite from May 28, 1986
Wayne Boyer	Southfield, MI	Enrolled Agent	Eight Months from May 12, 1986
Thomas McPhee	McAllen, TX	Enrolled Agent	Indefinite from June 15, 1986
Glen R. Verber	Houston, TX	Certified Public Accountant	Ninety Days from May 19, 1986
Beverly Worth	Winona Lake, IN	Enrolled Agent	Five Years from June 17, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section Affected	Subject	Published in the Bulletin	Expiration Date for Submission of Views
26 CFR 1.88–1, 1.468A–1 through 1.468A–8 added	Nuclear decommissioning costs	1986–31 I.R.B. 22	Sept. 8, 1986

Numerical Finding List[1]

Bulletin 1986–27 through 1986–33

Announcements:

86–84, 1986–27, I.R.B. *35*
86–85, 1986–30 I.R.B. *7*
86–86, 1986–30 I.R.B. *7*
86–87, 1986–30 I.R.B. *16*
86–88, 1986–30 I.R.B. *16*
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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–100, page 4.
Credit for producing fuel from a nonconventional source. A liquid coal-water mixture produced by taxpayer is not a synthetic fuel produced from coal and is, therefore, not a qualified fuel eligible for the credit as fuel produced from nonconventional sources under section 29(c)(1)(C) of the Code.

Rev. Rul. 86–101, page 5.
Partnerships; conversion of a general partnership interest into a limited partnership interest upon death of general partner. Conversion does not constitute disposition of partnership interest that closes the partnership year with respect to the deceased partner.

Rev. Rul. 86–102, page 5.
Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for September 1986.

Notice 86–9, page 19.
Relief is granted under section 7805(b) of the Code with respect to the product grouping rules of the final regulations under section 936(h).

ESTATE AND GIFT TAXES

T.D. 8095, page 6.
Regulations relate to the disclaimer of property transferred by gift or inheritance.

ADMINISTRATIVE

Announcement 86–93, page 20.
Guidance is provided to taxpayers claiming relief under the recent amendment to section 57(a)(9) of the Code that allows certain insolvent taxpayers to reduce the capital gains preference item for purposes of the Individual Alternative Minimum Tax.

Finding Lists begin on page 23.
Announcement of Disbarments and Suspensions on page 21.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 29.—Credit for Producing Fuel from a Nonconventional Source

(Also Section 48(l))

Credit for producing fuel from a nonconventional source. A liquid coal-water mixture produced by taxpayer is not a synthetic fuel produced from coal and is, therefore, not a qualified fuel eligible for the credit as fuel produced from nonconventional sources under section 29(c)(1)(C) of the Code.

Rev. Rul. 86-100

ISSUE

If a taxpayer produces a viscous, heavy, liquid coal-water mixture that can be used as a substitute for oil, then under section 29(c)(1)(C) (formerly section 44D) of the Internal Revenue Code, is that mixture a "synthetic fuel produced from coal" and therefore a qualified fuel which is eligible for the credit as fuel produced from nonconventional sources?

FACTS

Taxpayer produces a fuel by a process that finely grinds coal, mixes it with water, mechanically removes impurities (such as particles of pyritic sulfur) by flotation, and adds surfactants that adhere to the surface of each coal particle. Because the surfactants give each coal particle a negative electrical charge, the coal particles repel one another and remain in suspension. The resulting coal-water mixture has the physical properties of a viscous, heavy liquid that can be stored, pumped, and burned as a substitute for No. 6 oil in properly modified furnaces or boilers. The coal-water mixture is approximately 70 percent coal, 29 percent water, and 1 percent additives.

LAW AND ANALYSIS

Section 29(a) of the Code provides that there is allowed a credit of $3, multiplied by the barrel-of-oil equivalent of qualified fuels sold by the taxpayer to an unrelated person during the tax year.

Section 29(c)(1)(C) of the Code provides that the term "qualified fuels" includes liquid, gaseous, or solid synthetic fuels produced from coal (including lignite), including such fuels when used as feedstocks.

The credit allowed by section 29 (originally designated as section 44D) of the Code was added by section 231 of the Crude Oil Windfall Profit Tax Act of 1980, 1980-3 C.B. 1, 40. The conference committee report that accompanied that Act outlined the eligible sources for the credit and specifically included liquid, gaseous, or solid synthetic fuel from coal liquefaction or gasification facilities. That report also stated that solid synthetic fuel produced from coal liquefaction or gasification would include solvent refined coal. H.R. Rep. No. 96-817 (Conf. Rep.) 96th Cong., 2d Sess. 138 (1980), 1980-3 C.B. 245, 298.

Section 48(l)(3)(A)(iii) of the Code includes in the definition of alternative energy property (for purposes of allowing an investment tax credit under section 38 of the Code) equipment for converting an alternate substance into a synthetic liquid, gaseous, or solid fuel. This provision was added by section 301 of the Energy Tax Act of 1978, 1978-3 (Vol. 2) C.B. 1, 20. The Senate report that accompanied that Act specifically included, in the definition of alternative energy property, property used in coal liquefaction and gasification. S. Rep. No. 95–529, 95th Cong., 1st Sess. 75 (1977), 1978-3 (Vol. 2) C.B. 203, 267.

Both sections 29(c) and 48(l) reflect a congressional intent to encourage domestic energy conservation and production. In identifying certain fuels that qualify for the production credit, section 29 uses language almost identical to the language in section 48(l) that lists certain property that qualifies as energy property for purposes of the business energy tax credit. Qualified fuels, under section 29, include "liquid, gaseous, or solid synthetic fuels" produced from coal. Alternative energy property, under section 48(l), includes equipment for converting an alternate substance into a "synthetic liquid, gaseous, or solid fuel." Thus, the definition provided for the term "synthetic fuel" under section 48(l) and Income Tax Regulations thereunder is relevant to the interpretation of the term "synthetic fuel" in section 29(c)(1)(C).

Section 1.48-9(c)(5) of the regulations defines a synthetic fuel as one that must differ significantly in chemical composition, as opposed to physical composition, from the alternate substance used to produce it. That section further provides that synthetic fuel equipment does not include equipment that merely mixes an "alternate" substance with another substance. The regulation expressly states that synthetic fuel equipment does not include equipment that mixes coal and water to produce a slurry for purposes of transportation.

The Code and regulations recognize that a synthetic fuel is the result of substantial chemical change. Coal liquefaction and gasification processes, which were discussed in the congressional reports, are examples of processes that involve substantial chemical changes. Coal liquefaction and gasification processes are chemical processes that use pressure, heat, and the addition of hydrogen to change substantially the chemical composition of coal into substances that are chemically similar to oil or natural gas or noncoal-like solids. To produce solvent refined coal, finely ground coal is subjected to pressures up to 4,000 pounds per square inch and temperatures of about 800 degrees Fahrenheit in the presence of hydrogen and an oily hydrocarbon liquid solvent. Under these conditions, the coal is chemically changed by cracking and hydrogenation.

On the other hand, the process at issue in this revenue ruling is not a process similar to liquefaction or gasification because it does not result in a chemical change to the coal. It primarily results in a physical surface change, a coating, to the solid coal. As a result of that coating, mixing the coal with water produces a mixture that can be handled and used like a liquid. The lack of a chemical change to the coal itself precludes, under section 1.48-9(c)(5) of the regulations, a conclusion that the coal-water mixture is a "synthetic fuel" for purposes of the qualified fuels credit.

Section 1.48-9(c)(5) of the regulations clearly provides that equipment that merely mixes an alternate substance with another substance or mixes coal and water to form a slurry for transportation is not synthetic fuel equipment. The coal-water mixture in this situation differs from a slurry only in the manner in which the coal is held in suspension. In a slurry, agitation is used to keep the particles in suspension. Here, it is the polarization that keeps the particles in suspension. However, in both instances the processes produce a coal and water mixture with the required physical separation of particles necessary to produce the characteristics of a liquid. The presence of the surfactants does not contribute any improvement in the characteristics of the mixture as a fuel. Therefore, under the regulations, the equipment used is not synthetic fuel equipment. It follows that the product is not a synthetic fuel.

HOLDING

The coal-water mixture described in this revenue ruling is not a synthetic fuel produced from coal and thus under section 29(c)(1)(C) of the Code is not a qualified fuel eligible for credit.

Section 48(l).—Definitions; Special Rules; Energy Property

Whether a viscous, heavy liquid coal-water mixture produced by the taxpayer that can be used as a substitute for oil is a "synthetic fuel produced from coal" and, therefore, a qualified fuel that is eligible for the credit as fuel produced from nonconventional sources. See Rev. Rul. 86-100, page 4.

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term and long-term rates are set forth for the month of September 1986. See Rev. Rul. 86-102, this page.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of September 1986. See Rev. Rul. 86-102, this page.

Section 468.—Special Rules for Mining and Solid Waste Reclaimation and Closing Costs

Federal short-term, mid-term and long-term rates are set forth for the month of September 1986. See Rev. Rul. 86-102, this page.

Section 706.—Taxable Year of Partner and Partnership

26 CFR 1.706-1: Taxable years of partner and partnership.

Partnerships; conversion of a general partnership interest into a limited partnership interest upon death of general partner. Conversion does not constitute disposition of partnership interest that closes the partnership year with respect to the deceased partner.

Rev. Rul. 86-101

ISSUE

If a partnership agreement provides that, upon the death of a general partner, the partner's interest converts into that of a limited partner, does the partnership taxable year close with respect to a deceased partner under section 706 of the Internal Revenue Code?

FACTS

A, *B*, and *C* were general partners in *LP*, a limited partnership. The partnership agreement provided that, upon the death of any general partner, that partner's interest would be automatically converted into a limited partnership interest. All three general partners, as well as *LP*, were calendar year taxpayers. *A* died on July 1, and under the partnership agreement, *A*'s interest automatically became that of a limited partner.

LAW AND ANALYSIS

Section 706(c)(1) of the Code provides that, except in the case of a termination of a partnership and except as provided in section 706(c)(2), the taxable year of a partnership shall not close as the result of the death of a partner or the sale or exchange of a partner's interest in the partnership.

Section 706(c)(2)(A)(i) of the Code provides that the taxable year of a partnership shall close with respect to a partner who sells or exchanges the partner's entire interest in the partnership.

Section 706(c)(2)(B) of the Code provides that, other than at the end of the partnership's taxable year, the taxable year of a partnership shall not close with respect to a partner who sells or exchanges less than the partner's entire interest in the partnership.

Section 1.706-1(c)(3)(i) of the Income Tax Regulations provides that if a deceased partner's estate or other successor sells or exchanges its entire interest in the partnership or if its entire interest is liquidated, the partnership's taxable year with respect to the estate or other successor shall close on the date of the sale or exchange, or on the date of the completion of the liquidation.

Section 1.706-1(c)(3)(iv) of the regulations provides that if, under the terms of an agreement existing on the date of death of a partner, a sale or exchange of the decedent partner's interest in the partnership occurs upon that date, then the taxable year of the partnership with respect to the decedent partner shall close upon the date of death.

Rev. Rul. 84-52, 1984-1 C.B. 157, holds that, for purposes of section 721 of the Code, the conversion of a general partnership interest into a limited partnership interest is treated as a contribution to the partnership of the general partnership interest in exchange for the limited partnership interest.

The legislative history of section 706(c)(2) of the Code indicates that Congress did not intend to close the taxable year of a partnership with respect to a partner whose interest is liquidated, sold, or exchanged to an outsider unless the partner no longer retains any interest in the partnership. If the partner's interest is merely reduced, the partnership year remains open with respect to the partner. H.R. Rep. No. 1337, 83d Cong., 2d Sess. A226 (1954); S. Rep. No. 1622, 83d Cong., 2d Sess. 386 (1954).

In the present case, since *A*'s successor continued to hold an interest in the partnership, the conversion is not an exchange of the partner's entire partnership interest for purposes of section 706(c)(2)(A) of the Code or section 1.706-1(c)(3)(iv) of the regulations. Consequently, the general rule under section 706(c) applies and the partnership year as to *A* remains open.

HOLDING

A conversion of a general partnership interest into a limited partnership interest is an exchange that does not result in a disposition of the converting partner's entire partnership interest, and, therefore, the taxable year of the partnership is not closed under section 706(c)(2)(A) of the Code or section 1.706-1(c)(3)(iv) of the regulations.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 280G, 467, 468.)

Rev. Rul. 86-102

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of September 1986 are as follows:

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term				
AFR	6.50%	6.40%	6.35%	6.32%
110% AFR	7.16%	7.04%	6.98%	6.94%
120% AFR	7.83%	7.68%	7.61%	7.56%
Mid-Term				
AFR	7.21%	7.08%	7.02%	6.98%
110% AFR	7.94%	7.79%	7.72%	7.67%
120% AFR	8.68%	8.50%	8.41%	8.35%
Long-Term				
AFR	7.47%	7.34%	7.27%	7.23%
110% AFR	8.23%	8.07%	7.99%	7.94%
120% AFR	9.00%	8.81%	8.72%	8.65%

Section 2041.—Powers of Appointment

26 CFR 20.2041-3: Powers of appointment created after October 21, 1942.

T.D. 8095

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER B, SUBCHAPTER H, PART 20—ESTATE TAX; ESTATES OF DECEDENTS DYING AFTER AUGUST 16, 1954—PART 25—GIFT TAX; GIFTS MADE AFTER DECEMBER 31, 1954—PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Qualified Disclaimers

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the disclaimer of property transferred by gift or inheritance. Changes to the applicable law were made by the Tax Reform Act of 1976, the Revenue Act of 1978 and the Act of October 4, 1966. These regulations provide necessary guidance to the public for compliance with the law and affect those persons who disclaim an interest in property.

DATES: The regulations are effective for taxable transfers made after December 31, 1976, which create an interest in a person who disclaims that interest.

FOR FURTHER INFORMATION CONTACT: William A. Jackson of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T:202-566-4336, not a toll-free call).

SUPPLEMENTARY INFORMATION:

BACKGROUND

On July 22, 1980, the FEDERAL REGISTER published proposed amendments to the Estate and Gift Tax Regulations (26 CFR Parts 20 and 25) under sections 2041, 2045, 2055, 2056, 2511, 2514, and 2518 of the Internal Revenue Code of 1954 (Code) (45 FR 48922). The amendments were proposed to conform the regulations to section 2009(b) of the Tax Reform Act of 1976 (90 Stat. 1893), which added section 2518 to the Code; section 702 (m) of the Revenue Act of 1978 (92 Stat. 2935), which allowed a surviving spouse to receive an interest in property as a result of a qualified disclaimer by the spouse; and the Act of October 4, 1966 (80 Stat. 872), which allowed an interest disclaimed by a person other than the surviving spouse to be treated as passing from the decedent to the surviving spouse where the spouse receives the interest as a result of the disclaimer. A public hearing was held on November 18, 1980. After consideration of all comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

SUMMARY OF REVISIONS

Effective Dates

Sections 20.2041-3(d)(6)(i) and 25.2518-1(a) have been revised to clarify that section 2518 applies to all interests in property if the interest in the property was created by a taxable transfer made after December 31, 1976. Thus, section 2518 applies to a revocable trust created prior to December 31, 1976 if it becomes irrevocable after that date. The 9-month period in such a case would be measured from the date on which the transfer creating the interest became irrevocable.

Effect of a Qualified Disclaimer

One commentator suggested that §25.2518-1(b) be amended to clarify that a beneficiary of a generation-skipping trust who makes a qualified disclaimer is treated as never having been a beneficiary. No revision was made in paragraph (b) of §25.2518-1 because that paragraph already states that the disclaimed interest is treated as if it had never been transferred to the disclaimant and that the interest is treated as passing directly to the person entitled to receive the property as a result of the disclaimer.

The same commentator also suggested that §25.2056(d)-1(a) be amended to specify the effect of a nonqualified disclaimer by a surviving spouse. No change has been made under §25.2056(d)-1(a) because §25.2511-1(c)(1) already specifically states that any disposition which is not a qualified disclaimer constitutes the making of a gift.

Effect of Local Law

Several commentators believed that the proposed regulation under paragraph (c)(1) of §25.2518-1, relating to the effect of local law, is wrong because of the requirement that the disclaimer be effective under local law. In response to these comments, paragraph (c)(1) has been revised to clarify that even if the requirements of local law are not met, one can nevertheless make a qualified disclaimer under section 2518 if, under applicable local law, the interest is transferred, as a result of attempting the disclaimer, to another person without any direction on the part of the disclaimant. Mandatory actions by the disclaimant which are required under local law merely to divest ownership of the property in the disclaimant and vest it in another person will not disqualify the disclaimer for purposes of section 2518. Further, the rule under paragraph (c)(2) of §25.2518-1 has been changed to make it clear that whether a transfer is voidable has no effect on the determination of whether a disclaimer constitutes a qualified disclaimer. This Treasury decision does not contain regulations relating to the changes made to the law by the Economic Recovery Tax Act of 1981 which allows certain transfers to be treated as qualified disclaimers even if no effective disclaimer has been made under local law. Proposed regulations relating to this change will be published shortly in another project (LR-212-81).

Beneficiary Under Twenty-One Years of Age

In order to make a qualified disclaimer under section 2518, a disclaimer must be made no later than 9 months after the transfer creating the interest in the person disclaiming, or, if later, 9 months after the day the disclaimant attains age 21. The proposed regulations have been revised to clarify in paragraph (d)(3) of §25.2518-2 that in the case of a beneficiary of an interest in property who is under 21 years of age, any actions taken with regard to the interest by the beneficiary or a custodian prior to the beneficiary's twenty-first birthday will not be considered to be an acceptance of the interest by the beneficiary.

Joint Ownership

Several commentators believed the regulations should be revised to allow a qualified disclaimer to be made with respect to jointly owned property within 9 months of the death of the first joint tenant. Several other commentators believe that the regulations should allow at least the accretive portion to be disclaimed. Other commentators suggested that examples be inserted into the final regulations that illustrate the effect of the joint ownership rules in community property jurisdictions, the issue of acceptance, the effect of revocability, and the effect of former section 2515, relating to the creation of a joint tenancy.

A minor revision has been made in the regulations regarding the ability of a surviving joint tenant to disclaim the jointly held property. The general rule that a disclaimer of a joint interest must be made within 9 months of the transfer creating the interest remains unchanged because each joint tenant receives an interest in the entire property subject to the tenancy, as well as the rights of survivorship, at the time of the transfer creating the joint interest. See *Pearl M. Kennedy* v. *Commissioner*, Docket No. 33349-83, T.C. Memo, 1986-3, January 2, 1986. However, in the case of a joint tenancy between spouses or a tenancy by the entirety in real property created after 1976 and before 1982 where no election is made under section 2515, the surviving tenant can make a qualified disclaimer of the entire jointly held property (except any portion attributable to consideration furnished by the surviving tenant) within 9 months after the death of the first tenant to die if such tenant dies before 1982. If such tenant dies in 1982 or thereafter, the surviving tenant may only disclaim one-half of the jointly held property. In addition, a joint tenant cannot make a qualified disclaimer of any portion of the joint interest attributable to consideration furnished by that tenant. Examples have been added to the final regulations illustrating the other issues raised by the commentator.

Surviving Spouse

Under the proposed regulations, a surviving spouse could not make a qualified disclaimer if the spouse retained the power to direct the beneficial enjoyment of disclaimed property. Several commentators believe that the Revenue Act of 1978 reversed this result. No change has been made regarding the requirements that a surviving spouse must meet in order to make a qualified disclaimer. The statute states that the interest must pass to a person without any direction on the part of the person making the disclaimer. If the spouse retains the power to direct beneficial enjoyment of the disclaimed property, the disclaimer would violate this rule.

Disclaimer of Less than an Entire Interest

Section 25.2518-3 has been revised in response to the many comments received. Under the proposed regulations, all interests in income were treated as one separate interest and all interests in corpus were treated as another separate interest. Under the final regulations, each interest or power with respect to property that is separately created by the transferor is generally treated as a separate interest. Thus, a person could make a qualified disclaimer of one interest in corpus while retaining another interest in corpus, assuming that all other requirements of section 2518(b) have been met. However, if local law merges separately created interests, a qualified disclaimer will be allowed only if there is a disclaimer of the entire merged interest or an undivided portion of such merged interest. In addition, the final regulations provide that where a merger of separate interests would occur but for the creation by the transferor of a nominal interest, a qualified disclaimer will be allowed only if there is a disclaimer of all of the separate interests, or an undivided portion of all such interests, which would have merged but for the nominal interest.

Disclaimer of a Pecuniary Amount

Section 25.2518-3(c) of the proposed regulations has been revised to provide that a disclaimer of a specific pecuniary amount out of a pecuniary or nonpecuniary bequest or gift can be a qualified disclaimer provided that no income or other benefit of the disclaimed amount inures to the benefit of the disclaimant either prior to or subsequent to the disclaimer. Thus, following a disclaimer of a specific pecuniary amount, the disclaimed amount and any income attributable to such amount must be segregated from the portion of the gift or bequest that was not disclaimed. Further, the segregation of any assets making up the disclaimed amount must be made on the basis of the fair market value of the assets on the date of the disclaimer or on a basis fairly representative of the value changes that may have occurred between the date of the transfer and the date of the disclaimer. The final regulations also provide rules for making a disclaimer of a specific pecuniary amount after the beneficiary has already received a distribution from the gift or bequest.

Life Insurance and Annuity Contracts

Two commentators questioned the necessity of singling out life insurance proceeds and annuities because the same rules apply to such interests as apply to any other interest in property. In response to this comment, §25.2518-4 has been deleted from the final regulations.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. The notice of proposed rule-making relating to this final rule was published before January 1, 1981. Accordingly, a regulatory flexibility analysis under the Regulatory Flexibility Act is not required for this final rule.

PAPERWORK REDUCTION ACT

The collection of information requirements contained in this regulation have been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB (control number 1545-0959).

DRAFTING INFORMATION

The principal author of this regulation is William A. Jackson of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations.

Accordingly, 26 CFR Parts 20, 25, and 602 are amended as follows:

Paragraph 1. The authority citation for Part 20 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 2. Section 20.2041-3 (d) (6) is revised to read as follows:

§20.2041-3 Powers of appointment created after October 21, 1942

(d) *Releases, lapses, and disclaimers of general powers of appointment.*

(6)(i) A disclaimer or renunciation of a general power of appointment created in a taxable transfer after December 31, 1976, in the person disclaiming is not considered a release of the power if the disclaimer or renunciation is a qualified disclaimer as described in section 2518 and the corresponding regulations. If the disclaimer or renunciation is not a qualified disclaimer, it is considered a release of the power by the disclaimant.

(ii) The disclaimer or renunciation of a general power of appointment created in a taxable transfer before January 1, 1977, in the person disclaiming is not considered to be a release of the power. The disclaimer or renunciation must be unequivocal and effective under local law. A disclaimer is a complete and unqualified refusal to accept the rights to which one is entitled. There can be no disclaimer or renunciation of a power after its acceptance. In the absence of facts to the contrary, the failure to renounce or disclaim within a reasonable time after learning of its existence will be presumed to constitute an acceptance of the power. In any case where a power is purported to be disclaimed or renounced as to only a portion of the property subject to the power, the determination as to whether or not there has been a complete and unqualified refusal to accept the rights to which one is entitled will depend on all the facts and circumstances of the particular case, taking into account the recognition and effectiveness of such a disclaimer under local law. Such rights refer to the incidents of the power and not to other interests of the decedent in the property. If effective under local law, the power may be disclaimed or renounced without disclaiming or renouncing-such other interests.

Par. 3. There is added immediately after §20.2044-1, the following new section:

§20.2046-1 Disclaimed property.

This section shall apply to the disclaimer or renunciation of a taxable transfer creating an interest in the person disclaiming made after December 31, 1976. If a qualified disclaimer is made with respect to such a transfer, the Federal estate tax provisions are to apply with respect to the property interest disclaimed as if the interest had never been transferred to the person making the disclaimer. See section 2518 and the corresponding regulations for rules relating to a qualified disclaimer.

Par. 4. Section 20-2055-2(c) is revised to read as follows:

§20.2055-2 Transfers not exclusively for charitable purposes

(c) *Disclaimers*—(1) *Decedents dying after December 31, 1976.* In the case of a bequest, devise, or transfer made by a decedent dying after December 31, 1976, the amount of a bequest, devise or transfer for which a deduction is allowable under section 2055 includes an interest which falls into the bequest, devise or transfer as the result of either—

(i) A qualified disclaimer (see section 2518 and the corresponding regulations for rules relating to a qualified disclaimer), or

(ii) The complete termination of a power to consume, invade, or appropriate property for the benefit of an individual by reason of the death of such individual or for any other reason, if the termination occurs within the period of time (including extensions) for filing the decedent's Federal estate tax return and before such power has been exercised.

(2) *Decedents dying before January 1, 1977.* In the case of a bequest, devise or transfer made by a decedent dying before January 1, 1977, the amount of a bequest, devise or transfer, for which a deduction is allowable under section 2055 includes an interest which falls into the bequest, devise or transfer as a result of either—

(i) A disclaimer of a bequest, devise, transfer, or power, if the disclaimer is made within 9 months (15 months if the decedent died on or before December 31, 1970) after the decedent's death (the period of time within which the estate tax return must be filed under section 8075) or within any extension of time for filing the return granted pursuant to section 8081, and the disclaimer is irrevocable at the time the deduction is allowed, or

(ii) The complete termination of a power to consume, invade, or appropriate property for the benefit of an individual (whether the termination occurs by reason of the death of the individual, or otherwise) if the termination occurs within the period described in paragraph (c)(2)(i) of this section and before the power has been exercised. Ordinarily, a disclaimer made by a person not under any legal disability will be considered irrevocable when filed with the probate court. A disclaimer is a complete and unqualified refusal to accept the rights to which one is entitled. Thus, if a beneficiary uses these rights for his own purposes, as by receiving a consideration for his formal disclaimer, he has not refused the rights to which he was entitled. There can be no disclaimer after an acceptance of these rights, expressly or impliedly. The disclaimer of a power is to be distinguished from the release or exercise of a power. The release or exercise of a power by the donee of the power in favor of a person or object described in paragraph (a) of §20.2055-1 does not result in any deduction under section 2055 in the estate of the donor of a power (but see paragraph (b)(1) of §20.2055-1 with respect to the donee's estate).

Par. 5. Section 20.2056 (a)-1 (a) is amended by removing the phrase

“§20.2056(d)–1 states special rules concerning disclaimers of interests in property;” from the last sentence and inserting in its place “§§20.2056(d)–1 and 20.2056 (d)–2 state special rules concerning disclaimers of interests in property;”.

Par. 6. Section 20.2056(a)–1(b)(2) is amended by adding “§20.2056(d)–2” to follow “§20.2056(d)–1.”

Par. 7. Section 20.2056(d)–1 is revised to read as set forth below, and a new §20.2056(d)–2 is added to read as set forth below:

20.2056(d)–1 Marital deduction; effect of disclaimers of post-December 31, 1976 transfers.

(a) *Disclaimer by a surviving spouse.* If a surviving spouse disclaims an interest in property passing to such spouse from the decedent in a taxable transfer made after December 31, 1976, the efficacy of the disclaimer will be determined by section 2518 and the corresponding regulations. If a qualified disclaimer is determined to have beem made by the surviving spouse, the property interest disclaimed is treated as if such interest had never been transferred to the surviving spouse.

(b) *Disclaimer by a person other than a surviving spouse.* If an interest in property passes to one other than the surviving spouse from a decedent in a taxable transfer made after December 31, 1976 and—

(1) The person other than the surviving spouse makes a qualified disclaimer with respect to such interest in property, and

(2) The surviving spouse is entitled to such interest in property as a result of such disclaimer.

the disclaimed interest is treated as passing directly from the decedent to the surviving spouse. If the disclaimer is not a qualified disclaimer, the interest in property is considered as passing from the decedent to the person who made the disclaimer as if the disclaimer had not been made. See section 2518 and the corresponding regulations for rules relating to a qualified disclaimer.

§20.2056(d)–2. Marital deduction; effect of disclaimers of pre-January 1, 1977 transfers.

(a) *Disclaimer by a surviving spouse.* If an interest in property passes to a decedent's surviving spouse in a taxable transfer made by a decedent dying before January 1, 1977, and the decedent's surviving spouse makes a disclaimer of this property interest the disclaimed interest is considered as passing from the decedent to the person or persons entitled to receive the interest as a result of the disclaimer. A disclaimer is a complete and unqualified refusal to accept the rights to which one is entitled. It is, therefore, necessary to distinguish between the surviving spouse's disclaimer of a property interest and such surviving spouse's acceptance and subsequent disposal of a property interest. For example, if proceeds of insurance are payable to the surviving spouse and the proceeds are refused so that they consequently pass to an alternate beneficiary designated by the decedent, the proceeds are considered as having passed from the decedent to the alternate beneficiary. On the other hand, if the insurance company is directed by the surviving spouse to hold the proceeds at interest during such spouse's life and, upon this spouse's death, to pay the principal sum to another person designated by the surviving spouse, thus affecting a transfer of a remainder interest, the proceeds are considered as having passed from the decedent to the surviving spouse. See paragraph (c) of §20.2056(e)–2 with respect to a spouse's exercise or failure to exercise a right to take against a decedent's will.

(b) *Disclaimer by a person other than a surviving spouse*—(1) *Decedents dying after October 3, 1966 and before January 1, 1977.* This paragraph (b)(1) applies in the case of a disclaimer of property passing to one other than the surviving spouse from a decedent dying after October 3, 1966 and before January 1, 1977. If a surviving spouse is entitled to receive property from the decedent as a result of the timely disclaimer made by the disclaimant, the property received by the surviving spouse is to be treated as passing to the surviving spouse from the decedent. Both a disclaimer of property passing by the laws of intestacy or otherwise, as by insurance or by trust, and a disclaimer of bequests and devises under the will of a decedent are to be fully effective for purposes of computing the marital deduction under section 2056. A disclaimer is a complete and unqualified refusal to accept some or all of the rights to which one is entitled. It must be a valid refusal under State law and must be made without consideration. For example, a disclaimer for the benefit of a surviving spouse who promises to give or bequeath property to a child of the person who disclaims is not a disclaimer within the meaning of this paragraph (b)(1). The disclaimer must be made before the person disclaiming accepts any property under the disclaimed interest. In the case of property transferred by a decedent dying after December 31, 1970, and before January 1, 1977, the disclaimer must be made within 9 months after the decedent's death (or within any extension of time for filing the estate tax return granted pursuant to section 6081). In the case of property transferred by a decedent dying after October 3, 1966, and before January 1, 1971, the disclaimer must be made within 15 months after the decedent's death (or within any extension of time for filing the estate tax return granted pursuant to section 6061). If the disclaimer does not satisfy the requirements of this paragraph (b)(1), for the purpose of the marital deduction, the property is considered as passing from the decedent in the person who made the disclaimer as if the disclaimer had not been made.

(2) *Decedents dying after September 30, 1963 and before October 4, 1966.* This paragraph (b)(2) applies in the case of a disclaimer of property passing to one other than the surviving spouse from a decedent dying after September 30, 1963 and before October 4, 1966. If, as a result of the disclaimer by the disclaimant, the surviving spouse is entitled to receive the disclaimed property interest, then such interest shall, for the purposes of this paragraph (b)(2), be considered as passing from the decedent to the surviving spouse if the following conditions are met. First, the interest disclaimed was bequeathed or devised to the disclaimant. Second, the disclaimant disclaimed all bequests and devises under the will before the date prescribed for the filing of the estate tax return. Third, the disclaimant did not accept any property under the bequest or devise before making the disclaimer. The interests passing by disclaimer to the surviving spouse under this paragraph (b)(2) are to qualify for the marital deduction only to the extent that, when added to any other allowable marital deduction without regard to this paragraph (b)(2), they do not exceed the greater of the deductions which would be allowable for the marital deduction without regard to the disclaimer if the surviving spouse exercised the election under State law to take against the will, or an amount equal to one-third of the decedent's adjusted gross estate. If the disclaimer does not satisfy the requirements of this paragraph (b)(2), the

property is treated as passing from the decedent to the person who made the disclaimer, in the same manner as if the disclaimer had not been made.

(3) *Decedents dying before October 4, 1966.* Unless the rule of paragraph (b)(2) of this section applies, this paragraph (b)(3) applies in the case of a disclaimer of property passing to one other than the surviving spouse from a decedent dying before October 4, 1966. For the purpose of these transfers, it is unnecessary to distinguish for the purpose of the marital deduction between a disclaimer by a person other than the surviving spouse and a transfer by such person. If the surviving spouse becomes entitled to receive an interest in property from the decedent as a result of a disclaimer made by some other person, the interest is, nevertheless, considered as having passed from the decedent, not to the surviving spouse, but to the person who made the disclaimer, as though the disclaimer had not been made. If, as a result of a disclaimer made by a person other than the surviving spouse, a property interest passes to the surviving spouse under circumstances which meet the conditions set forth in §20.2056(b)-3 (relating to a life estate with a power of appointment), the rule stated in the preceding sentence applies, not only with respect to the portion of the interest which beneficially vests in the surviving spouse, but also with respect to the portion over which such spouse acquires a power to appoint. The rule applies also in the case of proceeds under a life insurance, endowment, or annuity contract which, as a result of a disclaimer made by a person other than the surviving spouse, are held by the insurer subject to the conditions set forth in §20.2056(b)-6.

Gift Tax Regulations

Par 8. The authority citation for Part 25 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 9. Section 25.2511-1 (c) is revised to read as follows:

§26.2511-1 Transfers in general.

* * * * *

(c)(1) The gift tax also applies to gifts indirectly made. Thus, any transaction in which an interest in property is gratuitously passed or conferred upon another, regardless of the means or device employed, constitutes a gift subject to tax. See further §25.2512-8 relating to transfers for insufficient consideration. However, in the case of a taxable transfer creating an interest in the person disclaiming made after December 31, 1976, this paragraph (c)(1) shall not apply to the donee if, as a result of a qualified disclaimer by the donee, the property passes to a different donee. Nor shall it apply to a donor if, as a result of a qualified disclaimer by the donee, a completed transfer of an interest in property is not effected. See section 2518 and the corresponding regulations for rules relating to a qualified disclaimer.

(2) In the case of taxable transfers creating an interest in the person disclaiming made before January 1, 1977, where the law governing the administration of the decedent's estate gives a beneficiary, heir, or next-of-kin a right completely and unqualifiedly to refuse to accept ownership of property transferred from a decedent (whether the transfer is effected by the decedent's will or by the law of descent and distribution) a refusal to accept ownership does not constitute the making of a gift if the refusal is made within a reasonable time after knowledge of the existence of the transfer. The refusal must be unequivocal and effective under the local law. There can be no refusal of ownership of property after its acceptance. In the absence of the facts to the contrary, if a person fails to refuse to accept a transfer to him of ownership of a decedent's property within a reasonable time after learning of the existence of the transfer, he will be presumed to have accepted the property. Where the local law does not permit such a refusal, any disposition by the beneficiary, heir, or next-of-kin whereby ownership is transferred gratuitously to another constitutes the making of a gift by the beneficiary, heir, or next-of-kin. In any case where a refusal is purported to relate to only a part of the property, the determination of whether or not there has been a complete and unqualified refusal to accept ownership will depend on all the facts and circumstances in each particular case, taking into account the recognition and effectiveness of such a purported refusal under the local law. In illustration, if Blackacre was devised to A under the decedent's will (which also provided that all lapsed legacies and devises shall go to B, the residuary beneficiary), and under the local law A could refuse to accept ownership in which case title would be considered as never having passed to A. A's refusal to accept Blackacre within a reasonable time of learning of the devise will not constitute the making of a gift by A to B. However, if a decedent who owned Greenacre died intestate with C and D as his only heirs, and under local law the heir of a decedent cannot, by refusal to accept, prevent himself from becoming an owner of intestate property, any gratuitous disposition by C (by whatever term it is known) whereby he gives up his ownership of a portion of Greenacre and D acquires the whole thereof constitutes the making of a gift by C to D.

* * * * *

Par 10. Section 25.2514-3(c) is amended by adding headings to paragraphs (c)(1) through (c)(4), by revising paragraph (c)(5), and by adding a new paragraph (c)(6). The added and revised provisions of §25.2514-3(c) read as follows:

§29.2514-3 Powers of appointment created after October 21, 1942.

* * * * *

(c) *Partial releases, lapses, and disclaimers of general powers of appointment created after October 21, 1942*—(1) *Partial release of power.* * * *

(2) *Power partially released before June 1, 1951.* * * *

(3) *Power partially released after May 31, 1951.* * * *

(4) *Release or lapse of power.* * *

(5) *Disclaimer of power created after December 31, 1976.* A disclaimer or renunciation of a general power of appointment created in a taxable transfer after December 31, 1976, in the person disclaiming is not considered a release of the power for gift tax purposes if the disclaimer or renunciation is a qualified disclaimer as described in section 2518 and the corresponding regulations. If the disclaimer or renunciation is not a qualified disclaimer, it is considered a release of the power.

(6) *Disclaimer of power created before January 1, 1977.* A disclaimer or renunciation of a general power of appointment created in a taxable transfer before January 1, 1977, in the person disclaiming is not considered a release of the power. The disclaimer or renunciation must be unequivocal and effective under local law. A disclaimer is a complete and unqualified refusal to accept the rights to which one is entitled. There can be no disclaimer or renunciation of a power after its acceptance. In the absence of facts to the contrary, the failure to renounce or disclaim within a reasonable time after learning of the existence of a power shall be

presumed to constitute an acceptance of the power. In any case where a power is purported to be disclaimed or renounced as to only a portion of the property subject to the power, the determination as to whether there has been a complete and unqualified refusal to accept the rights to which one is entitled will depend on all the facts and circumstances of the particular case, taking into account the recognition and effectiveness of such a disclaimer under local law. Such rights refer to the incidents of the power and not to other interests of the possessor of the power in the property. If effective under local law, the power may be disclaimed or renounced without disclaiming or renouncing such other interests.

* * *

Par. 11. New §§25.2518–1, 25.2518–2, and 25.2518–3 are added immediately after §25.2517–1 to read as follows:

§25.2518–1 *Qualified disclaimers of property; In general.*

(a) *Applicability*—(1) *In general.* The rules described in §§25.2518–1 through 25.2518–3 apply to the qualified disclaimer of an interest in property which is created in the person disclaiming by a taxable transfer made after December 31, 1976. In general, a qualified disclaimer is an irrevocable and unqualified refusal to accept the ownership of an interest in property. For rules relating to the determination of when a transfer occurs, see §25.2518–2(c)(3) and (4).

(2) *Example.* The provisions of paragraph (a)(1) of this section may be illustrated by the following example:

Example. W creates an irrevocable trust on December 10, 1968, and retains the right to receive the income for life. Upon the death of W, which occurs after December 31, 1976, the trust property is distributable to W's surviving issue, *per stirpes*. The creation of the remainder interest in the trust was a taxable transfer. Therefore, section 2518 does not apply to the disclaimer of the remainder interest because the taxable transfer was made prior to January 1, 1977. If, however, W had also retained the power to designate the person or persons to receive the trust principal at her death, and as a result no taxable gift was made of the remainder interest at the time of the creation of the trust, section 2518 would apply to any disclaimer made after W's death with respect to an interest in the trust property.

(b) *Effect of a qualified disclaimer.* If a peson makes a qualified disclaimer as described in section 2518(b) and §25.2518–2, for purpose of the Federal estate, gift, and generation-skipping transfer tax provisions, the disclaimed interest in property is treated as if it had never been transferred to the person making the qualified disclaimer. Instead, it is considered as passing directly from the transferor of the property to the person entitled to receive the property as a result of the disclaimer. Accordingly, a person making a qualified disclaimer is not treated as making a gift. Similarly, the value of a decedent's gross estate for purposes of the Federal estate tax does not include the value of property with respect to which the decedent, or the decedent's executor or administrator on behalf of the decedent, has made a qualified disclaimer. If the disclaimer is not a qualified disclaimer, for the purposes of the Federal estate, gift, and generation-skipping transfer tax provisions, the disclaimer is desregarded and the disclaimant is treated as having received the interest.

(c) *Effect of local law*—(1) *In general*—(i) *Interests created before 1982.* A disclaimer of an interest created in a taxable transfer before 1982 which otherwise meets the requirements of a qualified disclaimer under section 2518 and the corresponding regulations but which, by itself, is not effective under applicable local law to divest ownership of the disclaimed property from the disclaimant and vest it in another, is nevertheless treated as a qualified disclaimer under section 2518 if, under applicable local law, the disclaimed interest in property is transferred, as a result of attempting the disclaimer, to another person without any direction on the part of the disclaimant. An interest in property will not be considered to be transferred without any direction on the part of the disclaimant if, under applicable local law, the disclaimant has any discretion (whether or not such discretion is exercised) to determine who will receive such interest. Actions by the disclaimant which are required under local law merely to divest ownership of the property from the disclaimant and vest ownership in another person will not disqualify the disclaimer for purposes of section 2518(a). See §25.2518–2(d)(1) for rules relating to the immediate vesting of title in the disclaimant.

(ii) *Interests created after 1981.* [Reserved].

(2) *Creditor's claims.* The fact that a disclaimer is voidable by the disclaimant's creditors has no effect on the determination of whether such disclaimer constitutes a qualified disclaimer. However, a disclaimer that is wholly void or that is voided by the disclaimant's creditors cannot be a qualified disclaimer.

(3) *Examples.* The provisions of paragraphs (c) (1) and (2) of this section may be illustrated by the following examples:

Example (1). F dies testate in State Y on June 17, 1978. G and H are beneficiaries under the will. The will provides that any disclaimed property is to pass to the residuary estate. H has no interest in the residuary estate. Under the applicable laws of State Y, a disclaimer must be made within 6 months of the death of the testator. Seven months after F's death, H disclaimed the real property H received under the will. The disclaimer statute of State Y has a provision stating that an untimely disclaimer will be treated as an assignment of the interest disclaimed to those persons who would have taken had the disclaimer been valid. Pursuant to this provision, the disclaimed property became part of the residuary estate. Assuming the remaining requirements of section 2518 are met, H has made a qualified disclaimer for purposes of section 2518(a).

Example (2). Assume the same facts as in example (1) except that the law of State Y does not treat an ineffective disclaimer as a transfer to alternative takers. H assigns the disclaimed interest by deed to those who would have taken had the disclaimer been valid. Under these circumstances, H has not made a qualified disclaimer for purposes of section 2518 (a) because the disclaimant directed who would receive the property.

Example (3). Assume the same facts as in example (1) except that the law of State Y requires H to pay a transfer tax in order to effectuate the transfer under the ineffective disclaimer provision. H pays the transfer tax. H has made a qualified disclaimer for purposes of section 2518(a).

(d) *Cross-reference.* For rules relating to the effect of qualified disclaimers on the estate tax charitable and marital deductions, see §§20.2055–2(c) and 20.2056(d)—1 respectively. For rules relating to the effect of a qualified disclaimer of a general power of appointment, see §20.2041–3(d).

§25.2518–2 Requirements for a qualified disclaimer.

(a) *In general.* For the purposes of section 2518(a), a disclaimer shall be a qualified disclaimer only if it satisfies the requirements of this section. In general, to be a qualified disclaimer—

(1) The disclaimer must be irrevocable and unqualified:

(2) The disclaimer must be in writing:

(3) The writing must be delivered to the person specified in paragraph (b)(2) of this section within the time limitations specified in paragraph (c)(1) of this section;

(4) The disclaimant must not have accepted the interest disclaimed or any of its benefits; and

(5) The interest disclaimed must pass either to the spouse of the decedent or to

a person other than the disclaimant without any direction on the part of the person making the disclaimer:

(b) *Writing*—(1) *Requirements.* A disclaimer is a qualified disclaimer only if it is in writing. The writing must identify the interest in property disclaimed and be signed either by the disclaimant or by the disclaimant's legal representative.

(2) *Delivery.* The writing described in paragraph (b)(1) of this section must be delivered to the transfer of the interest, the transferor's legal representative, the holder of the legal title to the property to which the interest relates, or the person in possession of such property.

(c) *Time limit*—(1) *In general.* A disclaimer is a qualified disclaimer only if the writing described in paragraph (b)(1) of this section is delivered to the persons described in paragraph (b)(2) of this section no later than the date which is 9 months after the later of—

(i) The date on which the transfer creating the interest in the disclaimant is made, or

(ii) The day on which the disclaimant attains age 21.

(2) *A timely mailing of a disclaimer treated as a timely delivery.* Although section 7502 and the regulations under that section apply only to documents to be filed with the Service, a timely mailing of a disclaimer to the person described in paragraph (b)(2) of this section is treated as a timely delivery if the mailing requirements under paragraphs (c)(1), (c)(2) and (d) of §301.7502–1 are met. Further, if the last day of the period specified in paragraph (c)(1) of this section falls on Saturday, Sunday or a legal holiday (as defined in paragraph (b) of §301.7503–1), then the delivery of the writing described in paragraph (b)(1) of this section shall be considered timely if delivery is made on the first succeeding day which is not Saturday, Sunday or a legal holiday. See paragraph (d)(3) of this section for rules applicable to the exception for the individuals under 21 years of age.

(3) *Transfer.* For purposes of the time limitation described in paragraph (c)(1)(i) of this section, the 9-month period for making a disclaimer generally is to be determined with reference to the taxable transfer creating the interest in the disclaimant. With respect to inter vivos transfers, a taxable transfer occurs when there is a completed gift for Federal gift tax purposes regardless of whether a gift tax is imposed on the completed gift. Thus, gifts qualifying for the gift tax annual exclusion under section 2503(b) are regarded as taxable transfers for this purpose. With respect to transfers made by a decedent at death or transfers which become irrevocable at death, a taxable transfer occurs upon the date of the decedent's death. However, where there is a taxable transfer of an interest for Federal gift tax purposes and such interest is later included in the transferor's gross estate for Federal estate tax purposes, the 9-month period for making a qualified disclaimer is determined with reference to the earlier taxable transfer. In the case of a general power of appointment, the holder of the power has a 9-month period after the creation of the power in which to disclaim. A person to whom any interest in property passes by reason of the exercise or lapse of a general power may disclaim such interest within a 9-month period after the exercise or lapse. In the case of a nongeneral power of appointment, the holder of the power, permissible appointees, or takers in default of appointment must disclaim within a 9-month period after the original taxable transfer that created or authorized the creation of the power. If the transfer is for the life of an income beneficiary with succeeding interests to other persons, both the life tenant and the other remaindermen, whether their interests are vested or contingent, must disclaim no later than 9 months after the original taxable transfer. In the case of a remainder interest in property which an executor elects to treat as qualified terminable interest property under section 2056(b)(7), the remainder must disclaim within 9 months of the transfer creating the interest, rather than 9 months from the date such interest is subject to tax under section 2044 or 2519. A person who receives an interest in property as the result of a qualified disclaimer of the interest must disclaim the previously disclaimed interest no later than 9 months after the date of the taxable transfer creating the interest in the proceding disclaimant. Thus, if A were to make a qualified disclaimer of a specific bequest and as a result of the qualified disclaimer the property passed as part of the residue, the beneficiary of the residue could make a qualified disclaimer no later than 9 months after the date of the testator's death. See paragraph (d)(3) of this section for the time limitation rule with reference to recipients who are under 21 years of age.

(4) *Joint property*—(i) *In general.* Except as otherwise provided in paragraph (c)(4)(ii) of this section, a qualified disclaimer under section 2518(a) of an interest or any portion of an interest in a joint tenancy or a tenancy by the entirety must be made no later than 9 months after the transfer creating the tenancy. Thus, a surviving joint tenant cannot disclaim any part of the interest, including the survivorship interest, if more than 9 months have passed since the transfer creating the joint tenancy. In addition, a joint tenant cannot make a qualified disclaimer of any portion of the joint interest attributable to consideration furnished by that tenant.

(ii) *Tenancies in real property between spouses created before 1982.* In the case of joint tenancies between spouses or a tenancy by the entirety in real property created after 1976 and before 1982 where no election was made under section 2515, the surviving spouse must make a qualified disclaimer no later than 9 months after the date of death of the first spouse to die. Such a qualified disclaimer will be effective for—

(A) The entire joint interest (except any portion attributable to consideration furnished by the surviving spouse) if the date of death of the deceased spouse is before 1982; or

(B) One-half the value of the joint interest if the date of death of the deceased spouse is after 1981.

See examples (7) and (8) under paragraph (c)(5) of this section.

(5) *Examples.* The provisions of paragraphs (c)(1) through (c)(4) of this section may be illustrated by the following examples. For purposes of the following examples, assume that all beneficiaries are over 21 years of age.

Example (1). On May 13, 1978, in a transfer which constitutes a completed gift for Federal gift tax purposes, A creates a trust in which B is given a lifetime interest in the income from the trust. B is also given a nongeneral testamentary power of appointment over the corpus of the trust. The power of appointment may be exercised in favor of any of the issue of A and B. If there are no surviving issue at B's death or if the power is not exercised, the corpus is to pass to E. On May 13, 1978, A and B have two surviving children, C and D. If A, B, C or D wishes to make a qualified disclaimer, the disclaimer must be made no later than 9 months after May 13, 1978.

Example (2). Assume the same facts as in example (1) except that B is given a general power of appointment over the corpus of the trust. B exercises the general power of appointment in favor of C upon B's death on June 17, 1989. C may make a qualified disclaimer no later than 9 months after June 17, 1989. If B had died without exercising the general power of appointment, E could have made a qualified disclaimer no later than 9 months after June 17, 1989.

Example (3). F creates a trust on April 1, 1978, in which F's child G is to receive the income from the trust for life. Upon G's death, the corpus of the trust is to pass to G's child H. If either G or H wishes to make a qualified disclaimer, it must be made no later than 9 months after April 1, 1978.

Example (4). A creates a trust on February 15, 1978, in which B is named the income beneficiary for life. The trust further provides that upon B's death the proceeds of the trust are to pass to C, if then living. If C predeceases D, the proceeds shall pass to D or D's estate. To have timely disclaimers for purposes of section 2518, B, C, and D must disclaim their respective interest no later than 9 months after February 15, 1978.

Example (5). A, a resident of State Q, dies on January 10, 1979, devising certain real property to B. The disclaimer laws of State Q requires that a disclaimer be made with a reasonable time after a transfer. B disclaims the entire interest in real property on November 10, 1979. Although B's disclaimer may be effective under State Q law, it is not a qualified disclaimer under section 2518 because the disclaimer was made later than 9 months after the taxable transfer to B.

Example (6). A creates a revocable trust on June 1, 1980, in which B and C are given the income interest for life. Upon the death of the last income beneficiary, the remainder interest is to pass to D. The creation of the trust is not a completed gift for Federal gift tax purposes, but each distribution of trust income to B and C is a completed gift at the date of distribution. B and C must disclaim each income distribution no later than 9 months after the date of the particular distribution. In order to disclaim an income distribution in the form of a check, the recipient must return the check to the trustee uncashed along with a written disclaimer. A dies on September 1, 1982, causing the trust to become irrevocable, and the trust corpus is includible in A's gross estate for Federal estate tax purposes under section 2038. If B or C wishes to make a qualified disclaimer of his income interest, he must do so no later than 9 months after September 1, 1982. If D wishes to make a qualfied disclaimer of his remainder interest, he must do so no later than 9 months after September 1, 1982.

Example (7). On March 1, 1977, H and W purchase a tract of vacant land which is conveyed to them as tenants by the entirety. The entire consideration is paid by H. H does not elect, under section 2515, to have the transaction treated as a transfer for purposes of Chapter 12. H dies on June 1, 1981. On October 1, 1981, W disclaims the property. Assuming the other requirements of section 2518(b) are satisfied, W has made a qualified disclaimer because the transfer which created W's interest is treated as not occurring until H's death since no election was made under section 2515. Had an election been made under section 2515, then W's disclaimer of any of W's interest in the property would not be a qualified disclaimer.

Example (8). Assume the same facts as in example (7) except that H dies on September 3, 1982. W has until 9 months after September 3, 1984 to make a qualfied disclaimer, but she can only make a qualified disclaimer of one-half of the joint interest.

Example (9). On July 1, 1980, B transfers $10,000 to a bank account which is held jointly by B and C. Assume the transfer is not a completed gift for Federal gift tax purposes. The funds in the bank account may be withdrawn in full by either B or C at any time. C never receives funds from the bank account. B dies on August 15, 1989, and C disclaims the amount in the bank account on October 15, 1989. Assuming the remaining requirements of section 2518(b) are satisfied, C made a qualified disclaimer under section 2518(a) because it was made no later than 9 months after the taxable transfer that created an interest in C.

Example (10). H and W reside in State X, a community property state. On April 1, 1978, H and W purchase real property with community funds. The property is not held by H and W as jointly owned property with rights of survivorship. H and W hold the property until January 3, 1985, when H dies. H devises the portion of the property to W. On March 15, 1985, W disclaims the portion of the property devised to her by H. Assuming all the other requirements of section 2518(b) have been met, W has made a qualified disclaimer of the interest devised to her by H. However, W could not disclaim the interest in the property that she acquired on April 1, 1978.

(d) *No acceptance of benefits*—(1) *Acceptance.* A qualified disclaimer cannot be made with respect to an interest in property if the disclaimant has accepted the interest or any of its benefits, expressly or impliedly, prior to making the disclaimer. Acceptance is manifested by an affirmative act which is consistent with ownership of the interest in property. Acts indicative of acceptance include using the property or the interest in property; accepting dividends, interest, or rents from the property; and directing others to act with respect to the property or interest in property. However, merely taking delivery of an instrument of title, without more, does not constitute acceptance. Moreover, a disclaimant is not considered to have accepted property merely because under applicable local law title to the property vests immediately in the disclaimant upon the death of a decedent. The acceptance of one interest in property will not, by itself, constitute an acceptance of any other separate interests created by the transferor and held by the disclaimant in the same property. In the case of residential property, held in joint tenancy by some or all of the residents, a joint tenant will not be considered to have accepted the joint interest merely because the tenant resided on the property prior to disclaiming his interest in the property. The exercise of a power of appointment to any extent by the donee of the power is an acceptance of its benefits. In addition, the acceptance of any consideration in return for making the disclaimer is an acceptance of the benefits of the entire interest disclaimed.

(2) *Fiduciaries.* If a beneficiary who disclaims an interest in property is also a fiduciary, actions taken by such person in the exercise of fiduciary powers to preserve or maintain the disclaimed property shall not be treated as an acceptance of such property or any of its benefits. Under this rule, for example, an executor who is also a beneficiary may direct the harvesting of a crop of the general maintenance of a home. A fiduciary, however, cannot retain a wholly discretionary power to direct the enjoyment of the disclaimed interest. For example, a fiduciary's disclaimer of a beneficial interest does not meet the requirements of a qualified disclaimer if the fiduciary exercised or retains a discretionary power to allocate enjoyment of that interest amoung members of a designated class. See paragraph (a) of this section for rules relating to the effect of directing the redistribution of disclaimed property.

(3) *Under 21 years of age.* A beneficiary who is under 21 years of age has until 9 months after his twenty-first birthday in which to make a qualified disclaimer of his interest in property. Any action taken with regard to an interest in property by a beneficiary or a custodian prior to the beneficiary's twenty-first birthday will not be an acceptance by the beneficiary of the interest.

(4) *Examples.* The provisions of paragraph (d)(1), (2) and (3) of this section may be illustrated by the following examples:

Example (1). On April 9, 1977. A established a trust for the benefit of B, then age 22. Under the terms of the trust, the current income of the trust is to be paid quarterly to B. Additionally, one half the principal is to be distributed to B when B attains the age of 30 years. The balance of the principal is to be distributed to B when B attains the age of 40 years. Pursuant to the terms of the trust. B received a distribution of income on June 30, 1977. On August 1, 1977, B disclaimed B's right to receive both the income from the trust and the principal of the trust. B's disclaimer of the income interest is not a qualified disclaimer for purposes of section 2518(a) because B accepted income prior to making the disclaimer. B's disclaimer of the principal however, does satisfy section 2518(b)(3). See also §25.2518–3 for rules relating to the disclaimer of less than an entire interest in property.

Example (2). B is the recipient of certain property devised to B under the will of A. The will stated that any disclaimed property was to pass to C. B and C entered into negotiations in which it was decided that B would disclaim all interest in the real property that was devised to B. In exchange, C promised to let B live in the family home for life. B's disclaimer is not a qualified disclaimer for purposes of section 2518(a) because B accepted consideration for making the disclaimer.

Example (3). A received a gift of Blackacre on December 25, 1978. A never resided on Blackacre but when property taxes on Blackacre became due on July 1, 1979, A paid them out of personal funds. On August 15, 1979, A disclaimed the gift of Blackacre. Assuming all the requirements of section 2518 (b) have been met, A has made a qualified disclaimer of Blackacre. Merely paying the properly taxes does not consitute an acceptance of Blackacre even though A's personal funds were used to pay the taxes.

Example (4). A died on February 15, 1978. Pursuant to A's will, B received a farm in State Z. B requested the excutor to sell the farm and to give the proceeds to B. The executor then sold the farm pursuant to B's request. B then disclaimed $50,000 of the proceeds from the sale of the farm. B's disclaimer is not a qualified disclaimer. By requesting the executor to sell the farm B accepted the farm even though the executor may not have been legally obligated to comply with B's request. See also §25.2518–3 for rules relating to the disclaimer of less than an entire interest in property.

Example (5). Assume the same facts as in example (4) except that instead of requesting the executor to sell the farm, B pledged the farm as security for a short-term loan which was paid off prior to distribution of the estate. B then disclaimed his interest in the farm. B's disclaimer is not a qualified disclaimer. By pledging the farm as security for the loan, B accepted the farm.

Example (6). A delivered 1,000 shares of stock in Corporation X to B as a gift on February 1, 1980. A had the shares registered in B's name on that date. On April 1, 1980, B disclaimed the interest in the 1,000 shares. Prior to making the disclaimer, B did not pledge the shares, accept any dividends or otherwise commit any acts indicative of acceptance. Assuming the remaining requirements of section 2518 are satisfied, B's disclaimer is a qualified disclaimer.

Example (7). On January 1, 1980, A created an irrevocable trust in which B was given a testamentary general power of appointment over the trust's corpus. B executed a will on June 1, 1980, in which B provided for the exercise of the power of appointment. On September 1, 1980, B disclaimed the testamentary power of appointment. Assuming the remaining requirements of section 2518 (b) are satisfied, B's disclaimer of the testamentary power of appointment is a qualified disclaimer.

Example (8). H and W reside in X, a community property state. On January 1, 1981, H and W purchase a residence with community funds. They continued to reside in the house until H dies testate on February 1, 1990. Although H could devise his portion of the residence to any person, H devised his portion of the residence to W. On September 1, 1990, W disclaims the portion of the residence devised to her pursuant to H's will but continues to live in the residence. Assuming the remaining requirements of section 2518 (b) are satisfied, W's disclaimer is a qualified disclaimer under section 2518 (a). W's continued occupancy of the house prior to making the disclaimer will not by itself be treated as an acceptance of the benefits of the portion of the residence devised to her by H.

Example (9). In 1979, D established a trust for the benefit of D's minor children E and F. Under the terms of the trust, the trustee is given the power to make discretionary distributions of current income and corpus to both children. The corpus of the trust is to be distributed equally between E and F when E becomes 35 years of age. Prior to attaining the age of 21 years on April 8, 1982, E receives several distributions of income from the trust. E receives no distributions of income between April 8, 1982 and August 15, 1982, which is the date on which E disclaims all interest in the income from the trust. As a result of the disclaimer the income will be distributed to F. If the remaining requirements of section 2518 are met, E's disclaimer is a qualified disclaimer under section 2518(a). To have a qualified disclaimer of the interest in corpus, E must disclaim the interest no later than 9 months after April 8, 1982, E's 21st birthday.

Example (10). Assume the same facts as in example (9) except that E accepted a distribution of income on May 13, 1982. E's disclaimer is not a qualified disclaimer under section 2518 because by accepting an income distribution after attaining the age of 21, E accepted benefits from the income interest.

Example (11). F made a gift of 10 shares of stock to G as custodian for H under the State X Uniform Gifts to Minors Act. At the time of the gift, H was 15 years old. At age 18, the local age of majority, the 10 shares were deliverd to and registered in the name of H. Between the receipt of the shares and H's 21st birthday, H received dividends from the shares. Within 9 months of attaining age 21, H disclaimed the 10 shares. Assuming H did not accept any dividends from the shares after attaining age 21, the disclaimer by H is a qualified disclaimer under section 2518.

(e) *Passage without direction by the disclaimant of beneficial enjoyment of disclaimed interest.*

(1) *In general.* A disclaimer is not a qualified disclaimer unless the disclaimed interest passes without any direction on the part of the disclaimant to a person other than the disclaimant (except as provided in paragraph (e)(2) of this section. If there is an express or implied agreement that the disclaimed interest in property is to be given or bequeathed to a person specified by the disclaimant, the disclaimant shall be treated as directing the transfer of the property interest. The requirements of a qualified disclaimer under section 2518 are not satisified if—

(i) The disclaimant, either alone or in conjunction with another, directs the redistribution or transfer of the property or interest in property to another person (or has the power to direct the redistribution or transfer of the property or interest in property to another person unless such power is limited by an ascertainable standard); or

(ii) The disclaimed property or interest in property passes to or for the benefit of the disclaimant as a result of the disclaimer (except as provided in paragraph (e)(2) of this section).

If a power of appointment is disclaimed, the requirements of this paragraph (e)(1) are satisfied so long as there is no direction on the part of the disclaimant with respect to the transfer of the interest subject to the power or with respect to the transfer of the power to another person. A person may make a qualified disclaimer of a beneficial interest in property even if after such disclaimer the disclaimant has a fiduciary power to distribute to designated beneficiaries, but ony if the power is subject to an ascertainable standard. See examples (11) and (12) of paragraph (e) (5) of this section.

(2) *Disclaimer by surviving spouse.* In the case of a disclaimer made by a decedent's surviving spouse with respect to property transferred by the decedent, the disclaimer satisfies the requirements of this paragraph (e) if the interest passes as a result of the disclaimer without direction on the part of the surviving spouse either to the surviving spouse or to another person. If the surviving spouse, however, retains the right to direct the beneficial enjoyment of the disclaimed property in a transfer that is not subject to Federal estate and gift tax (whether as trustee or otherwise), such spouse will be treated as directing the beneficial enjoyment of the disclaimed property, unless such power is limited by an ascertainable standard. See examples (4), (5), and (6) in paragraph (e)(5) of this section.

(3) *Partial failure of disclaimer.* If a disclaimer made by a person other than the surviving spouse is not effective to pass completely an interest in property to a person other than the disclaimant because—

(i) The disclaimant also has a right to receive such property as an heir at law, residuary beneficiary, or by any other means; and

(ii) The disclaimant does not effectively disclaim these rights, the disclaimer is not a qualified disclaimer with respect to the portion of the disclaimed property which the disclaimant has a right to receive. If the portion of the disclaimed interest in property which the disclaimant has a right to receive is not severable property or an undivided portion of the property, then the disclaimer is not a qualified disclaimer with respect to any portion of the property. Thus, for example, if a disclaimant who is not a surviving spouse receives a specific bequest of a fee simple interest in property and as a result of the disclaimer of the entire interest, the property passes to a trust in which the disclaimant has a remainder interest, then the disclaimer will not be a qualified disclaimer unless the remainder interest in the property is also disclaimed. See §25.2518–3 (a) (1) (ii) for the definition of severable property.

(4) *Effect of precatory language.* Precatory language is a disclaimer naming takers of disclaimed property will not be considered as directing the redistribution or transfer of the property or interest in property to such persons if the applicable State law gives the language no legal effect.

(5) *Examples*. The provisions of this paragraph (e) may be illustrated by the following examples:

Example (1). A, a resident of State X, died on July 30, 1978. Pursuant to A's will, B, A's son and heir at law, received the family home. In addition, B and C each received 50 percent of A's residuary estate. B disclaimed the home. A's will made no provision for the distribution of property in the case of a beneficiary's disclaimer. Therefore, pursuant to the disclaimer laws of State X, the disclaimed property became part of the residuary estate. Because B's 50 percent share of the residuary estate will be increased by 50 percent of the value of the family home, the disclaimed property will not pass solely to another person. Consequently, B's disclaimer of the family home is a qualified disclaimer only with respect to the 50 percent portion that passes solely to C. Had B also disclaimed B's 50 percent interest in the residuary estate, the disclaimer would have been a qualified disclaimer under section 2518 of the entire interest in the home (assuming the remaining requirements of a qualified disclaimer were satisfied). Similarly, if under the laws of State X, the disclaimer has the effect of divesting B of all interest in the home, both as devisee and as a beneficiary of the residuary estate, including any property resulting from its sale, the disclaimer would be a qualified disclaimer of B's entire interest in the home.

Example (2). D, a resident of State Y, died testate on June 30, 1978. E, an heir at law of D, received specific bequests of certain severable personal property from D. E disclaimed the property transferred by D under the will. The will made no provision for the distribution of property in the case of a beneficiary's disclaimer. The disclaimer laws of State Y provide that such property shall pass to the decedent's heirs at law in the same manner as if the disclaiming beneficiary had died immediately before the testator's death. Because State Y's law treats E as predeceasing D, the property disclaimed by E does not pass to E as an heir at law or otherwise. Consequently, if the remaining requirements of section 2518(b) are satisfied, E's disclaimer is a qualified disclaimer under section 2518 (a).

Example (3). Assume the same facts as in example (2) except that State Y has no provision treating the disclaimant as predeceasing the testator. E's disclaimer satisfies section 2518 (b)(4) only to the extent that E does not have a right to receive the property as an heir at law. Had E disclaimed both the share E received under D's will and E's intestate share, the requirement of sectioa 2518 (b)(4) would have been satisfied.

Example (4). B died testate on February 13, 1980. B's will established both a marital trust and a nonmarital trust. The decedent's surviving spouse, A, is an income beneficiary of the marital trust and has a testamentary general power of appointment over its assets. A is also an income beneficiary of the nonmarital trust, but has no power to appoint or invade the corpus. The provisions of the will specify that any portion of the marital trust disclaimed is to be added to the nonmarital trust. A disclaimed 30 percent of the marital trust. (See §25.2518–3(b) for rules relating to the disclaimer of an undivided portion of an interest in property.) Pursuant to the will, this portion of the marital trust property was transferred to the nonmarital trust without any direction on the part of A. This disclaimer by A satisfies section 2518 (b)(4).

Example (5). Assume the same facts as in example (4) except that A, the surviving spouse, has both an income interest in the nonmarital trust and a testamentary nongeneral power to appoint amount designated beneficiaries. This power is not limited by an ascertainable standard. The requirements of section 2518 (b)(4) are not satisfied unless A also disclaims the non-general power to appoint the portion of the trust corpus that is attributable to the property that passed to the nonmarital trust as a result of A's disclaimer. Assuming that the fair market value of the disclaimed property on the date of the disclaimer is $250,000 and that the fair market value of the nonmarital trust (including the disclaimed property) immediately after the disclaimer is $750,000, A must disclaim the power to appoint one-third of the nonmarital trust's corpus. The result is the same regardless of whether the nongeneral power is testamentary or inter vivos.

Example (6). Assume the same facts as in example (4) except that A has both an income interest in the nonmarital trust and a power to invade corpus if needed for A's health or maintenance. In addition, an independent trustee has power to distribute to A any portion of the corpus which the trustee determines to be desirable for A's happiness. Assuming the other requirements of section 2518 are satisfied, A may make a qualified disclaimer of interests in the marital trust without disclaiming any of A's interests in the nonmarital trust.

Example (7). B died testate on June 1, 1980. B's will created both a marital trust and a nonmarital trust. The decedent's surviving spouse, C, is an income beneficiary of the marital trust and has a testamentary general power of appointment over its assets. C is an income beneficiary of the nonmarital trust, and additionally has the noncumulative right to withdraw yearly the greater of $5,000 or 5 percent of the aggregate value of the principal. The provisions of the will specify that any portion of the marital trust disclaimed is to be added to the nonmarital trust. C disclaims 50 percent of the marital trust corpus. Pursuant to the will, this amount is transferred to the nonmarital trust. Assuming the remaininag requirements of section 518(b) are satisfied, C's disclaimer is a qualified disclaimer.

Example (8). A, a resident of State X, died on July 19, 1979. A was survived by a spouse B, and three children, C, D, and E. Pursuant to A's will, B received one-half of A's estate and the children received equal shares of the remaining one-half of the estate. B disclaimed the entire interest B had received. The will made no provisions for the distribution of property in the case of a beneficiary's disclaimer. The disclaimer laws of State X provide that under these circumstances disclaimed property passes to the decedent's heirs at law in the same manner as if the disclaiming beneficiary had died immediately before the testator's death. As a result, C, D, and E are A's only remaining heirs at law, and will divide the disclaimed property equally among themselves. B's disclaimer includes language stating that "it is my intention, that C, D, and E will share equally in the division of this property as a result of my disclaimer. "State X considers these to be precatory words and gives them no legal effect. B's disclaimer meets all other requirements imposed by State X on disclaimers, and is considered as effective disclaimer under which the property will vest solely in C, D, and E in equal shares without any further action required by B. Therefore, B is not treated as directing the redistribution or transfer of the property. If the remaining requirements of section 2518 are met, B's disclaimer is a qualified disclaimer.

Example (9). C died testate on January 1, 1979. According to C's will, D was to receive ⅓ of the residuary estate with any disclaimed property going to E. D was also to receive a second ⅓ of the residuary estate with any disclaimed property going to F. Finally, D was to receive a final ⅓ of the residuary estate with any disclaimed property going to G. D specifically states that he is disclaiming the interest in which the disclaimed property is designated to pass to E. D has effectively directed that the disclaimed property will pass to E and therefore D's disclaimer is not a qualified disclaimer under section 2518(a).

Example (10). Assume the same facts as in example (9) except the C's will also states that D was to receive Blackacre and Whiteacre. C's will further provides that if D disclaimed Blackacre then such property was to pass to E and that if D disclaimed Whiteacre then Whiteacre was to pass to F. D specifically disclaims Blackacre with the intention that it pass to E. Assuming the other requirments of section 2518 are met, D has made a qualified disclaimer of Blackacre. Alternatively, D could disclaim an undivided disclaimer of Blackacre. Alternatively, D could disclaim an undivided portion of both Blackacre and Whiteacre. Assuming the other requirements of section 2518 are met, this would also be a qualified disclaimer.

Example (11). G creates an irrevocable trust on February 16, 1983, naming H, I and J as the income beneficiaries for life and F as the remainderman. F is also named the trustee and as trustee has the discretionary power to invade the corpus and make discretionary distributions to H, I or J during their lives. F disclaims the remainder interest on August 8, 1983, but retains his discretionary power to invade the corpus. F has not made a qualified disclaimer because F retains the power to direct enjoyment of the corpus and the retained fiduciary power is not limited by an ascertainable standard.

Example (12). Assume the same facts as in example (11) except that F may only invade the corpus to make distributions for the health, maintenance or support of H, I or J during their lives. If the other requirements of section 2518(b) are met, F has made a qualified disclaimer of the remainder interest because the retained fiduciary power is limited by an ascertainable standard.

§25.2518–3 Disclaimer of less than an entire interest.

(a) *Disclaimer of a partial interest*—(1) *In general*—(i) *Interest.* If the requirements of this section are met, the disclaimer of all or an undivided portion of any separate interest in property may be a qualified disclaimer even if the disclaimant has another interest in the same property. In general, each interest in property that is separately created by the transferor is treated as a separate interest. For example, if an income interest in securities is bequeathed to A for life, then to B for life, with the remainder interest in such securities bequeathed to A's estate, and if the remaining requirements of section 2518(b) are met, A could make a qualified disclaimer of either the income interest of the remainder, or an undivided portion of either interest. A could not, however, make a qualified disclaimer of the income interest for a certain number of years. Further, where local law merges interests separately created by the transferor, a qualified disclaimer will be allowed only if there is a disclaimer of the entire merged interest or an undivided portion of such merged interest. See example (12) in paragraph (d) of this section. See §25.2518–3(b) for rules relating to the disclaimer of an undivided portion. Where the merger of separate interests would occur but for the creation by the transferor of a nominal interest (as defined in paragraph (a)(1)(iv) of this section), a qualified disclaimer will be allowed only if there is a disclaimer of all the separate interests, or an undivided portion of all such interests, which would have merged but for the nominal interest.

(ii) *Severable property.* A disclaimant shall be treated as making a qualified disclaimer of a separate interest in property if the disclaimer relates to severable property and the disclaimant makes a disclaimer which would be a quailfied disclaimer if such property were the only property in which the disclaimant had an interest. If applicable local law does not recognize a purported disclaimer of severable property, the disclaimant must comply with the requirements of paragraph (c)(1) of §25.2518–1 in order to make a qualified disclaimer of the severable property. Severable property is property which can be divided into separate parts each of which, after severance, maintains a complete and independent existence. For example, a legatee of shares of corporate stock may accept some shares of the stock and make a qualified disclaimer of the remaining shares.

(iii) *Powers of appointment.* A power of appointment with respect to property is treated as a separate interest in such property and such power of appointment with respect to all or undivided portion of such property may be disclaimed independently from any other interests separately created by the transferor in the property if the requirements of section 2518(b) are met. See example (21) of paragraph (d) of this section. Further, a disclaimer of a power of appointment with respect to property is a qualified disclaimer only if any right to direct the beneficial enjoyment of the property which is retained by the disclaimant is limited by an ascertainable standard. See example (9) of paragraph (d) of this section.

(iv) *Nominal interest.* A nominal interest is an interest in property created by the transferor that—

(A) Has an actuarial value (as determined under §20.2031–10) of less than 5 percent of the total value of the property at the time of the taxable transfer creating the interest,

(B) Prevents the merger under local law of two or more other interests created by the transferor, and

(C) Can be clearly shown from all the facts and circumstances to have been created primarily for the purpose of preventing the merger of such other interests.

Factors to be considered in determining whether an interest is created primarily for the purpose of preventing merger include (but are not limited to) the following: the relationship between the transferor and the interest holder; the age difference between the interest holder and the beneficiary whose interests would have merged; the interest holder's state of health at the time of the taxable transfer; and, in the case of a contingent remainder, any other factors which indicate that the possibility of the interest vesting as a fee simple is so remote as to be negligible.

(2) *In trust.* A disclaimer is not a qualified disclaimer under section 2518 if the beneficiary disclaims income derived from specific property transferred in trust while continuing to accept income derived from the remaining properties in the same trust unless the disclaimer results in such property being removed from the trust and passing, without any direction on the part of the disclaimant, to persons other than the disclaimant or to the spouse of the decedent. Moreover, a disclaimer of both an income interest and a remainder interest in specific trust assets is not a qualified disclaimer if the beneficiary retains interest in other trust property unless, as a result of the disclaimer, such assets are removed from the trust and pass, without any direction on the part of the disclaimant, to persons other than the disclaimant or to the spouse of the decedent. The disclaimer of an undivided portion of an interest in a trust may be a qualified disclaimer. See also paragraph (b) of this section for rules relating to the disclaimer of an undivided portion of an interest in property.

(b) *Disclaimer of undivided portion.* A disclaimer of an undivided portion of a separate interest in property which meets the other requirements of a qualified disclaimer under section 2518(b) and the corresponding regulations is a qualified disclaimer. An undivided portion of a disclaimant's separate interest in property must consist of a fraction or percentage of each and every substantial interest or right owned by the disclaimant in such property and must extend over the entire term of the disclaimant's interest in such property and in other property into which such property is converted. A disclaimer of some specific rights while retaining other rights with respect to an interest in the property is not a qualified disclaimer of an undivided portion of the disclaimant's interest in property. Thus, for example, a disclaimer made by the devisee of a fee simple interest in Blackacre is not a qualified disclaimer if the disclaimant disclaims a remainder interest in Blackacre but retains a life estate.

(c) *Disclaimer of a pecuniary amount.* A disclaimer of a specific pecuniary amount out of a pecuniary or nonpecuniary bequest or gift which satisfies the other requirements of a qualified disclaimer under section 2518(b) and the corresponding regulations is a qualified disclaimer provided that no income or other benefit of the disclaimed amount inures to the benefit of the disclaimant either prior to or subsequent to the disclaimer. Thus, following the disclaimer of a specific pecuniary amount from a bequest or gift, the amount disclaimed and any income attributable to such amount must be segregated from the portion of the gift or bequest that was not disclaimed. Such a segregation of assets making up the disclaimer of a pecuniary amount must be made on the basis of the fair market value of the assets on the date of the disclaimer or on a basis that is fairly representative of value changes that may have occurred between the date of transfer and the date of the disclaimer. A pecuniary amount distributed to the disclaimant from the bequest or gift prior to the disclaimer shall be treated as a distribution of corpus from the bequest or gift. However, the acceptance of a distribution from the gift or bequest shall also be considered to be an acceptance of a proportionate amount of income earned by the bequest or gift. The proportionate share of income considered to be accepted by the disclaimant shall be determined at the time of the disclaimer according to the following formula:

$$\frac{\text{total amount of distributions received by the disclaimant out of the gift or bequest}}{\text{total value of the gift or bequest on the date of transfer}} \times \text{total amount of income earned by the gift or bequest between date of transfer and date of disclaimer.}$$

See examples (17), (18), and (19) in §25.2518–3(d) for illustrations of the rules set forth in this paragraph (c).

(d) *Examples.* The provisions of this section may be illustrated by the following examples:

Example (1). A, a resident of State Q, died on August 1, 1978. A's will included specific bequests of 100 shares of stock in X corporation; 200 shares of stock in Y corporation; 500 shares of stock in Z corporation; personal effects consisting of paintings, home furnishings, jewelry, and silver, and a 500 acre farm consisting of a residence, various outbuildings, and 500 head of cattle. The laws of State Q provide that a disclaimed interest passes in the same manner as if the disclaiming beneficiary had died immediately before the testator's death. Pursuant to A's will. B was to receive both the personal effects and the farm. C was to receive all the shares of stock in Corporation X and Y and D was to receive all the shares of stock in Corporation Z. B disclaimed 2 of the paintings and all the jewelry, C disclaimed 50 shares of Y corporation stock, and D disclaimed 100 shares of Z corporation stock. If the remaining requirements of section 2518(b) and the corresponding regulations are met, each of these disclaimers is a qualified disclaimer for purposes of section 2518(a).

Example (2). Assume the same facts as in example (1) except that D disclaimed the income interest in the shares of Z corporation stock while retaining the remainder interest in such shares. D's disclaimer is not a qualified disclaimer.

Example (3). Assume the same facts as in example (1) except that B disclaimed 300 identified acres of the 500 acres. Assuming that B's disclaimer meets the remaining requirements of section 2518(b), it is a qualified disclaimer.

Example (4). Assume the same facts as in example (1) except that A devised the income from the farm to B for life and the remainder interest to C. B disclaimed 40 percent of the income from the farm. Assuming that it meets the remaining requirements of section 2518(b), B's disclaimer of an undivided portion of the income is a qualified disclaimer.

Example (5). E died on September 13, 1978. Under the provisions of E's will, E's shares of stock in X, Y, and Z corporations were to be transferred to a trust. The trust provides that all income is to be distributed currently to F and G in equal parts until F attains the age of 45 years. At that time the corpus of the trust is to be divided equally between F and G. F disclaimed the income arising from the shares of X stock. G disclaimed 20 percent of G's interest in the trust. F's disclaimer is not a qualified disclaimer because the X stock remains in the trust. If the remaining requirements of section 2518(b) are met, G's disclaimer is a qualified disclaimer.

Example (6). Assume the same facts as in example (5) except that F disclaimed both the income interest and the remainder interest in the shares of X stock. F's disclaimer results in the X stock being transferred out of the trust to G without any direction on F's part. F's disclaimer is a qualified disclaimer under section 2518(b).

Example (7). Assume the same facts as in example (5) except that F is only an income beneficiary of the trust. The X stock remains in the trust after F's disclaimer of the income arising from the shares of X stock. F's disclaimer is not a qualified disclaimer under section 2518.

Example (8). Assume the same facts as in example (5) except that F disclaimed the entire income interest in the trust while retaining the interest F has in corpus. Alternatively, assume that G disclaimed G's entire corpus interest while retaining G's interest in the income from the trust. If the remaining requirements of section 2518(b) are met, either disclaimer will be a qualified disclaimer.

Example (9). G creates an irrevocable trust on May 13, 1980, with H, I, and J as the income beneficiaries. In addition, H, who is the trustee, holds the power to invade corpus for H's health, maintenance, support and happiness and a testamentary power of appointment over the corpus. In the absence of the exercise of the power of appointment, the property passes to I and J in equal shares. H disclaimed the power to invade corpus for H's health, maintenance, support and happiness. Because H retained the testamentary power to appoint the property in the corpus, H's disclaimer is not a qualified disclaimer. If H also disclaimed the testamentary power of appointment, H's disclaimer would have been a qualified disclaimer.

Example (10). E creates an irrevocable trust on May 1, 1980, in which D is the income beneficiary for life. Subject to the trustee's discretion, E's children, A, B, and C, have the right to receive corpus during D's lifetime. The remainder passes to D if D survives A, B, C, and all their issue. D also holds an inter vivos power to appoint the trust corpus to A, B, and C. On September 1, 1980, D disclaimed the remainder interest. D's disclaimer is not a qualified disclaimer because D retained the power to direct the use and enjoyment of corpus during D's life.

Example (11). Under H's will, a trust is created from which W is to receive all of the income for life. The trustee has the power to invade the trust corpus for the support or maintenance of D during the life of W. The trust is to terminate at W's death, at which time the trust property is to be distributed to D. D makes a timely disclaimer of the right to corpus during W's lifetime, but does not disclaim the remainder interest. D's disclaimer is a qualified disclaimer assuming the remaining requirements of section 2518 are met.

Example (12). Under the provisions of G's will A received a life estate in a farm, and was the sole beneficiary of property in the residuary estate. The will also provided that the remainder interest in the farm pass to the residuary estate. Under local law A's interests merged to give A a fee simple in the farm. A made a timely disclaimer of the life estate. A's disclaimer of a partial interest is not a qualified disclaimer under section 2518(a). If A makes a disclaimer of the entire merged interest in the farm or an undivided portion of such merged interest than A would be making a qualified disclaimer assuming all the other requirements of section 2518(b) are met.

Example (13). A, a resident of State Z, dies on September 3, 1980. Under A's will, Blackacre is devised to C for life, then to D for 1 month, remainder to C. Had A not created D's interest, State Z law would have merged C's life estate and the remainder to C to create a fee simple interest in C. Assume that the actuarial value of D's interest is less than 5 percent of the total value of Blackacre on the date of A's death. Further assume that facts and circumstances (particularly the duration of D's interest) clearly indicate that D's interest was created primarily for the purpose of preventing the merger of C's two interests in Blackacre. D's interest in Blackacre is a nominal interest and C's two interests will, for purposes of making a qualified disclaimer, be considered to have merged. Thus, C cannot make a qualified disclaimer of his remainder while retaining the life estate. C can, however, make a qualified disclaimer of both of these interests entirely or an undivided portion of both.

Example (14). A, a resident of State X, dies on October 12, 1978. Under A's will, Blackacre was devised to B for life, then to C for life if C survives B, remainder to B's estate. On the date of A's death, B and C are both 8 year old grandchildren of A. In addition, C is in good health. The actural value of C's interest is less than 5 percent of the total value of Blackacre on the date of A's death. No facts are present which would indicate that the possibility of C's contingent interest vesting is so remote as to be negligible. Had C's contingent life estate not been created, B's life estate and remainder interests would have merged under local law to give B a fee simple interest in Blackacre. Although C's interest prevents the merger of B's two interests and has an actual value of less than 5 percent, C's interest is not a nominal interest within the meaning of §25.2518–3(a)(1)(iv) because the facts and circumstances do not clearly indicate that the interest was created primarily for the purpose of preventing the merger of other interests in the property. Assuming all the other requirements of section 2518(b) are met, B can make a qualified disclaimer of the remainder while retaining his life estate.

Example (15). In 1981, A transfers $60,000 to a trust created for the benefit of B who was given the income interest for life and who also has a testamentary nongeneral power of appointment over the corpus. A transfers an additional $25,000 to the trust on June 1, 1984. At that time the trust corpus (exclusive of the $25,000 transfer) has a fair market value of $75,000. On January 1, 1985, B disclaims the right to receive income attributable to 25 percent of the corpus

$$\frac{\text{\$25,000 (1984) transfer)}}{\begin{array}{l}\text{\$100,000 (Fair market value}\\ \quad\text{of corpus immediately}\\ \quad\text{after the 1984 transfer)}\end{array}} = 25\%$$

Assuming that no distributions were made to B attributable to the $25,000, B's disclaimer is a qualified disclaimer for purposes of section 2518(a) if all the remaining requirements of section 2518(b) are met.

Example (16). Under the provisions of B's will, A is left an outright cash legacy of $50,000 and has no other interest in B's estate. A timely disclaimer by A of any stated dollar amount is a qualified disclaimer under section 2518(a).

Example (17). D bequeaths his brokerage account to E. The account consists of stocks and bonds and a cash amount earning interest. The total value of the cash and assets in the account on the date of D's death is $100,000. Four months after D's death, E makes a withdrawal of cash from the account for personal use amounting to $40,000. Eight months after D's death, E disclaims $60,000 of the account without specifying any particular assets or cash. The cumulative fair market value of the stocks and bonds in the account on the date of the disclaimer is equal to the value of such stocks and bonds on the date of D's death. The income earned by the account between the date of D's death and the date of E's disclaimer was $20,000. The amount of income earned by the account that E accepted by withdrawing $40,000 from the account prior to the disclaimer is determined by applying the formula set forth in §25.2518–3(c) as follows:

$$\frac{\$40{,}000}{\$100{,}000} \times \$20{,}000 = \$8{,}000$$

E is considered to have accepted $8,000 of the income earned by the account. If (i) the $60,000 disclaimed by E and the $12,000 of income earned prior to the disclaimer which is attributable to that amount are segregated from the $8,000 of income E is considered to have accepted, (ii) E does not accept any benefits of the $72,000 so segregated, and (iii) the other requirements of section 2518(b) are met, then E's disclaimer of $60,000 from the account is a qualified disclaimer.

Example (18). A bequeathed his residuary estate to B. The residuary estate had a value of $1 million on the date of A's death. Six months later, B disclaimed $200,000 out of this bequest. B received distributions of all the income from the entire estate during the period of administration. When the estate was distributed, B received the entire residuary estate except for $200,000 in cash. B did not make a qualified disclaimer since he accepted the benefits of the $200,000 during the period of estate administration.

Example (19). Assume the same facts as in example (18) except that no income was paid to B and the value of the residuary estate on the date of the disclaimer (including interest earned from date of death) was $1.5 million. In addition, as soon as B's disclaimer was made, the executor of A's estate set aside assets worth $300,000

$$\frac{\$200{,}000}{\$1{,}000{,}000} \times \$1{,}500{,}000$$

and the interest earned after the disclaimer on that amount in a separate fund so that none of the income was paid to B. B's disclaimer is a qualified disclaimer under section 2518(a).

Example (20). A bequeathed his residuary estate to B. B disclaims a fractional share of the residuary estate. Any disclaimed property will pass to A's surviving spouse, W. The numerator of the fraction disclaimed is the smallest amount which will allow A's estate to pass free of Federal estate tax and the denominator is the value of the residuary estate. B's disclaimer is a qualified disclaimer.

Example (21). A created a trust on July 1, 1979. The trust provides that all current income is to be distributed equally between B and C for the life of B. B also is given a testamentary general power of appointment over the corpus. If the power is not exercised, the corpus passes to C or C's heirs. B disclaimed the testamentary power to appoint an undivided one-half of the trust corpus. Assuming the remaining requirements of section 2518(b) are satisfied, B's disclaimer is a qualified disclaimer under section 2518(a).

Par. 12. The authority citation for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 13. Section 602.101(c) is amended by inserting in the appropriate place in the table:

"§25.2518–2(b) 1545–0959".

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue.

Approved July 16, 1986.

J. ROGER MENTZ,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on August 6, 1986, 8:45 a.m., and published in the issue of the Federal Register for August 7, 1986, 51 F.R. 28365)

Part III. Administrative, Procedural, and Miscellaneous

Application of Proposed Product Grouping Rules for Purposes of the Possessions Tax Credit

Notice 86–9

The Internal Revenue Service announced today that it will grant relief under section 7805(b) with respect to the product grouping rules of the final regulations under section 936(h), which were published in the Federal Register on June 13, 1986. Under section 1.936–5(a), question and answer 9, of those regulations, products may be "grouped" only on the basis of similarities in the production processes of the products. However, under the product grouping rules provided in Proposed Regulations section 1.936–5(a), question and answer 5, which were published in the Federal Register on January 10, 1984, taxpayers were permitted to group pharmaceutical products either on the basis of similarities in the production process or on the basis of active ingredient. This notice provides that, except as provided below, for taxable years beginning before July 1, 1986, taxpayers can continue to use either grouping method with respect to pharmaceutical products. Thus, no amended return will be required if taxpayers have grouped under either method for those years.

This limited grant of Section 7805(b) relief does not affect the determination under the final regulations of whether a product is a new product for purposes of satisfying the start-up significant business presence test. Accordingly, a product will be treated as a new product only if that product could not have been grouped on the basis of similarities in the production process. Furthermore, this limited grant of 7805(b) relief does not apply for any taxable year if—

(1) The taxpayer produced a product which could have been grouped with other products under an active ingredient grouping, but

(2) That product could not have been grouped with those other products based on similarities in production process, and

(3) The taxpayer, for that year, treats, or would treat on the filing of an amended return for that year, the subject product as a new product for purposes of the start-up significant business presence test.

Those taxpayers must utilize the grouping rules of the final regulations.

Part IV. Items of General Interest

Alternative Minimum Tax Computation

Announcement 86–93

Section 13208 of Public Law 99–272, Consolidated Omnibus Budget Reconciliation Action of 1985, 1986–29 I.R.B. 4, 36, amends section 57(a)(9) of the Internal Revenue Code to allow certain insolvent taxpayers to reduce the capital gains preference item for purposes of the Individual Alternative Minimum Tax. This relief is directed towards farm insolvencies and applies to transfers, sales or exchanges of farm land made after December 31, 1981. The statute states that the taxpayer had to be insolvent (excess of liabilities over fair market value of assets) immediately prior to the transaction. If a taxpayer claims relief under these provisions, he/she should notate, "SECTION 13208 RELIEF," on the dotted line next to Item 4(b), 60 percent Capital Gain deduction, on Form 6251, Alternative Minimum Tax Computation, so that the Internal Revenue Service can properly compute the tax liability.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Wayne Boyer	Southfield, MI	Enrolled Agent	Eight Months from May 12, 1986
Thomas McPhee	McAllen, TX	Enrolled Agent	Indefinite from June 15, 1986
Glen R. Verber	Houston, TX	Certified Public Accountant	Ninety Days from May 19, 1986
Beverly Worth	Winona Lake, IN	Enrolled Agent	Five Years from June 17, 1986
Robert D. Digby	North Little Rock, AR	Certified Public Accountant	Four Months from July 29, 1986
Jeffrey E. Ellis	Rockland, ME	Certified Public Accountant	Indefinite from July 2, 1986
Charles L. Honey	Prescott, AR	Attorney	One Year from July 2, 1986
Bernhardt Karp	Hudson, NY	Attorney & Certified Public Accountant	Indefinite from July 29, 1986
George N. Meros	Springfield, MO	Attorney	Indefinite from July 25, 1986
William G. Waldrop	Adamsville, AL	Certified Public Accountant	Indefinite from July 17, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federral Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

Finding List of Current Action on Previously Published Rulings[1]

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*Denotes entry since last publication

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

NOTES

NOTES

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1986-36

Internal Revenue
bulletin

Bulletin No. 1986-36
September 8, 1986

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–103, page 13.
Distribution from an eligible state deferred compensation plan; transfer to an individual retirement account. A single-sum cash distribution received or made available from an eligible state deferred compensation plan may not be rolled over on a tax-free basis into an individual retirement account.

Rev. Rul. 86–104, page 14.
Personal holding companies; extension of time to distribute dividends. A personal holding company cannot receive an extension of time as described under section 1.9100–1 of the regulations for a failure to timely distribute a deficiency as described under section 547 of the Code.

Rev. Rul. 86–105, page 15.
Estates; distributions of assets equal to stated fair market value. A bequest of unspecified assets with a fair market value specified in decedent's will is a bequest of a "specified sum of money" under section 663(a) of the Code. Furthermore, the bequest creates a right to receive a specific dollar amount the satisfaction of which results in the recognition of gain or loss to the estate.

T.D. 8092, page 5.
LR–191–82, page 19.
Temporary and proposed regulations under section 338(b) of the Code provide transitional rules relating to allocation of basis to new target's assets if an election is made under section 338 for a qualified stock purchase of an original target that occurred before January 29, 1986.

T.D. 8093, page 16.
Amendments to the temporary regulations under section 7872 of the Code relate to the tax treatment of both the lender and the borrower in certain below market interest rate loan transactions.

LR–141–83, page 19.
Proposed amendments to the regulations under section 453A of the Code relate to installment method reporting by dealers in personal property.

Announcement 86–95, page 25.
This Bulletin contains a list of organizations that no longer qualify as organizations contributions to which are deductible under section 170(c)(2) of the Code.

ADMINISTRATIVE

Rev. Proc. 86–36, page 18.
Investment credit; limitations with respect to noncorporate lessors. In determining the maximum term of the lease under section 46(e)(3) of the Code, the estimated useful life of the property shall be used for recovery property for which the Secretary has not prescribed a present class life.

Announcement 86–94, page 25.
The Service will conduct a nationwide series of seminars to assist people who file information returns on magnetic media meet the legal and technical filing requirements.

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Finding Lists begin on page 29.
Announcement Relating to Decisions of the Tax Court on page 4.
Announcement of Disbursements and Suspensions on page 27.

Department of the Treasury
Internal Revenue Service

T 22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Announcement Relating to Decisions of the Tax Court

It is the policy of the Internal Revenue Service to announce in the Internal Revenue Bulletin at the earliest practicable date the determination of the Commissioner to acquiesce or not acquiesce in a decision of the Tax Court which disallows a deficiency in tax determined by the Commissioner to be due.

Notice that the Commissioner has acquiesced or nonacquiesced in a decision of the Tax Court relates only to the issue or issues decided adversely to the Government.

Actions of acquiescences in adverse decisions shall be relied on by Revenue officers and others concerned as conclusions of the Service only to the application of the law to the facts in the particular case. Caution should be exercised in extending the application of the decision to a similar case unless the facts and circumstances are substantially the same, and consideration should be given to the effect of new legislation, regulations, and rulings as well as subsequent court decisions and actions thereon.

Acquiescence in a decision means acceptance by the Service of the conclusion reached, and does not necessarily mean acceptance and approval of any or all of the reasons assigned by the Court for its conclusions.

No announcements are made in the Bulletin with respect to memorandum opinions of the Tax Court.

The announcements published in the weekly Internal Revenue Bulletins are consolidated semiannually and annually. The semiannual consolidation appears in the first Bulletin for July and in the Cumulative Bulletin for the first half of the year and the annual consolidation appears in the first Bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner ACQUIESCES in the following decisions:

Taxpayer	Docket No.	*Report*	
		Volume	Page
Baumgardner, Est. of Richard B., June Baumgardner Gelbart, Personal Representative[1]	7435–81	85	445
Blount, Jr., Sherwood E., et ux[2]	34916–84	86	—

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[1] Acquiescence relating to whether the Tax Court has jurisdiction under section 6512(b) of the Code to determine an overpayment of interest as part of its jurisdiction to determine an overpayment of tax on which the interest was paid.

[2] Acquiescence in result relating to whether the first submission of an otherwise complete Form 1040, minus Form W–2, or the resubmission with attached Form W–2, begins the running of the statute of limitations on assessment under section 6501 of the Code. Acquiescence "in result" means acceptance of the decision of the Court but disagreement with some or all the reasons assigned for the decision.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 46.—Amount of Credit

26 CFR 1.46–1: Determination of amount.

The estimated useful life of property to be used for recovery property for which there has been no prescribed present class life. See Rev. Proc. 86–36, page 18.

Section 219.—Retirement Savings

Whether a single-sum cash distribution from an eligible state deferred compensation plan may be rolled over on a tax-free basis to an individual retirement account. See Rev. Rul. 86–103, page 13.

Section 338.—Certain Stock Purchases Treated as Asset Acquisitions

26 CFR 1.338–1T: Elections under section 338(g) of the Internal Revenue Code of 1954. (Temporary)

T.D. 8092

TITLE 26—INTERNAL REVENUE.— CHAPTER I, SUBCHAPTER A, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Allocation of Basis to New Target's Assets

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to section 338(b) of the Internal Revenue Code of 1954 ("Code") as added by the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") [1982–2 C.B. 462, 502]. The temporary regulations provide transitional rules relating to allocation of basis to new target's assets if an election is made under section 338 for a qualified stock purchase of an original target that occurred on or before January 29, 1986. This document also contains amendments to other temporary regulations under section 338. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations *** [page 19, this Bulletin].

EFFECTIVE DATE: These regulations under section 338 generally are effective with respect to stock acquisitions made after August 31, 1982.

FOR FURTHER INFORMATION CONTACT: Patricia Wendlandt of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, DC 20224, Attention: CC:LR:T (202-566-3458, not a toll-free number).

SUPPLEMENTARY INFORMATION: BACKGROUND

This document adds new temporary regulations §1.338(b)–4T to Part 1 of Title 26 of the Code of Federal Regulations. Section 338(b) was added top the Internal Revenue Code by section 224 of TEFRA (Pub. L. No. 97–248; 96 Stat. 485) and was amended by section 712(k) of the Tax Reform Act of 1984 (Pub. L. No. 98–369; 98 Stat. 948) [1984–3 C.B. 1, 456]. On January 29, 1986, T.D. 8072 was published in the Federal Register (51 FR 3583) [1986–1 C.B. 111] to implement section 338(b) of the Code by adding temporary regulations §§1.338(b)–1T, 1.338(b)–2T, and 1.338(b)–3T. (Due to typesetting errors, the Federal Register republished T.D. 8072 in its entirety on March 28, 1986 (51 FR 10617).) Conforming amendments are made to temporary regulations §§1,338(b)–2T, 1.338–1T, and 1.338–4T. Additional amendments are made to §§1.338–1T, 1.338-3T, 1.338–4T, and 1.338–5T to change the filing requirements for certain documents. Sections 1.338–1T, 1.338–4T, 1.338–5T, and 1.338(h)(10)–1T were most recently amended by T.D. 8088 [1986–1 C.B. 103] published in the Federal Register on May 16, 1986 (51 FR 17929). Section 1.338–3T was most recently amended by T.D. 7975, published in the Federal Register on September 6, 1984 (49 FR 35086) [1984–2 C.B. 81]. The temporary regulations added and amended by this document will provide certain transitional rules under section 338(b) of the Code and change the place for filing certain documents related to elections under section 338. These temporary regulations will remain in effect until superseded by later temporary or final regulations relating to these matters.

EXPLANATION OF PROVISIONS

Introduction

Section 338 generally provides that if a corporation ("purchasing corporation") acquires the stock of another corporation ("target") in a qualified stock purchase, the purchasing corporation may elect (or may be deemed to elect under certain consistency rules) to have the target treated as if it sold all of its assets (as "old target") at fair market value and then purchased those assets (as "new target"). The deemed sale of assets by old target takes place at the close of the day on which the qualified stock purchase occurred ("acquisition date") and generally is governed by the nonrecognition provisions of section 337. New target is deemed to purchase those assets ("acquisition date assets") at the beginning of the day after the acquisition date. Section 338(b) sets forth the framework for determining the aggregate amount of new target's deemed purchase price for old target's assets ("adjusted grossed-up basis") and allocating this amount among new target's acquisition date assets. The temporary regulations added by this document provide transitional rules relating to the method of allocating adjusted grossed-up basis among the assets of new target.

Allocation of Adjusted Grossed-up Basis Under §1.338(b)–2T

Section 1.338(b)–2T of the temporary regulations, published on January 29, 1986, prescribes the method for allocating adjusted grossed-up basis among new target's acquistion date assets. Section 1.338(b)–2T(b) identifies four classes of assets. "Class I assets" are cash, deposits in banks, and similar cash items.

"Class II assets" are certificates of deposit, United States government securities, certain marketable stocks and securities, foreign currency, and similar items. "Class IV assets" are intangible assets in the nature of goodwill and going concern value. All assets not described above are "Class III assets." As a general rule, a proportionate method of allocation is prescribed for the allocation of basis within each class of assets, although a residual method of allocation is prescribed for the allocation of basis within each class of assets, although a residual method of allocation is prescribed for allocation among the asset classes, allocation beginning with the lowest numbered class.

Under the existing temporary regulations, the amount of adjusted grossed-up basis allocated to any asset, other than Class IV assets, cannot exceed its fair market value. In general, the existing temporary regulations provide that adjusted grossed-up basis, after reduction by the amount of Class I assets, is allocated among Class II assets of target in proportion to their fair market values as of the beginning of the day after the acquisition date, then among Class III assets in such proportion, and, finally, to Class IV assets in such proportion. Thus, adjusted grossed-up basis is allocated within each class of assets to the extent of the fair market value of the assets in that class, with any remaining amount allocated to the next class of assets. The unallocated amount of adjusted grossed-up basis remaining after allocation among the Class III assets is allocated to Class IV assets.

Transitional Rule in Response to Public Comments

The temporary regulations under section 338(b), published on January 29, 1986, apply to qualified stock purchases that occurred after August 31, 1982, for which an election under section 338 applies. Several public comments received subsequent to publication of the temporary regulations have asserted that the temporary regulations constitute a departure from prior law. Accordingly, prospective application of these rules has been requested. In support of this request, comments have noted a lack of specific guidance concerning the allocation of adjusted grossed-up basis following the enactment of TEFRA in 1982 until the temporary regulations were published on January 29, 1986. Although the time for making a section 338 election has been extended many times so that taxpayers could postpone the election decision until all significant regulations under section 338 were published, taxpayers contend that fairness requires that adjusted grossed-up basis may be allocated among new target's assets in the manner permitted under the law for analogous cases.

Taxpayers assert that business necessity compelled them to act in advance of the publication of all significant regulations. As a result, in deciding whether to proceed with taxable stock acquisitions, taxpayers were compelled to predict the basis allocation method that would be prescribed. In doing so, it is asserted that they justifiably relied upon authority applicable to transactions analogous to section 338 transactions.

The Internal Revenue Service believes that the allocation method prescribed in the temporary regulations is a reasonable, proper, and correct allocation method. Nevertheless, due to the substantial period during which there were no regulations relating to the allocation of adjusted grossed-up basis, it has concluded that a transitional rule permitting the allocation of basis under rules which would govern the acquisition of a combination of assets for a lump sum is appropriate for qualified stock purchases that occurred before the regulations were published. Accordingly, this document adds a new §1.338(b)–4T to the temporary regulations under section 338(b) to provide such a rule.

If the purchase price for a business equals the aggregate fair market value of its assets, the residual method of allocation prescribed in §1.338(b)–2T will result in the same allocation as an allocation under the transitional allocation election. If the purchaser believes it paid a premium for the business, that is, an amount in excess of the aggregate fair market value of each of the underlying assets (including goodwill and going concern value), the purchaser may desire to use a proportionate allocation method which would provide for a "second-tier allocation," *i.e.*, an allocation of the premium to the target's assets in proportion to their respective fair market values. For a description of the second-tier method of allocation, see S. Rep. 313, 99th Cong., 2d Sess, 253 (1986).

The Internal Revenue Service believes that, as a factual proposition, the price paid for target stock will, in most cases, reflect the aggregate fair market value of all of the target's assets, including assets in the nature of goodwill and going concern value. Therefore, the Internal Revenue Service believes that in most cases the allocation of basis under the transitional allocation election will produce the same results as allocation of basis under the residual method prescribed in §1.338(b)–2T. For these reasons, the allocation of adjusted grossed-up basis under the transitional allocation election will be closely scrutinized by the Internal Revenue Service. Specifically, an allocation of basis to an asset in excess of its fair market value must be supported by facts and circumstances indicating that the purchase price for target stock exceeds the aggregate fair market value of all of the target's assets. The taxpayer bears the burden of establishing the existence of such facts and circumstances.

Operation of the New Provision

The new provision allows taxpayers to allocate adjusted grossed-up basis pursuant to the rules of Federal income tax law that apply to the purchase on the acquisition date of a combination of assets for a lump sum. For purposes of making an allocation under such method, the provisions of §1.338(b)–2T, other than paragraphs (a) and (c)(2) of that section, do not apply. In order to use such method of allocation, the purchasing corporation must make a "tansitional allocation election." The election is made by filing a "transitional allocation election statement" with the district director for the internal revenue district in which the purchasing corporation has its principal place of business. The statement also must be attached to the first return of new target. The transitional allocation election is irrevocable and can only be made for an original target the stock of which was acquired in a qualified stock purchase on or before January 29, 1986, or which was acquired after that date but pursuant to a binding contract in effect (or a tender offer outstanding) as of January 29, 1986. The transitional allocation election applies to the original target and to all affected targets that were acquired on or before January 29, 1986.

The allocation of adjustments to adjusted grossed-up basis resulting from events occurring after the close of new target's first taxable year is also subject to the transitional allocation election. Thus, such adjustments are allocated among target's acquisition date assets in the same manner as adjusted grossed-up basis is allocated under §1.338(b)–4T and, except as otherwise provided in §1.338(b)–4T(e)(3), the rules in §1.338(b)–3T do not apply. In addition, if the aggregate deemed sale price (ADSP) for old target is calculated under the elective formula described in §1.338–4T(h)(3), then the ADSP must be allocated among old target's assets pursuant to the method used to allocate adjusted grossed-up basis among new target's assets pursuant to the transitional allocation election. Conforming amendments are made to §1.338–4T to effect this result.

This document also contains certain amendments to §1.338–1T to provide additional guidance relating to the transitional allocation election.

Amendments to §1.338(h)(10)–1T

This document amends the regulations under section 338(h)(10) to conform the method of allocating MADSP among old target's assets to the method of allocating adjusted grossed-up basis among new target's assets. A similar amendment was made to §1.338–4T(h) for the allocation of ADSP among old target's assets by T.D. 8072, published in the Federal Register on January 29, 1986 (51 FR 3583, republished on March 28, 1986 (51 FR 10617): The amendment to §1.338(h)(10)–1T does not apply to qualified stock purchases that occurred on or before July 1, 1986.

Miscellaneous Amendments

This document also contains miscellaneous amendments to §§1.338–1T, 1.338–3T, 1.338–4T, and 1.338–5T. Prior to these amendments, the statement of section 338 election and other documents related to elections under section 338 generally were required to be filed with Service Centers. Beginning January 1, 1987, many documents relating to elections made under section 338 are required to be filed with the District Director for the internal revenue district in which is located the principal place of business or the principal office or agency of the purchasing corporation. Documents filed on or after July 1, 1986 and before January 1, 1987 may be filed with either the District Director or with any other office permitted under the regulations. These changes are necessary in order to more effectively administer the provisions of section 338. An amendment is also made to the Example in §1.338–4T(h)(3) *Answer 3* to clarify the method of allocating the aggregate deemed sale price under the elective formula under section 338(h)(11).

Regulatory Flexibility Act; Executive Order 12291; and Paperwork Reduction Act of 1980

A general notice of proposed rulemaking is not required by 5 U.S.C. 553 for temporary regulations. Accordingly, these temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required. The collection of information contained in these regulations has been submitted to the Office of Management and Budget in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB (Control number 1545-0702).

DRAFTING INFORMATION

The principal author of these temporary regulations is Patricia Wendlandt of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of Amendments to the Regulations

Accordingly, Parts 1 and 602 of Title 26 of the Code of Federal Regulations are amended as follows:

PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Paragraph 1. The authority citation for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805; * * * §§1.338–1T, 1.338–3T, 1.338–4T, 1.338–5T, 1.338(b)–2T, 1.338(b)–4T, and 1.338(h)(10)–1T also issued under 26 U.S.C. 338.

Par. 2. Section 1.338–1T is amended as follows:

1. Paragraph (c) is revised to read as set forth below.

2. The last sentence of paragraph (d)(3) is revised to read as set forth below.

3. Paragraph (e)(1)(ii)(A) is revised to read as set forth below.

4. The first sentence of paragraph (e)(1)(ii)(B) is revised to read as set forth below.

5. The heading of paragraph (e)(2) is revised to read as set forth below.

6. Paragraph (e)(2)(ii) is revised to read as set forth below.

7. Paragraph (e)(2)(iii) is revised to read as set forth below.

8. The first sentence of paragraph (e)(2)(iv) is amended by adding after the words "Service Center" the words "or District Director."

9. A new subdivision (vi) is added to paragraph (e)(2). The new subdivision reads as set forth below.

10. Paragraph (h)(2)(ii) is revised to read as set forth below.

11. The second sentence in paragraph (j)(4)(ii) is amended by removing the words "with the Internal Revenue Service Center(s) with which" and by adding in their place the words "in the Form 8023 filing place(s) where."

12. Paragraph (k)(1) is revised to read as set forth below.

13. A new sentence is added at the end of paragraph (k)(2)(i) to read as set forth below.

14. Paragraph (l)(3)(i) is amended by removing the words "with the appropriate Internal Revenue Service Center" and by adding in their place the words "in the appropriate Form 8023 filing place(s) (determined under paragraphs (c) and (d) of this section)."

§1.338–1T Elections under section 338(g) of the Internal Revenue Code of 1954 (temporary).

* * * * *

(c) *Time and manner of making election—(1) In general.* The purchasing corporation makes an election under section 338(g) for the original target only by filing, not later than the 15th day of the 9th month beginning after the month in which the acquisition date occurs (or if later, July 15, 1986), a statement of section 338 election in the Form 8023 filing place. The Form 8023 filing place is:

(i) For a statement of section 338 election that is filed before July 1, 1986, the Internal Revenue Service Center with which the purchasing corporation files its annual income tax return.

(ii) For a statement of section 338 election that is filed on or after January 1, 1987, the District Director (Attention: Chief of Examination) for the internal revenue district in which the purchasing corporation's income tax return would be filed if §1.6091–2(b) applied (*i.e.*, the internal revenue district in which is located the principal place of business or the principal office or agency of the corporation).

(iii) For a statement of section 338 election that is filed on or after July 1, 1986 and before January 1, 1987, either of the places described in subdivisions (i) and (ii) of this subparagraph (1).

(2) *Additional rules.* If the statement of section 338 election for the original target will cause section 338(a) to apply to other corporations ("affected targets") by reason of section 338(f)(1), a separate statement of section 338 election need not be filed for those affected targets. See paragraph (e)(1) of this section for requirement to attach a schedule containing information relating to the original target and the affected targets. See paragraph (k)(7) of this section for a required notice to the domestic shareholders of foreign targets in certain cases. See also para-

graph (k) of this section generally for other special rules applicable to certain foreign corporations and DISCs. For special rules applicable to certain statements of section 338 election filed on or after December 9, 1985, and on or before July 15, 1986, see paragraph (m) of this section.

(d) *Statement of section 338 election.* * * *

(3) *Qualified stock purchase made by several corporations in the aggregate.* * * * A copy of this single statement of section 338 election must be filed within the time specified in paragraph (c) of this section in the Form 83 filing place (determined under paragraph (c) of this section) of each such member.

(e) *Schedule; attachments to target returns*—(1) *Schedule of information relating to certain corporations and persons.* * * *

(ii) *Corrective statements*—(A) *Transitional rule.* If a statement of section 338 election filed on or before July 15, 1986, does not include the schedule with all of the required data, the requirements of paragraph (e)(1)(i) of this section will be satisfied if, on or before July 15, 1986, a corrective statement in the form of the schedule (containing all of the required data, and with a copy of the previously filed statement of section 338 election attached) is filed in the Form 8023 filing place(s) where a statement of section 338 election would be filed, under paragraphs (c) and (d) of this section, on the date the corrective statement is filed.

(B) *Regular exclusion election invalidated.* If, subsequent to the making of a regular exclusion election, that exclusion election is invalidated by reason of an invalidation event described in §1.338–5T(c)(2)(iii) and if, by reason of the invalidation event, a previously filed schedule under this subparagraph (1) incorrectly identifies certain corporations as excludible foreign target affiliates subject to a regular exclusion election, then the requirements of paragraph (e)(1)(i) of this section will be satisfied if, on or before the later of July 15, 1986, or the 120th day after the date of the invalidation event, a corrective statement in the form of an amended schedule (along with a copy of the previously filed statement of section 338 election) is filed in the Form 8023 filing place(s) where a statement of section 338 election would be filed, under paragraphs (c) and (d) of this section, on the date the corrective statement is filed. * * *

* * * * *

(2) *Attachments to target returns; additional filings with certain Service Centers and District Directors.* * * *

(ii) *Corrective statements*—(A) *Transitional rule.* If all of the required items (containing all of the information required to be included in those items) are not attached to a final return of old target or a first return of new target that is filed on or before July 15, 1986, the requirements of paragraph (e)(2)(i) of this section will be satisfied if on or before that date a corrective statement consisting of all of the required items (containing all of the information required to be included in those items) is filed with the Internal Revenue Service Center(s) with which the returns to which the required items should have been attached were filed. A corrective statement that is filed on or after January 1, 1987, must be attached to an amended return. Prior to that date, however, attachment to an amended return is optional.

(B) *Special rule if regular exclusion election invalidated.* If, under the circumstances described in paragraph (e)(1)(ii)(B) of this section (relating to invalidation of regular exclusion election), a previously filed schedule under this paragraph (e)(2) incorrectly identifies certain corporations as excludible foreign target affiliates subject to a regular exclusion election, then the requirements of paragraph (e)(2)(i) of this section will be satisfied only if, on or before the 120th day after the date of the invalidation event, a corrective statement in the form of an amended schedule (containing the information and attachment required by paragraph (e)(1)(ii)(B) of this section) is filed with the Internal Revenue Service Center(s) with which the returns to which the previously filed schedule was attached were filed. A corrective statement that is filed on or after January 1, 1987, must be attached to an amended return. Prior to that date, however, attachment to an amended return is optional.

(iii) *Additional filings with certain Service Centers and District Directors.* On or before the day on which any return or corrective statement described in paragraph (e)(2)(i) or (ii) of this section is filed, the required items also must be filed in the Form 8023 filing place(s) where a statement of section 338 election would be filed, under paragraphs (c) and (d) of this section, on the date the return or corrective statement is filed. If a gain recognition election under section 338(b)(3) is made in connection with the statement of section 338 election (so that a copy of the gain recognition statement ("GRS") under §1.338–4T(j)(2) is a required item pursuant to paragraph (e)(2)(i)(A) of this section and the required items are filed with a Service Center under paragraph (c)(1) of this section, then, on or before the day specified in the preceding sentence, the required items also must be filed with each other Internal Revenue Service Center with which each affected P group member (determined as of the day of filing) files its annual income tax return. For the definition of "affected P group member," see §1.338–4T(j)(2) *Answer 5(ii)(A)*. The required items need not, however, be filed with a Service Center or District Director that already has received the identical required items.

* * * * *

(vi) *Transitional allocation election statements.* A copy of the transitional allocation election statement prescribed in §1.338(b)–4T(c)(1) is required to be attached to the first return (or amended return) of the original target (and each affected target) as new target. A copy of the supplemental transitional allocation election statement prescribed by §1.338(b)–4T(c)(3) is required to be attached only to the first return of the new target (or new targets) identified in that statement.

* * * * *

(h) *Waiver: certain additions to tax and times to act, etc.* * * *

(2) *Elections or other actions required to be specified on a timely filed return.* * * *

(ii) *New target in purchasing group's consolidated return.* If new target is includible for its first taxable year in a consolidated return filed by the purchasing group on or before the later of July 15, 1986, or the last day for making the election under section 338, then any election or other action that must be specified in a timely filed return for new target's first taxable year (but which is not specified in the consolidated return) will be considered timely if specified in an amended return filed on or before the later of July 15, 1986, or such last day, with the Internal Revenue Service Center with which the consolidated return was filed. Before January 1, 1987, if the contents of the consolidated return itself are not affected by the election or other action, a separate statement may serve as a substitute for the amended return. Such separate statement must cite this provision and must include the name, address, and EIN of the parent corporation of the purchasing group.

* * * * *

(k) *Special rules for foreign corporations or DISCs*—(1) *Elections by certain foreign purchasing corporations*—(i) *In general.* This subparagraph (1) applies to a statement of section 338 election (or any other election under section 338) that is filed by a foreign purchasing corporation that is not required under §1.6012–2(g) (other than subparagraph (2)(i)(*b*)(*2*) thereof) to file a United States income tax return for its taxable year that includes the acquisition date.

(ii) *Place of filing.* An election to which this subparagraph (1) applies that is filed—

(A) Before July 1, 1986 must be filed with the Philadelphia Service Center, Philadelphia, Pennsylvania 19255.

(B) On or after January 1, 1987, must be filed with the District Director of the Foreign Operations District (Attention: Chief of Examination), 1325 K Street, NW., Washington, DC 20225.

(C) On or after July 1, 1986 and before January 1, 1987, may be filed in either of the places described in (A) or (B) of this subdivision (ii).

(iii) *Special rule.* Notwithstanding subdivision (ii) of this subparagraph (1), the items required (under paragraph (m) of this section and §1.338(b)–4T(b)) to be filed by such a foreign purchasing corporation with the District Director shall be filed with the District Director of the Foreign Operations District (Attention: Chief of Examination), 1325 K Street, N.W., Washington, DC 20225.

(2) *Election not required until relevant*—(i) *General rule.* * * * A transitional allocation election statement under §1.338(b)–4T for a qualifying foreign target must be filed on or before the last day that the qualifying purchasing corporation may file a statement of section 338 election.

* * * * *

Par. 3. Paragraph (b)(2) of §1.338–3T is revised to read as set forth below.

§1.338-3T Miscellaneous rules under section 224 of TEFRA (temporary).

* * * * *

(b) *Certain acquisitions of financial institutions.* * * *

(2) *Manner of electing out.* A purchasing corporation is considered to elect out only if the requirements of section 224(d)(3) of TEFRA are satisfied and the purchasing corporation files a statement of election-out within 30 days after adoption of the plan of complete liquidation of the financial institution specified in section 224(d)(3)(C) (or by May 8, 1984, if later) in the Form 8023 filing place(s) where a statement of section 338 election would be filed, under §1.338–1T (c) and (d), on the date the statement of election-out is filed.

Par. 4. Section 1.338–4T is amended as follows:

1. Paragraph (f)(6)(ii) *Answer 1* (i) is revised to read as set forth below.

2. A new sentence is added immediately after the first sentence of paragraph (f)(6)(ii) *Answer 1* (iii)(A). The new sentence reads as set forth below.

3. The first sentence of paragraph (f)(6)(ii) *Answer 2* (iv) is revised to read as set forth below.

4. The last sentence of paragraph (f)(6)(ii) *Answer 2* (iv) is amended by adding after the words "Service Center" the words "or District Director."

5. The second sentence in paragraph (h)(2)(iii) is removed and two new sentences are added in its place. The new sentences read as set forth below.

6. A new sentence is added immediately after the third sentence of paragraph (h)(3) *Answer 2* (vi). The new sentence reads as set forth below.

7. In the Example in paragraph (h)(3) *Answer 3*—

a. Subdivision (i) is amended by adding a new sentence immediately after the third sentence. The new sentence reads as set forth below.

b. Two new sentences are added at the end of subdivision (ii). The new sentences read as set forth below.

c. Subdivision (iii) is amended by adding a new sentence at the end to read as set forth below.

8. Paragraph (j)(2) *Answer 5* is amended by—

a. Revising subdivision (i) to read as set forth below.

b. Adding in the appropriate place a new subdivision (iii) to read as set forth below.

§1.338–4T Questions and answers relating to miscellaneous issues under section 338 (temporary).

* * * * *

(f) *Application of the asset consistency rule of section 338(e).* * * *

(6) *Carryover basis election exception under section 338(e)(2)(D) and (i).* * * *

(ii) *Procedure for making protective carryover election and affirmative action carryover election.*

Question 1: * * *

Answer 1: (i) *Filing procedure.* The protective carryover election is made in the form of a statement of protection carryover election ("protective carryover election sattement") filed within the period during which an express election may be made for T. A protective carryover election statement that is filed before July 1, 1986 must be filed with each Internal Revenue Service Center with which a corporation required to join in making the protective carryover election files its annual income tax return. A protective carryover election statement that is filed on or after January 1, 1987, must be filed with the District Director (Attention: Chief of Examination) for each internal revenue district in which a corporation required to join in making the protective carryover election would file its income tax return if §1.6091–2 (b) applied. A protective carryover election statement that is filed on or after July 1, 1986 and before January 1, 1987, may be filed in either of the places described in the preceding two sentences. For place to file in certain cases if the purchasing corporation is a foreign corporation, see §1.338–1T (k)(1).

* * * * *

(iii) *Contents of protective carryover election statement*—(A) *General rule.* * * * A protective carryover election statement that is filed on or after July 31, 1986 also must identify the purchaser(s) of T. * * *

* * * * *

Answer 2: * * *

(ii) *Filing procedure.* The supplemental statement is filed in the place(s) where a protective carryover election statement would be filed, under *Answer 1* (i) of this paragraph (f)(6)(ii), on the date the supplemental statement is filed. * * *

* * * * *

(h) *Determination of section 338(a)(1) deemed sale price.* * * *

(2) *Definitions.* * * *

(iii) *Allocable ADSP amount.* * * * Except as provided in section 7701(g) (relating to fair market value in the case of nonrecourse indebtedness), and unless a transitional allocation election under §1.338(b)–4T is made, the ADSP is allocated among T assets for this purpose in accordance with the rules in §1.338(b)–

2T (without regard to §1.338 (b)–2T (c)(2)). If a transitional allocation election under §1.338(b)–4T is made, the ADSP is allocated among T assets for this purpose in accordance with the rules in §1.338(b)–4T(e). * * *

* * * * *

(3) *Determination of ADSP.*

* * * * *

Answer 2. * * *

(vi) *Sample elective ADSP formula.* * * * In examples (1) through (9) of this subdivision (vi) it is assumed that a transitional allocation election under §1.338(b)–4T is not made. * * *

* * * * *

Answer 3: * * *

Example: (1) * * * The fair market value of T1's asset is $30,000. * * *

(ii) * * * Since the ADSP for T ($189,422.71) does not exceed the sum of the fair market values of all of T's assets ($215,000), and those assets are all Class III assets, its entire ADSP is allocated to those assets in proportion to their fair market values. See §1.338(b)–2T(c)(1) (relating to fair market value limitation).

(iii) * * * Since the ADSP for T1 ($29,651) does not exceed the fair market value of T1's only asset ($30,000), its entire ADSP is allocated to that asset.

* * * * *

(j) *Determination of basis of target assets after section 338 election.* * * *

(2) *Determination of adjusted grossed-up basis.*

* * * * *

Answer 5: (i) *Attachment to statement of section 338 election.* The gain recognition election is made in the form of a gain recognition statement ("GRS") that is attached to a timely filed statement of section 338 election (Form 8023) for T. In order for the gain recognition election to be valid, the statment of section 338 election (with the GRS attached) must be filed within the time specified in §1.338–1T(c) in the Form 8023 filing place(s) designated in §1.338–1T(c) and (d). The gain recognition election is irrevocable. For certain additional filing requirements if a gain recognition election is made, see §1.338–1T(e)(2).

* * * * *

(iii) *Transitional rules.* Notwithstanding subdivision (i) of this *Answer 5*—

(A) If the statement of section 338 election with the GRS attachment is filed with a Service Center under §1.338–1T(c)(1), then the gain recognition election will not be valid unless copies of the GRS are also filed with each other Service Center with which each affected P group members (as defined in this *Answer 5* (ii)(A)) files its annual income tax return.

(B) If a statement of section 338 election is filed on or before July 15, 1986, without the GRS attachment, the P group may make a valid gain recognition election by filing the GRS (with a copy of the previously filed statement of section 338 election attached) on or before that day at the place(s) specified in subdivision (i) of this *Answer 5* and, if applicable, subdivision (A) of this subdivision (iii).

* * * * *

Par. 5. Section 1.338–5T is amended as follows:

1. Paragraph (c)(2)(v)(C) is revised to read as set forth below.

2. Paragraph (j)(8)(ii) is revised to read as set forth below.

§1.338–5T International aspects of section 338 (temporary)

* * * * *

(c) *Application of section 338 to corporations and stock described in section 338(h)(6)(B).* * * *

(2) *Elective exclusion of foreign corporations from target affiliate status.* * * *

(v) *Procedure for making regular exclusion election.* * * *

(C) *Transitional rule.* If a regular exclusion election is not made in an express election filed on or before July 15, 1986, a regular exclusion election nonetheless may be made if, on or before July 15, 1986, a copy of the previously filed express election (generally Form 8023), with a copy of the regular exclusion statement attached, is filed in the Form 8023 filing place(s) where a statement of section 338 election would be filed, under §1.338–1T(c) and (d), on the date of the regular exclusion election is made.

* * * * *

(j) *Transitional rules for corporations and stock described in section 338(h)(6)(B).*

(8) *Transitional section 338(h)(6)(B) election procedures.* * * *

(ii) *Special procedure if express election filed on or before July 15, 1986.* If a transitional seciton 338(h)(6)(B) statement is not attached to an express election filed on or before July 15, 1986, a transitional election(s) nonetheless may be made if, on or before that date, a copy of the previously filed express election, with a copy of the transitional section 338(h)(6)(B) statement attached, is filed in the Form 8023 filing place(s) where a statement of section 338 election would be filed, under §1.338–1T(c) and (d), on the date the transitional election is made.

* * * * *

Par. 6. Section 1.338(b)–2T is amended by adding a new paragraph (a)(3). The new provision reads as follows:

§1.338(b)–2T Allocation of adjustd grossed-up basis among target assets (temporary).

(a) *Introduction.* * * *

(3) *Transitional allocation election.* For elective rules relating to the election of adjusted grossed-up basis for a qualified stock purchase for which the acquisition date is on or before January 29, 1986, see §1.338(b)–4T.

* * * * *

Par. 7. A new §1.338(b)–4T is added immediately after §1.338(b)–3T to read as follows:

§1.338(b)–4T Transitional allocation election under section 338 (temporary).

(a) *In general*—(1) *Scope.* This section provides a transitional allocation election relating to the allocation of adjusted grossed-up basis under section 338(b)(5) and §1.338(b)–2T. For consequences of a transitional allocation election, see generally paragraph (e) of this section.

(2) *Eligibility to make a transitional allocation election.* A transitional allocation election may only be made for an original target (and applies to any affected target described in paragraph (e)(1) of this section) for which the acquisition date is—

(i) On or after September 1, 1982, and on or before January 29, 1986, or

(ii) After January 29, 1986, but pursuant to a contract of sale, or an offer to purchase, that is binding on the purchasing corporation on that date and at all times thereafter.

(3) *Nomenclature and definitions.* The nomenclature set out in §1.338–4T(b)(1) also applies to this section. The definitions in §1.338(b)–3T(b)(2) also apply to this section.

(b) *Time and manner of making election*—(1) *In general.* P makes a transitional allocation election for an original target by filing a transitional allocation election statement prescribed by paragraph (c)(1) of this section with the District Director (Attention: Chief of

Examination) for the internal revenue district in which the purchasing corporation's income tax return would be filed if §1.6091-2(b) applied. If two or more corporations that are members of an affiliated group make a qualified stock purchase in the aggregate (see §1.338-1T(d)(3)), then a copy of the transitional allocation election statement prescribed by paragraph (c)(1) of this section must be filed with the District Director (Attention: Chief of Examination) in such internal revenue district for each purchasing corporation. The transitional allocation election statement must be filed on or before the later of (i) the due date, including extensions of time, for filing the first return of the original target as new target or (ii) November 3, 1986. The special rules in §1.338-1T(k)(1) and (2) apply to making the transitional allocation election for foreign corporations.

(2) *Additional filing requirements.* Pursuant to §1.338-1T(e)(2)(vi), a copy of the transitional allocation election statement also must be attached to the first return (or amended return) of the original target (and each affected target) as new target. Pursuant to §1.338-1T(e)(2)(vi), a supplemental transitional allocation election statement prescribed by paragraph (c)(3) of this section must be attached to the first return (or amended return) as new target of each affected target identified in that statement.

(c) *Contents of transitional allocation election statement*—(1) *In general.* The transitional allocation election statement must:

(i) Be identified prominently as a "Transitional Allocation Election Statement Under §1.338(b)-4T."

(ii) Contain the name, address, and employer identification number of the purchasing corporation(s) and the original target.

(iii) Indicate the date on which an express election was made for the original target.

(iv) State the date on which the first return (and, if applicable, the amended return) of the original target (and of each affected target) as a new target was filed. (If the first return of a target has not been filed, state the due date, including extensions of time, for filing such return or, if appropriate, indicate that new target is a foreign corporation that is not required to file a United States income tax return for its first taxable year as new target.)

(v) Have attached to it a photocopy of any extension, consent, or other document previously entered into or filed which extended the statute of limitations on assessment for the first taxable year of the original target (or any affected target) as new target.

(vi) With respect to the original target and with respect to each affected target, state that (A) "New target's adjusted grossed-up basis [exceeds by $[insert amount of the excess]] [does not exceed] the sum of the fair market values of its assets, including goodwill and going concern value, at the beginning of the day after the acquisition date" or (B) "It has not yet been determined whether new target's adjusted grossed-up basis exceeds the sum of the fair market values of its assets, including goodwill and going concern value, at the beginning of the day after the acquisition date and therefore P will file a supplemental transitional allocation election statement as required by §1.338(b)-4T(c)(3)."

(vii) With respect to the original target and with respect to each affected target (A) list (for each of asset classes I, II, III, and IV) (*1*) the aggregate fair market value of the assets in the class and (*2*) the aggregate amount of adjusted grossed-up basis allocated to the assets in the class or (B) state "The information required under §1.338(B)-4T(c)(2)(vii)(A) has not yet been determined and therefore P will file a supplemental transitional allocation election statement as required by §1.338(b)-4T(c)(3)."

(viii) Be signed (in the manner prescribed in §1.338-IT(d)(1)(vi)) by a person authorized to act on behalf of the purchasing corporation.

(2) *Special rules*—(i) *Time of determination.* The information required by paragraph (c)(1)(vi)(A) and (vii)(A) of this section must be determined no later than the date on which the first return (or amended return) of the particular new target as new target is filed.

(ii) *References to more than one target.* The statements required under paragraph (c)(1)(vi) and (vii) of this section may, in appropriate cases, be modified to apply to more than one target if the particular targets to which the statement applies are clearly and unambiguously identified.

(3) *Supplemental statements*—(i) *In general.* If the information required under paragraph (c)(1)(vi)(A) and (vii)(A) of this section for any target has not been determined as of the date the transitional allocation election statement is filed, P is required to file (at the place prescribed in paragraph (b) of this section) a supplemental transitional allocation election statement no later than the date the first return of that target as a new target is filed. The supplemental transitional allocation election statement must:

(A) Be identified prominently as a "Supplemental Transitional Allocation Election Statement Under §1.338(b)-4T for [insert name of target or targets for which the statement is being filed]."

(B) Contain the information required under paragraph (c)(1)(vi)(A) and (vii)(A) of this section.

(C) Have attached to it a copy of the transitional allocation election statement that was filed for the original target.

(D) State the dates on which all previously filed supplemental transitional allocation election statements were filed.

(E) Be signed (in the manner prescribed in §1.338-1T(d)(1)(vi)) by a person authorized to act on behalf of the purchasing corporation.

(ii) *Failure to timely file a valid supplemental statement.* If a supplemental transitional allocation election statement is required to be filed, then the transitional allocation election is not effective unless the purchasing corporation timely files a valid supplemental statement. A supplemental transitional allocation election statement that does not contain the information required under paragraph (c)(1)(vi)(A) and (vii)(A) of this section is invalid. The District Director or his delegate may, at any time in connection with the examination of any Federal income tax return that would be affected by a transitional allocation election, waive the requirement of filing a valid supplemental statement.

(d) *Irrevocability.* A transitional allocation election under this section, once made, is irrevocable.

(e) *Certain consequences of transitional allocation election*— (1) *Consistency rule.* A transitional allocation election for an original target shall apply to each affected target that would be eligible under paragraph (a)(2) of this section to make a transitional allocation election if it were an original target. Thus, if a transitional allocation election is made, then neither the original target nor any affected target may rely upon §1.338(b)-2T(b) for the purpose of allocating adjusted grossed-up basis. For rules relating to the exclusion of a transitional target affiliate, see §1.338-

5T(j) (relating to international aspects of section 338).

(2) *Allocation of adjusted grossed-up basis.* A corporation to which a transitional allocation election applies shall allocate adjusted grossed-up basis pursuant to the rules of Federal income tax law that apply to the purchase on the acquisition date of a combination of assets for a lump sum. The following table sets forth the subunits of §1.338(b)–2T and indicates whether each is applicable or inapplicable if a transitional allocation election is made.

Subunit of sec.. 1.338(b)–2T	Applicable	Inapplicable
(a)	X	
(b)		X
(c)(1)		X
(c)(2)	X	
(c)(3)		X
(d)		X

(3) *Allocation of subsequent adjustments to adjusted grossed-up basis.* If adjusted grossed-up basis is allocated under paragraph (e)(2) of this section and adjusted grossed-up basis is redetermined to take into account adjustment events that occur after the close of new target's first taxable year, the amount of the increase (or decrease), determined under §1.338(b)–3T(c)(3), shall be allocated among target's acquisition date assets pursuant to the method used to allocate adjusted grossed-up basis. The following table sets forth the subunits of §1.338(b)–3T and indicates whether each is applicable or inapplicable if a transitional allocation election is made.

Subunit of sec. 1.338(b)–3T	Applicable	Inapplicable
(a)	X	
(b)	X	
(c)	X	
(d)(1)		X
(d)(2)	X	
(e)(1)		X
(e)(2)	X	
(f)		X
(g)		X
(h)	X[1]	
(j)	X[2]	

[1] Paragraph (h) is applicable except to the extent it incorporates other provisions of §§1.338(b)–2T and 1.338(b)–3T that are inapplicable when a transitional allocation election is made.

[2] The examples in paragraph (j) apply only to the extent that they illustrate provisions of §1.338(b)–3T that are applicable with a transitional allocation election is made.

(4) *Careful scrutiny of allocation.* The transitional allocation election statement identifies taxpayers that allocate to any asset an amount of adjusted grossed-up basis that exceeds the asset's fair market value. The Internal Revenue Service will subject such allocations to careful scrutiny.

(5) *Coordination with allocation of ADSP.* If the elective formula under section 338(h)(11) is used to determine the aggregate deemed sale price for old target's assets, the allocable ADSP amount (as defined in §1.338–4T(h)(2)(iii) for each asset must be determined pursuant to the method used to allocate adjusted grossed-up basis among the assets of new target. Additional rules for determining the allocable ADSP amount if a transitional allocation election is made are contained in §1.338–4T(h) (2) and (3).

Par. 8. Section 1.338(h)(10)–1T is amended as follows:

1. Paragraph (f)(2)(ii) is revised to read as set forth below.

2. Example (2) in paragraph (g) is amended by—

a. Removing, from subdivision (iii), the words "paragraph (f)(2)(ii)" and by adding in their place the words "paragraph (f)(2)(ii)(A)."

b. Adding at the end a new subdivision (iv) to read as set forth below.

3. Example (7) in paragraph (g) is amended by—

a. Removing, from subdivision (ii)(B), the words "paragraph (f)(2)(ii)" and by adding in their place the words "paragraph (f)(2)(ii)(A)."

b. Adding at the end a new subdivision (ix) to read as set forth below.

§1.338(h)(10)–1T Elective recognition by selling consolidated group of deemed sale gain or loss on target's assets (temporary).

* * * * *

(f) *Deemed sale price.* * * *

(2) *Elective MADSP formula.* * * *

(ii) Then determining the deemed selling price by allocating MADSP among the assets of old T as follows:

(A) If the acquisition date is on or before July 1, 1986, or after that date but pursuant to a contract of sale that is binding on both the purchaser and the seller as of that date, the allocation to each asset shall be made in proportion to its relative fair market value.

(B) If the allocation under paragraph (f)(2)(ii)(A) of this section is not permitted, the allocation to each asset shall be made in accordance with the rules in §1.338(b)–2T (without regard to §1.338(b)–2T(c)(2)).

* * * * *

(g) Examples. * * *

Example (2). * * *

(iv) This example illustrates allocation of MADSP pursuant to the method described in paragraph (f)(2)(ii)(A) of this section. In this example, the same result also obtains using the method described in paragraph (f)(2)(ii)(B) because T has only Class III assets and MADSP does not exceed the sum of the fair market values of T's assets.

* * * * *

Example (7). * * *

(ix) This example illustrates allocation of MADSP pursuant to the method described in paragraph (f)(2)(ii)(A) of this section. In this example, the same result also obtains using the method described in paragraph (f)(2)(ii)(B) because T has only Class III assets and MADSP does not exceed the sum of the fair market value of T's assets.

* * * * *

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 9. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

§602.101 [Amended]

Par. 10. Section 602.101(c) is amended by inserting in the appropriate place in the table "§1.338(b)–4T . . . 1545–0702."

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

JAMES I. OWENS,
Acting Commissioner
of Internal Revenue

Approved June 26, 1986.

J. ROGER MENTZ,
Assistant Secretary
of the Treasury

(Filed by the Office of the Federal Register on June 27, 1986, 10:10 a.m., and published in the issue of the Federal Register for July 1, 1986, 51 F.R. 23737)

Section 408.—Individual Retirement Accounts

Whether a single-sum cash distribution from an eligible state deferred compensation plan may be rolled over on a tax-free basis to an individual retirement account. See Rev. Rul. 86-103, page 13.

Section 451.—General Rule for Taxable Year of Inclusion

26 CFR 1.451-2: Constructive receipt of income.

Whether a single-sum cash distribution from an eligible state deferred compensation plan may be rolled over on a tax-free basis to an individual retirement account. See Rev. Rul. 86-103, below.

Section 457.—Deferred Compensation Plans with Respect to Service for State and Local Governments

26 CFR 1.457-1: Compensation deferred under eligible state deferred compensation plans.
(Also Sections 219, 408, 451, 4973; 1.451-2.)

Distribution from an eligible state deferred compensation plan; transfer to an individual retirement account. A single-sum cash distribution received or made available from an eligible state deferred compensation plan may not be rolled over on a tax-free basis into an individual retirement account.

Rev. Rul. 86-103

ISSUE

If a single-sum cash distribution is received or made available from an eligible state deferred compensation plan under section 457(b) of the Internal Revenue Code, may that distribution be rolled over on a tax-free basis into an individual retirement account in the situations described below.

FACTS

Situation 1

A, an unmarried taxpayer, was an employee of state *S* until December 31, 1984, at which time *A* was separated from service with *S*. During 1985, *A* worked as an employee of a private company and earned $20,000. Also, during 1985, *A* established an individual retirement account (IRA) with a bank and contributed $2,000 to the IRA for 1985. Finally, in 1985, *A* received a single-sum distribution representing the benefits to which *A* was entitled under *S*'s eligible state deferred compensation plan. These benefits had not been made available to *A* under the plan before 1985. *A* immediately contributed the entire amount of the single-sum distribution to the IRA. *A* did not make any qualified voluntary employee contributions within the meaning of section 219(e)(2) of the Code during the year.

Situation 2

The facts are the same as in *Situation 1*, except that the single-sum distribution was not actually paid to *A* in 1985, but rather was made available to *A* in 1985 and at *A*'s direction, was contributed in 1985 by state *S* to the IRA established by *A*.

LAW AND ANALYSIS

Section 457(a) of the Code provides that, in the case of a participant in an eligible state deferred compensation plan, any amount of compensation deferred under the plan, and any income attributable to the amounts so deferred, will be includible in gross income only for the taxable year in which such compensation or other income is paid or otherwise made available to the participant or other beneficiary under the plan.

Section 451(a) of the Code provides that the amount of any item of gross income is included in gross income for the taxable year in which received by the taxpayer, unless under the method of accounting used in computing taxable income, such amount is to be poorly accounted for as of a different period.

Section 1.451-2(a) of the Income Tax Regulations provides, in part, that income, although not actually reduced to a taxpayer's possession, is constructively received in the taxable year during which it is credited to the taxpayer's account, set apart, or otherwise made available to the taxpayer so that the taxpayer may draw upon it at any time. However, income is not constructively received if the taxpayer's control of its receipt is subject to substantial limitations or restrictions.

Section 408(a) of the Code provides that the term "individual retirement account" means a trust created or organized in the United States for the exclusive benefit of an individual or the individual's beneficiaries, but only if the written governing instrument creating the trust meets requirements specified in that section.

Section 219(b) of the Code provides that the maximum allowable as a deduction for qualified retirement contributions to any individual for any taxable year shall not exceed the lesser of $2,000 or an amount equal to the compensation includible in the individual's gross income for such taxable year.

Section 219(e)(1) of the Code defines the term "qualified retirement contributions" to include any amount paid in cash for the taxable year by or on behalf of an individual for his benefit to an individual retirement plan. Section 7701(a)(37) defines "individual retirement plan" to include an individual retirement account described in section 408(a).

Under section 4973(a) of the Code, a tax is imposed on excess contributions to individual retirement accounts. The tax is imposed for each taxable year in an amount equal to six percent of the amount of the excess contributions (determined as of the close of the taxable year). The term "excess contributions" is defined, in part, in section 4973(b) as the excess (if any) of the amount contributed for the taxable year to an individual retirement account (other than a rollover contribution described in sections 402(a)(5), 402(a)(7), 403(a)(4), 403(b)(8), or 408(d) (3)) over the amount allowable as a deduction under section 219 for such contribution. However, a contribution to which section 408(d)(4) applies is not considered a contribution for purposes of section 4973(b).

Under section 408(d)(4) of the Code, excess contributions made during a taxable year may be distributed from an IRA tax-free if they are received on or before the due date (including extensions of time) for filing the individual's income tax return, if no deduction is allowed under section 219 as to the excess contributions, and if the distribution is accompanied by the amount of net income attributable to it. Such net income is includible in the individual's gross income for the taxable year in which the excess contribution is made.

In *Situation 1*, the single-sum distribution from *S*'s eligible state deferred compensation plan was paid to *A* in 1985. That amount is includible in *A*'s gross income for 1985 under section 457(a) of the Code, and does not qualify as a rollover amount under section 402(a)(5), 402(a)(7), 403(a)(4), 403(b)(8), or 408(d)(3). Accordingly, for purposes of section 4973(a), the total amount of contributions made to the IRA for 1985 exceeds the maximum amount allowable as a deduction under section 219 ($2,000) by the amount of the single-sum distribution.

In *Situation 2*, the analysis is identical to that for *Situation 1* except that the single-sum distribution from *S*'s plan was constructively received by *A* in 1985, because this amount, although not actually received, was made available in 1985 to *A* without any substantial limitations or restrictions. Section 451(a) of the Code and section 1.451-2(a) of the regulations. Therefore, the single-sum distribution is includible in *A*'s gross income for 1985 under section 457(a) of the Code and does not qualify as a rollover amount under section 402(a)(5), 402(a)(7), 403(a)(4), 403(b)(8), or 408(d)(3).

HOLDING

In both *Situation 1* and *Situation 2*, *A* must include in gross income for the year 1985 the amount of the single-sum distribution received or made available from *S*'s eligible state deferred compensation plan. *A* is entitled to a maximum deduction of $2,000 for contributions to the IRA for 1985. In addition, *A* is liable for the tax imposed by section 4973(a) of the Code on the amount of the single-sum distribution to the extent that the requirements of section 408(d)(4) are not met.

Section 547.—Deduction for Deficiency Dividends

26 CFR 1.547-2: Requirements for deficiency dividends.

Personal holding companies; extension of time to distribute dividends. A personal holding company cannot receive an extension of time as described under section 1.9100-1 of the regulations for a failure to timely distribute a deficiency dividend as described under section 547 of the Code.

Rev. Rul. 86-104

ISSUE

Can a personal holding company be granted an extension of time pursuant to section 1.9100-1 of the Income Tax Regulations in order for a distribution of dividends to qualify as "deficiency dividends" under section 547 of the Internal Revenue Code?

FACTS

X is a corporation all of whose issued and outstanding stock is owned by one individual. Because its income consists of interest and dividends and more than 50 percent in value of its outstanding stock is owned by one individual, *X* is a personal holding company within the meaning of section 542 of the Code. During the taxable year *X* failed to pay any dividends to its shareholder and as a result had a large amount of undistributed personal holding company income. *X* and the Internal Revenue Service reached an agreement concerning *X's* liability for the personal holding company tax imposed by section 541. After receiving X's signed acceptance of the terms of the agreement, the district director sent a registered letter to *X* evidencing acceptance of the agreement by the Internal Revenue Service and setting forth the procedures for the distribution of "deficiency dividends" as defined in section 547(d)(1). However, *X* failed to make such a distribution within 90 days after the date of registration of the letter.

LAW AND ANALYSIS

Section 541 of the Code provides that in addition to other taxes imposed by this chapter, there is imposed for each taxable year on the undistributed personal holding company income (as defined in section 545) of every personal holding company a personal holding company tax equal to 50 percent of the undistributed personal holding company income.

Section 547(a) of the Code provides that if a determination (as defined in section 547(c)) with respect to a taxpayer establishes liability for personal holding company tax imposed by section 541 (or by a corresponding provision of a prior income tax law) for any taxable year, a deduction shall be allowed to the taxpayer for the amount of deficiency dividends (as defined in section 547(d)) for the purpose of determining the personal holding company tax for such year, but not for the purpose of determining interest, additional amounts, or assessable penalties computed with respect to such personal holding company tax.

Section 547(c) of the Code provides that, for purposes of section 547, the term "determination" means: (1) a decision by the Tax Court or a judgment, decree, or other order by any court of competent jurisdiction, that has become final; (2) a closing agreement made under section 7121; or (3) under regulations prescribed by the Secretary, an agreement signed by the Secretary and by, or on behalf of, the taxpayer relating to the liability of the taxpayer for personal holding company tax.

Section 547(d)(1) of the Code provides that, for purposes of section 547, the term "deficiency dividends" means the amount of the dividends paid by the corporation on or after the date of the determination and before filing a claim under section 547(e), which would have been includible in the computation of the deduction for dividends paid under section 561 for the taxable year for which the liability for personal holding company tax exists, if distributed during such taxable year. No dividends shall be considered as deficiency dividends for purposes of section 547(a) unless distributed within 90 days after the determination.

Section 1.547-2(b)(1)(v) of the regulations provides that a determination under section 547(c)(3) of the Code may be made by an agreement signed by the district director or such other official to whom authority to sign the agreement is delegated, and by or on behalf of the taxpayer. The agreement shall set forth the total amount of the liability for personal holding company tax for the taxable year or years. An agreement under section 1.547-2(b)(1)(v) that is signed by the district director (or such other official to whom authority to sign the agreement is delegated) on or after July 15, 1963, shall be sent to the taxpayer at the taxpayer's last known address by either registered or certified mail. If registered mail is used for such purpose, the date of registration shall be treated as the date of determination, unless the dividend is paid by the corporation before the postmark date.

Under section 1.9100-1 of the regulations, the Commissioner has discretion, upon a showing of good cause by a taxpayer, to grant a reasonable extension of the time fixed by the regulations to make an election or other application for relief in respect of tax under subtitle A of the Code. The extension may not be granted if the time for making the election or application is expressly prescribed by law.

Rev. Proc. 79-63, 1979-2 C.B. 578, sets forth certain considerations that the Internal Revenue Service generally will use to determine whether, under the facts and circumstances of each situation, good cause for granting an extension of time fixed by the regulations to make an election or application has been shown and the other requirements of section 1.9100-1 of the regulations have been met. Section 3 of Rev. Proc. 79-63 provides that the scope of that revenue procedure is limited to requests for extensions of time fixed by the regulations for making on election and to applications for relief, in accordance with the specific language of section 1.9100-1. Thus the revenue procedure does not apply to requests for extensions of the time fixed by the Code for making an election or to applications for relief from statutory deadlines.

Section 547(d) of the Code sets a fixed period (90 days) within which the taxpayer must act following any of three types of determination, as defined in section 547(c). Section 1.547-2(b)(1) of the regulations merely clarifies when the determination occurs. Thus, it is the statute and not the regulations that fixes the time within which the dividend must be distributed if the personal holding company tax is to be avoided. The Commissioner has authority to clarify ambiguity in a statute by regulation (for example, the date on which a determination occurs and the 90-day period begins). However, the Commissioner does not have authority to extend a time period specified by statute unless the statute confers such authority. For an example of such authority, see section 338(g)(1).

HOLDING

The personal holding company cannot be granted an extension of time pursuant to section 1.9100–1 of the regulations in order for a distribution of dividends to qualify as deficiency dividends under section 547 of the Code.

Section 661.—Deduction for Estates and Trusts Accumulating Income or Distributing Corpus

26 CFR 1.661(a)–2: Deduction for distributions to beneficiaries.

Whether a distribution of assets equal to an amount specified in decedent's will is a distribution in satisfaction of a right to receive a distribution in a specific dollar amount. And whether the estate recognizes gain or loss on the distribution. See Rev. Rul. 86–105, below.

Section 662.—Inclusion of Amounts in Gross Income of Beneficiaries of Estates and Trusts Accumulating Income or Distributing Corpus

Whether a distribution of assets in an amount equal to an amount specified in decedent's will is included in the gross income of the distributee. See Rev. Rul. 86–105, below.

Section 663.—Special Rules Applicable to Sections 661 and 662

26 CFR 1.663(a)–1: Special rules applicable to sections 661 and 662; exclusions; gifts, bequests, etc. (Also Sections 661, 662; 1.661(a)–2.)

Estates; distributions of assets equal to stated fair market value. A bequest of unspecified assets with a fair market value specified in decedent's will is a bequest of a "specified sum of money" under section 663(a) of the Code. Furthermore, the bequest creates a right to receive a specific dollar amount the satisfaction of which results in the recognition of gain or loss to the estate.

Rev. Rul. 86–105

ISSUE

1. Whether a bequest of "assets, in cash or in kind or partly in each," with a fair market value at date of distribution equal to a specified amount is a bequest of a "specific sum of money" under section 663(a) of the Internal Revenue Code.

2. Whether such a bequest creates a right to receive a "specific dollar amount" described in section 1.661(a)–2(f)(1) of the regulations whose satisfaction by a distribution of property in kind will result in the realization of gain or loss by the estate.

FACTS

The decedent's will created a trust with the following provisions:

> I give assets, in cash or in kind or partly in each, the selection of which shall be in the absolute discretion of my executor, with a fair market value at the date of distribution equal to 2,000x dollars, to the trustee hereinafter named, to be held, administered and distributed as hereinafter provided.

On the date of distribution, the executor satisfied the bequest by transferring to the trust securities of *X* corporation that had been owned by the decedent and had a fair market value of 2,000x dollars and an adjusted basis of 2,500x dollars.

LAW AND ANALYSIS

Section 661(a) of the Internal Revenue Code allows as a deduction (not in excess of the distributable net income of the estate) in computing the taxable income of an estate, the sum of (1) any amount of income for such taxable year required to be distributed currently; and (2) any other amounts properly paid or credited or required to be distributed for such taxable year.

Section 663(a) of the Code provides that there shall not be included as amounts falling within section 661(a) and 662(a) any amount that, under the terms of the governing instrument, is properly paid or credited as a bequest of a specific sum of money or of specific property and that is paid or credited all at once or in not more than three installments

Section 1.663(a)–1(b)(1) of the Income Tax Regulations provides that in order to qualify as a gift or bequest of a specific sum of money or of specific property under section 663(a), the amount of money or the identity of the specific property must be ascertainable under the terms of a testator's will as of the date of death.

In this case, the decedent made a bequest of assets of a specified monetary value to be conveyed by the executor in cash or in kind, or partly in each, as the executor might determine. Since the monetary value of the bequest is ascertainable under the terms of the will as of the date of the decedent's death (subject only to availability of assets in the estate to satisfy the bequest), the bequest is of a specific sum of money for purposes of section 663(a) of the Code, notwithstanding that it may be paid in property other than money. See Rev. Rul. 82–4, 1982–1 C.B. 99, and Rev. Rul. 66–207, 1966–2 C.B. 243. Consequently, the estate is not allowed a deduction under section 661(a) of the Code in computing the taxable income of the estate when it pays the bequest.

Section 1.661(a)–2(f)(1) of the regulations provides that gain or loss is realized by the estate by reason of a distribution of property in kind if the distribution is in satisfaction of a right to receive a distribution in a specific dollar amount or in specific property other than that distributed.

Section 643(d)(3) of the Code provides an estate with an election to recognize gain or loss in the case of distributions of property. If the estate does not elect to recognize gain or loss, the basis of the property received by the beneficiary is generally the same as the estate's basis immediately before the distribution. As reflected in the legislative history of the Tax Reform Act of 1984, however, this election does not apply in those cases where a distribution of property results in recognition of gain or loss to the estate without regard to the enactment of section 643(d).

Since the distribution of the securities by the executor to the trustee is in satisfaction of a right to receive a "specific dollar amount" of 2,000x dollars, the satisfaction causes the estate to realize gain or loss under section 1.661(a)–2(f)(1) of the regulations. The executor transferred to the trust assets in kind that have depreciated from 2,500x dollars in satisfaction of the trust's right to receive a distribution in a specific dollar amount of 2,000x dollars. Therefore, the estate will realize a loss of 500x dollars (2,000x - 2,500x dollars) on the distribution of the shares of stock.

Section 662(a) of the Code provides rules for including in the gross income of a beneficiary of an estate described in section 661 the amounts specified in section 661(a) that are paid, credited, or required to be distributed. As noted above, section 663(a) of the Code provides that any amount that, under the terms of the governing instrument, is properly paid or credited as a bequest of a specific sum of money is not included in section 662(a). Consequently, the beneficiary does not include any amount in gross income under section 662(a) of the Code upon receipt of the bequest.

HOLDING

1. A bequest of "assets, in cash or in kind or partly in each," with a fair market value at date of distribution equal to a specified amount is a bequest of a "specific sum of money" under section 663(a) of the Code.

2. The bequest of unspecified property with a specified value at the date of distribution creates a right to receive a "specific dollar amount" under section 1.661(a)–2(f)(1) of the regulations. Therefore, gain or loss is realized by the estate upon a distribution in kind.

Section 4973.—Tax on Excess Contributions to Individual Retirement Accounts, Certain Section 403(b) Contracts, and Certain Individual Retirement Annuities

Whether a single-sum cash distribution from an eligible state deferred compensation plan may be rolled over on a tax-free basis to an individual retirement account. See Rev. Rul. 86–103, page 13.

Section 7872.—Treatment of Loans with Below-market Interest Rates

26 CFR 1.7872T: Exempted loans. (Temporary)

T.D. 8093

TITLE 26—INTERNAL REVENUE.—
CHAPTER I, SUBCHAPTER A, PART
1—INCOME TAX; TAXABLE YEARS
BEGINNING AFTER DECEMBER 31,
1953

Below-market loans

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains amendments to temporary regulations which were published August 20, 1985 in the Federal Register [1985–2 C.B. 343], relating to the Federal tax treatment of both the lender and the borrower in certain below market interest rate loan transactions. Changes to the applicable law were made by the Tax Reform Act of 1984. The regulations amend several of the exemptions set forth in the temporary regulations.

DATES: The regulations apply to below-market term loans made after June 6, 1984, and below-market demand loans outstanding after June 6, 1984, and are effective June 6, 1984.

FOR FURTHER INFORMATION CONTACT: Sharon L. Hall of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T), 202-566-3828, not a toll-free call.

SUPPLEMENTARY INFORMATION: BACKGROUND

This document amends temporary Income Tax Regulations (26 CFR Part 1) under section 7872 of the Internal Revenue Code of 1954.

IN GENERAL

Section 7872 treats certain below-market loans as economically equivalent to loans bearing interest at the applicable Federal rate coupled with a payment by the lender to the borrower sufficient to fund the payment of interest by the borrower. The temporary regulations published August 20, 1985 in the Federal Register provide for the exemption of certain below-market loans from the rules of section 7872 on the grounds that the application of section 7872 would not have a significant effect on any Federal tax liability of the lender or the borrower. If, however, one of the exempted loans is structured as such for tax avoidance purposes, the Service may recharacterize the transaction according to its economic substance and apply section 7872 in accordance with its terms. The exemptions include:

(1) loans made prior to July 1, 1986, to the extent excepted from the application of section 482 for the 6-month (or longer) period referred to in §1.482–2(a)(3);

(2) for periods prior to July 1, 1986, all money securities, and property received by a futures commission merchant or by a clearing organization (i) to margin, guarantee or secure contracts for future delivery on or subject to the rules of a qualified board or exchange (as defined in section 1256(g)(7)) or (ii) to purchase, margin guarantee or secure options contracts traded on or subject to the rules of a qualified board or exchange, and all money accruing to account holders as the result of such futures and options contracts; and

(3) loans to a charitable organization (described in section 170(c)), but only if the aggregate outstanding amount of loans by the lender to all such organizations does not exceed $10,000 at any time during the taxable year.

EXEMPTION FOR LOANS EXCEPTED UNDER SECTION 482

Commentators suggested that the exemption for loans made prior to July 1, 1986, to the extent excepted from the application of section 482 for the 6-month (or longer) period referred to in §1.482–2(a)(3) be made permanent. The Service believes that the treatment of transactions which would fall within the application of both section 482 and section 7872 should be consistent. Therefore, to the extent that a loan subject to section 482 will not have interest imputed under §1.482–2(a)(3), it is exempt from section 7872.

EXEMPTION FOR MONEY, SECURITIES AND PROPERTY RECEIVED BY FUTURES COMMISSIONS MERCHANTS, ETC.

Commentators suggested that the exemption for money, securities and property deposited with a futures commission merchant or with a clearing organization be made permanent. The Service has concluded that the interest arrangements of such deposits do not have a significant effect on the Federal tax liability of the borrower or lender. Accordingly, this document removes the limitation that only money, securities and property received prior to July 1, 1986 are exempt from the application of section 7872. Additionally, the regulations extend the exemption to margin payments received by a stockbroker and to clearing funds deposits.

The continued exemption from the below-market loan rules for these types of deposits reflects current practice with respect to such deposits, under which the level of commissions charged to customers is not based on whether deposits are made in the form of money or interest-bearing securities. If current practice evolves in the direction of large interest-free cash deposits and lower commissions to attempt to obtain an indirect deduction for commission expenses, the Service will reconsider whether this exemption is warranted.

EXEMPTIONS FOR LOANS TO CHARITABLE ORGANIZATIONS

Commentators suggested that the exemption for loans to a charitable organization be modified to apply the de minimis limitation to loans to each such organization, rather than to all such organizations. The Service has concluded that such a modification is appropriate and that the interest arrangements of gift loans subject to such limits will not have a significant effect on the Federal tax liability of the borrower or lender. The Service has additionally concluded that if loans to a charitable organization are not greater than $250,000 the interest arrangements of such loans will not have a significant effect on the Federal tax liability of the borrower or lender.

INAPPLICABILITY OF EXECUTIVE ORDER 12291

The Treasury Department has determined that these temporary regulations are not subject to review under Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

REGULATORY FLEXIBILITY ACT

A general notice of proposed rulemaking is not required by 5 U.S.C. 553 for temporary regulations. Accordingly, these temporary regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6.)

DRAFTING INFORMATION

The principal author of these regulations is Sharon L. Hall of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations on matters of both substance and style.

* * * * *

Amendments to the regulations.

The amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority for part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * * Section 1.7872–5T also issued under 26 U.S.C. 7872.

Par. 2. Section 1.7872–5T(b) is amended by revising paragraph (b)(9), (12) and (13) to read as follows.

§1.7872–5T Exempted Loans (Temporary)

* * * * *

(b) * * *

(9) Gift loans to a charitable organization (described in section 170(c)), but only if at no time during the taxable year will the aggregate outstanding amount of loans by the lender to that organization exceed $250,000. Charitable organizations which are effectively controlled, within the meaning of section 1.482–1(a)(1), by the same person or persons shall be considered one charitable organization for purposes of this limitation.

* * * * *

(12) Any loan excepted from the application of section 482 for the period referred to in §1.482–2(a)(3).

(13) All money, securities, and property—

(i) Received by a futures commission merchant or registered broker/dealer or by a clearing organization (A) to margin, guarantee or secure contracts for future delivery on or subject to the rules of a qualified board or exchange (as defined in section 1256(g)(7)), or (B) to purchase, margin, guarantee or secure options contracts traded on or subject to the rules of a qualified board or exchange, so long as the amounts so received to purchase, margin, guarantee or secure such contracts for future delivery or such options contracts are reasonably necessary for such purposes and so long as any commissions received by the futures commission merchant, registered broker/dealer, or clearing organization are not reduced for those making deposits of money, and all money accruing to account holders as the result of such futures and options contracts or

(ii) Received by a clearing organization from a member thereof as a required deposit to a clearing fund, guaranty fund, or similar fund maintained by the clearing organization to protect it against defaults by members.

There is need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue this Treasury decision with notice and public procedure under section (b) of section 553 of Title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

JAMES I. OWENS,
Acting Commissioner of Internal Revenue.

Approved June 30, 1986.

J. ROGER MENTZ,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on July 9, 1986, 8:45 a.m., and published in the issue of the Federal Register for July 10, 1986, 51 F.R. 25033, and corrected in the issue of the Federal Register for August 8, 1986, 51 F.R. 28553)

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.105: Examination of returns and claims for refund, credit, or abatement, determination of correct tax liability.
(Also Part I, Section 46; 1.46–1).

Rev. Proc. 86–36

SECTION 1. PURPOSE

.01 Section 46(e)(3) of the Internal Revenue Code places certain limitations on the availability of the investment tax credit (ITC) to noncorporate lessors. A noncorporate lessor is not allowed an ITC for property that the lessor has not manufactured or produced unless, among other requirements, the lease for the property is for a term (taking into account options to renew) that is less than 50 percent of that property's "useful life." In the case of recovery property (within the meaning of section 168), the useful life is the present class life for the property (as defined in section 168(g)(2)). The Secretary of the Treasury, however, has not prescribed a present class life for all property that qualifies as recovery property. This revenue procedure provides guidance on the application of section 46(e)(3) to such property.

SEC. 2. BACKGROUND

.01 A noncorporate lessor of property may claim the ITC for the property only if it meets the requirements of section 46(e)(3) of the Code. Under this section, a noncorporate lessor that is not the manufacturer or producer of the property must lease the property for a term that is less than 50% of the property's useful life. Section 211(d) of the Economic Recovery Tax Act of 1981, 1981-2 C.B. 256, 287, added the last sentence of section 46(e)(3), which provides: "In the case of any recovery property (within the meaning of section 168), the useful life shall be the present class life of such property (as defined in section 168(g)(2))."

.02 Section 168(g)(2) of the Code defines "present class life" as the class life (if any) which would be applicable with respect to any property as of January 1, 1981, under section 167(m). A list of all asset guideline classes and their present class lives as of January 1, 1981, is provided by Rev. Proc. 83–35, 1983–1 C.B. 745. The Tax Reform Act of 1984, section 31(d), 1984–3(Vol. 1) C.B. 26, added the following sentence at the end of section 168(g)(2): "If any property (other than section 1250 class property) does not have a present class life within the meaning of the preceding sentence, the Secretary may prescribe a present class life for such property which reasonably reflects the anticipated useful life of such property to the industry or other group."

.03 Rev. Proc. 83–35 sets forth not only the asset guideline classes and present class lives as of January 1, 1981, but also asset guideline depreciation periods and ranges and annual asset guideline repair allowance percentages for the Class Life Asset Depreciation Range (CLADR) System established under section 167(m) of the Code. Rev. Proc. 83–35 provides that the present class life for property included in an asset guideline class is the asset guideline period (midpoint class life) established for the class as of January 1, 1981. Because the CLADR system is not available for recovery property, no additional asset guideline classes have been established. To date, present class lives have not been prescribed for property that is not included in any of the asset guideline classes described in Rev. Proc. 83–35.

SEC. 3. CRITERION FOR DETERMINING THE MAXIMUM LEASE TERM PERMISSIBLE UNDER SECTION 46(e)(3) OF THE CODE FOR RECOVERY PROPERTY THAT HAS NO PRESENT CLASS LIFE

.01 Solely for the purpose of determining the maximum term of a lease permissible under section 46(e)(3) of the Code, for recovery property for which the Secretary has not prescribed a present class life, the estimated useful life of the property, determined at the time the property is placed in service, should be used.

.02 The rules for determining the estimated useful life of property without a present class life for purposes of section 46(e)(3) of the Code shall be the same as the rules provided by section 1.167(a)–1(b) of the Income Tax Regulations for determining the estimated useful life of property for purposes of depreciation.

.03 If, subsequent to the publication of this revenue procedure, the Secretary prescribes a present class life for any recovery property, the estimated useful life may not be used for that property for the purpose of determining the maximum term of the lease under section 46(e)(3) of the Code. However, present class lives prescribed subsequent to the publication of this revenue procedure will not apply retroactively.

SEC. 4. EFFECTIVE DATE

This revenue procedure applies to leases entered into after June 25, 1981, the effective date of the last sentence of section 46(e)(3).

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Basis of Target Corporation Assets

LR–191–82

SUMMARY: * * * [T]he Internal Revenue Service is issuing temporary regulations [page 5, this Bulletin] that add new §1.338(b)–4T to provide transitional rules relating to allocation of basis to new target's assets if an election is made under section 338 and that amend existing temporary regulations under section 338. The text of the new section also serves as the comment document for this notice of proposed rulemaking.

DATES:

Proposed effective date—The regulations are proposed to apply generally to stock acquisitions made after August 31, 1982.

Date for comments and requests for a public hearing—Written comments and requests for a public hearing must be delivered or mailed by September 2, 1986.

ADDRESS: Send commends and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T [LR–191–82], Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Patricia Wendlandt of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) or telephone 202-566-3458 (not a toll-free number).

SUPPLEMENTARY INFORMATION:
BACKGROUND

Temporary regulations * * * [page 5, this Bulletin] add new temporary regulations §1.338(b)–4T to Part 1 of Title 26 of the Code of Federal Regulations ("CFR") and amend existing temporary regulations under section 338. The final regulations that are proposed to be based on the new and amended temporary regulations would be added to Part 1 of Title 26 of the CFR. Those final regulations would provide guidance on the allocation of basis among the assets of a target corporation the stock of which was acquired in a qualified stock purchase after August 31, 1982, and before January 30, 1986, for which an election is made under section 338 of the Internal Revenue Code. Section 338(b) was added by section 224 of the Tax Reform and Fiscal Responsibility Act of 1982 ("TLFRA") (Pub. L. 97-248; 96 Stat. 485) and was amended by section 712(k) of the Tax Reform Act of 1984 (Pub. L. 98–369; 98 Stat. 948). For the text of the new and amended regulations, see T.D. 8092, * * * [page 5, this Bulletin]. The preamble to the temporary regulations explains the additions to the regulations.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6). The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before these proposed regulations are adopted, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the Federal Register. The collection of information requirements contained herein have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on the requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests persons submitting comments to OMB to also send copies of the comments to the Service.

DRAFTING INFORMATION

The principal author of these proposed regulations is Patricia Wendlandt of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

JAMES I. OWENS,
Acting Commissioner
of Internal Revenue

(Filed by the Office of the Federal Register on June 27, 1986, 10:10 a.m., and published in the issue of the Federal Register for July 1, 1986, 51 F.R. 23790)

Notice of Proposed Rulemaking

Installment Method Reporting by Dealers in Personal Property

LR–141–83

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to installment method reporting by dealers in personal property. Changes to the applicable tax law were made by the Installment Sales Revision Act of 1980. These proposed regulations would affect all dealers in personal property that report income from sales on the installment method and would provide them with the guidance to comply with the law.

DATES: Written comments and requests for a public hearing must be delivered or mailed by September 26, 1986. The amendments are proposed to take effect on October 20, 1980, and would apply to taxable years ending on or after that date.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR–141–83) Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Paulette Chernyshev of the

Legislation and Regulations Division. Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T), (202-566-3288), not a toll-free call).

SUPPLEMENTARY INFORMATION: BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) to provide rules under section 453A of the Internal Revenue Code of 1954 relating to installment method reporting by dealers in personal property. These amendments are proposed to reflect the addition of section 453A to the Code by the Installment Sales Revision Act of 1980 (94 Stat. 2247).

Prior to the enactment of the Installment Sales Revision Act of 1980, section 453 of the Code contained all of the rules relating to installment method reporting, including the rules applicable to dealers in personal property. Consequently, the regulations under old section 453 apply both to casual installment sales and installment sales by dealers in personal property. The amendments proposed in this document generally adopt the provisions of the old section 453 regulations that relate to installment method reporting by dealers in personal property.

Because the Installment Sales Revision Act amended the rules provided in old section 453(c), which related to dealers that changed from the accrual method to the installment method, the proposed amendments do not adopt the portion of the regulations relating to old section 453(c). Regulations on this subject will be proposed in a different project (LR-146-81).

TWO-PAYMENT RULE

The Senate Finance Committee Report suggested that Treasury regulations might eliminate the two-payment rule for dealers. In December 1980, Senator Long (then the chairman of the Senate Finance Committee) clarified the Report:

> It will be noted that prior law limited the use of the installment method to dealers who sell 'on the installment plan.' The same limitation is contained in new section 453A, and there was no intention to eliminate this statutory requirement. The point of the quoted sentence from the committee report was that in reviewing the regulations as to what constitutes an 'installment plan,' it is anticipated that the Treasury Department will consider the question of whether there are circumstances in which reliance on the two-payment rule is excessively formalistic. On the other hand, however, there is no intention that dealer transactions which do not meet the ordinary understanding of sales on the 'installment plan' are to qualify for the installment method. 126 CONG. REC. S16536 (daily ed. Dec. 13, 1980) (remarks of Sen. Long).

The Treasury Department has concluded that the two-payment rule serves to distinguish installment plan sales from ordinary 30-day account sales. Accordingly, no change has been made to the two-payment requirement for sales on the installment plan by dealers in personal property.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required. Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the notice and public procedure requirements of 5 U.S.C. 553 do not apply because the rules proposed herein are interpretative. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

DRAFTING INFORMATION

The principal author of these proposed regulations is Phoebe A. Mix of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury participated in developing the regulations on matters of substance and style.

Proposed amendments to the regulations

The proposed amendments to 26 CFR Part 1 are as follows:

INCOME TAX REGULATIONS (26 CFR Part 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.453A-1 and §1.453A-2 also issued under 26 U.S.C. 453A.

Par. 2. Section 1.453-1 is redesignated as §1.453A-1 and revised to read as follows:

§1.453A-1 Installment method of reporting income by dealers in personal property.

In general Section 453A permits dealers in personal property, that is, persons who regularly sell or otherwise dispose of personal property on the installment plan, to elect to return the income from the sale or other disposition thereof on the installment method. To the extent provided in paragraph (d) of §1.453A-2, sales under a revolving credit type plan will be treated as sales on the installment plan and the income from the sales so treated may be returned on the installment method. A dealer who makes sales of personal property under both a revolving credit plan and a traditional installment plan may elect to report only sales under the traditional installment plan on the installment method; or he may elect to report only sales under the revolving credit plan on the installment method; or he may elect to report both sales under the revolving credit plan and the traditional installment plan on the installment method. A traditional installment plan usually has the following characteristics:

(a) The execution of a separate installment contract for each sale of personal property, and

(b) The retention by the dealer of some type of security interest in such property.

Par. 3. Section 1.453-2 is redesignated as §1.453A-2 and revised to read as follows:

§1.453A-2 Special rules applicable to dealers in personal property.

(a) *In general.* A person who regularly sells personal property on the installment plan may adopt (but is not required to do so) one of the following four ways of protecting his interest in case of default by the purchaser;

(1) By an agreement that title is to remain in the vendor until the purchaser has completely performed his part of the transaction;

(2) By a form of contract in which title is conveyed to the purchaser immediately, but subject to a lien for the unpaid portion of the selling price;

(3) By a present transfer of title to the purchaser, who at the same time executes a reconveyance in the form of a chattel mortgage to the vendor; or

(4) By conveyance to a trustee pending performance of the contract and subject to its provisions;

(b) *Definition of sale on the installment plan*. The term "sale on the installment plan" means—

(1) A sale of personal property by the taxpayer under any plan for the sale or other disposition of personal property, which plan, by its terms and conditions, contemplates that each sale under the plan will be paid for in two or more payments, or

(2) A sale of personal property by the taxpayer under any plan for the sale or other disposition of personal property—

(1) Which plan, by its terms and conditions, contemplates that such sale will be paid for in two or more payments, and

(ii) Which sale is in fact paid for in two or more payments.

Normally, a sale under a traditional installment plan (as described in §1.453A-1 meets the requirements of subparagraph (1) of this paragraph. See paragraph (d) of this section for the application of the requirements of subparagraph (2) of this paragraph to sales under revolving credit plans.

(c) *Installment income of dealers in personal property*—(1) *In general*. The income from sales on the installment plan of a dealer, that is, a person regularly engaged in the sale of personal property on the installment plan, may be ascertained by treating as income that proportion of the total payments received in the taxable year from sales on the installment plan (such payments being allocated to the year against the sales of which they apply) which the gross profit realized or to be realized on the total sales on the installment plan made during each year bears to the total contract price of all such sales made during that respective year. However, if the dealer demonstrates to the satisfaction of the district director that income from sales on the installment plan is clearly reflected, the income from such sales may be ascertained by treating as income that proportion of the total payments received in the taxable year from sales on the installment plan (such payments being allocated to the year against the sales of which they apply) which either (i) the gross profit realized or to be realized on the total credit sales made during each year bears to the total contract price of all credit sales during that respective year, or (ii) the gross profit realized or to be realized on all sales made during each year bears to the total contract price of all sales made during that respective year. See, however, paragraph (d)(6)(vi) of this section for rules permitting, under certain circumstances, all sales under a revolving credit plan to be considered as having been made in the taxable year. A dealer who desires to compute income by the installment method shall maintain accounting records in such a manner as to enable an accurate computation to be made by such method in accordance with the provisions of this secton, section 446, and §1.446-1.

(2) *Gross profit and total contract price*. For purposes of subparagraph (1) of this paragraph, in computing the gross profit realized or to be realized on the total sales on the installment plan, there shall be included in the total selling price and, thus, in the total contract price of all such sales.

(i) The amount of carrying charges or interest which is determined at the time of each sale and is added to the established cash selling price of such property and is treated as part of the selling price for customer billing purposes, and

(ii) In the case of sales made in taxable years beginning on or after January 1, 1960, the amount of carrying charges or interest determined with respect to such sales which are added contemporaneously with the sale on the books of account of the seller but are treated as periodic service charges for customer billing purposes. Any charge in the amount of the carrying charges or interest in a year subsequent to the sale will not affect the computation of the gross profit for the year of sale but will be taken into account at the time the carrying charges or interest are adjusted. However, this subparagraph does not apply to sales of personal property under a revolving credit plan described in paragraph (d)(1) of this section. The application of this subparagraph to carrying charges or interest described in subdivision (ii) of this subparagraph may be illustrated by the following example:

Example: X Corporation makes sales on the traditional installment plan. The customer's order specifies that the total price consists of a cash price plus a "time price differential" of 1½ percent per month on the outstanding balance in his account and he is billed in this manner. On its books and for purposes of reporting to stockholders, X Corporation consistently makes the following entries each month when it records its sales. A debit entry is made to accounts receivable (for the total price) and balancing credit entries are made to sales (for the established selling price) and to a reserve account for collection expense (for the amount of the time price differential) In computing the gross profit realized or to be realized on the total sales on the installment plan, the total selling price and, thus, the total contract price for purposes of this paragraph would with respect to sales made in taxable years beginning on or after January 1, 1960, include the time price differential.

(3) *Carrying charges not included in total contract price*. In the case of sales by dealers in personal property made during taxable years beginning after December 31, 1963, the income from which is returned on the installment method, if the carrying charges or interest with respect to such sales is not included in the total contract price, payments received with respect to such sales shall be treated as applying first against such carrying charges or interest. For application of this rule to revolving credit sales, see paragraph (d)(6)(v) of this section.

(d) *Revolving credit plans*. (1) To the extent provided in this paragraph, sales under a revolving credit plan will be treated as sales on the installment plan. The term "revolving credit plan" includes cycle budget accounts, flexible budget accounts, continuous budget accounts, and other similar plans or arrangements for the sale of personal property under which the customer agrees to pay each billing-month (as defined in subparagraph (6)(iii) of this paragraph) as part of the outstanding balance of his account. Sales under a revolving credit plan do not constitute sales on the installment plan merely by reason of the fact that the total debt at the end of a billing-month is paid in installments. The terms and conditions of a revolving credit plan do not contemplate that each sale under the plan will be paid for in two or more payments and thus do not meet the requirements of paragraph (b)(1) of this section. In addition, since under a revolving credit plan payments are not generally applied to liquidate any particular sale, and since the terms and conditions of such plan contemplate that account balances may be paid in full or in installments, it is generally impossible to determine that a particular sale under a revolving credit plan is to be or is in fact paid for in installments so as to meet the requirments of paragraph (b)(2) of this section. However, subparagraphs (2) and

(3) of this paragraph provide rules under which a certain percentage of charges under a revolving credit plan will be treated as sales on the installment plan. For purposes of arriving at this percentage, these rules, in general, treat as sales on the installment plan those sales under a revolving credit plan (1) which are of the type which the terms and conditions of the plan contemplate will be paid for in two or more installments and (2) which are charged to accounts on which subsequent payments indicate that such sales are being paid for in two or more installments.

(2)(i) The percentage of charges under a revolving credit plan which will be treated as sales on the installment plan shall be computed by making an actual segregation of charges in a probability sample of the revolving credit accounts and by applying the rules contained in subparagraph (3) of this paragraph to determine what percentage of charges in the sample is to be treated as sales on the installment plan. (See subparagraph (5) of this paragraph for rules to be used of some of the sales under a revolving credit plan are nonpersonal property sales (as defined in subparagraph (6)(iv) of this paragraph).) Such segregation shall be made of charges which make up the balances in the sample accounts as of the end of each customer's last billing-month ending within the taxable year. (See subparagraph (6)9v) of this paragraph of rules to be used in determining which charges make up the balance of an account.) However, in making such segregation, any account to which a sale is charged during the taxable year on which no payment is credited after the billing-month within which the sale is made (hereinafter called the "billing-month" of sale") and on or before the end of the first billing-month ending in the taxpayer's next taxable year shall be disregarded and not taken into account in the determination of what percentage of charges in the sample is to be treated as sales on the installment plan. In order to obtain a probability sample, the accounts shall be selected in accordance with generally accepted probability sampling techniques. The appropriateness of the sampling technique and the accuracy and reliability of the results obtaned must, if requested, be demonstrated to the satisfaction of the district director. If the district director is not satisfied that the taxpayer's sample is appropriate or that the results obtained are accurate and reliable, the taxpayer shall recompute his sample percentage or make appropriate adjustments to his original computations in a manner satisfactory to the district director. The taxpayer shall maintain records in sufficient detail to show the method of computing and applying the sample.

(ii) For taxable years ending before January 31, 1964, a taxpayer who has reported for income tax purposes all or a portion of sales under a revolving credit plan as sales on the installment method may apply the percentage obtained for the first taxable year ending on or after such date in determining the percentage of charges under a revolving credit plan for such prior taxable year (or years) which will be treated as sales on the installment plan. However, in computing the percentage to be applied in determining the percentage of charges under a revolving credit plan which will be treated as sales on the installment plan for such prior taxable year or years), the rule stated in paragraph (c)(3) of this section shall not apply. See subparagraph (6)(v) of this paragraph for rules relating to the application of payments to finance charges for such prior taxable years.

(3) For the purpose of determining the percentage described in subparagraph (2) of this paragraph, a charge under a revolving credit plan will be treated as a sale on the installment plan only if such charge is a sale (as defined in subparagraph (6)(i) of this paragraph) and meets the requirments contained in subdivisions (i) and (ii) of this subparagraph.

(i) The sale must be of the type which the terms and conditions of the plan contemplate will be paid for in two or more installments. If the aggregate of sales charged during a billing-month to an account under a revolving credit plan exceeds the required monthly payment, then all sales during such billing-month shall be considered to be of the type which the terms and conditions of such plan contemplate will be paid for in two or more installments. The required monthly payment shall be the amount of the payment which the terms and conditions of the revolving credit contract require the customer to make with respect to a billing-month. If the amount of such payment is not fixed at the date the contract is entered into, but is dependent upon the balance of the account, then such amount shall be the amount that the customer is required to pay (but not including any past-due payments) as shown on the statement either (*a*) for the last billing-month ending within the taxpayer's taxable year or (*b*) for the billing-month of sale, whichever method the taxpayer adopts for all his accounts. A taxpayer shall not change such method of determining the required monthly payment based upon the balance of the account without obtaining the consent of the district director. In any case where the required monthly payment is not set in accordance with a consistent method used during the entire taxable year, the district director may determine the required monthly payment in accordance with the method used during the major portion of such taxable year if he determines that the use of such method is necessary in order to reflect properly the income from sales under a revolving credit plan. The requirements stated in this subdivision may be illustrated by the following examples:

Example (1). Under the terms of a revolving credit plan the required monthly payment to be made by customer A is $20. During the billing-month ending in December, sales aggregating $80 are charged to customer A's account, and during the next billing-month, ending in January, sales aggregating $19.95 and finance charges of $.60 are charged to A's account. Since the aggregate of sales charged to customer A's account during the billing-month ending in December ($80) exceeds the required monthly payment ($20), the terms and conditions of the plan contemplate that the sales charged during such billing-month are of the type which will be paid for in two or more installments. Sice the aggregate of sales charged to customer A's account during the billing-month ending in January ($19.95) does not exceed the required monthly payment, the sales making up the aggregate of sales in such billing-month are not of the type which the terms and conditions of the plan contemplate will be paid for in two or more installments.

Example (2). The terms of a revolving credit plan require a payment of 20 percent of the balance of the customer's account as of the end of the billing-month for which the statement is rendered. A customer makes purchases aggregating $25 in his next to the last billing-month ending within the taxpayer's taxable year, and the balance at the end of that month is $150. At the end of the customer's last billing-month ending within the taxpayer's taxable year, the balance of the account has decreased to $110. If the taxpayer determines the required monthly payment by reference to the payment required on the statement for the last billing-month ending within the taxable year and applies such method consistently to all accounts, then the sales making up the $25 aggregate of sales are of the type which the terms and conditions of the plan contemplate will be paid for in two or more installments. Although such aggregate was less than the $30 payment (20% . $150) required on the statement rendered for the billing-month of sale, it was more than the $22 (20% . $110) that the customer was required to pay on the statement rendered for his last billing-month ending within the taxable year and thus meets the requirements of this subdivision. If, however, the taxpayer determines the required monthly payment by reference to the payment required on the statement for the billing-month of sale, then the sales making up the aggregate of sales during such billing-month do not meet the requirements of this subdivision because such aggregate was less than the $30 payment required on the statement rendered for such month.

(ii) The sale must be charged to an account on which the first payment after the billing-month of sale indicates that the sale is being paid in installments. The first payment after the billing-month of sale indicates that the sale is being paid in installments if, and only if, such payment is an amount which is less than the balance of the account as of the close of the billing-month of sale. For purposes of this subdivision, such balance shall be reduced by any return or allowance credited to the account after the close of the billing-month of sale and before the close of the billing-month within which the first payment after the billing-month of sale is credited to the account, unless the taxpayer demonstrates that the return or allowance was attributable to a charge made in a month subsequent to the billing-month of sale. The requirements stated in this subdivision may be illustrated by the following examples, in which it is assumed that the taxpayer's annual accounting period ends on January 31.

Example (1). Customer A's revolving credit account shows the following sales and payments.

Month ending	Aggregate sales in month	Payments	Balance
December 20	$150	0	$150
January 20	75	$30	195
February 20	0	195	0

All sales made in the billing month ending December 20 meet the requirements of this subdivision because the first payment on the account after such billing-month ($30) was less than the balance of the account as of the close of such billing-month ($150); and none of the sales made in the billing month ending January 20 meets the requirements of this subdivision because the balance of the account as of the end of such billing-month was liquidated in one payment. By application of the rules of subparagraph (6)(v) of this paragraph, the balance in the account as of the last billing-month ending in the taxable year ($195) consists of $120 of the $150 of sales made in the billing month ending December 20 and all of the $75 of sales made in the billing month ending January 20. Therefore, $120 of the account balance meets the requirements of this subdivision and $75 does not.

Example (2). Customer B's revolving credit account shows the following sales and payments:

Month ending	Aggregate sales in month	Payments	Balance
December 20	$50	0	$50
January 20	100	0	150
February 20	0	$50	100

None of the sales made in the billing-month ending December 20 meets the requirements of this subdivision because the first payment credited to the account after such billing-month ($50) is not less than the balance of the account as of the close of such month ($50). All of the sales made in the billing month ending January 20 meet the requirements of this subdivision because the first payment after such billing month ($50) is less than the balance of the account as of the close of such month ($150).

Example (3). Customer C's revolving credit account shows the following purchases and credits:

Month ending	Item	Charges	Credits	Balance
Jan 20	Coal	$55		
	Dress	40		
	Shirt	5		
				$100
Feb 20	Return			
	Payments		$5	
			95	0

None of the sales made in the billing-month ending December 20 meets the requirements of this subdivision because the first payment credited to the account after such billing-month ($95) was equal to the balance of the account as of the end of such billing-month, $95. For this purpose, the balance of $100 is reduced by the $5 return which was credited to the account after the close of the billing-month of sale and before the close of the billing-month within which the first payment after the billing-month of sale is credited.

(4) The provisions of subparagraphs (2) and (3) of this paragraph may be illustrated by the following examples in which it is assumed that the taxpayer is a dealer in personal property whose annual accounting period ends on January 31.

Example (1). Customer A's revolving credit ledger account shows the following:

Month ending	Aggregate sales in month[1]	Returns and allowances	Payments	Finance charges	Balance
Jan 20	$15.00	0	0	0	$15.00
Feb 20	0	0	0	$0.15	15.15

[1] Including sales of personal property and nonpersonal property sales.

For purposes of the segregation provided for in subparagraph (2)(i) of this paragraph, customer A's account will be disregarded and not taken into account in the determination of what percentage of charges in the sample is to be treated as sales on the installment plan because no payment was credited to that account after the billing-month of sale and on or before February 20.

Example (2). This example is applicable with respect to sales made during taxable years beginning before January 1, 1964. Under the terms of Corporation X's revolving credit plan, payments are required in accordance with the following schedule:

Unpaid balance	Required monthly payment
0-$99.99	$20
$100-$199.99	40
$200-$299.99	60

Customer B's revolving credit ledger account for the period beginning on September 21, 1963, and ending February 20, 1964, shows the following:

Month ending—	Aggregate sales in month[1]	Returns and allowances	Payments	Finance charges	Balance
Oct 20	$55.00	0	0	0	$55.00
Nov 20	45.00	0	$20.00	$0.35	80.35
Dec 20	20.00	0	20.00	60	80.95
Jan 20	26.00	$5.00	20.00	61	82.56
Feb 20	0	10.00	72.56	0	0

[1] Including sales of personal property and nonpersonal property sales.

The three $20 payments and the $5 return or allowance made in the billing-months ending in the taxable year are applied. Under the rules in subparagraph (6)(v), to liquidate the earliest outstanding charges, first to the $55 aggregate of sales in the billing-month ending October 20 and next to $10 of the aggregate of sales made in the billing-month ending November 20. Thus, the balance of the account as of the close of the billing-month ending Janaury 20, $82.56, is made up as follows:

Remainder of sales in billing-month ending Nov. 20 ($45 $10)	$35.00
Finance charge for billing-month ending Nov. 20	35
Sales for billing-month ending Dec. 20	20.00
Finance charge for billing-month ending Dec. 20	0.50
Sales for billing month ending Jan. 20	26.00
Finance charge for billing-month ending Jan. 20	61
Total	82.56

The sales of $35 remaining from the aggregate of sales for the billing-month ending November 20 meet the requirements of subparagraph (3)(i) of this paragraph because the aggregate of sales charged during such billing-month ($45) exceeds the required monthly payment ($20), and such sales meet the requirements of subparagraph (3)(ii) of this paragraph because the first payment after the billing-month of sale ($20) is an amount less than the balance of the account as of the close of such month ($80.35). Therefore, $35 of sales will be treated as sales on the installment plan. The $20 aggregate of sales charged during the billing month ending December 20 does not meet the requirements of subparagraph (3)(i) of this paragraph because it is in an amount which does not exceed the required monthly payment ($20) (The finance charge of $0.60 added in the billing-month does not enter into the determination of the aggregate of sales for the month because the term "sales" (as defined in subparagraph (6)(i) of this paragraph) does not include finance charges). The $26 aggregate of sales for the billing-month ending January 20 does not meet the requirements of subparagraph (3)(ii) of this paragraph because the first payment after such billing month ($72.56) was equal to the balance of the account as of the close of such billing-month ($72.56) was equal to the balance of the account as of the close of such billing-month ($72.56). For this purpose, the balance of $82.56 is reduced by the $10 return or allowance which was credited after the billing-month of sale and before February 20. Thus, of the $82.56 balance of B's account as of the close of the last billing-month ending within the taxpayer's taxable year $35 will be treated as sales on the installment plan for purposes of determining the percentage provided for in subparagraph (2) of this paragraph.

Example (3). This example is applicable with respect to sales made during taxable years beginning after December 31, 1963. Assume the facts in example (2), except that Customer B's revolving credit ledger account is for the period beginning on September 21, 1964 and ending February 20, 1965. Since payments received are first used to liquidate any outstanding finance charges under the rule in subparagraph (6)(v); the $20 payment in December liquidated the $0.35 finance charge accrued at the end of the November billing-month and the $20 payment in January liquidated the $0.60 finance charge accrued at the end of the December billing month. The balance of the three $20 payments ($59.05) and the $5 return or allowance are applied (under the rules in subparagraph (6)(v)) to liquidate the earliest outstanding sales, first to the $55 aggregate of sales in the billing-month ending October 20 and next to $9.05 of the aggregate of sales made in the billing-month ending November 20. Thus, the balance of the account as of the close of the billing-month ending January 20, $82.56, is made up as follows.

Remainder of sales in billing-month ending Nov. 20 ($45 $9.05)	$35.95
Sales for billing month ending Dec. 20	20.00
Sales for billing month ending Jan. 20	26.00
Finance charge for billing month ending Jan 20	61
Total	82.56

The sales of $35.95 remaining from the aggregate of sales for the billing-month ending November 20 meet the requirements of subparagraph (3)(i) of this paragraph because the aggregate of sales charged during such billing-month ($45) exceeds the required monthly payment ($20) and such sales meet the requirements of subparagraph (3)(ii) of this paragraph because the first payment after the billing-month of sale ($20) is an amount less than the balance of the account as of the close of such month ($80.35). Therefore, $35.95 of sales will be treated as sales on the installment plan. The $20 aggregate of sales charged during the billing-month ending December 20 does not meet the requirements of subparagraph (3)(i) of this paragraph because it is in an amount which does not exceed the required monthly payment ($20). The $26 aggregate of sales for the billing-month ending January 20 does not meet the requirements of subparagraph (3)(ii) of this paragraph because the first payment after such billing-month ($72.56) was equal to the balance of the account as of the close of such billing-month ($72.56). For this purpose, the balance of $82.56 is reduced by the $10 return or allowance which was credited after the billing-month of sale and before February 20. Thus, of the $82.56 balance of B's account as of the close of the last billing month ending within the taxpayer's taxable year $35.95 will be treated as sales on the installment plan for purposes of determining the percentage provided for in subparagraph (2) of this paragraph.

(5) Sales under a revolving credit plan which are nonpersonal property sales (as defined in subparagraph (6)(iv) of this paragraph) do not constitute sales on the installment plan. Therefore, the charges under a revolving credit plan must be reduced by the nonpersonal property sales, if any, under such plan, before application of the sample percentage as provided for in subparagraph (2)(i) of this paragraph. The taxpayer may treat as the nonpersonal property sales under the plan for the taxable year an amount which bears the same ratio to the total sales under the revolving credit plan made in the taxable year as the total nonpersonal property sales made in such year bears to the total sales made in such year.

(6) For purposes of this paragraph—

(i) The term "sales" includes sales of services, such as a charge for watch repair, as well as sales of property, but does not include finance or service charges.

(ii) The term "charges" includes sales of services and property as well as finance or service charges.

(iii) A billing-month is that period of time for which a periodic statement of charges and credits is rendered to a customer.

(iv) The term "nonpersonal property sales" means all sales which are not sales of personal property made by the taxpayer. Thus, sales of a department leased by the taxpayer to another are nonpersonal property sales. Likewise, charges for services rendered by the taxpayer are nonpersonal property sales unless such services are incidental to and rendered contemporaneously with the sale of personal property, in which case such charges shall be considered as constituting part of the selling price of such property.

(v) Except as otherwise provided in this subdivision, each payment received from a customer under a revolving credit plan before the close of the last billing-month ending in the taxable year shall be applied to liquidate the earliest outstanding charges under such plan, notwithstanding any rule of law or contract provision to the contrary. For purposes of determining which charges remain in the balance of an account at the end of the last billing-month ending in the taxable year, the taxpayer may apply returns and allowances which are credited before the close of the last billing-month ending in the taxable year either (*a*) to liquidate or reduce the charge for the specific item so returned or for which an allowance is permitted, or (*b*) to liquidate or reduce the earliest outstanding charges. The method so selected for applying returns and allowances shall be followed on a consistent basis from year to year unless the district director consents to a change. Additionally, finance or service charges which are computed on the basis of the balance of the account at the end of the previous billing-month (usually reduced by payments during the current billing-month) are accrued at the end of the current billing-month and are therefore considered for purposes of determining the earliest outstanding charges, as charged to the accunt after any sales made during the current billing month. However, for purposes of determining which charges remain in the balance of an account at the end of the last billing-month ending in a taxable year which began after December 31, 1963, payments received during such year shall be applied during such year shall be applied first against any finance or service charges which were outstanding at the time such payment was received. The preceding sentence shall not apply with respect to a computation made for purposes of applying the rule described in subparagraph (2)(ii) of this paragraph.

(vi) The taxpayer shall allocate those sales under a revolving credit plan which are treated as sales on the installment plan to the proper year of sale in order to apply the appropriate gross profit percentage as provided for in paragraph (c) of this section. This allocation shall be made on the basis of the percentages of charges treated as sales on the installment plan which are attributable to each taxable year as determined in the sample of accounts described in subparagraph (2) of this paragraph. However, if the taxpayer demonstrates to the satisfaction of the district director that income from sales on the installment plan is clearly reflected, all sales may be considered as being made in the taxable year for purposes of applying the gross profit percentage.

(7) The provisions of this paragraph may be illustrated by the following example:

Example: Corporation X is a dealer in personal property and has elected to report on the installment method those sales under its revolving credit plan which may be treated as sales on the installment plan. Corporation X's taxable year ends on January 31, and the total balance of all its revolving credit accounts as of January 31, 1964, is $2,000,000. The total sales made in the taxable year are $10,000,000 of which $500,000 are nonpersonal property sales. The gross profit percentage realized or to be realized on all sales made in the taxable year is 40 percent. The amount of the gross profit contained in the year-end balance of $2,000,000 which may be deferred to succeeding years is computed as follows:

(i) In order to reduce the charges appearing in the year-end balance of revolving credit accounts receivable by the nonpersonal property sales contained therein, corporation X determines the amount of such nonpersonal property sales under the method permitted in subparagraph (5) of this paragraph. Corporation X first determines the ratio which total nonpersonal property sales made during the year ($500,000) bears to total sales made during the year ($10,000,000), and then applies the percentage (5 percent) thus obtained to the year-end balance of revolving credit accounts receivable ($2,000,000). The nonpersonal property sales thus determined ($100,000) is subtracted from such year-end balance to obtain the charges under the revolving credit plan appearing in the year-end balance ($1,900,000) to which the sample percentage is to be applied.

(ii) In accordance with generally accepted sampling techniques the taxpayer selects a probability sample of all revolving credit accounts having balances for billing-months ending in January 1964. The technique employed results in a random selection of accounts with total balances of $100,000.

(iii) Analysis of these sample accounts discloses that of the $100,000 of balances, $10,000 of balances are in accounts on which no payment was credited after a billing month of sale and on or before the end of the first billing-month ending in the taxable year beginning February 1, 1964. These balances are, therefore, disregarded and not taken into account in the determination of what percentage of sales in the sample is to be treated as sales on the installment plan. Of the remaining $90,000 of balances, the taxpayer determines, by analyzing the ledger cards in the sample, that $63,000 of balances are composed of sales which meet the requirements of subparagraph (3)(i) and (ii) of this paragraph and are thus treated as sales on the installment plan. The remaining $27,000 of balances either did not meet the requirements of subparagraph (3)(i) or (ii) of this paragraph or were not sales as defined in subparagraph (6)(i) of this paragraph). The percentage of charges in the sample treated as sales on the installment plan is, therefore, 70 percent ($63,000–$90,000).

(iv) The charges in the year-end balance which are to be treated as sales on the installment plan. $1,330,000 are computed by multiplying the charges determined in subdivision (i) of this subparagraph ($1,900,000) by the percentage obtained in subdivision (iii) of this subparagraph (70 percent).

(v) The deferred gross profit attributable to sales under the revolving credit plan for the taxable year. $532,000 is determined by multiplying the amount determined in subdivision (iv) of this subparagraph $1,330,000 by the gross profit percentage 40 percent. (Corporation X will be able to demonstrate to the satisfaction of the district director that (*a*) since the gross profit percentage for all sales does not vary materially from the gross profit percentage for all sales made under the revolving credit plan, (*b*) since only an insubstantial amount of sales included in year-end account balances was made prior to the taxable year, and (*c*) since the prior year's gross profit percentage does not vary materially from the gross profit percentage for the taxable year, income from sales on the installment plan will be clearly reflected by applying the current year's gross profit percentage for all sales under the revolving credit plan treated as sales on the installment plan.)

This notice of proposed rulemaking is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).

P.E. COATES
Acting Commissioner
of Internal Revenue.

(Filed by the Office of the Federal Register on July 25, 1986, 8:45 a.m., and published in the issue of the Federal Register for July 28, 1986, 51 F.R. 26903)

Information Returns Filed on Magnetic Media—Seminars

Announcement 86–94[1]

The Internal Revenue Service National Computer Center will be conducting a series of nationwide free seminars on magnetic media reporting of information returns. The seminars are designed to provide procedural information to help filers meet the legal and technical requirements of magnetic media reporting.

Following is a schedule of seminar sites and dates, as well as the telephone numbers of the IRS offices closest to those sites. Please contact those IRS offices for the exact locations and times.

CITY	*DATE*	*TELEPHONE NUMBER*
Aberdeen, SD	September 30	(605) 225-0250 (Ext. 262)
Albuquerque, NM	October 1	(800) 424-1040
Anchorage, AK	October 28	(907) 261-4231
Atlanta, GA	October 30	(404) 331-3808
Boise, ID	September 19	(208) 334-1307
Boston, MA	September 24	(617) 565-1645
Chicago, IL	October 1	(312) 886-7802
Cincinnati, OH	September 18	(513) 684-2828
Cleveland, OH	October 2	(216) 522-3414
Columbia, SC	October 29	(803) 253-3031
Dallas, TX	October 21 & 22	(214) 767-1428
Denver, CO	October 2	(303) 825-7041 or (303) 844-5854
Greensboro, NC	October 16	(919) 333-5620
Helena, MT	September 18	(406) 449-5392
Honolulu, HI	October 30	(808) 546-8932 (After Oct. 15, Call (808) 541-1000)
Houston, TX	October 23 & 24	(713) 954-6878
Kansas City, KS	October 9	(314) 425-6845
Laguna Niguel, CA	October 23	(714) 643-4060
Las Vegas, NV	October 10	(702) 388-6937
Little Rock, AR	October 29	(501) 378-5685
Los Angeles, CA	October 21 & 22	(213) 894-4574
Milwaukee, WI	September 30	(414) 291-3302
Nashville, TN	October 29	(615) 736-7291
New Orleans, LA	October 30	(504) 589-2801
New York, NY	October 21 & 22	(212) 264-3310 or (718) 780-6020
Omaha, NE	October 8	(402) 221-3501
Orlando, FL	October 30	(305) 648-6560 or (904) 791-2514
Philadelphia, PA	October 9 & 10	(215) 597-0512
Phoenix, AZ	October 24	(602) 261-3861
Portland, OR	September 17	(503) 221-3960
Richmond, VA	October 15	(804) 771-2289
Sacramento, CA	October 9	(916) 978-4083
St. Louis, MO	September 16	(314) 425-6845
St. Paul, MN	October 2	(612) 725-7320
Salt Lake City, UT	September 30	(800) 424-1040
San Francisco, CA	October 7 & 8	(415) 273-4233
Seattle, WA	September 16	(206) 442-4230

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[1] Based on News Release IR-86-109, dated August 12, 1986.

Deletions from Cumulative List of Organizations Contributions to Which Are Deductible Under Section 170 of the Code

Announcement 86–95

The names of organizations that no longer qualify as organizations described in section 170(c)(2) of the Internal Revenue Code of 1954 are listed below.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of annoucement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgment has been timely filed, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deductible. Protection under section 7428(c) would begin on September 8, 1986, (the date of publication of this announcement) and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is $1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

Affiliated Leadership League of and for the Blind of America, Washington, DC
Karum Group, The, Bellingham, WA
Ladies Auxiliary to Multi-Cap Booster, Inc., Mt. Clemens, MI
Northern McClain County Medical Authority, Inc., Blanchard, OK
Operation Outreach, Aptos, CA
Palo Alto Montessori School, Inc., Palo Alto, CA
Star Beach Retreat, Inc., Milton, FL

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practictioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Robert D. Digby	North Little Rock, AR	Certified Public Accountant	Four Months from July 29, 1986
Jeffrey E. Ellis	Rockland, ME	Certified Public Accountant	Indefinte from July 2, 1986
Charles L. Honey	Prescott, AR	Attorney	One Year from July 2, 1986
Bernhardt Karp	Hudson, NY	Attorney & Certified Public Accountant	Indefinite from July 29, 1986
George N. Meros	Springfield, MO	Attorney	Indefinite from July 25, 1986
William G. Waldrop	Adamsville, AL	Certified Public Accountant	Indefinite from July 17, 1986

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to identify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
David P. Rosenberg	Philadelphia, PA	Indefinite effective August 13, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federral Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

Finding List of Current Action on Previously Published Rulings[1]

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*Denotes entry since last publication

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–106, page 4.
Interest; loan from "Clifford" trust to grantor. Interest payments on a loan from a "Clifford" trust to its grantor are not deductible under section 163 of the Code when the loan is not a genuine debt.

Rev. Rul. 86–107, page 8.
Investment credit; limitation; luxury automobiles; price inflation adjustment. The automobile price inflation adjustment for passenger automobiles placed in service after December 31, 1984, and before April 3, 1985, and for passenger automobiles acquired by taxpayers pursuant to binding contracts in effect on April 1, 1985, and at all times thereafter, and placed in service after April 2, 1985, and before August 1, 1985, is 2.6 percent. For those vehicles, the amount of credit determined under section 46(a) may not exceed $1,000, and the recovery deductions for any taxable year after the first taxable year in the recovery period may not exceed $6,200. (Also, the recovery deductions for the first taxable year may not exceed $4,100.)

Ct. D. 2033, page 9.
Accounting methods; accrual; progressive slot machine jackpot. The taxpayer, a casino operator, was permitted to deduct the accrued increase in progressive slot machine jackpots. The payee and the time of payment were not known to the taxpayer at the close of the taxable year, but the liability was irrevocably established by State law. *Hughes Properties, Inc.*, Supreme Court of the United States.

T.D. 8096, page 4.
Regulations under sections 172 and 537 of the Code relate to product liability losses and accumulations for the payment of reasonably anticipated product liability losses.

LR–146–81, page 17.
Proposed amendments to the regulations under section 453A of the Code relate to installment method reporting by dealers in personal property.

EXEMPT ORGANIZATIONS

Announcement 86–96, page 18.
A list is given of organizations now classified as private foundations and an organization that is not a private operating foundation.

EMPLOYMENT TAX

Rev. Rul. 86–108, page 13.
Nonresident and resident aliens; services on the outer Continental Shelf. Services performed by nonresident and resident aliens on an oil rig temporarily attached to the outer Continental Shelf of the United States are "employment" for FICA purposes under section 3121(b) of the Code.

Rev. Rul. 86–109, page 14.
Employee compensation; deceased employee; death benefits; information reporting. A employer must report wages or other compensation for services performed by a former deceased employee and paid to the estate or the person entitled to receive the payment of the employee on Form 1099–MISC, Statement for Recipients of Miscellaneous Income, as nonemployee compensation. Rev. Ruls. 64–150 and 71–456 superseded.

EXCISE TAXES

Notice 86–10, page 16.
Windfall profit tax; inflation adjustment factor. For purposes of computing the windfall profit tax, the inflation adjustment for the quarter ending December 31, 1986, is 0.4679 for tier 1 or tier 2 oil and 0.6879 for tier 3 oil.

Finding Lists begin on page 24.
Announcement of Disbarments and Suspensions on page 22.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 163.—Interest

26 CFR 1.163–1: Interest deduction in general.

Interest; loan from "Clifford" trust to grantor. Interest payments on a loan from a "Clifford" trust to its grantor are not deductible under section 163 of the Code when the loan is not a genuine debt.

Rev. Rul. 86–106

ISSUE

Are any of the payments made pursuant to a purported loan agreement between the grantor of a "Clifford" trust and its trustee deductible as interest under section 163(a) of the Internal Revenue Code in the circumstances described below?

FACTS

On April 1, 1984, *A* created an irrevocable trust for *A*'s minor children. The trust agreement provides that *A*'s children are entitled to the income of the trust, which was to be distributed at least annually in equal shares. At the end of 10 years and one month, or upon the death of the last surviving beneficiary, whichever occurs first, the corpus is to be returned to *A*. Such a trust is frequently referred to as a "Clifford" trust.

At the time the trust was created, *A* contributed $50,000 in cash. At that time *A* and the trustee orally agreed that the entire corpus could be borrowed by *A* within 30 days. On April 15, 1984, the trustee transferred the $50,000 in cash to *A* in return for *A*'s note and a mortgage on *A*'s home. The note provides for adequate interest and adequate security within the meaning of section 675(3) of the Internal Revenue Code. The principal amount is due at the end of 5 years. The trustee is not a related or subordinate party with respect to the grantor within the meaning of section 672(c) of the Code.

LAW AND ANALYSIS

Section 163(a) of the Code states that a deduction shall be allowed for all interest paid or accrued within the taxable year on indebtedness. The term "interest" has been defined as compensation for the use or forbearance of money. *Deputy v. duPont*, 308 U.S. 488 (1940), 1940–1 C.B. 118. For interest to be deductible, the payments must arise from genuine indebtedness, that is, indebtedness in substance and not merely in form. *Knetsch v. United States*, 364 U.S. 361 (1960), 1961–1 C.B. 34; *Perrett v. Commissioner*, 74 T.C. 111 (1980).

Section 673(a) of the Code provides that the grantor of a trust will be treated as the owner of any portion of such trust in which the grantor has a reversionary interest in the corpus or the income therefrom if, as of its inception, such interest may reasonably be expected to become possessory within 10 years of its transfer to the trust.

Section 675(3) of the Code provides that the grantor will be treated as the owner of any portion of a trust in respect of which the grantor has not completely repaid the loan and any interest thereon before the beginning of the taxable year. Section 675(3) does not apply, however, if the loan to the grantor provides for an adequate rate of interest and adequate security and is made by a trustee who is not the grantor and who is not related or subordinate to the grantor.

In *Perrett*, the Tax Court reviewed a transaction similar to the one involving *A*. The taxpayer and his business partner each loaned money at 3 percent to separate trusts established for the benefit of their respective children. The money was then borrowed from the trusts by their partnership at 6 percent. The court concluded that the interposition of the trusts in the series of loans served no purpose other than to allow the taxpayer and his partner to make contributions to their children's trusts which they would attempt to deduct as interest. The court found that the transactions in substance were not loans. Therefore, no interest deductions were allowed for payments made by the partnership to the trusts.

An analogous arrangement was considered in Rev. Rul. 82–94, 1982–1 C.B. 31. In that ruling parents loaned money directly to a child on an interest free basis. Several days later the child loaned the money to the parents. The ruling concludes that the purported interest payable to the child is not deductible as interest. Although no trust was involved, the principles espoused in the ruling apply here. The circular flow of money lacks economic reality.

In this instance, just as in *Perrett* and Rev. Rul. 82–94, the parties have failed to create a genuine debtor-creditor relationship for federal tax purposes. The trust was merely a conduit for *A* to lend money to himself because of the prearrangement with the trustee to have the corpus returned in the form of a loan. The trust and loan serve no purpose except to create a circular flow of money designed to create a tax deduction for a gift to *A*'s child in the amount of the purported interest. This transaction is not a loan in substance. *Perrett v. Commissioner*, 74 T.C. at 134. Under the facts in the present situation, the note is a gratuitous promise to make a series of gifts in the future. *See Guaranty Trust. Co. v Commissioner*, 98 F.2d 62 (2d Cir. 1938). Because a genuine debtor-creditor relationship was not created, *A* may not deduct the annual payments to the trust even though the terms of the purported loan satisfied the requirements of section 675(3), and even though the identity of the trustee satisfied the requirements of section 672(c) of the Code.

Accordingly, no interest deduction is allowable for the $7,500 annual payments to the trust. Any subsequent renewals of the loan are, in the absence of clear and convincing evidence to the contrary, presumed to be have been prearranged, and are therefore subject to the above analysis.

HOLDING

Under the facts set forth above, the settlor's payments to the trust under the purported loan agreement do not constitute interest paid on indebtedness for purposes of section 163(a) of the Code, because there is no genuine indebtedness.

Section 172.—Net Operating Loss Deduction

26 CFR 1.172–4: Net operating loss carrybacks and net operating loss carryovers.

T.D. 8096

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, SUBCHAPTER H, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Product Liability Losses and Accumulations for Product Liability Losses

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document provides final regulations relating to product liability losses and accumulations for the payment of reasonably anticipated product liability losses. Changes to the applicable tax law were made by the Revenue Act of 1978. The regulations would provide the public with guidance needed to comply with the applicable parts of that act.

DATE: The amendments made by section 371 of the Revenue Act of 1978 generally are effective for taxable years beginning after September 30, 1979.

FOR FURTHER INFORMATION CONTACT: B. Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3935).

BACKGROUND

On March 25, 1983, the FEDERAL REGISTER published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under sections 172 and 537 of the Internal Revenue Code of 1954 (48 FR 12557) [1983-1 C.B. 970]. A few comments were received regarding this proposal. A public hearing was neither requested nor held. After consideration of all comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

PUBLIC COMMENTS

Proposed §1.172-13(b)(2)(iv) provided that amounts paid for insurance against product liability risks are not paid on account of product liability. Two commentators suggested that this provision be deleted in the final regulations. Alternatively, one commentator suggested that even if commercial product liability insurance premiums are not to be generally considered paid on account of product liability for purposes of section 172, so-called "retrospective premiums" should be. After consideration of these comments, the final regulations adopt §1.172-13(b)(2)(iv) as proposed. However, the final regulations clarify the definition of "product liability" by including certain amounts paid within that definition even if such amounts are paid to an insurance company. The final regulations state that an amount is considered paid on account of product liability (even if such amount is paid to an insurance company) if the amount otherwise qualifies as "product liability" and if the amount (1) is paid on account of specific claims against the taxpayer (or on account of expenses incurred in connection with the investigation or settlement of or opposition to such claims), subsequent to the events giving rise to the claims and pursuant to a contract entered into before those events, (2) is not refundable, and (3) is not applicable to other claims, other expenses or to subsequent coverage.

Another commentator suggested that the final regulations be clarified with respect to the interaction of the election under section 172(b)(3)(C) (relating to election to relinquish the entire carryback period) and the election under section 172(j)(3) (relating to election to forgo 10-year product liability loss carryback period). The final regulations are clarified by providing in §1.172-13(c)(4) that the election pursuant to section 172(b)(3)(C) does not preclude a product liability loss from being carried back 10 years.

One commentator suggested that the manner in which a taxpayer must elect to forgo the 10-year carryback period was unknown prior to the publication of the proposed regulations and that therefore those rules should only apply to elections made after the publication of the proposed regulations. In response to this comment, the final regulations provide that the statement to be filed with the Service must contain the information specified in §1.172-13(c)(3) only in the case of statements filed with the Service after April 25, 1983.

The proposed regulations stated that the term "product liability loss" includes, *inter alia,* expenses incurred in connection with the settlement of claims on account of alleged product liability. Additionally, the proposed regulations excluded from the definition of "product liability" liabilities arising under warranty theories relating to repair or replacement of the property that are essentially contract liabilities. One commentator suggested that the final regulations specifically include in the term "product liability loss" settlement expenses related to replacement products that are provided other than under the terms of a warranty. Since such expenses already are within the scope of this term, the final regulations are adopted without this change.

Section 537(b)(4) states that amounts accumulated for the payment of reasonably anticipated product liability losses are treated as accumulated for the reasonably anticipated needs of the business. The proposed regulations stated generally that whether an accumulation is reasonable in amount shall be determined in light of all the facts and circumstances of the taxpayer making such accumulation. The proposed regulations identified some factors that should be considered in determining the reasonableness of the accumulation. The final regulations provide that another factor to be considered in determining whether an accumulation is reasonable in amount is the fact that the taxpayer in accounting for its potential future liability took into account the reasonably estimated present value of the potential future liability.

REGULATORY FLEXIBILITY ACT

Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

NONAPPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

PAPERWORK REDUCTION ACT

The collection of information requirements contained in this regulation have been submitted to the Office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act of 1980. These requirements have been approved by OMB. (Assigned control number 1545-0863).

DRAFTING INFORMATION

The principal author of these regulations was George T. Magnatta of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, Part 1 and Part 602 of 26 CFR are amended as follows:

INCOME TAX REGULATIONS
PART 1

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 2. Section 1.172–4 is amended by removing "(a)(1)(viii), and (a)(1)(ix)" in paragraph (a)(1)(ii) and adding in its place "(a)(1)(viii), (ix), and (x)", and by adding a new paragraph (a)(1)(x). The added provision reads as follows:

§1.172–4 Net operating loss carrybacks and net operating loss carryovers.

(a) *General provisions*—(1) *Years to which loss may be carried.* * * *

(x) *Product liability losses.* A product liability loss (as defined in section 172(j) and §1.172–13(b)(1)) sustained in a taxable year beginning after September 30, 1979, by any taxpayer shall be carried back to the 10 preceding taxable years, unless the taxpayer elects (in accordance with the rules set forth in section 172(j)(3) and §1.172–13(c)) not to have this provision apply. Any unused portion of the net operating loss remaining after this 10-year carryback period shall be carried forward under the general provisions of section 172(b)(1)(B) and its status as a product liability loss shall be disregarded.

* * * * *

Par. 3. A new §1.172–13 is added after §1.172–12, to read as follows:

§1.172–13 Product liability losses.

(a) *Entitlement to 10-year carryback*—(1) *In general.* Unless an election is made pursuant to paragraph (c) of this section, in the case of a taxpayer which has a product liability loss (as defined in section 172(j) and paragraph (b)(1) of this section) for a taxable year beginning after September 30, 1979 (hereinafter "loss year"), the product liability loss shall be a net operating loss carryback to each of the 10 taxable years preceding the loss year.

(2) *Years to which loss may be carried.* A product liability loss shall first be carried to the earliest of the taxable years to which such loss is allowable as a carryback and shall then be carried to the next earliest of such taxable years, etc.

(3) *Example.* The application of this paragraph may be illustrated as follows:

Example. Taxpayer A incurs a net operating loss for taxable year 1980 of $80,000, of which $60,000 is a product liability loss. A's taxable income for each of the 10 years immediately preceding taxable year 1980 was $5,000. The product liability loss of $60,000 is first carried back to the 10th through the 4th preceding taxable years ($5,000 per year), thus offsetting $35,000 of the loss. The remaining $25,000 of product liability loss is added to the remaining portion of the total net operating loss for taxable year 1980 which was not a product liability loss ($20,000), and the total is then carried back to the 3rd through 1st years preceding taxable year 1980, which offsets $15,000 of this loss. The remaining loss ($30,000) is carried forward pursuant to section 172(b)(1) and the regulations thereunder without regard to whether all or any portion thereof originated as a product liability loss.

(b) *Definitions*—(1) *Product liability loss.* The term "product liability loss" means, for any taxable year, the lesser of—

(i) The net operating loss for the current taxable year (not including the portion of such net operating loss attributable to foreign expropriation losses, as defined in §1.172–11), or

(ii) The total of the amounts allowable as deductions under sections 162 and 165 directly attributable to—

(A) Product liability (as defined in paragraph (b)(2) of this section), and

(B) Expenses (including settlement payments) incurred in connection with the investigation or settlement of or opposition to claims against the taxpayer on account of alleged product liability. Indirect corporate expense, or overhead, is not to be allocated to product liability claims so as to become a product liability loss.

(2) *Product liability.* (i) The term "product liability" means the liability of a taxpayer for damages resulting from physical injury or emotional harm to individuals, or damage to or loss of the use of property, on account of any defect in any product which is manufactured, leased, or sold by the taxpayer. The preceding sentence applies only to the extent that the injury, harm, or damage occurs after the taxpayer has completed or terminated operations with respect to the product, including, but not limited to the manufacture, installation, delivery, or testing of the product, and has relinquished possession of such product.

(ii) The term "product liability" does not include liabilities arising under warranty theories relating to repair or replacement of the property that are essentially contract liabilities. For example, the costs incurred by a taxpayer in repairing or replacing defective products under the terms of a warranty, express or implied, are not product liability losses. On the other hand, the taxpayer's liability for damage done to other property or for harm done to persons that is attributable to a defective product may be product liability losses regardless of whether the claim sounds in tort or contract. Further, liability incurred as a result of services performed by a taxpayer is not product liability. For purposes of the preceding sentence, where both a product and services are integral parts of a transaction, product liability does not arise until all operations with respect to the product are completed and the taxpayer has relinquished possession of it. On the other hand, any liability that arises after completion of the initial delivery, installation, servicing, testing, etc., is considered "product liability" even if such liability arises during the subsequent servicing of the product pursuant to a service agreement or otherwise.

(iii) Liability for injury, harm, or damage due to a defective product as described in this subparagraph shall be "product liability" notwithstanding that the liability is not considered product liability under the law of the State in which such liability arose.

(iv) Amounts paid for insurance against product liability risks are not paid on account of product liability.

(v) Notwithstanding subparagraph (iv), an amount is paid on account of product liability (even if such amount is paid to an insurance company) if the amount satisfies the provisions of paragraph (b)(2)(i) through (iii) of this section and the amount—

(A) Is paid on account of specific claims against the taxpayer (or on account of expenses incurred in connection with the investigation or settlement of or opposition to such claims), subsequent to the events giving rise to the claims and pursuant to a contract entered into before those events,

(B) Is not refundable, and

(C) Is not applicable to other claims, other expenses or to subsequent coverage.

(3) *Examples.* Paragraph (b)(2) of this section is illustrated by the following examples:

Example (1). X, a manufacturer of heating equipment, sells a boiler to A, a homeowner. Subsequent to the sale and installation of the boiler, the boiler explodes due to a defect causing physical injury to A. A sues X for damages for the injuries sustained in the explosion and is awarded $250,000, which X pays. The payment was made on account of product liability.

Example (2). Assume the same facts as in example (1) and that A also sues under the contract with X to recover for the coat of the boiler and recovers $1,000, the boiler's replacement cost. The $1,000 payment is not a payment on account of product liability. Similarly, if X agrees to repair the destroyed boiler, any amount expended by X for such repair is not payment made on account of product liability.

Example (3). Y, a professional medical association is sued by B, a patient, in an action based on the malpractice of one of its doctors. B recovers $25,000. Because the suit was based on the services of B, the payment is not made on account of product liability.

Example (4). R, a retailer of communications equipment, sells a telecommunication device to C. R also contracts with C to service the equipment for 3 years. While R is installing the equipment the unit catches on fire due to faulty wiring within the unit and destroys C's office. Because R had not relinquished possession of the equipment when the fire started, any amount paid to C by R for the damage to C's property on account of the defective product is not payment on account of product liability.

Example (5). Assume the same facts as in example (4) except that the fire and resulting property damages occurred after R had installed the equipment and relinquished possession of it. Any amount paid for the property damages sustained on account of the defective product is payment on account of product liability.

Example (6). Assume the same facts as in example (4) except that the equipment catches on fire during the subsequent servicing of the unit. Because C is in possession of the unit during the servicing, any amount paid for the property damage sustained on account of the defective product would be payment on account of product liability.

Example (7). X, a manufacturer of computers, sells a computer to A. X also has its employees periodically service the computer for A from time to time after it is placed in service. After the initial delivery, installation, servicing, and testing of the computer is completed, the computer catches on fire while X's employee is servicing the equipment. This fire causes property damage to A's office and physical injury to A. Any amount paid for the property or physical damage sustained on account of the defective product is payment on account of product liability.

(c) *Election*—(1) *In general*. The 10-year carryback provision of this section applies, except as provided in this paragraph, to any taxpayer who, for a taxable year beginning after September 30, 1979, incurs a product liability loss. Any taxpayer entitled to a 10-year carryback under paragraph (a) of this section in any loss year may elect (at the time and in the manner provided in paragraph (c)(2) of this section) to have the carryback period with respect to the product liability loss determined without regard to the carryback rules provided by paragraph (a) of this section. If the taxpayer so elects, the product liability loss shall not be carried back to the 10th through the 4th taxable years preceding the loss year. In such case, the product liability loss shall be carried back or carried over as provided by section 172(b) (except subparagraph (1)(I) thereof) and the regulations thereunder.

(2) *Time and manner of making election*. An election by any taxpayer entitled to the 10-year carryback for the product liability loss to have the carryback with respect to such loss determined without regard to the 10-year carryback provision of paragraph (a) of this section must be made by attaching to the taxpayer's tax return (filed within the time prescribed by law, including extensions of time) for the taxable year in which such product liability loss is sustained, a statement containing the information required by paragraph (c)(3) of this section. Such election, once made for any taxable year, shall be irrevocable after the due date (including extensions of time) of the taxpayer's tax return for that taxable year.

(3) *Information required*. In the case of a statement filed after April 25, 1983, the statement referred to in paragraph (c)(2) of this section shall contain the following information:

(i) The name, address, and taxpayer identifying number of the taxpayer; and

(ii) A statement that the taxpayer elects under section 172(j)(3) not to have section 172(b)(1)(I) apply.

(4) *Relationship with section 172(b)(3)(C) election*. If a taxpayer sustains during the taxable year both a net operating loss not attributable to product liability and a product liability loss (as defined in section 172(j)(1) and paragraph (b)(1) of this section), an election pursuant to section 172 (b)(3)(C) (relating to election to relinquish the entire carryback period) does not preclude the product liability loss from being carried back 10 years under section 172(b)(1)(I) and paragraph (a)(1) of this section.

Par. 4. Section 1.537–1 is amended by revising the first two sentences of paragraph (a) and by adding a new paragraph (f) after paragraph (e). These amended and added provisions read as follows:

§1.537–1 Reasonable needs of the business.

(a) *In general*. The term "reasonable needs of the business" includes (1) the reasonably anticipated needs of the business (including product liability loss reserves, as defined in paragraph (f) of this section), (2) the section 303 redemption needs of the business, as defined in paragraph (c) of this section, and (3) the excess business holdings redemption needs of the business as described in paragraph (d) of this section. See paragraph (e) of this section for additional rules relating to the section 303 redemption needs and the excess business holdings redemption needs of the business. * * *

* * * * *

(f) *Product liability loss reserves*. (1) The term "product liability loss reserve" means, with respect to taxable years beginning after September 30, 1979, reasonable amounts accumulated for the payment of reasonably anticipated product liability losses, as defined in section 172(j) and §1.172–13(b)(1).

(2) For purposes of this paragraph, whether an accumulation for anticipated product liability losses is reasonable in amount and whether such anticipated product liability losses are likely to occur shall be determined in light of all facts and circumstances of the taxpayer making such accumulation. Some of the factors to be considered in determining the reasonableness of the accumulation include the taxpayer's previous product liability experience, the extent of the taxpayer's coverage by commercial product liability insurance, the income tax consequences of the taxpayer's ability to deduct product liability losses and related expenses, and the taxpayer's potential future liability to defective products in light of the taxpayer's plans to expand the production of products currently being manufactured, provided such plans are specific, definite and feasible. Additionally, a factor to be considered in determining whether the accumulation is reasonable in amount is whether the taxpayer, in accounting for its potential future liability, took into account the reasonably estimated present value of the potential future liability.

(3) Only those accumulations made with respect to products that have been manufactured, leased, or sold shall be considered as accumulations made under this paragraph. Thus, for example, accumulations with respect to a product which has not progressed beyond the development stage are not reasonable accumulations under this paragraph.

Par 5. Section 1.537–2 is amended by removing "or" at the end of paragraph (b)(4); by removing the period at the end of paragraph (b)(5) and adding "; or" in its place, and by adding a new paragraph (b)(6) after paragraph (b)(5). The amended provision reads as follows:

§1.537–2 Grounds for accumulation of earnings and profits.

* * * * *

(b) ***Reasonable accumulation of earnings and profits.*** *** * ***

(6) To provide for the payment of reasonably anticipated product liability losses, as defined in section 172(j), §1.172–13(b)(1), and §1.537–1(f).

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

PART 602

Par. 6. The authority citation for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 7. Section 602.101(c) is amended by inserting in the appropriate places in the table "§1.172–13 . . . 1545–0863".

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved August 11, 1986.

J. Roger Mentz
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on August 26, 1986, 8:45 a.m., and published in the issue of the Federal Register for August 27, 1986, 51 F.R. 30481)

Section 280F.—Limitation on Investment Tax Credit and Depreciation for Luxury Automobiles

26 CFR 1.280F–2T: Limitations on recovery deductions and the investment tax credit for certain passenger automobiles (temporary).

Investment credit; limitation; luxury automobiles; price inflation adjustment. The automobile price inflation adjustment for passenger automobiles placed in service after December 31, 1984, and before April 3, 1985, and for passenger automobiles acquired by taxpayers pursuant to binding contracts in effect on April 1, 1985, and at all times thereafter, and placed in service after April 2, 1985, and before August 1, 1985, is 2.6 percent. For those vehicles, the amount of credit determined under section 46(a) may not exceed $1,000, the recovery deduction for the first taxable year in the recovery period may not exceed $4,100, and the recovery deductions for any succeeding year in the recovery period may not exceed $6,200.

Rev. Rul. 86–107

ISSUE

What is the automobile price inflation adjustment for 1985 that is provided by section 280F(d)(7) of the Internal Revenue Code for passenger automobiles placed in service after December 31, 1984, and before April 3, 1985?

LAW AND ANALYSIS

Section 280F(a) of the Code, added by section 179(a) of the Tax Reform Act of 1984, 1984–3 (Vol. 1) C.B. 1, 221, limits, for any passenger automobiles, both the amount of the investment tax credit determined under section 46(a) and the amount of the recovery deduction for any tax year. Section 280F(d)(7) provides for a price inflation adjustment for automobiles placed in service after June 18, 1984. For calendar year 1984, the adjustment is zero.

Section 4 of the repeal of contemporaneous recordkeeping requirements, Pub. L. No. 99–44, 1985–2 C.B. 350 (the 1985 Act), reduced the limits in section 280F(a) and amended section 280F(d)(7) by making the inflation adjustment applicable only to cars placed in service after 1988. Section 6(e) of the 1985 Act provides, however, that the postponement provided in section 4 applies only to passenger automobiles placed in service after April 2, 1985. Moreover, the amendments made by section 4 do not apply to passenger automobiles acquired pursuant to a binding contract in effect on April 1, 1985, and at all times thereafter if such automobiles are placed in service before August 1, 1985. Therefore, the unreduced limitations imposed by section 280F(a) and the automobile price inflation adjustment provided by section 280F(d)(7) prior to its amendment by the 1985 Act apply to passenger automobiles placed in service after December 31, 1984, and before April 3, 1985, and to passenger automobiles acquired pursuant to a binding contract in effect on April 1, 1985, and all times thereafter and placed in service before August 1, 1985.

Prior to amendment by the 1985 Act, section 280F(d)(7) of the Code required that for each calendar year after 1984, an adjustment be made to the dollar limitations imposed by section 280F(a). Each calendar year, the dollar limitations were to be increased by an automobile price inflation adjustment and rounded to the nearest multiple of $100. The automobile price inflation adjustment was defined as the percentage (if any) by which the CPI automobile component for October of the preceding calendar year exceeds the CPI automobile component for October 1983.

The term "CPI automobile component" is defined in section 280F(d)(7)(B)(ii) of the Code as the "automobile component" of the Consumer Price Index for all Urban Consumers published by the Department of Labor (the CPI). The new car component of the CPI was 209.6 for October 1984 and 204.3 for October 1983. The October 1984 index exceeded the October 1983 index by 5.3. The Internal Revenue Service has therefore determined that the automobile price inflation adjustment under 280F(d)(7) was 2.6 percent. This adjustment is applicable to all passenger automobiles that were placed in service after December 31, 1984, and before April 3, 1985, and to passenger automobiles acquired by taxpayers pursuant to binding contracts in effect on April 1, 1985, and at all times thereafter, and placed in service after April 2, 1985, and before August 1, 1985. The dollar limitations in section 280F(a) (before its amendment by the 1985 Act) must therefore be increased by a factor of .026, and the resulting amount must be rounded to the nearest multiple of $100. Thus, the $6000 limitation in section 280F(a)(2)(A)(ii) becomes $6200. (Also, the $1000 limitation in section 280F(a)(1) remains $1000, and the $4000 limitation in section 280F(a)(2)(A)(i) becomes $4100.)

HOLDING

The automobile price inflation adjustment for passenger automobiles placed in service after December 31, 1984, and before April 3, 1985, and for passenger automobiles acquired by taxpayers pursuant to binding contracts in effect on April 1, 1985, and at all times thereafter, and placed in service after April 2, 1985, and before August 1, 1985, is 2.6 percent. For those vehicles, the recovery deductions for any taxable year in the recovery period after the first taxable year in the recovery period may not exceed $6200. (Also, the amount of credit determined under section 46(a) may not exceed $1000 and the recovery deductions for the first taxable year in the recovery period may not exceed $4100.

Section 446.—General Rule for Methods of Accounting

26 CFR 1.446–1: General rule for methods of accounting.

Whether the accrued increase in a progressive slot machine jackpot may be deducted when at the close of the tax year, the payee and time of payment are not determinable. See Ct. D. 2033, below.

Section 461.—General Rule For Taxable Year of Deduction

26 CFR 1.461-1: General rule for taxable year of deduction.

(Also Section 446; 1.446-1.)

Ct. D. 2033

SUPREME COURT
OF THE
UNITED STATES
No. 85-554

United States v.
Hughes Properties, Inc.
U.S.

On Writ of Certiorari
to the United States
Court of Appeals
for the Federal Circuit

June 3, 1986

Syllabus

Respondent, in its gambling casino in Reno, Nev., operated a number of "progressive" slot machines. In addition to paying fixed amounts when certain symbol combinations appear on their reels, these machines have a "progressive" jackpot that is won only when a different specified combination appears. The amount of the jackpot increases as money is gambled on the machine until the jackpot is won. A Nevada Gaming Commission regulation prohibits reducing the indicated payoff without paying the jackpot. Utilizing the accrual method of accounting, respondent's practice was, at the end of each fiscal year, to enter the total of the progressive jackpot amounts as an accrued liability on its books, and from that total to subtract the corresponding figure for the preceding year to produce the current tax year's increase in accrued liability. On its federal income tax returns for certain fiscal years, respondent claimed this net figure as a deduction under §162(a) of the Internal Revenue Code of 1954, as an ordinary and necessary business expense incurred during the taxable year. The Commissioner of Internal Revenue (Commissioner) disallowed the deductions on the ground that, under Treasury Regulations, an expense may not be deducted until "all the events have occurred which determine the fact of liability and the amount thereof can be determined with reasonable accuracy," and that, until a patron actually won a progressive jackpot, respondent's liability to pay the jackpot was contingent and therefore was not a deductible expense. Accordingly, the Commissioner determined deficiencies in respondent's income taxes for the years in question. Respondent paid the deficiencies, and when its claims for refunds were denied, brought suit in the Claims Court. The court granted respondent's motion for summary judgment, holding that respondent's liability to pay the progressive jackpots was fixed by the Nevada regulation. The Court of Appeals affirmed.

Held: Respondent was entitled to claim the deductions in question. Pp. 5–13.

(a) The "all events" test prescribed by the Treasury Regulations requires that before an expense can be regarded as "incurred" for federal income tax purposes, a liability must be fixed and absolute. Pp. 6–7.

(b) Here, the effect of the Nevada regulation was to fix respondent's liability. Identification of the winning players is irrelevant to respondent, since the obligation to pay exists and whether it turns out that the winner is one patron or another makes no difference as to liability. The event creating liability was the last play of each progressive slot machine before the end of the fiscal year, since that play fixed the jackpot amount irrevocably. That event occurred during the taxable year. *Brown* v. *Helvering,* 291 U.S. 193, distinguished. Pp. 8–9.

(c) Granting that the Commissioner has broad discretion to determine whether a taxpayer's accounting methods clearly reflect income, that financial accounting does not control for tax purposes, and that the mere desirability of matching expenses with income will not necessarily sustain a taxpayer's deduction, the disallowance of respondent's deductions was not justified. As noted, the jackpot liabilities were fixed, and only the exact times of payment and the winners' identity remained uncertain. Pp. 9–10.

(d) Nothing in the record indicates that respondent used its progressive slot machines for tax-avoidance purposes. Pp. 10–12.

(e) The potential that a casino operator might go out of business, or surrender or lose its license, or go into bankruptcy, with the result that the progressive jackpot would never be paid, does not prevent accrual of the expense. P. 12.

(f) One of the expenses that necessarily attends the production of income from a progressive slot machine is the commitment of a particular portion of the income generated to an irrevocable jackpot. Cf. *United States* v. *Anderson,* 269 U.S. 422. Respondent's true income from its progressive slot machines is only that portion of the money gambled that it is entitled to keep. Pp. 12–13.

760 F.2d 1292, affirmed.

BLACKMUN, J., delivered the opinion of the Court, in which BRENNAN, WHITE, MARSHALL, POWELL, REHNQUIST, and O'CONNOR, JJ., joined. STEVENS, J., filed a dissenting opinion, in which BURGER, C. J., joined.

JUSTICE BLACKMUN delivered the opinion of the Court.

This case concerns the deductibility for federal income tax purposes, by a casino operator utilizing the accrual method of accounting, of amounts guaranteed for payment on "progressive" slot machines but not yet won by playing patrons.

I

A

There is no dispute as to the relevant facts; many of them are stipulated. Respondent Hughes Properties, Inc., is a Nevada corporation. It owns Harolds Club, a gambling casino, in Reno, Nev. It keeps its books and files its federal income tax returns under the accrual method of accounting. During the tax years in question (the fiscal years that ended June 30 in 1973 to 1977, inclusive), respondent owned and operated slot machines at its casino. Among these were a number of what are called "progressive" machines. A progressive machine, like a regular one, pays fixed amounts when certain symbol combinations appear on its reels. But a progressive machine has an additional "progressive" jackpot, which is won only when a different specified combination appears. The casino sets this jackpot initially at a minimal amount. The figure increases, according to a ratio determined by the casino, as money is gambled on the machine. The amount of the jackpot at any given time is registered on a "payoff indicator" on the face of the machine. That amount continues to increase as patrons play the machine until the jackpot is won or until a maximum, also determined by the casino, is reached.

The odds of winning a progressive jackpot obviously are a function of the number of reels on the machine, the number of positions on each reel, and the number of winning symbols. The odds are determined by the casino, provided only that there exists a possibility that the winning combination of symbols can appear.[1]

The Nevada Gaming Commission closely regulates the casino industry in the State, including the operation of progressive slot machines. In September 1972, the Commission promulgated §5.110 of the Nevada Gaming Regulations. See App. 55. This section requires a gaming establishment to record at least once a day the jackpot amount registered on each progressive machine. §5.110.5. Furthermore.

> "[n]o payoff indicator shall be turned back to a lesser amount, unless the amount by which the indicator has been turned back is actually paid to a winning player or unless the change in the indicator reading is necessitated through a machine malfunction, in which case an explanation must be entered on the daily report as required in subsection 5." §5.110.2.

The Regulation is strictly enforced. Nevada, by statute, authorizes the Commission to impose severe administrative sanctions, including license revocation, upon any casino that wrongfully refuses to pay a winning customer a guaranteed jackpot. See Nev. Rev. Stat. §463.310 (1986).

It is respondent's practice to remove the money deposited by customers in its progressive machines at least twice every week and also on the last day of each month. The Commission does not regulate respondent's use of the funds thus collected, but, since 1977, it has required that a casino maintain a cash reserve sufficient to provide payment of the guaranteed amounts on all its progressive machines available to the public. Nev. Gaming Regs. §5.110(3); App. 56.

B

At the conclusion of each fiscal year, that is, at midnight on June 30, respondent entered the total of the progressive jackpot amounts shown on the payoff indicators as an accrued liability on its books. From that total, it subtracted the corresponding figure for the preceding year to produce the current tax year's increase in accrued liability. On its federal income tax return for each of its fiscal years 1973, 1974, 1975, and 1977, respondent asserted this net figure as a deduction under §162(a) of the Internal Revenue Code of 1954, as amended, 26 U.S.C. §162(a), as an ordinary and necessary expense "paid or incurred during the taxable year in carrying on any trade or business."[2] There is no dispute as to the amounts so determined or that a progressive jackpot qualifies for deduction as a proper expense of running a gambling business. See Tr. of Oral Arg. 7.

On audit, the Commissioner of Internal Revenue disallowed the deduction. He did so on the ground that, under Treas. Reg. §1.461–1(a)(2), 26 CFR §1.461–1(a)(2) (1985), an expense may not be deducted until "all the events have occurred which determine the fact of the liability and the amount thereof can be determined with reasonable accuracy." In his view, respondent's obligation to pay a particular progressive jackpot matures only upon a winning patron's pull of the handle in the future. According to the Commissioner, until that event occurs, respondent's liability to pay the jackpot is contingent and therefore gives rise to no deductible expense. Indeed, until then, there is no one who can make a claim for payment. See Tr. of Oral Arg. 11. Accordingly, the Commissioner determined deficiencies in respondent's income taxes for the years in question in the total amount of $433,441.88, attributable solely to the denial of these progressive jackpot deductions. Respondent paid the asserted deficiencies and filed timely claims for refund. When the claims were denied, respondent brought this suit for refunds in the Claims Court.

C

Each side moved for summary judgment. App. 15, 52. Respondent contended that the year-end amounts shown on the payoff indicators of the progressive slot machines were deductible, claiming that there was a reasonable expectation that payment would be made at some future date, that the casino's liability was fixed and irrevocable under Nevada law, that the accrual of those amounts conformed with generally accepted accounting principles, and that deductibility effected a timely and realistic matching of revenue and expenses.

The Claims Court denied the Government's motion for summary judgment but granted respondent's motion. 5 Cl. Ct. 641 (1984). It concluded that, under the Nevada Commission's rule, respondent's liability to pay the amounts on the progressive jackpot indicators became "unconditionally fixed," *id.*, at 645, at "midnight of the last day of the fiscal year," *id.*, at 647. The final event was "the last play (successful or not) of the machine before the close of the fiscal year, that is, the last change in the jackpot amount before the amount is recorded for accounting purposes." *id.*, at 645. A contrary result would mismatch respondent's income and expenses. The court acknowledged that, if respondent were to go out of business, it would not owe the jackpot amount to any particular person. *Id.*, at 646. Nevertheless, the jackpot indicator amount "would still continue to be an *incurred* liability fixed by state law, for which [respondent] would continue to be responsible" (emphasis in original). *Id.*, at 645.

The Claims Court further acknowledged that its ruling was in conflict with the decision of the Court of Appeals for the Ninth Circuit in *Nightingale* v. *United States*, 684 F.2d 611 (1982), having to do with another Nevada casino, but it declined to follow that precedent and specifically disavowed its reasoning. 5 Cl. Ct., at 644–647.

The Court of Appeals for the Federal Circuit affirmed the judgment "on the basis of the United States Claims Court opinion." 760 F.2d 1292, 1293 (1985). It ruled that, under the accrual method of accounting, an expense is deductible in the tax year in which all the events have occurred that determine the fact of liability and the amount thereof can be determined with reasonable accuracy, and that liability exists "if there is an obligation to perform an act and the cost of performance can be measured in money." *Ibid.* The liability here was not contingent upon the time of payment or the identity of the jackpot winner. Rather, it was fixed by the Commission's regulation. The "contrary conclusion" of the Ninth Circuit in *Nightingale* was noted. *Ibid.*

Because of the clear conflict between the two Circuits, we granted certiorari. 474 U.S.——(1985).

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[1] A 1976 study of the 24 4-reel progressive machines then in operation at respondent's casino revealed that the average period between payoffs was approximately 4½ months, although one machine had been in operation for 13 months and another for 35 months without a payoff as of September 1, 1976. The payoff frequency of the other 22 machines ranged from a high of 14.3 months to a low of 1.9 months.

[2] No deduction was asserted for fiscal 1976 because the aggregate accrued liability at the end of fiscal 1976 was less than that at the end of fiscal 1975.

II

Section 162(a) of the Internal Revenue Code allows a deduction for "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." Section 446(a) provides that taxable income "shall be computed under the method of accounting on the basis of which the taxpayer regularly computes his income in keeping his books." Under the "cash receipts and disbursements method," specifically recognized by §446(c)(1), a taxpayer is entitled to deduct business expenses only in the year in which they are paid. Treas. Reg. §§1.446–1(c)(1)(i) and 1.461–1(a)(1). The Code also permits a taxpayer to compute taxable income by the employment of "an accrual method." §446(c)(2). An accrual-method taxpayer is entitled to deduct an expense in the year in which it is "incurred," §162(a), regardless of when it is actually paid.

For a number of years, the standard for determining when an expense is to be regarded as "incurred" for federal income tax purposes has been the "all events" test prescribed by the Regulations. See Treas. Reg. §1.446–1(c)(1)(ii) (accruals in general); §1.451–1(a) (accrual of income); and §1.461–1(a)(2) (accrual of deductions). This test appears to have had its origin in a single phrase that appears in this Court's opinion in *United States* v. *Anderson*, 269 U.S. 422, 441 (1926) ("it is also true that in advance of the assessment of a tax, all the events may occur which fix the amount of the tax and determine the liability of the taxpayer to pay it"). Since then, the Court has described the "all events" test "established" in *Anderson*, as "the 'touchstone' for determining the year in which an item of deduction accrues," and as "a fundamental principle of tax accounting." *United States* v. *Consolidated Edison Co.*, 366 U.S. 380, 385 (1961) (citing cases).

Under the Regulations, the "all events" test has two elements, each of which must be satisfied before accrual of an expense is proper. First, all the events must have occurred which establish the fact of the liability. Second, the amount must be capable of being determined "with reasonable accuracy." Treas. Reg. §1.446–1(c)(1)(ii). This case concerns only the first element, since the parties agree that the second is fully satisfied.

III

The Court's cases have emphasized that "a liability does not accrue as long as it remains contingent." *Brown* v. *Helvering*, 291 U.S. 193, 200 (1934); accord, *Dixie Pine Co.* v. *Commissioner*, 320 U.S. 516, 519 (1944). Thus, to satisfy the all-events test, a liability must be "final and definite in amount," *Security Flour Mills Co.* v. *Commissioner*, 321 U.S. 281, 287 (1944), must be "fixed and absolute," *Brown* v. *Helvering*, 291 U.S. at 201, and must be "unconditional," *Lucas* v. *North Texas Lumber Co.*, 281 U.S. 11, 13 (1930). And one may say that "the tax law requires that a deduction be deferred until 'all the events' have occurred that will make it fixed and certain." *Thor Power Tool Co.* v. *Commissioner*, 439 U.S. 522, 543 (1979).

A

The Government argues that respondent's liability for the progressive jackpots was not "fixed and certain," and was not "unconditional" or "absolute," by the end of the fiscal year, for there existed no person who could assert any claim to those funds. It takes the position, quoting *Nightingale* v. *United States*, 684 F.2d, at 614, that the indispensable event "is the winning of the progressive jackpot by some fortunate gambler." It says that, because respondent's progressive jackpots had not been won at the close of the fiscal year, respondent had not yet incurred liability. Nevada law places no restriction on the odds set by the casino, as long as a possibility exists that the winning combination can appear. Thus, according to the Government, by setting very high odds respondent can defer indefinitely into the future the time when it actually will have to pay off the jackpot. The Government argues that if a casino were to close its doors and go out of business, it would not owe the jackpots to anyone. Similarly, if it were to sell its business, or cease its gaming operations, or go into bankruptcy, or if patrons were to stop playing its slot machines, it would have no obligation.

B

We agree with the Claims Court and with the Federal Circuit and disagree with the Government for the following reasons:

1. The effect of the Nevada Gaming Commission's regulations was to fix respondent's liability. Section 5.110.2 forbade reducing the indicated payoff without paying the jackpot, except to correct a malfunction or to prevent exceeding the limit imposed. App. 55. Respondent's liability, that is, its obligation to pay the indicated amount, was not contingent. That an extremely remote and speculative possibility existed that the jackpot might never be won,[3] did not change the fact that, as a matter of state law, respondent had a fixed liability for the jackpot which it could not escape. The effect of Nevada's law was equivalent to the situation where state law requires the amounts of the jackpot indicators to be set aside in escrow pending the ascertainment of the identity of the winners. The Government concedes that, in the latter case, the liability has accrued, Tr. of Oral Arg. 20–21, even though the same possibility would still exist that the winning pull would never occur.

2. The Government misstates the need for identification of the winning player. That is, or should be, a matter of no relevance for the casino operator. The obligation is there, and whether it turns out that the winner is one patron or another makes no conceivable difference as to basic liability.

3. The Government's heavy reliance on *Brown* v. *Helvering*, 291 U.S. 193 (1934), in our view, is misplaced. That case concerned an agent's commissions on sales of insurance policies, and the agent's obligation to return a proportionate part of the commission in case a policy was canceled. The agent sought to deduct from gross income an amount added during the year to his reserve for repayment of commissions. This Court agreed with the Commissioner's disallowance of the claimed deduction because the actual event that would create the liability—the cancellation of a particular policy in a later year—"[did] not occur during the taxable year," *id.*, at 200, but rather occurred only in the later year in which the policy was in fact canceled. Here, however, the event creating liability, as the Claims Court recognized, was the last play of the machine before the end of the fiscal year, since that play fixed the jackpot amount irrevocably. 5 Cl. Ct., at 645. That event occurred during the taxable year.

4. The Government's argument that the fact that respondent treats unpaid jackpots as liabilities for financial accounting purposes does not justify treating them as liabilities for tax purposes is unpersua-

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[3] An affidavit of the president of respondent's Harolds Club Division, submitted in the Claims Court in support of respondent's motion for summary judgment, states that all the progressive machine jackpots unpaid as of June 30, 1977, "were subsequently won and paid to customers." App. 62.

sive. Proper financial accounting and acceptable tax accounting, to be sure, are not the same. Justice Brandeis announced this fact well over 50 years ago; "The prudent business man often sets up reserves to cover contingent liabilities. But they are not allowable as deductions." *Lucas* v. *American Code Co.*, 280 U.S. 445, 452 (1930). See also *Brown* v. *Helvering*, 291 U.S., at 201–202, and *Lucas* v. *Structural Steel Co.*, 281 U.S. 264, 269 (1930). The Court has long recognized "the vastly different objectives that financial and tax accounting have." *Thor Power Tool Co.* v. *Commissioner*, 439 U.S. at 542. The goal of financial accounting is to provide useful and pertinent information to management, shareholders, and creditors. On the other hand, the major responsibility of the Internal Revenue Service is to protect the public fisc. *Ibid.* Therefore, although §446(c)(2) permits a taxpayer to use an accrual method for tax purposes if he uses that method to keep his books, §446(b) specifically provides that if the taxpayer's method of accounting "does not clearly reflect income," the Commissioner may impose a method that "does clearly reflect income." Thus, the "Commissioner has broad powers in determining whether accounting methods used by a taxpayer clearly reflect income." *Commissioner* v. *Hansen*, 360 U.S. 446, 467 (1959). See also *Thor Power Tool Co.* v. *Commissioner*, 439 U.S., at 532; *American Automobile Assn.* v. *United States*, 367 U.S. 687, 697–698 (1961). The Regulations carry this down specifically to "the accounting treatment of any item." Treas. Reg. §1.446–1(a)(1).

Granting all this—that the Commissioner has broad discretion, that financial accounting does not control for tax purposes, and that the mere desirability of matching expenses with income will not necessarily sustain a taxpayer's deduction, see *American Automobile Assn.* v. *United States*, 367 U.S., at 690; *Thor Power Tool Co.* v. *Commissioner*, 439 U.S., at 541—the Commissioner's disallowance of respondent's deductions was not justified in this case. As stated above, these jackpot liabilities were definitely fixed. A part of the machine's intake was to be paid out, that amount was known, and only the exact time of payment and the identity of the winner remained for the future. But the accrual method itself makes irrelevant the timing factor that controls when a taxpayer uses the cash receipts and disbursements method.[4]

5. The Government suggests that respondent's ability to control the timing of payouts shows both the contingent nature of the claimed deductions and a potential for tax avoidance. It speaks of the time value of money, of respondent's ability to earn additional income upon the jackpot amounts it retains until a winner comes along, of respondent's "virtually unrestricted discretion in setting odds," Brief for United States 31, and of its ability to transfer amounts from one machine to another with the accompanying capacity to defer indefinitely into the future the time at which it must make payment to its customers. All this, the Government says, unquestionably contains the "potential for tax avoidance." See *Thor Power Tool Co.* v. *Commissioner*, 439 U.S., at 538. And the Government suggests that a casino operator could put extra machines on the floor on the last day of the tax year with whatever initial jackpots it specifies and with whatever odds it likes, and then, on the taxpayer's theory, could take a current deduction for the full amount even though payment of the jackpots might not occur for many years, citing *Nightingale*, 684 F. 2d, at 615.

None of the components that make up this parade of horribles, of course, took place here. Nothing in this record even intimates that respondent used its progressive machines for tax-avoidance purposes. Its income from these machines was less than 1% of its gross revenue during the tax years in question. See App. 35–36. Respondent's revenue from progressive slot machines depends on inducing gamblers to play the machines, and, if it sets unreasonably high odds, customers will refuse to play and will gamble elsewhere. Thus, respondent's economic self-interest will keep it from setting odds likely to defer payoffs too far into the future.[5] Nor, with Nevada's strictly imposed controls, was any abuse of the kind hypothesized by the Government likely to happen. In any event, the Commissioner's ability, under §446(b) of the Code, 26 U.S.C. §446(b), to correct any such abuse is the complete practical answer to the Government's concern. If a casino manipulates its use of progressive slot machines to avoid taxes, the Commissioner has the power to find that its accounting does not accurately reflect its income and to require it to use a more appropriate accounting method. Finally, since the casino of course must pay taxes on the income it earns from the use of as-yet-unwon jackpots, the Government vastly overestimates the time value of respondent's deductions.

6. There is always a possibility, of course, that a casino may go out of business, or surrender or lose its license, or go into bankruptcy, with the result that the amounts shown on the jackpot indicators would never be won by playing patrons. But this potential nonpayment of an incurred liability exists for every business that uses an accrual method, and it does not prevent accrual. See, *e.g.*, *Wien Consolidated Airlines, Inc.* v. *Commissioner*, 528 F. 2d 735 (CA9 1976). "The existence of an absolute liability is necessary; absolute certainty that it will be discharged by payment is not." *Helvering* v. *Russian Finance & Constr. Corp.*, 77 F. 2d 324, 327 (CA2 1935). And if any of the events hypothesized by the Government should occur, the deducted amounts would qualify as recaptured income subject to tax. Treas. Reg. §1.461–1(a)(2).

7. Finally, the result in *United States* v. *Anderson*, 269 U.S. 422 (1926), a case to which the Government makes repeated reference, is itself instructive. The issue there was the propriety of the accrual of a federal munitions tax prior to its actual assessment. The assessment was required before the tax became due. The Government's position, in contrast to its position in the present case, was that the tax liability accrued before assessment. The Court held that the absence of the assessment did not prevent accrual of the tax. It recognized that the taxpayer's "true income for the year . . . could not have been determined without deducting . . . the . . . expenses attributable to the production of that income during the year." *Id.*, at 440. One of the expenses that nec-

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[4] The fact that Congress once briefly adopted statutory provisions that specifically would have permitted a taxpayer to deduct anticipated expenses by a reserve mechanism is hardly significant. See §§462(a) and (d)(1)(B) of the 1954 Code as originally adopted, 68A Stat. 158–159, repealed retroactively by the Act of June 15, 1955, ch. 143, §§1 and 3, 69 Stat. 134, 135. But see Deficit Reduction Act of 1984, §91(a), 98 Stat. 598.

[5] Respondent also is unlikely to set extremely high initial jackpots on its machines, since that practice would increase the casino's risk. The initial progressive jackpot amount is the casino's money. If a patron gets the winning combination soon after the machine goes into service, the casino will not have time to recoup the initial jackpot from money gambled by the public. Thus, casinos will tend to set rather low initial jackpots, relying on a percentage of the funds gambled by previous players to contribute the bulk of the progressive jackpot.

essarily attended the production of munitions income was the commitment of a particular portion of the revenue generated to a "reserve for munitions taxes." *Ibid.* Similarly, one of the expenses that necessarily attends the production of income from a progressive slot machine is the commitment of a particular portion of the revenue generated to an irrevocable jackpot. Respondent's true income from its progressive slot machines is only that portion of the money gambled which it is entitled to keep.

The judgment of the Court of Appeals is affirmed.

It is so ordered.

Section 691.—Recipients of Income in Respect of Decedents

26 CFR 1.691(a)-1: Income in respect of a decedent.

Whether an employer must report wages or other compensation for services performed by a deceased former employee and paid to the beneficiary or estate of the employee. See Rev. Rul. 86-109, page 14.

Section 3121.—Definitions

26 CFR 31.3121(a)-1: Wages.

Whether an employer must report wages or other compensation for services performed by a deceased former employee and paid to the beneficiary or estate of the employee. See Rev. Rul. 86-109, page 14.

26 CFR 31.3121(b)-3: Employment; services performed after 1954.
(Also 31.3121(e)-1.)
(Also Section 7701.)

Nonresident and resident aliens; services on the outer Continental Shelf. Services performed by nonresident and resident aliens on an oil rig temporarily attached to the outer Continental Shelf of the United States are "employment" for FICA purposes under section 3121(b) of the Code.

Rev. Rul. 86-108

ISSUE

Are services performed by resident and nonresident aliens on an oil rig attached to the outer Continental Shelf of the United States "employment" under section 3121(b) of the Internal Revenue Code for Federal Insurance Contributions Act (FICA) purposes?

FACTS

A foreign corporation employs individuals to operate an oil rig which is temporarily attached to the outer Continental Shelf of the United States. These individuals are resident aliens and nonresident aliens of the United States, within the meanings of Code sections 7701(b)(1)(A) and (B) of the case, respectively.

LAW AND ANALYSIS

Section 3121(b) of the Code provides that for FICA purposes the term "employment" includes (with certain exceptions) any service performed (1) within the United States by an employee for an employer regardless of the citizenship or residence of either party or (2) outside the United States by a citizen or resident of the United States as an employee for a United States employer.

Section 3121(e)(2) of the Code provides that when used in a geographical sense the term "United States" includes the Commonwealth of Puerto Rico, the Virgin Islands, Guam, and American Samoa.

Section 31.3121(e)-1(b) of the Employment Tax Regulations provides that when used in a geographical sense the term "United States" means the several states, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, Guam, and American Samoa.

Section 7701(a)(9) of the Code provides that under the Code, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof, the term "United States" when used in a geographical sense includes only the states and the District of Columbia.

Section 3(1) of the Outer Continental Shelf Lands Act (the Act), 43 U.S.C. section 1332(1) (1982), provides that it is declared to be the policy of the United States that the subsoil and seabed of the outer Continental Shelf appertain to the United States and are subject to its jurisdiction, control, and power of disposition. Section 4(a)(1) of the Act, 43 U.S.C. section 1333(a)(1), as amended, provides that the Constitution and laws and civil and political jurisdiction of the United States are extended to the subsoil and seabed of the outer Continental Shelf and to all artificial islands and all installations and other devices permanently or temporarily attached to the seabed which may be erected thereon for the purpose of exploring for, developing, or producing resources therefrom, or any such installation or other device (other than a ship or vessel) for the purpose of transporting such resources, to the same extent as if the outer Continental Shelf were an area of exclusive federal jurisdiction located within a state.

Rev. Rul. 81-257, 1981-2 C.B. 214, and Rev. Rul. 77-197, 1977-1 C.B. 344, hold that in view of the foregoing provisions of the Act, drilling rigs attached to the seabed of the outer Continental Shelf are within the United States for purposes of the air transportation tax imposed by section 4261 of the Code. Rev. Rul. 56-505, 1956-2 C.B. 891, holds that under these same provisions of the Act, submerged lands known as the Continental Shelf are part of the United States for purposes of the tax imposed by section 4371 on foreign insurance policies.

The above revenue rulings are based on the determination that because the Act treats the outer Continental Shelf as an area of exclusive federal jurisdiction located within a state for all purposes of fedreal law, the term "United States" in section 7701(a)(9) of the Code includes the outer Continental Shelf and oil rigs operating on it. For the same reason, the term "United States" in section 3121(e)(2) of the Code and section 31.3121(e)-1(b) of the regulations includes the outer Continental Shelf and oil rigs attached to it. Thus, services performed on such oil rigs are performed within the United States for purposes of the definition of employment in section 3121(b).

HOLDING

Services performed by resident and nonresident aliens of the United States for a foreign employer on an oil rig attached to the outer Continental Shelf of the United States are "employment" under section 3121(b) of the Code for FICA purposes.

26 CFR 31.3121(e)-1: State, United States, and citizen.

Whether services performed on an oil rig in the continental shelf of the United States are performed in the "United States." See Rev. Rul. 86-108, this page.

Section 3401.—Definitions

26 CFR 31.3401(a)-1: Wages.

Whether an employer must report wages or other compensation for services performed by a deceased former employee and paid to the beneficiary or estate of the employee. See Rev. Rul. 86-109, page 14.

Section 6401.—Information at Source

26 CFR 1.6401-2: Returns of information as to payments to employees.

Whether an employer must report wages or other compensation for services performed by a deceased

former employee and paid to the beneficiary or estate of the employee. See Rev. Rul. 86-109, below.

Section 6051.—Receipts for Employees

26 CFR 31.6051–1: Statement for employees.
(Also Sections 691, 3121, 3401, 6041; 1.691(a)–1, 31.3121(a)–1, 31.3401(a)–1, 1.6041–2).

Employee compensation; deceased employee; death benefits; information reporting. A employer must report wages or other compensation for services performed by a former deceased employee and paid to the estate or the person entitled to receive the payment of the employee on Form 1099–MISC, Statement for Recipients of Miscellaneous Income, as nonemployee compensation. Rev. Ruls. 64–150 and 71–456 superseded.

Rev. Rul. 86–109

ISSUE

(1) How must the former employer of a deceased employee report payments of the employee's accrued wages and vacation pay that are made to the estate of the employee or to a person who acquired the right to receive the payments?

(2) How must such an employer report payments of death benefits made to the employee's estate or to a person who acquired the right to receive the payments solely because of the death of the employee?

FACTS

Before *A*'s death on April 25, 1984, *A* was employed by *X*, a corporation, and was paid on a monthly basis. From January 1 to April 1, 1984, *A* received $12,000 in wages. When *A* died, *X* owed *A* $3,000 in wages and $2,000 in accrued vacation pay, all of which *X* paid to *A*'s estate. During 1984 *X* also paid $8,000 in death benefits to *A*'s estate. The death benefits were paid under a plan that qualified under section 403 of the Internal Revenue Code and that had been established by *X* for all of its employees. The benefits were not amounts for which *A* possessed a nonforfeitable right while living, but were paid solely by reason of *A*'s death.

LAW AND ANALYSIS

Issue 1

Under section 6051(a) of the Code, every person required to deduct and withhold from an employee a tax under section 3101, relating to the Federal Insurance Contributions Act (FICA), or section 3402, relating to income tax, must furnish to each such employee a written statement showing certain information with respect to the remuneration paid by that person to the employee during the calendar year. The statement must be furnished on or before January 31 of the succeeding year, or, if the employment is terminated before the close of the calendar year, within 30 days after the date of receipt of a written request from the employee if the 30-day period ends before January 31.

Section 691(a)(1) of the Code provides as a general rule that the amount of all items of gross income in respect of a decedent that are not properly includible in the taxable period in which the decedent died or a prior period (including the amount of all items of gross income in respect of a prior decedent, if the right to receive the amount was acquired by reason of the death of the prior decedent) must be included in the gross income for the taxable year when received, of: (A) the estate of the decedent, if the right to receive the amount is acquired by the decedent's estate from the decedent; (B) the person who by reason of the death of the decedent acquires the right to receive the amount, if the right to receive the amount is not acquired by the decedent's estate from the decedent; or (C) the person who acquires from the decedent the right to receive the amount by bequest, devise, or inheritance, if the amount is received after a distribution by the decedent's estate of such right.

Section 691(a)(3) of the Code provides that income in respect of a decedent is considered to have the same character in the hands of the recipient that it would have had in the hands of the decedent had the decedent received such amount while alive.

Under section 3121(a) of the Code, the term "wages" for purposes of the FICA means, with certain exceptions, all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash. Section 3401(a), relating to the withholding of income tax, contains a similar definition.

Section 1.6041–2(a)(1) of the Income Tax Regulations provides that wages, as defined in section 3401 of the Code, paid to an employee are to be reported on Form W–2.

Rev. Rul. 55–229, 1955–1 C.B. 75, concerns a lump sum payment representing accrued annual leave that was earned by a federal government employee and that is payable upon separation from the government. The ruling holds that this payment represents compensation for services rendered. The death of the employee and the receipt of the payment by a beneficiary of the employee does not change the nature and identity of the payment. Thus, under the provisions of section 691(a) of the Code, the payment is includible in the gross income of the beneficiary or estate.

Rev. Rul. 64–150, 1964–1 (Part 1) C.B. 448, states that under the general rule provided in section 691(a)(1) of the Code, the entire amount of salary earned by an employee, but unpaid at death, is income in respect of a decedent and is includible in the gross income of the recipient for the taxable year in which it is received. The amount includible as income in respect of a decedent is not reduced by any FICA withholding or other reduction required to be made from the entire salary earned. Under Rev. Rul. 64–150 an employer is required under section 6041(a) to report on Form 1099, accompanied by Form 1096, the total amount of salary, if $600 or more, unreduced by the amount of any deductions, even though only the net amount is actually paid to the deceased employee's estate or beneficiary.

Rev. Rul. 71–456, 1971–2 C.B. 354, concerns death benefits, and amounts representing regular compensation earned immediately preceding death but unpaid at the time of death, paid to beneficiaries and to the estates of deceased employees. The ruling holds that wages for purposes of the collection of income tax at source do not include these amounts but that wages for purposes of the FICA tax include amounts representing regular compensation that was earned immediately preceding death but was unpaid at the time of death and that are paid by an employer to a survivor of a former employee.

Subsequent to publication of Rev. Rul. 71–456, paragraph (14) was added to section 3121(a) of the Code, effective in the case of any payment made after December 1972. Section 3121(a)(14) excepts from the definition of wages, for FICA purposes only, payments by an employer to a survivor or the estate of a former employee made after the calendar year in which the employee died. Payments to a survivor before the close of the calendar year in which the employee died are subject to FICA.

In the present situation, *X* made payments to *A*'s estate before the close of the calendar year and, thus, the payments are subject to FICA tax. To ensure that *A* receives proper social security credit, the $5,000 in wages and accrued vacation pay earned by *A* prior to death but paid to *A*'s estate after *A*'s death should be included with the $12,000 paid before *A*'s death in Box 13, social security wages, of *A*'s final Form W-2. However, only $12,000 is taxable to *A* and should appear in Box 10, Wages, tips, other compensation.

The $5,000 in accrued wages and vacation pay that were paid to *A*'s estate are taxable to the estate. Under Rev. Rul. 64–150, all amounts earned but unpaid at an employee's death received by an estate or beneficiary of a deceased employee should be reported on Forms 1099 and 1096. Thus, the $5,000 paid to *A*'s estate should be reported on Form 1099 MISC, Statement for Recipients of Miscellaneous Income, as non-employee compensation.

Issue 2

Under section 101(b) of the Code, gross income does not include amounts received, not to exceed $5,000 (whether in a single sum or otherwise), by the beneficiaries of the estate of an employee, if the amounts are paid by or on behalf of an employer and are paid by reason of the death of the employee.

Section 3121(a)(13) of the Code excepts from the definition of wages for FICA purposes any payment or series of payments by an employer to an employee, or any dependent of the employee, that is paid (A) upon or after the termination of the employee's employment relationship because of death or retirement for disability, and (B) under a plan established by the employer that makes provisions for employees generally or a class or classes of employees. This provision does not apply to any payment or series of payments that would have been made if the employment relationship had not been so terminated. The definition of wages under section 3401 for purposes of income tax withholding does not contain an exemption that is similar to the exception in section 3121(a)(13).

Section 1.6041-2(b)(1) of the regulations provides that amounts (i) which are distributed or made available to a beneficiary, and to which section 402 of the Code (relating to employee trusts) or section 403 (relating to employer annuity plans) applies, or (ii) which are described in section 72(m)(3)(B) (relating to life insurance contracts) must be reported on Forms 1099, Statement for Recipients, and 1096, Annual Summary and Transmittal of U.S. Information Returns, to the extent that such payments are includible in the gross income of the beneficiary if the amounts so includible aggregate $600 or more in any calendar year.

Thus, unlike the amounts discussed in Issue 1, the death benefits are not wages for purposes of the FICA tax. Death benefits paid from a qualified plan are amounts paid solely by reason of the employee's death for which the employee did not possess a nonforfeitable right while living. They are reported on Form 1099R, Statement for Recipients of Total Distributions from Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Etc. The entire $8,000 in death benefits from a qualified plan paid by *X* to *A*'s estate should appear on Form 1099R, even though the recipient beneficiaries may exclude up to $5,000 from income as death benefits under section 101(b) of the Code.

HOLDING

Issue 1: Accrued wages and vacation pay of a deceased employee paid to an estate, or other person who has acquired the right to receive the payments, are reported on Form 1099-MISC. These payments are not considered wages for purposes of the collection of income tax at source and thus they do not appear in Box 10, Wages, tips, other compensation, of *A*'s final Form W-2. They are not considered wages for FICA purposes unless paid to the survivor or estate before the close of the calendar year in which the employee died. If they are paid before that date, the total amount of the payments appears in Box 13, Social security wages, of *A*'s final Form W-2, even though it does not appear in Box 10.

Issue 2: The entire amount of death benefits from a qualified plan paid to an estate, or other person who has acquired the right to receive the payments solely because of the death of the employee, should be reported on Form 1099R even though up to $5,000 may be exempt from income tax as death benefits under section 101(b) of the Code. The death benefits of $8,000 paid to *A*'s estate are reported on Form 1099R issued to *A*'s estate.

Death benefit payments from a nonqualified plan are also reported on Form 1099R.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 64–150 is clarified and, as clarified, is superseded.

Rev. Rul. 71–456 is modified and, as modified, is superseded.

Section 7701.—Definitions

The term "United States" includes the outer Continental Shelf and oil rigs attached to it. See Rev. Rul. 86–108, page 13.

Part III. Administrative, Procedural, and Miscellaneous

Inflation Adjustment for Computation of Windfall Profit Tax

Notice 86–10

Section 4989(b) of the Internal Revenue Code requires the determination of an inflation adjustment factor for use in computing the windfall profit tax.

The Service has determined that, for oil removed during the October-December quarter of 1986, the inflation adjustments are as follows:

Tier 1 or Tier 2 oil—0.4679
Tier 3 oil—0.6879

Worksheets for computation of the windfall profit tax are included in the Instructions for Form 6047, Windfall Profit Tax, and an explanation of the inflation adjustment may be found in the Specific Instructions for Line 4 of the worksheets.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Installment Method Reporting by Dealers in Personal Property; Changes from Accrual to Installment Method Reporting

LR-146-81

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document provides proposed regulations relating to installment method reporting by dealers in personal property. Changes to the applicable tax law were made by the Installment Sales Revision Act of 1980 [Pub. L. 96–471, 1980–2 C.B. 489]. These proposed regulations would affect all dealers in personal property who wish to report installment obligations on the installment method and would provide them with the guidance necessary to comply with the law.

DATES: Written comments and requests for a public hearing must be delivered by September 26, 1986. The amendments are proposed to be effective for taxable years ending after October 19, 1980.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR–146–81) Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Paulette Chernyshev of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T), (202) 566–3288, not a toll-free call.

SUPPLEMENTARY INFORMATION: BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 453A of the Internal Revenue Code of 1954 relating to changes from the accrual method to the installment method of accounting by dealers in personal property. For taxable years ending before October 20, 1980, the rules relating to such changes were contained in section 453(c) of the Code. Section 2 of the Installment Sales Revision Act of 1980 (Pub. L. 96–471, 94 Stat. 2251) amended section 453(c) (as amended, section 453(c) provides the definition of the installment method) and replaced the rules in old section 453(c) with those in section 453A.

Under old section 453(c), a dealer in personal property, upon changing from the accrual to the installment method of reporting, was required to include in income amounts received on account of installment obligations accrued in a previous year. Old section 453(c) provided an adjustment in tax for a dealer reporting previously taxed amounts on the installment method. The adjustment was equal to the lesser of the portion of the tax paid in the prior taxable year which was attributable to the gain on the installment payment received in the current taxable year or the portion of the tax for the current year which was attributable to the installment payment. For each of these years, the tax attributable to the gain on the installment payment was equal to the gain multiplied by the effective rate of tax (*i.e.*, the total tax as a percentage of gross income) for the year. Thus, gain was included in gross income twice and each time was taxed at the marginal rate of tax, but the adjustment on account of the double inclusion was computed at an effective rate of tax that was generally lower than either of the marginal rates at which the gain was taxed. These rules were not included in section 453A. In addition, the Installment Sales Revision Act repealed section 481(d). Before its repeal, section 481(d) provided that section 481 (relating to adjustments required by changes in method of accounting) did not apply to changes to which old section 453(c) applied.

In place of the adjustment provided in old section 453(c), Congress intended that the cut-off method be applied in accounting for changes by dealers from the accrual method to the installment method of reporting. Under the cut-off method provided in the proposed regulations, payments received by a dealer in the taxable year for which the dealer elected the installment method of reporting (or in subsequent years) in respect of an installment obligation which arose in a taxable year prior to the election year are not taken into account under the installment method. Such payments are accounted for only under the method of accounting in use in the prior year.

Additionally, because old section 453(c) was repealed, the proposed regulations provide that taxpayers may no longer revoke elections to use the installment method in the manner provided by old section 453(c)(4). A dealer may not change from the installment method to any other method of accounting without the consent of the Commissioner of Internal Revenue.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

Although this document is a notice of proposed rulemaking that solicits public comments, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, a regulatory flexibility analyses is not required under the Regulatory Flexibility Act (5 U.S.C. chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504 (h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies of those comments to the Service.

DRAFTING INFORMATION

The principal author of these regulations is Linda M. Kroening of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury participated in developing the regulation on matters of both substance and style.

* * * * *

Proposed amendments to the regulations

The proposed amendments to 26 CFR Parts 1 and 602 are as follows:

INCOME TAX REGULATIONS
(26 CFR PART 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.453A–3 also issued under 26 U.S.C. 453A.

Par. 2. Sections 1.453–7 and 1.453–8 are removed.

Par. 3. New §1.453A–3 is added at the appropriate place to read as follows:

§1.453A–3 Requirements for adoption of or change to installment method by dealers in personal property.

(a) *In general.* A dealer in personal property (within the meaning of §1.453A–1) may adopt or change to the installment method for a type or types of sales on the installment plan (within the meaning of §1.453A–2) in the manner prescribed in this section. This section does not apply to sales other than sales on the installment plan by dealers in personal property.

(b) *Time and manner of electing installment method reporting*—(1) *Time for election.* An election to adopt or change to the installment method for a type or types of sales must be made on an income tax return for the taxable year of the election, filed on or before the time specified (including extensions thereof) for filing such returns.

(2) *Adoption of installment method.* A taxpayer who adopts the installment method for the first taxable year in which sales are made on an installment plan of any kind must indicate in the income tax return for that taxable year that the installment method of accounting is being adopted and specify the type or types of sales included within the election. If a taxpayer in the year of the initial election made only one type of sale on the installment plan, but during a subsequent taxable year makes another type of sale on the installment plan and adopts the installment method for that other type of sale, the taxpayer must indicate in the income tax return for the subsequent year that an election is being made to adopt the installment method of accounting for the additional type of sale.

(3) *Change to installment method.* A taxpayer who changes to the installment method for a particular type or types of sales on the installment plan in accordance with this section must, for each type of sale on the installment plan for which the installment method is to be used, attach a separate statement to the income tax return for the taxable year with respect to which the change is made. Each statement must show the method of accounting used in computing taxable income before the change and the type of sale on the installment plan for which the installment method is being elected.

(4) *Deemed elections.* A dealer in personal property (including a person who is a dealer as a result of the recharacterization of transactions as sales) is deemed to have elected the installment method if the dealer treats a sale on the installment plan as a transaction other than a sale and fails to report the full amount of gain in the year of the sale. For example, if a transaction treated by a dealer as a lease is recharacterized by the Internal Revenue Service as a sale on the installment plan, the dealer will be deemed to have elected the installment method assuming the dealer failed to report the full amount of gain in the year of the transaction.

(c) *Consent.* A dealer in personal property may adopt or change to the installment method for sales on the installment plan without the consent of the Commissioner. However, a dealer may not change from the installment method to the accrual method of accounting or to any other method of accounting without the consent of the Commissioner.

(d) *Cut-off method for amounts previously accrued.* An election to change to the installment method for a type of sale applies only with respect to sales made on or after the first day of the taxable year of change. Thus, payments received in the taxable year of the change, or in subsequent years, in respect of an installment obligation which arose in a taxable year prior to the taxable year of change are not taken into account on the installment method, but rather must be accounted for under the taxpayer's method of accounting in use in the prior year.

(e) *Effective date.* This section applies to sales by dealers in personal property in taxable years ending after October 19, 1980. For rules relating to sales by dealers in personal property in taxable years ending before October 20, 1980, see 26 CFR 1.453–7 and 1.453–8 (rev. as of April 1, 1985).

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT
(26 CFR PART 602)

Par. 4. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 5. Section 602.101(c) is amended by inserting in the appropriate place in the table "§1.453A–3 . . . [ ]".

This notice of proposed rulemaking is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).

P.E. Coates,
Acting Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on July 25, 1986, 8:45 a.m., and published in the issue of the Federal Register for July 28, 1986, 51 F.R. 26909)

Foundations Status of Certain Organizations

Announcement 86–96

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

A New Beginning, Inc., Kansas City, KS
Abilene High Rollers, Abilene, TX
Activities of Daily Living Research Center, Inc., Rockville, MD
African Educational Project, Inc., Philadelphia, PA
Alternatives to Abortion of Brazos County, Inc., Bryan, TX
Amarillo Speech Hearing & Language Foundation, Inc., Amarillo, TX
American and International Friends of the Victoria & Albert Museum, Inc., New York, NY
American-Lebanon Private Spector Co-operation, Inc., Washington, DC
Animal Research Associates, Inc., San Diego, CA
Arbor Housing Associates, Seattle, WA
Area IV Senior Action Senate, Houston, TX
Area Ten Intercity Corp., Houston, TX
Art Deco Society of Washington, Inc., The, Washington, DC
Artsmedia, Inc., Richmond, VA
Association of Perinatal Education, The, Martinsville, VA
Atascosa County Fair Association, Charlotte, TX
Atchison Health Care, Atchison, KS
Athletes United for Peace, Inc., Lawrence, KS
Atrisco Valley Little League, Albuquerque, NM
Austin Area Black Leadership, Austin, TX
Aware Foundation, Johnstown, PA
Believers Ministries, The, Bedford, PA
Benjamin E. Mays National Educational Center, Inc., Washington, DC
Bereshis Foundation, The, Charlottesville, VA
Berks Ballet Theatre, Inc., Reading, PA
Brownfield Senior Citizens, Brownfield, TX
Burrowes Mansion Skirmish Committee, Matawan, NJ
Business Development Corp., Warrington, PA
C. Mildred Petaccio-Memorial Charitable Trust, The, Clifton, NJ
Cambodian Community Club of Washington State, Seattle, WA
Canes and Ables Organization for the Handicapped, Inc., Hackensack, NJ
Casa Puertoriquena De Paterson, Paterson, NJ
Catholic Housing Corporation of Centralia, Harrisburg, PA
Cavalier Daily Publishing, Inc., Charlottesville, VA
Center for Biblical Understanding, The, Martinsville, VA
Center for Community Organizations, Washington, DC
Center for Family Studies, Inc., Philadelphia, PA
Center for Palladian Studies in America, Inc., Charlottesville, VA
Center of More Abundant Life, Inc., The, Baltimore, MD
Chesapeake Bird Sanctuary, Inc., Upper Marlboro, MD
Child Growth and Development of Texas, Inc., Richmond, TX
Children Held Hostage, North Wales, PA
Christ In You, Ministry, Inc., Philadelphia, PA
Christian Gateways Ministries, New Boston, TX
Christian Health Ministries, Inc., Virginia Beach, VA
Christian Marriage Ministries, Austin, TX
Cibola General Hospital Foundation, Grants, NM
Citizens Concerned for Battered Women, Sterling, CO
Clint Reichert Memorial Charitable Trust, Hanover, PA
Coalition of the Ottawa Peoria, Miami, OK
Cobourg & District Historical Society, Cobourg, Ontario Canada
Community Christian Concern of Southern Oregon, Central Point, OR
Community Housing Resources Board, The Fund, Inc., Rockville, MD
Cornell Elementary Parents and Teachers Association, Coraopolis, PA
Cranberry Volunteer Ambulance Corps., Inc., Warrendale, PA
Creative Aging Center, Inc., Arvada, CO
Creative Artists Network, Philadelphia, PA
Dales Evans Sheltered Day Care Center, Inc., Uvalde, TX
Dallas Wheelchair Tennis Club, Dallas, TX
Damascus House, Inc., Baltimore, MD
Dance Rep, Inc., New York, NY
Dance World Foundation, Fairfax, VA
Del-Art Inc., Point Pleasant, PA
Delaware Valley Blind Beep Baseball League Adelphia House, Philadelphia, PA
Denver Civic Ventures, Inc., Denver, CO
Denver Days, Ltd., Denver, CO
Denver Indian Center, Inc., Denver, CO
Dial Inspiration Ministries, Inc., Abington, PA
Dr. Lillie Carroll Jackson Museum, Inc., Baltimore, MD
Dorchester Hospice Foundation, Inc., Cambridge, MD
Dulaney Valley Symphony Society, Inc., Towson, MD
Edward J. Courtney Memorial Building Trades Scholarship Foundation, Inc., The, Baltimore, MD
Elderly Care Institute, Allentown, PA
Energy Management Institute, Inc., Pittsburgh, PA
Fairfax County Crime Solvers, Fairfax, VA
Faith Outreach Ministries, Mesa, AZ
Father Joe Enotas Memorial Scholarship Fund, The, Austin, TX
Fellowship Urban Services Corp., East Orange, NJ
Floyd County Humane Society, The, Floyd, VA
4th and Rhode Island Avenue Business and Professional Assn., Washington, DC
Foundation Attacking Cancer of the Testicle, Bala, PA
Foundation of the Americas, El Paso, TX
Friends of Fort Davis National, Fort Davis, TX
Friends of Government House, Inc., Annapolis, MD
Friends of Light Opera in Virginia, Inc., Hampton, VA
Ganados Del Valle, Los Ojos, NM
Gerald Marks Colorectal Surgery Foundation, Philadelphia, PA
Gilbert N. Casady Anesthesiology, Hutchinson, KS
Harlingen Community Revitalization, Harlingen, TX
Heirgive Foundation, Phoenix, AZ
Hide and Seek Foundation, Inc., Gibbsboro, NJ
Hills Angels Gymnastic Team, Inc., Wheaton, MD
Historic Baltimore Society, Inc., Randallstown, MD
Historic Boise, Inc., Boise, ID
James Bay Cree Foundation of Quebec, Ottawa Ontario, Canada
Jesuit Institute for Holistic Spirituality, Milford, OH
Jicarilla Apache Centennial, Dulce, NM
John David Young, Jr. Urological Foundation, Rallston, MD
Kent County Medical Health Association, Inc., Chestertown, MD
Key Center Playground Project, Springfield, VA
Kipper Mease Memorial Scholarship, Pasadena, TX
L.B. Taylor Ministries, Inc., Philadelphia, PA

La Incorporacion Del Valle Alto, Canutillo, TX
Lao Community Association of Tucson, Arizona, Inc., Tucson, AZ
League of Women Voters of Denver Education Fund, Denver, CO
Legal Educational Office, Inc., San Miguel, NM
Lehigh Valley Housing Development Corp., Allentown, PA
Liberal Area Crime Commission, Inc., Liberal, KS
Light House Ministries, Pen Argyl, PA
Louisa United Methodist Housing Development Corp., Richmond, VA
Love and Kindness, Inc., Volunteer Services Council for Lindale Nursing Cen., Lindale, TX
Love, Sorrow, Lifting of Jesus Ministries, Inc., Pittsburgh, PA
Lovely Civic Community Corp., Philadelphia, PA
M.H. Residences Inc., Philadelphia, PA
MHA Housing, Inc., Wellsboro, PA
Martin Luther King, Jr. Community Center, Inc., Arlington, VA
Mary Munford Elementary School Parent-Teacher Organization of Richmond, VA, Richmond, VA
Maryland Business Advisory Center, Inc., Baltimore, MD
Masters Workshop, Inc., Wescosville, PA
McDonough Institute, The, Washington, DC
Mid Shore Parent Aide, Inc., Denton, MD
Moleculon Research Institute, Inc., Cambridge, MA
Montbello Center for Community Life, Inc., Denver, CO
Mount Vernon Amateur Radio Club, Inc., Alexandria, VA
National Foundation for Christian Education, Washington, DC
National Foundation on Gerontology for Teaching Research and Special Studies, San Antonio, TX
National Sportfishing Association of America, Ridge, MD
Netcare Residential Apartments, Columbus, OH
New Pathways Forum, Inc., Washington, DC
New Tradition Senior Citizen Center, McKees Rocks, PA
Nolan County Crime Stoppers, Inc., Sweetwater, TX
North American Forum on the Catechumonate, The, Washington, DC
Northridge Retirement Center, Inc., Lamesa, TX
Northwest Oklahoma City Community Services Association, Inc., Oklahoma City, OK
Oklahoma Production Center, Tahlequah, OK
Old Charlottesville, Inc., Charlottesville, VA
Old Telephone Museum, Inc., The, Morrill, ME
Open Door Bible Club, Inc., Butler, PA
Oral Histories of Fort Worth, Inc., Fort Worth, TX
Outreach Foundation, The, Bethesda, MD
P Street Beach Wildlife Association, Inc., Washington, DC
Para Paddlers, Inc., Boulder, CO
Patrick E. Gorman Scholarship Fund, Washington, DC
Pellekin Multi-Arts, Inc., Pittsburgh, PA
Penn Hills Volunteer Firemen's Association, Inc., Verona, PA
People Animals Love, Inc., Washington, DC
People's Educational and Cultural Exchange, Inc., Peabody, KS
Personal Development Foundation, Colorado Springs, CO
Phil Devries Ministries, Inc., West Chester, PA
Philadelphia Cooperation Office, Philadelphia, PA
Philippine Surgeons Charity, Inc., Langhorne, PA
Potomac Soccer Association, Potomac, MD
Prayer of Faith Ministry, Verona, PA
Prince George's Champion's Association, Inc., Bowie, MD
Progressive Foundation for Human Survival and Preservation, Inc., Newport News, VA
Racquetball Authority of Metropolitan Baltimore, Inc., Baltimore, MD
Richard Hatch Ministries, Inc., Pittsburgh, PA
Rockbridge Amateur Radio Club, Lexington, VA
St. Lawrence Centre Transformation Fund, Toronto, Ontario
Samaritan Counseling Center of Beaver Valley, Inc., Beaver, PA
San Juan Medical Foundation, Inc., Farmington, NM
Save Our Babies Foundation, Washington, DC
Search the Scriptures, Inc., Pittsburgh, PA
Second Generation Children of Holocaust Survivors, Inc., Baltimore, MD
Shenandoah Valley Historical Institute, Inc., Harrisonburg, VA
Shiloh Maranatha Ministry and Christian Academy, Inc., Ifeld, NM
Sick Kids (Need) Involved People, Inc., Severna Park, MD
Sickle Cell Anemia Foundation of Virginia, Richmond, VA
Snappy Toys, Inc., Baltimore, MD
Society for Urban Anthropology, The, Pittsburgh, PA
Society of Thoracic Radiology, Washington, DC
Southern Alleghanies Emergency Health Services Council, Inc., Altoona, PA
Southhampton Interagency Communication Committee Volunteer Program, The, Courtland, VA
Spay Neuter All Pets, Inc., Baltimore, MD
Specialized Carriers & Rigging Foundation, Washington, DC
Spokane Chiefs Hockey Education Foundation, Spokane, WA
Star Valley Senior Citizens, Inc., Afton, WY
State Police Memorial Association, The, West Trenton, NJ
Station to Station Writer's Collective, Inc., Washington, DC
Sunshine Foundation International, The, Pittsburgh, PA
Swaddlings, Inc., Annapolis, MD
Texas Health, Education, & Research Foundation, The, Houston, TX
The Plains Community League, The Plains, VA
Therapeutic Recreation Advisory Council, Albuquerque, NM
Thomas Nelson Community College Alumni Association, Hampton, VA
Thomas Nelson Community College Educational Foundation, Inc., Hampton, VA
Togetherness in Friendship, Inc., Trinidad, CO
Touch "N" Tech Children's Museum, Somerville, NJ
Trumpet Ministries, Bedford, PA
Trust for the Support of Residents of Wesley Village, Wilkes-Barre, PA
Tulsa County Area Livestock Association, Inc., The, Broken Arrow, OK
1219 Unemployed Charitable Trust, The, Braddock, PA
Upper Valley Mental Health Association, Vail, CO
Urban Environment Conference, Inc., Washington, DC
Using Space for America Foundation, Arlington, VA
Valley Center for the Arts, Inc., New Kensington, PA

Valve Manufacturers Association Foundation, Washington, DC
Victoria Safety Council, Victoria, TX
Virgin Islands Tae Kwon Do Federation, Inc., St. Thomas US, VI
Virginia Muslim Community, Richmond, VA
Volunteer Health Professionals, Inc., Oakland, MD
Volunteer Safety Patrol, San Antonio, TX
Vote, Inc., Williamsburg, VA
Washington Center for Attitudinal Healing, Inc., Washington, DC
Wattsburg Area Sports Corp., Erie, PA
West Hills Community Theatre, Inc., McKees Rocks, PA
Western Solidarity, Inc., Denver, CO
William A. Parker Health Care Scholarship Foundation, Inc., Bowie, MD
World Society for the Protection of Animals, Boston, MA
Worship Centers, Inc., Canon City, CO
Writing As Therapy Services, Florham Park, NJ
York River Medical Building, Inc., West Point, VA
Young Dillingers, Inc., Washington, DC
Youth Fellowship Athletic Association, Washington, DC
Ypapanti Home for the Elderly, Inc., East Pittsburgh, PA

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)-7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

The following organization, which has been treated as a private operating foundation described in section 4942(j)(3) of the Code, has now been classified as an organization that is not a private operating foundation. Grantors and contributors may no longer rely upon rulings or determinations that this organization is a private operating foundation. The organization is:

Pacific Research Foundation, La Jolla, CA

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practictioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Robert D. Digby	North Little Rock, AR	Certified Public Accountant	Four Months from July 29, 1986
Jeffrey E. Ellis	Rockland, ME	Certified Public Accountant	Indefinte from July 2, 1986
Charles L. Honey	Prescott, AR	Attorney	One Year from July 2, 1986
Bernhardt Karp	Hudson, NY	Attorney & Certified Public Accountant	Indefinite from July 29, 1986
George N. Meros	Springfield, MO	Attorney	Indefinite from July 25, 1986
William G. Waldrop	Adamsville, AL	Certified Public Accountant	Indefinite from July 17, 1986

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to identify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
David P. Rosenberg	Philadelphia, PA	Indefinite effective August 13, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor.
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

Finding List of Current Action on Previously Published Rulings[1]

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1986-38

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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

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SPECIAL ANNOUNCEMENT

Announcement 86–97, page 52.
A public hearing will be held on November 17, 1986, on proposed regulations relating to: (1) the tax treatment of debt instruments issued after July 1, 1982, that contain original issue discount, (2) the imputation of and the accounting for interest with respect to sales and exchanges of property occurring after December 31, 1984, and (3) safe haven interest rates for loans or advances between commonly controlled taxpayers and safe haven leases between such taxpayers.

INCOME TAX

Rev. Rul. 86–110, page 4.
S corporations; election; inadvertent termination; ineligible shareholder. A small business corporation whose election was terminated because stock for a limited period of time was inadvertently transferred to an ineligible trust will be treated as continuing to be an S corporation under section 1362(f) of the Code for the period specified by the Service during which the stock was held by the ineligible trust.

Rev. Rul. 86–112, page 12.
Limited partnerships. The states of Kansas, New Jersey, and Ohio are added to the list of states that have enacted legislation that corresponds to the Uniform Limited Partnership Act for purposes of section 301.7701–2 of the regulations. Rev. Rul. 84–80 amplified.

Ct. D. 2034, page 8.
Excess earned-income credit; past due child support. An excess earned-income credit is an overpayment for purposes of section 6402(a) of the Code and may be intercepted and applied to past due child support obligations under section 6402(c). *Sorenson*, Supreme Court of the United States.

EXEMPT ORGANIZATIONS

Announcement 86–98, page 52.
A list is given of organizations now classified as private foundations.

EMPLOYMENT TAXES

Rev. Rul. 86–111, page 5.
FICA tax liability. An employee is liable for unwithheld FICA taxes after the employer's liability for the taxes has been determined under section 3509 of the Code.

EXCISE TAXES

Rev. Rul. 86–113, page 6.
Manufacturers; truck; gross vehicle weight; use of readily attachable components. For purposes of determination of gross weight under section 4051(a) of the Code, the term "readily attachable components" is defined as springs, brakes, rims and tires. Rev. Ruls. 85–196 and 86–43 clarified.

TAX CONVENTIONS

Canada, page 13.
The "Convention between the United States of America and Canada with Respect to Taxes on Income and Capital" is reproduced.

ADMINISTRATIVE

T.D. 8097, page 6.
The due date is extended for certain requests for waiver or approval of a magnetic medium required for the filing of certain tax returns.

Finding Lists begin on page 57.
Announcement of Disbarments and Suspensions on page 55.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the Internal Revenue Bulletin as the source would be appropriate.

For sale by the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402. Prices: Domestic—$1.75 a single copy, $82.00 a year subscription. Foreign—$2.19 a single copy, $102.50 a year for subscription.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 1362.—Election; Revocation; Termination

S corporations; election; inadvertent termination; ineligible shareholder. A small business corporation whose election was terminated because stock for a limited period of time was inadvertently transferred to an ineligible trust will be treated as continuing to be an S corporation under section 1362(f) of the Code for the period specified by the Service during which the stock was held by the ineligible trust.

Rev. Rul. 86–110

ISSUE

If a corporation's election to be an S corporation is automatically terminated because the corporation inadvertently had one or more ineligible shareholders for a limited period of time before discovery and correction, is the corporation treated as continuing to be an S corporation under section 1362(f) of the Internal Revenue Code during the period when it had one or more ineligible shareholders?

FACTS

X corporation is an electing small business corporation. *A*, the majority shareholder of *X*, on advice of counsel, transferred shares of *X* stock to two irrevocable trusts for the benefit of *A*'s minor children. Neither trust was an eligible shareholder under section 1361(c)(2) or section 1361(d)(3) of the Code because neither trust was treated by sections 671 through 679 as entirely owned by an individual that is a citizen or resident of the United States and because each trust had more than one income beneficiary. Thus, under section 1362(d)(2), the transfer of stock to the trusts resulted in an automatic termination of the S corporation election.

It was not *A*'s desire or expectation to terminate the election when the transfer of the stock was made to the trusts. *A* acted on the advice of counsel that such transfers would not jeopardize the Subchapter S election, and *A* would not have made the transfers but for this advice. *X* and its shareholders continued to file returns and report income in a manner consistent with their belief that the election was still in effect.

Within a reasonable period of time after discovery of the termination, *A* took steps to correct the problem so that *X* once more qualified as a small business corporation. In addition *X*, and each shareholder of *X*, agreed to make any adjustments required by the Service with respect to such period as the Service might specify.

LAW AND ANALYSIS

Section 1361(a) of the Code provides that the term "S corporation" means, with respect to any tax year, a small business corporation for which an election under section 1362(a) is in effect.

Section 1361(b)(1) of the Code defines a "small business corporation" as a domestic corporation that is not an ineligible corporation and does not (A) have more than 35 shareholders, (B) have as a shareholder, a person (other than an estate and other than a trust described in section 1361(c)(2)) that is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than one class of stock.

Section 1361(c)(2) of the Code provides that four types of domestic trusts may be shareholders of an S corporation: a trust that is treated as owned by an individual who is a citizen or resident of the United States; a trust that was treated as owned by an individual who was a citizen or resident of the United States immediately before the death of the deemed owner and that continues in existence after such death, but only for the 60-day period (or 2-year period if the entire corpus of the trust is includible in the gross estate of the deemed owner) beginning on the day of the deemed owner's death; a trust with respect to stock transferred to it pursuant to the terms of a will, but only for the 60-day period beginning on the day on which such stock is transferred to it; and a trust created primarily to exercise the voting power of stock transferred to it.

Section 1361(d) of the Code provides that a qualified subchapter S trust can be treated as a trust described in section 1361(c)(2) if a beneficiary of the trust makes an election for such treatment. A qualified subchapter S trust is a trust the terms of which require that (i) during the life of the current income beneficiary, there shall be only one income beneficiary of the trust; (ii) any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary; (iii) the income interest of the current income beneficiary in the trust shall terminate on the life of the current income beneficiary, the trust shall distribute all of its assets to such beneficiary. In addition, all the income of the trust must be distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States.

Section 1362(d)(2) of the Code provides that an election under section 1362(a) will be terminated whenever (at any time on or after the first day of the first taxable year for which the corporation is an S corporation) the corporation ceases to be a small business corporation.

Section 1362(f) of the Code provides that if (1) an election by any corporation is terminated under section 1362(d)(2) or (3) of the Code, (2) the Secretary determines that the termination was inadvertent, (3) no later than a reasonable period of time after discovery of the terminating event, steps are taken so that the corporation is once more a small business corporation, and (4) the corporation, and each person who was a shareholder during the period specified under section 1362(f), agree to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to that period, then, notwithstanding the terminating event, such corporation will be treated as continuing to be an S corporation during the period specified by the Secretary.

S. Rep. No. 97–640, 97th Cong., 2d Sess. 12 (1982), 1982–2 C.B. 718, 723, discusses section 1362(f) of the Code. It states in part:

> If the Internal Revenue Service determines that a corporation's subchapter S election is inadvertently terminated, the Service can waive the effect of the terminating event for any period if the corporation timely corrects the event and if the corporation and the shareholders agree to be treated as if the election has been in effect for such period.

Under the facts presented, since *A* transferred stock to trusts that are ineligible shareholders under section 1361(b)(1) of the Code, *X* ceased to be a small business corporation, thereby terminating its S corporation election. However, the termination was inadvertent. *A* acted on advice of counsel and would not have made the transfers but for this advice. Further, *A* took the necessary steps to correct the problem within a reasonable time after discovery of the termination and *X* and its shareholders agreed to make such adjustments as may be required by the Secretary.

HOLDING

The S corporation is treated as continuing to be an S corporation under section 1362(f) of the Code for the period specified by the Service during which it had one or more ineligible shareholders.

Section 3101.—Rate of Tax

26 CFR 31.3101–1: Measure of employee tax.

Whether an employee is liable for the amount of unwithheld FICA taxes even after the employer's liability for the taxes has been determined under section 3509 of the Code. See Rev. Rul. 86–111, page 5.

Section 3102.—Deduction of Tax from Wages

26 CFR 31.3102–1: Collection of, and liability for, employee tax; in general.

Whether an employee is liable for the amount of unwithheld FICA taxes even after the employer's liability for the taxes has been determined under section 3509 of the Code. See Rev. Rul. 86–111, page 5.

Section 3509.—Determination of Employer's Liability for Certain Employment Taxes

(Also Sections 3101, 3102; 31.3101–1, 31.3102–1.)

FICA tax liability. An employee is liable for unwithheld FICA taxes after the employer's liability for the taxes has been determined under section 3509 of the Code.

Rev. Rul. 86–111

ISSUE

If an employer fails to deduct and withhold Federal Insurance Contributions Act (FICA) taxes with respect to an employee and if the employer's liability for the employee's share of FICA taxes is determined under section 3509 of the Internal Revenue Code, is the employee's liability for the unwithheld FICA taxes reduced by the employer's payment?

FACTS

In 1983 an employer, *ER*, failed to deduct and withhold employment taxes (including income tax withholding) from the wages of a worker because the employer erroneously treated the worker as an independent contractor for purposes of federal employment taxes (including income tax withholding). The employer did not intentionally disregard the requirement to deduct and withhold the employment taxes. In 1984, the Internal Revenue Service reclassified the worker an an employee and determined, under section 3509 of the Code, the amount of *ER*'s liability for unwithheld 1983 federal employment taxes. Pursuant to section 3509, *ER* was assessed, and *ER* paid, 20 percent of the unwithheld FICA tax. The relief provisions of section 530 of the Revenue Act of 1978, 1978–3 (Vol. 1) C.B. xi, 119–20, which were extended indefinitely by the Tax Equity and Fiscal Responsibility Act of 1982, section 269(c), 1982–2 C.B. 462, 536, do not apply.

The worker filed a Form 1040, U.S. Individual Income Tax Return, and a Schedule SE, Computation of Social Security self-Employment Tax, for 1983. After *ER* paid the assessment, the worker filed a Form 1040X, Amended U.S. Individual Income Tax Return, claiming a refund of the self-employment tax paid.

LAW AND ANALYSIS

Section 3101 of the Code imposes a tax on wages received by an employee with respect to employment (employee's share of FICA tax). Section 3102 requires that the tax imposed by section 3101 be collected by the employer of the taxpayer by deducting the amount of the tax from the wages paid. Every employer required to deduct the tax is liable for its payment.

Section 31.3102–1(c) of the Employment Tax Regulations provides that the employer is liable for the employee tax with respect to all wages paid by the employer to each employee whether or not it is collected from the employee. The regulation further provides that, until the employee tax is collected from the employee, the employee also is liable for the employee tax with respect to all wages received.

Section 3509 of the Code provides, in part, that if an employer, with respect to any employee, fails to deduct and withhold from wages the employee's share of FICA tax because the employer, without intentionally disregarding the requirement to deduct and withhold that tax, treated the employee as a nonemployee for purposes of that tax, the amount of the employer's liability for the employee's share of FICA tax shall be determined as if the taxes imposed under FICA were 20 percent of the amount determined under section 3101. (The amount is 40 percent if the employer failed to file information returns unless such failure was due to reasonable cause.)

Section 3509(d)(1) of the Code provides, in part, that if the amount of any liability for tax is determined under section 3509, then (A) the employee's liability for tax shall not be affected by the assessment or collection of the tax so determined, (B) the employer shall not be entitled to recover from the employee any tax so determined, and (C) section 6521 shall not apply. Under certain circumstances, section 6521 permits self-employment taxes paid to offset liability for the employee's share of FICA tax.

Section 3509(d)(1)(C) of the Code makes section 6521 inapplicable if the amount of any liability for tax is determined under section 3509. Thus, if the amount of the employer's liability for the employee's share of FICA is determined under section 3509, then section 6521 cannot effect a reduction in that employer liability. The only tax liability determined under section 3509, however, is the employer's. Moreover, section 3509(d)(1)(A) states that the employee's liability is not to be affected by the assessment and collection of the tax determined under section 3509. Accordingly, application of section 3509 to the employer's tax liability for the employee's share of FICA does not preclude the employee from enjoying the benefit of section 6521, if that section is otherwise available.

Section 3101 of the Code imposes FICA tax on an employee. Section 3102 requires an employer to collect the tax imposed by section 3101, and also makes the tax a liability of the employer. Thus, both the employee and the employer are liable for the employee's share of FICA taxes, although the intent is that the employer will collect it from the employee and remit it to the Government. Regardless of whether it is the employer or the Government who collects it from the employee, the employee is ultimately liable for the tax imposed by section 3101. Section 31.3102–1(c) of the regulations.

If section 3509 of the Code applies to an employer, the employer's liability for the employee's share of FICA tax equals a stated percentage of the amount determined under section 3101. However, the employee's liability is not affected by the collection from the employer of the tax liability determined under section 3509. Section 3509(d)(1)(A). Therefore, the employee remains fully liable for the tax imposed by section 3101.

HOLDING

If the employer's liability for the employee's share of FICA tax is determined under section 3509 of the Code, the employee is liable for the entire amount of the unwithheld FICA tax unreduced by any amount paid by the employer.

Section 4051—Imposition of Tax on Heavy Trucks and Trailers Sold at Retail

26 CFR 145.4051-1: Imposition of tax on heavy trucks and trailers sold at retail.

Manufacturers; trucks; gross vehicle weight; use of readily attachable components. For purposes of determination of gross weight under section 4051(a) of the Code, the term "readily attachable components" is defined as springs, brakes, rims and tires. Rev. Ruls. 85–196 and 86–43 clarified.

Rev. Rul. 86–113

Rev. Rul. 85–196, 1985–2 C.B. 205, as modified by Rev. Rul. 86–43, 1986–13 I.R.B. 36, concerns the determination of gross vehicle weight for purposes of the retailers excise tax on trucks that is imposed by section 4051(a) of the Internal Revenue Code. Rev. Rul. 85–196 provides that, for purposes of computing the gross vehicle weight of a vehicle pursuant to section 145.4051–1(e)(3) of the Temporary Excise Tax Regulations, the seller may not take into account any readily attachable components of the vehicle and gross vehicle weight must be determined solely on the basis of the strength of the chassis frame and the axle capacity and placement. Rev. Rul. 86–43 modified Rev. Rul. 85–196 to change its effective date from April 1, 1986, to October 1, 1986. In so doing, Rev. Rul. 86–43 held that, during the six-month postponement period, sellers at retail could not, by replacing a readily attachable component, lower the gross vehicle weight rating assigned to a vehicle by its manufacturer.

Under the now-repealed manufacturers excise tax on trucks imposed by former section 4061(a)(1) of the Code, the term "readily attachable components" was specifically defined in section 48.4061(a)–1(f)(3)(v) of the Manufacturer and Retailers Excise Tax Regulations as being springs, brakes, rims, and tires.

For purposes of determinations of gross vehicle weight under section 4051(a) of the Code, the term "readily attachable components" is similarly defined as springs, brakes, rims, and tires.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 85–196 and Rev. Rul. 86–43 are clarified.

Section 6011.—General Requirement of Return, Statement, or List

26 CFR 301.6011–2: Required use of magnetic media.

T.D. 8097

TITLE 26—INTERNAL REVENUE—CHAPTER 1, SUBCHAPTER F, PART 301—PROCEDURE AND ADMINISTRATION

Returns Required on Magnetic Media

AGENCY: Intenal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the required use of magnetic media for filing certain returns. The regulations extend the due date for certain requests for waiver or approval of a magnetic medium to July 31, 1986. The regulations apply to persons required to file Forms W–2 and W–2P in 1987.

EFFECTIVE DATE: The regulations are effective as of August 26, 1986, and generally apply to returns filed after December 31, 1986.

FOR FURTHER INFORMATION CONTACT: 1. Magnetic Media Reporting, Internal Revenue Service, National Computer Center, P.O. Box 1359, Martinsburg, West Virginia 25401–1359, 304–263–8700 (not a toll-free call), if the inquiry relates to the waiver procedure.

2. The following regional magnetic media coordinators of the Social Security Administration, if the inquiry relates to magnetic media filing for returns required on Form W–2 or W–2P:

SSA Regional Office	*For Persons Residing In*
Social Security Administration J.F. Kennedy Building Boston, Mass. 02203 ATTN: Joanne Shulman, Rm. 1109 617-223-4375 (not a toll-free call)	Connecticut Maine Massachusetts New Hampshire Rhode Island Vermont
Social Security Administration 26 Federal Plaza New York, New York 10007 ATTN: Anne Coe, Rm. 4012 212-264-0253 (not a toll-free call)	New Jersey New York Puerto Rico Virgin Islands
Social Security Administration P.O. Box 8788, 3535 Market Street Philadelphia, Penn. 19101 ATTN: Frank O'Brien, Rm. 8490 215-596-0474 (not a toll-free call)	Delaware District of Columbia Maryland Pennsylvania Virginia West Virginia
Social Security Administration P.O. Box 1684, 101 Marietta Tower Atlanta, Ga. 30301 ATTN: Pat McCarron, Suite 1804 404-221-2587 (not a toll-free call)	Alabama Florida Georgia Kentucky Mississippi North Carolina South Carolina Tennessee
Social Security Administration 300 South Wacker Drive Chicago, Illinois 60606 ATTN: Jim Juntunen, 32nd Floor 312-353-6717 (not a toll-free call)	Illinois Indiana Michigan Minnesota Ohio Wisconsin

Social Security Administration 1200 Main Tower, Room 1535 Dallas, Texas 75202 ATTN: Pat Insko 214-767-4311 (not a toll-free call)	Arkansas Louisiana New Mexico Oklahoma Texas
Social Security Administration 601 East 12th Street Kansas City, Mo. 64106 ATTN: Dale Fick, 4th Floor East 816-374-2095 (not a toll-free call)	Iowa Kansas Missouri Nebraska
Social Security Administration Federal Office Building 1961 Stout Street Denver, Col. 80294 ATTN: Rick Schremp, Rm. 1194 303-837-2364 (not a toll-free call)	Colorado Montana North Dakota South Dakota Utah Wyoming
Social Security Administration 100 Van Ness Avenue San Francisco, Cal. 94102 ATTN: Bill Brees, Systems Branch 415-556-4788 (not a toll-free call)	American Samoa Arizona California Guam Hawaii Nevada
Social Security Administration 2901 Third Avenue Seattle, Wash. 98121 ATTN: Jan Hotson, M/S 302 206-442-0468 (not a toll-free call)	Alaska Idaho Oregon Washington

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SUPPLEMENTARY INFORMATION: BACKGROUND

On March 25, 1986, the FEDERAL REGISTER published final regulations relating to section 6011 (e) of the Internal Revenue Code of 1954 (51 FR 10348) [T.D. 8081, 1986–17 I.R.B. 17]. The regulations were adopted to reflect the addition to the Code of section 6011 (e) by section 319 of the Tax Equity and Fiscal Responsibility Act of 1982 (Pub. L. 97–248, 96 Stat. 610) and its amendment by section 109 of the Interest and Dividend Tax Compliance Act of 1983 (Pub. L. 98–67, 97 Stat. 383).

Under those regulations, any person that is required to use certain forms, including Form W–2 (Wage and Tax Statement) or W–2P (Statement for Recipients of Annuities, Pensions, Retired Pay, or IRA Payments), for the purpose of making a return must provide the information required by such form on magnetic media, unless (a) the person is a low-volume filer with respect to the return or (b) the person is granted a waiver with respect to the return by the Internal Revenue Service. Failure to file a return on magnetic media when required to do so by the regulations is treated as a failure to file the return and may subject the person to the corresponding penalty.

Returns required on Form W–2 or W–2P for calendar year 1986 may generally be filed on the prescribed paper form if fewer than 500 returns were required to be filed on that form for the preceding calendar year. Returns required on such forms for calendar years after 1986 may generally be filed on the prescribed paper form if fewer than 250 returns were required to be filed on that form for the preceding calendar year. The regulations also provide that a person required to file a return on magnetic media may receive a waiver from such requirement in appropriate circumstances upon a showing of hardship.

In addition, under the regulations, persons subject to the magnetic media requirement are required to obtain prior consent to the use of the magnetic medium on which the information is to be submitted. The regulations provide that applications for consent to the use of a magnetic medium and requests for waiver generally must be filed at least 90 days before the filing of the first return for which the consent or waiver is requested. In the case of returns on Forms W–2 and W–2P filed in 1987 and 1988, however, the application for consent or request for waiver is due no later than June 30 of the preceding year. The regulations contained in this document extend the due date for applications for consent and requests for waivers to July 31, 1986, for Forms W–2 and W–2P to be filed in 1987.

EXECUTIVE ORDER 12291, REGULATORY FLEXIBILITY ACT AND PAPERWORK REDUCTION ACT

The Commissioner of Internal Revenue has determined that this rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis therefore is not required. A general notice of proposed rulemaking is not required by 5 U.S.C. 553 for final regulations subject to 5 U.S.C. 553(b)(B). Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is C. Scott McLeod of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

LIST OF SUBJECTS IN 26 CFR 301

Administrative practice and procedure, Bankruptcy, Courts, Crime, Employment taxes, Estate taxes, Excise taxes, Gift taxes, Income taxes, Investigations, Law enforcement, Penalties, Pensions, Statistics, Taxes, Disclosure of information, Filing requirements.

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 301 is amended as follows:

PROCEDURE AND ADMINISTRATION REGULATIONS

(26 CFR Part 301)

Paragraph 1. The authority citation for section 301.6601–2 continues to read as follows:

Authority: 26 U.S.C. 7805. * * * Section 301.6601–2 also issued under 26 U.S.C. 6011(e).

Par. 2. Section 301.6011–2 is amended as follows:

1. Paragraph(b)(2)(i) is amended by removing "June 30, 1986" and by adding in its place "July 31, 1986."

2. Paragraph(c)(4)(i)(A) is amended by removing "June 30, 1986" and by adding in its place "July 31, 1986."

This Treasury decision merely extends the due date for certain requests for waiver or approval of a magnetic medium. For this reason, it is found unnecessary to issue this Treasury decision with notice and public procedure under subsection (b) of section 553 of title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

JAMES I. OWENS,
Acting Commissioner
of Internal Revenue.

Approved AUGUST 11, 1986.

J. ROGER MENTZ,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on August 25, 1986, 8:45 a.m., and published in the issue of the Federal Register for August 26, 1986, 51 F.R. 30351)

Section 6401.—Amounts Treated as Overpayments

Ct. D. 2034

SUPREME COURT
OF THE
UNITED STATES
No. 84–1686

Sorenson v. Secretary of the Treasury
et al.
[U.S.]
On Writ of Certiorari to the
United States
Court of Appeals
For the Ninth Circuit

[January 15, 1986]

Syllabus

The Internal Revenue Code (IRC) allows an individual responsible for the support of a child living with him a credit against income taxes due equal to a certain percentage of so much of earned income as does not exceed a specified amount. If the credit exceeds tax liability, the excess is considered "an overpayment" of tax under IRC §6401(b). Section 6402(a) provides for a refund of "any overpayment" to the person who made it. Section 6402(c) requires the amount of "any overpayment" to be reduced by the amount of any past-due child-support payments assigned to a State. Section 464 of the Social Security Act (SSA) directs the Secretary of the Treasury to "intercept" tax refunds payable to persons who have failed to meet child-support obligations that have been assigned to a State. When petitioner's husband fell behind in support payments for a child of a previous marriage who was in the custody of his former wife, the latter, upon applying for welfare benefits from the State of Washington, assigned to the State, as required by the Aid to Families with Dependent Children program, her right to collect the unpaid child-support payments. Petitioner and her husband filed a joint federal income tax return for 1981 in which all income was attributable to petitioner's wages and unemployment compensation benefits and in which they anticipated a refund based in part on an earned-income credit. The Internal Revenue Service, however, notified them that a certain amount of the anticipated refund was being retained, under the authority of the tax-intercept law, and would be paid over to the State of Washington. Petitioner then filed a class action in Federal District Court, seeking a declaration that §464 of the SSA did not reach a refund attributable to an excess earned-income credit. The District Court granted summary judgment for the Government, and the Court of Appeals affirmed.

Held: An excess earned-income credit can properly be intercepted under the applicable statutes. Pp. 7–14.

(a) The IRC's treatment of earned-income credits supports the Government's position. The refundability of that credit is inseparable from its classification as an overpayment of tax. It is an "overpayment" for purposes not only of §6402(a), but also for purposes of §6402(c). Eligibility for an earned-income credit does not depend upon an individual's actually having paid any tax. The IRC's classification of the credit as an "overpayment" to be refunded is similarly independent of the individual's actually having made any payment. To the extent an excess credit is "payable" to an individual, it is payable as if it were a refund of tax paid. Pp. 7–12.

(b) There is no support for petitioner's claim that Congress did not intend the tax-intercept to reach excess earned-income credits. Although Congress never mentioned the earned-income credit in enacting the Omnibus Budget Reconciliation Act of 1981, which added §6402(c) to the IRC, it must have been aware, when it provided in §6402(c) that "*any* overpayment" to be refunded shall be reduced by the amount of any past-due child support, that this would include refunds attributable to excess earned-income credits. And, although the goals of the earned-income credit—to reduce the disincentive to work caused by social security taxes on earned income, to stimulate the economy by funneling funds to persons likely to spend the money immediately, and to provide for relief for low-income families hurt by rising food and energy prices—are important, it cannot be said that Congress concluded that they outweigh the goals served by the subsequently enacted tax-intercept program—securing child support from absent parents and reducing the number of families on welfare. Pp. 12–14.

752 F.2d 1433, affirmed.

BLACKMUN, J., delivered the opinion of the Court, in which BURGER, C. J., and BRENNAN, WHITE, MARSHALL, POWELL, REHNQUIST, and O'CONNOR, JJ., joined. STEVENS, J., filed a dissenting opinion.

JUSTICE BLACKMUN delivered the opinion of the Court.

The Internal Revenue Code and the Social Security Act direct the Secretary of the Treasury to "intercept" certain tax refunds payable to persons who have failed to meet child-support obligations. In this case, the United States Court of Appeals for the Ninth Circuit ruled that payments involving earned-income credits could be intercepted. 752 F.2d 1433 (1985). We granted certiorari, 472 U.S. —— (1985), because this ruling was in conflict with decisions of the Courts of Appeals for the Second and Tenth Circuits. See *Rucker* v. *Secretary of the Treasury,* 751 F. 2d 351 (CA10 1984); *Nelson* v. *Regan,* 731 F. 2d 105 (CA2), cert. denied *sub nom. Manning* v. *Nelson,* 469 U. S. —— (1984).

I

A

Stanley Sorenson, the husband of petitioner Marie Sorenson, was legally obligated to make child-support payments for a child of his previous marriage who was in the custody of his former wife. Mr. Sorenson was unemployed because of a disability and fell behind on those support payments. His former wife applied for welfare benefits from the State of Washington. Since 1975, the program for Aid to Families with Dependent Children (AFDC) has required, as a condition of eligibility, that applicants for welfare assign to the State concerned any right to child-support payments that has accrued at the time of assignment. Pub. L. 93–647, §101(c)(5)(C), 88 Stat. 2359, 42 U.S.C. §602(a)(26)(A).[1] Thus, Stanley Sorenson's former wife turned over to the State her right to collect the payments Mr. Sorenson had failed to make.

Stanley and Marie Sorenson also had their own dependent child living with them. They thus were potentially eligible to receive an earned-income credit. For the calendar year 1981, the time relevant to this lawsuit, §43 of the Internal Revenue Code of 1954, as amended, provided that an individual responsible for the support of a child living with him was allowed "as a credit against the tax imposed . . . for the taxable year an amount equal to 10 percent of so much of the earned income for the taxable year as does not exceed $5,000." As the amount of the taxpayer's earned income increased, the amount of the credit decreased, reaching zero when the taxpayer's adjusted gross income reached $10,000.[2]

Unlike certain other credits, which can be used only to offset tax that would otherwise be owed, the earned-income credit is "refundable." Thus, if an individual's earned-income credit exceeds his tax liability, the excess amount is "considered an overpayment" of tax under §6401(b), as it then read, of the 1954 Code.[3] Subject to specified setoffs, §6402(a) directs the Secretary to credit or refund "any overpayment" to the person who made it.[4] An individual who is entitled to an earned-income credit that exceeds the amount of tax he owes thereby receives the difference as if he had overpaid his tax in that amount.

B

In February 1982, petitioner and her husband timely filed a joint federal income tax return for the calendar year 1981. Petitioner had worked during part of that year, and all the Sorenson family income for the year was attributable to her wages and unemployment compensation benefits. By the return so filed, the Sorensons anticipated a refund of $1408.90, consisting in part of excess withholding on petitioner's wages and in part of an earned-income credit. The Internal Revenue Service, however, notified the Sorensons that $1,132 of the anticipated refund was being retained, under the authority granted it by the tax-intercept law, and would be paid over to the State of Washington because that State had been assigned the right to collect Mr. Sorenson's unpaid child-support obligations. See Second Declaration of Peter Greenfield, Exh. B, *Sorenson* v. *Secretary of the Treasury*, No. C82–441C (WD Wash.).

The tax-intercept law essentially directs the Secretary to give priority to a State's claim for recoupment of welfare payments made to a family who failed to receive child support, see §402(a)(26)(A) of the Social Security Act, as amended, 42 U.S.C. §602(a)(26)(A), over an individual's claim for refund of tax overpayment. See §6402(a), as amended, of the 1954 Code. The intercept law originally was enacted as part of the Omnibus Budget Reconciliation Act of 1981 (OBRA), Pub. L. 97–35, §2331, 95 Stat. 860. First, OBRA §2331(a) added §464 to the Social Security Act, 42 U.S.C. §664. That section directs the Secretaries of the Treasury and of Health and Human Services to establish a scheme by which a State is to notify the Secretary of the Treasury of persons who owe past-due child-support payments that have been assigned to it, and directs the Secretary of the Treasury to intercept tax-refund payments that would otherwise be paid to those persons:

> "Upon receiving notice from a State agency administering [an AFDC plan] . . . that a named individual owes past-due support which has been assigned to such State pursuant to section 402(a)(26), the Secretary of the Treasury shall determine whether any amounts, as refunds of Federal taxes paid, are payable to such individual (regardless of whether such individual filed a tax return as a married or unmarried individual). If the Secretary of the Treasury finds that any such amount is payable, he shall withhold from such refunds an amount equal to the past-due support, and pay such amount to the State agency (together with notice of the individual's home address) for distribution in accordance with section 457(b)(3)." §464(a), 42 U.S.C. §664(a).[5]

Section §2331(c) of OBRA amended the Internal Revenue Code. It added a new subsection to the provision governing the Secretary of the Treasury's authority to refund overpayments to taxpayers. The new subsection, §6402(c), requires the Secretary to withhold from the refund otherwise due the taxpayer the amount owed the State in past-due child support and to remit the amount withheld to the State:

> "The amount of any overpayment to be refunded to the person making the overpayment shall be reduced by the

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[1] Section 402(a)(26)(A) of the Social Security Act, as amended, 42 U.S.C. §602(a)(26)(A), requires the assignment to the State of "any rights to support from any other person such applicant may have (i) in his own behalf or in behalf of any other family member for whom the applicant is applying for or receiving aid, and (ii) which have accrued at the times such assignment is executed."

[2] By the Tax Reform Act of 1984, Pub. L. 98–369, §471(c)(1), 98 Stat. 826, Congress redesignated §43 as §32. By §1042 of that Act, 98 Stat. 1043, it raised the earned-income percentage from 10 to 11 percent, the maximum amount of the credit from $500 to $550, and the eligibility ceiling from $10,000 to $11,000.

[3] At the time relevant to this lawsuit, §6401(b) of the 1954 Code provided, in pertinent part:

> "If the amount allowable as credits under section 31 (relating to tax withheld on wages), and 39 (relating to certain uses of gasoline, special fuels, and lubricating oil), and 43 (relating to earned income credit), exceeds the tax imposed by subtitle A (reduced by the credits allowable under subpart A of part IV of subchapter A of chapter 1, other than the credits allowable under sections 31, 39, and 43), the amount of such excess shall be considered an overpayment."

Section 6401(b) was amended by the Tax Reform Act of 1984. section 474(r)(36) of that Act, 98 Stat. 846, designated existing §6401(b) as §6401(b)(1) and substituted the following language for the language quoted above:

> "If the amount allowable as credits under subpart C of part IV of subchapter A of chapter 1 (relating to refundable credits) exceeds the tax imposed by subtitle A (reduced by the credits allowable under subparts A, B, and D of such part IV), the amount of such excess shall be considered an overpayment."

The earned-income credit remains refundable under the revised provision, since it is within the category of "refundable credits." See Tax Reform Act of 1984, §471, 98 Stat. 825.

[4] The version of §6402(a) in effect for the tax year 1981 provided:

> "In the case of any overpayment, the Secretary, within the applicable period of limitations, may credit the amount of such overpayment, including any interest allowed thereon, against any liability in respect of an internal revenue tax on the part of the person who made the overpayment and shall, subject to subsection (c), refund any balance to such person."

The question presented by this case is the scope of subsection (c)—the provision governing the offset of past-due child-support payments.

Section 2653(b)(2) of the Spending Reduction Act of 1984, 98 Stat. 1155, amended §6402(a). Under amended §6402(a), the Secretary's authority, with respect to refunds payable after Dec. 31, 1985, and before Jan. 1, 1988, see §2653(c) of the 1984 Act, 98 Stat. 1156, is restricted by a new subsection (d) as well as by subsection (c) of §6402. Section 2653(b)(1) of the 1984 Act, 98 Stat. 1154, added the new subsection (d). Section 6402(d) requires the offset of debts owed to various federal agencies. Under §6402(d)(2), the collection of past-due child-support payments pursuant to §6402(c) has priority over the collection of debts covered by §6402(d).

> amount of any past-due support (as defined in section 464(c) of the Social Security Act) owed by that person of which the Secretary has been notified by a State in accordance with section 464 of the Social Security Act. The Secretary shall remit the amount by which the overpayment is so reduced to the State to which such support has been assigned and notify the person making the overpayment that so much of the overpayment as was necessary to satisfy his obligation for past-due support has been paid to the State. This subsection shall be applied to an overpayment prior to its being credited to a person's future liability for an internal revenue tax."

C

After negotiations concerning the status of tax refunds in community property States such as Washington—issues that are not germane to the question now presented to this Court—the Secretary ultimately withheld only half of the refund increment the Sorensons claimed. Petitioner then filed a class action in the United States District Court for the Western District of Washington seeking, among other things, a declaration that §464 of the Social Security Act did not reach a refund attributable to an excess earned-income credit. The District Court rejected the Secretary's jurisdictional arguments, which were renewed on appeal to the Court of Appeals but which are not pressed in this Court. See Brief for Respondents 5, n. 1. But it agreed with the Secretary's arguments on the merits and granted summary judgment for the Government. 557 F. Supp. 729 (1982).

The Court of Appeals affirmed that judgment. 752 F.2d 1433 (CA9 1985). It rejected petitioner's statutory construction arguments, and held that, since the Code expressly defined excess earned-income credits as "overpayments," and disbursed those excess credits to recipients through the income tax refund process, the credits were "payable '*as*' refunds of federal taxes paid" and therefore could be intercepted. *Id.*, at 1441 (emphasis in original). Congress used the broad terms "any amounts" and "any overpayment" in the tax-intercept law and gave no indication that it intended to exclude earned-income credit payments from these terms.

The Court of Appeals also rejected petitioner's argument that the Secretary's position conflicted with Congress' intention to provide benefits to the poor through the earned-income credit. First, the legislative history of §43 did not suggest that the earned-income credit was intended primarily as a type of welfare grant; rather, it was meant to negate the disincentive to work caused by social security taxes. Since the earned-income credit was payable as a lump sum, it was more like excess withholding, which was clearly reachable by the intercept program, than it was like wages, a portion of which Congress exempted from the assessment and collection process. See 752 F.2d, at 1443, n. 1. Second, had Congress intended to exempt earned-income credit payments from the intercept program, it could have done so expressly. Instead, it provided that any amount payable through the federal tax-refund process might be intercepted. "In the face of this rather clear statutory mandate," said the Court of Appeals, "we conclude that we are not free to speculate that Congress intended otherwise." *Id.*, at 1443.

II

Petitioner advances two arguments to support her claim that an excess earned-income credit cannot be intercepted. First, she claims that the language and structure of the interlocking statutory provisions that make up the intercept law exclude an earned-income credit from its reach: excess earned-income credits are neither "overpayments" nor "refunds of Federal taxes paid," and only those items are subject to interception. Second, she claims that permitting interception of an earned-income credit would frustrate Congress' aims in providing the credit, and thus that Congress could not have intended the intercept law to reach earned-income credits. We find neither argument persuasive.

A

The Internal Revenue Code's treatment of earned-income credits supports the Government's position. An individual can receive the amount by which his entitlement to an earned-income credit exceeds his tax liability only because §6401(b) of the Code defines that amount as an "overpayment," and §6402 provides a mechanism for disbursing overpayments, namely, the income tax refund process. The refundability of the earned-income credit is thus inseparable from its classification as an overpayment of tax. Petitioner therefore acknowledges that the excess earned-income credit is an "overpayment" for purposes of §6402(a), the general provision that authorizes all tax refunds. See n. 4, *supra*. If it were not, the Secretary would lack authorization for refunding it to her. She claims, however, that while an excess earned-income credit is an "overpayment" for purposes of §6402(a), it is not an "overpayment" for purposes of §6402(c), which requires that the "amount of any overpayment . . . shall be reduced by the amount of any past-due support" assigned to the State.

The normal rule of statutory construction assumes that " 'identical words used in different parts of the same act are intended to have the same meaning.' " *Helvering* v. *Stockholms Enskilda Bank*, 293 U.S. 84, 87 (1934), quoting *Atlantic Cleaners & Dyers* v. *United States*, 286 U.S. 427, 433 (1932). That the Internal Revenue Code includes an explicit definition of "overpayment" in the same subchapter strengthens the presumption. And that both subsections concern the tax-refund treatment of "overpayment[s]" is especially damaging to any claim "that the words, though in the same act, are found in such dissimilar connections as to warrant the conclusion that they were employed in the different parts of the act with different intent." *Stockholms Enskilda Bank*, 293 U.S., at 87.

Petitioner and the two Courts of Appeals that have excluded excess earned-income credits from the definition of "overpayment" used in §6402(c) offer two bases for their position. First, they believe that §6402(c) limits §6401(b)'s broad definition "by [using] the phrase 'overpayment to be refunded to the person making the overpayment.' " *Nelson* v. *Regan*, 731 F.2d, at 111; see *Rucker* v. *Secretary of the Treasury*, 751 F.2d, at 356. Not all overpayments, they suggest, are refunded to persons who "made" them, since some—those consisting of earned-income credits—may be refunded to persons who actually have not paid any tax. We disagree. *All* refunds made by the Secretary under §6402(a) are paid to "the person who made the overpayment." The phrase merely identifies the *person* entitled to the refund; it does not restrict the nature of

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[5] Section 464(a) was amended by the Child Support Enforcement Amendments of 1984, Pub. L. 98–378, §21.98 Stat. 1322, which authorized the interception and diversion of refunds for the benefit of non-AFDC children as well as children receiving AFDC benefits. The Amendments also provided additional procedural protections for refund claimants whose refunds are intercepted.

the refund itself. Petitioner must characterize herself as a person who has "made" an overpayment; otherwise, she cannot claim her excess earned-income credit. The phrase in §6402(c) on which petitioner and the Second and Tenth Circuits relied is virtually identical to the phrase used in §6402(a). Since the words cannot have the limiting effect petitioner proposes when used in §6402(a), no justification exists for giving them such a construction in §6402(c).

Second, petitioner and the Second and Tenth Circuits perceive a tension between §6401(b) and §6402(a)'s treatment of excess earned-income credits and §464(a)'s treatment of interceptable amounts. As used in those Code sections, "overpayment" includes more than "refunds of Federal taxes paid," the phrase used in the Social Security Act. Since §464 and §6402(c) were enacted simultaneously as part of OBRA, petitioner and the two Circuits believe that §6402(c) should be harmonized with §464 rather than with §6401(b) and 6402(a). See *Rucker* v. *Secretary of the Treasury*, 751 F.2d, at 357; *Nelson* v. *Regan*, 731 F.2d., at 111.

This second argument, it seems to us, misperceives the structure of the tax-intercept law, and manufactures a tension that need not exist. OBRA's placement of provisions regarding interception in both Acts reflects a division of functions. The tax-intercept program lies at the intersection of the Social Security Act's concern in subchapter IV, part D, with child support, and the Internal Revenue Code's concern in chapter 65, subchapter A with the treatment of credits in the tax-refund process. Section 464 addresses the concerns of the States that have received AFDC-related grants. It defines past-due child support, authorizes procedures by which the States can notify the Secretary of the Treasury of their entitlement to recover such past-due support, and directs the Secretary to aid the States, through his control over the tax-refund process, in recouping that support. Sections 6401 and 6402 addresses the operation of the tax-refund process under the Internal Revenue Code. They define the status of certain tax credits, set up a mechanism for disbursing refunds, and direct the Secretary to divert certain amounts from the refund process. To the extent that the tax-intercept law regulates the relationship of the Secretary of Treasury to refund claimants, it does so through §6402, and not through a provision that governs the Secretary's relationship to State agencies.

Petitioner, however, views §6402(c)'s reference to §464 as indicating that §464(a) is meant to be read into §6402(c) as a limitation on the Secretary's intercept powers. This argument depends on a somewhat strained construction of §6402(c)'s statement that "[t]he amount of any overpayment to be refunded to the person making the overpayment shall be reduced by the amount of any past-due support . . . owed by that person of which the Secretary has been notified by a State in accordance with section 464 of the Social Security Act." Petitioner claims that "[t]he words 'in accordance with section 464 of the Social Security Act' . . . do not modify 'has been notified by a State,' as one might initially assume. Rather they belatedly modify the words 'shall be reduced.'" Brief for Petitioner 18. In petitioner's view, her construction would lead to the conclusion that a refund can be reduced only to the extent that the refund represents a refund of tax actually paid, since that is all §464(a) permits.

We disagree with both petitioner's construction of §6402(c) and her reading of §464(a). First, it seems far more plausible that the words modify the nearest verb. If they are given this more natural reading, then §6402(c) directs the Secretary to intercept only that amount which properly is classified as past-due support and of which he properly has been notified.

But even if the reference in §6402(c) to §464 were read to refer solely to §464(a),[6] nothing in that subsection exempts excess earned-income credits from interception. Petitioner and the Second and Tenth Circuits recast their argument regarding the meaning of "overpayment" by contending that the amount of refund that is attributable to an excess earned-income credit is not a "refun[d] of Federal taxes paid," and that §464(a) permits interception of only "amounts, as refunds of Federal taxes paid":

> "A refund of federal taxes is a repayment of money paid by a taxpayer in excess of that taxpayer's liability. Although the earned income credit is given effect through the income tax return, the credit is not a tax refund because eligibility for the credit is not contingent upon payment of any federal income tax." *Rucker* v. *Secretary of the Treasury*, 751 F. 2d, at 356.

But just as eligibility for an earned-income credit does not depend upon an individual's actually having paid any tax, the Code's classification of the credit as an "overpayment" to be refunded by similarly independent of the individual's actually having made any payment. Cf. I.R.C. §6401(c). The Ninth Circuit correctly held that, to the extent an excess earned-income credit is "payable" to an individual, it is payable *as if* it were a refund of tax paid. 752 F. 2d, at 1441. Section 464(a)'s reference to the tax-refund process is best understood as a directive to the Secretary that he follow the procedures established by the Internal Revenue Code for calculating and disbursing refunds, rather than as an attempt implicitly to redefine terms given special meaning by the Code.

B

Nor do we agree with petitioner's claim that Congress did not intend the intercept program to reach excess earned-income credits. Petitioner and the Government agree that Congress never mentioned the earned-income credit in enacting OBRA. See Brief for Petitioner 24; Tr. of Oral Arg. 21. But it defies belief that Congress was unaware, when it provided in §6402(c) that "*any* overpayment to be refunded . . . shall be reduced by the amount of any past-due support" (emphasis added), that this would include refunds attributable to excess earned-income credits. Congress had previously expressly defined an excess earned-income credit as an "overpayment," in §6401(b) of the Internal Revenue Code—the section immediately preceding the section to which Congress added the intercept provision.[7]

What petitioner and the Second and Tenth Circuits are really claiming is that the intercept law should be read narrowly to avoid frustrating the goals of the earned-income credit program. The earned-income credit was enacted to reduce the disincentive to work caused by the imposition of social security taxes on earned income (welfare payments are not similarly taxed), to stimulate the economy by funneling funds to persons likely to spend the money immediately, and to provide relief for low-income families hurt by rising food and energy prices.[8] Each is an undeniably important objective. It is impossible, however, for us to say that these goals outweigh the goals served by the subsequently enacted tax-intercept program—securing child support from absent parents whenever possible and reducing the number of families on welfare.[9] Congress of course could conclude that families eligible for earned-income credits have a more compelling claim to the funds involved than do either the States or non-AFDC families. But it is equally clear that Congress could have decided that the more pressing need was to alleviate the "devasting consequences for children and the taxpayers" of the epidemic of nonsupport. See Hearings before the Senate Committee on Finance on Spending Reduction Proposals, 97th Cong., 1st Sess., pt. 1, p. 34 (1981) (statement of Secretary Schweiker).[10]

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[6] In light of Congress' specific reference to §646(c) earlier is §6402(c), it seems particularly likely that Congress would have referred subsection (a) of §464 expressly had it meant "in accordance with §464(a)" rather than in accordance with the entire scheme for identifying past-due support payments and notifying the Federal Government of such obligations set out in §464.

The ordering of competing social policies is a quintessentially legislative function. In light of Congress' decision to direct the interception of *any* overpayment otherwise refundable to a taxpayer, the Ninth Circuit correctly refused to "speculate that Congress intended otherwise." 752 F. 2d, at 1443. Its judgment, accordingly, is affirmed.

It is so ordered.

Section 7701.—Definitions

26 CFR 301.7701-2: Associations.

Limited partnerships. The states of Kansas, New Jersey, and Ohio are added to the list of states that have enacted legislation that corresponds to the Uniform Limited Partnership Act for purposes of section 301.7701-2 of the regulations. Rev. Rul. 84-80 amplified.

Rev. Rul. 86-112

In Rev. Rul. 84-80, 1984-1 C.B. 275, Rev. Rul. 84-180, 1984-2 C.B. 314, Rev. Rul. 85-178, 1985-2 C.B. 338, and Rev. Rul. 86-30, 1986-8 I.R.B. 23, the Internal Revenue Service listed several states that revised their limited partnership statutes following the promulgation of the Revised Uniform Limited Partnership Act. The Service determined that the legislation enacted by those states corresponds to the Uniform Limited Partnership Act ("ULPA") for purposes of section 301.7701-2 of the Procedure and Administration Regulations.

The Service has determined that the following additional states have enacted legislation that, as of the effective date, corresponds to ULPA for purposes of section 301.7701-2 of the regulations:

KANSAS: Kan. Stat. Ann. sections 56-1a101 through 56-1a601 (1983) effective January 1, 1984.

NEW JERSEY: N.J. State. Ann. sections 42:2A-1 through 42:2A-1 through 42:2A-72 (West Supp. 1985) effective January 1, 1985.

OHIO: Ohio Rev. Code Ann. sections 1782.01 through 1782.62 (Page Supp. 1984) effective April 1, 1985.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 84-80 is amplified.

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[7] That Congress could not have viewed the earned-income credit as immune from seizure to satisfy child-support obligations is suggested by a number of other factors as well. As the Government notes, once an individual has actually received his tax-refund payment, the proceeds of that refund, even if they reflect an earned-income credit component, are subject to levy under §6305 of the Code. The fact that the Government may not have used this cumbersome procedure, see Tr. of Oral Arg. 23-25, reflects the economic inefficiency of locating and pursuing a payment that cannot exceed $550 rather than a lack of authority to do so. And certainly no one has suggested that the former spouse to whom a support obligation not assigned to the State is owed would be precluded from employing the judicial process to attach and seize the credit once the recipient had received it.

[8] See, *e.g.*, S. Rep. No. 94-36, pp. 11, 33 (1975); H. R. Rep. No. 94-19, pp. 3-4, 29-31 (1975); Hearings on H. R. 2166 before the Senate Committee on Finance, 94th Cong., 1st Sess., pp. 66, 315 (1975); Hearings before the House Committee on Ways and Means on the President's Authority to Adjust Imports of Petroleum; Public Debt Ceiling Increase; and Emergency Tax Proposals, 94th Cong., 1st Sess., pp. 661, 742-743, 797 (1975); 104 Cong. Rec. 4609 (1975).

[9] See, *e.g.*, S. Rep. No. 98-387, pp. 5-8 (1984); Hearings before the Senate Committee on Finance on Spending Reduction Proposals, 97th Cong., 1st Sess., pt. 1, pp. 19, 34-35, 81, 312 (1981); Hearings before the House Committee on Ways and Means on Tax Aspects of the President's Economic Program, 97th Cong., 1st Sess., pt. 1, pp. 159, 237 (1981).

[10] Even if Congress' sole concern were providing funds to the neediest children involved, it is far from certain that all children living in households receiving refunds of earned-income credits are needier than all children owed past-due child support. When the earned-income credit is claimed at the end of the tax year (an individual can, pursuant to §3507 of the Code, receive an advance on his earned-income credit over the course of the year), it may in fact go to a recipient who is not currently needy. For example, an individual, with a dependent child, who was unemployed during most of 1981 and therefore earned only $5000, but found a job paying $20,000 per year on January 1, 1982, would have been able to claim in a tax return filed in April 1982 an earned-income credit of $500, despite the fact that, in late spring 1982, when the refund check ultimately arrived, the individual might no longer be needy.

PART II. Treaties and Tax Legislation

Subpart A—Tax Conventions

UNITED STATES—CANADA INCOME TAX CONVENTION[1]

Convention signed at Washington, D.C. on September 26, 1980;

Protocol signed at Ottawa June 14, 1983;

Protocol signed at Washington, D.C., March 28, 1984;

Ratification advised by the Senate of the United States of America on June 28, 1984;

Entered into force August 16, 1984.

CONVENTION BETWEEN THE UNITED STATES OF AMERICA AND CANADA WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL

The United States of America and Canada,

Desiring to conclude a Convention for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital,

Have agreed as follows:

ARTICLE I

Personal scope

This Convention is generally applicable to persons who are residents of one or both of the Contracting States.

ARTICLE II

Taxes covered

1. This Convention shall apply to taxes on income and on capital imposed on behalf of each Contracting State, irrespective of the manner in which they are levied.

2. The existing taxes to which the Convention shall apply are:

(a) In the case of Canada, the taxes imposed by the Government of Canada under Parts I, XIII and XIV of the Income Tax Act; and

(b) In the case of the United States, the Federal income taxes imposed by the Internal Revenue Code.

3. The Convention shall apply also to:

(a) Any identical or substantially similar taxes on income; and

(b) Taxes on capital, which are imposed after the date of signature of the Convention in addition to, or in place of, the existing taxes.

4. Notwithstanding the provisions of paragraphs 2(b) and 3, the Convention shall apply to:

(a) The United States accumulated earnings tax and personal holding company tax, to the extent, and only to the extent, necessary to implement the provisions of paragraphs 5 and 8 of Article X (Dividends);

(b) The United States excise taxes imposed with respect to private foundations, to the extent, and only to the extent, necessary to implement the provisions of paragraph 4 of Article XXI (Exempt Organizations); and

(c) The United States social security taxes, to the extent, and only to the extent, necessary to implement the provisions of paragraph 4 of Article XXIX (Miscellaneous Rules).

ARTICLE III

General definitions

1. For the purposes of this Convention, unless the context otherwise requires:

(a) When used in a geographical sense, the term "Canada" means the territory of Canada, including any area beyond the territorial seas of Canada which, in accordance with international law and the laws of Canada, is an area within which Canada may exercise rights with respect to the seabed and subsoil and their natural resources;

(b) The term "United States" means:

(i) The United States of America, but does not include Puerto Rico, the Virgin Islands, Guam or any other United States possession or territory; and

(ii) When used in a geographical sense, such term also includes any area beyond the territorial seas of the United States which, in accordance with international law and the laws of the United States, is an area within which the United States may exercise rights with respect to the seabed and subsoil and their natural resources;

(c) The term "Canadian tax" means the Canadian taxes referred to in paragraphs 2(a) and 3(a) of Article II (Taxes Covered);

(d) The term "United States tax" means the United States taxes referred to in paragraphs 2(b) and 3(a) of Article II (Taxes Covered);

(e) The term "person" includes an individual, an estate, a trust, a company and any other body of persons;

(f) The term "company" means any body corporate or any entity which is treated as a body corporate for tax purposes;

(g) The term "competent authority" means:

(i) In the case of Canada, the Minister of National Revenue or his authorized representative; and

(ii) In the case of the United States, the Secretary of the Treasury or his delegate;

(h) The term "international traffic" means any voyage of a ship or aircraft to transport passengers or property except where the principal purpose of the voyage is to transport passengers or property between places within a Contracting State;

(i) The term "State" means any national State, whether or not a Contracting State; and

(j) The term "the 1942 Convention" means the Convention and Protocol between the United States and Canada for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion in the case of Income Taxes signed at Washington on March 4, 1942, as amended by the Convention signed at Ottawa on June 12, 1950, by the Convention signed at Ottawa on August 8, 1956 and by the Supplementary Convention signed at Washington on October 25, 1966.

2. As regards the application of the Convention by a Contracting State any term not defined therein shall, unless the context otherwise requires and subject to the provisions of Article XXVI (Mutual Agreement Procedures), have the meaning which it has under the law of that State concerning the taxes to which the Convention applies.

ARTICLE IV

Residence

1. For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the

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[1] Protocol, page 25, Second Protocol, page 29, Treasury Department Technical Explanation, page 29.

laws of that State, is liable to tax therein by reason of his domicile, residence, place of management, place of incorporation or any other criterion of a similar nature, but in the case of an estate or trust, only to the extent that income derived by such estate or trust is liable to tax in that State, either in its hands or in the hands of its beneficiaries.

2. Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows:

(a) He shall be deemed to be a resident of the Contracting State in which he has a permanent home available to him; if he has a permanent home available to him in both States or in neither State, he shall be deemed to be a resident of the Contracting State with which his personal and economic relations are closer (centre of vital interests);

(b) If the Contracting State in which he has his centre of vital interests cannot be determined, he shall be deemed to be a resident of the Contracting State in which he has an habitual abode;

(c) If he has an habitual abode in both States or in neither State, he shall be deemed to be a resident of the Contracting State of which he is a citizen; and

(d) If he is a citizen of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

3. Where by reason of the provisions of paragraph 1 a company is a resident of both Contracting States, then if it was created under the laws in force in a Contracting State, it shall be deemed to be a resident of that State.

4. Where by reason of the provisions of paragraph 1 an estate, trust or other person (other than an individual or a company) is a resident of both Contracting States, the competent authorities of the States shall by mutual agreement endeavor to settle the question and to determine the mode of application of the Convention to such person.

5. Notwithstanding the provisions of the preceding paragraphs, an individual shall be deemed to be a resident of a Contracting State if:

(a) The individual is an employee of that State or of a political subdivision, local authority or instrumentality thereof rendering services in the discharge of functions of a governmental nature in the other Contracting State or in a third State; and

(b) The individual is subjected in the first-mentioned State to similar obligations in respect of taxes on income as are residents of the first-mentioned State.

The spouse and dependent children residing with such an individual and meeting the requirements of subparagraph (b) above shall also be deemed to be residents of the first-mentioned State.

ARTICLE V

Permanent establishment

1. For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of a resident of a Contracting State is wholly or partly carried on.

2. The term "permanent establishment" shall include especially:

(a) A place of management;
(b) A branch;
(c) An office;
(d) A factory;
(e) A workshop; and
(f) A mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

3. A building site or construction or installation project constitutes a permanent establishment if, but only if, it lasts more than 12 months.

4. The use of a drilling rig or ship in a Contracting State to explore for or exploit natural resources constitutes a permanent establishment if, but only if, such use is for more than 3 months in any twelve-month period.

5. A person acting in a Contracting State on behalf of a resident of the other Contracting State—other than an agent of an independent status to whom paragraph 7 applies—shall be deemed to be a permanent establishment in the first-mentioned State if such person has, and habitually exercises in that State, an authority to conclude contracts in the name of the resident.

6. Not withstanding the provisions of paragraphs 1, 2, and 5, the term "permanent establishment" shall be deemed not to include a fixed place of business used solely for, or a person referred to in paragraph 5 engaged solely in, one or more of the following activities:

(a) The use of facilities for the purpose of storage, display or delivery of goods or merchandise belonging to the resident;

(b) The maintenance of a stock of goods or merchandise belonging to the resident for the purpose of storage, display or delivery;

(c) The maintenance of a stock of goods or merchandise belonging to the resident for the purpose of processing by another person;

(d) The purchase of goods or merchandise, or the collection of information, for the resident; and

(e) Advertising, the supply of information, scientific research or similar activities which have a preparatory or auxiliary character, for the resident.

7. A resident of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because such resident carries on business in that other State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

8. The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not constitute either company a permanent establishment of the other.

9. For the purposes of the Convention, the provisions of this Article shall be applied in determining whether any person has a permanent establishment in any State.

Article VI

Income from real property

1. Income derived by a resident of a Contracting State from real property (including from agriculture or forestry) situated in the other Contracting State may be taxed in that other State.

2. For the purposes of this Convention, the term "real property" shall have the meaning which it has under the taxation laws of the Contracting State in which the property in question is situated and shall include any option or similar right in respect thereof. The term shall in any case include usufruct of real property and rights to explore for or to exploit mineral deposits, sources and other natural resources; ships and aircraft shall not be regarded as real property.

3. The provisions of paragraph 1 shall apply to income derived from the direct use, letting or use in any other form of real property and to income from the alienation of such property.

ARTICLE VII

Business profits

1. The business profits of a resident of a Contracting State shall be taxable only in that State unless the resident carries on business in the other Contracting State through a permanent establishment situated therein. If the resident carries on, or has carried on, business as aforesaid, the business profits of the resident may be taxed in the other State but only so much of them as is attributable to that permanent establishment.

2. Subject to the provisions of paragraph 3, where a resident of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the business profits which it might be expected to make if it were a distinct and separate person engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the resident and with any other person related to the resident (within the meaning of paragraph 2 of Article IX (Related Persons)).

3. In determining the business profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the permanent establishment, including executive and general administrative expenses so incurred, whether in the State in which the permanent establishment is situated or elsewhere. Nothing in this paragraph shall require a Contracting State to allow the deduction of any expenditure which, by reason of its nature, is not generally allowed as a deduction under the taxation laws of that State.

4. No business profits shall be attributed to a permanent establishment of a resident of a Contracting State by reason of the use thereof for either the mere purchase of goods or merchandise or the mere provision of executive, managerial or administrative facilities or services for such resident.

5. For the purposes of the preceding paragraphs, the business profits to be attributed to a permanent establishment shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.

6. Where business profits include items of income which are dealt with separately in other Articles of this Convention, then the provisions of those Articles shall not be affected by the provisions of this Article.

7. For the purposes of the Convention, the business profits attributable to a permanent establishment shall include only those profits derived from the assets or activities of the permanent establishment.

ARTICLE VIII

Transportation

1. Notwithstanding the provisions of Articles VII (Business Profits) and XIII (Gains), profits derived by a resident of a Contracting State from the operation of ships or aircraft in international traffic, and gains derived by a resident of a Contracting State from the alienation of ships or aircraft used principally in international traffic, shall be exempt from tax in the other Contracting State.

2. For the purposes of this Convention, profits derived by a resident of a Contracting State from the operation of ships or aircraft in international traffic include profits from:

(a) The rental of ships or aircraft operated in international traffic;

(b) The use, maintenance or rental of containers (including trailers and related equipment for the transport of containers) used in international traffic; and

(c) The rental of ships, aircraft or containers (including trailers and related equipment for the transport of containers) provided that such profits are incidental to profits referred to in paragraph 1, 2(a) or 2(b).

3. Notwithstanding the provisions of Article VII (Business Profits), profits derived by a resident of a Contracting State from a voyage of a ship where the principal purpose of the voyage is to transport passengers or property between places in the other Contracting State may be taxed in that other State.

4. Notwithstanding the provisions of Articles VII (Business Profits) and XII (Royalties), profits of a resident of a Contracting State engaged in the operation of motor vehicles or a railway as a common carrier or a contract carrier derived from:

(a) The transportation of passengers or property between a point outside the other Contracting State and any other point; or

(b) The rental of motor vehicles (including trailers) or railway rolling stock, or the use, maintenance or rental of containers (including trailers and related equipment for the transport of containers) used to transport passengers or property between a point outside the other Contracting State and any other point shall be exempt from tax in that other Contracting State.

5. The provisions of paragraphs 1, 3 and 4 shall also apply to profits or gains referred to in those paragraphs derived by a resident of a Contracting State from the participation in a pool, a joint business or an international operating agency.

6. Notwithstanding the provisions of Article XII (Royalties), profits derived by a resident of a Contracting State from the use, maintenance or rental of railway rolling stock, motor vehicles, trailers or containers (including trailers and related equipment for the transport of containers) used in the other Contracting State for a period or periods not expected to exceed in the aggregate 183 days in any twelve-month period shall be exempt from tax in the other Contracting State except to the extent that such profits are attributable to a permanent establishment in the other State and liable to tax in the other State by reason of Article VII (Business Profits).

ARTICLE IX

Related persons

1. Where a person in a Contracting State and a person in the other Contracting State are related and where the arrangements between them differ from those which would be made between unrelated persons, each State may adjust the amount of the income, loss or tax payable to reflect the income, deductions, credits or allowances which would, but for those arrangements, have been taken into account in computing such income, loss or tax.

2. For the purposes of this Article, a person shall be deemed to be related to another person if either person participates directly or indirectly in the management or control of the other, or if any third person or persons participate directly or indirectly in the management or control of both.

3. Where an adjustment is made or to be made by a Contracting State in accordance with paragraph 1, the other

Contracting State shall (notwithstanding any time or procedural limitations in the domestic law of that other State) make a corresponding adjustment to the income, loss or tax of the related person in that other State if:

(a) It agrees with the first-mentioned adjustment; and

(b) Within six years from the end of the taxable year to which the first-mentioned adjustment relates, the competent authority of the other State has been notified of the first-mentioned adjustment.

4. In the event that the notification referred to in paragraph 3 is not given within the time period referred to therein, and if the person to whom the first-mentioned adjustment relates has not received, at least six months prior to the expiration of such time period, notification of such adjustment from the Contracting State which has made or is to make such adjustment that State shall, notwithstanding the provisions of paragraph 1, not make the first-mentioned adjustment to the extent that such adjustment would give rise to double taxation.

5. The provisions of paragraphs 3 and 4 shall not apply in the case of fraud, willful default or neglect or gross negligence.

ARTICLE X

Dividends

1. Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other state.

2. However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident and according to the laws of that State; but if a resident of the other Contracting State is the beneficial owner of such dividends, the tax so charged shall not exceed:

(a) 10 per cent of the gross amount of the dividends if the beneficial owner is a company which owns at least 10 per cent of the voting stock of the company paying the dividends;

(b) 15 per cent of the gross amount of the dividends in all other cases.

This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid.

3. The term "dividends" as used in this Article means income from shares or other rights, not being debt-claims, participating in profits, as well as income subjected to the same taxation treatment as income from shares by the taxation laws of the State of which the company making the distribution is a resident.

4. The provisions of paragraph 2 shall not apply if the beneficial owner of the dividends, being a resident of a Contracting State, carries on business in the other Contracting State of which the company paying the dividends is a resident, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the holding in respect of which the dividends are paid is effectively connected with such permanent establishment of fixed base. In such case, the provisions of Article VII (Business Profits) or Article XIV (Independent Personal Services), as the case may be, shall apply.

5. Where a company is a resident of a Contracting State, the other contracting State may not impose any tax on the dividends paid by the company, except insofar as such dividends are paid to a resident of that other State or insofar as the holding in respect of which the dividends are paid is effectively connected with a permanent establishment or a fixed base situated in that other State, nor subject the company's undistributed profits to a tax, even if the dividends paid or the undistributed profits consist wholly or partly of profits or income arising in such other State.

6. Nothing in this Convention shall be construed as preventing a Contracting State from imposing a tax on the earnings of a company attributable to permanent establishments in that State, in addition to the tax which would be chargeable on the earnings of a company which is a resident of that State, provided that any additional tax so imposed shall not exceed 10 per cent of the amount of such earnings which have not been subjected to such additional tax in previous taxation years. For the purposes of this paragraph, the term "earnings" means the amount by which the business profits attributable to permanent establishments in a Contracting State (including gains from the alienation of property forming part of the business property of such permanent establishments) in a year and previous years exceeds the sum of:

(a) Business losses attributable to such permanent establishments (including losses from the alienation of property forming part of the business property of such permanent establishments) in such year and previous years;

(b) All taxes, other than the additional tax referred to in this paragraph, imposed on such profits in that State;

(c) The profits reinvested in that State, provided that where that State is Canada, such amount shall be determined in accordance with the existing provisions of the law of Canada regarding the computation of the allowance in respect to investment in property in Canada, and any subsequent modification of those provisions which shall not affect the general principle hereof; and

(d) Five hundred thousand Canadian dollars ($500,000) or its equivalent in United States currency, less any amounts deducted by the company, or by an associated company with respect to the same or a similar business, under this subparagraph (d); for the purposes of this subparagraph (d) a company is associated with another company if one company directly or indirectly controls the other, or both companies are directly or indirectly controlled by the same person or persons, or if the two companies deal with each other not at arm's length.

7. Notwithstanding the provisions of paragraph 5, a Contracting State, other than a Contracting State that imposes the additional tax on earnings referred to in paragraph 6, may tax a dividend paid by a company to the extent that the dividend is attributable to profits earned in taxable years beginning after the date of signature of the Convention if, for the three-year period ending with the close of the company's taxable period preceding the declaration of the dividend (or for such part of that three-year period as the company has been in existence, or for the first taxable year if the dividend was declared in that taxable year), at least 50 per cent of such company's gross income from all sources was included in the computation of the business profits attributable to a permanent establishment which such company had in that State; provided that where a resident of the other Contracting State is the beneficial owner of such dividend any tax so imposed on the dividend shall be subject to the limitations of paragraph 2 or the rules of paragraph 4, as the case may be.

8. Notwithstanding the provisions of paragraph 5, a company which is a resident of Canada and which has income

subject to tax in the United States (without regard to the provisions of the Convention) may be liable to the United States accumulated earnings tax and personal holding company tax but only if 50 per cent or more in value of the outstanding voting shares of the company is owned, directly or indirectly, throughout the last half of its taxable year by citizens or residents of the United States (other than citizens of Canada who do not have immigrant status in the United States or who have not been residents in the United States for more than three taxable years) or by residents of a third State.

ARTICLE XI

Interest

1. Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that State; but if a resident of the other Contracting State is the beneficial owner of such interest, the tax so charged shall not exceed 15 per cent of the gross amount of the interest.

3. Notwithstanding the provisions of paragraph 2, interest arising in a Contracting State shall be exempt from tax in that State if:

(a) The interest is beneficially owned by the other Contracting State, a political subdivision or local authority thereof or an instrumentality of such other State, subdivision or authority, and is not subject to tax by that other State;

(b) The interest is beneficially owned by a resident of the other Contracting State and is paid with respect to debt obligations issued at arm's length and guaranteed or insured by that other State or a political subdivision thereof or an instrumentality of such other State or subdivision which is not subject to tax by that other State;

(c) The interest is benefically owned by a resident of the other Contracting State and is paid by the first-mentioned State, a political subdivision or local authority thereof or an instrumentality of such first-mentioned State, subdivision or authority which is not subject to tax by that first-mentioned State;

(d) The interest is beneficially owned by a seller who is a resident of the other Contracting State and is paid by a purchaser in connection with the sale on credit of any equipment, merchandise or services, except where the sale is made between persons dealing with each other not at arm's length; or

(e) The interest is paid by a company created under the laws in force in the other Contracting State will respect to an obligation entered into before the date of signature of this Convention, provided that such interest would have been exempt from tax in the first-mentioned State under Article XII of the 1942 Convention.

4. The term "interest" as used in this Article means income from debt-claims of every kind, whether or not secured by mortgage, and whether or not carrying a right to participate in the debtor's profits, and in particular, income from government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures, as well as income assimilated to income from money lent by the taxation laws of the Contracting State in which the income arises. However, the term "interest" does not include income dealt with in Article X (Dividends).

5. The provisions of paragraph 2 and 3 shall not apply if the beneficial owner of the interest, being a resident of a Contracting State, carries on business in the other Contracting State in which the interest arises, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the debt-claim in respect of which the interest is paid is effectively connected with such permanent establishment or fixed base. In such case, the provisions of Article VII (Business Profits) or Article XIV (Independent Personal Services), as the case may be, shall apply.

6. For the purposes of this Article, interest shall be deemed to arise in a Contracting State when the payer is that State itself, or a political subdivision, local authority or resident of that State. Where, however, the person paying the interest, whether he is a resident of a Contracting State or not, has in a State other than that of which he is a resident a permanent establishment or a fixed base in connection with which the indebtedness on which the interest is paid was incurred, and such interest is borne by such permanent establishment or fixed base, then such interest shall be deemed to arise in the State in which the permanent establishment or fixed base is situated and not in the State of which the payer is a resident.

7. Where, by reason by a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the interest, having regard to the debt-claim for which it is paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of the Convention.

8. Where a resident of a Contracting State pays interest to a person other than a resident of the other Contracting State, that other State may not impose any tax on such interest except insofar as it arises in that other State or insofar as the debt-claim in respect of which the interest is paid effectively connected with a permanent establishment or a fixed base situated in that other State.

ARTICLE XII

Royalties

1. Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such royalties may also be taxed in the Contracting State in which they arise, and according to the laws of that State; but if a resident of the other Contracting State is the beneficial owner of such royalties, the tax so charged shall not exceed 10 per cent of the gross amount of the royalties.

3. Notwithstanding the provisions of paragraph 2, copyright royalties and other like payments in respect of the production or reproduction of any literary, dramatic, musical or artistic work (but not including royalties in respect of motion picture films and works on film or videotape for use in connection with television) arising in a Contracting State and beneficially owned by a resident of the other Contracting State shall be taxable only in that other State.

4. The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work (including motion picture films and works on film or videotape for use in connection with television), any patent, trademark, design or

model, plan, secret formula or process, or for the use of, or the right to use, tangible personal property or for information concerning industrial, commercial or scientific experience, and, notwithstanding the provisions of Article XIII (Gains), includes gains from the alienation of any intangible property or rights described in this paragraph to the extent that such gains are contingent on the productivity, use or subsequent disposition of such property or rights.

5. The provisions of paragraphs 2 and 3 shall not apply if the beneficial owner of the royalties, being a resident of a Contracting State, carries on business in the other Contracting State in which the royalties arise, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the right or property in respect of which the royalties are paid is effectively connected with such permanent establishment or fixed base. In such case the provisions of Article VII (Business Profits) or Article XIV (Independent Personal Services), as the case may be, shall apply.

6. For the purposes of this Article, royalties shall be deemed to arise in a Contracting State when the payer is that State itself, or a political subdivision, local authority or resident of that State. However:

(a) Except as provided in subparagraph (b), where the person paying the royalties, whether he is a resident of a Contracting State or not, has in a State other than that of which he is a resident a permanent establishment or a fixed base in connection with which the obligation to pay the royalties was incurred, and such royalties are borne by such permanent establishment or fixed base, then such royalties shall be deemed to arise in the State in which the permanent establishment or fixed base is situated and not in the State of which the payer is a resident; and

(b) Where the royalties are for the use of intangible property or tangible personal property in a Contracting State, then such royalties shall be deemed to arise in that State and not in the State of which the payer is a resident.

7. Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the royalties, having regard to the use, right or information for which they are paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisons of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.

8. Where a resident of a Contracting State pays royalties to a person other than a resident of the other Contracting State, that other State may not impose any tax on such royalties except insofar as they arise in that other State or insofar as the right or property in respect of which the royalties are paid is effectively connected with a permanent establishment or a fixed base situated in that other State.

ARTICLE XIII

Gains

1. Gains derived by a resident of a Contracting State from the alienation of real property situated in the other Contracting State may be taxed in that other State.

2. Gains from the alienation of personal property forming part of the business property of a permanent establishment which a resident of a Contracting State has or had (within the twelve-month period preceding the date of alienation) in the other Contracting State or of personal property pertaining to a fixed base which is or was available (within the twelve-month period preceding the date of alienation) to a resident of a Contracting State in the other Contracting State for the purpose of performing independent personal services, including such gains from the alienation of such a permanent establishment or of such a fixed base, may be taxed in that other State.

3. Gains derived by a resident of a Contracting State from the alienation of:

(a) Shares forming part of a substantial interest in the capital stock of a company which is not a resident of that State the value of which shares is derived principally from real property situated in the other Contracting State; or

(b) An interest in a partnership, trust or estate the value of which is derived principally from real property situated in the other Contracting State

may be taxed in that other State, provided that the laws in force in the first-mentioned State at the time of such alienation would, in comparable circumstances, subject to taxation gains derived by a resident of that other State. For the purposes of this paragraph,

(c) The term "real property" includes the shares of a company the value of which shares is derived principally from real property or an interest in a partnership, trust or estate referred to in subparagraph (b), but does not include property (other than mines, oil or gas wells, rental property or property used for agriculture or forestry) in which the business of the company, partnership, trust or estate is carried on; and

(d) A substantial interest exists when the resident and persons related thereto own 10 per cent or more of the shares of any class of the capital stock of a company.

4. Gains from the alienation of any property other than that referred to in paragraphs 1, 2 and 3 shall be taxable only in the Contracting State of which the alienator is a resident.

5. The provisions of paragraph 4 shall not affect the right of a Contracting State to levy a tax on gains from the alienation of property derived by an individual who is a resident of the other Contracting State if such individual:

(a) Was a resident of the first-mentioned State for 120 months during any period of 20 consecutive years; and

(b) Was a resident of the first-mentioned State at any time during the ten years immediately preceding the alienation of the property.

6. Where an individual (other than a citizen of the United States) who was a resident of Canada became a resident of the United States, in determining his liability to United States taxation in respect of any gain from the alienation of a principal residence in Canada owned by him at the time he ceased to be a resident of Canada, the adjusted basis of such property shall be no less than its fair market value at that time.

7. Where at any time an individual is treated for the purposes of taxation by a Contracting State as having alienated a property and is taxed in that State by reason thereof and the domestic law of the other Contracting State at such time defers (but does not forgive) taxation, that individual may elect in his annual return of income for the year of such alienation to be liable to tax in the other Contracting State in that year as if he had, immedi-

ately before that time, sold and repurchased such property for an amount equal to its fair market value at that time.

8. Where a resident of a Contracting State alienates property in the course of a corporate organization, reorganization, amalgamation, division or similar transaction and profit, gain or income with respect to such alienation is not recognized for the purpose of taxation in that State, if requested to do so by the person who acquires the property, the competent authority of the other Contracting State may agree, in order to avoid double taxation and subject to terms and conditions satisfactory to such competent authority, to defer the recognition of the profit, gain or income with respect to such property for the purpose of taxation in that other State until such time and in such manner as may be stipulated in the agreement.

9. Where a resident of a Contracting State alienates property which may in accordance with this Article be taxed in the other Contracting State and which was owned by a resident of the first-mentioned State on the date of signature of this Convention, the amount of the gain which is liable to tax in that other State in accordance with this Article shall be reduced by the proportion of the gain attributable (on a monthly basis), or such greater portion of the gain as is shown to the satisfaction of the competent authority of the other State to be reasonably attributable, to the period ending on December 31 of the year in which the Convention enters into force; the provisions of this paragraph shall not apply to property which on the date of signature of the Convention formed part of the business property of a permanent establishment or pertained to a fixed base in the other Contracting State.

ARTICLE XIV

Independent personal services

Income derived by an individual who is a resident of a Contracting State in respect of independent personal services may be taxed in that State. Such income may also be taxed in the other Contracting State if the individual has or had a fixed base regularly available to him in that other State but only to the extent that the income is attributable to the fixed base.

ARTICLE XV

Dependent personal services

1. Subject to the provisions of Articles XVIII (Pensions and Annuities) and XIX (Government Service), salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.

2. Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in a calendar year in the other Contracting State shall be taxable only in the first-mentioned State if:

(a) Such remuneration does not exceed ten thousand dollars ($10,000) in the currency of that other State; or

(b) The recipient is present in the other Contracting State for a period or periods not exceeding in the aggregate 183 days in that year and the remuneration is not borne by an employer who is a resident of that other State or by a permanent establishment or a fixed base which the employer has in that other State.

3. Notwithstanding the provisions of paragraphs 1 and 2, remuneration derived by a resident of a Contracting State in respect of an employment regularly exercised in more than one State on a ship, aircraft, motor vehicle or train operated by a resident of that Contracting State shall be taxable only in that State.

ARTICLE XVI

Artistes and athletes

1. Notwithstanding the provisions of Articles XIV (Independent Personal Services) and XV (Dependent Personal Services), income derived by a resident of a Contracting State as an entertainer, such as a theatre, motion picture, radio or television artiste, or a musician, or as an athlete, from his personal activities as such exercised in the other Contracting State, may be taxed in that other State, except where the amount of the gross receipts derived by such entertainer or athlete, including expenses reimbursed to him or borne on his behalf, from such activities do not exceed fifteen thousand dollars ($15,000) in the currency of that other State for the calendar year concerned.

2. Where income in respect of personal activities exercised by an entertainer or an athlete in his capacity as such accrues not to the entertainer or athlete but to another person, that income may, notwithstanding the provisions of Articles VII (Business Profits), XIV (Independent Personal Services) and XV (Dependent Personal Services), be taxed in the Contracting State in which the activities of the entertainer or athlete are exercised. For the purposes of the preceding sentence, income of an entertainer or athlete shall be deemed not to accrue to another person if it is established that neither the entertainer or athlete, nor persons related thereto, participate directly or indirectly in the profits of such other person in any manner, including the receipt of deferred remuneration, bonuses, fees, dividends, partnership distributions or other distributions.

3. The provisions of this Article shall not apply to the income of an athlete in respect of an employment with a team which participates in a league with regularly schedule games in both Contracting States.

ARTICLE XVII

Withholding of taxes in respect of independent personal services

1. Deduction and withholding of tax on account of the tax liability for a taxable year on remuneration paid to an individual who is a resident of a Contracting State (including an entertainer or athlete) in respect of the performance of independent personal services in the other Contracting State may be required by that other State, but with respect to the first five thousand dollars ($5,000) in the currency of that other State, paid as remuneration in that taxable year by each payer, such deduction and withholding shall not exceed 10 per cent of the payment.

2. Where the competent authority of a Contracting State considers that an amount that would otherwise be deducted or withheld from any amount paid or credited to an individual who is a resident of the other Contracting State in respect of the performance of independent personal services in the first-mentioned State is excessive in relation to the estimated tax liability for the taxable year of that individual in the first-mentioned State, it may determine that a lesser amount will be deducted or withheld.

3. The provisions of this Article shall not affect the liability of a resident of a Contracting State referred to in paragraph 1 or 2 for tax imposed by the other Contracting State.

ARTICLE XVIII

Pensions and annuities

1. Pensions and annuities arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State, but the amount of any pension included in income for the purposes of taxation in that other State shall not exceed the amount that would be included in the first-mentioned State if the recipient were a resident thereof.

2. However:

(a) Pensions may also be taxed in the Contracting State in which they arise and according to the laws of that State; but if a resident of the other Contracting State is the beneficial owner of a periodic pension payment, the tax so charged shall not exceed 15 per cent of the gross amount of such payment; and

(b) Annuities may also be taxed in the Contracting State in which they arise and according to the laws of that State; but if a resident of the other Contracting State is the beneficial owner of an annuity payment, the tax so charged shall not exceed 15 per cent of the portion of such payment that is liable to tax in the first-mentioned State.

3. For the purposes of this Convention, the term "pensions" includes any payment under a superannuation, pension or retirement plan, Armed Forces retirement pay, war veterans pensions and allowances and amounts paid under a sickness, accident or disability plan, but does not include payments under an income-averaging annuity contract or any benefit referred to in paragraph 5.

4. For the purposes of the Convention, the term "annuities" means a stated sum paid periodically at stated times during life or during a specified number of years, under an obligation to make the payments in return for adequate and full consideration (other than services rendered), but does not include a payment that is not a periodic payment or any annuity the cost of which was deductible for the purposes of taxation in the Contracting State in which it was acquired.

5. Benefits under the social security legislation in a Contracting State paid to a resident of the other Contracting State or a citizen of the United States shall be taxable only in the first-mentioned State.

6. Alimony and other similar amounts (including child support payments) arising in a Contracting State and paid to a resident of the other Contracting State shall be taxable only in that other State, but the amount included in income for the purposes of taxation in that other State shall not exceed the amount that would be included in income in the first-mentioned State if the recipient were a resident thereof.

ARTICLE XIX

Government service

Remuneration, other than a pension, paid by a Contracting State or a political subdivision or local authority thereof to a citizen of that State in respect of services rendered in the discharge of functions of a governmental nature shall be taxable only in that State. However, the provisions of Article XIV (Independent Personal Services), XV (Dependent Personal Services), or XVI (Artistes and Athletes), as the case may be, shall apply, and the preceding sentence shall not apply to remuneration paid in respect of services rendered in connection with a trade or business carried on by a Contracting State or a political subdivision or local authority thereof.

ARTICLE XX

Students

Payments which a student, apprentice or business trainee, who is or was immediately before visiting a Contracting State a resident of the other Contracting State, and who is present in the first-mentioned State for the purpose of his full-time education or training, receives for the purpose of his maintenance, education or training shall not be taxed in that State provided that such payments are made to him from outside that State.

ARTICLE XXI

Exempt organizations

1. Subject to the provisions of paragraph 3, income derived by a religious, scientific, literary, educational or charitable organization shall be exempt from tax in a Contracting State if it is resident in the other Contracting State but only to the extent that such income is exempt from tax in that other State.

2. Subject to the provisions of paragraph 3, income referred to in Articles X (Dividends) and XI (Interest) derived by a trust, company or other organization constituted and operated exclusively to administer or provide benefits under one or more funds or plans established to provide pension, retirement or other employee benefits shall be exempt from tax in a Contracting State if it is resident in the other Contracting State and its income is generally exempt from tax in that other State.

3. The provisions of paragraphs 1 and 2 shall not apply with respect to the income of a trust, company or other organization from carrying on a trade or business or from a related person other than a person referred to in paragraph 1 or 2.

4. A religious, scientific, literary, educational or charitable organization which is resident in Canada and which has received substantially all of its support from persons other than citizens or residents of the United States shall be exempt in the United States from the United States excise taxes imposed with respect to private foundations.

5. For the purposes of United States taxation, contributions by a citizen or resident of the United States to an organization which is resident in Canada, which is generally exempt from Canadian tax and which could qualify in the United States to receive deductible contributions if it were resident in the United States shall be treated as charitable contributions; however, such contributions (other than such contributions to a college or university at which the citizen or resident or a member of his family is or was enrolled) shall not be deductible in any taxable year to the extent that they exceed an amount determined by applying the percentage limitations of the laws of the United States in respect of the deductibility of charitable contributions to the income of such citizen or resident arising in Canada. The preceding sentence shall not be interpreted to allow in any taxable year deductions for charitable contributions in excess of the amount allowed under the percentage limitations of the laws of the United States in respect of the deductibility of charitable contributions.

6. For the purposes of Canadian taxation, gifts by a resident of Canada to an organization which is resident in the United States, which is generally exempt from United States tax and which could qualify in Canada to receive deductible gifts if it were created or established and resident in Canada shall be treated as gifts to a registered charity; however, such gifts (other than such gifts to a college or university at which the resident or a member of his family is or was enrolled) shall not be deductible in any taxable year to the

extent that they exceed an amount determined by applying the percentage limitations of the laws of Canada in respect of the deductibility of gifts to registered charities to the income of such resident arising in the United States. The preceding sentence shall not be interpreted to allow in any taxable year deductions for gifts to registered charities in excess of the amount allowed under the percentage limitations of the laws of Canada in respect of the deductibility of gifts to registered charities.

ARTICLE XXII

Other income

1. Items of income of a resident of a Contracting State, wherever arising, not dealt with in the foregoing Articles of this Convention shall be taxable only in that State, except that if such income arises in the other Contracting State it may also be taxed in that other State.

2. To the extent that income distributed by an estate or trust is subject to the provisions of paragraph 1, then, notwithstanding such provisions, income distributed by an estate or trust which is a resident of a Contracting State to a resident of the other Contracting State who is a beneficiary of the estate or trust may be taxed in the first-mentioned State and according to the laws of that State, but the tax so charged shall not exceed 15 per cent of the gross amount of the income; provided, however, that such income shall be exempt from tax in the first-mentioned State to the extent of any amount distributed out of income arising outside that State.

ARTICLE XXIII

Capital

1. Capital represented by real property, owned by a resident of a Contracting State and situated in the other Contracting State, may be taxed in that other State.

2. Capital represented by personal property forming part of the business property of a permanent establishment which a resident of a Contracting State has in the other Contracting State, or by personal property pertaining to a fixed base available to a resident of a Contracting State in the other Contracting State for the purpose of performing independent personal services, may be taxed in that other State.

3. Capital represented by ships and aircraft operated by a resident of a Contracting State in international traffic, and by personal property pertaining to the operation of such ships and aircraft, shall be taxable only in that State.

4. All other elements of capital of a resident of a Contracting State shall be taxable only in that State.

ARTICLE XXIV

Elimination of double taxation

1. In the case of the United States, subject to the provisions of paragraphs 4, 5, and 6, double taxation shall be avoided as follows: In accordance with the provisions and subject to the limitations of the law of the United States (as it may be amended from time to time without changing the general principle hereof), the United States shall allow to a citizen or resident of the United States, or to a company electing to be treated as a domestic corporation, as a credit against the United States tax on income the appropriate amount of income tax paid or accrued to Canada; and, in the case of a company which is a resident of the United States owning at least 10 percent of the voting stock of a company which is a resident of Canada from which it receives dividends in any taxable year, the United States shall allow as a credit against the United States tax on income the appropriate amount of income tax paid or accrued to Canada by that company with respect to the profits out of which such dividends are paid. Such appropriate amount shall be based upon the amount of income tax paid or accrued to Canada, but shall not exceed that proportion of the United States tax that taxable income arising in Canada bears to the entire taxable income.

2. In the case of Canada, subject to the provisions of paragraphs 4, 5 and 6, double taxation shall be avoided as follows:

(a) Subject to the provisions of the law of Canada regarding the deduction from tax payable in Canada of tax paid in a territory outside Canada and to any subsequent modification of those provisions (which shall not affect the general principle hereof), and unless a greater deduction or relief is provided under the law of Canada, income tax paid or accrued to the United States on profits, income or gains arising in the United States shall be deducted from any Canadian tax payable in respect of such profits, income or gains; and

(b) Subject to the provisions of the law of Canada regarding the determination of the exempt surplus of a foreign affiliate and to any subsequent modification of those provisions (which shall not affect the general principle hereof), for the purposes of computing Canadian tax, a company which is a resident of Canada shall be allowed to deduct in computing its taxable income any dividend received by it out of the exempt surplus of a foreign affiliate which is a resident of the United States.

3. For the purposes of this Article:

(a) Profits, income or gains (other than gains to which paragraph 5 of Article XIII (Gains) applies) of a resident of a Contracting State which may be taxed in the other Contracting State in accordance with the Convention (without regard to paragraph 2 of Article XXIX (Miscellaneous Rules)) shall be deemed to arise in that other State; and

(b) Profits, income or gains of a resident of a Contracting State which may not be taxed in the other Contracting State in accordance with the Convention (without regard to paragraph 2 of Article XXIX (Miscellaneous Rules)) or to which paragraph 5 of Article XIII (Gains) applies shall be deemed to arise in the first-mentioned State.

4. Where a United States citizen is a resident of Canada, the following rules shall apply:

(a) Canada shall allow a deduction from the Canadian tax in respect of income tax paid or accrued to the United States in respect of profits, income or gains which arise (within the meaning of paragraph 3) in the United States, except that such deduction need not exceed the amount of the tax that would be paid to the United States if the resident were not a United States citizen; and

(b) For the purposes of computing the United States tax, the United States shall allow as a credit against United States tax the income tax paid or accrued to Canada after the deduction referred to in subparagraph (a). The credit so allowed shall not reduce that portion of the United States tax that is deductible from Canadian tax in accordance with subparagraph (a).

5. Notwithstanding the provisions of paragraph 4, where a United States citizen is a resident of Canada, the following rules shall apply in respect of the items of income referred to in Article X (Dividends), XI (Interest) or XII (Royalties) which arise (within the meaning of paragraph 3) in the United States, as long as

the law in force in Canada allows a deduction in computing income for the portion of any foreign tax paid in respect of such items which exceeds 15 percent of the amount thereof:

(a) The deduction so allowed in Canada shall not be reduced by any credit or deduction for income tax paid or accrued to Canada allowed in computing the United States tax on such items;

(b) Canada shall allow a deduction from the Canadian tax in respect of the income tax paid or accrued to the United States on such items, except that such deduction need not exceed 15 per cent of the gross amount of such items that has been included in computing the income of the citizen for Canadian tax purposes; and

(c) For the purposes of computing the United States tax on such items, the United States shall allow as a credit against United States tax the income tax paid or accrued to Canada after the deduction referred to in subparagraph (b). The credit so allowed shall reduce only that portion of the United States tax on such items which exceeds 15 per cent of the amount thereof included in computing United States taxable income.

6. Where a United States citizen is a resident of Canada, items of income referred to in paragraph 4 or 5 shall, notwithstanding the provisions of paragraph 3, be deemed to arise in Canada to the extent necessary to avoid the double taxation of such income under paragraph 4(b) or paragraph 5(c).

7. For the purposes of this Article, any reference to "income tax paid or accrued" to a Contracting State shall include Canadian tax and United States tax, as the case may be, and taxes of general application which are paid or accrued to a political subdivision or local authority of that State, which are not imposed by that political subdivision or local authority in a manner inconsistent with the provisions of the Convention and which are substantially similar to the taxes of that State referred to in paragraphs 2 and 3(a) of Article II (Taxes Covered).

8. Where a resident of a Contracting State owns capital which, in accordance with the provisions of the Convention, may be taxed in the other Contracting State, the first-mentioned State shall allow as a deduction from the tax on the capital of that resident an amount equal to the capital tax paid in that other State. The deduction shall not, however, exceed that part of the capital tax, as computed before the deduction is given, which is attributable to the capital which may be taxed in that other State.

ARTICLE XXV

Non-Discrimination

1. Citizens of a Contracting State, who are residents of the other Contracting State, shall not be subjected in that other State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which citizens of that other State in the same circumstances are or may be subjected.

2. Citizens of a Contracting State, who are not residents of the other Contracting State, shall not be subjected in that other State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which citizens of any third State in the same circumstances (including State of residence) are or may be subjected.

3. In determining the taxable income of an individual who is a resident of a Contracting State there shall be allowed as a deduction in respect of any other person who is a resident of the other Contracting State and who is dependent on the individual for support the amount that would be so allowed if that other person were a resident of the first-mentioned State.

4. Where a married individual who is a resident of Canada and not a citizen of the United States has income that is taxable in the United States pursuant to Article XV (Dependent Personal Services), the United States tax with respect to such income shall not exceed such proportion of the total United States tax that would be payable for the taxable year if both the individual and his spouse were United States citizens as the individual's taxable income determined without regard to this paragraph bears to the amount that would be the total taxable income of the individual and his spouse. For the purposes of this paragraph.

(a) The "total United States tax" shall be determined as if all the income of the individual and his spouse arose in the United States; and

(b) A deficit of the spouse shall not be taken into account in determining taxable income.

5. Any company which is a resident of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which other similar companies of the first-mentioned State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of a third State, are or may be subjected.

6. Notwithstanding the provisions of Article XXIV (Elimination of Double Taxation), the taxation on a permanent establishment which a resident of a Contracting State has in the other Contracting State shall not be less favorably levied in the other State than the taxation levied on residents of the other State carrying on the same activities. This provision shall not be construed as obliging a Contracting State to grant to residents of the other Contracting State any personal allowances, reliefs and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents.

7. Except where the provisions of paragraph 1 of Article IX (Related Persons), paragraph 7 of Article XI (Interest) or paragraph 7 of Article XII (Royalties) apply, interest, royalties and other disbursements paid by a resident of a Contracting State to a resident of the other Contracting State shall, for the purposes of determining the taxable profits of the first-mentioned resident, be deductible under the same conditions as if they had been paid to a resident of the first-mentioned State. Similarly, any debts of a resident of a Contracting State to a resident of the other Contracting State shall, for the purposes of determining the taxable capital of the first-mentioned resident, be deductible under the same conditions as if they had been contracted to a resident of the first-mentioned State.

8. The provisions of paragraph 7 shall not affect the operation of any provision of the taxation laws of a Contracting State:

(a) Relating to the deductibility of interest and which is in force on the date of signature of this Convention (including any subsequent modification of such provisions that does not change the general nature thereof); or

(b) Adopted after such date by a

Contracting State and which is designed to ensure that a person who is not a resident of that State does not enjoy, under the laws of that State, a tax treatment that is more favorable than that enjoyed by residents of that State.

9. Expenses incurred by a citizen or resident of a Contracting State with respect to any convention (including any seminar, meeting, congress or other function of a similar nature) held in the other Contracting State shall, for the purposes of taxation in the first-mentioned State, be deductible to the same extent that such expenses would be deductible if the convention were held in first-mentioned State.

10. Notwithstanding the provisions of Article II (Taxes Covered), this Article shall apply:

(a) In the case of Canada, to all taxes imposed under the Income Tax Act; and

(b) In the case of the United States, to all taxes imposed under the Internal Revenue Code.

ARTICLE XXVI

Mutual agreement procedure

1. Where a person considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of this Convention, he may, irrespective of the remedies provided by the domestic law of those States, present his case in writing to the competent authority of the Contracting State of which he is a resident or, if he is a resident of neither Contracting State, or which he is a national.

2. The competent authority of the Contracting State to which the case has been presented shall endeavor, if the objection appears to it to be justified and if it is not itself able to arrive at a satisfactory solution, to resolve the case by mutual agreement with the competent authority of the other Contracting State, with a view to the avoidance of taxation which is not in accordance with the Convention. Except where the provisions of Article IX (Related Persons) apply, any agreement reached shall be implemented notwithstanding any time or other procedural limitations in the domestic law of the Contracting States, provided that the competent authority of the other Contracting State has received notification that such a case exists within six years from the end of the taxable year to which the case relates.

3. The competent authorities of the Contracting States shall endeavor to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. In particular, the competent authorities of the Contracting States may agree:

(a) To the same attribution of profits to a resident of a Contracting State and its permanent establishment situated in the other Contracting State;

(b) To the same allocation of income, deductions, credits or allowances between persons;

(c) To the same determination of the source, and the same characterization, of particular items of income;

(d) To a common meaning of any term used in the Convention;

(e) To the elimination of double taxation with respect to income distribution by an estate or trust;

(f) To the elimination of double taxation with respect to a partnership; or

(g) To increases in any other amounts referred to in the Convention to reflect monetary or economic developments.

They may also consult together for the elimination of double taxation in cases not provided for in the Convention.

4. Each of the Contracting States will endeavor to collect on behalf of the other Contracting State such amounts as may be necessary to ensure that relief granted by the Convention from taxation imposed by that other State does not enure to the benefit of persons not entitled thereto. However, nothing in this paragraph shall be construed as imposing on either of the Contracting States the obligation to carry out administrative measures of a different nature from those used in the collection of its own tax or which would be contrary to its public policy (order public).

5. The competent authorities of the Contracting States may communicate with each other directly for the purpose of reaching an agreement in the sense of the proceeding paragraphs.

ARTICLE XXVII

Exchange of information

1. The competent authorities of the Contracting States shall exchange such information as is necessary for carrying out the provisions of this Convention or of the domestic laws of the Contracting States concerning taxes covered by the Convention insofar as the taxation thereunder is not contrary to the Convention. The exchange of information is not restricted by Article I (Personal Scope). Any information received by a Contracting State shall be treated as secret in the same manner as information obtained under the taxation laws of that State and shall be disclosed only to persons or authorities (including courts and administrative bodies) involved in the assessment or collection of, the administration and enforcement in respect of, or the determination of appeals in relation to, the taxes covered by the Convention. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions.

2. If information is requested by a Contracting State in accordance with this Article, the other Contracting State shall endeavor to obtain the information to which the request relates in the same way as if its own taxation was involved notwithstanding the fact that the other State does not, at that time, need such information. If specifically requested by the competent authority of a Contracting State, the competent authority of the other Contracting State shall endeavor to provide information under this Article in the form requested, such as depositions of witnesses and copies of unedited original documents (including books, papers, statements, records, accounts or writings), to the same extent such depositions and documents can be obtained under the laws and administrative practices of that other State with respect to its own taxes.

3. In no case shall the provisions of paragraphs 1 and 2 be construed so as to impose on a Contracting State the obligation:

(a) To carry out administrative measures at variance with the laws and administrative practice of that or of the other Contracting State;

(b) To supply information which is not obtainable under the laws or in the normal course of the administration of that or of the other Contracting State; or

(c) To supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process, or information the disclosure of which would be contrary to public policy (ordre public).

4. Notwithstanding the provisions of Article II (Taxes Covered), for the pur-

poses of this Article the Convention shall apply:

(a) In the case of Canada, to all taxes imposed by the Government of Canada on estates and gifts and under the Income Tax Act; and

(b) In the case of the United States, to all taxes imposed under the Internal Revenue Code.

ARTICLE XXVIII

Diplomatic agents and consular officers

Nothing in this Convention shall affect the fiscal privileges of diplomatic agents or consular officers under the general rules of international law or under the provisions of special agreements.

ARTICLE XXIX

Miscellaneous rules

1. The provisions of this Convention shall not restrict in any manner any exclusion, exemption, deduction, credit or other allowance now or hereafter accorded by the laws of a Contracting State in the determination of the tax imposed by that State.

2. Except as provided in paragraph 3, nothing in the Convention shall be construed as preventing a Contracting State from taxing its residents (as determined under Article IV (Residence)) and, in the case of the United States, its citizens (including a former citizen whose loss of citizenship had as one of its principal purposes the avoidance of income tax, but only for a period of ten years following such loss) and companies electing to be treated as domestic corporations, as if there were no convention between the United States and Canada with respect to taxes on income and on capital.

3. The provisions of paragraph 2 shall not affect the obligations undertaken by a Contracting State:

(a) Under paragraphs 3 and 4 of Article IX (Related Persons), paragraphs 6 and 7 of Article XIII (Gains), paragraph 5 of Article XXIX (Miscellaneous Rules), paragraphs 3 and 5 of Article XXX (Entry into Force), and Articles XVIII (Pensions and Annuities), XIX (Government Service), XXI (Exempt Organizations), XXIV (Elimination of Double Taxation), XXV (Non-Discrimination) and XXVI (Mutual Agreement Procedure); and

(b) Under Article XX (Students), toward individuals who are neither citizens of, nor have immigrant status in, that State.

4. With respect to taxable years not barred by the statute of limitations ending on or before December 31 of the year in which the Convention enters into force, income from personal services not subject to tax by the United States under the 1942 Convention shall not be considered wages or net earnings from self-employment for purposes of social security taxes imposed under the Internal Revenue Code.

5. A United States citizen who is a resident of Canada and a beneficiary of a Canadian registered retirement savings plan may elect, under rules established by the competent authority of the United States, to defer United States taxation with respect to any income accrued in the plan but not distributed by the plan, until such time as a distribution is made from such plan, or any plan substituted therefor.

6. If 25 per cent or more of the capital of a company which is a resident of a Contracting State is owned directly or indirectly by individuals who are not residents of that State, and if by reason of special measures the tax imposed in that State on that company with respect to dividends (other than dividends referred to in paragraph 2(a) of Article X (Dividends)), interest or royalties arising in the other Contracting State is substantially less than the tax generally imposed by the first-mentioned State on corporate business profits, then, notwithstanding the provisions of Article X (Dividends), XI (Interest) or XII (Royalties), that other State may tax such dividends, interest or royalties as if there were no convention between the United States and Canada with respect to taxes on income and on capital.

ARTICLE XXX

Entry into force

1. This Convention shall be subject to ratification in accordance with the applicable procedures of each Contracting State and instruments of ratification shall be exchanged at Ottawa as soon as possible.

2. The Convention shall enter into force upon the exchange of instruments of ratification and, subject to the provisions of paragraph 3, its provisions shall have effect:

(a) For tax withheld at the source on income referred to in Articles X (Dividends), XI (Interest), XII (Royalties) and XVIII (Pensions and Annuities), with respect to amounts paid or credited on or after the first day of the second month next following the date on which the Convention enters into force;

(b) For other taxes, with respect to taxable years beginning on or after the first day of January next following the date on which the Convention enters into force; and

(c) Notwithstanding the provisions of subparagraph (b), for the taxes covered by paragraph 4 of Article XXIX (Miscellaneous Rules) with respect to all taxable years referred to in that paragraph.

3. For the purpose of applying the United States foreign tax credit in relation to taxes paid or accrued to Canada:

(a) Notwithstanding the provisions of paragraph 2(a) of Article II (Taxes Covered), the tax on 1971 undistributed income on hand imposed by Part IX of the Income Tax Act of Canada shall be considered to be an income tax for distributions made on or after the first day of January 1972 and before the first day of January 1979, and shall be considered imposed upon the recipient of a distribution, in the proportion that the distribution out of undistributed income with respect to which the tax has been paid bears to 85 per cent of such undistributed income; and

(b) The principles of paragraph 6 of Article XXIV (Elimination of Double Taxation) shall have effect for taxable years beginning on or after the first day of January 1976.

Any claim for refund based on the provisions of this paragraph may be filed on or before June 30 of the calendar year following that in which the Convention enters into force, notwithstanding any rule of domestic law to the contrary.

4. Subject to the provisions of paragraph 5, the 1942 Convention shall cease to have effect for taxes for which this Convention has effect in accordance with the provisions of paragraph 2.

5. Where any greater relief from tax would have been afforded by any provision of the 1942 Convention than under this Convention, any such provision shall continue to have effect for the first taxable year with respect to which the provisions of this Convention have effect under paragraph 2(b).

6. The 1942 Convention shall terminate on the last date on which it has effect in accordance with the preceding provisions of this Article.

7. The Exchange of Notes between the United States and Canada dated August

2 and September 17, 1928, providing for relief from double income taxation on shipping profits, is terminated. Its provisions shall cease to have effect with respect to taxable years beginning on or after the first day of January next following the date on which this Convention enters into force.

8. The provisions of the Convention between the Government of Canada and the Government of the United States of America for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on the Estates of Deceased Persons signed at Washington on February 17, 1961 shall continue to have effect with respect to estates of persons deceased prior to the first day of January next following the date on which this Convention enters into force but shall cease to have effect with respect to estates of persons deceased on or after that date. Such Convention shall terminate on the last date on which it has effect in accordance with the preceding sentence.

ARTICLE XXXI

Termination

1. This Convention shall remain in force until terminated by a Contracting State.

2. Either Contracting State may terminate the Convention at any time after 5 years from the date on which the Convention enters into force provided that at least 6 months' prior notice of termination has been given through diplomatic channels.

3. Where a Contracting State considers that a significant change introduced in the taxation laws of the other Contracting State should be accommodated by a modification of the Convention, the Contracting States shall consult together with a view to resolving the matter; if the matter cannot be satisfactorily resolved, the first-mentioned State may terminate the Convention in accordance with the procedures set forth in paragraph 2, but without regard to the 5 year limitation provided therein.

4. In the event the Convention is terminated, the Convention shall cease to have effect:

(a) For tax withheld at the source on income referred to in Articles X (Dividends), XI (Interest), XII (Royalties), XVIII (Pensions and Annuities) and paragraph 2 of Article XXII (Other Income), with respect to amounts paid or credited on or after the first day of January next following the expiration of the 6 months' period referred to in paragraph 2; and

(b) For other taxes, with respect to taxable years beginning on or after the first day of January next following the expiration of the 6 months' period referred to in paragraph 2.

In witness whereof, the undersigned, being duly authorized thereto by their respective Governments, have signed this Convention.

Done in two copies at Washington this twenty-sixth day of September, 1980, in the English and French languages, each text being equally authentic.

For the Government of the United States of America:

G. William Miller.

For the Government of Canada:

Allan J. MacEachen.

PROTOCOL AMENDING THE CONVENTION BETWEEN CANADA AND THE UNITED STATES OF AMERICA WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL SIGNED AT WASHINGTON ON SEPTEMBER 26, 1980

Canada and the United States of America,

Desiring to conclude a Protocol to amend the Convention with respect to Taxes on Income and on Capital signed at Washington on September 26, 1980 (hereinafter referred to as "the Convention"),

Have agreed as follows:

ARTICLE I

Subparagraph 1(h) of Article III (General Definitions) of the Convention shall be deleted and replaced by the following:

"(h) The term 'international traffic' with reference to a resident of a Contracting State means any voyage of a ship or aircraft to transport passengers or property (whether or not operated or used by that resident) except where the principal purpose of the voyage is to transport passengers or property between places within the other Contracting State;"

ARTICLE II

Paragraph 4 of Article V (Permanent Establishment) shall be deleted and replaced by the following:

"4. The use of an installation or drilling rig or ship in a Contracting State to explore for or exploit natural resources constitutes a permanent establishment if, but only if, such use is for more than three months in any twelve-month period."

ARTICLE III

Article VI (Income from Real Property) shall be deleted and replaced by the following:

"1. Income derived by a resident of a Contracting State from real property (including income from agriculture, forestry or other natural resources) situated in the other Contracting State may be taxed in that other State.

2. For the purposes of this Convention, the term "real property" shall have the meaning which it has under the taxation laws of the Contracting State in which the property in question is situated and shall include any option or similar right in respect thereof. The term shall in any case include usufruct of real property, rights to explore for or to exploit mineral deposits, sources and other natural resources and rights to amounts computed by reference to the amount or value of production from such resources; ships and aircraft shall not be regarded as real property.

3. The provisions of paragraph 1 shall apply to income derived from the direct use, letting or use in any other form of real property and to income from the alienation of such property."

ARTICLE IV

Paragraph 1 of Article VIII (Transportation) shall be deleted and replaced by the following:

"1. Notwithstanding the provisions of Articles VII (Business Profits), XII (Royalties) and XIII (Gains), profits derived by a resident of a Contracting State from the operation of ships or aircraft in international traffic, and gains derived by a resident of a Contracting State from the alienation of ships, aircraft or containers (including trailers and related equipment for the transport of containers) used principally in international traffic, shall be exempt from tax in the other Contracting State."

ARTICLE V

1. Paragraph 3 of Article XII (Royalties) shall be deleted and replaced by the following:

"3. Notwithstanding the provisions of paragraph 2, copyright royalties and other like payments in respect of the production or reproduction of any literary, dramatic, musical or artistic work (but not including royalties in respect of motion pictures and works on film, videotape or other means of reproduction for use in connection with television) arising in a Contracting State and beneficially owned by a resident of the other Contracting State shall be taxable only in that other State."

2. Paragraph 4 of Article XII (Royalties) shall be deleted and replaced by the following:

"4. The term 'royalties' as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work (including motion pictures and works on film, videotape or other means of reproduction for use in connection with television), any patent, trade mark, design or model, plan, secret formula or process, or for the use of, or the right to use, tangible personal property or for information concerning industrial, commercial or scientific experience, and, notwithstanding the provisions of Article XIII (Gains), includes gains from the alienation of any intangible property or rights described in this paragraph to the extent that such gains are contingent on the productivity, use or subsequent disposition of such property or rights."

3. Subparagraph 6(b) of Article XII (Royalties) shall be deleted and replaced by the following:

"(b) Where the royalties are for the use of, or the right to use, intangible property or tangible personal property in a Contracting State, then such royalties shall be deemed to arise in that State and not in the State of which the payer is a resident."

ARTICLE VI

1. Paragraph 3 of Article XIII (Gains) shall be deleted and replaced by the following:

"3. For the purposes of this Article the term 'real property situated in the other Contracting State'

(a) In the case of real property situated in the United States, means a United States real property interest and real property referred to in Article VI (Income from Real Property) situated in the United States; and

(b) In the case of real property situated in Canada means:

(i) Real property referred to in Article VI (Income from Real Property) situated in Canada;

(ii) A share of the capital stock of a company, the value of whose shares is derived principally from real property situated in Canada; and

(iii) An interest in a partnership, trust or estate, the value of which is derived principally from real property situated in Canada."

2. Paragraph 5 of Article XIII (Gains) shall be deleted and replaced by the following:

"5. The provisions of paragraph 4 shall not affect the right of a Contracting State to levy tax on gains from the alienation of property derived by an individual who is a resident of the other Contracting State if such individual:

(a) Was a resident of the first-mentioned State for 120 months during any period of 20 consecutive years preceding the alienation of the property; and

(b) Was a resident of the first-mentioned State at any time during the ten years immediately preceding the alienation of the property;

and if such property (or property for which such property was substituted in an alienation the gain on which was not recognized for the purposes of taxation in the first-mentioned State) was owned by the individual at the time he ceased to be a resident of the first-mentioned State."

3. Paragraph 9 of Article XIII (Gains) shall be deleted and replaced by the following:

"9. Where a person who is a resident of a Contracting State alienates a capital asset which may in accordance with this Article be taxed in the other Contracting State and

(a) That person owned the asset on September 26, 1980 and was resident in the first-mentioned State on that date; or

(b) The asset was acquired by that person in an alienation of property which qualified as a non-recognition transaction for the purposes of taxation in that other State;

the amount of the gain which is liable to tax in that other State in accordance with this Article shall be reduced by the proportion of the gain attributable on a monthly basis to the period ending on December 31 of the year in which the Convention enters into force, or such greater portion of the gain as is shown to the satisfaction of the competent authority of the other State to be reasonably attributable to that period. For the purposes of this paragraph the term "non-recognition transaction" includes a transaction to which paragraph 8 applies and, in the case of taxation in the United States, a transaction that would have been a non-recognition transaction but for Sections 897(d) and 897(e) of the Internal Revenue Code. The provisions of this paragraph shall not apply to

(c) An asset that on September 26, 1980 formed part of the business property of a permanent establishment or pertained to a fixed base of a resident of a Contracting State situated in the other Contracting State;

(d) An alienation by a resident of a Contracting State of an asset that was owned at any time after September 26, 1980 and before such alienation by a person who was not at all times after that date while the asset was owned by such person a resident of that State; or

(e) An alienation of an asset that was acquired by a person at any time after September 26, 1980 and before such alienation in a transaction other than a non-recognition transaction."

ARTICLE VII

1. Paragraph 3 of Article XVI (Artistes and Athletes) shall be deleted and replaced by the following:

"3. The provisions of paragraphs 1 and 2 shall not apply to the income of:

(a) An athlete in respect of his activities as an employee of a team which participates in a league with regularly schedule games in both Contracting States; or

(b) A team described in subparagraph (a)."

2. There shall be added to Article XVI (Artistes and Athletes) a new paragraph 4, as follows:

"4. Notwithstanding the provisions of Articles XIV (Independent Personal Services) and XV (Dependent Personal Services) an amount paid by a resident of a Contracting State to a resident of the other Contracting State as an inducement to sign an agreement relating to the performance of the services of an athlete (other than an amount referred to in paragraph 1 of Article

XV (Dependent Personal Services)) may be taxed in the first-mentioned State, but the tax so charged shall not exceed 15 per cent of the gross amount of such payment."

ARTICLE VIII

1. The Title of Article XVII shall be deleted and replaced by the following:

"WITHHOLDING OF TAXES IN RESPECT OF PERSONAL SERVICES"

2. Paragraph 2 of Article XVII (Withholding of Taxes in Respect of Personal Services) shall be deleted and replaced by the following:

> "2. Where the competent authority of a Contracting State considers that an amount that would otherwise be deducted or withheld from any amount paid or credited to an individual who is a resident of the other Contracting State in respect of the performance of personal services in the first-mentioned State is excessive in relation to the estimated tax liability for the taxable year of that individual in the first-mentioned State, it may determine that a lesser amount will be deducted or withheld."

ARTICLE IX

1. Paragraph 1 of Article XVIII (Pensions and Annuities) shall be deleted and replaced by the following:

> "1. Pensions and annuities arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State, but the amount of any such pension that would be excluded from taxable income in the first-mentioned State if the recipient were a resident thereof shall be exempt from taxation in that other State."

2. Subparagraph 2(b) of Article XVIII (Pensions and Annuities) shall be deleted and replaced by the following:

> "(b) Annuities may also be taxed in the Contracting State in which they arise and according to the laws of that State; but if a resident of the other Contracting State is the beneficial owner of an annuity payment, the tax so charged shall not exceed 15 per cent of the portion of such payment that would not be excluded from taxable income in the first-mentioned State if the beneficial owner were a resident thereof."

3. Paragraph 6 of Article XVIII (Pensions and Annuities) shall be deleted and replaced by the following:

> "6. Alimony and other similar amounts (including child support payments) arising in a Contracting State and paid to a resident of the other Contracting State shall be taxable as follows:
>
> (a) Such amounts shall be taxable only in that other State;
>
> (b) Notwithstanding the provisions of subparagraph (a), the amount that would be excluded from taxable income in the first-mentioned State if the recipient were a resident thereof shall be exempt from taxation in that other State."

ARTICLE X

Paragraph 2 of Article XXI (Exempt Organizations) shall be deleted and replaced by the following:

> "2. Subject to the provisions of paragraph 3, income referred to in Articles X (Dividends) and XI (Interest) derived by:
>
> (a) A trust, company or other organization which is resident in a Contracting State, generally exempt from tax in a taxable year in that State and constituted and operated exclusively to administer or provide benefits under one or more funds or plans established to provide pension, retirement or other employee benefits; or
>
> (b) A trust, company or other organization which is resident in a Contracting State, not taxed in a taxable year in that State and constituted and operated exclusively to earn income for the benefit of an organization referred to in subparagraph (a); shall be exempt from tax in that taxable year in the other Contracting State."

ARTICLE XI

1. Paragraph 1 of Article XXIV (Elimination of Double Taxation) shall be deleted and replaced by the following:

> "1. In the case of the United States, subject to the provisions of paragraphs 4, 5 and 6, double taxation shall be avoided as follows: In accordance with the provisions and subject to the limitations of the law of the United States (as it may be amended from time to time without changing the general principle hereof), the United States shall allow to a citizen or resident of the United States, or to a company electing to be treated as a domestic corporation, as a credit against the United States tax on income the appropriate amount of income tax paid or accrued to Canada; and, in the case of a company which is a resident of the United States owning at least 10 per cent of the voting stock of a company which is a resident of Canada from which it receives dividends in any taxable year, the United States shall allow as a credit against the United States tax on income the appropriate amount of income tax paid or accrued to Canada by that company with respect to the profits out of which such dividends are paid."

2. Paragraph 2 of Article XXIV (Elimination of Double Taxation) shall be deleted and replaced by the following:

> "2. In the case of Canada, subject to the provisions of paragraphs 4, 5 and 6, double taxation shall be avoided as follows:
>
> (a) Subject to the provisions of the law of Canada regarding the deduction from tax payable in Canada of tax paid in a territory outside Canada and to any subsequent modification of those provisions (which shall not affect the general principle hereof), and unless a greater deduction or relief is provided under the law of Canada, income tax paid or accrued to the United States on profits, income or gains arising in the United States shall be deducted from any Canadian tax payable in respect of such profits, income or gains;
>
> (b) Subject to the provisions of the law of Canada regarding the determination of the exempt surplus of a foreign affiliate and to any subsequent modification of those provisions (which shall not affect the general principle hereof), for the purposes of computing Canadian tax, a company which is a resident of Canada shall be allowed to deduct in computing its taxable income any dividend received by it out of the exempt surplus of a foreign affiliate which is a resident of the United States; and
>
> (c) Notwithstanding the provisions of subparagraph (a), where Canada imposes a tax on gains from the alienation of property that, but for the provisions of paragraph 5 of Article XIII (Gains), would not be taxable in Canada, income tax paid or accrued to the United States on such gains shall be deducted from

any Canadian tax payable in respect of such gains."

3. There shall be added to Article XXIV (Elimination of Double Taxation) a new paragraph 9, as follows:

"9. The provisions of this Article relating to the source of profits, income or gains shall not apply for the purpose of determining a credit against United States tax for any foreign taxes other than income taxes paid or accrued to Canada."

ARTICLE XII

Paragraph 6 of Article XXV (Non-Discrimination) shall be deleted and replaced by the following:

"6. Notwithstanding the provisions of Article XXIV (Elimination of Double Taxation), the taxation on a permanent establishment which a resident of a Contracting State has in the other Contracting State shall not be less favorably levied in the other State than the taxation levied on residents of the other State carrying on the same activities. This paragraph shall not be construed as obliging a Contracting State:

(a) To grant to a resident of the other Contracting State any personal allowances, reliefs and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents; or

(b) To grant to a company which is a resident of the other Contracting State the same tax relief that it provides to a company which is a resident of the first-mentioned State with respect to dividends received by it from a company."

ARTICLE XIII

1. Paragraph 2 of Article XXIX (Miscellaneous Rules) shall be deleted and replaced by the following:

"2. Except as provided in paragraph 3, nothing in the Convention shall be construed as preventing a Contracting State from taxing its residents (as determined under Article IV (Residence)) and, in the case of the United States, its citizens (including a former citizen whose loss of citizenship had as one of its principal purposes the avoidance of tax, but only for a period of ten years following such loss) and companies electing to be treated as domestic corporations, as if there were no convention between the United States and Canada with respect to taxes on income and on capital."

2. Subparagraph 3(a) of Article XXIX (Miscellaneous Rules) shall be deleted and replaced by the following:

"(a) Under paragraphs 3 and 4 of Article IX (Related Persons), paragraphs 6 and 7 of Article XIII (Gains), paragraphs 1, 3, 4, 5 and 6(b) of Article XVIII (Pensions and Annuities), paragraph 5 of Article XXIX (Miscellaneous Rules), paragraphs 3 and 5 of Article XXX (Entry into Force), and Articles XIX (Government Service), XXI (Exempt Organizations), XXIV (Elimination of Double Taxation), XXV (Non-Discrimination) and XXVI (Mutual Agreement Procedure); and"

3. Paragraph 4 of Article XXIX (Miscellaneous Rules) shall be deleted and replaced by the following:

"4. With respect to taxable years not barred by the statute of limitations ending on or before December 31 of the year before the year in which the Social Security Agreement between Canada and the United States (signed in Ottawa on March 11, 1981) enters into force, income from personal services not subject to tax by the United States under this Convention or the 1942 Convention shall not be considered wages or net earnings from self-employment for purposes of social security taxes imposed under the Internal Revenue Code."

4. Paragraph 5 of Article XXIX (Miscellaneous Rules) shall be deleted and replaced by the following:

"5. A beneficiary of a Canadian registered retirement savings plan may elect, under rules established by the competent authority of the United States, to defer United States taxation with respect to any income accrued in the plan but not distributed by the plan, until such time as a distribution is made from such plan, or any plan substituted therefor. The provisions of the preceding sentence shall not apply to income which is reasonably attributable to contributions made to the plan by the beneficiary while he was not a resident of Canada."

5. Paragraph 6 of Article XXIX (Miscellaneous Rules) shall be deleted and replaced by the following:

"6. Notwithstanding any other provision of the Convention,

(a) Where profits, income or gains derived by a trust is to be treated for the purposes of the Convention as income of a resident of a Contracting State, and a principal purpose for the establishment, acquisition or maintenance of the trust was to obtain a benefit under the Convention or the 1942 Convention for persons who are not residents of that State, Articles VI (Income from Real Property) through XXIV (Elimination of Double Taxation) shall not apply in relation to the profits, income or gains of the trust; and

(b) Articles VI (Income from Real Property) through XXIV (Elimination of Double Taxation) shall not apply to non-resident-owned investment corporations as defined under section 133 of the Income Tax Act of Canada, or under any similar provision enacted by Canada after the date of signature of the Protocol."

ARTICLE XIV

Paragraph 3 of Article XXX (Entry into Force) shall be deleted and replaced by the following:

"3. For the purposes of applying the United States foreign tax credit in relation to taxes paid or accrued to Canada:

(a) Notwithstanding the provisions of paragraph 2(a) of Article II (Taxes Covered), the tax on 1971 undistributed income on hand imposed by Part IX of the Income Tax Act of Canada shall be considered to be an income tax for distributions made on or after the first day of January 1972 and before the first day of January 1979 and shall be considered to be imposed upon the recipient of a distribution, in the proportion that the distribution out of undistributed income with respect to which the tax has been paid bears to 85 per cent of such undistributed income;

(b) The principles of paragraph 6 of Article XXIV (Elimination of Double Taxation) shall have effect for taxable years beginning on or after the first day of January 1976; and

(c) The provisions of paragraph 1 of Article XXIV shall have effect for taxable years beginning on or after the first day of January 1981.

Any claim for refund based on the provisions of this paragraph may be filed on or before June 30 of the calendar year following that in which the Convention enters into force, notwithstanding any rule of domestic law to the contrary."

ARTICLE XV

1. This protocol shall be subject to ratification in accordance with the applicable procedures of Canada and the United States and instruments of ratification shall be exchanged at Washington as soon as possible.

2. The Protocol shall enter into force upon the exchange of instruments of ratification and shall have effect in accordance with Article XXX (Entry into Force) of the Convention.

IN WITNESS WHEREOF, the undersigned, being duly authorized thereto by their respective Governments, have signed this Protocol.

Done in two copies at Ottawa this 14th day of June, 1983, in the English and French languages, each text being equally authentic.

FOR THE
GOVERNMENT
OF CANADA
Marc Lalonde

FOR THE
GOVERNMENT
OF THE
UNITED STATES
OF AMERICA
Paul H. Robinson, Jr.

SECOND PROTOCOL AMENDING THE CONVENTION BETWEEN THE UNITED STATES OF AMERICA AND CANADA WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL SIGNED AT WASHINGTON ON SEPTEMBER 26, 1980, AS AMENDED BY THE PROTOCOL SIGNED AT OTTAWA ON JUNE 14, 1983

The United States of America and Canada,

Desiring to conclude a second Protocol to amend the Convention with respect to Taxes on Income and on Capital signed at Washington on September 26, 1980, as amended by the Protocol signed at Ottawa on June 14, 1983 (hereinafter referred to as "the Convention"),

Have agreed as follows:

ARTICLE I

Paragraph 5 of Article XVIII (Pensions and Annuities) of the Convention shall be deleted and replaced by the following:

"5. Benefits under the social security legislation in a Contracting State paid to a resident of the other Contracting State shall be taxable as follows:

"(a) Such benefits shall be taxable only in that other State;

"(b) Notwithstanding the provisions of subparagraph (a), one-half of the total amount of any such benefit paid in a taxable year shall be exempt from taxation in that other State."

ARTICLE II

1. Subparagraph 3(a) of Article XXIX (Miscellaneous Rules) of the Convention shall be deleted and replaced by the following:

"(a) under paragraphs 3 and 4 of Article IX (Related Persons), paragraphs 6 and 7 of Article XIII (Gains), paragraphs 1, 3, 4, 5(b), and 6(b) of Article XVIII (Pensions and Annuities), paragraphs 5 and 7 of Article XXIX (Miscellaneous Rules), paragraphs 3 and 5 of Article XXX (Entry into Force), and Articles XIX (Government Service), XXI (Exempt Organizations), XXIV (Elimination of Double Taxation), XXV (Non-Discrimination), and XXVI (Mutual Agreement Procedure); and"

2. There shall be added to Article XXIX (Miscellaneous Rules) of the Convention a new paragraph 7, as follows:

"7. One-half of the total amount of benefits under the social security legislation in Canada paid in a taxable year to a resident of Canada who is a citizen of the United States shall be exempt from taxation in the United States."

ARTICLE III

1. This Protocol shall be subject to ratification in accordance with the applicable procedures of the United States and Canada and instruments of ratification shall be exchanged as soon as possible.

2. The Protocol shall enter into force upon the exchange of instruments of ratification and shall have effect in accordance with the provisions of Article XXX (Entry into Force) of the Convention.

IN WITNESS WHEREOF, the undersigned, being duly authorized thereto by their respective Governments, have signed this Protocol.

DONE in duplicate at Washington, this 28th day of March 1984, in the English and French languages, the two texts being equally authentic.

FOR THE
GOVERNMENT
OF THE
UNITED STATES
OF AMERICA:
Kenneth W. Dam

FOR THE
GOVERNMENT
OF CANADA:
Allan E. Gotlieb

TECHNICAL EXPLANATION OF THE CONVENTION BETWEEN THE UNITED STATES OF AMERICA AND CANADA WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL SIGNED AT WASHINGTON, D.C. ON SEPTEMBER 26, 1980

INTRODUCTION

In this technical explanation of the Convention between the United States and Canada signed on September 26, 1980 ("the Convention"), references are made to the Convention and Protocol between Canada and the United States with respect to Income Taxes signed on March 4, 1942, as amended by the Convention signed on June 12, 1950, the Convention signed on August 8, 1956 and the Supplementary Convention signed on October 25, 1966 (the "1942 Convention"). These references are intended to put various provisions of the Convention into context. The technical explanation does not, however, provide a complete comparison between the Convention and the 1942 Convention. Moreover, neither the Convention nor the technical explanation is intended to have implications for the interpretation of the 1942 Convention.

The technical explanation is an official guide to the Convention. It reflects policies behind particular Convention provisions, as well as understandings reached with respect to the interpretation and application of the Convention.

Article I. PERSONAL SCOPE

Article I provides that the Convention is generally applicable to persons who are residents of either Canada or the United States or both Canada and the United States. The word "generally" is used because certain provisions of the Convention apply to persons who are residents of neither Canada nor the United States.

Article II. TAXES COVERED

Paragraph 1 states that the Convention applies to taxes "on income and on capital" imposed on behalf of Canada and the United States, irrespective of the manner in which such taxes are levied. As of September 26, 1980 neither Canada nor the United States imposed taxes on capital. Paragraph 1 is not intended either to broaden or to limit paragraph 2, which provides that the Convention shall apply, in the case of Canada, to the taxes imposed by the Government of Canada under Part I, XIII, and XIV of the Income

Tax Act and, in the case of the United States, to the Federal income taxes imposed by the Internal Revenue Code ("the Code").

National taxes not generally covered by the Convention include, in the case of the United States, the estate, gift, and generation-skipping transfer taxes, the Windfall Profits Tax, Federal unemployment taxes, social security taxes imposed under section 1401, 3101, and 3111 of the Code, and the excise tax on insurance premiums imposed under Code section 4371. The Convention also does not generally cover the Canadian excise tax on net insurance premiums paid by residents of Canada for coverage of a risk situated in Canada. However, the Convention has the effect of covering the Canadian social security tax in certain respects because under Canadian domestic tax law no such tax is due if there is no income subject to tax under the Income Tax Act of Canada. Taxes imposed by the states of the United States, and by the provinces of Canada, are not generally covered by the Convention. However, if such taxes are imposed in accordance with the provisions of the Convention, a foreign tax credit is ensured by paragraph 7 of Article XXIV (Elimination of Double Taxation).

Paragraph 2 contrasts with paragraph 1 of the Protocol to the 1942 Convention, which refers to "Dominion income taxes." In addition, unlike the 1942 Convention, the Convention does not contain a reference to "surtaxes and excess-profits taxes."

Paragraph 3 provides that the Convention also applies to any taxes identical or substantially similar to the taxes on income in existence on September 26, 1980 which are imposed in addition to or in place of the taxes existing on that date. Similarly, taxes on capital imposed after that date are to be covered.

It was agreed that Part I of the Income Tax Act of Canada would meet the requirements of paragraph 3(a) if Canada were to enact a low flat rate tax on resource revenues which would not be deductible in computing income under Part I. This agreement is not intended to have implications for any other convention or for the interpretation of Code section 901 and 903. Further, the flat rate tax would not be a tax described in paragraphs 2 or 3. After Canada proposed enactment of an eight percent tax on oil and gas production revenues, it was confirmed that this tax was consistent with the understanding reached during the negotiations.

Paragraph 4 provides that, notwithstanding paragraphs 2 and 3, the Convention applies to certain United States taxes for certain specified purposes: the accumulated earnings tax and personal holding company tax are covered only to the extent necessary to implement the provisions of paragraphs 5 and 8 of Article X (Dividends); the excise taxes imposed with respect to private foundations are covered only to the extent necessary to implement the provisions of paragraph 4 of Article XXI (Exempt Organizations); and the social security taxes imposed under sections 1401, 3101, and 3111 of the Code are covered only to the extent necessary to implement the provisions of paragraph 4 of Article XXIX (Miscellaneous Rules). The pertinent provisions of Articles X, XXI, and XXIX are described below. Canada had no national taxes similar to the United States accumulated earnings tax, personal holding company tax, or excise taxes imposed with respect to private foundations.

Article II does not specifically refer to interest, fines and penalties. Thus, each Contracting State may, in general, impose interest, fines, and penalties or pay interest pursuant to its domestic laws. Any question whether such items are being imposed or paid in connection with covered taxes in a manner consistent with provisions of the Convention, such as Article XXV (Non-Discrimination), may, however, be resolved by the competent authorities pursuant to Article XXVI (Mutual Agreement Procedure). See, however, the discussion below of the treatment of certain interest under Articles XXIX (Miscellaneous Rules) and XXX (Entry Into Force).

Article III. GENERAL DEFINITIONS

Article III provides definitions and general rules of interpretation for the Convention. Paragraph 1(a) states that the term "Canada," when used in a geographical sense, means the territory of Canada, including any area beyond the territorial seas of Canada which, under international law and the laws of Canada, is an area within which Canada may exercise rights with respect to the seabed and subsoil and their natural resources. This definition differs only in form from the definition of Canada in the 1942 Convention; paragraph 1(a) omits the reference in the 1942 Convention to "the Provinces, the Territories and Sable Island" as unnecessary.

Paragraph 1(b)(i) defines the term "United States" to mean the United States of America. The term does not include Puerto Rico, the Virgin Islands, Guam, or any other United States possession or territory.

Paragraph 1(b)(ii) states that when the term "United States" is used in a geographical sense the term also includes any area beyond the territorial seas of the United States which, under international law and the laws of the United States, is an area within which the United States may exercise rights with respect to the seabed and subsoil and their natural resources.

Paragraph 1(c) defines the term "Canadian tax" to mean the taxes imposed by the Government of Canada under Parts I, XIII, and XIV of the Income Tax Act as in existence on September 26, 1980 and any identical or substantially similar taxes on income imposed by the Government of Canada after that date and which are in addition to or in place of the then existing taxes. The term does not extend to capital taxes, if and when such taxes are ever imposed by Canada.

Paragraph 1(d) defines the term "United States tax" to mean the Federal income taxes imposed by the Internal Revenue Code as in existence on September 26, 1980 and any identical or substantially similar taxes on income imposed by the United States after that date in addition to or in place of the then existing taxes. The term does not extend to capital taxes, nor to the United States taxes identified in paragraph 4 of Article II (Taxes Covered).

Paragraph 1(e) provides that the term "person" includes an individual, an estate, a trust, a company, and any other body of persons. Although both the United States and Canada do not regard partnerships as taxable entities, the definition in the paragraph is broad enough to include partnerships where necessary.

Paragraph 1(f) defines the term "company" to mean any body corporate or any entity which is treated as a body corporate for tax purposes.

The term "competent authority" is defined in paragraph 1(g) to mean, in the case of Canada, the Minister of National Revenue or his authorized representative and, in the case of the United States, the Secretary of the Treasury or his delegate. The Secretary of the Treasury has delegated the general authority to act as competent authority to the Commissioner of the Internal Revenue Service, who has redelegated such authority to the Assistant Commissioner (Compliance) with the concurrence, in certain cases, of the Assistant Commissioner (Technical). The Assistant Commissioner (Compliance) has redelegated authority to the Director of International Operations to administer programs for routine and specific exchanges of information and mutual assistance in collection and to the Director, Examination Division, to administer programs for simultaneous and industrial exchanges of information.

Paragraph 1(h) defines the term "international traffic" to mean any voyage of a ship or aircraft to transport passengers or property, except where the principal purpose of the voyage is transport between points within a Contracting State. A voyage of a ship or aircraft that includes stops in both Contracting States may thus not be international traffic if the principal purpose of the voyage is to transport passengers or property within a Contracting State.

Paragraph 1(i) defines the term "State" to mean any national State, whether or not a Contracting State.

Paragraph 1(j) establishes "the 1942 Convention" as the term to be used throughout the Convention for referring to the pre-existing income tax treaty relationship between the United States and Canada.

Paragraph 2 provides that, in the case of a term not defined in the Convention, the domestic tax law of the Contracting State applying to the Convention shall control, unless the context in which the term is used requires a definition independent of domestic tax law or the competent authorities reach agreement on a meaning pursuant to Article XXVI (Mutual Agreement Procedure). The term "context" refers to the purpose and background of the provision in which the term appears.

Pursuant to the provisions of Article XXVI, the competent authorities of the Contracting States may resolve any difficulties or doubts as to the interpretation or application of the Convention. An agreement by the competent authorities with respect to the meaning of a term used in the Convention would supersede conflicting meanings in the domestic laws of the Contracting States.

Article IV. RESIDENCE

Article IV provides a detailed definition of the term "resident of a Contracting State." The definition begins with a person's liability to tax as a resident under the respective taxation laws of the Contracting States. A person who, under those laws, is a resident of one Contracting State and not the other need look no further. However, the Convention definition is also designed to assign residence to one State or the other for purposes of the Convention in circumstances where each of the Contracting States believes a person to be its resident. The Convention definition is, of course, exclusively for purposes of the Convention.

Paragraph 1 provides that the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management, place of incorporation, or any other criterion of a similar nature. The phrase "any other criterion of a similar nature" includes, for U.S. purposes, an election under the Code to be treated as a U.S. resident. An estate or trust is, however, considered to be a resident of a Contracting State only to the extent that income derived by such estate or trust is liable to tax in that State either in its hands or in the hands of its beneficiaries. To the extent that an estate or trust is considered a resident of a Contracting State under this provision, it can be a "beneficial owner" of items of income specified in other articles of the Convention—e.g., paragraph 2 of Article X (Dividends).

Paragraphs 2, 3, and 4 provide rules to determine a single residence for purposes of the Convention for persons resident in both Contracting States under the rules set forth in paragraph 1. Paragraph 2 deals with individuals. A "dual resident" individual is initially deemed to be a resident of the Contracting State in which he has a permanent home available to him. If the individual has a permanent home available to him in both States or in neither, he is deemed to be a resident of the Contracting State with which his personal and economic relations are closer. If the personal and economic relations of an individual are not closer to one Contracting State than to the other, the individual is deemed to be a resident of the Contracting State in which he has an habitual abode. If he has such an abode in both States or in neither State, he is deemed to be a resident of the Contracting State of which he is a citizen. If the individual is a citizen of both States or of neither, the competent authorities are to settle the status of the individual by mutual agreement.

Paragraph 3 provides that if, under the provisions of paragraph 1, a company is a resident of both Canada and the United States, then it shall be deemed to be a resident of the State under whose laws (including laws of political subdivisions) it was created. Paragraph 3 does not refer to the State in which a company is organized, thus making clear that the tie-breaker rule for a company is controlled by the State of the company's original creation. Various jurisdictions may allow local incorporation of an entity that is already organized and incorporated under the laws of another country. Paragraph 3 provides certainty in both the United States and Canada with respect to the treatment of such an entity for purposes of the Convention.

Paragraph 4 provides that where, by reason of the provisions of paragraph 1, an estate, trust, or other person, other than an individual or a company, is a resident of both Contracting States, the competent authorities of the States shall by mutual agreement endeavor to settle the question and determine the mode of application of the Convention to such person. This delegation of authority to the competent authorities complements the provisions of Article XXVI (Mutual Agreement Procedure), which implicitly grant such authority.

Paragraph 5 provides a special rule for certain government employees, their spouses, and dependent children. An individual is deemed to be a resident of a Contracting State if he is an employee of that State or of a political subdivision, local authority, or instrumentality of that State, is rendering services in the discharge of functions of a governmental nature in any State, and is subjected in the first-mentioned State to "similar obligations" in respect of taxes on income as are residents of the first-mentioned State. Paragraph 5 provides further that a spouse and dependent children residing with a government employee and also subject to "similar obligations" in respect of income taxes as residents of the first-mentioned State are also deemed to be residents of that State. Paragraph 5 overrides the normal tie-breaker rule of paragraph 2. A U.S. citizen or resident who is an employee of the U.S. government in a foreign country or who is a spouse or dependent of such employee is considered to be subject in the United States to "similar obligations" in respect of taxes on income as those imposed on residents of the United States, notwithstanding that such person may be entitled to the benefits currently allowed by sections 911, 912, or 913 of the Code.

Article V. PERMANENT ESTABLISHMENT

Paragraph 1 provides that for the purposes of the Convention the term "permanent establishment" means a fixed place of business through which the business of a resident of a Contracting State is wholly or partly carried on. Article V does not use the term "enterprise of a Contracting State," which appears in the 1942 Convention. Thus, paragraph 1 avoids introducing an additional term into the Convention. The omission of the term is not intended to have any implications for the interpretation of the 1942 Convention.

Paragraph 2 provides that the term "permanent establishment" includes especially a place of management, a branch, an office, a factory, a workshop, and a mine, oil or gas well, quarry, or any other place of extraction of natural resources. Paragraph 3 adds that a building site or construction or installation project constitutes a permanent establishment if and only if it lasts for more than 12 months. Paragraph 4 provides that a permanent establishment exists in a Contracting State if the use of a drilling rig or drilling ship in that State to explore for or exploit natural resources lasts for more than 3 months in any 12 month period, but not if such activity exists for a lesser period of time.

Paragraph 5 provides that a person acting in a Contracting State on behalf of a resident of the other Contracting State is deemed to be a permanent establishment of the resident if such person has and habitually exercises in the first-mentioned State the authority to conclude contracts in the name of the resident. This rule does not apply to an agent of independent status, covered by paragraph 7. Under the provisions of paragraph 5, a permanent establishment may exist even in the absence of a fixed place of business. If, however, the activities of a person described in paragraph 5 are limited to the ancillary activities described in paragraph 6, then a permanent establishment does not exist solely on account of the person's activities.

There are a number of minor differences between the provisions of paragraphs 1 through 5 and the analogous provisions of the 1942 Convention. One important deviation is elimination of the rule of the 1942 Convention which deems a permanent establishment to exist in any circumstance where a resident of one State uses substantial equipment in the other State for any period of time. The Convention thus generally raises the threshold for source basis taxation of activities that involve substantial equipment (and that do not otherwise constitute a permanent establishment). Another deviation of some significance is elimination of the rule of the 1942 Convention that considers a permanent establishment to exist where a resident of one State carries on business in the other State through an agent or employee who has a stock of merchandise from which he regularly fills orders that he receives. The convention provides that a person other than an agent of independent status who is engaged solely in the maintenance of a stock of goods or merchandise belonging to a resident of the other State for the purpose of storage, display or delivery does not constitute a permanent establishment.

Paragraph 6 provides that a fixed place of business used solely for, or an employee described in paragraph 5 engaged solely in, certain specified activities is not a permanent establishment, notwithstanding the provisions of paragraphs 1, 2, and 5. The specified activities are: a) the use of facilities for the purpose of storage, display, or delivery of goods or merchandise belonging to the resident whose business is being carried on; b) the maintenance of a stock of goods or merchandise belonging to the resident for the purpose of storage, display, or delivery; c) the maintenance of a stock of goods or merchandise belonging to the resident for the purpose of processing by another person; d) the purchase of goods or merchandise, or the collection of information, for the resident; and e) advertising, the supply of information, scientific research, or similar activities which have a preparatory or auxiliary character, for the resident. Combinations of the specified activities have the same status as any one of the activities. The reference in paragraph 6(e) to specific activities does not imply that any other particular activities—for example, the servicing of a patent or a know-how contract or the inspection of the implementation of engineering plans—do not fall within the scope of paragraph 6(e) provided that, based on the facts and circumstances, such activities have a preparatory of auxiliary character.

Paragraph 7 provides that a resident of a Contracting State is not deemed to have a permanent establishment in the other Contracting State merely because such resident carries on business in the other State through a broker, general commission agent, or any other agent of independent status, provided that such persons are acting in the ordinary course of their business.

Paragraph 8 states that the fact that a company which is a resident of one Contracting State controls or is controlled by a company which is either a resident of the other Contracting State, whether through a permanent establishment or otherwise, does not automatically render either company a permanent establishment of the other.

Paragraph 9 provides that, for purposes of the Convention, the provisions of Article V apply in determining whether any person has a permanent establishment in any State. Thus, these provisions would determine whether a person other than a resident of Canada or the United States has a permanent establishment in Canada or the United States, and whether a person resident in Canada or the United States has a permanent establishment in a third State.

Article VI. INCOME FROM REAL PROPERTY

Paragraph 1 provides that income derived by a resident of a Contracting State from real property situated in the other Contracting State may be taxed by that other State. Income from real property includes, for purposes of Article VI, income from agriculture or forestry. Also, while "income derived . . . from real property" includes income from rights such as an overriding royalty or a net profits interest in a natural resource, it does not include income in the form of rights to explore for or exploit natural resources which a party receives as compensation for services (e.g., exploration services); the latter income is subject to the provisions of Article VII (Business Profits), XIV (Independent Personal Services), or XV (Dependent Personal Services), as the case may be. As provided by paragraph 3, paragraph 1 applies to income derived from the direct use, letting or use in any other form of real property and to income from the alienation of such property.

Generally speaking, the term "real property" has the meaning which it has under the taxation laws of the Contracting State in which the property in question is situated, in accordance with paragraph 2. In any case, the term includes any option or similar right in respect of real property, the usufruct of real property, and rights to explore for or to exploit mineral deposits, sources, and other natural resources. The reference to "rights to explore for or to exploit mineral deposits, sources and other natural resources" includes rights generating either variable or fixed payments. The term "real property" does not include ships and aircraft.

Unlike Article XIII A of the 1942 Convention, Article VI does not contain an election to allow a resident of a Contracting State to compute tax on income from real property situated in the other State on a net basis. Both the Internal Revenue Code and the Income Tax Act of Canada generally allow for net basis taxation with respect to real estate rental income, although Canada does not permit such an election for natural resource royalties. Also, unlike the 1942 Convention which in Article XI imposes a 15 percent limitation on the source basis taxation of rental or royalty income from real property, Article VI of the Convention allows a Contracting State to impose tax on such income under its internal law. In Canada the rate of tax on resource royalties is 25 percent of the gross amount of the royalty, if the income is not attributable to a permanent establishment in Canada under the Convention.

Article VII. BUSINESS PROFITS

Paragraph 1 provides that business profits of a resident of a Contracting State are taxable only in that State unless the resident carries on business in the other Contracting State through a permanent establishment situated in that other State. If the resident carries on, or has carried on, business through such a permanent establishment, the other State may tax such business profits but only so much of them as are attributable to the permanent establishment. The reference to a prior permanent establishment ("or has carried on") makes clear that a Contracting State in which a permanent establishment existed has the right to tax the business profits attributable to that permanent establishment, even if there is a delay in the receipt or accrual of such profits until after the permanent establishment has been terminated.

Any business profits received or accrued in taxable years in which the Convention has effect, in accordance with Article XXX (Entry Into Force), which are attributable to a permanent establishment that was previously terminated are subject to tax in the Contracting State in which such permanent establishment existed under the provisions of Article VII.

Paragraph 2 provides that where a resident of either Canada or the United States carries on business in the other Contracting State through a permanent establishment in that other State, both Canada and the United States shall attribute to that permanent establishment business profits which the permanent establishment might be expected to make if it were a distinct and separate person engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the resident and with any other person related to the resident. The term "related to the resident" is to be interpreted in accordance with paragraph 2 of Article IX (Related Persons). The reference to other related persons is intended to make clear that the test of paragraph 2 is not restricted to independence between a permanent establishment and a home office.

Paragraph 3 provides that, in determining business profits of a permanent establishment, there are to be allowed as deductions those expenses which are incurred for the purposes of the permanent establishment, including executive and administrative expenses, whether incurred in the State in which the permanent establishment is situated or in any other State. However, nothing in the paragraph requires Canada or the United States to allow a deduction for any expenditure which would not generally be allowed as a deduction under its taxation laws. The language of this provision differs from that of paragraph 1 of Article III of the 1942 Convention, which states that in the determination of net industrial and commercial profits of a permanent establishment there shall be allowed as deductions "all expenses, wherever incurred" as long as such expenses are reasonably allocable to the permanent establishment. Paragraph 3 of Article VII of the Convention is not intended to have any implications for interpretation of the 1942 Convention, but is intended to assure that under the Convention deductions are allowed by a Contracting State which are generally allowable by that State.

Paragraph 4 provides that no business profits are to be attributed to a permanent establishment of a resident of a Contracting State by reason of the use of the permanent establishment for merely purchasing goods or merchandise or merely providing executive, managerial, or administrative facilities or services for the resident. Thus, if a company resident in a Contracting State has a permanent establishment in the other State, and uses the permanent establishment for the mere performance of stewardship of other managerial services carried on for the benefit of the resident, this activity will not result in profits being attributed to the permanent establishment.

Paragraph 5 provides that business profits are to be attributed to a permanent establishment by the same method in every taxable period unless there is good and sufficient reason to change such method. In the United States, such a change may be a change in accounting method requiring the approval of the Internal Revenue Service.

Paragraph 6 explains the relationship between the provisions of Article VII and other provisions of the Convention. Where business profits include items of income which are dealt with separately in other Articles of the Convention, those other Articles are controlling.

Paragraph 7 provides a definition for the term "attributable to." Profits "attributable to" a permanent establishment are those derived from the assets or activities of the permanent establishment. Paragraph 7 does not preclude Canada or the United States from using appropriate domestic tax law rules of attribution. The "attributable to" definition does not, for example, preclude a taxpayer from using the rules of section 1.864-4(c)(5) of the Treasury Regulations to assure for U.S. tax purposes that interest arising in the United States is attributable to a permanent establishment in the United States. (Interest arising outside the United States is attributable to a permanent establishment in the United States based on the principles of Regulations sections 1.864-5 and 1.864-6 and Revenue Ruling 75-253, 1975-2 C.B. 203.) Income that would be taxable under the Code and that is "attributable to" a permanent establishment under paragraph 7 is taxable pursuant to Article VII, however, even if such income might under the Code be treated as fixed or determinable annual or periodical gains or income not effectively connected with the conduct of a trade or business within the United States. The "attributable to" definition means that the limited "force-of-attraction" rule of Code section 864(c)(3) does not apply for U.S. tax purposes under the Convention.

Article VIII. TRANSPORTATION

Paragraph 1 provides that profits derived by a resident of a Contracting State from the operation of ships or aircraft in international traffic are exempt from tax in the other Contracting State, even if, under Article VII (Business Profits), such profits are attributable to a permanent establishment. Paragraph 1 also provides that gains derived by a resident of a Contracting State from the alienation of ships or aircraft used principally in international traffic are exempt from tax in the other Contracting State even if, under Article XIII (Gains), those gains would be taxable in that other State. These rules differ from Article V of the 1942 Convention, which conditions the exemption in the State of source on registration of the ship or aircraft in the other State.

Paragraph 2(a) provides that profits covered by paragraph 1 include profits from the rental of ships or aircraft operated in international traffic. Such rental profits are included whether the rental is on a time, voyage, or bareboat basis, and irrespective of the State of residence of the operator.

Paragraph 2(b) provides that profits covered by paragraph 1 include profits derived from the use, maintenance or rental of containers, including trailers and related equipment for the transport of containers, if such containers are used in international traffic.

Paragraph 2(c) provides that profits covered by paragraph 1 include profits derived by a resident of a Contracting State from the rental of ships, aircraft, or containers (including trailers and related equipment for the transport of containers), even if not operated in international traffic, as long as such profits are incidental to profits of such person referred to in paragraphs 1, 2(a), or 2(b).

To the extent that profits described in paragraph 2 would also fall within Article XII (Royalties) (e.g., rent from the lease of a container), the provisions of Article VIII are controlling.

Paragraph 3 states that profits derived by a resident of a Contracting State from a voyage of a ship where the principal purpose of the voyage is to transport passengers or property between points in the other Contracting State is taxable in that other State, whether or not the resident maintains a permanent establishment there. Paragraph 3 overrides the provisions of Article VII. Profits from such a voyage do not qualify for exemption under Article VIII by virtue of the definition of "international traffic" in paragraph 1(h) of Article III (General Definitions). However, profits from a similar voyage by aircraft are taxable in the Contracting State of source only if the profits are attributable to a permanent establishment maintained in that State.

Paragraph 4 provides that profits derived by a resident of a Contracting State engaged in the operation of motor vehicles or a railway as a common carrier or contract carrier, and attributable to the transportation of passengers or property between a point outside the other Contracting State and any other point are exempt from tax in that other State. In addition, profits of such a person from the rental of motor vehicles (including trailers) or railway rolling stock, or from the use, maintenance, or rental of containers (including trailers and related equipment for the transport of containers) used to transport passengers or property between a point outside the other Contracting State and any other point are exempt from tax in that other State.

Paragraph 5 provides that a resident of a Contracting State that participates in a pool, a joint business, or an international operating agency is subject to the provisions of paragraphs 1, 3, and 4 with respect to the profits or gains referred to in paragraphs, 1, 3, and 4.

Paragraph 6 states that profits derived by a resident of a Contracting State from the use, maintenance, or rental of railway rolling stock, motor vehicles, trailers, or containers (including trailers and related equipment for the transport of containers) used in the other Contracting State for a period not expected to exceed 183 days in the aggregate in any 12-month period are exempt from tax in that other State except to the extent that the profits are attributable to a permanent establishment, in which case the State of source has the right to tax under Article VII. The provisions of paragraph 6, unlike the provisions of paragraph 4, apply whether or not the resident is engaged in the operation of motor vehicles or a railway as a common carrier or contract carrier. Paragraph 6 overrides the provisions of Article XII (Royalties), which would otherwise permit taxation in the State of source in the circumstances described.

Gains from the alienation of motor vehicle and railway rolling stock derived by a resident of a Contracting State are not affected by paragraph 4 or 6. Such gains would be taxable in the other Contracting State, however, only if the motor vehicles or rolling stock formed part of a permanent establishment maintained there. See paragraphs 2 and 4 of Article XIII.

Article IX. RELATED PERSONS

Paragraph 1 authorizes Canada and the United States, as the case may be, to adjust the amount of income, loss, or tax payable by a person with respect to arrangements between that person and a related person in the other Contracting State. Such adjustment may be made when arrangements between related persons differ from those that would obtain between unrelated persons. The term "person" encompasses a company resident in a third State with, for example, a permanent establishment in a Contracting State.

Paragraph 2 provides that, for the purposes of Article IX, a person is deemed to be related to another person if either participates directly or indirectly in the management or control of the other or if any third person or persons participate directly or indirectly in the management or control of both. Thus, if a resident of any State controls directly or indirectly a company resident in Canada and a company resident in the United States, such companies are considered to be related persons for purposes of Article IX. Article IX and the definition of "related person" in paragraph 2 may encompass situations that would not be covered by provisions in the domestic laws of the Contracting States. Nor is the paragraph 2 definition controlling for the definition of "related person" or similar terms appearing in other Articles of the Convention. Those terms are defined as provided in paragraph 2 of Article III (General Definitions).

Paragraph 3 provides that where, pursuant to paragraph 1, an adjustment is made or to be made by a Contracting State, the other Contracting State shall make a corresponding adjustment to the income, loss, or tax of the related person in that other State, provided that the other State agrees with the adjustment and, within six years from the end of the taxable year of the person in the first State to which the adjustment relates, the competent authority of the other State has been notified in writing of the adjustment. The reference to an adjustment which "is made or to be made" does not require a Contracting State to formally propose an adjustment before paragraph 3 becomes pertinent. The notification required by paragraph 3 may be made by any of the related persons involved or by the competent authority of the State which makes or is to make the initial adjustment. The notification must give details regarding the adjustment sufficient to apprise the competent authority receiving the notification of the nature of the adjustment. If the requirements of paragraph 3 are complied with, the corresponding adjustment will be made by the other Contracting State notwithstanding any time or procedural limitations in the domestic law of that State.

Paragraph 4 provides that in a case where the other Contracting State has not been notified as provided in paragraph 3 and if the person whose income, loss, or tax is being adjusted has not received notification of the adjustment within five and one-half years from the end of its taxable year to which the adjustment relates, such adjustment shall not be made to the extent that the adjustment would give rise to double taxation between the United States and Canada. Again, the notification referred to in this paragraph need not be a formal adjustment, but it must be in writing and must contain sufficient details to permit the taxpayer to give the notification referred to in paragraph 3.

If, for example, the Internal Revenue Service proposes to make an adjustment to the income of a U.S. company pursuant to Code section 482, and the adjustment involves an allocation of income from a related Canadian company, the competent authority of Canada must receive written notification of the proposed IRS adjustment within six years from the end of the taxable year of the U.S. company to which the adjustment relates. If such notification is not received in timely fashion and if the U.S. company does not receive written notification of the adjustment from the IRS within 5½ years from the end of its relevent taxable year, the IRS will unilaterally recede on the proposed section 482 adjustment to the extent that this adjustment would otherwise give rise to double taxation between the United States and Canada. The Internal Revenue Service will determine whether and to what extent the adjustment would give rise to double taxation with respect to income arising in Canada by examining the relevant facts and circumstances such as the amount of foreign tax credits attributable to Canadian taxes paid by the U.S. company, includng any carryovers and credits for deemed paid taxes.

Paragraph 5 provides that neither a corresponding adjustment described in paragraph 3 nor the cancelling of an adjustment described in paragraph 4 will be made in any case of fraud, willful default, neglect, or gross negligence on the part of the taxpayer or any related person.

Paragraphs 3 and 4 of Article IX are exceptions to the "saving clause" contained in paragraph 2 of Article XXIX (Miscellaneous Rules), as provided in paragraph 3(a) of Article XXIX. Paragraphs 3 and 4 of Article IX apply to adjustments made or to be made with respect to taxable years for which the Convention has effect as provided in paragraphs 2 and 5 of Article XXX (Entry Into Force).

Article X. DIVIDENDS

Paragraph 1 allows a Contracting State to impose tax on its residents with respect to dividends paid by a company which is a resident of the other Contracting State.

Paragraph 2 limits the amount of tax that may be imposed on such dividends by the Contracting State in which the company paying the dividends is resident if the beneficial owner of the dividends is a resident of the other Contracting State. The limitation is 10 percent of the gross amount of the dividends if the beneficial owner is a company that owns 10 percent or more of the voting stock of the company paying the dividends; and 15 percent of the gross amount of the dividends in all other cases. Paragraph 2 does not impose any restrictions with respect to taxation of the profits out of which the dividends are paid.

Paragraph 3 defines the term "dividends," as the term is used in this Article. Each Contracting State is permitted to apply its domestic law rules for differentiating dividends from interest and other disbursements.

Paragraph 4 provides that the limitations of paragraph 2 do not apply if the beneficial owner of the dividends carries on business in the State in which the company paying the dividends is a resident through a permanent establishment or fixed base situated there, and the stockholding in respect of which the dividends are paid is effectively connected with such permanent establishment or fixed base. In such a case, the dividends are taxable pursuant to the provisions of Article VII (Business Profits) or Article XIV (Independent Personal Services), as the case may be. Thus, dividends paid in respect of holdings forming part of the assets of a permanent establishment or fixed base or which are otherwise effectively connected with such permanent establishment or fixed base (i.e., dividends attributable to the permanent establishment or fixed base) will be taxed on a net basis using the rates and rules of taxation generally applicable to residents of the State in which the permanent establishment or fixed base is situated.

Paragraph 5 imposes limitations on the right of Canada or the United States, as the case may be, to impose tax on dividends paid by a company which is a resident of the other Contracting State. The State in which the company is not resident may not tax such dividends except insofar as they are paid to a resident of that State or the holding in respect of which the dividends are paid is effectively connected with a permanent establishment or fixed base in that State. In the case of the United States, such dividends may also be taxed in the hands of a U.S. citizen and certain former citizens, pursuant to the "saving clause" of paragraph 2 of Article XXIX (Miscellaneous Rules). In addition, the Contracting State in which the company is not resident may not subject such company's undistributed profits to any tax. See, however, paragraphs 6, 7, and 8 which, in certain circumstances, qualify the rules of paragraph 5. Neither paragraph 5 nor any other provision of the Convention restricts the ability of the United States to apply the provisions of the Code concerning foreign personal holding companies and controlled foreign corporations.

Paragraph 6 provides that, notwithstanding paragraph 5, a Contracting State in which is maintained a permanent establishment or permanent establishments of a company resident in the other Contracting State may impose tax on such company's earnings, in addition to the tax that would be charged on the earnings of a company resident in that State. The additional tax may not, however, exceed 10 percent of the amount of the earnings which have not been subjected to such additional tax in previous taxation years. Thus, Canada, which has a branch profits tax in force, may impose that tax up to the 10 percent limitation in the case of a United States company with one or more permanent establishments in Canada. This branch profits tax may be imposed notwithstanding other rules of the Convention, including paragraph 6 of Article XXV (Non-Discrimination).

For purposes of paragraph 6, the term "earnings" means the excess of business profits attributable to all permanent establishments for a year and previous years over the sum of: a) business losses attributable to such permanent establishments for such years; b) all taxes on profits, whether or not covered by the Convention (e.g., provincial taxes on profits and provincial resource royalties (which Canada considers "taxes") in excess of the mineral resource allowance provided for under the law of Canada), other than the additional tax referred to in paragraph 6; c) profits reinvested in such State; and d) $500,000 (Canadian, or its equivalent in U.S. dollars) less any amounts deducted under paragraph 6(d) with respect to the same or a similar business by the company or an associated company. The deduction under paragraph 6(d) is available as of the first year for which the Convention has effect, regardless of the prior earnings and tax expenses, if any, of the permanent establishment. The $500,000 deduction is taken into account after other deductions, and is permanent. For the purpose of paragraph 6, references to business profits and business losses gains and losses from the alienation of property forming part of the business property of a permanent establishment. The term "associated company" includes a company which directly or indirectly controls another company or two companies directly or indirectly controlled by the same person or persons, as well as any two companies that deal with each other not at arm's length. This definition differs from the definition of "related persons" in paragraph 2 of Article IX (Related Persons).

Paragraph 7 provides that, notwithstanding paragraph 5, a Contracting State that does not impose a branch profits tax as described in paragraph 6 (i.e., under current law, the United States) may tax a dividend paid by a company which is a resident of the other Contracting State if at least 50 percent of the company's gross income from all sources was included in the computation of business profits attributable to one or more permanent establishments which such company had in the first-mentioned State. The dividend subject to such a tax must, however, be attributable to profits earned by the company in taxable years beginning after September 26, 1980 and the 50 percent test must be met for the three-year period preceding the taxable year of the company in which the dividend is declared (including years ending on or before September 26, 1980) or such shorter period as the company had been in existence prior to that taxable year. Dividends will be deemed to be distributed, for purposes of paragraph 7, first out of profits of the taxation year of the company in which the distribution is made and then out of the profits of the preceding year or years of the company. Paragraph 7 provides further that if a resident of the other Contracting state is the beneficial owner of such dividends, any tax imposed under paragraph 7 is subject to the 10 or 15 percent limitation of paragraph 2 or the rules of paragraph 4 (providing for dividends to be taxed as business profits or income from independent personal services), as the case may be.

Paragraph 8 provides that, notwithstanding paragraph 5, a company which is a resident of Canada and which, absent the provisions of the Convention, has income subject to tax by the United States may be liable for the United States accumulated earnings tax and personal holding company tax. These taxes can be applied, however, only if 50 percent or more in value of the outstanding voting shares of the company is owned, directly or indirectly, throughout the last half of its taxable year by residents of a third State or by citizens or residents of the United States, other than citizens of Canada who are resident in the United States but who either do not have immigrant status in the United States or who have not been resident in the United States for more than three taxable years. The accumulated earnings tax is applied to accumulated taxable income calculated without the benefits of the Convention. Similarly, the personal holding company tax is applied to undistributed personal holding company income computed as if the Convention had not come into force.

Article X does not apply to dividends paid by a company which is not a resident of either Contracting State. Such dividends, if they are income of a resident of one of the Contracting States, are subject to tax as provided in Article XXII (Other Income).

Article XI. INTEREST

Paragraph 1 allows interest arising in Canada or the United States and paid to a resident of the other State to be taxed in the latter State. Paragraph 2 provides that such interest may also be taxed in the Contracting State where it arises, but if a resident of the other Contracting State is the beneficial owner, the tax imposed by the State of source is limited to 15 percent of the gross amount of the interest.

Paragraph 3 provides a number of exceptions to the right of the source State to impose a 15 percent tax under paragraph 2. The following types of interest beneficially owned by a resident of a Contracting State are exempt from tax in the State of source: [illegible]) interest beneficially owned by a Contracting State, a political subdivision, or a local authority thereof, or an instrumentality of such State, subdivision, or authority, which interest is not subject to tax by such state; b) interest beneficially owned by a resident of a Contracting State and paid with respect to debt obligations issued at arm's length which are guaranteed or insured by such State or a political subdivision thereof, or by an instrumentality of such State or subdivision (not by a local authority or an instrumentality thereof), but only if the guarantor or insurer is not subject to tax by that State; c) interest paid by a Contracting State, a political subdivision, or a local authority thereof, or by an instrumentality of such State, subdivision, or authority, but only if the payor is not subject to tax by such State; and d) interest beneficially owned by a seller of equipment, merchandise, or services, but only if the interest is paid in connection with a sale on credit of equipment, merchandise, or services and the sale was made at arm's length. Whether such a transaction is made at arm's length will be determined in the United States under the facts and circumstances. The relationship between the parties is a factor, but not the only factor, taken into account in making this determination. Furthermore, interest paid by a company resident in the other Contracting State with respect to an obligation entered into before September 26, 1980 is exempt from tax in the State of source (irrespective of the State of residence of the beneficial owner), provided that such interest would have been exempt from tax in the Contracting State of source under Article XII of the 1942 Convention. Thus, interest paid by a United States corporation whose business is not managed and controlled in Canada to a recipient not resident in Canada or to a corporation not managed and controlled in Canada would be exempt from Canadian tax as long as the debt obligation was entered into before September 26, 1980. The phrase "not subject to tax by that . . . State" in paragraph 3(a), (b), and (c) refers to taxation at the Federal levels of Canada and the United States.

The phrase "obligation entered into before the date of signature of this Convention" means: (1) any obligation under which funds were dispersed prior to September 26, 1980; (2) any obligation under which funds are dispersed on or after September 26, 1980, pursuant to a written contract binding prior to and on such date, and at all times thereafter until the obligation is satisfied; or (3) any obligation with respect to which, prior to September 26, 1980, a lender had taken every action to signify approval under procedures ordinarily employed by such lender in similar transactions and had sent or deposited for delivery to the person to whom the loan is to be made written evidence of such approval in the form of a document setting forth, or referring to a document sent by the person to whom the loan is to be made that sets forth, the principal terms of such loan.

Paragraph 4 defines the term "interest," as used in Article XI, to include, among other things, debt claims of every kind as well as income assimilated to income from money lent by the taxation laws of the Contracting State in which the income arises. In no event, however, is income dealt with in Article X (Dividends) to be considered interest.

Paragraph 5 provides that neither the 15 percent limitation on tax in the Contracting State of source provided in paragraph 2 nor the various exemptions from tax in such State provided in paragraph 3 apply if the beneficial owner of the interest is a resident of the other Contracting State carrying on business in the State of source through a permanent establishment or fixed base, and the debt claim in respect of which the interest is paid is effectively connected with such permanent establishment or fixed base (i.e., the interest is attributable to the permanent establishment or fixed base). In this case, interest income is to be taxed in the Contracting State of source as business profits—that is, on a net basis.

Paragraph 6 establishes the source of interest for purposes of Article XI. Interest is considered to arise in a Contracting State if the payer is that State, or a political subdivision, local authority, or resident of that State. However, in cases where the person paying the interest, whether a resident of a Contracting State or of a third State, has in a State other than that of which he is a resident a permanent establishment or fixed base in connection with which the indebtedness on which the interest was paid was incurred, and such interest is borne by the permanent establishment or fixed base, then such interest is deemed to arise in the State in which the permanent establishment or fixed base is situated and not in the State of the payer's residence. Thus, pursuant to paragraphs 6 and 2, and Article XXII (Other Income), Canadian tax will not be imposed on interest paid to a U.S. resident by a company resident in Canada if the indebtedness is incurred in connection with, and the interest is borne by, a permanent establishment of the company situated in a third State. "Borne by" means allowable as a deduction in computing taxable income.

Paragraph 7 provides that in cases involving special relationships between persons Article XI does not apply to amounts in excess of the amount which would have been agreed upon between persons having no special relationship; any such excess amount remains taxable according to the laws of Canada and the United States, consistent with any revelant provisions of the Convention.

Paragraph 8 restricts the right of a Contracting State to impose tax on interest paid by a resident of the other Contracting State. The first State may not impose any tax on such interest except insofar as the interest is paid to a resident of that State or arises in that State or the debt claim in respect of which the interest is paid is effectively connected with a permanent establishment or fixed base situated in that State. Thus, pursuant to paragraph 8 the United States has agreed not to impose tax on certain interest paid by Canadian companies to persons not resident in the United States, to the extent that such companies would pay U.S. source interest under Code section 861(a)(1)(C) but not under the source rule of paragraph 6. It is to be noted that paragraph 8 is subject to the "saving clause" of paragraph 2 of Article XXIX (Miscellaneous Rules), so the United States may in all events impose its tax on interest received by U.S. citizens.

Article XII. ROYALTIES

Generally speaking, under the 1942 Convention royalties, including royalties with respect to motion picture films, which are derived by a resident of one Contracting State from sources within the other Contracting State are taxed at a maximum rate of 15 percent in the latter State; copyright royalties are exempt from tax in the State of source, if the resident does not have a permanent establishment in that State. See Articles II, III, XIII C, and paragraph 1 of Article XI of the 1942 Convention, and paragraph 6(a) of the Protocol to the 1942 Convention.

Paragraph 1 of Article XII of the Convention provides that a Contracting State may tax its residents with respect to royalties arising in the other Contracting State. Paragraph 2 provides that such royalties may also be taxed in the Contracting State in which they arise, but that if a resident of the other Contracting State is the beneficial owner of the royalties the tax in the Contracting State of source is limited to 10 percent of the gross amount of the royalties. Paragraph 3 provides that, notwithstanding paragraph 2, copyright royalties and other like payments in respect of the production or reproduction of any literary, dramatic, musical, or artistic work, including royalties from such works on videotape cassettes for private (home) use, if beneficially owned by a resident of the other Contracting State, may not be taxed by the Contracting State of source. This exemption at source does not apply to royalties in respect of motion picture films and works on film or videotape for use in connection with television broadcasting. Such royalties are subject to tax at a maximum rate of 10 percent in the Contracting State in which they arise, as provided in paragraph 2 (unless the provisions of paragraph 5, described below, apply).

Paragraph 4 defines the term "royalties" for purposes of Article XII. "Royalties" means payments of any kind received as consideration for the use of the right to use any copright of literary, artistic, or scientific work, including motion picture films and works on film or videotape for private (home) use or for use in connection with television broadcasting, any patent, trademark, design or model, plan, secret formula or process, or any payment for the use of or the right to use tangible personal property or for information concerning industrial, commercial, or scientific experience. The term "royalties" also includes gains from the alienation of any intangible property or rights described in paragraph 4 to the extent that such gains are contingent on the productivity, use, or subsequent disposition of such intangible property or rights. Thus, a guaranteed minimum payment derived from the alienation of (but not the use of) any right or property described in paragraph 4 is not a "royalty." Any amounts deemed contingent on use by reason of Code section 871(e) are, however, royalties under paragraph 2 of Article III (General Definitions), subject to Article XXVI (Mutual Agreement Procedure). The term "royalties" does not encompass management fees, which are covered by the provisions of Article VII (Business Profits) of XIV (Independent Personal Services), or payments under a bona fide cost-sharing arrangement. Technical service fees may be royalties in case where the fees are periodic and dependent upon productivity or a similar measure.

Paragraph 5 provides that the 10 percent limitation on tax in the Contracting State of source provided by paragraph 2, and the exemption in the Contracting State of source for certain copyright royalties provided by paragraph 3, do not apply if the beneficial owner of the royalties carries on business in the State of source through a permanent establishment or fixed base and the right or property in respect of which the royalties are paid is effectively connected with such permanent establishment or fixed base (i.e., the royalties are attributable to the permanent establishment or fixed base). In that event, the royalty income would be taxable under the provisions of Article VII (Business Profits) or XIV (Independent Personal Services), as the case may be.

Paragraph 6 establishes rules to determine the source of royalties for purposes of Article XII. The first rule is that royalties arise in a Contracting State when the payer is that State, or a political subdivision, local authority, or resident of that State. Notwithstanding that rule, royalties arise not in the State of the payer's residence but in any State, whether or not a Contracting State, in which is situated a permanent establishment or fixed base in connection with which the obligation to pay royalties was incurred, if such royalties are borne by such permanent establishment or fixed base. Thus, royalties paid to a resident of the United States by a company resident in Canada for the use of property in a third State will not be subject to tax in Canada if the obligation to pay the royalties is incurred in connection with, and the royalties are borne by, a permanent establishment of the company in a third State. "Borne by" means allowable as a deduction in computing taxable income.

A third rule, which overrides both the residence rule and the permanent establishment rule just described, provides that royalties for the use of intangible property or tangible personal property arise in the Contracting State in which such property is used. Thus, consistent with the provisions of Code section 861(a)(4), if a resident of a third State pays royalties to a resident of Canada for the right to use intangible property in the United States, such royalties are considered to arise in the United States and are subject to taxation by the United States consistent with the Convention. Similarly, if a resident of Canada pays royalties to a resident of a third State, such royalties are considered to arise in the United States and are subject to U.S. taxation if they are for the right to use intangible property in the United States. The term "intangible property" encompasses all the items described in paragraph 4, other than tangible personal property.

Paragraph 7 provides that in cases involving special relationships between persons the benefits of Article XII do not apply to amounts in excess of the amount which would have been agreed upon between persons with no special relationship; any such excess amount remains taxable according to the laws of Canada and the United States, consistent with any relevant provisions of the Convention.

Paragraph 8 restricts the right of a Contracting State to impose tax on royalties paid by a resident of the other Contracting State. The first State may not impose any tax on such royalties except insofar as they arise in that State or they are paid to a resident of that State or the right or property in respect of which the royalties are paid is effectively connected with a permanent establishment or fixed base situated in that State. This rule parallels the rule in paragraph 8 of Article XI (Interest) and paragraph 5 of Article X (Dividends). Again, U.S. citizens remain subject to U.S. taxation on royalties received despite this rule, by virtue of paragraph 2 of Article XXIX (Miscellaneous Rules).

Article XIII. GAINS

Paragraph 1 provides that Canada and the United States may each tax gains from the alienation of real property situated within that State which are derived by a resident of the other Contracting State. The term "real property" is defined for this purpose in paragraph 2 of Article VI (Income From Real Property). The term "alienation" used in paragraph 1 and other paragraphs of Article XIII means sales, exchanges and other dispositions or deemed dispositions (e.g., change of use, gifts, death) that are taxable events under the taxation laws of the Contracting State applying the provisions of the Article.

Paragraph 2 of Article XIII provides that the Contracting State in which a resident of the other Contracting State "has or had" a permanent establishment or fixed base may tax gains from the alienation of personal property constituting business property if such gains are attributable to such permanent establishment or fixed base. Unlike paragraph 1 of Article VII (Business Profits), paragraph 2 limits the right of the source State to tax such gains to a twelve-month period following the termination of the permanent establishment or fixed base.

Paragraph 3 authorizes the Contracting State of source to tax gains derived from the alienation of certain stock and other interests, if such interests ultimately reflect value derived from real property situated in that State. The right to tax in the State of source applies when there is an alienation of either shares forming part of a substantial interest in the capital stock of a company which is not a resident of the taxpayer's State of residence, or an interest in a partnership, trust, or estate, but only if the value of such shares or interest, as the case may be, is derived principally from real property in the Contracting State of source. The term "principally" means more than 50 percent. The right accorded to the State of source depends, however, on the domestic law in force in the Contracting State of residence. Thus, if at the time of alienation the latter State does not, by reason of its domestic law, impose tax upon gains derived from the alienation of a class of shares or interests (such as shares in companies which are not residents of that State), then the State of source may not impose tax in reciprocal circumstances.

Subparagraph (c) of paragraph 3 provides that the term "real property" as used in the paragraph, does not include property—other than mines, oil or gas wells, rental property, or property used for agriculture or forestry—in which a business is carried on. The term does include the shares of a company which derive their value principally from real property (wherever located) and an interest in a partnership, trust, or estate the direct disposition of which would be subject to tax under the paragraph. Thus, taxation in the Contracting State of source is preserved through several tiers of entities if the value of the shares or interest alienated is ultimately dependent principally upon real property in that State.

A "substantial interest" exists only if, on or after the effective date of the Convention provided in Article XXX (Entry Into Force), the resident and any persons related to him own 10 percent or more of the shares of any class of the captial stock of a company. It is the intention that once a "substantial interest" exists, all stock that is part of such "substantial interest" is covered by paragraph 3, even if the percentage of ownership declines to less than 10 percent. The term "related persons" is not defined by the rules of Article IX (Related Persons); rather, the term is defined pursuant to paragraph 2 of Article III (General Definitions).

Paragraph 4 reserves to the Contracting State of residence the sole right to tax gains from the alienation of any property other than property referred to in paragraphs 1, 2, and 3.

Paragraph 5 states that, despite paragraph 4, a Contracting State may impose tax on gains derived by an individual who is a resident of the other Contracting State if such individual was a resident of the first-mentioned State for 120 months (whether or not consecutive) during any period of 20 consecutive years, and was a resident of that State at any time during the 10-year period immediately preceding the alienation of the property.

Paragraph 6 provides a rule to coordinate Canadian and Unites States taxation of gains from the alienation of a principal residence situated in Canada. An individual (not a citizen of the United States) who was a resident of Canada and becomes a resident of the United States may determine his liability for U.S. income tax purposes in respect of gain from the alienation of a principal residence in Canada owned by him at the time he ceased to be a resident of Canada by claiming an adjusted basis for such residence in an amount no less than the fair market value of the residence at that time. Under paragraph 2(b) of Article XXX, the rule of paragraph 6 applies to gains realized for U.S. income tax purposes in taxable years beginning on or after the first day of January next following the date when instruments of ratification are exchanged, even if a particular individual described in paragraph 6 ceased to be a resident of Canada prior to such date. Paragraph 6 supplements any benefits available to a taxpayer pursuant to the provisions of Code section 1034.

Paragraph 7 provides a rule to coordinate U.S. and Canadian taxation of gains in circumstances where an individual is subject to tax in both Contracting States and one Contracting State deems a taxable alienation of property by such person to have occurred, while the other Contracting State at that time does not find a realization or recognition of income and thus defers, but does not forgive, taxation In such a case the individual may elect in his annual return of income for the year of such alienation to be liable to tax in the latter Contracting State as if he had sold and repurchased the property for an amount equal to its fair market value at a time immediately prior to the deemed alienation. The provision would, for example, apply in the case of a gift by a U.S. citizen or a U.S. resident individual which Canada deems to be an income producing event for its tax purposes but with respect to which the United States defers taxation while assigning the donor's basis to the donee. The provision would also apply in the case of a U.S. citizen who, for Canadian tax purposes, is deemed to recognize income upon his departure from Canada, but not to a Canadian resident (not a U.S. citizen) who is deemed to recognize such income. The rule does not apply in the case of death, although Canada also deems that to be a taxable event, because the United States in effect forgives income taxation of economic gains at death. If in one Contracting State there are losses and gains from deemed alienations of different properties, then paragraph 7 must be applied consistently in the other Contracting State within the taxable period with respect to all such properties. Paragraph 7 only applies, however, if the deemed alienations of the properties result in a net gain.

Paragraph 8 concerns the coordination of Canadian and U.S. rules with respect to the recognition of gain on corporate organizations, reorganizations, amalgamations, divisions, and similar transactions. Where a resident of a Contracting State alienates property in such a transaction, and profit, gain, or income with respect to such alienation is not recognized for income tax purposes in the Contracting State of residence, the competent authority of the other Contracting State may agree, pursuant to paragraph 8, if requested by the person who acquires the property, to defer recognition of the profit, gain, or income with respect to such property for income tax purposes. This deferral shall be for such time and under such other conditions as are stipulated between the person who acquires the property and the competent authority. The agreement of the competent authority of the State of source is entirely discretionary and will be granted only to the extent necessary to avoid double taxation of income. This provision means, for example, that the United States competent authority may agree to defer recognition of gain with respect to a transaction if the alienator would otherwise recognize gain for U.S. tax purposes and would not recognize gain under Canada's law. The provision only applies, however, if alienations described in paragraph 8 result in a net gain. In the absence of extraordinary circumstances the provisions of the paragraph must be applied consistently within a taxable period with respect to alienations described in the paragraph that take place within that period.

Paragraph 9 provides a transitional rule reflecting the fact that under Article VIII of the 1942 Convention gains from the sale or exchange of capital assets are exempt from taxation in the State of source provided the taxpayer had no permanent establishment in that State. Paragraph 9 applies to property that on September 26, 1980 was owned by a resident of the other Contracting if it did not form part of the business property of a permanent establishment or pertain to a fixed base in the State of source. Paragraph 9 applies to deemed dispositions. In addition, paragraph 9 applies to a gain described in paragraph 1, even though such gain is also income within the meaning of paragraph 3 of Article VI.

Paragraph 9 provides that where a resident of Canada or the United States is subject to tax pursuant to Article XIII in the other Contracting State on gains from the alienation of property, the amount of the gain shall be reduced for tax purposes in that other State by the amount of the gain attributable to the period during which the property was held up to and including December 31 of the year in which the documents of ratification are exchanged. The gain attributable to such period is normally determined by dividing the total gain by the number of full calendar months the property was held by such person, including, in the case of property having a carryover basis, the number of months in which a predecessor in interest held the property, and multiplying such monthly amount by the number of full calendar months ending on or before December 31 of the year in which the instruments of ratification are exchanged. In a case where property with a carryover basis is alienated after September 26, 1980, paragraph 9 applies to the alienator if at the time he sells or exchanges the property he is a person entitled to the benefits of paragraph 9 and his basis in the property is carried over from that of a person who, on September 26, 1980, would have been entitled to claim exemption at source under the 1942 Convention had he sold the property at that time.

Upon a clear showing, however, a taxpayer may prove that a greater portion of the gain was attributable to the specified period. Thus, in the United States the fair market value of the alienated property at the treaty valuation date may be established under paragraph 9 in the manner and with the evidence that is generally required by U.S. Federal income, estate, and gift tax regulations. For this purpose a taxpayer may use valid appraisal techniques for valuing real estate such as the comparable sales approach (see Rev. Proc. 79–24, 1979–1 C.B. 595), and the reproduction cost approach. If more than one property is alienated in a single transaction each property will be considered individually.

A taxpayer who desires to make this alternate showing for U.S. tax purposes must so indicate on his U.S. income tax return for the year of the sale or exchange and must attach to the return a statement describing the relevant evidence. The U.S. competent authority or his authorized delegate will determine whether the taxpayer has satisfied the requirements of paragraph 9.

U.S. residents, citizens and former citizens remain subject to U.S. taxation on gains as provided by the Code notwithstanding the provisions of Article XIII, other than paragraphs 6 and 7. See paragraphs 2 and 3(a) of Article XXIX (Miscellaneous Rules).

Article XIV. INDEPENDENT PERSONAL SERVICES

Article XIV concerns the taxation of income derived by an individual in respect of the performance of independent personal services. Such income may be taxed in the Contracting State of which such individual is a resident. It may also be taxed in the other Contracting State if the individual has or had a fixed base regularly available to him in the other State for the purpose of performing his activities, but only to the extent that the income is attributable to that fixed base. The use of the term "has or had" ensures that a Contracting State in which a fixed base existed has the right to tax income attributable to that fixed base even if there is a delay between the termination of the fixed base and the receipt of accrual of such income.

Unlike Article VII of the 1942 Convention, which provides a limited exemption from tax at source on income from independent personal services, Article XIV does not restrict the exemption to persons present in the State of source for fewer than 184 days. Furthermore, Article XIV does not allow the $5,000 exemption at source of the 1942 Convention, which was available even if services were performed through a fixed base. However, Article XIV provides complete exemption at source if a fixed base does not exist.

Article XV. DEPENDENT PERSONAL SERVICES

Paragraph 1 provides that, in general, salaries, wages, and other similar remuneration derived by a resident of a Contracting State in respect of an employment are taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is exercised in the other Contracting State, the entire remuneration derived therefrom may be taxed in that other State but only if, as provided by paragraph 2, the recipient is present in the other State for a period or periods exceeding 183 days in the calendar year, or the remuneration is borne by an employer who is a resident of that other State or by a permanent establishment or fixed base which the employer has in that other State. However, in all cases where the employee earns $10,000 or less in the currency of the State of source, such earnings are exempt from tax in that State. "Borne by" means allowable as a deduction in computing taxable income. Thus, if a Canadian resident individual employed at the Canadian permanent establishment of a U.S. company performs services in the United States, the income earned by the employee from such services is not exempt from U.S. tax under paragraph 1 if such income exceeds $10,000 (U.S.) because the U.S. company is entitled to a deduction for such wages in computing its taxable income.

Paragraph 3 provides that a resident of a Contracting State is exempt from tax in the other Contracting State with respect to remuneration derived in respect of an employment regularly exercised in more than one State on a ship, aircraft, motor vehicle, or train operated by a resident of the taxpayer's State of residence. The word "regularly" is intended to distinguish crew members from persons occasionally employed on a ship, aircraft, motor vehicle, or train. Only the Contracting State of which the employee and operator are resident has the right to tax such remuneration. However, this provision is subject to the "saving clause" of paragraph 2 of Article XXIX (Miscellaneous Rules), which permits the United States to tax its citizens despite paragraph 3.

Article XV states that its provisions are overridden by the more specific rules of Article XVIII (Pensions and Annuities) and Article XIX (Government Services).

Article XVI. ARTISTES AND ATHLETES

Article XVI concerns income derived by a resident of a Contracting State as an entertainer, such as a theatre, motion picture, radio, or television artiste, or a musician, or as an athlete, from his personal activities as such exercised in the other Contracting State. Article XVI overrides Articles XIV (Independent Personal Services) and XV (Dependent Personal Services) to allow source basis taxation of an entertainer or athlete in cases where the latter Articles would not permit such taxation. Thus, paragraph 1 provides that certain income of an entertainer or athlete may be taxed in the State of source in all cases where the amount of gross receipts derived by the entertainer or athlete, including expenses reimbursed to him or borne on his behalf, exceeds $15,000 in the currency of that other State for the calendar year concerned. For example, where a resident of Canada who is an entertainer derives income from his personal activities as an entertainer in the United States, he is taxable in the United States on all such income in any case where his gross receipts are greater than $15,000 for the calendar year. Article XVI does not restrict the right of the State of source to apply the provisions of Articles XIV and XV. Thus, an entertainer or athlete resident in a Contracting State and earning $14,000 in wages borne by a permanent establishment in the other State may be taxed in the other State as provided in Article XV.

Paragraph 2 provides that where income in respect of personal activities exercised by an entertainer or an athlete accrues not to the entertainer or athlete himself but to another person, that income may, notwithstanding the provisions of Article VII (Business Profits), Article XIV, and Article XV, be taxed in the Contracting State in which the activities are exercised. The anti-avoidance rule of paragraph 2 does not apply if it is established by the entertainer or athlete that neither he nor persons related to him participate directly or indirectly in the profits of the other person in any manner, including the receipt of deferred remuneration, bonuses, fees, dividends, partnership distributions, or other distributions.

Thus, if an entertainer who is a resident of Canada is under contract with a company and the arrangement between the entertainer and the company provides for payments to the entertainer based on the profits of the company, all of the income of the company attributable to the performer's U.S. activities may be taxed in the United States irrespective of whether the company maintains a permanent establishment in the United States. Paragraph 2 does not affect the rule of paragraph 1 that applies to the entertainer or athlete himself.

Paragraph 3 provides that Article XVI does not apply to the income of an athlete in respect of an employment with a team which participates in a league with regularly scheduled games in both Canada and the United States. Such an athlete is entitled to the benefits of Article XV (Dependent Personal Services). Thus, the athlete's remuneration would be exempt from tax in the Contracting State of source if he is a resident of the other Contracting State and earns $10,000 or less in the currency of the State of source, or if he is present in that State for a period or periods not exceeding in the aggregate 183 days in the calendar year, and his remuneration is not borne by a resident of that State or a permanent establishment or fixed base in that State. Paragraph 3 does not affect the taxation of the employer of an athlete covered by the paragraph. The employer is taxable pursuant to other articles of the Convention, such as Article VII.

Article XVII. WITHHOLDING OF TAXES IN RESPECT OF INDEPENDENT PERSONAL SERVICES

Article XVII confirms that a Contracting State may require withholding of tax on account of tax liability with respect to remuneration paid to an individual who is a resident of the other Contracting State, including an entertainer or athlete, in respect of the performance of independent personal services in the first-mentioned State. However, withholding with respect to the first $5,000 (in the currency of the State of source) of such remuneration paid in that taxable year by each payor shall not exceed 10 percent of such payment. In the United States, the withholding described in paragraph 1 relates to withholding with respect to income tax liability and does not relate to withholding with respect to other taxes, such as social security taxes. Nor is the paragraph intended to suggest that withholding in circumstances not specifically mentioned, such as withholding with respect to dependent personal services, is precluded by the Convention.

Paragraph 2 provides that in any case where the competent authority of Canada or the United States believes that withholding with respect to remuneration for the performance of independent personal services is excessive in relation to the estimated tax liability of an individual to that State for a taxable year, it may determine that a lesser amount will be deducted or withheld. Paragraph 2 may thus result in a lesser withholding than the maximum authorized by paragraph 1.

Paragraph 3 states that the provisions of Article XVII do not affect the liability of a resident of a Contracting State for taxes imposed by the other Contracting State. The Article deals only with the method of collecting taxes and not with substantive tax liability.

Article XVIII A of the 1942 Convention authorizes the issuance of regulations to specify circumstances under which residents of the United States temporarily performing personal services in Canada may be exempted from deduction and withholding of United States tax. This provision is omitted from the Convention as unnecessary. The Code and regulations provide sufficient authority to avoid excessive withholding of U.S. income tax.

Article XVIII. PENSIONS AND ANNUITIES

Paragraph 1 provides that a resident of a Contracting State is taxable in that State with respect to pensions and annuities arising in the other Contracting State. However, the amount of any pensions included in such person's income is not to exceed the amount that would be included if the person were a resident of the Contracting State in which the pension arises. Paragraph 1 imposes no such restriction with respect to the amount that may be taxed in the State of residence in the case of annuities.

Paragraph 2 provides rules with respect to the taxation of pensions and annuities in the Contracting State in which they arise. If the beneficial owner of a periodic pension payment is a resident of the other Contracting State, the tax imposed in the State of source is limited to 15 percent of the gross amount of such payment. Thus, the State of source is not required to allow a deduction or exclusion for a return of capital to the pensioner, but its tax is limited in amount in the case of a periodic payment. Other pension payments may be taxed in the State of source without limit.

In the case of annuities beneficially owned by a resident of a Contracting State, the Contracting State of source is limited to a 15 percent tax on the portion of the payment that is liable to tax in that State under its taxation laws.

Paragraph 3 defines the term "pensions" for purposes of the Convention to include any payment under a superannuation, pension, or retirement plan, Armed-Forces retirement pay, war veterans pensions and allowances, and amounts paid under a sickness, accident, or disability plan. Thus, the term "pension" includes pensions paid by private employers as well as any pension paid by a Contracting State in respect of services rendered to that State. A pension for government service is covered. The term "pensions" does not include payments under an income averaging annuity contract or benefits paid under social security legislation. The latter benefits are taxed, pursuant to paragraph 5, only in the Contracting State paying the benefit. Income derived from an income averaging annuity contract is taxable pursuant to the provisions of Article XXII (Other Income).

Paragraph 4 provides that, for purposes of the Convention, the term "annuities" means a stated sum paid periodically at stated times during life or during a specified number of years, under an obligation to make payments in return for adequate and full consideration other than services rendered. The term does not include a payment that is not periodic or any annuity the cost of which was deductible for tax purposes in the Contracting State where the annuity was acquired. Items excluded from the definition of "annuities" are subject to the rules of Article XXII.

Paragraph 5 provides that benefits under social security legislation in Canada or the United States paid to a resident of the other Contracting State or to a citizen of the United States are taxable only in the Contracting State paying the benefit. Paragraph 5 encompasses benefits paid under social security legislation of a political subdivision, such as a province of Canada.

Paragraph 6 provides that only the State of which a person is resident has the right to tax alimony and other similar amounts (including child support payments) arising in the other Contracting State and paid to such person. However, the amount included in income for purposes of taxation in the State of residence is not to exceed the amount that would be included in income if the recipient were a resident of the Contracting State of source. Paragraph 6 does not define the term "alimony"; the term is defined pursuant to the provisions of paragraph 2 of Article III (General Definitions).

Article XVIII does not provide rules to determine the State in which pensions, annuities, alimony, and other similar amounts arise. The provisions of paragraph 2 of Article III are used to determine where such amounts arise for purposes of determining whether a Contracting State has the right to tax such amounts.

The entirety of Article XVIII is, by reason of paragraph 3(a) of Article XXIX (Miscellaneous Rules), an exception to the "saving clause." Thus, the rules in this Article change U.S. taxation of U.S. citizens and residents.

Article XIX. GOVERNMENT SERVICE

Article XIX provides that remuneration, other than a pension, paid by a Contracting State or political subdivision or local authority thereof to a citizen of that State in respect of services rendered in the discharge of governmental functions shall be taxable only in that State. (Pursuant to paragraph 5 of Article IV (Residence), other income of such a citizen may also be exempt from tax, or subject to reduced rates of tax, in the State in which he is performing services, in accordance with other provisions of the Convention.) However, if the services are rendered in connection with a trade or business, then the provisions of Article XIV (Independent Personal Services), Article XV (Dependent Personal Services), or Article XVI (Artistes and Athletes), as the case may be, are controlling. Whether functions are of a governmental nature may be determined by a comparison with the concept of a governmental function in the State in which the income arises.

Pursuant to paragraph 3(a) of Article XXIX (Miscellaneous Rules), Article XIX is an exception to the "saving clause." As a result, a U.S. citizen resident in Canada and performing services in Canada in the discharge of functions of a governmental nature for the United States is taxable only in the United States on remuneration for such services.

This provision differs from the rules of Article VI of the 1942 Convention. For example, Article XIX allows the United States to impose tax on a person other than a citizen of Canada who earns remuneration paid by Canada in respect of services rendered in the discharge of governmental functions to the United States. (Such a person may, however, be entitled to an exemption from U.S. tax as provided in Code section 893.) Also, under the provisions of Article XIX Canada will not impose tax on amounts paid by the United States in respect of services rendered in the discharge of governmental functions to a U.S. citizen who is ordinarily resident in Canada for purposes other than rendering governmental services. Under paragraph 1 of Article VI of the 1942 Convention, such amounts would be taxable by Canada.

Article XX. STUDENTS

Article XX provides that a student, apprentice, or business trainee temporarily present in a Contracting State for the purpose of his full-time education or training is exempt from tax in that State with respect to amounts received from outside that State for the purpose of his maintenance, education, or training, if the individual is or was a resident of the other Contracting State immediately before visiting the first-mentioned State. There is no limitation on the number of years or the amount of income to which the exemption applies.

The Convention does not contain provisions relating specifically to professors and teachers. Teachers are treated under the Convention pursuant to the rules established in Articles XIV (Independent Personal Services) and XV (Dependent Personal Services), in the same manner as other persons performing services. In Article VIII A of the 1942 Convention there is a 2-year exemption in the Contracting State of source in the case of a professor or teacher who is a resident to the other Contracting State.

Article XXI. EXEMPT ORGANIZATIONS

Paragraph 1 provides that a religious, scientific, literary, educational, or charitable organization resident in a Contracting State shall be exempt from tax on income arising in the other Contracting State but only to the extent that such income is exempt from taxation in the Contracting State in which the organization is resident. Since this paragraph, and the remainder of Article XXI, deal with entities that are not normally taxable, the test of "resident in" is intended to be similar—but cannot be identical—to the one outlined in paragraph 1 of Article IV (Residence). Paragraph 3 provides that paragraph 1 does not exempt from tax income of a trust, company, or other organization from carrying on a trade or business, or income from a "related person" other than a person referred to in paragraph 1 or 2.

Paragraph 2 provides that a trust, company, or other organization that is resident in a Contracting State and constituted and operated exclusively to administer or provide employee benefits or benefits for the self-employed under one or more funds or plans established to provide pension or retirement benefits or other employee benefits is exempt from taxation on dividend and interest income arising in the other Contracting State, if the income of such organization is generally exempt from taxation in the Contracting State in which it is resident. Pursuant to paragraph 3 the exemption at source provided by paragraph 2 does not apply to dividends or interest from carrying on a trade or business or from a "related person," other than a person referred to in paragraph 1 or 2. The term "related person" is not necessarily defined by paragraph 2 of Article IX (Related Persons).

Paragraph 4 provides an exemption from U.S. excise taxes on private foundations in the case of a religious, scientific, literary, educational, or charitable organization which is resident in Canada but only if such organization has received substantially all of its support from persons other than citizens or residents of the United States.

Paragraph 5 provides that contributions by a citizen or resident of the United States to an organization which is resident in Canada and is generally exempt from Canadian tax are treated as charitable contributions, but only if the organization could qualify in the United States to receive deductible contributions if it were resident in (i.e., organized in) the United States. Paragraph 5 generally limits the amount of contributions made deductible by the Convention to the income of the U.S. citizen or resident arising in Canada, as determined under the Convention. In the case of contributions to a college or university at which the U.S. citizen or resident or a member of his family is or was enrolled, the special limitation to income arising in Canada is not required. The percentage limitations of Code section 170 in respect of the deductibility of charitable contributions apply after the limitations established by the Convention. Any amounts treated as charitable contributions by paragraph 5 which are in excess of amounts deductible in a taxable year pursuant to paragraph 5 may be carried over and deducted in subsequent taxable years, subject to the limitations of paragraph 5.

Paragraph 6 provides rules for purposes of Canadian taxation with respect to the deductibility of gifts to a U.S. resident organization by a resident of Canada. The rules of paragraph 6 parallel the rules of paragraph 5. The current limitations in Canadian law provide that deductions for gifts to charitable organizations may not exceed 20 percent of income. Excess deductions may be carried forward for one year.

The term "family" used in paragraphs 5 and 6 is defined in paragraph 2 of the Exchange of Notes accompanying the Convention to mean an individual's brothers and sisters (whether by whole or half-blood, or by adoption), spouse, ancestors, lineal descendents, and adopted descendents. Paragraph 2 of the Exchange of Notes also provides that the competent authorities of Canada and the United States will review procedures and requirements for organizations to establish their exempt status under paragraph 1 of Article XXI or as an eligible recipient of charitable contributions or gifts under paragraphs 5 and 6 of Article XXI. It is contemplated that such review will lead to the avoidance of duplicative administrative efforts in determining such status and eligibility.

The provisions of paragraph 5 and 6 generally parallel the rules of Article XIII D of the 1942 Convention. However, paragraphs 5 and 6 permit greater deductions for certain contributions to colleges and universities than do the provisions of the 1942 Convention.

Article XXII. OTHER INCOME

Paragraph 1 provides that a Contracting State of which a person is a resident has the sole right to tax items of income, wherever arising, if such income is not dealt with in the prior Articles of the Convention. If such income arises in the other Contracting State, however, it may also be taxed in that State. The determination of where income arises for this purpose is made under the domestic laws of the respective Contracting States unless the Convention specifies where the income arises (e.g., paragraph 6 of Article XI (Interest)) for purposes of determining the right to tax, in which case the provisions of the Convention control.

Paragraph 2 provides that to the extent that income distributed by an estate of trust resident in one Contracting State is deemed under the domestic law of that State to be a separate type of income "arising" within that State, such income distributed to a beneficiary resident in the other Contracting State may be taxed in the State of source at a maximum rate of 15 percent of the gross amount of such distribution. Such a distribution will, however, be exempt from tax in the State of source to the extent that the income distributed by the estate or trust was derived by the estate or trust from sources outside that State. Thus, in a case where the law of Canada treats a distribution made by a trust resident in Canada as a separate type of income arising in Canada, Canadian tax is limited by paragraph 2 to 15 percent of the gross amount distributed to a U.S. resident beneficiary. Although the Code imposes tax on certain domestic trusts (e.g., accumulation trusts) and such trusts are residents of the United States for purposes of Article IV (Residence) and paragraph 2 of Article XXII, paragraph 2 does not apply to distributions by such trusts because, pursuant to Code sections 667(e) and 662(b), these distributions have the same character in the hands of a nonresident beneficiary as they do in the hands of the trust. Thus, a distribution by a domestic accumulation trust is not a separate type of income for U.S. purposes. The taxation of such a distribution in the United States is governed by the distribution's character, the provisions of the Code and the provisions of the Convention other than the provision in paragraph 2 limiting the tax at source to 15 percent.

Article XXIII. CAPITAL

Although neither Canada nor the United States currently has national taxes on capital, Article XXIII provides rules for the eventuality that such taxes might be enacted in the future. Paragraph 1 provides that capital represented by real property (as defined in paragraph 2 of Article VI (Income From Real Property)) owned by a resident of a Contracting State and situated in the other Contracting State may be taxed in that other State.

Paragraph 2 provides that capital represented by either personal property forming part of the business property of a permanent establishment of personal property pertaining to a fixed base in a Contracting State may be taxed in that State.

Paragraph 3 provides that capital represented by ships and aircraft operated by a resident of a Contracting State in international traffic and by personal property pertaining to the operation of such ships and aircraft are taxable only in the Contracting State of residence.

Paragraph 4 provides that all elements of capital other than those covered by paragraphs 1, 2, and 3 are taxable only in the Contracting State of residence. Thus, capital represented by motor vehicles or railway cars, not pertaining to a permanent establishment or fixed base in a Contracting State, would be taxable only in the Contracting State of which the taxpayer is a resident.

Article XXIV. ELIMINATION OF DOUBLE TAXATION

Paragraph 1 provides the general rules that will apply under the Convention with respect to foreign tax credits for Canadian taxes paid or accrued. The United States undertakes to allow to a citizen or resident of the United States, or to a company electing under Code section 1504(d) to be treated as a domestic corporation, a credit against the Federal income taxes imposed by the Code for the "appropriate amount" of income tax paid or accrued to Canada. In the case of a company which is a resident of the United States owning 10 percent or more of the voting stock of a company which is a resident of Canada (which for this purpose does not include a company electing under Code section 1504(d) to be treated as a domestic corporation), and from which it receives dividends in a taxable year, the United States shall allow as a credit against income taxes imposed by the Code the appropriate amount of income tax paid or accrued to Canada by the Canadian company with respect to the profits out of which such company paid the dividends.

The direct and deemed-paid credits allowed by paragraph 1 are subject to the limitations of the Code as they may be amended from time to time without changing the general principle of paragraph 1. Thus, as is generally the case under U.S. income tax conventions, provisions such as Code sections 901(c), 904, 905, 907, 908, and 911 apply for purposes of computing the allowable credit under paragraph 1.

The term "income tax paid to accrued" is defined in paragraph 7 of Article XXIV to include certain specified taxes which are paid or accrued. Paragraph 1 provides a credit for these specified taxes whether or not they qualify as creditable under Code section 901 or 903. However, if any portion of the Canadian taxes creditable under the Convention does not qualify as income taxes or "in lieu" taxes under the Code, the amount of direct and deemed-paid credit that may be claimed under the Convention may not exceed the proportion of the federal income taxes imposed by the Code that the taxpayer's taxable income arising in Canada bears to the taxpayer's worldwide taxable income. In other words, Canadian taxes made creditable solely by paragraph 1 are creditable only to the extent of a per country limitation computed with respect to Canada pursuant to the special source rules set forth in paragraphs 3 and 6, subject to U.S. limitation rules (e.g., Code sections 904(b)(2) and 904(f)). If, after application of these rules, a person has paid or accrued an amount to Canada in excess of the amount creditable against U.S. tax for a given year, the excess may be carried over to other years to offset U.S. tax on income arising in Canada under the Convention.

Any creditable taxes not covered by paragraph 1 (e.g., third State taxes) may not offset U.S. tax on income arising in Canada under the Convention. Thus, if the taxpayer elects to compute the foreign tax credit for any years using the special source rules set forth in paragraphs 3 and 6, a separate limitation is computed for taxes not covered by paragraph 1 without regard to the source rules of paragraphs 3 and 6, and the credit for such taxes may not exceed such limitation. The credit allowed under this separate limitation may not exceed the proportion of the Federal income taxes imposed by the Code that the taxpayer's taxable income from foreign sources (under the Code) not included in taxable income arising in Canada (and not in excess of total foreign source taxable income under the Code) bears to the taxpayer's worldwide taxable income. In any case the credit for taxes covered by paragraph 1 and the credit for other foreign taxes is limited to the amount allowed under an overall limitation computed by aggregating taxable income arising in Canada and other foreign source taxable income.

If Canadian taxes claimed as credits are income taxes or "in lieu" taxes under the Code, and such taxes exceed the proportion of U.S. tax that taxable income arising in Canada bears to the entire taxable income, such taxes qualify on the same basis as other creditable taxes to be absorbed by the separate limitation computed with respect to other taxes.

In a case where a taxpayer has different types of income subject to separate limitations under the Code (e.g., section 904(d)(1)(B) DISC dividends, foreign oil related income and "other" income) the Convention rules just described apply in the context of each of the separate Code limitations.

A taxpayer may, for any year, claim a credit pursuant to the rules of the Code. In such case, the taxpayer would be subject to the limitations established in the Code, and would forego the rules of the Convention that determine where taxable income arises. In addition, any Canadian taxes covered by paragraph 1 which are not creditable under the Code would not be credited. In the event that Canadian taxes creditable under the Code and other taxes creditable under the Code exceed the limitation provided in the Code, the credit for Canadian taxes is determined pro rata on the basis of the proportion that Canadian creditable taxes bear to total creditable taxes.

The following examples illustrate the application of Article XXIV:

Example 1. A United States corporate taxpayer has for the taxable year $100 of taxable income having a Canadian source under the Convention but a U.S. source under the Code (see, for example, paragraph 1 of Article VII (Business Profits) and paragraph 3(a) of Article XXIV); $100 of taxable income having a U.S. source under both the Convention and the Code; $80 of taxable income having a foreign (non-Canadian) source under the Code but a U.S. source under the Convention (see paragraph 3(b) of Article XXIV); and ($50) of loss having a Canadian source. The taxpayer pays $50 of foreign (non-Canadian) income taxes, and $20 of Canadian taxes which are income taxes under the Code. All the foreign source income of the taxpayer constitutes "other" income described in Code section 904(d)(1)(c). In this case, the Convention provides that there is $50 of Canadian source taxable income, and therefore up to $23 of Canadian taxes covered by the Convention

$\left(\frac{\$50}{\$230} \times \$105.80\right)$

qualify for the credit. Since the taxpayer has paid only $20 of Canadian taxes covered by the Convention, a credit is allowed in that amount. The limitation for Canadian taxes under the Convention is not available to absorb other foreign taxes. The limitation with respect to other foreign taxes and foreign non-Canadian income is $13.80

$\left(\frac{\$30}{\$230} \times \$105.80\right)$,

and foreign income taxes in that amount may be credited in addition to the $20 of Canadian taxes, for a total credit of $33.80; the taxpayer has a foreign tax credit carryover of $36.20 of non-Canadian income taxes.

Example 2. The facts are the same as in Example 1, except that foreign non-Canadian operations result in a loss of ($30) rather than net income of $80, and no foreign non-Canadian income taxes are paid. The Code limitation is zero, because there is no foreign source taxable income. The Convention still provides that there is $50 of Canadian source taxable income but the credit is limited to $9.20

$\left(\frac{\$20}{\$120} \times \$55.20\right)$.

The remaining $10.80 of Canadian taxes covered by the Convention ($20 − $9.20) are available as a carryover.

Example 3. The facts are the same as in Example 1 except that the first $100 of taxable income mentioned in Example 1 has a Canadian source under

both the Convention and the Code. The Convention still provides that there is $50 of Canadian source income and $20 of Canadian taxes covered by the Convention thereby qualify for credit
$\frac{(\$50}{\$230} \times \$105.80)$.
The limitation with respect to foreign non-Canadian taxes is $36.80
$\frac{(\$80}{\$230} \times \$105.80)$.
In this case, however, if the Canadian taxes covered by the Convention would qualify for credit under Code section 901 or 903, the taxpayer could elect the Code limitation of $59.80
$\frac{\$130}{\$230} \times \$105.80)$,
which is more advantageous than the separate limitations computed under the Convention because those limitations do not permit third State income taxes to be credited against U.S. tax on income arising in Canada.

Example 4. The facts are the same as in Example 3 except that $10 of the $20 Canadian taxes covered by the Convention would not be creditable under Code section 901 or 903. If the taxpayer elects to claim a credit for the Canadian taxes which are creditable solely by reason of the Convention, it must use the Convention rules to compute the credit limitation ($23 + $36.80 = $59.80).

Example 5. The facts are the same as in Example 1 except that the corporation pays $25 of Canadian taxes covered by the Convention which are income taxes under the Code and $12 of foreign non-Canadian income taxes. The Convention still provides that there is $50 of Canadian source taxable income, and $23 of Canadian taxes covered by the Convention thereby qualify for credit. In addition, the limitation of $13.80 with respect to other foreign taxes permits the crediting of non-Canadian taxes plus Canadian taxes covered by the Convention. The taxpayer has a foreign tax credit carryover of $.03 of Canadian taxes and $.17 of other taxes, which may qualify for credit in carryover years.

The Convention only provides a credit for amounts paid or accrued. The determination of whether an amount is paid or accrued is made under the Code.

The rules of paragraph 1 are modified in certain respects by rules in paragraphs 4 and 5 for income derived by United States citizens who are residents of Canada. Paragraph 4 provides two steps for the elimination of double taxation in such a case. First, paragraph 4(a) provides that Canada shall allow a deduction from (credit against) Canadian tax in respect of income tax paid or accrued to the United States in respect of profits, income, or gains which arise in the United States (within the meaning of paragraph 3(a)); the deduction against Canadian tax need not, however, exceed the amount of income tax that would be paid or accrued to the United States if the individual were not a U.S. citizen, after taking into account any relief available under the Convention.

The second step, as provided in paragraph 4(b), is that the United States allows as a credit against United States tax, subject to the rules of paragraph 1, the income tax paid or accrued to Canada after the Canadian credit for U.S. tax provided by paragraph 4(a). The credit so allowed by the United States is not to reduce the portion of the United States tax that is creditable against Canadian tax in accordance with paragraph 4(a).

The following example illustrates the application of paragraph 4.

A United States citizen resides in Canada and earns $250 of income from the performance of independent personal services, $100 of which would be taxable by the United States under the provisions of Article XIV (Independent Personal Services) if such person were not a citizen of the United States. Taxable income for U.S. purposes, taking into account the rules of Code section 913, is $150. By reason of paragraph 3(a), the $100 that may be taxed by the United States arises in the United States for purposes of Article XXIV. Assume that the U.S. tax on the $100 of profits arising in the United States would be $25, if the taxpayer were not a U.S. citizen; the $100 is the only income of the taxpayer arising in the United States; and the $150 is his total taxable income from all sources. Assume further that the tentative U.S. income tax liability of the taxpayer, on his worldwide income, is $60; and that the tentative Canadian tax on the $250 of income is $100. Canada allows $25 as a credit against $100, leaving a net Canadian tax of $75. The U.S. allows as a credit $35 ($60–$25) of the $75 Canadian tax. (Pursuant to paragraph 6, which carries out the objectives of paragraphs 4 and 5 and is discussed in more detail below, a total of $87.50 of the individual's taxable income arises in Canada for purposes of the U.S. foreign tax credit
$\frac{A}{\$150} \times \$60 = \$35; A = \$87.50)$.
Thus, paragraph 6 overrides paragraph 3(a) to source an additional $37.50 of taxable income as arising in Canada.) The additional $40 of Canadian tax is allowed as a foreign tax credit carryover, subject to the limitations of the Convention and the Code.

Paragraph 5 provides special rules for the elimination of double taxation in the case of dividends, interest, and royalties earned by a U.S. citizen resident in Canada. These rules apply notwithstanding the provisions of paragraph 4, but only as long as the law in Canada allows a deduction in computing income for the portion of any foreign tax paid in respect of dividends, interest, or royalties which exceeds 15 percent of the amount of such items of income, and only with respect to those items of income. The rules of paragraph 4 apply with respect to other items of income; moreover, if the law in force in Canada regarding the deduction for foreign taxes changes, the provisions of paragraph 5 shall not apply and the U.S. foreign tax credit for Canadian taxes and the Canadian credit for U.S. taxes will be determined solely pursuant to the provisions of paragraph 4.

The calculations under paragraph 5 are as follows. First, the deduction in computing income allowed in Canada shall be made with respect to U.S. tax on the dividends, interest, and royalties before any foreign tax credit is allowed by the United States with respect to income tax paid or accrued to Canada. Second, Canada shall allow a deduction from (credit against) Canadian tax for U.S. tax paid or accrued with respect to the dividends, interest, and royalties, but such credit need not exceed 15 percent of the gross amount of such items of income that have been included in computing income for Canadian tax purposes. (The credit may, however, exceed the amount of tax that the United States would be entitled to levy under the Convention upon a Canadian resident who is not a U.S. citizen.) Third, for purposes of computing the U.S. tax on such dividends, interest, and royalties, the United States shall allow as a credit against the U.S. tax the income tax paid or accrued to Canada after the 15 percent credit against Canadian tax for income tax paid to accrued to the United States. The United States is in no event obliged to give a credit for Canadian income tax which will reduce the U.S. tax below 15 percent of the amount of the dividends, interest, and royalties.

The rules of paragraph 5 are illustrated by the following example.

Example A. A U.S. citizen who is a resident of Canada receives $200 of income with respect to personal services performed within Canada and $100 of royalty income arising within the United States. Taxable income for U.S. purposes, taking into account the rules of Code section 913, is $120. U.S. tax (before foreign tax credits) is $50. The $100 royalty bears U.S. tax (before foreign tax credits) of $41.67
$\frac{(\$100}{\$120} \times \$50)$.
Under Canadian law a deduction of $26.67 (the excess of $41.67 over 15 percent of $100) is allowed in computing income. The Canadian tax on $273.33 of income is $170. Canada gives a credit against the $170 for $15, leaving a final Canadian tax of $155. Of the $155, $41.58 is attributable to the royalty
$\frac{(\$73.33}{\$273.33} \times \$170 - \$15))$.
Of this amount $26.67 ($41.67 − $15) is creditable against U.S. tax pursuant to paragraph 5 and $14.91 is a foreign tax credit carryover for U.S. purposes, subject to the limitations of paragraph 5. (An additional $8.33 of Canadian tax with respect to Canadian source services income is creditable against U.S. tax pursuant to paragraphs 3 and 4(b).)

The general rule for avoiding double taxation in Canada is provided in paragraph 2. Pursuant to paragraph 2(a) Canada undertakes to allow to a resident of Canada a credit against income taxes imposed under the Income Tax Act for the appropriate amount of income taxes paid or accrued to the United States. Paragraph 2(b) provides for the deduction by a Canadian company. In computing taxable income, of any dividend received out of the exempt surplus of a U.S. company which is an affiliate. The provisions of paragraph 2 are subject to the provisions of the Income Tax Act as they may be amended from time to time without changing the general principle of paragraph 2.

Paragraph 3 provides source rules for purposes of applying Article XXIV. Profits, income, or gains of a resident of a Contracting State which may be taxed in the other Contracting State in accordance with the Convention, for reasons other than the saving clause of paragraph 2 of Article XXIX (Miscellaneous Rules) (e.g., pensions and annuities taxable where arising pursuant to Article XVIII (Pensions and Annuities)), are deemed to arise in the latter State. This rule does not, however, apply to gains taxable under paragraph 5 of Article XIII (Gains) (i.e., gains taxed by a Contracting State derived from the alienation of property by a former resident of that State). Gains from such an alienation arise, pursuant to paragraph 3(b), in the State of which the alienator is a resident. Thus, if in accordance with paragraph 5 of Article XIII, Canada imposes tax on certain gains of a U.S. resident such gains are deemed, pursuant to paragraphs 2 and 3(b) of Article XXIV, to arise in the United States for purposes of computing the deduction against Canadian tax for the U.S. tax on such gain. Under the Convention such gains arise in the United States for purposes of the United States foreign tax credit. Paragraph 3(b) also provides that profits, income, or gains arise in the Contracting State of which a person is a resident if they may not be taxed in the other Contracting State under the provisions of the Convention (e.g., alimony), other than the "saving clause" of paragraph 2 of Article XXIX. Paragraph 3 does not affect the source of losses.

The rules of paragraphs 3 and 6 must be utilized by a person claiming a credit for Canadian taxes solely by reason of the Convention. A person claiming a credit for Canadian income taxes pursuant to the Code may, however, use the Code credit rules exclusively. Furthermore, a person claiming a credit for income taxes of a third State may not rely upon the rules of paragraphs 3 and 6 for purposes of treating income that would otherwise have a U.S. source as having a foreign source (i.e., in the situation where the rules of the Convention produce excess limitation after Canadian taxes are taken into account).

Paragraph 6 is necessary to implement the objectives of paragraphs 4(b) and 5(c). Paragraph 6 provides that where a U.S. citizen is a resident of Canada, items of income referred to in paragraph 4 or 5 are deemed for the purposes of Article XXIV to arise in Canada to the extent necessary to avoid double taxation of income by Canada and the United States consistent with the objectives of paragraphs 4(b) and 5(c). Paragraph 6 can override the source rules of paragraph 3 to permit a limited resourcing of income. The principles of paragraph 6 have effect, pursuant to paragraph 3(b) of Article XXX (Entry Into Force), for taxable years beginning on or after January 1, 1976. See the discussion of Article XXX below.

The application of paragraph 6 is illustrated by the following example.

Example B. The facts are the same as in Example A. The United States has undertaken, pursuant to paragraph 5(c) and paragraph 6, to credit $26.67 of Canadian taxes on royalty income that has a U.S. source under both paragraph 3 and the Code. The credit, however, only reduces the U.S. tax on the royalty income which exceeds 15 percent of the amount of such income included in computing U.S. taxable income. Pursuant to paragraph 6, for purposes of determining the U.S. foreign tax credit limitation under the Convention with respect to Canadian taxes $64.08 $\left(\frac{\$A}{\$120} \times \$50 = \$26.67;\ A = \$64.08\right)$ of taxable income with respect to the royalties is deemed to arise in Canada.

Paragraph 7 provides that any reference to "income tax paid or accrued" to Canada or the United States includes Canadian tax or United States tax, as the case may be. The terms "Canadian tax" and "United States tax" are defined in paragraphs 1(c) and 1(d) of Article III (General Definitions). References to income taxes paid or accrued also include taxes of general application paid or accrued to a political subdivision or local authority of Canada or the United States which are not imposed by such political subdivision or local authority in a manner inconsistent with the provisions of the Convention and which are substantially similar to taxes of Canada or the United States referred to in paragraphs 2 and 3(a) of Article II (Taxes Covered).

In order for a tax imposed by a political subdivision or local authority to fall within the scope of paragraph 7, such tax must apply to individuals, companies, or other persons generally, and not only to a particular class of individuals or companies or a particular type of business. The tax must also be substantially similar to the national taxes referred to in paragraphs 2 and 3(a) of Article II. Finally, the political subdivision or local authority must apply its tax in a manner not inconsistent with the provisions of the Convention. For example, the political subdivision or local authority must not impose its tax on a resident of the other Contracting State earning business profits within the political subdivision or local authority but not having a permanent establishment there.

Paragraph 8 relates to the provisions of Article XXIII (Capital). It provides that were a resident of a Contracting State owns capital which, in accordance with the provisions of Article XXIII, may be taxed in the other Contracting State, the State of residence shall allow as a deduction from (credit against) its tax on capital an amount equal to the capital tax paid in the other Contracting State. The deduction is not, however, to exceed that part of the capital tax, computed before the deduction, which is attributable to capital which may be taxed in the other State.

Article XXV. NON-DISCRIMINATION

Paragraphs 1 and 2 of Article XXV protect individual citizens of a Contracting State from discrimination by the other Contracting State in taxation matters. Paragraph 1 provides that a citizen of a Contracting State who is a resident of the other Contracting State may not be subjected in that other State to any taxation or requirement connected with taxation which is other or more burdensome than the taxation and connected requirements imposed on similarly situated citizens of the other State.

Paragraph 2 assures protection in a case where a citizen of a Contracting State is not a resident of the other Contracting State. Such a citizen may not be subjected in the other State to any taxation or requirement connected to taxation which is other or more burdensome than the taxation and connected requirements to which similarly situated citizens of any third State are subjected. The reference to citizens of a third State "in the same circumstances" includes consideration of the State of residence. Thus, pursuant to paragraph 2, the Canadian taxation with respect to a citizen of the United States resident in, for example, the United Kingdom may not be more burdensome than the taxation of a U.K. citizen resident in the United Kingdom. Any benefits available to the U.K. citizen by virtue of an income tax convention between the United Kingdom and Canada would be available to the U.S. citizen resident in the United Kingdom if he is otherwise in the same circumstances as the U.K. citizen.

Paragraph 3 assures that, in computing taxable income, an individual resident of a Contracting State will be entitled to the same deduction for dependents resident in the other Contracting State that would be allowed if the dependents were residents of the individual's State of residence. The term "dependent" is defined in accordance with the rules set forth in paragraph 2 of Article III (General Definitions). For U.S. tax purposes, paragraph 3 does not expand the benefits currently available to a resident of the United States with a dependent resident in Canada. See Code section 152(b)(3).

Paragraph 4 allows a resident of Canada (not a citizen of the United States) to file a joint return in cases where such person earns salary, wages, or other similar remuneration as an employee and such income is taxable in the United States under the Convention. Paragraph 4 does not apply where the resident of Canada earns wages which are exempt in the United States under Article XV (Dependent Personal Services) or earns only income taxable by the United States under provisions of the Convention other than Article XV.

The benefit provided by paragraph 4 is available regardless of the residence of the taxpayer's spouse. It is limited, however, by a formula designed to ensure that the benefit is available solely with respect to persons whose U.S. source income is entirely, or almost entirely, wage income. The formula limits the United States tax with respect to wage income to that portion of the total U.S. tax that would be payable for the taxable year if both the individual and his spouse were United States citizens as the individual's taxable income (determined without any of the benefits made available by paragraph 4, such as the standard deduction) bears to the total taxable income of the individual and his spouse. The term "total United States tax" used in the formula is total United States tax without regard to any foreign tax credits, as provided in subparagraph 4(a). (Foreign income taxes may, however, be claimed as deductions in computing taxable income, to the extent allowed by the Code.) In determining total taxable income of the individual and his spouse, the benefits made available by paragraph 4 are taken into account, but a deficit of the spouse is not.

The following example illustrates the application of paragraph 4.

> A, a Canadian citizen and resident, is married to B who is also a Canadian citizen and resident. A earns \$12,000 of wages taxable in the U.S. under Article XV (Dependent Personal Services) and \$2,000 of wages taxable only in Canada. B earns \$1,000 of U.S. source dividend income, taxed by the United States at 15 percent pursuant to Article X (Dividends). B also earns \$2,000 of wages taxable only in Canada. A's taxable income for U.S. purposes, determined without regard to paragraph 4, is \$11,700 (\$12,000 − \$2,000 (Code sections 151(b) and 873(b)(3)) + \$1,700 (Code section 63)). The U.S. tax (Code section 1(d)) with respect to such income is \$2,084.50. The total U.S. tax payable by A and B if both were U.S. citizens and all their income arose in the United States would be \$2,013 under Code section 1(a) on taxable income of \$14,800 (\$17,000 − \$200 (Code section 116) − \$2,000 (Code section 151)). Pursuant to paragraph 4, the U.S. tax imposed on A's wages from U.S. sources is limited to \$1,591.36
> $\left(\frac{\$11{,}700}{\$14{,}800} \times \$2{,}013\right).$
> B's U.S. tax liability with respect to the U.S. source dividends remains \$150.

The provisions of paragraph 4 may be elected on a year-by-year basis. They are purely computational and do not make either or both spouses residents of the United States for the purpose of other U.S. income tax conventions.

Paragraph 5 protects against discrimination in a case where the capital of a company which is a resident of one Contracting State is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State. Such a company shall not be subjected in the State of which it is a resident to any taxation or requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which are subjected other similar companies which are residents of that State but whose capital is wholly or partly owned or controlled, directly or indirectly, by one or more residents of a third State.

Paragraph 6 protects against discrimination in the case of a permanent establishment which a resident of one Contracting State has in the other Contracting State. The taxation of such a permanent establishment by the other Contracting State shall not be less favorable than the taxation of residents of that other State carrying on the same activities. The paragraph specifically overrides the provisions of Article XXIV (Elimination of Double Taxation), thus ensuring that permanent establishments will be entitled to relief from double taxation on a basis comparable to the relief afforded to similarly situated residents. Paragraph 6 does not oblige a Contracting State to grant to a resident of the other Contracting State any personal allowances, reliefs, and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents. The principles of paragraph 6 would apply with respect to a fixed base as well as a permanent establishment. Paragraph 6 does not, however, override the provisions of Code section 906.

Paragraph 7 concerns the right of a resident of a Contracting State to claim deductions for purposes of computing taxable profits in the case of disbursements made to a resident of the other Contracting State. Such disbursements shall be deductible under the same conditions as if they had been made to a resident of the first-mentioned State. These provisions do not apply to amounts to which paragraph 1 of Article IX (Related Persons), paragraph 7 of Article XI (Interest), or paragraph 7 of Article XII (Royalties) apply. Paragraph 7 of Article XXV also provides that, for purposes of determining the taxable capital of a resident of a Contracting State, any debts of such person to a resident of the other Contracting State shall be deductible under the same conditions as if they had been contracted to a resident of the first-mentioned State. This portion of paragraph 7 relates to Article XXIII (Capital).

Paragraph 8 provides that, notwithstanding the provisions of paragraph 7, a Contracting State may enforce the provisions of its taxation laws relating to the deductibility of interest, in force on September 26, 1980, or as modified subsequent to that date in a manner that does not change the general nature of the provisions in force on September 26, 1980; or which are adopted after September 26, 1980, and are designed to ensure that nonresidents do not enjoy a more favorable tax treatment under the taxation laws of that State than that enjoyed by residents. Thus Canada may continue to limit the deductions for interest paid to certain nonresidents as provided in section 18(4) of Part I of the Income Tax Act.

Paragraph 9 provides that expenses incurred by citizens or residents of a Contracting State with respect to any convention, including any seminar, meeting, congress, or other function of similar nature, held in the other Contracting State, are deductible for purposes of taxation in the first-mentioned State to the same extent that such expenses would be deductible if the convention were held in that first-mentioned State. Thus, for U.S. income tax purposes an individual who is a citizen or resident of the United States and who attends a convention held in Canada may claim deductions for expenses incurred in connection with such convention without regard to the provisions of Code section 274(h). Section 274(h) imposes special restrictions on the deductibility of expenses incurred in connection with foreign conventions. A claim for a deduction for such an expense remains subject, in all events, to the provisions of U.S. law with respect to the deductibility of convention expenses generally (e.g., Code sections 162 and 212). Similarly, in the case of a citizen or resident of Canada attending a convention in the United States, paragraph 9 requires Canada to allow a deduction for expenses relating to such convention as if the convention had taken place in Canada.

Paragraph 10 provides that, notwithstanding the provisions of Article II (Taxes Covered), the provisions of Article XXV apply in the case of Canada to all taxes imposed under the Income Tax Act; and, in the case of the United States, to all taxes imposed under the Code. Article XXV does not apply to taxes imposed by political subdivisions or local authorities of Canada or the United States.

Article XXV substantially broadens the protection against discrimination provided by the 1942 Convention, which contains only one provision dealing specifically with this subject. That provision, paragraph 11 of the Protocol to the 1942 Convention, states that citizens of one of the Contracting States residing within the other Contracting State are not to be subjected to the payment of more burdensome taxes than the citizens of the other State.

The benefits of Article XXV may affect the tax liability of a U.S. citizen or resident with respect to the United States. See paragraphs 2 and 3 of Article XXIX (Miscellaneous Rules).

Article XXVI. MUTUAL AGREEMENT PROCEDURE

Paragraph 1 provides that where a person considers that the actions of one or both of the Contracting States will result in taxation not in accordance with the Convention, he may present his case in writing to the competent authority of the Contracting State of which he is a resident or, if he is a resident of neither Contracting State, of which he is a national. Thus, a resident of Canada must present to the Minister of National Revenue (or his authorized representative) any claim that such resident is being subjected to taxation contrary to the Convention. A person who requests assistance from the competent authority may also avail himself of any remedies available under domestic laws.

Paragraph 2 provides that the competent authority of the Contracting State to which the case is presented shall endeavor to resolve the case by mutual agreement with the competent authority of the other Contracting State, unless he believes that the objection is not justified or he is able to arrive at a satisfactory unilateral solution. Any agreement reached between the competent authorities of Canada and the United States shall be implemented notwithstanding any time or other procedural limitations in the domestic laws of the Contracting States, except where the special mutual agreement provisions of Article IX (Related Persons) apply, provided that the competent authority of the Contracting State asked to waive its domestic time or procedural limitations has received written notification that such a case exists within six years from the end of the taxable year in the first-mentioned State to which the case relates. The notification may be given by the competent authority to take action, or a person related to the taxpayer. Unlike Article IX, Article XXVI does not require the competent authority of a Contracting State to grant unilateral relief to avoid double taxation in a case where timely notification is not given to the competent authority of the other Contracting State. Such unilateral relief may, however, be granted by the competent authority in its discretion pursuant to the provisions of Article XXVI and in order to achieve the purposes of the Convention. In a case where the provisions of Article IX apply, the provisions of paragraphs 3, 4, and 5 of that Article are controlling with respect to adjustments and corresponding adjustments of income, loss, or tax and the effect of the Convention upon time or procedural limitations of domestic law. Thus, if relief is not available under Article IX because of fraud, the provisions of paragraph 2 of Article XXVI do not independently authorize such relief.

Paragraph 3 provides that the competent authorities of the Contracting States shall endeavor to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. In particular, the competent authorities may agree to the same attribution of profits to a resident of a Contracting State and its permanent establishment in the other Contracting State; the same allocation of income, deductions, credits, or allowances between persons; the same determination of the source of income; the same characterization of particular items of income; a common meaning of any term used in the Convention; rules, guidelines, or procedures for the elimination of double taxation with respect to income distributed by an estate or trust, or with respect to a partnership; or to increase any dollar amounts referred to in the Convention to reflect monetary or economic developments. The competent authorities may also consult and reach agreements on rules, guidelines, or procedures for the elimination of double taxation in cases not provided for in the Convention.

The list of subjects of potential mutual agreement in paragraph 3 is not exhaustive; it merely illustrates the principles set forth in the paragraph. As in the case of other U.S. tax conventions, agreement can be arrived at in the context of determining the tax liability of a specific person or in establishing rules, guidelines, and procedures that will apply generally under the Convention to resolve issues for classes or taxpayers. It is contemplated that paragraph 3 could be utilized by the competent authorities, for example, to resolve conflicts between the domestic laws of Canada and the United States with respect to the allocation and apportionment of deductions.

Paragraph 4 provides that each Contracting State will endeavor to collect on behalf of the other State such amounts as may be necessary to ensure that relief granted by the Convention from taxation imposed by the other State does not enure to the benefit of persons not entitled to such relief. Paragraph 4 does not oblige either Contracting State to carry out administrative measures of a different nature from those that would be used by Canada or the United States in the collection of its own tax or which would be contrary to its public policy.

Paragraph 5 confirms that the competent authorities of Canada and the United States may communicate with each other directly for the purpose of reaching agreement in the sense of paragraphs 1 through 4.

Article XXVII. EXCHANGE OF INFORMATION

Paragraph 1 authorizes the competent authorities to exchange the information necessary for carrying out the provisions of the Convention or the domestic laws of Canada and the United States concerning taxes covered by the Convention, insofar as the taxation under those domestic laws is not contrary to the Convention. The authority to exchange information granted by paragraph 1 is not restricted by Article I (Personal Scope), and thus need not relate solely to persons otherwise covered by the Convention. It is contemplated that Article XXVII will be utilized by the competent authorities to exchange information upon request, routinely, and spontaneously.

Any information received by a Contracting State pursuant to the Convention is to be treated as secret in the same manner as information obtained under the taxation laws of that State. Such information shall be disclosed only to persons or authorities, including courts and administrative bodies, involved in the assessment or collection of, the administration and enforcement in respect of, or the determination of appeals in relation to the taxes covered by the Convention, and the information may be used by such persons only for such purposes. (In accordance with paragraph 4, for the purposes of this Article the Convention applies to a broader range of taxes than those covered specifically by Article II (Taxes Covered).)

In specific cases a competent authority providing information may, pursuant to paragraph 3, impose such other conditions on the use of information as are necessary. Although the information received by persons described in paragraph 1 is to be treated as secret, it may be disclosed by such persons in public court proceedings or in judicial decisions.

The provisions of paragraph 1 authorize the U.S. competent authority to continue to allow the General Accounting Office to examine tax return information received from Canada when GAO is engaged in a study of the administration of U.S. tax laws pursuant to a directive of Congress. However, the secrecy requirements of paragraph 1 must be met.

If a Contracting State requests information in accordance with Article XXVII, the other Contracting State shall endeavor, pursuant to paragraph 2, to obtain the information to which the request relates in the same manner as if its own taxation were involved, notwithstanding the fact that such State does not need the information. In addition, the competent authority requested to obtain information shall endeavor to provide the information in the particular form requested, such as depositions of witnesses and copies of unedited original documents, to the same extent such depositions and documents can be obtained under the laws or administrative practices of that State with respect to its own taxes.

Paragraph 3 provides that the provisions of paragraphs 1 and 2 do not impose on Canada or the United States the obligation to carry out administrative measures at variance with the laws and administrative practice of either State; to supply information which is not obtainable under the laws or in the normal course of the administration of either State; or to supply information which would disclose any trade, business, industrial, commercial, or professional secret or trade process, or information the disclosure of which would be contrary to public policy. Thus, Article XXVII allows, but does not obligate, the United States and Canada to obtain and provide information that would not be available to the requesting State under its laws or administrative practice or that in different circumstances would not be available to the State requested to provide the information. Further, Article XXVII allows a Contracting State to obtain information for the other Contracting State even if there is no tax liability in the State requested to obtain the information. Thus, the United States will continue to be able to give Canada tax information even if there is no U.S. tax liability at issue.

Paragraph 4 provides that, for the purpose of Article XXVII, the Convention applies, in the case of Canada, to all taxes imposed by the Government of Canada on estates and gifts and under the Income Tax Act and, in the case of the United States, to all taxes imposed under the Internal Revenue Code. Article XXVII does not apply to taxes imposed by political subdivisions or local authorities of the Contracting States. Paragraph 4 is designed to ensure that information exchange will extend to most national level taxes on both sides, and specifically to information gathered for purposes of Canada's taxes on estates and gifts (not effective for deaths or gifts after 1971). This provision is intended to mesh with paragraph 8 of Article XXX (Entry Into Force), which terminates the existing estate tax convention between the United States and Canada.

Article XXVIII. DIPLOMATIC AGENTS AND CONSULAR OFFICERS

Article XXVIII states that nothing in the Convention affects the fiscal privileges of diplomatic agents or consular officers under the general rules of international law or under the provisions of special agreements. However, various provisions of the Convention could apply to such persons, such as those concerning exchange of information, mutual agreement, and non-discrimination.

Article XXIX. MISCELLANEOUS RULES

Paragraph 1 states that the provisions of the Convention do not restrict in any manner any exclusion, exemption, deduction, credit, or other allowance accorded by the laws of a Contracting State in the determination of the tax imposed by that State. Thus, if a deduction would be allowed for an item in computing the taxable income of a Canadian resident under the Code, such deduction is available to such person in computing taxable income under the Convention. Paragraph 1 does not, however, authorize a taxpayer to make inconsistent choices between rules of the Code and rules of the Convention. For example, if a resident of Canada desires to claim the benefits of the "attributable to" rule of paragraphs 1 and 7 of Article VII (Business Profits) with respect to the taxation of business profits of a permanent establishment, such person must use the "attributable to" concept consistently for all items of income and deductions and may not rely upon the "effectively connected" rules of the Code to avoid U.S. tax on other items of attributable income. In no event are the rules of the Convention to increase overall U.S. tax liability from what liability would be if there were no convention.

Paragraph 2 provides a "saving clause" pursuant to which Canada and the United States may each tax its residents, as determined under Article IV (Residence), and the United States may tax its citizens (including any former citizen who lost his citizenship for the principal purpose of avoiding of U.S. income tax, but only for a period of 10 years following such loss) and companies electing under Code section 1504(d) to be treated as domestic corporations, as if there were no convention between the United States and Canada with respect to taxes on income and capital.

Paragraph 3 provides that, notwithstanding paragraph 2, the United States and Canada must respect certain specified provisions of the Convention in regard to residents, citizens, and section 1504(d) companies. Paragraph 3(a) lists certain paragraphs and Articles of the Convention that represent exceptions to the "saving clause" in all situations; paragraph 3(b) provides a limited further exception for students who have not acquired immigrant status in the State where they are temporarily present.

Paragraph 4 provides relief with respect to social security taxes imposed on employers, employees, and self-employed persons under Code sections 1401, 3101, and 3111. Income from personal services not subject to tax by the United States under the provisions of the 1942 Convention is not to be considered wages or net earnings from self-employment for purposes of the U.S. social security taxes with respect to taxable years of the taxpayer not barred by the statute of limitations (under the Code) ending on or before December 31 of the year in which instruments of ratification are exchanged. Thus, if instruments of ratification are exchanged in 1981 a resident of Canada earning income from personal services and such person's employer may apply for refunds of the employee's and employer's shares of U.S. social security tax paid attributable to the employee's income from personal services that is exempt from U.S. tax by virtue of the 1942 Convention. In this example, the refunds would be available for social security taxes paid with respect to taxable years not barred by the statute of limitations of the Code ending on or before December 31, 1981. For purposes of Code section 6611, the date of overpayment with respect to refunds of U.S. tax pursuant to paragraph 4 is the date on which instruments of ratification of the Convention are exchanged.

Under certain limited circumstances, an employee may, pursuant to paragraph 5 of Article XXX (Entry Into Force), claim an exemption from U.S. tax on wages under the 1942 Convention for one year after the Convention comes into force. The provisions of paragraph 4 would not, however, provide an exemption from U.S. social security taxes for such year.

Paragraph 4 does not modify existing U.S. statutes concerning social security benefits or funding. The Social Security Act requires the general funds of the Treasury to reimburse the social security trust funds on the basis of the records of wages and self-employment income maintained by the Social Security Administration. The Convention does not alter those records. Thus, any refunds of tax made pursuant to paragraph 4 would not affect claims for U.S. quarters of coverage with respect to social security benefits. And such refunds would be charged to general revenue funds, not social security trust funds.

Paragraph 5 provides a method to resolve conflicts between the Canadian and U.S. treatment of individual retirement accounts. Certain Canadian retirement plans which are qualified plans for Canadian tax purposes do not meet Code requirements for qualification. As a result, the earnings of such a plan are currently included in income, for U.S. tax purposes, rather than being deferred until actual distributions are made by the plan. Canada defers current taxes on the earnings of such a plan but imposes tax on actual distributions from the plan. Paragraph 5 is designed to avoid a mismatch of U.S. taxable income and foreign tax credits attributable to the Canadian tax on such distributions. Under the paragraph a United States citizen who is a resident of Canada and a beneficiary of a Canadian registered retirement savings plan may elect to defer U.S. taxation with respect to any income accrued in the plan but not distributed by the plan, until such time as a distribution is made from the plan or any substitute plan. The election is to be made under rules established by the competent authority of the United States.

Paragraph 6 provides that if 25 percent or more of the capital of a company which is a resident of a Contracting State is owned directly or indirectly by individuals who are not residents of that State, and if by reason of special measures the tax imposed in that State on that company with respect to dividends (other than direct investment dividends referred to in paragraph 2(a) of Article X (Dividends)), interest, or royalties arising in the other Contracting State is substantially less than the tax generally imposed by the first-mentioned State on corporate business profits, then, notwithstanding the provisions of Article X, XI (Interest), or XII (Royalties), the other State may tax such dividends, interest, or royalties as if there were no convention between the United States and Canada with respect to taxes on income and on capital. Thus, the Contracting State in which dividends, interest, or royalties arise may substitute its domestic law rate of tax on such income, which in the United States is currently 30 percent and in Canada is currently 25 percent, for the maximum rates provided for in the Convention, which range from zero to 15 percent.

The phrase "substantially less than" is subject to definition pursuant to paragraph 2 of Article III (General Definitions). In any event, the phrase does not include the situation under Canadian law where a privately owned company distributes its investment income in the form of dividends and receives a refund of up to 16⅔ percent of such a distribution. The effect of such a refund is not considered to produce tax "substantially less than" the tax generally imposed in Canada.

Article XXX. ENTRY INTO FORCE

Paragraph 1 provides that the Convention is subject to ratification in accordance with the procedures of Canada and the United States. The exchange of instruments of ratification is to take place at Ottawa as soon as possible.

Paragraph 2 provides, subject to paragraph 3, that the Convention shall enter into force upon the exchange of instruments of ratification. It has effect, with respect to source State taxation of dividends, interest, royalties, pensions, annuities, alimony, and child support, for amounts paid or credited on or after the first day of the second calendar month after the date on which the instruments of ratification are exchanged. For other taxes, the Convention takes effect for taxable years beginning on or after January 1 next following the date when instruments of ratification are exchanged. In the case of relief from United States social security taxes provided by paragraph 4 of Article XXIX (Miscellaneous Rules), the Convention also has effect for taxable years before the date on which instruments of ratification are exchanged.

Paragraph 3 provides special effective date rules for foreign tax credit computations with respect to taxes paid or accrued to Canada. Paragraph 3(a) provides that the tax on 1971 undistributed income on hand imposed by Part IX of the Income Tax Act of Canada is considered to be an "income tax" for distributions made on or after January 1, 1972 and before January 1, 1979. Any such tax which is paid or accrued under U.S. standards is considered to be imposed at the time of distribution and on the recipient of the distribution, in the proportion that the distribution out of undistributed income with respect to which the tax has been paid bears to 85 percent of such undistributed income. A person claiming a credit for tax pursuant to paragraph 3(a) is obligated to compute the amount of the credit in accordance with that paragraph.

Paragraph 3(b) provides that the principles of paragraph 6 of article XXIV (Elimination of Double Taxation), which provides for resourcing of certain dividend, interest, and royalty income to eliminate double taxation of U.S. citizens residing in Canada, have effect for taxable years beginning on or after January 1, 1976. The paragraph is intended to grant the competent authorities sufficient flexibility to address certain practical problems that have arisen under the 1942 Convention. It is anticipated that the competent authorities will be guided by paragraphs 4 and 5 of Article XXIV in applying paragraph 3(b) of Article XXX. Any claim for refund based on the provisions of paragraph 3 may be filed on or before June 30 of the calendar year following the year in which instruments of ratification are exchanged, notwithstanding statutes of limitations or other rules of domestic law to the contrary. For purposes of Code section 6611, the date of overpayment is the date on which instruments of ratification are exchanged, with respect to any refunds of U.S. tax pursuant to paragraph 3.

Paragraph 4 provides that, subject to paragraph 5, the 1942 Convention ceases to have effect for taxes for which the Convention has effect under the provisions of paragraph 2. For example, if under paragraph 2 the Convention were to have effect with respect to taxes withheld at source on dividends paid as of March 1, 1981, the 1942 Convention will not have effect with respect to such taxes.

Paragraph 5 modifies the rule of paragraph 4 to allow all of the provisions of the 1942 Convention to continue to have effect for the period through the first taxable year with respect to which the provisions of the Convention would otherwise have effect under paragraph 2(b), if greater relief from tax is available under the 1942 Convention than under the Convention.

Paragraph 6 provides that the 1942 Convention terminates on the last of the dates on which it has effect in accordance with the provisions of paragraph 4 and 5.

Paragraph 7 terminates the Exchange of Notes between the United States and Canada of August 2 and September 17, 1928 providing for relief from double taxation of shipping profits. The provisions of the Exchange of Notes no longer have effect for taxable years beginning on or after January 1 following the exchange of instruments of ratification of the Convention. The 1942 Convention, in Article V, had suspended the effectiveness of the Exchange of Notes.

Paragraph 8 terminates the Convention between Canada and the United States for the Avoidance of Double Taxation with Respect to Taxes on the Estates of Deceased Persons signed on February 17, 1961. The provisions of that Convention cease to have effect with respect to estates of persons deceased on or after January 1 of the year following the exchange of instruments of ratification of the Convention.

Article XXXI. TERMINATION

Paragraph 1 provides that the Convention shall remain in force until terminated by Canada or the United States.

Paragraph 2 provides that either Canada or the United States may terminate the Convention at any time after 5 years from the date on which instruments of ratification are exchanged, provided that notice of termination is given through diplomatic channels at least 6 months prior to the date on which the Convention is to terminate.

Paragraph 3 provides a special termination rule in situations where Canada or the United States changes its taxation laws and the other Contracting State believes that such change is significant enough to warrant modification of the Convention. In such a circumstance, the Canadan Ministry of Finance and the United States Department of the Treasury would consult with a view to resolving the matter. If the matter cannot be satisfactorily resolved, the Contracting State requesting an accommodation because of the change in the other Contracting State's taxation laws may terminate the Convention by giving the 6 months' prior notice required by paragraph 2, without regard to whether the Convention has been in force for 5 years.

Paragraph 4 provides that, in the event of termination, the Convention ceases to have effect for tax withheld at source under Articles X (Dividends), XI (Interest), XII (Royalties), and XVIII (Pensions and Annuities), and under paragraph 2 of Article XXII (Other Income), with respect to amounts paid or credited on or after the first day of January following the expiration of the 6 month period referred to in paragraph 2. In the case of other taxes, the Convention shall cease to have effect in the event of termination with respect to taxable years beginning on or after January 1 following the expiration of the 6 month period referred to in paragraph 2.

Part IV. Items of General Interest

Debt Instruments With Original Issue Discount Imputed Interest on Deferred Payment Sales or Exchanges of Property; and Safe Haven Interest Rates for Commonly Controlled Taxpayers—Public Hearing

Announcement 86–97

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to: (1) The tax treatment of debt instruments issued after July 1, 1982, that contain original issue discount, (2) the imputation of and the accounting for interest with respect to sales and exchanges of property occurring after December 31, 1984, and (3) safe haven interest rates for loans or advances between commonly controlled taxpayers and safe haven leases between such taxpayers.

DATES: The public hearing will be held on Monday, November 17, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Monday, October 27, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, Attn: CC:LR:T (LR–189–84), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W. Washington, D.C. 20224, telephone 202–566–3935 (not a toll-free call).

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under section 163(e), 446, 482, 483, and 1271 through 1275 of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Tuesday, April 8, 1986 (51 FR 12022) [1986–18 I.R.B. 4]. On June 24, 1986, the FEDERAL REGISTER published a notice that extended to September 2, 1986, the deadline for submitting written comments (51 FR 22947).

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted, or who submit, written comments within the time prescribed in the April 8 notice of proposed rulemaking and the June 24 extension and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Monday, October 27, 1986, an outline of oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

(Filed by the Office of the Federal Register July 1, 1986, 8:45 a.m., and published in the issue of the Federal Register for July 2, 1986, 51 F.R. 24162)

Foundations Status of Certain Organizations

Announcement 86–98

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

Abel/Angel Corporation, Columbus, OH
Abounding Love Ministries, Inc., San Luis Obispo, CA
Abudant Life Chapel, Inc., Lexington, KY
Alamo Club South of Kent County, Grand Rapids, MI
Alpha Omega Ministries, Inc., Louisville, KY
American Ontological Society, Ojai, CA
American Stage Directions, Portola Valley, CA
Antic, Cuyahoga Falls, OH
Antioch Youth Football Association, Inc., Antioch, CA
Aplastic Anemia Charitable Trust Foundation of Winchester, Ky, Inc., Winchester, KY
Appropriate Dwellings, Inc., Columbus, OH
Art for Peace, San Anselmo, CA
Asian Business League of Santa Clara Valley, San Jose, CA
Association For Retarded Citizens, Allen County First Housing Corp., Lima, OH
Association of Black Secretaries, Inc., Oakland, CA
Aware, Inc., Dayton, OH
Barrington Health Center, Inc., Indianapolis, IN
Batavia New York Elderly, Inc., Columbus, OH
Bethel-Alpha Housing Corp., Saginaw, MI
Bethsaida Manor, Inc., Dayton, OH
Black Hills Citizens For a Better Community, Grand Rapids, MI
Blind Adults of Marin, Inc., San Rafael, CA
Bodega Bay Community Association, Bodega Bay, CA
Bradford County Manor Volunteers, Towanda, PA
Branch County Coalition Against Domestic Violence, Coldwater, MI
Brick City Players, Inc., Cleveland, OH
Britt Airways Scholarship Program, Inc., Terre Haute, IN
Brookhill Swim Club, Lexington, KY
Brownette's Academy of Charm, Inc., Cleveland, OH
Brunswick Charities, Inc., Brunswick, OH
CDF Mendocino County Muster Team, Inc., Willits, CA
California Alzheimers and Related Diseases Association, Inc., Orangevale, CA
Cambodian New Generation, Inc., Oakland, CA

Cape May Beach Patrol Benevolent Association Scholarship Fund, Wildwood, NJ
Caring and Sharing, Mentor, OH
Casa De La Raza, Inc., San Francisco, CA
Caspin Housing Corp., Iron River, MI
Catholics United for Life of Michigan, Farmington Hills, MI
Chai House II, Inc., San Jose, CA
Childrens Museum of Northeastern Ohio, Canton, OH
Chinese Christian Medical Mission, Inc., Valparaiso, IN
Choice Place, Inc., Ashland, OH
Christmas Lake Village Scholarship Award Trust, Santa Claus, IN
Claude M. Spilman Jr. Center, Inc., Indianapolis, IN
Clay Township Historical Society, Algonac, MI
College Communications Foundation, Inc., Bloomington, IN
Columbia Cares Crusade, Inc., Columbia, KY
Columbus Area Alcohol and Drug Council, Inc., Columbus, IN
Committee on Biblical Exposition, Palo Alto, CA
Community Alcoholism Foundation of Greater Cincinnati, Cincinnati, OH
Community-Based Victim Restitution, Detroit, MI
Community Care Team of Brooklyn Heights, Cuyahoga Heights, Valley View, Cleveland, OH
Community Celebration of Southwest Philadelphia, Inc., Philadelphia, PA
Community Land Co-Op of Cincinnati, Cincinnati, OH
Concerned Parents of Novato, Novato, CA
Consumer Dental Health Association, Alamo, CA
Cooperative Campus Ministry of Youngstown, Inc., Youngstown, OH
Coventry Neighbors, Inc., Cleveland, OH
Cranford Lincoln Senior Housing, Inc., Cranford, NJ
Creative Growth and Awareness Through the Arts, Inc., Pittsburg, CA
Crosetti Dance Co., Inc., San Lorenzo, CA
Day Group Home, Inc., Buellton, CA
Dayspring Institute, Inc., Pleasant Hill, CA
Delaware Community Volunteer Fire Department, Inc., Osgood, IN
Dixon Parent Study Group, Dixon, CA
Downtown Foundation, Reno, NV
E.C. Reems Foundation, Oakland, CA
East Bay Vietnamese Association, Oakland, CA
El Paseo De Las Flores Familia En Accion Corp., San Jose, CA
ERUV, Inc., Columbus, OH
Essence Institute, Inc., Milpitas, CA
Ettas Residential Center, San Francisco, CA
Fair Oaks Soccer Club, Fair Oaks, CA
Fantasia Color Guard, Marion, OH
Fellowship at Barkley, Inc., Hopkinsville, KY
Filipina-Americans in Michigana Association, Inc., South Bend, IN
First 202 Housing Corporation, Dayton, OH
First 202 Housing Corporation, No. 2 McArthur Site, Dayton, OH
First 202 Housing Corporation, No. 3 Jefferson Township Site, Dayton, OH
Fisk University Cleveland Alumni Association, Inc., Cleveland, OH
Foundation for the Advancement of Economic and Social Education, Inc., Crawsfordville, IN
Foundation Ministries, Inc., Fort Wayne, IN
Friends of Allen House, Cincinnati, OH
Friends of Glenview Center, Bay Village, OH
Friends of Polish Art, Southfield, MI
Friends of the Capitol, East Lansing, MI
From Woman to Woman, Inc., Parkersburg, WV
Fulfill a Dream of Ohio, Inc., Youngstown, OH
GOA Heritage Foundation, El Cerrito, CA
Gabriel House, Incorporated, Bloomington, IN
Gary Bradds Scholarship Fund, Jamestown, OH
Gary City-Wide Development Corporation, Gary, IN
Glenn Lucky Charitable Foundation, Inc., South Lake Tahoe, CA
Global Salvage Recycling Center, Cincinnati, OH
God Ordained Deism, Oakland, CA
Golden Raiders Boosters Club, Warren, OH
Grand Haven Coast Guard Festival, Inc., Grand Haven, MI
Great Lakes Association of Industry and Rehabilitations, Cleveland, OH
Hastings Alumni for Action, San Francisco, CA
Holistic Learning Associates, Berkeley, CA
Hospice of the Ridge, Inc., Paradise, CA
Identity of America Ministries, Garberville, CA
Independence Through Athletics, Inc., Tracy, CA
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International Christian Youth Corp., Sacramento, CA
International Health and Research Foundation Research Institute for Immune Deficiency, Las Vegas, NV
Key West Charitable Trust for Historic Preservation, San Francisco, CA
Kiddie Kastle, Inc., U.S., VI
Kings County Junior Golf Foundation, Hanford, CA
La Colonia Santa Paula, Inc., Santa Paula, CA
Las Vegas Opportunities Industrialization Center of Clark, Co. Nevada, Las Vegas, NV
Lebanese Educational and Cultural Foundation, Inc., Moraga, CA
Life Guard, Inc., Las Vegas, NV
Linden Band Boosters, Stockton, CA
Living with Cancer, Trinidad, CA
Lucille Glass Mauzy Foundation, Danville, CA
Lunch Break, Red Bank, NJ
Manila-San Francisco Sister City Committee, San Francisco, CA
Marin Video Archives, Mill Valley, CA
Medical Properties Management, Inc., Traverse City, MI
Melanoma Foundation, San Francisco, CA
Ministry of Songs, Madera, CA
Morningstar Ministries of Central Pennsylvania, Inc., Williamsport, PA
Netcare Residential Apartments, Columbus, OH
Newark Job Bank Trade & Training Corp., Newark, NJ
Nicarauac La Pena and Art Gallery of San Francisco, San Francisco, CA
Northern California Al-Anon World Service Assembly, Rancho Cordova, CA
Nova Educational Services, Inc., Sacramento, CA
Pacific Stage Company, Pleasantown, CA
Piconet Gilroy, CA
Pittsburg Senior and Handicapped Homes, Inc., Pittsburg, CA
Pocket Girls Softball League, Inc., Sacramento, CA
Radioimaging, Palo Alto, CA
Range of Light, Coulterville, CA
Riddle Evangelistic Association, Inc., Roseville, CA
River City Oar and Paddle Foundation, Inc., Davis, CA

Robert and Dietra Davis Museum, Carnelian Bay, CA

Role Players Ensemble, San Ramon, CA

Royal Oaks Tennis Club, Watsonville, CA

Sacramento Lutheran Campus Ministry, Sacramento, CA

Santa Barbara County Bowl Fdn., Santa Barbara, CA

Santa Barbara Performing Arts Association, Santa Barbara, CA

Savo Island Cooperative Homes, Inc., Berkeley, CA

Sitting Room, The, Cotati, CA

Sonya Safe Ride Association, Reno, NV

Southern Nevada Youth Trade School, Las Vegas, NV

Spina Bifida Association of Central California, Inc., Fresno, CA

Students on Computers Kamp, Lindsay, CA

Sweetspirit Ministries, Inc., Watsonville, CA

Task Force Against Substance Abuse, Inc., Rumson, NJ

To Benefit Those in Need, San Francisco, CA

Urban Chumash of Ventura, Ventura, CA

Valley Womens Club Association of San Lorenzo Valley, Inc., Ben Lomond, CA

Vine Hill Amphitheater, Inc., Scotts Valley, CA

WHB Concepts, Inc., San Pablo, CA

West Bay Local Development Corp., San Francisco, CA

Western Counseling Association, Las Vegas, NV

Western Nevada Animal Protection Society, Yerington, NV

World for Jesus Ministries, Inc., Fresno, CA

Worlds Agri-Fair, Sacramento, CA

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practictioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Robert D. Digby	North Little Rock, AR	Certified Public Accountant	Four Months from July 29, 1986
Jeffrey E. Ellis	Rockland, ME	Certified Public Accountant	Indefinte from July 2, 1986
Charles L. Honey	Prescott, AR	Attorney	One Year from July 2, 1986
Bernhardt Karp	Hudson, NY	Attorney & Certified Public Accountant	Indefinite from July 29, 1986
George N. Meros	Springfield, MO	Attorney	Indefinite from July 25, 1986
William G. Waldrop	Adamsville, AL	Certified Public Accountant	Indefinite from July 17, 1986

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to identify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
David P. Rosenberg	Philadelphia, PA	Indefinite effective August 13, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor.
E—Estate
EE—Employee
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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1986-39

Internal Revenue

bulletin

Bulletin No. 1986-39
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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-114, page 14.
Mutual life insurance companies; differential earnings rate. The differential earnings rate for 1985 and the recomputed differential earnings rate for 1984 are set forth for use by mutual life insurance companies to compute their income tax liability for 1985.

Rev. Rul. 86-115, page 19.
Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for October 1986.

Rev. Rul. 86-116, page 4.
Investment credit; recapture; transfer of leasehold interest to partnership. The transfer of a leasehold interest in section 38 property to a partnership does not result in recapture of the investment credit under section 47(a) of the Code when the transfer is a mere change in the form of conducting the taxpayer's trade or business.

T.D. 8099, page 5.
Regulations under section 704(b) of the Code relate to allocations of loss and deduction attributable to nonrecourse debt of a partnership.

T.D. 8101, page 15.
LR-295-84, page 21.
Temporary and proposed regulations under section 817(h) of the Code relate to the diversification requirements for variable annuity, endowment, and life insurance contracts.

EXEMPT ORGANIZATIONS

Announcement 86-99, page 21.
A list is given of organizations now classified as private foundations and an organization that is not a private operating foundation.

ESTATE TAX

Rev. Rul. 86-117, page 19.
Credits against tax; property transferred in payment of state inheritance tax liability. The payment of state inheritance taxes in property other than cash constitutes "taxes actually paid" to the state for purposes of the federal estate tax credit. The amount "actually paid" is the lesser of the state inheritance tax liability discharged by the transfer of the property or the fair market value of the property on the date of the transfer. The estate realizes gain or loss upon the transfer measured by the difference between the estate's basis in the property and the amount of the state tax liability that was discharged.

Finding Lists begin on page 27.
Announcement of Disbarments and Suspensions begin on page 24.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 47.—Certain Dispositions, Etc., Of Section 38 Property

26 CFR 1.47–2: "Disposition" and "cessation". (Also Section 1.47–3.)

Investment credit; recapture; transfer of leasehold interest to partnership. The transfer of a leasehold interest in section 38 property to a partnership does not result in recapture of the investment credit under section 47(a) of the Code when the transfer is a mere change in the form of conducting the taxpayer's trade or business.

Rev. Rul. 86–116

ISSUE

Does the transfer of a leasehold interest in section 38 property to a partnership, under the circumstances described below, result in recapture of the investment credit under section 47(a) of the Internal Revenue Code?

FACTS

In 1980 the taxpayer, a corporation, leased certain section 38 property from an unrelated party for use in a trade or business. The section 38 property constituted substantially all of the assets used in the taxpayer's trade or business. The lessor made a valid election under section 48(d) of the Code to treat the taxpayer as the purchaser of the property for purposes of the investment credit.

In 1981 the taxpayer assigned the lease and transferred possession of the section 38 property to a partnership in which the taxpayer received a 50 percent interest. Simultaneously, the lessor transferred its title to the leased section 38 property (along with all its rights and obligations under the lease) to the same partnership in exchange for a partnership interest. Upon these simultaneous transfers to the partnership, the lease was terminated and the partnership received substantially all the assets necessary to conduct the taxpayer's trade or business.

LAW AND ANALYSIS

Section 47(a)(1) of the Code provides that if during any taxable year any property is disposed of or otherwise ceases to be section 38 property with respect to the taxpayer before the close of the useful life that was taken into account in computing the credit under section 38, the federal income tax for such taxable year shall be increased by an amount equal to the aggregate decrease in the credits allowed under section 38 for all prior years that would have resulted solely from substituting, in determining qualified investment, for such useful life the shorter actual useful life.

Section 47(b) of the Code provides that property shall not be treated as ceasing to be section 38 property with respect to the taxpayer by reason of a mere change in the form of conducting the trade or business so long as the property is retained in such trade or business as section 38 property and the taxpayer retains a substantial interest in such trade or business.

Section 1.47–2(b)(2) of the Income Tax Regulations provides that for purposes of paragraph (a) of section 1.47–1 (recomputation of credit allowed by section 38 of the Code), if, under section 1.48–4, the lessor of new section 38 property made a valid election to treat the lessee as having purchased such property for purposes of the credit allowed by section 38, that certain rules apply in determining whether such property is disposed of, or otherwise ceases to be section 38 property with respect to the lessee. The rules applicable to this transaction are set forth in section 1.47–2(b)(2) as follows:

(i) Generally, a mere disposition by the lessor of property subject to a lease shall not be considered to be a disposition by the lessee.

(iii) If a lease is terminated and the property is transferred by the lessee to the lessor or to any other person, such transfer shall be considered to be a dispostion by the lessee.

Section 1.47–3(f)(1) of the regulations provides that, notwithstanding the provisions of section 1.47–2, relating to "disposition" and "cessation," paragraph (a) of section 1.47–1 shall not apply to section 38 property that is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer by reason of a mere change in the form of conducting the trade or business in which such section 38 property is used, provided certain conditions are satisfied.

Under sections 1.47–3(f)(1)(ii) and (4) of the regulations, three conditions must be met for the "mere change in form" rule to apply to the assignment of a lease and transfer of possession of section 38 property with respect to which a valid section 48(d) election was made:

(a) the section 38 property is retained as section 38 property in the same trade or business;

(b) the transferor of section 38 property retains a substantial interest in such trade or business; and

(c) substantially all the assets (whether or not section 38 property) necessary to operate such trade or business are transferred to the transferee to whom such section 38 property is transferred.

As described earlier, the lease terminated when the taxpayer contributed its leasehold interest in the section 38 property to the partnership. Pursuant to section 1.47–2(b)(2)(iii) of the regulations, a disposition occurs if the lease is terminated and the property is transferred by the lessee to the lessor or to any other person. However, pursuant to section 1.47–3(f)(1), recapture is not required in a transaction that constitutes a mere change in the form of conducting the taxpayer's trade or business.

In this situation, the taxpayer's transfer to the partnership satisfies the conditions in sections 1.47–3(f)(1)(ii) and (4) of the regulations and is a mere change in the form of conducting the taxpayer's trade or business because: (1) the section 38 property was retained as section 38 property in the same trade or business; (2) the taxpayer retained a substantial interest in such trade or business; that is, the 50-percent partnership interest (*see* example 5 of section 1.47–3(f)(6) of the regulations); and (3) substantially all the assets necessary to operate the trade or business were transferred to the partnership.

HOLDING

The transfer of the leasehold interest in section 38 property to a partnership, under the circumstances described above, does not result in recapture of the investment credit under section 47(a) of the Code.

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26 CFR 1.47–3: Exceptions to the application of §1.47–1.

Whether transfer of a leasehold interest in section 38 property to a partnership will result in recapture

of the investment credit in certain circumstances. See Rev. Rul. 86-116, page 4.

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term and long-term rates are set forth for the month of October 1986. See Rev. Rul. 86-115, page 19.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of October 1986. See Rev. Rul. 86-115, page 19.

Section 468.—Special Rules for Mining and Solid Waste Reclamation and Closing Costs

Federal short-term, mid-term and long-term rates are set forth for the month of October 1986. See Rev. Rul. 86-115, page 19.

Section 704.—Partner's Distributive Share

26 CFR 1.704-1: Partner's distributive share.

T.D. 8099

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1—INCOME TAX, TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Allocations of Loss and Deduction Attributable to Nonrecourse Debt

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final Income Tax Regulations under section 704(b) of the Internal Revenue Code of 1954, relating to allocations of loss and deduction attributable to nonrecourse debt of the partnership. In addition, certain clarifying amendments are made to the existing final regulations under section 704(b). This Treasury decision reflects certain changes made to the law by the Tax Reform Act of 1976.

DATE: The amendments are effective for partnership taxable years beginning after December 31, 1975, except as otherwise provided in existing §1.704-1(b)(1)(ii), as modified by this Treasury decision.

FOR FURTHER INFORMATION: Contact John G. Schmalz of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. ATTN: CC:LR:T 202-566-3297.

SUPPLEMENTARY INFORMATION: BACKGROUND

On March 9, 1983, the FEDERAL REGISTER published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 704(b) of the Internal Revenue Code of 1954 [1983-1 C.B. 930]. Those amendments were proposed to conform the regulations to section 213(d) of the Tax Reform Act of 1976 (95 Stat. 1548). Numerous written comments were received during the comment period, and a public hearing was held on May 4, 1983. On December 31, 1985, the FEDERAL REGISTER (50 FR 53420) published final regulations (T.D. 8065) [1986-1 C.B. 254] under section 704(b). That Treasury decision adopted the proposed rules as revised by the Treasury decision, except that §1.704-1(b)(4)(iv), relating to allocations of loss and deduction attributable to nonrecourse debt, was reserved. The proposed regulations remained outstanding on that issue. Since December 31, 1985, the Treasury Department has continued to consider the public comment concerning this issue. After consideration of all the public comments concerning the issue of the allocation of loss and deduction attributable to nonrecourse debt, the proposed rules on this issue are finalized as revised by this Treasury decision.

In addition, certain clarifying changes are made to the final regulations that were published on December 31, 1985.

EXPLANATION OF PROVISIONS NONRECOURSE DEBT

The final regulations provide that allocations of loss and deduction attributable to nonrecourse debt shall be deemed to be made in accordance with the partners' interests in the partnership so long as four requirements are met. First, requirements *(1)* and *(2)* of §1.704-1(b)(2)(ii)(*b*), relating to the requirements to maintain capital accounts and have liquidation distributions made in accordance with capital account balances, must be satisfied. Second, the partnership agreement must provide that allocations of such loss and deduction are made in a manner that is reasonably consistent with allocations, which have substantial economic effect, of some other significant partnership item attributable to partnership property securing the nonrecourse liabilities (other than minimum gain recognized by the partnership). Third, either requirement *(3)* of §1.704-1(b)(2)(ii)(*b*), relating to the restoration of partners' deficit capital account balances, must be satisfied, or the partnership agreement must contain a "minimum gain chargeback." Fourth, all other material partnership allocations and capital account adjustments must be recognized under §1.704-1(b). Allocations not qualifying under this safe harbor must be made in accordance with the partners' overall economic interests in the partnership.

In addition, the final regulations clarify that the amount of a partner's share of minimum gain shall be treated as a limited deficit make-up obligation for purposes of the alternative economic effect test of existing §1.704-1(b)(2)(ii)(*d*). In addition, the regulations give guidance on the application of section 704(c) and section 704(c) principles in cases where nonrecourse debt is involved. Finally, the regulations clarify the treatment of deductions attributable to nonrecourse loans made to the partnership by a partner of the partnership but reserve §1.704-1(b)(4)(iv)(*h*) for rules to be proposed concerning the treatment of nonrecourse deductions attributable to nonrecourse loans made to the partnership by a person related to a partner of the partnership.

OTHER CLARIFYING CHANGES

The final regulations also contain several corrective and clarifying changes to the final regulations under section 704(b) that were published in the FEDERAL REGISTER on December 31, 1985.

PUBLIC COMMENTS AND CHANGES MADE IN RESPONSE TO PUBLIC COMMENTS

NONRECOURSE DEBT

Section 704(b), as amended by the Tax Reform Act of 1976, provides that a partner's distributive share of income, gain, loss, deduction, or credit (or item thereof) is determined in accordance with such partner's interest in the partnership (determined by taking into account all facts and circumstances) if either the partnership agreement does not provide for the distributive share, or the allocation to the partner under the partnership agreement does not have substantial economic effect.

Allocations of loss and deduction attributable to nonrecourse debt cannot have substantial economic effect since no partner of the partnership can bear the economic loss corresponding to the loss and deduction attributable to such nonrecourse debt. Such economic loss can only be borne by the nonrecourse lender. Because allocations of loss and deduction attributable to nonrecourse debt cannot have economic effect, section 704(b) mandates that such items must be allocated in accordance with the partners' interests in the partnership.

The proposed regulations published in March of 1983 provided that loss and deduction attributable to nonrecourse debt would be deemed to be in accordance with the partners' interests in the partnership if the partnership maintained capital accounts in accordance with the regulations, liquidating distributions were made in accordance with positive capital account balances, and either: (1) Partners were obligated to restore the deficit balances in their capital accounts upon liquidation of their interests in the partnership, or (2) the deficit capital account balances attributable to such loss and deduction did not exceed the amount of minimum gain and such minimum gain was allocated to the partners who were allocated such loss and deduction.

This rule was criticized by certain members of the public on conceptual grounds. These commentators contended that a partner's obligation to bear the burden of taxation on the minimum gain that resulted from loss and deduction attributable to nonrecourse debt was not necessarily a good indication of a partner's interest in the partnership. For example, under the proposed rule, so long as the partnership agreement contained a minimum gain chargeback provision, 100 percent of the loss and deduction attributable to nonrecourse debt could be allocated to a partner even though such partner's interest in every other partnership item was substantially less than 100 percent.

The Treasury Department has fully considered all of the public comment and agrees that a partnership should not be allowed to allocate loss and deduction attributable to nonrecourse debt in the manner described in the example in the preceding paragraph. Accordingly, the proposed rule has been modified to preclude this and similar types of tax-motiviated arrangements.

In addition, several other changes were made in response to the public comment. Several commentators asked for examples that explained the interaction between section 704(c) and the nonrecourse debt provision. Other commentators asked for more limited partnership examples and examples where partnership assets secure more than one partnership liability and where nonrecourse liabilities are secured by more than one partnership asset. Additional examples have been added in response to these comments.

Similarly, in response to commentators who asked for clarification of the rule in a case where partnership assets are subject to both recourse and nonrecourse liabilities, new rules and examples have been added to address so-called "stacking" problems.

Certain commentators asked for clarification of the rules where a partner made a purported nonrecourse loan to the partnership. The final regulations provide that allocations of loss and deduction attributable to such loans are not governed by the nonrecourse debt rules. Instead, such losses and deductions must be allocated to the lending partner under §1.704-1(b)(3). The Treasury Department is studying whether transactions involving loans to the partnership by persons related to partners should be governed by similar rules. If it determines that similar rules should be applicable to such cases, those rules will be proposed as part of another regulation project.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. The Internal Revenue Service has concluded that the final regulations contained herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is John G. Schmalz of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and the Treasury Department participated in developing these regulations both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 1 is amended as follows:

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 2. Section 1.704-1(b) is amended by revising paragraph (b)(4)(iv) and by adding examples (20) through (23) immediately after example (19) in paragraph (b)(5) to read as follows:

§1.704-1 Partner's distributive share.

* * * * *

(b) *Determination of partner's distributive share.* * * *

(4) *Special rules.* * * *

(iv) *Nonrecourse deductions—(a) Allocation of nonrecourse deductions.* An allocation of loss, deduction, or section 705(a)(2)(B) expenditure (or item thereof) attributable to nonrecourse liabilities of the partnership ("nonrecourse deductions") cannot have economic effect because, in the event there is an economic burden that corresponds to such an allocation, the creditor alone bears that burden. Thus, nonrecourse deductions must be allocated in accordance with the partners' interests in the partnership. Paragraph (b)(4)(iv)(*d*) of this section, however, provides a test under which certain allocations of nonrecourse deductions will be deemed to be in accordance with the partners' interests in the partnership. If that test is not satisified, the partners' distributive shares of nonrecourse deductions will be determined, under paragraph (b)(3) of this section, according to the partners' overall economic interests in the partnership.

(b) Determination of nonrecourse deductions. The amount of nonrecourse deductions for a partnership taxable year equals the net increase, if any, in the amount of partnership minimum gain during that taxable year. See Examples (20)(i), (21), and (22) of paragraph (b)(5) of this section. In determining such net increase for any partnership taxable year in which the capital accounts of the partners are increased pursuant to paragraph (b)(2)(iv)(*f*) of this section to reflect a revaluation of partnership property subject to one or more nonrecourse liabilities of the partnership, any decrease in partner-

ship minimum gain attributable to each such revaluation shall be added back to the net decrease or increase otherwise determined. See Example (22) (iii) of paragraph (b)(5) of this section. The nonrecourse deductions for a partnership taxable year shall consist first of depreciation or cost recovery deductions with respect to items of partnership property subject to one or more nonrecourse liabilities of the partnership to the extent of the increase in minimum gain attributable to the nonrecourse liabilities to which each such item of property is subject, with the remainder of such nonrecourse deductions, if any, made up of a pro rata portion of the partnership's other items of deduction, loss, and section 705(a)(2)(B) expenditure for that year. If, however, such depreciation or cost recovery deductions exceed the net increase in partnership minimum gain, a proportional share of each such deduction shall constitute a nonrecourse deduction. See example (23) of paragraph (b)(5) of this section. In addition, if the net increase in partnership minimum gain during a partnership taxable year exceeds the total amount of items of partnership loss, deduction, and section 705(a)(2)(B) expenditure for such year, then an amount of partnership loss, deduction, and section 705(a)(2)(B) expenditure for the partnership's next succeeding taxable year (or years) equal to such excess shall constitute nonrecourse deductions, as if there had been a net increase in partnership minimum gain during such succeeding year (or years) in the amount of such excess.

(c) Partnership minimum gain. The amount of partnership minimum gain is determined by computing, with respect to each nonrecourse liability of the partnership, the amount of gain (of whatever character), if any, that would be realized by the partnership if it disposed of (in a taxable transaction) the partnership property subject to such liability in full satisfaction thereof, and by then aggregating the amounts so computed. See examples (20)(i) and (iv), (21), and (22) of paragraph (b)(5) of this section. For the purpose of determining the amount of such gain, (*1*) the adjusted basis of partnership property subject to two or more liabilities of equal priority shall be allocated among such liabilities in proportion to the respective outstanding balances of such liabilities, and (*2*) the adjusted basis of partnership property subject to two or more liabilities of unequal priority shall be allocated to the liabilities of an inferior priority (in accordance with (*1*) above) only to the extent of the excess, if any, of the adjusted tax basis of such property over the aggregate outstanding balance of the liabilities of superior priority. Only the portion of the property's adjusted basis allocated to nonrecourse liabilities of the partnership shall be used in computing minimum gain. See example (20)(v) and (vi) of paragraph (b)(5) of this section. If partnership property subject to one or more nonrecourse liabilities of the partnership is, under paragraph (b)(2)(iv)(*d*) or (b)(2)(iv)(*f*) of this section, properly reflected on the books of the partnership at a book value that differs from the adjusted tax basis of such property, the determinations under this paragraph (b)(4)(iv) shall be made with reference to such book value. See example (22) of paragraph (b)(5) of this section.

(d) Requirements to be satisfied. Allocations of nonrecourse deductions shall be deemed to be made in accordance with the partners' interests in the partnership if, and only if—

(*1*) Throughout the full term of the partnership, requirements (*1*) and (*2*) of paragraph (b)(2)(ii)(*b*) of this section are satisfied,

(*2*) Beginning in the first taxable year in which there are nonrecourse deductions and thereafter throughout the full term of the partnership, the partnership agreement provides for allocations of nonrecourse deductions among the partners in a manner that is reasonably consistent with allocations, which have substantial economic effect, of some other significant partnership item attributable to the property securing nonrecourse liabilities of the partnership (other than minimum gain recognized by the partnership),

(*3*) Beginning in the first taxable year of the partnership in which the partnership has nonrecourse deductions and thereafter throughout the full term of the partnership, (*i*) requirement (*3*) of paragraph (b)(2)(ii)(*b*) of this section is satisfied, or (*ii*) the partnership agreement contains a "minimum gain chargeback" (as defined in paragraph (b)(4)(iv)(*e*) of this section), and

(*4*) All other material allocations and capital account adjustments under the partnership agreement are recognized under this paragraph (b) (without regard to whether allocations of adjusted tax basis and amount realized under section 613A(c)(7)(D) are recognized under paragraph (b)(4)(v) of this section).

(e) Minimum gain chargeback. **A partnership agreement contains a "minimum gain chargeback" if, and only if, it provides that, if there is a net decrease in partnership minimum gain during a partnership taxable year, all partners with a deficit capital account balance at the end of such year (excluding from each partner's deficit capital account balance any amount that such partner is obligated to restore under paragraph (b)(2)(ii)(*c*) of this section, as well as any addition thereto pursuant to the next to last sentence of paragraph (b)(4)(iv)(*f*) of this section computed with respect to the amount of partnership minimum gain after such net decrease) will be allocated, before any other allocation is made under section 704(b) of partnership items for such taxable year, items of income and gain for such year (and, if necessary, subsequent years) in the amount and in the proportions needed to eliminate such deficits as quickly as possible. For purposes of the preceding sentence, partners' capital accounts shall be reduced for the items described in paragraph (b)(2)(ii)(*d*)(*4*), (*5*), and (*6*) of this section.** Allocations of items of income and gain made pursuant to a minimum gain chargeback shall be deemed to be made in accordance with the partners' interests in the partnership if requirements (*1*) and (*2*) of paragraph (b)(2)(ii)(*b*) of this section are satisfied. The minimum gain chargeback allocated in any taxable year shall consist first of gains recognized from the disposition of items of partnership property subject to one or more nonrecourse liabilities of the partnership to the extent of the decrease in minimum gain attributable to the disposition of such items of property, with the remainder of such minimum gain chargeback, if any, made up of a pro rata portion of the partnership's other items of income and gain for that year. If, however, such gains exceed the amount of the minimum gain chargeback, a proportional share of each such gain shall constitute a part of the minimum gain chargeback. For purposes of paragraph (b)(2)(ii)(*d*)(*6*) of this section, offsetting increases to a partner's capital account taken into account under that paragraph shall not include income and gain that is expected to be allocated to such partner pursuant to a minimum gain chargeback.

(f) Partner's share of partnership minimum gain. A partner's share of partner-

ship minimum gain at the end of any partnership taxable year equals the aggregate nonrecourse deductions allocated to such partner (and such partner's predecessors in interest) up to that time, less such partner's (and such predecessors') aggregate share of the net decreases in partnership minimum gain up to that time. A partner's share of the net decrease in partnership minimum gain during a partnership taxable year equals an amount that bears the same relation to the net decrease in partnership minimum gain during such year as such partner's share of partnership minimum gain at the end of the prior taxable year of the partnership (or, if later, at the time immediately following the last time that the capital accounts of the partners are increased pursuant to paragraph (b)(2)(iv)(*f*) of this section to reflect a revaluation of partnership property subject to one or more nonrecourse liabilities of the partnership) bears to the amount of partnership minimum gain at the end of such prior taxable year (or such later date). See examples (20)(i) and (iv) and (21) of this paragraph (b)(5) of this section. In addition, if there is a decrease in partnership minimum gain in a taxable year of the partnership (whether or not there is a net decrease in partnership minimum gain during such year) attributable to the revaluation of partnership property subject to one or more nonrecourse liabilities of the partnership, each partner's share of partnership minimum gain as of the time of such revaluation shall be reduced by the amount of the increase in such partner's capital account attributable to such revaluation to the extent of the reduction in minimum gain caused by such revaluation. See example (22)(ii) of paragraph (b)(5) of this section. For purposes of paragraph (b)(2)(ii)(*d*) of this section, the amount of a partner's share of minimum gain shall be added to the limited dollar amount, if any, of the deficit balance in such partner's capital account that such partner is obligated to restore. See examples (20)(i) and (22)(i) of paragraph (b)(5) of this section.

(*g*) *Nonrecourse liabilities of the partnership where a partner has economic risk of loss.* The rationale for the special rule contained in this paragraph (b)(4)(iv) is that, in the event there is an economic burden that corresponds to the nonrecourse deductions, none of the partners will bear that burden. Accordingly, for purposes of this paragraph, a nonrecourse liability of the partnership is a liability of the partnership (or portion thereof) with respect to which none of the partners has any economic risk of loss (other than through their interests as partners in the partnership assets subject to the liability). Therefore, to the extent a partner may bear the burden of an economic loss corresponding to a loss, deduction, or section 705(a)(2)(B) expenditure attributable to a partnership liability that would be considered nonrecourse for purposes of §1.1001–2 (*e.g.*, a purported nonrecourse loan made by such partner to the partnership or guaranteed by such partner), allocations of such loss, deduction, or section 705(a)(2)(B) expenditure are not governed by this paragraph (b)(4)(iv). Instead, allocations of such loss or deduction shall be made in accordance with the partners' interests in the partnership under paragraph (b)(3) of this section. This will require allocations of such loss or deduction to be made to the partner or partners who bear the burden of an economic loss corresponding to such loss or deduction. See example (20)(vii) and (viii) of paragraph (b)(5) of this section.

(*h*) *Nonrecourse liabilities of the partnership where a person related to a partner has economic risk of loss.* [Reserved]

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(5) *Examples.* * * *

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Example (20). (i) RM and HB form a limited partnership to acquire and operate a commercial office building. RM, the limited partner, contributes $180,000, and HB, the general partner, contributes $20,000 to the partnership, which obtains an $800,000 nonrecourse loan and purchases the building (on leased land) for $1,000,000. The nonrecourse loan is secured only by the building, and no principal payments are due for 5 years. The partnership agreement provides that the partners' capital accounts will be determined and maintained in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances (as set forth in paragraph (b)(2)(ii)(*b*)(*2*) of this section), HB will be required to restore any deficit balance in his capital account following the liquidation of his interest (as set forth in paragraph (b)(2)(ii)(*b*)(*3*) of this section), and RM will not be required to restore any deficit balance in his capital account following the liquidation of his interest. The partnership agreement contains a qualified income offset (as defined in paragraph (b)(2)(ii)(*d*) of this section), and, as of the end of each partnership taxable year discussed herein, the items described in paragraphs (b)(2)(ii)(*d*)(*4*), (*5*), and (*6*) of this section are not reasonably expected to cause or increase a deficit balance in RM's capital account. In addition, the agreement contains a minimum gain chargeback (in accordance with paragraph (b)(4)(iv)(*e*) of this section). The partnership agreement provides that, except as otherwise required by its qualified income offset and minimum gain chargeback provisions, (a) all partnership items will be allocated 90 percent to RM and 10 percent to HB until the first time when the partnership has recognized items of income and gain that exceed the items of loss and deduction it has recognized over its life, and (b) all further partnership items will be allocated equally between RM and HB. Finally, the partnership agreement provides that all distributions, other than distributions in liquidation of the partnership or of a partner's interest in the partnership, will be made 90 percent to RM and 10 percent to HB until a total of $200,000 has been distributed, and thereafter all such distributions will be made equally to RM and HB. In each of the partnership's first 2 taxable years, it generates rental income of $95,000, operating expenses (including land lease payments) of $10,000, interest expense of $80,000, and a cost recovery deduction of $90,000, resulting in a net taxable loss of $85,000 in each of those years. The allocations of these losses 90 percent to RM and 10 percent to HB have substantial economic effect.

	RM	*HB*
Capital account upon formation	$180,000	$20,000
Less: net loss in years 1 and 2	(153,000)	(17,000)
Capital account at end of year 2	$27,000	$3,000

In the partnership's third taxable year, it again generates rental income of $95,000, operating expenses of $10,000, interest expense of $80,000, and a cost recovery deduction of $90,000, resulting in a net taxable loss of $85,000. If the partnership were to dispose of the building in full satisfaction of the nonrecourse liability at the end of that year, it would realize $70,000 of gain ($800,000 amount realized less $730,000 adjusted tax basis). Since the amount of partnership minimum gain at the end of that year (and the net increase in partnership minimum gain during that year) is $70,000, the amount of partnership nonrecourse deductions for that year is $70,000, consisting of cost recovery deductions allowable with respect to the building of $70,000. Pursuant to the partnership agreement all partnership items comprising the net taxable loss of $85,000, including the $70,000 nonrecourse deduction, are allocated 90 percent to RM and 10 percent to HB. The allocation of these items, other than the nonrecourse deductions, has substantial economic effect.

	RM	*HB*
Capital account at end of year 2	$27,000	$3,000
Less: net loss in year 3 (without nonrecourse deduction)	(13,500)	(1,500)
Less: nonrecourse deduction in year 3	(63,000)	(7,000)
Capital account at end of year 3	(49,500)	($5,500)

This allocation of the $70,000 nonrecourse deduction 90 percent to RM and 10 percent to HB satisfies requirement (*2*) of paragraph (b)(4)(iv)(*d*) of this section because the allocation is consistent with allocations, which have substantial economic effect, of other significant partnership items attributable to the building. Since the remaining requirements of paragraph (b)(4)(iv)(*d*) of this section are satisfied, the allocation of nonrecourse deductions is deemed to be made in accordance with the partners' interests in the partnership. At the end of the partnership's third taxable year, RM's and HB's shares of partnership minimum gain are $63,000 and $7,000, respectively. Therefore, pursuant to the next to last sentence in paragraph (b)(4)(iv)(*f*) of this section, RM is treated as obligated to restore a deficit balance in his capital account of $63,000, so that in the succeeding year RM could be allocated up to an additional $13,500 of partnership deductions, losses, and section 705(a)(2)(B) expenditures that are not nonrecourse deductions, and that allocation would be considered to have economic effect under the alternate economic effect test contained in paragraph (b)(2)(ii)(*d*) of this section even though such an allocation would increase a deficit capital account balance. If the partnership were to dispose of the building in full satisfaction of the nonrecourse liability at the beginning of the partnership's fourth taxable year (and had no other economic activity in that year), the partnership minimum gain would be decreased from $70,000 to zero. RM's and HB's shares of that net decrease would be $63,000 and $7,000, respectively. Upon such a disposition the minimum gain chargeback would require that RM be allocated an amount of that gain equal to $49,500 (the deficit balance in his capital account before any allocation is made to him under section 704(b) with respect to partnership items for the partnership's fourth taxable year).

(ii) Assume the same facts as originally stated in (i) except that the partnership agreement provides that all nonrecourse deductions of the partnership will be allocated equally between RM and HB. Furthermore, at the time the partnership agreement is entered into, there is a reasonable likelihood that over the partnership's life it will recognize amounts of income and gain significantly in excess of amounts of loss and deduction (other than nonrecourse deductions). The allocation of such excess equally between the partners pursuant to the partnership agreement will have substantial economic effect. The allocation of all items, other than the nonrecourse deductions, 90 percent to RM and 10 percent to HB has substantial economic effect.

	RM	*HB*
Capital account upon formation	$180,000	$20,000
Less: net loss in years 1 and 2	(153,000)	(17,000)
Capital account at end of year 2	27,000	3,000
Less: net loss in year 3 (without nonrecourse deduction)	(13,500)	(1,500)
Less: nonrecourse deduction in year 3	(35,000)	(35,000)
Capital account at end of year 3	($21,500)	($33,500)

The allocation of the $70,000 nonrecourse deduction equally between RM and HB satisfies requirement (2) of paragraph (b)(4)(iv)(*d*) of this section because the allocation is consistent with allocations, which will have substantial economic effect, of other significant partnership items attributable to the building. Since the remaining requirements of paragraph (b)(4)(iv)(*d*) of this section are satisfied, the allocation of nonrecourse deductions is deemed to be made in accordance with the partners' interests in the partnership. The allocation of the nonrecourse deductions 75 percent to RM and 25 percent to HB (or in any other ratio between 90 percent to RM/10 percent to HB and 50 percent to RM/50 percent to HB) also would satisfy requirement (2) of paragraph (b)(4)(iv)(*d*) of this section.

(iii) Assume the same facts as originally stated in (i) except that the partnership agreement provides that RM will be allocated 99 percent, and HB 1 percent, of all nonrecourse deductions of the partnership. This allocation of the $70,000 nonrecourse deduction does not satisfy requirement (2) of paragraph (b)(4)(iv)(*d*) because it is not reasonably consistent with allocations which have substantial economic effect, of any other significant partnership item attributable to the building. Therefore, the allocation of nonrecourse deductions will be disregarded, and the nonrecourse deductions of the partnership will be reallocated according to the partners' overall economic interests in the partnership, determined with reference to the factors set forth in paragraph (b)(3)(ii) of this section.

(iv) Assume the same facts as originally stated in (i) except that, at the beginning of the partnership's fourth taxable year, RM contributes $144,000 and HB contributes $16,000 of additional capital to the partnership, which the partnership uses to reduce the amount of its nonrecourse liability from $800,000 to $640,000. In addition, in the partnership's fourth taxable year, it again generates rental income of $95,000, operating expenses of $10,000, and a cost recovery deduction of $90,000, resulting in a net taxable loss of $85,000. If the partnership were to dispose of the building in full satisfaction of the nonrecourse liability at the end of that year, it would realize no gain ($640,000 amount realized less $640,000 adjusted tax basis). Therefore, the amount of partnership minimum gain at the end of the year is zero, which represents a net decrease in partnership minimum gain of $70,000 during the year. RM's and HB's shares of this net decrease are $63,000 and $7,000, respectively, so that at the end of the partnership's fourth taxable year, RM's and HB's shares of partnership's fourth taxable year, RM's and HB's shares of partnership minimum gain are zero. Therefore, pursuant to the next to last sentence in paragraph (b)(4)(iv)(*f*) of this section, RM is no longer treated as being obligated to restore any deficit balance in his capital account. Assuming the sum of the reductions to RM's capital account described in paragraph (b)(2)(ii)(*d*)(*4*), (*5*), and (*6*) of this section do not exceed $94,500, the minimum gain chargeback does not require that either RM or HB be allocated items of income and gain in the partnership's fourth taxable year even though there is a net decrease in partnership minimum gain during that year. This is true because at the end of the year, before any allocation is made under section 704(b) to RM with respect to partnership items for the fourth taxable year, RM's capital account balance is $94,500 (his capital account balance at the end of the partnership's third taxable year increased by his $144,000 capital contribution), and HB has a full deficit makeup obligation.

	RM	*HB*
Capital account at end of year 3	($49,500)	($5,500)
Plus: contribution	144,000	16,000
Less: net loss in year 4	(76,500)	(8,500)
Capital account at end of year 4	$18,000	$2,000

(v) Assume the same facts as originally stated in (i) except that the partnership incurred only a $700,000 nonrecourse loan and, in addition, incurred a $100,000 recourse loan, subordinate in priority to the nonrecourse loan, to which the partnership's building is also subject. Under paragraph (b)(4)(iv)(*c*) of this section, $700,000 of the adjusted basis of the building at the end of the partnership's third taxable year is allocated to the nonrecourse liability (with the remaining $30,000 allocated to the recourse liability) so that if the partnership disposed of the building in full satisfaction of the nonrecourse liability at the end of that year, it would realize no gain ($700,000 amount realized less $700,000 adjusted tax basis). Therefore, there is no minimum gain at the end of the partnership's third taxable year (and no increase in partnership minimum gain in such year). If, however, the $700,000 nonrecourse loan were subordinate in priority to the $100,000 recourse loan, under paragraph (b)(4)(iv)(*c*) of this section, only $630,000 of the adjusted basis of the building would be allocated to the $700,000 nonrecourse loan (the excess of the $730,000 adjusted tax basis of the building at the end of the partnership's third taxable year over the balance of the superior $100,000 recourse liability). In that case the balance of the $700,000 nonrecourse liability would exceed the adjusted tax basis of the building so allocated by $70,000 so that there would be $70,000 of minimum gain (and a $70,000 increase in partnership minimum gain) in the partnership's third taxable year.

(vi) Assume the same facts as originally stated in (i) except that RM and HB personally guarantee the "first" $100,000 of the $800,000 nonrecourse loan (*i.e.*, only if the building is worth less than $100,000 will they be called upon to make up any deficiency). Under paragraph (b)(4)(iv)(*c*) of this section, only $630,000 of the adjusted tax basis of the building is allocated to the 700,000 nonrecourse portion of the loan because the collateral will be applied first to satisfy the $100,000 guaranteed portion, in effect making it superior in priority to the remainder of the loan. On the other hand, if RM and HB were to guarantee the "last" $100,000 (*i.e.*, if the building is worth less than $800,000, they will be called upon to make up the deficiency up to $100,000), $700,000 of the adjusted tax basis of the building would be allocated to the $700,000 nonrecourse portion of the loan because the guaranteed portion in effect would be inferior in priority to it.

(vii) Assume the same facts as originally stated in (i) except that the $800,000 loan is made by HB, the general partner. Under paragraph (b)(4)(iv)(*g*) of this section, the $800,000 obligation does not constitute a nonrecourse liability of the partnership for purposes of this paragraph (b)(4)(iv). To the extent that such obligation constitutes a nonrecourse liability under §1.1001–2, $70,000 of the $90,000 cost recovery deduction in the partnership's third taxable year must be allocated in accordance with the partners' interests in the partnership, under paragraph (b)(3) of this section. HB bears the burden of any economic loss corresponding to that $70,000 deduction. Therefore, HB must be allocated the entire amount of such deduction.

(viii) Assume the same facts as in (vii) except that the $800,000 loan from HB to the partnership is a purchase money loan that "wraps around" a $700,000 underlying nonrecourse note (also secured by the building) issued by HB to an unrelated person in connection with HB's acquisition of the building. Under these circumstances if the partnership were to convey the building to HB in satisfaction of the partnership's $800,000 liability, HB would bear the economic risk of loss with respect to only $100,000 of the liability. Therefore, for purposes of this paragraph (b)(4)(iv), the $800,000 liability will be treated as a $700,000 nonrecourse liability of the partnership and a $100,000 liability (inferior in priority to the $700,000 liability) of the partnership to HB. Under paragraph (b)(4)(iv)(*g*) of this section, the $100,000 liability does not constitute a nonrecourse liability of the partnership for purposes of this paragraph (b)(4)(iv). To the extent that such obligation constitutes a nonrecourse liability under §1.1001–2, $70,000 of the $90,000 cost recovery deduction realized in the partnership's third taxable year must be allocated to HB.

Example (21). (i) RD and PK form a general partnership to acquire and operate residential real properties. Each partner contributes $150,000 to the partnership. The partnership obtains a $1,500,000 nonrecourse loan and purchases 3 apartment buildings (on leased land) for $720,000 ("Property A"), $540,000 ("Property B"), and $540,000 ("Property C") respectively. The nonrecourse loan is secured only by the 3 buildings, and no principal payments are due for 5 years. In each of the partnership's first 3 taxable years, it generates rental income of $225,000, operating expenses (including land lease payments) of $50,000, interest expense of $175,000, and cost recovery deductions on the 3 properties of $150,000 ($60,000 on Property A, $45,000 on Property B, and $45,000 on Property C), resulting in a net taxable loss of $150,000 in each of those years. If the partnership were to dispose of the 3 apartment buildings in full satisfaction of its nonrecourse liability at the end of its third taxable year, it would realize $150,000 of gain ($1,500,000 amount realized less $1,350,000 adjusted tax basis). Since the amount of partnership minimum gain at the end of that year (and the net increase in partnership minimum gain during that year) is $150,000, the amount of partnership nonrecourse deductions for that year is $150,000, consisting of cost recovery deductions allowable with respect to the 3 apartment buildings of $150,000. The result would be the same if the partnership obtained 3 separate nonrecourse loans that were "cross-collateralized" (*i.e.*, if each separate loan were secured by all 3 of the apartment buildings).

(ii) Assume the same facts as originally stated in (i) and that at the beginning of the partnership's fourth taxable year, the partnership (with the permission of the nonrecourse lender) disposes of Property A for $835,000 and uses a portion of the proceeds to repay $600,000 of the nonrecourse liability, reducing the balance to $900,000. As a result of the disposition, the partnership recognizes gain of $295,000 ($835,000 amount realized less $540,000 adjusted tax basis). Also during the partnership's fourth taxable year it generates rental income of $135,000 and operating expenses of $30,000, interest expense of $150,000, and cost recovery deductions of $90,000 ($45,000 on each remaining building). If the partnership were to dispose of the remaining 2 buildings in full satisfaction of its nonrecourse liability at the end of the partnership's fourth taxable year, it would realize gain of $180,000 ($900,000 amount realized less $720,000 aggregate adjusted tax basis), which represents the amount of partnership minimum gain at the end of such year. Since the amount of partnership minimum gain increased from $150,000 to $180,000 during the partnership's fourth taxable year, the amount of partnership nonrecourse deductions for such year is $30,000, consisting of cost recovery deductions allowable with respect to the 2 remaining apartment buildings.

Example (22). (i) OC and DR form a limited partnership to acquire and lease machinery that is 5-year recovery property. OC, the limited partner, and DR, the general partner, contribute $100,000 each to the partnership, which obtain an $800,000 nonrecourse loan and purchases the equipment for $1,000,000. The partnership elects under section 48(q)(4) to reduce the amount of investment tax credit in lieu of adjusting the tax basis of such machinery. The nonrecourse loan is secured only by the machinery. The principal amount of the loan is to be repaid $50,000 per year during each of the partnership's first 5 taxable years, with the remaining $550,900 of unpaid principal due on the first day of the partnership's sixth taxable year. the partnership agreement provides that the partners' captial accounts will be determined and maintaned in accordance with paragraph (b)(2)(iv) of this section, distributions in liquidation of the partnership (or any partner's interest) will be made in accordance with the partners' positive capital account balances (as set forth in paragraph (b)(2)(ii)(*b*)(*2*) of this section), DR will be required to restore any deficit balance in his capital account following the liquidation of his interest (as set forth in paragraph (b)(2)(ii)(*b*)(*3*) of this section), and OC will not be required to restore any deficit balance in his capital account following the liquidation of his interest. The partnership agreement contains a qualified income offset (as defined in paragraph (b)(2)(ii)(*d*) of this section), and, as of the end of each partnership taxable year discussed herein, the items described in paragraphs (b)(2)(ii)(*d*)(*4*), and (*5*), and (*6*) of this section are not reasonably expected to cause or increase a deficit balance in RM's capital account. In addition, the agreement contains a minimum gain chargeback (in accordance with paragraph (b)(4)(iv)(*e*) of this section). The partnership agreement provides that, except as otherwise required by its qualified income offset and minimum gain chargeback provisions, all partnership items will be allocated equally between OC and DR. Finally, the partnership agreement provides that all distributions, other than distributions in liquidation of the partnership or of a partner's interest in the partnership, will be made equally between OC and DR. In the partnership's first taxable year, it generates rental income of $130,000, interest expense of $80,000, and a cost recovery deduction of $150,000, resulting in a net taxable loss of $100,000. In addition, the partnership repays $50,000 of the nonrecourse liability, reducing that liability to $750,000. Allocations of these losses equally between OC and DR have substantial economic effect.

	OC	*DR*
Capital account upon formation	$100,000	$100,000
Less: net loss in year 1	(50,000)	(50,000)
Captial account at end of year 1	$50,000	$50,000

In the partnership's second taxable year it generates rental income of $130,000, interest expense of $75,000, and a cost recovery deduction of $220,000, resulting in a net taxable loss of $165,000. In addition, the partnership repays $50,000 of the nonrecourse liability, reducing that liability to $700,000, and distributes $2,500 of cash to each partner. If the partnership were to dispose of the machinery in full satisfaction of the nonrecourse liability at the end of that year, it would realize $70,000 of gain ($700,000 amount realized less $630,000 adjusted tax basis). Therefore, the amount of partnership minimum gain at the end of that year (and the net increase in partnership minimum gain during that year) is $70,000, and the amount of partnership nonrecourse deductions for that year is $70,000, consisting of cost recovery deductions allowable with respect to the machinery of $70,000. Pursuant to the partnership agreement all partnership items comprising the net taxable loss of $165,000, including the $70,000 nonrecourse deduction, are allocated equally between OC and DR. The allocation of these items, other than the nonrecourse deductions, has substantial economic effect.

	OC	*DR*
Capital account at end of year 1	$50,000	$50,000
Less: net loss in year 2 (without nonrecourse deduction)	(47,500)	(47,500)
Less: nonrecourse deduction in year 2	(35,000)	(35,000)
Less: distribution	(2,500)	(2,500)
Capital account at end of year 2	($35,000)	($35,000)

This allocation of the $70,000 nonrecourse deduction equally between OC and DR satisfies requirement (2) of paragraph (b)(4)(iv)(*d*) of this section because the allocation is consistent with allocations, which have substantial economic effect, of other significant partnership items attributable to the machinery. Since the remaining requirements of paragraph (b)(4)(iv)(*d*) of this section are satisfied, the allocation of nonrecourse deductions is deemed to be made in accordance with the partners' interests in the partnership. At the end of the partnership's second taxable year, OC's and DR's shares of partnership minimum gain are $35,000 each. Therefore, pursuant to the next to last sentence in paragraph (b)(4)(iv)(*f*) of this section, OC is treated as obligated to restore a deficit balance in his capital account of $35,000. If the partnership were to dispose of the machinery in full satisfaction of the nonrecourse liability at the beginning of the partnership's third taxable year (and had no other economic activity in that year), the partnership minimum gain would be decreased from $70,000 to zero. OC's and DR's shares of that net decrease would be $35,000 each. Upon such a disposition the minimum gain chargeback would require that OC be allocated an amount of that gain equal to $35,000 (the deficit balance in his capital account before any allocation is made to him under section 704(b) with respect to partnership items for the partnership's third taxable year). The minimum gain chargeback would not require that DR be allocated any amount of such gain, since he has a full deficit makeup obligation.

(ii) Assume the same facts as originally stated in (i) and that DT is admitted to the partnership at the beginning of the partnership's third taxable year. At the time of DT's admission, the fair market value of the machinery is $900,000. DT contributes $100,000 to the partnership (which amount the partnership invests in undeveloped land) in exchange for an interest in the partnership. Pursuant to paragraph (b)(2)(iv)(*f*) of this section, the capital accounts of OC and DR are adjusted upward to $100,000 each. This reflects the manner in which the partnership gain of $270,000 ($900,000 fair market value minus $630,000 adjusted basis) would be shared if the machinery were sold for its fair market value immediately prior to DT's admission to the partnership.

	OC	*DR*
Capital account before DT's admission	($35,000)	($35,000)
Deemed sale adjustment	135,000	135,000
Capital account adjusted for DT's admission	$100,000	$10,000

The partnership agreement is modified to provide that, except as otherwise required by its qualified income offset and minimum gain chargeback provisions, partnership income, gain, loss, and deduction, as computed for book purposes, will be allocated equally among the partners, and such allocations will be reflected in the partners' capital accounts. The partnership agreement also is modified to provide that depreciation and gain or loss, as computed for tax purposes, with respect to the machinery will be shared among the partners in a manner that takes account of the variation between such property's $630,000 adjusted tax basis and its $900,000 book value, in accordance with paragraph (b)(2)(iv)(*f*) of this section and the special rule contained in paragraph (b)(4)(i) of this section. Finally, the partnership agreement is modified to provide that DT will not be required to restore any deficit balance in his capital account following the liquidation of his interest. Since the requirements of paragraph (b)(2)(iv)(*g*) of this section are satisfied, the capital accounts of the partners (as adjusted) continue to be maintained in accordance with paragraph (b)(2)(iv) of this section. If the partnership were to dispose of the machinery in full satisfaction of the nonrecourse liability immediately following the revaluation of the machinery, it would realize no book gain ($700,000 amount realized less $900,000 book value). Thus, as a result of the revaluation of the machinery upward by $270,000, the partnership minimum gain is reduced from $70,000 immediately prior to such revaluation to zero. OC's and DR's shares of that decrease are $35,000 each.

(iii) Assume the same facts as in (ii) and that also during the partnership's third taxable year the partnership generates rental income of $130,000, interest expense of $70,000, a cost recovery deduction of $210,000, and a book depreciation deduction (attributable to the machinery) of $300,000. As a result the partnership has a net taxable loss of $150,000 and a net book loss of $240,000. In addition, the partnership repays $50,000 of the noncourse liability (after the date of DT's admission), reducing that liability to $650,000, and distributes $3,333 of cash to each partner. If the partnership were to dispose of the machinery in full satisfaction of the nonrecourse liability at the end of the year, $50,000 of book gain would result ($650,000 amount realized less $600,000 book value). Therefore, the amount of partnership minimum gain at the end of the year is $50,000, which represents a net decrease in partnership minimum gain of $20,000 during the year. (This is so even though there would be an increase in partnership minimum gain in the partnership's third taxable year if minimum gain were computed with reference to the adjusted tax basis of the machinery.) Nevertheless, pursuant to the second sentence of paragraph (b)(4)(iv)(*d*) of this section the amount of nonrecourse deductions of the partnership for its third taxable year is $50,000 (the net increase in partnership minimum gain during the year determined by adding back the $70,000 decrease in partnership minimum gain attributable to the revaluation of the machinery to the $20,000 net decrease in partnership minimum gain during the year). The $50,000 of partnership nonrecourse deductions for the year consist of book depreciation deductions allowable with respect to the machinery of $50,000. Pursuant to the partnership agreement all partnership items comprising the net book loss of $240,000, including the $50,000 nonrecourse deduction, are allocated equally among the partners. The allocation of these items, other than the nonrecourse deductions, has substantial economic effect. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the $210,000 cost recovery deduction for the partnership's third taxable year is, in accordance with section 704(c) principles, shared $55,000 to OC, $55,000 to Dr, and $100,000 to DT.

The allocation of the $50,000 nonrecourse deduction equally among OC, DR, and DT satisfies requirement (2) of paragraph (b)(4)(iv)(*d*) of this section because the allocation is consistent with allocations, which have substantial economic effect, of other significant partnership items attributable to the machinery. Since the remaining requirements of paragraph (b)(4)(iv)(*d*) of this section are satisfied, such allocation is deemed to be made in accordance with the partners' interest in the partnership. At the end of the partnership's third taxable year, OC's, DR's, and DT's shares of partnership minimum gain are $16,666 each.

	OC		*DR*		*DT*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account at end of year 2	($35,000)	$100,000	($35,000)	$100,000	$100,000	$100,000
Less: nonrecourse deduction	(9,166)	(16,666)	(9,166)	(16,666)	(16,666)	(16,666)
Plus: items other than nonrecourse deduction in year 3	(25,834)	(63,334)	(25,834)	(63,334)	(63,334)	(63,334)
Less: Distribution	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)
Capital account at end of year 3	($75,000)	$15,000	($75,000)	$15,000	$15,000	$15,000

(iv) Assume the same facts as in (iii) and that during the partnership's fourth taxable year the partnership generates rental income of $130,000, interest expense of $65,000, a cost recovery deduction of $210,000, and a book depreciation deduction (attributable to the machinery) of $300,000. As a result the partnership has a net taxable loss of $145,000 and a net book loss of $235,000. In addition, the partnership repays $50,000 of the nonrecourse liability, reducing that liability to $600,000, and distributes $5,000 of cash to each partner. If the partnership were to dispose of the machinery in full satisfaction of the nonrecourse liability at the end of the year, $300,000 of book gain would result ($600,000 amount realized less $300,000 book value). Therefore, the amount of partnership minimum gain as of the end of the year is $300,000, which represents a net increase in partnership minimum gain during the year of $250,000. Thus, the amount of partnership nonrecourse deductions for that year equals $250,000, consisting of book depreciation deductions of $250,000. Pursuant to the partnership agreement all partnership items comprising the net book loss of $235,000, including the $250,000 nonrecourse deduction, are allocated equally among the partners. That allocation of all items, other than the nonrecourse deductions, has substantial economic effect. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the $210,000 cost recovery deduction for the partnership's fourth taxable year is, in accordance with section 704(c) principles, shared $55,000 to OC, $55,000 to DR, and $100,000 to DT.

	OC		*DR*		*DT*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account at end of year 3	($75,000)	$15,000	($75,000)	$15,000	$15,000	$15,000
Less: nonrecourse deduction	(45,833)	(83,333)	(45,833)	(83,333)	(83,333)	(83,333)
Plus: items other than nonrecourse deduction in year 4	12,499	5,000	12,499	5,000	5,000	5,000
Less: Distribution	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)
Capital account at end of year 4	($113,334)	($68,333)	($113,334)	($68,333)	($68,333)	($68,333)

The allocation of the $250,000 nonrecourse deduction equally among OC, DR, and DT satisfies requirement (2) of paragraph (b)(4)(iv)(*d*) of this section. Since the remaining requirments of paragraph (b)(4)(iv)(*d*) of this section are satisfied, such allocation is deemed to be made in accordance with the partners' interest in the partnership. At the end of the partnership's third taxable year, OC's, DR's, and DT's shares partnership minimum gain are $100,000 each.

(v) Assume the same facts as (iv) and that at the beginning of the partnership's fifth taxable year it sells the machinery for $65,000 (using $600,000 of the proceeds to repay the nonrecourse liability), resulting in a taxable gain of $440,000 ($650,000 amount realized less $210,000 adjusted tax basis) and a book gain of $350,000 ($650,000 amount realized less $300,000 book basis). The partnership has no other items of income, gain, loss, or deduction for such year. As a result of the sale, partnership minimum gain is reduced from $300,000 to zero, reducing OC's, DR's, and DT's shares of partnership minimum gain to zero from $100,000 each. The minimum gain chargeback requires that OC and DT each be allocated an amount of that gain equal to $68,333 (the deficit balance in each of their capital accounts at the end of the partnership's fifth taxable year before any allocation is made to them under section 704(b) with respect to partnership items for that year). Thus, the allocation of the first $136,666 of book gain $68,333 to OC and $68,333 to DT is deemed to be made in accordance with the partners' interests in the partnership under paragraph (b)(4)(iv)(*e*) of this section. The allocation of the remaining $213,334 of book gain in a manner such that the total book gain is allocated equally among the partners has substantial economic effect. Consistent with the special partner's interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the $440,000 taxable gain is, in accordance with section 704(c) principles, shared $161,667 to OC, $161,667 DR, and $116,666 to DT.

	OC		*DR*		*DT*	
	Tax	*Book*	*Tax*	*Book*	*Tax*	*Book*
Capital account at end of year 4	($113,334)	($68,333)	($113,334)	($68,333)	($68,333)	($68,333)
Plus: minimum gain chargeback	94,691	68,333	—0—	—0—	68,333	68,333
Plus: additional gain	66,976	48,333	161,667	116,666	48,333	48,333
Capital account before liquidation	$48,333	$48,333	$48,333	$48,333	$48,333	$48,333

Example 23: (i) A partnership owns 4 properties, each of which is subject to a nonrecourse liability of the partnership. During a taxable year of the partnership, the following events take place. First, the partnership generates a cost recovery deduction (for both book and tax purposes) with respect to Property W of $10,000 and repays $5,000 of the nonrecourse liability secured only by that property, resulting in an increase in minimum gain with respect to that liability of $5,000. Second, the partnership generates a cost recovery deduction (for both book and tax purposes) with respect to Property X of $10,000 and repays none of the nonrecourse liability secured by that property, resulting in an increase in minimum gain with respect to that liability of $10,000. Third, the partnership generates a cost recovery deduction (for both book and tax purposes) of $2,000 on Property Y and repays $11,000 of the nonrecourse liability secured only by that property, resulting in a decrease in minimum gain with respect to that liability of $9,000 (although at the end of that year, there remains minimum gain with respect to that liability). Finally, the partnership borrows $5,000 on a nonrecourse basis giving as the only security for that liability Property Z, which is a parcel of undeveloped land with an adjusted tax basis (and book value) of $2,000, resulting in a net increase in minimum gain with respect to that liability of $3,000. The net increase in partnership minimum gain during that year is $9,000, so that the amount of nonrecourse deductions of the partnership for that taxable year is $9,000. Those nonrecourse deductions consist of $3,000 of cost recovery deductions with respect to Property W and $6,000 of cost recovery deductions with respect to Property X. The amount of nonrecourse deductions consisting of cost recovery deductions is determined as follows. With respect to the nonrecourse liability secured by Property Z, with respect to which there is no cost recovery deduction, the amount of cost recovery deductions that constitutes nonrecourse deductions is zero. Similarly, with respect to the noncourse liability secured by Property Y, for which there is no increase in minimum gain, the amount of cost recovery deductions that constitutes nonrecourse deductions is zero. With respect to each of the nonrecourse liabilities secured by Properties W and X, which are (i) secured by property with respect to which there are cost recovery deductions and (ii) for which there is an increase in minimum gain, the amount of cost recovery deductions that constitutes nonrecourse deductions equals the product obtained by multiplying the net increase in partnership minimum gain ($9,000) times a fraction, the numerator of which is the total cost recovery deductions with respect to the partnership property securing that particular liability to the extent of the increase in minimum gain with respect to that liability and the denominator of which is the sum of the numerators for each such liabilty. Thus, for the liability secured by Property W, the amount is $9,000 times $5,000/$15,000. For the liability secured by Property X, the amount is $9,000 times $10,000/$15,000. (If one depreciable property secured 2 partnership nonrecourse liabilities, the amount of cost recovery or book depreciation with respect to that property would be allocated among such liabilities in accordance with the method by which adjusted basis is allocated under paragraph (b)(2)(iv)(*b*) of this section.)

(ii) Assume the facts as in (i) except that the loan secured by Property Z is $15,000 (rather than $5,000), resulting in a net increase in minimum gain with respect to that liability of $13,000. Thus, the net increase in partnership minimum gain is $19,000, and the amount of nonrecourse deductions of the partnership for that taxable year is $19,000. Those nonrecourse deductions consist of $5,000 of cost recovery deductions with respect to Property W, $10,000 of cost recovery deductions with respect to Property X, and a pro rata portion of the partnership's other items of deduction, loss, and section 705(a)(2)(B) expenditure for that year. The method for computing the amounts of cost recovery deductions that constitute nonrecourse deductions is the same as in (i) for the liabilities secured by Properties Y and Z. With respect to each of the nonrecourse liabilities secured by Properties W and X, the amount of cost recovery deductions that constitutes nonrecourse deductions equals the total cost recovery deductions with respect to the partnership property securing that particular liability to the extent of the increase in minimum gain with respect to that liability.

Par. 3. Section 1.704–1(b) is further amended as follows:

1. Paragraph (b)(1)(i) is amended by inserting the word "three" immediately after the phrase "there are" in the second sentence thereof.

2. Paragraph (b)(1)(ii) is amended by inserting immediately after the phrase "May 1, 1986" the first time it appears in the second sentence thereof, the parenthetical phrase "(January 1, 1987, in the case of allocations of nonrecourse deductions as defined in paragraph (b)(4)(iv)(*a*) of this section)" and by deleting the phrase "as that term has" in the last sentence of that unit and adding in its place the phrase "or is in accordance with the partners' interests in the partnership as those terms have."

3. Paragraph (b)(1)(iii) is amended by adding a new sentence immediately before the last sentence to read as follows: "A deduction that appears to be a nonrecourse deduction deemed to be in accordance with the partners' interests in the partnership may not be such because purported nonrecourse liabilities of the partnership in fact constitute equity rather than debt."

4. Paragraph (b)(2)(ii)(*b*) is amended by inserting immediately before the last sentence thereof the following two new sentences: "Requirements (*2*) and (*3*) of this paragraph (b)(2)(ii)(*b*) are not violated if all or part of the partnership interest of one or more partners is purchased (other than in connection with the liquidation of the partnership) by the partnership or by one or more partners (or one or more persons related, within the meaning of section 267(b) (without modification by section 267(e)(1)) or section 707(b)(1), to a partner) pursuant to an agreement negotiated at arm's length by persons who at the time such agreement is entered into have materially adverse interests and if a principal purpose of such purchase and sale is not to avoid the principles of the second sentence of paragraph (b)(2)(ii)(*a*) of this section. In addition, requirement (*2*) of this paragraph (b)(2)(ii)(*b*) is not violated if, upon the liquidation of the partnership, the capital accounts of the partners are increased or decreased pursuant to paragraph (b)(2)(iv)(*f*) of this section as of the date of such liquidation and the partnership makes liquidating distributions within the time set out in that requirement (*2*) in the ratios of the partners' positive capital accounts, except that it does not distribute (*A*) reserves reasonably required to provide for liabilities (contingent or otherwise) of the partnership and (*B*) installment obligations owed to the partnership, so long as such withheld amounts are distributed as soon as practicable and in the ratios of the partners' positive capital account balances."

5. Paragraph (b)(2)(ii)(*d*) is amended by adding the parenthetical phrase "(other than increases pursuant to a minimum gain chargeback under paragraph (b)(4)(iv)(*e*) of this section)" to the end of the only sentence in (*6*) thereof, by adding the parenthetical phrase "(consisting of a pro rata portion of each item of partnership income, including gross income, and gain for such year)" in the penultimate sentence of that unit immediately after the phrase "income and gain," and by adding immediately before the last sentence of such unit a new sentence to read as follows: "Allocations of items of income and gain made pursuant to the immediately preceding sentence shall be deemed to be made in accordance with the partners' interests in the partnership if requirements (*1*) and (*2*) of paragraph (b)(2)(ii)(*b*) of this section are satisfied."

6. Paragraph (b)(2)(ii)(*f*) is amended by replacing the cross-reference to "(*4*), and (*5*), and (*6*) of paragraph (b)(2)(iv)(*d*) of this section" in the first sentence thereof with the cross-reference to "(*4*), (*5*), and (*6*) of paragraph (b)(2)(ii)(*d*) of this section."

7. Paragraph (b)(2)(ii)(*h*) is amended by adding the following new sentence immediately after the second sentence thereof: "(Thus, for example, if one partner who assumes a liability of the partnership is indemnified by another partner for a portion of such liability, the indemnifying partner (depending upon the particular facts) may be viewed as in effect having a partial deficit makeup obligation as a result of such indemnity agreement.)", and by adding at the end of the last sentence a new phrase to read as follows: "or partnership."

8. Paragraph (b)(2)(ii)(*i*) is amended by revising the first sentence thereof to read as follows: "Allocations made to a partner that do not otherwise have economic effect under this paragraph (b)(2)(ii) shall nevertheless be deemed to have economic effect, provided that as of the end of each partnership taxable year a liquidation of the partnership at the end of such year or at the end of any future year would produce the same economic results to the partners as would occur if requirements (*1*), (*2*), and (*3*) of paragraph (b)(2)(ii)(*b*) of this section had been satisfied, regardless of the economic performance of the partnership."

9. Paragraph (b)(2)(iii)(*c*) is amended by adding immediately after the parenthetical "(under this paragraph (b)(2)(iii)(*c*))" a new clause to read as follows:" and, for purposes of paragraph (b)(2)(iii)(*a*), it will be presumed that there is a reasonable possibility that the allocations will affect substantially the dollar amounts to be received by the partners from the partnership" and by deleting the phrase "(i) and (iv)" after "(7)."

10. Paragraph (b)(2)(iv)(*b*) is amended by deleting the word "securing" in the two places that it appears and by adding the phrase "secured by" in each such place.

11. Paragraph (b)(2)(iv)(*c*) is amended by revising the last sentence thereof to read as follows: "For purposes of this paragraph (b)(2)(iv)(*c*), liabilities are considered assumed only to the extent the assuming party is thereby subjected to personal liability with respect to such obligation, the obligee is aware of the assumption and can directly enforce the assuming party's obligation, and, as between the assuming party and the party from whom the liability is assumed, the assuming party is ultimately liable."

12. Paragraph (b)(2)(iv)(*d*)(*3*) is amended by revising the parenthetical phrase in the first sentence thereof to read "(see paragraph (b)(1)(vi) of this section)."

13. Paragraph (b)(2)(iv)(*f*) is amended by inserting the parenthetical phrase "(including intangible assets such as goodwill)" in the first sentence thereof immediately after the phrase "partnership property."

14. Paragraph (b)(2)(iv)(*f*)(*5*)(*ii*) is amended by inserting the phrase "the liquidation of the partnership or" immediately after the phrase "connection with."

15. Paragraph (b)(2)(iv)(*g*)(*3*) and (*m*)(*4*) is revised to read as set forth below:

Section 1.704–1 Partner's distributive share.

* * * * *

(b) *Determination of a partner's distributive share.* * * *

(2) *Substantial economic effect.* * * *

(iv) *Maintenance of capital accounts.* * * *

(*g*) *Adjustments to reflect book value.* * * *

(*3*) *Determining amount of book items.* The partners' capital accounts will not be considered adjusted in accordance with this paragraph (b)(2)(iv)(*g*) unless the amount of book depreciation, depletion, or amortization for a period with respect to an item of partnership property is the amount that bears the same relationship to the book value of such property as the depreciation (or cost recovery deduction), depletion, or amortization computed for tax purposes with respect to such property for such period bears to the adjusted tax basis of such property. If such property has a zero adjusted tax basis, the book depreciation, depletion, or amortization may be determined under any reasonable method selected by the partnership.

* * * * *

(*m*) *Section 754 elections.* * * *

(*4*) *Section 734 adjustments.* Except as provided in paragraph (b)(2)(iv)(*m*)(*5*) of this section, in the case of a distribution of property in liquidation of a partner's interest in the partnership by a partnership that has a section 754 election in effect for the partnership taxable year in which the distribution occurs, the partner who receives the distribution that gives rise to the adjustment to the adjusted tax basis of partnership property under section 734 shall have a corresponding adjustment made to his capital account. If such distribution is made other than in liquidation of a partner's interest in the partnership, however, except as provided in paragraph (b)(2)(iv)(*m*)(*5*) of this section, the capital accounts of the partners shall be adjusted by the amount of the adjustment to the adjusted tax basis of partnership property under section 734, and such capital account adjustment shall be shared among the partners in the manner in which the unrealized income and gain that is displaced by such adjustment would have been shared if the property whose basis is adjusted were sold immediately prior to such adjustment for its recomputed adjusted tax basis.

* * * * *

16. Paragraph (b)(2)(iv)(*j*) is amended by deleting the sentence "See example (2)(iii) of paragraph (b)(5) of this section."

17. Paragraph (b)(2)(iv)(*r*) is revised to read as follows:

(*r*) *Restatement of capital accounts.* With respect to partnerships that began operating in a taxable year beginning before May 1, 1986, the capital accounts of the partners of which have not been determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) since inception, such capital accounts shall not be considered to be determined and maintained in accordance with the rules of this paragraph (b)(2)(iv) for taxable years beginning after April 30, 1986, unless either—

(*1*) such capital accounts are adjusted, effective for the first partnership taxable year beginning after April 30, 1986, to reflect the fair market value of partnership property as of the first day of such taxable year, and in connection with such adjustment, the rules contained in paragraph (b)(2)(iv)(*f*)(*2*), (*3*), and (*4*) of this section are satisfied, or

(*2*) the differences between the balance in each partner's capital account and the balance that would be in such partner's capital account if capital accounts had been determined and maintained in accordance with this paragraph (b)(2)(iv) throughout the full term of the partnership are not significant (for example, such differences are solely attributable to a failure to provide for treatment of section 709 expenses in accordance with the rules of paragraph (b)(2)(iv)(*i*)(*2*) of this section or to a failure to follow the rules in paragraph (b)(2)(iv)(*m*) of this section), and capital accounts are adjusted to bring them into conformity with the rules of this paragraph (b)(2)(iv) no later than the end of the first partnership taxable year beginning after April 30, 1986.

However, compliance with the previous sentence will have no bearing on the validity of allocations that relate to partnership taxable years beginning before May 1, 1986.

18. Paragraph (b)(3)(i) is amended by deleting the phrase "with respect" in the first sentence thereof and adding in its place the phrase "(if any) corresponding," and by adding the phrase "Except with respect to partnership items that cannot have economic effect (such as nonrecourse deductions of the partnership),"

at the beginning of the second sentence thereof, and by adding immediately after the third sentence thereof a new sentence to read as follows: "(For example, in the case of an unexpected downward adjustment to the capital account of a partner who does not have a deficit make-up obligation that causes such partner to have a negative capital account, it may be necessary to allocate a disproportionate amount of gross income of the partnership to such partner for such year so as to bring that partner's capital account back up to zero.)"

19. Paragraph (b)(3)(iii) is amended by deleting the phrase "(i), (ii), and (iv)" after "(7)."

20. Paragraph (b)(4)(i) is amended by deleting the word "made" immediately before the phrase "in accordance with" in the third sentence thereof and by adding in its place the word "determined."

21. The second sentence of paragraph (b)(4)(v) is amended by deleting the word "are" the first time it appears and inserting in its place the word "is," by inserting the word "material" immediately after the phrase "and (*b*) all other," and by deleting the phrase "this paragraph" and by inserting in its place "this paragraph (b)."

22. *Example* (1) (ix) of paragraph (b)(5) is amended by adding the word "negotiable" immediately before the term "promissory note" in the first sentence thereof.

23. *Example* (7) (i) of paragraph (b)(5) is amended by adding a parenthesis after the phrase "deficit to the partnership" in the fourth sentence thereof.

24. *Example* (7) (iii) of paragraph (b)(5) is amended by deleting the phrase "general rules" and inserting in its place the phrase "second sentence" in the penultimate sentence thereof.

25. *Example* (13) (i) of paragraph (b)(5) is amended by adding immediately after the fourth sentence thereof a new sentence to read as follows: "The partnership uses the interim closing of the books method for purposes of section 706."

26. *Example* (14) (i) of paragraph (b)(5) is amended by adding immediately after the fourth sentence thereof a new sentence to read as follows: "The partnership uses the interim closing of the books method for purposes of section 706."

27. *Example* (18) (iii), is amended by in changing WN to WM in the penultimate sentence thereof.

28. *Example* (18) (vii) of paragraph (b)(5) is modified by deleting the phrase "under those principles MK must" in the last sentence thereof and adding in its place the phrase "under these facts those principles require MK to."

29. *Example* (18) (viii) of paragraph (b)(5) is amended by deleting the last two sentences thereof and by adding in their place two new sentences to read as follows: "Assume further that upon MK's admission WM and JL have adjusted capital account balances of $110,000 and $100,000, respectively. Consistent with the special partners' interests in the partnership rule contained in paragraph (b)(4)(i) of this section, the partnership agreement provides that the excess $10,000 cost recovery deduction ($110,000 less $100,000 included in MK's distributive share) is, in accordance with section 704 (c) principles, shared equally between WM and JL and is so included in their respective distributive shares for the partnership's third taxable year."

Par. 4. Section 1.704–1 (b)(0) is amended by adding, each on a separate line, the following lines to the table immediately after the line reference to 1.704–1(b)(4)(iv):

Allocation of nonrecourse deductions	1.704–1(b)(4)(iv)(*a*)
Determination of nonrecourse deductions	1.704–1(b)(4)(iv)(*b*)
Partnership minimum gain	1.704–1(b)(4)(iv)(*c*)
Requirements to be satisfied	1.704–1(b)(4)(iv)(*d*)
Minimum gain chargeback	1.707–1(b)(4)(iv)(*e*)
Partner's share of partnership minimum gain	1.704–1(b)(4)(iv)(*f*)
Nonrecourse liabilities of the partnership where a partner has economic risk of loss	1.704–1(b)(4)(iv)(*g*)
Nonrecourse liabilities of the partnership where a person related to a partner has economic risk of loss	1.704–1(b)(4)(iv)(*h*)

Lawrence B. Gibbs,
Commissioner.

Approved August 27, 1986.

J. Roger Mentz,
Assistant Secretary of the Treasury.

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Section 809.—Reduction in Certain Deductions of Mutual Life Insurance Companies

Mutual life insurance companies; differential earnings rate. The differential earnings rate for 1985 and the recomputed differential earnings rate for 1984 are set forth for use by mutual life insurance companies to compute their income tax liability for 1985.

Rev. Rul. 86–114

This revenue ruling contains the differential earnings rate for 1985 and the recomputed differential earnings rate for 1984. Under section 809 of the Internal Revenue Code, mutual life insurance companies use these rates in computing their income tax liability for 1985. This ruling also contains some of the figures on which the determinations of these rates are based. Announcement 86–36, 1986–12 I.R.B. 27, contained tentative determinations of these same rates.

Section 809(a) of the Code provides that, in the case of any mutual life insurance company, the amount of the deduction allowable under section 808 for policyholder dividends shall be reduced (but not below zero) by the "differential earnings amount." Any excess of the differential earnings amount over the amount of the deduction allowable under section 808 shall be taken into account as a reduction in the closing balance of reserves under subsections (a) and (b) of section 807. The "differential earnings amount "for any taxable year is an amount equal to the product of (a) the life insurance company's average equity base for the taxable year multiplied by (b) the "differential earnings rate" for such taxable year. The "differential earnings rate" for a taxable year is the excess of (a) the "imputed earnings rate" for the taxable year over (b) the "average mutual earnings rate" for the second calendar year preceding the calendar year in which the taxable year begins. The "imputed earnings rate" for any taxable year beginning after 1984 is an amount which bears the same ratio to 16.5 percent as the "current stock earnings rate" for the taxable year bears to the "base period stock earnings rate."

Section 809(f) of the Code provides that, in the case of any mutual life insurance company, if the "recomputed differential earnings amount" for any taxable year exceeds the differential earnings amount for such taxable year, such excess shall be included in life insurance gross income for the succeeding taxable year. If the differential earnings amount for any taxable year exceeds the recomputed differential earnings amount for such year, such excess shall be allowed as a life insurance deduction for the succeeding taxable year. The "recomputed differential earnings amount" for any taxable year is an amount calculated in the same manner as the differential earnings amount for such taxable year, but substituting the average mutual earnings rate for the calendar year in which the taxable year begins for the average mutual earnings rate for the second calendar year preceding the calendar year in which the taxable year begins. For example, the differential earnings rate for 1985 is based on the average mutual earnings rate for 1983, and the recomputed differential earnings rate for 1985 is based on the average mutual earnings rate for 1985.

For purposes of section 809 of the Code, the differential earnings rate for 1985, the rate used to calculate the recomputed differential earnings amount for 1984 (the "recomputed differential earnings rate" for 1984), and the figures on which these two rates are based are as follows:

Differential earnings rate for 1985	6.157 percent
Recomputed differential earnings rate for 1984	10.570 percent
Imputed earnings rate for 1985	16.323 percent
Base period stock earnings rate	18.221 percent
Current stock earnings rate for 1985	18.026 percent
Stock earnings rate for 1981	17.316 percent
Stock earnings rate for 1982	18.812 percent
Stock earnings rate for 1983	18.535 percent
Stock earnings rate for 1984	16.731 percent
Average mutual earnings rate for 1983	10.166 percent
Average mutual earnings rate for 1984	5.930 percent

Regulations under section 809 of the Code have not yet been issued, and when these regulations are issued, they may be effective for a period prior to the date of their issuance. Even if that is the case, however, in determining the rates that are to be used in computing 1985 tax liability, the Service will not change the procedures that governed its determination of the rates announced in this revenue ruling. For instance, for purposes of computing 1985 tax liability, the Service will not change the administrative procedures that controlled which companies' data were used in determining the two rates announced in this revenue ruling. (The rates are based on data from domestic companies only.) Regulations or other pronouncements, however, may result in a change in these and other procedures for determination of the rates to be used in computing the tax liability of subsequent years.

Section 817.—Treatment of Variable Contracts

26 CFR 1.817-5T: Diversification requirements for variable annuity, endowment, and life insurance contracts.

T.D. 8101

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER A, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Diversification Requirements for Variable Annuity, Endowment, and Life Insurance Contracts

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to the diversification requirements for variable annuity, endowment, and life insurance contracts. In addition, the text of the temporary regulations set forth in this document serves as the text of the proposed regulations * * * [page 21, this Bulletin]. Changes to the applicable tax law were made by the Tax Reform Act of 1984. The regulations affect issuers and policyholders of variable contracts and provide them with guidance concerning the tax treatment of those contracts.

DATES: The regulations are effective generally, to variable annuity, endowment, and life insurance contracts for taxable years beginning after December 31, 1983. (See §1.817-5T(h)(10)(i).)

FOR FURTHER INFORMATION CONTACT: Alice M. Bennett of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T), (202) 566-3238, not a toll-free call.

SUPPLEMENTARY INFORMATION: BACKGROUND

This document amends the Income Tax Regulations (26 CFR Part 1) to provide rules under section 817(h) of the Internal Revenue Code of 1954, relating to diversification requirements for variable annuity, endowment, and life insurance contracts. Section 817(h) was added to the Code by section 211(a) of the Tax Reform Act of 1984 (Pub. L. 98-369, 98 Stat. 750).

EXPLANATION OF PROVISIONS

Section 817(h) authorizes the Secretary of the Treasury to prescribe diversification standards for the investments underlying a variable annuity, endowment, or life insurance contract and provides that a variable contract generally will not be treated as an annuity, endowment, or life insurance contract unless those standards are satisfied. A safe harbor is provided, however, for variable contracts based on a segregated asset account that satisfies the diversification requirements applicable to regulated investment companies and does not hold more than 55 percent of its assets in cash, cash items, Government securities, and securities of regulated investment companies. In addition, and exception from the diversification requirement permits variable life insurance contracts to be based on a segregated asset account that holds only Treasury securities.

The temporary regulations provide that the investments of a segregated asset account underlying a variable contract are adequately diversified if no more than 55 percent of the value of its assets is represented by any one investment, no more than 70 percent is represented by any two investments, no more than 80 percent is represented by any three investments, and no more than 90 percent is represented by any four investments. A special rule is provided for segregated asset accounts underlying variable life insurance contracts. Under this rule, a segregated asset account is adequately diversified if it satisfies the general diversification requirement or if its assets other than Treasury securities are adequately diversified. For purposes of determining whether assets other than Treasury securities are adequately diversified, the generally applicable percentage limitations are increased, with the amount of the increase depending on the value of the Treasury securities.

The temporary regulations also provide that segregated asset accounts will be considered adequately diversified during start-up and liquidation periods. An account is generally allowed one year for each purpose. In the case of a real property account, however, the start-up period is five years and the liquidation period is two years. The start-up period is reduced or is not available in certain circumstances to prevent the use of multiple start-up periods to avoid the diversification requirement. In general, this limitation applies if more than 30 percent of the amount allocated to an account as of any date was shifted from another segregated asset account and is attributable to premium income received more than one year before such date (or five years before such date in the case of a real property account). The limitation is not taken into account for purposes of determining whether a start-up period would be allowed under the principles of Rev. Rul. 81–225, 1981–2 C.B. 12. Thus, the transitional rule for cases in which an insurance company would be considered the owner of the assets of a segregated asset account under those principles is applied without regard to the limitation. Under the transitional rule that limitation will not apply until December 15, 1986.

The temporary regulations treat all Government securities as a single investment for purposes of the diversification requirements. In general, any security (including a cash item) that is issued, guaranteed, or insured by the United States or an instrumentality of the United States is treated as a Government security for this purpose. Under a transitional rule, however, debt instruments secured by a mortgage on real property or representing an interest in a pool of debt instruments secured by such mortgages will not be treated as Government securities before 1987, even if issued, guaranteed, or insured by the United States or an instrumentality of the United States.

The temporary regulations in this document do not address any issues other than the diversification standards applicable to variable annuity, endowment, and life insurance contracts. In particular, they do not provide guidance concerning the circumstances in which investor control of the investments of a segregated asset account may cause the investor, rather than the insurance company, to be treated as the owner of the assets in the account. For example, the temporary regulations provide that in appropriate cases a segregated asset account may include multiple sub-accounts, but do not specify the extent to which policyholders may direct their investments to particular sub-accounts without being treated as owners of the underlying assets. Guidance on this and other issues will be provided in regulations or revenue rulings under section 817(d), relating to the definition of variable contract.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required. No general notice of proposed rulemaking is required by 5 U.S.C. 553 for temporary regulations. Accordingly, a Regulatory Flexibility Analysis is not required (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal authors of these regulations are Bruce H. Jurist and Linda M. Kroening of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * * *

Amendments to the regulations.

The amendments to 26 CFR Part 1 are as follows:

INCOME TAX REGULATIONS
(26 CFR Part 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 1.817–5T also issued under 26 U.S.C. 817(h).

Par. 2. Section 1.817–5T is revised to read as follows:

§1.817–5T Diversification requirements for variable annuity, endowment, and life insurance contracts.

(a) *In general.* For purposes of subchapter L, section 72, and section 7702(a), a variable contract (as defined in section 817(d)), other than a pension plan contract (as defined in section 818(a)), which is based on one or more segregated asset accounts shall not be treated as an annuity, endowment, or life insurance contract for any period for which the investments of any such account are not adequately diversified. In addition, a variable contract that is not treated as an annuity, endowment, or life insurance contract for any period by reason of the preceding sentence shall not be treated as an annuity, endowment, or life insurance contract for any subsequent period even if the investments are adequately diversified for such subsequent period. See sections 7702(g) and (h) for the treatment of a variable contract which is not treated as an annuity, endowment, or life insurance contract for Federal income tax purposes but which is a life insurance or endowment contract under other applicable (*e.g.*, State or foreign) law.

(b) *Diversification of investments*—(1) *In general.* (i) Except as otherwise provided in this paragraph and paragraph (c) of this section, the investments of a segregated asset account shall be considered adequately diversified for purposes of this section and section 817(h) only if—

(A) No more than 55% of the value of the total assets of the account is represented by any one investment;

(B) No more than 70% of the value of the total assets of the account is represented by any two investments;

(C) No more than 80% of the value of the total assets of the account is represented by any three investments; and

(D) No more than 90% of the value of the total assets of the account is represented by any four investments.

(ii) For purposes of this section—

(A) All securities of the same issuer, all interests in the same real property project, and all interests in the same commodity are each treated as a single investment;

(B) All government securities are treated as securities of a single issuer; and

(C) The members of an affiliated group (within the meaning of section 1504(a), determined without regard to the exceptions in section 1504(b)) ordinarily are treated as a single issuer.

(2) *Safe harbor.* A segregated asset account will be considered adequately diversified for purposes of this section and section 817(h) if—

(i) The account meets the requirements of section 851(b)(4) and the regulations thereunder; and

(ii) No more than 55% of the value of the total assets of the account is attributable to cash, cash items (including receivables), Government securities, and securities of other regulated investment companies.

(3) *Alternative diversification requirements for variable life insurance contracts.*

(i) A segregated asset account with respect to variable life insurance contracts will be considered adequately diversified for purposes of this section and section 817(h) if the requirements of paragraph (b)(1) or (b)(2) of this section are satisfied or if the assets of such account, other than Treasury securities, satisfy the percentage limitations prescribed in paragraph (b)(1) of this section increased by the product of (A) .5 and (B) the percentage of the value of the total assets of the account that is represented by Treasury securities. In determining whether the assets of an account, other than Treasury securities, satisfy the increased percentage limitations, such limitations are applied as if the Treasury securities were not included in the account (*i.e.*, the increased percentage limitations are not applied to Treasury securities and the value of the total assets of the account is reduced by the value of the Treasury securities).

(ii) See paragraphs (f) and (g) of this section for circumstances in which a segregated asset account is treated as the owner of Treasury securities held indirectly through certain pass-through entities and corporations taxed under subchapter M, chapter 1 of the Code.

(iii) The provisions of this paragraph (b)(3) may be illustrated by the following examples:

Example (1). On the last day of a quarter of a calendar year, a segregated asset account with respect to variable life insurance contracts holds assets having a total value of $100,000. The assets of the account are represented by Treasury securities having a total value of $90,000 and securities of Corporation A having a total value of $10,000. The 55% limit described in paragraph (b)(1)(i) of this section would be increased by 45% (0.5 × 90%) to 100%, and would then be applied to the assets of the account other than Treasury securities. Because no more than 100% of the value of the assets other than Treasury securities is represented by securities of Corporation A, the investments of the account will be considered adequately diversified.

Example (2). On the last day of a quarter of a calendar year, a segregated asset account with respect to variable life insurance contracts holds assets having a total value of $100,000. The assets of the account are represented by Treasury securities having a total value of $60,000, securities of Corporation A having a total value of $30,000, and securities of Corporation B having a total value of $10,000. The 55% and 70% limits described in paragraph (b)(1)(i) of this section would be increased by 30% (0.5 × 60%) to 85% and 100%, respectively, and would then be applied to the assets of the account other than Treasury securities. Securities of Corporation A represent 75%, and securities of Corporation B represent 25%, of the value of the assets of the account other than Treasury securities. Because no more than 85% of the value of the assets other than Treasury securities is represented by securities of Corporation A or B and no more than 100% of the value of the assets other than Treasury securities is represented by securities of Corporations A and B, the investments of the account will be considered adequately diversified.

(c) *Periods for which an account is adequately diversified*—(1) *In general.* A segregated asset account that satisfies the requirements of paragraph (b) of this section on the last day of a quarter of a calendar year (*i.e.*, March 31, June 30, September 30, and December 31) or within 30 days after such last day shall be considered adequately diversified for such quarter.

(2) *Start-up period.* (i) Except as provided in paragraph (c)(2)(iv) of this section, a segregated asset account that is not a real property account on its first anniversary shall be considered adequately diversified until such first anniversary.

(ii) Except as provided in paragraph (c)(2)(iv) of this section, a segregated asset account that is a real property account on its first anniversary shall be considered adequately diversified until the earlier of its fifth anniversary or the anniversary on which the account ceases to be a real property account.

(iii) For purposes of paragraph (c)(2)(i) and (ii) of this section, the anniversary of a segregated asset account is the anniversary of the date on which any amount received under a life insurance or annuity contract is first allocated to the account.

(iv) If more than 30 percent of the amount allocated to a segregated asset account as of any date is attributable to premium and investment income that was received more than one year before such date, paragraph (c)(2)(i) of this section shall not apply to the segregated asset account for any period after such date. Similarly, if more than 30 percent of the amount allocated to a segregated asset account as of any date is attributable to premium and investment income that was received more than 5 years before such date, paragraph (c)(2)(ii) of this section shall not apply to the segregated asset account for any period after such date. For this purpose, premium income is treated as received on the date on which such income is first received with respect to the variable contract (or with respect to any predecessor variable contract exchanged for the variable contract in a transaction to which section 1035 applied) and investment income is treated as received on the date on which such income is first credited to a segregated asset account on which such variable contract (or predecessor contract) is based. Also for this purpose, an amount allocated to a segregated asset account shall be treated as attributable to the most recently received premium and investment income.

(3) *Liquidation period.* A segregated asset account that satisfies the requirements of paragraph (b) of this section on the date a plan of liquidation is adopted shall be considered adequately diversified for—

(i) The one-year period beginning on the date the plan of liquidation is adopted if the account is not a real property account on such date; or

(ii) The two-year period beginning on the date the plan of liquidation is adopted if the account is a real property account on such date.

(d) *Aggregation of multiple accounts or funds*. Two or more accounts or funds are treated as a single segregated asset account for purposes of section 817(h) and this section only if the investment return and market value of each such account or fund must be allocated to the same variable contracts and in the identical proportions as the investment return and market value of each other such account or fund. This rule may be illustrated by the following example:

Example. Variable contracts are based on an account that consists of five sub-accounts. The contract provides that policyholders of variable contracts based on the account may specify what portion of each premium is to be invested in a particular subaccount, subject to the restriction that no more than 55% of any premium may be invested in any one sub-account, no more than 70% may be invested in any two sub-accounts, no more than 80% may be invested in any three sub-accounts, and no more than 90% may be invested in any four sub-accounts. The return on a variable contract based on this account will be computed with regard to the allocation of premiums among the sub-accounts. Thus, the investment return and market value of a sub-account may be allocated to different variable contracts or in different proportions than the investment return and market value of the other sub-accounts. Accordingly, each sub-account is treated as a separate segregated asset account for purposes of section 817(h) and this section. If any of the five sub-accounts fails to be adequately diversified, any variable contract based in part on the sub-account will not be treated as a variable annuity or life insurance contract.

(e) *Market fluctuations*. A segregated asset account that satisfies the requirements of paragraph (b) of this section at the end of any calendar quarter (or within 30 days after the end of such calendar quarter) shall not be considered nondiversified in a subsequent quarter because of a discrepancy between the value of its assets and the diversification requirements unless such discrepancy exists immediately after the acquisition of any asset and such discrepancy is wholly or partly the result of such acquisition.

(f) *Look-through rule for underlying investment company or trust*—(1) *In general.* If this paragraph applies, a beneficial interest in a regulated investment company, a real estate investment trust, or a trust that is treated under sections 671 through 679 as owned by the grantor or another person ("investment company or trust") shall not be treated as a single investment of a segregated asset account. Instead, a pro rata portion of each asset of the investment company or trust shall be treated, for purposes of this section, as an asset of the segregated asset account. In the case of a regulated investment company having one or more segregated portfolios of assets in respect of which a series of stock is preferred over all other series, each segregated portfolio of assets will be treated solely for purposes of this paragraph as a separate regulated investment company.

(2) *Applicability.* This paragraph shall apply if—

(i) All the beneficial interests in the investment company or trust (other than those described in paragraph (f)(3) of this section) are held by one or more segregated asset accounts of one or more insurance companies; and

(ii) Public access to such investment company or trust is available exclusively (except as otherwise permitted in paragraph (f)(3) of this section) through the purchase of a variable contract.

(3) *Interests not held by segregated asset accounts.* The application of this paragraph shall not be prevented by reason of beneficial interests in the investment company or trust that are—

(i) Held by the general account of a life insurance company or a corporation related in a manner specified in section 267(b) to a life insurance company, but only if the return on such interests is computed in the same manner as for the related variable contracts, there is no intent to sell such interests to the public, and a segregated asset account of such life insurance company also holds or will hold a beneficial interest in the investment company or trust;

(ii) Held by the manager, or a corporation related in a manner specified in section 267(b) to the manager, of the investment company or trust, but only if the holding of the interests is in connection with the creation or management of the investment company or trust, the return on such interests is computed in the same manner as for the related variable contracts, and there is no intent to sell such interests to the public;

(iii) Held by the trustee of a qualified pension or retirement plan; or

(iv) Held by the public, or treated as owned by policyholders pursuant to Rev. Rul. 81–225, 1981–2 C.B. 12, but only if (A) the investment company or trust was closed to the public in accordance with Rev. Rul. 82–55, 1982–1 C.B. 12, (B) all the assets of the investment company or trust are attributable to premium payments made by policyholders prior to September 26, 1981, or (C) all the assets of the investment company or trust are attributable to premium payments made in connection with a qualified pension or retirement plan.

(g) *Look-through rule for underlying partnership interest.* If a segregated asset account holds a partnership interest, other than a partnership interest registered under a Federal or State law regulating the offering or sale of securities, the segregated asset account will be deemed to own its proportionate share of each of the assets of the partnership. For purposes of this section, the interest of a partner in a partnership's assets shall be determined in accordance with his capital interest in the partnership.

(h) *Definitions.* The terms defined below shall, for purposes of this section, have the meanings set forth in such definitions:

(1) *Government security.* The term "government security" shall mean any security issued or (to the extent of the guaranteed or insured amount) guaranteed or insured by the United States or an instrumentality of the United States; or any certificate of deposit for any of the foregoing. For purposes of this paragraph (h)(1), an instrumentality of the United States shall mean any person that is treated for purposes of 15 U.S.C. 80a–2 (16), as amended, as a person controlled or supervised by and acting as an instrumentality of the Government of the United States pursuant to authority granted by the Congress of the United States.

(2) *Treasury security.* The term "Treasury security" shall mean a security the direct obligor of which is the United States Treasury.

(3) *Real property.* The term "real property" shall mean any property that is treated as real property under §1.856–3(d) except that it shall not include interests in real property.

(4) *Real property account.* A segregated asset account is a real property account on an anniversary of the account (within the meaning of paragraph (c)(2)(iii) of this section) or on the date a plan or liquidation is adopted if not less than the applicable percentage of the total assets of the account is represented by real property or interests in real property on such anniversary or date. For this purpose, the applicable percentage is 40% for the period ending on the first anniversary of the date on which premium income is first received, 50% for the year ending on the second anniversary, 60% for the year ending on the third anniversary, 70% for the year ending on the fourth anniversary, and 80% thereafter.

(5) *Commodity.* The term "commodity" shall mean any type of personal property other than a security.

(6) *Security.* The term "security" shall include a cash item and any partnership interest registered under a Federal or State law regulating the offering or sale of securities. The term shall not include any other partnership interest, any interest in real property, or any interest in a commodity.

(7) *Interest in real property.* The term "interest in real property" shall include the ownership and co-ownership of land or improvements thereon and leaseholds of land or improvements thereon. Such term shall not, however, include mineral, oil, or gas royalty interests, such as a retained economic interest in coal or iron ore with respect to which the special provisions of section 631(c) apply. The term "interest in real property" also shall include options to acquire land or improvements thereon, and options to acquire leaseholds of land or improvements thereon.

(8) *Interest in a commodity.* The term "interest in a commodity" shall include the ownership and co-ownership of any type of personal property other than a security, and any leaseholds thereof. Such term shall include mineral, oil, and gas royalty interests, including any fractional undivided interest therein. Such term also shall include any put, call, straddle, option, or privilege on any type of personal property other than a security.

(9) *Value.* The term "value" shall mean, with respect to investments for which market quotations are readily available, the market value of such investments; and with respect to other investments, fair value as determined in good faith by the managers of the segregated asset account.

(10) *Terms used in section 851.* To the extent not inconsistent with this para-

graph (h) all terms used in this section shall have the same meaning as when used in section 851.

(i) *Effective date*—(1) *In general.* This section is effective for taxable years beginning after December 31, 1983.

(2) *Exceptions.* (i) If, at all times after December 31, 1983, an insurance company would be considered the owner of the assets of a segregated asset account under the principles of Rev. Rul. 81–225, 1981–2 C.B. 12, this section will not apply to such account until December 15, 1986.

(ii) This section will not apply to any variable contract to which Rev. Rul. 77–85, 1977–1 C.B. 12, or Rev. Rul. 81–225, 1981–2 C.B. 12, did not apply by reason of the limited retroactive effect of such rulings.

(iii) In determining whether a segregated asset account is adequately diversified for any calendar quarter ending before July 1, 1987, debt instruments that are issued, guaranteed or insured by the United States or an instrumentality of the United States shall not be treated as Government securities if such debt instruments are secured by a mortgage on real property (other than real property owned by the United States or an instrumentality of the United States) or represent an interest in a pool of debt instruments secured by such mortgages.

There is need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it would be impractical to issue it first under the notice and comment procedure provided in 5 U.S.C. 553(b) or subject to the effective date limitation of 5 U.S.C. 553(d).

ROSCOE L. EGGER, JR.,
Commissioner
of Internal Revenue.

Approved August 15, 1986.

J. ROGER MENTZ
Acting Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on September 12, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 15, 1986, 51 F.R. 32633)

Section 1001.—Determination of Amount of and Recognition of Gain or Loss

26 CFR 1.1001–1: Computation of gain or loss.

Federal income tax consequences of a transfer of property in payment of state inheritance tax liability. See Rev. Rul. 86-117, this page.

Section 1014.—Basis of Property Acquired from a Decedent

26 CFR 1.1014–2: Property acquired from a decedent.

Basis of property acquired by the decedent's estate from the decedent. See Rev. Rul. 86–117, this page.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 280G, 467, 468, 483, 7882.)

Rev. Rul. 86–115

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of October 1986 are as follows:

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term				
AFR	6.09%	6.00%	5.96%	5.93%
110% AFR	6.71%	6.60%	6.55%	6.51%
120% AFR	7.33%	7.20%	7.14%	7.09%
Mid-Term				
AFR	6.97%	6.85%	6.79%	6.75%
110% AFR	7.68%	7.54%	7.47%	7.42%
120% AFR	8.39%	8.22%	8.14%	8.08%
Long-Term				
AFR	7.42%	7.29%	7.22%	7.18%
110% AFR	8.18%	8.02%	7.94%	7.89%
120% AFR	8.94%	8.75%	8.66%	8.59%

Section 2011.—Credit For State Death Taxes

26 CFR 20.2011–1: Credit for State death taxes.
(Also Sections 1001, 1014; 1.1001–1, 1.1014–2.)

Credits against tax; property transferred in payment of state inheritance tax liability. The payment of state inheritance taxes in property other than cash constitutes "taxes actually paid" to the state for purposes of the federal estate tax credit. The amount "actually paid" is the lesser of the state inheritance tax liability discharged by the transfer of the property or the fair market value of the property on the date of the transfer. The estate realizes gain or loss upon the transfer measured by the difference between the estate's basis in the property and the amount of the state tax liability that was discharged.

Rev. Rul. 86–117

ISSUES

1. Does the payment of state inheritance taxes with property, in lieu of cash, pursuant to state law, constitute "taxes actually paid" to a state for purposes of the federal estate tax credit under section 2011 of the Internal Revenue Code?

2. If so, does the estate realize gain or loss upon the disposition of property in payment of state inheritance tax liability?

FACTS

The decedent, *D*, a resident of state *ST*, died on April 16, 1984. Under the laws of *ST*, the inheritance tax liability of any beneficiary, heir, surviving joint tenant, or other transferee may be paid by the transfer of money, property other than money, or both, to the state or to a political subdivision of the state. In-kind payments of the tax liability by a transfer of property other than money are permitted only where the property will be used for public purposes and are subject to approval and acceptance by the governmental entity that receives the property.

Twelve months after *D*'s death, *D*'s executor filed a state inheritance tax return and, in part payment of the inheritance tax liability, transferred to the local political subdivision of *ST* a parcel of real estate that at the time had a fair market value of $77,000. The *ST* taxing authority certified that *ST*'s acceptance of the property constituted payment of $77,000 in satisfaction of the estate's inheritance tax liability. The executor filed a timely federal estate tax return in which the value of the transferred property was included as a part of *D*'s gross estate. On the federal estate tax return, the executor did not elect the alternate valuation date prescribed by section 2032 of the Code. The parcel was therefore included in the gross estate at its date of death fair market value, which was $70,000. After satisfying the state inheritance tax liability, *D*'s executor filed for a federal estate tax refund. The claim for refund was based on the payment of state inheritance taxes, including the $77,000 payment made by transferring the real estate.

LAW AND ANALYSIS

Section 2011 of the Code provides that, within the limitations of section 2011(b), the tax imposed by section 2001 shall be credited with the amount of any estate, inheritance, legacy or succession taxes actually paid to any state or the District of Columbia, in respect of any property included in the gross estate (not including any taxes paid with respect to the estate of a person other than the decedent).

Section 2011(c) provides that, in general, the credit allowed for state taxes described above shall include only such taxes as were actually paid and credit therefor claimed within 4 years after the filing of the estate tax return.

Section 2011 is specific that the amount for which a credit is claimed must be "actually paid." However, neither the Code nor the Estate Tax Regulations limit the medium of payment of state death taxes that qualify for the credit under section 2011 to cash payments.

Rev. Rul. 74–178, 1974–1 C.B. 196, holds that when an executor transfers appreciated property in settlement of a claim against the estate, the estate realizes gain measured by the excess of the amount of the claim over the estate's basis in the property.

Section 1001(a) of the Code provides, in part, that the gain from the disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 1011 for determining gain.

Section 1011(a) of the Code provides, in part, that the adjusted basis for determining the gain from the disposition of property shall be the basis determined under the applicable provisions of the Code.

Section 1014(a) of the Code provides, generally, that the basis of property in the hands of a person acquiring the property from a decedent shall be the fair market value of the property at the date of the decedent's death or, where there is an appropriate election, at the alternate valuation date as provided in section 2032.

The amount actually paid to a state or subdivision for state death taxes is not always equivalent to the amount of the tax liability discharged by the payment. For example, if a state accepts $2,000 in settlement of a tax liability of $3,000 dollars, the amount actually paid for purposes of section 2011 is $2,000. *See Commonwealth Trust Co. of Pittsburgh v. Driscoll,* 50 F. Supp. 949 (W.D. Pa. 1943), *aff'd per curiam,* 137 F.2d 653 (3d Cir. 1943), *cert. denied,* 321 U.S. 764 (1944), and *Smith v. Commissioner,* 59 F.2d 533 (7th Cir. 1932), *aff'g in pertinent part,* 23 B.T.A. 278 (1931). Similarly, the fact that the state accepts property worth $2,000 to discharge a tax liability of $3,000, even when the liability is undisputed, does not mean that $3,000 is the amount actually paid. Rather, $2,000, the fair market value of the property used to discharge the tax liability, is the amount actually paid.

Conversely, if for some reason the executor transfers property worth $3,000 in settlement of a $2,000 inheritance tax liability, only $2,000 is actually paid for purposes of section 2011. Any amount paid in excess of the tax liability discharged is not a payment of state tax.

For federal estate tax purposes, the fair market value of property is defined by section 20.2021–1(b) of the regulations. In general, the fair market value of property includible in a decedent's gross estate is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell, and both having reasonable knowledge of the relevant facts. The regulations also explain that the fair market value of an item is not determined by a forced sale price.

In any case in which the value of property affects the federal estate tax liability, the fair market value must be determined under section 2031 of the Code, and is within the jurisdiction of the Internal Revenue Service. This remains true even if the state, for its own purposes, assigns a different value.

In this case the estate realizes a $7,000 gain on the transaction, the difference between the liability satisfied and the basis in the property. If the property had had a fair market value less than the undisputed amount of the liability satisfied, the amount realized would have been only the fair market value. For example, if the property had had a fair market value of $75,000, the amount realized would have been $75,000, and the gain would have been only $5,000. The $2,000 excess of the undisputed liability that was satisfied over the fair market value of the property given in exchange is income from the discharge of indebtedness. Section 1.1001–2(c) of the Income Tax Regulations, Example (8).

HOLDINGS

1. The payment of state inheritance taxes in property, in lieu of cash, pursuant to state law, constitutes "taxes actually paid" to the state for purposes of the federal estate tax credit under section 2011 of the Code. The amount of state inheritance tax treated as paid under section 2011 of the Code is the lesser of: 1) the amount of state inheritance tax liability discharged by the transfer of the property, or 2) the fair market value of the property on the date of the transfer.

2. *D*'s estate realized a $7,000 gain measured by the difference between the estate's basis determined under section 1014 of the Code ($70,000) and the amount of the state tax liability that was discharged ($77,000).

Section 7872.—Treatment of Loans with Below-market Interest Rates

Federal short-term, mid-term, and long-term rates are set forth for the month of October 1986. See Rev. Rul. 86–115, page 19.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

LR–295–84

Diversification Requirements for Variable Annuity, Endowment, and Life Insurance Contracts

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking by cross-reference to temporary regulations.

SUMMARY: In the Rules and Regulations portion of this issue of the FEDERAL REGISTER, the Internal Revenue Service is issuing temporary regulations relating to the diversification requirements for variable annuity, endowment, and life insurance contracts. The text of the temporary regulations serves as the comment document for this notice of proposed rulemaking.

DATES: Written comments and requests for a public hearing must be delivered by November 14, 1986. The regulations are proposed to be effective, generally, for taxable years beginning after December 31, 1983.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR–295–84), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Alice M. Bennett, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3238, not a toll-free call.

SUPPLEMENTARY INFORMATION:
BACKGROUND

The temporary regulations (designated by a "T" following the section citation) * * * [page 15, this Bulletin], amend the Income Tax Regulations (26 CFR Part 1) to provide rules under section 817(h) of the Internal Revenue Code of 1954, as added by section 211(a) of the Tax Reform Act of 1984 (Pub. L. 98–369, 98 Stat. 750). Those temporary regulations prescribe diversification requirements for variable annuity, endowment, and life insurance contracts.

This document proposes to adopt those temporary regulations as final regulations; accordingly, the text of the temporary regulations serves as the comment document for this notice of proposed rulemaking. In addition, the preamble to the temporary regulations provides a discussion of the proposed and temporary rules.

For the text of the temporary regulations, * * * [see page 15, this Bulletin].

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

Although this document is a notice of proposed rulemaking that solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, a Regulatory Flexibility Analysis is not required (5 U.S.C. Chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

DRAFTING INFORMATION

The principal author of these proposed regulations is Linda M. Kroening of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * * *

ROSCOE L. EGGER, JR.
Commissioner
of Internal Revenue.

(Filed by the Office of the Federal Register on September 12, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 15, 1986, 51 F.R. 32664)

Foundations Status of Certain Organizations

Announcement 86–99

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

Amalgamated Labor Community Services Council, Lakewood, OH
Association for Retarded Citizens of Bowling Green and Warren County, Inc., The, Bowling Green, KY
Brooklyn Home Land Project, Inc. Brooklyn, NY
Buckeye Boys Choir, The, Springfield, OH
C.M.D. Association, Denver, CO
Career Outreach Program, Inc., Denver, CO
Caring House Church, Dallas, TX
Center Crime Stoppers, Inc., Center, TX
Central Linn Youth Association, Halsby, OR
Central Texas Council for the Deaf, Inc., Waco, TX
Centralia Pearl Street Fin Foundation, Centralia, WA
Chambers County Crime Stoppers, Inc., Mount Belvieu, TX
Chemical People-Communities Together, Westminster, CO
Chicago Council for Church and Community Change, Chicago, IL
Childrens Drug Abuse Network, Inc., The, Houston, TX
Children's Liver Donor Fund, Houston, TX
Christian Commerce Corp., Ft. Worth, TX
Christian Singles of Boulder Valley, Louisville, CO
Christian Witness Center, Inc., Edgerton, KS
City Wide Club of Clubs, Houston, TX
Clinic Foundation, The, Gallipolis, OH

Colorado Foundation for Personal Development, Englewood, CO
Colorado Shotokan Karate of America, Inc., Boulder, CO
Colorado State Fair Authority Trust, Pueblo, CO
Communications International, Inc., Dallas, TX
Community Centers of the Living Christ, Houston, TX
Concerned Citizens Against Pollution, Inc., Newgulf, TX
Conrad N. Hilton Memorial Park & Community Center, Cisco, TX
Consortium of Extragalactic Astronomy, Austin, TX
Cooke County Arts Council, Inc., Gainesville, TX
Coot Brown Ministries, Wichita Falls, TX
Core Area Neighborhoods Association, Inc., Fort Collins, CO
Covedale Share-A-Home Association, Cincinnati, OH
Creel Transport, Ft. Worth, TX
Crested Butte Mountain Educational Radio, Inc., Crested Butte, CO
Crime Fighters, Inc., Houston, TX
Crossfire Ministries, Inc., Arlington, TX
David K. Nicolai Memorial Scholarship Fund, Anchorage, AK
Fast Cleaning, Inc. Minneapolis, MN
Federal Way Foundation, Federal Way, WA
Film Alternative, The, Morgantown, OH
Flats Oxbow Association, Inc., Cleveland, OH
Fort Wayne Christian Leadership Conference—(Operation Breadbasket), Inc., Fort Wayne, IN
Forward Research Corporation, Battle Creek, MI
Freeway Traveling League Youth Softball, Highland Heights, OH
Friends of the Governors Residence, Lansing, MI
God's Storehouse, Inc., Wapakoneta, OH
Gospel Singing Messengers Evangelistic Association, Inc., The, Greentown, IN
Granville Preservation Association, Inc., Granville, OH
Hamilton County-West Share-A-Home, Inc., Cincinnati, OH
Handi-Van, Inc., Jefferson, KY
Harman Family Music Ministry Association, Windham, OH
Harrison County Gen Ealogical Society, Inc., Clarksburg, WV
Hartford Area Non-Profit Housing Corporation, Watervliet, MI
Heart Institute of Kentucky, Inc., Louisville, KY
Help Us Help Others, Inc., Bryants Store, KY
Helping Hands of Fort Wayne, Inc., Fort Wayne, IN
Hoagland Emergency Medical Services, Inc., Hoagland, IN
Holistic Science Foundation, Convoy, OH
Homemaker Health Care, Granville, OH
Honeycomb Resources, Inc., Indianapolis, IN
Hope Center, Inc., Dayton, OH
Hospice of Delaware County, Inc., Delaware, OH
Hospitality Outreach Training for Ongoing Opportunity Development, Inc., Portland, OR
Human Research and Development Co., Willowwick, OH
Indiana Federation on Children and Youth Inc., Indianapolis, IN
Indiana Minority Vendors Association, Inc., Indianapolis, IN
Indiana Runaway Hotline, Inc., Elwood, IN
Indianapolis Black Alumni Council, Inc., Indianapolis, IN
Indianapolis Community Housing Resource Board, Inc., Indianapolis, IN
Institute for Science and Halacha, Brooklyn, NY
Iwington Forestry Foundation, Inc., Indianapolis, IN
Jacket Boosters, Inc., Mt. Vernon, OH
Joe Kowatch Educational Fund, Ludington, MI
Johnstown Youth Athletic Association, Inc., Johnstown, OH
Jubilee Ranch Christian Community, Inc., The, Deer Park, WA
Kanawha Economic Development Corporation, Institute, WV
Kansas City Gay Pride Committee, Inc., Kansas City, MO
Kentuckiana Area Reading Extension, Inc., Louisville, KY
Kentucky Association for Gifted Education-Lexington, Inc., Lexington, KY
Kentucky Bluegrass Music Center, Inc., Louisville, KY
Kentucky Performing Arts, Inc., Lexington, KY
Kimball Pines Non-Profit Housing Corporation, Battle Creek, MI
Kirwood General Hospital Foundation, Detroit, MI
Koinonia Village, Inc., Cleveland, OH
Kwanza Committee, Inc., Columbus, OH
La Gracia Housing Corp., Midland, TX
La Zarauela De Albuquerque, Inc., Albuquerque, NM
Lao Family Community Incorporated of Lansing, Michigan, Lansing, MI
Latin America Pastors Assistance Fund, Inc., Randlett, OK
Latin American Ministries Partnership, Inc., South Bend, IN
Leadership Institute, Inc., Mansfield, TX
Lighthouse Ministries, Inc., Green River, WY
Lithuanian American Community Foundation, University Heights, OH
Little Friends Day Care Center, Inc., Louisburg, KS
Littleton Public Schools Building Authority, Littleton, CO
Longview Informed Families Together, Inc., Longview, TX
Lorraine Center, Inc., The, Wichita, KS
Louisville Christian Human Resource & Development Corp., Louisville, KY
Love, Inc., Grand Rapids, MI
Love Ministries of Spokane, Spokane, WA
Lower East Side Improvement Coalition, Inc., Youngstown, OH
Magical Child Foundation, Stillwater, OK
Magna Carta in America Foundation, Inc., Luling, TX
Mantua-Shalersville Firefighters Association, Mantua, OH
Marion Manor, Inc., Steubenville OH
McClain County Chemical Abuse Information Center, Inc., Purcell, OK
Metro Service, Inc., Denver, CO
Mexico Inland Missions, Inc., Desoto, TX
Mexico Mobile Ministries, Inc., Hidalgo, TX
Miami County Association for Retarded Citizens, Inc., Peru, IN
Michigan One Stop Export Counseling Service, Detroit, MI
Mid-Eastern Indiana Babe Ruth Association, Inc., Muncie, IN
Ministry In Action Living Center of Lufkin, Inc., Lufkin, TX
Minnesota Shakespeare Company, The, Minneapolis, MN
Montessori Childrens' House, Inc., The, Salt Lake City, UT
Morristown Historic Preservation Association, Morristown, OH
National Association of Corporation Directors, Inc., New Albany, IN
National Caucus and Center on Black Aged Housing Services of Pennsylvania, Inc., The, Philadelphia, PA
National Foundation for the Prevention of Obesity, Inc., Cincinnati, OH
National Independent Education Foundation, Salina, KS
National Prayer Committee, Inc., Garland, TX
National Self-Help Center for the Deaf/

Hearing Impaired, Inc., Austin, TX
Network of Black Churches, San Antonio, TX
New Courage Players, The, Houston, TX
New Mexico Association of Home Health Agencies, Inc., The, Albuquerque, NM
New Mexico Citizens Council on Alcoholism & Drug Abuse, Albuquerque, NM
New Mexico Organ Transplant Fund, Albuquerque, NM
Normana Texas Historical Museum & Community Association, Normana, TX
Northeast Wyoming Hospice, Gillette, WY
Northwest Kansas Family Shelter, Inc., Hays, KS
OBGC III, Inc., Columbus, OH
Oak Grove Work Activity Center, Inc., Lewisville, TX
Oklahoma Commission for Future Educational Leadership, Inc., Oklahoma City, OK
Oklahoma Institute of Continuing Legal Education, Inc., The, Edmond, OK
Oklahoma State Professional Culinary Association, Inc., The, Tulsa, OK
Oklahoma Teen Challenge, Inc., Bartlesville, OK
One Brotherhood of Man, Dallas, TX
Onward & Upward, Denver, CO
Open Heart Club, The, Colorado Springs, CO
Optimist Village, Inc., Orange, TX
Oregon Medical Professional Review Organization, Portland, OR
Oregon Student Athletic Fund, Inc., Portland, OR
Organization for Research for the Conservation of Animals, The, Lakewood, CO
Parents Assistance of Lawton, Inc., Lawton, OK
Parents of Special Children, Emporia, KS
Paul Ragland Evangelistic Association, Dallas, TX
Pecos Valley Gynmastics Club, Inc., Roswell, NM
Penalty Option Program, East Cleveland, OH
Pennsylvania Automative Association Foundation, Harrisburg, PA
Phillips County Area Council for Church & Social Action, Inc., West Helena, AR
Phoenix International Film Festival, Phoenix, AZ
Pilgrim Foundation, The, Commerce, TX
Portland Alumni of Sigma Chi, Inc., Portland, OR
Questhave Retreat, Escondido, CA
Ralph Hunsicker T/W, Philadelphia, PA
Rancho Los Amigos, Clint, TX
Rediscovery, Inc., Denver, CO
Revised Edition, Inc., Waco, TX
Royce J. Simpson Evangelistic Association, Inc., Mesquite, TX
St. Mary's School Trust Fund, Taylor, TX
San Antonio Educational Television, Inc., San Antonio, TX
San Antonio Employers Alliance for Employee Benefits, San Antonio, TX
Schola Antiqua, Inc., New York, NY
Self Reliance Center, Inc., Scottsdale, AZ
Sexual Abuse Prevention Project, Inc., Monroe, LA
Sid Bond Evangelistic Association, The, Shamrock, TX
Silver Creek Senior Citizens Council, Snowflake, AZ
Smith Ministries, Inc., Cave Creek, AZ
Socio-Emotional Learning Family, Philadelphia, PA
Solo Ministries, Inc., Tulsa, OK
South Austin Christian Businessman, Inc., Austin, TX
South Central Foundation on Chemical Dependency, Inc., Pratt, KS
Southern Baptist Advocate, Inc., Dallas, TX
Southside Concord Junior Football League, Inc., St. Louis, MO
Southwest Independent Media Studies, Austin, TX
Stay, Inc., Denver, CO
Stepfamily Associates of Houston, Houston, TX
Stephenville Music Club, The, Stephenville, TX
Stewart Neighborhood Park, Minneapolis, MN
Summit County Nursing Home Advocates, Inc., The, Akron, OH
Sunflower Alcohol Safety Action Project, Inc., Topeka, KS
Texart/150, Inc., Dallas, TX
Texas Association of Middle Eastern Dancers, El Paso, TX
Texas Chapter of the Foundation for North American Wild Sheep, Inc., Arlington, TX
Texas Enterprise Foundation, Inc., The, Ft. Worth, TX
Texas Flute Society, Arlington, TX
Texas Longhorn Breeders Foundation, Ft. Worth, TX
Texas Sheriffs Commemorative Foundation, Bellville, TX
Tucson Center for Attitudinal Healing, The, Tucson, AZ
Turtle Run Research Institute, Altus, OK
Tyrone Bowman Evangelistic Association, Philadelphia, PA
United States Kidney Disease Association, A Nonprofit Corp., Ft. Worth, TX
United Way of Fort Stockton, Inc., Ft. Stockton, TX
Utah Land Law Institute, Salt Lake City, UT
Val Verde Women & Family Violence Center, Inc., Del Rio, TX
Valley View Hospital & Medical Center Auxiliary, Thornton, CO
Victory Outreach of McAllen Inc., McAllen, TX
Vietnam Veteran's Leadership Program of Indiana, Inc., Hammond, IN
Vision Ministries, Inc., Fort Scott, TX
Wally Wood Ministries, Houston, TX
Western Neighbors, Inc., Tulsa, OK
Westgate Foundation, The, Denton, TX
Whitmore Lake Community Service Center, Inc., Whitmore Lake, MI
Wichita Association for Gifted Talented and Creative, Wichita, KS
Wichita Care Center, Inc., Wichita, KS
Wise County Crisis Center, Inc., Decatur, TX
Worship Evangelism Ministries, Inc., Midwest City, OK
Wyoming Association of Volunteers in Management, Gillette, WY
Youth Crisis Outreach, Inc., Tecumseh, OK
Youth Employment Service of Clovis, Inc., Clovis, NM

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

The following organization, which has been treated as a private operating foundation described in section 4942(j)(3) of the Code, has now been classified as an organization that is not a private operating foundation. Grantors and contributors may no longer rely upon rulings or determinations that this organization is a private operating foundation. The organization is:

Downey Rotary Foundation, Downey, CA

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practictioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Robert D. Digby	North Little Rock, AR	Certified Public Accountant	Four Months from July 29, 1986
Jeffrey E. Ellis	Rockland, ME	Certified Public Accountant	Indefinite from July 2, 1986
Charles L. Honey	Prescott, AR	Attorney	One Year from July 2, 1986
Bernhardt Karp	Hudson, NY	Attorney & Certified Public Accountant	Indefinite from July 29, 1986
George N. Meros	Springfield, MO	Attorney	Indefinite from July 25, 1986
William G. Waldrop	Adamsville, AL	Certified Public Accountant	Indefinite from July 17, 1986
Paul R. Beutler	Cold Spring, MN	Certified Public Accountant	Eighteen Months from August 13, 1986
Robert J. Sher	Hyattsville, MD	Attorney	Indefinite from August 22, 1986
Russell H. Strong	Breckinridge, TX	Certified Public Accountant	Indefinite from August 22, 1986
David G. Willemain	Towson, MD	Attorney	Indefinite from July 22, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Alton C. Bingham	Las Vegas, NV	Certified Public Accountant	August 16, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor.
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federral Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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8096, 1986–37 I.R.B. *4*
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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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*Denotes entry since last publication

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

SPECIAL ANNOUNCEMENT

Announcement 86–100, page 109.
A public hearing will be held on October 22, 1986, on proposed regulations under sections 88 and 468A of the Code relating to nuclear decommissioning costs.

ADMINISTRATIVE

Rev. Proc. 86–37, page 4.
Magnetic cassette and mini-disk reporting; information returns; Forms 1098, 1099, 5498, and W–2G. Requirements and conditions are set forth for filing Forms 1098, 1099, 5498, and W–2G on magnetic cassette or mini-disk instead of paper returns. Rev. Proc. 85–48 superseded.

Finding Lists begin on page 112.
Announcement of Disbarments and Suspensions on page 110.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the Internal Revenue Bulletin as the source would be appropriate.

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Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.602: Tax forms and instructions.

Rev. Proc. 86–37

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SECTION 18.

NOTE: THIS REVENUE PROCEDURE MAY ONLY BE USED T PREPARE CASSETTE OR MINI-DIS SUBMISSIONS FOR TAX YEAR 198 RETURNS. UPDATED COPIES AR PUBLISHED EACH YEAR. PLEAS READ THIS PUBLICATION CAREFULLY. **PERSONS REQUIRED TO FIL MAY BE SUBJECT TO PENALTIES FO FAILURE TO FOLLOW THE INSTRUCTIONS IN THIS REVENU PROCEDURE.** THESE INCLUDE PENALTIES OF $50 PER DOCUMENT FOR EACH DOCUMENT SUBMITTED WITHOUT A TAXPAYE IDENTIFICATION NUMBER (TIN OR WITH AN INCORRECT TIN. YOU MAY ALSO BE SUBJECT TO AN ADDITIONAL $50 PENALTY PER DOCUMENT FOR EACH DOCUMENT NOT SUBMITTED ON MAGNETIC MEDIA IF YOU ARE REQUIRED TO FILE THIS WAY OR IF YOU FILE LATE. THE MAXIMUM PENALTY IS $50,000 (THERE IS NO MAXIMUM FOR CERTAIN FORMS 1099–INT, 1099–DIV, 1099–OID, 1099–PATR, 5498, OR IF THE FAILURE TO FILE IS DUE TO INTENTIONAL DISREGARD OF THE FILING REQUIREMENTS). IRS **STRONGLY ENCOURAGES** FILERS TO REVIEW THEIR DATA FOR ACCURACY BEFORE SUBMISSION TO PREVENT ERRONEOUS NOTICES BEING MAILED TO PERSONS FOR WHOM REPORTS ARE FILED.

PART A.—GENERAL

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to provide the requirements and conditions for filing information return Forms 1098, 1099, 5498, and W–2G on cassette or mini-disk. Other revenue procedures provide instructions for filing on magnetic tape and magnetic diskette. *THIS REVENUE PROCEDURE IS TO BE USED FOR THE PREPARATION OF TAX YEAR 1986 INFORMATION RETURNS ONLY.* THIS PROCEDURE IS

UPDATED YEARLY TO REFLECT NECESSARY CHANGES. PLEASE READ THIS PUBLICATION CAREFULLY. Specifications for filing the following forms are contained in this procedure:

(a) Form 1098, Mortgage Interest Statement.

(b) Form 1099–A, Information Return for Acquisition or Abandonment of Secured Property. (For Mini-Disk only.)

(c) Form 1099–B, Statement for Recipients of Proceeds from Broker and Barter Exchange Transactions. (For Mini-Disk only.)

(d) Form 1099–DIV, Statement for Recipients of Dividends and Distributions.

(e) Form 1099–G, Statement for Recipients of Certain Government Payments.

(f) Form 1099–INT, Statement for Recipients of Interest Income.

(g) Form 1099–MISC, Statement for Recipients of Miscellaneous Income.

(h) Form 1099–OID, Statement for Recipients of Original Issue Discount.

(i) Form 1099–PATR, Statement for Recipients (Patrons) of Taxable Distributions Received From Cooperatives.

(j) Form 1099–R, Statement for Recipients of Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc.

(k) Form 5498, Individual Retirement Arrangement Information.

(l) Form W–2G, Statement for Recipients of Certain Gambling Winnings. (For Mini-Disk only.)

Specifications for filing Forms 1042S, 6248, 8027, W–2, and W–2P are contained in separate publications.

.02 Section 1.6045–1(l) of the Income Tax Regulations requires brokers and barter exchanges to use magnetic media to report *ALL* Form 1099–B data to IRS. *THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS.* Section 6011(e) of the Internal Revenue Code as amended by the Interest and Dividend Tax Compliance Act of 1983, Pub. L. 98–67, 1983–2 C.B. 352, 359, requires that any person, including corporations, partnerships, individuals, estates, and trusts, required to file more than 50 information returns *in the aggregate* for payments of interest (Forms 1099–INT and 1099–OID), dividends (Form 1099–DIV), or patronage dividends (Form 1099–PATR), for any calendar year, must file such returns on magnetic media. *THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS.* For example, if you must file 30 Forms 1099–DIV and 25 Forms 1099–INT, filing on magnetic media is required. In addition, for returns filed in 1987 (for tax year 1986), magnetic media reporting is required if you file 500 or more of *each* of the following forms: Forms W–2, W–2P, W–2G, 1098, 1099–A, 1099–G, 1099–MISC, 1099–R, 5498, 1042S, 6248, and 8027. *THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS.* Form W–2c is not included in these filing requirements. The 500 or more requirement for these forms will drop to 250 or more for returns (original or corrected) filed in 1988 (for tax year 1987) and later years. Forms W–2 and W–2P are filed with the Social Security Administration (SSA), *NOT* Internal Revenue Service (IRS). At this time, corrected returns filed on Form W–2c with SSA are not required on magnetic media. These requirements shall not apply if you establish that it will cause you undue hardship. Refer to Part A, Sec. 5.

.03 This procedure also provides the requirements and specifications for mini-disk filing under the Combined Federal/State Filing Program. Refer to Part A, Sec. 14. Cassette filers may not participate in this program due to the requirement that records on this program must be 360 characters in length. Cassette records cannot exceed 256 characters.

.04 The following revenue procedures and publications provide more detailed filing procedures for certain information returns:

(a) 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" provide further information on filing returns with IRS. These instructions are available at IRS offices.

(b) Rev. Proc. 84–24, 1984–1 C.B. 465, regarding preparation of transmittal documents (Forms 1096 and 4804) for information returns.

(c) Rev. Proc. 84–33, 1984–1 C.B. 502, regarding the optional method for agents to report and deposit backup withholding.

(d) Publication 1179, Specifications for Paper Substitutes for Forms 1096, 1098, 1099, 5498, and W–2G.

.05 This procedure supersedes the following revenue procedure: Rev. Proc. 85–48, 1985–2, C.B. 607, also published in Publication 1253 (Rev. 9–85), Requirements and Conditions for Filing Information Returns in the Forms 1098, 1099, 5498, and W–2G Series on Cassette or Mini-Disk.

.06 Refer to Part A, Sec. 15 for definitions of terms used in this publication.

SEC. 2. BACKGROUND—PRIOR YEAR CHANGES (TAX YEAR 1985)

DUE TO *NUMEROUS* LEGISLATIVE AND FORMS CHANGES BETWEEN TAX YEARS 1984 AND 1985, CHANGES WERE *NOT* LISTED INDIVIDUALLY UNDER THIS SECTION. THE ENTIRE PUBLICATION WAS REVISED. FOR TAX YEAR 1985, SEE REV. PROC. 85–48, 1985–2 C.B. 607, FOR SPECIFIC CHANGES.

SEC. 3. NATURE OF CHANGES—CURRENT YEAR (TAX YEAR 1986)

.01 The following changes must be incorporated into your programs for tax year 1986.

.02 GENERAL CHANGES ARE AS FOLLOWS:

(a) The note on the cover and which follows the table of contents was revised to alert filers that their data should be reviewed for accuracy before submission to prevent erroneous notices to persons for whom reports are filed.

(b) Part A, Section 1.02 lists the forms described in this revenue procedure that must be filed on magnetic media. *THESE REQUIREMENTS APPLY TO BOTH ORIGINAL AND CORRECTED RETURNS.* Corrected returns filed on Form W–2c with SSA are not required at this time on magnetic media.

(c) A note was added to Part A, Sec. 4.01 to alert filers that applications to file Forms W–2 and W–2P on magnetic media are requested from SSA; however, requests for undue hardship waivers and extensions of time to file Forms W–2 and W–2P on magnetic media are requested from the IRS National Computer Center. Waiver requests for these forms should have been filed by July 31, 1986, for tax year 1986 for returns to be filed in 1987.

(d) Transmitter Control Codes may be alpha/numeric. This has been noted in several places within the publication.

(e) The dates for submission of "*test*" files have been revised in Part A, Sec. 5. "*Test*" files should be submitted between August 15 and December 15 each year. Also, "*test*" data for the "A" Record must be actual data, not fictitious information.

(f) Part A, Sec. 5.04 has been revised to alert filers that a transmittal Form 4804, 4802 or computer generated substitute must accompany "test" files. The transmittal Forms 4804 and 4802 have been updated for 1986. Agencies who produce a computer generated substitute must update their format for these forms. The Form 4804 now includes a checkbox 1 to indicate the type of file (*e.g.*, original, correction, replacement, test).

(g) Part A, Sec. 5 includes new information concerning undue hardship waiver requests. Filers are now required to submit Form 8508, Request for Waiver From Filing Information Returns on Magnetic Media. *THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS WITH THE EXCEPTION OF FORM W–2c.*

(h) Part A, Sec. 6 has been updated to include the retention requirements for information returns and the new affidavit requirements for transmittal documents.

(i) For documents filed on paper with the appropriate service center, it is no longer necessary to note on the transmittal Form 1096 that a portion of the returns are being filed on magnetic media. This has been deleted from Part A, Sec. 6.07.

(j) Part A, Sec. 6.08 has been reworded to clarify that reports from different branches for one payer, *if submitted on the same file,* must be consolidated under one "A" Record for each type of information return.

(k) A note has been added to Part A, Sec. 7 that Form 5498 is used to report amounts contributed during or after the calendar year.

(l) Part A, Sec. 8(h) has been added to inform filers who file extension requests for multiple payers, that the request must include a list of all payers and their TINs (SSN or EIN).

(m) Part A, Sec. 10 alerts filers that the filing requirements apply to both original and corrected returns with the exception of Form W–2c filed with SSA. Refer to Part A, Sec. 1 for the filing requirements. Corrected returns should be aggregated and submitted as soon as possible but not later than October 1 of each year. Also, corrections should be submitted only for the returns filed in error, not the entire file.

(n) In prior years, cassette position 5 and mini-disk position 6 of the "B" Record were used as the corrected return indicator. Part A, Sec. 10.01 indicates that this has now been changed to cassette position 6 and mini-disk position 7. The Guidelines in Sec. 10 have also been updated to reflect this change. You must adjust your programs. This change was necessary to facilitate the need for a second position in the "B" Record Document Specific Code field.

(o) Transmittal Form W–3G is now obsolete. This form was used to transmit paper Forms 1099–R and W–2G. These two forms are now to be transmitted to the service center with Form 1096. References to Form W–3G have been deleted from this publication.

(p) Two new charts were added to the publication last year to provide instructions for filing corrections on magnetic media and on paper forms. Chart 2, Guidelines for Filing Corrected Returns on Paper Forms, has been deleted. The instructions for filing corrections on paper forms are now available in the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G."

(q) Part A, Sec. 10, Guidelines have been revised. If a return was filed with *NO* Payee TIN (SSN or EIN), or the return was filed with an incorrect Payee TIN, only one transaction is necessary to make the correction.

(r) Part A, Sec. 12 has been completely revised. Refer to this section for specific changes.

(s) Service center addresses have been deleted from this publication. They are available in the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G."

(t) Part A, Sec. 14.02 has been revised to inform filers of the authorization to sign consent Form 6847. Filers who have received approval to file on this program in prior years may be required to resubmit a consent Form 6847 signed by each payer. Refer to Part A, Section 14.02 for specific information.

(u) The dollar criteria in Table 2 of Part A, Sec. 14 has changed. For the state of Minnesota, Form 5498 must now be reported. Also, two footnotes for Minnesota have been deleted: $10.01 for Savings and Loan Associations and Credit Unions; and $600.01 for Rents and Royalties.

(v) Acceptable foreign country codes have been added to Part A, Sec. 16 to assist you in developing the address field.

(w) Part B, Sec. 1.18 has been revised to indicate changes made to the external media labels. Form 5064 is the external media label and has been updated for tax year 1986. You must use the updated label for 1986. These will be included in your magnetic media reporting packages.

.03 THE FOLLOWING CHANGE HAVE BEEN MADE TO THE PAYER TRANSMITTER "A" RECORD.

(a) A note has been added to Part B Sec. 3.03 and Part C, Sec. 2.03 to indicat that all alpha characters should be up percase.

(b) Form 1099–MISC, Amount Cod "8", Direct Sales Indicator, NOTE 1, ha been clarified.

(c) Form 1099–OID, the title of Amoun Code 2 has been changed from "State interest," to "Other periodic interest."

(d) Form 1099–R, the term "Insuranc Contracts" has been added to the title o the form and insurance premiums has bee added to Amount Code "5".

(e) Amount Code "7" has been adde to Form 1099–R to report "State incom tax withheld."

(f) A note has been added for reportin distributions from KEOGH plans on Form 1099–R.

(g) Form 5498, Amount Code "1" ha been changed to report, "Regular SE contributions made in 1986 and 1987 fo 1986." The regular SEP contributions hav been deleted from Amount Code "3" an now appear separately as Amount Cod "1".

(h) Form 5498, the title of Amount Cod "4" has been changed to "Life insuranc cost included in Code 1 or 3 (for endowment contracts only)."

(i) Amount Code "3" has been adde for Form W–2G to report "State incom tax withheld."

(j) The First Payer Name Line has been clarified for those reporting on Form 1098, "Mortgage Interest Statement." *Refer to the First Payer Name Line field description for specific information.*

.04 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE PAYEE "B" RECORD.

(a) A note has been added to Part B and Part C, Sec. 4.03 concerning invalid addresses.

(b) A note has been added to Part B, Sec. 4.06 and Part C, Sec. 4.08 to indicate that all alpha characters should be uppercase.

(c) The Document Specific Code field length has been increased from 1 to 2 positions. Cassette positions 4-5 and mini-disk position 5-6 now represent this coding. This change was necessary due to multiple coding required in certain cases for Form 1099–R.

(d) Additional coding has been added to the Document Specific Code for Form

1099–R. A Code "9" represents PS 58 Costs; Code "P" represents excess contributions refunded plus earnings on such excess contributions taxable in 1985; Code "A" represents distributions which qualify for 10-year averaging; Code "B" represents distributions which qualify for the death benefit exclusion; and Code "C" indicates that the distribution qualifies for both "A" and "B".

(e) The Document Specific Code, Direct Sales indicator has been clarified.

(f) In prior years, cassette position 5 and mini-disk position 6 of the Payee "B" Record were used as the corrected return indicator. This has now changed to cassette position 6 and mini-disk position 7. You must adjust your programs.

(g) Examples have been added to assist you in the development of the Name Control field.

(h) The Type of TIN indicator field has been clarified for those accounts which are questionable. Code "9" has been deleted.

(i) The Payer's Account Number for the Payee field has been clarified.

(j) The First Payee Name Line field description has been clarified for those reporting Form 1098, "Mortgage Interest Statement." *Refer to the First Payee Name Line field description for specific information.*

(k) The Payee City, Payee State, and Payee ZIP Code are three separate fields. If the payee lives outside of the United States, insert a "1" in position "1" of the Payee City field and spell out the name in the remaining positions. Use the appropriate Country Code as shown in Part A, Sec. 16 in the Payee State field. Some foreign countries utilize alpha characters in the ZIP Code. The use of alpha characters is only acceptable if there is a "1" in position "1" of the Payee City field.

.05 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE END OF PAYER "C" RECORD.

(a) Part B, Sec. 5.03 and Part C, Sec. 13.03 clarify the totals required in the "C" Record.

(b) Part B, Sec. 5.04 and Part C, Sec. 13.04 provide instructions to assist you in the development of the "C" Record.

.06 THE FOLLOWING CHANGES HAVE BEEN MADE TO THE END OF TRANSMISSION "F" RECORD.

(a) The Number of Payers field name and description have been reworded.

(b) The Number of Reels field description has been reworded.

SEC. 4. WAGE AND PENSION INFORMATION FILED WITH SSA

.01 Section 8(b), Public Law 94–202, 1976–1 C.B. 503, enacted in January 1976, authorized the combined reporting of FICA detailed information in one consolidated annual W–2 (Copy A) to the Federal government. AS A RESULT, FORMS W–2 AND W–2P ARE TO BE FILED WITH SSA NOT WITH IRS. Applications to file Forms W–2 and W–2P on magnetic media are to be mailed to SSA; however, undue hardship waivers and extensions of time to file Forms W–2 and W–2P are to be requested from the IRS National Computer Center, not from SSA. Requests for undue hardship exemption for these two forms must be filed with the IRS National Computer Center by July 31, 1986, for tax year 1986 for returns to be filed in 1987. Refer to Part A, Sec. 13 for the address and Part A, Sec. 5.08 and Sec. 8 for the required information.

.02 SSA will accept magnetic media filing of Forms W–2 and W–2P and has issued the following concerning this: TIB–4a, "*Magnetic Tape Reporting,* Submitting FICA Wage and Tax Data to the Social Security Administration"; TIB–4b, "*Magnetic Tape Reporting*, Submitting Annuity, Pension, Retired Pay or IRA Payment to the Social Security Administration"; and TIB–4c, "*Diskette Reporting,* Submitting FICA Wage and Tax Data to the Social Security Administration." Applications for filing Forms W–2 and W–2P on magnetic media appear in TIBs–4a, 4b, and 4c.

.03 Copies of Social Security Administration publications TIB–4a, 4b, and 4c are available from any local Social Security Administration office or the SSA Regional Magnetic Media Coordinators.

SEC. 5. APPLICATION FOR MAGNETIC MEDIA REPORTING AND REQUESTS FOR UNDUE HARDSHIP WAIVERS

.01 For purposes of this revenue procedure, the *PAYER* includes the person making the payments, a recipient of mortgage interest payments, a broker, a barter exchange, a trustee or issuer of an IRA, SEP or DEC, or a lender who acquires an interest in secured property or who has reason to know that the property has been abandoned. The *TRANSMITTER* is the organization preparing the cassette or mini-disk file. The payer and transmitter may be the same organization. Do not submit returns on cassette if you transmit for someone else due to the 256 character record restriction. Payers or their transmitters are required to complete Form 4419, Application for Magnetic Media Reporting of Information Returns. Copies of this form, for your use, are included in this publication. Requests for additional information or forms related to magnetic media processing should be addressed to the National Computer Center. Beginning January 1, 1986, magnetic media processing for *ALL* service centers was centralized at the National Computer Center. The address is listed in Part A, Sec. 13.

.02 Applications should be filed with the National Computer Center before "*test*" files are submitted. ("*Test*" files are submitted between August 15 and December 15 each year.) IRS will act on an application and notify the applicant, in writing, of authorization to file. A five character alpha/numeric *Transmitter Control Code* will be assigned and included in an acknowledgement letter within 30 days of receipt of the application. Cassette or mini-disk returns may not be filed with IRS until the application has been approved. Do not enter blanks in the "A" Record Transmitter Control Code field; enter the five character alpha/numeric Transmitter Control Code which is assigned to you by IRS after you have filed an application and it has been approved. Applications for approval to file Forms W–2 and W–2P on magnetic media must be filed with SSA, *NOT* with IRS. Refer to Part A, Sec. 4.

.03 After you have received approval to file on magnetic media, you do not need to reapply each year; however, notify IRS in writing if:

(a) there are hardware or software changes that would affect the characteristics of the magnetic media submission (*e.g.*, changing from cassette or mini-disk to tape filing or vice versa) a new Transmitter Control Code may be necessary or,

(b) you discontinue filing on magnetic media for a year (your five character alpha/numeric Transmitter Control Code may be reassigned).

If either of these conditions applies to you, you should contact IRS for clarification. In *ALL* correspondence, refer to your current five character alpha/numeric Transmitter Control Code to assist IRS in locating your files.

.04 IRS will assist new filers with their initial cassette or mini-disk submission by reviewing "*test*" files submitted in advance of the filing season. The "*test*" data should be *actual* data for the "A" Record, not fictitious information. This applies to all records submitted in the "*test*" file. Approved payers or transmitters should submit "*test*" files to the National Computer Center. You *MUST* submit a "*test*" file in order to participate in the Combined Federal/State Program; however, you are encouraged to submit "*test*" files if you are a new filer on magnetic media. As a guideline, IRS prefers that all "*test*" files be submitted between August 15 and December 15 each year. Refer to Part A, Sec. 13 for the address. Do not submit "*test*" cassettes or mini-disks after December 15. If you are unable to submit your "*test*" file by this date, you may *only* send a sample hardcopy printout or cassette or mini-disk dump to the National Computer Center which shows a sample of each type of record (A, B, C, K, and F) *used*. Clearly mark the hardcopy printout or dump as "TEST DATA" and include identifying information such as name, address, and telephone number of someone familiar with the "*test*" print or dump who may be contacted to discuss its acceptability. With all "*test*" data, include a transmittal Form 4804, 4802 or computer generated substitute marked as "TEST DATA" which identifies your five character alpha/numeric Transmitter Control Code and total record and money amounts. The transmittal Form 4804 and 4802 have been updated for tax year 1986. Agencies who produce a computer generated substitute must include the additional information required on these forms. The Form 4804 now includes a checkbox 1 to indicate the type of file (*e.g.*, original, correction, replacement, test). The "*test*" data must be a sample of *actual* data coded according to this revenue procedure.

.05 If your magnetic media files have been prepared for you in the past by a service agency, and you now have computer equipment compatible with that of IRS and wish to prepare your own files, you must request your own five character alpha/numeric Transmitter Control Code by filing an application, Form 4419, as described above.

.06 If you as an individual or organization are an approved filer on magnetic media and you change your name or the name of your organization, please notify the National Computer Center, in writing, so that your file may be updated to reflect the proper name.

.07 In accordance with section 1.6041–7(b) of the Income Tax Regulations, payments to providers of medical and health care services from separate departments of a health care carrier may be reported as separate returns on magnetic media. In this case, the headquarters office will be considered to be the transmitter, and the individual departments of the company filing reports will be considered to be payers. A *single* application form covering *all* the departments which will be filing on cassette or mini-disk should be submitted. One five character alpha/numeric Transmitter Control Code may be used for all departments.

.08 Any person required to file original or corrected returns on magnetic media may request a waiver from the filing requirements by submitting Form 8508, Request for Waiver from Filing Information Returns on Magnetic Media, with the IRS National Computer Center if filing on magnetic media would be an undue hardship. Requests for waivers for Forms W–2 and W–2P are due by July 31, 1986, for tax year 1986 for returns to be filed in 1987. For all other returns required to be filed on magnetic media, waiver requests must be filed at least 90 days before the returns are due. This waiver, if approved, will only provide exemption from magnetic media filing for one tax year. Filers may not apply for a waiver for more than one tax year at a time. You must reapply each year that a waiver is necessary. Copies of Form 8508 may be obtained from the IRS National Computer Center. See Part A, Sec. 13 for the address.

.09 Section 1.6045–1(l) of the Income Tax Regulations requires brokers and barter exchanges to use magnetic media in reporting *ALL* Form 1099–B data to IRS. *THIS REQUIREMENT APPLIES TO BOTH ORIGINAL AND CORRECTED RETURNS*. Generally, *NEW* brokers and *NEW* barter exchanges may request an undue hardship exemption by filing a request for waiver with the IRS National Computer Center by the end of the second month following the month in which they became a broker or barter exchange.

.10 *All* requests for magnetic media related undue hardship exemptions should be submitted to the IRS National Computer Center at least 90 days before the due date of the return, except as stated in Sec. 5.09. All requests for undue hardship for Forms W-2 and W-2P are to be filed with the IRS National Computer Center, not SSA, and must be filed by July 31, 1986, for tax year 1986 for returns to be filed in 1987. Refer to Part A, Sec. 13 for the address.

.11 If you request a waiver from filing on magnetic media and it *is* approved, *do not send a copy of the approved waiver to the service center where you file your paper returns*. Keep the waiver for your records. Do *not* staple, paperclip or use rubberbands on any scannable forms. Paper information returns are read by an optical scanner (OCR) at the service centers.

.12 Waivers are granted on a case-by-case basis and may be approved at the discretion of the National Computer Center. Refer to Part A, Sec. 13 for the address.

.13 If you are required to file on magnetic media but fail to do so, and you do not have an approved waiver on record, you may be subject to a failure to file penalty. Refer to Sec. 6.01 below.

.14 *An approved waiver from filing information returns on magnetic media does not provide exemption from ALL filing; you MUST submit your information returns on acceptable paper forms.*

.15 A cassette or mini-disk reporting package, which includes all the necessary transmittals, labels, and instructions, will be mailed to the last known address of all approved filers each year.

SEC. 6. FILING OF MAGNETIC MEDIA REPORTS

.01 If you do not file your returns on time, you may be subject to a $50 per document failure to file penalty. If you file without following the instructions in this revenue procedure, you may be subject to a $50 per document failure to file penalty. The maximum penalty is $50,000. However, there is no maximum penalty for returns of 1099–INT, 1099–OID, 1099–DIV, 1099–PATR, 5498 or if the failure to file is due to intentional disregard of the filing requirements.

.02 Generally, you are now subject to a $50 penalty for *each* failure to include the payee's correct TIN on an information return unless the payer can demonstrate that the payer met the due diligence requirements. Refer to Part A, Sec. 11.

.03 Rev. Proc. 84–24, 1984–1 C.B. 465, gives detailed information on preparing transmittal documents for information returns and is available at IRS offices. Specific guidelines are given on how to report the payer's name, address, and TIN on transmittal documents and information eturns. Instructions for multiple transittals and the submission of transmittals y service bureaus or agents are also covred.

.04 *THE CASSETTE OR MINI-DISK RECORDS ARE TO BE SUBMITTED 'O THE NATIONAL COMPUTER CENTER; HOWEVER, PAPER INFORMATION RETURNS ARE TO CONTINUE TO BE FILED WITH THE APPROPRIATE SERVICE CENTERS.* 'orm 4804, Transmittal of Information Returns Reported on Magnetic Media, nust accompany cassette or mini-disk ubmissions. If you file for multiple payers nd have the authority to sign the affidavit n Form 4804, you should also submit 'orm 4802, Transmittal for Multiple Magetic Media Reporting. *For IRS to ensure hat your actual data records were fornatted following THIS revenue procedure, include a hardcopy printout, fast print or cassette or mini-disk dump showing a ample of each type of record (A, B, C, K, and F) used on the cassette or minidisk*. This will be reviewed prior to actual processing to ensure that the data is in the proper format. *Be sure to include Form 4804, 4802 or computer generated listing with your cassette or mini-disk shipment. DO NOT MAIL THE CASSETTES OR MINI-DISKS AND THE TRANSMITTAL DOCUMENTS SEPARATELY.* IRS encourages the use of a computer generated Form 4804 which includes *all* necessary information requested on the actual form.

Paper information returns must be transmitted to the appropriate service center using Form 1096, Annual Summary and Transmittal of U.S. Information Returns. *Do not send information returns filed on paper forms to the National Computer Center.*

.05 The affidavit for Form 4804 should be signed by the payer; however, the transmitter, service bureau, paying agent, or disbursing agency may sign the affidavit on behalf of the payer if all of the following conditions are met:

(a) It has the authority to sign the affidavit under an agency agreement (either oral, written, or implied) that is valid under the state law.

(b)(i) It has the responsibility (either oral, written, or implied) conferred on it by the payer to request the TINs of recipients (or others for whom information is being reported), or

(ii) If the return of more than one payer is included in a single cassette or mini-disk submission, covered by a single Form 4804, each payer has attested by affidavit to the transmitter, service bureau, paying agent or disbursing agent that the payer has complied with the law in attempting to secure correct TINs.

(c) It signs the affidavit and adds the caption "For: (name of payer)."

.06 Although a duly authorized agent signs the affidavit, the payer is held responsible for the accuracy of the Form 4804, and the payer will be liable for penalties for failure to comply with filing requirements.

.07 DO NOT REPORT THE SAME INFORMATION ON PAPER FORMS THAT YOU REPORT ON MAGNETIC MEDIA. IF YOU REPORT PART OF YOUR RETURNS ON PAPER AND PART ON MAGNETIC MEDIA, BE SURE THAT DUPLICATE RETURNS, WITH THE SAME INFORMATION, ARE NOT INCLUDED ON BOTH. This does not mean that corrected documents are not to be filed. If a return has been prepared and submitted improperly, you must file a corrected return as soon as possible. Refer to Part A, Sec. 10 for requirements and instructions on filing corrected returns.

.08 Reports from different branches or locations for one payer, if submitted on the same file, *MUST* be consolidated under one Payer/Transmitter "A" Record for each type of information return. For example, all Forms 1099–INT for the same payer on a single file must be sorted together under one Payer/Transmitter "A" Record followed by the appropriate "B" Records and one "C" Record.

.09 Payers are required to retain a copy of the information returns filed with IRS or the ability to reconstruct the data for at least three years.

.10 Before submitting magnetic media files, include the following:

(a) A signed Form 4804 or computer generated substitute.

(b) A Form 4802 (if you transmit for multiple payers).

(c) A hard copy printout or listing of the first five and last two blocks of your file. The listing should show a sample of each type of record (A, B, C, K, and F) used on the magnetic media being submitted.

(d) The magnetic media with an external identifying label as described in Part B, Sec. 18 for Cassette and Part C, Sec. 1.06 for Mini-Disk.

(e) On the outside of the shipping container, include a Form 4801 or a substitute for the form which reads "DELIVER UNOPENED TO TAPE LIBRARY—MAGNETIC MEDIA REPORTING—BOX __ of __." If there is only one container, mark the outside as Box *1* of *1*. For multiple containers, include the sequence (*e.g.*, Box *1* of *33*, *2*, of *33*, etc.).

(f) If you were granted an extension and are filing late, include a copy of the approval letter with the magnetic media shipment.

.11 IRS will not pay or accept "Collect on Delivery" or "Charged to IRS" shipments of reportable tax information that an individual or organization is legally required to submit.

.12 Files returned to you due to coding or format errors are to be corrected and returned to IRS within 30 days of your receipt or the payer may be subject to a failure to file penalty.

SEC. 7. FILING DATES

.01 The dates prescribed for filing paper returns with IRS also apply to magnetic media filing. Magnetic media reporting to IRS for all types of Forms 1098, 1099, and W–2G must be on a calendar year basis. Form 5498 is used to report amounts contributed during or after the calendar year but not later than April 15.

.02 Information returns filed on magnetic media for Forms 1098, all types of Forms 1099, and W–2G must be submitted to IRS and postmarked by February 28. The due date for furnishing the required copy or statement to the recipient is January 31.

.03 Information returns filed on magnetic media for Form 5498 must be submitted to IRS and postmarked by May 31. Copies of this form or statements are due to the participant by May 31 for contributions made to IRAs and SEPs for the prior calendar year; however, participant copies or statements for DECs are due at the time the contribution is made or January 31, whichever is later. Form 5498 is filed for contributions to be applied to 1986 that are made between January 1, 1986, and April 15, 1987.

SEC. 8. EXTENSIONS OF TIME TO FILE

.01 If a payer or transmitter of returns *on magnetic media* filed with IRS or SSA is unable to submit their magnetic media file by the dates prescribed in Sec. 7.02 and 7.03 above, submit a letter requesting an extension of up to 30 days to file, as soon as you are aware that an extension will be necessary. In order to be considered, the request *MUST* be filed *before* the due date of the return; otherwise, you will be subject to the late filing penalty. The letter should be sent to the attention of the Magnetic Media Reporting Program at the IRS National Computer Center. See Part A, Sec. 13 for the address. The request should include:

(a) The filer's (or transmitter's, if filing for multiple payers) name and address.

(b) The filer's Taxpayer Identification Number (SSN or EIN).

(c) The tax year for which the extension of time is requested: tax year 1986.

(d) The name and telephone number of a person to contact who is familiar with the request.

(e) The type of returns and expected volume (*e.g.* 5000 Forms 1099-INT).

(f) The five character alpha/numeric Transmitter Control Code assigned to the organization or individual requesting the extension (if a number has been assigned).

(g) The reason for the delay and date that you *will* be able to file.

(h) If you file for multiple payers, the request must include a list of all payers and their TINs (SSN or EIN).

An approved extension for magnetic media filing does not provide additional time for supplying a copy to the payee.

.02 If an extension of time to file on magnetic media is granted by the National Computer Center, a *copy* of the letter *granting the extension MUST* be attached to the transmittal Form 4804 or computer generated substitute when the file is submitted.

SEC. 9. PROCESSING OF MAGNETIC MEDIA RETURNS

.01 All data received at the National Computer Center for processing will be given the same protection as individual returns (1040), and will be returned to the originator after processing. Files that are received timely by the National Computer Center will be returned to the filers by August 15 of the year in which submitted.

.02 *Due to the volume of input received and the cost to return special containers, special shipping containers should not be used for transmitting data to the National Computer Center since IRS cannot guarantee return of such containers.*

.03 Files will be returned to you for correction if they are unprocessable due to format or coding errors, or by the request of the filer. Unprocessable files must be corrected and returned to the National Computer Center within 30 days of your receipt or the payer may be subject to a failure to file penalty. The corrected files will be returned to the filer by the National Computer Center within 6 months of receipt. PLEASE BE SURE THAT YOUR FORMAT AND CODING COMPLY WITH THIS REVENUE PROCEDURE. *THIS REVENUE PROCEDURE IS TO BE USED FOR THE PREPARATION OF TAX YEAR 1986 INFORMATION RETURNS ONLY.* LEGISLATIVE AND FORMS CHANGES AFFECTING INFORMATION RETURNS MAY OCCUR EACH YEAR. THESE PROCEDURES ARE UPDATED TO REFLECT NECESSARY CHANGES. PLEASE READ THIS PUBLICATION CAREFULLY.

SEC. 10. HOW TO FILE CORRECTED RETURNS

.01 The filing requirements listed in Part A, Sec. 1 apply to both original and corrected returns. Corrections should be aggregated and filed as soon as possible but not later than October 1 of each year. *ALL FIELDS OR BOXES MUST BE COMPLETED WITH THE CORRECT INFORMATION, NOT JUST THE DATA FIELDS NEEDING CORRECTION.* Submit corrections only for the returns filed in error, not the entire file. If your complete file is in error, contact the National Computer Center immediately. If you file corrected returns on paper forms, submit Copy A to the appropriate service center. There are numerous types of errors. It may require more than one transaction to properly correct the initial error. In prior years, cassette position 5 and mini-disk position 6 of the "B" Record were used as the corrected return indicator. This has now changed to cassette position 6 and mini-disk position 7 of the "B" Record. You must adjust your programs. You are strongly encouraged to read this *ENTIRE* section before attempting to make *ANY* correction. If the initial return was filed as an aggregate, you must consider this in filing the corrected return.

.02 Corrected returns submitted to IRS on magnetic media, using a "G" coded Payee "B" Record, may be submitted on the same cassette or mini-disk as those corrections submitted *without* the "G" code; however, they must be submitted using a separate "A" Record. Corrected returns for different tax years may not be submitted on the same file. Corrected returns are to be identified as correction on the transmittal document and the *EXTERNAL* affixed label of the file.

.03 The instructions that follow wil provide information on how to file corrected returns on magnetic media. The 1986 "Instructions for 1099, 1098, 5498, 1096, and W-2G" provide more specific instructions for filing corrections on paper forms and are available from IRS.

.04 *If you are not required to file your corrections on magnetic media and you file them on paper forms, do not submit the paper returns to the National Computer Center. All paper returns, whether original or corrected, must be filed with the appropriate service center. Corrected returns filed on magnetic media must be filed with the National Computer Center.* Refer to Part A, Sec. 13 for the address.

.05 Statements to the recipient or participant should be identified as "CORRECTED" and should be provided to them as soon as possible.

.06 If you file corrected returns on paper forms, use IRS forms or acceptable OCR scannable paper substitutes. Pinhole feeds on the forms are not acceptable. Always submit Copy A to the appropriate service center. *NOTE:* Form W-2G is not required to be in OCR scannable format. Publication 1179, "Specifications for Paper Substitutes for Forms 1096, 1098, 1099, 5498, and W-2G" provides requirements and instructions.

.07 For instructions on filing information returns with IRS, refer to the 1986 "Instructions for Forms 1099, 1098, 5498, and W-2G." If these instructions are not included in your magnetic media reporting packages, request a copy from IRS.

.08 Type or machine print in black carbon based ink all information on returns filed on paper. Print money amounts without dollar signs ($), ampersands (&), asterisks (*), commas (,), or other special characters. Use decimal points (.) to indicate dollars and cents on paper forms only, not on magnetic media.

.09 Use the proper form. If you are in doubt, review the instructions noted in .07 above or contact your local IRS office.

.10 Use only the boxes provided on the paper forms. Do not add additional boxes.

.11 Do not change the title of any box on any forms and do not insert data in the untitled shaded areas.

.12 Use the same name and TIN (SSN or EIN) for the filer on the Form 1096 transmittal form and all related forms that follow.

.13 A separate transmittal Form 1096 is required for each *type* of paper information return filed in the 1098, 5498, W–2G, and 1099 series. DO NOT USE THE SAME TRANSMITTAL DOCUMENT TO FILE ORIGINAL AND CORRECTED RETURNS WHETHER ON PAPER FORMS *OR* MAGNETIC MEDIA. A transmittal Form 4804 or computer generated substitute is used to transmit magnetic media. A Form 4802 is a *continuation* form for a Form 4804. Please utilize a Form 4802 if you file on magnetic media for multiple payers and are an authorized agent for the payers.

.14 Do not cut, staple, fold, paperclip, tape, or use rubberbands on any paper information returns filed with IRS. This could impair the OCR scanning process. No photocopies of any forms are allowable.

.15 Use the correct tax year's forms to file information returns with IRS (*i.e.*, do not submit tax year 1986 returns using 1985 forms). The same is true for magnetic media filing. You must submit your returns filed on magnetic media using the revenue procedure for the tax year of the returns. Forms and revenue procedures are normally updated each year to include necessary changes.

.16 Most information returns contain a "VOID" box and a "CORRECTED" box. The "VOID" box is used only if you make an error while typing or printing the paper forms. Mark this box ONLY when you wish to return to be disregarded or passed over. The OCR scanner at the service centers *will not read* a "VOID" return; it will pass over it and go to the next form if the "VOID" box is marked. Do not confuse the "VOID" box and the "CORRECTED" box.

.17 On magnetic media files, the Payee "B" Record provides space to enter a Payer's Account Number for the Payee. This same account number may be provided on paper forms. In order to properly file corrected returns, this number will help identify the appropriate incorrect return. DO NOT ENTER A TIN (SSN OR EIN). *A PAYER'S ACCOUNT NUMBER FOR THE PAYEE MAY BE A CHECKING ACCOUNT NUMBER, SAVINGS ACCOUNT NUMBER, SERIAL NUMBER OR ANY OTHER NUMBER ASSIGNED TO THE PAYEE BY THE PAYER, WHICH WILL DISTINGUISH THE SPECIFIC ACCOUNT. THIS NUMBER MUST APPEAR ON THE INITIAL RETURN AND ON THE CORRECTED RETURN IN ORDER TO IDENTIFY AND PROCESS THE CORRECTION PROPERLY.*

.18 REVIEW THE CHART THAT FOLLOWS. The types of errors made will *normally* fall under one of the three categories listed. Next to each *type* of error made, you will find a list of instructions to tell you how to *properly* file the corrected return for *that* type of error. READ ALL OF THE INSTRUCTIONS LISTED AND FOLLOW THEM FOR THE TYPE OF ERROR MADE ON THE INITIAL RETURN. *IN SOME CASES TWO TRANSACTIONS ARE REQUIRED TO PROPERLY FILE CORRECTIONS. IF THE ORIGINAL RETURN WAS FILED AS AN AGGREGATE, YOU MUST CONSIDER THIS IN FILING THE CORRECTED RETURNS.*

Guidelines for Filing Corrected Returns on Magnetic Media

(PLEASE READ SEC. 10.01 THROUGH 10.18 OF THIS PUBLICATION BEFORE MAKING *ANY* CORRECTIONS)

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
1. Original return was filed with *NO* Payee TIN (SSN or EIN), *OR* the return was filed with an *INCORRECT* Payee TIN.	A. *Form 4804 and 4802 (or computer generated substitute)* 1. Prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers) or a computer generated substitute, that includes information related to this new file. 2. Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute. 3. Provide *ALL* requested information correctly. 4. Include a hardcopy print, listing or cassette or mini-disk dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format*. 5. If you are a Combined Federal/State filer on mini-disk, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer. B. *1098, 1099 Series, 5498 and W–2G Returns* 1. Prepare a new file. 2. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported. The information in the "A" Record will be the same as it was in the original submission.

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
	3. The Payee "B" Record must contain exactly the san information as submitted previously *EXCEPT:* insert "G" code in cassette position 6 or mini-disk position of the "B" Record and supply the correct TIN (SSN EIN). (In prior years, cassette position 5 and mini-di position 6 were used as the corrected return indicato This has now changed to cassette position 6 and mi disk position 7. You must adjust your programs.) **4. Corrected returns submitted to IRS using a "G" cod "B" Record may be submitted on the same cassette mini-disk as those returns submitted *without* the "C code; however, separate "A" Records are required.** **5. Mark the *EXTERNAL* label of the cassette or mi disk "MAGNETIC MEDIA CORRECTION."** **6. Submit the cassette(s) or mini-disk(s), a cassette or mi disk dump showing sample records coded for this ty of filing, and the transmittal document to the Nation Computer Center. (Refer to Part A, Sec. 13 for addre information.)**
2. Original return was filed with an incorrect money amount(s) in the Payee "B" Record, *OR* a money amount was reported using an incorrect Payment Amount Indicator in the original Payer/Transmitter "A" Record. Correct *Type Of Return* indicator ws used in the "A" Record. (NOTE: If the wrong *Type Of Return* indicator was used, see number 3 of this chart.)	**A. *Form 4804 and/or 4802 (or computer generated substitute)*** **1. Prepare a *new* transmittal Form 4804 (and 4802 if yo file for multiple payers), or a computer generated su stitute, that includes information related to this ne file.** **2. Mark the Correction box in Block 1 of the 1986 revi copy of Form 4804. If the 1986 form is not availabl write, type or machine print in uppercase lette "MAGNETIC MEDIA CORRECTION" at the top the transmittal form or computer generated substitut** **3. Provide *ALL* requested information correctly.** **4. Include a hardcopy print, listing or cassette or mi disk dump exhibiting a small sample of each type *record* (A, B, C, and F), which can be reviewed f accuracy and acceptability of record *format.*** **5. If you are a Combined Federal/State filer on mini-dis IRS will not transmit corrected returns to the state. Th will be the responsibility of the filer.** **B. *1098, 1099 Series, 5498 and W-2G Returns*** **1. Prepare a *new* file.** **2. Use a separate Payer/Transmitter "A" Record for eac *type* of return being reported. The information in th "A" Record will be the same as it was in the origina submission EXCEPT, the *correct* Amount Indicato will be used.** **3. The Payee "B" Record must contain exactly the sam information as submitted previously *EXCEPT:* insert "G" code in cassette position 6 or mini-disk position of the "B" Record *AND* report the correct payme amounts as they should have been reported on the initia return. (In prior years, cassette position 5 and mi disk position 6 were used as the corrected return i dicator. This has now changed to cassette position and mini-disk position 7. You must adjust your pro grams.)** **4. Corrected returns submitted to IRS using a "G" code "B" Record may be submitted on the same cassette mini-disk as those returns submitted *without* the "G code; however, separate "A" Records are required.**

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
	5. Mark the *EXTERNAL* label of the cassette or mini-disk "MAGNETIC MEDIA CORRECTION." 6. Submit the cassette(s) or mini-disk(s), a cassette or mini-disk dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for address information.) 3. The Payee "B" Record must contain exactly the same information as submitted previously *EXCEPT:* insert a "G" code in cassette position 6 or mini-disk position 7 of the "B" Record and supply the correct TIN (SSN or EIN). (In prior years, cassette position 5 and mini-disk position 6 were used as the corrected return indicator. This has now changed to cassette position 6 and mini-disk position 7. You must adjust your programs.) 4. Corrected returns submitted to IRS using a "G" coded "B" Record may be submitted on the same cassette or mini-disk as those returns submitted *without* the "G" code; however, separate "A" Records are required. 5. Mark the *EXTERNAL* label of the cassette or mini-disk "MAGNETIC MEDIA CORRECTION." 6. Submit the cassette(s) or mini-disk(s), a cassette or mini-disk dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for address information.)
2. Original return was filed with an incorrect money amount(s) in the Payee "B" Record, *OR* a money amount was reported using an incorrect Payment Amount Indicator in the original Payer/Transmitter "A" Record. Correct *Type Of Return* indicator ws used in the "A" Record. (NOTE: If the wrong *Type Of Return* indicator was used, see number 3 of this chart.)	A. *Form 4804 and/or 4802 (or computer generated substitute)* 1. Prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers), or a computer generated substitute, that includes information related to this new file. 2. Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute. 3. Provide *ALL* requested information correctly. 4. Include a hardcopy print, listing or cassette or mini-disk dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format.* 5. If you are a Combined Federal/State filer on mini-disk, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer. B. *1098, 1099 Series, 5498 and W-2G Returns* 1. Prepare a *new* file. 2. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported. The information in the "A" Record will be the same as it was in the original submission EXCEPT, the *correct* Amount Indicators will be used. 3. The Payee "B" Record must contain exactly the same information as submitted previously *EXCEPT:* insert a "G" code in cassette position 6 or mini-disk position 7 of the "B" Record *AND* report the correct payment amounts as they should have been reported on the initial return. (In prior years, cassette position 5 and mini-disk position 6 were used as the corrected return in-

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
	dicator. This has now changed to cassette position and mini-disk position 7. You must adjust your programs.) 4. Corrected returns submitted to IRS using a "G" code "B" Record may be submitted on the same cassette c mini-disk as those returns submitted *without* the "G code; however, separate "A" Records are required. 5. Mark the *EXTERNAL* label of the cassette or min disk "MAGNETIC MEDIA CORRECTION." 6. Submit the cassette(s) or mini-disk(s), a cassette or min disk dump showing sample records coded for this typ of filing, and the transmittal document to the Nationa Computer Center. (Refer to Part A, Sec. 13 for addres information.)
3. Original return was filed using the WRONG *Type of Return* indicator in the Payer/Transmitter "A" Record. (For example, a return was coded using the *Type of Return* indicator for 1099-DIV and it should have been coded for 1099-INT.) THIS WILL REQUIRE TWO SEPARATE TRANSACTIONS TO MAKE THE CORRECTION PROPERLY. READ AND FOLLOW *ALL* INSTRUCTIONS FOR *BOTH* TRANSACTIONS 1 AND 2.	*TRANSACTION 1:* Identify return submitted with an incorrec Type of Return indicator A. *Form 4804 and 4802 (or computer generated substitute)* 1. Prepare a *new* transmittal Form 4804 (and 4802 if yo file for multiple payers), or a computer generated sub stitute, that includes information related to this nev file. 2. Mark the Correction box in Block 1 of the 1986 revise copy of Form 4804. If the 1986 form is not available write, type or machine print in uppercase letter "MAGNETIC MEDIA CORRECTION" at the top o the transmittal form or computer generated substitute 3. Provide *ALL* requested information correctly. 4. Include a hardcopy print, listing or cassette or mini disk dump exhibiting a small sample of each type o *record* (A, B, C, and F), which can be reviewed fo accuracy and acceptability of record *format.* 5. If you are a Combined Federal/State filer on mini-disk IRS will not transmit corrected returns to the state. Thi will be the responsibility of the filer. B. *1098, 1099 Series, 5498 and W–2G Returns* 1. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported. The information in the "A" Record will be exactly the same as it was in the original submission using the same incorrect type o return indicator. 2. The corrected Payee "B" Record must contain the same information as submitted previously *EXCEPT:* insert a "G" code in cassette position 6 or mini-disk position 7 of the "B" Record and for *ALL* payment amounts *used,* enter "0" (zero). (In prior years, cassette position 5 and mini-disk position 6 were used as the corrected return indicator. This has now been changed to cassette position 6 and mini-disk position 7. You must adjust your programs.) 3. Corrected returns submitted to IRS using a "G" coded "B" Record may be submitted on the same cassette or mini-disk as those returns submitted *without* the "G" code; however, separate "A" Records are required. 4. Mark the *EXTERNAL* label of the cassette or mini-disk "MAGNETIC MEDIA CORRECTION."

Error Made on the Original Return Filed on Magnetic Media	How To File the Corrected Return on Magnetic Media
	5. Submit the cassette(s) or mini-disk(s), a cassette or mini-disk dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for address information.) *TRANSACTION 2:* Report the correct information A. *Form 4804 and 4802 (or computer generated substitute)* 1. If you submit records with the corrected information on a separate cassette or mini-disk from those that are "G" coded, prepare a *new* transmittal Form 4804 (and 4802 if you file for multiple payers), or a computer generated substitute, that includes information related to this new file. 2. Mark the Correction box in Block 1 of the 1986 revised copy of Form 4804. If the 1986 form is not available, write, type or machine print in uppercase letters "MAGNETIC MEDIA CORRECTION" at the top of the transmittal form or computer generated substitute. 3. Provide *ALL* requested information correctly. 4. Include a hardcopy print, listing or cassette or mini-disk dump exhibiting a small sample of each type of *record* (A, B, C, and F), which can be reviewed for accuracy and acceptability of record *format.* 5. If you are a Combined Federal/State filer on mini-disk, IRS will not transmit corrected returns to the state. This will be the responsibility of the filer. B. *1098, 1099 Series, 5498 and W–2G Returns* 1. Prepare a *new* file with the correct information in *ALL* records. 2. Use a separate Payer/Transmitter "A" Record for each *type* of return being reported and use the correct Type Of Return indicator. 3. *Do not code the Payee "B" Record as a corrected return for this type of correction.* 4. Provide all of the correct information. 5. Mark the *EXTERNAL* label of the cassette or mini-disk "MAGNETIC MEDIA CORRECTION." 6. Submit the cassette(s) or mini-disk(s), a cassette or mini-disk dump showing sample records coded for this type of filing, and the transmittal document to the National Computer Center. (Refer to Part A, Sec. 13 for address information.)

SEC. 11. TAXPAYER IDENTIFICATION NUMBER

.01 Under section 6109 of the Internal Revenue Code, recipients of all reportable payments on information returns are required to furnish taxpayer identification numbers (TINs) to the payer. The number must be furnished to the payer whether or not the payee is required to file a tax return or is covered by social security. Refer to Part A, Sec. 15 for a definition of Taxpayer Identification Number (TIN).

.02 The recipient's TIN is used to associate and verify amounts reported to IRS with corresponding amounts on tax returns. Therefore, it is particularly important that correct social security and employer identification numbers for payees be provided on magnetic media or paper forms submitted to IRS. *DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROES.*

.03 Under section 6676 of the Internal Revenue Code, *a $50 penalty* applies for each failure to furnish a TIN to another person who is required to file an information return, and for each failure to include a TIN on an information return. The penalty for payments other than interest or dividends applies unless the failures were due to reasonable cause and not willful neglect.

.04 With respect to all payers of interest and dividends, section 6676 of the Internal Revenue Code provides that the payer must self-assess a *$50 penalty* for each failure to include a payee's TIN or each inclusion of an incorrect TIN on an information return, unless the payer can demonstrate that the payer met the due diligence requirements in attempting to acquire correct TINs for payees. Use Form 8210, Self-Assessed Penalties Return.

.05 For any reportable payment, if the payee fails to provide a TIN to the payer, then backup withholding must be instituted for that payee. If the payer receives another TIN in the manner required from the payee within 30 days of notice from IRS, no withholding is required. If the payee has applied for a TIN, the payee may certify to this on Form W–9 by noting "Applied For" in the TIN block and by signing the form. This form then becomes an "awaiting-TIN certificate." If the TIN is not received and certified, if required, within 60 days, begin withholding and continue until you receive a TIN in the manner required.

.06 The TIN to be furnished to IRS depends primarily upon the manner in which the account is maintained or set up on the payer's record. The TIN to be provided must be that of the owner of the account. If the account is recorded in more than one name, furnish the TIN and name of one of the owners of the account. The TIN provided must be associated with the name of the payee provided in the first name line of the Payee "B" Record. For individuals, including sole proprietors, t payee TIN is the payee's social securi number. For other entities, the payee TI is the payee's employer identificatio number.

.07 Sole proprietors who are paye should show their employer identificatio number in the Payer/Transmitter "A Record. However, sole proprietors wh are not otherwise required to have an em ployer identification number should u their social security number.

.08 Sole proprietors' social securi numbers must be used in the Payee "B Record.

.09 The charts below will help you d termine the number to be furnished t IRS for recipients of reportable paymen (payees).

CHART 1. Guidelines for Social Security Numbers

For this type of account—	In the Taxpayer Identification Number field of the Payee "B" Record, enter the SSN of—	In the First Payee Name Line of th Payee "B" Record, enter the name of-
1. An individual's account.	The individual.	The individual.
2. A joint account (Two or more individuals, husband and wife).	The actual owner of the account. (If more than one owner, the first individual on the account.)	The individual whose SSN is entered.
3. Account in the name of a guardian or committee for a designated ward, minor, or incompetent person.	The ward, minor, or incompetent person.	The individual whose SSN is entered.
4. Custodian account of a minor (Uniform Gift to Minors Act).	The minor.	The minor.
5. The usual revocable savings trust account (grantor is also trustee).	The grantor-trustee.	The grantor-trustee.
6. A so-called trust account that is not a legal or valid trust under state law.	The actual owner.	The actual owner.
7. A sole proprietorship.	The owner.	The owner.

CHART 2. Guidelines for Employer Identification Numbers

For this account type—	In the Taxpayer Identification Number field of the Payee "B" Record, enter the EIN of—	In the First Payee Name Line of th Payee "B" Record, enter the name of-
1. A valid trust, estate, or pension trust.	Legal entity.[1]	The legal trust, estate, or pension trust.
2. A corporate account.	The corporation.	The corporation.
3. An association, club, religious, charitable, educational or other tax-exempt organization.	The organization.	The organization.
4. A partnership account held in the name of the business.	The partnership.	The partnership.
5. A broker or registered nominee/middleman.	The broker or nominee/middleman.	The broker or nominee/middleman.

CHART 2. Guidelines for Employer Identification Numbers—Continued

For this account type—	In the Taxpayer Identification Number field of the Payee "B" Record, enter the EIN of—	In the First Payee Name Line of the Payee "B" Record, enter the name of—
6. Account with the Department of Agriculture in the name of a public entity, such as state or local government, school district or prison, that receives agriculture program payments.	The public entity.	The public entity.

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[1] Do not furnish the identification number of the personal representative or trustee unless the name of the representative or trustee is used in the account title.

SEC. 12. EFFECT ON PAPER RETURNS

.01 Cassette or mini-disk reporting of the information returns listed in Part A, Sec. 1 applies only to the original (Copy A).

.02 For payments of dividends or interest (reported on Forms 1099–DIV, 1099–PATR, 1099–INT, or 1099–OID), the payer is required to furnish an official Form 1099 to a payee either in a separate mailing by First-Class mail or in person. These forms may not be combined or mailed with other information furnished to the recipient except Forms W–8, W–9, or other Forms 1099. The payer may use substitute Forms 1099 if they utilize the proper language, are substantially similar to the official forms and if the payer complies with all revenue procedures relating to substitute Forms 1099 in effect at the time (see Publication 1179). Copy B (For Recipient) of the substitute forms must contain the statement "This is important tax information and is being furnished to IRS. If you are required to file a return, a negligence penalty or other sanction will be imposed on you if this income is taxable and IRS determines that it has not been reported." The substitute form must contain instructions substantially similar to those on the back of Copy B of the official form.

.03 Statements to recipients for Forms 1098, 1099–A, 1099–B, 1099–G, 1099–MISC (except for substitute payments in lieu of dividends and tax-exempt interest), 1099–R, 5498, or W–2G need not be a copy of the paper form filed with IRS. It is important that income items be properly classified for Federal tax purposes on the statement the payer gives to recipients. The message "This information is being furnished to IRS" must appear on the statements. In addition, Form 1098 statements must contain the message, "The amount shown is deductible by you for Federal income tax purposes only to the extent it was actually paid by you and not reimbursed by another person." The space provisions on official paper forms do not agree with those used in magnetic media. The amount of space on paper forms is less than that allowed on magnetic media. Filers may wish to seek a substitute form for Copy B (For Recipient) that accommodates the space provisions used in magnetic media. Payers are permitted considerable flexibility in designing Copy B of the information return to be furnished to the payee. The payer may combine the information return data with other reports or financial or commercial notices so long as all required information is present and worded properly and the payee's copy is conducive to proper reporting of income on tax returns. (This does not apply to Forms 1099–INT, 1099–OID, 1099–DIV, and 1099–PATR. See .02 above for the requirements for these four forms.) However, when information not requested on the official form is included on these substitute statements, they can no longer be mailed with recipient copies of 1099–DIV, INT, OID, or PATR without violating the separate mailing requirements.

.04 If a portion of the returns is reported on cassette or mini-disk and the remainder is reported on paper forms, those returns not submitted on cassette or mini-disk (including corrected returns) may require a waiver depending on the type of return and volume. Returns filed on paper must be filed on official forms or on acceptable paper substitutes meeting the specifications in Publication 1179.

Do not submit proposed substitutes of Copy A to the National Computer Center.

Your proposed substitutes must comply to the official form and the specifications outlined in Publication 1179. *DO NOT* submit any substitutes for approval. Only those forms that comply with the official form and the specifications in Publication 1179 are acceptable.

SEC. 13. TO CONTACT THE IRS NATIONAL COMPUTER CENTER

.01 Effective January 1, 1986, magnetic media processing for all service centers was centralized at the IRS National Computer Center. Please direct all requests for IRS magnetic media related publications, information, undue hardship waivers, extensions or forms to the following addresses (if Postal Service or land carrier):

Magnetic Media Reporting
Internal Revenue Service
National Computer Center
Post Office Box 1359
Martinsburg, WV 25401–1359
or
Magnetic Media Reporting
Internal Revenue Service
National Computer Center
Route 9 & Needy Road
Martinsburg, WV 25401

Hours of operation at this address will be 8:30 A.M. until 8:00 P.M. Eastern Time Zone.

Requests for paper returns, publications or forms not related to magnetic media processing should be requested from local IRS offices or by calling the toll-free number in your area.

.02 The National Computer Center will process returns filed on magnetic media only. All information returns, including corrections, filed on paper forms should be submitted to the appropriate service center, not the National Computer Center. Organizations who file their information returns on magnetic media but who submit their corrected returns on paper forms, refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" for the service center addresses.

SEC. 14. COMBINED FEDERAL/STATE FILING

.01 The Combined Federal/State Program was established to simplify information returns filing for the taxpayer. IRS will accept, upon prior approval, mini-disk files containing state reporting information only for those states listed in Table 1 in this section. *FORMS 1098, 1099–A, 1099–B, AND W–2G CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM. DUE TO THE 256 CHARACTER RECORD RESTRICTION FOR CASSETTE FILERS, CASSETTE TAPES ARE NOT ACCEPTABLE ON THIS PROGRAM. EACH RECORD IN THE COMBINED FEDERAL/STATE PROGRAM MUST BE 360 CHARACTERS IN LENGTH; THEREFORE ONLY MINI-DISK FILES ARE ACCEPTABLE.*

.02 To request approval to participate in the Combined Federal/State Program, a "*test*" file, *coded for this program,* must be submitted by the transmitter to the IRS National Computer Center between August 15 and December 15 using the revenue procedure that will be used for the actual data files. Blanket approval will not be given to software packages. The "*test*" file is only required for the first year. Once you are approved, you do not need to resubmit "tests" each year, except when notified by IRS. Refer to Part A, Sec. 13 for the address. See Part A, Sec. 5.04 for general guidelines on submission of "*test*" files. Both the "*test*" file and the actual data file must conform *exactly* to the revenue procedure for the tax year of the *actual* data. Combined Federal/State records must be coded using each state's dollar criteria from Table 2 of this section for each *type* of return.

If the "*test*" file is determined to be acceptable, IRS will return it to the filer with Form 6847, Consent For Internal Revenue Service to Release Tax Information. The payer *must* complete Form 6847. The five character alpha/numeric Transmitter Control Code must be included on the form. The form should then be returned to IRS before IRS will release tax information to any of the participating states.

Form 6847 must be signed by one of the individuals listed at the bottom of the form. If the form is signed by an attorney-in-fact, the written consent from the taxpayer to the attorney-in-fact must be included with the Form 6847. This consent by language and/or scope must clearly indicate that the attorney-in-fact is empowered to authorize release of the information document returns to the state(s). A separate Form 6847 is required for each payer. A transmitter may not combine payers on one Form 6847 even though acting as attorney-in-fact for several payers. Form 6847 may be photocopied if you receive an insufficient number of the form. If you have filed on this program in the past and have not met these requirements, you must resubmit the Form 6847 with the proper signatures as specified. If you file for multiple payers, only code the records to go to the state(s) for those payers that participate and have properly submitted Form 6847. Do not submit *actual* data records coded for the Combined Federal/State Program without prior approval from IRS.

.03 States that participate in this program and the valid state code assigned to each are listed in Table 1 of this section. If the state that you wish information released to does *not* participate in the program, do *not* code your records for that state. If the state participates, if you have received prior approval, and if all other conditions are met, IRS will forward the tax information to the participating state at no charge to the filer. You do not need to reapply each year.

.04 *IF CORRECTIONS MUST BE MADE, IRS WILL NOT TRANSMIT CORRECTED RETURNS TO THE STATES; THIS WILL BE THE RESPONSIBILITY OF THE FILER.*

.05 IRS will make no attempt to process files with any deviations. Approval to participate in the Combined Federal/State Program will be revoked if any fil are submitted that do not *totally* conform

.06 IRS is acting as a forwarding ag *ONLY*. Some participating states requi separate notification that you are filing this manner. It is your responsibility contact the appropriate states for furth information.

.07 The appropriate state code shou be entered for those documents which me that state's filing requirements. *It is th filer's responsibility* to determine the sta code to be used and to obtain the filin requirements from the appropriate state(s

.08 If you meet all of the requiremen for this program, you *must* provide th state totals from the "K" Record on separate Form 4804, Transmittal of I formation Returns on Magnetic Media (Form 4802, Transmittal For Multip Magnetic Media Reporting) or comput generated substitute for each state, or y must include a listing which identifies ea state and the "K" Record totals for each

.09 If you have met *ALL* of the abo conditions:

(a) You must submit all records usi two 180 positions sectors which indica the appropriate coding related to this pr gram.

(b) The "C" Record *must* be followe by a "K" Record for each state. The "K Record indicates the number of paye being reported to each particular state.

(c) Payment amount totals and the val participating state code must be includ in the state totals "K" Record. Refer Part C, Sec. 15, for a description of t "K" Record.

(d) The "K" Record is followed by end of transmission "F" Record (if this the last record of the entire file).

.10 Only those states listed in Table below will receive information from IR *It is the filer's responsibility to file info mation returns with states that do not pa ticipate in this program.*

TABLE 1. PARTICIPATING STATES AND THEIR CODES

State	*Code*	*State*	*Code*	*State*	*Co*
Alabama	01	Iowa	19	New York	36
Arizona	04	Kansas	20	North Carolina	37
Arkansas	05	Maine	23	North Dakota	38
California	06	Massachusetts	25	Oregon	41
Delaware	10	Minnesota	27	South Carolina	45
District of Columbia	11	Mississippi	28	Tennessee	47
Georgia	13	Missouri	29	Wisconsin	55
Hawaii	15	Montana	30		
Idaho	16	New Jersey	34		
Indiana	18	New Mexico	35		

.11 To simplify filing, several of the participating states have been provided lists of their information return reporting requirements (see Table 2). This cumulative list is for information purposes only and represents dollar criteria. For complete information on state filing requirements, contact the appropriate state tax agencies.

TABLE 2. DOLLAR CRITERIA

STATE	1099–R	1099–DIV	1099–INT	1099–MISC	1099–PATR	1099–G	1099–OID	5498
Alabama	1500	1500	1500	1500	1500	NR	1500	NR
Arizona[a]	300	300	300	300	300	300	300	NR
Arkansas	2500	100	100	2500	2500	2500	2500	[g]
District of Columbia[b]	600	600	600	600	600	600	600	NR
Hawaii	600	10	10[c]	600	10	all	10	[g]
Idaho	600	10	10	600	10	10	10	[g]
Iowa	1000	100	1000	1000	1000	1000	1000	NR
Minnesota	600	10	10	600	10	10	10	[g]
Missouri	NR	NR	NR	1200[d]	NR	NR	NR	NR
Montana	600	10	10	600	10	10	10	[g]
New Jersey	1000	1000	1000	1000	1000	1000	1000	NR
New York	600	NR	600	600[e]	NR	600	NR	NR
North Carolina	100	100	100	600	100	100	100	[g]
Oregon	600[f]	10	10	600	10	10	10	NR
Tennessee	NR	25	25	NR	NR	NR	NR	NR
Wisconsin	500	100	100	100	100	NR	NR	NR

NR—No filing requirement.

Footnotes:

[a] These requirements apply to individuals and business entities.

[b] Amounts are for aggregates of several types of income from the same payroll.

[c] State regulation changing filing requirement from $600 to $10 is pending.

[d] The state would prefer those returns filed with respect to non-Missouri residents to be sent directly to the state agency.

[e] Aggregate of several types of income.

[f] Return required for state of Oregon residents only.

[g] Same as Federal requirement for this type of return.

*NOTE: Filing requirements for any state in Table 1 not shown on the above chart are the same as the Federal requirement.

SEC. 15. DEFINITIONS OF TERMS

Element	Description
b	Denotes a blank position. Enter blank(s) when this symbol is used (do *not* enter the letter "b"). This appears in numerous areas throughout the record descriptions.
Coding Range	Indicates the allowable codes for a particular type of statement.
EIN	Employer Identification Number that has been assigned by IRS.
Excess Golden Parachute Payment	Parachute payments (also called "golden parachutes") are certain payments in the nature of compensation that corporations make to key individuals, often in excess of their usual compensation, in the event that ownership or control of the corporation changes.
File	For purposes of this procedure, a file consists of all cassette or mini-disk records submitted by a Payer or Transmitter.
Payee	Person(s) or organization(s) receiving payments from the Payer, or for whom an information return must be filed.
Payer	Includes the person making payments, a recipient of mortgage interest payments, a broker, a barter exchange, a trustee or issuer of an IRA, SEP or DEC, or a lender who acquires an interest in secured property or who has reason to know that the property has been abandoned. The Payer will be held responsible for the completeness, accuracy and timely submission of cassette or mini-disk files.
Special Character	Any character that is not a numeral, a letter or a blank.
SSA	Social Security Administration.
SSN	Social Security Number.
Taxpayer Identification Number (TIN)	May be either an EIN or SSN.

Element	Description
Transfer Agent (Paying Agent)	The transfer agent or paying agent is the entity who has been contracted or authorized b the payer to perform the services of paying and reporting backup withholding (Form 941) The payer must submit to IRS a Form 2678, Employer Appointment of Agent under sectio 3504, which notifies IRS of the transfer agent relationship.
Transmitter	Person or organization preparing cassette or mini-disk file(s). May be Payer or agent of Payer
Transmitter Control Code (TCC)	A *five* character alpha/numeric number assigned by IRS to the transmitter prior to actua filing on magnetic media. This number is inserted in the "A" Record of your files and *mu* be present before the file can be processed. An application Form 4419 must be filed with IR to receive this number. See Part A, Sec. 5. (Abbreviation for this term is TCC.)

SEC. 16. U.S. POSTAL SERVICE STATE AND COUNTRY ABBREVIATIONS

.01 You *MUST* use the following U.S. Postal Service state abbreviations and foreign country codes when developing the state code portion of address fields. (This table provides state abbreviations only and does not represent those states participating in the Combined Federal/Sta Program. For a list of states that partic pate in the Combined Federal/State Pr gram, refer to Part A, Sec. 14.10.)

State	Code	State	Code	State	Cod
Alabama	AL	Kentucky	KY	North Dakota	ND
Alaska	AK	Louisiana	LA	Ohio	OH
Arizona	AZ	Maine	ME	Oklahoma	OK
Arkansas	AR	Maryland	MD	Oregon	OR
California	CA	Massachusetts	MA	Pennsylvania	PA
Colorado	CO	Michigan	MI	Rhode Island	RI
Connecticut	CT	Minnesota	MN	South Carolina	SC
Delaware	DE	Mississippi	MS	South Dakota	SD
District of Columbia	DC	Missouri	MO	Tennessee	TN
Florida	FL	Montana	MT	Texas	TX
Georgia	GA	Nebraska	NE	Utah	UT
Hawaii	HI	Nevada	NV	Vermont	VT
Idaho	ID	New Hampshire	NH	Virginia	VA
Illinois	IL	New Jersey	NJ	Washington	WA
Indiana	IN	New Mexico	NM	West Virginia	W
Iowa	IA	New York	NY	Wisconsin	W
Kansas	KS	North Carolina	NC	Wyoming	W

.02 The following list represents Canadian Provinces and the corresponding code to be associated with each.

Province	Code	Province	Code	Province	Co
Alberta	AB	British Columbia	BC	Labrador	L
Manitoba	MB			New Brunswick	N
Newfoundland	NF	Nova Scotia	NS	Northwest Territories	N
Ontario	ON	Prince Edward Island	PE		
Quebec	PQ			Saskatchewan	S
Yukon Territories	YK				

.03 The following list represents foreign countries and the corresponding code to be associated with each.

Foreign Country	Code
Afghanistan	AF
Albania	AL
Algeria	AG
American Samoa	AQ
Andorra	AN
Angola	AO
Antarctica	AY
Antigua & Barbuda	AC
Argentina	AR
Australia	AS
Austria	AU
Azores	PO
Bahamas, The	BF
Bahrain	BA
Bangladesh	BG
Barbados	BB
Belgium	BE
Belize (Formerly British Honduras)	BH
Benin (Formerly Dahomey)	DM
Bermuda	BD
Bhutan	BT
Bolivia	BL
Botswana	BC
Brazil	BR
British Indian Ocean Territory	IO
British Virgin Islands	VI
Brunei	BX
Bulgaria	BU
Burma	BM
Burundi	BY
Cambodia	CB
Cameroon	CM
Canada	CA
Canton & Enderbury Islands	EQ
Canary Islands	SP
Cape Verde, Republic of	CV
Cayman Islands	CJ
Central Africa Republic	CT
Chad	CD
Channel Islands	OC
Chile	CI
China (Peking)	CH
China (Taiwan)	TW
Christmas Island	KT
Cocos (Keeling) Islands	CK
Colombia	CO

Foreign Country	Code
Comoros	CN
Congo	CF
Cook Islands	CW
Costa Rica	CS
Cuba	CU
Cyprus	CY
Czechoslovakia	CZ
Denmark	DA
Djibouti (Formerly Afars & Issas)	DJ
Dominica	DO
Dominican Republic	DR
Ecuador	EC
Egypt	EG
El Salvador	ES
England	UK
Equatorial Guinea	EK
Ethiopia	ET
Falkland Islands (Also called Islas Malvinas)	FA
Faroe Islands	FO
Fiji	FJ
Finland	FI
France	FR
French Guiana	FG
French Polynesia	FP
French Southern & Antarctic Lands	FS
Gabon	GB
Gambia, The	GA
German Democratic Republic (East Germany)	GC
Germany, Federal Republic of (West Germany)	GE
Ghana	GH
Gibraltar	GI
Gilbert Islands	GS
Greece	GR
Greenland	GL
Grenada	GJ
Guadeloupe	GP
Guam	GQ
Guatemala	GT
Guinea	GV
Guinea-Bissau	PU
Guyana	GY
Haiti	HA
Heard Island & McDonald Island	HM

Foreign Country	Code
Honduras	HO
Hong Kong	HK
Hungary	HU
Iceland	IC
India	IN
Indonesia	ID
Iran (Also called Persia)	IR
Iraq	IZ
Ireland	EI
Isle of Man	OC
Israel	IS
Italy	IT
Ivory Coast	IV
Jamaica	JM
Japan	JA
Johnston Atoll	JQ
Jordan	JO
Kenya	KE
Korea, Democratic Peoples Republic of (North Korea)	KS
Kuwait	KU
Laos	LA
Lebanon	LE
Lesotho	LT
Liberia	LI
Libya	LY
Liechtenstein	LS
Luxembourg	LU
Macao	MC
Madagascar	MA
Malawi	MI
Malaysia	MY
Maldives	MV
Mali	ML
Malta	MT
Martinique	MB
Mauritania	MR
Mauritius	MP
Mexico	MX
Midway Islands	MQ
Monaco	MN
Mongolia	MG
Montserrat	MH
Morocco	MO
Mozambique	MZ
Nauru	NR
Navassa Island	BQ
Nepal	NP
Netherlands (Also called Holland)	NL
Netherlands Antilles	NA
New Caledonia	NC
Vanuatu (Also called New Hebrides)	NH
New Zealand	NZ
Nicaragua	NU

Foreign Country	Foreign Code
Niger	NG
Nigeria	NI
Niue	NE
Norfolk Island	NF
Northern Ireland	UK
Norway	NO
Oman	MU
Pakistan	PK
Panama	PM
Papua-New Guinea	PP
Paracel Islands	PF
Paraguay	PA
Peru	PE
Philippines	RP
Pitcairn	PC
Poland	PL
Portugal	PO
Portuguese Timor	PT
Puerto Rico	RQ
Qatar	QA
Reunion	RE
Romania	RO
Rwanda	RW
St. Christopher-Nevis-Anguilla (Also called St. Kitts)	SC
St. Helena	SH
St. Lucia	ST
St. Pierre & Miquelon	SB
St. Vincent	VC
San Marino	SM
Sao Tome and Principe	TP
Saudi Arabia	SA
Scotland	UK
Senegal	SG
Seychelles	SE
Sierra Leone	SL
Singapore	SN
Solomon Islands	BP
Somalia	SO
South Africa	SF
Southern Rhodesia	RH
South-West Africa (Also called Namibia)	WA
Spain	SP
Spratly Islands	PG
Sri Lanka (Also called Ceylon)	CE
Sudan	SU
Surinam	NS
Svalbard & Jan Mayen	JS
Swaziland	WZ
Sweden	SW
Switzerland	SZ
Syria	SY
Tanzania	TZ
Thailand	TH
Togo	TO
Tokelau Islands	TL
Tonga	TN
Trinidad & Tobago	TD
Trust Territory of the Pacific Islands	TQ
Tunisia	TS
Turkey	TU
Turks & Caicos Islands	TK
Tuvalu (Also called Ellice Islands)	TV
Uganda	UG
Union of Soviet Socialist Republics	UR
United Arab Emirates	TC
United Kingdom	UK
United States	US
Upper Volta	UV
Uruguay	UY
Vatican City	VT
Venezuela	VE
Vietnam	VM
Virgin Islands of the U.S.	VQ
Wake Island	WQ
Wales	UK
Wallis & Futuna	WF
Western Sahara	WI
Western Samoa	WS
Yemen (South)	YS
Yemen (North)	YE
Yugoslavia	YO
Zaire	CG
Zambia	ZA
Zimbabwe	RH

PART B. CASSETTE SPECIFICATIONS

SECTION 1. GENERAL

.01 The specifications contained in this part of the revenue procedure define the required format and contents of the records to be included in the cassette file. These specifications must be adhered to unless deviations have been specifically granted by IRS.

.02 In most instances, IRS will be able to process any compatible cassette files. IRS has a Burroughs B–94 model mini-computer with free standing NRZ and PE cassette devices, style B 9497–11 and B 9497–15, respectively. We understand that most Burroughs B–90 series mini-computers will produce compatible cassettes.

.03 A cassette contains a minimum of 282 feet (86m) of 2 track recording tape and a minimum of 6 inches (15.24 cm) of clear leader at both ends of the tape.

.04 Data is recorded on the cassette at a maximum density of 800 bits per inch (BPI) for NRZ cassettes and 1600 BPI for PE cassettes.

.05 The recording technique is either non-return to zero (NRZ) or Phase Encoded (PE).

.06 When the NRZ technique is used, both tracks of the cassette are recorded simultaneously; data is recorded on one track and a synchronizing clock impulse is recorded on the other.

.07 When the PE technique is used, there is no requirement for a separate clock pulse track; one track is recorded when the cassette is driven in one direction, and the other track is recorded when the tape drive is driven in the other direction. Therefore, two PE data tracks can be recorded over the full length of the tape.

.08 The data is recorded in blocks of characters, separated by interblock gaps (IBGs). Records may not span blocks.

.09 The recording mode is 9 channel ASCII (American Standard Coded Information Interchange) or EBCDIC (Extended Binary Coded Decimal Interchange Code).

.10 The industry standard for cassettes is odd parity.

.11 The maximum block size is 256 characters.

.12 Each block of characters is followed by two 8-bit Cyclic Redundanc Check (CRC) characters which serve as parity check on the data block durin reading operations.

.13 The data characters plus the CR characters are preceded and followed b a Preamble character and a Postambl character which serve to delimit the dat block.

.14 Tape marks which consist of a fixe number of null characters (all zero bit are used to delimit logical portions of th cassette and also to mark the end of th file of data.

.15 Cassettes may be either labeled unlabeled.

.16 Each block of data, including tap marks, are separated from the next bloc by the interblock gap (IBGs). The IB is 1.4 inches (3.5 cm) in length. A tap mark length is approximately 6 inches (1 cm) in length.

.17 The beginning of the tape is marke by a BOT mark. This is a hole in the tap used to define the start of the recordin tape. It is recommended that a tape mar reamble character, null character (one haracter in which all bits are zero), a ostamble character and ending label be laced on the cassette immediately after nd of tape (EOT) is reached.

.18 An external label, Form 5064, must ppear on each cassette submitted for rocessing. The following information is eeded:

(a) The transmitter's name.

(b) The five character alpha/numeric Transmitter Control Code.

(c) State of sender (*e.g.*, NY).

(d) Tape density.

(e) Check box (magnetic tape filers nly).

(f) Track (magnetic tape filers only).

(g) Recording code (*e.g.*, EBCDIC or SCII).

(h) The tax year of the data (*e.g.*, 1986).

(i) Document types (*e.g.*, 1099–INT).

(j) The total number of "B" Records fter each "A" Record (this figure is taken rom the "C" Records).

(k) A number assigned by the transmitter to the tape.

(l) The sequence of each cassette (*e.g.*, 01 of 008).

The external media label, Form 5064, vas updated for tax year 1986. You must se the updated label. This information vill assist IRS in processing the file or in ocating a file, should the transmitter request that it be returned due to errors. *RS advises that special shipping conainers not be used for transmitting data since it cannot be guaranteed that they will be returned.*

SEC. 2. RECORD LENGTH

.01 The cassette records defined in this revenue procedure may be blocked or unblocked, subject to the following:

(a) A block must not exceed 256 cassette positions.

(b) A record must be a minimum of 200 positions and a maximum of 256 positions. Due to this restriction, cassette filers may not participate in the Combined Federal/State Program; cassette filers may only report a maximum of six payment amounts for any single record; also, Forms 1099–A, 1099–B and W–2G cannot be filed on cassette.

(c) If the use of blocked records would result in a short block, all remaining positions of the block must be filled with 9's. DO NOT PAD A BLOCK WITH BLANKS.

(d) All records except the Header and Trailer Labels, may be blocked.

(e) Records may not span blocks.

SEC. 3. PAYER/TRANSMITTER "A" RECORD

.01 Identifies the payer and transmitter of the cassette file and provides parameters for the succeeding Payee "B" Records. IRS computer programs rely on the absolute relationship between the parameters and data fields in the "A" Record and the data fields in the "B" Records to which they apply.

.02 The number of "A" Records appearing on a cassette will depend on the number of payers and the different types of returns being reported. After the header label on the cassette, the first record appearing in the file must be an "A" Record. For cassette filing, the *actual* record lengths for the "A" and "B" Records must agree with whatever is entered in cassette positions 28–30 and 31–33 of the "A" Record. A transmitter may include Payee "B" Records for more than one payer on a cassette; however, each GROUP of Payee "B" Records must be preceded by an "A" Record. A single cassette may also contain different types of returns, but the types of returns *must* not be intermingled. A separate "A" Record is required for each type of return being reported. An "A" Record may be blocked with "B" Records; however, the initial record on a *file* must be an "A" Record. IRS will accept an "A" Record after a "C" Record. For cassette files, do not begin any record at the end of a block and continue the same record into the next block.

.03 All alpha characters entered in the "A" Record should be uppercase.

.04 *WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*

RECORD NAME: PAYER/TRANSMITTER "A" RECORD

Cassette Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "A".
2	Payment Year	1	REQUIRED. Must be the right most digit of the year for which information is being reported. (*e.g.*, if payments were made in 1986, enter "6"). Must be incremented each year.
3–5	Cassette Sequence Number	3	REQUIRED. The cassette sequence number incremented by 1, for each cassette tape on the file starting with 001. (Blanks are acceptable or all zeros.)
6–14	Payer's Federal EIN	9	REQUIRED. Must be the *valid* 9-digit number assigned to the payer by IRS. DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS. (Also see Part A, Sec. 11.07.)
15–16	Blank	2	REQUIRED. Enter blanks.
17	Type of Return	1	REQUIRED. Enter appropriate code from table below:

Type of Return	Code
1098	3
1099–DIV	1
1099–G	F
1099–INT	6

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Cassette Position	Field Title	Length	Description and Remarks
			1099–MISC 1099–OID 1099–PATR 1099–R 5498

NOTE: Forms 1099–A, 1099–B and W–2G cannot be filed on cassette due to the 256 character record restrictio

Cassette Position	Field Title	Length	Description and Remarks
18–23	Amount Indicators	6	REQUIRED. *In most cases, the boxes or Amount Indicators o paper information returns correspond with the Amount Codes us to file on magnetic media; however, should you notice discrepanci between this revenue procedure and paper forms, please disrega them and program according to this revenue procedure for yo returns filed on magnetic media.* For specific instructions on info mation to be reported in each Amount Code, refer to the 19 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G." T amount indicators entered for a given type of return indicate type(of payment(s) which were made. For each Amount Code entere in this field, a corresponding payment amount must appear in t Payee "B" Record. Example: If position 17 of the Payer/Transmitt "A" Record is "6" (for 1099–INT) and positions 18–23 are "123bbb this indicates that 3 payment amount fields are present in all of t following Payee "B" Records. The first payment amount field the Payee "B" Record will represent Earnings from savings a loan associations, credit unions, bank deposits, bearer certifica of deposit, etc., the second will represent Amount of forfeitu and the third will represent Federal income tax withheld. Enter t Amount Indicators in ASCENDING SEQUENCE (*i.e.*, 1247bb left-justify, filling unused positions with blanks. For any furth clarification of the Amount Indicator codes, you may contact t IRS National Computer Center.

Amount Indicators Form 1098— Mortgage Interest Statement

For Reporting Interest Received from Payer(s) on Form 1098:

Amount Code	Amount Type
1	Mortgage interest received from payer(s)
2	Optional field for items such as real estate taxes insurance paid from escrow

NOTE: THE PERSON FOR WHOM YOU ARE RECEIVING THE INTEREST NEED NOT FILE FO 1098, AND NO ADDITIONAL REPORTING IS REQUIRED FOR THE TRANSFER OF INTERE FROM THE SERVICING BANK TO THE LENDER.

Amount Indicators Form 1099–DIV— Dividends and Distributions

For Reporting a maximum of six Payments on Form 1099–DI

Amount Code	Amount Type
1	Gross dividends and other distributions on sto
2	Dividends qualifying for exclusion
3	Dividends not qualifying for exclusion
4	Federal income tax withheld
5	Capital gain distributions
6	Nontaxable distributions (if determinable)
7	Foreign tax paid
8	Cash liquidation distributions
9	Noncash liquidation distributions (Show fair m value)

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

assette osition	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–G— Certain Government Payments		For Reporting Payments on Form 1099–G:

Amount Code	Amount Type
1	Unemployment compensation
2	State or local income tax refunds
4	Federal income tax withheld
5	Discharge of indebtedness
6	Taxable grants
7	Agriculture payments

assette osition	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–INT— Interest Income		For Reporting Payments on Form 1099–INT:

Amount Code	Amount Type
1	Earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposit, etc.
2	Amount of forfeiture
3	Federal income tax withheld
4	Foreign tax paid (if eligible for foreign tax credit)
5	U.S. Savings Bonds, etc.

assette osition	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–MISC— Miscellaneous Income (See Notes 1, 2, and 3)		For Reporting a maximum of six Payments on Form 1099–MISC:

Amount Code	Amount Type
1	Rents
2	Royalties
3	Prizes and awards
4	Federal income tax withheld
5	Fishing boat proceeds
6	Medical and health care payments
7	Nonemployee compensation
8	Direct sales "*indicator*" (see NOTE 1)
9	Substitute payments in lieu of dividends or interest (see NOTE 2)

NOTE 1: Use Amount Code "8" to report that *direct sales* of consumer products of $5,000 or more to the payee on a buy-sell, deposit-commission, or other basis *for resale* were made. Do not use this indicator for amounts of less than $5,000. The use of Amount Code "8" actually reflects an *indicator of direct sales* and not an actual payment amount or amount code. The corresponding payment amount field in the Payee "B" Record MUST be reflected as 0000000100. This does not mean that a payment of $1.00 was made or is being reported. The use of Amount Code "8" relates directly to cassette position "4," Document Specific Code and NOTE 2 of the Payment Amount Field in the Payee "B" Record. (If you use Amount Code "8" in the "A" Record, you will enter a "1" in cassette position "4" of the "B" Record. For any other 1099–MISC Amount Codes, you will enter a "0" (zero) in cassette position "4" of the "B" Record.)

NOTE 2: Brokers are subject to a reporting requirement for payments received after 1984. Brokers who transfer securities of a customer for use in a short sale must use Amount Code 9 to report the aggregate payments received in lieu of dividends or tax-exempt interest on behalf of a customer while the short sale was open. Generally, for substitute payments in lieu of dividends, a broker is required to file a Form 1099–MISC for each affected customer who is *not* an individual. Refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" for detailed information. The instructions are available from IRS offices.

NOTE 3: If you are reporting Excess Golden Parachute Payments, use paper Forms 1099–MISC. Do not report these payments on magnetic media. See Part A, Sec. 15 for a definition of an Excess Golden Parachute Payment.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Cassette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–OID—Original Issue Discount		For Reporting Payments on Form 1099–OID:

Amount Code	Amount Type
1	Total original issue discount for 1986
2	Other periodic interest (the regular interest paid this obligation without regard to any original is discount)
3	Amount of forfeiture
4	Federal income tax withheld

Cassette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–PATR—Taxable Distributions Received From Cooperatives		For Reporting a maximum of six Payments on Form 1099–PAT

Amount Code	Amount Type
1	Patronage dividends
2	Nonpatronage distributions
3	Per-unit retain allocations
4	Federal income tax withheld
5	Redemption of nonqualified notices and retain locations
6	Investment credit (See NOTE)
7	Energy investment credit (See NOTE)
8	Jobs credit (See NOTE)

NOTE: The amounts shown for Amount Indicators "6," "7" and "8" must be reported to the payee; howeve since these amounts are not taxable, they need not be reported to IRS.

Cassette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–R—Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, etc. (See NOTE)		For Reporting a maximum of six Payments on Form 1099–R:

Amount Code	Amount Type
1	Amount includable as income (add amounts in cod 2 and 3)
2	Capital gain (for lump-sum distributions only)
3	Ordinary income
4	Federal income tax withheld
5	Employee contributions (profit-sharing or reti ment plans) or insurance premiums
6	IRA, SEP or DEC distributions
7	State income tax withheld
8	Net unrealized appreciation in employer's securiti
9	Other

NOTE: A distribution from a KEOGH plan should be reported in Amount Codes 1, 2 or 3 as appropriate.

Cassette Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 5498—Individual Retirement Arrangement Information		For Reporting Payments on Form 5498:

Amount Code	Amount Type
1	Regular SEP contributions made in 1986 and 19 for 1986. Include only employer contributions her Enter any employee contributions to a SEP in Co 3.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Cassette osition	Field Title	Length	Description and Remarks
		2	Rollover IRA, SEP or DEC contributions
		3	Regular IRA or DEC contributions made in 1986 and 1987 for 1986
		4	Life insurance cost included in Code 1 or 3 (for endowment contracts only)

NOTE: Form 5498 is filed for contributions to be applied to 1986 that are made between January 1, 1986, and April 15, 1987.

4–27	Blank	4	REQUIRED. Enter blanks.
8–30	"A" Record Length	3	REQUIRED. Enter the number of positions used or that you have allowed for the "A" Record. For cassette filing, the "actual" record length *must* agree with whatever you enter in this field. The record must not exceed 256 characters.
31–33	"B" Record Length	3	REQUIRED. Enter the number of positions used or that you have allowed for the "B" Record. For cassette filing, the "actual" record length *must* agree with whatever you enter in this field. The record must not exceed 256 characters.
34	Blank	1	REQUIRED. Enter blank.
35–39	Transmitter Control Code (TCC)	5	REQUIRED. Enter the five character alpha/numeric Transmitter Control Code assigned by IRS. See Part A, Sec. 15 for a definition of Transmitter Control Code (TCC). You must have a TCC to file *actual* data on this program.
40	Blank	1	REQUIRED. Enter blank.
41–80	First Payer Name	40	REQUIRED. Must be present or files will be returned for correction. Enter the name of the payer in the manner in which it is used in normal business. Any extraneous information must be deleted from the name line. Left-justify and fill with blanks. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
81–119	Second Payer Name	39	REQUIRED. The contents of this field are dependent upon the TRANSFER AGENT INDICATOR in position 120 of this record. If the Transfer Agent Indicator contains a "1", this field will contain the name of the Transfer Agent. If the Tranfer Agent Indicator contains a "0" (zero), this field will contain either a continuation of the First Payer Name field or blanks. Left-justify and fill unused positions with blanks. IF NO ENTRIES ARE PRESENT FOR THIS FIELD, FILL WITH BLANKS. (See Part A, Sec. 15 for a definition of Transfer Agent.)
120	Transfer Agent Indicator	1	REQUIRED. Identifies the entity in the Second Payer Name field. (See Part A, Sec. 15 for a definition of Transfer Agent.)

Code	*Meaning*
1	The entity in the Second Payer Name field is the Transfer Agent.
0 (zero)	The entity shown is *not* the Transfer Agent (*i.e.*, the Second Payer Name field contains either a continuation of the First Payer Name field or blanks).

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Cassette Position	Field Title	Length	Description and Remarks
121–160	Payer Shipping Address	40	REQUIRED. If the TRANSFER AGENT INDICATOR in p sition 120 is a "1", enter the shipping address of the Transfer Agen Otherwise, enter the shipping address of the payer. Left-justify a fill with blanks.
161–200	Payer City, State and ZIP Code	40	REQUIRED. If the TRANSFER AGENT INDICATOR in p sition 120 is a "1", enter the City, State, and ZIP Code of t Transfer Agent. Otherwise, enter the City, State, and ZIP Code the payer. Left-justify and fill with blanks.
201–256	Blank	56	REQUIRED. Enter blanks.

SEC. 4. PAYEE "B" RECORD—GENERAL FIELD DESCRIPTIONS

.01 The Payee "B" Record contains the payment information from the individual statements. When filing information documents on cassette(s), the format for the Payee "B" Records will vary in relation to the number of payment amount fields being reported. The number of payment amount fields will depend upon the number of Payment Amount Indicator Codes used in positions 18–23 of the Payer/Transmitter "A" Record. For example, if you are reporting 1099–INT, position 17 of the Payer/Transmitter "A" Record will be coded with a "6". If the Amount Indicators used to report this interest are Amount Codes "1", "2", and "3", then cassette positions 18–23 of the "A" Record will be coded "123bbb" (b represents a *blank* position). To correspond with Amount Indicators "1", "2", and "3" of the "A" Record, the "B" Record will contain three payment amount fields. Cassette positions 31–40 of the "B" Record will contain the payment amount to be reported for Amount Code "1" (Earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposits, etc.); cassette positions 41–50 of the "B" Record will contain the payment amount to be reported for Amount Code "2" (Amount of forfeiture); and cassette positions 51–60 of the "B" Record will contain the payment amount to be reported for Amount Code "3" (Federal income tax withheld). The First Payee Name Line *must* begin immediately after the last payment amount *that is indicated as being used*. In this example, the First Payee Name Line would begin in cassette position 61.

.02 All records must be a fixed length. Records may not span blocks. A block may not exceed 256 positions. DO NOT PAD A BLOCK WITH BLANKS. If the use of blocked records would result in a short block, all remaining positions of the block must be filled with 9s.

.03 All payee records *must contain correct payee name and address information* entered in the fields prescribed in this section. Records containing an invalid TIN (SSN or EIN) and having no address data present may be returned for correction. In searching for a payee address, if your efforts fail and you know that the address is invalid, supply the invalid address rather than leave the field blank.

.04 IRS must be able to identify the surname associated with the TIN (SSN or EIN) furnished on a statement. The specifications below include a field in the payee records called "Name Control" in which the first four alphabetic characters of the payee's surname or last name are to be entered by the payer. The surname or last name should appear first in the First Payee Name Line of all Payee "B" Records; however, if your records have been developed using the first name first, IRS programs will accept this but a blank must appear between the first and last name.

.05 If payers are unable to provide the first four characters of the surname, the Name Control Field may be left blank; however, compliance with the following will facilitate IRS computer programs in generating the Name Control.

(a) The surname of the payee whose TIN (SSN or EIN) is shown in the Payee "B" Record should always appear firs If, however, you enter the first name firs you must leave a blank space between th first and last name.

(b) In the case of multiple payees, on the surname of the payee whose TIN (SS or EIN) is shown in the Payee "B" Re ord must be present in the First Paye Name Line. Surnames of any other pa ees in the record must be entered in th Second Payee Name Line.

.06 All alpha characters entered in th "B" Record should be uppercase.

.07 *IRS STRONGLY ENCOURAGE FILERS TO REVIEW THEIR DAT FOR ACCURACY BEFORE SUBMI SION TO PREVENT ERRONEOU NOTICES BEING MAILED TO PE SONS FOR WHOM REPORTS AR FILED. FILERS SHOULD BE ESP CIALLY CAREFUL THAT THE TAXPAYER NAMES, SOCIAL S CURITY NUMBERS (SSNs), A COUNT NUMBERS, TYPES O INCOME, AND INCOME AMOUN ARE CORRECT. ALTHOUGH IR ENCOURAGES PAYERS TO FILL I THE PAYER'S ACCOUNT NUMBE FOR THE PAYEE FIELD, THE SHOULD NOT INCLUDE EXTRA NEOUS DIGITS AS THIS FIELD I LIMITED, IN MAGNETIC MEDI FILING, TO 10 POSITIONS.*

.08 *WHEN REPORTING FORM 109 "MORTGAGE INTEREST STAT MENT," THE "A" RECORD WIL REFLECT THE NAME OF THE R CIPIENT OF THE INTEREST. THE "B RECORD WILL REFLECT THE I DIVIDUAL PAYING THE INTERES AND THE AMOUNT PAID.*

RECORD NAME: PAYEE "B" RECORD

assette osition	Field Title	Length	Description and Remarks
	Record Type	1	REQUIRED. Enter "B".
-3	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported (*e.g.*, if payments were made in 1986, enter "86"). Must be incremented each year.
-5	Document Specific Code	2	REQUIRED for Forms 1099-R, 1099-MISC, and 1099-G. For *Form 1099-R*, enter the appropriate code for the Category of Total Distribution. For *Form 1099-MISC*, enter the appropriate code for Direct Sales. For *Form 1099-G*, enter the year of income tax refund. FOR ALL OTHER FORMS, ENTER BLANK. If only one code is used, left-justify and blank fill. (In prior years, cassette position 5 was used as a corrected return indicator. This position was needed for the Document Specific Code. Cassette position 6 now represents a corrected return. You must adjust your programs.)
	Category of Total Distribution (Form 1099-R only)		Use only for reporting on *Form 1099-R* to identify the Category of Total Distribution. You may select two codes except when using Code 9. Enter the applicable code from the table below. Code 7 below is *not required* for Amount Indicators 1, 2, and 3. A "0" (zero) is not a valid code for Form 1099-R. If you are reporting a distribution from a KEOGH plan, or from any other distribution, to which the following codes do not apply, enter blanks in this field.

Category	*Code*
Premature distribution (other than codes 2, 3, 4, 5, 8, or P)	1
Rollover	2
Disability	3
Death (includes payments to a beneficiary)	4
Prohibited transaction	5
Other	6
Normal IRA, SEP or DEC distributions	7
Excess contributions refunded plus earnings on such excess contributions	8
PS 58 Costs (see NOTE)	9
Excess contributions refunded plus earnings on such excess contributions taxable in 1985	P
Qualifies for 10-year averaging	A
Qualifies for death benefit exclusion	B
Qualifies for both A and B	C

NOTE: PS 58 Costs may be reported on Form 1099-R; however, Form W-2P (filed with SSA) is preferable. Since this is not actually a total distribution, a separate "B" Record is required to report PS 58 Costs. These costs may not be reported in combination with a total distribution. Refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W-2G," available from IRS offices.

	Field Title		Description and Remarks
	Direct Sales (Form 1099-MISC only)		Use only for direct sales reporting on *Form 1099-MISC*. If sales to the recipient of consumer products on a buy-sell, deposit-commission, or any other basis for resale, have amounted to $5,000 or more, ENTER "1". If you are filing 1099-MISC, with an Amount Indicator of "8" in the "A" Record, you must enter a code "1" in this field. For all other 1099-MISC Amount Codes in the "A" Record, enter a "0" (zero) in this field. (In Part B, Sec. 3, information concerning the direct sales indicator can be found under Amount Indicators, Form 1099-MISC, NOTE 1 in the "A" Record.) This code should appear in position "4." Position "5" will be blank.

RECORD NAME: PAYEE "B" RECORD—Continued

<table>
<tr><th>Cassette Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td></td><td>Refund is for Tax Year (Form 1099–G only)</td><td></td><td>Use only for reporting the tax year for which the refund was issued If the payment amount field associated with Amount Indicator 2 Income Tax Refunds, contains a refund, credit or offset that i attributable to an income tax that applies exclusively to income fro a trade or business and is not of general application, then enter th ALPHA equivalent of the year of refund from the table belo Otherwise, enter the NUMERIC Year for which the refund w issued. This code should appear in position 4. Position 5 will b blank.
<table>
<tr><th><i>Year for which Refund was Issued</i></th><th><i>Alpha Equivalen</i></th></tr>
<tr><td>1</td><td>A</td></tr>
<tr><td>2</td><td>B</td></tr>
<tr><td>3</td><td>C</td></tr>
<tr><td>4</td><td>D</td></tr>
<tr><td>5</td><td>E</td></tr>
<tr><td>6</td><td>F</td></tr>
<tr><td>7</td><td>G</td></tr>
<tr><td>8</td><td>H</td></tr>
<tr><td>9</td><td>I</td></tr>
<tr><td>0</td><td>J</td></tr>
</table></td></tr>
<tr><td>6</td><td>Blank or Corrected Return Indicator</td><td>1</td><td>REQUIRED. Enter blank. (Reserved for IRS use). Cassette po sition 6 is used to indicate a corrected return. Refer to Part A, Sec 10 for specific instructions on how to file corrected returns usin magnetic media. IN PRIOR YEARS, CASSETTE POSITION WAS USED AS THE CORRECTED RETURN INDICATOR THIS HAS NOW CHANGED TO POSITION 6. <i>YOU MUS ADJUST YOUR PROGRAMS.</i></td></tr>
<tr><td>7–10</td><td>Name Control</td><td>4</td><td>REQUIRED. Enter the first 4 letters of the surname of the paye Surnames of less than four (4) letters should be left-justified, fillin the unused positions with blanks. Special characters and imbedde blanks should be removed. IF THE NAME CONTROL IS NO DETERMINABLE BY THE PAYER, SUCH AS IN THE CAS OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A das (-) or ampersand (&) are the only acceptable special character The following examples may be helpful to you in developing th Name Control:
<table>
<tr><th><i>Name</i></th><th><i>Name Contro</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE*</td></tr>
<tr><td>James P. En Sr.</td><td>EN*</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must b left-justified and blank filled.</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued

Cassette Position	Field Title	Length	Description and Remarks
11	Type of TIN	1	REQUIRED. This field is used to identify the Taxpayer Identification Number (TIN) in positions 12–20 as either an Employer Identification Number, a Social Security Number, or the reason no number is shown. Enter the appropriate code from the following table: *Type of TIN* — *TIN* — *Type of Account* 1 — EIN — A business or an organization 2 — SSN — An individual blank — N/A — If the type of TIN is undeterminable, enter a blank. If a number is unobtainable due to legitimate cause; *e.g.*, number applied for but not received, enter a blank.
12–20	Taxpayer Identification Number	9	REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the payee (SSN or EIN, as appropriate). Where an identification number has been applied for but not received or where there is any other legitimate cause for not having an identification number, *enter blanks*. Refer to Part A, Sec. 11. *DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS.* Any record containing an invalid identification number in this field will be returned for correction.
21–30	Payer's Account Number for Payee	10	REQUIRED. Payer may use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payer's file should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. An account number can be any account number assigned by the payer to the payee (*i.e.*, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any number that will help identify the particular transaction that you are reporting. If a number is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.
	Payment Amount Fields (Must be Numeric)		The number of payment amounts is dependent upon and must agree with the number of Amount Indicators present in positions 18–23 of the "A" Record. For cassette filers, a maximum of six payment amounts may be present. *THE FIRST PAYEE NAME LINE MUST APPEAR IMMEDIATELY AFTER THE LAST PAYMENT AMOUNT INDICATED AS BEING USED.* For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one ten position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 41. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE 1). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS*. Example: If the Amount Indicators are reflected as "123bbb", the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367b", the "B" Records must have only 5 payment amount

RECORD NAME: PAYEE "B" RECORD—Continued

Cassette Position	Field Title	Length	Description and Remarks
			three payment amount fields. Payment amounts MUST be rig justified and unused positions MUST be zero filled. Federal incor tax withheld is not reported as a negative amount. NOTE 1: If any one payment amount exceeds "9999999999" (dolla and cents), as many SEPARATE Payee "B" Records as necessa to contain the total amount MUST be submitted for the Payee. NOTE 2: If you file 1099–MISC and use Amount Code "8" in t Amount Indicator field of the Payer/Transmitter "A" Record, yo must enter 0000000100 in the corresponding Payment Amount Fiel This will not represent an actual money amount; this is an indicat of direct sales. (Refer to Part B, Sec. 3, NOTE 1, of the Amou Indicators, Form 1099–MISC, for clarification.)
31–40	Payment Amount 1	10	This amount is identified by the indicator in position 18 of the Paye Transmitter "A" Record. *This amount must always be present.*

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "I RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POS TIONS 18–23 OF THE PAYER/TRANSMITTER "A" RECORD.

Cassette Position	Field Title	Length	Description and Remarks
41–50	Payment Amount 2	10	This amount is identified by the indicator in position 19 of the Paye Transmitter "A" Record. If position 19 is blank, do not provid for this payment amount.
51–60	Payment Amount 3	10	This amount is identified by the indicator in position 20 of the Paye Transmitter "A" Record. If position 20 is blank, do not provid for this payment amount.
61–70	Payment Amount 4	10	This amount is identified by the indicator in position 21 of the Paye Transmitter "A" Record. If position 21 is blank, do not provid for this payment amount.
71–80	Payment Amount 5	10	This amount is identified by the indicator in position in position 2 of the Payer/Transmitter "A" Record. If position 22 is blank, d not provide for this payment amount.
81–90	Payment Amount 6	10	This amount is identified by the indicator in position 23 of the Paye Transmitter "A" Record. If position 23 is blank, do not provid for this payment amount.

THE NEXT 160 POSITIONS MUST BEGIN IMMEDIATELY AFTER THE LAST PAYMENT AMOUNT FIELD IND CATED AS BEING USED. THE NUMBER OF PAYMENT AMOUNT FIELDS IS DETERMINED BY THE NUMBE OF AMOUNT INDICATORS IN POSITIONS 18–23 OF THE PAYER/TRANSMITTER "A" RECORD. (See Part B, Se 4.01 for an example.)

Cassette Position	Field Title	Length	Description and Remarks
	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediat after the last payment amount indicated as being used. Do not ent address information in this field.* If you use all payment amount the First Payee Name Line will begin in cassette position 91. Ent the name of the payee (preferably surname first) whose Taxpay Identification Number appears in positions 12–20 above. If few than 40 characters are required, left-justify and fill unused positio with blanks. If more space is required *for the name*, utilize t Second Payee Name Line field below. If there are multiple payee *only the name* of the payee whose Taxpayer Identification Numb has been provided should be entered in this field. The names of t other payees should be entered in the Second Payee Name Li field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAG INTEREST STATEMENT," THE "A" RECORD WILL R FLECT THE NAME OF THE RECIPIENT OF THE INTERES THE "B" RECORD WILL REFLECT THE INDIVIDUAL PA ING THE INTEREST AND THE AMOUNT PAID.*

RECORD NAME: PAYEE "B" RECORD—Continued

Cassette Position	Field Title	Length	Description and Remarks
	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in ths field*. If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number provided in positions 12–20 above. *Do not enter address information in this field*. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field*. (If the payee lives outside of the United States, insert a "1" in position "1" of this field and spell out the name of the city in the remaining positions.
	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "1" of the Payee City field.
	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "1" in the Payee City field is a "1".

THE FOLLOWING FIELD POSITIONS DESCRIBE PAYEE "B" RECORD POSITIONS FOLLOWING PAYEE ZIP CODE FORMS 1098, 1099-DIV, 1099-G, 1099-INT, 1099-MISC, 1099-OID, 1099-PATR, 1099-R AND 5498. FORMS 1099-A, 1099-B AND W-2G CANNOT BE FILED ON CASSETTE.

Cassette Position	Field Title	Length	Description and Remarks
250	Special Data Entries		REQUIRED. This portion of the Payee "B" Record may be used to record information for the payer. The Special Data Entries will begin in positions 201, 211, 221, 231, or 241 depending on the number of payment amounts used in the record. Special Data Entries may be used to make all records the same length; however, the "B" Record may not exceed 256 positions. If this field is not utilized, ENTER BLANKS.
251–256	Blank	6	REQUIRED. Enter blanks.

SEC. 5. END OF PAYER "C" RECORD

.01 The Control Total fields have been expanded from 12 to 15 positions. Adjust your programs accordingly.

.02 The End of Payer "C" Record is a summary record for a type of return for a given payer. It *MUST* be the same length as the "B" Records in the payer's file.

.03 The "C" Record will contain the total number of payees and the totals of the payment amount fields filed by a given payer. The "C" Record must be written after the last Payee "B" Record for each type of return for a given payer. For each "A" Record and group of "B" Records on the file, there must be a corresponding "C" Record.

.04 In developing the "C" Record, for example, if you used Amount Codes 1, 3, and 6 in the "A" Record, the totals from the "B" Records will appear in Control Totals 1, 2, and 3 of the "C" Record. Positions 53–142 would be zero filled and positions 143–256 would be blank filled *in this example*.

.05 Payers/Transmitters must verify the accuracy of the totals in the "C" Record and must enter the totals on the transmittal Form 4804, 4802 or computer generated substitute, which will accompany the shipment. The lines used on Forms 4804 and 4802 to record payment amounts correspond with the Amount Codes used in the "A" Record. These forms have been updated for 1986.

RECORD NAME: END OF PAYER "C" RECORD

Cassette Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "C".
2–7	Number of Payees	6	REQUIRED. Enter the total number of Payee "B" Records co ered by the preceding Payer/Transmitter "A" Record. Right-justi and zero fill.
8–22	Control Total 1	15	REQUIRED. Please note that all Control Total fields have be expanded from 12 to 15 positions. Enter accumulated totals fro Payment Amount 1. Right-justify and zero fill each Control Tot amount. IF LESS THAN NINE AMOUNT FIELDS ARE BEIN REPORTED, ZERO FILL UNUSED CONTROL TOTA FIELDS.
	If any corresponding Payment Amount fields are present in the Payee "B" Records, accumulate into th appropriate Control Total field. ZERO FILL UNUSED CONTROL TOTAL FIELDS. Please note that a Control Total fields have been expanded from 12 to 15 positions.		
23–37	Control Total 2	15	
38–52	Control Total 3	15	
53–67	Control Total 4	15	
68–82	Control Total 5	15	
83–97	Control Total 6	15	
98–256	Blank	159	REQUIRED. Enter blanks. (Enter the appropriate number of blanl in order to make the "C" Record length equal to the "B" Recor length.)

SEC. 6. END OF TRANSMISSION "F" RECORD

.01 The "F" Record is a summary of the number of payers and cassettes in the entire file.

.02 This record should be written after the last "C" Record of the entire file.

.03 Only a Tape Mark or a Tape Mark and Trailer Label may follow the "F Record (except when fixed blocks are use in this instance, 9s may follow the "F Record).

RECORD NAME: END OF TRANSMISSION "F" RECORD

Cassette Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "F".
2–5	Number of "A" Records	4	REQUIRED. You may enter the total number of Payer/Transmitt "A" Records in this transmission. Right-justify and zero fill or ent all zeros.
6–8	Number of Cassettes	3	REQUIRED. You may enter the total number of cassettes in th transmission. Right-justify and zero fill or enter all zeros.
9–30	Zero	22	REQUIRED. Enter zeros.
31–256	Blank	226	REQUIRED. Enter blanks.

PART C. BURROUGHS SUPER MINI-DISK SPECIFICATIONS

SECTION 1. GENERAL

.01 The specifications contained in this part of the revenue procedure prescribe the required format and contents of the records to be included in the Burroughs Super Mini-Disk (BSMD) file. These specifications must be adhered to unless deviations have been specifically granted by IRS in writing.

.02 IRS has a Burroughs B–94 mini-computer with 2 mini-disk drives: a Burroughs Super Mini-Disk, style B 9489–1 and a Burroughs Super Mini-Disk II, sty B 9489–21.

.03 It is our understanding that mo Burroughs B–90 series mini-computers w produce a mini-disk that will be compa ible with our system.

.04 To be compatible, a mini-disk must neet the following specifications in total:

(a) The Burroughs Super Mini-disk is flexible mylar disk with an iron oxide oating. The disk is 8 inches (20.3 cm) in liameter with a 1.5 inch (3.8 cm) center iole.

(b) There are 32 Sector Markers (holes) n the disk at a distance of 1.5 inches (3.8 m) from the center. These markers deine the 32 sectors in which data can be ecorded on each track of the disk.

(c) Recorded data is encoded using the Miller Frequency Mode (MFM) technique. Data transferred between the disk and the processor is encoded using the non return to zero (NRZ) technique.

(d) Bit serial data is written to the disk n the Burroughs standard 180 bytes per ector format.

(e) Number of usable sides is 2.

(f) Tracks per side is 88.

(g) Sectors per track is 32.

(h) Maximum recording density is 4774 bits per inch.

(i) When initializing the mini-disk, the name IRSTAX should be assigned to the mini-disk.

(j) The file name in the super mini-disk header label should be FED-MINI.

.05 Payers who can substantially conform to these specifications, but who require some minor deviations, MUST contact the National Computer Center. Under no circumstances may mini-disks deviating from the specifications in this revenue procedure be submitted without prior approval from IRS. If you file under the Combined Federal/State Program, your files must conform totally to this revenue procedure.

.06 An external label must appear on each mini-disk submitted for processing. The following information is needed:

(a) The transmitter's name.

(b) The five character alpha/numeric Transmitter Control Code.

(c) State of sender (*e.g.*, NY).

(d) Checkbox (for tape filers only).

(e) Tape density (for tape filers only).

(f) Track (for tape filers only).

(g) Recording Code (ASCII for mini-disk filers).

(h) The tax year of the data (*e.g.*, 1986).

(i) Document types (*e.g.*, 1099–INT).

(j) The total number of "B" Records after each "A" Record (this figure is taken from the "C" Record).

(k) A number assigned by the transmitter to each mini-disk.

(l) The sequence of each mini-disk (*e.g.*, 001 of 008).

The external media label, Form 5064, was updated for tax year 1986. You must use the updated label. This information will assist IRS in processing the file or in locating a file, should the transmitter request that it be returned due to errors. IRS advises that special shipping containers not be used for transmitting data since it cannot be guaranteed that they will be returned.

SEC. 2. PAYER/TRANSMITTER "A" RECORD

.01 Identifies the payer and transmitter of the mini-disk and provides parameters for the succeeding Payee "B" Records. IRS computer programs rely on the absolute relationship between the parameters and data fields in the "A" Record and the data fields in the "B" Records to which they apply.

.02 The number of "A" Records appearing on a mini-disk will depend on the number of payers and the different types of returns being reported. After the header label on the mini-disk, the first record appearing in the file must be an "A" Record. For mini-disk filing, the *actual* record lengths for the "A" and "B" Records must agree with whatever is entered in mini-disk positions 29–31 and 32–34 of the "A" Record. A transmitter may include Payee "B" Records for more than one payer on a mini-disk; however, each GROUP of Payee "B" Records must be preceded by an "A" Record. A single mini-disk may also contain different types of returns, but the types of returns *must* not be intermingled. A separate "A" Record is required for each type of return being reported. The initial record on a *file* must be an "A" Record.

.03 All alpha characters entered in the "A" Record should be uppercase.

.04 *WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST, THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*

RECORD NAME: PAYER/TRANSMITTER "A" RECORD

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". It is used to sequence the sectors making up a Service Record.
2	Record Type	1	REQUIRED. Enter "A". Must be the second position of each PAYER/TRANSMITTER Record.
3	Payment Year	1	REQUIRED. Must be the right most digit of the year for which information is being reported (*e.g.*, if payments were made in 1986, enter "6"). Must be incremented each year.
4–6	Mini-Disk Sequence Number	3	REQUIRED. Sequence number assigned by the Transmitter to each mini-disk starting with 001.
7–15	Payer's Federal EIN	9	REQUIRED. Must be the *valid* 9-digit number assigned to the payer by IRS. DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS. (Also see Part A, Sec. 11.07.)
16	Blank	1	REQUIRED. Enter blank.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
17	Combined Federal/State Filer	1	**REQUIRED. Enter the appropriate code from the table belo *Prior approval* is required. A Consent Form 6847 *must* be submitt to IRS before tax information will be released to the states. Ref to Part A, Sec. 14.11 for money criteria. Not all states particip in this program. If the Payer/Transmitter is not participating in t Combined Federal/State Filing Program, enter blanks. (Refer Part A, Sec. 14 for the requirements that *must* be met *prior* to actu participation in this program.) Forms 1098, 1099–A, 1099–B, a W-2G cannot be filed on this program. Filers who participate this program must incorporate state totals into corresponding "I Records as described in Part C, Sec. 15.** *Code* *Meaning* 1 **Participating in the Combined Federal/State Fili Program.** Blank **Not participating.**
18	Type of Return	1	**REQUIRED. Enter appropriate code from table below:** *Type of Return* — *Code* 1098 — 3 1099–A — 4 1099–B — B 1099–DIV — 1 1099–G — F 1099–INT — 6 1099–MISC — A 1099–OID — D 1099–PATR — 7 1099–R — 9 5498 — L W-2G — W
19-27	Amount Indicators	9	**REQUIRED. *In most cases, the boxes or Amount Indicators paper information returns correspond with the Amount Codes us to file on magnetic media; however, should you notice discrepanci between this revenue procedure and paper forms, please disrega them and program according to this revenue procedure for yo returns filed on magnetic media.* For specific instructions on info mation to be reported in each Amount Code, refer to the 19 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G." T amount indicators entered for a given type of return indicate type(of payment(s) which were made. For each Amount Code enter in this field, a corresponding payment amount must appear in t Payee "B" Record. Example: If position 18 of the Payer/Transmitt "A" Record is "6" (for 1099–INT) and positions 19–27 a "123bbbbbb", this indicates that 3 payment amount fields are pre ent in all of the following Payee "B" Records. The first payme amount field in the Payee "B" Record will represent Earnings fro savings and loan associations, credit unions, bank deposits, bea certificates of deposit, etc., the second will represent Amount forfeiture, and the third will represent Federal income tax withhel Enter the Amount Indicators in ASCENDING SEQUENCE (*i.e.* 1247bbbbb), left-justify, filling unused positions with blanks. F any further clarification of the Amount Indicator codes, you m contact the IRS National Computer Center.**

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks

SECTOR 1 (Continued)

Amount Indicators Form 1098 Mortgage Interest Statement (See NOTE)

For Reporting Mortgage Interest Received from Payer(s) on Form 1098:

Amount Code	Amount Type
1	Mortgage interest received from payer(s)
2	Optional field for items such as real estate taxes or insurance paid from escrow

NOTE: THE PERSON FOR WHOM YOU ARE RECEIVING THE INTEREST NEED NOT FILE FORM 1098, AND NO ADDITIONAL REPORTING IS REQUIRED FOR THE TRANSFER OF THE INTEREST FROM THE SERVICING BANK TO THE LENDER.

Amount Indicators Form 1099–A Acquisition or Abandonment of Secured Property

For Reporting the Acquisition or Abandonment of Secured Property on Form 1099–A:

Amount Code	Amount Type
2	Amount of debt outstanding
3	Amount of debt satisfied
4	Fair market value of property at acquisition or abandonment

Amount Indicators Form 1099–B Proceeds From Broker and Barter Exchange Transactions

For Reporting Payments on Form 1099–B:

Amount Code	Amount Type
2	Stocks, bonds, etc. (For Forward Contracts see NOTE below.)
3	Bartering
4	Federal income tax withheld
6	Profit (or loss) realized in 1986
7	Unrealized profit (or loss) on open contracts—12/31/85
8	Unrealized profit (or loss) on open contracts—12/31/86
9	Aggregate profit (or loss)

NOTE: The Payment Amount field associated with Amount Code 2 may be used to represent a loss when the reporting is for Forward Contracts. Refer to Payee "B" Record-General Field Descriptions, Payment Amount Fields, for instructions in reporting negative amounts.

Amount Indicators Form 1099–DIV–Dividends and Distributions

For Reporting Payments on Form 1099–DIV:

Amount Code	Amount Type
1	Gross dividends and other distributions on stock
2	Dividends qualifying for exclusion
3	Dividends not qualifying for exclusion
4	Federal income tax withheld
5	Capital gain distributions
6	Nontaxable distributions (if determinable)
7	Foreign tax paid
8	Cash liquidation distributions
9	Noncash liquidation distributions (Show fair market value)

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
	Amount Indicators Form 1099–G–Certain Government Payments		For Reporting Payments on Form 1099–G:

Amount Code	Amount Type
1	Unemployment compensation
2	State or local income tax refunds
4	Federal income tax withheld
5	Discharge of indebtedness
6	Taxable grants
7	Agriculture payments

Mini-Disk Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–INT–Interest Income		For Reporting Payments on Form 1099–INT:

Amount Code	Amount Type
1	Earnings from savings and loan associations, credit unions, bank deposits, bearer certificates of deposit, etc.
2	Amount of forfeiture
3	Federal income tax withheld
4	Foreign tax paid (if eligible for foreign tax credit)
5	U.S. Savings Bonds, etc.

Mini-Disk Position	Field Title	Length	Description and Remarks
	Amount Indicators Form 1099–MISC–Miscellaneous Income (See Notes 1, 2 and 3)		For Reporting Payments on Form 1099–MISC:

Amount Code	Amount Type
1	Rents
2	Royalties
3	Prizes and awards
4	Federal income tax withheld
5	Fishing boat proceeds
6	Medical and health care payments
7	Nonemployee compensation
8	Direct sales *"indicator"* (see NOTE 1)
9	Substitute payments in lieu of dividends or interest (see NOTE 2)

NOTE 1: Use Amount Code "8" to report that *direct sales* of consumer products of $5,000 or more to th payee on a buy-sell, deposit-commission, or other basis *for resale* where made. Do not use this indicator fo sales of less than $5,000. The use of Amount Code "8" actually reflects an *indicator* of *direct sales* and not a actual payment amount or amount code. The corresponding payment amount field in the Payee "B" Record MUST be reflected as 0000000100. This does not mean that a payment of $1.00 was made or is being reported. The use of Amount Code "8" relates directly to mini-disk position 5, Document Specific Code and NOTE of the Payment Amount Field in Sector 1 of the Payee "B" Record. (If you use Amount Code "8" in the "A" Record, you will enter a "1" in mini-disk position "5" of Sector 1 of the "B" Record. For any other 1099–MISC Amount Codes, you will enter a "0" (zero) in mini-disk position "5" of Sector 1 of the "B" Record.)

NOTE 2: Brokers are subject to a reporting requirement for payments received after 1984. Brokers who transfer securities of a customer for use in a short sale must use Amount Code 9 to report the aggregate payments received in lieu of dividends or tax-exempt interest on behalf of a customer while the short sale was open. Generally, for substitute payments in lieu of dividends, a broker is required to file a Form 1099–MISC for each affected customer who is *not* an individual. Refer to the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G" for detailed information. The instructions are available from IRS offices.

NOTE 3: If you are reporting Excess Golden Parachute Payments, use paper forms 1099–MISC. Do not report these payments on magnetic media. See Part A, Sec. 15 for the definition of an Excess Golden Parachute Payment.

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 1 (Continued)			
	Amount Indicators Form 1099–OID– Original Issue Discount	For Reporting	Payments on Form 1099–OID:
		Amount Code	Amount Type
		1	Total original issue discount for 1986
		2	Other periodic interest (the regular interest paid on this obligation without regard to any original issue discount)
		3	Amount of forfeiture
		4	Federal income tax withheld
	Amount Indicators Form 1099–PATR– Taxable Distributions Received From Cooperatives	For Reporting	Payments on Form 1099–PATR:
		Amount Code	Amount Type
		1	Patronage dividends
		2	Nonpatronage distributions
		3	Per-unit retain allocations
		4	Federal income tax withheld
		5	Redemption of nonqualified notices and retain allocations
		6	Investment credit (See NOTE)
		7	Energy investment credit (See NOTE)
		8	Jobs credit (See NOTE)

NOTE: The amounts shown for Amount Indicators "6," "7" and "8" must be reported to the payee; however, since these amounts are not taxable, they need not be reported to IRS.

	Amount Indicators Form 1099–R– Total Distributions From Profit-Sharing, Retirement Plans, Individual Retirement Arrangements, Insurance Contracts, Etc. (See NOTE)	For Reporting	Payments on Form 1099–R:
		Amount Code	Amount Type
		1	Amount includable as income (add amounts in codes 2 and 3)
		2	Capital gain (for lump-sum distributions only)
		3	Ordinary income
		4	Federal income tax withheld
		5	Employee contributions (profit-sharing or retirement plans) or insurance premiums
		6	IRA, SEP, or DEC distributions
		7	State income tax withheld
		8	Net unrealized appreciation in employer's securities
		9	Other

NOTE: A distribution from a KEOGH plan should be reported in Amount Codes 1, 2, and 3 as appropriate.

	Amount Indicators Form 5498– Individual Retirement Arrangement Information	For Reporting	Payments on Form 5498:
		Amount Code	Amount Type
		1	Regular SEP contributions made in 1986 and 1987 for 1986. Include only employer contributions here. Enter any employee contributions to a SEP in Code 3.
		2	Rollover IRA, SEP or DEC contributions
		3	Regular IRA or DEC contributions made in 1986 and 1987 for 1986
		4	Life insurance cost included in code 1 or 3 (for endownment contracts only)

NOTE: Form 5498 is filed for contributions to be applied to 1986 that are made between January 1, 1986, and April 15, 1987.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
	Amount Indicators Form W–2G– Certain Gambling Winnings		For Reporting Payments on Form W–2G: Amount Code — Amount Type 1 — Gross winnings 2 — Federal income tax withheld 3 — State income tax withheld 7 — Winnings from identical wagers
28	Blank	1	REQUIRED. Enter blank.
29–31	"A" Record Length	3	REQUIRED. This indicates the Record Length, *NOT* the Secto Length. Enter 360.
32–34	"B" Record Length	3	REQUIRED. This indicates the Record Length, *NOT* the Secto Length. Enter 360.
35	Blank	1	REQUIRED. Enter blank.
36–40	Transmitter Control Code (TCC)	5	REQUIRED. Enter the five character alpha/numeric Transmitte Control Code assigned by IRS. See Part A, Sec. 15 for a definitio of Transmitter Control Code (TCC). You must have a TCC to fi *actual* data on this program.
41	Blank	1	REQUIRED. Enter blank.
42–81	First Payer Name	40	REQUIRED. Must be present or files will be returned for correc tion. Enter the name of the payer in the manner in which it is use in normal business. Any extraneous information must be delete from the name line. Left-justify and fill with blanks. *NOTE: WHE REPORTING FORM 1098, "MORTGAGE INTEREST STATE MENT," THE "A" RECORD WILL REFLECT THE NAME O THE RECIPIENT OF THE INTEREST. THE "B" RECORL WILL REFLECT THE INDIVIDUAL PAYING THE INTERES AND THE AMOUNT PAID.*
82–120	Second Payer Name	39	REQUIRED. The contents of this field are dependent upon th TRANSFER AGENT INDICATOR in position 121 of this record If the Transfer Agent Indicator contains a "1," this field will contai the name of the Transfer Agent. If the Transfer Agent Indicato contains a "0" (zero), this field will contain either a continuatio of the First Payer Name field or blanks. Left-justify and fill unuse positions with blanks. IF NO ENTRIES ARE PRESENT FO THIS FIELD, FILL WITH BLANKS. (See Part A, Sec. 15 for definition of Transfer Agent.)
121	Transfer Agent Indicator	1	REQUIRED. Identifies the entity in the Second Payer Name field (See Part A, Sec. 15 for a definition of Transfer Agent.) *Code* — *Meaning* 1 — The entity of the Second Payer Name field is th Transfer Agent. 0 (zero) — The entity shown is *not* the Transfer Agent (*i.e.*, th Second Payer Name field contains either a continua tion of the First Payer Name field or blanks).
122–180	Blank	59	REQUIRED. Enter blanks.

RECORD NAME: PAYER/TRANSMITTER "A" RECORD—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2			
	Record Sequence	1	REQUIRED. Must be a "2". Use to sequence the sectors making up a Service Record.
2	Record Type	1	REQUIRED. Enter "A". Must be the second position of each PAYER/TRANSMITTER Record.
–42	Payer Shipping Address	40	REQUIRED. If the TRANSFER AGENT INDICATOR in position 121 of Sector 1 is a "1", enter the shipping address of the Transfer Agent. Otherwise, enter the shipping address of the payer. Left-justify and fill with blanks.
43–82	Payer City, State and ZIP Code	40	REQUIRED. If the TRANSFER AGENT INDICATOR in position 121 of Sector 1 is a "1", enter the city, state and ZIP Code of the Transfer Agent. Otherwise, enter the city, state and ZIP Code of the payer. Left-justify and fill with blanks.
83–180	Blank	98	REQUIRED. Enter blanks.

ADDITIONALLY, IF THE PAYER AND THE TRANSMITTER ARE THE SAME, THE "A" RECORD MAY BE TERMINATED WITH SECTOR 2 AS DESCRIBED ABOVE. HOWEVER, IF THE PAYER AND THE TRANSMITTER ARE NOT THE SAME OR THE TRANSMITTER INCLUDES FILES FOR MORE THAN ONE PAYER OR THIS IS A COMBINED FEDERAL/STATE FILING PAYER, THE FOLLOWING ITEMS ARE REQUIRED.

Mini-Disk Position	Field Title	Length	Description and Remarks
83–122	First Name Line of Transmitter	40	REQUIRED. Enter the name of the transmitter in the manner in which it is used in normal business. The name of the transmitter *must* be constant through the entire file. Left-justify and fill with blanks.
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service Record.
2	Record Type	1	REQUIRED. Enter "A". Must be the second position of each PAYER/TRANSMITTER Record.
3–42	Second Name Line of Transmitter	40	REQUIRED. Enter the second name line of the transmitter. Left-justify and fill with blanks. IF NO ENTRIES ARE PRESENT FOR THIS FIELD, FILL WITH BLANKS.
43–82	Transmitter Mailing Address	40	REQUIRED. Enter the mailing address of the transmitter. Left-justify and fill with blanks.
83–122	Transmitter City, State and ZIP Code	40	REQUIRED. Enter the City, State, and ZIP Code of the transmitter. Left-justify and fill with blanks.
123–180	Blank	58	REQUIRED. Enter blanks.

SEC. 3. PAYER/TRANSMITTER "A" RECORD—RECORD LAYOUT

PAYER/TRANSMITTER "A" RECORD—RECORD LAYOUT

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	MINI-DISK SEQUENCE NUMBER	PAYER'S FEDERAL EIN	BLANK	COMBINED FEDERAL/STATE FILER	TYPE OF RETURN
1	2	3	4–6	7–15	16	17	18

PAYER/TRANSMITTER "A" RECORD—RECORD LAYOUT—Continued

SECTOR 1 (Continued)

AMOUNT INDICATORS	BLANK	"A" RECORD LENGTH	"B" RECORD LENGTH	BLANK
19–27	28	29–31	32–34	35

SECTOR 1 (Continued)

TRANSMITTER CONTROL CODE	BLANK	FIRST PAYER NAME	SECOND PAYER NAME	TRANSFER AGENT INDICATOR	BLANK
36–40	41	42–81	82–120	121	122–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYER SHIPPING ADDRESS	PAYER CITY, STATE AND ZIP CODE	BLANK
1	2	3–42	43–82	83–180

IF THE PAYER AND THE TRANSMITTER ARE THE SAME, THE "A" RECORD MAY BE TERMINATED WIT SECTOR 2 AS DESCRIBED ABOVE. HOWEVER, IF THE PAYER AND THE TRANSMITTER ARE NOT THE SAM OR THE TRANSMITTER INCLUDES FILES FOR MORE THAN ONE PAYER OR THIS IS A COMBINED FEDERA STATE FILING PAYER, THE FOLLOWING ITEMS ARE REQUIRED.

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYER SHIPPING ADDRESS	PAYER CITY, STATE AND ZIP CODE	FIRST NAME LINE OF TRANSMITTER	BLANK
1	2	3–42	43–82	83–122	123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	SECOND NAME LINE OF TRANSMITTER	TRANSMITTER MAILING ADDRESS	TRANSMITTER CITY, STATE AND ZIP CODE	BLANK
1	2	3–42	43–82	83–122	123–180

SEC. 4. PAYEE "B" RECORDS—GENERAL INFORMATION FOR ALL FORMS

.01 This section contains the general information concerning the Payee "B" Record for all information returns. For detailed descriptions of the record refer to the following:

(a) Sec. 5. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORMS 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R AND 5498.

(b) Sec. 7. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM 1099–A.

(c) Sec. 9. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM 1099–B.

(d) Sec. 11. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM W–2G.

.02 The Payee "B" Record contains the payment information from the individual statements. When filing information documents on mini-disk(s), the format for the Payee "B" Records will vary in relation to the number of payment amount fields being reported. The number of payment amount fields will depend upon the number of Payment Amount Indicator Codes used in positions 19–27 of the Payer/Transmitter "A" Record. For example, if you are reporting 1099–INT, position 18 of the Payer/Transmitter "A" Record will be coded with a "6." If the Amount Indicators used to report this interest are Amount Codes "1," "2," and "3," the mini-disk positions 19–27 of the "A" Re ord will be coded "123bbbbbb" (b rep resents a *blank* position). To correspon with Amount Indicators "1," "2," and "3 of the "A" Record, the "B" Record wi contain three payment amount fields. Min disk positions 32–41 of the "B" Recor will contain the payment amount to b reported for Amount Code "1" (Earnin from savings and loan associations, cred unions, bank deposits, bearer certificate of deposit, etc.); mini-disk positions 42 51 of the "B" Record will contain th payment amount to be reported fo Amount Code "2" (Amount of forfei ure); and mini-disk positions 52–61 of th "B" Record will contain the paymen mount to be reported for Amount Code 3" (Federal income tax withheld). The irst Payee Name Line *must* begin imediately after the last payment amount *at is indicated as being used.* In this exmple, the First Payee Name Line would egin in mini-disk position 62.

.03 All payee records *must contain corect payee name and address information* ntered in the fields prescribed in this secon. Records containing an invalid TIN SSN or EIN) and having no address data resent may be returned for correction. n searching for a payee address, if your fforts fail and you know that the address invalid, supply the invalid address rather han leave the field blank.

.04 IRS must be able to identify the urname associated with the TIN (SSN or EIN) furnished on a statement. The specifications below include a field in the payee ecords called "Name Control" in which he first four alphabetic characters of the ayee's surname or last name are to be ntered by the payer. The surname or last ame should appear first in the First Payee Name Line of all Payee "B" Records; owever, if your records have been developed using the first name first, IRS rograms will accept this but a blank must ppear between the first and last name.

.05 If payers are unable to provide the irst four characters of the surname, the Name Control Field may be left blank; however, compliance with the following will facilitate IRS computer programs in generating the Name Control.

(a) The surname of the payee whose TIN (SSN or EIN) is shown in the Payee "B" Record should always appear first. If, however, you enter the first name first, you must leave a blank space between the first and last name.

(b) In the case of multiple payees, only the surname of the payee whose TIN (SSN or EIN) is shown in the Payee "B" Record must be present in the First Payee Name Line. Surnames of any other payees in the record must be entered in the Second Payee Name Line.

.06 Provision is also made in these specifications for data entries required by state or local governments. This should minimize the Payer/Transmitter's programming burden should payers desire to report on mini-disk to state or local governments. See Part A, Sec. 14, for the Combined Federal/State filing requirements.

.07 Those filers participating in the Combined Federal/State Filing Program *must* have 180 position sectors. Positions 127 and 128 in the Payee "B" Records *must* contain the appropriate state code for the state to receive the information. The file should also meet the money criteria described in Part A, Sec. 14.11. Do not code for the states unless prior approval to participate has been granted by IRS. See Part A, Sec. 14.10 for a list of the valid participating state codes. *FORMS 1098, 1099–A, 1099–B, AND W–2G CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.* Your files must meet all of the requirements specified in Part A, Sec. 14, in order to participate in this program.

.08 All alpha characters entered in the "B" Record should be uppercase.

.09 *IRS STRONGLY ENCOURAGES FILERS TO REVIEW THEIR DATA FOR ACCURACY BEFORE SUBMISSION TO PREVENT ERRONEOUS NOTICES BEING MAILED TO PERSONS FOR WHOM REPORTS ARE FILED. FILERS SHOULD BE ESPECIALLY CAREFUL THAT THEIR TAXPAYER NAMES, SOCIAL SECURITY NUMBERS (SSNs), ACCOUNT NUMBERS, TYPES OF INCOME, AND INCOME AMOUNTS ARE CORRECT. ALTHOUGH IRS ENCOURAGES PAYERS TO FILL IN THE PAYER'S ACCOUNT NUMBER FOR THE PAYEE FIELD, THEY SHOULD NOT INCLUDE EXTRANEOUS DIGITS AS THE FIELD IS LIMITED, IN MAGNETIC MEDIA FILING, TO 10 POSITIONS.*

.10 *WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*

SEC. 5. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORMS 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R, AND 5498.

.01 This section contains the general payment information from individual statements for Forms 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R, and 5498.

.02 In most instances each Payee "B" Record described in this section will be composed of two sectors on the mini-disk with positions 1–41 being a constant format and the variance occurring in positions 42–180 of the first sector and the entire second sector. In those instances where six or more payment amount fields are reported, each Payee "B" Record will be composed of three sectors on the minidisk with positions 1–41 of the first sector being a constant format and the variance occurring in positions 42–180 of the first sector and the entire second and third sectors.

RECORD NAME: PAYEE "B" RECORD

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–4	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported (*e.g.*, if payments were made in 1986, enter "86"). Must be incremented each year.

RECORD NAME: PAYEE "B" RECORD—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
5–6	Document Specific Code	2	**REQUIRED for Forms 1099–R, 1099–MISC, and 1099–G. F *Form 1099–R*, enter the appropriate code for the Category of To Distribution. For *Form 1099–MISC*, enter the appropriate code f Direct Sales. For *Form 1099–G*, enter the year of income tax refu FOR ALL OTHER FORMS, ENTER BLANK. If only one co is used, left-justify and blank fill. (In prior years, mini-disk positi 6 of the "B" Record was used as the corrected return indicat This position was needed for the Document Specific Code. Mi disk position 7 of the "B" Record now represents a corrected retur You must adjust your programs.)**
	Category of Total Distribution (Form 1099–R only)		**Use only for reporting on *Form 1099–R* to identify the Categ of Total Distribution. You may select two codes except when usi Code 9. Enter the applicable code from the table below. Code below is *not required* for Amount Indicators 1, 2, and 3. A " (zero) is not a valid code for Form 1099–R. If you are reporting distribution from a KEOGH plan or any other distribution whe the following codes do not apply, enter blanks in this field.**

Category	*Co*
Premature distribution (other than codes 2, 3, 4, 5, 8, or P)	1
Rollover	2
Disability	3
Death (includes payments to a beneficiary)	4
Prohibited transaction	5
Other	6
Normal IRA, SEP or DEC distributions	7
Excess contributions refunded plus earnings on such excess contributions	8
PS 58 Costs (See NOTE)	9
Excess contributions refunded plus earnings on such excess contributions taxable in 1985	[illegible]
Qualifies for 10-year averaging	A
Qualifies for death benefit exclusion	B
Qualifies for both A and B	C

NOTE: PS 58 Costs may be reported on Form 1099–R; howev Form W–2P (filed with SSA) is preferable. Since this is not actu a total distribution, a separate "B" Record is required to report 58 Costs. These costs may not be reported in combination wit total distribution. Refer to the 1986 "Instructions for Forms 10 1098, 5498, 1096, and W–2G," available from IRS offices.

Mini-Disk Position	Field Title	Length	Description and Remarks
	Direct Sales (Form 1099–MISC only)		**Use only for direct sales reporting on *Form 1099–MISC*. If s to the recipient of consumer products on a buy-sell, deposit-c mission, or any other basis for resale, have amounted to $5,000 more, ENTER " 1". If you are filing 1099–MISC, with an Amo Indicator of "8" in the "A" Record, you must enter a code "1 this field. For all other 1099–MISC Amount Codes in the " Record, enter a "0" (zero) in this field. (In Part C, Sec. 2, in mation concerning the direct sales indicator can be found un Amount Indicators, Form 1099–MISC, NOTE 1 in the "A" R ord.) This code should appear in position 5. Position 6 will be bla**
	Refund is for Tax Year (Form 1099–G only)		**Use only for reporting the tax year for which the refund was issu If the payment amount field associated with Amount Indicato Income Tax Refunds, contains a refund, credit or offset tha**

RECORD NAME: PAYEE “B” RECORD—Continued

<table>
<tr><th>ini-Disk
osition</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">ECTOR 1 (Continued)</td></tr>
<tr><td></td><td></td><td></td><td>attributable to an income tax that applies exclusively to income from a trade or business and is not of general application, then enter the ALPHA equivalent of the year of refund from the table below. Otherwise, enter the NUMERIC Year for which the Refund was issued. This code should appear in position 5. Position 6 will be blank.
<table>
<tr><th><i>Year for which Refund was Issued</i></th><th><i>Alpha Equivalent</i></th></tr>
<tr><td>1</td><td>A</td></tr>
<tr><td>2</td><td>B</td></tr>
<tr><td>3</td><td>C</td></tr>
<tr><td>4</td><td>D</td></tr>
<tr><td>5</td><td>E</td></tr>
<tr><td>6</td><td>F</td></tr>
<tr><td>7</td><td>G</td></tr>
<tr><td>8</td><td>H</td></tr>
<tr><td>9</td><td>I</td></tr>
<tr><td>0</td><td>J</td></tr>
</table></td></tr>
<tr><td>7</td><td>Blank or Corrected Return Indicator</td><td>1</td><td>REQUIRED. Enter blank. (Reserved for IRS use). Mini-disk position 7 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using magnetic media. IN PRIOR YEARS, MINI-DISK POSITION 6 WAS USED AS THE CORRECTED RETURN INDICATOR. THIS HAS NOW CHANGED TO POSITION 7. <i>YOU MUST ADJUST YOUR PROGRAMS.</i></td></tr>
<tr><td>-11</td><td>Name Control</td><td>4</td><td>REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (-) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the Name Control:
<table>
<tr><th><i>Name</i></th><th><i>Name Control</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE*</td></tr>
<tr><td>James P. En Sr.</td><td>EN *</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must be left-justified and blank filled.</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identification Number (TIN) in positions 13-21 as either an Employer Identification Number, a Social Security Number, or the reason no number is shown. Enter the appropriate code from the following table:</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued

<table>
<tr><th>Mini-Disk Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td></td><td></td><td></td><td>
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, ente blank. If the number is unobtainable due legitimate cause; <i>e.g.</i>, number applied for not received, enter a blank.</td></tr>
</table>
</td></tr>
<tr><td>13-21</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Nu ber of the payee (SSN or EIN, as appropriate). Where an iden fication number has been applied for but not received or whe there is any other legitimate cause for not having an identificati number, <i>enter blanks</i>. Refer to Part A, Sec. 11.
<i>DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL OR ALL ZEROS.</i> Any record containing an invalid identificati number in this field will be returned for correction.</td></tr>
<tr><td>22-31</td><td>Payer's Account Number for Payee</td><td>10</td><td>REQUIRED. Payer may use this field to enter the payee's accou number. The use of this item will facilitate easy reference to speci records in the payer's file should any questions arise. DO NO ENTER A TAXPAYER IDENTIFICATION NUMBER IN TH FIELD. An account number can be any account number assign by the payer to the payee (<i>i.e.</i>, checking account, savings accou etc.). THIS NUMBER WILL HELP TO DISTINGUISH TH INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOUL BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTIO MADE WITH THE ORGANIZATION, SHOULD MULTIPL RETURNS BE FILED. This information will be particularly ne essary if you need to file a corrected return. You are strongly e couraged to use this field. You may use any number that will he identify the particular transaction that you are reporting. If a nu ber is not determinable, enter blanks. If fewer than ten charact are required, right-justify filling the remaining positions with blan</td></tr>
<tr><td></td><td>Payment Amount Fields (Must be numeric)</td><td></td><td>The number of payment amounts is dependent upon and must ag with the number of Amount Indicators present in positions 19 of the "A" Record. <i>THE FIRST PAYEE NAME LINE MU APPEAR AFTER THE LAST PAYMENT AMOUNT IND CATED AS BEING USED.</i> For example, if you are reporting 109 INT and you used only Amount Indicator "3" in the Payer/Tra mitter "A" Record, then you will only use one ten position payme amount in the Payee "B" Record, right-justified, and the First Pay Name Line will begin in position 42. Each payment field that y allow for, or use, must contain 10 numeric characters (see NOT 1). Do not provide a payment amount field when the correspondi Amount Indicator in the Payer/Transmitter "A" Record is blan Each payment amount must be entered in dollars and cents. D not enter dollar signs, commas, decimal points, or <i>NEGATI PAYMENTS</i> (except those items that reflect a loss on Form 109 B and must be negative overpunched in the units position). E ample: If the Amount Indicators are reflected as "123bbbbb", Payee "B" Records must have only 3 payment amount fields. Amount Indicators are reflected as "12367bbbb", the "B" Reco must have only 5 payment amount fields. Payment amounts MU</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount.
			NOTE 1: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee.
			NOTE 2: If you file 1099–MISC and use Amount Code "8" in the Amount Indicator field of the Payer/Transmitter "A" Record, you must enter 0000000100 in the corresponding Payment Amount Field. This will not represent an actual money amount; this is an indicator of direct sales. (Refer to Part C, Sec. 2, NOTE 1, of the Amount Indicators, Form 1099–MISC, for clarification.)
32-41	Payment Amount 1	10	This amount is identified by the indicator in Position 19 of Sector 1, of the Payer/Transmitter "A" Record. *This amount must always be present.*

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19-27 OF SECTOR 1 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42-180 OF SECTOR 1, POSITIONS 1-180 OF SECTOR 2 AND POSITIONS 1-180 OF SECTOR 3, IF NEEDED, OF THE PAYEE "B" RECORD. USE THE APPROPRIATE FORMAT AS REQUIRED.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)

SECTOR 1 (Continued)			
2-81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13-21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
82-121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13-21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
122-180	Blank	59	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of ea PAYEE Record.
3-42	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and unused positions with blanks. The address MUST be present. T field MUST NOT contain any data other than the payee's mail address.
43-71	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused p sitions with blanks. *Do not enter state and ZIP Code information this field.* (If the payee lives outside of the United States, ente "1" in position "43" of this field and spell out the name of the c in the remaining positions.)
72-73	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign co try. You *MUST* use valid U.S. Postal Service abbreviations as sho in the table in Part A, Sec. 16. Use this field for state or coun information *only*. If the code used is for a foreign country, inser "1" in position "43" of the Payee City field.
74-82	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U Postal Service. If only the first 5 digits are known, left-justify a *fill the unused positions with blanks*. Use this field for the ZIP Co *only*. For foreign countries, alpha characters are acceptable as lo as position "43" in the Payee City field is a "1".
83-126	Blank	44	REQUIRED. Enter blanks.
127-128	State Code	2	REQUIRED. If this payee record is to be forwarded to a st agency as part of the Combined Federal/State Filing Program, ent the valid state code from Part A, Sec. 14.10. For those states *NO* participating in this program or for FORM 1098, ENTER BLANK
129-180	Blank	52	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediate after the last payment amount indicated as being used. Do not ent address information in this field.* Enter the name of the payee (pre erably surname first) whose Taxpayer Identification Number ap pears in positions 13–21 of Sector 1. If fewer than 40 characters a required, left-justify and fill unused positions with blanks. If mo space is required *for the name*, utilize the Second Payee Name Lin field below. If there are multiple payees, *only the name* of the pay whose Taxpayer Identification Number has been provided shou be entered in this field. The names of the other payees should b entered in the Second Payee Name Line field. *NOTE: WHEN RE PORTING FORM 1098, "MORTGAGE INTEREST STAT MENT," THE "A" RECORD WILL REFLECT THE NAME O THE RECIPIENT OF THE INTEREST. THE "B" RECOR WILL REFLECT THE INDIVIDUAL PAYING THE INTERES AND THE AMOUNT PAID.*
92–180	Blank	89	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 2			
	Record Sequence		REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
3–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
3–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
12–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
14–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–126	Blank	4	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.
129–180	Blank	52	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)

ECTOR 1 (Continued)			
2–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
2–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
2–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			required, left-justify and fill unused positions with blanks. If m space is required *for the name*, utilize the Second Payee Name L field below. If there are multiple payees, *only the name* of the pa whose Taxpayer Identification Number has been provided sho be entered in this field. The names of the other payees should entered in the Second Payee Name Line field. *NOTE: WHEN R PORTING FORM 1098, "MORTGAGE INTEREST STAT MENT," THE "A" RECORD WILL REFLECT THE NAME THE RECIPIENT OF THE INTEREST. THE "B" RECO WILL REFLECT THE INDIVIDUAL PAYING THE INTERE AND THE AMOUNT PAID.*
102–180	Blank	79	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Use to sequence the sectors mak up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of e PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is av able in the First Payee Name Line, *enter the remaining portion the name only in this field*. If there are multiple payees (*e.g.*, partn or joint owners), this field may be used for those payees' *na* who are not associated with the taxpayer identification number positions 13–21 of Sector 1. *Do not enter address information in field*. Left-justify and fill unused positions with blanks. FILL W BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIEL
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and unused positions with blanks. The address MUST be present. T field MUST NOT contain any data other than the payee's mail address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused sitions with blanks. *Do not enter state and ZIP Code informatio this field*. (If the payee lives outside of the United States, inser "1" in position "83" of this field and spell out the name of the in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign co try. You *MUST* use valid U.S. Postal Service abbreviations as sho in the table in Part A, Sec. 16. Use this field for state or cou information *only*. If the code used is for a foreign country, inse "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U Postal Service. If only the first 5 digits are known, left-justify *fill the unused positions with blanks*. Use this field for the ZIP C *only*. For foreign countries, alpha characters are acceptable as l as position "83" in the Payee City field is a "1".
123–126	Blank	4	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a s agency as part of the Combined Federal/State Filing Program, e the valid state code from Part A, Sec. 14.10. For those states N participating in this program or for Form 1098, ENTER BLAN

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 2 (Continued)			
9–180	Blank	52	REQUIRED. Enter blanks.
–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
–111	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
12–180	Blank	69	REQUIRED. Enter blanks.
ECTOR 2			
	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
3–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
3–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
12–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
			information *only*. If the code used is for a foreign country, inser "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U Postal Service. If only the first 5 digits are known, left-justify *fill the unused positions with blanks*. Use this field for the ZIP C *only*. For foreign countries, alpha characters are acceptable as l as position "83" in the Payee City field is a "1".
123–126	Blank	4	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a s agency as part of the Combined Federal/State Filing Program, e the valid state code from Part A, Sec. 14.10. For those states *N* participating in this program or for Form 1098, ENTER BLAN
129–180	Blank	52	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
82–121	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immedi after the last payment amount indicated as being used. Do not e address information in this field*. Enter the name of the payee (p erably surname first) whose Taxpayer Identification Number pears in positions 13–21 of Sector 1. If fewer than 40 characters required, left-justify and fill unused positions with blanks. If m space is required *for the name*, utilize the Second Payee Name L field below. If there are multiple payees, *only the name* of the pa whose Taxpayer Identification Number has been provided sho be entered in this field. The names of the other payees should entered in the Second Payee Name Line field. *NOTE: WHEN PORTING FORM 1098, "MORTGAGE INTEREST STA MENT," THE "A" RECORD WILL REFLECT THE NAME THE RECIPIENT OF THE INTEREST. THE "B" RECO WILL REFLECT THE INDIVIDUAL PAYING THE INTER AND THE AMOUNT PAID.*
122–180	Blank	59	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors ma up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)—Continued

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 2 (Continued)			
-42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field*. If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field*. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
3–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
3–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field*. (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
12–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
14–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
23–126	Blank	4	REQUIRED. Enter blanks.
27–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states NOT participating in this program or for Form 1098, ENTER BLANKS.
29–180	Blank	52	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)

ECTOR 1 (Continued)			
2–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–180	Blank	89	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors mak up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of e PAYEE Record.
3–42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the payment amount indicated as being used. Do not enter address formation in this field.* Enter the name of the payee (preferal surname first) whose Taxpayer Identification Number appear positions 13–21 of Sector 1. If fewer than 40 characters are requir left-justify and fill unused positions with blanks. If more space required *for the name,* utilize the Second Payee Name Line fi below. If there are multiple payees, *only the name* of the pay whose Taxpayer Identification Number has been provided sho be entered in this field. The names of the other payees should entered in the Second Payee Name Line field. *NOTE: WHEN PORTING FORM 1098, "MORTGAGE INTEREST STA MENT," THE "A" RECORD WILL REFLECT THE NAME THE RECIPIENT OF THE INTEREST. THE "B" RECO WILL REFLECT THE INDIVIDUAL PAYING THE INTERE AND THE AMOUNT PAID.*
43–82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is av able in the First Payee Name Line, *enter the remaining portion the name only in this field.* If there are multiple payees (*e.g.*, partn or joint owners), this field may be used for those payees' *na* who are not associated with the Taxpayer Identification Numbe positions 13–21 of Sector 1. *Do not enter address information in field.* Left-justify and fill unused positions with blanks. FILL WI BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIEL
83–122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and unused positions with blanks. The address MUST be present. T field MUST NOT contain any data other than the payee's mai address.
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors mak up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of e PAYEE Record.
3–31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused sitions with blanks. *Do not enter state and ZIP Code informatio this field.* (If the payee lives outside of the United States, inse "1" in position "3" of this field and spell out the name of the in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign co try. You *MUST* use valid U.S. Postal Service abbreviations as sh in the table in Part A, Sec. 16. Use this field for state or cou information *only.* If the code used is for a foreign country, inse "1" in position "3" of the Payee City field.
34–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the Postal Service. If only the first 5 digits are known, left-justify

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 3 (Continued)			
			fill the unused positions with blanks. **Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".**
3–126	Blank	84	**REQUIRED. Enter blanks.**
27–128	State Code	2	**REQUIRED. If this payee record is to be forwarded to a state agency as part of the Combined Federal/State Filing Program, enter the valid state code from Part A, Sec. 14.10. For those states *NOT* participating in this program or for Form 1098, ENTER BLANKS.**
29–180	Blank	52	**REQUIRED. Enter blanks.**

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 1 (Continued)			
2–51	Payment Amount 2	10	**This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.**
2–61	Payment Amount 3	10	**This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.**
62–71	Payment Amount 4	10	**This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.**
72–81	Payment Amount 5	10	**This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.**
82–91	Payment Amount 6	10	**This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.**
92–101	Payment Amount 7	10	**This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.**
102–180	Blank	79	**REQUIRED. Enter blanks.**
SECTOR 2			
1	Record Sequence	1	**REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.**
2	Record Type	1	**REQUIRED. Enter "B". Must be the second position of each PAYEE Record.**
3–42	First Payee Name Line	40	**REQUIRED. *The First Payee Name Line must appear after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098 "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.***
43–82	Second Payee Name Line	40	**REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of***

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
			the name only in this field. If there are multiple payees (*e.g.*, partn or joint owners), this field may be used for those payees' *na* who are not associated with the Taxpayer Identification Numbe positions 13–21 of Sector 1. *Do not enter address information in field.* Left-justify and fill unused positions with blanks. FILL W BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIEL
83–122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and unused positions with blanks. The address MUST be present. T field MUST NOT contain any data other than the payee's ma address.
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors ma up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of PAYEE Record.
3–31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused sitions with blanks. *Do not enter state and ZIP Code informatio this field.* (If the payee lives outside of the United States, inse "1" in position "3" of this field and spell out the name of the in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign co try. You *MUST* use valid U.S. Postal Service abbreviations as sho in the table in Part A, Sec. 16. Use this field for state or cou information *only*. If the code used is for a foreign country, inse "1" in position "3" of the Payee City field.
34–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the Postal Service. If only the first 5 digits are known, left-justify *fill the unused positions with blanks*. Use this field for the ZIP C *only*. For foreign countries, alpha characters are acceptable as as position "3" in the Payee City field is a "1".
43–126	Blank	84	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a s agency as part of the Combined Federal/State Filing Program, e the valid state code from Part A, Sec. 14.10. For those states N participating in this program or for Form 1098, ENTER BLAN
129–180	Blank	52	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING EIGHT PAYMENT FIELDS)

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42-51	Payment Amount 2	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
52-61	Payment Amount 3	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
62-71	Payment Amount 4	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE "B" RECORD (USING EIGHT PAYMENT FIELDS)—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
ECTOR 1 (Continued)			
2-81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
2-91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
2-101	Payment Amount 7	10	This amount is identified by the amount indicator in position 25, Sector 1, of the Payer/Transmitter "A" Record.
02-111	Payment Amount 8	10	This amount is identified by the amount indicator in position 26, Sector 1, of the Payer/Transmitter "A" Record.
12–180	Blank	69	REQUIRED. Enter blanks.
ECTOR 2			
	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
-42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
43–82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
83–122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING EIGHT PAYMENT FIELDS)—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of e PAYEE Record.
3–31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused sitions with blanks. *Do not enter state and ZIP Code information* *this field*. (If the payee lives outside of the United States, inser "1" in position "3" of this field and spell out the name of the in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign co try. You MUST use valid U.S. Postal Service abbreviations as sho in the table in Part A, Sec. 16. Use this field for state or coun information *only*. If the code used is for a foreign country, inser "1" in position "3" of the Payee City field.
34–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U Postal Service. If only the first 5 digits are known, left-justify *fill the unused positions with blanks*. Use this field for the ZIP C *only*. For foreign countries, alpha characters are acceptable as l as position "3" in the Payee City field is a "1".
43–126	Blank	84	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a s agency as part of the Combined Federal/State Filing Program, e the valid state code from Part A, Sec. 14.10. For those states *N* participating in this program or for Form 1098, ENTER BLAN
129–180	Blank	52	REQUIRED. Enter blanks.
SECTOR 1 (Continued)			

RECORD NAME: PAYEE "B" RECORD (USING NINE PAYMENT FIELDS)

Mini-Disk Position	Field Title	Length	Description and Remarks
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
92–101	Payment Amount 7	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
102–111	Payment Amount 8	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
112–121	Payment Amount 9	10	This amount is identified by the amount indicator in position Sector 1, of the Payer/Transmitter "A" Record.
122–180	Blank	59	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING NINE PAYMENT FIELDS)—Continued

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 2			
	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
-42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field. *NOTE: WHEN REPORTING FORM 1098, "MORTGAGE INTEREST STATEMENT," THE "A" RECORD WILL REFLECT THE NAME OF THE RECIPIENT OF THE INTEREST. THE "B" RECORD WILL REFLECT THE INDIVIDUAL PAYING THE INTEREST AND THE AMOUNT PAID.*
3-82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
3–122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
-31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32–33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
34–42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and

RECORD NAME: PAYEE "B" RECORD (USING NINE PAYMENT FIELDS)—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
			fill the unused positions with blanks. Use this field for the ZIP Co *only.* For foreign countries, alpha characters are acceptable as lo as position "3" in the Payee City field is a "1".
43–126	Blank	84	REQUIRED. Enter blanks.
127–128	State Code	2	REQUIRED. If this payee record is to be forwarded to a st agency as part of the Combined Federal/State Filing Program, ent the valid state code from Part A, Sec. 14.10. For those states *NO* participating in this program or for Form 1098, ENTER BLANK
129–180	Blank	52	REQUIRED. Enter blanks.

SEC. 6. PAYEE "B" RECORD—RECORD LAYOUTS FOR FORMS 1098, 1099–DIV, 1099–G, 1099–INT, 1099–MISC, 1099–OID, 1099–PATR, 1099–R AND 5498

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATIO NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	BLANK
22–31	32–41	42–81	82–121	122–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–71	72–73	74–82

SECTOR 2 (Continued)

BLANK	STATE CODE	BLANK
83–126	127–128	129–180

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATIO NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–91	92–180

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)—Continued

ECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

ECTOR 2 (Continued)

BLANK	STATE CODE	BLANK
123–126	127–128	129–180

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–111	112–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

SECTOR 2 (Continued)

BLANK	STATE CODE	BLANK
123–126	127–128	129–180

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–101	102–180

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)—Continued

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

SECTOR 2 (Continued)

BLANK	STATE CODE	BLANK
123–126	127–128	129–180

PAYEE "B" RECORD—RECORD LAYOUT (USING FIVE PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–81	82–121	122–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

SECTOR 2 (Continued)

BLANK	STATE CODE	BLANK
123–126	127–128	129–180

PAYEE "B" RECORD—RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)—Continued

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATIO NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

BLANK
92–180

PAYEE "B" RECORD—RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)—Continued

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE	BLANK
1	2	3–31	32–33	34–42	43–126	127–128	129–180

PAYEE "B" RECORD—RECORD LAYOUT (USING SEVEN PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	BLANK
92–101	102–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE	BLANK
1	2	3–31	32–33	34–42	43–126	127–128	129–180

PAYEE "B" RECORD—RECORD LAYOUT (USING EIGHT PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

PAYEE "B" RECORD—RECORD LAYOUT (USING EIGHT PAYMENT AMOUNT FIELDS)—Continued

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8	BLANK
92–101	102–111	112–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE	BLANK
1	2	3–31	32–33	34–42	43–126	127–128	129–180

PAYEE "B" RECORD—RECORD LAYOUT (USING NINE PAYMENT AMOUNT FIELDS)

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	PAYMENT AMOUNT 8	PAYMENT AMOUNT 9	BLANK
92–101	102–111	112–121	122–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK	STATE CODE	BLANK
1	2	3–31	32–33	34–42	43–126	127–128	129–180

SEC. 7. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM 1099–A

.01 This section contains the general payment information from individual statements for Form 1099–A. For detailed explanations of the 1099–A fields, request a copy of the 1986 "Instructions for Form 1099, 1098, 5498, 1096, and W–2G" available from IRS offices.

.02 For Form 1099–A, SECTOR 3 will be required if there is more than one payment field to be reported in the Payee "B" Record.

.03 FORM 1099–A CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.

RECORD NAME: PAYEE "B" RECORD
FORM 1099–A

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-4	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported (*e.g.*, if payments were made in 1986, enter "86"). Must be incremented each year.
5-6	Document Specific Code	2	REQUIRED. For Form 1099–A, enter blanks.
7	Blank or Corrected Return Indicator	1	REQUIRED. Enter blank. (Reserved for IRS use). Mini-disk position 7 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using magnetic media. IN PRIOR YEARS, MINI-DISK POSITION 6 WAS USED AS THE CORRECTED RETURN INDICATOR. THIS HAS NOW CHANGED TO POSITION 7. *YOU MUST ADJUST YOUR PROGRAMS.*
8-11	Name Control	4	REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (-) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the Name Control:

Name	*Name Control*
John Brown	BROW
John A. Lee	LEE*
James P. En Sr.	EN*
John O'Neill	ONEI
Mary Van Buren	VANB
John Diben Edetto	DIBE
Juan De Jesus	DEJE
John A. El-Roy	EL-R
Mr. John Smith	SMIT
Joe McCarthy	MCCA
Pedro Torres-Lopes	TORR
Mark D'Allesandro	DALL

*Name Controls of less than four (4) significant characters must be left-justified and blank filled.

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099-A

<table>
<tr><th>Mini-Disk Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identi cation Number (TIN) in positions 13–21 as either an Employe Identification Number, a Social Security Number, or the reason n number is shown. Enter the appropriate code from the followi table:
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, enter blank. If the number is unobtainable due t legitimate cause; <i>e.g.</i>, number applied for b not received, enter a blank.</td></tr>
</table></td></tr>
<tr><td>13–21</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Num ber of the payee (SSN or EIN, as appropriate). Where an identi fication number has been applied for but not received or whe there is any other legitimate cause for not having an identificatio number, <i>enter blanks</i>. Refer to Part A, Sec. 11.

<i>DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL OR ALL ZEROS</i>. Any record containing an invalid identifyi number in this field will be returned for correction.</td></tr>
<tr><td>22–31</td><td>Payer's Account Number for Payee</td><td>10</td><td>REQUIRED. Payer may use this field to enter the payee's accou number. The use of this item will facilitate easy reference to speci records in the payer's file should any questions arise. DO NO ENTER A TAXPAYER IDENTIFICATION NUMBER IN TH FIELD. An account number can be any account number assign by the payer to the payee (<i>i.e.</i>, checking account, savings account etc.). THIS NUMBER WILL HELP TO DISTINGUISH TH INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOUL BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTIO MADE WITH THE ORGANIZATION, SHOULD MULTIPL RETURNS BE FILED. This information will be particularly ne essary if you need to file a corrected return. You are strongly en couraged to use this field. You may use any number that will hel identify the particular transaction that you are reporting. If a num ber is not determinable, enter blanks. If fewer than ten characte are required, right-justify filling the remaining positions with blanks</td></tr>
<tr><td></td><td>Payment Amount Fields (Must be numeric)</td><td></td><td>The number of payment amounts is dependent upon and must agre with the number of Amount Indicators present in positions 19-2 of the "A" Record. The First Payee Name Line <i>must</i> appear im mediately after the last payment amount indicated as being used For example, if you are reporting 1099–INT and you used onl Amount Indicator "3" in the Payer/Transmitter "A" Record, the you will only use one ten position payment amount in the Paye "B" Record, right-justified, and the First Payee Name Line wi begin in position 42. Each payment field that you allow for, or use must contain 10 numeric characters (see NOTE). Do not provid a payment amount field when the corresponding Amount Indicato in the Payer/Transmitter "A" Record is blank. Each payment amou must be entered in dollars and cents. Do not enter dollar signs commas, decimal points, or <i>NEGATIVE PAYMENTS</i>. Example</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099-A

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
			If the Amount Indicators are reflected as "123bbbbbb", the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb", the "B" Records must have only 5 payment amount fields. Payment amounts MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee.
32–41	Payment Amount 1	10	This amount is identified by the indicator in position 19 of the Payer/Transmitter "A" Record. *This amount must always be present.*

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–180 OF SECTOR 1, POSITIONS 1–180 OF SECTOR 2 AND POSITIONS 1–180 OF SECTOR 3, IF NEEDED, OF THE PAYEE "B" RECORD. *FOR FORM 1099–A, SECTOR 3 WILL BE REQUIRED IF THERE IS MORE THAN ONE PAYMENT FIELD TO BE REPORTED IN THE PAYEE "B" RECORD.* USE THE APPROPRIATE FORMAT AS REQUIRED.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)
FORM 1099-A

SECTOR 1 (Continued)			
42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.,* partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
122–180	Blank	59	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued
FORM 1099–A

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
43–71	Payee City	29	**REQUIRED.** Enter the city, left-justified and fill the unused po sitions with blanks. *Do not enter state and ZIP Code information i this field.* (If the payee lives outside of the United States, insert "1" in position "43" of this field and spell out the name of the ci in the remaining positions.)
72–73	Payee State	2	**REQUIRED.** Enter the abbreviation for the state or foreign cou try. You *MUST* use valid U.S. Postal Service abbreviations as show in the table in Part A, Sec. 16. Use this field for state or countr information *only*. If the code used is for a foreign country, insert "1" in position "43" of the Payee City field.
74–82	Payee ZIP Code	9	**REQUIRED.** Enter the valid 9 digit ZIP Code assigned by the U.S Postal Service. If only the first 5 digits are known, left-justify an *fill the unused positions with blanks.* Use this field for the ZIP Cod *only*. For foreign countries, alpha characters are acceptable as lo as position "43" in the Payee City field is a "1".
83–88	Lender's Date of Acquisition or Abandonment	6	**REQUIRED** *FOR FORM 1099–A ONLY.* Enter the date of you acquisition of the secured property or the date you first knew o had reason to know that the property was abandoned in the form MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.
89	Liability Indicator	1	**REQUIRED** *FOR FORM 1099–A ONLY.* Enter the appropria indicator from table below: *Indicator* *Usage* 1 Borrower is personally liable for repayment of th debt. Blank Borrower is *not* liable for repayment of the debt.
90–126	Description	37	**REQUIRED** *FOR FORM 1099–A ONLY.* Enter a brief descrip tion of the property. For example, for real property, enter th address, section, lot and block. For personal property, enter th type, make and model (*e.g.*, Car–1986 Buick Regal or Office Equip ment, etc.).
127–180	Blank	54	**REQUIRED.** Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)
FORM 1099–A

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	**REQUIRED.** *The First Payee Name Line must appear immediate after the last payment amount indicated as being used. Do not ente address information in this field.* Enter the name of the payee (pref erably surname first) whose Taxpayer Identification Number ap pears in positions 13–21 of Sector 1. If fewer than 40 characters ar required, left-justify and fill unused positions with blanks. If mor space is required *for the name,* utilize the Second Payee Name Lin field below. If there are multiple payees, *only the name* of the paye whose Taxpayer Identification Number has been provided shoul be entered in this field. The names of the other payees should b entered in the Second Payee Name Line field.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued

FORM 1099-A

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
92–180	Blank	89	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-82	Blank	80	REQUIRED. Enter blanks.
83–88	Lender's Date of Acquisition or Abandonment	6	REQUIRED *FOR FORM 1099-A ONLY*. Enter the date of your acquisition of the secured property or the date you first knew or had reason to know that the property was abandoned in the format MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued

FORM 1099-A

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
89	Liability Indicator	1	REQUIRED *FOR FORM 1099–A ONLY*. Enter the appropria indicator from table below: *Indicator* *Usage* 1 Borrower is personally liable for repayment of th debt. Blank Borrower is *not* liable for repayment of the debt.
90–126	Description	37	REQUIRED FOR FORM 1099–A ONLY. Enter a brief description of the property. For example, for real property, enter th address, section, lot and block. For personal property, enter th type, make and model (*e.g.*, Car–1986 Buick Regal or Office Equipment, etc.).
127–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)

FORM 1099-A

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
62–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediate after the last payment amount indicated as being used. Do not ent address information in this field*. Enter the name of the payee (pre erably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters a required, left-justify and fill unused positions with blanks. If mo space is required *for the name*, utilize the Second Payee Name Li field below. If there are multiple payees, *only the name* of the paye whose Taxpayer Identification Number has been provided shou be entered in this field. The names of the other payees should b entered in the Second Payee Name Line field.
102–180	Blank	79	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of ea PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avai able in the First Payee Name Line, *enter the remaining portion the name only in this field*. If there are multiple payees (*e.g.*, partne or joint owners), this field may be used for those payees' *nam* who are not associated with the Taxpayer Identification Number positions 13–21 of Sector 1. *Do not enter address information in t field*. Left-justify and fill unused positions with blanks. FILL WIT BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIEL

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued

FORM 1099-A

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
43-82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
83-111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112-113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114-122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123-180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-82	Blank	80	REQUIRED. Enter blanks.
83-88	Lender's Date of Acquisition or Abandonment	6	REQUIRED *FOR FORM 1099-A ONLY*. Enter the date of your acquisition of the secured property or the date you first knew or had reason to know that the property was abandoned in the format MMDDYY. DO NOT ENTER HYPHENS OR SLASHES.
89	Liability Indicator	1	REQUIRED *FOR FORM 1099-A ONLY*. Enter the appropriate indicator from the table below: *Indicator* — *Usage* 1 — Borrower is personally liable for repayment of the debt. Blank — Borrower is *not* liable for repayment of the debt.
90-126	Description	37	REQUIRED *FOR FORM 1099-A ONLY*. Enter a brief description of the property. For example, for real property, enter the address, section, lot and block. For personal property, enter the type, make and model (*e.g.*, Car-1986 Buick Regal or Office Equipment, etc.).
127-180	Blank	54	REQUIRED. Enter blanks.

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)
FORM 1099–A

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	BLANK
22–31	32–41	42–81	82–121	122–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–71	72–73	74–82

SECTOR 2 (Continued)

LENDER'S DATE OF ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION	BLANK
83–88	89	90–126	127–180

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)
FORM 1099–A

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–91	92–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

SECTOR 2 (Continued)

BLANK
123–180

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued
FORM 1099-A

ECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	LENDER'S DATE OF ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION	BLANK
1	2	3–82	83–88	89	90–126	127–180

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)
FORM 1099–A

ECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–101	102–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

SECTOR 2 (Continued)

BLANK
123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	LENDER'S DATE OF ACQUISITION OR ABANDONMENT	LIABILITY INDICATOR	DESCRIPTION	BLANK
1	2	3–82	83–88	89	90–126	127–180

SEC. 9. PAYEE "B" RECORDS—FIELD DESCRIPTIONS FOR FORM 1099–B

.01 This section contains the general payment information from individual statements for Form 1099–B. For detailed explanations of the 1099–B fields, request a copy of the 1986 "Instructions for Form 1099, 1098, 5498, 1096, and W–2G" available from IRS offices.

.02 For Form 1099–B, SECTOR 3 will be required if there is more than one payment field to be reported in the Payee "B" Record.

.03 FORM 1099–B CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.

RECORD NAME: PAYEE "B" RECORD
FORM 1099–B

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". Used to sequence the sectors making up a Service PAYEE Record.

RECORD NAME: PAYEE "B" RECORD—Continued

FORM 1099-B

<table>
<tr><th>Mini-Disk Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td>2</td><td>Record Type</td><td>1</td><td>REQUIRED. Enter "B". Must be the second position of ead PAYEE Record.</td></tr>
<tr><td>3–4</td><td>Payment Year</td><td>2</td><td>REQUIRED. Must be the last two digits of the year for whi payments are being reported; <i>e.g.</i>, if payments were made in 198 enter "86". Must be incremented each year.</td></tr>
<tr><td>5–6</td><td>Document Specific Code</td><td>2</td><td>REQUIRED. For Form 1099–B, enter blanks.</td></tr>
<tr><td>7</td><td>Blank or Corrected Return Indicator</td><td>1</td><td>REQUIRED. Enter blank. (Reserved for IRS use.) Mini-disk po sition 7 is used to indicate a corrected return. Refer to Part A, Sec 10 for specific instructions on how to file corrected returns usin magnetic media. IN PRIOR YEARS, MINI-DISK POSITION WAS USED AS THE CORRECTED RETURN INDICATOR THIS HAS NOW CHANGED TO POSITION 7. <i>YOU MUS ADJUST YOUR PROGRAMS.</i></td></tr>
<tr><td>8–11</td><td>Name Control</td><td>4</td><td>REQUIRED. Enter the first 4 letters of the surname of the paye Surnames of less than four (4) letters should be left-justified fillin the unused positions with blanks. Special characters and imbedde blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINES NAME, LEAVE THIS FIELD BLANK. A das (-) or ampersand (&) are the only acceptable special character The following examples may be helpful to you in developing th Name Control:
<table>
<tr><th><i>Name</i></th><th><i>Name Control</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE*</td></tr>
<tr><td>James P. En Sr.</td><td>EN*</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must b left-justified and blank filled.</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identif cation Number (TIN) in positions 13–21 as either an Employe Identification Number, a Social Security Number, or the reason n number is shown. Enter the appropriate code from the table below
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, enter blank. If the number is unobtainable due</td></tr>
</table></td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued
FORM 1099-B

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 1 (Continued)			
			legitimate cause; *e.g.*, number applied for but not received, enter a blank.
3-21	Taxpayer Identification Number	9	REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the payee (SSN or EIN, as appropriate). Where an identification number has been applied for but not received or where there is any other legitimate cause for not having an identification number, *enter blanks*. Refer to Part A, Sec. 11. *DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s OR ALL ZEROS.* Any record containing an invalid identifying number in this field will be returned for correction.
2-31	Payer's Account Number for Payee	10	REQUIRED. Payer must use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payer's file should any questions arise. DO NOT ENTER A TAXPAYER IDENTIFICATION NUMBER IN THIS FIELD. An account number can be any account number assigned by the payer to the payee (*i.e.*., checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any number that will help identify the particular transaction that you are reporting. If a number is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.
	Payment Amount Fields (Must be numeric)		The number of payment amounts is dependent upon and must agree with the number of Amount Indicators present in positions 19–27 of the "A" Record. The First Payee Name Line *must* appear after the last payment amount indicated as being used. For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one ten position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS* (except those items that reflect a loss on Form 1099–B and must be negative overpunched in the units position). Example: If the Amount Indicators are reflected as "123bbbbbb", the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb", the "B" Records must have only 5 payment amount fields. Payment amounts MUST be right-justified and unused positions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee.
32–41	Payment Amount 1	10	This amount is identified by the amount indicator in position 19 of the Payer/Transmitter "A" Record. *This amount must always be present.*

RECORD NAME: PAYEE “B” RECORD—Continued

FORM 1099–B

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE “B RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF SECTOR 1 OF THE PAYER/TRANSMITTER “A” RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–180 OF SECTOR 1, POSITIONS 1–180 OF SECTOR 2, AND POSITIONS 1–180 OF SECTOR 3, OF THE PAYEE “B” RECORD. *FOR FORM 1099–B, SECTOR 3 WILL BE REQUIRED IF THERE IS MORE THA ONE PAYMENT FIELD TO BE REPORTED IN THE PAYEE “B” RECORD*. USE THE APPROPRIATE FORMAT A REQUIRED.

RECORD NAME: PAYEE “B” RECORD (USING ONE PAYMENT FIELD)

FORM 1099-B

SECTOR 1 (Continued)			
42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediat after the last payment amount indicated as being used. Do not ent address information in this field*. Enter the name of the payee (pre erably surname first) whose Taxpayer Identification Number a pears in positions 13–21 of Sector 1. If fewer than 40 characters a required, left-justify and fill unused positions with blanks. If mo space is required *for the name*, utilize the Second Payee Name Li field below. If there are multiple payees, *only the name* of the paye whose Taxpayer Identification Number has been provided shou be entered in this field. The names of the other payees should b entered in the Second Payee Name Line field.
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is avai able in the First Payee Name Line, *enter the remaining portion the name only in this field*. If there are multiple payees (*e.g.*, partne or joint owners), this field may be used for those payees' *nam* who are not associated with the Taxpayer Identification Number positions 13–21 of Sector 1. *Do not enter address information in th field*. Left-justify and fill unused positions with blanks. FILL WIT BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIEL
122–180	Blank	59	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a “2”. Used to sequence the sectors maki up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter “B”. Must be the second position of ea PAYEE Record.
3–42	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and unused positions with blanks. The address MUST be present. T field MUST NOT contain any data other than the payee's maili address.
43–71	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused sitions with blanks. *Do not enter state and ZIP Code information this field*. (If the payee lives outside of the United States, inser “1” in position “43” of this field and spell out the name of the in the remaining positions.)
72–73	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign co try. You *MUST* use valid U.S. Postal Service abbreviations as sho in the table in Part A, Sec. 16. Use this field for state or cou information *only*. If the code used is for a foreign country, inse “1” in position “43” of the Payee City field.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued
FORM 1099-B

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
74–82	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "43" in the Payee City field is a "1".
83–85	Blank	3	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* — *Usage* S — Date of Sale is the actual settlement date blank — Date of Sale is the trade date or this is an aggregate transaction .
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
93–100	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
101–126	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
127–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)
FORM 1099–B

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field*. Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.
92–180	Blank	89	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued
FORM 1099-B

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field*. If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field*. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field*. (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter 'B". Must be the second position of each PAYEE Record.
3–85	Blank	83	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indictor from table below: *Indicator* *Usage* S Date of Sale is the actual settlement date blank Date of Sale is the trade date or this is an aggregate transaction
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued
FORM 1099-B

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 3 (Continued)			
3–100	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zeros) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
01–126	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
27–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)
FORM 1099–B

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field*. Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.
102–180	Blank	79	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field*. If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field*. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued
FORM 1099-B

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
			field MUST NOT contain any data other than the payee's mailin address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information i this field*. (If the payee lives outside of the United States, insert "1" in position "83" of this field and spell out the name of the ci in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as show in the table in Part A, Sec. 16. Use this field for state or countr information *only*. If the code used is for a foreign country, insert "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S Postal Service. If only the first 5 digits are known, left-justify an *fill the unused positions with blanks*. Use this field for the ZIP cod *only*. For foreign countries, alpha characters are acceptable as lon as position "83" in the Payee City field is a "1".
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–85	Blank	83	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* *Usage* S Date of Sale is the actual settlement date blank Date of Sale is the trade date or this is an aggrega transaction
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099–B ONLY*. Enter the trade date o the actual settlement date of the transaction in the format MMDDY Enter blanks if this is an aggregate transaction. DO NOT ENTE HYPHENS OR SLASHES.
93–100	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Co mittee on Uniform Security Identification Procedures) number the items reported for Amount Indicator "2" (Stocks, bonds, etc. Enter blanks if this is an aggregate transaction. Enter "0" (zero if the number is not available. For CUSIP numbers with more th 8 characters, supply the *first* 8.
101–126	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief descripti of the item or services for which the proceeds are being reporte If fewer than 26 characters are required, left-justify and fill unus positions with blanks. For regulated futures contracts, enter RF Enter blanks if this is an aggregate transaction.
127–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)
FORM 1099-B

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 1 (Continued)			
2–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
2–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
2–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
2-111	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payee should be entered in the Second Payee Name Line field.
112–180	Blank	69	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.,* partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued
FORM 1099-B

Mini-disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
			fill the unused positions with blanks. Use this field for the ZIP Cod *only*. For foreign countries, alpha characters are acceptable as lon as position "83" in the Payee City field is a "1".
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors makin up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of eac PAYEE Record.
3–85	Blank	83	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099-B ONLY*. Enter appropriate i dicator from table below: *Indicator* *Usage* S Date of Sale is the actual settlement date blank Date of Sale is the trade date or this is an aggrega transaction
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099-B ONLY* Enter the trade date o the actual settlement date of the transaction in the format MMDDY Enter blanks if this is an aggregate transaction. DO NOT ENTE HYPHENS OR SLASHES.
93–100	CUSIP No.	8	REQUIRED *FOR FORM 1099-B ONLY*. Enter the CUSIP (Com mittee on Uniform Security Indentification Procedures) number o the items reported for Amount Indicator "2" (Stocks, bonds, etc. Enter blanks if this is an aggregate transaction. Enter "0" (zero if the number is not available. For CUSIP numbers with more th 8 characters, supply the *first* 8.
101-126	Description	26	REQUIRED *FOR FORM 1099-B ONLY*. Enter a brief descriptio of the item or services for which the proceeds are being reporte If fewer than 26 characters are required, left-justify and fill unuse positions with blanks. For regulated futures contracts, enter RF Enter blanks if this is an aggregate transaction.
127–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)
FORM 1099-B

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20 Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21 Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22 Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23 Sector 1, of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)—Continued

FORM 1099-B

ni-Disk sition	Field Title	Length	Description and Remarks
CTOR 1 (Continued)			
-121	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Indentification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.
2–180	Blank	59	REQUIRED. Enter blanks.
CTOR 2			
	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
-42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
3-82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unusd positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.
83-111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING FIVE PAYMENT FIELDS)—Continued

FORM 1099-B

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–85	Blank	83	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099–B ONLY*. Enter appropriate indicator from table below: *Indicator* *Usage* S Date of Sale is the actual settlement date blank Date of Sale is the trade date or this is an aggregate transaction.
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099-B ONLY*. Enter the trade date or the actual settlement date of the transaction in the format MMDDYY. Enter blanks if this is an aggregate transaction. DO NOT ENTER HYPHENS OR SLASHES.
93–100	CUSIP No.	8	REQUIRED *FOR FORM 1099–B ONLY*. Enter the CUSIP (Committee on Uniform Security Identification Procedures) number of the items reported for Amount Indicator "2" (Stocks, bonds, etc.). Enter blanks if this is an aggregate transaction. Enter "0" (zero) if the number is not available. For CUSIP numbers with more than 8 characters, supply the *first* 8.
101–126	Description	26	REQUIRED *FOR FORM 1099–B ONLY*. Enter a brief description of the item or services for which the proceeds are being reported. If fewer than 26 characters are required, left-justify and fill unused positions with blanks. For regulated futures contracts, enter RFC. Enter blanks if this is an aggregate transaction.
127–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)

FORM 1099–B

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 23, Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 24, Sector 1, of the Payer/Transmitter "A" Record.
92–180	Blank	89	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)—Continued
FORM 1099-B

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 2 (Continued)			
42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.
3-82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field*. If there are multiple payees (*e.g.*, partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
3-122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
123–180	Blank	58	REQUIRED. Enter blanks.
ECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3." Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32-33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You MUST use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
34-42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1."
3-85	Blank	43	REQUIRED. Enter blanks.
6	Data of Sale Indicator	1	REQUIRED *FOR FORM 1099-B ONLY.* Enter appropriate indicator from table below.

RECORD NAME: PAYEE "B" RECORD (USING SIX PAYMENT FIELDS)—Continued

FORM 1099-B

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
			Indicator *Usage* S Date of Sale is the actual settlement date blank Date of Sale is the trade date or this is an aggrega transaction
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099-B ONLY*. Enter the trade date the actual settlement date of the transaction in the format MMDDY Enter blanks if this is an aggregate transaction. DO NOT ENTE HYPHENS OR SLASHES.
93–100	CUSIP No.	8	REQUIRED *FOR FORM 1099-B ONLY*. Enter the CUSIP (Co mittee on Uniform Security Identification Procedures) number the items reported for Amount Indicator "2" (Stocks, bonds, etc Enter blanks if this is an aggregate transaction. Enter "0" (zero if the number is not available. For CUSIP numbers with more th 8 characters, supply the *first* 8.
101–126	Description	26	REQUIRED *FOR FORM 1099-B ONLY*. Enter a brief descripti of the item or services for which the proceeds are being reporte If fewer than 26 characters are required, left-justify and fill unus positions with blanks. For regulated futures contracts, enter RF Enter blanks if this is an aggregate transaction.
127–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)

FORM 1099–B

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
52–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
62–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
72–81	Payment Amount 5	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
82–91	Payment Amount 6	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
92–101	Payment Amount 7	10	This amount is identified by the amount indicator in position 2 Sector 1, of the Payer/Transmitter "A" Record.
102–180	Blank	79	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors mak up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of ea PAYEE Record.

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued

FORM 1099-B

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 2 (Continued)			
-42	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.
3-82	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees (*e.g.,* partners or joint owners), this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
83-122	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sector making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-31	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "3" of this field and spell out the name of the city in the remaining positions.)
32-33	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "3" of the Payee City field.
34-42	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "3" in the Payee City field is a "1".
43-85	Blank	43	REQUIRED. Enter blanks.
86	Date of Sale Indicator	1	REQUIRED *FOR FORM 1099-B ONLY.* Enter appropriate indicator from table below:

RECORD NAME: PAYEE "B" RECORD (USING SEVEN PAYMENT FIELDS)—Continued
FORM 1099-B

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 3 (Continued)			
			Indicator *Usage* S Date of Sale is the actual settlement date blank Date of Sale is the trade date or this is an aggreg transaction
87–92	Date of Sale	6	REQUIRED *FOR FORM 1099-B ONLY*. Enter the trade date the actual settlement date of the transaction in the format MMDDY Enter blanks if this is an aggregate transaction. DO NOT ENTE HYPHENS OR SLASHES.
93–100	CUSIP No.	8	REQUIRED *FOR FORM 1099-B ONLY*. Enter the CUSIP (Co mittee on Uniform Security Identification Procedures) numbe the items reported for Amount Indicator "2" (Stocks, bonds, etc Enter blanks if this is an aggregate transaction. Enter "0" (zero if the number is not available. For CUSIP numbers with more th 8 characters, supply the *first* 8.
101–126	Description	26	REQUIRED *FOR FORM 1099-B ONLY*. Enter a brief descripti of the item or services for which the proceeds are being report If fewer than 26 characters are required, left-justify and fill unus positions with blanks. For regulated futures contracts, enter RF Enter blanks if this is an aggregate transaction.
127–180	Blank	54	REQUIRED. Enter blanks.

SEC. 10. PAYEE "B" RECORD—RECORD LAYOUT FOR FORM 1099-B

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)
FORM 1099-B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	BLANK
22–31	32–41	42–81	82–121	122–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–71	72–73	74–82	83–85

SECTOR 2 (Continued)

DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
86	87–92	93–100	101–126	127–180

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

FORM 1099-B

CTOR 1

RECORD EQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

CTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–91	92–180

CTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

ECTOR 2 (Continued)

BLANK
123–180

ECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–85	86	87–92	93–100	101–126	127–180

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

FORM 1099-B

ECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

ECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–101	102–180

ECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

PAYEE "B" RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)—Continued

FORM 1099–B

SECTOR 2 (Continued)

BLANK
123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–85	86	87–92	93–100	101–126	127–180

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–111	112–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

SECTOR 2 (Continued)

BLANK
123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–85	86	87–92	93–100	101–126	127–180

PAYEE "B" RECORD—RECORD LAYOUT (USING FIVE PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATI NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

PAYEE "B" RECORD—RECORD LAYOUT (USING FIVE PAYMENT AMOUNT FIELDS)—Continued

FORM 1099–B

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–81	82–121	122–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE
1	2	3–42	43–82	83–111	112–113	114–122

SECTOR 2 (Continued)

BLANK
123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
1	2	3–85	86	87–92	93–100	101–126	127–180

PAYEE "B" RECORD—RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)

FORM 1099–B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

BLANK
92–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–180

PAYEE "B" RECORD—RECORD LAYOUT (USING SIX PAYMENT AMOUNT FIELDS)—Continued

FORM 1099-B

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–31	32–33	34–42	43–85

SECTOR 3 (Continued)

DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
86	87–92	93–100	101–126	127–180

PAYEE "B" RECORD--RECORD LAYOUT (USING SEVEN PAYMENT AMOUNT FIELDS)

FORM 1099-B

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	PAYMENT AMOUNT 5	PAYMENT AMOUNT 6
22–31	32–41	42–51	52–61	62–71	72–81	82–91

SECTOR 1 (Continued)

PAYMENT AMOUNT 7	BLANK
92–101	102–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	BLANK
1	2	3–42	43–82	83–122	123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–31	32–33	34–42	43–85

SECTOR 3 (Continued)

DATE OF SALE INDICATOR	DATE OF SALE	CUSIP NO.	DESCRIPTION	BLANK
86	87–92	93–100	101–126	127–180

EC. 11. PAYEE "B" RECORDS—FIELD ESCRIPTIONS FOR FORM W–2G

.01 This section contains the general ayment information from individual statements for Form W–2G. For detailed explanations of the W–2G fields, request a copy of the 1986 "Instructions for Forms 1099, 1098, 5498, 1096, and W–2G," available from IRS offices.

.02 When reporting information for Form W–2G, the Payee "B" Records must contain 3 Sectors.

.03 FORM W-2G CANNOT BE FILED UNDER THE COMBINED FEDERAL/STATE FILING PROGRAM.

RECORD NAME: PAYEE "B" RECORD
FORM W-2G

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1			
1	Record Sequence	1	REQUIRED. Must be a "1". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-4	Payment Year	2	REQUIRED. Must be the last two digits of the year for which payments are being reported; *e.g.*, if payments were made in 1986, enter "86." Must be incremented each year.
5-6	Document Specific Code	1	REQUIRED for Form W-2G.
	Type of Wager (Form W-2G only)		Use only for reporting the Type of Wager on *Form W-2G*. This code will appear in mini-disk position 5. Position 6 will be blank. *Category* — *Code* Horse Race Track (or Off Track Betting of a Horse Track nature) 1 Dog Race Track (or Off Track Betting of a Dog Track nature) 2 Jai-alai 3 State Conducted Lottery 4 Keno 5 Casino Type Bingo. DO NOT use this code for any other type of Bingo winnings; i.e., Church, Fire Dept., etc. 6 Slot Machines 7 Any other types of gambling winnings. This includes Church Bingo, Fire Dept. Bingo, unlabeled winnings, etc. 8
7	Blank or Corrected Return Indicator	1	REQUIRED. Enter blank. (Reserved for IRS use.) Mini-disk position 7 is used to indicate a corrected return. Refer to Part A, Sec. 10 for specific instructions on how to file corrected returns using magnetic media. IN PRIOR YEARS, MINI-DISK POSITION 6 WAS USED AS THE CORRECTED RETURN INDICATOR. *YOU MUST ADJUST YOUR PROGRAMS.*
8-11	Name Control	4	REQUIRED. Enter the first 4 letters of the surname of the payee. Surnames of less than four (4) letters should be left-justified, filling the unused positions with blanks. Special characters and imbedded blanks should be removed. IF THE NAME CONTROL IS NOT DETERMINABLE BY THE PAYER, SUCH AS IN THE CASE OF A BUSINESS NAME, LEAVE THIS FIELD BLANK. A dash (-) or ampersand (&) are the only acceptable special characters. The following examples may be helpful to you in developing the Name Control:

RECORD NAME: PAYEE "B" RECORD—Continued
FORM W-2G

<table>
<tr><th>Mini-Disk Position</th><th>Field Title</th><th>Length</th><th>Description and Remarks</th></tr>
<tr><td colspan="4">SECTOR 1 (Continued)</td></tr>
<tr><td></td><td></td><td></td><td>
<table>
<tr><th><i>Name</i></th><th><i>Name Control</i></th></tr>
<tr><td>John Brown</td><td>BROW</td></tr>
<tr><td>John A. Lee</td><td>LEE *</td></tr>
<tr><td>James P. En Sr.</td><td>EN *</td></tr>
<tr><td>John O'Neill</td><td>ONEI</td></tr>
<tr><td>Mary Van Buren</td><td>VANB</td></tr>
<tr><td>John Diben Edetto</td><td>DIBE</td></tr>
<tr><td>Juan De Jesus</td><td>DEJE</td></tr>
<tr><td>John A. El-Roy</td><td>EL-R</td></tr>
<tr><td>Mr. John Smith</td><td>SMIT</td></tr>
<tr><td>Joe McCarthy</td><td>MCCA</td></tr>
<tr><td>Pedro Torres-Lopes</td><td>TORR</td></tr>
<tr><td>Mark D'Allesandro</td><td>DALL</td></tr>
</table>
*Name Controls of less than four (4) significant characters must be left-justified and blank filled.
</td></tr>
<tr><td>12</td><td>Type of TIN</td><td>1</td><td>REQUIRED. This field is used to identify the Taxpayer Identification Number (TIN) in positions 13–21 as either an Employer Identification Number, a Social Security Number, or the reason no number is shown. Enter the appropriate code from the following table:
<table>
<tr><th><i>Type of TIN</i></th><th><i>TIN</i></th><th><i>Type of Account</i></th></tr>
<tr><td>1</td><td>EIN</td><td>A business or an organization</td></tr>
<tr><td>2</td><td>SSN</td><td>An individual</td></tr>
<tr><td>blank</td><td>N/A</td><td>If the type of TIN is undeterminable, enter a blank. If the number is unobtainable due to legitimate cause; <i>e.g.</i>, number applied for but not received, enter a blank.</td></tr>
</table>
</td></tr>
<tr><td>13–21</td><td>Taxpayer Identification Number</td><td>9</td><td>REQUIRED. Enter the valid 9-digit Taxpayer Identification Number of the Payee (SSN or EIN, as appropriate). Where an identification number has been applied for but not received or where there is any other legitimate cause for not having an identification number, <i>enter blanks</i>. Refer to Part A, Sec. 11.

<i>DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9s or ALL ZEROS.</i> Any record containing an invalid identifying number in this field will be returned for correction.</td></tr>
<tr><td>22–31</td><td>Payer's Account Number for Payee</td><td>10</td><td>REQUIRED. Payer may use this field to enter the payee's account number. The use of this item will facilitate easy reference to specific records in the payer's file should any questions arise. DO NOT ENTER A TAXPAYER IDENFIFICATION NUMBER IN THIS FIELD. An account number can be any account number assigned by the payer to the payee (<i>i.e.</i>, checking account, savings account, etc.). THIS NUMBER WILL HELP TO DISTINGUISH THE INDIVIDUAL PAYEE'S ACCOUNT WITH YOU AND SHOULD BE UNIQUE TO IDENTIFY THE SPECIFIC TRANSACTION MADE WITH THE ORGANIZATION, SHOULD MULTIPLE RETURNS BE FILED. This information will be particularly necessary if you need to file a corrected return. You are strongly encouraged to use this field. You may use any number that will help identify the particular transaction that you are reporting. If a num-</td></tr>
</table>

RECORD NAME: PAYEE "B" RECORD—Continued

FORM W-2G

ni-Disk ition	Field Title	Length	Description and Remarks
CTOR 1 (Continued)			
			ber is not determinable, enter blanks. If fewer than ten characters are required, right-justify filling the remaining positions with blanks.
	Payment Amount Fields (Must be numeric)		The number of payment amounts is dependent upon and must agree with the number of Amount Indicators present in positions 19–27 of the "A" Record. The First Payee Name Line *must* appear immediately after the last payment amount indicated as being used. For example, if you are reporting 1099–INT and you used only Amount Indicator "3" in the Payer/Transmitter "A" Record, then you will only use one ten position payment amount in the Payee "B" Record, right-justified, and the First Payee Name Line will begin in position 42. Each payment field that you allow for, or use, must contain 10 numeric characters (see NOTE). Do not provide a payment amount field when the corresponding Amount Indicator in the Payer/Transmitter "A" Record is blank. Each payment amount must be entered in dollars and cents. Do not enter dollar signs, commas, decimal points, or *NEGATIVE PAYMENTS*. Example: If the Amount Indicators are reflected as "123bbbbbb", the Payee "B" Records must have only 3 payment amount fields. If Amount Indicators are reflected as "12367bbbb", the "B" Records must have only 5 payment amount fields. Payment amounts MUST be right-justified and unused portions MUST be zero filled. Federal income tax withheld is not reported as a negative amount. NOTE: If any one payment amount exceeds "9999999999" (dollars and cents), as many SEPARATE Payee "B" Records as necessary to contain the total amount MUST be submitted for the Payee.
32–41	Payment Amount 1	10	This amount is identified by the indicator in position 19 of Sector 1 of the Payer/Transmitter "A" Record. *This amount must always be present.*

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)

FORM W-2G

SECTOR 1 (Continued)

DETERMINE AT THIS POINT THE NUMBER OF PAYMENT FIELDS TO BE REPORTED WITHIN THE PAYEE "B" RECORD. THIS CAN BE DETERMINED FROM THE NUMBER OF AMOUNT INDICATORS APPEARING IN POSITIONS 19–27 OF SECTOR 1 OF THE PAYER/TRANSMITTER "A" RECORD. FOLLOWING ARE THE FORMATS FOR COMPLETING POSITIONS 42–180 OF SECTOR 1, POSITIONS 1–180 OF SECTOR 2 AND POSITIONS 1–180 OF SECTOR 3, IF NEEDED, OF THE PAYEE "B" RECORD. *WHEN REPORTING INFORMATION FOR FORM W-2G, THREE SECTORS MUST BE USED TO MAKE UP A PAYEE "B" RECORD.* USE THE APPROPRIATE FORMAT AS REQUIRED.

42–81	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued

FORM W-2G

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 1 (Continued)			
82–121	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion* *the name only in this field.* If there are multiple payees, (*e.g.*, partners or joint owners) this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
122–180	Blank	59	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
43–71	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "43" of this field and spell out the name of the city in the remaining positions.)
72–73	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use the field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "43" of the Payee City field.
74–82	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "43" in the Payee City field is a "1".
83–180	Blank	98	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–60	Blank	58	REQUIRED. Enter blanks.
61–66	Date Won	6	REQUIRED *FOR FORM W–2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.
67–81	Transaction	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the ticke number, card number (and color, if applicable), machine seria

RECORD NAME: PAYEE "B" RECORD (USING ONE PAYMENT FIELD)—Continued
FORM W-2G

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 3 (Continued)			
			number or any other information that will help identify the winning transaction. If no entry, enter blanks.
-86	Race	5	REQUIRED *FOR FORM W–2G ONLY*. The race (or game) applicable to the winning ticket. If no entry, enter blanks.
7-91	Cashier	5	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
2-96	Window	5	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.
7–111	First ID	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
12–126	Second ID	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
27–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)
FORM W-2G

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
52–91	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.
92–180	Blank	89	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3-42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field*. If there are multiple payees, (*e.g.*, partners or joint owners) this field may be used for those payees' names who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field*. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.

RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued
FORM W-2G

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
43–82	Payee Mailing Address	40	**REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than payee's mailing address.**
83–111	Payee City	29	**REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field*. (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)**
112–113	Payee State	2	**REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.**
114–122	Payee ZIP Code	9	**REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".**
123–180	Blank	58	**REQUIRED. Enter blanks.**
SECTOR 3			
1	Record Sequence	1	**REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.**
2	Record Type	1	**REQUIRED. Enter "B". Must be the second position of each PAYEE Record.**
3–60	Blank	58	**REQUIRED. Enter blanks.**
61–66	Date Won	6	**REQUIRED *FOR FORM W-2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.**
67–81	Transaction	15	**REQUIRED *FOR FORM W–2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number, or any other information that will help identify the winning transaction. If no entry, enter blanks.**
82–86	Race	5	**REQUIRED *FOR FORM W–2G ONLY*. The race (or game) applicable to the winning ticket. If no entry, enter blanks.**
87–91	Cashier	5	**REQUIRED *FOR FORM W–2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.**
92–96	Window	5	**REQUIRED *FOR FORM W–2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.**
97–111	First ID	15	**REQUIRED *FOR FORM W–2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.**

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RECORD NAME: PAYEE "B" RECORD (USING TWO PAYMENT FIELDS)—Continued

FORM W-2G

ni-Disk sition	Field Title	Length	Description and Remarks
CTOR 3 (Continued)			
2–126	Second ID	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
7–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)

FORM W-2G

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 1 (Continued)			
-51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.
2–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
2–101	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field*. Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears on positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name*, utilize the Second Payee Name Line field below. If there are multiple payees, *only the name*, of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.
102–180	Blank	79	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field*. If there are multiple payees, (*e.g.*, partners or joint owners) this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field*. Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field*. (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)

RECORD NAME: PAYEE "B" RECORD (USING THREE PAYMENT FIELDS)—Continued
FORM W-2G

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only*. If the code is used for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks*. Use this field for the ZIP Code *only*. For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–60	Blank	58	REQUIRED. Enter blanks.
61–66	Date Won	6	REQUIRED *FOR FORM W-2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.
67–81	Transaction	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number or any other information that will help identify the winning transaction. If no entry, enter blanks.
82–86	Race	5	REQUIRED *FOR FORM W–2G ONLY*. The race (or game) applicable to the winning ticket. If no entry, enter blanks.
87–91	Cashier	5	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
92–96	Window	5	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.
97–111	First ID	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
112–126	Second ID	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
127–180	Blank	54	REQUIRED. Enter blanks.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)
FORM W–2G

SECTOR 1 (Continued)			
42–51	Payment Amount 2	10	This amount is identified by the amount indicator in position 20, Sector 1, of the Payer/Transmitter "A" Record.

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued

FORM W-2G

ini-Disk osition	Field Title	Length	Description and Remarks
ECTOR 1 (Continued)			
2–61	Payment Amount 3	10	This amount is identified by the amount indicator in position 21, Sector 1, of the Payer/Transmitter "A" Record.
2–71	Payment Amount 4	10	This amount is identified by the amount indicator in position 22, Sector 1, of the Payer/Transmitter "A" Record.
2–111	First Payee Name Line	40	REQUIRED. *The First Payee Name Line must appear immediately after the last payment amount indicated as being used. Do not enter address information in this field.* Enter the name of the payee (preferably surname first) whose Taxpayer Identification Number appears in positions 13–21 of Sector 1. If fewer than 40 characters are required, left-justify and fill unused positions with blanks. If more space is required *for the name,* utilize the Second Payee Name Line field below. If there are multiple payees, *only the name* of the payee whose Taxpayer Identification Number has been provided should be entered in this field. The names of the other payees should be entered in the Second Payee Name Line field.
112–180	Blank	69	REQUIRED. Enter blanks.
SECTOR 2			
1	Record Sequence	1	REQUIRED. Must be a "2". Used to sequence the sectors making up a service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–42	Second Payee Name Line	40	REQUIRED. If the payee name requires more space than is available in the First Payee Name Line, *enter the remaining portion of the name only in this field.* If there are multiple payees, (*e.g.*, partners or joint owners) this field may be used for those payees' *names* who are not associated with the Taxpayer Identification Number in positions 13–21 of Sector 1. *Do not enter address information in this field.* Left-justify and fill unused positions with blanks. FILL WITH BLANKS IF NO ENTRIES ARE PRESENT FOR THIS FIELD.
43–82	Payee Mailing Address	40	REQUIRED. Enter mailing address of payee. Left-justify and fill unused positions with blanks. The address MUST be present. This field MUST NOT contain any data other than the payee's mailing address.
83–111	Payee City	29	REQUIRED. Enter the city, left-justified and fill the unused positions with blanks. *Do not enter state and ZIP Code information in this field.* (If the payee lives outside of the United States, insert a "1" in position "83" of this field and spell out the name of the city in the remaining positions.)
112–113	Payee State	2	REQUIRED. Enter the abbreviation for the state or foreign country. You *MUST* use valid U.S. Postal Service abbreviations as shown in the table in Part A, Sec. 16. Use this field for state or country information *only.* If the code used is for a foreign country, insert a "1" in position "83" of the Payee City field.
114–122	Payee ZIP Code	9	REQUIRED. Enter the valid 9 digit ZIP Code assigned by the U.S. Postal Service. If only the first 5 digits are known, left-justify and *fill the unused positions with blanks.* Use this field for the ZIP Code *only.* For foreign countries, alpha characters are acceptable as long as position "83" in the Payee City field is a "1".

RECORD NAME: PAYEE "B" RECORD (USING FOUR PAYMENT FIELDS)—Continued
FORM W-2G

Mini-Disk Position	Field Title	Length	Description and Remarks
SECTOR 2 (Continued)			
123–180	Blank	58	REQUIRED. Enter blanks.
SECTOR 3			
1	Record Sequence	1	REQUIRED. Must be a "3". Used to sequence the sectors making up a Service PAYEE Record.
2	Record Type	1	REQUIRED. Enter "B". Must be the second position of each PAYEE Record.
3–60	Blank	58	REQUIRED. Enter blanks.
61–66	Date Won	6	REQUIRED *FOR FORM W–2G ONLY*. Enter the date of the winning event in MMDDYY format. This is not the date the money was paid, if paid after the date of the race (or game). DO NOT ENTER HYPHENS OR SLASHES.
67–81	Transaction	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the ticket number, card number (and color, if applicable), machine serial number of any other information that will help identify the winning transaction. If no entry, enter blanks.
82–86	Race	5	REQUIRED *FOR FORM W–2G ONLY*. The race (or game) applicable to the winning ticket. If no entry, enter blanks.
87–91	Cashier	5	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the initials of the cashier and/or the window number making the winning payment. If no entry, enter blanks.
92–96	Window	5	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the location of the person paying the winnings. If no entry, enter blanks.
97–111	First ID	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the first identification number of the person receiving the winnings. If no entry, enter blanks.
112–126	Second ID	15	REQUIRED *FOR FORM W–2G ONLY*. If applicable, the second identification number of the person receiving the winnings. If no entry, enter blanks.
127–180	Blank	54	REQUIRED. Enter blanks.

SEC. 12. PAYEE "B" RECORD—RECORD LAYOUT FOR FORM W–2G

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)
FORM W-2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	FIRST PAYEE NAME LINE	SECOND PAYEE NAME LINE	BLANK
22–31	32–41	42–81	82–121	122–180

PAYEE "B" RECORD—RECORD LAYOUT (USING ONE PAYMENT AMOUNT FIELD)—Continued

FORM W-2G

ECTOR 2

RECORD SEQUENCE	RECORD TYPE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–71	72–73	74–82	83–180

ECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–60	61–66	67–81	82–86	87–91

SECTOR 3 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
92–96	97–111	112–126	127–180

PAYEE "B" RECORD—RECORD LAYOUT (USING TWO PAYMENT AMOUNT FIELDS)

FORM W–2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–91	92–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–60	61–66	67–81	82–86	87–91

SECTOR 3 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
92–96	97–111	112–126	127–180

PAYEE “B” RECORD—RECORD LAYOUT (USING THREE PAYMENT AMOUNT FIELDS)

FORM W-2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13–21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–101	102–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–180

SECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–60	61–66	67–81	82–86	87–91

SECTOR 3 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
92–96	97–111	112–126	127–180

PAYEE “B” RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)

FORM W-2G

SECTOR 1

RECORD SEQUENCE	RECORD TYPE	PAYMENT YEAR	DOCUMENT SPECIFIC CODE	BLANK	NAME CONTROL	TYPE OF TIN	TAXPAYER IDENTIFICATION NUMBER
1	2	3–4	5–6	7	8–11	12	13-21

SECTOR 1 (Continued)

PAYER'S ACCOUNT NUMBER FOR PAYEE	PAYMENT AMOUNT 1	PAYMENT AMOUNT 2	PAYMENT AMOUNT 3	PAYMENT AMOUNT 4	FIRST PAYEE NAME LINE	BLANK
22–31	32–41	42–51	52–61	62–71	72–111	112–180

SECTOR 2

RECORD SEQUENCE	RECORD TYPE	SECOND PAYEE NAME LINE	PAYEE MAILING ADDRESS	PAYEE CITY	PAYEE STATE	PAYEE ZIP CODE	BLANK
1	2	3–42	43–82	83–111	112–113	114–122	123–180

PAYEE "B" RECORD—RECORD LAYOUT (USING FOUR PAYMENT AMOUNT FIELDS)—Continued

FORM W-2G

ECTOR 3

RECORD SEQUENCE	RECORD TYPE	BLANK	DATE WON	TRANSACTION	RACE	CASHIER
1	2	3–60	61–66	67–81	82–86	87–91

ECTOR 3 (Continued)

WINDOW	FIRST ID	SECOND ID	BLANK
92–96	97–111	112–126	127–180

SEC. 13. END OF PAYER "C" RECORD

.01 The Control total fields have been expanded from 12 to 15 positions. Adjust your programs accordingly.

.02 The End of Payer "C" Record is a summary record for a type of return for a given payer.

.03 The "C" Record will contain the total number of payees and the totals of the payment amount fields filed by a given payer. The "C" Record must be written after the last Payee "B" Record for each type of return for a given payer. For each "A" Record and group of "B" Records on the file, there must be a corresponding "C" Record.

.04 In developing the "C" Record, for example, if you used Amount Codes 1, 3, and 6 in the "A" Record, the totals from the "B" Records will appear in Control Total 1, 2, and 3 of the "C" Record. Positions 53–142 would be zero filled and position 143–180 would be blank filled in this example.

.05 Payers/Transmitters must verify the accuracy of the totals in the "C" Record and must enter the totals on the transmittal, Form 4804 and 4802 or computer generated substitute, which will accompany the shipment. The lines used on Forms 4804 and 4802 to record payment amounts correspond with the Amount Codes used in the "A" Record. These forms have been updated for 1986.

RECORD NAME: END OF PAYER "C" RECORD

Mini-Disk Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "C".
2–7	Number of Payees	6	REQUIRED. Enter the total number of Payee "B" Records covered by the preceding Payer/Transmitter "A" Record. Right-justify and zero fill.
8–22	Control Total 1	15	REQUIRED. Please note that all Control Total fields have been expanded from 12 to 15 positions. Enter accumulated totals from payment amount 1. Right-justify and zero fill each Control Total amount. IF LESS THAN NINE AMOUNT FIELDS ARE BEING REPORTED, ZERO FILL UNUSED CONTROL TOTAL FIELDS.
	If any corresponding Payment Amount fields are present in the Payee "B" Records, accumulate into the appropriate Control Total field. ZERO FILL UNUSED CONTROL TOTAL FIELDS. Please note that all Control Total field have been expanded from 12 to 15 positions.		
23–37	Control Total 2	15	
38–52	Control Total 3	15	
53–67	Control Total 4	15	
68–82	Control Total 5	15	
83–97	Control Total 6	15	
98–112	Control Total 7	15	
113–127	Control Total 8	15	

RECORD NAME: END OF PAYER "C" RECORD—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
128–142	Control Total 9	15	
143–180	Blank	38	REQUIRED. Enter blanks.

SEC. 14. END OF PAYER "C" RECORD—RECORD LAYOUT

END OF PAYER "C" RECORD—RECORD LAYOUT

(Please note that all Control Total fields have been expanded from 12 to 15 positions.)

RECORD TYPE	NUMBER OF PAYEES	CONTROL TOTAL 1	CONTROL TOTAL 2	CONTROL TOTAL 3	CONTROL TOTAL 4	CONTROL TOTAL 5
1	2–7	8–22	23–37	38–52	53–67	68–82

CONTROL TOTAL 6	CONTROL TOTAL 7	CONTROL TOTAL 8	CONTROL TOTAL 9	BLANK
83–67	98–112	113–127	128–142	143–180

SEC. 15. STATE TOTALS "K" RECORD

.01 The Control Total fields have been expanded from 12 to 15 positions. Adjust your programs accordingly.

.02 The State Totals "K" Record is a summary for a given payer and a given state in the Combined Federal/State Filing Program, used ONLY when State Reporting approval has been granted.

.03 The "K" Record will contain the total number of payees and the totals of the payment amount fields filed by a given payer for a given state. The "K" Record(s) must be written after the "C" Record for the related "A" Record.

.04 There *must* be a separate "K" Record for *each state* being reported.

.05 Refer to Part A, Sec. 14 for the requirements and conditions that must be met to file on this program.

RECORD NAME: STATE TOTALS "K" RECORD

Mini-Disk Position	Field Title	Length	Description and Remarks
1	Record Type	1	REQUIRED. Enter "K".
2–7	Number of Payees	6	REQUIRED. Enter the total number of Payee "B" Records being coded for this state. Right-justify and zero fill.
8–22	Control Total 1	15	REQUIRED. Please note that all Control Total fields have been expanded from 12 to 15 positions. Enter accumulated total from Payment Amount 1. Right-justify and zero fill each Control Total amount. IF LESS THAN NINE AMOUNT FIELDS ARE BEING REPORTED, ZERO FILL UNUSED CONTROL TOTAL FIELDS.
	If any corresponding Payment Amount fields are present in the Payee "B" Records, accumulate into the appropriate Control Total field. ZERO FILL UNUSED CONTROL TOTAL FIELDS. Please note that all Control Total fields have been expanded from 12 to 15 positions.		
23–37	Control Total 2	15	
38–52	Control Total 3	15	
53–67	Control Total 4	15	
68–82	Control Total 5	15	
83–97	Control Total 6	15	
98–112	Control Total 7	15	

RECORD NAME: STATE TOTALS "K" RECORD—Continued

Mini-Disk Position	Field Title	Length	Description and Remarks
13–127	Control Total 8	15	
128–142	Control Total 9	15	
43–178	Blank	36	**REQUIRED. Reserved for IRS use. Enter blanks.**
179–180	State Code	2	**REQUIRED. Enter the code assigned to the state which is to receive the information. Refer to Part A, Sec. 14.10.**

EC. 16. STATE TOTALS "K" RECORD—RECORD LAYOUT

STATE TOTALS "K" RECORD—RECORD LAYOUT

Please note that all Control Total fields have been expanded from 12 to 15 positions.)

RECORD TYPE	NUMBER OF PAYEES	CONTROL TOTAL 1	CONTROL TOTAL 2	CONTROL TOTAL 3	CONTROL TOTAL 4	CONTROL TOTAL 5
1	2–7	8–22	23–37	38–52	53–67	68–82

CONTROL TOTAL 6	CONTROL TOTAL 7	CONTROL TOTAL 8	CONTROL TOTAL 9	BLANK	STATE CODE
83–97	98–112	113–127	128–142	143–178	179–180

EC. 17. END OF TRANSMISSION "F" ECORD

.01 The "F" Record is a summary of he number of payers and mini-disks in he entire file.

.02 This record should be written after he last "C" Record (or "K" Record, when pplicable) of the entire file.

END OF TRANSMISSION "F" RECORD

Mini-Disk Position	Field Title	Length	Description and Remarks
1	Record Type	1	**REQUIRED. Enter "F".**
2–5	Number of "A" Records	4	**REQUIRED. You may enter the total number of Payer/Transmitter "A" Records in this transmission. Right-justify and zero fill or enter all zeros.**
6–8	Number of Mini-Disks	3	**REQUIRED. You may enter the total number of mini-disks in this transmission. Right-justify and zero fill or enter all zeros.**
9–30	Zero	22	**REQUIRED. Enter zeros.**
31–180	Blank	150	**REQUIRED. Enter blanks.**

EC. 18. END OF TRANSMISSION "F" RECORD—RECORD LAYOUT

END OF TRANSMISSION "F" RECORD—RECORD LAYOUT

RECORD TYPE	NUMBER OF "A" RECORDS	NUMBER OF MINI-DISKS	ZERO	BLANK
1	2–5	6–8	9–30	31–180

PART B. BURROUGHS SUPER MINI-DISK II SPECIFICATIONS

SECTION I. GENERAL

.01 The Burroughs Super Mini-Disk II is a flexible mylar disk with an iron oxide coating. The disk is 8 inches (20.3 cm) in diameter with a 1.5 inch (3.8 cm) center hole.

.02 There is one Index Hole which is used to indicate the beginning of a track on each side of the disk.

.03 Recorded data is encoded using the Miller Frequency Mode (MFM) technique. Data transferred between the disk and the processor in *NOT* encoded in any way. Serial data is written to the disk in a 180-byte sector format.

.04 Maximum bit density is 71 bits per inch.

.05 Track density is 150 tracks per inch.

.06 Data bytes per sector are 180.

.07 Data sectors per track are 60.

.08 Surfaces per disks are 2.

.09 When initialling the mini-disk, the name IRSTAX should be assigned to the mini-disk.

.10 The file name in the, mini-disk header label should be FED-MINI.

SEC. 2—SEC. 18

See Super Mini-Disk Specifications contained in Part C of this Revenue Procedure.

Part IV. Items of General Interest

Special Rules Relating to Nuclear Decommissioning Costs—Public Hearing

Announcement 86–100

SUMMARY: This document provides notice of a public hearing on proposed regulations with respect to special rules relating to nuclear decommissioning costs.

DATES: The public hearing will be held on Wednesday, October 22, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Thursday, October 9, 1986.

ADDRESS: The public hearing will be held in the IRS Commissioner's Conference Room, Third Floor, Room 3313, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, ATTN: CC:LR:T (LR-18-85), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202-566-3935 (not a toll-free call).

SUPPLEMENTARY INFORMATION: The subject of the public hearing is proposed regulations under sections 88 and 468A of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Thursday, July 10, 1986 (51 FR 25070) [1986-31 I.R.B. 4].

The rules of §601.601 (a) (3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Thursday, October 9, 1986, an outline of oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

(Filed by the Office of the Federal Register on September 16, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 17, 1986, 51 F.R. 3292")

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Directory of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary,and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Ser vice:

Name	Address	Designation	Term of Suspension
Paul R. Beutler	Cold Spring, MN	Certified Public Accountant	Eighteen Months from August 13, 1986
Robert J. Sher	Hyattsville, MD	Attorney	Indefinite from August 22, 1986
Russell H. Strong	Breckinridge, TX	Certified Public Accountant	Indefinite from August 22, 1986
David G. Willemain	Towson, MD	Attorney	Indefinite from July 22, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent enrolled actuary, and the date of disba ment or period of suspension. This a nouncement will continue to appear in t weekly Bulletin for five successive wee for each attorney, certified public a countant, enrolled agent or enrolled a tuary so suspended or disbarred and w later be consolidated and published in t Cumulative Bulletin.

After due notice and opportunity f hearing, the following individual has be disbarred from further practice before t Internal Revenue Service:

Name	Address	Designation	Effective Date
Alton C. Bingham	Las Vegas, NV	Certified Public Accountant	August 16, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
DR—Donor.
E—Estate
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federral Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-118, page 4.
Public utility property; expensed for regulatory purposes, capitalized for tax purposes. The taxpayer does not violate the ratable flow-through requirements of section 46(f)(2) of the Code when for regulatory purposes it expenses the cost of inside wiring and, in the year of the expense, reduces cost of service by the full amount of the investment tax credit allowable with respect to the inside wiring.

Rev. Rul. 86-119, page 8.
Mineral production payments; advance for interest in unproven property. If an investor advances money to an oil and gas producer for the right to the lesser of twice the amount advanced or a certain percentage of net proceeds from the sale of hydrocarbons produced from a particular property, and the only indication that hydrocarbons will be produced from the property is favorable geological and geophysical studies, the advanced money will be treated as consideration for a royalty interest.

T.D. 8098, page 9.
Final regulations under section 6050I of the Code relate to the requirement of reporting cash in excess of $10,000 received in a trade or business.

T.D. 8100, page 5.
Amendments to the regulations under sections 170 and 501 of the Code relate to the treatment of certain cooperative hospital service organizations.

Announcement 86-101, page 14.
The Service will soon issue temporary regulations that will limit the ability of certain taxpayers to change accounting periods without obtaining prior approval of the Commissioner.

Announcement 86-103, page 16.
This Bulletin contains a list of organizations that no longer qualify as organizations contributions to which are deductible under section 170 of the Code.

EXEMPT ORGANIZATIONS

T.D. 8100, page 5.
Amendments to the regulations under sections 170 and 501 of the Code relate to the treatment of certain cooperative hospital service organizations.

Announcement 86-102, page 14.
A list is given of organizations now classified as private foundations.

Finding Lists begin on page 19.
Announcement of Disbarments and Suspensions on page 17.

Department of the Treasury
Internal Revenue Service

T22.23:

1986-41

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

T22.23:

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.

With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 46.—Amount of Credit

26 CFR 1.46–6: Limitations in case of certain regulated companies.
(Also Section 48; 1.48–1.)

Public utility property; expensed for regulatory purposes, capitalized for tax purposes. The taxpayer does not violate the ratable flow-through requirements of section 46(f)(2) of the Code when for regulatory purposes it expenses the cost of inside wiring and, in the year of the expense, reduces cost of service by the full amount of the investment tax credit allowable with respect to the inside wiring.

Rev. Rul. 86–118

ISSUE

If a telephone public utility taxpayer elected to account for investment credit under section 46(f)(2) of the Internal Revenue Code, are the ratable flow-through requirements of that section violated in a situation where, for regulatory purposes, the taxpayer expenses the cost of inside wiring and reduces the cost of service in that accounting period by the amount of investment tax credit allowable with respect to the inside wiring?

FACTS

The taxpayer is a public utility telephone company subject to the Federal Communications Commission (FCC) and the State *A* Public Service Commission (PSC). Taxpayer made a valid election to account for the investment tax credit (ITC) under a special rule for ratable flow-through as provided by section 46(f)(2) of the Internal Revenue Code (prior to 1975, this section was designated 46(e)(2)). This election has been consistently followed in maintaining taxpayer's regulated books of account and in determining utility rates.

On March 31, 1981, the FCC issued a rate order (effective October 1, 1981) that amended the Uniform System of Accounts. The order changed the accounting treatment of certain station connection costs previously capitalized in Account 232, Station Connections. As a result of this change, certain future station connection costs associated with inside wiring were no longer to be capitalized but were to be charged to Account 605, Installation and Repairs of Station Equipment, and expensed in the year incurred. State *A* PSC, pursuant to FCC procedure, issued a rate order requiring the taxpayer and other public utility telephone companies to change their accounting treatment of the cost of inside wiring for ratemaking purposes from capitalization to expensing.

Rev. Rul. 84–24, 1984–1 C.B. 89, considered a factual situation similar to that described above and found the inside wiring to be an identifiable asset with a useful life beyond the current year. That ruling therefore holds that the cost of the inside wiring must be capitalized under section 263 of the Code and recovered under the provisions of section 168.

In compliance with Rev. Rul. 84–24, the taxpayer capitalized the cost of inside wiring for federal tax purposes. As required, however, by the State *A* PSC, the taxpayer expensed these costs. The cost of service in the year of the expense was reduced by the ITC allowable with respect to those costs.

LAW AND ANALYSIS

Section 46(f)(1) of the Code provides a general rule that no credit will be allowed by section 38 for public utility property: (A) if the taxpayer's cost of service for ratemaking purposes is reduced by reason of any portion of the credit allowed by section 38; or (B) if the taxpayer's rate base is reduced for ratemaking purposes by reason of any portion of the credit allowable by section 38 and such reduction in rate base is not restored or is restored less rapidly than ratably.

Section 46(f)(2) of the Code provides a special rule that, if the taxpayer makes an election under section 46(f)(2), the general rule of section 46(f)(1) does not apply, but no credit will be allowed by section 38 with respect to any public utility property: (A) if the taxpayer's cost of service for ratemaking purposes or in its regulated books of account is reduced by more than a ratable portion of the credit allowable by section 38, or (B) if the taxpayer's rate base is reduced by reason of any portion of the credit allowable by section 38.

Section 46(f)(6) of the Code provides that for purposes of determining ratable portions, the period of time used in computing depreciation expense for purposes of reflecting operating results in the taxpayer's regulated books of account shall be used.

Section 1.46–6(g)(2) of the Income Tax Regulations provides that what is "ratable" is determined by considering the period of time actually used in computing the taxpayer's regulated depreciation expense for the property for which a credit is allowed. "Regulated depreciation expense" is the depreciation expense for the property used by a regulatory body for purposes of establishing the taxpayer's cost of service for ratemaking purposes.

Section 1.46–6(b)(2) of the regulations defines "cost of service" as the amount required by a taxpayer to provide regulated goods or services. Cost of service includes operating expenses (including salaries, cost of materials, etc.) maintenance expenses, depreciation expenses, tax expenses, and interest expenses.

Section 1.46–6(b)(3) of the regulations defines "rate base" as the monetary amount that is multiplied by a rate of return to determine the permitted return on investment.

As is stated above, Rev. Rul. 84–24 holds that the cost charged to the inside wiring account of a public telephone company is a capital expenditure under section 263 of the Code and must be recovered under section 168.

In accounting for the ITC under section 46(f)(2) of the Code, the utility's cost of service for ratemaking purposes may be reduced by no more than a ratable portion of the credit allowed by section 38. Section 1.46–6(g)(2) of the regulations provides that the "ratable" portion is determined by considering the period of time actually used in computing the depreciation expense for the property for the purpose of establishing the taxpayer's cost of service for ratemaking purposes. In the present situation, the requirement to expense the cost of inside wiring in the year incurred for ratemaking purposes is not a method of depreciation. Thus, for purposes of section 1.46–6(g)(2) it is not immediately obvious what period of time should be treated as being used in computing the taxpayer's regulated depreciation expense. However, the essence of ratable flow-through under the sections of Code and regulations cited above is to match the periods in which the ITC reduces cost of service with the periods in which cost of service is increased by the cost of the item that gives rise to the credit. This principle can be applied not only when the item is depreciated for regulatory purposes but also when it is expensed. Therefore, the ratable flow-through limitation is satisfied if the investment tax credit is used to reduce cost of service in the same period that cost of service is increased by expensing the item that gives rise to the credit. If the cost of service is increased for ratemaking purposes by the total cost of the item in the year the item is placed in service, the full amount of the ITC may be used to reduce the cost of service in that year. However, if less than the total cost of the item is expensed in a single year for ratemaking purposes, no more than a proportionate part of the full ITC for that item may be used to reduce the cost of service in that year.

HOLDING

The taxpayer does not violate the ratable flow-through requirements of section 46(f)(2) of the Code when for regulatory purposes it expenses the cost of inside wiring and, in the year of the expense, reduces cost of service by the full amount of ITC allowable with respect to the inside wiring.

Section 48.—Definitions; Special Rules

26 CFR 1.48–1: Definition of section 38 property.

Whether, if a telephone public utility taxpayer elected to account for investment credit under section 46(f)(2) of the Code, the ratable flow-through requirements of that section are violated where, for regulatory purposes, the taxpayer expenses the cost of inside wiring and reduces the cost of service in that accounting period by the amount of investment tax credit allowable with respect to the inside wiring. See Rev. Rul. 86–118, page 4.

Section 170.—Charitable, etc., Contributions and Gifts

26 CFR 1.170A–9: Definition of section 170(b)(1)(a) organization.
(Also Section 501; 1.501(e)–1.)

T.D. 8100

TITLE 26—INTERNAL REVENUE,—
CHAPTER I, SUBCHAPTER A,—
INCOME TAX PART I—INCOME TAX;
TAXABLE YEARS BEGINNING AFTER
DECEMBER 31, 1953; PART 602—
OMB CONTROL NUMBERS UNDER
THE PAPERWORK REDUCTION ACT

Cooperative Hospital Service Organizations

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the treatment of certain cooperative hospital service organizations. Changes to the applicable tax law were made by the Revenue and Expenditure Control Act of 1968 and by the Tax Reform Act of 1976. The final regulations provide the public with the guidance needed to comply with those Acts and affect organizations seeking to qualify for tax exempt status as organizations described in section 501(e).

DATES: The regulations are effective generally for taxable years ending after June 28, 1968. In the case of an organization performing clinical services, the regulations are effective for taxable years ending after December 31, 1976. However, pursuant to the grant of section 7805(b) relief, an organization that has received a ruling or determination letter recognizing it as exempt under section 501(e) has 120 days from the date of publication of these regulations in the FEDERAL REGISTER to conform its operations to the requirements of the regulations.

FOR FURTHER INFORMATION CONTACT: Sylvia F. Hunt or Harry Beker of the Employee Plans and Exempt Organizations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention CC:EE) (202–566–6212).

SUPPLEMENTAL INFORMATION: BACKGROUND

On January 11, 1984, the Internal Revenue Service published proposed regulations in the FEDERAL REGISTER to amend the Income Tax Regulations (26 CFR Part 1) under sections 170 and 501 of the Internal Revenue Code of 1954 (49 FR 1384) [1984–1 C.B. 559]. By notice published in the FEDERAL REGISTER on March 26, 1984 (49 FR 11186), the public was invited to comment orally upon the issues addressed in the proposals. A public hearing was held on May 31, 1984.

This document contains final regulations under sections 170(b)(1)(A) and 501(e). These regulations are issued to conform the regulations to section 109(a) of the Revenue and Expenditure Control Act of 1968 (82 Stat. 269) and section 1312(a) of the Tax Reform Act of 1976 (90 Stat. 1730) and are issued under the authority contained in section 7805 of the Code (68A Stat. 917; 26 USC 7805).

COMMENTS AND REVISIONS

After consideration of all comments received regarding the proposed regulations, those proposed regulations are adopted, as revised, by this Treasury decision.

Several comments indicated uncertainty as to the meaning of certain of the provisions in the proposed regulations and requested clarification of the positions announced. These recommendations have generally been adopted and are reflected in the final regulations. Thus, for example, an allocation will be deemed sufficient if it consists of bookkeeping entries and written notice to the patron-hospitals; retention of net earnings may be based on the reasonably anticipated needs of the organization; permissible sources of investment income (particularly with respect to rents) have been clarified; radiology services are specifically included within the term "clinical"; and the term "voting rights" of patron-hospitals has been defined.

Other comments recommended more extensive changes concerning accounting and operation practices. These changes, it was noted, would allow greater flexibility for cooperative hospital service organizations. Where these recommendations are neither contrary to the statutory language nor inconsistent with Congressional intent, they have been incorporated in the final regulations. Thus, for example, capital contributions have been excluded from the definition of "net earnings" and need not satisfy the allocation and payment rules; the status of membership dues and related membership assessments, gifts and grants has been clarified; certain income derived from sources that are incidental to the conduct of exempt purposes or functions has been deemed permissible; a section 501(e) organization may own stock in and receive dividends from certain public corporations where such ownership is a condition for obtaining credit; de minimis services to other than patron-hospitals where mandated by a governmental unit as a condition for operating in a particular jurisdiction, or for other reasons, has been deemed permissible; and the effective date provision has been modified for a period sufficient to permit organizations that have already been recognized as exempt under section 501(e) to modify their operations to bring them into conformance with the requirements of the final regulations.

Certain comments, however, recommended changes that would permit cooperative hospital service organizations to engage in practices that are either beyond the scope of or directly contrary to the statutory language of section 501(e). Those recommendations were also inconsistent with the holding of *HCSC—Laundry v. United States,* 450 US 1 (1981). Accordingly, the final regulations do not incorporate recommendations that would, for example, permit a section 501(e) organization to engage in unrelated trade or business so long as those activities do not become the organization's primary purpose; establish wholly owned for-profit subsidiaries; generally sell services to other than patron-hospitals; engage in any services which are identified by the organization as cost-effective if performed centrally; or pay dividends on the organization's capital stock.

Conforming changes are also made under §1.170A–9(c)(1) and §1.501(k)–1 of the Income Tax Regulations.

NONAPPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this Regulation is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

REGULATORY FLEXIBILITY ACT

The Internal Revenue Service has concluded that the regulations herein are interpretative and that the notice and public procedure requirements of 5 USC 553 do not apply. Accordingly, these regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 USC chapter 6).

PAPERWORK REDUCTION ACT

The collection of information requirements contained in this regulation has been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB under control number 1545–0814.

DRAFTING INFORMATION

The principal author of these regulations is Harry Beker of the Employee Plans and Exempt Organizations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * *

Adoption of amendments to the regulations

Accordingly, the amendments to 26 CFR Parts 1 and 602 published as a notice of proposed rulemaking in the FEDERAL REGISTER on January 11, 1984 (49 FR 1384) are hereby adopted, as amended, to read as follows:

Paragraph 1. The authority citation for part 1 continues to read as follows:

Authority: 26 U.S.C. 7805

Par. 2. Paragraph (c)(1) of §1.170A–9 is revised to read as follows:

§1.170A–9 Definition of section 170(b)(1)(A) organization.

* * * * *

(c) *Hospitals and medical research organizations*—(1) *Hospitals.* An organization (other than one described in subparagraph (2) of this paragraph) is described in section 170(b)(1)(A)(iii) if:

(i) It is a hospital, and

(ii) Its principal purpose or function is the providing of medical or hospital care or medical education or medical research.

The term "hospital" includes (A) Federal hospitals and (B) State, county, and municipal hospitals which are instrumentalities of governmental units referred to in section 170(c)(1) and otherwise come within the definition. A rehabilitation institution, outpatient clinic, or community mental health or drug treatment center may qualify as a "hospital" within the meaning of subdivision (i) of this subparagraph if its principal purpose or function is the providing of hospital or medical care. For purposes of this subdivision, the term "medical care" shall include the treatment of any physical or mental disability or condition, whether on an inpatient or outpatient basis, provided the cost of such treatment is deductible under section 213 by the person treated. An organization, all the accommodations of which qualify as being part of a "skilled nursing facility" within the meaning of 42 USC 1395x(j), may qualify as a "hospital" within the meaning of subdivision (i) of this subparagraph if its principal purpose or function is the providing of hospital or medical care. For taxable years ending after June 28, 1968, the term "hospital" also includes cooperative hospital service organizations which meet the requirements of section 501(e) and §1.501(e)–1. The term "hospital" does not, however, include convalescent homes or homes for children or the aged, nor does the term include institutions whose principal purpose or function is to train handicapped individuals to pursue some vocation. An organization whose principal purpose or function is the providing of medical education or medical research will not be considered a "hospital" within the meaning of subdivision (i) of this subparagraph, unless it is also actively engaged in providing medical or hospital care to patients on its premises or in its facilities, on an inpatient or outpatient basis, as an integral part of its medical education or medical research functions. See, however, subparagraph (2) of this paragraph with respect to certain medical research organizations.

* * * * *

Par. 3. Section 1.501(e)–1 is redesignated as §1.501(k)–1.

Par. 4. The following new section is added immediately after §1.501(d)–1:

§1.501(e)–1 Cooperative hospital service organizations.

(a) *General rule.* Section 501(e) is the exclusive and controlling section under which a cooperative hospital service organization can qualify as a charitable organization. A cooperative hospital service organization which meets the requirements of section 501(e) and this section shall be treated as an organization described in section 501(c)(3), exempt from taxation under section 501(a), and referred to in section 170(b)(1)(A)(iii) (relating to percentage limitations on charitable contributions). In order to qualify for tax exempt status, a cooperative hospital service organization must—

(1) Be organized and operated on a cooperative basis,

(2) Perform, on a centralized basis, only one or more specifically enumerated services which, if performed directly by a tax exempt hospital, would constitute activities in the exercise or performance of the purpose or function constituting the basis for its exemption, and

(3) Perform such service or services solely for two or more patron-hospitals as described in paragraph (d) of this section.

(b) *Organized and operated on a cooperative basis*— (1) *In general.* In order to meet the requirements of section 501(e), the organization must be organized and operated on a cooperative basis (whether or not under a specific statute on cooperatives) and must allocate or pay all of its net earnings within 8½ months after the close of the taxable year to its patron-hospitals on the basis of the percentage of its services performed for each patron. To "allocate" its net earnings to its patron-hospitals, the organization must make appropriate bookkeeping entries and provide timely written notice to each patron-hospital disclosing to the patron-hospital the amount allocated to it on the books of the organization. For the record-keeping requirements of a section 501(e) organization, see §1.521–1(a)(1).

(2) *Percentage of services defined.* The percentage of services performed for each patron-hospital may be determined on the basis of either the value or the quantity of the services provided by the organization to the patron-hospital, provided such basis is realistic in terms of the actual cost of the services to the organization.

(3) *Retention of net earnings.* Exemption will not be denied a cooperative hospital service organization solely because the organization, instead of paying all net earnings to its patron-hospitals, retains an amount for such purposes as retiring indebtedness, expanding the services of the organization, or for any other necessary purpose and allocates such amounts to its patrons. However, such funds may not be accumulated beyond the reasonably anticipated needs of the organization. See, §1.537–1(b). Whether there is an improper accumulation of funds depends upon the particular circumstances of each case. Moreover, where an organization retains net earnings for necessary purposes, the organization's records must show each patron's rights and interests in the funds retained. For purposes of this paragraph, the term "net earnings" does not include capital contributions to the organization and such contributions need not satisfy the allocation or payment requirements.

(4) *Nonpatronage and other income.* An organization described in section 501(e) may, in addition to net earnings, receive membership dues and related membership assessment fees, gifts, grants and income from nonpatronage sources such as investment of retained earnings. However, such an organization cannot be exempt if it engages in any business other than that of providing the specified services, described in paragraph (c), for the specified patron-hospitals, described in paragraph (d). Thus, an organization described in section 501(e) generally cannot have unrelated business taxable income as defined in section 512, although it may earn certain interest, annuities, royalties, and rents which are excluded from unrelated business taxable income because of the modifications contained in sections 512(b)(1), (2) or (3). An organization described in section 501(e) may, however, have debt-financed income which is treated as unrelated business taxable income solely because of the applicability of section 514. In addition, exempt status under section 501(e) will not be affected where rent from personal property leased with real property is treated as unrelated business taxable income under section 512(b)(3)(A)(ii) solely because the rent attributable to the personal property is more than incidental or under section 512(b)(3)(B)(i) solely because the rent attributable to the personal property exceeds 50 percent of the total rent received or accrued under the lease. Exemption will not be affected solely because the determination of the amount of rent depends in whole or in part on the income or profits derived from the property leased. See, section 512(b)(3)(B))(ii). An organization described in section 501(e) may also derive nonpatronage income from sources that are incidental to the conduct of its exempt purposes or functions. For example, income derived from the operation of a cafeteria or vending machines primarily for the convenience of its employees or the disposition of by-products in substantially the same state they were in on completion of the exempt function (e.g., the sale of silver waste produced in the processing of x-ray film) will not be considered unrelated business taxable income. See, section 513(a)(2) and §1.513–1(d)(4)(ii). The nonpatronage and other income permitted under this subparagraph (4) must be allocated or paid as provided in subparagraph (1) or retained as provided in subparagraph (3).

(5) *Stock ownership*—(i) *Capital stock of organization.* An organization does not meet the requirements of section 501(e) unless all of the organization's outstanding capital stock, if there is such stock, is held solely by its patron-hospitals. However, no amount may be paid as dividends on the capital stock of the organization. For purposes of the preceding sentence, the term "capital stock" includes common stock (whether voting or nonvoting), preferred stock, or any other form evidencing a proprietary interest in the organization.

(ii) *Stock ownership as a condition for obtaining credit.* If by statutory requirement a cooperative hospital service organization must be a shareholder in a United States or state chartered corporation as a condition for obtaining credit from that corporate-lender, the ownership of shares and the payment of dividends thereon will not for such reason be a basis for the denial of exemption to the organization. See, e.g., National Consumer Cooperative bank, 12 USC §3001 et seq.

(c) *Scope of services*—(1) *Permissible services.* An organization meets the requirements of section 501(e) only if the organization performs, on a centralized basis, one or more of the following services and only such services: data processing, purchasing (including the purchasing and dispensing of drugs and pharmaceuticals to patron-hospitals), warehousing, billing and collection, food, clinical (including radiology), industrial engineering (including the installation, maintenance and repair of biomedical and similar equipment), laboratory, printing, communications, record center, and personnel (including recruitment, selection, testing, training, education and placement of personnel) services. An organization is not described in section 501(e) if, in addition to or instead of one or more of these specified services, the organization performs any other service (other than services referred to under paragraph (b)(4) that are incidental to the conduct of exempt purposes or functions).

(2) *Illustration.* The provisions of this subparagraph may be illustrated by the following example.

Example. An organization performs industrial engineering services on a cooperative basis solely for patron-hospitals each of which is an organization described in section 501(c)(3) and exempt from taxation under section 501(a). However, in addition to this service, the organization operates laundry services for its patron-hospitals. This cooperative organization does not meet the requirements of this paragraph because it performs laundry services not specified in this paragraph.

(d) *Patron-hospitals*—(1) *Defined.* Section 501(e) only applies if the organization performs its services solely for two or more patron-hospitals each of which is—

(i) An organization described in section 501(c)(3) which is exempt from taxation under section 501(a),

(ii) A constituent part of an organization described in section 501(c)(3) which is exempt from taxation under section 501(a) and which, if organized and operated as a separate entity, would constitute an organization described in section 501(c)(3), or

(iii) Owned and operated by the United States, a State, the District of Columbia, or a possession of the United States, or a political subdivision or an agency or instrumentality of any of the foregoing.

(2) *Business with nonvoting patron-hospitals*. Exemption will not be denied a cooperative hospital service organization solely because the organization (whether organized on a stock or membership basis) transacts business with patron-hospitals which do not have voting rights in the organization and therefore do not participate in the decisions affecting the operation of the organization. Where the organization has both patron-hospitals with voting rights and patron-hospitals without such rights, the organization must provide at least 50 percent of its services to patron-hospitals with voting rights in the organization. Thus, the percentage of services provided to nonvoting patrons may not exceed the percentage of such services provided to voting patrons. A patron-hospital will be deemed to have voting rights in the cooperative hospital service organization if the patron-hospital may vote directly on matters affecting the operation of the organization or if the patron-hospital may vote in the election of cooperative board members. Notwithstanding that an organization may have both voting and nonvoting patron-hospitals, patronage refunds must nevertheless be allocated or paid to all patron-hospitals solely on the basis specified in paragraph (b) of this section.

(3) *Services to other organizations*. An organization does not meet the requirements of section 501(e) if, in addition to performing services for patron-hospitals (entities described in subdivisions (i), (ii) or (iii) of subparagraph (1)), the organization performs any service for any other organization. For example, a cooperative hospital service organization is not exempt if it performs services for convalescent homes for children or the aged, vocational training facilities for the handicapped, educational institutions which do not provide hospital care in their facilities, and proprietary hospitals. However, the provision of the specified services between or among cooperative hospital service organizations meeting the requirements of section 501(e) and this section is permissible. Also permissible is the provision of the specified services to entities which are not patron-hospitals, but only if such services are de minimis and are mandated by a governmental unit as, for example, a condition for licensing.

(e) *Effective dates*. An organization, other than an organization performing clinical services, may meet the requirements of section 501(e) and be a tax exempt organization for taxable years ending after June 28, 1968. An organization performing clinical services may meet the requirements of section 501(e) and be a tax exempt organization for taxable years ending after December 31, 1976. However, pursuant to the authority contained in section 7805(b) of the Internal Revenue Code, these regulations shall not become effective with respect to an organization which has received a ruling or determination letter from the Internal Revenue Service recognizing its exemption under section 501(e) January 2, 1987.

Par. 5. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805

Par. 6. Section 602.101(c) is amended by inserting the following item in the appropriate place in the table:

§ 1.501(e)–1 1545–0814

This Treasury decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954, (68A Stat. 917; 26 USC 7805).

Roscoe A. Egger, Jr.
Commissioner of
Internal Revenue.

Approved August 15, 1986.

J. Roger Mentz,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on September 3, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 4, 1986, 51 F.R. 31613)

Section 501.—Exemption from Tax on Corporations, Certain Trusts, etc.

26 CFR 1.501(e)–1: Cooperative hospital service organizations.

Whether a cooperative hospital service organization can qualify as a charitable organization. See T.D. 8100, page 5.

Section 636.—Income Tax Treatment of Mineral Production Payments

26 CFR 1.636–3: Definitions.

Mineral production payments; advance for interest in unproven property. If an investor advances money to an oil and gas producer for the right to the lesser of twice the amount advanced or a certain percentage of net proceeds from the sale of hydrocarbons produced from a particular property, and the only indication that hydrocarbons will be produced from the property is favorable geological and geophysical studies, the advanced money will be treated as consideration for a royalty interest.

Rev. Rul. 86–119

ISSUE

If an investor advances money to an oil and gas producer for the right to the lesser of (a) twice the amount advanced or (b) *y* percent of the net proceeds from the sale of any hydrocarbons that are produced from a leased area that is not yet producing hydrocarbons, is the money treated, for federal income tax purposes, as consideration for a production payment or as consideration for a royalty interest? The answer to this question is determined by whether favorable geological and geophysical studies (G&G), in the absence of other facts that indicate the presence of oil or gas, such as adjacent hydrocarbon production, can be sufficient to underlie a reasonable expectation that no less than a specified sum will be paid out before the expiration of the lease.

FACTS

Z, an oil and gas producer, owns an undivided operating interest in a non-producing oil and gas lease on the continental shelf. *Z* believes, on the basis of geological and geophysical studies, that there is a high probability of finding hydrocarbons under the leased area. Aside from these studies, there are no factors indicating the presence of oil or gas. No exploratory wells have been drilled on the subject lease, nor have any successful exploratory wells been drilled on adjacent tracts.

Z entered into an agreement with Investor *A*, who advanced 10*x* dollars to *Z*, none of which was pledged for development of the property. *Z* will reimburse *A* by paying *A* *y* percent of the net monthly proceeds accruinng to *Z* from the sale of any hydrocarbons that are produced from the leased area until 20*x* dollars is received by *A*. No other reimbursement will be made to *A*.

LAW AND ANALYSIS

Section 636(a) of the Internal Revenue Code provides, generally, that a production payment carved out of mineral property will be treated, for income tax purposes, as if it were a mortgage loan on the property and will not qualify as an economic interest in the mineral property.

Section 1.636–3(a)(1) of the Income Tax Regulations provides that the term "production payment" means, in general, a right to a specified share of the production from mineral in place (if, as, and when produced), or the proceeds from such production. Such right must have an expected economic life (at the time of its creation) of shorter duration than the economic life of one or more of the mineral properties burdened thereby. A right to mineral in place has an economic life of shorter duration than the economic life of a mineral property burdened thereby only if such right may not reasonably be expected to extend in substantial amounts over the entire productive life of such mineral property. A production payment may be limited by a dollar amount, a quantum of mineral, or a period of time.

United States v. Morgan, 321 F.2d 781 (5th Cir. 1963), considered a retained right to a sum of money that was payable solely out of a specified percentage of mineral produced from a mineral property. The court held that such a right constitutes a production payment only if (1) an ordinarily prudent person dealing in mineral lands and leases could reasonably expect, at the time of creation of the right, that the specified sum will be paid out before the expiration of the lease, and (2) at the time of the creation of the right, the person retaining the right had such an expectation. Otherwise, the retained right is a royalty.

United States v. Foster, 324 F.2d 702 (5th Cir. 1963), held that, in appropriate circumstances, such expectation can reasonably be formed even though the burdened property is not yet producing any minerals. Although the burdened property at issue in that case was nonproducing, there was production on adjoining property, and 11.11 acres of adjoining property were included in a producing unit established by the Louisiana Commission of Conservation. The court found that it could have been, and must have been, predicted with reasonable accuracy at the time the retained right in that case was created that the right would be paid out before exhaustion of the burdened property. The court, therefore, concluded that the retained right was an oil payment and not a royalty.

In the instant case, no oil or gas had been found on the leased area or the adjacent tracts. When *A*'s right to proceeds from the production and sale of hydrocarbons was created, there were no factors (other than favorable geological and geophysical studies) that indicated the presence of oil or gas. Therefore, it could not have been reasonably expected that the specified sum of 20*x* dollars would be paid out before expiration of the lease. In light of the degree of uncertainty that still attaches to predictions based solely on geological and geophysical studies, *Z* cannot demonstrate that the right to proceeds conveyed to *A* was, at the time of its creation, reasonably expected to have an economic life of shorter duration than the economic life of the burdened mineral property. See ***Morgan***. Thus, the economic life requirement of section 1.636–3(a) of the regulations is not met. The present case is distinguishable from *Foster* because in *Foster* there was production on property adjoining the burdened property. Accordingly, *A*'s right to proceeds cannot be treated as a production payment.

HOLDING

The money advanced to *Z* for the right to *y* percent of the net proceeds from the sale of any hydrocarbons that are produced from the leased area described above is, for federal income tax purposes, consideration for sale of a royalty interest.

Section 6051I—Returns Relating to Cash Received in a Trade or Business

26 CFR 1.6051I–1: Returns relating to cash in excess of $10,000 received in a trade or business.

T.D. 8098

TITLE 26.—INTERNAL REVENUE SERVICE—CHAPTER I, SUBCHAPTER A, PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953
PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Returns Relating To Cash Payments In Excess of $10,000 Received In A Trade or Business

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the requirement of reporting cash in excess of $10,000 received in a trade or business. Changes to the applicable law were made by the Tax Reform Act of 1984. The regulations affect any person who, in the course of a trade or business in which such person is engaged, receives cash in excess of $10,000 in 1 transaction (or 2 or more related transactions). The regulations provide these persons with the guidance necessary to comply with the law.

DATES: The regulations apply to cash payments received after December 31, 1984.

FOR FURTHER INFORMATION CONTRACT: Arthur E. Davis of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T), 202-566-3238, not a toll-free call.

SUPPLEMENTARY INFORMATION: BACKGROUND

On May 23, 1985, the FEDERAL REGISTER published temporary regulations (T.D. 8025; 50 FR 21239) [1985–1 C.B. 348] and proposed amendments (50 FR 21308) to the Income Tax Regulations (26 CFR Part 1) under section 6050I of the Internal Revenue Code of 1954. These amendments were proposed to conform the regulations to section 146 of the Tax Reform Act of 1984 (P.L. 98–369, 98 Stat. 685). Twenty-eight written comments responding to this notice were received.

On September 19, 1985, a public hearing concerning these proposed regulations was held. Nine commentators spoke at this hearing. After consideration of all written comments and oral comments received at the public hearing regarding the proposed amendments those amendments are adopted as revised by this Treasury decision.

PUBLIC COMMENTS

Section 6050I provides that an information return must be made by any person engaged in a trade or business who receives, in the course of that trade or business, cash in excess of $10,000 in 1 transaction (or 2 or more related transactions). Several comments were received suggesting that an exception to the reporting requirements be established for attorney's fees. Because section 6050I and the legislative history to section 6050I make no provision for an exception of this type, the final regulations do not adopt the suggestion.

Several commentators requested that the regulations provide that each betting window at a pari-mutuel racetrack be considered a separate recipient for purposes of the reporting requirement. The proposed regulations included a rule which generally reached that result. The final regulations clarify this rule by adding an example illustrating that betting windows at a pari-mutuel racetrack are separate recipients if in the ordinary course of business the operator of each betting window does not have reason to know the identity of persons making wagers at other betting windows.

Question and answer 12 of the proposed regulations provided rules for reporting multiple cash payments relating to the same transaction. The final regulations adopt those rules without change. However, because of compliance concerns, the Internal Revenue Service is considering amending those rules to require, under the authority of section 6050I(b)(2)(D), reporting of the total amount of cash paid in multiple payments relating to the same transaction. If the Service issues a rule requiring the reporting of the total amount of cash in a transaction, the rule will apply prospectively only and there will be an opportunity for public comment on the rule.

SPECIAL ANALYSIS

Although a notice of proposed rulemaking soliciting public comments was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these regulations are not subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6). The Treasury Department has determined that these final regulations are not major rules under Executive Order 12291 or the Treasury and OMB implementation of the Order dated April 29, 1983. Accordingly, a Regulatory Impact Analysis is not required.

PAPERWORK REDUCTION ACT

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget ("OMB") in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB.

DRAFTING INFORMATION

The principal author of these regulations is Bruce H. Jurist of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, other personnel in the Internal Revenue Service and Treasury Department participated in developing the regulations on matters of both substance and style.

* * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 1 and Part 602 are amended as follows:

INCOME TAX REGULATIONS
(26 CFR Part 1)

Paragraph 1. The authority for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805 * * * Section 1.6050I–1 also issued under 26 U.S.C. 6050I.

Par. 2. The following new §1.6050I–1 shall be added at the appropriate place.

§1.6050I–1 Returns relating to cash in excess of $10,000 received in a trade or business.

(a) *Reporing requirement*—(1) *In genera.*. Any person (as defined in section 7701(a)(1)) who, in the course of a trade or business in which such person is engaged, receives cash in excess of $10,000 in 1 transaction (or 2 or more related transactions) shall, except as otherwise provided, make a return of information with respect to the receipt of cash.

(2) *Cash received for the account of another*. Cash in excess of $10,000 received by a person for the account of another must be reported under this section. Thus, for example, a person who collects delinquent accounts receivable for an automobile dealer must report with respect to the receipt of cash in excess of $10,000 from the collection of a particular account even though the proceeds of the collection are credited to the account of the automobile dealer (*i.e.*, where the rights to the proceeds from the account are retained by the automobile dealer and the collection is made on a fee-for-service basis).

(3) *Cash received by agents*—(i) *General rule*. Except as provided in paragraph (a)(3)(ii) of this section, a person who in the course of a trade or business acts as an agent (or in some other similar capacity) and receives cash in excess of $10,000 from a principal, must report the receipt of cash under this section.

(ii) *Exception*. An agent who receives cash from a principal and uses all of the cash within 15 days in a cash transaction (the "second cash transaction") which is reportable under section 6050I or section 5312 of Title 31 of the United States Code and the regulations thereunder (31 CFR Part 103), and who discloses the name, address, and taxpayer identification number of the principal to the recipient in the second cash transaction need not report the initial receipt of cash under this section. An agent will be deemed to have met the disclosure requirements of this paragraph (a)(3)(ii) if the agent discloses only the name of the principal and the agent knows that the recipient has the principal's address and taxpayer identification number.

(iii) *Example*. The following example illustrates the application of the rules in paragraphs (a)(3)(i) and (ii) of this section:

Example. B, the principal, gives D, an attorney, $75,000 in cash to purchase real property on behalf of B. Within 15 days D purchases real property for cash from E, a real estate developer, and discloses to E, B's name, address, and taxpayer identification number. Because the transaction qualifies for the exception provided in paragraph (a)(3)(ii) of this section, D need not report with respect to the initial receipt of cash under this section. The exception does not apply, however, if D pays E by means other than cash, or effects the purchase more than 15 days following receipt of the cash from B, or fails to disclose B's name, address, and taxpayer identification number (assuming D does not know that E already has B's address and taxpayer identification number), or purchases the property from a person whose sale of the property is not in the course of that person's trade or business. In any such case, D is required to report the receipt of cash from B under this section.

(b) *Multiple payments*. The receipt of cash deposits or cash installment payments (or other similar payments or prepayments) relating to a single transaction (or two or more related transactions) are reported under this section in different manners depending on the dollar amounts of the initial and subsequent payments. Reporting of multiple payments is effected as follows:

(1) *Initial and subsequent payments in excess of $10,000*. If the initial payment exceeds $10,000 and any subsequent payment exceeds $10,000, the recipient must report each payment that exceeds $10,000. These payments must be reported separately (or if the payments are made less than 15 days apart, the recipient may (if it so elects) make a single report with respect to such payments).

(2) *Initial payment only in excess of $10,000*. If the initial payment exceeds $10,000 but no subsequent payment exceeds $10,000, the recipient must report

with respect to the initial $10,000 payment (within 15 days of receipt of the initial payment), but need not report with respect to any subsequent payment.

(3) *Initial payment of $10,000 or less*. If the initial payment does not exceed $10,000, the recipient must aggregate the initial payment and subsequent payments made within one year of the initial payment until such aggregate amount exceeds $10,000, and report with respect to the aggregate amount within 15 days after receipt of the payment that causes the aggregate amount to exceed $10,000. Any subsequent payment which by itself exceeds $10,000 must be separately reported.

(c) *Meaning of terms*. The following definitions apply for purposes of this section—

(1) The term "cash" means the coin and currency of the United States or of any other country, which circulate in and are customarily used and accepted as money in the country in which issued. Cash includes United States notes and Federal Reserve notes, but does not include bank checks, travelers checks, bank drafts, wire transfers or other negotiable or monetary instruments not customarily accepted as money.

(2) The term "trade or business" has the same meaning as under section 162 of the Internal Revenue Code of 1954.

(3)(i) The term "transaction" means the underlying event precipitating the payer's transfer of cash to the recipient. Transactions include (but are not limited to) a sale of goods or services; a sale of real property; a sale of intangible property; a rental of real or personal property; an exchange of cash for other cash; the establishment or maintenance of or contribution to a custodial, trust, or escrow arrangement; a payment of a preexisting debt; a conversion of cash to a negotiable instrument; a reimbursement for expenses paid; or the making or repayment of a loan. A transaction may not be divided into multiple transactions in order to avoid reporting under this section.

(ii) The term "related transactions" means any transaction conducted between a payer (or its agent) and a recipient of cash in a 24-hour period. Additionally, transactions conducted between a payer (or its agent) and a cash recipient during a period of more than 24 hours are related if the recipient knows or has reason to know that each transaction is one of a series of connected transactions.

(iii) The following examples illustrate the definition of paragraphs (c)(3)(i) and (ii).

Example (1). A person has a tacit agreement with a gold dealer to purchase $36,000 in gold bullion. The $36,000 purchase represents a single transaction under paragraph (c)(3)(i) of this section and the reporting requirements of this section cannot be avoided by recasting the single sales transaction into 4 separate $9,000 sales transactions.

Example (2). An attorney agrees to represent a client in a criminal case with the attorney's fee to be determined on an hourly basis. In the first month in which the attorney represents the client, the bill for the attorney's services comes to $8,000 which the client pays in cash. In the second month in which the attorney represents the client, the bill for the attorney's services comes to $4,000, which the client again pays in cash. The aggregate amount of cash paid ($12,000) relates to a single transaction as defined in paragraph (c)(3)(i) of this section, the sale of legal services relating to the criminal case, and the receipt of cash must be reported under this section.

Example (3). A person intends to contribute a total of $45,000 to a trust fund, and the trustee of the fund knows or has reason to know of that intention. The $45,000 contribution is a single transaction under paragraph (c)(3)(i) of this section and the reporting requirement of this section cannot be avoided by the grantor's making five separate $9,000 cash contributions to a single fund or by making five $9,000 cash contributions to five separate funds administered by a common trustee.

Example (4). K, an individual, attends a one day auction and purchases for cash two items, at a cost of $9,240 and $1,732.50 respectively (tax and buyer's premium included). Because the transactions are related transactions as defined in paragraph (c)(3)(ii) of this section, the auction house is required to report the aggregate amount of cash received from the related sales ($10,972.50), even though the auction house accounts separately on its books for each item sold and presents the purchaser with separate bills for each item purchased.

Example (5). F, a coin dealer, sells for cash $9,000 worth of gold coins to an individual on three successive days. Under paragraph (c)(3)(ii) of this section the three $9,000 transactions are related transactions aggregating $27,000 if F knows, or has reason to know, that each transaction is one of a series of connected transactions.

(4)(i) The term "recipient" means the person receiving the cash. Except as provided in paragraph (c)(4)(ii) of this section, each store, division, branch, department, headquarters, or office ("branch") (regardless of physical location) comprising a portion of a person's trade or business shall for purposes of this section be deemed a separate recipient.

(ii) A branch that receives cash payments will not be deemed a separate recipient if the branch (or a central unit linking such branch with other branches) would in the ordinary course of business have reason to know the identity of payers making cash payments to other branches of such person.

(iii) *Examples*. The following examples illustrate the application of the rules in paragraphs (c)(4)(i) and (ii) of this section:

Example (1). N, an individual, purchases regulated futures contracts at a cost of $7,500 and $5,000, respectively, through two different branches of Commodities Broker X on the same day. N pays for each purchase with cash. Each branch of Commodities Broker X transmits the sales information regarding each of N's purchases to a central unit of Commodities Broker X (which settles the transactions against N's account). Under paragraph (c)(4)(ii) of this section the separate branches of Commodities Broker X are not deemed to be separate recipients; therefore. Commodities Broker X must report with respect to the two related regulated futures contracts sales in accordance with this section.

Example (2). P, a corporation, owns and operates a racetrack. P's racetrack contains 100 betting windows at which pari-mutuel wagers may be made. R, an individual, places cash wagers of $3,000 each at five separate betting windows. Assuming that in the ordinary course of business each betting window (or a central unit linking windows) does not have reason to know the identity of persons making wagers at other betting windows, each betting window would be deemed to be a separate cash recipient under paragraph (c)(4)(i) of this section. As no individual recipient received cash in excess of $10,000, no report need be made by P under this section.

(d) *Exceptions to the reporting requirements of section 6050I*—(1) *Receipt of cash by certain financial institutions*. A financial institution as defined in subparagraphs (A), (B), (C), (D), (E), (F), (G), (J), (K), (R), and (S) of section 5312(a)(2) of Title 31, United States code is not required to report the receipt of cash exceeding $10,000 under section 6050I.

(2) *Receipt of cash by certain casinos having gross annual gaming revenue in excess of $10,000,000*. (i) *In general*. If a casino receives cash in excess of $10,000 and is required to report the receipt of such cash directly to the Treasury Department under 31 CFR 103.22(a)(2) and 103.25 and is subject to the recordkeeping requirements of 31 CFR 103.36, then the casino is not required to make a return with respect to the receipt of such cash under section 6050I and these regulations.

(ii) *Casinos exempt under 31 CFR 103.45(c)*. Under the authority of section 6050I(c)(1)(A), the Secretary may exempt from the reporting requirements of section 6050I casinos with gross annual gaming revenue in excess of $1,000,000 that are exempt under 31 CFR 103.45(c) from reporting certain cash transactions to the Treasury Department under 31 CFR 103.22(a)(2) and 103.25. The determination whether a casino which is granted an exemption under 31 CFR section 103.45(c) will be required to report under section 6050I will be made on a case by case basis, concurrently with the granting of such an exemption.

(iii) *Reporting of cash received in a nongaming business.* Nongaming businesses (such as shops, restaurants, entertainment, and hotels) at casino hotels and resorts are separate trades or businesses in which the receipt of cash in excess of $10,000 is reportable under section 6050I and these regulations. Thus, a casino exempt under paragraph (d)(2)(i) or (ii) of this section must report with respect to cash in excess of $10,000 received in its nongaming businesses.

(iv) *Example.* The following example illustrates the application of the rules in paragraphs (d)(2)(i) and (iii) of this section:

Example. A and B are casinos having gross annual gaming revenue in excess of $1,000,000. C is a casino with gross annual gaming revenue of less than $1,000,000. Casino A receives $15,000 in cash from a customer with respect to a gaming transaction which the casino reports to the Treasury Department under 31 CFR 103.22(a)(2) and 103.25. Casino B receives $15,000 in cash from a customer in payment for accommodations provided to that customer at Casino B's hotel. Casino C receives $15,000 in cash from a customer with respect to a gaming transaction. Casino A is not required to report the transaction under section 6050I or these regulations because the exception for certain casinos provided in paragraph (d)(2)(i) ("the casino exception") applies. Casino B is required to report under section 6050I and these regulations because the casino exception does not apply to the receipt of cash from a nongaming activity. Casino C is required to report under section 6050I and these regulations because the casino exception does not apply to casinos having gross annual gaming revenue of $1,000,000 or less which do not have to report to the Treasury Department under 31 CFR 103.22(a)(2) and 103.25.

(3) *Receipt of cash not in the course of the recipient's trade or business.* The receipt of cash in excess of $10,000 by a person other than in the course of the person's trade or business is not reportable under section 6050I. Thus, for example, F, an individual in the trade or business of selling real estate, sells a motorboat for $12,000, the purchase price of which is paid in cash. F did not use the motorboat in any trade or business in which F was engaged. F is not required to report under section 6050I or these regulations because the exception provided in this paragraph (d)(3) applies.

(4) *Receipt is made with respect to a foreign cash transaction*—(i) *In general.* Generally, there is no requirement to report with respect to a cash transaction if the entire transaction occurs outside the United States (the fifty states and the District of Columbia). An entire transaction consists of both the transaction as defined in paragraph (c)(3)(i) of this section and the receipt of cash by the recipient. If, however, any part of an entire transaction occurs in the Commonwealth of Puerto Rico or a possession or territory of the United States and the recipient of cash in that transaction is subject to the general jurisdiction of the Internal Revenue Service under Title 26 of the United States Code, the recipient is required to report the transaction under this section.

(ii) *Example.* The following example illustrates the application of the rules in paragraph (d)(4)(i) of this section:

Example. W, an individual engaged in the trade or business of selling aircraft, reaches an agreement to sell an airplane to a U.S. citizen living in Mexico. The agreement, no portion of which is formulated in the United States, calls for a purchase price of $125,000 and requires delivery of and payment for the airplane to be made in Mexico. Upon delivery of the airplane in Mexico, W receives $125,000 in cash. W is not required to report under section 6050I or these regulations because the exception provided in paragraph (d)(4)(i) of this section ("foreign transaction exception") applies. If, however, any part of the agreement to sell had been formulated in the United States, the foreign transaction exception would not apply and W would be required to report the receipt of cash under section 6050I and these regulations.

(e) *Time, manner, and form of reporting*—(1) *Time of reporting.* The reports required by paragraph (a) of this section must be filed with the Internal Revenue Service by the 15th day after the date the cash is received. If a person elects to report as one payment several independently reportable payments received within a 15-day period (as described in paragraph (b)(1) of this section), the report must be filed with the Internal Revenue Service by the 15th day after the date the initial payment is received.

(2) *Form of reporting.* A report required by paragraph (a) of this section must be made on Form 8300. A return of information made in compliance with this paragraph must contain the name, address, and taxpayer identification number of the person from whom the cash was received; the name, address, and taxpayer identification number of the person on whose behalf the transaction was conducted (if the recipient knows or has reason to know that the person from whom the cash was received conducted the transaction as an agent for another person); the amount of cash received; the date and nature of the transaction; and any other information required by Form 8300. Form 8300 can be obtained from any Internal Revenue Service Forms Distribution Center.

(3) *Manner of reporting*—(i) *Where to file.* A person making a return of information under this section must file Form 8300 by mailing it to the address shown in the instructions to the form.

(ii) *Verification.* A person making a return of information under this section must verify the identity of the person from whom the reportable cash is received. Verification of the identity of a person who purports to be an alien must be made by examination of such person's passport, alien identification card, or other official document evidencing nationality or residence. Verification of the identity of any other person may be made by examination of a document normally acceptable as a means of identification when cashing or accepting checks (for example, a driver's license or a credit card). In addition, a return will be considered incomplete if the person required to make a return knows (or has reason to know) that an agent is conducting the transaction for a principal, and the return does not identify both the principal and the agent.

(iii) *Retention of returns.* A person required to make an information return under this section must keep a copy of each return filed for five years from the date of filing.

(f) *Requirement of furnishing statements*—(1) *In general.* Any person required to make an information return under this section must furnish a single, annual, written statement to each person whose name is set forth in a return ("identified person") filed with the Internal Revenue Service.

(2) *Form of statement.* The statement required by the preceding paragraph need not follow any particular format, but it must contain the following information:

(i) The name and address of the person making the return;

(ii) The aggregate amount of reportable cash received by the person who made the information return required by this section during the calendar year in all cash transactions relating to the identified person; and

(iii) A legend stating that the information contained in the statement is being reported to the Internal Revenue Service.

(3) *When statement is to be furnished.* Statements required under this paragraph (f) must be furnished to an identified person on or before January 31 of the year following the calendar year in which the cash is received. A statement shall be considered to be furnished to an identified person if it is mailed to the identified person at the identified person's last known address.

(g) *Cross-reference to penalty provisions*—(1) *Failure to file information return*. Any person who fails to make a return under section 6050I and paragraph (a) of these regulations shall be subject to the penalties provided in section 6652.

(2) *Failure to furnish statement*. Any person who fails to furnish any statement to identified persons under section 6050I and paragraph (f) of these regulations shall be subject to the penalties provided in section 6678.

(3) *Criminal penalties*. Any person who willfully fails to make a return under section 6050I and these regulations may be subject to criminal prosecution.

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

(26 CFR Part 602)

Par. 3. The authority citation for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. Section 602.101 (c) is amended by inserting in the appropriate place in the table "§1.6050I-1 * * * 1545-0892".

James I. Owens,
Acting Commissioner
of Internal Revenue.

Approved July 21, 1986.

J. Roger Mentz,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on September 3, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 4, 1986, 51 F.R. 31610)

Part IV. Items of General Interest

Limitation on Certain Changes of Annual Accounting Period

Announcement 86–101[1]

Legislation currently is pending that, if enacted, would revise substantially the federal income tax system. The Internal Revenue Service is concerned that certain taxpayers may attempt to change their annual accounting period in order to defer the application of certain provisions of that legislation. The Service also is concerned that certain pass-through entities (or investors in those entities) may attempt to change to a 52–53 week year in order to defer income to a year in which the lower rates contained in that legislation may apply. Therefore, the Service will issue temporary regulations to limit the ability of taxpayers to change their annual accounting period for these purposes.

In general, the temporary regulations will suspend the provisions of sections 1.441–2(c), 1.442–(c)(2), and 1.706–1(b) of the Income Tax Regulations, section 18.1378–1 of the Temporary Income Tax Regulations under the Subchapter S Revision Act of 1982, and any revenue procedure issued before September 18, 1986, that otherwise would permit a taxpayer to change its taxable year (including a change to a 52–53 week taxable year) either under a procedure that does not require the prior approval of the Commissioner or under expedited procedures for securing that approval. In addition, the temporary regulations will provide that, for the period to which the temporary regulations apply, approval of the Commissioner to a change of annual accounting period generally will be granted only if the taxpayer establishes a substantial business purpose by satisfying certain mechanical tests set forth in the temporary regulations. Approval also will be granted in certain cases in which the taxpayer has had a substantial acquisition or divestiture in the preceding twelve months that would justify a change in taxable year. Special rules will apply to certain taxpayers that wish to change to a 52–53 week taxable year that ends with reference to the end of the same month of the year as that in which the preceding taxable year ended.

The temporary regulation will prescribe procedures under which a taxpayer that satisfies the mechanical tests set forth in the temporary regulations or that is subject to the special rules relating to a 52–53 week year may change its taxable year without securing the prior approval of the Commissioner. A taxpayer that satisfies one of the mechanical tests or that is subject to the special rules relating to a 52–53 week year should follow the procedures set forth in the temporary regulations and should not file an application for approval under section 1.442–1(b) of the regulations.

The temporary regulations also will contain provisions to prevent the circumvention of these rules, such as through the use of tiered arrangements.

The temporary regulations generally will apply to any change in annual accounting period if the income tax return for the short period involved in the change is filed after September 29, 1986. The temporary regulations will not apply, however, in cases where the due date (without regard to extensions) for the short period involved in the change is before September 29, 1986, and the income tax return for the short period is timely filed (determined with regard to extensions). In addition, the temporary regulations will not apply to a change to a calendar year.

These special rules relating to changes in annual accounting period generally will apply only for a limited period of time that will be specified in the temporary regulations. That period will reflect the Service's concerns regarding the possible interaction between a change in taxable year and the effective date provisions of the pending tax reform legislation. For periods after the expiration of the temporary regulations, the Service may revise the procedures currently applicable to certain taxpayers.

Foundations Status of Certain Organizations

Announcement 86–102

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

A Wish Come True, Inc., Tiverton, RI
Access House, Inc., New York, NY
Adirondack Repertory Dance, Glenn Falls, NY
Aditus, Inc., Ludlow, MA
Agudsa Taharas Hamishpacha of Crown Heights Mikvah, Inc., Brooklyn, NY
Altiloria Art Alliance, New York, NY
Alumni Association of Massasoit Community College, Brockton, MA
American Ceramic Arts Society, Inc., New York, NY
American Civic Independence Foundation, Inc., Rockaway Beach, NY
American Friends of Mishkan Shimeon, Inc., Brooklyn, NY
Battle for Madison Commitee, Inc., The, Madison, CT
Beech Hill Scholarship, Ellsworth, ME
Birthright of Owego NY, Inc., Owego, NY
Blood Stream, Inc., New York, NY
Boston Stage Productions, Ltd., Boston, MA
Bragi Productions, Inc., Astoria, NY
Bronx Economic Neighborhood Development Corp., Bronx, NY
Bronx Park East Neighborhood Patrol, Inc., Bronx, NY
Bronx Red Cap Fund, Inc., Bronx, NY
Buc's Boys & Girls Association, Cambridge, MA
Cambridge Glaucoma Foundation, Inc., Cambridge, MA
Center for Language and Cerebral Function, Inc., Burlington, VT
Central New York Police Athletic League, Inc., Solvay, NY
Chakrachari Nishkalanki International Organization, Inc., Queens, NY
Children's Masquerade, Inc., New York, NY
Christian Community Charities, Inc., Brooklyn, NY
Cohasset Dramatic Club, Inc., Cohasset, MA

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[1] Also released as News Release IR–86–128, dated September 29, 1986.

Combined Health Appeal of Greater New York, Inc., New York, NY
Common Life, Inc., Boston, MA
Common Threads, Inc., New York, NY
Commonhealth Nutrition, Inc., Newton, MA
Community College of the Finger Lakes Student Assn., Canandaigua, NY
Community Transportation Fund for the Aged & Disabled, Inc., The, New Rochelle, NY
Composers in Red Sneakers, Incorporated, Watertown, MA
Connecticut Clergy & Laity Concerned, Inc., Danielson, CT
Conntac, Inc., Middletown, CT
Crisis Pregnancy Center, Inc., Simsbury, CT
Custody Intervention Panel, Inc., Buffalo, NY
Dedham Auxiliary Police Association, Inc., Dedham, MA
Dorothy Goodwin Charitable Trust, Lebanon, MA
Down East Health Care Foundation, Bangor, ME
Eastern Evaluation Research Society, Brooklyn, NY
Edu-Tainment and Info-Tainment Associates, Inc., Bronx, NY
Eternal Foundation of New Square Institutions, Inc., The, Brooklyn, NY
Family Advocacy Center, Inc., The, Marshfield, MA
Family Recovery, Inc., New York, NY
Federation of Puerto Rican Communities, Inc., New York, NY
Fellowship Time, Keene, NH
Feminist Spiritual Community, Portland, ME
Fifth Avenue Committee Housing Development Fund Corp., Brooklyn, NY
First Shiloh Baptist Church Housing of Buffalo, NY, Inc., Buffalo, NY
Foundation of Tribute to Mother Teresa, The, New York, NY
Friends of Childrens Psychiatric, West Seneca, NY
Friends of Cunningham Park, Inc., Fresh Meadow, NY
Friends of Fort Crailo, Rensselaer, NY
Friends of Horsey House, Inc., Hingham, MA
Friends of the Concertge Bouw, Inc., New York, NY
Friends of the Greenville Memorial Public Library, Greenville, NY
Friends of the Sea, Ltd., Windsor, CT
G.A.N.A. Development Project, Inc., New York, NY
Greater New Haven Community Chorus, Inc., New Haven, CT
Greenwich Soccer, Inc., Stamford, CT
Hamptons Workshop, Inc., The, Southhampton, NY
Harbinger Foundation, Inc., The, New York, NY
Helix Dance Foundation, Inc., New York, NY
Higher Education Opportunity Program Prof. Organization, Inc., Clinton, NY
Informed Citizens for Education, Inc., Edgartown, MA
Inner-City Outreach, Inc., Dorchester, MA
Institute of Astrology and Metaphysics, Ltd., Merrick, NY
Interlink Press Service, New York, NY
International Acts, Inc., New York, NY
International Friends of the Chilean Human Rights Commission, Inc., New York, NY
International Media Family, Inc., Southport, CT
Japan Society of Vermont, Inc., South Burlington, VT
Jerusalem Connection, The, New York, NY
Kalyan Ashram, Inc., Staten Island, NY
Lamoureux Foundation, Inc., Albany, NY
Latin American Music in Alternative, New York, NY
Lebanon Button Fund, Inc., Bedford, MA
Local Enterprise Assistance and Development Corp., New Haven, CT
Lower East Side Joint Planning Council, Inc., New York, NY
Make-A-Wish, Walpole, MA
Manchester Management Review, Inc., Manchester, NH
Manhattan Bridge Theatre, Inc., The, Brooklyn, NY
Massachusetts Vietnam Veterans Memorial Corp., Roslindale, MA
Memorial Hospital Foundation, Inc., Hollywood, FL
Mettowee Valley Youth Center, Inc., Pawlet, VT
Mohawk Valley Apartments, Inc., Clinton, NY
Natick Fourth of July, Inc., Natick, MA
National Billiary Atresia Foundation, Blauvelt, NY
National Chinese American Chamber of Industry & Commerce—USA, Inc., New York, NY
Needham Council for the Arts & Humanities, Inc., The, Needham, MA
Needham Soccer Club, Inc., Needham, MA
Neil Perkeil Memorial Fund, Inc., The, Woodmere, NY
Networking for Women in the Performing Arts, Inc., New York, NY
New Hampshire Association of Historic District Commissions, Exeter, NH
New Hampshire Intergroup Overates Anonymous Hooksett, NH
New Hampshire Wildlife Trust, Concord, NH
New York Association of School Psychologists, Syracuse, NY
N.Y.C. Partnership Housing Development Fund Company, Inc., New York, NY
New York City Twenty Fifth Precinct Gladiators, Inc., New York, NY
Newton Arts Center, Inc., Newtonville, MA
North Road Association, Inc., Monterey, MA
Nuevo Instituto De Centroamerica, Cambridge, MA
Old Colony Hospice, Inc., Stoughton, MA
Park Hope Nursing Home, Inc., Rochester, NY
Piermacelli Films, Inc., Leominster, MA
Piscataquis Valley Arts Council, Inc., Guilford, ME
Playground at Community School, Inc., Cumberland, RI
Playwrights Forum Theatre Co., Burlington, VT
Port Jefferson Lions Community Service Fund, Inc., Port Jefferson, NY
Portland Coalition for the Psychiatrically Labelled, Portland, ME
Project People to People, Inc., Dorchester, NH
Putnam Valley Friends of the Gifted, Lake Peekskill, NY
Rainbow Chimes, Inc., Huntington, NY
Real Sports & Education Foundation, Inc., Dorchester, MA
Respect Life, Inc., Spring Valley, NY
Respiratory Therapy Historical Society, Brooklyn, NY
Rhinebeck—Rheinbach Student Exchange Program, Inc., Rhinebeck, NY
RI Placement Coalition, Providence, RI
Rhode Island Resources, Inc., Woonsocket, RI
Russian Accent, Inc., Rego Park, NY
St. Stanislaus Community Association, Inc., Buffalo, NY
Samuel Huntington Parent Teacher Organization, Norwich, CT
Save Greenwich Cove, Inc., Old Greenwich, CT
Sebasticook Valley Foundation, Bangor, MA
Sickle Cell Center for Research, Inc., Saint Albans, NY
Simpson Street Development Association, Inc., Bronx, NY

Southern Tier Youth Advocacy, Inc., Painted Post, NY

Suffolk Association for Children with Learning Disabilities, Dix Hills, NY

Suffolk County Make-A-Wish Foundation, Inc., Greenland, NY

Theatre International, Inc., New York, NY

Trinity Neighborhood Association, Inc., Bronx, NY

Tri-Town Youth Services Bureau, Inc., Essex, CT

University Hospital Aid Association, Inc., Boston, MA

Upper Valley Criminal Justice Association, Lebanon, NH

VNA Hospice, Providence, RI

VNA, Inc., Providence, RI

Voice of the Armenian Church, Inc., The, Waltham, MA

Wareham Gatemen Baseball, Inc., Wareham, MA

Weston Home for the Retarded, Inc., Weston, MA

Widowed Persons Service of Greater Bangor, Inc., Bangor, ME

William Douglas Community Center, Northford, CT

William J. Seymour Society, Inc., The, Cambridge, MA

Wilmington Youth Soccer Association, Inc., Wilmington, MA

Woburn Auxiliary Firefighters Association, Inc., Woburn, MA

Women in Sales Association, Inc., Valhalla, NY

Woodmont Woods Elderly Housing, Inc., Milford, CT

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Deletions From Cumulative List of Organizations Contributions To Which Are Deductible Under Section 170 of the Code

Announcement 86–103

The names of organizations that no longer qualify as organizations contributions to which are deductible under section 170 of the Internal Revenue Code of 1954 are listed below.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that the organization no longer qualifies. However, the service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170 where the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of, the activities or deficiencies on the part of the organization which gave rise to the loss of qualification.

Moreover, if the Service has announced suspension of advance assurance of deductibility of contributions to an organization pending examination, and the qualification of the organization is subsequently terminated, contributions made after the date specified in the announcement in the Internal Revenue Bulletin are not deductible. In such a case the date of suspension will appear after the name of the organization to which it applies.

Copperweld Steel Company's Warren Employees Trust, Warren, OH.

Rodeo Evangelistic Ministry, Snyder, TX.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Paul R. Beutler	Cold Spring, MN	Certified Public Accountant	Eighteen Months from August 13, 1986
Robert J. Sher	Hyattsville, MD	Attorney	Indefinite from August 22, 1986
Russell H. Strong	Breckinridge, TX	Certified Public Accountant	Indefinite from August 22, 1986
David G. Willemain	Towson, MD	Attorney	Indefinite from July 22, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses or practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Alton C. Bingham	Las Vegas, NV	Certified Public Accountant	August 16, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified **describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).**

Clarified **is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.**

Distinguished **describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.**

Modified **is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).**

Obsoleted **describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.**

Revoked **describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.**

Superseded **describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.**

Supplemented **is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.**

Suspended **is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.**

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

_A_—Individual.
Acq.—Acquiescence.
_B_—Individual.
_BE_—Beneficiary.
_BK_—Bank.
_B.T.A._—Board of Tax Appeals.
_C_—Individual.
_C.B._—Cumulative Bulletin.
CFR—Code of Federal Regulations.
_CI_—City.
COOP—Cooperative.
_Ct.D._—Court Decision.
_CY_—County.
_D_—Decedent.
_DC_—Dummy Corporation.
_DE_—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation
_DR_—Donor.
_E_—Estate
_EE_—Employee.
_E.O._—Executive Order.
_ER_—Employer.
ERISA—Employee Retirement Income Security Act.
_EX_—Executor.
_F_—Fiduciary.
_FC_—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
_F.R._—Federal Register.
FUTA—Federal Unemployment Tax Act.
_FX_—Foreign Corporation.
_G.C.M._—Chief Counsel's Memorandum.
_GE_—Grantee.
_GP_—General Partner.
_GR_—Grantor.
_IC_—Insurance Company.
_I.R.B._—Internal Revenue Bulletin.
_LE_—Lessee.
_LP_—Limited Partner.
_LR_—Lessor.
_M_—Minor.
Nonacq.—Nonacquiescence.
_O_—Organization.
_P_—Parent Corporation.
PHC—Personal Holding Company.
_PO_—Possession of the U.S.
_PR_—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
_S_—Subsidiary.
_S.P.R._—Statements of Procedural Rules.
Stat.—Statutes at Large.
_T_—Target Corporation.
_T.C._—Tax Court.
_T.D._—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
_T.I.R._—Technical Information Release.
_TP_—Taxpayer.
_TR_—Trust.
_TT_—Trustee.
_U.S.C._—United States Code.
_X_—Corporation.
_Y_—Corporation.
_Z_—Corporation.

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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*Denotes entry since last publication

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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1986-42

Internal Revenue bulletin

Bulletin No. 1986-42
October 20, 1986

HIGHLIGHTS OF THIS ISSUE

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DEPOSITORY 376

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86-120, page 4.
Reacquisitions; repossession by former shareholder of the seller. The nonrecognition provision section 1038 of the Code will not apply to a former shareholder who has received an installment obligation from a corporation in a section 337 liquidation when that shareholder, upon the buyer's default, subsequently receives the real property used to secure the obligation.

Rev. Rul. 86-121, page 5.
Federal short-term, mid-term, and long-term rates. Section 1274(d) of the Code was amended by section 101(b)(1) of the 1985 imputed interest simplification act. Accordingly, Rev. Rul. 85-170 is declared obsolete.

T.D. 8104, page 5.
Regulations under sections 1374 and 1375 of the Code relate to a tax imposed on capital gains of certain S corporations and a tax imposed on the excess net passive income of certain S corporations that have accumulated earnings and profits from subchapter C years.

EXEMPT ORGANIZATIONS

Announcement 86-104, page 22.
A list is given of organizations now classified as private foundations.

EXCISE TAXES

Rev. Rul. 86-122, page 9.
Truck chassis and bodies; constructive sale price. When taxable truck bodies and chassis are sold by a dealer at both arm's length and non-arm's length, the dealer's constructive sale price on it's non-arm's-length sales is the lowest price at which the dealer regularly sells the article at arm's length.

T.D. 8103, page 10.
Amendments to the regulations under section 4996 of the Code relate to the definition of "removed from the premises" for purposes of the windfall profit tax.

LR-34-82, page 15.
Proposed regulations under section 4996 of the Code relate to the definition of "property" for purposes of the windfall profit tax.

Finding Lists begin on page 27.
Announcement of Disbarments and Suspensions on page 25.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the Internal Revenue Bulletin as the source would be appropriate.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 453.—Installment Method

26 CFR 1.453–9: Gain or loss on dispositions of installment obligation.

Whether a former shareholder who receives an installment obligation from a corporation in a section 337 liquidation recognizes gain when, upon the buyer's default, the former shareholder subsequently receives the real property used to secure the obligation. See Rev. Rul. 86–120, this page.

Section 1038.—Certain Reacquisitions of Real Property

26 CFR 1.1038–1: Reacquisitions of real property in satisfaction of indebtedness.
(Also Section 453; 1.453–9.)

Reacquisitions; repossession by former shareholder of the seller. The nonrecognition provision section 1038 of the Code will not apply to a former shareholder who has received an installment obligation from a corporation in a section 337 liquidation when that shareholder, upon the buyer's default, subsequently receives the real property used to secure the obligation.

Rev. Rul. 86–120

ISSUE

Does section 1038 of the Internal Revenue Code apply with respect to a reacquisition of real property under an installment obligation distributed to a shareholder by a corporation pursuant to a liquidation described in section 337 of the Code?

FACTS

A corporation adopted a plan of complete liquidation to which section 337 of the Code applied. During the following 12 months, it sold real property and accepted as payment for the property an installment obligation secured by the property. The installment obligation was later distributed to a shareholder in exchange for the shareholder's interest in the corporation. Following the liquidation, the buyer of the property defaulted on the obligation and the property was acquired by the former shareholder in full settlement of the installment obligation.

LAW AND ANALYSIS

Section 453(h) of the Code, as added by the Installment Sales Revision Act of 1980, section 2, 1980–2 C.B. 489, 491, generally provides that if a shareholder receives an installment obligation in connection with a corporate liquidation under section 337, the receipt of payments under the obligation (but not the receipt of the obligation) by the shareholder shall be treated as the receipt of payment for the stock.

Section 453B(a) of the Code generally provides that gain or loss is recognized when an installment obligation is satisfied at other than face value. Thus, a repossession of property in satisfaction of an installment obligation results in gain or loss as a disposition of the installment obligation. *Morrison v. Commissioner*, 12 T.C. 1178 (1949); *Boca Ratone Co. v. Commissioner*, 86 F.2d 9 (3rd Cir. 1936). In the case of an obligation that is subject to section 453(h), any gain or loss on disposition is considered as resulting from the sale or exchange of the shareholder's stock.

Notwithstanding section 453B(a), section 1038 generally provides that if a sale of a real property gives rise to indebtedness to the seller which is secured by the real property, and the seller later reacquires the property in partial or full satisfaction of the indebtedness, then no gain or loss will result to the seller from the reacquisition.

Section 1.1038–1(a)(3)(i) of the Income Tax Regulations states that section 1.1038–1 of the regulations applies only when the seller reacquires the real property in partial or full satisfaction of the indebtedness that arose from the sale of the real property and was secured by the property.

Neither the Internal Revenue Code nor the regulations define the term "seller" as used in section 1038. The legislative history, however, shows that, in enacting section 1038, Congress contemplated its application to a reacquisition of property by the original seller of the property. The Senate Report states:

> Your Committee believes it is inappropriate to measure gain upon repossession by reference to the fair market value of the repossessed property. Your Committee does not believe that merely because property *originally held by a seller* has been restored to him should constitute grounds for taxing any appreciation in value of this property to the seller at that time. Apart from any payments he may have received, he actually is in no better position than he was before he made the sale. As a result, your committee has concluded that instead of the repossession of the property being treated as a second sale of the property back to its *original holder*, it is desirable to consider instead that the first sale has been nullified.

S. Rep. No. 1361, 88th Cong., 2d Sess. 5 (1964), 1964–2 C.B. 828, 831 (Emphasis added.).

At the same time that Congress added section 453(h) to the Code, it also added section 1038(g). Section 1038(g) generally provides that, for purposes of section 1038(a), the acquisition of real property by the estate or beneficiary of the deceased seller shall be treated as a reacquisition by the seller. Thus, the estate or beneficiary generally succeeds to the same nonrecognition treatment under section 1038 to which the deceased seller would have been entitled. Significantly, no similar provision was added to allow a shareholder that receives an installment obligation under section 453(h) to be treated as the "seller" for purposes of section 1038.

Moreover, the circumstances under which section 1038(g) of the Code applies are fundamentally different from those in which section 453(h) applies. In cases to which section 1038(g) applies, a transfer of the real property from the decedent directly to the decedent's estate or beneficiary would not be taxable to the transferee. The nonrecognition treatment provided to the estate or beneficiary by virtue of section 1038(g) is thus consistent with the income tax consequences that would have been obtained had the original seller acquired the property in satisfaction of the installment debt and held the property until death. In contrast, in cases in which section 453(h) applies, a transfer of the real estate from the liquidating corporation directly to the shareholder would be taxable to the shareholder under section 331. Accordingly, permitting nonrecognition treatment under section 1038 when the shareholder acquires the property indirectly from the corporation's defaulting installment purchaser would put the shareholder in a better tax position than if the property were acquired directly from the corporation. There is no indication that Congress intended such a result.

In the instant case, the corporation was the owner and seller of the real property in question. Acquisition by the shareholder did not restore the property to the original seller. Rather, it placed the property in the hands of a person that acquired, through an exchange transaction with the original owner and seller, the right to possession upon default. The taxpayer is no more the original seller of the property than is a purchaser of installment contracts from a real estate vendor. *See* Rev. Rul. 68–523, 1968–2 C.B. 82, which concerns repossessions by the purchaser of such contracts and does not allow section 1038 treatment.

HOLDING

Section 1038 of the Code does not apply to the former shareholder's acquisition of the property, because the liquidated corporation, not the former shareholder, was the seller of the property for purposes of that section.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

Federal short-term, mid-term, and long-term rates. Section 1274(d) of the Code was amended by section 101(b)(1) of the 1985 imputed interest simplification act. Accordingly, Rev. Rul. 85–170 is declared obsolete.

Rev. Rul. 86–121

Section 1274(d) of the Internal Revenue Code, as amended by section 101(b)(1) of the 1985 imputed interest simplification act (the Act), Pub. L. No. 99–121, 1985–2 C.B. 367, provides that the applicable federal short-term, mid-term, and long-term rates shall be determined each month. These rates are published monthly in the Internal Revenue Bulletin. Section 1274(d), as amended, is effective for sales and exchange transactions made after June 30, 1985.

Prior to the amendment of section 1274(d) of the Code by section 101(b)(1) of the Act, the applicable federal rates were determined semiannually, and monthly rates were computed under the alternate method provided by section 1.1274–6T of the Temporary Income Tax Regulations. Rev. Rul. 85–170, 1985–2 C.B. 186, sets forth the short-term, mid-term, and long-term applicable federal rates for the six-month period, January 1, 1986, through June 30, 1986. Rev. Rul. 85–170 was first made public as an attachment to News Release IR–85–102, dated October 7, 1985. News Release IR–85–102 was distributed prior to the date of enactment of section 101(b)(1) of the Act.

As a result of the amendment of section 1274(d) by the section 101(b)(1) of the Act, Rev. Rul. 85–170 is hereby declared obsolete.

Section 1275.—Other Definitions and Special Rules

26 CFR 1.1375–1A: Tax imposed when passive investment income of corporation having subchapter C earnings and profits exceed 25 percent of gross receipts.

Rules define the term "passive investment income." See T.D. 8104, below.

Section 1374.—Tax Imposed on Certain Capital Gains

26 CFR 1.1374–1A: Tax imposed on certain capital gains.
(Also Section 1375; 1.1375–1A.)

T.D. 8104

TITLE 26.—INTERNAL REVENUE—
CHAPTER I, SUBCHAPTER A, PART
1—INCOME TAX; TAXABLE YEARS
BEGINNING AFTER DECEMBER 31,
1953; SUBCHAPTER H, PART 602—
OMB CONTROL NUMBERS UNDER
THE PAPERWORK REDUCTION ACT

Capital Gains Tax and Passive Income Tax with Respect to Certain S Corporations

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to a tax imposed on capital gains of certain S corporations and a tax imposed on the excess net passive income of certain S corporations that have accumulated earnings and profits from subchapter C years. Changes to the applicable law were made by the Subchapter S Revision Act of 1982 [Pub. L. 97–354, 1982–2, C.B. 702], as amended by the Technical Corrections Act of 1982 [Pub. L. 97–448, 1983–1 C.B. 451] and the Tax Reform Act of 1984 [Pub. L. 98–369, 1984–3 C.B. 1]. The regulations would provide the public with the guidance needed to comply with the law as amended by these Acts.

DATES: The amendments under section 1374 are generally effective for taxable years beginning after December 31, 1982, and the amendments under section 1375 are generally effective for taxable years beginning after 1981.

SUPPLEMENTARY INFORMATION:
BACKGROUND

Proposed amendments to the Income Tax Regulations (26 CFR Part 1) were published in the FEDERAL REGISTER (50 FR 27457) on July 3, 1985 [LR–267–82, 1985–2 C.B. 790]. Those amendments were proposed to conform the regulations to section 2 of the Subchapter S Revision Act of 1982 (96 Stat. 1669), as amended by section 305(d)(3) of the Technical Corrections Act of 1982 (96 Stat. 2400) and section 102(d)(1), 474(r), and 721(u) and (v) of the Tax Reform Act of 1984 (98 Stat. 623, 844, and 971).

Approximately 4 written comments were received in response to the notice of proposed rulemaking. No public hearing was requested. After consideration of all the public comments, the proposed amendments are adopted as revised by this Treasury decision.

IN GENERAL

Section 1374 imposes a tax on the capital gains of certain S corporations. The tax is imposed for any taxable year in which the S corporation has a net capital gain in excess of $25,000 for the taxable year if the amount of the net capital gain exceeds 50 percent of the taxable income for such year and the taxable income for such year is in excess of $25,000.

The amount of the tax is generally 28 percent of the amount of the net capital gain in excess of $25,000. However, in no case will the tax imposed by section 1374 on the corporation exceed the tax that would have been imposed by section 11 on the corporation if the corporation were not an S corporation. Section 1374(c) contains exceptions to the tax imposed by section 1374(a) and a special rule in the case of property with a substituted basis. Section 1374(d) and §1.1374–1A(d) define the term "taxable income" for purposes of section 1374.

Section 1375 imposes a tax on the excess net passive income of certain S corporations that have subchapter C earnings and profits. This tax can generally be avoided by the corporation distributing its subchapter C earnings and profits before the close of the taxable year. The tax is computed by multiplying the excess net passive income by the highest rate of tax specified in section 11(b). Section 1375(b) and §1.1375–1A(b) define the term "excess net passive income." A special rule contained in section 1375(c) ensures that a net capital gain that is taken into account under section 1375 in computing the passive income tax will not also be taken into account in determining the capital gains tax under section 1374. Section 1375(d) provides that the tax imposed by section 1375 may be waived in certain limited cases where an S corporation determined in good faith that it had no subchapter C earnings and profits at the end of a taxable year and it is later determined that it did have such earnings and profits. Section 1.1375–1A(d) provides rules concerning this waiver.

PUBLIC COMMENTS AND CHANGES IN RESPONSE TO PUBLIC COMMENTS

Several comments suggested minor technical refinements to the proposed rules. Other comments asked for additional guidance to clarify certain of the proposed rules. In general, the suggested changes have been made.

One of the changes made deals with the procedure for requesting a waiver of the tax imposed by section 1375. The final regulations provide that the request for waiver should be made to the district director rather than in the form of a ruling request to the National Office.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required. The Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

PAPERWORK REDUCTION ACT

The collection of information requirements contained in this regulation have been submitted to the Office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act of 1980. These requirements have been approved by OMB.

DRAFTING INFORMATION

The principal author of these final regulations is John G. Schmalz of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 1 and Part 602 are amended as follows:

INCOME TAX REGULATIONS
(26 CFR Part 1)

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805***.

§§1.1361–1 through 1.1361–16 [Removed]

Par. 2. Sections 1.1361–1 through 1.1361–16 are removed.

Par. 3. There are inserted immediately after §1.1348–3 the following new §§1.1361–0A, 1.1374–1A, and 1.1375–1A to read as follows:

§1.1361–0A Effective date.

(a) Except as otherwise provided in the regulations, the provisions of §§1.1374–1A and 1.1375–1A apply to taxable years beginning after December 31, 1982.

(b) The provisions of §§1.1374–1 through 1.1378–3 apply to a qualified casualty insurance electing small business corporation and to a qualified oil corporation for taxable years beginning after December 31, 1982, and the provisions of §§1.1374–1A and 1.1375–1A shall not apply. See section 6(c)(2), (3), and (4) of the Subchapter S Revision Act of 1982.

§1.1374–1A Tax imposed on certain capital gains.

(a) *General rule.* Except as otherwise provided in paragraph (c) of this section, if for a taxable year beginning after 1982 of an S corporation—

(1) The net capital gain of such corporation exceeds $25,000, and

(2) The net capital gain of such corporation exceeds 50 percent of its taxable income (as defined in paragraph (d) of this section) for such year, and

(3) The taxable income of such corporation (as defined in paragraph (d) of this section) for such year exceeds $25,000, section 1374 imposes a tax (computed under paragraph (b) of this section) on the income of such corporation. The tax is imposed on the S corporation and not on the shareholders.

(b) *Amount of tax.* The amount of tax shall be the lower of—

(1) An amount equal to the tax, determined as provided in section 1201(a)(2), on the amount by which the net capital gain of the corporation for the taxable year exceeds $25,000, or

(2) An amount equal to the tax which would be imposed by section 11 on the taxable income of the corporation (as defined in paragraph (d) of this section) for the taxable year were it not an S corporation.

No credit shall be allowable under part IV of subchapter A of chapter 1 of the Internal Revenue Code of 1954 (other than under section 34) against the tax imposed by section 1374(a) and this section. See section 1375(c)(2) and §1.1375–1A(c)(2) for a general rule that reduces the amount of the net capital gain of the corporation for purposes of this paragraph (b) in cases where a net capital gain is taxed as excees net passive income under section 1375. See section 1374(c)(3) and paragraph (c)(1)(ii) of this section for a special rule that limits the amount of tax on property with a substituted basis in certain cases.

(c) *Exceptions to taxation*—(1) *New corporations and corporations with election in effect for 3 immediately preceding years*—(i) *In general.* If an S corporation would be subject to the tax imposed by section 1374 for a taxable year pursuant to paragraph (a) of this section, the corporation shall, nevertheless, not be subject to such tax for such year, if:

(A) The election under section 1362(a) which is in effect with respect to such corporation for such year has been in effect for the corporation's three immediately preceding taxable years, or

(B) An election under section 1362(a) has been in effect with respect to such corporation for each of its taxable years for which it has been existence, unless there is a net capital gain for the taxable year which is attributable to property with a substituted basis within the meaning of paragraph (c)(1)(iii) of this section.

(ii) *Amount of tax on net captial gain attributable to property with a substituted basis.* If for a taxable year of an S corporation either paragraph (c)(1)(i) (A) or (B) of this section is satisfied, but the S corporation has a net capital gain for such taxable year which is attributable to property with a substituted basis (within the meaning of paragraph (c)(1)(iii) of this section), then paragraph (a) of this section shall apply for the taxable year, but the amount of tax determined under paragraph (b) of this section shall not exceed a tax, determined as provided in section 1201 (a), on the net capital gain attributable to property with a substituted basis.

(iii) *Property with substituted basis*. For purposes of this sectio, the term "property with a substituted basis" means:

(A) Property acquired by a corporation ("the acquiring corporation") during the period beginning 36 months before the first day of the acquiring corporation's taxable year and ending on the last day of such year;

(B) The basis of such property in the hands of the acquiring corporation is detemined in whole or in part by reference to the basis of any property in the hands of another corporation; and

(C) Such other corporation was not an S corporation throughout the period beginning the later of:

(1) 36 months before the first day of the acquiring corporation's taxable year. or

(2) The time such other corporation came into existence,

and ending on the date such other corporation transferred the property, the basis of which is used to determine, in whole or in part, the basis of the property in the hands of the acquiringg corporation. An S corporation and any predecessor corporation shall not be treated as one corporation for purposes of this paragraph (c)(1).

(iv) *Existence of a corporation*. For purposes of this section, a corporation shall not be considered to be in existence for any month which precedes the first month in which such corporation has shareholders or acquires assets or begins business, whichever is first to occur.

(v) *References to prior law included*. For purposes of this paragraph (c), the term "S corporation" shall include an electing small business corporation under prior subchapter S law, and the term "election under section 1362(a)" shall include an election under section 1372 of prior subchapter S law.

(iv) *Examples*. The provisions of this paragraph may be illustrated by the following examples:

Example (1): M Corporation was organized and began business in 1977. M subsequently made an election under section 1362(a) which was effective for its 1984 taxable year. If such election does not terminate under section 1362 for its taxable years 1984, 1985, and 1986. M is not subject to the tax imposed by section 1374 for its taxable year 1987, or for any subsequent year for which such election remains in effect, unless it has, for any such year, an excess of net long-term capital gain over net short-term capital loss attributable to property with a substituted basis. If there is such an excess for any such year, and the requirements of paragraph (a) of this section are met. M will be subject to the tax for such year. If there is no such excess for any year after 1986. M will not be subject to the tax for any such year even though the requirements of paragraph (a) of this section are met.

Example (2). N corporation was organized in 1983, and was an S corporation for its first taxable year. N is not subject to the tax imposed by section 1374 for 1983, or for any subsequent year for which its original election under section 1382(a) has not terminated under section 1362(d), unless for any such year, it has been an excess of net long-term capital gain over net short-term capital loss attributable to property with a substituted basis and the requirements of paragraph (a) of this section are met.

(2) *Treatment of certain gains of options and commodities dealers*—(i) *Exclusion of certain capital gains*. For purposes of this section, the net capital gain of any options dealer or commodities dealer shall be determined by not taking into account any gain or loss (in the normal course of the taxpayer's activity of dealing in or trading section 1256 contracts) from any section 1256 contract or property related to such a contract.

(ii) *Definitions*. For purposes of this paragraph (c)(2)—

(A) *Options dealer*. The term "options dealer" has the meaning given to such term by section 1256(g)(8).

(B) *Commodities dealer*. The term "commodities dealer" means a person who is actively engaged in trading section 1256 contracts and its registered with a domestic board of trade which is designated as a contact market by the Commodities Futures Trading Commission.

(C) *Section 1256 contracts*. The term "section 1256 contracts" has the meaning given to such term by section 1256(b).

(iii) *Effective dates*—(A) *In general*. Except as otherwise provided in this paragraph (c)(2)(iii). This paragraph (c)(2) shall apply to positions established after July 18, 1984, in taxable years ending after such date.

(B) *Special rule for options on regulated futures contracts*. In the case of any option with respect to a regulated futures contract (within the meaning of section 1256), this paragarph (c)(2) shall apply to positions established after October 31, 1983, in taxable years ending after such date.

(C) *Elections with respect to property held on or before July 18, 1984*. See §§1.1256(h)–1T and 2T for rules concerning an election to have this paragraph (c)(2) apply to certain property held on or before July 18, 1984.

(d) *Determination of taxable income*—(1) *General rule*. For purposes of this section, taxable income of the corporation shall be determined under section 63(a) as if the corporation were a C corporation rather than an S corporation, except that the following deductions shall not apply in the computation—

(i) The deduction allowed by section 172 (relating to net operating loss deduction), and

(ii) The deductions allowed by part VIII of subchapter B (other than the deduction allowed by section 248, relating to organization expenditures). For any taxable year in which a tax under this section is imposed on an S corporation, the S corporation shall attach a Form 1120 completed in accordance with this paragraph (d) and the instructions to form 1120S to its tax return field for such taxable year.

(2) *Special rule for net capital gains taxed as excess net passive income under section 1375*. See section 1375(c)(2) and §1.1375–1A for a special rule that reduces the taxable income of the corporation for purposes of section 1374(b)(2) and §1.1374–1A(b)(2) in cases where a net capital gain is taxed as excess net passive income under section 1375.

(e) *Reduction in pass-thru for tax imposed on capital gain*. See section 1366(f)(2) for a special rule reducing the S corporation's long-term capital gains and the corporation's gain from sales or exchanges of property described in section 1231 for purposes of section 1366(a) by an amount of tax imposed under section 1374 and this section.

(f) *Examples*. The following examples illustrate the principles of this section and assume that a tax will not be imposed under section 1375:

Example (1). Corporation M is an S corporation for its taxable year beginning January 1, 1983. For 1983 M has an excess of net long-term capital gain over net short-term capital loss in the amount of $30,000. However, its taxable income for the year is only $20,000 as a result of other deductions in excess of other income. Thus, although the excess of the net long-term captial gain over the net short-term capital loss exceeds $25,000 and also exceeds 50 percent of taxable income. M is not subject to the tax imposed by section 1374 for 1983 because its taxable income does not exceed $25,000.

Example (2). Corporation N is an S Corporation for its 1983 taxable year. For 1983, N has an excess of net long-term capital gain over net short-term capital loss in the amount of $30,000, and taxable income of $65,000. Thus, although N's net capital gain ($30,000) exceeds $25,000, it does not exceed 50 percent of the corporation's taxable income for the year (50 percent of $65,000, or $32,500), and therefore N is not subject to the tax imposed by section 1374 for such year.

Example (3). Assume that Corporation O, an S corporation, is subject to the tax imposed by section 1374 for its taxable year 1983. For 1983 O has an excess of net long-term capital gain over net short-term capital loss in the amount of $73,000, and taxable income within the meaning of section 1374, which includes capital gains and losses, of $100,000. The amount of tax computed under paragraph (b)(1) of this sections is 28 percent of $48.00 ($73,000—$25,000, or $13,440. Since this is lower than the amount computed under paragraph (b)(2) of this section, which is $25 750 ($3,750 + $4,500 + 7,500 + $10,000). $13,440 is the amount of tax imposed by section 1374.

Example (4). Assume that in example (3) the taxable income of O for 1983 is $35,000. This results from an excess of deductions over income with respect to items which were not included in determining the excess of the net long-term capital gain over the net short-term capital loss. In such case, the amount of tax, computed under paragraph (b)(2) of this section, is $5,500. Since this is lower than the amount computed under paragraph (b)(1) of this section, $5,550 is the amount of tax imposed by section 1374.

Example (5). Corporation P, an S corporation, for its taxable year 1983 has an excess of net long-term capital gain over net short-term capital loss in the amount of $65,000 and has taxable income of $80,000. P's election under section 1362 has been in effect for its three immediately preceding taxable years, but P, nevertheless, is subject to the tax imposed by section 1374 for 1983 since it has an excess of net long-term capital gain over net short-term capital loss (in the amount of $20,000) attributable to property with a substituted basis. The tax computed under paragraph (b)(1) of this section, $11,200 (28 percent of $40,000 ($65,000—$25,000)), is less than the tax compound under paragraph (b)(2) of this section, $17,750. However, under the limitation provided in paragraph (c) of this section which is applicable in this factual situation, the tax imposed by section 1374 for 1983 may not exceed $5,600 (28 percent of $20,000, the excess of net long-term capital gain over the net short-term capital loss attributable to property with a substituted basis).

§1.1375–1A Tax imposed when passive investment income of corporation having subchapter C earnings and profits exceed 25 percent of gross receipts.

(a) *General rule.* For taxable years beginning after 1981, section 1375(a) imposes a tax on the income of certain S corporations that have passive investment income. In the case of a taxable year beginning during 1982, an electing small business corporation may elect to have the rules under this section not apply. See the regulations under section 1362 for rules on the election. For purposes of this section, the term "S corporation" shall include an electing small business corporation under prior law. This tax shall apply to an S corporation for a taxable year if the S corporation has—

(1) Subchapter C earnings and profits at the close of such taxable year, and

(2) Gross receipts more than 25 percent of which are passive investment income.

If the S corporation has no subchapter C earnings and profits at the close of the taxable year (because, for example, such earnings and profits were distributed in accordance with section 1368), the tax shall not be imposed even though the S corporation has passive investment income for the taxable year. If the tax is imposed, the tax shall be computed by multiplying the excess net passive income (as defined in paragraph (b) of this section) by the highest rate of tax specified in section 11(b).

(b) *Definitions*—(1) *Excess net passive income*—(i) *In general.* The term "excess net passive income" is defined in section 1375(b)(1), and can be expressed by the following formula:

$$\text{ENPI} = \text{NPI} \times \frac{\text{PII} - (.25 \times \text{GR})}{\text{PII}}$$

Where:

ENPI = excess net passive income
NPI = net passive income
PII = passive investment income
GR = total gross receipts

(ii) *Limitation.* The amount of the excess net passive income for any taxable year shall not exceed the corporation's taxable income for the taxable year (determined in accordance with section 1374(d) and §1.1374–1A(d)).

(2) *Net passive income.* The term "net passive income" means—

(i) Passive investment income reduced by

(ii) The deductions allowable under chapter 1 of the Internal Revenue Code of 1954 which are directly connected (within the meaning of paragraph (b)(3) of this section) with the production of such income (other than deductions allowable under section 172 and part VIII of subchapter B).

(3) *Directly connected*—(i) *In general.* For purposes of paragraph (b)(2)(ii) of this section to be directly connected with the production of income, an item of deduction must have proximate and primary relationship to the income. Expenses, depreciation, and similar items attributable solely to such income qualify for deduction.

(ii) *Allocation of deduction.* If an item of deduction is attributable (within the meaning of paragraph (b)(3)(i) of this section) in part to passive investment income and in part to income other than passive investment income, the deduction shall be allocated between the two types of items on a reasonable basis. The portion of any deduction so allocated to passive investment income shall be treated as proximately and primarily related to such income.

(4) *Other definitions.* The terms "subchapter C earnings and profits," "passive investment income," and "gross receipts" shall have the same meaning given these terms in section 1362(d)(3) and the regulations thereunder.

(c) *Special rules*—(1) *Disallowance of credits.* No credit is allowed under part IV of subchapter A of chapter 1 of the Code (other than section 34) against the tax imposed by section 1375(a) and this section.

(2) *Coordination with section 1374.* If any gain—

(i) is taken into account in determining passive income for purposes of this section, and

(ii) is taken into account under section 1374.

The amount of such gain taken into account under section 1374(b) and §1.1374-1A(b)(1) and (2) in determining the amount of tax shall be reduced by the portion of the excess net passive income for the taxable year which is attributable (on a pro rata basis) to such gain. For purposes of the preceding sentence, the portion of excess net passive income for the taxable year which is attributable to such capital gain is equal to the amount determined by multiplying the excess net passive income by the following fraction:

$$\frac{\text{NCG–E}}{\text{NPI}}$$

Where:

NCG = net capital gain
NPI = net passive income.
E = Expense attributable to net capital gain

(d) *Waiver of tax in certain cases*—(1) *In general.* If an S corporation establishes to the satisfaction of the Commissioner that—

(i) It determined in good faith that it had no subchapter C earnings and profits at the close of the taxable year, and

(ii) During a reasonable period of time after it was determined that it did have subchapter C earnings and profits at the close of such taxable year such earnings and profits were distributed.

The Commissioner may waive the tax imposed by section 1375 for such taxable year. The S corporation has the burden of establishing that under the relevant facts and circumstances the Commissioner should waive the tax. For example, if an S corporation establishes that in good faith and using due diligence it determined that it had no subchapter C earnings and profits at the close of a taxable year, but it was later determined on audit that it did have subchapter C earnings and profits at the close of such taxable year, and if the corporation establishes that it distributed such earnings and profits within a reasonable time after the audit, it may be appropriate for the Commissioner to waive the tax on passive income for such taxable year.

(2) *Corporation's request for a waiver.* A request for waiver of the tax imposed by section 1375 shall be made in writing to the district director request and shall contain all relevant facts to establish that the requirements of paragraph (d)(1) of this section are met. Such request shall contain a description of how and on what date the S corporation in good faith and using due diligence determined that it had no subchapter C earnings and profits at the close of the taxable year, a description of how and on what date it was determined that the S corporation had subchapter C earnings and profits at the close of the year and a description (including dates) of any steps taken to distribute such earnings and profits. If the earnings and profits have not yet been distributed, the request shall contain a timetable for distribution and an explanation of why such timetable is reasonable. On the date the waiver is to become effective, all subchapter C earnings and profits must have been distributed.

(e) *Reduction in pass-thru for tax imposed on excess net passive income.* Set section 1366(f)(3) for a special rule reducing each item of the corporation's passive investment income for purposes of section 1366(a) if a tax is imposed on the corporation under section 1375.

Examples. The following examples illustrate the principles of this section:

Example (1). Assume Corporation M, an S corporation, has for its taxable year total gross receipts of $200,000, passive investment income of $100,000, $60,000 of which is interest income, and expenses directly connected with the production of such interest income in the amount of $10,000. Assume also that at the end of the taxable year Corporation M has subchapter C earnings and profits. Since more than 25 percent of Corporation M's total gross receipts are passive investment income, and since Corporation M has subchapter C earnings and profits at the end of the taxable year. Corporation M will be subject to the tax imposed by section 1375. The amount of excess net passive investment income is $45,000 ($90,000 × (50,000/100,000)). Assume that the other $40,000 of passive investment income is attributable to net capital gain and that there are no expenses directly connected with such gain. Under these facts $20,000 of the excess net passive income is attributable to the net capital gain ($45,000 × ($40,000/$90,000)). Accordingly the amount of gain taken into account under section 1374(b)(1) and the taxable income of Corporation M under section 1374(b)(2) shall be reduced by $20,000.

Example (2). Assume an S corporation with subchapter C earnings and profits has tax-exempt income of $400, its only passive income, gross receipts of $1,000 and taxable income of $250 and there are no expenses associated with the tax-exempt income. The corporation's excess net passive income for the taxable year would total $150 (400 × ((400 − 250)/400)). This amount is subject to the tax imposed by section 1375, notwithstanding that such amount is otherwise tax-exempt income.

OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT
(26 CFR Part 602)

Par. 4. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805 * * *.

Par. 5. Section 602.101(c) is amended by inserting in the appropriate places in the table

"§1.1374-1A(d). . .

ROSCOE L. EGGER, JR.,
Commissioner of
Internal Revenue

Approved September 3, 1986.

J. ROGER MENTZ,
Acting Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on September 25, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 26, 1986, 51 F.R. 34200)

Section 4051.—Imposition of Tax on Heavy Trucks and Trailers Sold at Retail

26 CFR 145.4051-1: Imposition of Tax on Heavy Trucks and Trailers Sold at Retail.

Constructive sales price in the case of sales of an article at non-arm's-length by a dealer who regularly sells the same article at arm's length. See Rev. Rul. 86-122, below.

Section 4052.—Definitions and Special Rules

26 CFR 145.4052-1: Special rules and definitions.
(Also Section 4051; 145.4051-1.)

Truck chassis and bodies; constructive sale price. When taxable truck bodies and chassis are sold by a dealer at both arm's length and non-arm's length, the dealer's constructive sale price on its non-arm's-length sales is the lowest price at which the dealer regularly sells the article at arm's length.

Rev. Rul. 86-122

ISSUE

When a truck dealer sells taxable truck bodies and chassis to its wholly owned subsidiary company for use in the company's business, what rule determines whether the sales are at less than fair market price for purposes of section 4052(b)(2) of the Internal Revenue Code, and, if they are at less than fair market price, how is a constructive sales price to be determined under that section?

FACTS

A corporate truck dealer sells taxable truck bodies and chassis to its wholly owned subsidiary company for use in the subsidiary's business. In all cases, the price for which the dealer sells a particular body or chassis to the subsidiary is lower than the lowest price for which the dealer regularly sells the same model truck body or chassis at retail to unrelated customers.

LAW AND ANALYSIS

Section 4051(a)(1) of the Code imposes on the first retail sale of certain articles (including in each case parts and accessories sold on or in connection therewith or with the sale thereof) a tax of 12 percent of the price for which the articles are sold. Among the taxable articles are truck bodies and chassis suitable for use with a vehicle which has a gross vehicle weight rating in excess of 33,000 pounds. Section 4052(a)(1) defines the term "first retail sale" as the first sale, for a purpose other than resale, after manufacture, production, or importation.

Section 145.4052-1(d)(1) of the Temporary Excise Tax Regulations provides that the price for which an article is sold includes the total consideration paid for the article whether that consideration is paid in money, services, or other forms. In addition, there shall be included any charge incident to placing the article in condition ready for use. Similar rules to section 4216(a) of the Code and the regulations thereunder, relating to charges to be included in the price and excluded from the price, shall apply. For example, charges for transportation, delivery, insurance, and installation (other than installation charges to which section 4051(b) applies), and other expenses actually incurred in connection with the delivery of an article to a purchaser pursuant to a bona fide sale shall be excluded from the price in computing the tax.

Section 4052(b)(2) of the Code provides that, in the case of any article sold (otherwise than through an arm's length transaction) at less than the fair market price, the tax under subchapter B of chapter 31, which includes section 4051, shall be computed on the price for which similar articles are sold at retail in the ordinary course of trade, as determined by the Secretary.

Section 145.4052–1(d)(4) of the temporary regulations, relating to sales not at arm's length, provides that a sale is considered to be made under circumstances other than at "arm's length" if

(i) one of the parties is controlled (in law or in fact) by the other, or there is common control, whether or not such control is actually exercised to influence the sale price, or

(ii) the sale is made pursuant to special arrangements between a seller and a purchaser.

In the case of an article sold otherwise than at arm's length, and sold at less than the fair market price, the tax imposed under section 4051(a)(1) or (b)(1) is to be computed on the price for which similar articles are sold at retail in the ordinary course of trade, as determined by the Commissioner. Once such a price has been determined, no further adjustment of such price shall be made.

For purposes of retail sales under section 4051(a)(1) of the Code, the Commissioner has determined that if a truck dealer regularly sells a certain article in both arm's length retail sales and non-arm's-length sales, the retail fair market price of the article is the lowest price at which the dealer regularly sells the article in the arm's length retail sales. Where the non-arm's-length sale price is less than at the fair market price, the Commissioner has determined that the constructive sales price for purposes of section 4052(b)(2) of the Code is the lowest price at which the dealer regularly sells the article to unrelated retail customers. *See also* Rev. Rul. 81–188, 1981–2 C.B. 211, which concerned the now-repealed manufacturers excise tax on automotive chassis and bodies. That ruling held that where a manufacturer regularly sold an article at retail in arm's length as well as non-arm's-length retail sales, the retail fair market price of the article was the lowest price at which the manufacturer regularly sold the article in the retail arm's length sales.

HOLDING

When taxable truck bodies and chassis are sold by a dealer to its wholly owned subsidiary company for use in the subsidiary's business, the lowest price at which the dealer regularly sells such articles to unrelated retail customers is the measure both of fair market price and of constructive sales price.

Section 4996.—Other Definitions and Special Rules [Windfall Profit Tax]

26 CFR 51.4996–1: Definitions.

T.D. 8103

TITLE 26—INTERNAL REVENUE.—
CHAPTER I, SUBCHAPTER D, PART
51—EXCISE TAX REGULATIONS
UNDER THE CRUDE OIL WINDFALL
PROFIT TAX ACT OF 1980

Definition of Removed from the Premises

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final Regulations.

SUMMARY: This document contains amendments to the final excise tax regulations concerning the definition of "removed from the premises" for purposes of the windfall profit tax. These amendments are being made to clarify when domestic crude oil is removed from the premises under the Crude Oil Windfall Profit Tax Act of 1980. These regulations provide the public with guidance needed for determining when the taxable event occurs for purposes of the imposition of the windfall profit tax under section 4986 of the Internal Revenue Code of 1954.

DATES: Paragraph (d)(3) of these final regulations is effective for domestic crude oil which under both rules set forth in T.D. 7844, *supra,* and the rules set forth in these final regulations is not treated as having been removed from the premises before October 23, 1986. Except as otherwise provided, paragraph (d)(2) and (4) of these final regulations is effective for domestic crude oil removed) from the premises (within the meaning of paragraph (d) of §51.4996–1, as amended) after February 29, 1980, under T.D. 7844 [1982–2 C.B. 321].

FOR FURTHER INFORMATION CONTACT: Beverly A. Baughman of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3297, not a toll-free call).

SUPPLEMENTARY INFORMATION: BACKGROUND

On April 4, 1980, the FEDERAL REGISTER published temporary and proposed regulations (45 FR 23384, 23400) [T.D. 7690, 1980–1 C.B. 259] under section 4996 and others. The temporary regulations defined removed from the premises and were required to give guidance as to when the tax imposed by the Crude Oil Windfall Profit Tax Act of 1980 is triggered. These temporary and proposed regulations were further amended by Treasury Decision 7755 and an accompanying notice of proposed rulemaking, both published on January 19, 1981 (45 FR 4873, 4950) [1981–1 C.B. 551]. The proposed regulations were finalized by Treasury Decision 7844, published on Nov. 5, 1982 (47 FR 50215).

On January 14, 1983, the FEDERAL REGISTER published proposed regulations (48 FR 1762) [LR–227–81, 1983–1 C.B. 1000] to amend §51.4996–1(d) of the Excise Tax Regulations (26 CFR Part 51), as promulgated by T.D. 7844. A public hearing was held on June 14, 1983. After consideration of all comments regarding the proposed amendments, those amendments are adopted as revised by this Treasury decision.

EXPLANATION OF PROVISIONS

In general.

Section 4986 imposes an excise tax on the windfall profit from taxable crude oil when it is removed from the premises. Current §51.4996-1(d)(1) states that, with certain exceptions, crude oil is removed from the premises when it is physically transported off the premises. Additionally, that section provides that crude oil is deemed removed when it is used, manufactured, or converted before it is removed. This document describes the exceptions to this general rule.

Injection or use in production.

One exception provided for in current §51.4996–1(d)(2) as well as in the proposed and final regulations is that crude oil that is injected into a well or used to power a production process or production equipment on the property (the proposed regulations used the term "premises") is not removed from the premises. To qualify for the exception such crude oil cannot leave the property (except for transportation to a storage facility in certain cases), nor can it be manufactured or converted. The final regulations add another qualification that requires that, in order for the exception to apply, the same person or persons who hold 100 percent of the operating interests in the portion of the property from which the injected oil is produced also must hold 100 percent of such interests in the portion of the property on which the oil is injected. Additionally, the final regulations provide that an election to treat separate and distinct reservoirs as separate properties is disregarded for purposes of this exception.

Transportation to contiguous tracts.

The proposed and final regulations clarify another exception provided for in current §51.4996–1(d)(3). This exception applies to crude oil that has not been manufactured, converted, sold or exchanged and that is to be used as powerhouse fuel, or injected into a well, on another part of the same tract or parcel of land from which it was produced or on a tract that is contiguous to the producing tract (or is in a group of tracts contiguous to the producing tract). Such crude oil may be transported between premises located on the same tract or parcel of land or from the producing tract or parcel of land to contiguous tracts or parcels of land in which the same persons hold 100 percent of the operating mineral interests without triggering removal. (The proposed regulations did not refer to premises located on the same tract or parcel of land.) However, pursuant to the proposed and final regulations, if any consideration is transferred to any holder of a mineral interest in the producing tract or parcel (or portion thereof) who holds a lesser interest or no interest in the tract or parcel (or portion) on which the crude oil is used, as compensation for the holder's interest in the transported oil, removal from the premises occurs. In the case of a holder of a lesser interest, consideration in the form of certain taxable crude oil is disregarded. In both instances the number of barrels of crude oil whose constructive sales price equals the fair market value of the total consideration transferred shall be deemed removed on the date the crude oil is transported.

For this purpose, contiguous is defined in the proposed and final regulations to require actual touching of the areas below the surface along a substantial common border that are subject to the right to produce crude oil. However, actual touching of the tracts or parcels of land on the surface is not required. For example, if a railroad right-of-way separates the tracts but the producer (or producers) who possess the right to produce in the areas on each side of the right-of-way also hold such interests in the area below the railroad right-of-way the tracts are contiguous.

Transportation to storage facilities; point of measurement.

Current §51.4996–1(d)(3)(ii) provides that crude oil shall not be considered removed from the premises when, prior to sale, it is transported a short distance to a storage facility. The final regulations clarify this storage tank exception by providing that crude oil in some instances may be transported to its first storage tank located 5 miles or less from the producing well (or in the case of an offshore well, 5 miles or less from the point the crude oil comes on shore) without triggering removal. (The proposed regulations stated that generally crude oil transported less than 2 miles from the premises to its first storage facility was deemed not removed from the premises.)

Several comments received on the proposed regulations, expressed concern that this exception might be interpreted so as to include transportation costs in the removal price of the crude oil. Therefore, this Treasury decision states that this exception is only for purposes of determining the timing of the imposition of the windfall profit tax and the date of the determination of the removal price. Additionally, these provisions clarify that the removal price of crude oil affected by the provisions is the removal price of the crude oil determined at the premises on which the crude oil was produced on the date that the crude oil is removed (or deemed removed) pursuant to §51.4996–1(d).

Additionally, several comments received on the proposed regulations suggested that the storage tank exception be amended to allow onshore-produced crude oil to be transported less than 10 miles to a storage tank without triggering removal. The commentators also recommended that the storage tank exception be only a safe-harbor rule and that the facts and circumstances of each case determine whether or not the crude oil is removed. These suggestions were rejected. Five miles or less from the producing well was determined to be a sufficient distance with regard to the transportation of onshore-produced crude oil to a storage tank. Additionally, the facts-and-circumstances test was rejected because it would be unduly difficult to administer in this case.

The storage tank exception provided for in the proposed and final regulations applies only if the crude oil has not been sold, exchanged, manufactured, or converted prior to the transportation. Removal will then generally be deemed to occur when crude oil is sold, exchanged, manufactured, converted, or withdrawn from its first storage facility.

The proposed regulations also provided that measurement of the crude oil in connection with its sale or exchange prior to its transportation to its first storage tank would trigger removal. Several commentators pointed out that this provision was unnecessary and confusing. They were concerned that this phrase might be interpreted to include the measurement of crude oil at the point of production solely for the purpose of allocating gross proceeds to producers. This language has been deleted from the final regulations.

Return to the tract or parcel of land.

The proposed and final regulations state that crude oil that is transported to the storage tank and later withdrawn from the storage facility but not deemed removed pursuant to §51.4996–1(d)(3)(ii)(A)(*2*), or (*3*) shall not subsequently be deemed removed in certain circumstances. Such crude oil shall be deemed not removed if it is returned directly from the storage tank to the property on which it was produced. Additionally, such crude oil transported directly from the storage tank to a tract or group of tracts contiguous to the producing tract shall be deemed not removed provided all the requirements regarding transportation between contiguous tracts are met.

Injected oil and recovered oil.

Current §51.4996–4 provides that, if oil that has been removed or deemed removed is injected into a well, the first crude oil recovered after injection (up to an amount equal to the amount injected) shall be deemed not removed. The final regulations expand upon this rule. They provide that if the injected oil has not been removed or deemed removed, the recovered oil shall be deemed to be the same category of crude oil as the injected oil. The categories of crude oil are tier 1 oil, tier 2 oil, newly discovered oil, tier 3 oil other than newly discovered oil, and exempt oil. Additionally, in the case of a property on which a qualified tertiary project is in effect, the recovered crude oil first shall be allocated to that portion of the production from the property that exceeds the base level (described in section 4993(b)(1)).

EFFECTIVE DATES

The amendments to the final regulations contained in paragraph (d)(3) of §51.4996–1 of this document shall apply to domestic crude oil which under both the rules set forth in T.D. 7844, *supra,* and under the rules set forth in these amendments, is not treated as having been removed from the premises before October 23, 1986. The amendments to the final regulations contained in paragraph (d)(2) and (4) of §51.4996–1 of this document shall apply to domestic crude oil removed (or deemed removed) from the premises (within the meaning of paragraph (d) of §51.4996–1, as amended) after February 29, 1980, under T.D. 7844.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that this final rule is not subject to review under Executive Order 12291. Accordingly, a Regulatory Impact Analyses is not required. Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is Beverly A. Baughman of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 51 is amended by revising paragraph (d)(2), (3), and (4) of §51.4996–1 to read as follows:

Paragraph 1. The authority for Part 51 continues to read in part:

Authority: 26 U.S.C. 7805. Section 51.4996–1(d) also issued under 26 U.S.C. 4997.

Par. 2. In §51.4996–1 the headings and texts of paragraph (d)(2), (3), and (4) are revised to read as follows:

§51.4996–1 Definitions.

* * * * *

(d) Removed from the premises; deemed removed. * * *

(2) *Crude oil not treated as removed when used for certain purposes*—(i) *In general.* Crude oil that is injected into any well on the producing property or used on the property to power a production process (such as a tertiary injection process or water flood) or production equipment (such as an artificial lift device) shall not be treated as removed from the premises under paragraph (d)(1) of this section, provided that the crude oil never left the property from which it was produced and was not manufactured or converted. In the case of crude oil so injected or used after September 23, 1986, the preceding sentence is applicable only of the person or persons who hold 100 percent of the operating mineral interests in the portion of the property from which the crude oil is produced also hold 100 percent of such interests in the portion of the property on which the crude oil is injected or used as powerhouse fuel. For example, if a property which existed on January 1, 1972, subsequently is subdivided and leased to different persons who each hold operating mineral interest in only one of the subdivisions, crude oil produced from one subdivision is treated as removed pursuant to paragraph (d)(1) of this section. For purposes of this paragraph (d)(2), if consideration is transferred to a mineral interest owner who does not hold the same percentage interest in the portion of the property from which the crude oil is produced as in the portion of the property on which the crude oil is injected or used as powerhouse fuel, the principles described in paragraph (d)(3)(i)(B)(*1*) shall apply for determing the number of barrels of crude oil that is deemed removed.

(ii) *Crude oil deemed not to have left property*—(A) *In general.* For purposes of this paragraph (d)(2), crude oil transported to a storage facility before being used on the property is deemed not to have left the property from which it was produced only if it is transported to its first storage facility pursuant to paragraph (d)(3)(ii) of this section, subsequently withdrawn from such storage facility, and used on the producing property without ever having been deemed removed from the premises pursuant to paragraph (d)(3)(ii)(A)(*2*) or (*3*) of this section. For example, assume that wells 1 and 2 on property A have separate premises. Crude oil is produced from well 1 on premises 1 and transported from premises 1 to its storage facility that is located off the property and two miles from the producing well. Later the crude oil is injected into well 2 on premises 2 without having been deemed removed from premises 1 pursuant to paragraph (d)(3)(ii)(A)(*2*) or (*3*) of this section. The crude oil is deemed not to have left the property and is not treated as removed when it is injected into well 2. However, if the crude oil is transported from premises 1 to a storage facility located more than five miles from the producing well prior to injection into either well 1 or well 2, it is removed when it is transported. For rules relating to the category of oil injected into a well and the category of crude oil recovered after injection, see paragraph (d)(4) of this section.

(B) *Separate reservoir election.* Solely for purposes of determining whether crude oil has left the property or otherwise been removed from the premises under this paragraph (d)(2), an election to treat separate and distinct reservoirs as separate properties shall be disregarded. For example, assume that a tract is underlain by two separate and distinct reservoirs which are treated as two separate properties. Crude oil produced from one reservoir is transported to its first storage facility located less than five miles from the producing well pursuant to paragraph (d)(3)(ii) of this section. Later the crude oil is injected into the second reservoir without having been deemed removed pursuant to paragraph (d)(3)(ii)(A)(*2*) or (*3*) of this section. The crude oil is deemed not to have left the property and is not treated as removed although it is used by the taxpayer (*i.e.,* reinjected into the producing reservoir).

(iii) *Removal price.* If, under this paragraph (d)(2), crude oil is not treated as removed but is later removed from the premises pursuant to this paragraph (d), its removal price shall be the constructive sales price, computed in accordance with the principles applicable for determining gross income from the property under section 613, on the date that the crude oil is removed or deemed removed from the premises. For purposes of the preceding sentence, the term constructive sales price means the constructive sales price at the premises on which the crude oil was produced, not at the physical location of the crude oil at the time is is removed (or deemed removed) pursuant to this paragraph (d).

(3) *Certain transported crude oil deemed not removed*—(i) *Transported to contiguous tracts*—(A) *In general.* This paragraph (d)(3)(i)(A) applies only for purposes of determining the timing of the imposition of the windfall profit tax and the date of the determination of the removal price (described in section 4988(c)). Except as provided in paragraph (d)(3)(i)(B) of this section, crude oil that is transported away from the premises from which it was produced to another portion of the same tract or parcel of land, or from the tract or parcel of land on which it was produced to a contiguous tract or parcel of land (or to a tract or parcel that is in a group of contiguous tracts or parcels that is contiguous to a producing tract or parcel) shall be deemed not removed from the premises if four conditions are met. These conditions are:

(*1*) The transported crude oil has not been manufactured, converted, sold, or exchanged;

(*2*) The crude oil is used to power a production process or production equipment, or is injected into a well, on a premises or tract or parcel of land described in the immediately preceding sentence;

(*3*) In the case of transportation between contiguous tracts or parcels of land, the same person or persons hold 100 percent of the operating mineral interests in each of the tracts or parcels of land; and

(*4*) In the case of transportation away from the premises to another portion of the same tract or parcel of land, the person or persons who hold 100 percent of the operating mineral interests in the portion of the property from which the crude oil is produced also hold 100 percent of such interests in the portion of the property on which the crude oil is injected or used as powerhouse fuel.

(B) *Exceptions.* (*1*) Except as provided in paragraph (d)(3)(i)(B)(*2*) of this section, paragraph (d)(3)(i)(A) does not apply if any consideration is or will be transferred to a holder of a mineral interest in the tract or parcel of land (or portion thereof) that produced the crude oil—

(*i*) Who does not hold a mineral interest in the tract or parcel (or portion) on which the crude oil is used, or

(*ii*) Who also holds a mineral interest in the tract or parcel (or portion) on which the crude oil is used that entitles that holder to a smaller share of production than the holder's share of production in the producing tract or parcel (or portion).

as compensation for the holder's interest in the crude oil transported. If any consideration is transferred, the number of barrels of crude oil whose constructive sales price (determined under the principles employed under section 613) equals the fair market value (in the case of crude oil transferred as consideration, such constructive sales price of the crude oil transferred as consideration) of the total consideration transferred shall be deemed removed on the date the crude oil is transported from the producing tract or parcel of land.

(*2*) Paragraph (d)(3)(i)(B)(*1*) of this section does not apply to taxable crude oil that is transferred as consideration to a holder of a mineral interest described in paragraph (d)(3)(i)(B)(*1*)(ii) and that is to be produced from the premises or tracts or parcels of land in the same calendar quarter as that in which the crude oil is transported pursuant to paragraph (d)(3)(i)(A) or in the immediately following calendar quarter.

(C) *Definition of contiguous.* As used in this paragraph (d)(3)(i), the term "contiguous" means actually touching along a substantial common border. There must be such actual touching below the surface of the areas that are subject to the right to produce crude oil, but physical touching of the tracts or parcels of land on the surface is not required. Thus, a road separating two tracts of land will not affect the contiguity of the tracts as long as the right to produce under the road is held by the same person or persons who hold such rights in the tracts or parcels of land on each side of the road.

(D) *Transportation to storage tank exception.* If crude oil, which has been transported to its first storage facility pursuant to paragraph (d)(3)(ii) of this section and subsequently withdrawn from such storage facility, and which has not been deemed removed from the premises pursuant to paragraph (d)(3)(ii)(A)(2) or (*3*), is transported directly from such storage facility to a premises or tract or parcel of land referred to in the second sentence of paragraph (d)(3)(i)(A) of this section, such crude oil shall be deemed not removed from the premises provided that it would have been deemed not removed if it had been transported directly to such premises, tract, or parcel from the producing premises.

(E) *Examples.* The provisions of this paragraph (d)(3)(i) may be illustrated by the following examples:

Example (1). Crude oil is transported from tract 1 where it was produced to contiguous tract 2 to power production equipment. A and B hold operating mineral interests in tracts 1 and 2 as indicated in the following table:

	Tract 1 (percent)	Tract 2 (percent)
A	80	45
B	20	55
	100	100

Additionally, C holds a royalty interest in tract 1 but not in tract 2. B agrees to pay A money to reflect the 35 percent (80% − 45%) difference in his operating mineral interests in tracts 1 and 2. A and B agree to pay C money for his royalty interest in the crude oil transported from tract 1. The number of barrels of crude oil whose constructive sales price equals the fair market value of the total consideration transferred to A and C is removed from the premises when it is transported from tract 1.

Example (2). D holds a 100% operating mineral interest in tract 3 and in tract 4. Tracts 3 and 4 are separated by a 100-foot wide area in which E railroad company holds a fee (including all mineral rights). Tracts 3 and 4 are not contiguous and, accordingly, crude oil is removed when it is transported from one of these tracts to the other.

(ii) *Transportation to a storage facility*—(A) *In general.* This paragraph (d)(3)(ii) applies only to crude oil transported away from the premises to its first storage facility. For purposes of determining the timing of the imposition of the windfall profit tax and the date of the determination of the removal price, such crude oil transported to such first storage facility located five miles or less from the producing well, or, in the case of an offshore well, five miles or less from the point the crude oil comes on shore, shall be deemed not removed from the premises provided that the transportation of the crude oil to such first storage facility is completed prior to manufacture, conversion, sale, or exchange. In those cases the crude oil shall be deemed removed on the first date that any of the following occurs:

(*1*) Withdrawal of the crude oil from such first storage facility; or

(*2*) Sale or exchange of the crude oil; or

(*3*) Manufacture or conversion of the crude oil.

(B) *Exceptions*. For exceptions to paragraph (d)(3)(ii)(*1*) of this section for crude oil returned to the property from which it was produced or to a tract or parcel of land or group of tracts or parcels of land contiguous to the one on which it was produced, see paragraphs (d)(2)(ii)(A) and (d)(3)(i)(D) of this section, respectively.

(iii) *Removal price*. If under paragraph (d)(3)(i)(A) or (D) or (ii)(A) crude oil is deemed not removed, but is later removed from the premises pursuant to this paragraph (d), its removal price shall be determined under the principles set forth in paragraph (d)(2)(iii) of this section.

(iv) *Effective date*. This paragraph (d)(3) shall apply to domestic crude oil which under both the rules set forth in T.D. 7844 (47 Fed. Reg. 50,275) 1982)), and the rules set forth in this paragraph (d)(3) is not treated as having been removed from the premises before October 23, 1986. For rules applicable to domestic crude oil not subject to this paragraph (d)(3), see 26 CFR 51.4996–1(d) (Rev. as of April 1, 1983).

(4) *Categories of oil injected into a well and recovered after injection*—(i) *Injection of oil that has not been removed*. If oil that has not been removed or deemed removed is injected into a well, the first crude oil recovered after injection and as a result of injection (up to an amount equal to the amount injected) shall be deemed to be of the same category of crude oil as the injected oil. For purposes of this paragraph (d)(4)(i) the categories of crude oil are tier 1 oil, tier 2 oil, newly discovered oil, tier 3 oil other than newly discovered oil, and exempt oil. In the case of a property on which a qualified tertiary project is in effect during the month in which the crude oil is recovered, such recovered crude oil first shall be allocated to that portion of the production from the property for the month that exceeds the base level (described in section 4993(b)(1)) for the property for that month. For example, assume that during the month, 500 barrels of tier 1 oil that have not been removed are injected into a property from which both tier 1 and tier 2 oil is produced. Additionally, a qualified tertiary project is in effect on the property. During the month 10,000 barrels of crude oil are produced from the property. Of that 10,000 barrels, 8,000 barrels is production which exceeds the base level amount for the property for the month. Pursuant to this paragraph (d)(4)(ii), 500 barrels of the 10,000 barrels produced are recovered tier 1 oil. The 500 barrels of recovered tier 1 oil are allocated to the 8,000 barrels which exceed the base level amount. Therefore, the remaining 7,500 barrels (8,000-500) of crude oil are allocated between tier 1 and tier 2 oil pursuant to section 4993(b)(3).

(ii) *Injection of oil that has been removed*. If oil that has been removed or deemed removed from the premises pursuant to this paragraph (d) is injected into a well (*e.g.*, "wash" or "frac" oil), the first crude oil recovered after injection and as a result of injection (up to an amount equal to the amount injected) shall be deemed not removed, provided the operator certifies the information required by paragraph (b)(7) of §51.6050C–1. The preceding sentence shall not apply to oil (A) which is a "hydrocarbon injectant" within the meaning of section 193(b) and (B) for which a deduction is allowable under section 193.

ROSCOE L. EGGER, JR.
Commissioner.

Approved February 9, 1986.

J. ROGER MENTZ,
Acting Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on September 22, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 23, 1986, 51 F.R. 33741)

Part IV. Items of General Interest

Withdrawal of Notice of Proposed Rulemaking—Notice of Proposed Rulemaking

Definition of Property for Purposes of the Windfall Profit Tax

LR-34-82

AGENCY: Internal Revenue Service, Treasury.

ACTION: Withdrawal of notice of proposed rulemaking—notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to the windfall profit tax on domestic crude oil imposed by title 1 of the Crude Oil Windfall Profit Tax Act of 1980. The regulations would clarify the meaning of the term "property" for purposes of the windfall profit tax. In addition, this document withdraws the notice of proposed rulemaking relating to the definition of "property" for purposes of the windfall profit tax that was published in the FEDERAL REGISTER on November 10, 1982 (47 FR 50924) [1982-2 C.B. 930].

DATES:

PROPOSED EFFECTIVE DATE

These regulations are proposed to be effective for crude oil removed after February 29, 1980.

DATES FOR COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Written comments and requests for a public hearing must be delivered or mailed by November 11, 1986. ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-34-82), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Robert H. Ginsburgh of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. (Attention: CC:LR:T) (202-566-3297).

SUPPLEMENTARY INFORMATION: BACKGROUND

This document contains proposed amendments to the Excise Tax Regulations under the Crude Oil Windfall Profit Tax Act of 1980 (26 CFR Part 51). These proposed regulations are to be issued under the authority of Code section 4997 (b) (94 Stat. 250, 26 U.S.C. 4997 (b)), which grants the Secretary of the Treasury of his delegate authority to prescribe regulations necessary or appropriate to carry out the purpose of the windfall profit tax (including changes in the application of the energy regulations), and the more general regulatory authority contained in Code section 7805 (68A Stat. 917, 26 U.S.C. 7805). This document also withdraws the proposed regulations relating to the definition of "property" for purposes of the windfall profit tax that were published in the FEDERAL REGISTER on November 10, 1982 (47 FR 50924).

Under the windfall profit tax taxable crude oil is divided into three tiers. The windfall profit tax rate depends, in part, on the tier of the crude oil. In order to determine the tier of taxable crude oil it is often necessary to determine the "property" from which the crude oil is produced. For example, the determinations of whether crude oil qualifies as crude oil from a stripper well property, newly discovered oil, or heavy oil (all these types of oil receive preferred treatment under the windfall profit tax) are made on a property-by-property basis.

"Property" is defined for windfall profit tax purposes in §150.4996-1(i) of the Temporary Excise Tax Regulations Under the Crude Oil Windfall Profit Tax Act of 1980 (26 CFR Part 150) as promulgated by Treasury Decision 7846, published on November 10, 1982 (47 FR 50858) [1982-2 C.B. 353]. The text of that Treasury decision also served as the text of a notice of proposed rulemaking published on the same day (47 FR 50924) [1982-2 C.B. 930]. Section 150.4996-1(i) provides that "property" generally is determined by reference to the geographical boundaries of the right to produce crude oil as such right existed on January 1, 1972, provided such right was in production in commercial quantities on that date. If such right was not in production in commercial quantities on January 1, 1972, the determination of "property" is generally made by reference to the geographical boundaries of the right to produce crude oil when crude oil is first produced thereafter in commercial quantities. For this purpose the term "commercial quantities" has the same meaning as that term has in proposed §51.4996-1(n). See the notice of proposed rulemaking relating to newly discovered crude oil (LR-224-81) [1982-2 C.B. 903] published on November 5, 1982 (47 FR 50306), for the content of proposed §51.4996-1(n).

Although paragraph (i)(1) of §150.4996-1 provides the general rule for determining "property," that paragraph and the notice of proposed rulemaking relating to "property" published in the Federal Register on the same date as that paragraph (47 FR 50924) reserved for subsequent publication the exceptions to the general rule. These proposed amendments would provide rules relating to the exceptions to the general rule for determining "property" as well as the general rule.

EXPLANATION OF PROVISIONS

Under the energy regulations, "property" generally was determined by reference to the right to produce crude oil. The Department of Energy and its predecessor agencies (hereinafter the term "DOE" refers to the Department of Energy and its predecessor agencies) recognized exceptions to this general rule. These exceptions included the following situations in which DOE either recognized multiple rights to produce from a single instrument, such as a lease or deed, or multiple properties from a single right to produce crude oil: (1) Separate development of specifically identified portions of a property, (2) noncontiguous tracts, (3) royalty owner accountability, (4) severance tax accountability, (5) very large tracts, and (6) separate reservoirs. In addition, DOE recognized a single property as a result of the aggregation of several separate rights to produce crude oil. Unitizations were the principal exception in this category.

The proposed amendments would amend §51.4996-4. This section would contain the rules relating to the definition of "property" for windfall profit tax purposes. This proposed section contains a general definition of "property," which is essentially the same as the definition in §150.4996-1(i)(1). In addition, paragraphs (c), (d), and (e) of proposed §51.4996-4 contain the exceptions to the general definition of "property." These exceptions are generally similar to those provided by DOE, but are mandatory rather than permissive.

Proposed §51.4996–4(b) provides a definition of the term "right to produce." This definition is essentialy the same as the definition contained in §150.4996–1(i)(2). However, proposed §51.4996–4(b) makes clear that a right to produce may arise from a farmout agreement. See examples (8), (9), (10), and (11) in paragraph (f) of §51.4996–4. No inference as to the proper treatment of farmout agreements for income tax purposes is to be drawn from their treatment under proposed §51.4996–4.

Proposed §51.4996–4(d)(6) provides that the operator of a property, rather than each producer, may elect to treat as separate properties each separate and distinct producing reservoir subject to the same right to produce. It also specifies the time and manner of making the election. Once the election is made it is irrevocable, applies to all producers who currently hold an interest in the property and all producers who acquire an interest in the property, and applies to newly-discovered producing reservoirs.

Proposed §51.4996–4(e)(2) provides that a recognized unitization shall be treated as a separate property except as otherwise provided in section 4988(b) (relating to the net income limitation). For this purpose the term "unitization" refers to the right to produce crude oil that arises from an agreement under which the persons holding the rights to produce crude oil with respect to different geographical areas agree to have the rights to produce operated on a unified basis and further agree to share in production on a stipulated percentage or fractional basis regardless of the geographical boundaries of the right to produce from which crude oil is produced. The proposed amendments make clear that an agreement merely among the holders of the working interests to operate several separate rights to produce as a single property does not result in a unitization that will be treated as a single property because the holders of the royalty interests are not parties to the agreement.

The proposed amendments provide that, in the case of a recognized unitization, if a portion of a property is not included in the unitized property, that portion is treated as a separate right to produce. However, a special rule is provided to prevent production from the nonunitized portion from being treated as newly discovered oil, stripper well oil, or heavy oil after the unitization if the production did not receive that treatment before the unitization.

COMMENTS AND REQUEST FOR PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is to be held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies of those comments to the Service.

SPECIAL ANALYSIS

The Commissioner of Internal Revenue has determined that a Regulatory Impact Analysis is not required because these final rules are not major rules under Executive Order 12291.

Although this document is a notice of proposed rulemaking which solicits public comments, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these proposed regulations was Mr. Douglas W. Charnas of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations, both on matters of substance and style.

* * * *

Proposed amendments to the regulations.

The proposed amendments to 26 CFR Part 51 relating to the definition of "property" for purposes of the windfall profit tax that were published in the FEDERAL REGISTER on November 10, 1982 (47 FR 50924), are hereby withdrawn, and the proposed amendments to 26 CFR Part 51 are as follows:

Paragraph 1. The authority citation of Part 51 continues to read in part:

Authority: Secs. 4997, 7805 Internal Revenue Code of 1954 (94 Stat. 249, 68A Stat. 917; (26 U.S.C. 4997, 7805)), * * *

Par. 2. Paragraph (c)(1) of §51.4989–1 is amended by removing "§150.4996–1(i)" and inserting in lieu thereof "§51.4996–4."

Par. 3. Section 51.4996–1 is amended by removing paragraph (i) and redesignating paragraphs (j), (k), (l), and (m) as (i), (j), (k), and (l), respectively.

Par. 4. Paragraph (b) of §51.4996–3 is amended by removing "paragraph (i) of §51.4996–1" and inserting in lieu thereof "§51.4996–4."

Par. 5. Section 51.4996–4 is added to read as follows:

§51.4996–4 Definition of property.

(a) *In general.* Except as otherwise provided in section 4988(b) and §51.4988–2 (relating to the net income limitation on windfall profit) and paragraphs (c) and (d) of this section, in the case of a right to produce crude oil in existence on January 1, 1972, that was in production in commercial quantities (as defined in paragraph (n)[1] of §51.4996–1) on that date, the "property" is determined by reference to the geographical boundaries of such right. If such right was not in production in commercial quantities on January 1, 1972, the determination of "property" is generally made by reference to the geographical boundaries of the right to produce crude oil when crude oil is first produced thereafter in commercial quantities.

(b) *Right to produce.* The right to produce crude oil is an operating or working interest. It may arise, for example, from a lease, sublease, farmout agreement or deed of a fee interest.

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[1] Section 51.4996–1(n) was proposed on November 5, 1982, 47 FR 50307.

(c) *Separate rights to produce from single instrument.* A single instrument, such as a lease or deed, shall be treated as having transferred more than one right to produce crude oil if—

(1) The instrument specifically identifies portions of the acreage covered by the instrument,

(2) The instrument creates significantly different rights and duties (particularly for exploration and drilling obligations) with respect to the specifically identified portions,

(3) The holders of the rights transferred by the instrument have in good faith relied upon such differences in their exploration and development activities,

(4) The holders of the rights transferred by the instrument have, since the inception of price controls on crude oil (or, if later, when production first began in commercial quantities from more than one such portion), consistently and historically accounted for such portions separately, and

(5) The holders of the rights transferred by the instrument have, since the inception of price controls (or, if later, when production first began in commercial quantities from more than one such portion), consistently and historically treated each such portion as a separate right to produce crude oil.

If the requirements of this paragraph are met, each specifically identified portion described in this paragraph shall be treated as a separate right to produce crude oil. The requirements of paragraph (c)(4) and (5) of this section shall be considered met if the rights transferred by the instrument are acquired after the inception of price controls and the holders of those rights have, since the acquisition of those rights (or, if later, when production first began in commercial quantities from more than one such portion), consistently and historically accounted separately for each specifically identified portion and treated each portion as a separate right to produce. If the holders of those rights consistently and historically treated specifically identified portions as separate rights to produce, but departed from such treatment to more closely comport with the definition of "property" as specifically set forth by the Department of Energy's predecessor agencies before the issuance of FEA Ruling 1977–1, the holders of those rights shall be considered to have consistently and historically treated such portions as separate rights to produce provided the holders of those rights readopted such treatment by January 1, 1978. For purposes of this section, the inception of price controls is treated as having occurred with the adoption of subpart L of 6 CFR Part 150 (38 FR 22546, August 22, 1973), effective August 19, 1973.

(d) *Separate properties from a single right to produce*—(1) *In general.* In limited situations, a single right to produce that would be a single property under the rules of paragraph (a) of this section shall be treated as more than one property. Those situations are set forth in this paragraph. Except as otherwise provided for in this paragraph and paragraph (c) of this section, a single right to produce that would be a single property under the rules of paragraph (a) of this section shall be treated as a single property (not subject to division into multiple properties).

(2) *Noncontiguous tracts.* An instrument transferring the right to produce crude oil may convey a single undifferentiated right to produce crude oil with respect to multiple, noncontiguous tracts. In this case, each noncontiguous tract shall be treated as a separate property if—

(i) The right to produce crude oil would be a single property under the rules of paragraph (a) of this section.

(ii) The noncontiguous tracts were developed and produced separately by the holders of the right to produce crude oil,

(iii) The holders of the right to produce crude oil have, since the inception of price controls on crude oil (or, if later, when production first began in commercial quantities from more than one such tract), consistently and historically accounted for each noncontiguous tract separately, and

(iv) The holders of the right to produce crude oil have, since the inception of price controls on crude oil (or, if later, when production first began in commercial quantities from more than one such tract), consistently and historically treated each noncontiguous tract as a separate property.

The principles of paragraph (c) of this section relating to whether the holders of the rights transferred by an instrument are considered to have consistently and historically accounted separately for specifically identified portions and treated each such portion as a separate right to produce crude oil shall apply for purposes of paragraph (d)(2)(iii) and (iv) of this section.

(3) *Royalty owner accountability.* A right to produce crude oil that would be treated as a single property under the rules of paragraph (a) of this section shall be treated as more than one property if—

(i) The instrument transferring the right to produce crude oil specifically identifies portions of the acreage covered by the right to produce crude oil the production from which is required to be measured and accounted for separately for purposes of accounting to royalty owners (but not overriding royalty owners, working interest owners, or other interest owners),

(ii) The instrument imposes no duty to account to the royalty owners of one such specifically identified portion for the production and sale of crude oil from another such specifically identified portion,

(iii) The holders of the right to produce crude oil have, since the inception of price controls on crude oil (or, if later, when production first began in commercial quantities from one such portion), consistently and historically accounted for such portions separately, and

(iv) The holders of the right to produce crude oil have, since the inception of price controls on crude oil (or, if later, when production first began in commercial quantities from one such portion), consistently, and historically treated each such portion as a separate property.

If the requirements of this subparagraph are met, each such specifically identified portion of the right to produce shall be treated as a separate property. The principles of paragraph (c) of this section relating to whether the holders of the rights transferred by an instrument are considered to have consistently and historically accounted separately for specifically identified portions and treated each such portion as a separate right to produce crude oil shall apply for purposes of paragraph (d)(3)(iii) and (iv) of this section. For purposes of this subparagraph, a division order is not an instrument which specifically requires production to be measured and accounted for separately for purposes of accounting to royalty owners.

(4) *Severance tax accountability.* A right to produce crude oil that would be treated as a single property under the rules of paragraph (a) of this section shall be treated as more than one property if—

(i) The instrument transferring the right to produce crude oil identifies portions of the acreage covered by the right to produce crude oil the production from which must be measured and accounted for separately for purposes of determining severance tax liability,

(ii) The severance tax liability as a result of the separate accounting is different from that which would have resulted had there not been such separate accounting,

(iii) The holders of the right to produce crude oil have, since the inception of price controls on crude oil (or, if later, when production first began in commercial quantities from one such portion), consistently and historically accounted for such portions separately, and

(iv) The holders of the right to produce crude oil have, since the inception of price controls (or, if later, when production first began in commercial quantities from one such portion), consistently and historically treated each such portion as a separate property.

If the requirements of this subparagraph are met, each such specifically identified portion of the right to produce crude oil shall be treated as a separate property. Thus, for example, separate accounting for severance tax purposes may be necessary in situations in which the rate of severance tax varies according to the value of the crude oil produced and sold from the right to produce which would be treated as a single property under the rules of paragraph (a) of this section. In such a situation, if the imposition of a severance tax has required the holders of the right to produce separately to account for production from specifically identified portions subject to the same right to produce, and if the holders of the right to produce have consistently and historically treated such specifically identified portions as separate properties, such specifically identified portions shall be treated as separate properties. However, if a severance tax is determined merely by applying a fixed rate to total production volume, separate property treatment is not allowed unless different rates of tax were applied to specifically identified portions. An *ad valorem* tax which is based on the value of crude oil remaining in reservoirs on the property is not a tax the rate of which varies according to the value of crude oil produced and sold from the property, and, accordingly is not in the nature of a severance tax the separate accounting of which would result in the treatment of specifically identified portions as separate properties. The principles of paragraph (c) of this section relating to whether the holders of the rights transferred by an instrument are considered to have consistently and historically accounted separately for specifically identified portions and treated each such portion as a separate right to produce shall apply for purposes of paragraph (d)(4)(iii) and (iv) of this section.

(5) *Very large tracts*—(i) *In general.* Separate geological structures subject to the same right to produce crude oil that would be treated as a single property under the rules of paragraph (a) of this section shall be treated as separate properties if the holders of the right to produce crude oil have, since the inception of price controls on crude oil (or, if later, when production first began from more than one such structure), consistently and historically accounted for separately and treated as separate properties each separate geological structure. The principles of paragraph (c) of this section relating to whether the holders of the rights transferred by an instrument are considered to have consistently and historically accounted separately for specifically identified portions and treated each such portion as a separate right to produce shall apply for purposes of determining whether the holders of the right to produce have consistently and historically accounted for separately and treated as separate properties each separate geological structure.

(ii) *Separate geological structures.* For purposes of this subparagraph, the term "geological structure" means layers of sedimentary rock which have been displaced from the horizontal by various forces of nature. Five general categories are recognized: (A) Faults, (B) anticlines, (C) monoclines, (D) synclines, and (E) domes.

(6) *Election to treat separate reservoirs as separate properties.* (i) *Effect of election*—(A) *In general.* The operator of a single right to produce crude oil (including a separate right to produce after the application of paragraph (c) of this section) that is treated as a single property under the rules of paragraph (a) of this section may elect to treat as separate properties each separate and distinct producing reservoir subject to the same right to produce crude oil that is not in communication with any other producing reservoir subject to the same right to produce crude oil. If an election is made, each such reservoir shall be treated as a separate property. Once made, an election is irrevocable, applies to all producers who currently hold an interest in the property and all producers who acquire an interest in the property, and applies to each separate and distinct newly-discovered producing reservoir that is not in communication with any other producing reservoir subject to the same right.

(B) *Commingled production.* For purposes of this subparagraph, reservoirs subject to the same right to produce crude oil are in communication if the production is commingled in a well bore located within the geographical boundaries of such right to produce crude oil, and all such reservoirs whose production is commingled with one another shall be treated as a single reservoir for so long as commingling continues. If production from two or more separate and distinct producing reservoirs is commingled after the effective date of an election to treat such reservoirs as separate properties, such reservoirs shall be treated as a single property as of the beginning of the month during which commingled production is begun. Production through a well bore from two or more reservoirs shall not be considered commingled if the well meets the following requirements:

(*1*) The well consists of two (or more) separate tubing strings run inside the casing (or one or more such strings and the annulus between such string or strings and the casing), each of which carries crude oil from a separate and distinct producing reservoir,

(*2*) The production from each reservoir can be separately measured at the wellhead, and

(*3*) The production capabilities of each reservoir are unaffected by any change in the production level of any other reservoir producing through the same well.

Production from two or more otherwise separate and distinct reservoirs shall not be considered commingled if the reservoirs are produced through different wells but such production is commingled in a single tank battery, provided that production is separately measured at the wellhead or that production volumes are allocated back to each well based on regular well tests.

(ii) *Method of making election.* An election pursuant to this subparagraph may be made by the operator at any time after crude oil is first produced in commercial quantities from more than one separate and distinct producing reservoir subject to the same right to produce crude oil. An election shall be effective as of the first day of the calendar month in which the election is made. However, if the election is made by the date that is 60 days after the date of publication of this subparagraph in the Federal Register in a Treasury decision, the election may be made effective as of an earlier date selected by the operator provided the operator has consistently and historically separately accounted for and treated as separate properties each separate and distinct producing reservoir subject to the same right to produce since such earlier date selected by the operator. Separate and distinct reservoirs shall not be treated as separate properties in the absence of an election pursuant to this subparagraph, notwithstanding the operator's consistent and historic treatment of such reservoirs as separate properties for price control purposes and the acceptance of such treatment by the Department of Energy (or any of its predecessor agencies), unless the operator establishes that the failure to make such election was due to reasonable cause. The principles of paragraph (c) of this section relating to whether the holders of the rights transferred by an instrument are considered to have consistently and historically accounted separately for specifically identified portions and treated each such portion as a separate right to produce shall apply for purposes of determining whether an operator has consistently and historically accounted for and treated as separate properties each separate and distinct producing reservoir. The operator shall make the election under this subparagraph by submitting a certification, signed under penalties of perjury by a petroleum engineer (who has been duly registered or certified in accordance with applicable state law, if any) to the Internal Revenue Service Center, Austin, Texas. The certification shall contain the following:

(A) A statement clearly indicating that an election is being made to treat as separate properties each separate and distinct producing reservoir subject to the same right to produce crude oil,

(B) The operator's name, address, and identifying number (employer identifying number, or, if none, social security number),

(C) A description of the property subject to the election including the location, identifying number (if any), and the names and identifying numbers or, if none, other sufficient identification of the leases or subleases composing the property.

(D) A statement that each reservoir is a producing reservoir that is separate and distinct from, and not in communication with, any other producing reservoir, and

(E) If the election is made before the date that is 60 days after the date of publication of this paragraph in the Federal Register in a Treasury decision, the date on which the election is effective.

(e) *Aggregation of rights to produce*—(1) *Aggregations other than unitizations*—(i) *In general.* An aggregation of rights to produce described in paragraph (e)(1)(ii), (iii), or (iv) of this section shall be treated as a single property provided the producers can demonstrate a bona fide reason for the aggregation.

(ii) *Undivided interests.* In certain situations, various persons may hold partial undivided interests in the right to produce crude oil from a particular area. It is not uncommon in these situations to aggregate the separate rights to produce before production begins from the area. These aggregations may occur voluntarily through a joint operating agreement or other type of agreement, or pursuant to compulsory state regulations. An aggregation in these situations in order to perfect the right to produce is considered an aggregation of separate rights to produce for purposes of this section.

(iii) *State required aggregations.* In certain situations, premises subject to separate rights to produce crude oil are required to be combined by a state regulatory agency as a condition to the operation of production activities. For example, a state regulatory agency may compel a "unit" to be formed by the owners of the tracts with respect to the surface area which overlies the portion of a reservoir that may be efficiently drained by a single well, provided the owners of at least a certain percent of the surface area agree to the formation of the unit. Such a combination of rights to produce is considered an aggregation of separate rights to produce for purposes of this section.

(iv) *Spacing requirements.* In states that maintain spacing requirements for crude oil wells, individual rights to produce crude oil may need to be combined, whether voluntary or involuntary, before a single well may be drilled and the right to produce made effective. Such a combination of rights to produce (sometimes known as a "drilling unit") is considered an aggregation of separate rights to produce for purposes of this section.

(2) *Unitizations*—(i) *In general.* A unitization (within the meaning of paragraph (e)(2)(ii) of this section) shall be treated as a single property (the "unitized property") except as otherwise provided in section 4988(b) and §51.4988–2 (relating to the net income limitation on windfall profit).

(ii) *Unitization defined.* The term "unitization" refers to the right to produce crude oil that arises from an agreement under which the persons holding the rights to produce crude oil with respect to different geographical areas agree to have the rights to produce operated on a unified basis and further agree to share in production on a stipulated percentage or fractional basis regardless of the geographical boundaries of the right to produce from which the crude oil is produced. A unitization occurs when a bona fide unitization agreement (within the meaning of paragraph (e)(2)(iii) of this section) is approved by the applicable governmental regulatory authority or by the Energy Regulatory Administration, or, if later, the effective date specifically set forth in the unitization agreement. However, notwithstanding the occurrence of the unitization, the unitization shall not be treated as having occurred for any month beginning before the unitized property sustained a significant alteration in producing patterns provided the operator of the unitized property certified (pursuant to the provisions of 10 CFR Part 205, Subpart G) to the Energy Regulatory Administration its intention to determine volumes (for price control purposes) of lower tier, upper tier, newly discovered, and stripper well property crude oil separately for all properties that constitute the unitized property. For purposes of the preceding sentence, a "significant alteration in producing patterns" means the occurrence of either (A) the application of extraneous energy sources by the injection of liquids or gases into the reservoir, or (B) the increase in production allowables for any property that constitutes the unitized property.

(iii) *Bona fide unitization agreement.* A unitization agreement is bona fide if the unitization is necessary, in accordance with sound engineering practice, to maximize production from the reservoir affected by the unitization, and if the agreement manifests an intent by the majority of the holders of royalty interests and working interests to some change in the underlying property and contractual rights of the various interest holders, particularly through their agreement to a participation formula. An agreement merely among the holders of the working interests to operate several separate rights to produce crude oil as a single property does not constitute a bona fide unitization agreement because the holders of the royalty interests are not parties to the agreement.

(3) *Special rules for unitizations or other aggregations*. If a unitized property or other aggregation treated as a single property under this paragraph encompasses less than the geographical boundaries of a right to produce crude oil as such right exists before the unitization or other aggregation, the portion of the geographical boundaries of such right to produce that is not encompassed by the unitized property or other aggregation shall be treated as a right to produce separate from the unitization or other aggregation. For purposes of section 4996(e) and §51.4996-3, crude oil produced from the portion of the right to produce crude oil that is not unitized or otherwise aggregated shall be treated as crude oil produced from property transferred as of the date of the unitization or other aggregation. However, the rule in the preceding sentence shall only apply to production from those reservoirs underlying such right to produce crude oil (as such right existed before the unitization or other aggregation) from which crude oil was produced in commercial quantities before the unitization or other aggregation through a well located within the geographical boundaries of such right to produce crude oil (as such right existed before the unitization or other aggregation).

(f) *Examples*. The provisions of this section may be illustrated by the following examples (references in the examples to production of crude oil mean production in commercial quantities):

Example (1). A purchased land in 1960 (receiving a standard special warranty deed) and used the land exclusively for farming until 1969 when he drilled a well in the southwest portion of the land. The well began producing crude oil in 1970 and is still in production. In 1973 A executed four oil and gas leases for portions of the land none of which included any area that ever had a producing well and each of which began producing crude oil in 1980. The boundaries of the "property" are determined by reference to the geographical boundaries of the fee interest held by A on January 1, 1972, because A's right to produce crude oil on January 1, 1972, was in production on that date.

Example (2). B purchased land in 1960 (receiving a standard special warranty deed) and used the land exclusively for farming. In 1973 B sold the west half of the land. In 1974 B drilled a well in the northeast portion of his land. The well began producing crude oil on February 1, 1974. "Property" is determined by reference to the geographical boundaries of B's fee interest on February 1, 1974, because those are the geographical boundaries of the right to produce crude oil when crude oil was first produced. Any "property" with respect to the land sold by B in 1973 will be determined by reference to the geographical boundaries of the right or rights pursuant to which crude oil is ultimately produced thereon.

Example (3). C purchased land in 1960 (receiving a standard special warranty deed) and used the land exclusively for farming. In 1970 C granted an oil and gas lease to D on the entire fee interest. In 1973 D drilled a well in the south half of the land. The well began producing crude oil in 1973. In 1974 D granted an oil and gas sublease to E on the north half of his lease. E drilled a well and began producing crude oil in 1974. "Property" is determined by the geographical boundaries of D's lease because those are the geographical boundaries of the right to produce crude oil when crude oil was first produced. "Property" is not determined by reference to the geographical boundaries of E's sublease because of the crude oil production from D's lease prior to execution of the sublease.

Example (4). On December 31, 1971, F granted an oil and gas lease to G on the north half of his fee interest and an oil and gas lease to H on the south half of his fee interest. Each lease provided that drilling was to commence within 5 years or the lease would expire. On January 1, 1973, G began drilling a well in the land subject to his lease. The well began producing crude on March 15, 1973. As of December 31, 1976, no well had been drilled on the land subject to H's lease and H's lease expired. G's lease was a right to produce crude oil pursuant to which the first production of crude oil after January 1, 1972, occurred. Thus, the boundaries of G's lease in 1973 constitute the "property" for purposes of the windfall profit tax. "Property" is not determined by reference to the geographical boundaries of H's lease because no crude oil was produced pursuant to that right to produce crude oil. Also, "property" is not determined by reference to the geographical boundaries of that portion of F's fee interest not subject to G's lease (upon expiration of H's lease) because no crude oil has been produced pursuant to that right to produce crude oil.

Example (5). Assume the same facts as in example (4) except that on December 31, 1973, H granted on oil and gas sublease to I on the west half of his lease an an oil and gas sublease to J on the east half of his lease. Under each oil and gas sublease drilling was to commence on the land subject to the sublease within 3 years or the sublease would expire. J drilled a well during February of 1974 which began producing crude oil that month. No production occurred on I's sublease by December 31, 1976, and, at that time, I's sublease expired. Because H's lease did not produce crude oil before H granted oil and gas subleases to I and J, "property" is determined by reference to the geographical boundaries of J's sublease. J's sublease was a right to produce crude oil pursuant to which crude oil was actually produced. "Property" is not determined by reference to the geographical boundaries of I's sublease because the sublease expired before crude oil was produced pursuant to that right to produce. "Property" is not determined by reference to the geographical boundaries of that portion of H's lease that was not subject to J's sublease (land formerly subject to I's sublease) because crude oil was not produced pursuant to H's right to produce crude oil therefrom after the expiration of I's sublease. As in example (4) another "property" is determined by reference to the geographical boundaries of G's lease.

Example (6). Assume the same facts as in example (5) except that on January 1, 1977, H granted an oil and gas sublease to K of the portion of his lease that was formerly subject to I's sublease. Under the sublease, K was to commence drilling within 1 year. K drilled a well during May of 1977 which began producing crude oil that month. "Property" is determined by reference to the geographical boundaries of K's sublease because there was no crude oil production pursuant to H's lease before H ganted oil and gas subleases to I and J nor was there crude oil production pursuant to I's sublease before it expired.

Example (7). In 1970 L acquired an oil and gas lease for a 1,600 acre tract. The lease assigned to L the right to produce crude oil from any portion of the tract for a primary term of 5 years after which the lease would expire, except as to sufficient acreage around each producing well (as of the expiration of the primary term) to constitute a drilling unit for each well. In 1971 L drilled 10 wells which began producing that year. The drilling unit for each well was 40 acres. L did not drill any other producing wells. In 1975, when the primary term of the lease expired, L's right to produce expired except for the 400 acres around the 10 producing wells. The boundaries of the "property" are determined by reference to the geographical boundaries of the 1,600 acre tract because those are the geograpical boundaries of L's right to produce crude oil on January 1, 1972, which was in production on that date.

Example (8). Assume that the right to produce crude oil for the 1,600 acre tract in example (7) was held be a lessee who entered into a farmout agreement with L in 1971. The agreement provided that L had the right to explore and drill for oil and gas on the tract for a period of 5 years, and that, for each producing well drilled by L, the lessee would assign to L the right to produce crude oil as to sufficient acreage around the well to constitute a drilling unit. In 1973 L drilled one well which began producing crude oil that year. The drilling unit for that well was 40 acres. In 1975, when the term of the agreement expired, L's right to produce expired except for the 40 acres around the producing well. The boundaries of the "property" are determined by reference to the geographical boundaries of the farmout agreement when L obtained production from the producing well. At that time the farmout agreement covered the entire 1,600 acre tract. Thus, "property" is determined by reference to the geographical boundaries of the 1,600 acre tract.

Example (9). M acquired an oil and gas lease for a 160 acre tract of land in 1965, and drilled a well in the southwest portion of the land in 1969. The well began producing crude oil in 1970, and is still producing crude oil. In 1973 M entered into a farmout agreement with N.

The agreement provided that N had the right to explore and drill for oil and gas on the east half of M's land for a period of 5 years. The agreement provided that if N drilled a well which produced crude oil, M would assign to N the entire working interest (the right to produce crude oil) for the east half of M's land and would retain an overriding royalty interest. The agreement further provided that after recovery by N of all costs of drilling, equipping, and operating the well out of the proceeds from the working interest's share of all crude oil, gas, and other hydrocarbons produced, saved and sold from the east half, M will have the right to convert the overriding royalty interest to an undivided one-half of the working interest in the east half. In 1975 N drilled a well in the southwest quarter of the east half which began producing crude oil that year, and M assigned to N the entire working interest in the east half of M's land. The boundaries of the "property" are determined by reference to the geographical boundaries of the lease held by M on January 1, 1972, because M's right to produce crude oil on January 1, 1972, was in production on that date and the farmout agreement was entered into after M's right to produce crude oil produced crude oil.

Example (10). Assume the same facts as in example (9) except that M did not drill the producing well in the southwest portion of his land until 1974, after M and N had entered into the farmout agreement. For purposes of determining property, the geographical boundaries of M's right to produce crude oil do not include the geographical boundaries of the farmout agreement because the agreement was entered into before M's right to produce crude oil produced crude oil. Thus, "property" is determined by reference to the geographical boundaries of the west half of M's land because those are the geographical boundaries of M's right to produce for property purposes when crude oil was first produced. "Property" is determined by reference to the geographical boundaries of the farmout agreement when N drilled a producing well on the east half of M's land. The fact that one-half of the working interest may revert to M after production has occurred does not affect property determinations.

Example (11). Assume the same facts as in example (10) except that the farmout agreement contains an express provision dividing the east half of M's land into quarters and requiring the quarters to be developed in a specific order, and provides that the right to produce crude oil will be transferred for a quarter when a producing well is drilled in that quarter. Also assume that N drilled a producing well in each quarter, N historically and consistently accounted for the production from each quarter separately and treated each quarter as a separate property, and that M assigned the right to produce crude oil for each quarter to N. The farmout agreement is treated as having created a separate right to produce for each quarter. "Property" is determined by reference to the geographical boundaries of each quarter of the east half of M's land at the time production first occurs from each quarter. Accordingly, each quarter is treated as a separate property. As in example (10), "property" is also determined by reference to the geographical boundaries of the west half of M's land.

Example (12). O purchased land in 1960 (receiving a standard special warranty deed), and used the land exclusively for farming until 1970 when O leased the land to P. The lease, which transferred to P the right to produce crude oil for the land, contains a provision that specifically identifies four separate tracts of the land. The lease also provides that each tract is to be developed in a specific order, and that at the end of 5 years the lease will expire except for those tracts which have a producing well. Pursuant to the terms of the lease, P drilled a well in the first tract which began producing crude oil in 1971. P developed the remaining three tracts in accordance with the terms of the lease. The last tract developed did not begin producing crude oil until 1973. From the time crude oil production began in 1971, P accounted for the production from each tract separately, and treated each tract as a separate property. Although P's lease transferred the right to produce crude oil from acreage which produced crude oil on January 1, 1972, "property" is not determined by reference to the geographical boundaries of P's lease. Rather, P's lease is treated as having transferred a separate right to produce for each tract. Thus, the geographical boundaries of each separate tract constitute a "property" for purposes of the windfall profit tax at the time production first occurs from that tract.

Example (13). Assume the same facts as in example (12) except that P, from 1971 until 1974, accounted for the production from each tract separately, and treated each tract as a separate property, but departed from that treatment in 1975, and began treating the four tracts as one property because he thought this treatment to more closely comport with the definition of "property" as explained in FEA Ruling 1975–15. Also assume that P readopted his initial treatment of the four tracts as separate properties in 1977 after the issuance of FEA Ruling 1977–1, and that P has consistently and historically continued such treatment since 1977. Although P has not actually met the requirements of paragraph (c)(4) and (5) of this section, he is treated as having met those requirements. Accordingly, the geographical boundaries of each tract constitute the "property" for purposes of the windfall profit tax.

Example (14). Q purchased land in 1960 (receiving a standard special warranty deed), and used the land exclusively for farming until 1970 when Q leased the land to R. The lease, which transferred to R the right to produce crude oil for the land, contains a provision that specifically identifies two separate tracts of the land, and requires production from each tract to be measured and accounted for separately. The lease also provides that (1) Q's son will receive from R a ⅐ royalty for one of the tracts and that Q's daughter will receive a ⅙ royalty for the other tract, (2) the lease will expire at the end of 5 years except for the tracts which have a producing well, and (3) R has no duty to account to the daughter for production from the son's tract or to the son for production from the daughter's tract. In 1971 R drilled a well in the son's tract which began producing crude oil that year. In 1973 R drilled a well in the north half of the daughter's tract. From the time crude oil production began in 1971, R accounted for the production from each tract separately, and treated each tract as a separate property. Although R had a single right to produce crude oil which produced crude oil on January 1, 1972, "property" is not determined by reference to the geographical boundaries of R's single right to produce (*i.e.*, R's lease). Rather, the geographical boundaries of each separate tract (*i.e.*, the son's tract and the daughter's tract) constitute a "property" for purposes of the windfall profit tax.

Example (15). (i) Assume the same facts as in example (14) except that in 1973 R assigned the right to produce crude oil for the south half of the daughter's tract before R drilled the well in the daughter's north half. Although R had assigned the right to produce for the south half of the daughter's tract before that tract produced crude oil, the geographical boundaries of the daughter's tract (*i.e.*, the north and south halves together) constitute a "property" for purposes of the windfall profit tax (except as otherwise provided in paragraph (d) of this section), because without the royalty owners accountability exception, which treats R's lease as two properties, R's lease would create a single property.

(ii) Assume further that two separate and distinct producing reservoirs that are not in communication with one another each underlie both the son's and daughter's tract. If R elects to treat the two reservoirs as separate properties, the son's tract will be treated as two properties and the daughter's tract will be treated as two properties. Thus, because of the combination of the royalty owner accountability exception (§51.4996–4(d)(3)) and the election to treat separate reservoirs as separate properties (§51.4996–4(d)(6)), the land covered by R's lease is treated as four separate properties.

Example (16). In 1965, five separate fee interest owners of five separate, contiguous tracts executed a single oil and gas lease which assigned their separate rights to produce gas and crude oil to S and retained a royalty interest. Under the terms of the lease the fee interest owners are to receive an amount equal to ⅛ of the production. In 1970 S assigned its right to produce to T before there was any production. The instrument assigning the right to produce specifically identified the five separate, contiguous tracts. In 1971 T drilled a well in one of the tracts which began producing crude oil that year. By 1975 T had fully developed the five tracts. Under the state law, T is required to separately account for the royalties for each of the five tracts covered by the lease because the lease does not state that the royalties must be apportioned. From the time crude oil production began in 1971, T accounted for the production from each tract separately, and treated each tract as a separate property. Although the instrument transferring the right to produce does not contain a provision specifically requiring production from specifically identified portions to be measured and accounted for separately, "property" is determined by reference to the geographical boundaries of each tract because T is required by state law to separately account for the royalties for each of the five tracts and T historically and consistently accounted for each tract separately and treated each tract as a separate property.

Example (17). U purchased land in 1960 (receiving a standard special warranty deed), and used the land exclusively for farming until 1971 when he granted an oil and gas lease on the north half of this land to V and an oil and gas lease on the south half to W. In 1975 V and W executed a single instrument by which they assigned their separate rights to produce to X. V and W each retained an overriding royalty interest. The instrument contains a provision that specifically identifies the two separate tracts, and requires production from each tract to be measured and accounted for separately for purposes of accounting for the overriding royalties. In 1975 X drilled a well in each tract, and each well began producing crude oil that year. From the time crude oil production first began in 1975, X accounted for the production from each tract separately, and treated each tract as a separate property. "Property" is determined by reference to the geographical boundaries of X's right to produce crude oil (both the north and south halves) because those are the geographical boundaries of the right to produce at the time of first production. "Property" is not determined by reference to the geographical boundaries of each tract because separate accounting for overriding royalties does not create separate properties from a single right to produce.

Example (18). Y purchased land in 1960 (receiving a standard special warranty deed), and used the land exclusively for farming until 1971 when he granted an oil and gas lease to Z on the entire fee interest. In 1973 Z, an integrated oil company, drilled a well in the southwest portion of the land which began producing crude oil that year. In 1974 Z drilled two more wells in the southwest portion of the land each of which began producing crude oil that year. The three wells are producing from the same geological structure, but no two wells are producing from the same reservoir. Z measures production from each well separately. For a 12-month period the average daily production from the three wells does not exceed 10 barrels per well. However, production from one well exceeded 10 barrels per day during that period and at all other times. In 1979 Z drilled a well in the northeast portion of the land. This well produces from a different geological structure than the other three wells. Z has historically and consistently accounted for the production from this well separately from the other three wells and has treated this well as a separate property. Z has two properties for windfall profit tax purposes. The geological structure containing the three wells is treated as one property and the geological structure containing the 1979 well is treated as another property. Production from the geological structure containing the three wells qualifies as tier 2 oil because that geological structure is treated as a stripper well property. Production from the geological structure containing the 1979 well is newly discovered oil because that property did not produce crude oil during 1978.

Example (19). Assume the same facts as in example (18) except that Z elects to treat each reservoir as a separate property. Because Z has four separate and distinct producing reservoirs each of which is not in communication with any other reservoir, Z has four properties for windfall profit tax purposes. The reservoir which began production in 1979 is treated as a newly discovered crude oil property. The two reservoirs which each did not exceed 10 barrels per well per day for a 12-month period qualify as stripper well properties. However, production from the reservoir that has always exceeded 10 barrels per well per day is treated as tier 1 oil as of the effective date of the election.

Example (20). A purchased land in 1960 (receiving a standard special warranty deed), and used the land for farming until 1971 when he granted an oil and gas lease to B on the west half of the land and an oil and gas lease to C on the east half. X and Y are separate and distinct reservoirs which each underlie both the west and east halves of A's land. In 1972 B drills a well in the west half which begins producing crude oil from reservoir X that year. In 1973 B reworks the 1972 well and begins producing crude oil from reservoir X as well as reservoir Y. After B reworks the well, the well meets the requirements of paragraph (d)(6)(i)(B) of this section. The production from reservoir X is not commingled in the well bore with the production from reservoir Y. In 1974 C drills a well in the east half which begins producing crude oil from reservoirs X and Y that year. The production from reservoir X is commingled in the well bore with the production from reservoir Y. C may not elect to treat reservoirs X and Y as separate properties because their production is commingled. However, the fact that the production from X and Y is commingled in the well bore located on C's property does not affect B's right to elect to treat reservoirs X and Y as separate properties. The production from reservoir X is not commingled with the production from reservoir Y in the well bore located on B's property. Thus, B may elect to treat reservoirs X and Y as separate properties.

Example (21). On January 1, 1983, a bona fide unitization agreement is approved by the state regulatory agency pursuant to which properties D, E, F, and the west half of G are unitized. The west half of G had production during 1978, but the east half had no producing wells located on it during 1978. On July 1, 1983, a well is drilled on the east half of G, and begins producing crude oil that month from the same reservoir from which G had previously produced crude oil. D, E, F, and the west half of G are a unitized property which is treated as a single property. The east half of G is treated as a separate right to produce after the unitization and creates a property at the time crude oil is produced from the well drilled on July 1, 1983. Production from the east half of property G is not newly discovered crude oil because production from that reservoir underlying that half is treated as production from a transferred property as of the date of the unitization for purposes of section 4996(e) and §51.4996–3 and production from G did not qualify as newly discovered crude oil before the unitization.

Example (22). Assume the same facts as in example (21) except that on July 1, 1983, a well is drilled on the east half of G, and begins producing crude oil that month from a different reservoir than that from which G had previously produced crude oil. Production from the well drilled on July 1, 1983, is not treated as production from a transferred property for section 4996(e) and §51.4996–3 purposes because no crude oil was produced from that reservoir through a well located on G before the unitization.

These proposed amendments are to be issued under the authority of Code section 4997(b) (94 Stat. 250, 26 U.S.C. 4997(b)), which grants the Secretary of the Treasury or his delegate authority to prescribe regulations necessary or appropriate to carry out the purpose of the windfall profit tax (including changes in the application of the energy regulations), and the more general regulatory authority contained in the Code section 7805 (68A Stat. 917, 26 U.S.C. 7805).

ROSCOE L. EGGER, JR.
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on September 24, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 25, 1986, 51 F.R. 34095)

Foundations Status of Certain Organizations

Announcement 86–104

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

Academy Arms Corp., Oneonta, NY
Adirondack Repertory Dance Theatre, Inc., Glenn Falls, NY
Alderwood Athletic Association, Alderwood, WA
Alternative Childbirth Taskforce, Inc., Evansville, IN
Anthracire Heritage, Inc., Shamokin, PA
Asean-U.S. Information Center Ltd., Annandale, VA
BJM Foundation, Inc., Kenton, OH
Burnside Housing Corporation, Bronx, NY
Caleb Foundation, Detroit, MI
Calumet Unemployed Workers Center, Inc., Gary, IN
Columbia Youth Soccer Federation, Vancouver, WA
Delaware Amateur Bowling Association, Wilmington, DE
Eielson Flyers Parent Booster Association, Fairbanks, AK
Eisenhower Basketball Booster Club, New Berlin, WI
Environmental Modification Laboratories, Inc., Paramus, NJ
Evangelist Roosevelt Moore's Crusade for Christ, Detroit, MI
Evergreen Park Central Junior High School Sports Group, Evergreen Park, IL
Friends of Cite Simone, Inc., Adelphi, MD
Garden City Parent Teacher Organization (P.T.O.), Indianapolis, IN
Head Injury Support Group of Southern New Jersey, Inc., The, Cherry Hill, NJ
Hegira, Inc., Westfield, MA
His Ministries, Inc., Rochester, IN
Inner City Nursing Home Resident Foundation, Cleveland, OH
Inventors Council of Ohio, Inc., Hilliard, OH
Korean Association of New York, Inc., New York, NY
Latino Educational Media Center, Inc., The, Bronx, NY
Lighthouse Christian Ministries, Columbus, OH
Lukas Foundation for the Mentally Handicapped, Inc., The, Little Neck, NY
Lutheran Housing Services, #4, Inc., Toledo, OH
Masonic Retirement Village, Inc., Taylor Mill, KY
Mattawamkeag Housing Corp., Lincoln, ME
Media Arts Growth Network Foundation, Cleveland, OH
Met Enterprises, Inc., Highland Park, MI
Michigan Crime Investigating Commission, Dearborn, MI
Middlesex County Bar Foundation, Inc., Cambridge, MA
Morristown Wrestling Club, Inc., Convent Station, NJ
National Hall of Fame for Persons with Disabilities, Inc., Columbus, OH
National Youth Science Camp Alumni Association, Inc., Morgantown, WV

Nebraska Coalition for Victims of Crime, Lincoln, NE
Neighborhood News, Inc., South Bend, IN
Nevins Towers Ltd., Methuen, MA
New Castle Indiana Elderly, Inc., Columbus, OH
New England Rural Community Assistance Program, Bellows Falls, VT
New Jerusalem Band, Lowellville, OH
New Life Foundation, Inc., Indianapolis, IN
New Nature Ministries, North Royalton, OH
Noble County Chamber of Commerce Elderly Housing Corp., Caldwell, OH
Noblesville Public Library Foundation, Inc., Noblesville, IN
Northeastern Indiana Emergency Medical Services, Inc., Fort Wayne, IN
Northern Ohio Early Music Society, Cleveland, OH
Northwest Network for a Nuclear Free and Independent Pacific, Seattle, WA
Norwood Band Boosters, Norwood, OH
Nouvelle Espoir Development, Cleveland, OH
OBGC III, Inc., Columbus, OH
Olivedale Fourth Housing Corp., Lancaster, OH
Olivedale Second Housing Corp., Lancaster, OH
Olivedale Third Housing Corporation, Lancaster, OH
One on One Program of Logan County, Bellfontaine, OH
Opera Pia International, Inc., New York, NY
Orchard Place Housing Corp., Lancaster, OH
Orchestra Parents Association of the Sandusky High School, Sandusky, OH
Oregon Avicultural Foundation, Portland, OR
Outwaite Homes Resident Council, Cleveland, OH
Oxford Revitalization Project, Inc., Oxford, NY
Parent Watch, Inc., Sparta, NJ
Phoenixville Youth/Babe Ruth League, Phoenixville, PA
Pine Lake Bible Grounds, Inc., Caldwell, OH
Pinecroft Acres, Inc., Troy, OH
Plaza View III, Inc., Youngstown, OH
Police Athletic League of Washington C. H. Ohio, Washington Court House, OH
Poltava Center, Inc., Parma, OH
Pops at the Park, Inc., Richmond, KY
Pretty Lake Adventure Centre, Inc., Kalamazoo, MI
Private Industry Council of Southwest Indiana, Inc., Evansville, IN
Proclaimed Word Ministries, Inc., New Martinsville, WV
Proclaimer Ministries, Inc., Martinsville, IN
Project Kids, Inc., Detroit, MI
Public Information and Education Committee, Inc., Louisville, KY
Rainbow House, Inc., Rowlesburg, WV
Reach, Inc., Florence, KY
Residential Care Center of Paducah, Inc., Paducah, KY
Residential Care Consortium Inc., Fall River, MA
Richard Allen Manor, Inc., Youngstown, OH
Roseview Manor, Inc., Williamstown, KY
Rough River Development, Inc., Leitchfield, KY
Rural Ohio Student Health Association, Toledo, OH
St. Charles Community Schools Foundation, St. Charles, MI
St. Vincent DePaul Society of Christ The King Parish, Inc., Madisonville, KY
Salamonie Area Historical Society, Inc., Warren, IN
Salt of the Earth Ministries, Bowling Green, KY
Salt Pond Community Broadcasting Company, South Blue Hill, ME
Samoan Community Services Center, Seattle, WA
Seattle Council for the Church and Social Action, The, Seattle, WA
Second Generation of Westchester, Inc., White Plains, NY
Seymour Kick-Off Club, Seymour, CT
Shawn Whitney Institute, Inc., Cranbury, NJ
Sheffield-Sheffield Lake Band Boosters, Inc., Sheffield Lake, OH
Sheffield Youth Hockey, Inc., Sheffield, MA
Sister City of Eaton, Inc., Eaton, OH
Solisti New York, Inc., New York, NY
South Central Endowment Foundation, Inc., Bloomington, IN
South Park Preservation Works, Inc., Dayton, OH
South Western Indiana Mavericks, Inc., Santa Claus, IN
Step Forward Enterprises, Inc., Steubenville, OH
Stryker Community Emergency Pantry, Stryker, OH
Substance Abuse Council Of The Rockaways, The, Hibernia, NJ
Sudan Illustrators, Inc., St. Louis, MO
Summit County Crisis Pregency Center, Akron, OH
Sunriver Caritable Fund, Inc., Sunriver, OR
Therapeutic Equestrian Association of Minnesota, Inc., Forest Lake, MN
Tipi, Inc., St. Paul, MN
Tippecanoe Crime Stoppers, Inc., Lafayette, IN
Tommy Hawk Ministries, Inc., Reynoldsburg, OH
Toxic Shock Syndrome Foundation, Southfield, MI
Toys to Share, Logan, OH
Tribute to Vietnam Veterans, Columbus, OH
Trotwood Elderly, Inc., Columbus, OH
Troupe Du Jour, Seattle, WA
UCT Ray of Hope, Inc., Columbus, OH
UCT Ray of Hope Florida, Inc., Columbus, OH
UCT Ray of Hope Kentucky, Inc., Columbus, OH
UCT Ray of Hope Zanesville, Inc., Columbus, OH
United Against Hunger, Inc., St. Joseph, MI
Universal Being, Inc., Columbus, OH
Universal Mind Community Church, Inc., Westerville, OH
Upper Ohio Valley Sexual Assault Help Center, Inc., Wheeling, WV
Urban League of Greater Toledo, Inc., Toledo, OH
Vietnam Veterans Leadership Program of Kentucky, Inc., Louisville, KY
Vincennes Swim Team, Inc., Vincennes, IN
Vistorious Women, Inc., Chavies, KY
WWD Development Corporation, Flint, MI
Waha, Inc., Wheeling, WV
Walloon Conservancy, Petoskey, MI
Warren Avenue Baptist Church Housing Project, Inc., Detroit, MI
Wayne County Sheriff's Crime Prevention Program, St. Clairs Shores, MI
West End Medical Center, Inc., Louisville, KY
West Virginia Council of Home Health Agencies, Inc., Morgantown, WV
Western Kentucky Kidney Procurement Agency, Inc., Louisville, KY
Westwood Housing Association, Inc., Centerville, OH
Williamsburg Area Community Center, Inc., Williamsburg, IN
Williamsburg Junior Athletic Association, Williamsburg, OH
Youth Coalition for Social Concerns, Inc., Ypsilant, MI
Zanesville City Schools Academic Fund, Zanesville, OH
Zionsville Area Shepherd Center, Zionsville, IN

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practictioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Robert D. Digby	North Little Rock, AR	Certified Public Accountant	Four Months from July 29, 1986
Jeffrey E. Ellis	Rockland, ME	Certified Public Accountant	Indefinte from July 2, 1986
Charles L. Honey	Prescott, AR	Attorney	One Year from July 2, 1986
Bernhardt Karp	Hudson, NY	Attorney & Certified Public Accountant	Indefinite from July 29, 1986
George N. Meros	Springfield, MO	Attorney	Indefinite from July 25, 1986
William G. Waldrop	Adamsville, AL	Certified Public Accountant	Indefinite from July 17, 1986

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to identify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
David P. Rosenberg	Philadelphia, PA	Indefinite effective August 13, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR— Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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______	1948-2	8.50
______	*1949-1*	*8.00*
______	*1949-2*	*3.25*
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______	1952-2	8.00
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______	1953-2	13.00
______	1954-1	13.00
______	1954-2	13.00
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______	1978-3-2	9.50
______	1979-1	15.00
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The Introduction on page 3 describes the purpose and content of this publication. The weekly Internal Revenue Bulletin is sold on a yearly subscription basis by the Superintendent of Documents. Current subscribers are notified by the Superintendent of Documents when their subscriptions must be renewed.

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Internal Revenue

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Bulletin No. 1986–43
October 27, 1986

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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–123, page 4.
Fringe benefits; aircraft valuation formula. For purposes of section 1.61–2T(g) of the temporary regulations, relating to the rule for valuing noncommercial flights on employer-provided aircraft, the Standard Industry Fare Level (SIFL) cents-per-mile rates and the terminal charges in effect on June 30, 1986, and for prior periods are set forth. Rev. Rul. 86–65 superseded.

Rev. Rul. 86–125, page 4.
Controlled corporation; stock distribution; active business. The active business requirement under section 355(b) of the Code is not met with regard to a rental office building if the building is managed by an unrelated real estate management company acting as an independent contractor. The limited activities of the corporation, undertaken through its president, are substantially indistinguishable from those carried on by a prudent real estate investor Rev. Rul. 73–237 distinguished.

Rev. Rul. 86–126, page 5.
Controlled corporation; stock distribution; active business. The active business requirement under section 355(b) of the Code is not met because of the absence of substantial operational and managerial activities under the circumstances described, where the business consists of leasing farmland to tenant farmers who plant, raise, harvest and sell the crop using their own equipment and supplies. The limited activities of the corporation, undertaken through its officers, in leasing the land, providing advice and consultation, and reviewing accounts are not substantial enough to meet section 355(b) requirements. Rev. Rul. 73–234 distinguished.

Rev. Proc. 86–38, page 10.
Automobile expenses; standard mileage rate. The standard mileage rate for 1986 for the first 15,000 miles of business use of an automobile that is not fully depreciated will be 21 cents per mile and 11 cents per mile for business use in excess of 15,000 miles. Rev. Proc. 82–61, as modified by Rev. Procs. 83–74, 84–72 and 85–49, is further modified.

Notice 86–11, page 9.
The applicable interest rate on the amount of additional tax attributable to any nonqualified withdrawals from a capital construction fund established under section 607 of the Merchant Marine Act is 11.09 percent for withdrawals made in taxable year 1986.

Announcement 86–105, page 19.
This Bulletin contains a list of organizations that no longer qualify as organizations contributions to which are deductible under section 170(c)(2) of the Code.

ESTATE TAX

Notice 86–12, page 9.
Technical amendments are set forth to section 20.2055–2 of the regulations, adopted by T.D. 8069, that relate to qualified conservation contributions.

EXCISE TAXES

T.D. 8102, page 6.
Regulations under sections 4701 and 6011 of the Code relate to the tax imposed on the issuer of registration-required obligations which are not issued in registered form.

LR-225-81, page 11.
Proposed regulations under section 4996 of the Code relate to production from a unitized property of imputed stripper well crude oil, imputed heavy crude oil, and imputed newly discovered crude oil.

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Finding Lists begin on page 24.
Announcement of Disbarments and Suspensions begin on page 20.
Announcement of Notice of Proposed Rulemaking on page 22.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 61.—Gross Income Defined

26 CFR 1.61–2T: Taxation of fringe benefits.

Fringe benefits; aircraft valuation formula. For purposes of section 1.61–2T(g) of the temporary regulations, relating to the rule for valuing noncommercial flights on employer-provided aircraft, the Standard Industry Fare Level (SIFL) cents-per-mile rates and the terminal charges in effect on June 30, 1986, and for prior periods are set forth. Rev. Rul. 86–65 superseded.

Rev. Rul. 86–123

For purposes of fringe benefit taxation under section 61 of the Internal Revenue Code, section 1.61–2T(g) of the Temporary Income Tax Regulations provides a rule for valuing noncommercial flights on employer-provided aircraft. Section 1.61–2T(g)(5) of the temporary regulations sets forth an aircraft valuation formula to determine the value of such flights. The value of a flight is determined by multiplying the base aircraft valuation formula for the period during which the flight was taken by the appropriate aircraft multiple provided in section 1.61–2T(g)(7) and then adding the applicable terminal charge. The value of a particular flight during the first 6 months of a calendar year is determined by using the base aircraft valuation formula (also known as the Standard Industry Fare Level formula or SIFL) and the terminal charge in effect on December 31 of the preceding year. The value of a particular flight during the last 6 months of a calendar year is determined by using the SIFL formula and terminal charge in effect on June 30 of that year. The SIFL cents-per-mile rates in the formula and the terminal charge are calculated by the Department of Transportation and are revised semi-annually.

The Department of Transportation has determined that the terminal charge in effect on June 30, 1986, is $26.02 and the SIFL formula in effect on June 30, 1986, is $.1423 per mile for the first 500 miles, $.1085 per mile for miles between 501 and 1500, and $.1043 per mile for miles over 1500.

The following chart sets forth the cumulative terminal charges and SIFL mileage rates:

Period	*Terminal Charge*	*SIFL Mileage Rates*
1/1/85–6/30/85	$27.05	Up to 500 miles = $.1480 per mile
		501–1500 miles = $.1128 per mile
		Over 1500 miles = $.1085 per mile
7/1/85–12/31/85	$25.62	Up to 500 miles = $.1402 per mile
		501–1500 miles = $.1069 per mile
		Over 1500 miles = $.1028 per mile
1/1/86–6/30/86	$26.19	Up to 500 miles = $.1433 per mile
		501–1500 miles = $.1092 per mile
		Over 1500 miles = $.1050 per mile
7/1/86–12/31/86	$26.02	Up to 500 miles = $.1423 per mile
		501–1500 miles = $.1085 per mile
		Over 1500 miles = $.1043 per mile

EFFECT ON OTHER REVENUE RULING

Rev. Rul. 86–65, 1986–19 I.R.B. 5, is superseded.

Section 162.—Trade or Business Expenses

26 CFR 1.162–17: Reporting and substantiation of certain business expenses of employees.

Simplified, optional method for computing the allowable deduction for the cost of operating an automobile for business purposes. See Rev. Proc. 86–38, page 10.

Section 167.—Depreciation

26 CFR 1.167(a)–1: Depreciation in general.

Simplified, optional method for computing the allowable depreciation deduction for the business use of an automobile. See Rev. Proc. 86–38, page 10.

Section 274.—Disallowance of Certain Entertainment, Etc., Expenses

26 CFR 1.274–5: Substantiation requirements.

Simplified optional method for computing allowable deductions for the cost of operating an automobile for business purposes. See Rev. Proc. 86–38, page 10.

Section 355.—Distribution of Stock and Securities of a Controlled Corporation.

26 CFR 1.355–1: Distribution of stock and securities of controlled corporation.

Controlled corporation; stock distribution; active business. The active business requirement under section 355(b) of the Code is not met with regard to a rental office building if the building is managed by an unrelated real estate management company acting as an independent contractor. The limited activities of the corporation, undertaken through its president, are substantially indistinguishable from those carried through its president, are substantially indistinguishable from those carried on by a prudent real estate investor. Rev. Rul. 73–237 distinguished.

Rev. Rul. 86–125

ISSUE

Whether a corporation is considered to be engaged in the active conduct of a trade or business within the meaning of section 355(b) of the Internal Revenue Code and section 1.355–1(c) of the Income Tax Regulations, under the following circumstances.

FACTS

P is a closely held corporation, which for more than 5 years has operated an insurance brokerage business. In addition, *P* has held all the stock of a subsidiary corporation, *S*, for more than 5 years. *S* owns a downtown office building, but *Z*, an unrelated real estate management company acting as an independent contractor, has been under contract to manage the property for many years. *Z* supplies and supervises janitors and maintenance personnel for *S's* office building. *Z* also arranges for all repairs to be made to the building by independent contracting companies. *Z* collects rents, pays all bills, including gas, water, sewage, electricity, and insurance, and, after deducting a monthly fee, remits the balance each month to *S*. *Z* advertises for tenants and negotiates the terms of the leases. Tenant complaints are directed to *Z*.

A, the president and principal stockholder of *P* and an officer of *S*, devotes some time to the operation of the office building. *A* visits the building to insure that the cleaning and maintenance done by *Z's* employees are done properly. In addition, *A* approves the leases negotiated by *Z's* employees and the contracts entered into for repair of the building. *A* attends to all matters concerning zoning, building permits, and other local laws and ordinances affecting the building. No other officers or employees of *P* or *S* attend to the operation of the office building. *P's* outside accountant audits monthly the itemized list of income and expenses collected and paid by *Z* and reports the results to *S*.

X, an unrelated corporation, operates a larger insurance brokerage business. *X* desired to acquire the insurance brokerage business of *P* solely in exchange for *X* voting common stock. *X*, however, would not acquire *P* if *P* continued to hold the *S* stock. The management of *P* believed the association of its business with *X* would ensure the future growth and profitability of *P*. Accordingly, *P* distributed the stock of *S* pro rata to the *P* shareholders. Since the distribution, *S* has continued to use the services of *Z* as it had prior to the transaction.

Except for the question here at issue, regarding the active conduct of a trade or business, the transfer meets all the requirements of section 355 of the Code and the regulations thereunder.

LAW AND ANALYSIS

Section 355(a) of the Code provides that under certain circumstances a corporation may distribute stock or securities in a corporation it controls to its shareholders or security holders in a transaction that is nontaxable to such shareholders or security holders. Furthermore, such a distribution of a subsidiary's stock can qualify for section 355 treatment when such distribution is followed by a second nonrecognition transaction in which the distributing corporation shareholders exchange their stock for stock in another corporation. Rev. Rul. 68–603, 1968–2 C.B. 148.

Section 355(b) of the Code requires that both the distributing and controlled corporations be engaged, immediately after the distribution, in the active conduct of a trade or business that has been actively conducted throughout the 5-year period ending on the date of distribution.

To meet the requirements of section 355(b) of the Code, each corporation must, as stated in *Rafferty v. Commissioner*, 452 F.2d 767, 772 (1st Cir. 1971), *cert. denied*, 408 U.S. 922 (1972), "engage in entrepreneurial endeavors of such a nature and to such an extent as to qualitatively distinguish its operations from mere investments. Moreover, there should be objective indicia of such corporate operations." Such objective indicia are found in active and substantial managerial and operational activities of the corporation. In addition, this business activity has to be activity of the corporation itself (through its officers and employees) and not the activity of independent contractors. Rev. Ruls. 80–181, 1980–2 C.B. 121, 79–394, 1979–2 C.B. 141, and 73–234, 1973–1 C.B. 180.

In Rev. Rul. 73–237, 1973–1 C.B. 184, it was held that a corporation engaged in the construction industry general contracting business is engaged in the active conduct of a trade or business within the meaning of section 355(b) of the Code, despite its utilization of independent subcontractors. However, in that revenue ruling, *X* corporation utilized its own salaried employees to submit bids, negotiate and enter into contracts with principals and with subcontractors, purchase or lease equipment and supplies, and supervise subcontractors to ensure compliance with contract specifications. As general contractor, *X* had the primary responsibility for the completion of each job. In analyzing *X's* activity in that revenue ruling, consideration has to be given to the fact that *X* was engaged not in construction, as such, but in general contracting. The business of general contracting is to an extent unique in that it presupposes that most, or all, of the actual construction work will be contracted out to subcontractors. However, the operation of a rental office building does not presuppose that either the managerial or operational activity will be contracted out.

In Rev. Rul. 73–237, the activity of *X*, carried on through its own employees, constituted active and substantial managerial and operational activity in the general contracting business. This activity of *X* contrasts with the activity carried on by *S* (through its officer) in the present situation. Here, the operational and management activity of the office building rental business is largely performed either by *Z* through *Z's* employees, or by independent contractors hired by *Z*. Clearly, *S* is not engaged in active and substantial operational and managerial activity with regard to the office building rental business. Although some of *S's* activities could be considered to be either managerial or operational, these activities are not different from those a prudent investor would be expected to undertake, and are not enough to "qualitatively distinguish its operations from mere investments." Thus, Rev. Rul. 73–237 is distinguishable from the present situation.

HOLDING

Because of the absence of substantial operational and managerial activities, the active business requirement of section 355(b) of the Code is not met, and the distribution of the stock is not governed by section 355. The *P* shareholders' receipt of the *S* stock constitutes a distribution of property made by *P* to its shareholders subject to the provisions of sections 301 and 311.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 73–237 is distinguished.

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26 CFR 1.355–1: Distribution of stock and securities of controlled corporation.

Controlled corporation; stock distribution; active business. The active business requirement under section 355(b) of the Code is not met because of the absence of substantial operational and managerial activities under the circumstances described, where the business consists of leasing farmland to tenant farmers who plant, raise, harvest and sell the crop using their own equipment and supplies. The limited activities of the corporation, undertaken through its officers, in leasing the land, providing advice and consultation, and reviewing accounts are not substantial enough to meet section 355(b) requirements. Rev. Rul. 73–234 distinguished.

Rev. Rul. 86–126

ISSUE

Whether a corporation is considered to be engaged in the active conduct of a trade or business within the meaning of section 355(b) of the Internal Revenue Code and section 1.355–1(c) of the Income Tax Regulations under the following circumstances.

FACTS

A and *B* are the only officers and shareholders of *P* corporation. Each has held

50 percent of *P*'s outstanding common stock for more than 5 years. *A* and *B* are both farmers who are engaged in the business of farming their own individual tracts of farmland not owned by *P*. *P* has for more than 5 years held title to large tracts of farmland elsewhere in the same state. Each tract of land held by *P* is leased for one year at a time to a tenant farmer who has agreed with *P* to share one-half of all income and expenses of the farm. Each party to the lease is responsible for securing the financing necessary to pay that party's share of expenses. In the case of each tract leased, the planting, raising, and harvesting of corn and soybeans (the only crops grown on these farms) are done by the tenant farmer. The tenant farmer also supplies the farm equipment used in these activities. The tenant farmer repairs and maintains the equipment, and also maintains the irrigation system, fences, and other fixtures located on the property. After consulting with *A* and *B*, the tenant farmer purchases all herbicides, insecticides, and fertilizers used on the property. Also after consulting with *A* and *B*, the tenant farmer contracts to sell the crops at a future date, or sells them when harvested. Each tenant farmer is responsible for accounting to *A* and *B* for *P*'s share of the proceeds.

A and *B* each devote to substantial part of their time to the operation of their own respective farms which are unconnected with the farmland owned by *P*. After completing work on their own properties, *A* and *B*, in their capacity as officers of *P*, occasionally inspect the crops and improvements located on each leased tract. If any corrective steps must be taken, *A* or *B* points out the problem to the tenant farmer, who makes the necessary corrections in the way the tenant farmer sees fit. *A* and *B* also decide each year what portion of each tract will be leased, in the light of soil conservation needs, market conditions, and federal price support and acreage reserve programs. They review each tenant farmer's accounting of operations and sales.

For valid business reasons, *P* will transfer to a newly-formed subsidiary corporation, *S*, one-half of all the property held by *P*, and then will distribute all the *S* stock to *B* in exchange for all *B*'s stock in *P*. After the distribution, *P* and *S* will continue to conduct operations in the same manner with tenant farmers as *P* had prior to the distribution.

Except for the question here at issue regarding the active conduct of a trade or business, the transfer will meet all the requirements of sections 368(a)(1)(D) and 355 of the Code and the regulations thereunder.

LAW AND ANALYSIS

Section 355(a) of the Code provides that under certain circumstances a corporation may distribute stock or securities in a corporation it controls to its shareholders or security holders in a transaction that is nontaxable to such shareholders or security holders.

Section 355(b) of the Code requires that both the distributing and controlled corporations be engaged, immediately after the distribution, in the active conduct of a trade or business that has been actively conducted throughout the 5-year period ending on the date of distribution.

To meet the requirements of section 355(b) of the Code, each corporation must, as stated in *Rafferty v. Commissioner*, 452 F.2d 767, 772 (1st Cir. 1971), *cert. denied*, 408 U.S. 922 (1972), "engage in entrepreneurial endeavors of such a nature and to such an extent as to qualitatively distinguish its operations from mere investments. Moreover, there should be objective indicia of such corporate operations." Such objective indicia are found in active and substantial managerial and operational activities of the corporation. In addition, this business activity has to be the activity of the corporation itself (through its officers and employees) and not the activity of independent contractors. Rev. Ruls. 80–181, 1980–2 C.B. 121, 79–394, 1979–2 C.B. 141, and 73–234, 1973–1 C.B. 180.

In Rev. Rul. 73–234, it was held that a corporation engaged in farming with tenant farmers was engaged in the active conduct of a trade or business within the meaning of section 355(b) of the Code. However, in that revenue ruling, *Y* corporation, through its employees, *A* and *B*, was engaged in hiring seasonal workers, purchasing and supplying equipment, maintaining equipment, arranging financing, planning all rotation and planting and harvesting of crops, purchasing livestock, planning livestock breeding, selling all crops and livestock, and accounting to the tenant farmers for their shares of the proceeds. This activity of *Y*, carried on through its own employees and constituting active and substantial managerial and operational activity, contrasts with the activity carried on by the employees of *P* in the present situation. Here, *P* either did not engage in the above activities at all, or engaged in them only on a limited basis. At best, *P* could be considered to engage in some managerial and operational activity but not enough to "qualitatively distinguish its operations from mere investments." Thus, Rev. Rul. 73–234 is distinguishable from the present situation.

HOLDING

Because of the absence of active and substantial operational and managerial activities, the active business requirement of section 355(b) of the Code is not met and *P*'s distribution of the *S* stock is not governed by section 355. *B* will recognize gain on the receipt of the *S* stock in exchange for *P* stock, and *P* will be subject to the provisions of section 311. See Rev. Rul. 74–516, 1974–2 C.B. 121.

In addition, because there is no distribution of stock or securities to *B* under section 354, 355, or 356 of the Code, the transfer of property from *P* to *S* does not meet the requirements of section 368(a)(1)(D). However, this transfer does meet the requirements of section 351(a). The fact that *P* distributed the *S* stock to *B* does not violate the control requirement of Section 351(c).

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 73–234 is distinguished.

Section 1016.—Adjustments to Basis

26 CFR 1.1016–3: Exhaustion, wear and tear, obsolescence, amortization, and depletion for periods since February 28, 1913.

Reduction of basis under optional standard mileage rate method for computing deductible expenses for business use of an automobile. See Rev. Proc. 86–38, page 10.

Section 4701.—Tax on Issuer of Registration-required Obligation not in Registered Form

26 CFR 46.4701–1: Tax on issuer of registration-required obligation not in registered form.
(Also Section 6011; 46.6011(a)–1.)

T.D. 8102

TITLE 26.—INTERNAL REVENUE— CHAPTER I, SUBCHAPTER D, SUBCHAPTER H, PART 46— REGULATIONS RELATING TO MISCELLANEOUS EXCISE TAXES

PAYABLE BY RETURN; PART 602—REPORTING AND RECORDKEEPING REQUIREMENTS

Tax on Issuer of Registration Required Obligation Not in Registered Form

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the excise tax imposed on the issuer of registration-required obligations which are not issued in registered form. This action is necessary because of changes to the applicable law made by the Tax Equity and Fiscal Responsibility Act of 1982. The regulations affect issuers of obligations and provide them with the guidance needed to comply with the law.

DATES: The regulations are generally effective for registration-required obligations not in registered form that are issued after December 31, 1982.

FOR FURTHER INFORMATION CONTACT: Timothy J. McKenna of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-4336, not a toll-free call).

SUPPLEMENTARY INFORMATION: BACKGROUND

On August 22, 1984, the FEDERAL REGISTER published proposed amendments to the Excise Tax Regulations (26 CFR Part 46) under section 4701 of the Internal Revenue Code of 1954 (49 FR 33285) [LR-9-83, 1984–2 C.B. 865]. These amendments were proposed to conform the regulations to section 310(b)(4) of the Tax Equity and Fiscal Responsibility Act of 1982 (the Act) (P.L. 97–248, 96 Stat. 597) [1982–2 C.B. 462]. No comments were received. A public hearing was not requested. Accordingly, the proposed amendments are adopted as revised by this Treasury decision.

IN GENERAL

Section 4701(a) provides that a tax is imposed on any person who issues a registration-required obligation which is not in registered form. The amount of the tax is one percent of the principal amount multiplied by the number of years (including portions thereof) from the date of issuance to the date of maturity. The terms "registration-required obligation" and "registered form" are defined in section 4701(b) as having the same meaning as when used in section 163(f) relating to the denial of a deduction for interest on certain obligations not in registered form. However, a registration-required obligation does not include any obligation required to be registered under section 103(j). Thus, the tax does not apply to those obligations which would otherwise be exempt from Federal income tax under section 103(a) or any other provision of law. While section 4701 applies generally to obligations issued after December 31, 1982, section 310(d)(3) of the Act also provides that section 4701 does not apply to any obligation issued after December 31, 1982, pursuant to the exercise of a warrant or the conversion of a convertible obligation, if the warrant or convertible obligation was issued before August 10, 1982, and offered or sold outside the United States without registration under the Securities Act of 1933.

In addition, §46.6011(a)–1(a) relating to the general requirement of making a return, statement or list by a person made liable for any tax imposed by this title, is amended to provide for the filing of Form 720 (Quarterly Federal Excise Tax Return) by those persons liable for the tax under section 4701.

CHANGE IN THE REGULATION

A minor clarification is made in these final regulations under §46.4701–1(b)(5), relating to the definition of "issuer". The regulations make a cross-reference to §1.163–5T(d), which generally treats the recipient of the proceeds from the issuance of a pass-through certificate as the issuer of such pass-through certificate. Temporary regulation §1.163–5T(d) was published in the Federal Register on August 20, 1985 (50 FR 33522) [T.D. 8046, 1985–2 C.B. 61], along with a cross-referenced notice of proposed rulemaking (50 FR 33552) with respect to which public comments were solicited. When the proposed regulations are published as final regulations, the cross-reference in §46.4701–1(b)(5) will be revised to refer to those final regulations.

In addition, a new paragraph (b)(7) was added to cross-reference to the definition of "issue price" in section 1273(b).

REGULATORY FLEXIBILITY ACT

Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

PAPERWORK REDUCTION ACT

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB under control number 1545–0023.

DRAFTING INFORMATION

The principal authors of these final regulations are Ada S. Rousso and Timothy J. McKenna of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations.

Accordingly, 26 CFR Parts 46 and 602 are amended as follows:

Part 46—[AMENDED]

Paragraph 1. The authority for Part 46 continues to read in part:

Authority: 26 U.S.C. 7805. * * * Sections 46.6011(a)–1 and 46.6011(a)–2 also issued under 26 U.S.C. 6011. * * *

Par. 2. Section 46.0–1 is amended as follows:

a. Paragraphs (a)(3) and (a)(4) are redesignated as paragraphs (a)(4) and (a)(5), respectively, and a new paragraph (a)(3) is inserted immediately after paragraph (a)(2) to read as set forth below.

b. Paragraph (b) is amended by removing the phrase "Subpart C of this part is reserved," and adding in its place "Subpart C of this part relates to the excise tax imposed by section 4701 on issuers of registration-required obligations not issued in registered form."

§46.0–1 Introduction.

(a) * * *

(3) the tax on the issuer of registration-required obligations not issued in registered form imposed by chapter 39 of the Internal Revenue Code of 1954, and * * *

* * * * *

Par. 3. A new Subpart C consisting of §46.4701–1 is added immediately after §48.4504–1 to read as set forth below.

Subpart C—Excise Tax on Obligations Not in Registered Form.

§46.4701–1 Tax on issuer of registration-required obligation not in registered form.

(a) *In general.* Section 4701 imposes a tax (determined under paragraph (c) of this section) on any person (referred to as the issuer) who issues an obligation that—

(1) Is a registration-required obligation, and

(2) Is not issued in registered form.

(b) *Definitions*—(1) *Person.* The term "person" includes all governmental entities.

(2) *Obligation.* The term "obligation" includes bonds, debentures, notes, certificates and other evidences of indebtedness regardless of how denominated.

(3) *Registration-required obligation.* The term "registration-required obligation" has the same meaning as when used in section 163(f) (and the regulations thereunder) which relates to the denial of a deduction for interest on certain obligations not in registered form. However, the term "registration-required obligation" does not include any obligation which would otherwise be exempt from Federal income tax under section 103(a) or any other provision of law.

(4) *Registered form.* The term "registered form" has the same meaning as when used in section 103(j) (and the regulations thereunder) which relates to obligations which must be in registered form to be tax-exempt.

(5) *Issuer.* Except as provided in §1.163–5T(d) (relating to pass-through certificates), the "issuer" is the person whose interest deduction would be disallowed solely by reason of section 163(f)(1).

(6) *Date of Issuance.* (i) for obligations intended to be offered to the public, the term "date of issuance" means the date the obligation is first sold to the public at the issue price.

(ii) For an obligation which is privately placed, the term "date of issuance" is the date the obligation is first sold by the issuer.

(7) *Issue price.* See section 1273(b) and the regulations thereunder for the definition of "issue price".

(c) *Rate and computation of tax.* The tax under section 4701(a) is imposed in an amount equal to the product of—

(1) 1 percent of the principal amount of the obligation, multiplied by

(2) The number of calendar years (or portions thereof) during the period beginning on the date of issuance of the obligation and ending on the date of maturity.

For purposes of this paragraph, the term "principal amount" for a discounted obligation is the issue price, and for all other obligations, including obligations sold at a premium, the term "principal amount" is the stated redemption price at maturity.

(d) *Payment of tax.* Every person who incurs liability for the tax imposed by section 4701 is required to file a return in accordance with section 6011 and §46.6011(a)–1 relating to the general requirement of a return, statement or list.

(e) *Effective date.* The provisions of this section shall apply to obligations issued after December 31, 1982, unless issued on the exercise of a warrant or the conversion of a convertible obligation if the warrant or obligation was offered or sold outside the United States without registration under the Securities Act of 1933 and was issued before August 10, 1982. See section 310(d)(3) of the Tax Equity and Fiscal Responsibility Act of 1982.

§46.6011 [Amended]

Par. 4. Section 46.6011(a)–1(a) is amended by removing the phrase "4371 or 4501(a)" from paragraph (a) wherever it appears and replacing it with the phrase "4371, 4501(a) or 4701".

Par. 5. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 6. Section 602.101(c) is amended by inserting in the appropriate place in the table:

"§46.4701–1(d) . . . 1545–0023".

Roscoe L. Egger, Jr.,
Commissioner of Internal Revenue.

Approved August 29, 1986.

J. Roger Mentz,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on September 19, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 22, 1986, 51 F.R. 33593)

Section 6011.—General Requirement of Return, Statement, or List

26 CFR 46.6011(a)–1: Returns.

The requirement that a return be filed by the issuer of registration-required obligations which are not issued in registered form. See T.D. 8102, page 6.

Part III. Administrative, Procedural, and Miscellaneous

Merchant Marine Act—Applicable Rate of Interest on Nonqualified Withdrawals from a Capital Construction Fund

Notice 86-11

AGENCY: Departments of Transportation; Commerce; Treasury; Maritime Administration; National Oceanic and Atmospheric Administration; Internal Revenue Service.

SUMMARY: The Secretaries of Transportation, Commerce and the Treasury, as required by the Merchant Marine Act, 1936, as amended, have determined and are jointly publishing the interest rate that shall apply during taxable year 1986 to "nonqualified withdrawals" made from a Capital Construction Fund.

DATES: The rate of interest that has been determined will apply to all nonqualified withdrawals from a Capital Construction Fund made between January 1, 1986 and December 31, 1986.

FOR FURTHER INFORMATION CONTACT: Russell Bigelow, Division of Capital Assets and Management, Maritime Administration, 400 Seventh Street SW., Washington, DC 20590, Tel. (202) 366-1908.

SUPPLEMENTARY INFORMATION: The Capital Construction Fund (CCF) Program, is authorized by section 607 of the Merchant Marine Act (Act). The act provides for the deferment of Federal income taxes on deposits of income in a CCF. The deposited funds are for the purpose of providing capital for the construction or reconstruction of vessels. The Maritime Administration (MARAD) administers the CCF program, under authority delegated by the Secretary of Transportation, for all vessels other than fishing vessels. The National Oceanic and Atmospheric Administration (NOAA) administers the CCF program for fishing vessels on behalf of the Secretary of Commerce. The Act requires the Secretaries of Transportation, Commerce and the Treasury, annually, to determine jointly and publish in the Federal Register the rate of interest that is applicable to all "nonqualified withdrawals" from a CCF (46 U.S.C. 1177(h)(4)(B), together with the tax. A nonqualified withdrawal is a withdrawal of funds not authorized by section 607. This annual determination is made in accordance with the procedure described at 46 CFR 394.7(e)(2)(ii) of the joint regulations that have been issued by MARAD, NOAA and the Internal Revenue Service. The applicable rate of interest for "nonqualified withdrawals", made in the taxable year 1986, shall be 11.09 percent, determined to the nearest one-hundredth of one percent. The determination was computed by multiplying eight percent by the ratio that the average yield on 5-year Treasury securities for the calendar year, immediately preceding the beginning of such taxable year, bears to the average yield on 5-year Treasury securities for the year 1970.

Dated: September 10, 1986.

John Gaughan,
Maritime Administrator.
Anthony J. Galio,
Administrator, National Oceanic and Atmospheric Administration.
J. Roger Mentz,
Assistant Secretary for Tax Policy.
James E. Saari,
Secretary, Maritime Administration, Maritime Subsidy Board.

(Filed by the Office of the Federal Register on September 17, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 18, 1986, 51 F.R. 33173)

Qualified Conservation Contributions—Technical Amendments

Notice 86-12

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final rule; technical amendments.

SUMMARY: This document contains technical amendments to Estate Tax Regulations §20.2055-2, which relates to transfers not exclusively for charitable purposes.

EFFECTIVE DATE: These amendments are effective December 18, 1980.

FOR FURTHER INFORMATION CONTACT: Ada S. Rousso of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. Telephone 202-566-3287 (not a toll-free number).

SUPPLEMENTARY INFORMATION: BACKGROUND

On January 14, 1986, the FEDERAL REGISTER published final regulations relating to Qualified Conservation Contributions, as adopted by T.D. 8069 (51 FR 1496). The provisions set forth in those regulations reflected changes made by the Tax Reform Act of 1984 and the Temporary Tax Provisions, Extentions.

Revisions for Title 26 of the Code of Federal Regulations were published for April 1, 1986, with the inclusion of T.D. 8069. T.D. 8069 amended regulations §20.2055-2 but inadvertently failed to revise cross references contained in paragraphs (e)(2), (f)(1) and (f)(2) of §20.2055-2.

NEED FOR AMENDMENTS

As published, Title 26 of the Code of Federal Regulations contains technical errors in §20.2055-2(e)(2), (f)(1) and (f)(2). Accordingly, technical amendments are being published to correct these errors.

LIST OF SUBJECTS
26 CFR Part 20
Estate Taxes.

Part 20 of Title 26 of the Code of Federal Regulations is amended as follows:

Paragraph 1: The authority for Part 20 continues to read as follows:

Authority: 26 U.S.C. 7805. * * *

Par. 2. Section 20.2055-2 is amended as follows:

1. Paragraph (e)(2)(vi)(*a*) is amended by revising the phrase "of this subdivision (v)" to read "of this subdivision (vi)".
2. Paragraph (e)(2)(vi)(*g*) is amended by revising the phrase "of this subdivision (v)" to read "of this subdivision (vi)".
3. Paragraph (e)(2)(vi)(*h*) is amended by revising the phrase "of this subdivision (v)" to read "of this subdivision (vi)".
4. Paragraph (e)(2)(vii)(*a*) is amended by revising the phrase "of this subdivision (vi)" to read "of this subdivision (vii)".
5. Paragraph (f)(1) is amended by revising the phrase "in paragraph (e)(2)(v)(*h*)" to read "in paragraph (e)(2)(vi)(*h*)".
6. Paragraph (f)(2) is amended by revising the phrase "in subdivision (iv), (v), or (vi)" to read "in subdivision (v), (vi), or (vii)".

7. Paragraph (f)(2)(iv) is amended by revising the phrase "paragraph (e)(2)(v)" to read "paragraph (e)(2)(vi)".

8. Paragraph (f)(2)(iv), Examples (1) thru (3), is amended by revising the phrase "(as defined in paragraph (e)(2)(v) of this section)" to read "(as defined in paragraph (e)(2)(vi) of this section)".

9. Paragraph (f)(2)(iv), Example (4), is amended by revising the phrase "paragraph (e)(2)(v)(*f*)" to read "paragraph (e)(2)(vi)(*f*)".

10. Paragraph (f)(2)(v) is amended by revising the phrase "described in paragraph (e)(2)(vi)" to read "described in paragraph (e)(2)(vii)".

DONALD E. OSTEEN,
Director, Legislation and Regulations Division.

(Filed by the Office of the Federal Register on September 8, 1986, 8:45 a.m., and published in the issue of the Federal Register for September 9, 1986, 51 F.R. 32071)

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26 CFR 601.105: Examination of returns and claims for refund, credit or abatement; determination of correct liability.
(Also Part I, Sections 162, 167, 274, 1016; 1.162–17, 1.167(a)–1, 1.274–5, 1.1016–3.)

Rev. Proc. 86–38

SECTION 1. PURPOSE

The purpose of this revenue procedure is to update Rev. Proc. 82–61, 1982–2 C.B. 849, as modified by Rev. Proc. 83–74, 1983–2 C.B. 593, Rev. Proc. 84–72, 1984–2 C.B. 735, and Rev. Proc. 85–49, 1985–2 C.B. 716, by stating that there have been no changes in the optional standard mileage rates for the business use of an automobile for 1986. This revenue procedure also states that depreciation is considered to be allowed at 9 cents per mile for 1986 if the optional method for computing the costs of business use of an automobile is used.

SEC. 2. PROCEDURE

.01. Paragraph (2)(b) of subsection .01 of section 3 of Rev. Proc. 82–61, which was modified by Rev. Proc. 83–74, Rev. Proc. 84–72 and Rev. Proc. 85–49, is further modified to read as follows:

In the case of automobiles placed in service for business purposes after December 31, 1979, and in which the optional method was used in 1980, 1981, 1982, 1983, 1984, 1985, or 1986, depreciation will be considered to have been allowed at the rate of 7 cents a mile for 1980 and 1981, 7.5 cents a mile for 1982, and 8 cents a mile for 1983, 1984, and 1985, and 9 cents a mile for 1986, except that if the "actual cost" method was used for one or more of those years the rates above will not apply to any year in which that method was used. This depreciation will act to reduce the basis of the automobile in determining adjusted basis as required by section 1016 of the Code. An automobile placed in service after December 31, 1979, with respect to which the optional method is used is considered to have a useful life of 60,000 miles of business use at the maximum standard mileage rate determined without reference to the age of the vehicle. After 60,000 miles of business use at the maximum standard mileage rate, the automobile will be considered fully depreciated. For purposes of this paragraph, an automobile will be considered to have been driven no more than 15,000 miles in any one year, even though the actual business mileage of the automobile may be greater.

.02. Paragraph 2(f) of subsection .01 of section 3 of Rev. Proc. 82–61 is amended by substituting "applicable mileage rate for the taxable year" for "20-cent mileage rate" to reflect the changes that occur from time to time in the optional standard mileage rate for the business use of an automobile.

SEC. 3. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 82–61, as modified by Rev. Proc. 83–74, Rev. Proc. 84–72 and Rev. Proc. 85–49, is further modified.

Part IV. Items of General Interest

Notice Of Proposed Rulemaking

Windfall Profit Tax; Rules RelatingTo Production From A Unitized Property Of Imputed Stripper Well Crude Oil, Imputed Heavy Crude Oil, And Imputed Newly Discovered Cured Oil

LR–225–81

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to the production from a unitized property of imputed stripper well crude oil, imputed heavy crude oil, and imputed newly discovered crude oil for purposes of the windfall profit tax. Changes to the applicable law were made by the Crude Oil Windfall Profit Tax Act of 1980 [Pub. L. 96–223, 1980–3 C.B. 1]. The regulations would provide guidance for determining whether all or a portion of the production from a unitized property will be treated as crude oil from a stripper well property, heavy oil, or newly discovered oil.

DATES: Written comments and requests for a public hearing must be delivered or mailed by December 1, 1986. The amendments are proposed to be effective for crude oil removed after February 29, 1980. However, the special rule contained in paragraph (e)(1) of proposed §51.4996–5 would be effective for months beginning after November 30, 1986.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR–225–81), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Gail H. Morse of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3297).

SUPPLEMENTARY INFORMATION:

BACKGROUND

This document contains proposed amendments to the Excise Tax Regulations Under the Crude Oil Windfall Profit Tax Act of 1980 (26 CFR Part 51).

Under the windfall profit tax taxable crude oil is divided into three tiers. The windfall profit tax rate depends, in part, on the tier of the crude oil. In order to determine the tier of taxable crude oil it is often necessary to determine the "property" from which the crude oil is produced. For example, the determinations of whether crude oil qualifies as crude oil from a stripper well property, newly discovered oil, or heavy oil (all these types of oil receive preferred treatment under the windfall profit tax) are made on a property-by-property basis.

"Property" is defined for windfall profit tax purposes in §150.4996–1(i) of the Temporary Excise Tax Regulations Under the Crude Oil Windfall Profit Tax Act of 1980 (26 CFR Part 150) as promulgated by Treasury decision 7846, published on November 10, 1982 (47 FR 50858) [1982–2 C.B. 353]. The text of that Treasury decision also served as the text of a notice of proposed rulemaking published on the same day (47 FR 50924) [LR–34–82, 1982–2 C.B. 930]. Section 150.4996–1(i) provides that "property" generally is determined by reference to the geographical boundaries of the right to produce crude oil as such right existed on January 1, 1972, provided such right was in production in commercial quantities on that date. If such right was not in production in commercial quantities on January 1, 1972, the determination of "property" is generally made by reference to the geographical boundaries of the right to produce crude oil when crude oil is first produced thereafter in commercial quantities.

Although §150.4996–1(i) provides the general rule for determining "property," paragraph (i)(4) of that section, which relates to unitizations, was reserved for subsequent publication. On September 25, 1986, a new notice of proposed rulemaking was published in the FEDERAL REGISTER (51 FR 34095) which generally provides that a unitization is treated as a single property. A new §51.4996–5 is added by this document which would provide rules for imputing stripper well oil, heavy oil, and newly discovered oil to a unitized property.

EXPLANATION OF PROVISIONS

Imputed oil

Because a unitization is generally treated as a single "property" for windfall profit tax purposes, the rules for determining whether crude oil produced from the unitized property qualifies as crude oil from a stripper well property, newly discovered oil, heavy oil, or incremental tertiary oil generally must be applied to the unitized property. For example, in order for all potential crude oil production from a unitized property to qualify as newly discovered oil, crude oil could not have been produced in commercial quantities during 1978 from the unitized property or from any portion of a property now included in the unitized property if the unitization occurred during or after 1978. Applying these rules to a unitized property can create a tax disincentive to unitizing properties. For example, the operator of a newly discovered crude oil property would not voluntarily unitize its property with properties that produced crude oil in commercial quantities during 1978 if the operator would not retain a benefit equal to the preferred tax treatment it has for crude oil produced from the newly discovered crude oil property without its inclusion within the unitized property.

The proposed rules provide that all or a portion of the crude oil produced from a unitized property within which is included a property that qualified as a stripper well property, newly discovered crude oil property, or heavy crude oil property before the unitization will be treated as crude oil from a stripper well property, newly discovered oil, or heavy oil, respectively. The portion of crude oil treated as crude oil from a stripper well property, newly discovered oil, or heavy oil is referred to as imputed stripper well crude oil, imputed newly discovered crude oil, or imputed heavy crude oil, respectively. The proposed rules generally determine the amount of imputed oil on the basis of the historical production levels for the properties composing the unitized property. However, several limitations apply. First, the proposed rules provide that for any particular month beginning after December 1, 1986, imputed oil is limited to the amount of crude oil allocated during that month by the unitization agreement to the properties (before inclusion within the unitization) or interests therein that give rise to the imputed oil. Second, the district director may adjust the amount allocated to certain newly discovered crude oil properties if the district director determines that the method of allocation used by the producers has as a principal purpose the avoidance of windfall profit tax. Finally, the district director may adjust the amount of any imputed oil if the district director determines that any of the properties composing the unit did not produce at its maximum feasible rate of production during the 12-month period immediately preceding the unitization.

Imputed stripper well crude oil

The proposed rules provide that, in determining imputed stripper well crude oil, condensate produced from a well other than an oil-producing well is not counted as crude oil produced during the 12-month period immediately preceding the establishment of the unit base production control level or the occurrence of the unitization.

Imputed newly discovered crude oil

Determining imputed oil on the basis of historical production levels may yield an undesirable result if a right to produce crude oil had no production before inclusion within the unit. Therefore, a special rule is provided in the case of a unitized property that contains a right to produce crude oil that was unitized before it produced crude oil in commercial quantities (referred to as a "newly discovered separate right to produce"). In this case, imputed newly discovered crude oil is determined by comparing the surface acreage within the unitized property of the newly discovered separate rights to produce the total surface acreage of the unitized property. For this purpose, surface acreage that is not underlain by proved developed or undeveloped oil and gas reserves affected by the unitization shall be disregarded. For this purpose, the terms "proved developed oil and gas reserves" and "proved undeveloped oil and gas reserves" are defined in proposed §51.4996–5(g)(3) and (4), respectively, and have the same meaning as the terms have in regulations promulgated by the Securities and Exchange Commission. See 17 CFR §201.4–10(a)(3) and (4). It is anticipated that these definitions generally will be applied for windfall profit tax purposes in a manner similar to the manner in which they are applied for financial reporting purposes.

If data is ascertained after the surface acreage is determined and such data would result in a more accurate determination of the surface acreage at the time of the unitization, the surface acreage must be redetermined using such data. For purposes of determining imputed newly discovered crude oil, the proposed rules provide that the term "newly discovered crude oil property" has the same meaning as that term has in proposed §51.4996–1(m)(2). Proposed §51.4996–1(m)(2) is contained in a notice of proposed rulemaking published in the Federal Register on November 5, 1982 (47 FR 50306).

Proposed §51.4996–5(e)(3) and (4) contains three special rules relating to imputed newly discovered crude oil. Under the rules for determining imputed stripper well crude oil, all production from a unitized property is treated as crude oil from a stripper well property if a stripper well property is unitized with a property that did not produce crude oil during the 12-month period immediately before the unitization. However, the rules for determining imputed newly discovered crude oil provide that if a right to produce crude oil that has never produced crude oil in commercial quantities is unitized with other properties, imputed newly discovered crude oil resulting from such right to produce is determined by comparing the surface acreage of such right to produce to the total surface acreage of the unitized property. The first special rule makes clear that imputed oil includes imputed newly discovered crude oil determined under the surface acreage method even though all production from the unitized property would be treated as crude oil from a stripper well property under the imputed stripper well crude oil provisions.

Although the first special rule provides that a certain portion of the production from the unitized property will be treated as imputed newly discovered crude oil even though all production would be treated as crude oil from a stripper well property under the imputed stripper well crude oil provisions, the second special rule permits producers who held an economic interest in the newly discovered separate rights to produce before the unitization to treat a certain portion of the production from the unitized property allocated to it as imputed stripper well crude oil. Finally, if a newly discovered crude oil property met the requirements of a stripper well property before the unitization, a producer may treat a certain portion of newly discovered crude oil allocated to that property after the unitization as crude oil produced from a property that qualifies as a stripper well property. Thus, an independent producer who treated its share of production from the property before the unitization as exempt stripper well oil generally may continue to treat its share of imputed newly discovered crude oil allocated to that property after the unitization as exempt stripper well oil.

Incremental tertiary recovery project.

Proposed §51.4996–5(f) provides that, solely for purposes of determining incremental tertiary oil and the effects of that determination on imputed oil, if a qualified tertiary recovery project (as defined in proposed paragraph (c) of §51.4993–1) is located on a unitized property and the unitized property is treated as more than one property under section 4993(d)(3) and proposed paragraph (e)(4) of §51.4993–1 (relating to a tertiary project which only affects a portion of a property), imputed oil will be determined by treating each property (as determined under sections 4993(d)(3) and proposed paragraph (e)(4) of §51.4993–1) as a separate unitized property. Proposed paragraphs (c) and (e)(4) of §51.4993–1 are contained in a notice of proposed rulemaking published in the Federal Register on September 10, 1984 (49 FR 35517) [LR–67–80, 1984–2 C.B. 835].

COMMENTS AND REQUEST FOR PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is to be held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies of those comments to the Service.

SPECIAL ANALYSIS

The Commissioner of the Internal Revenue has determined that these final rules are not major rules as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required.

Although this document is a notice of proposed rulemaking which solicits public comments, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. Chapter 6).

DRAFTING INFORMATION

The principal author of these proposed regulations was Douglas W. Charnas of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these regulations, both on matters of substance and style.

* * * * *

Proposed amendments to the regulations.

The proposed amendments to 26 CFR Part 51 are as follows:

Paragraph 1. The authority for Part 51 continues to read in part:

Authority: 26 U.S.C. 4997 and 7805. * * *

Par. 2. Paragraph (c)(1) of §51.4989–1 is amended by removing "150.4996–1(i)" and inserting in lieu thereof "51.4996–4."

Par. 3. Paragraph (m)(3) of §51.4996–1 (as proposed on November 5, 1982, in 47 FR 50307) is revised to read as follows:

§51.4996–1 Definitions.

* * * * *

(m) *Newly discovered oil.* * * *

(3) *Imputed newly discovered oil.* For rules relating to imputed newly discovered oil see paragraph (d) of §51.4996–5.

Par. 4. A new §51.4995–5 is added immediately after §51.4996–4, to read as follows:

§51.4996–5 Special rules for production from unitized properties.

(a) *Imputed oil.* For purposes of chapter 45 of the Code, any imputed stripper well crude oil, imputed heavy crude oil, or imputed newly discovered crude oil shall be treated as crude oil from a stripper well property, heavy oil, or newly discovered oil, respectively. However, see the special rules contained in paragraph (e) of this section.

(b) *Imputed stripper well crude oil*—(1) *Unitizations with BPCL established before August 1, 1977.* In the case of a unitized property for which a unit base production control level was established before August 1, 1977, the term "imputed stripper well crude oil" means, in a particular month, the number of barrels of crude oil equal to the total number of barrels of crude oil produced and sold during the 12-month period immediately preceding the establishment of a unit base production control level for the unitized property from all properties that constitute the unitized property that qualified as stripper well properties before inclusion within the unitized property multiplied by a fraction the numerator of which is the number of days in that particular month and the denominator of which is the number of days in that 12-month period. The number of barrels of imputed stripper well crude oil determined under this subparagraph shall not exceed the number of barrels of crude oil removed from the premises of the unitized property during that particular month.

(2) *Unitizations that occur after February 29, 1980, or with BPCL established after July 31, 1977.* In the case of a unitized property for which a unit base production control level was established after July 31, 1977, or for which the unitization occurs after February 29, 1980, provided a unit base production control level was not required, the term "imputed stripper well crude oil" means, in a particular month, the greater of:

(i) The number of barrels of crude oil equal to the total number of barrels of crude oil removed from the premises of the unitized property during that particular month multiplied by a fraction the numerator of which is the total number of barrels of crude oil produced and sold during the 12-month period immediately preceding the establishment of a unit base production control level or the occurrence of the unitization for the unitized property from all properties that constitute the unitized property that qualified as stripper well properties before inclusion within the unitized property and the denominator of which is the total number of barrels of crude oil produced and sold during that 12-month period from all properties that constitute the unitized property (including those that qualified as stripper well properties), or

(ii) The number of barrels of crude oil equal to the total number of barrels of crude oil produced and sold during the 12-month period immediately preceding the establishment of a unit base production control level or the occurrence of the unitization for the unitized property from all properties that constitute the unitized property that qualified as stripper well properties before inclusion within the unitized property multiplied by a fraction the numerator of which is the number of days in that particular month and the denominator of which is the number of days in that 12-month period. The number of barrels of crude oil determined under this subdivision shall not exceed the number of barrels of crude oil removed from the premises of the unitized property during that particular month. For purposes of this paragraph, condensate produced from a well other than an oil-producing well is not counted as crude oil produced during the 12-month period immediately preceding the establishment of a unit base production control level or the occurrence of the unitization.

(c) *Imputed heavy crude oil.* The term "imputed heavy crude oil" means, in a particular month, a portion of crude oil production of a unitized property for which a unit base production control level was established after August 16, 1979, or for which the unitization occurs after February 29, 1980, provided a unit base production control level was not required. That portion is the greater of:

(1) The number of barrels of crude oil equal to the total number of barrels of crude oil removed from the premises of the unitized property during that particular month multiplied by a fraction the numerator of which is the total number of barrels of crude oil produced and sold during the 12-month period immediately preceding the establishment of a unit base production control level or the occurrence of the unitization for the unitized property from all properties that constitute the unitized property that qualify as heavy crude oil properties (within the meaning of paragraph (g)(2) of this section) before inclusion within the unitized property and the denominator of which is the total number of barrels of crude oil produced and sold during that 12-

month period from all properties that constitute the unitized property (including those that qualified as heavy crude oil properties), or

(2) The number of barrels of crude oil equal to the total number of barrels of crude oil produced and sold during the 12-month period immediately preceding the establishment of a unit base production control level or the occurrence of the unitization for the unitized property from all properties that constitute the unitized property that qualified as heavy crude oil properties before inclusion within the unitized property multiplied by a fraction the numerator of which is the number of days in that particular month and the denominator of which is the number of days in that 12-month period. The number of barrels of crude oil determined under this subparagraph shall not exceed the number of barrels of crude oil removed from the premises of the unitized property during that particular month.

For purposes of this paragraph, the 12-month period prior to the inclusion of heavy crude oil property within a unitized property may be reduced to the number of days in the months in that period in which heavy crude oil was produced and sold.

(d) *Imputed newly discovered crude oil*—(1) *In general.* The term "imputed newly discovered crude oil" means, in a particular month, a portion of the crude oil production of a unitized property for which a unit base production control level was established after January 1, 1979, or for which the unitization occurs after February 29, 1980, provided a unit base production control level was not required. That portion is the sum of:

(i) The greater of:

(A) The number of barrels of crude oil equal to the total number of barrels of crude oil removed from the premises of the unitized property during that particular month multiplied by a fraction the numerator of which is the total number of barrels of crude oil produced and sold during the 12-month period immediately preceding the establishment of a unit base production control level or the occurrence of the unitization for the unitized property from all properties that constitute the unitized property that qualified as newly discovered crude oil properties (within the meaning of paragraph (m)(2) of §51.4996–1) before inclusion within the unitized property and the denominator of which is the total number of barrels of crude oil produced and sold during that 12-month period from all properties that constitute the unitized property (including those that qualified as newly discovered crude oil properties), or

(B) The number of barrels of crude oil equal to the total number of barrels of crude oil produced and sold during that 12-month period from all properties that constitute the unitized property that qualified as newly discovered crude oil properties before inclusion within the unitized property multiplied by a fraction the numerator of which is the number of days in that particular month and the denominator of which is the number of days in that 12-month period, plus

(ii) The number of barrels of crude oil equal to the total number of barrels of crude oil removed from the premises of the unitized property during that particular month multiplied by a fraction the numerator of which is the surface acreage within the unitized property of the separate rights to produce crude oil that were first included within the unitized property after 1978 and before they produced crude oil in commercial quantities (hereinafter referred to as "newly discovered separate rights to produce") and the denominator of which is the total surface acreage of the unitized property.

The number of barrels of crude oil determined under paragraph (d)(1)(i)(B) of this section shall not exceed the number of barrels of crude oil removed from the premises of the unitized property during that particular month. For purposes of making a determination under paragraph (d)(1)(ii) of this section, surface acreage that is not underlain by proved developed or undeveloped oil and gas reserves (within the meaning of paragraph (g)(3) and (4) of this section, respectively) affected by the unitization shall be disregarded. Also for purposes of this paragraph, the 12-month period immediately preceding the inclusion of newly discovered crude oil properties within a unitized property may be reduced to the number of days in the months in that period during which newly discovered crude oil was produced and sold. If, at any time, the operators of the unitized property ascertain data that would result in a more accurate determination of the surface acreage of the unitized property underlain by the reservoir at the time of the unitization than the determination that was previously made for such surface acreage, the operators must promptly redetermine the surface acreage underlain by the reservoir at the time of the unitization using the newly ascertained data and must notify the first purchasers and producers of any change since the unitization in the number of barrels of imputed oil resulting from the redetermination of the surface acreage.

(2) *Statement by petroleum engineer.* If any crude oil produced from a unitized property is determined to be imputed newly discovered crude oil under paragraph (d)(1)(ii) of this section, each operator of crude oil production from that unitized property shall keep in its records a statement, signed under penalties of perjury by a petroleum engineer (who has been duly registered or certified in accordance with applicable state law, if any) setting forth the following information:

(i) The operator's name and identifying number (employer identification number or, if none, social security number),

(ii) A description of the unitized property including the location, identifying number (if any), and the names and identifying numbers or, if none, other information sufficient to identify the constituent properties (within the meaning of paragraph (e)(6)(i)(B) of this section) composing the unitized property,

(iii) The name and identifying number (employer identification number or, if none, social security number) of each producer holding an operating mineral interest (within the meaning of section 614(d)) in the unitized property,

(iv) The surface acreage of that portion of each newly discovered separate right to produce that is underlain by a reservoir of the unitized property affected by the unitization, and

(v) A statement that the portion of the reservoir underlying the surface acreage of each newly discovered separate right to produce contains proved undeveloped oil and gas reserves.

The statement shall be made at the time the newly discovered separate right to produce is included in the unitized property, or, if later, by the date that is 90 days after the date of publication of this paragraph in the Federal Register in a Treasury decision, shall be kept at all times available for inspection by authorized internal revenue officers or employees, and shall be retained so long as the contents thereof may become material in the administration of any internal revenue law.

(e) *Special rules*—(1) *Limitation on imputed oil*—(i) *In general.* In a particular month beginning after November 30, 1986, the amount of imputed stripper well crude oil determined under paragraph (b) of this section, imputed heavy crude oil determined under paragraph (c) of this section, or imputed newly discovered crude oil determined under paragraph (d) of this section shall not exceed the number of barrels of crude oil removed from the premises of the unitized property during that month allocated by the unitization agreement to the constituent properties (within the meaning of paragraph (e)(6)(i)(B) of this section) or interests therein that qualified as stripper well properties, heavy crude oil properties, or newly discovered crude oil properties (including newly discovered separate rights to produce), respectively, before inclusion within the unitized property. However, if the unitized property includes only newly discovered separate rights to produce or properties that qualified as stripper well properties, heavy crude oil properties, or newly discovered crude oil properties before inclusion within the unitized property, the excess of any imputed oil determined under this section without regard to this subparagraph for a particular month over the amount determined with regard to this subparagraph shall be allocated among and treated as imputed stripper well crude oil, imputed heavy crude oil, and imputed newly discovered crude oil on the basis of each such imputed oil's proportionate share of production determined under this section without regard to this subparagraph for the particular month.

(ii) *District director's authority in the case of newly discovered separate rights to produce.* If the district director determines, based on all the facts and circumstances, that—

(A) The amount of crude oil allocated for a particular month by the unitization agreement to a constituent property that qualifies as a newly discovered separate right to produce exceeds the amount which would be allocated to such constituent property if the allocation were determined by multiplying total production from the unitized property for that month by a fraction the numerator of which is the proved undeveloped oil and gas reserves contained in the portion of the reservoir affected by the unitization underlying such constituent property and the denominator of which is the sum of the proved developed oil and gas reserves (within the meaning of paragraph (g)(3) of this section) and proved undeveloped reserves contained in the entire reservoir affected by the unitization, and

(B) A principal purpose of such allocation is the avoidance of windfall profit tax,

the district director may adjust such allocation, solely for purposes of applying the rule in paragraph (e)(1)(i) of this section, to more closely reflect the amount which results by multiplying total production from the unitized property for that month by such fraction. If the district director makes such an adjustment, the rule in paragraph (e)(1)(i) of this section shall be applied by using the amount allocated by the unitization agreement as adjusted by the district director.

(2) *Limitation of imputed oil based on district director's authority.* If the district director determines, based on all the facts and circumstances, that production on any constituent property was not maximum total potential production for the full 12-month period immediately preceding the establishment of a unit base production control level or the occurrence of the unitization (whichever is applicable in determining imputed oil), the district director may adjust the amounts of imputed oil from the unitized property to more closely reflect the maximum total potential production for the constituent properties during that 12-month period. In order for production from a constituent property to qualify as maximum total potential production, each oil-producing well (within the meaning of paragraph (b)(2) of this section) on the property must have been maintained for the full 12-month period at its maximum feasible rate of production in accordance with recognized conservation practices, and not have been significantly curtailed by reason of mechanical failure or other disruption in production, or insertion of devices that restrict the flow of production from any well.

(3) *Unitization including rights to produce from which no crude oil was produced before the unitization.* (i) The amount of each type of imputed oil for a particular month shall be determined under this section by first determining the amount of imputed newly discovered crude oil under paragraph (d)(1)(ii) of this section (subject to the limitation contained in paragraph (e)(1)(i) of this section). After the amount of imputed newly discovered crude oil is so determined, imputed oil is determined for the remaining crude oil production of the unitized property for the particular month by applying the rules of this section other than the rule contained in paragraph (d)(1)(ii) of this section. For example, if stripper well properties are unitized with a newly discovered separate right to produce and half of the production from the unitized property is determined to be imputed newly discovered crude oil under paragraph (d)(1)(ii) of this section (after application of the rules contained in paragraph (e)(1)(i) of this section), half of the crude oil removed from the unitized property shall be treated as newly discovered crude oil even though all of the production from the unitized property would be treated as crude oil from a stripper well property under paragraph (b) of this section.

(ii) If stripper well properties are unitized with newly discovered separate rights to produce, a producer may treat as imputed stripper well crude oil a certain amount of the producer's share of the imputed newly discovered crude oil determined under paragraph (d)(1)(ii) of this section (subject to the limitation contained in paragraph (e)(1)(i) of this section) that is allocated to the newly discovered separate rights to produce in which the producer (or a person for whom the producer is a successor in interest) held an economic interest in the crude oil in place in the ground immediately before the unitization. That amount is equal to A in the following formula:

$$A = B \times \frac{C \times \frac{D}{E}}{F}$$

In which:

A = An amount during a particular month that a producer may treat as crude oil from a stripper well property.

B = The amount of the producer's share of imputed newly discovered crude oil determined under paragraph (d)(1)(ii) of this section (subject to the rules contained in paragraph (e)(1)(i) and (e)(6) of this section) that is allocated to the newly discovered separate rights to produce in which the producer (or a person for whom the producer is a successor in interest) held an economic interest in the crude oil in place in the ground immediately before the unitization. However, this amount shall not exceed the product of the amount of imputed stripper well crude oil determined under this section without regard to paragraph (e)(1)(i) of this section multiplied by the percentage equal to the producer's share of the production allocated by the unitization agreement to the newly discovered separate rights to produce in which the producer (or a person for whom the producer is a successor in interest) held an economic interest in the crude oil in place in the ground immediately before the unitization. See example (5) in paragraph (e)(7) of this section.

C = The amount of total production from the unitized property during that month which would be treated as imputed stripper well crude oil under this section without regard to paragraphs (d)(1)(ii) and (e)(1)(i) of this section.

D = The surface acreage (as limited by paragraph (d)(1) of this section) within the unitized property of the newly discovered separate rights to produce.

E = The total surface acreage (as limited by paragraph (d)(1) of this section) of the unitized property.

F = The amount of production during that month from the unitized property that is allocated to such newly discovered separate rights to produce.

(4) *Properties that meet the requirements of both newly discovered crude oil properties and stripper well properties.* (i) Except as otherwise provided in paragraph (e)(4)(ii) of this section, if a unitized property includes any newly discovered crude oil properties that met the requirements of a stripper well property before inclusion within the unitization, a producer may treat as imputed stripper well crude oil a certain amount of the producer's share of certain imputed newly discovered crude oil that is allocated to such newly discovered crude oil properties in which the producer (or a person for whom the producer is a successor in interest) held an economic interest in the crude oil in the ground immediately before the unitization. For purposes of the preceding sentence, certain imputed newly discovered crude oil includes only imputed newly discovered crude oil that is attributable to production from newly discovered crude oil properties that also met the requirements of a stripper well property before the unitization. Such amount shall be equal to A in the following formula:

$$A = G \times \frac{C \times \frac{H}{I}}{J}$$

In which:

A = An amount during a particular month that a producer may treat as crude oil from a stripper well property.

G = The amount of the producer's share of imputed newly discovered crude oil attributable to the newly discovered crude oil properties that also met the requirements of a stripper well property before the unitization that is allocated to such newly discovered crude oil properties in which the producer (or a person for whom the producer is a successor in interest) held an economic interest in the crude oil in place in the ground immediately before the unitization.

C = The amount of total production from the unitized property during that month which would be treated as imputed stripper well crude oil (subject to the rules contained in this paragraph other than the rule in paragraph (e)(3)(ii) of this section) if the newly discovered crude oil properties that also met the requirements of a stripper well property before the unitization were treated as stripper well properties for purposes of determining imputed oil under this section.

H = The amount of crude oil produced and sold during the 12-month period immediately preceding the unitization from such newly discovered crude oil properties.

I = The amount of crude oil produced and sold during that 12-month period from all properties that constitute the unitized property.

J = The amount of production during that month from the unitized property that is allocated to such newly discovered crude oil properties.

For purposes of this subparagraph, the 12-month period immediately preceding the unitization may be reduced to the number of days in the months in that period in which all such newly discovered crude oil properties each met the requirements of a stripper well property.

(ii) If a unitized property is composed solely of stripper well properties and newly discovered crude oil properties that also met the requirements of a stripper well property before the unitization, a producer may treat all of its share of production from the unitized property as imputed stripper well crude oil.

(5) *Inclusion of less than entire property in unitization.* If less than an entire property is included in a unitization, only crude oil production from wells located on the portion of the property included in the unitization shall be counted as production from that property during the 12-month period immediately preceding the unitization for the purpose of determining the amount of imputed oil.

(6) *Allocation of crude oil among constituent properties*—(i) *In general.* Except as otherwise provided in paragraph (e)(6)(ii) of this section, in the case of a unitized property that produces crude oil of different categories, a constituent property's share of crude oil in each category shall be determined by the unitization agreement. For purposes of this paragraph, any amendment to a unitization agreement shall be effective for the first taxable period beginning after the amendment is made or, if later, the effective date stated in the amendment. If the unitization agreement does not explicitly allocate crude oil in a particular category among the constituent properties, crude oil in that category produced during the particular month shall be allocated among the constituent properties on the basis of each constituent property's proportionate share of crude oil produced in that category during the 12-month period immediately preceding the establishment of the unit base production control

level or, in the absence thereof, occurrence of the unitization, but only to the extent of the amount of the production of the unitized property during that month that is allocated to such constituent property by the unitization agreement. If one or more of the constituent properties had no crude oil production during that 12-month period, the amount of imputed newly discovered crude oil determined under paragraph (d)(1)(ii) of this section (subject to the limitation contained in paragraph (e)(1) of this section) shall be allocated among the constituent properties on the basis of each constituent property's share of total production from the unitized property as established by the unitization agreement. However, no such imputed newly discovered crude oil shall be allocated to a constituent property for which an amount equal to such constituent property's share of production from the unitized property as established by the unitization agreement for the particular month has been allocated after applying the rule contained in the second preceding sentence. Any amount of crude oil in a category that has not been allocated to constituent properties for the particular month after applying the rules contained in the three preceding sentences shall be allocated among the constituent properties on the basis of each constituent property's proportionate share of production for that month from the unitized property as established by the unitization agreement for which crude oil in any category has not been allocated after applying the rules contained in the three preceding sentences. For purposes of this paragraph—

(A) The categories of crude oil are tier 1 oil, crude oil from a stripper well property, tier 2 oil other than crude oil from a stripper well property, newly discovered oil, heavy oil, incremental tertiary oil, and exempt oil.

(B) The term "constituent property" refers to a portion of a unitized property that was a separate right to produce crude oil or a portion thereof immediately before the unitization.

(ii) *District director's authority*. If the district director determines, based on all the facts and circumstances, that the allocation of any category of crude oil produced from the unitized property among the constituent properties does not reflect the manner in which the constituent properties share the production of the unitized property, the district director may adjust such allocation to reflect the manner in which the constituent properties share the production of the unitized property unless it is established by clear and convincing evidence that such allocation does not have as one of its principal purposes the avoidance of windfall profit tax. For example, such an adjustment would be appropriate in a situation in which a unitization agreement allocates to a constituent property production in excess of its proportionate share of production before the unitization and burdens such constituent property with a disproportionately large share of expenses. An allocation of crude oil in a particular category among the constituent properties on a basis other than each constituent property's proportionate share of crude oil produced in that category during the 12-month period immediately preceding the establishment of a unit based production control level or occurrence of the unitization (whichever is applicable in determining imputed oil) is evidence that the allocation has as one of its principal purposes the avoidance of windfall profit tax.

(7) *Examples*. The provisions of this paragraph may be illustrated by the following examples:

Example (1). On January 1, 1983, property K is unitized with property L. A single crude oil reservoir underlies K and L. At the time of the unitization, K qualified as a stripper well property, but all production from L was tier 1 oil. During the 12-month period immediately preceding the unitization, K and L each produced 50,000 barrels of crude oil. The unitization agreement provides that K will be allocated 40 percent of production and L will be allocated 60 percent of production from the unitized property. During February of 1983, the unitized property produced 10,000 barrels of crude oil. Although 5,000 barrels would be treated as imputed stripper well crude oil under paragraph (b) of this section, paragraph (e)(1)(i) of this section limits imputed stripper well crude oil to 4,000 barrels because that is the amount allocated to K, the constituent property that qualified as a stripper well property before the unitization. The remaining production, 6,000 barrels, is tier 1 oil.

Example (2). Assume the same facts as example (1) except that L qualified as a newly discovered crude oil property before the unitization. Imputed stripper well crude oil is limited to 4,000 barrels as in example (1). Imputed newly discovered crude oil is not limited by paragraph (e)(1)(i) of this section, and, therefore, equals 5,000 barrels. Because the unitized property only includes a property that qualified as a stripper well property and a property that qualified as a newly discovered crude oil property before the unitization, the excess of imputed stripper well crude oil determined without regard to paragraph (e)(1)(i) of this section (5,000 barrels) over such imputed oil determined with regard to paragraph (e)(1)(i) (4,000 barrels) is allocated between imputed stripper well crude oil and imputed newly discovered crude oil on the basis of the proportionate share of production of such imputed oils determined under this section without regard to paragraph (e)(1)(i). Thus, of the 1,000 barrel excess, 500 barrels are treated as imputed stripper well crude oil and 500 barrels are treated as imputed newly discovered crude oil.

Example (3). Assume the same facts as in example (1) except that L is a newly discovered separate right to produce and that the surface acreage of L underlain by proved undeveloped oil and gas reserves is 80 acres and the entire surface acreage of the unitized property underlain by proved developed or undeveloped oil and gas reserves is 160 acres. Although all of the production from the unitized property during February would be treated as imputed stripper well crude oil under the rules of paragraph (b) of this section, paragraph (e)(3)(i) provides that imputed stripper well crude oil, imputed heavy oil, and imputed newly discovered crude oil shall be determined by first including the amount determined under paragraph (d)(1)(ii) of this section (subject to the limitation in paragraph (e)(1)(i) of this section). The amount of imputed newly discovered crude oil determined under paragraph (d)(1)(ii) of this section is not limited by paragraph (e)(1)(i) of this section. Thus, as in example (2), the amount of imputed newly discovered crude oil is 5,000 barrels for February. Also as in example (2), paragraph (e)(1)(i) of this section limits imputed stripper well crude oil to 4,000 barrels. The 1,000 barrel excess is allocated between imputed stripper well crude oil and imputed newly discovered crude oil because the unitized property only includes a property that qualified as a stripper well property before the unitization and a newly discovered separate right to produce. The excess is equally allocated between K and L because imputed oil determined without regard to paragraph (e)(1)(i) of this section would be 50 percent imputed stripper well crude oil and 50 percent imputed newly discovered crude oil.

Example (4). Assume the same facts as in example (3). In addition, assume that the unitization agreement does not explicitly allocate imputed stripper well crude oil and imputed newly discovered crude oil between K and L. As in example (3), 4,500 of the barrels produced during February are treated as imputed stripper well crude oil, and 5,500 barrels are treated as imputed newly discovered crude oil. Because the unitization agreement does not explicitly allocate these types of imputed oil, the imputed stripper well crude oil is allocated on the basis of K's and L's proportionate share of production from a stripper well property during the 12-month period immediately preceding the unitization. Because K was the only stripper well property before the unitization, imputed stripper well crude oil is allocated to K, but only to the extent of production allocated to K. Accordingly, 4,000 barrels of imputed stripper well crude oil are allocated to K. Because L was a newly discovered separate right to produce before the unitization, imputed newly discovered crude oil determined under paragraph (d)(1)(ii) of this section (5,000 barrels) is allocated on the basis of each constituent property's proportionate share of production from the unitized property as established by the unitization agreement. Accordingly, L is allocated 3,000 barrels of such imputed newly discovered oil. However, because K has already had allocated to it an amount of imputed stripper well crude oil equal to its share of production from the unitized property, no imputed newly discovered crude oil is allocated to it. The remaining 500 barrels of imputed stripper well crude oil and 2,500 barrels of imputed newly discovered crude oil are allocated to L because it is the only constituent property that has production allocated to it by the unitization agreement in excess of the production in the categories of crude oil allocated to the constituent properties after applying the rules contained in the third, fourth, and fifth sentences of paragraph (e)(6)(i) of this section.

Example (5). Assume the same facts as in example (4). In addition, assume that M holds a working interest in L that entitles M to 50 percent of the production allocated to L. Under paragraph (e)(3)(ii) of this section, the number of barrels of imputed newly discovered crude oil M is permitted to treat as imputed stripper well crude oil is determined by the following formula:

$$A = B \times \frac{C \times \frac{D}{E}}{F}$$

Although M's share of imputed newly discovered crude oil (factor B in the formula) would, in the absence of the second sentence describing factor B in paragraph (e)(3)(ii), be 2,750 barrels (50% of the 5,500 barrels of imputed newly discovered crude oil allocated to L as explained in example (4)), paragraph (e)(3)(ii) limits this amount (for purposes of permitting M to treat a portion of the imputed newly discovered crude oil as imputed stripper well crude oil) to the product of the amount of imputed stripper well crude oil determined under this section without regard to paragraph (e)(3)(i) of this section (5,000 bbls. = 10,000 bbls. × 80 acres/160 acres) multiplied by M's percentage of the share of the production allocated to L (50%). Thus, paragraph (e)(3)(ii) limits the amount to 2,500 barrels (5,000 bbls. × 50%). Accordingly, the formula is applied as follows:

Example (6). Assume the same facts as in example (2) except that L also met the requirements of a stripper well property before the unitization. In addition, assume that M holds a working interest in L that entitles M to 50 percent of the production allocated to L. Under paragraph (e)(4)(ii) of this section, M is permitted to treat all of her share of the production from the unitized property as imputed stripper well crude oil.

Example (7). (i) On January 1, 1983, properties N and O are unitized with P, a newly discovered separate right to produce. A single crude oil reservoir underlies N, O, and P. At the time of the unitization, N qualified as a stripper well property, but all production from O was tier 1 oil. During the 12-month period immediately preceding the unitization, N and O each produced 50,000 barrels of crude oil. The surface acreage of P underlain by proved undeveloped oil and gas reserves is 60 acres, and the entire surface acreage of the unitized property underlain by proved developed or undeveloped oil and gas reserves is 180 acres. Q holds a working interest in P that entitles Q to 50 percent of the production allocated to P. The unitization agreement provides that N and O will each be allocated 30 percent of the production from the unitized property and P will be allocated 40 percent of the production. The unitization agreement also provides that P will be allocated all the imputed stripper well crude oil of the unitized property, and that imputed newly discovered crude oil will be allocated as follows: 35 percent each to N and O and 30 percent to P. (Assume for purposes of this example that it is established by clear and convincing evidence that the allocation of imputed newly discovered crude oil among N, O, and P, and the allocation of all the imputed stripper well crude oil to P do not have as one of their principal purposes the avoidance of windfall profit tax.) During February of 1983, the unitized property produces 12,000 barrels of crude oil. Paragraph (e)(3)(i) of this section provides that imputed oil is determined by first determining the amount of imputed newly discovered crude oil under paragraph (d)(1)(ii) of this section (subject to the limitation contained in paragraph (e)(1)(i) of this section). Thus, 4,000 barrels are treated as imputed newly discovered crude oil.

$$12{,}000\text{ bbls.} \times \frac{60\text{ acres}}{180\text{ acres}}$$

Paragraph (e)(1)(i) of this section does not limit imputed newly discovered crude oil because the production from the unitized property allocated to P exceeds 4,000 barrels (40% × 12,000 = 4,800). Imputed oil for the remaining 8,000 barrels of production from the unitized property is determined under the rules of this section without regard to paragraph (d)(1)(ii) of this section. Under paragraph (b) of this section 4,000 of the remaining 8,000 barrels produced in February from the unitized property would be imputed stripper well crude oil.

$$8{,}000\text{ bbls.} \times \frac{50{,}000\text{ bbls.}}{100{,}000\text{ bbls.}}$$

However, O is allocated only 30 percent of the production from the unitized property. Thus, paragraph (e)(1)(i) of this section limits imputed stripper well crude oil to 3,600 barrels. 30% × 12,000 bbls. The remaining 4,400 barrels of production for February are tier 1 oil (12,000 bbls. − (4,000 bbls. + 3,600 bbls.)).

(ii) Under the unitization agreement P is allocated 40 percent of production, which is 4,800 barrels for February. Of this amount, 3,600 barrels are imputed stripper well crude oil because the unitization agreement allocates all imputed stripper well crude oil to P, and 1,200 barrels are imputed newly discovered crude oil because the unitization agreement allocates 30 percent of the imputed newly discovered crude oil to P (30% × 4,000 bbls.). Because the unitized property includes a newly discovered separate right to produce in which Q held an economic interest in the crude oil in place in the ground immediately before the unitization, Q may treat as imputed stripper well crude oil under paragraph (e)(3)(ii) of this section a certain amount of his share of the imputed newly discovered crude oil allocated to P. That amount is 250 barrels determined as follows:

$$250\text{ bbls.} = 600\text{ bbls.} \times \frac{6{,}000\text{ bbls.} \times \frac{60\text{ acres}}{180\text{ acres}}}{4{,}800\text{ bbls.}}$$

The 600 barrels are Q's share of the 1,200 barrels of imputed newly discovered crude oil determined under paragraph (d)(1)(ii) of this section allocated to P. The 6,000 barrels are the barrels of imputed stripper well crude oil determined without regard to paragraphs (d)(1)(ii) and (e)(1)(i) of this section. The 4,800 barrels are the total barrels allocated to P.

Example (8). On January 1, 1983, a unitized property is formed which is composed of properties R and S and the north halves of T and U. U qualified as a newly discovered crude oil property before the unitization. Fifty percent of the crude oil produced from T and U before the unitization came from wells located on the north halves of T and U and 50 percent from wells located on the south halves. Only crude oil produced from the north halves of T and U during the 12-month period immediately preceding the unitization is counted for purposes of determining the amount of imputed newly discovered crude oil.

(f) *Imputed oil for unitized property with incremental tertiary recovery project.* Solely for the purposes of determining incremental tertiary oil under section 4993 and the effects of that determination on imputed oil, if a qualified tertiary recovery project (as defined in paragraph (c) of §51.4993–1) is located on a unitized property and the unitized property is treated as more than one property under section 4993(d)(3) and paragraph (e)(4) of §51.4993–1 (relating to a tertiary project which only affects a portion of a property), each property (as determined under paragraph (e)(4) of §51.4993–1) is treated as a separate unitized property. The principles of this paragraph may be illustrated by the following example:

Example. (i) Properties A, B, and C were unitized in 1982. During the 12-month period immediately preceding the unitization, A produced 40,000 barrels of tier 1 oil, B produced 40,000 barrels of tier 2 oil, and C produced 160,000 barrels of newly discovered oil. During the 6-month period ending March 31, 1979, properties A and B each produced an average of 4,000 barrels per month, and C had no production during that period. On January 1, 1984, a qualified tertiary recovery project is begun on A. The project can reasonably be expected to significantly increase the ultimate recovery of crude oil from A and B, but not from C. Because the project cannot reasonably be expected to significantly affect the production from C, A and B are treated as a separate unitized property for incremental tertiary oil purposes. During January of 1984 the unitized property without regard to section 4993(d)(3) (the A, B, and C unitized property) produces 24,000 barrels of crude oil, 16,000 barrels of which are produced from C. The base level for incremental tertiary oil is determined by reference only to A and B. The aggregate monthly levels of A and B during the 6-month period (8,000 bbls.) are reduced by one percent per month for 1979, 1980, 1981, 1982 and 1983 for a total reduction of 4,800 bbls. (8,000 bbls. × 60%). Thus the base level is 3,200 bbls. (8,000 bbls. − 4,800 bbls.). Incremental tertiary oil for January of 1984 equals the excess of the January production of the A and B deemed unitized property over the base level or 4,800 barrels. (8,000 bbls. − 3,200 bbls. = 4,800 bbls.) The incremental tertiary oil is allocated between the tier 1 and tier 2 oil produced from the A and B deemed unitized property during January. Production for the A and B deemed unitized property would be 50 percent tier 1 oil and 50 percent tier 2 oil (assuming the rules under paragraph (e) of this section do not apply). Thus, for the A and B deemed unitized property, 1,600 barrels are treated as tier 1 oil (4,000 bbls. − (4,800 bbls. × 4,000 bbls./8,000 bbls.)), 1,600 barrels are treated as tier 2 oil, and 4,800 barrels are treated as tier 3 incremental tertiary oil.

(ii) Assume that without regard to the incremental tertiary oil provisions production from the A, B, and C unitized property for January would be treated under this section as 4,000 barrels of tier 1 oil, 4,000 barrels of tier 2 oil, and 16,000 barrels of tier 3 newly discoverd oil. Because of the incremental tertiary oil provisions, production from the A, B, and C unitized property for January is treated as 1,600 barrels of tier 1 oil, 1,600 barrels of tier 2 oil, 4,800 barrels of tier 3 incremental tertiary oil, and 16,000 barrels of tier 3 newly discovered oil.

(g) *Definitions*. For purposes of this section—

(1) *Unit base production control level*. The term "unit base production control level" has the same meaning that term had under section 212.75 of the energy regulations (10 CFR 212.75) before its removal effective March 30, 1981.

(2) *Heavy crude oil property*. The term "heavy crude oil property" means a property if crude oil produced and sold from that property during either—

(i) The last month before July 1979 in which crude oil was produced and sold from that property, or

(ii) The taxable period, had a weighted average gravity of 16.0 degrees API or less (corrected to 60 degrees Fahrenheit).

(3) *Proved developed oil and gas reserves*. For purposes of this section, "proved developed oil and gas reserves" are reserves that can be expected to be recovered through existing wells with existing equipment and operating methods. Additional oil and gas expected to be obtained through the application of fluid injection or other improved recovery techniques for supplementing the natural forces and mechanisms of primary recovery should be included as "proved developed oil and gas reserves"only after testing by a pilot project or after the operation of an installed program has confirmed through production response that increased recovery will be achieved.

(4) *Proved undeveloped oil and gas reserves*. For purposes of this section, "proved undeveloped oil and gas reserves" are reserves that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required for recompletion. Reserves on undrilled acreage shall be limited to those drilling units offsetting productive units that are reasonably certain of production when drilled. Proved reserves for other undrilled units can be claimed only where it can be demonstrated with certainty that there is continuity of production from the existing productive formation. Under no circumstances should estimates for proved undeveloped oil and gas reserves be attributable to any acreage for which an application of fluid injection or other improved recovery technique is contemplated, unless such techniques have been proved effective by actual tests in the area and in the same reservoir.

These proposed amendments are to be issued under the authority of Code section 4997(b) (94 Stat. 250, 26 U.S.C. 4997(b)), which grants the Secretary of the Treasury or his delegate authority to prescribe regulations necessary or appropriate to carry out the purpose of the windfall profit tax (including changes in the application of the energy regulations), and the more general regulatory authority contained in Code section 7805 (68A Stat. 917, 26 U.S.C. 7805).

Roscoe L. Egger, Jr.,
Commissioner of
Internal Revenue

(Filed by the Office of the Federal Register on September 29, 1986, 8:45 a.m., and published in the issue of Federal Register for September 30, 1986, 51 F.R. 34653)

Deletions from Cumulative List of Organizations Contributions to Which Are Deductible Under Section 170 of the Code

Announcement 86–105

The names of organizations that no longer qualify as organizations described in section 170(c)(2) of the Internal Revenue Code of 1954 are listed below.

Generally, the Service will not disallow deductions for contributons made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgment has been timely filed, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deductible. Protection under section 7428(c) would begin on October 27, 1986, (the date of publication of this announcement) and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is $1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

Copperweld Steel Company's Warren
Employees Trust, Warren, OH

Modern School of Music,
Washington, DC

World University, Inc.,
Hato Rey, PR

Annoucement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practible for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Robert D. Digby	North Little Rock, AR	Certified Public Accountant	Four Months from July 29, 1986
Jeffrey E. Ellis	Rockland, ME	Certified Public Accountant	Indefinite from July 2, 1986
Charles L. Honey	Prescott, AR	Attorney	One Year from July 2, 1986
Bernhardt Karp	Hudson, NY	Attorney & Certified Pubic Accountant	Indefinite from July 29, 1986
George N. Meros	Springfield, MO	Attorney	Indefinite from July 25, 1986
William G. Waldrop	Adamsville, AL	Certified Public Accountant	Indefinite from July 17, 1986
S. Melvin Apotheker	Miami, FL	Attorney	Indefinite from September 1, 1986
Sandra S. Behn	London, TN	Certified Public Accountant	Indefinite from September 12, 1986
Charles K. Hyter	Hutchinson, KS	Attorney	Indefinite from September 18, 1986
William Pyke	Dallas, TX	Certified Public Accountant	Eighteen Months from August 15, 1986
Alan Z. Richards	West Hempstead, NY	Attorney and Certified Public Accountant	Indefinite from September 20, 1986

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to identify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
David P. Rosenberg	Philadelphia, PA	Indefinite effective August 13, 1986
Paul Beecher	Torrance, CA	Indefinite effective September 25, 1986

Under 31 Code of Federal Regulations, Part 10, an enrolled agent, in order to avoid the institution of a proceeding for his disbarment of suspension from practice before the Internal Revenue Service, may offer his resignation. The Director of Practice, in his discretion, may accept the offered resignation of an enrolled agent.

To enable the public and other practitioners to identify such resigned enrolled agents, the Director of Practice will announce in the Internal Revenue Bulletin the name and address of each enrolled agent who has resigned and the effective date of resignation. This announcement will appear in the weekly Bulletin at the earliest practicable date after the action and will continue to appear in the weekly Bulletins for five successive weeks or for as many weeks as is practicable for each resigned enrolled agent, and will later be consolidated and published in the Cumulative Bulletin.

The following individual has entered a consent resignation from enrollment to practice before the Internal Revenue Service:

Name of Enrolled Agent	Address	Effective Date of Resignation
William E. Bonafede	Wakefield, RI	September 30, 1986

Under Section 330, Title 31 of the United States Code, the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
James L. Ketner	Charlotte, NC	Certified Public Accountant	September 27, 1986
George L. Weil	Orange, CT	Certified Public Accountant	September 27, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 51.4989–1, 51.4996–1, 51.4996–3 amended; 51.4996–4 added	Definition of "property" for purposes of the windfall profit tax	1986–42 I.R.B. 15	Nov. 11, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR— Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

NOTES

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______	1927-1	$8.00
______	*1927-2*	*18.00*
______	1928-1	8.00
______	1928-2	10.00
______	1929-1	13.00
______	*1929-2*	*3.50*
______	1930-1	8.50
______	1930-2	10.00
______	*1931-1*	*4.00*
______	1931-2	14.00
______	*1932-1*	*3.25*
______	1932-2	10.00
______	*1933-1*	*3.75*
______	*1933-2*	*4.00*
______	*1934-1*	(**)
______	1934-2	15.00
______	1935-1	8.00
______	*1935-2*	*15.00*
______	*1936-1*	*4.00*
______	*1936-2*	*15.00*
______	*1937-1*	*14.00*
______	1937-2	8.50
______	*1938-1*	*17.00*
______	*1938-2*	*14.00*
______	1939-1-1	9.50
______	1939-1-2	12.00
______	1939-2	10.00
______	1940-1	6.50
______	1940-2	15.00
______	1941-1	8.00
______	*1941-2*	*4.00*
______	1942-1	8.00
______	*1942-2*	*6.50*
______	*1943-(*)*	*11.00*
______	*1944-(*)*	*9.00*
______	1945-(*)	10.00
______	*1946-1*	*3.00*
______	1946-2	6.00
______	*1947-1*	*2.00*
______	1947-2	3.75
______	*1948-1*	*3.50*
______	1948-2	8.50
______	*1949-1*	*8.00*
______	*1949-2*	*3.25*
______	1950-1	7.00
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Internal Revenue
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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–124, page 4.
Mortgage revenue bonds and mortgage credit certificates; income limits. Guidelines prescribe the manner in which the income limits applicable to mortgage revenue bonds and mortgage credit certificates are to be applied to meet the requirements of section 1301 of the Tax Reform Act of 1986.

Rev. Rul. 86–127, page 4.
Credit for producing fuel from a nonconventional source. Prior to July 1, 1987, only section 103 gas that is produced from a formation that is located at a depth of more than 5,000 feet is deregulated for purposes of the Natural Gas Policy Act. Rev. Rul. 86–19 modified and superseded.

Rev. Rul. 86–128, page 10.
Federal short-term, mid-term, and long-term rates. For purposes of section 1274(d) of the Code, relating to certain transactions in which a debt instrument is issued for property, a table sets forth the applicable federal short-term, mid-term, and long-term rates for November 1986.

Rev. Proc. 86–39, page 11.
U.S. citizen abroad; waiver of residency requirements. Countries and time periods are listed that qualify for the waiver of residency requirements of section 911(d)(1) of the Code. Rev. Proc. 81–23 supplemented.

LR–262–82, page 25.
Proposed regulations under section 1361 of the Code relate to the definition of the term "S corporation."

Announcement 86–106, page 32.
A public hearing will be held December 1, 1986, on proposed regulations relating to transfers of property by U.S. persons to foreign corporations.

Announcement 86–107, page 32.
The temporary regulations under section 338(h)(10) of the Code will soon be amended to require the use solely of the MADSP formula for determination of deemed sale price.

EXEMPT ORGANIZATIONS

Ct. D. 2035, page 5.
Unrelated business taxable income; advertising revenues of monthly medical journal. The publication of paid advertising in a monthly medical journal is not substantially related to the educational purposes of the journal and the profits from advertising are unrelated business taxable income. **American College of Physicians,** Supreme Court of the United States.

ADMINISTRATIVE

Rev. Proc. 86–40, page 11.
Forms; magnetic tape; Form 1042S. Requirements and conditions under which withholding agents may file Form 1042S information returns on magnetic tape are updated. Rev. Proc. 85–53 superseded.

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Finding Lists begin on page 37.
Announcement of Disbarments and Suspensions begin on page 33.
Announcement of Notice of Proposed Rulemaking on page 35.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 25.—Interest on Certain Home Mortgages

Guidelines prescribe the manner in which the income limits applicable to mortgage credit certificates are to be applied. See Rev. Rul. 86-124, this page.

Section 29.—Credit For Producing Fuel From A Nonconventional Source

Credit for producing fuel from a nonconventional source. Prior to July 1, 1987, only section 103 gas that is produced from a formation that is located at a depth of more than 5,000 feet is deregulated for purposes of the Natural Gas Policy Act. Rev. Rul. 86–19 modified and superseded.

Rev. Rul. 86–127

This revenue ruling corrects Rev. Rul. 86–19, 1986–1 C.B. 4, which incorrectly stated that all section 103 gas is deregulated for purposes of the NGPA. This correction to Rev. Rul. 86–19 is effective as if it had originally appeared in Rev. Rul. 86–19. Rev. Rul. 86–19 should have read as follows:

Section 29(a) of the Code (formerly Section 44D(a)) provides a credit against income tax of $3 per barrel-of-oil equivalent of qualified fuels sold by the taxpayer during the taxable year, subject to stated conditions. Section 29(c)(1)(B) provides that the term "qualified fuels" includes "gas produced from . . . a tight formation." However, section 29(c)(2)(B)(i) provides that the term "gas produced from a tight formation" shall only include gas the price of which is regulated by the United States.

Section 121 of the Natural Gas Policy Act of 1978, Pub. L. No. 95–621, 15 U.S.C. section 3331 (1982) (NGPA) eliminated price controls as of January 1, 1985, on certain categories of natural gas classified under section 102(c) and section 103(c) of the NGPA. The Federal Energy Regulatory Commission (FERC) has issued regulations concerning the types of gas that were deregulated by section 121. *See* 49 Fed. Reg. 46,874 (Nov. 29, 1984). These regulations include amendments to 18 C.F.R. section 272.103(a), which defines "deregulated natural gas." *See* 49 Fed. Reg. 46,884. The FERC also decided that gas is deregulated if it falls into two or more categories any one of which is a deregulated category. *See* 49 Fed. Reg. 46,877–79.

Thus, gas produced and sold after December 31, 1984, that falls under any of the categories listed in 18 C.F.R. section 272.103(a) (as amended) is gas the price of which is not regulated by the United States. Gas produced from a tight formation is generally classified as section 107(c)(5) gas under the NGPA. However, a considerable amount of section 107(c)(5) gas also is classified as section 102 or 103 gas. Thus, if gas from a tight formation also qualifies under section 102 or is section 103 gas that is produced from a formation that is located at a depth of more than 5,000 feet, it is deregulated for purposes of the NGPA. (Section 103 gas that is produced from a formation that is located 5,000 feet or shallower from the surface will be deregulated for purposes of the NGPA as of July 1, 1987). In accordance with section 29(c)(2)(B)(i) of the Code, even if deregulated gas would otherwise qualify as gas produced from a tight formation, it is not a qualified fuel under section 29(c), and producers of the gas are not eligible for the credit allowed by section 29(a).

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 86–19 is modified and superseded.

Section 143.—Mortgage Revenue Bonds

(Also Section 25.)

Mortgage revenue bonds and mortgage credit certificates; income limits. Guidelines prescribe the manner in which the income limits applicable to mortgage revenue bonds and mortgage credit certificates are to be applied to meet the requirements of section 1301 of the Tax Reform Act of 1986.

Rev. Rul. 86–124[1]

This revenue ruling contains guidelines prescribing the manner in which the income limits applicable to mortgage revenue bonds and mortgage credit certificates are to be applied.

BACKGROUND

Section 1301 of the Tax Reform Act of 1986, Pub. L. 99–100 Stat. added new income limits to the requirements that must be met in order for interest on a qualified mortgage bond to be excluded from gross income under section 103(a) of the Internal Revenue Code. In general, new section 143(f) of the Code provides that the income requirement is met if all owner-financing provided under the issue is provided for mortgagors whose family income is 115 percent or less of the applicable median family income. New section 143(f)(2) provides that family income and area median gross income are to be determined by the Secretary after taking into account the regulations prescribed under section 8 of the United States Housing Act of 1937. The new income requirement, in general, applies to obligations issued after August 15, 1986.

These income requirements also apply to mortgage credit certificates issued under section 25 of the Code. A mortgage credit certificate provides a credit against federal income tax to the recipient of the credit for a portion of the interest paid on the recipient's mortgage loan on his or her principal residence.

With respect to any residence, section 143(f)(4) defines the term "applicable median family income" as the greater of—

(A) The area median gross income for the area in which the residence is located, or

(B) The area median gross income for the state in which the residence is located.

GUIDELINES

Until regulations are issued, determinations of family income and applicable median family income are to be made in the manner prescribed in this revenue ruling.

For purposes of section 143(f)(4), the "area median gross income" for an area or state must be determined in a manner consistent with the determination of "median gross income" for the area or state under section 8 of the United States Housing Act of 1937, as amended, with adjustments for areas of unusually high or low income. These adjustments must be made in the manner that these adjustments are made for purposes of section 8 of the United States Housing Act of 1937, as amended. Thus, in determining area median gross income, issuers must use the Revised Income Limits for Lower Income and Very Low Income under the Housing Act of 1937. The most recent limits were released by the Department of Housing and Urban Development in

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[1] Also released as News Release IR–86–136, dated October 14, 1986.

November 1985; these income limits may be relied upon until 30 days after the release of updated income limits. In using these limits, issuers must multiply the "very low income" limit for the area by 2.3 to apply the 115 percent limit of section 143(f)(1) and by 2.8 to apply the 140 percent limit of section 143(f)(3). Adjustments for family size are not required for purposes of determining area median gross income. (Issuers may, however, make adjustments for smaller and larger families if these adjustments are made with respect to all owner-financing provided under an issue.)

For purposes of applying the income requirements of section 143(f), the "family income" of a mortgagor (or mortgagors) is the mortgagor's annualized gross income. Annualized gross income is gross monthly income multiplied by 12. Gross monthly income is the sum of monthly gross pay; any additional income from overtime, part-time employment, bonuses, dividends, interest, royalties, pensions, Veterans Administration (VA) compensation, net rental income, *etc.;* and other income (such as alimony, child support, public assistance, sick pay, social security benefits, unemployment compensation, income received from trusts, and income received from business activities or investments). Information with respect to gross monthly income may be obtained from available loan documents executed during the 4-month period ending on the date of the closing of the mortgage, provided that any gross monthly income not included on the loan documents must be included by the issuer in determining gross monthly income. Thus, for example, if the mortgagor does not include alimony on the loan documents, the issuer in determining gross monthly income must determine the amount of alimony and add that amount to the amount shown on the loan documents. The income to be taken into account in determining the gross monthly income is the income of the mortgagor (or mortgagors) and any other person who is expected both to live in the residence being financed and to be secondarily liable on the mortgage.

Issuers who wish to use information from available loan documents under the restrictions described in the preceding paragraph may, for example, find that information on (1) lines 23D and 23E on the Application for VA of FMHA Home Loan Guaranty of the HUD/FHA Insured Mortgage (VA Form 26–1802a, HUD 92900, Jan. 1982), or (2) the total line from the Gross Monthly Income section of FHLMC Residential Loan Application form (FHLMC 65 Rev. 8/78).

For purposes of section 143(a)(2)(B)(ii) (relating to good faith effort to comply), in determining whether 95 percent or more of the proceeds devoted to owner-financing was devoted to residences with respect to which the income requirement was met, the issuer may rely on an affidavit of the mortgagor stating that the family income of the mortgagor does not exceed the applicable income limit.

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term and long-term rates are set forth for the month of November 1986. See Rev. Rul. 86–128, page 10.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of November 1986, See Rev. Rul. 86–128, page 10.

Section 468.—Special Rules for Mining and Solid Waste Reclaimation and Closing Costs

Federal short-term, mid-term and long-term rates are set forth for the month of November 1986. See Rev. Rul. 86–128, page 10.

Section 513.—Unrelated Trade or Business

26 CFR 1.513–1: Definition of unrelated trade or business.

Ct. D. 2035

SUPREME COURT
OF THE
UNITED STATES
No. 84–1737

United States v. American College
of Physicians
[U.S.]

On Writ of Certiorari to the
United States
Court of Appeals
for the Federal Circuit

[April 22, 1986]

Syllabus

Section 511(a)(1) of the Internal Revenue Code imposes a tax on the "unrelated business taxable income" of tax-exempt organizations. Section 512(a)(1) defines "unrelated business taxable income" as the gross income derived by such an organization from any "unrelated trade or business . . . regularly carried on by it," and §513(a) defines "unrelated trade or business" as "any trade or business the conduct of which is not substantially related" to the organization's tax-exempt purposes. Respondent tax-exempt organization, in furtherance of its exempt purposes of maintaining high standards in medical education and practice, encouraging research, and fostering measures for preventing disease and improving public health, publishes a monthly medical journal containing articles relevant to the practice of internal medicine. Each issue of the journal contains paid advertisements for pharmaceuticals, and medical supplies and equipment useful in the practice of internal medicine. After respondent had paid taxes on its net income from such advertisements in 1975, it filed a claim for a refund, and when the Government demurred, ultimately filed suit in the United States Claims Court, which held that the advertisements were not substantially related to respondent's tax-exempt purposes and that therefore the advertising proceeds were taxable. The Court of Appeals reversed. Taking the view that the Claims Court had focused too much on the commercial character of advertising business and not enough on the advertisement's contribution to the education of the medical journal's readers, the Court of Appeals that respondent had established the requisite substantial relation and its entitlement to exemption from taxation.

Held: Respondent must pay a tax on the profits it earns from the advertisements. Pp. 3–15.

(a) It is undisputed that respondent's publication of paid advertising is a "trade or business" and that the business is "regularly carried on." Pp. 4–6.

(b) There is no merit to the Government's argument that Congress and the Treasury intended to establish a blanket rule requiring the taxation of income from all commercial advertising by tax-exempt professional journals without a specific analysis of the circumstances. There is no support for such a rule in the regulations or in the legislative history of the Internal Revenue Code. Pp. 6–12.

(c) In this case, however, based on the Claims Court's finding of facts that are adequately supported by the record, and considering those facts in light of the applicable legal standard, it must be concluded that the advertisements in question were not "substantially related," or in the words of the implementing regulation did not "contribute importantly," to the medical journal's educational purposes. The Claims Court properly directed its attention to respondent's conduct of its advertising business, whereas the Court of Appeals erroneously focused exclusively upon the information conveyed by commercial advertising and consequently failed to give effect to the governing statute and regulations. Pp. 12–15.

743 F. 2d 1570, reversed.

MARSHALL, J., delivered the opinion for a unanimous Court. BURGER, C.J., filed a concurring opinion, in which POWELL, J., joined.

JUSTICE MARSHALL delivered the opinion of the Court.

A tax-exempt organization must pay tax on income that it earns by carrying on a business not "substantially related" to the purposes for which the organization has received its exemption from federal taxation. The question before this Court is whether respondent, a tax-exempt organiztion, must pay tax on the profits it earns by selling commercial advertising space in its professional journal, The Annals of Internal Medicine.

I

Respondent, the American College of Physicians, is an organization exempt from taxation under §501(c)(3) of the Internal Revenue Code.[1] The purposes of the College, as stated in its articles of incorporation, are to maintain high standards in medical education and medical practice; to encourage research, especially in clinical medicine; and to foster measures for the prevention of disease and for the improvement of public health. App. 16a. The principal facts were stipulated at trial. In furtherance of its exempt purposes, respondent publishes The Annals of Internal Medicine (Annals), a highly regarded monthly medical journal containing scholarly articles relevant to the practice of internal medicine. Each issue of Annals contains advertisements for pharmaceuticals, medical supplies, and equipment useful in the practice of internal medicine, as well as notices of positions available in that field. Respondent has a longstanding policy of accepting only advertisements containing information about the use of medical products, and screens profferred advertisements for accuracy and relevance to internal medicine. The advertisements are clustered in two groups, one at the front and one at the back of each issue.

In 1975, Annals produced gross advertising income of $1,376,322. After expenses and deductible losses were subtracted, there remained a net income of $153,388. Respondent reported this figure as taxable income and paid taxes on it in the amount of $55,965. Respondent then filed a timely claim with the Internal Revenue Service for refund of these taxes, and when the Government demurred, filed suit in the United States Claims Court.

The Claims Court held a trial and concluded that the advertisements in Annals were not substantially related to respondent's tax-exempt purposes. 3 Cl. Ct. 531 (1983). Rather, after finding various facts regarding the nature of the College's advertising business, it concluded that any correlation between the advertisements and respondent's educational purpose was incidental because "the comprehensiveness and content of the advertising package is entirely dependent on each manufacturer's willingness to pay for space and the imagination of its advertising agency." *Id.*, at 535. Accordingly, the court determined that the advertising proceeds were taxable.

The Court of Appeals for the Federal Circuit reversed. It held clearly erroneous the trial court's finding that the advertising was not substantially related to respondent's tax-exempt purpose. The Court of Appeals believed that the trial court had focused too much on the commercial character of the advertising business and not enough on the actual contribution of the advertisements to the education of the journal's readers. It held that respondent had established the requisite substantial relation and its entitlement to exemption from taxation. 743 F. 2d 1540, 1578 (1984). We granted the Government's petition for certiorari, 473 U.S. ____(1985), and now reverse.

II

The taxation of business income not "substantially related" to the objectives of exempt organizations dates from the Revenue Act of 1950, Ch. 994, 64 Stat. 906 (1950 Act). The statute was enacted in response to perceived abuses of the tax laws by tax-exempt organizations that engaged in profitmaking activities. Prior law had required only that the profits garnered by exempt organizations be used in furtherance of tax-exempt purposes, without regard to the source of those profits. See *Trinidad* v. *Sagrada Orden de Predicadores,* 263 U.S. 578, 581 (1924); *C. F. Mueller Co.* v. *Commissioner,* 190 F.2d 120 (CA3 1951); *Roche's Beach, Inc.* v. *Commissioner,* 96 F. 2d 776 (CA2 1938). As a result, tax-exempt organizations were able to carry on full-fledged commercial enterprises in competition with corporations whose profits were fully taxable. See Revenue Revision of 1950: Hearings before the House Committee on Ways and Means. Vol. I, 81st Cong., 2d Sess., 18–19 (1950) (hereinafter cited as 1950 House Hearings) (describing universities' production of "automobile parts, chinaware, and food products, and the operation of theatres, oil wells, and cotton gins"). Congress perceived a need to restrain the unfair competition fostered by the tax laws. See H. R. Rep. No. 2319, 81st Cong., 2d Sess., 36–37 (1950).

Nevertheless, Congress did not force exempt organizations to abandon all commercial ventures, nor did it levy a tax only upon businesses that bore no relation at all to the tax-exempt purposes of an organization, as some of the 1950 Act's proponents had suggested. See, *e.g.*, 1950 House Hearings, *supra*, at 4, 19, 165. Rather, in the 1950 Act it struck a balance between its two objectives of encouraging benevolent enterprise and restraining unfair competition by imposing a tax on the "unrelated business taxable income" of tax-exempt organizations. 26 U.S.C. §511(a)(1).

"Unrelated business taxable income" was defined as "the gross income derived by any organization from any unrelated trade or business . . . regularly carried on by it . . . " §512(a)(1). Congress defined an "unrelated trade or business" as "any trade or business the conduct of which is not substantially related . . . to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption . . . " §513(a). Whether respondent's advertising income is taxable, therefore, depends upon (1) whether the publication of paid advertising is a "trade or business," (2) whether it is regularly carried on, and (3) whether it is substantially related to respondent's tax-exempt purposes.

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[1] Title 26 U.S.C. §501(c)(3) exempts from taxation entities "organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes," with certain restrictions on their activities, including prohibition of political activity.

III

A

Satisfaction of the first condition is conceded in this case, as it must be, because Congress has declared unambiguously that the publication of paid advertising is a trade or business activity distinct from the publication of accompanying educational articles and editorial comment.

In 1967, the Treasury promulgated regulations interpreting the unrelated business income provision of the 1950 Act. The regulation defined "trade or business" to include not only a complete business enterprise, but also any component activity of a business. Treas. Reg. §1.513–1(b), 26 CFR §1.513–1(b) (1985) (first published at 32 Fed. Reg. 17657 (1967)).[2] This revolutionary approach to the identification of a "trade or business" had a significant effect on advertising, which theretofore had been considered simply a part of a unified publishing business. The new regulation segregated the "trade or business" of selling advertising space from the "trade or business" of publishing a journal, an approach commonly referred to as "fragmenting" the enterprise of publishing into its component parts:

> "activities of soliciting, selling, and publishing commercial advertising do not lose identity as a trade or business even though the advertising is published in an exempt organization periodical which contains editorial matter related to the exempt purposes of the organization." 26 CFR §1.513–1(b).

In 1969, Congress responded to widespread criticism of those Treasury regulations[3] by passing the Tax Reform Act of 1969, Pub. L. 91–172, 83 Stat. 487 (1969 Act). That legislation specifically endorsed the Treasury's concept of "fragmenting" the publishing enterprise into its component activities, and adopted, in a new §513(c), much of the language of the regulation that defined advertising as a separate trade or business:

> "Advertising, etc., activities . . . an activity does not lose identity as a trade or business merely because it is carried on . . . within a larger complex of other endeavors which may, or may not, be related to the exempt purposes of the organization." 26 U.S.C. §513(c).

The statute clearly established advertising as a trade or business, the first prong of the inquiry into the taxation of unrelated business income.

The presence of the second condition, that the business be regularly carried on, is also undisputed here. The satisfaction of the third condition, however, that of "substantial relation," is vigorously contested, and that issue forms the crux of the controversy before us.

B

According to the Government, Congress and the Treasury established a blanket rule that advertising published by tax-exempt professional journals can never be substantially related to the purposes of those journals and is, therefore, always a taxable business. Respondent, however, contends that each case must be determined on the basis of the characteristics of the advertisements and journal in question. Each party finds support for its position in the governing statute and regulations issued by the Department of the Treasury.

In its 1967 regulations, the Treasury not only addressed the "fragmentation" issue discussed above, but also attempted to clarify the statutory "substantially related" standard found in §513(a). It provided that the conduct of a tax-exempt business must have a causal relation to the organization's exempt purpose (other than through the generation of income), and that "the production or distribution of the goods or the performance of the services from which the gross income is derived must *contribute importantly* to the accomplishment of [the exempt] purposes." Treas. Reg. §1.513–1(d)(2), 26 CFR §1.513–1(d)(2) (1985) (emphasis added). In illustration of its new test for substantial relation, the Treasury provided an example whose interpretation is central to the resolution of the issue before us. Example 7 of Treas. Reg. §1.513–1(d)(4)(iv) involves "Z," an exempt association formed to advance the interests of a particular profession and drawing its membership from that profession. Z publishes a monthly journal containing articles and other editorial material that contribute importantly to the tax-exempt purpose. Z derives income from advertising products within the field of professional interest of the members:

> "Following a practice common among taxable magazines which publish advertising, Z requires its advertising to comply with certain general standards of taste, fairness, and accuracy; but within those limits the form, content, and manner of presentation of the advertising messages are governed by the basic objective of the advertisers to promote the sale of the advertised products. While the advertisements contain certain information, the informational function of the advertising is incidental to the controlling aim of stimulating demand for the advertised products and differs in no essential respect from the informational function of any commercial advertising. Like taxable publishers of advertising, Z accepts advertising only from those who are willing to pay its published rates. Although continuing education of its members in matters pertaining to their profession is one of the purposes for which Z is granted exemption, the publication of advertising designed and selected in the manner of ordinary commercial advertising is not an educational activity of the kind contemplated by the exemption statute; it differs fundamentally from such an activity both in its governing objective and in its method. Accordingly, Z's publication of advertising does not contribute importantly to the accomplishment of its exempt purposes; and the income which it derives from advertising constitutes gross income from unrelated trade or business." §1.513–1(d)(4)(iv), Example 7.

The Government contends both that Example 7 creates a *per se* rule of taxation for journal advertising income and that

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[2] The 1967 Treasury regulations at issue in this case, published in final form at 32 Fed. Reg. 17657 (1967), have not been amended in pertinent part since their promulgation, and references to those regulations herein are to the current version.

[3] See, *e.g.*, Moore, Current Problems of Exempt Organizations, 24 Tax L. Rev. 469, 476 (1969); Middleditch & Webster, The new unrelated business income Regs: what they mean; how to cope with them, 28 J. Tax. 174, 178 (1968); Webster. New proposals change definition of unrelated business income, 27 J. Tax. 42, 43 (1967); Weithorn & Liles, Unrelated Business Income Tax: Changes Affecting Journal Advertising Revenues, 45 Taxes 791, 798 (1967). See also Tax Reform, 1969: Hearings Before the House Committee on Ways and Means, 91st Cong., 1st Sess. 11129, 1184, 1223 (1969). Numerous bills were introduced in the 90th Congress, 1st Session, in an unsuccessful attempt to overturn the regulations, even before they became final. See, *e.g.*, H.R. 8765; H.R. 8766; H.R. 9103; H.R. 9468; H.R. 9661; H.R. 9763; H.R. 10150; H.R. 10997; H.R. 10998; H.R. 11491; H.R. 11492. And several years later, two federal courts struck down the 1967 regulations as exceeding pre-1969 statutory authority, insofar as they required the "fragmentation" of publishing activities. See *American College of Physicians* v. *United States*, 530 F. 2d 930, 933 (Ct. Cl. 1976); *Massachusetts Medical Society* v. *United States*, 514 F. 2d 153, 154 (CA1 1975).

Congress intended to adopt that rule, together with the remainder of the 1967 regulations, into law in the 1969 Act. We find both of these contentions unpersuasive.

Read as a whole, the regulations do not appear to create the type of blanket rule of taxability that the Government urges upon us. On the contrary, the regulations specifically condition tax exemption of business income upon the importance of the business activity's contribution to the particular exempt purpose at issue, and direct that "[w]hether activities productive of gross income contribute importantly to the accomplishment of any purpose for which an organization is granted an exemption depends *in each case* upon the facts and circumstances involved," *id.*, §1.513–1(d)(2) (emphasis added). Example 7 need not be interpreted as being inconsistent with that general rule. Attributing to the term "example" its ordinary meaning, we believe that Example 7 is best construed as an illustration of one possible application, under given circumstances, of the regulatory standard for determining substantial relation.

The interpretative difficulty of Example 7 arises primarily from its failure to distinguish clearly between the statements intended to provide hypothetical facts and those designed to posit the necessary legal consequences of those facts. Just at the point in the lengthy Example at which the facts would appear to end and the analysis to begin, a pivotal statement appears: "the informational function of the advertising is incidental to the controlling aim of stimulating demand for the advertised products." The Government's position depends upon reading this statement as a general proposition of law, while respondent would read it as a statement of fact that may be true by hypothesis of "Z" and its journal, but is not true of Annals.

We recognize that the language of the Example is amenable to either interpretation. Nevertheless, several considerations lead us to believe that the Treasury did not intend to set out a *per se* statement of law. First, when the regulations were proposed in early 1967, the Treasury expressed a clear intention to treat all commercial advertising as an unrelated business. See Technical Information Release No. 889, CCH 1967 Stand. Fed. Tax Rep. §6557. When the regulations were issued in final form, however, following much criticism and the addition of Example 7, they included no such statement of intention. 32 Fed. Reg. 17657 (1967). Second, a blanket rule of taxation for advertising in professional journals would contradict the explicit case-by-case requirement articulated in Treas. Reg. §1.513–1(d)(2), and we are reluctant to attribute to the Treasury an intention to depart from its own general principle in the absence of clear support for doing so. Finally, at the time the regulations were issued, the 1950 Act had been interpreted to mean that business activities customarily engaged in by tax-exempt organizations would continue to be considered "substantially related" and untaxed. See Note, The Macaroni Monopoly: The Developing Concept of Unrelated Business Income of Exempt Organizations, 81 Harv. L. Rev. 1280, 1291 (1968). A *per se* rule of taxation for activity, traditional among tax-exempt journals, of carrying commercial advertising would have been a significant departure from that prevailing view. Thus, in 1967 the idea of a *per se* rule of taxation for all journal advertising revenue was sufficiently controversial, its effect so substantial, and its statutory authorization so tenuous, that we simply cannot attribute to the Treasury the intent to take that step in the form of an ambiguous example, appended to a subpart of a subsection of a subparagraph of a regulation.

It is still possible, of course, that, regardless of what the Treasury actually meant by its 1967 regulations, Congress read those regulations as creating a blanket rule of taxation, and intended to adopt that rule into law in the 1969 Act. The Government appears to embrace this view, which it supports with certain statements in the legislative history of the 1969 Act. For example, the Government cites to a statement in the House Report, discussing, the taxation of advertising income of journals published by tax-exempt organizations:

> "Your committee believes that a business competing with taxpaying organizations should not be granted an unfair competitive advantage by operating tax free unless the business contributes importantly to the exempt function. It has concluded that by that standard, advertising in a journal published by an exempt organziation is not related to the organization's exempt functions, and therefore it believes that this income should be taxed." H. R. Rep. No. 91–413, pt. 1, p. 50 (1969).

Similar views appear in the Senate Report:

> "Present law.—In December 1967, the Treasury Department promulgated regulations under which the income from advertising and similar activities is treated as 'unrelated business income' even though such advertising for example may appear in a periodical related to the educational or other exempt purpose of the organization.
>
> "General reasons for change.—The committee agrees with the House that the regulations reached on appropriate result in specifying that when an exempt organization carries on an advertising business in competition with other taxpaying advertising businesses, it should pay a tax on the advertising income. The statutory language on which the regulations are based, however, is sufficiently unclear so that substantial litigation could result from these regulations. For this reason, the committee agrees with the House that the regulations, insofar as they apply to advertising and related activities, should be placed in the tax laws." S. Rep. No. 91–552, 75 (1969).

Based on this language, the Government argues that the 1969 Act created a *per se* rule of taxation for advertising income. The weakness of this otherwise persuasive argument, however, is that the quoted discussion appears in the Reports solely in support of the legislators' decision to enact §513(c), the provision approving the fragmentation of "trade or business." Although §513(c) was a significant change in the tax law that removed one barrier to the taxation of advertising proceeds, it cannot be construed as a comment upon the two other distinct conditions—"regularly carried on" and "not substantially related"—whose satisfaction is prerequisite to taxation of business income under the 1950 Act. Congress did not incorporate into the 1969 Act the language of the regulation defining "substantial relation," nor did the statute refer in any other way to the issue of the relation between advertising and exempt functions, even though that issue has been hotly debated at the hearings. See, *e.g.*, *Tax Reform, 1969: Hearings Before the House Committee on Ways and Means*, 91st Cong., 1st Sess., 1113, 1118, 1192, 1241 (1969). Thus, we have no reason to conclude from the Committee Reports that Congress resolved the dispute whether, in a specific case, a journal's carriage of advertising could so advance its educational objectives as to be "substantially related" to those objectives within the meaning of the 1950 Act.

It is possible that the Committees' discussion of advertising reflects merely an erroneous assumption that the "fragmentation" provision of §513(c), without more, would establish the automatic taxation of journal advertising revenue. Alternatively, the quoted passages could be read to indicate the Committees' intention affirmatively to endorse what they believed to be existing practice, or even to change the law substantially. The truth is that, other than a general reluctance to consider commercial advertisements generally as substantially related to the purposes of tax-exempt journals, no congressional view of the issue emerges from the quoted excerpts of the Reports.[4] Thus, despite the Reports' seeming endorsement of a *per se* rule, we are hesitant to rely on that inconclusive legislative history either to supply a provision *not* enacted by Congress, see *Commissioner* v. *Acker,* 361 U.S. 87, 93 (1959); J. Mertens, Law of Federal Income Taxation §3.29 (Weinstein rev. 1985), or to define a statutory term enacted by a prior Congress. See *SEC* v. *Sloan,* 436 U.S. 103, 121 (1978); *United States* v. *Price,* 361 U.S. 304, 313 (1960). *Cf. TVA* v. *Hill,* 437 U.S. 153, 193 (1978). We agree, therefore, with both the Claims Court and the Court of Appeals in their tacit rejection of the Government's argument that the Treasury and Congress intended to establish a *per se* rule requiring the taxation of income from all commercial advertisments of all tax-exempt journals without a specific analysis of the circumstances.[5]

IV

It remains to be determined whether, in this case, the business of selling advertising space is "substantially related"—or, in the words of the regulation, "contributes importantly"—to the purposes for which respondent enjoys an exemption from federal taxation. Respondent has maintained throughout this litigation that the advertising in Annals performs an educational function supplemental to that of the journal's editorial content. App. 7a. Testimony of respondent's witnesses at trial tended to show that drug advertising performs a valuable function for doctors by disseminating information on recent developments in drug manufacture and use. App. 27a, 38a, 43a. In addition, respondent has contended that the role played by the Food and Drug Administration, in regulating much of the form and content of prescription-drug advertisements, enhances the contribution that such advertisements make to the readers' education. All of these factors, respondent argues, distinguish the advertising in Annals from standard commercial advertising. Respondent approaches the question of substantial relation from the perspective of the journal's subscribers; it points to the benefit that they may glean from reading the advertisements and concludes that that benefit is substantial enough to satisfy the statutory test for tax exemption. The Court of Appeals took the same approach. It concluded that the advertisements performed various "essential" functions for physicians, 743 F. 2d, at 1576, and found a substantial relation based entirely upon the medically-related content of the advertisements as a group.

The Government, on the other hand, looks to the conduct of the tax-exempt organization itself, inquiring whether the publishers of Annals have performed the advertising services in a manner that evinces an intention to use the advertisements for the purpose of contributing to the educational value of the journal. Also approaching the question from the vantage point of the College, the Claims Court emphasized the lack of a comprehensive presentation of the material contained in the advertisements. It commented upon the "hit-or-miss nature of the advertising," 3 Cl. Ct., at 543, n. 3. and observed that the "differences between ads plainly reflected the advertiser's marketing strategy rather than their probable importance to the reader." *Id.,* at 534. "[A]ny educational function [the advertising] may have served was incidental to its purpose of raising revenue." *Id.,* at 535a.

We believe that the Claims Court was correct to concentrate its scrutiny upon the conduct of the College rather than upon the educational quality of the advertisements. For all advertisements contain some information, and if a modicum of informative content were enough to supply the important contribution necessary to achieve tax exemption for commercial advertising, it would be the rare advertisement indeed that would fail to meet the test. Yet the statutory and regulatory scheme, even if not creating a *per se* rule *against* tax exemption, is clearly antagonistic to the concept of a *per se* rule *for* exemption for advertising revenue. Moreover, the statute provides that a tax will be imposed on "any trade or business the *conduct* of which is not substantially related," 26 U.S.C. §513(a), directing our focus to the manner in which the tax-exempt organization operates its business. The implication of the statute is confirmed by the regulations, which emphasize the "manner" of designing and selecting the advertisements. See Treas. Reg. §1.513-1(d)(4)(iv), Example 7, 26 CFR §1.513-1(d)(4)(iv), Example 7 (1985). Thus, the Claims Court properly directed its attention to the College's conduct of its advertising business, and it found the following pertinent facts:

> "The evidence is clear that plaintiff did not use the advertising to provide its readers a comprehensive or systematic presentation of any aspect of the goods or services publicized. Those companies willing to pay for advertising space got it; others did not. Moreover, some of the advertising was for established drugs or devices and was repeated from one month to another, undermining the suggestion that the advertising was principally designed to alert readers of recent developments [citing, as examples, ads for Valium, Insulin and Maalox]. Some ads even concerned matters that had no conceivable relationship to the College's tax-exempt purposes." 3 Cl. Ct., at 534 (footnotes omitted).

These facts find adequate support in the record. See, *e.g.,* App. 29a-30a, 59a. Considering them in light of the applicable legal standard, we are bound to conclude that the advertising in Annals does not contribute importantly to the journal's educational purposes. This is not to say that the College could not control its publication of advertisements in such a way as to reflect an intention to contribute importantly to its educational functions. By coordinating the content of the advertisements with the editorial content of the issue, or by publishing only advertisements reflecting new developments in the pharmaceutical market, for example, perhaps the College could satisfy the stringent standards erected by Congress and the Treasury. In this case, however, we have concluded that the Court of Appeals erroneously focused exclusively upon the information that is invariably conveyed by commercial advertising, and consequently failed to give effect to the governing statute and regulations. Its judgment, accordingly, is

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[4] Indeed, different excerpts suggest that perhaps the House Committee did not construe the statute as creating a *per se* rule. It its explanation of §513(c), the House Report states that "the advertising contained in a publication of an exempt organization *may* be subject to the tax under section 511 even though the editorial content of the publication may be related to the exempt purposes of the organization." H. R. Rep. No. 91-413, pt. 2, 28 p. 26 (1969) (emphasis added).

[5] This conclusion is consistent with the Treasury's own approach to analogous problems. See, *e.g.,* Rev. Rul. 82-139, 1982-2 Cum. Bull. 108 (advertisements in county bar journal; no *per se* rule); Rev. Rul. 72-431, 1972-2 Cum. Bull. 281 (exempt organization's sale of mailing lists to commercial advertisers; no *per se* rule). Our rejection of the *per se* rule renders it unnecessary for us to address respondent's alternative argument that any such rule should apply only to associations organized under §501(c)(6) of the Internal Revenue Code.

Reversed.

Section 911.—Citizens or Residents of the United States Living Abroad

26 CFR 1.911–1: Partial exclusion for earned income from sources within a foreign country and foreign housing costs.

Foreign residency requirements waived for individuals residing in certain countries during specified time periods. See Rev. Proc. 86–39, page 11.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 280G, 467, 468, 483, 7872.)

Rev. Rul. 86–128

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of November 1986 are as follows:

	Period for Compounding			
	Annual	Semiannual	Quarterly	Monthly
Short-Term				
AFR	6.16%	6.07%	6.02%	5.99%
110% AFR	6.79%	6.68%	6.63%	6.59%
120% AFR	7.41%	7.28%	7.21%	7.17%
Mid-Term				
AFR	7.23%	7.10%	7.04%	7.00%
110% AFR	7.96%	7.81%	7.74%	7.69%
120% AFR	8.70%	8.52%	8.43%	8.37%
Long-Term				
AFR	7.71%	7.57%	7.50%	7.45%
110% AFR	8.50%	8.33%	8.25%	8.19%
120% AFR	9.29%	9.08%	8.98%	8.91%

Section 1441.—Withholding of Tax on Nonresident Aliens

26 CFR 1.1441–1: Requirement for withholding of tax on nonresident aliens, foreign partnerships, and foreign corporations.

Requirements and conditions under which Forms 1042S withholding information returns may be filed on magnetic tape. See Rev. Proc. 86–40, page 11.

Section 1442.—Withholding of Tax on Foreign Corporations

26 CFR 1.1442–1: Withholding of tax on foreign corporations.

Requirements and conditions under which Forms 1042S withholding information returns may be filed on magnetic tape. See Rev. Proc. 86–40, page 11.

Section 1443.—Foreign Tax-Exempt Organizations

26 CFR 1.1443–1: Foreign tax-exempt organizations.

Requirements and conditions under which Forms 1042S withholding information returns may be filed on magnetic tape. See Rev. Proc. 86–40, page 11.

Section 1461.—Liability for Withheld Tax

26 CFR 1.1461–2: Return of tax withheld.

Requirements and conditions under which Forms 1042S withholding information returns may be filed on magnetic tape. See Rev. Proc. 86–40, page 11.

Section 1462.—Withheld Tax as Credit to Recipient of Income

26 CFR 1.1462–1: Withheld tax as credit to recipient of income.

Requirements and conditions under which Forms 1042S withholding information returns may be filed on magnetic tape. See Rev. Proc. 86–40, page 11.

Section 1463.—Tax Paid by Recipient of Income

26 CFR 1.1463–1: Tax paid by recipient on income.

Requirements and conditions under which Forms 1042S withholding information returns may be filed on magnetic tape. See Rev. Proc. 86–40, page 11.

Section 1464.—Refunds and Credits with Respect to Withheld Tax

26 CFR 1.1464–1: Refunds or credits.

Requirements and conditions under which Forms 1042S withholding information returns may be filed on magnetic tape. See Rev. Proc. 86–40, page 11.

Section 6011.—General Requirement of Return, Statement or List

26 CFR 1.6011–1: General requirement of return, statement or list.

Requirements and conditions under which Forms 1042S withholding information returns may be filed on magnetic tape. See Rev. Proc. 86–40, page 11.

Section 7872.—Treatment of Loans with Below-market Interest Rates

Federal short-term, mid-term, and long-term rates are set forth for the month of November 1986. See Rev. Rul. 86–128, this page.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.105: Examination of returns and claims for refund, credit, or abatement; determination of correct tax liability.
(Also Part I Section 911; 1.911–1.)

Rev. Proc. 86–39

SECTION 1. PURPOSE

.01 This revenue procedure provides information to individuals who fail to meet the foreign residency requirements of section 911(d)(1) of the Internal Revenue Code for eligibility for the exclusion from gross income under section 911(a) of the foreign earned income and housing cost amounts because adverse conditions in a foreign country precluded the individual from meeting the foreign residency requirements of section 911(d)(1).

.02 Rev. Proc. 81–23, 1981–1 C.B. 693, lists countries in which the foreign residency requirements of section 911(d)(1) of the Code are waived under section 911(d)(4) because of adverse conditions present in those countries during the time periods indicated. This revenue procedure updates that list by relisting countries where the periods of adverse conditions are still in effect, by adding countries where periods of adverse conditions occurred after the publication of the list, and by removing countries where the period of adverse conditions ended prior to the publication of Rev. Proc. 81–23.

SEC. 2. BACKGROUND

.01 Section 911(a) of the Code allows foreign earned income and housing cost amounts to be excluded from the gross income of a "qualified individual" as defined in section 911(d)(1).

.02 Section 911(d)(1) of the Code defines the term "qualified individual" to mean an individual whose tax home is in a foreign country and who is (A) a citizen of the United States and establishes to the satisfaction of the Secretary that the individual has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, or (B) a citizen or resident of the United States and who, during any period of 12 consecutive months, is present in a foreign country or countries during at least 330 full days in such period.

.03 Section 911(d)(4) of the Code provides an exception to the residency requirements of section 911(d)(1). An individual who for any period is a bona fide resident of, or is present in, a foreign country, and who leaves that foreign country after August 31, 1978, will be treated as a qualified individual with respect to the period such individual was a bona fide resident of, or was present in, the foreign country if during such period the Secretary, after consultation with the Secretary of State, determines that individuals were required to leave the foreign country because of war, civil unrest, or similar adverse conditions in that foreign country which precluded the normal conduct of business by such individuals. An individual must establish that but for those conditions he or she could reasonably have been expected to meet the residency requirements.

.04 The following list of countries and time periods qualify for the exception to the residency requirements of section 911(d)(1) of the Code. An individual who left one of the following countries during the specified period shall be treated as a qualified individual, for purposes of section 911, with respect to the period during which that individual was a bona fide resident of, or present in, that foreign country, if such individual establishes that he or she could reasonably have been expected to meet the requirements of section 911(d) but for those conditions.

Country	*On or After*	*On or before*
Afghanistan	April 23, 1979	(still in effect)
Argentina	April 4, 1982	July 3, 1982
Bolivia	May 3, 1980	July 17, 1980
Chad	November 19, 1978	August 19, 1983
Colombia	November 13, 1984	(still in effect)
El Salvador	September 24, 1979	(still in effect)
Grenada	October 19, 1983	December 31, 1983
Iran	September 1, 1978	(still in effect)
Iraq	August 31, 1979	(still in effect)
Kuwait	September 13, 1983	June 13, 1984
Lebanon	August 31, 1979	(still in effect)
Libya	August 31, 1979	(still in effect)
Sudan	October 17, 1985	(still in effect)
Uganda	July 29, 1985	April 7, 1986

SEC. 3. INQUIRIES

If a taxpayer needs assistance on how to claim this exclusion, or on how to file an amended return, if applicable, the taxpayer should contact his or her local IRS Office or, for a taxpayer residing or traveling outside the United States, the nearest overseas IRS office.

SEC. 4. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 81–23 is updated.

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26 CFR 601.602: Tax forms and instructions.
(Also Part I, Sections 1441, 1442, 1443, 1461, 1462, 1463, 1464, 6011; 1.1441–1, 1.1442–1, 1.1443–1, 1.1461–2, 1.1462–1, 1.1463–1, 1.1464–1, 1.6011–1.)

Rev. Proc. 86–40

PART A—GENERAL

SECTION 1. PURPOSE AND NATURE OF CHANGES

The purpose of this Revenue Procedure is to update and supersede Rev. Proc. 85–53, 1985–2 C.B. 721, that sets forth the requirements and conditions under which withholding agents, as defined in Section 2.01 below, may file Form 1042S, Foreign Person's U.S. Source Income Subject to Withholding, on magnetic tape.

For Tax Year 1986 the following changes have been included in this revenue procedure:

.01 Part A, Section 2 has been revised to address requirements to report on magnetic tape when 500 or more forms are to be filed, and address requests for waiver of the magnetic tape filing requirement as a result of undue hardship.

.02 Part A, Section 3.05 has been inserted to address consolidation of withholding agent data.

.03 Part A, Section 5.03 has been inserted to address procedures for correcting magnetic tape files.

.04 Part A, Section 7, a new paragraph .06 has been inserted to clarify situations under which more than one record for a recipient is to be submitted.

.05 Part A, Section 8 has been deleted since the information has now been incorporated into the revised Part A, Section 2.

.06 Part B, Section 4, State Code Table. State Code "TT" has been added for the Mariana Islands. This new code value will apply to all state code references: Part B, Section 4, element 8 of the Transmitter "T" record; Part B, Section 5, element 6 of the Recipient "Q" record; Part B, Section 5, element 19 of the Recipient "Q" record; Part B, Section 6, element 7 of the Withholding Agent "W" record.

.07 Part B, Section 5, Country Code (element 11 of the Recipient "Q" record). One new country code has been added:

Country	*Country Code*
Aruba	AA

For Aruba, the Netherlands Antilles tax treaty rates will apply.

.08 Part B, Section 5, Income Code (element 21 of the Recipient "Q" record). Income Code 20 ("Other Income") has been reassigned a new code number of "50" and a new income category has been added as Income Code 20:

Income Code	*Meaning*
20	Earnings as an Artist or Athlete
50	Other Income (non-personal service compensations)

Note that if Compensations covered under Income Codes 16–19 are directly attributable to the recipient's occupation as an artist or athlete, Income Code 20 should be used.

The Meaning of Income Code "14" has been expanded to read "Pensions, annuities, alimony, and/or insurance premiums".

.09 Part B, Section 5, Recipient Type (element 22 of the Recipient "Q" record). A new recipient type code has been added and two other codes have been reassigned new numbers. "Other" recipient type has changed its code value from "09" to "19". "Unknown" recipient type has its code value changed from "10" to "20". Recipient Type "09" represents an "Artist or Athlete". Note that wherever appropriate, recipient type "09" should be used instead of recipient type "01" (Individual), '02' (Corporation), or "03" (Partnership).

.10 Part B, Section 5, Tax Rate (element 26 of the Recipient "Q" record). Tax Rate "08" has been added as a valid rate.

The tax treaty rates have changed on certain types of income for Canada, United Kingdom, and Italy.

Additionally, Barbados and Cyprus now are tax treaty countries.

.11 Effective January 1, 1987, the National Computer Center (NCC) will assume the responsibility for processing Forms 1042S on magnetic tape. Forms 1042S on MAGNETIC TAPE should no longer be sent to Philadelphia Service Center. Forms 1042 and any PAPER document Forms 1042S should continue to be filed at the Philadelphia Service Center.

SEC. 2. APPLICATION FOR TAPE REPORTING AND REQUESTS FOR UNDUE HARDSHIP WAIVERS

.01 A withholding agent is defined as any person or entity, U.S. or foreign, required to withhold U.S. tax on payments of income subject to withholding from sources within the United States as provided for in Chapter 3 of the Internal Revenue Code. A withholding agent may be an individual, partnership, corporation, trust, estate, government agency (Federal, State or local), association, or a tax-exempt foundation or organization.

.02 Withholding agents must use magnetic tape to file 500 or more Forms 1042S with the Internal Revenue Service (IRS) for calendar years beginning before January 1, 1987 (Tax Year 1986); 250 or more Forms 1042S for calendar year beginning on or after January 1, 1987 (Tax Year 1987 and subsequent years).

.03 Withholding agents or their agents are required to complete Form 4419, Application for Magnetic Media Reporting of Information Returns. Applications should be filed with the National Computer Center (NCC) 90 days before the due date of the return. The NCC will act on an application and notify the applicant in writing within 30 days of receipt of the application. Magnetic tape returns may not be filed with IRS until the application has been approved.

.04 Generally withholding agents using equipment compatible with IRS's equipment can presume that their application will be approved. Compatible tape characteristics are shown in PART "B", Section 1.01. Where the capability to prepare several types of tapes exists, IRS prefers that compatible tapes be prepared.

.05 If withholding agents propose to submit convertible tapes, IRS will attempt to find conversion facilities. Generally, an application to file on magnetic tape will be disapproved only when IRS is unable to obtain facilities to convert a withholding agent's file to a compatible form.

.06 IRS will assist new filers with their initial magnetic tape submission by reviewing "test" files submitted in advance of the filing season. Approved withholding agents or their agents should submit "test" files to the Magnetic Media Specialist at the National Computer Center. As a guideline, IRS prefers that all Form 1042S "test" files be submitted between January 1 and February 15. Clearly mark the tape as "TEST DATA", and include identification information such as name, address, and telephone number of someone familiar with the "test" tape who may be contacted to discuss its acceptability.

.07 Withholding agents required to file Forms 1042S on magnetic tape may receive a waiver from such requirements in appropriate circumstances upon showing a hardship. Requests for a waiver generally must be filed at least 90 days before the filing of the first return for which the waiver is requested. Withholding agents may not apply for a waiver for more than one year at a time. The waiver request must be a written statement containing the following identifying information:

(a) The withholding agent's name;

(b) The withholding agent's address;

(c) The withholding agent's Employer Identification Number (EIN);

(d) The date to which the waiver is requested;

(e) The name and telephone number of a person to contact regarding the information contained in the waiver;

(f) A statement regarding the cost which is causing the undue hardship condition; and

(g) A statement explaining any other reasonable attempts the withholding agent has made to comply with this magnetic media filing requirement.

Magnetic tape is the only permissible magnetic media for filing Forms 1042S and shall be filed in accordance with the applicable revenue procedures. Diskette and cassette reporting of Forms 1042S can not be accepted at this time. Withholding agents should also be aware of current revenue procedures relating to magnetic tape, diskette, and cassette reporting for wage and other information documents. Copies of these other revenue procedures, as well as all requests for filing Forms 1042S on magnetic tape (Form 4419), applicable revenue procedures, waiver requests (pertaining to magnetic media filing only), and any other questions you may have regarding Forms 1042S should be directed to:

Magnetic Media Reporting
Internal Revenue Service
National Computer Center
P.O. Box 1359
Martinsburg, West Virginia
25401–1359

The National Computer Center may also be contacted by telephone at (304)263–8700. The hours of operation for telephone contact are between 8:30 a.m. and 8:00 p.m., Eastern time.

The address for filing Forms 1042 or for filing any PAPER document Forms 1042S will be:

Internal Revenue Service
Philadelphia Service Center
Philadelphia, Pennsylvania 19255

SEC. 3. FILING OF TAPE REPORTS

.01 Packaging, shipping, and mailing instructions will be provided in the authorizing letter issued by IRS in response to an application for tape reporting.

.02 Withholding agents submitting a portion of their statements on magnetic tape and the remainder on paper forms, should file magnetic tape records at the National Computer Center and paper documents at the Philadelphia Service Center, in separate shipments (see Part A, Section 2.07, for addresses).

.03 The withholding agent's Form 1042 tax return is used to verify the number of Forms 1042S filed on paper and/or magnetic tape. For transmitters of Service Bureaus filing Form 1042S information on tape for several withholding agents, separate Forms 1042 must be filed by each withholding agent included in the transmittal. Since the required Form 1042 is a tax return (with or without a remittance attached), it must be filed separately from the shipment of magnetic tape. Any additional paper documents required to be submitted should accompany Form 1042. (See instructions for Form 1042, Annual Withholding Tax Return for U.S. Source Income of Foreign Persons.)

.04 Magnetic tape reporting to IRS for Forms 1042S must be on a calendar year basis. The dates prescribed for filing paper documents with IRS will also apply to magnetic tape filing. Files must be submitted to the National Computer Center by March 15. Copies of the Form 1042S information must be furnished to the income recipient by January 31. Requests for extensions of time for filing on magnetic media and related matters should be made to the National Computer Center (requests for extension of time for filing Forms 1042 and/or Forms 1042S on paper should be made to the Director, Philadelphia Service Center). If an extension has been granted by IRS, a copy of the letter granting the extension must be attached to the transmittal Form 4804 when the file is submitted.

.05 Forms 1042S (Recipient "Q" records) from different branches of the withholding agent's business activity should be consolidated under one withholding agent's "W" record, especially when one common name and Employer Identification Number (EIN) would be used for each of the branches. For example, Bank X has branch offices in two different states. It would be acceptable for Branch Y of Bank X to report Recipient "Q" records and associated "W" record as "Bank X, Branch Y" when Branch Y has its own EIN, and for Branch Z of Bank X to report separately its Recipient "Q" records and associated "W" record as "Bank X, Branch Z" using its own EIN. Branches should not report separately when those branches are using a common EIN (and name). Branches filing separately should not use a common address (for example the address of the parent bank) when that common address is not normally used for filing other types of returns with IRS. It is assumed that for each "W" record (which represents a unique withholding agent), there will be a corresponding Form 1042 submitted which will reflect the accumulation of the associated Recipient "Q" records.

.06 Enclose a transmittal in duplicate, in the first box of the tape shipment, with the following information:

(a) The complete name, address, and EIN of the transmitter of the tape file.

(b) Name, address, title, and telephone number of the person to contact regarding any tape file problem.

(c) The complete name and address to be used in returning the tape file.

(d) The manufacturer and model of the main frame and tape drives, the tape width, the density in characters per inch, and the recording code (BCD, Excess 3, Octal, etc.).

(e) The type of document being reported—i.e. Form 1042S.

(f) Total number of tape reels in the file.

.07 Standard mail shipments should be addressed to:

Magnetic Media Reporting
Internal Revenue Service
National Computer Center
P.O. Box 1359
Martinsburg, West Virginia
25401–1359

Shipments by land carriers (UPS, for example) should be addressed to:

Magnetic Media Reporting
Internal Revenue Service
Route 9
Needy Road
Martinsburg, West Virginia 25401

Note on the address side of the shipment:

"EXPEDITE FORM 1042S STATEMENTS ON MAGNETIC TAPE, DELIVER UNOPENED TO TAPE LIBRARY."

.08 The magnetic tape specifications contained in PART "B" of this revenue procedure must be strictly adhered to. Deviations will not be permitted under any circumstances. All magnetic tape filings will be scanned for completeness of required fields, mathematical verification, and proper format. Tapes failing to meet specifications will not be processed, but will be returned to the transmitter for correction (See also Part A, Section 5.03, below). Corrected files must be filed with the National Computer Center within 15 days from receipt of the returned file.

SEC. 4. PROCESSING OF TAPE STATEMENTS

.01 Normally, tapes will be returned to the transmitters by September 15 of the year in which submitted. However, if the tapes submitted are unprocessable, and must be returned for correction prior to processing, they will be returned within six months of the receipt of acceptable tapes. We suggest that the withholding agent retain the original tape until the expiration of the statute of limitations for assessment.

.02 IRS will prepare the appropriate statements for transmittal to treaty countries.

SEC. 5. CORRECTED STATEMENTS

.01 The appropriate paper forms will normally be used if it is necessary to correct Recipient "Q" records in the magnetic tape files. Since corrected statements supersede information previously supplied, all required data fields must be completed. Annotate each form "Corrected" at the top. Corrected documents should be bundled separately from other paper documents. When corrected documents are shipped separately, an amended Form 1042 must be filed, also suitably annotated.

.02 If the withholding agent discovers that a large volume of records submitted have to be corrected, the NCC magnetic tape coordinator should be contacted. He/She should ask that the original tape be returned so that the corrections can be made to it. If the NCC has already processed the tape, paper documents must be prepared for the ones needing corrections.

.03 When magnetic tape files are returned to the transmitter for data correction, a listing of the type of errors and frequency of such errors will be provided. The transmitter should correct the problems and submit a replacement tape file to the magnetic tape coordinator. Certain problems noted may not require any corrective action. For example, certain recipient "Q" records should have had their tax withheld at a particular tax rate, but the withholding agent, for whatever reason, withheld at a different tax rate. The transmitter (in conjunction with the withholding agent if necessary) should first verify that the tax rates in question are in fact the rates at which tax was withheld. Once verified, a letter should accompany the tape file stipulating that the tax rates are accurate as submitted.

SEC. 6. EFFECT ON PAPER DOCUMENTS

.01 Magnetic tape reporting to IRS eliminates the need for submission of paper Forms 1042S. However, withholding agents must continue to provide recipients with requisite information, although this need not be on a copy of Form 1042S.

.02 If only a portion of the statements are reported on magnetic tape and the remainder are reported on paper forms, those paper statements must be filed on the prescribed forms.

SEC. 7. DATA ENTRIES

.01 Since taxpayer identifying numbers are not required on all Forms 1042S (see specific Instructions for Withholding Agents, Copy C of the official Form 1042S), the specifications in PART "B" of this revenue procedure permit omission of such identifying numbers. Although identifying numbers are not always required for nonresident alien income recipients, IRS appreciates their being furnished when available.

.02 Recipient surnames are used to computer-generate Sort Names. Use an asterisk to indicate the beginning of the surname for this purpose. If the surname is the first name on the line, as may be the case for nationals of Asian countries, the asterisk is to be omitted. In the case of a partnership or joint ownership, or some other case where more than one individual is listed, asterisk only the first surname. A blank will always precede the asterisk when it is used, but no asterisk may be followed by a blank. Do not use an asterisk with corporate or any other business entity or governmental organization name, except partnerships or sole proprietorships. Never have more than one blank separating portions of a name line or an address field.

.03 In case of multiple recipients, the name of the person whose identifying number has been provided should be placed before all other names.

.04 Sometimes the recipient identification recorded on the withholding agent's records is lengthy, and exceeds the 105 characters allotted in the Recipient Name Line and Supplemental Name Lines on the magnetic tape records. This is most common in the case of trusts or other types of fiduciary accounts. The first 105 characters of the recipient identification normally provide sufficient descriptive data for IRS's purposes. IRS encourages all agents to truncate or abbreviate lengthy recipient descriptions.

.05 All monetary amount fields must show dollars and cents (omit the decimal point). For example, $135.72 must be shown as 13572, and $100 must be shown as 10000. All money amount fields are positive and must not be signed in any fashion. All money amounts must be right-justified and zero filled. Do not truncate any money amount fields. If the amount is more than the allowed space, prepare a second "Q" record to show the difference.

.06 There are several circumstances where more than one "Q" record is expected for a recipient. These situations include:

1) Different sources of income. For example, Recipient X derived income from Capital Gains (Income Code 09) and Industrial Royalties (Income Code 10). One "Q" record must be provided listing Income Code "09", and the Gross Income Paid and Tax Withheld pertaining solely to that type of income. A separate "Q" record must document the Income Code "10" information.

2) Change in Country Code during the year. for example, on July 1, the withholding agent received notification via Form 1001 that the recipient changed his official country for which tax treaty benefits apply from country X to country Y. One "Q" record must be provided reflecting Gross Income Paid, Tax Rate, and Tax Withheld for country X (reflecting income and withholding from January 1 through June 30). A second "Q" record must be provided reflecting Income, Tax Rate, and Tax Withheld for country Y (covering income and withholding from July 1 through December 31).

3) Change in a country's tax treaty rate during the year. For example, effective April 1, country X changed its tax treaty rate for a particular type of income from 10% to 20%. One "Q" record must be provided reflecting Gross Income Paid and Tax Withheld at the 10% rate (covering January 1 through March 31). A second "Q" record must also be provided reflecting Gross Income Paid and Tax Withheld at the 20% rate (covering April 1 through December 31).

Note that these three situations are NOT mutually exclusive. Therefore, if a recipient has two sources of income, each of which is derived from a country whose corresponding tax treaty rates changed during the year, and the recipient submitted a Form 1001 to the Withholding Agent changing his country code for tax purposes, as many as six (6) separate "Q" records must be provided.

Part "B"—Magnetic Tape Specifications

SECTION 1. GENERAL

.01 These specifications prescribe the required format and content of the records to be included in the file, but not the methods or equipment to be used in their preparation. Usually, IRS will be able to process, without translation, any compatible tape file. To be compatible, a tape file must meet all of the following:

Type of Tape—1/2 inch Mylar base, oxide coated

Interrecord Gap—.75 inch for 556 or 800 bpi density 7-track,
.6 inch for 800 bpi density 9-track,
.6 inch for 1600 bpi density,
.3 inch for 6250 bpi density 9-track

(a) When the Recording Mode is EBCDIC (Extended Binary Coded Decimal Interchange Code):

(1) Parity—Odd Parity

(2) Recording Density—800, 1600, or 6250 Densities

(3) 9 Channel

(b) When the Recording Mode is ASCII (American Standard Coded Information Interchange):

(1) Parity—Odd Parity

(2) Recording Density—800, 1600, or 6250 Densities

(3) 9 Channel

(c) When the Recording Mode is BCD (Binary Coded Decimal):

(1) Parity—Odd or Even Parity

(2) Recording Density—556 or 800 Densities

(3) 7 Channel or 9 Channel

.02 An acceptable tape file for each withholding agent will contain data records as follows:

(a) Single reel:

(1) a Transmitter "T" record; then

(2) one or more Recipient "Q" records followed by a specific Withholding Agent "W" record; then

(3) additional "Q" and "W" record sequences for other withholding agents as needed; then

(4) an End of Transmission "Y" record.

(b) Multiple Reels:

(1) a Transmitter "T" record at the beginning of each reel; then

(2) sequences of Recipient "Q" records followed with corresponding Withholding Agent "W" records; then

(3) an End of Reel "Z" record on every reel except that last; and

(4) an End of Transmission "Y" record ending the last reel.

(c) Notes:

(1) a sequence of Recipient "Q" records may be continued from one reel to the next if they apply to the same withholding agent, without the necessity of repeating the "W" record. The sequence might be, for example, QQQQZ (end of one reel); TQQQQW (beginning of next reel).

(2) the End of Reel "Z" record is identical to the Withholding Agent "W" record, except that it indicates the end of the reel, but not necessarily the end of a withholding agent's "Q" records. For example, when end of reel will be reached before the end of an agent's "Q" records, the "Z" record will be used in lieu of a "W" record. The next tape reel will begin with a "T" record, followed by the remaining "Q" records for the withholding agent.

.03 Affix an external label to each tape with the following information:

(1) Name of Transmitter.

(2) Number of "Q" records on that reel.

(3) Density (556, 800, 1600 CPI, etc.).

(4) Channel (7 or 9).

(5) Recording Mode (EBCDIC, ASCII, etc.).

(6) Parity (odd or even).

(7) Manufacturer and model of mainframe and tape drives

(8) Sequence number of reel, and total reels in the file (i.e. 1 of 3, 2 of 4, etc.).

.04 All records, including Header and Trailer Labels (if used) must be transmitted at the same density.

SEC. 2. CONVENTIONS AND DEFINITIONS

.01 Header Labels, Trailer Labels, Record Marks and Tape Marks are all optional. They may be used as required by the transmitter's equipment or programming. If used, they must conform to the following standards:

(a) Header Labels must begin VOL1, VOL2, HDR1, HDR2, or 1HDR. If used, they must be first record(s) on the reel immediately before the Transmitter "T" record. Header labels may not exceed 80 characters in length.

(b) Trailer Labels must begin 1EOR, 1EOF, EOF1, or EOR1. If used, they must be the last record(s) on the reel, after the "Z" or "Y" record and Tape Mark (if a Tape Mark is used). Trailer Labels may not exceed 80 characters in length.

(c) Record Marks, if used, may only follow the data portion of a record or block. All records are of uniform length, and record marks are not needed.

(d) Tape Marks, if used, must be IBM 001111 (Octal 17) in even parity. They always appear immediately after the "Z" or "Y" record. If Header and Trailer Labels are also used, the tape mark must follow the Header Label and must precede and/or follow the Trailer Label(s).

.02 Definitions:

Element	Description
b	Denotes a blank position. For compatibility with IRS equipment, if using BCD recording mode, use BCD bit configuration 010000 ("A" bit only) in even parity, 001101 ("841" bits) in odd parity.
Special Character	Any character that is not a numeral, a letter, or a blank.
Withholding Agent	Person or organization responsible for paying income and withholding taxes. The withholding agent is responsible for the completeness, accuracy, and timely submission of magnetic tape files.
Payer	Person or organization who is the originator of income and enters into a contractual agreement with the withholding agent for the purpose of disbursing income for the payer. For example, Corporation X is about to declare a dividend. Corporation X contracts Bank Y to calculate and distribute such dividends to recipients, and be responsible for withholding. Corporation X is considered the Payer and Bank Y is considered the Withholding Agent.
Transmitter	Person or organization preparing and filing tape files. May be the withholding agent or his agent.
Recipient	Person(s) or organization(s) receiving payments from a withholding agent.

Element	Description
Record	A group of related fields of information treated as a unit.
Blocked Records	Two or more records grouped together between interrecord gaps.
File	For the purpose of this Procedure, a file consists of all tape records submitted by a transmitter.
Reel	A spool of magnetic tape.
EIN	Employer Identification Number that has been assigned by the Service to the particular entity.
SSN	Social Security Number.

SEC. 3. RECORD LENGTH AND BLOCKING

.01 Tape records prescribed in the specifications may be blocked or unblocked, subject to the following:

(a) All data records are of a fixed length (450 positions).

(b) All records may be blocked, except Header and Trailer Labels.

(c) A block may not exceed 15,000 characters, although shorter blocks may be written as desired. If records are being blocked, but sufficient records are not available to fill a complete block, the block may either be "padded" with 9's to fill all unused positions or truncated after the last data record ("short block"). Do not pad the block with blanks, or create blank records (for example, Q followed by 449 blanks, etc.).

(d) Two forms of blocking are acceptable:

(1) Only "Q" Records are blocked; all other records are unblocked.

(2) All records, except Header and Trailer Labels, if used, are blocked. In this case, a "T" Record may only be the first record in the first block on the reel (first reel only); a "W" Record must follow all associated "Q" Records; and, "Y" or "Z" Records may only be the last record in the last block on the reel (only block padding (all 9's) could follow).

.02 The first position of each record indicates the record type:

Transmitter	T
Recipient	Q
Withholding Agent	W
End of Reel	Z
End of Transmission	Y

.03 The minimum file transmitted must consist of a Transmitter "T" record, a Recipient "Q" Record, a Withholding Agent "W" Record, and an End of Transmission "Y" Record.

SEC. 4. THE TRANSMITTER "T" RECORD

This record identifies the entity who prepares and transmits the magnetic tape file. The Transmitter and one of the withholding agents may be the same, but they need not be. The Transmitter "T" Record must be the first data record on a reel (preceded only by header labels, if any), and must appear on each reel in the file sent by the Transmitter. On multiple reel files the reel number must be incremented by 1 (one) for each tape reel after the first reel. Each "T" Record has a fixed length of 450 positions. The elements of data prescribed for each "T" Record are as follows:

Element	Positions	Title	Description
1	1	Record Type	Enter letter "T"
2	2 & 3	Tax Year	Enter the last two digits of the year for which income and withholding is being reported. All recipient "Q" and transmitter "T" Records on the file for every withholding agent *must* report payments for this year, and this year *only*. Transmit separate Forms 1042 and tape files for different tax years.
3	4 & 5	Reel Number	The two-digit serial number assigned by the Transmitter to this reel, starting with 01. If Header Labels are used, this should be the same as the Reel Sequence Number.
4	6–14	EIN	Enter the Employer Identification Number of the *Transmitter*. Omit hyphen.
5	15–54	Transmitter Name	Enter name of submitter of file; left justify and blank fill. Abbreviate if necessary to fit 40-character limit. Omit punctuation marks except hyphens and ampersands.
6	55–94	Street Address	Enter Street Address, PO Box, or other location of Transmitter. Left justify and blank fill. Abbreviate as needed to fit 40-character limit.
7	95–114	City	Enter City, Town, APO/FPO, etc. of Transmitter. Left justify and blank fill. Abbreviate to fit 20-character limit.
8	115 & 116	State Code	Enter two-letter PO Code as shown in the list below *only*. Do not spell out any state name.

State	Code	State	Code	State	Code
Alabama	AL	Maine	ME	Pennsylvania	PA
Alaska	AK	Maryland	MD	Rhode Island	RI
Arizona	AZ	Massachusetts	MA	South Carolina	SC
Arkansas	AR	Michigan	MI	South Dakota	SD
California	CA	Minnesota	MN	Tennessee	TN
Colorado	CO	Mississippi	MS	Texas	TX
Connecticut	CT	Missouri	MO	Utah	UT
Delaware	DE	Montana	MT	Vermont	VT
District of Columbia	DC	Nebraska	NE	Virginia	VA
Florida	FL	Nevada	NV	Washington	WA
Georgia	GA	New Hampshire	NH	West Virginia	WV
Hawaii	HI	New Jersey	NJ	Wisconsin	WI
Idaho	ID	New Mexico	NM	Wyoming	WY
Illinois	IL	New York	NY	American Samoa	AS
Indiana	IN	North Carolina	NC	Canada	CD
Iowa	IA	North Dakota	ND	Guam	GU
Kansas	KS	Ohio	OH	Mariana Islands	TT
Kentucky	KY	Oklahoma	OK	Puerto Rico	PR
Louisiana	LA	Oregon	OR	Virgin Islands	VI

Notes:

(1) For other Foreign countries use XX

(2) APO & FPO addresses *must* show a city, state, and Zip. Do *not* use "X" for APO & FPO; the four permissible State codes are "NY", "CA", "WA", and "FL".

Element	Positions	Title	Description
9	117–125	ZIP Code	Enter the Zip Code of the Transmitter for all U.S., U.S. Territory or Possession, APO/FPO addresses. For Transmitters using a 5 digit zip code, enter the zip code in the leftmost 5 positions and zero fill the remaining 4 positions. For Transmitters outside the U.S. enter nine zeros only. DO NOT blank fill.
10	126–450	Blanks	Blank fill the rest of the "T" Record.

SEC. 5. RECIPIENT "Q" RECORD

This Record contains complete name and address data for both Withholding Agent and Recipient of Income, together with all the particulars of the income paid and tax withheld. Complete Withholding Agent data is required because each Recipient "Q" Record is treated as if it were a separate Form 1042S, and is processed independently of other records. Since the "Q" Record is restricted to one type of income only, it may be necessary to write more than one "Q" Record for any given individual income recipient, who may have received income of more than one type (see Part A, Section 7.06). All recipient "Q" Records for a particular Withholding Agent must be written before the corresponding Withholding Agent "W" Record, and before "Q" Records for another Withholding Agent may be used (for example, they may be sorted alphabetically by surname, or by country code, or by country of the mailing address, etc.) at the convenience of the Transmitter or Withholding Agent, since the "Q" Records are fully independent. All "Q" Records have a fixed length of 450 positions. All Elements are required unless otherwise stated.

Element	Positions	Title	Description
1	1	Record Type	Enter Q only.
2	2–10	Agent EIN	Enter the 9-digit Employer Identification Number of the Withholding Agent. Omit the hyphen.
3	11–45	Agent Name	Enter the name of the Withholding Agent up to the limit of 35 characters. Abbreviate as needed, omitting punctuation. Left justify and blank fill.
4	46–80	Agent Address	Enter Street address, PO Box, or other location of the Agent to a limit of 35 characters. Abbreviate as needed, omitting punctuation. Left justify and blank fill.
5	81–100	City	Enter the city or town (or other locality name) up to the limit of 20 characters. Left justify and blank fill.

Element	Positions	Title	Description
6	101 & 102	State Code	Enter the two-character alphabetic code in the list in Sec. 4., above. *DO NOT* use CD (Canada), MX (Mexico), or XX (Other foreign country). If the state is not a U.S. state, blank fill this field and use the Country Code field (Element 11) to identify the foreign address. Do not spell out any state name.
7	103–111	Zip Code	Enter 9 numeric characters for all U.S. addresses (including territories, possessions, and APO/FPO). If a 5 digit zip code is used, enter the zip code in the leftmost 5 positions and zero fill the remaining 4 positions. Zero fill for addresses outside the U.S.
8	112	Account Type Code	Enter "1" for U.S. business or organization; Element 9 must have an EIN. Enter "2" for U.S. citizen or resident alien; Element 9 must have SSN. Enter "3" for nonresident alien persons, businesses, or organizations. Element 9 should contain an EIN or SSN if one is available. Enter "4" if "1" or "2" applies, but an SSN or EIN is not available for a legitimate reason; for example, a number has been applied for but not received.
9	113–121	TIN	Enter the recipient's U.S. identification number; if Element 8 has a "1" you must enter an EIN; if Element 8 has a "2" you must enter an SSN; if Element 8 has a "3", enter an EIN or SSN if available—otherwise enter blanks; if Element 8 has a "4" you must enter blanks.
10	122–136	Agent's ID Number	Enter the account number assigned by the Withholding agent for this recipient up to a maximum of 15 positions. This number is used to facilitate identification of the specific record if there is any correspondence. Left justify and blank fill. This Element will be all blank if account numbers are not assigned. This field may contain numeric or alphabetic characters, blanks, or hyphens.
11	137 & 138	Country Code	Enter two alphabetic characters from the list below which represents the official country for which Tax Treaty benefits are based. This may or may not be the same as the country given in Element 20, below. Entry of a true country code is mandatory. "OC" (country unknown or not identified) is to be used with great reluctance. THE TAPE FILE WILL BE RETURNED FOR CORRECTION IF A SUBSTANTIAL NUMBER OF "Q" RECORDS SHOW COUNTRY CODE "OC." WHENEVER COUNTRY CODE "OC" IS USED, THE RATE OF TAX WITHHELD MUST EQUAL 30%.

Country	Code
Afars & Issas DJ (now Djibouti)	DJ
Afghansitan	AF
Albania	AL
Algeria	AG
American Samoa	AQ
Andorra	AN
Angola	AO
Anguilla	AV
Antarctica	AY
Antigua & Barbuda	AC
Argentina	AR
Aruba	AA
Ashmore & Cartier Is.	AT
Australia	AS
Austria	AU
Azores	PO
Bahamas, The	BF
Bahrain	BA
Bangladesh	BG
Barbados	BB
Bassas da India	BS
Belgium	BE
Belize (formerly British Honduras)	BH
Benin (formerly Dahomey)	BN
Bermuda	BD
Bhutan	BT
Bolivia	BL
Botswana	BC
Bouvet Island	BV
Brazil	BR
British Honduras (now Belize)	BH
British Indian Ocean Territory	IO
British Virgin Islands	VI
Brunei	BX
Bulgaria	BU
Burkina (formerly Upper Volta)	UV

Country	Code	Country	Code	Country	Code
Burma	BM	German Democratic Republic (East Germany)	GC	Korea, Republic of (South Korea)	KS
Burundi	BY	Germany, Federal Republic of (West Germany)	GE	Kuwait	KU
Cambodia (formerly Kampuchea)	CB	Ghana	GH	Laos	LA
Cameroon	CM	Gibraltar	GI	Lebanon	LE
Canada	CA	Gilbert Islands (Kiribati)	KR	Lesotho	LT
Canary Islands	SP	Glorioso Islands	GO	Liberia	LI
Canton & Enderbury Islands (now Kiribati)	KR	Greece	GR	Libya	LY
Cape Verde	CV	Greenland	GL	Liechtenstein	LS
Cayman Islands	CJ	Grenada	GJ	Luxembourg	LU
Central African Republic	CT	Grenadine Islands (& St. Vincent)	VC	Macau	MC
Ceylon (now Sri Lanka)	CE	Guadeloupe	GP	Madagascar	MA
Chad	CD	Guam	GQ	Malawi	MI
Chile	CI	Guatemala	GT	Malaysia	MY
China, Peoples Republic (Mainland China)	CH	Guernsey	GK	Maldives	MV
China (Taiwan)	TW	Guinea	GV	Mali	ML
Christmas Island	KT	Guinea-Bissau	PU	Malta	MT
Clipperton Island	IP	Guyana	GY	Martinique	MB
Cocos (Keeling) Islands	CK	Haiti	HA	Mauritania	MR
Colombia	CO	Heard Island & McDonald Islands	HM	Mauritius	MP
Comoros	CN	Holland (Netherlands)	NL	Mayotte	MF
Congo	CF	Honduras	HO	Mexico	MX
Cook Islands	CW	Hong Kong	HK	Midway Islands	MQ
Coral Sea Islands Terr.	CR	Hungary	HU	Monaco	MN
Costa Rica	CS	Iceland	IC	Mongolia	MG
Cuba	CU	India	IN	Montserrat	MH
Cyprus	CY	Indonesia	ID	Morocco	MO
Czechoslovakia	CZ	Iran (formerly Persia)	IR	Mozambique	MZ
Denmark	DA	Iraq	IZ	Namibia (SW Africa)	WA
Djibouti (formerly Afars 7 Issas)	DJ	Iraq-Saudi Arabia Neutral Zone	IY	Nauru	NR
Dominica	DO	Ireland	EI	Navassa Island	BQ
Dominican Republic	DR	Isle of Man	IM	Nepal	NP
Ecuador	EC	Israel	IS	Netherlands (Holland)	NL
Egypt	EG	Italy	IT	Netherlands Antilles	NA
Ellice Islands (now Tuvalu)	TV	Ivory Coast	IV	New Caledonia	NC
El Salvador	ES	Jamaica	JM	New Hebrides (Vanuatu)	NH
England	UK	Jan Mayen	JN	New Zealand	NZ
Equatorial Guinea	EK	Japan	JA	Nicaragua	NU
Ethiopia	ET	Jersey	JE	Niger	NG
Europa Island	EU	Johnston Atoll	JQ	Nigeria	NI
Falkland Islands (also known as Islas Malvinas)	FA	Jordan	JO	Niue	NE
Faroe Islands	FO	Juan de Nova Island	JU	Norfolk Island	NF
Fiji	FJ	Kampuchea (now Cambodia)	CB	Northern Ireland	UK
Finland	FI	Kenya	KE	Northern Mariana Islands	CQ
France	FR	Kingman Reef	KQ	Norway	NO
French Guiana	FG	Kiribati (Canton & Enderbury & Gilbert Is.)	KR	Oman	MU
French Polynesia	FP	Korea, Democratic Peoples Republic of (North Korea)	KN	Pakistan	PK
French Southern & Antarctic Lands	FS			Palmyra Atoll	LQ
Gabon	GB			Panama (except Canal Zone)	PM
Gambia, The	GA			Papua-New Guinea	PP
Gaza Strip	GZ			Paracel Islands	PF
				Paraguay	PA
				Peru	PE
				Philippines	RP
				Pitcairn Islands	PC
				Poland	PL
				Portugal	PO

Country	Code	Country	Code	Country	Code
Portuguese Timor (Indonesia)	ID	South-West Africa (now Namibia)	WA	Uganda	UG
Puerto Rico	RQ	Spain	SP	Union of Soviet Socialist Republics	UR
Qatar	QA	Spratly Islands	PG	United Arab Emirates	TC
Reunion	RE	Sri Lanka (formerly Ceylon)	CE	United Kingdom	UK
Romania	RO	Sudan	SU	Upper Volta (now Burkina)	UV
Rwanda	RW	Suriname	NS	Uruguay	UY
St. Christopher-Nevis (also called St. Kitts)	SC	Svalbard	SV	Vanuatu (New Hebrides)	NH
St. Helena	SH	Swaziland	WZ	Vatican City	VT
St. Lucia	ST	Sweden	SW	Venezuela	VE
St. Pierre & Miquelon	SB	Switzerland	SZ	Vietnam	VM
St. Vincent & the Grenadines	VC	Syria	SY	Virgin Islands (US)	VQ
San Marino	SM	Taiwan	TW	Wake Island	WQ
Sao Tome and Principe	TP	Tanzania, United Republic of	TZ	Wales	UK
Saudi Arabia	SA	Thailand	TH	Wallis & Futuna	WF
Scotland	UK	Togo	TO	West Bank	WE
Senegal	SG	Tokelau	TL	Western Sahara	WI
Seychelles	SE	Tonga	TN	Western Samoa	WS
Sierra Leone	SL	Trinidad & Tobago	TD	Yemen (South) (Aden)	YS
Singapore	SN	Tromelin Island	TE	Yemen (North) (Sanaa)	YE
Solomon Islands	BP	Trust Territory of the Pacific Islands	NQ	Yugoslavia	YO
Somalia	SO	Tunisia	TS	Zaire	CG
South Africa	SF	Turkey	TU	Zambia	ZA
Southern Rhodesia (now Zimbabwe)	ZI	Turks & Caicos Islands	TK	Zimbabwe	ZI
		Tuvalu (Ellice Islands)	TV	(Other Countries)	OC

Element	Positions	Title	Description
12	139–173	1st Name Line	Enter full name of recipient, or if there are more than one, the name of the first recipient only. Use an asterisk to indicate the surname as shown in Part A, Section 7.02 above. Valid characters are alphabetic, numeric, ampersand (&), hyphen (-), slash (/), asterisk (*), or blank. Left justify and blank fill. A name MUST be entered here; if the recipient is a numbered bank account, and the true recipient is not known, the account number must be supplied here. It is NOT acceptable to have two or more consecutive blanks separating parts of a name. For example, "JOHNbbbbb*DOE" is unacceptable, whereas "JOHNb*DOE" is acceptable ("b" represents a blank position). THE TAPE FILE WILL BE RETURNED FOR CORRECTION IF A SUBSTANTIAL NUMBER OF "Q" RECORDS SHOW A BLANK 1st NAME LINE OR AN INVALID 1st NAME LINE.
13	174–208	2nd Name Line	Enter supplementary name information of the recipient on this line. Use this line for additional names (e.g. of partners or joint owners), for trade names, stage names, aliases. Use this line also for "care of", "via", or "through" information. Valid characters are alphabetic, numeric, Blank, ampersand (&), Hyphen (-), Slash (/), Pound Sign (#), and the percent(%). The percent (%) is valid in the first position only (as shorthand for "in care of"). Two or more consecutive, imbedded blanks between name parts is not acceptable. If no additional name data is to be provided, blanks are to be inserted. Left justify and blank fill.
14	209–243	3rd Name Line	Enter further name data if applicable; otherwise blank fill. Specifications are precisely as for the 2nd Name Line. See Street address, below.

NOTE: 105 total characters are available for name information. IRS encourages full identification of nonresident alien persons and organizations because data is furnished to their governments in accordance with tax treaties and exchange of information agreements.

Element	Positions	Title	Description
15	244–278	Street Address	Enter the recipient's full street address. Valid characters are alphabetic, numeric, blank, ampersand (&), Hyphen (-), Slash (/), and Pound Sign (#). Two or more consecutive, imbedded blanks between address parts are not acceptable. If the street, building, military installation or other name is too long for the 35-character allotment of this element, use the 2nd Name Line (or 3rd Name Line if 2nd Name Line already contains name information) as the *1st* Street Address Line, and continue on this line as a 2nd Street Address line. This line may be all blank, but only for legitimate reasons; for example, if the recipient is from a small town or islet or other place where a town or island name is sufficient to enable mail to be received. Left justify and blank fill.
16	279–303	City	Enter the name of City, Town, Village, Municipality or rural place of residence of the recipient. Valid characters are as in street address. Left justify, and blank fill. Two or more consecutive, imbedded blanks between city parts are not acceptabe. For U.S. military installations enter one of the following: APO New York FPO New York APO San Francisco FPO San Francisco APO Seattle FPO Seattle APO Miami FPO Miami The name of the installation or ship may not be entered here, but should be in the Street Address Line.
17	304–318	Province Name	Enter here the name of the Province, Foreign State (but *not* the U.S. State), County, Shire, District, Region, or other political subdivision. For many countries the province (or other political subunit) is an important part of the postal address. For Canada the Province should be given here. A Canadian province must be expressed as a two-character code from the Canadian Province Code List below. No other abbreviations may be used, nor may the Canadian Province name be written out in full. If a Province (or other policital subunit) is not available, blank fill this element. Valid characters are alphabetic, numeric, blank, ampersand (&), Hyphen (-), or Slash (/). Left justify, blank fill. Two or more consecutive, imbedded blanks between province parts are not acceptable.

Canadian Province and Codes

Province	*Province Code*
Alberta	AB
British Columbia	BC
Labrador	LB
Manitoba	MB
New Brunswick	NB
Newfoundland	NF
Nova Scotia (including Sable Island)	NS
Northwest Territories	NT
Ontario	ON
Prince Edward Island	PE
Quebec	PQ
Saskatchewan	SK
Yukon Territories	YK

18	319–327	Postal Code	Enter the Foreign or U.S. Postal Code (Zip Code), if available. Withholding Agents should make an effort to obtain postal codes, especially for the following countries: Belgium, Canada, France, Germany, Italy, Spain, Switzerland, Netherlands, and United Kingdom. For U.S. addresses (including all possessions) a Zip Code must be given. All postal codes should be left justified and blank filled. Alphabetic, numeric, and blank characters only are allowed here. Do not omit any blanks that may appear in the Zip Code.

Element	Positions	Title	Description
19	328 & 329	State Code	For all U.S. addresses enter the correct two-letter code as prescribed for Post Office use. The state code *must* be present of all U.S. addresses, including territories and APO/FPO. Leave blank for non-U.S. addresses. See list in Section 4, above.
20	330–349	Country Name	Enter the unabbreviated name of the recipients country. Omit political titles such as "People's Republic Of", "Kingdom Of", etc. Use the English Language name, as opposed to the native language name. For example, use "Finland" and not "Suomi". Leave this field blank for all U.S. addresses, including territories, and APO/FPO. Left justify and blank fill.
21	350 & 351	Income Code	Enter the two digit income code from the following list. Valid range is 01–23 or 50. If a given recipient receives more than one kind of income, additional "Q" records must be prepared, since only one income code may be shown per "Q" record.

Income Code List

01	Interest paid by U.S. obligators—general
02	Interest on real property mortgages
03	Interest paid to a controlling foreign corporation
04	Interest paid by foreign corporations (U.S. Agent)
05	Interest in tax-free government bond
06	Dividends paid by U.S. corporation general
07	Dividends paid by U.S. subsidiary to foreign parent corporation
08	Dividends paid by foreign corporations
09	Capital gains
10	Industrial royalties
11	Motion Picture or television copyright royalties
12	Other copyright royalties
13	Real Property income and natural resources royalties
14	Pensions, annuities, alimony, and/or insurance premiums
15	Scholarship or fellowship compensations
16	Compensations for independent personal services[1]
17	Compensations for dependent personal services[1]
18	Compensations for teaching[1]
19	Compensations during training[1]
20	Earnings as an Artist or Athlete
21	Social Security benefits
22	Railroad Retirement (Tier 1) benefits
23	Railroad Retirement (Tier 2) benefits
50	Other income (non-personal service compensations)

[1] If this income (codes 16-19) is from earnings as an artist or athlete, use Income Code 20.

Element	Positions	Title	Description
22	352 & 353	Type of Recipient Code	Enter two digit code from the list below. Valid range is 01–09, 19 or 20.

Code	*Type of Recipient*
01	Individual[1]
02	Corporation[1]
03	Partnership[1]
04	Fiduciary
05	Nominee
06	Government or International Organization
07	"Tax Exempt" Organization
08	Private Foundation
09	Artist or Athlete
19	Other
20	Type of Recipient unknown

1 If the income recipient is an artist or athlete, use Recipient Code 09.

Element	Positions	Title	Description
23	354–364	Gross Income Paid	Enter dollars and cents up to 11 characters. Do *not* enter decimal point. Right justify and zero fill. An income amount other than zero must be shown. For whole dollar amounts, the cents *must* be shown by zeros. For example, $1500 should be shown as 00000150000 where the leftmost 5 zeros are "filler" and the rightmost 2 zeros represent cents.
24	365	Exemption Code	Enter the one-digit exemption code from the list below. If the rate of tax shown is 00%, enter the code of 1–4 that applies. If the rate of tax shown is other than 00%, enter a zero in this field. *Code* — *Description* Zero — No exemption claimed, rate of tax is above 00% 1 — Income is effectively connected with a U.S. trade or business (Form 4224 must be attached to Form 1042) 2 — Income is exempt from tax by the Internal Revenue Code 3 — Income is non-U.S. sourced 4 — No withholding per treaty for this type of income
25	366	Correction Indicator	Enter the one position code to identify if this return is the original issuance, an amendment to a previously submitted return, or a total replacement to a previously submitted return. *Code* — *Description* Zero — Original return R — Replacement return A — Amended return
26	367 & 368	Rate of Tax	Enter two-digit tax rate. Do not use percent signs or decimal points. A valid rate must be shown. For fractional rates, drop the fraction (e.g. for 12½ use 12, and for 27½ use 27). Valid tax rates are: 00 02 04 05 08 10 12 14 15 20 25 27 30 Note that when an exemption code of 1–4 is used for element 24, the Rate of Tax *must* be zero.
27	369–379	Amount of Tax Withheld	Enter in dollars and cents the amount of tax withheld, if any. An amount must be shown if the Rate of Tax is greater than 00, or if income is not otherwise exempt from withholding. If the rate of tax is 00, the amount of tax withheld should be zero. Specifications are the same as for Element 23 (Gross Income Paid). Right justify and zero fill.
28	380–414	Payer's Name	Enter the name of the Payer of Income, if different from the Withholding Agent, up to the limit of 35 characters. Abbreviate as needed, omitting punctuation. Left justify and blank fill. If Withholding Agent and Payer are one in the same, blank fill Payer Name. Valid characters are alphabetic, numeric, blank, ampersand (&), and hyphen (-).
29	415–423	Payer's EIN	Enter the 9 digit numeric Payer's Employer Identification Number if element 28, Payer Name, is significant. Blank fill if unknown or Payer Name is blank.
30	424–450	(Reserved)	Blank Fill.

NOTE: All money fields must be mathematically verified by the transmitter before being sent to IRS.

SEC. 6. WITHHOLDING AGENT "W" RECORD

Enter a "W" record after the last "Q" record submitted for a particular Withholding Agent. The "W" record serves as a summary of the preceding "Q" record data, and enables the Service to double-check the correctness of information received. Several "W" records for different withholding agents may appear on the same Transmitter's file. Also, the "W" record may refer to "Q" records on more than one reel, provided all of the preceding "Q" records are for the same withholding agent. A "W" record may only be followed by new Recipient "Q" records for the next Withholding Agent, if any, or by a tape mark and/or trailer label when more reels follow this reel, or by an End of Transmission "Y" record, when this is the last reel of the file. The "W" record cannot be the last record on the file. Each "W" record has a fixed length of 450 positions. All elements of data in the "W" record are required as follows:

Element	Positions	Title	Description
1	1	Record Type	Enter the letter "W"
2	2 & 3	Payment Year	Enter the last two digits of the calendar year for which income and withholding are being reported. All recipient "Q" records must report payments for this year *only*. Different tax years may not appear on the same file.
3	4–12	EIN	Enter the 9 digits of the Employer Identification Number of the *Withholding Agent*. Omit the hyphen.
4	13–47	Agent Name	Enter the name of the Withholding Agent, up to the limit of 35 characters. Abbreviate as needed, omitting punctuation. Left justify and blank fill.
5	48–82	Agent Address	Enter the street address, P.O. Box, or other location of the withholding agent to a limit of 35 characters. Abbreviate as needed, omitting punctuation. Left justify and blank fill.
6	83–102	City	Enter the city, town, or other locality name up to the limit of 20 characters. Left justify and blank fill.
7	103–104	State	Enter the two-character alphabetic code from the list in Section 4 above.
8	105–113	Zip Code	Enter 9 numeric characters for all U.S. addresses (including territories, possessions, and APO/FPO). For 5 digit zip codes, left justify and zero fill. Zero fill for addresses outside the U.S.
9	114–121	"Q" Record Count	Enter the total number of "Q" records for this withholding agent; that is, the total count of "Q" records following the last "W" record, or if this is the first "W" record on the file, the total number of "Q" records since the "T" record. The presence of a "Z" or "T" record does not interrupt the count, which may therefore include consecutive "Q" records on more than one tape reel.
10	122–134	Total Gross Amount Paid	Enter the sum of all gross amounts paid in all "Q" records, counted in Element 9 above. Zero fill and right justify. Do not "round off" this total, since it is used as a "hash total" check on the "Q" records.
11	135–147	Total Tax Withheld	Enter the sum of all tax withheld amounts from all "Q" records counted in Element 9 above. Right justify, zero fill.
12	148–450	Blank fill	Blank fill up to the total of 450 characters.

SEC. 7. END OF REEL "Z" RECORD

End every reel of a file, except the last reel, with an End of Reel "Z" record. If the last record of that reel would otherwise be a "W" record, then do not use the "Z" record, but use the "W" record instead. A "Z" record may only appear as the last data record of a reel. If records are blocked, the "Z" record must be the last data record in the last block on the reel, but padding records (all 9's) may follow to fill the block. The "Z" record is identical in format to the "W" record. The "Z" record may only be preceded immediately by a "Q" record, and may only be followed by Trailer labels, if any, or a tape mark. Elements of the "Z" record differ from the same elements of the "W" record as follows: (1) Element 1 Record Type, will be a "Z" instead of "W"; (2) Element 9, Total Number of "Q" records, will include a count of all "Q" records since the last preceding "W" record or "T" record; (3) Elements 10 and 11 will likewise total corresponding amounts on "Q" records since the preceding "W" or "T" record.

SEC. 8. END OF TRANSMISSION "Y" RECORD

End the last reel on a file with an End of Transmission "Y" record. The "Y" record may only be preceded by a "W" record. It may only be followed by a tape mark or tape mark and a Trailer Label (if Trailer Labels are used), or a Trailer Label. The "Y" record will count the total number of withholding agents in the transmission, and the total number of tape reels in the file. The "Y" record has a fixed length of 450 positions, and all elements listed are required.

Element	Positions	Title	Description
1	1	Record Type	Enter letter "Y"
2	2–4	Withholding Agent Count	Enter the total number of withholding agents on this file. This count will be the same as the total number of "W" records. Right justify and zero fill.
3	5–7	Reel Count	Enter the total number of reels for this transmission. Right justify and zero fill.
4	8–450	Blank fill	Blank fill up to the end of the record.

SEC. 9. EFFECT ON OTHER DOCUMENTS

Revenue Procedure 85–53 is superseded.

Part IV. Items of General Interest

Notice of Proposed Rulemaking
Definition of S Corporation
LR-262-82

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed Income Tax Regulations concerning the definition of the term "S corporation." Changes to the applicable tax law were made by the Subchapter S Revision Act of 1982 [1982-2 C.B. 702] and the Tax Reform Act of 1984 [1984-3 C.B. (Vol. 1)1]. The regulations would provide guidance on the qualifications of an S corporation.

DATES: Written comments and requests for a public hearing must be delivered or mailed by December 8, 1986. The amendments are proposed to be effective for taxable years beginning after December 31, 1982.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue, Attention: CC:LR:T (LR-262-82), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Robert H. Ginsburgh of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T). Telephone: 202-566-3297 (not a toll-free number).

SUPPLEMENTARY INFORMATION: BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 1361 of the Internal Revenue Code of 1954. These amendments are proposed to conform the Income Tax Regulations to sections 2 and 6 of the Subchapter S Revision Act of 1982 (96 Stat. 1669) and to section 721(c) and (f) of the Tax Reform Act of 1984 (98 Stat. 967).

IN GENERAL

The proposed regulations provide that the term "S corporation" means, with respect to any taxable year, a small business corporation for which an election under section 1362(a) is in effect for that taxable year. In addition, the proposed regulations provide that the term "small business corporation" means a domestic corporation that is not an ineligible corporation and that does not have (1) more than 35 shareholders, (2) as a shareholder, a person (other than an estate and certain trusts) who is not an individual, (3) a nonresident alien as a shareholder, or (4) more than one class of stock.

SMALL BUSINESS CORPORATION DEFINED

Ineligible corporation

Under the proposed regulations, an ineligible corporation is a corporation that is (1) a member of an affiliated group (determined under section 1504 without regard to any exception contained in subsection (b) thereof), whether or not that affiliated group has ever filed a consolidated return, (2) a financial institution to which section 585 or 593 applies, whether or not that financial institution uses the reserve for bad debts method provided in section 166(c), (3) an insurance company subject to tax under subchapter L, chapter 1 of the Code, (4) a corporation to which an election under section 936 applies, or (5) a DISC or former DISC. Certain exceptions to these rules are provided in the proposed regulations, such as the exception for a qualified casualty insurance electing small business corporation.

Number of shareholders

Under the Subchapter S Revision Act of 1982, the number of permissible shareholders of a small business corporation has been increased to thirty-five. For purposes of determining whether a corporation has more than thirty-five shareholders, the proposed regulations provide that stock owned by a husband and wife (or by either of or both of their estates) is treated as if owned by one shareholder, regardless of the form in which they own such stock.

Shareholders must be individuals or estates

In general, the proposed regulations provide that a corporation in which any shareholder is a corporation, partnership, or trust, or a corporation in which any shareholder's interest in the stock of the corporation is a legal life estate, usufruct interest, or an interest for a term of years, does not qualify as a small business corporation. However, a corporation having a shareholder who has an interest in the stock of the corporation that is a legal life estate or usufruct interest for life, which interest was created or came into existence before January 1, 1983, will not thereafter fail to qualify as a small business corporation by reason of that interest. Moreover, a corporation having a shareholder who has an interest in the stock of the corporation that is a legal life estate or usufruct interest for life, which interest comes into existence after December 31, 1982 (excluding those interests that were created before January 1, 1983), will not thereafter fail to qualify as a small business corporation by reason of that interest if all of the following requirements are met: (1) That interest is owned by only one individual who is a citizen or resident of the United States, (2) the individual for whom that interest was created has not transferred that interest to any other person, and (3) that interest must terminate upon the death of the individual for whom that interest was created. If any requirement described in the preceding sentence ceases to be met, the corporation will cease to be a small business corporation.

Special rules for certain trusts

A subpart E trust, a voting trust, a certain type of testamentary trust, and a qualified subchapter S trust that is treated as a subpart E trust are permitted to be shareholders of a small business corporation. Under the proposed regulations, a subpart E trust is a trust all of which (income and corpus) is treated (under subpart E, part I, subchapter J, chapter 1 of the Code) as owned by one individual (whether or not the grantor) who is a citizen or resident of the United States. Special rules apply in the case of a husband and wife. The deemed owner of a subpart E trust (and not the trust) is treated as the shareholder for purposes of determining whether the corporation qualifies as a small business corporation. If the trust ceases to be a subpart E trust upon the death of the deemed owner, the estate of the deemed owner (and not the trust) is treated as the shareholder for a certain period provided the trust continues in existence after the death of the deemed owner.

The proposed regulations provide that a voting trust is a trust created primarily to exercise the voting power of stock transferred to it. In order to qualify as a voting trust for purposes of section 1361, such a trust must (1) delegate to one or more trustees the right to vote, (2) require all distributions with respect to the stock of the corporation held by the trust to be paid to, or on behalf of, the beneficial owners of that stock, (3) require title and possession of that stock to be delivered to those beneficial owners upon termination of the trust, and (4) terminate, under it terms or by state law, on or before a specific date or event. For purposes of determining whether the corporation qualifies as a small business corporation, each beneficial owner of the stock held by the trust (and not the trust) is treated as a shareholder.

A qualified subchapter S trust, as defined in the proposed regulations, is a trust that satisfies all of the following requirements: (1) All the income of the trust is distributed (or is required to be distributed) currently to one individual who is a citizen or resident of the United States, and (2) the terms of the trust require that (A) during the life of the current income beneficiary, there shall be only one income beneficiary of the trust, (B) any corpus distributed during the life of the current income beneficiary may be distributed only to that income beneficiary, (C) the current income beneficiary's income interest in the trust shall terminate on the earlier of that income beneficiary's death or the termination of the trust, and (D) upon the termination of the trust during the life of the current income beneficiary, the trust shall distribute all its assets to that income beneficiary. If the current income beneficiary of a qualified subchapter S trust makes the election under section 1361(d)(2), the trust is treated as a subpart E trust. Accordingly, the current income beneficiary of the trust (and not the trust) is treated as the shareholder for purposes of determining whether the corporation qualifies as a small business corporation. If the trust ceases to be treated as a subpart E trust upon the death of that income beneficiary, the estate of that income beneficiary (and not the trust) is treated as the shareholder for a certain period provided the trust continues in existence after the death of that income beneficiary.

QUALIFIED SUBCHAPTER S TRUST ELECTION

In order to be an eligible shareholder of an S corporation, a qualified subchapter S trust must have its beneficiary make the election provided in section 1361(d)(2), which permits a qualified subchapter S trust to be treated as a subpart E trust. The qualified subchapter S trust election must be made separately with respect to each corporation whose stock is held by the trust. Generally, the qualified subchapter S trust election must be filed within the 16-day-and-2-month period beginning on the date on which the stock of the corporation is transferred to the trust or within the 16-day-and-2-month period beginning on the first day of the first taxable year for which the election to be an S corporation is effective, whichever period of time occurs later. However, if stock of the corporation has been transferred to the trust on or before the date on which the corporation makes the election to be an S corporation, and if that election and that transfer are made before the beginning of the first day of the first taxable year for which that election is effective, the qualified subchapter S trust election must be filed within the 16-day-and-2-month period beginning on the date on which the corporation makes the election to be an S corporation. The qualified subchapter S trust election may not be made by a beneficiary of a subpart E trust (as described in section 1361(c)(2)(A)(i) without regard to section 1361(d)). In addition, the qualified subchapter S trust election may not be made by a beneficiary of a trust with respect to a corporation if a person (other than the beneficiary making that election or the spouse of that beneficiary) is treated under subpart E, part I, subchapter J, chapter 1 of the Code as the owner as to any part of that portion of the trust which consists of the stock of that corporation.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be made available for public inspection and copying. A public hearing will be held upon written request of any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on those requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on those requirements to OMB also send copies of those comments to the Service.

SPECIAL ANALYSES

The Commissioner of Internal Revenue has determined that a Regulatory Impact Analysis is not required because this proposed rule is not a major rule under Executive Order 12291.

The Commissioner of Internal Revenue has concluded that these proposed regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations are not subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

DRAFTING INFORMATION

The principal author of these proposed regulations is Robert H. Ginsburgh of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing these proposed regulations, both on matters of substance and style.

* * * * *

Proposed amendments to the regulations

The proposed amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority citation for Part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805; * * * §1.1361–1A(i)(3) and (4) also issued under 26 U.S.C. 1361 (d)(2)(B)(iii).

Par. 2. Section 1.1361–1A is added immediately after §1.1361–0A to read as follows:

§1.1361–1A S corporation defined.

(a) *In general*. For purposes of this title, the term "S corporation" means, with respect to any taxable year, a small business corporation (as defined in paragraph (b) of this section) for which an election under section 1362(a) is in effect for that taxable year. In addition, the term "C corporation" means, with respect to any taxable year, a corporation that is not an S corporation for that taxable year.

(b) *Small business corporation defined*. For purposes of subchapter S, chapter 1 of the Code and the regulations thereunder, the term "small business corporation" means a domestic corporation that is not an ineligible corporation (as defined in paragraph (d) of this section) and that does not have—

(1) More than 35 shareholders,

(2) As a shareholder, a person (other than an estate and other than certain trusts described in paragraph (h)(1) of this section) who is not an individual,

(3) A nonresident alien as a shareholder, or

(4) More than one class of stock.

The term "estate," for purposes of this paragraph, includes the estate of an individual in a case under title 11 of the United States Code.

(c) Domestic corporation. For purposes of paragraph (b) of this section, the term "domestic corporation" means a corporation as defined in section 7701(a)(3) created or organized in the United States or under the law of the United States or of any State or Territory.

(d) *Ineligible corporation*—(1) *General rule*. (i) Except as otherwise provided in this paragraph, the term "ineligible corporation" means a corporation that is—

(A) A member of an affiliated group (determined under section 1504 without regard to any exception contained in subsection (b) thereof), whether or not that affiliated group has ever filed a consolidated return,

(B) A financial institution to which section 585 or 593 applies, whether or not that financial institution uses the reserve for bad debts method provided in section 166 (c),

(C) An insurance company (other than a qualified casualty insurance electing small business corporation, as defined in paragraph (d)(1)(ii) of this section) subject to tax under subchapter L, chapter 1 of the Code,

(D) A corporation to which an election under section 936 applies, or

(E) A DISC or former DISC.

(ii) The term "qualified casualty insurance electing small business corporation" means any corporation described in section 831 (a) if—

(A) As of July 12, 1982, the corporation was an electing small business corporation (within the meaning of section 1371(a) and (b), as in effect on July 1, 1982) and was described in section 831(a),

(B) The corporation was formed before April 1, 1982, and proposed (through a written private offering first circulated to investors before April 1, 1982) to elect to be taxed as an electing small business corporation (within the meaning of section 1371(a) and (b), as in effect on July 1, 1982) and to be operated on an established insurance exchange, or

(C) The corporation is approved for membership on an established insurance exchange pursuant to a written agreement entered into before December 31, 1982, and the corporation is described in section 831(a) as of December 31, 1984.

However, this paragraph (d)(1)(ii) shall not apply unless, as of July 12, 1982, the corporation is actively seeking investors or otherwise shows a present intent to enter into the casualty insurance business.

A corporation shall not be treated as a qualified casualty insurance electing small business corporation unless an election made under section 1372(a) (as in effect on July 1, 1982) is in effect for the first taxable year of the corporation beginning after December 31, 1984. The provisions of subchapter S of chapter 1 of the Code as in effect on July 1, 1982, shall apply in the case of a qualified casualty insurance electing small business corporation except as provided in paragraph (d)(1)(iii) of this section.

(iii) The provisions of paragraph (d)(1)(ii) of this section shall cease to apply with respect to any corporation after—

(A) Any termination of the election of the corporation made under section 1372(a) (as in effect on July 1, 1982),

(B) The first date on which more than 50 percent of the stock of the corporation is newly owned stock (within the meaning of section 1378(c)(2) and (3) as in effect for any taxable year beginning after December 31, 1982, applied by substituting "December 31, 1984," for "December 31, 1982," each place it appears therein), or

(C) The corporation ceases to be described in section 831(a).

(2) *Inactive corporation exception*. (i) For purposes of paragraph (d)(1)(i)(A) of this section, a corporation (hereinafter in this subparagraph referred to as the parent corporation) shall not be considered during a period within its taxable year to be a member of an affiliated group solely by reason of the ownership of stock in another corporation (hereinafter in this subparagraph sometimes referred to as the subsidiary corporation) if the subsidiary corporation—

(A) Has not begun business at any time on or before the close of that period, and

(B) Does not have gross income for that period.

(ii) The determination under paragraph (d)(2)(i)(A) of this section of the date on which a subsidiary corporation begins business shall be made by taking into account all the facts and circumstances of the particular case. A corporation has not "begun business," however, merely because it is "in existence." Ordinarily, a corporation begins business when it starts the business operations for which it was organized. Mere organizational activities, such as the obtaining of the corporate charter, are not alone sufficient to show the beginning of business. An example of a corporation that has not begun business is a corporation incorporated for the sole purpose of reserving a corporate name in a State or States in which the parent corporation is not doing business. If the activities of a corporation have advanced to the extent necessary to establish the nature of its business operations, however, the corporation will be deemed to have begun business. For example, a corporation that acquires operating assets necessary for the type of business contemplated may be deemed to have begun business.

(iii) If a subsidiary corporation ceases to meet any of the requirements of paragraph (d)(2)(i) of this section, then the parent corporation's election under section 1362(a) shall terminate effective on and after the earlier of the first day that the subsidiary corporation begins business or the first day, determined under the subsidiary corporation's method of accounting, that the subsidiary corporation realizes gross income.

(iv) The application of this subparagraph may be illustrated by the following example:

Example. Corporation P, which uses the calendar year as its taxable year, in 1983 owns all the stock of Corporation S, which uses the calendar year as its taxable year. For purposes of paragraph (d)(1)(i)(A) of this section, P would not be considered at any time during 1983 to be a member of an affiliated group solely by reason of its ownership of S's stock if S has not begun business before January 1, 1984, and has no gross income for calendar year 1983. Thus, P could qualify as a small business corporation during 1983 if it meets the other requirements provided in section 1361(b). Assuming that P's ownership of S stock remains unchanged, P would cease to be a small business corporation on the day that S either begins business or realizes gross income (determined under S's method of accounting), whichever day occurs earlier.

(3) *Exception for foreign corporation or DISC.* (i) In the case of a corporation which on September 28, 1982, was an electing small business corporation (within the meaning of section 1371(a) and (b), as in effect before enactment of the Subchapter S Revision Act of 1982), and which then owned at least 80 percent of the stock of a foreign corporation, a DISC, or a former DISC (within the meaning of section 1504(b)(3) or (7)), the corporation shall not be treated as an ineligible corporation under paragraph (d)(1)(i)(A) of this section by reason of such ownership.

(ii) The provisions of paragraph (d)(3)(i) of this section shall cease to apply with respect to any S corporation after—

(A) Any termination of the election of the corporation made under section 1362(a),

(B) The first date on which more than 50 percent of the stock of the corporation is newly owned stock (within the meaning of section 1378(c)(2) and (3)), or

(C) The first date after September 28, 1982, on which the corporation ceases to meet such 80 percent ownership requirement.

(e) *Number of shareholders*—(1) *General rule.* A corporation does not qualify as a small business corporation if it has more than 35 shareholders. Ordinarily, the persons who would have to include in gross income dividends distributed with respect to the stock of the corporation are considered to be the shareholders of the corporation. For example, if stock (owned other than by a husband and wife) is owned by tenants in common or joint tenants, each tenant in common or joint tenant is generally considered to be a shareholder of the corporation (For special rules relating to stock owned by husband and wife, see paragraph (e)(2) of this section.). Persons for whom stock of a corporation is held by a nominee, guardian, custodian, or an agent are generally considered to be shareholders of the corporation. But if stock is owned by a partnership, the partnership (and not its partners) is considered to be the shareholder and the corporation does not qualify as a small business corporation.

(2) *Special rules relating to stock owned by husband and wife.* For purposes of paragraph (e)(1) of this section, stock owned by a husband and wife (or by either or both of their estates) shall be treated as if owned by one shareholder, regardless of the form in which they own such stock. However, for purposes of paragraphs (f) and (g) of this section, each spouse (or his or her estate) shall be treated as a shareholder. The treatment described in this subparagraph shall cease upon dissolution of the marriage for any reason other than death.

(f) *Shareholders must be individuals or estates*—(1) *General rule.* Except as otherwise provided in this paragraph (f) and paragraph (h) of this section, a corporation in which any shareholder is a corporation, partnership, or trust, or a corporation in which any shareholder's interest in the stock of the corporation is a legal life estate, usufruct interest, or an interest for a term of years, does not qualify as a small business corporation.

(2) *Special rule for split interests created or coming into existence before January 1, 1983.* A corporation having a shareholder who has an interest in the stock of the corporation that is a legal life estate or usufruct interest for life, which interest was created or came into existence before January 1, 1983, will not thereafter fail to qualify as a small business corporation by reason of that interest. For purposes of this paragraph (f), an interest shall be considered to be created before January 1, 1983, if the interest is created under the terms of a will executed before that date, and if the decedent dies before January 1, 1986, without having republished the will after December 31, 1982, by codicil or otherwise. For special rules relating to certain trusts that are not considered to be shareholders, see paragraph (h) of this section.

(3) *Special rule for split interests coming into existence on or after January 1, 1983.* A corporation having a shareholder who has an interest in the stock of the corporation that is a legal life estate or usufruct interest for life, which interest comes into existence after December 31, 1982 (excluding those interests that were created before January 1, 1983), will not thereafter fail to qualify as a small business corporation by reason of that interest if all of the following requirements are met.

(i) That interest is owned by only one individual who is a citizen or resident of the United States,

(ii) The individual for whom that interest was created has not transferred that interest to any other person, and

(iii) That interest must terminate upon the death of the individual for whom that interest was created.

If any requirement in subdivision (i), (ii), or (iii) of this subparagraph ceases to be met, the provisions of this subparagraph shall cease to apply as of the first date on which that requirement ceases to be met.

(g) *No nonresident alien shareholder.* A corporation having a shareholder who is a nonresident alien does not qualify as a small business corporation.

(h) *Special rules relating to trusts*—(1) *General rule.* For purposes of paragraphs (e)(1), (f)(1), and (g) of this section, the following rules apply to determine who is treated as a shareholder if stock is held by a trust. Except as otherwise provided in this subparagraph, if stock is held by a trust, the trust is considered to be the shareholder. However, the trust is not considered to be the shareholder in the following cases:

(i) In the case where stock is held by a subpart E trust (as defined in paragraph (h)(3)(i) of this section), the deemed owner of the trust (determined under subpart E, part I, subchapter J, chapter 1 of the Code) shall be treated as the shareholder. If the trust ceases to be a subpart E trust upon the death of the deemed owner, the estate of the deemed owner shall be treated as the shareholder of stock held by the trust when the deemed owner dies, provided the trust continues in existence after the death of the deemed owner. The estate ordinarily shall cease to be treated as the shareholder of that stock upon the earlier of the transfer of that stock by the trust or the expiration of the 60-day period beginning on the date on which the deemed owner dies. However, if the entire corpus of the trust is includible in the gross estate of the deemed owner, the estate shall cease to be treated as the shareholder of that stock upon the earlier of the transfer of that stock by the trust or the expiration of the 2-year period beginning on the date on which the deemed owner dies. For the purpose of determining whether the entire trust corpus is includible in the gross estate of the deemed owner, any community property interest in the trust held by the deemed owner's spouse which arises by reason of applicable State law shall be disregarded.

(ii) In the case where stock is held by a voting trust (as defined in paragraph (h)(3)(ii) of this section), each beneficial owner of the stock shall be treated as a shareholder.

(iii) In the case where stock is transferred to a trust (other than a subpart E trust, a voting trust, and a qualified subchapter S trust that is treated as a subpart E trust) pursuant to the terms of a will, the estate of the testator shall be treated as the shareholder of that stock until the earlier of the disposition of that stock by the trust or the expiration of the 60-day period beginning on the date on which that stock is transferred to the trust.

(iv) In the case where stock is held by a qualified subchapter S trust that is treated as a subpart E trust, the income beneficiary who is treated (under section 678(a)) as the owner of the stock because of an election made under section 1361(d)(2) shall be treated as the shareholder. If the trust ceases to be treated as a subpart E trust upon the death of that income beneficiary (*e.g.*, there is no successive income beneficiary nor is another person treated as the deemed owner of the trust as described in paragraph (h)(3)(i) of this section), the estate of that income beneficiary shall be treated as the shareholder of the stock with respect to which the income beneficiary made the election under section 1362(d)(2), provided the trust continues in existence after the death of that income beneficiary. The estate ordinarily shall cease to be treated as the shareholder of that stock upon the earlier of the transfer of that stock by the trust or the expiration of the 60-day period beginning on the date on which the deemed owner dies. However, if the entire corpus of the trust is includible in the gross estate of that income beneficiary, the estate shall cease to be treated as the shareholder of that stock upon the earlier of the transfer of that stock by the trust or the expiration of the 2-year period beginning on the date on which the deemed owner dies. For the purpose of determining whether the entire trust corpus is includible in the gross estate of the deemed owner, any community property interest in the trust held by the deemed owner's spouse which arises by reason of applicable State law shall be disregarded.

(2) *Foreign trusts.* For purposes of paragraph (h)(1) of this section, in any case where stock is held by a foreign trust, the trust is considered to be the shareholder. Thus, for example, if a foreign trust qualifies as a voting trust, any corporation in which the trust holds stock does not meet the qualifications of a small business corporation.

(3) *Certain trusts defined*—(i) *Subpart E trust.* For purposes of this section, a subpart E trust is a trust all of which (income and corpus) is treated (under subpart E, part I, subchapter J, chapter 1 of the Code) as owned by one individual (whether or not the grantor) who is a citizen or resident of the United States. For the purpose of determining whether the entire trust is treated as owned by one individual, a husband and wife who file a joint return, and each of whom is a citizen or resident of the United States, shall be treated as one individual.

(ii) *Voting trust.* A voting trust is a trust created primarily to exercise the voting power of stock transferred to it. In order to qualify as a voting trust for purposes of this section, such a trust must be represented by a written agreement, or written document (such as a will), that—

(A) Delegates to one or more trustees the right to vote,

(B) Requires all distributions with respect to the stock of the corporation held by the trust to be paid to, or on behalf of, the beneficial owners of that stock,

(C) Requires title and possession of that stock to be delivered to those beneficial owners upon termination of the trust, and

(D) Must terminate, under its terms or by state law, on or before a specific date or event.

(i) *Qualified subchapter S trust*—(1) *Definition.* A qualified subchapter S trust is a trust (including a trust that is represented by a will) that satisfies all of the following requirements:

(i) All the income (within the meaning of §1.643(b)–1) of the trust is distributed (or is required to be distributed) currently to one individual who is a citizen or resident of the United States, and

(ii) The terms of the trust meet all the requirements specified in paragraph (i)(2) of this section.

If a qualified subchapter S trust for which an election under section 1361(d)(2) has been made (as described in paragraph (i)(3) of this section) ceases to meet any requirement in paragraph (i)(2) of this section, the provisions of this paragraph (i) shall cease to apply as of the first day on which that requirement ceases to be met. If a qualified subchapter S trust for which an election under section 1362(d)(2) has been made (as described in paragraph (i)(3) of this section) ceases to meet any requirement in paragraph (i)(1)(i) of this section but continues to meet all the requirements in paragraph (i)(2) of this section, the provisions of this paragraph (i) shall cease to apply as of the first day of the first taxable year beginning after the first taxable year for which it ceased to meet any requirement in paragraph (i)(1)(i) of this section. See §§1.651(a)–2(a) and 1.663(b)–1(a) for the rules relating to the determination of whether all income of a trust is distributed (or is required to be distributed currently.

(2) *Terms of a qualified subchapter S trust.* For purposes of paragraph (i)(1)(ii) of this section, the terms of the trust must require that—

(i) During the life of the current income beneficiary, there shall be only one income beneficiary of the trust,

(ii) Any corpus distributed during the life of the current income beneficiary may be distributed only to that income beneficiary,

(iii) The current income beneficiary's income interest in the trust shall terminate on the earlier of that income beneficiary's death or the termination of the trust, and

(iv) Upon termination of the trust during the life of the current income beneficiary, the trust shall distribute all its assets to that income beneficiary.

The determination of whether the terms of a trust meet all the aforementioned requirements depends upon the terms of the trust instrument and the applicable local law. For example, a trust whose governing instrument provides that A is the sole income beneficiary of the trust is considered to have two income beneficiaries if, under the applicable local law, A and B are considered to be the income beneficiaries of the trust. Except as otherwise provided in this subparagraph, if the terms of a trust do not preclude the possibility that any of the aforementioned requirements will not be met, the trust shall not qualify as a qualified subchapter S trust. For example, if the terms of a trust are silent with respect to corpus distributions and distributions of corpus to a person other than the current income beneficiary are permitted under local law, the terms of the trust do not preclude the possibility that corpus will be distributed to a person other than the current income beneficiary. Any transferee of the current income beneficiary's income interest and any person treated as a beneficiary under §1.643(c)–1(a), (b), or (c) shall be treated as a current income beneficiary for purposes of this subparagraph. The fact that the terms of a trust do not preclude the current income beneficiary from transferring his or her interest in the trust or do not preclude a person other than the current income beneficiary named in the trust instrument from being treated as a beneficiary of the trust under §1.643(c)–1(a), (b), or (c) shall not preclude the trust from qualifying as a qualified subchapter S trust.

(3) *Qualified subchapter S trust election.* This paragraph applies to the election provided in section 1361(d)(2) to treat a qualified subchapter S trust (as defined in paragraph (i)(1) and (2) of this section) as a subpart E trust, and thus a qualifying shareholder. This election shall be made separately with respect to each corporation whose stock is held by the trust. The current income beneficiary of the trust or the legal representative of the current income beneficiary (or a natural or an adoptive parent of the current income beneficiary in the case where a legal representative has not been appointed, but only if the current income beneficiary is a minor) shall make this election by signing and filing with the service center with which the corporation files its income tax return a statement that—

(i) Contains the name, address, and taxpayer identification number of the current income beneficiary, the trust, and the corporation,

(ii) Identifies the election as an election made under section 1361(d)(2),

(iii) Specifies the date on which the election is to become effective (not earlier than 15 day and two months before the date on which the election is filed),

(iv) Specifies the date (or dates) on which the stock of the corporation has been transferred to the trust, and

(v) Provides all information necessary to show that the trust meets all the requirements set forth in paragraph (i)(1) and (2) of this section.

In general, the election under section 1361(d)(2) ("the QSST election") must be filed within the 16-day-and-2-month period beginning on the date on which the stock of the corporation is initially transferred to the trust or within the 16-day-and-2-month period beginning on the first day of the first taxable year for which the election under section 1362(a) ("the S election") is effective, whichever period of time occurs later. If stock of the corporation has been transferred to the trust on or before the date on which the corporation makes the S election, and if that election and that transfer are made before the beginning of the first day of the first taxable year for which the S election is effective, the QSST election must be filed within the 16-day-and-2-month period beginning on the date on which the corporation makes the S election. In the case of a trust (other than a qualified subchapter S trust) which ceases to be a subpart E trust (as defined in paragraph (h)(3)(i) of this section), the QSST election must be filed within the 16-day-and-2-month period beginning on the date on which the trust ceases to be a subpart E trust or, if applicable, the date on which the estate of the deemed owner ceases to be treated as a shareholder under paragraph (h)(1)(i) of this section. The QSST election may not be made by a beneficiary of a subpart E trust (as described in paragraph (h)(1)(i) of this section without regard to this paragraph (i)). In addition, the QSST election may not be made by a beneficiary of a trust with respect to a corporation if a person (other than such beneficiary or his or her spouse) is treated under subpart E, Part I, subchapter J, chapter 1 of the Code as the owner as to any part of that portion of the trust which consists of the stock of that corporation. The QSST election does not itself constitute an election as to the status of the corporation; the corporation must make the S election to be treated as an S corporation.

(4) *Coordination with grantor trust rules.* For purposes of subpart E, part I, subchapter J, chapter 1 of the Code, if a valid QSST election is made, the beneficiary shall be treated under section 678(a) as the owner of that portion of the trust which consists of the stock with respect to which such election was made, contrary provisions of section 678 notwithstanding.

(5) *Successive income beneficiary.* If a prior income beneficiary of a qualified subchapter S trust has made an election under section 1361(d)(2), a successive income beneficiary of that trust shall be treated as consenting to the election unless the successive income beneficiary affirmatively refuses to consent to the election. For this purpose, the term "successive income beneficiary" does not include any beneficiary of a separate trust that is newly created upon the death of the income beneficiary of the qualified subchapter S trust. A successive income beneficiary of the trust shall make the affirmative refusal to consent by signing and filing with the service center with which the corporation files its income tax return a statement that—

(i) Contains the name, address, and taxpayer identification number of the successive income beneficiary, the trust, and the corporation,

(ii) Identifies the refusal as an affirmative refusal to consent made under section 1361(d)(2), and

(iii) Sets forth the date on which the successive income beneficiary became the income beneficiary.

The affirmative refusal to consent must be filed within 15 days and 2 months after the date on which the successive income beneficiary became the income beneficiary. The affirmative refusal to consent shall be effective as of the date on which the successive income beneficiary became the income beneficiary.

(6) *Revocation of election under section 1361(d)(2).* An election made under section 1361(d)(2) may be revoked only with the consent of the Commissioner. An application for consent to revoke the election must be signed by the current income beneficiary and shall—

(i) Contain the name, address, and taxpayer identification number of the current income beneficiary, and of the trust and the corporation identified in connection with the election,

(ii) Identify the election being revoked as an election made under section 1361(d)(2), and

(iii) Explain why the current income beneficiary seeks to revoke the election.

The application for consent to revoke the election must be submitted to: Commissioner of the Internal Revenue, Attention: CC:IND, 1111 Constitution Avenue, N.W., Washington, D.C. 20224.

(j) *Examples.* The provisions of paragraphs (h) and (i) of this section may be illustrated by the following examples:

Example (1). (i) A, an individual who is a United States citizen, transfers in 1983 to a trust her shares of stock of Corporation M, a calendar year corporation with ten shareholders. Under the terms of the trust, A has the power to revest the entire corpus and the income therefrom in herself and B is the sole beneficiary. Moreover, the trust will continue in existence after A's death. Corporation M makes an election to be an S corporation that is effective for calendar year 1983. The trust qualifies as a subpart E trust described in section 1361(c)(2)(A)(i), and thus, A (and not the trust) is treated as the shareholder for purposes of section 1361(b)(1).

(ii) Assume the same facts as in example (1)(i) except that A dies without having exercised her power, and that upon A's death the trust ceases to be a subpart E trust because no individual is deemed to be the owner of the entire trust (income and corpus). Since the trust ceases to be a subpart E trust upon A's death, A's estate (and not the trust) is treated as the shareholder for purposes of section 1361(b)(1). Under section 2038, the entire corpus of the trust is includible in A's gross estate. Accordingly, A's estate shall cease to be treated as the shareholder of that stock upon the earlier of the transfer of that stock by the trust (other than to A's estate) or the expiration of the 2-year period beginning on the date on which A died.

(iii) Assume the same facts as in example (1)(ii) except that the terms of the trust also provide that, if A does not exercise her power before her death, B will have the power exercisable solely by himself to vest the entire corpus and the income therefrom in himself. Although A has died, the trust continues to qualify as a subpart E trust because, upon A's death, B is deemed to be the owner of the entire trust (income and corpus). Since the trust does not cease to be a subpart E trust upon A's death, B (and not the estate of A) is treated as the shareholder for purposes of section 1361(b)(1).

Example (2). C, the sole shareholder of an S corporation, establishes an irrevocable trust for the benefit of his son, D, and transfers shares of the corporation to the trust. The trust will terminate on the earlier of D's death or after 10 years and 1 day. Upon termination the trust corpus will revert to C and all accumulated but previously undistributed trust income will be distributed to D or his estate. During the term of the trust, D has a noncumulative power to withdraw all ordinary trust income, and all income allocable to trust corpus, earned during each taxable year. Under these facts, the trust does not qualify as a subpart E trust under section 1361 because for purposes of that section the entire trust (corpus and income) is not treated as owned by one individual. Accordingly, the trust is an ineligible shareholder and the corporation ceases to be an S corporation as of the date of the stock transfer.

Example (3). F holds interest in two S corporations, Corporation O and Corporation P. F directly owns his shares of stock in Corporation P. F's shares of stock in Corporation O are held by a subpart E trust with F as the deemed owner. F dies on July 1, 1983. The trust continues in existence after F's death but is no longer a subpart E trust. The entire corpus of the trust is not includible in F's gross estate. On August 1, 1983, F's shares of stock in Corporation P are transferred to the trust pursuant to the terms of F's will. Under section 1361(c)(2)(B)(iii), the last day on which F's estate could be treated as the shareholder of Corporation P would be September 29, 1983 (*i.e.*, the 59th day after the date of transfer). Since the stock of Corporation P was not held by the trust when F died, section 1361(c)(2)(B)(ii) does not apply with respect to that stock. With respect to the shares of stock in Corporation O held by the trust, section 1361(c)(2)(B)(ii) is applicable and the last day on which F's estate could be treated as the shareholder of Corporation P would be August 29, 1983 (*i.e.*, the 59th day after the date of death).

Example (4). (i) Corporation Q, a calendar year corporation with 15 shareholders, makes an election to be an S corporation that is effective for calendar year 1983. On July 1, 1983, G, a shareholder of Corporation Q, transfers his shares of Corporation Q stock to a trust with H as its current income beneficiary. The trust, which uses the calendar year as its taxable year, initially satisfies all the requirements to be a qualified subchapter S trust, even though its terms do not require that all income of the trust be distributed currently. On August 1, 1984, H makes a qualified subchapter S trust election (hereinafter in this paragraph referred to as QSST election) with respect to Corporation Q that becomes effective as of July 1, 1983. Accordingly, as of July 1, 1983, the trust is a qualified subchapter S trust that is treated as a subpart E trust and H is treated as the shareholder for purposes of section 1361(b)(1).

(ii) Assume the same facts as in example (4)(i), and further assume that, for the taxable year ending on December 31, 1983, the trust does not distribute all its income currently. As of January 1, 1984, the trust ceases to be a qualified subchapter S trust and the trust is no longer treated as a subpart E trust. Thus, the trust is considered to be the shareholder as of that date for purposes of section 1361(b)(1), and Corporation Q ceases to be an S corporation as of that date because the trust is an ineligible shareholder.

(iii) Assume the same facts as in example (4)(i) except that H dies on November 1, 1983, and that I and J become income beneficiaries of the trust after H's death. The trust ceases to be a qualified subchapter S trust as of that date because it has more than one current income beneficiary. For the 60-day period beginning on November 1, 1983, H's estate (and not the trust) is considered to be the shareholder for purposes of section 1361(b)(1) because the trust ceases to be treated as a subpart E trust upon H's death. See section 1361(c)(2)(A)(ii).

Example (5). On January 1, 1983, stock of Corporation R, a calendar year S corporation, is transferred to a trust that satisfies all the requirements to be a qualified subchapter S trust. The terms of the trust do not preclude the current income beneficiary, K, from assigning his income interest in the trust. K files in January 1983 a QSST election that is effective as of January 1, 1983. On July 1, 1983, K assigns his income interest in the trust to a person not named in the trust instrument. The assignee is treated as a current income beneficiary for purposes of determining whether the trust still qualifies as a qualified subchapter S trust. Because the assignee's income interest will terminate on K's death (rather than the assignee's), the trust does not meet the requirement set forth in section 1361(d)(3)(A)(iii). Accordingly, the trust ceases as of the date of the assignment to be a qualified subchapter S trust, and Corporation R ceases to be an S corporation as of the same date.

Example (6). Assume that the terms of a trust provide for termination of the trust only upon the death of the current income beneficiary. Although the terms of the trust fail to explicitly provide for the distribution of trust assets to the current income beneficiary upon termination of the trust during the life of the current income beneficiary, the requirement of section 1361(d)(3)(A)(iv) is met because the trust agreement precludes the possibility that the trust will terminate during the life of the current income beneficiary.

Example (7). On January 10, 1983, C transfers to a trust his shares of stock in Corporation S, a C corporation. C is the holder of the remainder interest and D, who is 13 years old, is the sole income beneficiary of the trust. The trust instrument provides that the trust shall terminate when D is 21 years old. The terms of the trust satisfy all the requirements to be a qualified subchapter S trust except the requirement of section 1361(d)(3)(A)(iv) that, upon termination of the trust during the life of the current income beneficiary, the corpus must be distributed to that income beneficiary. On February 10, 1983, C makes a gift of his remainder interest to D. Accordingly, as of February 10, 1983, the terms of the trust satisfy the requirement specified in section 1361(d)(3)(A)(iv) and the trust is a qualified subchapter S trust.

Example (8). (i) On January 1, 1983, stock of Corporation T, a calendar year corporation with 10 shareholders, is transferred to a trust that satisfies all the requirements to be a qualified subchapter S trust. On January 31, 1983, Corporation T files an election to be an S corporation that is to be effective for the taxable year beginning on January 1, 1983. In order for the election to be effective for that taxable year, the QSST election must be effective as of January 1, 1983, and must be filed within the period beginning on January 1, 1983, and ending on March 16, 1983 (*i.e.*, the 16-day-and-2-month period beginning on the first day of the first taxable year for which the election to be an S corporation is effective).

(ii) Assume the same facts as in example (9)(i) except that the election to be an S corporation is filed on April 1, 1983 (*i.e.*, it is filed after the 15th day of the 3rd month of the first taxable year for which its is to be effective but before the end of that taxable year). Although the election to be an S corporation is not timely filed for the 1983 taxable year, section 1362(b)(3) provides that the election is to be treated as made for the taxable year beginning on January 1, 1984. In order for that election to be effective for the 1984 taxable year, it must be valid when made. Thus, the QSST election must be filed within the 16-day-and-2-month period beginning on April 1, 1983, and ending on June 16, 1983 (and the election must state that it is to be effective on April 1, 1983).

(iii) Assume the same facts as in example (9)(i) except that the QSST election is filed on April 15, 1983 (*i.e.*, the 15th day of the 3rd month after the date on which the corporation makes the election to be an S corporation). Because the QSST election is not effective as of the beginning of Corporation T's 1983 taxable year, the election to be an S corporation is not valid for 1983. In that case, section 1362(b)(2) provides that the election to be an S corporation is to be treated as made for the taxable year beginning on January 1, 1984. Since the QSST election is filed within the 16-day-and-2-month period beginning on January 31, 1983, the date on which the corporation makes the election to be an S corporation, the election to be an S corporation is effective for the taxable year beginning on January 1, 1984 (provided the QSST election states that it is to be effective as of January 31, 1983, which is the date of the election to be an S corporation).

(k) *Application*. The rules contained in paragraphs (e)(2) and (h)(1) of this section apply solely for purposes of determining whether a corporation qualifies as a small business corporation. Thus, for example, the rules contained in paragraph (h)(1) of this section may not apply to determine who is a shareholder for purposes of section 1366 (*i.e.*, to whom the items of income, loss, deduction, or credit of the corporation are to be distributed).

(l) *Single class of stock.* [Reserved]

Roscoe L. Egger, Jr.
Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on October 6, 1986, 8:45 a.m., and published in the issue of the Federal Register for October 7, 1986, 51 F.R. 35659)

Transfers of Property by U.S. Persons to Foreign Corporations—Public Hearing

Announcement 86–106

SUMMARY: This document provides notice of a public hearing on proposed regulations relating to transfers of property by U.S. persons to foreign corporations.

DATES: The public hearing will be held on Monday, December 1, 1986, beginning at 10:00 a.m. Outlines of oral comments must be delivered or mailed by Monday, November 17, 1986.

ADDRESS: The public hearing will be held in the I.R.S. Auditorium, Seventh Floor, 7400 Corridor, Internal Revenue Building, 1111 Constitution Avenue, N.W., Washington, D.C. The requests to speak and outlines of oral comments should be submitted to the Commissioner of Internal Revenue, Attn: CC:LR:T (LR–3–86 or INTL–610–86), Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: B. Faye Easley of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, telephone 202–566–3935 (not a toll-free call).

SUPPLEMENT INFORMATION: The subject of the public hearing is proposed regulations under sections 367 and 6038B of the Internal Revenue Code of 1954. The proposed regulations appeared in the FEDERAL REGISTER for Friday, May 16, 1986 (51 FR 17990).

The rules of §601.601(a)(3) of the "Statement of Procedural Rules" (26 CFR Part 601) shall apply with respect to the public hearing. Persons who have submitted written comments within the time prescribed in the notice of proposed rulemaking and who also desire to present oral comments at the hearing on the proposed regulations should submit, not later than Monday, November 17, 1986, an outline of oral comments to be presented at the hearing and the time they wish to devote to each subject.

Each speaker will be limited to 10 minutes for an oral presentation exclusive of the time consumed by questions from the panel for the government and answers to these questions.

Because of controlled access restrictions attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after outlines are received from the speakers. Copies of the agenda will be available free of charge at the hearing.

By direction of the Commissioner of Internal Revenue:

D. Kevin Dolan
Associate Chief Counsel
(International).

(Filed by the Office of the Federal Register on October 9, 1986, 8:45 a.m., and published in the issue of the Federal Register for October 10, 1986, 51 F.R. 36409)

Amendment of Temporary Income Tax Regulations Under Section 338(h)(10)

Announcement 86–107

The Temporary Income Tax Regulations under section 338(h)(10) of the Internal Revenue Code will soon be amended to require use solely of the MADSP formula for determination of deemed sale price.

In general, if a corporation makes a qualified stock purchase of the stock of a target corporation from a group of affiliated corporations that files a consolidated return, the parties to the transaction may jointly make a section 338(h)(10) election. If this election is made, the target is deemed to have sold all its assets in a fully taxable transaction and thereafter to have liquidated. Section 1.338(h)(10)–1T(f) of the temporary regulations, published in the Federal Register on January 8, 1986 (T.D. 8068 1986–1 C.B. 165), generally provides that the price at which target is deemed to have sold each asset is its fair market value. Alternatively, the deemed sale price of each asset may be calculated by use of an elective formula ("the MADSP formula"), pursuant to which the deemed sale price of each asset is a proportionate share of an amount determined by reference to the actual purchase price of the target stock. The temporary regulations were amended, generally effective July 1, 1986 (T.D. 8092, 1986–36 I.R.B. 5), to require that, if the MADSP formula is used to calculate the deemed sale price of all assets, the MADSP amount must be allocated to each of the assets pursuant to the residual method of allocation.

The temporary regulations, as amended July 1, 1986, will be further amended to mandate use of the MADSP formula to determine the deemed sale price for qualified stock purchases for which the acquisition date is on or after November 10, 1986, unless the acquisition occurs pursuant to a binding contract entered into before that date.

Annoucement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practible for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
S. Melvin Apotheker	Miami, FL	Attorney	Indefinite from September 1, 1986
Sandra S. Behn	London, TN	Certified Public Accountant	Indefinite from September 12, 1986
Charles K. Hyter	Hutchinson, KS	Attorney	Indefinite from September 18, 1986
William Pyke	Dallas, TX	Certified Public Accountant	Eighteen Months from August 15, 1986
Alan Z. Richards	West Hempstead, NY	Attorney and Certified Public Accountant	Indefinite from September 20, 1986

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to identify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
Paul Beecher	Torrance, CA	Indefinite effective September 25, 1986

Under 31 Code of Federal Regulations, Part 10, an enrolled agent, in order to avoid the institution of a proceeding for his disbarment of suspension from practice before the Internal Revenue Service, may offer his resignation. The Director of Practice, in his discretion, may accept the offered resignation of an enrolled agent.

To enable the public and other practitioners to identify such resigned enrolled agents, the Director of Practice will announce in the Internal Revenue Bulletin the name and address of each enrolled agent who has resigned and the effective date of resignation. This announcement will appear in the weekly Bulletin at the earliest practicable date after the action and will continue to appear in the weekly Bulletins for five successive weeks or for as many weeks as is practicable for each resigned enrolled agent, and will later be consolidated and published in the Cumulative Bulletin.

The following individual has entered a consent resignation from enrollment to practice before the Internal Revenue Service:

Name of Enrolled Agent	Address	Effective Date of Resignation
William E. Bonafede	Wakefield, RI	September 30, 1986

Under Section 330, Title 31 of the United States Code, the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
James L. Ketner	Charlotte, NC	Certified Public Accountant	September 27, 1986
George L. Weil	Orange, CT	Certified Public Accountant	September 27, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 51.4989–1, 51.4996–1, 51.4996–3 amended; 51.4996–4 added	Definition of "property" for purposes of the windfall profit tax	1986–42 I.R.B. 15	Nov. 11, 1986
26 CFR 51.4989–1 amended; 51.4996–1 revised; 51.4996–5 added	Windfall profit tax; production from a unitized property of imputed stripper well crude oil, imputed heavy crude oil, and imputed newly discovered crude oil	1986–43 I.R.B. 11	Dec. 1, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR— Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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1986-45

Bulletin No. 1986-45
November 10, 1986

Internal Revenue bulletin

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–129, page 4.

Investment credit; ACRS; computer; employee. A taxpayer's use of a computer at home does not meet the "required as a condition of employment" requirement of section 280F(d)(3)(A) of the Code in the factual circumstances set forth. Thus, none of the taxpayer's use of the computer is treated as use in a trade or business. Therefore, the taxpayer is not allowed any investment credit or recovery deduction for the computer.

EMPLOYEE PLANS

Announcement 86–109, page 22.

In accordance with Section 12.02 of Rev. Proc. 84–23, set forth is a list of master or prototype plans closed by the National Office of the Internal Revenue Service as of September 30, 1986.

EXCISE TAXES

Rev. Rul. 86–130, page 5.

Trucks; glider kit; tax-bases. Tax bases are provided in 3 situations in which a truck tractor is overhauled through the use of a "glider kit."

ADMINISTRATIVE

Rev. Proc. 86–41, page 7.

Controlled corporation; stock and securities distribution; revised checklist for ruling request. A revised checklist sets forth the information and representations to be included in a request for a ruling under section 355 of the Code with respect to distributions of stock and securities of a controlled corporation. Rev. Proc. 81–41 superseded.

Rev. Proc. 86–42, page 12.

Reorganizations; standard representations for ruling requests. Standard representations to be included in a request for a ruling under section 368 of the Code with respect to acquisitive corporate reorganizations are set forth. Rev. Proc. 77–37 amplified.

Announcement 86–108, page 20.

Guidance is provided to taxpayers who may wish to pay actual or contested tax deficiencies in 1986 in order to assure that interest paid on such deficiencies will be fully deductible on their 1986 returns.

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Finding Lists begin on page 35.
Announcement of Disbarments and Suspensions begin on page 31.
Announcement of Notice of Proposed Rulemaking on page 33.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 280F.—Limitation On Investment Tax Credit and Depreciation For Luxury Automobiles; Limitation Where Certain Property Used For Personal Purposes

26 CFR 1.280F-6T: Special rules and definitions.

Investment credit; ACRS; computer; employee. A taxpayer's use of a computer at home does not meet the "required as a condition of employment" requirement of section 280F(d)(3)(A) of the Code in the factual circumstances set forth. Thus, none of the taxpayer's use of the computer is treated as use in a trade or business. Therefore, the taxpayer is not allowed any investment credit or recovery deduction for the computer.

Rev. Rul. 86–129

ISSUE

If under the circumstances described below, an employee taxpayer cannot practically perform the tasks required by the taxpayer's job without the assistance of a computer and the employee often performs work at home, then is the use of a personal computer in the taxpayer's home "required as a condition of employment" under section 280F(d)(3)(A) of the Internal Revenue Code? If not, is the taxpayer therefore denied any recovery deduction otherwise allowable with respect to the computer?

FACTS

A, an individual, is employed by *X*, a corporation. *X* conducts a significant amount of research and development. *A*, who has a doctorate in aerospace engineering, performs research for *X*. *A*'s job description, like the job descriptions of all engineers and scientists employed by *X*, provides that *A* will seek to accomplish the research objectives of *X* by whatever means *A* and *X* determine are necessary. These professional employees of *X* use personal computers provided by *X* in all aspects of the company's research and development activities, and many of their tasks cannot practically be performed without the assistance of a computer.

A purchased a computer and kept it at home. *A* purchased it because the computers at *X* are often being used by other employees during working hours, and *A* often performs work for *X* at home. No portion of *A*'s home meets the requirements of section 280A(c)(1) of the Code, which concerns business use of a dwelling unit. The computer is used exclusively by *A* in connection with the performance of services for *X*. *X* provided *A* with a written statement indicating that *X* required *A*, as a condition of *A*'s employment, to purchase the computer.

LAW AND ANALYSIS

Section 280F(b)(1) of the Code disallows the investment tax credit, and section 280F(b)(2) of the Code disallows the use of accelerated percentages under the accelerated cost recovery system (ACRS) when the credit and the use of the accelerated percentages are attributable to listed property that is not predominantly used in a qualified business use for a taxable year.

Section 280F(d)(3)(A) of the Code provides that, for purposes section 280F, any employee use of listed property will not be treated as use in a trade or business for purposes of determining the amount of any investment credit allowable under section 38 to the employee or any recovery deduction allowable to the employee unless the use of the property is for the convenience of the employer and required as a condition of employment.

Section 1.280F–6T(a)(1) of the Temporary Income Tax Regulations provides that employee use of listed property will not be treated as business/investment use for purposes of determining the amount of any credit allowable under section 38 of the Code to the employee or the amount of any recovery deduction allowable to the employee unless that use is for the convenience of the employer and required as a condition of employment.

Section 1.280F–6T(a)(2)(ii) of the temporary regulations provides that in order to satisfy the "condition of employment" requirement, the use of the property must be required in order for the employee to perform the duties of employment properly. Thus, the employer need not explicitly require the employee to use the property. Similarly, a mere statement by the employer that the use of the property is a condition of employment is not sufficient.

Section 280F(d)(3)(B) of the Code provides that the term "employee use" means any use in connection with the performance of service as an employee.

As defined in section 280F(d)(4) of the Code, generally, the term "listed property" includes any computer or peripheral equipment (as defined in section 168(j)(5)(D)). However, pursuant to section 280F(d)(4)(B), the term "listed property" does not include any computer or peripheral equipment used exclusively at a regular business establishment. For purposes of the preceding sentence, any portion of a dwelling unit is a regular business establishment if and only if the requirements of section 280A(c)(1) are met with respect to that portion.

Since the portion of *A*'s home where the personal computer is used does not meet the requirements of section 280A(c)(1) of the Code, the computer is "listed property." As such, it is not eligible for *any* investment tax credit, or *any* recovery deduction, otherwise allowable to *A* unless *A*'s use of the property is for the convenience of A's employer and is required as a condition of employment. Section 1.280–6T(a)(1) of the temporary regulations.

Congress' intent when it included the phrase "for the convenience of the employer and required as a condition of employment" in section 280F(d)(3)(A) of the Code is set out in the conference report as follows:

> Listed property which an individual owns in connection with his employment is eligible for the investment credit and ACRS deductions only if such property is required for the convenience of the employer and as a condition of employment. The conferees intend the terms "convenience of the employer" and "condition of employment" to have the same meaning with respect to this provision as it [*sic*] does with respect to the exclusion from gross income for lodging furnished to an employee. In order to satisfy the condition of employment requirement the property must be required in order for an employee to properly perform the duties of his employment. This requirement is not satisfied merely by an employer's statement that the property is required as a condition of employment. The conferees intend that the principles of *Dole v. Commissioner*, 43 T.C. 697, *aff'd.*, 351 F.2d 308, (1st Cir. 1965) apply.

H.R. Rep. No. 98–861 (Conf. Rep.), 98th Cong., 2d Sess. 1027 (1984), 1984–3 (Vol. 2) C.B. 1, 281. *See also* section 1.280F–6T of the temporary regulations.

In *Dole*, the United States Tax Court was faced with the question of whether three key employees of a woolen mill could exclude from gross income the value of houses provided by the employer. The houses were located 1 mile from the mill and were required by the employer to be occupied by the employees so that those employees were readily available in the event of an emergency at the mill. The court noted that there was no available lodging closer to the mill than that provided by the employer but that there was other available lodging located within 3 miles of the mill.

In holding that the rental value of the lodging provided to the employees was not excludable from gross income because the lodging did not meet the "condition of employment" test under section 119 of the Code, the court stated, at pages 705–706:

> We need to go no farther than the first requirement of the statute to decide, on the facts of these proceedings, that the petitioners were *not* required to accept the lodging provided by their employer in order to enable them to perform properly the duties of their employment. Merely because [the president of the employer company] insisted that petitioners occupy the company-owned houses to help promote the efficient operation of the mill does not, standing alone, mean that the statutory standard—required to accept such lodging as a condition of employment—is met. The standard prescribed by Congress is not subjective. It is objective. The employer's state of mind is not controlling. [Emphasis in the original].

Aside from the statement of the employer, there are no facts in the present situation that indicate the use of the computer at home by *A* is required for *A* to perform properly the duties of *A*'s employment. *A* can more easily and efficiently perform the duties of employment using the home computer, just as the employees in *Dole* would have been more readily available in the case of emergencies living in the employer-provided housing. However, as noted by the court in *Dole*, the fact that the property will enable the employee to more easily and efficiently perform the duties of employment does not mean the use of the property is required as a condition of employment. In order to satisfy the requirement that a home computer is required as a condition of employment there must be a clear showing that the employee cannot perform properly the duties of employment without it. That clear showing is lacking in this situation because there is no evidence that the computers supplied by *X* are insufficient to enable *A* properly to perform the duties of *A*'s employment.

HOLDING

The use of the home computer by *A* is not required as a condition of employment within the meaning of section 280F(d)(3)(A) of the Code. Therefore, under section 280F(d)(3) and section 1.280F–6T(a)(1) of the temporary regulations, none of *A*'s use of the computer is treated as use in a trade or business. Thus, *A* is not allowed any investment credit or recovery (depreciation) deduction for the computer. The straight line recovery method under section 280F(b)(2) also is not allowed because, under section 280F(d)(3) and section 1.280F–6T(a)(1) of the temporary regulations, *A* is treated as having no business use of the computer.

Section 355.—Distribution of Stock and Securities of a Controlled Corporation

26 CFR 1.355–1: Distribution of stock and securities of controlled corporation.

Checklist (questionnaire) with regard to information to be included in a request for a letter ruling under section 355 of the Code. See Rev. Proc. 86–41, page 7.

Section 368.—Definitions Relating to Corporate Reorganizations

26 CFR 1.368–1: Purpose and scope of exception of reorganization exchanges.

Standard representations for inclusion in requests for letter rulings regarding acquisitive reorganizations described in section 368 of the Code. See Rev. Proc. 86–42, page 12.

Section 4052.—Definitions and Special Rules

26 CFR 145.4052–1: Special rules and definitions.

Trucks; glider kit; tax-basis. Tax bases are provided in 3 situations in which a truck tractor is overhauled through the use of a "glider kit."

Rev. Rul. 86–130

ISSUE

If, in the situations described below, truck tractors are refurbished by use of a "glider kit" and other new components, are the refurbished truck tractors subject to the retailers excise tax imposed by section 4051(a)(1) of the Internal Revenue Code? If so, what is the tax base in each situation?

FACTS

Situation 1. A truck dealer receives a used highway truck tractor in a trade-in, overhauls it, and resells the overhauled truck tractor at retail. In the overhaul, a set of unassembled new parts commonly known as a "glider kit" is combined with other new components and with the retained used components.

A glider kit usually consists of a cab, fenders, dash instruments, wiring, steering wheel, steering gear, seats, chassis frame, front axle, and copper tubing for the brake system.

Situation 2. The owner of a used highway truck tractor purchases a glider kit and other new components and overhauls the truck tractor as in *Situation 1.* The owner then uses the overhauled vehicle in the operation of its business. The owner does not regularly sell such truck tractors at retail in arm's length transactions.

Situation 3. The owner of a used highway truck tractor delivers the vehicle to an unrelated truck repair shop for overhaul. The repair shop purchases a glider kit and other new components for incorporation into the truck tractor, overhauls the truck tractor, and delivers it to the owner for use in the operation of its business. The repair shop bills the owner for the completed overhaul operation. The owner does not regularly sell such truck tractors at retail in arm's length transactions.

LAW AND ANALYSIS

Section 4051(a)(1) of the Code imposes on the first retail sale of certain enumerated automotive articles (including in each case parts or accessories sold on or in connection therewith or with the sale thereof) a tax of 12 percent of the amount for which the article is so sold. Included among those articles are tractors of the kind chiefly used for highway transportation in combination with a trailer or semitrailer. The term "first retail sale" is defined in section 4052(a)(1) to mean the first sale, for a purpose other than for resale, after manufacture, production, or importation.

Section 4052(a)(3)(A) of the Code provides that, in general, if any person uses an article taxable under section 4051 before the first retail sale of such article, then that person shall be liable for tax under section 4051 in the same manner as if such article were sold at retail by the person.

Section 4052(a)(3)(C) of the Code provides that in the case of any person made liable for tax by section 4052(a)(3)(A), the tax shall be computed on the price at which similar articles are sold at retail in the ordinary course of trade, as determined by the Secretary.

Section 145.4052–1(c)(5)(ii) of the Temporary Excise Tax Regulations provides that if the seller of an article regularly sells such articles at retail in arm's length transactions, tax liability on its use of any such article shall be computed on its lowest established retail price for such articles in effect at the time of the taxable use. In establishing such price, there shall be included and excluded, as applicable, the charges and readjustments specified in sections 4216(a), 4216(f), and 6416(b)(1) of the Code as in effect at the time the tax liability on the use of the article is incurred. If the seller of an article does not regularly sell such articles at retail in arm's length transactions, a constructive price on which the tax shall be computed will be determined by the Commissioner. This price will be established after considering the selling practices and price structures of sellers of similar articles.

Section 4052(b)(1)(B)(iv) of the Code provides that in determining price for purposes of the retailers excise tax, there will be excluded the value of any component of such article if (1) the component is furnished by the first user of the article, and (2) such component has been used before such furnishing.

Section 48.0–2(a)(4)(i) of the Manufacturers and Retailers Excise Tax Regulations provides that the term "manufacturer" includes a person who produces a taxable article from scrap, salvage, or junk material, as well as from new or raw material, (1) by processing, manipulating, or changing the form of an article, or (2) by combining or assembling two or more articles.

Section 48.0–2(a)(4)(ii) of the regulations provides that, under certain circumstances, as where a person manufactures or produces a taxable article for another person who furnishes materials under an agreement whereby the person who furnished the materials retains title thereto and to the finished article, the person for whom the taxable article is manufactured or produced, and not the person who actually manufactures or produces it, will be considered the manufacturer.

Rev. Rul. 71–584, 1971–2 C.B. 358, which dealt with the now repealed manufacturers excise tax on trucks under section 4061(a)(1) of the Code, concerned the assembly of a truck tractor by a company for its own use, by combining a glider kit with salvaged parts from a used truck tractor removed from the company's own fleet. The revenue ruling concluded that the assembly of the glider kit and used components was an act of production or manufacture of an article taxable under section 4061(a)(1). That conclusion was based on the definition of the term "manufacturer" set forth in section 316.4(a) of Regulations 46 (made applicable to the 1954 Code by Treasury Decision 6091, 1954–2 C.B. 47). That definition is the same as the definition of "manufacturer" now found in section 48.0–2(a)(4)(i) of the regulations.

Thus, under section 48.0–2(a)(4)(i) of the regulations, an act of manufacture has occurred in the three situations described above. That act of manufacture results in the production of a new truck tractor that is subject to the tax imposed by section 4051(a)(1) of the Code upon the first sale at retail or the first use before a retail sale.

In *Situation 1*, the dealer is liable for tax under section 4051(a)(1) of the Code on its sale of the refurbished truck tractor at retail. In determining the taxable selling price of the vehicle, the dealer may not invoke section 4052(b)(1)(B)(iv) to exclude the value of the used components because the used components were not furnished by the first user of the new article, the dealer's vendee.

In *Situation 2*, the owner is liable for tax upon its use of the refurbished truck tractor in its business. The owner does not regularly sell such truck tractors at retail in arm's length transactions within the meaning of section 145.4052–1(c)(5)(ii) of the temporary regulations. Accordingly, the tax must be computed on a constructive price determined by the Commissioner. After consideration of the selling practices and price structures of sellers of refurbished truck tractors, the Commissioner has determined that the constructive sale price upon which tax is to be computed is the cost to the owner of all the components used by the owner in the manufacturing operation plus an amount equal to 150 percent of the owner's labor costs (including overhead) in the manufacturing operation. Unlike *Situation 1*, the person furnishing the used components, the owner, is the first user of the new article. Thus, under section 4052(b)(1)(B)(iv) of the Code, the owner may exclude the value of any used components furnished by the owner and incorporated into the new truck tractor. Where the owner believes that facts and circumstances justify using a markup rate of less than 150 percent, a specific ruling may be sought from the Internal Revenue Service. *See* Rev. Rul. 54–490, 1954–2 C.B. 416.

In *Situation 3*, as in *Situation 2*, the owner is liable for tax on its first use of the refurbished truck tractor in its business. Here again, the owner does not regularly sell such truck tractors at retail in arm's length transactions. Where the owner of the used truck tractor contracts with a repair shop to perform the overhaul operation, the Commissioner has determined that the constructive sale price upon which tax is to be computed is the amount the repair shop bills the owner for the completed overhaul operation, plus the cost of any new components furnished by the owner to the repair shop. As in *Situation 2*, since the owner is the first user of the new article, the value of any used components furnished by the owner to the repair shop and incorporated into the overhauled truck tractor is not included in the constructive sale price.

HOLDING

In *Situation 1*, the truck dealer has manufactured a taxable truck tractor and is subject tax under section 4051(a)(1) of the Code on its sale of the truck tractor. The tax is based on the sale price of the vehicle with no exclusion for the value of used components incorporated into the manufactured vehicle.

In *Situation 2*, the truck tractor owner manufactured a truck tractor and is liable for tax under section 4052(a)(3)(A) of the Code on its use of the vehicle. The tax base on its use of the truck tractor is the cost to the owner of parts and accessories (exclusive of the value of used components supplied by the owner) plus 150 percent of the owner's labor costs (including overhead) incurred in manufacturing the truck tractor.

In *Situation 3*, the owner of the truck tractor is considered to have manufactured a truck tractor and is liable for tax under section 4052(a)(3)(A) of the Code on its use of the vehicle. The truck tractor owner's tax base is the total cost to the owner for the manufacture of the truck tractor (exclusive of the value of used components supplied by the owner).

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.201: Rulings and determination letters.
(Also Part I, Section 355; 1.355–1.)

Rev. Proc. 86–41

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SECTION 1. PURPOSE

The purpose of this revenue procedure is to update Rev. Proc. 81–41, 1981–2 C.B. 605, which sets forth in a checklist questionnaire the information that must be included in a request for a ruling under section 355 of the Internal Revenue Code, relating to the nonrecognition of gain or loss on distributions of stock and securities of controlled corporations.

SEC. 2. BACKGROUND

The Internal Revenue Service receives many requests for rulings in which the information relating to the proposed transaction is not sufficient to permit a determination to be made. In those cases, it is necessary to obtain additional facts from the taxpayer before the request for a letter ruling can be considered. Obtaining these additional facts is time consuming for both Service personnel and taxpayers and delays issuance of the ruling letter.

This checklist will facilitate the filing and processing of requests for rulings under section 355 of the Code by showing specific information and representations to be included so that the requests will be as complete as possible when initially filed. Because the information and representations necessary to rule on a particular transaction depend upon all the facts and circumstances, information or representations in addition to those set forth in this revenue procedure may be required.

The authority and general procedures of the National Office of the Internal Revenue Service and of the Office of the District Directors of Internal Revenue with respect to the issuance of letter rulings and determination letters are outlined in Rev. Proc. 86–1, 1986–1 C.B. 395. See also Rev. Proc. 86–3, 1986–1 C.B. 416, relating to areas in which advance rulings generally will not be issued. These revenue procedures, along with the present checklist revenue procedure, are subject to periodic updating by the Service. Therefore, careful attention should be given to ensure usage of the most current revenue procedures.

Careful attention to all requirements of these revenue procedures will aid in the timely processing of letter ruling requests.

SEC. 3. CHANGES

.01 Section 1 is modified to indicate that the purpose of the revenue procedure is to update Rev. Proc. 81–41.

.02 Section 2 is modified to state that representations are now required, and to update references to revenue procedures cited.

.03 Section 4 is substantially altered. The taxpayer must now submit standard representations using the precise language specified herein, or submit an explanation why the representations cannot be made in the requested form. Sections 4.023, 4.024, 4.034, 4.035, 4.036, 4.051, 4.052, 4.055, and 4.06 are modified accordingly. To properly reflect applicable changes, some citations to Code sections and to revenue rulings and procedures have been added or deleted. Changes include:

1. Section 4.012 now requires taxpayers to submit information concerning any prior ruling requests submitted by the taxpayer (or predecessor) that were withdrawn in which the identical or similar issue was present.

2. Section 4.02 now indicates more precisely the information required regarding ownership interests in Distributing and Controlled.

3. Sections 4.031, 4.032, 4.033, 4.034, and 4.035 now deal with the active business issue in greater detail, including a request for separate employee information for different active businesses and a request for the percent of activities performed by independent contractors.

4. Section 4.036 now contains a centralized request for financial information, including pro forma balance sheets and profit and loss statements for each active business of Distributing, Controlled, and Other Corporations.

5. Section 4.04 now indicates more precisely the information required regarding business purpose. Included is a list of revenue rulings showing factual situations in which the Service has found a valid business purpose. It is emphasized that in some instances third party documentation may be essential in substantiating the business purpose.

6. Section 4.056(a) and (b) has been added to request information concerning investment and inactive assets held by Distributing and Controlled following the transaction.

7. Section 4.06 has been added to reference Rev. Proc. 77–37 for a continuity of equity interest representation, if shareholders are disposing of their stock.

8. Section 4.07 requests certain general information and now includes a cross reference to the information and statements required for all ruling requests pursuant to Rev. Proc. 86–1 and requires taxpayers to list the specific rulings being requested and the authorities supporting the rulings.

.04 Section 5 is modified to substitute Associate Chief Counsel (Technical) for Assistant Commissioner (Technical) and CC:C:R for T:C:R.

.05 Section 6 is modified to state that Rev. Proc. 81–41 is superseded.

SEC. 4. INFORMATION TO BE INCLUDED IN REQUESTS FOR RULINGS UNDER SECTION 355 OF THE CODE

Each of the items in this section should be specifically dealt with in the letter ruling request. If an item is not applicable, so state and briefly explain why. Standard representations are set forth throughout this section and are highlighted by the word "representation" in boldface type. These representations are of equal importance with the other factual information requested herein. The representations function to ensure that specific statutory and judicial requirements and administrative ruling guidelines are satisfied. Each representation set forth in this section should be submitted precisely in the language requested. If a representation cannot be submitted as requested, an explanation must be given. Variations of the language of the representations may delay processing the ruling request and will not be accepted unless reasons satisfactory to the Service are submitted. Submission of the information and representations should follow the format of this revenue procedure as closely as possible, with appropriate descriptive headings. Care must be taken to ensure that all the facts relating to the transaction are submitted.

.01 *Information regarding the distributing corporation (Distributing) and the corporation or corporations whose stock and securities are distributed (Controlled).*

1. Identification.—Name, taxpayer identification number, and place and date of incorporation of Distributing and Controlled.

2. Jurisdiction.—Identify the District Office that will have audit jurisdiction over the return of Distributing (referred to below as "taxpayer") and of Controlled(s). State whether, to the best knowledge of the taxpayer and the taxpayer's representatives, if any, the identical issue is in a return of the taxpayer (or of a related taxpayer within the meaning of section 267 of the Code, or a member of an affiliated group of which the taxpayer is also a member within the meaning of section 1504) and, if so, whether the issue (1) is being examined by a District Director, (2) has been examined by a District Director and (a) the statutory period of limitation either on assessment or for filing a claim for refund or credit of tax has not expired, and (b) a closing agreement covering the issue or liability has not been entered into by a District Director, (3) is being considered by an Appeals Office in connection with the taxpayer's return for an earlier period, (4) has been considered by an Appeals Office and (a) the statutory period of limitation either on assessment or for filing a claim for refund or credit of tax has not expired and (b) a closing agreement covering the issue or liability has not been entered into by an Appeals Office, or (5) is pending in litigation in a case involving the taxpayer or a related taxpayer. The request must contain a statement whether, to the best knowledge of the taxpayer and the taxpayer's representatives, the identical or a similar issue has been (i) submitted to the Service, but withdrawn before a ruling was issued, or (ii) ruled on by the Service to the taxpayer

or the taxpayer's predecessor and, if so, when and with what result. If, after the request is filed but before a ruling is issued, the taxpayer knows that an examination of the issue by a District Director has been started, the taxpayer must notify the National Office of this action. If a return is filed before a ruling is received from the National Office concerning the issue that is the subject of the request for ruling, a copy of the request must be attached to the return. This alerts the District Office and avoids premature District action on the issue.

3. Taxable year.—State the last day of the taxable year of Distributing and Controlled.

.02 *Ownership of interests in Distributing and Controlled.*

1. Stock in Distributing immediately prior to the distribution.—Provide a complete description of each class of Distributing's outstanding stock (throughout this document the word "stock" includes all forms of equity ownership) setting forth the rights and privileges of each class, including voting on nonvoting rights, dividend and liquidation preferences or limitations, and whether classified as common or preferred stock. State the number of shares and the percentage of each class of stock owned by each shareholder of Distributing prior to the distribution. However, if there are more than 25 shareholders, the statement in the preceding sentence may be limited by listing only those shareholders owning 5 percent or more of any class of stock, and then stating the total number of other shareholders together with the total number of shares and percentages which these other shareholders own of each class of stock. List all shareholders owning five percent or more of any class of stock who are foreign persons.

2. Capital Structure of Controlled immediately prior to the distribution.—Furnish a complete description of each class of Controlled's outstanding stock setting forth the rights and privileges of each class, including voting or nonvoting rights, dividend and liquidation preferences or limitations, and whether classified as common or preferred stock. Also describe all other outstanding interests (bonds, debentures, notes, warrants, options, etc.), and briefly explain why each of these items should or should not be considered a stock interest. State the number of shares and the percentage of each class of stock in Controlled owned by Distributing. If there are minority shareholders of Controlled, furnish information with respect to these shareholders similar to the information requested under section 4.021 above.

3. Description of stock, securities, and other property being distributed.

(a) Stock.—State the number of shares of each class of stock in Controlled being distributed. In addition, if preferred stock is distributed and it is contended that this stock is not "section 306 stock," within the meaning of section 306(c) of the Code, fully explain the reasons for this contention.

(b) Securities.—State the principal amount of each series of securities of Controlled being distributed.

(c) Other property.—State the amount and provide full particulars as to any property, other than stock and securities of Controlled, being distributed by Distributing including, but not limited to, cash and stock rights or warrants (see section 1.355–2(a) of the Income Tax Regulations). Submit the following REPRESENTATION: *The distributing and controlled corporations and their respective shareholders will each pay their own expenses, if any, incurred in connection with the transaction.*

(d) Timing.—State the date of the transaction and whether all the stock, securities, and other property is being distributed on that date. If all the stock, securities, and other property is not distributed on the same date, state the approximate length of the delay and the reasons for the delay in distribution.

4. Ownership of stock and securities immediately after the distribution.

(a) Interests in Controlled held by Distributing.

(1) Retention of stock or securities.—State the number of shares of each class of stock in, or the principal amount of each series of securities of, Controlled held by Distributing subsequent to the distribution, and the length of time Distributing will hold this interest.

(2) Issuance of debt.—State whether Controlled intends to issue debt instruments to Distributing after the distribution. If so, submit copies of the instruments or, if copies are not available, provide full particulars as to the principal amounts, terms, and reasons for the issuance.

(3) Purpose for Distributing holding a stock or security interest in Controlled.—If subsequent to the distribution, Distributing will hold a stock or security interest in Controlled, submit a detailed explanation of the purpose and why this should not be viewed as in pursuance of a plan having as one of its principal purposes the avoidance of federal income tax. See section 1.355–2(d) of the regulations.

(b) Interests in Controlled held by shareholders of Distributing.

(1) Pro rata.—State whether the distribution of Controlled stock is pro rata with respect to all the shareholders of Distributing. If so, fully describe the details of the transaction.

(A) Ownership.—Set forth the number of shares and the percentage of each class of stock outstanding in Distributing and Controlled to be owned by each shareholder immediately after the distribution. If there are more than 25 shareholders, see section 4.021 above for the information to be provided.

(B) Securities.—Identify any shareholders of Distributing receiving securities of Controlled and state the principal amount of each series of securities being received. With respect to each shareholder, state the principal amount of each series of Distributing securities being exchanged therefor, or, if no securities are being exchanged, so state. See section 1.355–2(e)(1) of the regulations.

(2) Non pro rata.—State whether the distribution of Controlled stock is non pro rata with respect to the shareholders of Distributing. If so, fully describe the details of the transaction.

(A) Ownership.—Set forth the number of shares and the percentage of each class of stock outstanding in Distributing and Controlled that each shareholder owns immediately after the distribution. If there are more than 25 shareholders, see section 4.021 above for the information to be furnished.

(B) Values.—Submit the following REPRESENTATION: *The fair market value of the controlled corporation stock and other consideration received by each shareholder of the distributing corporation approximately equals the fair market value of the distributing corporation stock surrendered by the shareholder in the exchange.*

(C) Securities.—Identify any shareholders of Distributing receiving securities of Controlled, and state the principal amount of each series of securities being received. With respect to each shareholder, state the principal amount of each series of securities of Distributing being surrendered in the transaction, or if no securities are being exchanged, so state.

of the Code). In addition, if Distributing or Controlled is not directly engaged in an Active Business, submit the following REPRESENTATION: *Following the transaction, at least 90 percent of the fair market value of the gross assets of [the corporation so indirectly engaged] will consist of the stock and securities of controlled corporations that are engaged in the active conduct of a trade or business as defined in section 355(b)(2) of the Code.* See Section 3.04 of Rev. Proc. 77–37, 1977–2 C.B. 568, 570.

5. Five-year requirement.—Provide the following information with respect to each Active Business described in sections 4.031, 4.032, and 4.034 above, conducted by Distributing, Controlled, and Other Corporations.

(a) Continuous operation.—State which Active Businesses have been continuously conducted, within the meaning of section 1.355–1(c) of the regulations, by Distributing, Controlled, and Other Corporations, for the 5-year period immediately preceding the date of distribution. Give the date each Active Business was commenced or acquired. If, for any active business, the 5-year period includes any time during which there was no business activity, or a significant amount of time during which there was a substantial reduction in business activity, identify the period of time, the type and amount of business activity during this period, and the reasons for the cessation or reduction in activity. See Rev. Rul. 82–219, 1982–2 C.B. 82.

(b) Stock ownership.—Identify Controlled and Other Corporations whose shares have been continuously held by Distributing or Controlled for the 5-year period immediately preceding the date of distribution.

(c) Active business acquired by Distributing, Controlled, or Other Corporations during the preceding 5-year period.

(1) Identify.—Identify the party from whom the business was acquired and the party's relationship to Distributing or its shareholders.

(2) Date.—State the date the business was acquired and the period of time the business had been previously conducted by Distributing, Controlled, or Other Corporation's predecessor in interest.

(3) Transaction.—Describe the transaction in which the business was acquired: for example, acquired in a reorganization under section 368(a)(1) of the Code, acquired by purchase, etc. If a ruling letter was issued with respect to the transaction, submit a copy.

(4) Consideration.—State the consideration given in the acquisition.

(5) Gain or loss.—State whether gain or loss was recognized, in whole or in part, by any party to the transaction.

(d) Stock of Controlled or Other Corporations acquired by Distributing, Controlled, or Other Corporations during the precedng 5-year period.

(1) Identity.—Identify the party from whom the stock was acquired and that party's relationship to Distributing or its shareholders.

(2) Date and consideration.—State the date the stock was acquired and the consideration given in the acquisition.

(3) Transaction.—Describe the transaction in which the stock was acquired: for example, acquired in a reorganization under section 368(a)(1) of the Code, acquired by purchase, etc. State whether control was acquired as a result of Distributing transferring cash or other liquid or inactive assets to Controlled (see section 4.0120 of Rev. Proc. 86–3). If a ruling letter was issued with respect to the transaction, submit a copy.

(4) Gain or loss.—State whether gain or loss was recognized, in whole or in part, by any party to the transaction.

(e) Changes in ownership.—Provide complete details concerning any changes in ownership of the stock of Distributing, Controlled, and Other Corporations during the 5-year period preceding the distribution, including, but not limited to, acquisitions, redemptions, recapitalizations, stock dividends, and sales. Information regarding sales of stock in which the issuing corporation is not a party need not be provided, if (i) the sale occurs on a recognized stock exchange or in an established market, and (ii) both the purchaser and the seller hold less than five percent of the corporation's stock before and after the sale.

(f) Continued operations.—If the transaction involves the vertical division of a single business (See *Commissioner v. Coady*, 289 F.2d 490 (6th Cir. 1961), *aff'g* 33 T.C. 771 (1960)), submit the following REPRESENTATION: *Following the transaction, the distributing and controlled corporations will each continue independently and with their separate employees the active conduct of all the integrated activities of the business conducted by the distributing corporation prior to consummation of the transaction.* If the transaction involves the separation of two or more active businesses, submit the following REPRESENTATION: *Following the transaction, the distributing and controlled corporations will each continue the active conduct of their respective businesses, independently and with their separate employees.* Additionally, if, following the transaction, Distributing and Controlled share the services of certain employees identify these employees and specify the services performed and the compensation arrangements.

(g) Change in business.—Describe any substantial change in the type of business activity during the preceding 5-year period such as the adding of new or the dropping of old products, changes in production capacity, extraordinary purchases, replacements or sales of assets, and change of business location (see section 1.355–4(b)(3) of the regulations).

6. Financial statements.

(a) Information as to assets and liabilities associated with the Active Businesses of Distributing and Controlled.—

(1) Balance sheets.—Submit a copy of the most recent balance sheets of Distributing, Controlled, and Other Corporations. State whether any property is being transferred by Distributing to Controlled, whether any transferred property is subject to liabilities, and whether Controlled is assuming any liabilities in the transaction. If property is being transferred from Distributing to Controlled, a pro forma balance sheet should be submitted clearly showing all assets transferred to each Controlled and all liabilities assumed or to which the property transferred is subject. In addition, if Controlled is receiving assets or assuming liabilities, submit the following REPRESENTATIONS: *(1) The total adjusted basis and the fair market value of the assets transferred to the controlled corporation by the distributing corporation each equal or exceed the sum of the liabilities assumed by the controlled corporation plus any liabilities to which the transferred assets are subject;* and *(2) The liabilities assumed in the transaction and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.* (Alternatively, state why these representations cannot be made.)

(2) Continuing indebtedness.— Submit the following REPRESENTATION: *No intercorporate debt will exist between the distributing corporation and the controlled*

corporation at the time of, or subsequent to, the distribution of the controlled corporation stock. Alternatively, submit a full description of all debts existing between Distributing and Controlled. If any debt exists between Controlled, as debtor, and Distributing, as creditor, state whether such debt arose in connection with a transfer of assets by Distributing to Controlled and whether the debt resulted from Controlled's assumption of an intradivisional obligation owing from one division of Distributing to another division of Distributing. In addition, if Controlled will be indebted to Distributing subsequent to the distribution of Controlled stock, submit the following REPRESENTATION: *The indebtedness owed by the controlled corporation to the distributing corporation subsequent to the distribution of the controlled corporation stock will not constitute stock or securities within the meaning of section 355 of the Code.*

(3) Section 38 property.—State whether any assets being transferred between Distributing and Controlled include property for which an investment tax credit was taken in prior years. If so, submit the following REPRESENTATION: *The investment tax credit previously computed with respect to the section 38 property transferred will be adjusted in the year of transfer to reflect an early disposition of the property pursuant to section 47(a)(1) and (5) of the Code.*

(4) Investment company.—If assets are transferred by Distributing to Controlled, or liabilities owed by Controlled to Distributing are cancelled, submit the following REPRESENTATION: *No two parties to the transaction are investment companies as defined in section 368(a)(2)(F) (iii) and (iv) of the Code.*

(5) Consideration received by Distributing.—Set forth all consideration received by Distributing in connection with the transaction.

(b) Profit and loss statements.—Submit separate unconsolidated profit and loss statements (including all applicable notes) for each of the past 5 years for each Active Business (sections 4.031, 4.032, and 4.034 above) relied on to satisfy the active trade or business requirement of section 355(b) of the Code for Distributing and each Controlled. The statements must show that each business has had gross receipts and operating expenses (including employee expenses such as payroll withholding taxes) representative of the active conduct of a trade or business for each of the past 5 years. Submit the following REPRESENTATION: *The 5 years of financial information submitted on behalf of the distributing, controlled, and other corporations is representative of each corporation's present operations, and, with regard to each corporation, there have been no substantial operational changes since the date of the last financial statements submitted.*

(c) Method of accounting.—State the overall method of accounting of Distribution and each Controlled. If Distributing is on the cash method of accounting or a similar method and Controlled is also on the cash method or similar method, or it is represented that Controlled will be on this method, then submit a statement as to whether any income items such as accounts receivable, or any items resulting from a sale, exchange or disposition which would have resulted in income to Distributing, or any items of expense, will be transferred to Controlled. If any of these items are being transferred, fully explain. Further, submit the following REPRESENTATION: *The distributing corporation neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.* If Distributing is on the cash method of accounting or similar method and Controlled is on the accrual method or similar method, a closing agreement will be required unless the following REPRESENTATION is submitted: *No income items, including accounts receivable or any items resulting from a sale, exchange or disposition or property, that would have resulted in income to the distributing corporation, and no items of expense, will be transferred to the controlled corporation, if the distributing corporation has earned the right to receive the income or could claim a deduction for the expense under the accrual or similar method of accounting.*

.04 *Business purpose.*

1. Detailed Description.—Describe in detail the business purpose for the distribution of the stock of Controlled.

2. Relevance of business purpose.—Explain how the business purpose is germane to the businesses of the corporations (see section 1.355-2(c) of the regulations). Also, see, generally, Rev. Rul. 85-127, 1985-2, C.B. 119; Rev. Rul. 85-122, 1985-2 C.B. 118; Rev. Rul. 82-131, 1982-2 C.B. 83; Rev. Rul. 82-130, 1982-2 C.B. 83; Rev. Rul. 78-383, 1978-2 C.B. 142; Rev. Rul. 77-22, 1977-1 C.B. 91; Rev. Rul. 76-527, 1976-2 C.B. 103; Rev. Rul. 76-187, 1976-1 C.B. 97; Rev. Rul. 75-337, 1975-2 C.B. 124; Rev. Rul. 72-530, 1972-2 C.B. 212; Rev. Rul. 70-18, 1970-1 C.B. 74; Rev. Rul. 69-460, 1969-2 C.B. 51; Rev. Rul. 68-603, 1968-2 C.B. 148; and Rev. Rul. 56-450, 1956-2 C.B. 201.

3. Need for present transaction.—Explain why other feasible ways of meeting the corporation's business needs were rejected in favor of the present transaction.

4. Third party documentation.—If the transaction is being undertaken at the request of, or under the advice of, persons other than Controlled or Distributing, explain fully.

Documentation of third party requests or advice may be essential to substantiate the business purpose for the distribution. (Illustrations of business purposes for which third party documentation would be requested are suggested by the facts of Rev. Ruls. 85-122, 82-131, 82-130, 77-22, 76-527, 75-337, and 69-460 *(Situation 2).*

.05 *Information relating to whether the transaction will be considered to be used principally as a device for the distribution of earnings and profits of Distributing, Controlled, or both.*

1. Liquidation or sale of assets.—Submit the following REPRESENTATION: *There is no plan or intention to liquidate either the distributing or controlled corporation, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation subsequent to the transaction, except in the ordinary course of business.* Alternatively, describe the subsequent transaction.

2. Disposition of stock or secuities.—Submit the following REPRESENTATION: *There is no plan or intention by the shareholders or security holders of the distributing corporation to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in, or securities of, either the distributing or controlled corporation subsequent to the transaction.* Alternatively, if a plan or intent to dispose exists, see section 1.355-2(b)(1) of the regulations as to what constitutes evidence of a device and provide the following information:

(a) Transaction.—Give complete details concerning the transaction, including any agreements existing between the parties and the number of shares of each class of stock or the amount of each series of securities that each shareholder or security holder will dispose of. If the disposition results from governmental action, explain fully how this action necessitates the shareholder disposition. See Rev. Ruls. 83–23, 1983–1 C.B. 82, and 78–383.

(b) Consideration.—State the consideration to be recieved by each shareholder and security holder.

3. Earnings and profits.—State whether either Distributing or Controlled will have any earnings and profits, within the meaning of section 316 of the Code, on the date of the distribution or at the close of their respective taxable years. This information aids the Service in determining whether the transaction is being used principally as a device for the distribution of earnings and profits. See Rev. Rul. 71–384, 1971–2 C.B. 181.

4. Non pro rata distribution.—State whether all or any part of the distribution, if considered taxable, would qualify as an exchange under section 302(a) of the Code (see Rev. Rul. 71–383, 1971–2 C.B. 180, and Rev. Rul. 64–102, 1964–1 (Part 1) C.B. 136).

5. Transfers between Distributing and Controlled.

(a) Contributions to capital.—Provide complete details concerning any contributions of property made by Distributing to the capital of Controlled as part of the transaction.

(b) Cancellation of indebtedness.—With respect to any indebtedness between Distributing and Controlled, give complete details concerning the principal amount of the indebtedness, the circumstances under which it arose, and the date and method under which the indebtedness will be discharged. See Rev. Rul. 83–114, 1983–2 C.B. 66.

(c) Continuing transactions between Distributing and Controlled.—Describe in detail any continuing transactions between Distributing and Controlled following the distribution. In addition, submit the following REPRESENTATION: *Payments made in connection with all continuing transactions between the distributing and controlled corporations will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.*

(d) Distribution to Distributing.—Provide complete details concerning any distributions of property by Controlled to Distributing in connection with the transaction.

6. Investment and inactive assets.

(2) Distributing.—State the total amount of investment assets, and other assets that are not used in an active business, that will be held by Distributing or by any of its subsidiaries. Explain the reason why Distributing or its subsidiaries will hold these assets.

(b) Controlled.—State the total amountof investment assets, and other assets that are not used in an active business, that will be held by Controlled or by any of its subsidiaries. Explain the reason why Controlled or its subsidiaries will hold these assets.

.06 *Continuity of shareholder interest*.—If any shareholder plans to dispose of stock in Distributing or Controlled, submit a representation that the shareholder disposition will not violate the requirement of a 50 percent in value continuing interest in stock ownership as specified in section 3.02 of Rev. Proc. 77–37. See section. 1.355–2(c) of the regulations.

.07 *General*

1. Other transactions.—State whether there have been, or will be, any related transactions, and, if so, briefly describe these other transactions and fully explain their relationship to, and impact on, the present transaction. Even if the transaction is thought to be unrelated, provide full details if it is contemplated that any stock is to be issued by Distributing or Controlled other than that already described as being distributed pursuant to the plan. Include a description of the stock of Distributing or Controlled being issued pursuant to a public offering or pursuant to the exercise of stock rights or warrants. See section 9.05 of Rev. Proc. 86–1.

2. Copy of plan.—Submit a copy of the plan of reorganization or distribution. Alternatively, state why a copy is not available.

3. Foreign corporation.—State whether either Distributing or Controlled is a foreign corporation. See section 367 of the Code.

4. Additional statements.—See Rev. Proc. 86–1 for additional information and statements that must be submitted with all ruling requests, including statements required under section 9.02 and 9.09 (relating to instructions to taxpayers).

5. Requested rulings.—List the rulings being requested in the exact wording desired, and provide statutory, regulatory, or other authority for their issuance.

6. Taxpayer's memorandum.—Submit the information required by section 9.08 of Rev. Proc. 86–1 (relating to relevant authorities regarding the tax results of the transaction).

SEC. 5. INQUIRIES

Inquiries in regard to this revenue procedure should refer to its number and should be addressed to the Associate Chief Counsel (Technical), Attention: CC:C:R, Internal Revenue Service, Washington, D.C. 20224.

SEC. 6. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 81–41 is superseded.

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26 CFR 601.201: Rulings and determination letters. (Also Part I, Section 368; 1.368–1.)

Rev. Proc. 86–42

SECTION 1. PURPOSE

The purpose of this revenue procedure is to amplify Rev. Proc. 77–37, 1977–2 C.B. 568, as amplified by Rev. Proc. 77–41, 1977–2 C.B. 574, Rev. Proc. 83–81, 1983–2 C.B. 598, and Rev. Proc. 84–42, 1984–1 C.B. 521, and superseded in part by Rev. Proc. 79–14, 1979–1 C.B. 496. Rev. Proc. 77–37, as amplified and superseded in part, sets forth certain operating rules of the Internal Revenue Service pertaining to issuing letter rulings and in determining whether it should decline to issue letter rulings.

SEC. 2. BACKGROUND

The Internal Revenue Service receives many requests for rulings in which the information relating to the proposed transaction is not sufficient to permit a determination to be made. In these cases, it is necessary to obtain additional facts from the taxpayer before the request for a letter ruling can be considered. Obtaining these additional facts is time consuming for both Service personnel and taxpayers and delays issuance of the letter ruling.

In addition to the operating rules set forth in Rev. Proc. 77–37, the Service has developed certain standard representations that must be submitted as a prerequisite to the issuance of rulings on the tax consequences of specific transactions. These representations ensure that specific statutory and judicial requirements and administrative ruling guidelines are satisfied. The purpose of this revenue procedure is to facilitate the filing and processing of requests for ruling for certain enumerated transactions under section 368(a)(1) of the Internal Revenue Code by showing specific representations to be included so that the requests will be as complete as possible when initially filed.

Because the information and representations necessary to rule on a particular transaction depend upon all the facts and circumstances, representations in addition to those set forth in this revenue procedure may be required. Careful attention to the preparation of the appropriate representations set forth below will aid in the timely processing of the letter ruling requests.

SEC. 3. PROCEDURE

Rev. Proc. 77–37 is amplified by adding the following as a new section 7 and renumbering the present sections 7 and 8 as sections 8 and 9:

SEC. 7. REPRESENTATIONS

Each representation set forth in this section ordinarily should be submitted in the application for a ruling under the applicable enumerated subparagraph of section 368(a)(1) of the Code. Each representation set forth in the appropriate subsection below should be submitted precisely in the language requested. If a representation cannot be submitted as requested, an explanation must be given. Variations of the language of the representations may delay processing the ruling request and will not be accepted unless reasons satisfactory to the Service are submitted.

The representations relating to the acquisitive reorganizations defined in section 368(a)(1) can be found in the following subsections of this section:

.01 Section 368(a)(1)(A)
.02 Section 368(a)(1)(A) and (a)(2)(D)
.03 Section 368(a)(1)(A) and (a)(2)(E)
.04 Section 368(a)(1)(B)
.05 Section 368(a)(1)(C)
.06 Section 368(a)(1)(D)
.07 Section 368(a)(1)(F)
.08 Miscellaneous representations

.01 Section 368(a)(1)(A) mergers or consolidations:

Legend: Acquiring = the surviving transferee corporation in a merger (or the new corporation formed in a consolidation)
Target = the transferor corporation

1. THE FAIR MARKET VALUE OF THE ACQUIRING STOCK AND OTHER CONSIDERATION RECEIVED BY EACH TARGET SHAREHOLDER WILL BE APPROXIMATELY EQUAL TO THE FAIR MARKET VALUE OF THE TARGET STOCK SURRENDERED IN THE EXCHANGE.

2. THERE IS NO PLAN OR INTENTION BY THE SHAREHOLDERS OF TARGET WHO OWN 1 PERCENT OR MORE OF THE TARGET STOCK, AND TO THE BEST OF THE KNOWLEDGE OF THE MANAGEMENT OF TARGET, THERE IS NO PLAN OR INTENTION ON THE PART OF THE REMAINING SHAREHOLDERS OF TARGET TO SELL, EXCHANGE, OR OTHERWISE DISPOSE OF A NUMBER OF SHARES OF ACQUIRING STOCK RECEIVED IN THE TRANSACTION THAT WOULD REDUCE THE TARGET SHAREHOLDERS' OWNERSHIP OF ACQUIRING STOCK TO A NUMBER OF SHARES HAVING A VALUE, AS OF THE DATE OF THE TRANSACTION, OF LESS THAN 50 PERCENT OF THE VALUE OF ALL OF THE FORMERLY OUTSTANDING STOCK OF TARGET AS OF THE SAME DATE. FOR PURPOSES OF THIS REPRESENTATION, SHARES OF TARGET STOCK EXCHANGED FOR CASH OR OTHER PROPERTY, SURRENDERED BY DISSENTERS, OR EXCHANGED FOR CASH IN LIEU OF FRACTIONAL SHARES OF ACQUIRING STOCK WILL BE TREATED AS OUTSTANDING TARGET STOCK ON THE DATE OF THE TRANSACTION. MOREOVER, SHARES OF TARGET STOCK AND SHARES OF ACQUIRING STOCK HELD BY TARGET SHAREHOLDERS AND OTHERWISE SOLD, REDEEMED, OR DISPOSED OF PRIOR OR SUBSEQUENT TO THE TRANSACTION WILL BE CONSIDERED IN MAKING THIS REPRESENTATION. (Alternatively, for publicly traded companies, submit the above representation substituting "5 percent" for "1 percent" where it appears.)

3. ACQUIRING HAS NO PLAN OR INTENTION TO REACQUIRE ANY OF ITS STOCK ISSUED IN THE TRANSACTION.

4. ACQUIRING HAS NO PLAN OR INTENTION TO SELL OR OTHERWISE DISPOSE OF ANY OF THE ASSETS OF TARGET ACQUIRED IN THE TRANSACTION, EXCEPT FOR DISPOSITIONS MADE IN THE ORDINARY COURSE OF BUSINESS OR TRANSFERS DESCRIBED IN SECTION 368(a)(2)(C) OF THE INTERNAL REVENUE CODE.

5. THE LIABILITIES OF TARGET ASSUMED BY ACQUIRING AND THE LIABILITIES TO WHICH THE TRANSFERRED ASSETS OF TARGET ARE SUBJECT WERE INCURRED BY TARGET IN THE ORDINARY COURSE OF ITS BUSINESS.

6. FOLLOWING THE TRANSACTION, ACQUIRING WILL CONTINUE THE HISTORIC BUSINESS OF TARGET OR USE A SIGNIFICANT PORTION OF TARGET'S HISTORIC BUSINESS ASSETS IN A BUSINESS.

7. ACQUIRING, TARGET, AND THE SHAREHOLDERS OF TARGET WILL PAY THEIR RESPECTIVE EXPENSES, IF ANY, INCURRED IN CONNECTION WITH THE TRANSACTION.

8. THERE IS NO INTERCORPORATE INDEBTEDNESS EXISTING BETWEEN TARGET AND ACQUIRING THAT WAS ISSUED, ACQUIRED, OR WILL BE SETTLED AT A DISCOUNT.

9. NO TWO PARTIES TO THE TRANSACTION ARE INVESTMENT COMPANIES AS DEFINED IN SECTION 368(a)(2)(F)(iii) AND (iv) OF THE INTERNAL REVENUE CODE.

10. TARGET IS NOT UNDER THE JURISDICTION OF A COURT IN A TITLE 11 OR SIMILAR CASE WITHIN THE MEANING OF SECTION 368(a)(3)(A) OF THE INTERNAL REVENUE CODE.

11. THE FAIR MARKET VALUE OF THE ASSETS OF TARGET TRANSFERRED TO ACQUIRING WILL EQUAL OR EXCEED THE SUM OF THE LIABILITIES ASSUMED BY ACQUIRING PLUS THE AMOUNT OF LIABILITIES, IF ANY, TO WHICH THE TRANSFERRED ASSETS ARE SUBJECT.

12. (If the transaction also meets the definition of a reorganization under section 368(a)(1)(D) of the Code, submit the following:)

THE TOTAL ADJUSTED BASIS OF THE ASSETS OF TARGET TRANSFERRED TO ACQUIRING WILL EQUAL OR EXCEED THE SUM OF THE LIABILITIES ASSUMED BY ACQUIRING, PLUS THE AMOUNT OF LIABILITIES, IF ANY, TO WHICH THE TRANSFERRED ASSETS ARE SUBJECT.

.02 Section 368(a)(1)(A) and (a)(2)(D) mergers

Legend: Parent = the controlling corporation

Sub = the acquiring corporation

Target = the transferor corporation

1. THE FAIR MARKET VALUE OF THE PARENT STOCK AND OTHER CONSIDERATION RECEIVED BY EACH TARGET SHAREHOLDER WILL BE APPROXIMATELY EQUAL TO THE FAIR MARKET VALUE OF THE TARGET STOCK SURRENDERED IN THE EXCHANGE.

2. THERE IS NO PLAN OR INTENTION BY THE SHAREHOLDERS OF TARGET WHO OWN 1 PERCENT OR MORE OF THE TARGET STOCK, AND TO THE BEST OF THE KNOWLEDGE OF THE MANAGEMENT OF TARGET, THERE IS NO PLAN OR INTENTION ON THE PART OF THE REMAINING SHAREHOLDERS OF TARGET TO SELL, EXCHANGE OR OTHERWISE DISPOSE OF A NUMBER OF SHARES OF PARENT STOCK RECEIVED IN THE TRANSACTION THAT WOULD REDUCE THE TARGET SHAREHOLDERS' OWNERSHIP OF PARENT STOCK TO A NUMBER OF SHARES HAVING A VALUE, AS OF THE DATE OF THE TRANSACTION, OF LESS THAN 50 PERCENT OF THE VALUE OF ALL OF THE FORMERLY OUTSTANDING STOCK OF TARGET AS OF THE SAME DATE. FOR PURPOSES OF THIS REPRESENTATION, SHARES OF TARGET STOCK EXCHANGED FOR CASH OR OTHER PROPERTY, SURRENDERED BY DISSENTERS OR EXCHANGED FOR CASH IN LIEU OF FRACTIONAL SHARES OF PARENT STOCK WILL BE TREATED AS OUTSTANDING TARGET STOCK ON THE DATE OF THE TRANSACTION. MOREOVER, SHARES OF TARGET STOCK AND SHARES OF PARENT STOCK HELD BY TARGET SHAREHOLDERS AND OTHERWISE SOLD, REDEEMED, OR DISPOSED OF PRIOR OR SUBSEQUENT TO THE TRANSACTION WILL BE CONSIDERED IN MAKING THIS REPRESENTATION. (Alternatively, for publicly traded companies, submit the above representation substituting "5 percent" for "1 percent" where it appears.)

3. SUB WILL ACQUIRE AT LEAST 90 PERCENT OF THE FAIR MARKET VALUE OF THE NET ASSETS AND AT LEAST 70 PERCENT OF THE FAIR MARKET VALUE OF THE GROSS ASSETS HELD BY TARGET IMMEDIATELY PRIOR TO THE TRANSACTION. FOR PURPOSES OF THIS REPRESENTATION, AMOUNTS PAID BY TARGET TO DISSENTERS, AMOUNTS PAID BY TARGET TO SHAREHOLDERS WHO RECEIVE CASH OR OTHER PROPERTY, TARGET ASSETS USED TO PAY ITS REORGANIZATION EXPENSES, AND ALL REDEMPTIONS AND DISTRIBUTIONS (EXCEPT FOR REGULAR, NORMAL DIVIDENDS) MADE BY TARGET IMMEDIATELY PRECEDING THE TRANSFER, WILL BE INCLUDED AS ASSETS OF TARGET HELD IMMEDIATELY PRIOR TO THE TRANSACTION.

4. PRIOR TO THE TRANSACTION, PARENT WILL BE IN CONTROL OF SUB WITHIN THE MEANING OF SECTION 368(c)(1) OF THE INTERNAL REVENUE CODE.

5. FOLLOWING THE TRANSACTION, SUB WILL NOT ISSUE ADDITIONAL SHARES OF ITS STOCK THAT WOULD RESULT IN PARENT LOSING CONTROL OF SUB WITHIN THE MEANING OF SECTION 368(c)(1) OF THE INTERNAL REVENUE CODE.

6. PARENT HAS NO PLAN OR INTENTION TO REACQUIRE ANY OF ITS STOCK ISSUED IN THE TRANSACTION.

7. PARENT HAS NO PLAN OR INTENTION TO LIQUIDATE SUB; TO MERGE SUB WITH AND INTO ANOTHER CORPORATION; TO SELL OR OTHERWISE DISPOSE OF THE STOCK OF SUB; OR TO CAUSE SUB TO SELL OR OTHERWISE DISPOSE OF ANY OF THE ASSETS OF TARGET ACQUIRED IN THE TRANSACTION, EXCEPT FOR DISPOSITIONS MADE IN THE ORDINARY COURSE OF BUSINESS OR TRANSFERS DESCRIBED IN SECTION 368(a)(2)(C) OF THE INTERNAL REVENUE CODE.

8. THE LIABILITIES OF TARGET ASSUMED BY SUB AND THE LIABILITIES TO WHICH THE TRANSFERRED ASSETS OF TARGET ARE SUBJECT WERE INCURRED BY TARGET IN THE ORDINARY COURSE OF ITS BUSINESS.

9. FOLLOWING THE TRANSACTION, SUB WILL CONTINUE THE HISTORIC BUSINESS OF TARGET OR USE A SIGNIFICANT PORTION OF TARGET'S BUSINESS ASSETS IN A BUSINESS.

10. PARENT, SUB, TARGET, AND THE SHAREHOLDERS OF TARGET WILL PAY THEIR RESPECTIVE EXPENSES, IF ANY, INCURRED IN CONNECTION WITH THE TRANSACTION.

11. THERE IS NO INTERCORPORATE INDEBTEDNESS EXISTING BETWEEN PARENT AND TARGET OR BETWEEN SUB AND TARGET THAT WAS ISSUED, ACQUIRED, OR WILL BE SETTLED AT A DISCOUNT.

12. NO TWO PARTIES TO THE TRANSACTION ARE INVESTMENT COMPANIES AS DEFINED IN SECTION 368(a)(2)(F)(iii) and (iv) OF THE INTERNAL REVENUE CODE.

13. TARGET IS NOT UNDER THE JURISDICTION OF A COURT IN A TITLE 11 OR SIMILAR CASE WITHIN THE MEANING OF SECTION 368(a)(3)(A) OF THE INTERNAL REVENUE CODE.

14. THE FAIR MARKET VALUE OF THE ASSETS OF TARGET TRANSFERRED TO SUB WILL EQUAL OR EXCEED THE SUM OF THE LIABILITIES ASSUMED BY SUB, PLUS THE AMOUNT OF LIABILITIES, IF ANY, TO WHICH THE TRANSFERRED ASSETS ARE SUBJECT.

15. NO STOCK OF SUB WILL BE ISSUED IN THE TRANSACTION.

.03 Section 368(a)(1)(A) and (a)(2)(E) mergers:

Legend: Parent = the controlling corporation

Sub = the merged corporation

Target = the surviving corporation

1. THE FAIR MARKET VALUE OF THE PARENT STOCK AND OTHER CONSIDERATION RECEIVED BY EACH TARGET SHAREHOLDER WILL BE APPROXIMATELY EQUAL TO THE FAIR MARKET VALUE OF THE TARGET STOCK SURRENDERED IN THE EXCHANGE.

2. THERE IS NO PLAN OR INTENTION BY THE SHAREHOLDERS OF TARGET WHO OWN 1 PERCENT OR

MORE OF THE TARGET STOCK, AND TO THE BEST OF THE KNOWLEDGE OF THE MANAGEMENT OF TARGET, THERE IS NO PLAN OR INTENTION ON THE PART OF THE REMAINING SHAREHOLDERS OF TARGET TO SELL, EXCHANGE, OR OTHERWISE DISPOSE OF A NUMBER OF SHARES OF PARENT STOCK RECEIVED IN THE TRANSACTION THAT WOULD REDUCE THE TARGET SHAREHOLDERS' OWNERSHIP OF PARENT STOCK TO A NUMBER OF SHARES HAVING A VALUE, AS OF THE DATE OF THE TRANSACTION, OF LESS THAN 50 PERCENT OF THE VALUE OF ALL OF THE FORMERLY OUTSTANDING STOCK OF TARGET AS OF THE SAME DATE. FOR PURPOSES OF THIS REPRESENTATION, SHARES OF TARGET STOCK EXCHANGED FOR CASH OR OTHER PROPERTY, SURRENDERED BY DISSENTERS OR EXCHANGED FOR CASH IN LIEU OF FRACTIONAL SHARES OF PARENT STOCK WILL BE TREATED AS OUTSTANDING TARGET STOCK ON THE DATE OF THE TRANSACTION. MOREOVER, SHARES OF TARGET STOCK AND SHARES OF PARENT STOCK HELD BY TARGET SHAREHOLDERS AND OTHERWISE SOLD, REDEEMED, OR DISPOSED OF PRIOR OR SUBSEQUENT TO THE TRANSACTION WILL BE CONSIDERED IN MAKING THIS REPRESENTATION (Alternatively, for publicly traded companies, submit the above representation substituting "5 percent" for "1 percent" where it appears.)

3. FOLLOWING THE TRANSACTION, TARGET WILL HOLD AT LEAST 90 PERCENT OF THE FAIR MARKET VALUE OF ITS NET ASSETS AND AT LEAST 70 PERCENT OF THE FAIR MARKET VALUE OF ITS GROSS ASSETS AND AT LEAST 90 PERCENT OF THE FIAR MARKET VALUE OF SUB'S NET ASSETS AND AT LEAST 70 PERCENT OF THE FAIR MARKET VALUE OF THE SUB'S GROSS ASSETS HELD IMMEDIATELY PRIOR TO THE TRANSACTION. FOR PURPOSES OF THIS REPRESENTATION, AMOUNTS PAID BY TARGET OR SUB TO DISSENTERS, AMOUNTS PAID BY TARGET OR SUB TO SHAREHOLDERS WHO RECEIVE CASH OR OTHER PROPERTY, AMOUNTS USED BY TARGET OR SUB TO PAY REORGANIZATION EXPENSES, AND ALL REDEMPTIONS AND DISTRIBUTIONS (EXCEPT FOR REGULAR, NORMAL DIVIDENDS) MADE BY TARGET WILL BE INCLUDED AS ASSETS OF TARGET OR SUB, RESPECTIVELY, IMMEDIATELY PRIOR TO THE TRANSACTION.

4. PRIOR TO THE TRANSACTION, PARENT WILL BE IN CONTROL OF SUB WITHIN THE MEANING OF SECTION 369(c)(1) OF THE INTERNAL REVENUE CODE.

5. TARGET HAS NO PLAN OR INTENTION TO ISSUE ADDITIONAL SHARES OF ITS STOCK THAT WOULD RESULT IN PARENT LOSING CONTROL OF TARGET WITHIN THE MEANING OF SECTION 368(c)(1) OF THE INTERNAL REVENUE CODE.

6. PARENT HAS NO PLAN OR INTENTION TO REACQUIRE ANY OF ITS STOCK ISSUED IN THE TRANSACTION.

7. PARENT HAS NO PLAN OR INTENTION TO LIQUIDATE TARGET; TO MERGE TARGET WITH OR INTO ANOTHER CORPORATION; TO SELL OR OTHERWISE DISPOSE OF THE STOCK OF TARGET EXCEPT FOR TRANSFERS OF STOCK TO CORPORATIONS CONTROLLED BY BY PARENT; OR TO CAUSE TARGET TO SELL OR OTHERWISE DISPOSE OF ANY OF ITS ASSETS OR OF ANY OF THE ASSETS ACQUIRED FORM SUB, EXCEPT FOR DISPOSITIONS MADE IN THE ORDINARY COURSE OF BUSINESS OR TRANSFERS OF ASSETS TO A CORPORATION CONTROLLED BY TARGET.

8. THE LIABILITIES OF SUB ASSUMED BY TARGET AND THE LIABILITIES TO WHICH THE TRANSFERRED ASSETS OF SUB ARE SUBJECT WERE INCURRED BY SUB IN THE ORDINARY COURSE OF ITS BUSINESS. (Alternatively) SUB WILL HAVE NO LIABILITIES ASSUMED BY TARGET, AND WILL NOT TRANSFER TO TARGET ANY ASSETS SUBJECT TO LIABILITIES, IN THE TRANSACTION.

9. FOLLOWING THE TRANSACTION, TARGET WILL CONTINUE ITS HISTORIC BUSINESS OR USE A SIGNIFICANT PORTION OF ITS HISTORIC BUSINESS ASSETS IN A BUSINESS.

10. PARENT, SUB, TARGET, AND THE SHAREHOLDERS OF TARGET WILL PAY THEIR RESPECTIVE EXPENSES, IF ANY, INCURRED IN CONNECTION WITH THE TRANSACTION.

11. THERE IS NO INTERCORPORATE INDEBTEDNESS EXISTING BETWEEN PARENT AND TARGET OR BETWEEN SUB AND TARGET THAT WAS ISSUED, ACQUIRED, OR WILL BE SETTLED AT A DISCOUNT.

12. IN THE TRANSACTION, SHARES OF TARGET STOCK REPRESENTING CONTROL OF TARGET, AS DEFINED IN SECTION 368(c)(1) OF THE CODE, WILL BE EXCHANGED SOLELY FOR VOTING STOCK OF PARENT. FOR PURPOSES OF THIS REPRESENTATION, SHARES OF TARGET STOCK EXCHANGED FOR CASH OR OTHER PROPERTY ORIGINATING WITH PARENT WILL BE TREATED AS OUTSTANDING TARGET STOCK ON THE DATE OF THE TRANSACTION.

13. AT THE TIME OF THE TRANSACTION, TARGET WILL NOT HAVE OUTSTANDING ANY WARRANTS, OPTIONS, COVERTIBLE SECURITIES, OR ANY OTHER TYPE OF RIGHT PURSUANT TO WHICH ANY PERSON COULD ACQUIRE STOCK IN TARGET THAT, IF EXERCISED OR CONVERTED, WOULD AFFECT PARENT'S ACQUISITION OR RETENTION OF CONTROL OF TARGET, AS DEFINED IN SECTION 368(c)(1) OF THE INTERNAL REVENUE CODE.

14. PARENT DOES NOT OWN, NOR HAS IT OWNED DURING THE PAST FIVE YEARS, ANY SHARES OF THE STOCK OF TARGET.

15. NO TWO PARTIES TO THE TRANSACTION ARE INVESTMENT COMPANIES AS DEFINED IN SECTION 368(a)(2)(F)(iii) AND (iv) OF THE INTERNAL REVENUE CODE.

16. ON THE DATE OF THE TRANSACTION, THE FAIR MARKET VALUE OF THE ASSETS OF TARGET WILL EXCEED THE SUM OF ITS LIABILITIES, PLUS THE AMOUNT OF LIABILITIES, IF ANY, TO WHICH THE ASSETS ARE SUBJECT.

17. TARGET IS NOT UNDER THE JURISDICTION OF A COURT IN A TITLE 11 OR SIMULAR CASE WITHIN THE MEANING OF SECTION

368(a)(3)(A) OF THE INTERNAL REVENUE CODE.

.04 Section 368(a)(1)(B) reorganizations:

Legend: Acquiring = the acquiring corporation

Target = the corporation whose stock is acquired

1. THE FAIR MARKET VALUE OF THE ACQUIRING STOCK RECEIVED BY EACH TARGET SHAREHOLDER WILL BE APPROXIMATELY EQUAL TO THE FAIR MARKET VALUE OF THE TARGET STOCK SURRENDERED IN THE EXCHANGE.

2. THERE IS NO PLAN OR INTENTION BY THE SHAREHOLDERS OF TARGET WHO OWN 1 PERCENT OR MORE OF THE TARGET STOCK, AND TO THE BEST OF THE KNOWLEDGE OF THE MANAGEMENT OF TARGET, THERE IS NO PLAN OR INTENTION ON THE PART OF THE REMAINING SHAREHOLDERS OF TARGET TO SELL, EXCHANGE, OR OTHERWISE DISPOSE OF A NUMBER OF SHARES OF ACQUIRING STOCK RECEIVED IN THE TRANSACTION THAT WOULD REDUCE THE TARGET SHAREHOLDERS' OWNERSHIP OF ACQUIRING STOCK TO A NUMBER OF SHARES HAVING A VALUE, AS OF THE DATE OF THE TRANSACTION, OF LESS THAN 50 PERCENT OF THE VALUE OF ALL OF THE FORMERLY OUTSTANDING STOCK OF TARGET AS OF THE SAME DATE. FOR PURPOSES OF THIS REPRESENTATION, SHARES OF TARGET STOCK SURRENDERED BY DISSENTERS OR EXCHANGED FOR CASH IN LIEU OF FRACTIONAL SHARES OF ACQUIRING STOCK WILL BE TREATED AS OUTSTANDING TARGET STOCK ON THE DATE OF THE TRANSACTION. MOREOVER, SHARES OF TARGET STOCK AND SHARES OF ACQUIRING STOCK HELD BY TARGET SHAREHOLDERS AND OTHERWISE SOLD, REDEEMED, OR DISPOSED OF PRIOR OR SUBSEQUENT TO THE TRANSACTION WILL BE CONSIDERED IN MAKING THIS REPRESENTATION. (Alternatively, for publicly traded companies, submit the above representation substituting "5 percent" for "1 percent" where it appears.)

3. TARGET HAS NO PLAN OR INTENTION TO ISSUE ADDITIONAL SHARES OF ITS STOCK THAT WOULD RESULT IN ACQUIRING LOSING CONTROL OF TARGET WITHIN THE MEANING OF SECTION 368(c)(1) OF THE INTERNAL REVENUE CODE.

4. ACQUIRING HAS NO PLAN OR INTENTION TO LIQUIDATE TARGET; TO MERGE TARGET INTO ANOTHER CORPORATION; TO CAUSE TARGET TO SELL OR OTHERWISE DISPOSE OF ANY OF ITS ASSETS, EXCEPT FOR DISPOSITIONS MADE IN THE ORDINARY COURSE OF BUSINESS; OR TO SELL OR OTHERWISE DISPOSE OF ANY OF THE TARGET STOCK ACQUIRED IN THE TRANSACTION, EXCEPT FOR TRANSFERS DESCRIBED IN SECTION 368(a)(2)(C) OF THE INTERNAL REVENUE CODE.

5. ACQUIRING HAS NO PLAN OR INTENTION TO REACQUIRE ANY OF ITS STOCK ISSUED IN THE TRANSACTION.

6. ACQUIRING, TARGET, AND THE SHAREHOLDERS OF TARGET WILL PAY THEIR RESPECTIVE EXPENSES, IF ANY, INCURRED IN CONNECTION WITH THE TRANSACTION.

7. ACQUIRING WILL ACQUIRE TARGET STOCK SOLELY IN EXCHANGE FOR ACQUIRING VOTING STOCK. FOR PURPOSES OF THIS REPRESENTATION, TARGET STOCK REDEEMED FOR CASH OR OTHER PROPERTY FURNISHED BY ACQUIRING WILL BE CONSIDERED AS ACQUIRED BY ACQUIRING. FURTHER, NO LIABILITIES OF TARGET OR THE TARGET SHAREHOLDERS WILL BE ASSUMED BY ACQUIRING, NOR WILL ANY OF THE TARGET STOCK BE SUBJECT TO ANY LIABILITIES.

8. AT THE TIME OF THE TRANSACTION, TARGET WILL NOT HAVE OUTSTANDING ANY WARRANTS, OPTIONS, CONVERTIBLE SECURITIES, OR ANY OTHER TYPE OF RIGHT PURSUANT TO WHICH ANY PERSON COULD ACQUIRE STOCK IN TARGET THAT, IF EXERCISED OR CONVERTED, WOULD AFFECT ACQUIRING'S ACQUISITION OR RETENTION OF CONTROL OF TARGET, AS DEFINED IN SECTION 368(c)(1) OF THE INTERNAL REVENUE CODE.

9. ACQUIRING DOES NOT OWN, DIRECTLY OR INDIRECTLY, NOR HAS IT OWNED DURING THE PAST FIVE YEARS, DIRECTLY OR INDIRECTLY, ANY STOCK OF TARGET.

10. FOLLOWING THE TRANSACTION, TARGET WILL CONTINUE ITS HISTORIC BUSINESS OR USE A SIGNIFICANT PORTION OF ITS HISTORIC BUSINESS ASSETS IN A BUSINESS.

11. NO TWO PARTIES TO THE TRANSACTION ARE INVESTMENT COMPANIES AS DEFINED IN SECTION 368(a)(2)(F)(iii) AND (iv) OF THE INTERNAL REVENUE CODE.

12. TARGET WILL PAY ITS DISSENTING SHAREHOLDERS THE VALUE OF THEIR STOCK OUT OF ITS OWN FUNDS. NO FUNDS WILL BE SUPPLIED FOR THAT PURPOSE, DIRECTLY OR INDIRECTLY, BY ACQUIRING, NOR WILL ACQUIRING DIRECTLY OR INDIRECTLY REIMBURSE TARGET FOR ANY PAYMENTS TO DISSENTERS. (Alternatively) THERE WILL BE NO DISSENTERS TO THE TRANSACTION.

13. ON THE DATE OF THE TRANSACTION, THE FAIR MARKET VALUE OF THE ASSETS OF TARGET WILL EXCEED THE SUM OF ITS LIABILITIES PLUS THE LIABILITIES, IF ANY, TO WHICH THE ASSETS ARE SUBJECT.

.05 Section 368(a)(1)(C) reorganizations:

Legend: Acquiring = the acquiring transferee corporation

Target = the transferor corporation

1. THE FAIR MARKET VALUE OF THE ACQUIRING STOCK RECEIVED BY EACH TARGET SHAREHOLDER WILL BE APPROXIMATELY EQUAL TO THE FAIR MARKET VALUE OF THE TARGET STOCK SURRENDERED IN THE EXCHANGE.

2. THERE IS NO PLAN OR INTENTION BY THE SHAREHOLDERS OF TARGET WHO OWN 1 PERCENT OR MORE OF THE TARGET STOCK, AND TO THE BEST OF THE KNOWLEDGE OF MANAGEMENT OF TARGET, THERE IS NO PLAN OR INTENTION ON THE PART OF THE REMAINING SHAREHOLDERS OF TARGET TO SELL, EXCHANGE, OR OTHERWISE DISPOSE OF A NUM-

BER OF SHARES OF ACQUIRING STOCK RECEIVED IN THE TRANSACTION THAT WOULD REDUCE THE TARGET SHAREHOLDERS' OWNERSHIP OF ACQUIRING STOCK TO A NUMBER OF SHARES HAVING A VALUE, AS OF THE DATE OF THE TRANSACTION, OF LESS THAN 50 PERCENT OF THE VALUE OF ALL OF THE FORMERLY OUTSTANDING STOCK OF TARGET AS OF THE SAME DATE. FOR PURPOSES OF THIS REPRESENTATION, SHARES OF TARGET STOCK EXCHANGED FOR CASH OR OTHER PROPERTY, SURRENDERED BY DISSENTERS, OR EXCHANGED FOR CASH IN LIEU OF FRACTIONAL SHARES OF ACQUIRING STOCK WILL BE TREATED AS OUTSTANDING TARGET STOCK ON THE DATE OF THE TRANSACTION. MOREOVER, SHARES OF TARGET STOCK AND SHARES OF ACQUIRING STOCK HELD BY TARGET SHAREHOLDERS AND OTHERWISE SOLD, REDEEMED, OR DISPOSED OF PRIOR OR SUBSEQUENT TO THE TRANSACTION WILL BE CONSIDERED IN MAKING THIS REPRESENTATION. (Alternatively, for publicly traded companies, submit the above representation substituting "5 percent" for "1 percent" where it appears.)

3. ACQUIRING WILL ACQUIRE AT LEAST 90 PERCENT OF THE FAIR MARKET VALUE OF THE NET ASSETS AND AT LEAST 70 PERCENT OF THE FAIR MARKET VALUE OF THE GROSS ASSETS HELD BY TARGET IMMEDIATELY PRIOR TO THE TRANSACTION. FOR PURPOSES OF THIS REPRESENTATION, AMOUNTS PAID BY TARGET TO DISSENTERS, AMOUNTS USED BY TARGET TO PAY ITS REORGANIZATION EXPENSES, AMOUNTS PAID BY TARGET TO SHAREHOLDERS WHO RECEIVE CASH OR OTHER PROPERTY, AND ALL REDEMPTIONS AND DISTRIBUTIONS (EXCEPT FOR REGULAR, NORMAL DIVIDENDS) MADE BY TARGET IMMEDIATELY PRECEDING THE TRANSFER WILL BE INCLUDED AS ASSETS OF TARGET HELD IMMEDIATELY PRIOR TO THE TRANSACTION.

4. ACQUIRING HAS NO PLAN OR INTENTION TO REACQUIRE ANY OF ITS STOCK ISSUED IN THE TRANSACTION.

5. ACQUIRING HAS NO PLAN OR INTENTION TO SELL OR OTHERWISE DISPOSE OF ANY OF THE ASSETS OF TARGET ACQUIRED IN THE TRANSACTION, EXCEPT FOR DISPOSITIONS MADE IN THE ORDINARY COURSE OF BUSINESS OR TRANSFERS DESCRIBED IN SECTION 368(a)(2)(C) OF THE INTERNAL REVENUE CODE.

6. TARGET WILL DISTRIBUTE THE STOCK, SECURITIES, AND OTHER PROPERTY IT RECEIVES IN THE TRANSACTION, AND ITS OTHER PROPERTIES, IN PURSUANCE OF THE PLAN OF REORGANIZATION.

7. THE LIABILITIES OF TARGET ASSUMED BY ACQUIRING AND THE LIABILITIES TO WHICH THE TRANSFERRED ASSETS OF TARGET ARE SUBJECT WERE INCURRED BY TARGET IN THE ORDINARY COURSE OF ITS BUSINESS.

8. FOLLOWING THE TRANSACTION, ACQUIRING WILL CONTINUE THE HISTORIC BUSINESS OF TARGET OR USE A SIGNIFICANT PORTION OF TARGET'S HISTORIC BUSINESS ASSETS IN A BUSINESS.

9. ACQUIRING, TARGET, AND THE SHAREHOLDERS OF TARGET WILL PAY THEIR RESPECTIVE EXPENSES, IF ANY, INCURRED IN CONNECTION WITH THE TRANSACTION.

10. THERE IS NO INTERCORPORATE INDEBTEDNESS EXISTING BETWEEN ACQUIRING AND TARGET THAT WAS ISSUED, ACQUIRED, OR WILL BE SETTLED AT A DISCOUNT.

11. NO TWO PARTIES TO THE TRANSACTION ARE INVESTMENT COMPANIES AS DEFINED IN SECTION 368(a)(2)(F)(iii) AND (iv) OF THE INTERNAL REVENUE CODE.

12. ACQUIRING DOES NOT OWN, DIRECTLY OR INDIRECTLY, NOR HAS IT OWNED DURING THE PAST FIVE YEARS, DIRECTLY OR INDIRECTLY, ANY STOCK OF TARGET.

13. THE FAIR MARKET VALUE OF THE ASSETS OF TARGET TRANSFERRED TO ACQUIRING WILL EQUAL OR EXCEED THE SUM OF THE LIABILITIES ASSUMED BY ACQUIRING, PLUS THE AMOUNT OF LIABILITIES, IF ANY, TO WHICH THE TRANSFERRED ASSETS ARE SUBJECT.

14. TARGET IS NOT UNDER THE JURISDICTION OF A COURT IN A TITLE 11 OR SIMILAR CASE WITHIN THE MEANING OF SECTION 368(a)(3)(A) OF THE INTERNAL REVENUE CODE.

.06 Section 368(a)(1)(D) acquisitive reorganizations:

Legend: Acquiring = the transferee corporation
Target = the transferor corporation

1. THE FAIR MARKET VALUE OF THE ACQUIRING STOCK AND OTHER CONSIDERATION RECEIVED BY EACH TARGET SHAREHOLDER WILL BE APPROXIMATELY EQUAL TO THE FAIR MARKET VALUE OF THE TARGET STOCK SURRENDERED IN THE EXCHANGE.

2. THERE IS NO PLAN OR INTENTION BY THE SHAREHOLDERS OF TARGET WHO OWN 1 PERCENT OR MORE OF THE TARGET STOCK, AND TO THE BEST OF THE KNOWLEDGE OF THE MANAGEMENT OF TARGET, THERE IS NO PLAN OR INTENTION ON THE PART OF THE REMAINING SHAREHOLDERS OF TARGET TO SELL, EXCHANGE, OR OTHERWISE DISPOSE OF A NUMBER OF SHARES OF ACQUIRING STOCK RECEIVED IN THE TRANSACTION THAT WOULD REDUCE THE TARGET SHAREHOLDERS' OWNERSHIP OF ACQUIRING STOCK TO A NUMBER OF SHARES HAVING A VALUE, AS OF THE DATE OF THE TRANSACTION, OF LESS THAN 50 PERCENT OF THE VALUE OF ALL OF THE FORMERLY OUTSTANDING STOCK OF TARGET AS OF THE SAME DATE. FOR PURPOSES OF THIS REPRESENTATION, SHARES OF TARGET STOCK EXCHANGED FOR CASH OR OTHER PROPERTY, SURRENDERED BY DISSENTERS OR EXCHANGED FOR CASH IN LIEU OF FRACTIONAL SHARES OF ACQUIRING STOCK WILL BE TREATED AS OUTSTANDING TARGET STOCK ON THE DATE OF THE TRANSACTION. MOREOVER, SHARES OF TARGET STOCK AND SHARES OF ACQUIRING STOCK HELD BY TARGET SHAREHOLDERS AND OTHERWISE SOLD, REDEEMED, OR DISPOSED OF PRIOR

TO SUBSEQUENT TO THE TRANSACTION WILL BE CONSIDERED IN MAKING THIS REPRESENTATION. (Alternatively, for publicly traded companies, submit the above representation substituting "5 percent" for "1 percent" where it appears.)

3. ACQUIRING WILL ACQUIRE AT LEAST 90 PERCENT OF THE FAIR MARKET VALUE OF THE NET ASSETS AND AT LEAST 70 PERCENT OF THE FAIR MARKET VALUE OF THE GROSS ASSETS HELD BY TARGET IMMEDIATELY PRIOR TO THE TRANSACTION. FOR PURPOSES OF THIS REPRESENTATION, AMOUNTS PAID BY TARGET TO DISSENTERS, AMOUNTS PAID BY TARGET TO SHAREHOLDERS WHO RECEIVE CASH OR OTHER PROPERTY, AMOUNTS USED BY TARGET TO PAY ITS REORGANIZATION EXPENSES, AND ALL REDEMPTIONS AND DISTRIBUTIONS (EXCEPT FOR REGULAR, NORMAL DIVIDENDS) MADE BY TARGET IMMEDIATELY PRECEDING THE TRANSFER WILL BE INCLUDED AS ASSETS OF TARGET HELD IMMEDIATELY PRIOR TO THE TRANSACTION.

4. AFTER THE TRANSACTION, THE SHAREHOLDERS OF TARGET WILL BE IN CONTROL OF ACQUIRING WITHIN THE MEANING OF SECTION 368(c)(2) OF THE INTERNAL REVENUE CODE.

5. ACQUIRING HAS NO PLAN OR INTENTION TO REACQUIRE ANY OF ITS STOCK ISSUED IN THE TRANSACTION.

6. ACQUIRING HAS NO PLAN OR INTENTION TO SELL OR OTHERWISE DISPOSE OF ANY OF THE ASSETS OR TARGET ACQUIRED IN THE TRANSACTION, EXCEPT FOR DISPOSITIONS MADE IN THE ORDINARY COURSE OF BUSINESS.

7. THE LIABILITIES OF TARGET ASSUMED BY ACQUIRING PLUS THE LIABILITIES, IF ANY, TO WHICH THE TRANSFERRED ASSETS ARE SUBJECT WERE INCURRED BY TARGET IN THE ORDINARY COURSE OF ITS BUSINESS AND ARE ASSOCIATED WITH THE ASSETS TRANSFERRED.

8. FOLLOWING THE TRANSACTION, ACQUIRING WILL CONTINUE THE HISTORIC BUSINESS OF TARGET OR USE A SIGNIFICANT PORTION OF TARGET'S HISTORIC BUSINESS ASSETS IN A BUSINESS.

9. AT THE TIME OF THE TRANSACTION, ACQUIRING WILL NOT HAVE OUTSTANDING ANY WARRANTS, OPTIONS, CONVERTIBLE SECURITIES, OR ANY OTHER TYPE OF RIGHT PURSUANT TO WHICH ANY PERSON COULD ACQUIRE STOCK IN ACQUIRING THAT, IF EXERCISED OR CONVERTED, WOULD AFFECT THE TARGET SHAREHOLDERS' ACQUISITION OR RETENTION OF CONTROL OF ACQUIRING, AS DEFINED IN SECTION 368(c)(2) OF THE INTERNAL REVENUE CODE.

10. ACQUIRING, TARGET, AND THE SHAREHOLDERS OF TARGET WILL PAY THEIR RESPECTIVE EXPENSES, IF ANY, INCURRED IN CONNECTION WITH THE TRANSACTION.

11. THERE IS NO INTERCORPORATE INDEBTEDNESS EXISTING BETWEEN ACQUIRING AND TARGET THAT WAS ISSUED, ACQUIRED, OR WILL BE SETTLED AT A DISCOUNT.

12. NO TWO PARTIES TO THE TRANSACTION ARE INVESTMENT COMPANIES AS DEFINED IN SECTION 368(a)(2)(F)(iii) AND (iv) OF THE INTERNAL REVENUE CODE.

13. THE FAIR MARKET VALUE OF THE ASSETS OF TARGET TRANSFERRED TO ACQUIRING WILL EQUAL OR EXCEED THE SUM OF THE LIABILITIES ASSUMED BY ACQUIRING, PLUS THE AMOUNT OF LIABILITIES, IF ANY, TO WHICH THE TRANSFERRED ASSETS ARE SUBJECT.

14. THE TOTAL ADJUSTED BASIS OF THE ASSETS OF TARGET TRANSFERRED TO ACQUIRING WILL EQUAL OR EXCEED THE SUM OF THE LIABILITIES TO BE ASSUMED BY ACQUIRING, PLUS THE AMOUNT OF LIABILITIES, IF ANY, TO WHICH THE TRANSFERRED ASSETS ARE SUBJECT.

15. TARGET IS NOT UNDER THE JURISDICTION OF A COURT IN A TITLE 11 OR SIMILAR CASE WITHIN THE MEANING OF SECTION 368(a)(3)(A) OF THE INTERNAL REVENUE CODE.

.07 Section 368(a)(1)(F) reorganizations:

Legend: Oldco = the transferor corporation
Newco = the surviving transferee corporation

1. THE FAIR MARKET VALUE OF THE NEWCO STOCK AND OTHER CONSIDERATION RECEIVED BY EACH OLDCO SHAREHOLDER WILL BE APPROXIMATELY EQUAL TO THE FAIR MARKET VALUE OF THE OLDCO STOCK SURRENDERED IN THE EXCHANGE.

2. THERE IS NO PLAN OR INTENTION BY THE SHAREHOLDERS OF OLDCO WHO OWN 1 PERCENT OR MORE OF THE OLDCO STOCK, AND TO THE BEST OF THE KNOWLEDGE OF MANAGEMENT OF OLDCO, THERE IS NO PLAN OR INTENTION ON THE PART OF THE REMAINING SHAREHOLDERS OF OLDCO TO SELL, EXCHANGE OR OTHERWISE DISPOSE OF ANY OF THE SHARES OF NEWCO STOCK RECEIVED IN THE TRANSACTION. (Alternatively, for publicly traded companies, submit the above representation substituting "5 percent" for "1 percent" where it appears.)

3. IMMEDIATELY FOLLOWING CONSUMMATION OF THE TRANSACTION, THE SHAREHOLDERS OF OLDCO WILL OWN ALL OF THE OUTSTANDING NEWCO STOCK AND WILL OWN SUCH STOCK SOLELY BY REASON OF THEIR OWNERSHIP OF OLDCO STOCK IMMEDIATELY PRIOR TO THE TRANSACTION.

4. NEWCO HAS NO PLAN OR INTENTION TO ISSUE ADDITIONAL SHARES OF ITS STOCK FOLLOWING THE TRANSACTION.

5. IMMEDIATELY FOLLOWING CONSUMMATION OF THE TRANSACTION, NEWCO WILL POSSESS THE SAME ASSETS AND LIABILITIES, EXCEPT FOR ASSETS DISTRIBUTED TO SHAREHOLDERS WHO RECEIVE CASH OR OTHER PROPERTY, ASSETS USED TO PAY DISSENTERS TO THE TRANSACTION, AND ASSETS USED TO PAY EXPENSES INCURRED IN CONNECTION WITH THE TRANSACTION, AS THOSE POSSESSED BY OLDCO IMMEDIATELY PRIOR TO THE TRANSACTION. ASSETS DISTRIBUTED TO SHAREHOLDERS WHO RECEIVE CASH OR OTHER PROPERTY, ASSETS USED TO PAY EXPENSES, ASSETS USED TO PAY DISSENTERS TO THE TRANSACTION, AND ALL REDEMPTIONS AND DISTRIBUTIONS (EXCEPT FOR REGULAR, NORMAL DIVIDENDS)

MADE BY OLDCO IMMEDIATELY PRECEDING THE TRANSACTION WILL, IN THE AGGREGATE, CONSTITUTE LESS THAN ONE PERCENT OF THE NET ASSETS OF OLDCO. DISSENTING SHAREHOLDERS WILL OWN LESS THAN ONE PERCENT OF THE OLDCO STOCK.

6. AT THE TIME OF THE TRANSACTION, OLDCO WILL NOT HAVE OUTSTANDING ANY WARRANTS, OPTIONS, CONVERTIBLE SECURITIES, OR ANY OTHER TYPE OF RIGHT PURSUANT TO WHICH ANY PERSON COULD ACQUIRE STOCK IN OLDCO.

7. NEWCO HAS NO PLAN OR INTENTION TO REACQUIRE ANY OF ITS STOCK ISSUED IN THE TRANSACTION.

8. NEWCO HAS NO PLAN OR INTENTION TO SELL OR OTHERWISE DISPOSE OF ANY OF THE ASSETS OF OLDCO ACQUIRED IN THE TRANSACTION, EXCEPT FOR DISPOSITIONS MADE IN THE ORDINARY COURSE OF BUSINESS.

9. THE LIABILITIES OF OLDCO ASSUMED BY NEWCO PLUS THE LIABILITIES, IF ANY, TO WHICH THE TRANSFERRED ASSETS ARE SUBJECT WERE INCURRED BY OLDCO IN THE ORDINARY COURSE OF ITS BUSINESS AND ARE ASSOCIATED WITH THE ASSETS TRANSFERRED.

10. FOLLOWING THE TRANSACTION, NEWCO WILL CONTINUE THE HISTORIC BUSINESS OF OLDCO OR USE A SIGNIFICANT PORTION OF OLDCO'S HISTORIC BUSINESS ASSETS IN A BUSINESS.

11. THE SHAREHOLDERS WILL PAY THEIR RESPECTIVE EXPENSES, IF ANY, INCURRED IN CONNECTION WITH THE TRANSACTION.

12. OLDCO IS NOT UNDER THE JURISDICTION OF A COURT IN A TITLE 11 OR SIMILAR CASE WITHIN THE MEANING OF SECTION 368(a)(3)(A) OF THE INTERNAL REVENUE CODE.

.08 Miscellaneous representations to be submitted, if applicable:

1. THE PAYMENT OF CASH IN LIEU OF FRACTIONAL SHARES OF (ACQUIRING, PARENT, OR OLDCO) STOCK IS SOLELY FOR THE PURPOSE OF AVOIDING THE EXPENSE AND INCONVENIENCE TO (ACQUIRING, PARENT, OR OLDCO) OF ISSUING FRACTIONAL SHARES AND DOES NOT REPRESENT SEPARATELY BARGAINED-FOR CONSIDERATION. THE TOTAL CASH CONSIDERATION THAT WILL BE PAID IN THE TRANSACTION TO THE TARGET SHAREHOLDERS INSTEAD OF ISSUING FRACTIONAL SHARES OF (ACQUIRING, PARENT, OR OLDCO) STOCK WILL NOT EXCEED ONE PERCENT OF THE TOTAL CONSIDERATION THAT WILL BE ISSUED IN THE TRANSACTION TO THE TARGET SHAREHOLDERS IN EXCHANGE FOR THEIR SHARES OF TARGET STOCK. THE FRACTIONAL SHARE INTERESTS OF EACH TARGET SHAREHOLDER WILL BE AGGREGATED, AND NO TARGET SHAREHOLDER WILL RECEIVE CASH IN AN AMOUNT EQUAL TO OR GREATER THAN THE VALUE OF ONE FULL SHARE OF (ACQUIRING, PARENT, OR OLDCO) STOCK.

2. NONE OF THE COMPENSATION RECEIVED BY ANY SHAREHOLDER-EMPLOYEES OF TARGET WILL BE SEPARATE CONSIDERATION FOR, OR ALLOCABLE TO, ANY OF THEIR SHARES OF TARGET STOCK; NONE OF THE SHARES OF ACQUIRING STOCK RECEIVED BY ANY SHAREHOLDER-EMPLOYEES WILL BE SEPARATE CONSIDERATION FOR, OR ALLOCABLE TO, ANY EMPLOYMENT AGREEMENT; AND THE COMPENSATION PAID TO ANY SHAREHOLDER-EMPLOYEES WILL BE FOR SERVICES ACTUALLY RENDERED AND WILL BE COMMENSURATE WITH AMOUNTS PAID TO THIRD PARTIES BARGAINING AT ARM'S-LENGTH FOR SIMILAR SERVICES.

3. ACQUIRING WILL PAY OR ASSUME ONLY THOSE EXPENSES OF TARGET THAT ARE SOLELY AND DIRECTLY RELATED TO THE TRANSACTION IN ACCORDANCE WITH THE GUIDELINES ESTABLISHED IN REV. RUL. 73–54, 1973–1 C.B. 187.

SEC. 4. EFFECTIVE DATE

This revenue procedure will apply to all ruling requests received in the National Office subsequent to November 10, 1986, the date of publication of this revenue procedure in the Internal Revenue Bulletin.

SEC. 5. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 77–37 is amplified.

Part IV. Items of General Interest

Instructions for Payment of Interest on Tax Deficiencies

Announcement 86–108

The Tax Reform Act of 1986 provides that interest on most tax deficiencies of non-corporate taxpayers will be treated as "personal interest" and will not be fully deductible after 1986. As a result, taxpayers may wish to pay actual or contested tax deficiencies in 1986 in order to assure that interest paid on such deficiencies will be fully deductible on their 1986 returns. The purpose of this announcement is to provide guidance to such taxpayers. This announcement interprets, and expands upon, the formal advice given to taxpayers concerning payments of deficiencies in Revenue Procedure 84–58, 1984–2 C.B. 501.

A. *General Considerations*

The following general considerations should aid in understanding the detailed instructions that follow.

1. Taxpayers should carefully review this announcement to assure that their payments can be properly credited by the Service. Despite its desire to assist taxpayers in settling their tax obligations, the Service can apply payments to interest accrued on tax deficiencies only if certain formalities are observed. To assure that the correct amount of a payment is posted as interest, the taxpayer should submit the appropriate form with any payment in order to enable the Service to assess the tax. Failure to observe these formalities may cause the payment to be applied to the taxpayer's underlying tax deficiency or to be posted to the taxpayer's account as a "cash bond." In either case, the taxpayer would receive no interest deduction for 1986.

2. Taxpayers will be bound by the consequences of paying contested liabilities. For example, a taxpayer who pays his or her entire potential tax liability before receiving a Statutory Notice of Deficiency will not have the right to petition the Tax Court for a redetermination of the deficiency and refund of such payment; instead, such a taxpayer will be able to obtain a refund only by successfully suing the Government in the Claims Court or a U.S. District Court. Similarly, a taxpayer who not only pays a deficiency but agrees to concede a case that is being contested in Tax Court may neither file a later claim for refund nor litigate the claim in either the Claims Court or the U.S. District Court.

As another example, if an investor in a tax shelter partnership that is not subject to the partnership audit rules (Code sections 6221–6233) pays a contested amount and if, at a later date, the Service offers to settle other similar cases on more favorable terms, the Service will not refund to the investor the excess of the amount paid in 1986 over the amount that the investor would have been required to pay under the later settlement offer.

3. The Service does not have the resources to accelerate the conclusion of a large number of examinations during 1986. Thus, a taxpayer whose returns are currently under examination may not know before the end of 1986 whether the revenue agent will propose deficiencies with respect to such returns. In these circumstances, the taxpayer may have to estimate the amount that he or she believes the revenue agent will propose as a tax deficiency and file an amended return that reflects such amount of additional tax for the year in question.

Furthermore, even those taxpayers who have received a Notice of Proposed Deficiency (or "30-day letter") indicating the amount that the revenue agent has proposed as a deficiency with respect to a particular tax return may have difficulty obtaining necessary assistance from the Service Appeals Officer or revenue agent assigned to their case, if they do not contact the Appeals Officer or revenue agent immediately. Ordinarily, taxpayers will be dealt with on a "first come, first served" basis; in most cases, however, the taxpayer will be able to make the appropriate payment without assistance from the Service.

4. In general, a taxpayer may not pay interest on a contested deficiency without simultaneously paying, or agreeing to pay, the underlying tax deficiency with respect to which the interest is being paid. A taxpayer may satisfy this requirement if the payment consists of interest accrued on a tax that has already been paid or if the taxpayer designates as interest an amount that is proportionate to the tax being paid for the year in question. For example, if a taxpayer has an asserted tax deficiency of $12,000 on which $6,000 of interest has accrued, the taxpayer may not simply pay $6,000 and designate the entire payment as interest. However, the taxpayer may pay $6,000 and designate up to $2,000 as interest, in which case the Service will apply the remaining $4,000 of the payment to the underlying tax deficiency. Similarly, if the taxpayer previously has paid $5,000 of the asserted $12,000 tax deficiency, the taxpayer may designate as interest the amount that accrued on the $5,000 prior to its payment, as well as the interest that subsequently has accrued with respect to that interest.

5. In limited circumstances, a taxpayer who agrees to pay a contested tax liability may pay the interest attributable to the deficiency before paying the actual amount of the deficiency. For example, if a taxpayer has received a Notice of Proposed Deficiency asserting a $10,000 tax liability, the taxpayer may execute the Form 870 enclosed with the Notice of Proposed Deficiency or may file an amended return (Form 1040X) for the year in question. If $5,000 of interest has accrued on the deficiency, the taxpayer may tender a payment of $5,000 with the executed Form 870 and request that the payment be applied to the accrued interest, and the Service will credit the entire payment to interest due on the deficiency. Taxpayers who utilize this procedure should understand, however, that, under normal collection procedures, the Service will bill them for the remaining tax deficiency and any subsequently accrued interest; if that amount is not paid when billed, the taxpayer's account will be turned over to the Collection Division for appropriate action.

6. Payments, once made and applied to tax deficiencies or interest thereon, cannot be refunded to the taxpayer, unless the Service or a Court later determines that the payment exceeds the taxpayer's legal liability for the year in question.

B. *Categories of Taxpayers*

Taxpayers wishing to make payments of contested or potentially contested tax deficiencies generally fall into one of several categories. The instructions that follow are provided for taxpayers in each category. The categories are:

(1) taxpayers who have petitioned the Tax Court for a redetermination of a de-

ficiency asserted by the Service in a Statutory Notice of Deficiency (a "90-day letter");

(2) taxpayers who have received a Statutory Notice of Deficiency, but have neither agreed to the proposed deficiency nor filed a petition for redetermination by the Tax Court;

(3) taxpayers whose returns have been examined by the Service and who have received a Notice of Proposed Deficiency (a "30-day letter"), but who have not received a Statutory Notice of Deficiency; and

(4) taxpayers who have not received the final results of a pending examination of their returns by the Service, as well as those who have been notified that their returns are to be examined, but as to which no actual examination has commenced.

C. *Detailed Instructions*

This section provides instructions to taxpayers falling into the categories enumerated above. Taxpayers should identify the category that corresponds to their situation and review the applicable instructions. Special rules may apply to taxpayers whose returns are involved in an entity-level audit under the partnership or S corporation audit rules. Those rules will be described in a subsequent announcement.

1. *Taxpayers Who Have Petitioned the Tax Court.*

a. *Taxpayers Desiring to Concede Their Tax Court Cases.* A taxpayer whose case is pending before the Tax court and who wishes to settle the case by conceding the entire asserted deficiency should contact the Service attorney or Appeals Officer who is assigned to the case. The attorney or Appeals Officer will prepare a decision document, through which the proposed deficiency will be incorporated into a final court decision. Such a final decision is binding on the taxpayer and may not be further contested in any court.

If a taxpayer executes a decision document agreeing to pay the entire amount in controversy before the Tax Court, the taxpayer may pay the accrued interest on the deficiency before the Service actually bills the taxpayer for the underlying deficiency amount. In making this payment, the taxpayer may estimate the amount due as interest, even if the amount of accrued interest has not been determined prior to execution of the decision document. In such a case, if the total amount of the deficiency and accrued interest exceeds the amount paid, the taxpayer will be billed for the balance. If the amount paid exceeds the amount of interest that had accrued as of the date of the payment, the excess will be applied to the underlying tax deficiency; any such excess is nondeductible.

b. *Taxpayers Desiring to Settle Their Tax Court Cases.* A taxpayer whose case is pending before the Tax Court and who wishes to settle the case on some basis other than a full concession should immediately contact the Service attorney or Appeals Officer who is assigned to the case. If a settlement is agreed to, the attorney or Appeals Officer will prepare the appropriate decision document. If the Service is unable to provide the taxpayer with a decision document in 1986, the taxpayer may utilize the procedure outlined in the next subsection, relating to taxpayers who wish to make payment on asserted deficiencies while continuing to litigate their cases in Tax Court. Under these circumstances, the appropriate Service attorney or Appeals Officer will process the decision document as soon as possible in 1987.

If the Service and the taxpayer are unable to reach agreement on a settlement, the taxpayer may utilize the procedure outlined immediately below for taxpayers who wish to make payment on asserted deficiencies being contested in Tax Court while continuing to litigate their cases in Tax Court.

c. *Taxpayers Desiring to Make a Payment in 1986, While Continuing to Contest the Asserted Deficiency in Tax Court.* A taxpayer whose case is pending in Tax Court may pay all or any portion of the amount in controversy in Tax Court and continue to litigate his or her case. In order to obtain an interest deduction for a payment made in 1986 while continuing to litigate in Tax Court, the taxpayer must simultaneously pay the amount of the contested tax deficiency to which the interest being paid is attributable. For example, if the amount of tax in controversy is $20,000 and the interest accrued on the contested tax liability is $10,000, the taxpayer can obtain an interest deduction of $5,000 only by tendering a total payment of $15,000 *and* designating that $5,000 of such payment be applied to interest on the contested tax liability. If the taxpayer fails to make any designation with such payment, the entire payment will be applied to the contested tax deficiency and no amount will be applied to interest on such deficiency.

Payments made under this procedure should be delivered to the Service attorney or Appeals Officer who is handling the case. If the final decision of the Tax Court is adverse to the taxpayer, the taxpayer will be billed for only the excess of the total deficiency and accrued interest over the amount paid; if the final decision is favorable to the taxpayer, any excess payments will be refunded to the taxpayer.

2. *Taxpayers Who Have Received a Statutory Notice of Deficiency But Have Not Petitioned the Tax Court.*

a. *Taxpayers Who Do Not Wish to Contest Their Notice of Deficiency.* If the taxpayer has received a Statutory Notice of Deficiency but has not petitioned the Tax Court and does not wish to contest the asserted deficiency, the taxpayer should sign the Form 870 included with the Statutory Notice and return it to the Service. If the taxpayer tenders a payment with the Form 870 and requests that the payment be applied to interest accrued on the deficiency, the Service will apply the payment first to the interest and then to the tax deficiency, and will bill the taxpayer for the remaining deficiency amount.

b. *Taxpayers Who Wish to Petition the Tax Court.* If the taxpayer has received a Statutory Notice of Deficiency and wishes to petition the Tax Court within the statutory period for a redetermination of such deficiency, the taxpayer may make a full or partial payment with respect to the asserted deficiency in 1986 without losing the right to petition the Tax Court for a redetermination of the deficiency. The taxpayer should tender, to the Service office that issued the Notice, a payment accompanied by a written statement designating the specific portion of the payment to be applied to interest and the portion to be applied to the asserted deficiency. The taxpayer must pay a proportionate amount of the underlying tax deficiency. Rev. Proc. 84–58, 1984–2 C.B. 501. If such a payment is made and no portion of the payment is designated as interest, the entire payment will be applied first against the asserted tax liability, then against asserted penalties, and only the remainder will be applied against interest accrued on the contested deficiency.

3. *Taxpayers Who Have Received a Notice of Proposed Deficiency.*

a. *Taxpayers Who Do Not Wish to Contest the Notice.* If the taxpayer has received a Notice of Proposed Deficiency and does not wish to contest the liability, the taxpayer should execute the Form 870 enclosed with the Notice of Proposed Deficiency and tender a payment for some or all of the asserted tax deficiency, penalties (if any), and accrued interest. The taxpayer may request that a partial payment be applied first against the accrued interest.

In lieu of the Form 870, the taxpayer may file with the appropriate Service Center an amended return (Form 1040X) for the year in question, reflecting the proposed deficiency on the return and tendering a payment for some or all of the entire amount of the asserted deficiency and accrued interest. As with an executed Form 870, the taxpayer may request that a partial payment be applied first against accrued interest.

If a taxpayer executes a Form 870 or files a Form 1040X for the entire amount of the proposed deficiency and accured interest and tenders only a partial payment, the Service will bill the taxpayer for the balance. If the taxpayer later wishes to reopen the case, the taxpayer must pay the balance due and file a claim for refund with the Service. If the claim is denied, the taxpayer will be required to file a suit in the Claims Court or U.S. District Court to recover the amount paid.

b. *Taxpayers Who Wish to Contest Some or All of the Notice*. If the taxpayer wishes to contest one or more items reflected in the Notice of Proposed Deficiency, the taxpayer has several options. First, the taxpayer may execute a Form 870 or 1040X with respect to some, but not all, of the proposed deficiency. As discussed above, the taxpayer may tender with the Form 870 or 1040X a payment allocated solely to interest, and the Service will bill the taxpayer for the balance; however, the interest payment may not exceed the amount accrued with respect to the increased liability reflected on the Form 870 or 1040X. If the total amount of the prior payments of tax is less than the entire amount of the tax that ultimately is asserted to have been due, the Service will issue the taxpayer a Statutory Notice of Deficiency and the taxpayer may petition the Tax Court for redetermination of the deficiency.

Alternatively, the taxpayer may file a Form 870 or Form 1040X with respect to the entire amount of the asserted deficiency. As discussed above, however, if the taxpayer's tax payments exceed the proposed adjustments, the taxpayer will be able to contest the asserted deficiency only by filing a claim for refund.

4. *Taxpayers Who Have Been Notified That Their Returns Are Under Examination, But Have Not Received Either a Notice of Proposed Deficiency or a Statutory Notice of Deficiency.*

In general, an interest deduction is not available for federal income tax purposes for any payment that is not attributable to indebtedness. Thus, if a taxpayer's return is under examination but the examination has not progressed to the point at which a proposed deficiency can be asserted, the taxpayer cannot make a payment and assure that it will be respected as interest for federal income tax purposes.

In such a case, however, the taxpayer may file an amended return (Form 1040X) for the year in question that reflects adjustments that the taxpayer expects may be asserted. As discussed above, the taxpayer may pay the entire amount shown to be due on the amended return, or the taxpayer may make a partial payment and request that it be applied first against the interest accrued on the underpayment of the recomputed tax. In the event of a partial payment, the Service will bill the taxpayer for the balance due.

If the Service completes the examination and later issues a Statutory Notice of Deficiency, the taxpayer will retain the right eventually to petition the Tax Court for redetermination of his or her entire liability for the year under examination. If the Service does not issue a Statutory Notice of Deficiency (because the taxpayer's payment exceeds the proposed adjustments) and the taxpayer wishes to reopen the case, the taxpayer will be able to obtain a refund for any overpayment only by filing a claim for refund with the Service. If the Service denies the claim, the taxpayer will be required to file a suit in the Claims Court or U.S. District Court to recover the amount paid.

Lists of Master and Prototype Plans Closed or Otherwise Disposed of Between July 1, 1986 and September 30, 1986, and Plans Omitted from Announcement 85–99

Announcement 86–109

This Announcement contains two lists of master and prototype (M&P) pension, annuity or profit-sharing plans submitted to the National Office of the Internal Revenue Service during 1984 by sponsoring organizations and mass submitters.

The first list (List A) includes those M&P plans that were timely submitted under Revenue Procedure 84–23, 1984–1 C.B. 457, by December 31, 1984, and were closed or otherwise disposed of by the Service between July 1, 1986, and September 30, 1986.

List A contains the names and addresses of the plans' sponsoring organization or mass submitter, symbols indicating the type of plan, and file folder number. It also shows the date of disposition of the plan and the type of disposition as follows: (1) favorable opinion letter (F), (2) unfavorable/nonopinion letter(U), (3) withdrawal letter(W), or (4) other(O).

Employers that adopted an approved M&P plan and, if appropriate, requested a determination letter on or before March 19, 1984, and received a favorable determination letter, retained reliance on their favorable letter under the provisions of Section 12 of Rev. Proc. 84–23. Other adopting employers will have the provisions of Section 12 of Rev. Proc. 84–23 applied to them also, provided the conditions outlined in Announcement 86–60, 1986–19 I.R.B. 17 are met. In either case, if the approved plan is included in List A, the employer must take further action in order to have continued reliance and to meet the compliance date described in Announcement 86–60.

If List A shows that the plan adopted by the employer received a favorable opinion letter, the employer must, within 12 months after the sponsor received the favorable letter, either (1) amend its existing plan by adopting the sponsor's M&P plan as approved by the Service, or (2) adopt an M&P plan of another sponsor on List A or another quarterly list, that has received a favorable letter (See Announcement 85–130, 1985–36 I.R.B. 58).

If List A shows that the plan was closed other than by issuance of a favorable opinion letter, such employer must either (1) make all amendments required by Section 5 of Rev. Proc. 84–23, including amendments to conform with the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) Pub. L. 97–248, 1982–2 C.B. 462, the Tax Reform Act of 1984 (TRA) Pub. L. 98–369, 1984–3 (Vol. 1) C.B. 1, and the Retirement Equity Act of 1984 (REA) Pub. L. 98–397, 1984–2 C.B. 433, and submit a request for a determination letter to the appropriate key district office, or (2) adopt an approved M&P plan of a sponsor that has received a favorable opinion letter and is listed in either Announcement 85–99, 1985–28 I.R.B. 4, or List B of this or the following Announcements: 85–165, 1985–47 I.R.B. 4; 86–43, 1986–14 I.R.B. 13, 86–70, 1986–21 I.R.B. 33, or 86–86, 1986–30 I.R.B. 7. In order to be afforded continued reliance and to meet the compliance date described in Announcement 86–60 the employer must adopt the amended plan by May 31, 1987.

After amending its existing plan or adopting another M&P plan, an employer must request a determination letter from the appropriate key district office in order to rely on the plan's qualification unless the employer adopts a standardized or paired plans within the meaning of Section 6.01 of Rev. Proc. 84–23.

The second list in this Announcement (List B) includes those M&P plans that were inadvertently omitted from the list published in Announcement 85–99. See Announcement 85–99 regarding when these plans must be adopted.

LISTING OF MASTER OR PROTOTYPE PLANS

Abbreviations:

Type of Closing
F = Favorable
U = Unfavorable/nonopinion
W = Withdrawal
O = Other

Type of Plan
P = Paired
S = Standardized (not paired)
NS = Nonstandardized
M = Money Purchase
T = Target Benefit
D = Defined Benefit

LIST A

Sponsors of Master and Prototype Plans

Allstate Life Insurance Co;Northbrook;IL; 50202160003-001; S; M; F; 09/22/86
American Dental Association;Chicago;IL; 50202680001-001; P; PS; F; 08/11/86
American Dental Association;Chicago;IL; 50202680001-002; P; M; F; 08/11/86
American Dental Association;Chicago;IL; 50302680001-003; NS; PS; F; 08/11/86
American Dental Association;Chicago;IL; 50302680001-004; NS; M; F; 08/11/86
American Exchange Bank;Madison;WI; 50302710001-001; NS; PS; F; 08/15/86
American Exchange Bank;Madison;WI; 50302710001-002; NS; PS; F; 08/15/86
American Exchange Bank;Madison;WI; 50302710001-003; NS; M; F; 08/15/86
American Exchange Bank;Madison;WI; 50302710001-004; NS; M; F; 08/15/86
American Health & Life Insurance Co;Baltimore;MD; 50202920001-003; S; PS; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50202920001-004; S; PS; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50202920002-003; S; PS; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50202920002-004; S; PS; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50202920003-003; S; M; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50202920003-004; S; M; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50202920004-003; S; M; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50202920004-004; S; M; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50302920001-001; NS; PS; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50302920001-002; NS; PS; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50302920002-001; NS; PS; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50302920002-002; NS; PS; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50302920003-001; NS; M; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50302920003-002; NS; M; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50302920004-001; NS; M; F; 09/22/86
American Health & Life Insurance Co;Baltimore;MD; 50302920004-002; NS; M; F; 09/22/86
American National Bank;Omaha;NE; 50303200001-001; NS; PS; F; 08/01/86
American National Bank;Omaha;NE; 50303200001-002; NS; M; F; 07/02/86
American National Bank & Trust Co of Michigan;Kalamazoo;MI; 50203330001-001; S; PS; F; 09/18/86
American National Bank & Trust Co of Michigan;Kalamazoo;MI; 50203330001-002; S; M; F; 09/18/86
American National Life Insurance Co;Galveston;TX; 50203520001-001; P; D; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50203520001-002; P; D; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50203520002-001; P; M; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50203520002-002; P; PS; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50203520002-006; S; T; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50303520001-003; NS; D; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50303520001-004; NS; D; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50303520001-005; NS; D; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50303520002-003; NS; M; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50303520002-004; NS; PS; F; 07/16/86
American National Life Insurance Co;Galveston;TX; 50303520002-005; NS; T; F; 07/16/86
American Optometric Association;St Louis;MO; 50203560001-001; P; PS; F; 08/11/86
American Optometric Association;St Louis;MO; 50203560001-002; P; M; F; 08/11/86
American Optometric Association;St Louis;MO; 50303560001-003; NS; PS; F; 08/11/86
American Optometric Association;St Louis;MO; 50303560001-004; NS; M; F; 08/11/86
Ameritrade Inc;Omaha;NE; 50258850001-001; P; PS; F; 08/08/86
Ameritrade Inc;Omaha;NE; 50258850001-002; P; M; F; 08/08/86
AmeriTrust Co NA;Cleveland;OH; 50203980001-001; S; M; F; 09/18/86
AmeriTrust Co NA;Cleveland;OH; 50203980001-002; S; PS; F; 09/18/86
AmeriTrust Co NA;Cleveland;OH; 50203980001-003; S; M; F; 09/18/86
AmeriTrust Co NA;Cleveland;OH; 50203980001-004; S; PS; F; 09/18/86
AmeriTrust Co NA;Cleveland;OH; 50203980002-001; S; M; F; 09/18/86
AmeriTrust Co NA;Cleveland;OH; 50203980002-002; S; PS; F; 09/18/86
AmeriTrust Co NA;Cleveland;OH; 50303980003-001; NS; M; F; 09/18/86
AmeriTrust Co NA;Cleveland;OH; 50303980004-001; NS; PS; F; 09/18/86
AmeriTrust Co NA;Cleveland;OH; 50303980005-001; NS; M; F; 09/18/86
AmeriTrust Co NA;Cleveland;OH; 50303980006-001; NS; PS; F; 09/18/86
Arlington Trust Co;Lawrence;MA; 50371870001-001; NS; PS; F; 08/08/86
Arlington Trust Co;Lawrence;MA; 50371870001-002; NS; M; F; 08/08/86
Arlington Trust Co;Lawrence;MA; 50371870002-001; NS; PS; F; 08/08/86
Arlington Trust Co;Lawrence;MA; 50371870003-001; NS; M; F; 08/08/86
Associated Administrative Co;Van Nuys;CA; 50204500001-001; S; PS; F; 09/25/86
Auto-Owners Life Insurance Co;Lansing;MI; 50204780001-001; P; M; F; 09/26/86
Auto-Owners Life Insurance Co;Lansing;MI; 50204780001-003; P; PS; F; 09/26/86
Auto-Owners Life Insurance Co;Lansing;MI; 50204780002-001; P; D; F; 09/26/86
Auto-Owners Life Insurance Co;Lansing;MI; 50204780002-003; P; D; F; 09/26/86
Auto-Owners Life Insurance Co;Lansing;MI; 50304780001-002; NS; M; F; 09/26/86
Auto-Owners Life Insurance Co;Lansing;MI; 50304780001-004; NS; PS; F; 09/26/86
Auto-Owners Life Insurance Co;Lansing;MI; 50304780002-002; NS; D; F; 09/26/86
Auto-Owners Life Insurance Co;Lansing;MI; 50304780002-004; NS; D; F; 09/26/86
Baltimore Life Insurance Co;Baltimore;MD; 50204930001-001; S; M; F; 09/24/86
Bancroft Convertible Fund Inc;New York;NY; 50204960001-001; P; PS; F; 09/24/86
Bancroft Convertible Fund Inc;New York;NY; 50204960001-002; P; M; F; 09/24/86
Bancroft Convertible Fund Inc;New York;NY; 50304960001-003; NS; PS; F; 09/24/86
Bancroft Convertible Fund Inc;New York;NY; 50304960001-004; NS; M; F; 09/24/86
Bank of Commerce & Trust Co;Lexington;KY; 50204150001-002; P; M; F; 09/18/86
Bank of Commerce & Trust Co;Lexington;KY; 50204150001-004; P; PS; F; 09/18/86
Bank of Commerce & Trust Co;Lexington;KY; 50304150001-001; NS; M; F; 09/18/86
Bank of Commerce & Trust Co;Lexington;KY; 50304150001-003; NS; PS; F; 09/18/86
Bank of Elkhorn;Elkhorn;NE; 50205590001-001; P; PS; F; 08/08/86
Bank of Elkhorn;Elkhorn;NE; 50205590001-002; P; M; F; 08/08/86
Bank of Lexington & Trust Co;Lexington;KY; 50206060001-002; P; M; F; 09/29/86
Bank of Lexington & Trust Co;Lexington;KY; 50206060001-004; P; PS; F; 09/29/86
Bank of Lexington & Trust Co;Lexington;KY; 50306060001-001; NS; M; F; 09/29/86
Bank of Lexington & Trust Co;Lexington;KY; 50306060001-003; NS; PS; F; 09/29/86
Bank of Mississippi;Tupelo;MS; 50306230001-001; NS; PS; F; 09/26/86
Bank of Mississippi;Tupelo;MS; 50306230001-002; NS; M; F; 09/26/86
Bank of San Diego;San Diego;CA; 50206640001-001; S; PS; F; 09/22/86
Bank of San Diego;San Diego;CA; 50206640002-001; S; M; F; 09/22/86
Bank of San Diego;San Diego;CA; 50306640001-002; NS; PS; F; 09/22/86
Bank of San Diego;San Diego;CA; 50306640001-003; NS; PS; F; 09/22/86
Bank of San Diego;San Diego;CA; 50306640001-004; NS; PS; F; 09/22/86
Bank of San Diego;San Diego;CA; 50306640002-002; NS; M; F; 09/22/86
Bank of San Diego;San Diego;CA; 50306640002-003; NS; M; F; 09/22/86
Bank of San Diego;San Diego;CA; 50306640002-004; NS; M; F; 09/22/86
Bank of San Diego;San Diego;CA; 50306640003-001; NS; D; F; 09/01/86
Bank of San Diego;San Diego;CA; 50306640003-002; NS; D; F; 09/01/86
Bank of San Diego;San Diego;CA; 50306640003-003; NS; D; F; 09/01/86
Bank of San Diego;San Diego;CA; 50306640003-004; NS; D; F; 09/01/86
Bank of San Diego;San Diego;CA; 50306640003-005; NS; D; F; 09/01/86
Bank One Akron NA;Akron;OH; 50207310001-001; S; PS; F; 08/06/86
Bank One Akron NA;Akron;OH; 50207310002-001; S; M; F; 08/06/86
Bank One Akron NA;Akron;OH; 50307310001-002; NS; PS; F; 08/06/86
Bank One Akron NA;Akron;OH; 50307310002-002; NS; M; F; 08/06/86
Bank One Columbus NA;Columbus;OH; 50207240001-001; S; PS; F; 08/25/86
Bank One Columbus NA;Columbus;OH; 50207240001-002; S; M; F; 08/25/86
Bank One Trust Co NA;Columbus;OH; 50229070001-001; S; PS; F; 08/25/86
Bank One Trust Co NA;Columbus;OH; 50229070003-001; S; M; F; 08/25/86
Bank One Trust Co NA;Columbus;OH; 50329070002-001; NS; PS; F; 08/25/86
Bank One Trust Co NA;Columbus;OH; 50329070004-001; NS; M; F; 08/25/86
Bear Stearns & Co;New York;NY; 50207960001-001; P; M; F; 09/01/86
Bear Stearns & Co;New York;NY; 50207960001-002; P; PS; F; 09/01/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-001; P; PS; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-002; P; M; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-003; P; PS; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-004; P; PS; F; 07/31/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-005; P; M; F; 07/31/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-006; P; M; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-011; P; PS; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-012; P; M; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-013; P; PS; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-014; P; PS; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-015; P; M; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50208310001-016; P; M; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50308310001-007; NS; PS; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50308310001-008; NS; PS; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50308310001-009; NS; M; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50308310001-010; NS; M; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50308310001-017; NS; PS; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50308310001-018; NS; PS; F; 07/30/86
Beverly Hills Bar Association;Beverly Hills;CA; 50308310001-019; NS; M; F; 07/30/86

Beverly Hills Bar Association;Beverly Hills;CA; 50308310001-020; NS; M; F; 07/30/86
Boatmens Bank of Cape Girardeau;Cape Girardeau;MO; 50208520001-001; S; PS; F; 08/29/86
Boatmens National Bank of St Louis;St Louis;MI; 50208540001-001; P; PS; F; 09/08/86
Boatmens National Bank of St Louis;St Louis;MI; 50208540001-002; P; PS; F; 09/08/86
Boatmens National Bank of St Louis;St Louis;MI; 50208540001-005; P; M; F; 09/08/86
Boatmens National Bank of St Louis;St Louis;MI; 50208540001-006; P; M; F; 09/08/86
Boatmens National Bank of St Louis;St Louis;MI; 50208540002-001; S; PS; F; 08/29/86
Boatmens National Bank of St Louis;St Louis;MI; 50308540001-003; NS; PS; F; 09/08/86
Boatmens National Bank of St Louis;St Louis;MI; 50308540001-004; NS; PS; F; 09/08/86
Boatmens National Bank of St Louis;St Louis;MI; 50308540001-007; NS; M; F; 09/08/86
Boatmens National Bank of St Louis;St Louis;MI; 50308540001-008; NS; M; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50239900001-001; S; PS; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50239900001-002; S; PS; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50239900001-005; S; M; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50239900001-006; S; M; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50239900004-001; S; PS; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50239900004-002; S; PS; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50239900004-003; S; M; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50339900001-003; NS; PS; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50339900001-004; NS; PS; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50339900001-007; NS; M; F; 09/08/86
Boatmens Trust Co;Clayton;MI; 50339900001-008; NS; M; F; 09/08/86
Bourbon Agricultural Deposit Bank & Trust Co;Paris;KY; 50208690001-002; P; M; F; 09/29/86
Bourbon Agricultural Deposit Bank & Trust Co;Paris;KY; 50208690001-004; P; PS; F; 09/29/86
Bourbon Agricultural Deposit Bank & Trust Co;Paris;KY; 50308690001-001; NS; M; F; 09/29/86
Bourbon Agricultural Deposit Bank & Trust Co;Paris;KY; 50308690001-003; NS; PS; F; 09/29/86
Bridges Investment Fund Inc;Omaha;NE; 50262110001-001; S; M; F; 09/17/86
Bridges Investment Fund Inc;Omaha;NE; 50262110001-002; S; PS; F; 09/17/86
Camden County Bar Association;Camden;NJ; 50213930001-001; P; M; F; 09/08/86
Camden County Bar Association;Camden;NJ; 50213930001-002; P; PS; F; 09/08/86
Casco Northern Bank NA;Portland;ME; 50209990002-001; S; PS; U; 08/13/86
Casco Northern Bank NA;Portland;ME; 50209990002-002; S; M; U; 08/13/86
Casco Northern Bank NA;Portland;ME; 50209990003-001; S; PS; U; 08/13/86
Central Bank;Walnut Creek;CA; 50210590001-001; S; PS; F; 08/15/86
Central Bank;Walnut Creek;CA; 50210590001-002; S; M; F; 08/15/86
Central Bank;Walnut Creek;CA; 50210590003-001; S; M; F; 08/29/86
Central Bank;Walnut Creek;CA; 50210590004-001; S; PS; F; 08/29/86
Central National Bank;San Angelo;TX; 50210880001-001; P; PS; O; 09/24/86
Central National Bank;San Angelo;TX; 50210880001-002; P; M; O; 09/25/86
Charles Schwab & Co Inc;San Francisco;CA; 50262470001-001; P; M; F; 09/01/86
Charles Schwab & Co Inc;San Francisco;CA; 50262470001-002; P; PS; F; 09/01/86
Chase Bank of Florida NA;St Petersburg;FL; 50245860001-001; P; PS; F; 07/21/86
Chase Bank of Florida NA;St Petersburg;FL; 50245860001-002; P; M; F; 07/21/86
Chicago Title & Trust Co;Chicago;IL; 50311690001-001; NS; PS; F; 08/18/86
Citizens Bank & Trust Co;Chillicothe;MO; 50312230001-001; NS; PS; F; 08/11/86
Citizens Bank & Trust Co;Chillicothe;MO; 50312230002-001; NS; M; F; 08/11/86
Citizens Bank & Trust Co;Chillicothe;MO; 50312230002-002; NS; PS; F; 08/11/86
Citizens Commercial Trust & Savings Bank of Pasadena;Pasadena;CA; 50312550001-002; NS; PS; O; 08/15/86
Citizens Commercial Trust & Savings Bank of Pasadena;Pasadena;CA; 50312550002-002; NS; M; O; 08/15/86
Citizens Commercial Trust & Savings Bank of Pasadena;Pasadena;CA; 50312550003-002; NS; D; O; 08/15/86
Citizens National Bank of Bowling Green;Bowling Green;KY; 50212990001-002; P; M; F; 09/29/86
Citizens National Bank of Evansville;Evansville;IN; 50212641801-001; P; M; F; 07/28/86
Citizens National Bank of Evansville;Evansville;IN; 50212641801-003; P; PS; F; 07/28/86
Citizens National Bank of Evansville;Evansville;IN; 50312641801-002; NS; M; F; 07/28/86
Citizens National Bank of Evansville;Evansville;IN; 50312641801-004; NS; PS; F; 07/28/86
CommerceNational Bank;Lexington;KY; 50250590001-002; P; M; F; 09/18/86
CommerceNational Bank;Lexington;KY; 50250590001-004; P; PS; F; 09/18/86
CommerceNational Bank;Lexington;KY; 50350590001-001; NS; M; F; 09/18/86
CommerceNational Bank;Lexington;KY; 50350590001-003; NS; PS; F; 09/18/86
Commercial Federal Savings & Loan Association;Omaha;NE; 50214940001-001; S; PS; F; 07/14/86
Commercial Federal Savings & Loan Association;Omaha;NE; 50214940001-002; S; M; F; 07/14/86
Commercial Federal Savings & Loan Association;Omaha;NE; 50214940002-001; S; T; F; 07/14/86
Commonwealth National Bank;Harrisburg;PA; 50215290001-002; P; PS; F; 08/04/86
Commonwealth National Bank;Harrisburg;PA; 50215290001-004; P; M; F; 08/04/86
Commonwealth National Bank;Harrisburg;PA; 50215290002-001; S; PS; F; 08/04/86
Commonwealth National Bank;Harrisburg;PA; 50215290002-002; S; M; F; 08/04/86
Commonwealth National Bank;Harrisburg;PA; 50215290002-003; S; PS; F; 08/04/86
Commonwealth National Bank;Harrisburg;PA; 50315290001-001; NS; PS; F; 08/04/86
Commonwealth National Bank;Harrisburg;PA; 50315290001-003; NS; M; F; 08/04/86
Community State Bank of Bloomington;Bloomington;MN; 50215510001-001; P; PS; F; 09/29/86
Community State Bank of Bloomington;Bloomington;MN; 50215510001-002; P; M; F; 09/29/86
Continental General Insurance Co;Omaha;NE; 50263180001-001; P; PS; F; 08/06/86
Continental General Insurance Co;Omaha;NE; 50263180001-002; P; M; F; 08/06/86
Country Capital Management Co;Bloomington;IL; 50216090002-001; S; PS; U; 08/13/86
Country Life Insurance Co;Bloomingon;IL; 50216100003-001; S; M; F; 08/11/86
Country Life Insurance Co;Bloomingon;IL; 50316100001-001; NS; M; F; 08/11/86
Country Life Insurance Co;Bloomingon;IL; 50316100001-002; NS; T; F; 08/11/86
Country Life Insurance Co;Bloomingon;IL; 50316100002-001; NS; PS; F; 08/11/86
Dean Witter Reynolds Inc;New York;NY; 50216610001-001; P; M; F; 08/14/86
Dean Witter Reynolds Inc;New York;NY; 50216610001-002; P; PS; F; 08/14/86
Dean Witter Reynolds Inc;New York;NY; 50316610001-003; NS; M; F; 08/14/86
Dean Witter Reynolds Inc;New York;NY; 50316610001-004; NS; PS; F; 08/14/86
Dean Witter Reynolds Inc;New York;NY; 50316610001-005; NS; T; F; 08/14/86
Dearborn Bank & Trust Co;Dearborn;MI; 50254091901-001; P; PS; F; 08/04/86
Dearborn Bank & Trust Co;Dearborn;MI; 50254091901-002; P; M; F; 08/04/86
Dearborn Bank & Trust Co;Dearborn;MI; 50354091901-003; NS; PS; F; 08/04/86
Dearborn Bank & Trust Co;Dearborn;MI; 50354091901-004; NS; M; F; 08/04/86
Douglas County Bank & Trust Co;Omaha;NE; 50217070001-001; S; PS; F; 07/30/86
Douglas County Bank & Trust Co;Omaha;NE; 50217070001-002; S; PS; F; 07/30/86
Douglas County Bank & Trust Co;Omaha;NE; 50217070002-001; S; M; F; 07/30/86
Douglas County Bank & Trust Co;Omaha;NE; 50217070002-002; S; M; F; 07/30/86
Douglas County Bank & Trust Co;Omaha;NE; 50317070001-003; NS; PS; F; 07/30/86
Douglas County Bank & Trust Co;Omaha;NE; 50317070001-004; NS; PS; F; 07/30/86
Douglas County Bank & Trust Co;Omaha;NE; 50317070002-003; NS; M; F; 07/30/86
Douglas County Bank & Trust Co;Omaha;NE; 50317070002-004; NS; M; F; 07/30/86
Drovers & Mechanics Bank;York;PA; 50252610001-002; P; PS; F; 07/31/86
Drovers & Mechanics Bank;York;PA; 50252610001-004; P; M; F; 07/31/86
Drovers & Mechanics Bank;York;PA; 50352610001-001; NS; PS; F; 07/31/86
Drovers & Mechanics Bank;York;PA; 50352610001-003; NS; M; F; 07/31/86
Equitable Life Assurance Society of the United States;New York;NY; 50217870004-001; S; M; F; 08/29/86
Equitable Life Assurance Society of the United States;New York;NY; 50217870005-001; S; M; F; 08/29/86
Equitable Life Assurance Society of the United States;New York;NY; 50317870008-001; NS; PS; F; 08/11/86
Equitable Life Assurance Society of the United States;New York;NY; 50317870008-002; NS; M; F; 08/11/86
Equitable Life Assurance Society of the United States;New York;NY; 50317870008-003; NS; PS; F; 08/11/86
Exchange National Bank of Chicago;Chicago;IL; 50218090001-001; P; PS; F; 08/18/86
Exchange National Bank of Chicago;Chicago;IL; 50218090001-002; P; M; F; 08/18/86
Far West Federal Bank;Portland;OR; 50271850001-001; S; PS; U; 08/18/86
Far West Federal Bank;Portland;OR; 50271850001-002; S; PS; U; 08/18/86
Far West Federal Bank;Portland;OR; 50271850002-001; S; M; U; 08/18/86
Far West Federal Bank;Portland;OR; 50271850002-002; S; M; U; 08/18/86
Far West Federal Bank;Portland;OR; 50271850003-001; S; D; U; 08/18/86
Far West Federal Bank;Portland;OR; 50271850003-002; S; D; U; 08/18/86
Farmers & Merchants Bank of Vandalia;Vandalia;IL; 50231580001-001; S; PS; U; 07/14/86
Farmers & Merchants Bank of Vandalia;Vandalia;IL; 50331580001-002; NS; PS; U; 07/14/86
Federal Life Insurance Co Mutual;Riverwoods;IL; 50219630001-001; P; PS; F; 09/04/86
Federal Life Insurance Co Mutual;Riverwoods;IL; 50219630001-002; P; M; F; 09/04/86
Fidelity Mutual Life Insurance Co;Radnor;PA; 50219920002-002; P; M; F; 06/25/86
Fidelity Mutual Life Insurance Co;Radnor;PA; 50219920002-004; P; PS; F; 06/25/86
Fidelity Mutual Life Insurance Co;Radnor;PA; 50319920002-001; NS; M; F; 06/25/86
Fidelity Mutual Life Insurance Co;Radnor;PA; 50319920002-003; NS; PS; F; 06/25/86
First Bank & Trust;Bryan;TX; 50320520001-001; NS; PS; F; 09/10/86
First Bank & Trust;Bryan;TX; 50320520001-002; NS; PS; F; 09/10/86
First Bank & Trust;Bryan;TX; 50320520002-001; NS; M; F; 09/10/86
First Bank & Trust;Bryan;TX; 50320520002-002; NS; M; F; 09/10/86
First Bulloch Bank & Trust Co;Statesboro;GA; 50321260001-001; NS; PS; F; 07/02/86
First Bulloch Bank & Trust Co;Statesboro;GA; 50321260001-002; NS; PS; F; 07/02/86
First City National Bank of Bryan;Bryan;TX; 50320110001-001; NS; PS; F; 09/10/86

First City National Bank of Bryan;Bryan;TX; 50320110001-002; NS; PS; F; 09/10/86
First City National Bank of Bryan;Bryan;TX; 50320110002-001; NS; M; F; 09/10/86
First City National Bank of Bryan;Bryan;TX; 50320110002-002; NS; M; F; 09/10/86
First Interstate Bank of Arizona NA;Phoenix;AZ; 50327260001-001; NS; PS; F; 08/01/86
First Interstate Bank of Arizona NA;Phoenix;AZ; 50327260001-002; NS; M; F; 08/01/86
First Interstate Bank of California;Los Angeles;CA; 50221940001-001; S; PS; U; 09/26/86
First Interstate Bank of California;Los Angeles;CA; 50221940001-002; S; M; U; 09/26/86
First Interstate Bank of Hawaii;Honolulu;HI; 50221960001-001; S; PS; U; 09/17/86
First Interstate Bank of Santa Fe NA;Santa Fe;NM; 50360470001-001; NS; PS; F; 09/24/86
First Interstate Bank of Santa Fe NA;Santa Fe;NM; 50360470001-002; NS; M; F; 09/24/86
First Investors Life Insurance Co;New York;NY; 50322040001-0[illegible]; NS; D; F; 07/16/86
First Investors Life Insurance Co;New York;NY; 50322040001-002; NS; D; F; 07/16/86
First Investors Life Insurance Co;New York;NY; 50322040001-003; NS; D; F; 07/16/86
First Investors Life Insurance Co;New York;NY; 50322040001-004; NS; D; F; 07/16/86
First Investors Life Insurance Co;New York;NY; 50322040002-001; NS; M; F; 09/29/86
First Investors Life Insurance Co;New York;NY; 50322040002-002; NS; M; F; 09/29/86
First Investors Life Insurance Co;New York;NY; 50322040003-001; NS; PS; F; 09/29/86
First Investors Life Insurance Co;New York;NY; 50322040003-002; NS; PS; F; 09/29/86
First National Bank;Dayton;OH; 50222300002-001; P; PS; F; 07/24/86
First National Bank;Dayton;OH; 50222300002-002; P; PS; F; 07/24/86
First National Bank;Dayton;OH; 50222300002-003; P; M; F; 07/24/86
First National Bank;Dayton;OH; 50222300002-004; P; M; F; 07/24/86
First National Bank;Dayton;OH; 50322300001-001; NS; PS; F; 07/24/86
First National Bank;Dayton;OH; 50322300001-002; NS; PS; F; 07/24/86
First National Bank;Dayton;OH; 50322300001-003; NS; M; F; 07/24/86
First National Bank;Dayton;OH; 50322300001-004; NS; M; F; 07/24/86
First National Bank & Trust Co;Escanaba;MI; 50223071803-001; S; M; F; 07/16/86
First National Bank & Trust Co;Escanaba;MI; 50223071803-002; S; PS; F; 07/16/86
First National Bank & Trust Co of Barrington;Barrington;IL; 50223340001-001; P; M; F; 09/17/86
First National Bank & Trust Co of Barrington;Barrington;IL; 50223340001-002; P; PS; F; 09/17/86
First National Bank in Brookings;Brookings;SD; 50223520001-001; S; M; F; 07/10/86
First National Bank in Brookings;Brookings;SD; 50223520001-002; S; PS; F; 07/10/86
First National Bank in Brookings;Brookings;SD; 50223520001-003; P; M; F; 07/10/86
First National Bank in Brookings;Brookings;SD; 50223520001-004; P; PS; F; 07/10/86
First National Bank in Brookings;Brookings;SD; 50223520002-001; S; M; F; 07/10/86
First National Bank in Brookings;Brookings;SD; 50223520002-002; S; PS; F; 07/10/86
First National Bank of Boston;Boston;MA; 50305190002-001; NS; D; F; 07/25/86
First National Bank of Boston;Boston;MA; 50305190002-002; NS; D; F; 07/25/86
First National Bank of Commerce;New Orleans;LA; 50224570001-001; S; PS; F; 07/28/86
First National Bank of Commerce;New Orleans;LA; 50224570001-002; S; PS; F; 07/28/86
First National Bank of Commerce;New Orleans;LA; 50224570001-003; S; M; F; 07/28/86
First National Bank of Commerce;New Orleans;LA; 50224570001-004; S; M; F; 07/28/86
First National Bank of Commerce;New Orleans;LA; 50324570001-005; NS; PS; F; 07/28/86
First National Bank of Commerce;New Orleans;LA; 50324570001-006; NS; PS; F; 07/28/86
First National Bank of Commerce;New Orleans;LA; 50324570001-007; NS; M; F; 07/28/86
First National Bank of Commerce;New Orleans;LA; 50324570001-008; NS; M; F; 07/28/86
First National Bank of Geneva;Geneva;IL; 50224950001-001; S; PS; F; 07/21/86
First National Bank of Geneva;Geneva;IL; 50224950001-002; S; PS; F; 07/21/86
First National Bank of Lancaster County;Lancaster;PA; 50225380001-002; P; PS; F; 08/04/86
First National Bank of Lancaster County;Lancaster;PA; 50225380001-004; P; M; F; 08/04/86
First National Bank of Lancaster County;Lancaster;PA; 50325380001-001; NS; PS; F; 08/04/86
First National Bank of Lancaster County;Lancaster;PA; 50325380001-003; NS; M; F; 08/04/86
First National Bank of Long Island;Woodbury;NY; 50225470001-001; P; PS; F; 08/08/86
First National Bank of Long Island;Woodbury;NY; 50225470001-002; P; M; F; 08/08/86
First National Bank of Long Island;Woodbury;NY; 50225470001-003; P; PS; F; 08/08/86
First National Bank of Long Island;Woodbury;NY; 50225470001-004; P; M; F; 08/08/86
First National Bank of Maryland;Baltimore;MD; 50225570001-001; P; PS; F; 08/18/86
First National Bank of Maryland;Baltimore;MD; 50225570001-002; P; M; F; 08/18/86
First National Bank of Maryland;Baltimore;MD; 50225570001-003; P; PS; F; 08/18/86
First National Bank of Maryland;Baltimore;MD; 50225570001-004; P; M; F; 08/18/86
First National Bank of Maryland;Baltimore;MD; 50325570001-005; NS; PS; F; 08/18/86
First National Bank of Maryland;Baltimore;MD; 50325570001-006; NS; M; F; 08/18/86
First National Bank of Maryland;Baltimore;MD; 50325570001-007; NS; PS; F; 08/18/86
First National Bank of Sullivan;Sullivan;IL; 50272180001-001; P; M; F; 09/08/86
First National Bank of Sullivan;Sullivan;IL; 50272180001-002; P; PS; F; 09/08/86
First National Bank of Winter Park;Winter Park;FL; 50259930001-003; P; M; F; 07/16/86
First National Bank of Winter Park;Winter Park;FL; 50259930001-004; P; PS; F; 07/16/86
First National Bank of Winter Park;Winter Park;FL; 50359930001-001; NS; M; F; 07/16/86
First National Bank of Winter Park;Winter Park;FL; 50359930001-002; NS; PS; F; 07/16/86
First Seneca Bank;Oil City;PA; 50328120001-001; NS; M; F; 09/01/86
First Seneca Bank;Oil City;PA; 50328120001-002; NS; PS; F; 09/01/86
First State Bank;Springdale;AR; 50228360001-002; P; M; F; 09/12/86
First State Bank;Springdale;AR; 50228360001-004; P; PS; F; 09/12/86
First State Bank;Springdale;AR; 50228360001-006; P; T; F; 09/12/86
First State Bank;Springdale;AR; 50328360001-001; NS; M; F; 09/12/86
First State Bank;Springdale;AR; 50328360001-003; NS; PS; F; 09/12/86
First State Bank;Springdale;AR; 50328360001-005; NS; T; F; 09/12/86
First United Trust Co;Oak Park;IL; 50344560001-001; NS; M; F; 09/29/86
First United Trust Co;Oak Park;IL; 50344560001-002; NS; M; O; 09/30/86
First United Trust Co;Oak Park;IL; 50344560002-001; NS; PS; F; 09/29/86
First United Trust Co;Oak Park;IL; 50344560002-002; NS; PS; O; 09/30/86
Fortune Federal Savings & Loan Association;Clearwater;FL; 50229600001-001; S; M; F; 07/23/86
Gary-Wheaton Bank;Wheaton;IL; 50330770001-001; NS; M; F; 09/29/86
Gary-Wheaton Bank;Wheaton;IL; 50330770001-002; NS; PS; F; 09/29/86
Great West Life Assurance Co;Englewood;CO; 50331620001-001; NS; D; F; 07/16/86
Great West Life Assurance Co;Englewood;CO; 50331620001-002; NS; D; F; 07/16/86
Great West Life Assurance Co;Englewood;CO; 50331620001-003; NS; D; F; 07/16/86
Great West Life Assurance Co;Englewood;CO; 50331620001-004; NS; D; F; 07/16/86
Great West Life Assurance Co;Englewood;CO; 50331620001-005; NS; D; F; 07/16/86
Groos Bank NA;San Antonio;TX; 50231840002-001; S; PS; U; 07/16/86
Groos Bank NA;San Antonio;TX; 50231840002-002; S; M; U; 07/16/86
Guaranty Bank & Trust Co;Alexandria;LA; 50332030002-001; NS; D; F; 08/11/86
Guaranty Bank & Trust Co;Alexandria;LA; 50332030002-002; NS; D; F; 08/11/86
Guaranty Bank & Trust Co;Alexandria;LA; 50332030002-003; NS; D; F; 08/11/86
Guaranty Bank & Trust Co;Alexandria;LA; 50332030002-004; NS; D; F; 08/11/86
Guaranty Bank & Trust Co;Alexandria;LA; 50332030002-005; NS; D; F; 08/11/86
Guardian Life Insurance Co of America;New York;NY; 50232200001-002; P; D; F; 09/10/86
Guardian Life Insurance Co of America;New York;NY; 50232200001-004; P; D; F; 09/10/86
Guardian Life Insurance Co of America;New York;NY; 50232200001-006; P; D; F; 09/10/86
Guardian Life Insurance Co of America;New York;NY; 50232200002-003; P; M, F; 09/08/86
Guardian Life Insurance Co of America;New York;NY; 50232200002-004; P; M; F; 09/08/86
Guardian Life Insurance Co of America;New York;NY; 50232200002-007; P; PS; F; 09/08/86
Guardian Life Insurance Co of America;New York;NY; 50232200002-008; P; PS; F; 09/08/86
Guardian Life Insurance Co of America;New York;NY; 50332200001-001; NS; D; F; 09/10/86
Guardian Life Insurance Co of America;New York;NY; 50332200001-003; NS; D; F; 09/10/86
Guardian Life Insurance Co of America;New York;NY; 50332200001-005; NS; D; F; 09/10/86
Guardian Life Insurance Co of America;New York;NY; 50332200002-001; NS; M; F; 09/08/86
Guardian Life Insurance Co of America;New York;NY; 50332200002-002; NS; M; F; 09/08/86
Guardian Life Insurance Co of America;New York;NY; 50332200002-005; NS; PS; F; 09/08/86
Guardian Life Insurance Co of America;New York;NY; 50332200002-006; NS; PS; F; 09/08/86
Guardian Life Insurance Co of America;New York;NY; 50332200002-009; NS; T; F; 09/08/86
Guardian Life Insurance Co of America;New York;NY; 50332200002-010; NS; T; F; 09/08/86
Guardian State Bank & Trust Co;Alliance;NE; 50270620001-001; S; PS; F; 08/06/86
Harris Trust & Savings Bank;Chicago;IL; 50332600002-001; NS; PS; F; 09/25/86
Harris Trust & Savings Bank;Chicago;IL; 50332600005-001; NS; PS; F; 09/25/86
Herzog Heine Geduld Inc;New York;NY; 50233230001-001; P; PS; F; 09/12/86
Herzog Heine Geduld Inc;New York;NY; 50233230001-002; P; M; F; 09/12/86
Home Fed Trust;San Diego;CA; 50371770002-001; NS; D; F; 08/11/86
Home Fed Trust;San Diego;CA; 50371770002-002; NS; D; F; 08/11/86
Home Fed Trust;San Diego;CA; 50371770002-003; NS; D; F; 08/11/86
Home Fed Trust;San Diego;CA; 50371770002-004; NS; D; F; 08/11/86
Home Fed Trust;San Diego;CA; 50371770002-005; NS; D; F; 08/11/86
Home Life Financial Assurance Corp;Largo;FL; 50245280001-001; S; PS; F; 08/28/86
Home Life Insurance Co;New York;NY; 50233630002-001; P; M; F; 07/31/86
Home Life Insurance Co;New York;NY; 50233630002-002; P; M; F; 07/31/86
Home Life Insurance Co;New York;NY; 50233630002-003; P; PS; F; 07/31/86
Home Life Insurance Co;New York;NY; 50233630002-004; P; T; F; 07/31/86
Home Life Insurance Co;New York;NY; 50233630002-005; P; PS; F; 07/31/86
Home Life Insurance Co;New York;NY; 50333630002-006; NS; M; F; 07/31/86
Home Life Insurance Co;New York;NY; 50333630002-007; NS; M; F; 07/31/86

Home Life Insurance Co;New York;NY; 50333630002-008; NS; PS; F; 07/31/86
Home Life Insurance Co;New York;NY; 50333630002-009; NS; PS; F; 07/31/86
Home Life Insurance Co;New York;NY; 50333630002-010; NS; T; F; 07/31/86
Howard Savings Bank;Livingston;NJ; 50233940001-001; S; PS; F; 09/26/86
Huntington National Bank;Huntington Beach;CA; 50265630001-001; S; PS; U; 09/22/86
Imperial Trust Co;Los Angeles;CA; 50255800001-001; P; PS; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50255800001-002; P; M; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800001-003; NS; PS; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800001-004; NS; PS; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800001-005; NS; M; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800001-006; NS; M; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800002-001; NS; D; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800002-002; NS; D; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800002-003; NS; D; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800002-004; NS; D; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800002-005; NS; D; F; 08/18/86
Imperial Trust Co;Los Angeles;CA; 50355800002-006; NS; D; F; 08/18/86
Indiana Statewide Association of Rural Electric Cooperatives Inc;Indianapolis;IN; 50365660001-001; NS; D; U; 09/29/86
Indiana Statewide Association of Rural Electric Cooperatives Inc;Indianapolis;IN; 50365660001-002; NS; D; U; 09/29/86
Indiana Statewide Association of Rural Electric Cooperatives Inc;Indianapolis;IN; 50365660001-003; NS; D; U; 09/29/86
Indiana Statewide Association of Rural Electric Cooperatives Inc;Indianapolis;IN; 50365660001-004; NS; D; U; 09/29/86
Indiana Statewide Association of Rural Electric Cooperatives Inc;Indianapolis;IN; 50365660001-005; NS; D; U; 09/29/86
Ivy Fund;Hingham;MA; 50271900001-001; S; M; F; 09/22/86
Ivy Fund;Hingham;MA; 50271900001-002; S; PS; F; 09/22/86
Jackson National Life Insurance Co;Lansing;MI; 50235460001-001; S; M; F; 08/06/86
Jackson National Life Insurance Co of Texas;Lansing;MI; 50270010001-001; S; M; F; 08/06/86
Jefferson Guaranty Bank;Metairie;LA; 50235550001-001; S; PS; F; 09/08/86
Jefferson Guaranty Bank;Metairie;LA; 50235550001-002; S; PS; F; 09/08/86
Jefferson Guaranty Bank;Metairie;LA; 50235550003-001; S; D; U; 07/14/86
Jefferson Guaranty Bank;Metairie;LA; 50235550003-002; S; D; U; 07/14/86
Jefferson Guaranty Bank;Metairie;LA; 50335550001-003; NS; M; F; 09/08/86
Jefferson Guaranty Bank;Metairie;LA; 50335550001-004; NS; M; F; 09/08/86
Jefferson Guaranty Bank;Metairie;LA; 50335550002-001; NS; M; O; 09/04/86
Jefferson Guaranty Bank;Metairie;LA; 50335550002-002; NS; M; O; 09/04/86
Jefferson Guaranty Bank;Metairie;LA; 50335550003-003; NS; D; U; 07/14/86
Jefferson Guaranty Bank;Metairie;LA; 50335550003-004; NS; D; U; 07/14/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50235670001-002; S; T; U; 09/10/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50235670003-002; S; D; U; 09/17/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50235670003-004; S; D; U; 09/17/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50235670004-002; S; M; U; 09/01/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50235670005-002; S; PS; U; 09/10/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50335670001-001; NS; T; F; 09/10/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50335670002-001; NS; M; F; 09/10/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50335670003-001; NS; D; F; 09/30/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50335670003-003; NS; D; F; 09/30/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50335670004-001; NS; M; F; 09/01/86
John Hancock Mutual Life Insurance Co;Boston;MA; 50335670005-001; NS; PS; F; 09/10/86
Key Life Insurance Co;Indianapolis;IN; 50372100001-001; NS; M; F; 07/21/86
Key Life Insurance Co;Indianapolis;IN; 50372100002-001; NS; PS; F; 07/21/86
Landscape Nursery Council;Dayton;OH; 50370920001-001; NS; PS; F; 09/01/86
LaSalle National Bank;Chicago;IL; 50236840001-002; S; PS; F; 09/01/86
LaSalle National Bank;Chicago;IL; 50336840001-001; NS; PS; F; 09/01/86
LaSalle National Bank;Chicago;IL; 50336840002-001; NS; PS; F; 09/01/86
Laurens State Bank;Laurens;IA; 50272130001-001; S; PS; F; 09/26/86
Lebanon Valley National Bank;Lebanon;PA; 50271840001-001; P; PS; F; 08/04/86
Lebanon Valley National Bank;Lebanon;PA; 50271840001-002; P; M; F; 08/04/86
Manufacturers Life Insurance Co;Toronto Ontario Canada; ; 50238420001-002; S; M; F; 08/20/86
Manufacturers Life Insurance Co;Toronto Ontario Canada; ; 50238420001-004; S; PS; F; 08/20/86
Manufacturers Life Insurance Co;Toronto Ontario Canada; ; 50238420001-006; S; T; F; 08/20/86
Manufacturers Life Insurance Co;Toronto Ontario Canada; ; 50338420001-001; NS; M; F; 08/20/86
Manufacturers Life Insurance Co;Toronto Ontario Canada; ; 50338420001-003; NS; PS; F; 08/20/86
Manufacturers Life Insurance Co;Toronto Ontario Canada; ; 50338420001-005; NS; T; F; 08/20/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50218160002-001; P; PS; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50218160002-002; P; PS; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50218160002-003; P; PS; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50218160002-004; P; PS; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50218160002-007; P; M; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50218160002-008; P; M; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50218160002-009; P; M; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50218160002-010; P; M; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50318160001-001; NS; D; F; 08/20/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50318160001-002; NS; D; F; 08/20/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50318160002-005; NS; PS; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50318160002-006; NS; PS; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50318160002-011; NS; M; F; 07/28/86
Marquette Bank Minneapolis NA;Minneapolis;MN; 50318160002-012; NS; M; F; 07/28/86
Marshall & Ilsley Trust Co;Milwaukee;WI; 50233190001-001; P; M; F; 09/08/86
Marshall & Ilsley Trust Co;Milwaukee;WI; 50233190001-002; P; PS; F; 09/08/86
Marshall & Ilsley Trust Co;Milwaukee;WI; 50333190002-001; NS; D; F; 09/01/86
Marshall & Ilsley Trust Co;Milwaukee;WI; 50333190002-002; NS; D; F; 09/01/86
Mayflower Warehousemens Association;Indianapolis;IN; 50378074501-001; NS; M; F; 08/06/86
Mechanical Contractors Association of New Jersey Inc;East Orange;NJ; 50371820001-001; NS; PS; F; 07/16/86
Mechanical Contractors Association of New Jersey Inc;East Orange;NJ; 50371820002-001; NS; M; F; 07/16/86
Med Center Bank;Houston;TX; 50372160001-001; NS; PS; U; 09/24/86
Med Center Bank;Houston;TX; 50372160001-002; NS; PS; U; 09/24/86
Mellon Bank Delaware NA;Wilmington;DE; 50218910001-001; P; M; F; 09/29/86
Mellon Bank Delaware NA;Wilmington;DE; 50218910001-002; P; M; F; 09/29/86
Mercantile Safe Deposit & Trust Co;Baltimore;MD; 50239470001-001; P; PS; F; 09/29/86
Mercantile Safe Deposit & Trust Co;Baltimore;MD; 50239470001-002; P; PS; F; 09/29/86
Mercantile Safe Deposit & Trust Co;Baltimore;MD; 50239470001-005; P; M; F; 09/29/86
Mercantile Safe Deposit & Trust Co;Baltimore;MD; 50239470001-006; P; M; F; 09/29/86
Mercantile Safe Deposit & Trust Co;Baltimore;MD; 50339470001-003; NS; PS; F; 09/29/86
Mercantile Safe Deposit & Trust Co;Baltimore;MD; 50339470001-004; NS; PS; F; 09/29/86
Mercantile Safe Deposit & Trust Co;Baltimore;MD; 50339470001-007; NS; M; F; 09/29/86
Mercantile Safe Deposit & Trust Co;Baltimore;MD; 50339470001-008; NS; M; F; 09/29/86
Mercantile Trust Co NA;St Louis;MO; 50239490701-002; S; PS; F; 09/08/86
Mercantile Trust Co NA;St Louis;MO; 50239490701-004; S; [illegible]; F; 09/08/86
Mercantile Trust Co NA;St Louis;MO; 50339490001-005; NS; PS; O; 09/05/86
Mercantile Trust Co NA;St Louis;MO; 50339490001-006; NS; M; O; 09/10/86
Mercantile Trust Co NA;St Louis;MO; 50339490001-007; NS; PS; O; 09/05/86
Mercantile Trust Co NA;St Louis;MO; 50339490001-008; NS; M; O; 09/05/86
Mercantile Trust Co NA;St Louis;MO; 50339490701-001; NS; PS; F; 09/08/86
Mercantile Trust Co NA;St Louis;MO; 50339490701-003; NS; M; F; 09/08/86
Meridian Life Insurance Co;Indianapolis;IN; 50239800001-001; S; M; F; 09/15/86
Merrill Lynch Asset Management Inc;New York;NY; 50270300001-001; P; PS; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50270300001-002; P; M; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50270300001-003; P; T; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50270300001-004; P; PS; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50270300001-005; P; M; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50270300002-001; P; D; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50270300002-002; P; D; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50370300003-001; NS; T; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50370300003-002; NS; PS; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50370300003-003; NS; M; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50370300004-001; NS; D; F; 09/22/86
Merrill Lynch Asset Management Inc;New York;NY; 50370300004-002; NS; D; F; 09/22/86
Metropolitan Mortgage & Securities Co Inc;Spokane;WA; 50239990001-001; P; M; U; 09/01/86
Metropolitan Mortgage & Securities Co Inc;Spokane;WA; 50239990001-002; P; PS; U; 09/01/86
Mid-America Life Assurance Co;Bloomington;IL; 50240210001-001; S; M; U; 07/18/86
Mid-Western Life Insurance Co;Enid;OK; 50240300001-001; S; PS; F; 07/18/86
Minnesota Mutual Life Insurance Co;St Paul;MN; 50240800001-001; P; PS; F; 08/25/86
Minnesota Mutual Life Insurance Co;St Paul;MN; 50240800001-003; P; M; F; 08/25/86
Minnesota Mutual Life Insurance Co;St Paul;MN; 50240800001-005; P; T; F; 08/25/86
Minnesota Mutual Life Insurance Co;St Paul;MN; 50240800002-001; P; D; F; 08/25/86
Minnesota Mutual Life Insurance Co;St Paul;MN; 50340800001-002; NS; PS; F; 08/25/86
Minnesota Mutual Life Insurance Co;St Paul;MN; 50340800001-004; NS; M; F; 08/25/86
Minnesota Mutual Life Insurance Co;St Paul;MN; 50340800001-006; NS; T; F; 08/25/86
Minnesota Mutual Life Insurance Co;St Paul;MN; 50340800002-002; NS; D; F; 08/25/86

Minnesota Mutual Life Insurance Co;St Paul;MN; 50340800002-003; NS; D; U; 08/25/86
Moore & Schley Cameron & Co;New York;NY; 50341120001-001; NS; M; F; 09/15/86
Moore & Schley Cameron & Co;New York;NY; 50341120001-002; NS; PS; F; 09/15/86
Mountain States Bank;Denver;CO; 50241280001-001; P; PS; F; 09/12/86
Mountain States Bank;Denver;CO; 50241280001-002; P; M; F; 09/12/86
Mountain States Bank;Denver;CO; 50341280001-003; NS; PS; F; 09/12/86
Mountain States Bank;Denver;CO; 50341280001-004; NS; M; F; 09/12/86
National Association of Mutual Insurance Companies;Indianapolis;IA; 50241651802-001; P; M; F; 08/15/86
National Association of Mutual Insurance Companies;Indianapolis;IA; 50241651802-002; P; PS; F; 08/15/86
National Association of Mutual Insurance Companies;Indianapolis;IA; 50241651802-003; P; T; F; 08/15/86
National Bank of Detroit;Detroit;MI; 50241980004-001; S; M; U; 08/18/86
National Bank of Detroit;Detroit;MI; 50241980004-002; S; PS; U; 08/18/86
National City Bank;Akron;OH; 50266860002-001; P; PS; F; 07/24/86
National City Bank;Akron;OH; 50266860002-002; P; PS; F; 07/24/86
National City Bank;Akron;OH; 50266860002-003; P; M; F; 07/24/86
National City Bank;Akron;OH; 50266860002-004; P; M; F; 07/24/86
National City Bank;Akron;OH; 50366860001-001; NS; PS; F; 07/24/86
National City Bank;Akron;OH; 50366860001-002; NS; PS; F; 07/24/86
National City Bank;Akron;OH; 50366860001-003; NS; M; F; 07/24/86
National City Bank;Akron;OH; 50366860001-004; NS; M; F; 07/24/86
National City Bank;Cleveland;OH; 50242310002-001; P; PS; F; 07/18/86
National City Bank;Cleveland;OH; 50242310002-002; P; PS; F; 07/18/86
National City Bank;Cleveland;OH; 50242310002-003; P; M; F; 07/18/86
National City Bank;Cleveland;OH; 50242310002-004; P; M; F; 07/18/86
National City Bank;Cleveland;OH; 50342310001-001; NS; PS; F; 07/18/86
National City Bank;Cleveland;OH; 50342310001-002; NS; PS; F; 07/18/86
National City Bank;Cleveland;OH; 50342310001-003; NS; M; F; 07/18/86
National City Bank;Cleveland;OH; 50342310001-004; NS; M; F; 07/18/86
National Farmers Union Life Insurance Co;Denver;CO; 50272260001-001; P; M; F; 09/29/86
National Farmers Union Life Insurance Co;Denver;CO; 50272260001-002; P; PS; F; 09/29/86
National Guardian Life Insurance Co;Madison;WI; 50242470001-003; S; PS; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50242470001-004; S; PS; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50242470002-003; S; PS; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50242470002-004; S; PS; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50242470003-003; S; M; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50242470003-004; S; M; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50242470004-003; S; M; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50242470004-004; S; M; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50342470001-001; NS; PS; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50342470001-002; NS; PS; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50342470002-001; NS; PS; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50342470002-002; NS; PS; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50342470003-001; NS; M; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50342470003-002; NS; M; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50342470004-001; NS; M; F; 09/22/86
National Guardian Life Insurance Co;Madison;WI; 50342470004-002; NS; M; F; 09/22/86
National Old Line Insurance Co;Little Rock;AR; 50242570001-001; S; D; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50242570001-003; S; D; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50242570001-005; S; D; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50242570001-007; S; D; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50242570002-001; S; M; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50242570002-003; S; PS; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50342570001-002; NS; D; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50342570001-004; NS; D; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50342570001-006; NS; D; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50342570001-008; NS; D; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50342570002-002; NS; M; F; 07/28/86
National Old Line Insurance Co;Little Rock;AR; 50342570002-004; NS; PS; F; 07/28/86
National Telephone Cooperative Association;Washington;DC; 50342740001-001; NS; D; F; 08/14/86
Neuberger & Berman Management Inc;New York;NY; 50271780001-003; S; PS; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50271780001-004; S; PS; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50271780002-003; S; PS; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50271780002-004; S; PS; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50271780003-003; S; M; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50271780003-004; S; M; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50271780004-003; S; M; F; 09/25/86
Neuberger & Berman Management Inc;New York;NY; 50271780004-004; S; M; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50371780001-001; NS; PS; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50371780001-002; NS; PS; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50371780002-001; NS; PS; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50371780002-002; NS; PS; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50371780003-001; NS; M; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50371780003-002; NS; M; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50371780004-001; NS; M; F; 09/22/86
Neuberger & Berman Management Inc;New York;NY; 50371780004-002; NS; M; F; 09/22/86
New England Mutual Life Insurance Co;Burlington;MA; 50243000001-006; P; D; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50243000001-007; P; D; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50243000001-008; P; D; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50243000002-006; P; M; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50243000002-007; P; PS; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000001-001; NS; D; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000001-002; NS; D; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000001-003; NS; D; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000001-004; NS; D; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000001-005; NS; D; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000002-001; NS; M; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000002-002; NS; M; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000002-003; NS; T; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000002-004; NS; PS; F; 07/02/86
New England Mutual Life Insurance Co;Burlington;MA; 50343000002-005; NS; PS; F; 07/02/86
Noddings-Calamos Asset Management Inc;Oak Brook;IL; 50370700001-001; NS; PS; U; 09/01/86
North Atlantic Life Insurance Co of America;Jericho;NY; 50343460001-001; NS; D; F; 07/23/86
North Atlantic Life Insurance Co of America;Jericho;NY; 50343460001-002; NS; D; F; 07/23/86
North Atlantic Life Insurance Co of America;Jericho;NY; 50343460001-003; NS; D; F; 07/23/86
North Atlantic Life Insurance Co of America;Jericho;NY; 50343460001-004; NS; D; F; 07/23/86
North Atlantic Life Insurance Co of America;Jericho;NY; 50343460001-005; NS; D; F; 07/23/86
North Atlantic Life Insurance Co of America;Jericho;NY; 50343460002-001; NS; M; F; 07/23/86
North Atlantic Life Insurance Co of America;Jericho;NY; 50343460002-002; NS; M; F; 07/23/86
North Atlantic Life Insurance Co of America;Jericho;NY; 50343460003-001; NS; PS; F; 07/23/86
North Atlantic Life Insurance Co of America;Jericho;NY; 50343460003-002; NS; PS; F; 07/23/86
Northern Kentucky Bank & Trust;Alexandria;KY; 50243880001-001; S; D; U; 07/18/86
Ohio Citizens Bank;Toledo;OH; 50244670002-001; P; PS; F; 07/24/86
Ohio Citizens Bank;Toledo;OH; 50244670002-002; P; PS; F; 07/24/86
Ohio Citizens Bank;Toledo;OH; 50244670002-003; P; M; F; 07/24/86
Ohio Citizens Bank;Toledo;OH; 50244670002-004; P; M; F; 07/24/86
Ohio Citizens Bank;Toledo;OH; 50344670001-001; NS; PS; F; 07/24/86
Ohio Citizens Bank;Toledo;OH; 50344670001-002; NS; PS; F; 07/24/86
Ohio Citizens Bank;Toledo;OH; 50344670001-003; NS; M; F; 07/24/86
Ohio Citizens Bank;Toledo;OH; 50344670001-004; NS; M; F; 07/24/86
Ohio Valley National Bank;Henderson;KY; 50244771802-001; S; M; F; 07/23/86
Ohio Valley National Bank;Henderson;KY; 50244771802-002; S; PS; F; 07/23/86
Old National Bank in Evansville;Evansville;IN; 50244961802-001; S; M; F; 07/28/86
Old National Bank in Evansville;Evansville;IN; 50244961802-003; S; PS; F; 07/28/86
Old National Bank in Evansville;Evansville;IN; 50344961802-002; NS; M; F; 07/28/86
Old National Bank in Evansville;Evansville;IN; 50344961802-004; NS; PS; F; 07/28/86
Packers National Bank in Omaha;Omaha;NE; 50345640001-002; NS; M; F; 07/02/86
Penn Square Mutual Fund;Reading;PA; 50267450001-001; P; PS; F; 09/15/86
Penn Square Mutual Fund;Reading;PA; 50267450001-002; P; M; F; 09/15/86
Pennsylvania National Life Ins Co;Harrisburg;PA; 50246270001-005; S; T; F; 08/13/86
Pennsylvania National Life Ins Co;Harrisburg;PA; 50246270001-006; S; T; F; 08/13/86
Pennsylvania National Life Ins Co;Harrisburg;PA; 50246270001-007; S; M; F; 08/13/86
Pennsylvania National Life Ins Co;Harrisburg;PA; 50246270001-008; S; PS; F; 08/13/86
Pennsylvania National Life Ins Co;Harrisburg;PA; 50346270001-001; NS; T; F; 08/13/86
Pennsylvania National Life Ins Co;Harrisburg;PA; 50346270001-002; NS; M; F; 08/13/86
Pennsylvania National Life Ins Co;Harrisburg;PA; 50346270001-003; NS; M; F; 08/13/86
Pennsylvania National Life Ins Co;Harrisburg;PA; 50346270001-004; NS; PS; F; 08/13/86
Peoples Bank & Trust Co;Grand Haven;MI; 50246470001-003; P; PS; F; 09/12/86
Peoples Bank & Trust Co;Grand Haven;MI; 50246470001-004; P; M; F; 09/12/86
Peoples Bank & Trust Co;Grand Haven;MI; 50346470001-001; NS; PS; F; 09/12/86
Peoples Bank & Trust Co;Grand Haven;MI; 50346470001-002; NS; M; F; 09/12/86

Peoples State Bank;Missouri Valley;IA; 50270560001-001; P; PS; F; 08/08/86
Peoples State Bank;Missouri Valley;IA; 50270560001-002; P; M; F; 08/08/86
Pikeville National Bank & Trust Co;Pikeville;KY; 50247480001-002; P; M; F; 09/29/86
Pikeville National Bank & Trust Co;Pikeville;KY; 50247480001-004; P; PS; F; 09/29/86
Pikeville National Bank & Trust Co;Pikeville;KY; 50347480001-001; NS; M; F; 09/29/86
Pikeville National Bank & Trust Co;Pikeville;KY; 50347480001-003; NS; PS; F; 09/29/86
Planters Bank & Trust Co of Virginia;Staunton;VA; 50347850001-001; NS; PS; F; 07/25/86
Planters Bank & Trust Co of Virginia;Staunton;VA; 50347850001-002; NS; PS; F; 07/25/86
Planters Bank & Trust Co of Virginia;Staunton;VA; 50347850002-001; NS; M; F; 07/25/86
Planters Bank & Trust Co of Virginia;Staunton;VA; 50347850002-002; NS; M; F; 07/25/86
Professional & Businessmens Association Inc;Austin;TX; 50348340001-001; NS; PS; F; 09/10/86
Professional & Businessmens Association Inc;Austin;TX; 50348340001-002; NS; PS; F; 09/10/86
Professional & Businessmens Association Inc;Austin;TX; 50348340002-001; NS; M; F; 09/10/86
Professional & Businessmens Association Inc;Austin;TX; 50348340002-002; NS; M; F; 09/10/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480001-001; NS; M; F; 08/11/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480001-002; NS; M; F; 08/11/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480001-003; NS; PS; F; 08/11/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480001-004; NS; PS; F; 08/11/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480001-005; NS; T; F; 08/11/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480002-001; NS; D; F; 08/11/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480002-002; NS; D; F; 08/11/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480002-003; NS; D; F; 08/11/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480002-004; NS; D; F; 08/11/86
Provident Indemnity Life Insurance Co;Norristown;PA; 50348480002-005; NS; D; F; 08/11/86
Prudential Bache Securities Inc;New York;NY; 50258150002-001; P; PS; F; 07/28/86
Prudential Bache Securities Inc;New York;NY; 50258150002-002; P; M; F; 07/28/86
Puritan Life Insurance Co;Providence;RI; 50248670001-001; S; PS; F; 09/24/86
Raymond James & Associates Inc;St Petersburg;FL; 50248930001-001; P; PS; F; 08/29/86
Raymond James & Associates Inc;St Petersburg;FL; 50248930001-002; P; M; F; 08/29/86
Santa Barbara Bank & Trust;Santa Barbara;CA; 50350190001-001; NS; M; F; 07/30/86
Santa Barbara Bank & Trust;Santa Barbara;CA; 50350190001-002; NS; PS; F; 07/30/86
Sanwa Bank California;Los Angeles;CA; 50237680001-001; P; PS; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50237680001-002; P; M; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50237680001-003; P; PS; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50237680001-004; P; PS; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50237680001-005; P; M; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50237680001-006; P; M; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50237680001-011; P; PS; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50237680001-012; P; M; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50237680001-013; P; PS; F; 09/01/86
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Sanwa Bank California;Los Angeles;CA; 50237680001-016; P; M; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50237680002-001; S; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50237680002-007; S; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680001-007; NS; PS; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50337680001-008; NS; PS; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50337680001-009; NS; M; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50337680001-010; NS; M; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50337680001-017; NS; PS; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50337680001-018; NS; PS; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50337680001-019; NS; M; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50337680001-020; NS; M; F; 09/01/86
Sanwa Bank California;Los Angeles;CA; 50337680002-002; NS; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680002-003; NS; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680002-004; NS; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680002-005; NS; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680002-006; NS; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680002-008; NS; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680002-009; NS; D; F; 08/13/86
Sanwa Bank California;Los Angeles;CA; 50337680002-010; NS; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680002-011; NS; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680002-012; NS; D; F; 08/11/86
Sanwa Bank California;Los Angeles;CA; 50337680003-001; NS; PS; F; 08/28/86
Sanwa Bank California;Los Angeles;CA; 50337580004-001; NS; M; F; 08/28/86
Sanwa Bank California;Los Angeles;CA; 50337680005-001, NS; PS; F; 08/28/86
Sanwa Bank California;Los Angeles;CA; 50337680006-001; NS; M; F; 08/28/86
Savings Bank of Mendocino County;Ukiah;CA; 50271630001-001; P; M; F; 07/16/86
Savings Bank of Mendocino County;Ukiah;CA; 50271630001-002; P; PS; F; 07/16/86
Savings Bank of Mendocino County;Ukiah;CA; 50271630001-003; P; M; F; 07/16/86
Savings Bank of Mendocino County;Ukiah;CA; 50271630001-004; P; PS; F; 07/16/86
Second National Bank of Richmond;Richmond;IN; 50250621901-001; P; PS; F; 09/12/86
Second National Bank of Richmond;Richmond;IN; 50250621901-002; P; M; F; 09/12/86
Security National Bank & Trust Co;Wheeling;WV; 50250940001-001; S; PS; F; 08/25/86
Security National Bank & Trust Co;Wheeling;WV; 50250940001-003; S; M; F; 08/25/86
Security National Bank & Trust Co;Wheeling;WV; 50350940001-002; NS; PS; F; 08/25/86
Security National Bank & Trust Co;Wheeling;WV; 50350940001-004; NS; M; F; 08/25/86
SIFE Trust Fund;Walnut Creek;CA; 50270280001-001; S; PS; F; 08/06/86
Society Bank NA;Dayton;OH; 50355210001-001; NS; PS; F; 09/19/86
Society Bank NA;Dayton;OH; 50355210002-001; NS; M; F; 09/19/86
Society Bank NA;Dayton;OH; 50355210003-001; NS; PS; F; 09/19/86
Society Bank NA;Dayton;OH; 50355210004-001; NS; M; F; 09/19/86
Society National Bank;Cleveland;OH; 50251860001-001; P; PS; F; 09/22/86
Society National Bank;Cleveland;OH; 50251860001-002; P; M; F; 09/22/86
Society National Bank;Cleveland;OH; 50351860002-001; NS; PS; F; 09/22/86
Society National Bank;Cleveland;OH; 50351860003-001; NS; M; F; 09/22/86
Society National Bank;Cleveland;OH; 50351860004-001; NS; PS; F; 09/22/86
Society National Bank;Cleveland;OH; 50351860005-001; NS; M; F; 09/22/86
Southern Medical Association;Birmingham;AL; 50252310001-001; S; D; F; 08/15/86
Southern Medical Association;Birmingham;AL; 50252310001-002; S; D; F; 08/15/86
Southern Medical Association;Birmingham;AL; 50252310001-003; S; D; F; 08/15/86
Southern Medical Association;Birmingham;AL; 50252310001-004; S; D; F; 08/15/86
Southern Medical Association;Birmingham;AL; 50252310002-001; S; PS; F; 07/25/86
Southern Medical Association;Birmingham;AL; 50252310002-002; S; M; F; 07/25/86
Southern Medical Association;Birmingham;AL; 50252310002-003; S; PS; F; 07/25/86
Southern Medical Association;Birmingham;AL; 50252310002-004; S; M; F; 07/25/86
Southern Ohio Bank;Cincinnati;OH; 50252360001-001; S; M; U; 08/25/86
Southern Ohio Bank;Cincinnati;OH; 50252360001-003; S; M; U; 08/25/86
Southern Ohio Bank;Cincinnati;OH; 50252360002-001; S; PS; U; 08/25/86
Southern Ohio Bank;Cincinnati;OH; 50252360002-003; S; PS; U; 08/25/86
Southern Ohio Bank;Cincinnati;OH; 50352360001-002; NS; M; U; 08/25/86
Southern Ohio Bank;Cincinnati;OH; 50352360002-002; NS; PS; U; 08/25/86
Sovran Bank NA;Richmond;VA; 50358510002-001; NS; M; F; 07/02/86
Sovran Bank NA;Richmond;VA; 50358510002-002; NS; PS; F; 07/02/86
Spencer County Bank;Santa Claus;IA; 50252661801-001; P; M; F; 07/18/86
Spencer County Bank;Santa Claus;IA; 50252661801-002; P; PS; F; 07/18/86
St Cloud National Bank & Trust Co;St Cloud;MN; 50252740001-001; S; PS; U; 07/14/86
St Cloud National Bank & Trust Co;St Cloud;MN; 50252740001-002; S; PS; U; 07/14/86
St Cloud National Bank & Trust Co;St Cloud;MN; 50252740002-001; S; M; U; 07/14/86
Standard Mutual Life Insurance Co;Lawrence;KS; 50252930001-001; S; D; F; 07/16/86
Standard Mutual Life Insurance Co;Lawrence;KS; 50252930001-002; S; D; F; 07/16/86
Standard Mutual Life Insurance Co;Lawrence;KS; 50352930001-003; NS; D; F; 07/16/86
Standard Mutual Life Insurance Co;Lawrence;KS; 50352930001-004; NS; D; F; 07/16/86
State Bank of De Pere;De Pere;WI; 50253141802-001; P; M; F; 07/23/86
State Bank of De Pere;De Pere;WI; 50253141802-002; P; PS; F; 07/23/86
State Farm Life Insurance Co;Bloomington;IL; 50253640001-001; P; M; F; 09/01/86
State Farm Life Insurance Co;Bloomington;IL; 50253640001-002; P; PS; F; 09/01/86
State Farm Life Insurance Co;Bloomington;IL; 50253640001-003; P; T; F; 09/01/86
State Farm Life Insurance Co;Bloomington;IL; 50253640003-001; S; M; F; 09/01/86
State Farm Life Insurance Co;Bloomington;IL; 50353640001-004; NS; M; F; 09/01/86
State Farm Life Insurance Co;Bloomington;IL; 50353640001-005; NS; PS; F; 09/01/86
State Farm Life Insurance Co;Bloomington;IL; 50353640001-006; NS; T; F; 09/01/86
State Mutual Life Assurance Co of America;Worcester;MA; 50253700001-003; S; PS; F; 07/11/86
State Mutual Life Assurance Co of America;Worcester;MA, 50253700002-003; S; M; F; 07/11/86
State Mutual Life Assurance Co of America;Worcester;MA; 50253700003-006; P; D; F; 07/11/86
State Mutual Life Assurance Co of America;Worcester;MA; 50253700003-007; P; D; F; 07/11/86
State Mutual Life Assurance Co of America;Worcester;MA; 50253700003-008; P; D; F; 07/11/86
State Mutual Life Assurance Co of America;Worcester;MA; 50253700003-009; P; D; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50253700003-010; P; D; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50253700004-003; P; PS; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50253700004-006; P; M; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50253700004-010; P; T; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50253700004-011; P; T; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50253700004-012; P; T; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700001-001; NS; PS; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700001-002; NS; PS; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700002-001; NS; M; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700002-002; NS; M; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700003-001; NS; D; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700003-002; NS; D; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700003-003; NS; D; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700003-004; NS; D; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700003-005; NS; D; F; 07/11/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700004-001; NS; PS; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700004-002; NS; PS; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700004-004; NS; M; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700004-005; NS; M; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700004-007; NS; T; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700004-008; NS; T; F; 07/14/86

State Mutual Life Assurance Co of America;Worcester;MA; 50353700004-009; NS; T; F; 07/14/86

State National Bank;Evanston;IL; 50353730001-001; NS; PS; F; 09/26/86

State National Bank;Evanston;IL; 50353730001-002; NS; PS; F; 09/26/86

State National Bank;Evanston;IL; 50353730002-001; NS; M; F; 09/26/86

State National Bank;Evanston;IL; 50353730002-002; NS; M; F; 09/26/86

Stone Fort National Bank;Nacogdoches;TX; 50268452601-006; S; PS; U; 09/11/86

T J Raney & Sons Inc;Little Rock;AR; 50254558301-001; P; PS; F; 09/15/86

T J Raney & Sons Inc;Little Rock;AR; 50254558301-002; P; M; F; 09/15/86

Texas American Bank Fort Worth NA;Fort Worth;TX; 50354760001-001; NS; PS; U; 07/28/86

Texas American Bank Fort Worth NA;Fort Worth;TX; 50354760001-002; NS; PS; U; 07/28/86

Texas American Bank Fort Worth NA;Fort Worth;TX; 50354760001-003; NS; M; U; 07/28/86

Texas American Bank Fort Worth NA;Fort Worth;TX; 50354760001-004; NS; M; U; 07/28/86

Texas Commerce Bank Arlington;Arlington;TX; 50254822601-006; S; PS; U; 09/11/86

Texas Commerce Bank Austin NA;Austin;TX; 50254832601-006; S; PS; U; 09/11/86

Texas Commerce Bank Beaumont NA;Beaumont;TX; 50254842601-006; S; PS; U; 09/11/86

Texas Commerce Bank Brownsville;Brownsville;TX; 50268652601-006; S; PS; U; 09/11/86

Texas Commerce Bank Corpus Christi NA;Corpus Christi;TX; 50254862601-006; S; PS; U; 09/11/86

Texas Commerce Bank Dallas NA;Dallas;TX; 50254972601-006; S; PS; U; 09/11/86

Texas Commerce Bank El Paso NA;El Paso;TX; 50217532601-006; S; PS; U; 09/11/86

Texas Commerce Bank Las Colinas;Irving;TX; 50254882601-006; S; PS; U; 09/11/86

Texas Commerce Bank Longview;Longview;TX; 50254902601-006; S; PS; U; 09/11/86

Texas Commerce Bank McAllen NA;McAllen;TX; 50223912601-006; S; PS; U; 09/11/86

Texas Commerce Bank NA;Houston;TX; 50254912601-006; S; PS; U; 09/11/86

Texas Commerce Bank NA;Lubbock;TX; 50254812601-006; S; PS; U; 09/11/86

Texas Commerce Bank New Braunfels NA;New Braunfels;TX; 50254922601-006; S; PS; U; 09/11/86

Texas Commerce Bank Odessa;Odessa;TX; 50254932601-006; S; PS; U; 09/11/86

Texas Commerce Bank of Fort Worth;Fort Worth;TX; 50254[illegible]2601-006; S; PS; U; 09/11/86

Texas Commerce Bank San Angelo NA;San Angelo;TX; 50254962601-006; S; PS; U; 09/11/86

Titonka Savings Bank;Titonka;IA; 50255340001-001; S; PS; F; 09/26/86

TransWorld Bank;Sherman Oaks;CA; 50255550001-001; P; M; F; 07/21/86

TransWorld Bank;Sherman Oaks;CA; 50255550001-002; P; PS; F; 07/21/86

Unified Management Corp;Indianapolis;IN; 50255980002-001; P; PS; F; 09/01/86

Unified Management Corp;Indianapolis;IN; 50255980002-002; P; M; F; 09/01/86

Union Bank & Trust Co NA;Grand Rapids;MI; 50256130001-003; P; PS; F; 09/22/86

Union Bank & Trust Co NA;Grand Rapids;MI; 50256130001-004; P; M; F; 09/22/86

Union Bank & Trust Co NA;Grand Rapids;MI; 50356130001-001; NS; PS; F; 09/22/86

Union Bank & Trust Co NA;Grand Rapids;MI; 50356130001-002; NS; M; F; 09/22/86

Union Central Life Insurance Co;Cincinnati;OH; 50356200002-001; NS; D; F; 09/12/86

Union Central Life Insurance Co;Cincinnati;OH; 50356200002-002; NS; D; F; 09/12/86

United States National Bank;Galveston;TX; 50257610001-001; P; PS; F; 07/02/86

United States National Bank;Galveston;TX; 50257610001-002; P; M; F; 07/02/86

United States National Bank;Galveston;TX; 50357610002-001; NS; PS; F; 07/02/86

United States National Bank;Galveston;TX; 50357610002-002; NS; M; F; 07/02/86

US Boston Investment Management Corp;Burlington;MA; 50280050002-001; S; D; F; 08/14/86

US Boston Investment Management Corp;Burlington;MA; 50280050002-002; S; D; F; 08/14/86

Valencia Bank;Irvine;CA; 50358030002-001; NS; D; F; 08/11/86

Valencia Bank;Irvine;CA; 50358030002-002; NS; D; F; 08/11/86

Valencia Bank;Irvine;CA; 50358030002-003; NS; D; F; 08/11/86

Valencia Bank;Irvine;CA; 50358030002-004; NS; D; F; 08/11/86

Valencia Bank;Irvine;CA; 50358030002-005; NS; D; F; 08/11/86

Valley Bank of Nevada;Las Vegas;NV; 50258130001-001; S; PS; F; 08/20/86

Valley Bank of Nevada;Las Vegas;NV; 50258130002-001; S; M; F; 08/20/86

Van Horn State Bank;Van Horn;TX; 50358320001-001; NS; PS; F; 07/16/86

Wells Fargo Bank;Los Angeles;CA; 50316290002-001; NS; PS; F; 09/24/86

Wells Fargo Bank;Los Angeles;CA; 50316290002-002; NS; M; F; 09/24/86

Western National Life Insurance Co;Amarillo;TX; 50259430001-001; S; M; F; 08/25/86

Western National Life Insurance Co;Amarillo;TX; 50259430001-002; S; PS; F; 08/25/86

Western National Life Insurance Co;Amarillo;TX; 50359430001-003; NS; M; F; 08/25/86

Western National Life Insurance Co;Amarillo;TX; 50359430001-004; NS; PS; F; 08/25/86

Zapp National Bank of St Cloud;St Cloud;MN; 50360400001-001; NS; M; F; 07/18/86

Zapp National Bank of St Cloud;St Cloud;MN; 50360400001-002; NS; PS; F; 07/18/86

LIST B

Plans Omitted from Announcement 85–99

Bank of Delaware; Wilmington, DE; 50305470002–001; NS; PS.

Bank of Delaware; Wilmington, DE; 50305470003–001; NS; PS.

United States Fidelity Guaranty Co; Baltimore, MD; 50349420001–002; NS; D.

United States Fidelity Guaranty Co; Baltimore, MD; 50349420001–003; NS; D.

Annoucement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practible for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
S. Melvin Apotheker	Miami, FL	Attorney	Indefinite from September 1, 1986
Sandra S. Behn	London, TN	Certified Public Accountant	Indefinite from September 12, 1986
Charles K. Hyter	Hutchinson, KS	Attorney	Indefinite from September 18, 1986
William Pyke	Dallas, TX	Certified Public Accountant	Eighteen Months from August 15, 1986
Alan Z. Richards	West Hempstead, NY	Attorney and Certified Public Accountant	Indefinite from September 20, 1986

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to identify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
Paul Beecher	Torrance, CA	Indefinite effective September 25, 1986
Michael Winston	Fort Lauderdale, FL	Six Months from October 20, 1986

Under 31 Code of Federal Regulations, Part 10, an enrolled agent, in order to avoid the institution of a proceeding for his disbarment of suspension from practice before the Internal Revenue Service, may offer his resignation. The Director of Practice, in his discretion, may accept the offered resignation of an enrolled agent.

To enable the public and other practitioners to identify such resigned enrolled agents, the Director of Practice will announce in the Internal Revenue Bulletin the name and address of each enrolled agent who has resigned and the effective date of resignation. This announcement will appear in the weekly Bulletin at the earliest practicable date after the action and will continue to appear in the weekly Bulletins for five successive weeks or for as many weeks as is practicable for each resigned enrolled agent, and will later be consolidated and published in the Cumulative Bulletin.

The following individual has entered a consent resignation from enrollment to practice before the Internal Revenue Service:

Name of Enrolled Agent	Address	Effective Date of Resignation
William E. Bonafede	Wakefield, RI	September 30, 1986

Under Section 330, Title 31 of the United States Code, the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
James L. Ketner	Charlotte, NC	Certified Public Accountant	September 27, 1986
George L. Weil	Orange, CT	Certified Public Accountant	September 27, 1986

Announcement Relating to Proposed Regulations Published With Notice of Proposed Rulemaking

Changes in regulations as announced below have been published in the Federal Register in tentative or proposed form to provide interested parties with an opportunity to file their objections or suggestions for consideration prior to final adoption of such regulations. These announcements will appear in the Bulletin during the period which has been prescribed for the submission and consideration of any views, arguments, or suggestions pertaining to the proposed regulations so published. Statement of such views, arguments or suggestions should be submitted in writing, preferably six copies, to the Commissioner of Internal Revenue, Attention: CC:LR:T, Washington, D.C. 20224.

Section affected	Subject	Published in the Bulletin	Expiration date for submission of views
26 CFR 51.4989–1, 51.4996–1, 51.4996–3 amended; 51.4996–4 added	Definition of "property" for purposes of the windfall profit tax	1986–42 I.R.B. 15	Nov. 11, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR— Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
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TFE—Transferee.
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T.I.R.—Technical Information Release.
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TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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1986-46

Internal Revenue bulletin

Bulletin No. 1986–46
November 17, 1986

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–131, page 4.
Controlled foreign corporations; exclusion of previously taxed earnings and profits. The proper method to be followed in adjusting the earnings and profits of a controlled foreign corporation to reflect a distribution of property to its domestic shareholder in a situation in which the property has an adjusted basis greater than its fair market value on the date of the distribution is set forth.

Rev. Rul. 86–132, page 5.
Taxation of DISC income to shareholders. This revenue ruling sets forth the "base period T-bill rate" for the periods ending September 30, 1984, September 30, 1985, and September 30, 1986, as required by section 995(f)(4) of the Code.

Rev. Rul. 86–133, page 13.
Net operating loss carryforwards; section 382 and section 383 limitation; interest rate. Adjustments are made to the applicable federal rates for purposes of the limits, under section 382 and section 383 of the Code, on the amount of a corporation's taxable income and income tax liability that can be offset by certain of its net operating loss carryforwards and by other tax attributes following an "ownership change" as defined in section 382(g).

Rev. Rul. 86–135, page 13.
Original issue discount; tax-exempt obligations; interest rate. Adjustments are made to the applicable federal rates under section 1274 of the Code for the determination of the original issue discount on tax-exempt obligations for purposes of section 1288(b)(1).

EXEMPT ORGANIZATIONS

Rev. Proc. 86–43, page 15.
Educational organization; the methodology test. Criteria are set forth to determine whether an organization's viewpoint or position is considered educational under section 501(c)(3) of the Code and section 1.501(c)(3)–1(d)(3) of the regulations.

Announcement 86–111, page 20.
A list is given of organizations now classified as private foundations.

EMPLOYMENT TAX

Page 13.
Railroad Retirement; rate determination; quarterly. The Railroad Retirement Board has determined that the rate of tax imposed by section 3221(c) of the Code shall be 24 cents for the quarter beginning January 1, 1987.

EMPLOYEE PLANS

Notice 86–13, page 17.
Determination and opinion letters issued by the Service will not be reviewed for the qualification requirements of the Tax Reform Act of 1986 until further notice is given.

ADMINISTRATIVE

Treasury Department Order 150–02, page 15.
Establishment of certain offices. Certain offices in the National Office of the Internal Revenue Service are established.

Announcement 86–110, page 18.
The Service invites public comments on projects needed to implement the Tax Reform Act of 1986.

Announcement 86–112, page 22.
Guidance is provided with respect to the information reporting of mortgage interest in situations involving points and other prepaid interest, interest received by cooperative housing corporations, interest received on behalf of another, interest received from nonresident aliens, and Rule of 78s accounting.

Announcement 86–115, page 24.
Form 1099B, Statement for Recipients of Proceeds From Real Estate, Broker, and Barter Exchange Transactions, has been revised.

Announcement 86–116, page 25.
A printing error in Rev. Proc. 86–41, relating to information and representations to be included in a request for a ruling under section 355 of the Code, is corrected.

Finding Lists begin on page 29.
Announcement of Disbarments and Suspensions begin on page 26.
Disposition of Declaratory Judgement Proceedings Under Section 7428 on page 23.

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Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

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The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 312.—Effect on Earnings and Profits

26 CFR 1.312–1: Adjustment to earnings and profits reflecting distributions by corporations.

The earnings and profits of a controlled foreign corporation must be adjusted to reflect the distribution of property to its domestic shareholder in a situation in which the property has an adjusted basis greater than its fair market value on the date of the distribution. See Rev. Rul. 86–131, below.

Section 501.—Exemption From Tax on Corporations, Certain Trusts, Etc.

26 CFR 1.501(c)(3)–1: Organizations organized and operated for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals.

Whether advocacy of a particular viewpoint or position by an organization is considered educational. See Rev. Proc. 86–43, page 14.

Section 959.—Exclusion From Gross Income of Previously Taxed Earnings and Profits

26 CFR 1.959–2: Exclusion from gross income of controlled foreign corporations of previously taxed earnings and profits.
(Also Section 312(a); 1.312–1.)

Controlled foreign corporations; exclusion of previously taxed earnings and profits. The proper method to be followed in adjusting the earnings and profits of a controlled foreign corporation to reflect a distribution of property to its domestic shareholder in a situation in which the property has an adjusted basis greater than its fair market value on the date of the distribution is set forth.

Rev. Rul. 86–131

ISSUE

How are the earnings and profits of a controlled foreign corporation to be adjusted to reflect a distribution to its domestic shareholder of property that has an adjusted basis that exceeds its fair market value?

FACTS

P, a domestic corporation, owns all of the outstanding stock of *FX1*, a controlled foreign corporation (CFC) within the meaning of section 957(a) of the Internal Revenue Code. On December 31, 1983, *FX1* purchased from an unrelated third party, in a transaction in which gain or loss was recognized, all of the outstanding shares of *FX2*, a CFC engaged in manufacturing.

On July 1, 1985, the fair market value of the *FX2* stock held by *FX1* was 50*x* dollars, and *FX1*'s adjusted basis in the *FX2* stock was 100*x* dollars. On that day, *FX1* distributed all of its *FX* stock to *P*.

On December 31, 1985, *FX1* had accumulated earnings and profits that had been previously included in *P*'s income as subpart F income.

LAW AND ANALYSIS

Since *FX1* acquired the stock of *FX2* within five years of the distribution of such stock in a transaction in which gain or loss was recognized, the distribution described above will not qualify as a taxfree distribution of stock under section 355 of the Code and will be treated as a dividend to the extent provided in sections 301 and 316. Section 355(a)(3)(B).

Section 301(b)(1)(C) of the Code provides that, in the case of a distribution to a corporate shareholder from a foreign corporation, the amount taken into account by the shareholder with respect to the property distributed (other than money) is the fair market value of such property. Under section 301(d)(4), such amount becomes the basis of the distributed property in the hands of the distributee. Under section 301(c)(1), the portion of the distribution that is a dividend, as defined in section 316, is included in gross income.

Section 316(a) of the Code provides that a dividend is any distribution of property made by a corporation to its shareholders out of its earnings and profits. Section 959 of the Code provides specific rules for the application of section 316 to the earnings and profits of a CFC. To the extent that an actual distribution is attributable to earnings and profits described in sections 959(c)(1) and 959(c)(2), which previously have been included in the gross income of a United States shareholder of a CFC, section 959(a) provides that such amount is not to be again included in the gross income of the United States shareholder when actually distributed. Section 959(d) provides that such amounts are generally to be treated as distributions that are not "dividends". Only those distributions, if any, attributable to section 959(c)(3) amounts constitute section 316 dividends. In determining the extent to which distributions are attributable to previously taxed earnings and profits, a distribution made by a foreign corporation is to be considered a distribution first out of earnings and profits attributable to amounts previously included in a United States shareholder's gross income under section 951(a)(1)(B) as an increase in earnings invested in United States property under section 956 (section 959(c)(1)), second as a distribution out of earnings and profits attributable to amounts previously included in gross income of a United States shareholder under section 951(a)(1)(A) as subpart F income (section 959(c)(2)), and finally as a distribution out of other earnings and profts (not yet included in a United States shareholder's income) (section 959(c)(3)).

Section 311(a) of the Code provides that, except as provided in section 311(d), no gain or loss is recognized to a corporation on the distribution of property with respect to its stock. Section 311(d)(1) provides that, if a corporation distributes property (other than an obligation of such corporation) to a corporate shareholder in a distribution to which section 301 applies and the fair market value of such property exceeds its adjusted basis in the hands of the distributing corporation, gain shall be recognized to the distributing corporation in an amount equal to such excess as if the property had been sold at the time of distribution. Section 311(d) does not result in the recognition of a loss on the distribution of property.

Section 312(a) of the Code provides that a corporation that distributes property with respect to its stock must decrease its earnings and profits (to the extent thereof) by the sum of:

(1) the amount of money,

(2) the principal amount of the obligations of such corporation (or, in the case of obligations having original issue discount, the aggregate issue price of such obligations), and

(3) the adjusted basis of the other property so distributed.

Under section 1.312–1(b) of the Income Tax Regulations, the reduction of earnings and profits for the adjusted basis of the "other property," as provided in section 312(a)(3), is to be made regardless of whether the property has appreciated or depreciated in value.

The rules of section 312(a) of the Code apply to distributions by a foreign corporation as well as a domestic corporation. *See H.H. Robertson Co. V. Commissioner*, 59 T.C. 53 (1972), *aff'd*, unpublished opinion (3d Cir. 1974). The distribution of *FX2* stock to *P* by *FX1* constitutes a distribution of "other property" within the meaning of section 312(a)(3) of the Code. The total earnings and profits of *FX1* will be reduced (but not below zero) by the adjusted basis of *FX2* stock distributed to *P* pursuant to section 1.312–1(b) of the regulations.

Because the section 959(c) components are intended to reflect the composition of the CFC's total earnings and profits, the section 959(c) components must be reduced by the same amount as the reduction under section 312(a)(3). However, pursuant to section 959(a), the section 959(c)(1) and 959(c)(2) components are reduced, to the extent thereof, by the amount of the dividend before application of section 959, which, under section 301(b)(1)(C), is generally the fair market value of the property distributed. In order to insure that the sum of the components described in section 959(c) will equal the CFC's total earnings and profits after the application of section 312(a)(3), the section 959(c)(3) component must be increased or decreased so that the total of the adjustments to the section 959(c) components equals the section 312(a)(3) reduction.

In the present situation, since the basis of the *FX2* stock (100*x* dollars) in the hands of *FX1* is in excess of the stock's fair market value (50*x* dollars), *FX1* will reduce its section 959(c)(1) and 959(c)(2) components of earnings and profits, to the extent thereof, by the fair market value of the *FX2* stock distributed to *P* and will reduce its section 959(c)(3) component by an amount equal to the difference between adjusted basis of the *FX2* stock and the amount used to reduce the section 959(c)(1) and 959(c)(2) components of earnings and profits. See the following example:

Earnings and Profits of *FX1* for purposes of section 959

	959(c)(1)	*959(c)(2)*	*959(c)(3)*	*Total*
E&P at 12/31/84	30	25	170	225
Plus E&P from 1985 Operations	*10*	*15*	*30*	*55*
Balance end of year prior to reduction for distribution	40	40	200	280
Reduce the 959(c)(1) and (c)(2) components, to the extent thereof, by the FMV (50*x*) of the *FX2* stock distributed	(40)	(10)	-0-	(50)
Reduce the 959(c)(3) component by the difference between the section 312(a)(3) adjustment (100*x*) and the portion of the FMV of *FX2* stock used to reduce the 959(c)(1) & (c)(2) components (50*x*)	-0-	-0-	(50)	(50)
Adjusted E&P that reflects the application of section 312(a)(3) at 12/31/85	-0-	30	150	180

As a result, *FX1*'s total earnings and profits will be properly adjusted to reflect the application of section 312(a)(3).

In a situation in which the fair market value of the property distributed to *P* by *FX1* exceeds *FX1*'s adjusted basis in such property, section 311(d), as amended by the Tax Reform Act of 1984, would require *FX1* to recognize gain in the amount of the appreciation in the property distributed, thereby increasing FX1's earnings and profits by that amount. *FX1*'s earnings and profits would be reduced (to the extent of *FX1*'s section 312 earnings and profits) by the amount of the basis of the property distributed, as adjusted to reflect the gain recognized on the distribution. This amount would be applied first against the previously taxed section 959(c)(1) and (c)(2) components, to the extent thereof, and the remainder, if any, would be applied against the section 959(c)(3) account.

HOLDING

Following a distribution out of earnings and profits by *FX1* to *P* of *FX2* stock, which had depreciated in value, *FX1*'s total earnings and profits will be adjusted: first, by reducing the section 959(c)(1) component, to the extent thereof, by the fair market value of the property distributed; second, by reducing the section 959(c)(2) component, to the extent thereof, by any excess of the fair market value of the distributed property over the total section 959(c)(1) component; and third, by reducing the section 959(c)(3) component by the difference, if any, between the section 312(a)(3) adjustment and the reductions in the section 959(c)(1) and 959(c)(2) components to reflect the application of section 312(a)(3).

Section 995.—Taxation of DISC Income to Shareholders

Taxation of DISC income to shareholders. This revenue ruling sets forth the "base period T-bill rate" for the periods ending September 30, 1984, September 30, 1985, and September 30, 1986, as required by section 995(f)(4) of the Code.

Rev. Rul. 86–132

Section 995(f)(1) of the Internal Revenue Code provides that a shareholder of a DISC shall pay for each taxable year interest in an amount equal to the product of the shareholder's DISC-related deferred tax liability for such year and the base period T-bill rate. This provision applies to tax years ending after December 31, 1984.

Section 995(f)(4) of the Code provides that the term "base period T-bill rate," as used in section 995(f)(1), means the annual rate of interest determined by the Secretary to be equivalent to the average investment yield of United States Treasury bills with maturities of 52 weeks which were auctioned during the 1 year period ending on September 30 of the calendar year ending with (or of the most recent calendar year ending before) the close of the taxable year of the shareholder.

Accordingly, the base period T-bill rate for the period ending September 30, 1984, is 10.96 percent. The base period T-bill rate for the period ending September 30, 1985, is 8.79 percent. The base period T-bill rate for the period ending September 20, 1986, is 6.92 percent. Pursuant to section 6622 of the Code interest shall be compounded daily.

Set forth below is a table providing factors reflecting daily compounding of the base period T-bill rate for any number of days in the shareholder's taxable year (including a 52-53 week accounting period) for both the 1984 and the 1985 base period T-bill rates. To compute the amount of the interest charge for the shareholder's taxable year, multiply the amount of the shareholder's DISC-related deferred tax liability (as defined in section 995(f)(2) of the Code) for such year by the base period T-bill rate factor corresponding to the number of days in the shareholder's taxable year for which the interest charge is being computed. Generally, the factor to be used will be the factor for 365 days. The factor to be used will be other than the factor for 365 days if the shareholder's taxable year for which the interest charge is being determined is a short taxable year, if the shareholder uses the 52–53 week taxable year, or if the shareholder's taxable year is a leap year.

ANNUAL RATE, COMPOUNDED DAILY

DAYS	10.96 PERCENT FACTOR	8.79 PERCENT FACTOR	6.92 PERCENT FACTOR
1	.000299454	.000240822	.000189589
2	.000598997	.000481702	.000379214
3	.000898630	.000722640	.000568875
4	.001198352	.000963636	.000758572
5	.001498165	.001204690	.000948305
6	.001798067	.001445802	.001138074
7	.002098059	.001686972	.001327878
8	.002398141	.001928200	.001517719
9	.002698312	.002169486	.001707596
10	.002998574	.002410831	.001897509
11	.003298925	.002652233	.002087457
12	.003599367	.002893694	.002277442
13	.003899898	.003135213	.002467463
14	.004200520	.003376789	.002657520
15	.004501231	.003618425	.002847613
16	.004802033	.003860118	.003037742
17	.005102924	.004101869	.003227907
18	.005403906	.004343679	.003418108
19	.005704978	.004585547	.003608345
20	.006006139	.004827473	.003798618
21	.006307392	.005069458	.003988927
22	.006608734	.005311501	.004179272
23	.006910166	.005553602	.004369654
24	.007211689	.005795761	.004560071
25	.007513302	.006037979	.004750525
26	.007815006	.006280255	.004941015
27	.008116800	.006522589	.005131540
28	.008418684	.006764982	.005322102
29	.008720658	.007007433	.005512700
30	.009022723	.007249942	.005703335
31	.009324879	.007492510	.005894005
32	.009627125	.007735136	.006084711
33	.009929461	.007977821	.006275454
34	.010231888	.008220564	.006466233
35	.010534406	.008463366	.006657048
36	.010837014	.008706226	.006847899
37	.011139712	.008949144	.007038786
38	.011442502	.009192122	.007229710
39	.011745382	.009435157	.007420669
40	.012048353	.009678251	.007611665

	ANNUAL RATE, COMPOUNDED DAILY		
DAYS	10.96 PERCENT FACTOR	8.79 PERCENT FACTOR	6.92 PERCENT FACTOR
41	.012351414	.009921404	.007802698
42	.012654566	.010164615	.007993766
43	.012957809	.010407885	.008184870
44	.013261143	.010651213	.008376011
45	.013564568	.010894600	.008567188
46	.013868083	.011138046	.008758402
47	.014171690	.011381550	.008949651
48	.014475387	.011625113	.009140937
49	.014779175	.011868734	.009332259
50	.015083054	.012112415	.009523617
51	.015387025	.012356153	.009715012
52	.015691086	.012599951	.009906443
53	.015995238	.012843807	.010097910
54	.016299482	.013087722	.010289414
55	.016603816	.013331696	.010480953
56	.016908242	.013575728	.010672529
57	.017212759	.013819820	.010864142
58	.017517367	.014063970	.011055791
59	.017822066	.014308179	.011247476
60	.018126856	.014552446	.011439197
61	.018431738	.014796773	.011630955
62	.018736711	.015041158	.011822749
63	.019041775	.015285602	.012014580
64	.019346931	.015530105	.012206446
65	.019652178	.015774667	.012398350
66	.019957516	.016019288	.012590289
67	.020262946	.016263968	.012782265
68	.020568468	.016508706	.012974278
69	.020874081	.016753504	.013166327
70	.021179785	.016998360	.013358412
71	.021485581	.017243276	.013550534
72	.021791468	.017488250	.013742692
73	.022097447	.017733284	.013934886
74	.022403518	.017978376	.014127117
75	.022709680	.018223528	.014319384
76	.023015934	.018468738	.014511688
77	.023322280	.018714008	.014704029
78	.023628718	.018959336	.014896405
79	.023935247	.019204724	.015088819
80	.024241868	.019450171	.015281268
81	.024548581	.019695677	.015473754
82	.024855386	.019941242	.015666277
83	.025162282	.020186866	.015858836
84	.025469271	.020432550	.016051432
85	.025776351	.020678292	.016244064
86	.026083523	.020924094	.016436733
87	.026390788	.021169955	.016629438
88	.026698144	.021415875	.016822180
89	.027005593	.021661854	.017014958
90	.027313133	.021907893	.017207773
91	.027620766	.022153991	.017400625
92	.027928490	.022400148	.017593513
93	.028236307	.022646364	.017786437
94	.028544216	.022892640	.017979399
95	.028852217	.023138975	.018172396

DAYS	ANNUAL RATE, COMPOUNDED DAILY 10.96 PERCENT FACTOR	 8.79 PERCENT FACTOR	 6.92 PERCENT FACTOR
96	.029160311	.023385369	.018365431
97	.029468497	.023631823	.018558502
98	.029776775	.023878336	.018751609
99	.030085145	.024124908	.018944753
100	.030393608	.024371540	.019137934
101	.030702163	.024618231	.019331151
102	.031010810	.024864981	.019524405
103	.031319550	.025111791	.019717696
104	.031628382	.025358661	.019911023
105	.031937307	.025605589	.020104387
106	.032246324	.025852578	.020297788
107	.032555434	.026099626	.020491225
108	.032864636	.026346733	.020684699
109	.033173931	.026593900	.020878210
110	.033483319	.026841126	.021071757
111	.033792799	.027088412	.021265341
112	.034102372	.027335757	.021458962
113	.034412038	.027583162	.021652619
114	.034721796	.027830627	.021846313
115	.035031647	.028078151	.022040044
116	.035341591	.028325735	.022233812
117	.035651628	.028573378	.022427616
118	.035961757	.028821081	.022621457
119	.036271980	.029068844	.022815335
120	.036582295	.029316666	.023009250
121	.036892703	.029564548	.023203201
122	.037203205	.029812490	.023397189
123	.037513799	.030060491	.023591214
124	.037824486	.030308552	.023785276
125	.038135266	.030556673	.023979374
126	.038446140	.030804854	.024173509
127	.038757106	.031053094	.024367681
128	.039068165	.031301394	.024561890
129	.039379318	.031549754	.024756136
130	.039690564	.031798174	.024950419
131	.040001903	.032046654	.025144738
132	.040313335	.032295193	.025339094
133	.040624861	.032543793	.025533487
134	.040936480	.032792452	.025727917
135	.041248192	.033041171	.025922384
136	.041559997	.033289950	.026116888
137	.041871896	.033538789	.026311428
138	.042183888	.033787687	.026506005
139	.042495974	.034036646	.026700620
140	.042808153	.034285665	.026895271
141	.043120426	.034534743	.027089959
142	.043432792	.034783882	.027284684
143	.043745251	.035033081	.027479446
144	.044057805	.035282339	.027674245
145	.044370451	.035531658	.027869081
146	.044683192	.035781037	.028063953
147	.044996026	.036030476	.028258863
148	.045308954	.036279974	.028453810
149	.045621975	.036529533	.028648793
150	.045935090	.036779152	.028843814

	ANNUAL RATE, COMPOUNDED DAILY		
DAYS	10.96 PERCENT FACTOR	8.79 PERCENT FACTOR	6.92 PERCENT FACTOR
151	.046248299	.037028831	.029038871
152	.046561602	.037278571	.029233966
153	.046874999	.037528370	.029429097
154	.047188489	.037778230	.029624266
155	.047502074	.038028149	.029819471
156	.047815752	.038278129	.030014714
157	.048129524	.038528170	.030209993
158	.048443390	.038778270	.030405310
159	.048757350	.039028430	.030600663
160	.049071404	.039278651	.030796054
161	.049385552	.039528932	.030991481
162	.049699795	.039779274	.031186946
163	.050014131	.040029675	.031382448
164	.050328561	.040280137	.031577987
165	.050643086	.040530660	.031773562
166	.050957705	.040781242	.031969175
167	.051272418	.041031885	.032164825
168	.051587225	.041282588	.032360513
169	.051902127	.041533352	.032556237
170	.052217122	.041784176	.032751998
171	.052532213	.042035061	.032947797
172	.052847397	.042286005	.033143632
173	.053162676	.042537011	.033339505
174	.053478049	.042788077	.033535415
175	.053793517	.043039203	.033731362
176	.054109079	.043290389	.033927346
177	.054424736	.043541637	.034123367
178	.054740487	.043792944	.034319426
179	.055056333	.044044313	.034515521
180	.055372273	.044295741	.034711654
181	.055688308	.044547231	.034907824
182	.056004438	.044798780	.035104031
183	.056320662	.045050391	.035300276
184	.056636981	.045302062	.035496557
185	.056953395	.045553794	.035692876
186	.057269903	.045805586	.035889232
187	.057586507	.046057439	.036085625
188	.057903205	.046309352	.036282056
189	.058219997	.046561327	.036478524
190	.058536885	.046813361	.036675028
191	.058853868	.047065457	.036871571
192	.059170945	.047317613	.037068150
193	.059488118	.047569830	.037264767
194	.059805385	.047822108	.037461421
195	.060122748	.048074447	.037658112
196	.060440206	.048326846	.037854841
197	.060757758	.048579306	.038051607
198	.061075406	.048831827	.038248410
199	.061393148	.049084409	.038445251
200	.061710986	.049337051	.038642128
201	.062028920	.049589755	.038839044
202	.062346948	.049842519	.039035996
203	.062665071	.050095344	.039232986
204	.062983290	.050348230	.039430013
205	.063301604	.050601177	.039627078

	ANNUAL RATE, COMPOUNDED DAILY		
DAYS	10.96 PERCENT FACTOR	8.79 PERCENT FACTOR	6.92 PERCENT FACTOR
206	.063620014	.050854185	.039824180
207	.063938519	.051107253	.040021319
208	.064257119	.051360383	.040218495
209	.064575814	.051613574	.040415709
210	.064894605	.051866825	.040612961
211	.065213492	.052120138	.040810250
212	.065532474	.052373511	.041007576
213	.065851551	.052626946	.041204940
214	.066170724	.052880442	.041402341
215	.066489993	.053133998	.041599779
216	.066809357	.053387616	.041797255
217	.067128817	.053641295	.041994768
218	.067448373	.053895035	.042192319
219	.067768024	.054148836	.042389907
220	.068087771	.054402698	.042587533
221	.068407613	.054656621	.042785196
222	.068727552	.054910606	.042982897
223	.069047586	.055164651	.043180635
224	.069367716	.055418758	.043378411
225	.069687942	.055672926	.043576224
226	.070008264	.055927155	.043774074
227	.070328682	.056181446	.043971962
228	.070649195	.056435797	.044169888
229	.070969805	.056690210	.044367851
230	.071290511	.056944684	.044565852
231	.071611313	.057199220	.044763890
232	.071932210	.057453816	.044961966
233	.072253204	.057708474	.045160079
234	.072574294	.057963194	.045358230
235	.027895481	.058217975	.045556419
236	.073216763	.058472817	.045754645
237	.073538141	.058727720	.045952908
238	.073859616	.058982685	.046151210
239	.074181187	.059237711	.046349548
240	.074502855	.059492799	.046547925
241	.074824618	.059747948	.046746339
242	.075146478	.060003158	.046944790
243	.075468435	.060258430	.047143280
244	.075790488	.060513764	.047341807
245	.076112637	.060769159	.047540371
246	.076434883	.061024615	.047738973
247	.076757225	.061280133	.047937613
248	.077079664	.061535713	.048136291
249	.077402199	.061791354	.048335006
250	.077724831	.062047057	.048533759
251	.078047560	.062302821	.048732549
252	.078370385	.062558647	.048931377
253	.078693307	.062814534	.049130243
254	.079016325	.063070483	.049329147
255	.079339440	.063326494	.049528088
256	.079662652	.063582566	.049727067
257	.079985961	.063838700	.049926084
258	.080309367	.064094896	.050125138
259	.080632869	.064351153	.050324231
260	.080956469	.064607472	.050523360

	ANNUAL RATE, COMPOUNDED DAILY		
DAYS	10.96 PERCENT FACTOR	8.79 PERCENT FACTOR	6.92 PERCENT FACTOR
261	.081280165	.064863853	.050722528
262	.081603958	.065120296	.050921734
263	.081927848	.065376800	.051120977
264	.082251835	.065633366	.051320258
265	.082575920	.065889994	.051519577
266	.082900101	.066146683	.051718933
267	.083224379	.066403435	.051918328
268	.083548754	.066660248	.052117760
269	.083873227	.066917123	.052317230
270	.084197797	.067174060	.052516738
271	.084522464	.067431059	.052716283
272	.084847228	.067688120	.052915867
273	.085172089	.067945243	.053115488
274	.085497048	.068202427	.053315147
275	.085822104	.068459674	.053514844
276	.086147257	.068716983	.053714579
277	.086472508	.068974353	.053914352
278	.086797856	.069231785	.054114163
279	.087123301	.069489280	.054314011
280	.087448844	.069746836	.054513897
281	.087774484	.070004455	.054713822
282	.088100222	.070262135	.054913784
283	.088426058	.070519878	.055113784
284	.088751991	.070777683	.055313822
285	.089078022	.071035549	.055513898
286	.089404150	.071293478	.055714012
287	.089730376	.071551469	.055914164
288	.090056699	.071809522	.056114353
289	.090383121	.072067637	.056314581
290	.090709640	.072325815	.056514847
291	.091036257	.072584054	.056715150
292	.091362971	.072842356	.056915492
293	.091689784	.073100720	.057115872
294	.092016694	.073359146	.057316289
295	.092343703	.073617635	.057516745
296	.092670809	.073876815	.057717238
297	.092998013	.071434798	.057917770
298	.093325315	.074393473	.058118340
299	.093652715	.074652211	.058318947
300	.093980213	.074911011	.058519593
301	.094307810	.075169873	.058720277
302	.094635504	.075428797	.058920998
303	.094963297	.075687784	.059121758
304	.095291187	.075946833	.059322556
305	.095619176	.076205945	.059523392
306	.095947263	.076465119	.059724266
307	.096275448	.076724355	.059925178
308	.096603732	.076983654	.060126128
309	.096932114	.077243015	.060327117
310	.097260594	.077502439	.060528143
311	.097589173	.077761925	.060729207
312	.097917850	.078021474	.060930310
313	.098246625	.078281085	.061131451
314	.098575499	.078540759	.061332630
315	.098904471	.078800495	.061533847

ANNUAL RATE, COMPOUNDED DAILY

DAYS	10.96 PERCENT FACTOR	8.79 PERCENT FACTOR	6.92 PERCENT FACTOR
316	.099233542	.079060294	.061735102
317	.099562711	.079320155	.061936395
318	.099891979	.079580079	.062137727
319	.100221346	.079840066	.062339097
320	.100550811	.080100115	.062540504
321	.100880375	.080360227	.062741950
322	.101210038	.080620401	.062943435
323	.101539799	.080880638	.063144957
324	.101869659	.081140938	.063346518
325	.102199618	.081401301	.063548117
326	.102529675	.081661726	.063749754
327	.102859832	.081922213	.063951429
328	.103190087	.082182764	.064153142
329	.103520441	.082443377	.064354894
330	.103850894	.082704053	.064556684
331	.104181446	.082964792	.064758513
332	.104512097	.083225594	.064960379
333	.104842847	.083486458	.065162284
334	.105173697	.083747386	.065364227
335	.105504645	.084008376	.065566208
336	.105835692	.084269429	.065768228
337	.106166838	.084530545	.065970286
338	.106498084	.084791723	.066172382
339	.106829429	.085052965	.066374517
340	.107160873	.085314270	.066576690
341	.107492416	.085575637	.066778901
342	.107824059	.085837067	.066981151
343	.108155800	.086098561	.067183439
344	.108487642	.086360117	.067385765
345	.108819582	.086621737	.067588130
346	.109151622	.086883419	.067790533
347	.109483762	.087145164	.067992974
348	.109816000	.087406973	.068195454
349	.110148339	.087668844	.068397972
350	.110480777	.087930778	.068600528
351	.110813314	.088192776	.068803123
352	.111145951	.088454837	.069005757
353	.111478688	.088716961	.069208428
354	.111811524	.088979147	.069411139
355	.112144460	.089241397	.069613887
356	.112477495	.089503711	.069816674
357	.112810631	.089766087	.070019500
358	.113143866	.090028527	.070222364
359	.113477201	.090291029	.070425266
360	.113810635	.090553595	.070628207
361	.114144170	.090816225	.070831187
362	.114477804	.091078917	.071034204
363	.114811539	.091341673	.071237261
364	.115145373	.091604492	.071440356
365	.115479307	.091867374	.071643489
366	.115813341	.092130320	.071846661
367	.116147476	.092393329	.072049871
368	.116481710	.092656401	.072253120
369	.116816044	.092919536	.072456408
370	.117150479	.093182735	.072659734
371	.117485014	.093445998	.072863098

Section 3221.—Rate of Tax

[Railroad Retirement Tax Act]

Determination of Quarterly Rate of Excise Tax for Railroad Retirement Supplemental Annuity Program

In accordance with directions in section 3221(c) of the Railroad Retirement Tax Act (26 U.S.C., Section 3221(c)), the Railroad Retirement Board has determined that the excise tax imposed by such section 3221(c) on every employer, with respect to having individuals in his employ, for each work-hour for which compensation is paid by such employer for services rendered to him during the quarter beginning January 1, 1987 shall be at the rate of 24 cents.

In accordance with directions in section 15(a) of the Railroad Retirement Act of 1974, the Railroad Retirement Board has determined that for the quarter beginning January 1, 1987, 29.0 percent of the taxes collected under sections 3211(b) and 3221(c) of the Railroad Retirement Tax Act shall be credited to the Railroad Retirement Account and 71.0 percent of the taxes collected under such sections 3211(b) and 3221(c) plus one hundred percent of the taxes collected under section 3221(d) of the Railroad Retirement Tax Act shall be credited to the Railroad Retirement Supplemental Account.

Dated: October 16, 1986.
By Authority of the Board.
BEATRICE EZERSKI,
Secretary to the Board.

(Filed by the Office of the Federal Register on October 22, 1986, 8:45 a.m., and published in the issue of the Federal Register for October 23, 1986, 51 F.R. 37687)

Section 382.—Limitation on Net Operating Loss Carryovers and Certain Built-In Losses Following Change in Control

Rev. Rul. 86–133

Sections 382 and 383 of the Internal Revenue Code were amended by section 621(a) and (b) of the Tax Reform Act of 1986 (the Act), Pub. L. No. 99–514, 100 Stat. _____. Following an "ownership change" as defined in section 382(g), sections 382 and 383 annually limit the amount of a corporation's (1) taxable income that can be offset by certain of its net operating loss (NOL) carryforwards and by other tax attributes, and (2) income tax liability that can be offset by other tax attributes. The NOL carryforwards and other tax attributes to which the limit applies are those that were available prior to the ownership change. This annual limitation is called "the section 382 limitation."

Section 382(b)(1) defines the section 382 limitation for any tax year ending after an ownership change as, in general, an amount equal to (A) the value of the stock of the corporation immediately prior to the ownership change, multiplied by (B) the long-term tax-exempt rate. Section 382(f)(1) provides that the long-term tax-exempt rate shall be the highest of the adjusted federal long-term rates in effect for any month in the three-calendar-month period ending with the calendar month in which the ownership change occurs. Section 382(f)(2) defines the term "adjusted federal long-term rate" as the federal long-term rate determined under section 1274(d), except that (A) paragraphs (2) and (3) thereof shall not apply, and (B) such rate shall be properly adjusted for differences between rates on long-term taxable and tax-exempt obligations. The Conference Report for the Act indicates that the adjusted federal long-term rate is to be computed as the yield on a diversified pool of prime, general obligation tax-exempt bonds with remaining periods to maturity of more than nine years. 2 H.R. Rep. No. 99–841 (Conf. Rep.), 99th Cong., 2d Sess. II–188 (1986).

Section 621(f) of the Act provides that the amendments made by section 621(a) and (b), in general, shall apply to any ownership change following (A) an owner shift involving a 5-percent shareholder, occurring after December 31, 1986, or (B) an equity structure shift occurring pursuant to a plan of reorganization adopted after December 31, 1986.

The adjusted federal long-term rate for the purpose of determining the long-term tax-exempt rate under section 382 is 6.41 percent for November 1986. This monthly rate is calculated in the same manner as the adjusted applicable federal rates for purposes of section 1288 are calculated.

To determine the long-term tax-exempt rate for purposes of section 382(b)(1)(B) of the Code for ownership changes that occur during January 1987, taxpayers must compare the adjusted federal long-term rates for November 1986, December 1986, and January 1987. The highest of these three adjusted federal long-term rates is the long-term tax-exempt rate for January 1987.

Each month, pursuant to section 1274(d), the Internal Revenue Service publishes a revenue ruling containing the applicable federal rates, including the federal long-term rates. In the future, the adjusted federal long-term rate for purposes of section 382 will also be published monthly in that revenue ruling. This monthly publication, starting with the rates for January 1987, will also specify the long-term tax-exempt rate for ownership changes that occur during that month (that is the highest of the adjusted federal long-term rates for that month and the prior two months).

Section 1288.—Treatment of Original Issue Discount on Tax Exempt Obligations

Rev. Rul. 86–135

Section 1288(b)(1) of the Internal Revenue Code provides that in applying section 483 or 1274 to determine original issue discount on tax-exempt obligations, appropriate adjustments shall be made to the section 1274 applicable federal rate (AFR) to take into account the tax exemption for interest on the obligations. Section 382(f)(1) provides that the long-term tax-exempt rate for purposes of section 382 shall be the highest of the adjusted federal long-term rates for the three months ending with the month in which the particular ownership change occurs. See Rev. Rul. 86–133, this page.

The AFR adjusted for section 1288 purposes (adjusted AFR) and the adjusted federal long-term rate for section 382 purposes for the month of November 1986 are listed below. In the future, the adjusted AFR, the adjusted federal long-term rate, and the long-term tax-exempt rate will be published on a monthly basis in conjunction with the AFR.

November 1986
Section 1288 Adjusted Federal Rates

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term	4.46%	4.41%	4.39%	4.37%
Mid-Term	5.36%	5.29%	5.36%	5.23%
Long-Term	6.41%	6.31%	6.26%	6.23%

Section 382 Rates

Adjusted federal long-term rate for November	6.41%
Long-term tax-exempt rate for ownership changes during __*__ (the highest of the adjusted federal long-term rates for the current month and the prior two months)	**

*Specific month to be supplied beginning in January 1987.

**To be supplied monthly beginning in January 1987.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.201: Rulings and determination letters.
(Also Part I, Section 501; 1.501(c)(3)–1.)

Rev. Proc. 86–43

SECTION 1. PURPOSE

The purpose of this revenue procedure is to publish the criteria used by the Internal Revenue Service to determine the circumstances under which advocacy of a particular viewpoint or position by an organization is considered educational within the meaning of section 501(c)(3) of the Internal Revenue Code, and within the meaning of section 1.501(c)(3)–1(d)(3) of the Income Tax Regulations.

SEC. 2. BACKGROUND

.01 Section 501(c)(3) of the Code provides for exemption from federal income tax for organizations that are organized and operated exclusively for purposes specified in that section, including educational purposes. Section 1.501(c)(3)–1(d)(3) of the regulations provides that the term "educational" relates to a) the instruction or training of the individual for the purpose of improving or developing his capabilities; or b) the instruction of the public on subjects useful to the individual and beneficial to the community. Under this regulation, an organization may be educational even though it advocates a particular position or viewpoint, so long as it presents a sufficiently full and fair exposition of the pertinent facts as to permit an individual or the public to form an independent opinion or conclusion. On the other hand, an organization is not educational if its principal function is the mere presentation of unsupported opinion.

.02 In applying section 1.501(c)(3)–1(d)(3) of the regulations, the Service has attempted to eliminate or minimize the potential for any public official to impose his or her preconceptions or beliefs in determining whether the particular viewpoint or position is educational. It has been, and it remains, the policy of the Service to maintain a position of disinterested neutrality with respect to the beliefs advocated by an organization. The focus of section 1.501(c)(3)–1(d)(3), and of the Service's application of this regulation, is not upon the viewpoint or position, but instead upon the method used by the organization to communicate its viewpoint or positions to others.

.03 Two recent court decisions have considered challenges to the constitutionality of section 1.501(c)(3)–1(d)(3) of the regulations. One decision held that the regulation was unconstitutionally vague. *Big Mama Rag, Inc. v. United States*, 631 F. 2d. 1030 (D.C. Cir. 1980). However, in *National Alliance v. United States*, 710 F. 2d 868 (D.C. Cir. 1983), the court upheld the Service's position that the organization in question was not educational. Although the latter decision did not reach the question of the constitutionality of section 1.501(c)(3)–1(d)(3), it did note that the methodology test used by the Service when applying the regulation "tend[s] toward ensuring that the educational exemption be restricted to material which substantially helps a reader or listener in a learning process." The court also noted that the application of this test reduced the vagueness found in the earlier *Big Mama Rag* decision.

.04 The methodology test cited by the court in *National Alliance* reflects the longstanding Service position that the method used by an organization in advocating its position, rather than the position itself, is the standard for determining whether an organization has educational purposes. This methodology test is set forth in Section 3 of this revenue procedure, and is used in all situations where the educational purposes of an organization that advocates a particular viewpoint or position are in question. Publication of this test represents no change either to existing procedures or to the substantive position of the Service.

SEC. 3. CRITERIA USED TO DETERMINE WHETHER ADVOCACY BY AN ORGANIZATION IS EDUCATIONAL

.01 The Service recognizes that the advocacy of particular viewpoints or positions may serve an educational purpose even if the viewpoints or positions being advocated are unpopular or are not generally accepted.

.02 Although the Service renders no judgment as to the viewpoint or position of the organization, the Service will look to the method used by the organization to develop and present its views. The method used by the organization will not be considered educational if it fails to provide a factual foundation for the viewpoint or position being advocated, or if it fails to provide a development from the relevant facts that would materially aid a listener or reader in a learning process.

.03 The presence of any of the following factors in the presentations made by an organization is indicative that the method used by the organization to advocate its viewpoints or positions is not educational.

1 The presentation of viewpoints or positions unsupported by facts is a significant portion of the organization's communications.

2 The facts that purport to support the viewpoints or positions are distorted.

3 The organization's presentations make substantial use of inflammatory and disparaging terms and express conclusions more on the basis of strong emotional feelings than of objective evaluations.

4 The approach used in the organization's presentations is not aimed at developing an understanding on the part of the intended audience or readership because it does not consider their background or training in the subject matter.

.04 There may be exceptional circumstances, however, where an organization's advocacy may be educational even if one or more of the factors listed in section 3.03 are present. The Service will look to all the facts and circumstances to determine whether an organization may be considered educational despite the presence of one or more of such factors.

SEC. 4. OTHER REQUIREMENTS

Even if the advocacy undertaken by an organization is determined to be educational under the above criteria, the organization must still meet all other requirements for exemption under section 501(c)(3), including the restrictions on influencing legislation and political campaigning contained therein.

Treasury Department Order
Order Number 150–02

Establishment of Certain Offices in the National Office of the Internal Revenue Service

By the authority vested in me as Secretary of the Treasury by Section 1002 of 31 U.S.C.; Section 7801(a) and 7803 of the Internal Revenue Code of 1954, as amended; Section 321(b) of 31 U.S.C., and Reorganization Plan No. 1 of 1952 as made applicable to the International Revenue Code of 1954 by Section 7804(a) of such Code and by Executive Order No. 10574, approved November 5, 1954; and as provided by Section 7802(b) of the Internal Revenue Code of 1954, the following offices continue uninterrupted as they existed prior to this order, with the following changes:

The office of Assistant Commissioner (Support and Services) under the Associate Commissioner (Policy and Management) is abolished;

The title of Assistant Commissioner (Human Resources) is changed to Assistant Commissioner (Human Resources Management and Support); and

Certain functional responsibilities are moved from the Office of the Associate Commissioner (Policy and Management). Specificially, functional responsibility for disclosure and for administration of regulations governing the practice of representives before the Service and the Bureau of Alcohol, Tobacco and Firearms are moved to the Associate Commissioner (Operations); functional responsibility for data security and for tax form and publication design is moved to the Associate Commissioner (Data Processing).

Also with this order, a paragraph on Assistant to the Commissioner (Legislative Liaison), published at the time of that position's creation, is dropped because that office is listed elsewhere, and other portions of text are resequenced and reworded solely for clarity, with no change in meaning.

1. *Office of Commissioner of Internal Revenue.* The Office of the Commissioner shall consist of the Commissioner, Deputy Commissioner, Assistants to the Commissioner, the Assistant to the Commissioner (Public Affairs), Assistant to the Commissioner (Legislative Liaison), Assistant to the Commissioner (Taxpayer Ombudsman), Assistant to the Commissioner (Equal Opportunity) and the Assistant to the Deputy Commissioner.

a. Except for the specific positions and titles in Sections 1 through 5 of this order, the Commissioner may create, abolish, or modify offices and positions within the Internal Revenue Service as may be necessary to effectively and efficiently provide for the administration of tax laws or other responsibilities assigned to the Internal Revenue Service. The authority of the Commissioner to create, abolish, or modify offices under this delegation is subject only to limitations that exist by law or Department of the Treasury rules and regulations.

2. *Office of the Associate Commissioner (Operations).* The Associate Commissioner (Operations) is the principal advisor to the Commissioner on policy matters affecting operations. The Associate Commissioner (Operations) is responsible for the following activities:

a. Serves as the spokesperson for the operating functions, which are: collection of delinquent accounts and securing of delinquent returns; investigation of criminal fraud involving any internal revenue laws (except those concerning alcohol, tobacco, or firearms); examination of tax returns; approval and subsequent examination of Employee Plans and Exempt Organizations; guidance on tax treaty administration, international compliance, and foreign tax administration assistance; disclosure; and adminstration of regulations governing the practice of representatives before the Internal Revenue Service and the Bureau of Alcohol, Tobacco and Firearms.

b. Supervises and provides policy guidance and direction to the Assistant Commissioner (Collection), Assistant Commissioner (Examination), Assistant Commissioner (Criminal Investigation), Assistant Commissioner (Employee Plans and Exempt Organizations); and the Assistant Commissioner (International).

c. Represents the Service, as designated by the Commissioner, to the Department of the Treasury, Office of Management and Budget, Congress, foreign tax authorities and the public on major cross-functional issues and discusses or explains the Service's policy formulation and long-term plans.

3. *Office of Associate Commissioner (Policy and Management).* The Associate Commissioner (Policy and Management) is the principal advisor to the Commissioner on policy matters affecting agency administration. The Associate Commissioner (Policy and Management) is responsible for the following activities:

a. Serves as the spokesperson for the management functions, which are: personnel administration; financial management; planning; research; training and employee development; management of the Service's real and personal property, equipment and support services; and operation of the Data Center.

b. Supervises and provides policy guidance and direction to the Assistant Commissioner (Human Resources Management and Support) and the Assistant Commissioner (Planning, Finance, and Research).

c. Represents the Service, as designated by the Commissioner, to the Department of the Treasury, Office of Management and Budget, Congress, and the public on major policy and management issues, and discusses or explains the Service's policy formulation and long-term plans.

4. *Office of Associate Commissioner (Data Processing).* The Associate Commissioner (Data Processing) is the principal advisor to the Commissioner on policy matters affecting data processing. The Associate Commissioner (Data Processing) is responsible for the following activities:

a. Serves as the spokesperson for the data processing functions, which are: processing of tax returns and information documents; accounting for all revenues collected by the Service; maintaining master files of all taxpayer accounts; managing all large-scale tax-processing computers in the Service, the tax information program; tax form and publication design; data security; and designing, developing, testing, and maintaining computer software used on large-scale tax-processing computers in the Service.

b. Supervises and provides policy guidance and direction to the Assistant Commissioner (Computer Services), the Assistant Commissioner (Returns and Information Processing), and the Assistant Commissioner (Tax System Redesign).

c. Represents the Service, as designated by the Commissioner, to the Department of the Treasury, Office of Management and Budget, Congress, and the public on major data processing issues, and discusses or explains the Service's policy formulation and long-term plans.

5. *The Assistant and Commissioner (Inspection) and the Deputy Assistant Commissioner (Inspection)* will, to ensure objectivity and integrity, report directly to the Commissioner and Deputy Commissioner.

6. *The Chief Counsel,* pursuant to delegated authority from the General Counsel, is authorized to take necessary action on all personnel and administrative matters pertaining to the Office of Chief Counsel, including but not limited to those

for the appointment, classification, promotion, demotion, reassignment, transfer or separation of officers or employees; however, all personnel and administrative matters concerning Senior Executive Service or Performance Management Recognition System employees in the Office of Associate Chief Counsel (International) whose primary duties do not involve litigation or in the Office of Associate Chief Counsel (Technical), shall be approved by the Commissioner of Internal Revenue prior to implementation.

a. The Corporation Tax and Individual Tax Divisions are under the supervision of the Chief Counsel, with the authority to supervise and evaluate the work of all offices and employees of these functions.

b. The Appeals Division is under the supervision of the Chief Counsel, and the Commisisioner of Internal Revenue will exercise line supervision over the Chief Counsel for this function.

c. The Commissioner of Internal Revenue will exercise the Service's final authority concerning substantive interpretation of the tax laws as reflected in legislative and regulatory proposals, revenue rulings, letter rulings, and technical advice memoranda.

7. The above changes shall be implemented at a date determined by the Commissioner of Internal Revenue. Effective immediately, the Commissioner of Internal Revenue is authorized to effect, at appropriate times and in an orderly manner, such transfers of functions, personnel, positions, equipment and funds as may be necessary to implement the provisions of this order.

8. All offices in existence within the Internal Revenue Service but not mentioned in this order are continued without interruption.

9. *Effect on Other Treasury Department Orders.* This order supersedes Treasury Department Order: 150–02, February 27, 1986.

Dated: July 30, 1986
James A. Baker III,

Secretary of
the Treasury.

(Filed by the Office of the Federal Register on August 20, 1986, 8:45 a.m., and published in the issue of the Federal Register for August 21, 1986, 51 F.R. 30022)

Determination and Opinion Letters Issued After the Tax Reform Act of 1986

Notice 86–13

BACKGROUND

The Tax Reforms Act of 1986 (P.L. 99–514) (Act), enacted on October 22, 1986, changed several of the qualification requirements under the Internal Revenue Code (Code) applicable to pension, profit-sharing and stock bonus plans. While most of the new qualification requirements are not effective until plan years beginning after December 31, 1986 or December 31, 1988, the provisions of the Act described below are effective retroactively.

1. Section 1136 of the Act and section 401(a)(27) of the Code. For years beginning after December 31, 1985, employer contributions to a profit sharing plan will not be limited to the employer's current or accumulated profits.

2. Section 1119 of the Act and section 401(a)(8) of the Code. For plan years beginning after December 31, 1985, forfeitures in a money purchase pension plan may be reallocated to other participants.

3. Section 1139 of the Act and sections 411(a)(11) and 417(e) of the Code. Generally, for plan years beginning after December 31, 1984, with respect to a distribution to a participant or beneficiary from a defined benefit plan where the present value of the total benefit exceeds $25,000, the maximum interest rate that may be used to determine such value is the lesser of the plan rate or 120% of the rate(s) the Pension Benefit Guaranty Corporation would use to value the benefit on plan termination.

4. Section 1116 of the Act and section 401(k) of the Code. A qualified cash or deferred arrangement described in section 401(k) of the Code may permit a participant to withdraw elective deferrals upon the occurrence of several specific events including termination of the plan, sale of substantially all the assets used in the trade or business, and sale of a subsidiary of a corporation. This provision is effective for distributions after December 31, 1984.

5. Section 1174 of the Act and section 409(d) of the Code. Effective for terminations of tax credit employee stock ownership plans after December 31, 1984, termination of the plan has been added to the exceptions to the requirement that employer securities may not be distributed from a participant's account before the end of the 84th month following allocation to the participant's account.

SCOPE OF PROGRAM

Effective with the enactment of the Act, until further notice is given, plans receiving determination and opinion letters from the Service will not have been reviewed for the qualification requirements of the Code as changed by the Act. However, any amendments by the Act of the qualification requirements of the Code that the Service may consider in the future will be specifically stated on such determination or opinion letters. The sponsor of a plan drafted to comply with the qualification requirements of the Code as they were in effect immediately before the enactment of the Act may rely on the Service's approval of the plan's language, as expressed in a determination or opinion letter, until further amendments are required by the Act.

Thus, plans that do not utilize the provisions described in Items 1 through 5 above will receive determination or opinion letters based on the qualification requirements in effect prior to the enactment of the Act. The language of such plans will not need to be amended until further notice.

Plans that do utilize any provision described in Items 1 through 5 above will not receive adverse determination or opinion letters by reason of such provisions. However, determination or opinion letters issued to such plans may not be relied upon with respect to whether such provisions meet the requirements of the Act.

The Act also contains Technical Corrections to the Tax Reform Act of 1984 and to the Retirement Equity Act. Some of the corrections are retroactively effective. The Service will review plans for compliance with the retroactively effective technical corrections that affect plan qualification. Sponsors of plans receiving favorable determination or opinion letters issued after enactment of the Act may rely on the Service's approval of the plan's language with respect to these provisions.

Taxpayers with questions or comments with respect to the application of this notice should call 202-566-3149 (not a toll-free number). Such communications will be considered in developing further guidance.

Part IV. Items of General Interest

Tax Reform Act of 1986—Comments on Projects to Implement

Announcement 86–110[1]

The Service asked for public comment on projects needed to implement the Tax Reform Act of 1986.

The Service released two lists, one presenting provisions of the Tax Reform Act of 1986 that are being given priority for early guidance by the Service and the Treasury Department and the other presenting regulations projects on which advice from professional organizations, law and accounting firms, and interested taxpayers is specifically requested.

The Service welcomes comments concerning the relative priority of the provisions listed and invites suggestions for additions to the list.

Submissions concerning regulations projects should identify issues on which guidance is needed and, if possible, analyze the issues and recommend how they should be resolved. Submissions are also invited concerning any other provisions of the Act. In many instances the Service will use means other than regulations to provide early guidance.

All comments or submissions should be addressed to:

Commissioner of Internal Revenue
CC:LR:T
Internal Revenue Service
Room 4429
Washington, D.C. 20224

The two lists are attached. The Service requests comments concerning projects on the priority list by Nov. 28, 1986, and all other comments as soon as possible. All material submitted will be available for public inspection and copying.

PRIORITY LIST

Act Sec.	*Subject*
—	Limits on Accounting Period Changes
—	Elections under Tax Reform Act of 1986
111	Increase in Earned Income Credit
121–23	Tax Treatment of Unemployment Compensation, Prizes and Awards, and Scholarships
132	Two-Percent Floor on Itemized Deductions
133	Medical Expense Deduction
142	Meals, Travel and Entertainment
144	Tax-Free Housing Allowances
201	Accelerated Cost Recovery System
211–13	Repeal of Investment Tax Credit
221	Limit on Use of Business Tax Credit
231	Research Credit
251	Rehabilitation Credit
252	Low-Income Housing Credit
405	Discharge of Indebtedness for Farmers
501	Limits on Passive Losses
501, 511 & 803	Coordination of Interest Deduction Limits
503	At-Risk Rules for Real Estate
511	Limits on Nonbusiness Interest
621	Limits on NOL Carryovers
631	Gain or Loss on Liquidation
641	Special Allocation Rules for Certain Asset Acquisitions
701	Alternative Minimum Tax
801	Limits on Use of Cash Method
802	Simplified Dollar Value LIFO Method for Small Businesses
803	Capitalization of Property-Production Costs
804	Accounting for Long-Term Contracts
806	Taxable Years of Certain Entities
811–12	Installment Obligations
1001	Exclusion for Interest on Installment Payments of Life Insurance Proceeds
1023	Discounting of Unpaid Losses of Property and Casualty Insurance Companies
1101–03	Individual Retirement Accounts
1105	$7,000 Limitations on Elective Deferrals
1106	Limits on Contributions and Benefits under Qualified Plans

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[1] Based on News Release IR–86–143, dated October 23, 1986.

PRIORITY LIST

Act Sec.	*Subject*
1107	Deferred Compensation Plans of State and Local Governments
1114	Definition of Highly Compensated Employee
1117	Nondiscrimination Requirements for Employer Matching Contributions and Employee Contributions
1132	Excise Tax on Reversion of Qualified Plan Assets to Employer
1133	Tax on Excess Distributions from Qualified Retirement Plans
1139	Interest Rate Assumptions
1140	Plan Amendments Not Required (Model Amendment)
1146	Treatment of Leased Employees
1161	Deductibility of Health Insurance Costs of Self-Employed Persons
1201	Separate Application of Code Section 904 with Respect to Certain Categories of Income
1212	Reciprocal Exemptions for Certain Transportation Income
1214	Interest and Dividends of 80-20 Companies
1215	Worldwide Group Allocation of Interest and Other Expenses
1221	Foreign Captive Insurance Companies
1231	Possession Tax Credit
1234	Foreign Compliance Provisions (Passports, Pensions)
1235	Treatment of Certain Passive Foreign Investment Companies
1241	Branch Profits Tax
1245	Information with Respect to Certain Foreign-Owned Corporations
1246	Withholding Tax on Amounts Paid by Partnerships to Foreign Partners
1248	Customs Limitation on Taxpayer's Basis in Property Imported from Related Persons
1261	Treatment of Foreign Currency Transactions
1275	Virgin Islands Corporations Allowed Possession Tax Credit
1301	Qualified Mortgage Bonds; Arbitrage on Tax Exempt Bonds; Information Reporting for Tax Exempt Bonds
1411	Unearned Income of Minor Children
1431–33	Generation-Skipping Transfer Tax
1501	Information Reporting Penalty
1511	Differential Interest Rate
1521	Reporting on Real Estate Transactions
1522	Reporting on Federal Contractors
1524	TINS for Dependents Claimed on Returns
1541	Estimated Tax Payments by Individuals
1543	Waiver of Penalties for 1986 Estimated Tax Underpayments Attributable to Tax Reform Act of 1986
1561	Suspension of Statute of Limitations
1564	Suspension of Interest Compounding
1571	Withholding Allowances to Reflect New Rate Schedules
1702	Collection of Diesel Fuel Tax
1703	Collection of Gasoline Tax
1704	Exemption from Social Security Coverage for Certain Clergy
1706	Employment Tax Status of Certain Technical Personnel
1843	Technical Corrections Relating to Alimony Payments
1898	Technical Corrections to the Retirement Equity Act of 1984

PROJECTS FOR WHICH THE IRS IS SEEKING ADVICE

Code Sec.	*File No.*	*Subject*
55–59	LR–107–86	Alternative minimum tax
89	EE–130–86	Valuation of health care coverage
103, 148	LR–90–86	Arbitrage on tax-exempt bonds
163, 263A 469	LR–125–86	Coordination of interest deduction limits
263A	LR–129–86	Capitalization of property production costs (other than interest)

PROJECTS FOR WHICH THE IRS IS SEEKING ADVICE

Code Sec.	*File No.*	*Subject*
263A	LR–120–86	Capitalization of interest
336, 337	LR–117–86	Recognition of gain and loss on distributions in liquidation (repeal of *General Utilities*)
367, 482	IL–937–86	Transfers and licenses of intangibles to foreign subsidiaries
382	LR–103–86	Limits on net operating loss carryovers
414 (q)	EE–129–86	Definition of "highly compensated employees"
414 (r)	EE–128–86	Rules covering "lines of business"
441, 706(b) 1378 (a)	LR–100–86	Taxable years of certain entities
453, 453C	LR–93–86	Installment obligations
460	LR–130–86	Accounting for Long-term Contracts
469	LR–126–86	Limits on passive losses
864	IL–935–86	Allocation of interest expense to foreign source income
884	IL–934–86	Branch profits tax
902, 960	IL–933–86	Foreign tax credit—deemed paid credit
904	IL–931–86	Foreign tax credit—separate limitations for passive and other categories of income
904	IL–932–86	Effect of losses on foreign tax credit
985–989	IL–936–86	Foreign currency transactions
1060	LR–118–86	Special allocation rules for certain asset acquisitions
1446	IL–938–86	Withholding by partnerships on effectively connected income of foreign partners
2601–2663	LR–127–86	Generation-skipping transfer tax
6045	LR– 94–86	Reporting on real estate transactions

Foundations Status of Certain Organizations

Announcement 86–111

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to recieve deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

Adult Activity Community Center for the Developmentally Disabled, Westminster, CA
Agape, Inc., Los Angeles, CA
Agency for Self Supportive Communities, Oakland, CA
Alma Brotherw Corporation, The, San Diego, CA
American Friends of Sadnat Enosh, Los Angeles, CA
American Friends of the Royal Philharmonic Orchestra, London, England
American Society of Camera Collectors, L.A., North Hollywood, CA
Arpeggio, Los Angeles, CA
Artreach, Inc., Louisville, KY
Asian Village, Inc., The, Los Angeles, CA
Aural Rehabilitation Enhancement Association, Inc., Southgate, KY
Aurodarshan International, Ojai, CA
Baby John Martinez Transplant Organ Organization, San Diego, CA
Beginnings Therapy Center, Los Angeles, CA
Benicia Sea Otters, Inc., Benicia, CA
Big Bands 80's Record Library, Los Angeles, CA
Building and Construction Trades Senior Housing, Inc., Canton, OH
California Corinthian Foundation, Manhattan Beach, CA
California Institute of Politics and Government, San Francisco, CA
California Polka Dancing Association, Claremont, CA
California Youth Advocate Program, Inc., San Diego, CA
Capitol City Comets Track Club, Columbus, OH
Carter Homes, Inc., Toledo, OH
Center for Applied Anomalous Phenomena, Fairfax, VA
Center Street Community Center, Inc., Springfield, OH
Charles Crest Corporation, Toledo, OH
Chasbon Theatre Workshop, Los Angeles, CA
Child Abuse Council of Western Nevada County, Grass Valley, CA
Chinese American Christian Friendship Alliance, Orange, CA
Christian Federation of Korean Women in USA, Inc., Los Angeles, CA
Christian Hope Center, Inc., San Luis Obispo, CA
Christian Way, Inc., National City, CA
Christians Against Poverty, Santa Ana, CA
Concerned Agencies of Metropolitan Los Angeles, Inc., Los Angeles, CA
Consolation Community of the Third Order of St. Francis, Van Nuys, CA
Counseling and Educational Associates, A Non Profit Corp., San Francisco, CA
Creative Resources, Inc., Washington, DC

Croswell Senior Citizen Housing Corp., Croswell, MI
Cypress Commons of Humboldt Co., Arcata, CA
Dance Espanol, Inc., Los Angeles, CA
Davisburg Softball League, Davisburg, MI
Delta County Trades & Labor Food Bank, Inc., Escanaba, MI
Development Fund for Black Students in Science and Technology, Washington, DC
Discovery Society, The, Beverly Hills, CA
Divorce Help Line, Inc., Indianapolis, IN
Door of Faith Congregation Church, Inc., Los Angeles, CA
Education for a Better Tomorrow (EBT), Inc., Merrillville, IN
Educational Center for State Data, Reno, NV
Empyrean Foundation, Honolulu, HI
Engine Company 62 Firefighters Association, Inc., Columbus, OH
Ernesto Lucio Ministries, Inc., Fresno, CA
Estate of Harry D. Taylor, Encino, CA
Eternal Treasures Ministry, Walnut, CA
Evolution Incorporated, Hollywood, CA
Ex-Convict Fellowship Program, Cleveland, OH
Executive Service Corp. of Northern California, San Francisco, CA
Filipino-American Educators Assoc. of San Diego, Chula Vista, CA
Finnish Olympic Association, U.S.A., Sherman Oaks, CA
Flowering Tree Foundation, Costa Mesa, CA
Food and Water, Inc., Hillsdale, NJ
Forest Research Farms, Inc., Corvallis, OR
Foundation Bridging the Difference, Sherman Oaks, CA
Foundation for Health Awareness, Irvine, CA
Foundation for the Study and Prevention of Breast Disease, Santa Monica, CA
Friends of Child Find, California, Inc., San Diego, CA
Friends of Chinese Olympians, Los Angeles, CA
Garden Pavilion Nursing Home, Inc., Atherton, CA
Ghetto Tennis Foundation, San Diego, CA
GI Enterprises, Bellflower, CA
Golden Retirement Age Spiritual Protection, Los Gatos, CA
Good News Mission, Canoga Park, CA
Hacienda Heights Area Chinese Association, Hacienda Heights, CA
Halcyon Center for Child Studies, Inc., Thousand Oaks, CA
Handicapped Educational Resources Organization, Salinas, CA
Harbor Area High Gain Program, Inc., Long Beach, CA
Harper-Spector Baseball Camp, Inc., San Gabriel, CA
Hawaii Music Festival Foundation, Honolulu, HI
Hawaiian Eye Foundation, Wahiawa, HI
Hesperia Area Recreation District Foundation, Hesperia, CA
Hiway 120 Alano Club of Manteca, Lathrop, CA
Hollywood Christian Ministries, Inc., Hollywood, CA
Hope House Recovery Services, Inc., Oklahoma City, OK
Hope of Israel, The, Covina, CA
H.O.P.E.S. for Handicapped, Inc., San Diego, CA
Housing Opportunity Movement, Inc., Bethlehem, PA
Humanitarian Air Lift Organization, Van Nuys, CA
In Depth Studies, Inc., Redlands, CA
In God We Trust Movement c/o Total Contract Maintenance, Inc., Wilmington, CA
Inner Development, Glendora, CA
Institute for Corporate Counsel Loyola Law School, Los Angeles, CA
Inter-Disciplinary Institute of Applied Religion, Glendale, CA
International Science & Industry Expo '84, El Paso, TX
International Tradition Cultural Services, Los Angeles, CA
Iranian Community Service Center, San Diego, CA
Islamic American Medical Assn., Los Angeles, CA
Jerome Verde Valley Club, The, Covina, CA
Julmar Share-a-Home Association, Cincinnati, OH
Kahea, Inc., Honolulu, HI
Kanfei Yonah, Los Angeles, CA
Kaulana Na Pua Institute, Inc., Honolulu, HI
KEIO University Alumni Association of America, Los Angeles, CA
Kickaway Handicaps, Inc., Reno, NV
Kids In Development Society, Newport Beach, CA
Korean Acupressure Assoc. in U.S.A., Los Angeles, CA
Korean-American Coalition, Inc., Los Angeles, CA
Korean-American Support Committee for L.A. Olympics, Inc., The, Los Angeles, CA
Korean United Methodist Youth Center, Los Angeles, CA
Korean Women's Patriotic League, Los Angeles, CA
La Casita For Women, Inc., Fullerton, CA
La Mirada Senior Adult Theatrical Association, La Mirada, CA
Latino Alano Club, National City, CA
Learning Techniques, National City, CA
Library Society of the Hawaii State Library, Honolulu, HI
Life Foundation of Medicine & Law, Inc., Marina Del Rey, CA
Lifeline Adult Day Health Care Center, Inc., Montebello, CA
Light Singers, The, Alhambra, CA
Lillian Frances Cancer Research Foundation, Inc., Nutley, NJ
Lincoln Charitable Fund, Inc., The, Washington, DC
Los Angeles Ballet Foundation, Santa Monica, CA
Los Angeles Four Corners, Canoga Park, CA
Louis Pasteur Library and Science Foundation, Los Angeles, CA
M and M Ministries, Inc., Lincoln, CA
Manna International Relief and Development, Redwood City, CA
Maui Community Support Group, Inc., Kihei, HI
Mercer County Youth Soccer League, Inc., Bluefield, WV
Midwife Services Birth and Family Studies Institute, Encinitas, CA
Ministry of Love, San Marcos, TX
Nansen Field Foundation, Rancho Palos Verdes, CA
National Advisory Council for Computer Implementation in Schools, Inc., Tucson, AZ
National Alliance for the Enrichment of the Families, Monterey Park, CA
National Association for Broadcast Entertainment And Education, Los Angeles, CA
National Association for Senior Citizens, Santa Ana, CA
National Association of Credit Counselors, Los Angeles, CA
National Center for Initiative Review Foundation, Englewood, CO
National Equine Sports Medicine Institute, Inc., Los Angeles, CA
National Hispanic Media Institute, Los Angeles, CA

National Treasures Foundation, Laguna Beach, CA
National Women's Political Caucus of California Education Fund, Inc., Laguna Beach, CA
Naylor Senior Housing, Inc., Compton, CA
Neda San Diego, San Diego, CA
New Hope Behavior, Inc., Los Angeles, CA
North American Division of the Doctor who Appreciates Society, Van Nuys, CA
Northern California Childrens Museum, San Francisco, CA
Oasis Community Cultural Center, Pasadena, CA
Obrero, Inc., San Diego, CA
112 Housing, Inc., Philadelphia, PA
Open Quest Institute, West Hollywood, CA
Oscar Joel Bryant Association, Los Angeles, CA
Outreach Evangelistic Association, Inc., La Porte, IN
Pacific Concerns Resource Center Education Fund, Honolulu, HI
Perris Valley Child Care Consortium, Perris, CA
Playhouse, Inc., The, Loma Linda, CA
Portland Foundation, Inc., Louisville, KY
Puente Hill Family Young Mens Christian Association, Inc., Hacienda Heights, CA
R. C. Travelers, Alta Loma, CA
Rainbow Hale Drop-In Child Care Center, Pearl City, HI
Raphael Heights Homes, Inc., Philadelphia, PA
Reach Beyond, Kailua, HI
Recreation-Athletic Booster Club, Inc., Mishawaka, IN
Recreational Debut, Wyoming, MI
Revelation International Evangelical Mission. Los Angeles, CA
Richard D. Sork Oncology Foundation, Los Angeles, CA
Riverside Astronomical Society, Woodcrest, CA
Roever Evangelistic Association, Inc., Lakewood, CA
Rural Educational Assistance Center, McKinleyville, CA
SLM Productions, North Hollywood, CA
St. Stephen's Church of God in Christ Christian School Foundation, Inc., San Diego, CA
San Bernardino City Grand Opera Company, San Bernardino, CA
San Diego Sailing Foundation, San Diego, CA
San Francisco Chinese Cultural Service Center, San Francisco, CA
San Francisco League of Urban Gardeners, San Francisco, CA
San Gabriel Mission High School Alumni Association, San Gabriel, CA
Sand Productions, Las Vegas, NV
Santa Ana Neighborhood Organization, Santa Ana, CA
Sea-Bri Foundation, Boulder City, NV
Shin Woo Mission, Inc., Los Angeles, CA
Sign of the Times—The San Diego, La Jolla, CA
Siskiyou County Indian Association, Yreka, CA
Smith Group Home, Inc., Stockton, CA
Society For Indo-Pacific Culture, Santa Monica, CA
Soroptimist Gardens Housing Corp., Glendale, CA
Southern California Demolay Foundation, San Diego, CA
Southern California NAPFE Elderly Housing Development Corp., Culver City, CA
Southern California Striders Masters Track Club, Beverly Hills, CA
Sports Community Foundation, Beverly Hills, CA
Straight Path Ministries, Inc., Santa Ana, CA
Szilard Institute, LaJolla, CA
T. S. James Ministries, Dana Point, CA
Tehachapi Music Boosters, Tehachapi, CA
Temple Arts Foundation, San Francisco, CA
Tennis Opportunity, Inc., Rancho Mirage, CA
Theatre Organ Society of San Diego, Lakeside, CA
Timberline Lodge Community, Inc., Redondo Beach, CA
Town and Country Hospice, Garden Grove, CA
Traditional Small Craft, & Rowing Association, South Bristol, ME
Trenton Neighborhood Development Corp., Trenton, NJ
Utsonia, Inc., Honolulu, HI
Valley of Colors of Coachella, Indio, CA
Victor Valley Inter-Group Central Office, Inc., Victorville, CA
Visual Information Productions, Ltd., Malibu, CA
WYS Help, Inc., Redondo Beach, CA
Wayne Foster Foundation for Success of The Blind, The, San Diego, CA
West Coast Aquaculture Foundation, Pacific Grove, CA
Western Labor Organizing Project, Venice, CA
Western Society of Clinical Nephrology, Mountain View, CA
Westside Junior Ballet Company, Los Angeles, CA
Word Counselors, Los Angeles, CA
World Civil Diplomacy Society, Inc., Los Angeles, CA
World Prayer Mission, Inc., The, Los Angeles, CA
Worldwide Hope Institution, Los Angeles, CA
Worldwide Light House, Los Angeles, CA
Yarbrough's Home & Care, Compton, CA
Yonsei University Association of Southern California, Los Angeles, CA
Youth Camps of America, Rancho Palos Verdes, CA
Youth for Seniors, Los Angeles, CA
Yugolslav-American Olypic Committee of So. California, San Pedro, CA

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classificaiton as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Information Reporting of Mortgage Interest

Announcement 86–112

This announcement concerns the reporting of mortgage interest payments under section 6050H of the Internal Revenue Code. Section 6050H of the Code provides that any person who is engaged in a trade or business and who receives at least $600 of interest on a mortgage in a calendar year from an individual must report the amount of interest received to the Internal Revenue Service (Service) and to the individual from whom the interest was received. The reporting requirement is effective for interest received after December 31, 1984. This announcement discusses the application of the reporting requuirement to interest received for calendar year 1986.

On August 20, 1985, the Service published proposed and temporary regulations relating to mortgage interest reporting (50 FR 33551, 33529). A public hearing was held on January 7, 1986.

On January 21, 1986, the Service published Announcement 86–3, 1986–3 I.R.B. 42. Announcement 86–3 modifies certain provisions of the temporary regulations with respect to mortgage interest received in 1985 and clarifies the application of certain other provisions of the temporary regulations. Taxpayers are reminded that certain of the modifications to the temporary regulations made by Announcement 86–3 apply only for interest received in calendar year 1985.

Points and other prepaid interest

The temporary regulations provide that points and other prepaid interest are not to be reported as interest received (§1.6050H–1T Q/A–17(c)).

Announcement 86–3 provides that for calendar year 1985, if an interest recipient cannot exclude the portion of interest that represents points or other prepaid interest received in that year, the recipient may report the points or other prepaid interest as part of interest. Announcement 86–3 also provides that an interest recipient who reports as interest an amount that may include points or other prepaid interest must provide the borrower with the notice described in the announcement.

For calendar year 1986 and thereafter, interest recipients must report interest received in accordance with the mortgage interest reporting regulations. Thus, as provided in the temporary regulations, interest recipients must not include points and other prepaid interest in reporting all interest received from an individual in a calendar year.

Interest received by cooperative housing corporations

The temporary regulations provide that cooperative housing corporations must report, as interest received in a trade or business, the respective amounts of their tenant-stockholders' proportionate shares of interest (see §1.6050H–1T Q/A–10). Announcement 86–3 suspends this requirement for calendar year 1985.

For calendar year 1986 and thereafter, cooperative housing corporations must comply with the mortgage interest reporting regulations. Thus, as provided in the temporary regulations, cooperative housing corporations must report the amount of their tenant-stockholders' proportionate shares of interest.

Interest received on behalf of another

The temporary regulations provide that interest received by a person on behalf of another must be reported by the first person receiving the interest (§1.6050H–1T Q/A–11). Announcement 86–3 provides that for calendar year 1985, any person who receives payments on behalf of another and who does not know the portion of the payment that represents interest need not report.

For calendar year 1986 and thereafter, persons who receive interest on behalf of another must comply with the mortgage interest reporting regulations. Thus, as provided in the temporary regulations, any person who receives interest on behalf of another and is the first person to receive the interest must report under section 6050H of the Code.

Interest received from nonresident aliens

The temporary regulations do not provide an exception from the reporting requirement for interest received from nonresident alien individuals.

Announcement 86–3 provides that for calendar year 1985, interest recipients may, but are not required to, report interest received from nonresident alien individuals. Announcement 86–3 also discusses the evidence required to determine whether an individual is a nonresident alien. In addition, the announcement states that the Service is considering the treatment of nonresident aliens for future years and invites comments from taxpayers.

The treatment of nonresident aliens is still under consideration. Thus, Announcement 86–3 remains in effect with respect to interest received from nonresident alien individuals. Accordingly, for calendar year 1986, taxpayers may, but are not required to, report interest received from nonresident alien individuals.

Rule of 78s method of accounting

Announcement 86–3 provides that interest recipients who are permitted by Rev. Proc. 83–40 to use the Rule of 78s method to calculate interest earned with respect to a transaction may report interest earned under the Rule of 78s method on that transaction as interest received from the borrower in a calendar year. Announcement 86–3 also provides that interest recipients must notify borrowers that the Rule of 78s method was used to calculate interest received and that the borrowers may not deduct the amount reported unless the borrowers are also properly using the Rule of 78s method to determine interest deductions.

Announcement 86–3 is still in effect with respect to interest recipients who use the Rule of 78s method to report interest earned. Thus, interest recipients who are properly using the Rule of 78s method may report interest earned under the Rule of 78s as interest received from the borrower in a calendar year. These interest recipients must satisfy the notification requirement of Announcement 86–3.

Section 7428(c) Validation of Certain Contributions Made During Pendency of Declaratory Judgment Proceedings

This announcement serves notice to potential donors that the organization listed below has recently filed a timely declaratory judgment suit under section 7428 of the Code, challenging revocation of its status as an eligible donee under section 170(c)(2).

Protection under section 7428(c) of the Code begins on the date that the notice of revocation is published in the Internal Revenue Bulletin and ends on the date on which a court first determines that an organization is not described in section 170(c)(2), as more particularly set forth in section 7428(c)(1). In the case of individual contributors, the maximum amount of contributions protected during this period is limited to $1,000.00, with a husband and wife being treated as one contributor. This protection is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for the revocation. This protection also applies (but without limitation as to amount) to organizations described in section 170(c)(2) which are exempt from tax under section 501(a). If the organization ultimately prevails in its declaratory judgment suit, deductibility of contributions would be subject to the normal limitations set forth under section 170.

Copperweld Steel Company's Warren Employees Trust
Warren, OH (Protection period begins October 14, 1986)

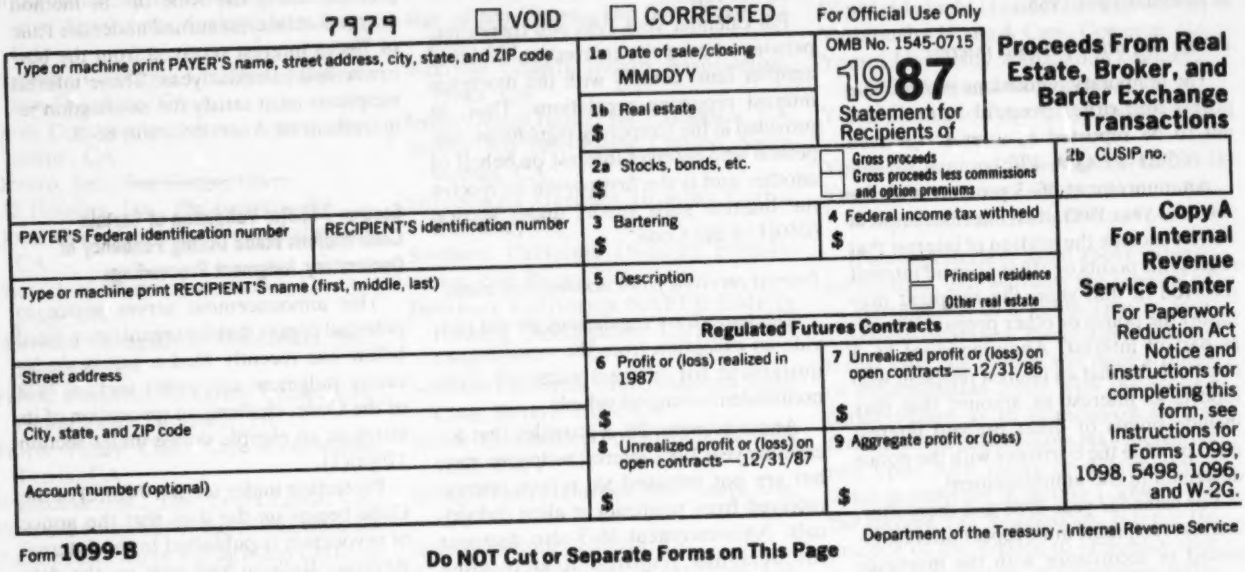
Revision of Form 1099–B, Statement for Recipients of Proceeds From Real Estate, Broker, and Barter Exchange Transactions

Announcement 86–115

Form 1099-B has been revised to provide for the reporting of real estate transactions closing after 1986, as required by the Tax Reform Act of 1986, which added section 6045(e) to the Internal Revenue Code.

New Box 1b "Real estate" has been added for reporting gross proceeds from a real estate transaction, and two checkboxes have been added to Box 5 to identify the nature of the property involved in the transaction. Other minor changes have also been made to the form.

A copy of the revised form, which will be available in Internal Revenue Service offices in early January, appears below.



7979 ☐ VOID ☐ CORRECTED For Official Use Only

Type or machine print PAYER'S name, street address, city, state, and ZIP code

1a Date of sale/closing MMDDYY

1b Real estate $

2a Stocks, bonds, etc. $

☐ Gross proceeds

☐ Gross proceeds less commissions and option premiums

2b CUSIP no.

OMB No. 1545-0715

1987

Statement for Recipients of

Proceeds From Real Estate, Broker, and Barter Exchange Transactions

PAYER'S Federal identification number

RECIPIENT'S identification number

3 Bartering $

4 Federal income tax withheld $

Copy A For Internal Revenue Service Center

Type or machine print RECIPIENT'S name (first, middle, last)

5 Description

☐ Principal residence

☐ Other real estate

Regulated Futures Contracts

Street address

6 Profit or (loss) realized in 1987 $

7 Unrealized profit or (loss) on open contracts—12/31/86 $

City, state, and ZIP code

8 Unrealized profit or (loss) on open contracts—12/31/87 $

9 Aggregate profit or (loss) $

Account number (optional)

For Paperwork Reduction Act Notice and instructions for completing this form, see Instructions for Forms 1099, 1098, 5498, 1096, and W-2G.

Form **1099-B**

Do NOT Cut or Separate Forms on This Page

Department of the Treasury - Internal Revenue Service

Correction of Rev. Proc. 86–41

Announcement 86–116

A printing error caused a portion of the text of Rev. Proc. 86–41, 1986–45 I.R.B. 7, to be omitted. This revenue procedure relates to information and representations to be included in a request for a ruling under section 355 of the Code. The text omitted should appear immediately after the last line of text in the third column on page 9.

The omitted text is as follows:

See section 1.355–2(e)(1) of the regulations.

(c) Interests in Controlled held by security holders of Distributing.

(1) Receiving stock.—Identify those security holders receiving Controlled stock, the total number of shares of each class of stock being received, and the principal amount of the securities of Distributing being exchanged. If no securities are being exchanged, so state. If the securities are held by more than 25 security holders, identify only those security holders owning in excess of 5 percent of the outstanding shares of any class of Controlled stock immediately after the distribution.

(2) Receiving securities.—Identify those security holders of Distributing receiving securities of Controlled, the principal amount being received by each holder, and the principal amount of the securities of Distributing being exchanged. See section 1.355–2(e)(1) of the regulations.

(d) Receipt of consideration other than with respect to stock.

(1) Shareholder in dual capacity.—Submit the following REPRESENTATION: *No part of the consideration distributed by the distributing corporation is being received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.*

(2) Other transfers.—State whether the shareholders of Distributing transfer or surrender any property in the transaction other than stock or securities of Distributing. If so, provide full details.

.03 *Information concerning the businesses of Distributing and Controlled.*

1. Distributing's businesses.

(a) Description of businesses remaining in Distributing.—Submit a complete description of each business conducted directly by Distributing for each of the past 5 years that will be retained by Distributing. Provide all information necessary to establish that each business described constitutes an active trade or business (Active Business) within the meaning of Rev. Rul. 75–160, 1975–1 C.B. 112. In general, the description should conclusively show that substantial managerial and operational activities have been directly carried on by each business of the corporation during each of the past 5 years. See Rev. Rul. 86–126, 1986–43 I.R.B. 5; Rev. Rul. 86–125, 1986–43 I.R.B. 4; Rev. Rul. 80–181, 1980–2 C.B. 121, amplifying Rev. Rul. 79–394, 1979–2 C.B. 141; Rev. Rul. 73–237, 1973–1 C.B. 184; Rev. Rul. 73–236, 1973–1 C.B. 183; and Rev. Rul. 73–234, 1973–1 C.B. 180.

(b) Description of businesses being transferred by Distributing to Controlled.—If, as part of the plan, Distributing transfers all the assets of one or more of its Active Businesses of part of the assets of a single Active Business (Rev. Rul. 64–147, 1964–1 (Part 1) C.B. 136) to either a newly formed or preexisting Controlled, identify and submit a complete description of each Active Business or part being transferred. See section 4.031(a) for the information to be submitted as to each Active Business transferred.

2. Controlled's businesses.—If Controlled is a preexisting corporation submit a complete description of each Active Business conducted directly by Controlled during each of the past 5 years. See section 4.031(a) for the information to be submitted as to each Active Business.

3. Employee information.—Submit separate lists for each Active Business listed in section 4.031 and 032, above, showing the job title and number of each category of managerial and operational employees employed in each Active Business for each of the past 5 years. Include a brief description of the type of duties performed by each category of employee during each of these years. Additionally, state whether either Distributing or Controlled utilizes independent contractors. If so, include a brief description of duties they perform, and the percent of the corporation's activities performed by independent contractors. State whether managerial or operational activities of an Active Business are conducted by employees of an affiliated corporation. If so, describe which activities are so conducted. See Rev. Rul. 79–394, amplified by Rev. Rul. 80–181.

4. Indirect conduct of trade or business through ownership of stock in other corporations.—If either Distributing or Controlled is not directly engaged in an Active Business and it is contended that either Distributing or Controlled will be so engaged indirectly through ownership of stock and securities in one or more corporations controlled by it or by a controlled subsidiary immediately after the distribution (Other Corporations) (see Rev. Rul. 74–382, 1974–2 C.B. 120), provide the information and representations requested in sections 4.031, 4.033, 4.035, and 4.036 (treating each Other Corporation as Distributing or Controlled, as appropriate, for this purpose) (see section 355(b)(2)(A).

The omitted text will appear in Rev. Proc. 86–41 when it is reprinted in 1986–2 C.B.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practible for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
S. Melvin Apotheker	Miami, FL	Attorney	Indefinite from September 1, 1986
Sandra S. Behn	London, TN	Certified Public Accountant	Indefinite from September 12, 1986
Charles K. Hyter	Hutchinson, KS	Attorney	Indefinite from September 18, 1986
William Pyke	Dallas, TX	Certified Public Accountant	Eighteen Months from August 15, 1986
Alan Z. Richards	West Hempstead, NY	Attorney and Certified Public Accountant	Indefinite from September 20, 1986

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to identify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
Michael Winston	Fort Lauderdale, FL	Six Months from October 20, 1986

Under 31 Code of Federal Regulations, Part 10, an enrolled agent, in order to avoid the institution of a proceeding for his disbarment of suspension from practice before the Internal Revenue Service, may offer his resignation. The Director of Practice, in his discretion, may accept the offered resignation of an enrolled agent.

To enable the public and other practitioners to identify such resigned enrolled agents, the Director of Practice will announce in the Internal Revenue Bulletin the name and address of each enrolled agent who has resigned and the effective date of resignation. This announcement will appear in the weekly Bulletin at the earliest practicable date after the action and will continue to appear in the weekly Bulletins for five successive weeks or for as many weeks as is practicable for each resigned enrolled agent, and will later be consolidated and published in the Cumulative Bulletin.

The following individual has entered a consent resignation from enrollment to practice before the Internal Revenue Service:

Name of Enrolled Agent	Address	Effective Date of Resignation
William E. Bonafede	Wakefield, RI	September 30, 1986

Under Section 330, Title 31 of the United States Code, the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
James L. Ketner	Charlotte, NC	Certified Public Accountant	September 27, 1986
George L. Weil	Orange, CT	Certified Public Accountant	September 27, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR— Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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______	1928-2	10.00
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______	*1929-2*	*3.50*
______	1930-1	8.50
______	1930-2	10.00
______	*1931-1*	*4.00*
______	1931-2	14.00
______	*1932-1*	*3.25*
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______	*1943-(*)*	*11.00*
______	*1944-(*)*	*9.00*
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______	1946-2	6.00
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______	1948-2	8.50
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______	1958-1	11.00
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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–134, page 4.

Taxes of foreign countries and possessions of the United States. For purposes of the foreign tax credit under section 901 of the Code, Netherlands WIR premiums allowable with respect to commitments to invest in qualified assets entered into after April 30, 1986, must be treated as reducing Netherlands income taxes paid or accrued for the taxable year or years in which the premiums are allowed.

Announcement 86–113, page 46.

The Service will soon issue temporary regulations that will limit the ability of certain taxpayers to change their annual accounting period and suspend the provisions of Rev. Proc. 72–51.

EXCISE TAXES

Rev. Rul. 86–137, page 5.

Collection of $3.00 tax on use of international travel facilities; payment made outside the U.S. to foreign charterer. When a payment for air transportation that is subject to the $3.00 tax is made outside the U.S. to a foreign charterer, the airline that furnishes the transportation triggering the $3.00 tax is required to collect, report and pay the tax. Rev. Rul. 75–296 distinguished.

TAX CONVENTIONS

Australia, page 7.

The convention between the United States and Australia with respect to taxes on income is reproduced.

ADMINISTRATIVE

Announcement 86–114, page 46.

Additional guidance is provided to taxpayers who may wish to pay actual or contested tax deficiencies in 1986 in order to assure that interest paid on such deficiencies will be fully deductible on their 1986 returns.

Finding Lists begin on page 51.
Announcement of Disbarments and Suspensions begin on page 48.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 901.—Taxes of foreign countries and possessions of the United States.

26 CFR 1.901–2: Income, war profits, or excess profits tax paid or accrued.

Taxes of foreign countries and possessions of the United States. For purposes of the foreign tax credit under section 901 of the Code, Netherlands WIR premiums allowable with respect to commitments to invest in qualified assets entered into after April 30, 1986, must be treated as reducing Netherlands income taxes paid or accrued for the taxable year or years in which the premiums are allowed.

Rev. Rul. 86–134

ISSUE

Whether investment incentives ("WIR premiums") granted by the Kingdom of the Netherlands should be treated as reducing Netherlands income taxes paid or accrued for purposes of the U.S. foreign tax credit in the situation described below.

FACTS

X is an accrual method, calendar year domestic corporation actively engaged in a trade or business through a permanent establishment within the Netherlands. Income derived by X's permanent establishment is subject to the Netherlands Corporation Income Tax Act of 1969, as amended. X's 1986 Netherlands income tax liability computed without regard to credits is Dfl. 50,000.

After May 1, 1986, X purchased and placed in service certain fixed assets for use in the Netherlands permanent establishment. The total cost of these assets was Dfl. 100,000.

The assets qualify for a Netherlands investment incentive under the 1978 Investment Account Act, as amended (*Wet Investeringsrekening*, abbreviated WIR) in the amount of Dfl. 12,500. WIR allows tax-free premiums to encourage investment in qualifying business use assets located in the Netherlands. Currently the basic WIR premium is equal to 12.5 percent of the cost of a qualifying asset. The basic WIR premium may be increased by one or more supplemental premiums. The premiums are allowed to Netherlands residents subject to the Netherlands corporation or individual income tax and also to non-residents of the Netherlands who operate there through a permanent establishment.

The amount of the WIR premium is not included in Netherlands taxable income and the premium does not reduce the Netherlands depreciable basis of a qualified asset for which a premium is allowed. In general, the WIR premium is allowable in the taxable year in which a commitment (contract) to invest in a qualifying asset is entered into, but the amount of the premium is limited in that year to the portion of the premium allowable with respect to the amount actually expended in the year to acquire the asset, and the rest of the premium is allowable in the earlier of the taxable year the asset is placed in service or the year the balance of the purchase price is paid.

If an asset for which a WIR premium has been allowed is disposed of within 8 years, the premium is recaptured in the same proportion as the amount received for the asset bears to the original cost. Recaptured premiums are not deductible from Netherlands taxable income and do not affect the calculation of gain or loss on the disposition of the asset for Netherlands income tax purposes.

In general, with respect to commitments to invest in qualified assets entered into after April 30, 1986, payment of the allowable WIR premiums by the Netherlands government to the investor (and repayment of recaptured premiums to the government by the investor on the disposition of a qualified asset) is effected only through the Netherlands income tax assessment system. The investor, whether a resident or a non-resident of the Netherlands, claims a credit or offset against the Netherlands corporate or individual income tax assessment for the amount of WIR premiums due, and shows an addition to tax for recaptured premiums. If the net amount of premiums due the investor exceeds the tax assessment (or if there is no tax liability), the excess of current WIR premiums over the current year's Netherlands income tax assessment may be carried back 3 taxable years and then carried forward 8 taxable years (or carried forward 12 years in the case of start-up companies) until used against the investor's Netherlands income tax liability. These are the same periods over which Netherlands net operating losses may be carried.

LAW AND ANALYSIS

Section 901 of the Code allows a credit, subject to the limitations of section 904, for the amount of income, war profits and excess taxes paid or accrued, or deemed paid under sections 902 or 960, to any foreign country or possession of the United States. When analyzing a foreign levy to determine if it is a creditable tax, principles developed under U.S. law, not foreign law control. *Biddle v. Commissioner*, 302 U.S. 573 (1938); section 1.901–2(a)(2) of the Income Tax Regulations. Thus, U.S. principles also control in determining whether an amount of foreign income tax has been reduced by means of a refund or credit. The controlling U.S. principles regarding the treatment of an amount of foreign income tax subject to reduction by refund or credit for purposes of the U.S. foreign tax credit are contained in section 1.901–2(e)(2) of the Income Tax Regulations.

Section 1.901–2(e)(2)(i) of the Income Tax Regulations provides that an amount is not tax paid or accrued to a foreign country to the extent that it is reasonably certain that the amount will be refunded, credited, rebated, abated or forgiven. This rule is illustrated by Example (2) of section 1.901–2(e)(2)(ii), where an initial foreign income tax liability of 100u is reduced under foreign law by an investment credit of 15u and a charitable contributions credit of 5u. Example (2) holds that the amount of foreign income tax paid or accrued is 80u. Thus, the investment credit must be treated as reducing the amount of foreign income tax paid or accrued.

Because the only manner in which a taxpayer can receive WIR premiums is as a credit or offset against Netherlands income tax assessments, section 1.901–2(e)(2)(i) and the holding of Example (2) directly apply to the treatment of WIR premiums allowable with respect to commitments to invest in qualified assets entered into after April 30, 1986, under the 1978 Investment Account Act, as amended. Accordingly, the Dfl. 12,500 amount is not income tax paid or accrued to the Netherlands because it is reasonably certain that a WIR premium equal to that amount will be allowed as a credit against X's pre-credit Netherlands income tax liability within the meaning of section 1.901–2(e)(2)(i). X's 1986 pre-credit Netherlands income tax liability of

Dfl. 50,000 must be reduced by Dfl. 12,500, the amount of the allowable WIR premium. The taxable year (or taxable years, if a carryback or carryover applies) in which the WIR premium is allowed as an offset against Netherlands income tax is the proper taxable year for which Netherlands income taxes are considered reduced. If a WIR premium that has been allowed with respect to commitments to invest in qualified assets entered into after April 30, 1986, is recaptured in a later taxable year, the amount of the recaptured premium shall be treated as an increase in Netherlands income tax for the taxable year in which the liability for the recaptured premium is paid or accrued.

HOLDING

Under the circumstances described above, for purposes of the U.S. foreign tax credit, WIR premiums allowable with respect to commitments to invest in qualified assets entered into after April 30, 1986, must be treated as reducing Netherlands income taxes paid or accrued for the taxable year or years in which the premium is allowed. WIR premiums described in the previous sentence that are recaptured in a later taxable year must be treated as an increase in Netherlands income taxes paid or accrued for the taxable year in which the liability for the recaptured premium is paid or accrued.

The holding of this revenue ruling does not apply to either the allowance or the recapture of a WIR premium allowable with respect to commitments to invest in qualified assets entered into before May 1, 1986.

Section 4261.—Imposition of Tax

(Also Sections 4263, 4291, 7805; 42.4291-1, 301.7805-1.)

Collection of $3.00 tax on use of international travel facilities; payment made outside the U.S. to foreign charterer. When a payment for air transportation that is subject to the $3.00 tax is made outside the U.S. to a foreign charterer, the airline that furnishes the transportation triggering the $3.00 tax is required to collect, report and pay the tax. Rev. Rul. 75–296 distinguished.

Rev. Rul. 86–137

ISSUE

If an independent travel agent operating abroad sells tour tickets that provide for round trip charter transportation furnished by an airline to and from a point in the United States and if payment for the tour is made outside the United States, who is responsible for collecting and paying to the U.S. Government the $3.00 tax imposed by section 4261(c) of the Internal Revenue Code on the use of international travel facilities?

FACTS

An independent travel agency located in a foreign country sells tours that include round-trip air transportation to the United States. For such flights, the travel agency charters aircraft from an airline. The airline receives a flat amount for the charter and furnishes the pilot and crew. The travel agency does not have an office or representative in the United States.

LAW AND ANALYSIS

Section 4261(c) of the Code imposes a tax of $3.00 upon any amount paid (whether within or without the United States) for any transportation of any person by air, if such transportation begins in the United States. The subsection is inapplicable to any transportation all of which is subject to the 8 percent tax on transportation of persons by air imposed by section 4261(a).

Section 4263(e) of the Code provides that for purposes of applying the tax on transportation of persons by air to a round trip, such round trip shall be considered to consist of transportation from the point of departure to the destination and of separate transportation thereafter.

Section 4291 of the Code provides that, except as otherwise provided in section 4263(a), every person receiving any payment for facilities and services on which a tax is imposed on the payor under Chapter 33 shall collect the amount of the tax from the person making such payment.

Section 4263(a) of the Code provides that if the payment upon which tax is imposed by section 4261 is made outside the United States for a prepaid order, exchange order, or similar order, the person furnishing the initial transportation pursuant to such order shall collect the amount of tax.

Section 49.4261-7(h)(2) of the Facilities and Services Excise Tax Regulations provides that the charterer of a conveyance who sells transportation must collect and account for section 4261 taxes with respect to amounts paid to it for transportation. This regulation is a reflection of the general rules of sections 4261 and 4291, and, like these general rules, it is subject to the exception set forth in section 4263(a).

Rev. Rul. 72–538, 1972–2 C.B. 577, holds that where the return part of a round trip from a foreign country begins in the United States, the $3.00 departure tax applies to the return trip.

Rev. Rul. 75–296, 1975–2 C.B. 440, considered an independent travel agency chartered by the Interstate Commerce Commission that sold tours and chartered aircraft from various carriers. The ruling held that the agency was acting as a principal and was required to collect the air transportation tax imposed by section 4261 of the Code, file returns, and pay the tax to the U.S. Government. The provision applicable to collection of tax in that ruling was section 4291, under which the person receiving payment for the transportation must collect the tax. The ruling concluded that the independent travel agencies received the payment.

In the present situation, the portion of the amount paid by the traveler to the foreign travel agency that represents payment for the return air transportation from the United States to the foreign country is subject to the $3.00 tax. Because the taxable transportation was paid for outside of the United States, the person furnishing the initial taxable transportation is required under section 4263(a) of the Code to collect the amount of the tax and pay it to the U.S. Government. Under Rev. Rul. 60–311, 1960–2 C.B. 341, the person who has possession, command and control of the aircraft is the person furnishing the taxable transportation. In this case, that person is the foreign airline and, unlike Rev. Rul. 75–296, section 4263(a) applies and not section 4291.

HOLDING

When a payment for air transportation that is subject to the $3.00 departure tax is made outside the United States to a foreign charterer, the airline that furnishes the taxable transportation is required to collect, report and pay to the U.S. Government the $3.00 tax for each traveler. The charterer may remit the amount of the tax to the airline on behalf of the travelers; if it does not, the airline must collect the tax directly from the travelers.

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 75–296 is distinguished

PROSPECTIVE APPLICATION

Under the authority contained in section 7805(b) of the Code, the conclusion in this revenue ruling will not be applied to payments for air transportation made before January 1, 1987.

Section 4263.—Special Rules

Who is responsible for collection and payment of the tax on the use of international travel facilities imposed by section 4261(c) of the Code when a foreign independent travel agent sells tickets abroad for a tour that includes round trip charter transportation furnished by an airline to and from a point in the United States? See Rev. Rul. 86–137, page 5.

Section 4291.—Cases Where Persons Receiving Payments Must Collect Tax

26 CFR 42.4291–1: Duty to collect tax.

Who is responsible for collection and payment of the tax on the use of international travel facilities imposed by section 4261(c) of the Code when a foreign independent travel agent sells tickets abroad for a tour that includes round trip charter transportation furnished by an airline to and from a point in the United States? See Rev. Rul. 86–137, page 5.

Section 7805.—Rules and Regulations

26 CFR 301.7805–1: Rules and regulations

Who is responsible for collection and payment of the tax on the use of international travel facilities imposed by section 4261(c) of the Code when a foreign independent travel agent sells tickets abroad for a tour that includes round trip charter transportation furnished by an airline to and from a point in the United States? See Rev. Rul. 86–137, page 5.

Part II. Treaties and Tax Legislation

Subpart A.—Tax Conventions

United States—Australia Income Tax Convention[1]

Convention signed at Sidney on August 6, 1982;

Ratification advised by the Senate of the United States of America on July 27, 1983;

Instruments of ratification exchanged on October 31, 1983.

CONVENTION BETWEEN THE GOVERNMENT OF THE UNITED STATES OF AMERICA AND THE GOVERNMENT OF AUSTRALIA FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME

The Government of the United States of America and the Government of Australia.

Desiring to conclude a Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income,

Have agreed as follows:

ARTICLE 1
PERSONAL SCOPE

(1) Except as otherwise provided in this Convention, this Convention shall apply to persons who are residents of one or both of the Contracting States.

(2) This Convention shall not restrict in any manner any exclusion, exemption, deduction, rebate, credit or other allowance accorded from time to time:

(a) by the laws of either Contracting State; or

(b) by any other agreement between the Contracting States.

(3) Notwithstanding any provision of this Convention, except paragraph (4) of this Article, a Contracting State may tax its residents (as determined under Article 4 (Residence)) and individuals electing under its domestic law to be taxed as residents of that state, and by reason of citizenship may tax its citizens, as if this Convention had not entered into force. For this purpose, the term "citizen" shall, with respect to United States source income according to United States law relating to United States tax, include a former citizen whose loss of citizenship had as one of its principal purposes the avoidance of tax, but only for a period of 10 years following such loss.

(4) The provisions of paragraph (3) shall not affect:

(a) the benefits conferred by a Contracting State under paragraph (2) of Article 9 (Associated Enterprises), paragraph (2) or (6) of Article 18 (Pensions, Annuities, Alimony and Child Support), Article 22 (Relief from Double Taxation), 23 (Non-Discrimination), 24 (Mutual Agreement Procedure) or paragraph (1) of Article 27 (Miscellaneous); or

(b) the benefits conferred by a Contracting State under Article 19 (Governmental Remuneration), 20 (Students) or 26 (Diplomatic and Consular Privileges) upon individuals who are neither citizens of, nor have immigrant status in, that State (in the case of benefits conferred by the United States), or who are not ordinarily resident in that State (in the case of benefits conferred by Australia).

ARTICLE 2
TAXES COVERED

(1) The existing taxes to which this Convention shall apply are:

(a) in the United States: the Federal income taxes imposed by the Internal Revenue Code, but excluding the accumulated earnings tax and the personal holding company tax; and

(b) in Australia; the Australian income tax, including the additional tax upon the undistributed amount of the distributable income of a private company.

(2) This Convention shall also apply to any identical or substantially similar taxes which are imposed by either Contracting State after the date of signature of this Convention in addition to, or in place of, the existing taxes. At the end of each calendar year, the competent authority of each Contracting State shall notify the competent authority of the other Contracting State of any substantial changes which have been made during that year in the laws of his State relating to the taxes to which this Convention applies or in the official interpretation of those laws or of this Convention.

ARTICLE 3
GENERAL DEFINITIONS

(1) For the purposes of this Convention, unless the context otherwise requires:

(a) the term "person" includes an individual, an estate of a deceased individual, a trust, a partnership, a company and any other body of persons;

(b) the term "company" means any body corporate or any entity which is treated as a company or body corporate for tax purposes;

(c) the terms "enterprise of one of the Contracting States" and "enterprise of the other Contracting State" mean an enterprise carried on by a resident of Australia or an enterprise carried on by a resident of the United States, as the context requires;

(d) the term "international traffic" means any transport by a ship or aircraft, except where such transport is solely between places within a Contracting State;

(e) the term "competent authority" means:

(i) in the case of the United States: the Secretary of the Treasury or his delegate; and

(ii) in the case of Australia: the Commissioner of Taxation or his authorized representative;

(f) the terms "Contracting State", "one of the Contracting States" and "the other Contracting State" mean the United States or Australia, as the context requires;

(g)(i) the term "United States corporation" means a corporation which, under United States law relating to United States tax, is a domestic corporation or an unincorporated entity treated as a domestic corporation, and which is not, under the law of Australia relating to Australian tax, a resident of Australia; and

(ii) the term "Australian corporation" means a company, as defined under the law of Australia relating to Australian tax, which, under that law, is a resident of Australia, and which is not, under United States law relating to United States tax, a domestic corporation or an unincorporated entity treated as a domestic corporation;

(h) the term "State" means any National State, whether or not one of the Contracting States;

(i) the term "United States tax" means tax imposed by the United States to which this Convention applies by virtue of Article 2 (Taxes Covered) and the term "Australian tax" means tax imposed by Australia to which this Convention applies by virtue of Article 2 (Taxes Covered), but neither term includes any amount which represents a penalty or interest imposed under the law of either Contracting State relating to United States tax or Australian tax;

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[1] Pertinent excerpts from Senate Report No. 98-16, page 16; Treasury Department Technical Explanation, page 33.

(j)(i) the term "United States" means the United States of America; and

(ii) when used in a geographical sense, the term "United States" means the states thereof and the District of Columbia and also includes:

(A) the territorial waters thereof; and

(B) the sea-bed and subsoil of the submarine areas adjacent to the coast thereof, but beyond the territorial waters, over which the United States exercises rights, in accordance with international law, for the purposes of exploration for, or exploitation of, the natural resources of those areas;

(k) the term "Australia" means the Commonwealth of Australia and, when used in a geographical sense, includes:

(i) the Territory of Norfolk Island;

(ii) the Territory of Christmas Island;

(iii) the Territory of Cocos (Keeling) Islands;

(iv) the Territory of Ashmore and Cartier Islands;

(v) the Coral Sea Islands Territory; and

(vi) any area adjacent to the territorial limits of Australia or of the said Territories in respect of which there is for the time being in force, consistently with international law, a law of Australia or of a State or part of Australia or of a Territory aforesaid dealing with the exploitation of any of the natural resources of the sea-bed and subsoil of the continental shelf;

(l) the term "resident of one of the Contracting States" and "resident of the other Contracting State" mean a resident of Australia or a resident of the United States, as the context requires.

(2) As regards the application of this Convention by one of the Contracting States, any term not defined herein shall, unless the context otherwise requires, have the meaning which it has under the laws of that State relating to the taxes to which this Convention applies.

ARTICLE 4
RESIDENCE

(1) For the purposes of this Convention:

(a) a person is a resident of Australia if the person is:

(i) an Australian corporation; or

(ii) any other person (except a company as defined under the law of Australia relating to Australian tax) who, under that law, is a resident of Australia,

provided that, in relation to any income, a person who:

(iii) is subject to Australian tax on income which is from sources in Australia; or

(iv) is a partnership, an estate of a deceased individual or a trust (other than a trust that is a provident, benefit, superannuation or retirement fund, or that is established for public charitable purposes or for the purpose of enabling scientific research to be conducted by or in conjunction with a public university or public hospital, the income of which is exempt from tax under the law of Australia relating to Australian tax),

shall not be treated as a resident of Australia except to the extent that the income is subject to Australian tax as the income of a resident, either in the hands of that person or in the hands of a partner or beneficiary, or, if that income is exempt from Australian tax, is so exempt solely because it is subject to United States tax; and

(b) a person is a resident of the United States if the person is:

(i) a United States corporation; or

(ii) any other person (except a corporation or unincorporated entity treated as a corporation for United States tax purposes) resident in the United States for purposes of its tax, provided that, in relation to any income derived by a partnership, an estate of a deceased individual or a trust, such person shall not be treated as a resident of the United States except to the extent that the income is subject to United States tax as the income of a resident, either in its hands or in the hands of a partner or beneficiary, or, if that income is exempt from United States tax, is exempt other than because such person, partner or beneficiary is not a United States person according to United States law relating to United States tax.

(2) Where by application of paragraph (1) an individual is a resident of both Contracting States, he shall be deemed to be a resident of the State:

(a) in which he maintain his permanent home;

(b) if the provisions of sub-paragraph (a) do not apply, in which he has an habitual abode if he has his permanent home in both Contracting States or in neither of the Contracting States; or

(c) if the provisions of sub-paragraphs (a) and (b) do not apply, with which his personal and economic relations are closer if he has an habitual abode in both Contracting States or in neither of the Contracting States.

(3) For the purposes of this paragraph, in determining an individual's permanent home, regard shall be given to the place where the individual dwells with his family, and in determining the Contracting State with which an individual's personal and economic relations are closer, regard shall be given to his citizenship (if he is a citizen of one of the Contracting States).

An individual who is deemed to be a resident of one of the Contracting States for any year of income, or taxable year, as the case may be by reason of the provisions of paragraph (2) shall, for all purposes of this Convention, be deemed to be a resident only of that State for such year.

ARTICLE 5
PERMANENT ESTABLISHMENT

(1) For the purpose of this Convention, the term "permanent establishment" means a fixed place of business through the business of an enterprise is wholly or partly carried on.

(2) The term "permanent establishment" shall include especially:

(a) a place of managment;

(b) a branch;

(c) an office;

(d) a factory;

(e) a workshop;

(f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources;

(g) an agricultural, pastoral or forestry property;

(h) a building site or construction, assembly or installation project which exists for more than 9 months; and

(i) an installation, drilling rig or ship that, for an aggregate period of at least 6 months in any 24 month period, is used by an enterprise of one of the Contracting States in the other Contracting State for dredging or for or in connection with the exploration or exploitation of natural resources of the sea-bed and subsoil.

(3) Notwithstanding paragraphs (1) and (2), an enterprise of one of the Contracting States shall not be regarded as having a permanent establishment solely as a result of one or more of the following:

(a) the use of facilities for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;

(b) the maintenance of a stock of goods or merchandise belonging to the enterprise for the purpose of storage, display or delivery;

(c) the maintenance of a stock of goods or merchandise belonging to the enterprise for the purpose of processing by another enterprise;

(d) the maintenance of a fixed place of business for the purpose of purchasing goods or merchandise, or for collecting information, for the enterprise;

(e) the maintenance of a fixed place of business for the purpose of activities which have a preparatory or auxiliary character, such as advertising or scientific research, for the enterprise;

(f) the maintenance of a building site or construction, assembly or installation project which does not exist for more than 9 months; or

(g) the use by that enterprise in the other Contracting State, of an installation, drilling rig or ship for dredging, or for or in connection with the exploration or exploitation of natural resources of the sea-bed and subsoil, provided that such use is not for an aggregate period of at least 6 months in any 24 month period.

(4) Notwithstanding paragraphs (1) and (2), an enterprise of one of the Contracting States shall be deemed to have a permanent establishment in the other Contracting State if:

(a) it carriers on business in that other State through a person, other than an agent of independent status to whom paragraph (5) applies, who has authority to conclude contracts on behalf of that enterprise and habitually exercises that authority in that other State, unless the activities of such person are limited to those mentioned in paragraph (3) which, if exercised through a fixed place of business, would not make that fixed place of business a permanent establishment under the provisions of that paragraph;

(b) it maintains substantial equipment for rental or other purposes within that other State (excluding equipment let under a hire-purchase agreement) for a period of more than 12 months;

(c) it engages in supervisory activities in that other State for more than 9 months in any 24 month period in connection with a building site or construction, assembly or installation project in that other State; or

(d) it has goods or merchandise belonging to it that:

(i) were purchased by it in that other State, and not subjected to prior substantial processing outside that other State; or

(ii) were produced by it or on its behalf in that other State, and are, after such purchase or production, subjected to substantial processing in that other State by an enterprise where either enterprise participates directly or indirectly in the management, control or capital of the other enterprise, or where the same persons participate directly or indirectly in the management, control or capital of both enterprises.

(5) An enterprise of one of the Contracting States shall not be deemed to have a permanent establishment in the other Contracting State merely because that enterprise carries on business in that other State through a broker, general commission agent, or any other agent of independent status, where such broker or agent is acting in the ordinary course of his business as a broker, general commission agent or other agent of independent status.

(6) The fact that a company which is a resident of one of the Contracting States controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other.

(7) The principles set forth in the preceding paragraphs of this Article shall be applied in determining for purposes of this Convention whether there is a permanent establishment in a State other than one of the Contracting States and whether an enterprise other than an enterprise of one of the Contracting States has a permanent establishment in one of the Contracting States.

ARTICLE 6
INCOME FROM REAL PROPERTY

(1) Income from real property may be taxed by the Contracting State in which such real property is situated.

(2) For the purposes of this Convention:

(i) a leasehold interest in land, whether or not improved, shall be regared as real property situated where the land to which the interest relates is situated; and

(ii) rights to exploit or to explore for natural resources shall be regarded as real property situated where the natural resources are situated or sought.

ARTICLE 7
BUSINESS PROFITS

(1) The business profits of an enterprise of one of the Contracting States shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the business profits of the enterprise may be taxed in the other State but only so much of them as it attributable to that permanent establishment.

(2) Subject to the provisions of paragraph (3), where an enterprise of one of the Contracting States carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the business profits which it might be expected to make if it were a distinct and independent enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment or with other enterprises with which it deals.

(3) In the determination of the business profits of a permanent establishment, there shall be allowed as deductions expenses which are reasonably connected with the profits (including executive and general administrative expenses) and which would be deductible if the permanent establishment were an independent entity which paid those expenses, whether incurred in the Contracting State in which the permanent establishment is situated or elsewhere.

(4) No business profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise.

(5) For the purposes of the preceeding paragraphs of this Article, the business profits to be attributed to the permanent establishment shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.

(6) Where business profits include items of income which are dealt with separately in other Articles of this Convention, then the provisions of those Articles shall not be affected by the provisions of this Article.

(7) Nothing in this Article shall affect the application of any law of a Contract-

ing State relating to the determination of the tax liability of a person in cases where the information available to the competent authority of that State is inadequate to determine the profits to be attributed to a permanent establishment, provided that, on the basis of the available information, the determination of the profits of the permanent establishment is consistent with the principles stated in this Article.

(8) Nothing in this Article shall in a Contracting State prevent the operation in that State of its law relating specifically to the taxation of any person who carries on the business of any form of insurance (as long as that law as in effect on the date of signature of this Convention is not varied otherwise than in minor respects so as not to affect its general character).

ARTICLE 8
SHIPPING AND AIR TRANSPORT

(1) Profits derived by a resident of one of the Contracting States from the operation in international traffic of ships or aircraft shall be taxable only in that State. For the purposes of this Article, profits from the operation in international traffic of ships or aircraft include:

(a) profits from the lease on a full basis of ships or aircraft operated in international traffic by the lessee, provided that the lessor either operates ships or aircraft otherwise than solely between places in the other Contracting State or regularly leases ships or aircraft on a full basis; and

(b) profits from the lease of ships or aircraft on a bare boat basis or of containers and related equipment, provided that such lease is merely incidental to the operation in international traffic of ships or aircraft by the lessor and the leased ships or aircraft are operated in international traffic, or the containers and related equipment are used in international traffic, by the lessee.

(2) The provisions of paragraph (1) shall apply to the share of the profits from the operation in international traffic of ships or aircraft derived by a resident of one of the Contracting States through participation in a pool service, in a joint transport operating organization or in an international operating agency.

(3) For the purposes of this Article, profits derived from the carriage by ships or aircraft of passengers, livestock, mail, goods or merchandise shipped in a Contracting State for discharge at another place in that State shall not be treated as profits from the operation in international traffic of ships or aircraft and may be taxed in that State.

ARTICLE 9
ASSOCIATED ENTERPRISES

(1) Where:

(a) an enterprise of one of the Contracting States participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State; or

(b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of one of the Contracting States and an enterprise of the other Contracting State,

and in either case conditions operate between the two enterprises in their commercial or financial relations which differ from those which might be expected to operate between independent enterprises dealing wholly independently with one another, then any profits which, but for those conditions, might have been expected to accrue to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.

(2) Where profits on which an enterprise of one of the Contracting States has been charged to tax in that State are also included, by virtue of paragraph (1), in the profits of an enterprise of the other Contracting State and taxed accordingly, and the profits so included are profits which might have been expected to have accrued to that enterprise of the other State if the conditions operative between the enterprises had been those which might have been expected to have operated between independent enterprises dealing wholly independently with one another, then the first-mentioned State shall make an appropriate adjustment to the amount of tax charged on those profits in the first-mentioned State. In determining such an adjustment, due regard shall be had to the other provisions of this Convention and the competent authorities of the Contracting State shall if necessary consult each other.

(3) Nothing in this Article shall affect the application of any Law of a Contracting State relating to the determination of the tax liability of a person, including determinations in cases where the information available to the competent authority of that State is inadequate to determine the income to be attributed to an enterprise, provided that, on the basis of the available information, the determination of that tax liability is consistent with the principles stated in this Article.

ARTICLE 10
DIVIDENDS

(1) Dividends paid by a company which is a resident of one of the Contracting States for the purposes of its tax, being dividends to which a resident of the other Contracting State is beneficially entitled, may be taxed in that other State.

(2) Such dividends may be taxed in the Contracting State of which the company paying the dividends is a resident for the purposes of its tax, and according to the law of that State, but the tax so charged shall not exceed 15 percent of the gross amount of the dividends.

(3) The term "dividends" in this Article means income from shares and other income assimilated to income from shares by the taxation law of the Contracting State of which the company making the distribution is a resident for the purposes of its tax.

(4) The provisions of paragraph (2) shall not apply if the person beneficially entitled to the dividends, being a resident of one of the Contracting States, carries on business in the other Contracting State, being the State of which the company paying the dividends is a resident, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the holding in respect of which the dividends are paid is effectively connected with such permanent establishment or fixed base. In such a case, the provisions of Article 7 (Business Profits) or Article 14 (Independent Personal Services), as the case may be, shall apply.

(5) Where a company is a resident of one of the Contracting States, the other Contracting State may not impose any tax on dividends paid by the company, except insofar as:

(a) a resident of that other State is beneficially entitled to the dividends;

(b) the holding in respect of which the dividends are paid is effectively connected with a permanent establishment or a fixed base situated in that other State; or

(c) that other State does not impose a tax of the kind described in paragraph (6) (excluding the accumulated earnings tax and the personal holding company tax imposed by the United States) and the dividends are paid out of profits attributable to one or more permanent establishments which such company had in that other State, provided that the gross income attributable to such permanent establishments constituted at least 50 percent of such company's gross income from all sources.

Where sub-paragraph (c) applies and sub-paragraphs (a) and (b) do not apply, any such tax shall not exceed 15 percent of the dividends.

(6) Nothing in this Convention shall be construed as preventing a Contracting State from imposing on the income of a company which is a resident of the other Contracting State, tax in addition to the taxes referred to in Article 2 in relation to the first-mentioned Contracting State which are payable by a company which is a resident of the first-mentioned State, provided that any such additional tax shall not exceed 15 percent of the amount by which the taxable income of the first-mentioned company of a year of income exceeds the tax payable on that taxable income to the first-mentioned State. Any tax payable to a Contracting State on the undistributed profits of a company which is a resident of the other Contracting State shall be calculated as if that company were not liable to the additional tax referred to in this paragraph and had paid dividends of such amount that tax equal to the amount of that additional tax would have been payable on the dividends in accordance with paragraph (2) of this Article.

ARTICLE 11
INTEREST

(1) Interest from sources in one of the Contracting States, being interest to which a resident of the other Contracting State is beneficially entitled, may be taxed in that other State.

(2) Such interest may be taxed in the Contracting State in which it has its source, and according to the law of that State, but the tax so charged shall not exceed 10 percent of the gross amount of the interest.

(3) Paragraph (2) shall not apply if the person beneficially entitled to the interest, being a resident of one of the Contracting States, has a permanent establishment in the other Contracting State or performs independent personal services in that other State from a fixed base situated therein and the indebtedness giving rise to the interest is effectively connected with such permanent establishment of fixed base. In such a case the provisions of Article 7 (Business Profits) or Article 14 (Independent Personal Services), as the case may be, shall apply.

(4) Where, owing to a special relationship between the payer and the person beneficially entitled to the interest, or between both of them and some other person, the amount of the interest paid, having regard to the indebtedness for which it is paid, exceeds the amount which might have been expected to have been agreed upon by the payer and the person so entitled in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In that case, the excess part of the amount of the interest paid shall remain taxable according to the law of each Contracting State, but subject to the other provisions of this Convention.

(5) The term "interest" as used in this Convention includes income which, under the taxation law of the Contracting State in which the income has its source, is assimilated to income from money lent.

(6) A Contracting State may not impose any tax on interest paid by a resident of the other Contracting State, except insofar as:

(a) such interest has its source in the first-mentioned State, or is interest to which a resident of that State is beneficially entitled; or

(b) the indebtedness in respect of which the interest is paid is effectively connected with a permanent establishment or a fixed base of the beneficial owner of the interest situated in the first-mentioned State.

(7) Interest shall be treated as income from sources in a Contracting State when the payer is that State itself or a political subdivision or local authority of that State or a person who is a resident of that State for the purposes of its tax. Where, however, the person paying the interest, whether he is a resident of one of the Contracting States or not, has in one of the Contracting States or outside both Contracting States a permanent establishment or fixed base in connection with which the indebtedness on which the interest is paid was incurred, and such interest is borne by such permanent establishment or fixed base, then such interest shall be deemed to have its source in the State in which the permanent establishment or fixed base is situated.

ARTICLE 12
ROYALTIES

(1) Royalties from sources in one of the Contracting States, being royalties to which a resident of the other Contracting State is beneficially entitled, may be taxed in that other State.

(2) Such royalties may be taxed in the Contracting State in which they have their source, and according to the law of that State, but the tax so charged shall not exceed 10 percent of the gross amount of the royalties.

(3) Paragraph (2) shall not apply if the person beneficially entitled to the royalties, being a resident of one of the Contracting States, has a permanent establishment in the other Contracting State or performs independent personal services in that other State from a fixed base situated therein, and the propery or rights giving rise to the royalties are effectively connected with such permanent establishment or fixed base. In such a case, the provisions of Article 7 (Business Profits) or Article 14 (Independent Personal Services), as the case may be, shall apply.

(4) The term "royalties" in this Article means:

(a) payments or credits of any kind to the extent to which they are consideration for the use of or the right to use any:

(i) copyright, patent, design or model, plan, secret formula or process, trademark or other like property or right;

(ii) industrial, commercial or scientific equipment, other than equipment let under a hire purchase agreement;

(iii) motion picture films; or

(iv) films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting;

(b) payments or credits of any kind to the extent to which they are considered for:

(i) the supply of scientific, technical, industrial or commercial knowledge or information owned by any person;

(ii) the supply of any assistance of an ancillary and subsidiary nature furnished as a means of enabling the application or enjoyment of knowledge or information referred to in sub-paragraph (b)(i) or of any other property or right to which this Article applies; or

(iii) a total or partial forbearance in respect of the use or supply of any property or right described in this paragraph; or

(c) income derived from the sale, exchange or other disposition of any property or right described in this paragraph to the extent to which the amounts realized on such sale, exchange or other disposition are contingent on the productivity, use or futher disposition of such property or right.

(5) Where, owing to a special relationship between the payer and the person beneficially entitled to the royalties or between both of them and some other person, the amount of the royalties paid or credited, having regard to what they are paid or credited for, exceeds the amount which might have been expected to have been agreed upon by the payer and the person so entitled in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In that case, the excess part of the amount of the royalties paid or credited shall remain taxable according to the law of each Contracting State, but subject to the other provisions of this Convention.

(6) (a) Royalties shall be treated as income from sources in a Contracting State when the payer is that State itself or a political subdivision or local authority of that State or a person who is a resident of that State for the purposes of its tax. Where, however, the person paying the royalties, whether he is a resident of one of the Contracting States or not, has in one of the Contracting States or outside both Contracting States a permanent establishment or fixed base in connection with which the liability to pay the royalties was incurred, and the royalties are borne by the permanent establishment or fixed base, then the royalties shall be deemed to have their source in the State in which the permanent establishment or fixed base is situated.

(b) Where sub-paragraph (a) does not operate to treat royalties as being from sources in one of the Contracting States, and the royalties relate to use or the right to use in one of the Contracting States of any property or right described in paragraph (4), the royalties shall be treated as income from sources in that State.

ARTICLE 13
ALIENATION OF PROPERTY

(1) Income or gains derived by a resident of one of the Contracting States from the alienation or disposition of real property situated in the other Contracting State may be taxed in that other State.

(2) For the purposes of this Article:

(a) the term "real property situated in the other Contracting State", where the United States is that other Contracting State, includes a United States real property interest, and real property referred to in Article 6 which is situated in the United States; and

(b) the term "real property", in the case of Australia, shall have the meaning which it has under the laws in force from time to time in Australia and, without limiting the foregoing, includes:

(i) real property referred to in Article 6;

(ii) shares or comparable interests in a company, the assets of which consist wholly or principally of real property situated in Australia; and

(iii) an interest in a partnership, trust or estate of a deceased individual, the assets of which consist wholly or principally of real property situated in Australia.

(3) Income or gains derived by an enterprise of one of the Contracting States from the alienation of ships, aircraft or containers operated or used by it in international traffic shall, except to the extent to which that enterprise has been allowed depreciation in the other Contracting State in respect of those ships, aircraft or containers, be taxable only in that State, and income described in subparagraph (4)(c) of Article 12 (Royalties) shall be taxable only in accordance with the provisions of Article 12.

(4) For the purposes of this Article, real property consisting of shares in a company referred to in sub-paragraph (2)(b)(ii), and interests in a partnership, trust or estate referred to in sub-paragraph (2)(b)(iii), shall be deemed to be situated in Australia.

ARTICLE 14
INDEPENDENT PERSONAL SERVICES

Income derived by an individual who is a resident of one of the Contracting States from the performance of personal services in an independent capacity shall be taxable only in that State unless such services are performed in the other Contracting State and:

(a) the individual is present in that other State for a period or periods aggregating more than 183 days in the taxable year or year of income of that other State; or

(b) the individual has a fixed base regularly available to him in that other State for the purpose of performing his activities, in which case so much of the income as is attributable to that fixed base may be taxed in such other State.

ARTICLE 15
DEPENDENT PERSONAL SERVICES

(1) Subject to the provisions of Article 18 (Pensions, Annuities, Alimony and Child Support) and 19 (Governmental Remuneration), salaries, wages and other similar remuneration derived by an individual who is a resident of one of the Contracting States in respect of an employment or in respect of services performed as a director of a company shall be taxable only in that State unless the employment is exercised or the services performed in the other Contracting State. If the employment is so exercised or the services so performed, such remuneration as is derived from that exercise or performance may be taxed in that other State.

(2) Notwithstanding the provisions of paragraph (1), remuneration derived by an individual who is a resident of one of the Contracting States in respect of an employment exercised in the other Contracting State or in respect of services performed in the other Contracting State as a director of a company shall be taxable only in the first-mentioned State if:

(a) the recipient is present in that other State for a period or periods not exceeding in the aggregate 183 days in the taxable year or year of income of that other State;

(b) the remuneration is paid by, or on behalf of, an employer or company who is not a resident of that other State; and

(c) the remuneration is not deductible in determining taxable profits of a permanent establishment, a fixed base or a trade or business which the employer or company has in that other State.

(3) Notwithstanding the preceding provisions of this Article, remuneration in respect of an employment exercised aboard a ship or aircraft operated in international traffic by a resident of one of the Contracting States may be taxed in that State.

ARTICLE 16
LIMITATION ON BENEFITS

(1) A person (other than an individual) which is a resident of one of the Contracting States shall not be entitled under this Convention to relief from taxation in the other Contracting State unless:

(a) more than 75 percent of the beneficial interest in such person (or in the case of a company, more than 75 percent of the number of shares of each class of the company's shares) is owned, directly or indirectly, by any combination of one or more of:

(i) individuals who are residents of the United States;

(ii) citizens of the United States;

(iii) individuals who are residents of Australia;

(iv) companies as described in sub-paragraph (b); and

(v) the Contracting States;

(b) it is a company in whose principal class of shares there is substantial and regular trading on a recognized stock exchange in one of the Contracting States; or

(c) the establishment, acquisition and maintenance of such person and the conduct of its operations did not have as one of its principal purposes the purpose of obtaining benefits under the Convention.

(2) For the purpose of sub-paragraph (1)(b), the term "a recognized stock exchange" includes, in relation to the United States, the NASDAQ System owned by the National Association of Securities Dealers, Inc.

(3) Where:

(a) income derived by a trustee is to be treated for the purposes of this Convention as income of a resident of one of the Contracting States; and

(b) the trustee derived the income in connection with a scheme a principal purpose of which was to obtain a benefit under this Convention,

then, notwithstanding any other provision of this Convention, the Convention does not apply in relation to that income.

ARTICLE 17
ENTERTAINERS

(1) Notwithstanding the provisions of Articles 14 (Independent Personal Services) and 15 (Dependent Personal Services), income derived by entertainers (such as theatrical, motion picture, radio or television artists, musicians and athletes) from their personal activities as such may be taxed in the Contracting State in which these activities are exercised, except where the amount of the gross receipts derived by any such entertainer, including expenses reimbursed to him or borne on his behalf, from such activities does not exceed ten thousand United States dollars ($10,000) or its equivalent in Australian dollars for the taxable year or year of income concerned.

(2) Where income in respect of activities exercised by an entertainer in his capacity as such accrues not to the entertainer but to another person, that income may, notwithstanding the provisions of Articles 7 (Business Profits), 14 (Independent Personal Services), and 15 (Dependent Personal Services), be taxed in the Contracting State in which the activities of the entertainer are exercised, unless it is established that neither the entertainer nor any person related to him participates directly or indirectly in any profits of such other person in any manner, including the receipt of deferred remuneration, bonuses, fees, dividends, partnership distributions or other distributions.

ARTICLE 18
PENSIONS ANNUITIES, ALIMONY AND CHILD SUPPORT

(1) Subject to the provisions of Article 19 (Governmental Remuneration), pensions and other similar remuneration paid to an individual who is a resident of one of the Contracting States in consideration of past employment shall be taxable only in that State.

(2) Social Security payments and other public pensions paid by one of the Contracting States to an individual who is a resident of the other Contracting State or a citizen of the United States shall be taxable only in the first-mentioned State.

(3) Annuities paid to an individual who is a resident of one of the Contracting States shall be taxable only in that State.

(4) The term "pensions and other similar remuneration", as used in this Article, means periodic payments made by reason of retirement or death, in consideration for services rendered, or by way of compensation paid after retirement for injuries received in connection with past employment.

(5) The term "annuities", as used in this Article, means stated sums paid periodically at stated times during life, or during a specified or ascertainable number of years, under an obligation to make the payments in return for adequate and full consideration (other than services rendered or to be rendered).

(6) Any alimony or other maintenance payments, including payments for the support of a minor child, arising in one of the Contracting States and paid to a resident of the other Contracting State, shall be taxable only in the first-mentioned State.

ARTICLE 19
GOVERNMENTAL REMUNERATION

Wages, salaries, and similar remuneration, including pensions, paid from funds of one of the Contracting States, of a state or other political subdivision thereof or of an agency or authority of any of the foregoing for labor or personal services performed as an employee of any of the above in the discharge of governmental functions to a citizen of that State shall be exempt from tax by the other Contracting State.

ARTICLE 20
STUDENTS

Where a student, who is a resident of one of the Contracting States or who was a resident of that State immediately before visiting the other Contracting State and who is temporarily present in that other State for the purpose of his full-time education, receives payments from sources outside that other State for the purpose of his maintenance or education, those payments shall be exempt from tax in that other State.

ARTICLE 21
INCOME NOT EXPRESSLY MENTIONED

(1) Items of income of a resident of one of the Contracting States which are not expressly mentioned in the foregoing Articles of this Convention shall be taxable only in that State.

(2) However, if such income is derived by a resident of one of the Contracting States from sources in the other Contracting State, such income may also be taxed in the State in which it has its source.

(3) The provisions of paragraph (1) shall not apply to income derived by a resident of one of the Contracting States which is effectively connected with a permanent establishment situated in the other Contracting State. In such a case, the provisions of Article 7 (Business Profits) shall apply.

ARTICLE 22
RELIEF FROM DOUBLE TAXATION

(1) Subject to paragraph (4) and in accordance with the provisions and subject to the limitations of the law of the United States (as it may be amended from time to time without changing the general principle hereof), in the case of the United States, double taxation shall be avoided as follows:

(a) the United States shall allow to a resident or citizen of the United States as a credit against United States tax the appropriate amount of income tax paid to Australia; and

(b) in the case of a United States corporation owning at least 10 percent of the voting stock of a company which is a resident of Australia from which it receives dividends in any taxable year, the United States shall also allow as a credit against United States tax the appropriate amount of income tax paid to Australia by that company with respect to the profits out of which such dividends are paid.

Such appropriate amount shall be based upon the amount of income tax paid to Australia. For purposes of applying the United States credit in relation to income tax paid to Australia the taxes referred to in sub-paragraph (1)(b) and paragraph (2) of Article 2 (Taxes Covered) shall be considered to be income taxes. No provision of this Convention relating to source of income shall apply in determining credits against United States tax for foreign taxes other than those referred to in sub-paragraph (1)(b) and paragraph (2) of Article 2 (Taxes Covered).

(2) Subject to paragraph (4), United States tax paid under the law of the United States and in accordance with this Convention, other than United States tax imposed in accordance with paragraph (3) of Article 1 (Personal Scope) soley by reason of citizenship or by reason of an election by an individual under United States domestic law to be taxed as a resident of the United States, in respect of income derived from sources in the United States by a person who, under Australian law relating to Australian tax, is a resident of Australia shall be allowed as a credit against Australian tax payable in respect of the income. The credit shall not exceed the amount of Australian tax payable on the income or any class thereof or on income from sources outside Australia. Subject to these general principles, the credit shall be in accordance with the provisions and subject to the limitations of the law of Australia as that law may be in force from time to time.

(3) An Australian corporation that owns at least 10 percent of the voting power in a United States corporation is, in accordance with the law of Australia as in force at the date of signature of this Convention, entitled to a rebate in its assessment, at the average rate of tax payable by it, in respect of dividends paid by the United States corporation that are included in the taxable income of the Australian corporation. However, should the law as so in force be amended so that the rebate in relation to the dividends ceases to be allowable under that law, Australia shall allow credit under paragraph (2) for the United States tax paid on the profits out of which the dividends are paid as well as for the United States tax paid on the dividends.

(4) For the purposes of computing United States tax, where a United States citizen is a resident of Australia, the United States shall allow as a credit against United States tax the income tax paid to Australia after the credit referred to in paragraph (2). The credit so allowed against United States tax shall not reduce that portion of the United States tax that is creditable against Australian tax in accordance with paragraph (2).

ARTICLE 23
NON-DISCRIMINATION

(1) Each Contracting State in enacting tax measures shall ensure that:

(a) citizens of a Contracting State who are residents of the other Contracting State shall not be subjected in that other State to any taxation or any requirement connected therewith which is more burdensome than the taxation or connected requirements to which citizens of that other State who are residents of that other State in the same circumstances are or may be subjected;

(b) except where the provisions of paragraph (1) of Article 9 (Associated Enterprises), paragraph (4) of Article 11 (Interest) or paragraph (5) of Article 12 (Royalties) apply, interest, royalties and other disbursements paid by a resident of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable profits of the resident of the first-mentioned State, be deductible under the same conditions as if they had been paid to a resident of the first-mentioned State;

(c) a corporation of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned State to any taxation or any requirement connected therewith which is more burdensome than the taxation or connected requirements to which other similar corporations of the first-mentioned State in the same circumstances are or may be subjected; and

(d) the taxation on a permanent establishment which a resident of a Contracting State has in the other Contracting State shall not be less favorably levied in that other State than the taxation levied on residents of that other State that carry on the same activities in the same circumstances.

(2) Nothing in this Article relates to any provision of the taxation laws of a Contracting State:

(a) in force on the date of signature of this Convention;

(b) adopted after the date of signature of this Convention but which is substantially similar in general purpose or intent to a provision covered by sub-paragraph (a); or

(c) reasonably designed to prevent the avoidance or evasion of taxes;

provided that, with respect to provisions covered by sub-paragraphs (b) or (c), such provisions (other than provisions in international agreements) do not discriminate between citizens or residents of the other Contracting State and those of any third State.

(3) Without limiting by implication the interpretation of this Article, it is hereby declared that, except to the extent expressly so provided, nothing in the Article prevents a Contracting State from distinguishing in its taxation laws between residents and non-residents solely on the ground of their residence.

(4) Where one of the Contracting States considers that the taxation measures of the other Contracting State infringe the principles set forth in this Article the Contracting States shall consult together in an endeavor to resolve the matter.

ARTICLE 24
MUTUAL AGREEMENT PROCEDURE

(1)(a) Where a resident of one of the Contracting States considers that the action of one or both of the Contracting States results or will result for him in taxation not in accordance with this Convention, he may, notwithstanding the remedies provided by the domestic laws of those States, present his case to the competent authority of the Contracting State of which he is a resident or citizen. The case must be presented within three years from the first notification of that action.

(b) Should the claim be considered to have merit by the competent authority of the Contracting State to which the claim is made, that competent authority shall seek to come to an agreement with the competent authority of the other Contracting State with a view to the avoidance of taxation contrary to the provisions of this Convention. Any agreement reached shall be implemented notwithstanding any time limits or other procedural limitations in the domestic law of the Contracting States.

(2) The competent authorities of the Contracting States shall seek to resolve by agreement any difficulties or doubts arising as to the application or interpretation of this Convention. In particular the competent authorities of the Contracting States may agree:

(a) to the same attribution of income, deductions, credits, or allowances of an enterprise of one of the Contracting States to its permanent establishment situated in the other Contracting State;

(b) to the same allocation of income, deductions, credits, or allowances between persons;

(c) to the same determination of the source of particular items of income;

(d) to the same meaning of any term used in this Convention; or

(e) to which of the Contracting States an individual described in sub-paragraph (2)(c) of Article 4 (Residence) has closer personal and economic relations.

(3) The competent authorities of the Contracting States may communicate with each other directly for the purpose of reaching an agreement in the sense of this Article.

ARTICLE 25
EXCHANGE OF INFORMATION

(1) The competent authorities shall exchange such information as is necessary for carrying out the provisions of this Convention or for the prevention of fraud or for the administration of statutory provisions concerning taxes to which this Convention applies provided the information is of a class that can be obtained under the laws and administrative practices of each Contracting State with respect to its own taxes.

(2) Any information so exchanged shall be treated as secret and shall not be disclosed to any persons other than those (including a Court or administrative body) concerned with the assessment, collection, administration or enforcement of, or with litigation with respect to, the taxes to which this Convention applies.

(3) No information shall be exchanged which would be contrary to public policy.

(4) If specifically requested by the competent authority of one of the Contracting States, the competent authority of the other Contracting State shall provide information under the Article in the form of copies of unedited original documents (including books, papers, statements, records, accounts or writings) to the same extent such documents can be obtained under the laws and administrative practices of that other State with respect to its own taxes.

(5) Each of the Contracting State shall endeavor to collect on behalf of the other Contracting State amounts equal to such taxes imposed by the other State as will ensure that any exemption or reduction in rate of tax granted under this Convention by that other State shall not be enjoyed by persons not entitled to such benefits.

ARTICLE 26
DIPLOMATIC AND CONSULAR PRIVILEGES

Nothing in this Convention shall affect diplomatic and consular privileges under the general rules of international law or under the provisions of special agreements.

ARTICLE 27
MISCELLANEOUS

(1)(a) Income derived by a resident of the United States which, under this Convention, may be taxed in Australia shall for the purposes of the income tax law of Australia and of this Convention be deemed to be income from sources in Australia.

(b) Income derived by a resident of Australia which, under this Convention, may be taxed in the United States, other than income taxed by the United States in accordance with paragraph (3) of Article 1 (Personal Scope) solely by reason of citizenship or by reason of an election by an individual under United States domestic law to be taxed as a resident of the United States, shall for the purposes of paragraph (2) of Article 22 (Relief from Double Taxation) and of the income tax law of Australia be deemed to be income from sources in the United States.

(c) Where paragraph (4) of Article 22 (Relief from Double Taxation) applies, income referred to in that paragraph shall be deemed to have its source in Australia to the extent necessary to give effect to the provisions of that paragraph.

(2) Any exemption from tax by one of the Contracting States provided for in Article 14 (Independent Personal Services), 15 (Dependent Personal Services), 17 (Entertainers) or 19 (Governmental Remuneration) shall be inapplicable to the extent that the income to which the exemption relates is not or, upon the application of the relevant Article of this Convention (prior to application of this paragraph), will not be subject to tax by the other Contracting State.

ARTICLE 28
ENTRY INTO FORCE

(1) This Convention shall be subject to ratification in accordance with the applicable procedures of each Contracting State, and instruments of ratification shall be exchanged at Washington, D.C., as soon as possible.

(2) The Convention shall enter into force upon the exchange of instruments of ratification and its provisions shall have effect:

(a) with respect to those dividends, interest and royalties to which Articles 10 (Dividends), 11 (Interest) and 12 (Royalties), respectively, apply and which are paid, credited or otherwise derived on or after the first day of the second month following the date on which the Convention enters into force; and

(b) with respect to all other income of a taxpayer, for the taxpayer's years of income or taxable years, as the case may be, commencing on or after the first day of the second month following the date on which the Convention enters into force.

(3) Subject to paragraph (4), the Convention between the Government of the United States of America and the Government of the Commonwealth of Australia for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income signed at Washington on May 14, 1953 (in this Article referred to as the 1953 Convention) shall cease to have effect with respect to taxes to which this Convention applies under paragraph (2).

(4) The 1953 Convention shall terminate on the expiration of the last date on which it has effect in accordance with the foregoing provisions of this Article.

ARTICLE 29
TERMINATION

(1) This Convention shall remain in force until terminated by a Contracting State. Either Contracting State may terminate the Convention at any time after 5 years from the date on which the Convention enters into force, provided that at least 6 months prior notice of termination has been given through the dip-

lomatic channel. In such event, the Convention shall cease to have effect:

(a) with respect to those dividends, interest and royalties to which Articles 10 (Dividends), 11 (Interest) and 12 (Royalties) respectively apply, and which are paid, credited or otherwise derived on or after the first day of January following the expiration of the 6 month period; and

(b) with respect to all other income of a taxpayer, for the taxpayer's years of income or taxable years, as the case may be, commencing on or after the first day of January following the expiration of the 6 month period.

(2) Notwithstanding the provisions of paragraph (1), upon prior notice to be given through the diplomatic channel, the provisions of paragraph (2) of Article 18 (Pensions, Annuities, Alimony and Child Support) may be terminated by either Contracting State at any time after this Convention enters into force.

Done in duplicate at Sydney this sixth day of August 1982.

SENATE EXECUTIVE REPORT NO. 98–16

[Bracketed numerals indicate official report page number]

TAX CONVENTION WITH THE GOVERNMENT OF AUSTRALIA

Mr. Percy, from the Committee on Foreign Relations, submitted the following report to accompany Treaty Doc. 97–28, 97th Cong., 2d sess.

The Committee on Foreign Relations, to which was referred the Tax Treaty with the Government of Australia[1] for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income (Treaty Doc. 97–28), having considered the same, reports favorably thereon, and recommends that the Senate give its advice and consent to ratification thereof.

I. PURPOSE

The principal purpose of the proposed income tax treaty between the United States and Australia is to reduce or eliminate potential double taxation of income earned by citizens and residents of either country from sources within the other country and to prevent avoidance or evasion of the income taxes of the two countries. The proposed treaty is intended to promote closer economic cooperation between the two countries and to eliminate possible barriers to trade caused by overlapping taxing jurisdictions of the two countries. It is intended to enable the countries to cooperate in preventing avoidance and evasion of taxes.

II. BACKGROUND

The proposed treaty with Australia was signed on August 6, 1982. The proposed treaty would replace the 1953 income tax treaty between the United States and Australia. The treaty was transmitted to the Senate for advice and consent to ratification on September 14, 1982.

III. SUMMARY

The proposed treaty is similar to other recent U.S. income tax treaties and to the model income tax treaty of the Organization for Economic Cooperation and Development (OECD) in many respects, but in certain respects it accords greater jurisdiction to tax to the country of source, rather than to the country of residence.

As in other U.S. tax treaties, the objectives of the treaty are principally achieved by each country agreeing to limit, in certain specified situations, its right to tax income derived from its territory by residents of the other. For example, the treaty contains the standard tax treaty provisions that neither country will tax the business income derived from sources within that country by residents of the other unless the business activities of the taxing country are substantial enough to constitute a permanent establishment or fixed base (Articles 7 or 14). Similarly, the treaty contains the standard "commercial visitor" exemptions under which residents of one country performing personal services in the other will not be required to pay tax in the other unless their contact with the other exceeds specified minimums (Articles 14, 15, and 17). The proposed treaty provides that dividends, interest, royalties, certain capital gains and certain other income derived by a resident of either country from sources within the other country, generally may be taxed by both countries (Articles 10, 11, 12, 13, and 21). Generally, however, dividends, interest, and royalties received by a resident of one country from sources within the other country are to be taxed by the source country on a restricted basis (Articles 10, 11, and 12).

In situations where the country of source retains the right under the proposed treaty to tax income derived by residents of the other country, the treaty generally provides for the relief of the potential double taxation by the country of residence allowing a foreign tax credit or, in certain cases, a partial exemption.

This treaty contains the standard provision (the "saving clause") contained in U.S. tax treaties that each country retains the right to tax its citizens and residents as if the treaty had not come into effect (Article 1). In addition, it contains the standard provision that the treaty will not be applied to deny any taxpayer any benefits he would be entitled to under the domestic law of the country or under any other agreement between the two countries (Article 1); that is, the treaty will be applied only to the benefit of taxpayers.

The proposed treaty differs in certain respects from many U.S. income tax treaties and the U.S. model. It also differs in significant respects from the present treaty with Australia.

(1) U.S. citizens who are not also U.S. residents are not generally covered. The U.S. model does cover such U.S. citizens. However, the United States has rarely been able to negotiate coverage for nonresident citizens.

(2) The proposed treaty does not provide for determination of a single residence for all corporations that are residents of both the United States and Australia under local law. The U.S. and Organization for Economic Cooperation and Development (OECD) model treaties do each provide for such a determination. The effect of the lack of such a provision in the proposed treaty is to deny certain treaty benefits to dual resident corporations. Although such corporations may under current law be able to deduct certain amounts in both countries, they would also have to include items of income in both countries. The proposed treaty might tend to encourage some dual resident companies to become residents of but one country so as to take advantage of certain treaty benefits.

(3) The definition of permanent establishment in the proposed treaty is somewhat broader than that in the U.S. model and in many existing U.S. treaties. The principal areas in which the proposed treaty departs from the U.S. model are the inclusion as a permanent establishment of a building site or construction, assembly or installation project that exists for more than 9 months and an installation, drilling rig or ship that, for at least 6 months in

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[1] Page 7: Technical Explanation, page 33.

any 24 month period, is used for dredging or for sea-bed and subsoil exploration or mining (rather than, in each case, the model's 12 months). In addition, maintaining substantial equipment in a country for more than 12 months or engaging in supervisory activities in connection with building sites, etc. for more than 9 months in any 24 month period would create permanent establishment status under the proposed treaty but not under the model.

(4) The proposed treaty does not contain a definition of the term "business profits," although certain categories of business profits are defined in various articles. This leaves to local law the definition of that term in some cases, and accordingly the profits must be attributed to a permanent establishment before those profits can be taxed by the country where the permanent establishment is located. Many U.S. treaties, and the U.S. model, define the term business profits to include income from rental of tangible personal property and from rental or licensing of films or tapes. Absence of this definition means that persons who earn such rental or licensing income could be subject to tax on a gross basis, not a net basis, in the source country unless they maintain a permanent establishment there.

(5) The proposed treaty does not allow investors in real property in the country not of their residence to elect to be taxed on such investments on a net basis. The U.S. model allows such an election. Although current Australian law and current U.S. law provide for net basis taxation, there is no guarantee that Australia will continue such treatment.

(6) The proposed treaty does not exempt from source country tax certain categories of income that would be exempt under the U.S. model treaty as shipping or aircraft income. These categories include: (1) income from leasing containers that is not incidental to the operation of ships or aircraft in international traffic by the lessor; and (2) income from leasing ships or aircraft on a full basis by persons that do not either operate ships or aircraft in international traffic or in their home country or regularly lease ships or aircraft on a full basis.

(7) The limit on the gross dividend withholding tax that the country of source may impose is 15 percent (Article 10) in contrast to the 5 percent limit on direct dividends and 15 percent limit on portfolio dividends in the U.S. model. The present treaty also allows a 15 percent rate.

(8) The withholding tax at source on gross interest is limited to 10 percent (Article 11) rather than the zero rate in the U.S. model. A zero rate is not generally achieved in many treaties, but is at times achieved for interest earned by banks on loans made into the source country. Although the present treaty does not limit the rate of the withholding tax on interest, the current Australian statutory withholding rate is 10 percent, while the analogous U.S. rate is 30 percent.

(9) The withholding tax at source on royalties is limited to 10 percent (Article 12) rather than the zero rate in the U.S. model. The present treaty does not generally limit source country taxation of royalties, but does exempt certain copyright royalties (not film and video royalties) from tax at source. The current Australian statutory withholding rate on royalty payments (which would be reduced to 10 percent by the proposed treaty) is 51 percent in many cases.

(10) The proposed treaty allows source country taxation of capital gains generally including gain on disposition of real estate (thus preserving U.S. tax under the Foreign Investment in U.S. Real Property Tax Act of 1980 ("FIRPTA")). The U.S. model generally permits source country taxation of real estate gain and gain from the alienation of personal property attributable to a permanent establishment or fixed base in the source country but prohibits other source country taxation of capital gains.

(11) The proposed treaty allows source country taxation of independent personal services on the basis of presence in that country for more than 183 days in a taxable year. The model treaty does not allow taxation on that basis. Under the model, independent personal services of a nonresident are taxable only if the nonresident has available a fixed base in the source country.

(12) The proposed treaty allows source country taxation of entertainers and athletes who earn more than $10,000 there during a taxable year; the comparable amount in the model treaty is $20,000.

(13) The present treaty exempts from source country taxation the salaries of teachers from the other country who visit for two years or less. The proposed treaty, like the U.S. model, subjects those amounts to its standard rules, which would ordinarily result in full source country taxation.

(14) The proposed treaty exempts alimony payments from taxation in the country of the recipient's residence, while allowing the payor's country to tax them. The model treaty exempts such payments from taxation in the country of the payor's residence, while allowing the country of the recipient's residence to tax them.

(15) The proposed treaty's nondiscrimination provision is more limited than the U.S. model and provisions found in many U.S. tax treaties because it does not apply to the tax rules that were in effect in either country on the date of signature, August 6, 1982, and because it does not prevent discrimination by States and localities in their tax laws. The present treaty, however, does not limit discrimination at all.

[5] (16) The proposed treaty provides for the exchange of information relating only to taxes it covers. The U.S. model treaty applies to taxes of every kind imposed by the contracting countries.

(17) The proposed treaty provides that any source country exemption of personal services income is inapplicable if the residence country exempts that income. The model treaty contains a similar provision that is not limited to personal services income. One effect of this provision is that a limited category of U.S. individuals who are exempt from U.S. tax on foreign earned income (under Code sec. 911) would be subject to Australian tax on Australian income.

IV. DATE OF ENTRY INTO FORCE AND TERMINATION

Entry into Force

The proposed treaty will enter into force upon the exchange of instruments of ratification. As a general rule, the treaty will become effective for taxable years beginning on or after the first day of the second month following the date on which the proposed treaty comes into force. With respect to dividends, interest and royalties that are the subject of the treaty rules under Articles 10, 11, and 12 respectively, the treaty will be effective for amounts paid, credited, or derived on or after the first day of the second month next following the date on which the convention enters into force. The existing treaty is to be phased out as the proposed treaty becomes effective. When the proposed treaty becomes fully effective the existing treaty will terminate.

Termination

The proposed treaty will continue in force indefinitely, but either country may terminate it at any time after five years from its entry into force by giving at least six months prior notice through the diplomatic channel. If termination occurs, the termination will be effective with respect to dividends, interest and royalties (to which Articles 10, 11, or 12 apply) for amounts paid, credited or otherwise derived on or after the first day of January following the expiration of the six months notice. Any termination will be effective with respect to other income for taxable years beginning on or after the first day of January following the expiration of the six months notice.

The proposed treaty contains a special rule allowing either country to terminate one treaty provision in Article 18 (exempting social security payments and other public pension payments from taxation on the basis of residence and citizenship) without terminating any other provision of the treaty. Such partial termination may occur, upon prior notice through the diplomatic channel, at any time after the treaty enters into force.

V. COMMITTEE ACTION

The Commitee on Foreign Relations held public hearings on the proposed Australian income tax treaty, and on other income tax treaties, on May 24, 1983. The Committee heard testimony in opposition to the treaty from Edward Woolley, Secretary and General Counsel of the Institute of International Container Lessors. The [6] Committee considered the proposed treaty on June 28, 1983, and ordered it favorably reported by a voice vote, with the recommendation that the Senate give its advice and consent to its ratification.

VI. COMMITTEE COMMENTS

The Committee on Foreign Relations approved the treaty, but expressed its serious concern with the treatment of container leasing income and with the extension of permanent establishment treatment to drilling rigs present in the taxing country for a limited period of time.

This treaty contains two provisions that depart from the U.S. model treaty in a way that adversely affects two important U.S. industries—the container leasing industry and the contract drilling industry. In some cases, a particular taxpayer or industry may receive better treatment under an existing treaty than under a newly negotiated treaty or may receive better treatment under the U.S. model treaty than under a specific treaty. Since a treaty is essentially a compromise between two countries with competing interests, that result is not unexpected. The central issue is whether the final agreement represents a bargain which is sufficiently favorable overall to the United States that it should be ratified. The Committee recognizes that the negotiation of a tax treaty involves a wide range of issues and a significant amount of give and take on both sides. In this case, the Committee notes that the proposed treaty is the result of fourteen years of negotiation and would benefit a number of U.S. industries with substantial investments in Australia. Therefore, the Committee believes that the appropriate course of action is to approve the treaty while indicating the disfavor with which it views the provisions allowing Australian taxation of U.S. container lessors and contract drillers.

The Commitee is, however, concerned that an individual industry not repeatedly pay the price for treaty relationships. The Committee will monitor treaties that are negotiated in the future to make sure that individual industries are not bearing the brunt of the bargain in those treaties, and will have to seriously consider rejecting treaties that do not contain the proper balance between the interest of a particular industry and benefits to a broad range of U.S. taxpayers.

Container leasing income

The proposed treaty would permit Australia to tax container leasing rentals as royalties subject to a withholding tax of 10 percent of the gross rental in certain cases unless the lease is merely incidental to the operation in international traffic of ships or aircraft by the lessor (Articles 8 and 12). Under the U.S. model, container leasing income is treated as transportation income and is exempt from tax at source even though the lessor is not engaged in international traffic of ships or aircraft.

The Committee is concerned with this provision for several reasons. First, it represents a significant departure from U.S. policy as expressed in the U.S. model income tax treaty and from recent U.S. practice. All the treaties that the United States has negotiated since adoption of the 1977 U.S. model have treated container leasing [7] income as either shipping income, exempt in the source country, or as business profits, taxable on a net basis. Second, inclusion of this provision seems to indicate that there is some justifiable distinction between container leasing income and other transportation income. The Committee does not believe that any such justifiable distinction exists. Third, it could allow Australia to impose a gross withholding tax that could exceed net income in certain cases. Fourth, it would place container leasing companies at a competitive disadvantage to shipping companies who lease containers in international traffic as an incidental prt of their business, and who would be exempt from tax on those container leases under the proposed treaty (as under the U.S. model treaty). Fifth, the taxation of container leasing income on the basis of the residence of the payor is inappropriate because it could lead to multiple taxation. If one country (such as Australia) taxes container leasing income of a U.S. lessor on the basis of residence of the lessee, while a third country (not a party to the treaty) taxes that income on the basis of location of the container, there may be double taxation. Although the United States, as residence country, would not claim primary taxing jurisdiction in this example, the overlapping claims of source country jurisdiction could result in extremely high tax rates.

The Committee has been advised that the Treasury does not view this provision as precedent. The Committee expresses its strong concern about this provision and advises the Treasury Department, in any future negotiations, to take all necessary steps to conform future treaties to the U.S. model treaty on this point.

Income from drilling activities

The proposed treaty contains a permanent establishment article that is broader than that contained in the U.S. or OCED model treaties. It would permit the country in which certain activities are carried on to tax income from those activities sooner than it would be able to under the model. Under the proposed treaty, U.S. enterprises that use an installation, drilling rig or ship for dredging or in connection with the exploration for or exploitation of natural resources of the Australian sea-bed and subsoil may be subject to Australian tax if they are present in Australian territory for as little as 6 months in any 24-month period. Under the U.S. model, they must be present there for at least one year. The practical effect of the provision could be to increase Australian taxation of mineral exploration activities. This expansion was made at the insistence of Australia.

The Committee wishes to express its strong concern with the treatment that contract drillers receive under this treaty. The contract drilling industry is important to the United States, and the Committee strongly supports the approach of the U.S. model income tax treaty for contract drillers for treaties to be negotiated in the future. The Committee wishes to stress that the acceptance of this provision in this particular treaty does not indicate that the Committee will accept similar treatment in treaties negotiated in the future; it does not view this provision as a precedent for treaties to be negotiated in the future.

VII. BUDGET IMPACT

[8] The Committee estimates that the effect of the proposed treaty on budget receipts will be to produce negligible revenue gains in fiscal years through 1988.

In accordance with the objectives of section 403 of the Budget Act, the Committee advises that the Director of the Congressional Budget Office has examined the Committee's budget estimate and agrees that the effect on budget receipts will be to produce negligible revenue gains in fiscal years through 1988. In keeping with the spirit of section 308(a) of the Budget Act, and after consultation with the Director of the Congressional Budget Office, the Committee states that the treaty does not provide any new budget authority or any new or increased tax expenditures.

VIII. EXPLANATION OF TREATY PROVISIONS

[9] Set forth below is an article-by-article explanation of the proposed income tax treaty between the United States and Australia.

ARTICLE 1

PERSONAL SCOPE

The personal scope article describes the persons who may claim the benefits of the treaty and contains other rules including the "saving clause."

The proposed treaty applies generally to residents of the United States and to residents of Australia, with specific exceptions designated in other articles. This follows other U.S. income tax treaties, the U.S. model income tax treaty, and the OECD model income tax treaty. The terms "resident of the United States" and "resident of Australia" are defined in Article 4.

The proposed treaty provides that it does not restrict any benefits accorded by internal law or by any other agreement between the United States and Australia. Thus, the treaty will apply only where it benefits taxpayers.

Like all U.S. income tax treaties, the proposed treaty also contains a "saving clause." Under this clause, with specific exceptions described below, the treaty is not to affect the taxation by either country of its citizens or its residents. The proposed treaty would not affect the taxation of individuals electing under its domestic law to be taxed as residents of that taxing country. Under U.S. law, nonresident aliens may elect to be taxed as residents in certain circumstances (see sec. 6013(g), allowing filing of joint returns in certain cases upon such an election). By reason of the saving clause, unless otherwise specifically provided in the proposed treaty, the United States will continue to tax its citizens who are residents of Australia. Residents for purposes of the treaty (and thus, for purposes of the saving clause) include corporations and other entities as well as individuals (Article 4 (Residence)).

Under Section 877 of the Internal Revenue Code of 1954 ("Code"), a former U.S. citizen whose loss of citizenship had as one of its principal purposes the avoidance of U.S. income, estate or gift taxes, will, in certain cases, be subject to tax for a period of 10 years following the loss of citizenship. The treaty contains the standard provision found in the U.S. model and most recent treaties specifically retaining the right to tax former citizens. Even absent a specific provision the Internal Revenue Service takes the position that the United States retains the right to tax former citizens resident in the treaty partner (Rev. Rul. 79–152, 1979–1 C.B. 237).

Exceptions to the saving clause are provided for certain benefits conferred by the articles dealing with Associated Enterprises (Article 9); Pensions, Annuities, Alimony and Child Support (Article 18); Relief from Double Taxation (Article 22); Nondiscrimination (Article 23); [10] Mutual Agreement Procedure (Article 24); and certain sourcing rules (Article 27).

In addition, the saving clause does not apply to the benefits conferred by one of the countries under the articles dealing with Governmental Renumeration (Article 19), Students (Article 20), or Diplomatic and Consular Privileges (Article 26), upon individuals (1) who are not citizens of that conferring country and (2) who in the case of the United States do not have immigrant status, or who in the case of Australia are not ordinarily resident in Australia.

ARTICLE 2

TAXES COVERED

The proposed treaty generally applies to the income taxes of the United States and Australia.

In the case of the United States, the proposed treaty applies to the Federal income taxes imposed by the Internal Revenue Code, but excluding the accumulated earnings tax and the personal holding company tax. In the case of Australia, the proposed treaty applies to the Australian income tax, including the additional tax upon the undistributed amount of the distributable income of a private company. Although the U.S. model treaty applies to the excise tax on private foundations and (in certain cases) to the excise tax on insurance premiums paid to foreign insurers, the proposed treaty does not apply to those taxes. Thus, the United States could continue to impose them.

The proposed treaty contains a provision generally found in U.S. income tax treaties to the effect that it will apply to substantially similar taxes that either country may subsequently impose. The proposed treaty also obligates the competent authority of each country, at the end of each calendar year, to notify the competent authority of the other country of any substantial changes that have been made during that year in the laws of his country relating to the taxes to which the treaty applies or in the official interpretation of those laws or of the treaty. This rules is similar to the rule of the U.S. model.

ARTICLE 3

GENERAL DEFINITIONS

Certain of the standard definitions found in most U.S. income tax treaties are contained in the proposed treaty. The proposed treaty deviates from the U.S. model in its definitions of U.S. corporation and Australian corporation.

The term "person" is defined to include an individual, an estate or trust, a partnership, a company and any other body of persons. A "company" is any body corporate or any entity which is treated as a company or body corporate for tax purposes. An enterprise of a country is defined as an enterprise carried on by a resident of that country. Although the treaty does not define the term "enterprise" it would have the same meaning that it has in other U.S. tax treaties—the trade or business activities undertaken by an individual, partnership, corporation, or other entity.

The proposed treaty defines international traffic as any transport by a ship or aircraft, except where the transport is solely between places in one of the contracting countries. Accordingly, purely domestic transport in the United States or in Australia is excluded.

[11] The U.S. competent authority is the Secretary of Treasury or his delegate. In fact, the U.S. competent authority function has been delegated to the Commissioner of the Internal Revenue Service, who has redelegated the authority to the Associate Commissioner (Operations). The Assistant Commissioner (Examination) has been delegated the authority to administer programs for simultaneous, spontaneous, and industry-wide exchanges of information. The Director, Foreign Operations District (formerly called the Director of the Office of International Operations), has been delegated the authority to administer programs for routine and specific exchanges of information and mutual assistance in collection. The Australian competent authority is the Commissioner of Taxation or his authorized representative.

The term "Contracting State" means the United States or Australia, as the context requires. The term "State" means any country, and is not necessarily limited to the United States and Australia.

The term "United States corporation" is defined to mean a corporation that (1) under U.S. tax law, is a domestic corporation or an unincorporated entity treated (under section 7701) as a domestic corporation, and (2) is not, under Australian tax law, a resident of Australia. Similarly, the term "Australian corporation" means a company (as defined under the Australian tax law) that (1) is (under the Australian tax law) a resident of Australia, and (2) is not, under U.S. tax law, a U.S. corporation or an unincorporated entity treated (under section 7701) as a U.S. corporation. Under Australian law, a resident company is defined as a company which is incorporated in Australia, or which, not being incorporated in Australia, carries on business in Australia and has either its central management and control in Australia, or its voting power controlled by shareholders who are residents of Australia.

The interaction of United States and Australian law can result in a corporation being a resident of both countries under local law. For example, a corporation incorporated in the United States but carrying on business and being managed in Australia would be considered a domestic corporation by both countries under their local laws. The treaty provides that such a dual resident corporation is neither a U.S. nor an Australian corporation and thus would not be entitled to the benefits due a "United States corporation" or an "Australian corporation" under the treaty. The proposed treaty may tend to encourage corporations to arrange their affairs so as to obtain certain treaty benefits by being a resident of only one country. In this definition of residence, the proposed treaty differs from the U.S. model treaty, which seeks to find a single residence for corporations for treaty purposes.

The proposed treaty defines the terms "United States tax" and "Australian tax" as meaning the taxes covered by the treaty, but not penalties or interest imposed under the tax law of either country. Thus, the right of a country to impose penalties or interest is not limited by the proposed treaty.

The "United States" means the United States of America, a term that does not include Puerto Rico, the Virgin Islands, Guam or any other United States possession or territory. The definition of the United States also includes, when the term is used in a geographical sense, [12] the territorial waters of the United States and the seabed and subsoil of the submarine areas adjacent to the coast of the United States but beyond the territorial waters of the United States, which, in accordance with international law and the laws of the United States, are areas within which the United States exercises rights to exploit or explore for natural resources. The intent of this rule is to cover the U.S. continental shelf consistent with the definition of continental shelf contained in section 638 of the Code. In accordance with that intent, it is immaterial that no exploitation or exploration had occurred or was occurring in any particular area at the time of the signing of the treaty.

Under the proposed treaty, the term "Australia" means the Commonwealth of Australia. The definition of Australia also includes, when the term is used in a geographical sense, the Territory of Norfolk Island, the Territory of Christmas Island, the Territory of Cocos (Keeling) Island, the Territory of Ashmore and Cartier Islands, the Coral Sea Islands Territory, and any area adjacent to the territorial limits of Australia or any of those named territories which, in accordance with international law, is an area in which there is for the time being in force a law of Australia or of one of its States or Territories dealing with the exploitation of any of the natural resources of the seabed and subsoil of the continental shelf. Therefore, income earned on the Australian continental shelf is covered. The terms "resident of one of the Contracting States" and "resident of the other Contracting State" mean a resident of Australia or a resident of the United States, as the context requires.

The proposed treaty also contains the standard provision that, unless the context otherwise requires or the competent authorities of the two countries establish a common meaning, all terms are to have the meaning which they have under the applicable tax laws of the country applying the treaty.

ARTICLE 4
RESIDENCE

The assignment of a country of residence is important because the benefits of the proposed treaty generally are available only to a resident of one of the countries as that term is defined in the treaty. Furthermore, double taxation is often avoided by the treaty assigning one of the countries as the country of residence where under the laws of the countries the person is a resident of both.

Under U.S. law, residence of an individual is important because a resident alien is taxed on his worldwide income, while a nonresident alien is taxed only on U.S. source income and on his income that is effectively connected with a U.S. trade or business. The Code, however, does not define the term "residence." Instead, IRS regulations state that an alien is a resident of the United States if he is actually present in the United States and is not a mere transient or sojourner. Whether he is a transient is determined by his intentions as to the length and nature of his stay. (See Treas. Reg. sec. 1.871-2(b).) A company is resident in the United States if it is organized in the United States.

The proposed treaty defines "resident of Australia" to include any Australian corporation (as defined in Article 3 so as to exclude corporations with dual residence). The definition also includes any other person (other than a company, as defined in the Australian [13] tax law) who is a resident of Australia under Australian tax law. However, two categories of persons are treated as residents of Australia only to a limited extent (described below). These two categories of persons are (1) persons who are subject to Australian tax only on Australian source income (including certain residents of Australian territories), and (2) partnerships, estates, and trusts (other than certain charitable and employee-benefit trusts). Persons in these two categories are treated as Australian residents only (1) to the extent that the income they derive is subject to Australian tax as the income of an Australian resident, whether in the hands of one of the specified persons or in the hands of a partner in or beneficiary of such a person and, (2) to the extent that their income is exempt from Australian tax solely because it is subject to U.S. tax.

The proposed treaty defines "resident of the United States" to include any United States corporation (as defined in Article 3 so as to exclude corporations with dual residence). The term "resident of the United States" would generally include unincorporated entities treated as U.S. corporations for U.S. tax purposes. Corporations that are not U.S. corporations are not residents of the United States for purposes of the proposed treaty. In addition, the term "resident of the United States" includes any other person that is a U.S. resident for purposes of U.S. tax law. However, a partnership, estate, or trust will be considered to be a U.S. resident only (1) to the extent that the income it derives is subject to U.S. tax, either in its hands or in the hands of its partners or beneficiaries, as the income of a U.S. resident and (2) to the extent that its income is exempt from U.S. tax for reasons other than nonresidency (e.g., as an exempt organization under section 501(c)(3) of the Code or as a qualifying pension trust under section 401(a)). For example, if the share of U.S. residents in the profits of a U.S. partnership is only one-half, Australia would have to reduce its withholding tax on only half of the Australian source income paid to the partnership.

This provision of the proposed treaty is generally based on the fiscal domicile article of the U.S. model and OECD model tax treaties and is similar to the provisions found in other U.S. tax treaties. Consistent with most U.S. income tax treaties, citizenship alone does not establish residence. As a result, U.S. citizens residing overseas are not entitled to the benefits of the treaty as U.S. residents. This result is contrary to U.S. treaty policy as expressed in the U.S. model. The U.S. position is achieved in very few treaties.

A set of "tie-breaking" rules is provided to determine residence in the case of an individual who, under the basic treaty definition, would be considered to be a resident of both countries. Such a dual resident individual will be deemed for all purposes of the treaty to be a resident of the country in which he maintains his permanent home. In determining an individual's permanent home, regard is to be given to the place where the individual dwells with his family. If this permanent home test is inconclusive (because the individual has a permanent home in both countries or in neither), the individual's residence is deemed to be the country in which he has an habitual abode. If this habitual abode test is in its turn inconclusive, the individual's residence is deemed to be the country with which [14] his personal and economic relations are closer. In determining the country with which such relations are closer, regard is to be given to the individual's citizenship (if he is a citizen of one of the countries). The competent authorities of the United States and Australia are specifically authorized to agree as to with which country an individual has closer personal and economic relations (Article 24 (Mutual Agreement Procedure)).

When the tie-breaking rules described above operate to deem an individual a resident of Australia or of the United States for any taxable year, that individual shall be deemed to be a resident of only that country for that year.

ARTICLE 5
PERMANENT ESTABLISHMENT

The proposed treaty contains a definition of the term "permanent establishment" which, with certain exceptions, follows the pattern of other recent U.S. income tax treaties, the U.S. model, and the OECD model.

The permanent establishment concept is one of the basic devices used in income tax treaties to limit the taxing jurisdiction of the host country and thus mitigate double taxation. Generally, an enterprise that is a resident of one country is not taxable by the other country on its business profits unless those profits are attributable to a permanent establishment of the resident in the other country. In addition, the reduced rates of, or certain exemptions from, tax provided for dividends, interest, and royalties will apply unless the asset generating the income is effectively connected with the permanent establishment, in which case such items of income are taxed as business profits. U.S. taxation of business profits is discussed under Article 7 (Business Profits).

In general, under the proposed treaty, a permanent establishment is a fixed place of business through which an enterprise engages in business in the other country. A permanent establishment includes a place of management, a branch, an office, a factory, a workshop, a mine, an oil or gas well, a quarry, or other place of extraction of natural resources, and an agricultural, pastoral, or forestry property. It also includes any building site or construction, assembly or installation project, if the site or project lasts for more than 9 months. This 9-month period differs from the 12-month period of the U.S. model treaty. If the site or project lasts for 9 months or less, it does not constitute a permanent establishment. The use of an installation, drilling rig or ship in a country to dredge or for or in connection with exploration for or exploitation of natural resources of the sea-bed and subsoil also gives rise to a permanent establishment if the use in that country is for at least 6 months in any 24 month period. This 6-of-24 months rule differs from the 12-month rule of the U.S. model treaty. If use of an installation, rig or ship does not last as much as 6 months in any 24-month period, that use does not give rise to a permanent establishment. The current treaty does not contain special rules for building sites, etc.

This general rule is modified to provide that a fixed place of business that is used solely for any or all of a number of specified activities will not constitute a permanent establishment. These activities include the use of facilities for storing, displaying, or delivering [15] merchandise belonging to the enterprise or for the maintenance of a stock of goods belonging to the enterprise for storage, display, or delivery, or for processing by another enterprise. These activities also include the maintenance of a fixed place of business for the purchase of goods or merchandise, for the collection of information, for advertising or scientific research, or for any other preparatory or auxiliary activities for the enterprise.

If an enterprise of one country does business in the other country through a person who has, and habitually exercises, the authority to enter into contracts in that other country in the name of the enterprise, then the enterprise will be deemed to have a permanent establishment in the other country. This rule does not apply where the activities of the agent are limited to those activities (described above) such as storage, display, or delivery of merchandise which are excluded from the definition of permanent establishment. The proposed treaty contains the usual provision that the agency rule will not apply if the agent is a broker, general commission agent, or other agent of independent status acting in the ordinary course of its business.

In addition, an enterprise of one country will be deemed to have a permanent establishment in the other country if it maintains in that other country substantial equipment for rental or other purposes for a period exceeding 12 months. This rule does not apply to equipment leased under a hire-purchase agreement. The treaty does not define the term "substantial equipment."

An enterprise of one country will also be deemed to have a permanent establishment in the other country if it engages in supervisory activities in that other country for more than 9 months in any 24-month period in connection with a building site or construction, assembly or installation project in that other country. This 9-of-24-months rule for such supervisory activities contrasts with the 9-months-of-existence rule, described above, for the maintenance of such a site or project. There is no special rule for such supervisory activities in the U.S. model treaty.

In certain cases described below, an enterprise of one country will also be deemed to have a permanent establishment in the other country if it owns goods or merchandise that a second enterprise subjects to substantial processing in that other country after the first enterprise either (1) bought them in that other country (if the goods or merchandise were not subjected to prior substantial processing outside that other country), or (2) produced them in that other country (or if the goods were produced for the enterprise in question in that other country). This rule applies only in cases where either the first or the second enterprise participates directly or indirectly in the management, control, or capital of the other, or where the same persons participate directly or indirectly in the management, control, or capital of both enterprises. This rule is not in the U.S. model treaty or the OECD model. As compared to the models, it creates a broader concept of permanent establishment and thus a broader taxing jurisdiction of the country in which certain goods or merchandise were purchased or produced. This rule supplements the power of the competent authorities to include profits of one associated enterprise in the income of another on an arm's-length basis (Article 9).

[16] The determination whether a company of one country has a permanent establishment in the other country is to be made without regard to the fact that the company may be related to a resident of the other country or to a person who engages in business in that other country. The relationship is thus not relevant; only the activities of the company being tested are relevant.

The provisions described above are to be applied to determine, for purposes of the treaty, whether an enterprise of a country other than Australia or the United States has a permanent establishment in Australia or the United States, and whether an Australian or U.S. enterprise has a permanent establishment in a third country.

ARTICLE 6
INCOME FROM REAL PROPERTY

This article covers income from owning real property. The rules governing income from the sale of real property are in Article 13.

Under the proposed treaty, income from real property may be taxed in the country where the real property is located. For purposes of the treaty, real property in a country will include leasehold interests in land (whether or not improved) located in that country. In addition, real property in a country will include rights to exploit or to explore for natural resouces situated or sought in that country. Thus, income from real property will include royalties and other payments in respect of the exploitation of natural resources (e.g., oil). It does not include interest on loans secured by real property.

Certain U.S. treaties and the current U.S. model treaty permit residents of one country to elect to be taxed on income from real property in the other country on a net basis. The proposed treaty does not contain that election, but such an election is provided for United States real property income under the Code (secs. 871(d) and 882(d)), and Australia taxes income from real property on a net basis. Also, certain treaties limit the tax a country may impose on rental or royalty income from real property. There is no limit in the proposed treaty.

Under Article 13 (Alienation of Property), gains on the sale, exchange or other disposition of real property (and shares of certain corporations owning real property) may also be taxed by the country where the property is located.

ARTICLE 7
BUSINESS PROFITS

U.S. Code rules

United States law distinguishes between the business income and the investment income of a nonresident alien or foreign corporation. A nonresident alien or foreign corporation is subject to a flat 30 percent rate (or lower treaty rate) of tax on certain U.S. source income if that income is not effectively connected with the conduct of a trade or business within the United States. The regular individual or corporate rates apply to income (from any source) which is effectively connected with the conduct of a trade or business within the United States.

The taxation of income as business or investment income varies depending upon whether the income is U.S. or foreign. In general, U.S. source periodic income (such as interest, dividends, rents and wages) and U.S. source capital gains are effectively connected with [17] the conduct of a trade or business within the United States only if the asset generating the income is used in or held for use in the conduct of the trade or business, or if the activities of the trade or business were a material factor in the realization of the income. All other U.S. source income of a person engaged in a trade or business in the United States is treated as effectively connected income.

Foreign source income is effectively connected income only if the foreign person has an office or other fixed place of business in the United States and the income is attributable to that place of business. Only three types of foreign source income can be effectively connected income: rents and royalties derived from the active conduct of a licensing business;

dividends, interest, or gain from stock or debt derived in the active conduct of a banking, financing or similar business in the United States; and certain sales income attributable to a United States sales office.

Except in the case of a dealer, trading in stocks, securities or commodities in the United States for one's own account does not constitute a trade or business in the United States and accordingly income from those activities is not taxed by the United States as business income. This concept includes trading through a U.S. based employee, a resident broker, commission agent, custodian or other agent or trading by a foreign person physically present in the United States.

Proposed treaty rules

Under the proposed treaty, business profits of an enterprise of one country are taxable in the other country only to the extent they are attributable to a permanent establishment in the other country through which the enterprise carries on business. This is one of the basic limitations on a country's right to tax income of a resident of the other country.

The taxation of business profits under the proposed treaty differs from United States rules for taxing business profits primarily by requiring more than merely being engaged in trade or business before a country can tax business profits and by substituting the "attributable to" standard for the Code's "effectively connected" standard. Under the Internal Revenue Code, all that is necessary for effectively connected business profits to be taxed is that a trade or business be carried on in the United States. Under the proposed treaty, on the other hand, some level of fixed place of business must be present and the business profits must be attributable to that fixed place of business.

The business profits of a permanent establishment are determined on an arm's-length basis. Thus, there is to be attributed to a permanent establishment the business profits which would reasonably be expected to have been derived by it if it were a distinct and independent entity engaged in the same or similar activities under the same or similar conditions and dealing at arm's-length with the enterprise of which it is a permanent establishment, or with any other enterprise with which it deals. Thus, for example, this arm's-length rule applies to transactions between the permanent establishment and a branch of the resident enterprise located in a third country. Amounts may be attributed whether they are from sources within or without the country in which the permanent establishment is located.

[18] In computing taxable business profits, deductions are allowed for expenses, wherever incurred, which are reasonably connected with those profits. These deductions include a reasonable allocation of executive and general administrative expenses and other expenses. Thus, for example, a U.S. company which has a branch office in Australia but which has its head office in the United States will, in computing the Australian tax liability of the branch, be entitled to deduct the executive, general administrative and other expenses incurred in the United States by the head office that are reasonably connected with the profits of the Australian branch. However, no expenses (wherever incurred) are to be deductible unless they would be deductible if the permanent establishment were an independent entity that paid them.

Unlike some U.S. treaties and the U.S. model, the proposed treaty does not define the term "business profits." Thus, to the extent not dealt with in other Articles, the term will be defined under the law of the two countries. If the definitions cause double taxation, the competent authorities could agree on a common meaning of the term.

Business profits will not be attributed to a permanent establishment merely by reason of the purchase of merchandise by a permanent establishment for the account of the enterprise. Thus, where a permanent establishment purchases goods for its head office, the business profits attributed to the permanent establishment with respect to its other activities will not be increased by a profit element in its purchasing activities.

The amount of profits attributable to a permanent establishment must be determined by the same method each year unless there is good and sufficient reason to change the method.

Where business profits include items of income which are dealt with separately in other articles of the treaty, those other articles, and not this Business Profits Article, will govern the treatment of those items of income. Thus, for example, film rentals are generally taxed under the provisions of Article 12 (Royalties), and not as business profits.

The proposed treaty contains a provision, not generally found in other treaties, that permits a country to determine the tax liability of a person under internal law where the information available to the competent authority of that country is inadequate to determine the profits attributable to a permanent establishment. However, on the basis of available information, the determination of the profits of the permanent establishment must be consistent with the principles of the Article.

The proposed treaty allows either country to continue to tax persons carrying on an insurance business under its internal law rather than under the treaty's business profits rules. This exception from treaty coverage continues so long as the law relating to insurance taxation in effect on the date of signature of the convention is not changed other than in minor respects that do not affect its general character.

ARTICLE 8
SHIPPING AND AIR TRANSPORT

As a general rule, the United States taxes the U.S. source income of a foreign person from the operation of ships or aircraft [19] to or from the United States. An exemption from U.S. tax is provided if the ship or aircraft is documented under the laws of a foreign country that grants an equivalent exemption to U.S. citizens and corporations. The United States has entered into agreements with a number of countries under which that country grants an exemption which results in the United States exempting that country's shipping.

The proposed treaty provides that profits which are derived by a resident of one country from the operation of ships or aircraft in international traffic ("shipping profits") shall be exempt from tax by the other country. International traffic means any tranportation by ship or aircraft, except where the transportation is solely between places in one of the countries (Article 3(1)(d) (General Definitions)). The proposed treaty also provides, in Article 8(3), that profits derived from the carriage by ships or aircraft of passengers, livestock, mail, goods or merchandise shipped in one country for discharge at another place in that country are not profits from international traffic and may be taxed in that country. This provision in Article 8(3) largely duplicates the effect of the definition of international traffic in Article 3(1)(d).

This exemption applies even if the ship or aircraft is not registered in either country. Thus, for example, income of a U.S. resident from the operation of a ship flying, for example, the Liberian flag would not be subject to Australian tax. This exemption based solely on residence is a liberalization of the rule in the present treaty that generally provides for an exemption only if the ship or aircraft is registered in the country of residence (or, in the case of the United States, corporate organization or citizenship) of the operator. The exemption also applies to income derived from the operation of ships and aircraft in international traffic through participation in a pool service, a joint transportation operating organization or an international operating agency.

Under the proposed treaty, certain profits from the rental of ships or aircraft would be exempt from tax in the country not the residence of the lessor as profits from the operation of ships and aircraft in international traffic. The rules governing the availability of the exemption differ according to whether the rental occurs on a full basis or a bare boat basis. (Rental on a full or bare boat basis refers to whether the ships or aircraft are leased fully equipped, manned and supplied or not.)

The proposed treaty exempts from tax (as shipping and aircraft income) a narrower category of leasing income than the U.S. model treaty exempts. Income from leasing ships or aircraft on a full basis is exempt under the proposed treaty if the ship or aircraft is operated by the lessee in international traffic and if the lessor either operates ships or aircraft otherwise than solely between places in the country not of his residence or regularly leases ships or aircraft on a full basis. Profits from the lease of ships or aircraft on a bare boat basis (or of containers and related equipment) for operation or use by the lessee in international traffic are shipping profits exempt under the treaty if the lease is merely incidental to the operation of ships and aircraft in international traffic by the lessor. Under the U.S. model treaty, income from leasing ships or aircraft (on a full or bare boat basis) is exempt if the lessee operates the ships or aircraft in international traffic or if the profits are incidental to other shipping or transport profits. The U.S. model treaty generally does not condition the exemption of container leasing income on any other activity of the lessor.

ARTICLE 9
ASSOCIATED ENTERPRISES

The proposed treaty, like most other U.S. tax treaties, contains an arm's-length pricing provision similar to section 482 of the Internal Revenue Code, which recognizes the right of each country to make an allocation of income to that country in the case of transactions between related enterprises, if an allocation is necessary to reflect the conditions and arrangements which would have been made between independent enterprises.

For purposes of the proposed treaty an enterprise of one country is related to an enterprise of the other country if one of the enterprises participates directly or indirectly in the management, control or capital of the other enterprise. The enterprises are also related if the same persons participate directly or indirectly in the management, control, or capital of both enterprises.

When a redetermination of tax liability has been properly made by one country, the other country will make an appropriate adjustment to the amount of tax paid in that country on the redetermined income. In making that adjustment due regard is to be given to other provisions of the treaty and the competent authorities of the two countries will consult with each other if necessary. To avoid double taxation, the proposed treaty's saving clause retaining full taxing jurisdiction in the country of residence or citizenship will not apply in the case of such adjustments.

These provisions of the proposed treaty are not intended to affect the application of any law in either country that relates to the determination of the tax liability of a person. This provision makes it clear that the U.S. retains the right to apply its intercompany pricing rules (section 482) and its rules relating to the allocation of deductions (sections 861, 862, and 863, and Treas. Reg. Section 1.861–8). Moreover, these provisions are not to supersede U.S. or Australian law relating to determinations in cases where the information available to the competent authority is inadequate to determine the income to be attributed to an enterprise, so long as the competent authority proceeds on the basis of available information consistently with these rules. Thus, the treaty does not affect the U.S. rule that the burden of proof is on the taxpayer.

ARTICLE 10
DIVIDENDS

The United States imposes a 30-percent tax on the gross amount of U.S. source dividends paid to nonresident alien individuals and foreign corporations. The 30-percent tax does not apply if the foreign recipient is engaged in a trade or business in the United States and the dividends are effectively connected with that trade or business. In such a case, the foreign recipient is subject to U.S. tax like a U.S. person at the standard graduated rates on a net basis. U.S. source dividends are dividends paid by a U.S. corporation, and certain dividends paid by a foreign corporation if at least 50 percent of the gross income of the foreign corporation, in the [21] prior three year period, was effectively connected with a U.S. trade or business of that foreign corporation.

Under the proposed treaty, dividends paid by a company that is a resident of one country, and to which a resident of the other country is beneficially entitled, may be taxed by both countries. However, the rate of tax that the country of which the payor is a resident may impose is limited to 15 percent of the gross amount of the dividends. This 15-percent rate is the rate found in the existing treaty with Australia. The current statutory rate in Australia is 30 percent. The proposed treaty's 15 percent rate is greater than the five-percent rate found in many U.S. treaties and the U.S. model with respect to dividends on direct investment, but Australia has not to date agreed to any treaty providing a lower rate.

The proposed treaty defines dividends as income from shares. Dividends also include income from other corporate rights which are taxed by the country in which the distributing corporation is resident in the same manner as income from shares. Under this provision, each country may apply its rules for determining when a payment by a resident company is on a debt obligation or an equity interest. Thus, for example, the United States could apply its section 385 rules for determining whether an interest is debt or equity.

The reduced rates of tax on dividends will apply unless the recipient has a permanent establishment (or fixed base in the case of an individual performing independent personal services) in the source country and the shareholdings on which the dividends are paid are effectively connected with the permanent establishment (or fixed base). Dividends effectively connected with a permanent establishment are to be taxed on a net basis as business profits (Article 7). Dividends effectively connected with a fixed base are to be taxed on a net basis as income from the performance of independent personal services (Article 14).

One country may not tax dividends paid by a company resident in the other country except in three cases: first, where a resident of the first country is beneficially entitled to the dividends; second, where the shares in respect of which the dividends are paid are effectively connected with a permanent establishment or a fixed base of the beneficial owner of the dividends in the taxing country; and third, where at least 50 percent of the paying company's gross income was attributable to one or more permanent establishments in the taxing country. In this last situation, however, the tax can be imposed only to the extent the dividends are paid out of the profits attributable to those permanent establishments and only if the country does not impose a tax not covered by the treaty (other than the U.S. accumulated earnings tax or personal holding company tax) such as the branch profits tax described in the following paragraph. The United States does not now impose a branch profits tax or similar tax, while Australia does. Thus, the United States, but not Australia, would now be authorized to tax dividends under this third (50 percent of gross income) provision. Under this provision, the rate of tax on the taxable portion is limited to the 15-percent withholding rate applicable to dividends. This third provision enables the United States to continue to tax dividends paid by foreign corporations doing substantial business in the United States. [22] The provision is, however, different from the U.S. rules because the proposed treaty's permanent establishment concept is more limited than the U.S. trade or business concept. (See discussion in Article 7 (Business Profits).)

The proposed treaty also reserves the right of the United States or Australia to impose a tax (such as a branch profits tax) on a source basis in addition to the regular corporate tax imposed on a permanent establishment maintained there on the earnings of such a permanent establishment. A country could impose such a tax under the proposed treaty only if it did not impose a tax on dividends on the ground that at least 50 percent of the paying company's gross income was attributable to one or more permanent establishments in the taxing country. The rate of tax is limited to 15 percent of net earnings after the ordinary income tax. (With the current 46 percent tax rate effective in Australia, this limitation is equivalent to a rate of 8.1 percent of pretax earnings.) The purpose of this provision is to permit Australia, subject to the special limitations, to continue to impose its so-called branch profits tax. The Australian tax is currently imposed at the rate of 5 percent of certain pre-tax Australian source income of a nonresident of Australia, whether or not that nonresident is a branch of a foreign corporation. The United States does not impose such a tax. This tax, like the U.S. withholding tax on certain dividends of foreign corporations that are attributable to a U.S. trade or business, serves as a substitute, as to the branch operations of foreign corporations, for the withholding tax imposed on payments by domestic subsidiaries to their foreign parents.

Australia imposes an undistributed profits tax on the retained earnings of private companies, generally those not listed on stock exchanges and 75 percent of whose beneficial ownership (or whose parent company's beneficial ownership) is in the hands of a small number of persons. Under the proposed treaty, Australia would grant some relief to private U.S. companies with undistributed Australian profits. Australia, under the proposed treaty, would have to calculate this undistributed profits tax on private companies that are U.S. residents as if those companies were not liable for the branch profits tax discussed above and as if those companies had paid dividends in such amounts that the withholding tax due on those dividends would equal the branch profits tax. For example, a U.S. resident private company earning $100 of Australian income would be subject to a regular Australian corporate tax of $46 and a branch profits tax of $5. Calculating the undistributed profits tax as if no branch profits tax were due would result in $54 (rather than $49) being treated as after-tax income. The branch profits tax of $5 equals the 15 percent withholding tax if that latter tax were applied to the amount of $33.33. Therefore, the undistributed profits tax would apply to $20.67 ($54–$33.33).

The treaty would allow the United States to adopt the Australian type of branch profits tax, subject to the same rules that apply to Australia.

ARTICLE 11
INTEREST

The United States imposes a 30-percent tax on U.S. source interest paid to foreign persons under the same rules that are applicable [23] to dividends. Under the Code, U.S. source interest generally is interest on debt obligations of U.S. persons, but not interest on deposits in banks. U.S. source interest also includes interest paid by a foreign corporation if at least 50 percent of the gross income of the foreign corporation, in the prior three year period, was effectively connected with a U.S. trade or business of that corporation.

Under the proposed treaty, interest may be taxed by a country if the beneficial owner of the interest is a resident of that country, the interest arose in that country, or the indebtedness to which the interest relates is effectively connected with a permanent establishment or fixed base of the beneficial owner of the interest in that country. The proposed treaty limits the withholding tax imposed by reason of source to 10 percent generally. The present treaty does not limit the withholding tax on interest, although the current Australian statutory rate of withholding tax is 10 percent. The U.S. model treaty provides for elimination of the withholding tax on portfolio interest (a zero rate), although this result is rarely achieved. The limitation in the proposed treaty applies only if the interest is beneficially owned by a resident of the other country; it does not apply if the recipient is a nominee for a nonresident.

The reduced tax rate will not apply if the recipient has a permanent establishment or fixed base in the source country and the debt claim is effectively connected with that permanent establishment or fixed base. In that event, the interest will be taxed as business profits (Article 7) or income from the performance of independent personal services (Article 14).

The proposed treaty addresses the issue of non-arm's-length interest charges between parties having a special relationship by providing that the amount of interest for purposes of the treaty will be the amount of arm's-length interest. The amount of interest in excess of the arm's-length interest will be taxable according to the laws of each country, taking into account the other provisions of this treaty (e.g., excess interest paid to a parent corporation may be treated as a dividend under local law and thus entitled to the benefits of Article 10 of this treaty).

The proposed treaty defines interest to include any income treated under the tax law of the source country as interest. Under this provision, each country may apply its rules for determining when a payment by a resident company is on a debt obligation or an equity interest. Thus, the United States could apply its section 385 rules for determining whether an interest is debt or equity.

The proposed treaty provides a source rule for interest (which is also used in Article 22 (Relief from Double Taxation) for foreign tax credit purposes). Interest will be sourced within a country if the payor is the government of that country, including political subdivisions and local authorities, or a resident of that country. Generally, this is consistent with U.S. source rules (section 861–862) which provide that interest income is sourced in the country in which the payor is resident. However, if the interest is borne by a permanent establishment (or fixed base) that the payor has in a country other than his country of residence and the indebtedness was incurred with respect to that permanent establishment (or fixed base), interest will be sourced in that country, regardless of the residence of the payor. Thus, for example, if an Australian resident [24] has a permanent establishment in France and that Australian resident incurs indebtedness to a U.S. person for that French permanent establishment, and the permanent establishment bears the interest, then the interest will, for purposes of the proposed treaty, have its source in France and Australia will not tax the interest.

Australian law now exempts from tax payments of interest to foreign governments and their agencies (including payments to the Export-Import Bank). The treaty does not guarantee that such exemption will continue.

ARTICLE 12
ROYALTIES

Under the same system that applies to dividends and interest, the United States imposes a 30-percent tax on U.S. source royalties paid to foreign persons. Royalties are from U.S. sources if they are for the use of property located in the United States. U.S. source royalties include royalties for the use of or the right to use intangibles in the United States. Such royalties include motion picture royalties.

The present treaty with Australia does not generally limit source country taxation of royalties. The present treaty exempts from source country taxation, however, royalties from the use of copyrights of literary, dramatic, musical, or artistic works, but does not limit source country taxation of royalties for motion pictures, videotapes, and the like.

Australia subjects royalties paid by Australian residents to U.S. persons (that are not exempt under the present treaty) to withholding of 51 percent of the gross royalty. This withholding provision is an enforcement mechanism for the income tax on royalties, which Australia imposes at the rate of 51 percent of the net royalty. (The 51 percent rates represent the sum of the regular corporate tax rate, 46 percent, and the rate of an additional tax (the "branch profits tax"), 5 percent, imposed on certain income from Australian sources earned by foreign persons.) Absent proof that expenses are associated with the royalty income and thus that the gross royalty and the net royalty are different, the U.S. recipient of the royalty is generally subject under the present treaty to tax at the rate of 51 percent of the gross royalty. Such proof has sometimes been difficult for U.S. taxpayers to supply. When the U.S. taxpayer cannot supply adequate proof, it pays Australian tax at the rate of 51 percent of the gross royalty. A special Australian statutory rate of 10 percent of the gross royalty applies to royalties received by nonresidents of Australia for the right to use motion picture or television films, videotapes, or related copyrights or advertising materials, however.

The proposed treaty provides for a limitation of the rate of source basis taxation of royalties. Royalties from source (under the royalty source rule discussed below) in one country that are beneficially owned by a resident of the other country may be taxed by both countries. However, the withholding tax imposed in the source country may not exceed 10 percent of the gross royalty. As noted above, the present treaty exempts from source country taxation only certain royalties, while allowing full source country taxation of most kinds of royalties (currently up to 51 percent of the gross amount in the case of Australia). Although the bulk of Australian [25] source royalty income would be subject to a lower rate of withholding tax under the proposed treaty than under the present treaty, certain copyright income that is exempt under the present treaty would be subject to taxation (at up to the 10-percent rate) under the proposed treaty. The 10-percent rate limitation in the proposed treaty applies only if the royalty is beneficially owned by a resident of the other country; it does not apply if the recipient is a nominee for a nonresident.

In certain cases, under the proposed treaty, income from leasing of ships, aircraft, and containers would be royalties subject to withholding tax at the source of up to 10 percent of gross receipts if the lessor had no permanent establishment in the source country (see Article 8 (Shipping and Air Transport)).

The U.S. model treaty exempts royalties from tax at source.

The reduced withholding tax rate does not apply where the beneficial owner has a permanent establishment in the source country or performs personal services in an independent capacity through a fixed base in the source country, and the property giving rise to the royalties is effectively connected with the permanent establishment or fixed base. In that event the royalties will be taxed as business profits (Article 7) or income from the performance of independent personal service (Article 14).

Royalties are defined as payments or credits for the use of, or the right to use, copyrights, patents, designs, models, plans, secret processes or formulae, trademarks or other similar property or rights. Royalties also include payments or credits for the use of, or the right to use, industrial, commercial, or scientific equipment (not leased under a hire-purchase agreement), motion picture films, films or video tapes for television use, and audio tapes for radio use. In addition, royalties include payments or credits for the supply of scientific, technical, industrial or commercial knowledge or information owned by any person, the supply of any ancillary and subsidiary assistance furnished to enable the application or enjoyment of such knowledge or of any other property or right to which this article applies, or any forbearance in respect of any such property or right. Thus, payments for the royalty-free use of a copyright or patent could be considered to involve a royalty. In addition, income from the disposition of any property or right described above constitutes royalty income to the extent that the amounts realized on the disposition are contingent on the productivity, use, or further disposition of such property or right.

The proposed treaty provides that in the case of royalty payments or credits between persons having a special relationship, only that portion of the payment or credit that represents an arm's-length royalty will be treated as a royalty under the treaty. Payments in excess of the arm's-length amount will be taxable according to the law of each country with due regard being given for the other provisions of the treaty. Thus, for example, any excess amount might be treated as a dividend subject to the taxing limitations of Article 10.

The proposed treaty provides special source rules for royalties. Generally, under U.S. tax rules (section 861–862) royalty income is sourced where the property or right is being used. The proposed treaty alters this rule in certain cases. If a royalty is paid by the [26] government of one of the countries, including political subdivisions and local authorities, or by a resident of one of the countries, then the income will generally be sourced in the country of residence of the payor. However, if the payor has a permanent establishment or fixed base in a country in connection with which the obligation to pay the royalty was incurred, and if the royalties are borne by the permanent establishment or fixed base, the royalties arise (for purposes of the proposed treaty) in the country in which the permanent establishment or fixed base is situated. Finally, if the above rules do not result in a U.S. or Australian source for the royalties, and if the royalties relate to the use of or the right to use rights or property in either the United States or Australia, then the source of the royalties will be that country.

ARTICLE 13
ALIENATION OF PROPERTY

Generally, gain realized by a nonresident alien or a foreign corporation from the sale of a capital asset is not subject to U.S. tax unless the gain is effectively connected with the conduct of a U.S. trade or business or, in the case of a nonresident alien, he is physically present in the United States for at least 183 days in the taxable year. However, under the Foreign Investment in Real Property Tax Act of 1980, as amended, a nonresident alien or foreign corporation is taxed by the United States on gain from the sale of a U.S. real property interest as if the gain were effectively connected with a trade or business conducted in the United States. A U.S. real property interest includes corporations holding U.S. real property.

Under the proposed treaty gains from the disposition of real property may be taxed in the country where the real property is situated. The proposed treaty defines real property situated in the United States and real property situated in Australia separately. Real property situated in the United States includes real property located here for the purposes of Article 6. It also includes United States real property interests. This definition allows the United States to tax any transaction of an Australian resident taxable under the Foreign Investment in Real Property Tax Act of 1980.

Real property situated in Australia includes any property that is real property under Australian law, as that law changes from time to time. Without limiting the broad reach of the Australian law test, the proposed treaty specifically includes in the definition of real property situated in Australia three categories of property: real property located there for the purposes of Article 6; shares (or comparable interests) in a company whose assets are wholly or principally Australian real property; and an interest in a partnership, trust, or estate whose assets are wholly or principally Australian real property. Such shares and interests are deemed to be situated in Australia, wherever the entity was created or is operated, and wherever any shares or other evidences of ownership may be found. The proposed treaty does not define the term "principally."

Gains from the sale or exchange of ships, aircraft or containers operated or used by an enterprise of one country in international traffic are taxable only by the country of residence. However, the other country (not the country of residence) may tax the gain to the extent that it allowed depreciation to that enterprise in respect [27] of such items. Thus, that country may recapture that depreciation. Gains from dispositions of property or rights that are subject to tax under the royalty article (Article 12) as contingent on productivity, use, or further disposition are taxable only under that article; that is, the source country tax is generally limited to 10 percent of the gross amount.

The U.S. model treaty generally allows the country that is not the country of residence to tax gains from dispositions of only enumerated property (such as real property located in that country or personal property attributable to a permanent establishment or fixed base in that country). Under the model treaty, gains from dispositions of other property are taxable only in the country of residence. The proposed treaty does not provide such a restriction. Therefore, gains from dispositions of property not mentioned in this article are subject to the general rule of Article 21 (Income Not Expressly Mentioned), which provides that income from sources within a country may be taxed in that country.

ARTICLE 14
INDEPENDENT PERSONAL SERVICES

The United States taxes the income of a nonresident alien at the regular graduated rates if the income is effectively connected with the conduct of a trade or business in the United States by the individual. (See discussion of U.S. taxation of business profits under Article 7 (Business Profits).) The performance of personal services within the United States can be a trade or business within the United States (sec. 864(b)).

The proposed treaty limits the right of a country to tax income from the performance of personal services by a resident of the other country. Under the proposed treaty, income from the performance of independent personal services is treated separately from income from the performance of personal services as an employee.

Income from the performance of independent personal services (i.e., services performed as an independent contractor, not as an employee) in one country by a resident of the other country is exempt from tax in the country where the services are performed, unless (1) the person performing the personal services is present in the country where the services are performed for more than 183 days during the taxable year or (2) the individual has a fixed base regularly available to him in that country for the purpose of performing the services. In the second situation, the source country can tax only that portion of the individual's income which is attributable to the fixed base.

Independent personal services include all independent activities, not merely those of persons in professions such as physicians, lawyers, engineers, architects, dentists, and accountants.

The proposed treaty provides a broader exemption from tax than the present treaty. While the present treaty contains a 183-day rule, it does not exempt income under that rule unless the person performing the services does so for or on behalf of a resident of the country of which he is resident. However, the present treaty does not contain the fixed base rule of the proposed treaty; under the present treaty, a fixed base maintained in a country for the purpose of performing services does not necessarily cause taxation of [28] those services in that country. The U.S. model treaty, by contrast, does not contain a 183-day rule, but rather allows taxation in the source country only on the basis of a fixed base regularly available to the individual performing the independent services.

ARTICLE 15
DEPENDENT PERSONAL SERVICES

Under the Code, the income of a nonresident alien from the performance of personal services in the United States is not taxed if the individual is not in the United States for at least 90 days during a taxable year, the compensation does not exceed $3,000, and the services are performed as an employee of a foreign person not engaged in a trade or business in the United States or they are performed for a foreign permanent establishment of a U.S. person.

Under the proposed treaty, income from services performed as an employee or as a director of a company in one country (the source country) by a resident of the other country will be taxable only in the country of residence if three requirements are met: (1) the individual is present in the source country for fewer than 184 days during the taxable year; (2) his employer or company is not a resident of the source country; and (3) the compensation is not deductible by a permanent establishment, fixed base or a trade or business of the employer in the source country.

Compensation derived by an employee aboard a ship or aircraft operated by a resident of one country in international traffic may be taxed by that country.

This article is modified in some respects for pensions (Article 18) and for compensation as a government employee (Article 19).

The present treaty does not distinguish between dependent and independent personal services. The present treaty rules are discussed in the discussion of Article 14, above. In addition, the present treaty contains a special rule for teachers that allows visits of up to two years duration without subjecting the visiting teacher to taxation in the country he visits. Under the proposed treaty, as in the U.S. model, teachers who perform dependent personal services will be subject to the general rules for employees.

ARTICLE 16
LIMITATION ON BENEFITS

The proposed treaty contains a provision which is intended to limit the benefits of the treaty to persons who are entitled to those benefits by reason of their residence in the United States or Australia.

The proposed treaty is intended to limit double taxation caused by the interaction of the tax systems of the United States and Australia as they apply to residents of the two countries. At times, however, residents of third countries attempt to use a treaty. Such use is known as "treaty shopping", and refers to the situation where a person who is not a resident of either country seeks certain benefits under the income tax treaty between the two countries. Under certain circumstances, and without appropriate safeguards, the nonresident is able indirectly to secure these benefits by establishing a corporation (or other entity) in one of the countries which as a resident of that country, is entitled to the benefits of the treaty. Additionally, it may be possible for the third country resident to repatriate funds to that third country from the entity [29] under favorable conditions (i.e., it may be possible to reduce or eliminate taxes on the repatriation) either through relaxed tax provisions in the distributing country or by passing the funds through other treaty countries (essentially, continuing to treaty shop), until the funds can be repatriated under favorable terms.

The proposed treaty contains provisions intended to limit the benefits of the treaty to bona fide residents of the two countries. This is accomplished by providig that a person other than an individual (such as a corporation, partnership or trust) is not entitled to the benefits of the convention unless it satifies any one of an ownership test, a public company test, or a good business purpose test. Under the ownership test, more than 75 percent of the beneficial interest (in the case of a company, more than 75 percent of the number of shares of each class of shares) in that entity must be owned directly or indirectly by any combination of one or more individual residents of Australia or the United States, citizens of the United States, publicly traded companies (discussed below), or the governments of the countries (the United States and Australia) themselves. This provision would, for example, deny the benefits of the reduced U.S. withholding tax rates on dividends, interest or royalities to an Australian company that is owned by individual residents of a third country.

Under the public company test, a company that is a resident of one of the countries and that has substantial and regular trading in its principal class of stock on a recognized stock exchange in the United States or Australia is entitled to the benefits of the treaty regardless of where its actual owners reside. In addition, any interest that such a company holds is a qualifying interest under the 75-percent test above. The term "recognized stock exchange" includes the NASDAQ System owned by the National Association of Securities Dealers, Inc. in the United States.

Under the good business purpose test, denial of treaty benefits does not occur if the acquisition, ownership and maintenance of an entity that is a resident of the United States of Australia and the conduct of its operations did not have as one of its principal purposes the purpose of obtaining benefits under the proposed treaty. Accordingly, the provision will not apply if it can be shown that there was no treaty shopping motive for forming the company and if its operation does not have as one of its principal purposes the purpose of obtaining the treaty benefits. Thus the burden of overcoming the treaty shopping rule, as under U.S. tax law generally, is on the taxpayer claiming treaty benefits.

The proposed treaty disallows treaty benefits to any income derived by a trustee that is treated as income of a resident of the United States or Australia for purposes of the treaty if the trustee derived that income in connection with a scheme one of whose principal purposes was to obtain a benefit under the treaty.

ARTICLE 17
ENTERTAINERS

The proposed treaty contains an additional set of rules which apply to the taxation of income earned by entertainers (such as theater, motion pictures, radio or television entertainers, musicians, and athletes). The proposed article supplements the other provisions dealing with the taxation of income from personal services [30] (Articles 14 and 15) and is intended, in part, to prevent entertainers and athletes from using the treaty to avoid paying any tax on their income earned in one of the countries.

Under the Article, one country may tax an entertainer who is a resident of the other country on the income from his personal services as an entertainer in that country during any year in which the gross receipts derived by him such activities, including his reimbursed expenses, exceed $10,000 or its equivalent in Australian dollars. (The comparable amount in the U.S. model treaty is $20,000.) Thus, if an Australian entertainer maintained no fixed base in the United States and performed (as an independent contractor) for two days in one taxable year in the United States for total compensation of $9,000, the United States could not tax that income. If, however, that entertainer's total compensation were $11,000, the full $11,000 (less appropriate deductions) would be subject to U.S. tax. As in the case of the other provisions dealing with personal services income, this provision does not bar the country of residence or, in the case of the United States, the country of citizenship, from also taxing that income (subject to a foreign tax credit).

In addition, the proposed treaty provides that where income in respect of personal services performed by an entertainer or athlete accrues not to the entertainer or athlete but rather to another person or entity, that income will be taxable by the country in which the services are performed in any situation where the entertainer or athlete shares directly or indirectly in the profits of the person or entity receiving the income. (This provision applies notwithstanding Articles 7, 14, and 15.) For this purpose, participation in the profits of the recipient of the income includes the receipt of deferred compensation, bonuses, fees, dividends, partnership distributions, or other distributions. The provision does not apply if it is established that neither the entertainer or athlete, nor related persons, participate directly or indirectly in the profits of the person or entity receiving the income in any manner. This provision is intended to prevent highly paid performers and athletes from avoiding tax in the country in which they perform by routing the compensation for their services through a third person such as a personal holding company or trust located in a country that would not tax the income.

ARTICLE 18
PENSIONS, ANNUITIES, ALIMONY AND CHILD SUPPORT

Under the proposed treaty, pensions and other similar remuneration paid to a resident of either country are subject to tax only in the recipient's country of residence. (This rule does not apply in the case of pensions which are paid to citizens of one country attributable to services performed by the individual for government entities of the other (Article 19 (Governmental Remuneration)).) The term, "pensions and other similar remuneration" is defined to mean periodic payments made by reason of retirement or death, in consideration for services rendered, or as compensation paid after retirement in consideration of injuries received in connection with past employment. Social Security payments and other similar public pension payments paid by one country to a resident of the other country or to a U.S. citizen will be taxable only by the paying [31] country. This rule, which is not overriden by the saving clause, exempts U.S. citizens and residents from U.S. tax on Australian social security payments and Australian residents from Australian tax on U.S. social security payments.

The proposed treaty also provides that annuities may be taxed only by the recipients' country of residence. Annuities are defined as stated sums paid periodically at stated times during life or during a specified or ascertainable number of years, under an obligation to make the payments in return for adequate and full consideration (other than services).

Under the proposed treaty alimony and maintenance payments (including child support payments) are taxable in the source country, but are exempt from residence country taxation. The saving clause does not supersede this rule, so U.S. citizens and residents who receive such Australian source payments would not be subject to U.S. tax on those payments. The U.S. model treaty distinguishes between alimony payments and child support payments. Under the model treaty, alimony payments (and other maintenance payments other than child support payments) are taxable only by the country of residence of the recipient, while child support payments are taxable only by the country of the payor. The child support rule in the U.S. model, like the proposed treaty rule, is not subject to the saving clause.

At present, Australian rules provide that alimony and child support payments are neither deductible to the payor nor income to the recipient.

ARTICLE 19
GOVERNMENTAL REMUNERATION

The proposed treaty contains the standard provision that as a general rule exempts wages of employees of one of the countries from tax in the other country. Under the proposed treaty, compensation paid by one country, its political subdivisions or their agencies or authorities, to one of its citizens for labor or services rendered in the discharge of governmental functions is taxable only by the paying country. Thus, for example, Australia would not tax the compensation of a U.S. citizen who is in Australia to perform services for the U.S. government in the discharge of governmental functions. This rule also applies to pensions paid in respect of past services. This provision is generally excluded from the saving clause for persons who are not citizens of or immigrants in the source country.

This provision of the proposed treaty is similar to the provision of the U.S. model treaty, although the U.S. model provides that the exemption does not apply to remuneration paid for services rendered in connection with a business carried on by one of the countries or by any of their political subdivisions.

ARTICLE 20
STUDENTS

Under the proposed treaty, an individual who is a resident of one country and who is temporarily present as a full-time student in the other country will generally be exempt from tax in the host country on payments from abroad for maintenance or education. This rule also applies to a student who was a resident of one country immediately before visiting the other country. There is no precise [32] limitation on the amount of income to which the exemption applies. The proposed treaty does not define the term "temporarily present." The U.S. model applies this rule to students who are "present" rather than "temporarily present" in the host country. The saving clause does not apply to this article.

ARTICLE 21
INCOME NOT EXPRESSLY MENTIONED

This article is a catch-all article intended to cover items of income not specifically covered in other articles, and to assign the right to tax third country income to only one of the countries. It applies to income from third countries as well as income from the United States and Australia.

As a general rule, items of income not otherwise dealt with in the proposed treaty which are derived by residents of either country shall be taxable only by the country of residence. However, if the income is sourced (or is effectively connected with a permanent establishment) in the other country, it may also be taxed by that country. The source of an item of income is determined under the domestic laws of the two countries unless the treaty contains a special rule. This provision, for example, gives the United States the sole right to tax income sourced in a third country and paid to a resident of the United States. This provision is subject to the saving clause, so U.S. citizens who are Australian residents would continue to be subject to U.S. taxation on their worldwide income.

The proposed treaty would generally allow the source country to tax capital gains of residents of the other country. In this respect, the proposed treaty differs from the U.S. model, which generally allows such source country taxation only in limited circumstances (see discussion under Article 13 (Alienation of Property)).

ARTICLE 22
RELIEF FROM DOUBLE TAXATION

Background

One of the two principal purposes for entering into an income tax treaty is to limit double taxation of income earned by a resident of one of the countries that may be taxed by the other country. The United States seeks unilaterally to mitigate double taxation by generally allowing U.S. taxpayers to credit the foreign income taxes that they pay against the U.S. tax imposed on their foreign source income. A fundamental premise of the foreign tax credit is that it may not offset the U.S. tax on U.S. source income. Therefore, the foreign tax credit provisions contain a limitation that ensures that the foreign tax credit offsets U.S. tax on only foreign source income. This limitation is computed on a worldwide consolidated basis. Hence, all income taxes paid to all foreign countries are combined to offset U.S. taxes on all foreign income. Separate limitations on the foreign tax credit are provided for certain interest and for DISC dividends.

A U.S. corporation that owns 10 percent or more of the voting stock of a foreign corporation may credit foreign taxes paid or deemed paid by that foreign corporation on earnings that are received as dividends (deemed paid credit). These deemed paid taxes are included in the U.S. shareholder's total foreign taxes paid for [33] the year the dividend is received and go into the general pool of taxes to be credited.

Australia has its own set of tax provisions designed to mitigate double taxation unilaterally. In general, Australian residents are exempt from Australian income tax on income from sources in countries other than Australia if that income has been subjected to full taxation in the foreign country. In the case of non-Australian source royalty or interest income that is exempt from foreign income tax or subject to a reduced tax by treaty, and in the case of certain foreign source dividends, however, Australia generally uses a foreign tax credit system to avoid double taxation. A general rule of Australian tax law provides that tax on dividends received by certain corporate residents of Australia from any source is rebated. The rebate is calculated by determining the average rate of tax payable on the company's taxable income and applying that rate to the net income from dividends. This rebate precludes the use of foreign tax credits for the affected dividends.

Unilateral efforts to limit double taxation are imperfect. Because of differences in rules as to when a person may be taxed on business income, a business may be taxed by two countries as if it were engaged in business in both countries. Also, a corporation or individual may be treated as a resident of more than one country and be taxed on a worldwide basis by both.

Part of the double tax problem is dealt with in other articles that limit the right of a source country to tax income, and that coordinate the source rules. This article provides further relief where both Australia and the Untied States will still tax the same item of income. This article is not subject to the saving clause, so that the country of citizenship or residence waives its overriding taxing jurisdiction to the extent that this article applies.

The present treaty generally provides for relief from double taxation by each country permitting a credit against its tax for the appropriate amount of taxes paid to the other country on income from sources within that other country. The credit is provided, however, only to the extent permitted under certain domestic laws.

The proposed treaty provides separate rules for relief from double taxation for the United States and Australia. In addition, it provides special rules covering U.S. citizens resident in Australia.

United States

The proposed treaty contains the provision that the United States will allow a citizen or resident a foreign tax credit for income taxes paid or accrued in Australia. This kind of provision is found in many U.S. treaties. The credit is to be computed in accordance with the provisions of and subject to the limitations of U.S. law (as those provisions and limitations may change from time to time without changing the general principles of the credit). The credit is limited to the amount of tax paid to Australia and cannot exceed the U.S. Code foreign tax credit limitations.

The proposed treaty also allows the U.S. deemed paid credit (section 902) to U.S. corporate shareholders of Australian corporations receiving dividends from those corporations if the U.S. company owns 10 percent or more of the voting stock of the Australian corporation. The credit is allowed for Australian income taxes paid [34] by the Australian corporation on the profits out of which the dividends are paid.

This article provides that Australian income taxes covered by the treaty (Article 2 (Taxes Covered)) are considered income taxes for purposes of the U.S. foreign tax credit. Accordingly, all such Australian taxes will be eligible for the U.S. foreign tax credit. These taxes would probably be creditable for U.S. tax purposes in the absence of the proposed treaty. The treaty's special source rules do not apply for purposes of computing the limitation for other foreign taxes.

Australia

The proposed treaty generally provides that Australia is to credit U.S. taxes paid by Australian residents on U.S. source income. This rule applies to persons who are Australian residents under Australian tax law (i.e., including dual resident companies). This credit is not to exceed the Australian tax payable on the U.S. source income or any class of that income or on income from non-Australian sources. Thus, if the income is exempt from Australian tax under Australian law, no credit is available. The credit is to be in accordance with the provisions and subject to the limitations of Australian law, as that law changes from time to time. The credit is not available for U.S. taxes paid by Australian residents solely because of U.S.

citizenship or solely by reason of an election under U.S. law to be taxed as a U.S. resident.

The proposed treaty provides an exemption-like system for dividends received by certain Australian corporations from U.S. corporations in which they own at least ten percent of the voting power. In accordance with Australian law as of the date of signature of the proposed treaty (August 6, 1982), such a recipient Australian corporation is entitled to a rebate in its tax assessment, at its average rate of tax, of the tax attributable to such dividends received. If, however, Australia changes its internal law so as not to allow this rebate in respect of such dividends. Australia is to allow a deemed-paid foreign tax credit for U.S. tax paid on profits out of which come dividends received by Australian corporations from U.S. corporations in which they are ten-percent shareholders.

The proposed treaty provides a special rule for U.S. citizens who are Australian residents. Such persons are generally entitled to a credit against U.S. tax liability in the amount of the Australian tax paid. Thus, Australia generally would have taxing jurisdiction over the income of such persons as residents of Australia, subject to exemption or a credit with respect to the U.S. tax on U.S. source income. This U.S. tax credit is not to reduce U.S. taxation on a source basis of such a person's U.S. source income.

ARTICLE 23
NONDISCRIMINATION

The proposed treaty contains a nondiscrimination provision relating to the taxes covered by the treaty similar to provisions embodied in other recent U.S. income tax treaties. This nondiscrimination provision differs from other recent treaties and from the U.S. model in that it allows existing practices to continue, and in that it does not cover either U.S. or Australian taxes not generally [35] covered by the proposed treaty or the taxes of States, localities, or other political subdivisions.

In general, under the proposed treaty, one country cannot discriminate by imposing more burdensome taxes (or requirements connected with taxes) on its residents who are citizens of the other country than on its residents who are also its citizens. Similarly, in general, one country cannot impose more burdensome taxes or connected requirements on permanent establishments of residents of the other country than it imposes on its comparable residents. These provisions do not, however, generally require either country to treat nonresidents as it treats residents. Thus, a country need not grant to residents of the other country the personal allowances, reliefs, or deductions for taxation purposes on account of personal status or family responsibilities that it grants to its own residents.

The rule of nondiscrimination also applies to corporations of one country which are owned in whole or in part by residents of the other country. The saving clause (which allows the country of residence or citizenship to tax notwithstanding certain treaty provisions) does not apply to this nondiscrimination article.

Each country is required (subject to the arm's-length pricing rules of Article 9(1) (Associated Enterprises), 11(4) (Interest), and 12(5) (Royalties)) to allow a resident to deduct interest, royalties, and other disbursements paid by the resident to a resident of the other country under the same conditions that it allows deductions for such amounts paid to residents of the same country as the payor.

The provision is not intended to override the right of the United States to tax foreign corporations on their dispositions of a U.S. real property interest because the effect of the provisions imposing the tax is not discriminatory. Also, the provision is not intended to permit foreign corporations to claim the benefit of U.S. provisions intended to eliminate U.S. double tax, such as the dividends received deduction.

The proposed treaty would permit a country to continue any discriminatory tax laws in force on August 6, 1982 (the date of the signing of the treaty), to adopt any later modification of those laws that does not change their general nature, or to adopt any discriminatory laws reasonably designed to prevent tax avoidance or evasion. Any such newly adopted modification or anti-avoidance law generally cannot favor citizens or residents of any third country over citizens or residents of the treaty partner (the United States or Australia) of the country adopting the modification. The proposed treaty does not require that either state extend to residents of the other country benefits granted to residents of a third country by treaty, however.

Although this provision does not comport with the U.S. model treaty, Australia has never agreed to a more comprehensive nondiscrimination rule than that of the proposed treaty.

If the United States or Australia considers that the tax measures of the other country violate this nondiscrimination clause, the countries are to consult together in an endeavor to resolve the matter.

[36] ARTICLE 24
MUTUAL AGREEMENT PROCEDURE

The proposed treaty contains the standard mutual agreement provision which authorizes the competent authorities of the United States and Australia to consult together to attempt to alleviate individual cases of double taxation not in accordance with the proposed treaty. The saving clause of the proposed treaty does not apply to this article, so that the application of this article may result in waiver (otherwise mandated by the proposed treaty) of taxing jurisdiction by the country of citizenship or residence.

Under the proposed article a resident of one country who considers that the action of the countries or either of them will cause him to pay a tax not in accordance with the treaty may present his case to the competent authority of the country of which he is a resident or citizen. The taxpayer must notify this competent authority of his case within three years from the time the taxpayer receives notice of the action he considers improper. The competent authority then makes a determination as to whether the claim has merit. If it is determined that the claim does have merit, that competent authority endeavors to come to an agreement with the competent authority of the other country to limit the taxation which is not in accordance with the provisions of the treaty.

The provision requires the waiver of the statute of limitations of either country so as to permit the issuance of a refund or credit notwithstanding the statute of limitations. The provision, however, does not authorize the imposition of additional taxes after the statute of limitations has run.

A provision directs the competent authorities to seek to resolve any difficulties or doubts arising as to the application of the convention. Specifically, they are authorized to agree to the attribution or allocation of income, deductions, credits, or allowances of an enterprise of one country to its permanent establishment in the other country (or between persons), to the determination of the source of income, to the common meaning of terms, and, for the purpose of determining residence under Article 4, to the country with which an individual has closer personal and economic relations.

The treaty authorizes the competent authorities to communicate with each other directly for purposes of reaching an agreement in the sense of the mutual agreement provision. These provisions make clear that it is not necessary to go through standard diplomatic channels in order to discuss problems arising in the application of the treaty and also removes any doubt as to restrictions that might otherwise arise by reason of the confidentiality rules of the United States or Australia.

ARTICLE 25
EXCHANGE OF INFORMATION

This article forms the basis for cooperation between the two countries in their attempts to deal with avoidance or evasion of their respective taxes and to enable them to obtain information so that they can properly administer the treaty. The proposed treaty provides for the exchange of information which is necessary to carry out the provisions of the proposed treaty or for the prevention of fraud or for the administration of statutory provisions concerning [37] taxes to which the convention applies, so long as the information could be obtained under the tax laws and practices of both countries.

Information exchanged is to be treated as secret, except that it may be disclosed to persons involved in the assessment or collection of, the administration and enforcement in respect of, or litigation concerning, the taxes to which the treaty applies. The information may be used for such purposes only. Persons involved in the administration of taxes include legislative bodies involved in the administration of taxes and their agents such as, for example, the U.S. General Accounting Office, with respect to such information as they consider to be necessary to carry out their oversight responsibilities. A country is not required to supply information the disclosure of which would be contrary to public policy.

Where specifically requested, the requested competent authority will attempt to provide the information in the form requested. Specifically, the competent authority will attempt to provide copies of unedited original documents (including books, papers, statements, records, accounts, or writings) to the extent that they can be obtained under the laws and practices of the requested state in the enforcement of its own tax laws.

A requested country is to use its subpoena or summons powers or any other powers that it has under its own laws to collect information requested by the other country. It is intended that the requested country may use those powers even if the requesting country could not under its own laws. Thus, it is not intended that the provision by strictly reciprocal. For example, once the U.S. Internal Revenue Service has referred a case to the Justice Department for possible criminal prosecution, the United States investigators can no longer use an administrative summons to obtain information. If, however, Australia could still use administrative process to obtain requested information, it would be expected to do so even though the United States cannot. The United States could not, however, tell Australia which of its procedures to use.

Each country will also collect taxes for the other country, but only to the extent necessary to ensure that benefits of the treaty are not going to persons not entitled to those benefits. The provision does not require a country to collect any other taxes of the other country. The collection activities are to be carried out only in accordance with the administrative measures used by the collecting country to collect its own tax, and not in a manner contrary to its sovereignty, security, or public policy. The present treaty contains a similar collection provision.

The U.S. model treaty provides for the exchange of information about all taxes imposed by either country (whether or not otherwise covered by the treaty). The proposed treaty is more limited, applying only for enforcement of the taxes listed in Article 2 as generally covered by the treaty (generally income taxes).

ARTICLE 26
DIPLOMATIC AND CONSULAR PRIVILEGES

The proposed treaty contains the rule found in other U.S. tax treaties that its provisions are not to affect the privileges of diplomatic agents or consular officials under the general rules of international law or the provisions of special agreements. Accordingly, [38] the convention will not defeat the general exemption from tax which a host country may grant to the salary of diplomatic officials of the other country. The saving clause does not apply to this article so that, for example, U.S. diplomats who are considered Australian residents would not be subject to Australian tax.

ARTICLE 27
MISCELLANEOUS

In this article, the proposed treaty provides miscellaneous rules, including primarily source rules for determining when an item of income arises in one of the countries. These source rules are used for the purpose of determining credits and exemptions under the treaty, and for determining source of income under Australian tax law. These source rules do not supersede the U.S. source of income rules for the purpose of internal U.S. law. They are not subject to the treaty's saving clause, however. Thus, the source rules may result in a waiver of taxing jurisdiction by the country of citizenship or residence.

The general source rule is that an item of income of a resident of one country that may be taxed in the other country under the treaty is considered to arise in that other country. Accordingly, income taxes paid to that other country on that income will be creditable (subject to any relevant limitations) in the country of residence.

The general source rule (described above) does not apply to income derived by an Australian resident that is taxable in the United States solely by reason of U.S. citizenship or solely by reason of an election to be treated as a U.S. resident. Such income will not be treated as U.S. source income. Income of a U.S. citizen resident in Australia is to be treated as Australian source income to the extent necessary to implement the special treaty rule of Article 22(4) (Relief from Double Taxation) that allows primary taxing jurisdiction to the United States on the U.S. source income of such a person (but at reduced treaty rates) while allowing primary taxing jurisdiction to Australia on the non-U.S. source income of such a person.

Any exemption from source basis taxation granted by one of the countries under Article 14 (Independent Personal Services), Article 15 (Dependent Personal Services), Article 17 (Entertainers), or Article 19 (Governmental Remuneration) does not apply to the extent that the income exempted under one of those articles is exempt from tax by the other country (the country of residence), whether under internal law or under the proposed treaty. The Internal Revenue Code exempts from U.S. tax certain income earned by U.S. individuals in foreign countries (sec. 911). In certain limited cases, the proposed treaty's denial of the exemption from source basis taxation would allow Australia to tax certain Australian source income of U.S. individuals that would otherwise be exempt under the treaty from Australian tax. Such income not exempt from Australian source-basis taxation would include primarily earnings from personal services of U.S. individuals who remain less than six months in Australia but spend enough time in other foreign countries to qualify under section 911.

[39] ARTICLE 28
ENTRY INTO FORCE

The proposed treaty is subject to ratification in accordance with the applicable procedures of each country and the instruments of ratification will be exchanged as soon as possible in Washington. In general, the proposed treaty will enter into force when the instruments of ratification are exchanged.

As a general rule, the treaty will become effective for taxable years beginning on or after the first day of the second month following the date on which the proposed treaty comes into force. With respect to dividends, interest and royalties that are the subject of the treaty rules under Articles 10, 11, and 12 respectively, the treaty will be effective for amounts paid, credited, or derived on or after the first day of the second month next following the date on which the convention enters into force.

The existing treaty is to be phased out as the proposed treaty becomes effective. When the proposed treaty becomes fully effective, the existing treaty will terminate.

ARTICLE 29
TERMINATION

The proposed treaty will continue in force indefinitely, but either country may terminate it at any time after five years from its entry into force by giving at least six months prior notice through the diplomatic channel.

If termination occurs, the termination will be effective with respect to dividends, interest and royalties (to which Articles 10, 11, or 12 apply) for amounts paid, credited or otherwise derived on or after the first day of January following the expiration of the six months notice. Any termination will be effective with respect to other income for taxable years beginning on or after the first day of January following the expiration of the six months notice.

The proposed treaty contains a special rule allowing either country to terminate one treaty provision in Article 18 (exempting social security payments and other public pension payments from taxation on the basis of residence and citizenship) without terminating any other provision of the treaty. Such partial termination may occur, upon prior notice through the diplomatic channel, at any time after the treaty enters into force.

UNITED STATES TREASURY DEPARTMENT TECHNICAL EXPLANATION OF THE CONVENTION BETWEEN THE GOVERNMENT OF THE UNITED STATES OF AMERICA AND THE GOVERNMENT OF AUSTRALIA FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME

This Convention, signed at Sydney, Australia on August 6, 1982, was negotiated on the basis of the U.S. Model Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital, published in May 1977, the revised U.S. model published in draft form in June 1981 (also referred to as the "U.S. model"), and the Model Double Taxation Convention on Income and Capital published by the Organization for Economic Cooperation and Development (OECD) in January 1977.

The technical explanation is an official guide to the Convention. It reflects policies behind particular Convention provisions, as well as understandings reached with respect to the interpretation and application of the Convention.

ARTICLE 1
PERSONAL SCOPE

This Article identifies the persons who come within the scope of the Convention (also referred to as "the Treaty") and establishes the relationship between it and domestic law.

Paragraph 1 states that, except where the Convention specifically provides otherwise, the Convention applies to residents of the United States and/or Australia. Certain provisions of the Convention may apply to residents of third countries, for example, paragraph 5 of Article 10 (Dividends), paragraph 6 of Article 11 (Interest), and Article 25 (Exchange of Information). The term "resident" is defined in Article 4 (Residence).

Paragraph 2 provides that the Convention may not increase tax above the liability that would result under domestic law or under other agreements between the Contracting States. If domestic law provides a more favorable treatment than the Convention, the taxpayer may apply the provisions of domestic law. For example, if certain interest income derived by nonresidents is exempt from tax by statute, but the treaty authorizes a tax at source of not more than 10 percent, the statutory exemption will apply. A taxpayer, however, may not make inconsistent choices between the rules of the Internal Revenue Code and the Convention rules.

Paragraph 3 contains the traditional "saving clause" under which each Contracting State reserved the right to tax its residents, as defined in Article 4 (Residence), as if the Convention had not come into effect. The two States also reserve the right so to tax their citizens, individuals electing under their respective domestic laws to be taxed as residents, and in the case of the United States, former citizens whose loss of citizenship had as one of its principal purposes the avoidance of tax. Such former citizens are taxable in accordance with section 877 of the Internal Revenue Code for 10 years following the loss of citizenship.

Paragraph 4 sets forth certain exceptions to the application of the saving clause where other provisions of the Convention present overriding policies. The saving clause does not override the benefits provided under paragraph 2 of Article 9 (Associated Enterprises), relating to correlative adjustments of tax liability, or the benefits of paragraphs 2 or 6 of Article 18 (Pensions, Annuities, Alimony and Child Support), relating to social security payments, alimony and child support. Social security payments and similar public pensions paid by Australia and alimony, child support and similar maintenance payments arising in Australia are taxable only by Australia even though the recipient may be a resident of the United States; similarly, social security payments by

Australia to a citizen of the United States, wherever resident, are taxable only in Australia. The benefits provided in Articles 22 (Relief from Double Taxation), 23 (Non-Discrimination), and 24 (Mutual Agreement Procedure), and the source rules of paragraph 1 of Article 27 (Miscellaneous) are also available to residents and citizens of the Contracting States, notwithstanding the saving clause.

In some cases, the saving clause overrides benefits otherwise conferred by the United States on citizens or persons having immigrant status in the United States and benefits otherwise conferred by Australia on citizens or persons ordinarily resident in Australia, but does not override those benefits when conferred on other residents of the respective States. This second category of exceptions to the saving clause concerns the benefits provided under Articles 19 (Governmental Remuneration), 20 (Students) and 26 (Diplomatic and Consular Privileges). The term "immigrant status" means a person admitted to the United States as a permanent resident under U.S. immigration laws (i.e., holding a "green card").

ARTICLE 2
TAXES COVERED

Paragraph 1 enumerates the existing taxes to which the Convention applies in each Contracting State.

In the United States these are the Federal income taxes imposed by the Internal Revenue Code, but excluding the accumulated earnings tax and the personal holding company tax. Social security taxes and excise taxes, such as those on private foundations and foreign insurers, are not covered by the Convention.

In Australia the Convention covers the income tax, including the additional tax on undistributed income of private (closely held) companies.

Paragraph 2 provides that taxes enacted after the date of signature of the Convention (August 6, 1982) are also covered if they are substantially similar to the taxes referred to in paragraph 1. The competent authorities agree to notify each other at the end of each calendar year of substantial changes in their income tax laws or in the official interpretation of those laws or of the Convention.

ARTICLE 3
GENERAL DEFINITIONS

Paragraph 1 defines some of the principal terms used throughout the Convention. Unless the context otherwise requires, the terms defined in this paragraph have a uniform meaning throughout. A number of other important terms are defined in other Treaty articles. For example, the term "resident" is defined in Article 4 (Residence), the term "permanent establishment" is defined in Article 5 (Permanent Establishment), and the term "royalties" is defined in Article 12 (Royalties).

The definitions of the terms "person", "company", "enterprise of a Contracting State", and "international traffic" are similar to the definitions in the U.S. Model.

The "competent authority" for the United States is the Secretary of the Treasury or his delegate, and for Australia the Commissioner of Taxation or his authorized representative.

The definitions of a United States corporation and an Australian corporation, respectively, exclude corporations which under the laws of the Contracting States are residents of both States. A corporation created and organized under the laws of a state of the United States is considered by the United States to be a United States corporation. Such a corporation could also be considered by Australia to be an Australian corporation if it is managed and controlled in Australia or if it does business there and its voting power is controlled by Australian resident shareholders. Typically, a corporation can avoid being a dual resident. If such a situation does arise, the dual resident corporation is not considered a resident of either country for purposes of the Treaty and is therefore not entitled to benefits granted by either State under the Treaty to residents of the other State.

The terms "United States" and "Australia" are defined to include the continental shelf areas of the two countries with respect to exploration and exploitation of their natural resources. For the United States, the definition of the continental shelf is interpreted in accordance with section 638 of the Internal Revenue Code and the regulations thereunder. The term "United States" does not include Puerto Rico, the Virgin Islands, Guam, or any other United States possession. The term "Australia" does include the Territories of Norfolk Island, Christmas Island, the Cocos Islands, Ashmore and Cartier Islands and the Coral Sea Islands; however, see also the discussion of paragraph 1(a)(iii) of Article 4 (Residence).

Definitions are provided for the terms "Contracting State," "State," "United States tax," "Australian tax," and "resident of one of the Contracting States." The covered taxes do not include penalty or interest charges. For example, the ceiling rate of tax at source of 15 percent on dividends under Article 10 (Dividends) does not include any penalty or interest charge for late payment of tax.

Paragraph 2 provides that terms not defined in the Convention shall have the meaning which they have under the laws of the Contracting State concerning the taxes to which the Convention applies, unless the context of the Convention requires a different interpretation. Under the terms of Article 24 (Mutual Agreement Procedure), the competent authorities may agree on a common definition of an otherwise undefined term. The term "context" includes the purpose and background of the provision in which the term appears. An agreement by the competent authorities with respect to the meaning of a term used in the Convention would supersede conflicting meanings in the domestic laws of the Contracting States.

ARTICLE 4
RESIDENCE

This Article sets forth rules for determining the residence of individuals, corporations, and other persons for purposes of the Convention. A definition of residence is important because, for the most part, only residents of the Contracting States may claim benefits under the Convention. The Convention definition is of course, exclusively for purposes of the Convention.

Paragraph 1 of this Article describes those persons who, for purposes of the Convention, are residents of Australia or the United States.

Subparagraph (a) provides that a resident of Australia means an Australian corporation and any other person (except a company that is not an Australian corporation) that is resident in Australia for purposes of its tax. However, if such a person is subject to Australian tax on income from Australian sources (but not on income from U.S. sources or other sources outside Australia), that person is not a resident of Australia for purposes of this Convention except to the extent that the income is subject to tax in Australia as the income of a resident or is exempt from Australian tax solely because it is subject to U.S. tax. This provision excludes residents of certain territories included within the definition of Australia in paragraph 1(k) of Article 3 (General Definitions) from claiming any Treaty reductions in United States tax on United States source income under the Treaty; although subject to Australian tax on their Australian source income, such persons are not subject to Australian tax on their United States source income and the reason is not solely because they are subject to U.S. tax. Similarly, a partnership, estate or trust is a resident of Australia for purposes of the Convention only to the extent that the income it derives is subject to Australian tax as the income of a resident either at the level of the partnership, estate or trust or in the hands of a partner or beneficiary, or, if that income is exempt from Australian tax under the Treaty, it is exempt solely because it is subject to U.S. tax. However, an Australian trust will be considered a resident of Australia, notwithstanding that its income is exempt from Australian tax, if the trust qualifies as a tax-exempt organization under Australian law because it is established for public charitable purposes or scientific research. Thus, a dividend paid by a U.S. corporation to an Australian partnership comprised equally of an Australian resident partner and an Indonesian resident partner would be treated as paid one half to an Australian resident and that half would enjoy the reduced rate of U.S. tax provided for in Article 10 (Dividends).

Subparagraph (b) provides tht a resident of the United States means a U.S. corporation and any other person resident in the United States for purposes of its tax. However, a partnership, estate or trust is a resident of the United States for purposes of the Convention only to the extent that the income it derives either is subject to U.S. tax as the income of a resident (either at the level of the entity or in the hands of a partner or beneficiary), or is exempt from U.S. tax for reasons other than the recipient's not being a U.S. person. Thus, a U.S. person that qualifies as a tax-exempt organization under U.S. law qualifies as a resident, and a recipient of tax-exempt income does not lose its status as a resident with respect to that income. The rule in paragraph 1 that tax-exempt organizations and recipients of tax-exempt income qualify as residents, notwithstanding that the income they derive is not subject to tax, is meant to be a clarification and not to imply that such tax-exempt organizations and other persons are not entitled to treaty benefits under conventions which do not include this or similar language.

Paragraph 2 provides a series of tie-breakers for assigning a single residence to an individual who, by the criteria of paragraph 1, would be a resident of both countries.

The first test is where the individual has a permanent home. If that test is inconclusive because the individual has a permanent home in both countries or in neither of them, the second test is where he has his habitual abode. If that test also fails to establish a single country of residence, because the individual has a habitual abode in both countries or in neither of them, he is deemed to be a resident of the country with which his personal and economic relations are closer. Citizenship, *per se*, is not recognized by Australia as a tie-breaker, but if the individual is a citizen of one of the Contracting States, that factor will be taken into account in determining where his personal and economic relations are closer. If these tests do not establish a single residence, the competent authorities will attempt to settle the question by mutual agreement under Article 24 (Mutual Agreement Procedure). Once an individual is assigned a residence under this paragraph for a taxable year, he is a resident only of that State for all purposes of the Convention for that year.

The residence of persons other than individuals is determined under the respective laws of the Contracting States. A dual resident company is treated as a resident of neither Contracting State for purposes of the convention. (See paragraph 1(g) of Article 3 (General Definitions)).

ARTICLE 5
PERMANENT ESTABLISHMENT

The rule governing the taxation by a Contracting State of business income derived by a resident of the other State utilize the concept of a "permanent establishment." Paragraph 1 of this Article defines in general terms the "permanent establishment" concept, and the following paragraphs give some specific illustrations of the meaning of the term.

A place of management, branch, office, factory, workshop and a place of extraction of natural resources, such as a well or quarry, are examples of a permanent establishment. Since a place of management would in most cases require an office, which is specifically noted in paragraph 2, the addition of that term will not generally cause a permanent establishment to exist where there would not otherwise be one.

A building site or construction or installation project will only be considered a permanent establishment if it lasts longer than 9 months, and an installation, drilling rig or ship used for dredging or exploring or exploiting offshore natural resources is a permanent establishment only if so used for at least 6 months in any 24-month period. In such a case, the site, project, installation, rig or ship constitutes a permanent establishment from the first day when work physically begins within the territory of a Contracting State. A series of contracts or projects which are interdependent both commercially and geographically are to be treated as a single project for the purpose of applying the 9-month and 6-month tests.

Paragraph 3 enumerates certain activities which may be undertaken singly or in combination without creating a permanent establishment. Although subparagraph (f) of this paragraph of the U.S. model was deleted, the same effect is obtained by the insertion of the reference to "one or more" in the introductory language of paragraph 3.

Paragraphs 4(a) and 5 consider the use of agents. A dependent agent who habitually exercises an authority to conclude contracts in the name of an enterprise is deemed to be a permanent establishment of that enterprise except to the extent that his activities are limited to those mentioned in paragraph 3 which would not constitute a permanent establishment under that paragraph. An enterprise of a Contracting State will not be considered to have a permanent establishment in the other State merely because it uses the services of an independent agent acting in the ordinary course of business in that other State.

Subparagraphs (b), (c) and (d) of paragraph 4 specify certain activities which constitute a permanent establishment even if not carried on through a fixed place of business like those enumerated in paragraph 2. Maintaining substantial equipment in a Contracting State for rental or other purposes for longer than 12 months constitutes a permanent establishment unless the equipment is leased under a "hire-purchase" agreement. Under Australian law the lessee under a "hire-purchase" agreement (a lease accompanied by certain lessee purchase options or rights) is treated for tax purposes as the owner of the leased property. The exception for hire-purchase agreements in this Article and elsewhere in the Convention (see Article 12 (Royalties)) was inserted at the request of Australia to distinguish such agreements from leases respected as such for tax purposes. Such a distinction is also made in the Commentary to Article 12 of the OECD Model Convention. Similarly, under the Internal Revenue Code, the terms of a "lease" may be such that for U.S. income tax purposes the lessee is treated as the owner of the property. For purposes of United States tax the exception for "hire-purchase" agreements simply confirms such treatment, which would also apply in the absence of such an explicit exception. See paragraph 2 of Article 3 (General Definitions). Engaging in supervisory activities at a building site or construction, assembly or installation project for more than 9 months in a 24-month period constitutes a permanent establishment. And, an enterprise which maintains goods in the other Contracting State which goods were either purchased there (and not previously processed elsewhere) or produced there by it or in its behalf, and are then substantially processed there by a related enterprise is deemed to have a permanent establishment in that other State. This provision was added at the request of Australia to permit it to tax a portion of the sale profit when goods are produced or purchased in Australia, processed there at cost by a related enterprise, and then sold. It is an alternative approach to allocating part of the profit to the processing operation in such a case, as the United States could do under section 482.

Paragraph 6 provides that control of one company by another does not of itself constitute either company a permanent establishment of the other. The determination as to whether a subsidiary is a permanent establishment of its parent corporation, or the converse, or whether two or more subsidiaries of the same corporation are permanent establishments of the parent or of each other is made by reference to the tests set out in paragraphs 1 through 5.

These same principles apply in determining whether an enterprise of a Contracting State has a permanent establishment in a third State or whether an enterprise of a third State has a permanent establishment in a Contracting State. Such a determination may be relevant, for example, in deciding the source of interest (paragraph 7 of Article 11 (Interest)) or royalties (paragraph 6 of Article 12 (Royalties)).

ARTICLE 6
INCOME FROM REAL PROPERTY

This Article provides that income from real property may be taxed by the Contracting State where the property is located. This rule does not confer an exclusive right of taxation on the State where the property is located. It simply provides that the situs State has the primary right to tax such income, regardless of whether the income is derived through a permanent establishment in that State or not. The provision in the U.S. Model for a binding election to be taxed on a net basis was deleted. Such an election is available under U.S. law and Australia taxes income from real estate on a net basis. The Article incorporates the rule that a leasehold interest in land and rights to exploit or explore for natural resources constitute real property situated where the land or resources, respectively, are situated. Except for those cases, the definition of real property is governed by the internal law of the Contracting State where the property is situated.

ARTICLE 7
BUSINESS PROFITS

This Article provides rules for the taxation by a Contracting State of income from business activity carried on by a resident of the other State.

Paragraph 1 provides that business profits of an enterprise of one Contracting State shall be taxable only in that State except to the extent that such profits are attributable to a permanent establishment through which the enterprise carries on business in the other Contracting State. (The term "enterprise of one of the Contracting States," used here and elsewhere in this Convention, excludes dual-resident corporations that are treated as residents of neither Contracting State for purposes of the Convention.)

Paragraph 2 provides that the profits to be attributed to a permanent establishment are those which it might be expected to make if it were an independent enterprise engaged in similar activities under similar conditions. The profits must reflect arm's length prices. The profits so attributed may be from income described in section 864(c)(4)(B) of the Internal Revenue Code which are attributable to a permanent establishment in the United States may be subject to tax by the United States. In addition, the limited "force of attraction" rule in I.R.C. section 864(c)(3) does not apply for U.S. tax purposes under the Convention.

Paragraph 3 provides that deductions shall be allowed for expenses incurred for the purposes of the permanent establishment, including, *inter alia*, executive and general administrative expenses, wherever incurred, if such expenses are reasonably connected with the profits of the permanent establishment and would be deductible if it were an independent entity. Australia and the United States will each allow an allocation to a permanent establishment of a portion of research and development and interest expenses incurred by the U.S. home office or elsewhere, provided that the expenses are reasonably connected with the profits of the permanent establishment.

Paragraph 4 states that no profits shall be attributed to a permanent establishment by reason of the mere purchase by it of goods or merchandise for the enterprise.

Paragraph 5 provides that, unless there is good and sufficient reason to the contrary, the same method of determining profits attributable to the permanent establishment shall be used each year.

Paragraph 6 provides that, where business profits include items of income dealt with in other articles of the Convention, the provisions of those other articles override the provisions of this Article. For example, the taxation of income of international shipping and aircraft operations is governed by Article 8 (Shipping and Air Transport) and not by this Article. Similarly, the taxation of dividends, interest, and royalties is controlled by Articles 10, 11, and 12, respectively; however, the terms of those Articles provide that where dividends, interest, or royalties derived by a resident of a Contracting State are attributable to a permanent establishment in the other Contracting State, the provisions of this Article do apply and the item of income is taxed as business profits.

Paragraph 7 was inserted at the request of Australia to permit the tax authorities of a Contracting State to apply the provisions of internal law in determining tax liability in cases where the information available to the competent authority is not adequate to measure accurately the profits of a permanent establishment. The Internal Revenue Service would have this power even in the absence of such a specific provision. The determination of profits in such cases, based on the available information, must be done consistently with the principles of this Article, i.e., it must seek to reflect arm's length pricing and appropriate deductions of expenses.

Notwithstanding the other provisions of this Article, paragraph 8 allows each State to apply its domestic law in taxing income from the insurance business, provided that such law remains the same as on the date the Convention was signed or is modified only in minor respects. In the case of a nonresident general insurance company which insures risks in Australia, Australia imposes its ordinary corporate tax rate (now 46 percent) on a deemed profit equal to 10 percent of the gross premiums from such insurance. The company may elect instead to be taxed on a net basis. The United States will apply its excise tax on insurance and reinsurance premiums of Australian insurers or will tax the net income of a U.S. trade or business of an Australian insurer, as appropriate.

Unlike the U.S. model, this Convention does not provide that business profits include income from the rental of tangible personal property and films. In this Convention those types of rentals are treated as royalties under Article 12 (Royalties). However, the maintenance of substantial equipment in the other Contracting State for more than 12 months (other than equipment leased under a "hire-purchase" agreement) constitutes a permanent establishment covered by this Article.

ARTICLE 8
SHIPPING AND AIR TRANSPORT

Paragraph 1 provides that each of the Contracting States shall exempt from tax profits derived by an enterprise of the other Contracting State from the international operation of ships or aircraft, including: (a) profits from the rental on a full basis of ships and aircraft operated in international traffic by the lessee (provided that the lessor also engages in the international operation of ships or aircraft or in the regular leasing of ships or aircraft on a full basis), and (b) profits from the rental of ships and aircraft on a bareboat basis and of containers and related equipment operated or used in international traffic by the lessee, provided in each case that the leasing activity is incidental to the operation of ships or aircraft in international traffic by the lessor. Rental on a full or bareboat basis refers to whether the ships or aircraft are leased fully equipped, manned and supplied.

For example, if a U.S. airline which operates internationally leases a plane on a bareboat basis to an Australian airline for use on its international routes, the rental income derived by the U.S. company is exempt from Australian tax under this Article. However, if the U.S. airline operates only within the United States, or if the leased plane is used only within Australia, the rental income is not exempt under this Article. Moreover, if a U.S. bank leases a plane on a bareboat basis to the Australian airline, either for use internationally or within Australia, that rental income is not exempt under this Article.

Income from the rental of ships, aircraft or containers which is not exempt from tax under this Article is taxable in accordance with Article 12 (Royalties). Australian law imposes tax on the net income after deducting expenses, subject to a maximum tax under Article 12 of 10 percent of the gross rental.

Paragraph 2 states that the provisions of this Article apply to the share of an enterprise of a Contracting State in the profits of a pool or joint venture, even though the other participants may be enterprises of third States not covered by this Convention. The profit shares of such third country participants are not affected by this Convention, but are taxable in accordance with internal law or under the provisions of another international agreement, if applicable.

Paragraph 3 merely clarifies that profits from the transport of goods or passengers picked up and discharged within the same Contracting State are not within the definition of international traffic and may be taxed by that State.

ARTICLE 9
ASSOCIATED ENTERPRISES

This article provides that, where related persons engage in transactions which are not at arm's-length, the Contracting States may make appropriate adjustments to their taxable income and tax liability.

Paragraph 1 states the general rule that where an enterprise of one Contracting State and an enterprise of the other Contracting State are related through management, control, or capital and their commercial or financial relations differ from those which would prevail between independent enterprises, the profits of the enterprises may be adjusted to reflect the profits which would have accrued if the two enterprises had been independent.

Paragraph 2 provides that, where one of the Contracting States has increased the profits of an enterprise of that State to reflect the amount that would have accrued to the enterprise had it been independent of an enterprise in the other Contracting State, the second State shall make an appropriate adjustment, decreasing the amount of tax which it has imposed on those profits. In determining such adjustments, due regard is to be had to the other provisions of the Convention. The competent authorities of the two States shall consult each other if necessary in implementing this provision.

Paragraph 3 clarifies that each Contracting State may apply its internal law in determining liability for its tax. For example, although paragraphs 1 and 2 refer to allocations of "profits" and "taxes," it is understood that such terms also include the components of the tax base and of the tax liability, such as income, deductions, credits, and allowances. The United States will apply its rules and procedures under section 482 of the Internal Revenue Code. Australia will apply the provisions of its income tax legislation, particularly with respect to the determination of taxable income in cases where the information available is inadequate to measure net income under the ordinary rules. Such determinations must be consistent in each case with the principles of arm's length transactions.

ARTICLE 10
DIVIDENDS

This Article limits the rate of tax which may be imposed by a Contracting State on dividends paid by a company which is a resident of that State for purposes of its tax to a resident of the other Contracting State. A dual resident corporation is a resident of each Contracting State "for purposes of its tax," but is a resident of neither State for purposes of the Convention.

Paragraph 1 states that such dividends may be taxed in the State of residence of the recipient. This provision, which is based on the OECD model, confirms the provision of paragraph 3 of Article 1 (Personal Scope) that each Contracting State reserves the right to tax its residents.

Paragraph 2 provides that such dividends may also be taxed in the Contracting State of which the paying company is a resident for the purposes of its tax, but such tax may not exceed 15 percent of the gross amount of the dividends when the beneficial owner is a resident of the other State. This limitation applies to the tax imposed by either State on dividends paid by a dual resident company to a resident of the other Contracting State; but since a dual resident company is not a resident of either State under Article 4 (Residence), it does not apply to dividends received by such a company. In the absence of a treaty, Australia, like the United States, imposes a tax of 30 percent on gross dividends paid to nonresidents. By treaty, Australia is willing to reduce that the tax to, but not below, 15 percent. The reciprocal 15 percent limit of taxation at source provided in this paragraph also applied in the 1953 Convention.

Paragraph 3 defines dividends as income from shares and income which under domestic law is assimilated to income from shares.

Paragraph 4 provides that when dividends benefically owned by a resident of one Contracting State are attributable to a permanent establishment or a fixed base which that resident maintains in the other State, of which the company paying the dividends is a resident, such dividends are not taxable in accordance with this Article, but in accordance with the provisions of Article 7 (Business Profits) or Article 14 (Independent Personal Services).

Paragraph 5 provides that a Contracting State may not impose tax on dividends paid by a company which is a resident of the other State, with three exceptions: (a) to the extent that the dividends are paid to a resident of the first State; (b) to the extent that the dividends are attributable to a permanent establishment or fixed base of the beneficial owner in the first State; or (c) to the extent that 50 percent or more of the gross income of the company paying the dividends is attributable to one or more of permanent establishments of that company in the first State and the dividends are paid out of the profits of such permanent establishment. Subparagraph (c) applies only if the taxing State does not impose branch profits tax of the kind described in paragraph 6. For this purpose, the U.S. accumulated earnings and personal holding company taxes are not taxes of the kind described in paragraph 6. If only subparagraph (c) applies, the tax is limited to 15 percent. The United States may also tax dividends received by U.S. citizens under paragraph 3 of Article 1 (Personal Scope).

Paragraph 6 authorizes the imposition of a branch profits tax in addition to the ordinary corporate tax on profits of a permanent establishment of a resident of the other Contracting State. Australia's ordinary corporate income tax rate is 46 percent, but the rate of tax on permanent establishments of nonresident corporations is 51 percent. Dividends distributed by Australian corporations to a U.S. corporation are subject to a tax of 15 percent. Distributions by an Australian branch of a U.S. company are not subject to a further tax. Thus, the additional 5 percentage points of tax on the branch profits serves as a substitute for a withholding tax on distributed profits. Under paragraph 6, Australia's additional tax may not exceed the amount which would result if the 15 percent dividend withholding tax were to be applied to the profits of the permanent establishment net of the corporate tax at the rate applicable to domestic corporations. For example, if a permanent establishment has taxable income of 100 in Australia and the ordinary corporate income tax rate is 46 percent, the additional tax on the branch profits may not exceed 15 percent of 54, or 8.1; i.e., the total tax on the branch may not exceed 54.1 percent (46 plus 8.1). The Australian tax of 51 percent is within this limit.

Paragraph 6 also provides that, if a nonresident company is liable to a tax on its undistributed profits, the amount of undistributed profits shall be calculated as if that company had paid the corporate income tax applicable to a domestic corporation and had distributed dividends of an amount such that the 15 percent tax on those dividends imposed in accordance with paragraph 2 of this Article would have equalled the additional tax. For example, with an Australian tax on domestic corporations of 46 percent and on permanent establishments of foreign corporations of 51 percent, a permanent establishment of a U.S. corporation would, for purposes of any Australian tax on undistributed profits, be deemed to have distributed profits of 33.33 and undistributed profits of 20.67 for each 100 of taxable income. (Profit of 100 after basic corporate tax of 46 leaves 54 available for distribution. Additional tax of 5 is equivalent to a 15 percent withholding tax on 33.33; 15% × 33⅓ = 5. Therefore, distributed profits are deemed to be 33.33 and the remainder of the after-tax profit of 54, or 20.67 is deemed to be undistributed.

ARTICLE 11
INTEREST

This Article limits the tax which may be imposed by either Contracting State on interest derived and beneficially owned by a resident of the other Contracting State. There is no corresponding provision in the 1953 Convention.

Paragraph 1 states that such interest may be taxed in the State of residence of the beneficial owner. This provision, which comes from the OECD model, confirms the provision of paragraph 3 of Article 1 (Personal Scope) that each Contracting State reserves the right to tax its residents.

Paragraph 2 provides that such interest may also be taxed by the State in which it has its source, but the tax is limited to 10 percent of the gross amount of the interest. Australia's statutory rate of tax on interest paid to nonresidents is generally 10 percent.

Paragraph 3 provides that, when interest benefically owned by a resident of one Contracting State is attributable to a permanent establishment or fixed base which that resident maintains in the other State, that interest is not taxable in accordance with this Article but in accordance with the provisions of Article 7 (Business Profits) or Article 14 (Independent Personal Services).

Paragraph 4 states that the provisions of this Article shall not apply to interest payments between related persons in excess of the amount which would have been agreed upon at arm's-length. Such excess amount shall be taxed according to the laws of each Contracting State, with regard also to the other provisions of this Convention.

Paragraph 5 defines interest as income assimilated to income from money lent under the tax law of the Contracting State where the income arises.

Paragraph 6 provides that a Contracting State may not tax interest paid by a resident of the other State, with three exceptions: (1) to the extent that the interest has its source in that State; (2) to the extent that the beneficial owner of the interest is a resident of that State; or (3) to the extent that the interest is attributable to a permanent establishment or fixed base of the owner in that State. Under these rules the United States may tax interest paid by an Australian company if the interest has its source in the United States in accordance with paragraph 7 of this Article, and in accordance with the Internal Revenue Code. Where such interest is beneficially owned by a resident of Australia, the U.S. tax will be reduced to 10 percent, in accordance with paragraph 2 of this Article. The United States may also tax interest received by U.S. citizens, pursuant to paragraph 3 of Article 1 (Personal Scope).

Paragraph 7 defines the source of interest. Interest has its source in a Contracting State if paid by that State, a political subdivision or local authority thereof, or a person who is a resident of that State for purposes of its tax, including a corporation which under the respective internal laws is a resident of both States. (Thus, interest paid by such a dual resident company may be eligible for the reduced rate provided in paragraph 2, although interest beneficially owned by such a company is not.) An exception to this general rule, which looks to the payer of the interest, provides that when the indebtedness is incurred in connection with and the interest is borne (deducted in computing taxable income) by a permanent establishment or fixed base which the payer has in a Contracting State, the interest has its source in that State.

The Convention does not provide for exemption at source of interest derived and beneficially owned by the Government of the other State or by a government instrumentality. Under Australian law, such interest, e.g., interest derived by the U.S. Government or the Export-Import Bank, is currently exempt from tax in Australia. Similarly, under U.S. law (I.R.C. section 892) interest derived by the Australian government would generally be exempt from U.S. tax.

ARTICLE 12
ROYALTIES

This Article limits the tax which may be imposed by either Contracting State on royalties derived and beneficially owned by a resident of the other Contracting State.

Paragraph 1 states that such royalties may be taxed in the State of residence of the beneficial owner. This provision, which comes from the OECD model, confirms the provision of paragraph 2 of Article 1 (Personal Scope) that each Contracting State reserves the right to tax its residents.

Paragraph 2 provides that such royalties may also be taxed by the State in which they have their source, but the tax is limited to 10 percent of the gross amount of the royalties. Under the 1953 Convention, copyright royalties (other than those related to films) are exempt from tax at source, but other royalties are taxable at the statutory rates. Australia's statutory tax on royalties paid to nonresidents, other than for films or video tapes, is withheld by the payer at the full corporate or individual tax rate on the gross amount less allowable expenses necessarily incurred in deriving the royalty. The Convention preserves the net basis of taxation by Australia, except that the amount of tax liability may not exceed 10 percent of the gross amount of the royalty paid. Payments for the use of films and video tapes are taxed by Australia at 10 percent of the gross amount. This practice is confirmed by this Article. On the U.S. side the statutory rate of 10 percent will be reduced to 10 percent.

Paragraph 3 provides that when royalties beneficially owned by a resident of one Contracting State are attributable to a permanent establishment or fixed base maintained by that resident in the other State, the royalties will not be taxed in accordance with the provisions of this Article but in accordance with the provisions of Article 7 (Business Profits) or Article 14 (Independent Personal Services).

Paragraph 4 contains a definition of the term "royalties." The definition is broader than the one in the U.S. Model. For purposes of this Convention, payments for the use of, or right to use, industrial, commercial or scientific equipment are treated as royalties, except when such equipment is leased under a "hire-purchase" agreement. Payments for the use of, or right to use, motion picture films and certain tapes are also taxed as royalties. And royalties, for purposes of this Article, include payments or credits for scientific, technical, industrial or commercial knowledge or information owned by any person, and payments or credits for ancillary assistance furnished to enable the application of any property or right to which this Article applies. The reference to knowledge or information "owned" is meant to indicate that the term "royalties" implies a property right as distinguished from personal services. An engineer or architect who prepares a design for a customer is considered to perform personal services, the remuneration for which is covered under Article 14 (Independent Personal Services) or 15 (Dependent Personal Services). An engineer or architect who supplies a preexisting design or blueprint is considered to be furnishing knowledge or information, the payment for which constitutes a royalty governed by this Article. The supply of ancillary services does not give rise to a royalty when supplied in connection with the sale of property, but does give rise to a royalty when supplied in connection with the leasing of any of the property or rights covered by this Article.

In some cases, income covered by this Article gives rise to a permanent establishment if the income-producing activity continues long enough. For example, payments for the leasing of industrial, scientific or commercial equipment (other than under a "hire-purchase" agreement) are taxable as royalties, but if the enterprise deriving the royalties maintains the equipment for rental in the other State for longer than 12 months, it is considered to have a permanent establishment in that other State under paragraph 4(b) of Article 5 (Permanent Establishment). In such a case the income is taxable from the beginning in accordance with Article 7 (Business Profits), as provided in paragraph 3 of this Article. Similarly, payments for the supply of supervisory services could in some cases constitute royalties; but if the services are furnished for more than 9 months in a 24 month period, the enterprise has a permanent establishment under paragraph 4(c) of Article 5 (Permanent Establishment), and the income is taxable in accordance with Article 7 (Business Profits), as provided in paragraph 3 of this Article.

Subparagraph (b)(iii) of paragraph 4 provides a special rule to deal with the situation of a disguised lease of a property right of the type covered by this paragraph. If, for example, an Australian company were to use in Australia a copyright or patent held by a U.S. company without paying a royalty to the U.S. company and the U.S. company were to forebear from selling the protected products in Australia in return for payment, the U.S. company would be treated as having received a royalty from the Australian company.

Subparagraph (c) of paragraph 4 provides that, to the extent that income from the disposition of any property or right described in this paragraph is contingent on the productivity or use or further disposition of such property or right, it is a royalty.

Paragraph 5 states that the provisions of this Article shall not apply to royalty payments between related persons in excess of the amount which would have been agreed upon at arm's-length. Such excess amount shall be taxed according to the laws of each Contracting State, with regard also to the other provisions of this Convention.

Paragraph 6 defines the source of royalties. In general, a royalty is considered to have its source in a Contracting State if paid by the Government or a resident of that State or by a company which under internal law is a resident of that State. (Thus, a royalty paid by a dual resident company may be eligible for the reduced rate provided in paragraph 2, although a royalty beneficially owned by such a company is not.) However, if a permanent establishment or fixed base in one of the Contracting States or in a third State incurs the liability to pay the royalties and bears the payment (deducts it in computing taxable income), the royalty is considered to have its source in the State where the permanent establishment or fixed base is located. Moreover, if under these rules a royalty is not considered to have a source in either State but it relates to the use of property or the right to use property in one of them, the royalty is considered to have its source where the property is used or where there is a right to use it. Thus, for example, if an Australian resident were to license a patent to a third country company, which in turn sublicenses the patent for use in the United States, the United States would tax the sublicense payment by the U.S. user to the third country company in accordance with U.S. law, or with the provisions of a U.S. treaty with that country, if applicable, and would also tax the license payment by the third country company to the Australian resident, subject to the limitation in paragraph 2. Third country residents cannot obtain the rate reduction provided in paragrah 2, since this Article applies only to royalties derived by residents of a Contracting State.

ARTICLE 13
ALIENATION OF PROPERTY

This Article provides rules for the taxation of certain gains derived by a resident of a Contracting State. In general, it provides that: (1) gains from the alienation of real property may be taxed where the real property is located; (2) gains derived from the alienation of ships or aircraft or related property may be taxed only by the State of which the enterprise is a resident, except to the extent that the enterprise has been allowed depreciation of the property in computing taxable income in the other State; and (3) gains from the alienation of property referred to in paragraph 4(c) of Article 12 (Royalties) are taxable under Article 12. Gains with respect to any other property are covered by Article 21 (Income Not Expressly Mentioned), which provides that gains effectively connected with a permanent establishment are taxable where the permanent establishment is located, in accordance with Article 7 (Business Profits), and that other gains may be taxed by both the State of source of the gain and the State of residence of the owner. Double taxation is avoided under the provisions of Article 22 (Relief from Double Taxation).

Paragraph 1 of Article 13 states the rule that gains derived from the alienation of real property situated in a Contracting State may be taxed by that State.

Paragraph 2 defines real property in each of the Contracting States. In the case of the United States, paragraph 2(a) explains that the term "real property situated in the other Contracting State" includes a United States real property interest as defined under the Foreign Investment in Real Property Tax Act, as amended. Thus, the United States retains its full taxing right under the law. In the case of Australia, paragraph 2(b) provides that real property has the meaning it has under Australian law and includes an interest in a company, partnership, trust or estate, the assets of which consist wholly or principally of real property situated in Australia.

Paragraph 3 provides that when an enterprise of a Contracting State derives gains with respect to the alienation of ships, aircraft, or containers operated or used by it in international traffic, the gain shall be taxable only in the State of residence of the enterprise, except to the extent that the enterprise has been allowed depreciation on that property in the other Contracting State. To the extent that depreciation deductions have reduced the tax on income from the operation of such ships, aircraft, or containers in the other State, that other State may recapture those depreciation deductions (but not in excess of the gain realized) when the property is disposed of. This paragraph also provides a cross-reference to paragraph 4(c) of Article 12 (Royalties) and states that gain on royalties described in that paragraph (royalties which are contingent on the use or productivity of the right or property) are taxable in accordance with that Article.

Paragraph 4 clarifies that real property consisting of shares in a company or interests in a partnership, estate or trust referred to in paragraph 2(b) is deemed to be situated in Australia.

ARTICLE 14
INDEPENDENT PERSONAL SERVICES

This Article concerns the taxation of income derived by a resident of one of the Contracting States from independent personal services.

The rule established in this Article is that, if an individual who is a resident of one Contracting State performs independent personal services in the other Contracting State, the income from those services may be taxed by that other State if the individual either is present in that other State for an aggregate of more than 183 days in the taxable year (or income year) or has a fixed base regularly available to him in that other State for the purpose of performing his activities. In the latter case, the other State may tax the income for services performed in that other State which is attributable to that fixed base.

It is understood that the term "fixed base" is analogous to the term "permanent establishment." Independent personal services include all personal services performed by an individual for his own account, including services performed as a partner in a partnership, where he receives the income and bears the losses arising from such services, except that services performed as a director of a company are covered by Article 15 (Dependent Personal Services).

ARTICLE 15
DEPENDENT PERSONAL SERVICES

This Article concerns the taxation of remuneration derived by a resident of one of the Contracting States as an employee or as a director of a company.

Pensions, annuities and remuneration of government employees are covered by Articles 18 and 19. Other remuneration of a resident of one of the Contracting States for employee services or for services performed as a director of a company may be taxed only in the State of residence unless the employment is exercised or the services are performed in the other State, in which case that other State may tax the remuneration for the services performed there, subject to the conditions set forth in paragraph 2.

Paragraph 2 provides that, even where a resident of one Contracting State performs services in the other State, that other State may not tax the income for such services if three conditions are met: (a) the recipient is present in that State for not more than 183 days in the taxable year (or income year); (b) the remuneration is paid by or on behalf of an employer, or, in the case of remuneration of directors, a company, that is not a resident of that State; and (c) the remuneration is not deductible in determining taxable profits of a permanent establishment, fixed base, or a trade or business of the employer or company in that State. If any one of these conditions is not met, e.g., if the employer is a resident of the State where the services are performed, the income may be taxed by that State. The insertion of the reference to a trade or business means that if, for example, an Australian resident is employed in the United States by a Bermuda company and his salary is deducted in determining the profits of the U.S. trade or business of that company, the salary is taxable in the United States even if the Bermuda company does not have a permanent establishment in the United States.

Paragraph 3 provides that remuneration derived for employment aboard a ship or aircraft operated in international traffic by a resident of a Contracting State may be taxed by that State. Under this provision, Australia may tax the remuneration of employees for services aboard ships or aircraft operated internationally by Australian residents. Similarly, the United States may tax such remuneration when the operator is a U.S. resident. However, under U.S. law, the United States taxes such income of a nonresident alien only to the extent it is derived from U.S. sources (i.e., within U.S. territorial waters). This paragraph does not confer an exclusive taxing right. Both Contracting States retain the right to tax their residents and citizens under paragraph 3 of Article 1 (Personal Scope).

ARTICLE 16
LIMITATION ON BENEFITS

This Article limits the benefits of the Convention to bona fide residents of the Contracting States. It is intended to prevent residents of third countries from inappropriately using a company which is a resident of one of the Contracting States as a conduit or similar vehicle to obtain Treaty benefits. Specifically, a person (other than an individual) which is a resident of one of the Contracting States is entitled to relief from taxation from the other Contracting State only if any of three alternative tests is met.

The first two tests are objective tests relating to the entity in question. If more than 75 percent of the beneficial interest in the person receiving the income is owned, directly or indirectly, by any combination of individuals who are residents of the Contracting States, citizens of the United States, the Contracting States themselves, or publicly traded companies which are residents of the Contracting States, the first test is met.

Under the second test a publicly traded company that is a resident of Australia or the United States is considered to have a sufficient nexus with Australia or the United States, respectively, so as to entitle it to treaty benefits. Under this test, Treaty benefits are not denied if there is substantial and regular trading of the principal class of shares of such a company on a recognized stock exchange in one of the Contracting States. A recognized stock exchange includes the NASDAQ system in the United States.

The third test recognizes that ownership of an entity that is a resident of the United States or Australia by persons resident in third countries is not uncommon. In view of the factors discussed below, granting Treaty benefits to such an entity often is consistent with the goals of the Treaty. Accordingly, under the third test, Treaty benefits are allowed if the establishment, acquisition and maintenance of the person and the conduct of its operations did not have as a principal purpose the purpose of obtaining Treaty benefits. This test would be met, for example, if an Australian company owned by third country residents conducts business operations in Australia and its U.S. investments are related or incidental to those business activities, or if the Australian tax burden equals or exceeds the tax reduction claimed under the Convention. It could also be met in other situations.

Paragraph 3, inserted at the request of Australia, provides a special rule concerning certain trust situations. The benefits of the Treaty do not apply to income derived by a trustee which under the Convention is treated as income of a resident of one of the Contracting States if a principal purpose of the use of the trust was to obtain a benefit under the Convention. For example, if an Australian resident establishes one or more U.S. accumulation trusts with Australian beneficiaries to receive dividends from Australian corporations in order to reduce the Australian tax on those dividends, the reduced rate provided in paragraph 2 of Article 10 (Dividends) will not apply.

This Article is not meant to impose any added burden on withholding agents, and withholding agents will not be required to verify a person's ownership or purposes.

In applying this Article the normal burden of proof rules apply. For example, under present U.S. procedures, an entity that is a resident of Australia and that believes it is entitled, under one of the alternative tests of this Article, to the 10 percent U.S. tax rate on interest provided by Article 11 (Interest) would merely file a U.S. Form 1001 with the appropriate withholding agent to claim the benefit. Of course, the Internal Revenue Service could, on audit, examine the transaction.

In view of a combination of factors—the tax burden imposed by both the United States and Australia; the fact that, even under treaties, Australia imposes source taxation on income of nonresidents of Australia at a level that is not insignificant; the fact that the Treaty's rate reductions on source taxation of passive income are not as great as those accorded by the United States in many other treaties; and the concerns of both countries about tax avoidance and evasion—this Convention is not expected to be the subject of abuse. It is, therefore, anticipated that residents of the Contracting States will typically satisfy at least one of the three exceptions. Consequently, it should rarely be necessary to deny Treaty's benefits under this Article.

ARTICLE 17
ENTERTAINERS

This Article provides certain exceptions to the rules otherwise governing income from personal services in the case of income derived by entertainers and athletes.

Paragraph 1 provides that a Contracting State may tax income derived by a resident of the other State from the performance of personal services in the first State as an entertainer or athlete if the gross receipts for such services, including expenses reimbursed or paid on his behalf, exceeds $10,000 (or the equivalent in Australian dollars) for the income year or taxable year concerned. In that case the full amount may be taxed by the first State, subject to any deductions allowable under its laws. This rule overrides the provisions of Articles 14 (Independent Personal Services) and 15 (Dependent Personal Services) by adding another basis for taxation at source. However, if the income does not exceed $10,000, whether the income may be taxed by the State where the services are performed is determined in accordance with Article 14 or 15, as the case may be.

Income derived from services rendered by producers, directors, technicians and others who are not artistes or athletes is taxable in accordance with Article 14 or 15, as appropriate.

Paragraph 2 corresponds to the provision in the U.S. Model. Where income for services performed by an entertainer or athlete accrues not to the entertainer or athlete but to another person, it may be taxed in the State where the activities are performed, without regard to the provisions of the Convention concerning business profits or income from personal services, unless it is established that neither the entertainer or athlete nor any related person participates in those profits in any manner.

ARTICLE 18
PENSIONS, ANNUITIES, ALIMONY AND CHILD SUPPORT

This Article deals with the taxation of pensions, social security payments, annuties, alimony and child support derived by individuals who are residents of a Contracting State or citizens of the United States.

Paragraph 1 provides that pensions derived and beneficially owned by a resident of one of the Contracting States in consideration of past employment, other than pensions covered in Article 19 (Governmental Remuneration), shall be taxable only in that State.

Paragraph 2 provides that public pensions, such as social security benefits, paid by one Contracting State to a resident of the other State or to a citizen of the United States are taxable only in the paying State. The reference to U.S. citizens is to ensure that a social security payment by Australia to a U.S. citizen resident in Australia shall be taxable only in Australia and not in the United States. The exemption of such income provided by this paragraph is excepted from the saving clause under paragraph 4 of Article 1 (Personal Scope).

Paragraph 3 provides that annuities paid to a resident of a Contracting State shall be taxable only in that State.

Paragraph 4 defines "pensions and similar remuneration" and paragraph 5 defines "annuities."

Paragraph 6 provides that alimony and other maintenance payments, including child support payments, are taxable only in the State where they arise. The definitions and source rules relating to alimony and child support payments are determined under the internal laws of the Contracting States. Under Australian law alimony and child support payments are exempt to the recipient and not deductible by the payer. Thus, under this provision, alimony arising in the United States and paid to a resident of Australia will be deductible by the payer but taxed to the recipient by the United States. Alimony arising in Australia and paid to a U.S. resident, and child support payments arising in either State and paid to a resident of the other State, will not be deductible by the payer and will not be taxed to the recipient. These exemptions are available to residents and citizens of the respective States as a result of paragraph 4 of Article 1 (Personal Scope).

ARTICLE 19
GOVERNMENTAL REMUNERATION

This article provides that remuneration, including pensions, paid by one of the Contracting States or a political subdivision, local authority or agency thereof to a citizen of that State for the performance of governmental functions is exempt from tax by the other State. If such remuneration is paid to an individual who is a resident, but not a citizen, of the employing State, whether it may be taxed by the other Contracting State is determined in accordance with the provisions of Articles 14 (Independent Personal Services), 15 (Dependent Personal Services), 17 (Entertainers) or 18 (Pensions, Annuities, Alimony and Child Support), as the case may be. If such remuneration is paid by one of the States to an individual who is a resident of the other State (or by Australia to a citizen of the United States), it may be taxed by that other State (or by the United States in the case of U.S. citizens) in accordance with paragraph 3 of Article 1 (Personal Scope). If such remuneration is paid to an individual who is not a resident of either State (and is not a citizen of the United States), it is not covered by this Convention.

Whether functions are of a governmental nature is determined by reference to the concept of a governmental function in the State in which the income arises.

ARTICLE 20
STUDENTS

This Article provides that, when a resident of one of the Contracting States goes to the other State for the purpose of full-time education, that other State may not tax payments received by the student for the purpose of his maintenance or education from sources outside that State.

ARTICLE 21
INCOME NOT EXPRESSLY MENTIONED

This Article provides that items of income derived by a resident of one of the Contracting States and not covered in the preceding articles may be taxed by the country of residence of the recipient. If from sources in the other State, such income may also be taxed by that other State. However, Article 7 (Business Profits) governs the taxation of such income to the extent it is effectively connected with a permanent establishment in that other State.

Among the items covered by this Article are prizes and income from the insurance business, which is specifically excluded from the provisions of Article 7 (Business Profits) by paragraph 8 of that Article. The source of such items of income is determined under the respective domestic laws of the two countries. Any difficulties or doubts in applying this Article, as in other cases, may be addressed in accordance with the provisions of Article 24 (Mutual Agreement Procedure).

ARTICLE 22
RELIEF FROM DOUBLE TAXATION

Paragraph 1 provides that the United States shall give a foreign tax credit for income taxes paid to Australia, subject to the limitations provided in U.S. law. The credit is allowed for taxes paid directly by or on behalf of the U.S. resident or citizen. In addition, in the case of a U.S. corporation owning at least 10 percent of the voting stock of an Australian corporation, credit is allowed for the underlying Australian corporate tax on the profits of the Australian corporation out of which dividends are paid to the U.S. corporation. The Australian taxes referred to in paragraphs 1(b) and 2 of Article 2 (Taxes Covered) are considered income taxes for purposes of the credit.

This guarantee of a foreign tax credit is independent of the statutory grant of a credit under the Internal Revenue Code, but the amount of the credit to be allowed is determined in accordance with the limitations provided in the Internal Revenue Code. Since the Convention does not provide credit for a tax which is believed not to be creditable under the Internal Revenue Code, no special per-country limitation is contained in the Convention. However, paragraph 1 provides that the Convention source rules may be used only for purposes of determining U.S. foreign tax credits for the Australian taxes covered by the Convention, i.e., not for taxes of other foreign countries.

In paragraph 2, Australia agrees to allow Australian residents a credit against Australian income tax equal to the income tax paid in the United States other than solely by reason of U.S. citizenship (i.e., the amount of tax which the United States is authorized under the Convention to impose at source on residents of Australia who are not U.S. citizens), subject to the limitations in Australian law which limit the credit to the Australian income tax payable on the income or any class thereof or on income from sources outside Australia.

Paragraph 3 confirms that an Australian corporation that owns at least 10 percent of the voting stock of a U.S. corporation is entitled to a rebate in its assessment, at the average rate of Australian tax payable by it, on dividends it receives from the U.S. corporation which are included in its taxable income in Australia. If Australian law providing this relief from tax on inter-corporate dividends should change so that the rebate is no longer allowable, Australia agrees to allow credit for the underlying U.S. tax on the profits out of which such dividends are paid (similar to the U.S. credit allowed under section 902 of the Internal Revenue Code) in addition to the direct credit referred to in paragraph 3.

Paragraph 4 provides a special rule for avoiding double taxation of a U.S. citizen who is a resident of Australia. Both the United States and Australia tax the worldwide income of such a person. The special rule provides that, in such a case, the United States will credit against the U.S. tax the Australian tax paid, net of the Australian foreign tax credit provided for in paragraph 2 (i.e., the Australian foreign tax credit for United States source-basin taxation). For purposes of computing the foreign tax credit limitation under this paragraph, the United States will recharacterize enough U.S.-source income as Australian-source income to allow this special credit to be utilized, but without reducing the U.S. tax below the amount the United States may impose under this Convention other than by reason of citizenship (i.e., the amount of U.S. tax that may be imposed on a source basis under this Convention on residents of Australia who are not U.S. citizens). This source rule is provided by paragraph 1(c) of Article 27 (Miscellaneous), subject to the limitation provided in this paragraph.

ARTICLE 23
NON-DISCRIMINATION

This Article provides certain criteria of nondiscriminatory application of the taxes covered by the Convention.

Paragraph 1 provides, first, that citizens of a Contracting State who are residents of the other State shall not be taxed less favorably in that other State than resident citizens of that other State who are in the same circumstances. It is understood that United States citizens who are not residents of the United States and Australian citizens who are not residents of the United States are not in the same circumstances with respect to the U.S. income tax, which is generally imposed on the worldwide income of U.S. citizens but not of Australian citizens.

Paragraph 1 also provides, in subparagraph (b), that interest, royalties, and other disbursements paid by a resident of a Contracting State to a resident of the other State shall be deductible for determining taxable profits under the same conditions as if they had been paid to a resident of the first-mentioned State. The term "other disbursements" is understood to include a reasonable allocation of executive and administrative expenses, research and development expenses, and other expenses incurred for a group of related enterprises.

Subparagraph (c) is the same as the corresponding paragraph in the U.S. Model. It requires that a Contracting State not impose more burdensome taxation on a subsidiary corporation owned by residents of the other Contracting State than it imposes on similar corporations which are locally owned.

Subparagraph (d) provides that a Contracting State may not impose more burdensome taxes on a permanent establishment of an enterprise of the other State than it imposes on its own enterprises carrying on the same activities in the same circumstances.

Paragraph 2 states that this Article does not affect the taxes of either Contracting State as in force on the date of signature of the Convention or tax laws subsequently enacted which are substantially similar to the existing taxes in purpose or are reasonably designed to prevent avoidance or evasion of tax. However, any subsequent tax measure must treat residents or citizens of the other State no less favorably than residents or citizens of a third State (except where the treatment of residents or citizens of third States is governed by an international agreement rather than by internal law).

Both Australia and the United States allow certain exemptions, deductions or rate reductions to residents taxed on their worldwide income which they do not extend to nonresidents not taxed on their worldwide income. For example, Australia imposes a 5 percent additional corporate tax on the profits of Australian branches of foreign corporations in lieu of a withholding tax on their profit remittances to the home office, denies to such branches the rebate on intercorporate dividends available to Australian corporations, and limits certain exemptions from the withholding tax on interest to funds borrowed abroad by domestic corporations owned and controlled by Australian residents. The United States does not extent to U.S. branches of foreign corporations the same deduction for dividends received from U.S. corporations which is available to U.S. corporations nor does it allow inclusion of income of foreign corporations in a consolidated return. Under this Article, those practices will not be in violation of the Convention; however, paragraph 2 in this regard is merely clarifying as neither Australia nor the United States would consider the foregoing provisions of its respective law to violate to nondiscrimination provisions even in the absence of the rule of paragraph 2.

Paragraph 3 states that differentiating in taxation laws between residents and nonresidents does not of itself constitute discrimination contrary to this Article. This is merely an elaboration of the principles contained in paragraph 1, which require equal treatment of residents in the same circumstances. Residents and nonresidents are not in the same circumstances, reflecting the fact that in both countries residents are taxable on their worldwide income whereas nonresidents in general are taxable only on income from sources in that country.

Paragraph 4 provides that the competent authorities will attempt to resolve any instances of discriminatory taxation which might arise as a result of the tax measures of either country. Taxpayers may also take advantage of the provisions of Article 24 (Mutual Agreement Procedure) in such cases.

ARTICLE 24
MUTUAL AGREEMENT PROCEDURE

This Article provides for cooperation between the competent authorities to resolve problems of double taxation.

Paragraph 1(a) provides that a taxpayer who considers that the actions of one or both of the Contracting States may result in taxation not in accordance with the Convention may present his case to the competent authority of the State of which he is a resident or citizen. However, he must present his case within three years from the first notification of the action giving rise to the potential double taxation.

Paragraph 1(b) provides that the competent authority, if it considers the claim to be justified, shall endeavor to resolve the case by mutual agreement with the competent authority of the other Contracting State. Any agreement reached shall be implemented without regard to any statutory time limits of the Contracting States. Thus, for example, if it is agreed that tax liability should be adjusted downward, a refund of the excess tax paid will be made even though the statute of limitations may have expired. However, no additional tax may be imposed if the statute of limitations has expired in the taxing State.

Paragraph 2 provides that the competent authorities shall endeavor by mutual agreement to resolve any difficulties or doubts which may airse in the interpretation or application of the Treaty. For example, the competent authorities may agree on the same allocation of income, deductions, credits or allowances; to the same determination of the source of particular items of income; on a common meaning of a term; and they may decide, for purposes of paragraph 2(c) of Article 4 (Residence) to which State an individual has closer personal and economic relations. They may also discuss the application of the provisions of domestic law regarding penalties, fines and interest in a manner consistent with the purposes of the Convention.

Paragraph 3 provides that the competent authorities may communicate with each other directly for the purpose of reaching agreements in accordance with this Article.

ARTICLE 25
EXCHANGE OF INFORMATION

This Article provides for the exchange of information between the competent authorities of the Contracting States for the purposes of implementing the provisions of the Convention or administering statutory provisions concerning taxes covered by the Convention. Its terms are substantially similar to the corresponding provisions of the U.S. model.

Paragraph 1 provides that the competent authorities shall exchange such information as is necessary for carrying out the provisions of the Convention or for administering statutory provisions concerning taxes covered by the Convention provided the information can be obtained under domestic laws and administrative practices with respect to each State's own taxes. Thus, provided that the information could be obtained in administering a domestic tax covered by the Convention, the competent authorities agree to exchange such information without regard to whether there is a domestic liability in the case in question. The information furnished could relate to a tax not covered by the Convention if it is relevant to enforcing a tax which is so covered. For example, it is possible that information relating to sales taxes or estate taxes could be needed to verify an item of income or expense for income tax purposes.

Paragraph 2 provides guarantees that the information exchanged shall be kept secret and may be disclosed only to persons, including a court or administrative body, concerned with the assessment, collection, administration or enforcement of the taxes covered by the convention or with litigation with respect to those taxes. Persons involved in the administration of taxes covered by the Convention include legislative bodies involved in the administration of taxes and their agents such as, for example, the United States General Accounting Office; therefore, information may be disclosed to them, subject to the limitations of this Article and the internal law of the respective Contracting

Paragraph 3 provides that neither State will furnish information to the other State under this Article if it would be contrary to its public policy to do so.

Paragraph 4 states that, when specifically requested by the competent authority of the other Contracting State, and provided that such documents could be obtained in enforcing its own taxes, copies of unedited original documents shall be provided.

In paragraph 5 the competent authorities of the two Contracting States agree to endeavor to collect taxes on behalf of the other State to the extent necessary to ensure that any exemption or reduction in rate of tax provided in the Convention is not enjoyed by persons not entitled to the benefits of the Convention.

ARTICLE 26
DIPLOMATIC AND CONSULAR PRIVILEGES

This Article corresponds to Article 27 of the U.S. model. It provides that the Convention shall not affect taxation privileges of diplomatic consular officials under other special agreements of international law.

ARTICLE 27
MISCELLANEOUS

This Article provides certain miscellaneous rules of taxation under the Convention.

Paragraph 1 provides source rules. Income derived by a resident of the United States which, under the Convention, may be taxed by Australia, is deemed to have its source in Australia. Income derived by a resident of Australia which may be taxed by the United States under the Convention, other than solely by reason of citizenship or because the individual elected under U.S. law to be taxed as a resident of the United States, is deemed to have its source in the United States. With respect to U.S. citizens who are residents of Australia, to the extent that income which they derive is taxed by the United States by virtue of paragraph 3 of Article 1 (Personal Scope), such income is deemed to have its source in Australia for purposes of giving affect to paragraph 4 of Article 22 (Relief from Double Taxation).

Paragraph 2 provides that certain exemptions granted with respect to earned income by the source country, in accordance with Articles 14 (Independent Personal Services), 15 (Dependent Personal

Services), 17 (Entertainers), or 19 (Governmental Remuneration), will be inapplicable to the extent that such income is not taxed by the residence country. For example, a United States resident who performs services in Australia as a self-employed person and who neither remains in Australia for 183 days nor has a fixed base in Australia, nevertheless may be taxed by Australia on the remuneration for the services performed there, notwithstanding Article 14 (Independent Personal Services), to the extent with such remuneration is exempt from U.S. income tax under section 911 of the Internal Revenue Code. The purpose of the exemption at source provided in the articles listed in this paragraph is to avoid double taxation, not to provide double exemption.

ARTICLE 27 [28]
ENTRY INTO FORCE

The Convention is subject to ratification in accordance with the applicable procedures of each Contracting State. The instruments of ratification will be exchanged at Washington, D.C.

The Convention enters into force on the date on which the instruments of ratification are exchanged. Its provisions take effect, with respect to dividends, interest and royalties paid, credited or otherwise derived, on or after the first day of the second month following the exchange of instruments of ratification and, with respect to all other income, for taxable years (or income years) beginning on or after the first day of the second month following the exchange of instruments of ratification.

The 1953 Convention shall cease to have effect with respect to taxes to which this Convention applies in accordance with the above provisions and shall terminate on the expiration of the last date on which it has effect.

ARTICLE 29
TERMINATION

The Convention shall remain in force indefinitely unless terminated by one of the Contracting States. Either State may terminate the Convention after five years from the date on which it enters into force by giving at least six months prior notice through diplomatic channels. In that event, the Convention will cease to have effect with respect to dividends, interest and royalties paid, credited or otherwise derived on or after January 1 following the expiration of the six-month period and, with respect to all other income, for taxable years (or income years) beginning on or after January 1 following the expiration of the six-month period.

As an exception to those general rules, the provisions of the Convention concerning social security benefits and similar public pensions provided in paragraph 2 of Article 18 (Pensions, Annuities, Alimony and Child Support) may be terminated by either Contracting State at any time by giving prior notice to the other State through diplomatic channels.

May 24, 1983

Part IV. Items of General Interest

Limitation on Certain Adoptions and Changes of Annual Accounting Period

Announcement 86–113[1]

Announcement 86–101, 1986–41 I.R.B. 14, informed taxpayers that the Internal Revenue Service will issue temporary regulations to limit the ability of taxpayers to change their annual accounting period in anticipation of the Tax Reform Act of 1986. Except for certain anti-abuse rules, Announcement 86–101 did not address adoptions of a taxable year.

This announcement informs taxpayers that the temporary regulations also will suspend the provisions of Rev. Proc. 72–51, 1972–2 C.B. 832, in the case of partnerships requesting approval for the adoption of an annual accounting period that would result in the deferral of income to the partners of three months or less. In addition, the temporary regulations will suspend the provisions of section 4.03 of Rev. Proc. 83–25, 1983–1 C.B. 689, relating to corporations making the election to be an S corporation and seeking to adopt or retain an annual accounting period that results in the deferral of income of three months or less to shareholders holding more than one-half of the shares of the stock of the corporation. The temporary regulations will provide that partnerships and corporations generally must establish a substantial business purpose for the adoption or retention of an annual, accounting period. This requirement will not apply, however, to an adoption or retention of an annual accounting period under a procedure (such as that of section 4.02 of Rev. Proc. 83–25) that is not suspended by the temporary regulations.

The suspension of Rev. Proc. 72–51 and Rev. Proc. 83–25 as they relate to adoptions or retentions of an annual accounting period generally will apply unless the application required to effect or request the adoption or retention is timely filed before. Thus, for example, the temporary regulations will not apply to a taxpayer that elected subchapter S status and adopted a taxable year pursuant to section 4.03 of Rev. Proc. 83–25 if the Form 2553 was timely filed before. The temporary regulations will not apply to an adoption by a partnership of a taxable year that begins before January 1, 1986.

In addition, the effective date stated in Announcement 86–101 with respect to the application of the temporary regulations to changes of annual accounting period will be modified. The temporary regulations relating to changes of annual accounting period generally will apply if the income tax return for the short period involved in the change is filed after September 29, 1986. The temporary regulations will not apply, however, if the application required to effect or request the change was timely filed before September 30, 1986.

Payments of Tax and Interest in Cases Arising Under Partnership or S Corporation Audit Procedures and Estimates of Interest Accrued on Tax Liabilities

Announcement 86–114

This announcement supplements Announcement 86–108, 1986–45 I.R.B. 20, which describes the procedures taxpayers should follow to make payments of interest with respect to tax deficiencies, that may be or have been proposed by the Service. This announcement provides guidance to taxpayers who wish to make payments with respect to partnership or S corporation items for partnership taxable years beginning after September 3, 1982 or S corporation taxable years beginning after December 31, 1982.[1] This announcement also provides a table that all taxpayers may use to estimate the amount of interest that has accrued on any federal tax liability.

Announcement 86–108 and this announcement supplement rather than supersede Rev. Proc. 84–58, 1984–2 C.B. 501. For example, a taxpayer who has received a Notice of Proposed Deficiency may make an advance payment allocated proportionately to tax and interest under Rev. Proc. 84–58, even though Announcement 86–108 does not expressly mention the advance payment procedure in that situation. To ensure appropriate administrative treatment of the payment, however, the Service encourages taxpayers to follow one of the procedures applicable to their circumstances outlined in this announcement and Announcement 86–108.

Several significant differences exist between unified examinations of partnership and S corporation returns and other examinations. If the taxpayer's partnership or S corporation is audited under the partnership audit rules (Code sections 6221–6233) or the S corporation audit rules (Code sections 6241–6245), the taxpayer will not receive a Notice of Proposed Deficiency (30-day letter) or Statutory Notice of Deficiency (90-day letter) with respect to the partnership or S corporation items and affected items subject to a computational adjustment. The taxpayer will receive a Notice of Computational Adjustment after final resolution of the partnership or S corporation case. In addition, the taxpayer may receive, after completion of the partnership or S corporation proceeding, a Notice of Proposed Deficiency or Statutory Notice of Deficiency with respect to certain "affected items" that require a partner- or shareholder-level determination.

Because of the special rules applicable to entity-level proceedings, failure to follow the procedures outlined below may result in administrative or legal inability to process the payment as a payment of interest.

Prior to Issuance of a Final Partnership Administrative Adjustment (FPAA)

If a Notice of Final Partnership Administrative Adjustment (FPAA) has not yet been issued and the taxpayer wishes to make an interest payment before the end of 1986, the taxpayer may file an amended return (Form 1040X) and a Request for Administrative Adjustment (Form 8082) consistent with what the taxpayer believes will be the final determination of the unified examination. The taxpayer's submission of the Forms 1040X and 8082 permits the Service to assess the additional tax reported and the interest thereon. Along with the Forms 1040X and 8082, the taxpayer either may pay tax and interest or may pay interest only, in which case the Service will bill the taxpayer for the unpaid balance and subsequently accrued interest.

A taxpayer who files the Forms 1040X and 8082 after a notice of the beginning of a partnership or S corporation proceeding has been issued will remain part of the unified examination proceeding. Accordingly, if the Notice of Computational Adjustment sent to the taxpayer upon completion of the final partnership or S corporation audit determination reflects less tax than that reported by the taxpayer on the Form 1040X, any excess tax and interest previously paid will be credited to the taxpayer's account. Conversely, if the Notice of Computational Adjustment reflects a tax liability that exceeds the amount reported by the taxpayer, the additional tax and accrued interest owed by the taxpayer will be assessed.

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[1] Also released as News Release IR–86–148, dated November 5, 1986.

[1] This announcement also applies to partnership taxable years ending after September 3, 1982, if the partnership has elected to be subject to the partnership audit procedures for such taxable years.

However, if the taxpayer files the Forms 1040X and 8082 before a notice of the beginning of a partnership (or S corporation) proceeding has been issued, the Service may remove the taxpayer from the unified examination proceedings under section 6227(c)(3) (or section 6244) by mailing a notice that the taxpayer's partnership (or S corporation) items will be treated as nonpartnership (or non-S corporation) items. If the Service does not mail this notice, the taxpayer remains part of the unified examination proceeding.

If the Service has a settlement position with respect to the particular partnership in which the taxpayer is an investor, the taxpayer may execute a Form 870–P agreeing to that position. The taxpayer may tender a payment allocated solely to interest, and the Service will bill the taxpayer for the unpaid balance and subsequently accrued interest. Execution of the settlement agreement binds both the taxpayer and the Service with respect to the partnership or S corporation items and removes the taxpayer from the unified proceeding. Thus, if the partnership or S corporation case is eventually resolved on some other basis, neither the taxpayer nor the Service may modify the settlement to reflect that later resolution.

Subsequent to Issuance of an FPAA

If the taxpayer wishes to make an interest payment after an FPAA has been issued, the taxpayer may enter into a settlement agreement (Form 870–P). The settlement agreement enables the Service to make the necessary computational adjustment and to assess the tax owed by the settling taxpayer. As a result, the taxpayer either may pay tax and interest or may pay interest only, in which case the Service will bill the taxpayer for the unpaid balance and any subsequently accrued interest. A taxpayer who wishes to tender an interest payment with the Form 870–P should estimate the amount of the computational adjustment and the interest due thereon and should submit a check designated as interest with the executed Form 870–P. The amount of the payment that exceeds the interest owed by the taxpayer will be credited against any unpaid tax.

The execution of a settlement agreement consistent with the FPAA removes the taxpayer from the scope of the unified proceeding and binds the taxpayer and the Service. Thus, neither the Service nor the taxpayer may modify the settlement agreement if the partnership or S corporation case is eventually resolved in a manner that is inconsistent with the FPAA.

In the alternative, a taxpayer may wish to make a payment while remaining in the partnership or S corporation proceeding until its conclusion. The taxpayer may do so by filing a Form 1040X that reflects the additional tax liability and tendering a check allocated to interest only or to tax and interest. The Form 1040X *must* contain the following waiver language:

> This Form 1040X reflects adjustments from ____________ (name of partnership/S corporation) for the year covered by this Form 1040X. Under I.R.C. §§6224(b)/6244, I/we hereby waive the restrictions on assessment and collection contained in I.R.C. §§6225/6244 with respect to the tax liability attributable to adjustments regarding the partnership or S corporation items and any other amounts that are subject to a computational adjustment under I.R.C. §§6231(a)(6)/6244 shown on this Form 1040X.

This waiver must be typed or handwritten on the back of the Form 1040X. Without the waiver, the Service may ultimately be unable to accept the taxpayer's payment as an interest payment and may eventually convert it into a cash bond. As described above, the Service will bill the taxpayer for any tax or subsequently accrued interest that is not paid with the Form 1040X. At the conclusion of the partnership or S corporation proceeding, the taxpayer will receive a Notice of Computational Adjustment reflecting the final determination of the entity-level proceeding. A Form 1040X filed after the FPAA has been issued shall not be treated as a return for purposes of the consistency requirements under section 6222(a) or 6242.

Taxpayers Having Both TEFRA and non-TEFRA Items

The unified partnership and S corporation proceeding rules provide separate audit, litigation, and assessment procedures for so-called TEFRA adjustments (*i.e.*, adjustments that are properly included in a computational adjustment under section 6231(a)(6) or section 6244, including partnership or S corporation items and affected items that do not require a partner- or shareholder-level determination). A taxpayer who has both TEFRA adjusments and non-TEFRA adjustments (including adjustments with respect to affected items that require a partner- or shareholder-level determination) with respect to the same taxable year should follow the procedures outlined in this announcement for the TEFRA adjustments and those outlined in Announcement 86–108 for the non-TEFRA adjustments.

Table for Estimating Interest

The table below provides a guide to estimating the amount of interest that has accured on a tax liability. Determine the amount of tax owed, locate the interest factor for the appropriate period, and multiply the tax owed by the interest factor. For example, if a taxpayer agrees to the waiver of restrictions on assessment and collection of $1,000 tax for calendar year 1984 on December 1, 1986, the estimated interest would be $1,000 × .1853 = $185.30.

Taxable Period	*Date of Remittance*			
	11/15/86	12/01/86	12/15/86	12/31/86
1977	1.3968	1.4063	1.4146	1.4241
1978	1.3029	1.3120	1.3200	1.3291
1979	1.1897	1.1984	1.2060	1.2147
1980	1.0018	1.0097	1.0167	1.0247
1981	.7886	.7956	.8018	.8090
1982	.4951	.5010	.5062	.5122
1983	.3252	.3305	.3351	.3404
1984	.1807	.1853	.1894	.1941
1985	.0563	.0605	.0642	.0684

This table shows factors for computing the approximate amount of interest which has accrued, depending on the date remittance was made and the date the tax was due, for individual returns of calendar year taxpayers. The chart assumes no complications such as restricted interest, net operating losses, interest on substantial underpayments attributable to tax motivated transactions, partial payments subsequent to the filing of the return, or penalties.

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[2] References in this announcement to a Notice of Final Partnership Administrative Adjustment (FPAA) should be read as referring also to a Notice of Final S Corporation Administrative Adjustment (FSAA), and references to Form 870–P should be read as referring also to Form 870–S.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in Internal Revenue Bulletin the names and addresses of practitioners who have been suspended from such practice, their designation as attorneys, certified public accountant, enrolled agent or enrolled actuary, and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletin for five successive weeks or for as many weeks as is practible for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
S. Melvin Apotheker	Miami, FL	Attorney	Indefinite from September 1, 1986
Sandra S. Behn	London, TN	Certified Public Accountant	Indefinite from September 12, 1986
Charles K. Hyter	Hutchinson, KS	Attorney	Indefinite from September 18, 1986
William Pyke	Dallas, TX	Certified Public Accountant	Eighteen Months from August 15, 1986
Alan Z. Richards	West Hempstead, NY	Attorney and Certified Public Accountant	Indefinite from September 20, 1986

Under 20 Code of Federal Regulations, Part 901, an enrolled actuary, in order to avoid the initiation or conclusion of a suspension or termination proceeding, may offer his/her consent to suspension of enrollment. The Executive Director, Joint Board for the Enrollment of Actuaries, may suspend enrollment in accordance with the consent offered. An enrolled actuary whose enrollment is suspended is prohibited from performing actuarial services under the Employee Retirement Income Security Act of 1974 (ERISA) during the period of suspension.

To enable employees of the Internal Revenue Service and others to identify enrolled actuaries under suspension, the Executive Director will announce in the Internal Revenue Bulletin the names and addresses of enrolled actuaries who have been suspended. This announcement will appear in the weekly Bulletin at the earliest practicable date following suspension and will continue to appear in the weekly Bulletin for at least three successive weeks for each enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

Name of Enrolled Actuary	Address	Term of Suspension
Michael Winston	Fort Lauderdale, FL	Six Months from October 20, 1986

Under 31 Code of Federal Regulations, Part 10, an enrolled agent, in order to avoid the institution of a proceeding for his disbarment of suspension from practice before the Internal Revenue Service, may offer his resignation. The Director of Practice, in his discretion, may accept the offered resignation of an enrolled agent.

To enable the public and other practitioners to identify such resigned enrolled agents, the Director of Practice will announce in the Internal Revenue Bulletin the name and address of each enrolled agent who has resigned and the effective date of resignation. This announcement will appear in the weekly Bulletin at the earliest practicable date after the action and will continue to appear in the weekly Bulletins for five successive weeks or for as many weeks as is practicable for each resigned enrolled agent, and will later be consolidated and published in the Cumulative Bulletin.

The following individual has entered a consent resignation from enrollment to practice before the Internal Revenue Service:

Name of Enrolled Agent	Address	Effective Date of Resignation
William E. Bonafede	Wakefield, RI	September 30, 1986

Under Section 330, Title 31 of the United States Code, the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any attorney, certified public accountant, enrolled agent, or enrolled actuary who has violated the rules and regulations governing such practice.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individuals have been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
James L. Ketner	Charlotte, NC	Certified Public Accountant	September 27, 1986
George L. Weil	Orange, CT	Certified Public Accountant	September 27, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR— Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–136, page 9.
Estimated tax; underpayment; penalties; corporations and individuals. No penalties will be imposed on underpayments of estimated tax existing during any period ending on or before the applicable date for filing 1986 calendar year returns to the extent the underpayments are attributable to changes made by the Tax Reform Act of 1986.

Rev. Rul. 86–138, page 5.
Partnerships; income and deductions; partnership computation. A subsidiary partnership in a multitiered arrangement must separately state items of income, gain, loss, deduction, and credit.

Rev. Rul. 86–139, page 6.
Partnerships; adjustments to basis; extension of time to make election. The Commissioner will consider requests for extensions of time to make the election provided in section 754 of the Code where the failure to make a timely election was not discovered until after the partnership terminated.

Rev. Rul. 86–140, page 7.
Information reporting; state taxes. State imposed taxes on dividends, on net capital gains, and on net taxable income of unincorporated businesses are income taxes for purposes of the information reporting requirements of section 6050E of the Code.

Announcement 86–117, page 31.
This Bulletin contains a list of organizations that no longer qualify as organizations contributions to which are deductible under section 170(c)(2) of the Code.

Announcement 86–118, page 32.
Mortgage revenue bonds; average annual mortgage originations. Issuers of mortgage revenue bonds may continue to rely on the average annual mortgage originations contained in Rev. Proc. 85–39 until new average annual mortgage originations are published.

EXEMPT ORGANIZATIONS

EE–154–78, page 11.
Proposed regulations relate to lobbying expenditures by public charities described in section 501(c)(3) of the Code.

EMPLOYEE PLANS

Rev. Rul. 86–142, page 4.
Deductions; contributions; limitations; brokers' commissions. Brokers' fees paid by qualified plans and Individual Retirement Arrangements (IRAs), are not separately deductible, but are subject to the deduction limits of section 404(a) of the Code for plans, and section 219 for IRAs.

Notice 86–14, page 10.
Minimum distributions from qualified plans and individual retirement accounts and annuities for calendar years 1985 and 1986 will not be required until December 31, 1987.

Finding Lists begin on page 33.

Department of the Treasury
Internal Revenue Service

T 22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 162.—Trade Or Business Expenses

26 CFR 1.162–10: Certain employee benefits.

Whether broker's fees paid by employers that maintain qualified plans or by owners of Individual Retirement Arrangements are separately deductible, or whether they are subject to the deduction limits of sections 219(a) and 404(a) of the Code. See Rev. Rul. 86–142, this page.

Section 164.—Taxes

26 CFR 1.164–1: Deduction for taxes.

State imposed taxes on dividends, on net capital gains, and on net taxable income of unincorporated businesses are income taxes for purposes of the information reporting requirements of section 6050E of the Code. See Rev. Rul. 86–140, page 7.

Section 212.—Expenses For Production Of Income

26 CFR 1.212–1: Nontrade or business expenses.

Whether broker's fees paid by employers that maintain qualified plans or by owners of Individual Retirement Arrangements are separately deductible, or whether they are subject to the deduction limits of sections 219(a) and 404(a) of the Code. See Rev. Rul. 86–142, this page.

Section 219.—Retirement Savings

26 CFR 1.219–1: Deduction for retirement savings.

Whether broker's fees paid by owners of Individual Retirement Arrangements are subject to the deduction limits of section 219(a) of the Code. See Rev. Rul. 86–142, this page.

Section 404.—Deduction for Contributions of an Employer to an Employees' Trust or Annuity Plan and Compensation Under a Deferred-Payment Plan

26 CFR 1.404(a)–1: Contributions of an employer to an employees' trust or annuity plan and compensation under a deferred payment plan; general rule.
(Also Sections 162, 212, 219; 1.162–10, 1.212–1, 1.219–1.)

Deductions; contributions; limitations; brokers' commissions. Brokers' fees paid by qualified plans and Individual Retirement Arrangements (IRAs), are not separately deductible, but are subject to the deduction limits of section 404(a) of the Code for plans, and section 219 for IRAs.

Rev. Rul. 86–142

ISSUES

(1) Are additional contributions made by the employer to reimburse the trust of a qualified plan for brokers' commissions on transactions involving plan assets deductible under section 162 or 212 of the Internal Revenue Code?

(2) Are additional contributions to an individual retirement account (IRA) within the meaning of section 408(a) to reimburse the IRA for brokers' commissions on transactions involving IRA assets deductible under section 162 or 212?

FACTS

Situation 1.

A corporation established a plan for its employees. The plan is qualified under section 401(a) of the Code and the related trust is exempt from tax under section 501(a). The plan year and the taxable year of the employer are the calendar year.

The plan provides that the employer will reimburse the trust for brokers' commissions charged in connection with the purchase and sale of securities for the employees' trust. The employer, over the plan year, makes the maximum deductible contribution to the plan under section 404 of the Code. During the plan year, the employer makes additional contributions to reimburse the trust for the brokers' commissions paid by the trust.

Situation 2.

An individual established an IRA within the meaning of section 408(a) of the Code on July 1, 1985, and upon establishment contributed the maximum amount allowable as a deduction under section 219 for that year. Later, during 1985, the individual made additional contributions to the IRA to reimburse the account for brokers' commissions incurred in connection with the purchase of securities on behalf of the IRA.

LAW AND ANALYSIS

Section 162 of the Code allows a deduction for the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.

Section 1.162–10(a) of the Income Tax Regulations provides that no deduction shall be allowed under section 162 of the Code if, under any circumstances, the amounts may be used to provide benefits under a stock bonus, pension, annuity, profit-sharing, or other deferred compensation plan of the type described in section 404(a).

Section 404(a) of the Code allows, subject to certain limitations, a deduction for employer contributions under a stock bonus, pension, profit-sharing, or annuity plan, or for compensation paid or accrued under a plan of deferred compensation, provided that such contributions or compensation satisfies the provisions of section 162 or 212.

Section 1.404(a)–3(d) of the regulations provides that expenses incurred by the employer in connection with a qualified employees' plan, such as trustee's fees and actuary's fees, that are not provided for by contributions under the plan are deductible by the employer under section 162 of the Code (relating to trade or business expenses), or section 212 (relating to expenses for production of income), to the extent that such expenses are ordinary and necessary. Amounts that are not ordinary and necessary expenses are not deductible under section 162.

Rev. Rul. 68–533, 1968–2 C.B. 190, holds that a sole proprietor's payment of trustee's fees that were expenses not provided for by contributions under a qualified plan are deductible by the sole proprietor under section 162 or 212 of the Code to the extent that they are ordinary and necessary. Such expenses are deductible in addition to the maximum deduction for employer contributions under the plan allowable by section 404.

The principles enunciated in the regulations under section 162 of the Code are equally applicable to section 212, except that the production of income requirement is substituted for the business requirement. Section 1.212–1(e) of the regulations provides in part that section 212 of the Code does not allow the deduction of any expenses which are disallowed by any of the provisions of Subtitle A of the Code (relating to Income Taxes) even though such expenses may be paid or incurred for one of the purposes specified in section 212.

Brokers' commissions are not recurring administrative or overhead expenses, such as trustee or actuary fees, incurred in connection with the maintenance of the trust or plan. Rather, brokers' commissions are intrinsic to the value of a trust's assets: buying commissions are part of the cost of the securities purchased and selling commissions are an offset against the sales price. Accordingly, employer contributions to reimburse the trust for brokers' commissions are used to provide benefits under the plan of which the trust is a part and thus are not deductible under section 162 or 212. Similarly, if instead of making additional contributions to the trust, the employer paid the brokers' commissions directly to the broker, such amounts are treated as though they had been contributed to the trust and used to provide benefits under the plan. Such direct payments thus are not deductible under section 162 or 212.

Amounts contributed (or treated as contributed) to a plan are deductible subject to the rules and limits in section 404. This is the case without regard to whether the amounts are used to pay brokers' commissions, administrative or overhead expenses (such as trustee or actuary fees), or cash benefits.

In situation (1), the employer's contributions to reimburse the trust for brokers' commissions are not deductible as a separate expense under section 162 or 212. Also, because such contributions result in the employer's total contributions exceeding the amount deductible under section 404 for the taxable year, such additional contributions are not deductible under section 404. Such contributions, however, may be deductible in future years under the carryover rules of section 404(a).

Section 219(a) of the Code provides that there shall be allowed as a deduction an amount equal to the qualified retirement contributions of the individual for the taxable year. Section 219(e)(1) provides that such contributions include amounts paid by or on behalf of an individual to an IRA.

Rev. Rul. 84–146, 1984–2, C.B. 61, discusses the deductibility of trustee's fees with respect to IRAs. It holds that, consistent with the rules governing deductions in connection with qualified plans, amounts paid by the IRA owner for such fees in connection with an IRA are deductible under section 212 of the Code to the extent they satisfy the requirements of that section, but that amounts paid that are not ordinary and necessary expenses, such as capital expenditures and disguised IRA contributions, are not deductible under section 212.

The analysis that applies to employer contributions to a trust to pay brokers' commissions on transactions involving qualified plan assets also applies to IRA contributions. Thus, IRA contributions to pay brokers' commissions on transactions involving IRA assets and direct payments by the IRA owner to a broker for commissions on transactions involving IRA assets are not deductible under section 162 or 212. Such contributions (and payments treated as IRA contributions) are deductible subject to the limits of section 219.

In Situation (2), the additional contributions to the IRA to reimburse the IRA for brokers' commissions result in the total IRA contributions for 1985 exceeding the amount that can be deducted under section 219 for 1985. The contributions that exceed the limits of that section are subject to the tax on excess contributions described in section 4973.

HOLDINGS

The employer contributions to the trust of the qualified plan in Situation (1) to reimburse the trust for brokers' commissions on transactions involving trust assets cannot be separately deducted as an ordinary and necessary business expense under sections 162 or 212 of the Code.

Similarly, the IRA contribution by the IRA owner in Situation (2) to pay brokers' commisions on transactions involving the assets of the IRA cannot be separately deducted under section 162 or 212 of the Code.

Section 702.—Income and Credits of Partner

26 CFR 1.702-1: Income and credits of partner.

Whether, in a multitiered partnership arrangement, the separate statement of income, gain, loss, deduction, or credit by the subsidiary partnership could affect the tax liability of a partner in the higher-tier partnership but not the tax liability of a partner of the subsidiary partnership. See Rev. Rul. 86–138, below.

Section 703.—Income and Deductions

26 CFR 1.703-1: Partnership computations.
(Also Section 702; 1.702-1.)

Partnerships; income and deductions; partnership computation. A subsidiary partnership in a multitiered arrangement must separately state items of income, gain, loss, deduction, and credit.

Rev. Rul. 86–138

ISSUE

Under section 703(a) of the Internal Revenue Code, is a subsidiary partnership in a multitiered arrangement required to state separately items of income, gain, loss, deduction, or credit if separate statement of these items could affect the tax liability of a partner in a higher-tier partnership in the multitiered arrangement but not the tax liability of a partner of the subsidiary partnership?

FACTS

S, a limited partnership, engages in construction activities. *X*, a corporation, is the sole general partner of *S*. *P*, a limited partnership, is the sole limited partner of *S*. The partners of *P* are all individuals. *S* and *P* are classified as partnerships under section 7701(a)(2) of the Code.

In the taxable year in question, *S* paid interest expense on indebtedness incurred to purchase property held for investment within the meaning of section 163(d)(3)(D) of the Code. *S* did not separately state the investment interest expense or the investment income in informing its partners of their distributive share of income, gain, loss, deduction, or credit on schedule K–1 (Form 1065) (Partner's Share of Income, Credits, Deductions, etc.) for the taxable year.

LAW AND ANALYSIS

Section 701 of the Code provides that a partnership as such shall not be subject to the income tax imposed by chapter 1 of the Code. Persons carrying on business as partners shall be liable for income tax only in their separate or individual capacities.

Section 702(a) of the Code provides that, in determining a partner's income tax, each partner must take into account separately the partner's distributive share of items enumerated in section 702(a)(1) through, (8). Under section 702(a)(7), a partner must take into account separately those items of income, gain, loss, deduction, or credit prescribed by regulations.

Section 1.702–1(a)(8)(ii) of the Income Tax Regulations provides that each partner must take into account separately the partner's distributive share of any partnership item which if separately taken into account by any partner would result in an income tax liability for that partner different from that which would result if that partner did not take the item into account separately.

Section 702(b) of the Code provides that the character of any item included in a partner's distributive share under paragraphs (1) through (7) of section 702(a) is determined as if the item were realized directly from the source from which realized by the partnership, or incurred in the same manner as incurred by the partnership.

Section 703(a)(1) of the Code provides that a partnership shall separately state the items described in section 702(a) of the Code in computing its taxable income.

Section 163(a) of the Code allows a deduction for all interest paid or accrued within the taxable year on indebtedness.

Section 163(d)(1) of the Code provides that, in the case of a taxpayer other than a corporation, the amount of investment interest otherwise deductible is limited to (A) $10,000 ($5,000, in the case of a separate return by a married individual), plus (B) the amount of the net investment income (as defined in section 163(d)(3)(A)), plus an additional amount in the case of net leases. Section 163(d)(3)(D) defines "investment interest" as interest paid or accrued on indebtedness incurred or continued to purchase or carry property held for investment.

Rev. Rul. 84–131, 1984–2 C.B. 37, concludes that in the case of a partnership whose partners are individuals, the partners must take into account separately their distributive shares of investment interest under section 163(d)(3)(D) of the Code.

The limitation on investment interest expense under section 163(d) of the Code does not apply to corporations. Under section 701, a partnership is not subject to the income tax. Because *S* has only a corporation and a partnership as partners, the tax liability of *S*'s partners cannot be affected by the section 163(d) limitation. However, *P*, the limited partner of *S*, has partners that are individuals. The tax liability of these individual partners of *P* may be affected by the section 163(d) limitation, and they therefore need a separate statement of their distributive share of investment income and investment interest expenses of *S* and *P*. *See* Rev. Rul. 84–131, 1984–2 C.B. 37. The fact that an item flows through an intermediate partnership does not change the character of the item. Therefore, in order to give effect to section 702(a)(8) and section 1.702–1(a)(8)(ii), *S* and *P* must separately state investment interest expense and investment income under section 703 of the Code.

HOLDING

Under section 703(a) of the Code, a subsidiary partnership in a multitiered arrangement must separately state those items of income, gain, loss, deduction, and credit which if separately taken into account by any partner of any partnership in the multitiered structure would result in an income tax liability for that partner different from that which would result if that partner did not take those items into account separately.

Section 708.—Continuation of Partnership

26 CFR 1.708–1: Continuation of partnership.

Requests for extensions of time to make section 754 elections after termination of partnership will be considered. See Rev. Rul. 86–139, below.

Section 743.—Optional Adjustment to Basis of Partnership Property

26 CFR 1.743–1: Optional adjustment to basis of partnership property.

Requests for extensions of time to make section 754 elections after termination of partnership will be considered. See Rev. Rul. 86–139, below.

Section 754.—Manner of Electing Optional Adjustment to Basis of Partnership Property

26 CFR 1.754–1: Time and manner of making election to adjust basis of partnership property.
(Also Sections 708, 743; 1.708–1, 1.743–1, 1.9100–1.)

Partnerships; adjustments to basis; extension of time to make election. The Commissioner will consider requests for extensions of time to make the election provided in section 754 of the Code where the failure to make a timely election was not discovered until after the partnership terminated.

Rev. Rul. 86–139

ISSUE

May the Commissioner grant a request for an extension of time to make the election provided in section 754 of the Internal Revenue Code where the failure to make a timely election was not discovered until after the partnership terminated under the provisions of section 708 of the Code?

FACTS

A and *B* were equal partners in *AB*, a calendar year partnership. *B* died on January 1, 1983. Upon *B*'s death, *B*'s estate succeeded to *B*'s interest in *AB*. The value of *B*'s partnership interest as determined for federal estate tax purposes greatly exceeded the adjusted basis of *B*'s share of partnership assets. During 1983, *B*'s estate was taxable on its distributable share of partnership income. *AB*'s partnership return for 1983 was filed on April 1, 1984. On May 1, 1984, *B*'s estate sold the interest in *AB* to *A*. Shortly thereafter, the executor of *B*'s estate discovered that the section 754 election was omitted from *AB*'s 1983 tax return and requested that the partnership file a request for an extension of time to make an election under section 754 of the Code in connection with the transfer of the partnership interest that occurred on January 1, 1983 when *B* died. The executor intends that the partnership's 1983 return be amended to reflect an increased basis in the estate's share of partnership assets, and a corresponding increase in the estate's deduction for depreciation.

LAW AND ANALYSIS

Section 708(b)(1)(A) of the Code provides that a partnership shall be considered as terminated if no part of any business, financial operation or venture of the partnership continues to be carried on by any of its partners in a partnership. Section 1.708–1(b)(1)(i)(a) of the Income Tax Regulations provides that upon the death of one partner in a two-member partnership, the partnership shall not be considered as terminated if the estate or other successor in interest of the deceased partner continues to share in the profits or losses of the partnership business. Upon a sale of the partnership interest by the estate of the deceased partner to the surviving partner, however, the partnership terminates. *See* Rev. Rul. 67–65, 1967–1 C.B. 168.

Section 754 of the Code provides that if a partnership files an election, the basis of partnership property shall be adjusted in the case of a transfer of a partnership interest in the manner provided in section 743. Under section 1.754–1(b) of the regulations, the election is made in a written statement filed with the partnership return for the taxable year during which the transfer occurs.

Section 743(b) of the Code provides that, in the case of a transfer of an interest in a partnership by a sale or exchange or upon the death of a partner, a partnership with respect to which the election provided in section 754 is in effect shall—(1) increase the adjusted basis of partnership property by the excess of the basis to the transferee partner of that partner's interest in the partnership over that partner's proportionate share of the adjusted basis of partnership property, or (2) decrease the adjusted basis of partnership property by the amount that the partner's share of such property exceeds the basis of that partner's interest in the partnership. Such increase or decrease constitutes an adjustment to the basis of partnership property with respect to the transferee partner only.

Section 1.9100-1(a) of the regulations provides that the Commissioner in the Commissioner's discretion may grant a reasonable extension of time for the making of an election upon the showing of good cause. Relief, however, may be granted only where the time for making the election is not expressly prescribed by statute and where the request for the extension is made before the time fixed by the regulations or within such time thereafter as the Commissioner may consider reasonable under the circumstances.

In this case, *AB* failed to make a timely section 754 election on its 1983 tax return with respect to the transfer of *B*'s partnership interest that took place upon *B*'s death. The availability of relief for the failure to file a timely election provided under section 1.9100-1 of the regulations depends on whether *AB* can show good cause for the failure and whether the election is made within the time deemed reasonable under the circumstances by the Commissioner. The fact that *AB* terminated under section 708(b)(1)(A) upon the sale of the interest by the estate to *A*, before the failure to make the election was discovered, does not preclude *AB* from showing good cause for the failure. The request for the extension, like the election itself, should be made on behalf of the partnership by the person empowered to file a return for a terminated partnership. Who that person is will vary depending on the facts of a given case.

Whether, under the facts and circumstances of each situation, the requirements of section 1.9100-1 have been met will depend upon the following factors:

(1) Due diligence of the taxpayer,

(2) Prompt action by the taxpayer,

(3) Intent of the taxpayer,

(4) Prejudice to the interests of the Government, and

(5) Statutory and regulatory objectives.

See Rev. Proc. 79-63, 1979-2 C.B. 578.

HOLDING

The Commissioner may grant a request for an extension of time to make the election provided in section 754 of the Code where the failure to make a timely election was not discovered until after the termination of the partnership under the provisions of section 708.

Section 6050E.—State and Local Income Tax Refunds

26 CFR 5f.6050E-1: Reporting of state and local income tax refunds.

Information reporting; state taxes. State imposed taxes on dividends, on net capital gains, and on net taxable income of unincorporated businesses are income taxes for purposes of the information reporting requirements of section 6050E of the Code.

Rev. Rul. 86-140

ISSUE

If, in the circumstances described below, a state imposes taxes on dividends, on net capital gains, and on the net taxable income of unincorporated businesses, are refunds, credits, or offsets to individuals of those taxes subject to the information reporting requirements of section 6050E of the Internal Revenue Code?

FACTS

The laws of state *X* impose tax *A* on the state's individual residents. Tax *A* is a tax on all dividends earned by, actually or constructively received by, or accrued or credited to, a taxpayer. The tax is imposed at a graduated rate and is imposed only if the taxpayer's adjusted gross income for federal income tax purposes is $20,000 or more. Under state law, the "dividends" on which the tax is imposed are those amounts that are taxable as dividends for federal income tax purposes, without regard to the dividend exclusion.

State *X* also imposes tax *B* on individual residents. Tax *B* is a tax of 7 percent on all net gains from the sale or exchange of capital assets, actually or constructively received by, or accrued or credited to, the taxpayer during the year. "Net gains" means gains from the sale or exchange of capital assets to the extent that those gains exceed losses from such sales. No capital gains tax is imposed if the net gains are less than $10, or if the taxpayer's adjusted gross income is less than $20,000 and the gains from the sale of the assets do not exceed (1) $200 for a husband and wife, or (2) $100 in all other cases.

State *X* also imposes tax *C*. Tax *C* is a tax on unincorporated businesses, trades, professions, or occupations conducted by, engaged in, or being liquidated by individuals. The tax, however, is not imposed on performance of services as employees or as officers or directors of corporations. The tax is 5 percent of the net taxable income of every unincorporated business wholly or partly carried on within the state and is in addition to other taxes imposed by the state. In computing net income for purposes of tax *C*, the taxpayer starts with gross income as defined for federal income tax purposes. The taxpayer then is allowed deductions for all items of loss and for all deductions directly connected with, or incurred in, the conduct of the business, if the items of loss and the deductions are allowable for federal income tax purposes. Allowable deductions include losses and deductions connected with any property used in the business, subject to certain modifications.

LAW AND ANALYSIS

Section 6050E(a) of the Code provides that every person who makes payments of refunds of state or local income taxes (or allows credits or offsets with respect to such taxes) during any calendar year to any individual aggregating $10 or more must make a return according to forms or regulations prescribed by the Secretary, setting forth the total amount of such payments, credits, or offsets, and the name and address of the individual to whom such payment, credit, or offset was made.

Section 6050E(b) of the Code generally requires that every person making a return under section 6050E(a) must send a statement to the individual whose name is on the return. However, no statement is required if it is determined in the manner provided by regulations that the individual did not claim itemized deductions under chapter 1 for the taxable year giving rise to the refund, credit, or offset.

Section 1.6050E-1(c) of the Income Tax Regulations provides that every refund officer shall make an information return for each calendar year. This return is required even if, under the exception for nonitemizers, the refund officer is not required to furnish a statement to the applicable taxpayer. "Refund officer" is defined in section 1.6050E-1(b)(1) as the officer or employee of a state or local taxing jurisdiction having control of payments of refunds or the allowance of credits or offsets, or the person appropriately designated for purposes of section 1.6050E-1.

Section 1.6050E-1(f) of the regulations provides that the information required to be reported includes the aggregate amount of refunds, credits, and offsets made or allowed during the calendar year with respect to the taxable year of the individual covered by the return; the name, address, and taxpayer identification number of the individual with respect to whom such payment, credit, or offset was made or allowed; the taxable year covered by the return; and such other information as may be required by the forms. In addition, the nature of the tax is required to be indicated on the Form 1099 in any case where the refund, credit, or offset is made or allowed with respect to a payment attributable to an income tax that applies exclusively to income from a trade or business and is not a tax of general application.

Under section 1.6050E–1(k)(1) of the regulations, generally every refund officer required to make an information return under section 1.6050E–1 must furnish to the individual whose identifying number is required to be shown on the return a written statement showing the aggregate amount shown on the information return of refunds, credits, and offsets made or allowed to the individual with respect to each taxable year of the individual, the name of the state or local taxing jurisdiction paying the refund, or allowing the credits or offsets, the taxable year giving rise to the refund, credit, or offset, and a legend stating that the amount is being reported to the Internal Revenue Service.

Section 1.6050E–1(k)(2) of the Code provides an exception to the general rule contained in section 1.6050E–1(k)(1). If the refund officer verifies that the individual did not claim itemized deductions for federal income tax purposes for the taxable year giving rise to the refund, credit, or offset, a statement need not be furnished to the individual. The exception, however, does not apply if the refund, credit or offset is made or allowed with respect to a payment attributable to an income tax that applies exclusively to income from a trade or business and is not a tax of general application.

Under section 62 of the Code, the term "adjusted gross income" in the case of an individual means gross income minus certain deductions. Under section 62(1), these deductions include the deductions allowed by chapter 1 (other than by part VII of subchapter B) that are attributable to a trade or business carried on by the taxpayer, if the trade or business does not consist of the performance of services by the taxpayer as an employee. Section 1.62–1(d) of the regulations states that to be deductible for the purposes of determining adjusted gross income, expenses must be those directly, and not those merely remotely, connected with the conduct of a trade or business.

Under section 63(f) of the Code, the term "itemized deductions" means the deductions allowable by chapter 1 other than the deductions allowable in arriving at adjusted gross income, the deductions for personal exemptions provided by section 151, and the direct charitable deduction.

For purposes of computing taxable income for federal income tax purposes, section 164(a) of the Code permits a deduction for state and local income taxes for the taxable year within which paid or accrued, according to the taxpayer's method of accounting. In addition, under section 1.164–1(a) of the regulations, state and local income taxes that are paid or accrued within the taxable year in carrying on a trade or business or an activity described in section 212 (relating to expenses for the production of income) are permitted as deductions.

The refund, credit, or offset of state or local income taxes that were deducted (with a resulting tax benefit) in a prior year is includible in a taxpayer's gross income. *See* section 111 of the Code. Section 6050E was enacted to assure that any individual taxpayer, whether or not engaged in a trade or business, who deducted a state or local income tax and later received a refund of any portion of those taxes deducted, would include that amount in gross income in the year in which the refund occurs. *See* S. Rep. No. 97–494 (Vol. 1), 97th Cong., 2d Sess. 250 (1982).

Principles developed under federal law, not state interpretations or designations, determine whether a payment falls within the meaning of the terms "taxes" and "income taxes" as used in federal statutes. *See* Rev. Rul. 79–180, 1979–1 C.B. 95; Rev. Rul. 76–215, 1976–1 C.B. 194; Rev. Rul. 71–49, 1971–1 C.B. 103; and Rev. Rul. 61–152, 1961–2 C.B. 42.

The word "taxes" has been defined as an enforced contribution, exacted pursuant to legislative authority in the exercise of the taxing power, and imposed and collected for the purpose of raising revenue to be used for public or governmental purposes and not as payment for some privilege granted or service rendered. The tax must be paid to a government levying the tax, to certain public benefit corporations created by that government for a public purpose, or to their agents. *See* Rev. Rul. 81–191, 1981–2 C.B. 49.

In general, an income tax is a direct tax on gains or profits. Gain is a necessary ingredient of income. *See Bank of America National Trust Savings Association v. United States*, 459 F.2d 513, 517 (Ct. Cl.), *cert. denied*, 409 U.S. 949 (1972). A tax can be an "income tax" even though it is restricted to only certain forms of income. *McGowan v. Commissioner*, 67 T.C. 599, 610 (1976).

The three taxes imposed by state *X* are exacted pursuant to legislative authority in the exercise of the taxing power of the state, and are imposed and collected by the state for the purpose of raising revenues to be used for a governmental function that serves public purposes. In addition, the three taxes fall on net income. They are taxes on gain or profit as opposed to gross receipts. As such, they are income taxes within the meaning of section 164(a) of the Code.

Taxes *A* and *B* are deductible from adjusted gross income as itemized deductions under section 164(a) of the Code. Tax *C*, however, is attributable to a trade or business carried on by the taxpayer that does not consist of the performance of services of an employee. As such, tax *C* is deductible from gross income under section 62(1). Thus, for purposes of the exception for nonitemizers in section 1.6050E–1(k)(2) of the regulations, tax *C* is an income tax that applies exclusively to income from a trade or business and is not a tax of general application. For that reason, the exception for nonitemizers does not apply to tax *C*.

HOLDING

If a refund, credit, or offset of any of the three state *X* taxes is made to an individual, the refund, credit, or offset is subject to the return requirements of section 6050E(a) of the Code and regulations thereunder. In the case of a refund, credit, or offset of taxes *A* and *B*, a statement under section 6050E(b) must also be furnished to the applicable taxpayer, unless pursuant to section 1.6050E–1(k)(2) the refund officer verifies that the taxpayer did not claim an itemized deduction of tax *A* or *B* for federal income tax purposes. In the case of a refund, credit, or offset of tax *C*, a statement must always be furnished to the taxpayer. Tax *C* is an income tax that applies exclusively to income from a trade or business and is not a tax of general application. Since it is a section

62 deduction in arriving at adjusted gross income, the nonitemizer exception from furnishing the statement under section 1.6050E–1(k)(2) does not apply. An itemized deduction. Thus, the exception from furnishing the statement under section 1.6050E–1(k)(2) does not apply.

Section 6654.—Failure by Individual to Pay Estimated Income Tax

26 CFR 1.6654–1: Addition to the tax in the case of an individual.

To the extent underpayments of estimated taxes are attributable to changes made by the Tax Reform Act of 1986 no penalties will be imposed for tax years ending on or before December 31, 1986, if the entire amount of estimated tax due is paid by the date established for filing returns for 1986 calendar year taxpayers. See Rev. Rul. 86–136, below.

Section 6655.—Failure by Corporation to Pay Estimated Income Tax

26 CFR 1.6655–1: Addition to the tax in the case of a corporation.
(Also Section 6654; 1.6654–1.)

Estimated tax; underpayment; penalties; corporations and individuals. No penalties will be imposed on underpayments of estimated tax existing during any period ending on or before the applicable date for filing 1986 calendar year returns to the extent the underpayments are attributable to changes made by the Tax Reform Act of 1986.

Rev. Rul. 86–136[1]

Sections 6654 and 6655 of the Internal Revenue Code impose an addition to tax on individuals and corporations, respectively, for failure to pay estimated taxes when due.

In calculating their estimated tax liability for taxable years beginning in 1985 and 1986, taxpayers may have relied on certain provisions of the Code, such as the investment tax credit of section 38(b)(1), that were subsequently modified or repealed by the Tax Reform Act of 1986 (the Act), (Pub. L. No. 99–514, 100 Stat.).

Section 1543 of the Act provides that no addition to tax shall be made under section 6654 or 6655 of the Code for any period before April 16, 1987 (March 16, 1987, in the case of a corporation), with respect to any underpayment, to the extent that the underpayment was created or increased by a provision of the Act.

The Statement of the Managers filed with the Conference Committee Report indicates that taxpayers shall have until the due date for calendar year returns (April 15, 1987, in the case of individuals, March 15, 1987, in the case of corporations) to pay their full 1986 income tax liability without incurring an addition to tax on account of an underpayment of estimated tax that is attributable to changes in the law made by the Act. (2 H.R. Rep. 99–841 (Conf. Rep.), 99th Cong, 2d Sess. II–798 (1986).) However, the Statement of the Managers also states that, "The conferees intend that no penalties be imposed under section 6655 on underpayments of estimated tax, but only to the extent that (1) the underpayment of an installment results from a taxpayer taking into account investment tax credits on property placed in service after December 31, 1985, and before the date of enactment of the Act, *and* (2) the taxpayer actually pays such underpayment within 30 days after the enactment of the Act." (Conf. Rep. at II–64, emphasis in the original.)

The statutory language of section 1543 of the Act determines the proper penalty relief. Accordingly, no penalties will be imposed on underpayments of estimated tax existing during any period ending on or before the applicable date for filing 1986 calendar year returns, but only to the extent the underpayments are attributable to changes made by the Act.

For example, assume that a taxpayer calculated its quarterly estimated tax payments based on its expected tax liability reduced by an anticipated investment tax credit for property placed in service after 1985. The taxpayer may obtain relief from the penalty imposed on underpayments of estimated tax to the extent its underpayment resulted from the repeal of the investment tax credit.

In a similar manner, a taxpayer that computed its expected regular tax liability using the Accelerated Cost Recovery System (ACRS) and subsequently elected to have the new ACRS rules apply after July 31, 1986, may obtain relief from the penalty imposed on underpayments of estimated tax to the extent that its underpayment resulted from the application of the new ACRS rules (including the mid-quarter convention under section 168(d)(3) of the Code (section 201(a) of the Act)).

Relief from the penalty imposed on underpayments of estimated tax is provided only for periods ending on or before the due date (determined without regard to any extensions) for filing 1986 calendar year returns. A taxpayer that uses a fiscal year as its taxable year will be subject to additions to tax under section 6654 or 6655 of the Code for underpayments of estimated tax existing after such date. In addition, since the Act provides no relief from interest imposed on underpayments of tax liability under section 6601, fiscal year taxpayers may owe interest on underpayments for periods ending on or before the applicable date for filing 1986 calendar year returns regardless of the cause of such underpayments.

For example, assume a corporate taxpayer that has a taxable year ending June 30 underpaid its estimated tax for both its 1986 and 1987 taxable years, solely because of changes made by the Act. With respect to the taxable year ending on June 30, 1986, no penalty will be imposed on the underpayment of estimated tax, although a penalty under section 6655 of the Code normally would accrue through September 15, 1986, the date prescribed for payment of the corporation's tax liability. Under section 6601, interest will run on any unpaid tax liability after September 15, 1986. With respect to the taxpayer's taxable year ending on June 30, 1987, no penalty will be imposed on underpayments of estimated tax existing on or before March 15, 1987. A penalty will be imposed on underpayments of estimated tax existing after March 15, 1987.

Taxpayers whose underpayments of estimated tax result solely from changes made to the Code by the Act should file Form 2210, Underpayment of Estimated Tax by Individuals, or Form 2220, Underpayment of Estimated Tax by Corporations, with their tax return or amended tax return for 1986. Taxpayers should write the word "waiver" in the left hand margin of Form 2210 or Form 2220 and attach a statement that no addition to tax should be assessed because the underpayment of estimated tax is due to changes in the law made by the Tax Reform Act of 1986. The statement should contain sufficient detail to illustrate the impact of the change made by the Act.

Taxpayers whose underpayments are partially due to changes made by the Act (and who are therefore entitled to partial relief) should clearly state the amount of penalty to be waived in addition to the explanatory statements otherwise required.

26 CFR 1.9100–1: Extension of time for making certain elections.

Requests for extensions of time to make section 754 elections after termination of partnership will be considered. See Rev. Rul. 86–139, page 6.

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[1] Also released as News Release IR–86–157, dated November 19, 1986.

Part III. Administrative, Procedural, and Miscellaneous

Required Distributions from IRAs and Qualified Plans, under Sections 401(a)(9), 408(a)(6), and 408(b)(3) of the Code and Amendments to IRAs as a result of Amendments by Section 521 of the Tax Reform Act of 1984.

Notice 86–14

This notice provides further guidance with respect to minimum required before-death and after-death distributions from qualified plans and individual retirement accounts and annuities (IRAs) pursuant to sections 401(a)(9), 408(a)(6), and 408(b)(3) of the Internal Revenue Code, as amended by section 521 of the Tax Reform Act of 1984 (TRA of 1984). Because regulations will not be published in sufficient time to provide guidance necessary to enable plan administrators and individuals to make required minimum distributions for 1985 and 1986 from qualified plans and IRAs by December 31, 1986, this notice further delays the date by which minimum distributions for 1985 and 1986 must be made.

Section 401(a)(9), as amended, requires qualified plans to make minimum distributions to certain participants and beneficiaries. Sections 408(a)(6) and (b)(3), as amended, require that distributions from IRAs be made, pursuant to regulations of the Secretary, under rules similar to those of section 401(a)(9) for qualified plans.

Notice 86-1, 1986–1 C.B. 381, provided generally that minimum distributions required for calendar year 1985 need not be made until December 31, 1986 from qualified plans and IRAs. Initial distributions required under the minimum distribution rules by April 1 of a year are distributions for the previous calendar year. For example, distributions to a retired employee who attained age 70½ in calendar year 1985 that are not required to be made until April 1, 1986, are considered distributions for the 1985 calendar year. The notice also provided that an IRA with a current favorable opinion letter need not be amended to provide the distribution rules in section 408(a)(6) and (b)(3), as amended, until further notice.

Required Distributions

Minimum distributions for calendar years 1985 and 1986 will not be required to be made from qualified plans and IRAs by December 31, 1986, but instead such 1985 and 1986 distributions (plus, except in the case of an individual with a required beginning date of April 1, 1988, the minimum distribution required for calendar year 1987) will be required to be made by December 31, 1987.

Regulations on minimum distributions will be published by March 1, 1987. The regulations will provide specific guidance for calculating the amount of the minimum distributions required to be made by December 31, 1987 for calendar years 1985, 1986 and 1987. Further, distributions from qualified plans or IRAs made in 1985 or 1986 (except to the extent rolled over to another plan or IRA) with respect to taxpayers for whom minimum distributions are required for such years will be credited towards the minimum distributions required to be made by December 31, 1987.

Elections Under section 242(b) of TEFRA

Distributions required to be made under a designation permitted by the transitional rules contained in section 242(b) of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) are not affected by this notice. The amendments to section 401(a)(9) enacted by TEFRA were retroactively repealed by the TRA of 1984, but the transitional rule election contained in section 242(b) of TEFRA was preserved. This transitional rule provides that a designation of a method of distribution may have been made before January 1, 1984 with respect to distributions from a qualified plan and that distributions made under such a designation will not cause the plan to be disqualified under section 401(a)(9) as amended. Notice 83–23, 1983–2 C.B. 418 provides guidance for distributions permitted by this transitional rule and the requirements with respect to such distributions. Failure to make any distribution of an amount specified at the time specified under the method of distribution provided in a designation under section 242(b) of TEFRA will be treated as a change in the designation and, thus, a revocation of the designation.

IRA Amendments

A sponsor of a master of prototype IRA with an opinion letter issued on or before December 31, 1985 need not amend to provide for the distribution rules in sections 408(a)(6) and (b)(3), as amended, until further notice.

Reliance

The guidance in this Notice may be relied upon to comply with sections 401(a)(9), 408(a)(6) and 408(b)(3), as amended, with respect to distributions for the 1985 and 1986 calendar years.

Part IV. Items of General Interest

Notice of Proposed Rulemaking

Lobbying by Public Charities

EE–154–78

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to lobbying expenditures by certain tax exempt public charities that are described in section 501(c)(3) of the Internal Revenue Code of 1954. Changes to the applicable tax laws were made by the Tax Reform Act of 1976. The regulations will provide the organizations the guidance needed to comply with the Act, and will primarily affect organizations electing the expenditure test under section 501(h).

DATES: Written comments and requests for a public hearing must be delivered or mailed by February 3, 1987. The amendments to parts 7, 20, 25, and 56 are proposed to be effective for taxable years beginning after December 31, 1976. Amendments to §§1.170A–1, 1.501(c)(3)–1, 1.501(c)(4)–1, 1.6033–2, and §53.4945–2(a) are also proposed to be effective for taxable years beginning after December 31, 1976. Section 1.504–1 is proposed to be effective October 5, 1976. Section 1.504–2 and the amendments to §§53.4945–2(d)(1) are proposed to be effective February 3, 1987.

ADDRESS: Send comments and requests for a public hearing to: Commissioner of Internal Revenue,
Attention: CC:LR:T:EE–154–78, Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Paul G. Accettura of the Employee Plans and Exempt Organizations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention:
CC:LR:T:EE–154–78, telephone 202–566–3544 (not a toll-free call).

SUPPLEMENTARY INFORMATION: BACKGROUND

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1), Temporary Income Tax Regulations under the Tax Reform Act of 1976 (26 CFR Part 7), Estate Tax Regulations (26 CFR Part 20), Gift Tax Regulations (26 CFR Part 25). Foundation and Similar Excise Taxes (26 CFR Part 53), and Public Charity Excise Taxes (26 CFR part 56), under sections 170, 501(c)(3), 501(c)(4), 504, 2055, 2522, 4911, 4945, 6001, 6011, and 6033 of the Internal Revenue Code of 1954. These amendments are proposed to conform the regulations to section 1307 of the Tax Reform Act of 1976 (90 Stat. 1720) and are to be issued under the authority contained in sections 501(h)(6), 504(b), 4911(f)(3) and 7805 of the Internal Revenue Code of 1954 (90 Stat. 1721, 1722, 1726, 68A Stat. 917; 26 U.S.C. 501(h)(6), 504(b), 4911(f)(3), 7805).

PRIOR LAW

A publicly supported charity is not an organization described in section 501(c)(3) ("a section 501(c)(3) organization") unless any lobbying it does is limited to an insubstantial part of its activities. If it is determined that a substantial part of an organization's activities consists of attempts to influence legislation, the public charity will lose its tax-exempt status. Before the passage of the Tax Reform Act of 1976, there was uncertainty about what constituted a "substantial part" of an organization's activities. Congress was aware that the loss of tax exemption could constitute a severe blow to an organization or could in some cases, have relatively little effect. This uncertain effect could tend to discourage enforcement. Further, Congress was aware of the belief that the vague standards of the substantial part test tended to encourage subjective and selective enforcement.

EXPENDITURE TEST

Under sections 501(h) and 4911, added by section 1307 of the Tax Reform Act of 1976, certain section 501(c)(3) organizations may elect to spend up to a certain percentage of their "exempt purpose expenditures" to influence legislation without violating section 501(c)(3). If an organization elects the "expenditure test" of sections 501(h) and 4911, specific limits on lobbying expenditures apply. Separate limits, the "lobbying nontaxable amount" and the "grass roots nontaxable amount," are established for all lobbying expenditures and for grass roots lobbying expenditures, respectively. A 25 percent excise tax is imposed on the greater of the amount by which an organization's lobbying expenditures exceed its lobbying nontaxable amount or the amount by which its grass roots expenditures exceed its grass roots nontaxable amount. Additionally, "ceiling amounts" equal to 150 percent of the lobbying nontaxable amount and 150 percent of the grass roots lobbying nontaxable amount are established. If an organization's lobbying expenditures or grass roots expenditures normally exceed the corresponding ceiling amount, the organization will cease to be described in section 501(c)(3) and therefore will cease to be exempt from tax.

DENIAL OF DEDUCTION FOR OUT-OF-POCKET EXPENDITURES IN CONNECTION WITH LOBBYING

Code section 170 provides income tax rules governing the deductibility of charitable contributions made to public charities and certain other organizations, including churches and church related organizations. Under income tax regulations that are substantially unchanged since 1958, no deduction is allowed for expenditures for the "promotion or defeat of legislation" including out-of-pocket expenditures incurred in connection with lobbying on behalf of organizations referred to above.

Section 1307(c) of the Tax Reform Act of 1976 ("Act") added Code section 170(f)(6). That section denies a deduction for out-of-pocket expenditures made in connection with lobbying on behalf of a charitable organization, but contains a parenthetical exclusion relating to churches or church-related organizations ("Disqualified organizations"). The parenthetical exclusion in that section is consistent with Congressional intent that the rules in section 1307 of the Act not apply to disqualified organizations. *See e.g.*, S. Rep. No. 938 Part 2, 94th Cong., 2d Sess. (1976) 84, reprinted in 1976–3 C.B. Vol. 3 at 726. Accordingly, these proposed regulations do not construe the parenthetical language of section 170(f)(6) to permit a deduction for out-of-pocket expenditures made in connection with lobbying on behalf of a disqualified organization. Instead, the proposed regulations provide that out-of-pocket lobbying expenditures incurred on behalf of disqualified organizations are governed by prior law as if section 1307 of the Act had not been enacted. Thus, the proposed regulations do not affect the denial of deductibility, under present regulations, for out-of-pocket expenditures made in connection with lobbying on behalf of any organization other than an eligible organization.

ALLOCATIONS BETWEEN LOBBYING AND OTHER PURPOSES

Where an activity of an organization covered by these proposed regulations includes both lobbying and other purposes, the proposed regulations provide several specific rules. Section 56.4911-2(c)(1) provides that if any part of an advertisement constitutes grass roots lobbying, the entire amount expended for, or in connection with, the advertisement constitutes a grass roots expenditure. Section 56.4911-2(d)(2) provides that an expenditure that is both a fund raising expenditure and an expenditure for grass roots lobbying will be considered an expenditure for grass roots lobbying in full. However, if one of these special rules does not apply, §56.4911-2(d)(1) provides that an activity involving both lobbying and other purposes will require an allocation, based on all the facts and circumstances, between that part of the expenditure which is treated as a lobbying expenditure and that part which is treated as a nonlobbying expenditure. The Internal Revenue Service specifically requests comments on suggested factors to be taken into account in administering the facts and circumstances allocation rules of §56.4911-2(d)(1).

MAKING AVAILABLE THE RESULTS OF NONPARTISAN ANALYSIS, STUDY, OR RESEARCH

Code section 4911(d)(2)(A) provides that the term "influencing legislation" does not include making available the results of nonpartisan analysis, study, or research. These proposed regulations construe nonpartisan analysis, study, or research by cross-reference to §53.4945-2(d)(1) (relating to a similar exception to the private foundation rules regarding lobbying). In addition, this document proposes to amend §53.4945-2(d)(1)(iv) (relating to making available the results of nonpartisan analysis, study, or research) to provide that the exception does not apply if the method of distribution favors those persons interested solely in one side of a particular issue. This corresponds to the existing requirement that the distribution may not be limited to persons on one side of an issue and is intended to promote broad and equitable distribution of the analysis, study, or research, to all interested persons. The proposed amendment to §53.4945-2(d)(1) has a proposed effective date of ninety days after publication of this notice in the Federal Register.

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER.

REGULATORY FLEXIBILITY ACT; EXECUTIVE ORDER 12291; PAPERWORK REDUCTION ACT OF 1980

Although this document is a notice of proposed rulemaking which solicits public comment, the Internal Revenue Service has concluded that the regulations proposed herein are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act. Comments on these requirements should be sent to the Office of Information and Regulatory Affairs of OMB, Attention: Desk Officer for Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests that persons submitting comments on these requirements to OMB also send copies of those comments to the Service.

SUPERSESSION

These regulations, when published in final form in the Federal Register, will supersede §7.0(c)(4) of the Temporary Income Tax Regulations under the Tax Reform Act of 1976.

DRAFTING INFORMATION

The principal author of these proposed regulations was George Baker of the Employee Plans and Exempt Organizations Division of the Office of Chief Counsel. Other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

* * * * *

Proposed amendments to the regulations

A new Part 56, Public Charity Excise Taxes, is proposed to be added to Title 26 of the Code of Federal Regulations, and amendments to 26 CFR Parts 1, 7, 20, 25, and 53 are proposed as follows:

INCOME TAX REGULATIONS
[26 CFR Part 1]

Paragraph 1. The authority citation for part 1 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Sections 1.504-1 and 1.504-2 also issued under 26 U.S.C. 504(b).

Par. 2. Section 1.170A-1 is amended by revising paragraph (h)(5), adding a new paragraph (h)(11), and revising paragraph (i). These revised and added provisions read as follows:

§1.170A-1 Charitable, etc., contributions and gifts; allowance of deduction.

* * * * *

(h) *Exceptions and other rules.* * * *

(5) No deduction shall be allowed under section 170 for amounts paid to an organization—

(i) Which is disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, or

(ii) Which participates in, or intervenes in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

For purpose of determining whether an organization is attempting to influence legislation or is engaging in political activities, see sections 501(c)(3), 501(h), 4911 and the regulations thereunder.

* * * * *

(11) No deduction shall be allowed under section 170 for out-of-pocket expenditures on behalf of an eligible organization (within the meaning of §1.501(h)–2(b)(1)) if the expenditure is made in connection with influencing legislation (within the meaning of section 501(c)(3) or §56.4911–2), or in connection with the payment of the organization's tax liability under section 4911. For the treatment of similar expenditures on behalf of other organizations, see paragraph (h)(6) of this section.

(i) *Effective date.* In general this section applies to contributions paid in taxable years beginning after December 31, 1969. Paragraph (h)(11), however, applies only to out-of-pocket expenditures made in taxable years beginning after December 31 1976.

Par. 3. In §1.501(c)(3)–1, paragraph (b)(3) is amended by adding the following sentence at the end:

§1.501(c)(3)–1 Organizations organized and operated for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals.

* * * * *

(b) *Organizational text.* * * *

(3) *Authorization of legislative or political activities.* * * * An organization's articles will not violate the provisions of subdivision (i) of this paragraph (b)(3) even though the organization's articles expressly empower it to make the election provided for in section 501(h) with respect to influencing legislation and, only if it so elects, to make lobbying or grass roots expenditures that do not normally exceed the ceiling amounts prescribed by section 501(h)(2)(B) and (D).

* * * * *

Par. 4. In §1.501(c)(3)–1, paragraph (c)(3)(ii) is amended by adding a new sentence at the end of subdivision (ii) to read as follows:

§1.501(c)(3)–1 Organizations organized and operated for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals.

* * * * *

(c) *Operational test.* * * *

(3) *"Action" organizations.* * * *

(ii) * * * An organization for which the expenditure test election of section 501(h) is in effect for a taxable year will not be considered an "action" organization by reason of this subdivision (ii) for that year if it is not denied exemption from taxation under section 501(a) by reason of section 501(h).

* * * * *

Par. 5. In §1.501(c)(4)–1, paragraph (a)(2)(ii) is amended by revising the last sentence and adding a new sentence immediately thereafter. The revised and added sentences read as follows:

§1.501(c)(4)–1 Civic organizations and local associations of employees.

(a) *Civic organizations.* * * *

(2) *Promotion of social welfare.* * * *

(ii) *Political or social activities.* * * * A social welfare organization that is not, at any time after October 4, 1976, exempt from taxation as an organization described in section 501(c)(3) may qualify under section 501(c)(4) even though it is an "action" organization described in

§1.501(c)(3)–1(c)(3)(ii) or (iv), if it otherwise qualifies under this section. For rules relating to an organization that is, after October 4, 1976, exempt from taxation as an organization described in section 501(c)(3), see section 504 and §1.504–1.

* * * * *

Par. 6. The following new §§1.501(h)–1 through 1.501(h)–3 are added in the appropriate place:

§1.501(h)–1 Application of the "expenditure test" to expenditures to influence legislation; introduction.

(a) *Scope.* Section 501(c)(3) requires, among other things, that an organization described therein be one "no substantial part of the activities of which is carrying on propaganda, or otherwise attempting to influence legislation, (except as otherwise provided in subsection (h)." This requirement is referred to as the "substantial part test." Under section 501(h), certain organizations described in section 501(c)(3) (see §1.501(h)–2) may elect the "expenditure test" described in this section, §1.501(h)–2, and §1.501(h)–3, as a substitute for the substantial part test. An organization that elects the expenditure test under section 501(h) may make expenditures for lobbying or for grass roots lobbying within limits determined under section 4911(c) (the limits being referred to as the "lobbying nontaxable amount" and "grass roots nontaxable amount") without incurring an excise tax under section 4911(a) and without loss of tax exemption as an organization described in section 501(c)(3) by reason of section 501(h). However, if an electing organization's lobbying expenditures or grass roots expenditures exceed the corresponding nontaxable amount, the organization is subject to an excise tax on the excess (see §§56.4911–1 *et seq.*). Further, under section 501(h) (see §1.501(h)–3), if an electing organization's lobbying or grass roots expenditures normally exceed its "lobbying ceiling amount" or "grass roots ceiling amount" (150 percent of the corresponding nontaxable amounts), the organization will cease to be described in section 501(c)(3). An organization that elects the expenditures test may nevertheless be determined to be an action organization under §1.501(c)(3)–1(c)(3)(iii) or (iv). An organization that does not elect the expenditure test (including an organization not eligible to elect, or disqualified from making the election) remains subject to the substantial part test. The substantial part test is applied without regard to the provisions of section 501(h) and 4911 and the regulations thereunder.

(b) *Effective date.* The provisions of §§1.501(h)–1 through 1.501(h)–3, are effective for taxable years beginning after December 31, 1976. An election made before *[the date that final regulations are published in the Federal Register]* under the provisions of §7.0(c)(4) or the instructions to Form 5768 will be effective under these regulations without again filing Form 5768.

§1.501(h)–2 Electing the expenditure test.

(a) *In general.* The election to be governed by section 501(h) may be made by an eligible organization (as described in paragraph (b) of this section) for any taxable year of the organization beginning after December 31, 1976, other than the first taxable year for which a voluntary revocation of the election is effective (see paragraph (d) of this section). The election is made by filing a completed Form 5768, Election/Revocation of Election by an Eligible Section 501(c)(3) Organization to Make Expenditures to Influence Legislation, with the appropriate Internal Revenue Service Center listed on that form. Under section 501(h)(6), the election is effective with the beginning of the taxable year in which the form is filed. For example, if an eligible organization whose taxable year is the calendar year files Form 5768 on December 31, 1979, the organization is governed by section 501(h) for its taxable year beginning January 1, 1979. Once made, the expenditure test election is effective (without again filing Form 5768) for each succeeding taxable year for which the organization is an eligible organization and which begins before a notice of revocation is filed under paragraph (d) of this section.

(b) *Organizations eligible to elect the expenditure test*—(1) *In general.* For purposes of section 501 (h) and the regulations thereunder, an organization is an eligible organization for a taxable year if, for that taxable year, it is—

(i) Described in section 501(c)(3) (determined, in any year for which an election is in effect, without regard to the substantial part test to section 501(c)(3)),

(ii) Described in section 501(h)(4) and paragraph (b)(2) of this section, and

(iii) Not a disqualified organization described in section 501(h)(5) and paragraph (b)(3) of this section.

(2) *Certain organizations listed.* An organization is described in section 501(h)(4) and this paragraph (b)(2) if it is an organization described in—

(i) Section 170(b)(1)(A)(ii) (relating to educational institutions),

(ii) Section 170(b)(1)(A)(iii) (relating to hospitals and medical research organizations),

(iii) Section 170(b)(1)(A)(iv) (relating to organizations supporting government schools),

(iv) Section 170(b)(1)(A)(vi) (relating to organizations publicly supported by charitable contributions),

(v) Section 509(a)(2) (relating to organizations publicly supported by admissions, sales, etc.), or

(vi) Section 509(a)(3) (relating to organizations supporting public charities), but only if the organization it supports is described in section 501(c)(3).

(3) *Disqualified organizations.* An organization is a disqualified organization described in section 501(h)(5) and this paragraph (b)(3) if the organization is—

(i) Described in section 170(b)(1)(A)(i) (relating to churches),

(ii) An integrated auxiliary of a church or of a convention or association of churches (see §1.6033–2(g)(5)), or

(iii) Described in section 501(c)(3) and affiliated (within the meaning of §56.4911–7) with one or more organizations described in subdivision (i) or (ii) of this paragraph (b)(3).

(4) *Other organizations ineligible to elect.* Under section 501(h)(4), certain organizations, although not disqualified organizations, are not eligible to elect the expenditure test. For example, organizations described in section 509(a)(4) are not listed in section 501(h)(4) and therefore are not eligible to elect. Similarly, private foundations (within the meaning of section 509(a)) are not eligible to elect. For the treatment of expenditures by a private foundation for the purpose of carrying on propaganda, or otherwise attempting, to influence legislation, see §53.4945–2.

(c) *New organizations.* A newly created organization may submit Form 5768 to elect the expenditure test under section 501(h) before it is determined to be an eligible organization and may submit Form 5768 at the time it submits its application for recognition of exemption (Form 1023). If the newly created organization is determined to be an eligible organization, the election will be effective under the provisions of paragraph (a) of this section, that is, with the beginning of the taxable year in which the Form 5768 is filed by the eligible organization. However, if a newly created organization is determined by the Service to be a private foundation, section 4945(d)(1) and §53.4945–2 will apply and the organization will be liable for excise taxes under section 4945 on amounts expended in attempts to influence legislation. Also, if a newly created organization is neither a private foundation (see §1.501(h)–2(b)(4)) nor a disqualified organization (see §1.501(h)–2(b)(3)), but is determined by the Service not to be an eligible organization, the organization's election will not be effective and the substantial part test will apply from the effective date of its section 501(c)(3) classification.

(d) *Voluntary revocation of expenditure test election*—(1) *Revocation effective.* An organization may voluntarily revoke an expenditure test election by filing a notice of voluntary revocation with the appropriate Internal Revenue Service Center listed on Form 5768. Under section 501(h)(6)(B), a voluntary revocation is effective with the beginning of the first taxable year after the taxable year in which the notice is filed. If an organization voluntarily revokes its election, the substantial part test of section 501(c)(3) will apply with respect to the organization's activities in attempting to influence legislation beginning with the taxable year for which the voluntary revocation is effective.

(2) *Re-election of expenditure test.* If an organization's expenditure test election is voluntarily revoked, the organization may again make the expenditure test election, effective no earlier than for the taxable year following the first taxable year for which the revocation is effective.

(3) *Example. X*, an organization whose taxable year is the calendar year, plans to voluntarily revoke its expenditure test election effective beginning with its taxable year 1985. *X* must file its notice of voluntary revocation on Form 5768 after December 31, 1983 and before January 1, 1985. If *X* files a notice of voluntary revocation on December 31, 1984, the revocation is effective beginning with its taxable year 1985. The organization may again elect the expenditure test by filing Form 5768. Under paragraph (d)(2) of this section, the election may not be made for taxable year 1985. Under paragraph (a) of this section, a new expenditure test election will be effective for taxable years beginning with taxable year 1986, if the Form 5768 is filed after December 31, 1985, and before January 1, 1987.

(e) *Involuntary revocation of expenditure test election.* If, while an election by an eligible organization is in effect, the organization ceases to be an eligible organization, its election is automatically revoked. The revocation is effective with the beginning of the first full taxable year for which it is determined that the organization is not an eligible organization. If an organization's expenditure test election is involuntarily revoked under this paragraph (e) but the organization continues to be described in section 501(c)(3), the substantial part test of section 501(c)(3) will apply with respect to the organization's activities in attempting to influence legislation beginning with the first taxable year for which the involuntary revocation is effective.

(f) *Supersession.* This section supersedes §7.0(c)(4) of the Temporary Income Tax Regulations under the Tax Reform Act of 1976, effective [the date that final regulations are published in the Federal Register.]

1.501(h)–3 Lobbying or grass roots expenditures normally in excess of ceiling amount.

(a) *Scope.* This section provides rules under section 501(h) for determining whether an organization that has elected the expenditure test and that is not a member of an affiliated group of organizations (as defined in §56.4911–7(e)) either normally makes lobbying expenditures in excess of its lobbying ceiling amount or normally makes grass roots expenditures in excess of its grass roots ceiling amount. Under section 501(h) and this section, an organization that has elected the expenditure test and that normally makes expenditures in excess of the corresponding ceiling amount will cease to be exempt from tax under section 501(a) as an organization described in section 501(c)(3). For similar rules relating to members of an affiliated group of organizations, see §56.4911–9.

(b) *Loss of exemption*—(1) *In general.* Under section 501(h)(1), an organization that has elected the expenditure test shall be denied exemption from taxation under section 501(a) as an organization described in section 501(c)(3) for the taxable year following a determination year if—

(i) The sum of the organization's lobbying expenditures for the base years exceeds 150 percent of the sum of its lobbying nontaxable amounts for the base years, or

(ii) The sum of the organization's grass roots expenditures for its base years exceeds 150 percent of the sum of its grass roots nontaxable amounts for the base years.

The organization thereafter shall not be exempt from tax under section 501(a) as an organization described in section 501(c)(3) unless, pursuant to paragraph (d) of this section, the organization reapplies for recognition of exemption and is recognized as exempt.

(2) *Special exception for organization's first election.* For the first, second, or third consecutive determination year for which an organization's first expenditure test election is in effect, no determination is required under paragraph (b)(1) of this section, and the organization will not be denied exemption from tax by reason of section 501(h) and this section if, taking into account as base years only those years for which the expenditure test election is in effect—

(i) The sum of the organization's lobbying expenditures for such base years does not exceed 150 percent of the sum of its lobbying nontaxable amounts for the same base years, and

(ii) The sum of the organization's grass roots expenditures for those base years does not exceed 150 percent of the sum of its grass roots nontaxable amounts for such base years.

If an organization does not satisfy the requirements of this paragraph (b)(2), paragraph (b)(1) of this section will apply.

(c) *Definitions.* For purposes of this section—

(1) The term "lobbying expenditures" means lobbying expenditures as defined in section 4911(c)(1) or section 4911(f)(4)(A) and §56.4911–2(a).

(2) The term "lobbying nontaxable amount" is defined in §56.4911–1(c)(1).

(3) An organization's "lobbying ceiling amount" is 150 percent of the organization's lobbying nontaxable amount for a taxable year.

(4) The term "grass roots expenditures" means grass roots expenditures as defined in section 4911(c)(3) or section 4911(f)(4)(A) and §56.4911–2(c).

(5) The term "grass roots nontaxable amount" is defined in §56.4911–1(c)(2).

(6) An organization's "grass roots ceiling amount" is 150 percent of the organization's grass roots nontaxable amount for a taxable year.

(7) In general, the term "base years" means the determination year and the three taxable years immediately preceding the determination year. The base years, however, do not include any taxable year preceding the taxable year for which the organization is first treated as described in section 501(c)(3).

(8) A taxable year is a "determination year" if it is a year for which the expenditure test election is in effect, other than the taxable year for which the organization is first treated as described in section 501(c)(3).

(d) *Reapplication for recognition of exemption*—

(1) *Time of application.* An organization that is denied exemption from taxation under section 501(a) by reason of section 501(h) and this section may apply on Form 1023 for recognition of exemption as an organization described in section 501(c)(3) for any taxable year following the first taxable year for which exemption is so denied. See subparagraphs (2) and (3) of this paragraph (d) for material to be included with an application described in the preceding sentence.

(2) *Section 501(h) calculation.* An application described in paragraph (d)(1) of this section must demonstrate that the organization would not be denied exemption from taxation under section 501(a) by reason of section 501(h) if the expenditure test election had been in effect for all of its last taxable year ending before the application is made by providing the calculations, described either in paragraph (b)(1)(i) and (ii) of this section or in §56.4911–9(b), that would have applied to the organization for that year.

(3) *Operations for disqualifying.* An application described in paragraph (d)(1) of this section must include information that demonstrates to the satisfaction of the Commissioner that the organization will not knowingly operate in a manner that would disqualify the organization for tax exemption under section 501(c)(3) by reason of attempting to influence legislation.

(4) *Re-election of expenditure test.* If an organization is denied exemption from tax for a taxable year by reason of section 501(h) and this section, and thereafter is again recognized as an organization described in section 501(c)(3) pursuant to this paragraph (d), it may again elect the expenditure test under section 501(h) in accordance with §1.501(h)–2(a).

(e) *Examples.* The provisions of this section are illustrated by the following examples, which also illustrate the operation of the tax imposed by section 4911.

Example (1). (1) The following table contains information used in this example concerning organization *X*.

Year	Exempt Purpose Expenditures (EPE)	Calculation	Lobbying Nontaxable Amount (LNTA)	Lobbying Expenditures (LE)
1979	$400,000	(20% of $400,000 =)	$80,000	$100,000
1980	$300,000	(20% of $300,000 =)	$60,000	$100,000
1981	$600,000	(20% of $500,000 + 15% of $100,000 =)	$115,000	$120,000
1982	$500,000	(20% of $500,000 =)	$100,000	$100,000
Totals:	$1,800,000		$355,000	$420,000

(2) Organization *X*, whose taxable year is the calendar year, was organized in 1971. *X* first made the expenditure test election under section 501(h) effective for taxable years beginning with 1979 and has not revoked the election. None of *X*'s lobbying expenditures for its taxable years 1979 through 1982 are grass roots expenditures. Under section 4911(a) and §56.4911–1(a), *X* must determine for each year for which the expenditure test election is effective whether it is liable for the 25 percent excise tax imposed by

section 4911(a) on excess lobbying expenditures. *X* is liable for this tax for each of its taxable years 1979, 1980 and 1981, because in each year its lobbying expenditures exceeded its lobbying nontaxable amount for the year. For 1979, the tax imposed by section 4911(a) is $5,000 [25% × ($100,000 − $80,000) = $5,000]. For 1980, the tax is $10,000. For 1981, the tax is $1,250.

(3) The taxable years 1979 through 1981 are all determination years under paragraph (c)(8) of this section. On its annual return for determination year 1979, the first year of its first election, *X* can demonstrate, under paragraph (b)(2) of this section, that its lobbying expenditures during 1979 ($100,000) do not exceed 150 percent of its lobbying nontaxable amount for 1979 ($120,000). For determination year 1980, under paragraph (b)(2), *X* can demonstrate that the sum of its lobbying expenditures for 1979 and 1980 ($200,000) does not exceed 150 percent of the sum of its lobbying nontaxable amounts for 1979 and 1980 ($210,000). For 1981, under paragraph (b)(2), *X* can demonstrate that the sum of its lobbying expenditures for 1979, 1980, and 1981 ($320,000) does not exceed 150 percent of the sum of its lobbying nontaxable amounts for 1979, 1980, and 1981 ($382,500). For each of the determination years 1979, 1980, and 1981, the first three years of its first election, *X* satisfies the requirements of paragraph (b)(2). Accordingly, no determination under paragraph (b)(1) of this section is required for those years, and *X* is not denied tax exemption by reason of section 501(h).

(4) Under paragraph (b)(1) of this section, *X* must determine for its determination year 1982 whether it has normally made lobbying expenditures in excess of the lobbying ceiling amount. This determination takes into account expenditures in base years 1979 through 1982. The sum of *X*'s lobbying expenditures for the base years ($420,000) does not exceed 150% of the sum of the lobbying nontaxable amounts for the base years (150% × $355 000 = $532,500). Accordingly, *X* is not denied tax exemption by reason of section 501(h).

Example (2). (1) The following table contains information used in this example concerning *W*.

Year	Exempt Purpose Expenditures (EPE)	Calculation	Lobbying Nontaxable Amount (LNTA)	Lobbying Expenditures (LF)	Grass roots Nontaxable Amount (25% of LNTA)	Grass roots Expenditures
1979	$700,000	(20% of $500,000 + 15% of $200,000 =)	$130,000	$120,000	$32,500	$30,000
1980	$800,000	(20% of $500,000 + 15% of $300,000 =)	$145,000	$100,000	$36,250	$60,000
1981	$800,000	(20% of $500,000 + 15% of $300,000 =)	$145,000	$100,000	$36,250	$65,000
1982	$900,000	(20% of $500,000 + 15% of $400,000 =)	$160,000	$150,000	$40,000	$65,000
Totals:	$3,200,000		$580,000	$470,000	$145,000	$220,000

(2) Organization *W*, whose taxable year is the calendar year made the expenditure test election under section 501(h) effective for taxable years beginning with 1979 and has not revoked the election. *W* has been treated as an organization described in section 501(c)(3) for each of its taxable years beginning with its taxable year 1974.

(3) Under section 4911(a) and §56.4911–1(a), *W* must determine for each year for which the expenditure test election is effective whether it is liable for the 25 percent excise tax imposed by section 4911(a) on excess lobbying expenditures. In 1980, 1981, and 1982, *W* has excess lobbying expenditures because its grass roots expenditures in each of those years exceeded its grass roots nontaxable amount for the year. Therefore, *W* is liable for the excise tax under section 4911(a) for those years. The tax imposed by section 4911(a) for 1980 is $5,937.50 [25% × ($60,000 − $36,250) = $5,937.50]. For 1981, the tax is $7,187.50. For 1982, the tax is $6,250.

(4) On its annual return for its determination years 1979, 1980, and 1981, the first three years of its first election, *W* demonstrates that it satisfies the requirements of paragraph (b)(2) of this section. Accordingly, no determination under paragraph (b)(1) of this section is required for those years, and *W* is not denied tax exemption by reason of section 501(h).

(5) On its annual return for its determination year 1982, *W* must determine under paragraph (b)(1) whether it has normally made lobbying expenditures or grass roots expenditures in excess of the corresponding ceiling amount. This determination takes into account expenditures in base years 1979 through 1982. The sum of *W*'s lobbying expenditures for the base years ($470,000) does not exceed 150% of the sum of *W*'s lobbying nontaxable amounts for those years (150% × $580,000 = $870,000). However, the sum of W's grass roots expenditures for the base years ($220,000) does exceed 150% of the sum of *W*'s grass roots nontaxable amounts for those years (150% × $145,000 = $217,500). Under section 501(h), *W* is denied tax exemption under section 501(a) as an organization described in section 501(c)(3) for its taxable year 1983. For its taxable year 1984, and any taxable year thereafter, *W* is exempt from tax as an organization described in section 501(c)(3) only if *W* applies for recognition of its exempt status under paragraph (d) of this section and is recognized as exempt from tax.

Example (3). (1) The following table contains information used in this example concerning organization *Y*.

Year	Exempt Purpose Expenditures (EPE)	Calculation	Lobbying Nontaxable Amount (LNTA)	Lobbying Expenditures (LF)	Grass roots Nontaxable Amount (25% of LNTA)	Grass roots Expenditures
1977	$700,000	(20% of $500,000 + 15% of $200,000 =)	$130,000	$182,000	$32,500	$30,000
1978	$800,000	(20% of $500,000 + 15% of $300,000 =)	$145,000	$224,750	$36,250	$35,000
Subtotal:	$1,500,000		$275,000	$406,750	$68,750	$65,000
1979	$900,000	(20% of $500,000 + 15% of $400,000 =)	$160,000	$246,000	$40,000	$50,000
Total:	$2,400,000		$435,000	$670,750	$108,750	$115,000

(2) Organization *Y*, whose taxable year is the calendar year, was first treated as an organization described in section 501(c)(3) on February 1, 1977. Y made the expenditure test election under section 501(h) effective for taxable years beginning with 1977 and has not revoked the election.

(3) For 1977, *Y* has excess lobbying expenditures of $52,000 because its lobbying expenditures ($182,000) exceed its lobbying nontaxable amount ($130,000) for the taxable year. Accordingly, *Y* is liable for the 25 percent excise tax imposed by section 4911(a). The amount of the tax is $13,000 [25% × $52,000 = $13,000].

(4) For 1978, *Y* again has excess lobbying expenditures and is again liable for the 25 percent excise tax imposed by section 4911(a). The amount of the tax is $19,937.50 [25% × ($224,750 − $145,000) = $19,937.50].

(5) For 1979, *Y's* lobbying expenditures ($264,000) exceed its lobbying nontaxable amount ($160,000) by $104,000, and its grass roots expenditures ($50,000) exceed its grass roots nontaxable amount ($40,000) by $10,000. Under §56.4911–1(b), *Y's* excess lobbying expenditures are the greater of $104,000 or $10,000. The amount of the tax, therefore, is $26,000 [25% × $104,000 = $26,000].

(6) Under paragrah (c)(8) of this section, 1977 is not a determination year because it is the first year for which the organization is treated as described in section 501(c)(3). For 1977, *Y* need not determine whether it has normally made lobbying expenditures or grass roots expenditures in excess of the corresponding ceiling amount for purposes of determining whether it is denied exemption under section 501(h) for its taxable year 1978.

(7) For determination year 1978, *Y* must determine whether it has normally made lobbying or grass roots expenditures in excess of the corresponding ceiling amount, taking into account expenditures for the base years 1977 and 1978. For *Y*, the determination under paragraph (b)(2) of this section considers the same base years as the determination under paragraph (b)(1) of this section and is, therefore, redundant. Accordingly, *Y* proceeds to determine, under (b)(1), whether it is denied exemption. *Y's* grass roots expenditures for 1977 and 1978 ($65,000) did not exceed 150 percent of the sum of its grass roots nontaxable amounts for those years ($103,125). *Y's* lobbying expenditures for 1977 and 1978 ($406,750) did not exceed 150% of its lobbying nontaxable amount for those years (150% × $275,000 = $412,500). Therefore, *Y* is not denied tax exemption under section 501(h) for its taxable year 1979.

(8) For determination year 1979, the sum of *Y's* grass roots expenditures in base years 1977, 1978, and 1979 does not exceed 150 percent of its grass roots nontaxable amount (calculation omitted). However, the sum of *Y's* lobbying expenditures for the base years ($670,750) does exceed 150% of the sum of the lobbying nontaxable amounts for those years (150% × $435,000 = $652,500). Since *Y* was not described in section 501(c)(3) prior to 1977, ony the years 1977, 1978, and 1979 may be considered in determining whether *Y* has normally made lobbying expenditures in excess of its lobbying ceiling. Therefore, *Y* determines that it has normally made lobbying expenditures in excess of its lobbying ceiling. Under section 501(h), *Y* is denied tax exemption under section 501(a) as an organization described in section 501(c)(3) for its taxable year 1980. For its taxable year 1981, and any taxable year thereafter, *Y* is exempt from tax as an organization described in section 501(c)(3) only if *Y* applies for recognition of its exempt status under paragraph (d) of this section and is recognized as exempt from tax.

Par. 7. Existing section 1.504–1 is removed and new §§1.504–1 and 1.504–2, to read as follows, are added in the appropriate place:

§1.504–1 Attempts to influence legislation; certain organizations formerly described in section 501(c)(3) denied exemption.

Section 504(a) and this section apply to an organization that is exempt from taxation at any time after October 4, 1976, as an organization described in section 501(c)(3), and that ceases to be described in that section because it—

(a) Is an "action" organization, within the meaning of §1.501(c)(3)–1(c)(3)(ii) or (iv), on account of activities occurring after October 4, 1976, or

(b) Is denied exemption under the provisions of section 501(h) (see §1.501(h)–3 or §56.4911–9).

This section does not apply, however, to an organization that was described in section 501(h)(5) and §1.501(h)–2(b)(3) (relating generally to churches) for its taxable year immediately preceding the first taxable year for which it is no longer an organization described in section 501(c)(3). An organization to which section 504(a) and this section apply shall not be treated as described in section 501(c)(4) at any time after the organization ceases to be described in section 501(c)(3). Further, an organization denied treatment as an organization described in section 501(c)(4) under this section may not be treated as an organization described in section 501(c) other than as an organization described in section 501(c)(3). For rules relating to recognition of exemption after exemption is denied under section 501(h), see §1.501(h)–3(d).

§1.504–2 Certain transfers made to avoid section 504(a).

(a) *Scope.* Under section 504(b), a transfer described in paragraph (b) or (c) of this section to an organization exempt from tax under section 501(a) may result in loss of exemption by the transferee unless the Commissioner determines, under paragraph (e) of this section, that the original transfer did not effect an avoidance of section 504(a). For purposes of this section, the term "transfer" includes any use by, or for the benefit of, the recipient of the transfer, but does not include any transfer made for adequate and full consideration.

(b) *Transferor and transferee commonly controlled—(1) Loss of exemption.* A transfer is described in this paragraph (b) if it is described in paragraph (b)(2) through (b)(6). The transferee of a transfer described in this paragraph will cease to be exempt from tax under section 501(a), unless the provisions of paragraph (e) of this section apply.

(2) *Transferor organization.* A transfer is described in this paragraph (b)(2) only if it is from an organization that—

(i) Is or was described in section 501(c)(3), but not in section 501(h)(5), and

(ii) Is determined to be an "action" organization (as defined in §1.501(c)(3)–1(c)(3)(ii) or (iv)), or is denied exemption from tax by reason of section 501(h) and either §1.501(h)–3 or §56.4911–9.

(3) *Transferor and transferee commonly controlled.* A transfer is described in this paragraph (b)(3) only if, at the time of the transfer or at any time during the transferee's ten taxable years following the year in which the transfer was made, the transferee is controlled (directly or indirectly), as defined in paragraph (f) of this section, by the same person or persons who control the transferor.

(4) *Time of transfer.* A transfer is described in this paragraph (b)(4) only if the transfer is made after February 3, 1987, and—

(i) After the date that is 24 months before the earliest of the effective date of the determination under section 501(h) that the transferor is not exempt, the effective date of the Commissioner's determination that the transferor is an "action" organization (as defined in §1.501(c)(3)(ii) or (iv)), or the date on which the Commissioner proposes to treat it as no longer described in section 501(c)(3), and

(ii) Before the transferor again is recognized as an organization described in section 501(c)(3).

(5) *Transferee.* A transfer is described in this paragraph (b)(5) only if the transferee is exempt from tax under section 501(a) but the transferee is neither—

(i) An organization described in section 501(c)(3), nor

(ii) An organization described in section 401(a) to which the transferor contributes as an employer.

(6) *Amount of transfer.* A transfer is described in this paragraph (b)(6) only if the amount of the transfer exceeds the lesser of 30 percent of the transferor's assets, or 50 percent of the transferee's assets, computed immediately before the transfer. For purposes of this paragraph (b)(6)—

(i) The amount of a transfer by a transferor is the sum of the amounts transferred to any number of transferees in any number of transfers, all of which are described in paragraphs (b)(2) through (b)(5) of this section, and the time of the transfer is the time of the first transfer so taken into account; and

(ii) The amount of a transfer to a transferee is the sum of the amounts transferred by a transferor to the transferee in any number of transfers, all of which are described in paragraphs (b)(2) through (b)(5) of this section, and the time of the transfer is the time of the first transfer so taken into account.

(c) *Other transfers—(1) Transfers included.* A transfer is described in this paragraph (c) if it would be described in paragraph (b) of this section except that either—

(i) The amount of the transfer is less than the amount determined in paragraph (b)(6) of this section, or

(ii) The transferor and transferee are not commonly controlled as described in paragraph (b)(3) of this section, or

(iii) The transferee is an organization described in sections 501(c)(3) and 501(h)(4).

(2) *Loss of exemption.* The transferee of a transfer described in this paragraph (c) will cease to be exempt under section 501(a) if the Commissioner determines on all the facts and circumstances that the transfer effected an avoidance of section 504(a). In determining whether a transfer effected an avoidance of section 504(a), the Commissioner may consider whether the transferee engages, or has engaged, in attempts to influence legislation and may also consider any of the factors enumerated in paragraph (e) of this section.

(d) *Date of loss of exempt status.* A transferee of a transfer described in paragraph (b)(c)(1)(ii), or (c)(1)(iii) of this section will cease to be exempt from tax under section 501(a) on the date that all the requirements of paragraph (b), (c)(1)(ii), or (c)(1)(iii) (other than the determination by the Commissioner) are satisfied. A transferee of a transfer described in paragraph (c)(1)(i) of this section will cease to be exempt from tax under section 501(a) on the date of the last transfer preceding notification of the transferee that the Commissioner proposes to treat the transferee as other than an exempt organization.

(e) *Transfers not in avoidance of section 504(a).* Notwithstanding paragraph (b) of this section, if, based on all the facts and circumstances, the Commissioner determines that a transfer described in paragraph (b) did not effect an avoidance of section 504(a), the transferee will not be denied exemption from tax by reason of section 504(b) and this section. In making the determination called for in the preceding sentence, the Commissioner may consider all relevant factors including:

(1) Whether enforceable and effective conditions on the transfer preclude use of any of the transferred assets for any purpose that, if it were a substantial part of an organization's activities, would be inconsistent with exemption as an organization described in section 501(c)(3);

(2) In the absence of conditions described in paragraph (e)(1) of this section, whether the transferred assets are used exclusively for purposes that are consistent with the transferor's exemption as an organization described in section 501(c)(3);

(3) Whether the assets transferred would be described in §53.4942(a)–2(c)(3) before, as well as after, the transfer if both the transferor and transferee were private foundations;

(4) Whether and to what extent the transfer would satisfy the provisions of §1.507–2(a)(7) and (8) if the transferor were a private foundation;

(5) Whether all of the transferred assets have been expanded during a period when the transferee was not controlled (directly or indirectly) by the same person or persons who controlled the transferor; and

(6) Whether the entire amount of the transferred assets were in turn transferred, before the close of the transferee's taxable year following the taxable year in which the transferred assets were received, to one or more organizations described in section 507(b)(1)(A) none of which controlled (directly or indirectly) by the same persons who control either the original transferor or transferee.

(f) *Control.* For purposes of section 504 and the regulations thereunder—

(1) The transferor will be presumed to control any organization with which it is affiliated within the meaning of §56.4911–7(a), or would be if both organizations were described in section 501(c)(3), and

(2) The transferee will be treated as controlled (directly or indirectly) by the same person or persons who control the transferor if the transferee would be treated as controlled under section 53.4942(a)–3(a)(3), for which purpose the transferor shall be treated as a private foundation.

Par. 8. Section 1.6033–2 is amended by adding paragraph (a)(2)(ii)(*k*). This added provision reads as follows:

§1.6033–2 Returns by exempt organizations; taxable years beginning after December 31, 1969.

(a) *In general.* * * *

(2) * * *

(ii) * * *

(*k*) Its lobbying expenditures, grass roots expenditures, exempt purpose expenditures, lobbying nontaxable amount, and grass roots nontaxable amount for the taxable year and for prior taxable years that are base years (within the meaning of §1.501(h)–3(c)(7)), if the organization has an election under section 501(h) in effect for the taxable year. An organization that is a member of an affiliated group of organizations (as defined in §56.4911–7(e)) but that is not a member of a limited affiliated group (as defined in §56.4911–10(b)) shall report this information based on the expenditures of all members of the group during the taxable year of the group that ends with or within the member's taxable year and for prior taxable years of the group that are base years (within the meaning of §56.4911–9(b)). For additional information required to be furnished by members of an affiliated group of organizations, and by controlling members in a limited affiliated group, see §§56.4911–9(d) and 56.4911–10(f)(1), respectively.

* * * * *

TEMPORARY INCOME TAX REGULATIONS UNDER THE TAX REFORM ACT OF 1976

[26 CFR Part 7]

Par. 9. The authority citation for part 7 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 10. In §7.0, paragraph (c)(4) is removed and paragraph (d) is amended by removing ", (c)(4)" from the first parenthetical phrase in the first sentence.

ESTATE TAX REGULATIONS

[26 CFR Part 20]

Par. 11. The authority citation for part 20 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 12. Section 20.2055–1(a)(2) is revised to read as follows:

§20.2055–1 Deduction for transfers for public, charitable, and religious uses; in general.

(a) *General rule.* * * *

(2) To or for the use of any corporation or association organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes (including the encouragement of art and for the prevention of cruelty to children or animals), if no part of the net earnings of the corporation or association inures to the benefit of any private stockholder or individual (other than as a legitimate object of such purposes), if the organization is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and if, in the case of transfers made after December 31, 1969, it does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

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GIFT TAX REGULATIONS

[26 CFR Part 25]

Par. 13. The authority citation for part 25 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 14. In §25.2522(a)–1, paragraph (a)(2) is revised to read as follows:

§25.2522(a)–1 Charitable and similar gifts; citizens or residents.

(a) * * *

(2) Any corporation, trust, community chest, fund, or foundation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, including the encouragement of art and the prevention of cruelty to children or animals, if no part of the net earnings of the organization inures to the benefit of any private shareholder or individual, if it is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and if, in the case of gifts made after December 31, 1969, it does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

* * * * *

Par. 15. In §25.2522(a)–1, paragraph (b)(2) is revised to read as follows:

§25.2522(a)–1 Charitable and similar gifts; citizens or residents.

(b) * * *

(2) It must not be disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation.

* * * * *

FOUNDATION AND SIMILAR EXCISE TAXES
[26 CFR Part 53]

Par. 16. The authority citation for part 53 continues to read in part:

Authority: 26 U.S.C. 7805 * * *

Par. 17. Section 53.4945–2 is amended as follows:

1. Paragraph (a)(5)(i) is revised to read as set forth below and paragraph (a)(5)(iii) is removed;
2. Paragraphs (a)(6) and (a)(7) are added as set forth below; and
3. In paragraph (d)(1)(iv), the last sentence is revised to read as set forth below.

§53.4945–2 Propaganda influencing legislation.

(a) *Propaganda influencing legislation, etc.* * * *

(5) *Grants to public organizations*—(i) *In general.* A grant by a private foundation to an organization described in section 509(a)(1), (2), or (3) does not constitute a taxable expenditure by the foundation under section 4945(d), other than under section 4945(d)(1), if the grant by the private foundation is not earmarked to be used for any activity described in section 4945(d)(2) or (5), is not earmarked to be used in a manner which would violate section 4945(d)(3) or (4), and there does not exist an agreement, oral or written, whereby the grantor foundation may cause the grantee to engage in any such prohibited activity or to select the recipient to which the grant is to be devoted. For purposes of this subdivision, a grant by a private foundation is earmarked if the grant is given pursuant to an agreement, oral or written, that the grant will be used for specific purposes. For the expenditure responsibility requirements with respect to organizations other than those described in section 509(a)(1), (2), or (3), see §53.4945–5. For rules for determining whether grants to public charities are taxable expenditures under section 4945(d)(1), see paragraphs (a)(6) and (a)(7) of this section.

* * * * *

(6) *Grants to public organizations that attempt to influence legislation*—(i) *In general.* A grant made by a private foundation to an organization described in section 509(a)(1), (2), or (3) (a "public charity" for purposes of paragraphs (a)(6) and (7) of this section), does not constitute a taxable expenditure under section 4945(d)(1) if it meets the requirements of this paragraph (a)(6).

(ii) *General support grant.* A general support grant by a private foundation to a public charity is not a taxable expenditure by the private foundation under section 4945(d)(1) to the extent that—

(A) The grant is not earmarked, within the meaning of §56.4911–4(f)(4), to be used in connection with an attempt to influence legislation, and

(B) The amount of the grant (as defined in paragraph (a)(6)(iv)(A) of this section)) does not exceed the greater of the amount expended by the grantee in the taxable year preceding the year of the grant or the amount budgeted for the year of the grant by the grantee for the sum of expenditures that constitute exempt purpose expenditures (within the meaning of §56.4911–4) other than lobbying expenditures (within the meaning of §56.4911–2(a)), plus expenditures for fund raising (see §56.4911–4(f)(1)).

(iii) *Specific project grant.* A grant by a private foundation to fund a specific project of a public charity is not a taxable expenditure by the foundation under section 4945(d)(1) to the extent that—

(A) The grant is not earmarked, within the meaning of §56.4911–4(f)(4), to be used in connection with an attempt to influence legislation, and

(B) The amount of the grant (as defined in paragraph (a)(6)(iv)(B) of this section) does not exceed the amount budgeted for the year of the grant by the granted organization for specific project activities that are not attempts to influence legislation.

(iv) *Special rules.* For purposes of paragraph (a)(6) of this section, the amount of a grantor's grant is the sum of—

(A) The sum of the grantor's general support grants (if any) and all specific project grants (if any) made to the same grantee for the same taxable year of the grantee, or

(B) The sum of the grantor's general support grants (if any) plus the grant for the specific project (but not grants for other specific projects, if any) made to the same grantee for the same taxable year of the grantee, plus

(C) Each grant (if any) attributed to the grantor even if made by another private foundation. For purposes of this paragraph (a)(6)(iv)(C), a grant is attributed to one private foundation (even if made by a second foundation) only if made in the same taxable year of the grantee to the same grantee under an oral or written agreement between the private foundation to which it is attributed and the other private foundation to make the grant. A grant described in the preceding sentence is counted once by each foundation.

(7) *Grants to organizations that cease to be described in 501(c)(3)—(i) Not taxable expenditure; conditions.* A grant to a public charity (as defined in paragraph (a)(6)(i) of this section) that thereafter ceases to be an organization described in section 501(c)(3) by reason of its attempts to influence legislation is not a taxable expenditure if—

(A) The grant meets the requirements of paragraph (a)(6) of this section,

(B) The grant is made before notice of the grantee organization's loss of tax exemption is given to the public,

(C) At the time the grant is made, no foundation manager (as defined in section 4946(b)(1)) of the grantor private foundation knows (or in the case of the taxes imposed by section 4945(a)(1) and (b)(1), has reason to know) that the grantee organization's ruling or determination letter has been or will be revoked, or is aware of the activities which would provide the basis for the revocation, and

(D) No disqualified person with respect to the private foundation, during the grantee's taxable year in which the grant is made, or the preceding or succeeding taxable year, controls, in whole or in part, the grantee organization's attempts to influence legislation.

(ii) *Examples.* The provisions of paragraphs (a)(6) and (a)(7) of this section are illustrated by the following examples:

Example (1). W, a private foundation, makes a general purpose grant to *Z*, a public charity described in section 509(a)(1). As an insubstantial portion of its activities, *Z* makes some attempts to influence the State legislature with regard to changes in the mental health laws. The amount of *Z*'s nonlobbying expenditures for the taxable year prior to the grant, as well as the amount budgeted for those expenditures for the taxable year of the grant, far exceed the amount of *W*'s general purpose grant. The use of the grant is not earmarked by *W* to be used in a manner which would violate section 4945(d)(1). In addition, there is no oral or written agreement whereby *W* may influence the choice by *Z* of the activity or recipient to which the grant is to be devoted. Even if the grant is subsequently devoted by *Z* to its legislative activities the grant by *W* is not a taxable expenditure under section 4945(d).

Example (2). *X*, a private foundation, makes a specific project grant to *Y* University for the purpose of conducting research on the potential environmental effects of certain pesticides. *X* does not earmark the grant for any purpose which would violate section 4945(d)(1) and there is no oral or written agreement or understanding whereby *X* may cause *Y* to engage in any activity described in section 4945(d)(1), (2), or (5), or to select any recipient to which the grant may be devoted. Further, *X* determines that *Y*'s budget for the project is reasonable and does not contain any amount for attempts to influence legislation. *Y* uses most of the funds for the research project; however, on its own volition, *Y* expends a portion of the grant funds to send a representative to testify at Congressional hearings on a specific bill proposing certain pesticide control measures. The portion of the grant funds expended with respect to the Congressional hearings is not treated as a taxable expenditure by *X* under section 4945(d)(1).

Example (3). *M*, a private foundation, makes a specific project grant of $150,000 to *P*, a public charity described in section 509(a)(1). In requesting the grant from *M*, *P* stated that the total budgeted cost of the project is $200,000, and that of this amount $20,000 is allocated to attempts to influence legislation related to the project. In making the grant, *M* did not earmark any of the funds from the grant to be used for attempts to influence legislation. *M*'s grant of $150,000 to *P* will not constitute a taxable expenditure under section 4945(d)(1) because *M* did not earmark any of the funds for attempts to influence legislation and because the amount of its grant ($150,000) does not exceed the amount allocated to specific project activities that are not attempts to influence legislation ($200,000 – $20,000 = $180,000).

Example (4). Assume the same facts as in example (3), except that *M*'s grant letter to *P* provides that *M* has the right to renegotiate the terms of the grant if there is a substantial deviation from those terms. This additional fact does not make *M*'s grant a taxable expenditure under section 4945(d)(1).

Example (5). Assume the same facts as in example (3), except that *M* made a specific project grant of $200,000 to *P*. Part of *M*'s grant of $200,000 will constitute a taxable expenditure under section 4945(d)(1). The amount of the grant ($200,000) exceeds by $20,000 the amount *P* allocated to specific project activities that are not attempts to influence legislation ($180,000). *M* has made a taxable expenditure of $20,000.

Example (6). Assume the same facts as example (3), except that *M* made a specific project grant of $180,000, and received from *P* an enforceable commitment that grant funds would not be used in connection with attempts to influence legislation. *M*'s grant is not a taxable expenditure under section 4945(d)(1).

Example (7). Assume the same facts as in example (3) except that *M* directed *P* to hire *A*, an individual, to expend $20,000 from the grant to engage in direct lobbying (within the meaning of §56.4911–2(b)) and grass roots lobbying (within the meaning of §56.4911–2(c)). *P* does not expend any other grant funds for lobbying activities. The $20,000 that is earmarked for direct lobbying and grass roots lobbying is a taxable expenditure under section 4945(d)(1).

Example (8). *R*, a public charity described in section 509(a)(1), requested *N*, a private foundation, to make a general purpose grant to it to aid *R* in carrying out its exempt purpose. In making this request, *R* notified *N* that it had elected the expenditure test under section 501(h) and that it expected to attempt to influence legislation in areas related to its exempt purpose. Since its formation, *R* generally has had exempt purpose expenditures (as defined in §56.4911–4) in excess of $7,000,000 in each of its taxable years, and has budgeted in excess of $7,000,000 of exempt purpose expenditures for the year of the grant. *N* made a grant of $200,000 to *R*. *N* did not earmark the funds for *R*'s attempts to influence legislation. The general purpose grant by *N* does not constitute a taxable expenditure under section 4945(d)(1).

Example (9). Assume the same facts as in example (8), except that *N* learns that *R* has had excess lobbying expenditures (within the meaning of §56.4911–1(b)) in some prior years. *N* also learns that in no year has *R*'s lobbying or grass roots expenditures (within the meaning of §56.4911–2(a) and (c)) exceeded the corresponding ceiling amount (within the meaning of §1.501(h)–3(c)(3) and (6)). *N* then makes the grant to *R*. After receiving the grant, *R* spends a large portion of its funds on influencing legislation and, as a consequence, is denied exemption from tax, as an organization described in section 501(c)(3), under section 501(h) and §1.501(h)–3. No disqualified person with respect to *N* controlled, in whole or in part, *R*'s attempts to influence legislation. The general purpose grant will not constitute a taxable expenditure under section 4945(d)(1).

* * * * *

(d) *Exceptions—(1) Nonpartisan analysis, study, or research.* * * *

(iv) *Making available results of analysis, study, or research.* * * * For purposes of this paragraph (d)(1)(iv), such presentations may not be limited to, be directed toward, or otherwise favor in any manner, persons who are interested solely in one side of a particular issue.

* * * * *

Par. 18. Title 26 is revised by adding a new Part 56 to read as follows:

Part 56—PUBLIC CHARITY EXCISE TAXES

Sec.

56.4911–1 Tax on excess lobbying expenditures.
56.4911–2 Lobbying expenditures, expenditures for direct lobbying, and grass roots expenditures.
56.4911–3 Activities not attempts to influence legislation.
56.4911–4 Exempt purpose expenditures.
56.4911–5 Communications with members.
56.4911–6 Records of lobbying and grass roots expenditures.
56.4911–7 Affiliated group of organizations.
56.4911–8 Excess lobbying expenditures of affiliated group.
56.4911–9 Application of section 501 (h) to affiliated groups of organizations.
56.4911–10 Members of a limited affiliated group of organizations.
56.6001–1 Notice or regulations requiring records, statements, and special returns.
56.6011–1 General requirement of return, statement, or list.

Authority: 26 U.S.C. 7805. Sec. 56.4911–7 also issued under 26 U.S.C. 4911(f)(3).

§56.4911–1 Tax on excess lobbying expenditures.

(a) *In general.* Section 4911(a) imposes an excise tax of 25 percent on the excess lobbying expenditures (as defined in paragraph (b) of this section) for a taxable year of an organization for which the expenditure test election under section 501(h) is in effect. The limit on expenditures for influencing legislation on which no tax is due from an organization for a taxable year is the lobbying nontaxable amount, or, on expenditures for influencing legislation through grass roots lobbying, the grass roots nontaxable amount (see paragraph (c) of this section). For rules concerning the application to the members of an affiliated group of organizations (as defined in §56.4911–7(e)) of the excise tax imposed by section 4911(a), see §56.4911–8.

(b) *Excess lobbying expenditures.* For any taxable year for which the expenditure test election under section 501(h) is in effect, the amount of an organization's excess lobbying expenditures is the greater of—

(1) The amount by which the organization's lobbying expenditures (within the meaning of §56.4911–2(a)) exceed the organization's lobbying nontaxable amount, or

(2) The amount by which the organization's grass roots expenditures (within the meaning of §56.4911–2(c)) exceed the organization's grass roots nontaxable amount.

(c) *Nontaxable amounts—(1) Lobbying nontaxable amount.* Under section 4911(c)(2), the lobbying nontaxable amount for any taxable year for which the expenditure test election is in effect is the lesser of—

(i) $1,000,000, or

(ii) To the extent of the organization's exempt purpose expenditures (within the meaning of §56.4911–4) for that year, the sum of 20 percent of the first $500,000 of such expenditures, plus 15 percent of the second $500,000 of such expenditures, plus 10 percent of the third $500,000 of such expenditures, plus 5 percent of the remainder of such expenditures.

(2) *Grass roots nontaxable amount.* Under section 4911(c)(4), an organization's grass roots nontaxable amount for any taxable year is 25 percent of its lobbying nontaxable amount for that year.

(d) *Examples.* The provisions of this section are illustrated by the examples in §1.501(h)-3.

(e) *Effective date.* The provisions of §§56.4911-1 through 56.4911-10 are effective for taxable years beginning after December 31, 1976.

§56.4911-2 Lobbying expenditures, expenditures for direct lobbying, and grass roots expenditures.

(a) *Lobbying expenditures.* An organization's lobbying expenditures for a taxable year for which the expenditures test election under section 501(h) is in effect are the sum of its expenditures for direct lobbying (as defined in paragraph (b) of this section) for the year and its grass roots expenditures (as defined in paragraph (c) of this section) for the year. In determining an organization's lobbying expenditures, no expenditure shall be counted twice.

(b) *Expenditures for direct lobbying defined*—(1) *Expenditures.* An expenditure for direct lobbying is any amount paid or incurred for, or in connection with, direct lobbying, or any amount treated as an expenditure for direct lobbying under paragraph (d) or (e) of this section or under §56.4911-5, or any amount included as an expenditure for direct lobbying under §56.4911-10(d)(2). Expenditures for direct lobbying include amounts paid or incurred as current or deferred compensation for an employee's services in connection with direct lobbying, and the allocable portion of administrative, overhead, and other general expenditures attributable to direct lobbying.

(2) *Direct lobbying communication defined.* A communication is an attempt to influence legislation through direct lobbying if the communication—

(i) Pertains to legislation being considered by a legislative body, or seeks or opposes legislation,

(ii) Reflects a view with respect to the desirability of the legislation (for this purpose, a communication that pertains to legislation but expresses no explicit view on the legislation shall be deemed to reflect a view on legislation if the communication is selectively disseminated to persons reasonably expected to share a common view of the legislation), and

(iii) Is either—

(A) With a member or employee of a legislative body, or

(B) With a government official or employee (other than a member or employee of a legislative body) who may participate in the formulation of legislation, but only if the principal purpose of the communication is to influence legislation.

(3) *Examples.* The provisions of this paragraph (b) are illustrated by the following examples:

Example (1). P is an organization for which the expenditure test election under section 501(h) is in effect. *P*'s employee, *A*, is assigned to approach members of Congress to gain their support for a pending bill. *A* spends several weeks researching the issue and contacting *P*'s directors to clarify *P*'s position on the bill. *P* then prints a position letter that is distributed to members of Congress. Additionally, *A* personally contacts several members of Congress or their staffs to seek support for *P*'s position on the bill. Amounts paid or incurred for, or in connection with, *A*'s research. *A*'s discussions with *P*'s directors, the position letter, and *A*'s Congressional contacts are expenditures for direct lobbying.

Example (2). Assume the same facts as in example (1), except that after *A* completes the research on the issue, it is decided by *P*'s directors that *P* will neither support nor oppose the bill. Under these circumstances, *A* has not engaged in any direct lobbying. Accordingly, *P*'s expenditures incurred for, or in connection with, *A*'s research are not expenditures for direct lobbying.

(c) *Grass roots expenditures*—(1) *Defined.* A grass roots expenditure is any amount paid or incurred for, or in connection with, grass roots lobbying, or any amount treated as grass roots expenditure under paragraphs (d) or (e) of this section or under §56.4911-5 or any amount included as a grass roots expenditure under §56.4911-10(d)(3). Grass roots expenditures include amounts paid or incurred as current or deferred compensation for an employee's services in connection with grass roots lobbying, and the allocable portion of administrative, overhead, and other general expenditures attributable to grass roots lobbying. "Grass roots lobbying" means an attempt to influence the general public, or any segment thereof, with respect to any legislation. A communication shall be considered an attempt to influence the general public, or a segment thereof, with respect to legislation if the communication—

(i) Pertains to legislation being considered by a legislative body, or seeks or opposes legislation,

(ii) Reflects a view with respect to the desirability of the legislation (for this purpose, a communication that pertains to legislation but expresses no explicit view on the legislation shall be deemed to reflect a view on legislation if the communication is selectively disseminated to persons reasonably expected to share a common view of the legislation), and

(iii) Is communicated in a form and distributed in a manner so as to reach individuals as members of the general public, that is, as voters or constituents, as opposed to a communication designed for academic, scientific, or similar purposes. A communication may meet this test even if it reaches the public only indirectly, as in a news release submitted to the media.

If any part of an advertisement constitutes grass roots lobbying, the entire amount expended for, or in connection with, the advertisement constitutes a grass roots expenditure.

(2) *Examples.* The provisions of this paragraph (c) are illustrated by the following examples:

Example (1). L, an organization for which the expenditure test under section 501(h) is in effect, places in local newspapers in State *W* an advertisement that asserts that lack of new capital is hurting the state's economy. The advertisement recommends that residents either invest more in local businesses or increase their savings so that funds will be available to others interested in making investments. Although the advertisement expresses a view with respect to a general problem that might receive legislative attention and is distributed in a manner so as to reach and influence many individuals, it does not constitute an attempt to influence the public with respect to legislation because it pertains to private conduct rather than legislation.

Example (2). Assume the same facts as in example (1), except that the advertisement, although not expressly calling for legislative action, also asserts that particular kinds of state tax incentives (which could not be implemented without legislation) would substantially increase capital formation. Thus, the advertisement is seeking action by the legislature and, at least in part, is addressed to individuals as voters or constituents rather than as potential investors. The advertisements reflects a view with respect to the desirability of the legislation. The advertisement constitutes an attempt to influence the public with respect to legislation, and the entire amount expended for, or in connection with, the advertisement is a grass roots expenditure.

Example (3). There is pending in the legislature of State *X* a proposal to amend certain laws concerning voting in state elections. As a public service, *M,* an organization in State *X* for which the expenditure test election is in effect places in local newspapers of general circulation an advertisement that explains both the current voting laws and the proposed amendments. The advertisement takes no position on the merits of the proposal. Under these circumstances, the advertisements does not reflect a view with respect to the desirability of the proposal and does not constitute an attempt to influence the general public with respect to the proposal.

Example (4). The legislature of State *Y* is considering a proposal to prohibit hunting on land owned by the State. *N,* an organization for which the expenditure test election is in effect, prepares a pamphlet that analyzes the proposal in detail but expresses no view on its merits. *N* arranges for distribution of the pamphlet to groups in State *Y* (with which it is not affiliated) that are opposed to hunting. The pamphlet pertains to legislation, and is deemed to reflect a view with respect to the desirability of the legislation by reason of its selective distribution to an audience reasonably expected to support the prohibition on hunting. The information is communicated in a form and distributed in a manner so as to reach individuals as voters or constituents. Expenditures for, or in connection with, the preparation and distribution of the pamphlet are grass roots expenditures.

Example (5). The legislature in State *Z* is considering a proposal to require pharmaceutical firms to test the safety of their products through certain laboratory procedures. *P*, an organization in State *Z* for which the expenditure test is in effect, prepares a detailed report on the usefulness of the tests that would be required under the proposal. The report concludes that the tests specified in the proposal are poorly designed. *P* distributes copies of the report to university professors in the field of health science without suggesting that the recipients make any attempt to influence the public with respect to the proposal. Although the report pertains to legislation and implies that the legislative proposal under consideration should not be enacted, the limited distribution of the report indicates that copies were furnished to the recipients as scholars in the field rather than as members of the general public, that is, as voters or constituents. The expenditures for the report, therefore, are not grass roots expenditures.

Example (6). Assume the same facts as in example (5), except that *P* also prepares a leaflet summarizing the report and distributes both the report and the leaflet only to academics in the field of health science who are known to oppose the legislation. The academics publicize their position by using the leaflets provided by *P*. *S*, an organization described in section 501(c)(4), of which the academics are members, also publicizes its opposition to the legislation using the leaflets provided by *P*. All amounts expended by *P* in connection with the report and the leaflets are grass roots expenditures since they were not communications designed for academic, scientific, or similar purposes.

Example (7). *Q*, an organization for which the expenditure test is in effect, pays for the radio broadcast of an advertisement that refers to a current controversy involving legislation and urges citizens to "become involved." The advertisement does not discuss the merits of any legislative proposal but it does offer a free booklet which analyzes and takes positions on various legislative proposals relating to the controversy. All expenditures for, or in connection with, the advertisement and the booklet are grass roots expenditures because together they constitute an attempt by *Q* to influence the public with respect to legislation.

Example (8). *R*, an organization for which the expenditure test is in effect, makes the services of *B*, one of its paid executives, available to *S*, an organization described in section 501(c)(4) of the Code. *B* works for several weeks to assist *S* in developing materials designed to influence public opinion on legislation. In performing this work, *B* uses office space and clerical assistance provided by *R*. *R* pays full salary and benefits to *B* during this period and receives no reimbursement from *S* for these payments or for the other facilities and assistance provided. All expenditures of *R*, including allocable office expenses, that are attributable to this assignment are grass roots expenditures because *B* was engaged in an attempt to influence the public on legislation.

(d) *Mixed purpose expenditures*—(1) *In general.* Except as provided in paragraphs (c)(1), (d)(2), and (d)(3) of this section, in the case of a mixed purpose expenditure, a reasonable allocation, based on all the facts and circumstances, must be made between the portion of the expenditure incurred for lobbying purposes and the portion incurred for charitable or fundraising purposes. For example, if a pamphlet has three articles of equal length, one of which constitutes an attempt to influence the general public with respect to legislation, and two of which relate to charitable, nonlobbying purposes, the cost of printing and mailing will be considered allocated reasonably if one-third of this cost is treated as a grass roots expenditure. See §56.4911–5 for rules with respect to certain communications with members.

(2) *Grass roots expenditures and fundraising.* If an expenditure (to which §56.4911–5 does not apply) is made for both grass roots lobbying purposes and fundraising purposes, the entire expenditure will be treated as a grass roots lobbying expenditure. For purposes of the preceding sentence, an expenditure for fundraising literature is not made for grass roots purposes if the fundraising literature merely mentions that the organization engages in attempts to influence legislation only to the extent consistent with section 501(c)(3) status.

(3) *Mixed lobbying.* If an expenditure (to which §56.4911–5 does not apply) is made for both direct lobbying and grass roots lobbying purposes, the expenditure will be treated as a grass roots expenditure except to the extent that the organization demonstrates that the expenditure was incurred solely for direct lobbying purposes.

(e) *Certain transfers treated as lobbying expenditures*—(1) *Transfer earmarked for grass roots purposes.* A transfer is a grass roots expenditure to the extent that it is earmarked (as defined in §56.4911–4(f)(4)) for grass roots lobbying purposes and is not described in §56.4911–4(e).

(2) *Transfer earmarked for direct and grass roots lobbying.* A transfer that is earmarked for direct lobbying purposes or for direct lobbying and grass roots lobbying purposes is treated as a grass roots expenditure in full except to the extent the transferor demonstrates that the amounts transferred were expended for direct lobbying purposes. This paragraph (e)(2) shall not apply to any expenditure described in §56.4911–4(e).

(3) *Certain transfers to organizations that lobby.* A transfer that is neither a controlled grant (as defined in §56.4911–4(f)(3)) nor an expenditure described is §56.4911–4(e) and that is made to an organization not described in section 501(c)(3) that engages in attempts to influence legislation is treated as a grass roots expenditure to the extent of the lesser of the amount of the transfer or the transferee's expenditures for grass roots lobbying. If the amount of the transfer exceeds the transferee's expenditures for grass roots lobbying, the excess will be treated as an expenditure for direct lobbying to the extent of the transferee's expenditures for direct lobbying. In applying the preceding two sentences, the expenditures of the transferee will be determined as if the regulations under section 4911 applied to the transferee.

(f) *Definitions.* For purposes of section 4911 and the regulations thereunder—

(1) *Legislation.* The term "legislation" includes action by the Congress, any state legislature, any local council, or similar legislative body, or by the public in a referendum, initiative, constitutional amendment, or similar procedure. The term "legislation" includes a proposed treaty required to be submitted by the President to the Senate for its advice and consent from the time the President's representative begins to negotiate its position with the prospective parties to the proposed treaty.

(2) *Action.* The term "action" is limited to the introduction, amendment, enactment, defeat to repeal of Acts, bills, resolutions, or similar items.

(3) *Legislative body.* The term "legislative body" does not include executive, judicial, or administrative bodies.

(4) *Administrative bodies.* The term "administrative bodies" includes school boards, housing authorities, sewer and water districts, zoning boards, and other similar Federal, State, or local special purpose bodies, whether elective or appointive.

§56.4911–3 Activities not attempts to influence legislation.

(a) *In general.* This section describes activities that are not attempts to influence legislation for purposes of section 4911. Accordingly, expenditures for, or in connection with, activities described in this section are not lobbying expenditures under §56.4911–2.

(b) *Nonpartisan analysis, study or research.* Under section 4911(d)(2)(A), "influencing legislation" does not include making available the results of nonpartisan analysis, study, or research. For guidance in determining whether an amount is paid or incurred for, or in connection with, making available the results of nonpartisan analysis, study, or research see §53.4945–2(d)(1).

(c) *Technical advice or assistance.* Under section 4911(d)(2)(B), "influencing legislation" does not include providing technical advice or assistance to a governmental body, a governmental committee, or a subdivision of either in response to a written request by the body, committee, or subdivision. For guidance in determining whether an amount is paid or incurred for, or in connection with, providing technical advice or assistance, see §53.4945–2(d)(2).

(d) *Self defense*—(1) *In general.* Under section 4911(d)(2)(C), "influencing legislation" does not include an appearance before or communication with any legislative body with respect to a possible action by the body that might affect the existence of the organization, its powers and duties, its tax-exempt status, or the deductibility of contributions to the organization. For guidance in determining whether an amount is paid or incurred for, or in connection with, these communications or appearances, see §53.4945–2(d)(3). See also, paragraphs (d)(2), (d)(3), and (d)(4) to this section concerning appearances on behalf of other organizations.

(2) *Affiliated group of organizations.* For an organization that is a member of an affiliated group of organizations (within the meaning of §56.4911–7(e)), "influencing legislation" does not include appearances before, or communications with, a legislative body with respect to a possible action by the body that might affect the existence of any other member of the group, its powers and duties, its tax-exempt status, or the deductibility of contributions to it.

(3) *Activities on behalf of member organizations.* For an organization that has a membership consisting solely of other organizations that are described in section 501(c)(3), "influencing legislation" does not include appearances before, or communications with, any legislative body with respect to a possible action by the body which might affect the existence of one or more of the member organizations, their powers, duties, or tax-exempt status, or the deductibility of contributions to one or more of the member organizations.

(4) *Limited affiliated group of organizations.* For an organization that is a member of a limited affiliated group of organizations under §56.4911–10, "influencing legislation" does not include appearances before, or communications with, the Congress of the United States with respect to a possible action by the Congress that might affect the existence of any member of the limited affiliated group, its powers and duties, tax-exempt status, or the deductibility of contributions to it.

§56.4911–4 Exempt purpose expenditures.

(a) Application. This section provides rules under section 4911(e) for determining an organization's "exempt purpose expenditures" for a taxable year for purposes of section 4911(c)(2) and §56.4911–1(c)(2), which define an organization's lobbying nontaxable amount by reference to its exempt purpose expenditures. In determining an organization's exempt purpose expenditures, no expenditure shall be counted twice by an organization.

(b) *Included expenditures.* Amounts paid or incurred by an organization that are exempt purpose expenditures include—

(1) Amounts paid or incurred to accomplish a purpose enumerated in section 170(c)(2)(B), including (but not limited to) the amount of any transfer made by the organization (other than a transfer described in paragraph (e) of this section) to another organization to accomplish the transferor's exempt purposes, and including amounts expended by an organization out of transfers (other than a transfer described in paragraph (e) of this section) for which the organization is the transferee,

(2) Amounts paid or incurred as current or deferred compensation for an employee's services in connection with a purpose enumerated in section 170(c)(2)(B),

(3) The allocable portion of administrative overhead, and other general expenditures attributable to the accomplishment of a purpose enumerated in section 170(c)(2)(B),

(4) Lobbying expenditures (as defined in §56.4911–2(a)) whether or not for a purpose enumerated in section 170(c)(2)(B),

(5) Amounts paid or incurred for, or in connection with, activities described in §56.4911–3,

(6) Amounts paid or incurred for, or in connection with, activities described in §56.4911–5 that are not lobbying expenditures, and

(7) A reasonable allowance for exhaustion, wear and tear, obsolescence or amortization, of assets to the extent used for one or more of the purposes described in paragraphs (b)(1) through (6) of this section, computed on a straight-line basis (for this purpose, an allowance for depreciation will be treated as reasonable if based on a useful life that would satisfy section 312(k)(3)(A) as in effect on January 1, 1985).

(c) *Excluded expenditures.* Notwithstanding paragraph (b) of this section, exempt purpose expenditures do not include—

(1) Amounts paid or incurred that are neither expenditures to accomplish a purpose enumerated in section 170(c)(2)(B) nor lobbying expenditures (as defined in §56.4911–2(a)),

(2) The amount of any transfer described in paragraph (e) of this section,

(3) Amounts paid to or incurred for a separate fund raising unit (as defined in paragraph (f)(2) of this section) of an organization or of an affiliated organization (see §56.4911–7(a)),

(4) Amounts paid to or incurred for any person not an employee, or any organization not an affiliated organization, if paid or incurred primarily for fund raising,

(5) Amounts paid or incurred that are properly chargeable to a capital account, determined in accordance with the principles that apply under sections 312(k)(1) and (3) (as in effect on January 1, 1985), to amounts paid or incurred in a trade or business,

(6) Amounts paid or incurred for a tax that is not imposed in connection with the organization's efforts to accomplish a purpose described in section 170(c)(2)(B), such as the taxes imposed under sections 511(a)(1) and 4911(a), and

(7) Amounts paid or incurred in connection with the production of income, whether or not described in section 512(a)(1).

(d) *Certain transfers treated as exempt purpose expenditures*—(1) An organization's transfer will be treated as an exempt purpose expenditure under paragraph (b)(1) of this section if it is—

(i) Described in either paragraph (d)(2) or (d)(3) of this section, and

(ii) Not described in paragraph (e) of this section.

(2) A transfer is described in this paragraph (d)(2) if it is made to an organization described in section 501(c)(3) in furtherance of the transferor's exempt purposes and is not earmarked for any purpose other than a purpose described in section 170(c)(2)(B). Thus, a payment of dues by a local or state organization to, respectively, a state or national organization that is described in section 501(c)(3) is considered an exempt purpose expenditure of the transferor to the extent it is not otherwise earmarked.

(3) A transfer is described in this paragraph (d)(3) if it is a controlled grant (as defined in paragraph (f)(3) of this section), but only to the extent of the amounts that are paid or incurred by the transferee that would be exempt purpose expenditures if paid or incurred by the transferor.

(e) *Transfers not exempt purpose expenditures*—(1) An organization's transfer is described in this paragraph (e) if it is described in one of paragraphs (e)(2) through (e)(4).

(2) A transfer is described in this paragraph (e)(2) if it is made to a member of any affiliated group (as defined in §56.4911–7(e)) of which the transferor is a member.

(3) A transfer is described in this paragraph (e)(3) if the Commissioner determines that the transfer artificially inflates the amount of the transferor's or transferee's exempt purpose expenditures. In general, the Commissioner will make that determination if a substantial purpose of a transfer is to inflate those exempt purpose expenditures. A transfer described in this paragraph will not be considered an exempt purpose expenditure of the transferor, but will be an exempt purpose expenditure of the transferee to the extent that the transferee expends the transfer in the active conduct of its charitable activities or attempts to influence legislation. Standards similar to those found in §53.4942(b)–1(b) may be applied in determining whether the transferee has expended amounts in the "active conduct" of its charitable activities or attempts to influence legislation.

(4) A transfer is described in this paragraph (e)(4) if it is not a controlled grant and is made to an organization not described in section 501(c)(3) that does not attempt to influence legislation.

(f) *Definitions*—(1) For purposes of paragraph (c) of this section, "fund raising" includes—

(i) Soliciting dues or contributions from members of the organization, from persons whose dues are in arrears, or from the general public,

(ii) Soliciting grants from businesses or other organizations, including organizations described in section 501(c)(3), or

(iii) Soliciting grants from a governmental unit referred to in section 170(c)(1), or any agency or instrumentality thereof.

(2) For purposes of paragraph (c) of this section, a separate fund raising unit of any organization must consist of either two or more individuals a substantial part of whose time is spent on fund raising for the organization, or any separate accounting unit of the organization that is devoted to fund raising.

(3) For purposes of this section, a "controlled grant" is a grant made by an eligible organization described in §1.501(h)–2(b) to an organization not described in section 501(c)(3) that meets the following requirements:

(i) The donor limits the grant to a specific project of the recipient that is in furtherance of the donor's exempt purposes; and

(ii) The donor maintains records to establish that the grant is used in furtherance of the donor's exempt purposes.

(4) A transfer, including a grant or payment of dues, is "earmarked" for a specific purpose—

(i) To the extent that the transferor directs the transferee to add the amount transferred to a fund established to accomplish the purpose, or

(ii) To the extent of the amount transferred or, if less, the amount agreed upon to be expended to accomplish the purpose, if there exists an agreement, oral or written, whereby the transferor may cause the transferee to expend amounts to accomplish the purpose or whereby the transferee agrees to expend an amount to accomplish the purpose.

(g) *Example.* The provisions of this section are illustrated by the following example:

Example. Organization *X* is an exempt organization described in section 501(c)(3) that is organized for the purpose of rehabilitating alcoholics. *X* elected to be subject to the provisions of section 501(h) in 1981. For 1981, *X* had the following expenditures that are included in its exempt purpose expenditures to the extent indicated.

Description	*Total*	*Includible*
Cost of real estate purchased for use as half-way house for alcoholics, attributable to the following:		
Land	30,000	-0-
Building	200,000	-0-
Depreciation 40-year useful life	-0-	5,000
Expenses of operating its half-way house.	170,000	170,000
Administrative expenses of the organization allocated to the operation of its half-way house.	95,000	95,000
Depreciation and allowances for equipment.	10,000	10,000
Expenses related to attempts to influence legislation (lobbying expenditures)	40,000	40,000
Amounts paid to *Z* by the organization for fundraising	35,000	-0-
		$320,000

For 1981, *X*'s exempt purpose expenditures total $320,000. The $35,000 paid by *X* to *Z* for fund raising is not included in the exempt purpose expenditures total. All lobbying expenses are included in full. Only depreciation computed on a straight-line basis is included in exempt purpose expenditures.

§56.4911–5 Communications with members.

(a) *In general.* For purposes of section 4911 and §56.4911–2, expenditures in connection with certain communications between an organization and its members are treated as expenditures for direct lobbying, as grass roots expenditures, or as other than lobbying expenditures in accordance with this section.

(b) *Communication directed only to members; excepted communication.* Expenditures for, or in connection with, a communication that pertains to legislation or proposed legislation are not lobbying expenditures if the communication satisfies the following requirements:

(1) The communication is directed only to members of the organization;

(2) The legislation or proposed legislation to which the communication relates is of direct interest to the organization and its members;

(3) The communication does not directly encourage the member to engage in direct lobbying (whether individually or through the organization); and

(4) The communication does not directly encourage the member to engage in grass roots lobbying, whether individually or through the organization.

(c) *Communication directed only to members; expenditures for direct lobbying.* Expenditures for, or in connection with, a communication that reflects a view with respect to the desirability of legislation and that satisfies the requirements of subparagraphs (1), (2), and (4) of paragraph (b) of this section, but does not satisfy the requirements of subparagraph (3) of such paragraph (b), are treated as expenditures for direct lobbying.

(d) *Communication directed only to members; grass roots expenditures.* Expenditures for, or in connection with, a communication that reflects a view with respect to the desirability of legislation and that satisfies the requirements of subparagraphs (1) and (2) of paragraph (b) of this section, but does not satisfy the requirements of subparagraph (4) of such paragraph (b), are treated as grass roots expenditures (whether or not the communication satisfies the requirements of subparagraph (3) of such paragraph (b)).

(e) *Written communications directed to members and nonmembers*—(1) *In general.* Expenditures for, or in connection with, any written communication that is designed primarily for members of an organization (but not directed only to members) and that reflects a view with respect to the desirability of legislation or proposed legislation of direct interest to the organization and its members, are treated as expenditures for direct lobbying or grass roots expenditures in accordance with paragraph (e)(2) or (e)(3) of this section.

(2) *Direct lobbying encouraged*—(i) *Lobbying expenditure amount.* If a written communication described in paragraph (e)(1) of this section directly encourages readers to engage individually or through the organization in direct lobbying but does not encourage them to engage in grass roots lobbying, the cost of the communication is allocated between expenditures for direct lobbying and grass roots expenditures in accordance with paragraphs (e)(2)(ii) and (iii) of this section. The portion of the cost to be allocated includes all costs of preparing all the material with respect to which readers are urged to engage in direct lobbying plus the mechanical and distribution costs attributable to the lineage devoted to this material (see §1.512(a)–1(f)(6)).

(ii) *Grass roots amount.* The amount allocable as a grass roots expenditure for a communication described in paragraph (e)(1) of this section is the amount calculated in paragraph (e)(2)(i) of this section multiplied by the sum of the nonmember subscribers percentage and the all other distribution percentage, both as defined in paragraph (f)(7) of this section. Solely for purposes of the allocation described in this paragraph (e)(2)(ii), the nonmember subscribers percentage is treated as zero unless it is greater than 15% of total distribution.

(iii) *Direct lobbying amount.* The amount allocable as an expenditure for direct lobbying for a communication described in paragraph (e)(1) of this section is the excess of the amount described in paragraph (e)(2)(i) of this section over the amount described in paragraph (e)(2)(ii) of this section.

(3) *Grass roots expenditure if grass roots lobbying encouraged.* The portion of the cost of a written communication described in paragraph (e)(1) of this section that constitutes a grass roots expenditure is—

(i) If the communication directly encourages readers to engage individually or collectively (whether through the organization or otherwise) in grass roots lobbying (whether or not it also encourages readers to engage in direct lobbying), the grass roots expenditure includes all the costs of preparing all the material with respect to which readers are urged to engage in grass roots lobbying the mechanical and distribution costs attributable to the lineage devoted to this material (see §1.512(a)–1(f)(6)); or

(ii) If the communication does not directly encourage readers to engage in direct lobbying (determined by applying the rule in paragraph (f)(6) of this section) and does not encourage readers to engage in grass roots lobbying, whether individually, collectively, through the organization, or otherwise, the amount described in paragraph (e)(2)(ii) of this section.

(f) *Definition and special rules.* For purposes of the regulations under section 4911—

(1) *Member; general rule.* A person is a member of an organization if the person—

(i) Pays dues or makes a contribution of more than a nominal amount,

(ii) Makes a contribution of more than a nominal amount of time, or

(iii) Is one of a limited number of "honorary" or "life" members who have more than a nominal connection with the organization and who have been chosen for a valid reason (such as length or service to the organization or involvement in activities forming the basis of the organization's exemption) unrelated to the organization's dissemination of information to its members.

(2) *Member; special rule.* A person not a member of an organization within the meaning of paragraph (f)(1) of this section may be treated as a member if the organization demonstrates to the satisfaction of the Internal Revenue Service that there is a good reason for its membership requirements not meeting the requirements of such paragraph (f)(1), and that its membership requirements do not operate to permit an abuse of the rules described in this section.

(3) *Member; affiliated group of organizations.* For purposes of this section, a person who is a member of an organization that is a member of an affiliated group of organizations (within the meaning of §56.4911–7(e)) is treated as a member of each organization in the affiliated group.

(4) *Member; limited affiliated group of organizations.* For purposes of this section, a person who is a member of an organization that is a member of a limited affiliated group of organizations (within the meaning of §56.4911–10(b)) is treated as a member of each organization in the limited affiliated group, but only to the extent that the communication relates to a national legislative issue (within the meaning of §56.4911–10(g)).

(5) *Subscriber.* A person is a subscriber to a written communication if—

(i) The person is a member of the publishing organization and the membership dues expressly include the right to receive the written communication, or

(ii) The person has affirmatively expressed a desire to receive the written communication and has paid more than a nominal amount for the communication.

(6) *"Self-defense" exception for communications with members.* For purposes of paragraphs (b)(3), (e)(2)(i), and (e)(3)(ii) of this section, a communication that directly encourages a member to engage in direct lobbying activities that are described in section 4911(d)(2)(C) and that would not be attempts to influence legislation if engaged in directly by the organization is treated as a communication that does not directly encourage a member to engage in direct lobbying.

(7) *Percentages of total distribution.* With respect to a communication described in paragraph (e)(1) of this section—

(i) "Member percentage" means the percentage of total distribution that represents distribution of a single copy to any member;

(ii) "Nonmember subscribers percentage" means the percentage of total distribution that represents distribution to nonmember subscribers (including libraries); and

(iii) "All other distribution percentage" means 100% reduced by the sum of the member percentage and the nonmember subscribers percentage.

§56.4911-6 Records of lobbying and grass roots expenditures.

(a) *Records of lobbying expenditures.* An organization to which the expenditure test under section 501(h) applies for a taxable year must keep a record of its lobbying expenditures for the taxable year. Lobbying expenditures of which an organization must keep a record include the following:

(1) Expenditures for grass roots lobbying, as described in paragraph (b) of this section;

(2) Amounts directly paid or incurred for direct lobbying, including payments to another organization earmarked for direct lobbying, fees and expenses paid to individuals or organizations for direct lobbying, and printing, mailing, and other direct costs of reproducing and distributing materials used in direct lobbying;

(3) The portion of amounts paid or incurred as current or deferred compensation for an employee's services in connection with direct lobbying;

(4) Amounts paid for out-of-pocket expenditures incurred on behalf of the organization and in connection with direct lobbying, whether or not incurred by an employee;

(5) The allocable portion of administrative, overhead, and other general expenditures attributable to direct lobbying;

(6) Expenditures for publications or for communications with members to the extent the expenditures are treated as expenditures for direct lobbying under §56.4911-5; and

(7) Expenditures for direct lobbying of a controlled organization (within the meaning of §56.4911-10(c)) to the extent included by a controlling organization (within the meaning of §56.4911-10(c)) in its lobbying expenditures.

(b) *Records of grass roots expenditures.* An organization to which the expenditure test under section 501(h) applies for a taxable year must keep a record of its grass roots expenditures for the taxable year. Grass roots expenditures of which an organization must keep a record include the following:

(1) Amounts directly paid or incurred for grass roots lobbying, including payments to other organizations earmarked for grass roots lobbying, fees and expenses paid to individuals or organizations for grass roots lobbying, and the printing, mailing, and other direct costs of reproducing and distributing materials used in grass roots lobbying;

(2) The portion of amounts paid or incurred as current or deferred compensation for an employee's services in connection with grass roots lobbying;

(3) Amounts paid for out-of-pocket expenditures incurred on behalf of the organization and in connection with grass roots lobbying, whether or not incurred by an employee;

(4) The allocable portion of administrative, overhead, and other general expenditures attributable to grass roots lobbying;

(5) Expenditures for publications or communications that are treated as expenditures for grass roots lobbying under §56.4911-5; and

(6) Expenditures for grass roots lobbying of a controlled organization (within the meaning of §56.4911-10(c)) to the extent included by a controlling organization (within the meaning of §56.4911-10(c)) in its grass roots expenditures.

§56.4911-7 Affiliated group of organizations.

(a) *Affiliation between two organizations*—(1) *In general.* For purposes of the regulations under section 4911, two organizations are affiliated, subject to the limitation described in paragraph (a)(2) of this section, if one organization is able to control action on legislative issues by the other by reason of interlocking governing boards (see paragraph (b) of this section) or by reason of provisions of the governing instruments of the controlled organization (see paragraph (c) of this section). The ability of the controlling organization to control action on legislative issues by the controlled organization is sufficient to establish that the organizations are affiliated; it is not necessary that the control be exercised.

(2) *Organizations not described in section 501(c)(3).* Two organizations, neither of which is described in section 501(c)(3), are affiliated only if there exists at least one organization described in section 501(c)(3) that is affiliated with both organizations.

(3) *Action on legislative issues.* For purposes of this section, the term "action on legislative issues" includes taking a position in the organization's name on legislation, authorizing any person to take a position in the organization's name on legislation, or authorizing any lobbying expenditures. The phrase does not include actions taken merely to correct unauthorized actions taken in the organization's name.

(b) *Interlocking governing boards*—(1) *In general.* Two organizations have interlocking governing boards if one organization (the controlling organization) has a sufficient number of representatives (within the meaning of paragraph (b)(5) of this section) on the governing board of the second organization (the controlled organization) so that by aggregating their votes, the representatives of the controlling organization can cause or prevent action on legislative issues by the controlled organization. If two organizations have interlocking governing boards, the organizations are affiliated without regard to how or whether the representatives of the controlling organization vote on any particular matter.

(2) *Majority or quorum.* Except as provided in paragraph (b)(3) or (4) of this section, the number of representatives of an organization (the controlling organization) who are members of the governing board of a second organization (the controlled organization) will be presumed sufficient to cause or prevent action on legislative issues by the controlled organization if that number either—

(i) Constitutes a majority of incumbents on the governing board, or

(ii) Constitutes a quorum, or is sufficient to prevent a quorum, for acting on legislative issues.

(3) *Votes required under governing instrument or local law.* Except as provided in paragraph (b)(4) of this section, if under the governing documents of an organization (the controlled organization), it can be determined that a lesser number of votes than the number described in paragraph (b)(2) of this section is necessary or sufficient to cause or to prevent action on legislative issues, the number of representatives of the controlling organization who are members of the governing board of the controlled organization will be considered sufficient to cause or prevent action on legislative issues if it equals or exceeds that number.

(4) *Representatives constituting less than 15% of governing board.* Notwithstanding paragraph (b)(2) or (3) of this section, if the number of representatives of one

organization is less than 15 percent of the incumbents on the governing board of a second organization, the two organizations are not affiliated by reason of interlocking governing boards.

(5) *Representatives.* (i) This paragraph (b)(5) describes members of the governing board of one organization (the controlled organization) who are considered representatives of a second organization (the controlling organization). Under this paragraph (b)(5), a member of the governing board of a controlled organization may be a representative of more than one controlling organization. A person with no authority to vote on any issue being considered by the governing board is not a representative of any organization.

(ii) A board member of one organization (the controlled organization) is a representative of a second organization (the controlling organization) if the controlling organization has specifically designated that person to be a board member of the controlled organization. For purposes of this paragraph (b)(5)(ii) and paragraph (b)(5)(iii) of this section, a board member of the controlled organization is specifically designated by the controlling organization if the board member is selected by virtue of the right of the controlling organization, under the governing instruments of the controlled organization, either to designate a person to be a member of the controlled organization's governing board, or to select a person for a position that entitles the holder of that position to be a member of the controlled organization's governing board.

(iii) A board member of one organization who is specifically designated by a second organization, a majority of the governing board of which is made up of representatives of a third organization, is a representative of the third organization as well as being a representative of the second organization pursuant to paragraph (b)(5)(ii) of this section.

(iv) A board member of one organization who is also a member of the governing board of a second organization is a representative of the second organization.

(v) A board member of one organization who is an officer or paid executive of the second organization is a representative of the second organization. Although titles are significant in determining whether a person is a member of the executive staff of an organization, any employee of an organization who possesses authority commonly exercised by an executive is considered an executive staff member for purposes of this paragraph (b)(5)(v).

(c) *Governing instrument.* One organization (the "controlling" organization) is affiliated with a second organization (the "controlled" organization) by reason of the governing instruments of the controlled organization if the governing instruments of the controlled organization expressly or by implication limit the independent action of the controlled organization on a legislative issue by requiring that it take into account the position of the controlling organization on that issue. Any limitation on the independent action of the controlled organization on a legislative issue is sufficient to establish the existence of the relationship of affiliation. It is immaterial how or whether the limiting power is exercised.

(d) *Three or more organizations affiliated*—(1) *Two controlled organizations affiliated.* If a controlling organization described in this section is affiliated with each of two or more controlled organizations described in this section, then the controlled organizations are affiliated with each other.

(2) *Chain rule.* If one organization is a controlling organization described in this section with respect to a second organization and that second organization is a controlling organization with respect to a third organization, then the first organization is affiliated with the third.

(e) *Affiliated group of organizations*—(1) *Defined.* For purposes of the regulations under section 4911, an affiliated group of organizations is a group of organizations—

(i) Each of which is affiliated with every other member for at least thirty days of the taxable year of the affiliated group (determined without regard to the election provided for in paragraph (e)(5) of this section),

(ii) Each of which is an eligible organization (within the meaning of §1.501(h)–2(b)(1)), and

(iii) At least one of which is an electing member organization (within the meaning of paragraph (e)(4) of this section).

Each organization in a group of organizations that satisfies the requirements of the preceding sentence is a member of the affiliated group of organizations for the taxable year of the affiliated group.

(2) *Multiple membership.* For any taxable year of an organization, it may be a member of two or more affiliated groups of organizations.

(3) *Taxable year of affiliated group.* If all members of an affiliated group have the same taxable year, that taxable year is the taxable year of the affiliated group. If the members of an affiliated group do not all have the same taxable year, the taxable year of the affiliated group is the calendar year, unless the election under paragraph (e)(5) of this section is made.

(4) *Electing member organization.* For purposes of the regulations under section 4911, an "electing member organization" is an organization to which the expenditure test election under section 501(h) applies on at least one day of the taxable year of the affiliated group of which it is a member. For purposes of the preceding sentence (and notwithstanding §1.501(h)–2(a)), the expenditure test is not considered to apply to the organization on any day before the date on which it files the Form 5768 making the expenditure test election.

(5) *Election of member's year as group's taxable year.* The taxable year of an affiliated group may be determined according to the provisions of this paragraph (e)(5) if all of the members of the affiliated group so elect. Under this paragraph (e)(5), each member organization shall apply the provisions of section 501(h) and 4911, and the regulations thereunder (unless the regulations provide otherwise), by treating its own taxable year as the taxable year of the affiliated group. The election may be made by an electing member organization by attaching to its annual return a statement from itself and every other member of the affiliated group that contains: the organization's name, address, and employer identification number; and its signed consent to the election provided for in this paragraph (e)(5). The election must be made no later than the due date of the first annual return of any electing member for a taxable year for which the member is liable for tax under section 4911(a), determined under §56.4911–8(d). The election may not be made or revoked after the due date of the return referred to in the preceding sentence except upon such terms and conditions as the Commissioner may prescribe.

(f) *Examples.* The provisions of this section are illustrated by the following examples.

Example (1). M, N, and *O* are eligible organizations within the meaning of §1.501(h)–2(b)(1). Each has a governing board made up of nine members. Five members on the board of *N* are also members of the board of *M*. *N* designates five individuals from among its board, officers, and executive staff members to serve on the board of *O*. *M* is affiliated with *N*, *N* is affiliated with *O*, and *M* is affiliated with *O*.

Example (2). *X*, an eligible organization, has a board consisting of 10 members. Five unaffiliated tax-exempt organizations each designate two individuals to serve on the governing board of *X*. A simple majority of the board of *X* is a quorum and may establish *X*'s position on legislative issues. *X* is not affiliated with any of the five autonomous organizations by reason of interlocking governing boards.

Example (3). *P* and *Q* are eligible organizations. The governing instruments of *Q* indicate that it will not take a position on legislation if *P* disapproves of the position. In addition, there is regular correspondence between *P* and *Q* with regard to positions on legislation. *P* is affiliated with *Q* regardless of whether *P* has ever vetoed a position taken by *Q*.

Example (4). The governing board of organization *R* resolves to adopt the position taken on legislative issues by organization *S*. *R* and *S* are eligible organizations and do not have interlocking governing boards. The governing instruments of *R* do not mention organization *S* and do not indicate that *R* is to be bound by the decisions on legislation of any organization. *R* and *S* are not affiliated.

Example (5). Organization *Z* is bound, under the terms of its governing instruments, by the legislative positions of Organization *Y*. Organization *Y*, however, is bound, under the terms of its governing instruments, by the legislative positions of Organization *X*. Organization *X* is affiliated with *Y* and *Z*; *Y* is affiliated with *X* and *Z*; and *Z* is affiliated with *X* and *Y*.

Example (6). Organizations *T* and *U* have interlocking boards of directors. *T* is the controlling organization. Organization *V* is bound, under the terms of its governing instruments, by the legislative positions of *U*. *T* and *V* are affiliated because *T* may cause or prevent action on legislative issues by *U*, and *V* is bound by *U*'s action. If *U* were the controlling organization, *T* and *V* would be affiliated as two organizations controlled by the same organization.

Example (7). Organization *A* is an organization described in section 501(c)(4). It is affiliated, as the controlling organization, with organizations *K* and *L*, both of which are described in 501(c)(3) and are eligible to elect under 501(h). If *K* elects under section 501(h), *K* and *L* are an affiliated group of organizations.

Example (8). *G*, *H*, *I*, and *J* are eligible organizations. *G*, *H*, and *I* have elected the expenditure test under section 501(h). The governing board of *J* has nine members. Under the governing instruments of *J*, organizations *G*, *H*, and *I* each designate three members of the governing board of *J*. Also under the governing instruments of *J*, action on legislative issues requires the approval of any seven board members. Because the three representatives of *G* may prevent action on legislative issues, *J* is affiliated with *G*. Similarly, *J* is affiliated with each of *H* and *I*. However, under none of the rules of affiliation is *G* affiliated with *H*, or *H* with *I*, or *I* with *G*. Therefore *J* is a member of one affiliated group comprising *G* and *J*, of another group comprising *H* and *J*, and of a third group comprising *I* and *J*.

Example (9). Organizations *C*, *D*, and *E* have been affiliated for many years and have all elected the expenditure test. Each has a taxable year ending July 31. For every day of the year ending July 31, 1982, they were eligible organizations, electing member organizations, and affiliated with each other. On no day of that year were they affiliated with any other eligible organization having a different taxable year. Therefore, the year ending July 31, 1982, is the taxable year of the affiliated group comprising *C*, *D*, and *E*.

§56.4911–8 Excess lobbying expenditures of affiliated group.

(a) *Application*. This section provides rules concerning the exempt purpose expenditures, lobbying expenditures, and grass roots expenditures of an affiliated group or organizations, and the application of the excise tax imposed by section 4911(a) on the excess lobbying expenditures of the group.

(b) *Affiliated group treated as one organization*. Under section 4911(f), an affiliated group of organizations is treated as a single organization for purposes of the tax imposed by section 4911(a). For any taxable year of the affiliated group, the group's lobbying expenditures, grass roots expenditures, and exempt purpose expenditures are equal to the sum of the lobbying expenditures, grass roots expenditures, and exempt purpose expenditures, respectively, paid or incurred by each member during the taxable year of the affiliated group. The lobbying and grass roots nontaxable amounts for the affiliated group for a taxable year are determined under section 4911(c)(2) and (4) and §56.4911–1(c) and are based on the sum of the exempt purpose expenditures described in the preceding sentence. The lobbying and grass roots ceiling amounts for the affiliated group for a taxable year are calculated under §1.501(h)–3(c)(3) and (6) based upon the nontaxable amounts determined pursuant to the preceding sentence.

(c) *Tax imposed on excess lobbying expenditures of affiliated group*. The excise tax under section 4911(a) is imposed for a taxable year of an affiliated group if the group has excess lobbying expenditures. For any taxable year of an affiliated group, the group's excess lobbying expenditures are the greater of—

(1) The amount by which the group's lobbying expenditures exceed the group's lobbying nontaxable amount, or

(2) The amount by which the group's grass roots expenditures exceed the group's grass roots nontaxable amount.

(d) *Liability for tax*—(1) *Electing organizations*. As provided in this paragraph (d), an electing member organization is liable for all or a portion of the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations. An organization that is liable under this paragraph (d) is not liable for any excise tax under section 4911 based on its own excess lobbying expenditures. A member of the affiliated group that is not an electing member organization is not liable for any portion of the excise tax that is imposed with respect to the affiliated group.

(2) *Tax based on excess lobbying expenditures*. If the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations is based upon the amount described in paragraph (c)(1) of this section, and at least one electing member has made lobbying expenditures, each electing member organization is liable for a portion of the tax equal to the amount of the tax multiplied by a fraction, the numerator of which is the electing member organization's lobbying expenditures paid or incurred during the taxable year of the affiliated group, and the denominator of which is the sum of the lobbying expenditures of all electing member organizations in the group paid or incurred during the taxable year of the affiliated group.

(3) *Tax based on excess grass roots expenditures*. If the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations is based upon the amount described in paragraph (c)(2) of this section, and at least one electing member has made grass roots expenditures, each electing member organization is liable for a portion of the tax equal to the amount of the tax multiplied by the fraction described in paragraph (d)(2) of this section, except that "grass roots expenditures" is substituted for "lobbying expenditures."

(4) *Tax based on exempt purpose expenditures*. If the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations is based upon the amount described in paragraph (c)(2) of this section, and if paragraphs (d)(2) and (d)(3) of this section do not apply because no electing organization has made lobbying or grass roots expenditures, respectively, each electing member organization is liable for a portion of the tax equal to the amount of tax multiplied by a fraction the numerator of which is the electing member organization's exempt purpose expenditures and the denominator of which is the exempt purpose expenditures of all the electing member organizations in the affiliated group.

(5) *Taxable year for which liable.* An electing member organization that is liable for all or a portion of the excise tax imposed by section 4911(a) on the excess lobbying expenditures of an affiliated group of organizations is liable for the tax as if the tax were imposed for its taxable year with which or within which ends the taxable year of the affiliated group.

(6) *Organization a member of more than one affiliated group.* If, under this paragraph (d), an organization is liable for its taxable year for two or more excise taxes imposed by section 4911(a) on the excess lobbying expenditures of two or more affiliated groups, then the organization is liable only for the greater of the two or more taxes.

(e) *Former member organization.* An electing member organization that ceases to be a member of an affiliated group of organizations, the taxable year of which is different from its own, must thereafter determine its liability under §56.4911–1 for the excise tax imposed by section 4911(a) as if its taxable year were the taxable year of the affiliated group of which it was formerly a member. An organization to which this paragraph (e) applies that is liable for the excise tax imposed by section 4911(a) is liable for the tax as if the tax were imposed for its taxable year within which ends the taxable year of the affiliated group of which it was formerly a member. The Commissioner may, at the Commissioner's discretion, permit an organization to disregard the rules of this paragraph (e) and to determine any liability under section 4911(a) based upon its own taxable year.

§56.4911–9 Application of section 501(h) to affiliated groups of organizations.

(a) *Scope.* This section provides rules concerning the application of the limitations of section 501(h) to members of an affiliated group of organizations (as defined in §56.4911–7(e)(1)).

(b) *Determination required.* For each taxable year of an affiliated group of organizations, the calculations described in §1.501(h)–3(b)(1)(i) and (ii) must be made, based on the expenditures of the group. If, for a taxable year of an affiliated group, it is determined that the sum of the affiliated group's lobbying or grass roots expenditures for the group's base years exceeds 150 percent of the sum of the group's corresponding nontaxable amounts for the base years, then under section 501(h), each member organization that is an electing member organization (as defined in §56.4911–7(e)(4)) at any time in the taxable year of the affiliated group shall be denied tax exemption beginning with its first taxable year beginning after the end of such taxable year of the affiliated group. Thereafter, exemption shall be denied unless (pursuant to §1.501(h)–3(d)) the organization reapplies and is recognized as exempt as an organization described in section 501(c)(3). For purposes of this section, the term "base years" generally means the taxable year of the affiliated group for which a determination is made and the group's three preceding taxable years. Base years, however, do not include any year preceding the first year in which at least one member of the group was treated as described in section 501(c)(3).

(c) *Member organizations that are not electing organizations.* An organization that is a member of an affiliated group of organizations but that is not an electing member organization remains subject to the "substantial part test" described in section 501(c)(3) with respect to its activities involving attempts to influence legislation.

(d) *Filing of information relating to affiliated group of organizations*—(1) *Scope.* The filing requirements described in this paragraph (d) apply to each member of an affiliated group of organizations for the taxable year of the member with which, or within which, ends the taxable year of the affiliated group.

(2) *In general.* Each member of an affiliated group of organizations shall provide to every other member of the group, before the first day of the second month following the close of the affiliated group's taxable year, its name, identification number, and the information required under §1.6033–2(a)(2)(ii)(*k*) for its expenditures during the group's taxable year and for prior taxable years of the group that are base years under paragraph (b). For groups electing under §56.4911–7(e)(5) to have each member file information with respect to the group based on its taxable year, each member shall provide the information required by the preceding sentence by treating each taxable year of any member of the group as a taxable year for the group.

(3) *Additional information required.* In addition to the information required by §1.6033–2(a)(2)(ii)(*k*), each member of an affiliated group of organizations must provide on its annual return the group's taxable year and, if the election under §56.4911–7(e)(5) is made, the name, identification number, and taxable year identifying the return with which its consent to the election was filed.

(4) *Information required of electing member organization.* In addition to the information required by §1.6033–2(a)(2)(ii)(*k*) and paragraph (d)(3) of this section, each electing member organization (as defined in §56.4911–7(e)(4)) must provide on its annual return—

(i) The name and identification number of each member of the group, and

(ii) The appropriate calculation described in §56.4911–8(d), if the organization is an electing member organization liable for all or any portion of the excise tax imposed by section 4911(a).

(e) *Example.* The provisions of this section may be illustrated by the following example:

Example. (1) *M*, *N*, and *O* are affiliated organizations under §56.4911–7(a). *M*'s taxable year ends November 30, *N*'s, January 31, and *O*'s, June 30. On June 20, 1979, *O* files Form 5768 to elect to be governed by the expenditure test. *M* files Form 5768 in December of 1979. Neither *M* nor *O* revokes the election and no organization makes the election provided for in §56.4911–7(e)(5). *M*, *N*, and *O* constitute an affiliated group of organizations, the first taxable year of which is the calendar year 1979.

(2) Because the organizations did not elect under §56.4911–7(e)(5) to use their own taxable years as the group's taxable years, the expenditures of the affiliated group for its first taxable year are the expenditures made by *M*, *N*, and *O* during calendar year 1979, and are reported by *M*, *N*, and *O* on their returns for their taxable years within which falls December 31, 1979. *M* reports the expenditures of the affiliated group for 1979 on its return for its taxable year ending November 30, 1980; and *O*, on its return for its taxable year ending June 30, 1980. *N* is not an electing member (as defined in §56.4911–7(e)(4)). Accordingly, under paragraph (d)(3)(i) of this section, it reports the name and identification number of each member of the group.

(4) For the affiliated group's taxable years 1979, 1980, 1981, and 1982, the group has excess lobbying expenditures. Under section 4911(f)(1)(B) and §56.4911–8(d), *M* and *O*, as electing member organizations, are liable for a portion of the 25 percent excise tax imposed on the group's excess lobbying expenditures, based on their respective shares of the lobbying expenditures of all electing member organizations. For 1979, the excess lobbying expenditures are $20,000 ($100,000 – $80,000). The tax is 25% of $20,000 or $5,000; *M* must pay $3,750 [($60,000/$80,000) × $5,000 = $3,750], and *O* must pay $1,250 [($20,000/$80,000) × $5,000 = $1,250]. For 1980, the tax is $10,000 and each must pay $5,000. For 1981, the tax is $1,250 *M* must pay $750 and *O* must pay $500. For 1982, the tax is $30,000. *M* must pay $24,000 and O must pay $6,000. *M* and *O* are not liable for any separate §4911 excise tax that otherwise would have been imposed on their separate excess lobbying expenditures.

(5) Under §56,4911–9(b), the group must make the calculation described in §1.501(h)–3(b)(1) 1982. The

(3) The following tables summarize the expenditures by the affiliated group for the calendar years indicated. None of the group's lobbying expenditures for its taxable years 1979 through 1982 were grass roots expenditures.

Table I: Group's Expenditures

Year	Exempt Purpose Expenditures (EPE)	Calculation	Lobbying Nontaxable Amount (LNTA)	Lobbying Expenditures (LE)
1979	$400,000	(20% × $400,000 =)	$80,000	$100,000
1980	$300,000	(20% × $300,000 =)	$60,000	$100,000
1981	$600,000	(20% × $500,000 + 15% × $100,000 =)	$115,000	$120,000
1982	$500,000	(20% × $500,000 =)	$100,000	$220,000
	Totals: $1,800,000	$355,000	$540,000	

	Exempt Purpose Expenditures		Lobbying Nontaxable Amount		Lobbying Expenditures		
	M	*O*	*M*	*O*	*M*	*O*	*M plus O*
1979	125,000	100,000	25,000	20,000	60,000	20,000	80,000
1980	100,000	50,000	20,000	10,000	40,000	40,000	80,000
1981	250,000	100,000	50,000	20,000	60,000	40,000	100,000
1982	200,000	100,000	40,000	20,000	160,000	40,000	200,000

following illustrates only the required calculation for the group's taxable year 1982. For its taxable year 1982, the group must determine whether it normally has made lobbying expenditures in excess of its lobbying ceiling amount. The determination takes into account the group's expenditures in base years 1979 through 1982. The sum of the group's lobbying expenditures for the base years ($540,000) exceeds 150% of the sum of the group's lobbying nontaxable amounts for the base years (150% × $355,000 = $532,000). Therefore, for its taxable year 1982, the group normally has made lobbying expenditures in excess of its lobbying ceiling amount. Under section 501(h) and §56.4911–9(b), *M* is not exempt from tax under section 501(a) as an organization described in section 501(c)(3) for its taxable year beginning December 1, 1983, and *O* is not exempt for its year beginning July 1, 1983. Whether *N*'s lobbying expenditures disqualify it for tax exemption at any time after January 1, 1979, is determined under the substantial part test of section 501(c)(3).

(f) *Cross reference*. For other provisions relating to members of an affiliated group of organizations, see §§56.4911–3(d)(2), 56.4911–4(c)(2), 56.4911–4(e), and 56.4911–5(f)(3).

§56.4911–10 Members of a limited affiliated group of organizations.

(A) *Scope*. This section provides additional rules for members of a limited affiliated group of organizations, as defined in paragraph (b) of this section (relating generally to organizations that are affiliated solely by reason of provisions of their governing instruments that extend control solely with respect to national legislation). Except otherwise provided in this section, §§56.4911–8 and 56.4911–9 do not apply to members of a limited affiliated group. Thus, as modified by this section, the regulations under sections 501(h) and 4911 apply to electing members of a limited affiliated group individually. For example, §§56.4911–2(b), 56.4911–2(c), and 56.4911–4 which, by their terms, include amounts described in paragraph (d) of this section, are used in applying sections 501(h) and 4911 to controlling member organizations (within the meaning of paragraph (c) of this section). Except as otherwise provided in this section, members of a limited affiliated group that are not electing organizations are subject to the substantial part test.

(b) *Members of limited affiliated group*. For purposes of section 4911, a limited affiliated group consists of two or more organizations that meet the following requirements:

(1) Each organization is a member of an affiliated group of organizations as defined in section 56.4911–7(e);

(2) No two members of the affiliated group described in paragraph (b)(1) of this section are affiliated by reason of interlocking governing boards under section 56.4911–7(b); and

(3) No member of the affiliated group described in paragraph (b)(1) of this section is, under its governing instrument, bound by decisions of one or more of the other such members on legislative issues other than national legislative issues.

Each organization in a group of organizations that satisfies the requirements of the preceding sentence is a member of the limited affiliated group.

(c) *Controlling and controlled organizations*. For purposes of this section, a member of a limited affiliated group is a controlling member organization if it controls one or more of the other members of the limited affiliated group, and a member of a limited affiliated group is a controlled member organization if it is controlled by one or more of the other members of the limited affiliated group. For purposes of the preceding sentence, whether an organization controls a second organization shall be determined by whether the second organization is bound, under its governing instruments, directly or indirectly, by actions taken by the first organization on national legislative issues.

(d) *Expenditures of controlling organization*— (1) *Scope*. This paragraph (d) applies to a controlling member organization that has the expenditure test election in effect for its taxable year. This paragraph (d) applies whether or not the organization is also a controlled member organization. In determining a controlling member organization's expenditures, no expenditure shall be counted twice.

(2) *Expenditures for direct lobbying*. A controlling member organization for which the expenditure test election is in effect shall include in its direct lobbying expenditures for its taxable year the direct lobbying expenditures (as defined in §56.4911–2(b)) paid or incurred with respect to national legislative issues during such year by each organization that is a member of the limited affiliated group and is controlled (within the meaning of paragraph (c) of this section) by such controlling member organization.

(3) *Grass roots expenditures*. A controlling member organization for which the expenditure test election is in effect shall include in its grass roots expenditures for its taxable year the grass roots expenditures (as defined in §56.4911–2(c)) paid or incurred with respect to national legislative issues during such year by each organization that is a member of the limited affiliated group and is controlled (within the meaning of paragraph (c) of this section) by such controlling member organization.

(4) *Exempt purpose expenditures*. The exempt purpose expenditures of a controlling member organization do not include the exempt purpose expenditures (other than lobbying expenditures described in paragraphs (d)(2) and (d)(3) of this section), of any organization that is a controlled member organization with respect to it.

(e) *Expenditures of controlled member.* A controlled member organization that is an electing organization but that does not control (within the meaning of paragraph (c) of this section) any organization in the limited affiliated group shall apply sections 501(h) and 4911 and the regulations thereunder without regard to the expenditures of any other member of the limited affiliated group.

(f) *Reports of members of limited affiliated groups*—(1) *Controlling member organization's additional information on annual return.* In addition to the information required by §1.6033-2(a)(2)(ii)(*k*), each controlling member organization for which the expenditure test election is in effect must provide on its annual return the name and identification number of each member of the limited affiliated group.

(2) *Reports of controlling members to other members.* Each controlling member organization for which an expenditure test election is in effect must notify each member that it controls of its taxable year in order for the controlled organization to prepare the report required by paragraph (f)(3) of this section. Such notification must be made before the beginning of the second month after the close of each taxable year of the controlling member for which the election is in effect.

(3) *Reports of controlled member organization.* Every controlled member organization (whether or not the expenditure test election is in effect with respect to it shall provide to each member of the limited affiliated group that controls it, before the first day of the second month following the close of the taxable year of each such controlling organization, its name, identification number, and the lobbying expenditures and grass roots expenditures on national legislative issues incurred by the controlled member organization.

(g) *National legislative issues.* The term "national legislative issue" means legislation, limited to action by the Congress of the United States or by the public in any national procedure. If an issue is both national and local, it is characterized as a national legislative issue if the contemplated legislation is Congressional legislation.

(h) *Examples.* The provisions of this section are illustrated by the following examples.

Example (1). State *X* has an income tax law that uses definitions contained in the Internal Revenue Code as it may be amended from time to time. Legislation to change a definition in the Internal Revenue Code is pending in Congress. This is a national legislative issue even though Congressional action may affect state law.

Example (2). Organization *M* takes a position favoring approval by Congress of a proposed amendment to the United States Constitution. This is a national legislative issue. After approval by Congress and submission to the states for ratification, the proposed amendment ceases to be a national legislative issue.

Example (3). *N*, *O*, and *P* are organizations described in section 501(c)(3) that do not have interlocking governing boards, within the meaning of §56.4911-7(b). *N* has elected the expenditure test under section 501(h). By virtue of the governing instruments of *O* and *P*, any decision made by *N* on national legislative issues (such as issues concerning action on acts, bills, resolutions, or similar items by Congress) binds both *O* and *P*. Under their governing instruments, *O* and *P* are not bound on any other issues. Therefore, *N*, *O*, and *P* constitute a limited affiliated group. If *P* sends a series of letters and pamphlets to members of Congress in support of bill *V*, their cost will be included in *N*'s and *P*'s expenditures for direct lobbying and in *N*'s and *P*'s exempt purposes expenditures, but will not be included in *O*'s lobbying expenditures. If *N* hires a lobbyist to solicit support for bill *V*, the cost of hiring the lobbyist will be includable only in *N*'s lobbying expenditures. Any lobbying expenditures incurred by either *O* or *P* on any issue that is not a national legislative issue will not be included in *N*'s lobbying expenditures.

Example (4). *Y* is an electing organization and a member of a limited affiliated group of organizations. *Y* controls organizations *A*, *B*, and *C* with respect to national legislative issues but is not controlled by any other organization. *Y*'s taxable year is the calendar year. During 1982, *A* dissolves on March 15th and *D*, also controlled by *Y* with respect to national legislative issues, is established on May 1st. For 1982 the limited affiliated group comprises *Y*, *A*, *B*, *C*, and *D*.

Example (5). *P*, *Q*, *R*, and *S* are electing organizations. The governing instruments of *Q* require it to adopt the positions on national legislative issues adopted by *P*, *R* is similarly bound by *Q*'s positions. *R* and *S* have interlocking governing boards, within the meaning of section 56.4911-7(b), but *S*'s governing instruments do not require it to adopt the position of any other organization on any legislative issues. Under §56.4911-7(e)(1), *P*, *Q*, *R*, and *S* are members of an affiliated group. Applying paragraph (b) of this section, it is determined that (1) *P*, *Q*, *R* and *S* are members of an affiliated group; and (2) *R* and *S* are affiliated by reason of interlocking governing boards. Accordingly, *P*, *Q*, *R* and *S* are not a limited affiliated group. Similarly *P*, *Q*, and *R* do not constitute a limited affiliated group because they are members of an affiliated group comprising *P*, *Q*, *R*, and *S*, two of whose members, *R* and *S*, are affiliated by reason of interlocking governing boards.

Example 6. *T*, *U*, *V*, and *W* are electing organizations. The governing instruments of *U* and *V* require them to adopt the positions on national legislative issues adopted by *T*, but do not require them to adopt the positions of any organization on any other legislative issues. The governing documents of *W* require it to adopt the positions of *V* on all legislative issues. Applying paragraph (b) of this section, it is determined that, (1) *T*, *U*, *V*, and *W* are all members of an affiliated group: (2) no two of *T*, *U*, *V*, and *W* are affiliated by reason of interlocking governing boards; but (3) *W* is bound, under its governing instrument, by decisions of *V* on legislative issues that are not national legislative issues. Accordingly, *T*, *U*, *V*, and *W* do not constitute a limited affiliated group. Similarly, *T*, *U*, and *V* do not constitute a limited affiliated group. *T*, *U*, *V*, and *W* are an affiliated group under §56.4911-7.

§56.6001-1 Notice or regulations requiring records, statements, and special returns.

(a) *In general.* The provisions of §53.6001-1 shall apply to any person subject to tax under chapter 41, Subtitle D, of the Code, by treating each reference to chapter 42 in §53.6001-1 as a reference to chapter 41.

(b) *Cross references.* See §56.4911-6 for general information on records of lobbying expenditures. See §§56.4911-9(d) and 56.4911-10(f) for information that members of an affiliated group and a limited affiliated group, respectively, are to provide to other members of the group and to the Internal Revenue Service.

§56.6011-1 General requirement of return, statement, or list.

Every organization liable for the tax imposed by section 4911(a) shall file an annual return with respect to the tax on the form prescribed by the Internal Revenue Service for that purpose and shall include the information required by the form and its instructions.

ROSCOE L. EGGER, JR.,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on November 4, 1986, 8:45 a.m., and published in the issue of the Federal Register for November 5, 1986, 51 F.R. 40211)

Deletions from Cumulative List of Organizations Contributions to Which Are Deductible Under Section 170 of the Code

Announcement 86-117

The names of organizations that no longer qualify as organizations described in section 170(c)(2) of the Internal Revenue Code of 1954 are listed below.

Generally, the Service will not disallow deductions for contributions made to a listed organization on or before the date of announcement in the Internal Revenue Bulletin that an organization no longer qualifies. However, the Service is not precluded from disallowing a deduction for any contributions made after an organization ceases to qualify under section 170(c)(2) if the organization has not timely filed a suit for declaratory judgment under section 7428 and if the contributor (1) had knowledge of the revocation of the ruling or determination letter, (2) was aware that such revocation was imminent, or (3) was in part responsible for or was aware of the activities or omissions of the organization that brought about this revocation.

If on the other hand a suit for declaratory judgment has been timely filed, contributions from individuals and organizations described in section 170(c)(2) that are otherwise allowable will continue to be deductible. Protection under section 7428(c) would begin on December 1, 1986, (the date of publication of this announcement) and would end on the date the court first determines that the organization is not described in section 170(c)(2) as more particularly set forth in section 7428(c)(1). For individual contributors, the maximum deduction protected is $1,000, with a husband and wife treated as one contributor. This benefit is not extended to any individual who was responsible, in whole or in part, for the acts or omissions of the organization that were the basis for revocation.

Genie Project, Inc., The, Waterbury, CT
Human Growth & Training Associates, Inc., Wilmington, NC
Isabel I. Gray fbo University of Louisville, Louisville, KY
Jaycee Boys Home, Inc., Rock Hill, SC
Michigan Association of School Boards, Inc., Lansing, MI

Average Annual Mortgage Originations

Announcement 86–118

Issuers of mortgage revenue bonds may rely on the average annual mortgage originations for each state, the District of Columbia, Guam, Puerto Rico, and the Virgin Islands, as published in Rev. Proc. 85–39, 1985–2 C.B. 443, for purposes of determining whether the required portion of bond proceeds will be made available for financing single-family, owner-occupied residences in targeted areas under the provisions of section 143(h) of the Internal Revenue Code. Section 143(h) was added by the Tax Reform Act of 1986, Pub. L. No. 99–514, section 1301, 100 Stat. , to replace former section 103A(h).

Section 103(a) of the Code provides that, with certain exceptions, gross income does not include interest on any state or local bond. If the applicable requirements set forth in sections 146, 147, 148, and 149 are satisfied, section 103(a) applies to a qualified mortgage bond. Section 143(a)(1)(A) provides that a qualified mortgage bond is a bond that is issued as part of a qualified mortgage issue. Section 143(a)(2)(A) provides that a qualified mortgage issue means an issue by a state or a political subdivision of the state of one or more bonds, but only if all of the proceeds of such issue (exclusive of issuance costs and a reasonably required reserve) are to be used to finance owner-occupied residences and certain additional requirements are satisfied.

This announcement addresses the additional requirement contained in section 143(h) of the Code. Section 143(h) requires that a portion of bond proceeds must be made available for owner financing of targeted area residences. A targeted area residence is a residence in either a qualified census tract or an area of chronic economic distress. The portion of the proceeds of an issue required to be made available in targeted areas is the lesser of (1) 20 percent of the proceeds, or (2) 40 percent of the average annual aggregate principal amount of mortgages executed during the immediately preceding 3 calendar years for single-family, owner-occupied residences in targeted areas within the jurisdiction of the issuing authority.

When determining the portion of the proceeds that must be made available for owner financing of targeted area residences under the second alternative, issures of mortgage revenue bonds may rely upon the amount produced by a formula described in section 6a.103A–2(h)(3) of the Temporary Income Tax Regulations (issued under former section 103A(h) of the Code). One component of the formula is the average annual mortgage originations for the state in which the issuing jurisdiction is located. Section 6a.103A–2(h)(3) provides that the issuing jurisdiction may use the Treasury Department estimate of the average annual mortgage originations published with the mortgage volume safe harbor estimate. Under former section 103A(g), a state volume cap was equal to the greater of 9 percent of the average annual mortgage originations or $200,000,000. The volume cap under section 146 is generally equal to the greater of $75 multiplied by the state population, or $250,000,000.

Rev. Proc. 85–39 contains the list of 1985 state ceiling safe harbor limitations for qualified mortgage bonds. It also lists the average annual mortgage originations for each state. Issuers of mortage revenue bonds may rely on the average annual mortgage originations published in Rev. Proc. 85–39 until new average annual mortgage originations are published.

Numerical Finding List[1]

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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December 8, 1986

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

SPECIAL ANNOUNCEMENT

Announcement 86–119, page 25.
Service One, Income Tax, of the Bulletin Index-Digest System has been revised. This Service provides a comprehensive and up-to-date method of researching Income Tax items published in 33 years of the Bulletin (1953–1985), and may now be purchased from the Superintendent of Documents, Washington, D.C. Estate and Gift Taxes (Service Two), Employment Taxes (Service Three), and Excise Taxes (Service Four) will be revised as of December 1986.

INCOME TAX

Rev. Rul. 86–141, page 6.
S corporations; transition rules for corporations converting to S corporation status. Guidance is provided to corporations who may wish to convert to S corporation status to obtain transition relief from the corporate level tax on built-in gains recognized by a former C corporation during the 10-year period after it becomes an S corporation.

Rev. Rul. 86–143, page 5.
Federal rates, adjusted federal rates, adjusted federal long-term rate, and the long-term tax-exempt rate. For purposes of sections 1274, 1288, 382 and other sections of the Code, a table sets forth the rates for December 1986.

Rev. Rul. 86–144, page 4.
Moratorium on application of section 1.861–8 of the regulations; combined taxable income of a Domestic International Sales Corporation (DISC) or a Foreign Sales Corporation (FSC). The moratorium on the application of section 1.861–8 of the regulations does not affect the calculation of the combined taxable income of a DISC or FSC and its related supplier.

Finding Lists begin on page 29.

Department of the Treasury
Internal Revenue Service

T22.23:

Rev. Proc. 86–44, page 15.
Areas in which the Service will now rule; reorganizations; section 368(a)(2)(E)(ii) "control" requirements. The Service will now rule as to whether a transaction qualifies under section 368(a)(1)(A) and (a)(2)(E) when there has been a prior redemption of stock of the acquired corporation as part of the plan of reorganization. Rev. Rul. 86–3 modified.

Ct. D. 2036, page 10.
Refunds and credits; Panama Canal Commission employees. U.S. citizen employees of the Panama Canal Commission are not entitled to refunds of federal income taxes paid on income received as a result of their work for the Commission. O'Connor, Supreme Court of the United States.

EMPLOYMENT TAXES

T.D. 8105, page 7.
LR–12–86, page 25.
Temporary and proposed regulations under sections 6011, 6071, 6157 and 6302 of the Code relate to the time and manner of making quarterly payments of the railroad unemployment repayment tax.

TAX CONVENTIONS

Rev. Rul. 86–145, page 14.
United States-United Kingdom Income Tax Convention; Article 15(2)(a). The term "tax year concerned" refers to the tax year in which personal services are performed rather than to the tax year in which compensation for those services is received.

ADMINISTRATIVE

Rev. Proc. 86–45, page 15.
Magnetic tape reporting; information returns; Form 8027. Requirements and conditions are set forth for submitting Form 8027, Employer's Annual Information Return of Tip Income and Allocated Tips, on magnetic tape. Rev. Proc. 84–69 superseded.

Page 23.
Social Security contribution and benefit base. The Secretary of the Department of Health and Human Services has announced that the contribution and benefit base for remuneration paid in 1987 and self-employment income earned in taxable years beginning in 1987 is $43,800.

Announcement 86–120, page 26.
Tables are provided for the withholding of income tax from total distributions paid in 1987 under a qualified pension, profit-sharing, or stock bonus plan. These tables will appear in Publication 493, Alternative Tax Withholding Methods and Tables.

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term and long-term rates are set forth for the month of December, 1986. See Rev. Rul. 86-143, page 5.

Section 382.—Limitation on Net Operating Loss Carryforwards and Certain Built-In Losses Following Ownership Change

The adjusted federal long-term rate is set forth for the month of December 1986. The long-term tax-exempt rates will be set forth beginning in January 1987. See Rev. Rul. 86-143, page 5.

Section 383.—Special Limitations on Unused Business Credits, Research Credits, Foreign Taxes, and Capital Losses

The adjusted federal long-term rate is set forth for the month of December 1986. The long-term tax-exempt rates will be set forth beginning in January 1987. See Rev. Rul. 86-143, page 5.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of December, 1986. See Rev. Rul. 86-143, page 5.

Section 468.—Special Rules for Mining and Solid Waste Reclaimation and Closing Costs

Federal short-term, mid-term and long-term rates are set forth for the month of December, 1986. See Rev. Rul. 86-143, page 5.

Section 483.—Special Limitations on Certain Excess Credits, etc.

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of December 1986. See Rev. Rul. 86-143, page 5.

Section 861.—Income from Sources within the United States

26 CFR 1.861–8: Computation of taxable income from sources within the United States and from other sources and activities.
(Also Section 994, 1.994–1.)

Moratorium on application of section 1.861–8 of the regulations; combined taxable income of a Domestic International Sales Corporation (DISC) or a Foreign Sales Corporation (FSC). The moratorium on the application of section 1.861–8 of the regulations does not affect the calculation of the combined taxable income of a DISC or FSC and its related supplier.

Rev. Rul. 86–144

ISSUE

Whether the moratorium on the application of section 1.861-8 of the Income Tax Regulations dealing with the allocation of research and development expenses, under section 223 of the Economic Recovery Tax Act of 1981 (ERTA 81), as extended by section 126 of the Tax Reform Act of 1984 (TRA 84), applies for the purpose of computing the combined taxable income of a Domestic International Sales Corporation (DISC), or a Foreign Sales Corporation (FSC), and its relates supplier.

FACTS

Situation 1

X is a calendar year domestic corporation engaged in the business of manufacturing products for sale both domestically and abroad. *Y* is a wholly owned domestic subsidiary of *X* that qualifies as a DISC under section 992 of the Code for the years 1983 and 1984. *X* pays a commission to *Y* in connection with the sale of export property by *X*. The income generated by the export sales consists of income which is United States source and foreign source income under sections 861 through 863. Both *X* and *Y* use the calendar year as their taxable year.

For the year ended December 31, 1983, *X* and *Y* elected to use the combined taxable income (CTI) method under section 994(a)(1) for determining *Y*'s taxable income and, correspondingly, *X*'s commission expense deduction. *X* incurred certain research or experimental expenses within the meaning of section 174 of the Internal Revenue Code during its 1983 tax year from activities conducted in the United States related to exported products. These research and experimental expenses constitute research and development expenses (R&D expenses) as that term is used for purposes of section 1.861-8 of the Income Tax Regulations relating to the allocation and apportionment of R&D expenses.

Situation 2

The facts are the same as in Situation 1, except that the R&D expenses were incurred in the tax year ending December 31, 1984.

Situation 3

The facts are the same as in Situation 1, except that the R&D expenses were incurred in the tax year ended December 31, 1985, and that *X* pays a commission to *Z* in connection with the sale of export property by *X*. *Z* is a wholly owned foreign subsidiary of *X* that qualifies as a FSC under section 923 of the Code.

LAW AND ANALYSIS

Section 994 of the Code provides that the taxable income of a DISC and its related supplier may be based on a transfer price calculated using the combined taxable income method. Under section 1.994–1(c)(6) of the regulations, the CTI of a DISC and its related supplier from a sale of export property is defined as the excess of the gross receipts (as defined in section 993(f)) of the DISC or its related supplier from the sale, over the total costs of the DISC and related supplier which relate to such gross receipts. Costs (other than cost of goods sold) that are treated as relating to gross receipts from sales of export property include (a) expenses, losses, and other deductions definitely related and therefore allocated thereto and (b) a ratable part of any other expenses, losses, or other deductions that are not definitely related to a class of gross income, determined under the rules set forth in section 1.861–8.

Section 1.861–8 of the regulations provides rules for the allocation and apportionment of expenses and deductions (*e.g.*, R&D expenses). Under Example 23 of section 1.861–8(g), R&D expenses are allocated and apportioned in two stages. In the first stage, R&D expenses are apportioned in order to calculate CTI for DISC and FSC purposes by treating the DISC or FSC and its related supplier as a single taxpayer. Section 1.861–8(f)(1)(iii) and Example 23 of Section 1.861–8(g). In the second stage, R&D expenses are apportioned for purposes of calculating the foreign tax credit limitation under section 904. Section 1.861–8(f)(1)(i).

The computation of CTI (first stage) does not involve geographic sourcing of income. It requires apportionment of R&D expenses between the statutory grouping of gross income from exports and other gross income. The sourcing of the income as United States source of foreign source is irrelevant when allocating deductions for purposes of determining CTI. On the other hand, geographic sourcing of income is required for purposes of calculating the foreign tax credit limitation in the second stage of apportionment.

Section 223 of the ERTA 81 provides that, for a taxpayer's first two taxable years beginning after August 13, 1981, all research and experimental expenditures (within the meaning of section 174 of the Code) which are paid or incurred in those taxable years for research activities conducted in the United States are to be allocated or apportioned to income from sources within the United States. Section 223 of ERTA 81 also directs the Treasury to conduct a study with respect to the impact which section 1.861–8 of the regulations would have on research and experimental activities conducted in the United States and on the availability of the foreign tax credit. The Conference Committee Report, H.R. Rep. No. 97–215, 97th Cong., 1st Sess. 224 (1981), 1981–2 C.B. 496, accompanying ERTA states that, during the two-year moratorium, research and experimental expenses which are paid or incurred in those taxable years for research activities conducted in the United States shall be allocated or apportioned to income from *sources within the United States* for all purposes under the Code.

Section 126 of the TRA 84 extends the moratorium on the research and experimental expense allocation rules to apply to taxpayer's taxable years beginning after August 13, 1983, and on or before August 1, 1985. In the event that the taxpayer's third taxable year commencing after August 13, 1981, does not begin during this period, the extension of the moratorium applies also to that taxable year. The Conference Committee Report, H.R. Rep. No. 98–861, 98th Cong., 2d Sess. 1262 (1984), 1984–3 (Vol. 2) C.B. 516, accompanying the TRA 84 states that the moratorium applies only to the allocation of research expenses for the purpose of *geographic sourcing* of income and that it does not apply for other purposes, such as the computation of combined taxable income of a DISC or FSC and its related supplier.

The moratorium under section 223 of ERTA 81 was enacted because of Congressional concern that the allocation and apportionment of R&D expenses under section 1.861–8 of the regulations could cause research activities performed in the United States to be moved abroad. The same concerns that resulted in the ERTA 81 legislation were present when Congress extended the moratorium by enacting section 126 of TRA 84. Prior to the moratorium, a percentage of all R&D expenses was apportioned between the U.S. and foreign source income. Section 1.861–8(e)(3). Expenses apportioned to foreign source income generally reduce the amount of the foreign tax credit by operation of the limitation contained in section 904. In order to encourage domestic research activities, Congress enacted the moratorium requiring the allocation or apportionment of domestic research and experimental expenses against U.S. source income. This allocation method provides a benefit to taxpayers performing research in the United States by increasing the amount of the foreign tax credit limitation.

The determination of CTI differs from that of foreign source taxable income. CTI determines the relative amount of income earned by a DISC or FSC and its related supplier from the export of U.S. manufactured goods and, thereby, the tax benefit derived from the export transaction. A taxpayer may derive gross receipts qualifying for DISC or FSC treatment, calculate CTI, and claim the related tax benefits with respect to export transactions irrespective of whether they generate foreign source or domestic source income. Therefore, the sourcing of income is not relevant for purposes of calculating CTI.

The moratorium enacted in section 223 of ERTA 81 and continued in section 126 of TRA 84 revised the allocation and apportionment of R&D expenses for identical reasons *i.e.*, in order to modify the calculation of foreign source taxable income and adjust the foreign tax credit limitation. The moratorium was not intended to modify the amount of DISC or FSC benefits derived from export transactions and, therefore, does not apply to the determination of CTI.

HOLDING

The moratorium on the application of section 1.861–8 of the regulations, as prescribed by section 223 of ERTA and as extended by section 126 of the TRA 84, does not affect the calculation of the combined taxable income of *X* and *Y* or *X* and *Z*. As a result, in all the situations described above, a portion of *X*'s research expenses will be apportioned between gross income from export sales, without regard to its source as domestic or foreign, and gross income from domestic sales under section 1.861–8 in the computation of the combined taxable income of the DISC or FSC and its related supplier.

Section 994.—Intercompany Pricing Rules

26 CFR 1.994–1: Inter-company pricing rules for DISC's.

The moratorium on the application of section 1.861–8 of the regulations does not affect the calculation of the combined taxable income of a DISC or FSC and its related supplier. See Rev. Rul. 86–144, page 4.

Section 1273.—Determination of Amount of Original Issue Discount

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of December 1986. See Rev. Rul. 86–143, this page.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 280G, 382, 383, 467, 468, 483, 1273, 1288, 7872.)

Rev. Rul. 86–143

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of December 1986 are as follows:

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term				
AFR	6.18%	6.09%	6.04%	6.01%
110% AFR	6.81%	6.70%	6.64%	6.61%
120% AFR	7.44%	7.31%	7.24%	7.20%
Mid-Term				
AFR	7.16%	7.04%	6.98%	6.94%
110% AFR	7.89%	7.74%	7.67%	7.62%
120% AFR	8.63%	8.45%	8.36%	8.30%
Long-Term				
AFR	7.71%	7.57%	7.50%	7.45%
110% AFR	8.50%	8.33%	8.25%	8.19%
120% AFR	9.29%	9.08%	8.98%	8.91%

For purposes of section 1288 of the Code, the short-term, mid-term, and long-term adjusted federal rates (adjusted AFR) for the month of December 1986 are as follows:

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-term				
AFR	4.13%	4.09%	4.07%	4.06%
Mid-term				
AFR	5.10%	5.04%	5.01%	4.99%
Long-term				
AFR	6.35%	6.25%	6.20%	6.17%

For purposes of section 382 of the Code, the adjusted federal long-term rate for December 1986 is 6.35 percent. The long-term tax-exempt rate for section 382 purposes will be published monthly beginning in January 1987.

Section 1288.—Treatment of Original Issue Discount on Tax-Exempt Obligations

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of December 1986. See Rev. Rul. 86-143, page 5.

Section 1362.—Election; Revocation; Termination

(Also Section 1374.)

S corporations; transition rules for corporations converting to S corporation status. Guidance is provided to corporations who may wish to convert to S corporation status to obtain transition relief from the corporate level tax on built-in gains recognized by a former C corporation during the 10-year period after it becomes an S corporation.

Rev. Rul. 86-141[1]

PURPOSE

Following the enactment of the Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. (Act), there has been uncertainty regarding the manner in which a corporation can obtain transition relief from the provisions of subtitle D of title VI of the Act by electing to be an S corporation. The provisions of subtitle D generally require a corporation to recognize gain or loss on a liquidating sale of its assets and on a liquidating or nonliquidating distribution of its assets (the repeal of the *General Utilities* doctrine). This revenue ruling interprets certain pertinent provisions of the Act and of subchapter S of the Internal Revenue Code that are applicable to a corporation that seeks to obtain transition relief by electing to be an S corporation.

LAW

Section 1374 of the Code, as amended by section 632 of the Act, generally imposes a corporate-level tax on the "built-in" gains recognized by a former C corporation during the 10-year period beginning with the first day of the first taxable year for which the corporation becomes an S corporation (built-in gains tax).

Section 633(b) of the Act contains the effective date for the amendments to section 1374 of the Code. It provides that the built-in gains tax shall apply in taxable years beginning after December 31, 1986, but only if the first taxable year for which the corporation is an S corporation is pursuant to an election made after December 31, 1986. Thus, as explained in the Conference Report, the amendments to section 1374 "will generally be effective with respect to S elections made after December 31, 1986." 2 H.R. Rep. No. 99-841 (Conf. Rep.), 99th Cong., 2d Sess. II-203 (1986). Section 1374, prior to its amendment by section 632 of the Act, continues to apply in situations where section 1374, as amended by the Act, is inapplicable.

Section 1362(a)(1) of the Code provides generally that a small business corporation, as defined in section 1361(b) (small business corporation), may make an election (S election) to be an S corporation. Section 1362(b)(1) provides that an S election may be made for the current or the following taxable year of the corporation, but an election may be effective for the current taxable year only if it is made on or before the 15th day of the third month of that year.

Section 18.1362-1 of the Temporary Income Tax Regulations provides that an S election should be made by filing Form 2553, Election by a Small Business Corporation, at the appropriate Internal Revenue Service Center along with the required consents of the shareholders. The regulations further provide, in effect, that section 1362(b)(2) of the Code (concerning certain elections that are made for a taxable year but are treated as made for the succeeding taxable year) applies only if a corporation meets all of the requirements provided in section 1361(b) at the time the election is made.

Section 1362(g) of the Code prohibits a small business corporation (and any successor corporation) from making a new S election with respect to any of the first five taxable years after a termination of its S election was effective pursuant to section 1362(d), unless the Secretary consents to such new election.

Section 633(d)(1)-(7) of the Act provides a transition rule for a qualified small corporation (qualified corporation) that completely liquidates prior to January 1, 1989. Section 633(d)(8) of the Act provides that rules similar to the rules of section 633(d) of the Act shall apply for purposes of applying section 1374 of the Code, as amended by the Act, in the case of a qualified corporation that becomes an S corporation before January 1, 1989.

Section 633(d)(1) of the Act provides that if a qualified corporation completely liquidates before January 1, 1989, it generally will not be subject to the repeal of the *General Utilities* doctrine.

Section 633(d)(2) of the Act, however, provides that section 633(d)(1) of the Act shall not apply, and thus gain or loss will be recognized, on the liquidating sale or distribution of certain items, including assets resulting in ordinary gain or loss and capital assets held for not more than 6 months. Further, section 633(d)(1) of the Act provides that this small corporation exception will be phased out where the applicable value of the corporation exceeds $5,000,000. If the applicable value of a corporation exceeds $5,000,000, gain or loss will be recognized to the extent that such gain or loss exceeds the applicable percentage of each gain or loss from capital assets held for more than 6 months. The applicable percentage equals 100 percent reduced by the amount that bears the same ratio to 100 percent as the excess of the applicable value over $5,000,000 bears to $5,000,000.

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[1] Also released as News Release IR-86-159, dated November 20, 1986.

Section 633(d)(5) of the Act generally defines "qualified corporation" as any corporation more than 50 percent (by value) of the stock in which is held by 10 or fewer "qualified persons," as defined in section 633(d)(6) of the Act, and the applicable value of which does not exceed $10,000,000.

Section 633(d)(4) of the Act defines "applicable value" as the fair market value of all of the stock of the corporation on the date of the adoption of the plan of complete liquidation (or if greater, on August 1, 1986).

ANALYSIS AND HOLDINGS

Conversion To S Corporation Status

As stated above, section 1374, as amended by the Act, is not applicable to an S corporation if its S election in effect after January 1, 1987, was made before that date. The date on which the S election is made is determinative, notwithstanding that the election may not be effective until a taxable year beginning after December 31, 1986. *See* Conference Report at II–203. A corporation with such an election in effect is subject to section 1374 as in effect prior to its amendment by the Act. In order to avoid section 1374, as amended by the Act, a corporation whose S election was terminated before January 1, 1987, must have made a new election before January 1, 1987. For example, a corporation whose S election was made in 1976 and was terminated in 1978 must make a new, valid S election prior to January 1, 1987, in order to avoid section 1374, as amended by the Act.

Section 1362 of the Code and section 18.1362–1 of the temporary regulations provide that, to make a valid S election, a corporation must be a small business corporation at the time the Form 2553 effecting the election is filed. Accordingly, a corporation that is not a small business corporation can avoid the provisions of section 1374, as amended by the Act, only if it becomes a small business corporation and then makes a valid S election before January 1, 1987. In addition, the election must be effective for the current or succeeding taxable year.

A corporation that does not make a valid S election prior to January 1, 1987, but is a qualified corporation as defined in section 633(d)(5) of the Act, may nevertheless qualify under section 633(d) of the Act for partial transition relief from the built-in gains tax imposed by section 1374, as amended by the Act. Under section 633(d)(8) of the Act, rules similar to those applicable to a liquidating corporation under section 633(d) of the Act apply for purposes of determining whether and to what extent this relief is available to a qualified corporation that makes an S election after December 31, 1986.

Such a qualified corporation that becomes an S corporation before January 1, 1989, unlike a qualified corporation that obtains transition relief from the repeal of the *General Utilities* doctrine under section 633(d)(1)–(7) of the Act, does not have to liquidate to qualify for relief from the amended provisions of section 1374 of the Code. This relief does not apply to the items described in section 633(d)(2) (which include ordinary income and short-term capital gain). Thus, the built-in gains tax imposed by section 1374, as amended by the Act, will apply to recognized built-in ordinary gains and recognized built-in short-term capital gains. Moreover, for a corporation with an applicable value between $5,000,000 and $10,000,000, this relief is limited to the applicable percentage of the gain from capital assets held for more than 6 months. Thus, the built-in gains tax will apply to the amount of any recognized built-in long-term capital gains in excess of the applicable percentage of each such gain. Section 1374, as it existed prior to the amendments made by the Act, will apply to the applicable percentage of each such gain.

The applicable value of a qualified corporation that becomes an S corporation is the greater of the fair market value of all of the stock of the corporation on either the date a valid S election is made or August 1, 1986.

S Elections After Terminations

Pursuant to section 1362(g) of the Code, the Secretary hereby consents to an election to convert to S corporation status by a small business corporation whose S election was terminated under section 1362(d) if it meets the following two conditions. First, the corporation makes the S election prior to January 1, 1987, or, in the case of a qualified corporation, the corporation becomes an S corporation before January 1, 1989. Second, the date that a revocation, as described in section 1362(d)(1), was filed under section 48.1362–3 of the temporary regulations or the effective date of a termination, as described in section 1362(d)(2)(B) or section 1362(d)(3)(A)(ii), occurred before October 22, 1986 (the date of enactment of the Act).

Any corporation that files a Form 2553 pursuant to the consent granted in the above paragraph should refer to this revenue ruling by either typing or legibly printing the following statement at the top of page 1 of Form 2553: "FILED UNDER REV. RUL. 86–141."

Section 1374.—Tax Imposed on Certain Capital Gains

The requirements that must be met by a corporation that makes an S election in order to obtain transition relief from the corporate-level tax on built-in gains recognized by a former C corporation during the 10-year period after it becomes an S corporation. See Rev. Rul. 86–141, page 6.

Section 6011.—General Requirement of Return, Statement, or List

26 CFR 31.6011(a)–3AT: Returns of the railroad unemployment repayment tax (temporary).

T.D. 8105

TITLE 26—INTERNAL REVENUE.—CHAPTER 1, SUBCHAPTER C, PART 31—EMPLOYMENT TAXES AND COLLECTION OF INCOME TAX AT SOURCE; PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Time and Manner of Making Quarterly Payments of the Railroad Unemployment Repayment Tax

AGENCY: Internal Revenue Service, Treasury.

ACTION: Temporary regulations.

SUMMARY: This document provides temporary regulations relating to the time and manner of making quarterly payments of the railroad unemployment repayment tax. The text of the temporary regulations set forth in this document also serves as the text of the proposed regulations * * * [page 25, this bulletin]. The temporary regulations reflect amendments to the Internal Revenue Code of 1954 with respect to quarterly payments of the railroad unemployment railroad tax made by section 231(b) of the Railroad Retirement Solvency Act of 1983 [Pub. L. 98–76, 1983–2 C.B. 375, 379], and provide guidance with respect to the time and manner of making those payments. (Amendments to the railroad unemployment repayment tax made by section 13301 of the Consolidated Omnibus Budget Reconciliation Act of 1985 do not affect the rules in this document.)

DATES: The regulations contained in this document are effective December 5, 1986 and apply to remuneration paid after June 30, 1986.

FOR FURTHER INFORMATION CONTACT: Gail H. Morse of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3297, not a toll-free call).

SUPPLEMENTARY INFORMATION

BACKGROUND

Railroad workers, unlike most other occupational groups within the United States, are not covered by the Federal Unemployment Tax Act (FUTA). Instead, such workers receive unemployment benefits under the Railroad Unemployment Insurance Act (RUIA), a separate program administered by the Railroad Retirement Board.

Railroad employers pay over to the Railroad Unemployment Insurance Trust Fund contributions on the wages of their employees ranging from .5 percent to 8 percent (the specific percentage for a calendar year depends upon the financial condition of the railroad unemployment insurance account on the preceding September 30). See 20 CFR Part 345, relating to employers' contributions and contribution reports under the Railroad Unemployment Insurance Act. Unlike the FUTA system, there are no individual employer experience ratings under RUIA. Rather, one experience rating is determined for the railroad industry as a whole and imposed on all employers.

When contributions are insufficient to pay railroad unemployment benefits, the program can borrow from the railroad retirement account and repay when the Railroad Unemployment Insurance Trust Fund has more cash than is needed to pay benefits. For 21 of the last 26 years the unemployment fund has had to borrow from the retirement system. In recent years such borrowing has increased and has been coupled with non-repayment of the borrowed funds. A crisis arose in the railroad industry with respect to the railroad retirement and unemployment compensation systems in 1982—by 1983 a shortfall in the retirement fund was expected due to the decline in rail employment relative to the number of retired railroad employees (resulting in an excess of benefit payments over contributions to the system) and increased borrowing by the unemployment system coupled with non-repayment of the borrowed funds. The expected shortfall caused Congress to act to insure the solvency of both the railroad retirement and the railroad unemployment accounts. The Railroad Retirement Solvency Act of 1983 (the Act) (Pub. L. 98–76, 97 Stat. 426) was intended to improve the financial status of both the railroad retirement and unemployment systems and to increase the likelihood that both systems would be able to meet their continuing benefit obligations.

In addition to provisions with respect to the retirement system and administration of the railroad unemployment system, the Act sought to provide for the repayment of funds borrowed by the railroad unemployment system which had not been repaid. Chapter 23A, added to the Internal Revenue Code of 1954 by section 231 of the Act, provides for the imposition of the railroad unemployment repayment tax. This tax is an excise tax on railroad employers (a term defined in the Act by reference to section 1 of the Railroad Unemployment Insurance Act) with respect to having individuals in their employ as well as a tax on the income of employee representatives. The tax is effective for remuneration paid after June 30, 1986, and, as amended by Section 13301 of the Consolidated Omnibus Budget Reconciliation Act of 1985 (Pub. L. 99–272, 100 Stat. 325), is equal to the applicable percentage of total rail wages for a particular taxable period. The applicable percentage, equal to the sum of the basic rate plus the surtax rate, will vary for each taxable period. The basic rate is applicable to taxable periods beginning after June 30, 1986, and before October 1, 1990. (This rate will terminate at an earlier date if loans made to the railroad unemployment fund before October 1, 1985, are repaid before October 1, 1990). The surtax rate is effective for any taxable period beginning after September 30, 1986, where, as of September 30 of the preceding taxable year, there is an outstanding balance of transfers (or unpaid interest thereon), made after September 30, 1985, to the railroad unemployment insurance account under section 10(d) of the Railroad Unemployment Insurance Act.

Section 6157 provides that the payment of the railroad unemployment repayment tax will be on a quarterly basis in such manner and at such time as regulations prescribed by the Secretary may provide.

The temporary regulations found in this document provide the time and manner of making quarterly payments of the railroad unemployment repayment tax.

EXPLANATION OF PROVISIONS

The temporary regulations reflect amendments to the Employment Tax Regulations under sections 6011, 6071, 6157, and 6302 of the Internal Revenue Code with respect to the requirement that there be quarterly payments of the railroad unemployment repayment tax.

Section 31.6011(a)–3AT(a) provides that rail employers shall make an annual return of the railroad unemployment repayment tax imposed by section 3321 on Form CT–1 (currently used for returns of railroad retirement tax). The Form CT–1 will thus provide for both the return of railroad retirement tax and the return of railroad unemployment repayment tax. The return is to be made for each taxable period (as defined in section 3322) in which the tax is imposed beginning with the period which commences on July 1, 1986. Section 31.6011(a)–3AT(b) provides that employee representatives (as generally defined in section 3323(d)) shall make a quarterly return of the railroad unemployment repayment tax on Form CT–2 (currently used for returns of railroad retirement tax). The Form CT–2 will thus provide for both the return of railroad retirement tax and the return of railroad unemployment repayment tax. The report is to be made for each calendar quarter of a taxable period in which the tax is imposed beginning with the period which commences on July 1, 1986.

Section 31.6071(a)–1T provides rules regarding the time for filing Forms CT–1 and CT–2. Section 31.6071(a)–1T(a) provides that Forms CT–1 and CT–2 are to be filed on or before the last day of the second calendar month following the period for which return is made (the same due date applicable to such returns filed in connection with railroad retirement taxes).

Section 31.6302(c)–2AT sets forth the rules governing the computation and payment by rail employers of the railroad unemployment repayment tax on a quarterly basis and provides for the deposit of the tax so computed with a Federal Reserve Bank or an authorized financial institution. The deposits are to be made by the last day of the first calendar month following the close of each of the first three calendar quarters of a taxable period.

However, no deposit is required with respect to any of the first three calendar quarters if the tax computed for the quarter plus unpaid amounts for prior quarters during the taxable period is $100 or less. No deposit of the railroad unemployment repayment tax is required for the last calendar quarter in any taxable period unless the amount of such tax reportable on Form CT–1 exceeds by more than $100 the sum of the amounts deposited in the preceding three calendar quarters. In cases where the reportable railroad unemployment retirement tax exceeds by more than $100 the sum of the amounts deposited in the preceding three calendar quarters, §31.6302(c)–2AT(b)(3) requires that the balance due be deposited with a Federal Reserve bank or with an authorized financial institution by the last day of the first calendar month following the taxable period for which the return is being filed. Where the railroad unemployment repayment tax reportable on Form CT–1 does not exceed by more than $100 the sum of the amounts deposited in the preceding three calendar quarters, that amount is to be remitted with Form CT–1. The preprinted Federal Tax Deposit coupon (Form 8109) is the form prescribed for making the deposits of the railroad unemployment repayment tax. Section 31.6302(c)–2AT(b)(1)(ii) requires that certain rail employers make their quarterly deposits of the railroad unemployment repayment tax by wire transfer to the Treasury. The wire payments will be credited to the rail employers' CT–1 account in the same manner as railroad retirement wire transfers. The wire deposit of the railroad unemployment repayment tax may not be made in the same wire deposit as any other tax.

REGULATORY FLEXIBILITY ACT; EXECUTIVE ORDER 12291; PAPERWORK REDUCTION ACT OF 1980

No general notice of proposed rulemaking is required by 5 U.S.C. 553(b) for temporary regulations. Moreover, the Internal Revenue Service has concluded that the regulations herein will not have a significant impact on a substantial number of small entities. Accordingly, the Regulatory Flexibility Act does not apply and no Regulatory Flexibility Analysis is required for this rule. The Commissioner of Internal Revenue has determined that this temporary rule is not a major rule as defined in Executive order 12291 and that a Regulatory Impact Analysis is therefore not required. The reporting requirements added by this document had been submitted to the Office of Management and Budget (OMB) in accordance with the requirements of the Paperwork Reduction Act of 1980. The reporting requirements have been approved by OMB.

DRAFTING INFORMATION

The principal author of these temporary regulations is Gail H. Morse of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and the Treasury Department participated in developing the regulations both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations.

Accordingly, 26 CFR Part 31 and Part 602 are amended as follows:

PART 31 EMPLOYMENT TAXES AND COLLECTION OF INCOME TAX AT SOURCE

Paragraph 1. The authority for Part 31 is amended by adding the following citation:

Authority: 26 U.S.C. 7805. * * * Section 31.6011(a)–3AT is also issued under the authority of 26 U.S.C. 6011; §31.6071(a)–1T is also issued under the authority of 26 U.S.C. 6071; §31.6157–1T is also issued under 26 U.S.C. 6157(d); and §31.6302(c)–2AT is also issued under 26 U.S.C. 6302.

Par. 2. A new section 31.6011(a)–3AT is added immediately following existing §31.6011(a)–3 to read as follows:

§31.6011(a)–3AT Returns of the railroad unemployment repayment tax (temporary).

(a) *Requirement*—(1) *Employers.* Every rail employer (as defined in section 3323(a) and section 1 of the Railroad Unemployment Insurance Act) shall make a return of the tax imposed by section 3321(a) (relating to the railroad unemployment repayment tax) for each taxable period (as defined in section 3322(a)) with respect to the total rail wages (as defined in section 3323(b)) paid by the rail employer during the taxable period. Form CT–1 is the form prescribed for use in making the return. One original and a duplicate of each return on Form CT–1 shall be filed with the director of the service center as designated in the instructions to Form CT–1. Rail wages taxable under section 3321(a) shall be reported in the return required under this section for the return period in which they are actually paid unless they were constructively paid in a prior return period, in which case such wages shall be reported only in the return for such prior period.

(2) *Employee representatives.* Each employee representative (as defined in section 3323(d)(2) and section 1 of the Railroad Unemployment Insurance Act) shall make a return of the tax imposed by section 3321(b) on the rail wages paid to him (as determined under section 3321(b)(2)) during each calendar quarter within a taxable period. Form CT–2 is the form prescribed for use in making the return. One original and a duplicate of each return on Form CT–2 shall be filed with the director of the service center as designated in the instructions to Form CT–2. Rail wages taxable under section 3321(b) shall be reported in the return required under this section for the return period in which they are actually paid unless they were constructively paid in a prior return period, in which case such wages shall be reported only in the return for such prior period.

(b) *Time and place for filing returns.* For provisions relating to the time and place for filing returns, see §31.6071(a)–1T and §31.6091–1, respectively.

Par. 3. A new §31.6071(a)–1T is added immediately following existing §31.6071(a)–1 to read as follows:

§31.6071(a)–1T Time for filing returns with respect to the railroad unemployment repayment tax (temporary).

(a) *In general.* Each return of the taxes imposed under section 3321(a) and (b) required to be made under §31.6011(a)–3AT shall be filed on or before the last day of the second calendar month following the period for which it is made.

(b) *Last day for filing.* For provisions relating to the time for filing a return when the prescribed due date falls on Saturday, Sunday, or a legal holiday, see the provisions of §301.7503–1 of this chapter (Regulations on Procedure and Administration).

(c) *Late filing.* For additions to the tax in the case of failure to file a return within the prescribed time, see the provisions of §301.6651–1 of this chapter (Regulations on Procedure and Administration).

Par. 4. Section 31.6157–1T is added immediately following existing §31.6157–1 to read as follows:

§31.6157–1T Cross reference (temporary).

For provisions relating to the time and manner of depositing the railroad unemployment repayment tax imposed by section 3321(a), see §31.6302(c)–2AT.

Par. 5. A new §31.6302(c)–2AT is added immediately following existing §31.6302(c)–2 to read as follows:

§31.6302(c)–2AT Use of Government depositaries in connection with the railroad unemployment repayment tax (temporary).

(a) *Effective date.* The provisions of this section apply with respect to the tax imposed by section 3321(a) on rail employers (as defined in section 3323(a)) on wages paid on or after July 1, 1986, during a taxable period.

(b) *Requirement*—(1) *Rail employers*—(i) *In general.* Except as provided in this section, every rail employer who is required by section 6157(d) to compute the tax imposed by section 3321(a) on a quarterly basis shall deposit the amount of the tax so computed with respect to a calendar quarter (other than the fourth quarter of a calendar year) with a Federal Reserve bank or with an authorized financial institution on or before the last day of the first calendar month following the close of the calendar quarter.

(ii) *Special rule for certain rail employers.* If, for the calendar year prior to the calendar year immediately preceding the current calendar year, the aggregate amount of taxes imposed under sections 3202 and 3221 of the Code (relating to the railroad retirement tax) with respect to an employer equaled or exceeded $1,000,000, such employer shall (except as provided below) deposit his undeposited railroad unemployment repayment tax imposed by section 3321(a) with respect to the current calendar year at the time such tax would otherwise be required to be deposited under this section in the manner set forth in Revenue Procedure 83–90, 1983–2 C.B. 615 (relating to transfers by wire to the Treasury). The funds transfer message described in Revenue Procedure 83–90 (with respect to the railroad retirement tax) shall be completed in the same manner as is prescribed in that Revenue Procedure, except that the amount required by items 12(f) shall be the amount of the railroad unemployment repayment tax (to be labeled as such by the rail employer). Item 12(g) is to be disregarded with respect to the use of the Revenue Procedure for deposits of the railroad unemployment repayment tax. A wire transfer required to be made by a rail employer with respect to the railroad unemployment repayment tax shall be made separately from any wire transfer required to be made with respect to any other tax.

(2) *Special rule where accumulated amount does not exceed $100.* The provisions of paragraph (b)(1) of this section shall not apply with respect to any calendar quarter if the amount of tax imposed by section 3321(a) for such calendar quarter as computed under section 6157, plus unpaid amounts for prior calendar quarters within the taxable period, does not exceed $100.

(3) *Requirement for deposit in lieu of payment with return.* If the amount of the tax reportable on a return of tax on Form CT–1 for a taxable period (as defined in section 3322(a)) exceeds by more than $100 the sum of the amounts deposited pursuant to paragraph (b)(1) of this section for such taxable period, the rail employer shall, on or before the last day of the first calendar month following the period, deposit the balance of the tax due with a Federal Reserve bank or with an authorized financial institution.

(4) *Special rule for third calendar quarter of 1986.* Notwithstanding paragraph (b)(1)(i) of this section, every rail employer required by section 6157(d) to compute the tax imposed by section 3321(a) for the third calendar quarter of 1986 shall deposit the tax so computed on or before December 15, 1986, in the manner provided by this section.

(c) *Depositary forms.* The provisions of paragraphs (b) and (c) of §31.6302(c)–2, relating to depositary forms, are incorporated in this §31.6302(c)–2A by reference.

PART 602 OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 6. The authority for Part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 7. Section 602.101(c) is amended by inserting in the appropriate places in the table: "§31.6011(a)–3AT . . . 1545–0955, "§31.6071(a)–1T . . . 1545–0955 "§31.6157–1T . . . 1545–0955 and "§31.6302(c)–2AT . . .1545–0955."

* * * * *

There is a need for immediate guidance with respect to the provisions contained in this Treasury decision. For this reason, it is found impracticable to issue it with notice and public procedure under subsection (b) of section 553 of title 5 of the United States Code or subject to the effective date limitation of subsection (d) of that section.

P.E. COATES,
Acting Commissioner of Internal Revenue.

Approved October 28, 1986.

J. ROGER MENTZ,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on October 31, 1986, 1:28 p.m., and published in the issue of the Federal Register for November 5, 1986, 51 F.R. 40167).

Section 6401.—Amounts Treated as Overpayments

26 CFR 301.6401–1: Amounts treated as overpayments.

Ct. D. 2036

SUPREME COURT OF THE UNITED STATES

No. 85–558

Robert E. O'Connor, et ux., v. United States

On Writs of Certiorari to the United States Court of Appeals for the Federal Circuit

[November 4, 1986]

JUSTICE SCALIA delivered the opinion of the Court.

Petitioners, United States citizen employees of the Panama Canal Commission and their spouses, seek refunds of income taxes collected on salaries paid by the Commission between 1979 and 1981. We granted certiorari to resolve conflicting appellate interpretations of an international agreement. 474 U.S.—(1986).

From 1904 to 1979, the United States exercised sovereignty over the Panama Canal and the surrounding 10-mile-wide Panama Canal Zone under the Isthmian Canal Convention, 33 Stat. 2234. On September 7, 1977, the United States and Panama signed the Panama Canal Treaty, T.I.A.S. No. 10030, which was ratified by the Senate on April 17, 1978, and took effect on October 1, 1979. The Treaty transferred to Panama sovereignty over the Canal and Zone, but gave the United States the right to operate the Canal until December 31, 1999. The vehicle for United States administration of the Canal is the Panama Canal Commission, a United States Government agency supervised by a Board of nine members, four of whom are Panamanian nationals proposed by the Government of Panama. See 22 U.S.C. §§3611, 3612; Panama Canal Treaty, Art. III, §3, T.I.A.S. No. 10030 (hereinafter Treaty).

Article III of the Treaty, entitled "Canal Operation and Management," specifies that "the rights and legal status of United States Government agencies and employees operating in the Republic of Panama pursuant to this Article, shall be governed by the Agreement in Implementation of this Article. . . ." Treaty, Art. III, §9. The latter agreement, signed simultaneously with the Treaty, see Panama Canal Treaty: Implementation of Article III, Sept. 7, 1977, T.I.A.S. No. 10031 (hereinafter Agreement), contains the provision that gives rise to the present dispute. Article XV of the Agreement, entitled "Taxation," provides as follows:

> "1. By virtue of this Agreement, the Commission, its contractors and subcontractors are exempt from payment in the Republic of Panama of all taxes, fees or other charges on their activities or property.
>
> "2. United States citizen employees and dependents shall be exempt from any taxes, fees or other charges on income received as a result of their work for the Commission. Similarly, they shall be exempt from payment of taxes, fees or other charges on income derived from sources outside the Republic of Panama.
>
> "3. United States citizen employees and dependents shall be exempt from taxes, fees or other charges on gifts or inheritance or on personal property, the presence of which within the territory of the Republic of Panama is due solely to the stay therein of such persons on account of their or their sponsor's work with the Commission.
>
> "4. The Coordinating Committee may establish such regulations as may be appropriate for the implementation of this Article."

The petitioners contend that §2 of this Article constitutes an express exemption of their Commission salaries from both Panamanian and United States taxation. See 26 U.S.C. §894(a) ("Income of any kind, to the extent required by any treaty obligation of the United States, shall not be included in gross income and shall be exempt from taxation under this subtitle"). The Claims Court agreed, *Coplin* v. *United States*, 6 Cl. Ct. 115 (1984), but was reversed by a five-judge panel of the Federal Circuit. *Coplin* v. *United States*, 761 F.2d 688 (1985). In a substantively identical case, the Eleventh Circuit has ruled for the taxpayers. *Harris* v. *United States*, 768 F.2d 1240 (1985), cert. pending, No. 85-1011. The same issue is presented in numerous cases still pending in the lower courts.[1]

We agree with the Federal Circuit. The first section of Article XV, which confers upon the Commission and its contractors an exemption "from payment *in the Republic of Panama* of all taxes" (emphasis added), establishes the context for the discussion of tax exemptions in the entire Article— so that when §§2 and 3 state that "United States citizen employees . . . shall be exempt" from taxes they are understood to be dealing only with taxes payable in Panama. In that regard the structure of Article XV is similar to that of Article XVI, which in most of its sections speaks generally of import duties, but is understood to refer only to *Panamanian* import duties principally because §1 sets the stage in that fashion by referring to "the customs laws and regulations *of the Republic of Panama.*" Agreement, Art. XVI, §1 (emphasis added).

There is some purely textual evidence, albeit subtle, of the understanding that Article XV applies only to Panamanian taxes: In conferring an exemption from property taxes, §3 displays an assumption that only personal property within the Republic of Panama is at issue; otherwise, that significant qualification to the operation of §3 would more naturally have been set forth as an explicit limitation ("personal property *within the territory of the Republic of Panama,* whose presence there," etc.) rather than being referred to incidentally in the modifying clause ("personal property, whose presence within the territory of the Republic of Panama," etc.). And the assumption that only personal property within Panama is at issue in turn reflects the more fundamental assumption that only *Panamanian* personal property taxes are being addressed.

More persuasive than the textual evidence, and in our view overwhelmingly convincing, is the contextual case for limiting Article XV to Panamanian taxes. Unless one posits the ellipsis of failing to repeat, in each section, §1's limitation to taxes "in the Republic of Panama," the Article takes on a meaning that is utterly implausible and has no foundation in the negotiations leading to the Agreement. For if the first sentence of §2 refers to United States as well as Panamanian taxes, then the second sentence of §2, and the totality of §3, must do so as well—with the consequence that United States citizen employees and their dependents would be exempt not only from United States income tax on their earnings from the Commission, but also from United States income tax on all income from sources outside Panama (*e.g.*, United States bank accounts), and from all United States gift and inheritance taxes. While, as the petitioners assert, there might have been some reason why Panama would insist that its inability to tax United States citizen Commission employees upon their earnings in Panama be matched by a detraction from the United States' sovereign power to tax those same earnings, there is no conceivable reason why this hypothetical "your-sovereignty-for-mine" negotiating strategy would escalate into a demand that the United States yield more sovereign prerogatives than it was asking Panama to forgo—and no imaginable reason why the United States would accept such an escalation, producing tax immunity of unprecedented scope.

The petitioners' attempts to explain why these broader tax consequences need not follow from their interpretation are unpersuasive. With regard to the second sentence of §2, they argue that the opening word "similarly" should be read to incorporate into that sentence the first sentence's restriction to "income received as a result of . . . work for the Commission." On this understanding, the second sentence provides a "simila[r]" tax exemption for Commission-related income "derived from sources outside the Republic of Panama," but allows both countries to tax non-Commission income. In addition to being an unnatural reading of "similarly" in this context, this interpretation is flatly inconsistent with the language of §2. Contrary to the petitioners' tacit assumption, the first sentence contains nothing limiting the scope of its exemption to income received as a result of work for the Commission *in Panama.* A person receiving a Commission salary for work performed in, for example, Bogota would seem plainly to qualify for exemption under this provision—rendering the second sentence, on the petitioners' understanding, superfluous. With regard to §3, the petitioners assert that its reference to taxation of property "within the territory of the Republic of Panama" is sufficient to demonstrate that only Panamanian taxation is intended to be covered. But as a reading of the provision will readily demonstrate, that reference applies only to personal property taxes; there is no comparable qualification on §3's exemption from taxes "on gifts or inheritance." That is limited, if at all, only by the implication that Panamanian taxes alone are at issue. In sum, we find the verbal distortions necessary to give plausible content, under the petitioners' theory, to the second sentence of §2 and §3, far less tolerable than the acknowledgment of ellipsis which forms the basis of the Government's interpretation.

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[1] After this case was argued, the President signed into law the Tax Reform Act of 1985, Pub. L. 99-514, —— Stat. ——. Section 1232(a) of that Act provides, in relevant part, that for "all taxable years whether beginning before, on, or after the date of the enactment of this Act (or in the case of any tax not imposed with respect to a taxable year, [for] taxable events after the date of enactment of this Act," no provision of the Treaty or Agreement "shall be construed as exempting (in whole or in part) any citizen or resident of the United States from any tax under the Internal Revenue Code of 1954 or 1986." Because we find that the Agreement, properly interpreted, provides for the same result, we do not rely upon the statute, and thus avoid confronting the constitutional questions posed by retroactive income taxation. See *United States* v. *Darusmont*, 449 U.S. 292, 296-301 (1981); *Welch* v. *Henry*, 305 U.S. 134, 146-151 (1938).

Not only is limitation of Article XV to Panamanian taxes in accord with the consistent application of the Agreement by the Executive Branch—a factor which alone is entitled to great weight, see *Sumitomo Shoji America, Inc.* v. *Avagliano,* 457 U.S. 176, 184–185 (1982)—but that application has gone unchallenged by Panama. It is undisputed that, pursuant to clear Executive Branch policy, the Panama Canal Commission consistently withheld United States income taxes from petitioners and others similarly situated, see Letter from John L. Haines, Jr., Deputy General Counsel, Panama canal Commission, to David Slacter, United States Department of Justice, Dec. 20, 1982, pp. 2–3, 1 App. in Nos. 85–504, 85–505, 85–506, and 85–507 (CAFC), pp. 61–62, and that Panama, which had four of its own nationals on the Board of the Commission, did not object. The course of conduct of parties to an international agreement, like the course of conduct of parties to any contract, is evidence of its meaning. See *Trans World Airlines, Inc.* v. *Franklin Mint Corp.,* 466 U.S. 243, 259–260 (1984); *Pigeon River Improvement, Slide & Boom Co.* v. *Charles W. Cox, Ltd.,* 291 U.S. 138, 158–161 (1934). Cf. Uniform Commercial Code §2–208(1) (1978).[2]

The petitioners contrast §2 with the following provision of the simultaneously executed Agreement in Implementation of Article IV, relating to taxation of United States Armed Forces and associated civilian personnel:

> "(2) Members of the Forces or the civilian component, and dependents, shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the United States Forces or for any of the service facilities referred to in Article XI or XVIII of this Agreement. Similarly, *as is provided by Panamanian law,* they shall be exempt from payment of taxes, fees, or other charges on income derived from sources outside the Republic of Panama." Panama Canal Treaty: Implementation of Article IV, Sept. 7, 1977, Art. XVI, §2, T. I. A. S. No. 10032 (emphasis added).

The petitioners contend that the variation in the phraseology of the two provisions demonstrates that the taxation provisions of the Article III Agreement were meant to be bilateral. We think not. It would be another matter if the variation at issue were alteration of the phrase "Panamanian taxes" in one agreement to merely "taxes" in the other; there would have been no reason to object to the former formulation *except* the belief that more than Panamanian taxes were covered. Several plausible reasons, however, would justify objection to the phrase "as is provided by Panamanian law." The most obvious is the concern that the phrase would be interpreted to leave future scope of the tax exemption within Panama's unilateral control, through the amendment of its domestic law. (To be sure, that reason would seemingly call for deletion of the phrase from both agreements rather than merely the Agreement in Implementation of Article III—but perhaps it was only with respect to the latter agreement, in which Panama had steadfastly opposed the whole concept of tax exemption, that unilateral Panamanian action was feared.) The surmise that the reason for deletion of the phrase in the Article III Agreement was its implication that only Panamanian taxes were covered would perhaps be reasonable if it were clear that the deletion was prompted by Panama. In fact, however, the deletion was made in the course of the American side's own internal drafting, before any text had even been presented to the Panamanians. (The phrase "as is provided by Panamanian law" was included in the June 26, 1977, United States draft of §2 of Art. XV, 1 App. in Nos. 85–504, 85–505, 85–506, and 85–507 (CAFC), p. 74, but was dropped from subsequent United States drafts, *id.,* at 77, 81.) The petitioners assert that this occurred as a consequence of the American side's knowledge that Panama would not accept a unilateral tax exemption provision and would accept a bilateral one—but they point to no Panamanian negotiating proposal supporting that speculation, which seems to us not inordinately credible on its face.

We find the petitioners' attempted reliance upon other elements of the negotiating history unavailing. While the Claims Court may have been correct that the negotiating history does not favor the Government's position sufficiently to overcome what that court regarded as a plain textual meaning in favor of the taxpayers, it certainly does not favor the taxpayers' position sufficiently to affect our view of the text. It contains, we may note, only a single (unhelpful) reference to United States income taxation—a silence that can perhaps be reconciled with the petitioners' position, but can hardly be said affirmatively to support it.

Finally, we find no significance in the fact, urged so strongly by the petitioners, that Article XV is entitled "Taxation" rather than "Panamanian Taxation." Of the twenty-one Articles of the Agreement, only two—Articles V and IX—are limited by title to Panamanian subject matter, though it is plain that most are so limited in their application. See, *e.g.,* Article VII ("Water Rights"); Article XII ("Entry and Departure"); Article XVI ("Import Duties").

The judgment of the court of appeals is

Affirmed.

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[2] The Government has contended, here and before the Court of Appeals, that the answer to the current question is illumined, if not conclusively determined, by a February 22, 1985, diplomatic note from the Government of Panama, indicating that it shares the United States' view that Article XV pertains only to Panamanian taxation. The petitioners assert that mutual agreement between the contracting parties on interpretation cannot be dispositive of third-party rights, and that the note is in any event inadmissible on various grounds. Since we would sustain the Government's position without reference to the note, we need not resolve these disputes.

Section 7872.—Treatment of Loans with Below-market Interest Rates

Federal short-term, mid-term, and long-term rates are set forth for the month of December 1986. See Rev. Rul. 86-143, page 5.

Part II. Treaties and Tax Legislation

Subpart A.—Tax Conventions

United States-United Kingdom Income Tax Convention 1980–1 C.B. 394

United States-United Kingdom Income Tax Convention; Article 15(2)(a). The term "tax year concerned" refers to the tax year in which personal services are performed rather than to the tax year in which compensation for those services is received.

Rev. Rul. 86–145

ISSUE

Whether the term "tax year concerned" as used in Article 15(2)(a) of the United States-United Kingdom Income Tax Convention ("Convention"), which entered into force on April 25, 1980, 1980–1 C.B. 394, refers to the tax year in which personal services are performed or to the tax year in which compensation for those services is received.

FACTS

A, a United Kingdom resident, was present in the United States for more than 183 days in 1985. *A* performed personal services during that period for an employer who was not a resident of the United States and who had no permanent establishment or fixed base in the United States. With respect to 1985, *A* was a resident of the United Kingdom and was not deemed a resident of the United States under Article 4 of the Convention. *A* was present in the United States for 30 days in 1986 and during that period was paid for the services performed when present in the United States in 1985. In each of those years, *A*'s United States tax year was the calendar year.

LAW AND ANALYSIS

Article 15(1) of the Convention provides the general rule that remuneration in respect of employment is taxable in the Contracting State where the employment is performed.

Article 15(2) of the Convention provides that, notwithstanding Article 15(1), remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if:

> (a) the recipient is present in that other State for a period not exceeding in the aggregate 183 days *in the tax year concerned;* and
>
> (b) the remuneration is paid by, or on behalf of, an employer who is not a resident of that other State; and
>
> (c) the remuneration is not borne as such by a permanent establishment or a fixed base which the employer has in that other State.

[Emphasis added.]

The Treasury Department Technical Explanation of the Convention, 1980–1 C.B. 455, 467, states that Article 15 of the Convention is based on Article 15 (Dependent Personal Services) of the 1977 OECD Model Convention (Model Convention). Article 15(1) of the Model Convention has a rule and exception similar to Article 15(2)(a) of the Convention. The focus of this exception is "employment of short duration abroad. . . . The exemption is limited to the 183-day period." Model Convention, Annex II, Commentaries on the Articles of the Model Convention, 131. Thus, the use of the term "in the tax year concerned" as part of the limitation on that exemption refers to the tax year in which the employment services being compensated are performed, and not to the tax year in which the compensation for the services is received.

Since *A* was present in the United States for more than 183 days in 1985, the exemption from United States taxation under Article 15(2)(a) of the Convention is unavailable to *A* with respect to the services *A* rendered during that year. The exemption is unavailable with respect to those services notwithstanding that *A* was paid for them in 1986 when *A* was present in the United States for less than 183 days.

HOLDING

For purposes of the 183-day limitation to the exemption under Article 15(2)(a) of the Convention, the term "tax year concerned" refers to the tax year in which the services being compensated are performed in a Contracting State by a resident of the other Contracting State and not to the tax year in which compensation for services is received.

Part III. Administrative, Procedural, and Miscellaneous

26 CFR 601.201: Rulings and determination letters.

Rev. Proc. 86–44

SECTION 1. BACKGROUND

Rev. Proc. 86–3, 1986–1 C.B. 416, lists areas in which rulings or determination letters will not be issued by the Internal Revenue Service. Section 5 of Rev. Proc. 86–3 is entitled Areas Under Extensive Study in Which Rulings or Determination Letters Will Not be Issued Until the Service Resolves the Issues Through Publication of a Revenue Ruling, Revenue Procedure, Regulations or Otherwise.

Section 5.19 provides: Section 368.—Definitions Relating to Corporate Reorganizations.—Whether a transaction qualifies under either section 368(a)(1)(B) or section 351(a) of the Code by reason of Rev. Rul. 67–448, 1967–2 C.B. 144, when the same transaction is structured under section 368(a)(1)(A) and 368(a)(2)(E) (as a reverse triangular merger) and fails to qualify for an advance ruling under those sections merely because (i), the "substantially all" requirement set forth in section 3.01 of Rev. Proc. 77–37, 1977–2 C.B. 568, is not met, or (ii), the "control" requirement of section 3689(a)(2)(E)(ii) is not met where the step transaction doctrine may be applied to treat a prior redemption of stock as part of the plan of reorganization.

SEC. 2. PROCEDURE

.01 Rev. Proc. 86–3 is amended by deleting clause (ii) from subsection .19 of section 5. The remainder of subsection .19 of section 5 is to remain, except that the designation "(i)" is deleted.

.02 The amended section 5.19 reads as follows:

Section 368.—Definitions Relating to Corporate Reorganizations.—Whether a transaction qualifies under either section 368(a)(1)(B) or section 351(a) of the Code by reason of Rev. Rul. 67–448, 1967–2 C.B. 144, when the same transaction is structured under sections 368(a)(1)(A) and 368(a)(2)(E) (as a reverse triangular merger) and fails to qualify for an advance ruling under those sections merely because the "substantially all" requirement" set forth in section 3.01 of Rev. Proc. 77–37, 1977–2 C.B. 568, is not met.

SEC. 3. EFFECTIVE DATE

This revenue procedure is effective for ruling requests on hand in the National Office on December 8, 1986, the date of publication of this ruling in the Internal Revenue Bulletin, and for all requests received thereafter.

SEC. 4. EFFECT ON OTHER REVENUE PROCEDURES

Rev. Proc. 86–3 is modified.

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26 CFR 601.602: Tax forms and instructions.

Rev. Proc. 86–45

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PART B. MAGNETIC TAPE SPECIFICATIONS

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PART A.—GENERAL

SECTION 1. PURPOSE

.01 The purpose of this revenue procedure is to provide the requirements and conditions for submitting Form 8027, Employer's Annual Information Return of Tip Income and Allocated Tips, on magnetic tape instead of filing paper returns. Form 8027 information is filed on paper and magnetic tape and sent annually to the Internal Revenue Service (IRS). The due date for submission of Form 8027 on magnetic tape to IRS is the last day of February.

.02 Section 301.6011–2 of the Regulations on Procedure and Administration requires that any person, including corporations, partnerships, individuals, estates and trusts, required to file 500 or more Forms 8027 in 1987 (for tax year 1986), must file such returns on magnetic media. For Forms 8027 filed in 1988 (for tax year 1987) and subsequent years, the requirement will drop to 250 or more returns (original *or* corrected). Please note that this requirement applies to both original *and* corrected returns. If you are required to file Forms 8027 on magnetic media and fail to do so, and you have not received a waiver from these filing requirements, you may be subject to a penalty of $50 per document for each document not submitted on magnetic tape, with a maximum penalty of $50,000.

.03 This procedure supersedes the following revenue procedure: Rev. Proc. 84–69, Publication 1239 (10–84), Requirements and Conditions for Submitting Form 8027, Employer's Annual Information Return of Tip Income and Allocated Tips, on Magnetic Tape.

SEC. 2. BACKGROUND—PRIOR YEAR CHANGES (TAX YEAR 1985)

.01 The following changes were made to Part B, Section 2:

(a) Record length is 372 tape positions.

(b) Block length is 10,044 tape positions.

.02 The following changes were made to Part B, Section 3:

(a) Header labels UHL1 and bLAB were added as standard labels that IRS programs can process.

(b) Trailer labels EOV1 and EOV2 were added as standard labels that IRS programs can process.

.03 The following changes were made to the record layout of the 8027 Magnetic Tape Record:

(a) The 15-position field, "Establishment Identification Number" was dropped.

(b) The 1-position field, "Establishment Type" was added.

(c) The 5-position field, "Establishment Serial Number" was added.

(d) The fields, "Establishment City" and "Employer City" no longer allow the use of hyphens as valid characters.

(e) Due to the fact that money amounts are no longer reported separately for the first quarter and last three quarters of the year, the following fields were consolidated for annual reporting:

(1) Charged Receipts.
(2) Charged Tips.
(3) Service Charges Less than 10 Percent.
(4) Indirect Tips.
(5) Direct Tips.
(6) Total Tips.
(7) Gross Receipts.

(f) The special character fields, "BLANK," "HYPHEN," "SLASH," and "AMPERSAND" were dropped.

(g) The 1-position field, "Amended 8027 Indicator" was added.

SEC. 3. NATURE OF CHANGES—CURRENT YEAR (TAX YEAR 1986)

.01 Numerous editorial changes have been made to the publication. Information concerning extensions and waivers has been added as well as applications for magnetic media. There have been no changes to the magnetic tape program or format.

SEC. 4. APPLICATION FOR MAGNETIC MEDIA REPORTING

.01 For the purposes of this revenue procedure, the EMPLOYER is the organization supplying the information and the TRANSMITTER is the organization preparing the magnetic media file. The employer and transmitter may be the same organization. Employers or their transmitters are required to complete Form 4419, Application for Magnetic Media Reporting of Information Returns. Requests for copies of this form or for additional information on magnetic media reporting should be addressed to the attention of the Magnetic Media Specialist at the National Computer Center. (See Part A, Sec. 12 of this revenue procedure.)

.02 Applications should be filed with the National Computer Center 90 days before the due date of the return. IRS will act on an application and notify the applicant, in writing, of authorization to file. A five-character Transmitter Control Code (TCC) will be assigned and included in an acknowledgement letter within 30 days of receipt of the application. Magnetic tape returns may not be filed with IRS until the application has been approved. Include your TCC in any correspondence with the Magnetic Media Specialist.

.03 Once authorization to file on magnetic tape has been granted to an employer or transmitter, it will remain in effect in succeeding years provided that all of the requirements of this revenue procedure are met and there are no equipment changes by the filer. Contact the Magnetic Media Specialist at the National Computer Center if you have questions concerning your application.

.04 IRS will assist new filers with their initial magnetic tape submission by encouraging the submission of test files for review in advance of the filing season. Approved employers or transmitters who wish to submit a test file should contact the Magnetic Media Specialist at the National Computer Center. The address is listed in Part A, Sec. 12 of this revenue procedure. IRS prefers that all "TEST" files be submitted between August 15 and December 15 of the year before the returns are due. Do not submit "TEST" tapes after January 1. If you are unable to submit your "TEST" file by the end of December, send a sample hardcopy printout or tape dump to the National Computer Center. Clearly mark the hardcopy printout or tape dump as "TEST DATA" and include identification information such as name, address, and telephone number of someone familiar with the "TEST" print or tape dump who may be contacted to discuss its acceptability.

.05 Only employers or transmitters using equipment compatible with IRS' equipment will have their applications approved. Compatible tape characteristics are shown in Part B, Sec. 1.

.06 If your magnetic tape files have been prepared for you in the past by a service agency and you now have computer equipment compatible with that of IRS and wish to prepare your own files, you must request your own five-character TCC by filing an application, Form 4419, as described above.

.07 If you as an individual or organization are an approved filer on magnetic tape and you change your name or the name of your organization, please notify the National Computer Center's Magnetic Media Specialist so that your file may be updated to reflect the proper name.

SEC. 5. FILING OF MAGNETIC MEDIA REPORTS

.01 If you do not file your returns on time, you may be subject to a $50 per document failure to file penalty. If you file without following the instructions in this revenue procedure, you may also be subject to a $50 per document failure to file penalty.

.02 Packaging, shipping, and mailing instructions will be provided by IRS within 45 days of the granting of approval. A magnetic tape reporting package, which includes all necessary transmittals, labels, and shipping instructions, will be mailed out between October and December of each year to all approved filers.

.03 With the IRS' concurrence, employers can submit a portion of their returns on magnetic media and the remainder on paper Forms 8027, provided there is NO DUPLICATE FILING. A Form 8027–T, Transmittal of Employer's Annual Report of Allocated Tips, must accompany paper submissions and a Form 4804, Transmittal of Information Returns Reported on Magnetic Media, must accompany magnetic media submissions. Indicate on Form 4804, in the blank captioned "Number of Payee Records," the total number of *establishments* being reported in this shipment. This figure should match the total number of tape records in your file. If you report on paper Forms 8027, send them to:

Internal Revenue Service
Andover Service Center
Andover, MA 05501

The National Computer Center processes magnetic media *only*. Do *not* send paper Forms 8027 to the National Computer Center.

.04 The affidavit which appears on Forms 8027–T and 4804 should be signed by the employer. A transmitter, service bureau, paying agent, or disbursing agent may sign the affidavit on behalf of the employer (or other person required to file) if the conditions in Items 1, 2(i) or 2(ii), and 3 below are met.

(1) It has the authority to sign the form under an agency agreement (oral, written, or implied) that is valid under state law.

(2)(i) It has the responsibility (oral, written, or implied) conferred on it by the employer (or other person required to file), to request the TINS of recipients (or others for whom information is being reported).

(ii) If the return of more than one employer is included in a single magnetic media submission, covered by a single Form 4804, each employer (or other person required to file) has attested by affidavit to the transmitter, service bureau, paying agent, or disbursing agent that the employer (or other person required to file) has complied with the law in attempting to secure correct TINS.

(3) It signs the form and adds the caption "For: (Name of employer (or other person required to file))."

.05 Although a duly authorized agent signs the affidavit, the employer is held responsible for the accuracy of the Form 8027 and will be liable for penalties for failure to comply with filing requirements.

.06 If a portion of the returns are submitted on paper documents, include a statement on the Form 8027–T that the remaining returns are being filed on magnetic media. Please note that Form 8027–T normally applies to the filing of information returns on paper; however, filers of magnetic media must review the Form 8027–T and file Form 8027–T if appropriate. DO NOT REPORT THE SAME INFORMATION ON PAPER FORMS THAT YOU REPORT ON MAGNETIC MEDIA. IF YOU REPORT PART OF YOUR RETURNS ON PAPER AND PART ON MAGNETIC MEDIA, BE SURE THAT DUPLICATE RETURNS, WITH THE SAME INFORMATION, ARE NOT INCLUDED ON BOTH.

.07 If an allocation of tips is based on a good faith agreement, a copy of the agreement must accompany the submission.

.08 If an allocation rate of less than 8% has been granted by the District Director, a copy of the determination letter must accompany the submission. Employers with more than one establishment can receive approval from one district in each Internal Revenue Service region where establishments are located (see Sec. 31.6053–3(h)(4) of the Employment Tax Regulations).

.09 If an amended return is being filed, it must be a complete return replacing the original return.

.10 Before submitting magnetic tape files, include the following:

(a) A signed Form 4804 or computer-generated substitute.

(b) A Form 4802 (if you transmit for multiple employers).

(c) A hardcopy printout or tape dump of the first five blocks and last two of your file.

(d) The magnetic tape with an external identification label as described in Part B, Sec. 1.

(e) On the outside of the shipping container, include a Form 4801 or a substitute for the form which reads "Deliver Unopened to Tape Library—Magnetic Media Reporting—Box __of__." If there is only one container, mark the outside as Box 1 of 1. For multiple containers, include the sequence (i.e., Box 1 of 33, 2 of 33, etc.).

(f) If you were granted an extension and are filing late, include a copy of the approved extension letter with the magnetic tape.

.11 IRS will not pay or accept "Collect on Delivery" or "Charge to IRS" shipments of reportable tax information that an individual or organization is legally required to submit. The current policy is to return magnetic materials or requested information at U.S. Government expense.

SEC. 6. FILING DATES

.01 Magnetic tape reporting to IRS for Form 8027 must be on a calendar year basis. Generally, the due date of either paper or tape Forms 8027 is the last day of February, unless such day falls on a Saturday, Sunday, or holiday. For tax year 1986, the due date for filing Forms 8027 will be March 2, 1987.

SEC. 7. EXTENSIONS OF TIME TO FILE

.01 If an employer or transmitter of Forms 8027 on magnetic tape is unable to submit their magnetic media file by the filing date, submit a letter requesting an extension of up to 30 days to file, as soon as you are aware that an extension will be necessary. In order to be considered, the request MUST be filed *before* the due date of the returns; otherwise, you will be subject to the late filing penalty. The letter should be sent to the attention of the Magnetic Media Reporting Program at the IRS National Computer Center. See Part A, Sec. 12 for the address. The request should include:

(a) The filer's name and address.

(b) The filer's Taxpayer Identification Number (SSN or EIN).

(c) The tax year for which the extension of time is requested (e.g., tax year 1986).

(d) The name and telephone number of a person to contact who is familiar with the request.

(e) The type of returns and expected volume (e.g., 1000 Forms 8027).

(f) The five-character TCC assigned to the organization or individual requesting the extension (if a number has been assigned).

(g) The reason for the delay and date that you will be able to file.

(h) If you file for multiple employers, the request must include a list of all employers and their Taxpayer Identification Numbers (EIN or SSN).

An approved extension for magnetic tape filing does not provide an extension to file the paper Forms 8027 with the Andover Service Center. Requests for an extension to file paper Forms 8027 should be submitted to the Andover Service Center. (See Part A, Sec. 5.03 for address.)

.02 If an extension of time to file on magnetic tape is granted by the National Computer Center, a copy of the letter granting the extension MUST be attached to the transmittal Form 4804 or computer-generated substitute when the file is submitted. CAUTION: AN EXTENSION TO FILE IS NOT AN EXTENSION TO ISSUE INFORMATION RETURN COPY TO EMPLOYEE.

SEC. 8. WAIVERS

.01 Any individual or organization required to file original or corrected Forms 8027 on magnetic tape may request a waiver from the filing requirements by submitting Form 8508, Request for Waiver from Filing Information Returns on Magnetic Media, with the IRS National Computer Center if filing on magnetic tape would be an undue hardship. File the waiver request at least 90 days before the Forms 8027 are due to be filed with IRS. IF APPROVED, THE WAIVER WILL PROVIDE EXEMPTION FROM MAGNETIC TAPE FILING FOR ONE TAX YEAR ONLY. Filers may not apply for a waiver for more than one tax year at a time. Copies of Form 8508 may be obtained from the IRS National Computer Center. See Part A, Sec. 12 for the address.

.02 ALL OF THE INFORMATION REQUESTED ON FORM 8508 MUST BE PROVIDED AS REQUESTED; OTHERWISE, THE WAIVER REQUEST WILL BE RETURNED TO YOU DUE TO INSUFFICIENT INFORMATION.

.03 If you request a waiver from filing on magnetic tape and it is approved, do NOT send a copy of the approved waiver to the Andover Service Center with your paper returns. Keep the waiver for your records.

.04 Waivers are granted on a case-by-case basis and may be approved at the discretion of the Magnetic Media Specialist at the National Computer Center.

.05 If you are required to file your Forms 8027 on magnetic tape but fail to do so, and you do NOT have an approved waiver on record, you may be subject to a failure to file penalty.

.06 An approved waiver from filing Forms 8027 on magnetic tape does not provide exemption from filing; you MUST still file those returns on paper forms with the Andover Service Center.

SEC. 9. PROCESSING OF MAGNETIC MEDIA RETURNS

.01 The National Computer Center will process tax information from magnetic media files. All magnetic media files that are received timely by the National Computer Center will be returned to the filers by August 15 of the year in which submitted. After January 1, 1986, all magnetic media processing, including the Allocated Tips processing, was centralized at the National Computer Center. Due to the volume of input received and the cost to return special containers, special shipping containers should not be used for transmitting data to the National Computer Center since IRS cannot guarantee return of such containers.

.02 All files submitted must conform *totally* to this revenue procedures. Files will be returned to you for correction if they are unprocessable due to format or coding errors, or by the request of the filer. Files must be corrected and returned to the National Computer Center within 30 days of receipt by the filer. The corrected files will be returned to the filer by the National Computer Center within 6 months of receipt. *Please be sure that your format and coding comply with this revenue procedure.*

SEC. 10. EFFECT ON PAPER RETURNS

.01 If a portion of the returns is reported on magnetic media and the remainder is reported on paper forms, those returns not submitted on magnetic media must be filed on Form 8027 with the Andover Service Center. (See Part A, Sec. 5 for address.)

SEC. 11. CORRECTED RETURNS, SUBSTITUTE FORMS AND COMPUTER-GENERATED FORMS

.01 If returns must be corrected or amended, approved magnetic media filers should make every attempt to provide such corrections on tape. The filer must contact the IRS for format and shipping instructions. A Form 4804 must accompany the shipment and the blank space next to the box marked "CORRECTION" should be checked.

.02 If corrections are not submitted on tape, employers must submit them on official Forms 8027. Substitute forms that have been previously approved by IRS, or computer-generated forms that are exact facsimiles of the official form (except for minor page size or print style deviations), may be submitted without re-obtaining IRS approval before using the form. In all other cases, IRS approval must be obtained before a substitute or computer-generated form can be used. Publication 1167, "Substitute Printed, Computer-Prepared, Computer-Generated Tax Forms and Schedules," which contains specifications for substitute paper returns, is available from most IRS offices.

.03 Requests for approval of computer-generated or substitute forms should be sent to the following address with a copy of the proposed form:

Internal Revenue Service
Attn: Substitute Forms Program
Room 7033, D:R:R:I
1111 Constitution Ave., N.W.
Washington, DC 20224

.04 Employers/establishments may send amended or corrected Forms 8027 to IRS to be processed. The original and corrected paper Forms 8027 will be sent to:

Internal Revenue Service
Andover Service Center
Andover, MA 05501

Code the corrected paper returns with a capital alpha "G" at the top of Form 8027 above the title of the form.

SEC. 12. MAGNETIC MEDIA SPECIALIST CONTACT

Requests for additional copies of this revenue procedure or for additional information on magnetic media reporting of Forms 8027 should be addressed to the attention of the Magnetic Media Specialist at the following address:

Internal Revenue Service
National Computer Center
P.O. Box 1359
Martinsburg, WV 25401–1359
Telephone (304) 263-8700

SEC. 13. DEFINITIONS

Element	Description
EIN	A nine-digit Employer Identification Number which has been assigned by Internal Revenue Service to the reporting entity.
Employer	The organization supplying the information.
Establishment	A food or beverage operation where tipping of food or beverage employees is customary.
File	For the purpose of this procedure, a file consists of all magnetic media records submitted by an Employer or Transmitter.
Transmitter	Person or organization preparing magnetic media file(s). May be Employer or agent of Employer.

SEC. 14. EFFECT ON OTHER DOCUMENTS

.01 Rev. Proc. 84–69, Publication 1239, (10–84) is superseded.

SEC. 15. TO CONTACT THE IRS NATIONAL COMPUTER CENTER

.01 Effective January 1, 1986, the magnetic media processing for Forms 8027 was relocated at the IRS National Computer Center. Please direct all requests for IRS magnetic media related publications, information, forms, transmittals, undue hardship waivers, or extensions to the following addresses:

If by U.S. Postal Service, send to:
Magnetic Media Reporting
Internal Revenue Service
National Computer Center
P.O. Box 1359
Martinsburg, WV 25401–1359

If by land carrier, send to:
Magnetic Media Reporting
Internal Revenue Service
National Computer Center
Route 9 and Needy Road
Martinsburg, WV 25401

Hours of operation at the National Computer Center are 8:30 AM until 8:00 PM Eastern Time Zone. The telephone number is (304) 263-8700.

.02 Requests for paper returns, publications, or forms *NOT* related to magnetic media processing should be requested from your local IRS office or by calling the toll-free number in your area.

PART B.—MAGNETIC TAPE SPECIFICATIONS

SECTION 1. GENERAL

.01 The magnetic tape specifications contained in this part of the procedure define the required format and contents of the records to be included in the file. THESE SPECIFICATIONS MUST BE ADHERED TO UNLESS DEVIATIONS HAVE BEEN SPECIFICALLY GRANTED BY IRS IN WRITING.

.02 IRS will be able to process any compatible tape files. Compatible tape files must meet any one set of the following:

(a) 7-track BCD (Binary Coded Decimal) with:

(1) Either Even or Odd Parity and

(2) A density of 556 or 800 BPI.

(b) 9-track EBCDIC (Extended Binary Coded Decimal Interchange Code) with:

(1) Odd Parity and

(2) A density of 800, 1600, or 6250 BPI.

(3) If you use *Univac* Series 1100, you must submit an interchange tape.

(c) 9-track ASCII (American Standard Coded Information Interchange) with:

(1) Odd Parity and

(2) A density of 800, 1600, or 6250 BPI.

.03 All compatible tapes files must have the following characteristics:

(a) Type of Tape — ½ inch mylar base, oxide coated; computer grade magnetic tape on reels of up to 2400 feet (731.52m) within the following specifications:

(1) Tape thickness: 1.0 or 1.5 mils.

(2) Reel Diameter: 10.5 inch (26.67 cm), 8.5 inch (21.59 cm), or 7 inch (17.78 cm).

(b) Interrecord Gap

(1) .75 inch for 556 or 800 BPI density (7-track).

(2) .6 inch for 800 or 1600 BPI density (9-track).

(3) .3 inch for 6250 BPI density (9-track).

.04 IRS programs are capable of accommodating some minor deviations. Filers who can substantially conform to these specifications, but do require some minor deviations, MUST contact the Magnetic Media Specialist at the Internal Revenue Service, National Computer Center in Martinsburg, WV. *Under no circumstances may tapes deviating from the specifications in this revenue procedure be submitted without prior written approval from IRS.*

.05 An external identification label, Form 5064, must appear on each tape submitted for processing. The following information is needed:

(a) The transmitter's name.

(b) The five-character TCC.

(c) The two-character state code (e.g., NY).

(d) Tape density.

(e) Indicate whether tape is labeled or unlabeled.

(f) Track (e.g., 7 or 9).

(g) Recording code (e.g., EBCDIC, ASCII, or BCD).

(h) The tax year of the data (e.g., 1986).

(i) Document type (e.g., 8027).

(j) Number of payees (indicate total number of establishments being reported).

(k) A reel number assigned by the transmitter (if applicable).

(l) The sequence of each reel (e.g., 001 of 008).

This information will assist IRS in processing or locating a specific file. *IRS advises that special shipping containers not be used for transmitting data since it cannot be guaranteed that they will be returned.*

SEC. 2. RECORD LENGTH

.01 The tape record defined in this procedure may be blocked or unblocked, subject to the following:

(a) A FIXED RECORD OF 372 POSITIONS IS REQUIRED.

(b) All records except the Header and Trailer Labels may be blocked.

(c) If records are blocked, the block MUST be 10,044 tape positions.

(d) If the use of blocked records would result in a short block, *all remaining positions of the block MUST be filled with 9's. DO NOT PAD A BLOCK WITH BLANKS.*

SEC. 3. OPTIONS FOR FILING

For the purposes of this procedure the following conventions must be used.

Header Label:

1. Employers may use standard headers provided they begin with 1HDR, HDR1, VOL1, VOL2, UHL1, or bLAB.
2. Consists of a maximum of 80 positions.
3. Header and Trailer Labels are optional unless more than one reel is being submitted. If more than one reel is being submitted, Header and Trailer Labels are REQUIRED.

IRS PREFERS STANDARD OR ANSI LABELED TAPES. IF YOU SUBMIT AN UNLABELED TAPE, THIS *MUST* BE INDICATED ON THE EXTERNAL LABEL AND ON THE FORM 4804 OR COMPUTER-GENERATED SUBSTITUTE.

Trailer Label:

1. Standard trailer labels may be used provided that they begin with 1EOR, 1EOF, EOR1, EOF1, EOV1, or EOV2.
2. Consist of a maximum of 80 positions.
3. Header and Trailer Labels are optional unless more than one reel is being submitted. If more than one reel is being submitted, Header and Trailer Labels are REQUIRED.

Record Mark:

1. Special character used to separate blocked records on tape.
2. Can be written only at the end of a record or block.
3. For odd parity tapes, use BCD bit configuration 011010 ("A82").

Tape Mark:

1. Used to signify the physical end of the recording on tape.
2. For even parity, use BCD configuration 001111 ("8421").
3. May follow the header label and precede and/or follow the trailer label.

RECORD NAME: 8027 MAGNETIC TAPE RECORD

Tape Position	Field Title	Length	Description and Remarks
1	Establishment Type	1	REQUIRED. This digit identifies the kind of establishment. Enter the number which describes the type of establishment, as shown below: 1 for an establishment that serves evening meals only (with or without alcoholic beverages). 2 for an establishment that serves evening meals and other meals (with or without alcoholic beverages). 3 for an establishment that serves only meals other than evening meals (with or without alcoholic beverages). 4 for an establishment that serves food, if at all, only as an incidental part of the business of serving alcoholic beverages.

RECORD NAME: 8027 MAGNETIC TAPE RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
2–6	Establishment Serial Number	5	REQUIRED. These five digits are for identifying individual establishments of an employer reporting under the same EIN. The employer numbers the various establishments uniquely until each establishment the employer is required to file a retun for has a number. NUMERICS ONLY.
7–46	Establishment Name	40	REQUIRED. Enter the name of the establishment. Left justify and fill unused positions with blanks. ALLOWABLE CHARACTERS ARE ALPHAS, NUMERICS. BLANKS, HYPHENS, AMPERSANDS, AND SLASHES.
47–86	Establishment Street Address	40	REQUIRED. Enter the street address of the establishment. Left justify and blank fill. ALLOWABLE CHARACTERS ARE ALPHAS, NUMERICS, SLASHES, HYPHENS, AMPERSANDS, AND BLANKS.
87–111	Establishment City	25	REQUIRED. Enter the city of the establishment. Left justify and blank fill. ALLOWABLE CHARACTERS ARE ALPHAS AND BLANKS.
112–113	Establishment State	2	REQUIRED. Enter state code of the establishment; must be one of the following:

State	*Code*
Alabama	AL
Alaska	AK
Arizona	AZ
Arkansas	AR
California	CA
Colorado	CO
Connecticut	CT
Delaware	DE
District of Columbia	DC
Florida	FL
Georgia	GA
Hawaii	HI
Idaho	ID
Illinois	IL
Indiana	IN
Iowa	IA
Kansas	KS
Kentucky	KY
Louisiana	LA
Maine	ME
Maryland	MD
Massachusetts	MA
Michigan	MI
Minnesota	MN
Mississippi	MS
Missouri	MO
Montana	MT
Nebraska	NE
Nevada	NV
New Hampshire	NH
New Jersey	NJ
New Mexico	NM
New York	NY
North Carolina	NC
North Dakota	ND
Ohio	OH
Oklahoma	OK
Oregon	OR

RECORD NAME: 8027 MAGNETIC TAPE RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks	
			Pennsylvania	PA
			Rhode Island	RI
			South Carolina	SC
			South Dakota	SD
			Tennessee	TN
			Texas	TX
			Utah	UT
			Vermont	VT
			Virginia	VA
			Washington	WA
			West Virginia	WV
			Wisconsin	WI
			Wyoming	WY
114–122	Establishment ZIP Code	9	REQUIRED. Enter the ZIP Code of the establishment. If using a five-digit ZIP Code, left justify the five-digit ZIP Code and fill the remaining four positions with blanks. If using a nine-digit ZIP Code, enter the number. ALLOWABLE CHARACTERS ARE NINE NUMERICS or FIVE NUMERICS AND FOUR BLANKS.	
123–131	Employer Identification Number	9	REQUIRED. Enter the nine-digit number assigned to the employer by IRS. DO NOT ENTER HYPHENS, ALPHA CHARACTERS, ALL 9's, or ALL ZEROS.	
132–171	Employer Name	40	REQUIRED. Enter the name of the employer as it appears on your tax forms (e.g., Form 941). Any extraneous information must be deleted. Left justify and blank fill. ALLOWABLE CHARACTERS ARE ALPHAS, BLANKS, NUMERICS, AMPERSANDS, HYPHENS, AND SLASHES.	
172–211	Employer Street Address	40	REQUIRED. Enter street and address of employer. Left justify and blank fill. ALLOWABLE CHARACTERS ARE ALPHAS, NUMERICS, HYPHENS, AMPERSANDS, SLASHES AND BLANKS.	
212–236	Employer City	25	REQUIRED. Enter the city of the employer. Left justify and blank fill. ALLOWABLE CHARACTERS ARE ALPHAS AND BLANKS.	
237–238	Employer State	2	REQUIRED. Enter state code of employer. Must be one of the abbreviations shown above in the state abbreviation table for Establishment State (Tape Positions 112–113).	
239–247	Employer ZIP Code	9	REQUIRED. Enter ZIP Code of employer. If using a five-digit ZIP Code, left justify the five-digit ZIP Code and fill the remaining four positions with blanks. If using a nine-digit ZIP Code, enter the number. ALLOWABLE CHARACTERS ARE NINE NUMERICS or FIVE NUMERICS AND FOUR BLANKS.	
248–259	Charged Tips	12	REQUIRED. Enter the total amount of tips that are shown on charge receipts for the calendar year. Field is in dollars and cents. Right justify and zero fill. NUMERICS ONLY. DO NOT ENTER DECIMAL POINTS, DOLLAR SIGNS, OR COMMAS.	
260–271	Charged Receipts	12	REQUIRED. Enter the total sales for the calendar year other than carryout sales or sales with an added service charge of 10 percent or more, that are on charge receipts with a charged tip shown. This includes credit card charges, other credit arrangements, and charges to a hotel room unless the employer's normal accounting practice consistently excludes charges to a hotel room. Do not include any state or local taxes in the amount reported. Right justify and zero fill. Field is in dollars and cents. If no entry, zero fill. NUMERICS ONLY. DO NOT INCLUDE DOLLAR SIGNS, DECIMAL POINTS, OR COMMAS.	

RECORD NAME: 8027 MAGNETIC TAPE RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
272–283	Service Charge Less Than 10 Percent	12	REQUIRED. Enter the total amount of service charges less than 10 percent that have been added to customer's bills and have been distributed to your employees for the calendar year. In general, service charges added to the bill are not tips since the customer does not have a choice. These service charges are treated as wages and are included on Form W-2. For a more detailed explanation, see Rev. Rul. 69–28, 1969–1 C.B. 270. Right justify and zero fill. Field is in dollars and cents. If no entry, zero fill. NUMERICS ONLY. DO NOT ENTER DOLLAR SIGNS, DECIMAL POINTS, OR COMMAS.
284–295	Indirect Tips Reported	12	REQUIRED. Enter the total amount of tips reported by indirectly tipped employees (e.g., busboys, service bartenders, cooks) for the calendar year. Do not include tips received by employees in December of the prior tax year but not reported until January. Include tips received by employees in December of the tax year being reported, but not reported until January of the subsequent year. Right justify and zero fill. Field is in dollars and cents. If no entry, zero fill. NUMERICS ONLY. DO NOT ENTER DOLLAR SIGNS, DECIMAL POINTS, OR COMMAS.
296–307	Direct Tips Reported	12	REQUIRED. Enter the total amount of tips reported by directly tipped employees (e.g., waiters, waitresses, bartenders) for the calendar year. Do not include tips received by employees in December of the prior tax year but not reported until January. Include tips received by employees in December of the tax year being reported, but not reported until January of the subsequent year. Right justify and zero fill. Field is in dollars and cents. If no entry, zero fill. NUMERICS ONLY. DO NOT ENTER DOLLAR SIGNS, DECIMAL POINTS, OR COMMAS.
308–319	Total Tips Reported	12	REQUIRED. Enter the total amount of tips reported by all employees (both indirectly tipped and directly tipped) for the calendar year. Do not include tips received in December of the prior tax year but not reported until January. Include tips received in December of the tax year being reported, but not reported until January of the subsequent year. Right justify and zero fill. Field is in dollars and cents. If no entry, zero fill. NUMERICS ONLY. DO NOT ENTER DOLLAR SIGNS, DECIMAL POINTS, OR COMMAS.
320–331	Gross Receipts	12	REQUIRED. Enter the total gross receipts from the provision of food and/or beverages for this establishment for the calendar year. Do not include receipts for carryout sales or sales with an added service charge of 10 percent or more. Do not include in gross receipts charged tips shown on charged sales (tape positions 248–259) unless you have reduced the cash sales amount because you have paid cash to tipped employees for tips they earned that were charged. Do not include state or local taxes in gross receipts. If you do not charge separately for food or beverages along with other services (such as a package deal for food and lodging), make a good faith estimate of the gross receipts attributable to the food or beverages. This estimate must reflect the cost of providing the food or beverages plus a reasonable profit factor. Include the retail value of complimentary food or beverages served to customers if tipping for them is customary and they are provided in connection with an activity engaged in for profit whose receipts would not be included as gross receipts from the provision of food or beverages (e.g., complimentary drinks served to customers at a gambling casino). Right justify and zero fill. Field is in dollars and cents. If no entry, zero fill. NUMERICS ONLY. DO NOT ENTER DOLLAR SIGNS, DECIMAL POINTS, OR COMMAS.

RECORD NAME: 8027 MAGNETIC TAPE RECORD—Continued

Tape Position	Field Title	Length	Description and Remarks
332–343	Tip Percentage Rate Times Gross Receipts	12	REQUIRED. Enter the amount determined by multiplying Gross Receipts for the year (tape positions 320–331) by the Tip Percentage Rate (tape positions 344–347). Right justify and zero fill. For example, if the value of Gross Receipts is "000045678900" and Tip Percentage Rate is "0800", multiply $456,789.00 by .0800 to get $36,543.12 and enter "000003654312". If tips are allocated using other than the calendar year, enter zeros; this may occur if you allocated tips based on the time period for which wages were paid or allocated on a quarterly basis. Field is in dollars and cents. NUMERICS ONLY. DO NOT ENTER DOLLAR SIGNS, DECIMAL POINTS, OR COMMAS.
344–347	Tip Percentage Rate	4	REQUIRED. Enter 8 percent (0800) unless a lower rate has been granted by the District Director. The determination letter must accompany the magnetic media submission. NUMERICS ONLY. DO NOT ENTER DECIMAL POINT.
348–359	Allocated Tips	12	REQUIRED. If Tip Percentage Rate Times Gross Receipts (tape positions 332–343) is greater than Total Tips Reported (tape positions 308–319), then the difference becomes Allocated Tips. Otherwise, enter all zeros. Right justify and zero fill. If tips are allocated using other than the calendar year, enter the amount of allocated tips from your records. Field is in dollars and cents. NUMERICS ONLY. DO NOT ENTER DOLLAR SIGNS, DECIMAL POINTS, OR COMMAS.
360	Allocation Method	1	REQUIRED. Enter the allocation method used if Allocated Tips (tape positions 348–359) is greater than zero as follows: 1 for allocation based on hours worked. 2 for allocation based on gross receipts. 3 for allocation based on a good faith agreement. The good faith agreement must accompany the magnetic media submission. If Allocated Tips is equal to zero, enter 0 (zero).
361–364	Number of Directly Tipped Employees	4	REQUIRED. Enter the total number of directly tipped employees employed by the establishment for the calendar year. Right justify and zero fill. NUMERICS ONLY.
365–369	Transmitter Control Code (TCC)	5	REQUIRED. Enter the 5 digit Transmitter Control Code assigned by the IRS.
370	Amended 8027 Indicator	1	REQUIRED. Enter blank for original return. Enter "G" for amended return. An amended return must be a complete new return replacing the original return.
371–372	IRS USE	2	Blanks.

Social Security Contribution and Benefit Base

The Secretary of the Department of Health and Human Services has determined—

* * * * *

Contribution and Benefit Base

General. The contribution and benefit base is $43,800 for remuneration paid in 1987 and self-employment income earned in taxable years beginning in 1987.

The contribution and benefit base serves two purposes:

(1) It is the maximum annual amount of earnings on which Social Security taxes are paid, and

(2) It is the maximum annual amount used in determining a person's Social Security benefits.

Computation. Section 230(c) of the Act provides a table with the contribution and benefit base for each year 1978, 1979, 1980, and 1981. For years after 1981, section 230(b) of the Act contains a formula for determining the contribution and benefit base. Under the prescribed formula, the contribution and benefit base for 1987 shall be equal to the 1986 base of $42,000 multiplied by the ratio of: (1) the average amount, per employee, of total wages for the calendar year 1985 to (2) the average amount of those wages for the calendar year 1984. Section 230(b) further provides that if the amount so determined is not a multiple of $300, it shall be rounded to the nearest multiple of $300.

Average Wages. The average wage for calendar year 1984 was previously determined to be $16,135.07. The average wage for calendar year 1985 has been determined to be $16,822.51 as stated herein.

Amount. The ratio of the average wage for 1985, $16,822.51, compared to that for 1984, $16,135.07, is 1,0426053. Multiplying the 1986 contribution and benefit base of $42,000 by the ratio 1.0426053 produces the amount of $43,789.42 which must then be rounded to $43,800. Accordingly, the contribution and benefit base is determined to be $43,800 for 1987.

(Filed by the Office of the Federal Register on November 3, 1986, 11:34 a.m., and published in the issue of the Federal Register for November 5, 1986, 51 F.R. 40256)

Part IV. Items of General Interest

Notice of Proposed Rulemaking

LR-12-86

Time and manner of making quarterly payments of the railroad unemployment repayment tax

SUMMARY: The Internal Revenue Service is issuing temporary employment tax regulations relating to the time and manner of making quarterly payments of the railroad unemployment repayment tax. The text of the temporary regulations serves as the comment document for this notice of proposed rulemaking.

DATES:

PROPOSED EFFECTIVE DATE

The proposed amendments would be effective 30 days after publication in the FEDERAL REGISTER of the Treasury decision finalizing these regulations and would be applicable to remuneration paid after June 30, 1986.

DATES FOR COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Written comments and requests for a public hearing must be delivered or mailed by January 5, 1987.

ADDRESS: Send comments and requests for a public hearing to Commissioner of Internal Revenue, Attention CC:LR:T (LR-12-86) Washington, D.C. 20224.

FOR FURTHER INFORMATION CONTACT: Gail H. Morse of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Ave., N.W., Washington, D.C. 20224, Attention CC:LR:T (202-566-3297, not a toll-free call).

SUPPLEMENTARY INFORMATION: BACKGROUND

The temporary regulations * * * amend the Employment Tax Regulations (26 CFR Part 31) under sections 6011, 6071, 6157, and 6302 of the Internal Revenue Code.

For the text of the temporary regulations see T.D. 8105 * * * [Page 7, this Bulletin]. The preamble to the temporary regulations explains the addition to the regulations.

REGULATORY FLEXIBILITY ACT AND EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. The Internal Revenue Service has concluded that the regulations herein will not have a significant impact on a substantial number of small entities. Accordingly, these proposed regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

COMMENTS AND REQUESTS FOR A PUBLIC HEARING

Before adopting these proposed regulations, consideration will be given to any written comments and requests for a public hearing that are submitted (preferably eight copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the FEDERAL REGISTER. The collection of information requirements contained herein have been submitted to OMB for review under the Paperwork Reduction Act, and comments on them should be sent to the Office of Information and Regulatory Affairs of OMB, Attn: Desk Officer for the Internal Revenue Service, New Executive Office Building, Washington, D.C. 20503. The Internal Revenue Service requests persons submitting comments to OMB to also send copies of the comments to the Service.

DRAFTING INFORMATION

The principal author of these proposed regulations is Gail H. Morse of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations both on matters of substance and style.

P. E. COATES
Acting Commissioner
of Internal Revenue.

(Filed by the Office of the Federal Register on October 31, 1986, 1:29 p.m., and published in the issue of the Federal Register for November 5, 1986, 51 F.R. 40232)

Revised Bulletin Index-Digest System

Announcement 86-119

The basic Income Tax (Service One) volume of the Bulletin Index-Digest System has been revised and may be purchased from the Superintendent of Documents. The basic volumes for Estate and Gift Taxes (Service Two), Employment Taxes (Service Three), and Excise Taxes (Service Four) will be revised as of December 1986.

The Bulletin Index-Digest System provides a fast and easy way to research Revenue Rulings, Revenue Procedures, Public Laws, Treasury Decisions and other tax related items of general interest published in the Internal Revenue Bulletin or Cumulative Bulletin. It is a comprehensive and up-to-date research tool that requires no filing or other clerical maintenance and provides a researcher with more than 33 years (1953 to present) of Bulletin material.

Service One includes a basic volume that covers the period 1953-1985 and a cumulative supplement covering material published in subsequent Bulletins. Cumulative supplements to the basic volume are issued quarterly.

The major portion of the Service consists of digests of Revenue Rulings, Revenue Procedures, Supreme Court Decisions, and other items published in the Bulletin. Each digest is preceded by descriptive key words that pinpoint the issue and is followed by the applicable Code and regulations sections and a citation to the Bulletin where the full text of the item may be found.

An "Introduction" and "How to Use Your Bulletin Index-Digest System" at the beginning of the basic volume explain the various parts of the book and, by the use of examples, suggest steps to follow for rapid research. Additional features include various finding lists to facilitate research in the Bulletin. Each item in the finding list includes a citation to a numbered digest or to the Bulletin.

This System enhances the utility of the Cumulative Bulletins maintained in libraries and offices. One or more of the Services also make a handy desk reference for anyone who needs to refer frequently to materials published in Internal Revenue Bulletins.

The new basic volume with subsequent supplements may be ordered on a subscription basis from the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402. Information for ordering the Services, domestic and foreign subscription price lists, and an order blank are contained on the back page of this Bulletin.

New Tables for Withholding Income Tax from Qualified Total Distributions Paid in 1987

Announcement 86–120

The following tables are for withholding Federal income tax from total distributions paid in 1987 under a qualified pension, profit-sharing, or stock bonus plan described in Internal Revenue Code section 401(a) or a qualified annuity plan described in Code section 403(a).

These tables are included in the January 1987 revision of Publication 493, Alternative Tax Withholding Methods and Tables (Including Tables for Withholding from Qualified Total Distributions).

Withholding Rate Schedule for Qualified Total Distributions Paid in 1987

(If the qualified total distribution is less than $200, no withholding is required.)

If the amount of the Qualified Total Distribution is:	Then, the amount of income tax withheld shall be:
Not over $20,000	5% of the Qualified Total Distribution
Over $ 20,000 but not over $ 40,000	$ 1,000 plus 13½% of excess over $ 20,000
Over $ 40,000 but not over $135,000	$ 3,700 plus 16⅔% of excess over $ 40,000
Over $135,000 but not over $205,000	$19,280 plus 22½% of excess over $135,000
Over $205,000 but not over $280,000	$35,030 plus 27% of excess over $205,000
Over $280,000 but not over $330,000	$55,280 plus 32% of excess over $280,000
Over $330,000	$71,280 plus 37% of excess over $330,000

Optional Withholding Table for Qualified Total Distributions Paid in 1987

If the amount of the Qualified Total Distribution is:			If the amount of the Qualified Total Distribution is:			If the amount of the Qualified Total Distribution is:		
At least	But less than	Income tax withholding is:	At least	But less than	Income tax withholding is:	At least	But less than	Income tax withholding is:
$ 0	$ 200	$ 0	42,000	43,000	4,028	92,000	93,000	12,228
200	400	10	43,000	44,000	4,192	93,000	94,000	12,392
400	600	20	44,000	45,000	4,356	94,000	95,000	12,556
600	800	30	45,000	46,000	4,520	95,000	96,000	12,720
800	1,000	40	46,000	47,000	4,684	96,000	97,000	12,884
1,000	1,500	50	47,000	48,000	4,848	97,000	98,000	13,048
1,500	2,000	75	48,000	49,000	5,012	98,000	99,000	13,212
2,000	2,500	100	49,000	50,000	5,176	99,000	100,000	13,376
2,500	3,000	125	50,000	51,000	5,340	100,000	101,000	13,540
3,000	3,500	150	51,000	52,000	5,504	101,000	102,000	13,704
3,500	4,000	175	52,000	53,000	5,668	102,000	103,000	13,868
4,000	4,500	200	53,000	54,000	5,832	103,000	104,000	14,032
4,500	5,000	225	54,000	55,000	5,996	104,000	105,000	14,196
5,000	6,000	250	55,000	56,000	6,160	105,000	106,000	14,360
6,000	7,000	300	56,000	57,000	6,324	106,000	107,000	14,524
7,000	8,000	350	57,000	58,000	6,488	107,000	108,000	14,688
8,000	9,000	400	58,000	59,000	6,652	108,000	109,000	14,852
9,000	10,000	450	59,000	60,000	6,816	109,000	110,000	15,016
10,000	11,000	500	60,000	61,000	6,980	110,000	111,000	15,180
11,000	12,000	550	61,000	62,000	7,144	111,000	112,000	15,344
12,000	13,000	600	62,000	63,000	7,308	112,000	113,000	15,508
13,000	14,000	650	63,000	64,000	7,472	113,000	114,000	15,672
14,000	15,000	700	64,000	65,000	7,636	114,000	115,000	15,836
15,000	16,000	750	65,000	66,000	7,800	115,000	116,000	16,000
16,000	17,000	800	66,000	67,000	7,964	116,000	117,000	16,164
17,000	18,000	850	67,000	68,000	8,128	117,000	118,000	16,328
18,000	19,000	900	68,000	69,000	8,292	118,000	119,000	16,492
19,000	20,000	950	69,000	70,000	8,456	119,000	120,000	16,656
20,000	21,000	1,000	70,000	71,000	8,620	120,000	121,000	16,820
21,000	22,000	1,135	71,000	72,000	8,784	121,000	122,000	16,984
22,000	23,000	1,270	72,000	73,000	8,948	122,000	123,000	17,148
23,000	24,000	1,405	73,000	74,000	9,112	123,000	124,000	17,312
24,000	25,000	1,540	74,000	75,000	9,276	124,000	125,000	17,476
25,000	26,000	1,675	75,000	76,000	9,440	125,000	126,000	17,640
26,000	27,000	1,810	76,000	77,000	9,604	126,000	127,000	17,804
27,000	28,000	1,945	77,000	78,000	9,768	127,000	128,000	17,968
28,000	29,000	2,080	78,000	79,000	9,932	128,000	129,000	18,132
29,000	30,000	2,215	79,000	80,000	10,096	129,000	130,000	18,296
30,000	31,000	2,350	80,000	81,000	10,260	130,000	131,000	18,460
31,000	32,000	2,485	81,000	82,000	10,424	131,000	132,000	18,624
32,000	33,000	2,620	82,000	83,000	10,588	132,000	133,000	18,788
33,000	34,000	2,755	83,000	84,000	10,752	133,000	134,000	18,952
34,000	35,000	2,890	84,000	85,000	10,916	134,000	135,000	19,116
35,000	36,000	3,025	85,000	86,000	11,080	135,000	136,000	19,280
36,000	37,000	3,160	86,000	87,000	11,244	136,000	137,000	19,505
37,000	38,000	3,295	87,000	88,000	11,408	137,000	138,000	19,730
38,000	39,000	3,430	88,000	89,000	11,572	138,000	139,000	19,955
39,000	40,000	3,565	89,000	90,000	11,736	139,000	140,000	20,180
40,000	41,000	3,700	90,000	91,000	11,900	140,000	141,000	20,405
41,000	42,000	3,864	91,000	92,000	12,064	141,000	142,000	20,630

Optional Withholding Table for Qualified Total Distributions Paid in 1987 (Continued)

If the amount of the Qualified Total Distribution is:			If the amount of the Qualified Total Distribution is:			If the amount of the Qualified Total Distribution is:		
At least	But less than	Income tax withholding is:	At least	But less than	Income tax withholding is:	At least	But less than	Income tax withholding is:
142,000	143,000	20,855	207,000	208,000	35,570	272,000	273,000	53,120
143,000	144,000	21,080	208,000	209,000	35,840	273,000	274,000	53,390
144,000	145,000	21,305	209,000	210,000	36,110	274,000	275,000	53,660
145,000	146,000	21,530	210,000	211,000	36,380	275,000	276,000	53,930
146,000	147,000	21,755	211,000	212,000	36,650	276,000	277,000	54,200
147,000	148,000	21,980	212,000	213,000	36,920	277,000	278,000	54,470
148,000	149,000	22,205	213,000	214,000	37,190	278,000	279,000	54,740
149,000	150,000	22,430	214,000	215,000	37,460	279,000	280,000	55,010
150,000	151,000	22,655	215,000	216,000	37,730	280,000	281,000	55,280
151,000	152,000	22,880	216,000	217,000	38,000	281,000	282,000	55,600
152,000	153,000	23,105	217,000	218,000	38,270	282,000	283,000	55,920
153,000	154,000	23,330	218,000	219,000	38,540	283,000	284,000	56,240
154,000	155,000	23,555	219,000	220,000	38,810	284,000	285,000	56,560
155,000	156,000	23,780	220,000	221,000	39,080	285,000	286,000	56,880
156,000	157,000	24,005	221,000	222,000	39,350	286,000	287,000	57,200
157,000	158,000	24,230	222,000	223,000	39,620	287,000	288,000	57,520
158,000	159,000	24,455	223,000	224,000	39,890	288,000	289,000	57,840
159,000	160,000	24,680	224,000	225,000	40,160	289,000	290,000	58,160
160,000	161,000	24,905	225,000	226,000	40,430	290,000	291,000	58,480
161,000	162,000	25,130	226,000	227,000	40,700	291,000	292,000	58,800
162,000	163,000	25,355	227,000	228,000	40,970	292,000	293,000	59,120
163,000	164,000	25,580	228,000	229,000	41,240	293,000	294,000	59,440
164,000	165,000	25,805	229,000	230,000	41,510	294,000	295,000	59,760
165,000	166,000	26,030	230,000	231,000	41,780	295,000	296,000	60,080
166,000	167,000	26,255	231,000	232,000	42,050	296,000	297,000	60,400
167,000	168,000	26,480	232,000	233,000	42,320	297,000	298,000	60,720
168,000	169,000	26,705	233,000	234,000	42,590	298,000	299,000	61,040
169,000	170,000	26,930	234,000	235,000	42,860	299,000	300,000	61,360
170,000	171,000	27,155	235,000	236,000	43,130	300,000	301,000	61,680
171,000	172,000	27,380	236,000	237,000	43,400	301,000	302,000	62,000
172,000	173,000	27,605	237,000	238,000	43,670	302,000	303,000	62,320
173,000	174,000	27,830	238,000	239,000	43,940	303,000	304,000	62,640
174,000	175,000	28,055	239,000	240,000	44,210	304,000	305,000	62,960
175,000	176,000	28,280	240,000	241,000	44,480	305,000	306,000	63,280
176,000	177,000	28,505	241,000	242,000	44,750	306,000	307,000	63,600
177,000	178,000	28,730	242,000	243,000	45,020	307,000	308,000	63,920
178,000	179,000	28,955	243,000	244,000	45,290	308,000	309,000	64,240
179,000	180,000	29,180	244,000	245,000	45,560	309,000	310,000	64,560
180,000	181,000	29,405	245,000	246,000	45,830	310,000	311,000	64,880
181,000	182,000	29,630	246,000	247,000	46,100	311,000	312,000	65,200
182,000	183,000	29,855	247,000	248,000	46,370	312,000	313,000	65,520
183,000	184,000	30,080	248,000	249,000	46,640	313,000	314,000	65,840
184,000	185,000	30,305	249,000	250,000	46,910	314,000	315,000	66,160
185,000	186,000	30,530	250,000	251,000	47,180	315,000	316,000	66,480
186,000	187,000	30,755	251,000	252,000	47,450	316,000	317,000	66,800
187,000	188,000	30,980	252,000	253,000	47,720	317,000	318,000	67,120
188,000	189,000	31,205	253,000	254,000	47,990	318,000	319,000	67,440
189,000	190,000	31,430	254,000	255,000	48,260	319,000	320,000	67,760
190,000	191,000	31,655	255,000	256,000	48,530	320,000	321,000	68,080
191,000	192,000	31,880	256,000	257,000	48,800	321,000	322,000	68,400
192,000	193,000	32,105	257,000	258,000	49,070	322,000	323,000	68,720
193,000	194,000	32,330	258,000	259,000	49,340	323,000	324,000	69,040
194,000	195,000	32,555	259,000	260,000	49,610	324,000	325,000	69,360
195,000	196,000	32,780	260,000	261,000	49,880	325,000	326,000	69,680
196,000	197,000	33,005	261,000	262,000	50,150	326,000	327,000	70,000
197,000	198,000	33,230	262,000	263,000	50,420	327,000	328,000	70,320
198,000	199,000	33,455	263,000	264,000	50,690	328,000	329,000	70,640
199,000	200,000	33,680	264,000	265,000	50,960	329,000	330,000	70,960
200,000	201,000	33,905	265,000	266,000	51,230	$330,000	and over	$71,280 plus 37% of excess over $330,000
201,000	202,000	34,130	266,000	267,000	51,500			
202,000	203,000	34,355	267,000	268,000	51,770			
203,000	204,000	34,580	268,000	269,000	52,040			
204,000	205,000	34,805	269,000	270,000	52,310			
205,000	206,000	35,030	270,000	271,000	52,580			
206,000	207,000	35,300	271,000	272,000	52,850			

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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1986-50

Internal Revenue

bulletin

Bulletin No. 1986–50
December 15, 1986

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–147, page 4.
LIFO; price indexes; department stores. The February 1986 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, February 28, 1986.

Rev. Proc. 86–46, page 6.
LIFO; price indexes; retail department stores. The 20-group (or pool) list set forth in Rev. Proc. 72–21 that was previously used by the United States Bureau of Labor Statistics is replaced with the new 23-group (or pool) list. Rev. Proc. 72–21 modified and superseded.

Rev. Proc. 86–47, page 8.
LIFO; price indexes; retail department stores. A procedure is provided for retail department stores that have elected to use the LIFO inventory identification method in conjunction with the retail method of valuing inventories and have elected to use the United States Bureau of Labor Statistics (BLS) department store price indexes to expeditiously obtain the approval of the Commissioner to change from a list of groups or pools previously used by BLS to a new expanded list of groups or pools.

EMPLOYEE PLANS

Announcement 86–121, page 13.
Changes made with respect to Individual Retirement Arrangements (IRAs) by the Tax Reform Act of 1986 are highlighted.

EXEMPT ORGANIZATIONS

Announcement 86–127, page 17.
A list is given of organizations now classified as private foundations.

EXCISE TAXES

Notice 86–16, page 6.
Windfall profit tax; inflation adjustment factor. For purposes of computing the windfall profit tax, the inflation adjustment for the quarter ending March 31, 1987, is 0.4781 for tier 1 or tier 2 oil and 0.7082 for tier 3 oil.

ADMINISTRATIVE

Rev. Rul. 86–146, page 5.
Adjusted interest rate; underpayments and overpayments. The adjusted rate of interest determined under section 6621 of the Code will be 9 percent on underpayments and 8 percent on overpayments beginning January 1, 1987.

Announcement 86–123, page 15.
New Form 1120–ND, Return for Nuclear Decommissioning Funds and Certain Related Persons, has been developed for use by qualified funds that are created by public utilities to pay the future costs of decommissioning nuclear power plants.

Announcement 86–124, page 15.
New Form 1120–W (FY) (1986–87), Fiscal Year Corporation Estimated Tax, has been developed for use by corporations whose tax years begin in 1986 and end in 1987.

Announcement 86–125, page 15.
New Form 5500EZ, Annual Return of One-Participant Pension Benefit Plan, has been developed for pension benefit plans that cover only an individual and the individual's spouse who wholly own a business.

Announcement 86–126, page 15.
New Form 8453–F, U.S. Fiduciary Income Tax Declaration for Magnetic Media/Electronic Filing, and Form 8453-P, U.S. Partnership Declaration for Magnetic Media/Electronic Filing, have been developed for use by estates and trusts, and partnerships, respectively, participating in the electronic/magnetic media filing pilot program.

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Finding Lists begin on page 21.
Announcement of Disbarments & Suspensions on page 19.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 446.—General Rule for Methods of Accounting

26 CFR 1.446–1: General rule for methods of accounting.

A procedure is provided for retail department stores that have elected to use the LIFO inventory identification method in conjunction with the retail method of valuing inventories and have elected to use the United States Bureau of Labor Statistics (BLS) department store price indexes to expeditiously obtain the approval of the Commissioner to change from a list of groups or pools previously used by BLS to a new expanded list of groups or pools. See Rev. Proc. 86–47, page 8.

Section 471.—General Rule for Inventories

26 CFR 1.471–8: Inventories of retail merchants.

The 20-group (or pool) list set forth in Rev. Proc. 72–21 that was previously used by the United States Bureau of Labor Statistics is replaced with the new 23-group (or pool) list. See Rev. Proc. 86–46, page 6.

26 CFR 1.471–8: Inventories of retail merchants.

A procedure is provided for retail department stores that have elected to use the LIFO inventory identification method in conjunction with the retail method of valuing inventories and have elected to use the United States Bureau of Labor Statistics (BLS) department store price indexes to expeditiously obtain the approval of the Commissioner to change from a list of groups or pools previously used by BLS to a new expanded list of groups or pools. See Rev. Proc. 86–47, page 8.

Section 472.—Last-in, First-out Inventories

26 CFR 1.471–1: Last-in, first-out inventories.

LIFO; price indexes; department stores. The February 1986 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, February 28, 1986.

Rev. Rul. 86–147

The following price indexes for February 1986 were issued by the Bureau of Labor Statistics on March 28, 1986, for use by department stores, and are accepted by the Internal Revenue Service, under section 1.472–1(k) of the Income Tax Regulations and Rev. Proc. 72–21, 1972–1 C.B. 745, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, February 28, 1986.

Indexes are prepared on a national basis for the store total, for 23 major groups of departments, and for three special combinations—soft goods, durable goods and miscellaneous goods. The store total index covers all departments, including some not listed separately, with the following exceptions: candy, foods, liquor, tobacco, as well as contract departments.

The major groups of departments for which indexes are prepared have been expanded from 20 to 23. These new groups are: (1) Group 21—Recreation and Education; (2) Group 22—Home Improvements; and (3) Group 23—Auto Accessories. A Miscellaneous Goods index is also introduced to reflect the aggregate movement of these three new groups. *See* Rev. Proc. 86–46, page 6, this Bulletin.

Although the new indexes are introduced in the February 1986 Department Store Inventory Price Indexes, January 1987 will be the first month for which there will be a percent change based on a 12-month period. The January 1986 indexes for the new groups are all 100. Rev. Proc. 86–46 modifies and supersedes Rev. Proc. 72–21.

Rev. Proc. 86–47, page 8, this Bulletin, sets forth the procedures required of taxpayers to change their method of accounting from that of using the 20 groups set forth in Rev. Proc. 72–21 to the method of using the 23 groups set forth in Rev. Proc. 86–46.

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS
(January 1941 = 100 unless otherwise noted)

	February 1985	February 1986	Percentage Change from February 1985 to February 1986[1]
1. Piece Goods	393.5	394.7	0.3
2. Domestics and Draperies	555.1	546.9	−1.5
3. Women's and Children's Shoes	542.3	523.4	−3.5
4. Men's Shoes	697.3	714.6	2.5
5. Infants' Wear	492.2	523.2	6.3
6. Women's Underwear	428.7	431.1	0.6
7. Women's and Girls' Hosiery	233.6	234.8	0.5
8. Women's and Girls' Accessories	437.2	444.5	1.7
9. Women's Outerwear and Girls' Wear	334.4	329.3	−1.5
10. Men's Clothing	459.3	465.0	1.2
11. Men's Furnishings	468.0	479.4	2.4
12. Boys' Clothing and Furnishings	425.7	432.7	1.6
13. Jewelry	687.7	670.3	−2.5

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[1] Absence of a minus sign before percentage change in this column signifies price increase

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS

(January 1941 = 100 unless otherwise noted)

	February 1985	February 1986	Percentage Change from February 1985 to February 1986[1]
14. Notions	481.5	472.6	−1.8
15. Toilet Articles and Drugs	630.0	657.2	4.3
16. Furniture and Bedding	526.2	540.0	2.6
17. Floor Coverings	459.3	461.6	0.5
18. Housewares	715.4	715.5	0.0
19. Major Appliances	245.7	241.3	−1.8
20. Radio and Television	107.7	100.4	−6.8
21. Recreation and Education	N/A	99.6	N/A
22. Home Improvements	N/A	100.4	N/A
23. Auto Accessories	N/A	99.7	N/A
Groups 1–15: Soft Goods	471.3	472.7	0.3
Groups 16–20: Durable Goods	443.9	444.0	0.0
Groups 21–23: Misc. Goods	N/A	99.8	N/A
Store Total	463.6	465.2	0.3

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[1] Absence of a minus sign before percentage change in this column signifies price increase

26 CFR 1.472–1: Last-in, first-out inventories.

The 20-group (or pool) list set forth in Rev. Proc. 72–21 that was previously used by the United States Bureau of Labor Statistics is replaced with the new 23-group (or pool) list. See Rev. Proc. 86–46, page 6.

26 CFR 1.472–1: Last-in, first-out inventories.

A procedure is provided for retail department stores that have elected to use the LIFO inventory identification method in conjunction with the retail method of valuing inventories and have elected to use the United States Bureau of Labor Statistics (BLS) department store price indexes to expeditiously obtain the approval of the Commissioner to change from a list of groups or pools previously used by BLS to a new expanded list of groups or pools. See Rev. Proc. 86–47, page 8.

Section 6621.—Determination of Rate of Interest

26 CFR 301.6621–1: Interest rate.

Adjusted interest rate; underpayments and overpayments. The adjusted rate of interest determined under section 6621 of the Code will be 9 percent on underpayments and 8 percent on overpayments beginning January 1, 1987.

Rev. Rul. 86–146[1]

Section 6621 of the Internal Revenue Code, as amended by the Tax Reform Act of 1986, section 1511, Pub. L. No. 99–514, 100 Stat.—, establishes differential rates for allowance of interest on tax overpayments and assessment of interest on tax underpayments. Under section 6621(a)(1), the overpayment rate is the sum of the short-term federal rate plus 2 percentage points. Under section 6621(a)(2), the underpayment rate is the sum of the short-term federal rate plus 3 percentage points.

Section 6621(b)(1) of the Code provides that the Secretary shall determine the short-term federal rate for the first month in each calendar quarter.

Section 6621(b)(2) of the Code provides that the federal short-term rate determined under section 6621(b)(1) for any month shall apply during the first calendar quarter beginning after such month.

Section 6621(b)(3) of the Code provides that the federal short-term rate for any month shall be the federal short-term rate determined during such month by the Secretary in accordance with section 1274(d), rounded to the nearest full percent (or, if a multiple of ½ of 1 percent, such rate shall be increased to the next highest full percent.)

Rounded to the nearest full percent, the federal short-term rate determined during the month of October is 6 percent. Accordingly, an overpayment rate of 8 percent and an underpayment rate of 9 percent are established for the calendar quarter beginning January 1, 1987. The rates apply to amounts bearing interest during that calendar quarter. Pursuant to section 6621(b)(2)(B) of the Code, the 9 percent rate applicable to individual estimated tax underpayments also applies through April 15, 1987.

Daily rates for compound interest for 8 percent and 9 percent were published in Tables 14 and 15 of Rev. Proc. 83–7, 1983–1 C.B. 583, 597, 598.

Compound interest rates for prior periods are set forth in the following table:

PERIOD	RATE	DAILY RATE TABLE IN 1983–1 C.B.
January 1, 1983-June 30, 1983	16%	Table 22, pg. 605
July 1, 1983-December 31, 1983	11%	Table 17, pg. 600
January 1, 1984-June 30, 1984	11%	Table 41, pg. 625
July 1, 1984-December 31, 1984	11%	Table 41, pg. 625
January 1, 1985-June 30, 1985	13%	Table 19, pg. 602
July 1, 1985-December 31, 1985	11%	Table 17, pg. 600
January 1, 1986-June 30, 1986	10%	Table 16, pg. 599
July 1, 1986-December 31, 1986	9%	Table 15, pg. 598

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[1] Also released as News Release IR–86–163, dated December 2, 1986.

Part III. Administrative, Procedural, and Miscellaneous

Inflation Adjustment for Computation of Windfall Profit Tax

Notice 86–16

Section 4989(b) of the Internal Revenue Code requires the determination of an inflation adjustment factor for use in computing the windfall profit tax.

The Service has determined that, for oil removed during the January-March quarter of 1986, the inflation adjustments are as follows:

Tier 1 or Tier 2 oil	0.4781
Tier 3 oil	0.7082

Worksheets for computation of the windfall profit tax are included in the Instructions for Form 6047, Windfall Profit Tax, and an explanation of the inflation adjustment may be found in the Specific Instructions for Line 4 of the worksheets.

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26 CFR 601.602: Forms and instructions.
(Also Part I, Sections 471, 472; 1.471–8, 1.472–1.)

Rev. Proc. 86–46

SECTION 1. PURPOSE

The purpose of this revenue procedure is to modify and supersede Rev. Proc. 72–21, 1972–1 C.B. 745, which sets forth the groups or pools used by the United States Bureau of Labor Statistics (BLS) in preparing price indexes for use by department stores that have elected to use the last-in, first-out (LIFO) inventory identification method in conjunction with the retail method of valuing inventories.

SEC. 2. BACKGROUND

.01 Section 1.472–1(k) of the Income Tax Regulations provides that if a taxpayer using the retail method of pricing inventories, authorized by section 1.471–8, elects to use in connection therewith the LIFO method authorized by section 472 of the Internal Revenue Code, the apparent cost of the goods on hand at the end of the year, determined pursuant to section 1.471–8, shall be adjusted to the extent of price changes therein taking place after the close of the preceding tax year. The amount of any apparent inventory increase or decrease to be eliminated in this adjustment shall be determined by reference to acceptable price indexes established to the satisfaction of the Commissioner.

.02 Price indexes prepared by BLS that are applicable to the goods in question are acceptable to the Commissioner under section 1.472–1(k) of the regulations. Monthly indexes are published by BLS and are subsequently published in the Internal Revenue Bulletin. The use of the BLS indexes is not mandatory. Indexes may be prepared by a taxpayer based upon its own data on prices and inventory quantities, subject to the provisions of section 1.472–1(k) of the regulations. Price indexes that are based upon inadequate records, or that are not subject to complete and detailed audit within the Internal Revenue Service, will not be approved.

.03 Section 1.472–8(a) of the regulations provides that under the dollar-value LIFO method of valuing inventories, the goods contained in the inventory are grouped into a pool or pools. Section 1.472–8(g) provides that any method of pooling used in computing the taxpayer's LIFO inventories shall be treated as a method of accounting. Any method of pooling shall be used for the year of adoption and for all subsequent tax years unless a change is required by the Commissioner in order to clearly reflect income, or unless permission to change is granted by the Commissioner as provided in section 1.446–1(e). A taxpayer must secure the consent of the Commissioner under section 1.446–1(e)(2)(i) before it changes its method of accounting for federal income tax purposes.

.04 Rev. Proc. 72–21 provides instructions and illustrations for the use of BLS indexes by a taxpayer who has elected to use the retail method of valuing inventories that are computed under the LIFO method. The last determination of the merchandise groups or pools for department stores was made by BLS in 1953, when 10 groups were added to the then existing 10 groups to reach the total of 20 groups set forth in Rev. Proc. 72–21.

.05 The lines of merchandise typically carried by full-line retail department stores have expanded since the 20 major groups were last revised in 1953. For this reason, BLS will now publish monthly indexes for three new groups and a monthly index for the aggregate of these groups. These new groups are listed in section 4.01 of this revenue procedure.

.06 Because the new indexes were introduced by BLS in February 1986, January 1987 will be the first month for which there will be a percent change based on a 12-month period. The January 1986 indexes for the new groups or pools are all 100.

.07 Rev. Proc. 86–47, page 8, this Bulletin, sets forth the procedures required of taxpayers to change their method of accounting from that of using the 20 groups or pools set forth in Rev. Proc. 72–21 to the method of using the 23 groups or pools set forth in this revenue procedure. Section 3.02 of Rev. Proc. 86–47 provides that its procedures, except as otherwise noted in section 3.03, apply to retail department stores (as described in section 3.01) for their first tax year ending on (or with reference to) a date that is on or after January 31, 1987. Section 3.03 of Rev. Proc. 86–47 provides that if retail department stores (as described in section 3.01) do not have the records necessary to (1) calculate the cost complement for each new expanded pool, or (2) separate its miscellaneous pool or pools into the new expanded pools, its procedures apply to affected retail department stores for their first tax year beginning on (or with reference to) a date that is after January 31, 1987.

SEC. 3. SCOPE

This revenue procedure applies to retail department stores that (1) have elected to use the LIFO inventory identification method in conjunction with the retail method of valuing inventories, and (2) have elected to use the BLS department store price indexes published monthly by the Service.

SEC. 4. THE 23 GROUPS PROVIDED BY BLS

.01 The following groups or combinations of groups are used by BLS as the basis for the preparation of indexes for use by department stores:

1. Piece Goods
2. Domestics and Draperies
3. Women's and Children's Shoes
4. Men's Shoes
5. Infants' Wear
6. Women's Underwear
7. Women's and Girl's Hosiery
8. Women's and Girl's Accessories

9. Women's Outerwear and Girl's Wear
10. Men's Clothing
11. Men's Furnishings
12. Boys' Clothing and Furnishings
13. Jewelry
14. Notions
15. Toilet Articles and Drugs
16. Furniture and Bedding
17. Floor Coverings
18. Housewares
19. Major Appliances
20. Radio and Television
21. Recreation and Education
22. Home Improvements
23. Auto Accessories
1–15: Soft Goods
16–20: Durable Goods
21–23: Miscellaneous Goods

SEC. 5. INSTRUCTIONS REGARDING THE USE OF INDEXES

.01 As illustrated in sections 5 and 6 of this revenue procedure, in using the group indexes, a department store taxpayer must apply to the inventory data for each of its departments separately the index for the group in which the department logically belongs. A given group index may be applicable to a number of departments in a department store.

.02 When one or more departments of a department store do not fit into any one of the 23 major groups or into either of the special combinations listed in section 4.01 of this revenue procedure, an index shall be employed that represents an average for the whole of the remainder of the store. This index may be the store total, as shown by BLS, or the total for those of the 23 major groups (or combination of groups) that most closely represents the coverage of the inventory carried in the department or departments that require an index. For example, in a particular department that carries apparel, piece goods, and notions, the index may be the total of groups 1, 3, 4, 7, 8, 9, 10, 11, 12, and 14 or whichever combination most closely represents the coverage of the inventory stock carried by the store.

SEC. 6. ILLUSTRATION OF FIRST YEAR PRICE ADJUSTMENT

.01 The method of making the first year price adjustments to the closing inventory values under the retail method, combined with the LIFO method, is illustrated for three hypothetical departments. In the first two departments there was an increase in the physical quantity of inventory during the year in question, as shown by the comparison of the adjusted retail value at the end of the year and the retail value at the beginning of the year. In the third department there was a decline in the physical quantity of inventory. In all three departments prices rose during the year, as shown by the index.

Method of Computing LIFO, Retail Inventory, Three Departments, First Year

Step No.	Item or computation	Department No.		
		1 Women's and children's shoes	2 Men's furnishings	3 Radio and television
	I. Data from taxpayer's books			
1	Opening inventory—retail value	$25,000	$40,000	$10,000
2	Opening inventory—mark-on percent	43.6%	45.2%	44.1%
3	Opening inventory—cost (1 reduced by 2)	$14,100	$21,920	$5,590
4	Mark-on on year's purchase (see step 12a)	44.7%	44.8%	44.6%
5	Closing inventory—retail method	$36,000	$42,000	$10,000
6	Closing inventory—mark-on percent	44.4%	44.9%	44.4%
7	Closing inventory—cost (FIFO) (5 reduced by 6)	$20,016	$23,142	$5,560
	II. Price Index Data			
8	Price index, close of year relative to prices at beginning of first LIFO Year as 100%	104.4%	103.4%	100.7%
	III. LIFO Computations			
9	Closing inventory—adjusted retail value (5/8)	$34,483	$40,619	$9,930
10	Increase (decrease) in year (9-1)	$9,483	$619	($70)
11	Increase at current prices (10×8)	$9,900	$640	
12a	Cost of increase (11 reduced by 4)	$5,475	$353	
12b	Cost of decrease (10 reduced by 2)			($39)
13	LIFO closing inventory (3 + 12a or 3 − 12b)	$19,575	$22,273	$5,551

Notes

(a) The mark-ons in steps 2 and 4 must be computed taking account of markdowns as well as mark-ups.

(b) In succeeding years the data to be used in steps 1, 2, and 3, to the extent applicable, must be taken from the taxpayer's books as of the beginning of the first year of the use of the LIFO method, and must be identical to those shown in the first year's computations.

(c) Steps 6 and 7 are shown to allow comparison of LIFO and FIFO inventories.

(d) The index in step 8 is the index of retail prices applicable to the goods in each department, showing the level of prices at the end of the year (104.4% in department 1) relative to the beginning of the year (100.0%).

SEC. 7. ILLUSTRATION OF SECOND AND THIRD YEAR ADJUSTMENTS

.01 To illustrate further the principles involved in making adjustments for additional years the data for Department 1 are shown below, the first year being repeated to show the continuity. The physical quantity of inventory increased in the first two years, but decreased in the third year, as indicated by the adjusted retail values (Line 9). Note that the decrease in the third year eliminated all of the second year's increase and part of the first year's increase, in that order, retaining in the closing inventory the merchandise appearing in the opening inventory "in the order of acquisition" (Line 10). Thus, it is necessary under the LIFO method to retain the identity of each annual increment to the inventory of each department. The price changes are measured by reference to the fixed prices at the beginning of the first LIFO year and the retail inventory value on each inventory date is adjusted to the price level on that date.

.02 These illustrations are intended to show the main principles involved in the LIFO adjustments to retail inventories, and are not intended to cover all accounting details of computations which may be required, particularly in later years, under the LIFO method.

Method of Computing LIFO, Retail Inventory Dept. No. 1, First Three Years

Step No.	Item or computation	First year	Second year	Third year
	I. Data from taxpayer's books			
1	Opening inventory—First LIFO year—retail	$25,000	$25,000	$25,000
2	Opening inventory—First LIFO year—mark-on percent	43.6%	43.6%	43.6%
3	Opening inventory—First LIFO year—cost (1 reduced by 2)	$14,100	$14,100	$14,100
4	Mark-on year's purchases	44.7%	44.8%	44.9%
5	Closing inventory given year—retail value	$36,000	$43,000	$34,000
	II. Price Index Data			
8	Price index, close of given year relative to prices at beginning of first LIFO year as 100%	104.4%	107.2%	104.5%
	III. LIFO Computations			
9	Closing inventory—adjusted retail value at price level of opening inventory for first LIFO year (5/8)	$34,483	$40,112	$32,536
10	Increase over opening inventory for first LIFO year (9-1)	$9,483	$15,112	$7,536
	a. Amount of increase attributable to first year	$9,483	$9,483	$7,536
	b. Amount of increase attributable second year		$5,629	0
11	Increase at prices existing when acquired:			
	a. First year's increase (10a × 104.4%)	$9,900	$9,900	$7,875
	b. Second year's increase (10b × 107.2%)		$6,035	
12	Cost of increases:			
	a. First year's increase (11a reduced by 44.7%)	$5,475	$5,475	$4,339
	b. Second year's increase (11b reduced by 44.87%)		$3,313	
	Add (3) above	$14,100	$14,100	$14,100
13	LIFO closing inventory (Sum of 12 and 3)	$19,575	$22,888	$18,439

SEC. 8. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 72–21 is modified and as modified is superseded.

SEC. 9. EFFECTIVE DATE

For taxpayers described in section 3.01 of Rev. Proc. 86–47, but not described in section 3.03 of Rev. Proc. 86–47, this revenue procedure is effective for tax years ending on (or with reference to) a date that is on or after January 31, 1987. For taxpayers described in sections 3.01 and 3.03 of Rev. Proc. 86–47, this revenue procedure is effective for tax years beginning on (or with reference to) a date that is after January 31, 1987.

Rev. Proc. 72–21 shall continue to be effective for tax years ending on (or with reference to) a date that is prior to January 31, 1987. For taxpayers described in sections 3.01 and 3.03 of Rev. Proc. 86–47, Rev. Proc. 72–21 shall continue to be effective for tax years beginning on (or with reference to) a date that is prior to January 31, 1987.

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26 CFR 601.602: Forms and instructions.
(Also Part I, Sections 446, 471, 472; 1.446–1, 1.471–8, 1.472–1.)

Rev. Proc. 86–47

SECTION 1. PURPOSE

The purpose of this revenue procedure is to provide a procedure whereby retail department stores using the retail method of valuing inventories and the last-in, first-out (LIFO) inventory identification method pursuant to the provisions of Rev. Proc. 72–21, 1972–1 C.B. 745, may expeditiously obtain the approval of the Commissioner of Internal Revenue to change from a list of groups or pools previously used by the United States Bureau of Labor Statistics (BLS) to a new expanded list of groups or pools.

SEC. 2. BACKGROUND

.01 Section 446(e) of the Internal Revenue Code and section 1.446–1(e)(2)(i) of the Income Tax Regulations provide that a taxpayer must secure the consent of the Commissioner before it changes its methods of accounting for federal income tax purposes. Section 1.44–1(e)(3)(i) requires that, in general, to obtain this consent a Form 3115, Application for Change in Accounting Method, must be filed within 180 days after the beginning of the tax year for which the proposed change is to be made. Section 1.446–1(e)(3)(ii) authorizes the Commissioner to prescribe administrative procedures setting forth the limitations, terms, and conditions deemed necessary to permit taxpayers to obtain consent to change their method of accounting in accordance with section 1.446–1(e)(2)(i).

.02 Section 1.472–8(g)(1) of the regulations provides that any method of pooling authorized by the regulations and used by the taxpayer in computing its LIFO inventories under the dollar-value method shall be treated as a method of accounting. Any LIFO pooling method, once adopted, must be continued for all subsequent tax years unless a change is required by the Commissioner in order to clearly reflect income, or unless permission to change the method is granted by the Commissioner under section 1.446–1(e).

.03 Section 1.472–1(k) of the regulations provides that if a taxpayer using the retail method of pricing inventories, authorized by section 1.471–8, elects to use in connection therewith the LIFO method, the apparent cost of the goods on hand at the end of the year, determined pursuant to section 1.471–8, shall be adjusted to the extent of price changes therein taking place after the close of the preceding tax year. The amount of any apparent inventory increase or decrease to be eliminated in this adjustment shall be determined by reference to acceptable price indexes established to the satisfaction of the Commissioner. Price indexes prepared by BLS that are applicable to the goods in question are acceptable to the Commissioner under 1.472–1(k).

.04 Section 1.472–8(g)(2)(i) of the regulations provides that a taxpayer that is permitted or required to change its method of dollar-value LIFO pooling shall combine or separate the LIFO value of its inventory for the base year and each yearly layer of increment in order to conform to the new pools. Each yearly layer of increment in the new pool or pools must be separately accounted for and a record thereof maintained, and any liquidation occurring in the new pool or pools subsequent to the formation thereof shall be treated in the same manner as if the new pool or pools had existed from the date the taxpayer first adopted the LIFO method. The combination or separation of the LIFO value of the inventory for the base year and each yearly layer shall be made in accordance with the appropriate method set forth in section 1.472–8(g)(2)(ii), unless the use of a different method is approved by the Commissioner. Section 1.472–8(g)(2)(ii) provides that in separating a pool, each item in the former pool shall be placed in an appropriate new pool. Every item in each new pool is then extended at its base-year unit cost and the extensions are totaled. The regulations provide further steps for the complete separation of the LIFO value of the dollar-value pool into the expanded pools.

.05 Rev. Proc. 72–21 provides instructions and illustrations for the use of BLS indexes by a taxpayer that has elected to use the retail valuation method and the LIFO inventory identification method. Rev. Proc. 72–21 sets forth the 20 groups or pools used by BLS as the basis for the preparation of the indexes.

.06 Beginning in February 1986, BLS replaced the 20-group list with a 23-group list. The additional groups are: (1) Group 21—Recreation and Education; (2) Group 22—Home Improvements; and (3) Group 23—Auto Accessories. *See* Rev. Proc. 86–46, page 6, this Bulletin, which modifies and supersedes Rev. Proc. 72–21 by replacing the 20-group list with the 23-group list. Because the new indexes were introduced by BLS in February 1986, January 1987 will be the first month for which there will be a percent change based on a 12-month period. The January 1986 indexes for the new groups or pools are all 100.

.07 Taxpayers that presently compute their LIFO inventory by reference to the pools set forth in Rev. Proc. 72–21 are required under section 1.472–1(k) of the regulations to change their LIFO pooling method to conform to the expanded number of pools set forth in Rev. Proc. 86–47.

.08 Retail department stores that carry goods covered by the expanded groups presently use a miscellaneous pool or pools for these and other goods and use the BLS Store Total index, or develop their own index or indexes, to compute the LIFO value of the miscellaneous pool or pools. For these taxpayers, a change in method of accounting to comply with the provisions of Rev. Proc. 86–46 will involve a separation of the present miscellaneous pool or pools.

.09 The procedure set forth in section 1.472–8(g)(2)(ii) of the regulations and the example provided therein presuppose that the taxpayer uses the double-extension method of computing its LIFO inventory value. Under that method, the quantity of each item in a dollar-value pool at the close of the tax year is extended at both base-year unit cost and current-year unit cost. The dollar-value LIFO retail method used by retail department stores, as illustrated in Rev. Proc. 72–21, is based upon the so-called "link-chain" method. Under this method, cumulative price indexes are developed and published by BLS with the acceptance of the Internal Revenue Service, and it is not possible to compute original base-year unit costs for items in each dollar-value pool.

SEC. 3. SCOPE

.01 This revenue procedure applies to a retail department store that: (1) Uses the retail valuation method and the LIFO inventory identification method pursuant to the provisions of Rev. Proc. 72–21; (2) uses a miscellaneous pool or pools for goods described in new groups 21, 22, or 23; and (3) uses the BLS store total index, or develops its own index or indexes, in computing the LIFO value of this miscellaneous pool or pools.

.02 Except as otherwise provided in section 3.03, this revenue procedure applies to a retail department store described in section 3.01 for its first tax year ending on (or with reference to) a date that is on or after January 31, 1987.

.03 If a retail department store described in section 3.01 for its tax year described in section 3.02 does not have the records necessary to (1) calculate the cost complement for each new expanded pool, or (2) separate its miscellaneous pool or pools into the new expanded pools, this revenue procedure applies to this retail department store for its first tax year beginning on (or with reference to) a date that is after January 31, 1987.

.04 Those taxpayers that are required under this revenue procedure to change their method of accounting and to whom this revenue procedure does not apply should file a Form 3115 with the Commissioner in accordance with section 1.446–1(e)(3) of the regulations and Rev. Proc. 84–74, 1984–2 C.B. 736, if applicable.

SEC. 4. APPLICATION

.01 In accordance with section 1.446–

1(e)(3)(ii) of the regulations the 180-day rule is waived, and under section 1.446–1(e)(2)(i) consent is hereby granted to taxpayers described in section 3.01 of this revenue procedure. This consent is granted for the tax year described in section 3.02 or section 3.03 of this revenue procedure and for which a taxpayer requests a change (year of change) by filing a current Form 3115, Application for Change in Accounting Method, in the manner described in section 6 of this revenue procedure. Consent is not granted unless the taxpayer complies with the provisions of this revenue procedure.

.02 In accordance with section 1.472–8(g)(2)(i) of the regulations, which allows the Commissioner to approve a procedure for separating LIFO pools different from that described in section 1.472–8(g)(2), the Service will approve the separation of present miscellaneous dollar-value pools of retail department stores into the expanded pools set forth in Rev. Proc. 86–46 in the manner set forth in sections 4.03 and 4.04 of this revenue procedure.

.03 The procedures required of retail department stores in separating a miscellaneous pool or pools into the expanded pools set forth in Rev. Proc. 86–46 are based on the principles of sections 1.472–8(g)(3) and 1.472–8(e)(3)(vi) of the regulations. These procedures in general are as follows: (1) The base-year cost and layers of increment previously computed under the former pooling method are retained; (2) in using the new pooling method the new base year is the year of change; and (3) since the retail method does not contemplate accounting for the individual items in inventory, the separation of the original base-year cost and layers of increment into the new pools is based on the relationship of the current retail value of each of the departments in the ending inventory with respect to the miscellaneous pool for the tax year immediately preceding the year of change. The year of change must be the tax years described in sections 3.02 or 3.03 of this revenue procedure.

.04 *Example.* (1) The taxpayer, a retail department store, with a fiscal tax year ending January 31, has used Rev. Proc. 72–21 to compute the LIFO value of its dollar-value pools. For purposes of its LIFO inventory valuation, the taxpayer's base year began on February 1, 1983. The taxpayer's inventory includes departments A, B, C, and D that were all grouped together in one miscellaneous dollar-value LIFO pool prior to January 31, 1986. Departments A and B include merchandise described in new Group 21, and Departments C and D include merchandise described in new Group 22. The taxpayer does not sell any merchandise described in new Group 23. The LIFO inventory value at retail, at January 31, 1986, is computed as follows:

	Jan. 31, 1986 inventory at Feb. 1, 1983 base-year prices	Pool ABCD ratio of total current year prices to total base-year prices	Jan. 31, 1986 inventory at LIFO retail value
Feb. 1, 1983 base	$10,000	100%	$10,000
Jan. 31, 1984 increment	1,000	110	1,100
Jan. 31, 1985 increment	5,000	120	6,000
Jan. 31, 1986 increment	4,000	125	5,000
	$20,000		$22,100

The above composition of the LIFO retail value of the original pool reflects the LIFO base and layers at January 31, 1986, which is the date that immediately precedes the separation of the original LIFO pool into the expanded new pools as required by Rev. Proc. 86–46.

(2) The extension of the quantities of departments A, B, C, and D at their respective current-year retail prices at January 31, 1986, is as follows:

Dept.	Current Retail Value
A	$ 5,000
B	3,000
C	7,000
D	10,000
	$25,000

This step presents the retail value of each department in the original LIFO pool. The individual departmental retail values need only be determined for those departments directly affected by the new pooling configuration. That is, retail values are determined only for those departments being removed from the previous miscellaneous LIFO pool.

(3) In applying the provisions of this revenue procedure, the taxpayer separates former pool ABCD into two pools, AB and CD. The computation of the allocation of current retail value, by base year and layer, between the two pools is made on the basis of the ratio of total current retail value ($25,000) to total old base-year prices ($20,000) and the relationship of LIFO retail value to current retail value (new base-year prices) as of January 31, 1986, as follows:

	I 2/1/83 old base price	II/I current retail value to old base price relationship	II 1/31/86 current retail value	III 1/31/86 inventory at LIFO retail value	III/II LIFO to current retail value relationship
Feb. 1, 1983 base	$10,000	125	$12,500	$10,000	80%
Jan. 31, 1984 increment	1,000	125	1,250	1,100	88
Jan. 31, 1985 increment	5,000	125	6,250	6,000	96
Jan. 31, 1986 increment	4,000	125	5,000	5,000	100
	$20,000	125%	$25,000	$22,100	

(4) The determination of the relationship between current retail value and old base price creates the ratio needed to translate old base prices to equivalent current base prices comprising the new base year (current retail value). Subsequently, a comparison of the new base-year price with the LIFO retail value results in a LIFO retail value to current retail value relationship. This relationship is used whenever a decrease in the LIFO retail inventory value occurs that results in the penetration of a layer or the base year inventories accumulated prior to the pool separation. In this event, the reductions of LIFO retail value and current retail value bear this relationship. For example, if the January 31, 1985, increment ($6,250) incurred a decrement of $3,125, the LIFO retail value would decrease by $3,000 ($3,125 × 96%).

(5) The ratio of the new base-year price of new pools AB and CD to the base-year price of former pool ABCD is 8,000/25,000 and 17,000/25,000, respectively. The allocation of the January 31, 1986, current retail value (new base-year price) of former pool ABCD to pools AB and CD is as follows:

	New base-year price to be allocated	Pool AB	Pool CD
2/1/83	$12,500	$4,000	$ 8,500
1/31/84	1,250	400	850
1/31/85	6,250	2,000	4,250
1/31/86	5,000	1,600	3,400
	$25,000	$8,000	$17,000

This step divides the components of the current retail value of the original LIFO pool into the separated components of the new pools. The overall relationship between the old and new pools at January 31, 1986, is used to allocate the current retail amount among the base year and layers, by pool.

(6) The LIFO retail value of new pools AB and CD at January 31, 1986, as allocated, is as follows:

Pool AB	Jan. 31, 1986, inventory at new base-year (Feb. 1, 1986) price	LIFO to current retail value relationship	Jan. 31, 1986, inventory at LIFO retail value
2/1/83	$ 4,000	80%	$ 3,200
1/31/84	400	88	352
1/31/85	2,000	96	1,920
1/31/86	1,600	100	1,600
	$ 8,000		$ 7,072
Pool CD			
2/1/83	$ 8,500	80	$ 6,800
1/31/84	850	88	748
1/31/85	4,250	96	4,080
1/31/86	3,400	100	3,400
	$17,000		$15,028
	$25,000		$22,100

This step completes the separation of the value of the original LIFO pool into the new pools. This is done by using the LIFO to current retail value relationship developed above to reduce the current retail value amounts to their appropriate LIFO retail values, by base year and layer.

(7) The above determined LIFO base and layers, at retail value, are then converted, by applying the appropriate cost complement percentages of the original pools for the various years, to produce the inventory valuation, at LIFO cost, for each pool.

(8) Once the separation of the original LIFO pool into the new pools has been completed, LIFO calculations are to be made as if the year of separation was the initial LIFO year. Increases in closing inventory at adjusted retail value (see step 9 in section 7.02 of Rev. Proc. 86–46) over new base-year prices (February 1, 1986) will result in increments and will be priced reflecting inflation from a base-year LIFO inventory as of the year of separation. Decreases in closing inventory at adjusted retail value under new base-year prices (February 1, 1986) will result in decrements and will be removed from inventory in reverse chronological order at the LIFO to current retail value relationship applicable to the year the inventory was initially recorded.

SEC. 5. COMPLIANCE WITH CONDITIONS

Taxpayers making a change in method of accounting with respect to its pooling method without complying with all the conditions of this revenue procedure will be deemed to have initiated the change without obtaining the consent of the Commissioner.

SEC. 6. MANNER OF EFFECTING CHANGE

.01 Except as otherwise provided in section 6.02 of this revenue procedure, taxpayers described in section 3.01 of this revenue procedure must effect the change in their methods of accounting for their first tax year ending on (or with reference to) a date that is on or after January 31, 1987.

.02 Taxpayers described in sections 3.01 and 3.03 of this revenue procedure must effect the change in their methods of accounting for their first tax year beginning on (or with reference to) a date that is after January 31, 1987.

.03 The change is effected pursuant to the provisions set forth in this revenue procedure by filing a current Form 3115, in duplicate. The original of the Form 3115 must be attached to the taxpayer's timely filed federal income tax return for the tax year of the change (determined with regard to extensions) or to an amended return for such year filed no later than the extended time period prescribed in section 6081 of the Code and the regulations thereunder. Solely for purposes of the preceding sentence, a federal income tax return which is filed late, but within the time period described in section 6081 of the Code and the regulations thereunder, shall be treated as timely, regardless of the fact that the taxpayer has not been granted an extension of time for filing its income tax return. At the time the original of the Form 3115 is filed with the federal income tax return, a copy of the Form 3115 must be filed with the National Office, addressed to the Commissioner of Internal Revenue, Attention: CC:C:C:1, 1111 Constitution Ave. N.W., Washington, DC 20224.

.04 Taxpayers described in sections 3.01 and 3.03 of this revenue procedure must sign and attach to the original and duplicate of the Form 3115 a copy of the following statement:

Under penalties of perjury, I certify that the books and records of [insert name of taxpayer] do not contain sufficient information to (1) calculate the cost complement for each new expanded pool, or (2) separate the miscellaneous pool or pools into the new expanded pools for [insert the taxpayer's tax year that is the first tax year ending on (or with reference to) a date that is on or after January 31, 1987].

The original of this representation statement must also be attached to the taxpayer's filed federal income tax return for its first tax year ending on (or with reference to) a date that is on or after January 31, 1987. This statement must be signed by a person (or persons) that has the authority to bind the taxpayer. For example, an officer must sign on behalf of a corporation, a general partner on behalf of a partnership, a trustee on behalf of a trust, or a sole proprietor on behalf of himself or herself.

.05 To assist in the processing of these changes in method of accounting and to ensure proper handling, reference to this revenue procedure shall be made a part of the Form 3115 by either typing or legibly printing the following statement at the top of page 1 of Form 3115: "FILED UNDER REV. PROC. 86–47.

.06 The signature of the individual preparing the application for the taxpayer must appear in the space at the bottom of page one on the Form 3115. An application made by an agent on behalf of a taxpayer must be accompanied by a power of attorney authorizing the agent to sign for the taxpayer. If the agent is also authorized to represent the taxpayer before the Service, to receive the original or a copy of correspondence concerning the request, or perform any other act(s) regarding the application on behalf of the taxpayer, the power of attorney must reflect such authorization(s). If the taxpayer is a member of an affiliated group that has elected to file a consolidated federal income tax return, the Form 3115 submitted on behalf of the taxpayer, as described above, must be signed by a duly authorized officer of the common parent. (See section 1.1502–77 of the regulations.)

SEC. 7. INQUIRIES

Inquiries in regard to this revenue procedure should refer to its number and be addressed to the Commissioner of Internal Revenue, Attention: CC:C:C:1, 1111 Constitution Avenue N.W., Washington, DC 20224.

SEC. 8. EFFECTIVE DATE

For taxpayers described in section 3.01 of this revenue procedure, but not described in section 3.03, this revenue procedure is effective for the first tax year ending on (or with reference to) a date that is on or after January 31, 1987. For taxpayers described in sections 3.01 and 3.03, this revenue procedure is effective for the first tax year beginning on (or with reference to) a date that is after January 31, 1987.

Part IV. Items of General Interest

General Description of the Tax Reform Act of 1986 Provisions Affecting Individual Retirement Arrangements

Announcement 86–121

This announcement highlights some of the changes made by the Tax Reform Act of 1986 (the Act) with respect to Individual Retirement Arrangements (IRAs). The announcement is intended to be a nontechnical explanation, rather than a comprehensive statement of the new rules concerning IRAs.

For a nontechnical explanation of the rules in effect before the new Act, as well as an explanation of the new law, see Internal Revenue Service Publication 590, which will be available at any IRS District office beginning early in January 1987.

This announcement may be used by a master or prototype IRA sponsor to update its disclosure statement, required by Treasury Regulations at section 1.408–6.

The Service expects to publish technical guidance concerning the Act changes to IRAs in the near future.

The nontechnical explanation follows:

The Tax Reform Act of 1986 (which we will call the Act) makes a number of major changes to the law governing the deductibility of contributions to Individual Retirement Arrangements (IRAs).

The changes made by the Act are generally not effective until January 1, 1987. This means that contributions made for 1987 are subject to the Act's new rules; however, you can still make a contribution for 1986 as late as April 15, 1987 under the old rules.

ELIGIBILITY

Under the new law, if neither you, nor your spouse, is an active participant (see A. below) you may make a contribution of up to the lesser of $2,000 (or $2,250 in the case of a spousal IRA) or 100% of compensation and take a deduction for the entire amount contributed. If you are an active participant but have an adjusted gross income (AGI) below a certain level (see B. below), you may make a deductible contribution as under current law. If, however, you or your spouse is an active participant and your combined AGI is above the specified level, the amount of the deductible contribution you may make to an IRA is phased down and eventually eliminated.

A. Active Participant

You are an "active participant" for a year if you are covered by a retirement plan. You are covered by a "retirement plan" for a year if your employer or union has a retirement plan under which money is added to your account or you are eligible to earn retirement credits. For example, if you are covered under a profit-sharing plan, certain government plans, a salary reduction arrangement (such as a tax sheltered annuity arrangement or a 401(k) plan), a simplified employee pension plan (SEP) or a plan which promises you a retirement benefit which is based upon the number of years of service you have with the employer, you are likely to be an active participant. Your Form W–2 for the year, starting with the 1987 tax year, should indicate your participation status.

You are an active participant for a year even if you are not yet vested in your retirement benefit. Also, if you make required contributions or voluntary employee contributions to a retirement plan, you are an active participant. In certain plans you may be an active participant even if you were only with the employer for part of the year.

You are not considered an active participant if you are covered in a plan only because of your service as 1) an Armed Forces Reservist, for less than 90 days of active service, or 2) a volunteer firefighter covered for firefighting service by a government plan. Of course, if you are covered in any other plan, these exceptions do not apply.

If you are married but file a separate tax return, your spouse's active participation does not affect your ability to make deductible contributions.

B. Adjusted Gross Income (AGI)

If you are an active participant, you must look at your Adjusted Gross Income for the year (if you and your spouse file a joint tax return you use your combined AGI) to determine whether you can make a deductible IRA contribution. Your tax return will show you how to calculate your AGI for this purpose. If you are at or below a certain AGI level, called the Threshold Level, you are treated as if you were not an active participant and can make a deductible contribution under the same rules as a person who is not an active participant.

If you are single, your threshold AGI level is $25,000. The threshold level if you are married and file a joint tax return is $40,000, and if you are married but file a separate tax return, the threshold level is $0.

If your AGI is less than $10,000 above your threshold level, you will still be able to make a deductible contribution but it will be limited in amount. The amount by which your AGI exceeds your Threshold Level (AGI − Threshold Level) is called your Excess AGI. The Maximum Allowable Deduction is $2,000 (or $2,250 for a Spousal IRA). You can estimate your Deduction Limit using Table I on Page 16, or calculate it as follows:

(Your Deduction Limit may be slightly higher if you use this formula rather than the Table).

$$\frac{10{,}000 - \text{Excess AGI}}{10{,}000} \times \text{Maximum Allowable Deduction} = \text{Deduction Limit}$$

You must round up the result to the next highest $10 level (the next highest number which ends in zero). For example, if the result is $1,525, you must round it up to $1,530. If the final result is below $200 but above zero, your Deduction Limit is $200. Your Deduction Limit cannot, in any event, exceed 100% of your compensation.

Example 1: Ms. Smith, a single person, is an active participant and has an AGI of $31,619. She calculates her deductible IRA contribution as follows:

Her AGI is $31,619

Her Threshold Level is $25,000

Her Excess AGI is (AGI − Threshold Level) or ($31,619 − $25,000) = $6,619

Her Maximum Allowable Deduction is $2,000

So, her IRA deduction limit is:

$$\frac{\$10{,}000 - \$6{,}619}{\$10{,}000} \times \$2{,}000 = \$676 \text{ (rounded to \$680).}$$

Example 2: Mr. and Mrs. Young file a joint tax return. Each spouse earns more than $2,000 and one is an active participant. They have a combined AGI of

$44,255. They may each contribute to an IRA and calculate their deductible contributions to each IRA as follows:

Their AGI is $44,255

Their Threshold Level is $40,000

Their Excess AGI is (AGI − Threshold Level) or ($44,255 − $40,000) = $4,255

The Maximum Allowable Deduction for each spouse is $2,000

So, each spouse may compute his or her IRA deduction limit as follows:

$$\frac{\$10{,}000 - \$4{,}255}{\$10{,}000} \times \$2{,}000 = \$1{,}149 \text{ (rounded to \$1,150).}$$

Example 3: If, in example 2, Mr. Young did not earn any compensation, or elected to be treated as earning no compensation, Mrs. Young could establish a Spousal IRA (consisting of an account for herself and one for her husband). The amount of deductible contributions which could be made to the two IRAs is calculated using a Maximum Allowable Deduction of $2,250 rather than $2,000.

$$\frac{\$10{,}000 - \$4{,}255}{\$10{,}000} \times \$2{,}250 = \$1{,}293 \text{ (rounded to \$1,300).}$$

The $1,300 can be divided between the two accounts, but neither IRA may receive a deductible contribution of more than $1,150.

Example 4: Mr. Jones, a married person, files a separate tax return and is an active participant. He has $1,500 of compensation and wishes to make a deductible contribution to an IRA.

His AGI is $1,500

His Threshold Level is $0

His Excess AGI is (AGI − Threshold Level) or ($1,500 − $0) = $1,500

His Maximum Allowable Deduction is $2,000

So, his IRA deduction limit is:

$$\frac{\$10{,}000 - \$1{,}500}{\$10{,}000} \times \$2{,}000 = \$1{,}700$$

Even though his IRA deduction limit under the formula is $1,700, Mr. Jones may not deduct an amount in excess of his compensation, so, his actual deduction is limited to $1,500.

SPOUSAL IRAs

As noted in Example 3 above, under the Act you may contribute to a Spousal IRA even if your spouse has earned some compensation during the year. Provided your spouse does not make a contribution to an IRA, you may set up a Spousal IRA consisting of an account for your spouse as well as an account for yourself. The maximum deductible amount for the spousal IRA is the lesser of $2,250 or 100% of compensation. This rule applies for 1986 spousal IRAs as well as 1987 spousal IRAs.

NONDEDUCTIBLE CONTRIBUTIONS TO IRAs

Even if you are above the threshold level and thus may not make a deductible contribution of $2,000 ($2,250 for a spousal IRA), you may still contribute up to the lesser of 100% of compensation or $2,000 to an IRA ($2,250 for a Spousal IRA). The amount of your contribution which is not deductible will be a nondeductible contribution to the IRA. You may also choose to make a contribution nondeductible even if you could have deducted part or all of the contribution. Interest or other earnings on your IRA contribution, whether from deductible or nondeductible contributions, will not be taxed until taken out of your IRA and distributed to you.

If you make a nondeductible contribution to an IRA you must report the amount of the nondeductible contribution to the IRS as a part of your tax return for the year.

You may make a $2,000 contribution at any time during the year, if your compensation for the year will be at least $2,000, without having to know how much will be deductible. When you fill out your tax return you may then figure out how much is deductible.

You may withdraw an IRA contribution made for a year any time before April 15 of the following year. If you do so, you must also withdraw the earnings attributable to that portion and report the earnings as income for the year for which the contribution was made. If some portion of your contribution is not deductible, you may decide either to withdraw the nondeductible amount, or to leave it in the IRA and designate that portion as a nondeductible contribution on your tax return.

IRA DISTRIBUTIONS

Because nondeductible IRA contributions are made using income which has already been taxed (that is, they are not deductible contributions), the portion of the IRA distributions consisting of nondeductible contributions will not be taxed again when received by you. If you make any nondeductible IRA contributions, each distribution from your IRAs will consist of a nontaxable portion (return of nondeductible contributions) and a taxable portion (return of deductible contributions, if any, and account earnings). Thus, you may not take a distribution which is entirely tax-free. The following formula is used to determine the nontaxable portion of your distributions for a taxable year:

$$\frac{\begin{array}{c}\text{Remaining}\\ \text{Nondeductible contributions}\end{array}}{\begin{array}{c}\text{Year-end total IRA}\\ \text{account balances}\end{array}} \times \begin{array}{c}\text{Total Distributions}\\ \text{(for the year)}\end{array} = \begin{array}{c}\text{Nontaxable distributions}\\ \text{(for the year)}\end{array}$$

To figure the year-end total IRA account balance you treat all of your IRAs as a single IRA. This includes all regular IRAs, as well as Simplified Employer Pension (SEP) IRAs, and Rollover IRAs. You also add back the distributions taken during the year.

Example: An individual makes the following contributions to his or her IRAs:

Year	*Deductible*	*Nondeductible*
1983	$2,000	
1984	1,800	
1987	1,000	$1,000
1989	600	1,400
	$5,400	$2,400

Deductible Contributions:	$5,400
Nondeductible Contributions:	2,400
Earnings on IRAs:	1,200
Total Account Balance of IRAs as of 12/31/91: (including distributions in 1991)	$9,000

In 1991 the individual takes a distribution of $3,000. The total account balance in the IRAs on 12/31/91 plus 1991 distributions is $9,000. The nontaxable portion of the distributions for 1991 is figured as follows:

$$\frac{\text{Total nondeductible contributions}}{\text{Total account balance in the IRAs plus distributions}} \qquad \frac{\$2,400}{\$9,000} \times \$3,000 = \$800$$

Thus, $800 of the $3,000 distribution in 1991 will not be included in the individual's taxable income. The remaining $2,200 will be taxable for 1991.

ROLLOVER IRA RULES

The Act made some changes in the rules for rollovers of *partial* distributions from retirement plans into IRAs. (A partial distribution is one which represents at least 50 percent of the amount owed to you from a retirement plan.)

After December 31, 1986, if you receive a partial distribution from an employer's pension plan after December 31, 1986, and the distribution is paid to you

1) because you separated from service with the employer.
2) because you became disabled while working for the employer, or
3) because of the death of your spouse while he or she was covered under the employer's plan, if you are named as a beneficiary.

then you may deposit that amount into a Rollover IRA.

IRA ARRANGEMENTS

In general, the above changes affect individual deduction provisions, rather than provisions required in IRA documents. Therefore, until further notice, trustees using Model IRAs and IRAs which have been approved under the IRA National Office Master and Prototype program need not amend their IRA documents to reflect the changes in the laws concerning IRAs.

New Form 1120–ND, Return For Nuclear Decommissioning Funds and Certain Related Persons

Announcement 86–123

New Form 1120–ND, Return For Nuclear Decommissioning Funds and Certain Related Persons, has been developed for use by qualified funds that are created by public utilities to pay the future costs of decommissioning nuclear power plants. These funds must file the Form 1120–ND to report contributions received, income earned, payment of the administrative expenses of the fund, the tax on income earned, and information on whether any acts of self-dealing have occurred during the tax year. Form 1120–ND must also be filed by trustees or disqualified persons who engage in acts of self-dealing with the fund.

Form 1120–ND must be filed within two and one-half months after the close of the taxpayer's tax year. It will be available beginning in January 1987.

New Form 1120–W (FY)(1986–87), Fiscal Year Corporation Estimated Tax

Announcement 86–124

New Form 1120–W (FY)(1986–87), Fiscal Year Corporation Estimated Tax, has been developed for use by corporations whose tax years begin in 1986 and end in 1987. The form highlights the changes made by the Tax Reform Act of 1986 that affect fiscal year taxpayers. It also provides a prorated tax computation for taxpayers whose tax years end after June 30, 1987, and includes a new computation of alternative tax under section 1201 of the Internal Revenue Code for all fiscal 1986–87 filers.

Corporations whose tax years begin in 1986 and end in 1987 should use this form to compute their estimated tax or recompute the amount due for each installment if estimated tax payments have already been made.

Form 1120–W (FY) (1986–87) will be available in January 1987.

New Form 5500EZ, Annual Return of One-Participant Pension Benefit Plan

Announcement 86–125

New Form 5500EZ, Annual Return of One-Participant Pension Benefit Plan, has been developed for use by pension benefit plans that cover only an individual or an individual and the individual's spouse who wholly own a business. This form may also be used for a plan or a partnership that covers only the partners, or the partners and their spouses, as long as the plan meets the coverage requirements of Internal Revenue Code section 410(b)(1) without being combined with any other plan.

The Form 5500EZ may not be used for a pension plan of a business that:

(a) is a member of an affiliated service group,

(b) is a member of a controlled group of corporations,

(c) is a member of a group of businesses under common control, or

(d) leases employees.

The use of Form 5500EZ will substantially reduce the reporting burden for small "one-participant" pension plans.

The Form 5500EZ will be available to the public in January 1987. It may be filed for plan years starting in 1986.

New Form 8453–F, U.S. Fiduciary Income Tax Declaration for Magnetic Media/Electronic Filing, and Form 8453–P, U.S. Partnership Declaration for Magnetic Media/Electronic Filing

Announcement 86–126

New Form 8453–F, U.S. Fiduciary Income Tax Declaration for Magnetic Media/Electronic Filing, and Form 8453–P, U.S. Partnership Declaration for Magnetic Media/Electronic Filing, have been developed for use by estates and trusts, and partnerships, respectively, participating in the 1986 electronic/magnetic media filing pilot program. These entities can use the program only for tax years ending on December 31, 1986. The details of the pilot program were published in the Federal Register, dated March 31, 1986.

The Form 8453–F program is limited to Forms 1041 with any of the following attachments:

Schedule D (Form 1041), Capital Gains and Losses
Schedule K–1 (Form 1041), Beneficiary's Share of Income, Deductions, Credits, etc.
Form W–2, Wage and Tax Statement
Form 6251, Alternative Minimum Tax Computation

The Form 8453–P program is limited to Forms 1065 with any of the following attachments:

Schedule D (Form 1065), Capital Gains and Losses
Schedule K (Form 1065), Partners' Shares of Income, Credits, Deductions, etc.
Schedule K–1 (Form 1065), Partner's Share of Income, Credits, Deductions, etc.

ESTIMATED DEDUCTION TABLE

If your Maximum Allowable Deduction is $2,000, use this table to estimate the amount of your contribution which will be deductible. (See page 13 for formula.)

Excess AGI	Deduction	Excess AGI	Deduction	Excess AGI	Deduction	Excess AGI	Deduction	Excess AGI	Deduction
$ 0.00	$2,000.00	$2,000.00	$1,600.00	$4,000.00	$1,200.00	$6,000.00	$800.00	$8,000.00	$400.00
50.00	1,990.00	2,050.00	1,590.00	4,050.00	1,190.00	6,050.00	790.00	8,050.00	390.00
100.00	1,980.00	2,100.00	1,580.00	4,100.00	1,180.00	6,100.00	780.00	8,100.00	380.00
150.00	1,970.00	2,150.00	1,570.00	4,150.00	1,170.00	6,150.00	770.00	8,150.00	370.00
200.00	1,960.00	2,200.00	1,560.00	4,200.00	1,160.00	6,200.00	760.00	8,200.00	360.00
250.00	1,950.00	2,250.00	1,550.00	4,250.00	1,150.00	6,250.00	750.00	8,250.00	350.00
300.00	1,940.00	2,300.00	1,540.00	4,300.00	1,140.00	6,300.00	740.00	8,300.00	340.00
350.00	1,930.00	2,350.00	1,530.00	4,350.00	1,130.00	6,350.00	730.00	8,350.00	330.00
400.00	1,920.00	2,400.00	1,520.00	4,400.00	1,120.00	6,400.00	720.00	8,400.00	320.00
450.00	1,910.00	2,450.00	1,510.00	4,450.00	1,110.00	6,450.00	710.00	8,450.00	310.00
500.00	1,900.00	2,500.00	1,500.00	4,500.00	1,100.00	6,500.00	700.00	8,500.00	300.00
550.00	1,890.00	2,550.00	1,490.00	4,550.00	1,090.00	6,550.00	690.00	8,550.00	290.00
600.00	1,880.00	2,600.00	1,480.00	4,600.00	1,080.00	6,600.00	680.00	8,600.00	280.00
650.00	1,870.00	2,650.00	1,470.00	4,650.00	1,070.00	6,650.00	670.00	8,650.00	270.00
700.00	1,860.00	2,700.00	1,460.00	4,700.00	1,060.00	6,700.00	660.00	8,700.00	260.00
750.00	1,850.00	2,750.00	1,450.00	4,750.00	1,050.00	6,750.00	650.00	8,750.00	250.00
800.00	1,840.00	2,800.00	1,440.00	4,800.00	1,040.00	6,800.00	640.00	8,800.00	240.00
850.00	1,830.00	2,850.00	1,430.00	4,850.00	1,030.00	6,850.00	630.00	8,850.00	230.00
900.00	1,820.00	2,900.00	1,420.00	4,900.00	1,020.00	6,900.00	620.00	8,900.00	220.00
950.00	1,810.00	2,950.00	1,410.00	4,950.00	1,010.00	6,950.00	610.00	8,950.00	210.00
1,000.00	1,800.00	3,000.00	1,400.00	5,000.00	1,000.00	7,000.00	600.00	9,000.00	200.00
1,050.00	1,790.00	3,050.00	1,390.00	5,050.00	990.00	7,050.00	590.00	9,050.00	200.00
1,100.00	1,780.00	3,100.00	1,380.00	5,100.00	980.00	7,100.00	580.00	9,100.00	200.00
1,150.00	1,770.00	3,150.00	1,370.00	5,150.00	970.00	7,150.00	570.00	9,150.00	200.00
1,200.00	1,760.00	3,200.00	1,360.00	5,200.00	960.00	7,200.00	560.00	9,200.00	200.00
1,250.00	1,750.00	3,250.00	1,350.00	5,250.00	950.00	7,250.00	550.00	9,250.00	200.00
1,300.00	1,740.00	3,300.00	1,340.00	5,300.00	940.00	7,300.00	540.00	9,300.00	200.00
1,350.00	1,730.00	3,350.00	1,330.00	5,350.00	930.00	7,350.00	530.00	9,350.00	200.00
1,400.00	1,720.00	3,400.00	1,320.00	5,400.00	920.00	7,400.00	520.00	9,400.00	200.00
1,450.00	1,710.00	3,450.00	1,310.00	5,450.00	910.00	7,450.00	510.00	9,450.00	200.00
1,500.00	1,700.00	3,500.00	1,300.00	5,500.00	900.00	7,500.00	500.00	9,500.00	200.00
1,550.00	1,690.00	3,550.00	1,290.00	5,550.00	890.00	7,550.00	490.00	9,550.00	200.00
1,600.00	1,680.00	3,600.00	1,280.00	5,600.00	880.00	7,600.00	480.00	9,600.00	200.00
1,650.00	1,670.00	3,650.00	1,270.00	5,650.00	870.00	7,650.00	470.00	9,650.00	200.00
1,700.00	1,660.00	3,700.00	1,260.00	5,700.00	860.00	7,700.00	460.00	9,700.00	200.00
1,750.00	1,650.00	3,750.00	1,250.00	5,750.00	850.00	7,750.00	450.00	9,750.00	200.00
1,800.00	1,640.00	3,800.00	1,240.00	5,800.00	840.00	7,800.00	440.00	9,800.00	200.00
1,850.00	1,630.00	3,850.00	1,230.00	5,850.00	830.00	7,850.00	430.00	9,850.00	200.00
1,900.00	1,620.00	3,900.00	1,220.00	5,900.00	820.00	7,900.00	420.00	9,900.00	200.00
1,950.00	1,610.00	3,950.00	1,210.00	5,950.00	810.00	7,950.00	410.00	9,950.00	200.00
								10,000.00	0.00

Excess AGI = Your AGI minus your Threshold Level:
If you are single, your Threshold Level is $25,000.
If you are married, your Threshold Level is $40,000.
If you are married and file a separate tax form, your Excess AGI = your AGI.

Foundations Status of Certain Organizations

Announcement 86–127

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

Aficionados De Golf of Tucson, Inc., Tucson, AZ
Altitude Unlimited, Inc., Boulder, CO
Alvarado Murphy and Assn., Inc., Chicago, IL
American Institute of Banking Austin Chapter, Austin, TX
American-Irish Heritage Foundation of Washington, D.C., Washington, DC
Assistance, Inc., Aurora, CO
Association for the Promotion of New Music, Ship Bottom, NJ
Awareness Americas, Inc., St. Paul, MN
Beebe Hospital Auxiliary, Inc., The, Lewes, DE
Big Bend Manta Ray Swim Team Boosters, Moses Lake, WA
Bread of Life Coffee House, St. Helens, OR
California Community Education Association, Oakland, CA
Calvin Simmons Center for the Performing Arts, Oakland, CA
Camerata Musica, Inc., Wichita, KS
Camerata Society of Lake Forest, Lake Bluff, IL
Camp Kirby For The Deaf, Quakertown, PA
Cathedral Homestead Apartments Housing Development Fund Corporation, New York, NY
Catholic Engaged Encounter of Washington, Seattle, WA
Centers for Gifted and Talented Riverside Center, Williamston, MI
Chemical People Task Force, Inc., Manasquan, NJ
Chicago Academy of Early Music, Chicago, IL
Chicago Center For Learning Disabilities, Chicago, IL
Chicago Federation Union of American Hebrew Congregations Elderly Housing Corp., Chicago, IL
Childbirth Circle, Inc., Suisun City, CA
Citizens United For A Better Community, Williamsport, PA
Clearview PTC, Inc., Washington, MO
Coastal Wool Alliance, Tomales, CA
Community Restitution, San Francisco, CA
Dennis C. Smith Ministries, Inc., Rosemead, CA
Elsa Balman Institute of Music, Inc., Norwalk, CA
Environmental Community Organization, The, Chicago, IL
Equal Rights for Fathers of Alaska, Anchorage, AK
Floating Nile Hospital Foundation, Clifton, VA
Foundation of Medford Roque Rotary, Medford, OR
Freeman Junior Development Program, Dallas, TX
Friends of LaSalle Language Academy Inc., Chicago, IL
Friends of The Elm Grove Library, Elm Grove, WI
Friends of the Spokane Planetarium, Spokane, WA
Friends of The Vaughn Cultural Center, Inc., St. Louis, MO
Friends of the Watts Tower Arts Center, Los Angeles, CA
Friends To The Families, Minneapolis, MN
Fullerton Union School Soccer Booster Club, Fullerton, CA
Great River Players, Inc., Keokuk, IA
Hank O'Donnell Scholarship Fund, Inc., The, Litchfield, CT
Help The Children, Chicago, IL
Hildebrand Villa, Inc., Dover, DE
Historic Lower East Side Neighborhood Association, Inc., Milwaukee, WI
Hmong Womens Assistance Project Association, Seattle, WA
H.O.P.E.S. House for Handicapped, San Diego, CA
Hot Springs Community Theatre, Inc., Hot Springs, SD
International Airline Training Fund of the United States of America, Inc., Rockville, MD
International Mussion Aid, Bellflower, CA
International Union of Biochemistry, Durham, NC
J. Burton Wiley Institute, Morristown, NJ
K Informationa Network, Tacoma, WA
Le Claire Silver Wave Association, Inc., Le Claire, IA
Leeds Community Building, Inc., Leeds, ND
Life Enrichment Foundation, Greenville, DE
Lincoln Consociates for the Performing Arts, Depoe Bay, OR
Livermore Junior Livestock Auction Boosters, Inc., Livermore, CA
Loma Rica-Browns Valley Volunteer Fire Company Inc., Browns Valley, CA
Magdalene Group Care Home, Inc., Kansas City, MO
Matagorda County Community Foundation, Inc., Bay City, TX
McBer Institution, The, Boston, MA
Metropolitan Productions, Inc., Houston, TX
Ministries of New Life, Inc., Leawood, KS
Minn We, Inc., St. Paul, MN
Mong Development, Inc., Chicago, IL
Monmouth Youth Hockey Association, Inc., Rumson, NJ
Mount Zion Human Development Corp., E. St. Louis, IL
National Archives Chicago Branch Birthday Fund, Evanston, IL
National Association of Business Councils Foundation, Inc., San Francisco, CA
National Association of Hispanic Journalists NAHJ, Los Angeles, CA
Nemaha Rescue Team, Nemaha, NE
New York Riding Program for the Handicapped, Inc., New York, NY
NY State Coalition for Criminal Justice Center for Justice Education, Inc., Albany, NY
Oasis R & R Corporation, Inc., Mesa, AZ
Oelwein Railroad Days, Inc., Oelwein, IA
Oregon Scholastic Chess Foundation, Portland, OR
Palmer Creek Fire Association, Healdsburg, CA
Panhandle Indian Center, Inc., Gering, NE
Park Ridge Speed Skating Club, Inc., Park Ridge, IL
Pendleton High School Faculty Scholarship Fund, Pendleton, OR
Powerhouse Productions, Inc., Phoenix, AZ
Raymore Peculiar Athletic Booster Club, Belton, MO
Roosevelt High School Foundation, Des Moines, IA

Rose of Sharon Home, Inc., Nowata, OK
Royal High School Booster Association, Simi Valley, CA
Ruch Community Library, Inc., Jacksonville, OR
Sacramento Council for International Visitors, Sacramento, CA
Sails For The U.S. Constitution Society, Minneapolis, MN
San Bruno Educational Foundation, San Bruno, CA
Scott House, Inc., Sacramento, CA
Scotts Flat Lake Preservation Society, Nevada City, CA
Shana Housing Development Fund Company, Inc., Riverdale, NY
Showcase Productions, Inc., Skokie, IL
Sonrise Outreach World Ministries, Inc., Broken Arrow, OK
Southeast Polk Community Awareness Group, Runnells, IA
Southern Indian Health Council, El Cajon, CA
Terry Hartman Memorial Trust Fund, The, Centerville, OH
Topp-Zillah Senior Transportation Project, Toppenish, WA
Transitional Living Center, Inc., Boise, ID
Two Rivers Area Theatre, Red Lake Falls, MN
Ultimate Players Association, Inc., Mesa, AZ
United Kenai Peninsula Crusade, Soldotna, AK
United Neighborhood Organization, Inc., Carrizo Springs, TX
United Vietnam Veterans Foundation, Philadelphia, PA
Valley County Hospital Foundation, Inc., Cascade, ID
Walnut Creek Historical Society, Walnut Creek, CA
Waterfowl Habitat, Inc., Bloomington, MN
We Care Ministries, Inc., Mesa, AZ
West Suburban Crime Stoppers Program, Inc., West Des Moines, IA
World of Faith Ministry, Dallas, TX
Zurlag Theatre, Chicago, IL

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and address of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletins for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Howard M. Belser	Decatur, AL	Attorney	Three Years from October 9, 1986
Kennard I. Mandell	Wellesley, MA	Attorney	Indefinite from October 1, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any person who has violated the rules and regulations governing the recognition of attorneys, certified public accountants, enrolled agents or enrolled actuaries to practice before the Internal Revenue Service.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been suspended from further practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Paul Adams, Jr.	Bristol, VA	Certified Public Accountant	Indefinite from September 11, 1986

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Leonard Bezark	King of Prussia, PA	Certified Public Accountant	October 19, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR— Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–148, page 4.
Office in the home; security system. Section 280A of the Code will disallow the deduction of business expenses and the recovery deduction attributable to the purchase of a security system by a taxpayer not engaged in a trade or business and, in the case of a security system purchased by a taxpayer engaged in a trade or business, section 280A will limit the deduction of the business expenses and recovery deduction to the gross income attributable to the office in the home.

Rev. Rul. 86–149, page 5.
Inventories; LIFO; real estate developer. Construction costs of completed homes and costs of construction in progress are capital expenditures under section 263 of the Code. Taxpayers cannot inventory such costs under LIFO inventory method. Rev. Rul. 69–536 amplified.

Rev. Rul. 86–150, page 7.
LIFO; price indexes; department stores. The March 1986 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, March 31, 1986.

T.D. 8106, page 8.
Regulations under section 1239 of the Code clarify the proper time for determination of relatedness of the transferor and transferee of depreciable property for purposes of section 1239.

Announcement 86–128, page 22.
Guidance is provided with respect to the application of certain provisions of the built-in gain tax imposed under section 1374 of the Code on S corporations that were formerly C corporations.

EMPLOYMENT TAXES

Announcement 86–122, page 21.
State and local government employers covered by agreements under section 218 of the Social Security Act will be subject to the provisions of the Internal Revenue Code for wages paid after December 31, 1986. Guidance in question and answer form is provided for the rules such employers should follow beginning January 1, 1987.

EXCISE TAXES

Pub. L. 99–662, page 10.
The Harbor Maintenance Revenue Act of 1986 imposes a tax on port use. Also, section 4042 of the Code relating to tax on fuel used in transportation on inland waterways, is amended.

Announcement of Disbarments and Suspensions on page 24.

Department of the Treasury
Internal Revenue Service

T22.23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

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Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 162.—Trade or Business Expenses

26 CFR 1.162–1: Business expenses.

Whether expenses attributable to a security system that protects an office in the home are deductible. See Rev. Rul. 86–148, this page.

Section 167.—Depreciation

26 CFR 1.167–1(a): Depreciation in general.

Whether the depreciation deduction attributable to a security system that protects an office in the home is deductible. See Rev. Rul. 86–148, this page.

Section 168.—Accelerated Cost Recovery System

Whether the recovery deduction attributable to a security system that protects an office in the home is deductible. See Rev. Rul. 86–148, this page.

Section 212.—Expenses For Production of Income

26 CFR 1.212–1: Nontrade or nonbusiness expenses.

Whether the expenses attributable to a security system that protects an office in the home are deductible. See Rev. Rul. 86–148, this page.

Section 263.—Capital Expenditures

26 CFR 1.263(a)–1: Capital expenditures; in general.

Whether a taxpayer engaged in the construction of homes must capitalize the construction cost or may the taxpayer inventory such costs. See Rev. Rul. 86–149, page 5.

Section 280A.—Disallowance Of Certain Expenses In Connection With Business Use Of Home, Rental Of Vacation Homes, Etc.

(Also Sections 162, 167, 168, 212; 26 CFR 1.162–1, 1.167–1, 1.212–1.)

Office in the home; security system. Section 280A of the Code will disallow the deduction of business expenses and the recovery deduction attributable to the purchase of a security system by a taxpayer not engaged in a trade or business and, in the case of a security system purchased by a taxpayer engaged in a trade or business, section 280A will limit the deduction of the business expenses and recovery deduction to the gross income attributable to the office in the home.

Rev. Rul. 86–148

ISSUE

Are the expenses attributable to the purchase and operation of a security system installed in a taxpayer's residence deductible either as trade or business expenses under sections 162 and 168 of the Internal Revenue Code or as expenses for the production of income under sections 212 and 168 of the Code?

FACTS

Situation 1

On January 1, 1986, *A*, an individual, began using an office in *A*'s residence exclusively on a regular basis for managing *A*'s extensive investment portfolio. The investments, consisting primarily of securities, generate substantial income. The square footage of *A*'s office is one-sixth of the total square footage of *A*'s residence.

A's office contains a computer and other office equipment. In order to protect this equipment and the investment certificates kept in the office, *A*, on April 1, 1986, contracted to purchase a central alarm security system. On April 8, 1986, the system was installed in *A*'s home. *A* pays a monthly fee to a security service company to maintain and monitor the system. The security system protects all the doors and windows in *A*'s home.

On *A*'s federal income tax return, *A* intends to deduct as an investment expense one-sixth of the annual recovery deduction allowable under section 168 of the Code and one-sixth of the annual expenses incurred to maintain and monitor the system.

Situation 2

On January 1, 1986, *B*, an individual, opened a dental office in *B*'s residence. The office is used on a regular basis to provide dental care to *B*'s patients and is used exclusively for that purpose. The square footage of *B*'s office is one-sixth of the total square footage of *B*'s residence. On April 1, 1986, *B* contracted to purchase a central alarm system that is the same as *A*'s. On April 8, 1986, the system was installed in *B*'s home. *B* also pays a security service company a monthly fee to maintain and monitor the system. The security system protects all the doors and windows in *B*'s home.

On *B*'s federal income tax return, *B* intends to deduct as a business expense one-sixth of the annual recovery deduction allowable under section 168 of the Code and one-sixth of the annual expenses incurred to maintain and monitor the system.

LAW AND ANALYSIS

Section 162 of the Code provides for the deduction of all ordinary and necessary expenses paid or incurred in carrying on any trade or business.

Section 212 of the Code permits an individual to deduct all the ordinary and necessary expenses paid or incurred for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income.

Section 167(a) of the Code provides that there shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence) of property used in a trade or business, or of property held for the production of income. In general, in the case of recovery property (within the meaning of section 168), the deduction allowable under section 168 shall be deemed to constitute the reasonable allowance provided by section 167.

Section 168(a) of the Code provides that there shall be allowed as a deduction for any taxable year the amount determined under section 168 with respect to recovery property. (For purposes of this revenue ruling, the deduction allowed under section 168 is termed the "recovery deduction.")

Section 168(c)(1) of the Code, subject to the exceptions provided in section 168(e) (which are not relevant here), provides that the term "recovery property" means tangible property of a character subject to the allowance for depreciation that is used in a trade or business or held for the production of income.

Section 280A(a) of the Code provides that, except as otherwise provided in section 280A, in the case of a taxpayer who is an individual or an S corporation, no deduction otherwise allowable will be allowed with respect to the use of a dwelling unit that is used by the taxpayer during the taxable year as a residence.

Section 280A(b) of the Code provides

that section 280(A)(a) will not apply to any deduction allowable to the taxpayer without regard to its connection with the taxpayer's trade or business (or with the taxpayer's income-producing activity).

Section 280A(c)(1) of the Code provides, in part, that section 280A(a) will not apply to any item to the extent such item is allocable to a portion of the dwelling unit that is exclusively used on a regular basis as (A) the principal place of business of any trade or business of the taxpayer, or (B) as a place of business that is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of the taxpayer's trade or business.

S. Rep. No. 94–938, 94th Cong., 2d Sess. 31, 149 (1976), 1976–3 (Vol. 3) C.B. 49, 187, describing the intended scope of section 280A, states that an allocable portion of expenses paid or incurred with respect to the use of a dwelling unit that is used by the taxpayer both as a residence and in connection with income producing activities described in section 212 of the Code will not be allowable as a deduction unless the income producing activity constitutes a trade or business. For example, no deduction is to be allowed if a taxpayer uses a portion of the residence (exclusively on a regular basis) to read financial periodicals and reports, clip bond coupons, and perform similar activities with respect to an investment portfolio, because such investment activities are not a trade or business. *See also Higgins v. Commissioner*, 312 U.S. 212 (1941), 1941–1 C.B. 339, in which the Supreme Court held that an investor's management of the investor's own investments, no matter how continuous or extensive, did not constitute a trade or business.

If an activity carried on in a portion of a dwelling unit meets one of the "use exceptions" provided in section 280A(c) of the Code (including use in a trade or business described in section 280A(c)(1)(A) or (B)), expenses attributable to that use of that portion of the dwelling unit may be deducted. In calculating what expenses are attributable to a use in a trade or business described in section 280A(c)(1)(A) or (B), the taxpayer may use any method of allocation that is reasonable under the circumstances.

Under section 280A(c)(5), the deductions allowed by reason of being attributable to a use that qualifies under section 280A(c)(1)(A) or (B) may not exceed the amount by which the gross income derived from that use of the dwelling unit for the taxable year exceeds the deductions (for example, interest and taxes) allocable to that use that are allowable for the taxable year whether or not the dwelling unit was so used.

In *Situation 1*, because *A*'s investment activities do not constitute a trade or business, expenses attributable to the residential security system are deductible only to the extent, if any, that they are deductible without regard to *A*'s income producing activity. *See* Section 280A(b). Because the recovery deduction and the monthly maintenance fee are not deductible without regard to the existence of *A*'s income producing activity, no portion of those items is deductible by *A*.

In *Situation 2*, because *B* uses the office in *B*'s residence exclusively on a regular basis to meet with patients in the normal course of *B*'s trade or business as a dentist, expenses allocable to the office are deductible, subject to the limitation of section 280A(c)(5). Because the security system protects every doorway and window of *B*'s residence, and because the square footage of the office is one-sixth of the total square footage of *B*'s residence, it was reasonable for *B* to use square footage as the basis for allocating the recovery deduction and the monthly maintenance fee that *B* paid for the security system. Accordingly, one-sixth of the recovery deduction and one-sixth of the monthly fee attributable to the security system is allocable to the office.

HOLDING

In *Situation 1*, no portion of the recovery deduction otherwise allowable under section 168 and the monthly maintenance fee that *A* paid for the security system is deductible under section 280A(a) of the Code because *A*'s investment activity is not a "trade or business."

In *Situation 2*, one-sixth of the recovery deduction otherwise allowable under section 168 and one-sixth of the monthly maintenance fee *B* paid for the security system are deductible, but only to the extent that the gross income derived from *B*'s business use of the office for the taxable year exceeds the deductions that are allocable to that use and are allowable for the taxable year whether or not the residence was so used.

Section 446.—General Rule for Methods of Accounting

26 CFR 1.446–1: General rule for methods of accounting.

Whether a taxpayer can use the last-in, first-out inventory method of accounting for the costs of its completed homes and homes under construction. See Rev. Rul. 86–149, below.

Section 471.—General Rule for Inventories

26 CFR 1.471–1: General rule for inventories.
(Also Sections 263, 446, 472; 1.263(a)–1, 1.446–1, 1.472–1.)

Inventories; LIFO; real estate developer. Construction costs of completed homes and costs of construction in progress are capital expenditures under section 263 of the Code. Taxpayers cannot inventory such costs under LIFO inventory method. Rev. Rul. 69–536 amplified.

Rev. Rul. 86–149

ISSUE

Whether a taxpayer engaged in the business of developing real estate may use the last-in, first-out (LIFO) inventory identification method in accounting for the costs of its completed homes and homes under construction, exclusive of land costs?

FACTS

The taxpayer is a real estate developer that keeps its books and records and files its federal income tax returns on an accrual method of accounting. Its principal business activity is developing real estate upon which it constructs residential homes.

The taxpayer uses an accumulated "job cost" method to account for its construction and development costs. Under this method, each home is treated as a separate costing unit to which all direct identifiable costs are charged and all overhead costs, including the variable overhead as well as the construction and architectural costs, are allocated. All costs that have been accumulated for a particular home under the job cost method are charged to cost of sales at the time of settlement with the purchaser of the home.

With its federal income tax return filed for the year ended 1984, the taxpayer filed a timely Form 970, Application to Use LIFO Inventory Method, for its "inventory" of completed new homes and jobs in progress. The cost of its building lots, including the various development costs of improving the lots such as streets, curbs and gutters, were not included in the application to use the LIFO method.

LAW AND ANALYSIS

Section 263(a)(1) of the Internal Revenue Code and section 1.263(a)–1(1) of the Income Tax Regulations provides that no deductions shall be allowed for any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate.

Section 1.263(a)–2 of the regulations sets forth examples of capital expenditures, including the cost of acquisition, construction, or erection of buildings, machinery and equipment, furniture and fixtures, and similar property having a useful life substantially beyond the tax year.

Section 446(a) of the Code states the general rule that taxable income shall be computed by a taxpayer under the method of accounting it regularly uses in keeping its books. Section 446(b), however, provides that where a taxpayer's accounting method does not clearly reflect income, the computation of taxable income shall be made under such method as, in the Secretary's opinion, does clearly reflect income.

Section 471 of the Code provides that whenever in the opinion of the Secretary the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer on such basis as the Secretary may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting income.

Section 472(a) of the Code allows a taxpayer to use the LIFO method in inventorying goods specified in an application to use such method filed at such time and in such manner as the Secretary may prescribe.

Section 1.471–1 of the regulations provides that inventories at the beginning and end of each tax year are necessary in every case in which the production, purchase or sale of merchandise is an income-producing factor.

Section 1.472–1(a) of the regulations provides that any taxpayer permitted or required to take inventories pursuant to the provisions of section 471 of the Code may elect with respect to those goods specified in its application and properly subject to inventory to compute its opening and closing inventories in accordance with the method provided by section 472.

Whether a real estate developer may use the LIFO method to account for the costs of its completed homes and jobs in progress is dependent upon whether the taxpayer is required or permitted to maintain inventories with respect to these costs. Historically, taxpayers engaged in the real estate business have not been permitted to inventory real estate held for sale to customers. *Atlantic Coast Realty Co. v. Commissioner*, 11 B.T.A. 416 (1928); Rev. Rul. 69–536, 1969–2 C.B. 109. In *Atlantic Coast Realty Co.*, the United States Board of Tax Appeals concluded that, based on the purpose and legislative intent of the inventory provisions, the use of inventories is inappropriate for a taxpayer engaged in buying and selling lands. As stated by the Board of Tax Appeals on page 419:

> The use of inventories must be reasonably necessary to the determination of income. The basis of their use must be prescribed by the Commissioner, not arbitrarily, but in conformity to the best accounting practice in the trade or business and as most clearly reflecting income. The language indicates no intention to recognize in any trade a new method of determining income or a new limitation upon income, but only a recognition of the use of inventories in such trades or businesses, like "manufacturing and merchandise concerns" as had been found to require such accounting practice.

Unlike a manufacturing or merchandise concern, the use of inventories for the valuation of either unimproved land or developed real estate is unnecessary for the determination of income and generally impractical as a method to value real estate. *See Atlantic Coast Realty Co.* Real estate is unique and is particularly subject to specific accounting of costs including the tracing of costs to individual parcels and the separate computations of gains or losses on sales. *See* for example, Rev. Rul. 66–247, 1966–2 C.B. 198, which states that capitalized costs incurred in the construction of a house for speculative sale should be applied against the amount realized upon the sale of the house for purposes of determining gain or loss.

Instead of being a more convenient method of accounting, as it is with large stocks of merchandise, an inventory method for real estate could be so cumbersome and uncertain as to be generally impractical. *Atlantic Coast Realty Co.* For this reason, neither the land nor the materials and supplies used to construct the houses on the lots are considered merchandise or goods within the meaning of section 471 of the Code and its regulations. *See Homes by Ayres v. Commissioner*, 795 F. 2d 832 (9th Cir. 1986), *aff'g* T.C.M. 1984–475; *W. C. & A. N. Miller Development Co. v. Commissioner*, 81 T.C. 619 (1983); *see also Francisco Sugar Co. v. Commissioner*, 47 F. 2d 555 (2nd Cir. 1931), *aff'g in part* 14 B.T.A. 1062 (1929). Instead, the property and its improvements constitute real estate held for sale by the taxpayer. *See* section 263(a)(1).

In the instant situation, therefore, the taxpayer is neither permitted nor required to maintain inventories. Its job order cost method for accumulating the costs of its completed but unsold homes and construction in progress is not an inventory method but a capitalization method even though it may approximate the results of a specific identification inventory method. *W.C. & A.N. Miller Development Co.* As stated by the United States Tax Court in *W.C. & A.N. Miller Development Co.* on pages 632 and 633:

> There is a fundamental difference between capitalization and an inventory method. Under capitalization, gain will be determined pursuant to section 1001 on each individual home when it is sold, and such gain is to be determined based generally on the taxpayer's actual cost for that particular home. Since the specific identification method of inventory valuation is only one of several permissible inventory methods, there is not necessarily the requirement under this method that actual cost be used in arriving at cost of goods sold.

Thus, the Tax Court held that a seller of homes cannot maintain inventories.

A taxpayer engaged in the real estate business capitalizes its costs in accordance with section 263 of the Code. Under section 263(a)(1), costs incurred in the construction of homes and other permanent improvements to real property are not currently deductible. Instead the cost of unsold homes and construction in progress is capital expenditure that becomes part of the cost of the real estate, which, in turn, is recovered either through a depreciation allowance if the property is used in a trade or business, or as an offset against the price received in the subsequent sale or disposition of such property.

By utilizing the LIFO method of inventory accounting for its completed but unsold houses and costs of construction in progress, the taxpayer may be, in effect, deducting a portion of its construction costs before it has actually disposed of the real property. For example, as con-

struction costs increase, the LIFO method will produce a cost of goods sold deduction in excess of the cost specifically attributable to the particular real property actually disposed of during the year and in effect the taxpayer will be currently deducting the cost of improving other real property prior to its sale. Thus, as a consequence of utilizing the LIFO inventory method in conjunction with its job order cost method, the taxpayer is selectively combining attributes of both an inventory method and a capitalization method with a resulting distortion of income within the meaning of section 446(b) of the Code.

HOLDING

A taxpayer engaged in the business of developing real estate may not use the LIFO inventory identification method to account for its completed homes and homes under construction, exclusive of land costs.

Any change from the taxpayer's present method of accounting for its construction costs to the method described in this revenue ruling is a change in method of accounting to which sections 446 and 481 of the Code and the regulations thereunder apply.

This ruling is identified as a designated ruling pursuant to section 5.12(2) of Rev. Proc. 84–74, 1984–2 C.B. 736.

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 69–536, 1962–2 C.B. 109 amplified.

Section 472.—Last-in, First-out Inventories

26 CFR 1.472–1: Last-in, first-out inventories.

LIFO; price indexes; department stores. The March 1986 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, March 31, 1986.

Rev. Rul. 86–150

The following price indexes for March 1986 were issued by the Bureau of Labor Statistics on April 24, 1986, for use by department stores, and are accepted by the Internal Revenue Service, under section 1.472–1(k) of the Income Tax Regulations and Rev. Proc. 72–21, 1972–1 C.B. 745, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, March 31, 1986.

Indexes are prepared on a national basis for the store total, for 23 major groups of departments, and for three special combinations—soft goods, durable goods and miscellaneous goods. The store total index covers all departments, including

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS
(January 1941 = 100 unless otherwise noted)

	March 1985	March 1986	Percentage Change from March 1985 to March 1986[1]
1. Piece Goods	392.6	404.2	3.0
2. Domestics and Draperies	547.8	558.9	2.0
3. Women's and Children's Shoes	551.9	529.4	−4.1
4. Men's Shoes	711.9	718.5	0.9
5. Infants' Wear	498.5	523.8	5.1
6. Women's Underwear	430.3	432.3	0.5
7. Women's and Girls' Hosiery	236.2	237.5	0.6
8. Women's and Girls' Accessories	440.6	450.3	2.2
9. Women's Outerwear and Girls' Wear	351.4	340.6	−3.1
10. Men's Clothing	465.9	470.1	0.9
11. Men's Furnishings	477.4	478.1	0.1
12. Boys' Clothing and Furnishings	432.4	436.0	0.8
13. Jewelry	692.3	660.7	−4.6
14. Notions	485.2	472.6	−2.6
15. Toilet Articles and Drugs	631.7	659.1	4.3
16. Furniture and Bedding	530.9	540.9	1.9
17. Floor Coverings	465.1	460.3	−1.0
18. Housewares	717.5	713.5	−0.6
19. Major Appliances	242.8	245.7	1.2
20. Radio and Television	107.3	100.8	−6.1
21. Recreation and Education	N/A	99.2	N/A
22. Home Improvements	N/A	99.3	N/A
23. Auto Accessories	N/A	99.6	N/A
Groups 1–15: Soft Goods	478.1	478.4	0.1
Groups 16–20: Durable Goods	445.8	445.3	−0.1
Groups 21–23: Misc. Goods	N/A	99.3	N/A
Store Total	469.0	468.2	−0.2

[1] Absence of a minus sign before percentage change in this column signifies price increase

some not listed separately, with the following exceptions: candy, foods, liquor, tobacco, as well as contract departments.

The major groups of departments for which indexes are prepared have been expanded from 20 to 23. These new groups are: (1) Group 21—Recreation and Education; (2) Group 22—Home Improvements; and (3) Group 23—Auto Accessories. A Miscellaneous Goods index is also introduced to reflect the aggregate movement of these three new groups. *See* Rev. Proc. 86–46, 1986–50, I.R.B. 6.

Although the new indexes were introduced in the February 1986 Department Store Inventory Price Indexes, January 1987 will be the first month for which there will be a percent change based on a 12-month period. The January 1986 indexes for the new groups are all 100. Rev. Proc. 86–46 modifies and supersedes Rev. Proc. 72–21.

Rev. Proc. 86–47, 1986–50 I.R.B. 8, sets forth the procedures required of taxpayers to change their method of accounting from that of using the 20 groups set forth in Rev. Proc. 72–21 to the method of using the 23 groups set forth in Rev. Proc. 86–46.

26 CFR 1.472–1: Last-in, first-out inventories.

Whether a real estate developer can use the last-in, first-out inventory method of accounting with respect to construction cost of completed homes and construction in progress. See Rev. Rul. 86–149, page 5.

Section 1239.—Gain from Sale of Depreciable Property Between Related Taxpayers

26 CFR 1.1239–1: Gain from sale or exchange of depreciable property between certain related taxpayers after October 4, 1976.

T.D. 8106

TITLE 26.—INTERNAL REVENUE—CHAPTER I, SUBCHAPTER A, PATR 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1983

Income Taxes; Time for Determining Relationship of Persons Transferring Depreciable Property

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations under section 1239 which clarify the proper time for determination of the relatedness of the transferor and transferee of depreciable property for purposes of section 1239. These final regulations provide the public with guidance as to the proper time for determining relatedness under section 1239. This amendment does not reflect amendments to section 1239 made by the Installment Sales Revision Act of 1980, the Technical Corrections Act of 1982 and the Tax Reform Act of 1984.

EFFECTIVE DATE: The regulations are effective for transfers after January 6, 1983.

FOR FURTHER INFORMATION CONTACT: Robert Beatson of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC 20224 (Attention: CC:LR:T) (202-566-3459).

SUPPLEMENTARY INFORMATION: BACKGROUND

On January 6, 1983, the **Federal Register** published proposed amendments (48 FR 667) to the Income Tax Regulations (26 CFR Part 1) under section 1239 of the Internal Revenue Code of 1954 [1983–1 C.B. 989]. One comment was received regarding this proposal. A public hearing was neither requested nor held. After consideration of this comment, these amendments are adopted as revised by this Treasury Decision.

EXPLANATION OF PROVISIONS

Section 1239 disallows capital gains treatment on the sale or exchange of depreciable property between related taxpayers as defined in section 1239(b). This section is designed to prevent the immediate payment of a capital gains tax in return for the elimination over a period of years of income taxes on an equivalent amount of ordinary income as a result of the additional depreciation deduction allowable on the increased basis of the transferred property.

PUBLIC COMMENT

The proposed amendments to section 1239 state that a taxpayer and an entity are considered related if there is 80-percent ownership before or immediately after the sale or exchange of depreciable property. This rule does not make any distinction between whether the selling party is the shareholder or the corporation. Additionally, the proposed amendments state that where there is a sale or exchange between two entities, there is relatedness if a shareholder has 80-percent ownership (either actual or constructive ownership) of the transferor before the sale or exchange of depreciable property and the same shareholder has 80-percent ownership (either actual or constructive ownership) of the transferee immediately after the sale or exchange of depreciable property.

The commentator noted that the appropriate time for determining whether a person and a controlled entity are "related persons" when the person sells property to or exchanges property with the entity should be immediately after the sale or exchange of the property. After consideration of this comment, the final regulations provide that when a person sells property to or exchanges property with a controlled entity, the proper time for determining relatedness is immediately after the sale or exchange. Thus, the holding in *Robishaw* v. *United States*, 616 F.2d 507 (Ct. Cl. 1980) is not followed. The commentator further suggested that the appropriate time for determining whether a person and a controlled entity are "related persons" when the entity sells property to or exchanges property with the person should be before the sale or exchange of the property. After consideration of this comment, it has not been adopted since it is believed that abusive situations may result under such a rule. Thus, when a controlled entity sells property to or exchanges property with a person, the time for determining relatedness is immediately before or immediately after the sale or exchange of the depreciable property.

The final regulations also do not adopt the proposed example.

REGULATORY FLEXIBILITY ACT

Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

NON-APPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis therefore is not required.

DRAFTING INFORMATION

The principal author of this final regulation is Robert Beatson of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulation both on matters of substance and style.

* * * * *

Adoption of amendments to the regulations

Accordingly, 26 CFR Part 1 is amended as follows:

PART 1—[AMENDED]

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 2. Section 1.1239–1 is amended by redesignating paragraph (c)(3) as (c)(5) and adding new paragraphs (c)(3) and (c)(4). New paragraphs (c)(3) and (c)(4) read as follows:

§1.1239–1 Gain from sale or exchange of depreciable property between certain related taxpayers after October 4, 1976.

* * * * *

(c) *Rules of construction.* * * *

(3) *Relationship determination for transfers made after January 6, 1983—taxpayer and an 80-percent owned entity.* For purposes of paragraph (b)(2) of this section with respect to transfers made after January 6, 1983—

(i) If the transferor is an entity, the transferee and such entity are related if the entity is an 80-percent owned entity with respect to such transferee either immediately before or immediately after the sale or exchange of depreciable property, and

(ii) If the transferor is not an entity, the transferee and such transferor are related if the transferee is an 80-percent owned entity with respect to such transferor immediately after the sale or exchange of depreciable property.

(4) *Relationship determination for transfers made after January 6, 1983—two 80-percent owned entities.* For purposes of paragraph (b)(3) of this section, with respect to transfers made after January 6, 1983, two entities are related if the same shareholder both owns 80 percent or more in value of the stock of the transferor before the sale or exchange of depreciable property and owns 80 percent or more in value of the stock of the transferee immediately after the sale or exchange of depreciable property.

* * * * *

James I. Owens,
Acting Commissioner of Internal Revenue.

Approved: November 14, 1986.

J. Roger Mentz,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on November 25, 1986, 8:45 a.m., and published in the issue of the Federal Register for November 26, 1986, 51 F.R. 42835)

Subpart B.—Legislation and Related Committee Reports

Public Law 99–662
99th Congress H.R. 6[1]
November 17, 1986:

An Act to provide for the conservation and development of water and related resources and the improvement and rehabilitation of the Nation's water resources infrastructure.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled.

SECTION 1. This Act may be cited as the "Water Resources Development Act of 1986."

* * * * *

Title XIV—Revenue Provisions

SEC. 1401. SHORT TITLE.

This title may be cited as the "Harbor Maintenance Revenue Act of 1986."

SEC. 1402. IMPOSITION OF HARBOR MAINTENANCE TAX.

(a) General Rule.—Chapter 36 of the Internal Revenue Code of 1954 (relating to certain other excise taxes) is amended by inserting after the chapter heading the following new subchapter.

"Subchapter A—Harbor Maintenance Tax

"Sec. 4461. Imposition of tax.
"Sec. 4462. Definitions and special rules.

"SEC. 4461. IMPOSITION OF TAX.

"(a) General Rule.—There is hereby imposed a tax on any port use.

"(b) Amount of Tax.—The amount of the tax imposed by subsection (a) on any port use shall be an amount equal to 0.04 percent of the value of the commercial cargo involved.

"(c) Liability and Time of Imposition of tax.—

"() Liability.—The tax imposed by subsection (a) shall be paid by—

"(A) in the case of cargo entering the United States, the importer,

"(B) in the case of cargo to be exported from the United States, the exporter, or

"(C) in any other case, the shipper.

"(2) Time of Imposition.—Except as provided by regulations, the tax imposed by subsection (a) shall be imposed—

"(A) in the case of cargo to be exported from the United States, at the time of loading, and

"(B) in any other case, at the time of unloading.

"SEC. 4462. DEFINITIONS AND SPECIAL RULES.

"(a) Definitions.—For purposes of this subchapter—

"(1) Port Use.—The term 'port use' means—

"(A) the loading of commercial cargo on, or

"(B) the unloading of commercial cargo from, a commercial vessel at a port.

"(2) Port.—

"(A) In general.—The term 'port' means any channel or harbor (or component thereof) in the United States, which—

"(i) is not an inland waterway, and

"(ii) is open to public navigation.

"(B) Exception for certain facilities.—The term 'port' does not include any channel or harbor with respect to which no Federal funds have been used since 1977 for construction, maintenance, or operation, or which was deauthorized by Federal law before 1985.

"(C) Special rule for Columbia River.—The term 'port' shall include the channels of the Columbia River in the States of Oregon and Washington only up to the downstream side of Bonneville lock and dam.

"(3) Commercial cargo.—

"(A) In general.—The term 'commercial cargo' means any cargo transported on a commercial vessel, including passengers transported for compensation or hire.

"(B) Certain items not included.—The term 'commercial cargo' does not include—

"(i) bunker fuel, ship's stores, sea stores, or the legitimate equipment necessary to the operation of a vessel, or

"(ii) fish or other aquatic animal life caught and not previously landed on shore.

"(4) Commercial vessel.—

"(A) In general.—The term 'commercial vessel' means any vessel used—

"(i) in transporting cargo by water for compensation or hire, or

"(ii) in transporting cargo by water in the business of the owner, lessee, or operator of the vessel.

"(B) Exclusion of ferries.—

"(i) In general.—The term 'commercial vessel' does not include any ferry engaged primarily in the ferrying of passengers (including their vehicles) between points within the United States, or between the United States and contiguous countries.

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[1] House Report No. 99–251 Part III, page 13, and Conference Report No. 1013, page 17.

"(ii) Ferry.—The term 'ferry' means any vessel which arrives in the United States on a regular schedule during its operating season at intervals of at least once each business day.

"(5) Value.—

"(A) In general.—The term 'value' means, except as provided in regulations, the value of any commercial cargo as determined by standard commercial documentation.

"(B) Transportation of passengers.—In the case of the transportation of passengers for hire, the term 'value' means the actual charge paid for such service or the prevailing charge for comparable service if no actual charge is paid.

"(b) Special Rule for Alaska, Hawaii, and Possessions.—

"(1) In general.—No tax shall be imposed under section 4461(a) with respect to—

"(A) cargo loaded on a vessel in a port in the United States mainland for transportation to Alaska, Hawaii, or any possession of the United States for ultimate use of consumption in Alaska, Hawaii or any possession of the United States.

"(B) cargo loaded on a vessel in Alaska, Hawaii, or any possession of the United States for transportation to the United States mainland for ultimate use or consumption in the United States mainland.

"(C) the unloading of cargo described in subparagraph (A) or (B) in Alaska, Hawaii, or any possession of the United States, or in the United States mainland, respectively, or

"(D) cargo loaded on a vessel in Alaska, Hawaii, or a possession of the United States and unloaded in the State or possession in which loaded.

"(2) Cargo does not include crude oil with respect to Alaska.—For purposes of this subsection, the term 'cargo' does not include crude oil with respect to Alaska.

"(3) United States mainland.—For purposes of this subsection, the term "United States mainland" means the continental United States (not including Alaska).

"(c) Coordination of Tax Where Transportation Subject to Tax Imposed by Section 4042.—No tax shall be imposed under this subchapter with respect to the loading or unloading of any cargo on or from a vessel if any fuel of such vessel has been (or will be) subject to the tax imposed by section 4042 (relating to tax on fuel used in commercial transportation on inland waterways).

"(d) Nonapplicability of Tax To Certain Cargo.—

"(1) In General.—Subject to paragraph (2), the tax imposed by section 4461(a) shall not apply to bonded commercial cargo entering the United States for transportation and direct exportation to a foreign country.

"(2) Imposition of charges.—Paragraph (1) shall not apply to any cargo exported to Canada or Mexico—

"(A) during the period—

"(i) after the date on which the Secretary determines that the Government of Canada or Mexico (as the case may be) has imposed a substantially equivalent tax, fee, or charge on commercial vessels or commercial cargo utilizing ports of such country, and

"(ii) subject to subparagraph (B), before the date on which the Secretary determines that such tax, fee, charge has been discontinued by such country, and

"(B) with respect to a particular United States port (or to any transaction or class of transactions at any such port) to the extent that the study made pursuant to section 1407(a) of the Water Resources Development Act of 1986 (or a review thereof pursuant to section 1407(b) of such Act) finds that—

"(i) the imposition of the tax imposed by this subchapter at such port (or to any transaction or class of transactions at such port) is not likely to divert a significant amount of cargo from such port to a port in a country contiguous to the United States, or that any such diversion is not likely to result in significant economic loss to such port, or

"(ii) the nonapplicability of such tax at such port (or to any transaction or class of transactions at such port) is likely to result in significant economic loss to any other United States port.

"(e) Exemption for United States.—No tax shall be imposed under this subchapter on the United States or any agency or instrumentality thereof.

"(f) Extension of Provisions of Law Applicable to Customs Duty.—

"(1) In general.—Except to the extent otherwise provided in regulations, all administrative and enforcement provisions of customs laws and regulations shall apply in respect of the tax imposed by this subchapter (and in respect of persons liable therefor) as if such tax were a customs duty. For purposes of the preceding sentence, any penalty expressed in terms of a relationship to the amount of the duty shall be treated as not less than the amount which bears a similar relationship to the value of the cargo.

"(2) Jurisdiction of courts and agencies.—For purposes of determining the jurisdiction of any court of the United States or any agency of the United States, the tax imposed by this subchapter shall be treated as if such tax were a customs duty.

"(3) Administrative provisions applicable to tax law not to apply.—The tax imposed by this subchapter shall not be treated as a tax for purposes of subtitle F or any other provision of law relating to the administration and enforcement of internal revenue taxes.

"(g) Special Rules.—Except as provided by regulations—

"(1) Tax imposed only once.—Only 1 tax shall be imposed under section 4461(a) with respect to the loading on and unloading from, or the unloading from and the loading on, the same vessel of the same cargo.

"(2) Exception for intraport movements.—Under regulations, no tax shall be imposed under section 4461(a) on the mere movement of cargo within a port.

"(h) Regulations.—The Secretary may prescribe such additional regulations as may be necessary to carry out the purposes of this subchapter including, but not limited to, regulations—

"(1) providing for the manner and method of payment and collection of the tax imposed by this subchapter,

"(2) providing for the posting of bonds to secure payment of such tax,

"(3) exempting any transaction or class of transactions from such tax where the collection of such tax is not administratively practical, and

"(4) providing for the remittance or mitigation of penalties and the settlement or compromise of claims."

(b) Clerical Amendment.—The table of subchapters for chapter 36 of the Internal Revenue Code of 1954 is amended by inserting the following before the item relating to subchapter D:

"Subchapter A. Harbor maintenance tax."

(c) Effective Date.—The amendments made by this section shall take effect on April 1, 1987.

SEC. 1403. CREATION OF HARBOR MAINTENANCE TRUST FUND.

"(a) In General.—Subchapter A of chapter 98 of the Internal Revenue Code of 1954 (relating to establishment of trust funds) is amended by adding after section 9504 the following new section:

"SEC. 9505. HARBOR MAINTENANCE TRUST FUND.

"(a) Creation of Trust Fund.—There is hereby established in the Treasury of the United States a trust fund to be known as the 'Harbor Maintenance Trust Fund," consisting of such amounts as may be—

"(1) appropriated to the Harbor Maintenance Trust Fund as provided in this section,

"(2) transferred to the Harbor Maintenance Trust Fund by the Saint Lawrence Seaway Development Corporation pursuant to section 13(a) of the Act of May 13, 1954, or

"(3) credited to the Harbor Maintenance Trust Fund as provided in section 9602(b).

"(b) Transfer to Harbor Maintenance Trust Fund of Amounts Equivalent to Certain Taxes.—There are hereby appropriated to the Harbor Maintenance Trust Fund amounts equivalent to the taxes received in the Treasury under section 4461 (relating to harbor maintenance tax).

"(c) Expenditures From Harbor Maintenance Trust Fund.—Amounts in the Harbor Maintenance Trust Fund shall be available, as provided by appropriation Acts, for making expenditures—

"(1) to carry out section 210(a) of the Water Resources Development Act of 1986 (as in effect on the date of enactment of this section),

"(2) for payments of rebates of tolls or charges pursuant to section 13(b) of the Act of May 13, 1954 (as in effect on April 1, 1987), and

"(3) for the payment of all expenses of administration incurred—

"(A) by the Department of the Treasury in administering subchapter A of chapter 36 (relating to harbor maintenance tax), but not in excess of $5,000,000 for any fiscal year, and

"(B) for periods during which no fee applies under paragraph (9) or (10) or section 13031(a) of the Consolidated Omnibus Budget Reconciliation Act of 1985."

(b) Authorization of Appropriations.—There are authorized to be appropriated to the Department of the Treasury (from the fees collected under paragraphs (9) and (10) of section 13031(a) of the Consolidated Omnibus Budget Reconciliation Act of 1985) such sums as may be necessary to pay all expenses of administration incurred by such Department in administering subchapter A of chapter 36 of the Internal Revenue Code of 1954 for periods to which such fees apply.

(c) Clerical Amendment.—The table of sections for subchapter A of chapter 98 of the Internal Revenue Code of 1954 as amended by adding after the item relating to section 9504 the following new item:

"Sec. 9505. Harbor Maintenance Trust Fund."

(d) Effective Date.—The amendments made by this section shall take effect on April 1, 1987.

SEC. 1404. INLAND WATERWAYS TAX.

(a) In General.—Subsection (b) of section 4042 of the Internal Revenue Code of 1954 (relating to tax on fuel used in commercial transportation on inland waterways) is amended to read as follows:

"(b) Amount of Tax.—The tax imposed by subsection (a) shall be determined from the following table:

If the use occurs:	The tax per gallon is:
Before 1990	10 cents
During 1990	11 cents
During 1991	13 cents
During 1992	15 cents
During 1993	17 cents
During 1994	19 cents
After 1994	20 cents

(b) Fuel Use on Tennessee-Tombigbee Waterway Subject to Inland Waterway Tax.—Section 206 of the Inland Waterways Revenue Act of 1978 is amended by adding at the end thereof the following:

"(27) Tennessee-Tombigbee Waterway: From its confluence with the Tennessee River to the Warrior River at Demopolis, Alabama."

(c) Effective Date.—The amendments made by this section shall take effect on January 1, 1987.

SEC. 1405. INLAND WATERWAYS TRUST FUND.

(a) In General.—Subchapter A of chapter 98 of the Internal Revenue Code of 1954 (relating to establishment of trust fund(s) is amended by adding after section 9505 the following new section:

"SEC. 9506. INLAND WATERWAYS TRUST FUND.

"(a) Creation of Trust Fund.—There is hereby established in the Treasury of the United States a trust fund to be known as the 'Inland Waterways Trust Fund', consisting of such amounts as may be appropriated or credited to such Trust Fund as provided in this section or section 9602(b).

"(b) Transfer to Trust Fund of Amounts Equivalent to Certain Taxes.—There are hereby appropriated to the Inland Waterways Trust Fund amounts equivalent to the taxes received in the Treasury under section 4042 (relating to tax on fuel used in commercial transportation on inland waterways).

"(c) Expenditures From Trust Fund.—

"(1) In general.—Except as provided in paragraph (2), amounts in the Inland Waterways Trust Fund shall be available, as provided by appropriation Acts, for making construction and rehabilitation expenditures for navigation on the inalnd and coastal waterways of the United States described in section 206 of the Inland Waterways Revenue Act of 1978, as in effect on the date of the enactment of this section.

"(2) Exception for certain projects.—Not more than ½ of the cost of any construction to which section 102(a) of the Water Resources Development Act of 1986 applies (as in effect on the date of the enactment of this section) may be paid from the Inland Waterways Trust Fund."

(b) Conforming Amendments.—Sections 203 and 204 of the Inland Waterways Revenue Act of 1978 (relating to Inland Waterways Trust Fund) are hereby repealed.

(c) Clerical Amendment.—The table of sections for subchapter A of chapter 98 of the Internal Revenue Code of 1954 is amended by adding at the end thereof the following new item:

"Sec. 9506. Inland Waterways Trust Fund."

(d) Effective Date.—

(1) In general.—The amendments made by this section shall take effect on January 1, 1987.

(2) Inland waterways trust fund treated as continuation of old trust fund.—The Inland Waterways Trust Fund established by the amendments made by

this section shall be treated for all purposes of law as a continuation of the Inland Waterways Trust Fund established by section 203 of the Inland Waterways Revenue Act of 1978. Any reference in any law to the Inland Waterways Trust Fund established by such section 203 shall be deemed to include (wherever appropriate) a reference to the Inland Waterways Trust Fund established by this section.

* * * * *

House of Representatives
Report No. 99–251 Part III
1st Session
[Bracketed numerals indicate official report page numbers]

PORT REVENUE ACT OF 1985

SEPTEMBER 23, 1985

Mr. Rostenkowski, from the Committee on Ways and Means, submitted the following Report To accompany H.R. 6[1]

The Committee on Ways and Means, to whom was referred the bill (H.R. 6) to provide for the conservation and development of water and related resources and the improvement and rehabilitation of the Nation's water resources infrastructure, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

* * * * *

[7] I. SUMMARY

A. Background of Legislation

H.R. 6 (the "Water Resources Conservation, Development and Infrastructure Improvement and Rehabilitation Act of 1985") was ordered reported on June 26, 1985, by the Committee on Public Works and Transportation. The bill was reported on August 1, 1985 (H. Rep. No. 99–251, Part 1), and was referred to the Committee on Interior and Insular Affairs for a period ending not later than September 5, 1985 (later extended to September 16, 1985), to the Committee on Merchant Marine and Fisheries for a period ending not later than September 15, 1985 (later extended to September 23, 1985), and to the Committee on Ways and Means for a period ending not later than September 23, 1985.

H.R. 6 was reported with amendments, by the Committee on Interior and Insular Affairs on September 16, 1985 (H. Rep. 99–251, Part 2). The Committee on Merchant Marine and Fisheries ordered H.R. 6 reported, with amendments, on September 12, 1985.

The Committee on Ways and Means held a public hearing on H.R. 6 on September 5, 1985, and ordered the bill favorably reported with an amendments on September 18, 1985.

B. Committee on Ways and Means Amendment

Port Use Tax and Trust Fund

Port use tax

The Committee amendment imposes a new 0.04 percent (4 cents per $100) excise tax on the value of commercial cargo loaded onto or unloaded from a commercial vessel at a port in the United States.

The port use tax does not apply to cargo when loaded or unloaded at ports in Hawaii or any possession of the United States; also, the tax does not apply to cargo when loaded on a vessel at any port in the United States for transportation to Hawaii or a U.S. possession for ultimate use of consumption in Hawaii or the possession. If the cargo loaded in Hawaii or a U.S. possession is unloaded at a port in the United States, then the port use tax applies when the cargo is so unloaded.

The tax does not apply to fish or other aquatic animal life caught during a voyage. Also, the tax does not apply to the United States Government or any Federal agency or instrumentality.

The port use tax does not apply to cargo where the transportation of that cargo has been (or will be) subject to the excise tax on diesel or other fuels used on the inland waterways under Code section 4042. A credit is allowed against the port use tax for Saint Lawrence Seaway tolls paid with respect to the cargo being loaded or unloaded, with any unused credit allowed as a carryover to apply against future port use tax liability of the taxpayer.

[8] Administration of the port use tax

Generally, as determined under Treasury regulations, the port use tax is to be administrated by the U.S. Customs Service, with penalties applicable as they are under the customs laws, and not under the tax administrative procedures of Subtitle F of the Internal Revenue Code. For purposes of determining court jurisdiction, the tax is to be treated as if it were a customs duty.

Port Trust Fund

The committee amendment establishes a new Port Infrastructure Development and Improvement Trust Fund in the Treasury. The Trust Fund is to receive amounts equivalent to revenues from the new port use tax. In addition, the committee amendment authorizes appropriations to the Trust Fund of sufficient general revenues for each fiscal year such that the total of port use tax revenues and general revenues for the fiscal year equals $1 billion. The trust Fund statute is placed in the Trust Fund Code of the Internal Revenue Code.

Under the committee amendment, permitted expenditures out of the Trust Fund generally are the same as under the bill as reported by the Committee on Public Works and Transportation, with an added provision to authorize payment out of the Trust fund for Treasury expenses in administering the port use tax.

Effective date

These provisions are effective on January 1, 1986. Thus, the port use tax applies to cargo loaded or unloaded on or after January 1, 1986.

Inland Waterways Trust Fund

Waterways trust fund statute

The committee amendment places the Inland Waterways Trust Fund statute in the Trust Fund Code of the Internal Revenue Code. The amendment specifies that not more than one-third of the cost of any waterway construction project under section 202(a) of the bill and not more than one-sixth of certain relocation costs under section 202(b) of the bill may be paid out of the Trust Fund. This provision is effective on January 1, 1986.

Waterways subject to fuel tax

The committee amendment adds the Tennessee-Tombigbee Waterway to the list of inland and intracoastal waterways the commercial use of which is subject to the inland waterways fuel tax under Code section 4042.[1] There is no other change in the fuel tax.

This provision is effective on January 1, 1986.

II. EXPLANATION OF COMMITTEE AMENDMENT

The amendments to H.R. 6 by the Committee on Ways and Means provide a revenue title (Title XVIII) for the bill, relating to [9] the imposition of a new port use tax, establishment of a new Port Infrastructure Development and Improvement Trust Fund, and certain changes relating to the Inland Waterways Trust Fund and the waterways subject to the inland waterways fuel tax.

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[1] Public Law 99–662, page 10.

[1] The fuel excise tax is currently 8 cents per gallon, and is scheduled to increase to 10 cents per gallon on October 1, 1985.

A. Port Use Tax and Trust Fund

1. Imposition of port use tax (sec. 1702(a) of the bill and new secs. 4461–4462 of the Internal Revenue Code)

Present Law

Federal expenditures for harbors and port development historically have been financed from general revenues. No Federal user taxes or fees have been imposed for these specific expenditures.

Reasons for Change

The Committee on Ways and Means agrees that additional Federal investment is needed for port infrastructure development and for maintenance of such capital assets in order to expand, improve, and maintain U.S. ports and harbors for waterborne commerce. Such investments in U.S. ports and harbors will facilitate economic development and make the Nation's water transportation system more efficient.

The Committee on Ways and Means also agrees that a larger portion of Federal expenditures on port and harbor development and maintenance should be borne by the direct beneficiaries of such expenditures. Therefore, the committee amendment imposes a new port use tax. The tax is an *ad valorem* excise tax based on the value of the cargo loaded on or unloaded from ports financed (in part or whole) by the Federal Government. This will make it a uniform excise tax paid by the principal beneficiaries of Federal port development and maintenance costs. The tax rate is set at a level which the committee believes will not cause competitive or economic burdens on the ports or users. The committee emphasizes that it will very carefully review any future proposed increase or other expansion of this tax.

The Committee on Ways and Means believes that the port use tax should not apply to ports in Hawaii or in U.S. possessions to the extent that the cargo is being shipped into or among these islands because of their high dependence on waterborne commerce in their economies. However, cargo shipped through or from these islands to the continental U.S. (including Alaska) is to be subject to the tax when the cargo is unloaded. The Committee on Ways and Means does not wish to provide an incentive for importers to ship cargo through these islands to the mainland (and Alaska) in order to avoid the port use tax.

The Committee on Ways and Means agrees that the tax should not apply to fish and other aquatic animal life caught during a voyage. However, the tax would apply to shipments or processed fish, etc.

The Committee on Ways and Means determined that the port use tax should not be incurred where the Saint Lawrence Seaway toll charge is paid. The committee amendment therefore allows a credit against the port use tax, with carryovers, for such tolls paid to or on behalf of the Saint Lawrence Seaway Development Corporation. The committee was concerned that cargo shipped through the Seaway would bear a double burden of the toll charges and the port use tax. The committee decided to allow a credit against the port use tax for tolls paid rather than creating taxes paid against tolls in order to avoid affecting the amount of tolls paid since they are set through bilateral negotiations between the United States and Canada.

In addition, the committee amendment provides that the port use tax is not to be imposed with respect to cargo where the inland waterways fuel tax is paid. Further, the Committee on Ways and Means believes that the port use tax should not apply to cargo shipped by the United States Government.

The committee amendment provides that the effective date for imposition of the port use tax is January 1, 1986, in order to give the Treasury Department lead time to implement the tax.

Explanation of Provisions

Tax rate

The committee amendment imposes a new port use tax of 0.04 percent (4 cents per $100) on the value of commercial cargo loaded onto or unloaded from a commercial vessel at a port in the United States.

Coverage of tax

Port use subject to tax.—The port use tax applies to commercial cargo loaded or unloaded at any port or channel in the United States (see exemption for Hawaii and U.S. possessions, below) with a depth authorized by law of more than 14 feet. The tax does not apply at any port or channel with respect to which no Federal funds have been used for construction, maintenance, or operation.

Definitions.—The term "commercial cargo" means any waterborne cargo other than fuel supplies, ship's stores, sea stores, or legitimate equipment for the vessel (i.e., used on or in the vessel for its operation). A "commercial vessel" is any vessel used (a) in the business of transporting cargo by water for compensation or hire, or (b) in transporting cargo by water in the business of the owner, lessee, or operator of the vessel (other than fish or other aquatic animal life caught on voyage).

For purposes of the port use tax, "value" means (a) in the case of an arms length transaction, the sales price as determined under the principles of Code section 4216(a)[2]; or (b) in any other case, a constructive sales price determined under Treasury regulations. To the extent provided in regulations, value may be determined on the basis of standard commercial documentation.

Exemption for Hawaii and U.S. possessions.—The committee amendment provides that the port use tax generally does not apply to cargo loaded or unloaded at ports in Hawaii or in the possessions of the United States (Puerto Rico, U.S. Virgin Islands, Guam, American Samoa, Northern Marianas, and the Trust Territory of the Pacific Islands). In addition, the tax does not apply with respect to any cargo loaded at a U.S. port on a vessel for transportation to Hawaii or any possession of the United States for ultimate use or consumption in Hawaii or the U.S. possession. Thus, for example, the tax would apply for waterborne cargo shipped from San Francisco through Hawaii for ultimate use or consumption in a foreign country.

The tax would also apply to waterborne cargo shipped from Hawaii or a possession when the cargo is unloaded at a mainland U.S. port (including Alaska).

Credit for Saint Lawrence Seaway tolls paid.—The committee amendment provides a credit against the port use tax on cargo for any Saint Lawrence tolls paid to or on behalf of the Saint Lawrence Seaway Development Corporation by the person liable for the tax with respect to that cargo. The taxpayer subject to the port use tax is to be allocated that portion of the Saint Lawrence Seaway tolls paid which is attributable to such cargo. That portion of the toll so allocated may be used as a credit against the port use tax.

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[2] Under Section 4216(a), the price for purposes of imposing an excise tax includes any charge for coverings and containers and any charge for placing the article in a condition packed ready for shipment.

The credit for Seaway tolls paid is not to exceed the port use tax liability for any taxable period. Any excess amount of such tolls over the port use tax liability for the taxable period may be carried over to be applied against future port use tax liability of the taxpayer. The credit may not be transferred to another taxpayer but it may be used by the same taxpayer against port use tax liability incurred at any U.S. port.

Other exemptions.—The port use tax is not to be imposed with respect to any cargo if any portion of the water transportation of the cargo has been (or will be) subject to the inland waterways fuel tax (under sec. 4042). Further, the port use tax does not apply to the United States Government or any agency or instrumentality thereof.

Payment of port use tax

The port use tax is to be paid by the importer in the case of cargo entering the U.S., by the exporter in the case of cargo to be exported from the U.S., and by the shipper in the case of other waterborne cargo (i.e., cargo loaded or unloaded at U.S. ports involving shipment between U.S. ports).

The Treasury Department is to prescribe regulations so that there is only one payment of the port use tax with respect to the transportation of any cargo on the *same* vessel. For example, waterborne cargo shipped on the same vessel from Seattle to Los Angeles is to be subject to only one payment of the port use tax. Treasury regulations are to prescribe whether the tax in such a case is to be imposed on the loading or on the unloading of the cargo. Waterborne cargo shipped on one vessel between two ports in the United States and then transferred to another vessel at a subsequent U.S. port is subject to another port use tax.

In addition, the committee amendment provides that Treasury regulations are to be prescribed exempting any transaction or class of transactions from the port use tax where the collection of the [12] tax is not administratively practical (i.e., some *de minimis* level of tax per shipped item or class of items or for a taxable period that may be exempted from payment of the tax and filing of a port use tax return).

Effective Date

The port use tax provisions are effective on January 1, 1986.

2. Customs administration of port use tax (sec. 1702(a) of the bill and new Code sec. 4462(g))

Present Law

There are currently no Federal taxes assessed on port use in the United States. There is, however, a substantial body of law relating to the importation of merchandise and the collection of customs duties. The Tariff Act of 1930, as amended (codified in volume 19 of the U.S. Code), and the Customs Regulations of the United States (volume 19 of the *Code of Federal Regulations*) set out detailed rules and procedures for the classification and appraisal of imported merchandise and for the enforcement of customs laws.

Reasons for Change

Since the U.S. Customs Service currently has a strong presence at ports of entry and is experienced at appraising imported merchandise, the Committee on Ways and Means concluded that it would be more appropriate for the Customs Service, rather than the Internal Revenue Service, to collect and administer the port use tax provided for in this title.

Explanation of Provision

In order to facilitate Customs Service administration and collection of the port use tax, the committee amendment provides that all administrative and enforcement provisions of U.S. customs laws are to apply with regard to the cargo subject to the port use tax under this title of the bill as if the cargo were imported merchandise. The committee amendment further provides that Customs Service penalty provisions are to apply with respect to failures to comply with the port use tax provisions, and that the jurisdiction of courts and agencies is to be determined on the basis as if the tax imposed in this title of the bill were actually a customs duty. Thus, the Court of International Trade is to have primary jurisdiction for actions arising pursuant to this section. Further, since the customs laws and regulations are to apply, the committee amendment specifies that the administrative provisions of subtitle F of the Internal Revenue Code are to be inapplicable to the collection and administration of the port use tax.

3. Port Trust Fund (sec. 1703 of the bill and new sec. 9505 of the Code)

Present Law

There is currently no special fund or trust fund relating to Federal financing of ports and harbors. Such Federal expenditures [13] have been financed from general fund appropriations. There are several Federal trust funds receiving tax revenues earmarked for specific Federal expenditure purposes.

Currently, there are four trust funds within the Trust Fund Code of the Internal Revenue Code (Chapter 98): Black Lung Disability Trust Fund (sec. 9501); Airport and Airway Trust Fund (sec. 9502); Highway Trust Fund (sec. 9503); and Aquatic Resources Trust Fund (sec. 9504)

(The Inland Waterways Trust Fund is also added to the Internal Revenue Code by section 1704 of the bill (see B., below)).

Reasons for Change

The Committee on Ways and Means concluded that revenues from the new port use tax should go into a new trust fund in the Treasury to be available for costs of Federally-financed port projects. The committee amendment modifies the trust fund provisions in the bill as reported by the Committee on Public Works and Transportation in two respects: (1) the committee amendment specifies that general revenues, and not customs duty revenues, are authorized to be appropriated to the trust fund so that when added to the port use tax revenues appropriated to the trust fund would equal $1 billion per fiscal year; and (2) the committee amendment places the Port Trust Fund statute in the Trust Fund Code of the Internal Revenue Code. This latter provision is consistent with trust fund legislation in recent years.

Explanation of Provisions

Establishment of trust fund; transfer of revenues to the trust fund

The committee amendment establishes a new trust fund in the Treasury, the "Port Infrastructure Development and Improvement Trust Fund" (referred to herein as the "Port Trust Fund"). The committee amendment places this trust fund in the Trust Fund Code of the Internal Revenue Code.

The Port Trust Fund is to receive monies from the following three sources:

(1) amounts equivalent to revenues from

the new port use tax (new Code sec. 4461) are to be appropriated to the trust fund;

(2) amounts from general revenues equal to $1 billion less amounts received from the port use tax revenues are authorized to be appropriated to the trust fund; and

(3) interest earned on trust fund investments is to be credited to the trust fund.

Management of trust fund

Under the general provisions of the Trust Fund Code (sec. 9601), amounts appropriated to the trust fund are to be transferred at least monthly on the basis of estimates by the Secretary of the Treasury. Adjustments in estimated amounts so transferred are to be made by the Secretary.

The Secretary of the Treasury (under Code sec. 9602) is to manage the trust fund, and is to report to the Congress each year on the financial condition and results of the trust fund operations [14] during the preceding fiscal year and on its expected condition and operations during the next five fiscal years.

Any trust fund monies not necessary to meet current withdrawals are to be invested in interest-bearing obligations of the United States. Interest earned on such investments is to be credited to the trust fund.

Expenditures from trust fund

Amounts in the Port Trust Fund are to be available, as provided by appropriation Acts, for making expenditures for the following purposes:

(1) feasibility studies for, and construction, operation, and maintenance of, projects for ports by the Secretary of the Army;

(2) feasibility studies for, and construction, rehabilitation, operation, and maintenance of, projects for ports for the Saint Lawrence Seaway by the Saint Lawrence Seaway Development Corporation;

(3) relocations of utilities, structures, and other improvements, necessary for construction, operation, and maintenance of such projects;

(4) making payments to any non-Federal interest (i.e., a State or local governmental entity) which has planned and designed or planned, designed, and constructed a port in accordance with section 104 of this bill;

(5) grants under sections 113[3] and 114[4] of this bill; and

(6) the payment of all expenses incurred by the Department of the Treasury in administering the port use tax.

For purposes of the above trust fund expenditures, the term "construction" includes any planning, designing, engineering, and surveying which is necessary to carry out a project for a port and which is performed after authorization of the project. The term "port" has the meaning given such term by section 115 of the bill.[5] (See also discussion of port use tax coverage, A.1., above.) Any reference to a section of the Water Resources Conservation, Development, and Infrastructure Improvement and Rehabilitation Act of 1985 shall be treated as a reference to such section as in effect on the date of the enactment of the bill.

Effective Date

The trust fund provisions are effective on January 1, 1986.

B. Inland Waterways Trust Fund

Present Law and Background

In general, Federal expenditures for construction, operation, and maintenance costs of U.S. waterways have been financed from general revenues, rather than from fees or taxes imposed on navigation users. In the Inland Waterways Revenue Act of 1978, however, Congress imposed an inland waterways fuel excise tax, and provided for transfer of these tax revenues to an Inland Waterways Trust Fund. Amounts in the Trust Fund are available, as provided by authorization and appropriation acts, for making construction and rehabilitation expenditures for navigation on the specified waterways the commercial use of which is subject to the fuel excise tax. Amounts transferred to this trust fund have not been appropriated from the trust fund, which had an estimated balance of $192 million at the end of fiscal year 1985.

The fuel tax is imposed on diesel and other liquid fuels used by commercial cargo vessels on 26 designated inland or intracoastal waterways of the United States (Code sec. 4042). Included among the specified waterways are the Mississippi River upstream from Baton Rouge, La., the Mississippi River tributaries, Columbia-Snake Rivers Inland Waterways, part of the Willamette River in Oregon, and the Gulf and Atlantic Intracoastal Waterways. (See Treas. Reg. sec. 48.4042-1(g).) The tax does not apply to fuel used by deep-draft ocean-going vessels, recreational vessels, or noncargo vessels (such as passenger vessels and fishing boats).

The present tax rate of 8 cents per gallon is scheduled to increase to 10 cents per gallon on October 1, 1985.

Reasons for Change

The Committee on Ways and Means agrees that the Tennessee-Tombigbee Waterway should be added to the list of inland waterways the commercial use of which is subject to the inland waterways fuel tax. This waterway was not operational when the existing 26 specified waterways were included in the enactment of the Inland Waterways Revenue Act of 1978 (P.L. 95–502).

In addition, the Committee on Ways and Means determined that the provisions of the Inland Waterways Trust Fund should be part of the Trust Fund Code of the Internal Revenue Code. This action is consistent with the placing of other trust funds in the Internal Revenue Code in recent years. (See also A, 3., above, relating to the new Port Trust Fund.)

Explanation of Provision

Inland waterways subject to fuel tax

The committee amendment adds the Tennessee-Tombigbee Waterway to the list of specified inland and intracoastal waterways the commercial use of which is subject to the inland waterways fuel tax: that portion from Pickwick Pool on the Tennessee River at RM 215 to Demopolis, Ala., on the Tombigbee River at RM 215.4.

Inland Waterways Trust Fund

The committee amendment places the statutory provisions of the existing Inland

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[3] Section 113 of the bill as reported by the Committee on Public Works and Transportation authorizes grants to a non-Federal interest operating a port project for provision of emergency response services in such port.

[4] Section 114 authorizes a grant for construction of a new port office at the Morro Bay Harbor, Calif.

[5] Section 115 defines "port" as (a) any port or channel in the United States with a depth authorized by law of more than 14 feet, including any channel administered by the Saint Lawrence Seaway Development Corporation and any channel connecting the Great Lakes, and (b) any lock or other improvement on such channel; except that such term does not include a entrance channel providing access solely to a harbor with an authorized depth of 14 feet or less and does not include the Bonneville Lock and Dam project on the Columbia River.

Waterways Trust Fund in the Trust Fund Code of the Internal Revenue Code (Chapter 98). The committee amendment also specifies that not more than one-third of the costs of seven waterway lock and dam projects listed in section 202(a) of this bill are to be financed from this trust fund and that not more than one-sixth of certain related relocation expenses under section 202(b) of this bill are to be financed from this trust fund.

The Inland Waterways Trust Fund under the committee amendment is to be treated for all purposes of law as a continuation of the existing Inland Waterways Trust Fund as established by section 203 of the Inland Waterways Revenue Act of 1978.

Effective Date

These provisions are effective on January 1, 1986.

C. Coordination with Other Provisions of H.R. 6

The revenue title of H.R. 6 (Title XVII), as added by the Committee on Ways and Means, states that nothing in any other provision of the bill is to be construed as (1) imposing (or exempting from) any tax, (2) establishing any trust fund which are not also authorized by this title. Thus, Title XVII would override any other tax or exemption from tax (or "fees") or trust fund provisions elsewhere in the bill.

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Conference Report No. 99–1013
2nd Session
[Bracketed numerals indicate official report page numbers]

WATER RESOURCES DEVELOPMENT ACT OF 1986

October 17, 1986

Mr. Howard, from the committee of conference, submitted the following conference report to accompany H.R. 6[1]

The committee of conference on the disagreeing votes of the two Houses on the amendment of the Senate to the bill (H.R. 6) to provide for the conservation and development of water and related resources and the improvement and rehabilitation of the Nation's water resources infrastructure, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

* * * *

[228] TITLE XIV—REVENUE PROVISIONS

A. Port Use Tax and Trust Fund

1. Port use tax

Present law

Ports and harbors financing.—Federal expenditures for harbors and port development and maintenance have been financed from general revenues. No Federal user taxes or charges have been imposed for these expenditures.

Customs Service.—The U.S. Customs Service administers the collection of customs duties. The Tariff Act of 1930, as amended (19 U.S.C.), and the Customs Regulations set forth detailed rules and procedures for the classification and appraisal of imported merchandise and for the administration and enforcement of customs laws.

Saint Lawrence Seaway tolls.—The Saint Lawrence Seaway Development Corporation and the Saint Lawrence Seaway Authority of Canada jointly impose tolls for the commercial use of the Saint Lawrence Seaway. The tolls are per metric ton of cargo, varying by class of cargo and by specific portion of the Seaway.

House bill

Imposition of tax.—The House bill imposes an excise tax on the use of a U.S. harbor or channel ("port") by a commercial vessel for loading or unloading of commercial cargo. The tax is 0.04 percent (4 cents per $100) on the value of the cargo.

Applicability of tax.—The port use tax does not apply with respect to:

(1) a port on which no Federal funds have been used for construction, operation, or maintenance;

(2) cargo the transportation of which is subject to the inland waterways fuel tax;

(3) cargo when loaded or unloaded at ports in Hawaii or in U.S. possession, or when loaded on a vessel at a U.S. port for ultimate use or consumption in Hawaii or a possession (the tax applies when cargo loaded in Hawaii or a possession is unloaded at a U.S. port);

(4) transportation of passengers;

(5) cargo consisting of fish or other aquatic animal life caught on the voyage;

(6) cargo shipped by the U.S. Government or Federal agencies; and

(7) de minimis transactions, to the extent prescribed in Treasury regulations.

Payment of tax.—The tax is payable by the importer, exporter, or shipper of the cargo. The tax is imposed only once with respect to transportation of any cargo on the same vessel.

[229] *Administration of tax.*—The port use tax is to be administered and enforced by the U.S. Customs Service in a manner similar to customs duties.

Seaway tolls.—The House bill provides a credit against the port use tax for Saint Lawrence Seaway tolls paid (U.S. portion). The credit for Seaway tolls paid is not to exceed the port use tax liability for the taxable period, but any excess credit may be carried over against any future port use tax liability.

Effective date.—January 1, 1986.

Senate amendment

Port use charge.—The Senate amendment imposes a charge (in the Internal Revenue Code) on the use of a U.S. port by a commercial vessel for loading or unloading of commercial cargo, and on the use of Great Lakes navigation improvements (other than the Saint Lawrence Seaway) for loading, unloading, or transporting commercial cargo. Passenger vessels also are subject to the charge, with value generally determined by reference to the prices paid by passengers for their transportation.

Port maintenance charge.—The Senate amendment imposes a charge (in the Internal Revenue Code) of ½ cent per registered ton on the use by commercial vessels of such ports or Great Lakes improvements other than for loading, unloading, or transportation (i.e., for fueling, refitting, repair, etc.). This charge cannot be imposed more than three times per year with respect to a particular vessel.

Appplicability of charges.—The port use charge does not apply with respect to:

(1) ports deauthorized prior to 1985, or ports receiving no U.S. funds since 1977;

(2) cargo the transportation of which is subject to the inland waterways fuel tax;

(3) cargo shipped from the U.S. mainland to Alaska, Hawaii, or a U.S. possession for local use, or cargo shipped from Alaska, Hawaii, or a U.S. possession to the U.S. mainland for local use (the charge applies to cargo shipped to or from a foreign country and to shipments of crude

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[1] Public Law 99–662, page 10.

oil with respect to Alaska);

(4) short-haul ferrying (if regularly scheduled) of passengers and vehicles between U.S. points or between the United States and Canada or Mexico;

(5) fish or other aquatic animal life caught in voyage by a U.S. vessel, if not previously landed onshore;

(6) cargo shipped by the U.S. Government or Federal agencies;

(7) de minimis transactions, to the extent prescribed by Treasury regulations; and

(8) bonded cargo entering the U.S. for transportation and direct exportation to a foreign country. This exemption does not apply (a) if Canada imposes a similar port use charge or (b) to U.S. ports (or classes of cargo) if the mandated cargo diversion study (see below) shows that the charge is not likely to result in a significant diversion of cargo or that the nonapplicability [230] of the charge to a given U.S. port would cause economic harm to another U.S. port.

Payment of charges.—The port use charge is payable the same as under the House bill port use tax. Only one port use tax may be imposed with respect to (1) the transportation of the same cargo on the same vessel, and (2) the loading and unloading of identical cargo at one port. The port maintenance charge is payable by the vessel owner.

Administration of charges.—The port use and port maintenance charges are to be administered and enforced by the U.S. Customs Service in the same manner as provided under the House Bill.

Seaway tolls.—The Senate amendment provides for rebates of Saint Lawrence Seaway tolls (U.S. portion), to be paid out of the Trust Fund (see below).

Effective date.—April 1, 1986.

Conference agreement

Port use tax or charge.—The conference agreement follows the House bill, designating the use tax ("harbor maintenance tax") as an excise tax in the Internal Revenue Code. The rate (0.04 percent of the value of the cargo) is the same as in both the House bill and the Senate amendment. The conference agreement provides that the tax applies on use by a commercial vessel of a U.S. port for the loading or unloading of commercial cargo on or from the vessel, but does not include the additional provision in the Senate amendment that would also have applied with respect to use of Great Lakes navigation improvements for transporting cargo.

Port maintenance charge.—The conference agreement does not include the Senate amendment.

Applicablity of port use tax.—The conference agreement generally follows the Senate amendment with respect to the application of and exemption from the tax. The conference agreement includes the following modifications.

(1) the tax does not apply with respect to cargo loaded on a vessel in Alaska, Hawaii, or a U.S. possession and unload in the same State or possession in which loaded;

(2) the fish and aquatic animal exemption is not limited to U.S. vessels; and

(3) the exemption for transportation and direct exportation of bonded cargo also does not apply if Mexico imposes a similar port use tax.

Payment of tax.—The conference agreement follows the House bill and the Senate amendment.

Administration of tax.—The conference agreement follows the House bill and the Senate amendment.

Seaway tolls.—The conference agreement follows the Senate amendment, providing for rebates of Saint Lawrence Seaway tolls (U.S. portion), to be paid out of the Trust Fund (see below).

Effective date.—Under the conference agreement, the port use tax applies to use of ports in loading or unloading of cargo occurring on or after April 1, 1987.

[231] 2. Port (Harbor) Trust Fund

Present Law

No provision (see *Present law* under 1., above). There are several existing trust funds financed from earmarked excise taxes.

House bill

Establishment.—The House bill establishes the "Port Infrastructure Development and Improvement Trust Fund" in the Treasury. The statutory provisions for the Trust Fund are placed in the Trust Fund Code of the Internal Revenue Code.

Funding.—The Trust Fund is to receive amounts equivalent to revenues from the new port use tax. Also, the House bill authorizes annual appropriations to the Trust Fund equal to $1 billion less the amounts received from the port use tax revenues for the fiscal year. In addition, the Trust Fund will earn interest on investments of any cash balance.

Expenditures from the Fund.—Amounts in the Trust Fund are to be available, as provided by appropriation Acts, for making expenditures for:

(1) construction, rehabilitation, operation, and maintenance costs (including feasibility studies) for U.S. ports;

(2) construction, rehabilitation, operation, and maintenance costs (including feasibility studies) for Saint Lawrence Seaway ports;

(3) relocation costs for utilities, structures, and other improvements necessary for construction, operation, and maintenance of projects in (1) or (2), above;

(4) payments to a State or local government entity for eligible costs incurred in planning, designing, or construction under section 104 of the bill;

(5) grants under section 113 of the bill (provision of port emergency response services);

(6) grant for construction of a new port office at Morro Bay Harbor, California; and

(7) Treasury Department expenses in administering the port use tax.

Effective date.—January 1, 1986.

Senate amendment

Establishment.—The Senate amendment establishes a "Harbor Maintenance Trust Fund" in the Treasury. The Statutory provisions for the Trust Fund are placed in the Trust Fund Code of the Internal Revenue Code.

Funding.—The Trust Fund is to receive amounts equivalent to revenues from the port use and port maintenance charges, and revenues from the U.S. portion of Saint Lawrence Seaway tolls. In addition, the Trust Fund will earn interest on investments of any cash balance.

Expenditures from the Fund.—Amounts in the Trust fund are to be available, as provided by appropriation Acts, for making expenditures for:

(1) up to 40 percent of U.S. harbor (port) operation and maintenance costs (including Great Lakes navigational projects);

[232] (2) 100 percent of eligible Saint Lawrence Seaway operation and maintenance costs; and

(3) rebates of the U.S. portion of Saint Lawrence Seaway tolls to payors.

Effective date.—April 1, 1986.

Conference agreement

Establishment of Trust Fund.—The

conference agreement follows the Senate amendment.

Funding.—The conference agreement generally follows the Senate amendment.

Expenditures from the Trust Fund.—The conference agreement generally follows the Senate amendment, as modified to reflect the Trust Fund expenditure provisions in section 210(a) of the conference agreement. Also, under the conference agreement, the costs of the customs service incurred in administering and collecting the harbor maintenance tax are to be reimbursed from the customs user fee enacted in 1986. In the event such fee is repealed, such costs, not to exceed $5 million annually, are to be reimbursed from the Harbor Maintenance Trust Fund.

Effective date.—April 1, 1987.

3. Studies

House bill

No provision.

Senate amendment

Port use charge and cargo diversion.—The Secretary of the Treasury, in consultation with the Secretaries of the Army and Transportation (and other appropriate Federal agencies) and with representatives of U.S. ports, is to conduct a study to determine the impact of the port use charge of potential diversions of cargo to Canada and Mexico from U.S. ports. The Secretary's report is to be made to the Congress within one year after enactment of the bill.

Saint Lawrence Seaway tolls.—The Secretary of State, in consultation with the Secretary of Transportation, is to initiate discussions with Canada regarding reducing or eliminating all tolls on the Saint Lawrence Seaway and international Great Lakes. The Secretary is to report to the Congress on the progress of such discussions within two years after enactment.

Conference agreement

The conference agreement follows the Senate amendment, with a modification to include Treasury consultation with the U.S. Trade Representative with respect to the port use tax and cargo diversion study.

B. Inland Waterways Fuel Tax and Trust Fund

1. Fuel tax

Present law

Fuel tax rate.—An excise tax of 10 cents per gallon is imposed on diesel and other liquid fuels used by commercial cargo vessels on [233] designated inland or intracoastal waterways (Code sec. 4042). (The present tax rate was increased from 8 cents per gallon on October 1, 1985, under the rate schedule enacted in 1978). Amounts equivalent to the revenues from the tax are transferred to the Inland Waterways Trust Fund.

Waterways subject to tax.—The tax applies to taxable fuel used on 26 designated inland or intracoastal waterways (including the Mississippi River upstream from Baton Rouge, La., the Mississippi River tributaries, Columbia-Snake Rivers Inland Waterways, and the Gulf and Atlantic Intracoastal Waterways).

House bill

Fuel tax rate.—The House bill does not increase the rate of the inland waterways fuel tax.

Waterways subject to tax.—The House bill adds the Tennessee-Tombigbee Waterway to the list of inland waterways the use of which is subject to the fuel tax.

Effective date.—January 1, 1986.

Senate amendment

Fuel tax rate.—The Senate amendment increases the fuel tax rate by one cent per gallon per year, beginning on January 1, 1988, until the tax reaches 20 cents per gallon on January 1, 1997, and thereafter.

Waterways subject to tax.—The Senate amendment is the same as the House bill.

Effective date.—The increase in the fuel tax rate is effective on January 1, 1988 and January 1 of each year until 1997. The addition of the Tennessee-Tombigbee Waterway to the list of waterways with respect to which the fuel tax applies is effective April 1, 1986.

Conference agreement

Fuel tax rate.—The conference agreement provides that the inland waterways fuel tax is increased to 11 cents per gallon on January 1, 1990, to 13 cents per gallon on January 1, 1991, to 15 cents per gallon on January 1, 1992, to 17 cents per gallon on January 1, 1993, to 19 cents per gallon on January 1, 1994, and to 20 cents per gallon on January 1, 1995, and thereafter.

Waterways subject to tax.—The conference agreement follows the Senate amendment, effective on January 1, 1987.

2. Inland Waterways Trust Fund

Present law

Establishment and funding.—The Inland Waterways Trust Fund was established by section 203 of the Inland Waterways Revenue Act of 1978, and currently is not within the Trust Fund Code of the Internal Revenue Code (Chapter 98). Chapter 98 includes the Black Lung Disability Trust Fund, the Airport and Airway Trust Fund, the Highway Trust Fund, and the Aquatic Resources Trust Fund.

Amounts equivalent to the revenues from the inland waterways fuel excise tax are transferred to the Trust Fund. The Trust Fund also earns interest on investments of any cash balance.

Expenditures from the Fund.—Amounts in the Trust Fund, are available, as provided by authorization and appropriations Acts, for making construction and rehabilitation expenditures for navigation on the specified inland and intracoastal waterways, the commercial use of which is subject to the fuel tax.

House bill

Statute.—The House bill places the Inland Waterways Trust Fund in the Trust Fund Code of the Internal Revenue Code. The Trust Fund under the transferred statutory provision is treated as a continuation of the existing Trust Fund.

Expenditures from the Fund.—The House bill retains the general expenditure purposes of the Trust Fund as under present law, subject to the limitation that expenditures from the Trust Fund cannot be used to finance more than (1) one-third of the costs of specified inland waterways lock and dam projects or more than one-sixth of the costs of necessary relocation of pipelines, electricity, or communications cables or lines of related facilities in connection with such projects.

Effective date.—January 1, 1986.

Senate amendment

Statute.—The Senate amendment is the same as the House bill.

Expenditures from the Fund.—The Senate amendment provides that the Trust Fund is to pay, subject to appropriations Acts, one-half the costs (construction, rehabilitation, modification, and post-authorization planning) of certain specified inland waterways lock and dam projects.

Effective date.—April 1, 1986.

Conference agreement

Statute.—The conference agreement follows the House bill and the Senate amendment.

Expenditures from the Trust Fund.—The conference agreement generally follows the Senate amendment, as modified to reflect the Trust Fund expenditure purposes included in title III, section 844, and section 1103(j) of the conference agreement.

Effective date.—January 1, 1987.

* * * *

Part IV. Items of General Interest

State and Local Governments Covered by "218 Agreements"—FICA TAXES

Announcement 86–122

State and local government employers that are covered by "218 agreements" (agreements under section 218 of the Social Security Act, 42 U.S.C. section 418 (1985 Supp.)) will be subject to the Internal Revenue Code with respect to wages paid after December 31, 1986. This announcement explains, in question and answer form, the rules that these employers should follow, beginning January 1, 1987.

Section 218 of the Social Security Act provides that a state may enter into a voluntary agreement with the Secretary of Health and Human Services to provide social security coverage for its employees or employees of local governments within the state. Generally, before enactment of the Omnibus Budget Reconciliation Act of 1986 (OBRA), section 9002, Pub. L. No. 99–509, 100 Stat.—, wages paid by state and local government employers were excluded from taxation under the Federal Insurance Contributions Act (FICA) by section 3121(b)(7) of the Code.

Q1. What changes did OBRA make to the Social Security Act?

A1. OBRA amended section 218 of the Social Security Act with the result that starting in 1987 state governments are relieved from (1) collecting social security contributions from local governments and (2) liability for verifying and depositing the amounts owed by local governments.

Q2. What changes did OBRA make to the Internal Revenue Code?

A2. Among other changes, OBRA enacted sections 3121(b)(7)(E) and 3126 of the Code. Section 3121(b)(7)(E) provides that services covered under a 218 agreement will be treated as employment for purposes of FICA, effective with respect to wages paid after December 31, 1986. Section 3126 specifies who must file the FICA tax return, Form 941 (See Q&A 5).

Q3. What is the effect of providing that services under a 218 agreement are subject to FICA?

A3. States are no longer responsible for collecting the social security contributions from local governments and reporting those amounts to the Social Security Administration. Rather, each state and local government employer covered by a 218 agreement must file returns with the Internal Revenue Service and deposit FICA taxes through the Federal Tax Deposit (FTD) system.

Q4. What return should be used to report the FICA taxes?

A4. Employers covered by 218 agreements should use Form 941, Employer's Quarterly Federal Tax Return, to report FICA taxes starting with the return due for the calendar quarter ending March 31, 1987. Employers covered by 218 agreements should no longer file Form 941E, Quarterly Return of Withheld Federal Income Tax and Hospital Insurance (Medicare) Tax. Employers covered by 218 agreements should report all FICA taxes (including medicare tax) and withheld federal income tax on Form 941 even if the employers have some employees who are not covered by 218 agreements or some employees who are subject only to medicare tax. Employers not covered by 218 agreements, including those with federal employees on their payrolls, should continue to file Form 941E. Under no circumstances should an employer file both Form 941 and Form 941E.

Q5. Who is responsible for filing Form 941?

A5. Form 941 must be filed by the officer or employee of the state or local government or the appropriate agency or instrumentality of the state or local government having control of the payment of the wages or appropriately designated for that purpose.

Q6. What employer identification number should be used on the return?

A6. State and local government employers must use their individual employer identification numbers and not the numbers assigned to the states by the Social Security Administration for purposes of payment of section 218 contributions. If a state or local government employer has not been assigned an employer identification number, it should file Form SS-4, Application for Employer Identification Number, with the appropriate Internal Revenue Service Center.

Q7. How must taxes due under a section 218 agreement be paid to the federal government?

A7. For wages paid after December 31, 1986, FICA taxes will generally be deposited through the Federal Tax Deposit (FTD) system. The dates for deposit will depend on whether the aggregate amount of FICA taxes and undeposited withheld federal income taxes due is $3,000 or more, between $500 and $3,000, or less than $500. See Circular E, Employer's Tax Guide, for more information.

Q8. What rules apply to employers with undeposited taxes of $3,000 or more?

A8. Employers with an aggregate amount of undeposited withheld federal income tax and FICA taxes due on Form 941 of $3,000 or more must deposit the taxes using Form 8109, Federal Tax Deposit Coupon, with an authorized financial institution or with a Federal Reserve bank or branch within 3 banking days after the close of the eighth-monthly period in which the liability arises. Eighth-monthly periods end on the 3rd, 7th, 11th, 15th, 19th, 22nd, 25th, and last day of each month.

Q9. What rules apply to employers with undeposited taxes of $500 or more but less than $3,000?

A9. Employers with an aggregate amount of undeposited withheld federal income tax and FICA taxes of $500 or more, but less than $3,000, must generally deposit the taxes within 15 days after the end of a month. See Circular E.

Q10. What rules apply to employers with undeposited taxes of less than $500?

A10. Undeposited taxes of less than $500 at the end of any month other than the last month of a quarter do not have to be deposited. Those amounts are carried over to the following month within the quarter. Employers with undeposited taxes of less than $500 at the end of a quarter must pay the taxes directly to IRS with Form 941 or deposit them by the due date of Form 941.

Q11. What transition rules apply to the deposit rules set out in Q&A 7–10?

A11. There are two transition rules that apply to state and local government employers covered by 218 agreements.

First, for wages paid before October 1, 1988, the deposit schedule for FICA taxes may be determined separately from the deposit schedule for withheld federal income tax.

Second, for state or local government employers subject to the eighth-monthly deposit rules as determined under the first transition rule, the following rules apply:

(1) for wages paid before October 1, 1987, the employer may make its deposit of FICA taxes within 7 banking days after the close of the eighth-monthly period;

(2) for wages paid after September 30, 1987, and before October 1, 1988, the deposit of FICA taxes may be made within 5 banking days after the close of the eighth-monthly period.

An employer making deposits under the transition rules should use separate deposit coupons for deposits of the withheld federal income tax and the FICA taxes.

Starting on October 1, 1988, FICA taxes and withheld federal income tax must be aggregated for purposes of the deposit rules (Q&A 7–10).

Q12. What interest rate applies to late payments of taxes by state and local government employers?

A12. State and local government employers are subject to the interest rate on underpayments determined under section 6621 of the Code. The rate for the first quarter of 1987 is 9 percent.

Q.13 What penalties apply to state and local government employers?

A13. Absent a showing of reasonable cause, employers are subject to penalties for late filing and late payment under section 6651 of the Code and to penalties for failing to deposit or for claiming overstated deposits under section 6656.

Q14. What impact does OBRA have on state and local government employers not covered by 218 agreements?

A14. State and local government employers not covered by 218 agreements should continue to file Form 941E to report withheld federal income tax as well as medicare tax for employees hired after March 31, 1986. See Rev. Rul. 86–88, 1986–28 I.R.B. 10. Treatment of medicare tax for employees hired after March 31, 1986, by employers not covered by 218 agreements was not affected by OBRA.

State and local government employers not covered by 218 agreements are reminded that the transition rules (set out in Q&A 11) do not apply to them. They must make deposits under the rules applicable to all employers and must aggregate withheld federal income tax with any medicare tax and any non-section 218 agreement FICA taxes due.

Q15. Where should state and local government employers look for additional information?

A15. For additional information about reporting and payment of federal employment taxes, see Circular E, available at any IRS office.

Application of the Section 1374 Built-in Gain Tax To S Corporations

Announcement 86–128

The Tax Reform Act of 1986 (the Act) modifies the treatment of S corporations that were formerly C corporations by imposing a corporate-level tax under section 1374 of the Internal Revenue Code on certain "built-in" gains (gains arising prior to the conversion to S corporation status) that are recognized by the corporation (built-in gain tax). This built-in gain tax is applicable to S corporations for taxable years beginning after December 31, 1986, but only if the S election for the corporation is made after December 31, 1986. (Rev. Rul. 86–141 explains the rules applicable to corporations that seek to make an S election prior to January 1, 1987.)

The built-in gain tax is intended both to complement the amendments to the Code made by the Act that repeal the *General Utilities* doctrine and to prevent the circumvention of the purposes of those amendments. Section 337(d)(1) of the Code, as amended, provides, in part, that the Secretary shall prescribe regulations to prevent circumvention of the purposes of such amendments through the use of any provision of law or regulations, including specifically part III of subchapter C of the Code (corporate reorganization provisions).

The Internal Revenue Service has received numerous requests for clarification regarding the application of certain provisions of the built-in gain tax. This announcement informs taxpayers of the manner in which regulations will clarify the application of these provisions in five areas.

I. Section 1374(b)(1) of the Code provides that the tax is imposed on the lesser of the recognized built-in gains of an S corporation or the amount that would be its taxable income if it were not an S corporation. Section 1374(d)(2) generally defines "recognized built-in gain" as any gain recognized during the recognition period on the disposition of any asset. The "recognition period" is defined in section 1374(d)(3). The Service will issue regulations defining "disposition of any asset" for purposes of the built-in gain tax to include not only sales or exchanges but other income-recognition events that effectively dispose of or relinquish the taxpayer's right to claim or receive income. For instance, the term "disposition of any asset" will include the collection of accounts receivable by a cash method taxpayer and the completion of a long-term contract performed by a taxpayer using the completed contract method of accounting.

II. Inquiries have been made as to the treatment of inventory under the built-in gain tax. Section 1374(d)(2)(A) of the Code, in effect, excludes from the built-in gain tax the gain from the disposition of an asset if the S corporation establishes that the asset was not held at the beginning of the corporation's first taxable year for which the corporation was an S corporation pursuant to the S election that was in effect at the time the gain was recognized (first taxable year as an S corporation). The Service will issue regulations providing that, for purposes of section 1374(d)(2)(A), the inventory method used by the taxpayer for tax purposes (FIFO, LIFO, etc.) shall be used to identify whether goods disposed of following conversion to S corporation status were held by the corporation at the time of conversion. Thus, for example, a corporation using the LIFO inventory method will not be subject to the built-in gain tax with respect to sales of inventory except to the extent that a LIFO layer existing prior to the beginning of the first taxable year as an S corporation is invaded after the beginning of that year.

III. The Service is concerned about possible use of certain transactions under the corporate reorganization provisions of the Code to circumvent the application of the built-in gain tax. Under section 1374(c)(1) of the Code, the built-in gain tax does not apply to a corporation that always has been an S corporation. Under section 1374(c)(2), the aggregate gain of a corporation that is subject to the built-in gain tax is limited to the net unrealized built-in gain in the assets held at the beginning of the corporation's first taxable year as an S corporation. Section 1374(d)(2) limits recognized built-in gain to the extent that the S corporation establishes either that the asset disposed of was not held by the S corporation as of the beginning of its first taxable year as an S corporation or that such recognized gain exceeds the excess of the asset's fair market value as of the beginning of its first taxable year as an S corporation over its adjusted basis at that time. These provisions raise the question whether the built-in gain tax applies to the disposition by an S corporation of appreciated property received from a C corporation in a tax-free exchange to the extent the property received is transferred basis property (as defined in section 7701(a)(43)).

To prevent the use of the corporate reorganization provisions of the Code to circumvent the built-in gain tax, the regulations will provide that transferred basis property acquired by an S corporation from a C corporation or a former C corporation, such as transferred basis property acquired in a tax-free merger of a C corporation into an S corporation, generally is subject to the built-in gain tax notwithstanding that the transferee corporation always has been an S corporation or that the assets were not held as of the beginning of that corporation's first taxable year as an S corporation.

For purposes of section 1374 of the Code, as amended by the Act, the acquisition of such transferred basis property will be treated as a conversion to S corporation status as to that property. Therefore, the net unrealized built-in gain with respect to such property will be measured when the property is received. Such property will be subject to the built-in gain tax if disposed of by the transferee S corporation within 10 years of receipt by the transferee S corporation. The recognition period will begin on the date the property is received.

Similar rules will apply when an S corporation that is subject to the built-in gain tax transfers property to another S corporation in a transaction under the corporate reorganization provisions of the Code. In this instance, the regulations will provide that the built-in gain tax will apply to the transferee S corporation and that the ten-year recognition period for the assets received by the transferee S corporation will be reduced by the portion of the recognition period of the transferor that had expired prior to the transfer.

IV. A related issue concerns the treatment of exchanged basis property (as defined in section 7701(a)(44) of the Code) that is received by an S corporation that is subject to the built-in gain tax. Such property includes assets received in transactions under section 1031 (like-kind exchanges) or section 1033 (involuntary conversions). The regulations will provide that the net unrealized built-in gain of assets subject to the built-in gain tax when so transferred will be preserved in the assets received in the exchange. Therefore, such exchanged basis property will be subject to the built-in gain tax if disposed of by the transferee S corporation during the recognition period. The regulations will provide that the expiration date of the ten-year recognition period, as defined in section 1374(d)(3), that is applicable to the transferred property will apply to such exchanged basis property.

V. The Service is concerned that the built-in gain tax may be circumvented by the contribution of certain built-in loss assets (assets with adjusted bases in excess of their fair market values) to the corporation prior to its conversion to S corporation status because the tax is limited to the corporation's net unrealized built-in gain, as defined in section 1374(d)(1). The Service will issue regulations that provide special treatment for the contribution of built-in loss assets to corporations prior to their conversion to S corporation status. In appropriate cases, the regulations will prohibit the reduction of the corporation's net unrealized built-in gain through such contributions if the contributions are undertaken to limit or avoid the application of the built-in gain tax.

It is anticipated that the regulations will implement rules similar to those provided in section 336(d)(2) (as amended). Under such rules, the loss inherent in property contributed to a corporation within 2 years of the earlier of (1) the beginning of the first taxable year as an S corporation or (2) the filing of its S election will not reduce the net unrealized built-in gain, as defined in section 1374(d)(1), unless, for example, the taxpayer demonstrates a clear and substantial relationship between the contributed property and the conduct of the corporation's current or future business enterprises.

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and address of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletins for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under the consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Howard M. Belser	Decatur, AL	Attorney	Three Years from October 9, 1986
Kennard I. Mandell	Wellesley, MA	Attorney	Indefinite from October 1, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any person who has violated the rules and regulations governing the recognition of attorneys, certified public accountants, enrolled agents or enrolled actuaries to practice before the Internal Revenue Service.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been suspended from further practice before the Internal Revenue Service.

Name	Address	Designation	Term of Suspension
Paul Adams, Jr.	Bristol, VA	Certified Public Accountant	Indefinite from September 11, 1986

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Leonard Bezark	King of Prussia, PA	Certified Public Accountant	October 19, 1986

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified, below*).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1954 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified and superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR— Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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DEPOSITORY

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 86–151, page 4.

Losses; casualty; disaster areas; year of deduction. Disaster areas in which losses during 1986 qualify for special tax treatment under section 165(i) of the Code are listed. Also, Rev. Rul. 84–178 (list of disaster areas in 1984) and Rev. Rul. 85–195 (list of disaster areas in 1985) are supplemented.

Rev. Rul. 86–152, page 10.

Inventories; LIFO; timber cut under a section 631(a) election. A taxpayer may not use the LIFO inventory identification method in arriving at the adjusted basis of timber for purposes of computing gain or loss when the timber is cut under a section 631(a) election. Rev. Rul. 60–244 clarified.

Rev. Rul. 86–153, page 12.

LIFO; price indexes, department stores. The April 1986 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, April 30, 1986.

Rev. Rul. 86–154, page 14.

Interest on loans; effectively connected to branch office. Securities held by a U.S. branch of a foreign bank and recorded on its books are attributable to the U.S. branch or to the home office.

Rev. Rul. 86–155, page 15.

Foreign base company income; gross income. Gross income from the engineering, fabrication, and installation of offshore drilling platforms is determined according to section 1.61–3(a) of the regulations after the income from such activities is classified according to the standards set forth in section 1.954(f)(2). Rev. Rul. 83–118 revoked.

Rev. Rul. 86–157, page 13.

Mutual life insurance companies; differential earnings rates. The recomputed differential earnings rate for 1984 published in Rev. Rul. 86–114, 1986–39 I.R.B. 14, is corrected. The differential earnings rate for 1985 and the other figures on which these rates are based that are set forth in Rev. Rul. 86–114 are restated. Mutual life insurance companies use these rates to compute their income tax liability for 1985. Rev. Rul. 86–114 modified and superseded.

Rev. Rul. 86–158, page 16.

Federal rates; adjusted federal rates; adjusted federal long-term rate, and the long-term tax-exempt rate. For purposes of sections 1274, 1288, 382, and other sections of the Code, a table sets forth the rates for January 1987.

T.D. 8107, page 7.

Regulations under section 172 of the Code relate to the taxable years to which a net operating loss of a real estate investment trust may be carried.

Notice 86–17, page 19.

The branch profits tax provided by section 884(a) of the Code will not generally be imposed on (1) the complete termination of a foreign corporation's U.S. trade or business, (2) certain liquidations or reorganizations of a foreign corporation that has conducted a U.S. trade or business, or (3) a section 351 incorporation of a foreign corporation's U.S. trade or business.

Announcement 86–129, page 22.

Guidance is provided with respect to the diversification requirements under section 817(h) of the Code that are applicable to variable annuity, endowment, and life insurance contracts.

TAX CONVENTIONS

Rev. Rul. 86–156, page 18.

Netherlands; equipment rental payments; business profits. U.S. source payments for equipment rentals are exempt from U.S. income tax as business profits under Article III of the U.S.-Netherlands Income Tax Convention.

ADMINISTRATIVE

Rev. Proc. 86–48, page 20.

Election to expense certain depreciable business assets. The proposed revenue procedure provides guidance to taxpayers who made elections under section 179 of the Code to expense amounts that exceed the dollar limitations imposed by section 280F(a)(2) of the Code.

Notice 86–15, page 19.

The correct title and address is provided for the office of the new Assistant Commissioner (International) that was established May 12, 1986, to coordinate the various international activities of the Service.

Announcement 86–130, page 22.

Information reporting rules under section 6049 of the Code are set forth for brokers and middlemen who hold interests as nominees in certificates of deposit and other instruments issued at a discount.

Announcement 86–131, page 23.

Publication 1212, List of Original Issue Discount Instruments (Rev. Dec. 86), is supplemented to provide information to banks, brokers, and other middlemen regarding Treasury bills issued at a discount and maturing during January through June 1987.

Finding Lists begin on page 25.
Announcement of Disbarments and Suspensions on page 24.

Department of the Treasury
Internal Revenue Service

T22. 23:

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenues at the least cost to the public, and in a manner that warrants the highest degree of public confidence in our integrity, efficiency and fairness. To achieve that purpose, we will:

—Encourage and achieve the highest possible degree of voluntary compliance in accordance with the tax law and regulations;

—Advise the public of their rights and responsibilities;

—Determine the extent of compliance and the causes of noncompliance;

—Do all things needed for the proper administration and enforcement of the tax laws;

—Continually search for and implement new, more efficient and effective ways of accomplishing our Mission.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1954 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1954.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts.

Part IV.—Items of General Interest.
With the exception of the disbarment and suspension list included in this part, none of these announcements is consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provides (1) finding lists of items published in the Bulletin, (2) digests of revenue rulings, revenue procedures, and other published items, and (3) indexes of Public Laws, Treasury Decisions, and Tax Conventions.

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the Internal Revenue Bulletin as the source would be appropriate.

For sale by the Superintendent of Documents U.S. Government Printing Office, Washington, D.C. 20402. Prices: Domestic—$1.75 a single copy. $82.00 a year subscription. Foreign—$2.19 a single copy. $102.50 a year for subscription.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1954

Section 165.—Losses

26 CFR 1.165–11: Election in respect of losses attributable to a disaster.

Losses; casualty; disaster areas; year of deduction. Disaster areas in which losses during 1986 qualify for special tax treatment under section 165(i) of the Code are listed. Also, Rev. Rul. 84–178 (list of disaster areas in 1984) and Rev. Rul. 85–195 (list of disaster areas in 1985) are supplemented.

Rev. Rul. 86–151

LAW AND ANALYSIS—HOLDING

Under section 165(i) of the Internal Revenue Code, if a taxpayer suffers a loss attributable to a disaster occurring in an area subsequently determined by the President of the United States to warrant assistance by the Federal Government under the Disaster Relief Act of 1974, sections 101 and 102, 42 U.S.C. sections 5121 and 5122 (1982), 1974–2 C.B. 414, then the taxpayer may elect to take a deduction for that loss on the taxpayer's federal income tax return for the taxable year immediately preceding the taxable year in which the disaster occurred.

The election to deduct for the preceding year must be made on or before the later of (1) the original due date of the taxpayer's income tax return for the year in which the disaster occurred, or (2) the due date of the preceding year's return (taking into account extensions of time for filing granted to the taxpayer). Section 1.165–11 of the Income Tax Regulations. This section of the regulations sets forth the procedures for making an election with respect to such losses.

The provisions of section 165(i) of the Code apply only to losses that are otherwise deductible under section 165(a). An individual taxpayer may deduct losses if they are incurred in a trade or business, if they are incurred in a transaction entered into for profit, or if they are casualty losses under section 165(c)(3).

As of November 30, 1986, the President had determined that the areas listed below have been adversely affected by disasters of sufficient severity occurring during 1986 to warrant disaster assistance by the Federal Government under the Disaster Relief Act of 1974.

There may be areas in which a disaster occurred during 1986 and which the President, after November 30, 1986, declares eligible for disaster assistance under the Disaster Relief Act of 1974. Information concerning these areas will be published in a supplemental revenue ruling. If possible, this information will be included in this revenue ruling when it is published in the Cumulative Bulletin.

Disaster Areas in 1986	Type of Disaster	Date Disaster Occurred or Began
Alaska		
Boroughes of North Slope and Northwest Arctic	Arctic sea storm, high winds, and wave action	September 20, 1986
Boroughes of Kenai Peninsula, Matanuska-Susitna, Valdez-Cordova, and Yukon-Koyukuk	Severe storms and flooding	October 10, 1986
Portion of the Alaska Railroad south of the Community of Healy		
California		
Counties of Alameda, Alpine, Amador, Butte, Calaveras, Colusa, Contra Costa, Del Norte, El Dorado, Fresno, Glenn, Humboldt, Lake, Lassen, Madera, Marin, Mendocino, Modoc, Mono, Napa, Nevada, Placer, Plumas, Sacramento, San Benito, San Joaquin, San Mateo, Santa Clara, Santa Cruz, Shasta, Sierra, Solano, Sonoma, Sutter, Tehama, Trinity, Tuolumne, Yolo, and Yuba	Severe storms, landslides, mudslides, and flooding	February 12, 1986
Illinois		
Counties of Adams, Calhoun, Cook, Jersey, Kane, Lake, McHenry, and St. Clair	Severe storms and flooding	September 21, 1986
Indiana		
County of Randolph	Tornadoes	March 10, 1986

Disaster Areas in 1986	Type of Disaster	Date Disaster Occurred or Began
Kansas		
Counties of Allen, Bourbon, Chautauqua, Cherokee, Cowley, Elk, Labette, Montgomery, Neosho, and Wilson	Severe storms and flooding	October 2, 1986
Michigan		
Counties of Allegan, Arenac, Bay, Clare, Clinton, Genesee, Gladwin, Gratiot, Huron, Ionia, Isabella, Kent, Lake, Lapeer, Macomb, Manistee, Mason, Mecosta, Midland, Montcalm, Muskegon, Newaygo, Oceana, Osceola, Ottawa, Saginaw, Sanilac, Shiawassee, Tuscola, and Van Buren	Severe storms and flooding	September 10, 1986
Missouri		
Counties of Bates, Benton, Boone, Callaway, Cass, Clark, Cole, Cooper, Franklin, Gasconade, Henry, Howard, Johnson, Lewis, McDonald, Miller, Moniteau, Montgomery, Morgan, Osage, Pettis, Ralls, Saline, Scotland, Shelby, St. Charles, St. Clair, St. Louis, Vernon, and Warren	Severe storms and flooding	September 18, 1986
Montana		
Counties of Chouteau, Daniels, Dawson, Deer Lodge, Fergus, Glacier, Granite, Liberty, Petroleum, Phillips, Pondera, Powell, Sanders, Teton, Toole, and Valley	Heavy rains, landslides, ice jams, and flooding	February 24, 1986
Counties of Blaine, Garfield, Hill, McCone, Phillips, Rosebud, and Valley	Severe storms and flooding	September 25, 1986
Nevada		
Counties of Douglas, Humboldt, Lyon, Storey, and Washoe	Severe storms and flooding	February 15, 1986
Carson City (City) and portions of the Fort McDermitt Indian Reservation located in Nevada		
New Hampshire		
Counties of Cheshire, Hillsborough, and Sullivan	Severe storms and flooding	July 29, 1986
Oklahoma		
Counties of Adair, Beckham, Blaine, Caddo, Canadian, Cherokee, Cleveland, Comanche, Creek, Custer, Delaware, Garfield, Grady, Grant, Greer, Haskell, Kay, Kingfisher, Kiowa, Logan, Major, Mayes, McClain, Muskogee, Noble, Nowata, Okfuskee, Oklahoma, Okmulgee, Osage, Ottawa, Pawnee, Payne, Pottawatomie, Rogers, Sequoyah, Tillman, Tulsa, Wagoner, Washington, and Washita	Severe storms and flooding	September 26, 1986

Disaster Areas in 1986	Type of Disaster	Date Disaster Occurred or Began
Pennsylvania		
County of Allegheny	Severe storms and flooding	May 30, 1986
Puerto Rico		
Municipalities of Aguada, Aibonito, Anasco, Arecibo, Barceloneta, Barranquitas, Caguas, Camuy, Cayey, Ciales, Coamo, Corozal, Florida, Hatillo, Jayuya, Lares, Luquillo, Manati, Moca, Morovis, Orocovis, San German, San Sebastian, Toa Baja, Utuado, and Villalba	Heavy rains, landslides, and flooding	April 25, 1986
South Dakota		
Counties of Aurora, Beadle, Brookings, Clark, Codington, Day, Deuel, Douglas, Edmunds, Faulk, Grant, Hamlin, Hand, Hutchinson, Jerauld, Kingsbury, Lyman, Potter, Roberts, Sanborn, Spink, Sully, Tripp, Turner, and Walworth	Severe storms and flooding	March 22, 1986
Texas		
Nolan County	Severe storms, rains, and tornadoes	April 19, 1986
Trust Territory of the Pacific		
Island of Ponape	Typhoon Lola	May 16, 1986
Utah		
Counties of Cache, Morgan, Wasatch, and Weber	Heavy rains, snowmelt, and flooding	February 12, 1986
Washington		
Counties of Clallam, Jefferson, and King	Severe storms landslides, and flooding	January 16, 1986
Cowlitz County	Heavy rains, landslides, and flooding	February 22, 1986
City of Spokane	Severe storms and flood damage	May 20, 1986
Wisconsin		
Counties of Milwaukee and Waukesha	Severe storms	August 6, 1986
Counties of Dodge, Fond du Lac, Kenosha, Milwaukee, Ozaukee, Sheboygan, Washington, and Waukesha	Severe storms and flooding	September 10, 1986

The following are areas in which disasters occurred prior to 1986 and which the President, on September 10, 1986, declared eligible for disaster assistance under the Disaster Relief Act of 1974.

Disaster Area in 1984	Type of Disaster	Date Disaster Occurred or Began
Texas		
Motley County Independent School District	Tornadoes	May 1, 1984

Disaster Area in 1985	Type of Disaster	Date Disaster Occurred or Began
Maryland		
Oldtown School in Allegany County	Severe storms and flooding	November 4, 1985

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 84–178, 1984–2 C.B. 48, and Rev. Rul. 85–195, 1985–2 C.B. 69, are supplemented.

Section 172.—Net Operating Loss Deduction

26 CFR 1.172–1: Net operating loss deduction.

T.D. 8107

TITLE 26.—INTERNAL REVENUE.—
CHAPTER I, SUBCHAPTER A, PART
1.—INCOME TAX; TAXABLE YEARS
BEGINNING AFTER DECEMBER 31,
1953

Taxable Years to Which the Net Operating Loss of a Real Estate Investment Trust May Be Carried

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations under section 172(b)(1)(E). These amendments will conform the regulations to changes made by the Act of December 24, 1980 (Pub. L. 96–595), the Economic Recovery Tax Act of 1981, and the Technical Corrections Act of 1982. These regulations provide guidance to officers and employees of the Internal Revenue Service and the public with respect to the taxable years to which a net operating loss of a real estate investment trust (hereinafter REIT) may be carried.

DATE: These regulations are generally effective for net operating losses in taxable years ending after December 31, 1975; however, the regulations conforming to section 207(a)(2)(B)(i) of the Economic Recovery Tax Act of 1981 (§1.172–10(a)(3)) shall apply to the determination of the net operating loss deduction for taxable years ending after October 4, 1976, for net operating losses sustained in taxable years ending after December 31, 1972.

FOR FURTHER INFORMATION CONTACT: Mitchell H. Rapaport of the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (202-566-3740).

BACKGROUND

On June 26, 1984, the FEDERAL REGISTER published proposed amendments to the Income Tax Regulations (26 CFR Part 1) under section 172 of the Internal Revenue Code of 1954 (49 FR 26102) [1984–2 C.B. 841]. The amendments were proposed to conform the regulations to the amendments made by section 1606 of the Tax Reform Act of 1976 (Pub. L. 94–455, 90 Stat. 1755), section 1 of the Act of December 24, 1980 (Pub. L. 96–595, 94 Stat. 3464) and by section 207(a) and (c)(1) and (3) of the Economic Recovery Tax Act of 1981 (Pub. L. 97–34, 95 Stat. 225, 226) (as amended by section 102(d)(1) and (2) of the Technical Corrections Act of 1982 (Pub. L. 97–448, 96 Stat. 2370)). The proposed regulations also contained amendments to update the existing regulations under section 172 and delete provisions that are no longer applicable. The Service did not receive any written comments in response to the notice of proposed rulemaking. No public hearing was requested or held. Accordingly, the proposed regulations are adopted as proposed.

NON-APPLICABILITY OF EXECUTIVE ORDER 12291

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a regulatory impact analysis is not required.

REGULATORY FLEXIBILITY ACT

Although a notice of proposed rulemaking that solicited public comment was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public procedure requirements of 5 U.S.C. 553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

DRAFTING INFORMATION

The principal author of these regulations is Mitchell H. Rapaport of the Legislation and Regulations Division of the Office of the Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and the Treasury Department participated in developing the regulations, on matters of both substance and style.

* * * * *

Amendments to the regulations

The amendments to 26 CFR Part 1 are as follows:

Paragraph 1. The authority for Part 1 continues to read in part:

Authority: 26 U.S.C. 7805. * * *

Par. 2. Section 1.172–1 is amended by removing paragraph (f), by redesignating paragraphs (g) and (h) as paragraphs (f) and (g), respectively, and by revising paragraph (e) to read as follows:

§1.172–1 Net operating loss deduction.

* * * * *

(e) *Low applicable to computations.* (1) In determining the amount of any net operating loss carryback or carryover to any taxable year, the necessary computations involving any other taxable year shall be made under the law applicable to such other taxable year.

(2) The net operating loss for any taxable year shall be determined under the law applicable to that year without regard to the year to which it is to be carried and in which, in effect, it is to be deducted as part of the net operating loss deduction.

(3) The amount of the net operating loss deduction which shall be allowed for any taxable year shall be determined under the law applicable to that year.

* * * * *

Par. 3. Section 1.172–2 is revised to read as follows:

§1.172–2 Net operating loss in case of a corporation.

(a) *Modification of deductions.* A net operating loss is sustained by a corporation in any taxable year if and to the extent that, for such year, there is an excess of deductions allowed by chapter 1 of the Code over gross income computed thereunder. In determining the excess of deductions over gross income for such purpose—

(1) *Items not deductible.* No deduction shall be allowed under—

(i) Section 172 for the net operating loss deduction, and

(ii) Section 922 in respect of Western Hemisphere trade corporations:

(2) *Dividends received.* The 85-percent limitation provided by section 246(b) shall not apply to the deductions otherwise allowed under—

(i) Section 243(a) in respect of dividends received from domestic corporations,

(ii) Section 244 in respect of dividends received on preferred stock of public utilities, and

(iii) Section 245 in respect of dividends received from foreign corporations: and

(3) *Dividends paid.* The deduction granted by section 247 in respect of dividends paid on the preferred stock of public utilities shall be computed without regard to subsection (a)(1)(B) of Section 247.

(b) *Example.* The following example illustrates the application of paragraph (a):

Example. For the calendar year 1981, the X corporation has gross income of $400,000 and total deductions allowed by chapter 1 of the Code of $375,000, exclusive of any net operating loss deduction and exclusive of any deduction for dividends received or paid. Corporation X in 1981 received $100,000 of dividends entitled to the benefits of section 243(a). These dividends are included in Corporation X's $400,000 gross income. Corporation X has no other deductions to which section 172(d) applies. On the basis of these facts, Corporation X has a net operating loss for the year 1981 of $60,000, computed as follows:

Deductions for 1981	$375,000
Plus: Deduction for dividends received, computed without regard to the limitation provided in section 246(b) (85% of $100,000)	85,000
Total	460,000
Less: Gross income for 1981 (including $100,000 dividends)	400,000
Net operating loss for 1981	60,000

(c) *Qualified real estate investment trusts.* For taxable years ending after October 4, 1976, the net operating loss of a qualified real estate investment trust (as defined in §1.172–10(b) is computed by taking into account the adjustments described in section 857(b)(2) (other than the deduction for dividends paid, as defined in section 561), as well as the modifications required by paragraph (a)(1) of this section. Thus, for example, the special deductions for dividends received, etc., provided in part VIII of subchapter B (other than section 248), as well as the net operating loss deduction under section 172, are not allowed in computing the net operating loss of a qualified real estate investment trust.

Par. 4. Section 1.172–3 is amended as follows:

1. Paragraph (a) is amended by removing the phrase "beginning after December 31, 1953," by removing "of 1954," and by removing the clause; "this rule shall apply even though the loss year is otherwise subject to the Internal Revenue Code of 1939," and by adding a period after the word "thereunder";

2. Paragraph (b) is amended by removing the phrase "in case of a taxable year beginning after December 31, 1963,";

3. Paragraph (e) is removed; and

4. Paragraph (f) is redesignated as paragraph (e).

Par. 5. Section 1.172–4 is amended as follows:

1. Paragraph (a)(5) is removed;

2. Existing paragraph (a)(6), (7), and (8) are redesignated as paragraph (a)(5), (6), and (7), respectively;

3. Newly redesignated paragraph (a)(7) is amended by removing "1371" and adding "1361" in lieu thereof and by removing "(g)" and adding "(f)" in lieu thereof; and

4. Paragraphs (a)(1) and (b) are revised to read as follows:

§1.172–4 Net operating loss carrybacks and net operating loss carryovers.

(a) *General provisions*—(1) *Years to which loss may be carried*—(i) *In general.* In order to compute the net operating loss deduction the taxpayer must first determine the part of any net operating losses for any preceding or succeeding taxable years which are carrybacks or carryovers to the taxable year in issue.

(ii) *General rule for carrybacks and carryovers.* Except as provided in section 172(b)(1)(C), (D), (E), (F), (G), (H), (I), and (J), paragraphs (a)(1)(iii), (iv), (v), and (vi) of this section, and §1.172–10(a), a net operating loss shall be carried back to the 3 preceding taxable years and carried over to the 15 succeeding taxable years (5 succeeding taxable years for a loss sustained in a taxable year ending before January 1, 1976).

(iii) *Loss of a regulated transportation corporation.* Except as provided in subdivision (iv) of this subparagraph and §1.172–19(a), a net operating loss sustained by a taxpayer which is a regulated transportation corporation (as defined in section 172(g)(1)) in a taxable year ending before January 1, 1976, shall, subject to the provisions of section 172(g) and §1.172–8, be carried back to the taxable years specified in paragraph (a)(1)(ii) of this section and shall be carried over to the 7 succeeding taxable years.

(iv) *Loss attributable to foreign expropriation.* If the provisions of section 172(b)(3)(a) and §1.172–9 are satisfied, the portion of a net operating loss attributable to a foreign expropriation loss (as defined in section 172(h) shall not be a net operating loss carryback to any taxable year preceding the taxable year of such loss and shall be a net operating loss carryover to each of the 10 taxable years following the taxable year of such loss.

(v) *Loss of a financial institution.* A net operating loss sustained in a taxable year beginning after December 31, 1975, by a taxpayer to which section 585, 586, or 593 applies shall be carried back (except as provided in §1.172–10(a)) to the 10 preceding taxable years and shall be carried over to the 5 succeeding taxable years.

(vi) *Loss of a Bank for Cooperatives.* A net operating loss sustained by a taxpayer which is a Bank for Cooperatives (organized and chartered pursuant to section 2 of the Farm Credit Act of 1933 (12 U.S.C. 1134)) shall be carried back (except as provided in §1.172–10(a)) to the 10 preceding taxable years and shall be carried over to the 5 succeeding taxable years.

* * * * *

(b) *Portion of net operating loss which is a carryback or a carryover to the taxable year in issue.* (1) A net operating loss shall first be carried to the earliest of the several taxable years for which such loss is allowable as a carryback or a carryover, and shall then be carried to the next earliest of such several taxable years, etc. Except as provided in §1.172–9, the entire net operating loss shall be carried back to such earliest year.

(2) The portion of the loss which shall be carried to any of such several taxable years subsequent to the earliest taxable year is the excess of such net operating loss over the sum of the taxable incomes (computed as provided in §1.172–5) for all of such several taxable years preceding such subsequent taxable year.

(3) If a portion of the net operating loss for a taxable year is attributable to a foreign expropriation loss (as defined in section 172(h)) and if an election under paragraph (c) of §1.172–9 is made with respect to such portion of the net operating loss, then see §1.172–9 for the separate treatment of such portion of the net operating loss.

* * * * *

Par. 6. Section 1.172–5 is amended as follows:

1. Paragraph (a)(1) is removed;

2. Paragraph (a)(2), (3), (4), and (5) are redesignated as paragraph (a)(1)(2), (3), and (4), respectively;

3. Newly redesignated (a)(3) is amended by removing "1371" and adding "1361" in lieu thereof and by removing "paragraph (g)" and adding "paragraph (f)" in lieu thereof;

4. Newly redesignated (a)(4) is amended by removing "§1.172–12(b)" and adding "§1.172–10(b)" in both places that "§1.172–12(b)" appears and by removing "paragraph (a)(3)" and "paragraph (a)(3)(i)" and adding "paragraph (a)(2)"

and "paragraph (a)(2)(i)", respectively, in lieu thereof; and

5. Paragraph (b) is removed and reserved.

Par. 7. Paragraph (a) of §1.172–7 is amended by removing the last sentence thereof.

Par. 8. Section 1.172–8 is removed.

Par. 9. Section 1.172–9 is removed.

Par. 10. Section 1.172–10 is redesignated as §1.172–8 and amended as follows:

1. Paragraph (d) is removed.
2. Paragraph (e) is redesignated as paragraph (d); and
3. Paragraph (a) is revised to read as follows:

§1.172–8 Net operating loss carryovers for regulated transportation corporations.

(a) *In general.* A net operating loss sustained in a taxable year ending before January 1, 1976, shall be a carryover to the 7 succeeding taxable years if the taxpayer is a regulated transportation corporation (as defined in paragraph (b) of this section) for the loss year and for the 6th and 7th succeeding taxable years. If, however, the taxpayer is a regulated transportation corporation for the loss year and for the 6th succeeding taxable year, but not for the 7th succeeding taxable year, then the loss shall be a carryover to the 6 succeeding taxable years. If the taxpayer is not a regulated transportation corporation for the 6th succeeding taxable year then this section shall not apply. A net operating loss sustained in a taxable year ending after December 31, 1975, shall be a carryover to the 15 succeeding taxable years.

* * * * *

Par. 11. Section 1.172–11 is redesignated as §1.172–9 and amended as follows:

1. Paragraph (c)(2) is removed;
2. Paragraph (c)(3) is redesignated as paragraph (c)(2) and is amended by removing "subparagraphs (1) and (2)" and adding "subparagraph (1)" in lieu thereof, by removing "172(b)(3)(C)(ii)" and adding "172(b)(3)(A)(ii)" in lieu thereof, and by removing the flush material under subdivision (iv);
3. Paragraph (d) is removed;
4. Paragraphs (e) and (f) are redesignated respectively as paragraphs (d) and (e) and are amended by removing "paragraph (a)(1)(v)" and adding "paragraph (a)(1)(iv)" in each place it appears; and
5. Newly redesignated paragraph (d) is further amended by removing "paragraph (c)" and adding "paragraph (a)" in lieu thereof and by removing "paragraph (c)(2)" and adding "paragraph (a)" in lieu thereof.

Par. 12. Section 1.172–12 is redesignated as §1.172–10 and amended as follows:

1. Paragraph (a)(2) is redesignated as paragraph (a)(8);
2. Paragraph (c) is redesignated as paragraph (d);
3. Newly redesignated paragraph (d) is amended by removing "§§1.172–2(e)" and adding "§§1.172–2(c)" in its place; and
4. New paragraphs (a)(1) through (7) and (c) are added to read as follows:

§1.172–10 Net operating losses of real estate investment trusts.

(a) *Taxable years to which a loss may be carried.* (1) A net operating loss sustained by a qualified real estate investment trust (as defined in paragraph (b)(1) of this section) in a qualified taxable year (as defined in paragraph (b)(2) of this section) ending after October 4, 1976, shall not be carried back to a preceding taxable year.

(2) A net operating loss sustained by a qualified real estate investment trust in a qualified taxable year ending before October 5, 1976, shall be carried back to the 3 preceding taxable years. However, see §1.857–2(a)(5), which does not allow the net operating loss deduction in computing real estate investment trust taxable income for taxable years ending before October 5, 1976.

(3) A net operating loss sustained by a qualified real estate investment trust in a qualified taxable year ending after December 31, 1972, shall be carried over to the 15 succeeding taxable years. However, see §1.857–2(a)(5).

(4) A net operating loss sustained by a qualified real estate investment trust in a qualified taxable year ending before January 1, 1973, shall be carried over to the 8 succeeding taxable years. However, see §1.857–2(a)(5).

(5) A net operating loss sustained in a taxable year for which the taxpayer is not a qualified real estate investment trust generally may be carried back to the 3 preceding taxable years; however, a net operating loss sustained in a taxable year ending after December 31, 1975, shall not be carried back to any qualified taxable year. However, see §1.857–2(a)(5) with respect to a net operating loss sustained in a taxable year ending before January 1, 1976.

(6) A net operating loss sustained in a taxable year ending after December 31, 1975, for which the taxpayer is not a qualified real estate investment trust generally may be carried over to the 15 succeeding taxable years.

(7)(i) A net operating loss sustained in a taxable year ending before January 1, 1976, for which the taxpayer is not a qualified real estate investment trust generally may be a net operating loss carryover to each of the 5 succeeding taxable years. However, where the loss was a net operating loss carryback to one or more qualified taxable years, the net operating loss, in accordance with paragraph (a)(7)(ii) of this section, shall be—

(A) Carried over to the 15 succeeding taxable years if the loss could be a net operating loss carryover to a taxable year ending in 1981, or

(B) Carried over to the 5, 6, 7, or 8 succeeding taxable years if paragraph (a)(7)(i)(A) of this section does not apply.

(ii) For purposes of determining whether a net operating loss could be a carryover to a taxable year ending in 1981 under paragraph (a)(7)(i)(A) of this section or, where paragraph (a)(7)(i)(A) of this section does not apply, to determine the actual carryover period under paragraph (a)(7)(i)(B) of this section, the net operating loss shall have a carryover period of 5 years, and such period shall be increased (to a number not greater than 8) by the number of qualified taxable years to which such loss was a net operating loss carryback; however, where the taxpayer acted so as to cause itself to cease to be a qualified real estate investment trust and the principal purpose for such action was to secure the benefit of the allowance of a net operating loss carryover under section 172(b)(1)(B), the net operating loss carryover period shall be limited to 5 years. However, see §1.857–2(a)(5).

* * * * *

(c) *Examples.* The provisions of this section may be illustrated by the following examples:

Example (1)–(i) *Facts.* X was a qualified real estate investment trust for the taxable years ending on December 31, 1972, and December 31, 1973. X was not a qualified real estate investment trust for the taxable years ending on December 31, 1971, and December 31, 1974. X sustained a net operating loss for the taxable year ending on December 31, 1974.

(ii) *Applicable carryback and carryover periods.* The net operating loss must be carried back to the 3 preceding taxable years. Under §1.857–2(a)(5) the net operating loss deduction shall not be allowed in computing real estate investment trust taxable income for the years ending December 31, 1972, and December 31, 1973. Where a net operating loss is sustained in a taxable year ending before January 1, 1976, for which the taxpayer is not a qualified real estate investment trust and the loss is a net operating loss carryback to one or more qualified taxable years, the carryover period is determined under §1.172–10(a)(7); the carryover period is determined by first applying the rule provided in paragraph (a)(7)(ii) of this section to obtain the carryover period for purposes of determining whether the net operating loss could have been a net operating loss carryover to a taxable year ending in 1981. Under these facts, paragraph (a)(7)(ii) of this section provides for a 7-year carryover period (5 years increased by the 2 qualified taxable years to which the loss was a net operating loss carryback); therefore, since the carryover period provided for by paragraph (a)(7)(ii) of this section would allow the net operating loss to be a net operating loss carryover to a taxable year ending in 1981, under paragraph (a)(7)(ii)(A) of this section the applicable carryover period is 15 years (provided that X did not act so as to cause itself to cease to qualify as a real estate investment trust for the principal purpose of securing the benefit of a net operating loss carryover under section 172 (b)(1)(B)).

Example (2)–(i) *Facts*. The facts are the same as in *example* (1) except that the taxable year ending December 31, 1973, was not a qualified taxable year for X.

(ii) *Applicable carryback and carryover periods*. The net operating loss must be carried back to the 3 preceding taxable years. Section 1.857–2(a)(5) provides that the net operating loss deduction shall not be allowed in computing real estate investment trust taxable income for the year ending December 31, 1972. Under these facts the carryover period is determined under §1.172–10(a)(7). Paragraph (a)(7)(ii) of this section provides for a 6 year carryover period (5 years increased by the 1 qualified taxable year to which the loss was a net operating loss carryback); therefore, since a 6 year carryover period would not allow the net operating loss to be a net operating loss carryover to a taxable year ending in 1981, paragraph (a)(7)(i)(A) of this section does not apply. Where the rule stated in paragraph (a)(7)(i)(A) of this section does not apply, paragraph (a)(7)(i)(B) of this section provides that the applicable carryover period is the carryover period determined under paragraph (a)(7)(ii) of this section, which, in this case, is 6 years (provided that the principal purpose for X acting so as to cause itself to cease to qualify as a real estate investment trust was not to secure the benefit of the allowance of a net operating loss carryover under section 172(b)(1)(B)).

Par. 13. Paragraph (e)(1)(ii) of §1.857–6 is amended by removing "1.172–5(a)(5)" and by adding "§1.172–5(a)(4)" in lieu thereof.

Par. 14. Paragraph (d) of §1.6411–1 is removed.

Lawrence B. Gibbs,
Commissioner of
Internal Revenue.

Approved November 14, 1986.

J. Roger Mentz,
Assistant Secretary
of the Treasury.

(Filed by the Office of the Federal Register on December 1, 1986, 8:45 a.m., and published in the issue of the Federal Register for December 2, 1986, 51 F.R. 43344)

Section 179.—Election To Expense Certain Depreciable Business Assets

Guidance is provided for taxpayers who made elections under section 179 of the Code to expense amounts that exceed the dollar limitations imposed by section 280F(a)(2) of the Code. See Rev. Proc. 86–48, page 20.

Section 280F.—Limitation on Investment Tax Credit and Depreciation for Luxury Automobiles; Limitation Where Certain Property Used for Personal Purposes

Guidance is provided for taxpayers who made elections under section 179 of the Code to expense amounts that exceed the dollar limitations imposed by section 280F(a)(2) of the Code. See Rev. Proc. 86–48, page 20.

Section 280G.—Golden Parachute Payments

Federal short-term, mid-term, and long-term rates are set forth for the month of January 1987. See Rev. Rul. 86–158, page 16.

Section 382.—Limitation on Net Operating Loss Carryforwards and Certain Built-In Losses Following Ownership Change

The adjusted federal long-term rate is set forth for the month of January 1987. The long-term tax-exempt rates will be set forth beginning in January 1987. See Rev. Rul. 86–158, page 16.

Section 383.—Special Limitations on Unused Business Credits, Research Credits, Foreign Taxes, and Capital Losses

The adjusted federal long-term rate is set forth for the month of January 1987. The long-term tax-exempt rates will be set forth beginning in January 1987. See Rev. Rul. 86–158, page 16.

Section 467.—Certain Payments for the Use of Property or Services

Federal short-term, mid-term and long-term rates are set forth for the month of January 1987. See Rev. Rul. 86–158, page 16.

Section 468.—Special Rules for Mining and Solid Waste Reclamation and Closing Costs

Federal short-term, mid-term, and long-term rates are set forth for the month of January 1987. See Rev. Rul. 86–158, page 16.

Section 472.—Last-in, First-out Inventories

26 CFR 1.472–1: Last-in, first-out inventories.
(Also Sections 611, 631, 1012; 1.611–3, 1.631–1 1.1012–1.)

Inventories; LIFO; timber cut under a section 631(a) election. A taxpayer may not use the LIFO inventory identification method in arriving at the adjusted basis of timber for purposes of computing gain or loss when the timber is cut under a section 631(a) election. Rev. Rul. 60–244 clarified.

Rev. Rul. 86–152

ISSUE

Can a taxpayer that has elected to treat the cutting of timber as a sale or exchange under section 631(a) of the Internal Revenue Code use a last-in, first-out (LIFO) inventory identification method in arriving at the adjusted basis of the timber for purposes of computing gain or loss when the timber is cut?

FACTS

The taxpayer, a domestic corporation, owns timber lands from which substantial quantities of timber are cut each year for use in its manufacturing operations. The taxpayer elected to treat the cutting of timber as a sale or exchange under section 631(a) of the Code.

The taxpayer operates on a 35 year cutting cycle. After it cuts a tract of timber, taxpayer reforests that tract and does no further cutting there for 35 years. In 1985, the taxpayer cut timber it had planted on 9*x* acres in 1950. On its federal income tax return filed for 1985, the taxpayer reported the cutting as a sale or exchange under section 631(a) of the Code. The "section 1231 gain" reported on the cutting was computed by subtracting the taxpayer's adjusted depletion basis for the timber from the fair market value of the timber on the first day of the taxpayer's 1985 tax year. The taxpayer determined its adjusted basis for depletion for the timber, under the LIFO method, by using its cost for the planting of 9*x* acres of timber that was added to this merchantable timber account in 1985.

LAW AND ANALYSIS

Section 1.631–1(d)(1) of the Income Tax Regulations provides that if the cutting of timber is considered as a sale or exchange pursuant to an election made under section 631(a) of the Code, gain or loss shall be recognized to the taxpayer in an amount equal to the difference between the adjusted basis for depletion in the hands of the taxpayer of the timber that has been cut during the tax year and the fair market value of such timber as of the first day of the tax year in which such timber is cut. The adjusted basis for depletion of the cut timber shall be based upon the number of units (feet board measure, log scale, or other units) of timber cut during the tax year that are considered to be sold or exchanged and upon the depletion unit of timber in the timber account or accounts pertaining to the timber cut, and shall be computed in the same manner as is provided in section 611 and the regulations thereunder with respect to the computation of the allowance for depletion.

Section 1.631–1(d)(3) of the regulations provides that the fair market value as of the beginning of the tax year of the standing timber cut during the year shall be considered to be the cost of such timber, in lieu, of the actual cost or other basis of such timber, for all purposes for which such cost is a necessary factor.

Section 1.631–1(d)(4) of the regulations provides that for any tax year for which the cutting of timber is considered to be a sale or exchange of such timber under section 631(a) of the Code, the timber so cut shall be considered as property used in the trade or business for purposes of section 1231, along with other property of the taxpayer used in the trade or business as defined in section 1231(b), regardless of whether such timber is property of a kind that would properly be includible in the inventory of the taxpayer if on hand at the close of the tax year or properly held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business.

Section 1.611–3(b)(3) of the regulations provides that when a taxpayer has elected to treat the cutting of timber as a sale or exchange of such timber under the provisions of section 631(a) of the Code, the taxpayer shall reduce the timber account containing such timber by an amount equal to the adjusted depletion basis of such timber.

Section 1.611–3(c)(1) of the regulations provides that every taxpayer claiming or expecting to claim a deduction for depletion of timber property shall keep accurate ledger accounts in which shall be recorded the cost or other basis provided by section 1012 of the Code of the property and land together with subsequent allowable capital additions in each account and all other adjustments provided by section 1016 and the regulations thereunder.

Section 1.611–3(c)(2) of the regulations provides that the timber accounts shall be credited each year with the amount of the charges to the depletion account computed in accordance with paragraph (b) of this section.

Section 1.611–3(b)(2) of the regulations sets forth the manner in which the depletion unit of the timber for a given timber account in a given year is to be computed. The depletion unit of the timber for a given timber account in a given year shall be the quotient obtained by dividing (i) the basis provided by section 1012 of the Code and adjusted as provided by section 1016, of the timber on hand at the beginning of the year plus the cost of the number of units acquired during the year plus proper additions to capital, by (ii) the total number of units of timber on hand in the given account at the beginning of the year plus the number of units acquired during the year plus (or minus) the number of units required to be added (or deducted) by way of correcting the estimate of the number of units remaining available in the account.

Section 1012 of the Code provides that the basis of property is its cost. Section 1.1012–1(a) of the regulations provides that cost is the amount paid for property in cash or other property.

Section 1016 of the Code provides for an adjustment to basis for the amount of depletion allowed as a deduction in computing taxable income.

Section 471 of the Code provides that whenever in the opinion of the Secretary the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by the taxpayer on such basis as the Secretary may prescribe as conforming as nearly as possible to the best accounting practice in the trade or business and as most clearly reflecting the income of such business or trade.

Section 472(a) of the Code provides that a taxpayer may use the LIFO method in inventorying goods.

Section 1.472–2(e)(8)(x) of the regulations provides, among other examples not pertinent here, that the use of actual cost of cut timber or the cost determined under section 631(a) of the Code is neither inconsistent with the inventory method referred to in section 1.472–1 nor at variance with the requirements of section 1.472–2(c). Section 1.472–2(e)(8)(x) further provides that under section 1.472–2(e)(1)(vi) either of these costing methods may be used to ascertain income, profit, or loss for credit purposes or for purposes of financial reports regardless of whether such method is also used by the taxpayer for federal income tax purposes.

The use of the LIFO method in computing the taxpayer's adjusted depletion basis under section 631(a) of the Code is incompatible with the requirements of section 1.611–3 of the regulations. Under the LIFO concept the latest cost incurred in acquiring timber added to the merchantable timber account would be applied against the timber being cut during the year. Sections 1.611–3(b)(2) and 1.611–3(c) require specific identification of the cost or other basis of each unit of timber under section 1012 and the adjustment to this basis of each unit under section 1016 for depletion.

When a section 631(a) election is in effect two realization events occur with respect to the timber. First, the deemed sale or exchange upon the cutting of the timber results in a section 1231 gain to the taxpayer to the extent the fair market value of the timber cut exceeds the actual basis of the timber cut, which basis is a cost basis with adjustments to reflect depletion and capital additions as required under section 1016 of the Code. The fair market value, as of the beginning of the tax year in which the standing timber is cut, becomes the cost basis of such timber See section 1.631–1(d)(3) of the regulations. The second realization event occurs when the cut timber product is carried in inventory by the taxpayer and subsequently sold. Section 1.631–1(e)(2) states that the fact that the fair market value as of the first day of the tax year in which the timber is cut is deemed to be the cost of such timber shall not preclude the taxpayer from computing its inventories upon the basis of cost or market, whichever is lower, if such method is used by the taxpayer. Nor shall it preclude the taxpayer from computing it inventories under the LIFO inventory method.

Rev. Rul. 60–244, 1960–2 C.B. 167, holds that a taxpayer who elects to treat the cutting of timber as sale or exchange under section 631(a) of the Code and adopts the LIFO method under section 472, may use, in financial statements to shareholders and for credit purposes, an inventory reserve reflecting the difference between the fair market value of the timber cut and the adjusted cost basis of such timber, determined without reference to such fair market value. See also section 1.472–2(e)(8)(x) of the regulations. The references to the use of the LIFO inventory method in Rev. Rul. 60–244 and section 1.472–2(e)(8)(x) are made with respect to the inventory valuation of cut timber subsequent to the section 631(a) computation. Rev. Rul. 60–244 and section 1.472–2(e)(8)(x) do not sanction use of the LIFO method in arriving at the adjusted depletion basis of the timber.

HOLDING

The taxpayer cannot use a LIFO inventory identification method in arriving at the adjusted depletion basis of timber for the purpose of computing the gain or loss when timber is cut and treated as a sale or exchange under section 631(a) of the Code.

Any change in the taxpayer's method of accounting to conform with the conclusion of this revenue ruling is a change in method of accounting to which the provisions of section 446 and 481 of the Code apply.

This ruling is identified as a designated ruling pursuant to section 5.12(2) of Rev. Proc. 84–74, 1984–2 C.B. 736.

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 60–244 is clarified.

26 CFR 1.472–1: Last-in, first-out inventories.

LIFO; price indexes; department stores. The April 1986 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, April 30, 1986.

Rev. Rul. 86–153

The following price indexes for April 1986 were issued by the Bureau of Labor Statistics on May 23, 1986, for use by department stores, and are accepted by the Internal Revenue Service, under section 1.472–1(k) of the Income Tax Regulations and Rev. Proc. 72–21, 1972–1 C.B. 745, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, April 30, 1986.

Indexes are prepared on a national basis for the store total, for 23 major groups of departments and for three special combinations—soft goods, durable goods and miscellaneous goods. The store total index covers all departments, including some not listed separately, with the following exceptions: candy, foods, liquor, tobacco, as well as contract departments.

The major groups of departments for which indexes are prepared have been expanded from 20 to 23. These new groups are: (1) Group 21—Recreation and Education; (2) Group 22—Home Improvements; and (3) Group 23—Auto Accessories. A Miscellaneous Goods index is also introduced to reflect the aggregate movement of these three new groups. *See* Rev. Proc. 86–46, 1986–50 I.R.B. 6.

Although the new indexes were introduced in the February 1986 Department Store Inventory Price Indexes, January 1987 will be the first month for which there will be a percent change based on a 12-month period. The January 1986 indexes for the new groups are all 100. Rev. Proc. 86–46 modifies and supersedes Rev. Proc. 72–21.

Rev. Proc. 86–47, 1986–50 I.R.B. 8, sets forth the procedures required of taxpayers to change their method of accounting from that of using the 20 groups set forth in Rev. Proc. 72–21 to the method of using the 23 groups set forth in Rev. Proc. 86–46.

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS

(January 1941 = 100 unless otherwise noted)

	April 1985	April 1986	Percentage Change from April 1985 to April 1986[1]
1. Piece Goods	391.3	403.0	3.0
2. Domestics and Draperies	541.5	541.7	0.0
3. Women's and Children's Shoes	557.8	531.1	−4.8
4. Men's Shoes	711.3	726.1	2.1
5. Infants' Wear	487.3	529.9	8.7
6. Women's Underwear	435.6	431.3	−1.0
7. Women's and Girls' Hosiery	234.5	238.4	1.7
8. Women's and Girls' Accessories	436.8	452.6	3.6
9. Women's Outerwear and Girls' Wear	350.1	343.4	−1.9
10. Men's Clothing	473.4	475.9	0.5
11. Men's Furnishings	479.3	479.5	0.0
12. Boys' Clothing and Furnishings	436.2	440.6	1.0
13. Jewelry	691.1	669.4	−3.1
14. Notions	486.1	472.6	−2.8
15. Toilet Articles and Drugs	633.2	660.9	4.4
16. Furniture and Bedding	544.3	542.1	−0.4
17. Floor Coverings	460.4	468.8	1.8
18. Housewares	717.3	711.6	−0.8
19. Major Appliances	244.4	250.0	2.3
20. Radio and Television	106.5	100.7	−5.4
21. Recreation and Education	N/A	99.0	N/A

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS

(January 1941 = 100 unless otherwise noted)

	April 1985	April 1986	Percentage Change from April 1985 to April 1986[1]
22. Home Improvements	N/A	97.2	N/A
23. Auto Accessories	N/A	99.6	N/A
Groups 1-15: Soft Goods	477.8	479.2	0.3
Groups 16-20: Durable Goods	449.1	446.7	−0.5
Groups 21-23: Misc. Goods	N/A	98.9	N/A
Store Total	469.7	468.7	−0.2

[1] Absence of a minus sign before percentage change in this column signifies price increase

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Section 483.—Special Limitations on Certain Excess Credits, etc.

The adjusted applicable federal short-term, mid-term, and long-term rates are set fortn for the month of January 1987. See Rev. Rul. 86–158, page 16.

Section 611.—Allowance of Deduction for Depletion

26 CFR 1.611–3: Rules applicable to timber.

Whether a taxpayer can use the last-in, first-out inventory identification method in arriving at the adjusted basis of timber for purposes of computing gain or loss when the timber is cut. See Rev. Rul. 86–152, page 10.

Section 631.—Gain or Loss in the Case of Timber, Coal, or Domestic Iron Ore

26 CFR 1.631–1: Election to consider cutting as sale or exchange.

Whether a taxpayer can use the last-in, first-out inventory identification method in arriving at the adjusted basis of the timber for purposes of computing gain or loss when the timber is cut under a section 631(a) election. See Rev. Rul. 86–152, page 10.

Section 809.—Reduction in Certain Deductions of Mutual Life Insurance Companies

Mutual life insurance companies; differential earnings rates. The recomputed differential earnings rate for 1984 published in Rev. Rul. 86–114, 1986–39 I.R.B. 14, is corrected. The differential earnings rate for 1985 and the other figures on which these rates are based that are set forth in Rev. Rul. 86–114 are restated. Mutual life insurance companies use these rates to compute their income tax liability for 1985. Rev. Rul. 86–114 modified and superseded.

Rev. Rul. 86–157

This revenue ruling restates the differential earnings rate for 1985 and corrects the recomputed differential earnings rate for 1984. These rates were published in Rev. Rul. 86–114, 1986–39 I.R.B. 14. Under section 809 of the Internal Revenue Code, as amended by the Tax Reform Act of 1986, 1986–3 (Vol. 1) C.B. [illegible], mutual life insurance companies use these rates in computing their income tax liability for 1985. This ruling also restates some of the figures on which the determinations of these rates are based. Announcement 86–36, 1986–12 I.R.B. 27, contained tentative determinations of these same rates.

Section 809(a) of the Code provides that, in the case of any mutual life insurance company, the amount of the deduction allowable under section 808 for policyholder dividends shall be reduced (but not below zero) by the "differential earnings amount." Any excess of the differential earnings amount over the amount of the deduction allowable under section 808 shall be taken into account as a reduction in the closing balance of reserves under subsections (a) and (b) of section 807. The "differential earnings amount" for any taxable year is an amount equal to the product of (a) the life insurance company's average equity base for the taxable year multiplied by (b) the "differential earnings rate" for such taxable year. The "differential earnings rate" for a taxable year is the excess of (a) the "imputed earnings rate" for the taxable year over (b) the "average mutual earnings rate" for the second calendar year preceding the calendar year in which the taxable year begins. The "imputed earnings rate" for any taxable year beginning after 1984 is an amount that bears the same ratio to 16.5 percent as the "current stock earnings rate" for the taxable year bears to the "base period stock earnings rate."

Section 809(f) of the Code provides that, in the case of any mutual life insurance company, if the "recomputed differential earnings amount" for any taxable year exceeds the differential earnings amount for such taxable year, such excess shall be included in life insurance gross income for the succeeding taxable year. If the differential earnings amount for any taxable year exceeds the recomputed differential earnings amount for such year, such excess shall be allowed as a life insurance deduction for the succeeding taxable year. The "recomputed differential earnings amount" for any taxable year is an amount calculated in the same manner as the differential earnings amount for such taxable year, but substituting the average mutual earnings rate for the calendar year in which the taxable year begins for the average mutual earnings rate for the second calendar year preceding the calendar year in which the taxable year begins. For example, the differential earnings rate for 1985 is based on the average mutual earnings rate for 1983, and the recomputed differential earnings rate for 1985 (a rate that is used in the computation of tax liability for 1986) is based on the average mutual earnings rate for 1985.

For purposes of section 809 of the Code, the differential earnings rate for 1985, the rate used to calculate the recomputed differential earnings amount for 1984 (the "recomputed differential earnings rate" for 1984), and the figures on which these two rates are based are as follows:

Differential earnings rate for 1985	6.157 percent
Recomputed differential earnings rate for 1984	10.754 percent*
Imputed earnings rate for 1985	16.323 percent
Base period stock earnings rate	18.221 percent
Current stock earnings rate for 1985	18.026 percent
Stock earnings rate for 1981	17.316 percent
Stock earnings rate for 1982	18.812 percent
Stock earnings rate for 1983	18.535 percent
Stock earnings rate for 1984	16.731 percent
Average mutual earnings rate for 1983	10.166 percent
Average mutual earnings rate for 1984	5.930 percent

*Rev. Rul. 86–114 incorrectly stated this rate as 10.570 percent.

The Tax Reform Act of 1986 retroactively amended section 809 of the Code to change the procedures for computing these rates. As indicated above, however, these procedural changes (such as excluding data from certain companies) did not result in any changes to the rates set forth in Rev. Rul. 86–114. The change in the recomputed differential earnings rate for 1984 is a result of a computational error, not of a procedural change or the gathering of additional data.

Regulations under section 809 of the Code have not yet been issued, and when these regulations are issued, they may be effective prior to the date of their issuance. Even if that is the case, however, in determining the rates that are to be used in computing 1985 tax liability, the Service will not change the administrative procedures that governed its determination of the rates announced in this revenue ruling. Moreover, the Service generally will not restate any of the rates announced in this ruling to reflect subsequent changes in the data on which the rate is based, such as a change resulting from the audit of a life insurance company. Regulations or other pronouncements, however, may result in a change in these and other procedures for determination of the rates to be used in computing the tax liability of subsequent years.

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 86–114 is modified and superseded.

Section 864.—Definitions

26 CFR 1.864–4: U.S. source income effectively connected with U.S. business.

Interest on loans; effectively connected to branch office. Securities held by a U.S. branch of a foreign bank and recorded on its books are attributable to the U.S. branch or to the home office.

Rev. Rul. 86–154

ISSUE

Whether, in the situations described below, securities held by a United States branch of a foreign bank and recorded on its books are attributable to the United States branch or to the home office.

FACTS

P, a foreign corporation whose home office is located in foreign country *X*, is actively engaged in the conduct of the banking business within the United States within the meaning of section 1.864–4(c)(5)(i) of the Income Tax Regulations through *B* and *C*, *P*'s United States branch offices. *B* has in its possession and has recorded on its books interest bearing securities of related and unrelated United States corporations evidencing funds advanced by *B* to these borrowers. Typically, the branch offices' participation in the loan acquisition process varies and is described in the situations presented below.

Situation 1: Unrelated Party Loans

B has full-time permanent employees who are account officers. These account officers contact financial officers of medium size United States companies. Through scheduled appointments, the account officers propose terms to prospective customers, and, if a customer is interested in the terms being offered, the customer executes a credit application. *B* transmits the credit application to *C*, which is staffed with personnel particularly capable of performing credit analysis, security evaluation, and other research functions. *C*'s findings are forwarded to *B*. The account officer incorporates *C*'s findings into a loan package which is forwarded to a credit committee composed of officers from *B* and *C*. The credit committee generally approves or rejects the loan package. In some cases, the committee will suggest modification of terms, in which case further negotiation by the account officer with the customer is necessary. Once the customer has agreed to terms and those terms are approved by the credit committee, *B* prepares the loan documentation and forwards it to the customer for signature. After the customer has signed, *B* funds the loan.

Situation 2: Related Party Loans

P has a wholly-owned United States subsidiary, *S*, which is actively engaged in equipment leasing and related services. *S* is in need of additional funding for expansion of its operations. The home office of *P* reviews *S*'s expansion plans, evaluates the customer orders and the credit worthiness of the customers' future receivables, and approves the loan. *P* funds the loan through *B*, by increasing *B*'s capital and having *B* loan the funds to *S*. *B* actually disperses the funds to *S*. As evidence of the loan, *S* executes a promissory note in favor of *B*. *B* services the loan throughout its term.

Situation 3: Loan Participations

An unrelated foreign multinational corporation, *Z*, is solicited by *P*'s home office and negotiates with that office for lines of credit that far exceed the funding capability of an individual branch such as *B*. In cases where *P* has approved such a large line of credit, it does so in anticipation that its various branches will participate in the funding of the loan. Regarding *B*'s participation, *P*'s home office forwards the loan documentation to *B* and instructs *B*, subject to *B*'s normal credit analysis and other loan review procedures, to fund a part of the loan to *Z*. *Z*'s wholly-owned domestic subsidiary contacts *B* for purposes of obtaining the designated loan amount. With the benefit of the information contained in the prior loan documentation forwarded from *P*, an independent global credit analysis is not performed by *B*. However, an account officer of *B* negotiates with *Z*'s United States subsidiary for the necessary collateral which is standard under *B*'s loan practices. *C* performs a thorough credit analysis of *Z*'s domestic subsidiary, evaluates the collateral and confirms to *B* that the collateral is adequate to secure the loan. *B* funds the loan.

LAW AND ANALYSIS

Section 881(a)(1) of the Internal Revenue Code generally imposes a tax of 30 percent on any interest received by a foreign corporation from United States sources, to the extent the interest is not effectively connected with the conduct of a United States trade or business. Although "portfolio interest" is exempt from the 30% withholding tax under section 881(c), "portfolio interest" does not include interest received by a bank on an extension of credit made pursuant to a loan agreement entered into in the ordinary course of its trade or business, unless the interest is paid on an obligation of the United States Government. Section 881(c)(3)(A).

Section 1.864–4(c)(5)(ii) and (iii) of the regulations provides special rules for determining whether income from securities is effectively connected with the active conduct of a banking, financing, or similar business within the United States. Subdivision (ii) requires the securities be acquired in the course of conducting specified activities, or, the securities consist of particular types. In addition, the securities must be considered attributable to a United States office through which the banking, financing, or similar business is carried on.

Subdivision (iii) provides that a security is attributable to a United States office only if such office actively and materially participates in soliciting, negotiating, or performing other activities required to arrange the acquisition of the security. However, a United States office need not have been the only active participant in arranging the acquisition of the security.

HOLDING

Situation 1

The activities of *B* and *C* are considered to be active and material with respect to the acquisition of the security. *B* or *C* solicited and negotiated the loan, performed the credit analysis and loan review, and approved the loan. These factors demonstrate that *P*'s branch office operation had the requisite authority and capability to make the loan and in fact performed all material functions with respect to the making of the loan. Accordingly, the interest income from the security held by *B* is considered effectively connected with the active conduct of a banking and finance business in the United States.

Situation 2

B did not actively and materially participate in the acquisition of the loan merely because it funded the loan. All essential functions in connection with the loan were performed by *P*'s home office. Therefore, the interest income received with respect to the security evidencing the related party loan to *Z* is not effectively connected with the active conduct of the banking, financing, or similar business within the United States. The Service will closely scrutinize loans made to related parties to determine whether a United States branch office actively and materially participates in arranging the acquisition of the securities. Absent facts clearly indicating active and material participation by a United States branch office including contemporaneous written evidence documenting such participation, it will be presumed that the office did not actively and materially participate.

Situation 3

B's and *C*'s activities are considered active and material. Although *P*'s home office solicited and negotiated the overall line of credit, *B* negotiated the collateral for the loan and *C* performed an independent credit analysis and evaluation of the collateral prior to the granting of the loan. The fact that *P*'s home office also actively and materially participated in the acquisition does not affect this result.

Section 954.—Foreign Base Company Income

26 CFR 1.954–1(f): Classification of an item of income.

Foreign base company income; gross income. Gross income from the engineering, fabrication, and installation of offshore drilling platforms is determined according to section 1.61–3(a) of the regulations after the income from such activities is classified according to the standards set forth in section 1.954–1(f)(2). Rev. Rul. 83–118 revoked.

Rev. Rul. 86–155

ISSUES

(1) For purposes of potentially characterizing income derived by a controlled foreign corporation from the engineering, fabrication, and installation of certain offshore drilling platforms as either foreign base company sales income or foreign base company services income as defined in section 954(d) and (e), respectively, is such income considered sales income or services income?

(2) In computing the gross income of a controlled foreign corporation for purposes of section 954(b)(3) of the Internal Revenue Code, are gross contract prices charged for the engineering, fabrication, and installation of certain offshore drilling platforms reduced by expenses attributable to these contracts?

FACTS

P, a domestic parent corporation, owns all of the stock in *FS*, a controlled foreign corporation (CFC) as defined in section 957 of the Code. Their activities consist principally of the engineering, fabrication, and installation of fixed offshore platforms, pipelines, and other facilities used in oil and gas drilling and production operations conducted in all major oil and gas producing areas of the world. *P* and *FS* do not themselves conduct exploration or drilling operations.

P's operations outside the United States are conducted through *FS*. Both *P* and *FS* utilize the completed contract method of accounting set forth in section 1.451–3(d) of the Income Tax Regulations.

LAW AND ANALYSIS

ISSUE (1)

Subject to exceptions, foreign base company services income, as defined in section 954(e) of the Code, and foreign base company sales income, as defined in section 954(d), consititute foreign base company income under section 954(a), which, subject to certain limitations, is includible in subpart F income. Foreign base company services income does not include any item of income which is appropriately classified as sales income, including income derived from the manufacture and sale of property. Furthermore, foreign base company sales income does not include any item of income which is appropriately classified as services income. In determining whether income from the engineering, fabrication, and installation of offshore drilling platforms potentially consitututes either foreign base company services income or foreign base company sales income, it is necessary as an initial matter to characterize such income as either services income or as sales income.

Section 1.954–1(f) of the regulations provides rules for the classification of an item of income for purposes of section 954 of the Code and sections 1.954–1 through 1.954–5. In general, income derived by a CFC from the performance of each integrated business transaction is considered a single item of income and will be classified in accordance with the predominant character of the transaction, even though an incidental part of the income could be characterized as a different class of income. However, in situations in which a CFC is engaged in performing separate business transactions, even though pursuant to the same contract or arrangement, the income from each such transaction shall be separately considered for purposes of classification under the predominant character test. Section 1.954–1(f)(2).

The determination of whether income from a single contract or arrangement constitutes separate items of income for classification purposes and the classification of each item of income as either sales or services income for subpart F purposes are factual determinations to be made by applying the standards set forth in section 1.954–1(f)(2) of the regulations. Therefore, in the present situation, the classification of *FS*'s income derived from its engineering, fabrication, and installation activities as services income, sales income, or a combination thereof depends upon the facts and circumstances of each contract or arrangement.

ISSUE (2)

Section 954(b)(3)(A) of the Code provides that, if foreign base company income derived by a CFC is less than 10 percent of its gross income, then no part of the gross income from the taxable year will be treated as foreign base company income. The determination of gross income and deductions for purposes of section 954 is made under section 952 and the regulations thereunder. Section 1.954–1(c) of the regulations.

Section 1.952–2(a)(1) of the regulations generally provides that gross income of a CFC for any taxable year is determined by treating the CFC as a domestic corporation taxable under section 11 of the Code and by applying the principles of section 61 and the regulations thereunder. Section 1.952–2(c)(4) states that the term "gross income" may not have the same meaning as the term "gross receipts." Under section 1.61–2(a) "gross income" from a manufacturing, merchandising or mining business generally means total sales less the cost of goods sold.

Whether direct labor and certain other costs incurred in the engineering, fabrication, and installation of the offshore drilling platforms described above are taken into account in computing "gross income" from those activities depends on whether the income derived from the activities constitutes sales income rather than services income. As discussed above, costs includible in cost of goods sold will be taken into account in determining gross income from manufacturing, merchandising, or mining but will not be taken into account in determining gross income from services. In order to compute the gross income from the engineering, fabrication, and installation of offshore drilling platforms, it is first necessary to determine whether the income derived from those activities constitutes separate items of income and to classify the item or items of income derived from such activities in the manner described above with respect to Issue (1). Gross income can then be determined pursuant to the rules of section 61 of the Code and the regulations thereunder.

Section 451 of the Code and the regulations thereunder are timing provisions for determining the recognition of income. *See* section 1.61–1(b)(3) of the regulations. Section 61 of the Code is applied for purposes of determining the amount of gross income of a CFC. The gross income from manufacturing activities by a CFC is computed by reducing gross receipts by costs of goods sold; whereas, the amount of gross income derived from performing services is equal to gross receipts.

HOLDINGS

Issue (1)

The classification of income from the engineering, fabrication, and installation of offshore drilling platforms as sales or services income for purposes of potentially characterizing such income as foreign base company sales or services income is a factual determination to be made by applying the standards set forth in section 1.954–1(f)(2) of the regulations to the facts and circumstances of each contract or arrangement.

Issue (2)

For purposes of section 954(b)(3) of the Code, gross income from the engineering, fabrication, and installation of offshore drilling platforms will be determined pursuant to section 1.61–3(a) of the regulations after the income from such activities is classified according to the standards set forth in section 1.954–1(f)(2).

EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 83–118, 1983–2 C.B. 27, is revoked.

Section 1012.—Basis of Property – Cost

26 CFR 1.1012–1: Basis of property.

Whether a taxpayer can use the last-in, first-out inventory identification method in arriving at the adjusted basis of the timber for purposes of computing gain or loss when the timber is cut under a section 631(a) election. See Rev. Rul. 86–152, page 10.

Section 1273.—Determination of Amount of Original Issue Discount

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of January 1987. See Rev. Rul. 86–158, below.

Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

(Also Sections 280G, 362, 467, 468, 483, 1273, 1288, 7872; 1.483–1.)

Rev. Rul. 86–158

For purposes of section 1274(d) of the Internal Revenue Code, the short-term, mid-term, and long-term applicable federal rates (AFR) for the month of January 1987 are as follows:

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-Term				
AFR	6.13%	6.04%	6.00%	5.97%
110% AFR	6.75%	6.64%	6.59%	6.55%
120% AFR	7.38%	7.25%	7.19%	7.14%
Mid-Term				
AFR	6.93%	6.81%	6.75%	6.72%
110% AFR	7.63%	7.49%	7.42%	7.38%
120% AFR	8.34%	8.17%	8.09%	8.03%

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Long-Term				
AFR	7.41%	7.28%	7.21%	7.17%
110% AFR	8.17%	8.01%	7.93%	7.88%
120% AFR	8.93%	8.74%	8.65%	8.58%

For purposes of section 1288 of the Code, the short-term, mid-term, and long-term adjusted federal rates (adjusted AFR) for the month of January 1987 are as follows:

	Period for Compounding			
	Annual	*Semiannual*	*Quarterly*	*Monthly*
Short-term				
AFR	3.88%	3.84%	3.82%	3.81%
Mid-term				
AFR	4.92%	4.86%	4.83%	4.81%
Long-term				
AFR	5.90%	5.82%	5.78%	5.75%

For purposes of section 382 of the Code, the adjusted federal long-term rate and the long-term tax-exempt rate for January 1987 are as follows:

Adjusted federal long-term rate for January	5.90%
Long-term tax-exempt rate for ownership changes during January (the highest of the adjusted federal long-term rates for the current month and the prior two months)	6.41%

Section 1288.—Treatment of Original Issue Discount on Tax-Exempt Obligations

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of January 1987. See Rev. Rul. 86–158, page 16.

Section 7872.—Treatment of Loans with Below-market Interest Rates

Federal short-term, mid-term, and long-term rates are set forth for the month of January 1987. See Rev. Rul. 86–158, page 16.

Part II. Treaties and Tax Legislation

Subpart A.—Tax Conventions

United States-Netherlands Income Tax Convention, 1950–1 C.B. 92; 1967–2 C.B. 472.

Netherlands; equipment rental payments; business profits. U.S. source payments for equipment rentals are exempt from U.S. income tax as business profits under Article III of the U.S.-Netherlands Income Tax Convention.

Rev. Rul. 86–156

ISSUE

Whether photocopy machines are "other like property" within the meaning of Article IX of the United States—Netherlands Income Tax Convetion (the Treaty), 1950–1 C.B. 92, as amended by the Protocol of December 30, 1965 (1965 Protocol), 1967–2 C.B. 472, and, if not, whether payments for the lease thereof constitute industrial or commercial profits within the meaning of Article III of the Treaty.

FACTS

P, a corporation organized under the laws of the Netherlands, owns 100 percent of the stock of *S*, a corporation organized under the laws of the United States. *P* manufactures photocopy machines and leases them to *S*, and *S* makes periodic rental payments to *P*. *P* carries on a portion of its manufacturing operations in the Netherlands. *P* is not engaged in a trade or business within the United States through a permanent establishment. *S* subleases the photocopy machines to its United States customers.

LAW AND ANALYSIS

Article IX of the Treaty, prior to the 1965 Protocol, specifically exempted United States source royalties paid to a Netherlands corporation for the use of industrial, commercial, or scientific equipment, provided that the Netherlands corporation was not engaged in a trade or business within the United States through a permanent establishment.

Article IX(2), as amended by the 1965 Protocol, exempts United States source royalties, rentals, or amounts paid as consideration for the use of, or right to use, copyrights, artistic or scientific works, patents, designs, plans, secret processes or formulae, trademarks, motion picture films, films or tapes for radio or television broadcasting, or other like property or rights, or information concerning industrial, commercial or scientific knowledge, experience or skill, provided that the Netherlands corporation does not have a permanent establishment within the United States to which such amounts are attributable.

Article III(1) of the Treaty, as amended by the 1965 Protocol, exempts industrial or commercial profits derived by a Netherlands enterprise to the extent not attributable to a permanent establishment in the United States. Article II(1)(g) defines a Netherlands enterprise as an industrial or commercial enterprise or undertaking carried on in the Netherlands by the taxpayer. Article III(5) of the Treaty, as amended by the 1965 Protocol, provides that industrial or commercial profits means income derived from the active conduct of a trade or business, but does not include income described in Article IX(2).

Other treaties use the phrase "other like property or rights" in relation to intangibles such as patents and copyrights, and use independently the phrase "industrial, commercial or scientific equipment." For example, Article XII(4)(a)(i) of the United States-Australia Income Tax Convention, T.I.A.S. No. 10773, exempts payments and credits for the use of any "copyright, patent . . . or other like property or right." Article XII(4)(a)(ii) separately exempts payments for the use of, or the right to use, "industrial, commercial or scientific equipment. . . ."

Where payments for the use of industrial, commercial or scientific equipment are to be exempted by the royalties article in a treaty, that article specifically states that such property is included within its scope. Therefore, the phrase "other like property or rights" contained in Article IX(2) of the Treaty, as amended by the 1965 Protocol, modifies only the items specifically enumerated in Article IX(2). The items of tangible property included in Article IX(2) are tapes, films, and artistic or scientific works. None of the items enumerated could possibly incorporate equipment. Consequently, the phrase "other like property or rights" cannot be interpreted to refer to industrial, commercial, or scientific equipment. Payments for the use of industrial, commercial or scientific equipment, therefore, are not covered by Article IX(2) and are exempt, if at all, under the business profits article (Article III) of the Treaty.

Article III(5) of the Treaty defines "industrial or commercial profits" as "income derived from the active conduct of a trade or business." Article III(1) provides that the exemption for industrial or commercial profits derived by a Netherlands enterprise is applicable only to income that is not attributable to a permanent establishment in the United States.

The phrases "industrial or commercial profits" and "income derived from the active conduct of a trade or business" do not require such profits or income of the Netherlands enterprise be derived by an active trade or business within the United States, but merely require that the income be derived from the active conduct of a trade or business conducted in whole or in part in the Netherlands by the Netherlands enterprise.

Article III of the Treaty, therefore, exempts United States source rentals or other payments for the use of industrial, commercial, or scientific equipment, provided that such amounts are attributable to a trade or business actively conducted in whole or in part in the Netherlands by the Netherlands enterprise and are not attributable to a permanent establishment in the United States.

HOLDING

Under the facts of this case, the rentals for photocopy machines derived by *P* from *S* constitute industrial or commercial profits derived by a Netherlands enterprise. Furthermore, the rentals are not attributable to a permanent establishment of *P* in the United States. Therefore, the rentals are exempt from United States tax under Article III of the Treaty.

Part III. Administrative, Procedural, and Miscellaneous

Assistant Commissioner (International)—Title and Address

Notice 86–15

A new Assistant Commissioner (International) office was established May 12, 1986, to coordinate the Internal Revenue Service's various international tax activities. Three former organizations, the Foreign Operations District, The International Programs Section of the Assistant Commissioner (Examination), and the Tax Administration Advisory Services Division, were consolidated and restructured to form the new organization. The Assistant Commissioner (International) reports to the Associate Commissioner (Operations) and has multifunctional responsibility for international tax program development and compliance.

Pending the issuance of revised Internal Revenue Service documents such as publications, Revenue Procedures, and the Regulations under Title 26 of the USC, the following title and address will be used:

Internal Revenue Service
Assistant Commissioner (International)
ATTN: (when provided)
950 L'Enfant Plaza South, S.W.
Washington, D.C. 20024

The above title and address will be substituted for Director, Foreign Operations District (or in the older documents, Director, Office of International Operations) at the various Post Office boxes and 1325 K Street address in Washington, D.C.

Regulations To Be Published Under §884 (The Branch Profits Tax)

Notice 86–17

The Internal Revenue Service is herein announcing that, under regulations to be prescribed, the branch profits tax will not generally be imposed on (1) the complete termination of a foreign corporation's United States trade or business, (2) certain liquidations or reorganizations of a foreign corporation that has conducted a U.S. trade or business, or (3) a section 351 incorporation of a foreign corporation's U.S. trade or business.

Section 884(a) of the Internal Revenue Code of 1986, as added by section 1241 of the Tax Reform Act of 1986, imposes a 30-percent branch profits tax on a foreign corporation's after-tax U.S. earnings that are not reinvested in the corporation's U.S. business. The branch profits tax is imposed on the "dividend equivalent amount" for the taxable year. Generally, the dividend equivalent amount is the foreign corporation's earnings and profits attributable to income that is effectively connected with the conduct of a U.S. trade or business (1) decreased by increases in the foreign corporation's U.S. net equity during the taxable year and (2) increased by decreases in the foreign corporation's U.S. net equity during the taxable year.

Section 884(g) authorizes the Secretary to prescribe such regulations as may be necessary or appropriate to carry out the purposes of section 884. The principal purpose of section 884 is to equalize the tax treatment of U.S. branches and subsidiaries of foreign corporations.

The liquidation of a U.S. subsidiary of a foreign corporation would not generally result in a tax on the foreign parent corporation. In order to provide similar treatment where the foreign corporation has operated through a U.S. branch rather than through a U.S. subsidiary, regulations will be promulgated under section 884(g) to provide generally that the branch profits tax will not be imposed for the year in which a foreign corporation completely terminates its U.S. trade or business. Subject to an anti-abuse rule, a foreign corporation that completely terminates its U.S. trade or business (for example, by selling all its U.S. trade or buisness assets and investing the proceeds in portfolio obligations) will not be considered, for purposes of the branch profits tax, to have either effectively connected earnings and profits for the taxable year or a decrease in U.S. net equity as of the end of the taxable year. The foreign corporation will not, therefore, be subject to the branch profits tax for the taxable year. The regulations will also provide that the foreign corporation will not incur a branch profits tax if it completely liquidates in connection with the complete termination of the trade or business. For purposes of these rules, a foreign corporation with more than one U.S. branch will be considered to have a single U.S. trade or business. Thus, a foreign corporation with branches in New York and California must cease all activities of both branches in order to terminate completely its U.S. trade or business and avoid the branch profits tax under the foregoing rules.

Under the anti-abuse rule, the complete termination of a foreign corporation's U.S. trade or business may result in a branch profits tax liability if the foreign corporation, or any other related person, conducts a U.S. trade or business with any assets of the terminated trade or business or reinvests any of the proceeds from the sale of the assets of the terminated trade or business in a U.S. trade or business. This anti-abuse rule, will prevent, for example, a foreign corporation from terminating its U.S. trade or business and reinvesting less than the full amount of its U.S. net equity in U.S. trade or business assets.

Notwithstanding the foregoing, the following rules will apply when one foreign corporation transfers assets to a second foreign corporation pursuant to a distribution in liquidation described in section 332 or a nondivisive tax-free reorganization and the second corporation continues to conduct a U.S. trade or business previously conducted by the transferor. If the taxable year of the transferor closes as of the date of the liquidation or reorganization, the transferor's U.S. net equity as of the close of its short taxable year and its effectively connected earnings and profits must be computed for purposes of determining the branch profits tax for the short taxable year. The regulations will provide that, for purposes of these computations, U.S. net equity and effectively connected earnings and profits will be computed without regard to the transfer to the second corporation pursuant to the liquidation or reorganization. Thus, such transfer will not itself increase the transferor's dividend equivalent amount for the short taxable year and will not, therefore, increase its branch profits tax liability, if any, for such year. If, however, the transferor corporation has a dividend equivalent amount for the short year arising from other events (for example, from effectively connected earnings and profits realized prior to the transfer), the corporation may have a branch profits tax liability for such year.

The regulations will provide that, in situations described in the immediately preceding paragraph, the transferee corporation may be subject to the branch profits tax on an amount equal to the post-1986 effectively connected earnings and profits of the transferor corporation on which the branch profits tax was not previously imposed due to an increase in its U.S. net equity. The transferee corporation may be subject to the branch profits tax on this amount to the extent the transferee's U.S. net equity is reduced.

The preceding two paragraphs do not address transactions in which the transferee would not be subject to the branch profits tax after the transaction.

Finally, the regulations will provide generally that the incorporation of all of the U.S. trade or business activities of a foreign corporation into a wholly-owned U.S. subsidiary in a transaction described in section 351(a) will not be treated as a decrease in U.S. net equity of the foreign corporation and will not, therefore, increase the dividend equivalent amount of the foreign corporation and result in the imposition of the branch profits tax. The regulations will determine the extent to which events subsequent to the transfer, such as distributions from the U.S. subsidiary to the foreign parent or sale of the stock of the subsidiary by the foreign parent, will trigger either a branch profits or withholding tax on the parent.

The rules contained in this notice will be effective until superseded by regulations. Taxpayers may rely on these rules with respect to the specific transactions described herein.

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26 CFR 601.602: Tax forms and instructions.
(Also Sections 179, 280F.)

Rev. Proc. 86–48

SECTION 1. PURPOSE

This revenue procedure provides guidance to taxpayers who made elections under section 179 of the Internal Revenue Code to expense amounts that exceed the dollar limitations imposed by section 280F(a)(2) of the Code. Under this procedure, in the limited circumstances described below, the Internal Revenue Service will recognize a limited modification of an election under section 179 if made on an amended return filed before the expiration of the period for filing a claim for credit or refund.

SEC. 2. BACKGROUND

.01 Section 179(a) of the Code permits a taxpayer to elect to treat the cost of any section 179 property as an expense that is not chargeable to capital account. The election must be made for the taxable year in which the section 179 property is placed in service.

.02 Section 179(c)(1) of the Code provides that any election under section 179 shall specify the items of section 179 property to which the election applies and the portion of the cost of each item which is to be taken into account under section 179(a). In addition, an election under section 179(a) shall be made on the taxpayer's income tax return for the taxable year. Section 179(c)(2) of the Code provides that any election made under section 179, and any specification contained in any such election, may not be revoked except with the consent of the Secretary.

.03 Pursuant to sections 179(d)(9) and 168(d)(1) of the Code, prior to computing investment tax credit under section 46 and deductions with respect to recovery property under section 168, a taxpayer must reduce the basis of the property subject to the section 179 election by the amount of the cost elected to be expensed.

.04 Under section 179(b) of the Code, for taxable years ending on or before December 31, 1986, $5,000 is the aggregate cost that may be expensed under section 179(a). With respect to property placed in service after December 31, 1986 in taxable years ending after such date, however, the limit is $10,000.

.05 Section 280F(a)(2) of the Code limits the deduction allowed for the cost recovery of passenger automobiles. For passenger automobiles placed in service after June 18, 1984, and before January 1, 1985, the recovery deduction allowed for the taxable year in which the automobile is placed in service is limited to $4,000. For passenger automobiles placed in service after December 31, 1984, and before April 3, 1985, and for automobiles placed in service before August 1, 1985, that are acquired by the taxpayer pursuant to a binding contract in effect on April 1, 1985, and at all times thereafter, the recovery deduction allowed for the taxable year the automobile is placed in service is limited to $4,100. *See* Rev. Rul. 86–107, 1986–37 I.R.B. 8. For all other passenger automobiles placed in service after April 2, 1985, and before January 1, 1989, the recovery deduction allowed for the taxable year in which the taxpayer places the automobile in service is limited to $3,200.

.06 Under section 280F(d)(1) of the Code, any deductions allowable under section 179 are subject to the limitations of sections 280F(a) and (b) in the same manner as if they were recovery deductions allowed under section 168. Thus, if the dollar limitations imposed by section 179 exceed the dollar limitations imposed by section 280F, then even though a taxpayer may elect under section 179 to expense the cost or a portion of the cost of a passenger automobile in excess of the section 280F(a)(2) dollar limitation, the taxpayer's deduction is limited to the amount allowed by section 280F(a)(2). Notwithstanding that limitation, the taxpayer must reduce its basis in the section 179 property by the full amount of its section 179 election. *See* sections 168(d)(1) and 179(d)(9), which refer to the amount of the taxpayer's election under section 179 and the amount allowed as a deduction by section 179(a), respectively.

.07 For example, if a taxpayer, unaware of the limitations of section 280F of the Code, purchased and placed in service in 1984 an automobile costing $11,000 and if that taxpayer elected under section 179 to expense $5,000 of the cost, the taxpayer's basis is reduced by the full $5,000 that the taxpayer originally elected to expense, even though the taxpayer is allowed to expense only $4,000 in the first recovery year. The remaining $1,000 of the amount that the taxpayer elected to deduct under section 179 but is precluded from deducting by section 280F(a)(2) becomes part of the "unrecovered basis." *See* sections 1.280F–2T(c)(1) and (e) Example (4) of the Temporary Income Tax Regulations. Accordingly, the remaining $1,000 elected to be deducted under section 179 as well as the deduction allowed under section 168 for the first recovery year would not be recoverable until a year after the end of the ACRS recovery period. In addition, the investment credit and the deductions allowed under section 168 would be calculated on a basis of $6,000 ($11,000 less the $5,000 basis reduction) rather than on a basis of $7,000 ($11,000 less $4,000, the maximum amount that can be expensed in the first year).

SEC. 3. TAXPAYERS AFFECTED

.01 This revenue procedure applies if (1) a taxpayer, on the taxpayer's return filed before the expiration of the time for filing, made an election under section 179 of the Code to expense the cost or a portion of the cost of a passenger automobile that was placed in service after June 18, 1984, and before January 1, 1986, and (2) the amount so elected was in excess of the dollar limitations imposed by section 280F(a)(2).

SEC. 4. PROCEDURE

.01 The Service will permit a limited modification of an election under section 179 of the Code if a request is made on an amended return filed before the expiration of the period under section 6511 for filing a claim for credit or refund. The Service will permit a modification only to the extent that the modification reduces the taxpayer's section 179 expense election to the maximum amount allowable under section 280F(a)(2) for the taxable year the property is placed in service. On the amended return, the taxpayer may adjust its basis to correspond with the amount correctly claimed as a section 179 expense election. The amended return should be filed with the appropriate Internal Revenue Service Center and include the statement "FILED UNDER REV. PROC. 86-48."

.02 A taxpayer may not reallocate to any other property that portion of its section 179 expense election that exceeded the recovery deduction limitation under section 280F(a)(2) of the Code.

SEC. 5. EFFECTIVE DATE

This revenue procedure shall be effective for requests made on amended returns filed after December 29, 1986, the date of publication of this revenue procedure.

Part IV. Items of General Interest

Diversification Requirements for Variable Annuity, Endowment, and Life Insurance Contracts

Announcement 86–129

This announcement concerns the diversification requirements under section 817(h) of the Internal Revenue Code that are applicable to variable annuity, endowment, and life insurance contracts.

Section 817(h) of the Code authorizes the Secretary of the Treasury to prescribe diversification requirements for the investments underlying a variable annuity, endowment, or life insurance contract and provides that a variable contract generally will not be treated as an annuity, endowment, or life insurance contract unless those requirements are satisfied. Temporary and proposed regulations prescribing diversification requirements under section 817(h) were published in the Federal Register on September 15, 1986 (51 FR 32633, 32664).

The effective date provisions set forth in the temporary regulations will be modified as described in this announcement in final regulations under section 817(h). Taxpayers can rely on this announcement until final regulations under section 817(h) are published in the Federal Register.

The temporary regulations generally are effective for taxable years beginning after December 31, 1983. Section 1.817–5T(i)(2) of the Temporary Income Tax Regulations, however, provides three exceptions to this general effective date. First, the regulations do not apply to a segregated asset account until December 15, 1986, if an insurance company would be considered the owner of the underlying assets under the principles of Rev. Rul. 81–225, 1981–2 C.B. 12. Because, under the regulations, diversification is tested as of the end of each calendar quarter, or within 30 days thereafter, the effect of this rule is to require a qualifying segregated asset account to satisfy the diversification requirements of the regulations on December 31, 1986, or within 30 days thereafter. Second, the regulations do not apply to any contract that was grandfathered under Rev. Rul. 77–85, 1977–1 C.B. 12, or Rev. Rul. 81–225. Third, certain debt instruments are not treated as government securities for purposes of determining whether a segregated asset account is adequately diversified for any calendar quarter ending before July 1, 1987.

The final regulations under section 817(h) will provide an additional exception to the general effective date rule in the case of a segregated asset account that is invested in government securities. Section 1.817–5T(b)(1)(ii)(B) of the temporary regulations provides that, for purposes of the diversification requirements, all government securities are treated as securities of a single issuer. The final regulations under section 817(h), however, will provide that, for purposes of determining whether a segregated asset account is adequately diversified for any calendar quarter ending before July 1, 1987, each government agency or instrumentality will be treated as a separate issuer.

Information Reporting for Brokers and Middlemen Holding Debt Instruments Issued at a Discount

Announcement 86–130

This announcement concerns information reporting rules under section 6049 of the Internal Revenue Code for brokers and middlemen who hold interests as nominees in certificates of deposit and other debt instruments issued at a discount. The Internal Revenue Service will amend the Income Tax Regulations under section 6049 of the Code; affected taxpayers may rely on this announcement until these regulations are issued.

BACKGROUND

Section 6049 of the Code and regulations under that section require every person who makes payments of interest (including original issue discount), or who receives payments of interest as a nominee and makes payments to another person with respect to the interest received, in an aggregate amount of $10 or more to make an information return and to provide the payee with a written statement setting forth the amount of these payments.

Section 6049(b) of the Code provides that, except as otherwise provided in regulations, an issuer or nominee need not provide a written statement to certain holders. Section 1.6049–4(c)(1)(ii)(L) of the regulations provides that brokers are treated as exempt recipients.

The Service on December 12, 1986, issued section 1.6049–5T of the Temporary Income Tax Regulations, relating to reporting by brokers of interest and original issue discount on and after January 1, 1986. This temporary regulation requires that brokers and other middlemen that hold as nominees certificates of deposit originally issued at a discount to report to holders the amount of OID includible for each year. The temporary regulation generally requires reporting for calendar year 1986 and thereafter with respect to debt instruments held on or after June 1, 1986. Before January 1, 1987, however, reporting is required only with respect to debt instruments held by a broker or middleman as a nominee on or after June 1, 1986, that also were sold by the broker or middleman to the owner.

Section 1.6049–5(c) of the regulations permits a payor (other than an issuer) to rely upon information contained in the Service's Publication 1212 in discharging its reporting obligations to provide a written statement to the payee. Certificates of deposit described in the temporary regulation issued on December 12, 1986, are not listed in this publication because, given the volume of certificates of deposit described in the temporary regulation, it would not be practical to compile OID information for Publication 1212 with respect to these certificates.

The Service thus recognizes that a broker or middleman required to report OID to the holder of a certificate of deposit or debt instrument described in the temporary regulation issued on December 12, 1986, may not possess information sufficient to comply adequately and accurately with the reporting requirement imposed by this regulation because (1) OID information is not available with respect to the certificate in Publication 1212 and (2) the broker or middleman, qualifying as an exempt recipient within the meaning of section 6049(b) and section 1.6049–4(c)(1) of the regulations, has not received a written statement containing this information from the issuer of the certificate.

Reporting Requirements

Accordingly, the Internal Revenue Service will amend section 1.6049–4 of the regulations to provide that a broker or middleman holding as a nominee a debt instrument described in section 1.6049–5T(a) or (b) of the temporary regulation may waive its status as an exempt recipient and request that the issuer of the debt instrument provide it with a written statement setting forth the information required by section 1.6049–3 of the regulations with respect to the debt instrument. In that event, the issuer will be required to provide a written statement to such broker. A broker may waive its exempt status for any debt instrument held on or after June 1, 1986.

COMMENTS WELCOMED

The Service welcomes comments from affected taxpayers on the reporting requirements discussed in this announcement. Comments may be directed to the Legislation and Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224 (Attention: CC:LR:T) (LR–2–86).

Supplemental Information on Treasury Bills for Publication 1212

Announcement 86–131

Banks, brokers, and other middlemen who report discount on Treasury bill redemptions on Form 1099–INT must use the owner's purchase price, where available, to determine the amount of discount to report. Usually this information can be obtained from the owner's or middleman's records. However, if the owner's purchase price is *not* available from existing records, the middleman must report the discount as if the holder had purchased the Treasury bill at its original issue price. In this case, the middleman must use as the original issue price the noncompetitive issue price for the longest-maturity Treasury bill maturing on that date.

For Treasury bill redemptions in cases where the owner's purchase price *cannot* be determined, a list of the noncompetitive issue prices and corresponding amounts of discount to be reported on Form 1099-INT for Treasury bills maturing during January through June 1987 appears below. This list, which should also help middlemen determine any amounts subject to backup withholding, supplements the list that appears in Publication 1212, *List of Original Issue Discount Instruments* (Rev. Dec. 1986).

SHORT TERM UNITED STATES TREASURY BILLS ISSUED AT A DISCOUNT AND MATURING JANUARY–JUNE 1987

CUSIP Number	Maturity Date	Issue Date	Noncompetitive Issue Price (% of Principal Amount)	Dollar Amount of Discount to be Reported as Interest for 1987 (Per $1,000 of Maturity Value)
912794KV	01/02/87	07/03/86	96.970	30.30
KN	01/08/87	07/10/86	97.043	29.57
KW	01/15/87	07/17/86	97.068	29.32
LT	01/22/87	01/23/86	92.609	73.91
KY	01/29/87	07/31/86	97.022	29.78
KP	02/05/87	08/07/86	97.103	28.97
KZ	02/12/87	08/14/86	97.169	28.31
LX	02/19/87	02/20/86	92.730	72.70
LB	02/26/87	08/28/86	97.295	27.05
KQ	03/05/87	09/04/86	97.386	26.14
LC	03/12/87	09/11/86	97.295	27.05
MB	03/19/87	03/20/86	93.317	66.83
MC	03/26/87	09/25/86	97.275	27.25
MD	04/02/87	10/02/86	97.285	27.15
ME	04/09/87	10/09/86	97.407	25.93
MF	04/16/87	04/17/86	93.994	60.06
MG	04/23/87	10/23/86	97.275	27.25
MH	04/30/87	10/30/86	97.366	26.34
MJ	05/07/87	11/06/86	97.321	26.79
MK	05/14/87	05/15/86	93.761	62.39
ML	05/21/87	11/20/86	97.250	27.50
MM	05/28/87	11/28/86	97.290	27.10
MN	06/04/87	12/04/86	97.240	27.60
MP	06/11/87	06/12/86	93.337	66.63
MQ	06/18/87	12/18/86	97.179	28.21
MR	06/25/87	12/26/86	97.205	27.95

Announcement of the Disbarment, Suspension, or Consent to Voluntary Suspension of Attorneys, Certified Public Accountants, Enrolled Agents and Enrolled Actuaries from Practice Before the Internal Revenue Service

Under 31 Code of Federal Regulations, Part 10, an attorney, certified public accountant, enrolled agent or enrolled actuary, in order to avoid the institution or conclusion of a proceeding for his disbarment or suspension from practice before the Internal Revenue Service, may offer his consent to suspension from such practice. The Director of Practice, in his discretion, may suspend an attorney, certified public accountant, enrolled agent or enrolled actuary in accordance with the consent offered.

Attorneys, certified public accountants, enrolled agents, and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify practitioners under consent suspension from practice before the Internal Revenue Service, the Director of Practice will announce in the Internal Revenue Bulletin the names and address of practitioners who have been suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary and the date or period of suspension. This announcement will appear in the weekly Bulletin at the earliest practicable date after such action and will continue to appear in the weekly Bulletins for five successive weeks or for as many weeks as is practicable for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended and will later be consolidated and published in the Cumulative Bulletin.

The following individuals have been placed under the consent suspension from practice before the Internal Revenue Service:

Name	Address	Designation	Term of Suspension
Howard M. Belser	Decatur, AL	Attorney	Three Years from October 9, 1986
Kennard I. Mandell	Wellesley, MA	Attorney	Indefinite from October 1, 1986

Under Section 330, Title 31 of the United States Code (1970 ed.), the Secretary of the Treasury, after due notice and opportunity for hearing, is authorized to suspend or disbar from practice before the Internal Revenue Service any person who has violated the rules and regulations governing the recognition of attorneys, certified public accountants, enrolled agents or enrolled actuaries to practice before the Internal Revenue Service.

Attorneys, certified public accountants, enrolled agents and enrolled actuaries are prohibited in any Internal Revenue Service matter from directly or indirectly employing, accepting assistance from, being employed by or sharing fees with, any practitioner disbarred or under suspension from practice before the Internal Revenue Service.

To enable attorneys, certified public accountants, enrolled agents and enrolled actuaries to identify such disbarred or suspended practitioners, the Director of Practice will announce in the Internal Revenue Bulletin the names and addresses of practitioners who have been disbarred or suspended from such practice, their designation as attorney, certified public accountant, enrolled agent or enrolled actuary, and the date of disbarment or period of suspension. This announcement will continue to appear in the weekly Bulletin for five successive weeks for each attorney, certified public accountant, enrolled agent or enrolled actuary so suspended or disbarred and will later be consolidated and published in the Cumulative Bulletin.

After due notice and opportunity for hearing, the following individual has been suspended from further practice before the Internal Revenue Service.

Name	Address	Designation	Term of Suspension
Paul Adams, Jr.	Bristol, VA	Certified Public Accountant	Indefinite from September 11, 1986

After due notice and opportunity for hearing, the following individual has been disbarred from further practice before the Internal Revenue Service:

Name	Address	Designation	Effective Date
Leonard Bezark	King of Prussia, PA	Certified Public Accountant	October 19, 1986

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc. published in Internal Revenue Bulletins 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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[1] A cumulative finding list for previously published rulings mentioned in Internal Revenue Bulletin 1986–1 through 1986–26 will be found in Internal Revenue Bulletin 1986–27, dated July 7, 1986.

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